28th ANNUAL WEALTH CREATION STUDY (2018-2023)

Hockey-Stick Returns

The power of Economic Profit

HIGHLIGHTS

- Economic Profit is a superior metric to Accounting Profit to understand true profitability of a company.
- TEM (Trend, Endowment and Moves) is a sound strategy for companies to move up the Economic Profit Power Curve.
- Successful TEM companies bought at reasonable price improve the chances of Hockey-Stick Returns.
- Mid and small caps are favorably placed to deliver Hockey-Stick returns.
- After two decades of sustained decline, PSU stocks are on a comeback.

TOP 10 WEALTH CREATORS (2018-2023)

BIGGEST

Rank	Company	Wealth Created (INR b)
1	Reliance Industries	9,638
2	TCS	6,774
3	ICICI Bank	4,155
4	Infosys	3,618
5	Bharti Airtel	2,808
6	Hind. Unilever	2,718
7	State Bank of India	2,442
8	Bajaj Finance	2,285
9	Adani Enterprises	1,746
10	HCL Technologies	1,636

FASTEST

Company	5-year Price CAGR (%)
Lloyds Metals	79
Adani Enterprises	78
Tube Investments	63
Linde India	56
Adani Power	52
Capri Global	50
Varun Beverages	50
Deepak Nitrite	49
Persistent Systems	46
J B Chem & Pharma	45

CONSISTENT

Company	No. of years outperformed	5-year Price CAGR (%)
Capri Global	5	50
Varun Beverages	5	50
Grindwell Norton	5	30
ICICI Bank	5	26
Adani Enterprises	4	78
Tube Investments	4	63
Linde India	4	56
Adani Power	4	52
J B Chem & Pharma	4	45
SRF	4	44

Raamdeo Agrawal (Raamdeo@MotilalOswal.com) / **Shrinath Mithanthaya** (Shrinath.Mithanthaya@gmail.com)
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Motilal Oswal 28th Annual Wealth Creation Study

Abbreviations and Terms used in this report

Abbreviation / Term	Description
2013, 2018, 2023, etc	Reference to years for India are financial year ending March, unless otherwise stated
Avg	Average
CAGR	Compound Annual Growth Rate
INR bn	Indian Rupees in billion
L to P / P to L	Loss to Profit / Profit to Loss. In such cases, calculation of PAT CAGR is not possible
Price CAGR	In the case of aggregates, Price CAGR refers to Market Cap CAGR
WC	Wealth Created
Wealth Created	Increase in Market Capitalization over the last 5 years, duly adjusted for corporate actions such as fresh equity issuance, mergers, demergers, share buybacks, etc.

Note: Capitaline database has been used for this study. Source of all exhibits is MOFSL analysis, unless otherwise stated

Wealth Creation Study

Objective, Concept & Methodology

Objective

The foundation of Wealth Creation is to buy businesses at a price substantially lower than their “intrinsic value” or “expected value”. The lower the market value compared to the intrinsic value, the higher is the margin of safety. Every year, as in the past 28 years, we endeavor to cull out the characteristics of businesses that create value for their shareholders.

As Phil Fisher says, “*It seems logical that even before thinking of buying any common stock, the first step is to see how money has been most successfully made in the past.*” Our Wealth Creation Studies are attempts to study the past as a guide to the future, and gain insights into the various dynamics of stock market investing.

Concept & Methodology

Wealth Creation is the process by which a company enhances the market value of the capital entrusted to it by its shareholders. It is a basic measure of success for any commercial venture. For listed companies, we define Wealth Created as the difference in market capitalization over a period of last five years, duly adjusted for corporate events such as fresh equity issuance, mergers, demergers, share buybacks, etc.

We rank the top 100 companies in descending order of absolute Wealth Created, **subject to the company’s stock price at least outperforming the benchmark index (BSE Sensex in our case).** These top 100 Wealth Creators are also ranked according to speed (i.e. price CAGR during the period under study).

We define **Consistent Wealth Creators** based on the number of years the stock has outperformed in each of the last 5 years. Where the number of years is the same, the stock price CAGR decides the rank.

