Alpesh Patel's Newsletter

Exclusively for ShareScope Alpesh Patel Special Edition Subscribers
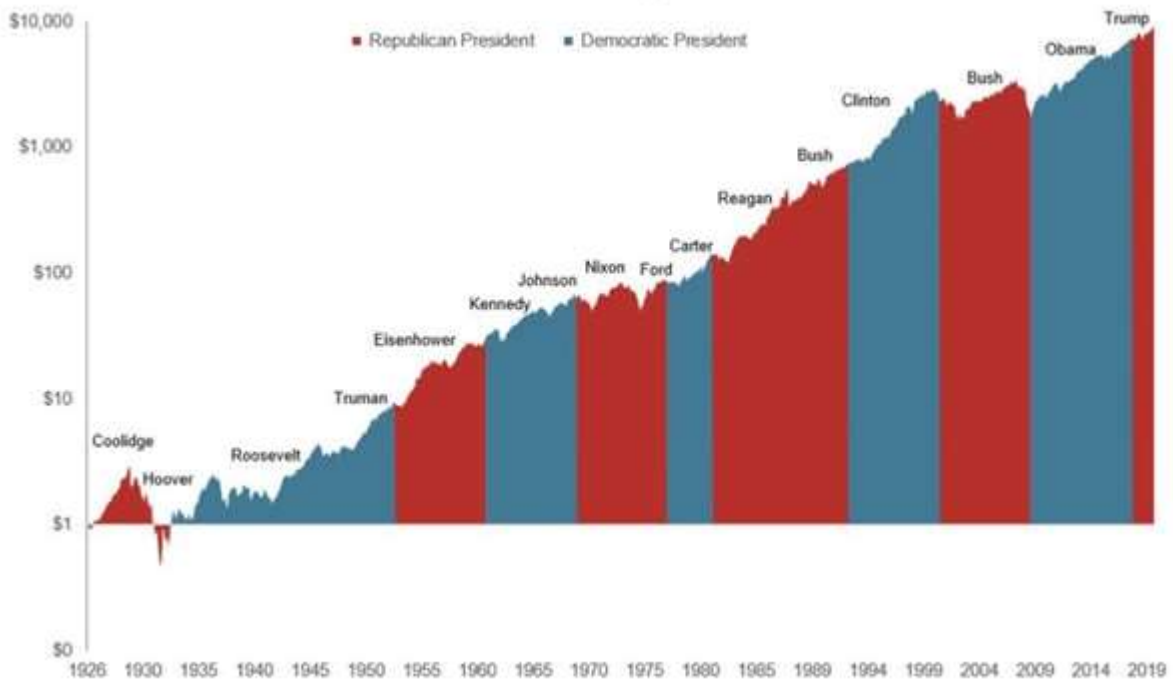
11 November 2020

Overview
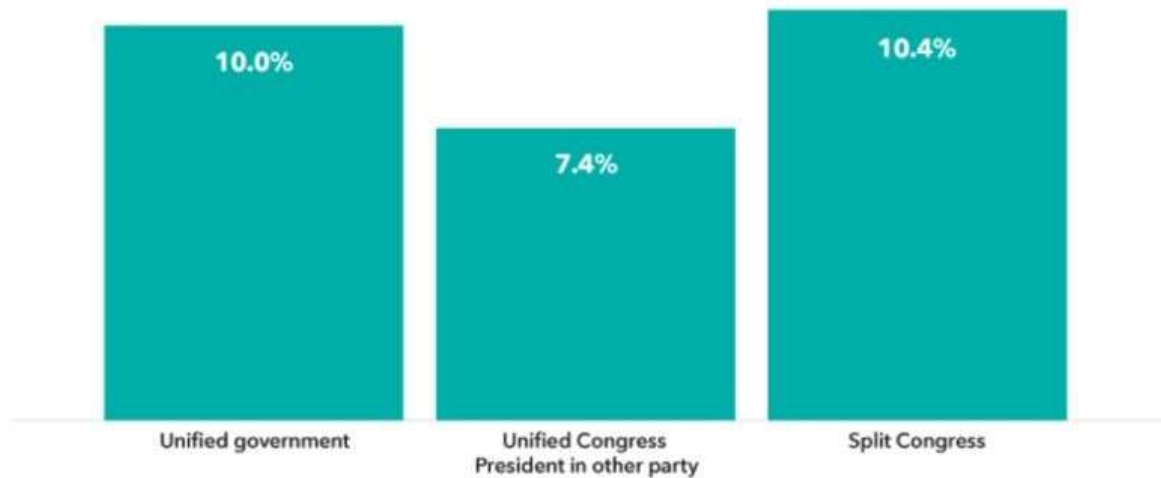
Too early to say if the FTSE has bottomed.

