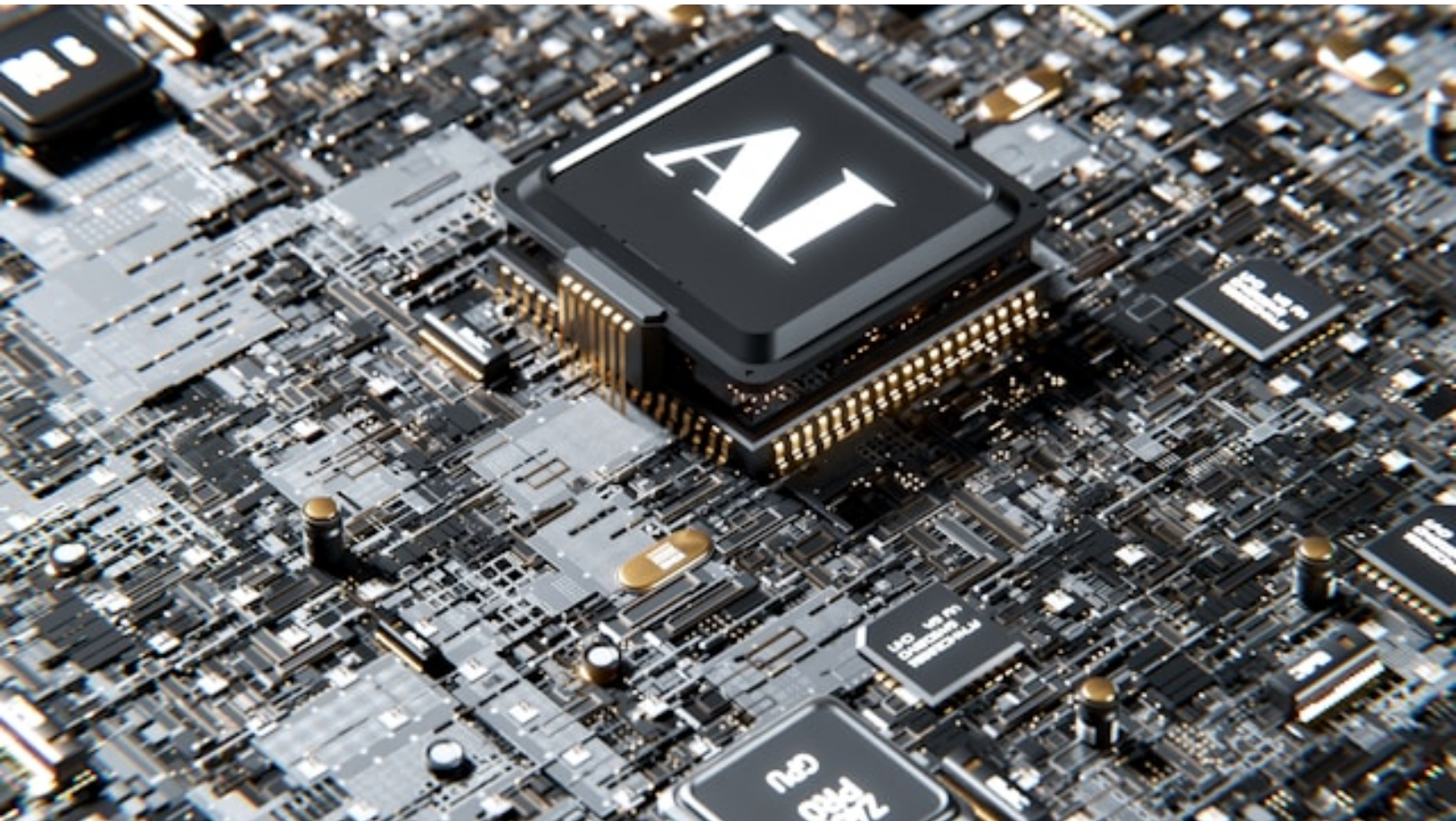


# How Irrational is Nvidia's Stock Price? That's Not the Right Question. Let's Discuss.

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I got my start in portfolio management and equity analysis in 1997, just as the “dot com” bubble, as that period became known after the fact, was gaining steam. Technology was one of the S&P 500 sectors I was responsible for following to discover and pitch investment ideas to the mutual fund management team.

Like today, with AI, technology was at a major inflection point with the advent of the internet, email, and network computing. It was exciting, and it was very easy to get caught up in the possibilities of what this new technology would portend for the future. Today, we are told that the most important AI technology company is Nvidia (NVDA); during the dot com bubble years (1997-2000), CSCO was at the center of internet and network computing growth story. There were other integral players in the build-out thesis, like Taiwan Semiconductor (TSMC), ASML (ASML), and Broadcom (AVGO), and they were the likes of Sun Microsystems (acquired by ORCL), EMC Corp. (acquired by DELL), and Intel (INTC).

Looking back on what internet and network computing ushered in over the last quarter century, one cannot dispute how revolutionary this technology inflection was. History teaches us that one technology revolution can sow the seeds for the next revolution. Since 1975, technology revolutions appear to occur every 25 years. In the mid-1960s, Gordon Moore theorized that transistors placed on a semiconductor chip would double every two years with minimal additional cost. Gordon Moore was an executive at Intel, and by 1975, his theory began to manifest itself and proved out over the next 34 years. Following my 25-year technology revolution theory, the late 1990s saw the beginning of an entirely new semiconductor-based computing application: network computing and the internet. Now, nearly 25 years after the late 1990s, we are seemingly entering the Artificial Intelligence (AI) computing age.