We define **All-round Wealth Creators** based on the summation of ranks, under each of the 3 categories – Biggest, Fastest and Consistent. Where the scores are tied, the stock price CAGR decides the All-round rank.

Report structure

We present the 2018-2023 Wealth Creation Study highlights in pages 2-3. The detailed findings are presented in pages 32-48. Appendix 1 (pages 50-51) ranks the top 100 Wealth Creators by size, Appendix 2 (pages 52-53 ranks the same 100 Wealth Creators by speed, Appendix 3 (pages 54-55) lists the Consistent Wealth Creators, Appendix 4 (pages 56-57) presents the All-round Wealth Creators, and Appendix 5 (pages 58-59) provides an alphabetical listing of the Wealth Creators.

This year’s theme study titled “**Hockey Stick Returns: The power of Economic Profit**” is featured in pages 4-31.

Wealth Creation 2018-2023: Highlights

Reliance emerges as the largest Wealth Creator for the 5th time in a row

- For the fifth time in succession, **Reliance Industries** has emerged the largest Wealth Creator over 2018-23.
- This takes Reliance's overall No.1 tally to 10 in the last 17 five-year study periods.

Exhibit 1 **Top 10 Biggest Wealth Creators (2018-23)**

Rank	Company	Wealth Created		CAGR (%)		P/E (x)		RoE (%)	
		INR bn	% share	Price	PAT	2023	2018	2023	2018
1	Reliance Inds	9,638	13.7	22	13	24	15	9	12
2	TCS	6,774	9.6	18	10	28	21	47	30
3	ICICI Bank	4,155	5.9	26	35	18	23	16	7
4	Infosys	3,618	5.1	20	9	25	16	37	24
5	Bharti Airtel	2,808	4.0	16	45	49	115	11	2
6	Hind. Unilever	2,718	3.9	14	14	59	55	20	72
7	SBI	2,442	3.5	16	L to P	8	N.A.	17	-2
8	Bajaj Finance	2,285	3.2	26	36	30	41	21	16
9	Adani Enterprise	1,746	2.5	78	34	81	30	7	4
10	HCL Tech	1,636	2.3	18	11	20	16	22	24
Total of Top 10		**37,819**	**54**	**21**	**22**	**23**	**25**	**16**	**11**
Total of Top 100		**70,488**	**100**	**22**	**22**	**26**	**27**	**16**	**11**

Lloyds Metals has emerged the Fastest Wealth Creator

- A low-profile company, **Lloyds Metals**, has emerged the Fastest Wealth Creator with 2018-23 Price CAGR of 79%.
- INR 1 million invested in 2018 in the top 10 Fastest Wealth Creators would be worth INR 10 million in 2023, a return CAGR of 59% vi/s 12% for the BSE Sensex.

Exhibit 2 **Top 10 Fastest Wealth Creators (2018-23)**

Rank	Company	Price Appn. (x)	Price CAGR %	PAT CAGR %	Mkt Cap (INR bn)		P/E (x)	
					2023	2018	2023	2018
1	Lloyds Metals	19	79	125	127	3	14	22
2	Adani Enterprises	18	78	34	1,995	172	81	30
3	Tube Investments	11	63	53	491	42	37	27
4	Linde India	9	56	91	344	38	65	179
5	Adani Power	8	52	L to P	739	92	7	N.A.
6	Capri Global	8	50	26	134	16	66	25
7	Varun Beverages	8	50	50	901	113	57	53
8	Deepak Nitrite	7	49	59	251	34	30	41
9	Persistent Systems	7	46	25	352	55	38	18
10	J B Chem & Pharma	6	45	31	153	26	37	24

Capri Global is the Most Consistent Wealth Creator

- We define Consistent Wealth Creators based on the number of years the stock has out-performed in each of the last 5 years. Where the number of years is the same, the stock price CAGR decides the rank.
- Based on this, over 2018-23, yet another low-profile company, **Capri Global**, has emerged as the Most Consistent Wealth Creator. It has outperformed the BSE Sensex in all the last 5 years, and has the highest price CAGR of 50%.

