



PORTFOLIO UPDATE

July 2008

Domestic Market Commentary

June proved to be a big setback to the stock market, which had been moving higher off its March 10th low. A few indexes have dropped back to, or even below, their March lows. (Although in late June, the Dow Jones Industrial Average fell below its March 10th low, other indexes and benchmarks have stayed above their March low.) The cause for the most recent decline was a return to a scenario of events that have caused investors to sell stocks in the past. The price of oil hit a record high by reaching the \$140 -per-barrel range. The price of gold rose and the dollar weakened against the Euro, although neither of these returned to record levels. Amid those price moves in late June, a Consumer Price Index (CPI) was released which showed inflation back slightly above 4% on a trailing 12-month basis. We saw a similar pattern for oil, gold, the Euro, and stock prices occur when oil raced from about \$90 to \$110 per barrel in February and March of this year.

During the first few years of this decade, oil traded in the \$20- to \$30-per-barrel range. On a weekly basis it broke above \$30 for the last time November 7, 2003. Since that date, the S&P 500 Index (large-cap), the S&P Mid-Cap 400 and the S&P Small-Cap 600 are up 32%, 55%, and 46% respectively. The last time the Euro only cost \$1.00 on a weekly basis was December 12, 2002. We think if investors knew back in 2002 and 2003 that oil was going from \$30 to \$140 per barrel, and that the dollar was going to lose over 55% of its value, they may have predicted a much worse situation than exists today for inflation, GDP, unemployment, corporate earnings, and interest rates. Currently, inflation is slightly above 4% and, as of last quarter, GDP was still growing. Unemployment is at 5.5%, which is still below levels seen in late 2002 and early 2003. Operating earnings per share for the S&P 500 companies grew by 86% from 2002 through 2007 and are predicted to be 10% higher for 2008. Interest rates are still quite moderate, with the six-month T-Bill yielding an annualized 2.2% and the 10-year government bond at slightly under 4%. We believe that all this put together suggests that the rise in the cost of oil and the devaluation of the dollar have not had the dire consequences some observers might have predicted.

Over the last five years, the stock market has had setbacks and sharp downturns in reaction to oil prices and the value of the dollar that have lasted only a month or two. While the volatility was unpleasant, it generally proved prudent and profitable to ride through those times. Stock prices bounced back as those dips proved to be overreactions as the movements of oil and currencies were not as economically damaging as initially feared. Given ICON's valuation readings and our belief that duration and depth of these oil- and currency-related dips are unpredictable, we have chosen the same strategy of riding through these volatile times. However, this time it is more difficult for the investor because the volatility has lasted longer (about six months so far) than in previous periods. It is also complicated by the sub-prime mortgage situation and floods that have damaged crops. In our opinion, these are short-term events that do not affect the long-term fundamentals.

As the market moved higher through mid-May, the potential industry and sector leadership picture improved, but the latest dip in the market has disrupted ICON's readings. Industry value/price and relative strength metrics are designed to identify one- to two-year themes. These metrics are not designed to capture themes that reverse every month or so. We expect that when the market breaks out of this range, we may have to do some rotation to get to favored industries. As you would expect when our market V/P ratio is 1.29, it is easy for us to find industries and stocks we believe are on sale. We will be looking for the right combination of value and strength that suggest to us the ability to lead the market for a year or more. In late June more industries in the Information Technology sector demonstrated those traits, so we increased exposure to that sector.

Bond Market Commentary

It is interesting that in a setting where investors worry about inflation due to oil and currencies, the yield on the 10-year government bond declined rather than increased in late June. We do not expect this is the beginning of a new bull market in bonds, but instead, as stated in the June commentary, we believe this is just one more phase of a sideways trading range.

International Market Commentary

Most foreign markets retreated in June, giving back much of their gains off the mid-March low. In fact, going back to last fall, we have seen that international markets have moved together. We always get skeptical when most country markets move in a synchronized manner. In our opinion, this suggests the moves are based on emotions rather than logic. Europe, for example, with a rising Euro has not experienced all the elements that bother U.S. investors, yet markets there have behaved very similarly to the U.S. market. If logic were ruling, it seems to us that European markets should behave very differently than those in the U.S., as they are facing a very different currency and oil setting due to the strength of the Euro.



The rollover in June had a similar affect to our international industry readings as we saw in the U.S. The leadership that appeared fairly clear in March and April faded. Based on value and what we saw in March and April, we think we know what the leadership will look like if there is a break-out to the upside, but we will be ready to rotate into new industries which look attractive.

Summary

In estimating intrinsic value for stocks, we like to differentiate between events that are short-term and those that cause a long-term, fundamental change. Oil, currencies, crops, and sub-prime problems all appear to us to be short-term. As such, they are not having much of an effect on our valuation calculations. Based on this, it appears to us that investors have overreacted.

Prepared by ICON's Investment Committee.

Past performance does not guarantee future results. Opinions and forecasts regarding sectors, industries, companies, countries and/or themes, and portfolio composition and holdings may differ significantly from the indexes and 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.

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ICON's value-based investing model is an analytical, quantitative approach to investing that employs various factors, including projected earnings growth estimates, 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 not guarantees of future results. Value investing involves risks and uncertainties and does not guarantee better performance or lower costs than other investment methodologies.

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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 the primary indicator of U.S. inflation and is used to make cost-of-living adjustments to billions of dollars in benefit payments.

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Sources: Bloomberg Finance, L.P., FactSet Research Systems, Inc.

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