

Most Attractive Stocks for August 2014

20 Large/Mid Cap and 20 Small Cap Stocks

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- **Figure 1 shows 10 new stocks that make our August lists.**
- **FREE Company Valuation Reports for 2 of the new stocks are in the Free Archive on our website.**
- **The Most Attractive Stocks portfolio (-5.2%) underperformed the S&P 500 (-2.2%) last month.**
- **Figure 4 shows the 12 stocks that outperformed from July's report.**
- **See Appendix C for data on returns, volatility and portfolio turnover for our Most Attractive Stocks Portfolio.**
- **Most Attractive Stocks have high and rising returns on capital (ROIC) and low market expectations for future profits.**
- **Barron's recently highlighted our stock-picking as amongst the best of all Wall Street firms. See our website for details.**

Figure 1: Additions for August

Large Cap Additions		Small Cap Additions	
Ticker	Company Name	Ticker	Company Name
CHKP	Check Point Software Technologies	ATRI	Atrion Corporation
CI	Cigna Corporation	FF	FutureFuel Corp
MENT	Mentor Graphics Corp	KMPR	Kemper Corporation
NTAP	NetApp, Inc.	RWT	Redwood Trust, Inc.
		TAX	Liberty Tax, Inc.
		WRLD	World Acceptance Corp

Sources: New Constructs, LLC

Please see Appendix B for explanations of additions and deletions to the large and small cap lists.

The 20 Most Attractive Large/Mid Cap Stocks for August

We recommend that investors equal-weight holdings in all 20 Large/Mid Cap Most Attractive Stocks.

Figure 2: 20 Most Attractive Large/Mid Cap Stocks for August

Ticker	Company Name	High-Quality Earnings			Cheap Valuation			Market Value (\$mm)	
		As of Last Fiscal Year			as of 07/31/14				
		Positive Economic EPS	Rising ROIC (% point increase)	High-Ranking ROIC (by Quintile)	Positive Free Cash Flow Yield	Low Price-to-Economic Book Value	Short Market-Implied GAP (years)		
1	VR	Validus Holdings, Ltd.	\$2.52	2%	2nd	18%	0.4	Less than 1	\$3,316
2	TRV	The Travelers Companies, Inc.	\$3.91	4%	2nd	12%	0.6	Less than 1	\$30,365
3	NLY	Annaly Capital Management	\$3.01	13%	Top Quintile	12%	0.2	Less than 1	\$10,517
4	NTAP*	NetApp Inc.	\$1.69	15%	Top Quintile	11%	1.1	5	\$12,565
5	AHL	Aspen Insurance Holdings, Ltd.	\$0.78	1%	3rd	10%	0.7	Less than 1	\$2,618
6	CB	The Chubb Corp	\$5.19	6%	Top Quintile	9%	0.7	Less than 1	\$21,199
7	ALL	The Allstate Corp	\$2.67	1%	2nd	8%	0.7	Less than 1	\$25,367
8	CHKP*	Check Point Software Technologies	\$2.94	39%	Top Quintile	7%	1.2	4	\$13,049
9	NUS	Nu Skin Enterprises, Inc.	\$5.17	16%	Top Quintile	7%	0.8	Less than 1	\$3,460
10	PGR	The Progressive Corp	\$1.28	5%	Top Quintile	7%	0.9	Less than 1	\$13,877
11	F	Ford Motor Company	\$0.20	1%	3rd	7%	1.0	Less than 1	\$67,301
12	PETM	PetSmart Inc.	\$2.80	1%	Top Quintile	6%	1.2	4	\$6,760
13	VMI	Valmont Industries, Inc.	\$6.10	2%	Top Quintile	5%	1.2	8	\$3,915
14	TRW	TRW Automotive Holdings	\$3.62	1%	Top Quintile	5%	1.2	6	\$11,330
15	DOX	Amdocs Ltd.	\$1.27	1%	2nd	5%	1.0	Less than 1	\$7,254
16	DFS	Discover Financial Services	\$2.43	1%	Top Quintile	5%	1.2	5	\$28,471
17	AXS	Axis Capital Holdings, Ltd.	\$1.31	2%	3rd	4%	0.7	Less than 1	\$4,650
18	MENT*	Mentor Graphics Corp	\$0.63	1%	2nd	4%	1.1	2	\$2,250
19	RE	Everest Re Group, Ltd.	\$14.70	6%	Top Quintile	3%	0.4	Less than 1	\$7,189
20	CI*	Cigna Corporation	\$3.09	2%	2nd	3%	1.2	1	\$24,189

