

March 2024

From the front page of today's WSJ:

## **The Stock Market's Magnificent Seven Is Now the Fab Four**

It is a bullish signal that the market is rallying without the likes of Apple and Tesla, some investors say

*By Hardika Singh*

The Magnificent Seven trade is beginning to fizzle—and yet, the stock market is still heading higher.

The S&P 500 climbed 10% in the first quarter, its best start to a year since 2019, even though two of its biggest constituents suffered double-digit declines.

Apple shares fell 11% in the first three months of the year, while Tesla dropped almost 30%. Alphabet shares sputtered for much of the period before making a run in the past three weeks and ending up 8%.

The other four big tech stocks in the group known as the Magnificent Seven - Nvidia, Meta Platforms, Microsoft, Amazon.com - continued their meteoric run and outpaced the broader market. Some market strategists have dubbed them the new Fab Four. ...

All of the S&P 500's sectors, except real estate, logged gains in the first quarter. Small-caps, industrial and financial-services stocks are among those that jumped, fueling bets that the broader market might have more room to run.

Much of the enthusiasm is tied to hopes that the economy has escaped a deep recession and that the Federal Reserve will soon pivot to cutting interest rates, even if not at the pace some investors had previously hoped. A frenzy over the future of artificial intelligence has added to the zeal. ...

The S&P 500's market value has swelled more than \$9 trillion since late October, and the index has set 22 record closes in 2024. ...

Nvidia continues to be a stock-market star. The graphics-chip maker has indicated demand for the computing power that underlies AI remains astronomical. Its shares have jumped more than 80% to start the year, after more than tripling in 2023.

By some metrics, Nvidia has displaced Tesla as the most popular stock among individual investors. It is currently the biggest average holding in individual investors' portfolios, at about 9%, VandaTrack data show.

Meta shares, meanwhile, have soared partly thanks to Meta's investments in artificial intelligence that have made targeted ads smarter. The social-media company recently said it would pay its first shareholder dividend. Microsoft stole the crown of biggest U.S. company from Apple earlier this year, with a valuation that topped \$3 trillion, and Amazon has sharply improved its profitability.

Despite their recent gains, some of the stocks look less pricey than they did last year. Nvidia is trading at 35 times its projected earnings over the next 12 months, below its peak of 62 in May of last year. Amazon's

multiple is 40, down from 2023's high of 62. The S&P 500 is trading at 21 times future earnings, slightly up from last year's highs of 19.

The Fab Four are responsible for nearly half of the S&P 500's first-quarter advance, according to Howard Silverblatt, senior index analyst at S&P Dow Jones Indices. ...

Last year, any hint of weakness in the Magnificent Seven would have sent the broader market tumbling. In fact, for much of the year, those seven stocks were responsible for all of the S&P 500's advance.

This year is a different story. Tesla is struggling on numerous fronts. The electric-vehicle maker is facing pressure from Chinese competitors, which have rapidly expanded their presence around the globe in recent years. It has also warned of notably slower growth in 2024, and its profit margins have taken a hit.

Apple's woes have been mounting, too. The Justice Department recently sued the company, accusing it of monopolistic behavior. European authorities are cracking down on its app store. Plus, it is facing another weak iPhone demand cycle, and investors are worried that Apple is behind in the current wave of excitement around AI.

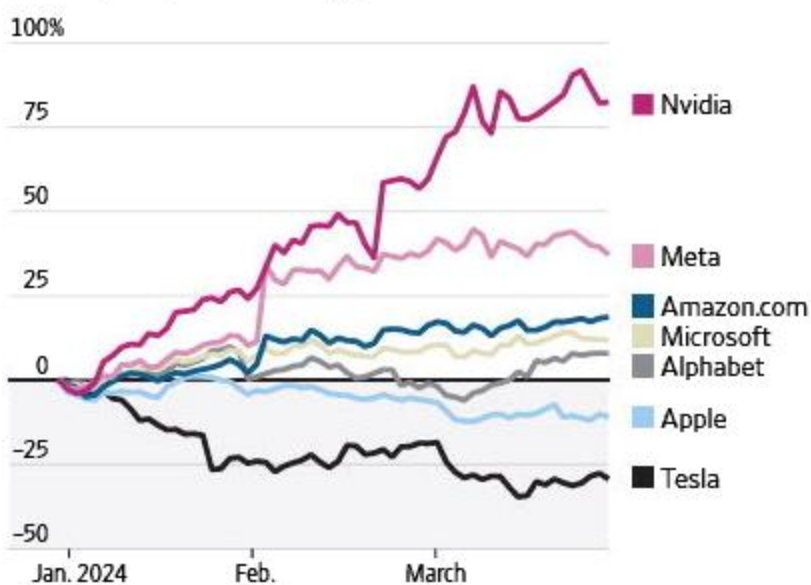
Bespoke Investment Group data show Apple shares underperformed the S&P 500 over the 200 days through Tuesday by the widest margin since October 2013.

From Bespoke last Wednesday:

## One Bad Apple

Can the market rally without Apple? For years you've heard this question asked within broader market conversations. It's been especially the case in more recent years as Apple (AAPL) has been the largest company in the world and at one point last year even accounted for over 7% of the entire S&P 500. Just as the question has been asked, though, the market has answered. Over the last 200 trading days, the S&P 500 is up 21%, and during that time, shares of AAPL have dropped over 6%. As shown below, the 27.2 percentage point performance gap between the two ranks as the widest since October 2013. Looking over even a shorter time frame, over the last 100 trading days, the S&P 500 is up over 24% while AAPL is down fractionally. In the entire period since the iPod was first launched in late 2001, this current period is the first time that the S&P 500 has been up 20% or more over a 100-trading day period while AAPL was down.

Share-price performance, year to date



\*First quarter 2024 data are estimates and the rest are projections.  
Source: FactSet (performance); John Butters, senior earnings analyst at FactSet (earnings growth)

## Apple (AAPL) vs S&P 500 200-Day Performance Spread: 1999 - 2024



We are concerned about the level of speculation in the market, as exemplified by the frenzy over AI, and Bitcoin. This is not going to end well for those participating. However, Momentum is a Factor we are well aware of, and invest in for clients focused on Capital Appreciation, Funds only. Two of our favorite quotes:

**“I think the reason why we got into such idiocy in investment management is best illustrated by a story that I tell about the guy who sold fishing tackle. I asked him, “My God, they’re purple and green. Do fish really take these lures?” And he said, “Mister, I don’t sell to fish.” - Charlie Munger**

**"But as long as the music is playing, you’ve got to get up and dance. We’re still dancing.” - Charles Prince, CEO Citigroup, July 9, 2007**

From Bespoke last Thursday:

### Five Straight

Barring a 2% sell-off in the final hour of trading today, the S&P 500 will end March with a gain of more than 1%, making it the 5th straight month with 1%+ gains. Since WW2, there have only been twelve prior five-month streaks like this, and they're shown in the table below. Next to each occurrence, we show how the S&P did in the months and year following. As shown, the month after these five-month winning streaks has been hit or miss. We've actually seen declines in the next month four out of the last five times this has happened. But maybe more notable is that one year after these prior twelve occurrences, the S&P was higher all twelve times with an average gain of 14.3%.

Of course, past performance is no guarantee of future results, but we think market historicals are a good way to stay grounded during market run-ups and pullbacks. ...

## S&P 500 Streaks of 5 Months With 1%+ Gains: 1945 - 2024

5th 1% Month	5 Month Gain (%)	S&P 500 Performance (%)			
		One Month	Three Months	Six Months	One Year
7/31/58	15.55	1.19	8.77	17.44	28.23
3/31/61	22.36	-0.03	-1.06	2.14	6.46
5/31/75	32.95	4.43	-4.68	0.10	9.91
2/28/83	22.95	3.31	9.68	11.04	6.08
3/31/91	23.43	0.03	-1.08	3.37	7.59
4/30/95	13.45	3.63	9.20	12.98	27.09
3/31/98	20.46	0.91	2.91	-7.69	16.76
1/31/99	33.67	-3.23	4.34	3.84	8.97
8/31/03	18.84	-1.19	4.98	13.58	9.55
12/31/06	11.09	1.41	0.18	6.00	3.53
5/31/13	14.34	-1.50	0.14	10.74	17.96
8/31/20	35.43	-3.92	3.47	8.88	29.21
3/31/24	25.15				
<b>Average</b>		<b>0.42</b>	<b>3.07</b>	<b>6.87</b>	<b>14.28</b>
<b>Median</b>		<b>0.47</b>	<b>3.19</b>	<b>7.44</b>	<b>9.73</b>
<b>% Positive</b>		<b>58.3</b>	<b>75.0</b>	<b>91.7</b>	<b>100.0</b>
<b>All Periods Since 1945</b>					
<b>Average</b>		<b>0.72</b>	<b>2.15</b>	<b>4.33</b>	<b>8.77</b>
<b>% Positive</b>		<b>60.2</b>	<b>65.3</b>	<b>69.1</b>	<b>72.7</b>

As for the reason we don't short, another favorite quote:

“The market can remain irrational longer than you can remain solvent” - John Maynard Keynes

From Bloomberg's Evening Briefing last Tuesday:

**Short sellers** are still betting billions of dollars that the rally of cryptocurrency-linked stocks, fueled by a surge in Bitcoin, will end. Total short interest has increased to almost \$11 billion this year, and more than 80% of it is bets against MicroStrategy and Coinbase Global. Paper losses for the shorts meanwhile have mounted to almost \$6 billion. Still, they are doubling down, betting on a crypto collapse.

From Global Investment Strategy last Monday:

## Second Quarter 2024 Strategy Outlook: Balancing Act

### I. Macroeconomic Outlook

#### Why Low Unemployment Is BAD For Stocks

One might think that stocks fare best when unemployment is low. **Chart 1** challenges that assumption. It shows that the S&P 500 has consistently produced better returns when the unemployment rate is high rather than low. How can one explain this curious finding? One reason is that equity valuations tend to become stretched when

times are good and unemployment is low. But a more ominous reason is that the unemployment rate is a highly mean-reverting series: When it gets down to very low levels, it usually starts rising again (**Chart 2**).

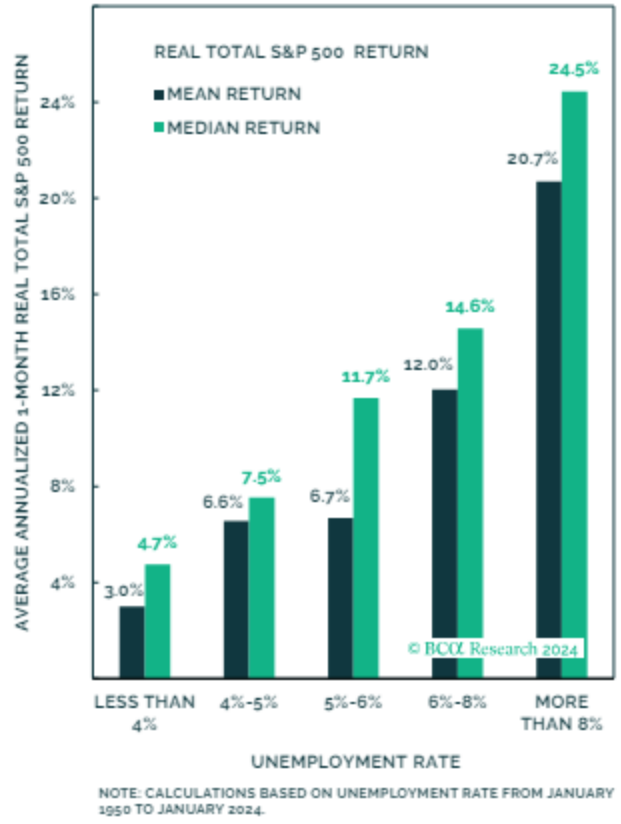
Why can't the unemployment rate go down and stay down? The answer is ... that inflation becomes more sensitive to changes in economic slack when the economy approaches full employment. Such a nonlinear relationship between inflation and unemployment was evident during the late 1960s and reappeared again during the pandemic. ...

When many people are unemployed, firms can hire more workers without having to offer them substantially higher wages. In contrast, when everyone who wants a job has a job, the only way that firms can hire more workers is by poaching them from other firms. To do so, they need to offer higher wages, which puts upward pressure on inflation. ...

### On A Knife-Edge

... On the one hand, if demand reaccelerates, inflation will rise, forcing the central bank to hike rates. On the other hand, if demand decelerates, unemployment will start increasing. Since one person's income is another person's spending, rising unemployment tends to feed on itself.

