CPI *Insights*

eva Dimensions
Better Decisions. More Value.

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CPI, for corporate performance index, is a summary score of financial excellence that rates a company against peers on a percentile scale. It tends to confirm a company's TSR rank when the rank is right, challenges TSR when it is wrong, and explains the factors that are determining TSR in any case.

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A Good Company or a Good Buy? *Can you use CPI to pick stocks and beat the market? No, a great company may be no bargain at all if its priced too high. Picking undervalued stocks calls for a different model, which we call PRVit (pronounced "prove-it," standing for the performance-risk-valuation investment technology). It uses 24 metrics to develop a buy-hold-sell index. It finds stocks that are trading for less than CPI says they are worth. It is featured on Fidelity.com and Bloomberg, and underpins a global equity research service that we provide to institutional investors. In this issue, we apply CPI and PRVit to Amazon and Gentex and illustrate the differences.*

CPI is an index of excellence. It rates the management quality and the firm's financial prowess. It ranks companies by how well they are performing—in terms of earning and increasing EVA—and by how highly valued they are—in terms of market-to-book premiums and investors' expectations for growth in EVA. It essentially is the sum of a percentile "P-score" (for Performance) and "V-Score" (for Value). Said simply, CPI = P + V, it's performance *plus* value.

In CPI, a higher valuation is better because that indicates a company has invested resources wisely. It also typically signals confidence that management has cleared a runway to lift EVA profits in the years ahead.

But a higher valuation is a *minus* for investors. It's an impediment to earning a high rate of return. The higher a stock is priced, the lower the return will end up being for any given level of performance.

Investors also are concerned with risk. They ask: Is the company reliable and predictable, with established franchises, or is it skittish and uncertain, and caught up in commodity battles? Is it cyclical and apt to fall off the rails when the economy loses steam, or is it resilient in downturns? Is it precariously financed, or does it have staying power and strong cash flows? All these factors are subsumed in a percentile risk score, "R," and the higher it is, the less attractive a stock is to own at a given price.

PRVit combines performance, risk and value into a buy-hold-sell rating score. Whereas CPI rates quality, with P plus V, PRVit rates affordability, with (P-R)/V; it's the company's performance score, less its risk score, divided by its valuation score, relative to peers. It's a risk-adjusted return-on-value index, and the higher it is, the more attractive a stock is to buy, and the lower it is, the more the stock should be shunned or sold short.

AMZN	USA	CPI Score: 81
Sales	**Sales Growth**	**3-Year Trend Growth**
$ 120,637	25.9%	21.5%
EVA	**EVA Margin**	**3-Yr Trend EVA Mo**
$ 4,458	3.7% (71)	1.15% (82)
MVA	**MVA Margin**	**Mkt-Imp Mo**
$ 354,392	294% (76)	2.02% (76)

Financial data through June 30th, 2016; Market Data as of October 20th, 2016

Let's use Amazon as a case study. Its CPI, as you might expect, is quite good, a score 81 among internet and catalogue retailers. EVA and MVA margins both run high and near 75th percentile. Trend line EVA growth was 1.15% of sales per annum, or 82nd percentile, over the past three years, and the market-implied forecast for EVA Momentum is better still, over 2% a year, putting Amazon into the upper quartile on both counts. Amazon has been a superlative performer, with no notable weaknesses in any dimension. Bezos and company well deserve an 81st percentile rating on the corporate excellence scale