* Addition to the Large/Mid Cap Most Attractive list in August

Most Attractive Stocks are Ranked by Free Cash Flow Yield in Descending Order

Sources: New Constructs, LLC

The 20 Most Attractive Small Cap Stocks for August

We recommend that investors equal-weight holdings in all 20 Small Cap Most Attractive Stocks.

Figure 3: 20 Most Attractive Small Cap Stocks for August

Rank	Ticker	Company Name	High-Quality Earnings			Cheap Valuation			Market Value (\$mm)
			As of Last Fiscal Year			as of 07/31/14			
			Positive Economic EPS	Rising ROIC (% point increase)	High-Ranking ROIC (by Quintile)	Positive Free Cash Flow Yield	Low Price-to-Economic Book Value	Short Market-Implied GAP (years)	
1	MTEX	Mannatech Inc.	\$1.40	23%	Top Quintile	34%	0.4	Less than 1	\$33
2	IQNT	Inteliquent Inc	\$0.76	12%	Top Quintile	26%	0.7	Less than 1	\$344
3	EMCI	EMC Insurance Group, Inc.	\$0.95	1%	2nd	24%	0.7	Less than 1	\$396
4	WRLD*	World Acceptance Corp	\$7.00	3%	Top Quintile	18%	0.6	Less than 1	\$804
5	REGI	Renewable Energy Group	\$4.25	26%	Top Quintile	12%	0.2	Less than 1	\$434
6	CTCM	CTC Media, Inc.	\$0.39	1%	Top Quintile	10%	0.8	Less than 1	\$1,506
7	JBSS	John B. Sanfilippo & Son, Inc.	\$0.67	1%	3rd	10%	1.0	3	\$292
8	KMPR*	Kemper Corporation	\$1.00	7%	2nd	10%	0.8	9	\$1,915
9	USNA	USANA Health Sciences, Inc.	\$4.71	7%	Top Quintile	9%	0.9	Less than 1	\$889
10	UVE	Universal Insurance Holdings	\$1.29	15%	Top Quintile	9%	0.6	Less than 1	\$427
11	ODC	Oil-Dri Corporation Of America	\$0.93	4%	2nd	9%	1.1	7	\$191
12	MOFG	MidwestOne Financial Group	\$0.67	1%	3rd	7%	0.6	Less than 1	\$199
13	FF*	FutureFuel Corp	\$0.86	14%	Top Quintile	7%	1.0	6	\$683
14	OFG	OFG Bancorp	\$0.96	5%	2nd	6%	0.7	Less than 1	\$718
15	NRCIB	National Research Corporation	\$1.56	2%	Top Quintile	6%	1.3	3	\$276
16	TAX*	Liberty Tax, Inc.	\$1.23	1%	Top Quintile	5%	1.2	Less than 1	\$440
17	EXLS	ExlService Holdings, Inc.	\$0.87	1%	Top Quintile	5%	1.1	4	\$917
18	RWT*	Redwood Trust, Inc.	\$1.19	5%	Top Quintile	5%	0.7	Less than 1	\$1,575
19	ATRI*	Atrion Corporation	\$8.30	2%	Top Quintile	5%	1.5	9	\$553
20	RLI	RLI Corporation	\$1.61	3%	Top Quintile	4%	1.2	3	\$1,837

* Addition to the Small Cap Most Attractive list in August

Most Attractive Stocks are Ranked by Free Cash Flow Yield in Descending Order

Sources: New Constructs, LLC

Most Attractive Stocks: Monthly Updates

The Most Attractive Stocks portfolio (-5.2%) underperformed the S&P 500 (-2.2%) last month. 12 stocks from our July Most Attractive Large Cap and Small Cap lists outperformed the S&P 500, and 6 stocks had positive returns. See Figure 4 for details. For updates on the performance of all of last month's Most Attractive stocks, see Appendix A. We measure our July performance based on closing prices from July 02, 2014 to July 31, 2014. We published last month's report to subscribers on July 02, 2014 and to the general public, for purchase, on July 09, 2014.

