Goldman SMALL CAP RESEARCH

# The Goldman Guide

VOLUME 5 | ISSUE 18 | MAY 4, 2014

**INSIDE THIS ISSUE:**



### *KEY TAKEAWAYS*

- *GDP growth is weak.*
- *No one is fooled by declining unemployment rates anymore. The real number is workforce participation rate.*
- *A tale of 2 markets means big NASDAQ names are to be avoided but micro caps should be accumulated.*
- *Blue chips may be the best performers for the interim.*
- *The market can't seem to rise without help from housing.*
- *We may not see a sustained rally until after midterm elec-*

### *KEY STATISTICS*

| Index | Close | 2014 |
|---|---|---|
| DJIA | 16513 | -.03% |
| S&P 500 | 1881 | 1.8% |
| NASDAQ | 4124 | -1.3% |
| Russell 2000 | 1129 | -0.3% |

(figures are rounded)

## The Secret To Market Growth

***H****appy Cinco de May to everyone. In honor of the celebration, we elected to highlight trends in the market including the real key to stock market growth.*

**Economic growth is not exactly a confidence builder.**

The recent economic news is anything but pretty. Last week, the U.S. Commerce Department reported a preliminary estimate for first quarter 2014 GDP performance and the figures, if accurate, reflect  the smallest quarterly gain in three years. Although no one was anticipating a bang-up quarter due to the poor weather in the eastern half of the country during the period, the 0.1% gain barely registers any growth at all.

Moreover, big gains for the period such as in consumer spending are masked by the higher fees paid to utilities so the actual numbers might be even poorer.  When one lifts up the hood the picture appears really ugly with business equipment spending and government spending declining , along with home construction.

Against this backdrop, economists are now forced to reduce the GDP growth for the year which may have an impact on the quantitative easing strategy employed by the Federal Reserve. On the plus side, despite the announced $10 billion drop in bond buying by the Fed, stocks staged a mild rally on the news for the first time in months. Still...

**...even good news doesn't help.**

Yes, the unemployment rate is now 6.3%, a 5 year low. But you and other investors can see right through this scam number now. With 92 million out of work, and the workforce participation rate steadily declining, the sleight of hand didn't help stocks and may be an impediment going forward.

# *A Tale of Two Markets*

The dramatic shift in stocks the past six weeks or so has highlighted a serious dichotomy in equities: “The Haves” and “Have Nots” and the spread between the two is likely to widen rather than narrow. If you wish to be on the right side of the aisle, you should probably first recognize the current trends.

The “Haves” are represented by the 30 components of the Dow which closed at a record at one point last week. Interestingly, this event coincided with the Federal Reserve indicating its plans to cut back on its quantitative easing program by reducing the bond buying by $10 billion to $45 billion, beginning in May, as we mentioned above. For bulls, this is potentially a decent sign for blue chips as it could help reduce some volatility.

The notable “Have Nots” are former NASDAQ darlings Twitter (NASDAQ – TWTR) and LinkedIn (NASDAQ – LNKD), which are both down 40-50% from their year highs achieved just a few short weeks ago. Even with the drops, both stocks are trading at nosebleed levels based on next year’s P/E. LinkedIn trades 55x Wall Street 2015 forecasts while Twitter’s P/E is actually above 155, which is ironically greater than the 140 characters one can use in a single tweet. (Perhaps when it drops below 140 some will think it is a bargain…)

Other “Have Nots” that seem to have fallen under the radar include the micro cap segments. Volumes are down in the micro cap sector by around 50% as investors have been paralyzed and spooked by the recent volatility. This precipitous drop has prompted market makers to widen spreads which exacerbates the problem further. In the absence of higher volume where they can make money, the market makers raise offers on buys and lower them on sells to make up for the reduced activity. As a result, it is not uncommon to see a stock trade up or down 10% or light activity.

Going forward, the blue chip “Haves” are likely to continue their upward path given their solid EPS growth and reasonable valuations. Conversely, the NASDAQ losers that still trade at ridiculous premiums will probably not see accumulation until valuations change. As volume slowly creeps higher on underfollowed micro caps, accumulation and higher prices are more likely to return a lot sooner in this segment than with the more well-known NASDAQ names.

## *The Trigger...*

**...will be housing. It has to get better for the market to move higher.**

With so much of our economy dependent upon housing and construction, these segments must see real growth in order for the shaken stock market players to regain their mojo and become more engaged. Unfortunately, housing stocks and mortgage applications figures have been terrible, partly due to the poor Q1 weather as well as higher interest rates.

For the bears, the weak GDP combined with declining, new mortgage applications spells more trouble for stocks and a confirmation that the current market valuation is too high and will decline by 10% or more from current levels. For the bulls, the fact that first quarter earnings thus far are not terrible and that the signs for the second quarter appear promising bode well for equities going forward, thus confirming that valuations are reasonable.

For me, I believe that valuations are indeed a bit high and while a better second quarter will help stocks bounce back, we may not really see a prolonged rise in stocks again until after the mid-term elections in the fall, unless we see consecutive, monthly growth in the housing and mortgage segments.

