Small-Caps Break Record, Nasdaq Hits 14-Year High

By Oliver Renick and Cecile Vannucci - Dec 26, 2014

The Russell 2000 (RTY) Index climbed to an all-time high and the Nasdaq Composite Index reached a level unseen since 2000 as an equities rally that started last week continued through one of the slowest trading days of the year.

The Russell 2000 of small-cap companies gained 0.7 percent to a record 1,215.21 at 4 p.m. in New York. The Nasdaq Composite jumped 0.7 percent to the highest level since March 2000, as biotechnology companies rebounded a second day. The Standard & Poor’s 500 Index (SPX) rose 0.3 percent to 2,088.77. The Dow Jones Industrial Average (INDU) added 23.50 points, or 0.1 percent, to 18,053.71. About 3.3 billion shares traded hands on U.S. exchanges, the second-lightest day of trading this year. The slowest was on Dec. 24, when the market closed at 1 p.m.

U.S. exchanges were closed yesterday for Christmas. Most major markets around the globe were shut today.

“We’ve had quite a run here,” Eric Cinnamond, who manages the $691 million Aston/River Road Independent Value Fund, said by phone from Louisville, Kentucky. “The consensus has been that the domestic economy is improving and small-caps are more exposed to that than large-cap multinational companies. Managers are making sure they’re owning what’s working and the herd mentality is at extremes right now.”

The Russell 2000 and Nasdaq Composite (CCMP) have shown resilience this year. The Russell recovered from a correction that saw it slip 11 percent over a five-week period starting in early September. The index has surged 16 percent since reaching a one-year low on Oct. 13.

Bouncing Back

The Nasdaq Composite closed below 4,000 twice this year, on Feb. 3 and April 11. It has rallied 20 percent since then, and is now 4.8 percent below its all-time closing high of 5,048.62, set on March 10, 2000. The Nasdaq 100 Index, which jumped 0.7 percent today, is about 20 points away from reaching a 14-year high.

Even with its 4.4 percent gain in 2014, the Russell still trails the S&P 500 and Dow, growing at less than half the pace.

Both the S&P 500 and the Dow are at records this week after posting their biggest rally in three years. The recent gains are taking the Dow up 1.3 percent for the month and 8.9 percent this year. The gauge has advanced for seven straight days, the longest streak since March 2013. The S&P 500 has risen 1 percent in December and 13 percent for the year.

“Momentum has been building in the last month for small-cap names,” Michael James, a Los Angeles-based managing director of equity trading at Wedbush Securities Inc., said by phone. ‘It’s merely playing catch up. Given that the Russell has lagged through this year, people are trying to find beta for performance.’”

Valuation Concern

It hasn’t been a smooth year for small-cap stocks. The Russell 2000 lost 2.8 percent over a three-day period starting July 15 after the Federal Reserve expressed concern about valuations among social-media and biotech companies.

“Valuation metrics in some sectors do appear substantially stretched -- particularly those for smaller firms in the social-media and biotechnology industries,” the central bank wrote in assessing the U.S. stock market.
The Fed’s concern came after small-caps and Internet shares were the biggest victims of a market retreat early in the year as investors dumped the best performers of the bull market.

Small-cap shares also fell faster than the broader market during an August selloff sparked by concern that a selloff in oil prices and slowing growth in China and Europe would hurt the U.S. economy.

The Russell 2000 will trail the benchmark index in 2015, Bank of America Corp. analysts wrote in a note to clients earlier this month. Small-cap companies remain expensive and will appreciate less than larger ones as interest rates increase, the analysts led by Jill Carey Hall said.

**Oil Slump**

The slump in oil prices threatened the stock rally earlier this month, with the S&P 500 closing at a seven-week low on Dec. 16. The index recouped its losses faster than in comparable drops earlier this year as the Fed said it will be patient on the timing of interest-rate increases and the U.S. economy expanded at the fastest pace in more than a decade.

Since the bull market began in 2009, the Dow has risen 176 percent, propelled by better-than-estimated corporate results and three rounds of Fed bond buying. The S&P 500 has more than tripled during that period. Even with slumps in 2014 risking to derail a bull market in its sixth year, the Dow’s worst retreat was only about 7 percent, and the gauge recovered from each drop in two months.

The Chicago Board Options Exchange S&P 500 Volatility Index, the gauge of S&P 500 swings known as the VIX (VIX), slumped 39 percent in the previous six trading days, its biggest plunge since January 2013. The index rose 0.9 percent today for the first increase in seven days.

**Biotech Companies**

Seven of 10 major groups in the S&P 500 advanced, with utilities and health-care companies jumping more than 0.8 percent. Energy shares dropped less than 0.1 percent.

Gilead Sciences Inc. added 2.7 percent as RBC Capital Markets analyst Michael Yee said the company should “aggressively” repurchase shares following an 18 percent drop earlier in the week. The drugmaker could “easily” buy $10 billion over the next year “without issues,” Yee wrote.

The Nasdaq Biotechnology Index rallied 2.3 percent, rebounding for a second day. The gauge recovered from losses earlier this year, reaching a record on Dec. 19 before this week’s volatility.

Biotech shares had slumped this week as investors fear health insurers and companies that manage patient’s drug benefits will put new pressure on how much the industry can charge for breakthrough treatments. The selloff was prompted by Express Scripts Holding Co.’s announcement that it would block its U.S. patients from getting Gilead’s $1,100-a-pill hepatitis C medicine.

Pfizer Inc. climbed 0.7 percent, and Celgene Corp. added 3.4 percent for the best performance in the S&P 500.

**Internet Rally**

Internet stocks also rallied today. Groupon Inc., LinkedIn Corp. and Amazon.com Inc. advanced more than 1.5 percent. The Dow Jones Internet Composite Index is still 4.6 percent below a 14-year high reached in March.

Amazon advanced as online retailers are on pace to sell more products online than ever this holiday season.

More than 10 million new customers this holiday season tried Amazon Prime, the company’s $99 annual subscription that offers delivery discounts and video streaming, Amazon said today. The service may boast more than 30 million members, Robert W. Baird analyst Colin Sebastian wrote in a note to clients.
Newmont Mining Corp. advanced 1.5 percent as gold climbed the most in more than two weeks.

Airline stocks advanced as the price of oil declined. Republic Airways Holdings Inc. paced gains in the group, adding 1.9 percent. JetBlue Airways Corp. climbed 1.2 percent.

McDonald’s Corp. led an advance in the Dow, adding 1 percent. Walt Disney (DIS) gained 0.7 percent. The shares have climbed 5.4 percent since Dec. 16. Caterpillar Inc (CAT) rose 0.5 percent, extending a seven-day rally to 5.5 percent.

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