OUR BEST IDEAS NEWSLETTER

Valuentum Securities

Stock Analysis: From Value through Momentum Investing

November 15, 2013
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Valuentum Securities Inc.
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Portfolio Return	Benchmark Return	Outperformance
67.1%	40.8%	26.4%

Portfolio Inception Date: May 17, 2011

INSIDE THIS ISSUE

1 The Best Ideas Portfolio Continues to Trounce the Market

2 Third-Quarter Industrial Earnings Support Exposure in Best Ideas Portfolio (see article for tickers)

5 Looking for Alpha? It's In Our Best Ideas Newsletter (tickers: BIDU, BWLD)

7 General Electric Reveals Order Strength; Registers Record Backlog (ticker: GE)

8 Our Best Ideas Portfolio (see article for tickers)

9 Record Results For Ford and Precision Castparts (tickers: F, PCP)

11 Third-Quarter Churn Rate at DirecTV's US Business Is Best In 6 Years (ticker: DTV)

11 Union Pacific Reports Best-Ever Quarterly Results; Thesis Remains Intact (ticker: UNP)

12 No Disappointments in "Waste Land" (tickers: RSG, WCN, WM)

13 Rio Tinto Says Iron Ore Production Breaks Record; Iron Ore Prices Recover (ticker: RIO)

14 Visa And Mastercard Gushing With Cash (tickers: V, MA)

15 The Curious Cases of Intuitive Surgical and Teva Pharma: What We Have Learned (tickers: ISRG, TEVA)

18 Surveying Valuentum Buying Index Performance In The Restaurant Space (see article for tickers)

20 Ideas for Your Radar

22 Featured Reports: GE, CLR, EOG

25 Our Stock-Selection Methodology

The Best Ideas Portfolio Continues to Trounce the Market

By Brian Nelson, CFA

For our new members, this is our Best Ideas Newsletter. We house our Best Ideas portfolio in this monthly publication. The Best Ideas portfolio can always be found on page 8 of the Best Ideas Newsletter.

The Best Ideas portfolio includes companies that have passed the test of our analyst team. First, these firms generally have scored highly on the Valuentum Buying Index, a rating system that ranks the timeliness of ideas on the basis of 1 through 10 (with 10 being the best).

Once a best idea is added to the portfolio, we typically hold on to it until it registers a 1 or 2 on the Valuentum Buying Index. We may make tactical changes to a stock's weighting in the portfolio or remove a position on the basis of diversification considerations, but for the most part, the Valuentum Buying Index is the primary criteria for portfolio additions and removals.

So far, the Valuentum Buying Index has performed wonderfully. An update on the performance calculation of the Valuentum Buying Index can be found at the following link:

http://www.valuentum.com/articles/20131026_1

Ideas included in the Best Ideas portfolio should be considered our best ideas at any given time. We intend to capture the entire stock pricing cycle (VBI: high → low) with the ideas in the portfolio and not truncate profit potential. Incremental ideas such as General Electric this month, for example, should be considered our next best idea after portfolio constituents.

The market continues to rocket higher, and the cash-rich Best Ideas portfolio continues to keep pace. We trust you're happy with fresh all-time highs!

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= All Time High!

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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.

Third-Quarter Industrial Earnings Support Exposure in Best Ideas Portfolio

By Brian Nelson, CFA

For starters, our piece on General Electric's (GE) third-quarter earnings (see page 7) is a must-read. The step-up in backlog and order trends at the industrial behemoth are quite remarkable, and we think GE's performance bodes well for the sector as a whole. Still, let's drill down on a few themes across the industrial space and how our Best Ideas portfolio is well-positioned to capture the strength of underlying trends.

Danaher (DHR)

Danaher reported third-quarter results that showed revenue expansion of 5.5% and diluted net earnings per share growth of 9%. The company generated 30 basis points of operating-margin improvement and generated more than $800 million in free cash flow, or **about 17.8% of revenue** (a very strong number). 'Test & Measurement' revenues faced modest pressure, 'Environmental' sales leapt 10% (4.5% core), 'Life Sciences & Diagnostics' revenue jumped 10.5% (6% core), 'Dental' sales advanced 4.5% (3.5% core), and revenue from 'Industrial Technologies' increased 1% (-1% core).

The firm's 'Life Sciences & Diagnostics' segment—which houses Beckman Coulter, Leica, and Radiometer—revealed the greatest absolute increase in revenue expansion and the best operating profit margin improvement (+250 basis points) of any of Danaher's business lines. The segment's gem Beckman Coulter, which Danaher acquired in early 2011, makes devices that automate biomedical testing (blood, immunoassay, chemical), and its systems are found in hospitals around the world. The firm bumps heads with firms such as Becton, Dickinson (BDX), Johnson & Johnson (JNJ), Siemens (SI), Roche and Abbott (ABT). We're viewing Danaher's strong performance in this area as support for our holding the Health Care Select SPDR (XLV) in the portfolio of our Best Ideas Newsletter.

Dover (DOV)

Dividend Aristocrat Dover reported third-quarter results that revealed 7% revenue growth and 20% earnings expansion. Bookings jumped 9%, segment margins improved 100 basis points, and free cash flow jumped 30% to $283 million (about 12% of revenue). Though the company noted bookings expansion was broad-based, the firm's overall book-to-bill was 0.96 (we'd prefer this to be greater than 1). Still, we're not reading too much into the slight shortfall in replacing revenue with new orders. The strongest performing segment on an organic basis continues to be its 'Communication Technologies' operations.

Segment	2012 Revenue Mix	2013F Organic Growth	2013F Acquisition Growth*	Total
Communication Technologies	19%	6% - 7%	-	6% - 7%
Energy	27%	≈ 3%	≈ 3%	≈ 6%
Engineered Systems	42%	≈ 2%	≈ 8%	≈ 10%
Printing & Identification	12%	1% - 2%	-	1% - 2%
Total	**≈ $8.1 B**	**≈ 3%**	**≈ 4%**	**≈ 7%**

Image Source: Dover

Third-Quarter Industrial Earnings...continued on next page

Third-Quarter Industrial Earnings...from previous page

The company's 'Communication Technologies' segment serves the consumer electronics market in design and assembly of micro-acoustic audio equipment for use in personal mobile handsets. Dover noted that it experienced solid growth in this division thanks to new smartphone product launches. We believe we're adequately exposed to this strength via our position in Apple (AAPL) in the portfolio of our Best Ideas Newsletter.

Honeywell (HON)

Honeywell's third-quarter results weren't as strong as we would have liked, but they weren't bad either. Revenue advanced 1% on an organic basis and net income nudged 4% higher on 90 basis-points of improvement in operating margin. Free cash flow came in at $937 million or about 9.7% of sales in the period. On an organic basis, the firm's 'Transportation Systems' segment showed the most promise, jumping 5% from the year-ago quarter (its 'Aerospace' division was weighed down by defense and space shipment delays and DoD challenges).

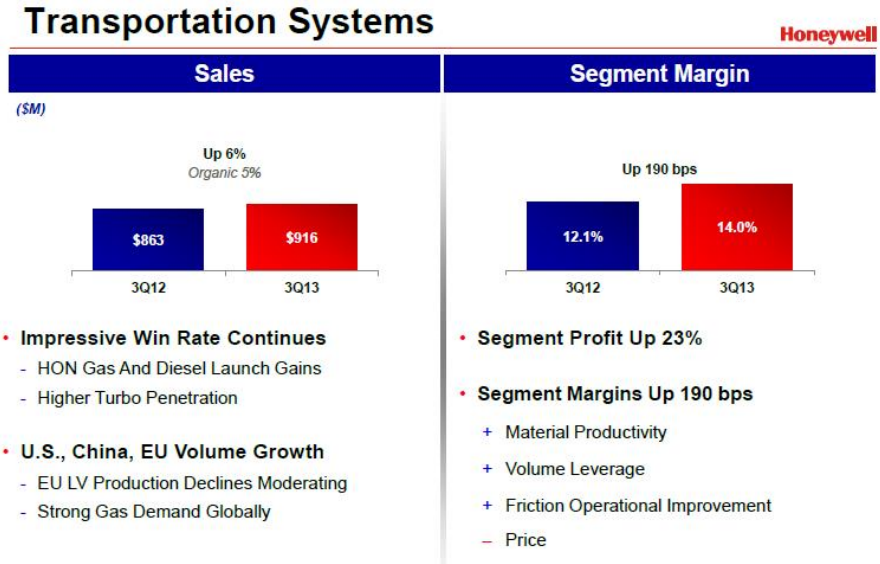

Image Source: Honeywell

The firm's 'Transportation Systems' division makes engine-boosting systems for passenger cars and commercial vehicles. It is also a leading provider of braking products. We were pleased to see the strength in this division of Honeywell and welcomed management's comments on the call suggesting that European light vehicle production declines are moderating. We think this bodes well for Best Ideas portfolio holding Ford (F).

Ingersoll-Rand (IR)

Ingersoll-Rand issued third-quarter results that showed revenue growth of 4% and better-than-expected adjusted earnings per share from continuing operations. The company noted that bookings advanced 7% and that its adjusted operating margin increased 140 basis points to 14% from 12.6%. Ingersoll-Rand's 'Residential' segment led the charge with adjusted segment revenue improvement of 6%.

Third-Quarter Industrial Earnings...continued on next page

*Third-Quarter Industrial Earnings…*from previous page

The firm's 'Residential' segment provides customers with a broad range of products and services including mechanical and electronic locks and energy-efficient HVAC systems. This segment houses well-known brands such as American Standard, Schlage and Trane. Management noted that "orders were up double digits in commercial HVAC units," a positive sign for the US construction markets and for peers Lennox (LII) and Johnson Controls (JCI). Though we think many firms are ultimately levered to the health of the US construction markets (and we remain cognizant of the negative impact rising interest rates may cause), we continue to be exposed to the housing recovery via diversified banking ETFs, the Financial Select SPDR (XLF) and SPDR S&P Bank ETF (KBE). We're not looking to increase our exposure to the housing or banking sector at this time.

