The Goldman Guide

Goldman SMALL CAP RESEARCH

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INSIDE THIS ISSUE:

KEY TAKEAWAYS

- ⇒ *Post-election insanity is just not helpful*
- ⇒ *Fears of a post-election bubble are overblown but frothy valuations for certain indices are not*
- ⇒ *Year-end profit taking, portfolio re-balancing are about to take hold. See how they impact stocks.*
- ⇒ *Big pharma may be the best play in the near term. See valuations of key names*
- ⇒ *NASDAQ stocks are the best value and S&P 500 stocks could be the best GARP/value versus small cap*

THE MAJOR INDICES

Index	Close	2016
DJIA	19171	10.0%
S&P 500	2192	7.2%
NASDAQ	5256	5.0%
Russell 2000	1314	15.7%

(figures are rounded)

Give It A Chance

There is no denying that since the November election, there has been a tangible increase in racist and anti-Semitic attacks. And that is just wrong. It's also weird for me to drive down the road and see a guy holding up a sign that say: "We elected a racist President and I won't accept it." I wondered out loud if he will be standing there for the next 4 years. It also made me think of the ABBA hit single "Take a Chance on Me." Shouldn't we give President-elect Trump a chance?

On a related note, is it us or has the animosity between the Trump and Clinton supporters increased post-election? From complaining about the electoral college to accusations of voter fraud, the contentiousness is still running hot. One of the more comical that illustrates this paranoia is the rant by **PepsiCo (NYSE – PEP)** CEO Indra Nooyi.

Check out the link below.
http://www.businessinsider.com/pepsico-ceo-mourns-trump-win-2016-11

The country elected a president not an all-powerful dictator who can order someone to take you away based on your sexual orientation! This mood is one of the overriding reasons Trump won. A great number of people were tired of Obama wielding his executive power to circumvent Congress, and Clinton offered no rebuke. The Trump supporters are not innocent either. The out-right rejection of Mitt Romney illustrates this, as he is a moderate and ideal for Secretary of State, in our humble opinion. Finally, the vindictiveness over the Clinton email scandal and call for prosecution at all costs is yet another example. The precedent for leniency was established from the other side forty years ago, when the Democrats did not pursue Nixon after his resignation. In summary, we all need to take a Xanax®!

The Stock Market Today

U.S. Stock Market Index Performance 12/5/2016								
Index	Close	52-Wk Hi	52-Wk Low	Hi Date	Low Date	% off High	% from Low	% Above 200-DMA
DJIA	19,171	19,225	15,451	11/30/16	1/20/16	0.3%	24.1%	6.3%
S&P 500	2,192	2,214	1,810	8/15/16	2/11/16	1.0%	21.1%	3.8%
NASDAQ	5,256	5,404	4,210	11/29/16	2/11/16	2.7%	24.8%	4.7%
Russell 2000	1,314	1,347	943	11/25/16	2/11/16	2.4%	39.3%	11.5%
Average						1.6%	27.3%	6.6%
Sources: www.BarChart.com, Goldman Small Cap Research								

There is a ton of talk about a pending post-election bubble, and doom and gloom once the new Administration takes office. That may all be true. Unlikely, but could happen. What is more reasonable is that we went too far too fast, as is often the case. The pendulum swings too far in one direction and then does the same in the other. Still, dig on this. If I was a betting man, I would largely stay away from the mega caps and small caps. Yes, small caps. But, just for a spell.

As you can see from the table, all indices are up big from their February lows. But, the Russell 2000 Index is killing it! From the low on 2/11/16 to the high on 11/25/16 the index is up 42.8%! Wow. This is December and I see some year-end profit-taking in our future which could put pressure on stocks, rather than this bubble nonsense. Moreover, institutions are in the throes of portfolio re-balancing and restructuring for next year which adds to volatility. So, the net 2 weeks could be a bit dicey, followed by fun.

As to the DJIA, it is up 10% year-to-date and with a RSI over 73, it is frothy. Frankly, what appears to be the best buys are NASDAQ stocks, where some of the profit-taking may have even started. I would not be surprised to see this index offer the net near term gains.

Play of the Day

Earlier we mentioned Xanax, the treatment offered by **Pfizer, Inc. (NYSE – PFE)** to combat panic and anxiety. This was calculated as right after the election we noted that the pharmaceutical and biotech industries were set to take off with what most believe will be a reprieve from Obamacare from the Congress and President Trump. Below is a simple table offering some basic statistics from both U.S. and international big pharma firms to give you a 10,000-foot view.