Have a great week!

# The Goldman Guide

1498 Reisterstown Road, Suite 286 Baltimore Maryland 21208 Phone: 410.609.7100
info@goldmanresearch.com www.goldmanresearch.com

Launched in May 2010, *The Goldman Guide* is a free weekly publication of Goldman Small Cap Research and is written by Founder Rob Goldman with contributions from the GSCR contributor team. This non-sponsored investment newsletter seeks to provide investors with market, economic, political and equity-specific insights via an action-oriented, straight to the point approach. No companies mentioned in this newsletter are current sponsored research clients of the Company or its parent, unless noted, With rare exceptions, all companies or investment ideas mentioned in this publication are publicly traded stocks listed either on the NYSE or the NASDAQ. Goldman Small Cap Research members and contributors' bios, certifications, and experience can be found on our website: www.goldmanresearch.com .

**Disclaimer**

This newsletter was prepared for informational purposes only. *Goldman Small Cap Research*, (a division of Two Triangle Consulting Group, LLC) produces non-sponsored and sponsored (paid) investment research. Goldman Small Cap Research is not affiliated in any way with Goldman Sachs & Co.

The Firm's non-sponsored research publications category, ***Select Research,*** reflects the Firm's internally generated stock ideas, along with economic, industry and market outlooks. In virtually all cases, stocks mentioned in **Select Research** offerings are listed on the NYSE or the NASDAQ. Publications in this category include the weekly newsletter *The Goldman Guide*, daily Market Monitor blogs, Special Reports, and premium products such as *The 30-30 Report*. Goldman Small Cap Research analysts are neither long nor short stocks mentioned in this newsletter.

***Opportunity Research*** reports, updates and Microcap Hot Topics articles reflect sponsored (paid) research but can also include non-sponsored micro cap research ideas that typically carry greater risks than those stocks covered in Select Research category. It is important to note that while we may track performance separately, we utilize many of the same coverage criteria in determining coverage of all stocks in both research formats. Please view the company's individual disclosures for each engagement, which can be found in company-specific ***Opportunity Research*** reports, updates and articles.

Goldman Small Cap Research has not been compensated for any content in this issue.

All information contained in this newsletter and in our reports were provided by the companies mentioned via news releases, filings, and their websites or generated from our own due diligence. Economic, market data and charts are provided by a variety of sources and are cited upon publication. Stock performance data is derived from Yahoo! Finance. Our analysts are responsible only to the public, and are paid in advance to eliminate pecuniary interests, retain editorial control, and ensure independence.

The information used and statements of fact made have been obtained from sources considered reliable but we neither guarantee nor represent the completeness or accuracy. *Goldman Small Cap Research* did not make an independent investigation or inquiry as to the accuracy of any information provided by the Company, other firms, or other financial news outlets. *Goldman Small Cap Research* relied solely upon information provided by companies through filings, press releases, presentations, and through its own internal due diligence for accuracy and completeness. Such information and the opinions expressed are subject to change without notice. A *Goldman Small Cap Research* report, update, article, blog, note, or newsletter is not intended as an offering, recommendation, or a solicitation of an offer to buy or sell the securities mentioned or discussed. This newsletter does not take into account the investment objectives, financial situation, or particular needs of any particular person. This newsletter does not provide all information material to an investor's decision about whether or not to make any investment. Any discussion of risks in this presentation is not a disclosure of all risks or a complete discussion of the risks mentioned. Neither *Goldman Small Cap Research*, nor its parent, is registered as a securities broker-dealer or an investment adviser with the FINRA or with any state securities regulatory authority.

ALL INFORMATION IN THIS REPORT OR NEWSLETTER IS PROVIDED "AS IS" WITHOUT WARRANTIES, EXPRESSED OR IMPLIED, OR REPRESENTATIONS OF ANY KIND. TO THE FULLEST EXTENT PERMISSIBLE UNDER APPLICABLE LAW, *TWO TRIANGLE CONSULTING GROUP, LLC* WILL NOT BE LIABLE FOR THE QUALITY, ACCURACY, COMPLETENESS, RELIABILITY OR TIMELINESS OF THIS INFORMATION, OR FOR ANY DIRECT, INDIRECT, CONSEQUENTIAL, INCIDENTAL, SPECIAL OR PUNITIVE DAMAGES THAT MAY ARISE OUT OF THE USE OF THIS INFORMATION BY YOU OR ANYONE ELSE (INCLUDING, BUT NOT LIMITED TO, LOST PROFITS, LOSS OF OPPORTUNITIES, TRADING LOSSES, AND DAMAGES THAT MAY RESULT FROM ANY INACCURACY OR INCOMPLETENESS OF THIS INFORMATION). TO THE FULLEST EXTENT PERMITTED BY LAW, *TWO TRIANGLE CONSULTING GROUP*, *LLC* WILL NOT BE LIABLE TO YOU OR ANYONE ELSE UNDER ANY TORT, CONTRACT, NEGLIGENCE, STRICT LIABILITY, PRODUCTS LIABILITY, OR OTHER THEORY WITH RESPECT TO THIS PRES-