1Q15 Sector Ratings For ETFs & Mutual Funds

At the beginning of the first quarter of 2015, only the Consumer Staples sector earns an Attractive-or-better rating. Sector ratings are based on the aggregation of our fund ratings for every ETF and mutual fund in each sector.

Investors looking for sector funds that hold quality stocks should look no further than the Consumer Staples and Information Technology sectors. These sectors house the most Attractive-or-better rated funds. Figures 4 and 7 provide details. The primary driver behind an Attractive fund rating is good portfolio management, or good stock picking, with low total annual costs.

Note that the Attractive-or-better Predictive ratings do not always correlate with Attractive-or-better total annual costs. This fact underscores that (1) cheap funds can dupe investors and (2) investors should invest only in funds with good stocks and low fees.

See Figures 4 through 13 for a detailed breakdown of ratings distributions by sector. Platinum members have access to comprehensive reports on all sectors and investment styles.

Figure 1: Ratings For All Sectors

Sector	Predictive Rating	Portfolio Management Rating	Total Annual Costs Rating
Financials	Dangerous	Dangerous	Attractive
Utilities	Dangerous	Dangerous	Attractive
Health Care	Dangerous	Dangerous	Attractive
Energy	Dangerous	Dangerous	Neutral
Materials	Neutral	Dangerous	Attractive
Telecom	Neutral	Dangerous	Attractive
Cons Disc	Neutral	Neutral	Very Attractive
Industrials	Neutral	Neutral	Attractive
Info Tech	Neutral	Neutral	Neutral
Cons Staples	Very Attractive	Neutral	Very Attractive

Source: New Constructs, LLC and company filings

To earn an Attractive-or-better Predictive Rating, an ETF or mutual fund must have high-quality holdings and low costs. Only the top 30% of all ETFs and mutual funds earn our Attractive or better ratings.

Fidelity MSCI Consumer Staples Index ETF (FSTA) is our top rated Consumer Staples fund. It gets our Very Attractive rating by allocating over 27% of its value to Attractive-or-better-rated stocks.

Walmart (WMT) is one of my favorite stocks held by FSTA. Walmart has long been one of my favorite stocks, and remains a leader in the retail industry. While 2014 financial results had a few hiccups, a strong holiday season and new initiatives have positioned Walmart well going into 2015. As history has shown us, Walmart is able to handle the changing retail environment and continue creating profit growth. Over the past decade, Walmart has grown after-tax profit (NOPAT) by 7% compounded annually. With over $14 billion in free cash flow (FCF) in 2014, as well as a return on invested capital (ROIC) of 12%, Walmart not only has the ability to explore future growth options, but has proven to generate high returns on money invested into the business.

At its current price of ~$86/share, Walmart has a price to economic book value (PEBV) ratio of 1.0. This ratio implies the market expects Walmart to never meaningfully grow NOPAT again. This expectation flies in the face of Walmart's impressive history of profitability. Walmart is excelling in its core business and expanding into other spaces, and should easily surpass such low expectations this year.

