ICON

Portfolio Update December 2016

By Craig Callahan, DBA | ICON Founder & President **Published 12'1'2016**

Domestic Equities

In the "blink of an election" investors have gone from pricing in one economic view of the future to pricing in a very different view. The table below shows the year-over-year change in real gross domestic product (GDP) and the Consumer Price Index (CPI).

	2010	2011	2012	2013	2014	2015	2016*	2017*	2018*
Real GDP	2.5%	1.6%	2.2%	1.7%	2.4%	2.6%	1.6%	2.2%	2.2%
CPI	1.6%	3.2%	2.1%	1.5%	1.6%	0.1%	1.3%	2.3%	2.4%
*Data for 2016, 2017 and 2018 are estimates from a Bloomberg survey of economists.									

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

Prior to the election, investors appeared to be pricing various assets with the expectation of a continuation of real GDP in the 1.6% to 2.2% range and CPI in the 1.5% to 2.4% range: generally slow growth with minimal inflation, similar to what we have seen the last few years. President-elect Trump campaigned on a platform of stimulating economic growth through fiscal measures such as infrastructure spending and tax cuts, and it appears he has a Republican-controlled Congress with a similar mindset.

The market drifted lower in October, hitting a low November 4, 2016, the Friday before the election. We believe many investors are anticipating faster economic growth, and the S&P 1500 Index was up about 6.3% off that low through November 30, 2016. Further, with the anticipation of slightly higher inflation accompanying that faster growth, the yield on the 10-year U.S. Treasury Note rose from about 1.78% on November 4, 2016, to close to 2.38% on November 30, 2016.

As you may recall, based on our estimate of the market's overall value, we have been calling for stock prices to break out of the sideways market to the upside. We believe the election results and the anticipation of faster economic growth accelerated the market's path upward. Further, the sector leadership over the past month appears sensible to us. The table on the right shows returns for the S&P 1500 sector indexes from the low on November 4 through November 30. For over a year, our portfolios have maintained an overweight position in the Financials sector relative to the broad S&P 1500 Index. The Financials sector has been the leading sector not only during this recent November move but also dating back to the market low of February 11, 2016. Apparently investors expect banks and other Financials sector industries to benefit from anticipated faster growth, higher interest rates and de-regulation. We believe the move in the Industrials and Materials sectors is related to the potential focus on infrastructure spending.

S&P 1500 Sector Index Returns 11/4/16-11/30/16	
Financials	15.6%
Industrials	10.8%
Energy	9.8%
Materials	8.9%
Consumer Discretionary	7.1%
Telecommunication Services	6.0%
Health Care	3.3%
Information Technology	2.9%
Real Estate	1.0%
Consumer Staples	2.1%
Utilities	2.1%

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

ICON's overall average market value-to-price (V/P) ratio has dipped below 1.00 recently, partly due to the rise in stock prices but mostly because of the increase in the yield on the 10-year U.S. Treasury Note. Although the market V/P is below 1.00, we do not see the extreme over-pricing typical of many market peaks. We have seen an increase in bullish sentiment this month as measured by the American Association of Individual Investors (AAII) Sentiment Survey. We believe this survey can often be overly bullish at market peaks and overly bearish at bottoms. On November 3, 2016, 23.6% of those participating in the survey were bullish while 34.3% were bearish. Just three weeks later on November 24, the percentage of those surveyed who were bullish had increased to 49.9% while the percentage who were bearish had declined to 22.1%. We do not see this ratio of bulls to bears as near the extreme we believe is typical of many market peaks.

International Equities

In addition to U.S. equities, the other big post-election winner was the U.S. Dollar, which gained strength presumably on investors' anticipation of faster U.S. economic growth and higher interest rates – a standard recipe for a stronger currency. Stocks in Japan rallied in response to the weaker Yen as did stocks in China where its currency weakened relative to the U.S. Dollar. Although the Euro weakened, European stocks, in general, did not receive a boost. Emerging markets, many of which are U.S. dollar based, dropped sharply at first but inched back up later in November. Some emerging country V/Ps are working their way up our list, but we will leave exposure to emerging markets underweight for the time being.

Bonds

As inflation is one variable investors consider when pricing bonds, a yield on the 10-year U.S. Treasury Note in the 2.40% range suggests to us investors expect only a slight increase in inflation as a result of potential fiscal stimulus and tax decreases. We agree and do not see the potential for a significant increase in inflation. We believe our economy has the capacity to produce more goods and services without significant upward pressure on prices. Also, the strong dollar can help keep inflation down.

Finally, OPEC and other oil producers are struggling just to keep the price of a barrel in the $50 range, let alone raising it. All in all, with only a modest increase in inflation, we do not fear or expect a sharp rise in long term interest rates.

Summary

Many investors seem uncertain about where the economy will go. Talking heads in the media seem to be in constant disagreement about the impact of any potential fiscal stimulus on growth, interest rates and inflation. Analysts and economists can only guess about what an infrastructure spending measure or a new tax code would look like, let alone forecast market reactions. While this setting could lead to some daily volatility as analysts revise their "guesses" and investors react to news events, we are inclined to ride through the uncertainty until we see over-pricing and other behaviors we believe are typical of many market peaks.

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.

Gross Domestic Product (GDP) is the total value of goods and services produced in the national economy in a given year. It is the primary indicator of economic growth.

The Consumer Price Index (CPI) is a measure of the average change in prices over time of goods and services purchased by households. The CPIs are based on prices of food, clothing, shelter, fuels, transportation fares, charges for doctors' and dentists' services, drugs, and other goods and services that people buy for day-to-day living.

The AAII Investor Sentiment Survey measures the percentage of individual investors who are bullish, bearish, and neutral on the stock market for the next six months; individuals are polled from the ranks of the AAII membership on a weekly basis. Only one vote per member is accepted in each weekly voting period.

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

Please visit ICON online at InvestwithICON.com or call 1-800-828-4881 for the most recent copy of ICON's Form ADV, Part 2.

5299 DTC Boulevard, 12th Floor
Greenwood Village, CO 80111
1-800-828-4881 • InvestwithICON.com