Large Cap Global Core Pick List
March 2019

Editor's Note: *We are revamping our pick lists to create a more user-friendly resource for investment ideas. We welcome any thoughts you have on aspects of our pick lists you find most useful and what you'd like to see. Ultimately, we want to know how you use our lists so that we can better serve your needs. Please submit feedback to arc@morningstar.com.*

Sector Valuations

The market appears fairly valued, with the market-capitalization-weighted average, uncertainty-adjusted price/fair value ratio for S&P 500 index constituents that are under active Morningstar research coverage at 99% as of Feb. 28, slightly higher than last month's ratio of 98%.

The S&P 500 rose by 2.97% in February, closing at 2,784.49 at the end of the month. On a relative basis, the utilities sector was the most expensive, trading at 108% of fair value. Energy was the cheapest, trading at 92% of fair value. Please refer to the table later in the report for more details on sector valuation.

As of Feb. 28, the Global Large Cap Pick List was priced at 82% of fair value. Consumer staples constituents presented the greatest opportunity, with a market-capitalization-weighted average price/fair value near 75%.

Portfolio Commentary: Changes

We made several changes to the list this month. Beginning in communication services, we added shares of **CenturyLink** CTL ($22 fair value estimate). Conversely, we removed **Comcast** CMCSA ($45 fair value estimate). Analyst Matthew Dolgin notes:

> "We believe CenturyLink's businesses lack a moat and have long-term deflationary pricing trends, so we project virtually no sales growth over our five-year forecast. However, management is hitting its synergy targets following the 2017 Level 3 acquisition and showing an ability to grow EBITDA, despite continuing revenue weakness. With the firm's 2019 guidance in line with our projections, we expect no major change to our $22 fair value estimate.
>
> "Although the dividend cut may be painful for shareholders in the near term, due both to the stock's negative reaction to the news and reduced dividend income, we strongly believe the move is good news for long-term shareholders, and we applaud management for making the move, although they probably could have foreshadowed it in a better way."

In the consumer discretionary sector, we added **Fiat Chrysler Automobiles** FCAU ($29 fair value estimate) and removed **Mattel** MAT ($21 fair value estimate). Analyst Richard Hilgert details:

> "In our view, the market continues to unfairly discount the shares of Fiat Chrysler. We have maintained significant discounts in Stage I forecast compared with management's five-year plan announced in June 2018. While management forecasts 7% annual revenue growth through 2022 to EUR 157 billion, we estimate revenue peaks at EUR 127 billion in 2020, then declines slightly in 2021 and 2022 to our midcycle assumption of EUR 124 billion, including the assumption that Magneti Marelli will be sold in the second quarter this year. Five-year plan adjusted EBIT margin reaches 9% to 11% in 2022 versus our estimated 7.2% peak in 2020, and then contraction to 5.8% in our 2022 midcycle assumption."

In the consumer staples sector, we omitted **Philip Morris International** PM ($102 fair value estimate) and **General Mills** GIS ($57 fair value estimate), while adding **Kraft Heinz** KHC ($60 fair value estimate) and **Kellogg** K ($81 fair value estimate). Analyst Erin Lash details:

> "For nearly three years, Kraft Heinz's strategic bent has centered on driving out inefficiencies from the organization (by reducing its workforce, rationalizing its North American manufacturing network, and enhancing its supply chain). And the tangible gains that have resulted from these efforts are undeniable. More specifically, the firm now boasts operating margins in the mid-20s, a level that towers above the mid- to high teens generated by its packaged-food peers.

Elizabeth Collins, CFA
Global Head of Equity and Corporate Credit Research

Daniel Rohr, CFA,
Director of Equity Research, North America

Lorraine Tan, CFA
Director of Equity Research, Asia-Pacific

Alex Morozov, CFA
Director of Equity Research, Europe

Patrick Dunn
Director of Global Research Operations

This list surfaces large-cap global stocks within each sector that we believe warrants consideration. Selection criteria are based on uncertainty-adjusted price/fair value ratios. The above-mentioned selection criteria are applied against all constituents of the Morningstar rated universe.

"However, sales have languished, falling 1% on an organic basis on average since fiscal 2015. We think the missing piece of the puzzle has been effective brand spending, which has amounted to just 2%-3% of sales annually at Kraft Heinz versus mid- to high-single-digit levels at peers. Management has articulated a desire to up the ante on its brand investments to hone its organic operations, but we've yet to see evidence that it is willing to sacrifice profitability to any material extent over a longer horizon to do so."

Turning to the energy sector, we added shares of **MPLX** MPLX ($44 fair value estimate). We dropped **Exxon Mobil** XOM ($90 fair value estimate). Analyst Stephen Ellis notes:

"The end game for MPLX is building a significant asset base at the developing NGL market hub in the northeastern United States, similar to Mont Belvieu in importance, including eventual control over NGL exporting capabilities from the East Coast. MPLX has nearly all of the assets in place to do this, with the exception of direct ethane and propane (or LPG) exporting facilities. Much of the partnership's efforts over the past few years have focused on debottlenecking NGL volumes out of the Marcellus and Utica and providing Midwestern and western Canadian producers with access to cheaper natural gasoline and condensate."

In the financials sector, **Westpac Banking** WBK ($24 fair value estimate) was removed from the list, replaced with **Mitsubishi UFJ Financial Group** MUFG ($7.12 fair value estimate). Analyst Michael Makdad details:

"MUFG is making Indonesia's Bank Danamon a consolidated subsidiary and owns roughly 20% stakes in banks in the Philippines and Vietnam. MUFG should be able to achieve returns commensurate with the cost of equity in the growing markets of Southeast Asia where it has scale and can import some expertise from more developed markets, but it will struggle to earn good returns in North America where the market is competitive and its costs are high. The key to MUFG's overall profitability remains its domestic franchise, which is mostly dependent upon the macroeconomic environment (level of interest rates, and intensity of loan demand) but also MUFG's ability to trim costs as it reconfigures operations for a more digitalized banking era."

