AAII Shadow Stock Portfolio: From Theory to Practical Application

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- The Model Shadow Stock Portfolio developed from an attempt to codify the some of the most persuasive academic theories into a set of practical selection and trading rules that an individual investor could follow with minimal effort
- The portfolio has allowed us to share the problems and procedures of managing a portfolio of small stocks using a quantitative approach

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Invest Where You Have the Advantage

- Individuals can take positions in micro-cap stocks without distorting the price
- Individuals can invest in thousands of micro-cap stocks that mutual funds and other institutions cannot touch
- Individuals can time buying and selling to match their tax situation and produce a higher aftertax return

Primary Size Consideration: Market Capitalization

- Market Capitalization (Market Cap): Price per share times the number of shares outstanding
- Common measure of company size
- Represents public consensus of a company’s net worth

Performance by Market Cap

Decile	1926 to 2018 Annual Return (%)	Standard Deviation (%)	Serial Correlation Annual Return	Serial Correlation Ret Above Decile 1	No. of Firms	Largest Stock	% of Total Market Cap	% of Total Cos
1-Largest	9.3	18.8	0.06	--	191	$1,073.4 bil	69.1	6.1
2	10.4	21.4	0.00	0.21	202	$29.02 bil	12.1	6.5
3	10.9	23.2	(0.03)	0.30	192	$13.46 bil	6.2	6.2
4	10.7	25.4	(0.03)	0.26	222	$7.25 bil	4.2	7.1
5	11.2	26.0	(0.03)	0.27	219	$4.50 bil	2.6	7.0
6	11.2	27.0	0.01	0.31	286	$2.99 bil	2.3	9.2
7	11.4	28.9	0.01	0.29	284	$1.96 bil	1.4	9.1
8	11.3	32.7	0.00	0.29	348	$1.29 bil	1.1	11.2
9	11.3	36.8	0.06	0.31	444	$727.8 mil	0.7	14.3
10-Smallest	12.9	42.1	0.14	0.40	725	$312.6 mil	0.3	23.3
Large Cap, S&P 500	10.0	19.8	0.01		500	$1,073.4 bil	80.0	16.1
Mid Cap, Deciles 3-5	10.9	24.3	(0.03)		633	$13.46 bil	13.0	20.3
Small Cap, Deciles 6-8	11.3	28.5	0.01		918	$2.99 bil	4.8	29.5
Micro Cap, Deciles 9-10	11.9	38.5	0.08		1,169	$727.8 mil	1.0	37.6
Treasury Bills	3.3	3.1	0.92					
Inflation	2.9	4.0	0.64					

Source: Duff & Phelps, Morningstar

Time Frame and Performance

	Percentage of Holding Periods That Resulted in Better Performance (1926 to 2019)		(2000 to 2019)	
Holding Period	Small Cap Outperform	Large Cap Outperform	Small Cap Outperform	Large Cap Outperform
1 Month	50% (563)	50% (565)	52% (125)	48% (115)
5 Year	56% (598)	44% (471)	59% (106)	41% (75)
10 Year	68% (686)	32% (323)	74% (89)	26% (32)
20 Year	88% (779)	12% (110)	100% (1)	0% (0)
30 Year	96% (740)	4% (29)		

Source: Morningstar, "Stocks, Bonds, Bills and Inflation," Chicago.

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Primary Size Consideration: Market Capitalization

- Investable universe: Stocks in the lowest 10% of market cap as defined by NYSE-listed companies
  - NYSE-listed stocks used to establish market cap levels
- Currently buy NYSE, Nasdaq and Amex-listed stocks with market cap below $300 million
  - Original cutoff: $55 million in 1993
  - Highest cutoff: $300 million since December 2013

Secondary Size Consideration: Liquidity

- Only interested in stocks that have an adequate market for us to take a position
  - Avoid stocks in danger of being delisted
- Currently buy stocks with a minimum market cap of $30 million
  - Original minimum of $10 million in 1993
  - Current minimum of $30 since December 2012
- No OTC stocks (bulletin board or pink sheets)

Secondary Size Consideration: Liquidity

- Minimum share price of $4
- Use limit orders to control buy/sell prices
- Be cautious of stocks with average daily trading volume that is less than 10x the amount needed for your position

Primary Value Consideration: Price-to-Book-Value Ratio

- Book Value = Assets – Liabilities
  - Also called shareholder's equity
- Price-to-Book Value: Relates market's assessment of company's net worth to accounting measure of company's net worth
- Financial structures of all industries not comparable; most studies with book value exclude financial stocks
  - Shadow Stock Portfolio excludes financial sector

Primary Value Consideration: Price-to-Book-Value Ratio

- Book value based on historical accounting measures
  - Items of real and substantial value may not appear on the balance sheet (i.e., customer loyalty, copyrights, patents, etc.)
  - Historical, depreciated value of items carried on book may not reflect the current market value or replacement value
  - Share repurchases may also lower book value

Primary Value Consideration: Price-to-Book-Value Ratio

- Price-to-book-value ratio works because, on average, over a number of companies and a number of years, accounting book value is a “close-enough” estimate of economic value
- The smaller the market cap, the higher the future return

Primary Value Consideration: Price-to-Book-Value Ratio

- The lower the price-to-book ratio, the higher the future return
  - Ratio worked well independently and with small caps
  - Price-to-book ratio better predictor than price-earnings ratio

Primary Value Consideration: Price-to-Book-Value Ratio

	Average Monthly Returns (July 1963 to December 1990) (%)										
		High			Price-to-Book-Value Ratio						Low
	All	1	2	3	4	5	6	7	8	9	10
All Stocks	**1.23**	**0.64**	**0.98**	**1.06**	**1.17**	**1.24**	**1.26**	**1.39**	**1.40**	**1.50**	**1.63**
Size Deciles											
1-Largest	**0.89**	0.93	0.88	0.84	0.71	0.79	0.83	0.81	0.96	0.97	**1.18**
2	**0.95**	0.44	0.89	0.92	1.00	1.05	0.93	0.82	1.11	1.04	**1.22**
3	**1.08**	0.66	1.13	0.91	0.95	0.99	1.01	1.15	1.05	1.29	**1.55**
4	**1.07**	0.95	1.00	0.99	0.83	0.99	1.13	0.99	1.16	1.10	**1.47**
5	**1.15**	0.70	0.98	1.14	1.23	0.94	1.27	1.19	1.19	1.24	**1.50**
6	**1.24**	0.88	0.65	1.08	1.47	1.13	1.43	1.44	1.26	1.52	**1.49**
7	**1.19**	0.39	0.72	1.06	1.36	1.13	1.21	1.34	1.59	1.51	**1.47**
8	**1.22**	0.56	0.88	1.23	0.95	1.36	1.30	1.30	1.40	1.54	**1.60**
9	**1.22**	0.43	1.05	0.96	1.19	1.33	1.19	1.58	1.28	1.43	**1.79**
10-Smallest	**1.47**	**0.70**	**1.14**	**1.20**	**1.43**	**1.56**	**1.51**	**1.70**	**1.71**	**1.82**	**1.92**

