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A better way for obtaining your value tilt

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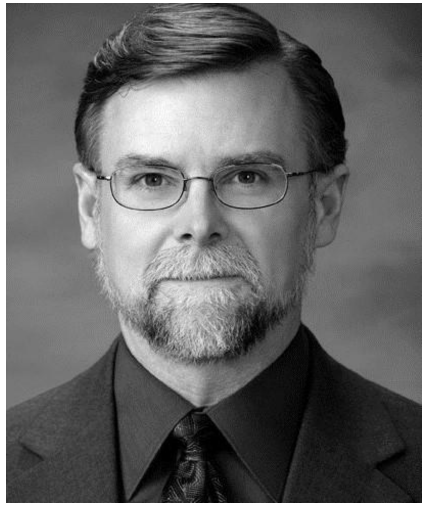

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Conventional wisdom

- Conventional wisdom prescribes a permanent fixed tilt towards value
- This conclusion is based on the following assumptions about the value risk premium
  - Sufficient size
  - Sufficient consistency
  - Some diversification benefit
- Convention wisdom is wrong
- It lacks even the slightest degree of consistency, and instead is painfully episodic

We showed that conventional wisdom is wrong

- The value premium exists
- It’s large and spans all geographies (US, international, and EM)
- Unfortunately . . . It is strongly episodic
- Moreover, it’s diversification properties are chaotic

But, why now

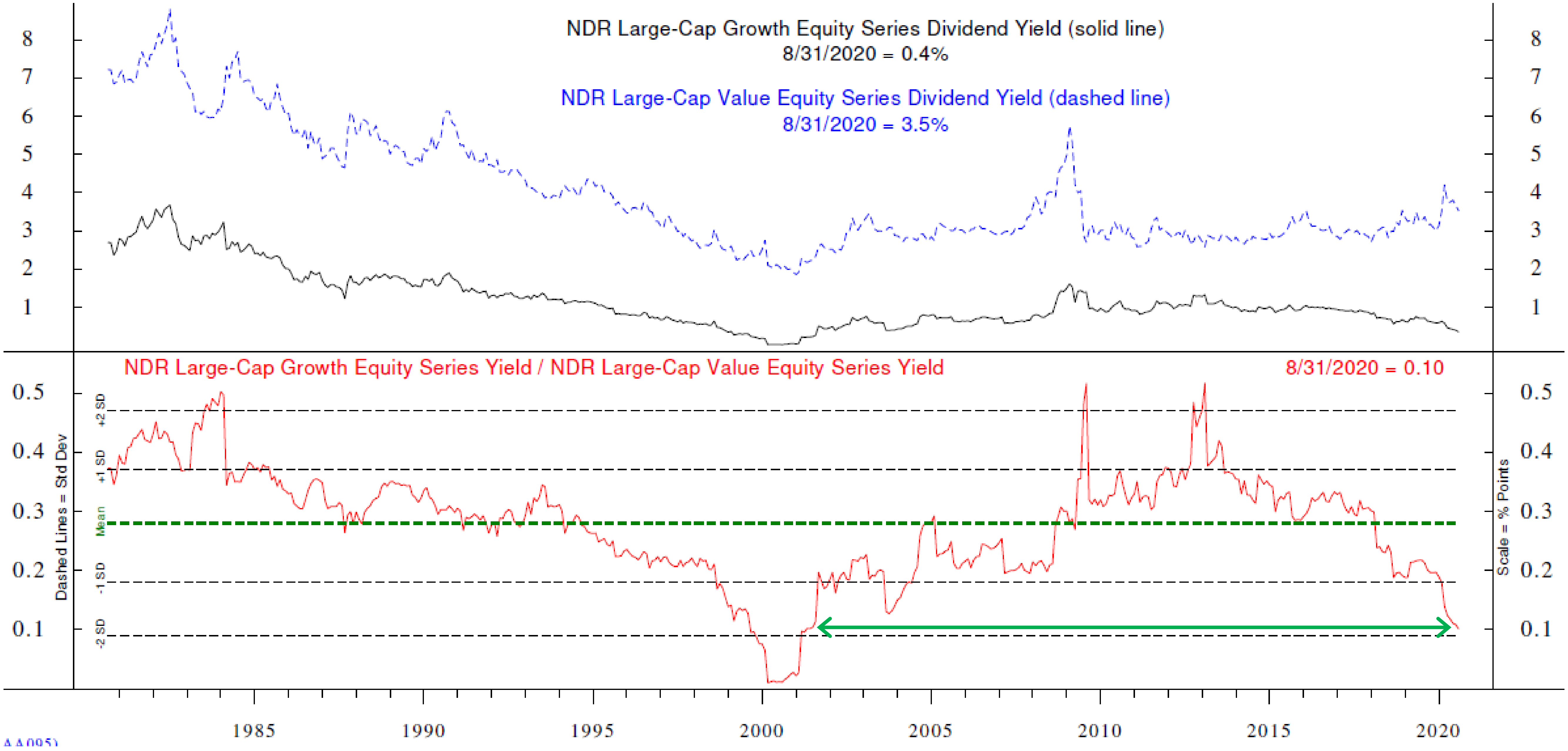
Valuations

Comparative fundamental valuations, continued

	Growth (large cap)	Value (large cap)
Price/earnings ratio	25.8	16.4
Price/book ratio	4.6	2.0
Return on equity	22.4%	16.4%
Earnings per share growth rate	19.1%	12.5%
PEG ratio (P/E divided by earnings growth)	1.35	1.31
Dividend yield	0.68%	2.82%
Technology weighting	24.0%	10.7%

Statistics as of September 30, 2020

Based on earnings yield, value is the cheapest in 19 years



But, why now

Technology, very similar to the 2000 bear market

Tech wreck of 2000 and the small cap risk premium

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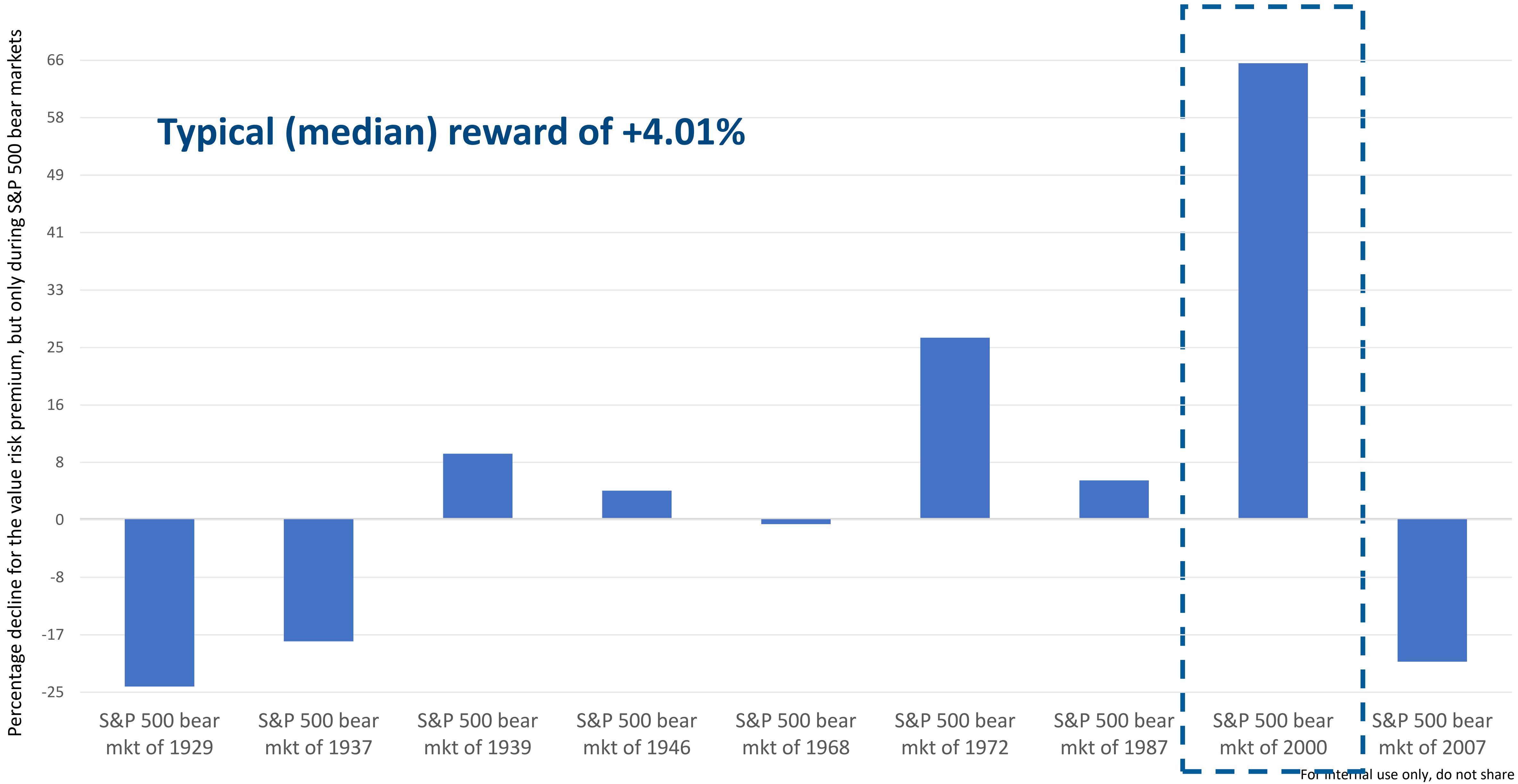
Value risk premium is random (noisy) during S&P 500 bear markets

