ICON Insights

Market Commentary - November 2020

Published 11'3'2020

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Equities

Through October 31, 2020, the S&P 1500 Index is up 48.3% off its low March 23, 2020. We believe this is the beginning of a new bull market that could last at least two to three years. As bull markets never go straight up, this one has retreated off its high of September 2. It attempted to resume its upward path in early October but sold off through the second half of the month over virus, fiscal stimulus and election uncertainties.

One survey of investor sentiment shows investors remaining bearish throughout the six month advance. That leads us to believe there are many investors participating in the market one way or another without much conviction. As an example, they may not believe the market can go higher but their momentum model tells them to invest. Or they buy one particular stock because of its special appeal, but they don't like the broad market. Lacking a belief in the overall market, these investors are very jittery and quick to sell. While we expect the market to move higher over the next year, there may be more short term declines like we saw in late October.

The stock market is a market of stocks. We believe we get a better view of the market at the stock level than at the "30,000 foot" view or guessing about elections and the virus. Let's look at corporate earnings. The table shows rates of change for earnings for the large-cap S&P 500, mid-cap S&P 400 and the small-cap S&P 600 indexes based on a survey of analyst who forecast earnings. It shows a drop in earnings for 2020, but an impressive rebound in 2021 and more growth into 2022. The smaller the market capitalization the bigger the drop in 2020 but also the bigger the rebound. Of course these analysts can be wrong and they can change their forecasts, but for the time being this expected growth in earnings can support higher stock valuations.

Earnings Rate of Change

Year	Large 500	Mid 400	Small 600
2020	-9.7%	-17.3%	-25.5%
2021	23.2%	41.4%	84.7%
2022	15.7%	18.9%	21.2%

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

The late October dip in the market did not alter our sector and industry preferences. As for consumer related sectors we favor Consumer Discretionary over Consumer Staples and Financials. In the sciences, we favor Information Technology over Healthcare. For natural resources, the ICON system finds attractive value in Industrials and Materials but not in Energy. Generally, these preferences give our portfolios a tilt toward economically sensitive industries and sectors.

Bonds

For the year, the yield on the 10-year Treasury note hit a low of .508% on August 4 and has risen to .875% to end October. Although higher, the yield is still below expected inflation according to a survey of economists reported in Bloomberg. They are calling for CPI increases of 1.9% in 2021 and 2.0&% in 2022. We don't find this negative real return attractive and therefore favor short term corporate bonds.

Summary

Based on our valuation readings, stock prices, on average, would have to move up about 15% just to get to fair value. This puts us in disagreement with analysts claiming stocks are expensive based on a simplistic Price/Earnings (P/E) ratio*. This is nothing new as during the eleven year bull market from March 2009 to February 2020, there were similar claims yet the market moved higher. We believe that when considering all of the fundamentals of valuation - earnings, growth, risk and interest rates - stocks, on average, are attractively priced today and can move higher over the next year.

*We have written papers citing the deficiencies of the P/E ratio. Please call ICON if you would like copes of those papers. (800) 828-4881

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.

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. Total return figures for the unmanaged sector indexes do include the reinvestment of dividends and capital gain distributions but do not reflect deductions for commissions, management fees, and expenses. The unmanaged Standard & Poor's (S&P) SmallCap 600 Index is an unmanaged index of 600 domestic stocks chosen for their market capitalization, liquidity, financial viability, and sector representation. 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) MidCap 400 Index is a widely recognized unmanaged mid-cap index of 400 domestic stocks chosen for their market capitalization, liquidity, and industry group representations.

Price/Earnings (P/E) Ratio is the price of a stock divided by its earnings per share. 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 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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