INVESTORPLACE

# THE SILICON VALLEY SUPERCYCLE

*Your Secret Playbook for Making a Fortune in Technology Stocks*

BRIAN HUNT
CEO, INVESTORPLACE

On January 9, 2007, the legendary Steve Jobs took the stage at a San Francisco technology conference and delivered one of the most important corporate presentations in U.S. history.

The Apple CEO told the audience, "Every once in a while, a revolutionary product comes along and changes everything."

Jobs explained how Apple's new product was part revolutionary new mobile phone, part breakthrough communications device, and part music player with touch-screen interface. Jobs called this 3-in-1 product the "iPhone."

You know the rest of the story. The iPhone went on to become one of the most popular consumer products in history. It fundamentally changed the way people live. Apple has sold more than 1 billion iPhones since Jobs' presentation. The iPhone played the primary role in Apple becoming the world's largest, most valuable company.

Jobs made good on his promise. The iPhone changed everything.

Of course, Apple shareholders made fortunes along with way. The day before Jobs' iPhone presentation, Apple stock traded at $12.21 per share. Twelve years later, Apple stock traded at $195 share, a 16-fold increase.

The enormous cash flows Apple started generating allowed it to pay shareholders dividends as well. By 2018, shareholders who bought Apple in 2007 were earning a 20% yield on their investments.

In a world of low interest rates and low dividend yields, earning a safe 20% yield on your money with one of the world's best companies is extraordinary.

This story – and hundreds of others like it – shows the incredible wealth-creation power of technological innovation. No other kind of business can create great wealth in a short time like a technology business.

Just consider these tech companies, their innovations, and the returns made by early shareholders:

- Microsoft, computer software: Early investors made more than 100,000%.
- Cisco Systems, internet infrastructure: Early investors made more than 30,000%.
- Amazon.com, online retailer: Early investors made more than 70,000%.

And the list goes on… and on… and on.

Most folks know that successful tech companies like Microsoft and Apple have made their shareholders a lot of money. But what most people ***don't*** know is that there's a secret playbook the world's best investors follow to consistently make these huge profits from technological innovations and the stock prices they send soaring.

You can think of this playbook as a mental framework… a unique way of thinking about the business world that maybe one American in 100,000 is aware of.

Because this way of seeing the business world is so powerful – and because so few people are aware of it – your knowledge of it will give you ***an enormous advantage over others in life***.

When it comes to your ability to create wealth, this framework will allow you to become a giant among men.

These are bold claims, I know. In this guide, I'll make good on them and more.

Below is ***The Secret Playbook for Making a Fortune in the World's Most Powerful Stocks***

## The Financial Engine That Can Make You a Millionaire in a Hurry

Over the past 20 years, a new kind of aristocracy has taken power in the United States.

Members of this aristocracy make more money in one month than most people make in a lifetime. They don't wait in line at airports. They travel the country in private jets and helicopters. Thanks to their private chefs, personal trainers, housekeepers, nannies, and personal assistants, they typically do whatever they feel like doing. Because of their wealth, this group has incredible political influence. They can literally rewrite laws.

This new aristocracy consists of the founders, executives, and investors behind the world's top technology companies. Members of this exclusive club are the people behind businesses like Apple, Facebook, Amazon, Google, Twitter, Uber, and Netflix.

The highest-level members of this new aristocracy are worth tens of billions of dollars. Even a member on the lower rung can make over $2 million a year. Most of them work in or near California's famous Silicon Valley.

Members of this upper class not only amass huge wealth, but they do it quickly. The new Silicon Valley aristocracy is full of twenty- and thirtysomethings worth hundreds of millions of dollars.

One month, a tech-smart college dropout is living with his parents and driving a used Hyundai. The next month, he's worth $50 million and driving one of his three Ferraris.

The driver of all this new wealth?

**Scalability.**

The word ***scalability*** is repeated over and over in Silicon Valley for good reason.

A business **must** have scalability in order to grow large in a short time (that is, "***Make you a ton of money quickly***").

Scalability is the ability of a business to massively grow revenues while minimally growing the costs associated with producing those revenues.

For example, a lawn-mowing business is not scalable. If you own a lawn-mowing business and want to double in size, you'll have to buy twice as many lawn mowers as you have now, and you'll have to hire twice as many lawn-mower operators as you have now. Because of this, your revenue cannot soar far beyond your costs.

On the other side of the spectrum, you have social media businesses like Facebook and Twitter. These businesses are very scalable.

It took a lot of work in the early days to create the technologies and businesses behind Facebook and Twitter. But once they were created, these two businesses could add new users and increase their advertising revenues much faster than they increased costs. Their market values exploded higher as a result.

They grew to huge sizes faster than just about any other kind of businesses in U.S. history.

Software companies are very scalable as well. A company like Microsoft must spend money and time creating and developing software like Office. But once the product is created, Microsoft can produce and sell additional copies of the software at minimal cost… so the company's sales can rise much faster than costs.

Don't get me wrong: Owners of non-scalable businesses (like a lawn-mowing business) can grow wealthy. Many people have done so in the past. Many people will do so in the future.

But if your goal as an investor is to own businesses that can make you a lot of money quickly, then you must focus your attention and capital on **scalable** technology businesses.

Thanks to the huge increase in communications bandwidth over the past 20 years, technology companies are scaling – and creating stunning amounts of wealth for shareholders – faster than ever before.

This is thanks to the "network effect."

## How the Network Effect Works

The "network effect" is one of the most powerful wealth-creation forces on the planet.

The network effect occurs when each new user of a service or product increases the value of that service or product.

Take the telephone…

In its very early stages, the telephone wasn't a hugely valuable invention.

That's because only a few people had telephones.

If you had an early version of the telephone, you couldn't talk to many other people.

After all… they didn't have telephones!

However, once more and more people saw the value in telephones, they started buying more of them.

After a while, you could talk to dozens of people who had telephones instead of just two or three people with telephones.

What followed was a virtuous, self-reinforcing cycle.

The more people who had telephones, the more valuable the telephone network became.

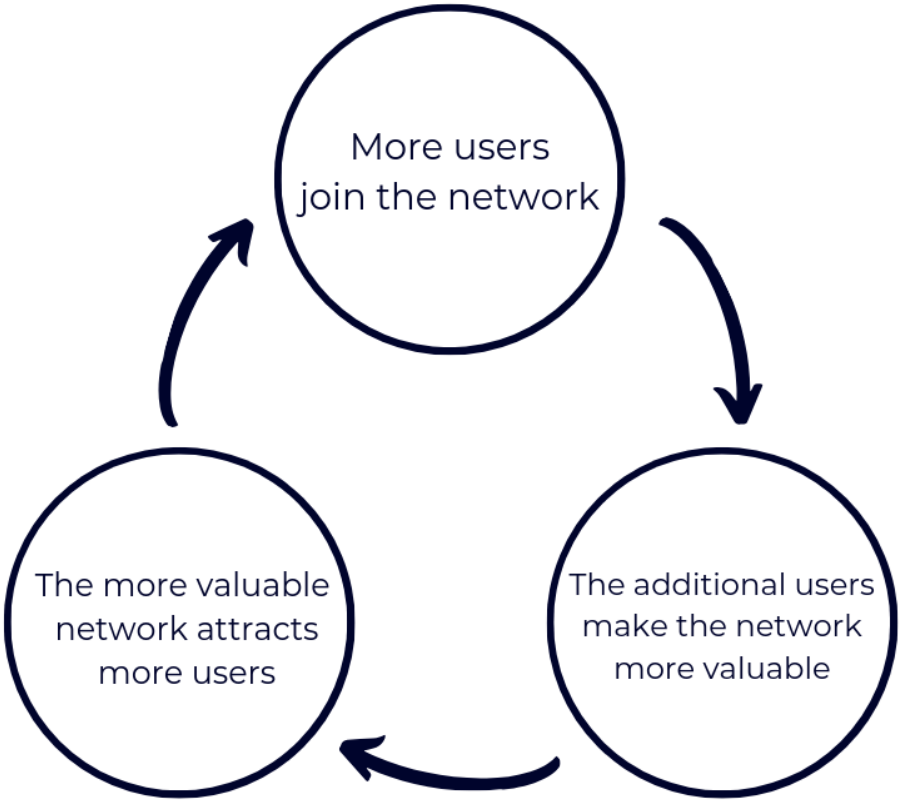
The more valuable the telephone network became, the more people bought telephones.

As even more people bought telephones, the telephone network became even more valuable…

And so on.

This kind of virtuous, self-reinforcing cycle is called a "positive feedback loop."

Here's what it looks like:




For another look at the network effect, let's turn to one of the biggest business success stories of our time: Google.

In the early 2000s, Google founders Sergey Brin and Larry Page developed the most efficient way of searching the internet. Their service was far better than other early search engines.

As a result, lots of people wanted to use Google's search engine.

The more users Google attracted, the more people wanted to ensure their website was listed with Google.

The more people that had their website listed on Google, the better Google's search results got.

The better Google's search results got, the more users Google attracted.

In addition to serving internet searchers, Google also developed a way to deliver targeted advertising.

For example, a person searching for vacation ideas was served with travel-related advertising.

The more people visited Google, the more advertisers wanted to advertise on Google.

The more advertisers Google had, the more targeted the advertisements became… which attracted even more users.

Google created a virtuous, self-reinforcing cycle that exploited the network effect to the tune of creating a company worth more than $700 billion. Sergey Brin and Larry Page became two of the world's richest people.

Scalable technology and the network effect are the forces behind nearly all of the mega-successful technology winners of the past 20 years.

***Microsoft, which has generated 100,000% shareholder gains since its IPO, leveraged the network effect in a stunning fashion.

As more people used Microsoft programs like Word and Excel, more people wanted to use them to be compatible with friends and colleagues.

***Uber, which went public in 2019 at a giant $82 billion valuation, is another great case study in the network effect.

The more users Uber attracted, the more drivers it attracted. The more drivers Uber attracted, the better it could serve customers. The better Uber served customers, the more customers it attracted.

This created a virtuous, self-reinforcing cycle that made its pre-IPO shareholders obscenely rich. Tech investor Chris Sacca turned a $300,000 investment into more than $1 billion with Uber.