Parker-Hannifin (PH)

Parker-Hannifin's fiscal 2014 first-quarter (calendar 2013 third-quarter) results were relatively mediocre, but the firm's fiscal year 2014 guidance stole the show.

Revised FY2014 Guidance

Reconciliation to prior guidance

	Low	Midpoint	High
Diluted EPS	$ 7.78	$ 8.08	$ 8.38
Diluted EPS - Excluding Expected JV Gain	$ 6.10	$ 6.40	$ 6.70

Though we're not exactly comfortable with the wide earnings outlook range, the company did note that order rates turned positive in the period. The aerospace segment was a relatively sore spot for Honeywell given its defense exposure, but Parker-Hannifin noted that orders jumped 11% in its 'Aerospace Systems' segment. On the call, the firm noted that its commercial aerospace aftermarket and commercial aerospace OEM markets remain positive and that its aerospace backlog is at an "all-time high." Our favorite idea in the aerospace industry continues to be Best Ideas portfolio holding Precision Castparts (PCP).

Valuentum's Take

We like what we're seeing in the industrial sector. General Electric's performance provided a nice backdrop for the future outlook, and underlying trends in the calendar third-quarter results of Danaher, Dover, Honeywell, Ingersoll-Rand, and Parker-Hannifin play into the hands of the exposure we currently have in the portfolio of our Best Ideas Newsletter. This is not by accident.

Strength in Danaher's Beckman Coulter division supports our healthcare exposure, while smartphone proliferation shown in Dover's quarter showcases the market strength behind Best Ideas portfolio holding Apple. Honeywell's 'Transportation Systems' business is encouraging for Ford, while resilience in the construction markets revealed in Ingersoll-Rand's third-quarter indirectly supports underlying banking strength in the US (and our diversified exposure there). And finally, Parker-Hannifin's aerospace order growth and backlog speak to our well-documented exposure to the aerospace end market and our current position in Precision Castparts.

Looking for Alpha? It's In Our Best Ideas Newsletter

By RJ Towner

Best Ideas portfolio holdings Buffalo Wild Wings (BWLD) and Baidu (BIDU) reported fantastic third-quarter results sending both of their shares higher!

Baidu was added to our Best Ideas portfolio August 1, 2013 at $133.60 per share. A 23% gain in just a couple months isn't too bad, and we're expecting further upside to shares. Buffalo Wild Wings has been a holding in our Best Ideas portfolio for some time, with our cost basis at $65.42 -- shares have doubled and then some since that time.

Remember: We run a relatively concentrated portfolio of best ideas, so when we highlight a new idea, it's a big deal. We put our reputation on the line with each and every call we make. Our best ideas are always included in our Best Ideas portfolio, while our best dividend growth ideas are always included in our Dividend Growth portfolio.

Buffalo Wild Wings

The saying "Make everything as simple as possible, but not simpler" was coined by legendary physicist Albert Einstein, and it aptly applies to Buffalo Wild Wings. The firm isn't reinventing the wheel by any means; it simply provides customers reasonably priced wings and beer with dozens of TVs to watch live sports.

Buffalo Wild Wings' business model continues to be tremendously successful with **revenue surging 28%** year-over-year to $316 million in its third quarter (same store sales increased 4.8% and 3.9% at company-owned and franchised restaurants). **Diluted earnings per share jumped 65%** year-over-year to $0.95 thanks in part to lower chicken wing costs. Both figures exceeded consensus estimates.

The firm generated $25.8 million in free cash flow during the period, an impressive number given that it spent nearly $100 million on expanding its store footprint. Buffalo Wild Wings is only in the "fifth inning" of its expansion efforts. With 959 locations, the company sees the opportunity to nearly double its restaurant count to 1,700 units. For 2014, the firm expects to achieve 20% net earnings growth and open its 1,000th store during the year.

Management also noted that its current food to drink mix is 79/21. Alcohol and beverage sales are far more profitable than food sales, so each percentage point shift in the mix in favor of beverages provides Buffalo Wild Wings with even greater earnings power. The company is also adding new products (salads) that appeal to different customers, expanding its consumer profile. Buffalo Wild Wings isn't settling for adequate performance, rather CEO Sally Smith and company, like a great sports organization, are sticking to the plan and striving for excellence.

*Looking for Alpha?...*continued on next page

*Looking for Alpha?...*from previous page

Baidu

Search has been very, very good to our Best Ideas portfolio. Google (GOOG), another Best Ideas portfolio holding, posted strong third-quarter earnings October 17 that sent shares north of $1,000 each for the first time in history.

Baidu, often considered the Google of China, followed suit in its third quarter. Top-line expansion was tremendous, with sales soaring 42% year-over-year to $1.5 billion. Earnings per share were about equal to the year-ago period at $1.48, but that figure easily exceeded consensus estimates. The firm remains in expansion mode, akin to Google a few years ago or Facebook (FB) and Amazon (AMZN) now. Nevertheless, even as operating expenses grew, **the firm generated $575 million in free cash flow during the third quarter, equal to about 40% of total revenue**.

Baidu continues to find new online marketing customers, but it also is generating 19% more revenue per online marketing customer than it was a year ago. With hundreds of millions of dollars spent to improve its search algorithm and service, Baidu continues to fend-off competition from the likes of Qihoo 360, **controlling more than 60% of all search traffic in China (see image below)**. We believe this success has been largely aided by the company's decision to plough resources into improving the Baidu algorithm and mobile experience.

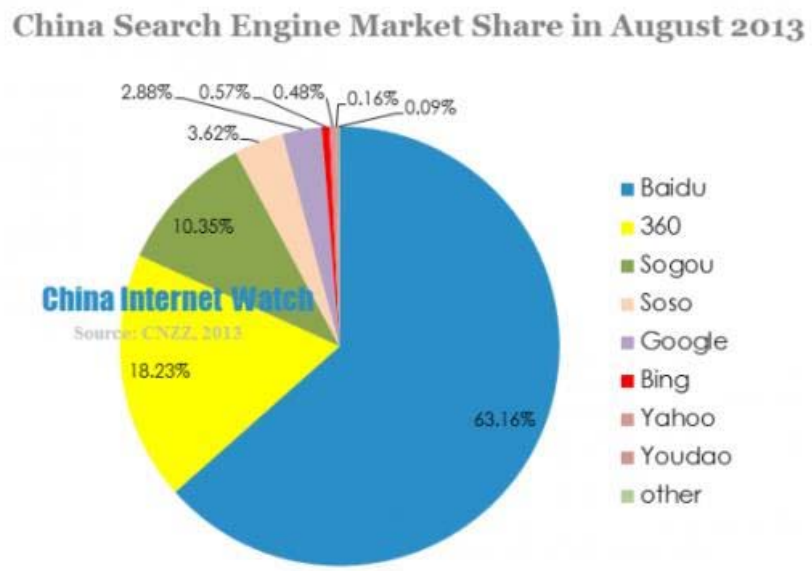

Image Source: China Internet Watch

Without question, the Chinese Internet market represents one of the best secular growth opportunities. Not only does the market already have more than **double the amount of users in the US**, but it also has roughly half the penetration rate. The company shows no signs of slowing, guiding to fourth-quarter revenue growth of 45.5%-46.9% compared to the prior-year period.

Valuentum's Take

Baidu and (especially) Buffalo Wild Wings have been solid performers in our Best Ideas portfolio. Baidu's shares continue to rapidly converge to our fair value estimate, while Buffalo Wild Wings' shares are starting to get a little pricey. Both portfolio holdings, however, have years of growth ahead of them. We trust you continue to profit greatly!

General Electric Reveals Order Strength; Registers Record Backlog

By Brian Nelson, CFA

General Electric (GE) put up a darling of an order number with its third-quarter financial results. Though revenue and operating income faced pressure during the period due to asset reductions at GE Capital and foreign-exchange headwinds, the industrial conglomerate's order performance was off the charts: **US orders jumped 18%**, **Europe orders advanced 17%**, and **growth market orders leapt 22%**.

Needless to say, the global business environment improved significantly during the third quarter, and we're not sure the threat of a US government shutdown (and by extension, the shutdown itself) did much to impede the business of global industrial conglomerates. **GE's backlog of equipment and services at the end of the quarter was its highest ever at $229 billion (up $6 billion sequentially)**, resulting in a book-to-bill ratio of 1.2 (a number above 1 is solid). We pay more attention to the pace of the firm's orders and book-to-bill ratio (as an indication of future performance) than we do its already-reported (past) results.

We were also pleased that the firm continues to shrink GE Capital and that industrial segment margins continue to advance (up 120 basis points in the quarter). Given the order strength, one may think GE is offering some hefty discounts, but management indicated that infrastructure **order pricing was flat** during the period. If that's the case, we can only expect margins on its current order book to be better than existing performance, particularly as management rolls out simplification efforts across the organization. GE generated industrial cash flow of $5.9 billion in the quarter, excluding NBCUniversal deal-related items, and now sits on $87 billion of consolidated cash and cash equivalents.

Valuentum's Take

General Electric has transformed itself from the days it had to slash its dividend back in 2009, as GE Capital is much smaller and poses less risk to the overall financial health of the organization. It's hard not to like the pace of orders, the size of its backlog, and the trajectory of industrial segment margins. We added the firm's shares to the portfolios of our Dividend Growth Newsletter and Best Ideas Newsletter on October 21.

