SCHLINDWEIN ASSOCIATES
INVESTMENT COUNSEL

Magnificent

In just over two years, the broad U.S. stock market, as measured by the S&P 500 Index, has reached a new, all-time high. Much focus, however, has been on the performance of a handful of tech-oriented stocks dubbed the "Magnificent 7". Ever creative, the financial industry even offers an exchanged-traded fund focused solely on these stocks. Investors generally benefit from markets reaching new highs, particularly if they have exercised discipline to stay invested through lows and highs. No matter how magnificent the recent performance, jumping from one theme to the next can be costly if timing is off. A review of recent market cycles may be informative for investment strategy ahead.

PERSPECTIVE

In an homage to the "Nifty Fifty" of the 1970s, investors today are enticed by the "Magnificent 7" – Alphabet, Amazon, Apple, Meta, Microsoft, Nvidia and Tesla. Cycle trends for these stocks are shown in Chart I. In the downside from early 2022, these stocks on average lost almost 50% of their value, and each one individually experienced a bear market performance of more than -20%. The upside to the recent new all-time market high has been led by the outsized performances of META and NVDA. Holding the "Magnificent 7" as a group resulted in a total period gain of +19%. As an example of bad timing, the outcome for a frustrated holder of META in the downside who then jumped to the less damaged AAPL for the upside was a cumulative -49% loss.

Return patterns of the "Magnificent 7" exemplify the investment adage of higher risk begetting higher reward. Cycle trends for these stocks relative to those of the broad U.S. stock market, as measured by the S&P 500 Index, are shown in Chart II. Stock weightings in the S&P 500 Index are by market size, and the "Magnificent 7" represent a large 29% share of the Index. While the downside for the S&P 500 was a bear market loss at -25%, the "Magnificent 7" loss was almost twice as large. However, the upside recovery was even more pronounced for the "Magnificent 7", outgaining the S&P 500 3-to-1. For the total period, the outperformance of the "Magnificent 7" was six times the S&P 500 Index's modest gain of +3%.

The return patterns of the "Magnificent 7" are notably different from those of the average U.S. stock. Cycle trends are shown in Chart III. The downside of the average U.S. stock was comparable to that of the S&P 500 Index, and the "Magnificent 7" loss was almost twice as large as that of each measure. The "Magnificent 7" upside recovery was even more pronounced than that of the average U.S. stock at a ratio of 4.5-to-1. While the "Magnificent 7" posted a double-digit gain for the total period, the average U.S. stock is yet to reach its prior high. To fully recover from a -25% loss requires at least a subsequent +33% gain, and the average stock has fallen short.

INVESTMENT IMPLICATIONS

Any investor would be thrilled to achieve the levels of gains recently delivered by the stocks of the "Magnificent 7". But how many investors could withstand the pain of losing almost 50% of their investment before such gains materialized? Realizing one's investment-loss pain threshold in real-time would be very costly if the outcome was selling out at the low and missing the subsequent gain. It is important to understand loss tolerance before investing begins. From there, an appropriate allocation to anything magnificent can be determined.

CHART I

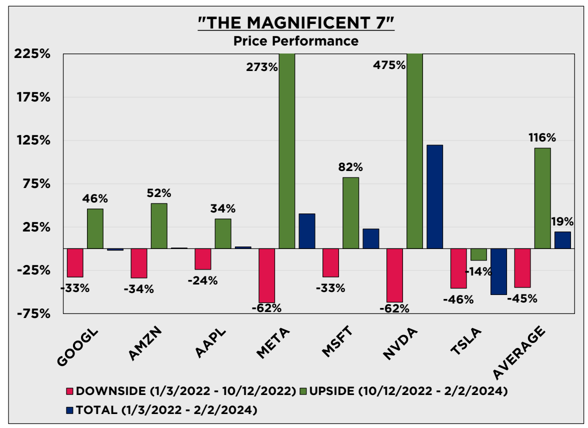

CHART II

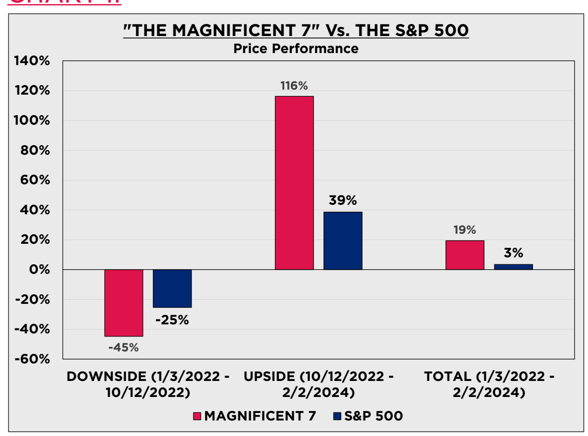

CHART III