Sevens Report Alpha Webinar:

Setting Up for 2021

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S&P 500 Earnings & Multiple Assumptions

S&P 500 EPS Estimates

- 2021: $175 (ish).
- 2022: $195 (ish).

Current Market Multiple Assumptions

- Current (S&P 500 at 3,800)
  - 21.7X 2021 Earnings
  - 19.5X 2022 Earnings
  - Neither of these numbers are *that* expensive given the current macro set up (fiscal stimulus, 0% rates).
- Future (A 20-22X 2022 Earnings)
  - 4290 in the S&P 500 is justifiable.
  - 11.4% gain from current levels.

But, S&P 4000 is not inevitable.

There are three sources of risk to the current bullish scenario:

1. **Economic disappointment**
2. **Political pressure on earnings**
3. **Yield spike.**

Risk 1: When Does the Economy Need to Return to Normal?

- WSJ Economic Forecasting Survey has Q2 ’21 GDP at 4.2%, Q3 GDP at 4.3% and Q4 GDP at 3.8%.
- That essentially tells us that Wall Street consensus has the economy largely back to “normal” between April and June of 2021.
- A ‘normal” economy is very much priced into the 2021 S&P 500 EPS and the 2022 S&P 500 EPS.
- If the recovery takes longer than expected, that is a risk to earnings, and that will be a headwind on stocks.

Risk 2: What Democrat Policies Would Hurt Earnings?

- Democrats have several policy initiatives that could hurt corporate earnings.
  - Increase in the corporate tax rate. President-elect Biden has advocated for an increase in the corporate tax rate to 28% from the current 21%.
  - Increased regulation. Potential $15-dollar minimum wage, along with increased ESG regulations for public corporations could pressure expected corporate EPS.
  - If either of these initiatives get enacted, expect some pressure on expected corporate earnings and potentially share prices.

Risk 3: Rising Yields

- This last risk is the one to watch for, because it'd be an unintended consequence.
- The main reason markets are comfortable with a 20X multiple on the S&P 500 is because bond yields are so low. It's intensifying the TINA trade into stocks.
- But, if longer dated Treasury yields begin to rise as Democrats unleash more stimulus and debt/deficits continue to rise, then the **market multiple will have to come down. Put simply, investors will stop paying such a valuation premium in stocks once less risky assets (like bonds) can offer a decent yield.**

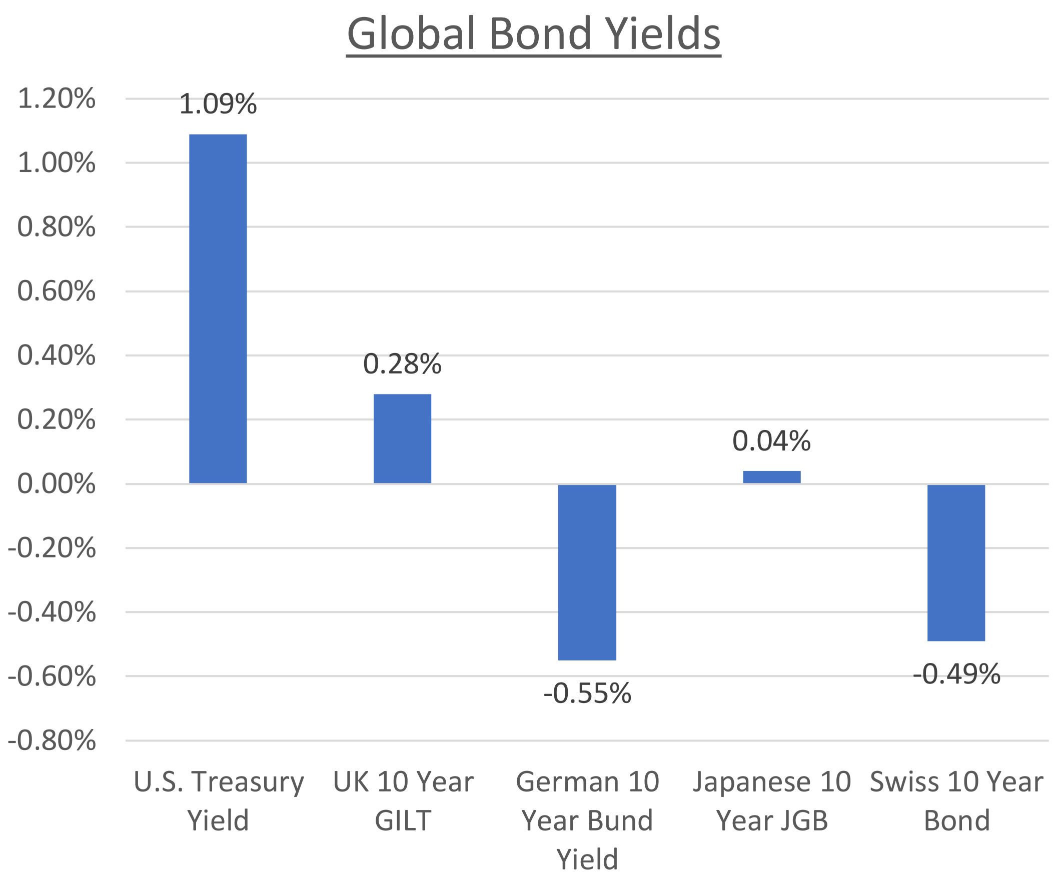
Will Rising Yields Pressure Multiples?

