Cetera® Investment Management LLC

The '90s Called:

10 Ways Today Is Like, Totally the 1990s—And Why It's Not

Cetera®

If you've been feeling a little déjà vu these days, it's with good reason. The '90s are making a comeback—or so it would seem. Both then and now, we saw a reboot of *Star Wars* films, are watching Jerry Seinfeld on TV (*Seinfeld* then, *Comedians in Cars Getting Coffee* today), and became fascinated with the evolution of digital technology. But the similarities aren't just cultural—today's market environment also has some striking parallels to that previous era. Both in the '90s and the current decade, value stocks have lagged significantly behind growth stocks, tech stocks have led the bull market, and U.S. equities have outpaced international stocks. And while there are also stark differences, the long list of commonalities with the 1990s is noteworthy.

So much so, in fact, we've identified 10 areas in which current market conditions closely resemble that heady decade that ended nearly 20 years ago. We share their similarities and differences, what we think this means for the markets—and what we think you should keep an eye on in the coming months.

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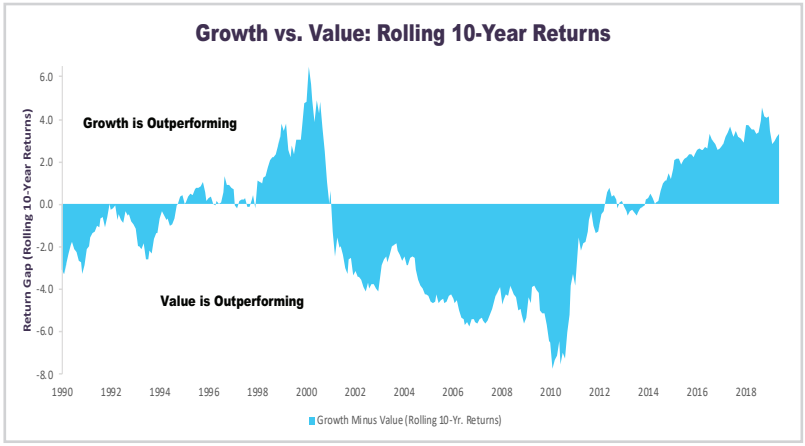
#1: Growth Outperforming Value

Growth stocks have lately outperformed value stocks for the longest stretch and widest margin since the late 1990s, albeit not as extremely. Outsized gains in the technology sector were, in both periods, the impetus for strong growth stock performance.



Source: Cetera Investment Management, Morningstar, Russell Investments. Rolling 10-year returns are annualized. Growth stocks are represented by the Russell 1000 Growth Index and Value stocks are represented by the Russell 1000 Value Index. Data as of 5/31/2019.

1990s

- Over the duration of the entire 1990s bull market, growth outperformed value by 5.8% annualized.
- Over the final 18 months of the 1990s (July 1998 to December 1999), the Russell 1000 Growth Index was up 53.4%, compared to a 10.7% gain for the Russell 1000 Value Index.

Today

- In the current bull market, growth stocks have outperformed value stocks by 2.7%, annualized through May 2019.
- Growth stock outperformance intensified in the second half of this bull market, where growth stocks have outperformed value stocks by 5.8% annualized over the last five years.

What Does It Mean?

The relationship between growth and value stocks is cyclical. Value stocks have produced superior long-term performance, but there have been long stretches of underperformance, as was the case in both the 1990s and the current bull market. Strong value outperformance lasted for more than a decade following the 1990s and if history is any guide, we may see value stock outperformance again in the next cycle.

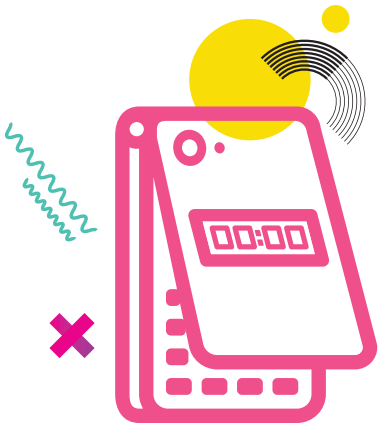
BULL MARKETS OF ALL STRIPES ARE CYCLICAL.

Michael Jordan, still regarded as one of the best basketball players ever in the game, led the Chicago Bulls to six NBA championships in the 1990s. But even MJ's success wasn't without its ups and downs. In his own words: ***"I've missed more than 9,000 shots in my career. I've lost almost 300 games. Twenty-six times I've been trusted to take the game-winning shot...and missed. I've failed over, and over and over again in my life. And that is why I succeed."***[1] And succeed he has. Today his net worth is estimated at $1.7 billion.[1]

[1] Forbes (https://www.forbes.com/profile/Michael-Jordan/#349e094d2d83). Retrieved on 02/05/2019.

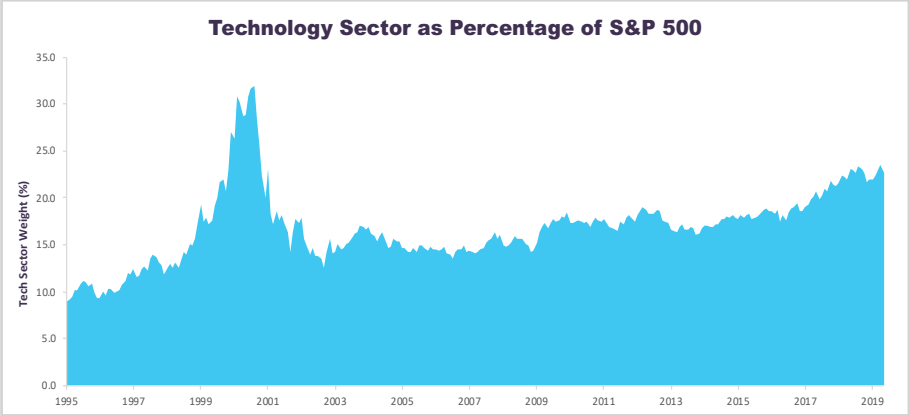
#2: Technology Sector Makes Up a Large Portion of S&P 500

In both the 1990s and in the recent bull market, the technology sector made up a large portion of the market and attributed to much of the returns from both periods.



