OUR BEST IDEAS NEWSLETTER

Valuentum Securities

Stock Analysis: From Value through Momentum Investing

February 15, 2017
Volume 7 Issue 2

Valuentum Securities Inc.
www.valuentum.com info@valuentum.com

Portfolio Return	Benchmark Return	Outperformance
124.0%	92.9%	31.1pts

See page 8.

The Best Ideas Portfolio (see page 8): AAPL, MO, BWLD, BRK-B, CSCO, CVS, FB, XLF, GE, GM, GOOG, GOOGL, XLV, INTC, JNJ, KBE, KMI, KORS, PYPL, PCLN, RSG, SDY, TEVA, UNP, XLE, XLU, V

Inside This Issue

Goals of the Best Ideas Newsletter: We want to deliver positive returns, year after year, in addition to outperforming the market benchmark. We may not always be successful, however. Our Best Ideas portfolio is generally found on page 8 of each edition.

"Each individual company report and dividend report on the website contains a wealth of analytical information, including the company's fair value estimate, fair value range, Valuentum Buying Index rating, Dividend Cushion ratio, among other items."
- Brian Nelson, CFA

Brian Nelson, CFA
President, Equity Research
brian@valuentum.com

Kris Rosemann
Associate Investment Analyst
kris@valuentum.com

= ALL TIME HIGH

KEY CONCEPT: Stocks in the Best Ideas portfolio (see page 8), which have generally registered a 9 or 10 on the VBI when added, should be considered our best ideas at any point in time. After adding firms to the Best Ideas portfolio, we may tactically trade around these positions when they have VBI ratings between 3 and 8 depending on the size of their weighting in the portfolio or the attractiveness of them relative to other opportunities (a score of 3 through 8 is equivalent to a 'we'd hold'). We tend to remove firms from the Best Ideas portfolio when they register a 1 or 2 ("we'd sell"). Contact us for more details about how the team utilizes the Valuentum Buying Index to run the portfolio.

Why Portfolio Holdings Can Sometimes Have Low VBI Ratings

By Brian Nelson, CFA

Q: Most of the stocks in the Best Ideas Newsletter portfolio carry a Valuentum Buying Index rating of 6 or lower. Why?

A: This is a great question because it gives us the opportunity to explain the robustness and multi-faceted dynamics of the Valuentum Buying Index methodology. First, the Valuentum Buying Index, or the VBI, breaks down into three in-depth, standalone processes: a discounted cash-flow process, a relative value process, and a technical/momentum assessment. Each of these three pillars of the Valuentum Buying Index contain analytical insight contributing to the overall investment consideration beyond a one integer system. The combination of these three criteria results in each firm's Valuentum Buying Index rating (from 1 through 10, with 10 being the best).

To get a feel for how much work goes into just one pillar of the process, for example, here's a short video on our discounted cash-flow process:

http://www.valuentum.com/categories/20110615

Each individual company report and dividend report on the website contains a wealth of analytical information, including the company's fair value estimate, fair value range, Valuentum Buying Index rating, Dividend Cushion ratio, among other items. Our team at Valuentum uses the exact reports that our members do as we manage the two newsletter portfolios.

We use the Valuentum Buying Index, housed in each firm's 16-page report, as a source of idea generation. Typically, we consider adding firms to the Best Ideas Newsletter portfolio and Dividend Growth Newsletter portfolio when shares register a 9 or 10 on the Valuentum Buying Index and generally hold them until they register a 1 or 2 on the Valuentum Buying Index. We do not add every company that registers a high Valuentum Buying Index rating to the newsletter portfolios, however.

Similar in thinking as if you were to imagine a value investor not adding every undervalued stock to his/her portfolio, we have a qualitative overlay, too. There are always tactical and sector weighting considerations in any portfolio

Why Portfolio Holdings...continued on next page

*Why Portfolio Holdings…*from previous page

Image Source: Andrew Steele

construction, for one, but whereas studies suggest high-VBI-rated entities outperform low-VBI-rated entities across large sample sizes, the Best Ideas Newsletter portfolio and Dividend Growth Newsletter portfolio are much more concentrated. Any idea added to the portfolios must pass muster with the Valuentum Team.

Once a company is added, at certain times during the holding period, stocks in the newsletter portfolios may register lower VBI ratings than companies outside of the portfolios. This can be confusing at times, but a lower VBI rating for a newsletter holding generally showcases something very good. In most cases, it means that shares of the company held in the portfolio have advanced to the fair value estimate, which is driving the lower VBI rating compared to the one when it was added.

If the ratings of non-holdings are higher than those of newsletter portfolio holdings, but have not crossed the threshold of a 9 or 10 (the equivalent of a "we'd consider buying" rating), they have not met the criteria for consideration. Those that do still have to "fit" in the portfolio in the context of tactical or sector weighting considerations. If they don't, they're not added.

We frequently say that our best ideas at any given time are always included in the portfolio of our Best Ideas Newsletter, and our best dividend growth ideas at any given time are always included in the portfolio of the Dividend Growth Newsletter. These are the companies that 1) have triggered the "consider buying" signal (a 9 or 10 on the Valuentum Buying Index) and 2) have received the thumbs-up from our team, while others have not.

The goals of the two newsletter portfolios are as follows (on next page):

Why Portfolio Holdings …continued on next page

*Intro…*from previous page

> The Best Ideas portfolio seeks to find firms that have good value and good momentum characteristics and typically holds each idea from a Valuentum Buying Index rating of a 9 or 10 (consider buying) to a rating of a 1 or 2 (consider selling). Just like a value manager may not include every single undervalued company in the market in his/her portfolio, not all highly-rated companies on the Valuentum Buying Index are included in the portfolio. We may tactically add to or trim existing positions in the portfolio on the basis of sector or broader market considerations, but we seek to capture a stock's entire pricing cycle (from being underpriced with strong momentum to being overpriced with poor momentum). The goal of the Best Ideas portfolio is to generate a positive return each year and to exceed the performance of a broad market benchmark. We won't always be successful, however.

> The Dividend Growth portfolio seeks to find underpriced dividend growth gems that generate phenomenal levels of cash flow and have pristine, fortress balance sheets, translating into excellent Valuentum Dividend Cushion ratios. Firms in the portfolio may have lengthy dividend growth track records, but we focus most of our efforts on assessing the future safety and dividend growth potential of holdings. The goal of the Dividend Growth portfolio is to generate a mid-to-high single digit annual return over rolling three-to-five year periods. Though we apply our best efforts, we may come up short sometimes. That said, we have yet to have a Dividend Growth portfolio holding cut its dividend, and we credit this to the Valuentum Dividend Cushion methodology.

That said, we continue to be flexible when it comes to striving to meet goals of the newsletter portfolios, and we may look to add certain exposure to companies that may not have the highest ratings in our coverage. For example, a deeply-undervalued company with a solid and fast-growing dividend may make the cut for inclusion into the Dividend Growth Newsletter portfolio, even if its Valuentum Buying Index rating may only be a 6, for example. Alternatively, if we're lacking preferred industry exposure (e.g. restaurants), we may add an undervalued restaurant to the Best Ideas Newsletter portfolio, even if its Valuentum Buying Index may only be a 7 on the scale.

No matter what we do, however, we try to be as transparent as possible. There should be no surprises when it comes to the ideas we surface.

Gilead Sciences Continues Its Meltdown

Valuentum has been out of Gilead in the newsletter portfolios for some time. As the Best Ideas Newsletter portfolio continues to make new highs, Gilead continues to set new 52-week lows. This is the power of "portfolio thinking," something we've been preaching for a long time.

By Alexander J. Poulos

Gilead Sciences (GILD) burst into the mainstream in 2015 due to its aggressively priced treatment for hepatitis C (HCV). The company gained notoriety as it priced the treatment at $1,000 per tablet, garnering scorn from politicians on both sides of the political aisle. The original treatment (Sovaldi) was improved on with Harvoni, as Gilead ushered in a new age of cures for a dreaded infectious disease. The difficulty in modeling such treatment is the lack of chronic use, once a patient completes the 12-week course of therapy, with a few exceptions, they are "cured" thus negating the need for chronic treatment. The share price has collapsed in the past year, retracing the entirety of the advance since the product class was first introduced onto the marketplace. The article below will discuss our view of the company in light of recent events.

HCV Franchise

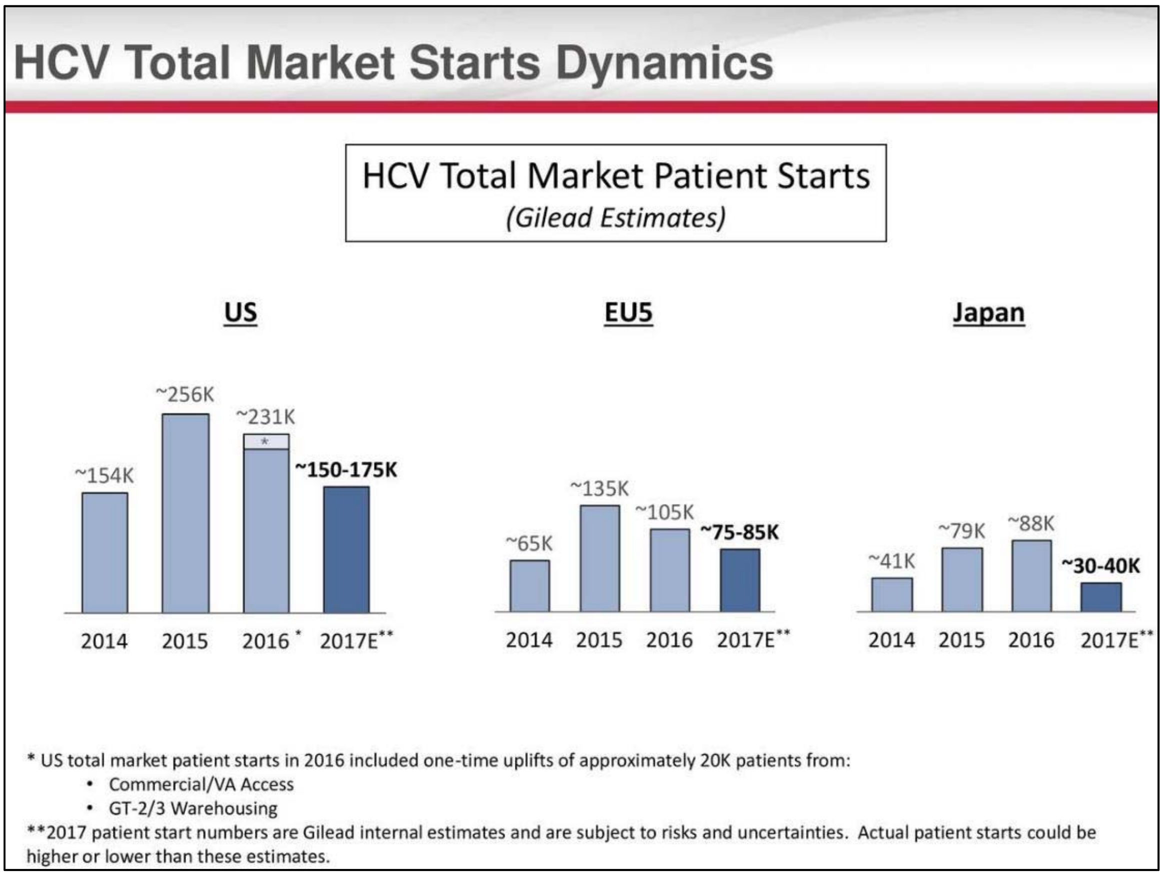


Image Source: Gilead Sciences

The unique dynamics of the HCV marketplace continue to confound most, yet we have a more nuanced point of view. The marketplace was rational with a large rush of patients seeking treatment once a functional cure with minimal side effects became commercially available. This large bolus of patients, in spite of payer protests, accounted for the spike in treatments in the US and Europe. These patients were "warehoused" in anticipation of a revolutionary treatment with a benign side effect profile. As the backlog of patients continues to be worked off, the marketplace is naturally declining as the available patient pool shrinks. The vexing portion is the unpredictable nature of the HCV revenue stream. We

Gilead Sciences...continued on next page

***Gilead Sciences...*from previous page**

view the HCV market through a similar lens as a branded pharmaceutical product that has lost patent exclusivity with a notable exception. Unlike the market dynamics in the patented pharmaceutical space with a rapid loss of share in 3 years (often 80% or more of sales), we expect Gilead's HCV revenue will continue well into the end of next decade.

The story remains complicated, however, and for those with a shorter term view, the decline in the HCV volume may continue to plague the company's share price. The market tends to punish companies that report a continuous decline in revenues, as the valuation context creates a mitigating effect on cash-flow growth over the long haul. Thus, it is very likely that Gilead will remain firmly in the penalty box for the rest of 2017, barring an acquisition, which itself may be fraught with selection, integration and overpayment risk. A deal could even be met with severe skepticism. We continue to prefer longer-term ideas in the newsletter portfolios, and we still believe it was the prudent move to remove Gilead from the Best Ideas Newsletter portfolio last year. The company's recent earnings report may have very well confirmed our fear that the HCV marketplace has not bottomed as many expected. That said, we remain intrigued by the cash-flow generating capacity of the company, and as with all companies in our coverage, we continue to watch shares carefully. The rest of this article will discuss the HIV market along with Gilead's pipeline.

HIV Pipeline

Well before Gilead became a household name, the company grew based on its dominance in the HIV market. We like how Gilead has expanded its HIV franchise by combining new products together to create a single-dose tablet, therefore dramatically reducing the pill load the patient would need to track and consume. By materially reducing the pill burden, Gilead can increase compliance. The increase in compliance aids in negotiations with payers and produces far higher patient outcomes. Aside from the increase in patient outcomes, the combination products allow for a clever bit of lifecycle management. By periodically introducing a new combination product, Gilead can expand the longevity of its HIV franchise.

Products	Patent Expiration	
	U.S.	E.U.
Hepsera	2014	2016
AmBisome	2016	2008
Macugen	2017	2017
Tamiflu	2017	2016
Letairis	2018	2020
Viread	2018*	2017
Ranexa	2019**	2023
Atripla	2021	2017
Cayston	2021	2021
Emtriva	2021	2016
Truvada	2021	2017
Lexiscan	2022	2025
Complera/Eviplera	2022	2022
Vitekta	2023	2028
Zydelig	2025	(2025)
Sovaldi	2029	2028
Stribild	2029	2028
Genvoya	2029	2028
Tybost	2029	2027
Harvoni	2030	2030

Dates in parentheses reflect the estimated expiration date of patents which may issue from currently pending applications. The estimated expiration dates do not include any potential additional exclusivity (e.g., patent term extension, supplementary protection certificates or pediatric exclusivity) that has not yet been granted.

Image Source: Gilead Sciences

Gilead Sciences...continued on next page

***Gilead Sciences...*from previous page**

From our point of view, Gilead is well along in introducing its next generation of combination products, this time utilizing Tenofovir alafenamide (TAF) in place of Tenofovir disoproxil fumarate (TDF). TAF main selling point is the product can be used in a smaller amount, thus reducing the side effect profile. The key benefit is the product is far easier on the kidneys, which become a challenge as the patient ages.

The improvement in the overall side-effect profile should allow Gilead to gain additional traction in the HIV market. Thus far, Gilead has been able to transition a significant portion of its patient base away from its legacy products that lose patent protection in the US in 2021 to the improved version that utilizes TAF. Also, a small percentage that was treated with a non-Gilead product is being converted as well.