***Or, take Facebook.

With every new user, Facebook became more valuable as a business.

As its social network's value increased, its new sign-ups increased. Millions upon millions of people signed up for Facebook because millions upon millions of other people were signing up for Facebook.

Facebook became popular because it was popular… and leveraged the network effect.

Early shareholders made more than 1,000 times their money.

***Amazon is another grand case study of the network effect creating stunning wealth in a short time.

As Amazon linked product sellers to product buyers, the usefulness of its online marketplace grew. As the value of the marketplace grew, more product sellers wanted in on it.

This drew in more consumers… which drew in more sellers… and so on.

The power of the network effect sent Amazon shares up more than 97,000% from its IPO and made founder Jeff Bezos the world's richest man.

By now, you can see the golden thread here. You can see how scalable technology businesses that leverage the network effect can make their shareholders rich in relatively short time frames.

But be warned: Investing in these businesses the wrong way is a recipe for financial disaster. To make giant returns without taking giant risks, you must know the secret playbook for investing in scalable technology businesses.

This playbook will allow you to invest in these businesses at precisely the right times… while also avoiding the pitfall of investing in them at precisely the wrong times.

The power of this concept – not investing at the wrong time – cannot be overstated. As you're about to learn, ***you can lose big money in the greatest, most world-changing technologies if you invest in them at the wrong time.***

Below, you'll find our framework – our playbook – for making big money in the world's most powerful stocks.

In it, I show you how each and every revolutionary technology goes through a six-phase "lifecycle." But more than that, I'll show investors like you two strategies to hit that lifecycle at the most opportune times.

## A Revolutionary Technology and Its Six Phases of Stock Market Life

Think of all the amazing innovations of the past 120 years: automobiles… airplanes… radio… television…. computers… the internet… mobile phones…

These innovations changed the world and made many people very wealthy.

Most people don't realize it, but investments in these innovative new industries followed a predictable "lifecycle" that – when timed properly – made investors massive returns with minimal risks.

And I'm confident in saying that investments in every innovation you're hearing about now – or will hear about in the future – ***will follow the same predictable lifecycle.***

Some phases of this lifecycle are terrible for stock market investors in terms of risk vs. reward.

Some phases of this lifecycle are incredible for stock market investors in terms of risk vs. reward.

If you know how these phases work and what to do during each phase, there's no reason you can't make giant returns in technology stocks without taking giant risks.

Here are the six phases of a revolutionary technology's investment lifecycle…

## Phase 1: The Science Project

During the 1980s and '90s, the home computer went from being a rarity to being a common feature in American homes.

During the personal computer boom, investors in top computer maker Dell made more than 80,000%. Investors in top computer software maker Microsoft made over 9,000%.

But decades before computers made their way into American homes and made investors

tons of money, many computers were in use at government research facilities, large corporations, and universities.

In other words, tech-smart people knew for years that personal computers would likely become a big thing in America. But the technology itself was so new, so expensive to produce, and so cutting edge that it was more "science project" than "investment opportunity."

You see this situation play out all the time. Reports of a new technology hit science journals, industry conferences, and even some mainstream media outlets. People get excited about the technology's potential.

However, the technology is in such an early phase that it's at least a decade from widespread use… and a least a decade from offering great investment opportunity.

For example, early computers in the 1950s and '60s were the size of entire rooms and cost millions of dollars.

There's no way those early computers could have caught on with a broad audience and generated tens of billions of dollars in revenue for computer makers. It was much too early in the game.

Or, moving forward a few decades, consider one very promising, very "hot" technology that was all over the mainstream press in 2017: virtual reality.

Virtual reality is the name for technology that can immerse you into amazing new worlds from the comfort of your living room sofa. After putting on special goggles or a special headset, you experience a computer simulation that essentially tricks your brain into thinking

it's really in a different world, like time traveling in ancient Egypt… or flying by Saturn in a spaceship… or attending a Harvard lecture… or living the life of a famous rock star.

Sounds cool, right? It's no wonder virtual reality appeared a lot in the press in 2017.

But virtual reality also appeared in the mainstream press back in the 1980s… the 1990s… and the 2000s.

Virtual reality excited entrepreneurs and investors for decades. But good virtual reality products didn't start hitting the shelves of American stores until 2016 and 2017.

Virtual reality sounded really cool in 1990… and some great aspects of the technology existed back then… but the "whole package" simply didn't exist.

It was still in **The Science Project** phase.

The unfortunate reality for technology enthusiasts and investors is that it often takes decades for a promising innovation to go from the discovery and development stage to the "mass adoption" stage.

Mass adoption is when a device or product is fast enough, good enough, small enough, and cheap enough to be both desirable ***and*** in the price range of most consumers – when it's ***scalable***. This is the stage where the product can generate billions of dollars in sales and send stock prices soaring (we'll cover this phenomenon in a moment).

In this earliest phase of a revolutionary technology's lifecycle, it is very hard for stock market investors to make money in it. There will be very few or zero public companies that represent "pure plays" on the technology. They'll hardly exist.

Most of the innovation happens at small, private companies (often funded by venture capitalists) or in the research facilities of larger companies. And much of the money poured into discovering and developing the innovation at this stage takes a decade or more to pay off. A good portion of it never pays off at all.

The payoffs start to happen in Phase 2…

## Phase 2: The First Boom

Once investors and businesses have invested many years and huge amounts of money (which runs into the billions of dollars these days) into an innovation, it is ready for the next stage.

During **The First Boom**, the innovation moves out of laboratories and beyond clunky prototypes… and actually finds buyers in the form of early adopters. Early adopters are individuals and corporations who don't mind spending money and taking a risk on new, potentially revolutionary technologies.

For example, the internet really took America by storm from 1996 to 2001. This is when adoption soared from about 10% of American adults using the internet to more than half of American of adults using the web.

However, early adopters were using the internet in the early '90s, years before it caught on with most people.

During this **First Boom** phase, the innovation is still in its early stages. It is a shadow of its future self and it will cost much more than its future self. It generates a fraction of the sales it will generate in the future.

Remember, it's mostly just early adopters who are buying and using it. Back in 1992, internet speeds were very slow, and even that slow access was expensive.

However, in the stock market, early, real-life applications – a modest batch of early sales – is all that's needed to trigger massive stock rallies.

For example, internet use in America didn't really take off until 1995-'96. But years before that, pure-play internet companies staged huge share-price rallies. This is because early investors spotted the technology's enormous potential, noticed it was starting to generate revenue, and piled into the shares.

Take the case of Cisco, one of the leading makers of the "plumbing" the internet needs to exist and function (modems, switches, routers, etc.). Although the web wasn't being adopted by the masses from 1992 to 1995, Cisco shares during that stretch soared by ninefold.


The stock prices of tech companies tend to soar before the technology itself is adopted by the masses and generates billions in sales because the stock market often acts as a "discounting mechanism."

That is, the stock market tends to look into the future. A given day's stock prices are not based on what is happening on that day. ***A given day's stock prices are based on what the market expects to happen in the future***.

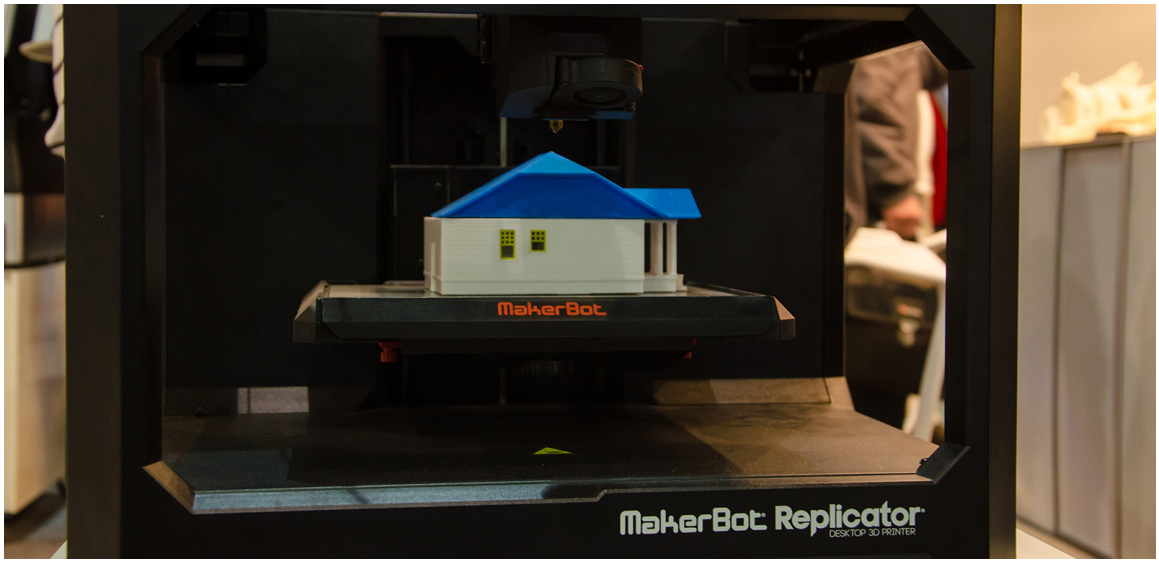
Said another way, future expectations for companies get "baked in" to current prices.

Although some pure-play tech stocks will be soaring during this stage, the innovation will not be on the radar of most retail investors. It will not be on the radar of most professional investors either. It's not going to be constantly covered by mainstream newspapers and TV networks.

Instead, the pure-play stocks on the innovation will be in a "stealth" bull market… where only the most informed, most "ahead of the curve" investors make money. These stealth bull markets can be outrageously profitable for early investors.

We already saw how Cisco soared before most folks ever set up an email account. Another example is the story of 3D printing from 2010 to 2014.

3D printing – also called "additive manufacturing" – is the process of printing physical objects from three-dimensional models, usually by machines that "print" many thin layers of material in succession. A 3D printer can "print" toys, tools, machine parts, furniture, and hundreds of other things.

