

## The Best & Worst Telecom Sector ETFs

*Structural Integrity – and – Investment Merits*

### Trust

We deliver the whole truth by incorporating critical data from the Financial Footnotes and MD&A that other firms miss.

### Performance

The value and success of our ratings are unrivaled. Click here for proof.

### More Reports

Click here and enter a ticker to buy more of our reports.

- **Broadband HOLDRS (BDH) is our top pick for Telecom sector ETFs**
- **We rate the investment merit of the top 3 Telecom sector ETFs.**
- **We benchmark the individual ETFs against the entire Telecom sector and the S&P 500.**
- **This research enables investors to analyze ETFs and mutual funds as they do stocks.**
- **We offer custom and enhanced ETFs based on our top-ranked stock rating system.**
- **Our ETF analysis is based on aggregation of models for companies held by the fund and weighted according to the fund's allocations to those companies, excluding cash.**



**Figure 1: The Investment Merit of the Top Telecom Sector ETFs**

Fund/Benchmark	% of Fund Allocated to Each Rating					Overall Fund Rating
	Very Attractive	Attractive	Neutral	Dangerous	Very Dangerous	
BDH	12.0%	0.0%	67.6%	14.0%	0.5%	Attractive
TTH	0.0%	33.8%	53.8%	4.2%	1.4%	Neutral
<b>Overall Sector</b>	<b>0.1%</b>	<b>29.1%</b>	<b>46.2%</b>	<b>22.4%</b>	<b>2.2%</b>	<b>Neutral</b>
VOX	0.7%	32.8%	29.4%	28.3%	4.8%	Neutral

\* % may not add up to 100% due to the exclusion of cash and holdings not in our coverage universe.

Sources: New Constructs, LLC and company filings

## Methodology

---

Our Risk/Reward ratings have a solid track record of outperformance for investors.

[Barron's ranked us #1 for stock-picking.](#)

This report offers recommendations on Telecom sector ETFs and benchmarks for (1) investors considering buying Telecom sector ETFs and for (2) comparing individual ETFs to the Telecom sector and the S&P 500. Our analysis is based on aggregating results from our models on each of the companies included in every ETF and the overall sector (43 companies) based on data as of April 20<sup>th</sup>, 2011. We aggregate results for the ETFs in the same way the ETFs are designed. Our goal is to empower investors to analyze ETFs in the same way they analyze individual stocks.

To make an informed ETF investment, investors must consider:

- 1) **Structural Integrity:** ability of an investment vehicle to fulfill its stated objective. We use [XTF, an ETF research firm](#), to find the top 3 Telecom sector ETFs with the best structural integrity rating.
- 2) **Investment Merit:** investment quality of the ETF based on its holdings. We apply our stock rating system to each ETF's holdings to determine its investment merit.

Given the [success](#) of our rating system for individual stocks, we believe its application to groups of stocks (i.e. ETFs and funds) helps investors make more informed ETF and mutual fund buying decisions. Barron's featured our unique ETF research in "[The Danger Within](#)".

## Recommendations Summary

---

Custom ETFs: [Contact us](#) for best-of-breed and enhanced ETF products for a particular sector or index.

### **If you require exposure to the Telecom sector:**

We recommend investors buy Broadband HOLDERS (BDH). BDH is the only Telecom sector ETF to earn an Attractive Overall Risk/Reward rating.

### **If you require exposure to any other sector:**

We recommend investors review our [Sector ETF Roadmap](#) report or our [9 other sector ETF reports](#), beginning with our Consumer Staples, Consumer Discretionary and Health Care sector reports, which are the only sectors to earn an Attractive Overall Risk/Reward rating.

### **If you require exposure to an Telecom ETF or an index ETF:**

We recommend investors buy the following Telecom ETFs over an S&P 500 ETF: Telecom HOLDERS (TTH) and BDH. The S&P 500 and TTH both earn Neutral Overall Risk/Reward ratings but TTH allocates a higher percentage of value to Attractive-or-better-rated stocks.