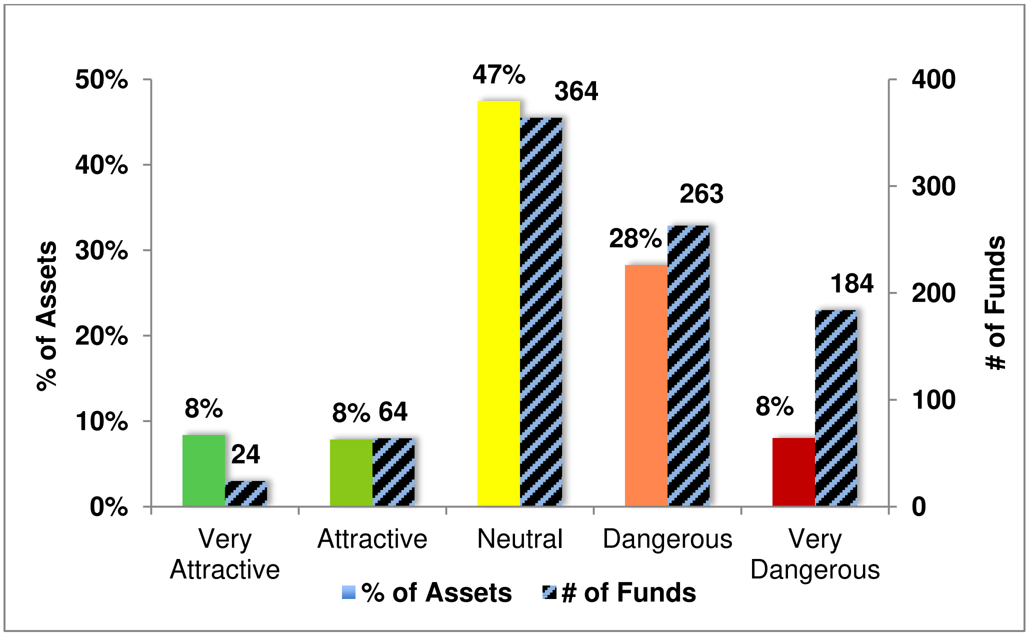
Rydex Real Estate Fund (RYREX) is my worst Financials fund. It gets my Very Dangerous rating by allocating over 63% of its value to Dangerous-or-worse-rated stocks, and to make matters worse, charges investors annual costs of 7.85%.

Crown Castle International Corporation (CCI) is one of my least favorite stocks held by RYREX and gets my Dangerous rating. Crown Castle has been rapidly spending money for years, but is failing to increase profits. Over the past three years, Crown Castle has increased its invested capital by 39% compounded annually. However, NOPAT has increased only 2% over the same time period. This expansion of the balance sheet without any increases in profits, has also led to Crown Castle earning a bottom-quintile ROIC of 3%.The company is rapidly bleeding cash, with -$5 billion in free cash flow last year.

Despite these glaring issues, the market has priced Crown Castle for further growth. To justify its current valuation of ~$79/share, CCI must grow NOPAT by 10% compounded annually for the next 15 years. Crown Castle has given investors reason to be cautious about its ability to grow profits, and with negative free cash flow, meeting future obligations may become difficult for the company. Investors should avoid Crown Castle.

Figure 2 shows the distribution of our Predictive Ratings for all sector ETFs and mutual funds.

Figure 2: Distribution of ETFs & Mutual Funds (Assets and Count) by Predictive Rating



Source: New Constructs, LLC and company filings

Figure 3 offers additional details on the quality of the sector funds. Note that the average Total Annual Cost of Very Dangerous funds is over seven times that of Very Attractive funds.

Figure 3: Predictive Rating Distribution Stats

	Very Attractive	Attractive	Neutral	Dangerous	Very Dangerous
# of ETFs & Funds	24	64	364	263	184
% of ETFs & Funds	3%	7%	40%	29%	20%
% of TNA	8%	8%	47%	28%	8%
Avg. TAC	0.29%	0.52%	0.69%	1.00%	2.08%

* Avg TAC = Weighted Average Total Annual Costs

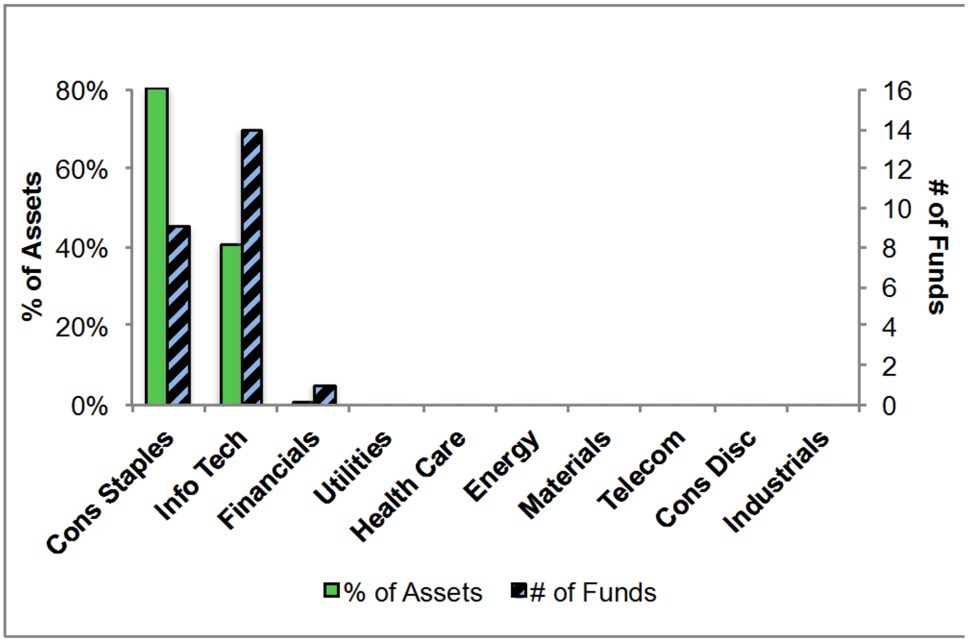
Source: New Constructs, LLC and company filings

