

INSIDE THIS ISSUE:

All Signs Point to Smallville
A Virgin No Longer

KEY TAKEAWAYS

- ⇒ *Investors are stuck in neutral and are ignoring the small cap buy signs*
- ⇒ *Big cap is not the place to be due to economic issues valuation while small stocks are the beneficiaries of market negatives*
- ⇒ *Airlines is one sector that has great operating leverage*
- ⇒ *VA's founder is one of the most recognized faces and names in business and the stock is dirt cheap*

KEY STATISTICS

Index	Close	2015
DJIA	17749	-0.0%
S&P 500	2053	-0.0%
NASDAQ	4872	2.9%
Russell 2000	1232	2.2%

(figures are rounded)

WHAT THE MARKET IS TELLING YOU TO BUY

Does recent trading mean that investors should beware the ices of March? We don't think so. Ask the average investor and the current sentiment is more like "to be or not to be"—or in the current environment, "to buy or not to buy, *that* is the question."

One example of this stance is the change in the latest AAI Investor Sentiment Survey. There was a big jump in the Neutral category and slight increase in the Bearish category, with a decline in the Bullish sentiment. In fact, the current 43% Neutral sentiment is substantially higher than the 31% long term average, indicating investors know not what to do..

This paralysis is fueled by concerns over rising rates (which we outlined last week), the rising dollar, weak oil prices, and fair value for equities. As we head into the most exciting week of the year where millions of Americans will fill out their brackets by picking winners in the NCAA Basketball Tournament, we see no reason not to be decisive and buy. What is most important—it is telling us what to buy, and not to buy.

Signal #1: Rising rates.

In our view, the Fed is not in a rush to raise rates. They know that the "favorable" unemployment numbers are as fake as my friend's wife's orgasms. Higher unemployment should mean higher GDP growth but it simply is not there. And, inflation? Key non-gasoline prices are *de*-creasing.

Look, rates will rise, but not today. It will likely occur mid-year and this event is already reflected in stocks. Interest-rate sensitive stocks like utilities are down and financials, which benefit from higher rates, is the #1 or #2 biggest sector weighting in some leading indices and ETFs. Regardless, rising rates means growth stocks are the place to be.

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Signal #2: The Rising Dollar

Investors freaked out late last week as the dollar rose sharply, especially against the euro, given the central bank's recent and proposed measures. A reasonably strong dollar is a good thing, but too strong can hurt multinationals' sales abroad, since home country currencies buy less U.S. goods. When sales in these currencies are translated into dollars it also has a negative effect on big U.S. corporations. Therefore, big cap stocks in the U.S. can fall under prolonged pressure. On the plus side, a high value dollar will attract foreign investments, propping up our values. Still, investing in companies with no sales abroad are not impacted by the dollar rise. Thus, small growth companies are likely to be the beneficiary of this trend and more dollars should move into this category.

Signal #3: Weak Oil Prices

U.S. GDP growth and pricing power are negatively impaired by the continued drop in oil prices but, big buyers of oil and gas that have thin margins, such as airlines, trucking, and other transport companies benefit. Perhaps consumers will finally use these bucks for additional spending cash instead of socking it away, thus helping consumer discretionary companies. The market is telling us that is not yet the case. Moreover, declining prices indicate that consumer companies are having pricing issues. Once this abates, this sector will be in favor. Until then, there is not a great deal of reason to buy into the space aside from some cheap apparel companies due to seasonality.

Signal #4: Fair Value for Stocks

Stocks are indeed likely fairly valued, on a long term basis. Still, I would venture to say that there is more risk with big caps than small caps given the concerns outlined above. For example, the S&P 500 Index trades at a 12-month forward P/E of 17.55 while the NASDAQ 100 trades 18.75x. The Russell 2000 trades only ever so slightly higher, at 18.92x. This is interesting especially when one takes into account that on a YTD basis, the index is up 2.5%, the same as the NASDAQ 100, yet the RUT does not have the advantage of the heavy weighting of big performers such as Apple (NASDAQ—AAPL) and Amazon (NASDAQ—AMZN) which are up an average of roughly 16%! Plus, this index is crazy tech-heavy, while the RUT's biggest sector weighting is financials, followed by health care and technology. The bottom line? It is understandable if investors are ambivalent about big cap. After all, given current trends, small is where it's at!

A Virgin No Longer

Now that we have determined that the place to be is in the small cap growth category, are there stocks that fulfill the previously outlined criteria?

- ◆ Since rates have not yet risen, its borrowing is not yet impacted.
- ◆ A rising dollar does not hurt the stock.
- ◆ It is definitely aided by falling oil.
- ◆ It trades at a reasonable valuation with solid brand recognition.

The answer is affirmative of course and there is even one that has a bigtime face of the company to lead the brand. Plus, since I already made an allusion to orgasms, this week's featured stock is perfect for this issue.

Virgin Airways Inc. (NYSE—VA—\$34.77) is known for its mood-lit cabins, three beautifully designed classes of service and innovative fleet wide amenities — like touch-screen personal entertainment, Wi-Fi and power outlets at every seat, **VA** has built a loyal following of flyers and earned a host of awards since launching in 2007 — including being named both the "Best U.S. Airline" in *Condé Nast Traveler's* Readers' Choice Awards and "Best Domestic Airline" in *Travel + Leisure's* World's Best Awards for the past seven consecutive years.

Founded and 25% owned by famed businessman Richard Branson, **VA** went public in November in one of the largest airline IPOs in history, to much fanfare. The Company is very forward thinking in its technology offerings and approach and it is already winning many fans in the U.S. The stock is cheap now that is down about 20% off of its December 2014 high. At current levels the stock trades 7.7x 2015 estimated EPS, despite its newfound operating leverage. Now that it has some trading history behind it, and it benefits from the factors above, we believe that accumulation will occur in the near term. We expect the stock could approach its \$45 high in the coming months, which still reflects only a 10x multiple on FY15 earnings per share.



The Goldman Guide

1498 Reisterstown Road, Suite 286 Baltimore Maryland 21208 Phone: 410.609.7100

info@goldmanresearch.com www.goldmanresearch.com

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