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Stock Fair Value Briefing

Everyone appears to be waiting for something before they can decided where the market and the economy are headed. Ms. Yellen is waiting for inflation, Mr. Draghi is waiting for economic growth, some investors are waiting for earnings, others are waiting for a correction, and some just can't believe growth can continue because, well, it has been going on for so long. Everyone is waiting for something else to occur.

U.S. LARGE, MID & SMALL CAP				
Ticker	Name	Relative Value	Curr Pr	Under/Over
IVV	iShares Core S&P 500 ETF	107.4%	$ 248.49	
IJH	iShares Core S&P Mid-Cap ETF	118.5%	$ 177.16	
IJR	iShares Core S&P Small-Cap ETF	114.6%	$ 71.26	

Figure 1: U.S. Market Capitalization Fair Values for major capitalization categories.
Source: ISN

We have been concentrating on fair valuations and the changes within valuations for markets, sectors, industry groups and individual stocks. The message continues to indicate slow and steady growth with hesitations when the market gets ahead of itself.

Over the past month relative values advanced in largecap and smallcap capitalization areas while midcap retreated from being very near the cautionary level.

Largecap stocks have remained very close to the 107.0% - 109.0% Fv range for the past several months and each time market pricing gets ahead of fair value support, we see a retreat back to the safety range. Returns year-to-date have been good and above average at 10.42%. As long as the market continues to move within the fair expectation range the market can continue on a positive trend for some time.

Smallcap has struggled all year and performed well below the long-term average only posting a 3.64% return for the year. Even with valuations 14.6% above fair value, returns are low and have been negative for most of the first half. There have been great expectations for smallcap stocks since late last year, but they are having difficulty materializing. It may well take the remaining part of the year for underlying values (revenues, earnings, dividends) to move up to current expectation levels while unfortunately muting returns. Once that occurs, smallcap could easily post an excellent 2018.

Midcap is the one area that gives us a bit of caution. Earlier in the year this capitalization area moved into the cautionary level above 120% Fv, but never reached overvaluation of 130% Fv. Market returns have been acceptable at 7.15% for the year, but the remainder of 2017 could be very difficult to muster up much more than what we see so far.

U.S. LARGE CAP		
Name	Relative Value	Under/Over
Consumer Discretionary	104.7%	
Consumer Staples	103.5%	
Energy	102.0%	
Financials	105.3%	
Health Care	108.4%	
Industrials	109.1%	
Information Technology	111.5%	
Materials	107.1%	
Telecommunication Services	93.6%	
Utilities	108.0%	

Figure 2: U.S. Largecap Sector Relative Fair Valuations for Major Sector Classifications. Source: ISN

Sector Valuations

All large cap sectors remained above 100% FV, except for Telecommunication Services at 93.6% Fv. The struggling stock within the sector is CenturyLink [CTL] at 71.8% Fv. Information Technology took the top spot away from Industrials reaching 111.5% Fv, a 2.0 point increase from last month. Advanced Micro Devices [AMD] is experiencing intense pressure from the market to perform resulting in one of the

U.S. MID CAP		
Name	**Relative Value**	**Under/Over**
Consumer Discretionary	124.3%	
Consumer Staples	101.2%	
Energy	94.4%	
Financials	120.5%	
Health Care	117.8%	
Industrials	112.7%	
Information Technology	127.8%	
Materials	118.2%	
Telecommunication Svcs	98.8%	
Utilities	119.4%	

Figure 3 U.S. Mid cap Sector Relative Fair Valuations for major Sector Classifications. Source: ISN

highest overvaluations in the market. The stock is performing well, but we just wonder if expectations are just too high to reach.

Industrials remains in second place at 109.1% Fv which is a significant easing of overvaluation pressure when it reached 115.2% Fv earlier in the year.

Mid cap Financials have eased away from overvaluation conditions (130%+ Fv) just two months ago and now reside just inside cautionary levels at 120.5% Fv. This supports last month's easing from overvaluation pressures that were built up earlier in the year.

