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# INVESTMENT COMMENTARY & OUTLOOK

**January 27, 2020**

2019 was a year of great stock market performance and flat earnings. In some respects, it was the opposite of 2018 when earnings were up more than 20% while stocks were down. Yet if we take the averages for both years for both EPS growth and stock performance, the two years were pretty normal—on average. The 4th quarter of 2019 will be the last lackluster quarter for the S&P 500's earnings. Looking forward to 2020, the S&P 500 will be having much more favorable year-over-year comparisons, so we expect positive guidance from many flagship companies.

We are off to a strong start to the New Year, which feels like 1999, and was our strongest year ever. That is the good news. The bad news is that you may remember that the stock market peaked early the following year in March 2000. Since we have been publishing research for 40+ years, we feel obligated to tell you the similarities between 1999 and today.

First, big technology stocks are increasingly dominating the S&P 500. Not only does the technology sector now represent approximately 29% of the S&P 500, but just five technology stocks, namely Apple, Alphabet (Google), Amazon.com, Facebook, and Microsoft, now account for approximately 18% of the S&P 500. Back in March 2000, seven giant technology stocks accounted for a whopping 54% of the S&P 500! What is happening is that the capitalization weighting of the S&P 500, the NASDAQ 100, and over $4+ trillion in ETFs are all systematically pouring money into technology stocks.

*Navellier & Associates does not own* **Apple, Alphabet** (Google), **Amazon, Facebook**, *and* **Microsoft** *in managed accounts and our sub-advised mutual fund. Louis Navellier and his family own* **Apple**, *and* **Amazon**, *but do not own* **Alphabet** (Google), **Facebook**, *and* **Microsoft** *in personal accounts.*

Second, although capitalization weighted indexing ignores fundamentals, eventually, one of the giant technology stock bubbles will be "pricked," so the question is: when will that happen? Sometime in 2021 is our most likely guess, after the Presidential election and possibly another Fed key interest rate hike.

Third, according to *The Wall Street Journal*, approximately 40% of the stocks in the S&P 500 and 75% of the IPO market do not have positive earnings. Some of these money-losing stocks could trigger a correction, especially now that U.S. manufacturing activity is at a 10-year low due to Boeing's woes, a glut of vehicles for sale, and a slowing domestic energy sector.

*Navellier & Associates does not own Boeing in managed accounts and our sub-advised mutual fund. Louis Navellier and his family do not own Boeing in personal accounts.*

Fourth, China is still struggling and its vehicle sales plunged 8.2% in 2019 to 25.8 million vehicles. This was the second straight year that vehicle sales contracted in China, which is now impacting global growth, like German industrial production and factory orders. Although "Phase One" of the U.S. trade deal was recently implemented and the U.S. removed China as a "currency manipulator," China's supply channels have been disrupted and its imports to the U.S. plunged 20.9% last year, so it will be interesting if China gets its "mojo" back or will be permanently impacted by the U.S. trade tiff.

Finally, we noticed during the NCAA National Championship Game in the Superdome that as President Trump and the First Lady came on the field with the military before the National Anthem that the crowd was chanting "USA, USA," which naturally bodes well for his re-election chances in November. Although most of those football fans were likely from "red states" the South because the teams were from Louisiana and South Carolina, it will be interesting if President Trump tries to make a "cameo" appearance on the field with the military again at the Superbowl, which is expected to be a more diverse crowd.

It is obvious to us that Wall Street likes President Trump's optimistic message and is anticipating his re-election, so a major correction may be postponed until 2021. As a side note, 3.5% unemployment at a 50-year low and a record number of people working has been an electoral advantage in every election in recent memory.

## INDEXING DOMINATION

Despite the fact that small-to-mid capitalization stocks are in the midst of a "January effect" and "melting up" on higher trading volume, index investing continues to make big mega-capitalization stocks even bigger, which is why there are now three companies with over $1 trillion market capitalizations. The following S&P 500 decline chart from Bespoke illustrates that so far this year, indexing has caused some interesting anomalies, like the fact that the stocks that have done the best so far this year have (1) High Share Prices, (2) High Market Capitalization, (3) High P/E Ratios, (4) Highest Price to Sales, (5) Lowest Dividend Yields, and (6) Best Performance in 2019:

**S&P 500 Decile Performance: YTD 2020 (Through 1/17)**

| | Decile 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | Decile 10 |
|---|---|---|---|---|---|---|---|---|---|---|
| Share Price (Highest to Lowest) | 3.67% | 4.03% | 1.99% | 2.51% | 1.44% | 3.07% | 2.29% | 1.36% | 0.77% | 1.40% |
| Market Cap (Largest to Smallest) | 2.91% | 2.65% | 2.05% | 2.08% | 2.65% | 2.40% | 2.31% | 2.44% | 1.68% | 1.36% |
| P/E Ratio (Lowest to Highest) | 0.17% | 1.10% | 2.05% | 1.69% | 1.58% | 2.41% | 2.04% | 3.45% | 4.05% | 3.99% |
| PEG Ratio (Lowest to Highest) | 1.34% | 1.47% | 2.24% | 2.91% | 2.52% | 2.87% | 2.14% | 2.47% | 2.16% | 1.69% |
| Price to Sales (Lowest to Highest) | 0.23% | 1.33% | 2.35% | 2.42% | 0.66% | 1.32% | 2.08% | 3.76% | 3.89% | 4.50% |
| Dividend Yield (Highest to Lowest)* | 1.54% | 0.90% | 0.91% | 1.87% | 1.32% | 2.61% | 2.17% | 3.72% | 3.01% | 3.61% |
| Short Interest (Lowest to Highest) | 2.03% | 1.97% | 2.90% | 2.67% | 1.48% | 2.13% | 1.72% | 2.09% | 2.90% | 2.64% |
| % Institutional Owners. (Lowest to Highest) | 1.63% | 3.37% | 1.21% | 2.37% | 2.27% | 2.18% | 2.62% | 2.98% | 2.23% | 1.68% |
| Analyst Ratings (Best to Worst) | 2.75% | 1.63% | 2.40% | 2.52% | 2.12% | 2.76% | 2.11% | 2.09% | 2.37% | 1.78% |
| % International Revenues (Most to Least)** | 2.69% | 2.24% | 3.66% | 3.05% | 2.14% | 2.60% | 2.94% | 2.52% | 2.36% | 1.22% |
| 2019 % Chg (Best to Worst) | 3.40% | 3.16% | 2.81% | 2.58% | 1.94% | 3.03% | 1.57% | 1.05% | 1.21% | 1.85% |

