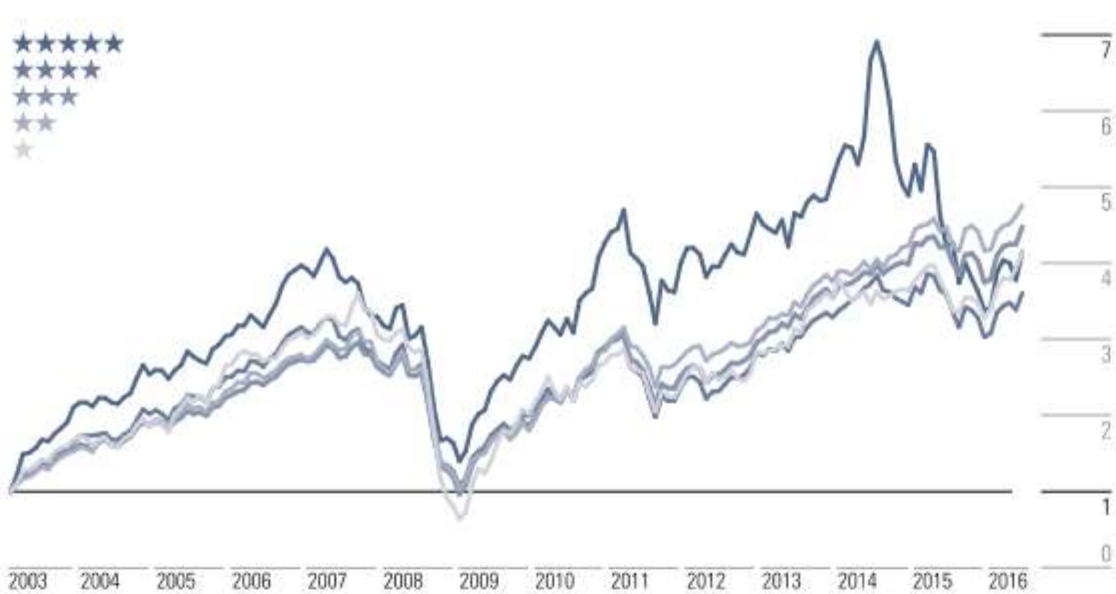
Valuentum's Turn

On Tuesday we received a copy of Valuentum's latest Best Ideas Newsletter from one of our DIYers. While we had previously written about Valuentum's Quantitative approach and their misleading method of calculating relative performance, it was prior to our Website's launch. Before starting Valuentum, Brian Nelson, CFA claims to have created Morningstar's stock rating model, which is based on DCF. From Investopedia: "Discounted cash flow (DCF) is a valuation method" that uses "future free cash flow projections and discounts them ... to arrive at present value estimates." On December 5, 2016 Morningstar published a study "Analyzing the Performance of our Stock Recommendations". Exhibit 3 from the Executive Summary shows the results when "we constructed equal weighted portfolios based on a stock's star rating (5 being the best) at the beginning of each month."

Exhibit 3 Aggregate Portfolio Returns by Star Rating



Source: Morningstar

So in an effort to build a better mouse trap Nelson latches on to the well established synergistic benefit of combining Value and Momentum. However, the Value Factor has nothing to do with DCF, and screening for stocks that meet both Value and Momentum criteria that do work isn't the best way to combine these two Factors anyway. From our website: "As both Value and Momentum have withstood the rigors of academic scrutiny, why not combine the two into a kind of super factor? Alpha Architects has studied this strategy, and found that while both value and momentum belong in a portfolio, they work best separately, not as a single factor. "The evidence suggests that a value and momentum system, which combines both pure value and pure momentum into a single portfolio, may prevent a value-only investor or a momentum-only investor from suffering through extended, long-term stretches of poor performance."... At HCM, we follow these findings and see allocations to both Value and Momentum as essential to any account dedicated to Capital Appreciation."

What we first noticed from Valuentum's latest issue is that their relative performance claims were missing. Digging into their archived issues, we discovered that the last time they were prominently featured was last June:

OUR BEST IDEAS NEWSLETTER

Valuentum Securities

Stock Analysis: From Value through Momentum Investing

January 15, 2018
Volume 8 Issue 1

Valuentum Securities Inc.
www.valuentum.com info@valuentum.com

The Best Ideas Portfolio (see page 8): AAPL, MO, BRK-B, CSCO, CVS, DG, FB, GM, GILD, GOOG, GOOGL, XLV, INTC, JNJ, PYPL, PCLN, SDY, UNP, XLE,VRNT, V

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OUR BEST IDEAS NEWSLETTER

Valuentum Securities

Stock Analysis: From Value through Momentum Investing

June 15, 2017
Volume 7 Issue 6

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Portfolio Return	Benchmark Return	Outperformance
130.7%	100.4%	30.3pts

See page 8.