Source: The Cross-Section of Expected Stock Returns, Eugene Fama & Kenneth French, The Journal of Finance, June 1992

Primary Value Consideration: Price-to-Book-Value Ratio

- Buy stocks with price-to-book-value ratio in the bottom 10%
  - Currently, maximum P/B is 0.90
    - Original cutoff of 0.61 in 1993
    - Lowest cutoff of 0.60 from August 2000 to October 2003
    - Highest cutoff of 1.00 from June 2015 to October 2019
  - S&P 500 P/B:
    - Currently: 3.53; Year Ago: 3.50 (Barron's)
- Rank stocks by P/B

Secondary Value Consideration: Price-to-Sales Ratio

- Current price divided by the sales per share over the most recent 12 months
- Many feel that sales are not as influenced (as earnings or book value might be) by the many management assumptions trickling through the accounting books
- The price-to-sales ratio can provide a meaningful valuation tool when negative earnings render earnings-based models useless

Secondary Value Consideration: Price-to-Sales Ratio

- Stocks and industries with normally high profit margins trade with higher price-to-sales ratios
  - Using a static cutoff, such as price-to-sales ratio below 1.2, may always exclude certain industries even if out-of-favor based upon other value measures
  - Some investors vary price-to-sales ratio cutoffs based upon growth cycle and/or profit margins

Secondary Value Consideration: Price-to-Sales Ratio

- Price-to-sales ratio works as overall predictor of performance, but may overlook high-margin businesses

Secondary Value Consideration: Price-to-Sales Ratio

- Buy: Price-to-sales ratio must be less than 1.2
  - Established as a filter on August 1996
    - Original cutoff: 0.54 (August 1996)
    - Highest cutoff: 1.2 (November 2003 to present)
  - "Super Stocks," by Kenneth L. Fisher, Dow Jones
  - Financial Analysts Journal, March/April 1996: "Do Sales-Price and Debt-Equity Explain Stock Returns Better Than Book-Market and Firm Size?"
  - "What Works on Wall Street: A Guide to the Best-Performing Investment Strategies of All Time," by James P. O'Shaughnessy, McGraw-Hill

Levels of Key Factors Over Time

Period Ending	Maximum Value of Lowest (10th) NYSE Decile: Market Cap ($ Mil)	Maximum Value of Lowest (10th) NYSE Decile: Price-to-Book-Value (X)	Maximum Values for Shadow Stock Candidates: Market Cap ($ Mil)	Maximum Values for Shadow Stock Candidates: Price-to-Book-Value (X)	Maximum Values for Shadow Stock Candidates: Price-to-Sales (X)
Jun 1993	60	0.85	55	0.61	--
Dec 1993	66	0.99	55	0.61	--
Dec 1994	60	0.87	60	0.65	--
Dec 1995	81	0.95	60	0.65	--
Dec 1996	93	1.01	100	0.70	0.54
Dec 1997	123	1.13	125	0.85	0.54
Dec 1998	100	0.82	125	0.85	1.00
Dec 1999	95	0.65	125	0.85	1.00
Dec 2000	90	0.50	125	0.85	1.00
Dec 2001	115	0.73	125	0.60	1.00
Dec 2002	130	0.68	125	0.60	1.00
Dec 2003	243	1.02	125	0.70	1.20
Dec 2004	300	1.20	200	0.80	1.20
Dec 2005	310	1.09	200	0.80	1.20
Dec 2006	380	1.19	200	0.80	1.20
Dec 2007	303	0.84	200	0.85	1.20
Dec 2008	127	0.52	200	0.80	1.20
Dec 2009	230	0.79	200	0.80	1.20
Dec 2010	287	0.93	200	0.80	1.20
Dec 2011	238	0.76	200	0.80	1.20
Dec 2012	266	0.85	240	0.80	1.20
Dec 2013	385	1.06	300	0.80	1.20
Dec 2014	326	0.94	300	0.80	1.20
Dec 2015	249	0.77	300	1.00	1.20
Dec 2016	370	1.04	400	1.00	1.20
Dec 2017	387	1.00	400	1.00	1.20
Dec 2018	276	0.72	400	1.00	1.20
Dec 2019	305	0.86	300	0.90	1.20
Jul 2020	312	0.70	300	0.90	1.20

Source: Kenneth R. French, AAII's Stock Investor Pro. Data as of 7/21/2019.

Shadow Stock Financial Considerations

- Positive earnings from continuing operations over the last quarter and trailing 12 months (last 4 quarters)
  - When available, consensus estimates must also be positive for current quarter and year
- Avoid any stock that was sold from the portfolio in the last two years
  - Avoid marginal stocks that are forever marginal, creating high transaction costs
  - Avoid cyclical stocks going from profits, to losses, to profits, etc.