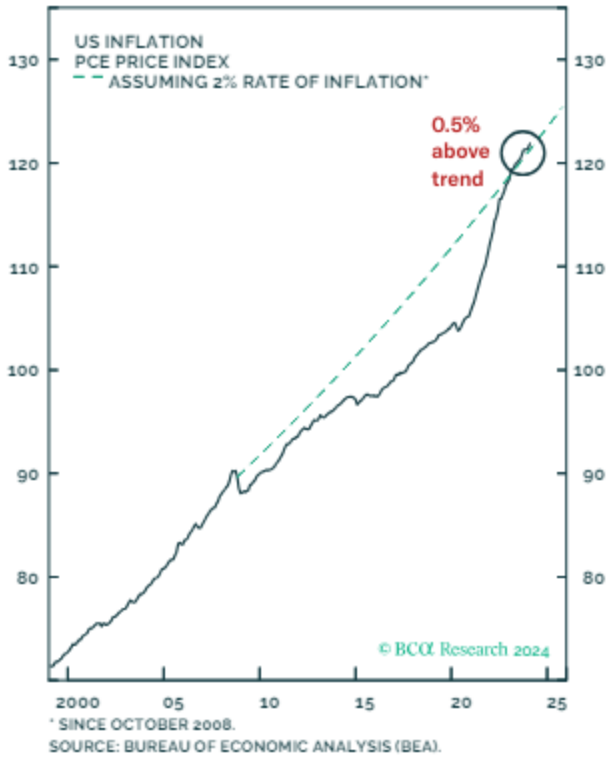
**CHART 1**  
**Stocks Do Best When Unemployment Is High, Not Low**



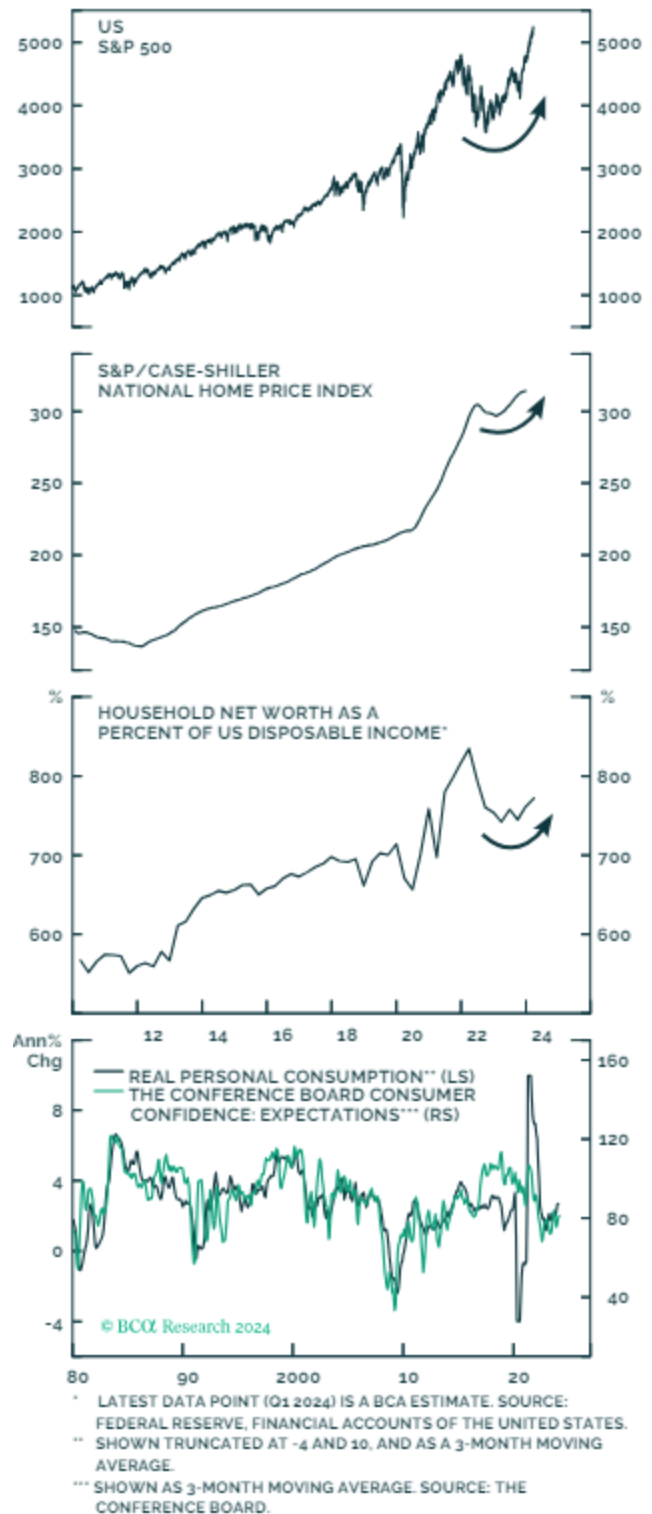
**CHART 2**  
**The Unemployment Rate Is A Highly Mean-Reverting Series**



**CHART 5**  
**The Fed Has Used Its “Get Out Of Jail Free” Card**



**CHART 10**  
**Some Tailwinds For US Households**



Ironically, it is much easier to conduct monetary policy when unemployment is elevated. When there are many jobless workers, the central bank can simply keep interest rates below their neutral level, allowing the economy to grow at an above-trend pace. ...

This highlights an important point: The wave of inflation that the US experienced over the past three years cannot be safely repeated.

As **Chart 5** highlights, the current level of the PCE deflator is back to where it would have been had inflation averaged 2% since the Global Financial Crisis. In other words, the Fed received one free “get out of jail” card by virtue of having undershot its inflation target following the GFC.

That card has now been played, which means the Fed has to tread carefully to ensure that inflation does not start rising again. ...

**Fire or Ice?**

Is the US economy destined to overheat or freeze over? It is a tough call, but we would say that there is a 20% probability the economy overheats, a 70% probability it freezes over, and just a 10% probability that it threads the needle and achieves a true soft landing or "Goldilocks" outcome.

The case for fire is buttressed by the fact that financial conditions have eased significantly since last October. ... this is imparting a positive impulse to aggregate demand.

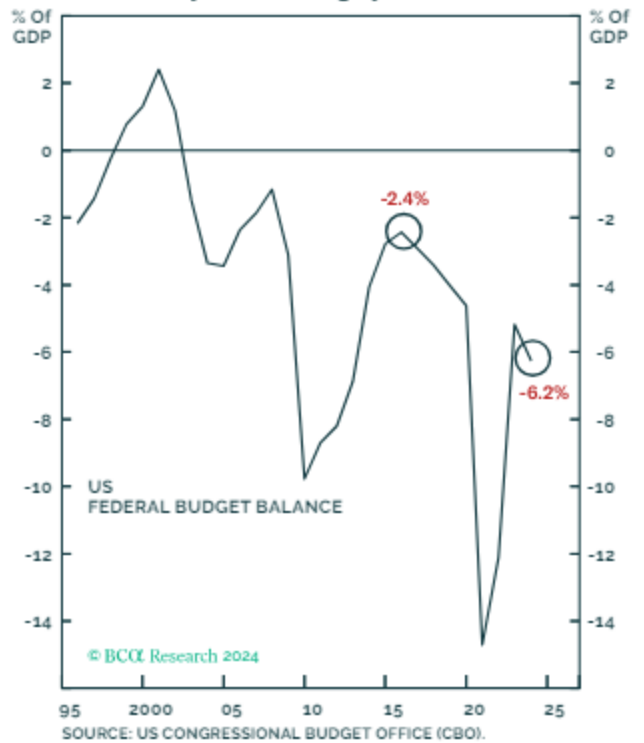
Thanks to the recovery in both equity and real estate prices, household wealth is rising at a solid pace (**Chart 10**). This is lifting consumer confidence and consumption.

Fiscal policy remains highly stimulative. The Congressional Budget Office estimates that the federal budget deficit reached 6.2% of GDP in 2023. In 2015, prior to the Trump tax cuts, the budget deficit stood at only 2.4% of GDP (**Chart 11**).

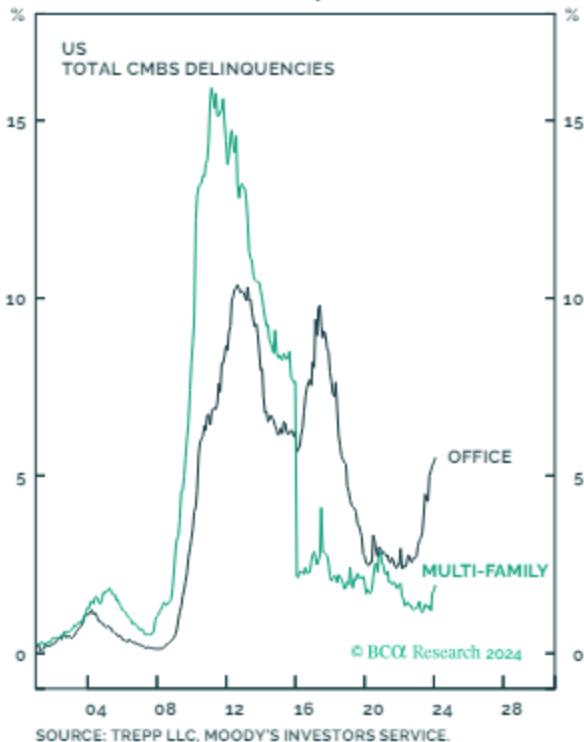
Manufacturing activity is showing signs of stabilization. Capex intentions have perked up. Manufacturing construction is booming, especially in the tech sector.

On the inflation front, both the CPI and PPI surprised on the upside in February, continuing the string of generally hotter-than-expected readings seen in January. More refined measures of inflation such as trimmed-mean, median, sticky price, and the New York Fed's Multivariate core PCE have all moved off their lows.

**CHART 11**  
**Fiscal Policy Remains Highly Stimulative**



**CHART 17**  
**Will Multi-Family Commercial Real Estate Be The Next Shoe To Drop?**



**CHART 18**  
**Oversupply In Multi-Family Housing During The Pandemic Is Suppressing Rent Growth**

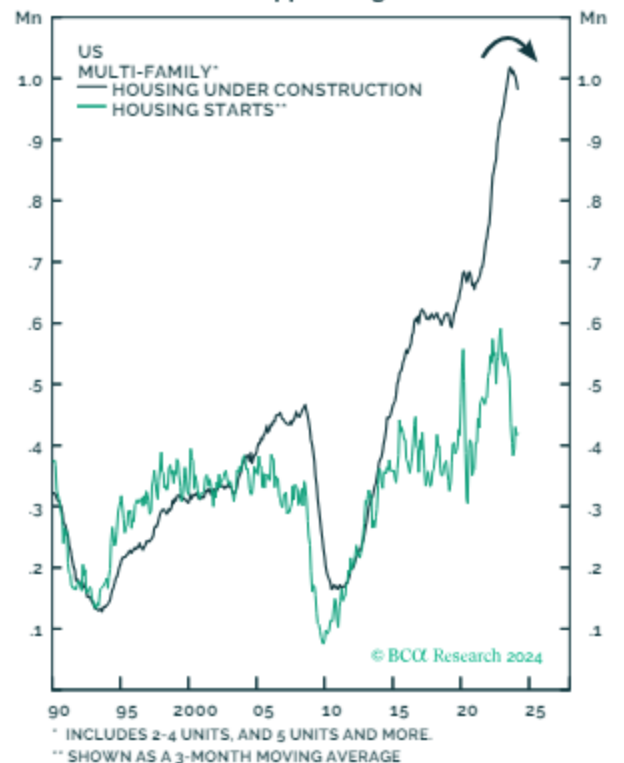


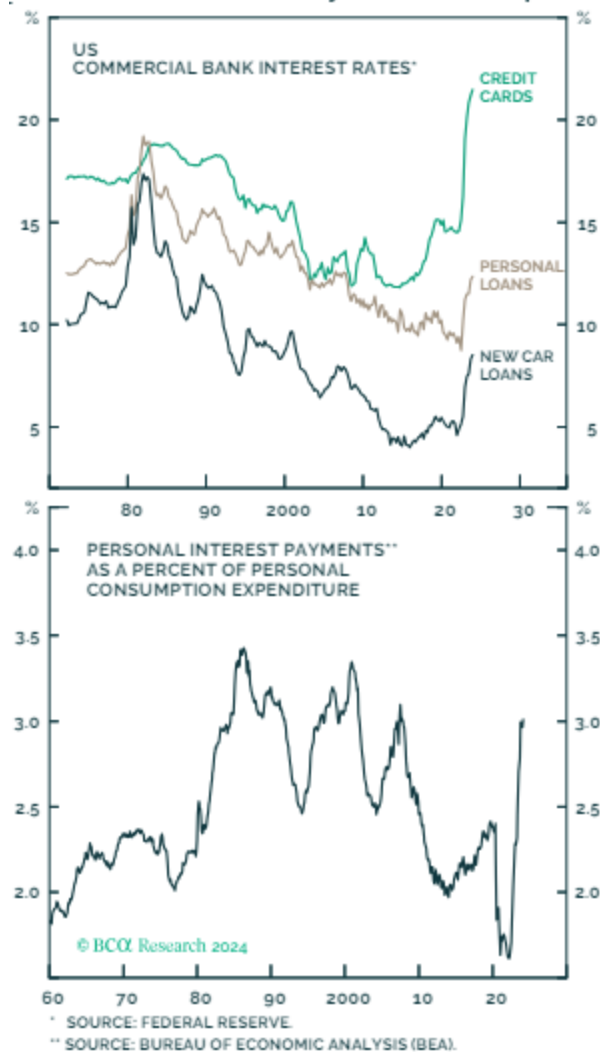
CHART 19

**Consumer Loan Delinquencies Have Risen**



CHART 20

**Credit Card Interest Rates Are At Record Highs And Personal Interest Payments Have Jumped**



**Cold Comfort**

What about the case for ice? Here one could point to wage growth, which has continued to soften. Leading indicators such as job openings, the quits rate, advertised wages, and most business surveys of labor availability all suggest that wage growth will decelerate further.

