Sevens Report Alpha Webinar:
A Deep Dive into the Growth to Value Rotation

Thursday, March 4th, 2020

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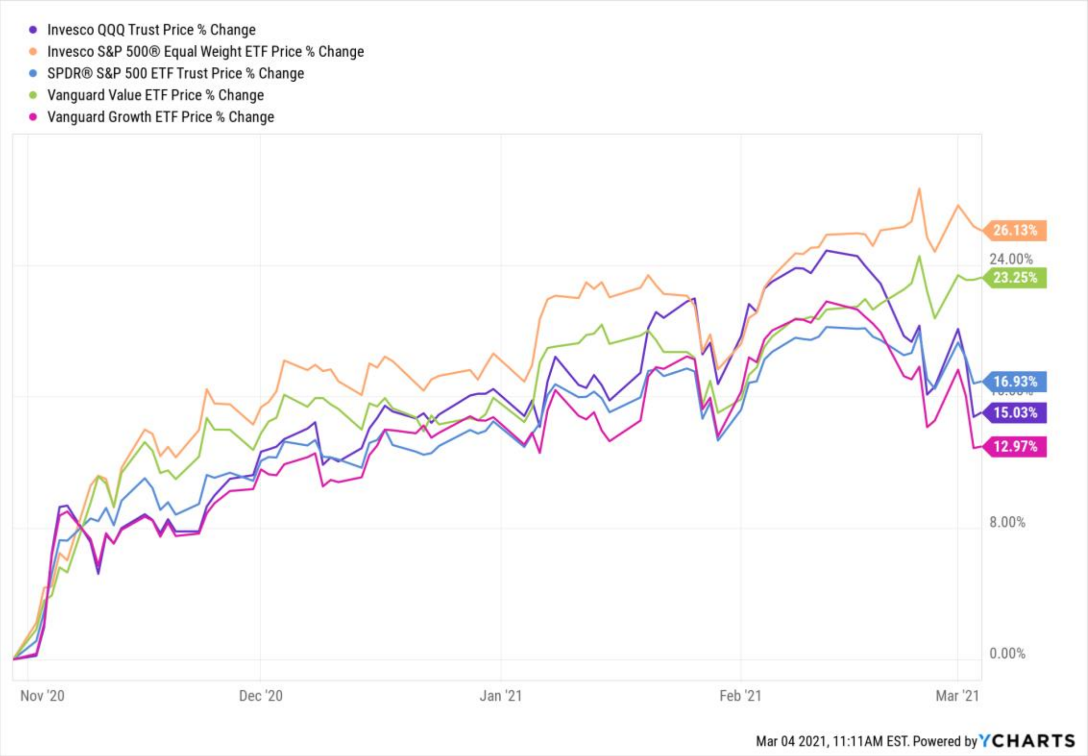
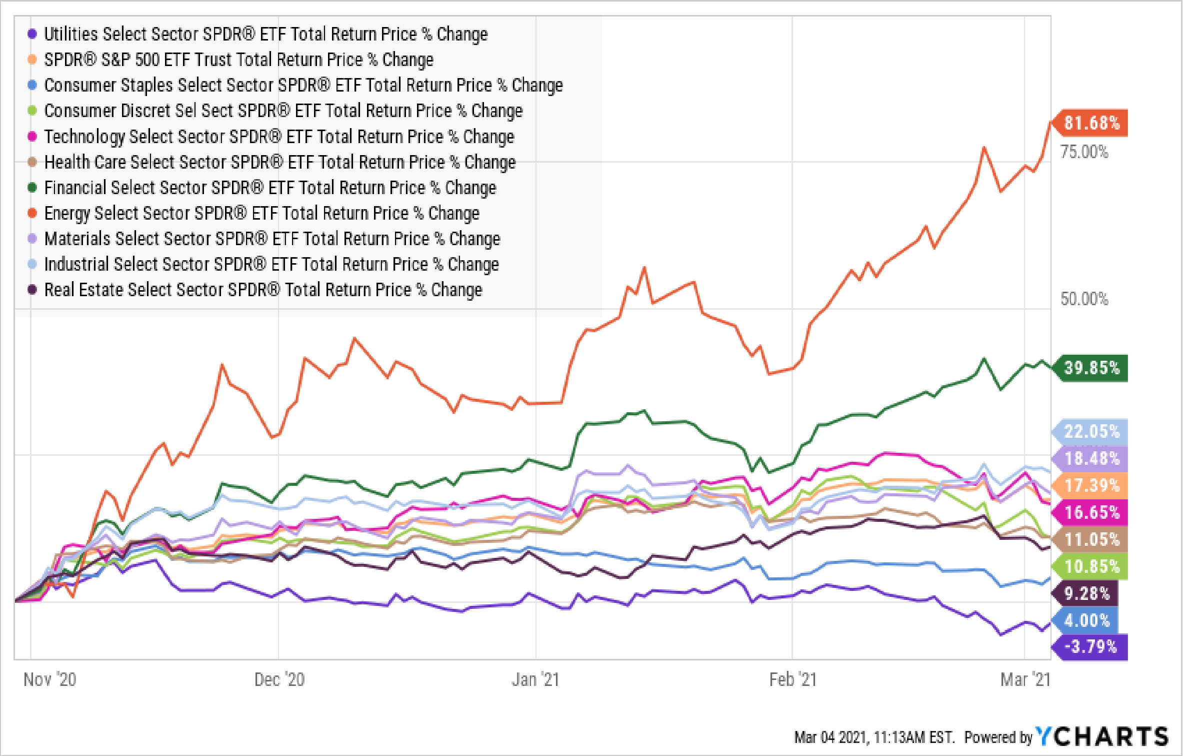
Growth To Value Rotation: How Powerful Is It?