WE ALL FLIPPED FOR THE FLIP

Introduced in 1996, Motorola's innovativeStarTAC clamshell phone saw sales of about 60 million through the end of the 90s.[2] By contrast, Apple sold more than one billion iPhones worldwide from 2007 to 2017.[3]



Source: Cetera Investment Management, Morningstar, Standard & Poor's. Data is as of 5/31/2019.

1990s

- Technology stocks drove the returns in the 1990s.
  - The tech-heavy Nasdaq Index produced a return of 1,389% in the 1990s bull market.
- With high returns, the size of the sector grew. From 1995 to 2000, the technology sector grew more than threefold within the S&P 500.
  - In 1995, technology represented 8.9% of the index. By the end of 1999, the sector accounted for over 30% of the index.

Today

- Tech stocks drove the returns in the current bull market, too.
  - The Nasdaq returned more than 500% from the start of the bull market in March 2009 through June 2019.
- The tech sector's weight within the S&P 500 was 14.4% at the end of 2008 and rose to as high as 23.4% in 2018.

What Does It Mean?

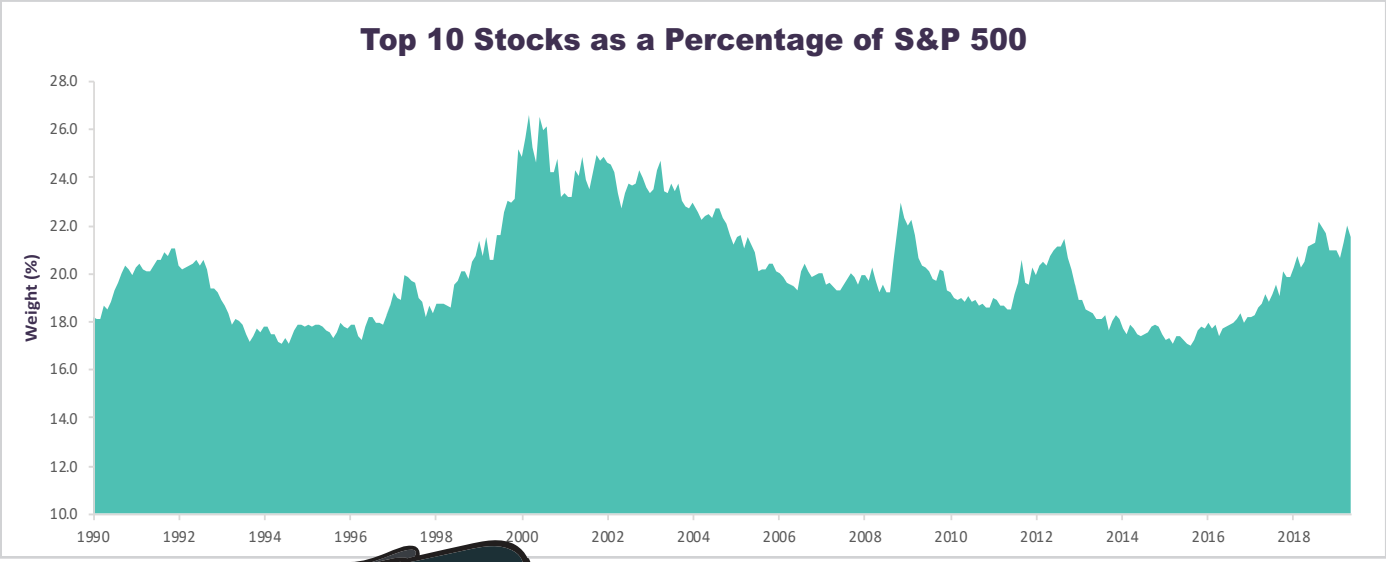
While tech stocks had an outsize impact on both time periods, technology sector performance in the 1990s was more extreme than today. Returns and the size of the tech sector grew at a faster rate in the 1990s than in the current cycle. We do not anticipate the tech sector to grow as large as it did in the late 1990s.

[2] The Gadget We Miss: The Motorola StarTAC (https://medium.com/people-gadgets/the-gadget-wemiss-the-motorola-startac-9bc12db9eedb). Data as of05/13/2013.

[3] Statista (https://www.statista.com/statistics/263401/global-apple-iphone-sales-since-3rdquarter-2007/). Data as of 01/10/2017.

#3: A Small Number of Stocks Make Up Much of the Market

The 10 largest stocks, as a percentage of the S&P 500, experienced a sharp rise in the late 1990s. That trend has repeated in recent years.



Source: Cetera Investment Management, Morningstar, Standard & Poor's. Data is as of 5/31/2019.

1990s

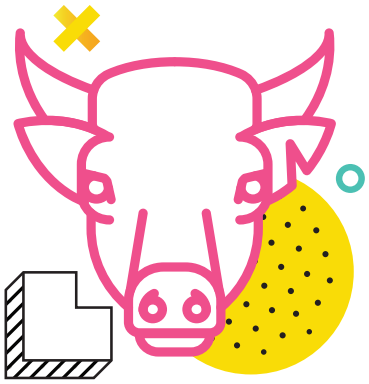
- In 1995, the 10 largest stocks accounted for 17.3% of the S&P 500 Index, and the combined market cap was roughly $800 billion.
- By the end of 1999, the combined market cap of the top 10 largest S&P 500 stocks climbed to $3.1 trillion, or 25.2% of the S&P 500 total market cap.

Today

- The FAANG stocks (Facebook, Apple, Amazon, Netflix, and Google) represent approximately 12% of the S&P 500 Index. The top 10 largest stocks make up nearly 22% of the S&P 500 and have a combined $6.4 trillion in total market cap as of June 2019.
- The FAANG stocks have produced returns that have significantly outpaced the overall market in recent years.

