JOHN DEL VECCHIO'S

Hidden Fortunes

UNCOVERING THE STOCKS THAT PAY YOU FIRST

10 Stocks NOT to Touch Right Now

By: John Del Vecchio, Forensic Accountant & Editor of *Hidden Fortunes*

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Rising tides do not lift all boats. Until late 2018, it was easy sailing in the stock market. Since the 2009 lows, it's been almost straight up. For nearly every stock.

But, starting in 2018, something changed. Many individual stocks started to falter even as the indexes hugged their highs. By the time anyone noticed that the market was under pressure, more than 50% of the stocks in the S&P 500 Index were already in bear market territory.

A lot of boats have started to sink.

The thing is, we've experienced one of the longest bull markets. Ever.

When we do have a bear market, it'll be nastier than normal. That's because all the excesses of the last 10 years, like quantitative easing, boosted asset prices to nosebleed levels. Stock valuations hit historical highs. That story won't end well.

Another thing happened along the way. Investors piled into index funds. Those funds bought every stock, good or bad. That also pushed their prices up way too high. It created stocks that everyone owns! So, what happens when investors rush for the exits all at once? Stocks will likely overreact to the downside.

Chances are you own several stocks that may be hazardous to your wealth as we head into the next bear market, whenever that is.

This report highlights a handful of stocks that I think could do real damage to a portfolio in 2020 and beyond due to bear market activity and over-ownership.

How did I come up with this list?

Over 10 years ago, I developed my own software that analyzed the financial statements of public companies. It uses many formulas that I developed myself having pored over the financial filings of more than 1,000 public companies.

It's called Forensic Accounting Stock Trackers (FAST). FAST quickly separates the wheat from the chaff in the market. Just because a company reports $1.00 of earnings per shares doesn't mean it's real.

Accounting rules allow for a lot of leeway that management can use to their advantage. They can make the numbers look better than they really are. Then you, the average investor, get the wool pulled over your eyes. Meanwhile, management gets to reach into the cookie jar and enrich themselves through an inflated stock price.

In the institutional world, big investors pay a lot of money for lists like this. Some firms paid up to $500,000 a year for a list of the top-scoring stocks from one major trading firm I did business with. That's too rich for my own blood, and I developed my own tools. They liked *my* first book on this topic so much that they used it to sell *their* software. Today, there's about $800 million managed using some of the FAST formulas I developed.

I like to focus on the stocks that might do damage to a portfolio. I call them "clunkers."

What can you do about these potential clunkers?

If you want to profit from stocks falling apart, you could short them. Shorting a stock means selling it now and then (hopefully) buying it back at a cheaper price. You profit from the difference.

Shorting stocks has been brutal the last 10 years. I should know. I've been doing it professionally for about two decades. Most of my colleagues are out of business. Some are probably in insane asylums from banging their heads against the wall as crappy companies saw their stock prices soar to the moon.

But shorts in a bear market will probably pay off even bigger than the last two crises. That's because the last two bubbles were created by hype in the internet market and real estate. Now, *everything* is inflated. There's nowhere to hide!

The second thing you could do if you own these stocks is watch them. Closely. Every move. Risk is higher here. So, a whiff of something not right with the company and it's time to bail. You can also tighten stops in order to lock in gains.

Third, you can sell. You can sell now. You can sell later. Sell when it's right for you.

Finally, you can do nothing. Sometimes the best thing to do is nothing. But, when market valuations are at extremes, market sentiment is way too bullish, and stocks are starting to break down, sitting around spitting into the wind isn't a strategy I like. I don't want to take a 75% loss. Even if it's on paper.

These are the type of losses we're looking at here. Without further ado, here's the list of stocks that worry me for 2019 and beyond.

The Clunkers for 2020

Apple (Nasdaq: AAPL) is the most widely held stock.

It's often the biggest component of virtually any portfolio you can own. Especially if you own an exchange-traded fund (ETF).

Not only is Apple over-owned, it's finest days may be behind it.

How so?

Well, recently, Apple's management told investors that it has decided to stop disclosing iPhone unit sales.

According to the company's CFO, Luca Maestri, the "number of units sold in a quarter is not representative of the underlying state of the business."

To put it mildly, that's a ridiculous statement.

Of course iPhone unit sales matter!

