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Delta Insights
a weekly commentary on investing

August 28, 2020

Crossing the Karman Line

Occasionally, markets rocket higher. In 1998, between July 21 and October 8, the NASDAQ lost about 33% of its value. The NASDAQ then appreciated by 278% from about 1,357 to 5,132 on March 10, 2000. The fuel was investor enthusiasm for the endless growth possibilities of the Internet.

At some point in 2000, the NASDAQ metaphorically crossed the Karman Line. The Karman Line is the boundary between Earth's atmosphere and outer space, roughly 50 to 60 miles above sea level. In physics, it is where aerodynamics stop and astronautics begin. For investors, the valuation support for the NASDAQ disappeared and investor irrational exuberance began freeing stocks of the restrictions of valuation gravity. Over the next couple of years, growth concerns and valuation issues reemerged. By October 2002, the NASDAQ depreciated by about 80%.

Is history repeating itself? From the February high to the March low 2020, the NASDAQ declined by about 33%. Since the low, it has launched higher with accelerating velocity. We are just five months past the low and the NASDAQ has appreciated by about 75% from the bottom. Apple went public in 1984. It took about 35 years to reach $1 trillion market capitalization. Less than a year after reaching $1 trillion, the valuation is now $2.1 trillion. Apple is typical of many very large capitalization technology stocks today. Investor enthusiasm is being driven partly by the COVID-19 virus accelerating economic migration onto the Internet.

Gravity is always present. Whether it is aerodynamics, astronautics or the stock market, what goes up generally comes down. As valuations rise, so does risk. Jumping over the high expectation bar is harder than stepping over the low bar.

Stock risk also tends to rise with stock concentration. Facebook, Amazon, Apple, Microsoft and Google now represent 37% of the Russell 1000 growth index. This is the highest level of index concentration since 1995. There have been several trading days in the past few weeks when the market attained new highs with more stocks down than up.

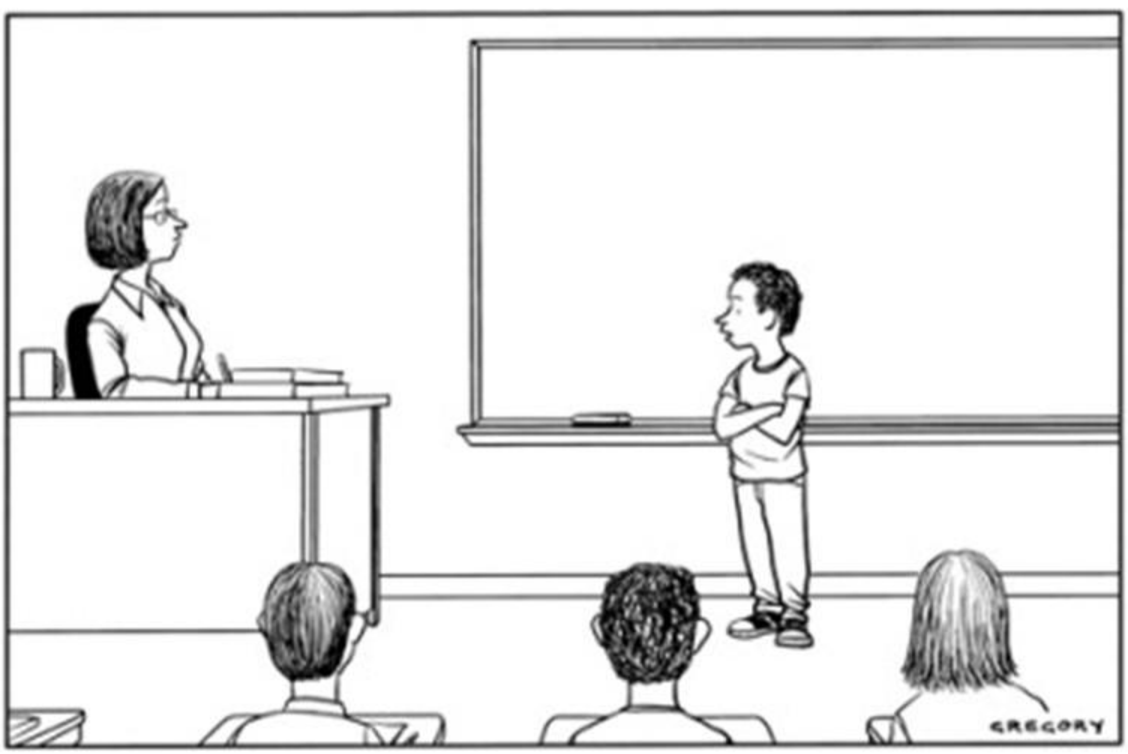
Does the rapidly rising market and elevated valuations mean the NASDAQ should be sold now? Not necessarily. One of most persistent factors in stock investing is momentum. The market rarely demonstrates this much momentum. Interest rates are at all-time lows. In prior *Delta Insights*, we have talked about how low rates help raise multiples. The current Baa Corporate Bond Yield (at 3.32%) suggests a market multiple of about 30x. Fundamentally, COVID-19 is significantly accelerating the secular trend towards virtual commerce. According to *The Wall Street Journal*, 29.1% of all U.S. retail sales in the second quarter were through Walmart, Amazon, Target, Home Depot, Lowe's and Costco. The gains came at the expense of small business and traditional brick and mortar stores that do not have a great online presence.

