



Featured Stock in September's Exec Comp & ROIC Model Portfolio

Two new stocks made September's [Exec Comp Aligned with ROIC Model Portfolio](#), available to members as of September 15, 2022.

Recap From August's Picks

Our Exec Comp Aligned with ROIC Model Portfolio (-8.9%) underperformed the S&P 500 (-8.1%) from August 12, 2022 through September 13, 2022. The best performing stock in the portfolio was up 7%. Overall, six out of the 15 Exec Comp Aligned with ROIC stocks outperformed the S&P 500 from August 12, 2022 through September 13, 2022.

Buy the Exec Comp Aligned with ROIC Model Portfolio

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](#).

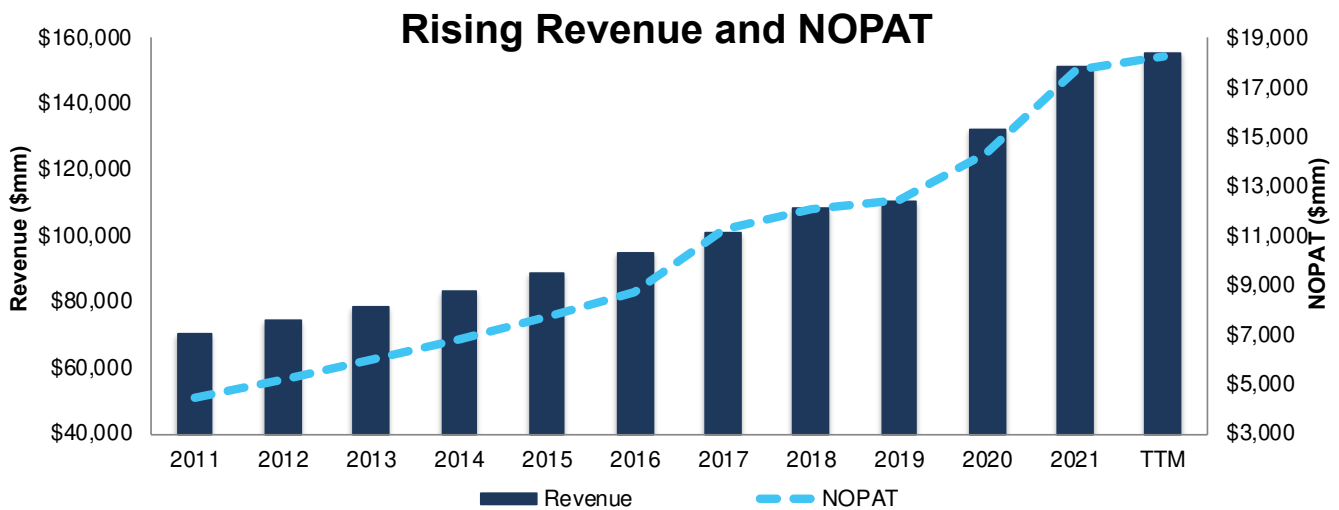
This Model Portfolio includes stocks that earn an [Attractive or Very Attractive](#) rating and align executive compensation with improving ROIC. This combination provides a uniquely well-screened list of long ideas because the [primary driver of shareholder value creation](#) is return on invested capital ([ROIC](#)).

New Feature Stock for September: The Home Depot, Inc. (HD: \$272/share)

The Home Depot, Inc. (HD) is the featured stock in September's Exec Comp Aligned with ROIC Model Portfolio. We made HD a [Long Idea](#) on [September 8, 2022](#). Since then, the stock is down 9% compared to a 5% decline for the S&P 500.

Home Depot grew revenue and net operating profit after tax ([NOPAT](#)) by 8% and 15% compounded annually, respectively, over the past ten years. The company's NOPAT margin rose from 6% in fiscal 2011 to 12% over the trailing-twelve-months (TTM), while invested capital turns rose from 1.9 to 2.9 over the same time. Rising NOPAT margins and invested capital turns drive [ROIC](#) from 12% in fiscal 2011 to 36% TTM.

Figure 1: Home Depot's Revenue & NOPAT: Fiscal 2011 – TTM



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](#).

