OUR BEST IDEAS NEWSLETTER

Valuentum Securities
Stock Analysis: From Value through Momentum Investing

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Valuentum Securities Inc.
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Portfolio Return	Benchmark Return	Outperformance
59.5%	32.6%	26.8%

Portfolio Inception Date: May 17, 2011

Inside This Issue

Reshaping the Investor Psyche

By Brian Nelson, CFA

I remember Barack Obama's "Yes, we can" mantra in his 2008 presidential election run. He made people feel good about themselves; he made people feel like they were more than just a statistic; he made people believe that change could happen. He made us believe we could make a difference.

We find ourselves at a similar crossroads in investing history. During the past several decades as mutual funds proliferated and the thoughts of yester-year thinkers prevailed, the investment community adopted downright absurd notions that served the needs of financial institutions instead of investors. Buy-and-hold became an investing style. Timing the market became widely accepted as not viable. Technical and momentum analysis became voodoo. The use of a backward-looking star rating became a way to judge a mutual fund. Things, for the lack of a better phrase, got way out of whack.

Today, the investor psyche is being reshaped.

1) Investors now know that asset managers love buy-and-hold investors because financial institutions continue to reap fees on their investments without fear of asset flight. They now understand why most of the widely-disseminated research out there is geared toward spreading the word of a buy-and-hold strategy. Today, investors no longer ponder why asset managers want investors to accept (without question) the strategy of buy and hold…forever. **Investors are wising up to the true intentions of financial institutions.**

2) Investors are learning that timing the market is not only possible, it is inevitable--in fact, it is what every investor from Warren Buffett to David Einhorn to Carl Icahn is doing. When Mr. Buffett, for example, buys Burlington Northern or Heinz, he has waited for…

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= All Time High!

__Goals of our Best Ideas Newsletter__: At Valuentum, we task ourselves with a tall order. While most investment newsletters compare themselves to a market benchmark, we go one step further. We want to deliver positive returns to you, our subscriber, year after year, in addition to outperforming the market benchmark. Our best ideas portfolio is generally found on page 8 of each edition.

Reshaping the Investor Psyche…from the previous page

opportunity for Mr. Market to give him an entry point in these securities. He is not buying blindly – he is timing the market. 'You can't time the market' is now viewed as an excuse used by money managers to explain poor performance. Timing is everything! Investors are learning that those that say 'you can't time the market' have either zero experience in individual security selection or have failed miserably at timing the market in the past. **This tagline is no longer working - investors are now shunning those that say 'you can't time the market'. Yes, you and every investor can and does.**

3) A ton of academic research and empirical evidence has come to the forefront in recent years regarding the existence/efficacy of technical/momentum investing—even Eugene Fama, the father of modern finance, has credited momentum as the biggest embarrassment to market efficiency (a). Investors are reading about it -- they are putting two and two together. Can financial institutions generate investment banking fees from technical/momentum analysis? Nope. So, investors are learning why groundbreaking research in this area isn't getting much press. They're learning that financial institutions want to serve as many clients as possible. They are grasping the reasons why financial institutions tell investors to ignore price movements. They're learning that it's easier to tell customers to ignore price movements than actually address the questions of each and every deserving investor. **Investors are not standing for this anymore.**

4) Investors are learning about star ratings. They understand that backward-looking ratings are now more advertising and less substance. Investors are learning of the benefits funds receive from advertising a fancy star rating that shows its fund is better than peers (over the past 1, 3, and 5-year periods). But just as investors have suffered from the likes of Eastman Kodak or Lehman Brothers, they are learning that any star rating that is based entirely on past performance has little, if any practical value. Investors no longer want backward-looking analysis. They no longer want to drive their car down the expressway while looking through the rear-view mirror. They don't want to see their nest eggs erased or their college funds wiped out**. Investors are catching up to these shenanigans and demanding forward-looking assessments.** They're tired of losing money on yesterday's winners. They're demanding tomorrow's success stories.

You, a Valuentum member, wouldn't be reading this if you weren't reshaping the investor psyche, too. The days of financial institutions deceiving investors are over. Investing is being changed forever.

Yes, we can.

Learn the 13 Steps To Understand the Stock Market:

http://www.valuentum.com/articles/20121028

(a) "Of all the potential embarrassments to market efficiency, momentum is the primary one." Eugene Fama, the Robert R. McCormick Distinguished Service Professor of Finance at the University of Chicago GSB. Excerpt from: An Experienced View on the Markets and Investing; published in Financial Analyst Journal, Volume 68, Number 6. Page 18. November/December 2012.

Margins Will Drive Apple's iPhone 5S and 5C Outcome

By RJ Towner

Apple (AAPL) announced the release of its iPhone 5S and its even longer-awaited "cheap" iPhone 5C Tuesday, both of which we believe will be a big hit with consumers. The firm is also reportedly close to announcing a deal with China's largest mobile carrier, China Mobile, which will help Apple sell even more units.

Image Source: Apple

The iPhone 5C is one of the most anticipated products in Apple's history, and not because people thought it would be the best product ever, but rather because it is believed to be Apple's emerging-market solution. The phone will retail (unlocked) for $549, $100 below the price of the 5S.

The phone contains an internal steel construction and polycarbonate (plastic) encasing. The phone will also run iOS7, and it is roughly on par with the iPhone 5, technically speaking. Somewhat surprisingly, the phone will replace the 5 as the "middle phone," with the 4S model becoming the cheapest iPhone on the market ($450 unlocked, free on most major US carriers).

In our view, the pricing signals that the iPhone 5 had a poor gross margin profile, but we do not believe the same can or will be said about the 5C. Though we do not have access to precise gross margins from the company (nobody does at this time), we think 5C's gross margin is better than those of the 4S—Apple's previous highest-margin phone. And while we think the 5C won't cannibalize too many sales from other iPhone versions, the margin profile/differential could make cannibalization a positive for total gross margin dollars, and thus profits.

Still, we fully expect skeptics to attack the 5C on the basis of its still-hefty price tag, arguing that the phone is not yet priced for emerging-market success. In any case, Apple has left a lot of room with respect to price (given our assumptions regarding gross margins on the phone), and introducing its first emerging-market solution at a $549 price level will make another one rolled out in the future at a lower price even more attractive. Apple has long been successful at gauging consumer psychology, and this could be the first step at preserving its brand as it eases into lower-priced solutions.

*Margins Will Drive Apple's iPhone...*continued on next page

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The 5S

Image Source: Apple

Apple also did a fantastic job with the 5S, in our view. Though the 4S and 3GS had incremental upgrades, neither really provided that much of an incentive to upgrade from the 4 and 3G, respectively. The 5S is clearly superior to the 5, making it more likely that consumers opt to upgrade early or sell previous models to pay for the 5S.

By adding a fully functional fingerprint scanner to grant access, the 5S immediately becomes more attractive to enterprise customers that may fear phone theft and security breaches. This also hurts Blackberry's (BBRY) reputation as the leader in phone security.

Additionally, Apple has come out with its A7 processor for the iPhone 5S, giving the smartphone computing power on-par with a desktop computer and similar battery life to the 5. This chip allows the phone to have more realistic graphics for mobile gaming and better picture capture. The chip is probably an underestimated development as Apple could now become a more prominent player in video gaming. We believe it's even possible that the firm may be planning to get into the console wars at some point.

The iPhone 5S will also have a new M7 chip. The chip sounds like a tremendous value-add to the iPhone ecosystem. Here's Apple's own description:

> *"It's designed specifically to measure motion data from the accelerometer, gyroscope, and compass — a task that would normally fall to the A7 chip. But M7 is much more efficient at it. Now fitness apps that track physical activity can access that data from the M7 coprocessor without constantly engaging the A7 chip. So they require less battery power.*
>
> *M7 knows when you're walking, running, or even driving. For example, Maps switches from driving to walking turn-by-turn navigation if, say, you park and continue on foot. Since M7 can tell when you're in a moving vehicle, iPhone 5s won't ask you to join Wi-Fi networks you pass by. And if your phone hasn't moved for a while, like when you're asleep, M7 reduces network pinging to spare your battery."*

*Margins Will Drive Apple's iPhone...*continued on page 7

Is the New PayPal App a Game-Changer for eBay?

By RJ Towner

eBay's PayPal (EBAY) released the updated version of its iOS and Android mobile application. This release marks the latest attempt for a digital wallet to usurp the importance of the credit/debit card and "simplify" payments.

By no means is this the first attempt for a company to push a digital wallet. Google Wallet (GOOG) has failed to gain much traction, not because it is exclusive to Android, but mostly because it isn't a very intuitive program and awareness isn't high.

Apple's Passbook (AAPL) has snuck into the marketplace to become the fourth most popular mobile commerce app. Passbook differs from Google Wallet in the sense that it isn't used much for payments, but rather for boarding passes, sports tickets, and company loyalty cards. This is where the app actually adds value: consumers do not have to worry about printing a ticket or cluttering a wallet with a loyalty card.

So What About PayPal?

The new PayPal app has already garnered both positive and negative reviews. Overall, the product is definitely an improvement over previous iterations. New location services allow users to see which nearby businesses accept PayPal payments. A new photo feature lets users upload a photo for merchants to confirm purchases. Transferring money remains relatively straightforward.

As great as the new features are, the usefulness of the new features may be lacking. We tested out 'location services' to find local businesses, but we had a few issues. The most obvious issue was the wild measurement inaccuracy—off by several miles. The subsequent suggestions then became hard to identify. By comparison, Facebook's (FB) check-in feature suggested more relevant (and closer) locations.

Unfortunately, the other issue could do much more damage to the attractiveness of PayPal's digital wallet—acceptance remains low. Although this is likely to change, we think PayPal will still have a difficult time convincing retailers and consumers that a change from the status quo is necessary. This is one reason why we remain bullish on Best Ideas Newsletter portfolio holding Visa's (V) long-term prospects: the current system works exceptionally well, and there is no clamoring for change.

That's not to say change can't occur. No one really thought the CD player was so bad, but the MP3 and iPod quickly changed everyone's mind. The problem, in our view, is that the digital wallet simply isn't an upgrade from the existing payment infrastructure.

Some consumers will flock to the new payment system, and PayPal may even provide retailers with great incentives to accept mobile wallets, but the system simply isn't better than the tried-and-true credit card. Plus, consumers cannot stop carrying wallets since they need identification and (often) cash anyways, so the incremental impact of carrying a credit or debit card is extremely small. We won't dismiss the possibility of digital wallet success, but it may take a new form factor (smartwatch?) to make it a relatively more attractive alternative.

Valuentum's Take

The digital wallet could be the future of payments, but we do not believe the future is now. The existing payment infrastructure remains superior, in our view, so we do not see a mass exodus away from card payments anytime soon. The system isn't perfect (think splitting a check), so there could be opportunity for the digital wallet to compensate for the card's shortcomings. Of course, PayPal payments online continue to grow at a rapid clip, and PayPal seems likely to continue to dominate the space. Because we think the movement away from cash payments remains a powerful trend, we continue to hold shares of both eBay and Visa in the portfolio of our Best Ideas Newsletter.

