AAII Webinar Series: Investing Like a Stock Superstar

Wayne A. Thorp, CFA

Senior Financial Analyst &

Head of New Product Development

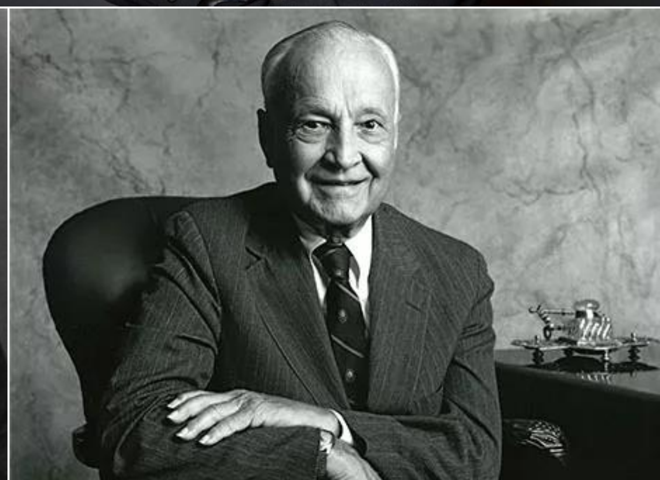
AAII

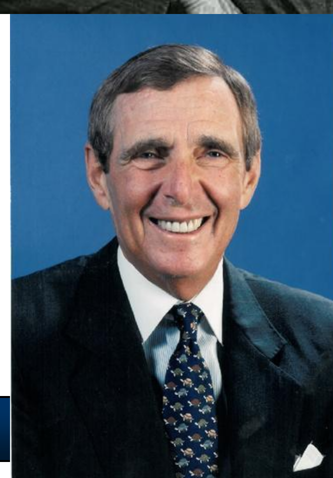
wayne@aaii.com

www.twitter.com/WayneTAAII






AAII Stock Screens

https://www.aaii.com/stockideas/

aaii.com/stockideas/gurus

Guru Screens

AAII has developed 42 different stock selection strategies based on the investment philosophies of such investing "gurus" as Warren Buffett, Benjamin Graham, Kenneth Fischer and William O'Neil.

Performance Data as of 5/29/2020

Performance | Characteristics

Ordered By: Risk Index

Excel | Print

	Guru Strategy	Guru	Factors: V	G	M	S	EE	Y	Q	I	O	Annual Price Gain (%): 2020 YTD	1 Yr	3 Yr	5 Yr	10 Yr	Inc.	Risk Index
☆	O'Shaughnessy: Tiny Titans Screen	Jim O'Shaughnessy	V		M	S						-17.9	16.5	7.6	5.7	8.7	20.5	1.95
★	O'Neil's CAN SLIM Screen	William O'Neil		G	M							5.5	-8.5	-5.0	-2.7	7.1	18.0	1.83
☆	Stock Market Winners Screen	Marc Reinganum	V	G	M							-28.4	-18.2	-1.0	7.7	18.9	17.7	1.41
☆	O'Neil's CAN SLIM Revised 3rd Edition Screen	William O'Neil		G	M							-11.2	-2.6	8.2	12.6	19.8	17.5	1.93
☆	Graham--Enterprising Investor Revised	Benjamin Graham	V					Y	Q	I		-8.9	23.0	-5.1	-1.3	5.1	16.5	1.78
☆	Driehaus Revised Screen	Richard Driehaus		G	M	S	EE					-50.3	-39.2	-18.0	-4.9	7.9	15.0	2.23
★	Neff Screen	John Neff	V	G								-28.2	-15.8	-2.7	-4.0	4.8	13.7	1.67
★	Dreman With Est Revisions Screen	David Dreman	V	G			EE					-16.0	-4.9	1.9	5.1	13.1	13.6	1.49
☆	Piotroski: High F-Score Screen	Joseph Piotroski	V						Q			-45.0	-53.7	-33.4	-25.0	-1.1	13.5	2.12
☆	O'Neil's CAN SLIM No Float Screen	William O'Neil		G	M							-10.0	-5.3	3.1	4.6	9.5	13.3	1.36
☆	O'Shaughnessy: Small Cap Growth & Value Screen	Jim O'Shaughnessy	V		M	S						-37.9	-27.0	-7.2	-2.1	7.4	13.3	1.53
★	Buffett: Hagstrom Screen	Warren Buffett	V	G					Q			-2.5	12.3	4.3	5.8	11.8	12.6	1.12
☆	Lakonishok Screen	Josef Lakonishok	V		M							-22.0	-8.3	-1.5	3.6	9.7	12.2	1.22

