



Model Portfolio: August 2017: Exec Comp Aligned With ROIC

15 Large/Mid/Small Cap Stocks

Trust

We deliver the whole truth by incorporating critical data from the Financial Footnotes and MD&A that other firms miss.

Performance

The value and success of our ratings are noteworthy. See media features and accolades.

More Reports

Click here to access our research and become a member.



- Figure 1 shows five new stocks that make our August list.
- The Executive Compensation Aligned With ROIC Portfolio (-3.9%) underperformed the S&P 500 (+0.7%) last month.
- Since inception, this model portfolio is up 17% while the S&P 500 is up 18%.
- Figure 8 shows the four stocks that outperformed from July's report.
- The stocks in this model portfolio earn an Attractive or Very Attractive rating. All of the companies have executive compensation plans that are aligned with return on invested capital (ROIC).
- ROIC is by far the [biggest driver](#) of stock valuation.

Figure 1: Additions for August

Portfolio Additions	
Ticker	Company Name
CULP	Culp Inc.
ESRX	Express Scripts Inc.
PLXS	Plexus Corporation
SMP	Standard Motor Products
STX	Seagate Technology

Sources: New Constructs, LLC

This model portfolio is updated around the 15th of every month.

Please see Appendix B for explanations of additions and deletions to the [Executive Compensation Aligned With ROIC Model Portfolio](#).

The 5 “Accurate ROIC Calculation/Strong Alignment with Exec Comp” Stocks for August

We recommend that investors equal-weight holdings in all 5 stocks.

Figure 2: 5 Accurate ROIC Calculation/Strong Alignment with Exec Comp Stocks for August

			High-Quality Earnings		Cheap Valuation				Executive Compensation Plans Aligned with ROIC
			As of Last Twelve Months		as of 8/14/17				
Ticker	Company Name	Sector	Positive Economic EPS	Return On Invested Capital (ROIC)	Positive Free Cash Flow Yield	Low Price-to-Economic Book Value	Short Market-Implied GAP (years)	Market Value (\$mm)	Proxy Statement
NVR	NVR Inc.	Consumer Discretionary	\$102.49	21%	4%	1.2	1	\$10,265	NVR Proxy Statement
KMB	Kimberly-Clark Corp	Consumer Staples	\$4.79	17%	4%	1.1	2	\$42,993	KMB Proxy Statement
CBRL	Cracker Barrel Old Country	Consumer Discretionary	\$6.76	14%	5%	0.9	Less than 1	\$3,682	CBRL Proxy Statement
SMP*	Standard Motor Products	Consumer Discretionary	\$1.72	12%	4%	0.9	Less than 1	\$1,042	SMP Proxy Statement
CULP*	Culp Inc.	Consumer Discretionary	\$0.87	11%	4%	0.9	Less than 1	\$346	CULP Proxy Statement

* Addition to the list in August

Stocks are ranked by ROIC in Descending Order

Sources: New Constructs, LLC

The 5 “Flawed ROIC Calculation/Strong Alignment with Exec Comp” Stocks for August

We recommend that investors equal-weight holdings in all 5 stocks.

Figure 3: 5 Flawed ROIC Calculation/Strong Alignment with Exec Comp Stocks for August

			High-Quality Earnings		Cheap Valuation				Executive Compensation Plans Aligned with ROIC
			As of Last Twelve Months		as of 8/14/17				
Ticker	Company Name	Sector	Positive Economic EPS	Return On Invested Capital (ROIC)	Positive Free Cash Flow Yield	Low Price-to-Economic Book Value	Short Market-Implied GAP (years)	Market Value (\$mm)	Proxy Statement
HAS	Hasbro Inc.	Consumer Discretionary	\$3.46	17%	5%	1.1	2	\$12,288	HAS Proxy Statement
STX*	Seagate Technology	Information Technology	\$2.30	17%	15%	0.7	Less than 1	\$9,499	STX Proxy Statement
GWW	W.W. Grainger Inc.	Industrials	\$8.01	14%	8%	0.8	Less than 1	\$9,634	GWW Proxy Statement
IIN	Insteel Industries	Industrials	\$0.56	11%	1%	1.2	2	\$490	IIN Proxy Statement
PLCE	Childrens Place	Consumer Discretionary	\$3.91	11%	7%	0.8	Less than 1	\$1,828	PLCE Proxy Statement

* Addition to the list in August

Stocks are ranked by ROIC in Descending Order

Sources: New Constructs, LLC

The 5 “Weak Alignment with Exec Comp” Stocks for August

We recommend that investors equal-weight holdings in all 5 stocks.