The very large technology companies today have much better business models than the leading companies of twenty years ago. Today's market leaders are often near-monopolies with very low capital requirements and high margins. The return on capital (ROC) of companies like Microsoft, Facebook, Google and Amazon is inherently higher than that of capital-intensive companies like Caterpillar, Ford, Exxon, etc. Software usually has much higher margins than manufacturing. The very high margins create significant cash flow which is used to reinvest in the business or buy emerging competitive companies which strengthens the monopoly and stability of the margins.

This week, the market is bullish with the S&P 500 and NASDAQ achieving new all-time highs. As price appreciates and breadth diminishes, risk rises. Delta Investment Management specializes in risk-mitigation through active account management. We seek to participate in bullish markets and avoid major bearish markets.

Give Us a Call Today

We have unique and sophisticated investment methods that seek to capture the stock market's gains while minimizing drawdowns in bear markets. If you would like to learn more about how we manage money, we invite you to give us a call at **(415) 249-6337**, visit www.deltaim.com or email us at info@deltaim.com.



"Anyone following me on Twitter already knows what I did this past summer."

Delta Stock Market Dashboard

MARKET SENTIMENT IS

BULLISH

THIS WEEK'S NUMBER IS

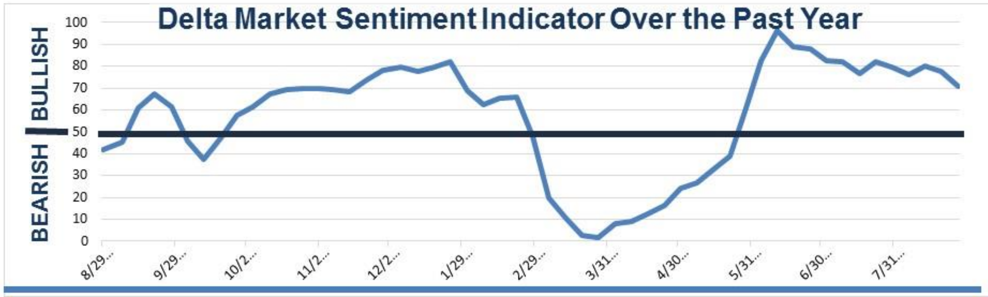
70.6

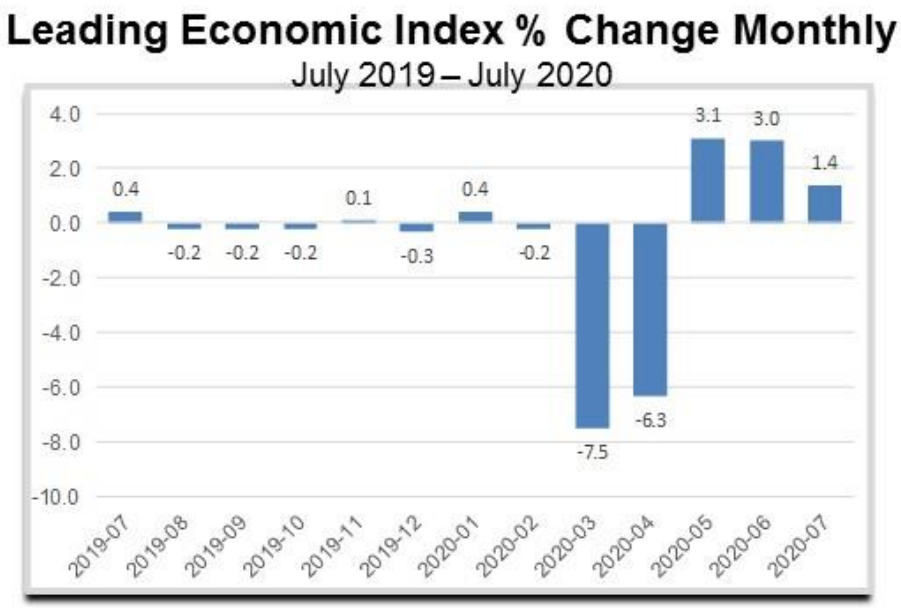
Our technical indicator decreased from 77.6 to 70.6 this week

INDICATOR STATISTICS

Consecutive Bullish Weeks:	14
Cycle Inception Date:	5/28/2020
Range:	60.9 – 96.2
Mean:	80.2
Bullish Weeks YTD:	22
Bearish Weeks YTD:	13
*S&P 500	14.9%
*DJIA	12.4%
*NASDAQ	24.3%

** Percentage change during current cycle*





Source: The Conference Board, updated monthly – last update 8/20/2020