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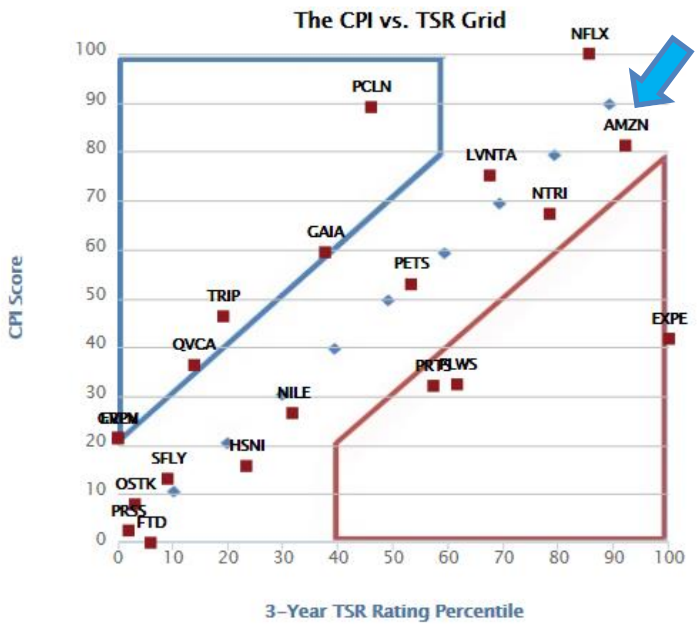
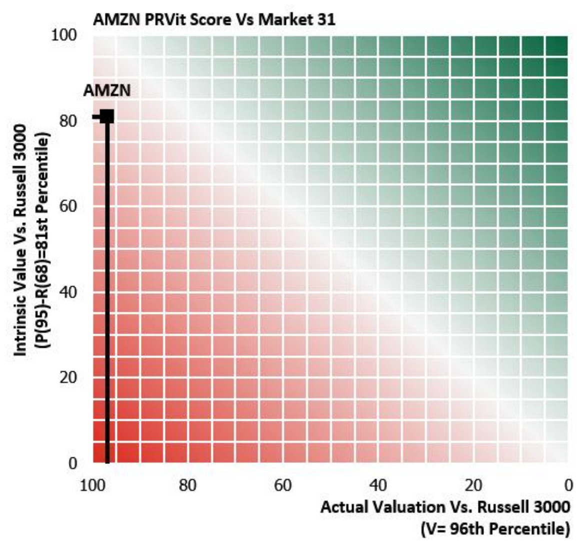


Amazon's CPI also does a good job of accounting for its 3-year TSR rank, as is evident on the grid at left, which charts internet and catalogue retailing players. AMZN plots right along the lower-left to upper-right diagonal, as do most peers, the only real exceptions being Priceline (PCLN), a blue-zone Dangerfield, and Expedia (EXPE), a red-zone Dandy Don. But those aside, the correlation is clear. CPI does indeed tend to align with, and explain, relative TSRs ranked over the ***prior*** three years.

CPI scores, however, do not align with ***forecast*** TSRs, with the TSRs in the years ahead. CPI is not predictive, and nor is it intended to be. PRVit, though, is. The question PRVit answers is, is Amazon a ripe buy at today's stock price, given how highly valued it has become? And there the answer is, no.



PRVit can be visualized on a grid, as at right. A company's P-R score—its risk-adjusted performance score, a measure of its intrinsic value—plots south to north, on the Y axis. Its composite V score plots right to left, backwards, on the X axis, with higher valuations more westward. Fairly-valued stocks thus plot along the upper-left to lower-right diagonal. Along that line, you tend get what you pay for. The stocks are trading at prices that aptly reflect their intrinsic P-R values. Buy those, and you can expect to earn a normal competitive return compared to all other stocks. The stocks to buy fall into in the upper-right green zone, which is where P-R outstrips V. The ones to sell or sell short appear in the lower-left red zone, which is where the firm's intrinsic P-R value falls short of the V you must pay.

That's where Amazon plots. PRVit rates it a sell, with a score of 31 on a 100-point scale. AMZN is a great company—it's P score is 95, and risk-adjusted P score is 81 (PRVit judges AMZN to be a relatively risky stock)—but it is trading at such a high valuation—at a V-score of 96, nearly off the charts—that PRVit could find you much better buys elsewhere, stocks that offer much more value at a more reasonable price. In sum, Amazon's P+V score, its CPI, is high, but its (P-R)/V ratio, its PRVit score, is low. Admire CPI, buy PRVit, is the mantra.

