ICON

Portfolio Update

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Domestic Equities

The broad market has generally gone sideways since early December, except for a surge January 25 that took most indexes to all-time highs. That surge allowed the broad market to post a slight gain for January. Corporate earnings are supporting stock prices at these levels. For the S&P 1500 Index, as of this writing, 559 companies have reported fourth quarter 2016 earnings. On average, these companies have beaten earnings expectations by 3.46%. Further, these same 559 companies have averaged growth in earnings per share of 5.96% over earnings per share reported in the fourth quarter of 2015. Earnings growth paused in 2015 due in large part to the drop in the price of oil and the strength of the U.S. Dollar. Some analysts labeled that situation an "earnings recession." Based on the most recent quarter, earnings, on average, are growing again.

Rather than being surrounded by enthusiasm and optimism, the recent all-time highs and the Dow Jones Industrial Average closing above 20,000 were greeted mostly with skepticism. Some analysts contend the bull market has gone on too long, as it began March 2009, nearly 8 years ago. We disagree with that notion because we do not believe bull markets have any time limitations. Each bull market is different. Other analysts suggest price/earnings (P/E) ratios are too high and that stocks are expensive. Again, we disagree. We recently wrote a research report where we showed the simplistic P/E ratio for the broad market to be unreliable as a predictor of future returns. Instead, we prefer our own valuation system and rely on the ICON value-to-price (V/P) ratio. Our overall average V/P ratio ended January at 0.97, suggesting stocks in our database, on average, are about 3% over-priced relative to our estimate of intrinsic value – not the extreme reading we believe is typical of market peaks. We also believe our estimate of intrinsic value has a conservative tilt as the unknown factors of fiscal stimulus, infrastructure spending, tax cuts and deregulation and their potential to stimulate growth in earnings are not built in yet.

The Financials sector remains our largest sector weighting. At the industry level, 11 of the 14 industries in the Financials sector have V/P ratios greater than 1.00. Given these readings, we have not reduced that Financials sector exposure. 157 of the 213 companies in the S&P 1500 Financials Index have reported fourth quarter earnings. On average, they are 10.4% higher than a year earlier, a pace of growth almost double the average for the broad-market S&P 1500 Index mentioned above. In addition, those reporting companies are beating fourth quarter earnings expectations by 5.26%, again better than the average for the S&P 1500 Index.

International Equities

After a sluggish 2016, international equities markets have kicked in to start 2017. Returns are getting an extra lift from the decline in the value of the U.S. Dollar relative to various currencies such as the Euro, Yen and Pound. The advance is global, as returns seem equally spread over Europe and Asia. Emerging markets are doing very well with China, Taiwan, South Korea and India among the leaders. Those moves seem sustainable to us based on our V/P readings.

Bonds

From November 4, 2016 through December 16, 2016, the yield on the 10-Year U.S. Treasury Note rose from 1.78% to 2.60%. Since that peak it has drifted basically sideways, ending January at 2.45%. It fluctuates daily in reaction to any hints and guesses as to what fiscal stimulus may come out of Washington. We generally believe that inflation and inflation expectations are the biggest determinants of the yield. Even with fiscal stimulus and potentially faster GDP growth, we do not expect a boost in inflation, so the current yield makes sense to us. We do not expect the yield to move much higher.

Summary

Stocks, on average, are not cheap, as they often are at great buying opportunities, nor are they expensive, as is typical of market peaks. If the market would surge higher, say about 10%, we would be sellers and raise cash. At current levels, however, we are content holding existing positions as our portfolios are still tilted toward areas we believe are better than average 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.

Sources: Bloomberg, FactSet

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