Bloomberg

# Stock Crowding Risk Is Back With Everyone Buying the Same Thing

By Lu Wang and Melissa Karsh , 5th March 2019

- Mutual funds, hedge funds acted similarly during year-end rout
- A measure of market crowdedness has risen to a two-year high


*The danger was particularly pronounced last year in the FANG complex of Facebook, Amazon, Netflix and Google's parent Alphabet. Photographer: Jason Alden/Bloomberg*

All year, evidence has built that professional money managers reformed their ways after last quarter's equity rout. Hedge funds stepped back from the market. They put more faith in their stock-picking skills.

In one regard, though, equity managers haven't changed much. It's their propensity to all own the same thing. That can be seen in a measure of crowdedness in the market that's higher than it's been in two years.

Goldman Sachs assesses the trend by counting how many companies are among the 50 most-owned by hedge funds and mutual funds alike, going by filings. Right now it's 13, the most since early 2017. Both sets of investors have boosted bets on industrial and technology stocks while retreating from drugmakers and banks, Goldman's data showed.

To strategists led by David Kostin, the concentration is a sign of conviction among stock pickers. And the bets are paying off: industrial and tech stocks have led the market's rebound in the first two months of

2019. But anyone who watched crowded stocks bear the brunt of selling in the October-December carnage has seen the risk of unwinding. That is, too much money is chasing the same stocks. When it pulls out, the decline is that much worse.

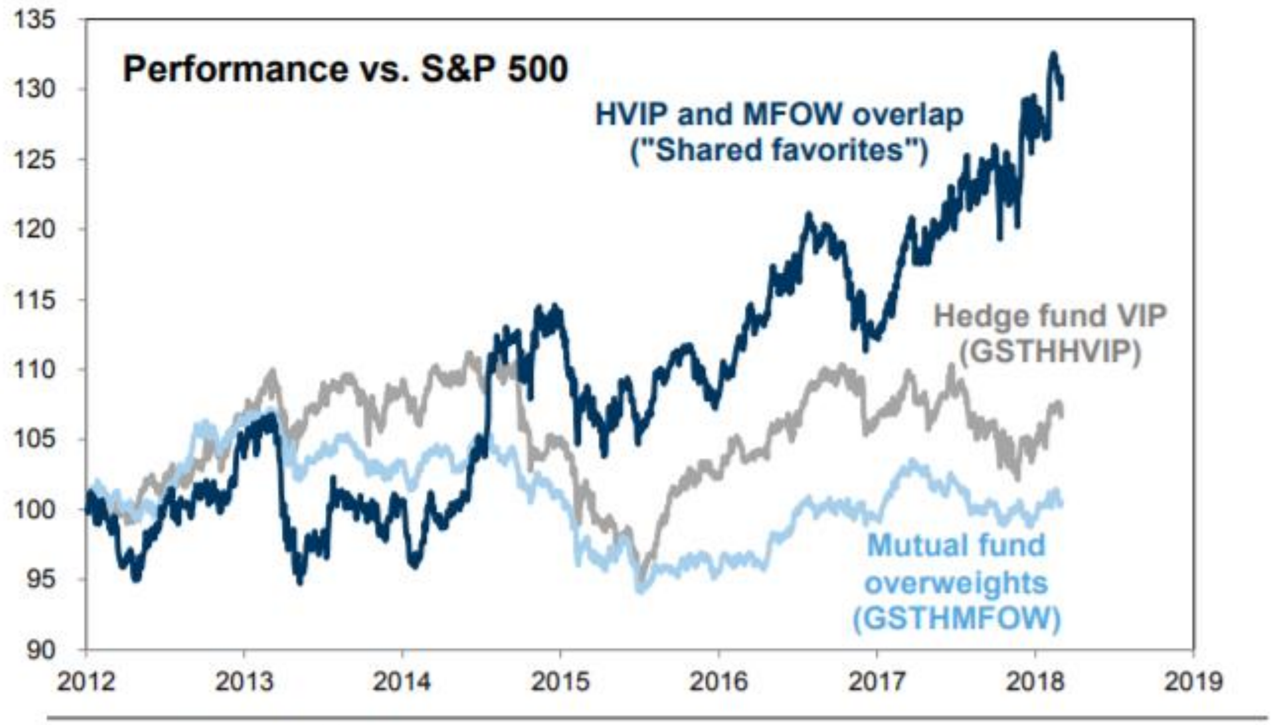
“Hedge funds once again appear to have crowded into similar stocks, and have done so with increased leverage. That momentum typically feeds on itself,” said Christopher Hillary, chief executive officer and portfolio manager at Denver-based Roubaix Capital, which has about $120 million under management. “When the market reverses, however, you have the equal and opposite reaction as everyone runs for the exits at the same time. That is what occurred in late 2018, and we see no less risk in the market today.”

The danger was particularly pronounced last year in the FANG complex of Facebook, Amazon, Netflix and Google’s parent Alphabet. The quartet sank during the March-April sell-off, and again in the fourth quarter.

Alphabet remains a shared favorite by mutual funds and hedge funds tracked by Goldman Sachs. Stocks that entered the list include Electronic Arts, PayPal, T-Mobile and UnitedHealth Group.

Read more: Forget FANGs, Lay Off Drugs. Industrials Are the New Big Trade (Bloomberg, 22nd feb 2019)

To be sure, investors are piling into these stocks for a reason, among them earnings growth. At 15 percent, the group’s average estimated median profit growth this year is almost triple the S&P 500’s, Goldman Sachs data showed.



Source: Goldman Sachs Global Investment Research

Historically, companies loved by both mutual funds and hedge funds have tended to outperform the market by a higher frequency. On a monthly basis since 2013, an equal-weighted list of such stocks has beaten the S&P 500 two-thirds of the time, compared with less than 60 percent for those favored by either fund category. Over the stretch, the group has returned 19 percent a year, beating the S&P 500 by 5 percentage points.

“Great minds think alike,” Kostin wrote in a note Friday.

For now, that’s good news when the stocks are all up. But watch out when sentiment shifts.