Figure 4: 12 Stocks that Outperformed From July's Report

Large Cap			Small Cap		
Ticker	Company Name	Change From 07/02/14	Ticker	Company Name	Change From 07/02/14
PETM	Petsmart Inc.	13.9%	NSR	Neustar Inc.	5.9%
TRW	TRW Automotive Holdings	13.7%	NRCIB	National Research Corporation	4.0%
SYMC	Symantec Corporation	4.1%	MTEX	Mannatech Inc.	2.8%
ALL	The Allstate Corp	-0.9%	NNI	Nelnet Inc.	-1.0%
NLY	Annaly Capital Management	-1.0%	STRT	Strattec Security Corp	-1.4%
F	Ford Motor Company	-1.2%	REGI	Renewable Energy Group	-1.7%
S&P 500	S&P 500	-2.2%	S&P 500	S&P 500	-2.2%

Sources: New Constructs, LLC

Note: Gain/Decline performance analysis excludes transaction costs and dividends.

Most Attractive Stocks: Methodology

Stocks make our Most Attractive list because they have:

1. **High-Quality Earnings** based on:
 - a. Returns on Invested Capital that are rising; and
 - b. Economic Earnings/Cash Flows that are positive.

AND

2. **Cheap Valuations** based on:
 - a. *Free-Cash Flow Yields*¹ that are positive;
 - b. *Price-to-Economic Book Value (EBV)*² ratios that are relatively low; and
 - c. *Growth Appreciation Periods*³ (GAP) that are relatively low.

Only stocks that earn an Overall Rating of Very Attractive are allowed on our Most Attractive Stocks lists.

The above characteristics also qualify stocks for a 'Very Attractive' or 'Attractive' Rating, according to our Risk/Reward Rating system. Figure 4 shows our Risk/Reward Rating analysis, which we apply to the 3000+ companies that we cover. Stocks get a grade of 1 to 5 for each criterion, 5 being the worst and 1 being the best score. The Overall score is based on the average score of all five criteria. Stocks must get an average score of 1.4 or below to be rated Very Attractive. For the most part, only Very Attractive stocks qualify for our Most Attractive Stocks lists.

Figure 5: New Constructs Risk/Reward Rating for Stocks

Overall Risk/Reward Rating	Quality of Earnings		Valuation		
	Economic vs Reported EPS	Return on Invested Capital (ROIC)	FCF Yield	Price-to-EBV Ratio	Growth Appreciation Period (yrs)
Very Dangerous	Misleading Trend	Bottom Quintile	<-5%	> 3.5 or <-1 > 0	> 50
Dangerous	False Positive	4th Quintile	-5%<-1%	2.4 > 3.5 or <-1	20 > 50
Neutral	Neutral EP	3rd Quintile	-1%<3%	1.6 > 2.4	10 > 20
Attractive	Positive EP	2nd Quintile	3%<10%	1.1 > 1.6	3 > 10
Very Attractive	Rising EP	Top Quintile	>10%	0 > 1.1	0 > 3

Sources: New Constructs, LLC

¹ Free-Cash Flow Yields measure the % of the total value of the firm for which the Free Cash Flows of the firm account. The formula is FCF/Current Enterprise Value.

² Economic Book Value (EBV) measures the no-growth value of the business based on its annual after-tax cash flow. The Formula for EBV is: (NOPAT / WACC) + Excess Cash + Non-operating assets – Debt (incl. Operating Leases) - Value of Outstanding Stock Options – Minority Interests.

³ Growth Appreciation Period measures the number of years, implied by the market-price, that a company will grow its economic earnings. This measure assigns a numerical value to the width of the moat around a firm's business.

Explanation of Risk/Reward Rating System

Our Risk/Reward Rating System assigns a rating to every stock under our coverage according to what we believe are the 5 most important criteria for assessing the risk versus reward of stocks. See table that follows for details.