Firms usually stop hiring before they start firing. Consistent with a softening labor market, the hiring rate is at a six-year low. Firms also tend to let go of temporary workers before they shed permanent staff. This makes temp employment a useful leading indicator for recessions. Temp employment is back to where it was in 2010.

Supporting the case that the economy is cooling down, bank lending has slowed, the broad money supply is shrinking, and corporate bankruptcies are rising.

Commercial real estate remains under pressure. Delinquency rates have risen sharply in the office sector (**Chart 17**). They will rise in the apartment sector, too. The number of apartments under construction surged during the pandemic (**Chart 18**). The resulting wave of supply is hitting the market now, which is suppressing rent growth and causing developers to initiate fewer new projects.

**Consumer Delinquencies Rising**

In the consumer realm, both credit card and auto loan delinquencies have climbed to their highest level since 2012, an ominous development considering that the unemployment rate was over 8% back then (**Chart 19**).

The average credit card interest rate stands at 21%, the highest in history. As a percent of consumption, personal interest payments have jumped 1.4 percentage points from their lows (**Chart 20**). Credit card balances rose by



CHART 22

**First-Time Home Buyers Are Feeling The Pinch**



15% in Q4 2023 relative to the same quarter a year earlier. With the Fed’s Survey of Senior Loan Officers indicating that banks have become significantly less willing to extend consumer credit, credit card spending growth will slow.

Recent home buyers, confronted with the double whammy of high home prices and mortgage rates, are feeling the pinch most severely. For them, mortgage payments now account for 40% of their incomes – the highest percentage in four decades (**Chart 22**).

Meanwhile, the accumulated pandemic savings that helped power consumption growth over the past three years have largely been depleted. This is especially true for poorer households. In real terms, the value of bank deposits and money market funds held by the bottom 20% of income earners is 19% below 2019 levels (**Chart 23**).

**The Paradox of Thrift**

In January, the personal savings rate stood at 3.8% – half of what it was in 2019 (**Chart 24**). Having run down their pandemic reserves and unable to rack up ever-higher credit card balances, US households will have no choice but to tighten their belts.

It will be difficult for the savings rate to normalize without triggering a recession. If consumers collectively try to spend less and save more, employment and income will drop. In fact, overall income could drop so much that aggregate savings end up falling – a phenomenon John Maynard Keynes called the “paradox of thrift.” Such a perverse outcome occurred during the Great Depression (**Chart 25**).

CHART 23

**Excess Savings Have Become Depleted, Especially Among The Poorest Households**

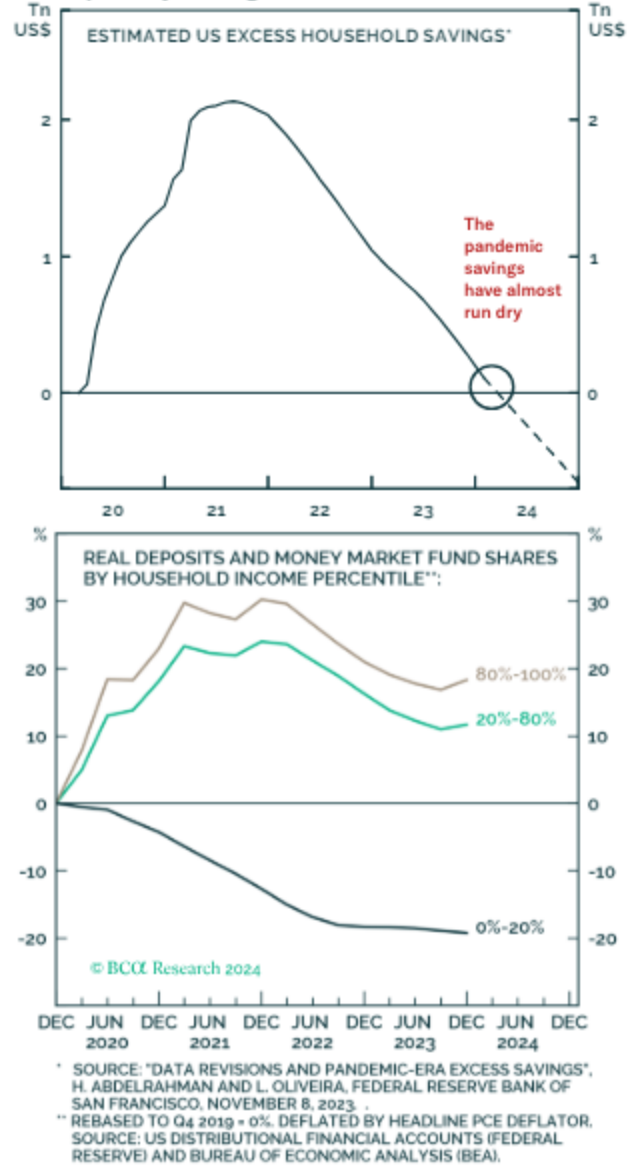
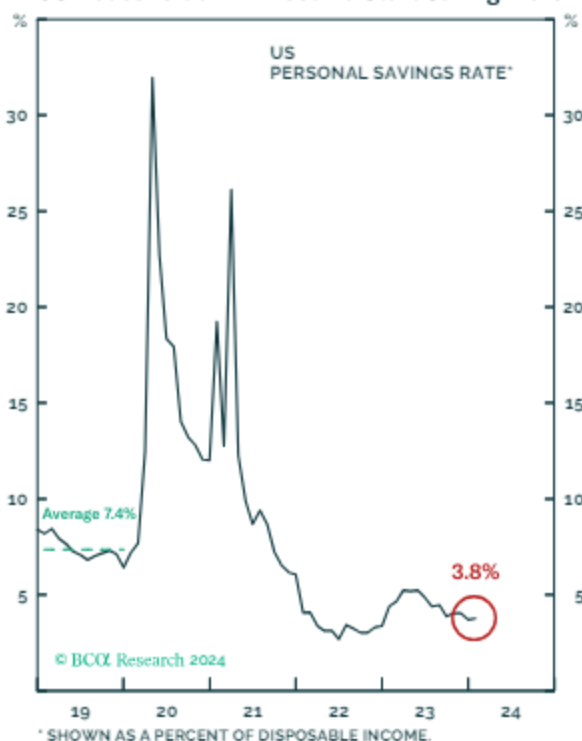


CHART 24  
**US Households Will Need To Start Saving More**



To be clear, we are not predicting another depression. Among other things, monetary and fiscal policy will be much more responsive than they were in the 1930s. But an increase in the unemployment rate to about 6% – similar to what happened during the relatively mild 2001 recession – is probable.

The bottom line is that the temperature of the US economy is falling. While a reheating is still possible, a more likely outcome is that the economy will freeze over, probably towards the end of this year or in early 2025 when job openings have declined to the point that workers who lose their jobs will struggle to find new ones.

### Europe: False Dawn?

The euro area barely skirted a recession in 2023. Real GDP was unchanged in Q4 quarter-over-quarter and was up only 0.1% year-over-year. Germany was the standout laggard. German GDP shrank by 0.2% year-over-year in Q4 2023, whereas French GDP rose 0.7% and GDP in Italy and Spain increased by 0.6% and 2%, respectively.

Euro area growth should perk up a bit over the next few quarters as the global manufacturing cycle stabilizes. Korean exports tend to lead the euro area manufacturing PMI. They have risen in recent months. The new orders-to-inventory component of the Swedish manufacturing PMI also tends to lead the euro area one. It has moved back above zero

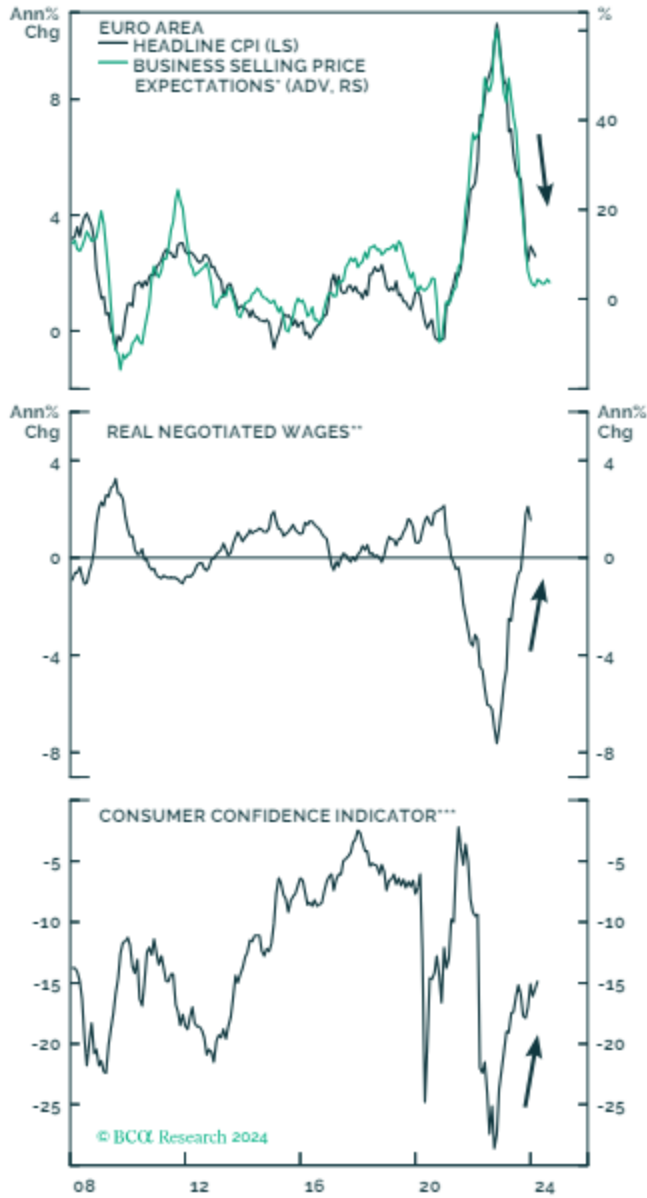
While euro area inflation surprised on the upside in February, it remains well off its highs. Falling inflation has allowed real wages to start growing again, which has bolstered consumer confidence (**Chart 27**).

CHART 25  
**The Paradox Of Thrift: The Case Of The Great Depression**



CHART 27

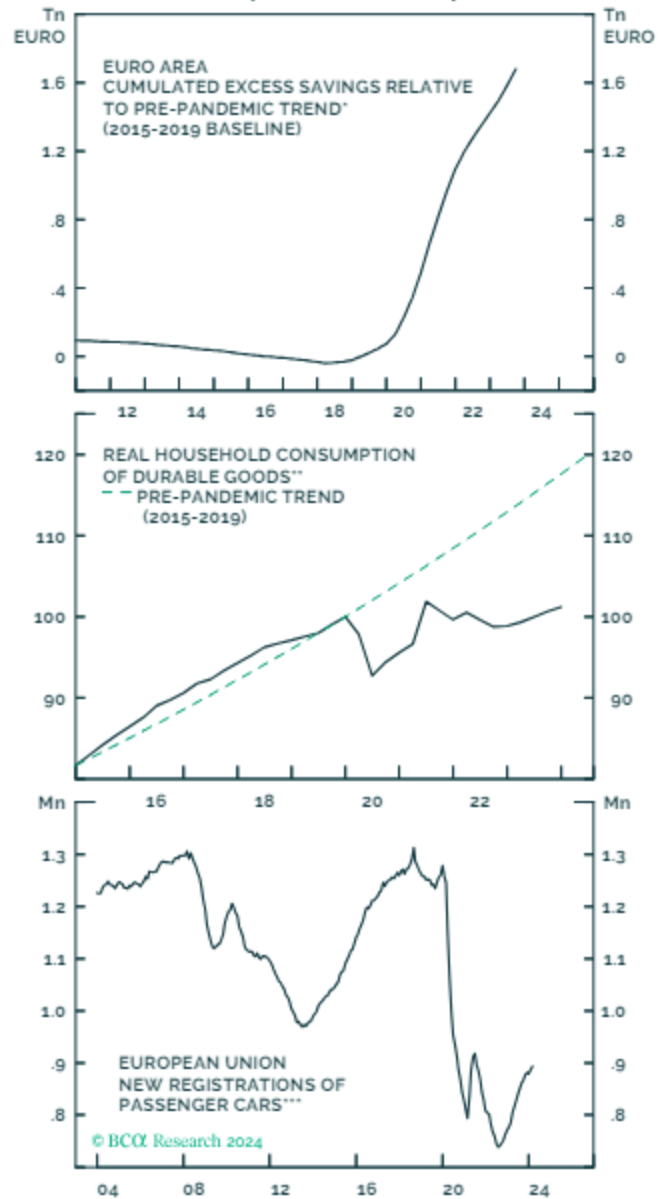
**Falling Inflation In Europe Has Lifted Real Wages And Consumer Confidence**



\* SHOWN ADVANCED BY 6 MONTHS. SOURCE: EUROPEAN COMMISSION SURVEY.  
 \*\* DEFLATED BY HEADLINE CPI.  
 \*\*\* SOURCE: DIRECTORATE GENERAL FOR ECONOMIC AND FINANCIAL AFFAIRS (DG ECFIN).

CHART 28

**A Lot Of Pent-Up Demand In Europe**



\* BASED ON BCA CALCULATIONS.  
 \*\* INCLUDES GERMANY, FRANCE, ITALY, SPAIN, AND THE NETHERLANDS. REBASED TO Q4 2019 = 100.  
 \*\*\* SHOWN AS A 12-MONTH MOVING AVERAGE. SOURCE: EUROPEAN AUTOMOBILE MANUFACTURERS' ASSOCIATION.