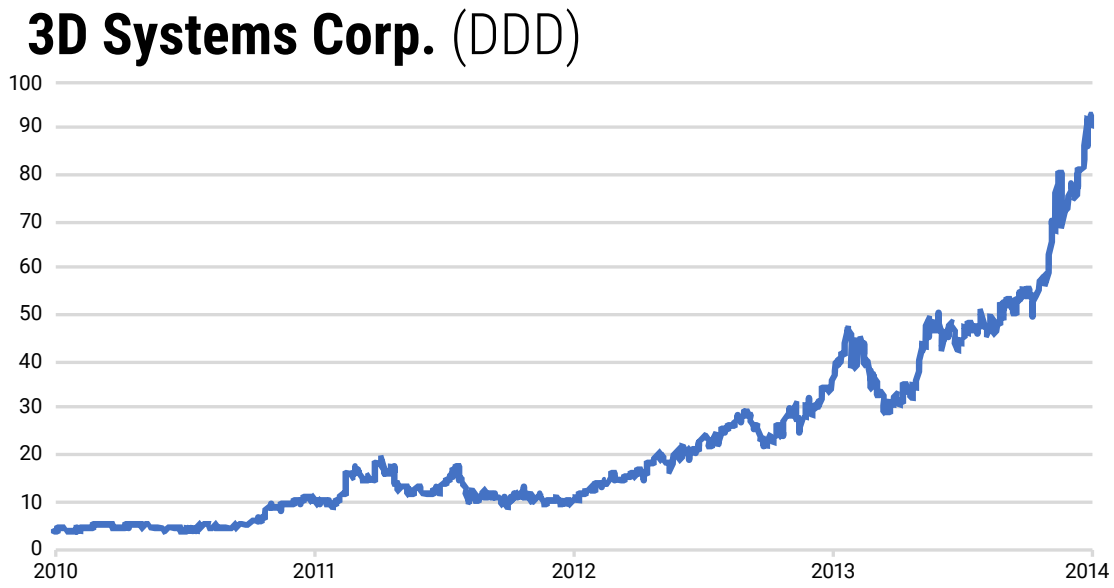



The promise of 3D printing is incredible. Instead of a world where most manufacturing is done in mega factories far away from where finished products are used, we could have a world of “decentralized” manufacturing.

Need a new part for your car? Just download the part’s specifications and quickly make it with the 3D printer in your garage.

**The First Boom** phase of 3D printing occurred from 2010 to 2014. During this four-year span, shares of the top 3D printing firm, 3D Systems, skyrocketed from $3.88 per share to about $93 per share.

That’s a stunning 24-fold increase.

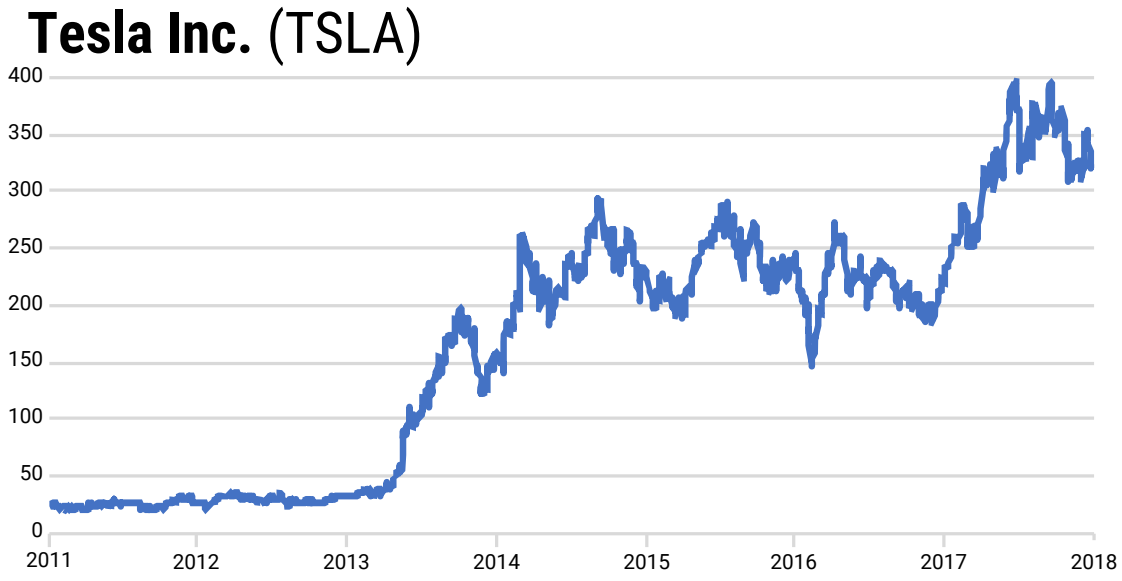


Or, take the story of modern electric vehicles.

Most people don't know this, but electric cars have been around for over 100 years. Some of the world's first cars ran on electricity. However, gasoline-powered cars eventually proved to be the best mass-market option.

But starting around 2012, investors began to take note of what inventor Elon Musk was doing with electric cars at Tesla.

Driven by modest sales to early adopters and the promise of clean, carbon-free electric cars, investors went wild for Tesla shares and fueled a giant Phase 2 rally. During this rally, Tesla's stock climbed from $25 per share to $290 per share in less than three years (an 11-fold increase).



Like any big stock rally, a Phase 2 stock rally does not go up in straight line. There are short-term corrections along the way. This is just the natural ebb and flow of the stock market. **The First Boom** is marked by a trend of rallies being larger and longer than the short-term declines.

Of course, a great innovation, a great story, and skyrocketing stocks can't stay secret forever.

A big Phase 2 stock rally can last three years or more. During the final part of **The First Boom**, the innovation will attract more buyers beyond just the early adopters.

More mainstream media outlets will run features on the innovation and all the money being made by early investors. More people will catch onto the story and buy shares in the innovative companies. The stealth bull market will start becoming an audible, visible bull market.

The final part of Phase 2 is when this audible, visible bull market becomes a noisy, rambunctious bull market.

Identifying the point at which the middle of Phase 2 transitions to the end of Phase 2 is more art than science.

But in a nutshell, the end of Phase 2 is when people go wild for the story, develop insane future expectations, and bid the stocks to unreasonably expensive levels.

This sets the stage for disappointment and plummeting stocks.

The end of Phase 2 has several hallmarks. The innovation will start appearing frequently in the mainstream media. Stocks in the sector will advance by large amounts very quickly. During this phase, it's not uncommon to see stocks advance by 50% or 100% in just a few months

Additionally, the sector will begin to draw investment from people who normally never buy stocks. You will see investment "gurus" make aggressive predictions about how stocks related to the innovation will go to the moon. You will see the creation of investment funds and newsletters dedicated to the innovation.

The number of privately held startups in the industry going public will surge. This is because companies want to cash in on all the investor interest in the sector and raise money.

Another hallmark of this phase is the appearance of "momentum" investors. These people don't try to buy low and sell high. ***They try to buy high and sell higher.***

Whether they consciously acknowledge it or not, many people buy stocks for the simple reason that they are going up… and they don't want to "miss out" on the big profits being made in a very exciting sector.

In other words, at the end of Phase 2, you see a tremendous amount of optimism toward the innovation. That leads to a tremendous amount of capital flowing into the industry.

The optimism creates a self-reinforcing cycle that feeds on itself. Rising prices draw in capital… which causes stock prices to rise even more… which draws in more capital… which causes stock prices to rise even more…

And so on.

You could say the industry and its stocks become popular because they're popular.

Eventually, all this investor interest bids stock prices to insane levels.

During **The First Boom**, stocks will become overvalued in every sense of the word. If the companies in the sector produce earnings, they will begin to trade for 50… 100… even 200 times earnings (instead of more reasonable multiples of earnings like 15 or 20).

If the companies in the sector do not make money, they will begin to trade for insane multiples of sales, like 20 or 30 times sales.

Greedy investors dazzled by the story will justify the insane valuations by saying "it's a new paradigm" and "this time it's different."

During this time of wild enthusiasm, some critics will point how the stocks are very expensive and, therefore, dangerous.

Supporters of the trend will say the critics "just don't get it." They'll call the critics "old fashioned" and "stuck in the past."

While all these things are happening in the capital markets, the technology itself will be rapidly advancing. The huge capital flows will allow companies to invest billions in newer and better versions of the technology.

The companies will not be pressured by their investors to turn a profit. The investors will be chiefly interested in headline-making new advances… so headline-making advances will be made.

However, no matter how great they are, no company and no technology can live up to insane, unrealistic expectations.

Phase 3 is when those expectations are dashed.

## Phase 3: The First Crash

In the stock market, you have **reality** – how much revenue and profit a company generates – and you have **expectations** – how much revenue and profit people expect the company to generate in the future.

During Phase 2 of a revolutionary technology's lifecycle, **reality** and **expectations** diverge massively.

Phase 3 is when reality exerts itself and throws a lake full of ice-cold water on expectations.

Did you ever watch the Wile E. Coyote and Road Runner cartoon?