Shadow Stock Financial Considerations

- Avoid stocks not listed on U.S. exchanges and Chinese firms
  - Potential for different accounting procedures
  - Withholding taxes on dividends
- Avoid financial stocks, leasing & rental companies, REITs & limited partnerships, etc.
  - High levels of acceptable liabilities make it difficult to make meaningful comparisons of popular ratios
- Avoid companies that have not filed a quarterly SEC report (10-Q) in last six months

Building Your Shadow Stock Portfolio: Placing Trades

- Exercise care if the average daily volume is not 10x the amount needed for your position
  - It will be difficult (costly) to build or sell position
  - You may need to slowly move in & out of position
- If necessary, build a position gradually. With low/zero commissions, it is often better to place partial orders than to try to establish a large position all at once

- Avg. Daily Volume: 352,256
  - \$5,000 ÷ \$7.34 = ~680 shares × 10 = 6,800 minimum daily volume
  - 352,256 ÷ 10 = ~35,200 shares maximum supported position
  - 35,200 × \$7.34 = \$258,368 maximum dollar position

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Use Limit Orders for Buy & Sell Trades

- If the quoted bid-ask spread is more than 2% (ask price minus bid price, divided by ask price), try to place a limit order between the bid and ask price to keep the transaction cost low
- If bid-ask spread is less than 2%, place limit orders at the ask for a buy and at the bid for sell

Portfolio Construction

- 10-stock portfolio: minimum number of holdings
- 15 to 20 stocks: $100,0000 to $1 million
- 25+ stocks: Over $1 million
- Try to invest equal dollar amounts in each security
- If building a portfolio slowly by adding stocks over time, try to establish positions that will represent desired portfolio percentage

Knowing When to Sell

- Sell process just as important as buy process
- Investors tend to sell winning positions too quickly & hold onto losing positions for too long
  - Investors hate to give up some of the gain from a winner and would rather lock in a small profit than hold on for larger gain, but risk giving up some of the profit
  - Investors like to hold onto losing positions to try and break even

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Knowing When to Sell

- Rules help to overcome emotions
  - Sell when stock is no longer attractive and better opportunities are available
  - Consider rebalancing when positions put portfolio way out of balance
  - Shadow Stock Portfolio sell rules (value & size) normally keep positions from getting too large for very long

Shadow Stock Portfolio Sell Rules

- **Price-to-book-value ratio** > 3x current buy factor
  - 3 × 0.9 = 2.7
  - Sell if there are suitable replacements
- **Market cap** > 3x current buy factor
  - 3 × \$300 mil = \$900 million
  - Sell if there are suitable replacements
- **Adjusted EPS 12m** < \$0
  - Not GAAP earnings
  - Stock placed on probation when quarterly results push trailing EPS negative
  - If subsequent quarter has negative EPS while trailing EPS still negative, stock is sold
    - If subsequent quarterly EPS is positive but trailing EPS is negative, stock remains on probation
  - **Sell even if no suitable replacements**
- Sell holdings **older than four years**, unless up more than 40% since purchase (~10% annual gain)
  - Sell if there are suitable replacements

Shadow Stock Portfolio Management Rules

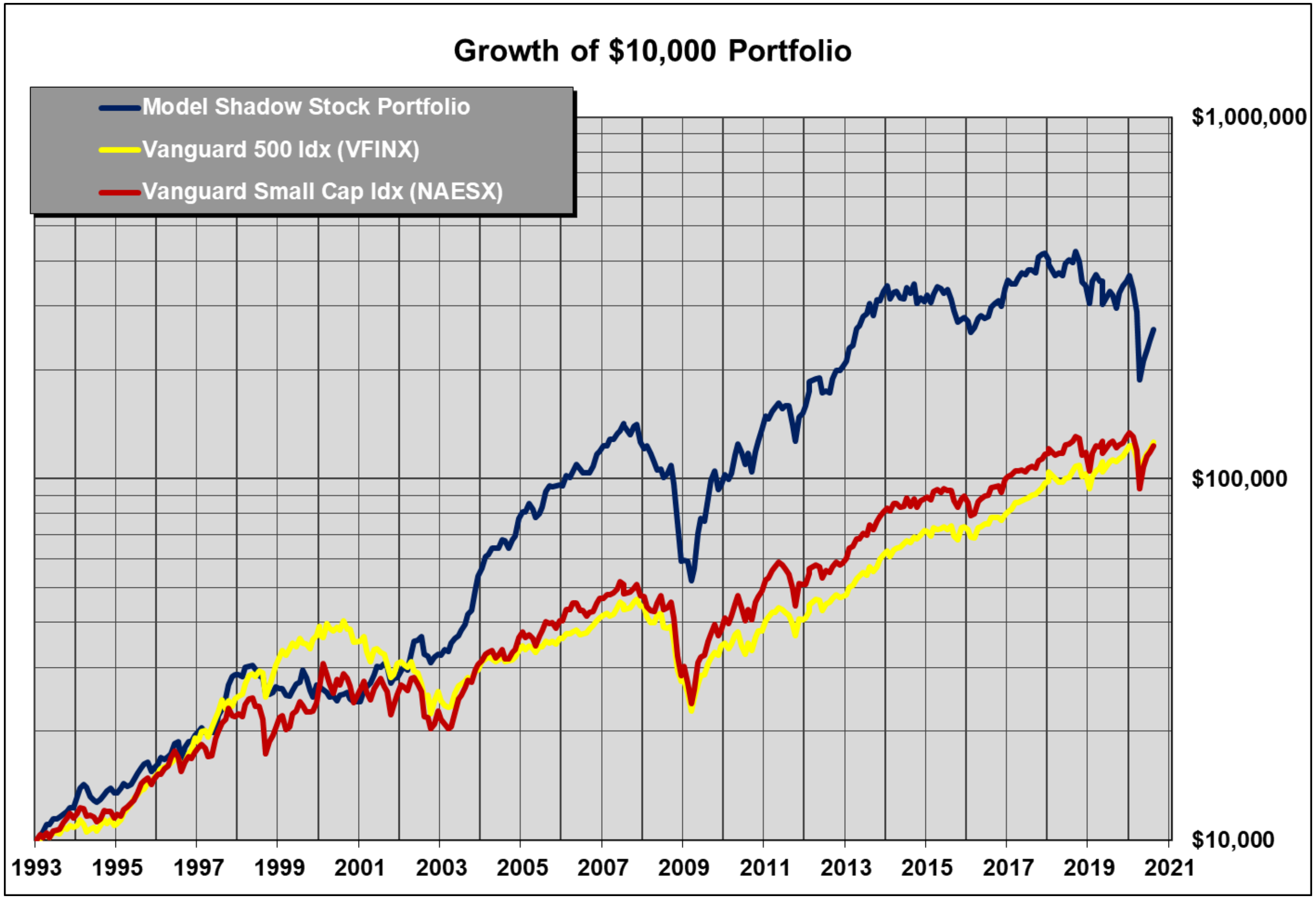
- Decisions are made at the end of the quarter once the earnings results have been announced
  - Typically in late February, May, August & November
- Use best judgment for mergers/tenders, but still follow rules
- Best to focus on transaction costs
  - Give preference to stocks with lower bid-ask spreads