Overall Risk/Reward Ranking	The Overall Risk/Reward Ranking provides a final rating based on the equal-weighted average rating of each criterion.
Very Dangerous	FCF Yield is not included in the average.
Dangerous	FCF Yield is not included in the average.
Neutral	All criteria are equal-weighted in the average calculation.
Attractive	All criteria are equal-weighted in the average calculation.
Very Attractive	All criteria are equal-weighted in the average calculation.

Economic vs Reported EPS	Rates stocks based on how their Economic Earnings compare to their Reported Earnings. Values based on Latest Fiscal Year.
Very Dangerous	Negative and declining Economic Earnings despite positive and rising Reported Earnings
Dangerous	Same as above except Reported Earnings are not rising or Reported Earnings are not positive
Neutral	Negative Economic and Reported Earnings
Attractive	Economic Earnings are positive
Very Attractive	Economic Earnings are positive and rising

Return on Invested Capital (ROIC)	Rates stocks based on their ROIC. Values based on Latest Fiscal Year.
Bottom Quintile	Very Dangerous = the bottom 20% of Russell 1000 companies
4th Quintile	Dangerous = the bottom 40% of Russell 1000 companies
3rd Quintile	Neutral = the middle 20% of Russell 1000 companies
2nd Quintile	Attractive = the top 40% of Russell 1000 companies
Top Quintile	Very Attractive = the top 20% of Russell 1000 companies

FCF Yield	Rates stocks based on their Free Cash Flow Yield. Values based on Latest Closing Stock price and Latest Fiscal Year.
<-5%	Very Dangerous = less than or equal to -5%
-5%<-1%	Dangerous = more than -5% but less than or equal to -1%
-1%<3%	Neutral = more than -1% but less than or equal to +3%
3%<10%	Attractive = more than +3% but less than or equal to +10%
>10%	Very Attractive = more than +10%

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Price-to-EBV Ratio	Rates stocks based on their Price-to-Economic Book Value Ratio. Values based on Latest Closing Stock price and Latest Fiscal Year.
>3.5 or -1>0	Very Dangerous = greater than or equal to 3.5 or less than 0 but greater than -1
2.4>3.5 or <-1	Dangerous = greater than or equal to 2.4 but less than 3.5 and less than or equal to -1
1.6>2.4	Neutral = greater than or equal to 1.6 but less than 2.4
1.1>1.6	Attractive = greater than or equal to 1.1 but less than 1.6
0>1.1	Very Attractive = greater than or equal to 0 but less than 1.1

Growth Appreciation Period (yrs)	Rates stocks based on their Market-Implied Growth Appreciation Period. Values based on Latest Closing Stock price and Default Forecast Scenario.
>50	Very Dangerous = greater than or equal to 50 years
20>50	Dangerous = at least 20 years but less than 50
10>20	Neutral = at least 10 years but less than 20
3>10	Attractive = at least 3 years but less than 10
0>3	Very Attractive = at least 0 years but less than 3