Figure 4: 5 Weak Alignment with Exec Comp Stocks for August

			High-Quality Earnings		Cheap Valuation				Executive Compensation Plans Aligned with ROIC
			As of Last Twelve Months		as of 8/14/17				
Ticker	Company Name	Sector	Positive Economic EPS	Return On Invested Capital (ROIC)	Free Cash Flow Yield	Low Price-to-Economic Book Value	Short Market-Implied GAP (years)	Market Value (\$mm)	Proxy Statement
SBUX	Starbucks Corporation	Consumer Discretionary	\$1.70	23%	4%	1.6	5	\$76,844	SBUX Proxy Statement
ORLY	O'Reilly Automotive	Consumer Discretionary	\$9.28	21%	5%	1.0	Less than 1	\$17,466	ORLY Proxy Statement
ABC	AmerisourceBergen	Health Care	\$4.94	16%	5%	0.7	Less than 1	\$17,546	ABC Proxy Statement
ESRX*	Express Scripts	Health Care	\$3.42	11%	9%	0.6	Less than 1	\$35,410	ESRX Proxy Statement
PLXS*	Plexus Corporation	Information Technology	\$1.36	10%	4%	0.9	Less than 1	\$1,717	PLXS Proxy Statement

* Addition to the list in August

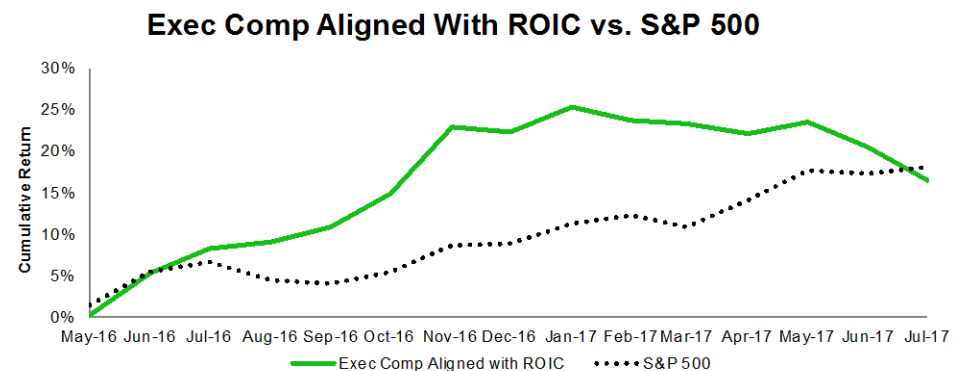
Stocks are ranked by ROIC in Descending Order

Sources: New Constructs, LLC



Exec Comp Aligned With ROIC: Overall Performance

Per Figure 5, The Exec Comp Aligned with ROIC Portfolio has underperformed since inception in May 2016. Since then, the Exec Comp Aligned with ROIC Portfolio has cumulative returns of 17% compared to 18% for the S&P 500. A detailed breakdown of last month's performance can be seen on the next page.

Figure 5: Performance of Exec Comp Aligned With ROIC Model Portfolio

Sources: New Constructs, LLC

Note: Gain/Deline performance analysis excludes transaction costs and dividends.

Figure 6: Monthly Return of Exec Comp Aligned With ROIC

	Portfolio Returns					
	2Q16	3Q16	4Q16	1Q17	2Q17	17-Jul
Exec Comp Aligned With ROIC	5.3%	5.6%	11.4%	1.1%	-2.9%	-3.9%
SP 500	5.4%	-1.4%	5.0%	2.0%	6.4%	0.7%

Sources: New Constructs, LLC

Note: Gain/Deline performance analysis excludes transaction costs and dividends.

Figure 7: Cumulative Return of Exec Comp Aligned With ROIC

	Cumulative Portfolio Returns					
	2Q16	3Q16	4Q16	1Q17	2Q17	17-Jul
Exec Comp Aligned With ROIC	5%	11%	22%	23%	21%	17%
S&P 500	5%	4%	9%	11%	17%	18%

Sources: New Constructs, LLC

Note: Gain/Deline performance analysis excludes transaction costs and dividends.

Exec Comp Aligned With ROIC: Monthly Updates

The [Exec Comp Aligned With ROIC Portfolio](#) (-3.9%) underperformed the S&P 500 (+0.7%) last month. Four stocks from our July Exec Comp Aligned With ROIC lists outperformed the S&P 500, and four stocks had positive returns. See Figure 8 for details. For updates on the performance of all of last month's stocks, see Appendix A. We measure our July performance based on closing prices from July 13, 2017 to August 14, 2017. We published last month's report to subscribers on July 13, 2017.