*Decile 10 of dividend yield category is made up of all stocks that pay no dividend.
**Decile 10 of international revenues category is made up of all stocks that have no international revenues.

Source: Bespoke

These are some interesting anomalies that are suggesting that some stocks are now grossly overvalued. Naturally, Tesla fits the definition of a stock that hits all six of these Bespoke criteria and is the poster stock for overvaluation. Tesla was recently worth more than both Ford or GM combined and trades at over 10 times sales.

Navellier & Associates does not own Tesla General Motors of Ford in managed accounts and our sub-advised mutual fund. Louis Navellier and his family do not own Tesla General Motors or Ford in personal accounts.

In the third quarter, Tesla's U.S. sales plunged 39%, but its international sales for the Model 3 soared. Despite its third-quarter earnings surprise, Tesla has missed analyst consensus estimates in 3 of the past 4 quarters, so if the company misses again, its "bubble" could be "pricked." Furthermore, new Tesla registrations plunged 46.5%

in California (its biggest domestic market) during the fourth quarter, according to a Dominion Cross-Sell report, which collates data from state motor vehicle records.

We should also add that Tesla's Model 3 and upcoming Model Y are expected to have strong international sales, but these two models will eventually be overwhelmed by all the electric vehicle competition in the pipeline from VW Group (Audi, Bentley, Lamborghini, Seat, Porsche, and VW), Jaguar, Mercedes, and Volvo. As a result, we expect Tesla's bubble will eventually be "pricked" when its international sales peak.

Another interesting stock market anomaly is that after Apple's stock soared 89% in 2019 while energy stocks in the S&P 500 barely rose 6% (including dividends), Apple is now worth more than all the energy stocks in the S&P 500! One reason for the "Apple versus energy sector price anomaly" is that many "blue states" have banned fossil fuel investments, so there has been persistent selling pressure in energy companies from ESG (Environmental, Social & Corporate Governance) index products.

Frankly, without energy, the U.S. economy would grind to a halt, including virtually all Apple products. Clearly, a bubble is forming under some stocks that are overweighted in the S&P 500 (as well as the NASDAQ 100), while some stocks that are underweighted are lagging the S&P 500, partially because they are excluded from ESG index products. The big news in 2020 may be the "mean reversion" in many energy stocks, especially now that the U.S. is the largest energy producer and exporter in the world!

In the meantime, we are proud to announce that Jason Bodner from Navellier MarketMail did a new white paper for our Private Client Group entitled "Pump Up the Volume." In this fascinating white paper, Jason thoroughly analyzes the "Big Money" flow on Wall Street from indexing and ETFs and strives to analyze its potential impact. The "Velocity of Big Money" from indexing and ETFs now dominates trading and has recently caused a perpetually overbought market. Jason's exhaustive research concluded that as trading volume slows, a pullback or consolidation could soon be forthcoming. Here is a link to Jason's new white paper:

**CLICK HERE: Navellier White Paper: Pump Up The Volume**

## SUMMARY

Our dividend growth and conservative growth portfolios do not own any "bubble stocks" since we are careful to always have strong sales and even stronger earnings due to profit margin expansion. The bottom line is all good bull markets like to climb a "wall of worry" and we really do not see any major risk outside of some "bubble stocks" being "pricked" if they post disappointing sales, earnings, or guidance. Popular indices like the S&P 500 and the NASDAQ 100 are artificially boosting these fundamentally inferior bubble stocks.

The financial media will likely oscillate between optimism and pessimism throughout 2020. Believe it or not, during Presidential election years, the negative news tends to be light, since most successful candidates have positive messages. Overall, the theme of the current Presidential campaign seems to be "peace and prosperity."

Consumer confidence remains very strong and will be the driving force behind GDP growth in 2020. The upcoming State of the Union speech from our "Cheerleader in Chief" is expected to cite strong retail sales, record low unemployment, the likely return of 3% GDP growth, higher personal income as well as continued peace and prosperity.

Since 2020 is a Presidential election year, the candidates will be promising everything and anything, which in turn, tends to boost both consumer and investor confidence. Domestic issues that impact voters are expected to dominate the Presidential campaign, but President Trump's desire to get out of "endless wars" and his aggressive intervention to squelch terrorists as well as proxy wars will likely be debated. The impeachment circus should be over before the Super Bowl and appears to be primarily a tool for political parties to raise campaign funds.

The "melt up" up that we are witnessing is somewhat seasonal in nature, which is why new pension funding tends to create a "January effect" each year. Furthermore, our fundamentally superior stocks are an oasis amidst the chaos that tends to dominate the news. There is no doubt that 2020 has already commenced with some chaotic news, but the stock market is expected to rotate into our fundamentally superior oasis stocks, so we believe that this year could be one of our strongest years ever!

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