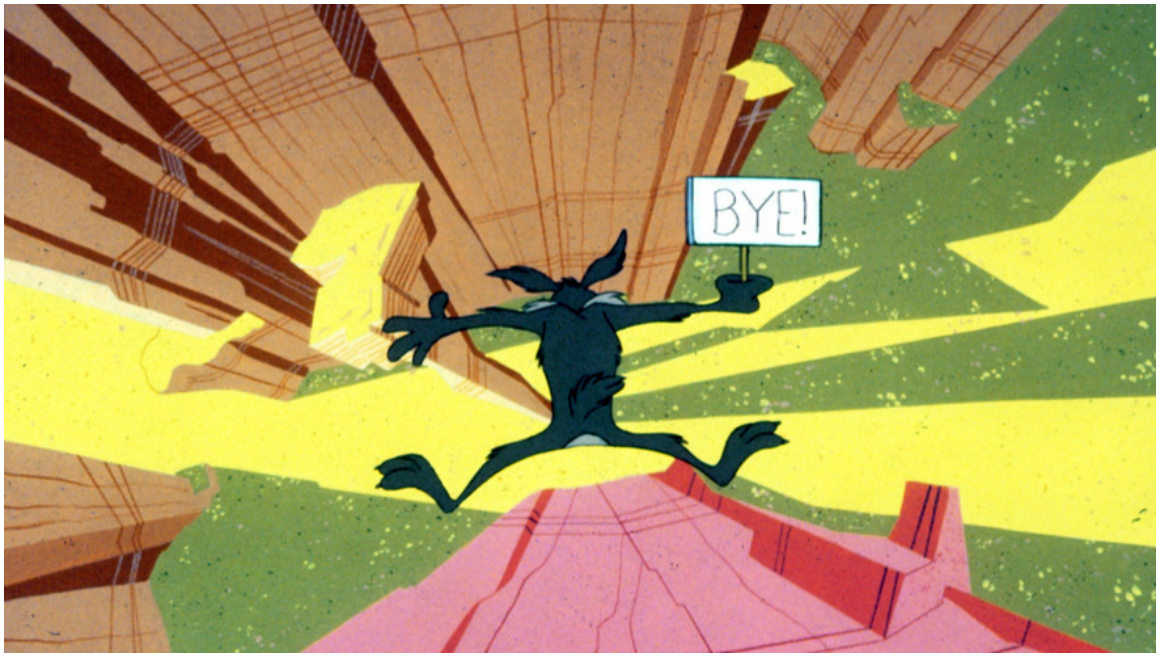
Even if you didn't, you might be familiar with the cartoon's iconic chase scenes. Wile E. Coyote chases the Road Runner. The Road Runner comes to an abrupt stop. Wile E. Coyote continues running… and doesn't realize he has run off a cliff. Eventually, reality asserts itself – and Wile E. Coyote plummets to the ground.

Warner Bros

During this part of Phase 3, business reality (sales, profits, cash in the bank, etc.) is the ground on which Wile E. Coyote is running.

The stock market's expectations are Wile E. Coyote himself.

Eventually, the market's expectations overshoot reality. Stock market valuations exceed what is merited by what is happening in real life. The stocks become like Wile E. Coyote… gravity exerts itself… and the stocks plummet to Earth.




Warner Bros

That's why we call this phase **The First Crash**.

The 1999–2000 internet mania is without a doubt the best example of Phase 3 craziness in modern times. All the hallmarks were there.

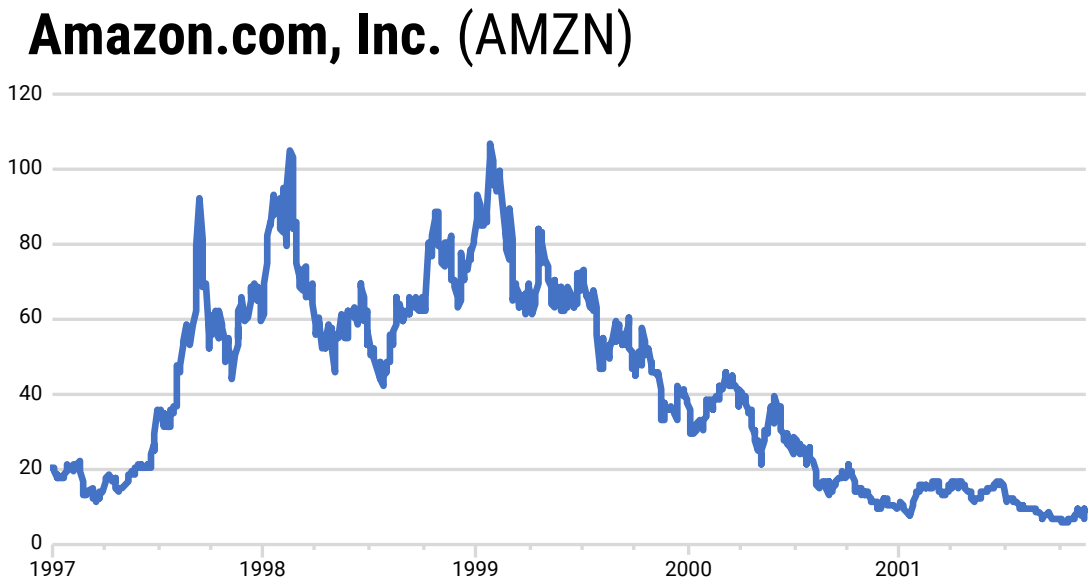
The internet boom was all over the mainstream press. Stocks soared 50%–100% in just months. New investment funds dedicated to the sector sprung up like mushrooms after a rainstorm. Initial public offerings in the space soared. People who normally didn't buy stocks put their life savings into internet stocks. Self-appointed experts predicted boom times for years. Valuations climbed to insane levels.

Then, reality set in.

During the Phase 2 mania, Cisco shares soared more than 700% in just over two years.

Then, in Phase 3, they plummeted.


Amazon shares soared more than 1,300% in just over two years… then plummeted.



I just told you about the boom investors in 3D Systems enjoyed from 2010 to 2014. The stock climbed 24-fold during the boom. People went wild for the 3D printing industry and developed insane expectations for the technology.

As you can see from the chart below, the boom turned to bust. 3D Systems fell more than 90% in a few years.

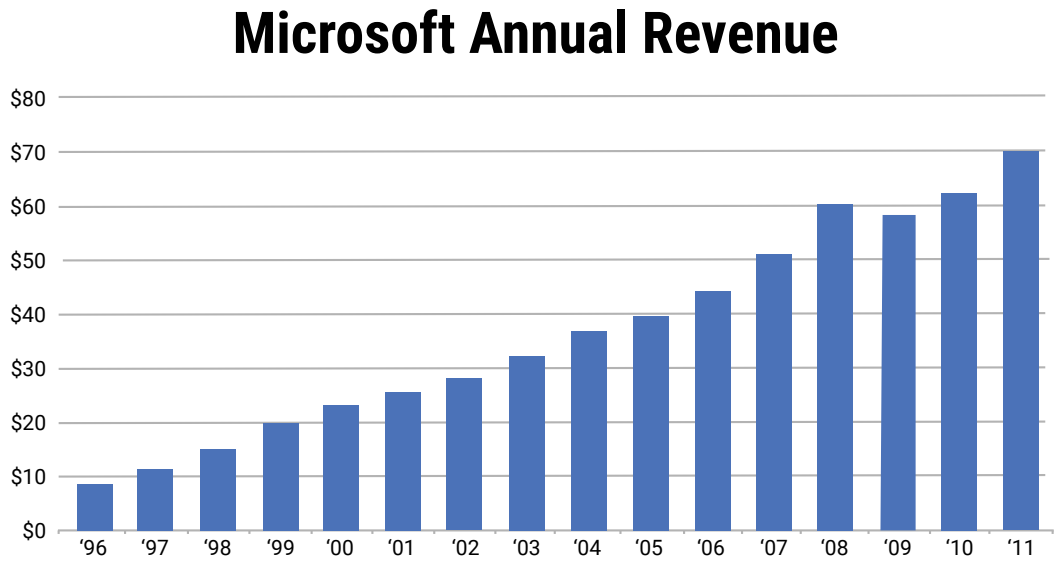

However, it's important to remember that during the wild mania and ensuing bust, technological progress continues at a rapid pace.

Granted, **The First Crash** will deprive a company of the huge investment flows it enjoyed during **The First Boom**. But if the underlying technology is truly useful to humanity, technological advancement will continue even in an environment of reduced capital flows.

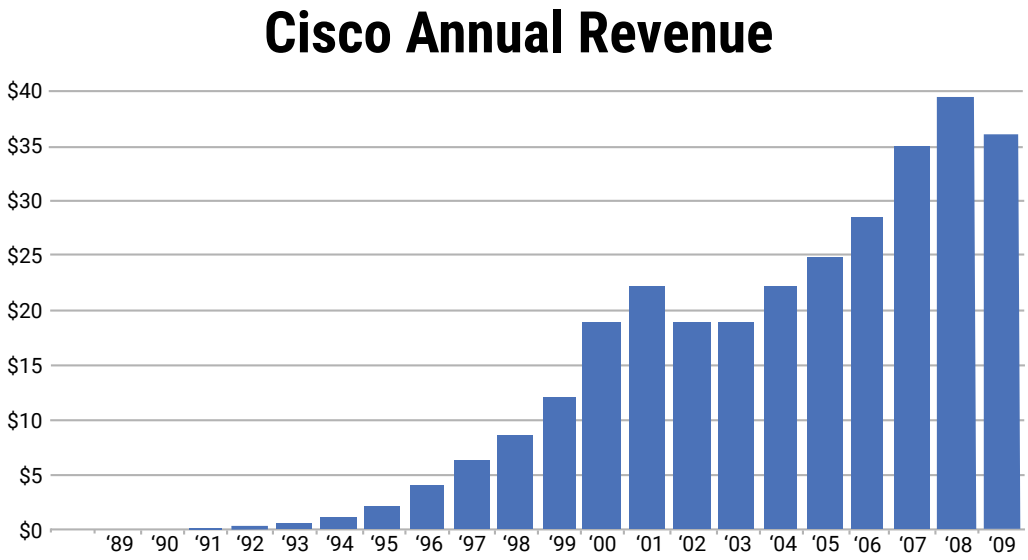
Also, tech companies can still ring up steady or even increasing sales during Phase 3.

For example, although Microsoft's stock was hammered during the 2000–'02 bear market, sales of its software products continued to climb.

The chart below shows Microsoft's revenue growth from 1996 through 2006. Although Microsoft's share price fell more than 60% during the tech crash, its revenue kept going up.




Or, consider internet "plumbing" maker Cisco. Although its share price dropped more than 85% from 2000 to 2003, Cisco's sales remained relatively steady during those years. The chart below shows Cisco's revenue by year from 1996 through 2006.




This kind of healthy business growth isn't much consolation to investors.

Their focus will be on a stock they purchased for $50 per share go down to $40 per share… then $30 per share… then $20 per share…

And then we go into Phase 4…

## Phase 4: The Hangover

Phase 4 is the unpleasant period that follows **The First Crash**.

Remember, Phase 2 is defined by investors bidding stocks up to absurd valuations, which creates the conditions for a crash in Phase 3. It's not uncommon for companies to fall 50%, 60%, even 75%+ in these post-boom crashes.

The declines can be so large because the previous excesses can be so large. If a stock selling for 100 times earnings falls 50%, it is still trading for an expensive 50 times earnings.