Disclosure:

RJ Towner owns shares of the following companies mentioned in this article: AAPL, V

Pay TV Is Getting Friendly with Netflix

By RJ Towner

Since it successfully transitioned from a DVD rental service to a content streaming powerhouse, Netflix (NFLX) is now viewed as a major threat to pay TV. The story goes that consumers will eventually "cut the cord" and abandon pay TV while relying exclusively on Netflix and online video service Hulu for content. Though there are many reasons why we think this trend is overblown, Liberty Global's (LBTYA) Virgin Media has taken another step toward eliminating this competitive threat: Virgin subscribers will be able to access a Netflix app via TiVo set-top boxes.

Liberty Global is controlled by none other than media mogul John Malone. Malone is best known for his bold M&A deals throughout the years and has various holdings throughout the media distribution space, including a sizeable position in Best Ideas Newsletter portfolio holding DirecTV (DTV). Though he no longer sits as chairman of DirecTV, this deal could signal that other content distributors are viewing Netflix as a network partner rather than a competitor.

We think Virgin Media's move is a significant development. Netflix could begin to position itself closer to the likes of Time Warner's (TWX) HBO, becoming a premium Internet TV station (content producer) rather than a content distributor (purchaser). We've already seen Netflix take strides toward becoming a content producer with the likes of Arrested Development, Orange is the New Black, and House of Cards. Gaining access to TV audiences could give Netflix a broader reach and increase the firm's legitimacy as a content creator.

On top of lifting Netflix's fortunes, the integration with pay TV could help content distributors. With Netflix included, a pay TV offering becomes even more compelling, and more importantly, decreases the incentive for consumers to cut the cord. Importantly, if distributors help Netflix grow, Netflix may become even more interested in fighting content cost inflation.

Valuentum's Take

Though the situation isn't receiving too much press, we think Virgin Media's move could mark an interesting turning point in content distributors' view of non-pay TV competitors. Instead of distributors bidding endlessly for content, turning Netflix into a partner could help the cohort contain content costs. We hold shares of DirecTV in the portfolio of our Best Ideas Newsletter and continue believe Netflix is one of the most expensive stocks on the market today.

*Margins Will Drive Apple's iPhone…*from page 4

It is clear that the M7 lays the groundwork for the iWatch, particularly since it is designed to track movement while consuming less power. Historically, Apple has loved to tease users with potential new products, and this may be the first hint we receive that the iWatch is real. More importantly, it may suggest that the iWatch's battery life exceeds that of the ill-fated Galaxy Gear smartwatch.

With this load of upgrades, plus an improved camera, we believe Apple has successfully maintained product differentiation between the 5S and the 5C. There's no doubt that the 5S is the superior product, but the 5C is no slouch either.

Valuentum's Take

When it comes to Apple, it can be hard to draw a distinction between what the finance community and what the average consumer thinks. Investors are constantly viewing blogs, reading rumors, and essentially getting information about Apple products before the general public. This doesn't mean that Apple is "out of surprises" but rather it signifies how badly the investing public and Apple fans want information about Apple products before Apple reveals them.

For many consumers in the US, purchasing an iPhone every 2 years isn't a decision, but rather an afterthought. We think demand will continue to be strong for the iPhone, and we think the 5C and 5S carry stronger gross margins, which will help reaccelerate Apple's earnings expansion. The less expensive 5C and 4S could also be what are necessary for the firm to improve its performance in emerging markets like China without diluting the Apple brand.

Both phones also come with colorful cases that should fit the phone perfectly since the cases are made by Apple. These cases aren't expensive ($29 for the 5C and $39 for the 5S), but likely carry robust gross margins as well, helping the company take some of the revenue away from case designers that have made fortunes of the iPhone in the past. With margin upside possible in the near term, we continue to hold shares of the firm in both of our actively managed portfolios.

Are You Ready for Some Football? Google Is.

By Valuentum Analysts

Digital news firm AllThingsD broke the story that Best Ideas Newsletter portfolio holding Google (GOOG) could be in talks with the NFL over exclusive rights for the NFL Sunday Ticket package, which allows consumers to view every NFL game. Another Best Idea portfolio holding, DirecTV (DTV), currently holds exclusive rights for Sunday Ticket through the 2014 season, which costs the firm $1 billion annually.

Why It Makes Sense for Google

On the surface, such an idea seems interesting for Google. With the exclusive Sunday Ticket package, Google could really make a push into the TV business. Google could even pair the package with a purchase of the Google Chromecast, a portable online TV portal that launched with some hype, but since has faded into relative obscurity. Or, Google could make the NFL Sunday Ticket available via its Android operating system. This would be a clever way to get users into the Google ecosystem.

Why It Doesn't Make Sense for the NFL

It sounds great for Google, but we don't think the NFL will go for it. The Google Chromecast doesn't have nearly the reach of DirecTV's 20 million US subscriber base. Additionally, games not viewed on local networks don't count for Nielsen ratings, meaning ratings of games do not look as attractive if more viewers are watching on Sunday Ticket. If ratings look lower, advertising demand declines, hurting the local affiliates and the large TV networks that have forked over billions of dollars to secure exclusive rights. The companies that drive the NFL's revenue such as Fox (FOX, FOXA) and CBS (CBS) would not be happy with lower advertising revenue, which is the reason these companies paid for the rights in the first place.

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Our Best Ideas Portfolio

By Valuentum Analysts

Portfolio Return	Benchmark Return	Outperformance
59.5%	32.6%	26.8%

Portfolio Inception Date: May 17, 2011

= All Time High!

Below we outline the constituents of our portfolio and their respective weightings and returns thus far. Each subsequent issue discusses Valuentum's latest changes to the portfolio, a summary of new names on our watch list (please see page 21), as well as analysis and trends impacting companies in our Best Ideas portfolio. We currently have about 30% of our portfolio in cash, a level we're looking to bring down in coming months. Typically, we like to have the most cash when the market is making new highs and fully invested when the market is putting in short-term lows.

Our investment process is completely transparent and easy to implement in your own portfolio. The goal of our Best Ideas Newsletter is to outperform the S&P 500 Index and to generate positive returns each year regardless of the market environment. Firms added to our Best Ideas portfolio are the cream of the crop based on our stock-selection methodology.

OUR BEST IDEAS PORTFOLIO -- as of September 15, 2013								Best Ideas Portfolio Inception Date: May 17, 2011		
Portfolio Holdings	Symbol	Initial VBI*	Current VBI**	First Purchase	Cost Basis ($)	Total Shares	Price/Share ($)	Current Value ($)	% of Portfolio	% Return (dividends included)
Bullish										
Apple Corp.	AAPL	10	6	17-Jun-11	363.43	23	464.90	10,692.70	6.7%	30.6%
Altria Group	MO	8	6	28-Jun-11	26.43	252	34.84	8,779.68	5.5%	47.1%
Baidu	BIDU	10	10	1-Aug-13	133.60	20	142.64	2,852.80	1.8%	6.5%
Buffalo Wild Wings	BWLD	7	6	13-Jul-11	65.42	77	109.82	8,456.14	5.3%	67.6%
DirecTV	DTV	9	6	15-Apr-13	55.02	55	61.77	3,397.35	2.1%	12.0%
eBay	EBAY	10	3	3-Oct-11	31.04	100	53.82	5,382.00	3.4%	73.4%
Financial Select SPDR Fund	XLF	NA	6	9-Jan-11	13.46	150	20.20	3,030.00	1.9%	52.7%
Ford Motor	F	7	7	12-Sep-11	10.69	650	17.35	11,277.50	7.1%	65.1%
Google	GOOG	10	6	23-Oct-12	683.49	4	889.07	3,556.28	2.2%	29.7%
Health Care ETF	XLV	9	5	22-May-12	36.60	125	51.21	6,401.25	4.0%	42.5%
Intel	INTC	6	6	12-Sep-11	20.48	150	23.44	3,516.00	2.2%	20.4%
Intuitive Surgical	ISRG	5	3	22-May-12	489.51	7	375.00	2,625.00	1.6%	-23.5%
Precision Castparts	PCP	8	3	6-Jun-11	152.07	40	232.23	9,289.20	5.8%	52.7%
SPDR S&P Bank ETF	KBE	NR	NR	9-Jan-12	21.07	100	30.29	3,029.00	1.9%	46.7%
Republic Services	RSG	8	6	19-May-11	31.42	201	33.00	6,633.00	4.2%	13.2%
Rio Tinto	RIO	9	3	22-May-12	46.40	75	49.99	3,749.25	2.4%	12.9%
Teva Pharma	TEVA	6	6	24-Jul-13	41.22	77	38.34	2,952.18	1.9%	-6.4%
Union Pacific	UNP	6	6	24-Jul-13	159.34	20	154.75	3,095.00	1.9%	-2.6%
Visa	V	7	6	30-Nov-11	107.46	60	189.00	11,340.00	7.1%	77.1%
Cash								49,131.27	30.8%	0.0%
Bearish										
SPDR S&P 500 Trust ETF	SPY - put option		7	23-May-13	644.25	1	280.00	280.00	0.2%	-56.5%
---> $160 strike, December 2013 expiration										
Best Ideas Portfolio Value								**159,465.60**		**59.5%**
S&P 500 Index (SPY)				17-May-11	132.69	754	169.33	127,613.23	96.2%	
Cash								5,018.46	3.8%	
Benchmark Portfolio Value								**132,631.70**		**32.6%**
Relative Outperformance										**26.8%**

This portfolio is not a real money portfolio. Data as of September 15, 2013. Cost basis includes commissions. Results include dividends, but not interest received on cash balance.

* VBI score at the time we added the firm to the portfolio.

** See our methodology regarding the Valuentum Buying Index (VBI).

*Are You Ready for Some Football?...*from page 7

Further, any attempt to move consumers into the Android ecosystem may limit eyeballs, and valuable eyeballs at that. Apple's iOS (AAPL) users spend far more on apps ($0.19 avg.) than Android users ($0.06 avg.). We already know that Apple commands a large percentage of the US smartphone market, and more importantly, evidence suggests iOS users are a relatively more attractive audience to sell to.

Does the NFL really want to encroach on its largest revenue sources AND lucrative iOS users? We doubt it.

DirecTV and Apple Could Partner

Although the NFL has a deal in place with Verizon (VZ) for streaming content exclusively over its smartphones, the deal does not cover tablets. In our view, it could make sense for DirecTV and Apple to partner to help fend off Google. DirecTV could offer its Sunday Ticket mobile application exclusively to iOS users, and we doubt there would be much backlash because the iPad already dominates so much of the tablet market. It could marginally boost iPad sales, but more importantly, it would prevent Google from cornering any exclusive content.