Ratings by Sector

Figure 4 presents a mapping of Very Attractive funds by sector. The chart shows the number of Very Attractive funds in each sector and the percentage of assets in each sector allocated to funds that are rated Very Attractive.

One interesting note is that over 40% of assets are held in only 8% of the funds in the Information Technology sector.

Figure 4: Very Attractive ETFs & Mutual Funds by Sector



Source: New Constructs, LLC and company filings

Figure 5 presents the data charted in Figure 4.

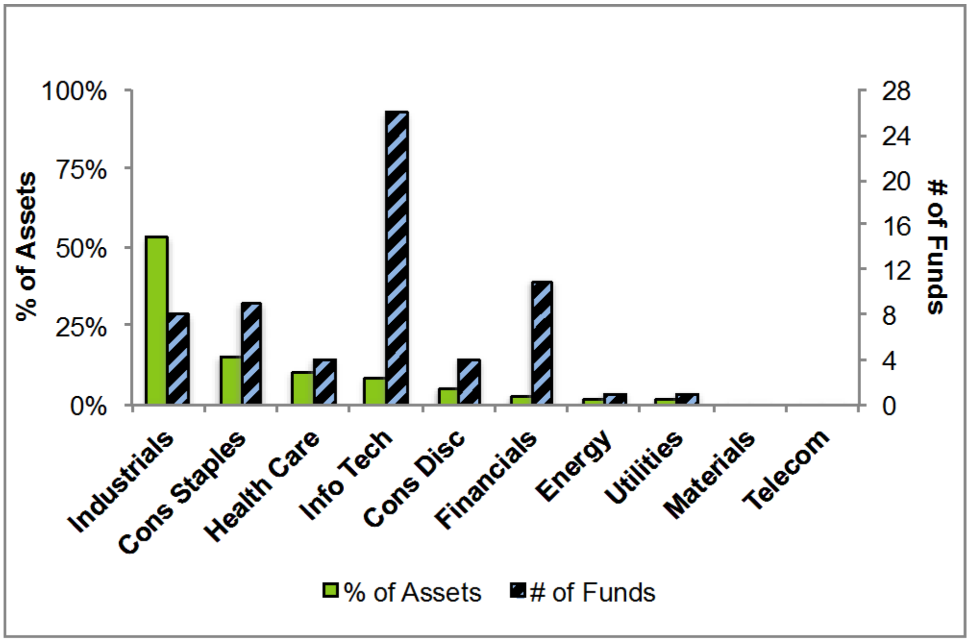
Figure 5: Very Attractive ETFs & Mutual Funds by Sector

Sector	% of Sector Assets	# of Very Attractive Funds	# of Very Attractive Funds as a % of Sector
Cons Staples	80%	9	36%
Info Tech	41%	14	8%
Financials	0%	1	0%
Industrials	0%	0	0%
Health Care	0%	0	0%
Cons Disc	0%	0	0%
Energy	0%	0	0%
Utilities	0%	0	0%
Telecom	0%	0	0%
Materials	0%	0	0%

Source: New Constructs, LLC and company filings

Figure 6 presents a mapping of Attractive funds by sector. The chart shows the number of Attractive funds in each sector and the percentage of assets allocated to Attractive-rated funds in each sector.