After taking such a shot to the gut, the stocks in a sector need time to recover. Many people who invested in the sector will be so traumatized and so disappointed with the stocks that they will swear off the sector forever.

Take, for example, someone who invests $50,000 into a sector only to watch the value of that investment decline to just $10,000. ***That's $40,000 up in smoke***.

It's a tall order to ask them to ever come back to the sector. Think of it this way: Would you go back to a crazy significant other who intentionally lit your house on fire?

**The Hangover** can last for years.

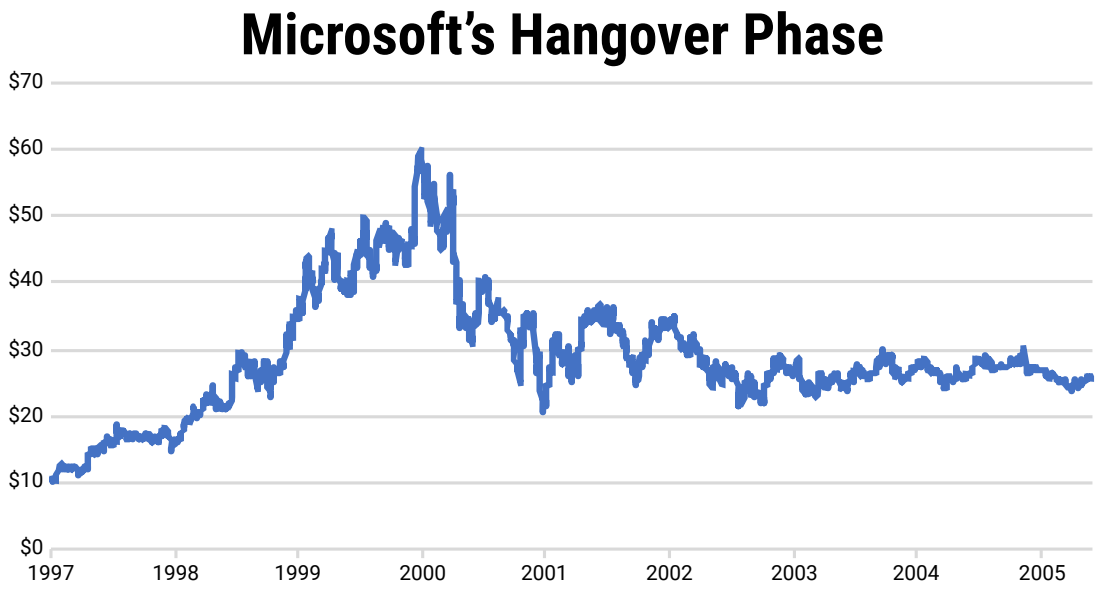
From an investment perspective, the hallmark of Phase 4 is a grinding, demoralizing period of sideways-to-down stock price movement. Every rally with the potential to excite investors is met with overwhelming selling pressure. The financial media runs stories that claim "the party's over."

These media stories typically sound so gloomy that the average reader will think, ***"What a horrible situation. What a horrible industry to invest in. I'll make sure to always avoid it."***

**The Hangover** can last for years.

To get an idea of what it looks like, see the chart below. It displays the price action of Microsoft from 1997 to 2004. The party was fun up until 2000 (**The First Boom**). Then came **The First Crash**.

And then came **The Hangover** – years of disappointing stock price action.




Despite rough times for stock prices, technological progress continues to advance during Phase 4, just as it does during every phase of the investment lifecycle.

In the discussion of Phase 3, I noted that although a tech sector's bear market will deprive it of the huge investment flows it enjoyed during its Phase 2 boom, if the underlying technology is truly useful to humanity, advancement will continue. That goes for Phase 4 as well.

In fact, at this point in a technology's lifecycle, it will be close to or entering "mass adoption" phase.

Remember, mass adoption is when a product or service is scalable – when it's fast enough, good enough, small enough, and cheap enough to be both desirable ***and*** in the price range of most consumers. Think the internet in the mid- to late 1990s.

The mass-adoption stage is where the product or service can generate billions of dollars in sales. Put differently, ***this is when the technology can change the world.***

However, good luck explaining all that to most investors.

We humans like to hold grudges… even against stocks. It can take years for people to warm back up to a sector that has erased so much wealth and caused so much pain.

It's also worth noting that an environment of investor disgust and reduced capital flows will accelerate the emergence of a sector's strong players and weak players.

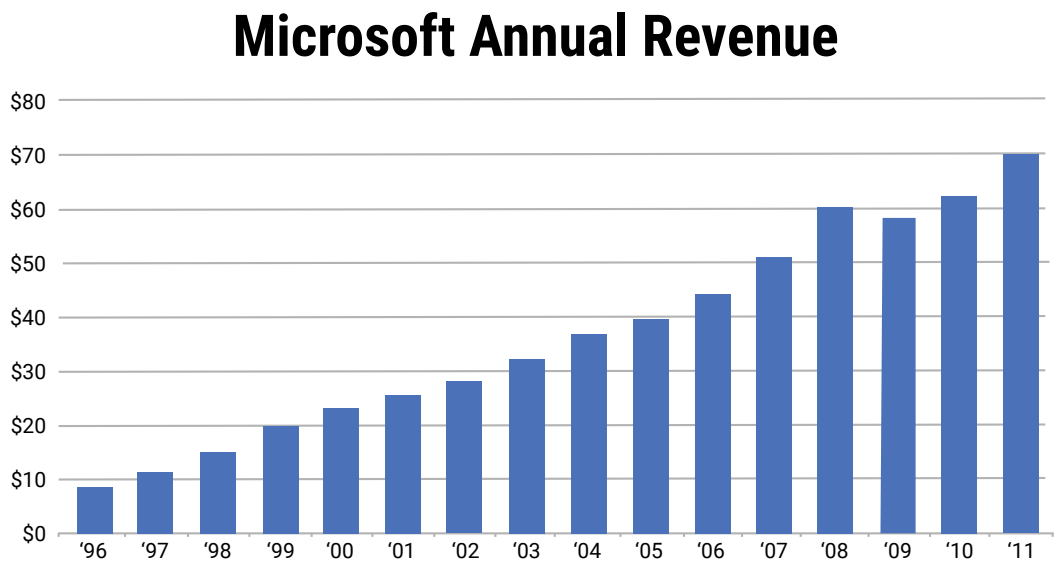
During Phase 2, enthusiastic investors will embrace almost any company and throw money at it. Companies with weak technology and weak business models can survive for years.

That's not the case during **The Hangover**.

During this phase of investor disgust and reduced capital flows, only the companies with the best technologies and best business models survive and thrive. They will buy up competitors or drive them out of business. They will reach more and more customers. They will continue to invest in research and development, which will allow them to create better versions of the product or service.

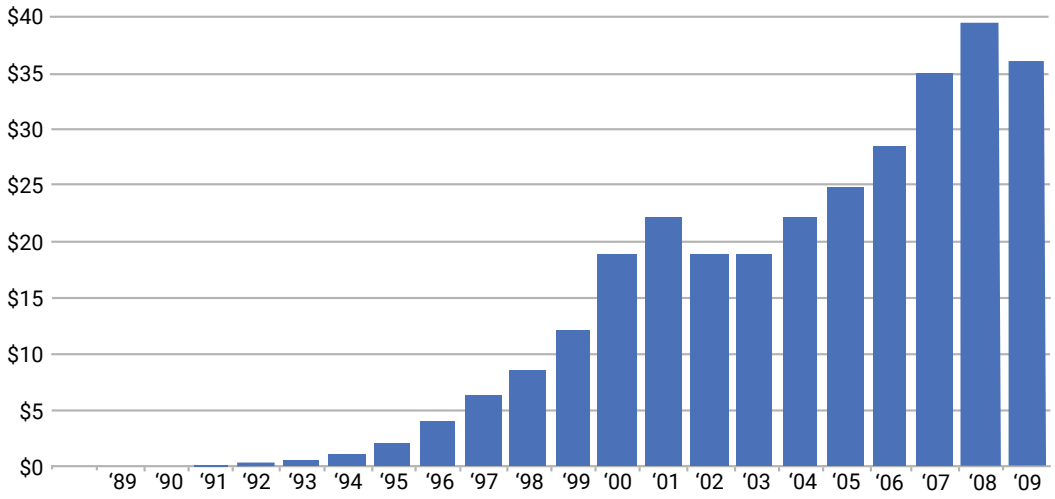
Let's look at Microsoft and Cisco during the post-bust years again. After the 2000–'02 tech stock crash, Microsoft's shares stagnated for years.

However, the business continued to grow sales, improve products, and eliminate competitors.




It was the same case with Cisco. Although Cisco shares were stagnant for years after the dot-com crash, the company steadily grew its sales.

## Cisco Annual Revenue




In addition to extremely negative investor perception, stocks in Phase 4 have overvaluation counting against them. During this phase, businesses must "work off" the excessive overvaluations built up during Phase 3.

They do so in a two-part process.

For Part 1, a business's stock price must go down.

For Part 2, its earnings must go up.

Here's how it works…

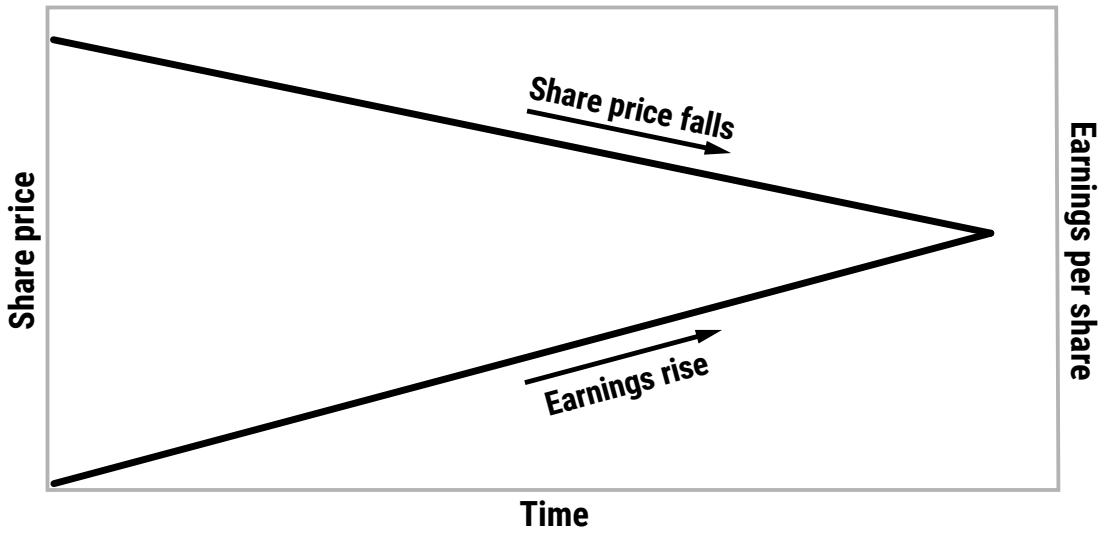
Let's take a hypothetical business, Horizon Technologies. It's a great data storage and security business and one of the clear leaders in its industry.

