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Domestic Equities

The broad market generally surged higher in February, continuing the advance that began the Friday before the election, November 4, 2016. Supporting higher stock prices, companies reported earnings for the fourth quarter and fiscal year 2016, which on average, beat forecasts. Not only were earnings better than expected but the economy is doing better than forecasters thought last Fall. Citigroup Global Markets gathers data on economic forecasts and then computes a score when the data is released. The release is called the Citi Economic Surprise Index and it includes data such as GDP, factory output, jobs and durable goods, among others. Since November 17, 2016, the reported data has exceeded the previous expectations. In other words, for three and a half months the economy has been doing better than many had predicted, which may be giving investors growing confidence to take stock prices higher.

We began March with an ICON market value/price (V/P) ratio of 0.98, indicating stocks in the ICON database are priced about 2% above our estimate of fair value – slightly over-priced but not to the extreme typical of many peaks. We also do not see other behaviors and data we would expect to see at a market peak. For example, we would expect investor sentiment to be very bullish at a peak, but it is not currently. We would also expect a very low level of short selling, but that is not the case. We see credit spreads declining, suggesting investors are gradually pricing in decreasing probabilities of bond defaults, but they are not down to the level of the last stock market peak when a high level of confidence prevailed. Pricing in the options market is one way to gauge investor sentiment. Lately it is neutral, not near an extreme we would expect at a market peak. As a result of these observations, we have not moved to a defensive posture and are holding positions we believe to be priced below our estimate of fair value.

After a very sluggish 2016, certain industries in the Healthcare sector have come alive, propelling the S&P 1500 Sector Index to be the best performing sector index in February. In mid-February we reduced the ICON Tactical Allocation Portfolios (ITAP) exposure to the Financials sector and established a position in the Healthcare sector. Financials is still a "hold" according to our system and remains overweight. We just needed some of its allocation for Healthcare. In the market, we see sector leadership flip-flops on a daily basis as investors react to news or earnings. Our system is designed to have a longer time horizon based on value and try to ignore the daily gyrations.

International Equities

We have similar sector value readings internationally as in the U.S. The Financials sector appears to be the best value, while at the bottom are the Energy sector and some of the so-called recession-proof, defensive sectors. As for countries, developed northern and central European countries are generally at the top of our rankings. In emerging markets, Asian countries generally offer the best value, but some Central and South American countries have had V/P ratios move above 1.00.. In mid-February we increased our international exposure to emerging markets. These markets had a delayed reaction to the U.S. election and lagged most other markets at first, but joined the global advance in late December.

Bonds

It is our opinion that the most important determinant of long-term interest rates is the expectation for inflation. We expect any increase in the FED's target for the Federal Funds rate to be viewed as a war against any potential inflation. While the FED may succeed in taking the Federal Funds rate higher, we expect longer-term bond investors will be comforted in the view that a higher Federal Funds rate will help keep inflation low. Therefore, we do not see longer rates rising in the near future. Since mid-November the yield on the 10-Year U.S. Treasury Note has been in the 2.30% to 2.60% range. This seems sensible to us given the current inflation setting.

Summary

Analysts throughout the investment industry still do not have a clear picture of what changes to the tax code and infrastructure spending will come out of Washington. As more becomes known, we expect to see changes to our valuation readings. If and when that happens, we will move from any over-priced positions into those we consider under-priced and may hold cash if we see extreme over-pricing along with conditions typical of market peaks. For the time being, we like being invested in issues we consider to be values.

The data quoted represents past performance, which is no guarantee of future results.

Opinions and forecasts regarding sectors, industries, companies, countries and/or themes, and portfolio composition and holdings, are all subject to change at any time, based on market and other conditions, and should not be construed as a recommendation of any specific security, industry, or sector.

Investing in securities involves inherent risks, including the risk that you can lose the value of your investment. An investment concentrated in sectors and industries may involve greater risk and volatility than a more diversified investment. Investments in international securities may entail unique risks, including political, market, regulatory and currency risks. In general, there is less governmental supervision of foreign stock exchanges and securities brokers and issuers. Investing in fixed income securities such as bonds involves interest rate risk. When interest rates rise, the value of fixed income securities generally decreases. High-yield bonds involve a greater risk of default and price volatility than U.S. Government and other higher-quality bonds.

ICON's value-based investing model is an analytical, quantitative approach to investing that employs various factors, including projected earnings growth estimates and bond yields, in an effort to determine whether securities are over- or underpriced relative to ICON's estimates of their intrinsic value. ICON's value approach involves forward-looking statements and assumptions based on judgments and projections that are neither predictive nor guarantees of future results. Value readings are contingent on several variables including, without limitation, earnings, growth estimates, interest rates and overall market conditions. Although valuation readings serve as guidelines for our investment decisions, we retain the discretion to buy and sell securities that fall beyond these guidelines as needed. Value investing involves risks and uncertainties and does not guarantee better performance or lower costs than other investment methodologies.

ICON's value-to-price ratio is a ratio of the intrinsic value, as calculated using ICON's proprietary valuation methodology, of a broad range of domestic and international securities within ICON's system as compared to the current market price of those securities. According to our methodology, a V/P reading of 1.00 indicates stocks are priced at intrinsic value. We believe stocks with a V/P reading below 1.00 are overvalued while stocks with a V/P reading above 1.00 are undervalued. For example, we interpret a V/P reading of 1.15 to mean that for every $1.00 of market value, there is $1.15 of intrinsic value which has not yet been realized in the market price.

The unmanaged Standard & Poor's Composite 1500 (S&P 1500) Index is a broad-based capitalization-weighted index comprising 1,500 stocks of Large-cap, Mid-cap, and Small-cap U.S. companies. The unmanaged Standard & Poor's (S&P) Composite 1500 Sector Indexes track the performance of sectors that comprise the S&P Composite 1500 Index. Total return for the unmanaged indexes include the reinvestment of dividends and capital gain distributions but do not reflect deductions for commissions, management fees, and expenses. The Portfolios' composition may differ significantly from the indexes. Individuals cannot invest directly in an index.

The 10-year yield is the benchmark 10-year yield to maturity reflected by the current issue 10 year U.S. Treasury note.

Source: Bloomberg, FactSet

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