We applaud the management team at Gilead for a stellar bit of lifecycle management. By introducing the new TAF-based regiments well before the patents on the TDF products lapse in the US, the company has expanded its patent estate by roughly eight years to the end of 2029. We expect the bulk of the patient population to convert over well before the patent expiration in 2021, thus ensuring Gilead HIV revenue stream well into the end of the next decade.

In addition to the TAF rollout, Gilead is developing a novel class to combat the HIV infection. The new product is Bictegravir, an unboosted integrase inhibitor. Thus far, the product has demonstrated a benign side-effect profile with Gilead slated to release phase 2 data comparing Bictegravir against Dolutegravir in combination with Emtricitabine/Tenofovir Alafenamide. Dolutegravir is manufactured by VIIV Healthcare, Gilead's chief rival in the HIV space. A positive head-to-head result, if achieved, should allow for Gilead's new product to steal share in addition to giving clinicians a new approach to combat HIV.

We expect Gilead to remain a force in the HIV market, but for the company to attain top line revenue growth and approach its old high, in our view, a new franchise outside of infectious disease will need to be developed. Thus far, Gilead has made some attempts to gain share in the oncology space with Zydelig, but while the product has been approved it can be considered a "failure" as the side-effect profile remains troublesome. In addition, the company recently reported a clinical failure of Momelotinib for the treatment of Myelofibrosis. We view the oncology pipeline as uninspiring, thus necessitating the need to hire Alexander Rivas from Novartis (NVS) to head up Gilead's Oncology division. We consider the hire as a positive one, yet it will take time to see if Rivas can turn around the company's floundering fortunes in Oncology.

Non-Alcoholic Steatohepatitis

The area that retains the greatest potential of a new cornerstone "franchise" for Gilead is a treatment for Non-Alcoholic Steatohepatitis or better known by the acronym NASH. NASH is the more dangerous form of Non-Alcoholic Fatty Liver Diseases, a disorder where fat accumulates in the liver. The danger with NASH is for the disease to progress into cirrhosis, a condition where the liver ceases to function properly. NASH is a natural target market for Gilead as it will expand on its expertise in HCV as both diseases primarily affect the function of the liver. Also, from a cost perspective, Gilead will be able to utilize the extensive sales force that has built a lasting relationship with hepatologists from the promotion of its HCV franchise. This may bestow on Gilead a competitive advantage over chief rival Allergan (AGN), as the latter will need to build a sales force assuming its recently-acquired products reach the market.

Gilead disclosed some important phase 2 results for Selonsertib, an apoptosis signal-regulating kinase 1 (ASK1) inhibitor, as part of a likely multi-drug regimen to treat NASH. The product has been moved into Phase 3 testing after consulting with the FDA on a clinical trial design. Selonsertib is being tested on patients with an F3 and F4 score to determine efficacy. The severity of liver Fibrosis is measured on a 0-4 scale with the most severe case assigned a 4. The treatment for NASH remains an area of significant

***Gilead Sciences*...continued on next page**

*Gilead Sciences...*from previous page

unmet need; it seems the company is focusing on the patient who is most "ill" with testing, a wise approach in light of what is undoubtedly going to be a lifetime treatment with a heavy cost burden. In addition to Selonsertib, Gilead is looking to pair the product with GS-0979 an allosteric acetyl-CoA carboxylase (ACC) inhibitor and GS-9674 an FXR agonist, to combat NASH from a variety of angles.

An ACC inhibitor works by targeting a key enzyme needed for the development of fat that will be deposited in the liver. The compound was acquired in a deal with Nimbus Therapeutics with Gilead agreeing to pay up to $1.2 billion based on the achievement of certain milestones. Gilead also acquired GS-0979 in a deal with privately-held Phenex Pharmaceuticals for $470 million in addition to undisclosed royalties.

Gilead expects to have additional phase 2 data for 12 and 24 weeks of treatment for each product by the middle of this year. Depending on the data read, Gilead will push forth with combinations to develop an optimal treatment regimen. We will be watching the data carefully; a win in NASH would diversify the company away from the HCV market, thus potentially returning the company firmly to top-line growth.

Balance Sheet and the Role of M&A

By virtue of the tremendous amount of free cash the company generates, Gilead continues to have financial flexibility (even with long-term liabilities of ~$28.3 billion). The company now holds over $32 billion in cash, with an accumulation every quarter. The cash-rich balance sheet coupled with the decline in revenue has brought forth a sonic scream for the company to engage in M&A activity. While we agree, M&A should be a natural part of the business model, one which Gilead has utilized with success in the past (its Pharmasset purchase for $11.2 billion hatched its dominance in the HCV franchise), the biggest return may be generated from acquiring clinical or phase 1 assets instead of de-risked near-term pipeline assets. This is risky.

For example, Tesaro Pharmaceuticals (TSRO) continues its ascent with the company's market capitalization now exceeding $9.8 billion. Tesaro's advance is galvanized with what may prove to be a best-in-class PARP inhibitor, fueling speculation of a takeout by one of the larger entrenched pharma companies in a similar manner to the recently-completed Medivation deal. For someone to acquire Tesaro, a hefty premium will need to be paid, which may limit the overall return that can be generated in a hotly competitive field. The management team at Gilead has commented numerous times that some of the premiums paid are uneconomical at this point, a view with which we agree with. We prefer to see additional deals similar to the Phenex, Nimbus, and Galapagos deal that will be discussed below.

Inflammatory Disease

The treatment of inflammatory disease remains the single-largest area of drug spending in the ultra-expensive specialty pharmaceuticals business. Gilead is now well-represented in infectious disease, but was noticeably absent, until a deal was struck with Galapagos for its lead compound Filgotinib for the treatment of Crohn's Disease and Rheumatoid Arthritis. Galapagos originally had a partnership with Abbvie (ABBV) for the rights to co-develop the product. Abbvie decided to go with its in-house wholly-owned product ABT-494, thus jolting Galapagos. Gilead stepped in, backed by the abundance of cash generated from its HCV franchise, to scoop up the drug at an attractive price.

Figotinib continues to impress in the clinical labs with a particular emphasis on Crohn's disease. While it was difficult to compare different drug trial results as the control mechanisms vary, the side-effect profile for Filgotinib is very promising. The mechanism for Filgotinib's more benign side-effect profile rests with the molecule's ability to target the Janus Kinase enzyme selectively. The older class of meds that lack specificity such as Tofacitinib (Xeljanz) have been plagued with an unwanted side-effect profile. The increased risk of adverse side effects has led to the issuance of a "Boxed Warning" over concerns of an increase in infections and the development of Shingles.

*Gilead Sciences...*continued on page 9

= ALL TIME HIGH

The Best Ideas Portfolio

By Valuentum Analysts

Portfolio Return	Benchmark Return	Outperformance
124.0%	92.9%	31.1pts

Below we outline the constituents of the portfolio and their respective weightings and returns thus far (please note that many stocks have been removed since inception). Each subsequent issue discusses Valuentum's latest changes to the portfolio and analysis and trends impacting companies in our Best Ideas portfolio.

We currently have ~11% of the portfolio in cash, a level we're looking to bring down in coming months. Tactically, 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 portfolio 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, the Valuentum Buying Index.

THE BEST IDEAS PORTFOLIO -- as of February 15, 2017 — **Best Ideas Portfolio Inception Date: May 17, 2011**

Portfolio Holdings	Symbol	Initial VBI*	Current VBI**	Fair Value	P/FV	First Purchase	Cost/Shr ($)	# Shares	Total Cost ($)	Price/Shr ($)	Current Value ($)	Cumulative Div's Rec'd	% of Portfolio	% Return (dividends included)
Bullish														
Apple Corp.	AAPL	10	7	$159.00	0.85	17-Jun-11	51.92	107	5,569.33	135.51	14,499.57	1,211.81	6.5%	182.1%
Altria Group	MO	8	6	$58.00	1.24	28-Jun-11	28.39	157	4,471.86	72.17	11,330.69	2,475.56	5.1%	208.7%
Berkshire Hathaway	BRK-B	6	5	$160.00	1.05	20-Apr-16	146.13	69	10,089.97	167.28	11,542.32		5.2%	14.4%
Buffalo Wild Wings	BWLD	6	6	$190.00	0.83	27-Aug-15	179.81	16	2,876.90	158.00	2,528.00		1.1%	-12.1%
Cisco	CSCO	9	3	$42.00	0.78	14-Nov-14	26.33	221	5,831.87	32.82	7,253.22	332.84	3.2%	30.1%
CVS Health	CVS	9	9	$103.00	0.77	6-Jan-17	81.84	79	6,479.36	79.41	6,273.39	39.50	2.8%	-2.6%
Energy Select SPDR	XLE	NR	NR	NA	NMF	6-Oct-15	67.14	143	9,608.02	73.37	10,491.91	320.79	4.7%	12.5%
Facebook	FB	6	7	$172.00	0.78	29-Jan-16	112.10	50	5,612.00	133.44	6,672.00		3.0%	18.9%
Financial Select SPDR	XLF	NA	6	NA	NMF	9-Jan-11	13.46	178	2,405.83	24.52	4,369.93	290.05	2.0%	93.7%
General Electric	GE	7	6	$36.00	0.84	21-Oct-13	25.99	375	9,761.75	30.35	11,381.25	1,077.00	5.1%	27.6%
General Motors	GM	6	6	$43.00	0.86	26-Aug-16	31.65	132	4,184.80	37.08	4,894.56	100.32	2.2%	19.4%
Google - Class C	GOOG	10	7	$924.00	0.89	23-Oct-12	450.92	7	3,170.42	818.98	5,732.86	10.35	2.6%	81.1%
Google - Class A	GOOGL	10	7	$924.00	0.89	4-Apr-14	Split	7	Split	837.32	5,861.24		2.6%	+++
Health Care ETF	XLV	9	6	NA	NMF	22-May-12	36.60	125	4,582.00	73.66	9,207.50	529.61	4.1%	112.5%
Intel	INTC	6	7	$42.00	0.86	12-Sep-11	20.48	150	3,086.50	36.05	5,407.50	673.50	2.4%	97.0%
Johnson & Johnson	JNJ	6	7	$121.00	0.97	29-Jan-16	104.18	54	5,632.72	117.20	6,328.80	170.10	2.8%	15.4%
SPDR S&P Bank ETF	KBE	NR	NR	NA	NMF	9-Jan-12	21.07	100	2,114.00	45.62	4,562.00	266.14	2.0%	128.4%
Kinder Morgan	KMI	5	6	$20.00	1.11	17-Feb-16	17.29	157	2,721.53	22.27	3,496.39	78.50	1.6%	31.4%
Michael Kors	KORS	8	3	$66.00	0.58	27-Aug-15	43.44	68	2,953.80	38.05	2,587.40		1.2%	-12.4%
PayPal	PYPL	UR	6	UR	UR	17-Jul-15	Spin-off	100	Splt	41.87	4,187.00		1.9%	+++
Priceline	PCLN	10	6	$1551.00	1.06	26-Feb-15	1239.49	6	7,450.91	1648.96	9,893.76		4.4%	32.8%
Republic Services	RSG	8	6	$48.00	1.23	19-May-11	31.42	201	6,329.42	59.11	11,881.11	1,287.42	5.3%	108.1%
SPDR S&P Dividend ETF	SDY	NR	NR	NA	NMF	20-Apr-16	81.33	124	10,091.92	87.84	10,892.16	197.09	4.9%	9.9%
Teva Pharma	TEVA	6	6	$58.00	0.63	24-Jul-13	41.22	77	3,180.94	36.77	2,831.29	364.09	1.3%	0.5%
Union Pacific	UNP	6	6	$97.00	1.13	24-Jul-13	79.67	40	3,193.80	109.78	4,391.20	264.20	2.0%	45.8%
Utilities Select SPDR	XLU	NR	NR	NA	NMF	18-Mar-14	41.12	83	3,419.96	49.05	4,071.15	366.85	1.8%	29.8%
Visa	V	7	7	$84.00	1.04	30-Nov-11	26.86	188	5,064.39	87.54	16,457.52	393.71	7.3%	232.7%
Latest changes: 79 shares of CVS purchased (1/6).														
Cash -- changes in monthly cash balance reflects dividends received and trading gains/losses, where applicable.											24,998.18		11.2%	0.0%
Bearish														
For investors seeking 'short' or 'put option' exposure, please consider firms with VBI ratings with 1 and 2 as ideas.														
Best Ideas Portfolio Value									Original --> 100,000.00	Current -->	**224,023.90**			**124.0%**
S&P 500 Index (SPY)						17-May-11	132.69	754	100,000.00	234.92	177,044.24	15,870.40	91.8%	
Cash											15,870.40		8.2%	
Benchmark Portfolio Value											**192,914.64**			**92.9%**
Relative Outperformance														**31.1 pts**

Data as of February 15, 2017. 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). Best Ideas portfolio is not a real money portfolio.

*Gilead Sciences…*from page 7

In addition to the indication for Crohn's, Filgotinib is in phase 3 for the indication of Rheumatoid Arthritis, the most lucrative yet crowded field in inflammatory disease. Galapagos has wisely designed the trial with an arm utilizing top-selling product Humira as a control, thus offering an inspiring reference point. The trial is dubbed "Finch" which commenced in August 2016. The trial is designed to run for 52 weeks, allowing ample time to gather data. A key selling point of Filgotinib is the delivery mechanism; the product does not require injection such as top-selling product Humira. Instead, Filgotinib comes in a convenient oral dosage form, which we expect will be used for marketing purposes to highlight the convenience and ease-of-use of the product.

Conclusion

We view Gilead Sciences through the lens of a pharmaceutical company in that it has lost the patent protection of one of its primary compounds. The upside, as reflected in the upper bound of our fair value range, is that the rate of decline may be far less than the traditional patent exclusivity loss (as the HCV franchise enjoys patent protection out well through the end of the next decade). The issue is the drop in overall patient population has severely hampered year over year revenue growth.

That said, we view the cash flow generated from Gilead Sciences' existing franchises very favorably, and we view Gilead as better positioned from a patent expiration perspective than most of its pharma/biotech competitors. Its strong free cash flow should allow for generous annual dividend hikes, with Gilead recently announcing a bump in the quarterly payout to $0.52 cents for 2017. The current yield is over 3%, in line with its large-cap competitors.

We've always liked the company that "cured" hep C, and we still think shares of Gilead are cheap, but our experience in the market told us to get out when we did, and this proved to be the right move. We substituted the company's shares with Johnson & Johnson (JNJ), and we've been pleased with the relative alpha generated. If Gilead's technicals settle, we may re-add them to the Best Ideas Newsletter portfolio. Remember: each idea should be viewed in the context of the newsletter portfolios, and the Best Ideas Newsletter portfolio continues to set all-time highs.

Disclosures: Healthcare and biotech contributor Alexander J. Poulos is long Gilead Sciences. Valuentum does not own Gilead nor does it include it in its newsletter portfolios.

The Bottom Line: Altria's Translates to Dividend Growth

Altria continues to successfully battle a challenging demand environment for cigarette volumes across its industry, and the company has once again rolled out expectations for meaningful earnings-per-share growth in 2017. Altria's stock is among the best performers in history – find out why.

By Kris Rosemann

Some readers may be surprised that (Altria) is a top performer for investors in the face of the onslaught of government restrictions and legal actions that have cost the firm tens of billions of dollars and threaten the cigarette manufacturer with bankruptcy.

But in the capital markets, bad news for the firm often is transformed into good news for investors. Many shun the stock in the company and fear that its legal liability for producing a dangerous product--cigarettes--will eventually crush the firm. This aversion to the firm pushes down the price of (Altria's) shares and raises the return to investors who stick with the stock.

As long as the firm survives and continues to be very profitable, paying out a good fraction of its earnings in the form of dividends, investors will continue to do extraordinarily well.