Some data on the US election: (I also gave my view on banking stocks and how invest past the election on the BBC: https://youtu.be/WjMkmR5HshI?list=PLAlwg0f72DYanrzS-VYUhA6BZfvdLMZHZ

Growth of a Dollar Invested in the S&P 500: January 1926–December 2019

S&P 500 Index average annual return (1933-2019)

Sources: Capital Group, Strategas. As of 31/12/19. Unified government indicates White House, House and Senate are controlled by the same political party. Unified Congress indicates House and Senate are controlled by the same party, but the White House is controlled by a different party. Split Congress indicates House and Senate are controlled by different parties, regardless of the White House control.

Just the Status Quo
U.S. stocks have been outperforming for a decade now

Normalized As Of 11/05/2010 · ■ MSCI USA Price Return USD Index - Last Price
■ MSCI ACWI Excluding United States Index - Last Price

Source: Bloomberg

Dow Jones Industrial Average Performance		
When U.S. government has:	% gain/annum	% of time
Democratic President, Republican Congress	9.1%	10.1%
Democratic President, Split Congress	10.4%	3.4%
Democratic President, Democratic Congress	7.2%	33.4%
Republican President, Republican Congress	7.3%	23.5%
Republican President, Split Congress	-2.9%	11.5%
Republican President, Democratic Congress	2.4%	18.4%

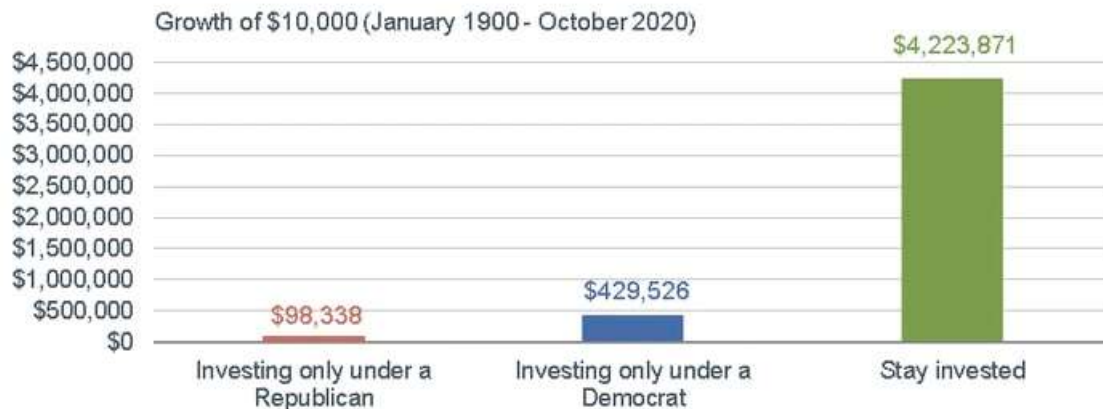Source: Charles Schwab.

S&P 500 Price Index

Calendar year returns

	Average	% of time
Republican	12.9%	11%
Democrat	9.8%	27%
Divided gov't	7.8%	62%

Real GDP

Year-over-year % change, annual

	Average	% of time
Republican	2.8%	11%
Democrat	4.0%	27%
Divided gov't	2.8%	62%

Staying Invested vs. Investing in Single Party

Growth of $10,000 (January 1900 - October 2020)

