



ETF & Mutual Fund Rankings: Materials Sector

The Materials sector ranks sixth out of the ten sectors as detailed in our [4Q16 Sector Ratings for ETFs and Mutual Funds](#) report. [Last quarter](#), the Materials sector ranked fifth. It gets our Dangerous rating, which is based on an aggregation of ratings of 10 ETFs and 11 mutual funds in the Materials sector as of October 17, 2016. See a recap of our [3Q16 Sector Ratings here](#).

Figure 1 ranks from best to worst the nine Materials ETFs that meet our liquidity standards and Figure 2 shows the five best and worst-rated Materials mutual funds. Not all Materials sector ETFs and mutual funds are created the same. The number of holdings varies widely (from 23 to 121). This variation creates drastically different investment implications and, therefore, ratings.

Investors should not buy any Materials ETFs or mutual funds because none get an Attractive-or-better rating. If you must have exposure to this sector, you should buy a basket of Attractive-or-better rated stocks and avoid paying undeserved fund fees. Active management has a [long history](#) of not paying off.

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 (only 4)				
XLB	4%	38%	55%	Neutral
SLX	0%	17%	53%	Neutral
IYM	5%	40%	52%	Neutral
FXZ	12%	31%	54%	Neutral
Worst ETFs				
FMAT	4%	38%	53%	Dangerous
VAW	4%	38%	53%	Dangerous
PSCM	2%	25%	57%	Dangerous
PYZ	0%	50%	50%	Dangerous
XME	0%	9%	91%	Dangerous

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

Sources: New Constructs, LLC and company filings

Guggenheim S&P 500 Equal Weight Materials ETF (RTM) is excluded from Figure 1 because its 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				
FMFEX	6%	28%	47%	Neutral
FSDPX	6%	28%	47%	Neutral
FSCHX	8%	35%	37%	Neutral
FMFCX	6%	28%	47%	Neutral
VMIAX	4%	38%	52%	Dangerous
Worst Mutual Funds				
RYBAX	4%	31%	50%	Dangerous
FMFTX	6%	28%	47%	Dangerous
FMFAX	6%	28%	47%	Dangerous
RYBCX	4%	31%	50%	Very Dangerous
RYBMX	4%	31%	50%	Very Dangerous

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

Sources: New Constructs, LLC and company filings

Materials Select Sector SPDR Fund (XLB) is the top-rated Materials ETF and Fidelity Advisor Materials Fund (FMFEX) is the top-rated Materials mutual fund. Both earn a Neutral rating.

SPDR S&P Metals & Mining ETF (XME) is the worst rated Materials ETF and Rydex Basic Materials Fund (RYBMX) is the worst rated Materials mutual fund. XME earns a Dangerous rating and RYBMX earns a Very Dangerous rating.

157 stocks of the 3000+ we cover are classified as Materials stocks.

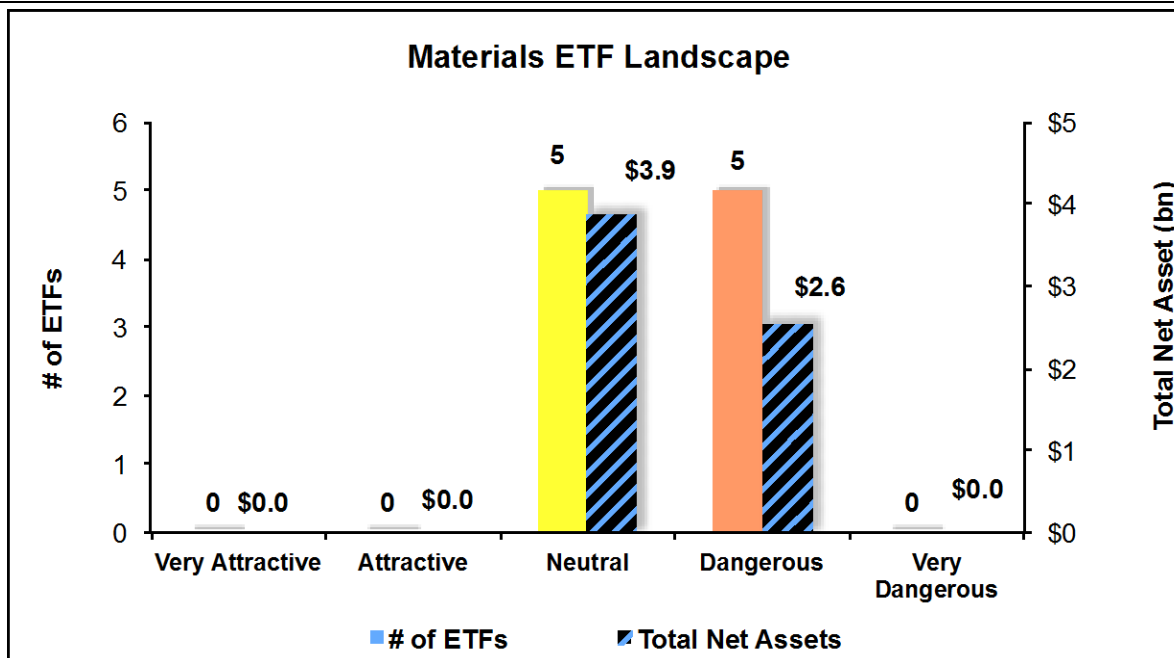
LyondellBasell Industries NV (LYB: \$80/share) is one of our favorite stocks held by Materials ETFs and mutual funds and earns a Very Attractive rating. Since 2011, LYB has grown after-tax profit ([NOPAT](#)) by 10% compounded annually. The company has improved its return on invested capital ([ROIC](#)) from 17% in 2011 to a top-quintile 20% over the last twelve months (TTM). Despite the improving fundamentals, LYB remains undervalued. At its current price of \$80/share, LYB has a price-to-economic book value ([PEBV](#)) ratio of 0.8. This ratio means the market expects LYB's NOPAT to permanently decline by 20%. If LYB can [grow NOPAT by just 3% compounded annually for the next decade](#), the stock is worth \$130/share today – a 63% upside.

