# Featured Stocks in November's Most Attractive/Most Dangerous Model Portfolios

**Recap From October's Picks**

Our Most Attractive Stocks (-1.3%) outperformed the S&P 500 (-3.2%) from October 7, 2020 through November 2, 2020 by 1.9%. The best performing large cap stock gained 12% and the best performing small cap stock was up 21%. Overall, 25 out of the 40 Most Attractive stocks outperformed the S&P 500.

Our Most Dangerous Stocks (-0.5%) underperformed the S&P 500 (-3.2%) as a short portfolio from October 7, 2020 through November 2, 2020 by 2.7%. The best performing large cap stock fell by 14% and the best performing small cap stock fell by 17%. Overall, 14 out of the 35 Most Dangerous stocks outperformed the S&P 500 as shorts.

The Most Attractive/Most Dangerous Model Portfolios underperformed as an equal-weighted long/short portfolio by 0.4%.

Get the best fundamental research

Only our research utilizes the superior data and earnings adjustments featured by the HBS & MIT Sloan paper, "Core Earnings: New Data and Evidence." The successes of these model portfolios highlight the value of our machine learning and AI Robo-Analyst technology[1], which helps clients fulfill the fiduciary duty of care and make smarter investments[2].

18 new stocks make our Most Attractive list this month, and one new stock falls onto the Most Dangerous list this month. November's Most Attractive and Most Dangerous stocks were made available to members on November 4, 2020.

Our Most Attractive stocks have high and rising returns on invested capital (ROIC) and low price to economic book value ratios. Most Dangerous stocks have misleading earnings and long growth appreciation periods implied by their market valuations.

## Most Attractive Stocks Feature for November: Intel Corporation (INTC: $46/share)

Intel Corporation (INTC), is the featured stock from November's Most Attractive Stocks Model Portfolio.

We recently made Intel a Long Idea in August 2020 and while the stock is down 7% (vs. S&P 500 up 6%) since then, INTC still offers excellent risk/reward.

Intel has grown revenue by 7% compounded annually and net operating profit after-tax (NOPAT) by 15% compounded annually over the past three years. Longer term, the firm has grown NOPAT by 11% compounded annually over the past decade.

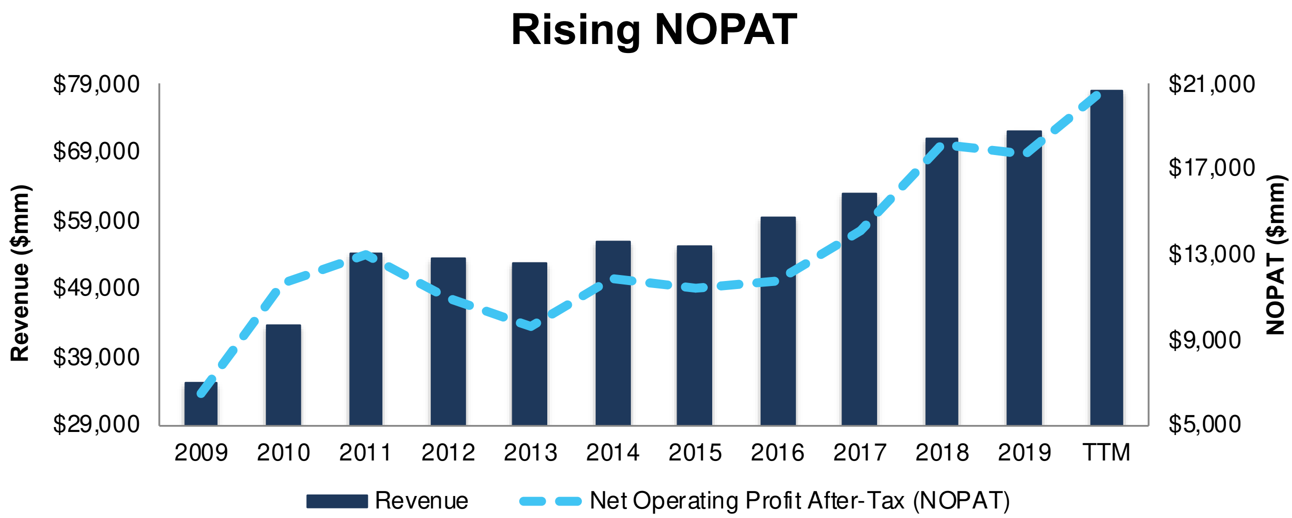
Intel's NOPAT margin increased from 20% in 2016 to 27% over the trailing-twelve-months (TTM) while its ROIC improved from 15% in 2016 to 18% TTM.