As for DirecTV, we think a deal with Apple would help the firm move closer to turning a profit on the expensive package. In our view, DirecTV wouldn't receive much (if any) backlash for partnering with Apple, and it could pave the way for further collaboration down the road.

Valuentum's Take

After considering the NFL's viewpoint, we see little reason why there would be a change in the status quo. The league generates more revenue than any other sports league, and it wants to grow its revenue as much as possible. We simply do not believe a long-term partnership with Google helps the NFL achieve that goal.

Ultimately, we suspect the status quo will remain with DirecTV as the exclusive Sunday Ticket rights holder. The NFL might not even be serious about selling the package to Google and could simply be using the threat as a way to receive a higher bid from DirecTV.

Coincidentally, we hold shares of Google, DirecTV, and Apple in our Best Ideas Newsletter portfolio, so we're largely hedged from any unforeseen negatives that may come about from the situation with respect to any one particular player (as another will likely benefit).

Disclosure:

RJ Towner owns shares of the following companies mentioned in this article: AAPL

Lululemon's Growth Slows in the Second Quarter

By RJ Towner

Athletic apparel maker Lululemon (LULU) posted strong second quarter results, though the pace of both revenue and earnings growth has slowed. Revenue jumped 22% year-over-year to $345 million, slightly above consensus estimates. Earnings-per-share wasn't quite as strong, flat year-over-year at $0.39, but it still came in line with consensus expectations. Year-to-date, free cash flow stands at $26.9 million, equal to 4% of total revenue.

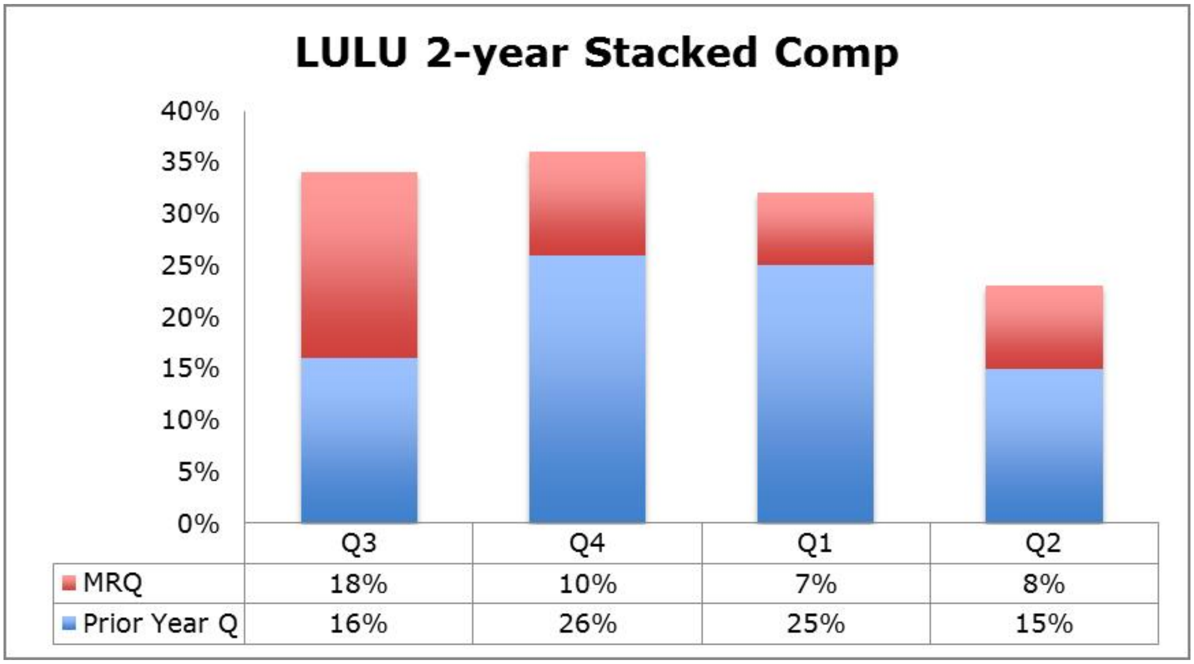


Image Source: Company Filings, Valuentum

The market is displeased with Lululemon's slowing comp sales growth of 8%, which is the firm's second consecutive quarter below a double-digit growth rate. Still, the 2-year stacked comp remains strong at 23%. Nearly any other company would be pleased with such a strong two-year trend, but Lululemon investors have become accustomed to 2-year stacked comps in excess of 30% (as shown above). Though growth slowed in the second quarter, we're pleased with how well stores held up during the period, especially as other retailers experienced a significantly lower rate of expansion.

Lululemon is also facing margin contraction. The weakness isn't much of a surprise given the robust 55%+ gross margins the firm has posted during the past few years, and it makes sense that, for sales to continue to grow at a high double-digit pace, the firm will have to sacrifice a little margin. Overall, the company's gross margin declined 110 basis points year-over-year to 54%. Still, the margin is well above that of competitors such as Nike (NKE) and Under Armour (UA).

Lululemon's SG&A as a percentage of revenue jumped 80 basis points year-over-year, to 31.1%. Without the same robust comparable sales growth, the firm isn't leveraging fixed costs to the same degree it was in previous quarters. This dragged the firm's overall operating margin down 190 basis points year-over-year, to 22.9% of sales—still an incredible figure for a retailer but down materially from prior periods.

*Lululemon's Growth Slows...*continued on next page

*Lululemon's Growth Slows …*from previous page

	August 4, 2013		February 3, 2013
Finished goods	$	186,717	$	163,008
Raw materials		571		583
Provision to reduce inventory to market value		(24,284)		(8,369)
	$	163,004	$	155,222

Image Source: LULU 10-Q

The other issue at Lululemon is that the 'Provision to reduce inventory to market value' has jumped since the beginning of the year, now sitting at $24.2 million as a result of the black luon pants issue. The current figure is only down slightly from the $25 million at the end of the first quarter, suggesting either these pants are mostly worthless or the firm is having additional inventory issues. We're keeping a close eye on the situation.

Looking ahead to the third quarter, Lululemon issued below-consensus guidance of $370-$375 million in sales driving earnings per share of $0.39-$0.41. Surprisingly, management reduced the full-year earnings outlook to $1.94 to $1.97 per share, below prior expectations of $1.96-$2.01 and even below the firm's initial fiscal year 2013 outlook of $1.95-$1.99. The full-year revenue outlook was also reduced slightly to $1.625-$1.635 billion from $1.67 billion. The reduced annual targets may reflect the need for the company to accept lower prices on some of the inventory it isn't moving (as well as the inevitable reality of slowing sales growth).

Valuentum's Take

As we noticed last quarter, CEO Christine Day's departure has coincided with growth slowing at Lululemon. That doesn't mean the company is ruined or that growth won't continue, but it certainly does suggest that expansion won't be as rosy as it was in the past. The firm is dealing with inventory and product expansion issues, and is starting to face increasing competition.

We think the brand itself is extremely valuable and continues to resonate with consumers. However, the current valuation simply doesn't provide a large enough margin of safety for us to be interested in establishing a position in the portfolio of our Best Ideas Newsletter.

Air Quality Standards Take Aim at Coal

By RJ Towner and Brian Nelson, CFA

After competing with an abundance of lower-priced, cleaner natural gas, coal miners may now have to deal with more demand headwinds as governments aim to reduce coal burning.

The US

Expectations are already for as much as 27 gigawatts' worth of coal generation (about 8.5% of the US coal fleet) to retire by 2016. This percentage could rise to nearly 17% (one-sixth) by 2020, according to the Energy Information Administration. In addition to the expected retirements, the Environmental Protection Agency (EPA) plans to block all new coal-fired plants unless the construction of these plants coincides with expensive technology that captures greenhouse gas emissions.

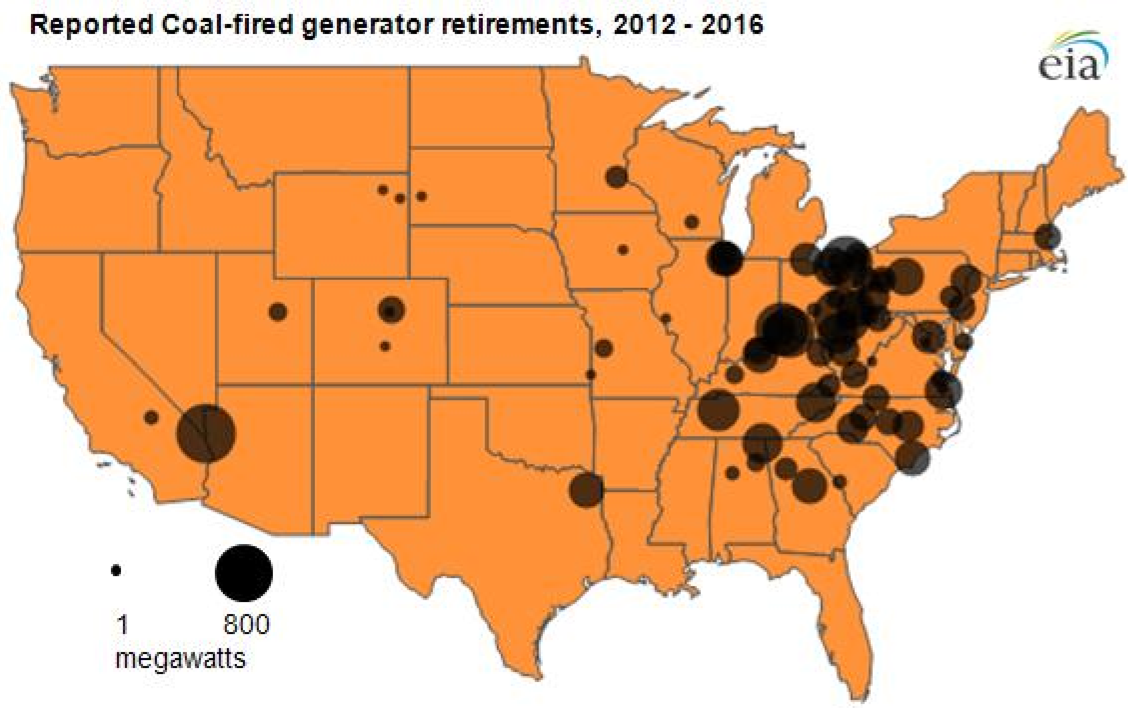


Image Source: Energy Information Administration

Though the EPA forecasts that no traditional coal-fired power plants (1) will be built in the next eight years, the rules, if enacted, would make coal consumption even less attractive for US power plants. Estimates suggest, for example, that building a new coal plant with carbon capture could cost nearly twice as much as that of a natural gas plant. In turn, US coal producers continue to export more coal, increasing global supply (putting pressure on global prices).

