

## The Innovative Genius of the Magnificent Seven

The other day, Tom Lee noted in a Macro Minute video that [Granny Shots](#) is our core stock portfolio – the best of the best. Since its inception in 2019, the list has outperformed the benchmark S&P 500 by a wide margin, and it’s outperforming again in 2023 as technology stocks continue to drive major averages higher. Consider Granny Shots performance:

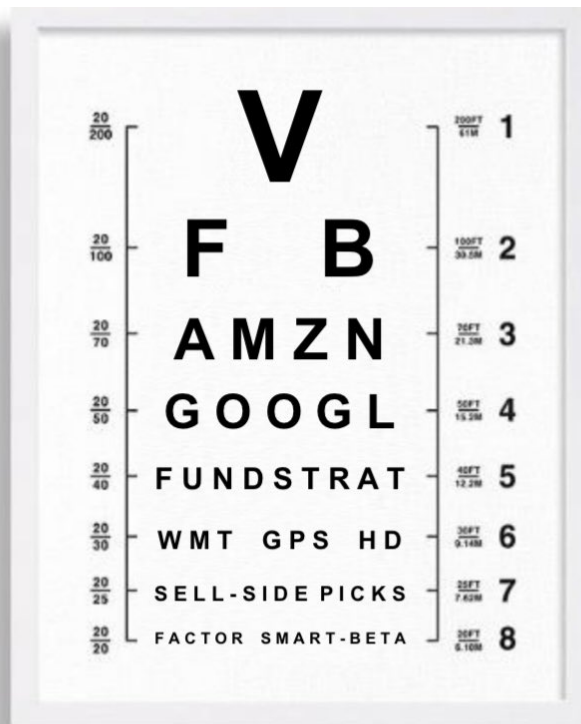
- +8,320 bps vs. S&P 500 since inception
- +266 bps vs. S&P 500 YTD
- Up 17% YTD on an absolute basis

This year is “on track to be one of the best years for Grannies, ever, looking to be even better than 2021,” Lee noted last week. He wasn’t mincing words, as the Granny Shots have centered on innovation and artificial intelligence to deliver superior returns to our members for more than four years. Notice AI as one of our inaugural themes back in May 2019:

Appendix:

### Vision Series Thematic

- World going “asset heavy”
- Auto-mation/ AI
- Millennials
- Asset heavy portfolio



The bulk of the outperformance has come from a sliver of the market – all large tech companies that generate cash, own a competitive advantage in their space, and innovate in extraordinary ways. The group of gunslingers dominating the tech rally since last October's lows have been dubbed as the "Magnificent Seven" – Nvidia (\$NVDA), Tesla (\$TSLA), Meta (\$META), Apple (\$AAPL), Amazon (\$AMZN), Microsoft (\$MSFT), and Alphabet (\$GOOG). All seven are Granny Shots, and Lee has been recommending nearly all of them for years, well before "artificial intelligence" became the buzzword it is today. Our macro work has always focused on the "long game," trends and themes that could play out over multiple years.

As you'll see below, many of those names are up more than four-fold since Lee added them to the portfolio, despite sizable drawdowns in 2022. Today, Lee notes that many recent college graduates still aspire to work at the big tech companies, which employ some of the country's brightest minds in computer science, engineering, and software. And while some onlookers argue their valuations are now stretched, Lee reminded investors of one of famed Fidelity manager Peter Lynch's core investment principles: You have to pay up for quality.

"As Peter Lynch would say, you don't want to be valuation-sensitive when you buy great companies," Lee said this month. "There isn't really another Apple out there or another Nvidia. As long as they're central to what's happening, especially AI or the consumer, I don't know if you want to say rate hikes will kill their stories."

In this *Signal From Noise*, we revisit the Magnificent Seven: Their performance, why they've outperformed drastically, and why we remain constructive on the names for the years ahead. As with any specific stock mentioned in this column, investors should conduct further research before acting on an investment. Much depends on one's risk profile, time horizon, and investment objective.