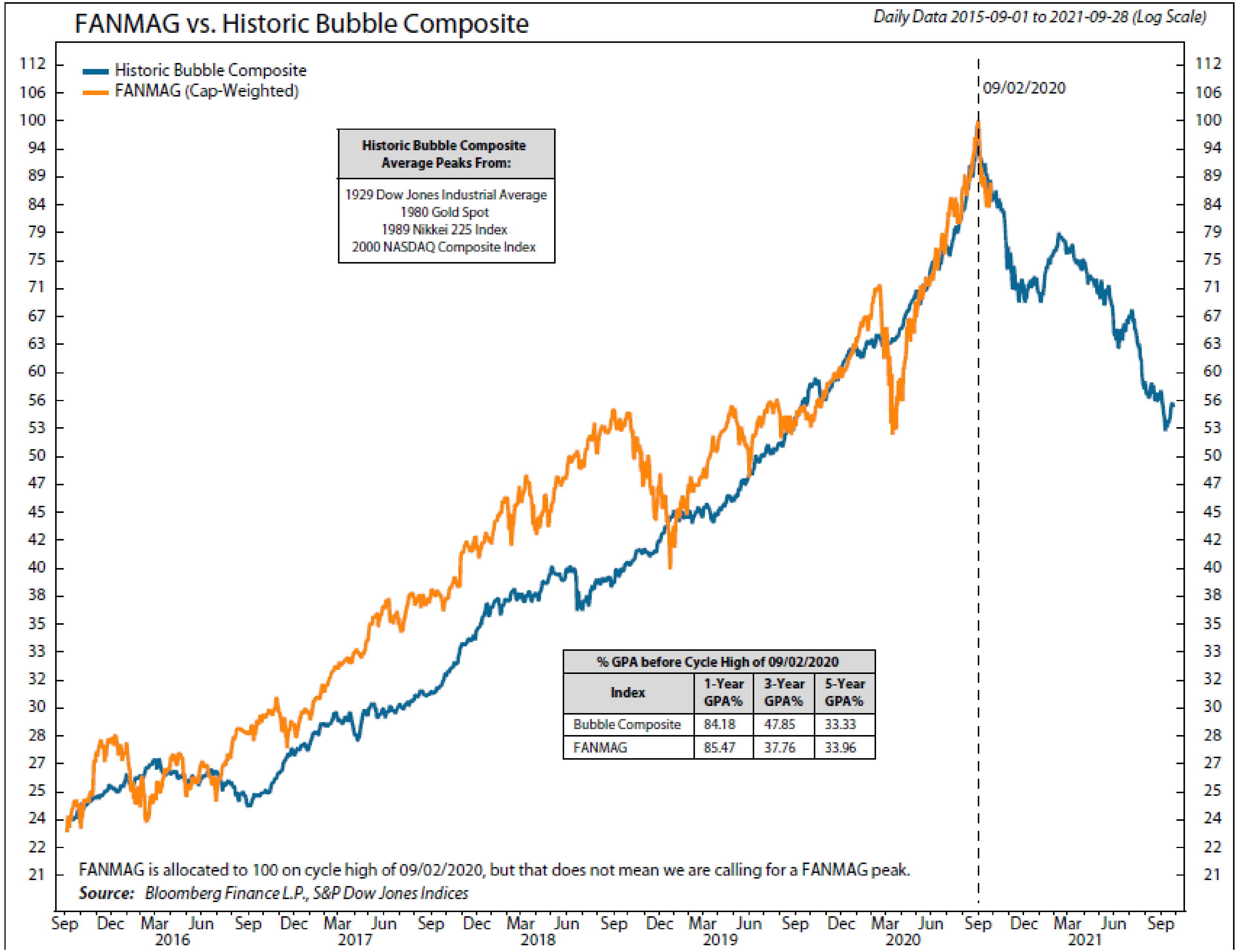


FANMAG - a classic bubble

FANMAG to blame

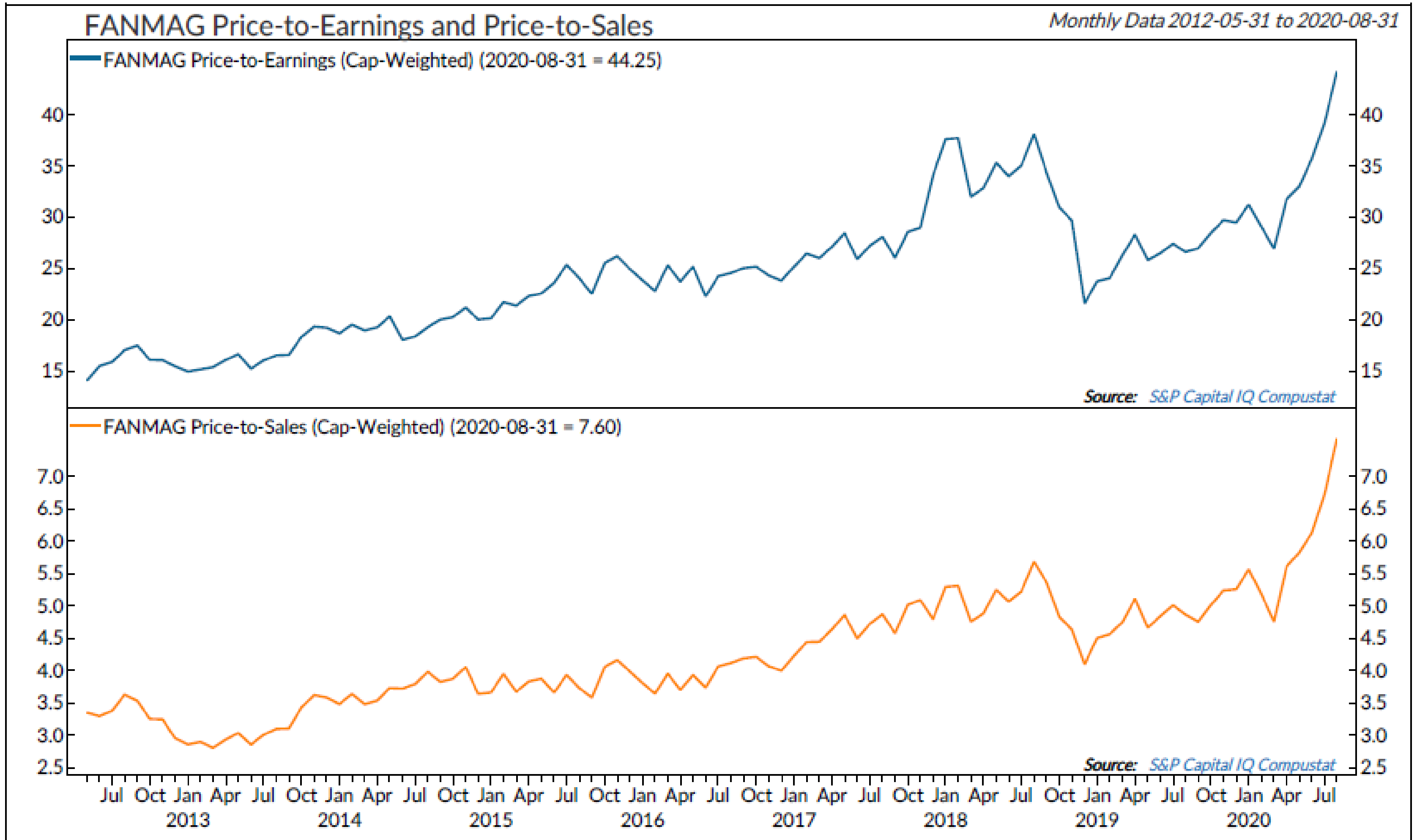
The main culprits of Growth's recent surge are a handful of mega-cap Growth stocks. The six FANMAG stocks posted gains similar to our composite of four widely accepted bubbles over the past one, three, and five years **(chart, right)**.

FANMAG following bubble trajectory



FANMAG - a classic bubble, continued

Record high FANMAG P/E and P/S



Ticker	Name
FB	Facebook
AMZN	Amazon.com
NFLX	Netflix
MSFT	Microsoft
AAPL	Apple
GOOGL	Alphabet

FANMAG valuations

The rally in FANMAG stocks has left them expensive. The price/earnings and price/sales ratios for FANMAGs are at record highs **(chart, left)**.

But, why now

The current value bear market is long in the tooth

Current bear market for the value risk premium is long in the tooth

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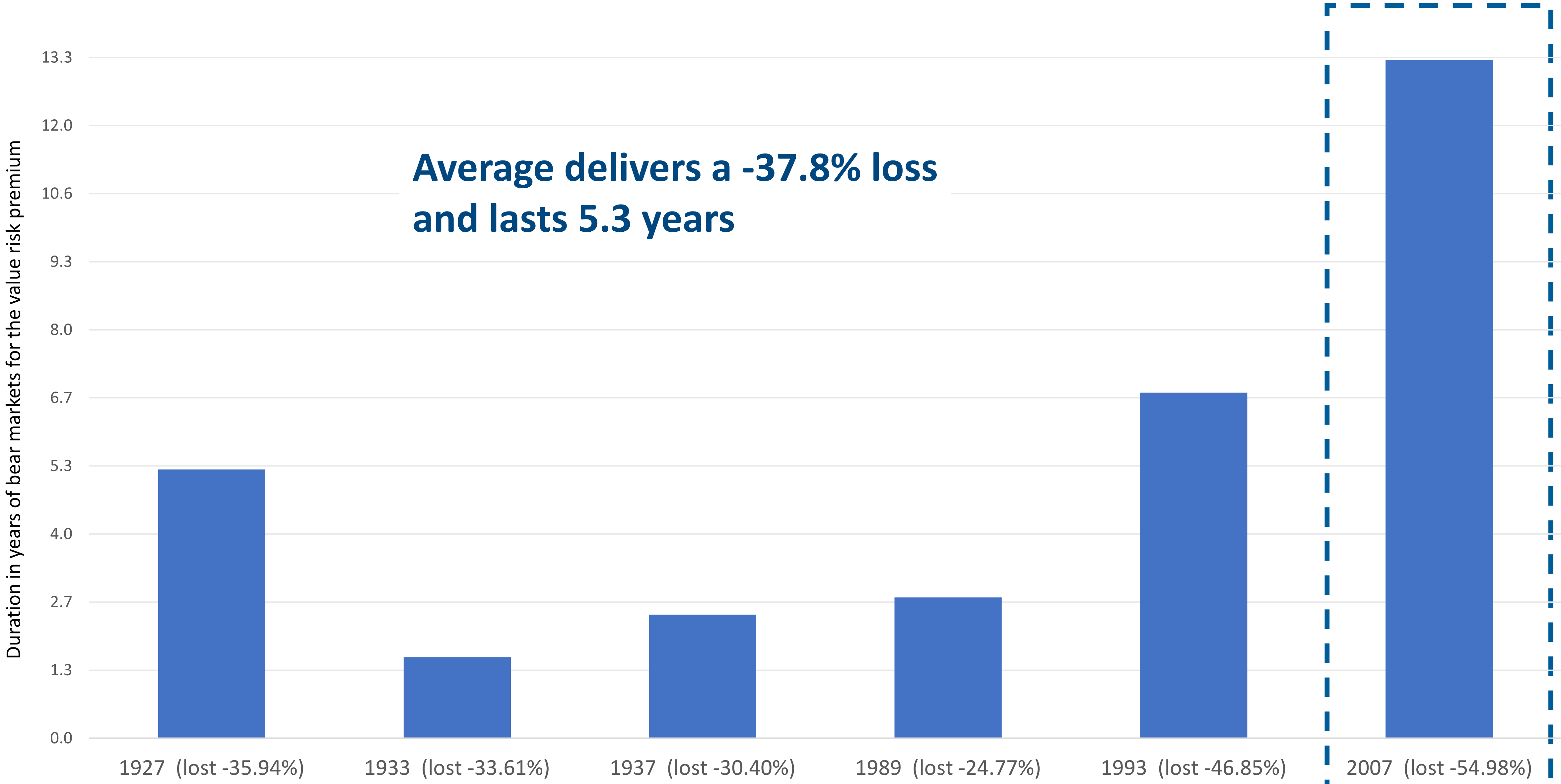
Bear markets for the value risk premium have been both severe and long-lasting



