LAWSON KROEKER

As we see it

March 2021

"There is nothing like higher prices to attract more buyers. In department stores you mark merchandise down to move it. On Wall Street you mark it up.
- Michael Metz*"*

Is it 1999 again?

Similar to the late '90s, the market continues to reach new highs, driven by a select group of companies. New businesses and active traders are racing to the market. In April 1999, we saw much of the same behavior as we wrote in our ***As We See It***:

> *"The question of where the market is has to do with what you look at. The movements of the major averages are deeply influenced by well-known companies that have large capitalizations. For example, the 50 largest companies in the Standard & Poor's 500 Stock Index accounted for 54.9% of its total value as of December 31, 1998…This type of situation where performance is chasing performance becomes self-reinforcing as investors, including mutual funds, are channeling their funds to a shrinking list of recent winners."*

Almost 22 years later we see many of the same characteristics in today's market. The largest companies dominate the market's performance and the market once again lacks breadth in performance. In some ways, the lack of diversification from the S&P 500 Index may be more pronounced today. Strong momentum has pushed the top five companies to comprise almost one quarter of the S&P 500's total valuation, and momentum is the strongest in the technology sector, which has seven of the top ten names in the S&P 500.

In 1999, the top 10 companies in the S&P 500 Index encompassed less than 24% of the index's overall weight and outperformed the remainder of the index by less than 8%. Today, the top 10 names are valued substantially higher, make up 32% of the index and outperformed the smaller constituents by over 22% in 2020. In fact, the Russell 1000 Growth Index outperformed the Russell 1000 Value Index by 36% in 2020 - the largest spread since 1979.

It is still too early to tell if the large-cap technology companies will continue their outperformance. 2020 was certainly a year where momentum's self-reinforcing mechanism was alive and well. However, an interesting observation is to look at how the top performers in 1999 fared in the years ahead. The top 10 companies in 1999 saw a harder fall to earth the following three years (2000-2002) as momentum eventually lost its steam. Value stocks held their ground far better than technology and mega cap holdings from 2000-2002.

Comparison of 1999 vs 2020 Markets

S&P 500 - 1999

	Top 10 Holdings	Remaining Holdings
Median Market Cap ($B)	177.9	6.6
Median Price / Earnings	21.1	17.7
Relative Weight	23.6%	76.4%
Average Return (1999)	30.7%	22.8%
Average Return (2000-02)	-18.2%	1.4%

S&P 500 - 2020

	Top 10 Holdings	Remaining Holdings
Median Market Cap ($B)	778.0	25.4
Median Price / Earnings	36.8	25.3
Weight in Index	32%	68%
Average Return (2020)	31.0%	8.7%

Initial Public Offerings (IPOs) have also reemerged at a rate not seen since the late '90s as new companies were enticed by the market offering higher valuations and requiring less operating history. In the late '90s, new companies went public at such a high rate that critics quipped all that was needed was a business plan scribbled on a napkin. We currently have another strong wave of technology IPOs combined with a new group called Special Purpose Acquisition Companies (SPACs). If IPOs once had proving their operating acumen easy, SPACS may have it even better as they go public first and promise to deliver a business plan later. As empty holding companies armed with little more than a quarterback and cash, SPACs are proliferating and earning increasing premiums on their cash balances before an operating company is produced.

Online trading created a new phenomenon in the '90s that resonates today. Discount brokerage firms offered retail investors more direct access to the stock market in the 1990s with lower trading commissions. Online research aimed at retail investors as well as day trading thrived. Given the market's positive momentum in the large technology companies at the time, it was hard to go wrong for many retail investors, at least for a while. As the technology bubble burst at the turn of the millennium, day trading left many humbled and volumes diminished. Today, the market's momentum is back and has enticed a new crop of retail investors who are armed with ideas from online forums. This new group of retail investors have assimilated in such size that they have exploited pockets of the market once thought to only be the realm of institutional investors. It remains too early to test the strength of their resolve, but one must wonder how many of these new entrants will endure if momentum fails to deliver easy profits.

Capital often flows to where the lights shine the brightest. As we write this over 20 years later, the largest technology firms are again outperforming handily, and new market participants are thriving from IPOs to SPACs to day traders. Is this time any different?

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