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"Rhyming the Reagan Era"

For the second quarter, the NASDAQ rose 3.9% and for the first half of 2017 the composite gained 14.3%. It was the leading index by a wide margin as the S&P 500 rose 8.497% and the Dow lagged slightly at 8.27%. There was much attention at the end of 2016 to the Trump Trade, but there was no follow-through by the names that led in the wake of Trump's surprise victory in November. Instead, a wide range of NASDAQ names, including FANG names, began to lead in January and were among the most robust gainers as the first half concluded. I think it is fair to say that the market looked at the potential positives, like reduced regulation and lower taxes, and largely ignored the turmoil in the nation's capitol. Given the surprising and sometimes disturbing things going on in D.C., it's possible the market will have a different, less positive response in the future, but for now the market is regarding doings in Washington as a sideshow and not critical to the current psychology. Some suggest that the market is displaying a "contrarian streak" and its "psychological mischief" is on full display.

Another hallmark of the current market is its resilience. Despite the substantial build-up of distribution days—the NASDAQ showed six and the S&P 500 had 4 at the end of the quarter. The market ended the quarter on a cautionary note as its uptrend came under pressure. Despite this change in current condition and hesitant action as well as some modest profit-taking in leading names, the market ended the quarter in an overall steady state.

Among the key components of the NASDAQ Composite contributing to its outperformance are semiconductors, software and internets. In the post-July 4 rally, among the fourteen industry groups that rallied significantly—2% or more—seven came from the computer, electronics and chip sectors. The current market focus and outperformance by growth names and innovative companies is not surprising to long-time market observers. It is common and usual for growth names, as opposed to cyclicals and value plays, to outperform during extended bull runs. Admittedly, there has been a lot of worrying about current conditions because of Washington, North Korea, the Fed and recent suggestions that conditions are right for a recession, but markets look ahead and climb walls of worry. As a growth-focused investor, it is my objective to place money in the most productive places. To fully accomplish that goal there must be a strong market and from there it is a matter of selecting innovators and rapidly growing companies that are superior to 90% of all publicly traded names on the basis of metrics such as earnings and revenue growth and margins. Then it is a matter of timing and often the optimum time to invest is on a robust earnings report—think Facebook in July 2013. For more than a year after its IPO, Facebook's earnings were uninspiring, but that changed on July 25 2013; since then the stock has risen 339%. Portfolio stocks, by-in-large, have been outperforming throughout this year. What confuses some is that, at times, like late last year, the market does not favor growth names.

Will this continue? Many observers see parallels to the Reagan Era. The Reagan presidency coincided with the start of a market super-cycle in August 1982. While one can debate how important any president is to the performance of markets, it's useful to identify the big picture items that are common among strong market cycles. Reagan was the most optimistic of the last five presidents and also pro-business. A president plays no role in company innovation, but he can help by staying out of the way by refraining from excess regulation. Both George W. Bush and Barack Obama, through their economic policies, created obstacles to particular industries and the entire economy. Clinton signed the Internet Tax Freedom Act in 1998 and the internet-content group rose over 1200% during his presidency. Similarly, the generic drug group rose 859% in the wake of the Drug Price Competition and Patent Act of 1984. As we know, regulations, while well-intended, often have unintended consequences that leave whole sectors or industries in the dark as has been the case with bio-techs in recent years. The companies continue to innovate, but despite compelling valuations, the stocks continue to struggle.

Markets look forward and not unsurprisingly in the wake of a "joyless bull market" in recent years, markets are now encouraged by the prospect of a business-friendly environment with lower taxes and fewer stifling regulations like the Reagan Era. To many observers, the period before us looks like 1982 and the recent past bears a strong resemblance to the period from 1968 to 1982. In the past two years, the markets have been stuck in neutral. While history doesn't repeat itself exactly, it does, as Mark Twain quipped, "rhyme." The market, using this historical precedent, may be on the cusp of an exciting new uptrend. The post-election was a bit of a head-fake, but the Dow made a new all-time high of 18,873 post-election…and has kept going. While the Dow surged post-election, the NASDAQ struggled, but since the NASDAQ has turned from laggard to leader and it's not just the FANG names all of which are portfolio companies, but other innovators like Tesla, Apple, Alibaba and Adobe. If the current conditions continue to pertain, the period ahead may be " rhymin' " with its historical precedent. In the past, lower taxes, fewer regulations and renewed optimism along with renewed confidence have laid the groundwork for robust market gains. Imagine, if you will what might happen if, in addition, passive investors ditch their ETF's and index funds and invest in individual stocks….

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