Ned Davis Research - makes the same observation

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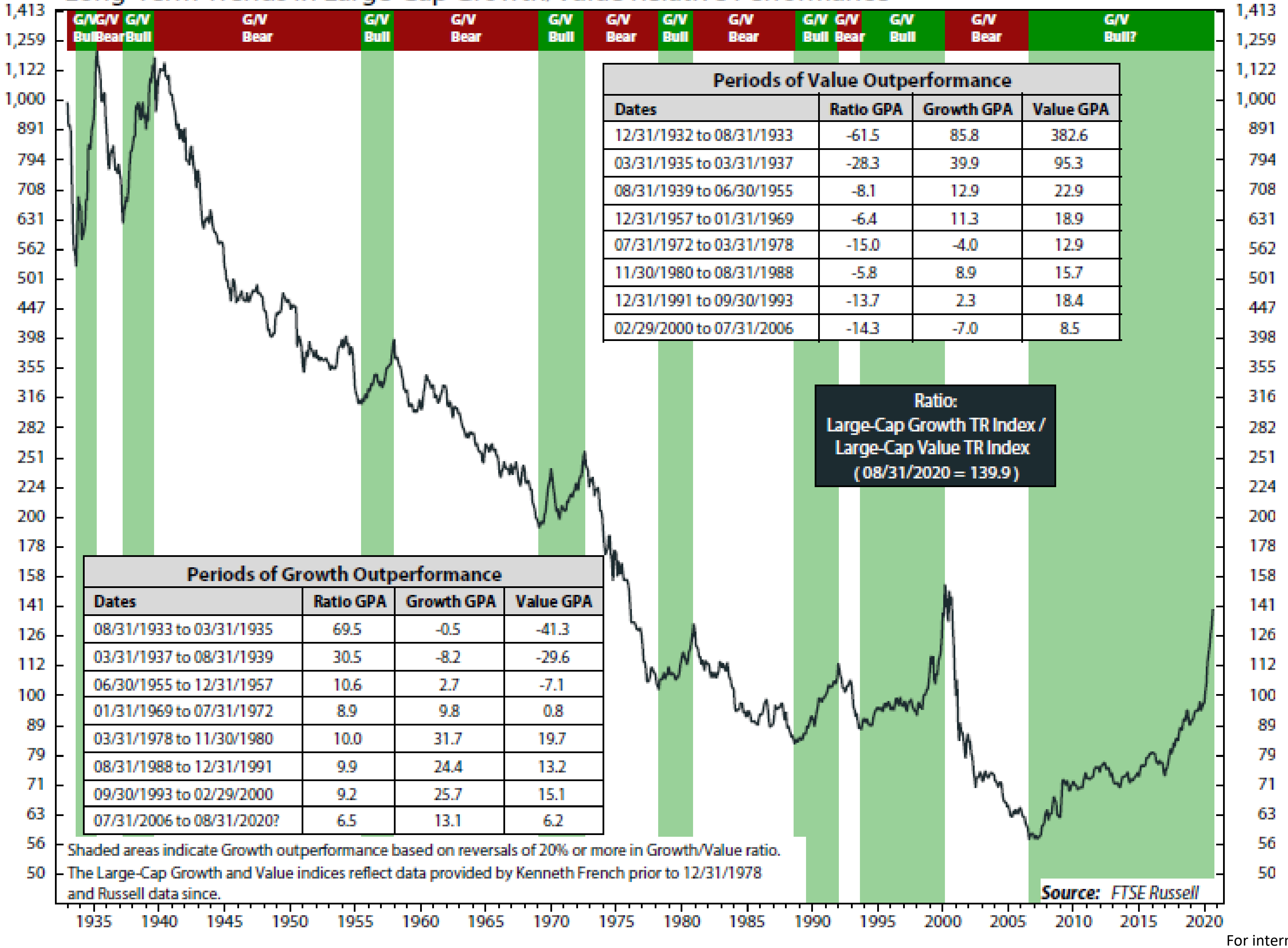
Long-Term Trends in Large-Cap Growth/Value Relative Performance



Periods of Value Outperformance

Dates	Ratio GPA	Growth GPA	Value GPA
12/31/1932 to 08/31/1933	-61.5	85.8	382.6
03/31/1935 to 03/31/1937	-28.3	39.9	95.3
08/31/1939 to 06/30/1955	-8.1	12.9	22.9
12/31/1957 to 01/31/1969	-6.4	11.3	18.9
07/31/1972 to 03/31/1978	-15.0	-4.0	12.9
11/30/1980 to 08/31/1988	-5.8	8.9	15.7
12/31/1991 to 09/30/1993	-13.7	2.3	18.4
02/29/2000 to 07/31/2006	-14.3	-7.0	8.5

Periods of Growth Outperformance

Dates	Ratio GPA	Growth GPA	Value GPA
08/31/1933 to 03/31/1935	69.5	-0.5	-41.3
03/31/1937 to 08/31/1939	30.5	-8.2	-29.6
06/30/1955 to 12/31/1957	10.6	2.7	-7.1
01/31/1969 to 07/31/1972	8.9	9.8	0.8
03/31/1978 to 11/30/1980	10.0	31.7	19.7
08/31/1988 to 12/31/1991	9.9	24.4	13.2
09/30/1993 to 02/29/2000	9.2	25.7	15.1
07/31/2006 to 08/31/2020?	6.5	13.1	6.2

Shaded areas indicate Growth outperformance based on reversals of 20% or more in Growth/Value ratio.
The Large-Cap Growth and Value indices reflect data provided by Kenneth French prior to 12/31/1978 and Russell data since.

Source: *FTSE Russell*

But, why now

The ten largest names in the S&P 500 Index are 82% technology

82% of the ten largest S&P 500 names are technology (by weight)

Apple	Berkshire Hathaway
Microsoft	Johnson & Johnson
Amazon	Procter & Gamble
Alphabet	Visa
Facebook	NVIDIA

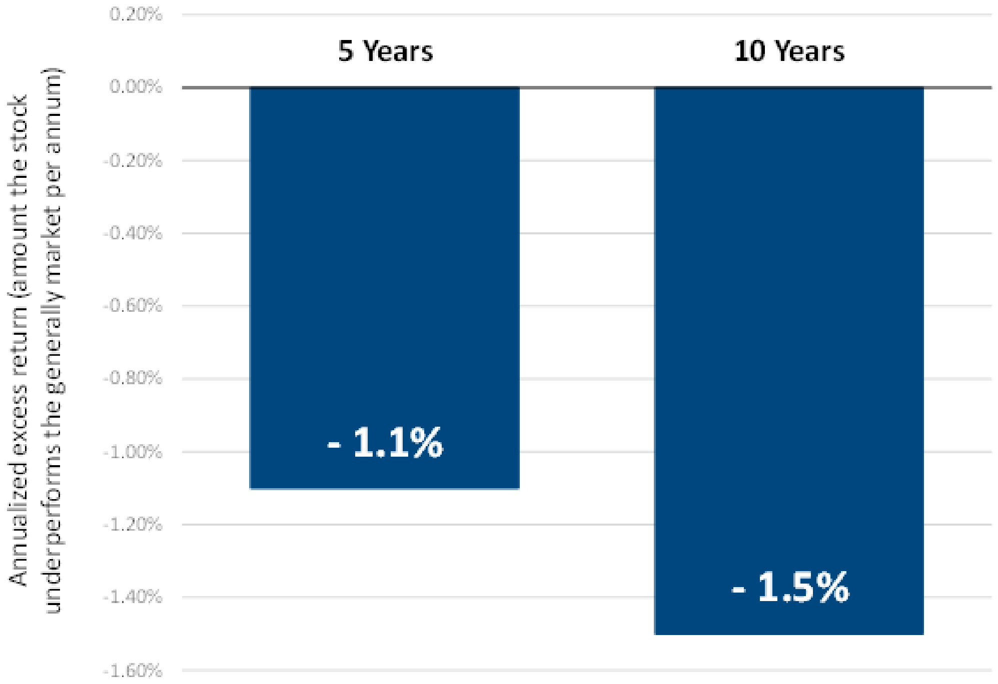
Excluding the largest companies on a global basis

Just leaving out the single largest company has historically added **+0.22%** per year[7] over and above the relevant index fund. If instead, one excluded the ten largest companies, the resulting portfolio outperformed by **+0.46%** per year[7]. In contrast, if one excluded the single largest company in each country, the resulting portfolio outperformed the comparable index fund by **+0.35%** per year[7].

Just here in the U.S.

In the U.S., once a company becomes one of the ten largest, its future performance underperforms by a wide margin[8].

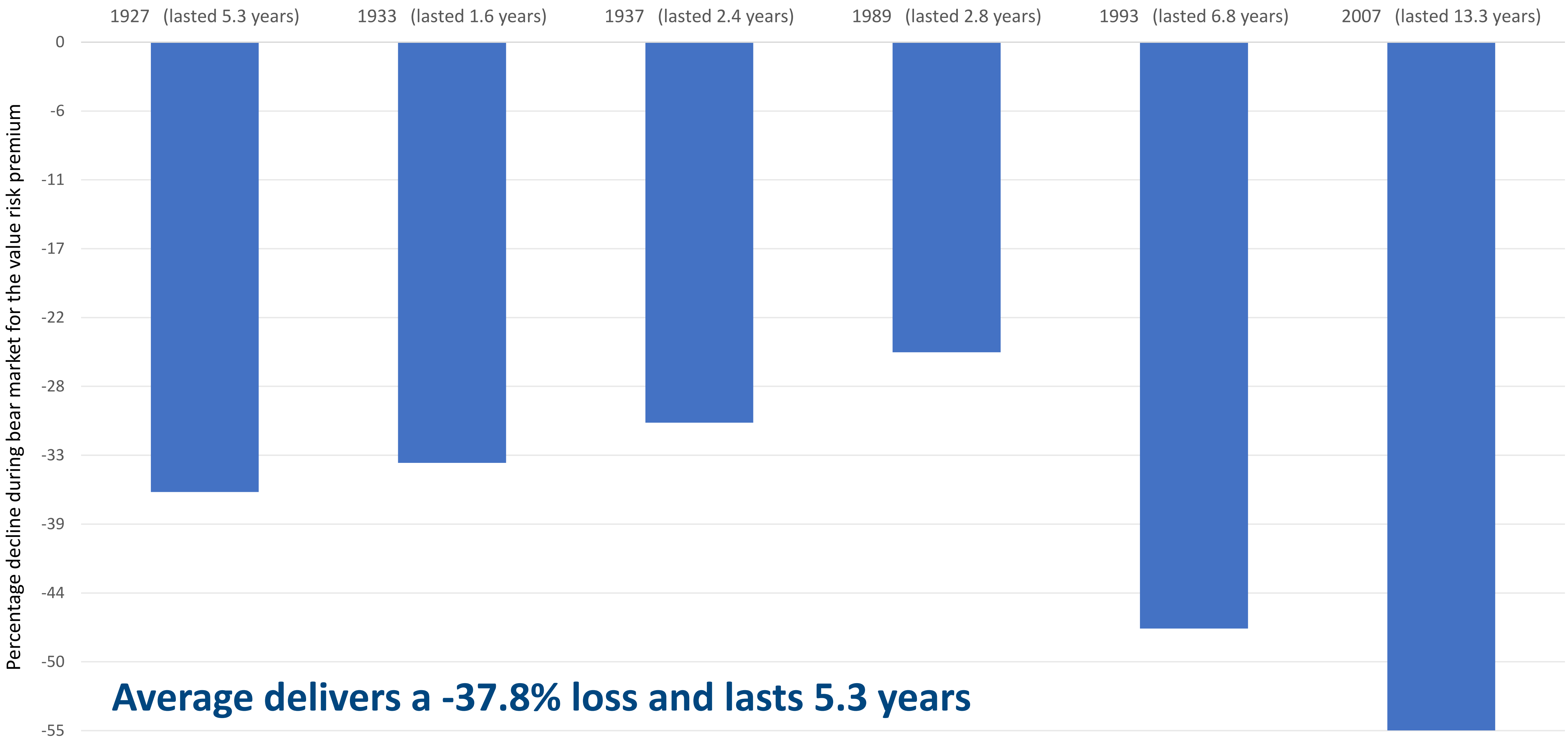
Periods after a company first became one of the ten largest stocks