What Does It Mean?

Strong gains in the FAANG stocks highlight the narrow market leadership in recent years, reminding investors of the narrow leadership of the late 1990s. At the time, returns were concentrated within mega cap stocks, which were heavily represented by technology companies. We have seen a rise in market share of the top 10 stocks in recent years, but not to the level reached in 1999.

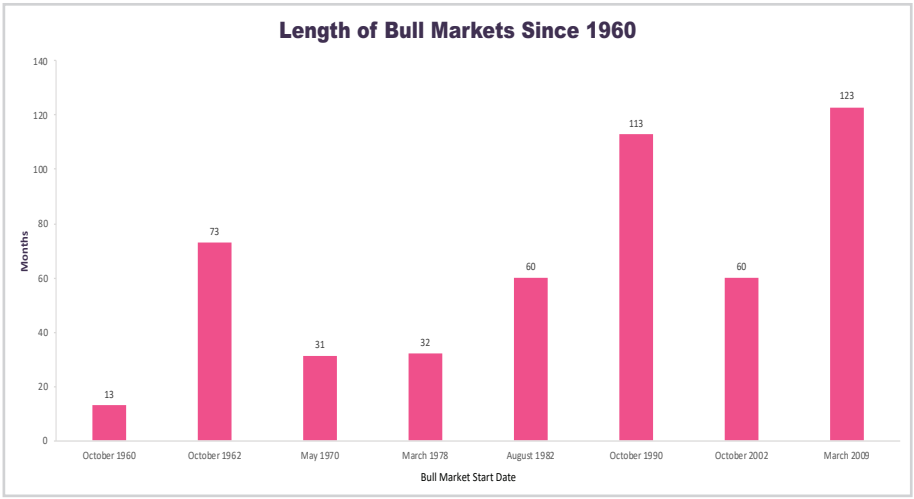


GO BULLS!

The current bull market is now the longest in U.S. history, lasting over 10 years since it began in 2009.

#4: Record-Setting Bull Markets

The 1990s and now both have very long bull market runs of over 100 months without a 20% pullback, the threshold for where a bull market ends. The average bull market has lasted 62 months since 1960, almost half as long as the 1990s and current bull markets.



Source: Cetera Investment Management, JPMorgan. Data as of 6/25/2019.

1990s

- The 1991 to 2000 bull market is the second longest bull market in history, lasting 113 months, with nine consecutive calendar years of positive returns.
- The S&P gained 513% (total return) over the duration of the 1990s bull market. A majority of the gains from the 1990s bull market occurred between 1995 and 1999, when returns surpassed 20% for five straight calendar years.

Today

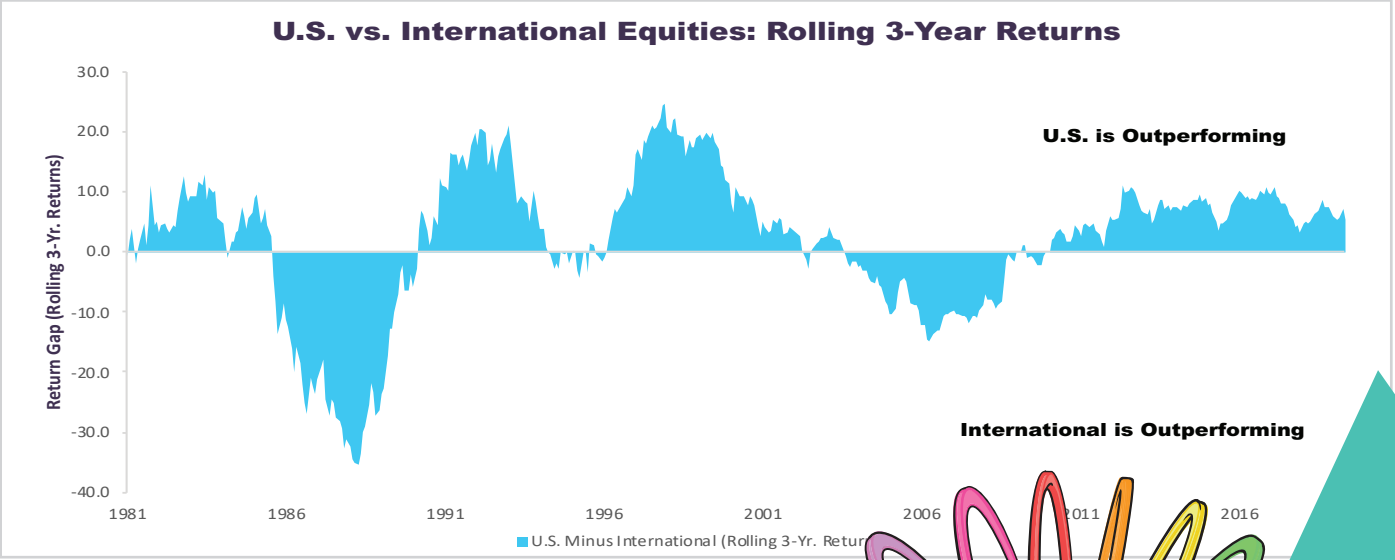
- The most recent run in stocks has not reached the astonishingly high gains of the last five years of the 1990s.
- The long grind higher for stocks in this bull market has produced a 435% gain (total return as of 6/25/2019), but with more modest annual returns relative to the 1990s bull market.

What Does It Mean?

