Goldman SMALL CAP RESEARCH

The Goldman Guide

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INSIDE THIS ISSUE:

KEY TAKEAWAYS

- ⇒ *Big swings higher last week were very narrow—it did not reach the broader market*
- ⇒ *Health care ad biotech will try and repeat the tech performance but it is likely to be short-lived*
- ⇒ *Future valuations for big cap growth stocks (Like NASDAQ 100) are now higher than the Russell 2000 which indicates moves here in conjunction with August earnings results*
- ⇒ *Teaching moments: Sentiment*

THE MAJOR INDICES

Index	Close	2015
DJIA	18086	1.5%
S&P 500	2127	3.3%
NASDAQ	5210	10.0%
Russell 2000	1267	5.1%

(figures are rounded)

Going Up?

Last week's Guide focused on the fact that earnings season is upon us and would have the greatest impact on stocks in the near term.

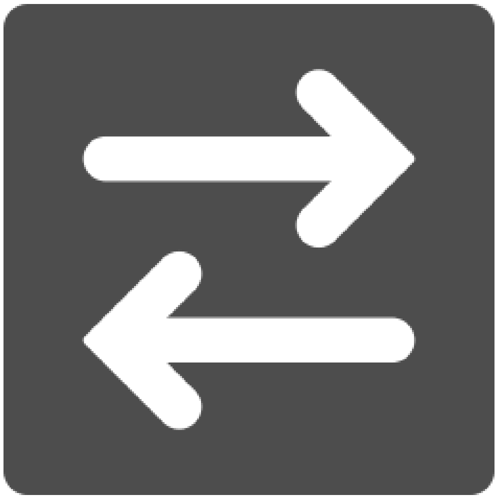
We were 100% on target but did not even dream that the NASDAQ Composite would jump by over 4% in a matter of days!

It is always amazing to see the pendulum swing so swiftly. This is why investors are always encouraged to stay invested at least to some degree because one can never tell when or the magnitude of strong bullish moves. I thought that the reports would be good and make investors feel better about the future and we would all have an opportunity to generate nice gains. Wow.

By now you know that the crazy strong earnings reports from Google (NASDAQ—GOOG) and Netflix (NASDAQ—NFLX) really helped take NASDAQ to new heights. As you will see later in this issue, it has also sparked a major and swift change investment pro sentiment which is likely to be with us, even if just for a spell.

Afraid or kicking yourself that you missed one of the greatest rallies of the year? Don't be. First, it is not over yet. Second, this move is a good thing for small stocks and they have yet to make a move higher commensurate with their larger cap growth stock brethren.

A Flip-Flop, Another Move, Small Stocks Join In



To be clear, last week's sharp moves higher were not necessarily broadly based. In fact, they were largely contained to the big names that reported and some of their peers. So, if stocks in your portfolio did not move much, take comfort that you are not alone in this regard. That does not mean it will not happen soon enough, however.

The first thing likely to happen, we believe is a move in big pharma and biotech stocks that release quarterly financials this week (such as Celgene—NASDAQ—CELG and Bristol-Myers—NYSE—BMY). Surely, investors will run these shares higher if the earnings results warrant it. However, since this group has been on fire for so long, and the figures are unlikely to be better than the tech numbers from last week, it will probably be a short-lived rally.

Interestingly, one benefit of the mega-cap NASDAQ rally is the way valuations have flip-flopped. For months and months, the forward 12-month P/E on the Russell 2000 Index has consistently been higher than that of the NASDAQ 100, which is not unusual. After last week, the NDQ P/E is now higher than the Russell! (19.6x vs 19.1x)

This means, that the next group to move is small caps. They report later than their large cap brethren anyway but for anyone concerned that valuations are getting ahead of themselves during this typical short term summer rally, small is good!

By the way, the small stocks, for the most part have lagged in July, with the exception of IPOs. Since most report in August, we see a brief rise higher in general for the next few weeks before the usual fall swoon, and end of year jumps.

Say What?

This week, we have a combo of news on two key sectors, along with very topical news items.

NY Post

http://nypost.com/2015/07/18/obama-has-been-collecting-personal-data-for-a-secret-race-database/

Wake up, read, withhold outrage until later.