Unlike in the US, European households are still clinging to a significant amount of excess pandemic savings. There is also a lot of pent-up demand for consumer durable goods. Vehicle registrations, for example, are still 30% below 2019 levels (**Chart 28**).

**No Fiscal Offset to the Looming Credit Squeeze**

Despite these positive developments, significant risks remain. The ECB's latest Bank Lending Survey showed that banks continued to tighten lending standards in Q4 2023, albeit at a more gradual pace than in prior quarters. The money supply is shrinking while the credit impulse remains deep in negative territory.

The ECB reckons that 30% of household loans will reset to higher rates within the next 12 months. In Spain and Italy, more than two-thirds of loans will be repriced. As a result, the interest burden of households will increase meaningfully.

European fiscal policy is set to become more restrictive. The IMF estimates that the euro area will face a negative fiscal thrust of 1% of GDP in 2024. In Germany, where the Constitutional Court has blocked the spending of residual pandemic funds, the fiscal thrust will be negative 1.4% of GDP.

### **European Labor Markets Holding Up... For Now**

So far, European labor markets have held up reasonably well. Despite barely any growth in GDP, employment in the euro area rose by nearly 0.6% in 2023 while the unemployment rate ticked down from 6.6% in January 2023 to 6.4% in January 2024.

Beneath the surface, however, there are signs that labor demand is weakening. According to Eurostat, the job vacancy rate fell from 3.1% in Q4 2022 to 2.7% in Q4 2023. More timely data from Indeed, a large job postings site, suggests that job openings have continued to decline across much of the euro area this year. In the UK, the Office for National Statistics estimates that job openings dropped to 908,000 in the three months ending February 2024, down 30% from their mid-2022 peak.

Just as in the US, our guess is that the European labor market will finally crack towards the end of this year, pushing the region into recession.

### **China: Structural Headwinds**

China's economy grew by 5.2% in 2023, surpassing the government's target of 5%. For 2024, the authorities are once again targeting growth of "about 5%."

Meeting this year's target will not be easy. Last year, the economy was buoyed by the lifting of Covid restrictions in January 2023. That tailwind has now faded.

A stabilization in global manufacturing activity in 2024 should help matters. Notably, China's production of smartphones has bounced off its lows. Exports of electric vehicles have soared, allowing China to surpass both Europe and Japan to become the world's top automotive exporter.

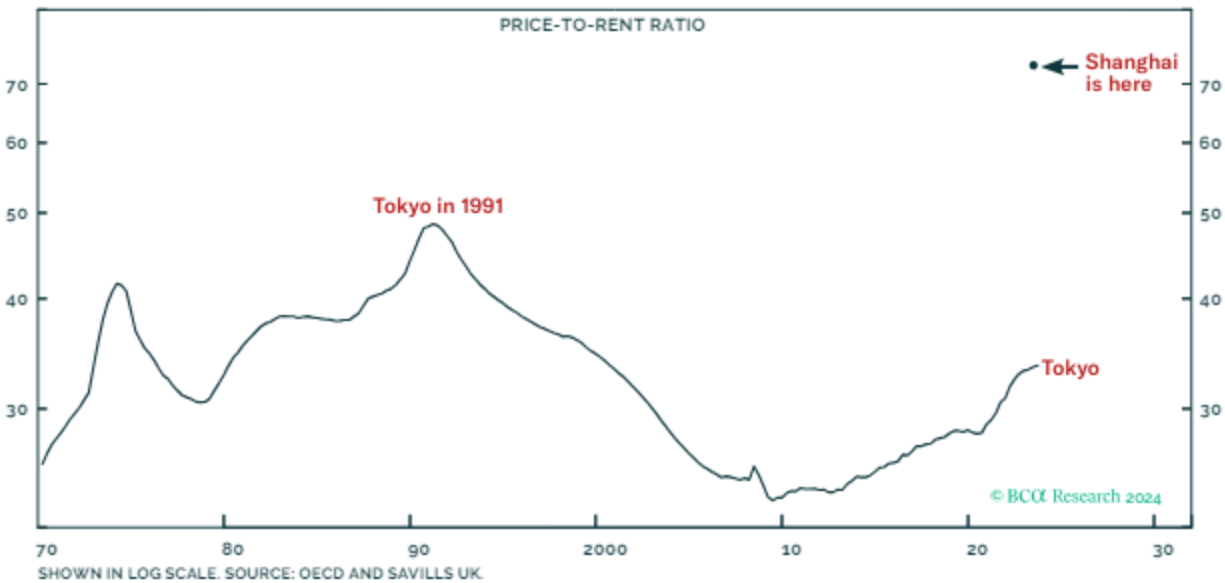
The risk for China is that the rebound in manufacturing exports will be undercut by the ongoing geopolitical rift between itself and some of its trading partners. This is especially the case if Donald Trump, who now leads Joe Biden in opinion polls, wins the presidency in November.

### **Housing Blues**

Meanwhile, China's housing market continues to weaken. Housing starts, as proxied by the amount of building floor space started, have plunged by 61% since March 2021. Home sales are down 47% from their highs.

Officially, new home prices are only 3% below their peak. However, this is simply because the authorities maintain tight controls over new home transactions. On the secondary market, existing home prices are down 9% from their peak and by over 20% in some cities. And they have much further to fall. Due to government efforts to support developers in finishing previously stalled projects, housing completions rose in 2023 (Chart 34).

CHART 35  
**China's Housing Bubble Is Arguably Even Worse Than Japan's Was**



The fact that Chinese homes are still more expensive relative to rents than were Japanese homes in the early 1990s is not helping matters (**Chart 35**). Neither does the fact that the demand for Chinese housing is set to shrink over the coming decades. Back in 2019, the UN estimated that the Chinese working-age population would contract by 40% over the remainder of the century. Its latest estimate, published in 2022, foresees a 60% drop (**Chart 36**). And even that may be optimistic given that the birth rate fell further in 2023.

China's Brewing Deflation Problem Against the backdrop of sluggish growth and a deteriorating property market, deflationary forces are setting in. The GDP deflator contracted by 1% in Q4 2023. Export prices are down 11% from their highs. The average monthly salary for newly hired workers has been shrinking since mid-2023.

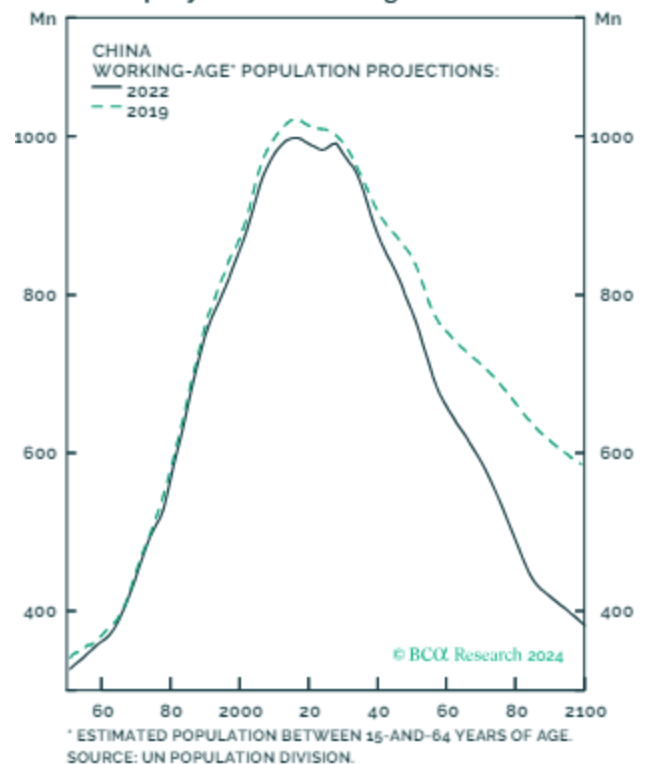
While inflation did accelerate in February, this was mainly due to the timing of the Lunar New Year (for example, tourism price inflation jumped from 1.8% year-over-year in January to 23.1% in February). The producer price index declined by a greater-than-expected 2.7% year-over-year in February.

Falling prices are putting upward pressure on real interest rates. Whereas commercial bank lending rates are at record lows in nominal terms, they are near multi-decade highs in real terms. Reflecting these developments, total social financing flows came in well below consensus expectations in February

### No Irrigation-Style Fiscal Stimulus

On the fiscal front, the government has moved cautiously to loosen fiscal policy while eschewing the irrigation-style stimulus programs of the past. In an incremental move, the

CHART 36  
**China's Working-Age Population Is Set To Fall Rapidly Over The Coming Decades**



authorities announced earlier this month that they will issue RMB 1 trillion in “ultra-long” Treasury bonds (typically with tenors exceeding 30 years). The issuance of these bonds will not count against the government’s official on-budget deficit target of 3% of GDP. They have also authorized RMB 3.9 trillion in local government special bond issuance, up from RMB 3.8 trillion in 2023.

The risk is that these allocated funds will not be fully spent. In 2023, overall government spending fell short of the budget target by RMB 1.7 trillion. As a result, the fiscal spending impulse ended up being 0.4% of GDP, well below the 1.7% of GDP based on the 2023 budget.

Spending came in below target in 2023 mainly because land sales – which account for 20% of local government spending – declined by 13%. The fact that Beijing is optimistically assuming that local government land sales will be flat in 2024 raises the risk that spending will again fall short of target.

Taking all these considerations on board, Arthur Budaghyan, BCA’s Chief Emerging Markets Strategist, expects the combined credit and aggregate fiscal spending impulse to reach 5% of GDP in his baseline scenario. This is considerably less than the magnitude of the impulse achieved during the 2009, 2012-13, 2016, and 2020 stimulus episodes.

## II. Financial Markets

### A. Global Asset Allocation

#### The Party Is Winding Down

This publication continues to zig while others zag. Going into 2023, most professional forecasters expected the US to be in a recession by now (**Chart 41**). In contrast, we wrote in December 2022 that “growth will surprise to the upside in 2023” while “inflation will come down rapidly.” ...

As we noted at the time, ... a recession would start just when inflation was closer to target, unemployment was still low, and most everyone was convinced that a soft landing had been achieved.

After staying in the bullish camp for all of 2023, we shifted our equity recommendation to neutral at the start of this year. We expect to move our equity recommendation to underweight later this year. ...

### B. Equities

#### Blow-Off Rally Possible, But Downside Risks Are Growing

CHART 41  
Going Into Last Year, A US Recession Was Widely Expected... But It Has Not Materialized So Far

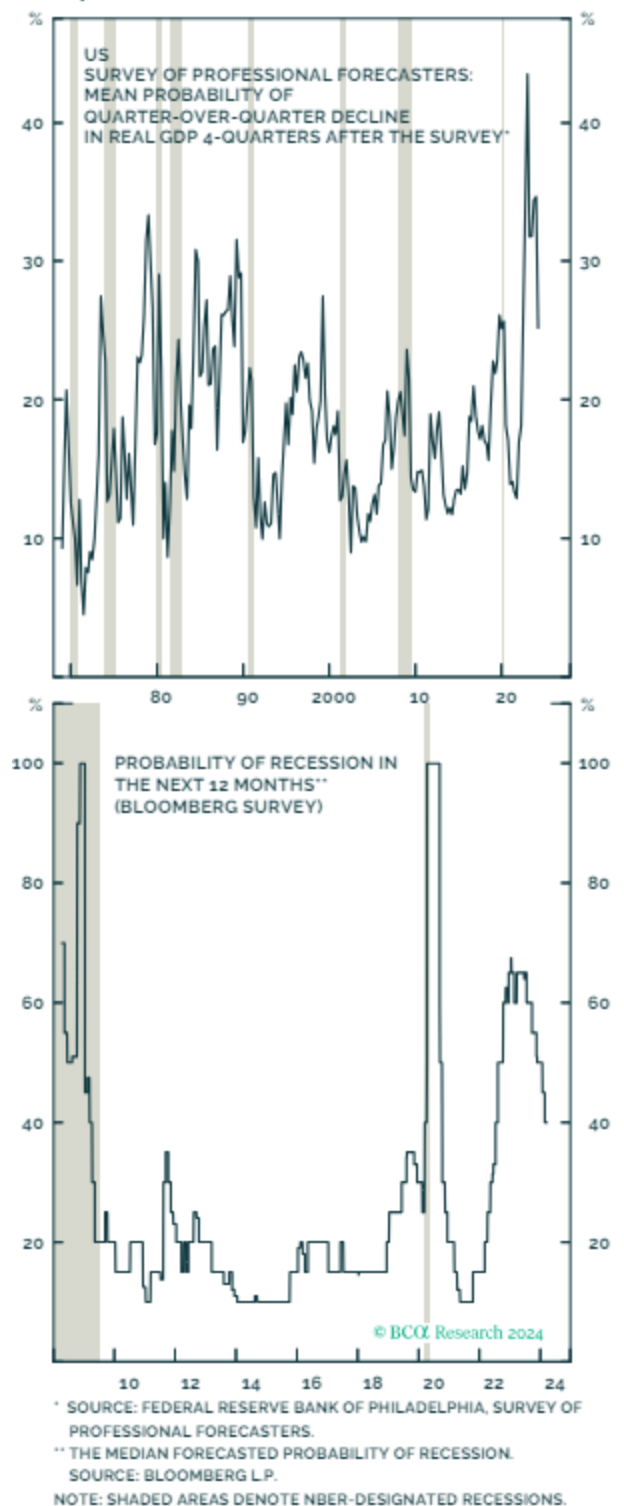


TABLE 1  
**On Average, Stocks Have Peaked Six Months Before The Onset Of A Recession**

RECESSIONS	S&P 500 PEAK* (MONTHS)	S&P 500 TROUGH* (MONTHS)	PEAK-TO-TROUGH DECLINE (%)
DEC '69 - NOV '70	-13	+6	-36%
NOV '73 - MAR '75	-11	+10	-48%
JAN '80 - JUL '80	0	+2	-17%
JUL '81 - NOV '82	-8	+12	-27%
JUL'90 - MAR '91	-2	+3	-20%
MAR '01 - NOV '01	-7	+18	-49%
DEC '07 - JUN '09	-2	+14	-57%
<b>AVERAGE</b>	<b>-6</b>	<b>+10</b>	<b>-36%</b>

\* RELATIVE TO THE START OF NBER-DESIGNATED RECESSIONS.