For example, buy Gentex, a specialist in dimmable auto and aero mirrors and commercial smoke alarms and signaling devices. It currently rates a CPI score of 88 versus its peers. It's only blemish amid a bevy of admirable CPI metrics is trading for a low multiple of EVA. The stock is priced for a slight deterioration in EVA in years ahead. From a CPI perspective, though, the company's simply superb, double-digit, 12.7% EVA profit margin, its torrid, 2.2% EVA Momentum growth pace over the past three years, and its upper-decide wealth creation index are decisive, and lead to the judgement it is an outstanding company. But from a PRVit perspective, the stock looks cheap. It is trading for an attractively low valuation. PRVit currently rates Gentex 97, a strong buy, based on its (P-R)/V index.

GNTX	USA	CPI Score: 88
Sales	Sales Growth	3-Year Trend Growth
$ 1,665	11.8%	13.8%
EVA	EVA Margin	3-Yr Trend EVA Mo
$ 211	12.7% (100)	2.19% (100)
MVA	MVA Margin	Mkt-Imp Mo
$ 2,864	172% (94)	-0.07% (29)

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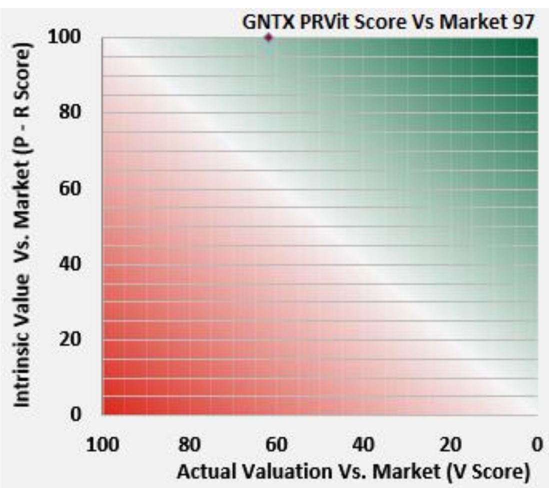
Score	Metric	GNTX	25th	50th	75th	% Russell
96	**Performance Score (P)** — Higher is better					
92	**P1 Profitability** — Financial strength in generating a return on capital over the full cost					
	EVA Margin (EVA/Sales)	12.9%	-4.5%	0.5%	4.7%	93
	EVA Spread (EVA/Capital)	13.3%	-2.9%	0.4%	3.9%	93
92	**P2 Trend** — The growth rate in the firm's economic profit (its EVA)					
	EVA Momentum (vs Cap)	3.0%	-1.4%	0.3%	1.6%	86
	3 Year Trend (ΔEVA/Cap)	2.3%	-0.8%	0.1%	1.0%	88
	Last Quarter (ΔEVA/Cap)	3.0%	-1.5%	0.2%	1.7%	84
1	**Risk Score (R)** — Lower is better					
6	**R1 Volatility** — Variability in stock price and the EVA profit margin					
	Stock Price Volatility	23%	25%	33%	46%	20
	EVA Margin Variability	1.1%	1.6%	3.1%	7.4%	15
14	**R2 Vulnerability** — Leveraged, negative cash flow firms are suspect					
	Free Cash Flow Rate	20%	9%	2%	-8%	9
	Op Cash Gen Return	50%	59%	27%	12%	31
	Total Debt/Total Capital	10%	10%	32%	50%	25
	Total Debt/EBITDAR	0.3	1.2	2.5	4.4	8
65	**Valuation Score (V)** — Lower is better					
75	**V1 Wealth Ratios** — Valuation multiples to book capital (as adjusted)					
	MVA Margin	194%	12%	76%	198%	75
	MVA Spread	201%	9%	51%	151%	80
30	**V2 Wealth Multiples** — Valuation multiples to cash flow, earnings, EVA					
	EBITDAR Multiple	7.1	6.9	9.2	12.7	28
	NOPAT Multiple	14.2	17.4	23.3	32.1	12
	Future Growth Reliance	6%	5%	28%	65%	26