In the healthcare sector, we removed shares of **Alexion Pharmaceuticals** ALXN ($172 fair value estimate) and **Laboratory Corp. of America** LH ($184 fair value estimate). We added **AbbVie** ABBV ($102 fair value estimate) and **Gilead Sciences** GILD ($83 fair value estimate) in their place. Analyst Karen Andersen states:

"We believe AbbVie supports a narrow moat based on patent-protected drugs, intellectual intangibles, and a powerful salesforce. As is the case for most drug firms, the core of AbbVie's moat lies in its portfolio of patent-protected drugs. However, unlike AbbVie's Big Pharma peers, which tend to carry wide moats, one drug (Humira) represents the majority of AbbVie's sales (more than 50%) and profits (greater than 70%). As a result of both emerging branded competition to Humira in the immediate term and a potential generic biosimilar threat in 2018-20, we believe excess returns are likely to persist for 10 years, but we cannot be as certain of this for our 20-year outlook, which would be needed for a wide moat rating. While we do model in Humira sales declines beginning in 2020, the rate of decline will likely be more gradual than a typical small molecule-branded drug facing generic competition, because of the complexities in developing and marketing a biosimilar (generic biologic)."

Concerning the industrials sector, we added shares of **Fluor** FLR ($50 fair value estimate) and **General Dynamics** GD ($209 fair value estimate). We dropped **Raytheon** RTN ($213 fair value estimate) and **Rolls-Royce Holdings** RYCEY ($15 fair value estimate). Analyst Chris Higgins notes:

"Incumbency and technological know-how have allowed General Dynamics to consistently generate returns well above its cost of capital. The 17% average return on invested capital from 2009 to 2017 was well above its cost of capital and supports our wide moat rating. This period included a 25% reduction in U.S. defense spending from 2008 to 2015 and a downturn in the business jet market where total deliveries in the market went from 1,315 jets in 2008 to 696 jets in 2011. General Dynamics derives its wide moat from intangible assets, efficient scale, and switching costs."

In the information technology sector **Microsoft** MSFT ($125 fair value estimate), **Qorvo** QRVO ($86 fair value estimate), and **Western Digital** WDC ($67 fair value estimate) were removed from the list. We replaced them with **Nokia** NOK ($8 fair value estimate), **Applied Materials** AMAT ($49 fair value estimate), and **Alliance Data Systems** ADS ($220 fair value estimate). Analyst Abhinav Davuluri writes:

> "With spending skewed to logic and foundry investments (particularly with extreme ultraviolet lithography accounting for a larger portion of equipment spending), Applied's share of wafer fab equipment is set to be lower in 2019. Our fair value estimate of $49 per share incorporates our view that the wide-moat firm's top line will decline in the low double digits in fiscal 2019. Nevertheless, our positive thesis on the rise in capital intensity for semiconductor fabrication is intact. As we look beyond 2019, we anticipate memory-related investments to resume growth as chipmakers pursue advanced 3D NAND and DRAM technologies that require more tools from the likes of Applied."

In the materials sector, we removed shares of **Martin Marietta Materials** MLM ($240 fair value estimate). We added **WRKCo** WRK ($53 fair value estimate) in its place. Analysts Charles Gross and Andrew Lane explain:

> "A few years of robust corrugated profitability has elicited a supply response that we expect to negatively impact WestRock's pricing over time, which will narrow margins considerably in the long run. These effects could be magnified should global shipping volumes get impacted by an increased taste for tariffs. All that said, we think the market is too pessimistic on WestRock. Our $53 per share fair value estimate assumes that consolidated operating margins contract from 9.8% in fiscal 2018 to 8.2% in fiscal 2023."

Concerning the real estate sector, we added shares of **Vornado Realty Trust** VNO ($76 fair value estimate). We dropped **Boston Properties** BXP ($143 fair value estimate). Analyst Michael Wong notes:

> "We do like several areas of Vornado's portfolio in terms of growth prospects, but even trophy properties struggle to earn excess returns, given their enormous development costs. Specifically, certain costs have outpaced asking rents over the past several years. In 2011, concrete costs (including labor) were approximately $75 per foot—those costs are now approximately $90 per foot. The main concern going forward lies in the increasing cost of labor, given the rebound in multifamily construction over the past several years. We view the real opportunity for Vornado in the expansion of Manhattan's far west side, where the Hudson Yards project is attracting a new wave of tenants."

Fair Value Changes

We made five significant fair value changes this month among the list's remaining constituents. In the information technology sector, we lowered the fair value estimate for **Baidu** BIDU to $262 per share from $322. Analyst Chelsey Tam comments:

> "In light of the weaker economy in China, trade war tensions and weaker demand for advertising, we are reducing our fair value estimate for Baidu by 19% to $262 per share. Wide-moat Baidu's shares continue to be undervalued for long-term investors. Its monthly active user base of 990 million across Baidu's family of apps poses a strong network effect and is difficult to displace. We expect revenue growth to reach 26% in 2018 and decelerate to 18% in 2019 and 15% in 2020 due to slowing economy before picking up to 17% in 2021 as the economy recovers. Revenue growth will then decelerate and reach 11% by 2022. Non-GAAP EBIT margin is expected to be 27.2% in 2018 and 20.3% in 2019 and will rise gradually to 22.3% by 2023. We assume investments in marketing, research and development and content amid intense competition will keep margins from significantly improving in the next five years. The recent weaker economy should have more adverse impact on merchants' advertising demand and therefore online marketing services segment, and less impact on the subscription of iQiyi, a key component in the others revenue segment. This is also given that paid subscription for content is still in a secular uptrend, whereas search, a key component in the online marketing services segment, is close to saturation."

Also in the information technology sector, we lowered the fair value estimate for **Activision Blizzard** ATVI to $62 per share from $69. Analyst Neil Macker comments:

> "Activision Blizzard ended 2018 on a weak note as top

and bottom-line fourth quarter non-GAAP results came in below the Street projections. The firm issued very conservative guidance for 2019 which management is now labeling a transition year. The new guidance of non-GAAP 2019 revenue of $6.3 billion is well below the previous consensus estimate of $7.3 billion. Activision also announced an 8% workforce reduction across its divisions with most of the losses hitting the nondevelopment staff. Management plans to reallocate the savings to increase size of its core franchise development teams as the firm looks to speed up the timing and cadence of its major titles and post-release content. We are maintaining our narrow economic moat rating but are lowering our fair value estimate to $62 from $69 to account for the loss of Destiny 2 and the impact of transitional 2019.

"GAAP revenue for the quarter improved 17% year over year to $2.4 billion (versus guidance of $2.2 billion). Console GAAP revenue improved by 19% year over year to $808 million as Call of Duty Black Ops 4 launched strongly in the front half of the quarter. Black Ops 4 outsold Black Ops 3 in their respective launch quarters and digital full-game downloads hit 40% versus last year's WWII installment. After the weak launch of the Destiny 2 expansion, Forsaken, in the third quarter and underperformance in the fourth quarter, Activision sold its publishing rights for the title back to its development partner, Bungie. PC GAAP revenue grew 5% to $482 million as Black Ops 4 tripled the PC copies sold by Black Ops 3."