The Bottom Line…continued on next page

*The Bottom Line…*from previous page

> *-- "The Future For Investors," Jeremy J. Siegel explaining why Altria (MO) "has been the golden company that beat the market by 9 percent per year over the last half century and left every other firm far behind in the race to be number one (through 2003)."*

Altria (MO) has been one of the best-performing stocks in history, and we continue to include the company in both the Best Ideas Newsletter portfolio and Dividend Growth Newsletter portfolio. Shares of the tobacco giant yield ~3.4% at current price levels, and we like the resilience of the payout thanks in part to the powerful product pricing dynamics inherent to its business model and the financial flexibility its equity stake in beer giant AB-InBev (BUD) provides. Altria's policy is to maintain a dividend payout ratio target of roughly 80% of adjusted diluted earnings per share, and it continues to hold its long-term target of average annual adjusted diluted earnings per share growth of 7%-9%, despite a challenging cigarette volume environment. This speaks to how important pricing power is in the tobacco business. The company's 2017 adjusted earnings per share guidance in the range of $3.26-$3.32 implies a rate of growth above its long-term goals (and that may also mean better-than-expected dividend growth for 2017, too).

That said, Altria's 2016 fourth quarter report, released February 1, did little to change our opinion of the company's valuation or dividend strength, the former stretched, in our view. Cigarette volumes remain under pressure (total cigarette unit volume at Altria dropped 4.8% in the quarter, in line with the drop witnessed at brand Marlboro), but pricing gains offset the largely expected declines to a degree. Net revenue fell 1% in the quarter from the year-ago period, but operating companies income (OCI) leapt 4.3% in the quarter as adjusted OCI margins expanded a full 2 percentage points. Adjusted diluted earnings per share advanced 1.5% on a year-over-year basis, helped by stronger pricing, lower benefits costs and lower tobacco and health litigation items in its 'Smokeable Products' segment and higher pricing and volume in its 'Smokeless Products' segment (along with a slightly lower share count). In light of Altria's total return to shareholders of 20.5% in 2016 (better than the S&P 500 and the S&P Food, Beverage and Tobacco Index), we think CEO Marty Barrington described the year correctly in the press release: "Altria had another outstanding year."

Looking ahead to the full-year 2017, Altria expects adjusted diluted earnings per share to grow 7.5%-9.5%, slightly above its long-term goal, to a range of $3.26-$3.32. The company is in the midst of a productivity initiative, announced January 2016, that it expects to deliver $300 million in annualized cost savings by the end of 2017, and it is projecting another $50 million in annualized cost savings by the end of 2018 to come from the facilities consolidation initiative it announced in October 2016. Management continues to do fine job, growing the bottom line, despite industry pressures, and its MarkTen e-vapor product is now available in "stores representing about 55% of the e-vapor category volume in retail channels."

In 2017, we're looking for the expectations of high-single digit earnings per share advancement to translate into another solid increase in the quarterly dividend come late August (Altria typically increases its payout each August). Though the company's net debt position weighs on its Dividend Cushion ratio of 1.1--net debt was ~$9.3 billion at the end of 2016--its 10.2% equity stake in beer giant AB-InBev--estimated at ~$17.6 billion at the end of 2016--gives it considerable financial flexibility and inspires further confidence in the dividend. In the event Altria really wants to ramp up its payout, an opportunistic one-time dividend from the cash proceeds of its AB-Inbev sale would be a significant catalyst for shares.

Though shares of Altria are fully-valued, in our opinion, most of the rest of the broader market is overheated. At the moment, we plan to continue to hold shares of Altria in the newsletter portfolios, as we continue to evaluate the risk/reward profile. Altria was added to both the Best Ideas Newsletter portfolio and Dividend Growth Newsletter portfolio below the $30 per-share mark. The company has been one of the best performing stocks since the inception of the portfolios, too. Altria's weighting in the respective portfolios is 4%-6%.

Best Ideas Roundup: Visa, Facebook, Buffalo Wild Wings

Let's take a look at the recent earnings reports and outlooks for three key holdings in the Best Ideas Newsletter portfolio.

By Brian Nelson, CFA

Visa

There are three reasons why we like Visa (V) as a core holding in the Best Ideas Newsletter portfolio. First, electronic commerce and the proliferation of using 'plastic' to pay for just about anything (a cashless society) plays into the hands of the credit card network. It continues to benefit from uninterrupted secular growth. Second, Visa gets paid every time someone uses one of its credit cards, and the company, unlike American Express (AXP) or Discover (DFS), doesn't hold credit risk (its business model depends on volume growth, not on whether customers repay their debts). Third, the company's financials are incredible: its capital-light business model generates lofty operating margins and a significant amount of free cash flow.

On February 2, Visa reported solid first-quarter results for fiscal 2017. During the quarter, net operating revenue advanced 25%, helping to drive 23% growth in both adjusted net income and earnings per share. Payments volume expansion, on a constant-dollar basis, was 39% over the prior year, at $1.8 trillion. We liked the tone of the report, too. New CEO Alfred Kelly (he just completed his first quarter at the company) noted "fiscal 2017 is off to a terrific start…driven by accelerating growth in payments volume, cross-border commerce and processed transactions in virtually all regions around the world."

Management also pointed to good momentum in its business, and it indicated the integration of Visa Europe is proceeding well. Visa remains committed to the burgeoning China market for the long term--it's looking forward to formally submitting its licensing application and setting up its processing infrastructure there (but awaiting PBOC formalities). The company ended 2016 with cash, cash equivalents, and available-for-sale investment securities of $13.2 billion, against a long-term debt load of $14.1 billion, and will be using buybacks to "offset the equity dilution from the Visa Europe acquisition."

Looking ahead, Visa reaffirmed its financial outlook for fiscal full-year 2017, including its impressive annual operating margin guidance in the mid-60s. On a GAAP basis, for fiscal 2017, net revenue growth is targeted in the range of 16%-18% on a nominal dollar basis, while annual GAAP earnings-per-share growth is expected in the low-30s on a nominal basis. Visa's fundamental backdrop remains incredibly strong, and the company will remain a core holding in the Best Ideas Newsletter portfolio.

From the first-quarter fiscal 2017 conference call:

> "…we're in a growth industry, and there's a huge opportunity in front of us. The global opportunity to digitize cash and check is enormous. We have a vibrant core business in developed regions with even more growth opportunities in the international and emerging markets with low penetration rates. Governments and emerging middle classes are leading the way to digitize more payments in developing countries, while e-commerce is displacing cash and check in developed countries. Through our focus on technological innovation and partnership development, Visa is well positioned for sustained growth going forward."

Facebook

Facebook (FB) is back on top, setting all-time highs again.

We include Facebook in the Best Ideas Newsletter portfolio for a number of reasons. First and foremost, a greater understanding of human psychology and what drives individuals—the need for connection and/or to feed their egos and beyond—is partly why we think the company will be a long-term winner. People will always be people. CEO Mark Zuckerberg and company have been able to tap into the best way to capitalize on human psychology and have built a business model around this core essence of humanity. Facebook is not a fad, but is an ingrained part of the make-up of society, one that will not go away

*Best Ideas Roundup…*continued on next page

***Best Ideas Roundup…*from previous page**

anytime soon. The Best Ideas Newsletter portfolio would not be complete without it, in our opinion.

The social media giant reported strong fourth quarter 2016 results February 1. The financial performance of Facebook remains phenomenal. Advertising revenues advanced 53% in the quarter, dwarfing the increase in total costs and expenses and driving a near-80% jump in income from operations. During the period, Facebook's operating margin advanced to 52% from 44% in the same quarter of 2015 (its non-GAAP operating margin was 64% in the fourth quarter). Net income and diluted earnings per share more than doubled in the fourth quarter and nearly tripled during full-year 2016, to $3.49. Free cash flow, as defined as cash flow from operations less all capital expenditures, came in at $11.6 billion during the year, padding the company's debt-free balance sheet of $29.45 billion.

Free Cash Flow ($ in millions)	Q4'14	Q1'15	Q2'15	Q3'15	Q4'15	Q1'16	Q2'16	Q3'16	Q4'16
Net cash provided by operating activities	$ 2,087	$ 2,123	$ 2,266	$ 2,538	$ 3,393	$ 3,477	$ 3,665	$ 4,036	$ 4,930
Purchases of property and equipment	517	502	549	780	692	1,132	995	1,095	1,269
Free Cash Flow	$ 1,570	$ 1,621	$ 1,717	$ 1,758	$ 2,701	$ 2,345	$ 2,670	$ 2,941	$ 3,661

Image Source: Facebook

Internal metrics, in terms of daily active users (DAU), mobile DAUs, monthly active users (MAUs) and mobile MAUs were healthy, too. Both mobile DAUs and mobile MAUs increased more than 20% during the full-year 2016, while mobile ad revenue accounted for ~84% of total advertising revenue in the quarter (up 4 percentage points in the same-period last year). There were a number of fascinating insights from the conference call, too, including further experimentation with Live 360 video, expanding ways to grow its ecosystem of video content, and commentary surrounding combating fake news, spam and clickbait. Management also said that it continues to be excited about what's ahead for virtual reality (VR).

Looking ahead to 2017, Facebook is conservatively guiding the markets to expect that its "ad revenue growth rate will come down meaningfully in 2017," but that isn't saying much. Growth was phenomenal in fiscal 2016, and the law of large numbers is inevitable (as the base of revenue increases, it becomes much harder to keep achieving accelerated growth). On the cost side, Facebook continues to invest and views 2017 as an "aggressive investment year." There's nothing wrong with that as investments in head count, R&D, content sales and marketing should all pave the way to achieve longer-term priorities. The company noted that the board authorized a $6 billion stock repurchase program beginning in 2017, so earnings-per-share growth in the year will be robust. We liked the update.

Buffalo Wild Wings

One of our favorite restaurant concepts, Buffalo Wild Wings (BWLD) reported mixed results February 7, just a day after activist investor Marcato (which owns a ~5% stake in the company) said it has nominated four candidates to the board at the company. Buffalo Wild Wings' stock-price performance has been choppy as of late, but we believe in the long-term value of this concept, and management has a number of unique levers (item sizes and the like) it can pull to continue to drive earnings performance and keep costs in check. "B-dubs," as it is informally called, represents our restaurant exposure in the Best Ideas Newsletter portfolio, while Cracker Barrel (CBRL) represents our restaurant exposure in the Dividend Growth Newsletter portfolio.

We think a focus on full-year 2016 performance and the company's outlook for 2017 may be best for insight into our reasons for continuing to hold B-dubs. First, December marked a difficult month for the restaurant ("exacerbated by the calendar shift of the Christmas holiday"), but several of its key programs *seem to be driving positive traffic roughly six weeks into 2017*. Total revenue and

***Best Ideas Roundup…*continued on next page**

*Best Ideas Roundup…*from previous page

company-owned restaurant sales advanced ~10% during 2016, even though same-store sales trends continue to face pressure in the year. Net earnings per share were roughly flat on the year (up 3%), but we think the concept has all of the makings of a long-term winner. Free cash flow in 2016 was ~$141 million, compared to ~$65 million in the prior year (the measure is targeted in the range of $160-$170 million in 2017).

Looking ahead, Buffalo Wild Wings will continue to have to deal with a very challenging restaurant environment, but the company's earnings target range of $5.60-$6.00 for 2017 looks achievable (operating income growth is targeted in the 9%-13% range), and an "expanded share repurchase program with an accelerated timeline to achieve (its) target of 1.5x net debt to EBITDA by year-end" may offer some flexibility to hit that bottom-line range, too. During 2017, same-store sales growth is targeted in the range of 1%-2% as the company collectively adds dozens of stores in the US (15 company-owned and 15 franchised) and internationally (20 franchised)--it will add 2 company-owned and 12-15 franchised R Taco restaurants. The Buffalo Wild Wings concept is differentiated, and activist Marcato may be the shot in the arm the executive team needs. It may be several quarters, however, before a real catalyst emerges.

Amazon's Future May Be Rich, But So Is Its Valuation

Amazon continues to disrupt the traditional retail landscape and its cloud-based services are gaining momentum, but shares look to be running ahead of its fundamental trajectory. Let's take a look at its most recent quarter.

By Kris Rosemann

Shares of Amazon (AMZN) are trading at more than 40 times 2016 free cash flow, a tremendous level, even for a company whose top-line is growing as quickly as Amazon's. High levels of uncertainty regarding its long-term operating margin increases the challenges in deriving the company's "true" intrinsic value, and while we're fans of the e-commerce giant's increasing free cash flow generation, we're not comfortable anointing Amazon Web Services (AWS), the true driver of its profitability and free cash flow improvements, as a long-term winner in the rapidly evolving cloud-based services space. Though far from its roots during the dot-com bubble, Amazon is still a speculative idea, in our view, and simply put, the current price tag is too high for us to consider.

That said, the momentum Amazon is seeing in its free cash flow generation of late is encouraging as it reported February 2 that operating cash flow in 2016 jumped 38% from the year-ago period, to $16.4 billion, and free cash flow leapt to $9.7 billion in the year from $7.3 in 2015. The company's top line continues to expand, net sales in the fourth quarter advanced 22% on a year-over-year basis, which outpaced operating income growth in the quarter due to more aggressive spending in areas such as fulfillment facility development, Amazon Prime, and video content.

Management is anticipating the increased spending to continue into 2017, and has issued guidance for operating income to fall in the first quarter of the year, even as it continues to expect solid double-digit growth on its top line. Revenue growth is projected to be in a range of 14%-23%, a rather wide range and one that came in below consensus estimates for the quarter. Shares were punished for the lower-than-anticipated top-line guidance, but the bigger issue remains margin uncertainty, from our point of view.

At this point in time, we agree that it is rational to expect strong revenue growth for the foreseeable future for Amazon, but a reasonable picture of the long-term margin profile of the company continues to be obscure. For example, in the first quarter of 2017, a quarter that was more than a month underway when guidance was issued, management is guiding operating margin to be in a range of 0.7%-2.7%. Not only are these margins razor thin, but even the high end of the guidance is roughly a one percentage point contraction from the first quarter of 2016. To justify Amazon's current price tag, normalized operating margins in the mid-single-digit range *are absolutely necessary*.

*Amazon's Future…*continued on next page

*Amazon's Future…*from previous page

Amazon's long-term goal to optimize free cash flow will benefit from growth in the higher margin Amazon Web Services business, which is now at a $14 billion revenue annual run rate, but it may not be large enough to buoy near-term bottom-line performance as the company continues to invest in its lower-margin consumer facing business. Maintaining momentum in AWS won't be easy, but we think management has a solid handle on how the business is shaping up. It announced multiple price cuts to its AWS products in the fourth quarter of 2016, something that is becoming commonplace as new and improved functionalities are developed and operating efficiencies are extracted. Competition will remain intense, potentially further pressuring pricing, and other industry heavyweights, such as Microsoft's (MSFT) Azure platform, are seeing similar momentum.

All in, we're anticipating Amazon continuing to drive significant top-line growth, and investors are likely to continue bidding shares higher in this frothy market. However, we don't make many trades in the newsletter portfolios that offer little fundamental support should investor sentiment, often a fickle beast, surrounding the stock change unexpectedly. We're not doubting the staying power of Amazon, in either its eCommerce or AWS operations, but the future landscape of cloud-based services is one characterized by massive amounts of uncertainty and outside of AWS we're not sure the firm has an long-term answer to its past profitability woes. Amazon's building momentum in free cash flow generation is a welcome sight, and its balance sheet health is worth noting--its net cash balance was ~$18.3 billion at the end of 2016--but with shares at more than 40 times 2016 free cash flow, we're simply not interested.

Is AbbVie a Value Trap?