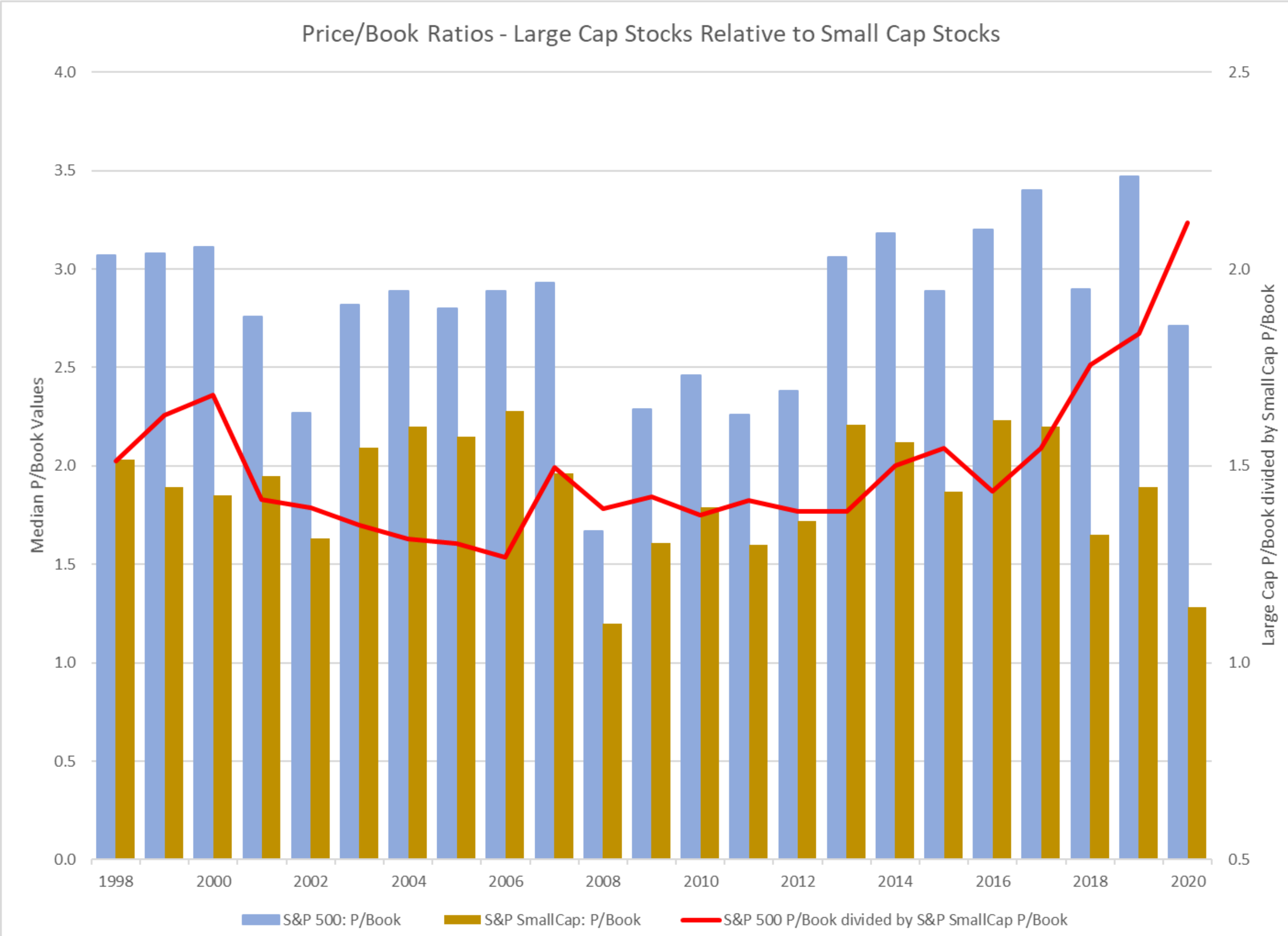
Shadow Stock Portfolio Management Rules

- If proceeds from stocks sold are greater than required to buy average position of all qualified stocks:
  - Invest average portfolio position in qualified stocks
  - Keep up to 5% of portfolio in cash
  - Distribute excess of 5% among underweighted positions that still qualify as buys
  - If over 10% of the portfolio is in cash, the price-to-book-value ratio can be raised

Year	Model Shadow Stock Portfolio	Vanguard 500 Index (VFINX)	Vanguard Small Cap Index (NAESX)
1993	32.3	9.9	18.7
1994	2.0	1.2	(0.5)
1995	20.7	37.4	28.7
1996	22.3	22.9	18.1
1997	44.3	33.2	24.6
1998	(8.9)	28.6	(2.6)
1999	(0.0)	21.1	23.1
2000	(7.7)	(9.1)	(2.7)
2001	21.4	(12.0)	3.1
2002	10.8	(22.1)	(20.0)
2003	73.1	28.5	45.6
2004	43.7	10.8	19.9
2005	17.9	4.8	7.4
2006	29.4	15.6	15.6
2007	(1.8)	5.4	1.2
2008	(50.8)	(37.0)	(36.0)
2009	72.3	26.5	36.1
2010	45.4	14.9	27.7
2011	6.3	2.0	(2.8)
2012	33.3	15.8	18.0
2013	61.0	32.2	37.6
2014	(5.8)	13.5	7.4
2015	(15.2)	1.3	(3.8)
2016	29.8	11.8	18.2
2017	14.0	21.7	16.1
2018	(24.4)	(4.5)	(10.5)
2019	19.6	31.3	27.2
YTD*	(29.1)	2.2	(8.2)
Inception	**12.5**	**9.6**	**9.5**

**Through Jul 21, 2020.*





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Keep a Long-Term Perspective

- Micro-cap stocks tend to have consecutive periods of overperformance and then underperformance
- Micro-cap stocks have more volatility than large-cap stocks; important to maintain diversified portfolio and consider all asset classes and foreign markets as well as domestic markets