Figure 8: Four Stocks That Outperformed From July's Report

Exec Comp Aligned With ROIC		
Ticker	Company Name	Change From 7/13/17
NVR	NVR Inc.	8.5%
ORLY	O'Reilly Automotive Inc.	7.5%
SBH	Sally Beauty Holdings	3.6%
FL	Foot Locker	1.5%
S&P 500	S&P 500	0.7%

Sources: New Constructs, LLC

Note: Gain/Decline performance analysis excludes transaction costs and dividends.



Exec Comp Aligned With ROIC: Methodology

Stocks on the Exec Comp Aligned With ROIC list must earn an Attractive or Very Attractive rating. Stocks earn an Attractive or Very Attractive rating when they have:

1. **High-Quality Earnings** based on:

- Returns on Invested Capital that are rising; and
- Economic Earnings/Cash Flows that are positive.

AND

2. **Cheap Valuations** based on:

- Free-Cash Flow Yields¹ that are positive;
- Price-to-Economic Book Value (EBV)² ratios that are relatively low; and
- Growth Appreciation Periods³ (GAP) that are relatively low.

Figure 9 shows our Risk/Reward Rating analysis, which we apply to each of the 3000+ companies that we cover. Stocks get a grade of 1 to 5 for each criterion, 5 being the worst and 1 being the best score. The Overall score is based on the average score of all five criteria. Stocks must get an average score of 1.4 or below to be rated Very Attractive.

Figure 9: New Constructs Risk/Reward Rating for Stocks

Risk/Reward Rating ⑦	Quality of Earnings		Valuation		
	Econ vs Reported EPS ⑧	ROIC ⑨	FCF Yield ⑩	Price to EBV ⑪	GAP ⑫
Very Unattractive	Misleading Trend	Bottom Quintile	< -5%	> 3.5 or < -1	> 50
Unattractive	False Positive	4th Quintile	-5% < -1%	2.4 < 3.5 or < -1	20 < 50
Neutral	Neutral EE	3rd Quintile	-1% < 3%	1.6 < 2.4	10 < 20
Attractive	Positive EE	2nd Quintile	3% < 10%	1.1 < 1.6	3 < 10
Very Attractive	Rising EE	Top Quintile	> 10%	0 < 1.1	0 < 3

Sources: New Constructs, LLC

Up to 15 stocks can make it into this model portfolio. These 15 stocks are broken into three groups of five:

- Group 1: fairly accurate calculations of ROIC and strong alignment with executive compensation.
- Group 2: question marks over their ROIC calculations but good alignment with executive compensation.
- Group 3: weak alignment with executive compensation and put more value on metrics such as EPS.

¹ Free-Cash Flow Yields measure the % of the total value of the firm for which the Free Cash Flows of the firm account. The formula is FCF/Current Enterprise Value.

² Economic Book Value (EBV) measures the no-growth value of the business based on its annual after-tax cash flow. The Formula for EBV is: (NOPAT / WACC) + Excess Cash + Non-operating assets – Debt (incl. Operating Leases) - Value of Outstanding Stock Options – Minority Interests.

³ Growth Appreciation Period measures the number of years, implied by the market-price, that a company will grow its economic earnings. This measure assigns a numerical value to the width of the moat around a firm's business.



Ultimately, any alignment between executive compensation and ROIC is better than none, but by using superior calculations and aligning a larger percentage of compensation with ROIC, the stocks in Group 1 do the best job of incentivizing shareholder value creation.

To be fair, calculating an accurate ROIC is not easy by any means. We have spent millions of dollars on technology to help us collect and model data as accurately as is humanly possible; so our standards are a little high. Still, we think investors should have high standards in this area.

For more on the methodology behind the Exec Comp Aligned With ROIC Model Portfolio, [click here](#).



Explanation of Risk/Reward Rating System

Our Risk/Reward Rating System assigns a rating to every stock under our coverage according to what we believe are the 5 most important criteria for assessing the risk versus reward of stocks. See table that follows for details.

Risk/Reward Ranking	The Risk/Reward Ranking provides a final rating based on the equal-weighted average rating of each criterion.
Very Unattractive	FCF Yield is not included in the average.
Unattractive	FCF Yield is not included in the average.
Neutral	All criteria are equal-weighted in the average calculation.
Attractive	All criteria are equal-weighted in the average calculation.
Very Attractive	All criteria are equal-weighted in the average calculation.