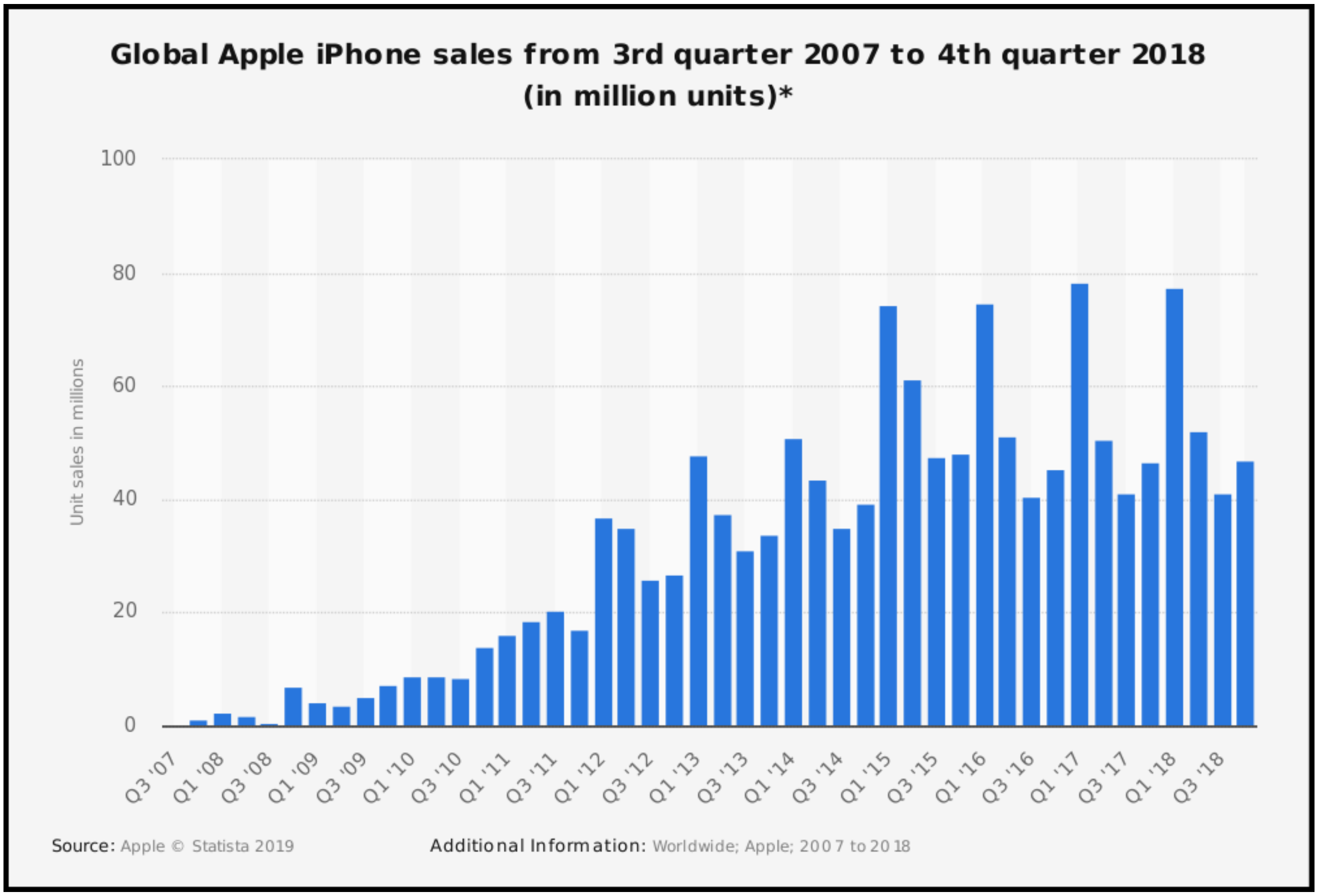
Analysts and investors burn the midnight oil to try and forecast iPhone sales. It's a key metric in the performance of the company.

Unfortunately for Apple, unit sales are starting to look lackluster.

What’s saved Apple is that the average selling price has been much higher than investors expected. But the gap between Apple’s prices and the rest of the industry are large enough to drive a Mack truck through!

How much more can Apple squeeze consumers with minor changes like a better camera?!

That’s the question.



