

Weekly Commentary

The Magnificent Seven's Surge and Potential Correction Ahead

The Magnificent Seven (Apple, Amazon, Alphabet, Microsoft, Nvidia, Meta and Tesla) have significantly outperformed the broader market this year, accounting for nearly 80% of the S&P 500's return. According to survey data from Bank of America research, the most crowded trade among fund managers today is long mega-cap technology stocks. It is a reasonable assumption that retail participation in these stocks is quite high too.

Table 1: Contribution to Index Return by Magnificent Seven

	ACWI	S&P 500	Russell 1000 Growth
Alphabet (Google)	0.7%	1.2%	2.1%
Amazon	0.8%	1.4%	2.5%
Apple	1.2%	2.0%	3.8%
Meta (Facebook)	0.7%	1.2%	0.6%
Microsoft	1.2%	2.3%	4.3%
Nvidia	1.1%	2.0%	3.6%
Tesla	0.4%	0.6%	1.1%
Index Return	6.8%	10.7%	23.2%
Other Constituents	0.7%	0.0%	5.1%
M7 % of Return	89.6%	100.4%	77.8%

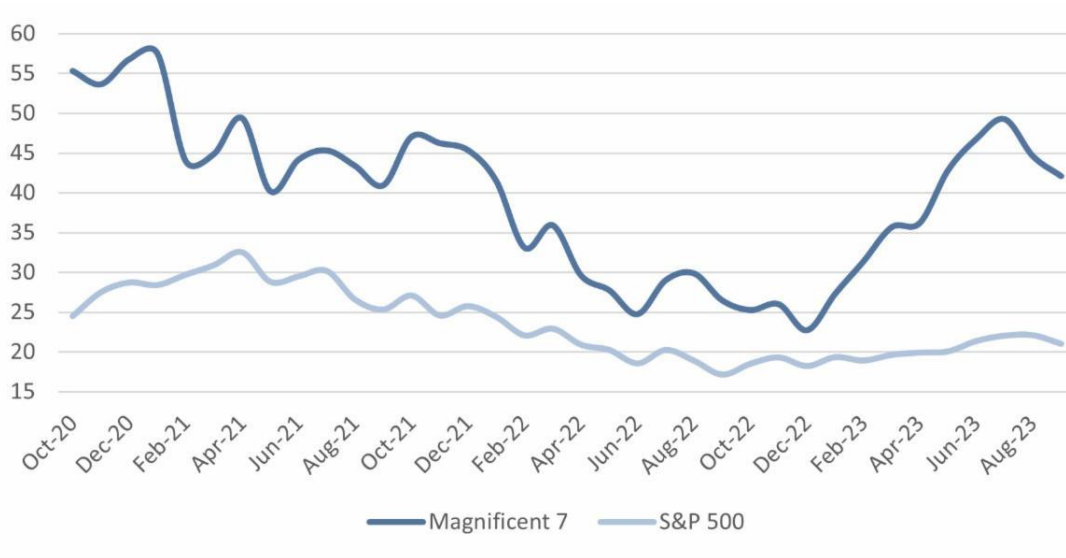
Source: Bloomberg, Mill Creek. Data as of October 31, 2023.

In 2023, the price-to-earnings valuation of the S&P 500 has hovered between 18-20 times. However, for the Magnificent Seven basket, this ratio has expanded from approximately 23 times at the start of the year to approximately 42 times today. We find this valuation premium excessive, and it is difficult to reconcile how these stock prices have continued to move higher, given the rise in interest rates. To justify this higher ratio, stock prices or interest rates (discount rates) will need to decrease. As of now, the basket has fallen about 11% from its highs in July 2023.

We continue to believe that mega-cap technology stocks may be the most vulnerable to a re-rating (price correction) in a higher for longer environment. As such, our global equity portfolios remain diversified with positions in value, small-cap, and international stocks. In a narrow market like 2023, it takes discipline not to chase what has worked recently, and we would strongly encourage long-term investors to stay the course with their equity exposure.

Fig. 1: High tech valuations leave them vulnerable to re-rating

Magnificent 7 vs. S&P 500 - Multiple Expansion



Source: Bloomberg, Mill Creek.

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