In the financials sector, we lowered the fair value estimate for **Credit Suisse Group** CS to $20 per share from $23. Analyst Johann Scholtz comments:

"We decrease our fair value estimate for Credit Suisse to $20 from $23, this is equal to 1.3 times tangible book value as of Dec. 31, 2018, and 15 times our 2019 earnings per share estimate. Credit Suisse returned to profitability in 2018, and with a much lower drag on performance from the noncore portfolio, we anticipate robust annualised earnings growth over the next four years of 23%. We expect wealth management client-invested assets to grow 4% annually in the medium term through a combination of market gains and moderate net new money growth, mainly in Asia. We forecast that blended fees from asset management and wealth management will remain stable at 0.65% of assets under management. We anticipate investment banking fees to increase by an average of 1% annually and see a 11% compound annual growth rate in trading revenue, from a depressed base."

Also in the financials sector, we lowered the fair value estimate for **ING Groep** ING to $17 per share from $18.50. Analysts Derya Guzel and Niklas Kammer comment:

"We lower our fair value estimate to $17 from $18.5 per ADR after incorporating full-year 2018 results into our analysis, rolling our model forward, and taking a harder stance on loan loss provision assumptions. Our fair value estimate reflects a price/book ratio of 1.1 times and a price/earnings ratio of 11 times our 2019 estimates. We expect net interest income margins to remain flat at 1.7% until 2023, while net fee and commission income grows at a 3% CAGR. We anticipate cost reductions to bring ING's efficiency ratio toward the top of its targeted range of 50%-52%. Provisions for loan losses have been low over the past two years with 12 basis points and 11 basis points for 2017 and 2018, respectively. We do not think this level is sustainable, however, and anticipate the total provision ratio to trend toward 25 basis points by 2023."

In the industrials sector, we lowered the fair value estimate for **Fanuc** FANUY to $22 per share from $25. Analyst Dan Baker comments:

"Wide-moat Fanuc posted weaker third-quarter fiscal 2018 (quarter ending December 2018) results featuring an 20% year-over-year decrease in revenue and 42% decrease in operating income. Management made mild reductions to its full-year guidance with operating profit guidance reduced by 2% to JPY 147.9 billion. Highlighting the potential impact of the trade war, Fanuc's sales in China were down 56%, and the Americas were down 19%. We downgrade our earnings forecast by midteens levels and increase our capital expenditure forecasts, reducing our fair value estimate to JPY 23,700 (and USD 21.50 per ADR) from JPY 28,000 (and USD 25 per ADR) previously, and we retain our wide moat rating. Our fair value estimate implies an adjusted price/earnings ratio of 34 times."

Adjusted Price/Fair Value Ratio

Attractiveness	Lower Bound	Upper Bound	Notes
Cheap	0.000	0.800	Assets are trading at or below Morningstar's "Consider Buying" price.
Undervalued	0.801	0.900	Assets are trading above Morningstar's "Consider Buying" price, but are still at a discount to our fair value estimate.
Fully Valued	0.901	1.100	Assets are trading within a band that is not materially different from Morningstar's fair value estimate.
Overvalued	1.101	1.250	Assets are trading above Morningstar's fair value estimate, but are still below our "Consider Selling" price.
Expensive	1.251	—	Assets are trading at or above Morningstar's "Consider Selling" price.

Fair Value Per Sector

Sector	S&P Sector Weight (%)	Sector P/V (%)	Pick List P/V (%)
Communication Services	9.80	97.22	84.36
Consumer Discretionary	9.67	96.51	81.99
Consumer Staples	7.04	97.44	74.86
Energy	5.34	92.12	84.42
Financials	12.37	95.91	85.80
Health Care	14.52	103.83	81.68
Industrials	9.07	101.03	86.67
Information Technology	20.08	100.33	87.71
Materials	2.49	99.25	85.06
Real Estate	2.73	104.22	91.77
Utilities	3.21	108.00	90.48

Largest Negative and Positive Price Movements During February

Company	Ticker	Beg. Price Per Share (USD)	End Price Per Share (USD)	Return (%)
CVS Health	CVS	65.55	57.83	-11.78
Activision Blizzard	ATVI	47.24	42.14	-10.80
L Brands	LB	27.84	26.14	-6.11
Celgene	CELG	88.46	83.12	-6.04
Baidu ADR	BIDU	172.63	162.54	-5.84
Macerich	MAC	46.16	43.60	-5.55
BT Group ADR	BT	15.26	14.45	-5.31
Allergan	AGN	143.98	137.71	-4.35
Tencent Holdings ADR	TCEHY	44.61	42.81	-4.03
Fanuc ADR	FANUY	17.04	16.54	-2.91
Alexion Pharmaceuticals	ALXN	122.96	135.33	10.06
ING Groep ADR	ING	11.87	13.22	11.37
Skyworks Solutions	SWKS	73.04	81.66	11.80
Western Digital	WDC	44.99	50.30	11.80
Intel	INTC	47.12	52.96	12.39
Albemarle	ALB	80.73	91.29	13.08
Raytheon	RTN	164.76	186.50	13.19
Philip Morris International	PM	76.72	86.94	13.32
Mattel	MAT	11.84	14.42	21.79
Hanesbrands	HBI	14.99	18.59	24.02

Large Cap Global Core Picks (Data as of Feb. 28, 2019)

