Peregrine asset advisers

3rd Quarter 2020 Market Overview
The best thing about 2020…

Defying conventional wisdom with dizzying volatility, the stock market *seems* to be *immune* from travails of life in 2020.

Why is this?

The pandemic caused a 35% decline in the S&P 500 but even more astounding, has been the rapid rebound. In just over six months, the market has regained all its loss, making it the swiftest recovery of its kind in history.

Yet, this is happening during the *worst economy in 80 years*. COVID, the election, and other deleterious factors should have pushed the market down.

The S&P 500 gained 8.40% in the third quarter and this followed a 20% gain for the second quarter. How can the stock market flourish under these prevailing circumstances?

The typical reason given is Fed stimulus and government rescue packages but there is a more profound, yet simplistic explanation.

It is evident the pandemic has sparked a behavioral change in market participants. A meaningful class of investors has been transformed into "stock market players", engaging in frenzied, speculative activity. These players adopt a video game mentality, heavily influenced by FOMO (fear of missing out) and flashing news stories.

The surge in speculative activity encompasses a broad spectrum; from the Robinhood trader to famed investors and hedge fund billionaires. Consequently, this has created a speculative bubble, not unlike what we saw in 1999-2000.

The dilemma facing investment management is to gauge how long the bubble will last. On one hand, rising prices amidst a speculative fever can be richly rewarding. On the other hand, the risk becomes outsized and a "Day of Reconciliation" would likely be more severe than we are accustomed.

Currently, the landscape is fostering bubble-like behavior. People believe the market is impervious to the economy. Market momentum is strong. News flow is interpreted favorably which triggers short term price advances. Rising COVID cases are largely ignored while "players" chase stocks deemed fashionable.

The preponderance of speculative activity centers on technology stocks. The innovation and disruptiveness of these companies certainly merits attention. Accordingly, the prices of these stocks have been pushed to lofty levels as if these companies are infallible.

We know, in fact, that no stock is infallible. The opposite assurance can be made. A fundamental precept of investing is you cannot promise a stock will rise, but you can virtually guarantee, that eventually, a stock will fall by a meaningful amount.

Will valuation matter?

Below is a table showing recognized stock market leaders along with our favorite, General Mills.

	2021 sales	2021 earnings	market cap
Netflix	29,223	4,068	244 billion
Nvdia	15,780	3,622	352 billion
Tesla	42,296	3,412	417 billion
General Mills	17,516	2,253	38 billion

(sales and earnings in millions)

Netflix, Nvidia, and Tesla are excellent companies, marked by impressive innovation and disruptive technology. They are a part of the "new economy narrative".

By comparison, General Mills has comparable sales and earnings but notice the drastic difference in market value. This is an example of the widespread valuation differential which exists in the stock market. It might also signal investment opportunity as the new market "players" might ignore favorable developments in the market.

Sticking with the essentials

Conservative, steady, and recession-resistant businesses remain core holdings for our client accounts. These stocks pay attractive dividends and should soon enjoy better price performance in a zero-interest rate, weakened economy.

We also favor companies that offer vital services such as Verizon and transportation companies like truckers and UPS.

Our client accounts also continue to hold income producing bonds for diversification and shelter from volatility.

Dan Botti
Investment Manager 10/16/2020

Peregrine Asset Advisers ● 9755 SW Barnes Rd. Suite 295 ● Portland Oregon 97225●
503.459.4651 ● www.peregrineaa.com