### **If you are looking for exposure to the best stocks in the market:**

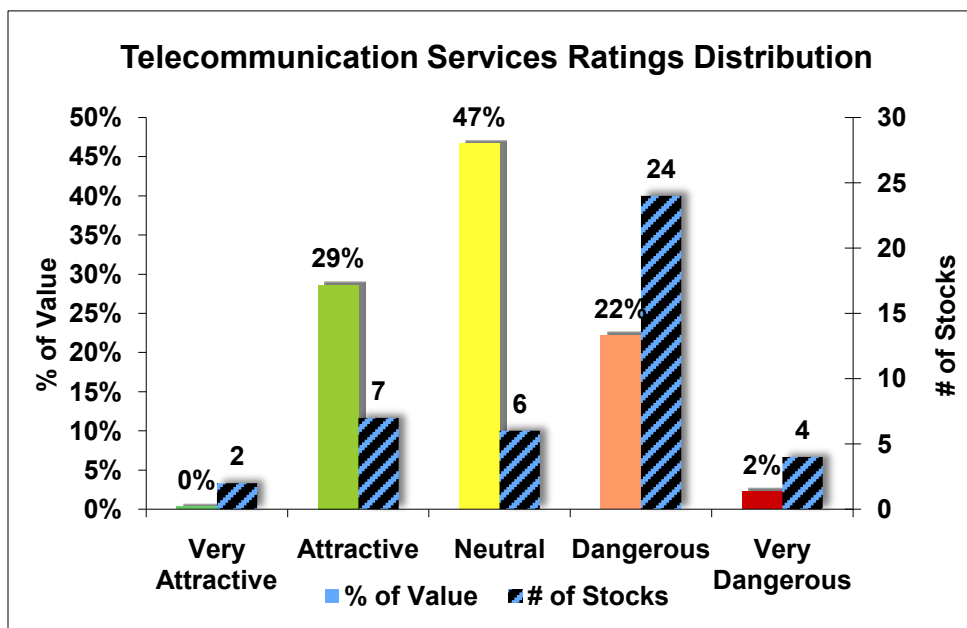
We recommend you buy our [Most Attractive Stocks](#).

**Recommendations Detail**

Click [here](#) for more info on risk/reward rating system and our approach to equity research.

If you want to be in a sector ETF, the Consumer Staples, Consumer Discretionary and Health Care sectors are the best places to shop due to their Attractive Overall Risk/Reward ratings. Figure 2 shows how the Telecom sector's stocks and the market value attributed to them stack up under the microscope of our risk/reward rating system.

**Figure 2: Telecom Sector – Allocation & Holdings by Risk/Reward Rating**



Sources: New Constructs, LLC and company filings

The Telecom sector has 29% of its value invested in Attractive-or-better-rated stocks and 24% of its value invested in Dangerous-or-worse-rated stocks. Although the Telecom sector only earns a Neutral Overall Risk/Reward rating, its heavy weightings of Attractive-or-better-rated stocks create large opportunity for Attractive-or-better-rated ETFs.

The key takeaway is that the Telecom sector offers both good and poor investment opportunities. The value of each ETF is derived from its constituents, so ETFs like BDH that overweight Attractive-or-better-rated stocks are great investment opportunities while ETFs that overweight Neutral-or-worse-rated stocks should be avoided or sold short.

When analyzing the Telecom sector ETFs, we started by identifying those ETFs with acceptable structural integrity as measured by XTF. We chose the Telecom sector ETFs with the highest XTF ratings where we cover at least 90% of the value of the ETF. Due to the small size of the Telecom sector, only 3 ETFs met our criteria. For details on the XTF structural integrity ratings as well as the holdings and weightings for each ETF, see [XTF.com](http://XTF.com).

**Figure 3: Telecom ETFs With Acceptable Structural Integrity**

TICKER	ETF Description	# of Holdings *	XTF RATING
TTH	Telecom HOLDRS	11	7.2
VOX	Vanguard Telecommunications Services Index	37	7
BDH	Broadband HOLDRS	17	5.4

\* # of Holdings excludes cash

Sources: New Constructs, LLC; XTF and company filings

[Contact us](#) for details on our ratings for any stocks in any equity ETF.