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Keep a Long-Term Perspective

- Maintain reasonable expectations
- Market is reasonably efficient, but not in the academic sense that all information is instantaneously reflected in prices of all stocks. Nevertheless, information will eventually lead to stock price adjustments
  - Adjustments quicker for large caps than micro caps

Keys to Long-Term Success

- To succeed with the Shadow Stock approach:
  - Need enough time to manage a stock portfolio
    - Approach designed so that it only needs a careful examination quarterly, perhaps an 8-hour commitment
    - If one has time, the portfolio can be reviewed monthly to keep up to date on earnings and company news
  - Need an interest in managing a portfolio—in good times and bad
  - Need discipline to follow the program once you have committed to it
  - Important to control turnover with micro-cap stocks

AAII Resources

- Home page for AAII Model Shadow Stock Portfolio

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Welcome to AAII Shadow Stocks

July Model Shadow Stock Portfolio Update

Next Wednesday, July 22, at 7:30 p.m. CDT, AAII president John Bajkowski will host a webinar on the Model Shadow Stock Portfolio. To register, click here.

Eleven stocks met the initial selection criteria for the Model Shadow Stock Portfolio as of July 13, 2020, up from eight passing stocks one month ago. AAII members can see and research which companies are currently passing the initial selection criteria in the Shadow Stock Ideas table on AAII.com. The list of Shadow Stock Ideas is updated daily—Tuesday through Saturday.

Read more

Latest Journal Commentary:

Model Shadow Stock Portfolio Chooses From Small Pool of Qualifying Stocks

A rising stock market combined with more companies reporting negative quarterly and trailing 12-month earnings during the latest earnings reporting cycle resulted in a dramatic decline in qualifying companies.

Latest Shadow Stock Portfolio Alerts

COMPANY (TICKER)	ACTION	DATE
Penn Virginia Corporation (PVAC)	BUY	6/15/2020
Flexsteel Industries, Inc. (FLXS)	SELL	6/15/2020

See Historical Alerts →

Shadow Stock Portfolio Performance

	YTD Return (%)	Annual Return (%)				Ann'l Std Dev (%)	3-Year Risk-Adj Ret (%)*
		1-Year	5-Year	10-Year	20-Year		
Shadow Stock Portfolio	-34.1	-27.1	-6.3	8.2	12.1	32.1	-20.4
Vanguard 500 Idx (VFINX)	-3.1	7.4	10.6	13.8	5.8	16.7	10.6

As of 6/30/2020

See Performance →

User's Guide

To help you start investing in your own Shadow Stock Portfolio, we created this User's Guide. Here you will find information about the strategy used for the Shadow Stock Portfolio, instructions on how to set up your initial portfolio, as well as how to follow the portfolio after setting it up and the rules for when to sell.

See User's Guide →

Actual AAII Model Shadow Stock Portfolio

- "Actual Portfolio" section updated monthly & lists current portfolio holdings
- Current price to book & market cap
- Special notes (e.g., currently qualifies, earnings probation)

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AAII Model Shadow Stock Portfolio
Shadow Stock Portfolio Rules
Year-to-Year Performance
Transaction History

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Company	Ticker	Current Price ($)	52-Week High ($)	52-Week Low ($)	Market-Cap Size ($ mil)	Price-Earnings Ratio (X)	Price-to-Book Ratio (X)	Rel Price Strgth (%)	Notes
Hallador Energy Co	HNRG	0.65	5.87	0.60	19.7	na	0.11	5	earnings probation 2019q4
Penn Virginia Corporation	PVAC	11.11	37.12	0.99	168.4	0.50	0.25	8	currently qualifies
Bassett Furniture Industries Inc.	BSET	8.00	18.24	4.25	79.9	na	0.53	12	
Beazer Homes USA, Inc.	BZH	11.32	17.23	4.39	351.2	11.10	0.64	32	
Big 5 Sporting Goods Corporation	BGFV	4.34	4.14	0.65	94.7	24.90	0.54		

Pay attention to notes about current qualifiers, earnings probation, valuation & market cap

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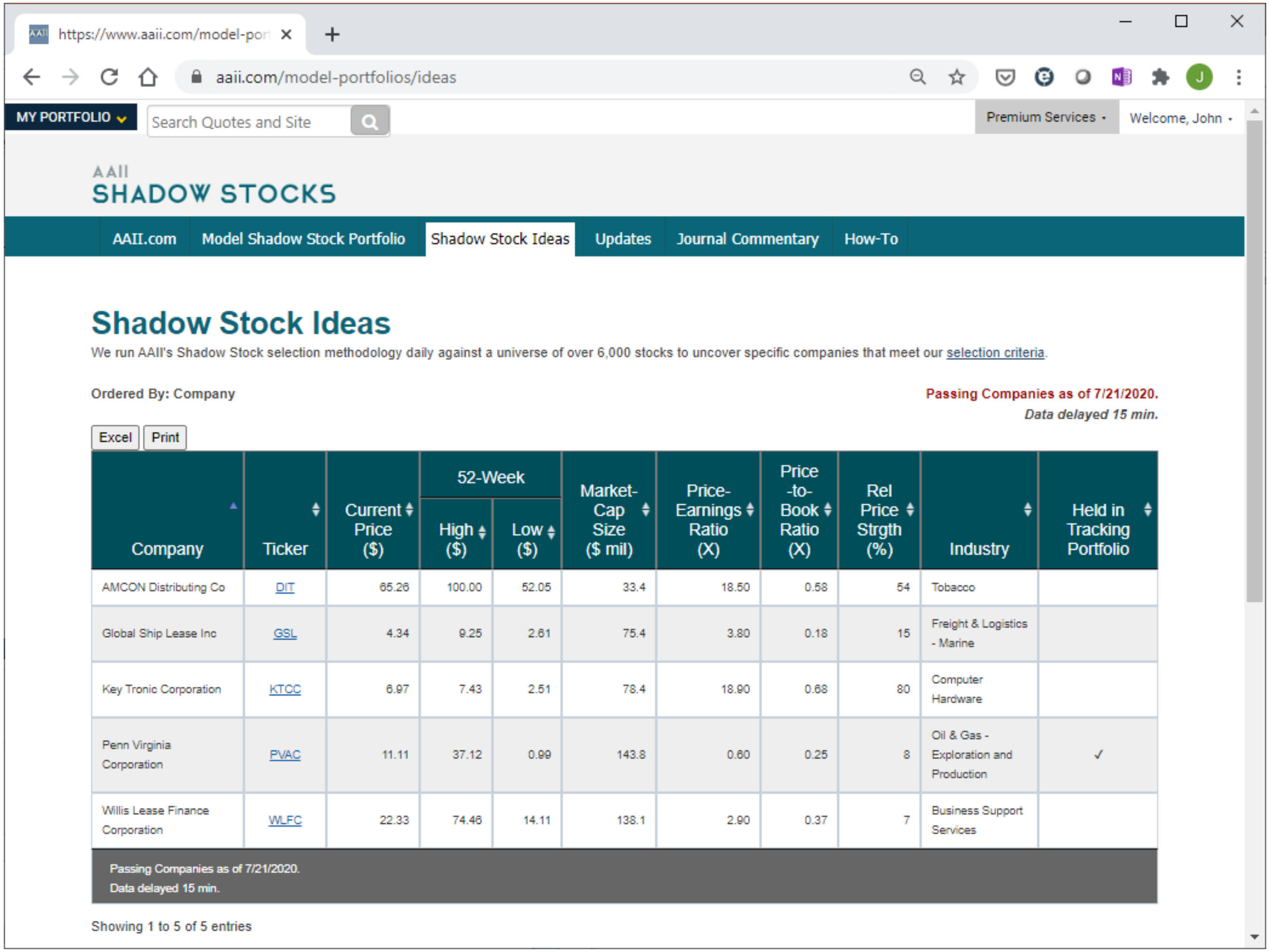