Economic vs Reported EPS	Rates stocks based on how their Economic Earnings compare to their Reported Earnings. Values based on Latest Fiscal Year.
Very Unattractive	Negative and declining Economic Earnings despite positive and rising Reported Earnings
Unattractive	Same as above except Reported Earnings are not rising or Reported Earnings are not positive
Neutral	Negative Economic and Reported Earnings
Attractive	Economic Earnings are positive
Very Attractive	Economic Earnings are positive and rising

Return on Invested Capital (ROIC)	Rates stocks based on their ROIC. Values based on Latest Fiscal Year.
Bottom Quintile	Very Unattractive = the bottom 20% of Russell 1000 companies
4th Quintile	Unattractive = the bottom 40% of Russell 1000 companies
3rd Quintile	Neutral = the middle 20% of Russell 1000 companies
2nd Quintile	Attractive = the top 40% of Russell 1000 companies
Top Quintile	Very Attractive = the top 20% of Russell 1000 companies

FCF Yield	Rates stocks based on their Free Cash Flow Yield. Values based on Latest Closing Stock price and Latest Fiscal Year.
<-5%	Very Unattractive = less than or equal to -5%
-5%<-1%	Unattractive = more than -5% but less than or equal to -1%
-1%<3%	Neutral = more than -1% but less than or equal to +3%
3%<10%	Attractive = more than +3% but less than or equal to +10%
>10%	Very Attractive = more than +10%



Price-to-EBV Ratio	Rates stocks based on their Price-to-Economic Book Value Ratio. Values based on Latest Closing Stock price and Latest Fiscal Year.
>3.5 or -1>0	Very Unattractive = greater than or equal to 3.5 or less than 0 but greater than -1
2.4>3.5 or <-1	Unattractive = greater than or equal to 2.4 but less than 3.5 and less than or equal to -1
1.6>2.4	Neutral = greater than or equal to 1.6 but less than 2.4
1.1>1.6	Attractive = greater than or equal to 1.1 but less than 1.6
0>1.1	Very Attractive = greater than or equal to 0 but less than 1.1

Growth Appreciation Period (yrs)	Rates stocks based on their Market-Implied Growth Appreciation Period. Values based on Latest Closing Stock price and Default Forecast Scenario.
>50	Very Unattractive = greater than or equal to 50 years
20>50	Unattractive = at least 20 years but less than 50
10>20	Neutral = at least 10 years but less than 20
3>10	Attractive = at least 3 years but less than 10
0>3	Very Attractive = at least 0 years but less than 3



Appendix A – Performance of Stocks on July's Report

Figure 10: Performance of All Stocks From July's Report

Exec Comp Aligned With ROIC		
Ticker	Company Name	Change From 7/13/17
NVR	NVR Inc.	8.5%
ORLY	O'Reilly Automotive Inc.	7.5%
SBH	Sally Beauty Holdings	3.6%
FL	Foot Locker	1.5%
S&P 500	S&P 500	0.7%
KBAL	Kimball International	-0.9%
GWW	W.W. Grainger	-1.8%
KMB	Kimberly-Clark Corp	-1.8%
LEA	Lear Corp	-3.1%
CBRL	Cracker Barrel Old Country Store	-3.6%
PLCE	Childrens Place	-3.9%
HOG	Harley-Davidson Inc.	-6.8%
SBUX	Starbucks Corporation	-8.8%
HAS	Hasbro Inc.	-12.1%
ABC	AmerisourceBergen Corp	-13.8%
IIIN	Insteel Industries	-23.1%
Portfolio Return		-3.9%

Sources: New Constructs, LLC

Note: Gain/Decline performance analysis excludes transaction costs and dividends.



Appendix B – Additions and Deletions

Accurate ROIC Calculation/Strong Alignment With Exec Comp

Deletions:

- FL - Displaced by improved rank of other stocks
- LEA - Displaced by improved rank of other stocks

Additions:

- CULP - Addition by improved rank over other stocks
- SMP - Addition by improved rank over other stocks

Flawed ROIC Calculation/Strong Alignment With Exec Comp

Deletions:

- KBAL - Expected to file 10-K within current month

Additions:

- STX - Addition by improved rank over other stocks

Weak Alignment With Exec Comp

Deletions:

- HOG - Displaced by improved rank of other stocks
- SBH - Displaced by improved rank of other stocks

Additions:

- ESRX - Addition by improved rank over other stocks
- PLXS - Addition by improved rank over other stocks

New Constructs® - Research to Fulfill the Fiduciary Duty of Care

Ratings & screeners on 3000 stocks, 450 ETFs and 7000 mutual funds help you make prudent investment decisions.

