



Filing Season Finds: Friday, March 10

Our latest forensic accounting red flag is from a struggling small-cap stock that only looks more dangerous the deeper you dig.

We pulled this highlight from yesterday's research of 42 10-K filings, from which our [robo-analyst](#) technology collected 5,533 data points. Our analyst team used this data to make 965 forensic accounting [adjustments](#) with a dollar value of \$108 billion. The adjustments were applied as follows:

- 400 income statement adjustments with a total value of \$7 billion
- 412 balance sheet adjustments with a total value of \$42 billion
- 152 valuation adjustments with a total value of \$60 billion

Figure 1: Filing Season Diligence

	Filings Parsed	Data Points Collected	# of Adjustments	Total Value of Adjustments (\$Billions)
Yesterday	42	5,533	965	\$108
Filing Season Total	1,466	209,761	35,722	\$12,367

Sources: New Constructs, LLC and company filings.

We believe this research is necessary to close the gap between the suitability and [fiduciary standard](#) of investment advice services.

Today's Forensic Accounting Needle In A Haystack Is For Consumer Discretionary Investors

Analyst Alec Estrada found an unusual item yesterday in Ascent Capital Group's (ASCMA) 10-K.

On [page 32](#), ASCMA revealed that the revaluation of a dealer liability in 4Q16 earned the company \$7.2 million in [hidden non-operating income](#) (13% of reported operating income). Sure enough, eliminating this unusual item shows that ASCMA's 13% increase in reported operating income was entirely artificial. Net operating profit after tax ([NOPAT](#)) was essentially flat at ~\$55 million in 2016.

With \$1.8 billion in [total debt](#), ASCMA needs to grow its cash flows significantly to keep up with interest payments. Our research in the footnotes sheds a light on ASCMA's stagnant cash flows and suggests that liquidation may be in its future.

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Disclosure: David Trainer, Alec Estrada, and Sam McBride receive no compensation to write about any specific stock, sector, style, 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.

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.

The drivers of our [forward-looking fund ratings](#) are Portfolio Management (i.e. the aggregated ratings of its holdings) and Total Annual Costs. The Total Annual Costs Rating ([details here](#)) captures the all-in cost of being in a fund over a 3-year holding period, the average period for all fund investors.

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.

Additional Information

Incorporated in July 2002, [New Constructs](#) is an independent publisher of investment research that provides clients with consulting and research services. We specialize in quality-of-earnings, forensic accounting and discounted cash flow valuation analyses for all U.S. public companies. We translate accounting data from 10Ks into economic financial statements, i.e. [NOPAT](#), [Invested Capital](#), and [WACC](#), to create [economic earnings models](#), which are necessary to understand the true profitability and valuation of companies. Visit the [Free Archive](#) to download samples of our research. New Constructs is a [BBB accredited](#) business and a member of the [Investorside Research Association](#).

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