

Radian Group Inc. (RDN)

\$16.05 (As of 09/02/20)

Price Target (6-12 Months): **\$17.00**

Long Term: 6-12 Months

Zacks Recommendation:
Neutral

(Since: 08/11/20)

Prior Recommendation: Underperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

5-Strong Sell

Zacks Style Scores:

VGM:C

Value: A

Growth: D

Momentum: D

Summary

Radian Group remains focused on improving mortgage insurance portfolio to drive long-term earnings growth. Business restructuring intensifies its focus on core business and services with higher-growth potential, ensuring predictable and recurring fee-based revenue stream. Based on strong credit characteristics of new loans insured, declining claim payments aid the company. Solid persistency and rise in new mortgage insurance business are driving insurance in force to increase. Shares of Radian Group have underperformed the industry in a year's time. Moreover, escalating expenses tend to weigh on operating margin expansion. Increased provision for losses in mortgage insurance business concerns us. Given the pandemic, the company expects slowdown in purchase loan volume. Nevertheless, solid capital position enables the company to deploy capital.

Data Overview

52-Week High-Low	\$26.32 - \$9.53
20-Day Average Volume (Shares)	1,860,520
Market Cap	\$3.1 B
Year-To-Date Price Change	-36.2%
Beta	1.66
Dividend / Dividend Yield	\$0.50 / 3.1%
Industry	Insurance - Multi line
Zacks Industry Rank	Bottom 32% (170 out of 251)

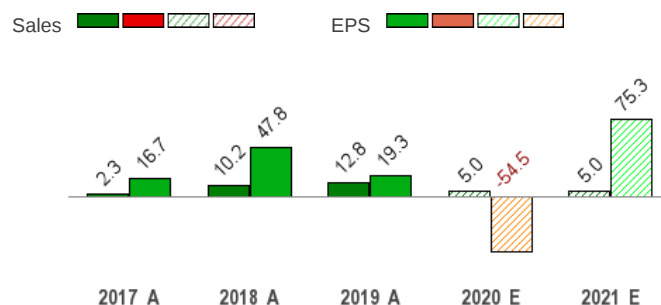
Last EPS Surprise	-289.5%
Last Sales Surprise	NA
EPS F1 Estimate 4-Week Change	-25.8%
Expected Report Date	11/04/2020
Earnings ESP	0.0%

P/E TTM	7.6
P/E F1	11.0
PEG F1	2.2
P/S TTM	2.1

Price, Consensus & Surprise



Sales and EPS Growth Rates (Y/Y %)



Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021					1,456 E
2020	351 A	289 A			1,387 E
2019	309 A	343 A	325 A	344 A	1,321 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$0.56 E	\$0.58 E	\$0.60 E	\$0.61 E	\$2.56 E
2020	\$0.80 A	-\$0.36 A	\$0.48 E	\$0.60 E	\$1.46 E
2019	\$0.73 A	\$0.80 A	\$0.81 A	\$0.86 A	\$3.21 A

*Quarterly figures may not add up to annual.

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 09/02/2020. The reports text is as of 09/03/2020.

Overview

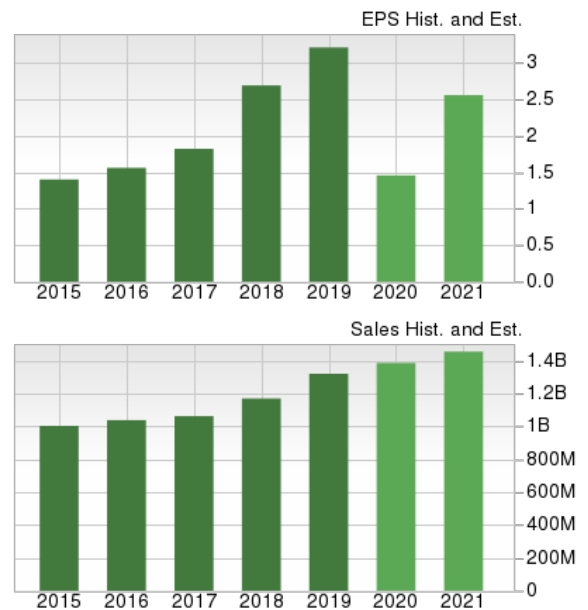
Founded in 1977 and headquartered in Philadelphia, PA, Radian Group Inc. is a credit enhancement company which supports homebuyers, mortgage lenders, loan servicers and investors with a suite of private mortgage insurance and related risk-management products and services. Radian trades on the New York Stock Exchange under the symbol RDN.

The company had two business segments — Mortgage Insurance and Real Estate Services.

- **Mortgage Insurance (99% of 2019 net premiums earned)** – This segment provides credit-related insurance coverage, principally through private mortgage insurance and risk management services, to mortgage lending institutions. The company conducts mortgage insurance business primarily through Radian Guaranty, its principal mortgage insurance subsidiary. Mortgage insurance is of immense importance in the U.S. housing finance system as it offers home ownership at affordable rates and pacify risks related to residential mortgage loans. In 2019, net premiums earned in the segment increased 12.7% year over year to \$1.1 billion, mainly attributable to strong volume growth in the mortgage insurance business.