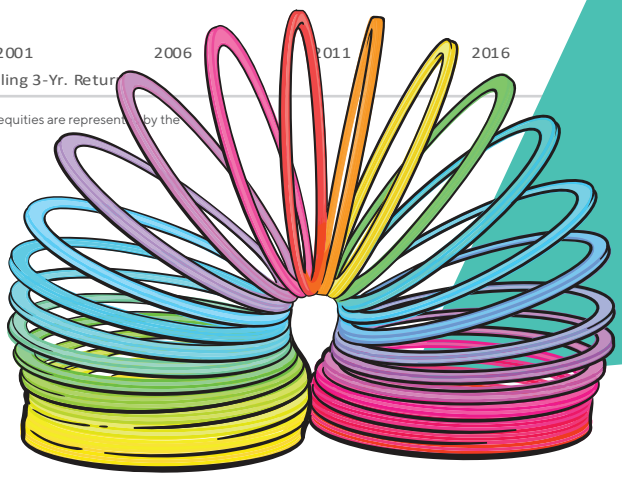
The most recent run in stocks has not reached the astonishingly high gains of the last five years of the 1990s, but the current bull market is now the longest in U.S. history at 123 months and counting. The S&P 500 narrowly avoided reaching bear market territory near the end of 2018, extending the bull market into 2019.

#5: International Equity Underperformance

Another common thread between the 1990s bull market and our current one is the long period of U.S. stocks outperforming international equities.



Source: Cetera Investment Management, Morningstar, Standard & Poor's, MSCI. Rolling three-year returns are annualized. U.S. equities are represent by the S&P 500 Index. International equities are represented by the MSCI EAFE Index. Data as of 5/31/2019.



1990s

- The S&P 500 outgained the MSCI EAFE Index by more than 10% annualized from the inception to conclusion of the 1990s bull market.
- A lost decade of Japanese equity returns following one of the biggest equity bubbles in the 1980s suppressed the index returns compared to the U.S. in the 1990s.

Today

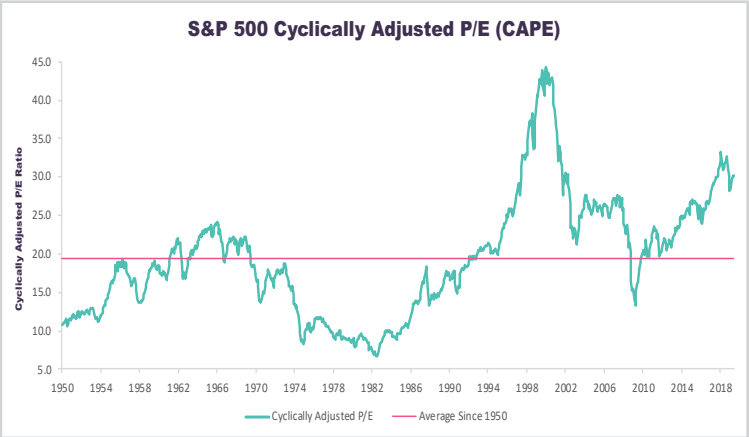
- U.S. stocks are outpacing international equity returns by 6.5% annualized this bull market and the total return for the S&P 500 has doubled the MSCI EAFE Index (as of 6/25/2019).
- Japan and Europe both suffered additional recessions following the financial crisis, while the U.S. has experienced relatively stable economic growth.

What Does It Mean?

While international equities have lagged U.S. equity returns for the duration of the current bull market, the gap between them was even wider in the 1990s. In both cases, market valuations for international equities also fell compared to their U.S. counterparts. However, international equities outperformed U.S. equities coming out of the 1990s bull market. We could see a repeat of that outperformance in the future based on the current valuation gap and cyclical nature of equity returns between the U.S. and international indices.

#6: High Equity Valuations

U.S. equity valuations in both periods are well above their long-term averages. The historical average for price to earnings (P/E) ratios and cyclically adjusted 10-year P/E ratios (CAPE) are 15 and 19.4, respectively.



Source: Cetera Investment Management, YCharts, Robert Shiller, and Standard & Poor's. Data as of 5/31/2019.

1990s

- The P/E ratio for the S&P 500, based on trailing 12-month earnings, peaked to 28.2 in 1999.
- The CAPE ratio, which looks at the trailing 10 years of earnings, adjusted for inflation, peaked at a historical high of 44.2 in 1999.

Today

- The P/E ratio for the S&P 500 (trailing 12-month earnings) hit a cyclical high of 24.0 in January 2018. Valuations for large cap stocks have receded over the last year and a half, but remain above their 15-year average.
- The CAPE reached a cyclical peak of 33.3 in early 2018. The late 1990s was the only time it has been higher.

What Does It Mean?

Stocks have appeared expensive for the last few years versus most periods. However, they have dropped and the January 2018 cyclical high in valuations didn't come close to the valuation levels reached in the late 1990s, especially when you factor in the current environment of low core inflation, interest rates, and bond yields. It's likely that today's high valuations will result in returns that are below average over the next 5 to 10 years, but a repeat of the 2000 to 2002 valuation-driven crash is not our base-case projection.

THE DECADE RETURNS

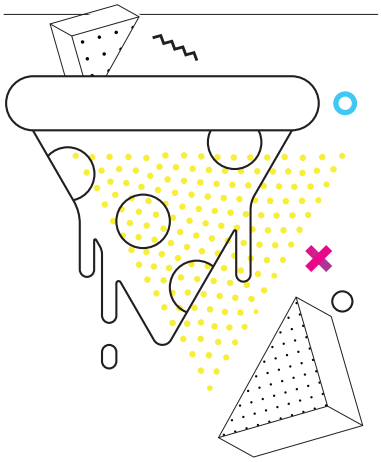
The 90's saw no less than three actors playing the Caped Crusader, better known as The Batman, in theaters: Michael Keaton, Val Kilmer, and George Clooney.

Since 2000, two actors have donned the cape and cowl to be the Dark Knight in a live-action film: Christian Bale and Ben Affleck. We leave it to you as to who wins for best portrayal, but the box-office (adjusted-gross domestic or worldwide—your pick) has resoundingly knighted Christian Bale for the top spot.[4]

[4] Box Office Mojo (https://www.boxofficemojo.com/franchises/chart/?id=batman.htm). Retrieved 02/04/2019.