AMERICAN ASSOCIATION OF INDIVIDUAL INVESTORS https://www.aaii.com/stocks/scre

aaii.com/stocks/screens/59#passingcompanies

Passing Companies

Stocks That Currently Pass The O'Shaughnessy: Tiny Titans Screening Model

Passing companies as of 6/8/2020. Companies are ranked by Relative Strength 52wk (d)

Print Excel

Company Name	Ticker	Exchange	Market Cap Q1	PE	Price/Sales	Yield	% Rank-Rel Strength 52 week
Atlanticus Holdings Corp	ATLC	M	238.0	9.5	0.5	0.0	98
Centrus Energy Corp	LEU	A	104.1	15.1	0.5	0.0	98
Hovnanian Enterprises, Inc.	HOV	N	149.9	0.0	0.1	0.0	98
Nautilus, Inc.	NLS	N	207.8	0.0	0.6	0.0	97
Moneygram International Inc	MGI	M	211.3	0.0	0.2	0.0	96
Universal Technical Institute, Inc.	UTI	N	244.9	21.8	0.6	0.0	96
Wayside Technology Group, Inc.	WSTG	M	104.5	18.6	0.5	2.7	96
FlexShopper Inc	FPAY	M	36.7	0.0	0.4	0.0	95

aaii.com/stocks/screens/59#passingcompanies

O'Shaughnessy: Tiny Titans Screen ☆

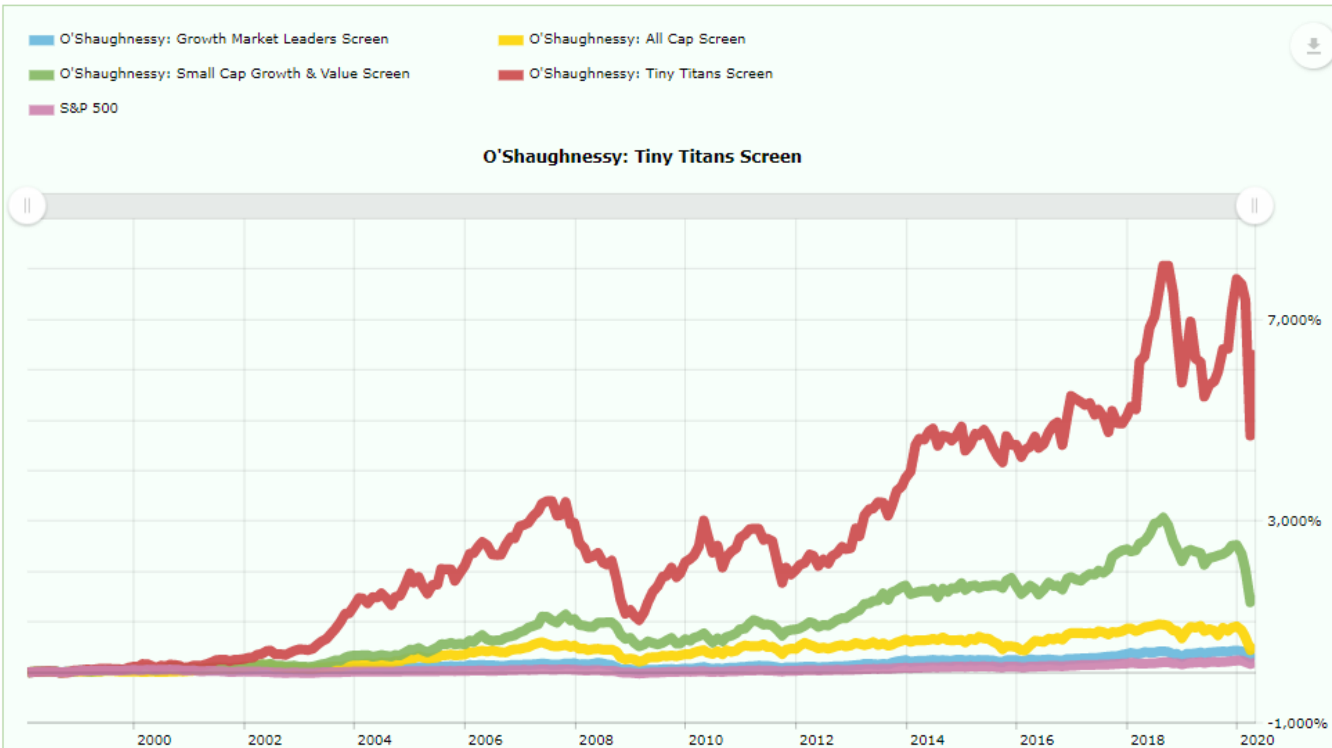
O'Shaughnessy tries to predict the future using historical long-term trends.