That said, we see our Granny Shots stock-picking product as a tangible way to outperform the market without the mountains of work required to evaluate individual stocks. Remember that, since 1926, most of the U.S. stock market's returns have come from less than 4% of companies. Identifying those is a monumental task, but the following businesses have continued to prove their worth over and over.

## Nvidia

Word is out on Nvidia, which has *the* product: a data processing chip that's key to A.I. development, including the livelihood of ChatGPT and Bard. But the company is hardly new to us, as the semiconductor leader has been a Granny Shot for four and a half years, gaining nearly 1,000%. Last fall, we reiterated our view on [semiconductors](#), Nvidia included. The stock has since risen three-fold.



The price could be stretched in the short run, though for long-term investors, we still believe Nvidia is one of the best names to own in A.I. Its data center revenue alone stands at about 24% and is growing quickly. We're only in the early innings of the A.I. revolution, so when the technology matures, Nvidia's data center revenue could be its top revenue segment. Co-founder and CEO Jensen Huang has said, "Software is eating the world, but A.I. is going to eat software."

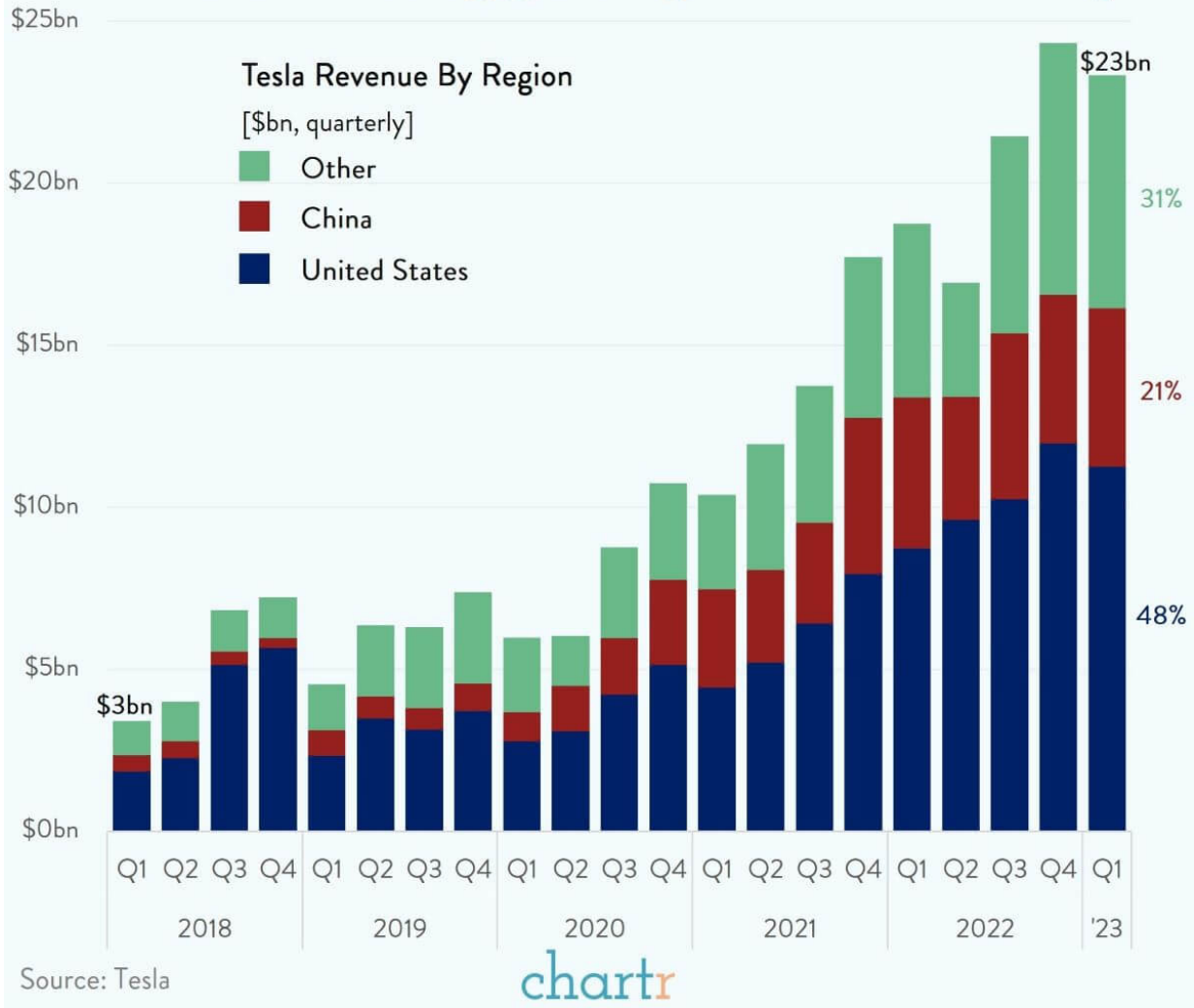
Drawdowns in excess of 20% are routine for Nvidia, whose share price was cut in half last year alone. But the demand for its chips is growing. It pioneered graphics processing units (GPUs) to make video games more realistic, and it's since expanded to AI chips used in supercomputers, data centers, and even drug development. Nvidia's GPUs function as accelerators for central processing units, or CPUs, made by other companies, and it's working on "supercomputers" combining its own CPUs and GPUs. Its chips are also used for bitcoin mining and self-driving electric cars. Whether the rally continues this year is unknown. What's clear to us is that, as Lee said this month, the company's numerous competitive advantages are unlikely to change anytime soon.