With uncertainty surrounding the patent of blockbuster drug Humira, AbbVie is looking to deliver another success story from its pipeline. Is it headed for a patent cliff? Let's take a look.

By Alexander J. Poulos and Kris Rosemann

A successful operator in the pharmaceutical industry (XLV) is often characterized by having high margins, allowing for copious amounts of free cash flow generation, which can be returned to shareholders via dividends. In today's yield-starved market environment, major pharma, and the above-average yields of some players within, remains in demand, but investors must be cognizant of the unique risks that face the industry. One key risk remains the loss of patent protection on drugs and treatments that leads to the aforementioned attractive margins. Once a patent is lost, shares are often punished on the news of a loss of a meaningful patent.

Such a development can lure investors into a "value trap." As pharma and biotech (IBB) companies approach the patent cliff, it is common for investors to sell on the news that a patent has been lost, pushing the stock price lower. Over-starved investors searching for attractive yields at a discount may be enticed to swoop in and scoop up shares at the lower price-to-earnings ratio that might result from such an event. However, evaluating the patents of a pharma company prior to investing is a must, from our point of view, and initiating a position in a firm approaching a patent cliff is a major no-no.

This concept should not be too foreign for Valuentum members, as it is related to the momentum aspect of our methodology. Just as we evaluate the most opportune time to initiate a position in a company based on the momentum in its share price, the most opportune time to enter a position in a pharma firm may be as it is beginning to turn the corner with respect to its patent cliff, not as it is approaching the patent cliff. Let's take a look at some of the challenges facing AbbVie (ABBV) to further illustrate the point.

Humira

Overdependence on a single product can be a recipe for disaster, especially in the pharma arena where patents eventually expire and generic competition enters the market, providing meaningful top-line pressure and a potential value trap as described above. As a blockbuster drug, in AbbVie's case Humira, is under patent and in its growth phase, the sales growth potential and operating leverage are extremely

*Is AbbVie…*continued on next page

*Is AbbVie...*from previous page

appealing, but as the patent expires, a tremendous challenge exists in replacing revenue lost to new generic entrants.

Humira, a treatment for a wide range of inflammatory diseases, currently accounts for over 60% of all of AbbVie's sales, and management has masterfully marketed and expanded the disease states Humira can be used to treat. Label expansion aided in the rapid growth and success of the product, and Humira remains one of the top-selling branded pharmaceutical products in the world. However, 2017 may be the last full year of protected sales for Humira, and management's greatest challenge now revolves around developing a host of competing products to lap the expected sales erosion when Humira inevitably faces a biosimilar challenge.

IP Estate

Slides

Inflammatory Disease Remains a Key Driver of the Specialty Drug Trend

			Trend		
Rank	Therapy Class	PMPY Spend ($)	Utilization (%)	Unit Cost (%)	Total (%)
1	Inflammatory conditions	89.10	10.3	14.7	25.0
2	Multiple sclerosis	53.31	3.5	6.2	9.7
3	Oncology	49.62	9.3	14.4	23.7
4	Hepatitis C	38.44	-2.2	9.2	7.0
5	Human immunodeficiency virus	31.53	4.6	12.0	16.6
6	Growth deficiency	7.12	2.8	2.8	5.6
7	Cystic fibrosis	6.64	12.5	40.9	53.4
8	Pulmonary hypertension	5.85	13.4	4.8	18.1
9	Hemophilia	5.79	4.9	15.4	20.4
10	Sleep disorders	4.57	5.5	18.5	24.1
	Total Specialty	$341.21	6.8%	11.0%	17.8%

Express Scripts. Drug Trend Report 2015. Available at: http://lab.express-scripts.com/lab/drug-trend-report. Accessed April 11, 2016.

Image Source: Express Scripts

The unit cost for specialty pharmacy continues to grow well above the rate of inflation, thus putting enormous strain on national healthcare budgets. In fairness, the field continues to deliver a host of new treatments especially in the area of oncology, but we see the rapid acceptance of biosimilars as an excellent way to bring cost rationalization into the arena. As seen in the above image, drugs used to treat infalmmatory diseases saw the largest spending increase in 2015 thanks to a combination of advancing costs and utilization rates. Such a development makes Humira, inflammatory disease market leader in terms of share, a likely target for price-cutting biosimilars.

*Is AbbVie...*continued on next page

*Is AbbVie…*from previous page

Adalimumab, the chemical name for Humira composition of matter patent, expired in December of 2016; a composition of matter patent covers the compound thus preventing competition. AbbVie also has a non-composition of matter patent which is expected to remain valid through 2022; non-composition of matter patents often attract a patent challenge from the generic drug companies as they jockey to gain the ability to first bring to market an authorized generic for the product. The management team at AbbVie remains steadfast that they will rigorously enforce its IP estate, a view we share. Where we differ is in the ultimate success of the effort, as a biosimilar for Humira is likely to be brought to market well before 2022, in our opinion, but more specific timing of such an entrant is difficult to forecast.

What we do know is the European patent for Humira will expire in 2018, and October 2018 looks to be the month a biosimilar will enter the European market. The management team at AbbVie remains confident they will be able to stem the decline, though no such guarantee can be made. For context, the recent entrance of a biosimilar of Amgen's (AMGN) Neupogen is a prime example of market share loss that can be expected once an effective biosimilar enters the market. Neupogen worldwide sales eroded 25% on a year-over-year basis in the first nine months of 2016 after biosimilars were first launched in September of 2015.

We're not convinced AbbVie will be able to retain the bulk of its market share and price once a biosimilar enters the market. To compound matters further, in what we view as a tone-deaf move in this ultra-sensitive pricing environment, AbbVie announced a price hike of 8.4% on Humira. Though we acklowledge the negotiations with the PBM's will ultimately negate much if not all of the price hike, such a price increase only attracts attention to the lack of competition surrounding the drug.

Leonard Schleifer, the outspoken CEO of Regeneron Pharmaceuticals (REGN), and his firm are posing a significant threat to the long-term viability of the Humira franchise. In addition to it taking a stance against routine, unwarranted drug price hikes, Regeneron has a competing product dubbed Sarilumab that is awaiting marketing approval from the FDA. Regeneron and its partner Sanofi (SNY) funded a head to head comparison study pitting Sarilumab against Humira, and the data showed Sarilumab posted superior results in the study, ample ammunition that will be used to carve out a niche for Sarilumab in the marketplace. We would not be at all surprised if Regeneron/Sanofi aggressively price Sarilumab in a similar manner to what we've seen in the hepatitis C market, which have helped lead to a lowering of net treatment cost per patient.

Regeneron and Sanofi received a complete response letter from the FDA stating deficiencies in the factory that would be used to produce the product, delaying the commercial release of the treatment. However, Regeneron expects to resubmit the license application in the first quarter of 2017 and anticipates a two-month review cycle, putting an action date from the FDA in the second quarter of 2017.

Sarilumab is not the only competitive threat to AbbVie's Humira; additional products have gained marketing approval with Cosentyx and Taltz the most recent examples. As the number of competitors increases, the PBM's will utilize the increase in competition to drive down price through formulary exclusions. We believe it is unrealistic to expect Humira to not only maintain its market share but also implement price increases to expand revenues at a double-digit clip through 2022. AbbVie will need to develop new products to make up for the loss of revenue from Humira beginning in 2018 with European sales.

Imbruvica

Imbruvica is a Bruton's tyrosine kinase inhibitor that is used to treat a range of diseases most notably

*Is AbbVie…*continued on next page

*Is AbbVie...*from previous page

varying forms of Leukemia. AbbVie purchased a 50% stake in the molecule when it acquired Pharmacyclics for $21 billion in 2015. Imbruvica remains the key compound, as AbbVie views Imbruvica as a clinical backbone to power its oncology pipeline. The product is partnered with Johnson and Johnson (JNJ) with peak expected sales north of $7 billion targeted for AbbVie's stake--it controls 100% of the US sales and receives royalties from international sales. Thus far, the product seems well on track, generating more than $1.8 billion in sales for AbbVie in 2016.

Part of Imbruvica's ability to hit AbbVie peak sales figure will come from label expansion. The product remains well on track with recent approval for Marginal Zone Lymphoma among other indications. Our outlook for Imbruvica remains favorable for now with the most notable challenger coming from AstraZeneca's (AZN) recently acquired compound Acalabrutinib. AstraZeneca is angling for an early approval for Acalabrutinib in patients who are resistant to treatment with Imbruvica via an expected submission at some point in 2017. From the initial data reads, Acalabrutinib does hold particular promise as the molecule is better tolerated by the patients it has been studied on. At this time, Acalabrutinib seems to pose the greatest challenge to Imbruvica yet most of the indications will not be filed until 2020, giving AbbVie ample time to establish Imbruvica as the gold standard of care.

The all-important IP estate for Imbruvica is secure with the US patent in force through 2027, while the international patent does not expire until 2029. We feel based on Imbruvica's impressive lead backed with a solid, long-dated patent that the treatment will become a core franchise for AbbVie once the Humira patent expires. The product will not make up for the entire revenue decline--Humira sales topped $16 billion in 2016--yet it should form the basis of a stable, high-value oncology franchise with lengthy patent protection.

Infectious Disease

AbbVie's quest to carve out a chunk of the lucrative hepatitis C market continues to underwhelm. Management initially had high hopes for the unit; those dreams have been thoroughly dashed by Gilead Sciences (GILD) and to a lesser extent Merck (MRK). AbbVie's initial foray into price competition via an exclusive deal with Express Scripts (ESRX) has done little to grow market share, with industry juggernaut Gilead still controlling over 85% of the overall US market for hepatitis C. The overarching challenge in the hep C market is that the eligible pool of candidates continues to decline as patients are cured after a short course of therapy.

In our view, the hep C market remains in terminal decline with little that can be done to increase the overall size of the market, and we're looking at the market through a similar lens of a product that has lost patent protection except with a more drawn out revenue decline. To compound matters, the exclusive formulary deal with Express Scripts has lapsed with Gilead's lead product Harvoni now gaining coverage.

The decline can be seen in AbbVie's revenue with Viekira Pak totaling just over $1.5 billion in sales for 2016, a decrease of more than 6% from last year's total, underscoring the declining patient dynamics in the hep C market. We do not hold in high regards the sales potential of newer, shorter course therapies and feel AbbVie would be better suited focusing on inflammatory disease and oncology as the two largest drivers of revenue and profits going forward.

Role of the Dividend

Due to the uncertain nature of the IP estate protecting Humira and declining hep C market, the main draw of shares of AbbVie at this point is its 4.2% dividend yield. We like the company's dividend

*Is AbbVie...*continued on next page

*Is AbbVie...*from previous page

potential--its Dividend Cushion ratio currently sits just above parity (1)--based on the free cash flow generating potential of its portfolio, but the uncertainty surrounding the driver of 60% of its total revenue adds material risk to the safety of the payout. Should AbbVie fail to protect its blockbuster drug from material sales erosion prior to generating replacement revenue from its pipeline or via label expansions, free cash flow will ultimately falter, limiting the true upside potential of the dividend. Shares are currently changing hands within our fair value range, and we're not interested in taking on the risk of a potential patent cliff to gain exposure to a fairly valued equity.

These Medical Instruments Won't Heal Your Portfolio

The medical instruments industry is a group characterized in part by diversity, and as such, there are ideas of all shapes and sizes. Let's dig into two overvalued companies in the space and what put them in their current positions.

By Alexander J. Poulos and Kris Rosemann

The medical instruments industry has something to offer investors of all strategies. From growth candidates to defensive plays to dividend growth ideas, the medical instruments industry has you covered. However, we're not seeing much valuation opportunity in the medical instruments industry at this point in time. The market's advance post the election of Donald Trump has stretched many companies' valuation metrics past historical norms, and this note intends to highlight two of the most overvalued names in the space. The list is by no means comprehensive but includes two of the most aggressively priced, from our point of view.

Mettler-Toledo (MTD)

Mettler-Toledo is the world's largest manufacturer of weighing devices; its products are used in laboratory, industrial, and food retailing applications. Mettler's reach is widespread through a multitude of diverse industries from precision lab equipment used for the research of new therapeutic products to commercial scales used to weigh heavy-duty trucks, but the most common everyday use of Mettler's scale products is found in grocery store checkout lines via their incorporation into POS systems.

Mettler's share price gains over the past five years have been nothing short of impressive, but one of our primary concerns at this juncture is the lack of meaningful sales growth over the past five years, a

*These Medical Instruments...*continued on next page

*These Medical Instruments…*from previous page

statement that appears to contradict the recent share price action. Though there has been some volatility, Mettler's revenue has advanced a mere 7% since 2012, good for a compound annual growth rate of only ~1.4%, hardly the kind of growth that warrants a price of nearly 28 times the midpoint of 2017 earnings guidance. The inability to meaningfully grow revenue may very well be a sign the end market for Mettler's products is mature, and rapid revenue and profit growth are simply not available. It is our opinion that Mettler should be classified as a low growth company in a mature market, yet shares continue to trade well above the upper bound of our fair value range.

Fueling Mettler's advance has been the company's ability to expand margins. The expansion of margins--it set a quarterly gross margin record in the fourth quarter--coupled with Mettler's share repurchase plan allowed the company to post a double-digit increase in earnings per share in 2016. The stellar increase in the share price not only limits management's ability to continue retiring a similar number of shares, thus restricting the boost to earnings per share figures, but it also makes repurchasing shares an increasingly value-destroying proposition as share prices continue to march higher (any buybacks above our fair value estimate range, we think are value destroying). Mettler spent $500 million on share repurchases in 2016, nearly $60 million more than it was able to generate in cash flow from operations. Clearly, we're not fond of such aggressive value-destroying activity, and the executive team plans to buyback another $500 million in shares in 2017.

Looking ahead to 2017, management is expecting local currency sales growth to be approximately 5.5% over 2016 levels and adjusted earnings per share growth to be 12%-13%. This earnings guidance assumes a $0.31 benefit (roughly 2% of 2016 adjusted earnings per share) from the new accounting standard associated with the tax impact of stock option deductions, but it also reveals expectations for the company's bottom line growth to continue outpacing its sales growth. Mettler is targeting EBIT margin expansion of one percentage point in 2017, a goal that becomes more impressive after considering the recent margin performance the firm has put up. Despite our admiration for Mettler-Toledo's ability to continue expanding margins, there are too many red flags to get us interested in shares at current price levels. Our fair value estimate for shares of Mettler-Toledo currently sits at $317, well below its lofty share price.

Align Technology (ALGN)

*These Medical Instruments…*continued on next page

*These Medical Instruments…*from previous page

Align Technology is another example of a stock whose share have impressed over the past five years. The outperformance has garnered the attention of momentum players who have stretched the company's valuation far above a reasonable, fair value, from our point of view. Align's primary product is the Invisalign Orthodontic system used in place of traditional braces. The advantage of the system is discretion; the system uses near invisible trays to correctly align the patient's teeth. Its target demographic is a teenager with concern placed on 'looks,' as a mouth with metal braces draws unwanted attention, not to mention the embarrassing potential for food to be caught in the braces.

The Invisalign system continues to drive robust revenue gains, more specifically an attractive double-digit annual rate. As revenues continue to push higher, we expect margins to expand thanks to efficiencies of scale, and Align has not disappointed in recent years as its operating margin has grown to just over 23% in 2016 from less than 19% in 2011, while net revenues have advanced more than 75%. However, operating margin peaked at more than 25% in 2014 as currency fluctuations have hurt Align's reported financial performance in the past two years, a negative side effect of the company's international growth efforts. We view currency headwinds as largely transient and their impact is not reflective of the fundamental strength of the business.