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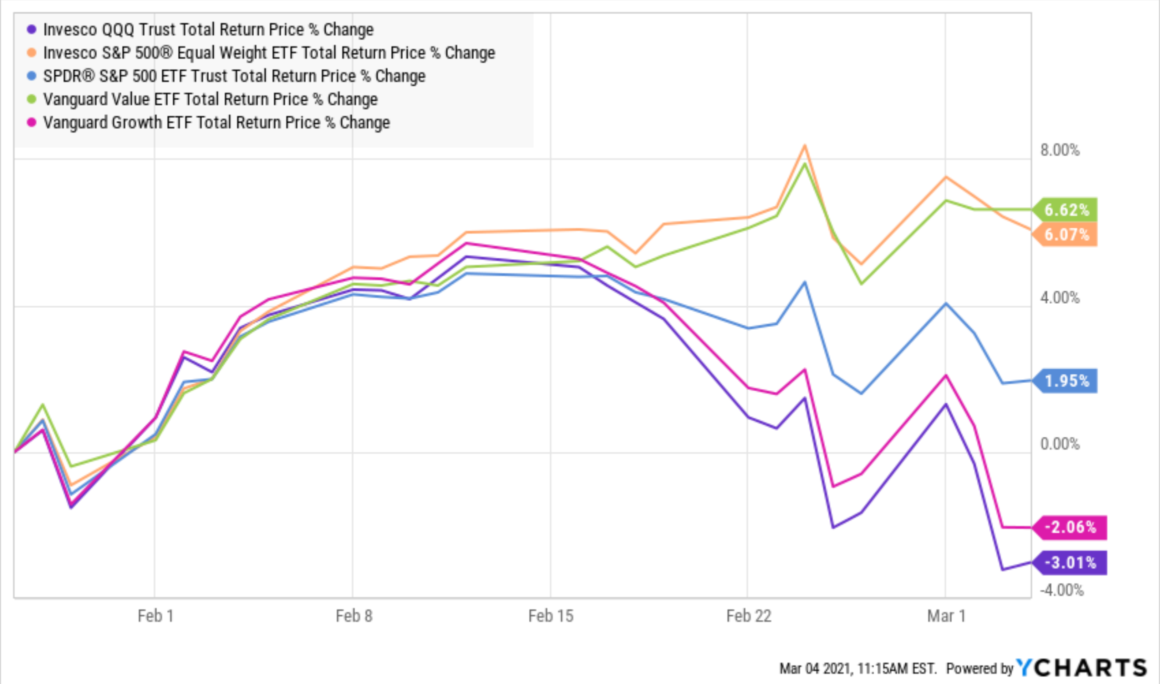
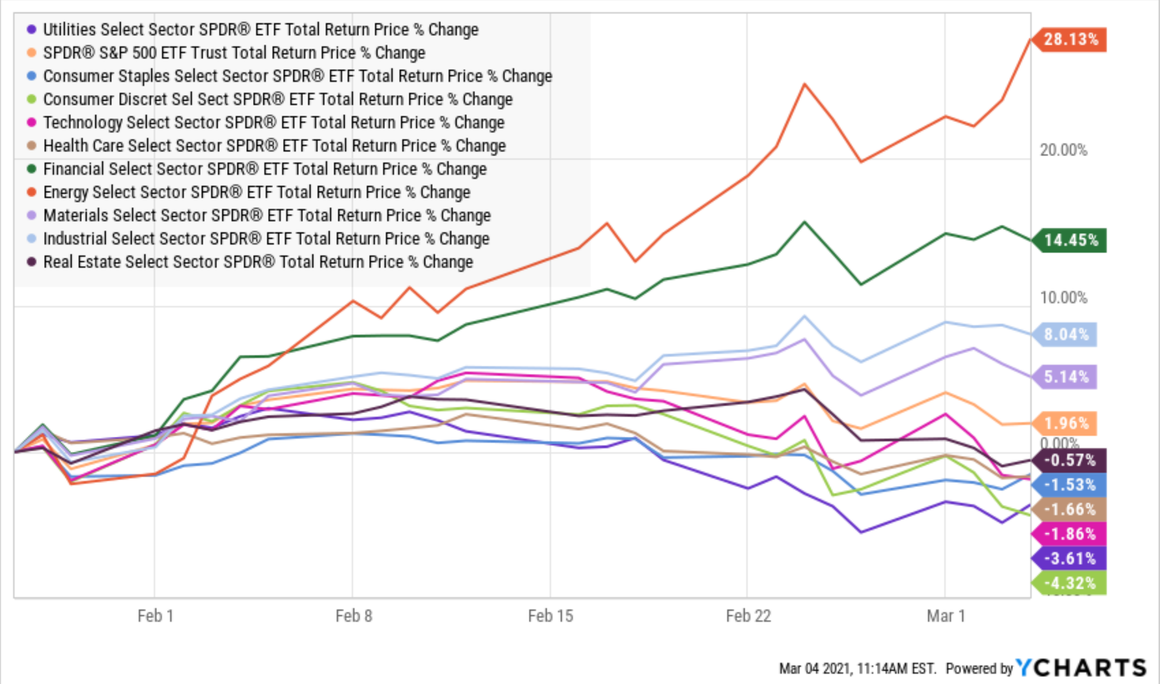