Figure 3 clearly shows that not all Telecom ETFs are made the same. Different ETFs have meaningfully different numbers of holdings and, therefore, different allocations to holdings. Given the differences in holdings and allocations, these ETFs will likely perform quite differently.

After determining the structural integrity, we analyzed the investment merit of each ETF based on how it allocates value to each stock it holds. Figure 4 shows how the 3 Telecom sector ETFs stack up versus each other, the overall sector and the S&P 500 based on their Overall Risk/Reward ratings and the allocation of their holdings by rating.

**Figure 4: Investment Merit Based on Holdings and Allocations**

Fund/Benchmark	% of Fund Allocated to Each Rating					Overall Fund Rating
	Very Attractive	Attractive	Neutral	Dangerous	Very Dangerous	
BDH	12.0%	0.0%	67.6%	14.0%	0.5%	Attractive
TTH	0.0%	33.8%	53.8%	4.2%	1.4%	Neutral
<b>S&amp;P 500</b>	<b>21.2%</b>	<b>21.1%</b>	<b>34.0%</b>	<b>16.9%</b>	<b>6.8%</b>	<b>Neutral</b>
<b>Overall Sector</b>	<b>0.3%</b>	<b>28.6%</b>	<b>46.6%</b>	<b>22.2%</b>	<b>2.2%</b>	<b>Neutral</b>
VOX	0.7%	32.8%	29.4%	28.3%	4.8%	Neutral

\* % may not add up to 100% due to the exclusion of cash and holdings not in our coverage universe.

Sources: New Constructs, LLC; XTF and company filings

**Attractive ETFs:**

BDH earns an Attractive Overall Risk/Reward rating and therefore, is the only Telecom ETF we recommend.

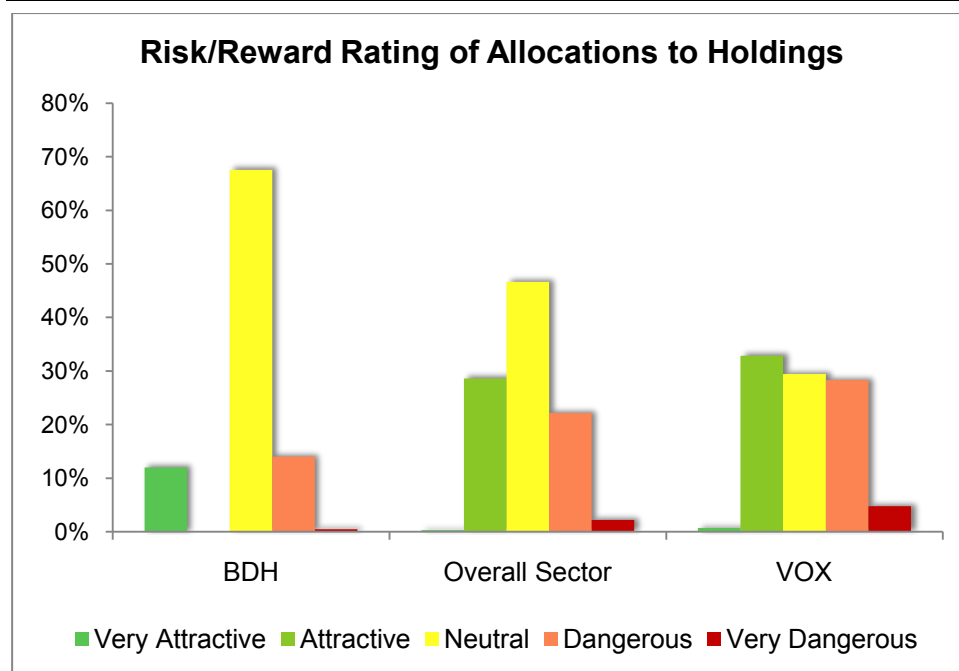
**Neutral ETFs:**

TTH and VOX allocate the value of their fund in a way that earns them a Neutral Overall Risk/Reward rating. We recommend investors buy the Very Attractive and Attractive stocks in this sector before buying any of the Telecom ETFs except BDH. [Contact us](#) for the full list of the 9 Telecom companies that earn an Attractive-or-better Overall Risk/Reward rating. Figure 5 contrasts the differences in investment merit between BDH, VOX, and the overall sector.