- Investing only under a Republican: $98,338
- Investing only under a Democrat: $429,526
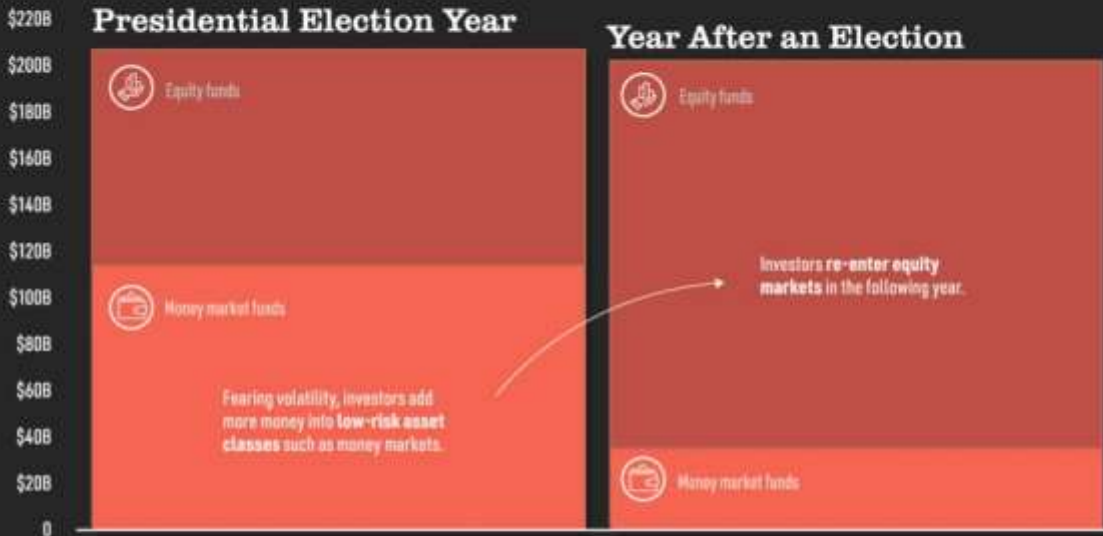- Stay invested: $4,223,871

Source: Charles Schwab, Bloomberg, as of 10/2/2020. For illustrative purposes only. The above chart shows what a hypothetical portfolio value would be if a hypothetical investor invested $10,000 in a portfolio that tracks the Dow Jones Industrial Average on 1/1/1900 under three different scenarios: a Republican presidential administration; a Democratic presidential administration; or staying invested in the market throughout the entire period noted. Chart does not reflect effects of fees, expenses or taxes.

SHOULD A **U.S. ELECTION** AFFECT YOUR ASSET MIX?

Volatility rises during election season, causing many investors to reduce their portfolio's risk exposure. Here's why sticking to your long-term asset mix is the smarter decision.

Average Net Fund Flows 1992-2019

Presidential Election Year

Equity funds

Money market funds

Fearing volatility, investors add more money into **low-risk asset classes** such as money markets.

Year After an Election

Equity funds

Investors **re-enter equity markets** in the following year.

Money market funds

Scale: $220B, $200B, $180B, $160B, $140B, $120B, $100B, $80B, $60B, $40B, $20B, 0

This decision may be flawed.

Source: Morningstar (Dec 2019)

On average, the S&P 500 has generated positive returns in election years regardless of who won.
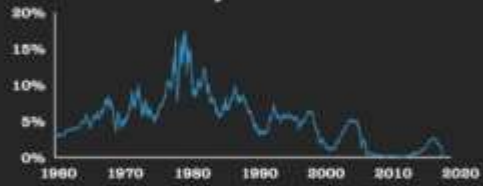
Average S&P 500 Return in Presidential Election Years 1928-2016

New president is elected	9.3%
Incumbent president win	13.4%
All election years	11.3%
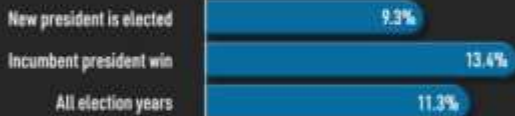
Source: Morningstar (Dec 2019)

Meanwhile, yields on money market securities have been deteriorating since the 1980s.

1 Year U.S. Treasury Bill Rates

Chart axis: 20%, 15%, 10%, 5%, 0% — years 1960, 1970, 1980, 1990, 2000, 2010, 2020

Source: Macrotrends (Oct 2020)

Investors may be tempted to deviate from their long-term asset mix during election season. Given the positive performance of equities during these periods, doing so may compromise future results.

