Cap-Weighted Indices Resistant to Vaccine

S&P 500 has worst performance versus Stratified Weight

November 25, 2020

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Vaccine Themes

Tourism ⇧

Corporate Real Estate ⇧

Oil & Gas ⇧

Technology ⇩

As the number of Coronavirus infections continues to make new highs, equity markets have instead focused on the positive news regarding the three largest vaccination trials.

On November 9th, Pfizer announced that their vaccine produced in collaboration with BioNTech reduces infections in 90% of cases. The S&P 500 rose 1.2% on the day but suffered from a rotation away from large cap technology stocks. Alternative weighted strategies outperformed significantly, with the Syntax Stratified LargeCap index rising 3.8% for its strongest relative performance ever recorded (+2.6%, see Exhibit 1 below).

Moderna and AstraZeneca followed suit by releasing the results of their studies showing comparable, if not marginally improved efficacy. The market digested the news in similar fashion and the reversal of travel and oil related companies continued.

As the market continues to discount an end to the pandemic, we look at the recent trends in the context of their component themes to determine the drivers of the performance and whether there is capacity for the reversal to persist.

We find that the majority of the performance of cap versus alternative weight is driven by the relative exposure to three vaccine beneficiaries: Tourism, Corporate Real Estate and Oil at the expense of Technology. According to Affinity, the S&P 500 has 14.9% in vaccine beneficiary themes vs 23.8% for Stratified weight and 40% in Technology stocks which underperform following positive vaccine news, versus 17.5% for Stratified weight.

Exhibit 1: Index performance on Vaccine news days

Date	Vaccine News	Nasdaq	S&P 500 Index	Stratified LargeCap	**Stratified rel S&P 500**
9-Nov-20	Pfizer-BioNTech	-2.7%	1.2%	3.8%	**2.6%**
16-Nov-20	Moderna	-0.4%	1.2%	2.0%	**0.9%**
23-Nov-20	Oxford-AstraZeneca	-0.4%	0.6%	1.5%	**0.9%**

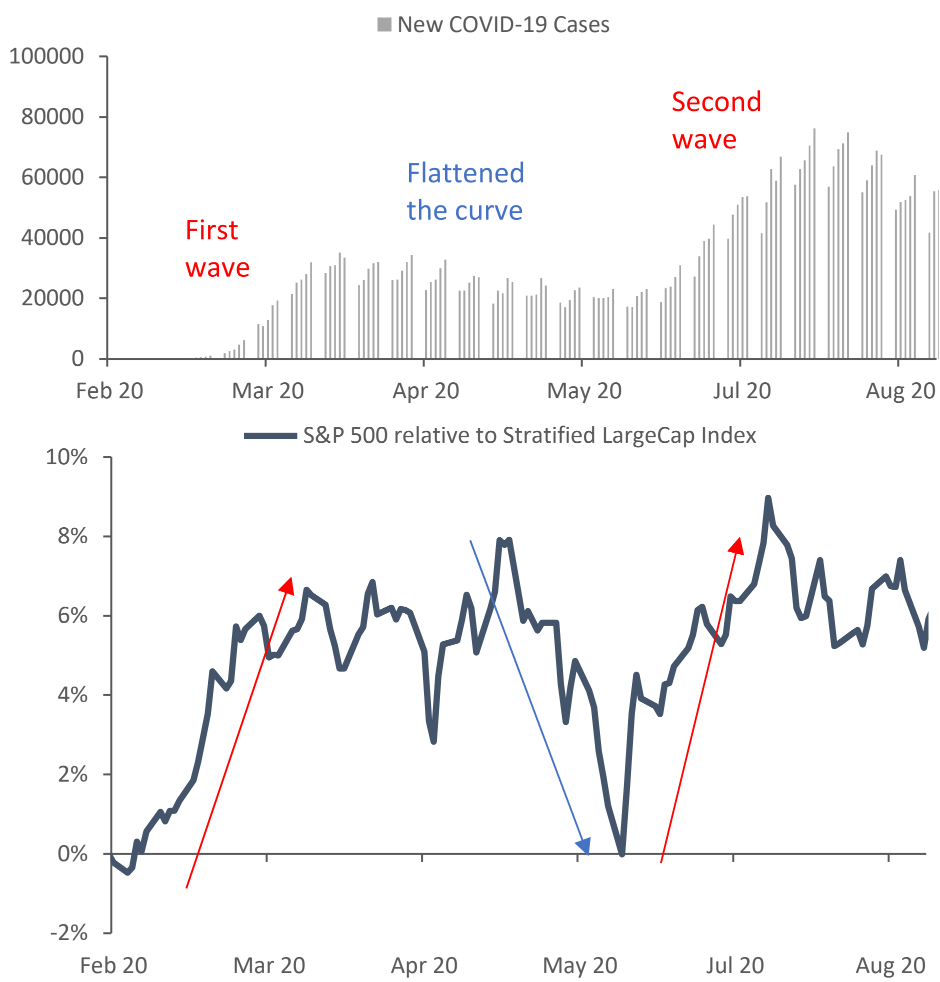
Performance does not reflect fees or implementation costs as an investor cannot directly invest in an index.
Source: S&P Dow Jones Indices, Syntax.

Cap-weight correlated with the virus since pandemic began

The recent relative performance of cap-weighted indices versus their alternative weighted counterparts will not come as a surprise. Since the market became focused on the pandemic on Feb 20th, the performance of the S&P 500 versus alternative weight products has been correlated with the trend in new infections. As cases grew in the US, alternative weight indices which are underweight mega-cap technology stocks underperformed the cap-weighted benchmark by 6.5%. However, as cases dissipated in May, investors moved back into value stocks and the S&P 500 gave back all its relative outperformance over Stratified weight (Exhibit 2).

