



Featured Stock in August's Dividend Growth Model Portfolio

Thirteen stocks were added to our [Dividend Growth Stocks Model Portfolio](#) this month, which was made available to members on August 26, 2022.

Recap From July's Picks

On a price return basis, our Dividend Growth Stocks Model Portfolio (+1.7%) underperformed the S&P 500 (+1.9%) by 0.2%, and on a total return basis, the Model Portfolio (+2.0%) outperformed the S&P 500 (+1.9%) by 0.1%. The best performing stock was up 16%. Overall, 12 out of the 30 Dividend Growth Stocks outperformed the S&P 500 from July 28, 2022 through August 24, 2022.

[Buy the Dividend Growth Stocks Model Portfolio](#)

This model portfolio mimics an "All Cap Blend" style with a focus on dividend growth. Selected stocks earn an [Attractive or Very Attractive rating](#), generate positive free cash flow (FCF) and [economic earnings](#), offer a current dividend yield >1%, and have a 5+ year track record of consecutive dividend growth. This model portfolio is designed for investors who are more focused on long-term capital appreciation than current income, but still appreciate the power of dividends, especially growing dividends.

This report leverages our cutting-edge [Robo-Analyst technology](#) to deliver [proven-superior](#)¹ fundamental research and support more cost-effective fulfillment of the [fiduciary duty of care](#).

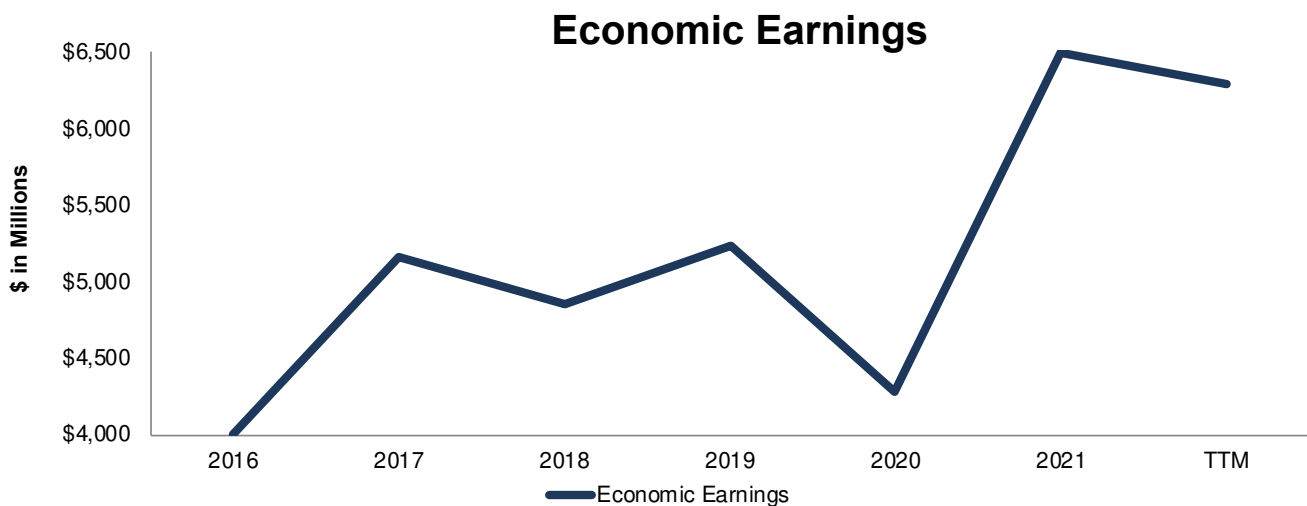
Featured Stock From August: McDonald's Corporation (MCD: \$256/share)

McDonald's Corporation (MCD) is the featured stock from August's Dividend Growth Stocks Model Portfolio.

We made McDonald's a [Long Idea](#) in [November 2019](#), and since then, the stock is up 31% compared to a 30% gain for the S&P 500. See our latest update on McDonald's [here](#).

McDonald's has grown [economic earnings](#) by 10% compounded annually over the past five years. McDonald's net operating profit after-tax (NOPAT) margin rose from 24% in 2016 to 37% over the trailing twelve months (TTM), while the company's return on invested capital (ROIC) rose from 14% to 18% over the same time.

