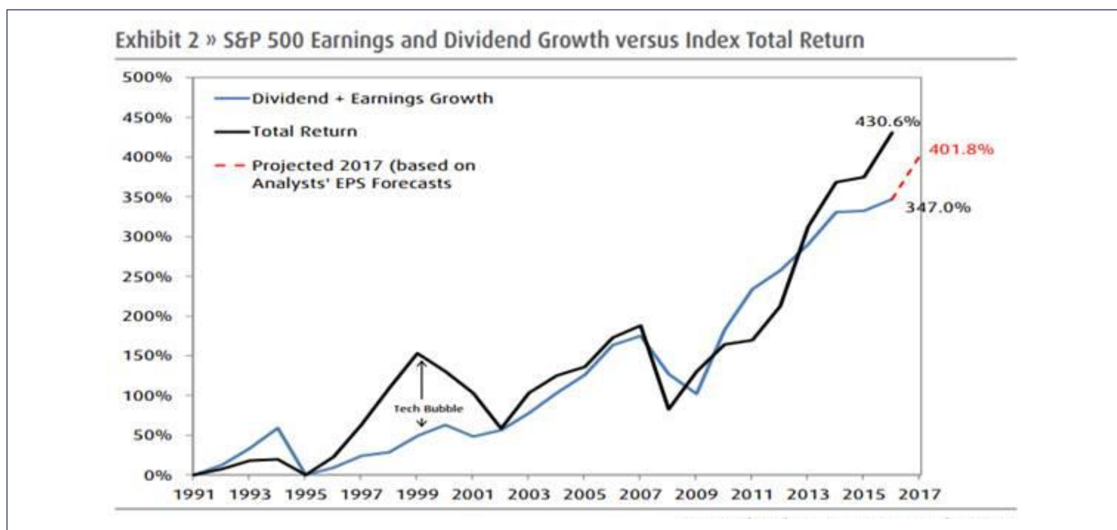
Market Recap

Focus in FAANG

Source: FactSet

With technology shares leading the market, the media has put considerable emphasis on the FAANG stocks (Facebook, Apple, Amazon, Netflix, and Google) as the primary driver of recent returns. These companies compete in a variety of industries, but they all possess technology-focused DNA and are beneficiaries of (and agents of change in) huge secular shifts that are reshaping the world around us. Market pundits may be prone to hyperbole, but the focus on FAANG is understandable – this privileged club includes 4 of the 5 largest companies (by market capitalization) in the S&P 500 and, collectively, account for a little over 10% of the overall index weight. While most agree that these mega-cap stocks have substantial runway for long-term growth, some nervous investors have begun to fret that FAANG performance has led to a top-heavy market. Those concerned may take comfort that an equal-weighted version of the S&P 500 (which disregards market capitalization) is up nearly as much in 2017 – equal-weighted returns are roughly 7% YTD vs. 9% for the S&P 500.

Earnings are Ultimate Driver of Equity Returns



Source: Bloomberg, BMO Private Bank

While equity markets can be subject to strong fluctuations caused by a variety of factors, the long-term performance of an equity index will be predominantly driven by the underlying earnings growth of the companies comprising that index. Shorter-term deviations from this relationship are typically expressed through increases or decreases to market P/E ratios – the relative value investors are assigning to a given level of earnings. Given consensus earnings growth estimates of 10.6% and 11.3% in FY17 and FY18, alongside the current environment of low inflation and low interest rates warranting higher P/E multiples, current valuation levels are relatively stable and reasonable. That being said, earnings will need to meet consensus expectations in order to maintain current P/E levels and see strong returns moving forward.