*Air Quality Standards Take Aim at Coal...*continued on next page

*Air Quality Standards Take Aim at Coal…*from the previous page

The combination of trouble on both the domestic and international horizons is certainly not welcomed by precarious coal producers such as James River Coal (JRCC), Arch Coal (ACI), and Walter Energy (WLT), which remain heavily levered.

Railroads CSX (CSX) and Norfolk Southern (NSC) are already feeling the pain from lower coal volumes. Volume declined 4% year-over-year during Norfolk's second quarter, with total coal revenue falling 17% year-over-year to $626 million. Coal volumes declined 6% year-over-year during CSX's second quarter, dragging total coal revenue down 6% year-over-year to $770 million. Coal still comprises 25% of revenues and 22% of revenues at CSX and Norfolk, respectively, so any decline can materially harm performance.

However, it isn't a zero sum game by any means. Pipelines that move natural gas owned by the likes of Berkshire Hathaway's MidAmerican Energy (BRK.A) and Kinder Morgan (KMP) should benefit from increased shipments. Additionally, railroads will now have excess capacity available to ship different products (think crude by rail). In 2012, railroads moved more crude oil than ever before.

China

While the EPA plan remains in the works, Beijing unveiled a clean air action plan Thursday morning aimed at curbing pollution. The magnitude of the plan is large:

> *"The capital's 2013-2017 plan aims to cut annual coal consumption by 13 million tonnes and keep it within 10 million tonnes by 2017, compared with 23 million tonnes in 2012."*

In other words, Beijing expects to cut coal consumption by 57% over just the next five years. China currently accounts for nearly 50% of global coal consumption, though 23 million tonnes is a small portion of the total 3.8 billion tonnes consumed in China during 2011. Even a consumption cut of 13 million tonnes does little to reduce overall coal consumption. However, the fear is that other municipalities will follow Beijing's lead and create similar plans. Global coal giants such as Rio Tinto (RIO) and BHP (BHP) will feel the pain if China as a country decides to shun coal to a greater extent.

Still, the plan in itself isn't enough to ruin overall global coal demand. In fact, we think coal will remain a key energy source, but natural gas will overtake it as the second-most used fuel by 2025, in our opinion.

Valuentum's Take

Coal producers continue to deal with a bevy of headwinds, and further government regulation creates an environment for more negative hurdles going forward. We currently have no positions in any company that exclusively produces coal, though Best Ideas Newsletter portfolio holdings Rio Tinto and Union Pacific (UNP) do have modest exposure via coal production and transportation, respectively.

For more information, please select the following link for Valuentum's joint outlook on the coal and railroad industries: http://www.valuentum.com/articles/20130701_2

(1) "the EIA's AEO 2012 Early Release (AEO 2012 ER) does not forecast new unplanned coal capacity without CCS through 2020." (page 5-5)

LinkedIn Acknowledges Its Stock Is Overpriced

By RJ Towner

Business social networking site LinkedIn (LNKD) announced that it would execute a secondary public offering that closed September 10. LinkedIn offered 5,381,166 shares of its Class A common stock at a price of $223 per share for proceeds of $1.2 billion. When a well-capitalized company like LinkedIn offers stock, it can often signal that the company believes its shares are overvalued.

As of its most recent quarter, LinkedIn had over $800 million in cash and short-term investments against no long-term debt. The company was also free cash flow positive (albeit free cash flow wasn't robust) in fiscal year 2012. LinkedIn isn't in dire need of cash, so we think the company either has a large acquisition in mind or it could simply be looking to capitalize on its expensive stock, creating value for shareholders. Anytime a firm raises cash at a level above our estimate of intrinsic value, management is creating value for existing shareholders, in our view.

Potential Targets

The rumored potential target for LinkedIn is German business networking site Xing. Rumors began circulating several weeks ago, with the big hurdle to an acquisition being Hubert Burda Media Holding GmbH which currently owns 52.6% of the company and would demand a large premium.

Interestingly, we aren't huge fans of this potential acquisition. For one, LinkedIn already has a tremendous global presence, and in a global economy that deemphasizes the importance of location and region, we think a social network with a global network is infinitely more valuable.

Additionally, revenue growth is significantly slower at Xing than it is at LinkedIn. Second-quarter revenues at the firm were up 15% year-over-year to 20.9 million euros—not a terrible growth rate by any means, but well below what we've come to expect from LinkedIn (59% revenue growth in the most recent quarter). Earnings were 30% higher than a year ago, but at 2.7 million euros, the figure would hardly impact LinkedIn's bottom line.

Plus, LinkedIn already fills the business networking position of someone's online life. Facebook (FB), Twitter, Instagram, LinkedIn, and even SnapChat all fill different roles in one's "social" life—Xing would overlap directly with LinkedIn, so we believe its future growth potential isn't strong.

What about Monster (MWW) as a potential acquisition candidate? The stock trades at an incredibly low EV/EBITDA multiple, but the company is on the road to irrelevancy. LinkedIn is clearly stealing market share as Monster's revenues flounder, and we simply do not see a compelling reason for LinkedIn to take out its competitor when nature appears ready to take its course.

In our view, neither acquisition makes much sense. A merger with either Paychex (PAYX) or ADP (ADP) would be a significantly better strategic fit (given the human resources overlap), but we doubt either occurs as ADP possess a larger market capitalization than LinkedIn, and Paychex would cost the company at least $16 billion (20% premium to current enterprise value).

Valuentum's Take

LinkedIn stated that it would use the offering to "bolster" the firm's already strong balance sheet. Without many logical acquisition targets, the offering could mean higher capital investment spending going forward, or as we speculated earlier, the company is simply raising money while its stock is incredibly expensive. We have no interest in establishing a long position in LinkedIn in the portfolio of our Best Ideas Newsletter.

The Price-to-Earnings Ratio Is a Formula (P/E) and So Is Einstein's Mass-Energy Equivalence (E=MC squared); We Hope Investors Understand That There Is a Lot of Thought Behind Both

By Brian Nelson, CFA

I Couldn't Sleep Last Night

I was reading an article about the price-to-earnings (PE) ratio yesterday from one of our competitors that…I think…was attempting to sell its data screener to unsuspecting readers. The article made it sound like the PE ratio was the holy grail of investing, and if investors just used it, they'd be well on their way to knowing everything there is to know about valuation.

First, I was saddened. This competitor has far greater reach than Valuentum, and having trained hundreds of equity and credit analysts across three continents, I know that instructing analysts with 20+ years of experience on how to 'unlearn' the wrong ways of doing things is a lot harder than molding a freshly-minted graduate into a top analyst on the Street. When our competitors engage in these types of shenanigans, they are making Valuentum's work harder – much harder.

Second, I was overwhelmed. I suddenly remembered that, in the many years I have been in this business, I have come across dozens of articles just like the one our competitor had recently printed. It got me thinking that it's nearly impossible nowadays for a pure, open-minded learner to actually find good information to absorb – and what I mean by good is accurate, complete information (I don't think our competitor was purposely trying to mislead but probably just trying to sell its product). I believe the financial industry has now become more about what a select few with large distribution mechanisms/networks think than what actually is the truth. For those that know me personally, you can probably imagine that I was starting to breathe heavily at this point.

And then I became terrified. What if investors, after reading the article from our competitor, become armed with a sense of invincibility and scoop up every low-PE stock out there, thinking that they had found the secret to perpetual outperformance? After all, the market has gone straight up this year, so unsuspecting readers might be drawn in and associate one with the other. Frankly, I am terrified at how some investors seek only immediate gratification—meaning that if an idea doesn't work out in the next two weeks, something is wrong. After all, look at some of the advertising out there: real-time and millisecond quotes. It's as if real-time or up-to-the-second is better than correct. I'll take being correct over "fast-and-furious" any day of the week.

I was up all night mulling over these thoughts. But I'm hoping that conveying Valuentum's views on the construction of the PE ratio might help me sleep better tonight. At the very least, we'll put correct, complete information out there. So here goes…

The Price-to-Earnings Ratio is a Formula (P/E) and So Is Einstein's Mass-Energy Equivalence (E=MC squared): We Hope Investors Understand That There Is a Lot of Thought Behind Both

The price-to-earnings (PE) ratio seems so easy, right? The trailing PE is just the price per share of the stock divided by the annual net diluted earnings per share the firm generated in its last fiscal year. The forward PE is the price per share of the stock divided by next fiscal year's annual net diluted earnings per share of the firm (or the forward 12-month period).

*The PE Ratio…*continued on next page

*The PE Ratio...*from previous page.

The PE is probably the most common measure to help investors compare how cheap or expensive a firm's shares are, as stock prices, for lack of a better term, are arbitrary. For example, firms like Warren Buffett's Berkshire Hathaway (BRK.A), which has never split its stock, have traded as high as $175,000 per share, while other well-known companies like Sprint (S) can trade for just a few bucks per share. And Citigroup (C) was once a penny stock before its 10-to-1 reverse split in 2011.

It's only when investors compare a firm's share price to its annual net diluted earnings per share that they can get a sense for whether a company's shares are expensive (overvalued) or cheap (undervalued). The higher the PE, the more expensive the company's stock – all else equal. This seems way too simple, so why would we (or better yet, how could we) devote so much time to talking about such a basic financial concept? Well, the truth is that the PE ratio is not as simple as you think (and even some of the most seasoned investors continue to use this powerful multiple incorrectly).

How the PE Ratio Is Used Incorrectly

As Valuentum members know, the second pillar of our Valuentum Buying Index™ considers a company's forward PE ratio by comparing this measure to that of its industry peers to determine if the company is trading at a comparatively attractive valuation. If the firm's PE is lower than its peer median, an investor is paying less per unit of earnings than the median of its peer group. Investors are getting a good deal in this case, all else equal, right? Well, the problem is that companies are never equal, and even comparisons among firms that are in the same industry can be misleading.

It is also inappropriate for investors to apply a firm's historical median (or average) price-to-earnings ratio to the same firm's future earnings stream. But why? It's the same stock. Shouldn't it be relevant and applicable? Well, yes and no. First, it's great for investors to have an idea of what "multiple range" a company has traded at in the past – there's lots of value to this, and most relevant for cyclical firms (mainly industrials) that may, from a fundamental standpoint, exhibit similar (but not identical) patterns with respect to both earnings and their PE through the course of each economy cycle: think Boeing (BA) and the commercial aerospace cycle; Ford (F) and consumer demand for auto sales; or United Continental (UAL) with respect to premium air travel demand. But for less-cyclical firms (and even for cyclicals where structural industry dynamics have altered over time), investors are wrongly assuming that the forward outlook of the past (which determined the historical multiple) will be the same as the forward outlook of the present (which determines the current multiple). This, unfortunately, is never true.

So what is an investor to do? We know that it's imperfect to compare a firm's current or forward PE ratio to its peers or even to the median or average of its peers. No two firms are identical. And it's even more imperfect to compare a firm's current or forward price-to-earnings ratio to its historical measure. Look at Apple's outlook in 2002 versus its outlook in 2009 – a lot different, would you say? One wouldn't apply the same multiple to Apple in both years, or if you did, it would be for different reasons/underlying factors.