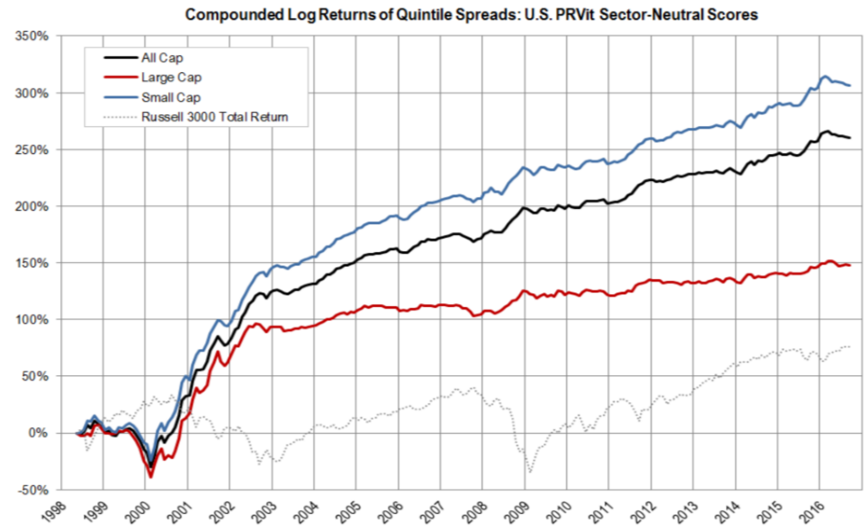
The table at left presents many of the metrics that PRVit considers to determine a stock's P, R, and V scores. Unlike CPI, which is based on the four most essential metrics, PRVit brings a broader array of sensors into play. EVA Momentum, for example, is gauged three ways—over the past three-years as with CPI, but also, over the past year and for the most recent quarter. PRVit traces out the full arc of the EVA curve to detect any faltering or hardening in the EVA trajectory. As for Gentex, all three readings are solid and near the 85th percentile compared to Russell 3,000 firms.

That consistency also is reflected in a very low risk score. Gentex's stock price and EVA Margin are relatively unflappable, it generates a strong positive cash flow, and it is conservatively financed. Its stability and staying power are indeed impressive. Its risk score, R, is 1.

Despite these glowing marks, Gentex trades for a V score of just 65. It's priced at a 75th percentile set of price-to-book, or MVA, ratios, but at only the 30th percentile on multiples of earnings, cash flow and EVA. Future Growth Reliance, the metric appearing at the very bottom of the table, reflects this. It is the percent of the firm's value that depends on, and is at risk of, continued growth in EVA. For Gentex, it is 6%. Just 6% of the company's enterprise value depends on growing EVA. Almost 3 out of 4 companies on the market are priced for more rapid EVA Momentum.



Put it all together, and Gentex looks dirt cheap compared to its intrinsic P-R value. It plots in the upper right "buy zone" on the heat map at left, corresponding to a PRVit score of 97.



Does PRVit work? The chart at right shows the result from mid-1998 through Q3 of 2016 of buying the stocks that PRVit rated 80-100 and shorting the overpriced ones that scored 0-20 in each industry. That strategy, essentially a bet on PRVit, shown in black, significantly outperformed the Russell 3000, shown in gray (PRVit does even better with small cap stocks than more actively-followed large caps). Which is why institutional investors in the US and Europe are using it for stock selection and portfolio management, and why corporate CFOs and IR Directors consult it for insights into how the market is perceiving, or misperceiving, their stock.

