ETF & Mutual Fund Rankings: Small Cap Blend Style

The Small Cap Blend style ranks tenth out of the twelve fund styles as detailed in our 3Q16 Style Ratings for ETFs and Mutual Funds report. Last quarter, the Small Cap Blend style ranked tenth. It gets our Dangerous rating, which is based on aggregation of ratings of 26 ETFs and 715 mutual funds in the Small Cap Blend style as of August 4, 2016. See a recap of our 2Q16 Style Ratings here.

Figures 1 and 2 show the five best and worst rated ETFs and mutual funds in the style. Not all Small Cap Blend style ETFs and mutual funds are created the same. The number of holdings varies widely (from 21 to 2,478). This variation creates drastically different investment implications and, therefore, ratings.

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

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				
IJR	11%	34%	48%	**Neutral**
VIOO	11%	34%	47%	**Neutral**
SLY	12%	35%	47%	**Neutral**
EES	18%	32%	34%	**Neutral**
EZM	17%	37%	37%	**Neutral**
Worst ETFs				
NASH	14%	25%	51%	**Neutral**
RWJ	11%	31%	50%	**Neutral**
FYX	14%	34%	40%	**Neutral**
EQWS	9%	18%	46%	**Dangerous**
RWK	12%	38%	46%	**Dangerous**

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

Sources: New Constructs, LLC and company filings

Victory CEMP U.S. Discovery Volatility Index (CSF) and iShares Enhanced U.S. Small Cap ETF (IESM) and 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				
BOSOX	27%	48%	21%	Very Attractive
PXQSX	12%	44%	24%	Attractive
WSVIX	22%	44%	23%	Attractive
PQSCX	12%	44%	24%	Attractive
VVPSX	24%	23%	25%	Attractive
Worst Mutual Funds				
WFSMX	6%	23%	52%	Very Dangerous
TNVAX	3%	18%	48%	Very Dangerous
RYROX	4%	14%	23%	Very Dangerous
RYRRX	4%	14%	23%	Very Dangerous
PASMX	11%	16%	52%	Very Dangerous

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

Sources: New Constructs, LLC and company filings

Four mutual funds are excluded from Figure 2 because their total net assets (TNA) are below $100 million and do not meet our liquidity minimums. See our mutual fund screener for more details.

iShares Core S&P Small-Cap ETF (IJR) is the top-rated Small Cap Blend ETF and Boston Trust Small Cap Fund (BOSOX) is the top-rated Small Cap Blend mutual fund. IJR receives a Neutral rating and BOSOX receives a Very Attractive rating.

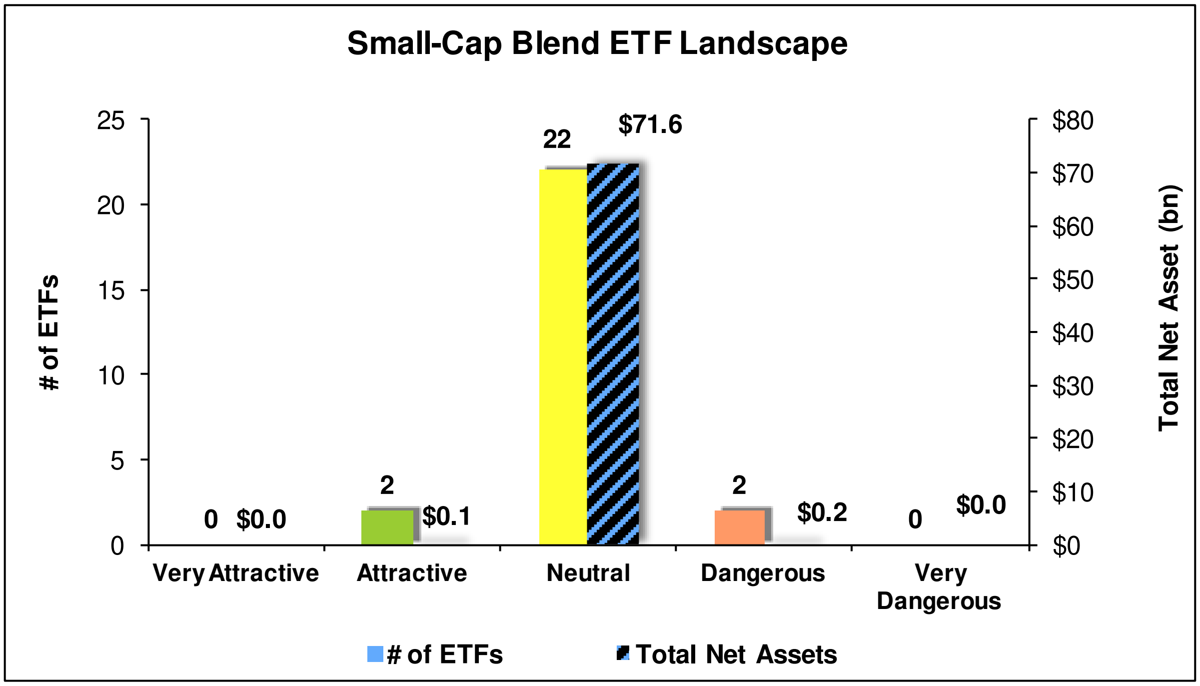
Oppenheimer Mid Cap Revenue ETF (RWK) is the worst rated Small Cap Blend ETF and Pacific Advisors Small Cap Value Fund (PASMX) is the worst rated Small Cap Blend mutual fund. RWK earns a Dangerous rating and PASMX earns a Very Dangerous rating.

