Basic Materials 3 Underweight 4.0 -8.4 Moved to Underweight due to trade concerns, past peak global economic growth, and emerging market stresses. The sector had benefitted from synchronized global growth and rebounding commodity prices—despite the end of the commodity super-cycle and secular slowdown of Chinese economic growth. Favor packaging and diversified chemicals. Look for pullback opportunities in metals.

Consumer Discretionary 10 Favorably Neutral 2.8 10.0 Job and wage growth, advanced consumer deleveraging, pent-up housing demand, high optimism, and tax reform fiscal stimulus are sector positives. Fed tightening is a headwind. Favor value retailers and home-related due to favorable fundamentals and restaurants, hotels, and casinos for consumer experiences. Many names in this space benefit from tax reform.

Consumer Staples 7 Favorably Neutral 1.9 0.8 Favorably Neutral with healthy dividend and improving technicals. Pricing power for premium brands is being challenged by online and discount retailers, but steady growth and high dividends make this sector an appealing anchor. Favor select drug retailers, household product, and beverage companies.

Energy 5 Overweight -1.6 -6.2 Oil supply and demand are in better balance. Longer term, near inelastic demand growth from China and other emerging markets coupled with improved developed world growth should support the group. Favor quality: select major integrateds and refineries, select exploration & production, and select MLPs.

Financials 14 Neutral 2.8 -2.0 Moved to Neutral as yield curve continues to flatten. This group benefits from lower regulation, tax reform, and higher interest rates. A steady domestic environment, improving housing, lighter regulation, and lower corporate taxes remain positives for regional banks. Bank dividends are well supported by strong cash flow. Valuation is also favorable. Favor regional banks, capital markets, insurance, and consumer finance.

Health Care 16 Overweight 7.1 16.5 Our defensive sector Overweight. Favorable demographics and fewer uninsured should ensure that outlays for health care remain strong. Uncertainty around the future of the Affordable Care Act and drug prices remain a concern, especially for hospitals and pharmaceuticals. Favor medical devices, biotech, and managed care. Pharmaceuticals are core holdings but rising bond yields present a headwind for this bond surrogate industry.

Industrials 9 Underweight 3.8 -2.9 Moved to Underweight on trade concerns. The sector is benefiting from U.S. and global economic growth and pent-up demand for corporate capital expenditures. Sector is also a beneficiary of tax reform. However, structural emerging market weakness and the end of the commodity super-cycle remain concerns. Favor blue-chip conglomerates with above-market dividends, high quality transports, and Defense.

Information Technology 20 Favorably Neutral -1.9 8.9 Favorably Neutral. Information technology spending is growing as consumer tech spending remains strong and tech equipment investment rebounds. Many large cap technology companies are cash rich and look attractive on a dividend yield basis. Sector should benefit from tax reform and higher corporate capital expenditures. Favor software and internet services. We also view Semiconductors as a core holding.

Real Estate 3 Favorably Neutral 5.6 5.6 FavorablyNeutral. Fundamentals are decent but we are late in the cycle with capacity additions at a cyclical high; valuation remains full and rising interest rates present a potential headwind for this bond surrogate sector.

Communication Services 10 Favorably Neutral -0.6 -5.7 Favorably Neutral on this new sector, which replaces the bond surrogate Telecom sector with a growth-oriented, lower yielding sector. The sector has significant exposure to the advertising cycle and heavy concentration in two stocks that are taking significant advantage of the secular shift to online advertising. We are favorable on the sector’s business and consumer spending exposure but are Neutral due to heavy concentration in two names.

Utilities 3 Neutral 3.6 8.5 Moved to Neutral on this fixed income proxy with poor industry fundamentals and full valuation. Pricing power is hurt by low natural gas prices with independent power producers most impacted. Alternatives (solar) are hurting demand growth. Favor integrated electric utilities.

S&P 500 2.0 5.1 Performance figures are through 11/30/18. Sources: ISG, Morningstar Direct, Indata