This recovery was short-lived and as the virus lingered and a second wave of cases spread into the rest of the country, investors moved back into technology companies and cap-weighted products once again outperformed.

Exhibit 2: Coronavirus cases and the S&P 500 relative to the Stratified LargeCap index



Performance does not reflect fees or implementation costs as an investor cannot directly invest in an index. Source: CDC, S&P Dow Jones Indices, Syntax.

Vaccine Themes

Using Affinity™ we measure the performance of groups of stocks in the S&P 500 through a variety of different lenses and isolate four themes that are linked to the Coronavirus pandemic (i.e. diverged during the first and second infection waves).

The results are very intuitive. The Affinity Technology theme consistently outperformed during the first and second waves and the Tourism and Corporate Real Estate thematics, together with Oil & Gas (i.e. Vaccine themes) outperformed when cases fell in May and it looked as though the virus was under control.

The relative performance of these themes explained 85% of the relative outperformance of cap versus stratified weight (in Exhibit 3). This is due in part to the significantly different exposures that the Stratified weight and cap weight have to these themes (Exhibit 4).

Vaccine Themes

Tourism ⇧

Corporate Real Estate ⇧

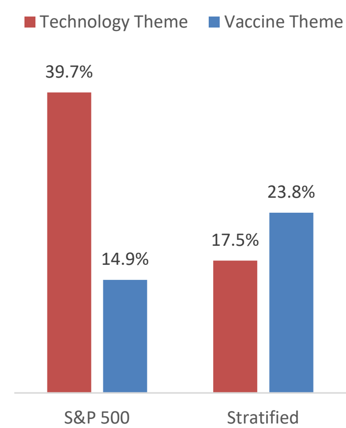
Oil & Gas ⇧

Technology ⇩

Exhibit 3: Performance of COVID-19 sensitive themes

Performance does not reflect fees or implementation costs as an investor cannot directly invest in an index. Please see important disclaimers regarding backtested data prior to inception. Source: S&P Dow Jones Indices, Syntax.

Exhibit 4: S&P 500 vs Stratified LargeCap Index Exposure

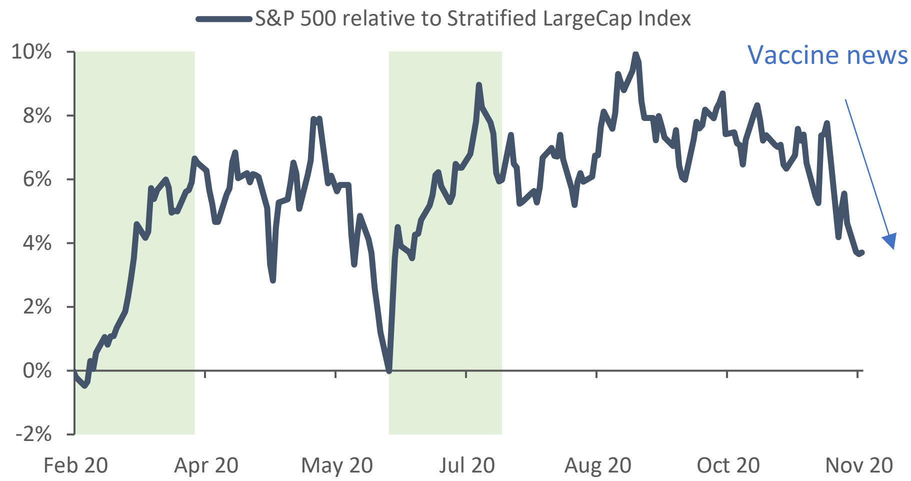


Source: Affinity

And if it was all a bad dream?

Using Feb 20th as an anchor date for a pre-COVID market, we find that the S&P 500 would underperform the Stratified LargeCap by 3% for the two indices to return to the same levels (Exhibit 5).

Exhibit 5: S&P 500 relative to Stratified LargeCap index since 2/20/20



Performance does not reflect fees or implementation costs as an investor cannot directly invest in an index. Source: Syntax

We also see a strong fundamental reason for the Stratified LargeCap index to outperform the S&P 500. Using each index's valuation multiples on 2/20/20 as target levels, we find that the S&P 500 is 8-9% overvalued and the Stratified LargeCap index is 3.5% undervalued (Exhibit 6).

Exhibit 6: Upside potential if multiples return to 2/20/20 levels

	P/Sales			**Dividend Yield**		
	Feb 20	current	**Upside**	Feb 20	current	**Upside**
S&P 500	2.29	2.50	**-8.2%**	1.94	1.76	**-9.3%**
Stratified LargeCap	1.28	1.24	**3.4%**	2.22	2.30	**3.5%**

We use two transparent valuation metrics P/Sales and Dividend Yield, rather than earnings or cash flow-based metrics which are more opaque and volatile. Source: Syntax, Bloomberg Estimates (BEst)

There are of course many reasons why prices and valuations should not revert to pre-crisis levels, such as the secular change to peoples' working habits that the pandemic merely accelerated.

However, such views are open to debate and with pent-up demand for companies aligned with the vaccine themes, we believe there is plenty of scope for these trends to continue.

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Past performance is no guarantee of future results. All performance presented prior to the index inception date is backtested performance. Backtested performance is not actual performance, but is hypothetical. The inception date of the Syntax Stratified LargeCap Index was December 27, 2016. The backtest calculations are based on the same methodology that was in effect when the index was officially launched. However, back-tested data may reflect the application of the index methodology with the benefit of hindsight, and the historic calculations of an index may change from month to month based on revisions to the underlying economic data used in the calculation of the index. Charts and graphs are provided for illustrative purposes only.

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