On average, the S&P 500 has peaked six months before the start of a recession (**Table 1**). If the next recession begins towards the end of this year or in early 2025, this provides a short window for equities to move higher. ...

### How Much Downside?

Our base case is that the S&P 500 will fall to as low as 3600 during the next recession. Such a price target may seem very pessimistic, but it is built on only two assumptions, both of which are quite reasonable, in our view.

The first assumption is that the forward P/E ratio troughs at 16 (it is currently 21). That is not especially onerous given that the average forward P/E multiple between 2012 and 2019 was 15.8 – a period that did not even encompass a recession.

The second assumption is that forward earnings estimates fall by 10% from current levels. Again, this is not a terribly onerous assumption. As **Chart 43** shows, earnings estimates have typically declined by more than 10% during recessions. For example, in the 2001 recession – one of the mildest on record – earnings estimates fell by 18%.

The downward risk to earnings is amplified by the fact that profit margins remain quite elevated. Our measure of forward profit margins – calculated by dividing forward price-to-earnings by forward price-to-sales – stands at 12.9%, well above the average of 10.9% between 2012 and 2019.

### Magnificent 7 to the Rescue? Don't Count On It

CHART 43  
**Even A Mild Recession Could Lead To A Meaningful Decline In The S&P 500**

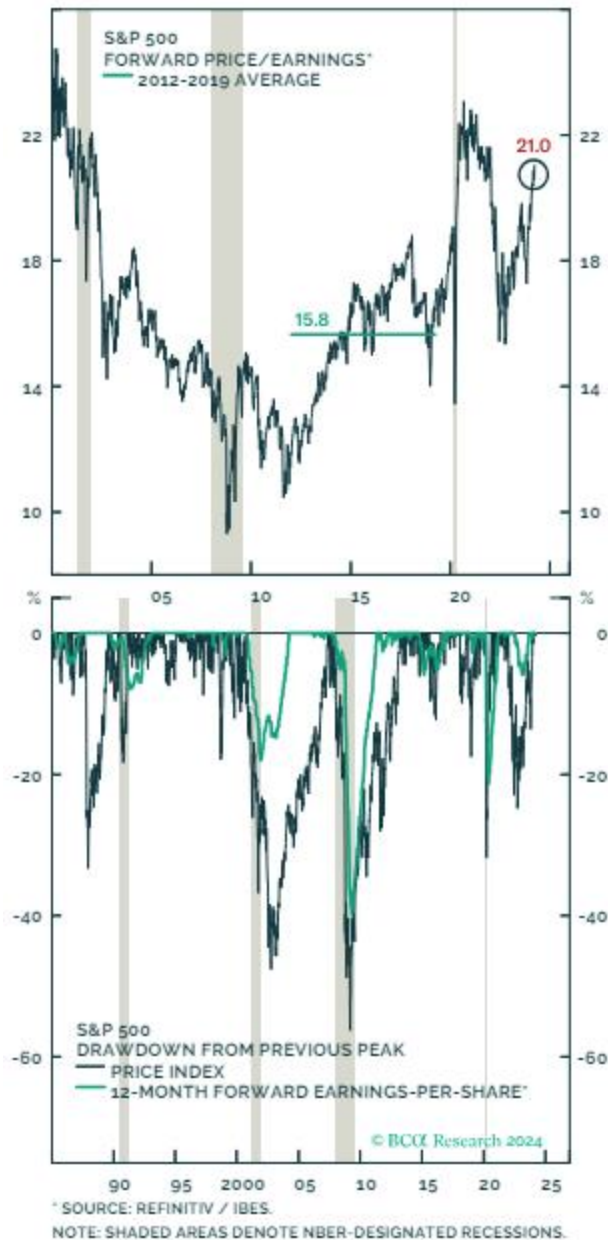


CHART 45  
Cheap For A Reason



One might argue that today's high valuations are justified by the dominance of tech stocks in the S&P 500. There is certainly some truth to that claim .... While it is true that the S&P 500 would trade at only 18.8-times forward earnings if Alphabet, Amazon, Apple, Meta, Microsoft, and Nvidia were excluded from the index, it is equally true that the remaining 494 stocks saw earnings contract by 1.3% year-over-year in Q4 2023 (Chart 45). So, they are cheaper, but cheaper for a reason.

In any case, it is far from obvious that these so-called magnificent stocks will stay magnificent. Already, people are talking about the Magnificent 6 (or 4 as headlined in the WSJ today) instead of the Magnificent 7 because Tesla has been the worst performing stock in the S&P 500 so far this year. History is littered with companies such as RCA, Kodak, Polaroid, Atari, Commodore, Novell, Digital, Sinclair, Wang, Iomega, Corel, Netscape, Altavista, AOL, Compaq, Sun, Lucent, 3Com, and RIM that were once major players in the tech sector, only to fade into oblivion.

CHART 46  
Will Nvidia Follow In Cisco's Footsteps?



NOTE: VERTICAL LINE DENOTES THE PEAK IN CISCO SHARE PRICE (MARCH 27, 2000). NEGATIVE P/E VALUES BETWEEN 2001 AND 2002 AND ABNORMALITIES IN EARNINGS DUE TO EXTRAORDINARY TAX CHARGE IN 2018 ARE OMITTED.



Even if Nvidia avoids the fate of these companies, that does not make it a good investment at current valuations. Consider, for example, the case of Cisco. In 2000, Cisco traded at 37-times sales, making it the most valuable listed company in the world (**Chart 46**). Since then, Cisco's earnings-per-share have increased nearly tenfold, with sales-per-share rising almost as much. Yet, the stock remains 38% below its 2000 highs.

Nvidia shareholders should take notice. Today, as it happens, Nvidia also trades at 37-times sales. Will Nvidia share Cisco's fate? Our guess is yes. The lesson is clear: A good company may not turn out to be a good stock.

### **Sector Strategy: Cozying Up to Defensives**

In the investment world, timing is everything. While we are skeptical that today's mega cap tech stocks will deliver outsized returns over the long haul, for now, they continue to benefit from the halo effect of AI euphoria. ...

Notably, we have a more favorable view of consumer staples, utilities, and especially, health care. While earnings momentum in the health care sector has been weak, the earnings picture should improve over the next few years as prices reset to a higher level (health care prices are often subject to long-term contracts, and hence, are not adjusted as often as prices in the rest of the economy). Health care stocks are also relatively cheap and will benefit from the long-term secular tailwind of an aging population.

### **US Equities Will Outperform During the Next Recession, But Not By Much**

... we are overweight the US ... over a 6-to-12 month horizon within a broad equity portfolio. US stocks have delivered much faster earnings-per-share growth over the past 16 years and nothing in the recent data suggests that trend has changed (**Chart 47**).

... we are neutral on the euro area and emerging markets, although we expect to downgrade both regions later this year in advance of the global economic downturn. ...

US stocks typically outperform their overseas peers during global recessions, both because the US dollar tends to appreciate when global growth is weakening (which boosts the value of US stocks in common-currency terms), and also because non-US stocks tend to be somewhat more cyclical.

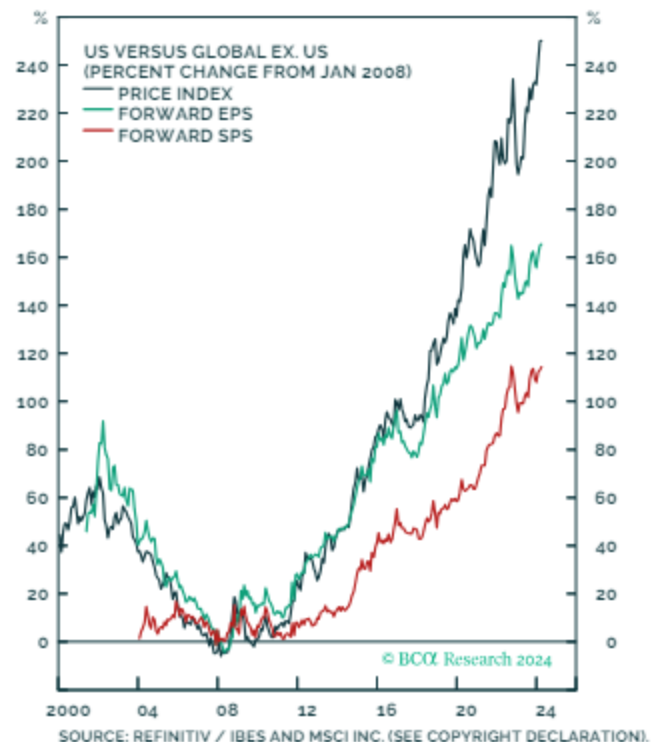
That said, we do not expect US stocks to outperform their global peers by very much. The main reason is that US stocks are relatively expensive. In particular, high-flying US tech stocks are vulnerable to re-rating in an environment of increased risk aversion. ...

### ***C. Fixed Income***

#### **The New Normal, Same As The Old Normal**

Back in June 2019, we wrote: *"Fed policy is likely to proceed in two stages: An initial stage characterized by a highly accommodative monetary policy, followed by a second stage where the Fed is raising rates aggressively in*

**CHART 47**  
**Superior Earnings Growth Has Powered US Equity Outperformance**



*response to galloping inflation. The first stage, which will end in late 2021, will be heaven for risk assets. The subsequent stage, which will feature a global recession, will be hell. In the end, we expect the fed funds rate to reach 4.75%, representing thirteen more 25-basis point hikes than implied by current market pricing.”*

Needless to say, we did not foresee the tidal wave of fiscal deficits that the pandemic would unleash. But even in 2019, it was clear to us that the narrative of secular stagnation that Larry Summers championed, or the notion of a “new normal” that Bill Gross espoused, was flawed. There was no “new normal” following the Global Financial Crisis.

There was a “new abnormal,” a period of exceptionally high unemployment, intense household deleveraging, and subdued homebuilding.

By 2019, all of that had changed. The unemployment rate had fallen back below 4%, the deleveraging cycle had ended, and the housing market had become characterized by a shortage of homes rather than a glut of homes. In short, it was clear that interest rates would eventually need to rise, and by mid-2023 they had.

### **Structural Forces Will Prop Up Yields...**

Will bond yields drop from current levels? Over a 5-to-10 year horizon, we think not. Structurally, many forces will support yields. These include rising populism, ebbing globalization, and the green transition, which will require trillions in new spending.

In addition, baby boomers are leaving the labor market en masse. While they were working, they accumulated a lot of assets. In the US, baby boomers hold more than half of all household wealth (**Chart 49**). Now, rather than working and saving, they are spending down their wealth. The global pool of savings is shrinking, putting upward pressure on equilibrium real interest rates and bond yields.

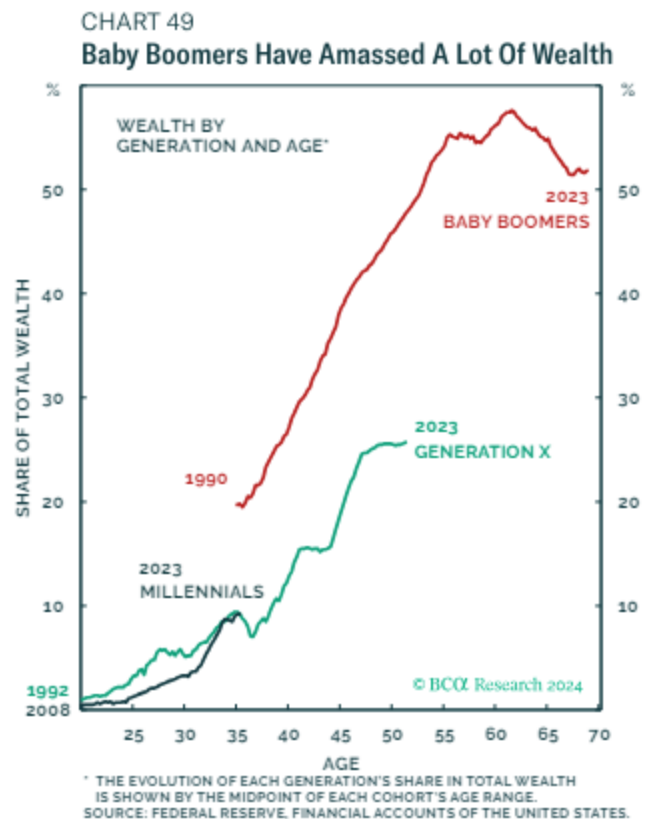
Although the disinflationary impact of AI could potentially counteract some of these inflationary forces, our bet is that the 10-year Treasury yield will still be between 4% and 5% in five years’ time.