Why Do We Use the PE Ratio

Okay, you may then ask: why does Valuentum use a PE ratio at all in its process if the measure is so imperfect? Good question. The answer rests in its simplicity – and also stems from the reasons behind our writing this article in the first place. All investors do not use a discounted cash-flow process to value equities, and as a result, resort to the PE ratio to make decisions. As a result, there exists what we'd describe to be self-fulfilling market forces (buying and selling) that make the price-to-earnings ratio a meaningful consideration.

In other words, if Portfolio Manager A likes a stock because its PE ratio is trading at the lower end of its historical PE valuation range or is trading at a discount to its peers' average PE, he/she might buy it, and this buying pressure itself causes the stock to rise, therefore making the PE in this form relevant. In other words, if other investors (especially the ones with deep pockets) are paying attention to it, you should, too.

*The PE Ratio...*continued on next page

*The PE Ratio…*continued from the previous page.

In fact, this idea hits at the heart of our process at Valuentum – striving to have a complete understanding of all market forces (investment philosophies) that drive stock prices, such that we can capitalize on them. For this reason, and this reason alone, we include a relative value assessment in our process, and the forward PE and PEG (price-earnings-to-growth) ratios, more specifically.

How Do We View the PE Ratio

So, with that said, how do we look at the PE then? Valuentum followers know that we use a discounted cash-flow valuation process (the first pillar of our Valuentum Buying Index) to uncover the intrinsic worth of every company in our coverage universe. Okay, now you may ask: "Why do you use a free cash flow model when stock prices are driven by earnings? Didn't we just define the stock price as a function of its earnings and a P/E multiple (the share price divided by net diluted earnings per share is the PE)?" Well, yes. But earnings are a component of cash flow, and evaluating future free cash flows has its benefits.

For starters, the variations between earnings and cash flow not only arise in working capital changes over time (their influence on a firm's cash flow from operations), but also in the timing of the cost of replacing those assets that generate earnings (capital expenditures versus depreciation). Plus, varying levels of interest rates paid on debt loads can also muddy the waters on earnings – not to mention that there are various ways to account for rent expense (whether to capitalize such assets or to allow the expense to flow through the operating line). So there are some major differences between assessing a company's value based on earnings versus based on using a discounted cash-flow model. And because earnings quality (are earnings being converted to cash flow?) and capital efficiency (how much capital needs to be plowed back into the firm to maintain earnings) are critical to assessing the health of a company and its valuation, using free cash flow to evaluate companies is a superior process.

My Aha Moment…sometime in 2006

But what many investors fail to understand is that the P/E multiple is precisely – you guessed it – a short-form discounted cash-flow model. I first uncovered this groundbreaking relationship with a number of my colleagues back in 2006 when I guess you can say my 'aha' moment happened.

You're probably like "great, but what does this mean?" Well, a PE ratio is not to be calculated from the stock price to determine if the stock is cheap or expensive, but instead, it should be derived from the company's fundamentals to determine where the firm should be trading at.

It basically represents the difference between saying a firm is trading at 20 times earnings and saying a firm SHOULD be trading at 20 times earnings. A stock trading at 20 times may be cheap or expensive in the first case, but we know that a stock trading at 20 times is fairly valued in the second.

In order to discover what PE multiple is appropriate to place on a firm's earnings stream (its net diluted earnings per share) to arrive at a fair value or price target, investors use a discounted cash flow process.

By calculating the present value of a company's future enterprise free cash flows, factoring in the firm's net balance sheet impact and making other adjustments (and then dividing by diluted shares outstanding), the investor arrives at equity value per share. Taking this equity value per share and dividing it by next fiscal year's earnings of the firm leaves you with – drum roll please – the forward price-to-earnings (P/E) ratio.

Because a discounted cash-flow process captures the unique intricacies of the exact firm one is modeling at the exact time one is modeling it (and taking into consideration all future factors at the time), it is far superior to any relative peer or historical PE multiple analysis.

2006 was a great year.

*The PE Ratio…*continued on the next page

*The PE Ratio…*from previous page.

Why We're Fans of the Discounted Free Cash Flow Model

By now, you can probably see why we're such big fans of using a discounted free cash flow valuation model. Though there are many, many ways of looking at a stock—in fact, varying perspectives remain core to our process—using a free cash flow process is perhaps the only way investors can truly arrive at the "correct" intrinsic PE multiple to place on a company's earnings.

Let's examine this even further. For example, have you ever wondered why capital-light companies (software, advertising companies) garner higher earnings multiples than capital-intensive companies (auto manufacturers)? Well, capital-intensive companies have to re-invest a significant amount of earnings back into their businesses, thereby reducing future free cash flow, and by extension, the PE multiple investors are willing to pay for that earnings stream. Simply put, not all earnings streams are created equal – even given equivalent future expected growth trajectories in them. Investors should prefer the earnings stream in this case that requires the least amount of re-invested maintenance capital.

Nuts & Bolts

Okay…on to demystifying the PE ratio. At this point, we hope that we have at least convinced you to be careful about arbitrarily placing a PE multiple on a firm's next year's earnings to arrive at a target price (fair value). Even if that multiple is based on historical ranges (medians or averages) or is comparable to industry peers, investors fall short of capturing the uniqueness of a company's future cash flow stream via a discounted cash flow process, which considers all of the qualitative factors of a company –from a competitive assessment to the company's efficiency initiatives and beyond (yes, even management's strategy). Using a discounted free cash flow model forces investors to think about the key valuation drivers of a company long into the future, thereby reinforcing forward-looking analysis and a critical understanding of what we'd describe as needle-moving inputs (revenue, WACC, etc.).

Even analysts with 20+ years' experience need help in this area. Trust me.

Without further delay, below is our complete definition of the price-to-earnings ratio. It's not all that sexy, but neither are all the nuts and bolts behind Einstein's mass-energy equivalence. You'll notice that the PE ratio is forward-looking and considers many more components than many investors think:

Forward Price to Earnings Ratio = {[(Sum of Discounted Future Enterprise Free Cash Flows – Total Debt – Preferred Stock + Total Cash)/Shares Outstanding]/ Next Fiscal Year's Earnings Per Share}

So Then, What Are the Drivers of a Firm's Stock Price?

Upon further examination of the definition of the PE ratio above, one can see that it is just a short-form discounted cash-flow model. And because the PE ratio is also a function of the price of a stock, the factors of a discounted cash-flow model then become the drivers behind the firm's stock price. Below, we show how a number of qualitative factors influence the PE multiple and (by extension) stock prices and whether each factor is positively or negatively correlated to them. You'll notice the list is much more comprehensive than what many investors point to as the main reason for different PE ratios: varying future growth rates.

*The PE Ratio…*continued on next page

*The PE Ratio …*from previous page.

Revenue Growth: Impacts Future Enterprise Cash Flows (Mostly Positive)

Operating Earnings Growth: Impacts Future Enterprise Cash Flows (Positive)

Taxes: Impacts After-tax Earnings; Cost of Debt (Mostly Negative)

Capital Expenditures: Impacts Future Enterprise Cash Flows (Negative)

Return on Invested Capital (ROIC): Function of Operating Earnings and Net New Investment, Capital Expenditures (Positive)

Risk-free Rate, 10-year Treasury: Impacts WACC (Negative)

Discount Rate (WACC): Impacts Present Value of Enterprise Cash Flows (Negative)

Total Debt: Impacts Enterprise Value and Discount Rate (Mostly Negative)

Preferred Stock: Impacts Enterprise Value and Discount Rate (Mostly Negative)

Total Cash: Impacts Enterprise Value (Positive)

Shares Outstanding: Changes in Shares Outstanding (Neutral, assuming reinvestments' ROIC equal the firm's WACC)

Key Takeaways

The key takeaways are: 1) without using a discounted cash-flow model, the PE ratio that should be applied to a company's earnings stream can never be appropriately solved, and by extension, 2) when investors assign an arbitrary price-to-earnings multiple to a company's earnings (based on historical trends or industry peers), they are essentially making estimates for all of the drivers behind a discounted cash-flow model in one fell swoop (and sometimes hastily). This ends badly almost all of the time.

As earnings for next year are often within sight and can be estimated with some confidence (though this certainly varies among firms), calculating the price-to-earnings ratio, in our opinion, is of far greater importance than worrying about whether a firm will beat or miss earnings in its next fiscal year. Because the PE ratio is a discounted cash-flow model that considers the long-term qualitative dynamics of a particular entity, cash-flow analysis remains the first and most important pillar of our Valuentum Buying Index.

As with Einstein's mass-energy equivalence, the PE ratio is a formula, and both have deep, underlying theoretical support. Just like you can't stop at 'e=mc squared' to fully understand all of physics, you can't stop at the PE ratio (or any ratio for the matter) to fully understand all of valuation.

Aha…

Now I can sleep!

Is Innovation Back at McDonald's?

By Valuentum Analysts

August Sales

August sales at McDonald's were volatile across geographies. US same-store sales grew just 0.2% year-over-year during August, which CEO Don Thompson blamed on a "challenging environment." Interestingly, Thompson addressed the challenging environment, which we agree with, rather than blaming a bad economy, which has so often been the case. In fact, we think an improving economy may leave McDonald's at a disadvantage as consumers trade-up and no longer demand as much value.

The opposite phenomenon was borne out in Europe, where comp sales grew 3.3% year-over-year on top of a 3.1% comp growth rate during August of 2012. This runs counter to the rest of 2013 that has been fairly weak in Europe. In fact, same-store sales are down 0.2% year-to-date. Regardless, management noted strength across the UK and France that was offset by weakness in Germany. Europe now looks a bit like the US a few years ago, in our view, so we are confident that sales will remain strong for the rest of 2013.

As for Asia-Pacific, sales declined 0.5% year-over-year compared to a 5.7% gain in August of the prior year. Management noted that performance was down across major markets like China, Japan, and Australia. Given Yum! Brands' (YUM) poor performance in China during August, we tend to think China may be dragging down results at McDonald's as well. We'll keep a close eye on the region, but we tend to believe the problem is a secular issue in China at this point.

Finally some innovation?

Overshadowing the August sales results are reports regarding new product innovation from McDonald's. Not only is the company rolling out its wings nationwide, but the firm will also release a Steak, Egg, & Cheese Biscuit sandwich on its breakfast menu. Though the sandwich registers just 10 calories less than a Big Mac, it is a new item that differs from existing products. This will help drive new traffic into restaurants, as product selection has remained fairly stagnant.

In addition to a new breakfast sandwich, McDonald's is testing a family-sized box meal package. Available as an exclusive promotion with the Kansas City Chiefs at this time, the "Blitz Box" sells for $14.99 and includes 2 Quarter Pounders with cheese, 2 medium fries, and 20-piece order of Chicken McNuggets. This idea isn't revolutionary: just a few years ago, Taco Bell ran a promotion for its $5 box package that was a fantastic value for consumers. However, McDonald's entry into the family style may allow the firm to better position itself to gain sales on large, family style events.