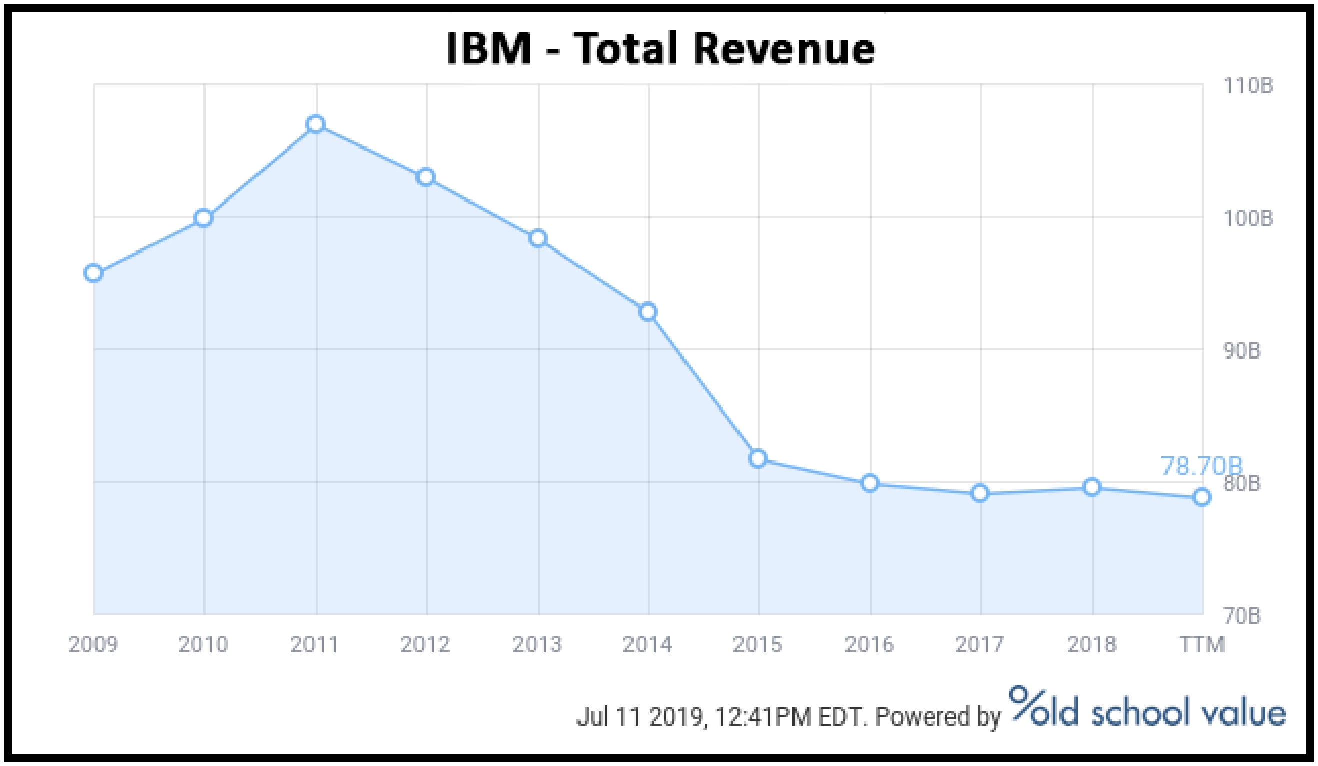
If there were a manual on forensic accounting and a huge tipoff that a company is about to come unglued, Rule No. 1 would be that if a company stops reporting important data to investors, look out below.

Companies don’t stop reporting key data when the numbers look great. Instead they highlight them in the press release!

IBM (NYSE: IBM) has been one of my favorite punching bags for years. I've shorted the stock numerous times in this bull market. Successfully.

I've recommended to newsletter subscribers several times to short the stock in this bull market. Successfully, too.

I don't think the bottom is in. The stock continues to perform poorly. Eventually, it could become irrelevant. IBM is over-owned because it's a major component of the large indexes like the Dow Jones Industrial Average. But maybe not for long…



IBM is like the Titanic. It hit the iceberg a long time ago. The ship is sinking. The orchestra is playing on deck.

Clueless investors have been duped by management, who wasted tens of billions of dollars in capital buying back stock and supporting the dividend as the business around it melted like an ice cube.

