Core Alternative Capital

As we approach the end of 2020, many advisors and investors are beginning to take stock of their portfolios and prepare for their upcoming year end reviews. But one of the more curious aspects necessary to understand and properly evaluate updated returns and risk statistics is the concept of "underlying market breadth dynamics."

"Market breadth" refers to measures that help to describe what is driving market performance. E.g. one aspect of market breadth is advance/decline, which measures the number of stocks gaining versus the number of stocks declining; the implication being that in a cap-weighted index, a mega cap stock like Apple might have an outsized effect on the return of the market, while a large number of smaller stocks might be moving in the opposite direction (in 2020, about 40% of stocks in the S&P are negative YTD, despite the index being up over 16% as a whole). Another measure related to advance/decline is market attribution, which calculates how much each stock added or subtracted from the total market return. For example, in 2020 AAPL has gained 81.3% through 12/24; starting the year as the largest component of the S&P 500 with a weight of 4.6%, Apple has contributed 3.7% to the market, which alone accounts for over 22% of the entire market return. **For one company to represent over 1/5 of the entire market's return, we have to recognize that something odd is occurring**.

Another measure of "market breadth" is dispersion, which is a simple calculation of the difference between various segments of the market, and how much each have contributed to the whole. One example is Growth vs Value. In 2020 the dispersion between these two market segments is greater than 30%, which not only matches the largest gap between the two groups of stocks as far back as data allowed to the mid 1990s, but it also represents the first time on record when a gap greater than a few percent manifested when Growth is positive and Value is negative (+31% vs -0.5% through 12/23).

So as we talk to investors and clients when reviewing 2020 performance, we must make extra effort to understand what has driven our portfolios and underlying strategies to the results that they have achieved. Just because the S&P 500 is up over 16% YTD does not mean that it is a perfectly appropriate measuring stick for all of our holdings. What has driven results may help illuminate or explain how we've gotten to where we find ourselves.