Because Horizon is a high-quality business, investors got very excited about it during the Phase 2 boom and bid its stock market value to 100 times its annual earnings.

Since Horizon earned $2 per share, its peak share price was $200 per share (100 × 2).

But now, we're in a post-crash environment… and Horizon must work off its overvaluation in order to become a compelling investment.

Here's how it can get there…




During Year 1 of the post-boom crash, Horizon's stock falls 40% to $120 per share.

However, the data storage company grows its earnings to $2.50 per share, an impressive 25% annual growth rate.

At the end of Year 1, Horizon's stock price is $120, and it earns $2.50 per share. This gives us a price/earnings multiple of 48 (120 / 2.50). Still an expensive stock.

During Year 2 of the post-boom crash, Horizon's stock falls another 10% to reach $108 per share. However, the data storage firm grows its earnings by 25% again. It earns $3.13 per share.

This gives us a P/E multiple of 34.5 (108 / 3.13). Still an expensive stock.
During Year 3 of the post-boom crash, Horizon's stock falls 20% to reach $86.40 per share. Still, the company advances its data storage technology and its business plan.

Horizon grows its annual earnings by 25% again to $3.90 per share. This gives us a P/E ratio of 22 (86.40 / 3.90), which is a very reasonable price to pay for a dominant, fast-growing business.

Remember, a P/E ratio has two parts… the "P" and the "E."

The more the "P" falls and the "E" rises, the cheaper the stock will be.

I've spent a good amount of time showing you the example of Horizon Technologies for a simple reason: ***The Phase 4 process of declining stock prices and rising earnings is absolutely crucial for investors***.

You could think of this process as the "prep work" that must be done before high-quality tech firms become high-quality investment opportunities.

Although **The Hangover** can seem miserable, it's actually a healthy process for potential shareholders. You can think of this phase as a brutal training program for elite military personnel. Many people who enter these programs drop out because they are so difficult. Just like how many people give up on military training because it's so difficult, many businesses drop out of the industry landscape during the difficult Phase 4.

Only companies with the best technology and the best business models make it. Those who make it through the program are tough as nails – forged by fire.

If a company can walk through Phase 4's "valley of death" and come out on the other side, chances are good that it's got great products or services… chances are good that it's going to be a long-term dominator in its sector… and chances are good it will make its shareholders a lot of money.

This pleasant turn of events happens in Phase 5…

## Phase 5: The Payoff

In the stock market, just as in life, there are periods of darkness followed by light… periods of cold followed by warmth.

Phase 5 is when darkness turns to light.

It's the spring that follows winter.

As with all phases of a revolutionary technology's investment lifecycle, progress in the technology itself advances.

As I detailed in Phase 4, a high-quality technology business with a severely overvalued stock must go through **The Hangover**… a long period of "working off" that overvaluation.

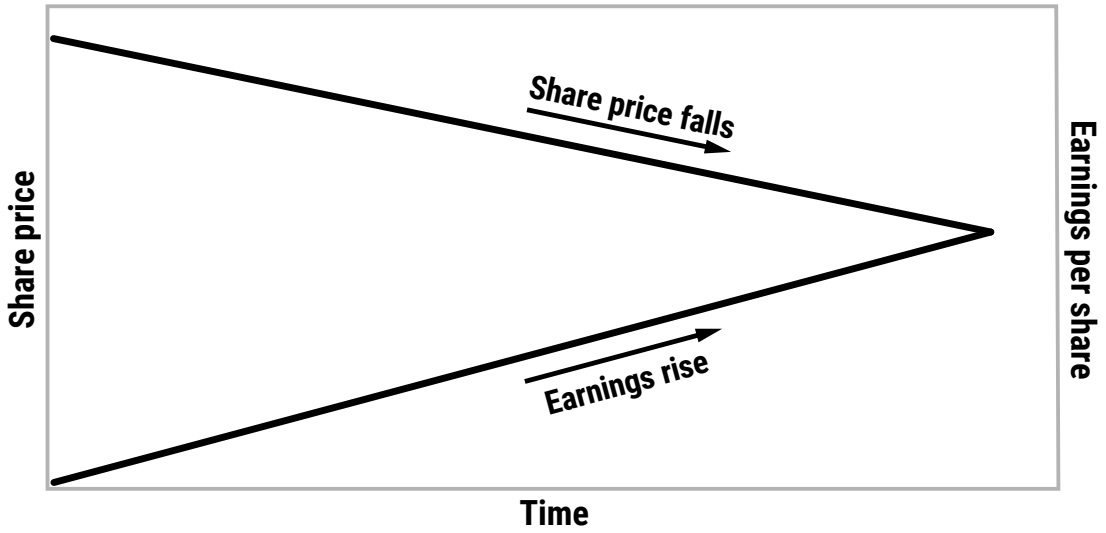
For the business to get cheap enough to represent a compelling investment opportunity, the earnings must rise substantially and the stock price must fall substantially. (You can lose money in a great business if you pay a stupidly expensive price for your ownership stake.)

We need to see the "P" drop and the "E" rise to create a "convergence" that kicks off **The Payoff**.

**The Payoff** begins when a dominant technology company's share price falls enough and its earnings rise enough to create a compellingly low P/E ratio.

(For the record, you can use other valuation metrics like price/sales or price/cash flow or enterprise value/EBITDA to evaluate businesses. But to keep things brief and simple, I'm using P/E here. No matter what metric you use, the concept is the same.)

Again, here's what that "stock price falling, earnings rising" convergence looks like:




At this point in the lifecycle, the technology will most likely have achieved mass adoption.

In fact, many consumers could already have their second or third versions of the technology. They could have their second or third smartphone… their second or third desktop computer… or their second or third 3D printer.

With mass adoption comes robust revenues and profits for the one or two or three firms that now control the market.

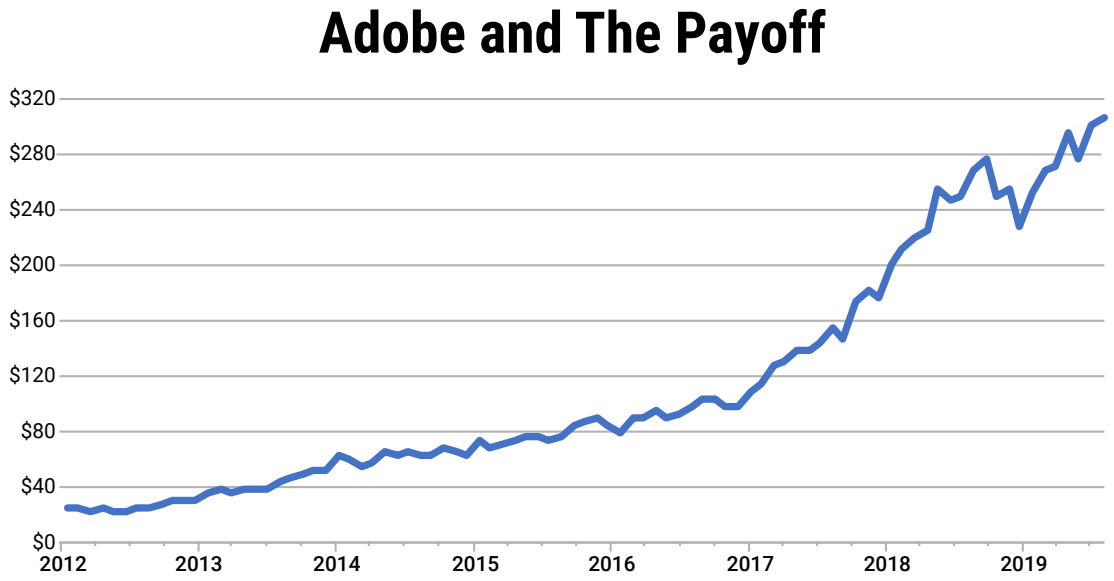
The companies enjoying that market control can direct a good portion of their revenues toward research and development, which will further cement their dominant positions and insulate them from competition. These dominant firms might also start returning capital to shareholders in the form of dividends or share buybacks.

For example, by 2003, Microsoft had grown so dominant in the software space and was generating so much cash that it paid its first ever dividend. It went on to generate a more than 600% return for shareholders over the next 16 years.

