The Maleficent 7

For months, I warned that the market trend was positive, but risks were elevated. One of the biggest risks to the market was poor breadth. A handful of stocks were driving the market's returns. This small group of stocks' outperformance was masking bearish trends in many stocks even as the market-cap-weighted indexes were marching higher.

Now, those stocks have broken. The Magnificent 7 has turned into the Maleficent 7 (due to my lack of creativity in this moment, I am stealing that phrase from Goldman Sachs).

Here's a chart from March 11, 2025, that shows the start of the Magnificent 7 breakdown.

Exhibit 1: The Magnificent 7 have lagged during the recent drawdown

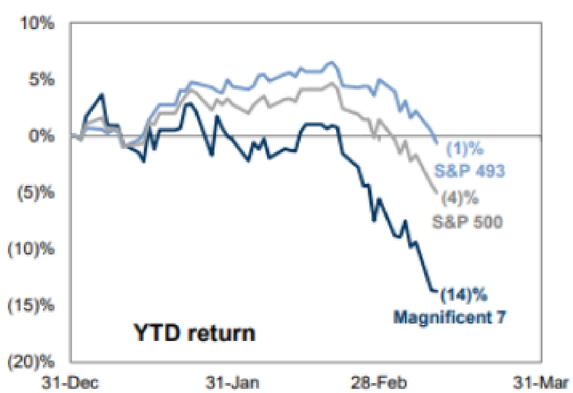
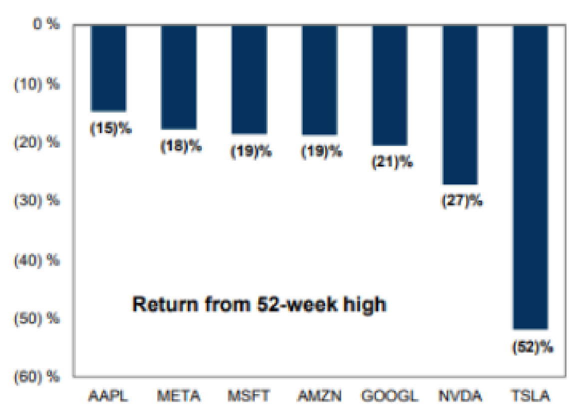


Exhibit 2: Performance of the Magnificent 7 vs. 52-week high



Source: FactSet, Goldman Sachs Global Investment Research. As of March 11, 2025.

Since then***, it's gotten worse, and the group is well into bear territory. Apple is down 13.0% on the year, and 16.2% off its 52-week high. Nvidia slid 18.3% in 2025 and is 28.4% off its 52-week high.

Interestingly enough, since "Tampon Tim," the Governor of Minnesota, cheered Tesla's dramatic fall, the stock has bounced back 17.3%. However, it's still 46.1% below its 52-week high.

Blood is everywhere. While my strategies navigated the stealth bear market quite well, the recent broad-based, aggressive selling has also hit them.

They have not been spared.

Nothing has as risk assets as a whole have taken it on the chin.

Bitcoin has been cratered 21.3% since it hit a new high in November 2024.

Several themes I highlighted during the stealth bear market phase included:

- Own value stocks versus Growth stocks
- Own foreign Stocks versus U.S. stocks
- Own small stocks versus Large stocks
- Own the average stock in the S&P 500 versus the S&P 500

Value is up about 1% on the year compared to a 10.2% loss in growth stocks. Meanwhile, foreign stocks are up 7.9% in 2025 compared with a 5.2% loss in the S&P 500. Emerging markets are up 3.7%.

Small stocks continue to perform relatively poorly, down 9.2% on the year compared to the 5.2% loss in the S&P 500.

Lastly, the average stock in the S&P 500 is down about 1.8%.

So, most of those spread trades have narrowed nicely. At least thus far in 2025.

Those trades have saved me. Gold has, too. I discussed my gold position prior to the election.

During the recent meltdown, I discussed buying the dip. The market went from oversold to very oversold to very, very oversold.

I stopped once market sentiment – instead of just price action – reached extremely bearish levels.

My most significant allocation was to the equal-weight S&P 500 (ticker: RSP) and other trades listed in the spread trades above.

I don't know if I'm "right" until after the fact. The market rallies only to get pressed again. It could be finding a bottom, or that bottom could fall out from beneath it. *A lot* of speculative money was wagered on margin. That will need to come to an end before anything positive can happen.

For now, I will continue to wait and see if the S&P 500 hits 5,250.

Another thing that will likely happen is a change of leadership. Generally, the leaders from one market cycle are not the leaders of the next.

This makes sense in the context of capitalism as the key drivers of the markets and economy change over time.

I found the following charts helpful in that regard.

First, the forward multiples of the top five companies today are well below the Dot Com Bubble. More interestingly, they're also well below where they were five years ago. To some degree, the stocks grew into their valuations. Other than in 2022, not much market bloodshed was required to keep the market moving along.

Figure 1. Top five tech companies 1997-2002 and 2019-2024, average 12-month forward price-to-earnings multiple

Source: Bloomberg, Man Group calculations, as of February 2025.

The following chart is fascinating.

The chart nicely highlights the leadership from one cycle to the next. As I noted, market leadership often changes.

The Nifty Fifty stocks of the late 1970s were gone by the Dot Com Era, and the leadership has changed once again.

One exception is Microsoft, which lost relevance only to emerge once again as a dominant force. It's rare. Kudos to Microsoft!

Figure 5. Share of top five companies by market cap in S&P 500

Source: Deutsche Bank, as of 31 January 2025.

From here, it will be important to watch to see if leadership changes signal a new phase of the market.

On any sustained bounceback, I expect two things to happen.

First, small companies will outperform. This bodes well for my strategies because they tend to be focused on smaller companies (but not always). Second, lower-quality companies will outperform. This does not favor my strategies because the models require high-quality financials. To overcome that, though, the momentum factor is designed to help to some degree.

It will be interesting to see if stocks can find any relief this week as the tariffs hit. I don't know if they were looking for any reason to sell off, but the tariff noise certainly provided one.

A few weeks ago on March 5th, I noted to a subscriber in a private email that I thought India might drop their tariffs against the U.S. I now see that they might. Will they? Will other countries follow?

Possibly there could be some clarity regarding tariffs. If so, buying the dip is the right play. Otherwise, I'll revisit my allocations at 5,250 on the S&P 500.

The last point is that we are at the end of the first quarter, and investor sentiment is as bad as it has been since 2022. If I were the CFO of a public company, I would stuff all the worst aspects of the business as possible into this quarter. That is called “throwing in the kitchen sink.”

I would talk everything down as much as I could. This would allow me to set up the financials for a good run for 18 – 24 months (it's all legal).

So, we might see a lot of bad news from companies. They may guide down their earnings prospects, which could lead to a lot more volatility in stocks over the next handful of weeks. But that would also be helpful in clearing a path to much better performance going forward.

****calculated for March 27, 2025*