Aspen Insurance Holdings (AHL: $45/share) is one of our favorite stocks held by VVPSX and earns an Attractive rating. Since 2003, AHL has grown after-tax profit (NOPAT) by 6% compounded annually. The company has improved its return on invested capital (ROIC) from -7% in 2005 to 9% over the last twelve months. Despite improvements in the underlying economics of the business, AHL remains undervalued. At its current price of $45/share, Aspen Insurance has a price-to-economic book value (PEBV) ratio of 0.6. This ratio means that the market expects Aspen's NOPAT to permanently decline by 40%. If Aspen can continue growing NOPAT by just 6% compounded annually for the next 5 years, the stock is worth $106 today – a 135% upside.

Olin Corporation (OLN: $21/share) is one of our least favorite stocks held by RYRRX and earns a Dangerous rating. We featured OLN as a Danger Zone pick in June 2014, and it remains a dangerous investment. Since 2011, Olin's NOPAT has declined by 28% compounded annually. The company's ROIC has fallen from an already low 6% in 2009 to a bottom-quintile 2% over the last twelve months. Despite the deteriorating fundamentals, OLN is significantly overvalued. To justify its current price of $21/share Olin must grow NOPAT by 21% compounded annually for the next 13 years. Considering the history of profit decline, the downside risk to this stock outweighs the potential reward.

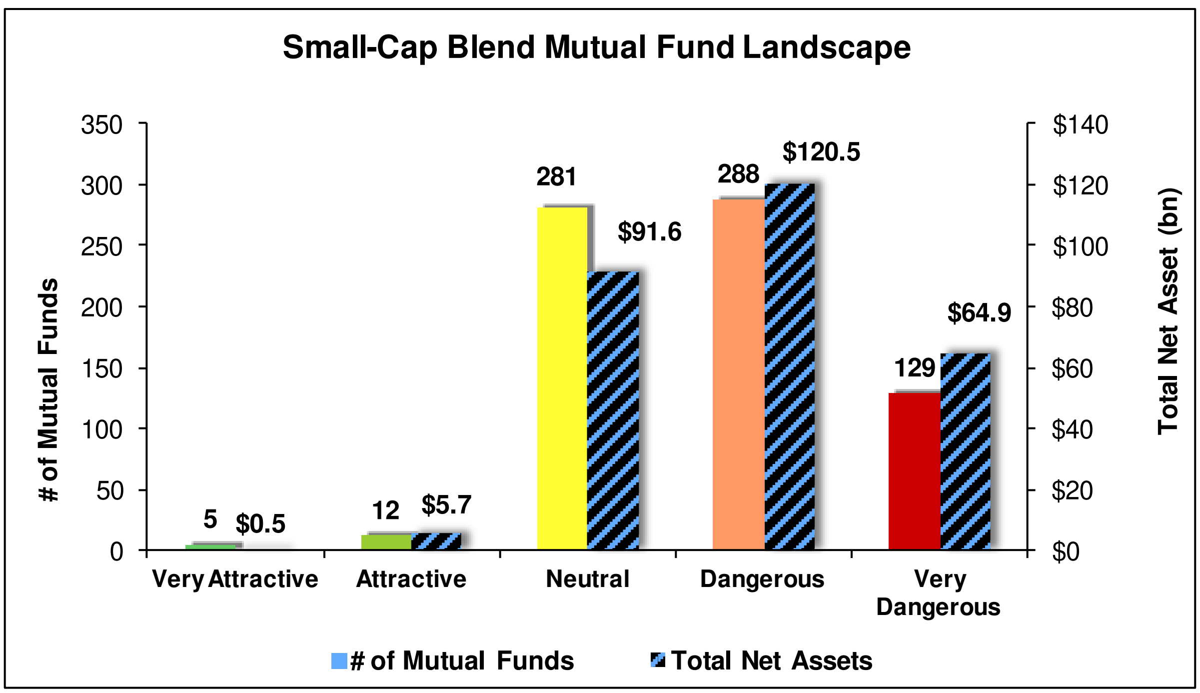
Figures 3 and 4 show the rating landscape of all Small Cap Blend ETFs and mutual funds.

Figure 3: Separating the Best ETFs From the Worst Funds



Sources: New Constructs, LLC and company filings

Figure 4: Separating the Best Mutual Funds From the Worst Funds



Sources: New Constructs, LLC and company filings

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Disclosure: David Trainer and Kyle Martone receive no compensation to write about any specific stock, style, or theme.

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We find it. You benefit. Cutting-edge technology enables us to scale our forensic accounting expertise across 3000+ stocks. We shine a light in the dark corners of SEC filings so our clients can make safer, more informed decisions.

Our stock rating methodology instantly informs you of the quality of the business and the fairness of the stock's valuation. We do the diligence on earnings quality and valuation so you don't have to.

In-depth risk/reward analysis underpins our ratings. Our rating methodology grades every stock, ETF, and mutual fund according to what we believe are the 5 most important criteria for assessing the quality of an equity. Each grade reflects the balance of potential risk and reward of buying that equity. Our analysis results in the 5 ratings described below. Very Attractive and Attractive correspond to a "Buy" rating, Very Dangerous and Dangerous correspond to a "Sell" rating, while Neutral corresponds to a "Hold" rating.

QUESTION: Why shouldn't fund research be as good as stock research? Why should fund investors rely on backward-looking price trends?

ANSWER: They should not.

Don't judge a fund by its cover. Take a look inside at its holdings and understand the quality of earnings and valuation of the stocks it holds. We enable you to choose the best fund based on its stock-picking merits so you do not have to rely solely on backward-looking technical metrics.

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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.

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