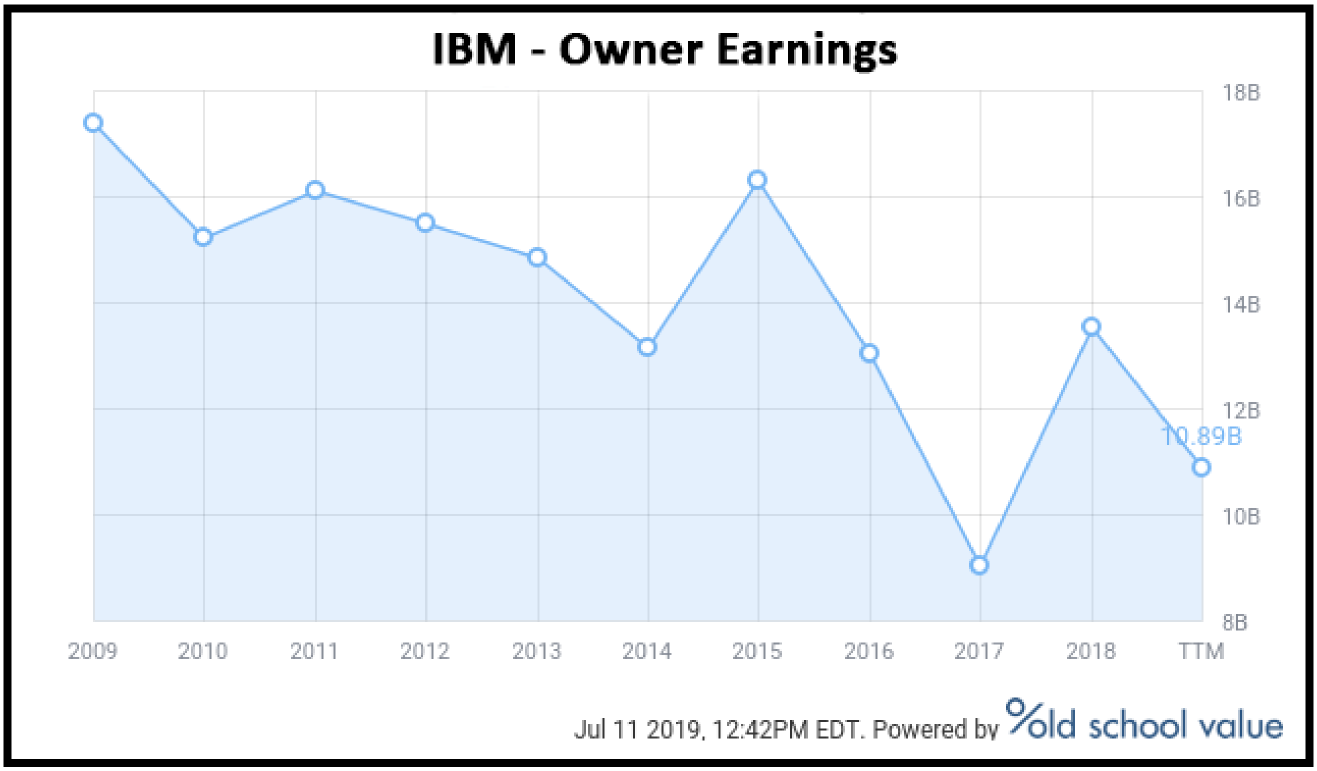
A huge problem facing IBM is, back in the old days, when large contracts came up for renewal, nearly 100% of the time the customer renewed the deal with IBM. Often at a higher price. Business was sort of on autopilot. There was a saying that buyers never got fired for doing business with IBM.

Times have changed. Competition is fierce. The world is flat.

Competitors in India are more agile. Deals don't get renewed like they used to. Pricing is under pressure. Growth is slowing. Cash flow is weakening.

The company can't get back the billions of dollars it wasted to engineer its financial statements.

When IBM gets kicked out of the big indexes, there will be lots of sellers. The next bear market will also likely see threats to the company's dividend. It's no longer a widow and orphan stock.