Company	Ticker	Economic Moat™	Uncertainty Rating	Current Price (USD)	Fair Value (USD)	Adj. Price/ Fair Value	Morningstar Rating	Market Cap (USD Mil)	Industry	Relative Attractiveness
Communication Services—Undervalued										
Vodafone Group ADR	VOD	Narrow	High	17.85	33	0.77	★★★★★	47,782.28	Telecom Services	Cheap
Telefonica ADR	TEF	Narrow	High	8.65	15	0.80	★★★★★	44,838.76	Telecom Services	Cheap
Baidu ADR	BIDU	Wide	High	162.54	262	0.81	★★★★	56,655.03	Internet Content & Information	Undervalued
BT Group ADR	BT	Narrow	High	14.45	23	0.81	★★★★	28,371.32	Telecom Services	Undervalued
Tencent Holdings ADR	TCEHY	Wide	High	42.81	64	0.83	★★★★	407,284.24	Internet Content & Information	Undervalued
CenturyLink	CTL	None	Very High	13.19	22	0.84	★★★★	14,253.90	Telecom Services	Undervalued
Activision Blizzard	ATVI	Narrow	High	42.14	62	0.84	★★★★	32,187.96	Electronic Gaming & Multimedia	Undervalued
Consumer Discretionary—Undervalued										
LKQ	LKQ	Narrow	Medium	27.70	47	0.73	★★★★★	8,814.21	Auto Parts	Cheap
Hanesbrands	HBI	Narrow	Medium	18.59	27	0.79	★★★★★	6,718.87	Apparel Manufacturing	Cheap
L Brands	LB	Narrow	High	26.14	44	0.80	★★★★	7,191.77	Apparel Stores	Undervalued
Fiat Chrysler Automobiles	FCAU	None	Very High	14.73	29	0.80	★★★★	28,930.79	Auto Manufacturers	Undervalued
Daimler	DDAIF	None	High	60.05	97	0.81	★★★★★	64,109.43	Auto Manufacturers	Undervalued
Bayerische Motoren Werke ADR	BMWYY	Narrow	High	28.16	44	0.82	★★★★	55,011.99	Auto Manufacturers	Undervalued
Volkswagen ADR	VWAPY	None	High	17.15	27	0.82	★★★★	87,591.86	Auto Manufacturers	Undervalued
Volkswagen ADR	VWAGY	None	High	17.61	27	0.83	★★★★	87,591.86	Auto Manufacturers	Undervalued
Nissan Motor ADR	NSANY	None	High	17.29	26	0.83	★★★★	33,940.69	Auto Manufacturers	Undervalued
Expedia Group	EXPE	Narrow	High	123.31	183	0.84	★★★★	18,150.04	Leisure	Undervalued
Consumer Staples—Cheap										
British American Tobacco ADR	BTI	Wide	Low	36.74	59	0.62	★★★★★	84,262.75	Tobacco	Cheap
Anheuser-Busch InBev ADR	BUD	Wide	Low	78.16	118	0.66	★★★★★	152,619.70	Beverages - Brewers	Cheap
Imperial Brands ADR	IMBBY	Wide	Low	33.60	48	0.70	★★★★★	31,986.41	Tobacco	Cheap
Kraft Heinz	KHC	None	Medium	33.19	60	0.70	★★★★★	40,473.04	Packaged Foods	Cheap
Conagra Brands	CAG	Narrow	Medium	23.37	35	0.78	★★★★★	11,349.45	Packaged Foods	Cheap
Kellogg	K	Wide	Medium	56.26	81	0.80	★★★★	19,347.51	Packaged Foods	Cheap
Energy—Undervalued										
Enterprise Products Partners	EPD	Wide	Low	27.65	36	0.78	★★★★★	60,350.59	Oil & Gas Midstream	Cheap
Energy Transfer	ET	None	Medium	14.79	22	0.78	★★★★★	38,740.80	Oil & Gas Midstream	Cheap
Total ADR	TOT	None	Medium	56.91	77	0.83	★★★★	148,358.79	Oil & Gas Integrated	Undervalued
Royal Dutch Shell ADR Class A	RDS.A	Narrow	Medium	62.21	83	0.83	★★★★	256,459.77	Oil & Gas Integrated	Undervalued
MPLX Partnership Units	MPLX	Narrow	Medium	33.16	44	0.84	★★★★	26,334.31	Oil & Gas Midstream	Undervalued
Royal Dutch Shell ADR Class B	RDS.B	Narrow	Medium	63.61	83	0.84	★★★★	256,459.77	Oil & Gas Integrated	Undervalued

Large Cap Global Core Picks (Data as of Feb. 28, 2019)

Company	Ticker	52 Week High	52 Week Low	Total Return YTD (Daily)	Total Return 1-Yr (Daily)	Div. Per Share TTM	Div. Yield % Current	Div. Yield % Forward	EPS Est. Growth % Mean 5-Yr	Forward EPS Est.
Communication Services										
Vodafone Group ADR	VOD	30.20	17.70	-7.42	-30.80	1.85	9.75	6.11	9.64	1.28
Telefonica ADR	TEF	10.22	7.70	2.25	-5.32	0.46	5.40	5.27	18.13	0.81
Baidu ADR	BIDU	284.22	153.78	2.48	-35.59	—	—	—	21.33	8.21
BT Group ADR	BT	17.51	13.53	-4.93	-7.33	1.06	6.72	4.08	4.63	1.87
Tencent Holdings ADR	TCEHY	60.00	31.54	8.46	-21.80	0.11	0.26	0.26	17.45	1.41
CenturyLink	CTL	24.20	12.74	-12.94	-13.13	2.16	16.38	7.58	-19.09	1.18
Activision Blizzard	ATVI	84.68	39.85	-9.51	-41.91	0.34	0.81	0.88	7.58	2.02
Consumer Discretionary										
LKQ	LKQ	40.20	22.74	16.73	-29.84	—	—	—	13.79	2.51
Hanesbrands	HBI	22.57	11.57	49.56	-1.08	0.60	3.23	3.23	8.46	1.87
L Brands	LB	50.26	23.71	3.00	-42.75	2.40	8.03	4.59	4.90	2.78
Fiat Chrysler Automobiles	FCAU	24.41	14.01	1.87	-30.49	—	—	5.01	5.41	4.87
Daimler	DDAIF	86.57	50.64	13.80	-24.80	4.17	7.49	7.49	-9.23	9.75
Bayerische Motoren Werke ADR	BMWYY	37.73	25.97	4.41	-15.21	1.62	5.57	5.57	-0.19	4.46
Volkswagen ADR	VWAPY	43.75	14.97	9.09	-53.53	0.93	5.47	5.47	-3.93	3.54
Volkswagen ADR	VWAGY	21.57	14.70	12.88	-9.10	0.46	2.62	2.62	-3.93	3.54
Nissan Motor ADR	NSANY	21.50	15.28	8.44	-12.83	1.02	5.70	5.78	0.80	2.67
Expedia Group	EXPE	139.77	101.37	9.46	18.43	1.24	1.01	1.04	14.61	7.64
Consumer Staples										
British American Tobacco ADR	BTI	60.81	30.67	15.32	-33.29	2.72	7.24	7.39	-16.00	4.15
Anheuser-Busch InBev ADR	BUD	117.06	64.55	18.77	-23.28	4.24	4.22	4.22	6.55	4.70
Imperial Brands ADR	IMBBY	38.87	28.70	12.89	-1.00	2.30	7.26	10.23	7.92	3.54
Kraft Heinz	KHC	68.59	31.82	-22.89	-46.77	2.50	7.53	4.82	3.39	3.06
Conagra Brands	CAG	39.43	20.22	10.40	-32.96	0.85	3.64	3.64	5.23	2.12
Kellogg	K	74.98	54.14	-1.32	-11.69	2.20	3.91	3.98	7.93	4.27
Energy										
Enterprise Products Partners	EPD	30.05	23.10	14.21	15.56	1.71	6.24	6.29	7.54	1.94
Energy Transfer	ET	19.19	11.68	14.27	3.29	1.22	8.25	8.25	-15.04	1.45
Total ADR	TOT	65.69	49.70	9.06	5.58	2.95	5.17	5.11	14.06	5.98
Royal Dutch Shell ADR Class A	RDS.A	73.86	55.04	8.37	4.27	3.76	6.04	6.04	14.81	5.76
MPLX Partnership Units	MPLX	39.01	28.32	11.58	3.36	2.44	7.63	7.81	23.51	2.47
Royal Dutch Shell ADR Class B	RDS.B	76.99	56.26	7.69	4.97	3.76	5.91	5.91	14.81	5.76