- This last point is important, because if we get yields rising to the point where they pressure multiples, the market impact can be substantial.
- Every 1 point drop in the market multiple is worth 175 points in the S&P 500 (and maybe 195 points). That's around 5% per point.

- Current Multiple Equation:
  - 2021 S&P 500 Earnings of $175 * 21.7X = 3800.
  - Multiple Declining Scenarios:
    - 2021 S&P 500 Earnings of $175 * 20X = 3500. 8% decline.
    - 2021 S&P 500 Earnings of $175 * 19X = 3325. 13% decline.
- This is why yields and inflation are so important this year – because of the interplay with the multiple.

Will Rising Yields Pressure Multiples? (cont'd)

- Positively, there factors in place that will limit the rise in Treasury yields.
  - Where else is there to go? The world is awash in capital and it must find a home. There is no other asset that can compete with U.S. Treasuries for liquidity and stability. Until there's an alternative or the U.S. fiscal situation gets much worse, that will limit the rise in Treasuries. **The global nature of the bond markets helps Treasuries significantly.**
  - The Fed. If the Fed becomes spooked by the rise in the 10-year yield, it could simply increase the duration of QE to limit the rise (the Bank of Japan has done something similar in the past).



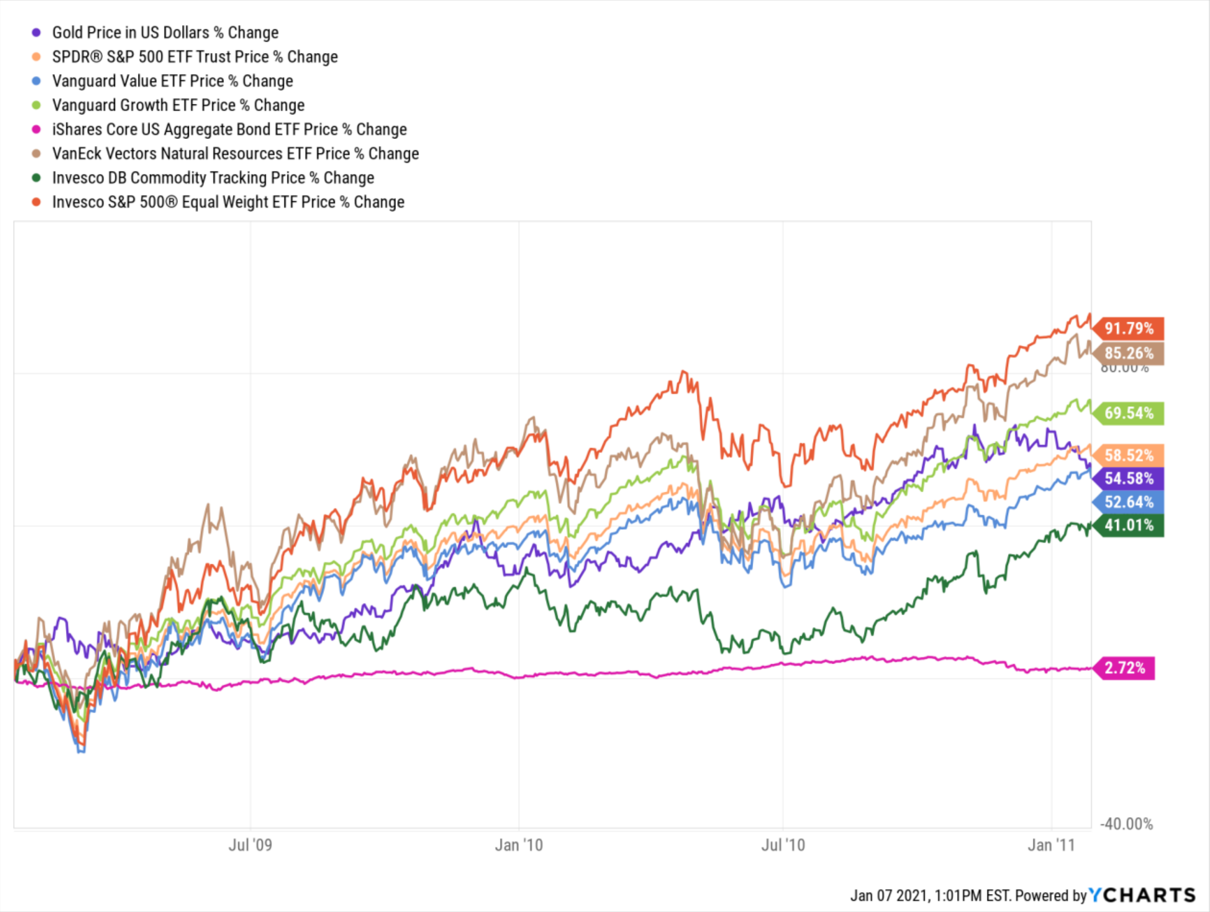
Alternative Assets – What To Expect

Alternative Assets – What To Expect (cont'd)

- Bitcoin, stocks, real estate and other assets have risen as markets have reacted to surging stimulus and record debt/deficits.
- Bitcoin, in part because of its libertarian-like appeal and lack of liquidity, has seen the most substantial benefit as the dollar has fallen.