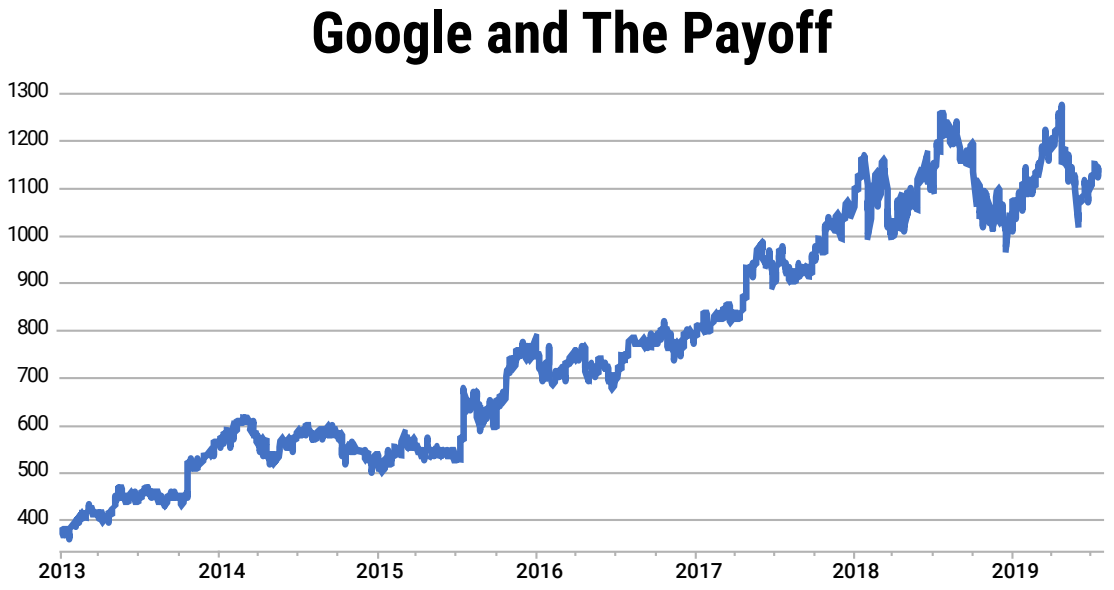
During **The Payoff**, stock prices of these dominant firms are unlikely to soar 100% in a single year like their younger selves did during the early days.

However, these companies can still be excellent, stable growth stocks with the potential to generate 10%–20% annual returns for years. Microsoft is a good example of this.

Another good example is Adobe Systems, the maker of the world's most popular PDF programs. As Adobe dominated its market and enjoyed the profits that go with that dominance, shares climbed more than ninefold from 2012 to mid-2019.




Another example of an established industry dominator enjoying **The Payoff** is Google (which later became part of the holding company known as Alphabet). As Google dominated the search engine market, its shares nearly quadrupled in value from mid-2012 to mid-2019.




A dominant technology company can enjoy more than a decade of growing revenues, growing cash flows, and limited threats to its position. But nothing lasts forever, especially in the technology business.

Eventually, all dominant technology companies enter Phase 6, **The Danger Zone**.

## Phase 6: The Danger Zone

Eastman Kodak… IBM… Blackberry… Nokia… Hewlett-Packard.

The history of business contains many examples of large, seemingly strong technology companies getting eaten alive by competitors who created better technologies, better products, and better services.

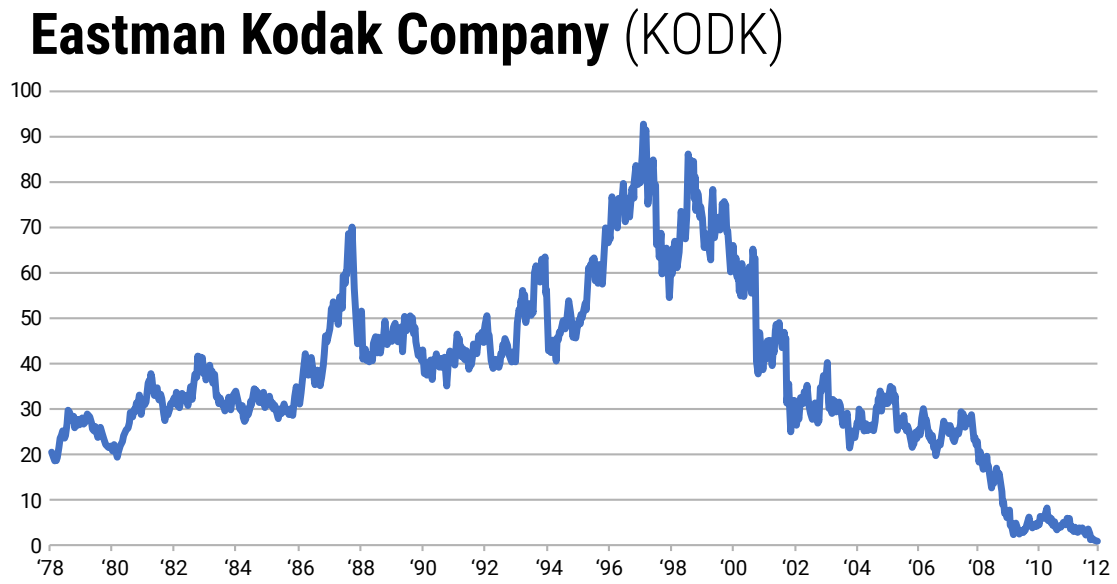
This is why investors who enjoy the gains during Phase 5 will eventually be confronted with a serious dilemma:

***Should you hold on to your dominant blue chip and bank on it being able to change its products, its culture, and often its entire business model as technology and customers change?***

That can be a heck of a lot to ask of a company that has been doing things a certain way for more than 20 years.

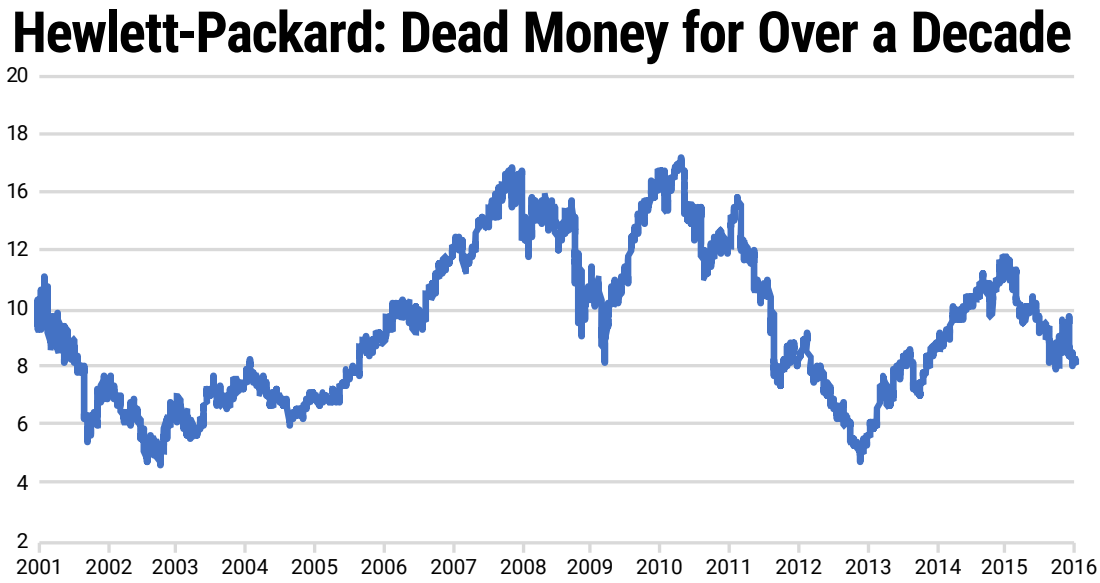
For example, Eastman Kodak was the world's dominant photography company for decades. Its employees were the developers of digital photography.

However, Kodak's managers were set in their ways. They dismissed the threat from digital photography. The company was crippled by this threat and eventually went broke.



Or, take Compaq Computer. In the 1990s, Compaq was one of the world's dominant personal computer makers. By the end of the decade, it was being overtaken by competitors like Dell.

Eventually, a shaky Compaq was sold to another once dominant blue-chip tech company, Hewlett-Packard, in 2001. The acquisition is widely considered one of the worst in U.S. corporate history. Shares of the company now known as HP Inc. were generally dead money for over a decade.




I don't know about you, but I'd rather not risk my capital on a large technology company executing a substantial business overhaul. It's a high-wire act with little room for error.

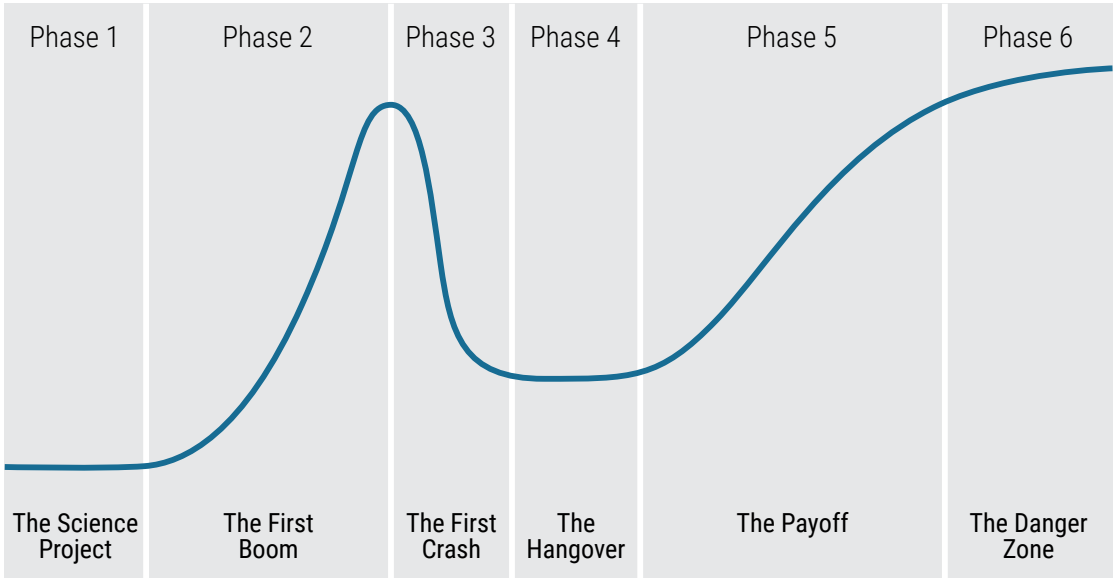
For me, it comes down to opportunity cost. The transition from Phase 5 to Phase 6 is marked by a slowdown in revenue and earnings growth in the dominant companies. Instead of growing at 10% or 15%, growth slows to 5% or 8%.

While an older technology is moving into **The Danger Zone**, other newer technologies will be entering their Phase 2s and Phase 5s. I'd rather deploy my capital in those areas.

That is why a once-dynamic, once-revolutionary company that is now experiencing slow growth and facing grave competitive threats should not get your investment capital.