- **Services (1%)** – This segment is primarily a fee-for-service business that offers a broad array of mortgage, real estate and title services to market participants across the mortgage and real estate value chain. These services include technology and turn-key solutions, which provide information and other resources used to originate, evaluate, acquire, securitize, service and monitor residential real estate and loans secured by residential real estate. These services are primarily provided to mortgage lenders, financial institutions, investors and government entities. The company extends Services offerings primarily through its subsidiaries, including Clayton, Green River Capital, Radian Settlement Services and Red Bell.

The company made a series of acquisitions to enhance its product offerings. In 2018, it acquired the businesses of EnTitle Direct (in March) and Independent Settlement Services (in November), as well as the assets of Five Bridges (in December), to enhance its product offerings.



Source: Zacks Investment Research

Reasons To Buy:

- ▲ **Price Performance** – Shares of Radian Group have declined 28.5% in the past year, compared with the industry's decline of 13.6%. Nonetheless, its solid fundamentals should help shares bounce back.
 - ▲ **Improvement in the quality and size of mortgage insurance in force** – Radian's mortgage insurance portfolio is expected to create a strong foundation for future earnings. In the second quarter of 2020, new mortgage insurance written (NIW) increased 37% year over year backed by rebound in the housing market. NIW in the second quarter aided the company to grow primary insurance in force by 5% to \$241.3 billion. The company expects to write new mortgage insurance business of more than \$75 billion in 2020. Given the increase in persistency, insurance in force is expected to rise going forward, thereby enhancing the company's strong foundation for future earnings. Moreover, the company remains focused on improving its mortgage insurance portfolio, the main catalyst of long-term earnings growth.
 - ▲ **Declining claim payments** – There has been a significant reduction in the company's claims' payments over the last few years. In the second quarter of 2020, net claims paid were \$22.8 million, down 29.6% from the prior-year figure. Given the strong credit characteristics of the new loans insured, we expect the company to see fewer claims than before.
 - ▲ **Maintaining capital in compliance with regulations** –The company has been able to maintain its capital within the mandated level. As of Jun 30, 2020, Radian Guaranty's risk-to-capital ratio was 13.3:1 compared with 13.6:1 as of Dec 31, 2019. Nonetheless, excess available resources to support PMIERS were \$2.4 billion as of Jun 30, 2020, 73% above Radian Guaranty's minimum required assets of about \$3.2 billion. During the second quarter, excess available resources to support PMIERS increased by \$361 million.
 - ▲ **Strengthening Capital Position** – Radian Group took a few initiatives that will consolidate its capital structure by extending debt maturities while enhancing financial flexibility. The company strengthened available liquidity by extending the term of existing credit facility and issuing \$525 million of senior notes due 2025. As of Jun 30, Radian Group's capital position remains solid with \$1.1 billion of available liquidity.
- Also, the company has been effectively trying to lower its debt level over the last few years. However, as of Jun 30, 2020, debt to capital ratio deteriorated 800 bps to 26% from 2019 end level but was better than the industry average of 30.3%. Further, times interest earned ratio has been improving over the years. The improvement in this ratio indicates that the firm will be able to meet current obligations in the near future without any difficulties. Though times interest earned of 11.3 in the second quarter of 2020 was lower than year-ago figure of 13.7, it was better than the industry average of 4.3. Strong capital position reflects financial strength
- ▲ **Capital Deployment** - Radian Group maintains a solid balance sheet with sufficient liquidity and strong cash flows. A strong capital position helps Radian Group deploy capital via share repurchases and dividend hikes that enhance shareholders value. In Feb 2020, the board of directors hiked its quarterly dividend to 12.5 cents per share from its prior dividend payout of 0.25 cents. Its current dividend yield is 3.1%, which compares favorably with the industry average of 2.8%. However, on Mar 25, 2020, the company has suspended its share repurchase program due to the outbreak of the COVID-19 pandemic.

Radian is poised for long-term growth on declining delinquency, lower levels of paid claims and an improving risk-based capital ratio, which reflect an improvement in its operating environment.

Reasons To Sell:

▼ **Rising Expenses to Hurt Margin Expansion** – Over the last few years, Radian Group has been witnessing rising expenses, primarily owing to increase in provision for loss, policy acquisition costs, cost of services, other operating expenses, loss on extinguishment of debt, impairment of goodwill, and amortization & impairment of other intangible assets. Total expenses surged 119% year over year in the second quarter of 2020 on account of higher provision for losses. Higher expenses continue to weigh on margin expansion. Net margin in the second quarter of 2020 contracted 1330 year over year. The insurer should strive to generate a higher revenue growth rate than the rate of increase in expenses, else, expenses will likely tend to weigh on the operating margin expansion.

New stricter regulations, increasing mortgage rates pose, below the mark ratings, reduction of annual premium of FHA are some of the headwinds faced by the company over the near term.

