

PersonalFinance

43 YEARS OF PROFITS IN BULL & BEAR MARKETS

UNDER THE RADAR



Under the Radar

By Jim Pearce and the team of analysts at Investing Daily

Sometimes, Wall Street isn't out to get you as an investor. Sometimes, Wall Street is just too blind to find the best stocks. Perhaps that's because some of these companies are in towns that the pinstriped investment bankers wouldn't dare travel to, lest they get stuck staying at a Motel 6 and eating at the local Denny's rather than the Four Seasons.

But there's also another reason: Many successful companies don't need Wall Street. They don't constantly issue new stock or bonds; they don't engage in crazy takeovers and mergers; they don't involve themselves in complex financial maneuvers that feed investment bankers and brokers along with business consultants.

They just plod along, doing their jobs without fanfare, all for the benefit of their shareholders. Again, you won't hear or read any flashy reports touting these companies. But at *Personal Finance*, we don't care about anything except finding the best stocks and bonds for you, the subscriber. We cover stocks like these under-the-radar companies regularly. Keep reading for the full story on our top 10 undiscovered picks.

#1: Integrated Device Technology

Integrated Device Technology (NSDQ: IDTI) sells at a downright bargain. Founded nearly four decades ago, the company has a diverse product mix that positions it for outstanding growth in the \$334 billion global semiconductor market. We see the bottom line compounding at a high-double-digit clip over the next few years.

For many years IDTI has been a leading supplier of several ubiquitous semiconductors, like high-performance timing chips that coordinate signals between digital circuits. Such chips are crucial for computer networking, wireless infrastructure, and large-scale data storage, among other applications. IDTI is also a top provider of semiconductors necessary for creating digital memory, regulating power consumption and charging widely used medical devices, including MRIs.

Yet another indispensable offering: a broad line of switches that link up computer systems. These technologies are essential for wireless communication. They also improve image quality for video and

teleconferencing, as well as electronic components in military aircraft and naval vessels.

The company also expects big things from a recent acquisition, ZMDI, a highly profitable German chipmaker. The buyout immediately made IDTI a force in the steadily expanding, multibillion-dollar market for components of smart sensors that improve handling and safety in cars and the precision of industrial machinery.

Hyundai Motor, Kia Motors, and General Electric are a few of ZMDI's biggest customers. Such connections should help additional sales of IDTI semiconductors, such as those compatible with automotive infotainment systems.

IDTI is financially healthy, even after shelling out \$307 million for ZMDI, and should continue to generate a lot of free cash for years to come.

#2: Main Street Capital

Your brother-in-law is supposedly sitting on a fortune in a house he bought just a year or two ago, and he gloats about it every time the family gets together.

Although owning an appreciating asset like that is nice, it can be equally lucrative for the lender that makes the purchase possible in the first place.

In real estate, a lender makes money on the mortgage interest; if times get tough, the lender forecloses and grabs the property. Profit comes in two ways. First, the yield earned is generally higher than interest expenses, and second, by managing the types and maturities of the mortgages, the companies can cash in on market gains as well.

This isn't for amateurs, as many an investor of thrifts in the 1980s will tell you, as well as believers in Wall Street's faltering top picks, Fannie Mae and Freddie Mac. During the past decade, a few mortgage companies nearly got wiped out by poor judgment and shoddy management skills.

Just like in any market, you have to know what to buy and what to avoid. We focus on the companies that had a track record of making it through the troubled times for interest rates and the lending market. And the best in the business is in Houston, Texas: **Main Street Capital** (NYSE: MAIN).

#3: PPL

PPL (NYSE: PPL) is a utility company delivering electricity and natural gas to customers in the United States and the United Kingdom.

For the first time in three years, PPL's unit, PPL Electric Utilities, filed to raise delivery rates with the Pennsylvania Public Utility Commission. This will allow PPL to invest more in upgrading its utility systems to provide more reliable service to its customers.

Greg Dudkin, PPL Electric Utilities president said, "Almost all of the increase we are requesting will go directly into enhancing the reliability of our electric system, reducing the number of power outages. At the same time, we are focused on operating more efficiently to make sure electric service from PPL remains a good value for our customers."

As a regulated utility, PPL isn't subject to the same market forces as its unregulated peers, which allows it to adjust rates in response to market conditions. With the Federal Reserve sounding more hawkish by the day, higher rates in America could reduce the dollar's value, allowing some of the company's U.K.-based earnings to be recast at a more favorable exchange rate with the pound.

#4: On Assignment

The Great Recession ended more than seven years

ago, but many employers remain wary of hiring permanent workers. Their timidity is a boon to California-based staffing agency **On Assignment** (NYSE: ASGN).

