Directions

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FALL 2020

CLS INVESTMENTS

Fear of Missing Out

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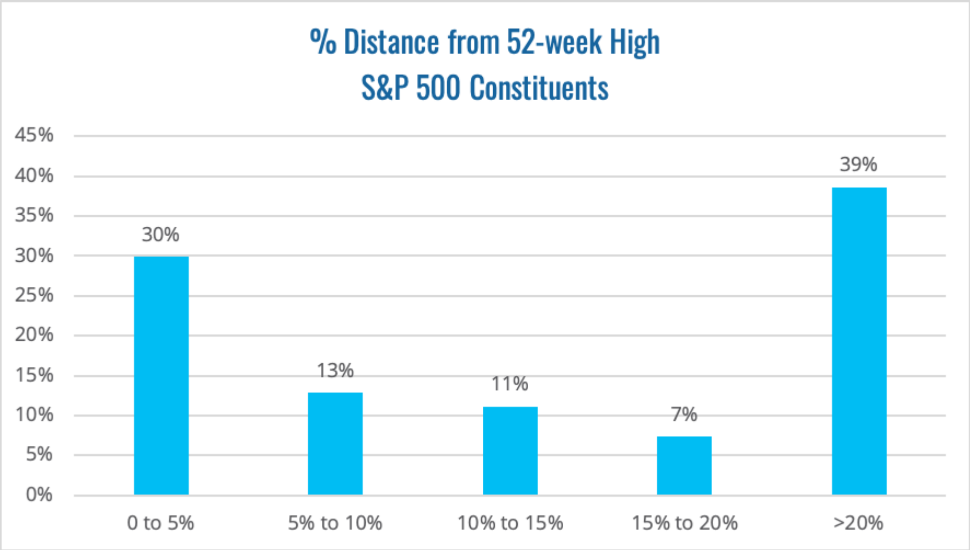
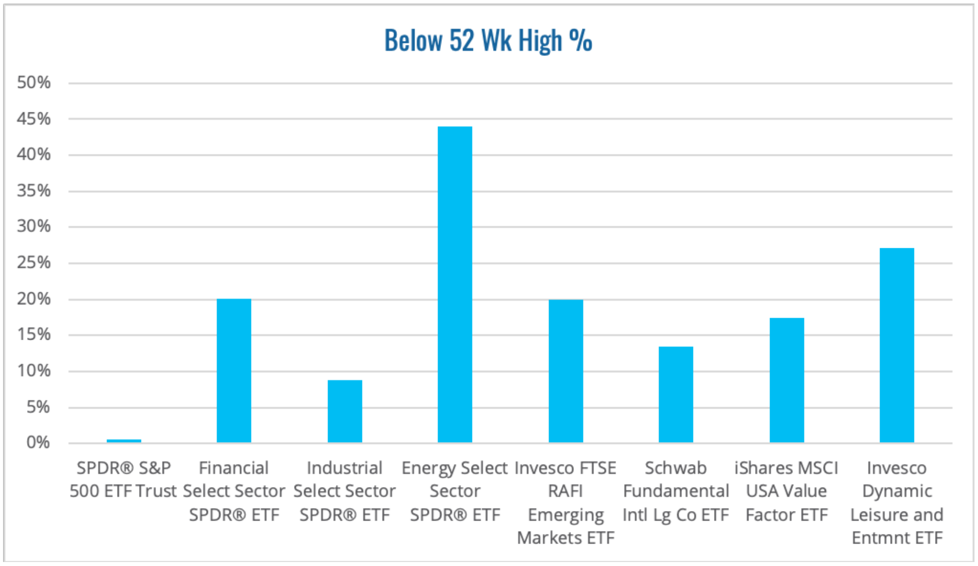
What a year it has been in the markets. Not only did we see the fastest bear market in history, but we followed it up with the best 100-trading-day return and quickest-ever recovery from a 30% drop in U.S. stock market history. The word 'unprecedented' has become common vernacular at this point. Now, as we see several stocks and even whole areas of the market at all-time highs, it may leave investors feeling like they have missed the boat on a fantastic buying opportunity. While the past five months have been tremendous for many areas of the market, not all areas have fully recovered, and there are still many attractive values available to investors.

With news headlines focused on the broad indices, i.e., the S&P 500 reaching new all-time highs, and the likes of Apple, Amazon, and Tesla's huge returns, the chart below may come as a surprise to investors.