Our Best Ideas Portfolio

By Valuentum Analysts

Portfolio Return	Benchmark Return	Outperformance
67.1%	40.8%	26.4%

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, as well as analysis and trends impacting companies in our Best Ideas portfolio. We currently have about 25% 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 November 14, 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	528.16	12,147.68	7.3%	48.9%
Altria Group	MO	8	3	28-Jun-11	26.43	252	37.70	9,500.40	5.7%	57.9%
Baidu	BIDU	10	10	1-Aug-13	133.60	20	158.99	3,179.80	1.9%	18.7%
Buffalo Wild Wings	BWLD	7	6	13-Jul-11	65.42	77	145.35	11,191.95	6.7%	121.9%
DirecTV	DTV	9	6	15-Apr-13	55.02	55	64.35	3,539.25	2.1%	16.7%
eBay	EBAY	10	10	3-Oct-11	31.04	100	52.88	5,288.00	3.2%	70.4%
Financial Select SPDR Fund	XLF	NA	6	9-Jan-11	13.46	150	21.03	3,154.50	1.9%	59.5%
Ford Motor	F	7	7	12-Sep-11	10.69	650	17.09	11,108.50	6.6%	63.6%
NEW: General Electric	**GE**	**7**	**7**	**21-Oct-13**	**26.18**	**300**	**26.99**	**8,097.00**	**4.8%**	**3.0%**
Google	GOOG	10	6	23-Oct-12	683.49	4	1035.23	4,140.92	2.5%	51.1%
Health Care ETF	XLV	9	5	22-May-12	36.60	125	54.01	6,751.25	4.0%	50.7%
Intel	INTC	6	6	12-Sep-11	20.48	150	24.39	3,658.50	2.2%	26.1%
Intuitive Surgical	ISRG	5	3	22-May-12	489.51	7	397.27	2,780.89	1.7%	-19.0%
Precision Castparts	PCP	8	6	6-Jun-11	152.07	40	248.87	9,954.80	6.0%	63.6%
SPDR S&P Bank ETF	KBE	NR	NR	9-Jan-12	21.07	100	31.88	3,188.00	1.9%	54.8%
Republic Services	RSG	8	7	19-May-11	31.42	201	34.99	7,032.99	4.2%	20.3%
Rio Tinto	RIO	9	6	22-May-12	46.40	75	51.75	3,881.25	2.3%	16.7%
Teva Pharma	TEVA	6	3	24-Jul-13	41.22	77	38.35	2,952.95	1.8%	-6.4%
Union Pacific	UNP	6	3	24-Jul-13	159.34	20	158.30	3,166.00	1.9%	-0.4%
Visa	V	7	7	30-Nov-11	107.46	47	200.15	9,407.05	5.6%	88.1%
NEW: Facebook	**FB - call option**			**21-Oct-13**	**963.25**	**5 contracts**	**33.00**	**165.00**	**0.1%**	**-82.9%**
---> $80 strike, March 2014 expiration										
Cash								42,835.33	25.6%	0.0%
Bearish										
SPDR S&P 500 Trust ETF	SPY - put option			23-May-13	644.25	1 contract	0.00	0.00	0.0%	-100.0%
---> $160 strike, December 2013 expiration										
Best Ideas Portfolio Value								**167,122.01**		**67.1%**
S&P 500 Index (SPY)				17-May-11	132.69	754	179.27	135,104.38	96.0%	
Cash								5,650.01	4.0%	
Benchmark Portfolio Value								**140,754.39**		**40.8%**
Relative Outperformance										**26.4%**

This portfolio is not a real money portfolio. Data as of November 14, 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).

Standard Disclaimer: Our Best Ideas List is for information purposes only and should not be considered a solicitation to buy or sell any security. Valuentum is not responsible for any errors or omissions or for results obtained from the use of our Best Ideas List and accepts no liability for how readers may choose to utilize the content.

Record Results For Ford and Precision Castparts

By Valuentum Analysts

I guess you can say a 'Red Letter Day' for our Best Ideas portfolio can be more appropriately called a 'Green Letter Day,' as stock-market advances are typically colored in green. That happened this month for two holdings in our Best Ideas portfolio: Ford (F) and Precision Castparts (PCP). These are two companies that we have pounded the table on repeatedly during the past couple years.

Ford Posts Record 3Q Pre-Tax Profit

Ford (F) posted excellent third-quarter results that showed fantastic top and bottom-line performance. Total company revenue advanced an impressive 12% thanks to wholesale volume expansion of 16% and **year-over-year share gains in all regions.** The auto maker also posted record third-quarter pre-tax profit of $2.59 billion, an increase of $426 million (19.7%) compared with a year ago – and marks the 17th consecutive quarter of profitability. Bullet points in press releases from Ford haven't been this good in a long time, and **we expect them to get even better**:

• **Record** third quarter pre-tax profit for Automotive sector; continued strong results in North America and a combined profit for regions outside North America for first time since second quarter 2011; **record** third quarter profit for Asia Pacific Africa; profitable in South America; loss in Europe, but improved substantially from second quarter and a year ago. Ford Credit remained solidly profitable

• **Record** third quarter Automotive operating-related cash flow of $1.6 billion; 14th consecutive quarter of positive operating-related cash flow; strong liquidity of $37.5 billion, an increase of $400 million from the end of the second quarter

• Improved full year company financial guidance: Ford now expects total company pre-tax profit to be higher than 2012, improved from prior guidance of equal to or higher than 2012. Ford also now expects Automotive operating margin to be higher than last year rather than about equal. Ford continues to expect Automotive operating-related cash flow to be substantially higher than 2012

Wow! We've been highlighting Ford as one of our best ideas since 'We Outline(d) Our Bullish Case for Ford' in August 2011. It's hard not to like the firm's progress on operational metrics, and the auto maker continues to exceed originally-planned financial metrics for 2013.

	2012 Full Year Results	2013 Full Year Plan	2013 Full Year Outlook	Memo: 2013 First Nine Months Results
Planning Assumptions				
Industry Volume* -- U.S. (Mils.)	14.8	15.0 - 16.0	15.9	15.8
Industry Volume* -- Europe (Mils.)**	14.0	13.0 - 14.0	13.6	13.6
Industry Volume* -- China (Mils.)	19.0	19.5 - 21.5	21.7	21.6
Operational Metrics				
Compared with Prior Year:				
- U.S. Market Share	15.2 %	Higher	On Track	15.8 %
- Europe Market Share**	7.9	About Equal	On Track	8.0
- China Market Share***	3.2	Higher	On Track	4.0
- Quality	Mixed	Improve	Mixed	Mixed
Financial Metrics				
Compared with Prior Year:				
- Total Company Pre-Tax Operating Profit (Bils.)****	$ 8.0	About Equal	Higher	$ 7.3
- Automotive Operating Margin****	5.3 %	About Equal / Lower	Higher	6.2 %
- Automotive Operating-Related Cash Flow (Bils.)*****	$ 3.4	Higher	Substantially Higher	$ 5.6

* *Includes medium and heavy trucks*
** *The 19 markets Ford tracks*
*** *Includes Ford and JMC brand vehicles produced in China by unconsolidated affiliates*
**** *Excludes special items; Automotive operating margin is defined as Automotive pre-tax results, excluding special items and Other Automotive, divided by Automotive revenue*
***** *See "Operating-Related Cash Flows Reconciliation to GAAP" table on page 13; full year 2012 reconciliation provided in Ford's 2012 Form 10-K report*

Image Source: Ford

*Record Results...*continued on next page

Record Results…**from previous page**

Our fair value estimate for Ford is $22 per share, but we could see valuation upside to as much as $30 per share (the high end of our fair value range), if North American performance continues to be strong and Europe turns the corner. We're still holding the outsize position in Ford in the portfolio of our Best Ideas Newsletter.

Precision Castparts Blows By Fiscal 2Q Expectations

Metal-bending aerospace supplier, Precision Castparts (PCP), posted fantastic second-quarter fiscal 2014 results. The company registered **record** sales of $2.36 billion (up 23%; 6% organic), **record** diluted earnings per share of $2.90 from continuing operations (up 28%), and a **record** consolidated segment operating margin of 27.5%. Management credited strong commercial aerospace demand, a steady recovery in power markets, and top- and bottom-line contributions from TIMET. The firm's commentary continues to be very positive, and the following is what management had to share about the outlook for each of the firm underlying business segments:

Investment Cast Products: "Going forward, accelerated sales gains will be driven by further demand from production rate step-ups on existing platforms, continued frequency of takeoffs and landings, and the segment's increased penetration on the new development engines for re-engined narrow-body aircraft platforms, which are scheduled to ramp up quickly into full production."

Forged Products: "Similar to Investment Cast Products, the segment is well-positioned to benefit from ramps in commercial aircraft build rates and the acceleration of the new re-engining narrow-body platforms."

Airframe Products: "From a performance point of view, the segment is successfully moving higher volumes over an improving cost structure and is rapidly integrating new acquisitions into the overall operations."

Our thesis regarding Precision Castparts' potential for significant operating margin expansion remains intact (notice it set a record in that department this quarter). We're huge fans of CEO Mark Donegan and his demonstrated ability to continue to take costs out of the business. Valuentum members should be aware of our well-documented positive view on the burgeoning aerospace cycle. Precision Castparts remains a core holding in the portfolio of our Best Ideas Newsletter.

"At this moment in time, the opportunities for this Company are better than ever." – CEO Mark Donegan, October 24, 2013.

Third-Quarter Churn Rate at DirecTV's US Business Is Best In 6 Years

By Brian Nelson, CFA

DirecTV (DTV) reported better-than-expected third-quarter results. The firm's quarterly revenue of $7.9 billion advanced more than 6% on a year-over-year basis, while third-quarter earnings per share exceeded forecasts by more than $0.27, coming in at $1.28, an impressive bottom-line showing. The firm repurchased $1.3 billion of stock in the third quarter, which led to the significant bottom-line beat. With every share of stock that DirecTV purchases, management is generating economic profit for shareholders.