**Dangerous ETFs:**

This report does not include any Dangerous-or-worse-rated ETFs.

**Figure 5: Attractive and Neutral Telecom Sector ETFs**



Sources: New Constructs, LLC; XTF and company filings

**Benchmark Comparisons**

**Sector Benchmark**

BDH outperforms the overall Telecom sector in quality-of-earnings ratings. BDH earns a Very Attractive Economic vs. Reported Earnings rating because its Economic Earnings are positive and rising. BDH has an ROIC of 16.9%, earning it a Very Attractive rating, compared to the sector's Dangerous-rated ROIC of 5%.

The Telecom sector outperforms BDH in valuation ratings. The sector has a FCF Yield of 8.1%, earning it an Attractive rating, and a GAP of 20 years compared to BDH's FCF Yield of 4.5% and GAP of 27 years.

**Figure 6: BDH – Risk/Reward Rating**

Overall Risk/Reward Rating	Quality of Earnings		Valuation		
	Econ v Reported Earnings (bn)	ROIC	FCF Yield	Price-to-EBV	GAP (yrs)
Very Dangerous	Misleading Trend	Bottom Quintile	<-5%	>3.5 or -1<0	More than 50
Dangerous	False Positive	4th Quintile	-5%<-1%	2.4<3.5 or <-1	20<50
Neutral	Neutral EE	3rd Quintile	-1%<3%	1.6<2.4	10<20
Attractive	Positive EE	2nd Quintile	3%<10%	1.1<1.6	3<10
Very Attractive	Rising EE	Top Quintile	>10%	0<1.1	Less than 3
Market-Weighted Avg	\$0.90 / \$2.46	16.9%	4.5%	1.3	27

Sources: New Constructs, LLC and company filings

**Figure 7: Telecom Sector – Risk/Reward Rating**

Overall Risk/Reward Score	Quality of Earnings		Valuation		
	Econ v Reported EPS	ROIC	FCF Yield	Price-to-EBV	GAP (yrs)
Very Dangerous	Misleading Trend	Bottom Quintile	<-5%	>3.5 or -1<0	More than 50
Dangerous	False Positive	4th Quintile	-5%<-1%	2.4<3.5 or <-1	20<50
Neutral	Neutral EE	3rd Quintile	-1%<3%	1.6<2.4	10<20
Attractive	Positive EE	2nd Quintile	3%<10%	1.1<1.6	3<10
Very Attractive	Rising EE	Top Quintile	>10%	0<1.1	Less than 3
Market-Weighted Avg	\$-0.40 / \$1.76	5.0%	8.1%	1.9	20
Median	\$-0.43 / \$0.54	4.4%	2.5%	3.7	38

Sources: New Constructs, LLC and company filings

BDH more effectively allocates capital than the overall Telecom sector. Per [Figure 4](#) above, BDH allocates 12% of its value to Very Attractive-rated stocks while the sector only allocates 0.3%. BDH also only allocates 0.5% of its value toward Very Dangerous-rated stocks compared to the sector's Very Dangerous weighting of 2.2%.

For explanation and details behind our risk/reward rating system, see one of our Company Valuation reports, which are available for free [here](#).

### Market Benchmark

BDH and the S&P 500 have comparable quality-of-earnings rating. BDH and the S&P 500 both earn Very Attractive ratings for Economic vs. Reported Earnings and ROIC.

BDH and the S&P 500 also have comparable valuation ratings. BDH and the S&P have the same Price-to-EBV and GAP rating but BDH's FCF Yield of 4.5% earns it an Attractive rating compared to the S&P 500's Neutral-rated FCF Yield of 2.4%.