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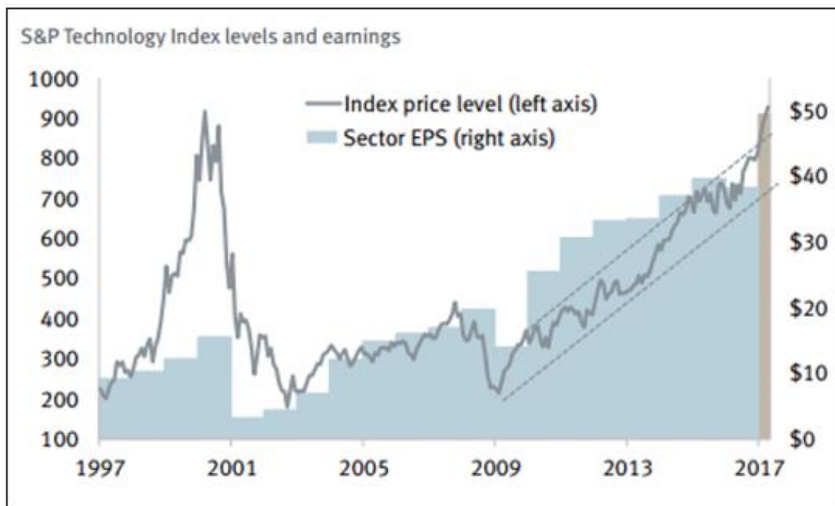
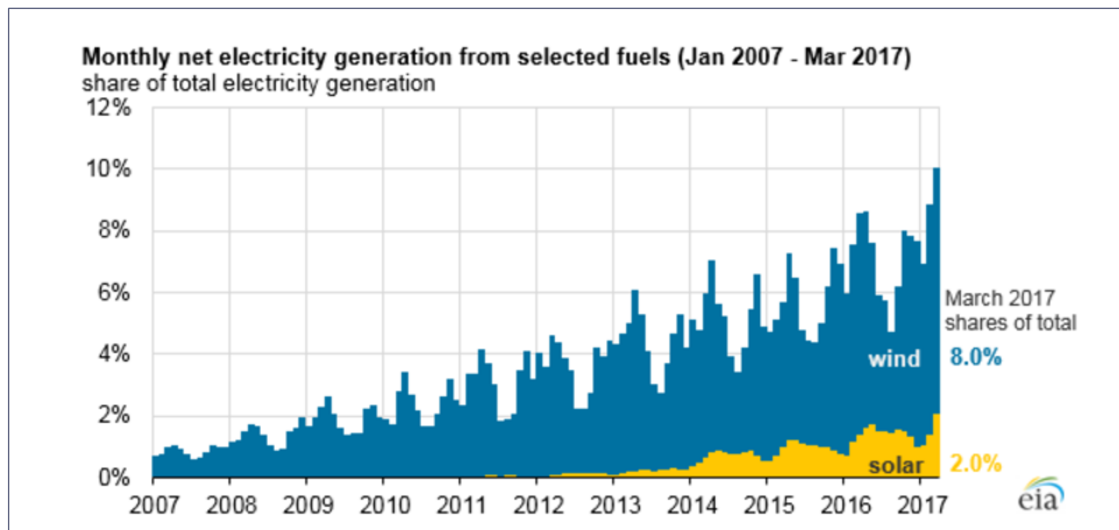
Dot.com Bubble 2.0? Not So Fast…



Source: RBC Wealth Management, Bloomberg

The S&P 500 Technology Index recently passed the peak market price achieved in 2000, but there is little debate that the fundamental backdrop is much healthier today. The Dot.com era of the late 1990s was characterized by a feeling that technology was going to dramatically change the world, and manifested itself in irrational exuberance. The irony is that widely-held belief in the power of technology was directionally right – over the past 25 years no sector has performed better – but investors at the height of the bubble were too quick to bless the underlying economics of unproven business models (think delivery service Webvan or online retailer Pets.com) and even more haphazard in the valuations they were willing to pay. In a sector notorious for the dramatic impact of disruptive forces, and with the benefit of hindsight, technology investors appear to have (re)learned one enduring lesson – in the long run, stocks follow earnings.

The Rise of Wind and Solar Power



Source: U.S. Energy Information Administration

Developed, in part, as a way to combat the sky-high oil prices of 2007 and 2008, renewable energies like wind and solar have seen sustained growth and momentum over the last decade. Comprising less than 1% of total electricity generation in the U.S. in 2007, wind and solar power now account for 10%, and are expected to rise to 34% by 2040 as these renewable energy sources achieve cost parity with coal and fossil fuels. The price of solar electricity in the U.S. already has fallen nearly 75% since 2009, with an additional 66% decline expected by 2040. Likewise, onshore wind power is 30% cheaper than it was in 2009 and is projected to decline another 47% by 2040, while the cost of offshore wind is estimated to fall 71%. Even as the price of oil has dropped to between $40-$50 per barrel recently, the demand for – and investment in – clean energy shows no sign of slowing down.

Contact: If you have any questions or comments, please do not hesitate to contact us at 703.992.6164. For more information about Harbour Capital Advisors, please visit our website at www.harbourcapitaladvisors.com.

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