Large Cap Global Core Picks (Data as of Feb. 28, 2019)

Financials—Undervalued

Company	Ticker	Economic Moat™	Uncertainty Rating	Current Price (USD)	Fair Value (USD)	Adj. Price/ Fair Value	Morningstar Rating	Market Cap (USD Mil)	Industry	Relative Attractiveness
American International Group	AIG	None	Medium	43.20	76	0.71	★★★★★	37,561.81	Insurance - Diversified	Cheap
Capital One Financial	COF	Narrow	Medium	83.58	119	0.80	★★★★★	39,105.47	Credit Services	Undervalued
UBS Group	UBS	Narrow	High	12.67	21	0.80	★★★★	47,306.60	Banks - Global	Undervalued
Credit Suisse Group ADR	CS	Narrow	High	12.31	20	0.81	★★★★★	31,488.83	Banks - Global	Undervalued
Mitsubishi UFJ Financial Group ADR	MUFG	None	Medium	5.22	7	0.82	★★★★	67,211.81	Banks - Global	Undervalued
Wells Fargo	WFC	Wide	Medium	49.89	65	0.85	★★★★	226,970.65	Banks - Global	Undervalued
ING Groep ADR	ING	None	Medium	13.22	17	0.85	★★★★	51,514.06	Banks - Global	Undervalued

Healthcare—Undervalued

Company	Ticker	Economic Moat™	Uncertainty Rating	Current Price (USD)	Fair Value (USD)	Adj. Price/ Fair Value	Morningstar Rating	Market Cap (USD Mil)	Industry	Relative Attractiveness
Allergan	AGN	Wide	Medium	137.71	240	0.72	★★★★★	45,804.34	Drug Manufacturers - Specialty & Generic	Cheap
CVS Health	CVS	Narrow	Medium	57.83	96	0.73	★★★★★	75,010.26	Health Care Plans	Cheap
McKesson	MCK	Wide	Medium	127.16	210	0.74	★★★★★	24,392.50	Medical Distribution	Cheap
Cardinal Health	CAH	Wide	Medium	54.34	82	0.78	★★★★★	16,194.22	Medical Distribution	Cheap
Celgene	CELG	Narrow	Medium	83.12	120	0.80	★★★★	58,363.90	Drug Manufacturers - Major	Cheap
DaVita	DVA	Narrow	Medium	56.90	79	0.81	★★★★	9,468.16	Medical Care	Undervalued
Bayer ADR	BAYRY	Wide	High	20.09	32	0.81	★★★★★	74,580.98	Drug Manufacturers - Major	Undervalued
Roche Holding ADR	RHHBY	Wide	Low	34.65	42	0.83	★★★★★	236,381.24	Drug Manufacturers - Major	Undervalued
AbbVie	ABBV	Narrow	Medium	79.24	102	0.85	★★★★	116,885.62	Drug Manufacturers - Major	Undervalued
Gilead Sciences	GILD	Wide	Medium	65.02	83	0.86	★★★★	82,933.70	Drug Manufacturers - Major	Undervalued
AmerisourceBergen	ABC	Wide	Medium	83.30	106	0.86	★★★★	17,583.79	Medical Distribution	Undervalued
Bristol-Myers Squibb	BMY	Wide	Medium	51.66	65	0.86	★★★★	84,344.04	Drug Manufacturers - Major	Undervalued

Industrials—Undervalued

Company	Ticker	Economic Moat™	Uncertainty Rating	Current Price (USD)	Fair Value (USD)	Adj. Price/ Fair Value	Morningstar Rating	Market Cap (USD Mil)	Industry	Relative Attractiveness
Stericycle	SRCL	Narrow	High	44.58	83	0.77	★★★★★	4,038.72	Waste Management	Cheap
Siemens ADR	SIEGY	Narrow	Medium	54.59	78	0.80	★★★★★	88,612.15	Diversified Industrials	Undervalued
ABB ADR	ABB	Wide	Medium	19.71	25	0.85	★★★★	42,108.15	Diversified Industrials	Undervalued
Fanuc ADR	FANUY	Wide	High	16.54	22	0.88	★★★★	32,233.64	Diversified Industrials	Undervalued
Fluor	FLR	Narrow	High	37.60	50	0.88	★★★★	5,248.11	Engineering & Construction	Undervalued
General Dynamics	GD	Wide	Medium	170.22	209	0.88	★★★★	49,063.52	Aerospace & Defense	Undervalued
Emerson Electric	EMR	Wide	Medium	68.15	83	0.88	★★★★	41,886.34	Diversified Industrials	Undervalued

Large Cap Global Core Picks (Data as of Feb. 28, 2019)