BOOM OR BUST!

Some 48% of the 90s era dotcom companies survived the crash through 2004,[5] including Akamai, Shutterfly, GeoCities, and those where-are-they-now startups Amazon, eBay, and Google.



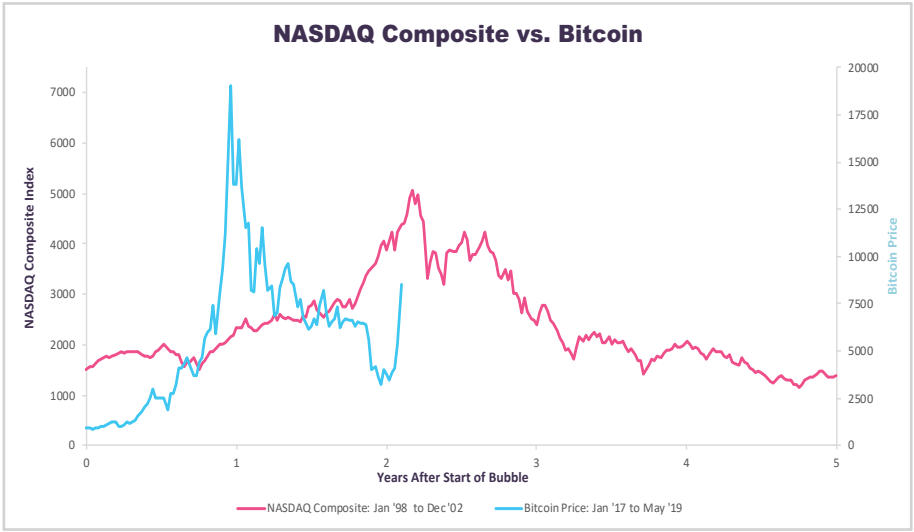
A BIT OF PIE!

Cryptocurrencies (such as Bitcoin) are digital assets that can be exchanged like money outside of any banking system. They exist only digitally—the crypto part being the cryptography used to secure and verify transactions. On May 22, 2010, the first Bitcoin purchase ever made was for two pizzas: 10,000 Bitcoin total. Had the pizzeria kept the Bitcoin and exchanged them at Bitcoin's peak value, they would have received $197,832,100.00. Those pizza's better have had everything on them!

[5] Berlin, L. (2008, November 21). Lessons of survival,from the dot-com attic. The New York Times. (https://www.nytimes.com/2008/11/23/business/23proto.html). Retrieved 02/04/2019.

#7: Speculative Bubbles

The dot-com stock bubble drove the sharp rise in equity prices during the final years of the 1990s bull market. A speculative bubble was also present in recent years within cryptocurrencies.



Source: Cetera Investment Management, Yahoo Finance, Nasdaq. Data as of 5/31/2019.

1990s

- Exuberance over internet-related businesses created a bubble in technology stocks, which peaked in March 2000.
- The eventual crash resulted in the Nasdaq declining by 78% from its peak, while the S&P 500 fell by 49%.

Today

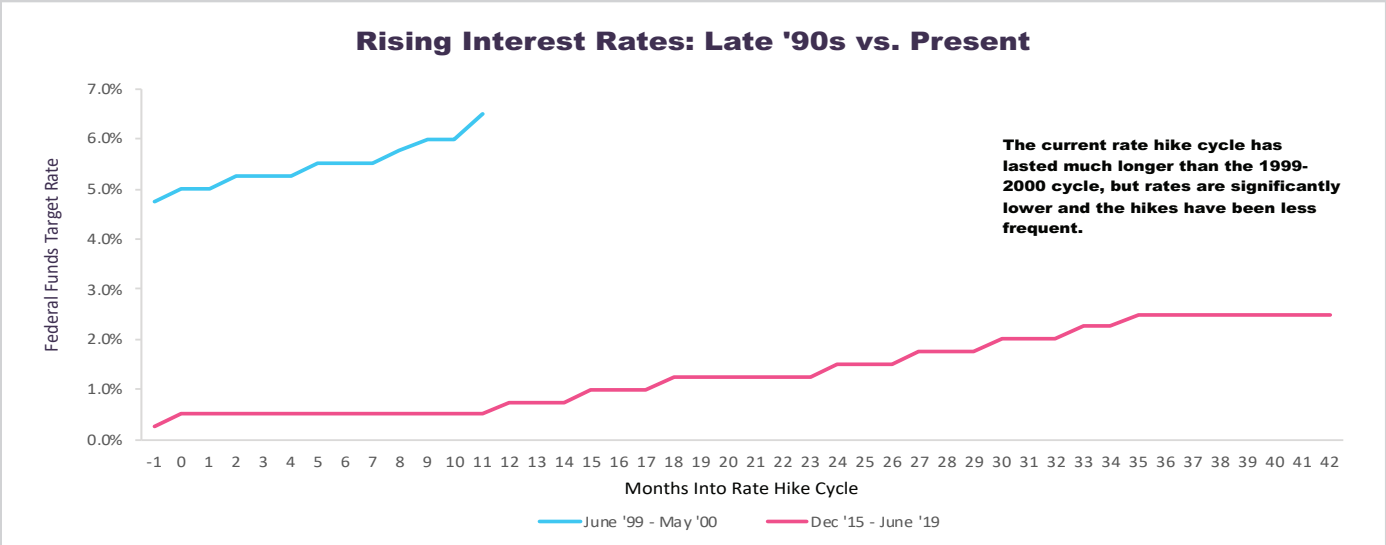
- Cryptocurrencies and blockchain became the new and exciting technological developments many thought would change the way the world operates, driving the price of cryptocurrencies into the stratosphere in 2017.
- The cryptocurrency bubble eventually popped in December 2017, resulting in declines of more than 80% for the major cryptocurrencies. Some of the losses have been recovered in recent months, however, as cryptocurrencies are experiencing another rally.

What Does It Mean?

