



## Filing Season Finds: Week Of March 4-10

Our latest featured stock is an oil giant whose reported earnings and real cash flows are heading in opposite directions.

Last week, our analysts parsed 452 filings and collected 58,771 data points. In total, they made 9,978 [adjustments](#) with a dollar value of \$1.5 trillion. That breaks down into:

- 4,279 income statement adjustments with a total value of \$101 billion
- 4,051 balance sheet adjustments with a total value of \$605 billion
- 1,648 valuation adjustments with a total value of \$748 billion

**Figure 1: Filing Season Diligence**

	Filings Parsed	Data Points Collected	# of Adjustments	Total Value of Adjustments (\$Billions)
Last Week	452	58,771	9,978	\$1,454
Filing Season Total	1,530	217,567	37,078	\$12,917

Sources: New Constructs, LLC and company filings.

During the past week of [filing season](#), we found [significant non-operating expenses](#) from Guidance Software (GUID), a big [change in expected return on plan assets](#) for Target (TGT), and [several red flags](#) for [Valeant Pharmaceuticals](#) (VRX). Follow us on [Twitter](#) and check out the hashtag [#filingseasonfinds](#) for regular updates on our research.

Every year in this six-week stretch from mid-February through the end of March we parse and analyze roughly 2,000 10-Ks to update our [models](#) for companies with a 12/31 fiscal year end. This effort is made possible by the combination of expertly trained human analysts with what we call the “[Robo-Analyst](#).” The Robo-Analyst uses machine learning and natural language processing to automate much of the parsing process.

### A Fiduciary Level of Diligence

Our technology enables us to deliver fundamental diligence at a previously impossible scale. We believe that in time investors will come to demand this level of diligence when it comes to their investment advice.

Only by reading through the footnotes and making adjustments to [reverse accounting distortions](#) can advisors go beyond the suitability standard and provide a fiduciary level of diligence to their clients.

### One Company To Watch In 2017

Based on our analysis of the Royal Dutch Shell’s (RDS.A) 20-F (the international equivalent of a 10-K) last week, we have downgraded the stock from Dangerous to Very Dangerous.

Analyst Hunter Gray made a number of adjustments to account for hidden non-operating expenses in Shell’s 20-F, including:

- Impairment losses of \$1.9 billion on [page 129](#)
- Inventory [write-downs](#) of \$566 million on [page 136](#)
- Non-operating pension charges of \$169 million on [page 141](#)

This may seem like good news for Shell, until we look at its 2015 20-F and see that those non-operating expenses were \$9.3 billion, \$1.1 billion, and \$656 million in 2015.

Shell’s GAAP EPS rose by 91% in 2016, but that increase was entirely the result of the non-operating expenses artificially depressing its profitability in 2015. Shell’s net operating profit after tax ([NOPAT](#)) actually declined by 3% last year.



Investors betting on Shell's recovery need to look past the income statement to see that cash flows are in decline.

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*Disclosure: David Trainer, Hunter Gray, and Sam McBride receive no compensation to write about any specific stock, sector, style, or theme.*

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### ***How New Constructs Creates Value for Clients***

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.

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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