Figure 6: Attractive ETFs & Mutual Funds by Sector



Source: New Constructs, LLC and company filings

Figure 7 presents the data charted in Figure 6.

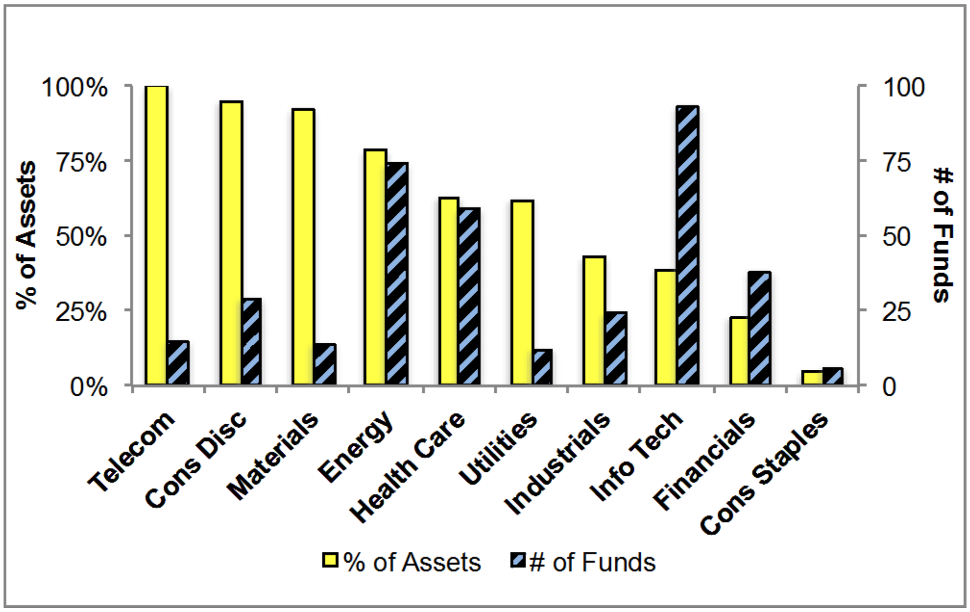
Figure 7: Attractive ETFs & Mutual Funds by Sector

Sector	% of Sector Assets	# of Attractive Funds	# of Attractive Funds as a % of Sector
Industrials	53%	8	21%
Cons Staples	15%	9	36%
Health Care	10%	4	3%
Info Tech	8%	26	15%
Cons Disc	5%	4	11%
Financials	2%	11	4%
Energy	2%	1	1%
Utilities	2%	1	3%
Telecom	0%	0	0%
Materials	0%	0	0%

Source: New Constructs, LLC and company filings

Figure 8 presents a mapping of Neutral funds by sector. The chart shows the number of Neutral funds in each sector and the percentage of assets allocated to Neutral-rated funds in each sector.

Figure 8: Neutral ETFs & Mutual Funds by Sector



Source: New Constructs, LLC and company filings

Figure 9 presents the data charted in Figure 8.

