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Misleading Indexes and Tesla Drama

It used to be that most of us gauged stock market performance relative to an index of 500 stocks called the Standard & Poor's 500 (S&P 500). It may be that the S&P 500 is no longer a good reflection of financial reality.

We noted last month that the performance of the S&P 500 is dominated by just seven stocks. Because the S&P 500 is a "market-cap weighted" index (the larger the company, the greater the impact on the index), the index appears to no longer be a reliable indicator of the "overall" market.

Last week, economist David Rosenberg tweeted that six stocks (Facebook, Google, etc.) in that index have increased over 30% this calendar year. The other 494 stocks are up closer to 3%. He may not be totally accurate with his tweet but the concept is valid.

So if you don't own those six stocks, you may feel like you are underachieving. You are not underachieving. In every period of time, you can always find an investment that is doing better than your investments. Those investments almost always involve taking more risk than is necessary to reach your goals. And when you are experiencing a rather long bull market (arguably 9½ years now), it becomes increasingly easy to forget just how much pain can be inflicted by a market correction.

We don't ever forget that. We won't ever forget that.

The best performing asset class last year (Emerging Markets) happens to be the worst performing asset class this year. The primary reason is the increasing value of the U.S. Dollar worldwide. Most of these nations have debt that is denominated in dollars, and as their currency declines (relative to the dollar), the amount they owe increases without them borrowing another penny. It's like your mortgage company calling to say that the amount you owe on your house just increased from $300,000 to $350,000. Oops!

The potentially good news (someday) for these Emerging Market nations is that the value of the dollar can (and usually does) eventually decline again, making their debt much easier to pay. Stay tuned.

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We don't own Tesla stock in our clients' accounts. We never have. Probably never will. But that doesn't mean we are not entertained by the battle going on between the Tesla bulls, who own the stock because Elon Musk can do no wrong, and the Tesla bears, who have "shorted" Tesla stock unmercifully, banking on the idea that Elon Musk has already done plenty wrong. The number of Tesla shares that have been sold short (*selling shares you don't own with the idea you will buy the shares back at a lower price someday, a bet that things are not going as well as the company would lead you to believe, also known as "short interest"*) is over 25% of the total shares outstanding! It's hard to find another stock with short interest of even 10%.

That means a lot of investors are really, really, really pessimistic about the future of Tesla!

Remember, if you are short a stock, you are betting the price will decline. If you are wrong and the price increases, you may have to buy that stock back in the future at a higher price. It's the same as buying high and selling low, only in reverse. And it hurts just the same.

As we have said many times, you can be correct and appear to be incorrect for a long time. Short-selling a stock and watching it increase in value can try your patience, particularly in a 9½ year bull market where almost all stocks go up no matter what. Even if that stock ultimately declines and your bet proves to be correct, watching the price initially go up is painful . . . because, theoretically that stock price can go to "infinity," which means your loss could be infinite. But as one famous short-seller said, "I've seen a lot more stocks go to zero than I've seen go to infinity."

Which brings us to early August. Like most Chief Executive Officers who have a large stake in the company they are running, Elon Musk probably gets irritated by short-sellers because they keep the stock price from increasing as much as it could. However, there's not much one can do about people selling your stock except proving them wrong by making your company deliver its product as promised, something the short-sellers are pretty sure is not going to happen at Tesla.

There's not much you can do . . . unless you are Elon Musk.

In early August, Musk tweeted that he had decided to take Tesla private, by paying shareholders $420 per share. And he assured his Twitter followers that he had arranged the financing to make this happen. Allegedly.

The stock shot up to almost $380 per share (it was below $300 in July), which created instant losses in tons of short-seller accounts.

Never mind that he wasn't more specific with how he intended to acquire over $50 billion for this "project."

A couple of weeks later, Musk admitted that taking the company private was probably a low likelihood and the stock has since declined well below $300, currently around $280, depending on what minute we are typing this.

Some are calling Musk's tweet an attempt to manipulate the price of Tesla's stock, intentionally making the price go up, causing the short-sellers to buy their shares in a panic, thereby driving the stock price even higher.

Stock price manipulation is frowned upon by the Securities Exchange Commission — so much so that, if it is proven, one could find oneself in prison. And as Martha Stewart discovered, fame doesn't necessarily provide protection from the SEC.

We don't have a dog in this fight, because we don't own TSLA and we are not short TSLA, but it is entertaining. And it is another reminder that investing serious money for a long time with minimal risk needn't involve investing in the names always grabbing the headlines.

Later this month, it is widely expected that the Federal Reserve will raise rates again as it attempts to bring short-term interest rates to a more "normal" level (whatever "normal" is). This will be the third rate hike this year and yet long-term interest rates stubbornly remain relatively low.

In the second quarter, Gross Domestic Product (GDP) popped to a growth rate of 4.2%, which was not an uncommon number "back in the day," but our economy has been running closer to a 2% average growth rate (with spikes well above and well below) annually since the Great Recession of 2008 (see graph below). It remains to be seen if our economy has fully recovered or is benefitting from the transitory effects of recent tax cuts and de-regulation.

Regardless of the reason, corporate profits were up over 20% this past quarter. The housing market (a great barometer of an economy) continues to see strong demand for new homes. Low mortgage rates could be contributing to that demand.

And in the labor market, unemployment is near all-time lows (3.9%) and there are more job openings than there are people looking for jobs. And if you have tried to hire someone competent to come do work around your house, you know what we are talking about.

For all these reasons, the U.S. stock market has been calm lately and the Volatility Index (VIX) remains low.

It’s nice to know what has happened. But at Boyer Corporon Wealth Management, we continue to remain focused on what is going to happen.

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This past week marked the 11th anniversary of Boyer Corporon Wealth Management. On the day after Labor Day, 2007, we departed the inefficient world of “broker/dealers” (B/D) and established a “Registered Investment Advisor” (RIA). Being an RIA provides us the ability to manage our clients’ financial lives much more efficiently.

And, oh, by the way, not a minute too soon. The period 2008–2009 brought the worst stock market experience in 80 years, but being structured as an RIA gave us the flexibility to help our clients sidestep a vicious hit to their net worth. That would have been virtually impossible had we still been working as a B/D.

It was the best move we ever made and we have never looked back. Our assets under management have tripled since then and our employment has more than doubled. Providing clients “Peace of Mind” will always be the guideline that shapes every decision made at Boyer Corporon Wealth Management.

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