Miscellaneous Large Cap Pharma Metrics

(Source: Yahoo! Finance)

Company	Ticker	Market Cap	Price	Dividend Yield	Forward P/E	ROA	ROE	Operating Margin	Profit Margin
Pfizer, Inc.	PFE	$192B	$31.63	3.8%	12.1	5.2%	9.5%	27.3%	11.6%
Eli Lilly and Company	LLY	$71B	$67.71	3.1%	17.1	6.0%	15.8%	17.1%	11.7%
Merck & Co., Inc.	MRK	$169B	$61.13	3.1%	15.7	6.0%	12.3%	24.0%	13.8%
Sanofi S.A.	SNY	$108B	$40.02	4.2%	13.6	--	--	21.8%	12.3%
GlaxoSmithKline plc	GSK	$94B	$37.70	5.0%	13.7	6.9%	4.8%	23.3%	1.1%
AstraZeneca plc	AZN	$67B	$25.89	3.5%	14.1	3.5%	14.9%	13.8%	10.3%
Bristol-Myers Squibb Co.	BMY	$94B	$55.96	2.7%	18.8	10.0%	22.0%	28.3%	18.2%

We will leave the investigation of Company pipelines up to you, but at first blush, **PFE** might be a strong candidate for a stock pick while **AZN** might be one to avoid. An important metric that we did not consider which is along the lines of ROA and ROE is Return on Investment Capital (ROIC), a popular valuation metric for pharmaceutical firms. Finally, if you do not want to stock pick there is a plethora of ETF's to choose from. **iShares US Pharmaceuticals (NYSE – IHE)** offers exposure in Dow Jones size firms. The **ETF SPDR S&P Pharmaceuticals (NYSE – XPH)** offers a broader exposure into biotech and the small cap space in this sector. Whatever you decide, just remember we are a country of laws, and everyone needs to respect each other and chill out!

Say What?

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

The New York Post

http://nypost.com/2016/12/03/market-manipulation-creates-serious-risk-for-short-term-gain/

A must-read

USA Today

http://www.usatoday.com/story/money/personalfinance/2016/12/04/overdraft-coming-prepaid-cards-heavy-restrictions/94763686/

A terrible idea. Sign of a sub-prime lending top?

Marketwatch

http://www.marketwatch.com/story/the-trump-rally-in-the-stock-market-may-be-turning-into-a-bubble-2016-12-03

Overblown, but instructive, pardon the pun.

Bloomberg

https://www.bloomberg.com/news/articles/2016-12-02/fewer-women-are-managing-funds-in-the-u-s

A little surprising.

ZeroHedge:

http://www.zerohedge.com/news/2016-12-04/these-countries-have-nearly-eliminated-cash-circulation

Interesting news and perspective.

Notable Numbers

AAII Sentiment Survey (figures rounded)

	Current	Last Week	*Long Term Avg*
Bullish	44%	50%	*39%*
Neutral	31%	34%	*31%*
Bearish	25%	28%	*30%*

I think even the most bullish investor has to get nervous when half of all respondents to the AAII Investor Sentiment Survey categorize themselves as Bullish. So, with a down week and talk of a post-election bubble following the big rise, it is no surprise that a bunch of Bulls went into huddle mode, either in the Neutral or Bearish category. Expect further attrition in anticipation of modest declines.

The Investor Intelligence figures suggest that Bulls are over 50% also and that the ratio of Bulls to Bears is around 2.5 to 1. A little excited, are we?

Look, for the week ended 11/16/16, equity fund inflows experienced a whopping $23 billion inflow. The money had to be put to use so the market jumps were, in effect, a fait accompli. Since then, the inflows/outflows are flattish the past 2 weeks and may need more inflows to sustain market increases.

Yes, we lean toward GARP stocks and feel most comfortable with this approach. But, geez...the 12-month forward P/E on the Russell 2000 Index is a whopping 19.4x versus 18.4x for the S&P 500. Interestingly, once 4Q's results are out, the multiple on the S&P 500 will enjoy a drop because the poor year-over-year comparisons for energy stocks will turn positive, thus raising EPS and reducing P/E. The Russell 2000 will enjoy that as well but only to a small extent. Therefore, in small caps, it is time to be a cautious an careful stock picker.

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