

afg 50

- client benefits
- performance
- selection criteria
- content

AFG 50:

- An actively managed portfolio of 50 stocks, remaining sector-neutral.
- Long-only and targeting turnover of less than 40% annually.

Our Goals:

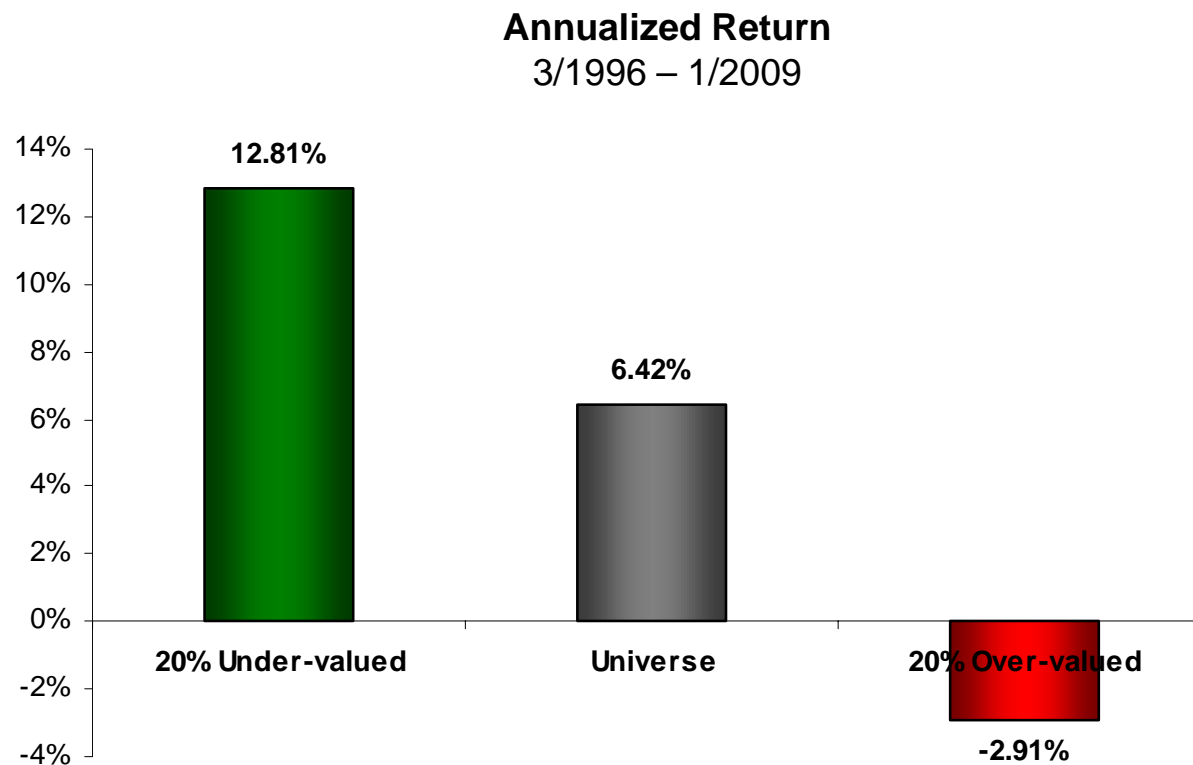
- To consistently beat the index our clients are most often measured against, the S&P 500.
- To serve as an outsourced research team, distributing relevant content to our clients on a weekly basis.
- To provide consistent, actionable buy ideas in each major economic sector.



Selection Process

A Starting Point.....Valuation Works

Screening allows AFG analysts to identify buy candidates in each sector that meet the characteristics of out-performing companies.



Line Item Forecasting – the Pro Forma Builder

Companies from our custom screening process are modeled at the line-item level to fine-tune target prices and eliminate unattractive stocks.

- Upon a company's quarterly earnings announcement, the AFG 50 valuation model is updated to reflect management forecasts and operating performance.
- Income statement forecasting, tying to company forecasts and accurately reflecting the consensus earnings expectations.
- Line item balance sheet detail, with attention to working capital management and expectations for capital expenditures.
- Attention to capital structure and free cash flow allocation regarding share repurchase and dividend payments.

Qualitative Factors

On top of quantitative research, analysts spend a significant amount of time understanding the company's strategy and risks.