[1] Harvard Business School features the powerful impact of our research automation technology in the case New Constructs: Disrupting Fundamental Analysis with Robo-Analysts.
[2] This paper compares our analytics on a mega cap company to Bloomberg and Capital IQ (SPGI) in a detailed appendix.



Important Disclosure Information is contained on the last page of this report.
The recipient of this report is directed to read these disclosures.

**Figure 1: Revenue & NOPAT Since 2009**




Sources: New Constructs, LLC and company filings

### INTC Is Undervalued

At its current price of $46/share, INTC has a price-to-economic book value (PEBV) ratio of 0.6. This ratio means the market expects Intel's NOPAT to permanently decline by 40%. This expectation seems overly pessimistic for a firm that grew NOPAT by 5% compounded annually over the past two decades.

Even if Intel's NOPAT margin falls to 22% (10-year average, compared to 27% TTM) and the firm grows NOPAT by just 2% compounded annually for the next decade, the stock is worth $63/share today – a 37% upside. See the math behind this reverse DCF scenario.

### Critical Details Found in Financial Filings by Our Robo-Analyst Technology

As investors focus more on fundamental research, research automation technology is needed to analyze all the critical financial details in financial filings as shown in the Harvard Business School and MIT Sloan paper, "Core Earnings: New Data and Evidence".

Below are specifics on the adjustments we make based on Robo-Analyst findings in Intel's 10-K and 10-Q's:

Income Statement: we made $5.4 billion of adjustments, with a net effect of removing $3.2 billion in non-operating income (4% of revenue). You can see all the adjustments made to Intel's income statement here.

Balance Sheet: we made $43 billion of adjustments to calculate invested capital with a net decrease of $4 billion. One of the largest adjustments was $8.8 billion in asset write-downs. This adjustment represented 8% of reported net assets. You can see all the adjustments made to Intel's balance sheet here.

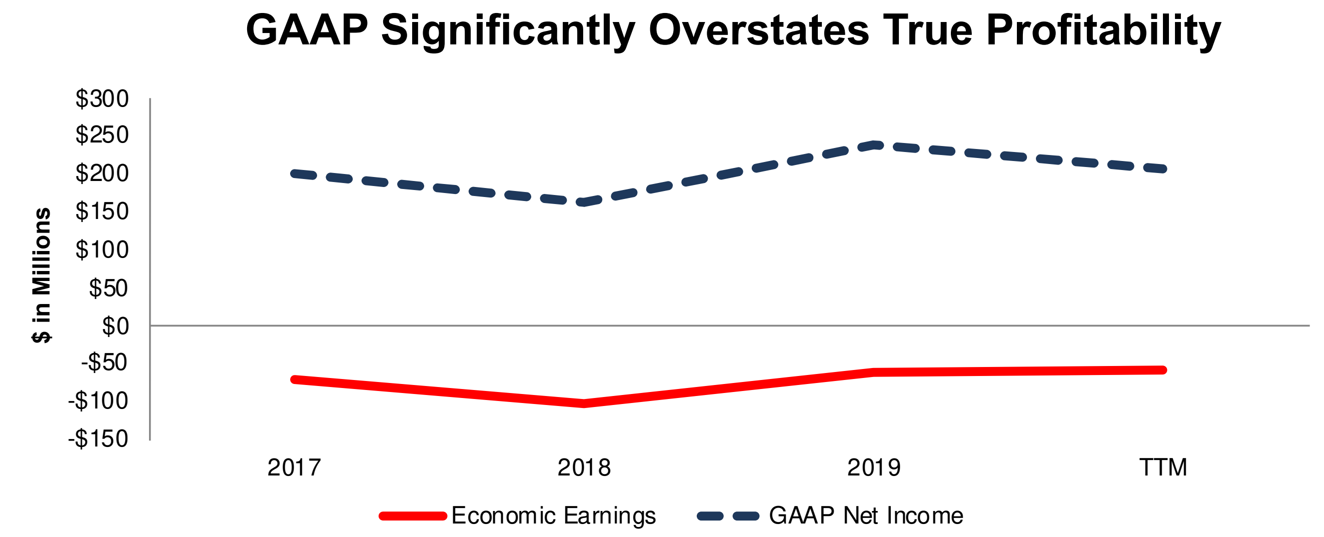
Valuation: we made $63.8 billion of adjustments with a net effect of decreasing shareholder value by $17.6 billion. Apart from total debt, the most notable adjustment to shareholder value was $23 billion in excess cash. This adjustment represents 12% of Intel's market cap. See all adjustments to Intel's valuation here.

## Most Dangerous Stocks Feature: First Industrial Realty Trust, Inc. (FR: $43/share)

First Industrial Realty Trust, Inc. (FR) is the featured stock from November's Most Dangerous Stocks Model Portfolio.