And so, we are at the end of the revolutionary technology investment lifecycle. Here's what it looks like:

## The Lifecycle of Revolutionary Tech Investments




While it's easy to see which of these phases are best for investors (2 and 5), knowing how to make money in those phases isn't so obvious.

That's what the next part of our playbook is all about...

# The Right Strategy for the Right Phase

Like I said, it's easy to see that Phase 2 and Phase 5 are best for investors.

It's also easy to see that phases 1, 3, 4, and 6 are unattractive or even dangerous.

Here's what that means:

In Phase 1, we want to study the technology and the potential players – but not invest.

In Phase 2, we want to be shareholders.

In Phase 3, we want to be out with our profits.

In Phase 4, we want to be spectators, studying the sector and figuring out who the winner or small group of winners will be.

In Phase 5, we want to own the businesses that dominate the industry – and vacuum up all the profits.

In Phase 6, we need to decide if we want to own a large, slow-growing technology firm that is a good candidate for disruption, or if we should cash in our chips and deploy them elsewhere.

Said another way, we want to be invested in advance of and during bull markets – and not be invested in advance of or during bear markets.

Of course, that's easier said than done.

But that's why I've put together this simple, straightforward playbook.

You already know the phases of the revolutionary technology investment lifecycle. And now I'm going to show you two different investment strategies you can use to get a great balance of risk vs. reward.

## Strategy 1 – Buy a Basket

During Phase 2 – **The First Boom** – you're sure to see dozens of companies, both public and private, working furiously to become the winner of whatever epic technology race they are in.

In the early days of the internet, tons of companies were trying to create the best search engine… the best online store… the best email system… etc. In the early days of the automobile industry, more than 100 carmakers were trying to become the world leader.

During these early periods, it's virtually impossible to consistently pick the one or two companies out of dozens that will emerge as the winner(s) in 10 years' time. Placing all your chips on just one or two companies is a risky way to invest in the sector.

Instead of placing an all-or-nothing bet, investors should use what I call the **Buy a Basket** approach during Phase 2.

Putting all your money in a single company can pay off massively if it "threads the needle" and comes out on top. But doing so exposes you to significant downside risk. If there is a major problem at your chosen company (like a technology problem, an accounting scandal, or a crazy management decision), you could suffer a big loss.

That's why I like the **Buy a Basket** approach.

When I say, "buy a basket," I mean pick four to 10 of the best companies in a sector – and buy all of them.

By purchasing a basket of the best companies, you get lots of upside potential, but a good measure of diversification and downside protection. You avoid the risk of losing big on one concentrated bet.

When you **Buy a Basket** of four to 10 companies, you'll probably wind up holding some losers. But the winners will more than make up for them, providing you with an outstanding "blended" return.

For example, let's say you buy shares in 10 promising companies in Phase 2 of a big technology trend. You hold shares for four years. Some of your investments don't work out. Some do okay. A few do spectacularly well.

Your returns look like this:

| Investment | Return |
|---|---|
| Stock 1 | 30% |
| Stock 2 | -90% |
| Stock 3 | -83% |
| Stock 4 | 495% |
| Stock 5 | -25% |
| Stock 6 | -59% |
| Stock 7 | 784% |
| Stock 8 | -42% |
| Stock 9 | 879% |
| Stock 10 | -5% |
| Average | 188% |

You bought 10 different stocks. Four went up. Six went down.

That's just a 40% success rate.

But because you hit a few big winners (No. 4, No. 7, and No. 9), you made an outstanding average return of 188%.

And you made this excellent return while being right just 40% of the time. That's the power of hitting some big home runs.

This, by the way, is the thinking employed by the world's top venture capitalists – the backers of early-stage, privately held companies.

The best VCs know more than half of their investments won't work out. But the hits will be so large that they more than make up for the losing investments.

It's not always possible to **Buy a Basket** in a sector. Sometimes, there aren't many good individual companies trading at good prices in a sector at the same time.

But when it's possible to do so, buying a handful of high-quality companies is a great way to invest in a revolutionary technology in its early stage. We get exposure to high-quality businesses, but we avoid single-company risk.

However, **Buy a Basket** is not the optimal strategy for investing in advance of Phase 5, the second of our moneymaking phases.

Sometimes it's not even possible – and it's almost never necessary.

Here's what works…

## Strategy 2 - Buy the Best

Remember the "valley of death" that defines Phase 4 of a revolutionary technology's investment lifecycle?

By the time a revolutionary technology sector gets through that valley, it's almost always clear who the winners are.

Remember, those tough times accelerate the emergence of strong players and weak players. The weak players go bankrupt or are acquired by the strong players. The field of competitors grows much smaller… sometimes leaving a field of just one player.

If there is a difficult part about investing in Phase 5, it isn't figuring out which companies have the best technologies, the best business models, and the strongest balance sheets.

By the time Phase 4 and **The Hangover** is near its end, figuring out the best businesses is easy.

***They are often the only ones still around.***

If there's a difficult part about investing in Phase 5, it's figuring out when to buy the outstanding businesses.

Remember, Phase 4 often features rallies that can excite people and get them thinking prices have broken out to new bull-market levels… only to have those rallies extinguished by selling pressure. A sector's **Hangover** can contain a dozen "fake-outs before the breakout."

The hard question to answer is, ***"When does Phase 4 become Phase 5?"***

Answering this question is just as much art as it is science. There's no one indicator or one analytical method that serves as the "magic bullet" for all technology investment lifecycles.

However, there are some signs that signal when Phase 4 is in the rearview mirror.

Those signs are:

- The dominant, high-quality sector leaders become cheaper than the broad market, despite their outstanding annual revenue and earnings growth rates in excess of 15%. We're looking for the convergence of lower stock prices and higher sales and profits.

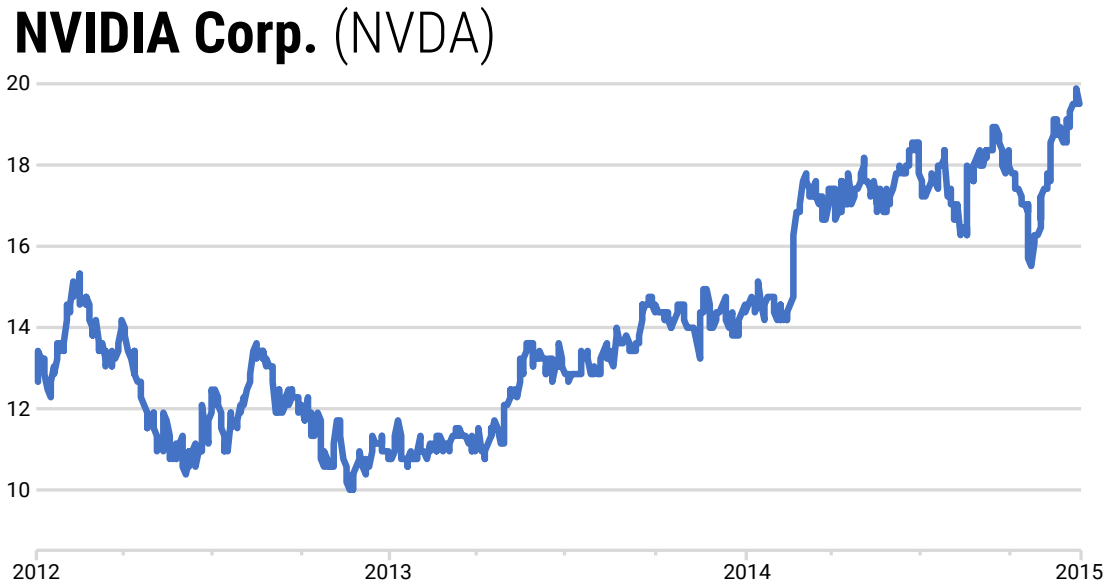
- Utter disinterest in the sector from the investment public. Signs of disinterest are investment fund closings, a lack of coverage in the financial media, and the stocks rading cheaply.

- Bad news and disappointing earnings reports are met NOT with stock price declines, but by stable – or even positive – price movements. When a stock or sector holds steady or even gains in price in the days after negative news hits the wires, it's a strong indication that anyone who wanted to sell the stock has already sold. When nobody is left to sell, you are left only with buyers.

- Meaningful share-price breakouts. A price breakout occurs when a stock reaches its highest price during a given time period, like 52 weeks. A meaningful price breakout indicates that most sellers are out of the market and buyers are the dominant force.

- A pattern of "higher highs and high lows" over the course of a year. When a stock consistently registers short-term price highs that are higher than the previous highs and short-term lows that are higher than the previous lows, you very well could have a new bull market on your hands.

You can see a series of "higher highs and higher lows" in the chart below. It's a chart of top technology firm NVIDIA from 2012 to 2015. As you can see, the stock suffered a sell-off in 2012, and then went on to register a series of "higher highs and higher lows."




Figuring out when Phase 4 (which is bad for investors) is ready to transition into Phase 5 (which is good for investors) comes down to the "weight of the evidence" among the factors listed above.

When you see all five of them, you are very likely at the end of Phase 4 – and it's time to **Buy the Best**.

When the weight of the evidence indicates a tech sector is about to emerge from the valley of death… from **The Hangover**… just follow a simple, reliable strategy that has produced excellent returns for over a century…

**Buy the Best** – the largest, strongest players. They are often the only ones left.

For example, after the 2000–'02 tech bear market, it was obvious Microsoft was the best desktop software business. It was obvious Cisco was the best network equipment business. It was obvious Amazon was the best online retail business.

## Summing Up

Thanks to the magic of scalability – the ability of a business to massively grow revenues while minimally growing costs - no other kind of business can create great wealth in a short time like a technology business.

While many people know how successful tech companies like Microsoft and Apple have made their shareholders wealthy, most people don't know how each and every revolutionary technology goes through a six-phase lifecycle.

Most people don't know how to profitably invest in the phases of the lifecycle.

Now, you do.

## How to Profit From a Revolutionary Technology


The knowledge in this playbook can help you consistently make large capital gains from technological innovations and the stock prices they send soaring.

Because this way of seeing the business world is so powerful – and because so few people are aware of it – ***your knowledge of it will give you an enormous advantage over others in life***.

I hope you use this advantage to its fullest and reap the rewards.

Regards,

Brian Hunt