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 4Q16 Style Ratings for ETFs and Mutual Funds report. Last quarter, the Small Cap Blend style ranked tenth as well. It gets our Dangerous rating, which is based on an aggregation of ratings of 24 ETFs and 749 mutual funds in the Small Cap Blend style as of November 8, 2016. See a recap of our 3Q16 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 2110). 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				
EES	18%	32%	35%	**Attractive**
IJR	11%	35%	46%	**Neutral**
VIOO	10%	34%	45%	**Neutral**
SLY	11%	35%	46%	**Neutral**
FNDA	14%	32%	48%	**Neutral**
Worst ETFs				
NASH	13%	27%	43%	**Neutral**
RWJ	11%	33%	46%	**Neutral**
EQWS	9%	19%	45%	**Dangerous**
SMDV	7%	40%	53%	**Dangerous**
RWK	16%	38%	42%	**Dangerous**

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

Sources: New Constructs, LLC and company filings

Validea Market Legends ETF (VALX) and Victory CEMP US Discovery Enhanced Volatility ETF (CSF) 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

Ticker	Allocation of Mutual Fund Holdings: Attractive-or-better Stocks	Neutral Stocks	Dangerous-or-worse Stocks	Predictive Rating
Best Mutual Funds				
BOSOX	31%	47%	16%	Very Attractive
VSENX	11%	41%	31%	Attractive
JSERX	11%	41%	31%	Attractive
JSEQX	11%	41%	31%	Neutral
VSEIX	11%	41%	31%	Neutral
Worst Mutual Funds				
RSPFX	6%	24%	49%	Very Dangerous
AESAX	10%	23%	47%	Very Dangerous
WFSMX	2%	19%	57%	Very Dangerous
TFSSX	8%	29%	39%	Very Dangerous
BRDAX	6%	20%	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.

WisdomTree SmallCap Earnings Fund (EES) is the top-rated Small Cap Blend ETF and Boston Trust Small Cap Fund (BOSOX) is the top-rated Small Cap Blend mutual fund. EES earns an Attractive rating and BOSOX earns a Very Attractive rating.

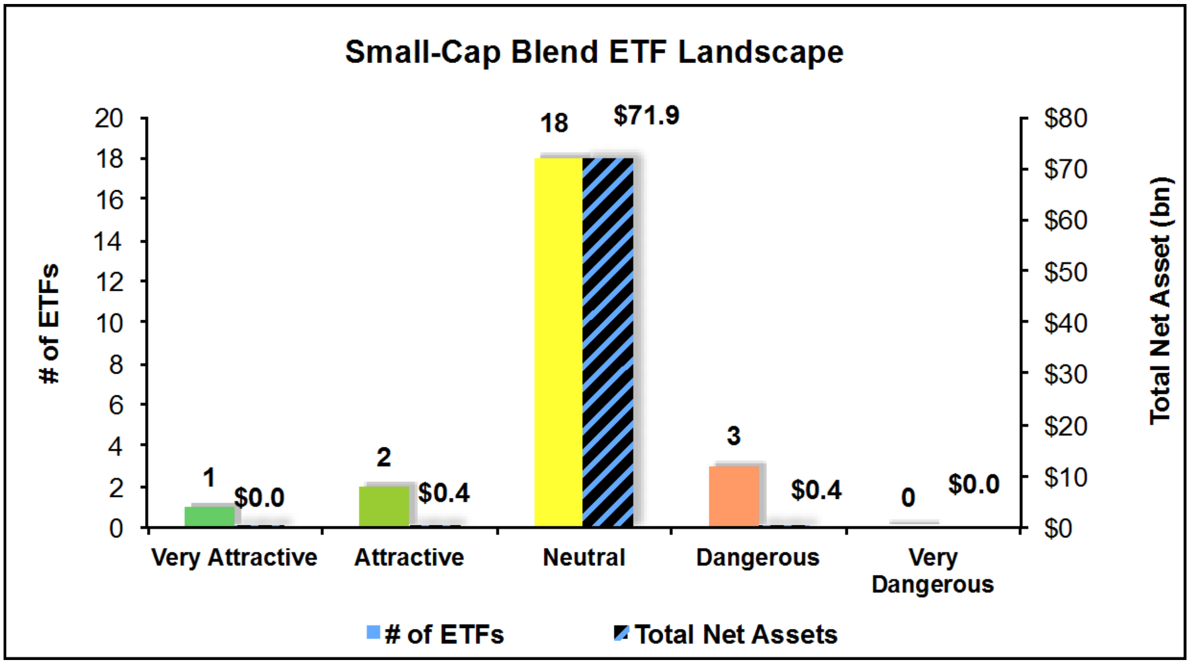
Oppenheimer Mid Cap Revenue ETF (RWK) is the worst rated Small Cap Blend ETF and B. Riley Diversified Equity Fund (BRDAX) is the worst rated Small Cap Blend mutual fund. RWK earns a Dangerous rating and BRDAX earns a Very Dangerous rating.