The Best Ideas Portfolio (see page 8): AAPL, MO, BWLD, BRK-B, CSCO, CVS, DG, FB, GM, GOOG, GOOGL, XLV, INTC, JNJ, PYPL, PCLN, SDY, UNP, XLE, XLU, VRNT, V

I Care
By Brian Nelson, CFA

INSIDE THIS ISSUE

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Now, as mentioned above, we have previously written about how this deceptive comparison is calculated. As can be seen below, Valuentum's Portfolio had a cumulative Return of 149.1% from May 17, 2011 to December 15, 2017. The tiny print under the last column's % Return reads "(Dividends included)". That is fine, unless the benchmark you compare against, in this case the S&P 500, doesn't include dividends. Now, note that as of December 15th Valuentum's portfolio had 28.7% cash. That was also fine. As Burton G. Malkiel, the renowned emeritus professor of economics at Princeton and author of the 1973 classic "A Random Walk Down Wall Street: The Time-Tested Strategy for Successful Investing", recently stated: **"Nobody can consistently time the market, and those who try it usually fail."** What isn't fine is to futher lower the S&P 500's return by the average cash held by your portfolio, 8.4%.

Nelson has decided to abandon a model portfolio approach for a "list-and-weighting format" as also detailed on Page 8 of this month's issue shown below. If we go by weighting, his best idea is to hold 5%-30% of your portfolio in Cash. He is also recommending that up to 10% of your portfolio be hed in each of 3 stocks (BRK-B, FB, and V), and a further 8% in Google. According to a January 16, 2017 paper by ASU professor Hendrik Bessembinder: "Most common stocks do not outperform Treasury Bills. Fifty eight percent of common stocks have holding period returns less than those on one-month Treasuries over their full lifetimes on CRSP. When stated in terms of lifetime dollar wealth creation, the entire gain in the U.S. stock market since 1926 is attributable to the best-performing four percent of listed stocks. ... The results also help to explain why active

Simulated Best Ideas Newsletter Portfolio

New for 2018! See page 9.

