Don’t Be Misled by Flawed Metrics

The quality of Wall Street research has been steadily going down over the last couple of decades.

To phrase that sentence better: Wall Street analysts are becoming more manipulative. One of their most devious tricks is to publish lower EPS estimates for stocks they like so it is easier for the companies to “beat”.

Frankly, there isn’t much substance to Wall Street research nowadays, just narratives and added confusion to hide the truth.

How are investors supposed to see through this noise? Our CEO, David Trainer, not only outlined the problem but also provided solutions during his appearance on the Value Spotlight podcast. Check it out below.

Watch the Value Spotlight Podcast Replay

To cut through the misleading narratives, investors need rigorous, independent research grounded in sound economic principles.

Proven metrics such as return on invested capital (ROIC) and economic earnings offer a more accurate view of a company’s true profitability than the often misleading "adjusted" metrics that dominate modern earnings releases.

These adjusted figures, particularly adjusted EBITDA, are rife with inconsistencies. Not only do companies differ in how they calculate this metric, but they also commonly exclude legitimate operating expenses, which only, inflates profitability. This practice paints a rosier picture of financial health than reality warrants.

The structural incentives on Wall Street to uphold bullish ratings have contributed to the widespread use of these customized, non-GAAP metrics.

Adjustments are just the tip of the iceberg, though, when it comes to misleading metrics. Companies often exploit both legal and, at times, borderline illegal accounting practices to obscure real expenses and financial risks.

Where do companies hide these crucial details?

They are buried deep in the footnotes and MD&A sections of company filings, or the areas routinely overlooked by most investors and many research firms.

The only way to truly understand the health of the underlying business of a company is to go through the footnotes in the filings.

There are no shortcuts to truly understanding a company’s financial health. It requires thorough, diligent analysis of the complete financial filings, the kind of analysis we specialize in.

Lucky for you if you are reading this message, you’ve already found a resource that delivers proven-superior, footnote-level data and research at scale – empowering you to compete on more equal footing with Wall Street. To learn more, watch the replay of our appearance in the Value Spotlight podcast.

Watch the Value Spotlight Podcast Replay

Want data that can generate alpha in any market?

Learn more about our memberships here.

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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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