Source: Morningstar Direct 9/1/2020

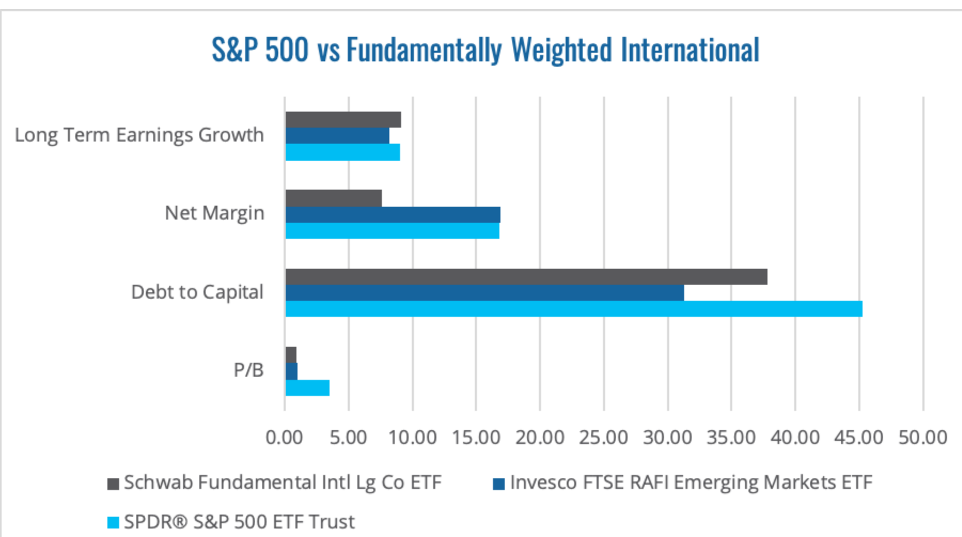
While I was well aware that it has been a narrowly led market, I still would not have thought 39% of the S&P 500 remains more than 20% below its 52-week highs. Not only does this point to how few names have surged off the lows, but it also goes to show that less-popular names have plenty of room left to run in the recovery. The chart on the following page shows a few ETFs which may offer opportunities. While the S&P 500 is at its 52-week high, these other products are currently anywhere from 8% to even 44% off their highs.



Source: Morningstar Direct 9/1/2020

Energy remains well below its previous high, in spite of the bounce back in oil prices. Financials have also struggled in the recovery, given the low-interest-rate environment. The leisure and entertainment sector was hit hard by the economic shutdown; its stock prices still reflect the ongoing hurt, but may provide an attractive opportunity as areas continue to reopen and activity expands.

Each of these market segments arguably have more attractive valuations, and most have sounder balance sheets and higher growth expectations, than the S&P 500. Digging in a little further to a couple of international names illustrates this very clearly. Both developed and emerging markets with a value tilt are now trading below book value and at a fraction of the U.S. market. As mentioned previously, these steep discounts come with less debt on their balance sheets and similar margins and growth rates.



Source: Morningstar Direct 9/1/2020

As we have seen the dollar continue to sell off, this presents another tailwind for international markets, which is an area that seems ripe for potential outperformance moving forward.

1 Morningstar Direct 9/1/2020
2 [W3](W3) 9/07/2020

Don’t Get Baited!

JACKSON LEE, CFA
Quantitative Portfolio Manager

My family and I recently went crabbing on Galveston Island, a beautiful spot between West Bay and the Gulf of Mexico, with a friend as our guide. Since we were first-timers, he tried to describe what crabbing is like on our drive over. It’s simple, he said. Put your bait on the hook, cast it into the bay, and wait for the crab to bite (or pinch in this case). That sounded easy and a lot like fishing, which I am more experienced with. I was ready to catch a lot of crabs!

Then I was reminded that reality rarely lives up to expectations. The crabs outsmarted me with their vigilance, and I was surprised how quickly they could move.

It also reminded me of investing. As Warren Buffett once said, “Investing is simple, but not easy.” During the pandemic, many people, including gamblers, have turned to the stock market for entertainment (having no sports to bet on). Online brokerages, such as Fidelity, TD Ameritrade, Robinhood, and others, have reported an uptick in account growth. Fidelity added 1.17 million new retail accounts in the second quarter, while TD Ameritrade added 661,000 accounts.[1,2] Robinhood, a popular trading app whose median customer age is 31, added 3 million accounts during the first four months of 2020.[3]

We have always encouraged people to invest, and we will continue to do so. However, there is a fine line between gambling and investing, and many learned that lesson the hard way last week. Some of the most popular names amongst Robinhood traders saw double-digit drawdowns last week. DocuSign, Zoom Video, and Tesla all fell nearly 20%, while NVDIA and Apple slid more than 10% compared to the S&P 500’s loss of 4%. Despite the drawdown, all five stocks have experienced triple-digit gains so far this year with an average return of 300%, beating the S&P 500 by more than 40x and the tech-heavy NASDAQ index by 11x!