While First Industrial's GAAP net income improved from $46 million in 2014 to $208 TTM, the firm's economic earnings, the true cash flows of the business, remain negative and improved at a much slower pace, per Figure 2. The firm's NOPAT margin fell from 41% in 2019 to 36% TTM and ROIC fell from 6% to a bottom-quintile 5% over the same time.

**Figure 2: GAAP Net Income vs. Economic Earnings**




Sources: New Constructs, LLC and company filings

### FR Provides Poor Risk/Reward

Despite its poor fundamentals, FR is still priced for significant profit growth and is overvalued.

To justify its current price of $43/share, First Industrial must achieve a 47% NOPAT margin (highest since 2002, compared to 36% TTM) and grow NOPAT by 11% compounded annually over the next decade. See the math behind this reverse DCF scenario. This expectation seems overly optimistic given that First Industrial's NOPAT over the past two decades has fallen by 1% compounded annually.

Even if First Industrial can maintain its TTM NOPAT margin of 36% and grow NOPAT by 8% compounded annually for the next 10 years, the stock is worth just $24/share today, a 44% downside to the current stock price. See the math behind this reverse DCF scenario.

Each of these scenarios also assumes First Industrial is able to grow revenue, NOPAT, and FCF without increasing working capital or fixed assets. This assumption is unlikely, but allows us to create best-case scenarios that demonstrate how high expectations embedded in the current valuation are. For reference, First Industrial's invested capital has grown by an average of $169 million (40% of 2019 revenue) per year since 2015.

### Critical Details Found in Financial Filings by Our Robo-Analyst Technology

As investors focus more on fundamental research, research automation technology is needed to analyze all the critical financial details in financial filings as shown in the Harvard Business School and MIT Sloan paper, "Core Earnings: New Data and Evidence".

Below are specifics on the adjustments we make based on Robo-Analyst findings in First Industrial's 10-K and 10-Q's:

Income Statement: we made $188 million of adjustments, with a net effect of removing $62 million in in non-operating income (14% of revenue). You can see all the adjustments made to First Industrial's income statement here.

Balance Sheet: we made $221 million of adjustments to calculate invested capital with a net decrease of $10 million. One of the largest adjustments was $74 million for midyear acquisitions. This adjustment represented 2% of reported net assets. You can see all the adjustments made to First Industrial's balance sheet here.

Valuation: we made $1.9 billion of adjustments with a net effect of decreasing shareholder value by $1.6 billion. Apart from total debt, the most notable adjustment to shareholder value was $43 million in minority interests. This adjustment represents 1% of First Industrial's market cap. See all adjustments to First Industrial's valuation here.

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

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## *Footnotes adjustments matter. We are the ONLY source.*

We provide ratings, models, reports & screeners on U.S. 3,000 stocks, 700 ETFs and 7,000 mutual funds.

**HBS & MIT Sloan research reveals that:**

- **Markets are inefficiently assessing earnings because no one reads the footnotes.**
- **Corporate managers hide gains/losses in footnotes to manage earnings.**
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Combining human expertise with NLP/ML/AI technologies (featured by Harvard Business School), we shine a light in the dark corners (e.g. footnotes) of hundreds of thousands of financial filings to unearth critical details.

The HBS & MIT Sloan paper, Core Earnings: New Data and Evidence, shows how our superior data drives uniquely comprehensive and independent debt and equity research.

This paper compares our analytics on a mega cap company to other major providers. The Appendix details exactly how we stack up.

***Learn more.***

Quotes from HBS & MIT Sloan professors on our research:

### *Get better research:*

*"…the NC dataset provides a novel opportunity to study the properties of non-operating items disclosed in 10-Ks, and to examine the extent to which the market impounds their implications."* – page 20

### *Pick better stocks:*

*"Trading strategies that exploit cross-sectional differences in firms' transitory earnings produce abnormal returns of 7-to-10% per year." – Abstract*

### *Avoid losses from using other firms' data:*

*"…many of the income-statement-relevant quantitative disclosures collected by NC do not appear to be easily identifiable in Compustat…" – page 14*

### *Build better models:*

*"Core Earnings [calculated using New Constructs' novel dataset] provides predictive power for various measures of one-year-ahead performance…that is incremental to their current-period counterparts." – page 4*

### *Exploit market inefficiencies:*

*"These results … suggest that the adjustments made by analysts and Compustat to better capture core earnings are incomplete. Moreover, the non-core items identified by NC produce a measure of core earnings that is incremental to alternative measures of operating performance in predicting an array of future income measures." – page 26*

### *Fulfill fiduciary duties:*

*"An appropriate measure of accounting performance for purposes of forecasting future performance requires detailed analysis of all quantitative performance disclosures detailed in the annual report, including those reported only in the footnotes and in the MD&A." – page 33-34*

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