## Tesla

Tesla sometimes gets categorized as a car company, but it's really a technology and energy company, a view Lee held when he made the Elon Musk-led giant a Granny Shot in January 2019. Shares have since risen 10x as the electric vehicle market has a first-mover advantage, a controversial but visionary CEO, and enormous [A.I. capabilities](#).

Now Tesla is eyeing China, home to more than 50% of the world's EVs. China is contributing about \$5 billion in revenue or 21% of Tesla's total figure. Its most productive factor, in Shanghai, made over 700,000 Model Y and Model 3 vehicles last year, more than half of the company's output.

# The Chinese Market Has Been Pivotal In Tesla's Staggering Growth Story

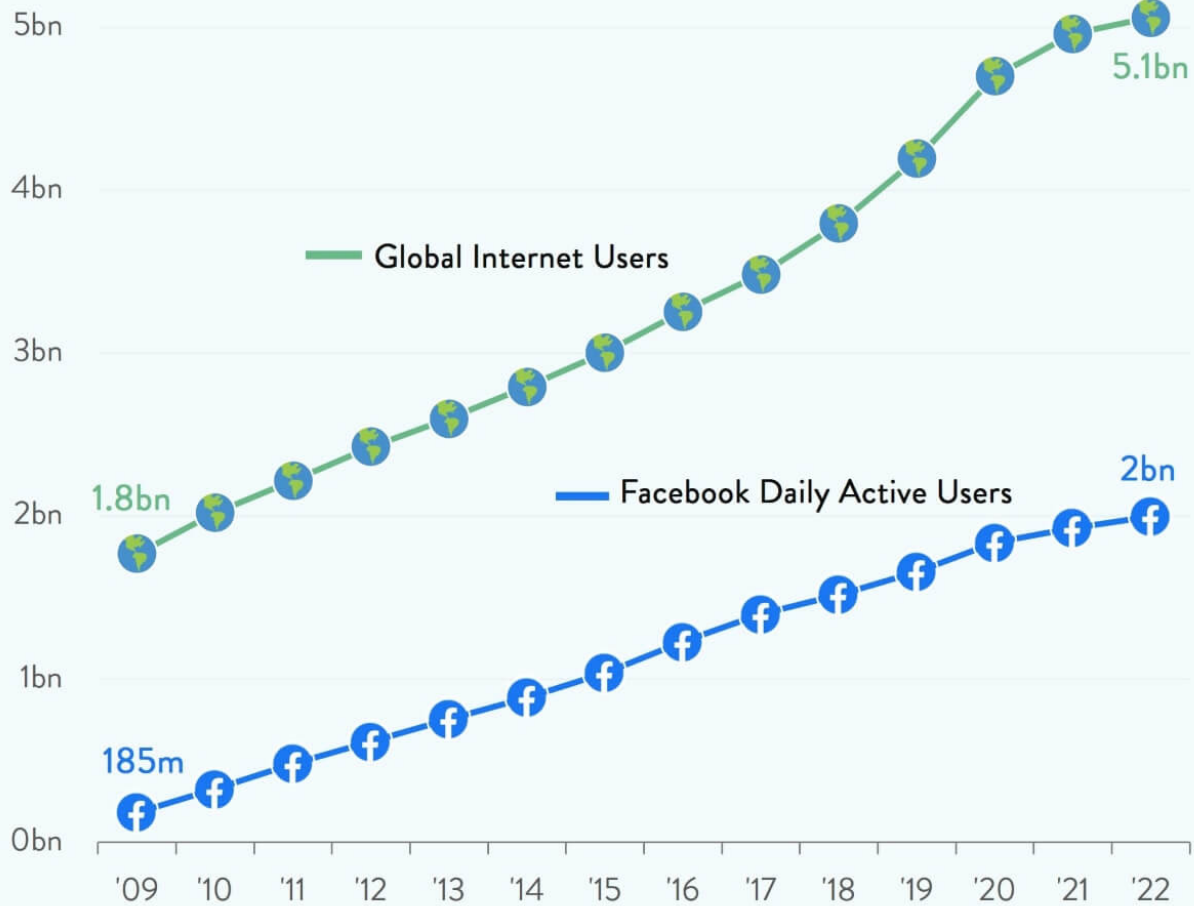


After a brutal 2022, Tesla shares have risen nearly 140% this year, mostly on hopes that Tesla will continue to innovate in A.I. with full-self driving vehicles, “robotaxis,” and an autonomous humanoid robot capable of performing unsafe, repetitive, or boring tasks. At a steep valuation today, the question many investors are asking: But how much of that is already priced into the stock price? It’s a fair question, but we believe Tesla has continued to be a tech and A.I. pioneer, not just a car company.

## Meta

Lee added Meta, currently a “Super Granny” shot, in July 2022. It’s up about 70% since amid a scorching rally this year, thanks to its 3 billion-plus daily users on its social media sites and its incorporation of A.I. into nearly everything it does. Nearly 40% of global internet users are on Facebook daily. From 2013 to 2022, its operating income soared from \$2.8 billion to \$28.9 billion. It’s utilizing A.I. to keep users engaged incrementally longer, and it’s trading at a reasonable forward price-to-earnings ratio of 25 despite its 125% YTD.

