Best & Worst ETFs and Mutual Funds: Mid Cap Blend Style

The Mid Cap Blend style ranks eighth out of the twelve fund styles as detailed in my Style Rankings for ETFs and Mutual Funds report. It gets my Dangerous rating, which is based on aggregation of ratings of 19 ETFs and 303 mutual funds in the Mid Cap Blend style as of July 29, 2014. Prior reports on the best & worst ETFs and mutual funds in every sector and style are here.

Figures 1 and 2 show the five best and worst-rated ETFs and mutual funds in the style. Not all Mid Cap Blend style ETFs and mutual funds are created the same. The number of holdings varies widely (from 23 to 3152). This variation creates drastically different investment implications and, therefore, ratings. The best ETFs and mutual funds allocate more value to Attractive-or-better-rated stocks than the worst, which allocate too much value to Neutral-or-worse-rated stocks.

To identify the best and avoid the worst ETFs and mutual funds within the Mid Cap Blend sector, investors need a predictive rating based on (1) the stocks ratings of the holdings, (2) the all-in expenses of each ETF and mutual fund, and (3) the fund's rank compared to all other ETFs and mutual funds. As a result, only the cheapest funds with the best holdings receive Attractive or better ratings. Investors need not rely on backward-looking ratings. My fund rating methodology is detailed here.

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

Get my ratings on all ETFs and mutual funds in this style by searching for Mid Cap Blend on my mutual fund and ETF screener.

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				
EZM	10%	38%	46%	**Neutral**
CZA	11%	30%	44%	**Neutral**
VO	12%	32%	53%	**Neutral**
IJH	8%	36%	54%	**Neutral**
IVOO	7%	36%	54%	**Neutral**
Worst ETFs				
MVV	7%	36%	54%	**Neutral**
SCHM	9%	30%	56%	**Dangerous**
RSCO	8%	26%	56%	**Dangerous**
UVU	14%	23%	58%	**Dangerous**
GSRA	8%	29%	55%	**Dangerous**

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

Sources: New Constructs, LLC and company filings

PowerShares Fundamental Pure Mid Core Portfolio ETF (PXMC), ProShares Ultra Russell Mid Cap Growth ETF (UKW), and QuantShares U.S. Market Neutral Anti-Beta Fund ETF (BTAL) 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				
LSIRX	15%	40%	38%	Attractive
SMBYX	15%	40%	38%	Attractive
CIPIX	15%	45%	30%	Attractive
SMCPX	15%	40%	38%	Attractive
CIPMX	15%	45%	30%	Attractive
Worst Mutual Funds				
HSOAX	2%	27%	66%	Very Dangerous
SPMAX	9%	24%	59%	Very Dangerous
PMVCX	5%	32%	63%	Very Dangerous
PAMVX	5%	32%	63%	Very Dangerous
MDPSX	5%	26%	37%	Very Dangerous

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

Sources: New Constructs, LLC and company filings

Boston Trust Midcap Fund (BTMFX) is excluded from Figure 2 because its total net assets (TNA) are below $100 million and do not meet our liquidity minimums.

WisdomTree Mid Cap Earnings Fund ETF (EZM) is my top-rated Mid Cap Blend ETF and Legg Mason Partners Equity Trust: ClearBridge Mid Cap Core Fund (LSIRX) is my top-rated Mid Cap Blend mutual fund. EZM earns my Neutral rating and LSIRX earns my Attractive rating.

ALPS GS Risk-Adjusted Return U.S. Large Cap index ETF (GSRA) is my worst-rated Mid Cap Blend ETF and Mid-Cap ProFund (MDPSX) is my worst-rated Mid Cap Blend mutual fund. GSRA earns my Dangerous rating and MDPSX earns my Very Dangerous rating.

Figure 3 shows that 252 out of the 2518 stocks (over 10% of the market value) in Mid Cap Blend ETFs and mutual funds get an Attractive-or-better rating. However, 0 out of 19 Mid Cap Blend ETFs and 11 out of 303 Mid Cap Blend mutual funds (less than 4% of total net assets) get an Attractive-or-better rating.