▼ **Increased Provision for Losses in Mortgage Insurance Business** – The company's provision for losses increased due to the high vulnerability of the mortgage insurance business in the market. The metric rose more than six-fold in the second quarter of 2020 resulting in lower net income. Given the pandemic, the company expects slowdown in purchase loan volume. Also, the company estimates considerable increase in mortgage finance volumes to result in lower persistency across insurance portfolio.

▼ **Low Rate Environment**- A low interest rate environment has been weighing on investment portfolio yield over time as the company reinvests maturing assets and operating cash flows. Given that the Fed has stated that there will be no recovery in rate any time soon, we expect investment portfolio yield to continue to suffer.

Last Earnings Report

Radian Group Falls Short of Q2 Earnings Estimates

Radian Group reported second-quarter 2020 operating loss of 36 cents per share in contrast to the Zacks Consensus Estimate of earnings of 19 cents and the year-ago earnings of 80 cents.

The company witnessed elevated loss provision due to the increase in the number of new defaults, which include defaults of loans subject to forbearance programs implemented, attributable to the COVID-19 pandemic.

Quarter Ending	06/2020
Report Date	Aug 07, 2020
Sales Surprise	NA
EPS Surprise	-289.47%
Quarterly EPS	-0.36
Annual EPS (TTM)	2.11

Quarter in Details

Operating revenues declined 15.7% year over year to \$289 million, attributable to lower net premiums earned, services revenue, net investment income and other income.

MI New Insurance Written grew 37% year over year to \$25.5 billion backed by rebound in the housing market.

Primary mortgage insurance in force was \$241.3 billion as on Jun 30, 2020, up 5% year over year.

Persistency — percentage of mortgage insurance in force that remains in the company's books after a 12-month period — was 70.2% as of Jun 30, 2020, down 1320 basis points year over year.

Primary delinquent loans were 69,742 as of Jun 30, 2020, up more than three-fold year over year.

Total expenses surged 119% year over year to \$406.7 million on account of higher provision for losses.

Segment Update

Earlier, the company reported results under two segments – Mortgage Insurance and Services. This year in January, Radian decided to divest Clayton Services LLC to Covius Holdings. Apart from reorganizing its Services segment, the deal highlighted the company's focus on growing its core mortgage and real estate businesses. Hence, from the first quarter of 2020, the company started reporting results under Mortgage and Real Estate segments.

Net premiums earned by the **Mortgage** segment were \$247.6 million, down 16.4% year over year. Claims paid were \$22.8 million in the quarter under review, down 29.6% year over year. Loss ratio deteriorated to 122.8% from year-ago figure of 15.9%.

The **Real Estate** segment reported a 5.4% year-over-year decrease in total revenues to \$26.1 million. Adjusted earnings before interest, income taxes, depreciation and amortization (Real Estate adjusted EBITDA) was negative \$0.7 million, compared with negative \$0.5 million in the year-ago quarter.

Financial Update

As of Jun 30, 2020, Radian Group had solid cash balance of \$68.4 million, down 26.3% from 2019-end level. Debt to capital ratio deteriorated 800 bps to 26% from 2019 end level.

Book value per share, a measure of net worth, grew 13% year over year to \$20.82 as of Jun 30, 2020.

Adjusted net operating return on equity was (7.1%) versus 18.2% in the year-ago quarter.

Risk-to-capital ratio of Radian Guaranty as of second-quarter end was 13.3:1, lower than 13.6:1 from 2019 end level.

Excess available resources to support PMIERS were \$2.4 billion as of Jun 30, 2020, 73% above Radian Guaranty's minimum required assets of about \$3.2 billion. During the second quarter, excess available resources to support PMIERS increased by \$361 million.

Recent News

Radian Group Declares Quarterly Dividend — Aug 12, 2020

The board of directors of Radian Group declared a quarterly dividend of 125 cents per share. The dividend will be paid out on Sep 4 to shareholders of record as of Aug 24.

Radian Group Unveils New Digital Platform – Jul 29, 2020

Radian Group has introduced a digital platform known as MyRadian in a bid to enable customers to access valuation and asset management services at one convenient location and with a single login.

Valuation

Radian's shares are down 36.2% and 28.5% in the year-to-date period and over the trailing 12-month period, respectively. Stocks in the Zacks sub-industry and the Zacks Finance sector are down 23.5% and 13.9% in the year-to-date period, respectively. Over the past year, the Zacks sub-industry and sector are down 13.6% and 5.1%, respectively.

The S&P 500 index are up 6.9% in the year-to-date period and 17.5% in the past year.

The stock is currently trading at 0.77x trailing 12-month book value, which compares to 1.2x for the Zacks sub-industry, 2.58x for the Zacks sector and 4.66x for the S&P 500 index.

Over the past five years, the stock has traded as high as 1.68x and as low as 0.49x, with a 5-year median of 1.23x. Our Neutral recommendation indicates that the stock will perform in-line than the market. Our \$17 price target reflects 0.81x trailing 12- month book value.