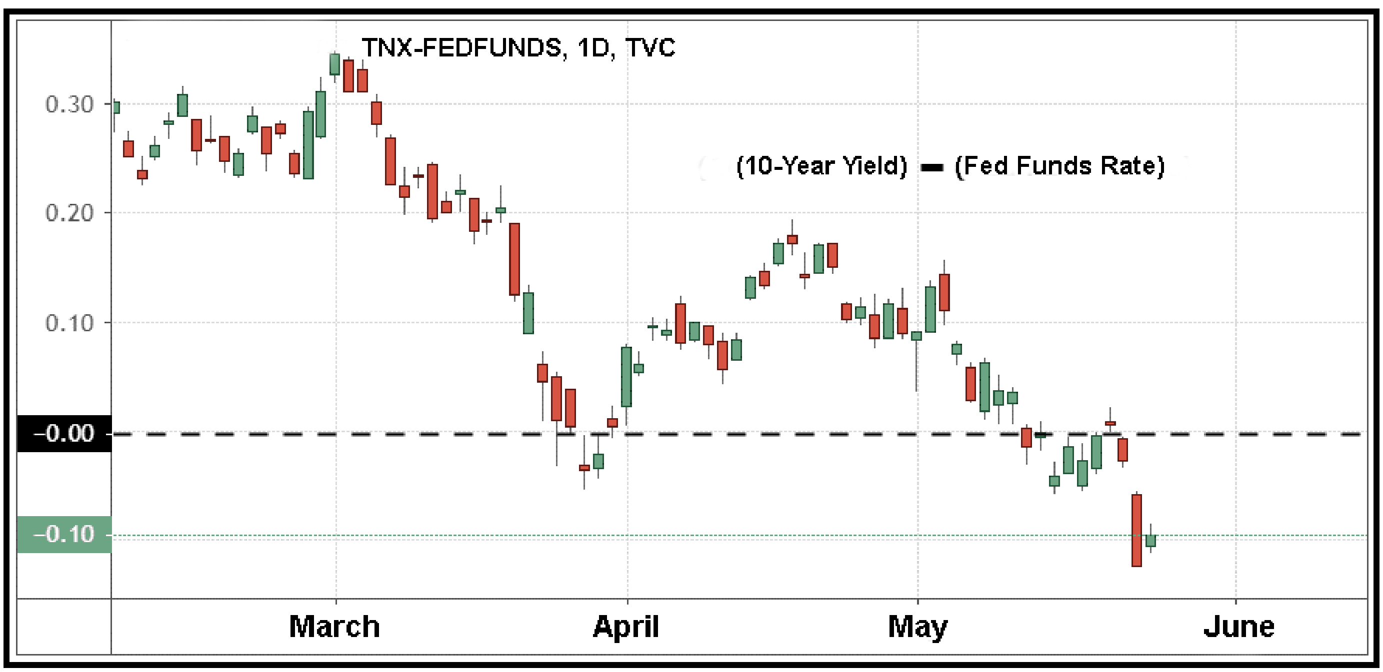
The Big Bank Stocks mostly move in the same direction. It's a highly correlated trade. So, I'm not singling out a particular company like Lehman Brothers or Bear Stearns, both of which bit the dust in the last crisis.

This time around there isn't an obvious catalyst in my opinion. A dozen years ago, it was obvious that the housing market was overheated, and banks were playing games with goofy mortgages. But bank stocks started to head south in 2018 *before* the rest of the market.

It's not just the United States, either. Stocks like Deutsche Bank (NYSE: DB) and UBS Group (NYSE: UBS) have been pounded. The fact that they are already in the dumps before anyone knows why makes me think there could be a huge shoe to drop. And it might be on a global scale bigger than anything we have seen in the last 20 years or more.

Who knows what types of exposures these foreign banks have?! I know one thing: It's complex. It's not transparent. So, when something is complicated, and you have no idea what you're looking and, it's best to run away as fast as you can.

An inverting yield curve won't help banks either. The shrinking spread between their funding costs and return on lending could further throw a wet blanket on their returns going forward.



Netflix (Nasdaq: NFLX) has proven that betting against the media giant has been one of the biggest losing propositions of the last market cycle.