Kraton Corporation (KRA: \$34/share) is one of our least favorite stocks held by Materials ETFs and mutual funds and earns a Very Dangerous rating. Kraton's [economic earnings](#) have declined from \$39 million in 2010 to -\$50 million TTM. The company's ROIC has declined from 13% in 2010 to a bottom-quintile 3% TTM. Despite the deterioration in business fundamentals, KRA is priced for significant profit growth. To justify its current price of \$34/share, KRA must [grow NOPAT by 20% compounded annually for the next decade](#). This expectation seems overly optimistic given Kraton's NOPAT has declined by 20% compounded annually over the past five years.



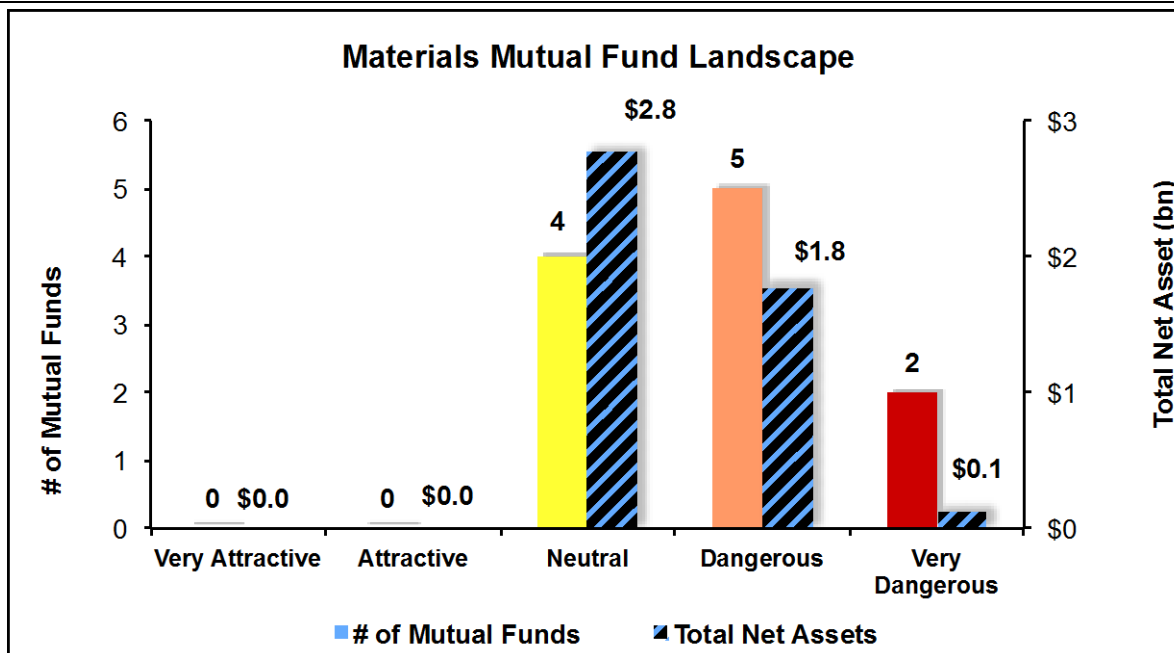
Figures 3 and 4 show the rating landscape of all Materials ETFs and mutual funds.

Figure 3: Separating the Best ETFs From the Worst ETFs



Sources: New Constructs, LLC and company filings

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



Sources: New Constructs, LLC and company filings

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



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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.

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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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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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