Align Technology continues to expect impressive revenue growth moving forward; its long-term operating model calls for annual growth between 15%-25%, which is expected to be driven largely by continued growth in the Invisalign system. Such a target may be in danger of a downward revision after the FDA recently cleared two directly competing products from Dentsply Sirona (XRAY) and 3M (MMM) in early 2017. Management is guiding for 2017 sales growth to be above the midpoint of its long-term operating model despite assuming average selling prices (ASP) to be flat to slightly up from 2016. Align is still the undeniable leader in the invisible braces market, but competition is coming, potentially bringing pricing pressure with it.

Similar to its ASP pricing guidance, operating margins for 2017 are expected to be flat to slightly up compared to 2016 results, and we're not expecting a company that continues to expand as rapidly as Align to pursue considerable margin-expanding initiatives of the cost-cutting variety at this point in time. In fact, strong marketing spending trends can be expected to continue in the near term. The catalyst for shares continues to be overall company growth, but we also like the company's balance sheet as it holds more than $640 million in cash, cash equivalents and marketable securities and no debt as of the end of 2016.

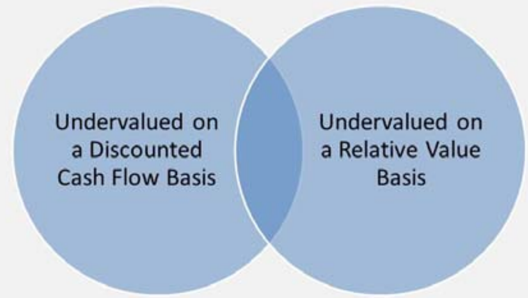
Despite management's expectations for robust growth to continue throughout its business, we see little opportunity to generate alpha via a position in Align Technology. Shares are trading well above the upper bound of our fair value range and are changing hands at more than 33 times 2017 consensus earnings estimates as of this writing. The company offers no income generation via dividend payments, though it is buying back stock, a move we see as significantly value-destructive at this point in time (similar to Mettler-Toledo's situation). Over $96 million was spent on share buybacks in 2016, and the firm has $300 million available under its 2016 repurchase plan that was announced in April.

Investors chomping at the bit for exposure to a unique orthodontic technology appear to have missed the boat on this idea. Management is going to have to continue executing flawlessly to grow into its current valuation, in our view, and we wouldn't be surprised to see shares punished for even the slightest disappointment. Competition may still not yet be a real threat to Align's growth trajectory, but we would like to see management acknowledge the presence of new market entrants some time in the near future, if only to reassure investors that no stone will go unturned in its quest to grow into its overheated valuation. Our fair value estimate for shares of Align Technology is $74, below its share price.

The Watch List

By Valuentum Analysts

The Valuentum Buying Index (VBI), which places a considerable emphasis on a firm's valuation, is the primary driver behind companies 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).



"By overlaying a relative valuation process on a robust forward-looking discounted cash flow valuation methodology, "pure" value investors add an extra degree of conviction to their undervalued ideas. For the ideas in this screen to register the highest rating on the Valuentum Buying Index, however, the market would also have to agree that shares are undervalued, as evidenced by an advancing stock price, one that has good momentum." – Valuentum's Brian Nelson, CFA

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, 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.

Company Name	Symbol	DCF Valuation	Relative Valuation	P/FV	Fair Value Estimate
Supervalu	SVU	UNDERVALUED	ATTRACTIVE	0.48	$10.00
Xerox	XRX	UNDERVALUED	ATTRACTIVE	0.59	$12.00
Omega Healthcare	OHI	UNDERVALUED	ATTRACTIVE	0.60	$48.00
Prudential Financial	PRU	UNDERVALUED	ATTRACTIVE	0.67	$116.00
Viacom	VIA	UNDERVALUED	ATTRACTIVE	0.67	$66.00
CNO Financial	CNO	UNDERVALUED	ATTRACTIVE	0.69	$23.00
Synaptics	SYNA	UNDERVALUED	ATTRACTIVE	0.69	$76.00
Celgene	CELG	UNDERVALUED	ATTRACTIVE	0.70	$141.00
Korn/Ferry	KFY	UNDERVALUED	ATTRACTIVE	0.71	$33.00
Mylan	MYL	UNDERVALUED	ATTRACTIVE	0.72	$53.00
Jabil Circuit	JBL	UNDERVALUED	ATTRACTIVE	0.73	$30.00
Juniper Networks	JNPR	UNDERVALUED	ATTRACTIVE	0.73	$31.00
Buffalo Wild Wings	BWLD	UNDERVALUED	ATTRACTIVE	0.74	$190.00
Super Micro	SMCI	UNDERVALUED	ATTRACTIVE	0.74	$29.00
Express Scripts	ESRX	UNDERVALUED	ATTRACTIVE	0.75	$91.00
MetLife	MET	UNDERVALUED	ATTRACTIVE	0.75	$56.00
Regal Beloit	RBC	UNDERVALUED	ATTRACTIVE	0.75	$76.00
CA Tech	CA	UNDERVALUED	ATTRACTIVE	0.75	$42.00
AIG	AIG	UNDERVALUED	ATTRACTIVE	0.76	$78.00
Red Robin	RRGB	UNDERVALUED	ATTRACTIVE	0.76	$60.00
Hanesbrands Inc	HBI	UNDERVALUED	ATTRACTIVE	0.76	$30.00
Mellanox Tech	MLNX	UNDERVALUED	ATTRACTIVE	0.77	$53.00
Interface	TILE	UNDERVALUED	ATTRACTIVE	0.79	$21.00
CVS Caremark	CVS	UNDERVALUED	ATTRACTIVE	0.79	$103.00
Vitamin Shoppe	VSI	UNDERVALUED	ATTRACTIVE	0.79	$32.00
Cracker Barrel	CBRL	UNDERVALUED	ATTRACTIVE	0.79	$171.00

The price-to-fair value measures reflect the metric at the time of report publishing and may differ from today's metric.

*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.

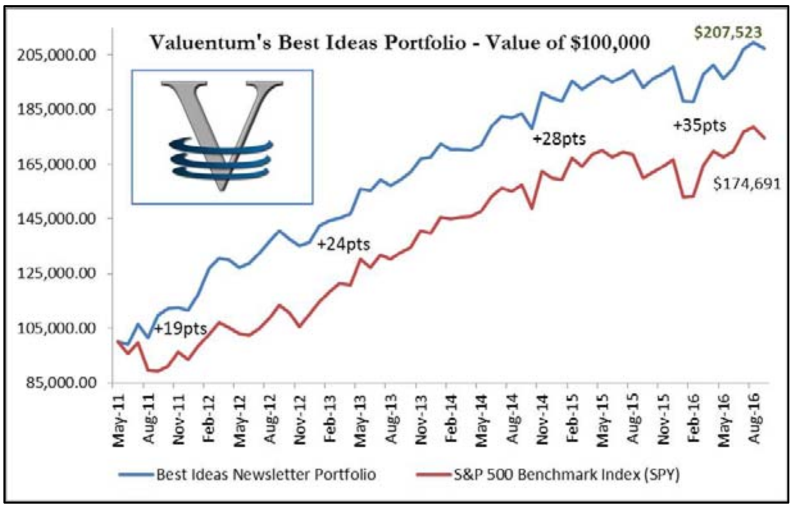
Company Name	Symbol	Sector	Industry	VBI
CVS Caremark	CVS	Consumer Staples	Food Retailers	9
Jabil Circuit	JBL	Information Technology	Electronic Suppliers	9
AIG	AIG	Financials	Insurance - Property & Casualty	8
Prudential Financial	PRU	Financials	Insurance - Life	8

Amphenol Corp	APH	Information Technology	Electronic Suppliers	2
AO Smith Corp	AOS	Industrials	Electrical Equipment - industrial	2
Arch Capital	ACGL	Financials	Insurance - Property & Casualty	2
Bio-Rad	BIO	Health Care	Medical Devices	2
Drew Indust	DW	Industrials	Recreational Vehicles	2
Infinity	IPCC	Financials	Insurance - Property & Casualty	2
Johnson Outdoors Inc	JOUT	Consumer Discretionary	Sporting Goods	2
Lancaster Colony	LANC	Consumer Staples	Food Products	2
Manhattan Associates Inc	MANH	Information Technology	Software	2
MGM Resorts	MGM	Consumer Discretionary	Gaming	2
Natural Resource Partners	NRP	Energy	Industrial Minerals	2
New Oriental Education	EDU	Consumer Discretionary	Education Services	2
Nordson	NDSN	Industrials	Machinery & Tools	2
Northern Trust	NTRS	Financials	Banks & Money Centers	2
Nu Skin	NUS	Consumer Discretionary	Luxury - Established Brands	2
NuVasive	NUVA	Health Care	Medical Instruments	2
South Jersey	SJI	Energy	Utilities	2
State Auto	STFC	Financials	Insurance - Property & Casualty	2
Amazon.com	AMZN	Consumer Discretionary	Internet & Catalog Retail	1
American Electric	AEP	Energy	Utilities - Large	1
Badger Meter	BMI	Industrials	Electrical Equipment	1
Brown-Forman	BF.B	Consumer Staples	Beverages - alcoholic	1
Church & Dwight	CHD	Consumer Staples	Household Products	1
General Mills	GIS	Consumer Staples	Food Products - Large	1
Heartland	HTLD	Industrials	Air Freight & Logistics	1
Hyatt	H	Consumer Discretionary	Hotels	1
IDEX	IEX	Industrials	Machinery & Tools	1
IDEXX	IDXX	Health Care	Diagnostic Substances	1
Illinois Tool Works	ITW	Industrials	Machinery & Tools	1
Jack in the Box	JACK	Consumer Discretionary	Restaurants - Fast Food & Coffee	1
Kraft Heinz	KHC	Consumer Staples	Food Products - Large	1
Lockheed Martin	LMT	Industrials	A&D Prime	1
McDonald's	MCD	Consumer Discretionary	Restaurants - Fast Food & Coffee	1
MSCI	MSCI	Information Technology	Software	1
Neogen	NEOG	Health Care	Diagnostic Substances	1
Northrop Grumman	NOC	Industrials	A&D Prime	1
Quad/Graphics Inc	QUAD	Consumer Discretionary	Book Publishing	1
Rayonier	RYN	Industrials	Building Materials	1
Toro Co	TTC	Industrials	Machinery & Tools	1
Ulta Salon	ULTA	Consumer Discretionary	Personal Services	1

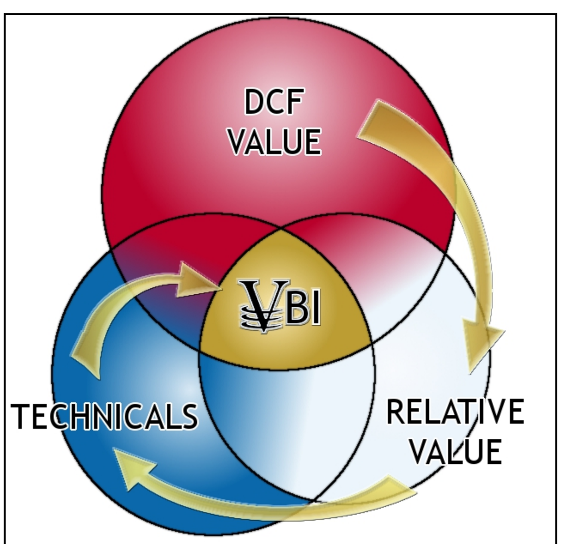
Our Methodology – The Valuentum Buying Index (VBI)

By Valuentum Analysts

At Valuentum, 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 deep-pocketed institutional investors that are interested in the stock for reasons based on their respective investment mandates, the more likely it will be bought and the more likely the price will move higher to converge to its true intrinsic value (buying a stock pushes its price higher). On the other hand, we think the worst stocks will be shunned by most investment disciplines and display expensive valuations, poor technicals and deteriorating momentum indicators.



Stocks that meet our demanding criteria fall in the center of the Venn diagram below, displaying attractive characteristics from a discounted cash-flow basis, a relative value basis, and with respect to a technical and momentum assessment. The size of the circles reveals the relative emphasis we place on each investment consideration, while the arrows display the order of our process -- value first then technicals and momentum last. We may like firms that are undervalued both on a DCF basis and relative value basis, but we won't like firms just because they're currently exhibiting attractive technical or momentum indicators. We're not traders or speculators. We're long-term investors and want to have complete confirmation and conviction in the best ideas we deliver to our subscribers.



Our Methodology – The Valuentum Buying Index continued from previous page

The center of the Venn diagram on the previous page, 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). Because our process factors in a technical and momentum assessment after we evaluate a firm's investment merits via our rigorous DCF and relative-value process, we think we're better able to pinpoint the best entry and exit points on the most undervalued stocks.

Research firms that just focus on valuation may encourage investors to buy a stock all the way down (a falling knife), while those that just use technical and momentum indicators may expose portfolios to significantly overpriced stocks at their peaks. Only when both sides of the investment spectrum are combined can investors get the best stocks on the market today at the best prices, in our view.

Let's examine the chart below, which showcases how the Valuentum process has the greatest profit potential of any investing strategy. The Valuentum process targets adding stocks to actively-managed portfolios when both value and momentum characteristics are "good" and removing them when both value and momentum characteristics are "bad" (blue circles: Buy --> Sell). The Valuentum strategy captures the entire equity pricing cycle, while the value and momentum strategies individually truncate profits.

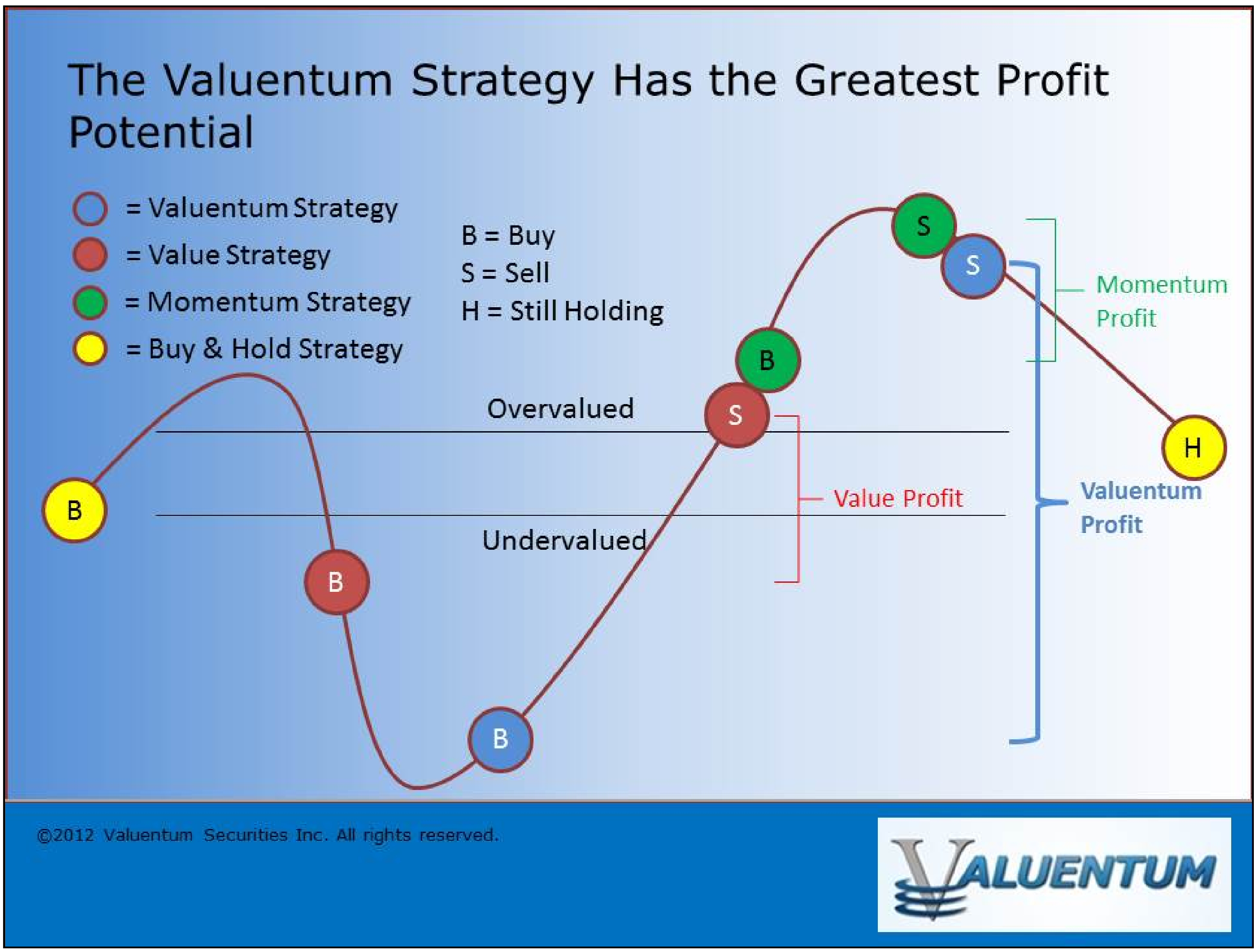


Illustration for educational purposes only.

