



The First Cut

Patrick O'Shaughnessy's Millennial Investor Strategy

The First Cut is designed as a starting point for investors. Each issue we list the top stocks that pass relatively simple screens of interest to individual stock pickers. AAI's Stock Investor Pro screening software is used to generate the First Cut listing.

Patrick O'Shaughnessy gives five traits millennial investors should look for in a stock in his book, "Millennial Money: How Young Investors Can Build a Fortune" (Palgrave Macmillan, 2014). Those traits are value, earnings quality, shareholder orientation, return on invested capital (ROIC) and momentum. He says owning stocks with these characteristics will lead to a portfolio that is both unique and performs well over time. He gives a summary of his approach in this issue's Stock Strategies article on page 15.

Rather than requiring absolute values for each criteria (e.g., return on invested capital of at least X%), Patrick uses composite rank scores. A ranking is assigned to each criterion to determine how favorable or unfavorable a company is relative to all other stocks for that characteristic. A composite score is then calculated based on the rankings for each criterion.

Three of the criteria, price-to-free cash flow (a measure of value), 26-week relative price strength (a measure of momentum)

and return on invested capital, are built into AAI's stock screening and fundamental database, *Stock Investor Pro*. Rankings for price-to-free cash flow and relative price strength are also calculated by the program. Cash from operations less net income divided by market capitalization (earnings quality) and cash from financing divided by market capitalization (shareholder orientation) require the use of custom fields.

Calculating the rankings and the composite scores requires the use of a spreadsheet. The list of passing companies was exported to Microsoft Excel. The inverse of price-to-free-cash-flow ranking was calculated to assign higher rankings to the stocks with the lowest valuations for purposes of determining the composite score. Rankings were calculated in Excel for earnings quality, shareholder orientation and return on invested capital. The individual ranks for each criterion were then added together to create a stock's composite score. Higher scores are better.

The universe of stocks was restricted to exchange-listed stocks.

Stocks within the financial sector were excluded because of the structure of their financial statements. Passing stocks were required to have the data necessary for calculating all five criteria and the composite score. These restrictions narrowed the set of available stocks to 1,660. The 25 stocks with the highest composite scores make this issue's First Cut.

Fields for use in *SI Pro* are shown on page 17. You can download instructions for creating the screen and a spreadsheet of the Excel ranking formulas at the online version of this article.

—Charles Rotblut,
CFA, Editor,
AAII Journal

Firms Passing O'Shaughnessy's Millennial Investor Approach Ranked by Composite Score

Company (Ticker)	Value Rank* (%)	Earnings Quality Rank (%)	Shareholder Orientation Rank (%)	ROIC Rank (%)	Momentum Rank (%)	Composite Score	Industry
Otelco (OTEL)	98	98	99	100	56	451	Communications Services
Take-Two Interactive Software (TTWO)	91	82	95	96	81	445	Software & Programming
CYS Investments (CYS)	99	99	100	84	60	442	Real Estate Operations
EDENOR S.A. (ADR) (EDN)	74	98	74	99	91	436	Electric Utilities
American Capital Agency (AGNC)	85	95	100	73	67	420	Real Estate Operations
Paragon Offshore PLC (PGN)	99	99	99	60	62	420	Oil Well Services & Equip
Pampa Energia S.A. (ADR) (PAM)	89	94	44	95	96	418	Electric Utilities
Internet Gold Golden Lines (IGLD)	100	100	100	62	56	418	Communications Services
Amsurg Corp. (AMSG)	89	76	85	90	76	416	Healthcare Facilities
Dynex Capital (DX)	94	96	99	76	49	414	Real Estate Operations
Oci Resources LP (OCIR)	94	85	87	92	56	414	Non-Metallic Mining
Flanigan's Enterprises (BDL)	85	82	91	63	93	414	Restaurants
Transportadora de Gas del Sur (TGS)	74	88	82	78	88	410	Oil & Gas Operations
Spark Energy (SPKE)	93	58	97	99	62	408	Natural Gas Utilities
Envirostar (EVI)	89	90	93	97	32	401	Misc. Capital Goods
Daxor Corp. (DXR)	90	97	97	89	26	398	Medical Equip & Supplies
Argan (AGX)	96	93	27	94	87	397	Construction Services
Weight Watchers Int'l (WTW)	88	71	52	96	89	395	Personal Services
Orbitz Worldwide (OWW)	83	84	52	98	77	394	Recreational Activities
Skilled Healthcare Group (SKH)	88	92	95	26	92	393	Healthcare Facilities
URS Corp. (URS)	87	83	95	42	86	393	Construction Services
Zagg (ZAGG)	89	86	95	29	91	390	Apparel/Accessories
Cablevision Systems Corp. (CVC)	60	85	92	75	78	390	Broadcasting & Cable TV
Verizon Communications (VZ)	70	74	85	89	73	390	Communications Services
HealthSouth Corp. (HLS)	58	74	82	93	81	388	Healthcare Facilities

*Calculated as the inverse of the rank shown in SI Pro, to give stocks with lower valuations higher scores.

Source: AAI's Stock Investor Pro/Thomson Reuters. Data as of 10/10/2014.