Nasdaq-100 Equal Weighted™ Index: Another Tactical Opportunity at Hand?

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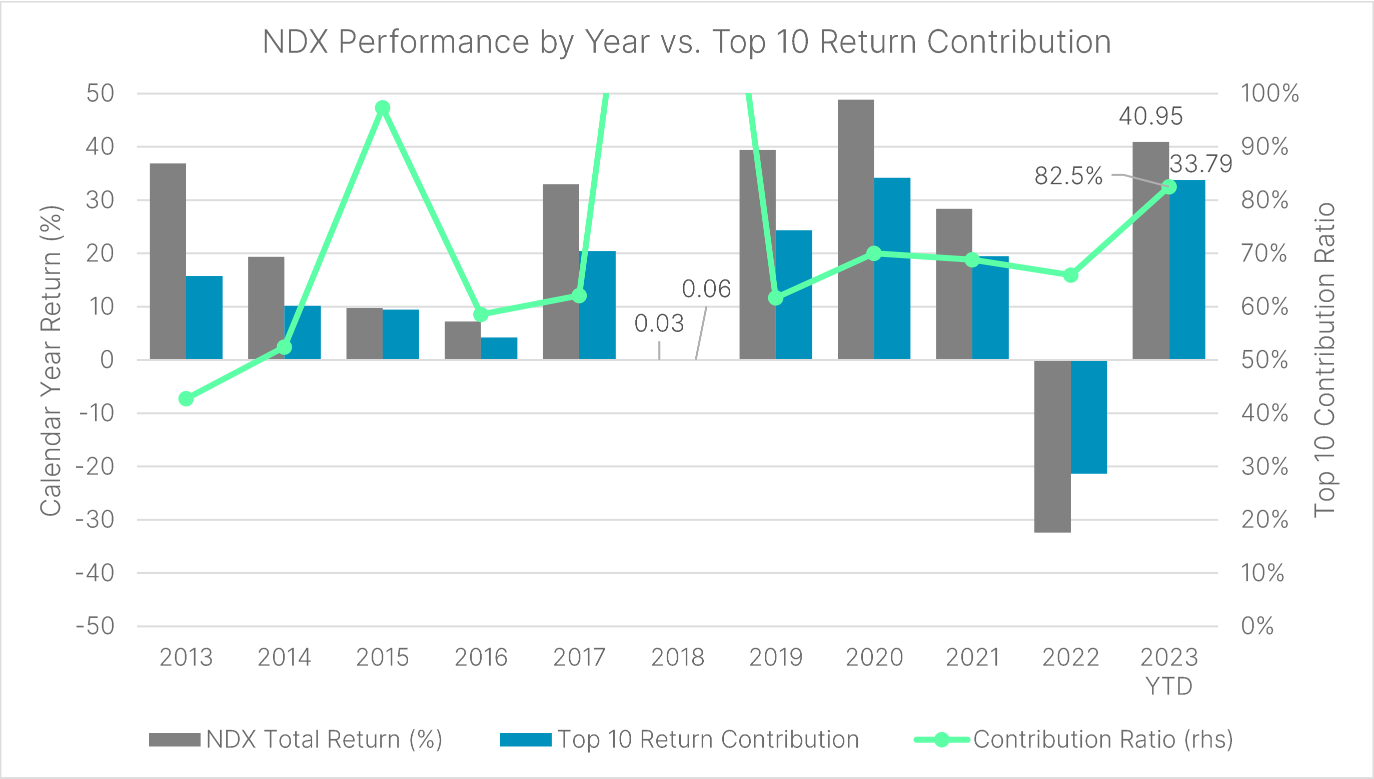
The Nasdaq-100® (NDX®) has experienced an extraordinary run-up in 2023, up 40.9% on a price-return basis YTD (as of November 8). Driven by eye-popping returns across its largest constituents – the "Magnificent Seven" of Apple, Microsoft, Alphabet, Amazon, Meta Platforms, Tesla, and Nvidia – the index has once again attained valuations last seen prior to the bear market in 2022. The Nasdaq-100 Equal-Weighted™ Index (NDXE™) has seen much more muted gains, up only 17.9% YTD. It outperformed NDX by approximately 8% in 2022, and may yet again be primed for a period of outperformance as valuations across the rest of the indexes' constituents either catch up to the Magnificent Seven, or vice versa.

Since the Magnificent Seven is a fairly recent grouping preference by the investment community – and there have been multiple iterations of FANG/FAANG/FANGMA over the past decade – it may be simplest to consider an analysis of the top 10 largest index constituents (company-level), by weight, over each of the past 10 years to put 2023's performance concentration in perspective. Specifically, the top 10 highest-weighted companies in the Nasdaq-100 (based on average weights throughout the year) contributed 33.8% of the index's 40.9% YTD return, for a contribution ratio of 82.5%. This is indeed higher than any year in the past decade except 2015, when they contributed 97.3% of that year's 9.7% index-level total return. On average, over the decade preceding 2023, the top 10 NDX weights contributed only 64.2% of the index's returns. (We are excluding consideration of 2018, during which the index returned 0.03%).