For an investor aware of what happened to the darling stocks of the dot-com bubble in the years following the 2000 crash, the question of the day is whether today’s multi-trillion-dollar mega-cap technology stocks present another bubble risk.

This is not an easy question to answer confidently, and the metrics that need to be used to provide the answer are uncertain because they will lie in the future. Equity markets are good at instantaneously pricing new information, but they are very suspect when pricing in future financial metrics. The primary driver of bubbles is often the market taking the path of least resistance to price in a mostly linear path for future metrics important to valuing equity. There are situations early in a technology paradigm shift when that linear path of least resistance underestimates the pace and impact of a technology shift. But, as the pace and impact of a particular technology shift becomes pervasive and dominates the psyche of growth investors, linear growth thinking moves from undershooting to overshooting the future financial metrics of the most integral dominant companies.

Today, the company that is most talked about and whose success is most directly leveraged to the future of AI computing is Nvidia (NVDA). Like Cisco Systems (CSCO) in the late 1990s, its stock price and valuation have been parabolic. See the comparative chart of these two companies below:

source : bespoke

## Nvidia (NVDA) Since May 2016 vs Cisco (CSCO) Since AOL IPO



*Performance compares CSCO since IPO of AOL in Feb 1992 to NVDA since May 2016 when Sundar Pichai called Alphabet an AI first company.*

A picture like this is interesting but not even close to conclusive because other data comes into play in addition to a stock's price action. From my perspective, Nvidia (NVDA) is better positioned competitively than Cisco Systems was in the late 1990s. The technology marketplace is much more global than in the late 1990s, providing Nvidia with a much larger total addressable market than the dominant U.S. technology companies of the late 1990s. Lastly, Nvidia's growth has outpaced expectations to a greater extent than did Cisco's during the dot com bubble years, which has kept Nvidia's profit multiple valuation metrics from rising to the stratospheric levels assigned to Cisco System's (CSCO) just before the burst of the dot com bubble in 2000.

Given that my professional investing experiences began during the Dot Com bubble years, I am naturally hesitant to chase stocks like Nvidia (NVDA) in the face of so much hype. However, I am also unwilling to emphatically state that stocks like NVDA are in a 1999-type bubble. If I were an analyst today who had to assign a Buy, Sell, or Hold rating on NVDA, I would have to choose Hold. Fortunately, I do not need to publish a rating on stocks. I now have to make client-by-client account decisions, often driven by considerations beyond valuation and growth factors, such as individual stock size weighting within an account and tax considerations.

We hold NVDA stock in some of our client portfolios today, with the earliest purchase date from January 2019, when the split-adjusted price per share was \$3.44. We have not purchased any shares since



January of this year, when the price per share was just under \$70 on a split-adjusted basis. With the stock currently trading at just over \$130 per share, we are content to look for less obvious opportunities with what we would consider a greater valuation margin of safety to invest in the so-called AI revolution. \$130 per share does not tell an investor anything valuable, but what \$130 per share means in terms of what value the market is placing on Nvidia as a company can be informative. At \$130 per share, the market is valuing Nvidia at \$3.2 Trillion. At \$3.2 trillion, Nvidia is valued at:

- Over two times the combined value of all 40 companies listed on the German Dax, including, for reference sake, Airbus SE, BMW AG, Volkswagen Group AG, SAP SE, Siemens AG, and Mercedes Benz Group AG.
- Greater than the combined value of Tesla (TSLA), Exxon Mobile (XOM), Amazon (AMZN), and Disney (DIS).
- Greater than the total value of all U.S. agricultural land and structures (2022 USDA estimate of U.S. agricultural land and structures - \$3.18 trillion).

With a career that has now spanned two major technology revolutions, I feel fortunate to have acquired the lessons learned over the last 25 years to guide our portfolio decisions not only when conditions are precarious but also when they become euphoric. We are very cognizant that human nature is a constant in markets. The names of companies change, and the growth stories change, but the psychological “fear of missing out” (FOMO) element of financial greed is constant. We will always stand back, look away from stock price-driven momentum arguments, and look at the bigger value picture that adds sobriety to the investment process.



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Disclosure:

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- [The Standard & Poor's 500](#), or simply the S&P 500, is a stock market index tracking the performance of 500 large companies listed on stock exchanges in the United States. It represents the stock market's performance by reporting the risks and returns of the biggest companies. Investors use it as the benchmark of the overall market, to which all other investments are compared.
- The NASDAQ Composite Index is a large market-cap-weighted index of more than 2,500 stocks, American depositary receipts (ADRs), and real estate investment trusts (REITs), among others. Along with the Dow Jones Average and S&P 500, it is one of the three most-followed indices in US stock markets. The composition of the NASDAQ Composite is heavily weighted towards information technology companies.
- [The Dow Jones Industrial Average \(DJIA\)](#), also known as the Dow 30, is a stock market index that tracks 30 large, publicly owned blue-chip companies trading on the New York Stock Exchange (NYSE) and the Nasdaq.
- The Russell 2000 index is an index measuring the performance approximately 2,000 small-cap companies in the Russell 3000 Index, which is made up of 3,000 of the biggest US stocks. The Russell 2000 serves as a benchmark for small-cap stocks in the United States.
- The Russell 2500 Index measures the performance of the 2,500 smallest companies in the Russell 3000 Index, with a weighted average market capitalization of approximately \$4.3 billion, median capitalization of \$1.2 billion and market capitalization of the largest company of \$18.7 billion.

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