Name	Ticker	Return (Day to Day) 2020-01-01 to 2020-09-06 USD	Drawdown During First Week of September 2020
S&P 500 TR USD		**7.48%**	**-4.28%**
NASDAQ Composite TR USD		**26.91%**	**-6.16%**
DocuSign Inc	DOCU	191.81%	-19.55%
Zoom Video Communications Inc	ZM	443.64%	-19.18%
Tesla Inc	TSLA	399.99%	-18.33%
NVIDIA Corp	NVDA	114.87%	-12.02%
NIO Inc ADR	NIO	347.26%	-10.64%
Average		**299.51%**	**-15.94%**

Source: Morningstar Direct 9/4/2020

Unfortunately, these gains will probably not be realized by most Robinhood traders. Many are inexperienced and might have jumped on the wagon too late. To make things worse, Robinhood reported that $111 million of its $180 million order-flow revenue in the second quarter came from options.[3] While options are great tools if used correctly, investors with less knowledge could take on a lot more risk than they realize.

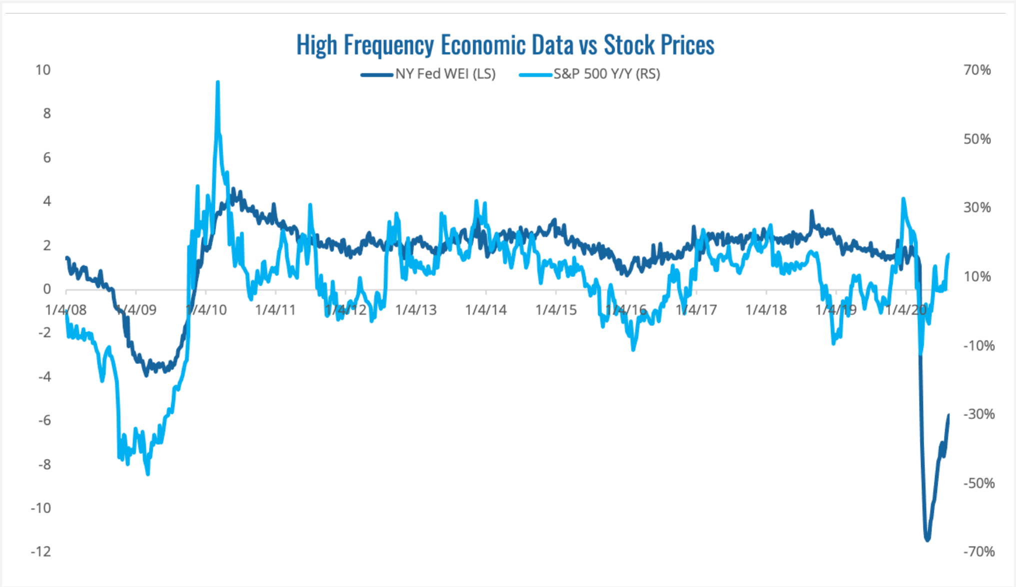
1 Fidelity Investments 9/7/2020
2 TD Ameritrade 9/7/2020
3 Business Insider 9/7/2020
4 W3 9/7/2020

Is the Economy Healing?

GRANT ENGELBART
CFA, CAIA, CLS Director of Research and Senior Portfolio Manager

Thankfully, the answer to that question appears to be 'yes'. With the help of a brand-new series of economic data (!), we are now able to review how the economy has recovered, thus far, without relying on GDP data, which typically lags significantly. The New York Federal Reserve has developed a weekly economic index (WEI) data point, which utilizes daily and weekly data to generate a real-time expectation of GDP growth. The index was created with data going back to 2008, as you can see here, and in the graph below. It includes 10 high-frequency data points, such as jobless claims, same-store sales, steel production, fuel sales, and electricity output, amongst others. It's pretty exciting — a brand new economic data series doesn't just pop up all that often!

The potential benefit of high-frequency economic data is, of course, having more up-to-date information. GDP has a quarterly lag and, as a result, typically doesn't provide anything too shocking when it comes out. As we know, the stock market and the economy are not the same thing, but stocks do typically react and are impacted by economic data. However, stocks are also forward-looking, whereas economic data is backward-looking. This new high-frequency data series more closely aligns with how the stock market has reacted. This is worth noting because you can see the decline in WEI has been massive and unprecedented. The stock market did drop 30%+ earlier in the year, but due to the quick recovery, the blip isn't as noticeable when looking at year-over-year performance. While many may be focused on the huge decline in economic activity, this new data series is one of our first glimpses into the massive rebound we've seen.