**Figure 8: BDH – Risk/Reward Rating**

Overall Risk/Reward Rating	Quality of Earnings		Valuation		
	Econ v Reported Earnings (bn)	ROIC	FCF Yield	Price-to-EBV	GAP (yrs)
Very Dangerous	Misleading Trend	Bottom Quintile	<-5%	>3.5 or -1<0	More than 50
Dangerous	False Positive	4th Quintile	-5%<-1%	2.4<3.5 or <-1	20<50
Neutral	Neutral EE	3rd Quintile	-1%<3%	1.6<2.4	10<20
Attractive	Positive EE	2nd Quintile	3%<10%	1.1<1.6	3<10
Very Attractive	Rising EE	Top Quintile	>10%	0<1.1	Less than 3
Market-Weighted Avg	\$0.90 / \$2.46	16.9%	4.5%	1.3	27

Sources: New Constructs, LLC and company filings

**Figure 9: S&P 500 – Risk/Reward Rating**

Overall Risk/Reward Score	Quality of Earnings		Valuation		
	Econ v Reported EPS	ROIC	FCF Yield	Price-to-EBV	GAP (yrs)
Very Dangerous	Misleading Trend	Bottom Quintile	<-5%	>3.5 or -1<0	More than 50
Dangerous	False Positive	4th Quintile	-5%<-1%	2.4<3.5 or <-1	20<50
Neutral	Neutral EE	3rd Quintile	-1%<3%	1.6<2.4	10<20
Attractive	Positive EE	2nd Quintile	3%<10%	1.1<1.6	3<10
Very Attractive	Rising EE	Top Quintile	>10%	0<1.1	Less than 3
Market-Weighted Avg	\$0.74 / \$4.06	18.3%	2.4%	1.5	24
Median	\$0.26 / \$2.24	7.9%	3.2%	1.5	12

Sources: New Constructs, LLC and company filings

BDH more effectively allocates capital than the S&P 500. Per [Figure 4](#) above, it may appear that the S&P does a better job of allocating capital since it allocates 42.3% of its value to Attractive-or-better-rated stocks compared to BDH's 12% weighting. However, BDH's 12% is allocated to companies with substantially more attractive investment opportunities. BDH also only allocates 14.5% of its value to Dangerous-or-worse-rated stocks while the S&P 500 allocates 23.7%.

**Appendix: Risk/Reward Rating System**

Our Risk/Reward Rating System assigns a rating to every stock we cover 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.

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

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

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

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



<b>Price-to-EBV Ratio</b>	<b>Rates stocks based on their Price-to-Economic Book Value Ratio. Values based on Latest Closing Stock price and Latest Fiscal Year.</b>
>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

<b>Growth Appreciation Period (yrs)</b>	<b>Rates stocks based on their Market-Implied Growth Appreciation Period. Values based on Latest Closing Stock price and Default Forecast Scenario.</b>
>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

## New Constructs® – Profile

### **How New Constructs Creates Value for Clients**

1. **Superior Recommendations** – Our [stock picks](#) consistently outperform. See our track record in our [stock-picking accolades](#) and [Proof Is In Performance](#) reports.
2. **More Accurate Research** – Our [patented Research Platform](#) for [reversing accounting distortions](#) and [discounted cash flow analysis](#) leverages better data to deliver smarter research.
3. **Time Savings** – We check the fine print in thousands of corporate filings so you don't have to. As reported by [Barron's](#), our expertise in analyzing SEC filings delivers [Hidden Gems and Red Flags](#) that drive long-term stock-picking success.
4. **Transparency** – We are proud to share the results of our analysis of over 50,000 10Ks. See the [Corporate Disclosure Transgressions](#) report we provided the SEC. Our reports detail all data and assumptions. Company Models enable users to change them.
5. **Objectivity** – New Constructs is an independent research firm, not tied to Wall Street or investment banking services. Our models are driven by comprehensive high-quality data not stories. See our [presentation to the Senate Banking Committee](#), the SEC and many others in DC.

### **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.

### **Additional Information**

Incorporated in July 2002, [New Constructs](#) is an independent publisher of investment research that provides clients with consulting, advisory and research services. We specialize in quality-of-earnings, forensic accounting and discounted cash flow valuation analyses for all U.S. public companies. We translate accounting data from 10Ks into economic financial statements, i.e. [NOPAT](#), [Invested Capital](#), and [WACC](#), to create [economic earnings models](#), which are necessary to understand the true profitability and valuation of companies. Visit the [Free Archive](#) to download samples of our research. New Constructs is a [BBB accredited](#) business and a member of the [Investorside Research Association](#).