- But, the U.S. dollar very much remains the world's reserve currency. That's not just by choice, but also by necessity – there is no currency that can compete with the dollar as a reserve currency.
- Bottom line, fringes of the market are reacting to surging debt and deficits, and that can continue. But, the sheer magnitude of the gains is more a function of lack of liquidity than it is driven by evidence of an impending collapse in the dollar and/or Treasuries.
- In sum, Bitcoin, like gold, is as much a statement as it is an investment. And, for those that want to own it, they need to understand that and accept that fact, and the volatility.

Cross Asset Review – Last Democrat Controlled Government

- The last time markets delt with a Democrat led-Washington was from January '09 – January '11.
- Dollar Index: 84.62 (01/09) to 78.91 (01/11). That's a -7.2% decline.
- Stocks and Gold rose astonishingly similar amounts (58.6% and 58.5%).
- Bonds lagged (AGG 2.72% cumulative return).
- Implies a positive outlook for Bitcoin also.



Alpha Strategies To Consider If Past Is Prologue:

- Smart Beta Pioneer (RSP). Issue Date: 9/7/17.
- Commodities (PDBC/GNR/RLY). Issue Date: 9/18/18.
- Socially Responsible Investing (ESGV). Issue Date: 3/26/19.
- How To Responsible Allocate to Gold (GLD/SGOL/GDX). Issue Date: 7.2.19.
- What Outperforms in a Declining Dollar Environment (XSOE/FXE/GDX). Issue Date: 8.11.2020.
- COVID Vaccine Beneficiaries (JETS/PEJ/KBE/REZ). Issue Date: 8.25.2020.
- Four Post Election Tactical Strategies (LIT/ICLN/ESGV/VIS/PAVE/CHT/MJ/XSOE). Issue Date: 11.17.2020.
- Bitcoin (GBTC). Issue Date: 12.1.2020.