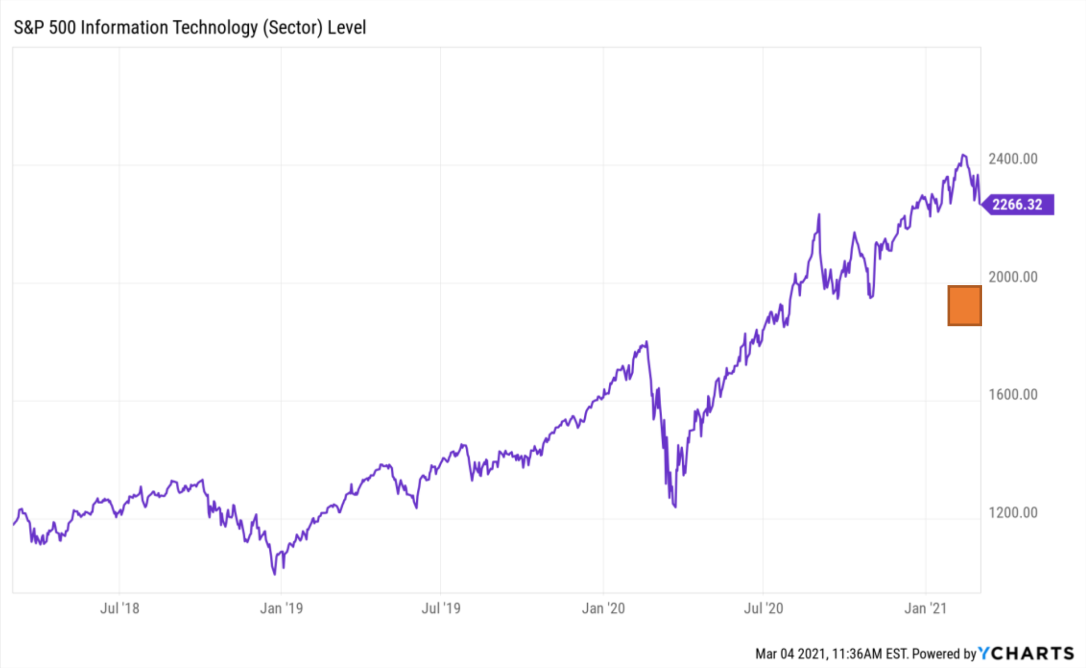
Diving Deeper into “Growth” and “Value”