By Valuentum Analysts

SIMULATED BEST IDEAS PORTFOLIO -- as of December 15, 2017											Best Ideas Portfolio Inception Date: May 17, 2011			
Portfolio Holdings	Symbol	Initial VBI*	Current VBI**	Fair Value	P/FV	First Purchase	Cost/Shr ($)	# Shares	Total Cost ($)	Price/Shr ($)	Current Value ($)	Cumulative Div's Rec'd	% of Portfolio	% Return (dividends included)
Bullish														
Apple Corp.	AAPL	10	7	$199.00	0.87	17-Jun-11	51.92	54	2,817.63	173.97	9,394.38	1,380.65	3.8%	282.4%
Altria Group	MO	8	6	$58.00	1.24	28-Jun-11	28.39	78	2,228.73	71.67	5,590.26	2,621.41	2.2%	268.4%
Berkshire Hathaway	BRK-B	6	6	$183.00	1.08	20-Apr-16	146.13	69	10,089.97	197.78	13,646.82		5.5%	35.3%
Cisco	CSCO	9	7	$42.00	0.91	14-Nov-14	26.33	221	5,831.87	38.19	8,439.99	525.11	3.4%	53.7%
CVS Health	CVS	9	4	$88.00	0.83	6-Jan-17	81.84	79	6,472.36	73.08	5,773.32	158.00	2.3%	-8.4%
Dollar General	DG	4	7	$89.00	1.02	13-Apr-17	68.83	50	3,448.50	90.93	4,546.50	26.00	1.8%	32.6%
Energy Select SPDR	XLE	NR	NR	NA	NMF	6-Oct-15	67.14	143	9,608.02	68.72	9,826.96	568.61	3.9%	8.2%
Facebook	FB	6	7	$219.00	0.82	29-Jan-16	136.15	92	12,539.34	180.18	16,576.56		6.7%	32.2%
General Motors	GM	6	7	$43.00	0.95	26-Aug-16	31.65	132	4,184.80	40.95	5,405.40	250.80	2.2%	35.2%
Gilead Sciences	GILD	7	7	$109.00	0.69	31-Jul-17	76.32	61	4,662.52	75.57	4,609.77	63.44	1.9%	0.2%
Google - Class C	GOOG	10	6	$1147.00	0.93	23-Oct-12	450.92	7	3,170.42	1064.19	7,449.33	10.35	3.0%	135.3%
Google - Class A	GOOGL	10	6	$1147.00	0.93	4-Apr-14	Split	7	Split	1072.00	7,504.00		3.0%	+++
Health Care ETF	XLV	NR	NR	NA	NMF	22-May-12	36.60	125	4,582.00	83.70	10,462.50	640.49	4.2%	142.3%
Intel	INTC	6	5	$48.00	0.93	12-Sep-11	20.48	150	3,086.50	44.56	6,684.00	796.35	2.7%	142.4%
Johnson & Johnson	JNJ	6	7	$130.00	1.10	29-Jan-16	104.18	54	5,632.72	142.46	7,692.84	349.38	3.1%	42.8%
PayPal	PYPL	NR	6	$58.00	1.30	17-Jul-15	Spin-off	100	Split	75.65	7,565.00		3.0%	+++
Priceline	PCLN	10	3	$2018.00	0.87	26-Feb-15	1239.49	3	3,732.46	1760.00	5,280.00		2.1%	41.5%
SPDR S&P Dividend ETF	SDY	NR	NR	NA	NMF	20-Apr-16	81.33	124	10,091.92	93.77	11,627.48	379.37	4.7%	19.0%
Utilities Select SPDR	XLU	NR	NR	NA	NMF	18-Mar-14	41.12	83	3,419.96	55.02	4,566.66	469.85	1.8%	47.3%
Verint Systems	VRNT	6	6	$50.00	0.84	13-Apr-17	38.95	87	3,395.65	41.85	3,640.95		1.8%	7.2%
Visa	V	7	6	$91.00	1.25	30-Nov-11	26.86	188	5,064.39	113.82	21,398.16	492.41	8.6%	332.2%
Latest changes: Removed UNP (8/18), Halved AAPL (8/18), Halved PCLN (8/18).														
Cash -- changes in monthly cash balance reflects dividends received and trading gains/losses, where applicable.											71386.23		28.7%	0.0%
Bearish														
For investors seeking 'short' or 'put option' exposure, please consider firms with VBI ratings with 1 and 2 as ideas.														
Best Ideas Portfolio Value								Original -->	100,000.00	Current -->	**249,067.11**			**149.1%**
S&P 500 Index (SPY)						17-May-11	132.69	754	100,000.00	266.51	200,851.61	18,471.20	91.6%	
Cash											18,471.20		8.4%	
Benchmark Portfolio Value											**219,322.81**			**119.3%**
Relative Outperformance														**29.7 pts**

Data as of December 15, 2017. The cost basis of positions includes commissions. The Best Ideas Newsletter portfolio's performance includes dividends received, but not interest received on cash balances. The Best Ideas Newsletter portfolio is not a real money portfolio. The 'Benchmark Portfolio Value' reflects dividends received and held as cash.

* VBI rating at the time we added the firm to the portfolio.

** See our methodology regarding the Valuentum Buying Index (VBI). Best Ideas portfolio is not a real money portfolio.

strategies, which tend to be poorly diversified, most often underperform." In contrast, HCM establishes 2% positions at most in individual stocks, and trims them back once they reach 4% of a portfolio, being sure to hold at least a year in taxable accounts.

Other questions abound. Why would you recommend buying a stock that is trading above your Fair Value estimate? Seven of the 16 recommended stocks have a P/FV of 102% to 139%. In contrast, HCM will sell a stock once it becomes fully valued, again taking tax considerations into account on timing.

Next comes his VBI rating, which ranges from 1(Worst) to 10 (Best). This rating is supposedly the whole point of his Quantitative System of combining Value with Momentum, and yet he is recommending a 3 (PCLN) and a 4 (CVS) rated stock. In contrast, HCM doesn't buy a stock unless it meets all of our criteria, which includes Insider Buying. That is why we use Transitional Funds, building a portfolio's individual stock positions over time.

Valuentum's Best Ideas

By Valuentum Analysts

Note: This edition of this newsletter, the January 2018 edition, features ideas in list-and-weighting format, as announced several months ago.

