Portfolio Strategy

BAIRD
Institutional Equities & Research

What is the Baird Estimate Revision Model (ERM) Platform?

The Baird Estimate Revision Model (ERM) is a proprietary screening process that attempts to reveal key inflections in sell-side analyst sentiment, before these inflections are widely recognized by the Street. The model seeks to identify companies with improving or deteriorating earnings prospects, based upon the truism that forward profit expectations drive stock performance over time. The model was developed by Baird's Senior Portfolio Strategist, Brian Rauscher, and key attributes include:

1. Highly proprietary portfolio tool that is complementary to a client's existing investment process
2. Informs on timing of entry and exit points once the fundamental investment decision is made
3. Established as a monthly recurring review process, but data updated weekly for ad hoc analysis
4. Customizable for portfolio, focus list, sector, or benchmark analysis
5. Benchmarks analyzed include:
   - S&P 500, S&P 400, S&P 600
   - R1000, R2000
   - MSCI Developed Market Index (Global Mid & Large Cap)

How does the ERM work?

The model integrates an objective, two-step, estimate revision analysis to determine how the sell-side community is viewing a given company, then overlays a more subjective valuation and price momentum discipline to give better insight on shorter-term trading dynamics.

The first step of the analysis is the proprietary Analyst Sentiment Measure (ASM), which examines the aggregate estimates from the analyst community, and identifies second derivative change in the proportion of analysts that are raising versus lowering forward profit expectations. The goal of the ASM is to identify key inflections in analyst sentiment before these changes are widely recognized. This step provides a better sense of the breadth of the analyst revision activity.

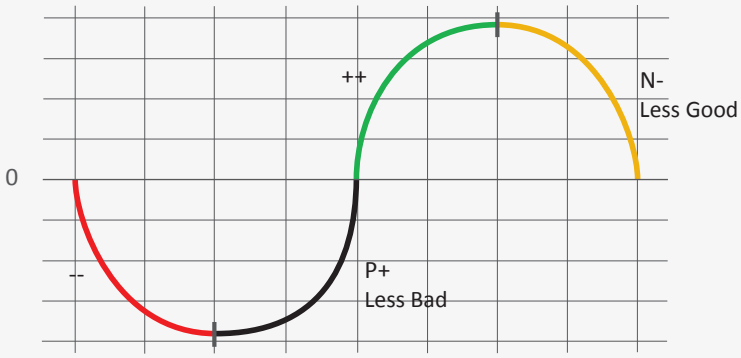
The second step of the analysis looks at the percentage change in forward consensus estimates over the previous 90-day period. This step in the analysis can be an important confirmation of the second derivative inflections indicated by the ASM above, and provides a better understanding of the magnitude of estimate revisions activity.

Products built on the ERM Platform include:

- Monthly Client ERM Updates: Sent on Friday of first full week of each month, and customized to the client's need, as discussed above.
- Cross-Check Publication: Done on monthly and ad hoc basis, this product identifies high-conviction ideas from the Baird fundamental analyst team that screen favorably in the ERM.
- Caution Zone Publication: Done on monthly and ad hoc basis, this piece identifies stocks that screen unfavorably in our ERM, and can be used by clients to identify names in the portfolio potentially at risk, or to potentially help clients identify and generate short alpha.

Below contains a graphical representation of the Estimate Revision Cycle. Please contact your Baird Sales Broker for more information.

Earnings Revision Cycle



Earnings Revision Model Key

-- **Stock price is generally acting poorly and still too early to get aggressively long.**

DOUBLE MINUS – Earnings revisions deteriorating on an absolute basis signaling that the bottom-up consensus is now actively lowering forward expectations.

P+ **Probablity is rising that the stock price may be nearing a bottom, which leads to a high-quality entry point.**

EARLY POSITIVE SIGNAL – Earnings revisions have experienced a positive inflection (second derivative turn) though absolute activity remains negative.

++ **Stock price is generally acting well and is becoming a momentum play.**

DOUBLE PLUS – Earnings revisions improving on an absolute basis signaling that the bottom-up consensus is now actively raising forward expectations.

N- **Probablity is rising that the stock price may be topping, which leads to a high-quality trim/exit point.**

EARLY NEGATIVE SIGNAL – Earnings revisions have experienced a negative inflection (second derivative turn) though absolute activity remains positive.