- Growth effectively means:
  - Tech sector
    - Large cap tech
    - Semiconductors
  - Pandemic beneficiaries
    - Online payments
    - Video conferencing
    - Cloud
  - Momentum names
    - Bitcoin
    - Electric Vehicles
    - SPACS
- Value effectively means:
  - Financials
  - Energy
  - Commodities/Hard Asset Plays
  - “Reopening” Stocks
    - Airlines
    - Hotels
    - Cruise lines
    - Hotel Booking Sites

Growth Tier 1: Large Cap Tech – Buy the Dip

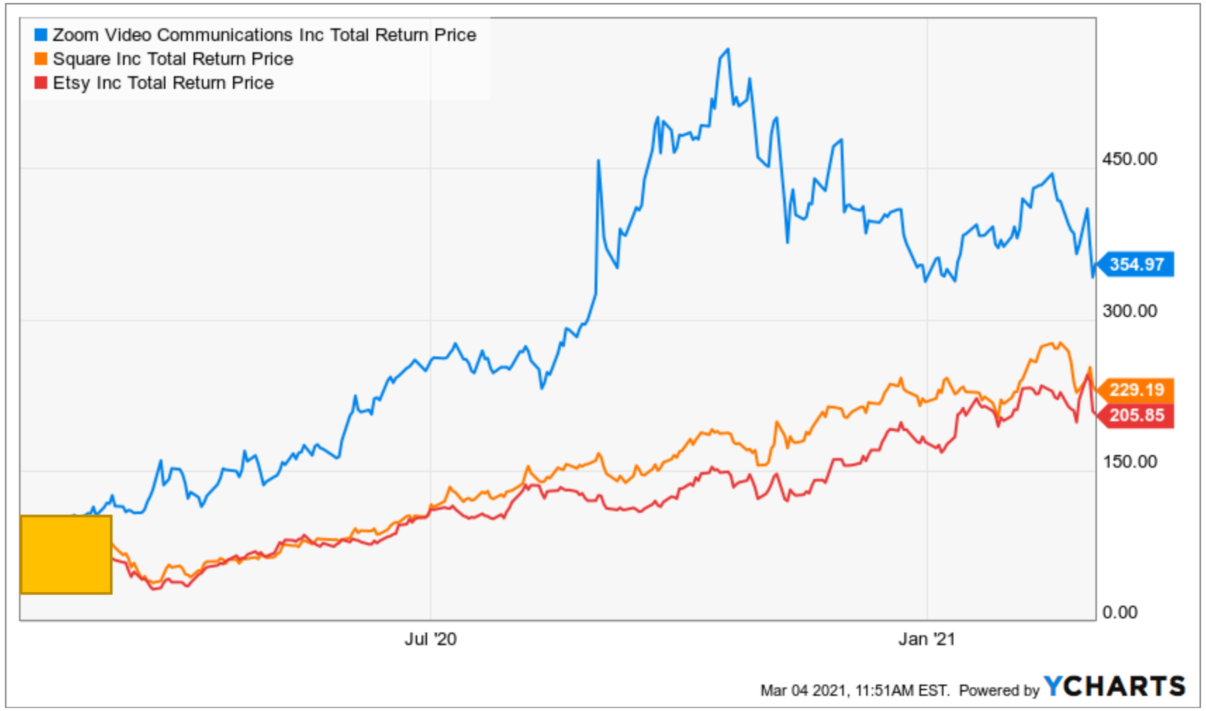
- Super Cap Tech – Think heavyweights in the S&P 500 Information Technology ETF.
  - AAPL/MSFT/NVDA/INTC/ADBE.
  - Good companies at high valuations.