- What does the competitive landscape look like and does the company maintain a sustainable competitive advantage? What are the barriers to entry in this industry?
- What specific business or economic risk does the company face?
- What, if any, significant litigation is the company facing? What regulation is the company subjected to?
- Have there been any changes in the executive management team?
- Has the company had any significant write-offs or poor earnings quality?
- Has the company recently made any significant acquisitions and, if so, what are the strategic implications and costs?
- Where are the company's growth opportunities? How is the company spending any excess cash?
- What did we learn from the company's most recent earnings call and what was the tone of analyst questions?
- Has the company recently gained or lost any significant clients? How diversified is the company's client base?
- What exposure does the company have to supplier costs and how much pricing flexibility does the company maintain?
- What do recent quarterly sales and margin trends tell us?

Correlation Analysis

As a final overlay, we examine the correlation between attractive stocks within a sector. Diversifying across uncorrelated stocks leads to better portfolio construction.

Tickers	<u>AZO</u>	<u>BBY</u>	<u>CVS</u>	<u>DRI</u>	<u>DDS</u>	<u>EFX</u>	<u>HRB</u>	<u>HD</u>	<u>LOW</u>
AZO	1.00	0.39	0.22	-0.01	0.13	0.28	0.09	0.36	0.44
BBY	0.39	1.00	0.38	0.23	0.27	0.41	0.21	0.64	0.48
CVS	0.22	0.38	1.00	0.40	0.09	0.18	0.15	0.21	0.25
DRI	-0.01	0.23	0.40	1.00	0.23	0.19	0.30	0.34	0.30
DDS	0.13	0.27	0.09	0.23	1.00	0.18	0.29	0.34	0.26
EFX	0.28	0.41	0.18	0.19	0.18	1.00	0.22	0.51	0.30
HRB	0.09	0.21	0.15	0.30	0.29	0.22	1.00	0.22	0.29
HD	0.36	0.64	0.21	0.34	0.34	0.51	0.22	1.00	0.70
LOW	0.44	0.48	0.25	0.30	0.26	0.30	0.29	0.70	1.00

AFGView.com: see the AFG 50 interface for return tracking and performance

Full Reports: a full 8-page report on each AFG 50 name, emailed to our client base and available on the AFG website.

Backup List: each sector contains 2 backup companies. These companies are followed and modeled out by our analysts.

Quarterly Updates: between full reports, analysts will release quarterly updates to summarize earnings calls and reinforce our investment recommendation.

Acquisition Analysis: for significant acquisitions that affect AFG 50 stocks or their competitors, analysts will issue a report analyzing the purchase price and the strategic impact of the combination. Past reports covered Oracle's acquisition of PeopleSoft, Harrah's acquisition of Caesar's, and Proctor & Gamble's acquisition of Gillette.

Q: What is the AFG50?

A: The AFG50 is a focused group of stocks designed to beat the index our clients are most often measured against: the S&P500. Our further goal with this product is to act as an outsourced fundamental analyst group, providing yet another resource our clients can utilize. The AFG 50 is long-only, targets annual turnover below 40%, and will remain sector-neutral relative to the S&P500.

Q: What is the selection process and criteria for AFG50 Companies?

A: The stocks selected for the AFG 50 must meet a set of decision rules developed by The Applied Finance Group related to each company's intrinsic value and market price. More importantly, each company meeting our first hurdle is then reviewed by an analyst team to address the qualitative issues that a model cannot identify. AFG analysts also strive to achieve a desired level of diversification within sectors, avoiding any unintended exposure to a given economic factor.

Q: How often will reports be issued on companies within the AFG50?

A: Each month, we will be releasing 3-5 detailed reports reviewing existing holdings or new additions to the portfolio. In addition, each quarter, we will perform a quarterly deconstruction of the portfolio's performance, discuss the driving themes behind each sector, and provide a sector snapshot of the S&P500.

Q: How will the information be distributed to AFG50 recipients?

A: There is an AFG 50 tab on AFGView.com. It contains access to all company reports, models, and notes in addition to daily and cumulative performance. We will also send out emails notifying the release of new reports with web links.

Q: How will AFG50 recipients be informed on companies that fall in/out of the AFG50?

A: Clients will be notified via email of all transactions to AFG 50 companies. In addition, the AFG 50 web module will contain a log of all past transactions showing sells and corresponding buys.

Q: What information will be conveyed to justify those companies falling out of the portfolio?

A: Once we have decided to sell a stock, we will issue a note that describes why we are selling and justification for the stock we have chosen as a replacement.

AFG analysts are available to answer your questions or discuss individual stocks within each economic sector. Sector responsibilities break out as follows:

Andrew McFadden

- Information Technology
- Telecommunication Services
- Industrials

Jun Wang, CFA

- Consumer Discretionary
- Consumer Staples
- Financials

Alex Plascencia

- Health Care
- Energy
- Materials

Mark Everette

- Utilities