The Goldman Guide

Goldman SMALL CAP RESEARCH

VOLUME 7 | ISSUE 33 | AUGUST 14, 2016

INSIDE THIS ISSUE:

KEY TAKEAWAYS

⇒ *The VIX is at a 2 year low. When it is low stocks drop and it rises.*

⇒ *Best way to play it is to buy TVIX or calls on the VIX*

⇒ *Trailing 12-month P/E on S&P 500 index is highest level since 2010*

⇒ *Our pick as #1 Hillary Clinton stock is a generics drug power trading at a big discount to its EPS growth rate, and has 35% upside*

THE MAJOR INDICES

Index	Close	2016
DJIA	18,544	6.4%
S&P 500	2183	6.8%
NASDAQ	5221	4.3%
Russell 2000	1231	8.3%

(figures are rounded)

Apply To Affected Area

Statistically speaking the major indices hit new highs last week. Considering they barely budged from a week earlier and earnings season is basically over, color me unimpressed.

If ever there was a time for stocks to start a mini-fall it is now. Let's start with the VIX. According to this weekend's edition of Barron's. a boatload of calls have been purchased in recent days on the CBOE Volatility Index, or the VIX. That means a lot of money is being wagered on a market fall. And these late September calls, not something further out.

Look, a bet on the VIX year-to-date might be one of the worst investments of the year. **VelocityShares Daily 2x VIX St ETN (NYSE—TVIX—$22.63)**, our fave play on the VIX just underwent a reverse split and that may stem the bleeding. Still, on a YTD basis, the damn thing is down over 82% and recently hit a 2-year low.

Conventional wisdom might say that it is going lower. The reality is that at current levels (VIX—$11.55) the index is well below its $19 average. Moreover, chartists will tell you that when it is at an excruciating low level, it tends to make a big swing to the upside which coincides with a drop in the market. Conversely, a big jump usually means stocks are now attractive. When you are sick you apply Vicks for healing. Now, you should apply VIX calls or buy TVIX to do the same in order to stave off market declines.

The Stock Market Today

U.S. Stock Market Index Performance 8/12/2016								
Index	Close	52-Wk Hi	52-Wk Low	Hi Date	Low Date	% off High	% from Low	% Above 200-DMA
DJIA	18,576	18,638	15,370	8/11/16	8/24/15	0.3%	20.9%	6.8%
S&P 500	2,184	2,188	1,810	8/11/16	2/11/16	0.2%	20.7%	7.2%
NASDAQ	5,233	5,239	4,210	8/9/16	2/11/16	0.1%	24.3%	8.2%
Russell 2000	1,230	1,236	943	8/8/16	2/11/16	0.5%	30.4%	10.0%
Average						0.3%	24.1%	8.0%
Sources: www.BarChart.com, Goldman Small Cap Research								

It is almost like joke. Most of the indices above are up between 20-30% from their lows just six months ago. Tell me that does not give you pause. It just feels like we gotta go down before we go up, and we can go up big.

Digging Deeper

According to Factset, the current trailing 12-month P/E on the S&P 500 Index of 19.5x is the highest since 2010 when it hit 22.5x on 2/10/10. It is also currently above the 5-year, 10-year, and 15-year averages. That is a major negative, right? You tell me.

The market rose by 25% from that point until year-end. So is this all nonsense? Not at all. You can't look at numbers at face value or history without context. That year, the EPS on the S&P 500 Index jumped by 40% in 2010 compared with 2009, so of course the index went bananas.

The difference is that right now, we will be lucky to eke out a tiny bit of growth over 2015 which is a year that saw a paltry 1.3% move in the index. So, it is a scary event. Truth be told, the same index enjoyed a 15% EPS growth rate from 2010 to 2011 yet the index only rose by 2%, due in part to high valuations.

The bottom line? Expect declines followed by a strong 4Q16 with a return to EPS growth for the first time in ages, and a 13% EPS growth rate in 2017, the highest in 6 years.

Say What?

Great info, insights, and hard-hitting stories make up this week's *Say What?* feature...

The New York Post

http://nypost.com/2016/08/12/smaller-reigns-supreme-in-hedge-funds/

For those of you that invest in any funds, aside from ETFs, the smaller, the better.

Marketwatch

http://www.marketwatch.com/story/technical-analyst-stocks-have-come-through-an-internal-bear-market-2016-08-12

A good sign?.

The New York Times

http://www.nytimes.com/2016/08/14/sports/olympics/soviet-doping-plan-russia-rio-games.html?hp&action=click&pgtype=Homepage&clickSource=story-heading&module=photo-spot-region&region=top-news&WT.nav=top-news

I guess we should not be surprised.

Bloomberg

https://www.bloomberg.com/gadfly/articles/2016-08-12/trade-of-the-week-panhandling-with-a-florida-man

Florida residents, this is for you.

ZeroHedge:

http://www.zerohedge.com/news/2016-08-12/trump-deliberately-throwing-election-clinton

Conspiracy theorists, unite!