DirecTV US added 139,000 net new subscribers in the period as it achieved the lowest third-quarter churn rate in 6 years. DirecTV US ARPU (average revenue per user) growth was 6.2%, and DirecTV Latin American subscriber growth was strong over the last year's quarterly mark. OPBDA (operating profit before depreciation and amortization) advanced 12% and 23% in DirecTV US and DirecTV Latin America, respectively. Consolidated OPBDA jumped 15%, showcasing the firm's strong operating leverage (operating income advanced more than twice as fast as sales expansion), and free cash flow increased 17%, to $372 million (or 4.7% of sales).

Valuentum's Take

DirecTV remains a holding in the portfolio of our Best Ideas Newsletter, and we didn't see anything in its third-quarter results that would challenge our valuation thesis on the company. We'd like to continue to see the firm gobble up its undervalued stock in the periods ahead and expect valuation upside to $80 per share on the basis of our fair value estimate.

Union Pacific Reports Best-Ever Quarterly Results; Thesis Remains Intact

By Valuentum Analysts

Union Pacific (UNP) reported its "best-ever quarterly results" when it posted third-quarter performance. The quarterly results, in our opinion, were truly fantastic. The company's operating ratio came in at a record 64.8% (the firm's best ever—1.8 points better than the year-ago period), as the railroad offset lower coal and grain volumes with strong pricing and productivity improvements. Operating revenue advanced 4% thanks mainly to core pricing gains, which translated into 10% and 13% increases in operating income and diluted earnings per share, respectively. The strength came in spite of lost revenue and increased costs from the flooding in Colorado (which hurt operating income by roughly $10 million). Year-to-date, Union Pacific has hauled in $2.25 billion in free cash flow, or 13.8% of revenue (a very nice figure). Our thesis on Union Pacific remains intact, and the firm remains a holding in the portfolio of our Best Ideas Newsletter.

No Disappointments in "Waste Land"

By Brian Nelson, CFA

The US non-hazardous solid-waste services industry generates annual revenue in excess of $50 billion, a staggering number just to keep our streets clean. Waste Management (WM), Republic Services (RSG), and Waste Connections (WCN) dominate this market, generating greater than 60% of industry revenues and controlling an equal percentage of valuable disposal capacity. The top line for the group can be expected to expand at a nominal-GDP rate, with **pricing growth** in the industry adding an additional tailwind thanks to recent consolidation (Republic Services/Allied Waste), a rational focus on return on invested capital, and cost pressures facing independent mom-and-pop trash companies and municipalities.

Operators generate strong and predictable cash flow. Within the collection line of a waste hauler's business, residential services provided to municipalities and individual households are on a service-based model (not-volume based) and can largely be viewed as insulated from economic pressures. Such a constant revenue stream helps to mitigate cyclical pressures in a trash taker's commercial collection and industrial roll-off lines, which also fall into the overall waste-collection category. Cell-by-cell landfill build-out provides additional flexibility with respect to capital outlays, as haulers can scale back expenditures during troubled economic times.

Year-to-date, Waste Management's third-quarter performance shows free cash flow (cash from operations less capital expenditures) of $1.03 billion, roughly 9.8% of sales, while Republic Services' year-to-date mark of $448.5 million represents 7.1% of sales. Waste Management more effectively converts sales to free cash flow, as capital expenditures (as a percentage of sales) are roughly 3 percentage points lower than those of Republic (7.9% versus 11%). We think Republic's capital requirements will steadily decline in coming years to a high-single-digit mark as percentage of sales once the hefty equipment expenditures of today are completed.

Transfer and disposal is the most lucrative revenue stream in the waste business. **Landfill ownership can largely be viewed as the primary competitive advantage for a solid-waste operator.** Though anyone that can finance a truck can bid on collection routes (service is undifferentiated), new entrants are at a significant disadvantage for disposal. For starters, building a landfill is expensive, time-consuming (permits can take 3-7 years to obtain, sometimes longer), and NIMBY (not-in-my-backyard) opposition has only increased with suburban sprawl. Subtitle D of the Resource Conservation and Recovery Act (1991) significantly increased the cost and complexity of landfill ownership (composite liners, leachate collection systems, zoning, etc.). As a result, many landfills in the US have been closed, and disposal airspace should only become more valuable over time.

Since collected waste must go somewhere (direct haul is only practical for 40-50 miles), the company that controls the disposal assets in a given "wasteshed" (locality) often dictates pricing. Owning the only dump in town also limits hefty tipping fees paid to other participants. Waste Management and Republic Services internalize—dispose of into their own company-owned landfills—more than 60% of collected waste, bolstering operating margins relative to privately-held, independent operators. Importantly, landfilling still represents the most prominent form of disposal, declining only 3 percentage points (as a percentage of generation) during the last decade. Materials recovery (including recycling) should continue its march upward, but the pace of this trend is far from tragic for the waste-hauling sector.

*No Disappointments...*continued on next page

No Disappointments...**from previous page**

Waste Management's and Republic Services' third-quarter pricing trends certainly didn't disappoint. The former put up core pricing expansion of 3.9%, while the latter posted an average yield increase of 1.3% for the period. Though these numbers may not seem aggressive, they are quite meaningful across the large revenue bases of the two garbage giants. The commentary of Waste Management's CEO David Steiner regarding ongoing pricing expansion was particularly encouraging:

"In the third quarter, collection and disposal yield was 2.3%, the fifth quarter of sequential improvement, and **nearly triple the yield** we saw in the third quarter of 2012."

Valuentum's Take

We're huge fundamental fans of the garbage hauling industry and hold Republic Services in the portfolio of our Best Ideas Newsletter. The structural characteristics of the garbage industry are among the strongest in our coverage universe given the value of landfill ownership.

Rio Tinto Says Iron Ore Production Breaks Record; Iron Ore Prices Recover

By Valuentum Analysts

Mining giant Rio Tinto (RIO) issued impressive third-quarter production results that revealed record production and shipments of Western Australia iron ore thanks to the opening of its Pilbara 290 port and rail expansion (ahead of schedule and significantly under budget). We think this good news has only been sweetened by the recent recovery in iron ore prices, following a near-term bottom in early June. It's important to note, however, that iron ore prices remain in a defined downtrend, and while we view the recent pricing performance as positive, we're not celebrating just yet.

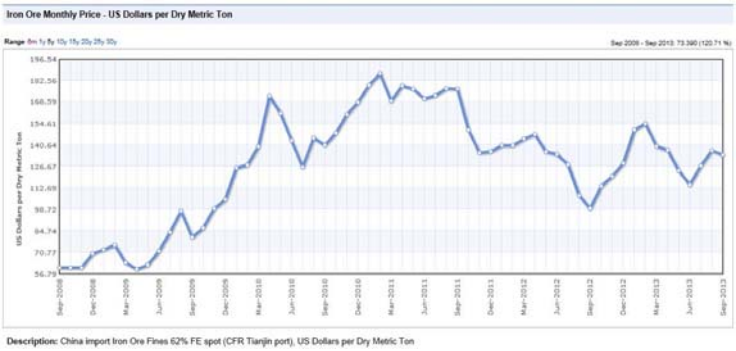

Image Source: http://www.indexmundi.com/commodities/?commodity=iron-ore&months=60

Still, fundamentals are starting to brighten up just a bit for the mining group. Economic performance in China is starting to improve, and the country's iron ore imports set a record in September at 74.6 million tons, up 8% from August and 15% on a year-over-year basis. Steel production in China has come in better than expected during the past couple months, and while we will enter into a seasonally-weaker period in the next few months, the recent performance has certainly been a pleasant surprise.

Valuentum's Take

Iron ore prices will continue to be volatile and the road ahead will be bumpy, but we think Rio Tinto has valuation upside beyond $60 per share on a base-case scenario. The firm also represents our only exposure to the basic materials sector in the portfolio of our Best Ideas Newsletter. We're not making any changes to the weighting of our position at this time.

Visa And MasterCard Gushing With Cash

By RJ Towner

Best Ideas Newsletter portfolio holding Visa (V) and its rival MasterCard (MA) reported results for their respective calendar third quarters.

Visa's top-line continues to expand, growing 8.8% year-over-year during its fiscal year 2013 fourth quarter to $2.9 billion, a tad shy of consensus estimates on nearly $1.1 trillion in gross dollar volume. The combination of the firm inking more major deals than usual (which increased incentives) and foreign exchange effects lowered reported revenue growth by 1.5 percentage points. Visa's net income per share jumped 20% year-over-year to $1.85, in-line with consensus estimates. For the fiscal year, earnings per share soared 23% year-over-year to $7.59. Free cash flow, adjusted for some timing issues related to the merchants opting out of the legal settlement with Visa and MasterCard (accrued litigation), was equal to $6.9 billion.

MasterCard's third quarter results were similarly strong thanks to a 16% year-over-year increase in revenue to $2.2 billion, which was slightly above consensus expectations (the firm had $1 trillion in gross dollar volume). Earnings per share followed suit, surging 18% year-over-year to $7.27, above consensus estimates. Year-to-date, MasterCard's free cash flow is terrific at $2.9 billion, equal to 46% of total revenue. Though eBay's PayPal (EBAY) and other smaller entrants have attempted to steal payment volume share, Visa and MasterCard remain unrivaled cash machines.

Guidance

Visa painted a rosy picture for fiscal year 2014, in our view. The company expects double-digit revenue growth, mid-to-high teens earnings-per-share expansion, and **free cash flow of $5 billion**. The firm marginally lowered its revenue target that it had issued at its investor day, but we think revenue could accelerate if a weak October turns out to just be an aberration. Visa's CFO Byron Pollitt noted:

"While October's first three weeks have upticked slightly to 9%, there has currently been some constraint in U.S. consumer spend, showing up in our numbers in both debit and credit. Our guidance encompasses what we are seeing in September and October and presumes that a tepid recovery in U.S. economic growth continues."