The Washington Post

http://www.washingtonpost.com/posteverything/wp/2015/07/17/black-america-has-been-playing-by-white-americas-rules-if-we-want-reconciliation-its-time-for-white-america-to-share-the-burden/?hpid=z10

And now, to be fair, another viewpoint...from Jeff Bezos' newspaper

Marketwatch

http://www.marketwatch.com/story/abc-denver-affiliate-to-air-first-ever-us-television-cannabis-commercial-2015-07-17

Yes, it is a real market and we all better get used to it.

Investor's Business Daily

http://news.investors.com/technology/071815-762183-q2-earnings-preview-of-biib-nvs-bmy-lly-vrx-abbv.htm?ref=HPLNews

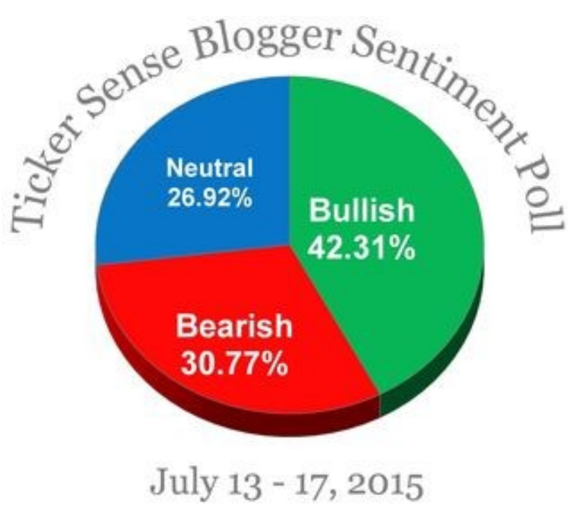
Will they have the same impact on pharma that tech did on tech last week?

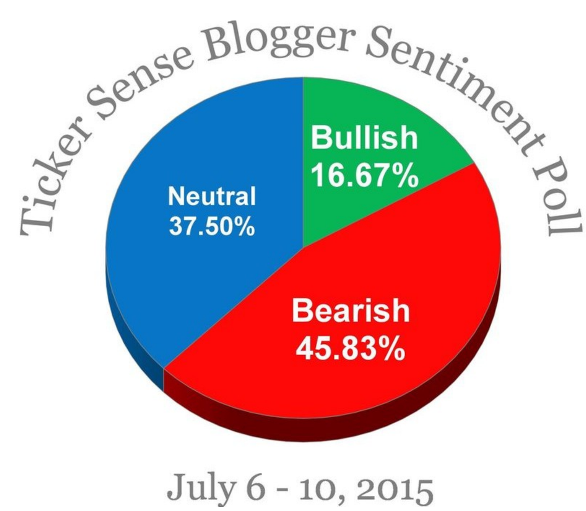
Just the Stats!

AAII Sentiment Survey (courtesy of AAII.com, figures rounded)

Last Week	Long Term Avg
Bullish 31%	39%
Neutral 46%	31%
Bearish 23%	30%

Well, we thought that there would not be much movement from one week to the next in the TickerSense Poll. We could not be more wrong! It just goes to show you how quickly things change on a dime, including investor pro sentiment. We knew we were reaching





bottom of the bearish sentiment, but big moves are usually followed by common sense.

In this case, common sense is likely to mean higher Neutral and lower Bearish ahead with few changes in the Bullish category.

Movers and Changers

We have hinted at changes ahead in the small cap pick we have made this year in The Goldman Guide. Now is the time to be a bit more specific before we pull the trigger.

Skechers USA (NYSE—SKX—$121.25 –NR) is one of our big winners, up over 81% year-to-date. The Company is due to release its quarterly financials in the next week. We would be sellers on the news and may change our sentiment on the share, due merely to valuation. The stock currently trades 28x this year's EPS and 22x next year's EPS. While that is still cheaper than Under Armour (NYSE—UA), which is on fire, it is above the P/E afforded Nike (NYSE—NKE) and has been getting pricey for a while.

Voltari (NASDAQ—VLTC—$9.89—NR), the Carl Icahn-owned company, made another big move late last week. It is another "sell into strength" candidate. It reached a cray $21.00+ earlier this year and if it approaches $15 let loose!

Last week, we highlighted a company called Travelzoo (NASDAQ—TZOO) that was due to report financials. We cautioned that due to the wide variance in estimates it would be very difficult for the stock to rally and that the outcome of its results could be a negative surprise. Sure enough, not only were comparisons from last year down, as expected, but they did not meet current expectations. Consequently, the stock dove 20%.

Key Lesson: If there is a wide difference in analyst expectations, especially when it is followed by fewer than 5 analysts, there is more risk than meets the eye!

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