



Featured Stock in July’s Exec Comp & ROIC Model Portfolio

Two new stocks make July’s Exec Comp Aligned with ROIC Model Portfolio, available to members as of July 14, 2023.

Recap from June Picks

Our Exec Comp Aligned with ROIC Model Portfolio (+5.6%) outperformed the S&P 500 (+0.8%) from June 15, 2023 through July 12, 2023. The best performing stock in the portfolio was up 19%. Overall, 13 out of the 15 Exec Comp Aligned with ROIC Stocks outperformed the S&P from June 15, 2023 through July 12, 2023.

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](#).

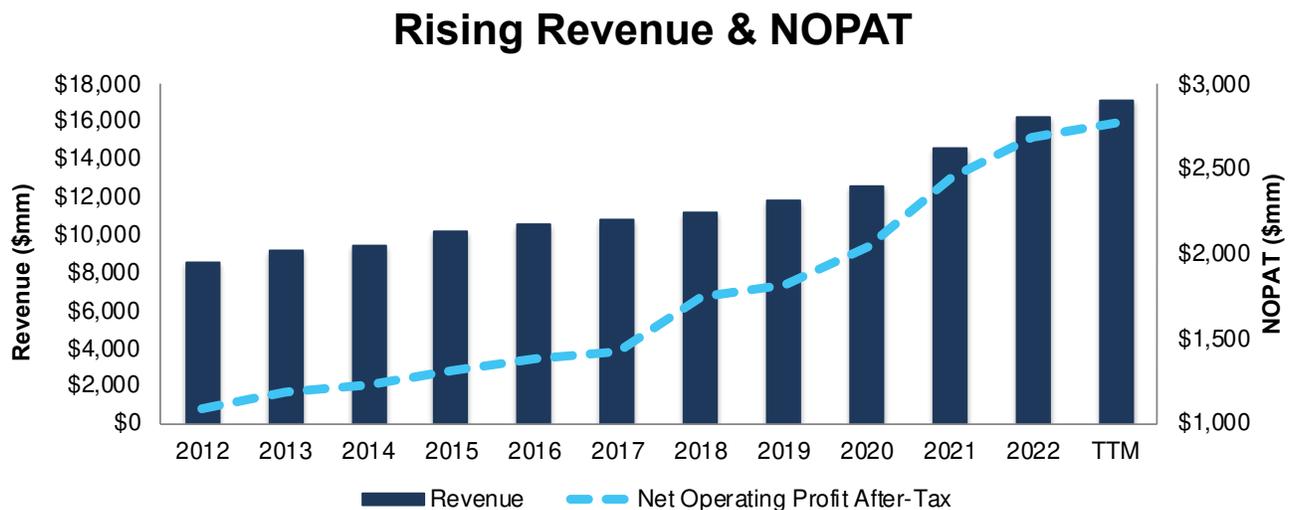
This Model Portfolio includes stocks that earn an [Attractive or Very Attractive](#) rating and align executive compensation with improving ROIC. This combination provides a unique list of long ideas as the [primary driver](#) of shareholder value creation is return on invested capital ([ROIC](#)).

New Stock Feature for July: AutoZone Inc. (AZO: \$2,505/share)

AutoZone (AZO) is the featured stock in July’s Exec Comp Aligned with ROIC Model Portfolio. We originally made AutoZone a Long Idea in [February 2014](#) and reiterated it in [January 2022](#), and the stock remains undervalued.

AutoZone has grown revenue and net operating profit after tax ([NOPAT](#)) by 7% and 10% compounded annually, respectively, since 2012. The company’s NOPAT margin improved from 13% in 2016 to 16% in the trailing twelve months (TTM), while [invested capital turns](#) rose from 1.8 to 2.2 over the same time. Rising NOPAT margins and invested capital turns drive the company’s return on invested capital ([ROIC](#)) from 23% in 2016 to 36% in the TTM.

Figure 1: AutoZone’s Revenue & NOPAT: 2012 – 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](#).