MasterCard, on the other hand, doesn't provide nearly as detailed guidance, though management commented that it anticipates the firm will meet its goal of compound annual revenue growth of 11-13% and diluted earnings per share growth of at least 20%.

Valuentum's Take

We were very pleased with the results from both Visa and MasterCard. Though we hold shares of Visa in the portfolio of our Best Ideas Newsletter, we do not envision adding to our position at present price levels.

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

The Curious Cases of Intuitive Surgical and Teva Pharma: What We Have Learned

By Brian Nelson, CFA

Within every portfolio, there will be a couple companies that do not live up to immediate expectations. Two such companies in our Best Ideas portfolio that haven't yet delivered on our theses are Intuitive Surgical (ISRG) and Teva Pharma (TEVA). We hold the Healthcare Select SPDR ETF (XLV) in the Best Ideas portfolio as well (it has been a top performer) and our healthcare picks—Johnson & Johnson (JNJ) and Medtronic (MDT)—have performed wonderfully in our Dividend Growth portfolio, but we're still waiting for our theses to be confirmed with respect to Intuitive Surgical and Teva Pharma.

Before we go any further, however, we think it is important to reiterate that the size of the weighting of a position in our actively-managed portfolios indicates the conviction we have in the idea. For example, our portfolio weightings in Intuitive Surgical and Teva Pharma are 1.7% and 1.9%, respectively. By comparison, our weightings in Apple (AAPL) and Ford (F), for example, are nearly 7%, suggesting we like the latter two ideas several times more than the former two ideas. **The size of the weighting in our actively-managed portfolios tells you just how confident we are in the idea relative to others.** With respect to Intuitive Surgical and Teva Pharma, new pieces of information came to light after we had established our position in each company.

Intuitive Surgical: Blindsided by ACOG President's Aggressive Comments

For Intuitive Surgical, it was the extreme negative publicity **mid-March** following a publication posted by American Congress of OB/GYN (ACOG) President James T. Breeden, MD. We were quite surprised with how passionate the president was **against** robotic surgery. We show the full publication below:

> "Many women today are hearing about the claimed advantages of robotic surgery for hysterectomy, thanks to widespread marketing and advertising. Robotic surgery is not the only or the best minimally invasive approach for hysterectomy. Nor is it the most cost-efficient. It is important to separate the marketing hype from the reality when considering the best surgical approach for hysterectomies.
>
> The outcome of any surgery is directly associated with the surgeon's skill. Highly skilled surgeons attain expertise through years of training and experience. Studies show there is a learning curve with new surgical technologies, during which there is an increased complication rate. Expertise with robotic hysterectomy is limited and varies widely among both hospitals and surgeons. While there may be some advantages to the use of robotics in complex hysterectomies, especially for cancer operations that require extensive surgery and removal of lymph nodes, studies have shown that adding this expensive technology for routine surgical care does not improve patient outcomes. Consequently, there is no good data proving that robotic hysterectomy is even as good as—let alone better—than existing, and far less costly, minimally invasive alternatives.
>
> Vaginal hysterectomy, performed through a small opening at the top of the vagina without any abdominal incisions, is the least invasive and least expensive option. Based on its well-documented advantages and low complication rates, this is the procedure of choice whenever technically feasible. When this approach is not possible, laparoscopic hysterectomy is the second least invasive and costly option for patients.
>
> Robotic hysterectomy generally provides women with a shorter hospitalization, less discomfort, and a faster return to full recovery compared with the traditional total abdominal hysterectomy (TAH) which requires a large incision. However, both vaginal and laparoscopic approaches also require fewer days of hospitalization and a far shorter recovery than TAH. These two established methods also have proven track records for outstanding patient outcomes and cost efficiencies.

*The Curious Cases…*continued on next page

*The Curious Cases…*from previous page.

> At a time when there is a demand for more fiscal responsibility and transparency in health care, the use of expensive medical technology should be questioned when less-costly alternatives provide equal or better patient outcomes. Hysterectomy is one of the most common major surgeries in the US and costs our health care system more than $5 billion a year.
>
> At a price of more than $1.7 million per robot, $125,000 in annual maintenance costs, and up to $2,000 per surgery for the cost of single-use instruments, robotic surgery is the most expensive approach. A recent Journal of the American Medical Association study found that the percentage of hysterectomies performed robotically has jumped from less than 0.5% to nearly 10% over the past three years. A study of over 264,000 hysterectomy patients in 441 hospitals also found that robotics added an average of $2,000 per procedure without any demonstrable benefit.
>
> If most women undergoing hysterectomy for benign conditions each year chose a vaginal or laparoscopic procedure—rather than TAH or robotic hysterectomy—performed by skilled and experienced surgeons, pain and recovery times would be reduced while providing dramatic savings to our health care system. Conversely, an estimated $960 million to $1.9 billion will be added to the health care system if robotic surgery is used for all hysterectomies each year.
>
> Aggressive direct-to-consumer marketing of the latest medical technologies may mislead the public into believing that they are the best choice. Our patients deserve and need factual information about all of their treatment options, including costs, so that they can make truly informed health care decisions. Patients should be advised that robotic hysterectomy is best used for unusual and complex clinical conditions in which improved outcomes over standard minimally invasive approaches have been demonstrated."

Frankly, we were blindsided. When someone of this industry authority presents a case against continued product adoption of robotic surgery, it will cause a hiccup in demand whether the comments are biased or not.

Our view is that President Breeden was speaking more to a constituency than as a medical professional with hard facts, indirectly flattering doctors at times: "the outcome of any surgery is directly associated with the surgeon's skill." We also picked up a 'resistance to change' disposition in his comments: "studies show there is a learning curve with new surgical technologies, during which there is an increased complication rate. Expertise with robotic hysterectomy is limited and varies widely among both hospitals and surgeons." Breeden's appeal to a constituency—where the majority may not yet be experts on robotic hysterectomy—lead us to believe that not all comments may be free from bias. A 'learning curve,' for example, should not be relevant as an impediment to a product's **long-term** adoption, if its efficacy is documented in many instances, as Breeden outlined:

> "while there may be some advantages to the use of robotics in complex hysterectomies, especially for cancer operations that require extensive surgery and removal of lymph nodes…; robotic hysterectomy generally provides women with a shorter hospitalization, less discomfort, and a faster return to full recovery compared with the traditional total abdominal hysterectomy (TAH) which requires a large incision…; patients should be advised that robotic hysterectomy is best used for unusual and complex clinical conditions in which improved outcomes over standard minimally invasive approaches have been demonstrated."

*The Curious Cases…*continued on next page

*The Curious Cases…*from previous page.

The slowdown in orders for the *da Vinci* has certainly materialized since President Breeden's publication, but we think there's enough positive substance in the president's comments that suggests robotic surgery still has a long runway of future growth. With Intuitive Surgical pumping more and more money into research and development (it invested $170 million in 2012), we think it is just a matter of time before the firm is able to make the cost decision a very easy one for hospitals.

Though unlikely given the tone of the publication, it's possible that President Breeden was simply calling on Intuitive Surgical to become more efficient (and using his constituency to enact change). For one, we do find it quite unusual that the idea of making robotic surgery less expensive wasn't even mentioned. The publication simply tried to counter the adoption of robotic surgery, without even acknowledging the ability of Intuitive Surgical to use pricing to attract more placements (and lower the cost equation for hospitals).

Investors should continue to expect a highly-volatile stock and a flurry of contradictory information with respect to Intuitive Surgical's products in coming weeks, months, and years. However, it is our view that robotic surgery is here to stay, and the potential for Intuitive Surgical to make in-roads into other robotic surgery applications is an open-ended opportunity not appropriately captured in its market price. The recent slowdown in *da Vinci* orders may just be the catalyst that creates another breakthrough product at the firm.

Takeaway: It's likely that investors may see Intuitive Surgical's shares at $200 before they hit $600 again, but the long-term is still bright. Shares are down about 20% from our cost basis.

Teva: Copaxone Disappointment; Management Controversy

The fundamental path of Teva was equally surprising.

Shortly after we established a position, the hurdles with respect to its multiple-sclerosis drug Copaxone (which accounts for roughly half of profits) became even greater:

> "The U.S Federal Court of Appeals confirmed validity of select COPAXONE patents through May 2014, but not others including one patent expiring September 2015. We are disappointed with this part of the Appeals Court decision and we will appeal that decision. I want to remind you that COPAXONE is a complex synthetic peptide. We believe that a purported generic version would need full scale, placebo-controlled clinical trials in RRMS patients. As a consequence, we are not sure of a generic timing or approval. In addition to appealing the court's decision, this company has been preparing for the potential launch of the generic COPAXONE. In May 2013, the U.S. FDA accepted our submission for a more convenient schedule of three times weekly dosing of COPAXONE, 40 milligrams per meal. We anticipate FDA actions in the first quarter of 2014, and if approved we are prepared with an aggressive launch strategy for the first half of 2014."

The patent expiration of its current large profit-driver Capaxone in May 2014 is roughly a full year earlier than what we had been expecting prior to initiating our position in the firm in our Best Ideas portfolio.

Then, we were blindsided again. CEO Jeremy Levin stepped down as CEO – the day before the firm released third-quarter results. Certainly, this management change was not anticipated, and while the firm's quarterly performance wasn't bad, the abrupt exit by CEO Levin does bring into question the firm's long-term strategy.

Still, Teva's global generic opportunity is arguably the best within our coverage universe, and we're excited about its NTE pipeline, which we're expecting to be a multi-billion dollar revenue stream in coming years. The company is uniquely-positioned to capture the NTE opportunity because of the firm's ability to combine its generic and branded-drug expertise across indications.