Valuations were not a concern for investors as enthusiasm soared, allowing dot-com stocks to move aggressively higher until they reached a peak in March 2000 before crashing. Cryptocurrency gains in 2017 dwarfed the returns experienced in dot-com stocks of the late 1990s. Fortunately, the 2018 cryptocurrency crash did not affect the overall economy or equity markets because the market cap in this space is still relatively small.

#8: Rising Fed Funds Rates

The Federal Reserve implemented rate hikes in the late 1990s. We're currently in another rate hike cycle, although rates are much lower today than in the 1990s, and all signs point to the Fed cutting rates in the second half of 2019.



Source: Cetera Investment Management, Federal Reserve Bank of St. Louis, Board of Governors of the Federal Reserve System. Data as of 6/25/2019.

1990s

- Between June 1999 and May 2000, the Federal Reserve raised interest rates five times, pushing rates from 4.75% to 6.5%.

Today

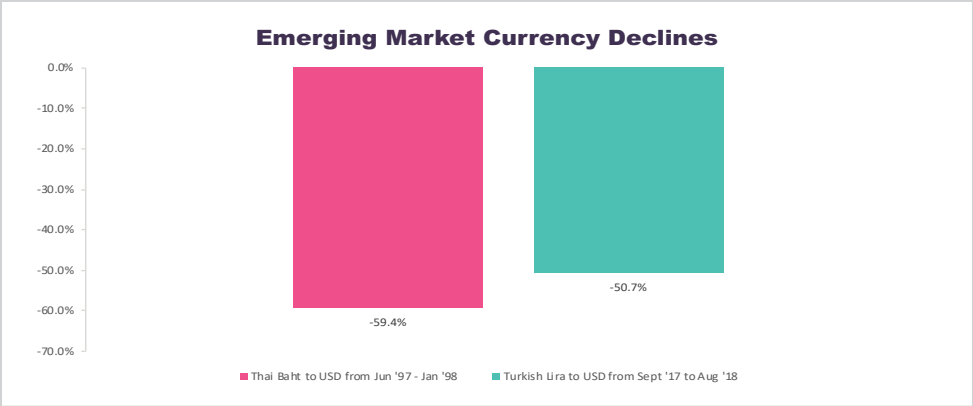
- The current Federal Reserve rate hike cycle started nearly four years ago. Over this period, the Federal Reserve has raised interest rates from near zero to a range of 2.25% to 2.50%.
- The Federal Reserve is signaling a reversal in policy in the second half of the year and market participants expect as many as four rate cuts by year-end.

What Does It Mean?

The late 1990s rate hike cycle was much shorter and rates were a lot higher than they are in the current cycle. It is expected that interest rates move lower in the second half of 2019, ending the current rate hike cycle. There are parallels here, but the level of interest rates and length of the rate hike cycle are not comparable in these two periods.

#9: Emerging-Market Currency Crisis

An emerging-market currency crisis made headlines in the summer of 2018 sparking fears of a 1997 Asian financial crisis repeat. The epicenter was in Thailand in 1997 and in Turkey in 2018. The collapse in the Turkish lira sparked fears of contagion spreading through the emerging world. Fortunately, the crisis did not spread.



Source: Cetera Investment Management, YCharts, Federal Reserve. Thai Baht decline relative to the U.S. dollar shown is from June 17, 1997 to January 12, 1998. Turkish Lira decline relative to the U.S. dollar shown is from September 8, 2017 to August 13, 2018.

1990s

- In 1997, a currency crisis began with the collapse of the Thai baht and eventually spread to several emerging nations in Asia. The Thai baht declined 59.4% relative to the U.S. dollar between June 1997 and January 1998.
- The fallout from the Thai baht collapse was severe and widespread. U.S. stocks almost fell into a bear market over concerns that the Asian financial crisis would cause a collapse in global economic stability.

Today

- An emerging-market currency crisis occurred in Turkey in mid-2018, where the Turkish lira experienced a sizeable drop in valuation.
- The value of the Turkish lira fell by 50.7% relative to the U.S. dollar when it reached a bottom in August 2018. The MSCI Turkey Index fell by 60% and the Turkish Central Bank raised interest rates to 24% to prevent further devaluation of the lira. The sharp increase in interest rates has helped prevent the Turkish lira from collapsing further. The lira stabilized in the fourth quarter of 2018.

What Does It Mean?

The current emerging market currency crisis in Turkey did not have severe consequences on global markets. Turkey represents less than 1% of the total global economy, the Turkish stock market is only a fraction of total stock market capitalization, and other emerging nations are in better shape economically and source less debt with foreign currencies than in the 1990s.

> **The currency crisis in Turkey did not have severe consequences on global markets, as it represents less than 1% of the total global economy.**

#10: Long Economic Expansions

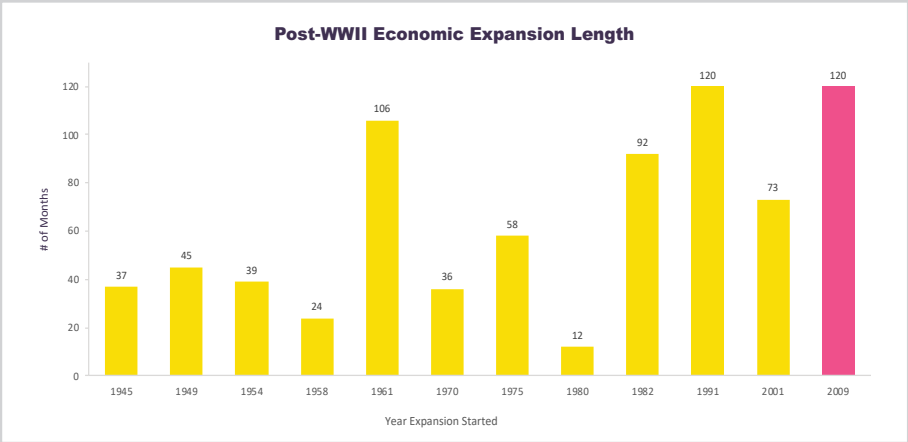
CASTING A SPELL

The 1990s saw the debut of a young wizard called Harry Potter. In the two decades since, the "boy who lived" has sparked his own economic expansion. The combined U.S. first-print run of the three novels that kicked off the series totaled 800,000 copies. By contrast, the last three novels, published between 2003 and 2007, had U.S. first-print runs totaling 29.2 million copies,[6] and the Harry Potter brand is worth an estimated $25 billion.[7] *Accio* profits!

