BCWM
PROVIDING PEACE OF MIND

DON'T TRY THIS AT HOME
(we are professionals)

The wonderful (and dangerous) thing about our business is that it frequently appears to be so simple. And some days it actually IS simple . . . until it isn't.

> *True story. Back in the good old "dot com" days, we had a client call up and say "I just got a hot tip. I want to buy 1,000 shares of a stock." He gave us the name of the stock and we bought it for him. Five days later . . . maybe four . . . he called back in a panic and said, "OMG, I told you to buy the wrong stock. I meant to buy this other* (similarly sounding) *stock. Let's buy 1,000 shares of the correct stock right now. By the way, that stock that I bought in error? How has it done?" It was only up 65 points. That's right. He made $65,000 in less than a week and he bought the wrong stock!*

That's the kind of stock market it was in 1999–2000. You could buy anything and make $65,000 in less than a week. If you weren't buying dot-com stocks, you were considered an idiot. A couple of clients fired us because we didn't own all of the hot names.

Of course, the hot names hadn't really generated any "earnings" yet (you know, the money that's left over *after* you have paid *all* your expenses). Because it became so difficult to ascertain when these companies might actually begin to have money left over after expenses, investors decided that "earnings" was just too high of a bar. So they began to compare the stock price to the company's "revenues" (you know, the money you have *before* you pay *any* expenses).

And then these speculators would stand around at cocktail parties bragging about buying their latest internet stock purchase and how much money they had made in only three days. "I just bought JDS Uniphase at $100/share and it's already up to $200/share." *(For the record, JDS Uniphase traded as high as $1,100/share before falling to $4/share in 2009.)*

Of course, the real kiss of death is when a sector gets *so hot* that some investment company decides to capitalize on its hotness by creating a mutual fund of all the hot stocks in that sector. Why buy one stock when you can own 'em all via a mutual fund, right?

We don't mean to pick on Merrill Lynch, but there is no better way to illustrate the insanity of those times than to talk about the Merrill Lynch Internet Strategies Fund, which was established March 31, 2000, which, it turned out, was the absolute peak of internet stock price performance.

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To establish a fund of this nature *near* the top of the trend is not uncommon. But Merrill Lynch, not to be outdone by any of its competitors, established its fund at THE top. As soon as the Merrill Lynch Internet Strategies Fund was established, internet stocks began their eighteen-month slide. As a group, they declined over 70%. And in October 2001, after it declined 77%, Merrill Lynch quietly folded what was left of their Internet Strategies Fund into another mutual fund. Ouch!

(On a side note, the Merrill Lynch Internet Strategies Fund also carried with it an annual expense ratio of 2.68%! . . . further evidence that the creators of this fund were just a tad bit out of touch with reality.)

Why do we reminisce?

Because today is starting to feel like the year 2000. Stock trading is beginning to exhibit behavior similar to that seen in the dot-com era. Not so much tech stocks — although any company remotely related to anything "digital" is likely to be a popular stock today.

No, what is happening today is a result of several new circumstances all coming together to create a perfect stock-trading storm.

First, as of just a couple years ago, stock trading became free. Zero commissions. Nada. In 2000, when you traded stocks, you not only had to pay a commission when you bought them but you also had to pay a commission when you sold them. Commissions ate up a chunk of your gains. And if you lost money on the trade, you lost even more because of commissions. Today, virtually all discount brokerage firms charge $0 for commissions. (Kind of silly to call them discount brokers anymore since they are all charging $0).

Second, you can trade stocks on your smartphone, literally buying one minute and selling the next, if you wish. Remember the guy who called us to buy 1,000 shares of a stock because of a hot tip? He wouldn't need to call us today. He could do it himself using his phone.

Playing the stock market on your phone has become like a video game for some people.

Third, COVID-19 temporarily (we hope it's temporary) ended professional and college sports and thereby ended gambling on professional and college sports. There are millions of people (mostly guys, probably) who love to gamble on professional and college sports. Millions.

Just because sports are on a hiatus doesn't mean gambling addicts are also on hiatus. Gamblers still want to gamble. With the elimination of commissions and the ease of using smartphones to trade stocks, gambling on the price of stocks became the next best thing.

Hundreds of thousands of new trading accounts have been established this year at the various discount brokerage firms.

And the gamblers are gambling. And just like in 2000, these gamblers are not buying stocks as a result of analyzing a company's financials and believing in its products. No, they are buying stocks with the sole purpose of selling them to someone else at a higher price . . . and soon.

Case in point: On February 20, Hertz Global Holdings (the rental car company) was quietly trading around $20/share, right before *everyone* in the world quit traveling . . . and renting cars.

Fast forward a few months (May 26) and Hertz is trading at 55 cents/share. Why? Because Hertz is broke and filing for bankruptcy. When it can't rent cars, it can't pay its debts.