The takeaways are: mutual fund managers allocate too much capital to low-quality stocks and Mid Cap Blend ETFs hold poor quality stocks.

Figure 3: Mid Cap Blend Style Landscape For ETFs, Mutual Funds & Stocks

	Very Attractive	Attractive	Neutral	Dangerous	Very Dangerous
# of Stocks	68	184	649	1251	366
% of Style	3%	8%	35%	39%	16%
# of ETFs	0	0	15	4	0
% of ETFs	0%	0%	79%	21%	0%
% of TNA	0%	0%	98%	2%	0%
# of MFs	0	11	151	107	34
% of MFs	0%	4%	50%	35%	11%
% of TNA	0%	4%	53%	41%	3%

Sources: New Constructs, LLC and company filings

As detailed in "Cheap Funds Dupe Investors", the fund industry offers many cheap funds but very few funds with high-quality stocks, or with what I call good portfolio management.

Investors need to tread carefully when considering Mid Cap Blend ETFs and mutual funds, as no ETFs and only 11 mutual funds in the Mid Cap Blend style allocate enough value to Attractive-or-better-rated stocks to earn an Attractive rating.

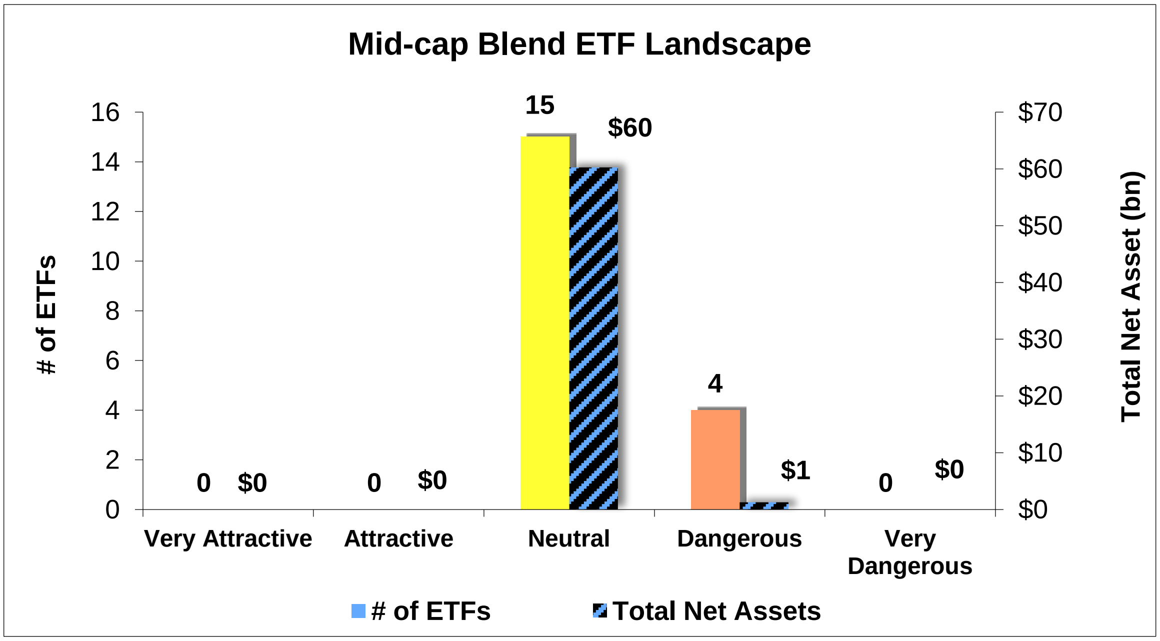
Zimmer Holdings, Inc. (ZMH) is one of my favorite stocks held by Mid Cap Blend ETFs and mutual funds and earns my Attractive rating. Over the past decade, ZMH has grown after-tax profit (NOPAT) by 12% compounded annually. ZMH currently earns a return on invested capital (ROIC) of 16%, which puts it in the top quintile of all companies I cover. The company has also generated positive economic earnings since going public in 2001. Investors have taken notice of this impressive NOPAT growth as the stock is up over 28% in the past year. However, ZMH still has great upside. Even at its current price of ~$100/share, ZMH has a price to economic book value (PEBV) ratio of 1.2. This ratio implies that the market expects ZMH to grow NOPAT by only 20% for the remaining life of the corporation. Based on ZMH's strong history of profit growth I expect the company to surpass this expectation.