The table below shows summary valuation data for RDN

Valuation Multiples - RDN					
		Stock	Sub-Industry	Sector	S&P 500
P/B TTM	Current	0.77	1.2	2.58	4.66
	5-Year High	1.68	1.98	2.91	4.76
	5-Year Low	0.49	0.85	1.72	2.83
	5-Year Median	1.23	1.48	2.54	3.76
P/S F12M	Current	2.31	0.77	6.23	4.4
	5-Year High	4.41	1.74	6.67	4.4
	5-Year Low	1.56	0.77	4.97	2.53
	5-Year Median	2.90	1.26	6.07	3.07
P/E F12M	Current	7.3	8.40	16.94	23.94
	5-Year High	12	12.61	16.94	23.94
	5-Year Low	3.29	6.62	11.6	15.25
	5-Year Median	7.82	9.92	14.26	17.6

As of 09/02/2020

Industry Analysis Zacks Industry Rank: Bottom 32% (170 out of 251)



Source: Zacks Investment Research

Top Peers

Company (Ticker)	Rec	Rank
Arch Capital Group Ltd. (ACGL)	Neutral	3
Aegon NV (AEG)	Neutral	4
American International Group, Inc. (AIG)	Neutral	3
Essent Group Ltd. (ESNT)	Neutral	4
FBL Financial Group, Inc. (FFG)	Neutral	3
The Hartford Financial Services Group, Inc. (HIG)	Neutral	3
MGIC Investment Corporation (MTG)	Neutral	3
Prudential Financial, Inc. (PRU)	Neutral	3

The positions listed should not be deemed a recommendation to buy, hold or sell.

Industry Comparison Industry: Insurance - Multi Line				Industry Peers		
	RDN	X Industry	S&P 500	ACGL	ESNT	MTG
Zacks Recommendation (Long Term)	Neutral	-	-	Neutral	Neutral	Neutral
Zacks Rank (Short Term)	5	-	-	3	4	3
VGM Score	C	-	-	C	C	C
Market Cap	3.07 B	3.33 B	24.30 B	13.04 B	4.25 B	3.23 B
# of Analysts	3	2	14	4	3	3
Dividend Yield	3.12%	2.48%	1.6%	0.00%	1.69%	2.51%
Value Score	A	-	-	B	C	A
Cash/Price	0.45	0.34	0.07	0.24	0.30	0.12
EV/EBITDA	3.37	3.67	13.46	7.13	4.42	3.89
PEG F1	2.22	1.22	3.09	3.25	NA	1.72
P/B	0.77	0.81	3.25	1.10	1.17	0.74
P/CF	4.29	7.15	13.12	10.12	6.46	4.63
P/E F1	11.12	9.80	22.15	32.46	11.44	8.58
P/S TTM	2.10	0.79	2.57	1.80	4.62	2.63
Earnings Yield	9.10%	9.56%	4.29%	3.08%	8.73%	11.62%
Debt/Equity	0.40	0.24	0.70	0.33	0.00	0.19
Cash Flow (\$/share)	3.74	3.45	6.93	3.17	5.85	2.06
Growth Score	D	-	-	D	D	D
Historical EPS Growth (3-5 Years)	21.54%	8.76%	10.41%	14.06%	33.14%	16.38%
Projected EPS Growth (F1/F0)	-54.62%	-6.10%	-4.75%	-64.89%	-41.64%	-39.49%
Current Cash Flow Growth	14.35%	7.19%	5.22%	21.44%	16.72%	-1.16%
Historical Cash Flow Growth (3-5 Years)	18.31%	1.69%	8.49%	15.01%	42.51%	19.13%
Current Ratio	1.37	0.47	1.35	0.61	1.26	0.47
Debt/Capital	28.37%	20.31%	42.92%	24.00%	0.00%	15.97%
Net Margin	30.45%	4.27%	10.25%	15.88%	49.62%	42.08%
Return on Equity	10.99%	7.13%	14.66%	6.97%	14.53%	11.87%
Sales/Assets	0.21	0.19	0.50	0.19	0.22	0.20
Projected Sales Growth (F1/F0)	0.00%	0.00%	-1.42%	14.76%	0.00%	0.00%
Momentum Score	D	-	-	B	C	F
Daily Price Change	3.28%	0.43%	1.82%	1.68%	4.05%	3.58%
1-Week Price Change	5.29%	1.60%	2.59%	4.43%	3.22%	6.62%
4-Week Price Change	5.59%	1.64%	4.80%	4.25%	4.89%	12.88%
12-Week Price Change	-4.97%	-1.32%	6.31%	-2.22%	3.11%	5.76%
52-Week Price Change	-28.51%	-13.05%	5.43%	-21.29%	-21.72%	-24.92%
20-Day Average Volume (Shares)	1,860,520	138,515	1,788,967	1,132,959	653,151	3,833,826
EPS F1 Estimate 1-Week Change	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
EPS F1 Estimate 4-Week Change	-25.81%	0.00%	0.00%	51.72%	8.54%	-8.24%
EPS F1 Estimate 12-Week Change	-27.53%	2.30%	3.89%	15.56%	-15.44%	-7.48%
EPS Q1 Estimate Monthly Change	18.75%	0.00%	0.00%	540.00%	56.49%	22.92%

Source: Zacks Investment Research

Zacks Style Scores

The Zacks Style Score is as a complementary indicator to the Zacks rating system, giving investors a way to focus on the highest rated stocks that best fit their own stock picking preferences.