Company	Ticker	52 Week High	52 Week Low	Total Return YTD (Daily)	Total Return 1-Yr (Daily)	Div. Per Share TTM	Div. Yield % Current	Div. Yield % Forward	EPS Est. Growth % Mean 5-Yr	Forward EPS Est.
Financials										
American International Group	AIG	58.85	36.16	9.62	-22.43	1.28	2.96	2.96	12.33	5.27
Capital One Financial	COF	101.44	69.90	11.10	-13.02	1.60	1.91	1.91	0.20	12.00
UBS Group	UBS	19.32	11.61	2.34	-29.79	0.66	5.12	5.12	13.90	1.49
Credit Suisse Group ADR	CS	18.79	10.23	13.35	-31.54	0.26	2.11	2.11	20.60	1.28
Mitsubishi UFJ Financial Group ADR	MUFG	7.20	4.64	7.19	-23.95	0.19	3.59	3.59	3.40	0.70
Wells Fargo	WFC	59.82	43.02	9.24	-11.68	1.64	3.41	3.61	9.10	5.71
ING Groep ADR	ING	18.00	10.21	24.02	-20.78	0.72	5.34	5.34	3.40	1.64
Healthcare										
Allergan	AGN	197.00	125.84	3.58	-8.83	2.88	2.11	2.15	12.58	9.11
CVS Health	CVS	82.15	57.56	-10.97	-11.66	2.00	3.46	3.46	8.98	6.80
McKesson	MCK	160.87	106.11	15.46	-13.78	1.46	1.19	1.23	7.64	14.17
Cardinal Health	CAH	73.23	42.17	21.84	-18.75	1.89	3.48	3.51	59.29	5.37
Celgene	CELG	95.30	58.59	29.69	-4.59	—	—	—	16.56	14.61
DaVita	DVA	79.11	48.25	10.57	-20.99	—	—	—	15.67	4.86
Bayer ADR	BAYRY	32.80	16.58	14.34	-28.51	0.84	4.05	4.05	6.98	2.04
Roche Holding ADR	RHHBY	34.98	26.30	11.49	23.60	1.05	3.12	3.16	7.10	2.49
AbbVie	ABBV	121.45	75.77	-12.89	-28.18	3.59	4.98	5.40	14.59	8.66
Gilead Sciences	GILD	82.72	60.32	3.95	-14.52	2.28	3.51	3.88	14.15	7.05
AmerisourceBergen	ABC	101.39	69.36	12.50	-10.82	1.54	1.87	1.92	7.56	7.47
Bristol-Myers Squibb	BMY	68.22	44.30	0.17	-19.53	1.61	3.12	3.17	19.34	4.36
Industrials										
Stericycle	SRCL	71.43	34.36	21.50	-28.87	—	—	—	8.58	4.25
Siemens ADR	SIEGY	70.90	51.51	1.22	-13.97	2.15	3.98	3.98	3.89	4.61
ABB ADR	ABB	24.74	18.05	3.68	-15.45	0.83	4.19	4.19	11.19	1.36
Fanuc ADR	FANUY	25.89	14.10	9.83	-31.66	0.83	4.81	6.37	-1.82	0.58
Fluor	FLR	62.08	29.78	16.77	-32.81	0.84	2.23	2.23	16.86	3.72
General Dynamics	GD	230.00	143.87	8.87	-21.81	3.63	2.19	2.19	8.84	12.64
Emerson Electric	EMR	79.70	55.39	14.88	-1.35	1.95	2.86	2.88	9.14	4.07

Large Cap Global Core Picks (Data as of Feb. 28, 2019)

Company	Ticker	Economic Moat™	Uncertainty Rating	Current Price (USD)	Fair Value (USD)	Adj. Price/ Fair Value	Morningstar Rating	Market Cap (USD Mil)	Industry	Relative Attractiveness
Information Technology—Undervalued										
Microchip Technology	MCHP	Wide	Medium	86.87	112	0.85	★★★★	20,585.49	Semiconductors	Undervalued
DXC Technology	DXC	None	High	65.86	91	0.86	★★★★	17,668.34	Information Technology Services	Undervalued
Qualcomm	QCOM	Narrow	High	53.39	72	0.87	★★★★	64,618.22	Semiconductors	Undervalued
Intel	INTC	Wide	Medium	52.96	65	0.88	★★★★	238,161.12	Semiconductors	Undervalued
Nokia Oyj ADR	NOK	None	High	6.09	8	0.88	★★★★	33,828.12	Communication Equipment	Undervalued
Skyworks Solutions	SWKS	Narrow	High	81.66	105	0.89	★★★★	14,214.12	Semiconductors	Undervalued
Applied Materials	AMAT	Wide	High	38.34	49	0.89	★★★★	36,399.71	Semiconductor Equipment & Materials	Undervalued
Alliance Data Systems	ADS	Narrow	High	173.00	220	0.89	★★★★	9,168.60	Credit Services	Undervalued
Canon ADR	CAJ	None	Medium	28.80	34	0.90	★★★★	31,171.55	Business Equipment	Undervalued
Materials—Undervalued										
Albemarle	ALB	Narrow	High	91.29	130	0.85	★★★★	9,654.27	Specialty Chemicals	Undervalued
WRKCo A	WRK	None	High	37.38	53	0.85	★★★★	9,545.83	Packaging & Containers	Undervalued
Real Estate—Fully Valued										
Macerich	MAC	Narrow	High	43.60	57	0.88	★★★★	6,154.63	REIT - Retail	Undervalued
Vornado Realty Trust	VNO	None	High	67.31	76	0.94	★★★	12,824.94	REIT - Office	Fully Valued
Utilities—Fully Valued										
Dominion Energy	D	Wide	Low	74.09	84	0.88	★★★★	59,869.70	Utilities - Diversified	Undervalued

Large Cap Global Core Picks (Data as of Feb. 28, 2019)

Company	Ticker	52 Week High	52 Week Low	Total Return YTD (Daily)	Total Return 1-Yr (Daily)	Div. Per Share TTM	Div. Yield % Current	Div. Yield % Forward	EPS Est. Growth % Mean 5-Yr	Forward EPS Est.
Information Technology										
Microchip Technology	MCHP	104.20	60.70	21.29	-0.68	1.46	1.68	1.68	11.44	6.86
DXC Technology	DXC	96.75	49.19	23.87	-26.55	0.75	1.14	1.15	6.11	8.73
Qualcomm	QCOM	76.50	48.56	-6.19	-15.00	2.43	4.55	4.65	14.29	4.70
Intel	INTC	57.60	42.36	13.52	9.91	1.20	2.29	2.38	6.56	4.91
Nokia Oyj ADR	NOK	6.65	5.07	4.64	9.08	0.24	3.88	3.88	18.20	0.35
Skyworks Solutions	SWKS	115.98	60.12	22.41	-23.92	1.40	1.79	1.86	11.23	7.47
Applied Materials	AMAT	62.40	28.79	17.72	-32.04	0.70	2.09	2.09	6.75	3.95
Alliance Data Systems	ADS	250.27	142.58	15.69	-27.23	2.28	1.35	1.46	-13.86	25.39
Canon ADR	CAJ	38.51	26.37	4.35	-22.56	1.51	2.50	5.27	0.05	1.85
Materials										
Albemarle	ALB	112.90	71.89	18.45	-7.77	1.34	1.47	1.61	11.31	6.30
WRKCo A	WRK	67.96	35.20	0.20	-40.47	1.75	4.74	4.87	10.00	8.29
Real Estate										
Macerich	MAC	60.95	40.90	2.47	-20.97	2.97	6.83	6.88	-7.52	0.36
Vornado Realty Trust	VNO	77.59	59.48	9.58	5.10	2.52	3.79	3.92	-5.50	1.67
Utilities										
Dominion Energy	D	77.19	61.53	4.96	5.77	3.28	4.62	4.62	6.37	4.22