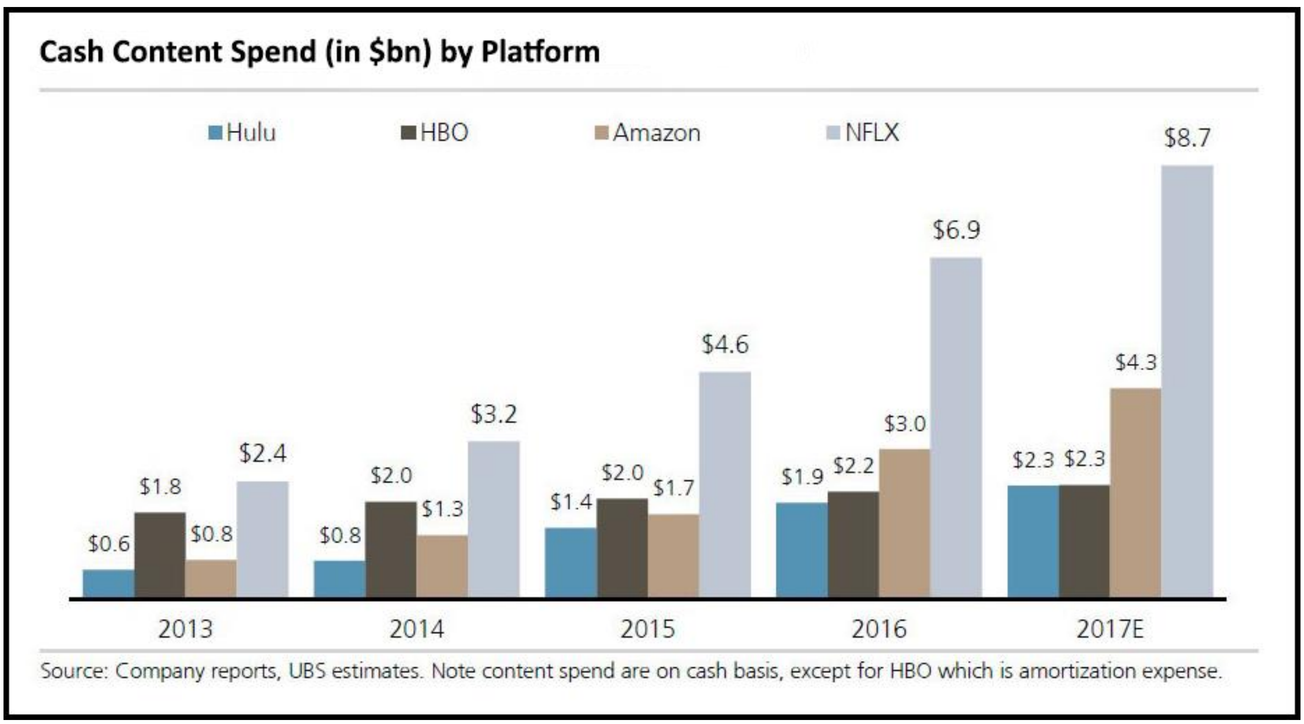
The company has crushed it. Even though the stock got punched in the nose at the end of 2018, it still dramatically outperformed the stock market and has been a total winner. So, what's different this time?

The earnings quality is terrible. Cash flow performance is weak. What's worse is that I don't know how it gets any better.

You see, Netflix is forced into spending billions and billions of dollars on new content to stay competitive. If you pay attention to popular media, you would think that Netflix original programming is knocking the socks off the competition and that all those billions of dollars is money well spent.

Details, details. Of the most views on Netflix, "The Office" is No. 1. "Friends" ranks second. "Parks and Recreation" is third. The problem with this? Well, Netflix doesn't own those shows. So, they could be pulled. Meanwhile, the company needs to invest another $100 million to keep "Friends" on the platform.

As for their own content? The top spot is at No. 14 with "Orange Is the New Black," with just 0.74% of the views. Overall, deteriorating earnings quality, weak cash flow, and some hype is a poor recipe for a stock's performance.



Deere & Company (NYSE: DE) has been making agricultural equipment for over 180 years. So, a bear market is unlikely to wipe the company out. Unless it's a 100-year storm. That said, Deere's earnings quality scores have deteriorated sharply in recent periods.

What's more troubling is that the company heavily financed sales in recent years.

Financing can be dangerous because aggressive terms may cause a customer to buy something today that they otherwise would have waited until a later date to purchase.

As a result, revenue is pulled forward and "stolen" from the future. Now you have to find a new customer to fill that stolen revenue. Of course, if business is booming, a company wouldn't have to offer favorable terms in the first place.

The problem is, in bear markets, credit typically freezes up. In addition, if the economy tanks, what are they going to do, repossess a tractor in the middle of the night?! It's not worth much.

In the last bear market, Deere's stock fell about 65%. With heavy financing of sales this time around, I fear the next rough patch could fare far worse.

Deere & Company Worldwide Financial Services Operations										
	2009	**2010**	**2011**	**2012**	**2013**	**2014**	**2015**	**2016**	**2017**	**2018**
Revenues	\$2,283	\$2,298	\$2,373	\$2,454	\$2,569	\$2,805	\$2,816	\$2,919	\$3,179	\$3,560
Operating profit(2)	242	499	725	712	870	921	963	701	715	792
Net income	203	373	471	460	565	624	633	468	477	942
Total assets(3)	25,869	27,439	29,746	34,449	38,604	42,737	40,866	40,837	42,596	45,720
Financing receivables and leases-net	20,091	21,847	24,965	28,293	32,922	36,022	34,613	34,730	35,857	38,072
Trade accounts and notes receivable-net	2,346	2,980	2,807	3,333	3,556	3,554	3,553	3,371	4,134	4,906
Receivables and leases administered-net	22,729	25,029	27,918	31,746	36,559	39,629	38,188	38,116	40,001	42,985

You would think when the CEO of a company smokes weed on a podcast and gets busted by the Securities and Exchange Commission that investors would run the other way!