But, why now

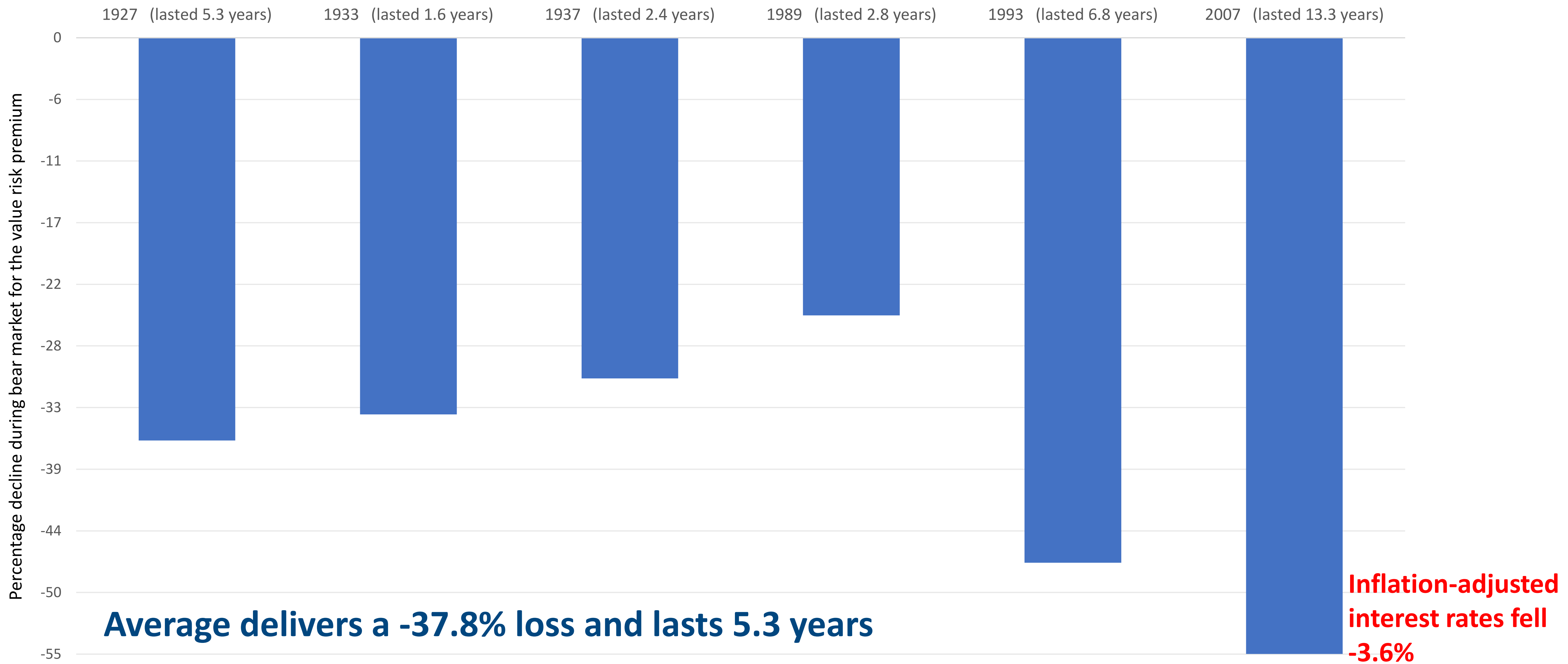
Last week, a question was posed . . . *"Are higher future interest rates an added reason?"*

Bear markets for the value risk premium have been both severe and long-lasting



Value risk premium bear markets

Bear markets for the value risk premium have been both severe and long-lasting



Value risk premium bear markets

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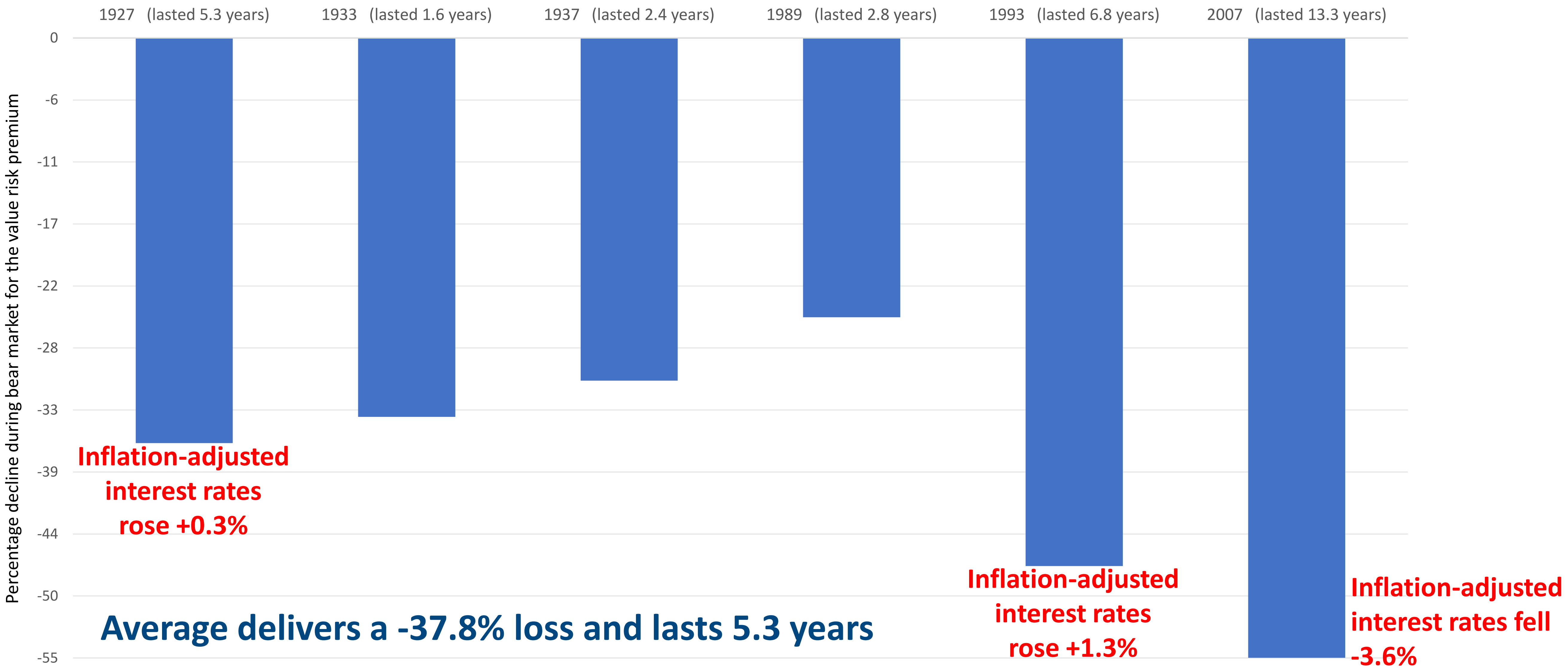
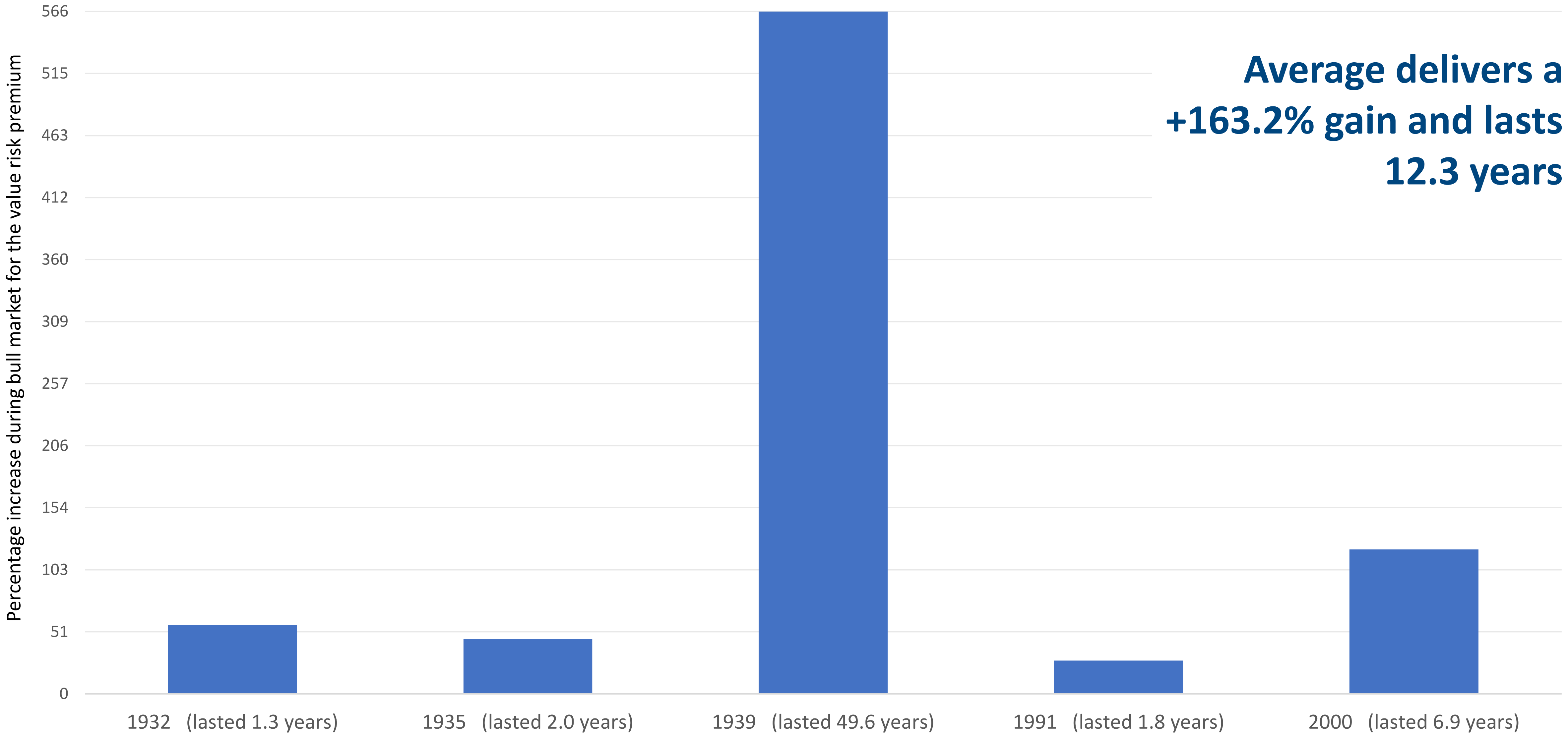
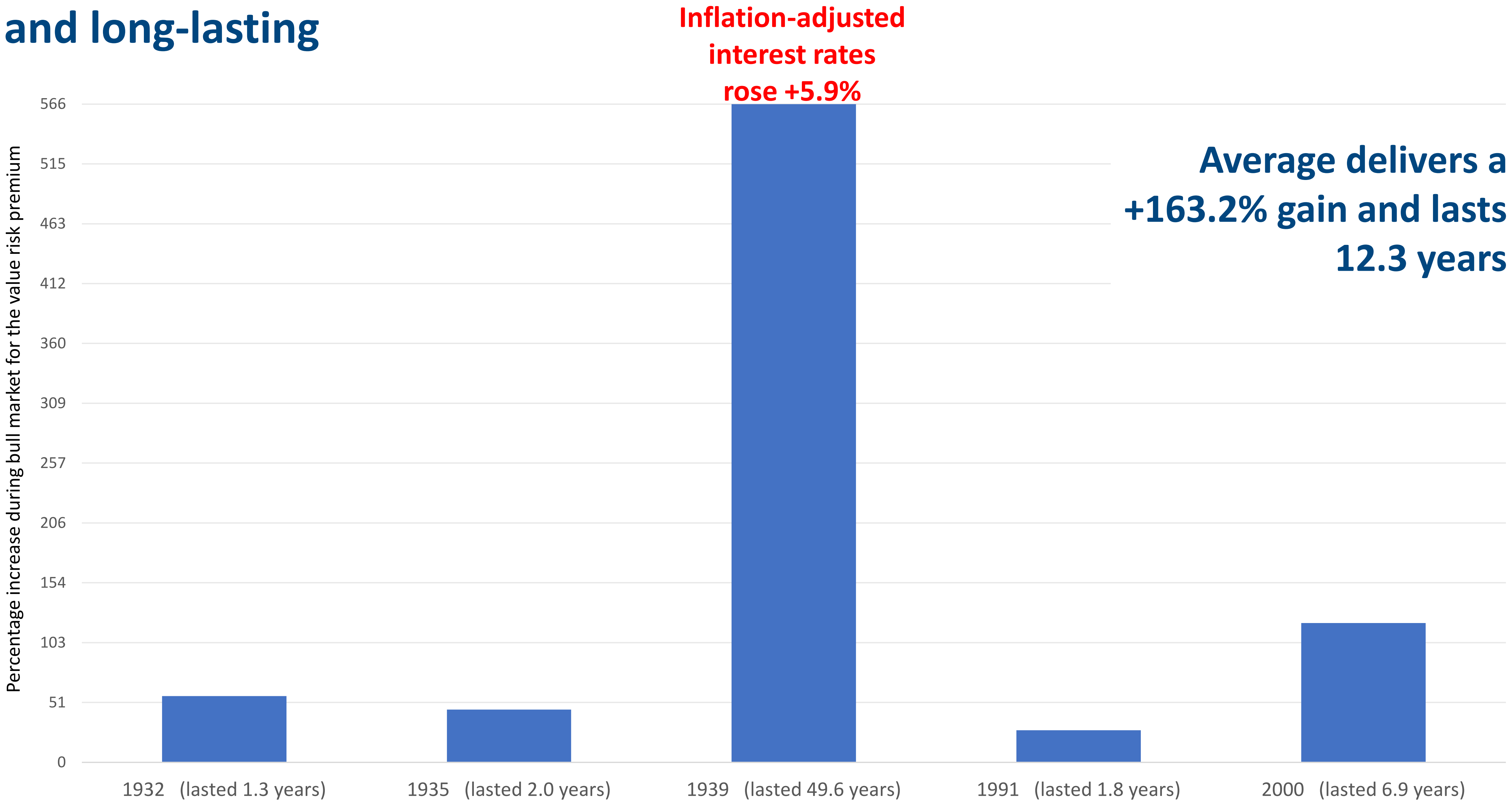