Our Methodology – The Valuentum Buying Index continued on next page

Our Methodology – The Valuentum Buying Index continued from previous page

Furthermore, Valuentum subscribers are less likely to be involved in value traps because we demand material revenue and earnings growth for firms to earn a 10 on our Valuentum Buying Index. Value traps often occur as a result of secular declines in a firm's products or services, resulting in deteriorating revenue and earnings trends (and a falling stock price). Valuentum subscribers are less likely to be exposed to these "falling knives" since our process requires firms to not only be undervalued but also be exhibiting bullish technical and momentum indicators before we would consider adding them to our actively-managed portfolios.

Since the stock market is a forward-looking mechanism, price usually leads fundamentals. Without a turnaround in price, the risk that the fundamentals of an undervalued stock have not turned for the positive is higher. Where value strategies may encourage the buying of a stock all the way down regardless of whether fundamentals ever turn (red circles: Buy --> Sell), the Valuentum strategy simply steers clear of these situations. We wait for technical improvement in the equity, which often precedes fundamental changes at the company.

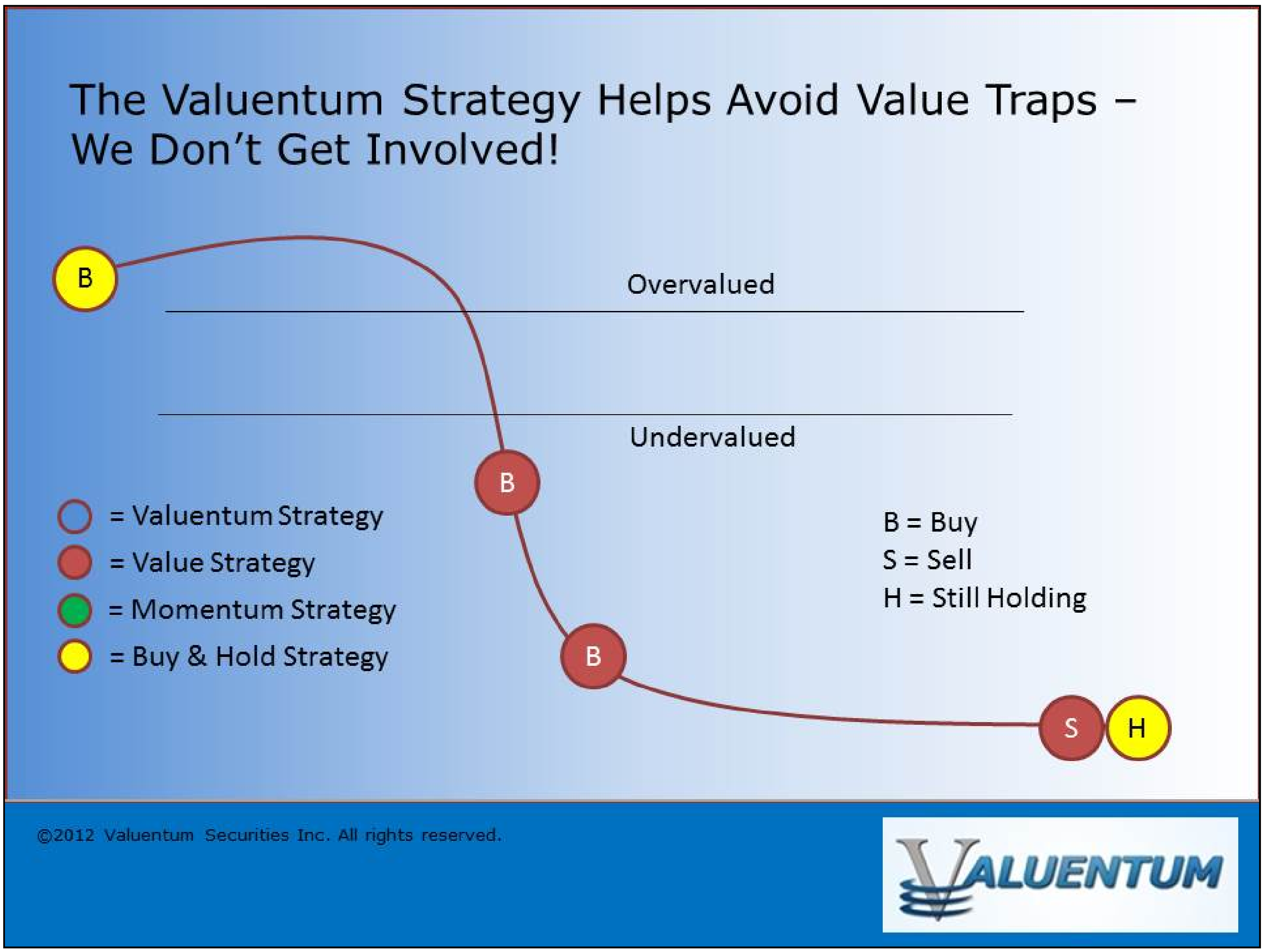


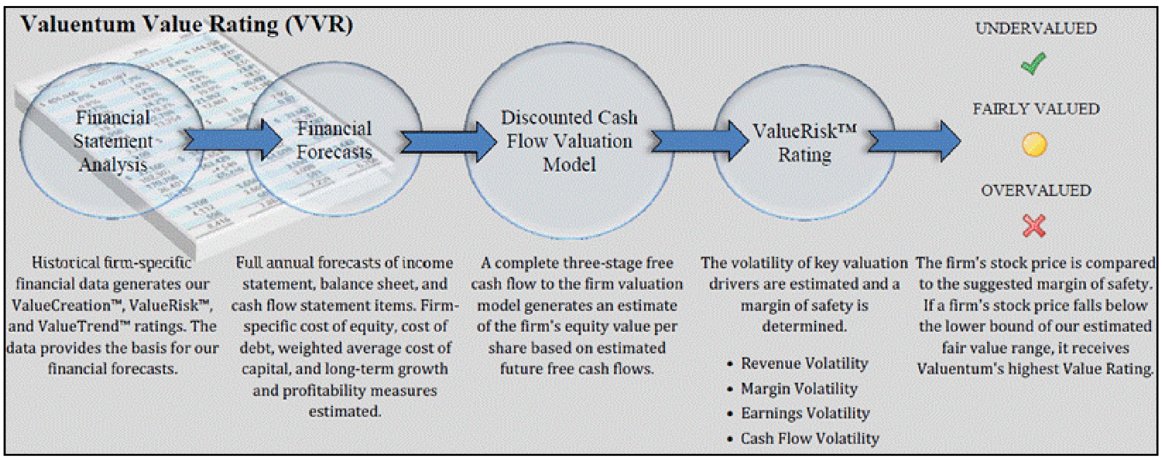
Illustration for educational purposes only.

Our Methodology – The Valuentum Buying Index continued on next page

Our Methodology – The Valuentum Buying Index continued from previous page

I. We Use a Rigorous Discounted Cash Flow Valuation Process

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. We compare a company's return on invested capital (ROIC) to our estimate of its weighted average cost of capital (WACC) to assess whether it is creating economic profit for shareholders (ROIC less WACC equals economic profit). Firms that have improving economic profit spreads over their respective cost of capital score high on our ValueCreation and ValueTrend measures, while firms that have relatively stable returns score well with respect to our ValueRisk evaluation, which impacts our margin-of-safety assessment.



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. A forward-looking Economic Castle rating is then derived.

We then 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.

We think a focus on discounted cash-flow valuation prevents investors from exposing their portfolios to significantly overpriced stocks at their peaks. The chart below reveals how pure momentum investors may expose their portfolios to pricing extremes and dramatic falls (green circles: Buy --> Sell). We stay away from these situations.

Our Methodology – The Valuentum Buying Index continued on next page

Our Methodology – The Valuentum Buying Index continued from previous page

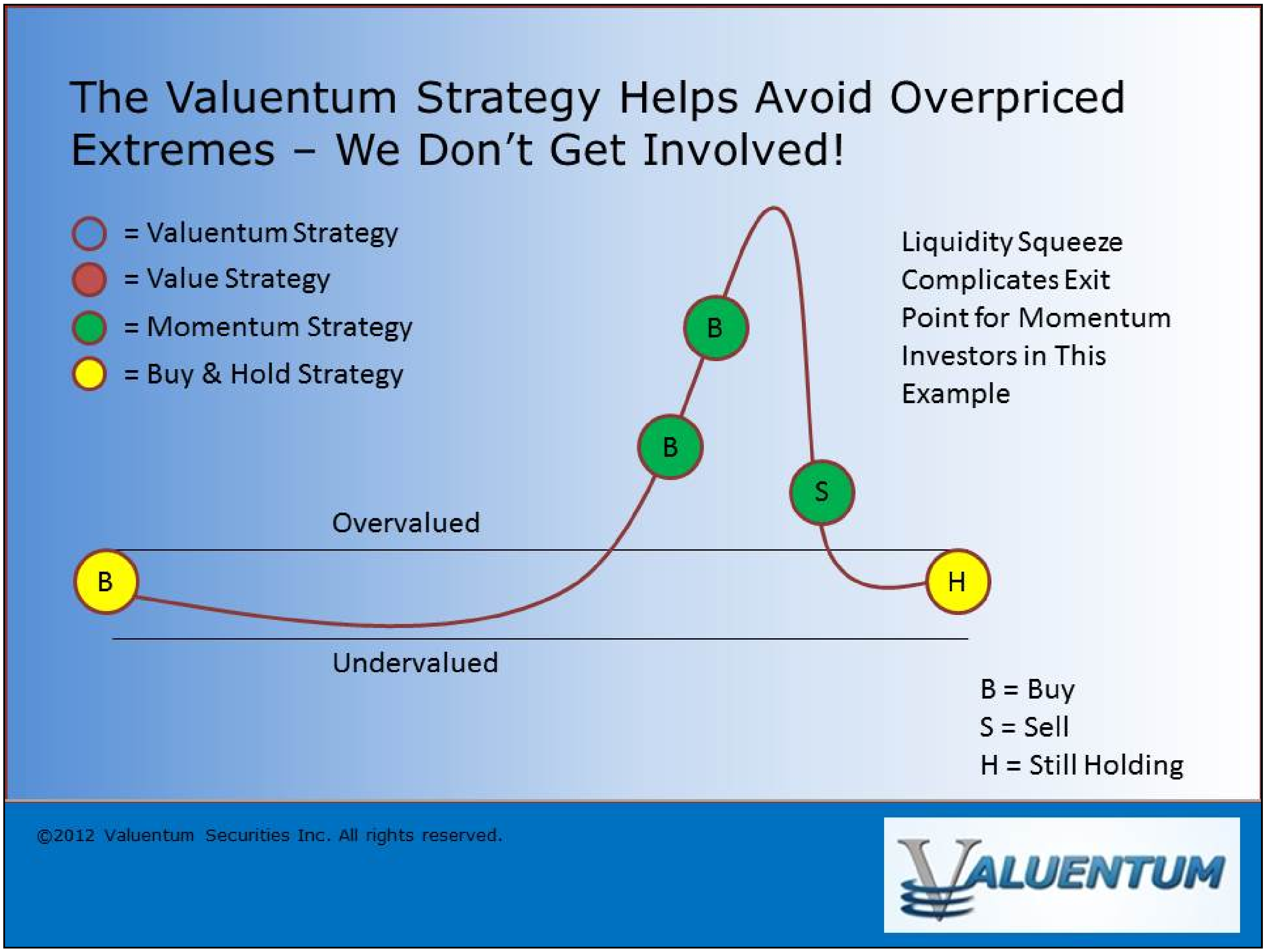


Illustration for educational purposes only.

II. We Perform 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, 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 making buy/sell decisions. 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.

III. We Seek to Avoid Value Traps, Falling Knives 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 whether it has 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 (but only after it meets our stringent

Our Methodology – The Valuentum Buying Index continued on next page

Our Methodology – The Valuentum Buying Index continued from previous page

valuation criteria). Rigorous valuation analysis and technical analysis are not mutually exclusive, and we believe both can be used together to bolster returns. An evaluation of a stock's 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.

We embrace the idea that the future is inherently unpredictable and that not all fundamental factors can be included in a valuation model. By extension, we use technical and momentum analysis to help safeguard us against value traps, falling knives, and the opportunity cost of holding an undervalued equity for years before it converges to fair value. Other research firms do not consider opportunity cost as a legitimate expense for investors.

Putting It All Together - the Valuentum Buying Index

Though the time frame varies depending on each idea, we expect our best ideas to work out over a 12-24 month time horizon (on average) -- any shorter than that is mostly luck, in our view. We tend to add firms to our Best Ideas portfolio when they register a 9 or 10 on our Valuentum Buying Index (VBI) and tend to remove firms from our Best Ideas portfolio when they register a 1 or 2 on our VBI.

We like to maximize profits on every idea, with the understanding that momentum does exist and that prices over and under shoot intrinsic value all of the time. A value strategy (10 --> 5) truncates potential profits, while a momentum strategy (4 --> 1) ignores profits generated via value assessments. We're after the entire profit potential, as shown below.