## Almost 40% Of Internet Users Are Logging Into Facebook Every Day



Source: Company Reports, ITU via Our World In Data, DataReportal

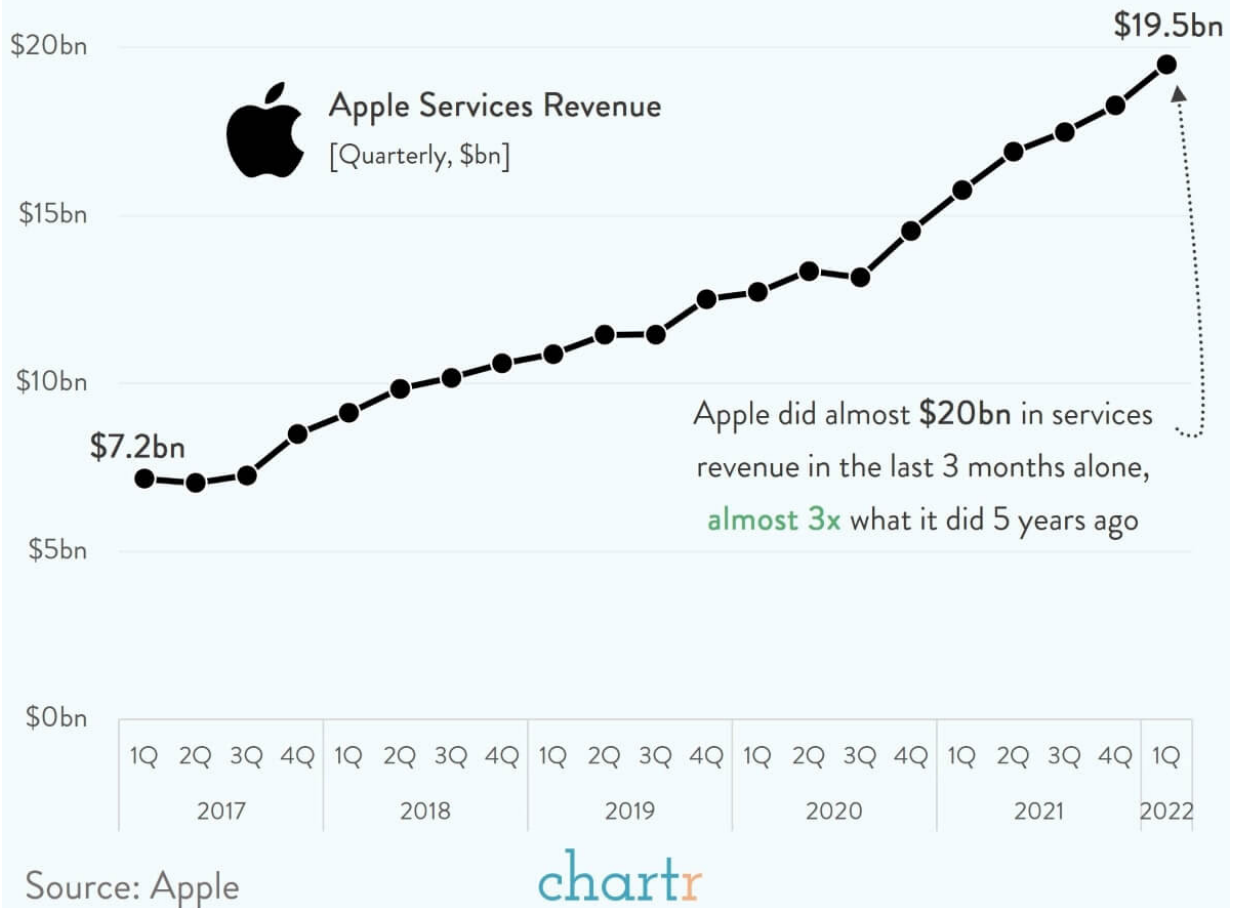
Meta has promoted an open-source approach to AI to widen access to the technology. In February, it released its LLaMA large language model under an open-source license, allowing anyone to view and manipulate the code. The company is hoping that will help it compete against rivals Google and Microsoft. Wall Street remains bullish on its investments in A.I., and while regulators are still skeptical about whether Big Tech can handle A.I. responsibility, Meta is innovating while CEO Mark Zuckerberg heralded 2023 as the “year of efficiency” for the company that turned 19 earlier this year.

## Apple

Apple received one of its most resounding pieces of praise ever just last month from a very wealthy man in Omaha. Warren Buffett, whose Berkshire Hathaway began buying Apple shares in 2016, said Apple is “probably the best business I know in the world,” an endorsement that means something. He underscored how indispensable its devices are to users, namely the iPhone. He hailed Tim Cook as “one of the classiest CEOs” and said Steve Jobs’ handpicked successor has run the company “extraordinarily” well, adding: “We’ll never own a business that makes so many people happier and is so useful for them.”