Value risk premium bull markets

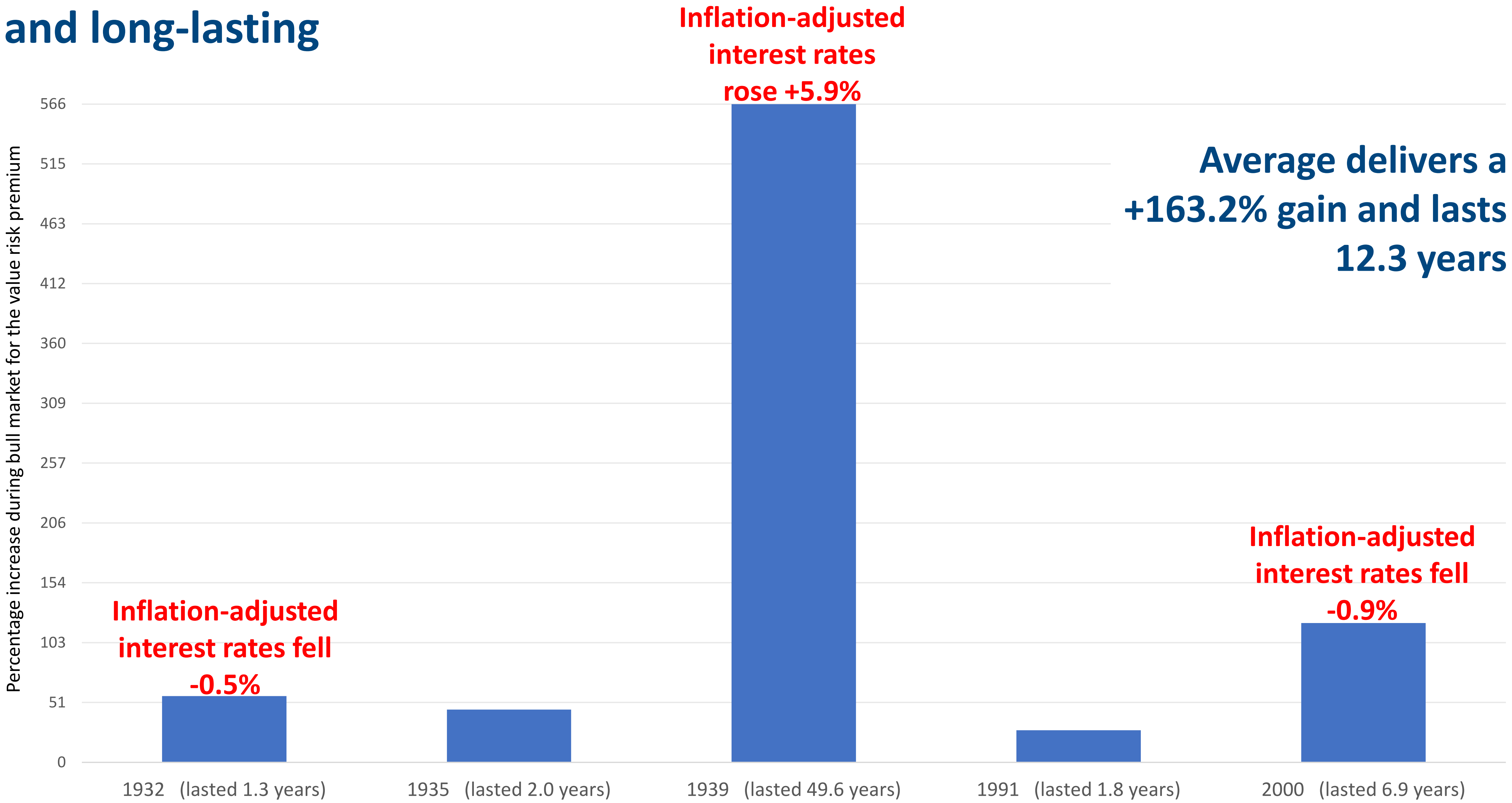
Bull markets for the value risk premium have been both bountiful and long-lasting



Bull markets for the value risk premium have been both bountiful and long-lasting

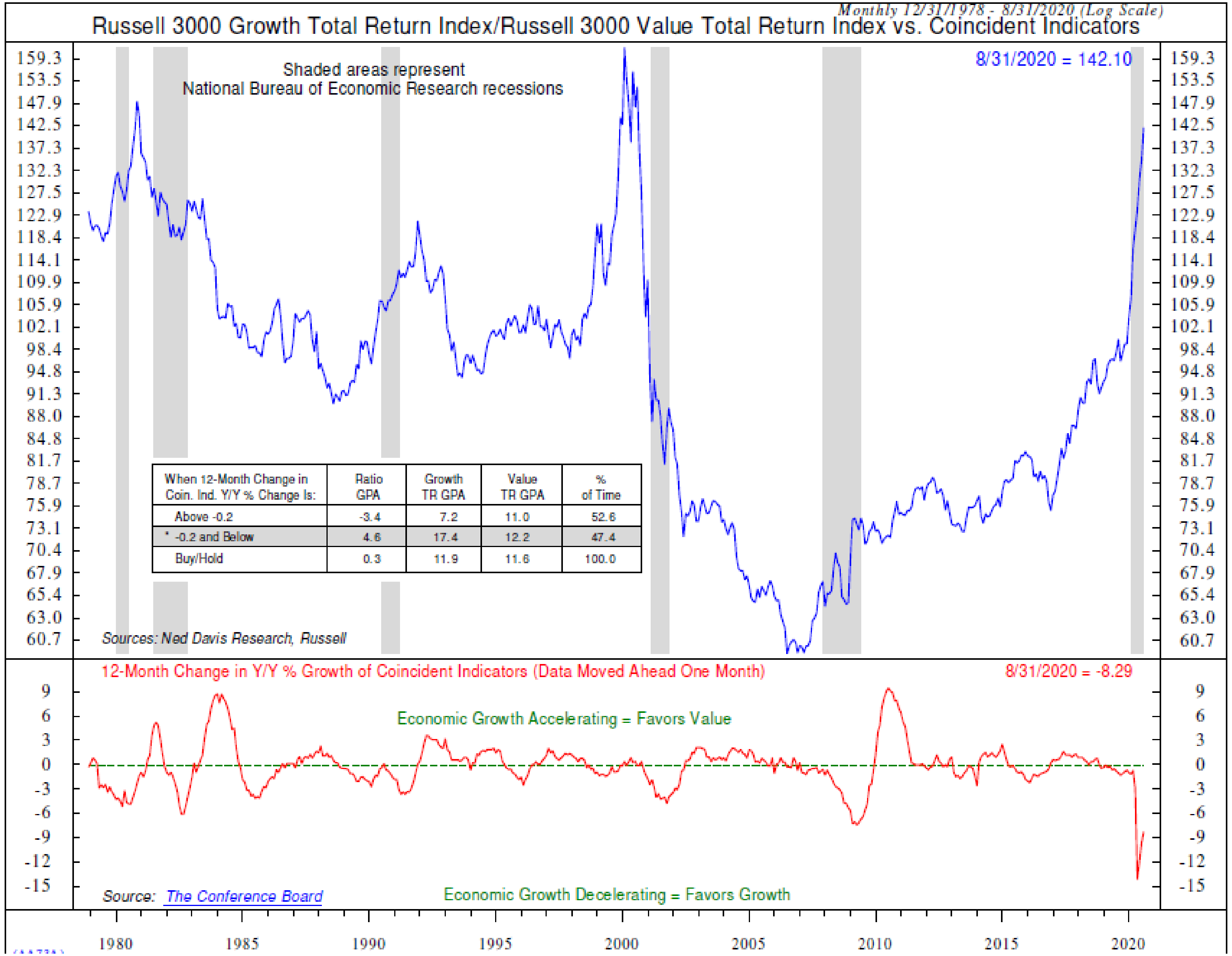


Bull markets for the value risk premium have been both bountiful and long-lasting



NDR suggests it is not interest rates, but economic growth

Decelerating economic growth favors Growth



When 12-Month Change in Coin. Ind. Y/Y % Change Is:	Ratio GPA	Growth TR GPA	Value TR GPA	% of Time
Above -0.2	-3.4	7.2	11.0	52.6
* -0.2 and Below	4.6	17.4	12.2	47.4
Buy/Hold	0.3	11.9	11.6	100.0

Since cyclical Value stocks are tied to the economy and many Growth stocks can generate EPS growth regardless of economic conditions, Growth has tended to outperform Value when economic growth has been decelerating **(chart, left)**.