Source: Bloomberg, NY Federal Reserve 8/14/2020

While we are still below water from 2019 economic activity, we have bounced off the lows and continue to do so. I believe this helps to explain the rebound in stocks, which many investors have scratched their heads about. Stocks appear to be pricing in a return to more normal economic activity, at some point in the future.

1 Bloomberg, NY Federal Reserve 9/7/2020
2 W3

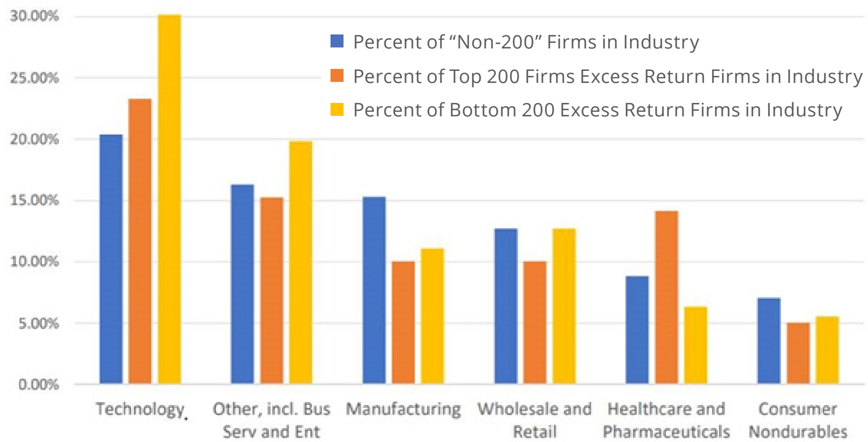
Questions from Investors Like You

CASE EICHENBERGER
CIMA, CLS Senior Client Portfolio Manager

Recently, I have seen tech stocks take a beating. Are they still the best investments?"

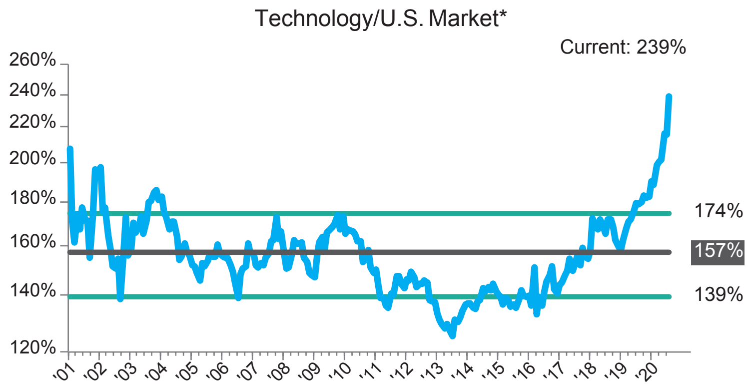
Tech stocks have enjoyed a miraculous 15-year annualized return of 13.5%[1]. With new technologies at our fingertips, the sector may seem like an unstoppable train of compounding returns. But beware. The historical numbers say otherwise. The chart below from [Hendrik Bessembinder](), a professor at Arizona State University, illustrates that tech stocks are more likely than any other sector of the market to end up in the list of 'worst stocks' than 'best stocks.'

Percent of Extreme Cumulative Return Firm/Decade Observations From Each Industry



Source: Hendrik Bessembinder. "Extreme Stock Market Performers, Part II: Do Technology Stocks Dominate?" 7/22/2020

However, just because tech stocks at times may seem more like lottery tickets, that doesn't mean you shouldn't consider investing in them. Just be sure to diversify to other sectors, industries, and countries to attempt to take advantage of better-priced buying opportunities. The chart below shows just how expensive tech stocks have recently become when compared to the rest of the market. The grey line in the center represents the long-term average valuation and the green lines represent one standard deviation away from the average.



Remember: Before jumping in on the latest craze, consider the price you may have to pay for them!

Source: CLS Chart Pack. MSCI Technology Sector relative to the CRSP U.S. Total Market Index as of 8/31/2020

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1 *Morningstar Direct 9/11/2020*
2 *[Extreme Stock Market Performers, Part II: Do Technology Stocks Dominate?]() 7/22/2020*
3 *[W3]() 6/30/20*

Disclosures:

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