*The Curious Cases…*continued on next page

*The Curious Cases…*from previous page.

Investors should fully expect the next 12-24 months to be difficult for the company with respect to year-over-year comparisons, but we still feel comfortable holding shares in the portfolio of our Best Ideas Newsletter. The long-term opportunity for lower-cost generics in an environment where governments across the globe are looking to cut expenses and become more efficient is just too great to pass up, in our view.

Takeaway: Losing close to half of its profits in coming years as a result of losing exclusivity on Copaxone will translate into some tough sledding for Teva Pharma investors. However, we still believe the long-term is bright.

Valuentum's Take: What We've Learned

With respect to Intuitive Surgical, we became so enamored with the long-term prospects of robotic surgery that we were just too flexible with our entry point. The firm's Valuentum Buying Index rating was a 5 when it entered our Best Ideas portfolio. **We intend to better follow our own methodology** and don't intend to make a leap just to gain exposure to a long-term story without substantial VBI support first. This is a process error on our part.

With respect to Teva Pharma, the appeal of the long term was a contributing factor, too. Though we added the firm to the portfolio with a VBI rating of 6, Teva has registered a 9 in the past. Interestingly, **we think Teva Pharma is an example of the strength of our methodology**. In a situation where the firm will lose more than half of profits in coming years and where a controversial and unexpected change in the executive suite occurred, shares are down a meager 8%. We believe Teva highlights the positive risk/reward profile of firms that register a 9 or 10 on the VBI. When things go unexpectedly and incredibly wrong, stocks with VBI ratings of 9 and 10 remain very resilient.

Surveying Valuentum Buying Index Performance In The Restaurant Space

By Valuentum Analysts

The stock-selection methodology, the Valuentum Buying Index, is as simple as an efficacious stock-selection methodology can be. However, that doesn't mean that the Valuentum Buying Index is simple. The Valuentum Buying Index considers the rigors of a discounted cash-flow process, the considerations of relative valuation techniques, and the transparency of pricing information via market indicators.

Yet despite its straightforwardness, the Valuentum Buying Index casts a discerning eye on the equities it monitors. The Valuentum Buying Index does not make a 'call' on every company. It only views a 9 or a 10 on the measure to be actionable on the long side, and it only views a 1 or 2 on the measure to be actionable on the short side. And only the best ideas included in the Best Ideas portfolio and Dividend Growth portfolio can be considered our best ideas at any given time. The Valuentum Buying Index's breadth may be unmatched, and its sorting mechanism may be unrivaled by any other methodology.

*Surveying Valuentum Buying Index Performance…*continued on next page

Surveying Valuentum Buying Index Performance…**from previous page**

Within the restaurant industry, long ideas highlighted by the Valuentum Buying Index and/or included in our Best Ideas portfolio averaged a 118.6% return over the measurement period (1), while short ideas registered 58.5 percentage points of underperformance relative to the average restaurant return (2). The Valuentum Buying Index identified 2 out of the top 4 best performers—Buffalo Wild Wings (BWLD) and Cracker Barrel (CBRL)—as long ideas and the worst performer as a short idea—BJ's Restaurants (BJRI). Though there is always room for better performance, we applaud the Valuentum Buying Index for its high marks in the restaurant industry.

(1) The performance of long Best Ideas portfolio holdings is measured by comparing the price at the date they were added to the portfolio to the price of the date that they were removed. If they are still holdings, the current price is applied. The performance of firms that register a 9 or 10 on the Valuentum Buying Index and were not included in the Best Ideas portfolio is measured by comparing the price at the date they registered a 9 or a 10 to the price of the date they registered a 1 or a 2. If they have not registered a 1 or 2 after registering a 9 or 10, the current price is applied. A simple average of the performance of portfolio holdings and firms registering a 9 or 10 on the Valuentum Buying Index results in a 118.6% return.

(2) The performance of firms that register a 1 or 2 on the Valuentum Buying Index and were not included in the Best Ideas portfolio is measured by comparing the price at the date they registered a 1 or a 2 to the price of the date they registered a 9 or a 10. If they have not registered a 9 or 10 after registering a 1 or 2, the current price is applied. A simple average of the performance of short portfolio holdings and firms registering a 1 or 2 on the Valuentum Buying Index results in a 4.5% return. The average restaurant return is measured from July 13, 2011 to present. The start date was chosen to match the date Best Ideas portfolio holding Buffalo Wild Wings was added to the portfolio. The average restaurant return over this time period was 63%. 4.5% less 63% equals 58.5%.

Historical Valuentum Buying Index information for each company is included on page 16 of each respective report.

= Best Ideas Portfolio Holding
= Valuentum Buying Index (9, 10)
= Valuentum Buying Index (1, 2)

Company Name	Price, as of July 13, 2011	Price, as of November 11, 2013	Percentage Gain*	Actionable VBI Rating	Long Ideas	Short Ideas
Domino's Pizza (DPZ)	23.77	66.70	180.6%	Not Actionable		
Papa John's (PZZA)	31.68	75.96	139.8%	Not Actionable		
Cracker Barrel (CBRL)	46.30	110.21	138.0%	**VBI: 9 (December 2, 2011), actionable price $48.70**	**126.3%**	
Buffalo Wild Wings (BWLD)	67.83	143.07	110.9%	Added to Best Ideas Portfolio (July 13, 2011)	110.9%	
Red Robin (RRGB)	37.65	79.30	110.6%	Not Actionable		
Starbucks (SBUX)	38.33	79.07	106.3%	Not Actionable		
Famous Dave's (DAVE)	11.01	20.05	82.1%	VBI: 2 (July 5, 2013), actionable price $15.41		30.1%
Brinker (EAT)	24.87	44.78	80.1%	Not Actionable		
Jack in the Box (JACK)	23.74	41.58	75.1%	Not Actionable		
Sonic Corp (SONC)	10.75	18.73	74.2%	Not Actionable		
Chipotle (CMG)	325.18	525.02	61.5%	VBI: 2 (April 20, 2012), actionable price $419.26		25.2%
Bob Evans (BOBE)	33.54	53.32	59.0%	Not Actionable		
Denny's (DENN)	4.10	6.50	58.5%	Not Actionable		
Texas Roadhouse (TXRH)	17.35	27.39	57.9%	Not Actionable		
Wendy's (WEN)	5.12	8.05	57.2%	Not Actionable		
DineEquity (DIN)	52.69	80.47	52.7%	Not Actionable		
Cheesecake Factory (CAKE)	32.76	47.39	44.7%	Not Actionable		
Yum! Brands (YUM)	53.19	69.80	31.2%	Not Actionable		
Tim Hortons (THI)	46.71	60.01	28.5%	Not Actionable		
Panera (PNRA)	131.75	167.00	26.8%	Not Actionable		
McDonald's (MCD)	79.24	97.20	22.7%	Not Actionable		
Darden Restaurants (DRI)	48.20	52.14	8.2%	Not Actionable		
Arcos Dorados (ARCO)	20.51	11.37	-44.6%	Not Actionable		
BJ's Restaurants (BJRI)	55.51	27.21	-51.0%	**VBI: 1 (April 20, 2012), actionable price $46.80**		**-41.9%**
Average Return			63.0%		**118.6%**	4.5%

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
USG Corp	USG	UNDERVALUED	ATTRACTIVE	0.60
Baidu	BIDU	UNDERVALUED	ATTRACTIVE	0.62
Huntsman	HUN	UNDERVALUED	ATTRACTIVE	0.63
Broadcom	BRCM	UNDERVALUED	ATTRACTIVE	0.65
Nabors Industries	NBR	UNDERVALUED	ATTRACTIVE	0.67
Riverbed Technology	RVBD	UNDERVALUED	ATTRACTIVE	0.68
Realty Income Corp	O	UNDERVALUED	ATTRACTIVE	0.68
eBay	EBAY	UNDERVALUED	ATTRACTIVE	0.71
Verint	VRNT	UNDERVALUED	ATTRACTIVE	0.71
Deluxe	DLX	UNDERVALUED	ATTRACTIVE	0.72
Johnson Outdoors Inc	JOUT	UNDERVALUED	ATTRACTIVE	0.72
Tyson Foods	TSN	UNDERVALUED	ATTRACTIVE	0.75
DIRECTV	DTV	UNDERVALUED	ATTRACTIVE	0.77
NASDAQ	NDAQ	UNDERVALUED	ATTRACTIVE	0.78
AIG	AIG	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
eBay	EBAY	Consumer Discretionary	Internet & Catalog Retail	10
AIG	AIG	Financials	Insurance - Property & Casualty	9
Deluxe	DLX	Information Technology	Staffing Services	9
NASDAQ	NDAQ	Financials	Exchanges	9
USG Corp	USG	Industrials	Building Materials	9