Appendix A – Performance of Stocks on July’s Report

Figure 6: Performance of All Stocks From July’s Report

Large Cap			Small Cap		
Ticker	Company Name	Change From 07/02/14	Ticker	Company Name	Change From 07/02/14
PETM	PetSmart Inc.	13.9%	NSR	Neustar Inc.	5.9%
TRW	TRW Automotive Holdings	13.7%	NRCIB	National Research Corporation	4.0%
SYMC	Symantec Corporation	4.1%	MTEX	Mannatech Inc.	2.8%
ALL	The Allstate Corp	-0.9%	NNI	Nelnet Inc.	-1.0%
NLY	Annaly Capital Management	-1.0%	STRT	Strattec Security Corp	-1.4%
F	Ford Motor Company	-1.2%	REGI	Renewable Energy Group	-1.7%
SPX	S&P 500	-2.2%	SPX	S&P 500	-2.2%
DOX	Amdocs Ltd.	-2.5%	JBSS	John B. Sanfilippo & Son, Inc.	-2.9%
RE	Everest Re Group, Ltd.	-2.7%	MOFG	MidwestOne Financial Group	-3.6%
DFS	Discover Financial Services	-2.8%	ODC	Oil-Dri Corporation Of America	-5.2%
AXS	Axis Capital Holdings, Ltd.	-3.1%	OB	OneBeacon Insurance Group	-6.0%
TRV	The Travelers Companies, Inc.	-5.3%	EXLS	ExlService Holdings, Inc.	-6.8%
VR	Validus Holdings, Ltd.	-5.5%	RLI	RLI Corporation	-6.9%
VMI	Valmont Industries, Inc.	-5.5%	UVE	Universal Insurance Holdings	-6.9%
BEN	Franklin Resources Inc	-5.9%	TMP	Tompkins Financial Corp	-7.4%
CB	The Chubb Corp	-6.1%	EMCI	EMC Insurance Group, Inc.	-9.5%
AGO	Assured Guaranty, Ltd.	-6.3%	OFG	OFG Bancorp	-13.3%
PGR	The Progressive Corp	-7.0%	CTCM	CTC Media, Inc.	-14.3%
AHL	Aspen Insurance Holdings, Ltd.	-11.8%	RGR	Sturm Ruger & Company	-16.2%
XLNX	Xilinx Inc.	-15.7%	USNA	USANA Health Sciences, Inc.	-19.0%
NUS	Nu Skin Enterprises, Inc.	-18.9%	IQNT	Inteliquent Inc	-26.6%
Large Cap Portfolio Return		-3.5%	Small Cap Portfolio Return		-6.8%
Combo (Large and Small Cap) Return			-5.2%		

Sources: New Constructs, LLC

Note: Gain/Decline performance analysis excludes transaction costs and dividends.

Appendix B – Additions and Deletions

Most Attractive Large/Mid Cap Stocks

Deletions:

- SYMC - Stock price increased 4.1% since July report.
- AGO - Displaced by improved rank of other stocks.
- BEN - Displaced by improved rank of other stocks.
- XLNX - Displaced by improved rank of other stocks.

Additions:

- MENT - Stock price decreased 9.7% since July report.
- CI - Stock price decreased 3.0% since July report.
- CHKP - Addition by decrease in rank of other stocks.
- NTAP - Addition by decrease in rank of other stocks.

Most Attractive Small Cap Stocks

Deletions:

- NSR - Stock price increased 5.9% since July report.
- NNI - Displaced by improved rank of other stocks.
- OB - Displaced by improved rank of other stocks.
- RGR - Displaced by improved rank of other stocks.
- STRT - Displaced by improved rank of other stocks.
- TMP - Displaced by improved rank of other stocks.

Additions:

- ATRI - Stock price decreased 13.0% since July report.
- FF - Stock price decreased 7.4% since July report.
- RWT - Stock price decreased 5.5% since July report.
- KMPR - Stock price decreased 5.2% since July report.
- TAX - Addition by decrease in rank of other stocks.
- WRLD - Addition by decrease in rank of other stocks.

Appendix C – Portfolio Metrics

Figure 7: Performance and Risk Metrics

Portfolio	Portfolio Returns			Volatility (Annualized)			Sharpe Ratio			Beta		
	1 year annualized	3 year annualized	Since Inception	1 year annualized	3 year annualized	Since Inception	1 Year	3 Year	Since Inception	1 Year Average	3 Year Average	Average Since Inception
Most Attractive Large	26%	15%	10%	14%	16%	21%	1.9	0.9	0.5	1.0	0.9	1.0
Most Attractive Small	29%	12%	10%	13%	20%	26%	2.2	0.6	0.4	0.95	0.95	0.94
Most Attractive Small and Large	28%	14%	10%	12%	18%	23%	2.3	0.8	0.5	0.96	0.94	0.96
S&P 500	22%	14%	6%	12%	13%	17%	1.9	1.0	0.3			
Russell 2000	21%	13%	7%	17%	20%	22%	1.2	0.6	0.3			

Source: New Constructs, LLC

Figure 8: Portfolio Turnover

Portfolio	Monthly Turnover		
	1 Year Average	3 Year Average	Average Since Inception
Most Attractive Large	38%	30%	28%
Most Attractive Small	39%	31%	29%
Most Attractive Small and Large	39%	31%	28%

Source: New Constructs, LLC

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1. Based on the complete set of financial information available.
2. Standard for all companies.
3. A more accurate representation of the true underlying cash flows of the business.

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