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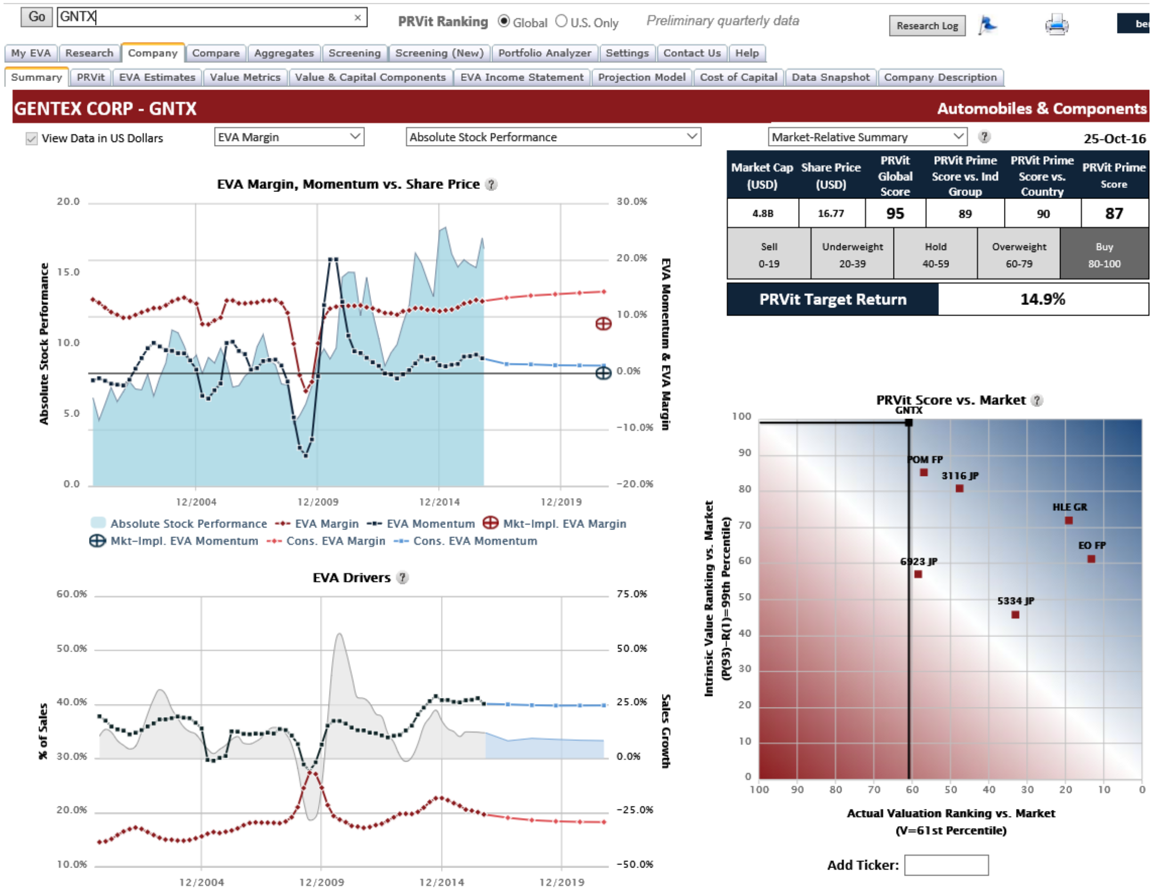
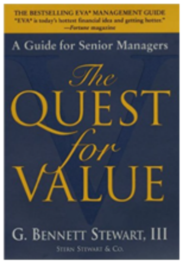
Investor *Express* is the portal to PRVit research; contact info@evadimensions.com for a demo



EVA Dimensions

- Bennett Stewart launches EVA with 1991 book, *The Quest for Value*
- *Fortune* magazine editors feature EVA on September, 1993 cover with headline, "EVA – It's the Real key to Creating Wealth"
- Hundreds of companies adopt EVA globally – Coca-Cola, AT&T, Equifax, Eli Lilly, Herman Miller, Monsanto, Halliburton, Brahma Beer (now AB InBev), Kao Brands (Japan), Lafarge, Port of Singapore Authority, Temasek, TATA Group, CEMEX, FEMSA, are a few
- EVA Dimensions spins out in 2006 to convert EVA to a new ratio framework, automate it with software and data, and serve corporations and investors
- Enhanced EVA model presented in the 2013 book, *Best-Practice EVA*
- Early corporate adopters include Dow Chemical, PepsiCo



EVA Dimensions is a financial technology and advisory firm.

We help our clients to make better decisions and create more value with the power of EVA.

We license software that companies use to compute, analyze, benchmark and value EVA in reporting, planning and M&A applications, and that investors use to pick stocks and manage portfolios.

We also provide the training and support needed to transition management teams and directors onto EVA.

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