MARKETS IN A MINUTE

INVESTMENTS   VISUAL CAPITALIST

Election year	President	Dow Jones Industrial Average Peformance (%)			
		Post-Election Year	Mid-Term Year	Pre-Election Year	Outgoing Election Year
1900	William McKinley	-8.7	-0.4	-23.6	42.6
1904	Theodore Roosevelt	37.8	-2.3	-37.7	46.6
1908	William Taft	15.0	-17.8	0.2	7.7
1912	Woodrow Wilson	-10.3	-30.7	81.7	-4.2
1916	Woodrow Wilson	-21.7	10.5	30.5	-32.9
1920	Warren Harding	12.3	21.5	-2.7	26.2
1924	Calvin Coolidge	30.0	0.3	27.7	49.5
1928	Herbert Hoover	-17.2	-33.8	-52.7	-22.6
1932	Franklin Roosevelt	63.7	5.4	38.5	24.8
1936	Franklin Roosevelt	-32.8	27.7	-2.8	-12.6
1940	Franklin Roosevelt	-15.4	7.6	13.8	11.8
1944	Franklin Roosevelt	27.0	-8.1	2.2	-2.1
1948	Harry Truman	13.1	17.4	14.4	8.4
1952	Dwight Eisenhower	-3.8	44.0	20.8	2.3
1956	Dwight Eisenhower	-12.8	34.0	16.4	-9.3
1960	John Kennedy	18.7	-10.8	17.0	14.6
1964	Lyndon Johnson	10.9	-18.9	15.2	4.3
1968	Richard Nixon	-15.2	4.8	6.1	14.6
1972	Richard Nixon	-16.6	-27.6	38.3	17.9
1976	Jimmy Carter	-17.3	-3.1	4.2	14.9
1980	Ronald Reagan	-9.2	19.6	20.3	-3.7
1984	Ronald Reagan	27.7	22.6	2.3	11.8
1988	George Bush	27.0	-4.3	20.3	4.2
1992	Bill Clinton	13.7	2.1	33.5	26.0
1996	Bill Clinton	22.6	16.1	25.2	-6.2
2000	George W. Bush	-7.1	-16.8	25.3	3.1
2004	George W. Bush	-0.6	16.3	6.4	-33.8
2008	Barack Obama	18.8	11.0	5.5	7.3
2012	Barack Obama	26.5	7.5	-2.2	13.4
2016	Donald Trump	25.1	-5.6	22.3	N/A
	Ovearall average	6.7	2.9	12.2	7.7
	Republican average	5.2	3.4	5.6	10.5
	Democrat average	8.4	2.4	19.8	4.8

Source: Charles Schwab, Bloomberg, S&P Dow Jones Indices, as of 12/31/2019. For illustrative purposes only.

Macro Outlook 2021
A V(accine)-Shaped Recovery
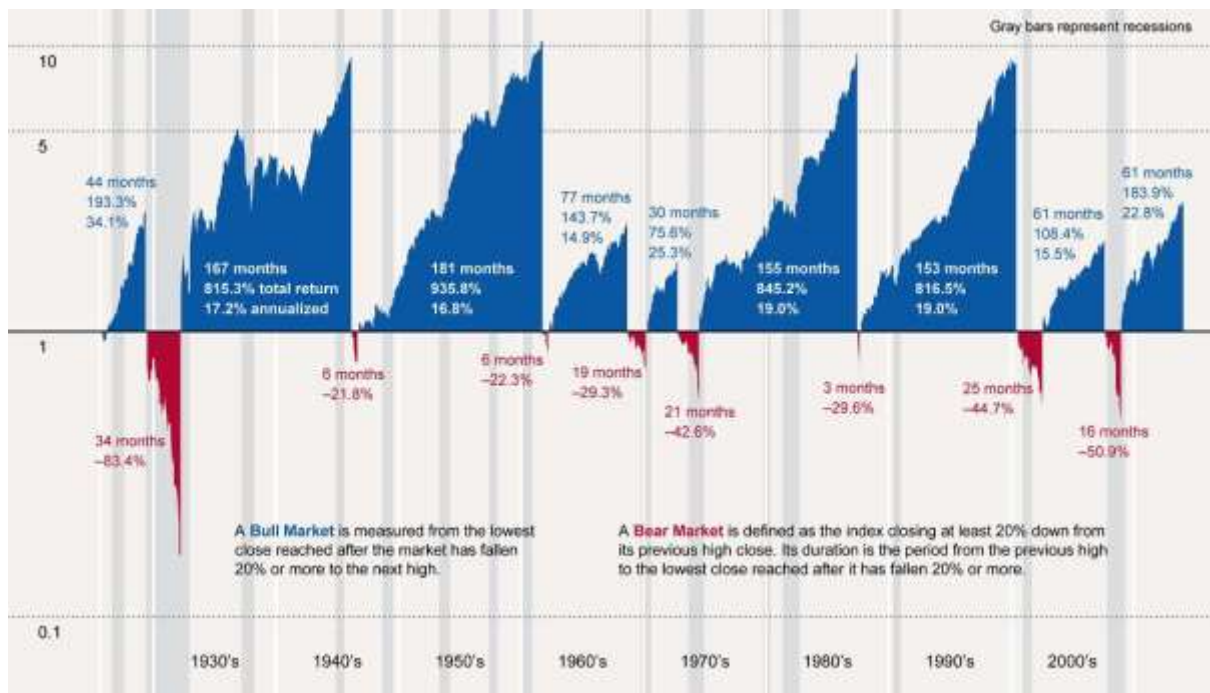Jan Hatzius, Daan Struyven, Sid Bhushan, Daniel Milo – 07 Nov 2020

