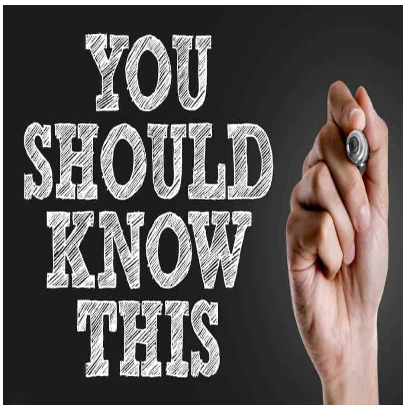

Tech Stock Selloff: Here’s What’s Really Going on

Description

Tech stocks have been weak lately, with the NASDAQ having declined 10% since February 9. While 2021 has seen stocks rise slightly overall, some tech stocks are in bear mode.

For most investors, this is just a slightly turbulent market. It’s not really a big deal. But for investors who’ve tied their fortunes entirely to “hype” stocks with extreme valuations, this has been a steeper correction than March 2020. **Tesla** has declined 36% from its top, and other popular tech stocks (**Palantir**, **Square**) are in a similar boat. Not all tech stocks have posted huge losses, but some of the more overhyped ones have. In this article, I’ll attempt to explain what’s going on — and what you can do to protect yourself from a pullback.

Sector rotation into value stocks

The biggest single reason why tech stocks are declining right now is because investors are “sector rotating” into value stocks. Sector rotation is a strategy where you move from one sector to another in hopes of profiting from the right stocks at the right time. For the past year, tech was the sector to be in. Many tech stocks not only survived but thrived in amid the COVID-19 pandemic, growing their earnings faster than in previous years. **Shopify** (TSX:SHOP)(NYSE:SHOP) would be the classic example here. Before COVID hit, it was growing its revenue at 45% year over year. After the pandemic hit, it averaged more than 90%. The pandemic-driven surge in online shopping treated that company well. But when the economy re-opens, it could all come to an end.

This is why many investors are now moving into value stocks. Beaten-down sectors like energy and banks are just now starting to recover. **TD Bank**, for example, just recently posted a strong quarter, with earnings up 10%. As a result, it set a record high. Even **Air Canada** has been rallying, despite its continued billion-dollar losses. Basically, investors expect these companies to come surging back to life when the pandemic ends. And they’re hoping to get in before the recovery becomes obvious — and everybody else has the same idea.

Expected deceleration

Related to the first factor is expected revenue growth deceleration in tech.

As previously mentioned, many top tech stocks actually *gained* because of the pandemic. With retail stores closed, people had nowhere to shop but online. E-commerce stocks profited immensely. But when the pandemic ends, that party is over. So now, top tech companies are expecting growth to slow.

Shopify, for example, recently told its investors to expect deceleration. **Facebook's** CFO said the same thing. It's not exactly clear when or by how much tech revenue growth is going to slow down. But these companies' own insiders are saying it will happen.

Foolish takeaway

The correction we're seeing now in certain segments of the tech industry was bound to happen. After the COVID-19 market crash, tech companies put out earnings numbers that made them look like "safe havens" amid all the volatility. Logically, investors jumped in. But eventually, tech stocks reached stratospheric valuations. In some cases, their shares went up a lot more than earnings did. Now, it's beginning to look like COVID is on its way out. So, the main catalyst tech stocks had profited from may disappear. As a result, smart money is going all in on value.

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andrewbutton