Name	Symbol	Sector	Industry	VBI
Badger Meter	BMI	Industrials	Electrical Equipment	1
Brown-Forman	BF.B	Consumer Staples	Beverages - alcoholic	1
China Life	LFC	Financials	Insurance - Life	1
Cooper Co	COO	Health Care	Medical Instruments	1
Heartland	HTLD	Industrials	Air Freight & Logistics	1
J&J Snack	JJSF	Consumer Staples	Food Products	1
J.C. Penney	JCP	Consumer Discretionary	Multiline Retail	1
Lancaster Colony	LANC	Consumer Staples	Food Products	1
McGrath	MGRC	Industrials	Rental and Leasing	1
Northern Trust	NTRS	Financials	Banks & Money Centers	1
Pool Corp	POOL	Consumer Discretionary	Sporting Goods	1
Public Storage	PSA	Industrials	Rental and Leasing	1
TCF Financial	TCB	Financials	Banks & Money Centers	1
Vertex Pharma	VRTX	Health Care	Pharmaceuticals	1
Annie's Inc	BNNY	Consumer Staples	Food Products	2
Boston Beer	SAM	Consumer Staples	Beverages - alcoholic	2
CIRCOR Intl	CIR	Industrials	Electrical Equipment	2
Famous Dave's	DAVE	Consumer Discretionary	Restaurants	2
GameStop	GME	Consumer Discretionary	Specialty Retailers	2
HEICO	HEI	Industrials	A&D Suppliers	2
Infinity	IPCC	Financials	Insurance - Property & Casualty	2
Regeneron	REGN	Health Care	Biotechnology	2
Selective Insurance	SIGI	Financials	Insurance - Property & Casualty	2
Sun Life	SLF	Financials	Insurance - Life	2
The Allstate Corp	ALL	Financials	Insurance - Property & Casualty	2
United Natural	UNFI	Consumer Staples	Food Retailers	2
Washington Post	WPO	Consumer Discretionary	Media - newspapers	2

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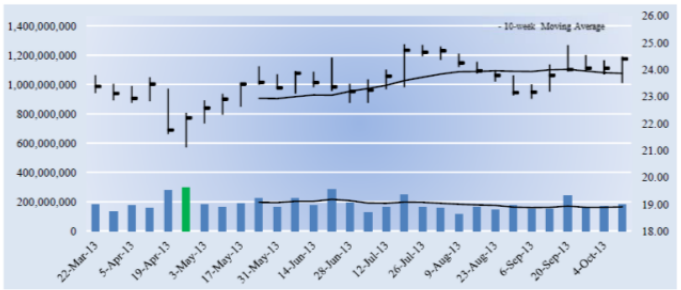
General Electric GE FAIRLY VALUED

Buying Index™ 7 **Value Rating**

Last Close	Estimated Fair Value	Fair Value Range	Investment Style	Sector	Industry
$24.40	$28.00	$22.00 - $34.00	MEGA-CAP VALUE	Industrials	Conglomerates

General Electric has paid an amazing ~$150 billion in dividends since 1970.

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	FAIRLY VALUED
Relative Valuation	ATTRACTIVE
ValueCreation™	EXCELLENT
ValueRisk™	LOW
ValueTrend™	POSITIVE
Cash Flow Generation	STRONG
Financial Leverage	HIGH
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

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)	$257,762
Avg Weekly Vol (30 wks)	183,177
30-week Range (USD)	21.11 - 24.95
Valuentum Sector	Industrials
5-week Return	4.9%
13-week Return	2.8%
30-week Return	5.3%
Dividend Yield %	3.1%
Dividends per Share	0.76
Forward Dividend Payout Ratio	45.3%
Est. Normal Diluted EPS	2.09
P/E on Est. Normal Diluted EPS	11.7
Est. Normal EBITDA	47,912
Forward EV/EBITDA	11.7
EV/Est. Normal EBITDA	10.4
Forward Revenue Growth (5-yr)	1.8%
Forward EPS Growth (5-yr)	13.0%

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

Investment Highlights

• General Electric'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.

• GE is one of the largest and most diversified industrial and financial firms in the world--with products and services ranging from aircraft engines, power generation, water processing, and household appliances to medical imaging, business and consumer financing and industrial products.

• GE has strong liquidity, a large backlog, and major cost programs underway to deal with anything the economic environment has to throw at it. The firm has a balanced capital allocation strategy with significant cash returned to shareholders in recent years. Emerging market growth and infrastructure investments are key sources of expansion.

• 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.

• GE boasts a very nice dividend yield, and its Dividend Cushion score is solid. The firm has paid an amazing ~$150 billion in dividends since 1970.

Relative Valuation

	Forward P/E	PEG	Price / FV
3M	17.7	2.7	113.4%
Honeywell	16.7	1.9	108.5%
Tyco Intl	18.9	NMF	97.1%
United Technologies	17.6	1.6	113.9%
Peer Median	17.7	1.9	111.0%
General Electric	**14.6**	**1.4**	**87.1%**

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

Returns Summary

	3-year Historical Average
Return on Equity	11.9%
Return on Assets	3.3%
ROIC, with goodwill	28.2%
ROIC, without goodwill	61.8%

ROIC = Return on Invested Capital; NMF = Not Meaningful

Financial Summary

	----- Actual -----		Projected
Fiscal Year End:	Dec-11	Dec-12	Dec-13
Revenue	147,300	147,359	145,885
Revenue, YoY%	-1.9%	0.0%	-1.0%
Operating Income	34,643	29,914	33,347
Operating Margin %	23.5%	20.3%	22.9%
Net Income	14,074	14,679	17,618
Net Income Margin %	9.6%	10.0%	12.1%
Diluted EPS	1.33	1.39	1.68
Diluted EPS, YoY %	12.1%	4.9%	20.7%
Free Cash Flow (CFO-capex)	20,709	17,243	13,428
Free Cash Flow Margin %	14.1%	11.7%	9.2%

In Millions of USD (except for per share items)

Leverage, Coverage, and Liquidity

In Millions of USD

Total Debt	367,599
Net Debt	241,733
Total Debt/EBITDA	9.4
Net Debt/EBITDA	6.2
EBITDA/Interest	3.1
Current Ratio	0.6
Quick Ratio	0.6

NMF = Not Meaningful

Structure of the Conglomerates Industry — GOOD

The industrial conglomerate industry is characterized by firms that operate various business lines on a global scale. Demand for industrial products tends to be cyclical in nature, and most firms couple their manufacturing operations with generally more stable services businesses to mitigate fundamental volatility. Firms tend to have bargaining power over suppliers due to industry dominance and boast substantial resources to adapt to changing conditions or competitive threats. Most sell products under powerful and recognizable brand names and look to emerging markets for future growth. We like the group.

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Page 1

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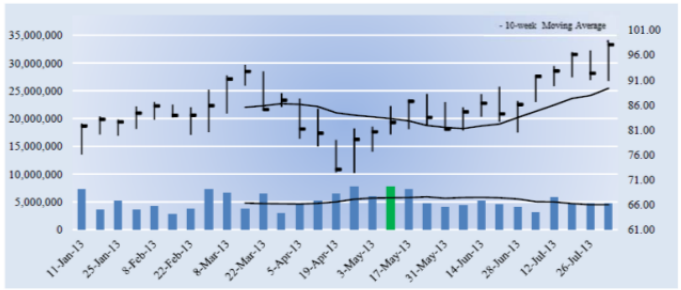
Continental Resources CLR UNDERVALUED 13.2%

Buying Index™ 7 — Value Rating ✓

Last Close	Estimated Fair Value	Fair Value Range	Investment Style	Sector	Industry
$98.07	$148.00	$111.00 - $185.00	LARGE-CAP BLEND	Energy	Independent Oil & Gas

We like Continental Resource's position in the Bakken and view it as an acquisition target.

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	NEUTRAL
ValueCreation™	EXCELLENT
ValueRisk™	MEDIUM
ValueTrend™	POSITIVE
Cash Flow Generation	WEAK
Financial Leverage	MEDIUM
Growth	AGGRESSIVE
Technical Evaluation	BULLISH
Relative Strength	STRONG
Money Flow Index (MFI)	NEUTRAL
Upside/Downside Volume (U/D)	BULLISH
Near-term Technical Support, 10-week MA	89.00

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)	$17,479
Avg Weekly Vol (30 wks)	5,050
30-week Range (USD)	72.35 - 99.01
Valuentum Sector	Energy
5-week Return	13.1%
13-week Return	21.7%
30-week Return	28.0%
Dividend Yield %	0.0%
Dividends per Share	0.00
Forward Dividend Payout Ratio	0.0%
Est. Normal Diluted EPS	6.44
P/E on Est. Normal Diluted EPS	15.2
Est. Normal EBITDA	3,016
Forward EV/EBITDA	11.7
EV/Est. Normal EBITDA	6.2
Forward Revenue Growth (5-yr)	28.7%
Forward EPS Growth (5-yr)	29.6%

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

Investment Highlights

• Continental Resources 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. We expect the firm's return on invested capital (excluding goodwill) to expand to 23.2% from 18.5% during the next two years.

• Continental Resources is an independent crude oil and natural gas exploration and production company with properties in the North, South and East regions of the US, including the Bakken and Red River units.

• Continental Resources' cash flow generation is below what we'd expect from an average company in our coverage universe, and the firm's financial leverage is somewhat elevated. If cash flows continue to be weak, we'd grow more cautious on the firm's overall financial health.

• The firm remains focused on crude oil (as opposed to natural gas). More than 70% of its total proved reserves are of the black-liquid variety. We like the company's position in the Bakken and view it as an acquisition target.

• At year-end 2012, the company had more than 785 MMBoe of proved reserves, a 54% year-over-year gain. The company boasts strong EBITDAX and cash margins.