Following the results of the US election, Goldman Sachs Research has revised its projections for 2021 growth.

*GS forecast as of November 2020
Note: All forecasts calculated on calendar year basis.

Goldman Sachs

REAL GDP GROWTH PERCENT CHANGE YOY	2020*	2021
WORLD	-3.9	6.0
USA	-3.5	5.3
JAPAN	-5.3	3.3
EURO AREA	-7.2	5.3
Germany	-5.8	3.7
France	-9.2	7.0
Italy	-8.7	6.0
Spain	-11.6	7.1
UK	-10.5	6.1
CHINA	2.0	7.5
INDIA	-8.9	10.0
RUSSIA	-4.0	5.0
BRAZIL	-4.6	4.0

Country	Population	NATIONAL DEBT	GDP-GROSS DOMESTIC PRODUCT	PUBLIC DEBT TO GDP RATIO	EXTERNAL DEBT TO GDP RATIO
USA	330,536,310	$27,221,506,814,210	$21,246,778,981,092	96.52%	122.33%
CHINA	1,439,018,309	$7,388,301,356,542	$14,572,935,176,276	50.70%	16.06%
JAPAN	126,568,201	$12,268,809,246,083	$4,539,957,937,703	270.24%	92.51%
GERMANY	83,852,312	$2,959,326,092,008	$3,760,493,181,249	78.69%	168.12%
U K	67,861,900	$3,526,478,277,229	$3,461,577,779,906	101.88%	286.74%
FRANCE	65,247,596	$3,043,843,692,462	$2,662,064,382,114	114.34%	250.29%
INDIA	1,377,944,969	$2,316,665,472,140	$2,906,050,938,196	79.72%	21.32%

I am not worried about debt. I buy stocks not to gamble, but to remove my concerns. My picks are companies which will not fall as far when the market does and rise when it rises.

Gray bars represent recessions

A Bull Market is measured from the lowest close reached after the market has fallen 20% or more to the next high.

A Bear Market is defined as the index closing at least 20% down from its previous high close. Its duration is the period from the previous high to the lowest close reached after it has fallen 20% or more.

Market drawdown	Historical Frequency
10%	Every 11 months
15%	Every 24 months
20%	Every four years
30%	Every decade
40%	Every few decades
50%	2-3 times per century

S&P 500 Index daily returns, Dec. 31, 1979, through Dec. 31, 2019

Thirteen of the 20 best trading days occurred in years with negative annual returns

Nine of the 20 worst trading days occurred in years with positive annual returns

Past performance is no guarantee of future results. The performance of an index is not an exact representation of any particular investment, as you cannot invest directly in an index.

Source: Vanguard.

The key question is which are the top stocks to rally with the vaccine.

To find the top stocks to rally with a vaccine I have used the following hypothesis:

- We should look for companies which before the pandemic were not in a decline. After all, even after the pandemic they would still fall.
- They should be companies which rose in the year before the market peaked ie upto 21st February 2020, because that's when the lockdown began (UK) and stocks fell for 4 weeks.
- They should be companies which fell during the month 21st February to 21st March 2020. That is they were impacted.
- They over the past 6 months have not recovered. Again, if they had, then there is no gain to be had.
- They should be otherwise healthy companies. We do not want ones on the brink of bankruptcy, since the vaccine implementation may seen them collapse. So for these companies I would look for ones with high Altman scores and good CROCI scores.
- Of course we want ones which have started rising now after the vaccine has been announced.

