ETF & Mutual Fund Rankings: Large Cap Value Style

The Large Cap Value style ranks first out of the twelve fund styles as detailed in our 2Q16 Style Ratings for ETFs and Mutual Funds report. Last quarter, the Large Cap Value style ranked second. It gets our Attractive rating, which is based on aggregation of ratings of 47 ETFs and 906 mutual funds in the Large Cap Value style as of April 29, 2016. See a recap of our 1Q16 Style Ratings here.

Figures 1 and 2 show the five best and worst rated ETFs and mutual funds in the style. Not all Large Cap Value style ETFs and mutual funds are created the same. The number of holdings varies widely (from 17 to 1020). This variation creates drastically different investment implications and, therefore, ratings.

Investors seeking exposure to the Large Cap Value style should buy one of the Attractive-or-better rated ETFs or mutual funds from Figures 1 and 2.

Figure 1: ETFs with the Best & Worst Ratings – Top 5

	Allocation of ETF Holdings			
Ticker	Attractive-or-better Stocks	Neutral Stocks	Dangerous-or-worse Stocks	Predictive Rating
Best ETFs				
WBIF	41%	42%	0%	Very Attractive
WBIG	30%	45%	4%	Very Attractive
QDF	38%	37%	21%	Very Attractive
QDEF	39%	37%	21%	Very Attractive
IOO	23%	30%	17%	Very Attractive
Worst ETFs				
DVY	17%	31%	50%	Neutral
SDOG	32%	33%	33%	Neutral
PEY	20%	37%	43%	Dangerous
FDL	26%	22%	52%	Dangerous
RDIV	23%	17%	57%	Dangerous

* Best ETFs exclude ETFs with TNAs less than $100 million for inadequate liquidity.

Sources: New Constructs, LLC and company filings

First Trust NASDAQ Rising Dividend Achievers ETF (RDVY) and FlexShares Quality Dividend Dynamic Index Fund (QDYN) are excluded from Figure 1 because their total net assets (TNA) are below $100 million and do not meet our liquidity minimums.

Figure 2: Mutual Funds with the Best & Worst Ratings – Top 5

	Allocation of Mutual Fund Holdings			
Ticker	**Attractive-or-better Stocks**	**Neutral Stocks**	**Dangerous-or-worse Stocks**	**Predictive Rating**
Best Mutual Funds				
KDHIX	42%	43%	14%	Very Attractive
KDHSX	42%	43%	14%	Very Attractive
KDHTX	42%	43%	14%	Very Attractive
WILCX	43%	23%	30%	Very Attractive
FMIEX	43%	23%	30%	Very Attractive
Worst Mutual Funds				
CDGRX	18%	39%	19%	Very Dangerous
CFJIX	30%	37%	28%	Very Dangerous
GHTCX	11%	5%	60%	Very Dangerous
SIMFX	11%	17%	34%	Very Dangerous
GHTAX	11%	5%	60%	Very Dangerous

* Best mutual funds exclude funds with TNAs less than $100 million for inadequate liquidity.

Sources: New Constructs, LLC and company filings

TS&W Equity Portfolio (TSWEX), Legg Mason BW Dynamic Large Cap Value (LMBGX, LMBEX), and Aston/Cornerstone Large Cap Value Fund (AAVIX) are excluded from Figure 2 because their total net assets (TNA) are below $100 million and do not meet our liquidity minimums.

Absolute Shares WBI Tactical LCV Shares (WBIF) is the top-rated Large Cap Value ETF and Deutsche CROCI Equity Dividend Fund (KDHIX) is the top-rated Large Cap Value mutual fund. Both earn a Very Attractive rating.

