A Terrible Business With An Incredibly Optimistic Valuation

Do you ever wonder how disconnected a stock's valuation can possibly get from the fundamentals of the underlying business?

That question is hard to answer with traditional valuation tools and ratios. But, answering that question is exactly what our reverse discounted cash flow (DCF) model allows us to do for the thousands of stocks we cover.

During a recent Earnings Recap session, we reviewed Affirm (AFRM: $62/share) and did a deep dive into its valuation. The results were shocking. Rarely will you see a stock with a valuation so disconnected from the fundamentals of the business. Let's get specific

Expectations Investing Analysis on AFRM

As we do for all of our Reverse DCF Case Studies, we use our valuation models to quantify the future performance of the company required to justify its current stock price.

Specifically, our model shows that to justify ~$62/share Affirm would have to:

1. grow revenue at 26.3% compounded annually for 8 years while also
2. improving its return on invested capital (ROIC) from -8% to 122% and
3. improving its net operating profit after tax (NOPAT) from $0.3 billion to $3.6 billion.

Let's put some context around those expectations.

Benchmarking Expectations for AFRM

First, growing revenue at 26.3% CAGR for 8 years means Affirm's revenue would be $15 billion in 2033. While also growing revenue at a rapid pace, the stock price implies Affirm will also increase its ROIC and NOPAT to very high levels. See Figure 1 for details.

Figure 1: Ranking Affirm's Expected Cash Flows to the S&P 500

Implied Rank in the S&P 500	Key Operating Metric	TTM Values	Values Implied by Current Stock Price
4	ROIC	-8%	122%
126	NOPAT	-$0.3	$3.6
250	Revenue	$2.8	$15.0

$ in billions

Sources: New Constructs, LLC and company filings.

Video Case Study: A Terrible Business with A Worse Valuation

As we discuss in our latest reverse DCF case study video, we think there are several reasons why the expectations embedded in Affirm's current stock price are too high.

Competitive Realities

Large revenue growth, like what's embedded in Affirm's stock price, implies significant market share gains. We note that market share gains are typically won with lower prices, which are not possible with a company that must also increase its ROIC and NOPAT to very high levels.

In other words, Affirm's stock price is implying a doubly-incredible future where the company enjoys huge revenue growth and NOPAT and ROIC improvement as well.

Where to Find Good Stocks

We're not here just to warn you about the bad stocks, we're here to help you find good ones, too. We provide our proven-superior ratings on over 3,300 stocks. Unlike Wall Street, where 95% of the stocks get a Buy or Hold Rating, less than 15% of our stocks get an Attractive or Very Attractive Rating. We work hard to provide the best fundamental research in the world. We're constantly providing free training and stock picks to help investors make more money and invest with peace of mind.

Figure 2: How To Find The Right Stocks: The Robo-Analyst Rating System

	Quality of Earnings		Valuation		
Risk/Reward Rating	Economic vs Reported EPS	ROIC	2 yr Avg FCF (excl cash) Yield	Price to EBV	Market-Implied GAP
Very Unattractive	Misleading Trend	Bottom Quintile	< -5%	> 3.5 or -1 < 0	> 50
Unattractive	False Positive	4th Quintile	-5% < -1%	2.4 < 3.5 or < -1	20 < 50
Neutral	Neutral EE	3rd Quintile	-1% < 3%	1.6 < 2.4	10 < 20
Attractive	Positive EE	2nd Quintile	3% < 10%	1.1 < 1.6	3 < 10
Very Attractive	Rising EE	Top Quintile	> 10%	0 < 1.1	0 < 3
Actual Values					
	$1.81 vs. $4.79	13%	-3%	0.8	< 1 yr

Sources: New Constructs, LLC and company filings.

We think the MOMO, YOLO, SPAC, NFT, meme stock and meme coin trading ploys are bad for investors, bad for our stock market, and bad for our country. We're here to give you proven-superior investment research that is good for the long-term health of your portfolio and your peace of mind.

More Expectations Investing Case Studies

Too few investors have the tools to unveil the details behind stock valuations. We make it clear and easy. Math is math. It's not supposed to be hard. Wall Street wants to keep you in the dark by making you think it is too hard to get the truth about valuation.

We shed light into the dark corners of the market and make them into opportunities to profit.

If you enjoyed seeing what we show for Affirm's real cash flows as well as the future revenue expectations baked into the stock price, you'll love our other reverse DCF case studies.

If you're interested in seeing more examples of how our DCF model works, I recommend checking out the Reverse DCF Case Studies here in our Online Community. To join our Online Community, complete this form.

Our community is free to join as is access to the Reverse DCF case studies.

How To Avoid the Landmines

Whenever stocks get super expensive, it is only a matter of time before they fall back to earth as the law of competition inevitably proves the expectations for future cash flows to be overly optimistic.

We have multiple Model Portfolios, including our Zombie Stocks list, to warn investors of stocks to avoid and alert them to stocks that get our Attractive rating. We also provide best-in-class ratings for stocks, ETFs, and mutual funds.

We hope you enjoy this research. Feel free to share with friends and colleagues!

This article was originally published on February 27, 2025.

Disclosure: David Trainer, Kyle Guske II, and Hakan Salt receive no compensation to write about any specific stock, sector, style, or theme.

Questions on this report or others? Join our online community and connect with us directly.

It's Official: We Deliver 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. The stock market is missing footnotes – and only we have that critical data.
2. Legacy fundamental datasets suffer from significant inaccuracies, omissions, and biases.
3. Our proprietary drives novel alpha. Our measures of Core Earnings and Earnings Distortion materially improve stock picking and forecasting of profits.

Best Fundamental Data in the World

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

Ernst & Young 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 Harvard Business School. 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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