Sanderson Farms (SAFM: $92/share) is one of our favorite stocks held by EES and earns an Attractive rating. SAFM was also a featured Long Idea in August 2015. Over the past decade, Sanderson Farms has grown after tax profit (NOPAT) by 12% compounded annually. The company has improved its return on invested capital (ROIC) from 7% in 2012 to 13% over the trailing twelve months (TTM). Despite the improvement in the underlying economics of the business, SAFM remains undervalued. At its current price of $92/share, SAFM has a price-to-economic book value (PEBV) ratio of 0.9. This ratio means the market expects SAFM's NOPAT to permanently decline by 10%. If SAFM can grow NOPAT by just 3% compounded annually over the next decade, the stock is worth $140 today – a 52% upside.

Mack-Cali Reality Corp (CLI: $25/share) is one of our least favorite stocks held by TFSSX and earns a Very Dangerous rating. Over the five years alone, CLI's NOPAT has declined from $210 million in 2011 to -$15 million TTM. The company's ROIC has fallen from 5% in 2011 to a bottom-quintile 0% TTM. Worse yet, CLI has not generated positive economic earnings in any year of our model, which dates back to 1998. Despite the deteriorating fundamentals, CLI remains overvalued. To justify its current price of $26/share, CLI must immediately achieve 10% NOPAT margins (compared to -3% TTM) and grow revenue by 15% compounded annually for the next 17 years.

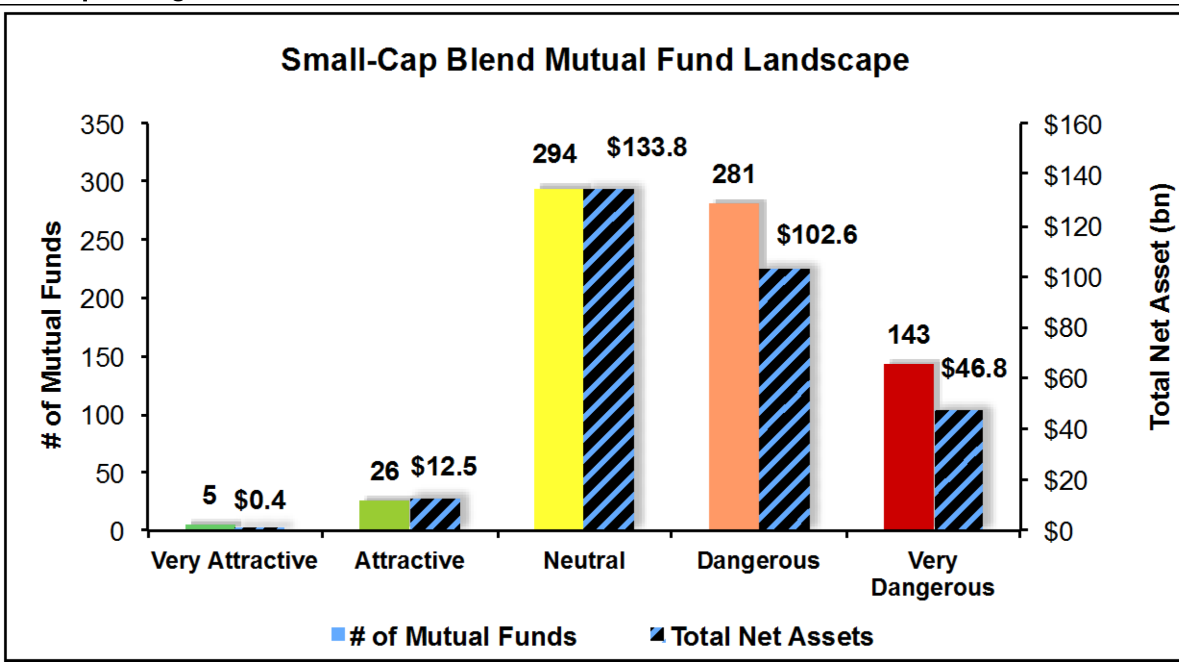
Figures 3 and 4 show the rating landscape of all Small Cap Blend ETFs and mutual funds.

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, Kyle Guske 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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