Fair Value Changes

Company	Ticker	Old Fair Value (USD)	New Fair Value (USD)	Change (%)
Baidu ADR	BIDU	322	262	-18.63
Credit Suisse Group ADR	CS	23	20	-13.04
Fanuc ADR	FANUY	25	22	-12.00
Activision Blizzard	ATVI	69	62	-10.14
ING Groep ADR	ING	18.5	17	-8.11
Canon ADR	CAJ	36	34	-5.56
CBS Class B	CBS	71	68	-4.23
Microsoft	MSFT	130	125	-3.85
Macerich	MAC	59	57	-3.39
DaVita	DVA	81	79	-2.47
BT Group ADR	BT	23.5	23	-2.13
Raytheon	RTN	212	213	0.47
Expedia Group	EXPE	180	183	1.67
Vodafone Group ADR	VOD	32	33	3.13

Research Methodology for Valuing Companies

Overview

At the heart of our valuation system is a detailed projection of a company's future cash flows, resulting from our analysts' research. Analysts create custom industry and company assumptions to feed income statement, balance sheet, and capital investment assumptions into our globally standardized, proprietary discounted cash flow, or DCF, modeling templates. We use scenario analysis, in-depth competitive advantage analysis, and a variety of other analytical tools to augment this process. Moreover, we think analyzing valuation through discounted cash flows presents a better lens for viewing cyclical companies, high-growth firms, businesses with finite lives (e.g., mines), or companies expected to generate negative earnings over the next few years. That said, we don't dismiss multiples altogether but rather use them as supporting cross-checks for our DCF-based fair value estimates. We also acknowledge that DCF models offer their own challenges (including a potential proliferation of estimated inputs and the possibility that the method may miss short-term market-price movements), but we believe these negatives are mitigated by deep analysis and our long-term approach.

Morningstar's equity research group (we", "our") believes that a company's intrinsic worth results from the future cash flows it can generate. The Morningstar Rating for stocks identifies stocks trading at a discount or premium to their intrinsic worth—or fair value estimate, in Morningstar terminology. Five-star stocks sell for the biggest risk-adjusted discount to their fair values, whereas 1-star stocks trade at premiums to their intrinsic worth.

Four key components drive the Morningstar rating: (1) our assessment of the firm's economic moat, (2) our estimate of the stock's fair value, (3) our uncertainty around that fair value estimate and (4) the current market price. This process ultimately culminates in our single-point star rating.

Economic Moat

The concept of an economic moat plays a vital role not only in our qualitative assessment of a firm's long-term investment potential, but also in the actual calculation of our fair value estimates. An economic moat is a structural feature that allows a firm to sustain excess profits over a long period of time. We define economic profits as returns on invested capital (or ROIC) over and above our estimate of a firm's cost of capital, or weighted average cost of capital (or WACC). Without a moat, profits are more susceptible to competition. We have identified five sources of economic moats: intangible assets, switching costs, network effect, cost advantage, and efficient scale.

Companies with a narrow moat are those we believe are more likely than not to achieve normalized excess returns for at least the next 10 years. Wide-moat companies are those in which we have very high confidence that excess returns will remain for 10 years, with excess returns more likely than not to remain for at least 20 years. The longer a firm generates economic profits, the higher its intrinsic value. We believe low-quality, no-moat companies will see their normalized returns gravitate toward the firm's cost of capital more quickly than companies with moats.

To assess the sustainability of excess profits, analysts perform ongoing assessments of the moat trend. A firm's moat trend is positive in cases where we think its sources of competitive advantage are growing stronger; stable where we don't anticipate changes to competitive advantages over the next several years; or negative when we see signs of deterioration.

Morningstar Equity Research Star Rating Methodology

Economic Moat   Stewardship
Financial Health   Moat Trend
Fundamental Analysis

Morningstar Fair Value
Valuation

$\frac{\text{Price}}{\text{Fair Value}}$
Uncertainty
Margin of Safety

Morningstar Rating™ For Stocks
★★★★★

Estimated Fair Value

Combining our analysts' financial forecasts with the firm's economic moat helps us assess how long returns on invested capital are likely to exceed the firm's cost of capital. Returns of firms with a wide economic moat rating are assumed to fade to the perpetuity period over a longer period of time than the returns of narrow-moat firms, and both will fade slower than no-moat firms, increasing our estimate of their intrinsic value.

Our model is divided into three distinct stages:

Stage I: Explicit Forecast

In this stage, which can last five to 10 years, analysts make full financial statement forecasts, including items such as revenue, profit margins, tax rates, changes in working-capital accounts, and capital spending. Based on these projections, we calculate earnings before interest, after taxes (EBI) and the net new investment (NNI) to derive our annual free cash flow forecast.

Stage II: Fade

The second stage of our model is the period it will take the company's return on new invested capital—the return on capital of the next dollar invested ("RONIC")—to decline (or rise) to its cost of capital. During the Stage II period, we use a formula to approximate cash flows in lieu of explicitly modeling the income statement, balance sheet, and cash flow statement as we do in Stage I. The length of the second stage depends on the strength of the company's economic moat. We forecast this period to last anywhere from one year (for companies with no economic moat) to 10–15 years or more (for wide-moat companies). During this period, cash flows are forecast using four assumptions: an average growth rate for EBI over the period, a normalized investment rate, average return on new invested capital (RONIC), and the number of years until perpetuity, when excess returns cease. The investment rate and return on new invested capital decline until a perpetuity value is calculated. In the case of firms that do not earn their cost of capital, we assume marginal ROICs rise to the firm's cost of capital (usually attributable to less reinvestment), and we may truncate the second stage.

Stage III: Perpetuity

Once a company's marginal ROIC hits its cost of capital, we calculate a continuing value, using a standard perpetuity formula. At perpetuity, we assume that any growth or decline or investment in the business neither creates nor destroys value and that any new investment provides a return in line with estimated WACC.