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Welcome, John

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Shadow Stock Ideas

We run AAII's Shadow Stock selection methodology daily against a universe of over 6,000 stocks to uncover specific companies that meet our selection criteria.

Ordered By: Company

Passing Companies as of 7/21/2020.
Data delayed 15 min.

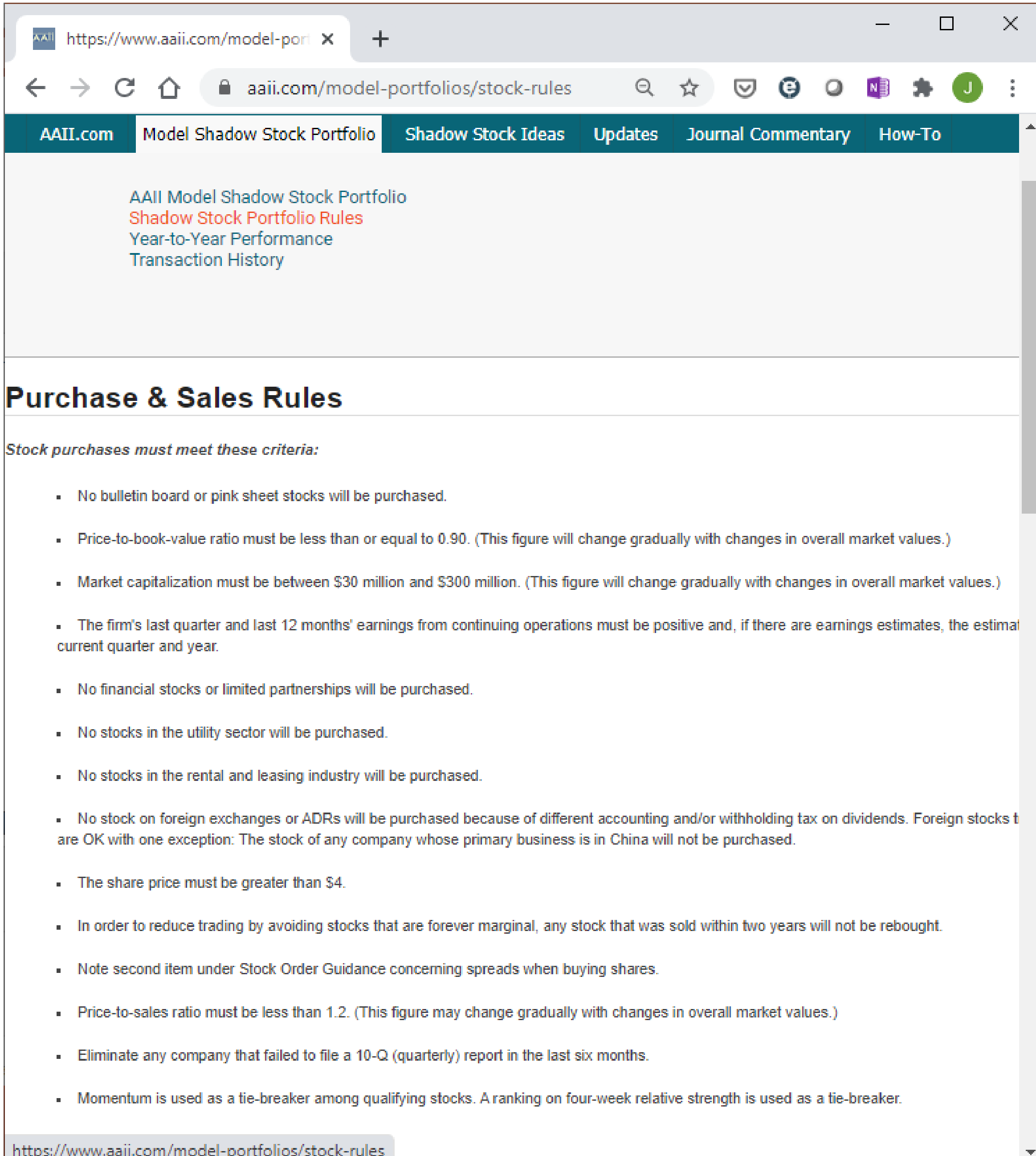
Excel | Print

Company	Ticker	Current Price ($)	52-Week High ($)	52-Week Low ($)	Market-Cap Size ($ mil)	Price-Earnings Ratio (X)	Price-to-Book Ratio (X)	Rel Price Strgth (%)	Industry	Held in Tracking Portfolio
AMCON Distributing Co	DIT	65.26	100.00	52.05	33.4	18.50	0.58	54	Tobacco	
Global Ship Lease Inc	GSL	4.34	9.25	2.61	75.4	3.80	0.18	15	Freight & Logistics - Marine	
Key Tronic Corporation	KTCC	6.97	7.43	2.51	78.4	18.90	0.68	80	Computer Hardware	
Penn Virginia Corporation	PVAC	11.11	37.12	0.99	143.8	0.60	0.25	8	Oil & Gas - Exploration and Production	✓
Willis Lease Finance Corporation	WLFC	22.33	74.46	14.11	138.1	2.90	0.37	7	Business Support Services	

Passing Companies as of 7/21/2020.
Data delayed 15 min.