Figure 9: Neutral ETFs & Mutual Funds by Sector

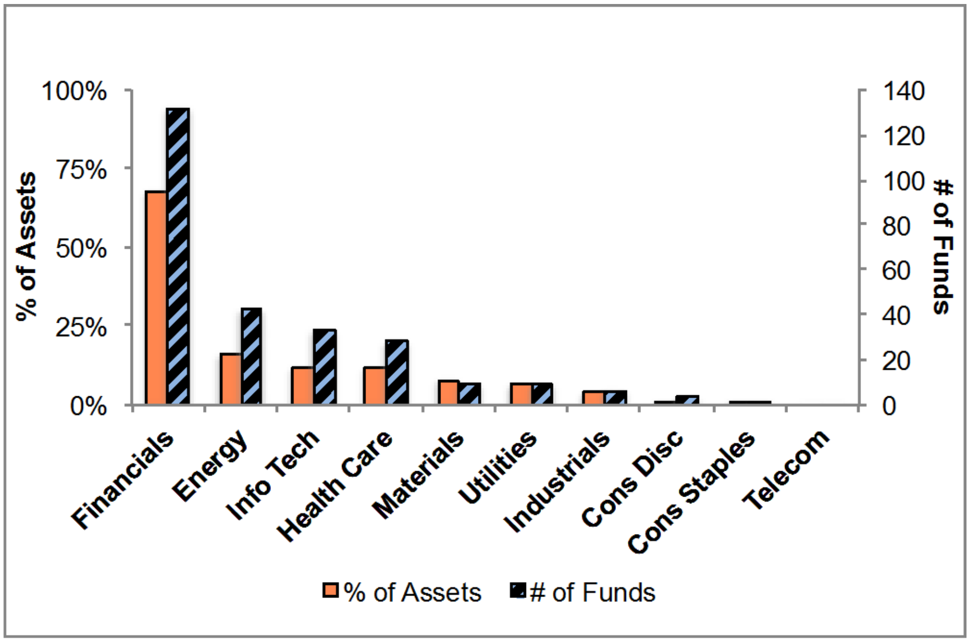
Sector	% of Sector Assets	# of Neutral Funds	# of Neutral Funds as a % of Sector
Telecom	100%	15	79%
Cons Disc	95%	29	78%
Materials	92%	14	54%
Energy	79%	74	52%
Health Care	63%	59	49%
Utilities	62%	12	32%
Industrials	43%	24	63%
Info Tech	39%	93	54%
Financials	23%	38	13%
Cons Staples	4%	6	24%

Source: New Constructs, LLC and company filings

Figure 10 presents a mapping of Dangerous funds by fund sector. The chart shows the number of Dangerous funds in each sector and the percentage of assets allocated to Dangerous-rated funds in each sector.

The landscape of sector ETFs and mutual funds is littered with Dangerous funds. Investors in Financials funds have put over 68% of their assets in Dangerous-rated funds.

Figure 10: Dangerous ETFs & Mutual Funds by Sector



Source: New Constructs, LLC and company filings

Figure 11 presents the data charted in Figure 10.

Figure 11: Dangerous ETFs & Mutual Funds by Sector

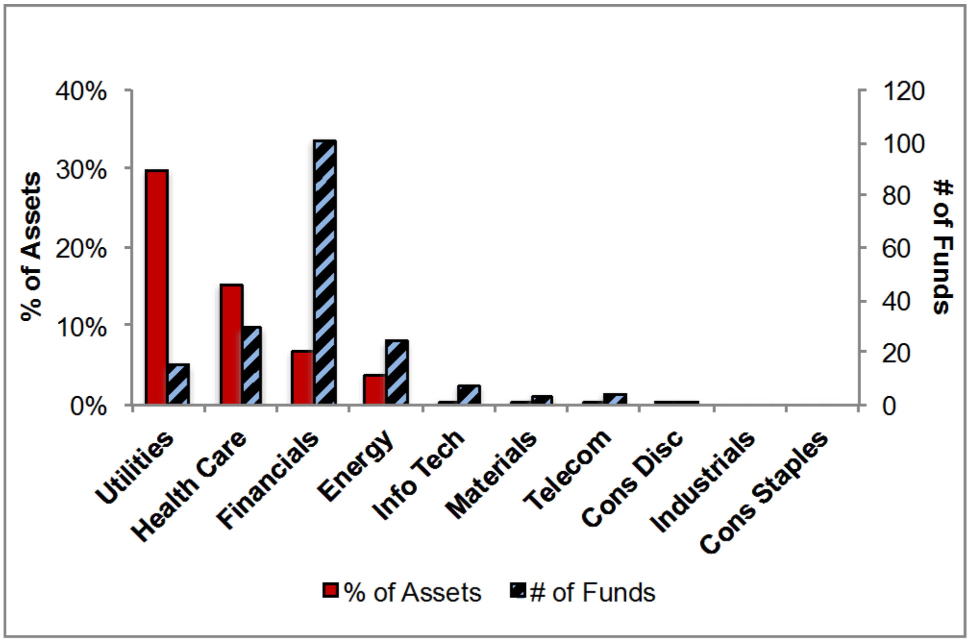
Sector	% of Sector Assets	# of Dangerous Funds	# of Dangerous Funds as a % of Sector
Financials	68%	132	47%
Energy	16%	42	30%
Info Tech	12%	33	19%
Health Care	12%	28	23%
Materials	8%	9	35%
Utilities	6%	9	24%
Industrials	4%	6	16%
Cons Disc	0%	3	8%
Cons Staples	0%	1	4%
Telecom	0%	0	0%