Academic research has proven that stocks with the best Value, Growth and Momentum characteristics outperform the market. The Zacks Style Scores rate stocks on each of these individual styles and assigns a rating of A, B, C, D and F. We also produce the VGM Score (V for Value, G for Growth and M for Momentum), which combines the weighted average of the individual Style Scores into one score. This is perfectly suited for those who want their stocks to have the best scores across the board.

Value Score	A
Growth Score	D
Momentum Score	D
VGM Score	C

As an investor, you want to buy stocks with the highest probability of success. That means buying stocks with a Zacks Recommendation of Outperform, which also has a Style Score of an A or a B.

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Returns quoted represent past performance which is no guarantee of future results. Investment returns and principal value will fluctuate so that when shares are redeemed, they may be worth more or less than their original cost. Current performance may be higher or lower than the performance shown.

Investing involves risk; principal loss is possible. There is no guarantee that companies that can issue dividends will declare, continue to pay or increase dividends.

Glossary of Terms and Definitions

52-Week High-Low: The range of the highest and lowest prices at which a stock has traded during the past year. This range is determined based on the stock's daily closing price which may differ from the intra-day high or low. Many investors use it as a technical indicator to determine a stock's current value and future price movement. The idea here is that if price breaks out from the 52-week range, in either direction, the momentum may continue in the same direction.

20-Day Average Volume (Shares): The average number of shares of a company traded in a day over the last 20 days. It is a direct indication of a security's overall liquidity. The higher the average daily trading volume, the easier it is to enter or exit the stock at a desired price with more buyers and sellers being available.

Daily Price Change: This is the percentage difference between a trading day's closing price and the prior trading day's closing price. This item is updated at 9 p.m. EST each day.

1-Week Price Change: This is the percentage change in a stock's closing price over the last 5 trading days. This change reflects the collective buying and selling sentiment over the 1-week period.

A strong weekly price increase for the stock, especially when accompanied by increased volume, is an indication of it gaining momentum.

4-Week Price Change: This is the percentage change in a stock's closing price over the last 20 trading days or past 4 weeks. This is a medium-term price change metric and an indication of the stock gaining momentum.

12-Week Price Change: This is the percentage change of a stock's closing price over the last 60 trading days or past 12 weeks. Similar to 4-week price change, this is a medium-term price change metric. It shows whether a stock has been enjoying strong investor demand, or if it has been in consolidation, or distress over this period.

52-Week Price Change: This is the percentage change in a stock's closing price over the last 260 trading days or past 52 weeks. This long-term price change metric is a good reference point for investors. Some investors seek stocks with the best percentage price change over the last 52 weeks, expecting the momentum to continue.

Market Cap: The number of outstanding common shares of a company times its latest price per share. This figure represents a company's size, which indicates various characteristics, including price stability and risk, in which investors could be interested.

Year-To-Date Price Change: Change in a stock's daily closing price in the period of time beginning the first day of the current calendar year through to the previous trading day.

of Analysts: Number of EPS estimates used in calculating the current-quarter consensus. These estimates come from the brokerage analysts tracking this stock. However, the number of such analysts tracking this stock may not match the number of estimates, as all brokerage analysts may not come up with an estimate or provide it to us.

Beta: A measure of risk commonly used to compare the volatility of a stock to the overall market. The S&P 500 Index is the base for calculating beta and carries a value of 1. A stock with beta below 1 is less risky than the market as a whole. And a stock with beta above 1 is riskier.

Dividend: The portion of earnings a company is expected to distribute to its common shareholders in the next 12 months for each share they own. Dividends are usually paid quarterly. Dividend payments reflect positively on a company and help maintain investors' trust. Investors typically find dividend-paying stocks appealing because the dividend adds to any market price appreciation to result in higher return on investment (ROI). Moreover, a steady or increasing dividend payment provides investors a cushion in a down market.

Dividend Yield: The ratio of a company's annual dividend to its share price. The annual dividend used in the ratio is calculated based on the most recent dividend paid by the company. Dividend yield is an estimate of the dividend-only return from a stock in the next 12 months. Since dividend itself doesn't change frequently, dividend yield usually changes with a stock's price movement. As a result, often an unusually high dividend yield is a result of weak stock price.

S&P 500 Index: The Standard & Poor's 500 (S&P 500) Index is an unmanaged group of securities considered to be representative of the stock market in general. It is a market-capitalization-weighted index of stocks of the 500 largest U.S. companies. Each stock's weight in the index is proportionate to its market value.

Industry: One of the 250+ groups that Zacks classifies all stocks into based on the nature of business. These groups are termed as expanded (aka "X") industries and map to their respective (economic) sectors; Zacks has 16 sectors.