All this suggests that investors with long-term horizons should be structurally neutral duration. ...

### **... But Cyclically, the Risk to Yields**

Is to the Downside In contrast to the longer-term outlook, the cyclical risks to bond yields are tilted to the downside. We ultimately expect the 10-year Treasury yield to drop to 3% during the next recession, as the Fed cuts rates to 2%. If that were to happen, investors would earn a total return of 13.1%.

As with equities, timing is everything. For now, US inflation remains a bit sticky, and investors have become increasingly convinced that a recession has been avoided. Thus, we do not expect yields to fall much over the next



few months. The big decline in yields will only come when the fear of recession returns. ...

### E. Commodities

#### Near-Term Upside for Oil and Industrial Metals, But Pain Awaits Once The Recession Begins

Since bottoming in mid-December, the price of Brent oil has increased by 14.5%. Copper prices have also managed to gain some altitude, rising by 8.4% since February 9.

Crude oil and industrial metals prices should continue to grind higher over the next few months thanks to a weaker dollar and a stabilization in the global manufacturing cycle. ...

However, once the next recession begins, oil and metals prices will decline.

#### Long-Term Outlook Better for Industrial Metals

Looking beyond the next recession, the outlook for metals is more favorable than for oil. The transport sector accounts for about 60% of global petroleum demand. According to the IEA, despite some recent slowing in demand growth, EVs will comprise 20% of auto sales in 2024, up from 18% in 2023 and 14% in 2022. EV penetration is set to rise to 35% in 2030, more than double what the IEA expected just two years ago (**Chart 62**). The shift towards electric vehicles will steadily erode the demand for oil.

On the flipside, the proliferation of EVs will bolster demand for industrial metals, as they are heavily used in both the vehicles themselves and in the electricity distribution networks necessary to support them. BCA's commodity strategists estimate that the global renewable-energy transition will require refined copper supply to double over the next 10 years. They reckon that this additional demand will more than offset the likely decrease in demand stemming from weaker Chinese real estate investment.

The supply outlook also points to more upside for metals prices and crude oil prices. Mining capex has been weak for the past ten years. Metal inventories remain near record lows. Political uncertainty continues to

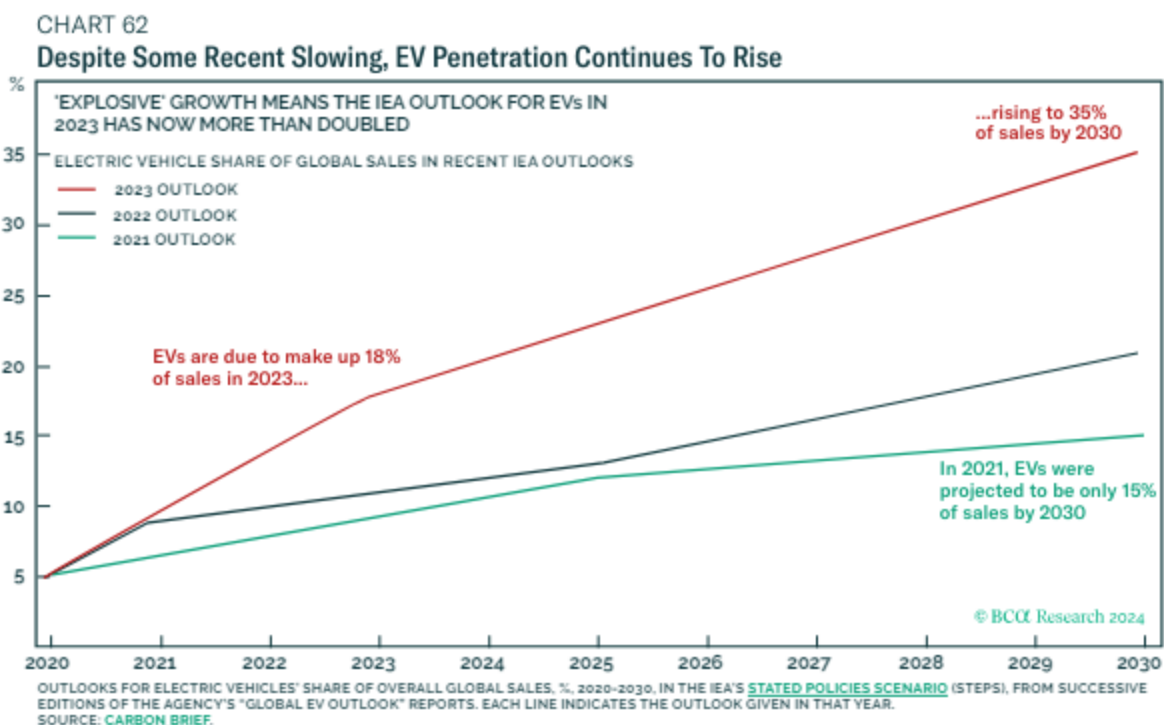
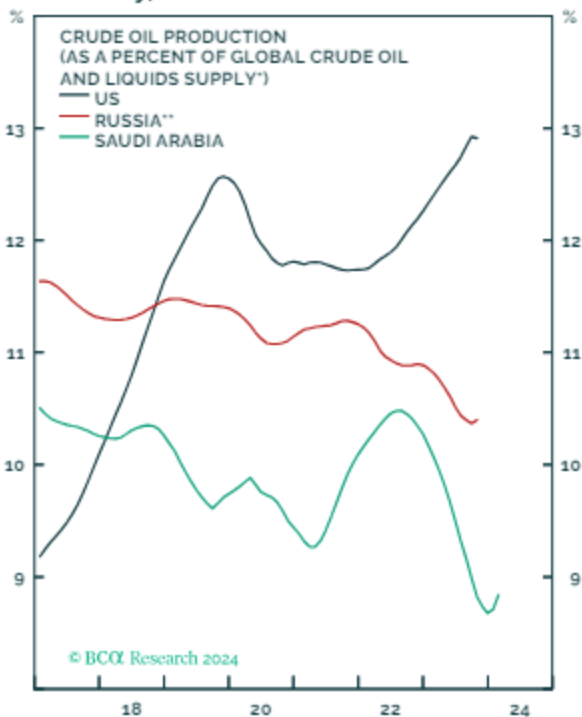
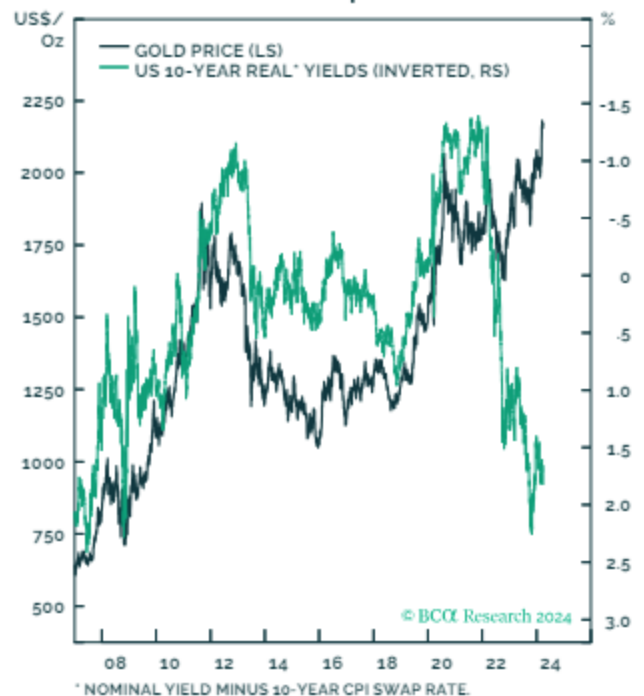


CHART 65  
Drill Baby, Drill



\* SUPPLY INCLUDES PRODUCTION OF CRUDE OIL (INCLUDING LEASE CONDENSATES), NATURAL GAS PLANT LIQUIDS, BIOFUELS, OTHER LIQUIDS, AND REFINERY PROCESSING GAINS.  
 \*\* SERIES INCLUDES CRUDE AND CONDENSATES.  
 SOURCE: US EIA.  
 NOTE: SERIES SHOWN SMOOTHED EXCEPT FOR LATEST DATA POINT.

CHART 66  
Gold Prices Have Decoupled From Real Yields



hamper mining investment in many countries.

Admittedly, much the same can be said about oil supply.

However, there is one big difference: US oil production has returned to record highs. The US now accounts for 13% of global crude oil output, up from 9% in 2017 (Chart 65). Saudi Arabia's share has fallen to a multi-decade low. For OPEC, it only makes sense to cut oil production to defend prices if it is still generating enough revenue on its remaining output. As US production marches higher, the ability of OPEC to maintain control of oil prices could diminish.

### Gold Is Expensive But Supported By Central Bank Purchases

Up until early 2022, gold prices generally moved in line with real bond yields (Chart 66). That made sense: Since gold does not generate any cash flow, the opportunity cost of holding gold should reflect the inflation-adjusted return on interest-bearing assets

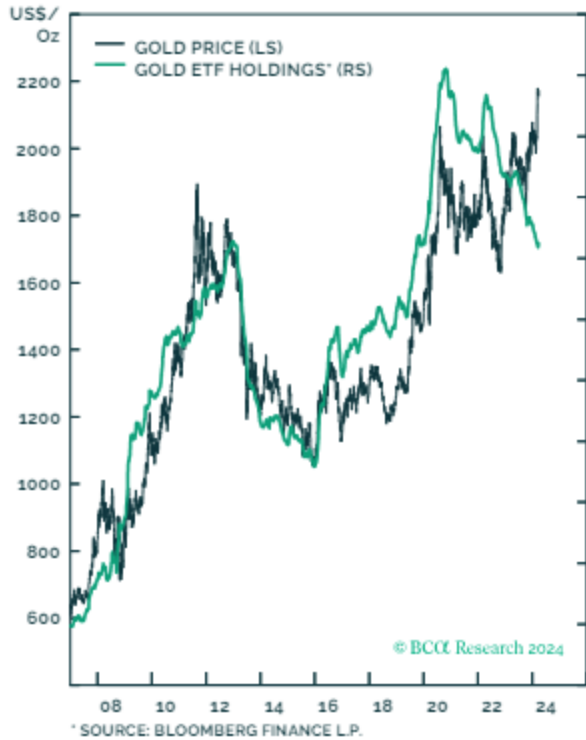
Over the last two years, however, real rates have risen but gold prices have not fallen. In fact, they hit a record high earlier this month.

Gold's resilience cannot be easily chalked up to retail demand. Inflows into gold ETFs have been trending lower for the past three years (Chart 67).

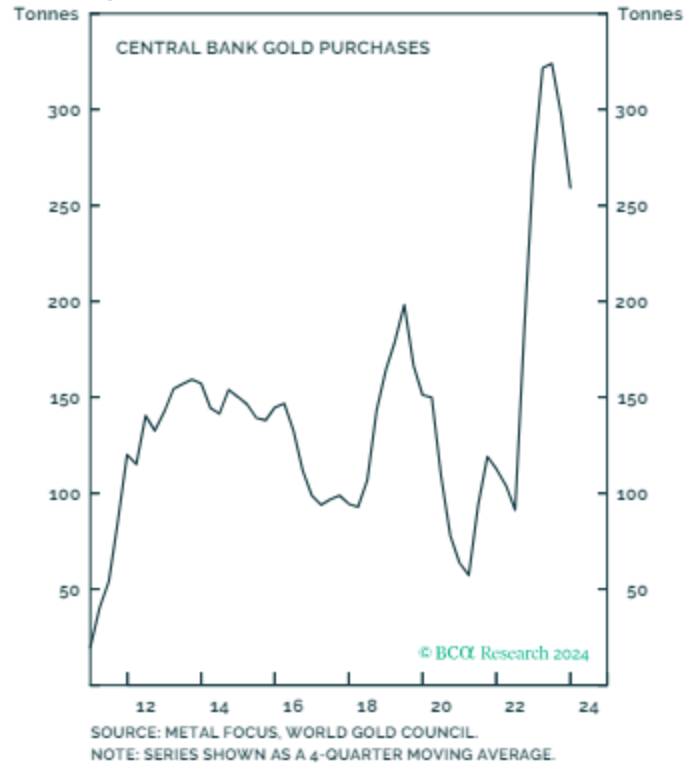
A more plausible explanation is that central banks have stepped up gold buying. According to the World Gold Council, while central bank gold purchases have eased of late, they are still double what they were between 2010 and 2022 (Chart 68). Notably, China now holds 4% of its foreign reserves in gold, up from 1% in 2014.

Given the prospect of further central bank gold buying, we are reluctant to short gold.