Guru
Jim O'Shaughnessy

Factors
Value, Size, Momentum

Strategy Performance | Passing Companies | Learn How To Do It

Strategy Performance



Export Performance Data

	Since Inception	YTD Return	5-Year Return	10-Year Return		
Performance	20.5%	-17.9%	5.7%	8.7%	Avg # of Monthly Holdings	25
+/- S&P 500	+15.3	-12.2	-1.9	-2.1	Turnover %	38.6%

Performance data as of 5/29/2020.

https://www.aaii.com/stocks/scre

aaii.com/stocks/screens/59#learnhow

Learn How To Do It

Invest Using The O'Shaughnessy: Tiny Titans Screening Model

At a Glance

Guru
Jim O'Shaughnessy

Factors
Value, Size, Momentum

YTD Performance
-17.9%

5-Year Performance
5.7%

Performance Since Inception
20.5%

Performance data as of 5/29/2020

O'Shaughnessy tries to predict the future using historical long-term trends.

O'Shaughnessy: Tiny Titans Screen represents AAII's interpretation of the investment approach and is not determined by the original strategist. The list of passing companies represents a hypothetical portfolio, which is used to track the screen's performance on a chart.

Predicting the future of the market is almost impossible, but that doesn't stop investors from trying. In his newest book, "Predicting the Markets of Tomorrow: A Contrarian Investment Strategy for the Next Twenty Years," James O'Shaughnessy argues that investors can predict where the markets are going by simply looking at historical long-term trends.

Through an examination of stock market history, O'Shaughnessy developed four stock selection approaches for individual investors that attempt to take maximum advantage of market trends. He focuses on finding stocks among the various market capitalizations that are most likely to do well based on his research.

O'Shaughnessy studied data dating back to the late 1790s and found that equity markets tend to move in trends of about 20 years. According to this pattern, a 20-year trend began in early 2000 during which greater returns will be earned by small- and mid-cap stocks and large-cap value stocks. The previous 20-year cycle favored large-cap growth stocks, while small- and mid-cap stocks and large-cap value stocks were, on average, underperforming the market.

Featured Stock Superstar: James O'Shaughnessy

James O'Shaughnessy

- Founder & co-chief investment officer of O'Shaughnessy Asset Management (OSAM)
- Prior to founding OSAM, director of systematic equity at Bear Stearns Asset Management and a senior managing director of the firm
- Long recognized as one of America's leading financial experts and a pioneer in quantitative equity analysis
- In February 2009, Forbes.com included Jim in a series on "Legendary Investors" along with Benjamin Graham, Warren Buffett and Peter Lynch
- Author of four books on investing, including "What Works on Wall Street"
- 2019 recipient of AAII's Cloonan Award for Excellence in Investment Education