Huge demand for On Assignment's temporary and temp-to-hire employees, the type of workers gun-shy employers increasingly seek to keep a lid on costs yet still get the job done, is driving earnings.

And why not? For a fee, employers get willing workers without any upfront commitment, while the staffing agency assumes the entire administrative burden. Employers that eventually plan to hire get a long look at job prospects before making a decision.

Specialization is On Assignment's path to profits. Rather than supplying a broad range of workers, the firm looks to fill highly skilled professional roles in areas such as information technology (IT), digital marketing, finance, and government. Supplying highly skilled workers means the agency can charge a premium for temp help.

Often, demand for these temps is as much about a need for expertise as it is about employers' reluctance to hire permanently. IT, in particular, evolves so rapidly that using temp labor makes it easier for employers to bring in cutting-edge talent as needed.

The company fuels its growth with acquisitions. It bought Apex Systems to better compete in the red-hot IT market and has since boosted the division's revenue and profits by cross-selling through other divisions.

It bought Valesta, a small Belgian staffing firm known for its clinical research, biotechnology and medical device experts. CyberCoders was a 2013 acquisition, as was physician-staffing specialist Whitaker Medical. The latter was combined with Vista, a similar agency On Assignment acquired nearly a decade ago. On Assignment sold Vista for \$123 million, three times the original purchase price.

We're bullish on the company as it continues to make acquisitions, invests in existing divisions, and uses excess cash for share repurchases and debt repayment.

#5: Eastman Chemical

Eastman Chemical Co. (NYSE: EMN) is a prime example of how a so-called "boring" company can quickly become exciting. The global specialty chemical company makes the polymers and resins that most consumer goods use, selling these raw materials in 100 countries.

More than 42% of its revenue comes from the United States, but Eastman is tapping the emerging Asia-Pacific region, where a burgeoning middle-class population will

fuel consumerism and the demand for Eastman's products.

Well-diversified geographically, Eastman has no more than 18% of revenue in the 11 chemical markets it covers. Eastman's revenue is also diversified by sector, with 18% coming from transportation, 16% from building and construction, 15% from consumables and 15% from tobacco. The remaining revenue comes from seven smaller sectors.

#6: Avangrid

Utilities such as Avangrid (NYSE: AGR) deliver electricity or gas—not generate power—and that structure is even better for protecting investors in a recession than traditional utilities.

Also called “wires” or “grid” firms, these utilities are more insulated from commodity price swings because they don't buy and burn gas, coal or oil. For Avangrid, this inherent stability means both its yield and stock price will be protected when the next recession hits.

A great grid company must sit in a region where the demand for electricity remains stable in good and bad economic times. Earnings of Spain's grid operator, for example, suffered steep declines when less electricity was used as Spain's economy faltered during the 2008 financial crisis.

Avangrid's safety comes in part because its grid, or distribution business, generates 76% of revenue. That business is based on eight regulated electric and natural gas utilities serving 3.1 million customers in New York and New England, regions associated with consistent demand.

Growth is baked into the future partly because of Avangrid's strength in renewable energy, a growth industry. About a quarter of the firm's revenue comes from renewables now. Analysts at our sister publication, *Utility Forecaster*, which focuses on utilities exclusively, believe that utilities such as Avangrid, with their large wires and pipe networks, represent the future, as they are increasingly relied on to support growth in renewables such as wind and solar.

Avangrid is in a good position to take advantage of this growth. The company was formed last year by the merger of UIL Holdings, a highly regarded electric and natural gas utility, and Iberdrola USA, the second-largest U.S. wind power producer.

The company is developing renewable energy power sources at a fast clip, and its projects are usually supported by long-term power purchase agreements that shield the company from price volatility. But renewables

are only the icing on the cake. The utility will also boost revenue through a number of electric and natural gas distribution projects scheduled for the future, as well as interstate transmission expansion projects.

#7: Walgreens Boots Alliance

What if I told you that you could buy a stock today that is, (1) trading at only 11 times this year's earnings; (2) paying a forward annual dividend yield of 2.5%; (3) grew net earnings by 27% during its most recent quarter; and (4) its largest potential competitor just decided it is not going to get into this company's business?

Sounds enticing, right? Now, suppose I told you this company is PF Growth portfolio holding **Walgreens Boots Alliance** (NasdaqGS: WBA), the retail pharmacy chain that until recently was considered by many to be Amazon's next victim? Hmm... perhaps you'd like to ponder that a moment before hitting the 'Buy' button at your online brokerage account to scoop up shares while they're cheap.