Consumer Discretionary joined Financials and Information Technology at cautionary levels posting a Fv score of 124.3% up from 118.8%. Live Nation Entertainment [LYV], Southby's [BID] and The New York Times [NYT] all contributed in pushing the sector into a cautionary valuation.

Information Technology remained at this cautionary level (127.8% Fv). Coherent [COHR], Take-Two [TTWO] and Fair Isacc [FICO] all assisted in keeping the sector high.

Energy continues to be undervalued at 94.4% Fv but, did come closer to full fair value throughout the month moving up from a heavily discounted level of 86.6% Fv. Southwestern Energy [SWN], SM Energy [SM] and Oceaneering International [OII] are contributing to the sector's lower valuation.

The only other midcap sector under full fair value in Telecom, just as in the largecap area but, the variation is only 5.6 points and the stocks in the sector are all very close to full fair value.

Small cap sectors are all above 100% Fv except for one, yes, it is Energy. The smallcap energy sector is following in their larger brothers footsteps at 93.1% Fv where 18 of the 32 stocks carry an undervaluation status.

Only two smallcap sectors are in cautionary territory, Information Technology and just barely, Materials. Kulicke & Soffa [KLIC], Rogers [ROG] and Lumentum [LITE] are all contributing to this high sector valuation.

U.S. SMALL CAP		
Name	**Relative Value**	**Under/Over**
Consumer Discretionary	114.7%	
Consumer Staples	119.3%	
Energy	93.1%	
Financials	115.4%	
Health Care	117.7%	
Industrials	110.9%	
Information Technology	124.6%	
Materials	120.2%	
Telecommunication Services	111.5%	
Utilities	118.0%	

Figure 4 U.S. Mid cap Sector Relative Fair Valuations for major Sector Classifications. Source: ISN

Industry Valuations

Food & Staples Retailing industry group remains under full fair value at 95.3% Fv, 1.6 points below last month. The other sector that was below full fair value last month, Pharmaceuticals & Biotechnology was able to move above the 100% Fv line to 104.2% Fv. Charles River Labs [CRL], MiMedx Group [MDXG] and Nektar

Therapeutics [NKTR] all are contributing to the industry group's higher valuation.

Four industry groups were at cautionary levels last month now there are three. Only one of the previous four remains, Semiconductors at 124.1% Fv moving down from 126.5% Fv.

U.S. Industry Group All Market Cap		
Name	RelativeValue	Under/Over
Automobiles & Components	113.7%	
Banks	116.0%	
Capital Goods	110.8%	
Commercial & Professional Servic	115.6%	
Consumer Durables & Apparel	128.3%	
Consumer Services	110.8%	
Diversified Financials	108.0%	
Food & Staples Retailing	95.3%	
Food Beverage & Tobacco	110.0%	
Health Care Equipment & Service	120.4%	
Household & Personal Products	101.2%	
Insurance	119.8%	
Materials	116.5%	
Media	109.5%	
Pharmaceuticals & Biotechnology	104.2%	
Real Estate	101.8%	
Retailing	105.1%	
Semiconductors and Semiconduc	124.1%	
Software & Services	111.5%	
Technology Hardware & Equipme	119.9%	
Transportation	105.7%	

Figure 5 U.S. Industry Group Relative Fair Valuations, Source: ISN

Banks, Insurance and Materials all moved back to within fair value range (80% Fv to 120% Fv). Banks and Insurance retreated the most and it was no surprise. Long time readers of these briefs are well aware that we never subscribed to the euphoria the market gave rising interest rates. We always felt the benefit was not as strong as expected and that rates would not rise as fast as expected. A hockey stick type of rate increase at the Fed would have been highly unlikely given the rest of the world's central bankers easing activities coinciding with very low inflation rates domestically.

Two new industry groups have joined Semiconductors in cautionary territory and they are: Consumer Durables at 128.3% Fv and Health Care at 120.4% Fv.

iRobot [IRBT] and Installed Building Products [IBP] are both contributing to Consumer Durables high valuation but, both have shown softness in the most recent period. In Health Care, Align Technology [ALGN] and Inogen [INGN] are pushing the industry group higher.