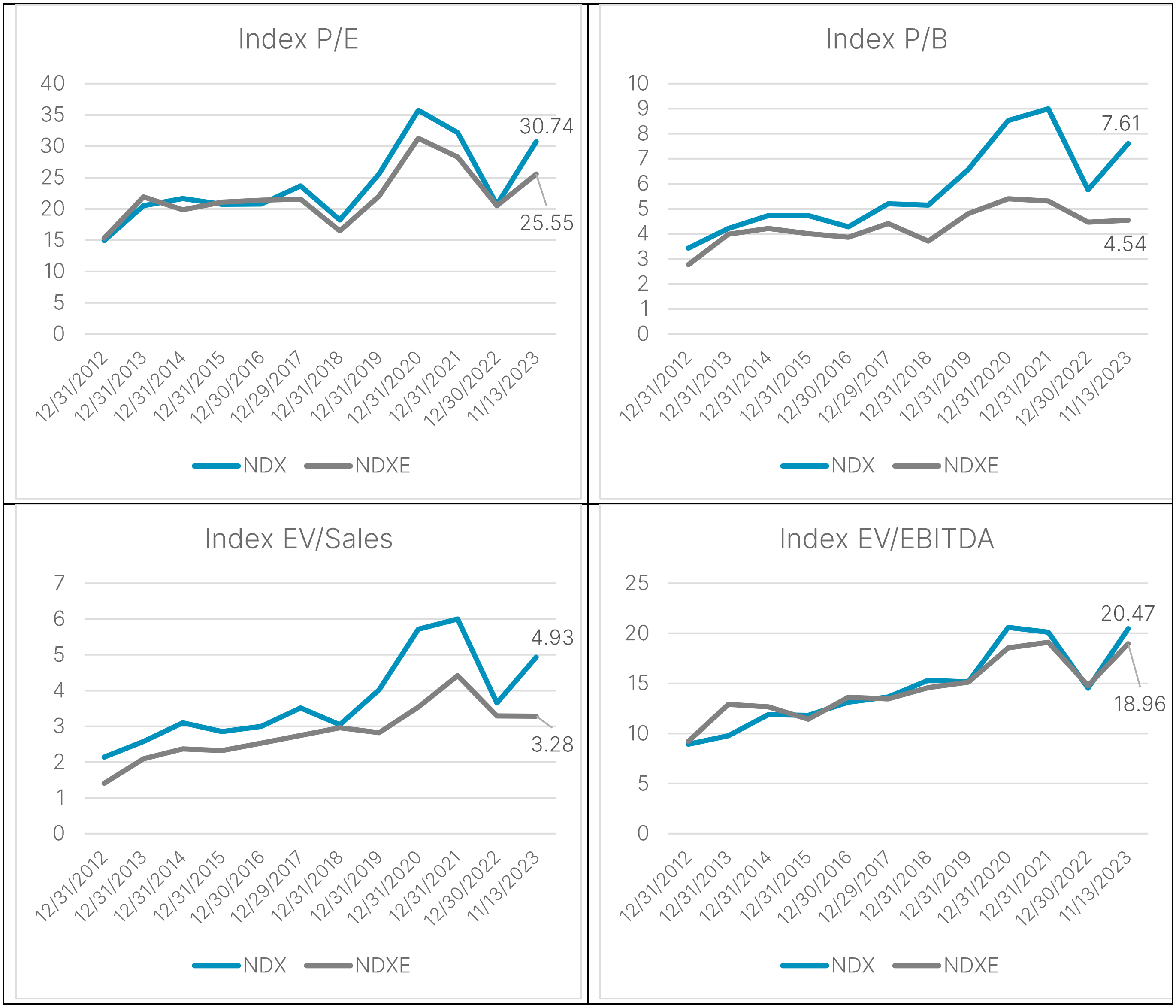


NDX vs. NDXE: Index Valuations Diverging Yet Again

As of November 13, NDX was at a trailing P/E multiple of 30.74, while NDXE was at 25.55 – a discount of 17%. This is a considerable rebound for NDX off of year-end 2022 levels of 20.68; for NDXE, the rebound is about half as dramatic, off of a base level of 20.49.

On a price-to-book basis, the valuation gap is now even more extreme, with NDX at a P/B multiple of 7.61 vs. 4.54 for NDXE: a 40% discount for the equal-weight version.

On an enterprise-value-to-sales basis, NDXE is at a 33% discount to NDX.
On an enterprise-value-to-EBITDA basis, NDXE is at only a 7% discount.



NDXE Can Offer Investors a Tactical, Complementary Tool to Manage NDX Exposure

As we can see historically, valuations tend to stay pretty close between the two versions of the Nasdaq-100, with the cap-weighted index subject to reversion towards the equal-weighted version following a pronounced divergence, as in 2020-2021. And as we've illustrated in the past, market leadership for the largest companies is constantly changing: of the Nasdaq-100's top 10 largest constituents today, only one (Microsoft) ranked in the top

10 at the turn of the century; a decade later, on December 31, 2009, only four (Microsoft, Apple, Alphabet, Amazon) ranked in the top 10. While betting against the Nasdaq-100 has not proven to be an enduring strategy for much of the past two decades, the index is very much prone to swings in performance and valuations that are driven by its largest constituents. Investors who recognize the benefits of tracking the index for its fundamental strength and exposure to innovation-driven growth can always look to its equal-weighted version as a tactical tool for navigating market fluctuations.

Sources: Nasdaq Global Indexes, FactSet, Bloomberg.