Figure 1: McDonald's Economic Earnings Since 2016



Sources: New Constructs, LLC and company filings

¹ Our research utilizes our [Core Earnings](#), a more reliable measure of profits, as proven in [Core Earnings: New Data & Evidence](#), written by professors at Harvard Business School (HBS) & MIT Sloan and published in [The Journal of Financial Economics](#).



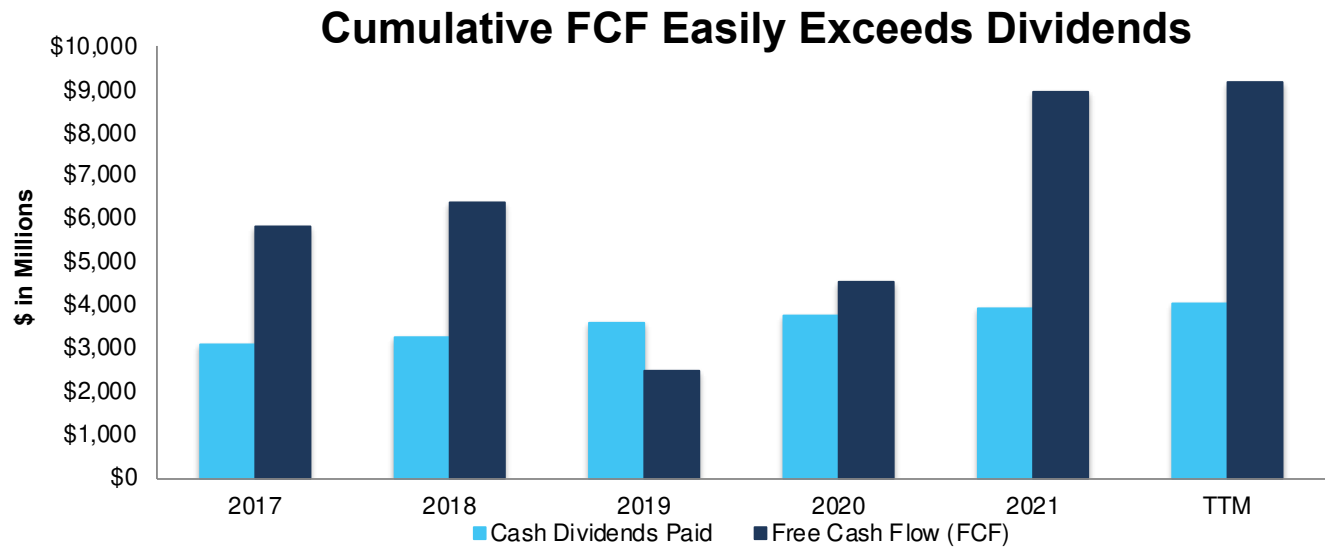
FCF Exceeds Dividends by a Wide Margin

McDonald's has increased its dividend in each of the past [46 years](#). The company increased its regular dividend from \$3.83/share in 2017 to \$5.25/share in 2021, or 8% compounded annually. The current quarterly dividend, when annualized, equals \$5.52/share, and provides a 2.2% dividend yield.

More importantly, McDonald's strong free cash flow ([FCF](#)) easily exceeds the company's growing dividend payments. From 2017 – 2021, McDonald's cumulative \$28.2 billion (15% of current market cap) in FCF is 60% more than the \$17.6 billion in dividends paid out, per Figure 2. Over the TTM, the company generated \$9.2 billion in FCF and paid out \$4.0 billion in dividends.

Figure 2 also shows that McDonald's FCF significantly exceeded its dividend payments in four of the past five years.

Figure 2: Free Cash Flow vs. Regular Dividend Payments



Sources: New Constructs, LLC and company filings

Companies with FCF well above dividend payments provide higher quality dividend growth opportunities because we know the company generates the cash to support a higher dividend. On the other hand, the dividend of a company where FCF falls short of the dividend payment over time cannot be trusted to grow or even maintain its dividend because of inadequate free cash flow.

McDonald's Has Upside Potential

At its current price of \$256/share, MCD has a price-to-economic book value ([PEBV](#)) ratio of 1.5. This ratio means the market expects McDonald's NOPAT to grow no more than 50% above current levels. This expectation seems overly pessimistic for a company whose TTM NOPAT is 66% above 2015 levels.

If McDonald's maintains its TTM NOPAT margin of 37% and grows NOPAT by just 5% compounded annually for the next fifteen years, the stock would be worth \$315+/share today – a 23% upside. [See the math behind the reverse DCF scenario.](#)

Should the company grow NOPAT more in line with historical growth rates, the stock has even more upside. Add in McDonald's 2.2% dividend yield and history of dividend growth, and it's clear why this stock is in August's Dividend Growth Stocks Model Portfolio.