Zacks Industry Rank: The Zacks Industry Rank is determined by calculating the average Zacks Rank for all stocks in the industry and then assigning an ordinal rank to it. For example, an industry with an average Zacks Rank of 1.6 is better than an industry with an average Zacks Rank of 2.3. So, the industry with the better average Zacks Rank would get a better Zacks Industry Rank. If an industry has the best average Zacks Rank, it would be considered the top industry (1 out of 250+), which would place it at the top 1% of Zacks-ranked industries. Studies have shown that roughly half of a stock's price movement can be attributed to the industry group it belongs to. In fact, the top 50% of Zacks-ranked industries outperforms the bottom 50% by a factor of more than 2 to 1.

Last EPS Surprise: The percentage deviation of a company's last reported earnings per share from the Zacks Consensus Estimate. Companies with a positive earnings surprise are more likely to surprise again in the future (or miss again if they recently missed).

Last Sales Surprise: The percentage deviation of a company's last reported sales from the Zacks Consensus Estimate.

Expected Report Date: This is an estimated date of a company's next earnings release. The information originated or gathered by Zacks Investment Research from its information providers or publicly available sources is the basis of this estimate.

Earnings ESP: The Zacks Earnings ESP compares the Most Accurate Estimate to the Zacks Consensus Estimate for the yet-to-be reported quarter. The Most Accurate Estimate is the most recent version of the Zacks Consensus EPS Estimate. The idea here is that analysts revising their estimates closer to an earnings release have the latest information, which could potentially be more accurate than what they and others contributing to the consensus had predicted earlier. Thus, a positive or negative Earnings ESP reading theoretically indicates the likely deviation of the actual earnings from the consensus estimate. However, the model's predictive power is significant for positive ESP readings only. A positive Earnings ESP is a strong predictor of an earnings beat, particularly when combined with a Zacks Rank #1 (Strong Buy), #2 (Buy) or #3 (Hold). Our research shows that stocks with this combination produce a positive surprise nearly 70% of the time.

Periods:

TTM: Trailing 12 months. Using TTM figures is an effective way of analyzing the most-recent financial data in an annualized format that helps neutralize the effects of seasonality and other quarter-to-quarter variation.

F1: Current fiscal year. This period is used to analyze the estimates for the ongoing full fiscal year.

F2: Next fiscal year. This period is used to analyze the estimates for the next full fiscal year.

F12M: Forward 12 months. Using F12M figures is an effective way of analyzing the near-term (the following four unreported quarters) estimates in an annualized manner. Instead of typically representing estimates for the full fiscal year, which may not represent the nitty-gritty of each quarter, F12M figures suggest an all-inclusive annualized estimate for the following four quarters. The annualization helps neutralize the potential effects of seasonality and other quarter-to-quarter variations.

P/E Ratio: The price-to-earnings ratio measures a company's current market price per share relative to its earnings per share (EPS). Usually, the trailing-12-month (TTM) EPS, current-fiscal-year (F1) EPS estimate, or forward-12-month (F12M) EPS estimate is used as the denominator. In essence, this ratio shows what the market is willing to pay today for each dollar of EPS. In other words, this ratio gives a sense of what the relative value of the company is at the already reported level of earnings or at a future level of earnings.

It is one of the most widely-used multiples for determining the value of a company and helps comparing its valuation with that of a competitor, the industry group or a benchmark.

PEG Ratio: The price/earnings to growth ratio is a stock's P/E ratio using current fiscal year (F1) EPS estimate divided by its expected EPS growth rate over the coming 3 to 5 years. This ratio essentially determines a stock's value by factoring in the company's expected earnings growth and is thus believed to provide a more complete picture than just the P/E ratio, particularly for faster-growing companies.

P/S Ratio: The price-to-sales ratio is calculated as a company's current price per share divided by trailing 12 months (TTM) sales or revenues per share. This ratio shows what the market is willing to pay today for each dollar of TTM sales per share. The P/S ratio is at times the only valuation metric when the company has yet to become profitable.

Cash/Price Ratio: The cash-to-price ratio or Cash Yield is calculated as cash and marketable securities per share divided by the company's current share price. Like the earnings yield, which shows the anticipated yield (or return) on a stock from earnings for each dollar invested, the cash yield does the same, with cash being the source of return instead of earnings. For example, a cash/price ratio of 0.08 suggests a return of 8% or 8 cents for every \$1 investment.

EV/EBITDA Ratio: The EV/EBITDA ratio, also known as Enterprise Multiple, is calculated as a company's enterprise value (market capitalization + value of total long-term debt + book value of preferred shares - cash and marketable securities) divided by EBITDA (earnings before interest, taxes, depreciation and amortization). Usually, trailing-12-month (TTM) or forward-12-month (F12M) EBITDA is used as the denominator.

EV/Sales Ratio: The enterprise value-to-sales ratio is calculated as a company's enterprise value (market capitalization + value of total long-term debt + book value of preferred shares - cash and marketable securities) divided by annual sales. It is an expansion of the P/S valuation, which uses market value instead of enterprise value. The EV/Sales ratio is perceived as more accurate than P/S, in part, because the market capitalization does not take a company's debt into account when valuing it.

EV/CF Ratio: The enterprise value-to-cash flow ratio is calculated as a company's enterprise value (market capitalization + value of total long-term debt + book value of preferred shares - cash and marketable securities) divided by the trailing-12-month (TTM) operating cash flow. It's a measure of how long it would take to buy the entire business if you were able to use all the company's operating cash flow.