Exhibit 3 **Top 10 Most Consistent Wealth Creators (2018-23)**

Rank	Company	No. of years of outperformance	2018-23 Price CAGR (%)	2018-23 PAT CAGR (%)	RoE (%) 2023	RoE (%) 2018	P/E (x) 2023	P/E (x) 2018
1	Capri Global	5	50	26	6	5	66	25
2	Varun Beverages	5	50	50	31	12	57	53
3	Grindwell Norton	5	30	19	19	15	59	39
4	ICICI Bank	5	26	35	16	7	18	23
5	Adani Enterprises	4	78	34	7	4	81	30
6	Tube Investments	4	63	53	33	12	37	27
7	Linde India	4	56	91	17	1	65	179
8	Adani Power	4	52	L to P	36	N.M.	7	N.M.
9	J B Chem	4	45	31	16	7	37	24
10	SRF	4	44	36	21	13	33	24

N.M. – Not Meaningful

Adani Enterprises is the Best All-round Wealth Creator for the second time in a row

- We define All-round Wealth Creators based on the summation of ranks, under each of the 3 categories – Biggest, Fastest and Consistent. Where the scores are tied, the stock price CAGR decides the All-round rank.
- Based on the above criteria, **Adani Enterprises** has emerged as the Best All-round Wealth Creator.

Exhibit 4 **Top 10 All-round Wealth Creators (2018-23)**

All-round Rank	Company	Rank: Biggest	Rank: Fastest	Rank: Consistent	Total of Ranks	2018-23 Price CAGR (%)
1	Adani Enterprises	9	2	5	16	78
2	Varun Beverages	21	7	2	30	50
3	Adani Power	23	5	8	36	52
4	Tube Investments	30	3	6	39	63
5	ICICI Bank	3	37	4	44	26
6	SRF	25	11	10	46	44
7	Linde India	49	4	7	60	56
8	Adani Energy	19	15	32	66	39
9	LTIMindtree	24	30	18	72	29
10	Reliance Industries	1	50	21	72	22

Detailed findings page 32 onwards.

Theme Study

Hockey-Stick Returns

The Power of Economic Profit

"You can shift the odds of strategy by capitalizing on your endowment, riding the right trends, and most important, making a few big moves."