Showing 1 to 5 of 5 entries

- "Shadow Stock Ideas" list is updated **daily** and lists all stocks currently passing initial buy rules
- You will need to monitor any stocks purchased from this list since they may not be part of our model portfolio



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Shadow Stock Portfolio Rules
Year-to-Year Performance
Transaction History

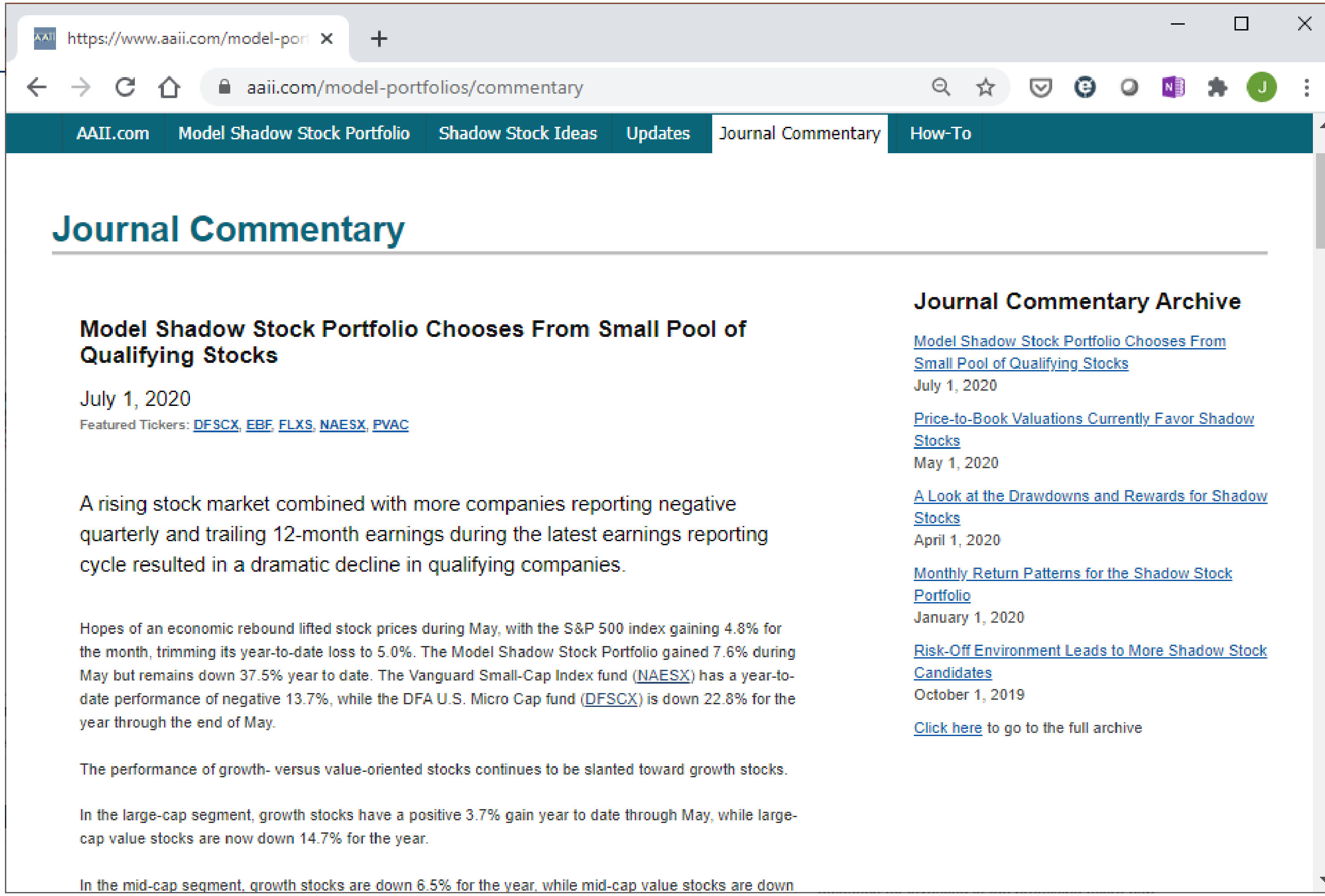
Purchase & Sales Rules

Stock purchases must meet these criteria:

- No bulletin board or pink sheet stocks will be purchased.
- Price-to-book-value ratio must be less than or equal to 0.90. (This figure will change gradually with changes in overall market values.)
- Market capitalization must be between $30 million and $300 million. (This figure will change gradually with changes in overall market values.)
- The firm's last quarter and last 12 months' earnings from continuing operations must be positive and, if there are earnings estimates, the estimat current quarter and year.
- No financial stocks or limited partnerships will be purchased.
- No stocks in the utility sector will be purchased.
- No stocks in the rental and leasing industry will be purchased.
- No stock on foreign exchanges or ADRs will be purchased because of different accounting and/or withholding tax on dividends. Foreign stocks t are OK with one exception: The stock of any company whose primary business is in China will not be purchased.
- The share price must be greater than $4.
- In order to reduce trading by avoiding stocks that are forever marginal, any stock that was sold within two years will not be rebought.
- Note second item under Stock Order Guidance concerning spreads when buying shares.
- Price-to-sales ratio must be less than 1.2. (This figure may change gradually with changes in overall market values.)
- Eliminate any company that failed to file a 10-Q (quarterly) report in the last six months.
- Momentum is used as a tie-breaker among qualifying stocks. A ranking on four-week relative strength is used as a tie-breaker.

https://www.aaii.com/model-portfolios/stock-rules

- Current Model Shadow Stock Portfolio rules can always be found in this section
- Rules are divided into sections dealing with initial buy criteria, sell criteria, guidelines for placing orders, and overall portfolio management rules



