Free Stock Pick from our Most Dangerous Stocks Model Portfolio for March 2025

Earlier this week, Reuters reported that Taiwan Semiconductor Manufacturing Co. (TSM) reached out to Nvidia (NVDA), Advanced Micro Devices (AMD), Qualcomm (QCOM), and Broadcom (AVGO) to pitch a joint venture that would run Intel's (INTC) foundries. New Intel CEO, Lip-Bu Tan, has a big decision to make regarding the future of Intel's foundry business, perhaps sooner than anyone may have anticipated.

After the Reuters report, the stocks mentioned jumped. Although a joint venture of this caliber is not to be taken lightly, its impact on the prices of the stocks for these companies should be scrutinized. Even though the market is becoming more efficient, hype and momentum have not left the building. We're a long way from a perfectly efficient market – thank goodness, or there would be no reason for any of us to be in the market.

I realize that is a small consolation for what has been a rough year for many investors. We cannot turn back the clock and fix your portfolio, but we can help you protect your portfolio going forward. Our research has always focused on serving you, the investor, first and foremost by giving you research based on real diligence that you can trust. Following the whims and noise of the market might be fun in the short term, but, in the long term, it is dangerous.

We prefer to avoid danger, and this week we make it easy for you to avoid danger in the stock market by giving you a free stock pick from our Most Dangerous Stocks Model Portfolio. This Model Portfolio finds the worst of the worst stocks in any kind of market. The stocks in this Model Portfolio have both terrible fundamentals and expensive valuations. In other words, the risk/reward for these stocks is very dangerous.

This free stock feature provides a concise summary of how we pick stocks for this Model Portfolio. It is not a full Danger Zone report, but it gives you insight into the rigor of our research and approach to picking stocks. Whether you're a subscriber or not, we think it is important that you're able to see our research on stocks on a regular basis.

We're proud to share our work. Please feel free to share it with your friends and family.

Keep an eye out for the free pick from our Most Attractive Stocks Model Portfolio, which will be published this week as well! The work that goes into that report is just as valuable.

We update this Model Portfolio monthly. The latest Most Attractive and Most Dangerous stocks Model Portfolios were updated and published for clients on March 5, 2024.

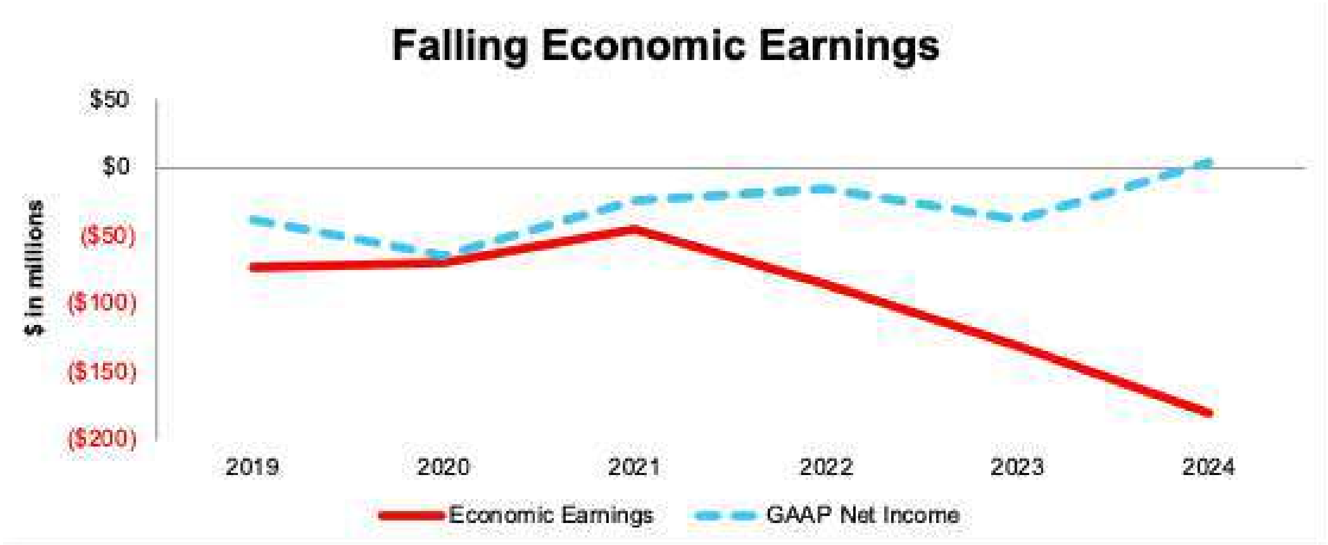
Free Most Dangerous Stock Pick: Krispy Kreme Inc. (DNUT)

Krispy Kreme Inc. (DNUT: $6/share) is the featured stock from March's Most Dangerous Stocks Model Portfolio.

Krispy Kreme's net operating profit after tax (NOPAT) margin fell from 9% in 2019 to 1% in 2024, while the company's invested capital turns rose from 0.3 to 0.5 over the same time. Falling NOPAT margins offset the improved capital turns and drive Krispy Kreme's return on invested capital (ROIC) from an already low 3.1% in 2019 to 0.7% in 2024.

Krispy Kreme's economic earnings, the true cash flows of the business, fell from -$73 million in 2018 to -$181 million in the TTM. Meanwhile, the company's GAAP net income rose from -$37 million to $3 million over the same time. Whenever GAAP earnings rise while economic earnings decline, investors should beware.

Figure 1: Krispy Kreme' Economic vs GAAP Earnings Since 2019



Sources: New Constructs, LLC and company filings

DNUT Provides Poor Risk/Reward

Despite its poor and declining fundamentals, Krispy Kreme's stock is priced for significant profit growth, and we believe the stock is overvalued.

To justify its current price of $6/share, Krispy Kreme must improve its NOPAT margin to 3% (compared to 1% in 2024) and grow revenue by 16% (compared to 12% compounded annually over the last five years) compounded annually over the next ten years. In this scenario, Krispy Kreme's NOPAT would grow 25% compounded annually to $220 million in 2034. We think these expectations are overly optimistic, especially considering the company's NOPAT fell 23% compounded annually over the last five years.

Even if Krispy Kreme improves its NOPAT margin to 3% and grows revenue 12% compounded annually through 2034, the stock would be worth no more than $2/share today – a 70% downside to the current stock price. The huge amount of debt piled onto the company by the private equity firm that IPO'd Krispy Kreme makes it hard for equity investors to get much value, if any.

Each of these scenarios also assumes Krispy Kreme can grow revenue, NOPAT, and FCF without increasing working capital or fixed assets. This assumption is unlikely but allows us to create best case scenarios that demonstrate the high expectations embedded in the current valuation.

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 Krispy Kreme's 10-K:

Income Statement: we made around $200 million in adjustments, with a net effect of removing just under $50 million in non-operating expenses. Professional members can see all adjustments made to Krispy Kreme's income statement on the GAAP Reconciliation tab on the Ratings page on our website.

Balance Sheet: we made over $600 million in adjustments to calculate invested capital with a net increase of around $600 million. One of the most notable adjustments was for operating leases. Professional members can see all adjustments made to Krispy Kreme's balance sheet on the GAAP Reconciliation tab on the Ratings page on our website.

Valuation: we made over $1.8 billion in adjustments, all of which decreased shareholder value. The most notable adjustment to shareholder value was for total debt. Professional members can see all adjustments to Krispy Kreme's valuation on the GAAP Reconciliation tab on the Ratings page on our website.

This article was originally published on March 13, 2025.

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