That's the problem for Walgreens. Despite being a value investor's dream, it can't shake the perception that another shoe is about to drop. Consider the string of exogenous events that have dogged Walgreens over the past couple of years:

- First, it was Great Britain's decision to exit the E.U. in June 2016 that killed Walgreens' upward momentum (Walgreens is headquartered in Illinois but owns extensive operations in England and Europe).
- Next, it was a rumor in November 2017 that Amazon was contemplating entering the online pharmacy business that sent Walgreens' share price reeling. WBA dropped from above \$80 to below \$65 in just six weeks. However, as it became apparent that Amazon was not an immediate threat to its business, its share price rallied all the way back to \$80 by late January.
- Finally, the threat of a trade war with Asia and Europe in early 2018 not only drove the entire stock market into correction territory, but was particularly punishing for Walgreen's given its dual geographic identity, pushing it back below \$65.

However, some unexpected good news arrived shortly after that; CNBC reported that Amazon has abandoned its plan to enter the hospital pharmacy business due to logistical and marketing challenges.

With Amazon out of the way, it is entirely possible that none of those threats will end up having a material

impact on Walgreens' future profitability. If so, then it should only be a matter of time, and not a lot of it, until its share price starts heading back up.

Income investors should be happy about the dividend hike the company's board of directors announced this year. In June, Walgreens will pay a quarterly dividend of 40 cents per share, an increase of nearly 7%. For the record, that means 2018 will be the 42nd consecutive year that Walgreens has raised its dividend.

Growth investors should be encouraged by the fact the company raised its guidance for the remainder of 2018. Walgreens now expects its adjusted diluted EPS (earning per share) to come in between \$5.85 to \$6.05. If so, then its PEG ratio (PER to earnings growth) of 0.92 falls below the 1.0 limit that growth fund guru Peter Lynch used with great success to identify undervalued growth stocks.

#8: Marathon Petroleum

Marathon Petroleum Corp. (NYSE: MPC) has roots dating back to 1887 when the Ohio Oil Co. was formed. To this day it remains headquartered in Findlay, Ohio, and is the largest oil refiner in the Midwest. In 2011 its predecessor entity, Marathon Ashland Petroleum, split into two separate businesses, resulting in Marathon Petroleum taking full control of its "downstream" refining and pipeline assets.

Marathon conducts its refining business through seven facilities throughout the Midwest and Gulf Coast to maximize efficiency and reduce capital expenditures. These seven refineries account for almost 10% of the total refining capacity in the United States, generating over 1 million barrels per day. In addition, the company is one of the largest domestic producers of asphalt, a byproduct of the refining process.

The company also operates the largest private inland fleet of vessels, including 18 inland towboats and 205 barges that operate out of 79 company-owned light product and asphalt terminals. Its trucking division consists of 173

transport trucks that move crude oil and light products from the terminals and pipeline plants to the refineries. Marathon owns or leases over 8,400 miles of pipeline that deliver over 2 million barrels per day of crude oil and light product.

Marathon also owns the Speedway chain of gas stations and convenience stores, with more than 2,800 locations in nine states. It is the fourth-largest domestically owned and operated convenience store chain in the country, with annual merchandise sales in excess of \$4.9 billion and approximately 6 billion gallons of fuel sold.

Like all refiners, the company is subject to wide swings in the cost of crude, which can be difficult to predict, but Marathon operates a tight business model that is less susceptible to outside disruption.

#9: Chubb Ltd.

Chubb Ltd. (NYSE: CB) is one of the world's largest property and casualty insurers and operates in 54 countries. It was formed when Chubb Corp. and ACE Ltd merged.

The deal combined two of the largest insurers in the U.S. and is the largest merger ever in the insurance industry. Property and casualty insurers have been struggling against falling premiums amid tough competition in the sector, even as low interest rates have suppressed investment income.

By combining operations, the two companies save about \$650 million in expenses. We believe the deal makes solid strategic sense. Although some lines of business probably will need to be divested, we don't think that will affect the company's revenue or earnings in a big way. The upshot: Chubb Ltd. is a buy-and-hold company if ever we've seen one.

#10: Check out the Growth Portfolio on www.PFNewsletter.com for our newest Under the Radar picks!

IMPORTANT NOTES:

Guidance concerning the stocks highlighted in this report is believed to be accurate and represent our best advice at the time of writing. However, market conditions change constantly and guidance at the time of this writing may not reflect our latest advice. For our current take on any stock in this report, it is vitally important that you check the Portfolio tables on the website and confirm that the stock still earns a buy rating. Furthermore, confirm that the stock trades below our current buy limit. Do not buy any stocks above our recommended buy limits. If a stock's price exceeds our buy limit, wait for a pullback or invest in another Portfolio holding that trades below our buy limit. Any advice in the Portfolio tables, a recent issue of the publication, or our email alerts always trumps older advice in this special report. We reserve the right to substitute special reports as market trends dictate.

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