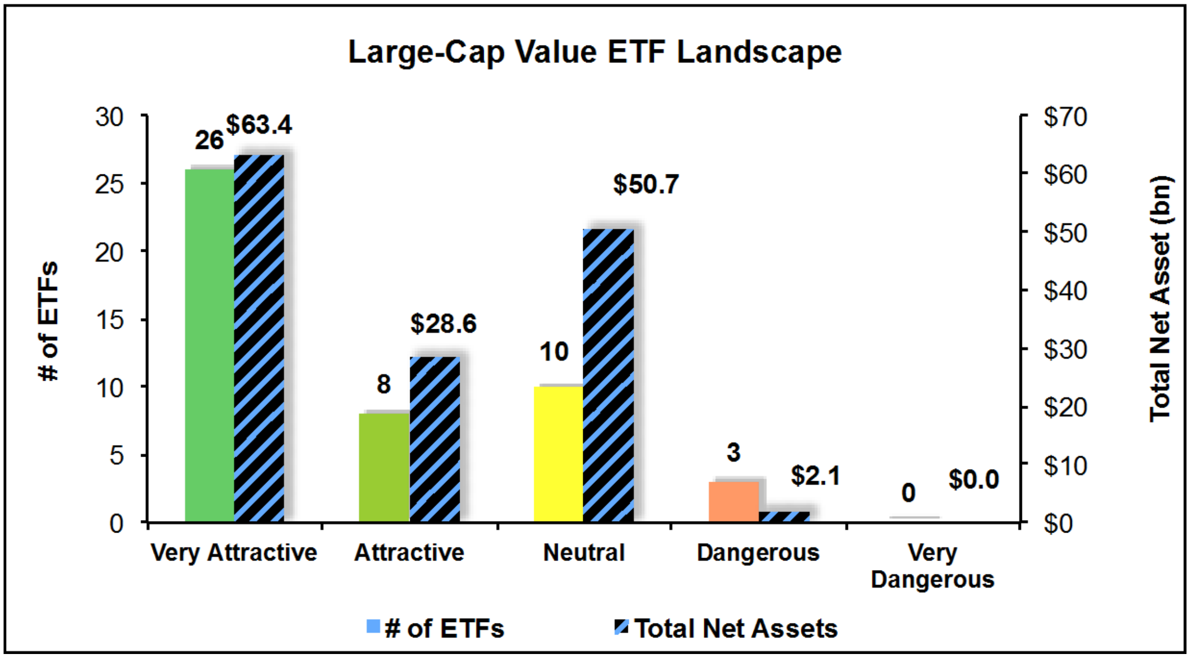
Oppenheimer Ultra Dividend Revenue ETF (RDIV) is the worst rated Large Cap Value ETF and Good Harbor Tactical Equity Income Fund (GHTAX) is the worst rated Large Cap Value mutual fund. RDIV earns a Dangerous rating and GHTAX earns a Very Dangerous rating.

The Progressive Corp (PGR: $33/share) is one of our favorite stocks held by WBIF and earns an Attractive rating. Since 1998, Progressive has grown after-tax profit (NOPAT) by 6% compounded annually. The company consistently earns a double-digit return on invested capital (ROIC) and currently earns a top-quintile 19%. Progressive has also generated a cumulative $3.9 billion in free cash flow over the past five years. Despite the long-term track record, PGR still presents a buying opportunity for true value investors. At its current price of $33/share, PGR has a price-to-economic book value (PEBV) ratio of 1.1. This ratio means that the market expects Progressive's NOPAT to only increase by 10% over its remaining corporate life. If Progressive can grow NOPAT by just 5% compounded annually over the next decade, the stock is worth $46/share today – a 39% upside.

CenturyLink ($31/share) remains one of our least favorite stocks held by RDIV and earns a Dangerous rating. CenturyLink was placed in the Danger Zone in February 2015. CenturyLink has failed to generate positive economic earnings in any year of our model, which dates back to 1998. Even worse, over the past decade, CTL's economic earnings have declined from -$152 million to -$1.2 billion. CenturyLink has never earned a ROIC above 7% and currently earns a bottom-quintile 4%. Despite over a decade of value destruction, CTL is still priced for significant growth. To justify its current price of $31/share, CenturyLink must grow NOPAT by 10% compounded annually for the next 11 years. These expectations seem overly optimistic and leave CTL with significant downside risk.