**CHART 67**  
**Inflows Into Gold ETFs Have Been Trending Lower**



**CHART 68**  
**Central Bankers Have Been Stocking Up On Gold**



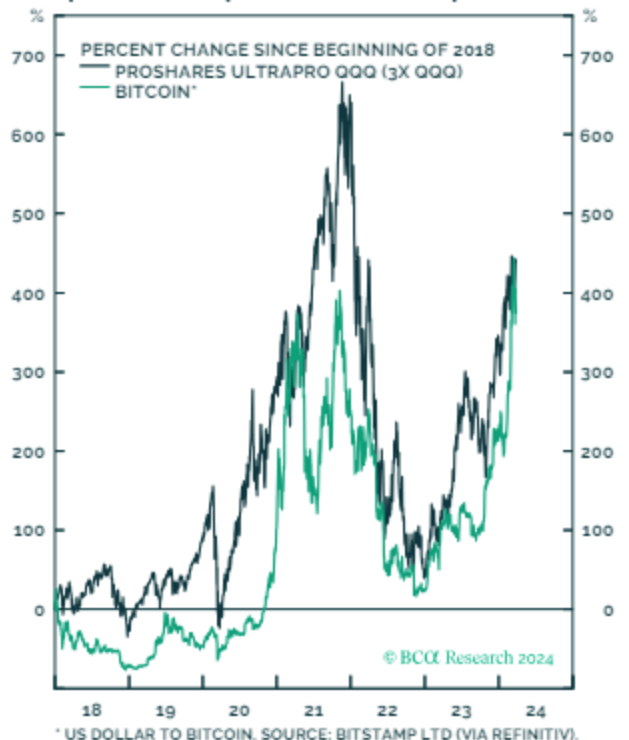
That said, owning gold at current prices has become increasingly risky. Gold is expensive in real terms. It is also trading well above average production costs, which currently stand at \$1340 an ounce. Investors concerned about inflation would be better off buying TIPS rather than gold.

### Reiterating a Negative Outlook on Crypto Assets

The price of Bitcoin hit a record high earlier in March. It is up 57% year-to-date. Unlike in the past, most of Bitcoin’s defenders have not even bothered to trot out the standard “use case” arguments to explain why the price has risen. It is simply all about “flows” now, specifically inflows into newly authorized Bitcoin ETFs.

But “use case” does matter. Within days of ChatGPT’s release, a cornucopia of useful applications appeared utilizing the new tool. Sixteen years after the introduction of Bitcoin, not a single major application has appeared that does not involve fraud or speculation. **Chart 70** shows that Bitcoin’s price has essentially tracked the triple-levered Nasdaq-100 ETF over the past five years.

**CHART 70**  
**Bitcoin's Trajectory Has Mirrored The Highly Speculative Triple-Levered Nasdaq-100 ETF**



If speculative stocks end up falling during the next recession, as seems likely, so will Bitcoin. We are maintaining our long-term BTC price target of \$5,000.

His classic "Thinking, Fast and Slow" was one of the three books that I used in the class, "Advanced Topics in Investing", that I taught for 6 years at OU. From the WSJ:

## The Psychologist Who Turned the Investing World on Its Head

Daniel Kahneman gave people an understanding of what drives financial decisions

By *Jason Zweig*

March 29, 2024

Daniel Kahneman explained investors to themselves.

A psychologist at Princeton University and winner of the Nobel Prize in economics, Kahneman died on March 27, age 90.

Before the pioneering work done by Kahneman and his research partner, Amos Tversky, who died in 1996, economists had assumed that people were “rational,” meaning we are self-interested, use all available information to make unbiased decisions, and our preferences are consistent.

Kahneman and Tversky showed that’s nonsense. Their findings, directly or indirectly, inspired change across the business world, including the redesign of organ-donation programs and improvements in planning for [multibillion-dollar infrastructure projects](#).

Kahneman was a pioneer of what became known as behavioral economics, although he always saw himself as a psychologist. Investors who take Kahneman and Tversky’s lessons to heart can minimize fees, losses and regrets. Kahneman may well have had more influence on investing than anyone else who wasn’t a professional investor.

I first met Danny, as everyone called him, at a conference on behavioral economics in 1996. For years, as an investing journalist, I had wondered: Why are smart people so stupid about money?

About five minutes into Danny’s presentation, I realized he had the answers—not only to that question, but to nearly every mystery of financial behavior.

Why do we sell our winners too soon and hang onto our losers too long? Why don’t we realize that most hot streaks are just luck? Why do we say we have a high tolerance for risk and then suffer the torments of the damned when the market falls? Why do we ignore the odds when we know they’re stacked against us?

Danny paced softly back and forth at the front of the room, his blue-green eyes sparkling with amusement as he documented these behaviors and demolished conventional economic theory.

For decades, he and Tversky had conducted experiments, almost childlike in their simplicity, to see how people really think and behave.

No, Danny said, money lost isn’t the same as money gained. Losses feel at least twice as painful as gains feel pleasant. He asked the conference attendees: If you’d lose \$100 on a coin toss if it came up tails, how much would you have to win on heads before you’d take the bet? Most of us said \$200 or more.

No, people don't incorporate all available information. We think short streaks in a random process enable us to predict what comes next. We think jackpots happen more often than they do, making us overconfident. We think disasters are more common than they are, making us suckers for schemes that purport to protect us.

Ask people if they want to take a risk with an 80% chance of success, and most say yes. Ask instead if they'd incur the same risk with a 20% chance of failure, and many say no.

Noting that the stocks people sell outperform the ones they buy, Danny joked that "the cost of having an idea is 4%."

I wasn't just struck by his insights; I was stricken by them. I immediately bought all three of the books he had edited. For days, I sat in a windowless room, reading feverishly, red pen in hand, scribbling notes, underlining entire paragraphs, peppering the margins with arrows and exclamation points.

In 2001, a year before Danny won the Nobel, I wrote [a long profile of him](#).

"The most important question to ask before making a decision," he told me, "is 'What is the base rate?'"

He meant you should begin every major decision by figuring out the objective odds of success, given the historical range of outcomes in similar situations.

If you're thinking of starting a new business, your gut might tell you there's no way you can fail. According to the Bureau of Labor Statistics, however, half of new businesses [die within the first five years](#). That base rate comes from millions of startups, each of which also expected to succeed. You, on the other hand, are a sample of one.

Knowing that the base rate is 50/50 shouldn't deter you from trying, but it should prevent you from being unrealistically optimistic.

Danny knew base rates weren't quite everything. He told me that before he proposed to his second wife, Anne Treisman, he said to her: "I'm Jewish, you're not. I'm neurotic, you're not. Almost half of all marriages end in divorce. The base rates are against us."

"Oh, who cares about base rates!" she replied. Their marriage lasted four decades; Treisman died in 2018.

In 1969, Danny was teaching at the Hebrew University in Jerusalem when he asked Tversky, a mathematical psychologist and colleague there, to visit his class.

In his guest lecture, Tversky argued humans aren't that bad at estimating risks and probabilities.

"I just don't believe it!" exclaimed Danny, who was studying visual perception. He already believed that just as optical illusions fool the eye, cognitive illusions fool the mind.

The two men continued their debate over lunch—and [for many years after](#). Amos was organized, confident, quantitatively brilliant. Danny was untidy, self-doubting, astoundingly intuitive. Together, they were intellectual lightning in a bottle.

In 1971, to decide whose name would be listed as lead author on the first scientific paper they published together, the two men flipped a coin. Over the next quarter-century, they published more than two dozen papers together.

In 2006, Danny asked me to [help him write a book](#). I auditioned for a few months, coming up with several different proposals for how to structure the project. We finally got started in early 2007.

What eventually emerged was “[Thinking, Fast and Slow](#),” published late in 2011: an internationally bestselling memoir that also offered an encyclopedic explanation of how the human mind works.

Early on, Danny took me to lunch with his wife near the Princeton campus. When he stepped away, I asked Anne, “Do you think Danny is crazy for wanting to do this book with me?”

“No,” she said. “But you might be crazy for wanting to do it with him.”

In the beginning, I wrote the first drafts of chapters that never saw the light of day. Gradually, Danny took over the writing, agonizing over every sentence, as I rewrote and edited.

Late in 2007, as we were polishing the chapter called “The Illusion of Validity,” I woke up one night in an icy sweat, pulse racing, gasping for air. My wife rushed me to the emergency room. It turned out I hadn’t had a heart attack; I’d had a panic attack, the only one in my life before or since.

Danny was even more alarmed than I was.

In 2008 I moved on, joining The Wall Street Journal. Neither of us would ever publicly discuss our book divorce; Danny finished the final third of the book without me.

“Collaborations don’t always end well,” he’d warned me on our first day of work together, “so I want to make sure you will always think of me as a mensch,” a good person.

And so I do—the most complicated mensch I’ve ever known.

Working on the book exposed me to three of Danny’s qualities I hadn’t previously encountered in their full intensity. Only years later did I realize that I’ve internalized them as a journalist and an investor. Or so I hope.

First, Danny saw everything through a child’s eyes or, as some people call it, “beginner’s mind.” No one else I’ve ever known has so often asked: Why? Instead of assuming the status quo is valid, Danny always started by wondering whether it made any sense.

He was also relentlessly self-critical. I once showed him a letter I’d gotten from a reader telling me—correctly but rudely—that I was wrong about something. “Do you have any idea how lucky you are to have thousands of people who can tell you you’re wrong?” Danny said.

Finally, Danny could rework what we had already done as if it had never existed. Most people hate changing their mind; he liked nothing better, when the evidence justified it. “I have no sunk costs,” he would say.

One of his favorite words, while working on the book, was “miserable.” He used it to describe whatever we had just written; the process of writing a book; and, above all, himself.

Danny’s misery was largely rooted in the decades he and Amos had spent exploring the failings of the human mind by picking apart their own errors of thought and judgment.

Taking the outside view on everything else had given Danny the outside view on himself. He embodied the ultimate form of self-knowledge: to distrust yourself above all.

He knew full well how smart he was, but he also knew how foolish he could be. Noticing that he intuitively stereotyped a bespectacled child as “the young professor,” Danny realized people extrapolate the future from almost no data at all. After buying an expensive apartment, he laughed at knowing that he would also overpay to furnish it.



Born in 1934 in what today is Tel Aviv, Israel, while his mother was visiting there, Danny was raised in France. He spent much of his childhood hiding from the Nazis in barns and chicken coops in the French countryside.

He insisted that didn't explain much about him; after all, not every survivor of the Holocaust had become a self-critical psychologist fascinated by financial behavior.

Instead, he credited his success to hard work—but even more to luck, especially meeting Tversky.

Danny also insisted that studying the pitfalls and paradoxes of the human mind didn't make him any better at problem-solving than anybody else: "I'm just better at recognizing my mistakes after I make them."

For all his knowledge of how foolish investors can be, Danny didn't try to outsmart the market. "I don't try to be clever at all," he told me. Most of his money was in index funds. "The idea that I could see what no one else can is an illusion," he said.

"All of us would be better investors," he often said, "if we just made fewer decisions."

## Follow-ups

From The Economist:

### **Donald Trump joins the meme-stock frenzy**

Investors in his SPAC may get burned, but they don't seem to mind

Mar 20th 2024

There is a spirited corner of the internet where MAGA die-hards go to talk politics, God and the stockmarket. On Reddit and Rumble (a kind of far-right YouTube) they pump up their man Donald Trump and his social-media company, Truth Social, which they pray will soon go public via a [special-purpose acquisition company](#) (SPAC). Together they pore over its latest filings with the Securities and Exchange Commission (SEC), then they read a Bible verse or two. One Old Testament proverb—"Buy the truth and do not sell it"—is almost too apt. "That's what we're doing here, folks," says Chad Nedohin, a hype-man on Rumble. "Literally, as a team of investors, we have bought into truth and we are never selling because we are diamond-handed hodlers". That is crypto-speak for "hold on for dear life".

Faith is a prerequisite for this merry band of meme-stock traders. Truth Social's path to the public markets has been long and fraught, dogged by an SEC probe, lawsuits by disgruntled former employees and a cash crunch. At last a flotation looks imminent. On March 22nd investors in a SPAC—a listed pot of capital—called [Digital World Acquisition Corp](#) (DWAC) will vote on whether to merge with Truth Social's parent company, Trump Media & Technology Group. If enough assent the combined firm will start trading under the NASDAQ ticker DJT.

The deal comes at an opportune time. Trump Media is running on fumes: in the first three quarters of last year it lost \$49m and had just \$1.8m cash on hand as of September. Through the merger it will raise about \$240m, estimates Michael Ohlrogge of New York University School of Law. At DWAC's current share price the new entity will have a market capitalization of \$6.3bn. As with other meme stocks, that makes no economic sense. The firm has reported 8.9m sign-ups for Truth Social but prefers not to disclose how many are active daily. "Focusing on these KPIs might not align with the best interests" of Trump Media, says its prospectus.

Mr Trump will own a stake worth \$4.1bn. But a six-month lock-up, during which he cannot sell, makes paper gains of little use in his present liquidity crunch. In February he was fined nearly half a billion dollars for fraud at his [property business](#); by March 25th he must secure a bond for that amount while he appeals against the judgment.

That is proving tricky: about 30 bond companies have turned him down so far because he lacks enough cash for collateral. He has asked an appeals court to reduce the bond. If it refuses he will have to sell assets or ask a rich supporter to bail him out. Failing that Letitia James, the prosecutor who brought the case, could freeze his bank accounts or seize some of his property. She likes to say that she can see 40 Wall Street, one of Mr. Trump's towers, from her office.

