Churchill Management Group

Monthly Market Update

September 14, 2020

TACTICAL STRATEGIES

PREMIER WEALTH TACTICAL & PREMIER WEALTH TACTICAL CORE

Large-cap tech stocks have been on a tear since March, but we finally saw our first meaningful pullback right before the Labor Day weekend. The tech-heavy Nasdaq corrected 11% in six days, with many leading stocks being hit especially hard.

The markets had marched higher throughout August, even seeing, to the surprise of many, an acceleration in gains in the second half of the month. In the context of that extreme buying frenzy, the sharp selling in early September can be viewed as a positive – a healthy pullback that helps taper the excessive speculation we have seen in tech stocks.

With valuations rivaling only what we have seen in the dotcom bubble, it is probably wise to be somewhat cautious despite the unprecedented support from both the fiscal and monetary side. In addition, we are now in September, which tends to be the most volatile month of the year. We also have what will likely be a very heated election coming up.

The big question, obviously, is whether this is the beginning of something more serious, or simply a healthy pullback. The market, especially in large-cap techs, has exhibited some bubble-like behavior, and that should be noted. Leadership has been very narrow and the price appreciation relentless. The Nasdaq has made an incredible dash right off the March lows, without a meaningful decline until earlier this month.

The concentration among tech Large Caps has created some major extremes. Today, Apple is larger than all of the Russell 2000 small caps combined! While it seems unfathomable that this market can go higher, if this is a bubble, it can go on for longer. As Maynard Keynes said, “markets can remain irrational longer than you can remain solvent.” In other words, do not bet against bubble runs in the short term.

Our perspective has been to take a more measured approach whereby we participate, but with a healthy dose of caution.

Sharp corrections followed by sharp recoveries are emblematic of bubble-like environments. There is no arguing that the current correction we are seeing has been rather abrupt. It is not uncommon to see a full recovery to new highs in just two to four weeks following these sharp corrections.

Should there be one; the pace of a full recovery will yield another clue as to the type of market we are experiencing. If this is ultimately a top, history also suggests that we will see significant attempts to make new highs which fail. That action creates what we call a topping process and should send us a warning sign.

It is not hard to build a case for volatility, given valuations in nosebleed territory, an uncertain election with the major tax consequences that follow, and a traditionally bad time of year for stocks. In addition, all that comes with the backdrop of one of the largest economic declines in history caused by a pandemic.

The bullish case continues to rely on strong recovery hopes but most heavily on keeping the stimulus flowing, and speculation remaining rampant. “Don’t fight the Fed” is an old saw on Wall Street. It has never been more apt than during the last decade. Ultra-low interest rates and large asset purchases have spurred asset prices to record heights.

We will continue to monitor the action closely. While it is never easy to sit through any type of a correction, there are enough signs that give credence to the presence of a bubble-like environment. That opens the possibility that stocks can go higher and for longer than most people would expect. Obviously, one can never be sure. We do have a healthy dose of caution, as the bearish case is as clear as day.

Should the facts change, we will too. Whether that means increasing or decreasing our exposure levels, we will let the market tell us.

TACTICAL OPPORTUNITY

The model still holds a percentage in cash as the narrow strength in the market has meant fewer buy signals. Even with recent profit taking, it has been a good run for the mega caps like Apple, Amazon, Alphabet, and Walmart. Microsoft has been slightly down, and there has been some lag from healthcare holdings. Recent purchases have been directed away from the technology mega caps.

FULLY INVESTED

ETF SECTOR ROTATION

The markets have been on more of a wild ride, unsure if they want to have a rotation, or stick with the leadership in Growth and Technology. We have seen this several times over the past several months.

Since the start of August, this has led to a strange mix of winners. The Growth-oriented Consumer Discretionary, where Amazon is found, and Communications (e.g., Alphabet, Facebook) have outperformed. However, so have the more defensive Consumer Staples (just barely), with hopes of a global recovery in Materials and Industrials.

The recent sell-off notwithstanding, Tech has essentially mimicked the market over the past six weeks. The Energy sector has continued to lag. The model saw a light reduction in its Healthcare holdings over the past month.

For the broad markets, Value posted a rare victory over Growth. Will the trend hold? It is too early to tell, but no buy signals yet.

Globally, Internationals have lagged slightly. We recently opened a position in Emerging Markets, which has been positive but slightly behind the U.S. The model continues to prefer the U.S. to Europe.

EQUITY GROWTH AND VALUE

Though bumpy, tech-oriented Growth names still have had some of the best runs since the start of August. Names like Nvidia, Apple, Facebook, and Chipotle had nice runs, as did companies such as Caterpillar and others in Industrials and Materials. The model still has a focus on Growth, but recent swaps have been aimed at adding a Value hedge to the portfolios.

EQUITY GROWTH OPPORTUNITY

The portfolio endured some volatility as the Technology sector took a quick and needed pullback, affecting our overweight Technology holdings. However, we have not had any holdings trigger a sell and the portfolio has remained rather constant. If we see a breach in support or deterioration in the market leadership, we will not hesitate to tinker with the portfolio allocation. At this point, we are watchful yet patient with the exposure to the leading, yet volatile, Technology sector.

EQUITY DIVIDEND INCOME

Some steady, relative moves from a variety of dividend holdings have helped, notably Broadcom, UPS, and Target. Weakness has been noticeable from Energy holdings, but the model remains relatively light in that sector. With less Technology, the dividend strategy has offered a nice hedge as the market decides if it wants to switch directions in terms of leadership.

For a full description of each strategy, please click here.

Best regards,

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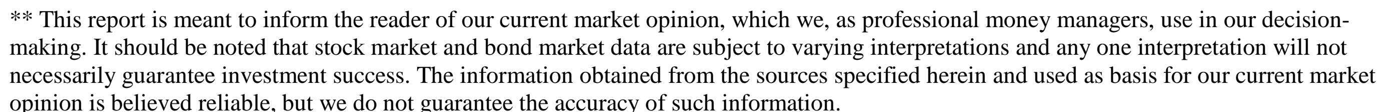

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