CONSOL Energy, Inc. (CNX) is one of my least favorite stocks held by Mid Cap Blend ETFs and mutual funds and earns my Very Dangerous rating. CNX's NOPAT declined by 20% compounded annually from 2008 to 2013. Over the same time period, the company's ROIC has fallen from 10% to a bottom quintile 3%. CNX has generated positive economic earnings in only one of the last 14 years. These downward trends have continued during 2014 as CNX reported a net loss in 2Q14. Even so, CNX's stock is still up over 8%, which leaves it overvalued. To justify its current price of ~$40/share, CNX must grow NOPAT by 11% compounded annually for the next 22 years. This expectation is awfully optimistic given CNX's rapidly declining NOPAT over the past five years. Investors should avoid CNX.

Figures 4 and 5 show the rating landscape of all Mid Cap Blend ETFs and mutual funds.

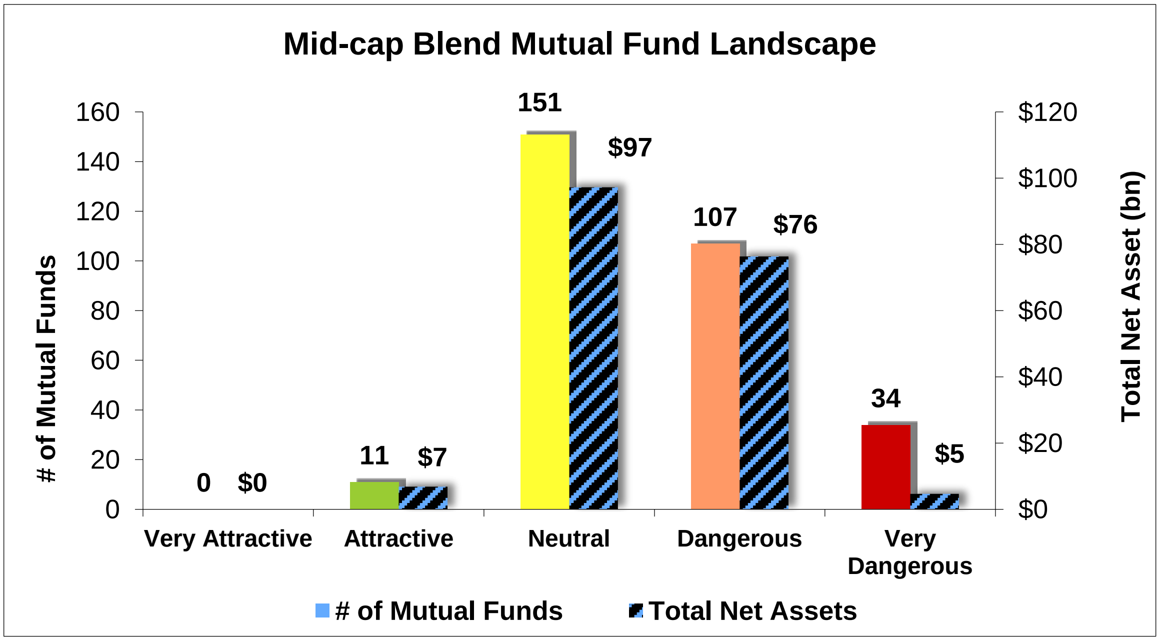
My Style Rankings for ETFs and Mutual Funds report ranks all styles and highlights those that offer the best investments.

Figure 4: Separating the Best ETFs From the Worst Funds



Sources: New Constructs, LLC and company filings

Figure 5: Separating the Best Mutual Funds From the Worst Funds



Sources: New Constructs, LLC and company filings

Review my full list of ratings and rankings along with reports on all 19 ETFs and 303 mutual funds in the Mid Cap Blend style.

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

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