

# HARRIS ASSOCIATES

## Beneath the Surface

September 2023

Many investors have been trepidatious when it comes to the positive market movement we have seen in 2023. Coming off a rocky, potentially oversold 2022 positive momentum made sense. However, given the global macroeconomic questions, investors speculated that stocks looked expensive through the first six months of this year. By digging deeper and employing our long-term valuation-based approach, there are still opportunities to be had.

The lack of market breadth was an important and relevant topic coming out of the second quarter as we discussed in great detail at the time. Five stocks contributed to 80% of the market's mid-teens return through June 30. That lack of diversity of positive contributors has been exacerbated through the end of the third quarter. Seven companies make up 84% of the market's year-to-date return as of September 30.

In terms of market capitalization, the S&P 500 has never been more concentrated than it is today. We highlighted that as of June 30, 20 names composed approximately 30% of the index. Fast forward three months: now the weight of the top 10 stocks is a shade under 32%. The momentum of the first six months continued through the next three—winners kept winning and losers kept losing.

### Weight of the top 10 stocks in the S&P 500

% of market capitalization of the S&P 500



Source: Nate Geraci, Bloomberg. Dates depicted 09/30/1996 to 9/30/2023.

The market's concentration in those top few names has driven that expensive appearance. When the financial press has implored that "stocks look expensive," that is a fair characterization when the S&P 500 was priced at 23x earnings, especially when you factor in current interest rate levels. Historically speaking, interest rates and P/E ratios have exhibited an inverse relationship: higher interest rates lead to lower P/E multiples for stocks. So, given the highest interest rates since before the global financial crisis, how could the S&P 500 support a P/E multiple in approximately the 65th percentile of its historical distribution?

As we have too often come to expect in the modern news cycle, it's important to dig past the headline. Looking back almost a decade paints an incredibly interesting picture relative to 2023.

Through the end of September, the S&P 500 was up 12%, which is a reasonable comparison to the 11% appreciation in 2014. Going deeper highlights the differences between the two periods. A few comparisons include that the median stock has appreciated 1% in 2023 versus 16.24% in 2014 and the equal-weighted S&P 500 has increased 0.58% this year compared to 12% in 2014. All this to say, there is a lot of value below the surface, and many of the technology names that have driven the market in 2023 look relatively expensive.

To be sure, there are some real concerns that have kept a weight on some portions of the market: macroeconomic and the ongoing geopolitical tensions. Many people express trepidation around the consumer and their spending abilities in the current environment. Given the consumer is approximately two-thirds of the economy, it is a reasonable concern.

We still do not know the impact of student loan repayments restarting in October. The pace of inflation has slowed but prices are still comparatively elevated. People are paying more at the pump and that has a large impact on the consumer psyche (positive or negative merits notwithstanding). For the first time ever, the U.S. surpassed \$1 trillion dollars in credit card debt. That's a headline number that would give anyone pause. But, if you look at it as a percent of total bank deposits, it is just 6% of total deposits; the lowest number in two decades. That could be a function of wealth inequality or people leveraging cash on hand to enjoy the rewards programs of their various credit cards.

Depending on your preferences, different macroeconomic variables can paint the user's preferred picture. The credit card debt anecdote above is a good example of leveraging interpretation to make two wholly different points. This is why we do our best to tune out the macroeconomic topics du jour and look at what a company's earnings power is in a "normal" environment. For example, we value automakers and auto parts suppliers on what a normal seasonally adjusted annual rate of production is; we value the oil and gas companies based on what we believe the long-term equilibrium oil price should be; we value our financials by normalizing interest rates; and so on across a variety of industries and companies.

All this is to say that a market index that has expensive headline P/E multiple driven by 10 names means there is plenty of value for us to discover. This is not to say all stocks are cheap or that fixed income alternatives have not become more attractive. To be clear, bonds have

become more attractive, and the risk/reward trade-off is an important topic to consider. But for clients concerned about their equity exposure, we believe the ability to capitalize on opportunity via active management has never been more important and present.

Gas prices will impact sentiment, inflation could increase demand for private label versus brand names when wandering through the grocery store, and the 2024 U.S. presidential race is likely to move markets one way or the other. Stock prices may fluctuate on whatever the news of the day is, while business values are generally much more stable, which gives investors a window of positivity for equities.