The EV/CF ratio is perceived as more accurate than the P/CF ratio, in part, because the market price does not take a company's debt into account when valuing it.

EV/FCF Ratio: The enterprise value-to-free cash flow metric compares a company's enterprise value to its trailing-12-month (TTM) free cash flow (FCF). This metric is very similar to the EV/CF ratio, but is considered a more exact measure owing to the fact that it uses free cash flow, which subtracts capital expenditures (CAPEX) from a company's total operating cash flow, thereby reflecting the actual cash flow available for funding growth activities and payments to shareholders.

P/EBITDA Ratio: The P/EBITDA ratio is calculated as a company's per share market value divided by EBITDA (earnings before interest, taxes, depreciation, and amortization). This metric is very similar to the EV/EBITDA ratio, but is considered a little less exact measure as it uses market price, which does not take a company's debt into account. However, since EBITDA is often considered a proxy for cash income, the metric is used as a measure of what the market is willing to pay today for each dollar of the company's cash profitability in the trailing 12 months (TTM) or forward 12 months (F12M).

P/B Ratio: The price-to-book ratio is calculated as a company's current price per share divided by its book value (total assets – liabilities – preferred stocks) per share. In short, the book value is how much a company is worth. In other words, it reflects the total value of a company's assets that its common shareholders would receive if it were to be liquidated. So, the P/B ratio indicates whether you're paying higher or lower than what would remain if the company went bankrupt immediately. Investors typically use this metric to determine how a company's stock price stacks up to its intrinsic value.

P/TB Ratio: The price-to-tangible-book value ratio is calculated as a the per share market value of a company divided by the value of its tangible assets (total assets – liabilities – preferred stocks – intangible assets) per share. Tangible book value is the same thing as book value except it excludes the value of intangible assets to get a step closer to the baseline value of the company.

P/CF Ratio: The price-to-cash flow ratio measures a company's per share market price relative to its trailing-12-month (TTM) operating cash flow per share. This metric is used to determine whether a company is undervalued or overvalued relative to another stock, industry or sector. And like the P/E ratio, a lower number is typically considered better from the value perspective.

One of the reasons why P/CF ratio is often preferred over P/E ratio is the fact that operating cash flow adds back non-cash expenses such as depreciation and amortization to net income. This feature helps valuing stocks that have positive cash flow but are not profitable because of large noncash charges.

P/FCF Ratio: The price-to-free cash flow ratio is an extension of P/CF ratio, which uses trailing-12-month (TTM) free cash flow per share instead of operating cash flow per share. This metric is considered a more exact measure than P/CF ratio, as free cash flow subtracts capital expenditures (CAPEX) from a company's total operating cash flow, thereby reflecting the actual cash flow available for funding activities that generate additional revenues.

Earnings Yield: The earnings yield is calculated as current fiscal year (F1) EPS estimate divided by the company's current share price. The ratio, which is the inverse of the P/E ratio, measures the anticipated yield (or return) from earnings for each dollar invested in a stock today.

For example, earnings yield for a stock, which is trading at \$35 and expected to earn \$3 per share in the current fiscal year (F1), would be 0.0857 ($3/35 = 0.0857$) or 8.57%. In other words, for \$1 invested in the stock today, the yield from earnings is anticipated to be 8.57 cents.

Investors most commonly compare the earnings yield of a stock to that of a broad market index (such as the S&P 500) and prevailing interest rates, such as the current 10-year Treasury yield. Since bonds and stocks compete for investors' dollars, stock investors typically demand a higher yield for the extra risk they assume compared to investors of U.S. Treasury-backed securities that offer virtually risk-free returns. This additional return is referred to as the risk premium.

Debt/Equity Ratio: The debt-to-equity ratio is calculated as a company's total liabilities divided by its shareholder equity. This metric is used to gauge a company's financial leverage. In other words, it is a measure of the degree to which a company is financing its operations through debt versus its own funds. The higher the ratio, the higher the risk for shareholders.

However, this ratio is difficult to compare across industry groups where ideal amounts of debt vary. Some businesses are more capital intensive than others and typically require higher debt to finance their operations. So, a company's debt-to-equity ratio should be compared with other companies in the same industry.

Cash Flow (\$/share): Cash flow per share is calculated as operating cash flow (after-tax earnings + depreciation + other non-cash charges) divided by common shares outstanding. It is used by many investors as a measure of a company's financial strength. Since cash flow per share takes into consideration a company's ability to generate cash by adding back non-cash expenses, it is regarded by some as a more accurate measure of a company's financial situation than earnings per share, which could be artificially deflated.

Current Ratio: The current ratio or liquidity ratio is a company's current assets divided by its current liabilities. It measures a company's ability to pay short-term obligations. A current ratio that is in line with the industry average or slightly higher is generally considered acceptable. A current ratio that is lower than the industry average would indicate a higher risk of distress or default. A higher number is usually better. However, a very high current ratio compared to the industry average could be an indication of inefficient use of assets by management.