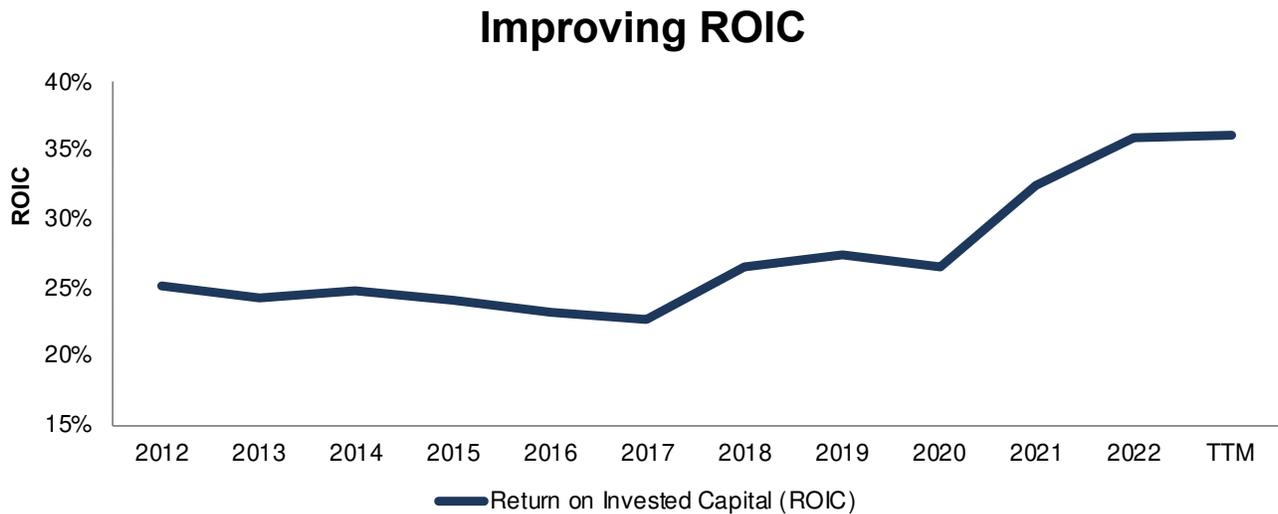


Executive Compensation Properly Aligns Incentives

AutoZone’s executive compensation plan aligns the interests of executives and shareholders by tying its annual incentive awards to economic profit, which, similar to our [economic earnings](#), is driven by NOPAT and ROIC. According to AutoZone’s proxy [statement](#), the company uses economic profit because it “ensures that growth, as well as the cost of growth, are balanced and achieved in a manner that maximizes the long-term interests of our shareholders.”

The company’s inclusion of economic profit, which is primarily driven by ROIC, as a performance goal has helped create shareholder value by driving higher ROIC and [economic earnings](#). When we calculate ROIC using our [superior fundamental data](#), we find that AutoZone’s ROIC has increased from 25% in 2012 to 36% in the TTM. Economic earnings rose from \$963 million to \$2.3 billion over the same time.

Figure 2: AutoZone’s ROIC: 2012 – TTM



Sources: New Constructs, LLC and company filings

AZO Has Further Upside

At the current price of \$2,505/share, AZO has a price-to-economic book value ([PEBV](#)) ratio of 1.3. Though the company’s PEBV ratio is higher than other Long Ideas, we believe AutoZone’s competitive moat positions it for further growth and the stock still holds upside potential.

Even if AutoZone’s NOPAT margin falls to 14% (10-year average, compared to 16% in the TTM) and the company’s revenue grows 7% compounded annually over the next decade (equal to compound annual growth rate over past decade), the stock would be worth \$3,016/share today – a 20% upside. [See the math behind this reverse DCF scenario](#). In this scenario, AutoZone’s NOPAT grows 6% compounded annually through 2032.

For reference, AutoZone has grown NOPAT by 10% compounded annually since 2012. 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 made based on Robo-Analyst findings in AutoZone’s 10-Qs and 10-K:

Income Statement: we made \$411 million in adjustments with a net effect of removing \$253 million in [non-operating expenses](#) (1% of revenue). Clients can see all adjustments made to AutoZone’s income statement on the GAAP Reconciliation tab on the Ratings page on our website.

Balance Sheet: we made \$1 billion in adjustments to calculate invested capital with a net increase of \$332 million. One of the largest adjustments was \$301 million (4% of reported net assets) in [other comprehensive income](#). Clients can see all adjustments made to AutoZone’s balance sheet on the GAAP Reconciliation tab on the Ratings page on our website.



Valuation: we made \$12.1 billion in adjustments, with a net effect of decreasing shareholder value by \$12 billion. Apart from [total debt](#), the most notable adjustment to shareholder value was \$1.4 billion in value of [outstanding ESO's after tax](#). This adjustment represents 3% of AutoZone's market value. Clients can see all adjustments to AutoZone's valuation on the GAAP Reconciliation tab on the Ratings page on our website.

This article was originally published on [July 20, 2023](#).

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

Questions on this report or others? Join our [Society of Intelligent Investors](#) and connect with us directly.



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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