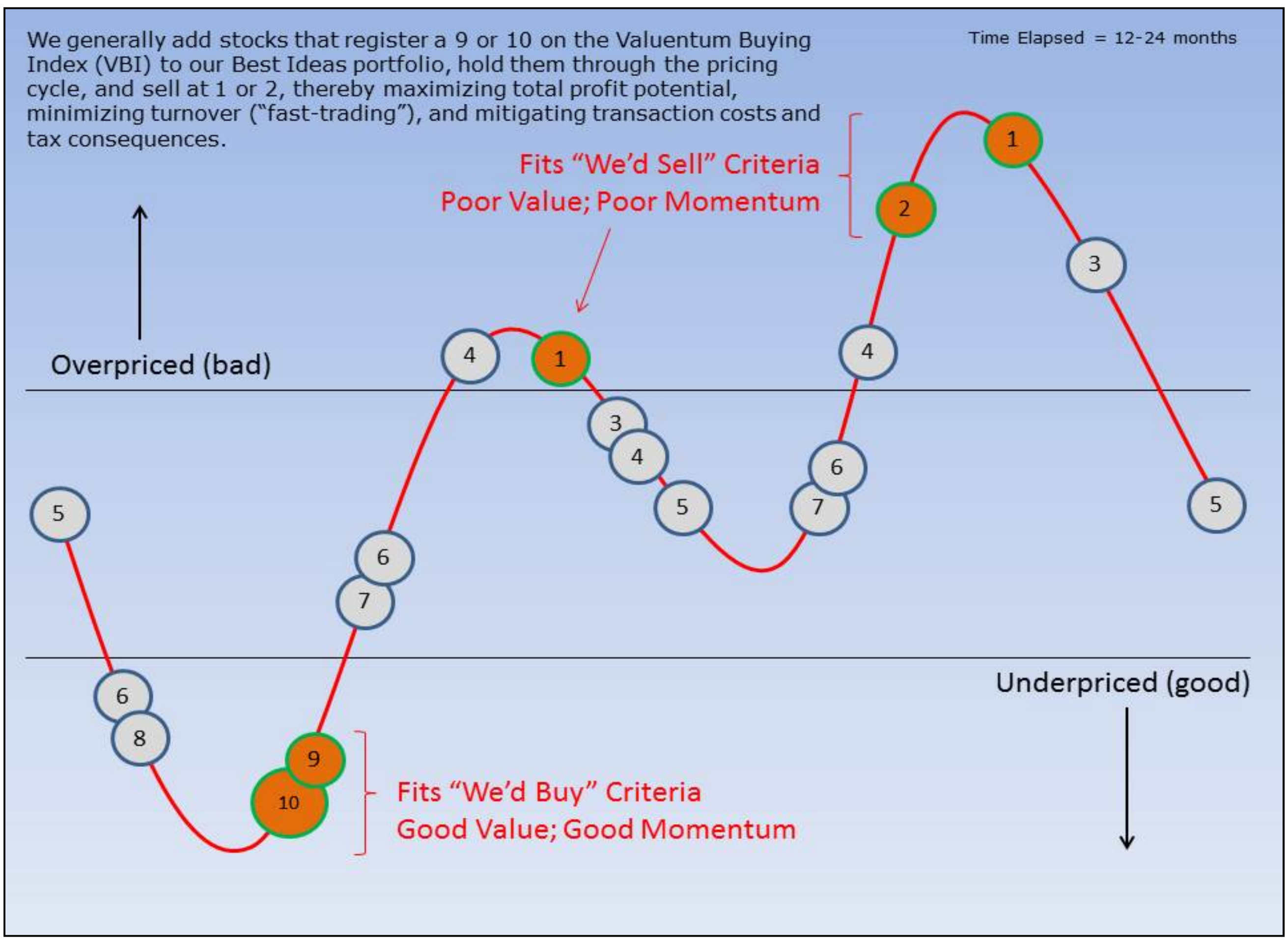


Illustration for educational purposes only.

Our Methodology – The Valuentum Buying Index continued on next page

Our Methodology – The Valuentum Buying Index continued from previous page

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"). Please click here to view an enlarged pdf version. 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 there could be large number of companies garnering either high or low scores, especially at market lows or tops, respectively.

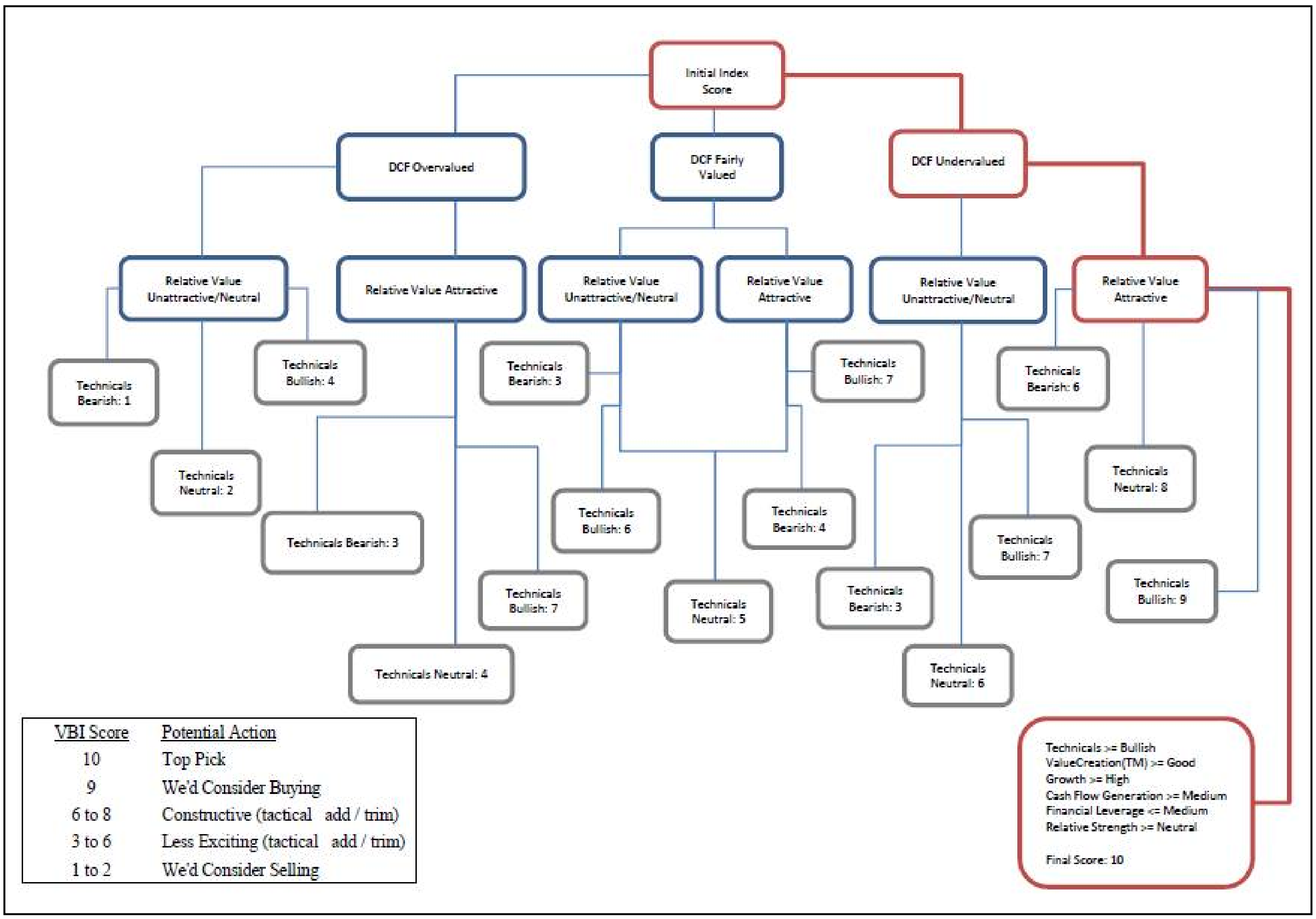


Illustration for educational purposes only.

Our Methodology – The Valuentum Buying Index continued on next page

About the Fair Value Range

By Valuentum Analysts

Understanding the Fair Value Range and Why It's Important

FAQ: Why do you use such a wide fair value range for certain companies?

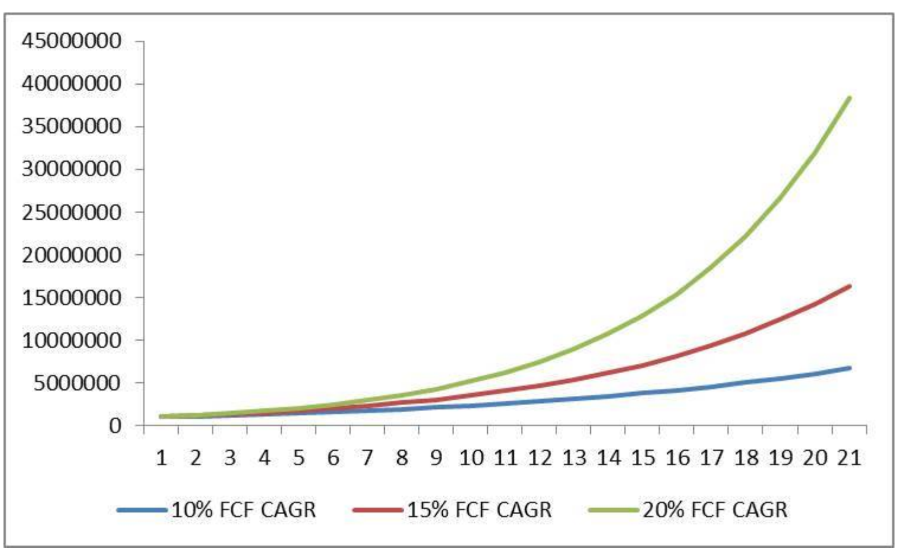
One of the most important concepts of the Valuentum methodology (and valuation in general) is the understanding that the value of a company is a range of probable valuation outcomes, not a single point estimate. Even well-seasoned stock analysts are guilty of saying that a company's shares are worth exactly $25 or a firm's stock is worth exactly $100. The reality is that, in the first case, the company's shares are probably worth somewhere between $20 and $30, and in the latter case, the stock is worth somewhere between $75 and $125.

Why? Because all of the value of a company is generated in the future (future earnings and free cash flow), and the future is inherently unpredictable (unknowable). If the future could be predicted with absolute certainly (knowable), then a stock analyst could say a company's shares are worth precisely this, or that a firm's stock is worth precisely that. Not *because he or she would know where the stock would be trading at*, but because he or she would know precisely what future free cash flows would be (and all other modeling facts-not assumptions in this case) and arrive at the exact and **non-debatable** value of the firm.

But the truth of the matter is that nobody knows the future, and analysts can only estimate what a company's future free cash flow stream will look like. Certain unexpected factors will hurt that free cash flow stream relative to forecasts, while other unexpected factors will boost performance. That's how a downside fair value estimate and an upside fair value estimate is generated, or in the words of Warren Buffett and Benjamin Graham how a "margin of safety" is generated. Only the most likely scenario represents the point fair value estimate. Any stock analyst that says a company is worth a precise figure--whether it's $1 or $100--falls short of understanding one of the most important factors behind valuation.

But why the large range in many cases?

Well, there are many firms in our coverage universe that have a very large range of outcomes in their future free cash flow growth. And because discounting free cash flows is an integral part of calculating the fair value estimate of a company, the range of fair values will also be large. To illustrate this point, let's take a look at the difference between the levels of free cash flows in Year 20 under three different future growth rates: 10%, 15%, and 20%. Though the growth rate between each scenario is but 5 percentage points, the magnitude of the free cash flow difference is astounding many years into the future, and our discounted cash-flow process considers the long-term intrinsic value of firms.



About the Fair Value Range continued on next page

About the Fair Value Range continued from previous page

Under these future free-cash-flow scenarios, if we assume an 8% discount rate and 100,000 shares outstanding (and no debt), the difference in the fair value estimate between the upside case (green line) and downside case (blue line) would be an incredible $68 per share ($82 per share less $14 per share). That's a huge fair value range (80%+), and all because of just a 10 percentage point difference in a future free cash flow growth assumption. For firms that are growing cash flows at 200% or 300% per annum, a large range of fair value outcomes is not only inevitable but also very reasonable. In other words, the Valuentum framework provides an avenue to quantify the upside and downside risks investors are taking in high uncertainty and fast-growing enterprises.

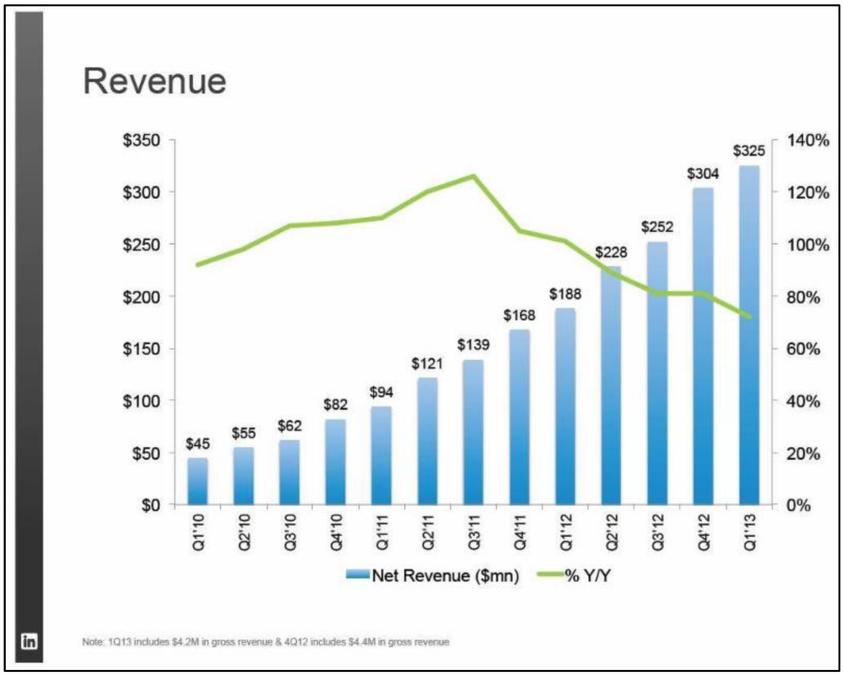


Image Source: LinkedIn

To really hit this point home, shown above is a slide of LinkedIn's (LNKD) revenue from the first quarter of 2010 through the first quarter of 2013. The green line (mapped to the right axis) shows LinkedIn's revenue growth rate. Let's assume revenue expansion translates into similar free cash flow growth expectations (not exactly a precise assumption, given the leverage in LinkedIn's business model), but bear with us for simplistic illustrative purposes. Will LinkedIn's revenue/cash flows expand at a 20% rate, a 40% rate, or a 60% rate (or an even greater pace) through year 20?

It's a very, very difficult question to answer. Remember how significant that 10 percentage point spread was in the hypothetical example above? Well, it's even more significant for LinkedIn. We know LinkedIn's free cash flows will expand, and expand fast, but just how fast is certainly debatable. To a very large extent, that's why LinkedIn's range of probable outcomes (fair value range) is so large. Understanding the cone of fair value outcomes of a company is helpful because the size of the range tends to be positively correlated to the equity's volatility. If you recall, look at what happened to LinkedIn's stock recently when investors ratcheted down their long-term growth assumptions (and by extension, the company's intrinsic value).

Shares collapsed in a huge way.

About the Fair Value Range continued on next page

About the Fair Value Range **continued from previous page**

But it was largely because of that same weakness in equity pricing that drove Microsoft (MSFT) to take the leap to buy LinkedIn's equity outright just a few months later. Over just a very short period of time, LinkedIn's shares effectively collapsed and then surged as the chart below shows (its intrinsic value range didn't change much, however). Having a fair value range that adequately captures both the upside and downside cases for a company's shares remains an integral part of stock investing. Not only does it help hone in on the potential risk-reward profile of an equity at any given time, it also helps reveal the attractiveness of various "entry" or "exit" points using a robust free-cash-flow based and fundamentally-sound intrinsic value estimate as the anchor.

We're scouring our coverage universe for firms that are trading outside of their respective fair value ranges. A firm trading below the low end of its fair value range, for example, is undervalued, while a firm trading above its fair value range is overvalued. The fair value range for each company captures the inherent uncertainty of the trajectory of that firm's unique future free cash flow stream. For the 1,000+ companies we include in our coverage universe, we provide a discounted cash flow derived fair value estimate and a corresponding fair value range -- *and a robust discounted cash-flow process is only one aspect of our service.*

How We Use the Valuentum Buying Index in the Best Ideas Newsletter Portfolio

By Valuentum Analysts

We often receive questions about how we use the Valuentum Buying Index (VBI) rating system, but we think it is equally important to mention that it is only one of the many facets of our website and services. For example, if you haven't checked out the Dividend Cushion ratios on the stocks in your portfolio or the dividend growth product (from individual reports to the newsletter and beyond), surely you are not maximizing your membership! We love dividends, but you can also trust us to make sure you're aware of the real risks of any dividend strategy in today's market.