- Prior to the pandemic, the IT sector was trading around 22X earnings.
- Now, it's trading around 26X earnings (a record).
- Consensus S&P IT sector earnings for 2021 are around $87.
- If the IT sector trades back to a pre-pandemic valuation of 22X earnings, that's 1914 in the S&P IT sector.
- Currently the S&P IT sector is at 2269.
- So, we could see up to a 16%-ish decline in tech – at which point these names would be a "Buy."



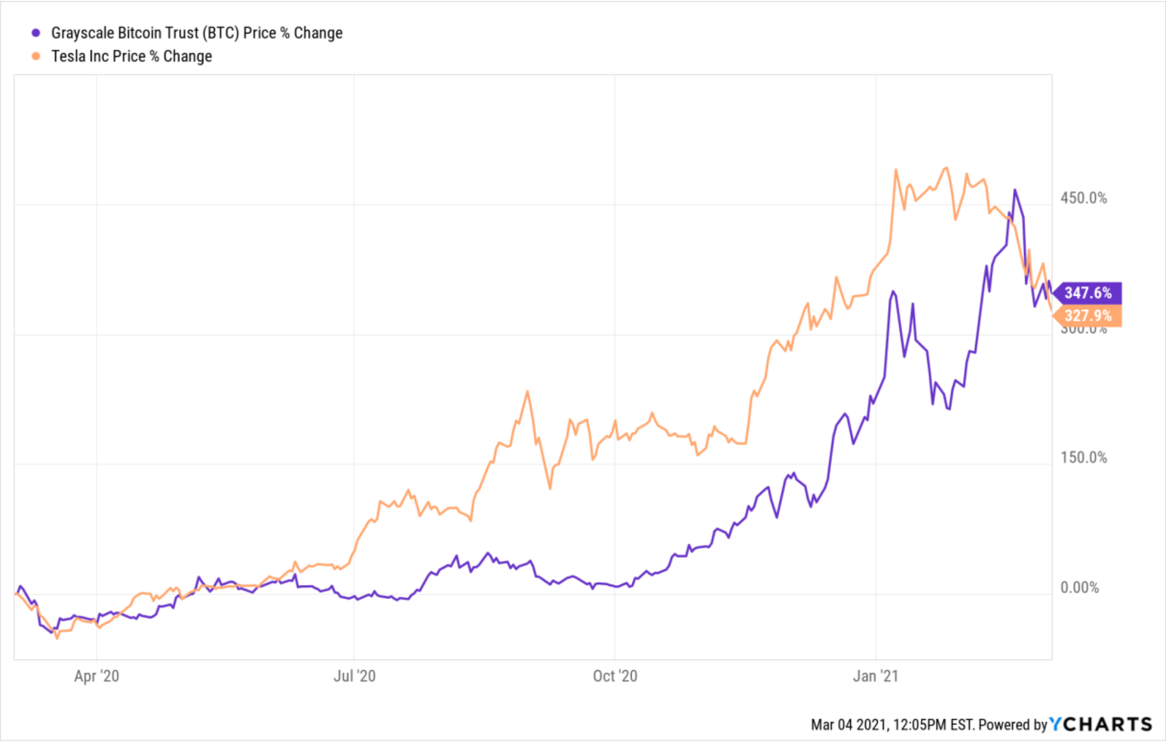
Growth Tier 2: Pandemic Beneficiaries

- These are smaller tech companies that have seen outsized gains thanks to the pandemic.
- Example: Zoom (ZM).
  - Pre-Pandemic Fwd P/E: 21X
  - Current Fwd P/E: 86X
  - Earnings: Fiscal 2020 $0.09. Fiscal 2021: $2.25. Fiscal 2022: $3.71.
  - If we assume $3.71 EPS and put a 50X multiple on it, ZM = $185.50.
  - That's a 48% decline from here.
- Point being: These pandemic beneficiaries (small companies that have seen sales explode due to the pandemic) can fall a lot farther before getting anywhere close to reasonable valuations in a non-pandemic world.
- Similar names: Square (SQ), Etsy (ETSY).