As for DJT, economic reality should sink in eventually. If and when Mr Trump liquidates his holdings the share price will drop. Since the beginning of 2019 nine out of ten SPACs have lost value after combining with their target company, notes Michael Klausner of Stanford Law School. On average the share prices of post-merger spacs have declined by 60%. Target companies got a good deal in these mergers while spac shareholders who stuck through the listing—mostly unsophisticated retail investors—took a bath.

The DJT crowd hears the critics; it just thinks they are wrong. Back in 2022, when the sec was investigating the deal, Mr Nedohin, the Rumble hype-man, insisted that Trump Media was not a Ponzi scheme. “This is different,” he assured his excitable followers. “We are helping promote a company that has the potential to be a trillion dollars easily...It will be paying out!”

From the front page of Wednesday's WSJ:

## **Truth Social Stock Climbs 16% After Debut**

BY AMRITH RAMKUMAR

Shares of Donald Trump's social-media company surged 16% on their first day of trading, boosting the Republican presidential candidate's fortune. The question is, how soon can he tap his roughly \$4.5 billion stake in Truth Social?

That is up to the board of Truth Social's parent. The group includes his eldest son, three former members of his administration and the former congressman who took a leading role in defending the former president in his first impeachment trial.

Truth Social's parent began trading Tuesday under the ticker DJT, Trump's initials. Its shares soared as much as 59% after the opening bell and swung throughout the day before settling well below their peak after a wild session.

Tuesday's rally gives the early-stage company a market value of about \$8 billion. The valuation makes Trump's approximately 60% stake worth about \$4.5 billion. Those values will continue swinging with the stock price. Trading was so intense that Nasdaq temporarily halted trading after the opening bell. ...

The company is struggling to attract users and advertisers to compete with larger social-media platforms, but that isn't stopping Trump supporters from lifting up the stock.

Trading in the stock is a pattern similar to the one seen in shares of videogame retailer GameStop and other stocks popular on social media in recent years.

The timing couldn't be better for Trump. On Monday, an appeals court ruled Trump can pay \$175 million to put his \$454 million civil-fraud judgment on hold during his appeal. Trump hadn't been able to get a bond to cover the whole judgment.

The \$175 million is a fraction of Trump's newfound wealth, but his shares are just out of reach. Typically, people involved in the type of deals that brought Truth Social to the market aren't allowed to sell or borrow against their shares for six months.

The board would need to grant Trump a waiver if he wished to make such moves before then. That isn't unheard of, but boards typically wait a month or more before letting a big owner sell. They risk setting off a flood of selling that could cause big losses for independent investors. ...

Shannon Devine, a spokeswoman for Truth Social's parent, said this article is "clearly the latest in a long line of sloppy, poorly researched hit pieces on Truth Social by The Wall Street Journal." She didn't say what was misleading or inaccurate in this or previous articles.

Granting Trump a waiver to sell could be risky for the board because he is by far the largest shareholder and the main reason individual investors have been buying the stock. Any signal that he is selling or likely to sell could dent the share price and fuel concerns about Truth Social's future. Trump is getting this huge windfall because his supporters banded together on social media to push up the stock. Shares of the SPAC that became Truth Social rose 35% on Monday and surged in advance of the deal closing. ...

If the stock does fall after an early share sale by Trump, such a move could add to a number of lawsuits from investors or people involved in the deal. Several lawsuits were filed by insiders seeking additional shares leading up to the merger's completion. ...

Many professional investors said the stock is disconnected from the reality of Truth Social's business, which posted about \$5 million in sales and tens of millions in losses from its 2021 launch to September 2023.

From Morningstar:

## Trump Media Is Not a Meme Stock. It's a Cryptocurrency

Investors aren't buying DJT for future cash flows.

**John Rekenhaller** Mar 28, 2024

### Stage Number One: Concept Stock

When I [first wrote](#) about Digital World Acquisition Corp., in January 2022, its business operations were merely an idea. To be sure, DWAC existed. It was a [special-purpose acquisition company](#), or SPAC, established for the purpose of buying another firm. DWAC's value consisted of its commitment to buy privately held Trump Media & Technology Group, which had yet to offer a product.

I researched DWAC's stock conventionally, evaluating four scenarios for Trump Media's business possibilities, ranging from bearish to strongly bullish. The upshot: Because the ex-president would receive majority ownership when the transaction was completed, retail shareholders would be greatly diluted. They would lose money unless the company's value exceeded \$10 billion.

The responses to that column showed that I had misread the situation. The comments were entirely motivated by politics. Not a single reader addressed my numbers. In doing the fundamental analysis, I had whistled into a hurricane.

## **Stage Number Two: Emerging Growth**

One month after my article ran, Trump Media debuted its social-media platform, Truth Social. Although the launch attracted far more attention than is customary with new businesses, its media reception was similar. Trump Media's public-relations department crowed about its initial success. Some outlets dutifully republished the company's releases, while others were skeptical, presenting counterevidence. In other words, the business press behaved as usual.

Although the business had yet to report results, DWAC investors became wary. As is often the case with concept stocks—or with most other things, come to think of it—the anticipation trumped the reality. Closing at \$92.90 the day after Truth Social's inception, DWAC's stock began a long, painful slide. Eighteen months later, its price bottomed at \$12.46, making for an 87% loss. Ouch!

Contributing to the stock's problems were ongoing SEC investigations, which continually delayed the acquisition. Originally scheduled for September 2022, the purchase date was initially postponed to June 2023, and then pushed back again. Management was also forced to restate its financial statements, as the SEC determined that several of its filings had been materially in error.

## **Stage Number Three: Hibernation**

By summer 2023, the bloom was thoroughly off the rose. Not only were market-research sites reporting low adoption rates for Truth Social, but its business model had lost favor. Elon Musk's purchase of Twitter had highlighted the industry's woes. Because few users will pay for social-media services, suppliers rely upon advertising revenue—and advertisers have fled sites with political controversies.

Finally, SPACs were in disrepute, as most of their stocks had performed poorly.

In short, DWAC looked to be dead in the water. Its acquisition had been deferred and its executives rebuked. Meanwhile, the company that it planned to buy was struggling. Under such conditions, SPAC investors typically veto the scheduled deal, thereby forcing the organization to return the par value of their shares.

However, as I learned after publishing my 2022 column, Donald Trump's presence changes the ordinary rules. After all, DWAC was not buying *any* business; it was purchasing one that would be owned, branded, and promoted by the ex-president. Big difference! Millions of potential investors who otherwise would not have bothered with DWAC wished to care. They just needed a reason.

## **Stage Number Four: Rejuvenation**

They found it in January of this year, when the oft-postponed merger finally appeared on the horizon. By then, Trump Media's financial results had been released, as part of DWAC's filing process, and they were breathtakingly bad. Not only had Truth Social [received only \\$2.3 million](#) in revenue during the first six months of 2023, but [business had been flat](#) during the following quarter.

To greatly understate the matter, those results failed to meet the company's projections. In October 2021, Trump Media had provided its initial [financial forecast](#). After posting negligible revenue in 2022, the presentation stated, Trump Media would post \$144 million in sales in 2023, followed by \$835 million this year. Not so much! (By now, most of Trump Media's revenues were projected to come not from its social-media site,

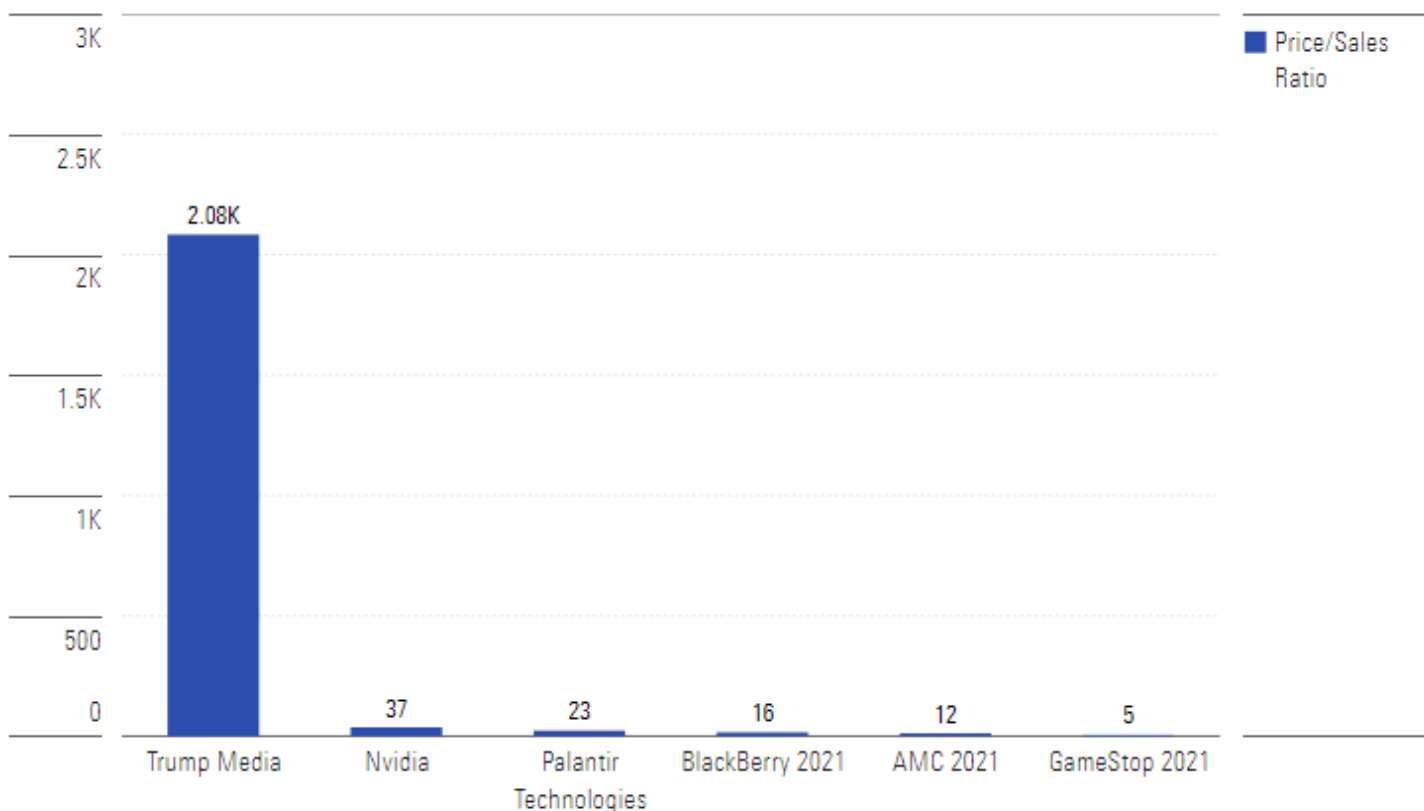
but instead from an entertainment streaming service called TMTG+. However, the latter has never been created.)

None of which, of course, has mattered to investors. The newly public Trump Media & Technology Group [DJT](#), which consists of the merger of DWAC's \$300 million cash position and the Truth Social platform, is worth a great deal. How much, exactly, is unclear. *The Wall Street Journal's* James Mackintosh valiantly [tackled the math](#), which is tricky because the level of shareholder dilution depends upon several circumstances, but his appraisal did not match the company's. Since Trump Media's representatives did not respond to his questions, the issue remains unresolved.

In any case, DJT's valuation is extraordinarily steep. The chart below compares its price/sales ratio to the peak values for three celebrated 2021 meme stocks, along with the current ratios of two celebrated 2024 stocks, Palantir Technologies [PLTR](#) and Nvidia [NVDA](#). (When calculating Trump Media's ratio, I annualized its nine-month sales and used Mackintosh's share estimate.) Truly, there is no comparison.

## Sky High: A Look at Trump Media's Valuation

How DJT compares with 2024's stock darlings and 2021's meme stocks (price/sales ratios)



Data as of Mar 27, 2024. Morningstar Direct

## Stage Number Five: Cryptocurrency

Many observers have called Trump Media a meme stock, but the label does not fit. Meme stocks consist either of established firms that have stagnated, such as 2021's stars, or they are growth stories, as with this year's heroes. In either case, meme-stock investors care about their companies' business operations. When I [wrote](#) in January 2021 about GameStop [GME](#), several shareholders quarreled with my assessment of the company's prospects. But business results are not the issue with Trump Media. If they were, the DWAC transaction never would have been consummated, and DJT stock never would have come to market.

Trump Media is instead a cryptocurrency. As with bitcoin, people buy Trump Media not for future cash flows but because: 1) they expect its price to rise, and 2) they feel an affiliation for the asset. Bitcoin owners are members of a club. So, too, are Trump Media investors, to an even greater degree. For them, DJT shares represent a currency by which they can express their beliefs and commitment.

Which is why I will make no forecasts about Trump Media's stock price. In January 2022, I offered my view on DWAC, correctly as it turned out. I will not make a second attempt as the normal investment rules no longer apply. Predicting DJT's fortune is like predicting the direction of bitcoin. Others may try, but not me.

From Bespoke on Mar. 17th:

Following "finfluencers," or financial influencers, might not be such a good idea if you're taking their investment advice. According to one study, on average, investors following these finfluencers underperformed the market by 0.35% per month, translating to an annualized underperformance of 4.1%. While a minority of top-performing finfluencers outperformed the market significantly, a substantial portion exhibited "antiskill," meaning their recommendations resulted in statistically significant negative returns. Interestingly, the study found that those with the most followers were more likely to offer poor advice, suggesting that popularity on social media platforms might not correlate with financial acumen.