Introducing Altman Scores for Stocks

As this source says:

"The **Z-score formula for predicting bankruptcy** was published in 1968 by Edward I. Altman, who was, at the time, an Assistant Professor of Finance at New York University. The formula may be used to predict the probability that a firm will go into bankruptcy within two years. Z-scores are used to predict corporate defaults and an easy-to-calculate control measure for the financial distress status of companies in academic studies. The Z-score uses multiple corporate income and balance sheet values to measure the financial health of a company.

The Z-score is a linear combination of four or five common business ratios, weighted by coefficients. The coefficients were estimated by identifying a set of firms which had declared bankruptcy and then collecting a matched sample of firms which had survived, with matching by industry and approximate size (assets).

Altman applied the statistical method of discriminant analysis to a dataset of publicly held manufacturers. The estimation was originally based on data from publicly held manufacturers, but has since been re-estimated based on other datasets for private manufacturing, non-manufacturing and service companies.

The original data sample consisted of 66 firms, half of which had filed for bankruptcy under Chapter 7."

Introducing CROCI

This is a measure of cash flow. This source puts it like this:

Cash return on capital invested (**CROCI**) is an advanced measure of corporate profitability, originally developed by Deutsche Bank's equity research department in 1996 (it now sits within DWS Group).This measure compares a post-tax, pre-interest cash flow to the gross level of capital invested and is a useful measure of a company's ability to generate cash returns on its investments.

In principle, this ratio is similar to the ROE ratio, but CROCI is calculated on a cash basis and on an EV-basis, taking into account assets funded by all the company's security-holders. CROCI is calculated as the internal rate of return in a particular year of a company's gross post-tax cash flows after investing the gross capital invested over the total asset life of the firm. In principle, this should be equivalent to the ratio of the free cash flow of that year to the net capital invested, provided depreciation is calculated economically and the only capex is for maintenance.

Returns: For most sectors we analyse CROCI and focus on identifying Q1 CROCI stocks

Goldman Sachs

CROCI measures the cash flow companies generate on the gross cash invested in the business

Q1 CROCI stocks have delivered substantial outperformance over time
Total shareholder returns of companies in each sector-relative CROCI quartile
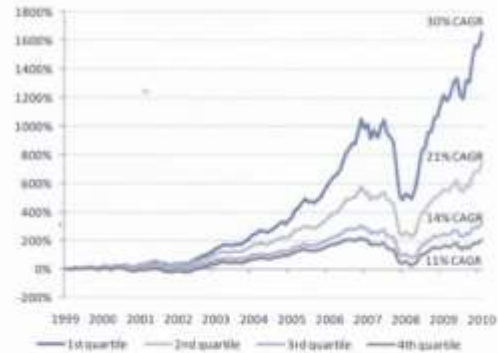
Source: Quantum database, Goldman Sachs Research.

Goldman Sachs Global Investment Research

The higher the CROCI, the more the ability of the ability of the company to generate cash and research above from Goldman Sachs shows those companies perform the best.

Risk Warning

Of course there remains a risk warning. I don't like gambling on how long it will take to issue a vaccine and get it out there. And there is another problem. No measure of a company is fool proof. Add to that that if 75% of people only take the vaccine and it is 90% effective, then we still have a sizeable group, maybe around a third, who are unprotected.

Beware too, that stocks which have lept in the past two days, may see some profit-taking before the strategy of them eventually resuming their pre-lockdown trend resumes.

Which Stocks Don't Make the Cut

For instance JD Sports, Computacenter, Kainos, does not make our list because it's already rallied and benefitted from home gym clothes buyers after the initial dip from the virus. That's not to say those companies may not rise for other reasons not linked to the virus. Here I am looking at virus strategies.

Carnival didn't make the cut because there are other companies with better financials.

Which Stocks to Rally with the Vaccine? FTSE 350

So with all the above in mind. Which will do well potentially?

From the FTSE 350, I find:

Countryside Properties [CSP], Morgan Sindall [MGNS], 4imprint Group [FOUR],

Which Stocks to Rally with the Vaccine? US Shares 500

And using the same principles these stood out for me in US stocks:

American International Group [AIG], Chubb [CB], CDW, Globe Life [GL], Hartford Financial [HIG], Trandign [TDG].

