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HEIJIN CAPITAL BI-WEEKLY INVESTMENT COMMENTARY

December 1st – December 15th, 2019

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Commentary Overview

Market Snapshot

INDEX	CLOSE	2 WEEKS	YTD
Dow Jones Industrial Average	28,135	+1.27%	+20.51%
S&P 500 Index	3,169	+1.76%	+26.25%
NASDAQ	8,735	+1.95%	+31.04%
10-yr Treasury Yield	1.82%	+0.04%	-0.9%
Oil ($/bbl)	$60.07	+8.4%	+30.4%
Bonds	$112.81	-0.4%	+8.2%

*bonds are represented by the iShares Core U.S. Aggregate Bond ETF (NYSEARCA:AGG)

Market Outlook & Strategy

Investment Analysis

SK Hynix: Investing in Smartphone Memory

As smartphone makers run out of options and ideas on how to improve the hardware of the devices enough to convince people to buy a new smartphone, they have begun to rely on software and software-related upgrades to justify new smartphone purchases. For instance, the common practice in recent years of adding more and more cameras lenses to the smartphones is not due to a novel breakthrough invention that allowed the combination of camera images from multiple lenses. Indeed, from a technological standpoint, it would have already been possible to include two camera lenses on the iPhone 5 or even earlier. However, during that time, hardware changes for each upgrade, such as fingerprint sensor, impermeability, or standard hardware improvements, were significant enough to justify new smartphone models. Nevertheless, since the iPhone 6 smartphone generation, smartphone markers were not able to make significant visible hardware upgrades, besides removing the bezel, so they began focusing on software upgrades such as multiple cameras or face recognition.

Although adding a camera is a hardware improvement, the real challenge was to build the imaging processing software to combine both camera images. Similarly, the infrared camera used for FaceID was not the breakthrough, but the software behind it was. There are many similar examples with other new smartphone features, but what all these smartphone features have in common is a higher requirement for memory, more precisely DRAM. DRAM, a specific type of RAM, is a type of memory that smartphones (and computers) use to store data used by the processor. DRAM is about 100 times faster than the storage people use to save files, photos or videos. Although the higher speed, DRAM is not used as storage because it is significantly more expensive, and all the data gets lost when the device shuts down. Applications such as dual cameras increase the demand for DRAM significantly since multiple pictures need to be stored before the processor can process them.

Another major upgrade for smartphones that will gain traction in the next year is 5G. Similarly to how multiple cameras lead to higher requirements for DRAM, faster internet and the expected data volumes will also lead to higher DRAM requirements. Moreover, everything that requires AI, such as AI interfacing for 5G, will further increase the demand for DRAM.

The DRAM market, as the general semiconductor market, suffered from overproduction and high competition over the last few years. Sometimes the prices were pushed down so hard by competition that manufacturers produced at cost. The semiconductor market is currently in a very pessimistic mood, which might have lead companies to underestimate the potential growth in the DRAM market. For instance, the demand growth for DRAM is expected to increase by 25% in 2020, over 18% in 2019, but stocks do not seem to reflect this.

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An opportunity to profit from the surge in DRAM demand the South Korean company SK Hynix. The company is the largest producer of DRAM and delivers to high profile companies such as Apple and Google. In terms of market share, SK Hynix has the highest yearly market share growth in the sector. The company did not have an easy month since it corrected guidance for it corrected its expectations for profit and sales downwards; however, its stock price has remained stable, suggesting that investors were already pricing in the correction and were still confident of the company.

Heijin's take on the situation is that an overly pessimistic semiconductor market has blinded investors from recognizing the potential upside of the DRAM market due to increased implementation of software and memory costly upgrades and due to 5G's natural increase of memory requirements. SK Hynix is the leading DRAM producer, and it has recently corrected its forecasts downwards, which significantly reduces the downside risk since investors are already pricing it in.