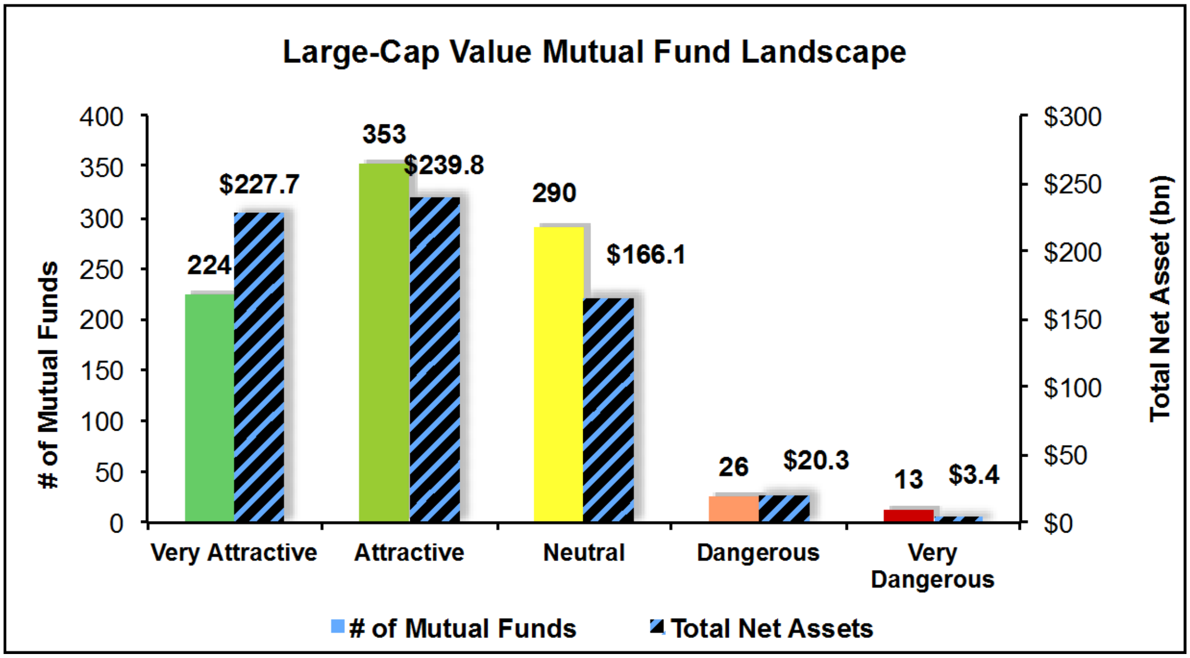
Figures 3 and 4 show the rating landscape of all Large Cap Value ETFs and mutual funds.

Figure 3: Separating the Best ETFs From the Worst Funds



Sources: New Constructs, LLC and company filings

Figure 4: Separating the Best Mutual Funds From the Worst Funds



Sources: New Constructs, LLC and company filings

Disclosure: David Trainer and Kyle Guske II receive no compensation to write about any specific stock, style, or theme.

New Constructs® – Profile

How New Constructs Creates Value for Clients

We find it. You benefit. Cutting-edge technology enables us to scale our forensic accounting expertise across 3000+ stocks. We shine a light in the dark corners of SEC filings so our clients can make safer, more informed decisions.
Our stock rating methodology instantly informs you of the quality of the business and the fairness of the stock's valuation. We do the diligence on earnings quality and valuation so you don't have to.

In-depth risk/reward analysis underpins our ratings. Our rating methodology grades every stock, ETF, and mutual fund according to what we believe are the 5 most important criteria for assessing the quality of an equity. Each grade reflects the balance of potential risk and reward of buying that equity. Our analysis results in the 5 ratings described below. Very Attractive and Attractive correspond to a "Buy" rating, Very Dangerous and Dangerous correspond to a "Sell" rating, while Neutral corresponds to a "Hold" rating.

QUESTION: Why shouldn't fund research be as good as stock research? Why should fund investors rely on backward-looking price trends?
ANSWER: They should not.

Don't judge a fund by its cover. Take a look inside at its holdings and understand the quality of earnings and valuation of the stocks it holds. We enable you to choose the best fund based on its stock-picking merits so you do not have to rely solely on backward-looking technical metrics.

The drivers of our forward-looking fund ratings are Portfolio Management (i.e. the aggregated ratings of its holdings) and Total Annual Costs. The Total Annual Costs Rating (details here) captures the all-in cost of being in a fund over a 3-year holding period, the average period for all fund investors.

Our Philosophy About Research

Accounting data is not designed for equity investors, but for debt investors. Accounting data must be translated into economic earnings to understand the profitability and valuation relevant to equity investors. Respected investors (e.g. Adam Smith, Warren Buffett and Ben Graham) have repeatedly emphasized that accounting results should not be used to value stocks. Economic earnings are what matter because they are:

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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