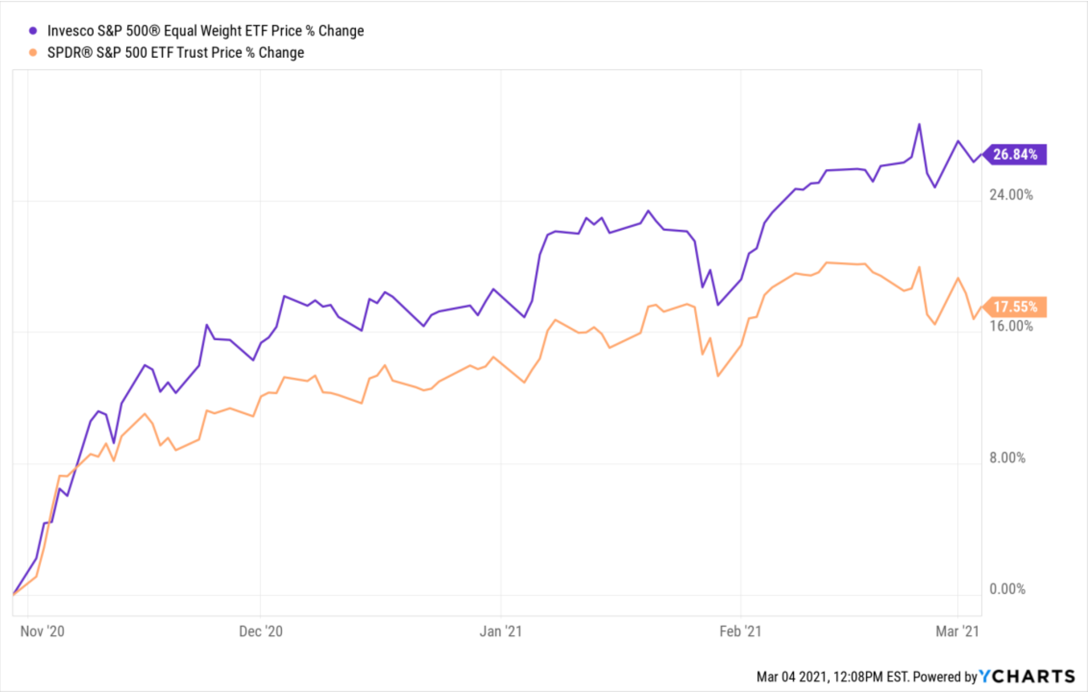


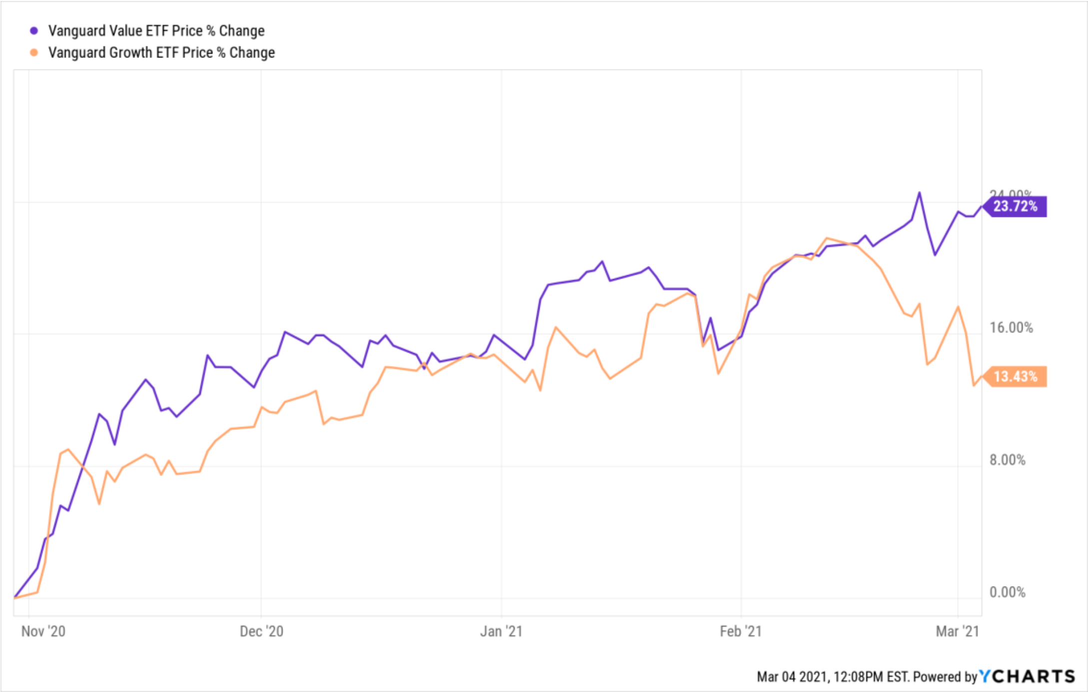
Growth Tier 3: Bubblicious Names

- Stocks and crypto currencies that have become driven by cult like demand and pure momentum – so much so that they've blown way past and reasonable way to value them.
- TSLA/Bitcoin/SPACs
- When the bubble bursts on these is anyone guess, but the downside in these names is extreme, if the rotation out of growth accelerates.
- Bottom line: There's the potential for a lot of unwind in this rotation.