O’Shaughnessy’s Keys for Successful Investing

1. Find a great strategy
2. Stick with it

Discipline Is Key

- Even the best stock selection strategies will go through periods where they underperform the market
- Having the discipline and perseverance to stay the course through these periods is essential to profiting from these strategies
- Majority of investors fail to beat market averages because they do not follow a disciplined approach

Factor Investing

- O'Shaughnessy is a proponent of "factor investing"
  - Factors are characteristics of stocks that are most indicative of strong total and risk-adjusted returns
  - Calls his methodology "fundamental quant"
- Common investment factors
  - Value
  - Quality
  - Financial Strength
  - Momentum
  - Growth
  - Estimate Revisions

Buy Cheap Stocks

- There is a wealth of academic research and real-world performance that shows value investing outperforms the overall market in the long term
- There are numerous metrics for measuring value, and some fall into and out of favor while others have become less effective over time
  - Initially, O'Shaughnessy found that the price-to-sales ratio was the best single factor for value investors
    - Admits that one of his biggest mistakes was ever labeling a single value factor "king"
  - Accounting rules and structural changes in the market have reduced the efficacy of book value and, thus, price to book
- However, he has since discovered that using multiple factors to build a value "composite" delivers higher, less volatile and more consistent returns

Factor Composites

- By some estimates, there are hundreds or more investment factors
- Individually, these factors fall into and out of favor and have their strengths and weaknesses
- O’Shaughnessy’s research revealed that combining similar factors into a single composite offers better results than any one factor

Value Composite

- O'Shaughnessy put together a Value Composite Score using these factors
  - Price-to-sales ratio
  - Price-earnings ratio
  - Enterprise-value-to-EBITDA ratio
  - Price-to-free-cash-flow ratio
  - Shareholder yield (dividend yield + rate of share repurchases)
- Average the percentile rankings for each factor to arrive at score from 1 to 100
  - Lower the score the better
- AAII added price-to-book-value ratio to its Value Composite
- AAII's Value Composite takes the average of the percentile rankings for these six value factors and then re-ranks the average

Single-Factor vs. Value Composite

U.S. LARGE CAP (Value: Cheapest Quintile) (1963 - 2018)	Arithmetic Average of Excess Total Returns by Period					
	1963-1975	1976-1985	1986-1995	1996-2005	2006-2012	2013-2018
EV/FCF	2.76%	3.28%	5.03%	6.88%	-0.71%	0.74%
P/FCF	2.69%	3.33%	4.87%	6.17%	0.22%	0.66%
P/OCF	3.03%	3.01%	2.28%	5.03%	0.80%	-0.42%
EV/EBITDA	2.29%	3.59%	2.10%	4.12%	0.61%	0.08%
P/E	2.93%	4.76%	0.58%	3.36%	1.09%	0.49%
P/EBITDA	2.06%	2.66%	1.24%	2.96%	1.41%	0.03%
P/S	1.40%	2.70%	0.54%	3.10%	-0.13%	0.44%
P/B	4.29%	1.50%	1.24%	0.94%	-0.35%	-1.71%
AVERAGE: 8 METRICS	**2.68%**	**3.10%**	**2.23%**	**4.07%**	**0.37%**	**0.04%**
COMPOSITE (EW)*	**3.69%**	**4.73%**	**2.88%**	**3.90%**	**0.66%**	**0.41%**

Source: OSAM Calculations.

Quality Matters

- Some stocks are cheap for a reason
- O'Shaughnessy also found that factors can help investors avoid potential traps
  - Avoiding stocks with questionable quality can help you pick better stocks to own
- Created composite scores for earnings quality and financial strength
- Value identifies what to potentially own and "quality" filters out stocks to avoid

Earnings Quality

- Identifies companies that are aggressively reporting or misrepresenting their earnings
- Accounting choices can inflate earnings by delaying expenses or recognizing earnings early
  - Permitted under GAAP but could signal problems with the company
- Companies that are aggressively manipulating their earnings cannot sustain it forever and tend to underperform in the future