As always, we thank you for entrusting us with your investment assets and your continued support. Lastly, the best compliment we can receive is a referral from a satisfied client. We appreciate your referrals and handle them with the utmost care.

Thomas W. Delaney, CFA  
Portfolio Manager



Back Row: Zorica Zdravkovic, Tom Delaney, Andrew Gluck, Alix Havey, Ian Horvath, Clyde McGregor, Kate Feit, Alexander Cyrus  
Front Row: Mark Small, Kaylin Price, Michael Mangan, Emily Neumark

Past performance is no guarantee of future results. Current performance may be lower or higher than the performance data quoted. All returns reflect the reinvestment of dividends and capital gains and the deduction of transaction costs.

The specific securities identified and described in this report do not represent all the securities purchased, sold, or recommended to advisory clients. There is no assurance that any securities discussed herein will remain in an account's portfolio at the time one receives this report or that securities sold have not been repurchased. It should not be assumed that any of the securities, transactions, or holdings discussed herein were or will prove to be profitable.

The information, data, analyses, and opinions presented herein (including current investment themes, the portfolio managers' research and investment process, and portfolio characteristics) are for informational purposes only and represent the investments and views of the portfolio managers and Harris Associates L.P. as of the date written and are subject to change without notice. This content is not a recommendation of or an offer to buy or sell a security and is not warranted to be correct, complete or accurate. Certain comments herein are based on current expectations and are considered "forward-looking statements". These forward looking statements reflect assumptions and analyses made by the portfolio managers and Harris Associates L.P. based on their experience and perception of historical trends, current conditions, expected future developments, and other factors they believe are relevant. Actual future results are subject to a number of investment and other risks and may prove to be different from expectations. Readers are cautioned not to place undue reliance on the forward-looking statements.

The price to earnings ratio ("P/E") compares a company's current share price to its per-share earnings. It may also be known as the "price multiple" or "earnings multiple", and gives a general indication of how expensive or cheap a stock is. Investors should not base investment decisions on any single attribute or characteristic data point.

The S&P 500 Total Return Index is a float-adjusted, capitalization-weighted index of 500 U.S. large-capitalization stocks representing all major industries. It is a widely recognized index of broad, U.S. equity market performance. Returns reflect the reinvestment of dividends. This index is unmanaged and investors cannot invest directly in this index.

Investing in value stocks presents the risk that value stocks may fall out of favor with investors and underperform growth stocks during given periods.

Harris Associates L.P. does not provide tax or legal advice. Please consult with a tax or legal professional prior to making any investment decisions.

©2023 Harris Associates L.P. All rights reserved.

SCM-9595PWM-01/24

# Additional Notes

This material has been provided for information purposes only to investment service providers or other Professional Clients, Qualified or Institutional Investors and, when required by local regulation, only at their written request. This material must not be used with Retail Investors.

To obtain a summary of investor rights in the official language of your jurisdiction, please consult the legal documentation section of the website ([im.natixis.com/intl/intl-fund-documents](http://im.natixis.com/intl/intl-fund-documents))

**In the EU:** Provided by Natixis Investment Managers International or one of its branch offices listed below. Natixis Investment Managers International is a portfolio management company authorized by the Autorité des Marchés Financiers (French Financial Markets Authority - AMF) under no. GP 90-009, and a public limited company (société anonyme) registered in the Paris Trade and Companies Register under no. 329 450 738. Registered office: 43 avenue Pierre Mendès France, 75013 Paris. **Germany:** Natixis Investment Managers International, Zweigniederlassung Deutschland (Registration number: HRB 129507): Senckenberganlage 21, 60325 Frankfurt am Main. **Italy:** Natixis Investment Managers International Succursale Italiana, Registered office: Via San Clemente 1, 20122 Milan, Italy. **Netherlands:** Natixis Investment Managers International, Netherlands (Registration number 000050438298). Registered office: Stadsplateau 7, 3521AZ Utrecht, the Netherlands. **Spain:** Natixis Investment Managers International S.A., Sucursal en España, Serrano nº90, 6th Floor, 28006 Madrid, Spain. **Sweden:** Natixis Investment Managers International, Nordics Filial (Registration number 516412-8372- Swedish Companies Registration Office). Registered office: Covendrum Stockholm City AB, Kungsgatan 9, 111 43 Stockholm, Box 2376, 103 18 Stockholm, Sweden. **Or,**