The case for high dividend stocks

The case for value, in general and right now

High dividend stocks as a best possible expression of value

- Current income
- Zombie filter
- Sustainability
- Profitability
- Growing income
- Tangibles vs intangibles

A better expression of value

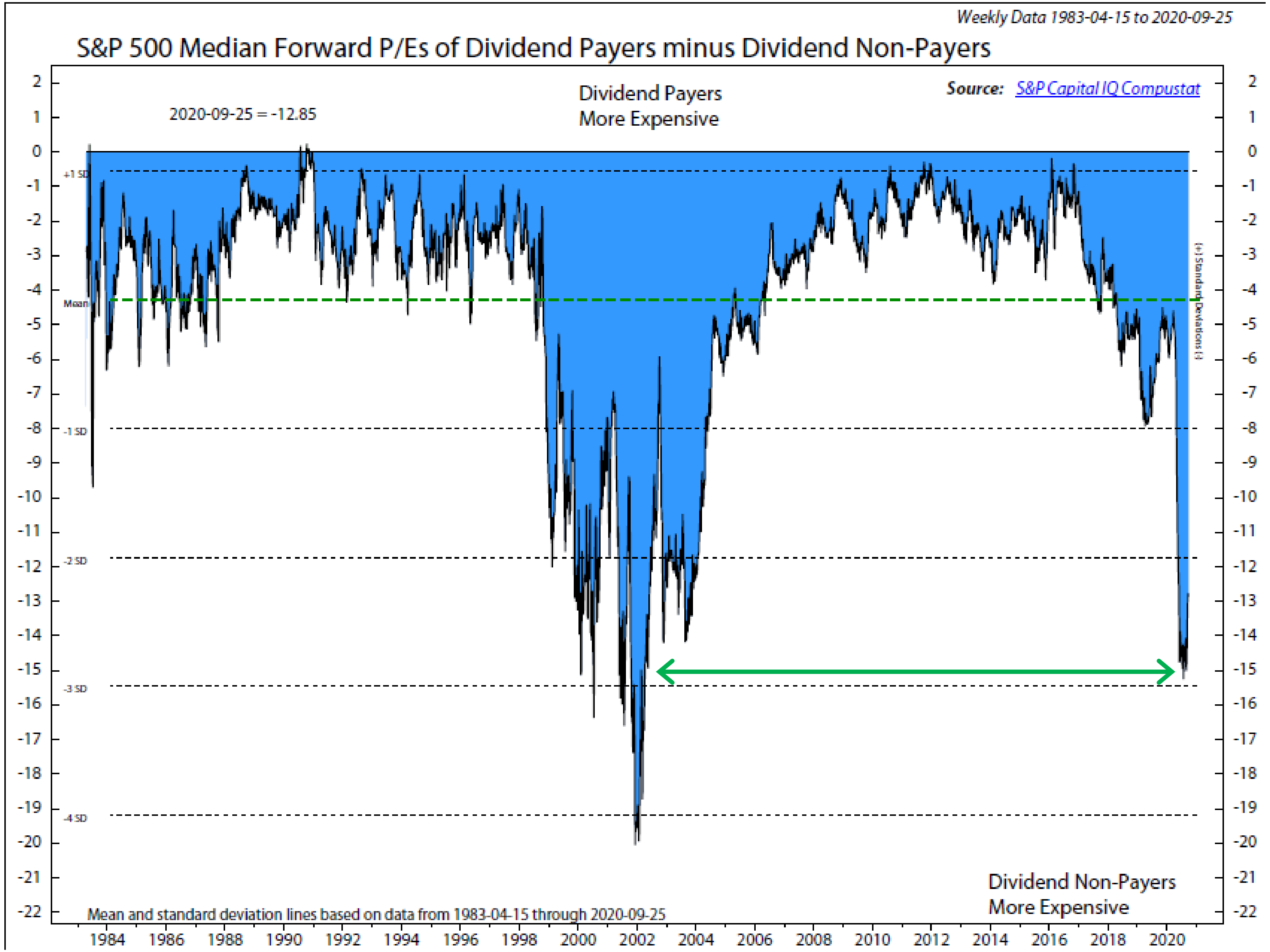
- Current income
- Zombie filter
- Sustainability
- Profitability
- Growing income
- Tangibles vs intangibles

With interest rates so low, we have a need for current income

- Solution
- Build out a value portfolio centered on high current income

And, dividend paying stocks are the most undervalued in 18 years

Dividend Payers cheap vs Non-Payers



With so much free money, zombies are proliferating

- By some estimates, 19% of all US companies are zombies
- Any value portfolio must filter out prospective zombies
- One more reason to emphasize high current income

Sustainability - the curse of any high income portfolio

- Portfolios built to emphasize high current income
- Must avoid the trap of sustainability
- Appropriate filters must be engaged

Profitability - a dependably rewarded factor

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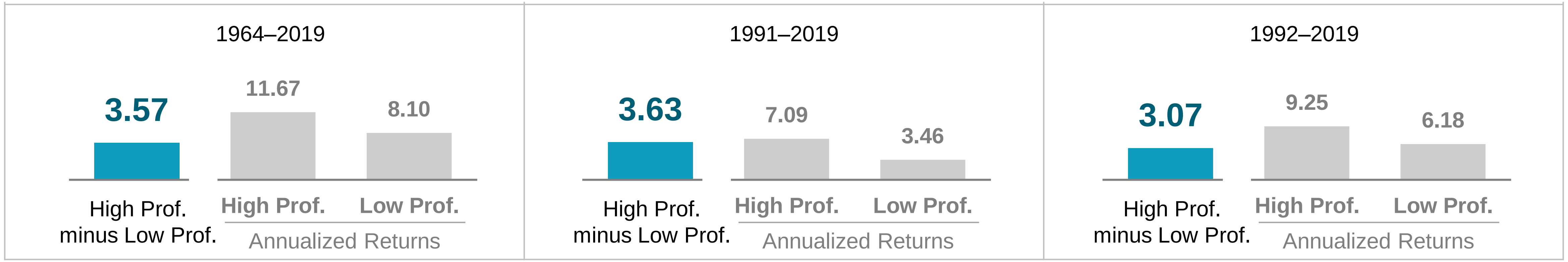
US Stocks | Developed ex US Markets Stocks | Emerging Markets Stocks

Profitability

Relative performance of high profitability stocks vs. low profitability stocks (%)



- Ideally, we reflect the profitability factor within our high current income value portfolio

Growing income - the sweet spot for any high income portfolio

- Historically, dividend paying stocks have meaningfully outperformed non-dividend paying stocks

- But more important . . . Stocks with growing dividends have outperformed even more

- Ideally, a portfolio emphasizing high current income will also seek growing income and therefore growing dividends

Tangibles vs intangibles

- Campbell R. Harvey

- Report of Value’s Death May Be Greatly Exaggerated
- SSRN working paper, August 2020
- Harvey, Arnott, Kalesnik, Linnainmaa

Value portfolios must not be based on book value

The world has changed

Shift from manufacturing to a service-based economy means that traditional book value has become less relevant.