Earnings Quality Composite

- O'Shaughnessy put together an Earnings Quality Composite Score using these factors:
  - Current accruals to total assets
  - Change in operating assets
  - Total accruals to total assets
  - Depreciation to capital expenditures
- To make things easier, O'Shaughnessy created a single field
  - (Cash From Operations – Net Income) ÷ Market Cap
- Score from 1 to 100
  - Lower the score the better

Financial Strength

- Whereas Earnings Quality focused on earnings and cash flow, Financial Strength shifts focus to the balance sheet
- If a company cannot meet its (debt) obligations, it will fail, wiping out owners' equity

Financial Strength Composite

- O'Shaughnessy put together a Financial Strength Composite Score using these factors
  - Debt-to-equity ratio
  - Cash-flow-to-debt ratio
  - External financing
  - 1-year change in long-term debt
- As a proxy for cash flow to debt (debt coverage), AAII's uses times interest earned
- Average the percentile rankings for each factor to arrive at score from 1 to 100
  - Higher the score the better

NAVIENT®

Navient Corp. (NAVI) holds the portfolio of education loans insured or federally guaranteed under the Federal Family Education Loan Program (FFELP). It also holds the portfolio of Private Education Loans. It services its own portfolio of education loans, as well as education loans owned by the U.S. Department of Education (ED), financial institutions and nonprofit education lenders. It also provides business processing services to guaranty agencies and colleges and universities.

Value Composite Score

- **Navient Value Score: 16 (1 is best)**
  - Price-to-sales ratio: 37 (0.99)
  - Price-earnings ratio: 7 (5.3)
  - Price-to-book ratio: 24 (0.80)
  - Enterprise-value-to-EBITDA ratio: 98 (129.2)
  - Price-to-free-cash-flow ratio: 5 (1.6)
  - Shareholder yield: 1 (25.8%)

Earnings Quality Score

- **Navient Earnings Quality Score: 87 (100 is best)**
  - (1,284 CFO – 364 NI) ÷ 1,708.6 Mkt Cap
    = 0.538

Financial Strength Score

- **Navient Financial Strength Score: 89 (100 is best)**
  - Debt-to-equity ratio: --
  - Coverage ratio: -- (the company has net operating interest *income*)
  - External financing (Cash from financing ÷ Total assets): 89 (–0.08)
  - Year-over-year change in long-term debt (latest quarter vs. same quarter a year prior): 69 (–7.8%)

Stock Superstars Report (SSR) O'Shaughnessy Portfolio

- O'Shaughnessy's multi-factor screening strategy is the cornerstone for the O'Shaughnessy Portfolio & Watchlist for the Stock Superstars Report
- 10-stock portfolio & watchlist
- Stocks must meet criteria of AAII's O'Shaughnessy screening strategy
- Additional criteria for liquidity
- Qualitative vetting
- Quant-driven sell rules

O'Shaughnessy Portfolio Watchlist

Group 3: O'Shaughnessy Portfoli

stocksuperstars.com//oShaughnessyPortfolio.cfm?ct=9a488883e98a014903498048189f624c9df0e1dd20e6c54c24ccfb1fdf95d...

AAII.com | Home | Latest | Superstars Portfolio | Group 1 O'Neil | Group 2 Dreman | Group 3 O'Shaughnessy | Group 4 Neff | Monthly Report | How To | Subscriptions

Group 3: James O'Shaughnessy Strategy

James O'Shaughnessy is the founder, chairman and chief investment officer of O'Shaughnessy Asset Management, LLC. O'Shaughnessy is considered a pioneer in quantitative equity analysis. O'Shaughnessy has authored several books, including What Works on Wall Street (1997), for which he backtested 44 years of stock market data to find out which quantitative strategies have worked over the years and which haven't.

O'SHAUGHNESSY STRATEGY

Portfolio Holdings | Portfolio Analysis | Portfolio Watchlist | Portfolio News

Data as of 6/5/2020. Delayed up to 15 mins.