Provided by Natixis Investment Managers S.A. or one of its branch offices listed below. Natixis Investment Managers S.A. is a Luxembourg management company that is authorized by the Commission de Surveillance du Secteur Financier and is incorporated under Luxembourg laws and registered under n. B 115843. Registered office of Natixis Investment Managers S.A.: 2, rue Jean Monnet, L-2180 Luxembourg, Grand Duchy of Luxembourg. **Belgium:** Natixis Investment Managers S.A., Belgian Branch, Gare Maritime, Rue Picard 7, Bte 100, 1000 Bruxelles, Belgium.

**In Switzerland:** Provided for information purposes only by Natixis Investment Managers, Switzerland Sàrl, Rue du Vieux Collège 10, 1204 Geneva, Switzerland or its representative office in Zurich, Schweizergasse 6, 8001 Zürich.

**In the British Isles:** Provided by Natixis Investment Managers UK Limited which is authorised and regulated by the UK Financial Conduct Authority (register no. 190258) - registered office: Natixis Investment Managers UK Limited, One Carter Lane, London, EC4V 5ER. When permitted, the distribution of this material is intended to be made to persons as described as follows: **in the United Kingdom:** this material is intended to be communicated to and/or directed at investment professionals and professional investors only; **in Ireland:** this material is intended to be communicated to and/or directed at professional investors only; **in Guernsey:** this material is intended to be communicated to and/or directed at professional services providers which hold a license from the Guernsey Financial Services Commission; **in Jersey:** this material is intended to be communicated to and/or directed at professional investors only; **in the Isle of Man:** this material is intended to be communicated to and/or directed at only financial services providers which hold a license from the Isle of Man Financial Services Authority or insurers authorised under section 8 of the Insurance Act 2008.

**In the DIFC:** Provided in and from the DIFC financial district by Natixis Investment Managers Middle East (DIFC Branch) which is regulated by the DFSA. Related financial products or services are only available to persons who have sufficient financial experience and understanding to participate in financial markets within the DIFC, and qualify as Professional Clients or Market Counterparties as defined by the DFSA. No other Person should act upon this material. Registered office: Unit L10-02, Level 10, ICD Brookfield Place, DIFC, PO Box 506752, Dubai, United Arab Emirates

**In Japan:** Provided by Natixis Investment Managers Japan Co., Ltd. Registration No.: Director-General of the Kanto Local Financial Bureau (kinsho) No.425. Content of Business: The Company conducts investment management business, investment advisory and agency business and Type II Financial Instruments Business as a Financial Instruments Business Operator.

**In Taiwan:** Provided by Natixis Investment Managers Securities Investment Consulting (Taipei) Co., Ltd., a Securities Investment Consulting Enterprise regulated by the Financial Supervisory Commission of the R.O.C. Registered address: 34F., No. 68, Sec. 5, Zhongxiao East Road, Xinyi Dist., Taipei City 11065, Taiwan (R.O.C.), license number 2020 FSC SICE No. 025, Tel. +886 2 8789 2788.

**In Singapore:** Provided by Natixis Investment Managers Singapore Limited (NIM Singapore) having office at 5 Shenton Way, #22-05/06, UIC Building, Singapore 068808 (Company Registration No. 199801044D) to distributors and qualified investors for information purpose only. NIM Singapore is regulated by the Monetary Authority of Singapore under a Capital Markets Services Licence to conduct fund management activities and is an exempt financial adviser. Mirova Division (Business Name Registration No.: 53431077W) and Ostrum Division (Business Name Registration No.: 53463468X) are part of NIM Singapore and are not separate legal entities. This advertisement or publication has not been reviewed by the Monetary Authority of Singapore.

**In Hong Kong:** Provided by Natixis Investment Managers Hong Kong Limited to professional investors for information purpose only.

**In Australia:** Provided by Natixis Investment Managers Australia Pty Limited (ABN60 088 786 289) (AFSL No. 246830) and is intended for the general information of financial advisers and wholesale clients only.