Relative Valuation

	Forward P/E	PEG	Price / FV
Anadarko	25.7	NMF	91.4%
Apache	8.6	NMF	92.1%
Devon Energy	17.2	0.7	93.3%
Occidental Petroleum	12.5	2.7	97.7%
Peer Median	14.8	1.7	92.7%
Continental Resources	**29.2**	**1.4**	**66.3%**

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

Returns Summary

	3-year Historical Average
Return on Equity	15.5%
Return on Assets	6.0%
ROIC, with goodwill	17.4%
ROIC, without goodwill	17.4%

ROIC = Return on Invested Capital; NMF = Not Meaningful

Leverage, Coverage, and Liquidity

In Millions of USD

Total Debt	1,254
Net Debt	1,201
Total Debt/EBITDA	1.0
Net Debt/EBITDA	0.9
EBITDA/Interest	16.6
Current Ratio	0.8
Quick Ratio	0.7

NMF = Not Meaningful

Financial Summary

	----- Actual -----		Projected
Fiscal Year End:	Dec-10	Dec-11	Dec-12
Revenue	839	1,650	2,380
Revenue, YoY%	34.0%	96.6%	44.3%
Operating Income	476	878	1,030
Operating Margin %	56.8%	53.2%	43.3%
Net Income	168	429	611
Net Income Margin %	20.1%	26.0%	25.7%
Diluted EPS	0.99	2.41	3.36
Diluted EPS, YoY %	135.5%	142.9%	39.7%
Free Cash Flow (CFO-capex)	-278	137	272
Free Cash Flow Margin %	-33.1%	8.3%	11.4%

In Millions of USD (except for per share items)

Structure of the Independent Oil & Gas Industry — POOR

The oil and gas business is highly competitive in the exploration, acquisition, and production of reserves. Changes in deepwater drilling laws and other regulatory initiatives can add uncertainty to operations. The trajectory of global economic growth, the actions of OPEC, and political and environmental uncertainty are other key factors. A strong balance sheet to manage through the commodity price cycle is necessary for survival. With the group's profitability largely driven by the volatile prices of oil, natural-gas and NGLs, we're not that excited about the structure of this commodity-producing space.

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Page 1

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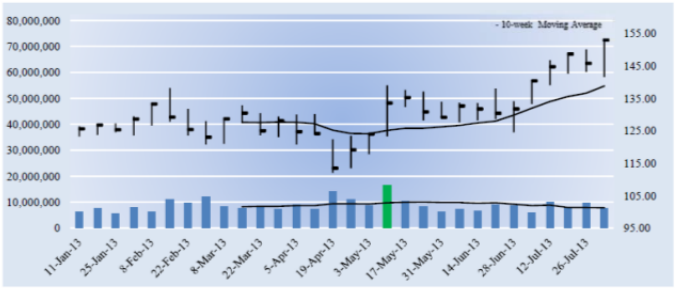
EOG Resources EOG FAIRLY VALUED

Buying Index™ 6 **Value Rating**

Last Close	Estimated Fair Value	Fair Value Range	Investment Style	Sector	Industry
$153.03	$196.00	$127.00 - $265.00	LARGE-CAP BLEND	Energy	Independent Oil & Gas

EOG Resources is the largest crude oil producer in the South Texas Eagle Ford Shale and North Dakota Bakken, which should drive significant reserve and production growth.

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	FAIRLY VALUED
Relative Valuation	NEUTRAL
ValueCreation™	POOR
ValueRisk™	HIGH
ValueTrend™	POSITIVE
Cash Flow Generation	WEAK
Financial Leverage	LOW
Growth	AGGRESSIVE
Technical Evaluation	BULLISH
Relative Strength	STRONG
Money Flow Index (MFI)	NEUTRAL
Upside/Downside Volume (U/D)	BULLISH
Near-term Technical Support, 10-week MA	139.00

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)	$40,747
Avg Weekly Vol (30 wks)	8,682
30-week Range (USD)	112.05 - 153.21
Valuentum Sector	Energy
5-week Return	14.4%
13-week Return	22.8%
30-week Return	22.2%
Dividend Yield %	0.5%
Dividends per Share	0.75
Forward Dividend Payout Ratio	13.2%
Est. Normal Diluted EPS	9.22
P/E on Est. Normal Diluted EPS	16.6
Est. Normal EBITDA	8,595
Forward EV/EBITDA	8.2
EV/Est. Normal EBITDA	5.3
Forward Revenue Growth (5-yr)	17.8%
Forward EPS Growth (5-yr)	25.6%

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

Investment Highlights

• EOG Resources' average return on invested capital has trailed its cost of capital during the past few years, indicating weakness in business fundamentals and an inability to earn economic profits through the course of the economic cycle. We think there are better quality firms out there.

• EOG operates primarily in the US, Canada, Trinidad, UK, China, and Argentina. The firm is the largest crude oil producer in the South Texas Eagle Ford Shale and North Dakota Bakken, which should drive significant reserve and production growth.

• EOG Resources' cash flow generation and financial leverage aren't much to speak of. The firm's free cash flow margin has averaged about -27.6% during the past three years, much lower than the mid-single-digit range we'd expect for cash cows. Total debt-to-EBITDA was 0.9 last year, while debt-to-book capitalization stood at 28.4%.

• Although we think there may be a better time to dabble in the firm's shares based on our DCF process, the firm's stock has outperformed the market benchmark during the past quarter, indicating increased investor interest in the company.

• We're expecting some pretty impressive production growth at EOG in coming years. During the past seven years, for example, the company posted a 38% compound annual growth rate in production.

Relative Valuation

	Forward P/E	PEG	Price / FV
Anadarko	25.7	NMF	91.4%
Apache	8.6	NMF	92.1%
Devon Energy	17.2	0.7	93.3%
Occidental Petroleum	12.5	2.7	97.7%
Peer Median	14.8	1.7	92.7%
EOG Resources	**27.0**	**1.5**	**78.1%**

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

Returns Summary

	3-year Historical Average
Return on Equity	5.6%
Return on Assets	2.9%
ROIC, with goodwill	10.5%
ROIC, without goodwill	10.5%

ROIC = Return on Invested Capital; NMF = Not Meaningful

Leverage, Coverage, and Liquidity

In Millions of USD

Total Debt	5,009
Net Debt	4,393
Total Debt/EBITDA	0.9
Net Debt/EBITDA	0.8
EBITDA/Interest	26.9
Current Ratio	1.3
Quick Ratio	0.8

NMF = Not Meaningful

Financial Summary

	----- Actual -----		Projected
Fiscal Year End:	Dec-10	Dec-11	Dec-12
Revenue	6,100	10,126	11,680
Revenue, YoY%	27.4%	66.0%	15.4%
Operating Income	1,266	3,144	2,578
Operating Margin %	20.8%	31.1%	22.1%
Net Income	161	1,091	1,539
Net Income Margin %	2.6%	10.8%	13.2%
Diluted EPS	0.63	4.10	5.67
Diluted EPS, YoY %	-70.9%	549.2%	38.3%
Free Cash Flow (CFO-capex)	-2,873	-2,372	1,193
Free Cash Flow Margin %	-47.1%	-23.4%	10.2%

In Millions of USD (except for per share items)

Structure of the Independent Oil & Gas Industry — POOR

The oil and gas business is highly competitive in the exploration, acquisition, and production of reserves. Changes in deepwater drilling laws and other regulatory initiatives can add uncertainty to operations. The trajectory of global economic growth, the actions of OPEC, and political and environmental uncertainty are other key factors. A strong balance sheet to manage through the commodity price cycle is necessary for survival. With the group's profitability largely driven by the volatile prices of oil, natural-gas and NGLs, we're not that excited about the structure of this commodity-producing space.

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Page 1

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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**

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.

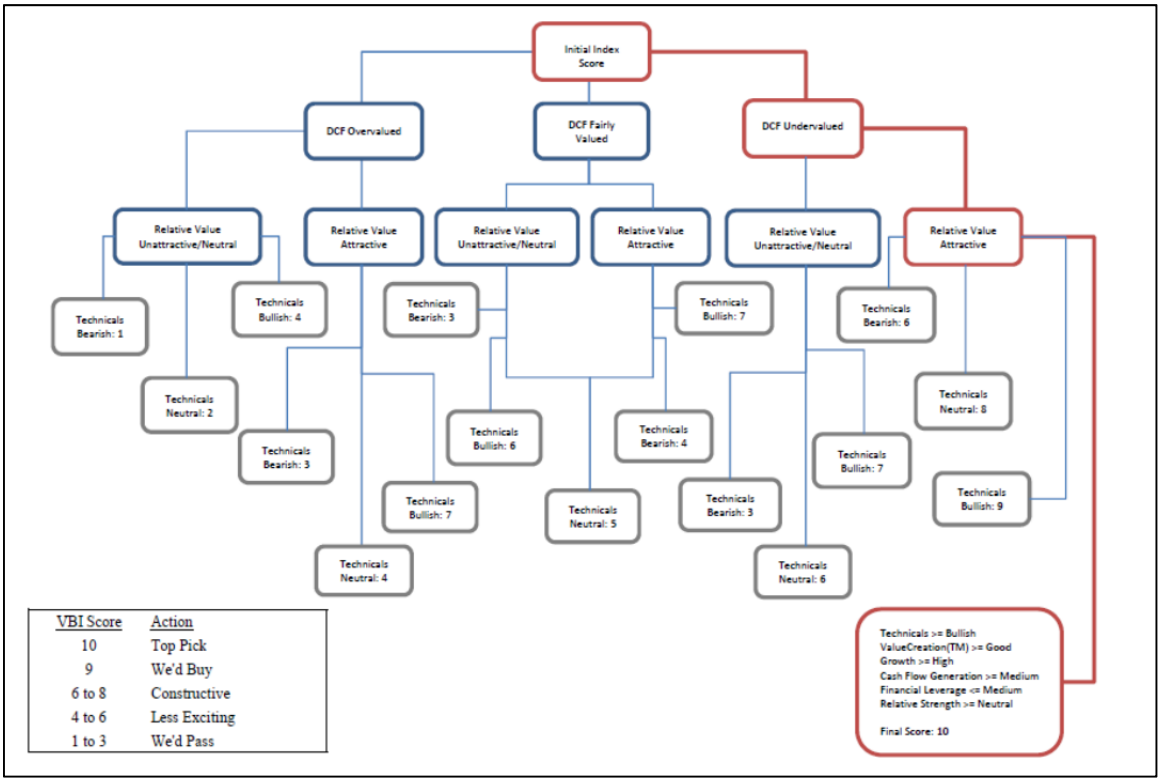
Avoiding Value Traps and Opportunity Cost

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 11

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