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PEAK CAPITAL MANAGEMENT

Professional Investment Management

BLOG POST

Analyst Corner
Part 1
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Macro View – Evergrande Fundamentals

On Monday September 20th, the S&P 500 fell by more than 75 points or -1.69% after fears that the world's most indebted property developer, China Evergrande Group, was on the brink of defaulting on its loans. Some say that the financial fiasco China is facing with Evergrande will largely remain contained in China, which was reiterated by Federal Reserve Chair Jerome Powell, who expressed that the United States has limited exposure to Evergrande's debt and will likely not experience any spillover dangers. While the Evergrande situation in China is on every investor's mind, the reality is that stock market valuations are overstretched, and many believe the market is long overdue a decline. Yardeni Research's weekly look at stock-market fundamentals noted that the S&P 500's 20.8 forward price-to-earnings (P/E) multiple remained near levels last seen ahead of the dot-com crash. The index's price-to-sales (P/S) multiple of 2.8 is as high as it has been since data was first available in 2004. Adding Evergrande to the equation when investors are already concerned about proposed tax increases, the debt crisis, and inflation results in more uncertainty around market direction. And unfortunately, conventional wisdom says that uncertainty is detrimental for markets.

Taking Stock – Value Back in Favor?

Historically, the stock market has performed poorest during the month of September and is often dubbed the "September Effect." As treasury yields pushed higher after hawkish sentiment from the Federal Reserve, we saw several technology companies' stock prices drastically decline. As of 9/28/2021, iShares S&P 500 Growth ETF (IVW), which screens based on sales growth, earnings growth to price, and momentum, was down -5.19% MTD (YCharts). Not surprisingly, many of the largest holdings include some of the FANG names: Facebook, Amazon, Netflix, and Alphabet. Consequently, over that same period, the iShares S&P 500 Value ETF (IVE), which screens companies based on price to book value, price to earnings, and price to sales, was only down -2.49% (YCharts). If yields continue to rise, this could weigh heavily on growth companies, specifically those in the technology sector, and result in further declines. With interest rates and energy prices rising once again, value names may experience another phase of outperformance.