Value Tier 1: Easily Adding Value Sectors to Portfolios





Value Tier 2: Targeted Sectors

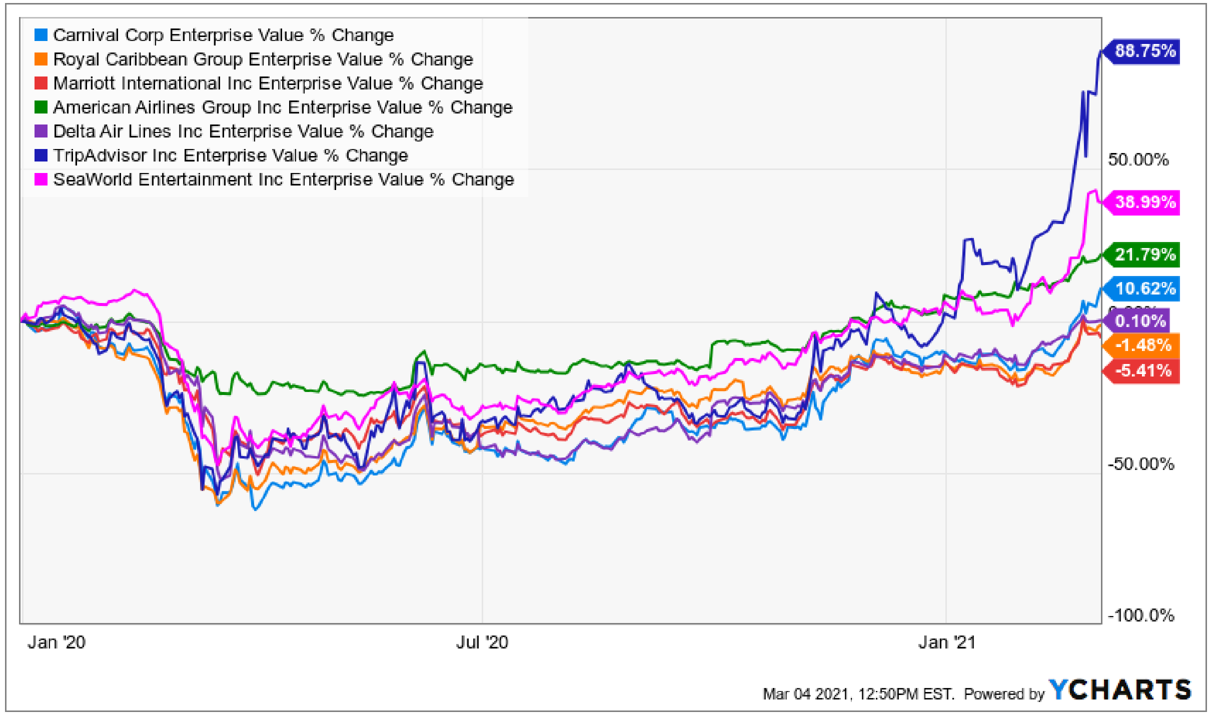
- Value sectors that benefit as growth accelerates and have a positive correlation to current macro trends.
  - Financials (XLF/KRE/KBE/IYG) – Positive correlation to higher yields.
  - Energy (XLE) – Positive correlation to rising inflation.
  - Industrials (XLI) – Increased government spending and a possible infrastructure bill.

- Forward P/E’s (and pre-pandemic multiples):
  - Financials: 15.1X up from 13X-ish.
    - EPS growth expected at 22% in ‘21 and ‘12% in ‘22.
  - Industrials: 24.8X up from 18X-ish.
    - EPS growth expected at 72% in ’21 and 35% in ‘22.
  - Materials: 20.3X essentially flat.
    - EPS growth expected at 34% in ‘21 and 9% in ’22.
  - Energy: 26X (Totally dependent on oil prices).

Value Tier 2: Targeted Sectors

Value Tier 3: Get Out and Spend Names

- Travel & Leisure names have seen huge gains lately on anticipation of an economic re-opening.
- But, many of these names are not trading at discounts, because of the measures they've taken to stay in business.
- Airlines, cruise lines, hotels, etc. have raised massive amounts of capital via equity offerings of bond offerings, so much so that the "Enterprise Value" of these companies is now higher than it was pre-pandemic.
- Point being: There's still upside in these names, but that's going to be based on better than expected performance and re-opening. These are worth risk capital, but they aren't cheap and a continued rally isn't a slam dunk.



Bottom Line

- Growth/Tech
- Super Cap Tech names have more room to fall, but another 10% - 15% lower and we think that's a buying opportunity.
- Pandemic beneficiaries remain very expensive and if earnings disappoint, then the downside is still substantial.
- Momentum plays remain near the stratosphere, and their decline could continue weigh on tech broadly, and the markets generally, for a while.

- Value
- Adding broad value exposure to a balanced portfolio has insulated investors from the tech decline and we think that continues.
- The combination of expected earnings growth and still reasonable valuations make the value sectors (financials/industrials/energy/materials) attractive even after this recent outperformance.
- The "Get Out and Spend" names offer additional upside on an economic re-opening, but they aren't cheap anymore considering EV and we see these are more tactical plays on a reopening (so 3-6 month holding time).