- Past *AAII Journal* articles dealing with Model Shadow Stock Portfolios are presented in the "Commentaries" section
- Helpful articles to gain an overview of the issues that come up in managing a micro-cap portfolio and how the rules evolve as market conditions change

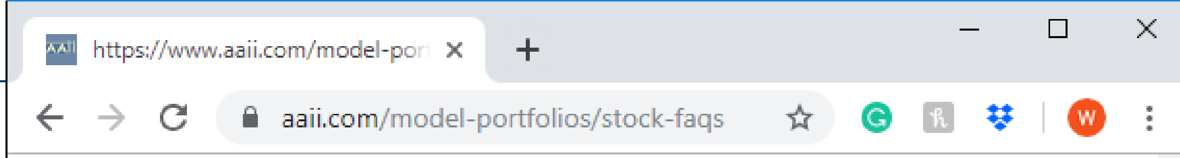
AAII.com | Model Shadow Stock Portfolio | Shadow Stock Ideas | Updates | Journal Commenta

AAII Model Shadow Stock Portfolio
Shadow Stock Portfolio Rules
Year-to-Year Performance
Transaction History

YEAR-TO-YEAR PERFORMANCE

Year	Annual Rate of Return (%)			Cumulative Growth of $10,000		
	Model Shadow Stock Portfolio	Vanguard 500 Index (VFINX)	Vanguard Small Cap Index (NAESX)	Model Shadow Stock Portfolio	Vanguard 500 Index (VFINX)	Vanguard Small Cap Index (NAESX)
1993	32.3	9.9	18.7	$13,230	$10,989	$11,870
1994	2.0	1.2	-0.5	$13,492	$11,118	$11,810
1995	20.7	37.4	28.7	$16,291	$15,282	$15,204
1996	22.3	22.9	18.1	$19,927	$18,775	$17,959
1997	44.3	33.2	24.6	$28,756	$25,010	$22,375
1998	-8.9	28.6	-2.6	$26,188	$32,168	$21,790
1999	0.0	21.1	23.1	$26,187	$38,945	$26,831
2000	-7.7	-9.1	-2.7	$24,163	$35,418	$26,116
2001	21.4	-12.0	3.1	$29,325	$31,160	$26,926

- Historical Return link brings up performance chart
- Year-to-Year Performance link brings up table of annual performance



Model Shadow Stock Portfolio FAQs

Site Mechanics

See latest changes to the model portfolio
Get notification of portfolio changes
See actual buy and sell prices
Model Shadow Stock Portfolio list versus the Shadow Stock Ideas
How often the Shadow Stock Ideas list is updated

Implementing the Portfolio

How to get started
Using AAII's Stock Investor Pro to find shadow stocks
How much money should be invested
How to choose your starting 10 stocks
Diversifying your stock picks
Why many qualifying stocks are trending down
Best way to place orders when buying small stocks
Handling spreads in small stocks
Choosing a broker
What to do if stock price moves up when buying
Is there a mutual fund that follows the model?

Portfolio Management Issues

Stocks that no longer show up on Portfolio or Ideas lists
Stocks bought between quarterly reviews
Holdings that are losing money
Buyouts
Delistings
Handling dividends
Rebalancing your portfolio

FAQs (Frequently Asked Questions)

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Members subscribing to the "AAII Model Shadow Stock Portfolio Update" receive a monthly email with the latest portfolio changes and current performance along with alerts to additions/deletions

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July Model Shadow Stock Portfolio Update

Featured Tickers: AAL, CMLS, CVU, DLA, EBF, HOFT, HURC, LMT, MESA, NAESX, NOC, PVAC, RICK, STRT, TCS, TOL, TSQ, UAL, VFINX

by John Bajkowski | July 15, 2020

Next Wednesday, July 15, at 7:30 p.m. CDT, AAII president John Bajkowski will host a webinar on the Model Shadow Stock Portfolio. To register, click here.

Eleven stocks met the initial selection criteria for the Model Shadow Stock Portfolio as of July 13, 2020, up from eight passing stocks one month ago. AAII members can see and research which companies are currently passing the initial selection criteria in the **Shadow Stock Ideas** table on AAII.com. The list of Shadow Stock Ideas is updated daily—Tuesday through Saturday.

Of the 11 qualifying companies, two are currently held in the Model Shadow Stock tracking portfolio: Hooker Furniture Corp. (**HOFT**) and Penn Virginia Corp. (**PVAC**). Strattec Security Corp. (**STRT**) came off the list of qualifying companies over the course of the last month, while Hooker Furniture was added. Qualifying companies are those held in the Model Shadow Stock Portfolio that currently meet the initial purchase rules. (They are designated as "currently qualifies" in the notes column of the Model Shadow Stock Portfolio table on AAII.com. However, if you go online, the notes may not match the list discussed here since the notes on the website table are dynamically updated daily.)

As of July 13, 2020, Ennis Inc. (**EBF**) had the highest price-to-book-value ratio in the Model Shadow Stock Portfolio. Its ratio of 1.45 is above the 0.90 maximum value used for initially qualifying a stock for inclusion to the portfolio. However, stocks are not removed from the portfolio until their price-to-book-value ratio rises to three times the initial maximum value (2.70).

As we have noted, it may help you to think about values below 0.90 as being attractive, while values three times above the initial maximum are expensive. Allowing the price-to-book ratio to expand for stocks that you own allows your winners to run up a little, since the price-to-book ratio typically gets larger as the stock price goes up. The initial price-to-book level is adjusted over time to reflect the changing market conditions, and valuation and size requirements are being examined for the next quarterly portfolio review.

The Model Shadow Stock Portfolio looks for stocks with a market capitalization (share price times shares outstanding) greater than $30 million but less than $300 million when

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Derek Hageman
Open House: Dividend Investing
Wednesday, July 29, 2020, 7:30 p.m. CDT

Alliance for Investor Education Panel
Staying the Course In a Time of Upheaval: What to do Now?
Wednesday, August 5, 2020, 7:30 p.m. CDT

Wayne Thorp
Investing Like a Stock Superstar: A Contrarian Approach to Seeking Fundamental Growth
Wednesday, August 12, 2020, 7:30 p.m. CDT

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