New Constructs leverages the latest in machine learning to analyze structured and unstructured financial data with unrivaled speed and accuracy. The firm's forensic accounting experts work alongside engineers to develop proprietary NLP libraries and financial models. Our investment ratings are based on the best fundamental data in the business for stocks, ETFs and mutual funds. Clients include many of the top hedge funds, mutual funds and wealth management firms. David Trainer, the firm's CEO, is regularly featured in the media as a thought leader on the fiduciary duty of care, earnings quality, valuation and investment strategy.

To fulfill the Duty of Care, research should be:

1. **Comprehensive** - All relevant publicly-available (e.g. 10-Ks and 10-Qs) information has been diligently reviewed, including footnotes and the management discussion & analysis (MD&A).
2. **Un-conflicted** - Clients deserve unbiased research.
3. **Transparent** - Advisors should be able to show how the analysis was performed and the data behind it.
4. **Relevant** - Empirical evidence must provide [tangible, quantifiable correlation](#) to stock, ETF or mutual fund performance.

Value Investing 2.0: Diligence Matters: Technology is Key to Value Investing With Scale

Accounting data is only the beginning of fundamental research. It must be translated into economic earnings to truly understand profitability and valuation. This translation requires deep analysis of footnotes and the MD&A, a process that our [robo-analyst technology](#) empowers us to perform for thousands of stocks, ETFs and mutual funds.



DISCLOSURES

New Constructs®, LLC (together with any subsidiaries and/or affiliates, "New Constructs") is an independent organization with no management ties to the companies it covers. None of the members of New Constructs' management team or the management team of any New Constructs' affiliate holds a seat on the Board of Directors of any of the companies New Constructs covers. New Constructs does not perform any investment or merchant banking functions and does not operate a trading desk.

New Constructs' Stock Ownership Policy prevents any of its employees or managers from engaging in Insider Trading and restricts any trading whereby an employee may exploit inside information regarding our stock research. In addition, employees and managers of the company are bound by a code of ethics that restricts them from purchasing or selling a security that they know or should have known was under consideration for inclusion in a New Constructs report nor may they purchase or sell a security for the first 15 days after New Constructs issues a report on that security.

DISCLAIMERS

The information and opinions presented in this report are provided to you for information purposes only and are not to be used or considered as an offer or solicitation of an offer to buy or sell securities or other financial instruments. New Constructs has not taken any steps to ensure that the securities referred to in this report are suitable for any particular investor and nothing in this report constitutes investment, legal, accounting or tax advice. This report includes general information that does not take into account your individual circumstance, financial situation or needs, nor does it represent a personal recommendation to you. The investments or services contained or referred to in this report may not be suitable for you and it is recommended that you consult an independent investment advisor if you are in doubt about any such investments or investment services.

Information and opinions presented in this report have been obtained or derived from sources believed by New Constructs to be reliable, but New Constructs makes no representation as to their accuracy, authority, usefulness, reliability, timeliness or completeness. New Constructs accepts no liability for loss arising from the use of the information presented in this report, and New Constructs makes no warranty as to results that may be obtained from the information presented in this report. Past performance should not be taken as an indication or guarantee of future performance, and no representation or warranty, express or implied, is made regarding future performance. Information and opinions contained in this report reflect a judgment at its original date of publication by New Constructs and are subject to change without notice. New Constructs may have issued, and may in the future issue, other reports that are inconsistent with, and reach different conclusions from, the information presented in this report. Those reports reflect the different assumptions, views and analytical methods of the analysts who prepared them and New Constructs is under no obligation to insure that such other reports are brought to the attention of any recipient of this report.

New Constructs' reports are intended for distribution to its professional and institutional investor customers. Recipients who are not professionals or institutional investor customers of New Constructs should seek the advice of their independent financial advisor prior to making any investment decision or for any necessary explanation of its contents.

This report is not directed to, or intended for distribution to or use by, any person or entity who is a citizen or resident of or located in any locality, state, country or jurisdiction where such distribution, publication, availability or use would be contrary to law or regulation or which would be subject New Constructs to any registration or licensing requirement within such jurisdiction.

This report may provide the addresses of websites. Except to the extent to which the report refers to New Constructs own website material, New Constructs has not reviewed the linked site and takes no responsibility for the content therein. Such address or hyperlink (including addresses or hyperlinks to New Constructs own website material) is provided solely for your convenience and the information and content of the linked site do not in any way form part of this report. Accessing such websites or following such hyperlink through this report shall be at your own risk.

All material in this report is the property of, and under copyright, of New Constructs. None of the contents, nor any copy of it, may be altered in any way, copied, or distributed or transmitted to any other party without the prior express written consent of New Constructs. All trademarks, service marks and logos used in this report are trademarks or service marks or registered trademarks or service marks of New Constructs.

Copyright New Constructs, LLC 2003 through the present date. All rights reserved.