[6] Movavi Blog (https://www.movavi.com/blog/harry-potter.html). Data as of 07/31/2019. Retrieved 02/06/2019.

[7] Meyer, K. (2016, April 6). Harry Potter's $25 billion magic spell. Money. (http://money.com/money/4279432/billion-dollar-spell-harrypotter/). Retrieved 02/05/2019.

The two longest economic expansions in U.S. history are the 1990s expansion and the current expansion. Both expansions are roughly double the length of the average recovery since World War II.



Source: Cetera Investment Management, National Bureau of Economic Research (NBER). Data as of 6/25/2019.

1990s

- The longest U.S. expansion on record was the 1990s expansion, which lasted 120 months, beginning in 1991 and ending in 2001.
- There were seven calendar years in which economic growth exceeded 3% during the 1991 to 2001 expansion. In fact, GDP growth exceeded 4% every year from 1997 to 2000.
- The unemployment rate fell to as low as 3.8% in 2000.

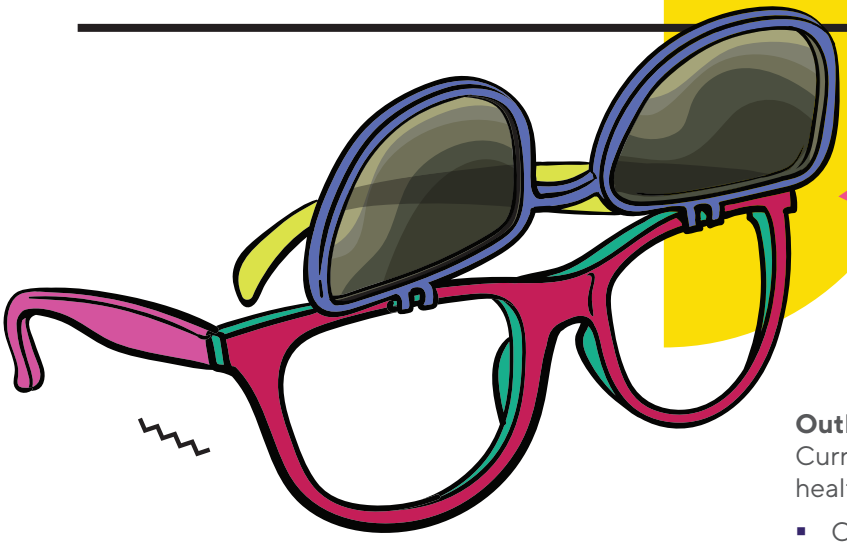
Today

- The current economic expansion, which began in 2009, will be the longest U.S. economic recovery on record at the end of July.
- Economic growth has been stable throughout this expansion, but we haven't experienced consistent growth of 3% plus for an extended period in the current recovery.
- The unemployment rate dropped to a 49-year low of 3.6% in 2019.

What Does It Mean?

The pace of economic growth has not been able to keep up with the late 1990s, but this expansion becomes the longest on record at the end of July. The current recovery has benefited from strong monetary support from the Federal Reserve, and since early 2018, strong fiscal support from the implementation of tax reform for individuals and corporations. Moreover, there has been positive jobs growth for the longest stretch on record. All of these factors are having a positive impact on consumer sentiment, which is elevated due to low unemployment, sizeable stock market gains in recent years, and sustained economic growth.

Where the Similarities End



Today's market environment shares many similarities with the late 1990s, and while some of those parallels are scary, the current environment is a less-extreme version of that decade. We don't think the end of this bull market will be as terrifying as the sharp selloff markets experienced from 2000 to 2002. We may be in the longest bull market run now, but returns pale in comparison to the '90s.

The 31-month bear market that followed the 1990s bull market was one of the worst in history based on market losses. Just as that bear market didn't last forever, the current bull market won't either, and there will be another recession at some point in the future. While we are not predicting one in the near term, we expect one eventually, though nothing as severe as the financial crisis of 2008 to 2009.

Putting recessions in perspective, since World War II:

- There have been 12 bear markets, and the average S&P 500 decline during these periods is 32%.
- The last two bear markets (2000 to 2002 and 2007 to 2009) resulted in a S&P 500 decline of roughly 50%, considerably higher than most bear markets in the post-WWII era.
- Excluding the last two bear markets, which were historical outliers, the average S&P 500 bear market decline was 28%.
- Seven out of the 12 bear markets had a market decline of less than 30%.

A drawdown as severe as the last two bear markets does not seem as likely this time around in the absence of a major asset bubble and is even more unlikely if the next recession is not severe.

Outlook Remains Constructive

Current market and economic fundamentals remain healthy in the U.S.:

- Corporate earnings grew at a rate of 20% year-over-year in 2018 and the expectation is for single-digit earnings growth in 2019.
- The S&P 500 P/E ratio (May 2019) is at a 21% discount from the January 2018 peak and a 33% discount from the peak reached in 1999.
- Fortunately, interest rates are still historically low and are unlikely to jump significantly higher from current levels in this cycle.
- The unemployment rate is near a 50-year low, and jobs growth remains positive.
- Consumer spending is still growing, aided by low unemployment.
- U.S. services activity, which represents roughly two-thirds of the economy, remains healthy.

