ETF & Mutual Fund Rankings: Mid Cap Growth Style

The Mid Cap Growth style ranks eighth out of the twelve fund styles as detailed in our 3Q16 Style Ratings for ETFs and Mutual Funds report. Last quarter, the Mid Cap Growth style ranked ninth. It gets our Neutral rating, which is based on aggregation of ratings of 10 ETFs and 370 mutual funds in the Mid Cap Growth style as of August 4, 2016. See a recap of our 2Q16 Style Ratings here.

Figure 1 ranks from best to worst the nine Mid-Cap growth ETFs that meet our liquidity standards and Figure 2 shows the five best and worst-rated Mid-Cap growth mutual funds. Not all Mid Cap Growth style ETFs and mutual funds are created the same. The number of holdings varies widely (from 20 to 2280). This variation creates drastically different investment implications and, therefore, ratings.

Investors seeking exposure to the Mid Cap Growth 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 (only 4)				
BFOR	28%	44%	17%	Very Attractive
MDYG	12%	45%	39%	Attractive
IVOG	12%	45%	39%	Attractive
IJK	12%	45%	39%	Attractive
Worst ETFs				
VOT	11%	34%	51%	Neutral
PXMG	6%	39%	48%	Neutral
FNY	8%	32%	51%	Neutral
JKH	6%	37%	50%	Neutral
DWAQ	10%	53%	33%	Neutral

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

Sources: New Constructs, LLC and company filings

Validea Market Legends ETF (VALX) is excluded from Figure 1 because its 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				
FUQIX	18%	68%	9%	Very Attractive
IMIDX	19%	60%	15%	Very Attractive
CMIDX	19%	60%	15%	Very Attractive
MCMFX	19%	46%	24%	Attractive
EISMX	8%	58%	21%	Attractive
Worst Mutual Funds				
TAAGX	5%	29%	45%	Very Dangerous
ALMAX	7%	28%	45%	Very Dangerous
ETAGX	10%	16%	51%	Very Dangerous
HSOAX	3%	33%	45%	Very Dangerous
TWNAX	5%	28%	44%	Very Dangerous

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

Sources: New Constructs, LLC and company filings

Barron's 400 ETF (BFOR) is the top-rated Mid Cap Growth ETF and Fidelity SAI US Quality Index Fund (FUQIX) is the top-rated Mid Cap Growth mutual fund. Both earn a Very Attractive rating.

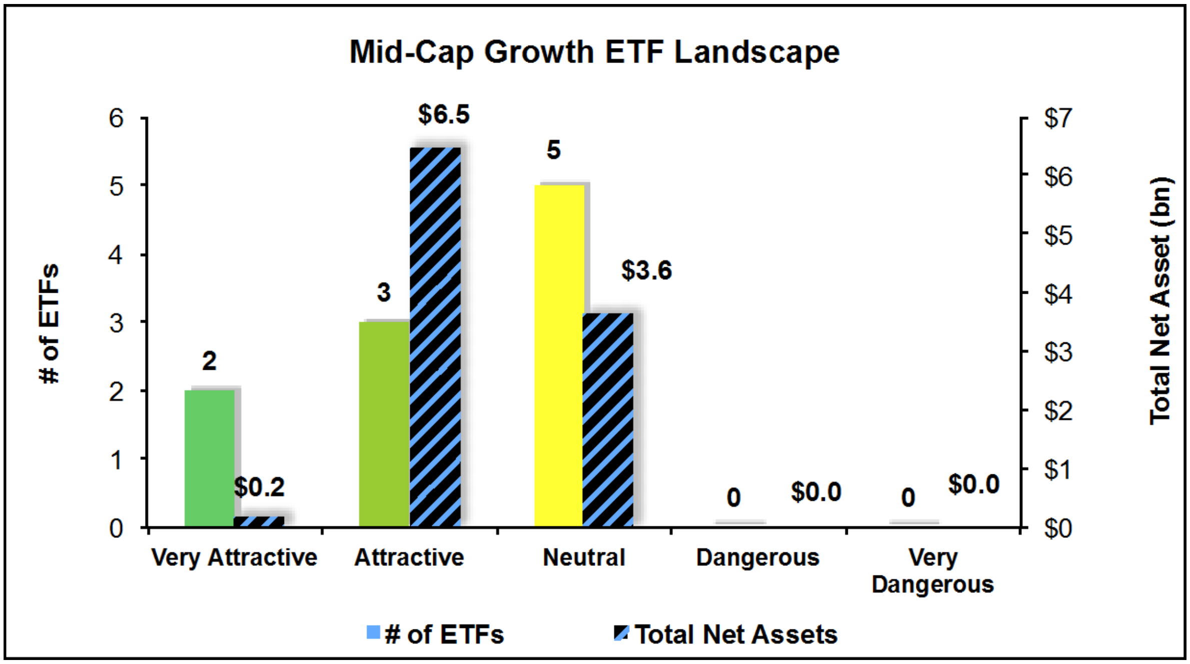
DWA NASDAQ Momentum Portfolio (DWAQ) is the worst rated Mid Cap Growth ETF and New Opportunities Fund (TWNAX) is the worst rated Mid Cap Growth mutual fund. DWAQ earns a Neutral rating and TWNAX earns a Very Dangerous rating.