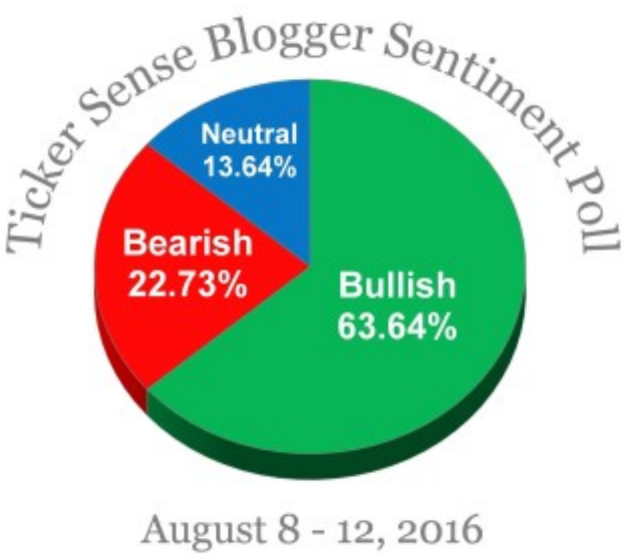
Notable Numbers

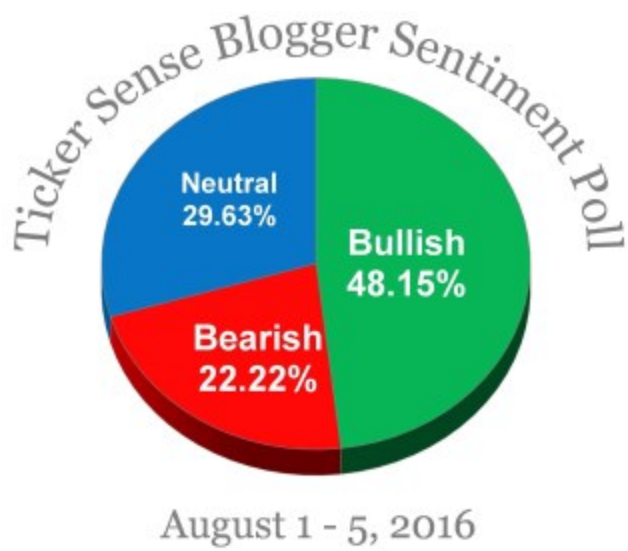
AAII Sentiment Survey (figures rounded)

	Current	Last Week	*Long Term Avg*
Bullish	31%	30%	*39%*
Neutral	42%	43%	*31%*
Bearish	27%	27%	*30%*

WTF? Basically no change in the AAII survey but big changes in the Ticker Sense poll? This time I am following the retail guys. Bulls are on the move again and correction camp is on the exit ramp, according to Investors Intelligence. Makes no sense to my behind.

We continue to see equity outflows at a slow but steady pace. At some point the numbers will change and I believe that will come with a re-valuation and a desire by foreign investors to own U.S. assets.





The # 1 Hillary Clinton Stock

I saw a "prediction machine" figure the other day that stated Hillary Clinton has an 88% chance of winning the 2016 Presidential Election. Barring any surprises, Donald Trump seems destined to lose. That got me thinking. If there was one stock I had to buy that could be a direct beneficiary of a Clinton presidency it is **Teva Pharmaceutical (NASDAQ—TEVA—$53.86—NR)**.

I have a long history with this stock. It was the first one I ever covered as an analyst and it was a monster winner even back then. I also believe I took them on one of their first non-deal roadshows in the U.S. Back then, the stock had a market cap of several hundred million. Today, it is $49 billion. To put it in perspective, if you bought $1000 worth of stock when I initiated coverage, it would be worth over $28,000 today. Anyway...here is the 411 on Teva.

Teva is the global leader in the production and sale of generics, bar none. For 25 years they have grown via M&A, most recently the $45B acquisition of Allergan's generics business. The Company also produces its own specialty branded products in the central nervous system arena (Copaxone for MS is a multi-billion dollar in sales drug, as an example) along with respiratory treatment products, cancer, women's health, and others.

The big picture for Teva as it relates to Queen Hillary is that there is nothing the Democrats (and especially Hill) like to do more than rail against high drug prices. That fits perfectly with the core Teva generics business which is the antithesis of the high priced drug market, even though they do sell some high ticket branded names.

On an investment level, the stock is trading around 10x this year's EPS and less than 9x next year's EPS despite the expected 15% growth rate. (How about a stock trading *below* its EPS growth rate for a change?) The Company has a 25% operating margin and grows revenue and EPS by the mid-teens, yet it is down 17% YTD. At 2.5 sales and 10x EPS the stock is too cheap and could jump 35% or more in a year, and once it makes a move could sustain a rise on technicals alone.

Since we are going down memory lane, Gene Marcial of Forbes (formerly BusinessWeek) did a piece recently on Teva and has quoted me many time over the years.

http://www.forbes.com/sites/genemarcial/2016/08/12/tevas-value-rises-with-transformation-into-global-pharma-giant/?

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