Which Stocks to Rally with the Vaccine? Nasdaq 100

Here I found Fiserv [FISV]. Again, that's not to say others wont do well on other strategies.

Which Stocks Look Good Generally?

The vaccine, US elections, Brexit are all big news items and that means gambling around them is not wise. Instead a proper selection method should include a diligent approach to examining valuation, growth, income, performance, volatility, including CROCI, Sortino and Alpha.

For me these stocks stood out:

Medifast, Alphabet, Apple, CDW, Crocs, Garmin, IMCD, Microsoft, UnitedHealth, Vipshop, Amazon, Amerisource, Costco.

Another useful reminder for those thinking of gambling around news:

WHY DOES TRADING LOOK LIKE GAMBLING TO 90% OF LOSERS?

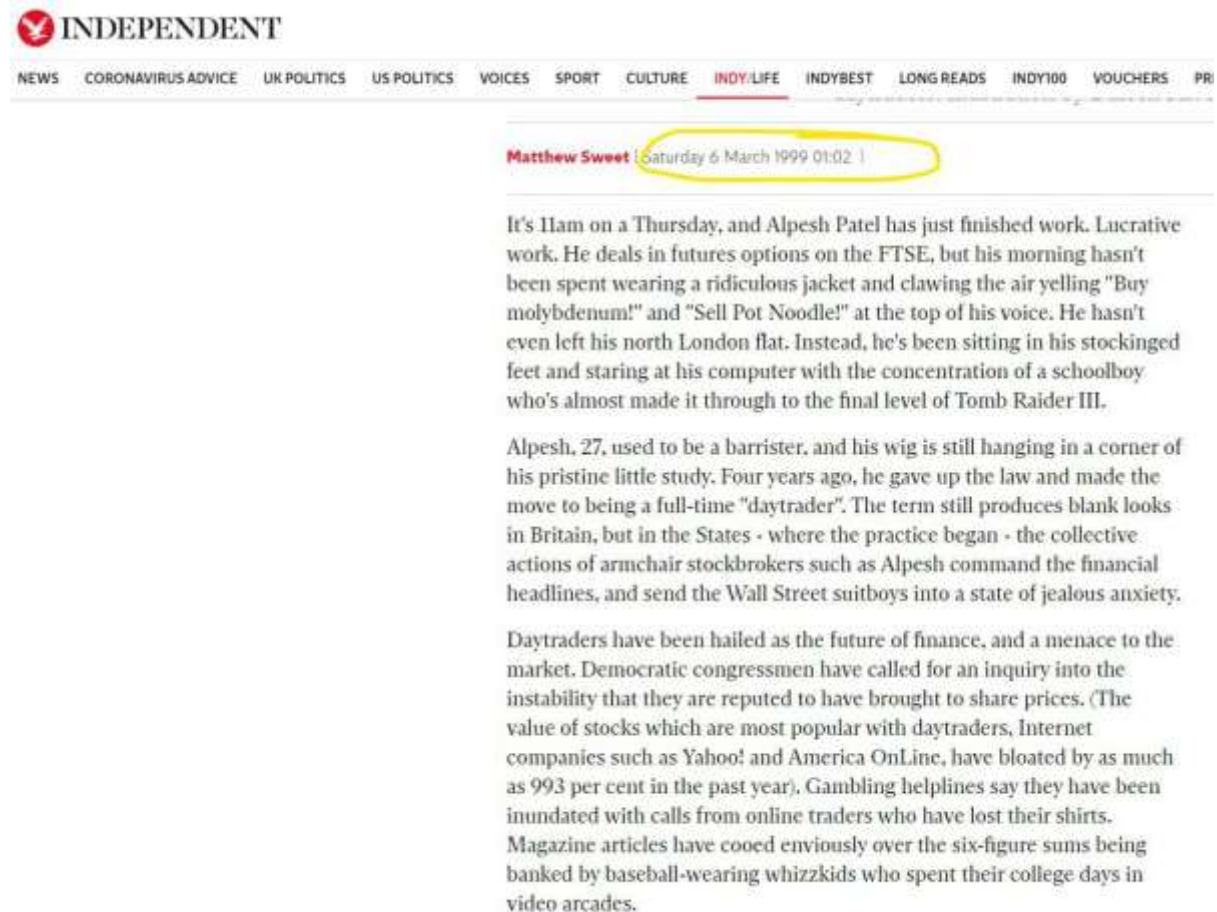| Trader	Gambler
Trades small position relative to capital	Trades big money relative to capital
Does a lot of small trades	Does a few big trades
Follows the trends established in the market	Steps in front of market reaction by guessing the news
Never adds to a losing position	Adds to a losing position
Starts small size in a trade and adds to it if trend makes it more profitable	Starts big, takes small profit
Places a stop loss just outside range of market noise, so clearly knows when strategy not working	No stop loss or very far away
A string of losing trades would not impact the account much	A string of even 3 losses would see account down 10-50%