Well, that hasn't been the case with **Tesla (Nasdaq: TSLA)**.

That concerns me. Tesla has an inflated market value and faces increasing competition.

The company benefitted greatly from the sale of environmental credits to other car companies. But those types of tailwinds are unlikely to prop up the stock as they go away.

The balance sheet is bloated with debt, and it would not be surprising if the company comes hat-in-hand looking for more money. Meanwhile, big automakers are rapidly moving into the electric and self-driving space.

As competition heats up, the company's performance is already starting to falter. Recently, deliveries have fallen short of expectations while inventory has built up.

Time to take another toke on that joint.

TSLA	Sep-17	Dec-17	Mar-18	Jun-18	Sep-18	Dec-18	Mar-19
Quarterly Customer Deposits	686.1	853.9	984.8	942.1	90.58	792.6	768.3
Vehicles in Transit	4,858	3,380	6,100	15,058	11,824	2,907	10,600

Under Armour (NYSE: UAA) was a key growth stock not too long ago.

Every manager needed to own it when the company was growing at over 25% and blowing away its competitors. Back then, I shorted it.

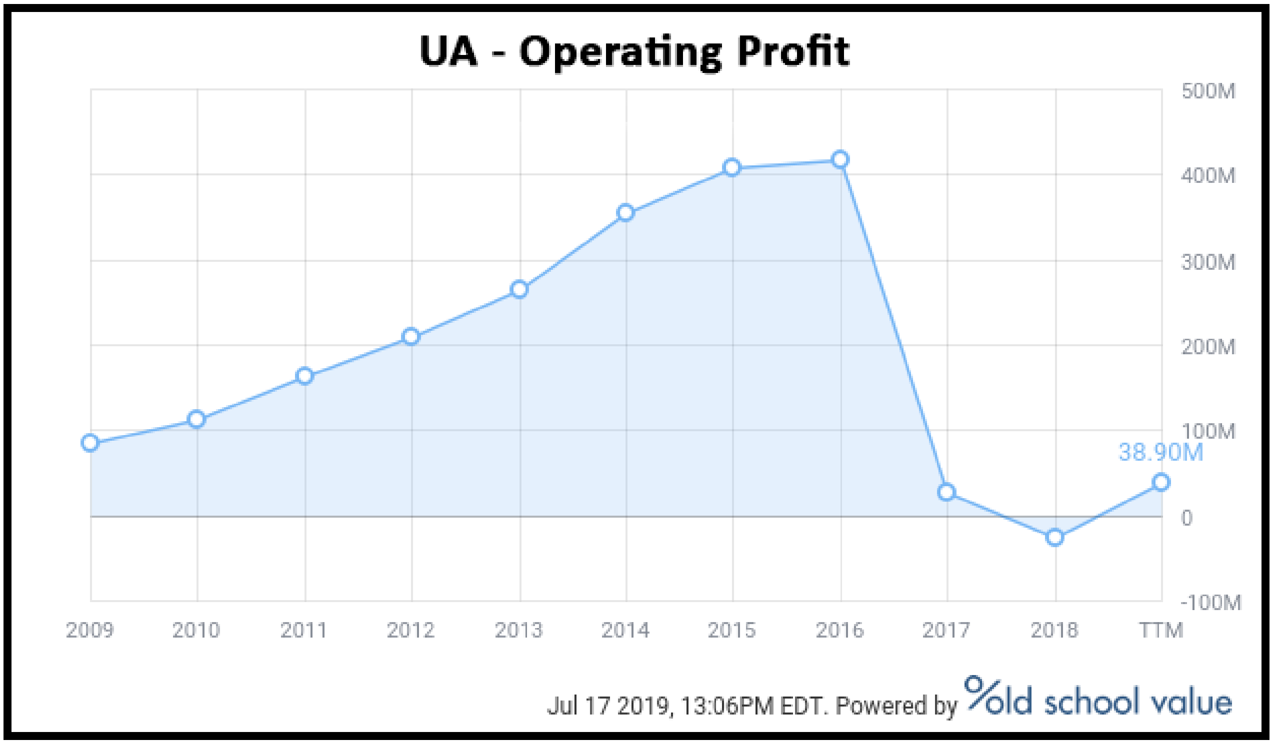
The stock cratered, and I made a tidy profit. It went so low it looked like an interesting buy. So, I recommended buying it in *Hidden Profits*. We made a quick 49.27% return as the stock rebounded sharply.