Debt/Capital Ratio: Debt-to-capital ratio is a company's total debt (interest-bearing debt + both short- and long-term liabilities) divided its total capital (interest-bearing debt + shareholders' equity). It is a measure of a company's financial leverage. All else being equal, the higher the debt-to-capital ratio, the riskier the stock.

However, this ratio can vary widely from industry to industry, the ideal amount of required debt being different. Some businesses are more capital intensive than others and typically require higher debt to finance their operations. So, a company's debt-to-capital ratio should be compared with the same for its industry.

Net Margin: Net margin is calculated as net income divided by sales. It shows how much of each dollar in sales generated by a company translates into profit. For example, if a company's net margin is 15%, its net income is 15 cents for every \$1 of sales it makes.

A change in margin can reflect either a change in business conditions, or a company's cost controls, or both. If a company's expenses are growing faster than sales, its net margin will decline. However, different net margin rates are considered good for different industries, so it's better to compare net margin rates of companies in the same industry group.

Return on Equity: Return on equity (ROE) is calculated as trailing-12-month net income divided by trailing-12-month average shareholder equity (including reinvested earnings). This metric is considered a measure of how effectively management is using a company's assets to generate profits. For example, if a company's ROE is 10%, it creates 10 cents profits for every \$1 shareholder equity, which is basically the company's assets minus debt. A company's ROE deemed good or bad depends on what's normal for its peers or industry group.

Sales/Assets Ratio: The sales-to-assets ratio or asset utilization ratio or asset turnover ratio is calculated as a company's annual sales divided by average assets (average of assets at the beginning of the year and at the year's end). This metric helps investors understand how effectively a company is using its assets to generate sales. For example, a sales-to-assets ratio of 2.5 indicates that the company generated \$2.50 in sales for every \$1 of assets on its books.

The higher the sales-to-assets ratio, the better the company is performing. However, similar to many other ratios, the asset turnover ratio tends to be higher for companies in certain industries/sectors than in others. So, a company's sales-to-assets ratio should be compared with the same for its industry/sector.

Historical EPS Growth (3-5 Years): This is the average annual (trailing-12-month) EPS growth rate over the last 3-5 years. This metric helps investors see how a company's EPS has grown from a long-term perspective.

Note: There are many factors that can influence short-term numbers — a recession will reduce this number, while a recovery will inflate it. The longterm perspective helps smooth out short-term events.

Projected EPS Growth (F1/F0): This is the estimated EPS growth rate for the current financial year. It is calculated as the consensus estimate for the current fiscal year (F1) divided by the reported EPS for the last completed fiscal year (F0).

Current Cash Flow Growth: It measures the latest year-over-year change in operating cash flow. Cash flow growth tells an investor how quickly a company is generating inflows of cash from operations. A positive change in the cash flow is desired and shows that more 'cash' is coming in than going out.

Historical Cash Flow Growth (3-5 Years): This is the annualized change in cash flow over the last 3-5 years. The change in a longer period helps put the current reading into proper perspective. By looking at the rate, rather than the actual dollar value, the comparison across the industry and peers becomes easier.

Projected Sales Growth (F1/F0): This metric looks at the estimated sales growth for the current year. It is calculated as sales estimate for the current fiscal year (F1) divided by the reported sales for the last completed fiscal year (F0).

Like EPS growth, a higher rate is better for sales growth. A look at a company's projected sales growth instantly tells you what the outlook is for their products and services. However, different sales growth rates are considered good for different industries, so it's better to compare sales growth rates of companies in the same industry group.

EPS F1 Estimate 1-Week Change: The percentage change in the Zacks Consensus EPS estimate for the current fiscal year over the past week. The change in a company's consensus EPS estimate (or earnings estimate revision) has proven to be strongly correlated with the near-term price movement of its shares. It is an integral part of the Zacks Rank.

If a stock's consensus EPS estimate is \$1.10 now versus \$1.00 a week ago, that will be reflected as a 10% upward revision. If, on the other hand, it went from \$1.00 to 90 cents, that would be a 10% downward revision.

EPS F1 Estimate 4-Week Change: The percentage change in the Zacks Consensus EPS estimate for the current fiscal year over the past four weeks.

A stock's earnings estimate revision in a 1-week period is important. But it's more meaningful to look at the longer-term revision. And, of course, the 4-week change helps put the 1-week change into proper perspective.

EPS F1 Estimate 12-Week Change: The percentage change in the Zacks Consensus EPS estimate for the current fiscal year over the past 12 weeks.

This metric essentially shows how the consensus EPS estimate has changed over a period longer than 1 week or 4 weeks.

EPS Q1 Estimate Monthly Change: The percentage change in the Zacks Consensus EPS estimate for the current fiscal quarter over the past four weeks.

While the revision in consensus EPS estimate for the current fiscal year is strongly correlated with the near-term price movement of its shares, the estimate revision for the current fiscal quarter is an important metric as well, especially over the short term, and particularly as a stock approaches its earnings date. If a stock's Q1 EPS estimate decreases ahead of its earnings release, it's usually a negative sign, whereas an increase is a positive sign.