With new products hitting menus, McDonald's is also testing new value menus without the strict $1 price tag. This is one of McDonald's largest issues: consumers are addicted to the Dollar Menu, but franchisees hate the products that weigh on margins and constrain revenue growth. If McDonald's can find a happy medium, we think the company will be better off in the long-term with happy franchisees and customers.

Valuentum's Take

McDonald's August same-store sales results weren't great, but we are very excited to see the company engage in some new product innovation and work to solve its Dollar Menu issues. Although we would love to see McDonald's new products become blockbuster successes, we're simply pleased to see the company return to innovating rather than one-time boosts (a la expanding breakfast hours).

Our primary concern has been that the innovation well had run dry, but recent news suggests we may have simply seen an innovation lull over the past year. Nevertheless, we believe shares of McDonald's look fairly valued.

Ideas for Your Radar

By Valuentum Analysts

Our Valuentum Buying Index (VBI), which places a considerable emphasis on a firm's valuation, is the primary driver behind names included in our Best Ideas portfolio (see page 8). However, the size of our coverage universe lends itself to a plethora of new ideas beyond the ones we seek to capitalize on. Below, we provide a unique screen that sorts companies we feel are undervalued on both a DCF and relative value basis (the first two pillars of our VBI; the third is a technical assessment).

We update this screen monthly and deliver it to you in our newsletter (for your added convenience, we also post it on our site). You'll see we often hold a number of these firms in our portfolio (e.g. BIDU, DTV), and we continue to monitor the remainder for the most opportune time to add them. The names on this list are the cream of the crop for the value investor and can supplement your "shopping list" of new ideas.

Name	Symbol	DCF Valuation	Relative Valuation	Price/Fair Value
Baidu	BIDU	UNDERVALUED	ATTRACTIVE	0.62
Huntsman	HUN	UNDERVALUED	ATTRACTIVE	0.63
Jabil Circuit	JBL	UNDERVALUED	ATTRACTIVE	0.66
NASDAQ	NDAQ	UNDERVALUED	ATTRACTIVE	0.67
Nabors Industries	NBR	UNDERVALUED	ATTRACTIVE	0.67
Teva Pharma	TEVA	UNDERVALUED	ATTRACTIVE	0.70
Reinsurance Group	RGA	UNDERVALUED	ATTRACTIVE	0.72
Microsoft	MSFT	UNDERVALUED	ATTRACTIVE	0.73
Koppers	KOP	UNDERVALUED	ATTRACTIVE	0.73
Helen of Troy	HELE	UNDERVALUED	ATTRACTIVE	0.75
Tyson Foods	TSN	UNDERVALUED	ATTRACTIVE	0.76
DIRECTV	DTV	UNDERVALUED	ATTRACTIVE	0.77
Johnson Outdoors Inc	JOUT	UNDERVALUED	ATTRACTIVE	0.77
Assurant Inc	AIZ	UNDERVALUED	ATTRACTIVE	0.79
Protective Life	PL	UNDERVALUED	ATTRACTIVE	0.79

Ideas... continued on next page

*Ideas…*from previous page

The initial table below showcases firms that fit the bill of the Valuentum investor, with each posting a 9 or a 10 on our index. These are names that we may swap into our portfolio on the long side (if not already held) should their upside potential become greater than our current holdings.

We also show firms that register a 1 or 2 on our VBI. These names represent put-option candidates. We provide the respective lists below, and each firm's report can be found on our website.

Name	Symbol	Sector	Industry	VBI
Baidu	BIDU	Information Technology	Internet Software & Svcs	10
Helen of Troy	HELE	Consumer Staples	Household Products	9
Jabil Circuit	JBL	Information Technology	Electronic Suppliers	9
Johnson Outdoors Inc	JOUT	Consumer Discretionary	Sporting Goods	9
NASDAQ	NDAQ	Financials	Exchanges	9
Protective Life	PL	Financials	Insurance - Life	9
Reinsurance Group	RGA	Financials	Insurance - Life	9
Tyson Foods	TSN	Consumer Staples	Food Products	9

Name	Symbol	Sector	Industry	VBI
Badger Meter	BMI	Industrials	Electrical Equipment	1
Bank of NY Mellon	BK	Financials	Banks & Money Centers	1
China Life	LFC	Financials	Insurance - Life	1
Heartland	HTLD	Industrials	Air Freight & Logistics	1
HSBC	HBC	Financials	Banks & Money Centers	1
Hyatt	H	Consumer Discretionary	Hotels	1
KB Home	KBH	Consumer Discretionary	Homebuilders	1
McGrath	MGRC	Industrials	Rental and Leasing	1
Northern Trust	NTRS	Financials	Banks & Money Centers	1
Simpson	SSD	Industrials	Machinery & Tools	1
American Express	AXP	Financials	Banks & Money Centers	2
Famous Dave's	DAVE	Consumer Discretionary	Restaurants	2
First American	FAF	Financials	Insurance - Property & Casualty	2
GameStop	GME	Consumer Discretionary	Specialty Retailers	2
Mercury General	MCY	Financials	Insurance - Property & Casualty	2
Rayonier	RYN	Industrials	Conglomerates	2
Selective Insurance	SIGI	Financials	Insurance - Property & Casualty	2
Washington Post	WPO	Consumer Discretionary	Media - newspapers	2

Valuentum Retail Equity Research | Visit us at www.valuentum.com | Ratings as of 3-Jul-2013 | Data as of 28-Jun-2013

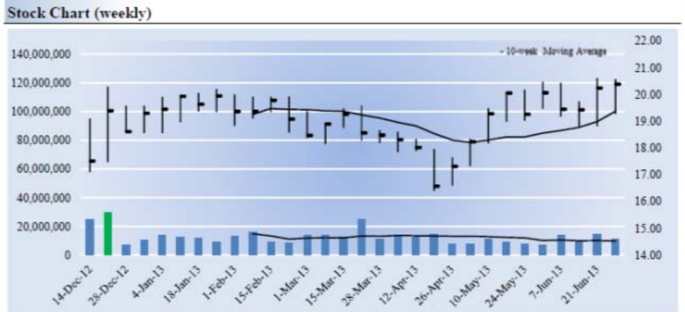
Jabil Circuit JBL UNDERVALUED 7.9%

Buying Index™ 9 **Value Rating** ✓

Last Close	Estimated Fair Value	Fair Value Range	Investment Style	Sector	Industry
$20.38	$31.00	$22.00 - $40.00	MID-CAP VALUE	Information Technology	Electronic Suppliers

Jabil is focused on expanding its position as a global provider of electronic manufacturing services/solutions.

Stock Chart (weekly)



The week with the highest trading volume out of the last 13 weeks was a week of heavy buying, or accumulation (green bar).

Investment Considerations

DCF Valuation	UNDERVALUED
Relative Valuation	ATTRACTIVE
ValueCreation™	EXCELLENT
ValueRisk™	MEDIUM
ValueTrend™	NEGATIVE
Cash Flow Generation	MEDIUM
Financial Leverage	MEDIUM
Growth	MODEST
Technical Evaluation	BULLISH
Relative Strength	STRONG
Money Flow Index (MFI)	NEUTRAL
Upside/Downside Volume (U/D)	BEARISH
Near-term Technical Support, 10-week MA	19.00

DCF = Discounted Cash Flow; MFI, U/D = Please see glossary. MA = Moving Average

Business Quality

ValueRisk™ \ ValueCreation™	Very Poor	Poor	Good	Excellent
Low				
Medium				■
High				
Very High				

Firms that generate economic profits with little operating variability score near the top right of the matrix.

Company Vitals

Market Cap (USD)	$4,304
Avg Weekly Vol (30 wks)	12,715
30-week Range (USD)	16.39 - 20.61
Valuentum Sector	Information Technology
5-week Return	3.5%
13-week Return	10.2%
30-week Return	11.4%
Dividend Yield %	1.6%
Dividends per Share	0.32
Forward Dividend Payout Ratio	14.1%
Est. Normal Diluted EPS	3.20
P/E on Est. Normal Diluted EPS	6.4
Est. Normal EBITDA	1,297
Forward EV/EBITDA	4.4
EV/Est. Normal EBITDA	3.7
Forward Revenue Growth (5-yr)	6.0%
Forward EPS Growth (5-yr)	17.2%

NMF = Not Meaningful; Est. = Estimated; FY = Fiscal Year

Returns Summary — 3-year Historical Average

Return on Equity	17.8%
Return on Assets	4.7%
ROIC, with goodwill	23.8%
ROIC, without goodwill	24.1%

ROIC = Return on Invested Capital; NMF = Not Meaningful

Leverage, Coverage, and Liquidity

In Millions of USD

Total Debt	1,676
Net Debt	459
Total Debt/EBITDA	1.7
Net Debt/EBITDA	0.5
EBITDA/Interest	8.6
Current Ratio	1.5
Quick Ratio	0.6

NMF = Not Meaningful

Investment Highlights

- Jabil Circuit earns a ValueCreation™ rating of EXCELLENT, the highest possible mark on our scale. The firm has been generating economic value for shareholders for the past few years, a track record we view very positively. Return on invested capital (excluding goodwill) has averaged 24.1% during the past three years.
- Jabil Circuit's valuation is compelling at this time. The firm is trading at a nice discount to our estimate of its fair value, even after considering an appropriate margin of safety. The firm's forward earnings multiple and PEG ratio also look attractive versus peers.
- Jabil Circuit's cash flow generation and financial leverage are at decent levels, in our opinion. The firm's free cash flow margin and debt-to-EBITDA metrics are about what we'd expect from an average firm in our coverage universe.
- Jabil is focused on expanding its position as a global provider of electronic manufacturing services/solutions. The industry is highly competitive, and heavy exposure to struggling customer Research In Motion adds uncertainty.
- Though Jabil Circuit boasts a very strong Valuentum Dividend Cushion score, the firm's yield isn't as high as some of our other dividend growth ideas.