However, I worry that the company isn't out of the woods.

One of my primary concerns had been a buildup in inventory. When that didn't translate into sales, the company's world fell apart. It got so bad that the stock was too low to be too concerned about inventory issues. Those were baked into the cake.

Then the stock doubled. It's come back a bit, but inventory buildup is still an issue. It's high, and it's not being resolved. And retail growth is subpar. Direct to consumer sales continue to trend poorly. As a result, I'm concerned that the ship has not been righted.

Meanwhile, margins are likely to come under more pressure, earnings quality is trending poorly, and shareholders are being diluted.



In a world where everyone is on the go, the market for energy drinks should be on fire.

Not for **Monster Beverage (Nasdaq: MNST)**.

The company has taken it on the chin as a wave of bad news has washed over the company.

Recently, Monster has had some tension with Coca-Cola, as it goes to arbitration over whether Coke's plans for new energy drink offerings violate the terms of an agreement between the two companies.

That's not the only competition knocking on the door.

Wells Fargo recently published survey results that show Red Bull gaining market share, Bang drinks picking up steam, and, most importantly, that retail growth is trending toward 4.5%. That compares to prior expectations for a 6.3% increase.

Monster scores an "F" in the FAST model for expectations, which suggests Wall Street hasn't reflected this new reality into their consensus numbers.

Overall earnings quality and shareholder yield score failing grades as well.

So, if expectations do come down, which likely means lower stock prices, the company isn't rewarding shareholders first, which might provide a floor to the stock.

As a result, an already weakening stock could get much weaker.

NVIDIA (Nasdaq: NVDA) shares have already been demolished.

After hitting nearly $290 in October 2018, they were around $130 by Christmas Eve. Not exactly the present shareholders were wanting for the holiday. Instead, they got a lump of coal.

Despite the beating the company took in the fourth quarter, its FAST scores are "Fs" across the board. As a result, the bottom might not be in yet.

One of the biggest problems facing the company is pricing power. Pricing power as in they have little of it.

Prices for the company's graphics processing units are plummeting. Price cuts of 25% to 50% in 2018 for certain products have been the order of the day.

Despite the pricing pressure, the company trades at a premium to its peers relative to sales. If profit margins come under pressure from weak pricing, it will be a challenge to justify the valuation premium. As a result, lower stock prices could be ahead.

And last, but not least we have **Alphabet (Nasdaq: GOOGL)**.

Its Google platform is the world's dominant search and online advertising engine… and that has led to boatloads of cash flow.

However, that cash flow hasn't translated into much of a second act.

Remember Google Glass?

There are the cloud and hardware businesses, but many other players are in those, too.

Why would Google command premium profit margins in such a competitive space? The FAST letter grade for Expectations is an "F," meaning Wall Street is too bullish on the prospects for these smaller business units.

One disturbing trend sticks out like a sore thumb in the company's numbers. It's CAPFLOW, which is the amount of capital expenditures relative to its cash flow is soaring.

Historically this number has been less than half of what it is today. That means more and more is being invested to maintain cash flow with no apparent payoff.

It could be an indication that the company is struggling to find its footing in other market to support the business for a maturing search market.

	2010	2011	2012	2013	2014	2015	2016	2017	2018	TTM
CAPFLOW	41%	30%	24%	44%	58%	46%	40%	67%	63%	60%

Uncovering the Clunkers

So, there you have it. I've highlighted a handful of stocks that could prove to be troublesome going into 2020.

These clunkers have the potential to do some real damage to your portfolio. And chances are you own at least one of them, if not more.

Consider my suggestion on how to manage these clunkers: short them, sell them, carefully watch them, or do nothing about them. Each option is not without its own risk.

How do you find alternatives for these troubled stocks?

In *Hidden Fortunes*, I go above and beyond to spot the hidden gems that'll prosper, even in the economic turmoil that lies ahead. And I continue to share my findings on which new, or old, stocks have slipped into the precarious territory of the clunkers.

Curious for more? Check out my back issues of *Hidden Fortunes* on dentresearch.com using your new login credentials and look for the next monthly issues hitting your inbox soon to join me on quest to uncover the gems of the market.

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