LegacyTexas Financial Group Inc. (LTXB: $28/share) is one of our favorite stocks held by BFOR and earns an Attractive rating. Since 2006, LegacyTexas has grown after-tax profit (NOPAT) by 37% compounded annually. LTXB has improved its return on invested capital (ROIC) from 2% in 2006 to 11% during the last twelve months. Despite the impressive improvement in fundamentals, LTXB is still undervalued. At its current price of $28/share, LTXB has a price-to-economic book value (PEBV) ratio of 1.1. This ratio means that the market expects LTXB's NOPAT to grow by only 10% from current levels. If LegacyTexas can grow NOPAT by just 9% compounded annually for the next decade, the stock is worth $37/share today – a 32% upside.

CoStar Group (CSGP: $205) is one of our least favorite stocks held by HSOAX and earns a Dangerous rating. Since 2011, CoStar's NOPAT has declined by 15% compounded annually. Costar's ROIC has fallen from 11% in 2011 to a bottom-quintile 4% over the last twelve months. Worst of all, in 15 of the last 18 years, CoStar Group has generated negative economic earnings. Given the poor fundamentals, CSGP is overvalued. To justify its current price of $205/share, CSGP must grow NOPAT by 34% compounded annually for the next 16 years. Such high expectations seem overly optimistic given the profit decline at CSGP. Moreover, few, if any, firms throughout history have grown profits by nearly 30% for two decades. These high expectations baked into CSGP make it one to avoid.

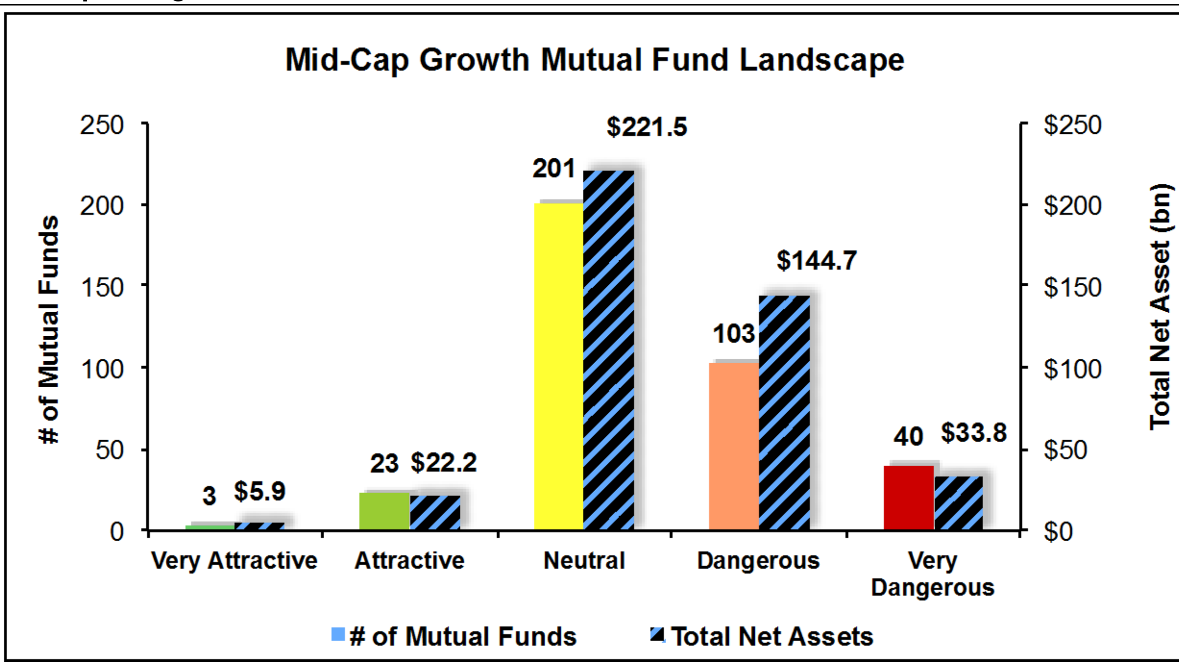
Figures 3 and 4 show the rating landscape of all Mid Cap Growth ETFs and mutual funds.

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

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Disclosure: David Trainer and Kyle Martone 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.

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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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