Relative Valuation

	Forward P/E	PEG	Price / FV
Amphenol Corp	22.4	2.3	129.9%
Corning	11.0	NMF	109.5%
LG Display	40.5	NMF	79.1%
Molex	19.9	2.5	108.7%
Peer Median	21.2	2.4	109.1%
Jabil Circuit	**9.0**	**0.6**	**65.7%**

Price / FV = Current Stock Price divided by Estimated Fair Value

Financial Summary

Fiscal Year End:	Aug-11 (Actual)	Aug-12 (Actual)	Aug-13 (Projected)
Revenue	16,519	17,152	18,181
Revenue, YoY%	23.2%	3.8%	6.0%
Operating Income	603	622	705
Operating Margin %	3.7%	3.6%	3.9%
Net Income	381	395	459
Net Income Margin %	2.3%	2.3%	2.5%
Diluted EPS	1.73	1.87	2.27
Diluted EPS, YoY %	122.5%	8.3%	21.6%
Free Cash Flow (CFO-capex)	369	137	309
Free Cash Flow Margin %	2.2%	0.8%	1.7%

In Millions of USD (except for per share items)

Structure of the Electronic Suppliers Industry — **POOR**

The electronic suppliers industry is composed of firms that provide services to companies that use electronic components. The industry is very cyclical, subject to rapid changes in technology, and highly competitive (from both rivals and customers). Participants generally do not have proprietary manufacturing processes, and performance is tied to the success of their customers' products in the market. Significant pricing pressure and shifts in market share are common, and component supply shortages and rising commodity costs can pressure margins. We don't like the structure of the group.

Please select the following link (or copy to your browser) to view the full 16-page report:

http://www.valuentum.com/search2?searchtext=jbl&searchtype=symbol

Valuentum Retail Equity Research | Visit us at www.valuentum.com | Ratings as of 6-Jun-2013 | Data as of 31-May-2013

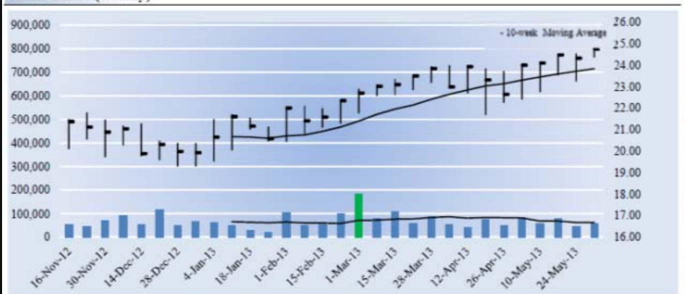
Johnson Outdoors Inc JOUT UNDERVALUED 5.1%

Buying Index™ 9 **Value Rating** ✓

Last Close	Estimated Fair Value	Fair Value Range	Investment Style	Sector	Industry
$24.75	$32.00	$26.00 - $38.00	SMALL-CAP VALUE	Consumer Discretionary	Sporting Goods

Johnson Outdoors operates in highly competitive markets.

Stock Chart (weekly)



The week with the highest trading volume out of the last 13 weeks was a week of heavy buying, or accumulation (green bar).

Investment Considerations

DCF Valuation	UNDERVALUED
Relative Valuation	ATTRACTIVE
ValueCreation™	GOOD
ValueRisk™	LOW
ValueTrend™	POSITIVE
Cash Flow Generation	MEDIUM
Financial Leverage	LOW
Growth	MODEST
Technical Evaluation	BULLISH
Relative Strength	NEUTRAL
Money Flow Index (MFI)	NEUTRAL
Upside/Downside Volume (U/D)	BULLISH
Near-term Technical Support, 10-week MA	24.00

DCF = Discounted Cash Flow; MFI, U/D = Please see glossary. MA = Moving Average

Business Quality

ValueRisk™ \ ValueCreation™	Very Poor	Poor	Good	Excellent
Low			■	
Medium				
High				
Very High				

Firms that generate economic profits with little operating variability score near the top right of the matrix.

Company Vitals

Market Cap (USD)	$232
Avg Weekly Vol (30 wks)	68
30-week Range (USD)	19.28 - 24.75
Valuentum Sector	Consumer Discretionary
5-week Return	9.2%
13-week Return	8.2%
30-week Return	20.7%
Dividend Yield %	0.0%
Dividends per Share	0.00
Forward Dividend Payout Ratio	0.0%
Est. Normal Diluted EPS	2.17
P/E on Est. Normal Diluted EPS	11.4
Est. Normal EBITDA	48
Forward EV/EBITDA	4.1
EV/Est. Normal EBITDA	3.8
Forward Revenue Growth (5-yr)	2.2%
Forward EPS Growth (5-yr)	13.6%

NMF = Not Meaningful; Est. = Estimated; FY = Fiscal Year

Returns Summary — 3-year Historical Average

Return on Equity	11.3%
Return on Assets	6.8%
ROIC, with goodwill	11.9%
ROIC, without goodwill	13.3%

ROIC = Return on Invested Capital; NMF = Not Meaningful

Leverage, Coverage, and Liquidity

In Millions of USD

Total Debt	9
Net Debt	-50
Total Debt/EBITDA	0.3
Net Debt/EBITDA	NMF
EBITDA/Interest	13.5
Current Ratio	3.1
Quick Ratio	1.7

NMF = Not Meaningful

Investment Highlights

• Johnson Outdoors Inc scores fairly well on our business quality matrix. The firm has put up solid economic returns for shareholders during the past few years with relatively low volatility in its operating results. Return on invested capital (excluding goodwill) has averaged 13.3% during the past three years.

• Johnson Outdoors makes branded seasonal, outdoor recreation products used primarily for fishing from a boat, diving, paddling, hiking and camping. Its brands include Minn Kota, Humminbird, and Eureka, among others.

• Johnson Outdoors Inc's cash flow generation and financial leverage aren't much to speak of. The firm's free cash flow margin has averaged about 4.2% during the past three years, lower than the mid-single-digit range we'd expect for cash cows. However, the firm's cash flow should be sufficient to handle its low financial leverage.

• The firm's share price performance has been roughly in line with that of the market during the past quarter. We'd expect the firm's stock price to converge to our fair value estimate within the next three years, if our forecasts prove accurate.

• Johnson Outdoors operates in highly competitive markets. Its primary rivals include Brunswick, Garmin, and Lowrance. Barriers to entry are limited.

Relative Valuation

	Forward P/E	PEG	Price / FV
Black Diamond	148.0	0.5	99.7%
Callaway Golf	-8.8	NMF	114.2%
Nautilus Inc	23.3	1.9	133.2%
Pool Corp	27.8	1.8	131.9%
Peer Median	25.6	1.8	123.0%
Johnson Outdoors Inc	**12.4**	**1.7**	**77.3%**

Price / FV = Current Stock Price divided by Estimated Fair Value

Financial Summary

	----- Actual -----		Projected
Fiscal Year End:	Sep-11	Sep-12	Sep-13
Revenue	407	412	433
Revenue, YoY%	6.5%	1.2%	5.0%
Operating Income	18	18	31
Operating Margin %	4.3%	4.3%	7.2%
Net Income	33	10	19
Net Income Margin %	8.0%	2.5%	4.4%
Diluted EPS	3.51	1.08	2.00
Diluted EPS, YoY %	398.8%	-69.3%	85.2%
Free Cash Flow (CFO-capex)	22	20	18
Free Cash Flow Margin %	5.3%	4.8%	4.2%

In Millions of USD (except for per share items)

Structure of the Sporting Goods Industry NEUTRAL

The seasonal sporting goods industry is heavily tied to sporting trends and relies on large athletic partners to distribute their athletic goods and apparel. Exclusive licenses can help certain firms achieve competitive advantages, and while scale helps, small companies have been able to carve out favorable niches. Unlike other apparel industries, we have yet to see tremendous online competition emerge. Potential firearm regulation could negatively impact sales, but most companies are well diversified. We're neutral on the space, but continued consolidation could ultimately benefit industrywide pricing and margins.

VALUENTUM

Page 1

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Valuentum Retail Equity Research | Visit us at www.valuentum.com | Ratings as of 7-May-2013 | Data as of 3-May-2013

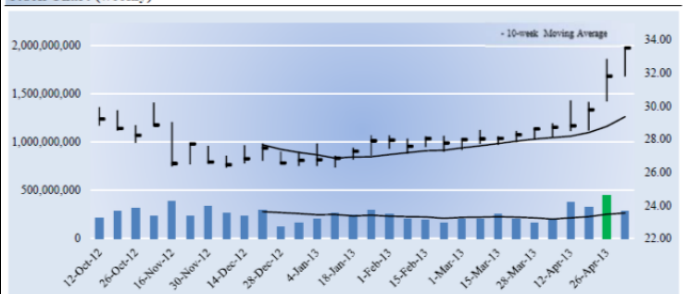
Microsoft MSFT UNDERVALUED 10.5%

Buying Index™ 8 | **Value Rating** ✓

Last Close	Estimated Fair Value	Fair Value Range	Investment Style	Sector	Industry
$33.49	$46.00	$37.00 - $55.00	MEGA-CAP VALUE	Information Technology	Software

Microsoft is one of the biggest bargains on the market today.

Stock Chart (weekly)



The week with the highest trading volume out of the last 13 weeks was a week of heavy buying, or accumulation (green bar).

Investment Considerations	
DCF Valuation	UNDERVALUED
Relative Valuation	ATTRACTIVE
ValueCreation™	EXCELLENT
ValueRisk™	LOW
ValueTrend™	POSITIVE
Cash Flow Generation	STRONG
Financial Leverage	LOW
Growth	MODEST
Technical Evaluation	NEUTRAL
Relative Strength	STRONG
Money Flow Index (MFI)	OVERBOUGHT
Upside/Downside Volume (U/D)	BULLISH
Near-term Technical Support, 10-week MA	29.00

DCF = Discounted Cash Flow; MFI, U/D = Please see glossary. MA = Moving Average

Business Quality — ValueCreation™

ValueRisk™	Very Poor	Poor	Good	Excellent
Low				
Medium				
High				
Very High				

Firms that generate economic profits with little operating variability score near the top right of the matrix.

Company Vitals	
Market Cap (USD)	$284,866
Avg Weekly Vol (30 wks)	249,422
30-week Range (USD)	26.26 - 33.52
Valuentum Sector	Information Technology
5-week Return	16.9%
13-week Return	20.2%
30-week Return	13.0%
Dividend Yield %	2.7%
Dividends per Share	0.92
Forward Dividend Payout Ratio	33.0%
Est. Normal Diluted EPS	3.28
P/E on Est. Normal Diluted EPS	10.2
Est. Normal EBITDA	38,643
Forward EV/EBITDA	7.0
EV/Est. Normal EBITDA	6.0
Forward Revenue Growth (5-yr)	5.8%
Forward EPS Growth (5-yr)	12.9%

NMF = Not Meaningful; Est. = Estimated; FY = Fiscal Year

Returns Summary	3-year Historical Average
Return on Equity	38.7%
Return on Assets	20.5%
ROIC, with goodwill	75.4%
ROIC, without goodwill	119.9%

ROIC = Return on Invested Capital; NMF = Not Meaningful

Leverage, Coverage, and Liquidity
In Millions of USD

Total Debt	11,944
Net Debt	-51,096
Total Debt/EBITDA	0.4
Net Debt/EBITDA	NMF
EBITDA/Interest	81.4
Current Ratio	2.6
Quick Ratio	2.4

NMF = Not Meaningful

Investment Highlights

• Microsoft's business quality (an evaluation of our ValueCreation™ and ValueRisk™ ratings) ranks among the best of the firms in our coverage universe. The firm has been generating economic value for shareholders with relatively stable operating results for the past few years, a combination we view very positively.