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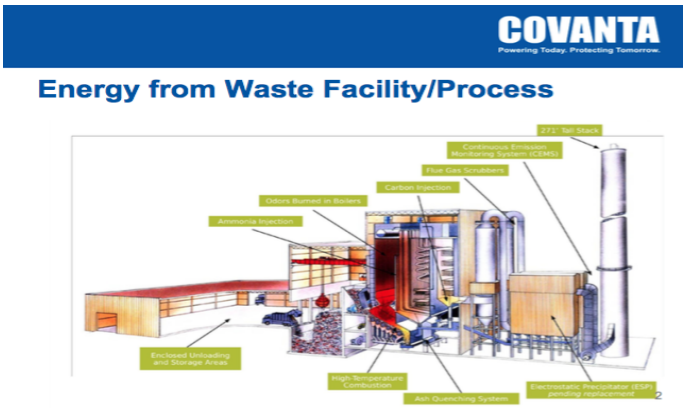
Investment Analysis
Alternative Energy

It is clear that 2019/20 is the year of climate awareness, with the likes of the teenage activist Greta Thunberg winning the Times person of the year 2019. Even fossil fuel behemoths such as Shell and BP, acknowledge the fact that they are situated in a dying industry in need of evolution. With their research indicating that by 2050 one-third of the world's energy will need to come from solar, wind, and other renewable resources. The continued depletion of fossil fuel stores, worsening of the climate crisis and increased energy demand from an ever-increasing population means that this sector is, and will continue to be one of the most important sectors of our lifetime. The following firms are some of the most promising Alternative energy stocks on Heijin's radar:

Covanta holdings corp. (NYSE: CVA) - Covanta Environmental Solutions is a leading provider of environmental services across a wide range of industries including pharmaceuticals, consumer products, health and beauty, food, automotive, chemicals, and other industrial manufacturers. Their services help solve some of the toughest challenges faced by these industries. One of Convanta's holdings divisions is a waste recycling plant, that converts refuse into clean energy. Covanta's Energy-from-Waste facilities (see figure 1 for details of process) annually convert approximately 21 million tons of waste into power for over one million homes and recycle approximately 600,000 tons of metal. Which to put it into perspective, it is enough to build nearly six Golden Gate Bridges and manufacture three billion aluminum beverage cans every year. According to the U.S. EPA, for every ton of municipal solid waste processed at Energy-from-Waste facilities, greenhouse gas emissions are reduced by approximately one ton. This is due to the avoidance of methane from landfills, the offset of greenhouse gases from fossil fuel electrical production and the recovery of metals for recycling.



The energy company reported $0.10 earnings, the per share for the previous quarter, topping analysts' consensus estimates of $0.04 by $0.06. The company also marginally beat analysts' revenue estimates of $464.96 million, generating $465 million. Covanta had a net margin of 0.37% and a return on equity of 0.69%. The business's revenue for the quarter was up 2.0% compared to the same quarter last year. The firm is currently trading over 20% below its fair

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value ($14.69 'v' $19.36). Despite the firm's mid-level volatility, the firm has good growth potential, a solid and diverse revenue stream and a brilliant dividend yield at 6.81%.

NextEra Energy Inc (NYSE: NEE) - Nextera energy is the world's largest producer of solar and wind energy in the world, with 45,900 megawatts of generating capacity. Combined with its subsidiary companies, Florida Power & Light, NextEra Energy Resources, NextEra Energy Partners, Gulf Power Company, and NextEra Energy ServicesNextera provides energy to 5 million homes in Florida. By 2030, Nextera aims to install more than 30 million solar panels across Florida. In addition to wind and solar, NextEra Energy Resources owns and operates generating plants powered by natural gas, nuclear energy, and oil. Nextera energy stock is showing serious, robust growth with revenues up 26% year-on-year, with earnings for the next year predicted to grow an impressive 10.7%. The firm, beat their EPS estimate by $0.12, at $2.39. Moreover organic EPS growth is expected to rise over 10% YonY in the coming years. NextEra Energy also had a return on equity of 10.59% and a net margin of 16.92%. Nextera has also been able to negate the risk from cheap natural gas, by gaining exposure to the market themselves. All in all, NextEra looks like they will continue to maintain the stranglehold they have over the solar/wind renewables market. Heijin sees this as a classic growth play with a high, reliable dividend profile (2.11%).

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