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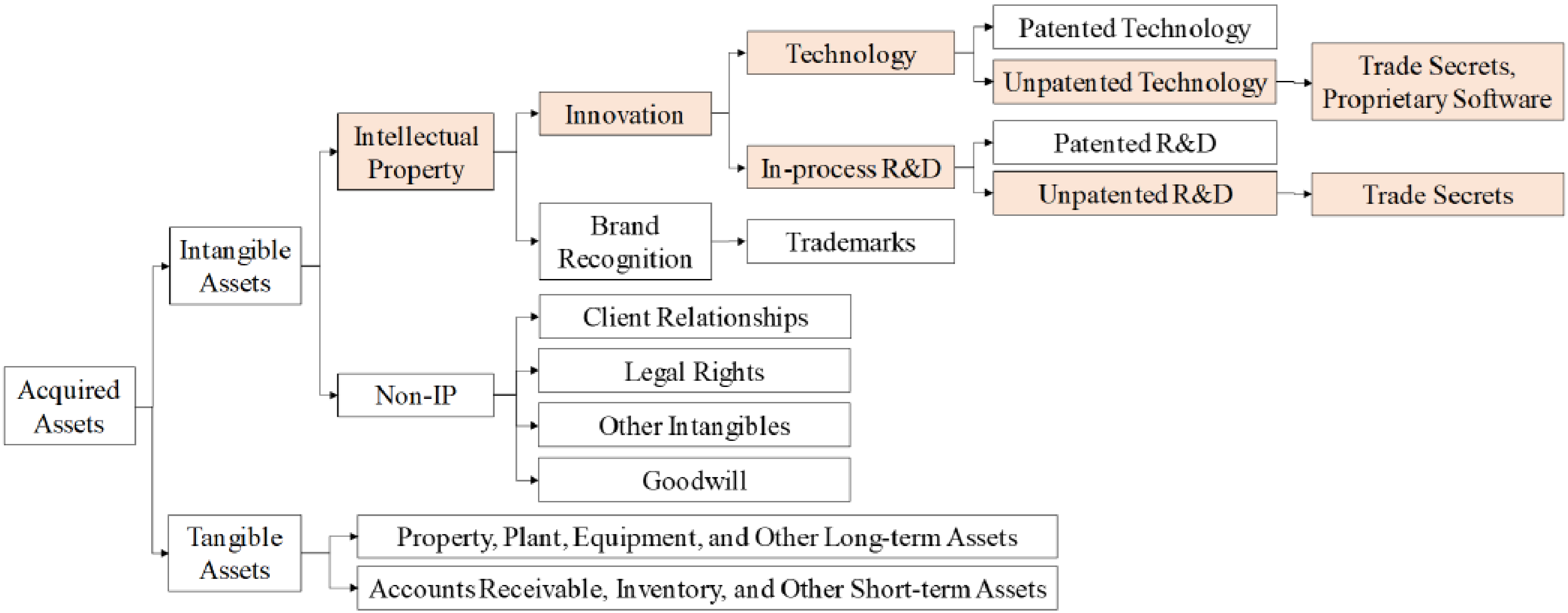
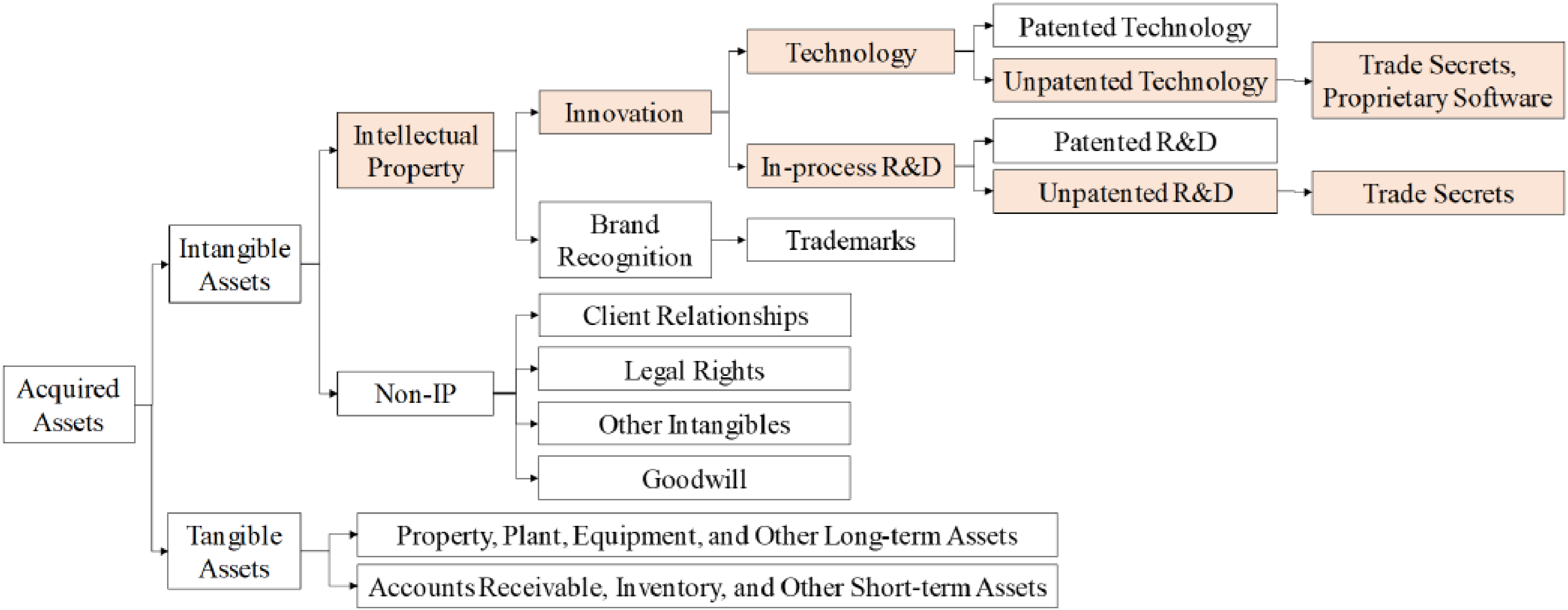
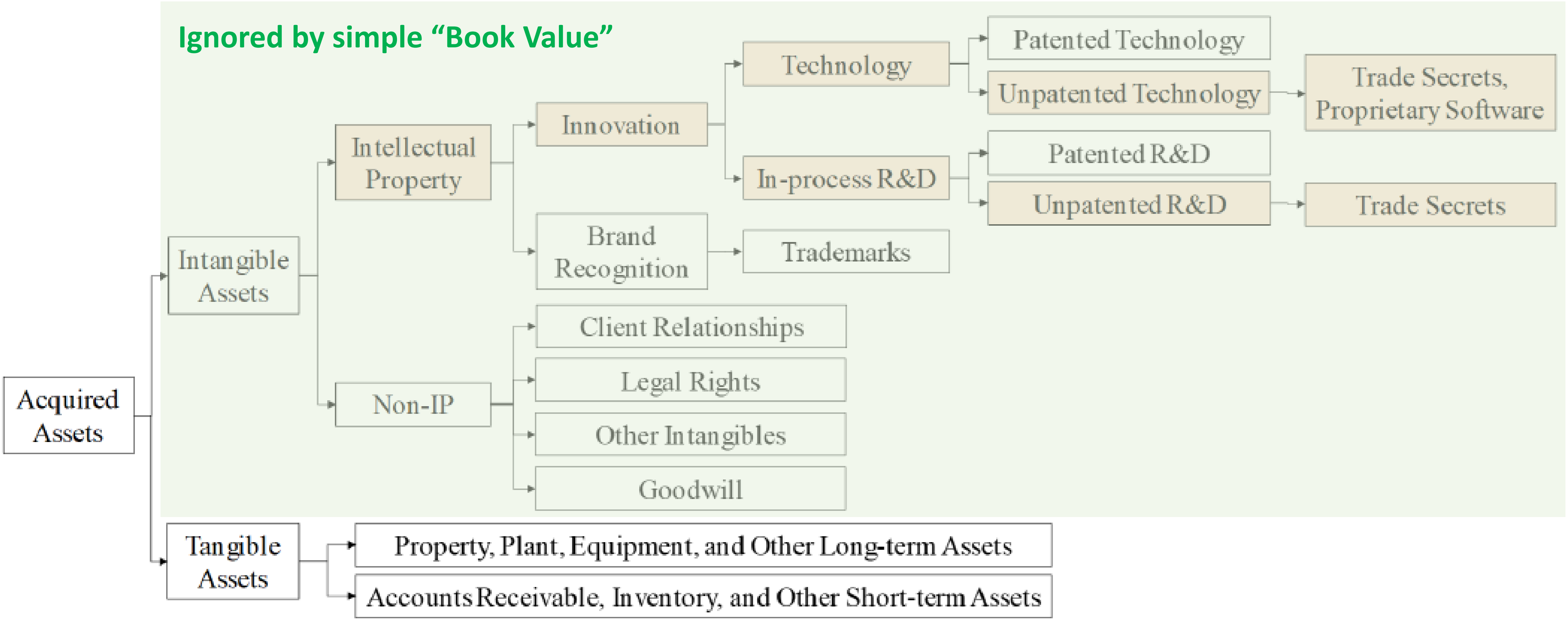
What are intangibles?



Value portfolios must not be based on book value, continued



Value portfolios must not be based on book value, continued



Julex provides a superior solution

High Dividend Strategy - A better expression of value

Julex Capital - the firm

- **Employee-owned, established 2012**

- **Quantitative, rules-based investment process**

- **Strategy Focus:**
  - Tactical strategies – limit loss
  - Quantitative equity strategies - generate alpha

- **Experienced Team**
  - Institutional investment experience
  - Portfolio management team includes 3 Ph.D.'s

- **GIPS compliance verified by ACA Performance Services**

The investment professionals

Team	Role	Experience	Education
Henry Ma Ph.D., CFA	President Chief Investment Officer	Geode Capital – Hedge Fund Manager Loomis Sayles – Director of Quantitative Research Fortis Investments - Director of Quantitative Research Sun Life Financial– Portfolio Manager	Ph.D. Economics – Boston University BA, MA – Peking University
George Xiang Ph.D., CFA	Portfolio Manager Research	State Street Global Advisors (SSGA) – Head of Quantitative Research Loomis Sayles – Senior Quantitative Analyst Conseco Capital – Quantitative Research Manager	Ph.D., Mathematics – Purdue University BA – Nankai University
Frank Zhuang Ph.D.	Portfolio Manager Research	Ericsson – Senior Engineer Nortel, Alcatel/Lucent - Senior Research Scientist	Ph.D. Electric Engineering – University of Maryland MS – West Virginia University
Jeffrey Megar CFA	Investment Committee Member	F-Squared Investments – Senior Vice President State Street Global Advisors – Senior Portfolio Manager Fortis Investments – Senior Portfolio Manager Cypress Tree Investment Management	MBA – Northeastern University BA – Framingham State University
Liam Flaherty	Research	MFS Investments - Independent Contractor MassMutual - Internship	BA – Babson College
Bo Wang	Research		Ph.D. Candidate, Economics – Boston College BA – Renmin University of China

High Dividend - Strategy highlights

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High Dividend & Excess Return	Quantitative and Disciplined Approach	Robust and Consistent Factors
• Expected 4-5% dividend yield • Outperform Russell 1000 Index over the long run • Semi-Annual Rebalanced: Mar/Sep.	• Model driven investment process • No emotional bias	• Consistent dividend • Quality companies

The investment process

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US Top 1500 Stocks

Step 1: Dividend Consistency

- Positive dividend growth
- Payout ratio <1 (remove top 5% extreme payout ratio)
- Free cash flow > 75% * dividend

Step 2: Quality

- Remove bottom 50% companies with the lowest ROA
- Remove companies with negative equity

Step 3: Price Momentum

- Remove 20% companies with the weakest price momentum

- Maximum 15 stocks in each sector
- Maximum 6 stocks in each industry
- Four Groups: Financial, Cyclical, non-cyclical and commodity-related

Select a portfolio of 25 stocks with the highest dividend scores

Dividend score
= (universal ranking
+ group ranking + sector ranking)/3

The investment process

- Current income
- Profitability
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US Top 1500 Stocks

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The investment process

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US Top 1500 Stocks

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- Positive dividend growth
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- Free cash flow > 75% * dividend

- Zombie filter
- Sustainability
- Profitability

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Select a portfolio of 25 stocks with the highest dividend scores