• The firm's shares are trading at an attractive level at this time. Given the company's track record of solid business performance, we'd take a closer look at picking up some of the firm's shares.

• Microsoft has an excellent combination of strong free cash flow generation and low financial leverage. We expect the firm's free cash flow margin to average about 31.7% in coming years. Total debt-to-EBITDA was 0.4 last year, while debt-to-book capitalization stood at 15.3%.

• Investors continue to focus on Microsoft's Windows business because it's been the bread-and-butter of the company for such a long time, but we think the company's other segments continue to be underappreciated. Shares look incredibly cheap at current levels, while providing investors with a fantastic dividend growth opportunity.

• The firm sports a very nice dividend yield of 2.7%. We expect the firm to pay out about 33% of next year's earnings to shareholders as dividends.

Relative Valuation	Forward P/E	PEG	Price / FV
Adobe Systems	32.3	2.1	114.7%
F5 Networks	16.7	1.5	90.8%
Oracle	12.3	1.5	79.5%
Salesforce.com	85.4	NMF	108.3%
Peer Median	24.5	1.5	99.6%
Microsoft	**12.0**	**1.3**	**72.8%**

Price / FV = Current Stock Price divided by Estimated Fair Value

Financial Summary	---- Actual ----		Projected
Fiscal Year End:	Jun-11	Jun-12	Jun-13
Revenue	69,943	73,723	78,884
Revenue, YoY%	11.9%	5.4%	7.0%
Operating Income	27,161	27,956	30,367
Operating Margin %	38.8%	37.9%	38.5%
Net Income	23,150	16,978	23,474
Net Income Margin %	33.1%	23.0%	29.8%
Diluted EPS	2.69	2.00	2.79
Diluted EPS, YoY %	28.2%	-25.9%	39.7%
Free Cash Flow (CFO-capex)	24,639	29,321	24,857
Free Cash Flow Margin %	35.2%	39.8%	31.5%

In Millions of USD (except for per share items)

Structure of the Software Industry — **VERY GOOD**

Firms that serve the mature software markets—or those consisting of basic business applications—have powerful distribution channels, large installed bases, and fortress balance sheets. These entrenched competitors benefit from significant customer switching costs, which make it nearly impossible for new entrants to gain a foothold. Participants generally benefit from high-margin license revenue and generate significant returns on investment. Still, the shift to cloud computing has created both opportunities and challenges, and the enterprise software landscape continues to evolve. We like the group.

Please select the following link (or copy to your browser) to view the full 16-page report:

http://www.valuentum.com/search2?searchtext=msft&searchtype=symbol

Our Methodology – The Valuentum Buying Index (VBI)

By Valuentum Analysts

But how, you will ask, does one decide what [stocks are] "attractive"? Most analysts feel they must choose between two approaches customarily thought to be in opposition: "value" and "growth,"...We view that as fuzzy thinking...Growth is always a component of value [and] the very term "value investing" is redundant.

-- Warren Buffett, Berkshire Hathaway annual report, 1993

At Valuentum, we take Buffett's thoughts one step further. We think the best opportunities arise from a complete understanding of all investing disciplines in order to identify the most attractive stocks at any given time. Valuentum therefore analyzes each stock across a wide spectrum of philosophies, from deep value through momentum investing. We think companies that are attractive from a number of investment perspectives--whether it be growth, value, income, momentum, etc.--have the greatest probability of capital appreciation and relative outperformance. The more investors that are interested in the stock for reasons based on their respective investment mandates, the more likely it will move higher.

As such, the Valuentum Buying Index (VBI) combines rigorous financial and valuation analysis with an evaluation of a firm's technicals and momentum indicators to derive a score between 1 and 10 for each company (10=best). The VBI places considerable emphasis on a firm's DCF valuation, its relative valuation versus peers (both forward PE and PEG ratios), as well as its technicals in order to help investors pick the best entry and exit points on the most interesting stocks. We believe our methodology helps identify the most attractive stocks at the best time to buy, helping to avoid value traps and lagging performance due to the opportunity cost of holding a stock with great potential but at an inopportune time.

A Rigorous, Discounted Cash Flow Valuation Assessment

Our methodology starts with in-depth financial statement analysis, where we derive our ValueCreation, ValueRisk, and ValueTrend ratings, which together provide a quantitative assessment of the strength of a firm's competitive advantages. After evaluating historical trends, we then make full annual forecasts for each item on a company's income statement and balance sheet to arrive at a firm's future free cash flows. We derive a company-specific cost of equity (using a fundamental beta based on the expected uncertainty of key valuation drivers) and a cost of debt (considering the firm's capital structure and synthetic credit spread over the risk-free rate), culminating in our estimate of a company's weighted average cost of capital (WACC). We don't use a market price-derived beta, as we embrace market volatility, which provides investors with opportunities to buy attractive stocks at bargain-basement levels.

We assess each company within our complete three-stage free cash flow to the firm (enterprise cash flow) valuation model, which generates an estimate of a company's equity value per share based on its discounted future free cash flows and the company's net balance sheet impact, including other adjustments to equity value (namely pension and OPEB adjustments). Our ValueRisk rating, which considers the underlying uncertainty of the capacity of the firm to continue to generate value for shareholders, sets the margin of safety bands around this fair value estimate. For firms that are trading below the lower bound of our margin of safety band, we consider these companies undervalued based on our DCF process. For firms that are trading above the higher bound of our margin of safety band, we consider these companies overvalued based on our DCF process.

A Forward-Looking Relative Value Assessment

Our discounted cash-flow process allows us to arrive at an absolute view of the firm's intrinsic value. However, we also understand the critical importance of assessing firms on a relative value basis,

Our Methodology – The Valuentum Buying Index continued on next page

Our Methodology – The Valuentum Buying Index continued from previous page

versus both their industry and peers. Many institutional money-managers--those that drive stock prices—pay attention to a company's price-to-earnings (PE) ratio and price-earning-to-growth (PEG) ratio in determining whether entities are undervalued. With this in mind, we have included a forward-looking relative value assessment in our process to further augment our rigorous discounted cash-flow process. If a company is undervalued on both a price-to-earnings ratio and a price-earnings-to-growth (PEG) ratio versus industry peers, we would consider the firm to be attractive from a relative value standpoint.

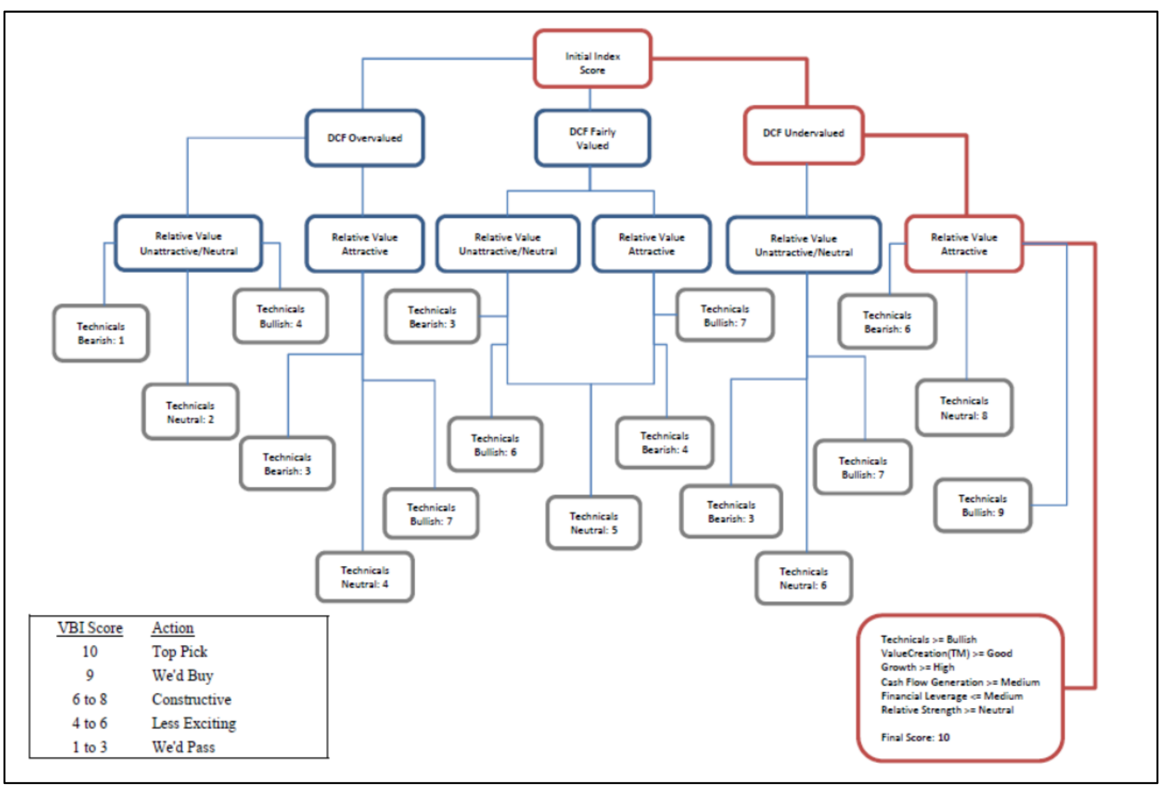
Avoiding Value Traps and Opportunity Cost

Once we have estimated a firm's intrinsic value on the basis of our discounted cash-flow process, determined if it is undervalued according to its firm-specific margin of safety bands, and assessed its relative value versus industry peers, we then evaluate the company's technical and momentum indicators to pin-point the best entry and exit points on the stock. An evaluation of its moving averages, relative strength, upside-downside volume, and money flow index are but a few considerations we look at with respect to our technical and momentum assessment of a company's stock.

Putting It All Together - the Valuentum Buying Index

Let's follow the red line on the flow chart below to see how a firm can score a 10, the best mark on our index (a "Top Pick"). First, the company would need to be 'UNDERVALUED' on a DCF basis and 'ATTRACTIVE' on a relative value basis. The stock would also have to be exhibiting 'BULLISH' technicals. The firm would need a ValueCreation rating of 'GOOD' or 'EXCELLENT', exhibit 'HIGH' or 'AGGRESSIVE' growth prospects, and generate at least a 'MEDIUM' or 'NEUTRAL' assessment for cash flow generation, financial leverage, and relative price strength.

This is a tall order for any company, but we're looking to deliver the very best of ideas to our clients and subscribers. Firms that don't make the cut for a 10 are ranked accordingly, with the least attractive stocks garnering a score of 1 ("We'd sell"). Most of our coverage universe falls between 3 and 7, but at any given time thee could be large number of companies garnering either high or low scores, especially at market lows or tops, respectively.



Valuentum Best Ideas Newsletter: Volume 3, Issue 9

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