With about 2 billion active Apple devices worldwide, we believe there’s still ample room for continued growth. Whether the Apple Vision Pro becomes the company’s next big thing is almost ancillary; the core business of iPhones and services is that healthy. Apple’s services business alone makes more than double what Netflix makes per quarter. With people holding onto their phones for longer, Apple is unlikely to keep selling quite as many iPhones going forward. But Apple keeps growing its “walled garden,” a strong economic moat and cycle that keeps its rabid consumer base loyal. Its \$99 billion in profit last year was more than those of JP Morgan and Citi combined.

# Apple's Services Side-Hustle Is Now An \$80bn+ Annual Business



There's also Apple's push into financial services, another substantial endeavor driven by a cornerstone product, Apple Pay, which has roughly 75% adoption among iPhone users. Apple is competing with Mastercard and Visa with features enabling iPhones and iPads to send and receive payments. iPhones could eventually replace leather wallets altogether. The possibilities aren't difficult to imagine for Apple's continued emergence in finance.

Lee added Apple to the Granny Shots list at inception in January 2019, and the share price has soared roughly 350% since. It was one of Lee's top picks out of the pandemic and he reiterated his positive view again in his 2023 outlook. It has gained 51% so far this year.

## Amazon

Like Apple, Amazon became a Granny Shot in January 2019. It has since underperformed the S&P 500 by about 15% over the period, but we remain constructive on the e-commerce and cloud giant. When Andy Jassy replaced founder Jeff Bezos as CEO two years ago, we kept Amazon in our marquee portfolio, not only because of Amazon’s dominance in online retail but because Jassy joined Amazon in 1997, worked under Bezos, then helped formulate the idea that would become Amazon Web Services (AWS).





Amazon Prime is still a behemoth, with U.S. subscribers surging from about 27 million in 2013 to more than 170 million just eight years later. Meanwhile, in his annual shareholder [letter](#), Jassy said AWS has an \$85 billion annualized revenue run rate and “is still early in its adoption curve,” adding that Amazon is still in its “early days.” Jassy reminded investors that Amazon has been working on its own large-language models for years, believing “it will transform and improve virtually every customer experience.” Many of the world’s richest investors hold Amazon in their portfolios, and we believe it’s for good reason.

## Microsoft

As Microsoft shares climb higher, analysts have been raising their price targets to the high \$300s, with one Evercore analyst raising his to \$400, writing: “The infusion of A.I. across Microsoft’s product portfolio represents a potential \$100 billion incremental revenue uplift in 2027.” Lee has been bullish on Microsoft’s A.I. capabilities and cloud growth (Azure) since December 2019, when he added the Bill Gates-founded company to Granny Shots. It has since beaten the S&P by about 90%. Much of that appreciation derived from the growth of Office 365 and Azure, which helped Microsoft add \$100 billion in revenue over the past four years. A.I. could drive another \$100 billion in revenue.

