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# ICON Insights

Market Commentary - November 2017

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## Domestic Equities

If an investor with terrible timing had invested $1.00 into the S&P 1500 Index on October 9, 2007 (the pre-recession market peak), and held it through Friday October 27, 2017, (slightly over 10 years), that dollar would have more than doubled to $2.08. That doubling would have occurred despite the investor's riding down the 17-month bear market surrounding the "financial crisis" and "great recession". On the other hand, if an investor with perfect timing had invested that $1.00 into the S&P 1500 Index at the market bottom, March 9, 2009, that dollar would have grown to $4.65. Viewed either way, this bull market over the last eight and a half years has been impressive. The key to participating in either of these two hypothetical situations was being invested and holding steadily during this time.

From what we've seen and heard, we do not believe that holding steadily during the bull market has been the norm. There were plenty of concerns (some real, some not) to distract investors, including inflation, deflation, double dip recession, stubborn unemployment and the European debt crises of 2010 and 2011. The imperfect nature of the economic expansion bothered some investors as economic growth never surged to a steady 3% to 4% annual pace. Throw in historically low interest rates that puzzled some analysts, Brexit, a sharp drop in the price of oil and polarizing politics and you have a list of reasons we suspect many investors have not fully participated in the bull market.

Guided by our valuation readings, we have used these monthly Portfolio Updates for more than eight years to opine that the market could keep moving higher. During the first four years, stocks, on average, were frequently priced at 10% to 30% discounts from our estimate of fair value. In that setting, returns were driven by two factors: prices trying to catch value and value growing as corporate earnings grew. The last four years stock prices have generally been right near our estimate of fair value. The current situation is similar to what we correctly described last April when we wrote "With stocks priced, on average, near our estimate of fair value, potential returns can simply come from earnings growing and therefore, fair value growing. We like that possibility so we are content being invested in our favorite industries and sectors." Now, with our ICON market V/P beginning November at 1.01, we believe the broad market can move high with earnings propelling fair value higher.

| S&P 1500 Sector Index Returns | |
|---|---|
| As of 10/31/2017 | |
| Information Technology | 35.9% |
| Healthcare | 19.6% |
| Materials | 19.2% |
| Utilities | 16.0% |
| Financials | 14.8% |
| Industrials | 14.6% |
| Consumer Discretion | 13.7% |
| Real Estate | 6.5% |
| Consumer Staples | 4.8% |
| Energy | -8.5% |
| Telecommunication Services | -11.9% |

Data quoted represents past performance, which does not guarantee future results.

The table at right shows year-to-date returns for S&P 1500 Sector indexes through Tuesday, October 31. In February we reduced our allocation in Financials and increased our stake in Health Care. In April, we reduced our positions in Consumer Discretionary and Materials to rotate into Information Technology. We are generally pleased with our limited allocations, as we have been tilted toward the above average sectors while tilting away from lesser performing sectors. We do not see any of the behaviors or conditions that would indicate it is time for a major rotation.

## International Equities

In international markets we see the same dual factor driver of returns that we've seen domestically: stock prices at a discount to our estimate of fair value and growing earnings. Indexes of developed markets and emerging markets have outpaced the U.S. market this year. Based on valuation, we expect that leadership to continue. Valuation readings for developed markets favor Europe whereas Asia appears better for Emerging Markets.

## Bonds

For the last year the yield on the 10-year Treasury note has been in the 2.10% to 2.60% range, which appears sensible to us given the inflation outlook and economic growth. Currently, we do not see a catalyst that could drive the yield outside of that range in either direction.

## Summary

As of Tuesday October 31, 327 of the S&P 500 companies have reported third quarter earnings. They have beaten estimates by an average of 4.6% and are up 8.0% year-over-year. Leading the pace, 40 of 68 Information Technology companies have reported, and their earnings per share are up an average of 24.8% from a year ago and have beaten estimates by 10.9%. In our valuation equation, with all else being equal, the more a company earns, the greater its intrinsic value. We are in a setting where earnings are growing, value is growing and stock prices are just trying to keep pace.

***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) 500 Index is a market value-weighted index of large-cap common stocks considered representative of the broad market. 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 figures for the unmanaged sector indexes do include the reinvestment of dividends and capital gain distributions but do not reflect the costs of managing a mutual fund.*

*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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