No matter your strategy or process though, the Valuentum Buying Index rating system is still a helpful tool to have at your disposal, even if you are not using it. Admittedly, the VBI, as we call it, is not as easy to use as 1, 2, 3, or even buying 9s and 10s and selling 1s and 2s until their VBI changes upon the next update. Within any quantitative process, we value the human, qualitative overlay, which captures a wealth of experience and common sense. We want to make sure that we're surfacing the best ideas for members, and flying blind is never a good strategy, in our opinion. With prudence and care, the VBI process is carried out.

In probably one of the most obvious cases, for example, an experienced investor knows when a price-to-earnings (P/E) ratio isn't informative (as in the case of negative or negligible earnings), but a quantitative rating system that uses a P/E ratio, which the VBI does, may not know any better. Of course the VBI has checks and balances to adjust for such instances, but we believe the human, qualitative overlay is still extremely important, especially when considering various business models and unique "un-modelable" risks (particularly with respect to the banks). In our opinion, a golf club is only as good as the player that uses it, and in a similar light, a financial model or a rating system is only as good as the user that applies it.

That said, we stake so much on the performance of the portfolios in the Best Ideas Newsletter and Dividend Growth Newsletter. They represent the outcome of all of the work we do on the website, rolled into one final assessment: our best ideas for each respective strategy. Sure we have other screens on the website, but those are just screens -- listings of companies with similar data and information. The ideas in the portfolios in the Best Ideas Newsletter and Dividend Growth Newsletter have undergone a painstaking process with our analyst team to ensure that we're delivering the very best to members within a portfolio setting. The thoughts behind the weighting of each idea and the portfolio management process revealed in full transparency on a month to month basis may be worth the cost of a membership alone, even if you're not using the portfolios!

Here's why. In a market environment where more than 90% of large-cap funds have trailed the S&P 500 in the 5-year period ending August 31, 2016, the Best Ideas Newsletter portfolio has exceeded the market return by 33 percentage points over a similar time period. Absolutely phenomenal. What's more, we didn't hide behind standard quarterly reviews and updates either, sending out pre-packaged information to members. We showcased this performance in full transparency, and we had to write every single day to capture interest! When patience is the secret to success in investing, do you know how much could have gone wrong when having to produce daily? Obviously, we're very disciplined, but we also credit the portfolio outperformance to the VBI methodology itself.

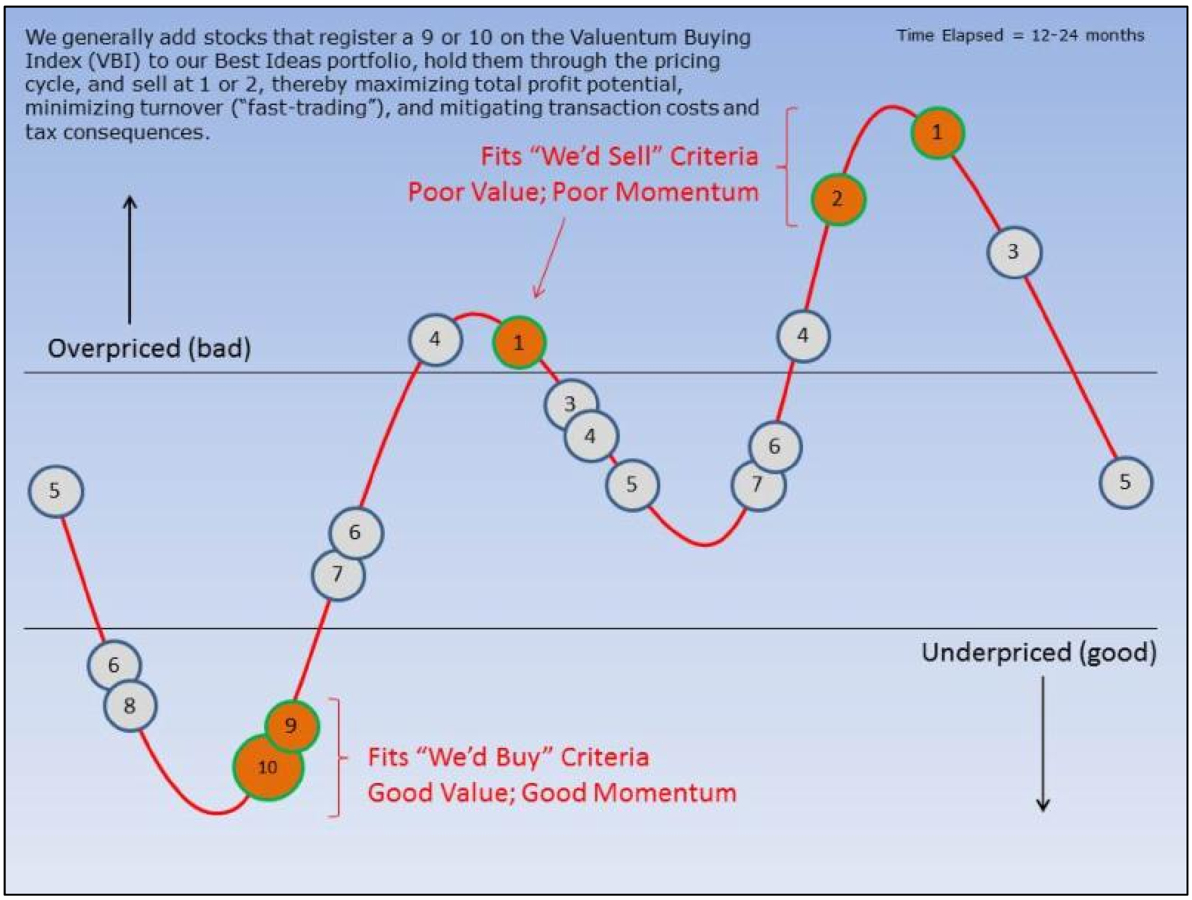
Let's talk about how the VBI helps to inform which ideas we include in the Best Ideas Newsletter portfolio (not the Dividend Growth Newsletter portfolio as additional criteria must be met, namely as it relates to yield and Dividend Cushion ratio). That's such an important word, "informs." Notice how we didn't say "dictate" in this reference. For starters, we've noticed via our statistical backtesting that the momentum factor behind our process tends to be much more pronounced (powerful) over longer periods of time. This was one of the interesting findings of our academic white paper study. We try to replicate this dynamic with the update cycle of our reports (and the time horizon for our ideas to work out). That's why our

*How We Use...*continued on next page

How We Use continued from previous page

reports are updated regularly (generally on a quarterly basis) or after material events and not daily or weekly. Perhaps most practically though, we don't want to whipsaw our membership, nor do we think churn is the way to generate outperformance.

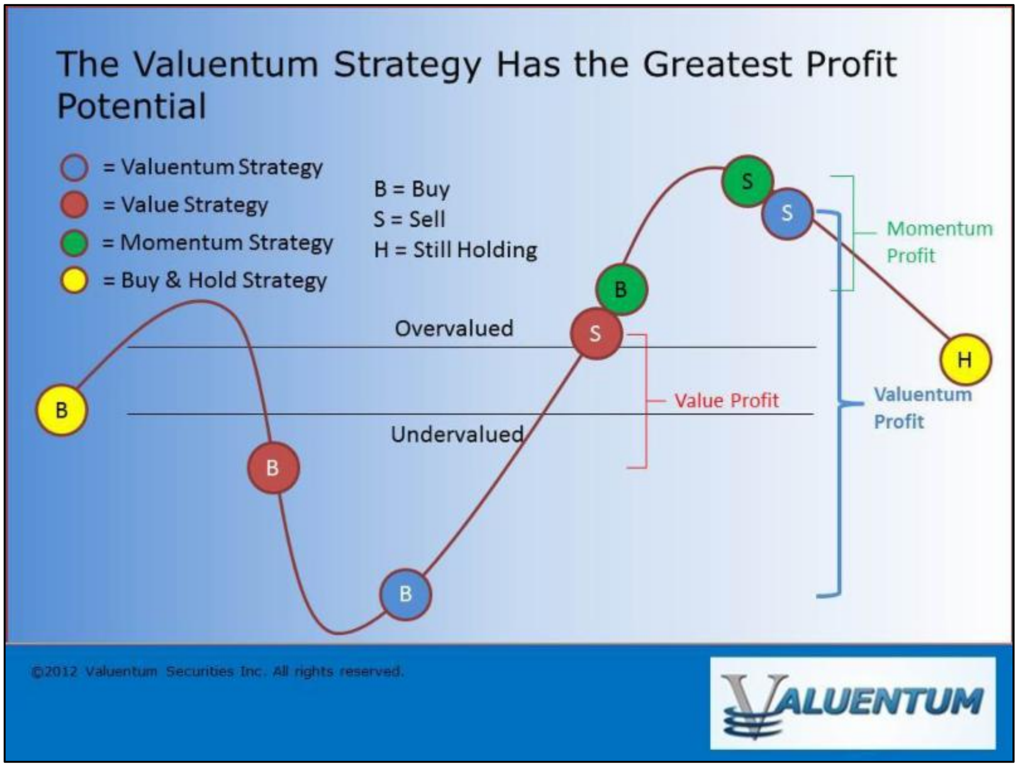
Though the time frame varies depending on each idea that we consider for the Best Ideas Newsletter portfolio, we expect our best ideas to generally work out over a 12-24 month time horizon (on average). Our holding period is targeted to be much, much longer for some ideas in the Dividend Growth Newsletter portfolio, however. Here is where the VBI rating system becomes somewhat more advanced than a simple 1, 2, 3. We tend to add stocks to the Best Ideas Newsletter portfolio when they register a 9 or 10 on the Valuentum Buying Index (VBI), hold them for some time depending on a number of variables (the VBI, market conditions, sector weightings within the portfolio itself), and then we tend to remove stocks from our Best Ideas Newsletter portfolio when they register a 1 or 2 on the VBI. You'll notice that we have a qualitative overlay for the Best Ideas Newsletter portfolio (and one for the Dividend Growth Newsletter portfolio, too, though it is based on dividend-related considerations).



But why don't we churn and burn by updating daily and trading a lot? Obviously, we don't think that's the secret to success. In quite the opposite approach, we like to maximize profits on every idea that we pursue, with the understanding that momentum does exist and that prices over and under shoot intrinsic value all of the time. For example, as shown in the image above, a value strategy (10 --> 5) truncates potential profits, while a momentum strategy (4 --> 1) ignores profits generated via value assessments. At Valuentum, we're after the entire profit potential of each idea. So, for example, if a firm is added to the Best Ideas Newsletter portfolio as a 10 and is removed as a 5, we would have truncated profit potential by not letting it run to lower ratings. Most of our highly-rated Valuentum Buying Index rated stocks have generated the vast outperformance of the Best Ideas portfolio, but these stocks' ratings declined over time as they were held (a good thing -- a declining VBI rating generally means the share price has advanced, assuming all else is well).

*How We Use...*continued on next page

How We Use continued from previous page



Critically, regarding the Valuentum process, as it is executed in the Best Ideas Newsletter portfolio, we do not add all firms that register a 9 or 10, nor do we add the ones we do immediately thereafter. For example, Google (GOOG, GOOGL), now Alphabet, a current Best Ideas Newsletter portfolio holding, registered a 10 on the Valuentum Buying Index, but we remained patient and didn't add the company to our portfolio until after it reported earnings at the time, providing us with an even better entry point (as new information came to light). There are more "structural/timing" instances like the one with Alphabet, for example, that are extremely difficult to capture in any model, and understandably aren't as obvious to those outside looking in.

But why not add every highly-rated stock to the Best Ideas Newsletter portfolio? Think of it as if you were to imagine a value investor not adding and holding every undervalued stock to his/her portfolio. He or she wants the very best ones -- obviously, that means having to leave some good ideas behind. And then, of course, there are always tactical and sector weighting considerations in any portfolio construction, yet another reason why the human touch remains a vital aspect of the Valuentum process. At the core of how we use the VBI in the Best Ideas Newsletter portfolio, however, is a qualitative portfolio management overlay. The VBI rating helps to inform the process, but the Valuentum team makes the allocation decisions of the newsletter portfolio on the basis of a number of other firm-specific and portfolio criteria. Sometimes, under certain market conditions, we may have to relax the VBI criteria entirely in order to achieve newsletter portfolio goals.

Okay, a couple examples. Take pre-split eBay (EBAY), which many years ago included PayPal (PYPL), as an example of our process in action. The stock initially flashed a rating of 10 in late September 2011, and we added it to the Best Ideas Newsletter portfolio. The VBI rating changed to a 6 in December 2011 and then back to a 10 in May 2012, but because the rating never breached a 1 or 2, we did not remove the position from the Best Ideas Newsletter portfolio. In the case of pre-split eBay, we sought to capture the entire pricing cycle and avoided truncating it as most pure value investors often do (and what we would had done, if we had removed the stock at that time). In many ways, pre-split eBay/PayPal has become one of the better examples to use for illustrating the prolonged outperformance driven by undervalued stocks that are beginning to generate good momentum. [We no longer include eBay in the newsletter portfolio, but its split-off PayPal is retained.]

*How We Use...*continued on next page

How We Use **continued from previous page**

There have been more straightforward opportunities in the Best Ideas Newsletter portfolio, too, especially in the case of EDAC Tech, which had tripled since it was added to the newsletter portfolio (never registering below a 9 along the way), and then of course, Apple (APPL), Visa (V) and Altria (MO), but it is usually through the nuances of the process that one truly comes to understand it. The VBI ratings on each stock's most recent 16-page report, downloadable directly from the website at www.valuentum.com, reflect our current opinion on the company. The VBI rating system, as with all methodologies, helps to inform the investment decision process, but in constructing the newsletter portfolio, a qualitative overlay is not only necessary, in our view, but helps to optimize performance. If the returns of the Best Ideas Newsletter portfolio during the past 5+ years are any measure of the VBI rating system, it is performing fantastically well.

About Our Name

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 to momentum investing. And a combination of the two approaches found on each side of the spectrum (value/momentum) in a name couldn't be more representative of what our analysts do here; hence, we're called Valuentum.

Valuentum Best Ideas Newsletter: Volume 7, Issue 2

Valuentum's Best Ideas Newsletter is published monthly. To receive this newsletter on a monthly basis, please subscribe to Valuentum by visiting our website at www.valuentum.com. Or contact us at info@valuentum.com.

Image Source, page 2: https://www.flickr.com/photos/enderst07/4810954845/in/photolist-8k8pgk-2uKyU-91W9FR-7Ww83p-7KFqnJ-2gvJoq-xbBDw-7QpV8y-5YKyQs-5Y5kW-93aPCq-aiEhXH-2Nyvfg-Hi1Bun-58vQCQ-9ncKu8-pqiJNt-bAd4AH-9grzfE-fUnHWJ-2FNUzm-9tQh9o-9tMj4F-9tMiYv-i6cpkf-bvgXuq-9PBH3p-aYFfb-5YpgQU-bTQwfx-oDUmkG-4Dstpc-qyvtPJ-6R5BGh-56eXRT-wTgzo-6CrL7s-bTQwf4-nk92Zb-5DeuzB-dHtrZR-nP133a-MGqW-5JE9tz-a42jmC-qD9gxe-5huQJc-dYLSDd-4rXNeM-9rhvoN