## DISCLOSURES

---

New Constructs®, LLC (together with any subsidiaries and/or affiliates, "New Constructs") is an independent organization with no management ties to the companies it covers. None of the members of New Constructs' management team or the management team of any New Constructs' affiliate holds a seat on the Board of Directors of any of the companies New Constructs covers. New Constructs does not perform any investment or merchant banking functions and does not operate a trading desk.

New Constructs' Stock Ownership Policy prevents any of its employees or managers from engaging in Insider Trading and restricts any trading whereby an employee may exploit inside information regarding our stock research. In addition, employees and managers of the company are bound by a code of ethics that restricts them from purchasing or selling a security that they know or should have known was under consideration for inclusion in a New Constructs report nor may they purchase or sell a security for the first 15 days after New Constructs issues a report on that security.

New Constructs is affiliated with Novo Capital Management, LLC, the general partner of a hedge fund. At any particular time, New Constructs' research recommendations may not coincide with the hedge fund's holdings. However, in no event will the hedge fund receive any research information or recommendations in advance of the information that New Constructs provides to its other clients.

## DISCLAIMERS

---

The information and opinions presented in this report are provided to you for information purposes only and are not to be used or considered as an offer or solicitation of an offer to buy or sell securities or other financial instruments. New Constructs has not taken any steps to ensure that the securities referred to in this report are suitable for any particular investor and nothing in this report constitutes investment, legal, accounting or tax advice. This report includes general information that does not take into account your individual circumstance, financial situation or needs, nor does it represent a personal recommendation to you. The investments or services contained or referred to in this report may not be suitable for you and it is recommended that you consult an independent investment advisor if you are in doubt about any such investments or investment services.

Information and opinions presented in this report have been obtained or derived from sources believed by New Constructs to be reliable, but New Constructs makes no representation as to their accuracy, authority, usefulness, reliability, timeliness or completeness. New Constructs accepts no liability for loss arising from the use of the information presented in this report, and New Constructs makes no warranty as to results that may be obtained from the information presented in this report. Past performance should not be taken as an indication or guarantee of future performance, and no representation or warranty, express or implied, is made regarding future performance. Information and opinions contained in this report reflect a judgment at its original date of publication by New Constructs and are subject to change without notice. New Constructs may have issued, and may in the future issue, other reports that are inconsistent with, and reach different conclusions from, the information presented in this report. Those reports reflect the different assumptions, views and analytical methods of the analysts who prepared them and New Constructs is under no obligation to insure that such other reports are brought to the attention of any recipient of this report.

New Constructs' reports are intended for distribution to its professional and institutional investor customers. Recipients who are not professionals or institutional investor customers of New Constructs should seek the advice of their independent financial advisor prior to making any investment decision or for any necessary explanation of its contents.

This report is not directed to, or intended for distribution to or use by, any person or entity who is a citizen or resident of or located in any locality, state, country or jurisdiction where such distribution, publication, availability or use would be contrary to law or regulation or which would be subject New Constructs to any registration or licensing requirement within such jurisdiction.

This report may provide the addresses of websites. Except to the extent to which the report refers to New Constructs own website material, New Constructs has not reviewed the linked site and takes no responsibility for the content therein. Such address or hyperlink (including addresses or hyperlinks to New Constructs own website material) is provided solely for your convenience and the information and content of the linked site do not in any way form part of this report. Accessing such websites or following such hyperlink through this report shall be at your own risk.

All material in this report is the property of, and under copyright, of New Constructs. None of the contents, nor any copy of it, may be altered in any way, copied, or distributed or transmitted to any other party without the prior express written consent of New Constructs. All trademarks, service marks and logos used in this report are trademarks or service marks or registered trademarks or service marks of New Constructs.

Copyright New Constructs, LLC 2003 through the present date. All rights reserved.