**In New Zealand:** This document is intended for the general information of New Zealand wholesale investors only and does not constitute financial advice. This is not a regulated offer for the purposes of the Financial Markets Conduct Act 2013 (FMCA) and is only available to New Zealand investors who have certified that they meet the requirements in the FMCA for wholesale investors. Natixis Investment Managers Australia Pty Limited is not a registered financial service provider in New Zealand.

**In Colombia:** Provided by Natixis Investment Managers International Oficina de Representación (Colombia) to professional clients for informational purposes only as permitted under Decree 2555 of 2010. Any products, services or investments referred to herein are rendered exclusively outside of Colombia. This material does not constitute a public offering in Colombia and is addressed to less than 100 specifically identified investors.

**In Latin America:** Provided by Natixis Investment Managers International.

**In Uruguay:** Provided by Natixis Investment Managers Uruguay S.A., a duly registered investment advisor, authorised and supervised by the Central Bank of Uruguay. Office: San Lucar 1491, Montevideo, Uruguay, CP 11500. The sale or offer of any units of a fund qualifies as a private placement pursuant to section 2 of Uruguayan law 18,627.

**In Mexico:** Provided by Natixis IM Mexico, S. de R.L. de C.V., which is not a regulated financial entity, securities intermediary, or an investment manager in terms of the Mexican Securities Market Law (Ley del Mercado de Valores) and is not registered with the Comisión Nacional Bancaria y de Valores (CNBV) or any other Mexican authority. Any products, services or investments referred to herein that require authorization or license are rendered exclusively outside of Mexico. While shares of certain ETFs may be listed in the Sistema Internacional de Cotizaciones (SIC), such listing does not represent a public offering of securities in Mexico, and therefore the accuracy of this information has not been confirmed by the CNBV. Natixis Investment Managers is an entity organized under the laws of France and is not authorized by or registered with the CNBV or any other Mexican authority. Any reference contained herein to "Investment Managers" is made to Natixis Investment Managers and/or any of its investment management subsidiaries, which are also not authorized by or registered with the CNBV or any other Mexican authority.

**In Brazil:** Provided to a specific identified investment professional for information purposes only by Natixis Investment Managers International. This communication cannot be distributed other than to the identified addressee. Further, this communication should not be construed as a public offer of any securities or any related financial instruments. Natixis Investment Managers International is a portfolio management company authorized by the Autorité des Marchés Financiers (French Financial Markets Authority - AMF) under no. GP 90-009, and a public limited company (société anonyme) registered in the Paris Trade and Companies Register under no. 329 450 738. Registered office: 43 avenue Pierre Mendès France, 75013 Paris.

The above referenced entities are business development units of Natixis Investment Managers, the holding company of a diverse line-up of specialised investment management and distribution entities worldwide. The investment management subsidiaries of Natixis Investment Managers conduct any regulated activities only in and from the jurisdictions in which they are licensed or authorized. Their services and the products they manage are not available to all investors in all jurisdictions. It is the responsibility of each investment service provider to ensure that the offering or sale of fund shares or third party investment services to its clients complies with the relevant national law.

The provision of this material and/or reference to specific securities, sectors, or markets within this material does not constitute investment advice, or a recommendation or an offer to buy or to sell any security, or an offer of any regulated financial activity. Investors should consider the investment objectives, risks and expenses of any investment carefully before investing. The analyses, opinions, and certain of the investment themes and processes referenced herein represent the views of the portfolio manager(s) as of the date indicated. These, as well as the portfolio holdings and characteristics shown, are subject to change. There can be no assurance that developments will transpire as may be forecasted in this material. The analyses and opinions expressed by external third parties are independent and does not necessarily reflect those of Natixis Investment Managers. Past performance information presented is not indicative of future performance.

Although Natixis Investment Managers believes the information provided in this material to be reliable, including that from third party sources, it does not guarantee the accuracy, adequacy, or completeness of such information. This material may not be distributed, published, or reproduced, in whole or in part.

All amounts shown are expressed in USD unless otherwise indicated.

Natixis Investment Managers may decide to terminate its marketing arrangements for this product in accordance with the relevant legislation