Study: Valuentum released a new study on its fair value estimates! Please download the paper at the following link: https://www.valuentum.com/downloads/20171031/download

Why the Simulated Newsletter Portfolio Format Changes?

We're constantly improving at Valuentum and incorporating members' suggestions as we go.

What we have found from members' feedback is that a meaningful percentage of subscribers are having a different experience than what is reflected in the newsletters. For example, many have not been excited about our Visa (V) and Apple (AAPL), and Johnson & Johnson (JNJ) and Intel (INTC) ideas, the top two respective weightings in each simulated newsletter portfolio, respectively. Many may not have known that these had been our favorite ideas either.

In some cases, what we've found is that the showcasing of the measurements is not helping our readership as much as we previously thought. Because of this and incorporating feedback, we believe we needed to make a change to a different presentation style--one that makes it easier to find our best ideas--so we've opted for the list-and-weighting format, as shown in the table below. We think this makes the most sense, too, as it gets our favorite ideas at the top.

We also continue to conduct extensive studies on our research methodologies. Pasted below, for example, are links to two of the most recent papers we've put together on our calculated fair value estimates and Valuentum Buying Index ratings, respectively. These ratings are included in each company's 16-page reports and are a core part of our product offering. Both of these papers were written in 2017:

Fair Value Estimates (pdf): https://www.valuentum.com/downloads/20171031/download

Valuentum Buying Index ratings:
https://www.valuentum.com/articles/Value_and_Momentum_Within_Stocks_Too

Valuentum's BEST IDEAS -- as of January 15, 2018

Portfolio Holdings	Symbol	Div Yield %	Fair Value	Economic Castle	VBI Rating	P/FV	Last Close	% of Portfolio
Berkshire Hathaway	BRK-B	0.00%	$183.00	NA	6	1.15	210.16	5.5%-10%
Facebook	FB	0.00%	$238.00	Very Attractive	7	0.75	179.37	5.5%-10%
Visa	V	0.65%	$91.00	Attractive	6	1.32	120.09	5.5%-10%
Apple Corp.	AAPL	1.42%	$203.00	Highest Rated	6	0.87	177.09	4%-5.5%
SPDR S&P Dividend ETF	SDY	3.21%	NA	NA	UR	NMF	95.72	4%-5.5%
Energy Select SPDR	XLE	3.04%	NA	NA	UR	NMF	77.42	4%-5.5%
Health Care ETF	XLV	1.47%	NA	NA	UR	NMF	86.82	4%-5.5%
Cisco	CSCO	2.91%	$42.00	Very Attractive	7	0.97	40.87	2.5%-4%
CVS Health	CVS	2.53%	$88.00	Attractive	4	0.90	78.78	2.5%-4%
Google - Class C	GOOG	0.00%	$1181.00	Very Attractive	6	0.95	1122.26	2.5%-4%
Google - Class A	GOOGL	0.00%	$1181.00	Very Attractive	6	0.96	1130.65	2.5%-4%
Intel	INTC	2.51%	$48.00	Attractive	7	0.90	43.24	2.5%-4%
Johnson & Johnson	JNJ	2.32%	$130.00	Attractive	7	1.12	145.76	2.5%-4%
Altria Group	MO	3.79%	$58.00	Very Attractive	6	1.20	69.61	2.5%-4%
Dollar General	DG	1.05%	$89.00	Attractive	7	1.11	99.10	1.5%-2.5%
Gilead Sciences	GILD	2.63%	$109.00	Very Attractive	7	0.72	79.02	1.5%-2.5%
General Motors	GM	3.44%	$43.00	Attractive	7	1.02	44.07	1.5%-2.5%
Priceline	PCLN	0.00%	$2018.00	Highest Rated	3	0.95	1919.40	1.5%-2.5%
PayPal	PYPL	0.00%	$58.00	Attractive	6	1.39	80.54	1.5%-2.5%
Verint Systems	VRNT	0.00%	$50.00	Very Attractive	6	0.86	43.05	1.5%-2.5%
Cash consideration	-	-	-	-	-	-	-	5%-30%

UR = Under Review
This portfolio is not a real money portfolio. Data as of January 15, 2018.

Ideas may not add up to 100% on either the low % or high % due to rounding and/or other combinations / permutations.

Even for DIYers, it is a caveat emptor world out there.