Source: New Constructs, LLC and company filings

Figure 12 presents a mapping of Very Dangerous funds by fund sector. The chart shows the number of Very Dangerous funds in each sector and the percentage of assets in each sector allocated to funds that are rated Very Dangerous.

Taking into account the number of Dangerous funds from above, as well as the number of Very Dangerous funds shown below, the Financials sector has over 230 Dangerous-or-worse rated funds. Buyer beware.

Figure 12: Very Dangerous ETFs & Mutual Funds by Sector



Source: New Constructs, LLC and company filings

Figure 13 presents the data charted in Figure 12.

Figure 13: Very Dangerous ETFs & Mutual Funds by Sector

Sector	% of Sector Assets	# of Very Dangerous Funds	# of Very Dangerous Funds as a % of Sector
Utilities	30%	15	41%
Health Care	15%	29	24%
Financials	7%	101	36%
Energy	4%	24	17%
Info Tech	0%	7	4%
Materials	0%	3	12%
Telecom	0%	4	21%
Cons Disc	0%	1	3%
Industrials	0%	0	0%
Cons Staples	0%	0	0%

Source: New Constructs, LLC and company filings

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

Appendix: Predictive Fund Rating System

New Constructs' Predictive fund Ratings enable smarter investing by assessing the key drivers of future fund performance. We start by analyzing every funds' holdings based on New Constructs' stock ratings, which are regularly featured as among the best by Barron's. Next, we measure and rank the all-in fund expenses. Finally, we rank the fund compared to all other funds to identify the best and worst funds in the market.

Intuitively, there are two drivers for future fund performance.

1. Stock-picking (Portfolio Management Rating) and
2. Fund expenses (Total Annual Costs Rating)

Our Predictive Fund Rating is based on these drivers and the fund's ranking:

1. Top 10% = Very Attractive Rating
2. Next 20% = Attractive Rating
3. Next 40% = Neutral Rating
4. Next 20% = Dangerous Rating
5. Bottom 10% = Very Dangerous Rating

The figure below details the criteria that drive our Predictive Rating system for funds. The two drivers of our predictive ratings system are Portfolio Management and Total Annual Costs. The Portfolio Management ratings (detail here) is the same as our Stock Rating (detail here) except that we incorporate Asset Allocation (details here). The Total Annual Costs Ratings (details here) captures the all-in costs of being in a fund over a 3-year holding period, the average period for all mutual funds.

Predictive Rating	Portfolio Management Rating						Total Annual Costs
	Business Strength		Valuation			Cash Allocation	
	Quality of Earnings	Return on Invested Capital	FCF Yield	Price to Economic Book Value	Market-Implied Duration of Growth		
Very Dangerous	Misleading Trend	Bottom Quintile	< -5%	>3.5 or -1<0	> 50	> 20%	> 4 %
Dangerous	False Positive	4th Quintile	-5% < -1%	2.4<3.5 or <-1	20 < 50	8% < 20%	2% < 4%
Neutral	Neutral EE	3rd Quintile	-1% < 3%	1.6 < 2.4	10 < 20	2.5% < 8%	1% < 2%
Attractive	Positive EE	2nd Quintile	3% < 10%	1.1 < 1.6	3 < 10	1% < 2.5%	0.5% < 1%
Very Attractive	Rising EE	Top Quintile	> 10%	0 < 1.1	0 < 3	<1%	< 0.5%

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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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