Alpesh Patel

Help Page

Some interesting things you might like:
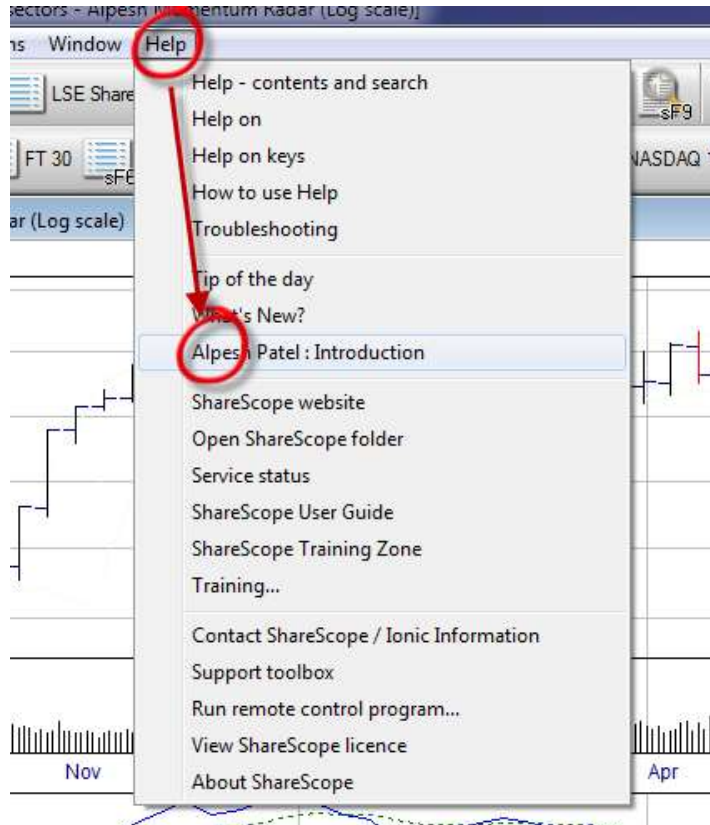
Personal

Personal? Well no travel. I can show you a bunch of pictures of me on zoom calls? How about some more past hits?

INDEPENDENT

NEWS   CORONAVIRUS ADVICE   UK POLITICS   US POLITICS   VOICES   SPORT   CULTURE   INDY/LIFE   INDYBEST   LONG READS   INDY100   VOUCHERS   PR

Matthew Sweet | Saturday 6 March 1999 01:02 |

It's 11am on a Thursday, and Alpesh Patel has just finished work. Lucrative work. He deals in futures options on the FTSE, but his morning hasn't been spent wearing a ridiculous jacket and clawing the air yelling "Buy molybdenum!" and "Sell Pot Noodle!" at the top of his voice. He hasn't even left his north London flat. Instead, he's been sitting in his stockinged feet and staring at his computer with the concentration of a schoolboy who's almost made it through the final level of Tomb Raider III.

Alpesh, 27, used to be a barrister, and his wig is still hanging in a corner of his pristine little study. Four years ago, he gave up the law and made the move to being a full-time "daytrader". The term still produces blank looks in Britain, but in the States - where the practice began - the collective actions of armchair stockbrokers such as Alpesh command the financial headlines, and send the Wall Street suitboys into a state of jealous anxiety.

Daytraders have been hailed as the future of finance, and a menace to the market. Democratic congressmen have called for an inquiry into the instability that they are reputed to have brought to share prices. (The value of stocks which are most popular with daytraders, Internet companies such as Yahoo! and America OnLine, have bloated by as much as 993 per cent in the past year). Gambling helplines say they have been inundated with calls from online traders who have lost their shirts. Magazine articles have cooed enviously over the six-figure sums being banked by baseball-wearing whizzkids who spent their college days in video arcades.