Critical Details Found in Financial Filings by Our [Robo-Analyst Technology](#)

Below are specifics on the adjustments we make based on Robo-Analyst findings in McDonald's 10-Ks and 10-Qs:

Income Statement: We made \$2.8 billion in adjustments with a net effect of removing \$988 million in [non-operating expenses](#) (4% of revenue). Clients can see all adjustments made to McDonald's income statement on the GAAP Reconciliation tab on the Ratings page on our website.

Balance Sheet: We made \$12.8 billion in adjustments to calculate invested capital with a net decrease of \$1.6 billion. The most notable adjustment was \$2.8 billion (6% of reported net assets) in [asset write-downs](#). Clients can see all adjustments made to McDonald's balance sheet on the GAAP Reconciliation tab on the Ratings page on our website.

Valuation: We made \$50.0 billion in adjustments with a net effect of decreasing shareholder value by \$47.0 billion. Apart from total debt, the most notable adjustment to shareholder value was \$1.4 billion in [excess cash](#). This adjustment represents <1% of McDonald's market value. Clients can see all adjustments to McDonald's valuation on the GAAP Reconciliation tab on the Ratings page on our website.

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Disclosure: David Trainer, Kyle Guske II, Matt Shuler, and Brian Pellegrini receive no compensation to write about any specific stock, style, or theme.

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It's Official: We Offer the Best Fundamental Data in the World

Many firms claim their research is superior, but none of them can prove it with independent studies from highly-respected institutions as we can. Three different papers from both the public and private sectors show:

1. Legacy fundamental datasets suffer from significant inaccuracies, omissions and biases.
2. Only our “novel database” can overcome these flaws and provides [materially superior](#) fundamental data.
3. Our proprietary measures of [Core Earnings](#) and [Earnings Distortion](#) materially improve stock picking and forecasting of profits.

Best Fundamental Data in the World

Forthcoming in [The Journal of Financial Economics](#), a top peer-reviewed journal, [Core Earnings: New Data & Evidence](#) proves our Robo-Analyst technology overcomes material shortcomings in legacy firms’ data collection processes to provide superior [fundamental data](#), [earnings](#) models, and [research](#). More [details](#).

Key quotes from the paper:

- “[New Constructs’] *Total Adjustments* differs significantly from the items identified and excluded from Compustat’s adjusted earnings measures. For example... 50% to 70% of the variation in *Total Adjustments* is not explained by S&P Global’s (SPGI) *Adjustments* individually.” – pp. 14, 1st para.
- “A final source of differences [between New Constructs’ and S&P Global’s data] is due to data collection oversights...we identified cases where Compustat did not collect information relating to firms’ income that is useful in assessing core earnings.” – pp. 16, 2nd para.

Superior Models

A top accounting firm features the superiority of our ROIC, NOPAT and Invested Capital research to Capital IQ & Bloomberg’s in [Getting ROIC Right](#). See the [Appendix](#) for direct comparison details.

Key quotes from the paper:

- “...an accurate calculation of ROIC requires more diligence than often occurs in some of the common, off-the-shelf ROIC calculations. Only by scouring the footnotes and the MD&A [as New Constructs does] can investors get an accurate calculation of ROIC.” – pp. 8, 5th para.
- “The majority of the difference...comes from New Constructs’ machine learning approach, which leverages technology to calculate ROIC by applying accounting adjustments that may be buried deeply in the footnotes across thousands of companies.” – pp. 4, 2nd para.

Superior Stock Ratings

Robo-Analysts’ stock ratings outperform those from human analysts as shown in this [paper](#) from Indiana’s Kelley School of Business. Bloomberg features the paper [here](#).

Key quotes from the paper:

- “the portfolios formed following the buy recommendations of Robo-Analysts earn abnormal returns that are statistically and economically significant.” – pp. 6, 3rd para.
- “Our results ultimately suggest that Robo-Analysts are a valuable, alternative information intermediary to traditional sell-side analysts.” – pp. 20, 3rd para.

Our mission is to provide the best fundamental analysis of public and private businesses in the world and make it affordable for all investors, not just Wall Street insiders.

We believe every investor deserves to know the whole truth about the profitability and valuation of any company they consider for investment. More details on our cutting-edge technology and how we use it are [here](#).



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