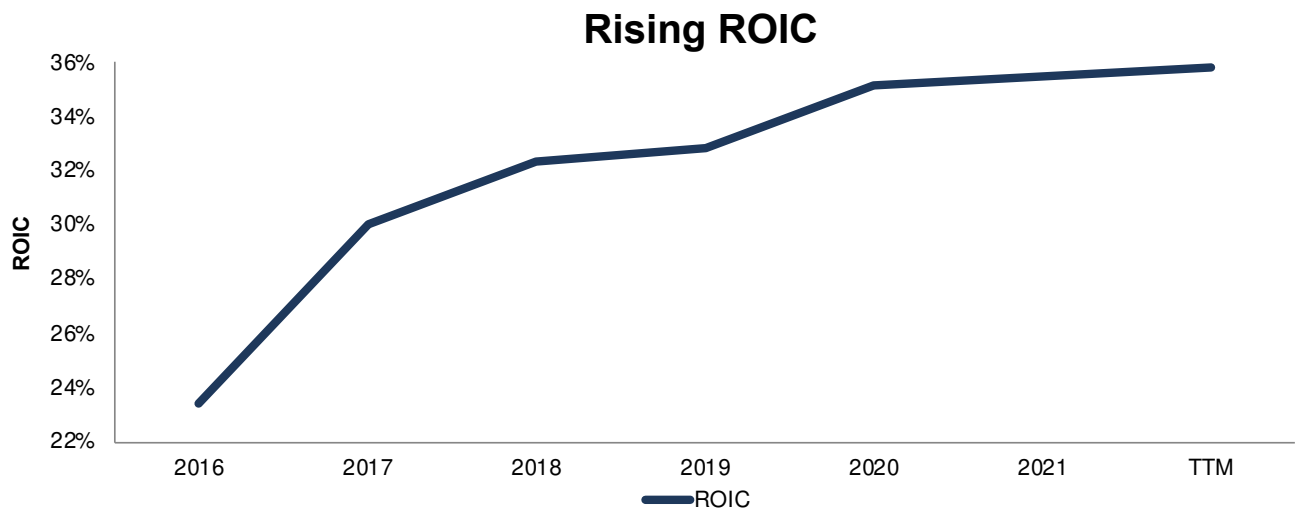


Executive Compensation Properly Aligns Executive Incentives

Home Depot's executive compensation plan aligns executives' interests with shareholders' interests by tying the payout of equity awards to a three-year return on invested capital (ROIC) target.

Home Depot's inclusion of ROIC as a performance goal has helped create shareholder value through rising ROIC and [economic earnings](#). Home Depot's ROIC improved from 23% in fiscal 2016 to 36% over the TTM, and the company's economic earnings rose from \$6.7 billion to \$15.1 billion over the same period.

Figure 2: Home Depot's ROIC: Fiscal 2016 – TTM



Sources: New Constructs, LLC and company filings

Home Depot Is Undervalued

At its current price of \$272/share, HD has a price-to-economic book value (PEBV) ratio of 1.2. This ratio means the market expects Home Depot's NOPAT to grow by no more than 20%. This expectation seems overly pessimistic for a company that has grown NOPAT by 15% compounded annually over the past decade and 9% compounded annually over the past 20 years.

If Home Depot maintains its TTM NOPAT margin of 12%, and the company grows NOPAT by just 5% compounded annually over the next 15 years, the stock would be worth \$390+/share today – a 43% upside. [See the math behind this reverse DCF scenario](#). Should the company grow NOPAT more in line with historical growth rates, the stock has even more upside.

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 Home Depot's 10-Qs and 10-Ks:

Income Statement: we made \$2.0 billion in adjustments, with a net effect of removing \$1.3 billion in [non-operating expenses](#) (1% of revenue). Clients can see all adjustments made to Home Depot's income statement on the GAAP Reconciliation tab on the Ratings page on our website.

Balance Sheet: we made \$6.3 billion in adjustments to calculate invested capital with a net increase of \$5.6 billion. One of the largest adjustments was \$1.1 billion (2% of reported net assets) in [asset write-downs](#). Clients can see all adjustments made to Home Depot's balance sheet on the GAAP Reconciliation tab on the Ratings page on our website.

Valuation: we made \$48.3 billion in adjustments, all of which decreased shareholder value. Apart from [total debt](#), the most notable adjustment to shareholder value was \$565 million in [deferred tax liabilities](#). This adjustment represents <1% of Home Depot's market cap. Clients can see all adjustments to Home Depot's valuation on the GAAP Reconciliation tab on the Ratings page on our website.

This article originally published on [September 22, 2022](#).



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” enables investors to overcome these flaws and apply [reliable](#) fundamental data in their research.
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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