Thematic Growth Equity: A Second Time Around?

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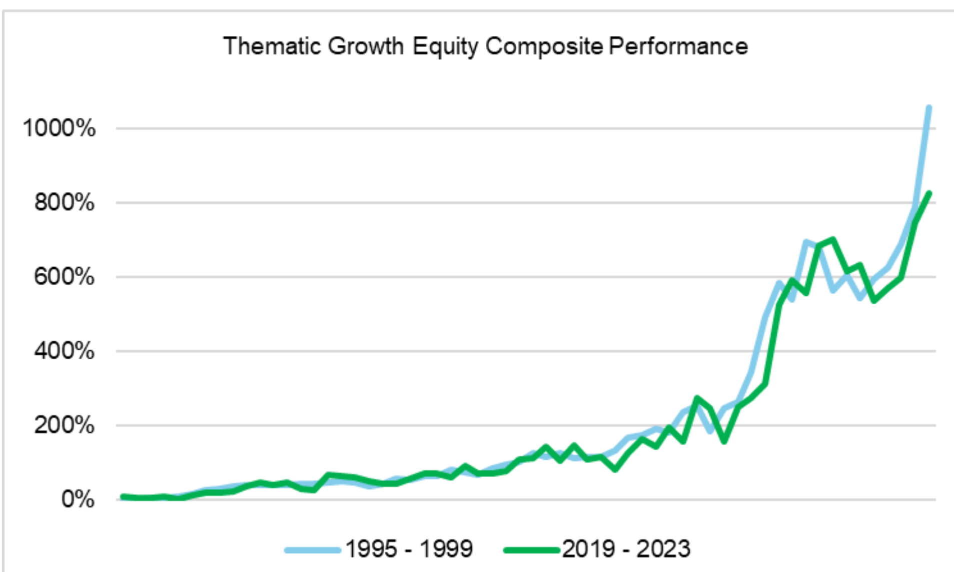
In October 1994, we began managing money using our thematic growth equity strategy. That same strategy is being used today to manage almost $200 million. Back then, most economists and market technicians had a neutral outlook for the economy and financial markets. However, the following month, in November, the Republicans gained control over Congress and began implementing the policies in the innovative “Contract with America.” These changes benefited growth stocks in general, but the whole stock market did well until the beginning of 2000. In this favorable environment for stocks, our growth equity strategy gained 26% in the fourth quarter of 1994 and another 38% in 1995. One of our biggest errors was thinking that the rally could not continue. We were wrong! In 1996, our strategy gained 17%; in 1997, it gained 36%; in 1998, it gained 174%; and in 1999, it gained 96%. Favorable economic policy fostered by collaboration between Congress and the President combined with the need to ensure a safe transition in the information technology world to the year 2000 led to this unusual performance over these years.

There are some significant similarities between the late ’90s and today. Instead of benefiting from a technology boom as was the case in the late Nineties, the current bull market advance appears to have begun back in 2019. Starting in that year, our thematic growth equity strategy gained 23%. In 2020, the strategy rose by nearly 50%; in 2021, a gain of 21%; and in 2023, a gain of 30%. This record was interrupted by the bear market in 2022 when the strategy lost 36%. The strategy is currently up 31% through the end of June. The current environment feels a lot like the late ‘90s, yet we are not near the cumulative return of our strategy in the late Nineties of 1,454% as you can see in the chart below. So, is this the second time around?



Today, information technology remains just as important, if not more important, back then. With the advances in artificial intelligence and companies' commitments to further develop and expand this technology, no end event like Y2K is in sight. There are no limits to the use of artificial intelligence across industries. What began as a race to build giant models trained on mountains of data (read OpenAI's GPT-4) is shifting to build cheaper, faster, and more specialized models. As Satya Nardella of Microsoft said recently: "I think we increasingly believe it's going to be a world of different models." As investors, we interpret this to mean there is still room to run as the stock market advance broadens as more medium and small companies get involved with this technology.

The important question for investors is, where do we go from here? One consideration is the similarities from a political perspective. The upcoming November elections may usher in major changes in government policy similar to the changes in 1994. The continued stock market advance in the face of a weakening economy is a testimonial to how the markets are good forecasters of the future. Our thematic growth equity strategy is positioned to reflect these expectations.