Because a dollar earned today is worth more than a dollar earned tomorrow, we discount our projections of cash flows in stages I, II, and III to arrive at a total present value of expected future cash flows. Because we are modeling free cash flow to the firm—representing cash available to provide a return to all capital providers—we discount future cash flows using the WACC, which is a weighted average of the costs of equity, debt, and preferred stock (and any other funding sources), using expected future proportionate long-term, market-value weights.

Uncertainty around that fair value estimate

Morningstar's Uncertainty Rating captures a range of likely potential intrinsic values for a company and uses it to assign the margin of safety required before investing, which in turn explicitly drives our stock star rating system. The Uncertainty Rating represents the analysts' ability to bound the estimated value of the shares in a company around the Fair Value Estimate, based on the characteristics of the business underlying the stock, including operating and financial leverage, sales sensitivity to the overall economy, product concentration, pricing power, and other company-specific factors.

Analysts consider at least two scenarios in addition to their base case: a bull case and a bear case. Assumptions are chosen such that the analyst believes there is a 25% probability that the company will perform better than the bull case, and a 25% probability that the company will perform worse than the bear case. The distance between the bull and bear cases is an important indicator of the uncertainty underlying the fair value estimate.

Our recommended margin of safety widens as our uncertainty of the estimated value of the equity increases. The more uncertain we are about the estimated value of the equity, the greater the discount we require relative to our estimate of the value of the firm before we would recommend the purchase of the shares. In addition, the uncertainty rating provides guidance in portfolio construction based on risk tolerance.

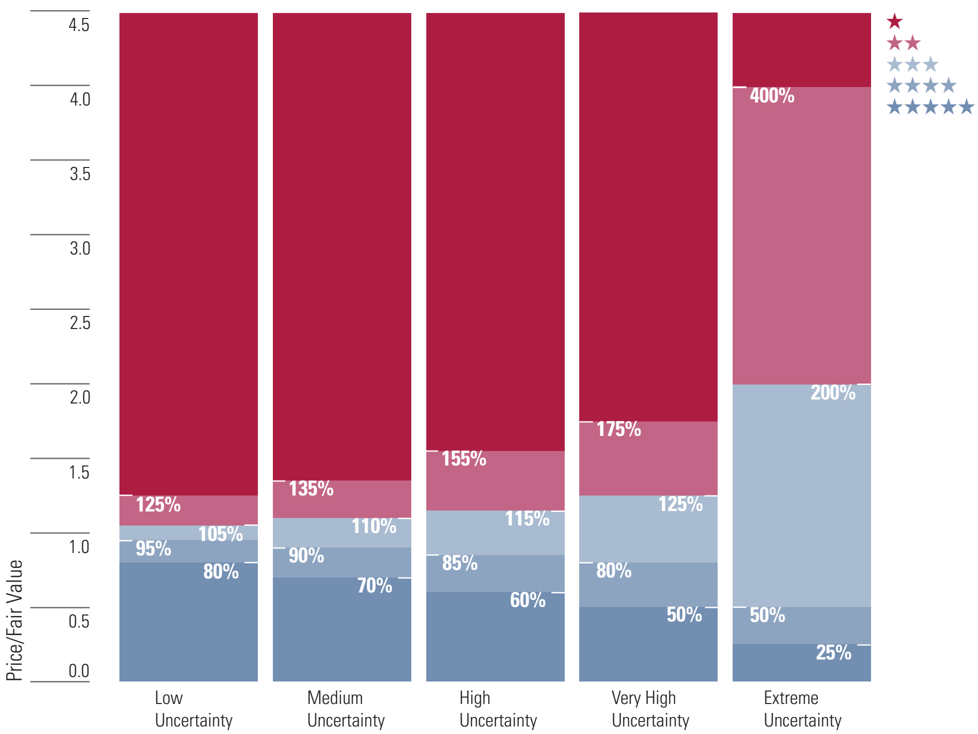
Our uncertainty ratings for our qualitative analysis are low, medium, high, very high, and extreme.

- Low–margin of safety for 5-star rating is a 20% discount and for 1-star rating is 25% premium.
- Medium–margin of safety for 5-star rating is a 30% discount and for 1-star rating is 35% premium.
- High–margin of safety for 5-star rating is a 40% discount and for 1-star rating is 55% premium.
- Very High–margin of safety for 5-star rating is a 50% discount and for 1-star rating is 75% premium.
- Extreme–margin of safety for 5-star rating is a 75% discount and for 1-star rating is 300% premium.

basis, and the star rating is automatically re-calculated at the market close on every day the market on which the stock is listed is open. Our analysts keep close tabs on the companies they follow, and, based on thorough and ongoing analysis, raise or lower their fair value estimates as warranted.

Please note, there is no predefined distribution of stars. That is, the percentage of stocks that earn 5 stars can fluctuate daily, so the star ratings, in the aggregate, can serve as a gauge of the broader market's valuation. When there are many 5-star stocks, the stock market as a whole is more undervalued, in our opinion, than when very few companies garner our highest rating.

Morningstar Equity Research Star Rating Methodology



Market Price

The market prices used in this analysis and noted in the report come from exchange on which the stock is listed which we believe is a reliable source.

For more details about our methodology, please go to www.global.morningstar.com/equitydisclousures.

Morningstar Star Rating for Stocks

Once we determine the fair value estimate of a stock, we compare it with the stock's current market price on a daily

We expect that if our base-case assumptions are true the market price will converge on our fair value estimate over time, generally within three years (although it is impossible to predict the exact time frame in which market prices may adjust).

Our star ratings are guideposts to a broad audience and individuals must consider their own specific investment goals, risk tolerance, tax situation, time horizon, income needs, and complete investment portfolio, among other factors.

The Morningstar Star Ratings for stocks are defined below:

★★★★★ We believe appreciation beyond a fair risk-adjusted return is highly likely over a multiyear time frame. Scenario analysis developed by our analysts indicates that the current market price represents an excessively pessimistic outlook, limiting downside risk and maximizing upside potential.

★★★★ We believe appreciation beyond a fair risk-adjusted return is likely.

★★★ Indicates our belief that investors are likely to receive a fair risk-adjusted return (approximately cost of equity).

★★ We believe investors are likely to receive a less than fair risk-adjusted return.

★ Indicates a high probability of undesirable risk-adjusted returns from the current market price over a multiyear time frame, based on our analysis. Scenario analysis by our analysts indicates that the market is pricing in an excessively optimistic outlook, limiting upside potential and leaving the investor exposed to Capital loss.

Risk Warning

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