Nevertheless, Risks Are Building

Market volatility has picked up following a very calm 2017, resulting in two separate market corrections in 2018 (meaning 10% or more drawdowns). The S&P 500 declined by 19.8% from its all-time high in late December, narrowly missing bear market territory. Domestic economic growth last year was the strongest in years, but a few areas of concern are developing, namely a drop in the pace of jobs growth, weakening manufacturing growth, and an inversion in parts of the yield curve.

Global economic data has also been a concern. The global manufacturing PMI, a proxy for global manufacturing activity and global economic strength, has been trending lower since December 2017. A rise of inward-looking populist leaders, elevated trade war rhetoric, and geopolitical risk in several global regions provide additional apprehension for the state of the global economy.

Conclusion

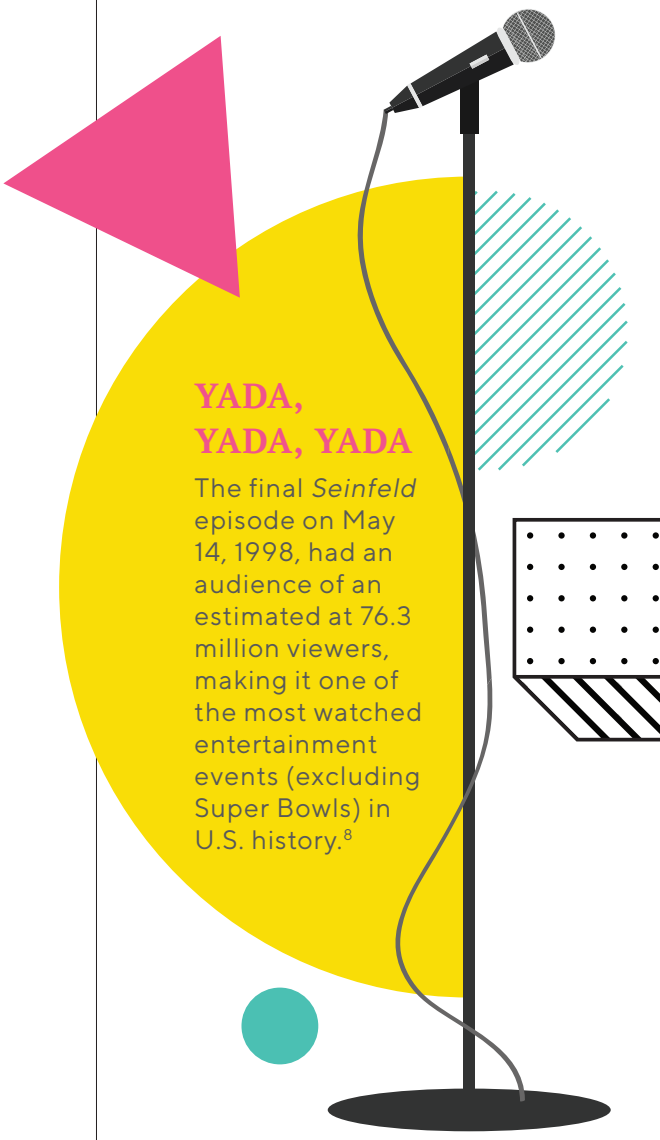
One of the most popular TV show in the late 1990s was *Seinfeld*, notable for being a show about nothing. Back then, the only way to watch it was on a standard analog television broadcast over regular airwaves. In 2012, Jerry Seinfeld made his return as the star of another TV show, *Comedians in Cars Getting Coffee.* But unlike the former program, you can only watch this show streamed over the internet on a smart TV, smartphone, computer, or tablet.

The euphoria that caused a bubble in internet-related stocks in the late 1990s was largely about the ways in which the internet would change the world forever. The technology available in the late 1990s had not developed to match the mania in equity prices. Technologically, that's definitely not a story about nothing. Smartphones, tablets, and internet-connected smart TVs didn't even exist when the final episode of *Seinfeld* aired 20 years ago. The internet has transformed other areas of our lives including the way we shop, conduct business, communicate, and socialize.

Similarities between now and the 1990s exist, but only up to a point. The 1990s bull market ended with a severe crash–a repeat of a crash that severe isn't a likely outcome because valuations are not as extreme as they were in the late 1990s. Market fundamentals are still on solid footing and the economy continues to grow at a solid pace.

- In this environment, we remain constructive on holding risk assets in the second half of the year, with the understanding that volatility is likely to pick up as economic growth slows and the bull market matures.
- A tilt toward value stocks may be prudent following years of underperformance and because valuations are more reasonable.
- An allocation to international equities also makes sense to diversify risks and to have exposure to economies that are earlier in their economic cycle than in the U.S.
- Let us not forget the lost decade that followed the tech crash. U.S. equities in the 2000s was one of the only asset classes that was negative during that decade.

For these reasons, we recommend a balanced allocation lined up with long-term fixed-income targets to dampen portfolio volatility.



YADA, YADA, YADA

The final *Seinfeld* episode on May 14, 1998, had an audience of an estimated at 76.3 million viewers, making it one of the most watched entertainment events (excluding Super Bowls) in U.S. history.[8]

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The MSCI EAFE is designed to measure the equity market performance of developed markets (Europe, Australasia, Far East) excluding the U.S. and Canada. The Index is market-capitalization weighted.

MSCI Turkey Index measures the performance of the large and mid cap segments of the Turkish stock market. It is composed of 24 constituents and covers approximately 85% of the Turkey equity universe.

Russell 1000 Value Index measures the performance of the large cap value segment of the U.S. equity universe. It includes those Russell 1000 Index companies with lower price-to-book ratios and lower forecasted growth values.

Russell 1000 Growth Index measures the performance of the large cap growth segment of the U.S. equity universe. It includes those Russell 1000 Index companies with higher price-to-book ratios and higher forecasted growth values.

The Nasdaq composite is an index that tracks more than 3,000 domestic and international based companies that trade on the Nasdaq Stock Market. This index has a high weight of information technology stocks.

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