In a bankruptcy, debtors (bond owners) get paid first. If there is anything left (which there isn't or they wouldn't be bankrupt . . . get it?) it goes to shareholders. Well, apparently gambling stock traders didn't "get it," because all of a sudden, Hertz's stock price was doing a Lazarus.

Quarantined at home with no sports to bet on, gamblers (for whatever reason) zeroed in on Hertz.

The next day, it more than doubled to $1.31/share. Ten days later Hertz is up 422% to $5.53/share!!! For a company that is worth *zero*!

But gamblers don't care. All they want is to buy it at $3/share, hoping to sell it to someone dumber at $4.

Hertz is now trading back down at $1.47/share, which is probably $1.47 more than it should be.

Then there is Eastman Kodak, the photography company that made a left turn many years ago when the entire picture-taking world made a right turn.

As recently as three weeks ago, Kodak's stock was trading at $2.10/share, a total value of roughly $91 million.

Then, the U.S. International Development Finance Corporation said it was going to "loan" Kodak $765 million to launch "Kodak Pharmaceuticals, a new arm of the company that will produce pharmaceutical components."

Without making any comment on the validity or quality of these "components," generally a loan is something that must eventually be repaid, thus it doesn't increase the net worth of a business at all. And although we concede that a loan might help a business entity begin making new products that might ultimately raise the company's value, we wouldn't get too excited just yet.

But *somebody* got excited over that news. Because Kodak stock went from below $3/share to almost $8 the next day.

Then the gamblers really took over and ran it up to $33 the *next* day! And that's when the last guy got caught holding the bag. Over the following three days it went to $29, $22, $14, and now $10/share, where it is trading as we write this.

And, oh, by the way, the government announced this week that it will delay the approval process for that $765 million loan.

Insanity.

And don't forget Nikola, a company that's kind of a Tesla for trucks. Nikola just announced total revenues (remember, the stuff you have *before* expenses) for the last quarter of $36,000. Thirty-six thousand dollars? The stock is trading at a price that represents a market value of $14 billion! BCWM made more than $36,000 in the previous quarter and we're pretty sure we would not be able to find a buyer willing to pay us $14 billion.

Obviously, investors are speculating that Nikola has a bright future — but $14 billion?

Many (most) of these gamblers opened their new investment accounts at the market bottom in March. Their entire experience is that stocks only go up and that gambling on the stock market pays off . . . just like in 2000. We've heard numerous stories of unemployed people who have become full-time day traders, expecting this market trend to continue.

History seems to be repeating itself. And when it finishes repeating this particular chapter, you don't want be that person holding the bag.

Recently, it was reported that the U.S. economy just experienced its worst quarter on record. So how is it that the stock market has almost completely recovered? Last month, we offered a couple explanations — there aren't many great investment alternatives to stocks, and (just possibly) the stock market is banking on better times being part of the North American future.

But it could be that we are not getting a proper visual of the "stock market." The most popular quoted indicator of stock market performance is typically the Standard & Poor's 500 Index (SPX). (Quick question: How many companies are in the SPX? Answer: There are actually 505, but you are not stupid if you said 500.)

Occasionally, the SPX doesn't provide an accurate view of what most of America is experiencing. That's because the SPX is a "market cap weighted" index . . . meaning that the larger companies (such as Apple, worth $1.9 trillion) are given more credence than the smaller companies (such as H&R Block, worth only $4 billion).

Just five companies (Apple, Amazon, Google, Facebook, and Microsoft), comprising nearly 25% of the value of the index, have a much greater impact on the SPX than do the other 500 companies.

Sometimes, in order to get a better idea of what the rest of the world is really doing, it makes sense to look at the S&P 500 “**equally** weighted index,” where all 505 stocks are treated **equally** when calculating the performance of the index.

The reason for boring you with all this is that in the past twelve months, the SPX is up almost 12% and the equally weighted index is barely up at all. The two calculations differ by almost 11.5%.

The SPX tells you “all’s well with the world.” The equally weighted index says, “not so much.”

Why is any of this meaningful? Because the last time the difference between the SPX and the equally weighted index was 11.5% or more? . . . the year 2000, right before the dot-com collapse.

So don’t feel like you’ve missed out when you hear a story about someone who just started day-trading and made a fortune. Most companies are still struggling in this difficult environment and gamblers trading bankrupt stocks will eventually get burned just like they did in the dot-com era.

At BCWM, we work hard to avoid unnecessary and excessive risk. We understand the dangers that lurk in the securities markets. Even if a vaccine is developed tomorrow, the global economy will still struggle for years to recuperate from COVID-19. We continue to expect an erratic stock market and lower interest rates.

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