Company	Ticker	Sector: Industry	Watchlist Alert		Current Price	Value Score	P/B	P/FCF	P/E	P/S	EV/EBITDA	Shareholder Yield	Financial Strength Score	Earnings Quality Score
			Date	Price										
Gain Capital Holdings Inc	GCAP	Financials: Investment Banking & Brokerage Services	05/29/2020	$6.280	$6.060	2	0.77	1.3	5.1	0.60	na	3.9%	85	88
Abercrombie & Fitch Co.	ANF	Consumer Cyclicals: Retailers - Apparel & Accessories	05/22/2020	$11.180	$14.170	2	0.82	na	na	0.26	3.2	4.8%	63	77
National Western Life Group Inc	NWLI	Financials: Insurance - Life & Health	05/29/2020	$195.930	$215.260	5	0.37	2.2	8.4	1.14	2.4	0.2%	96	82
Bassett Furniture Industries Inc.	BSET	Consumer Cyclicals: Home Furnishings	06/03/2020	$6.730	$9.680	11	0.47	44.1	na	0.19	4.0	4.1%	95	80
Natural Gas Services Group, Inc.	NGS	Energy: Oil & Gas - Related Services and Equipment	05/29/2020	$6.260	$8.000	13	0.40	na	na	1.30	1.9	(0.7%)	95	87
Westlake Chemical Partners LP	WLKP	Basic Materials: Chemicals - Commodity	04/17/2020	$15.470	$22.220	14	1.47	2.3	12.0	0.74	2.8	(0.2%)	86	86
Atlantic Power Corp	AT	Utilities: Utilities - Electric	06/03/2020	$2.150	$2.130	16	na	2.3	na	0.81	8.2	1.6%	81	89
Navient Corp	NAVI	Financials: Consumer Lending	04/30/2020	$7.620	$9.200	16	0.87	1.7	5.7	1.07	129.2	25.3%	89	87
Broadwind Inc	BWEN	Energy: Renewable Energy Equipment & Services	05/29/2020	$2.620	$3.050	19	1.18	3.8	na	0.27	5.3	(5.1%)	92	82

AMERICAN ASSOCIATION OF INDIVIDUAL INVESTORS

$1 Trial for Today's Attendees

http://www.stocksuperstars.com/subscribe/trial1m.cfm

AAII: Stock Superstars

stocksuperstars.com/subscribe/trial1m.cfm

AAII American Association of Individual Investors

☑ YES, give me full 1-month access to *AAII Stock Superstars Report*. **All for only $1.**

My *AAII Stock Superstars* access includes:

- 4 Superstar Guru Portfolios
- Superstar Watchlists for more stock ideas
- Company snapshots, commentaries and more at stocksuperstars.com

Claim your $1 Trial now:

» Click Here to Start the Login/Order Process

You're Fully Protected by Our Money-Back Guarantee!

MONEY-BACK GUARANTEE

Risk-Free Access:

For $1 enjoy all Stock Superstars subscriber benefits for 1 month—read every issue, get access to our complete portfolio, read all the weekly updates, enjoy unlimited access to the subscriber-only website and all the investing tools it offers —and judge for yourself whether or not it's right for you.

If you're not completely thrilled with the service for any reason, simply drop us a note (or give us a call at 1-800-428-2244) and we'll promptly issue you a **100% refund during your trial, no questions asked. You don't risk a single penny and our special report and all subscriber materials are yours to keep.**

Thank You!

Contact me at wayne@aaii.com
with questions or comments
about this presentation

Contact SSR at ssr@aaii.com

Upcoming Webinars:

Register at
www.aaii.com/webinars

Craig Israelsen on Retirement Portfolio Analysis: A Multi-Decade Review

Wednesday, June 17, 2020, 7:30 p.m. CDT

Wayne A. Thorp on Making the Grade: Factor Investing With A+ Investor

Wednesday, June 24, 2020, 7:30 p.m. CDT

Charles Rotblut on Introducing the AAII Way for Creating a Wealth Plan

Wednesday, July 1, 2020, 7:30 p.m. CDT