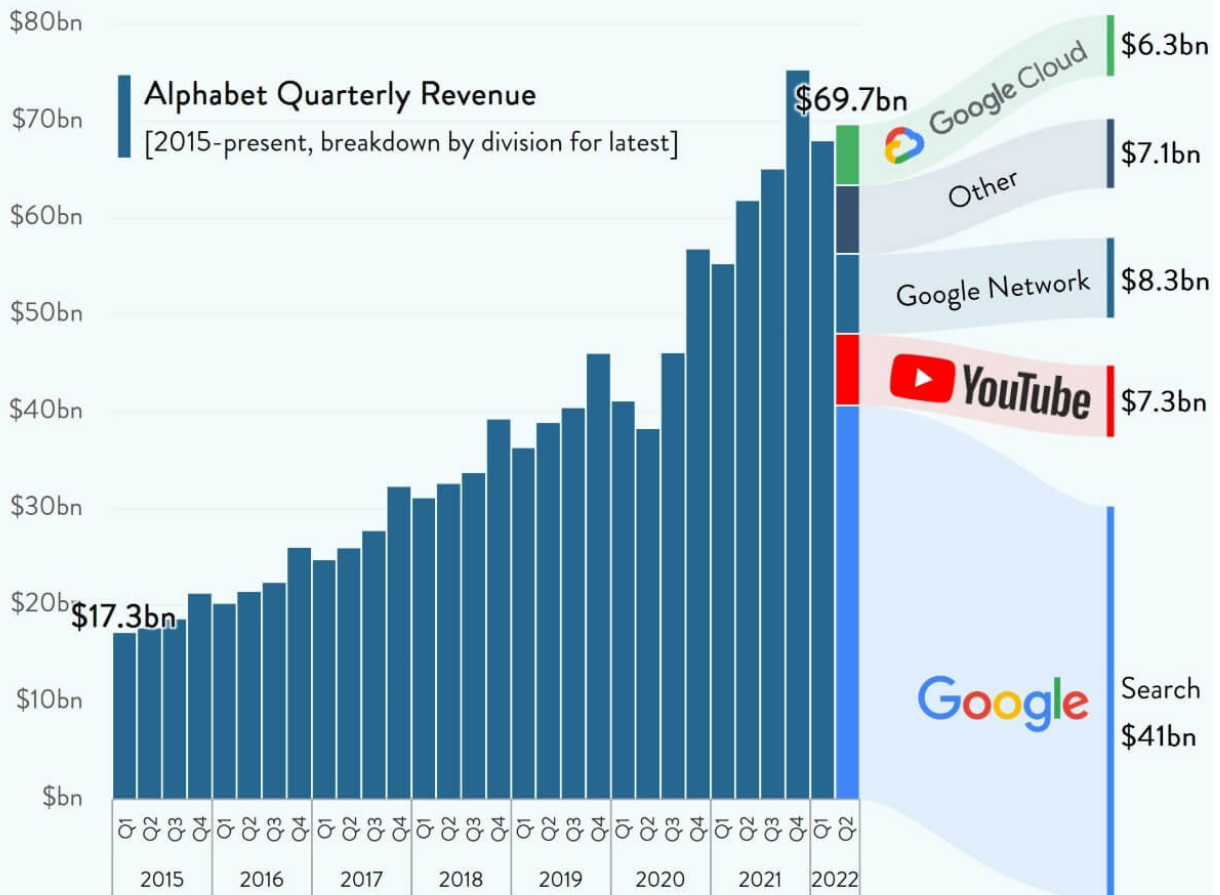
Back in 2019, the company invested \$1 billion in ChatGPT-maker OpenAI. In January, Microsoft announced it was investing another \$10 billion in OpenAI, giving it access to some of the most popular and advanced artificial intelligence systems. Microsoft’s market share in search is tiny compared with Alphabet, but AI-powered Bing and Edge are gaining traction.

CEO Satya Nadella said this year that AI-powered search is the biggest thing to happen to the company in the nine years he’s been CEO, saying, “I have not seen something like this since I would say 2007-08 when the cloud was just coming out.” Speaking of the cloud, Azure is still growing like a weed. Even Microsoft’s cybersecurity segment, which reports more than \$15 billion in revenue, is becoming more and more a core piece of its pie.

## Alphabet

There are worries that ChatGPT and other A.I. will disrupt Alphabet’s core business, Google Search. Google parent, Alphabet, has been a Granny Shot since 2019, outpacing the S&P by more than 50%. Alphabet has managed to grow its revenue every single year, led by Google Search, which represents more than half of Alphabet’s total business. YouTube is much smaller but growing mightily.

# Alphabet Has Diversified As It's Grown, But It's Still About Search



Source: Alphabet, Koyfin

charttr

N.B. "YouTube" is just YouTube Ads

Just like the other six companies outlined above, we believe Alphabet is a revolutionary company in artificial intelligence. CEO Sundar Pichai has said A.I. will be “more profound than fire or electricity,” while unveiling A.I. technology in Gmail that can produce replies in seconds. That’s likely only scratching the surface of what Alphabet will be able to do A.I.-wise in the decade ahead. “You will see us be bold,” Pichai told The New York Times this year.

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