Dividend score = (universal ranking + group ranking + sector ranking)/3

The portfolio - Sep 30, 2020

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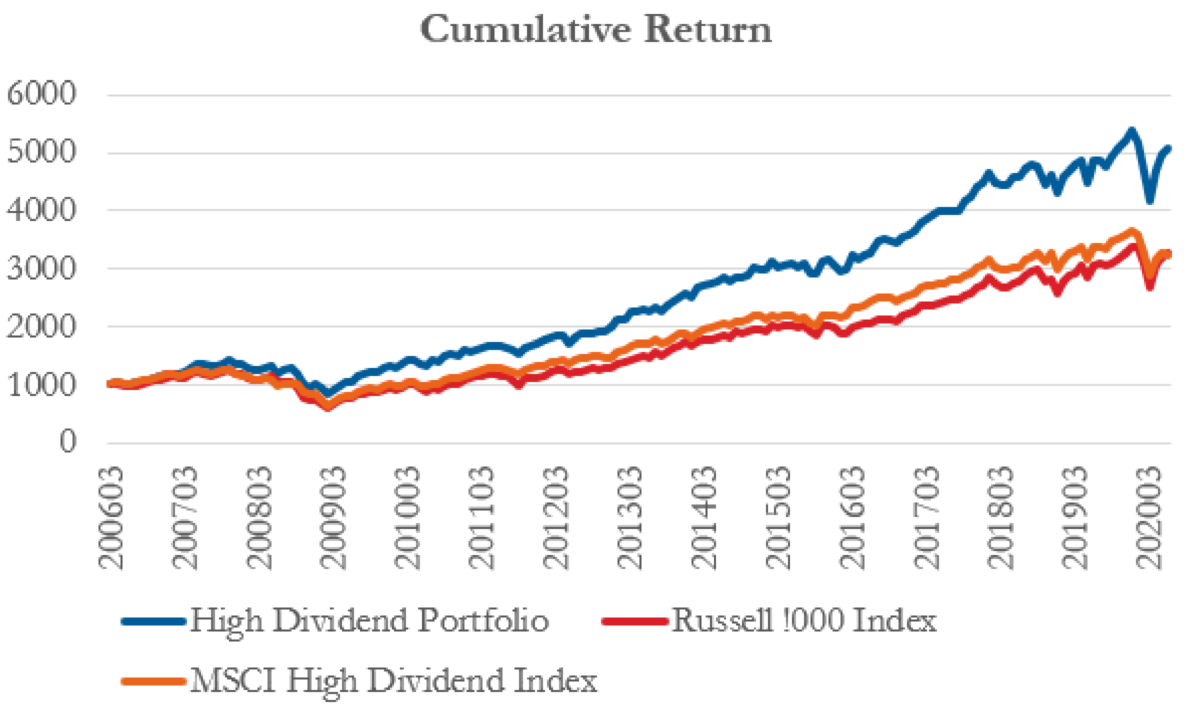
Symbol	Company	Sector	Industry	Yield	Weight
MRK	Merck & Co Inc	Healthcare	Drug Manufacturers	2.81	4%
KO	Coca-Cola Co	Consumer Defensive	Beverages - Non-Alcoholic	3.28	4%
PFE	Pfizer Inc	Healthcare	Drug Manufacturers	4.06	4%
NVS	Novartis AG	Healthcare	Drug Manufacturers	3.56	4%
CSCO	Cisco Systems Inc	Technology	Hardware	3.38	4%
ABBV	AbbVie Inc	Healthcare	Drug Manufacturers	5	4%
SNY	Sanofi SA	Healthcare	Drug Manufacturers	3.4	4%
BBL	BHP Group PLC	Basic Materials	Metals & Mining	6.11	4%
GSK	GlaxoSmithKline PLC	Healthcare	Drug Manufacturers	5.14	4%
MMM	3M Co	Industrials	Industrial Products	3.57	4%
RIO	Rio Tinto PLC	Basic Materials	Metals & Mining	6.13	4%
EMR	Emerson Electric Co	Industrials	Industrial Products	2.85	4%
PAYX	Paychex Inc	Industrials	Business Services	3.25	4%
K	Kellogg Co	Consumer Defensive	Consumer Packaged Goods	3.3	4%
LYB	LyondellBasell Industries NV	Basic Materials	Chemicals	6.14	4%
MXIM	Maxim Integrated Products Inc	Technology	Semiconductors	2.77	4%
STX	Seagate Technology PLC	Technology	Hardware	5.49	4%
NTAP	NetApp Inc	Technology	Hardware	4.12	4%
PKG	Packaging Corp of America	Consumer Cyclical	Packaging & Containers	3.02	4%
SNA	Snap-on Inc	Industrials	Industrial Products	2.85	4%
HBI	Hanesbrands Inc	Consumer Cyclical	Manufacturing - Apparel & Accessories	3.86	4%
INGR	Ingredion Inc	Consumer Defensive	Consumer Packaged Goods	3.15	4%
NATI	National Instruments Corp	Technology	Software	2.87	4%
MSM	MSC Industrial Direct Co Inc	Industrials	Industrial Distribution	4.46	4%
MCY	Mercury General Corp	Financial Services	Insurance	5.6	4%
Total				4.0	100%

Fundamental portfolio characteristics

	High Dividend Stock Portfolio	Vanguard Russell 1000 Index Fund
# of Securities	25	1,009
Market Capitalization	70,871.1	409,136.0
Active Share	96.2	--
Dividend Yield	4.0	1.7
Price/Earnings	15.7	26.7
P/E using FY1 Est	14.2	24.3
P/E using FY2 Est	13.3	20.7
Est 3-5 Yr EPS Growth	5.4	12.8
Price/Cash Flow	10.5	13.8
Price/Book	3.7	3.5
Price/Sales	1.8	2.4
ROE	29.6	23.5
ROA	11.16	9.34
Port. MPT Tracking Error	10.50	--
Port. MPT Beta	0.92	1.00
Port. MPT Volatility	32.04	33.21

Back tested performance history - Showing what you want to see

March 2006-June. 2020	High Dividend Portfolio	Russell 1000 Index	MSCI High Dividend Index
Annual Return	12.0%	8.7%	8.6%
Standard Deviation	14.2%	15.3%	13.8%
Sharpe Ratio (risk free rate =0%)	0.84	0.57	0.62
Maximum Drawdown	-41.2%	-51.1%	-50.1%
Dividend Yield	4.32%	2.03%	3.44%



Year	High Dividend Portfolio	Russell 1000 Index	MSCI High Dividend Index
2006 (Mar. – Dec)	17.8%	12.1%	17.7%
2007	15.0%	5.8%	0.0%
2008	-25.6%	-37.6%	-27.6%
2009	31.8%	28.4%	18.4%
2010	19.8%	16.1%	15.9%
2011	7.2%	1.5%	14.3%
2012	16.6%	16.4%	10.6%
2013	30.1%	33.1%	28.9%
2014	15.7%	13.2%	14.9%
2015	2.3%	0.9%	0.7%
2016	17.4%	12.1%	16.3%
2017	24.2%	21.7%	19.5%
2018	-3.6%	-4.8%	-2.3%
2019	25.1%	31.4%	22.5%
2020 (Jan - Jun)	-5.9%	-2.8%	-11.4%

Note: The performance results shown on this slide are HYPOTHETICAL based on back test modeled results and are gross returns before investment management fees.

Data Source: FactSet, Julex Capital Management, Gurufocus

Back tested performance history - Showing what you want to see

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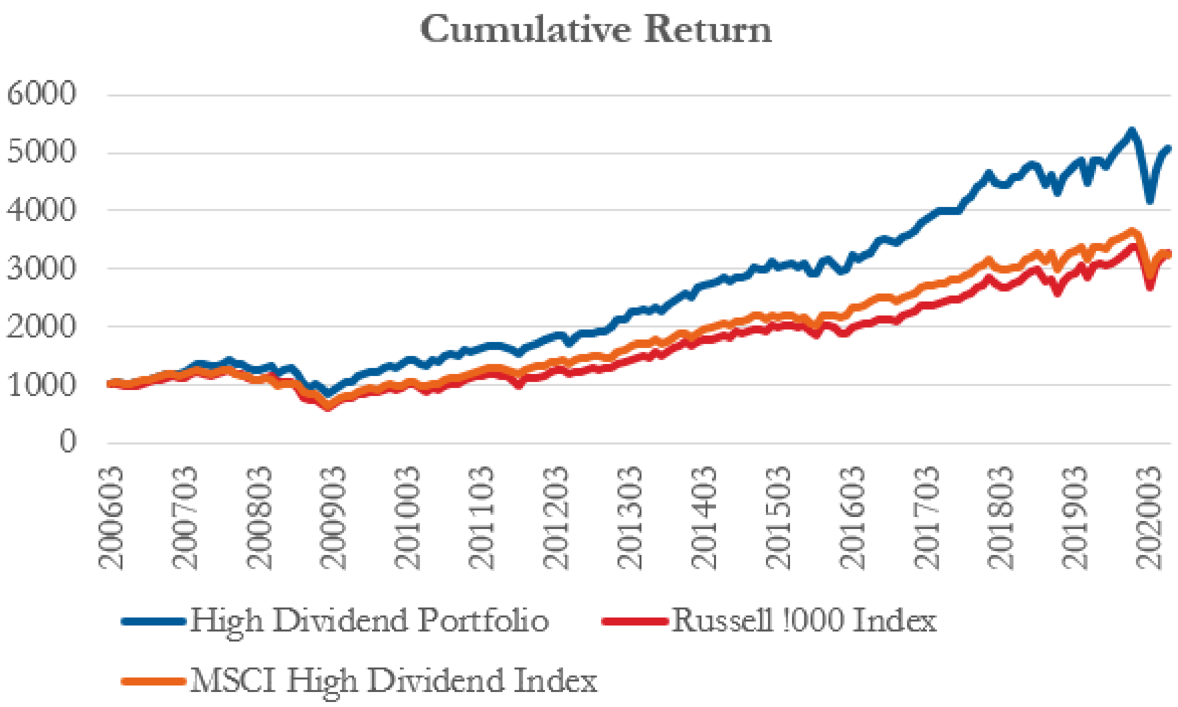

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2011	7.2%	1.5%	14.3%
2012	16.6%	16.4%	10.6%
2013	30.1%	33.1%	28.9%
2014	15.7%	13.2%	14.9%
2015	2.3%	0.9%	0.7%
2016	17.4%	12.1%	16.3%
2017	24.2%	21.7%	19.5%
2018	-3.6%	-4.8%	-2.3%
2019	25.1%	31.4%	22.5%
2020 (Jan - Jun)	-5.9%	-2.8%	-11.4%

And for Q3, the portfolio earned **+6.2%** versus the High Dividend Index at **+3.8%**

Note: The performance results shown on this slide are HYPOTHETICAL based on back test modeled results and are gross returns before investment management fees.

Data Source: FactSet, Julex Capital Management, Gurufocus

Friday, Oct 23rd at 11am Eastern

Today, are bonds an “investment” or just a “speculation”?

For more information contact

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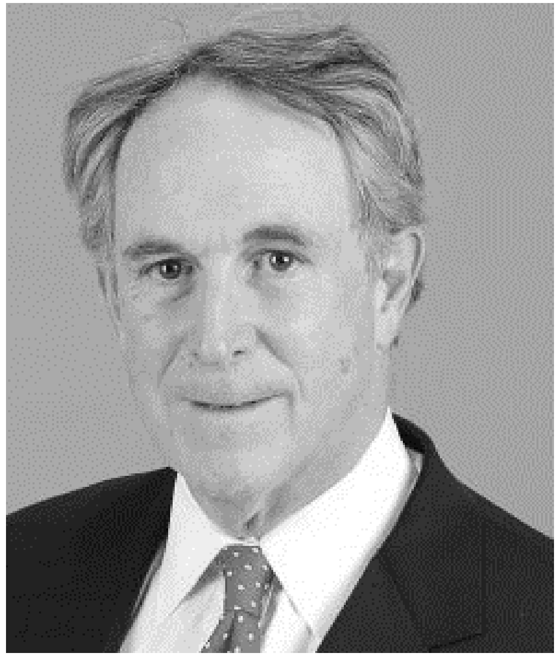

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