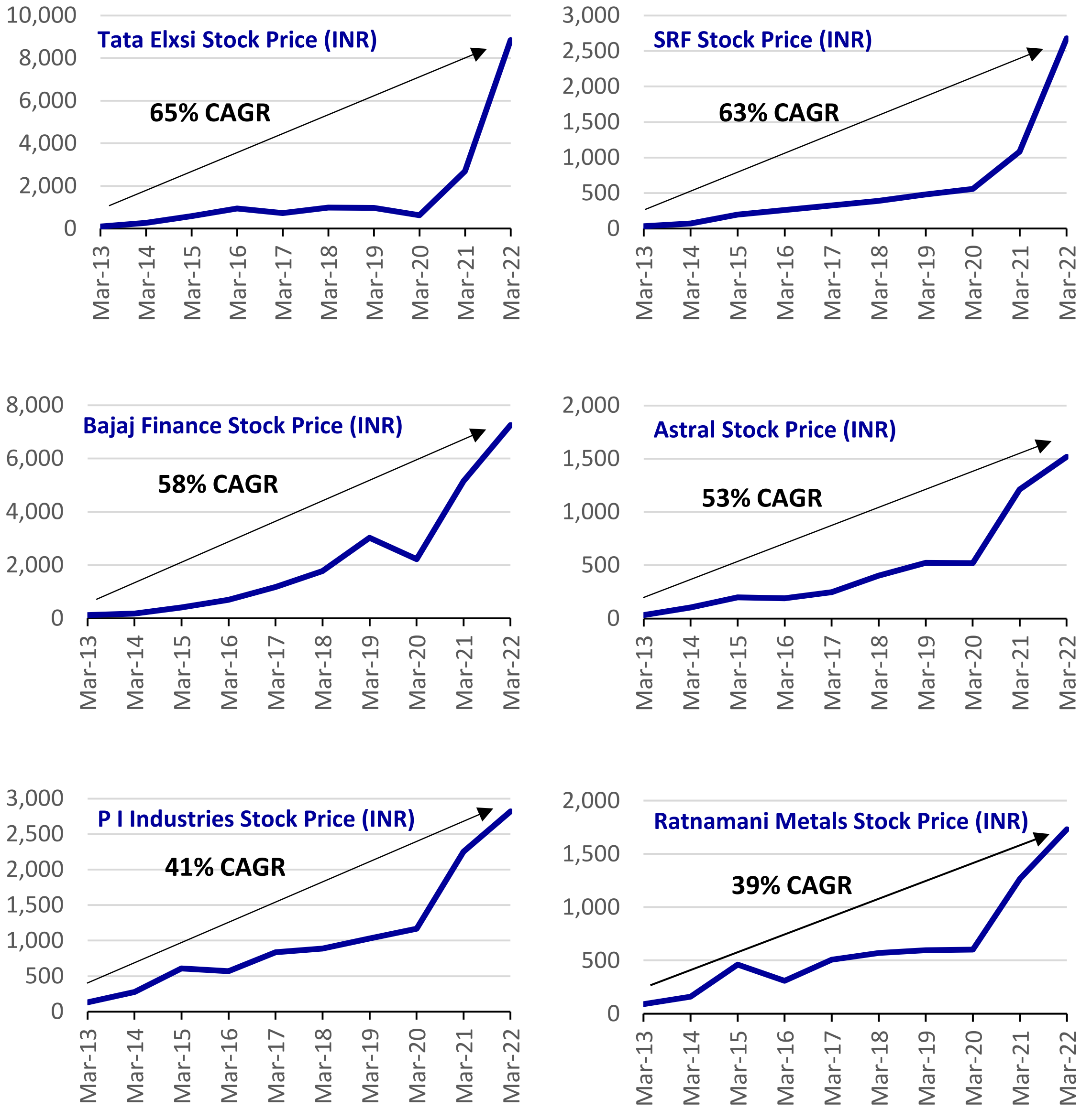
– From the book "Strategy Beyond The Hockey Stick"

1. What does Hockey-Stick Returns mean?

Sharp and sustained rise in stock price

For the purposes of this report, Hockey-Stick returns refers to a sharp and sustained rise in the price of a stock. This leads to a hockey-stick formation of the price chart, translating into handsome returns for the stockholders.

Exhibit 1 **Examples of Hockey Stick Returns (2013-22)**



1.1 What causes Hockey-Stick Returns

The most basic equation of equity investing is –

EPS (Earning Per Share) x P/E (Price-to-Earnings) = Stock Price

or

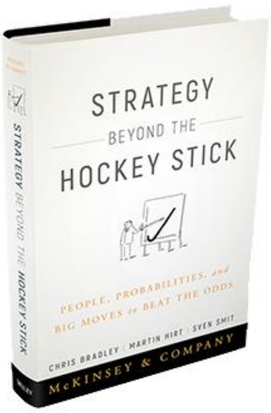
PAT (Profit After Tax) x P/E = Market capitalization

The above makes it clear that Hockey-Stick Returns is caused by Hockey-Stick earnings and/or Hockey-Stick P/E (or any other relevant valuation metric). Exhibit 2 presents the 2013-22 earnings CAGR and valuation expansion for the 6 stocks charted earlier.

Exhibit 2 **Hockey-Stick Returns are caused by Hockey-Stick Earnings and/or Hockey-Stick valuation**

	2013-22 CAGR			PAT (INR bn)		P/E (x)	
Company	**Price**	**PAT**	**P/E**	**2013**	**2022**	**2013**	**2022**
Tata Elxsi	**65%**	**37%**	**20%**	0.3	5.5	19	100
SRF	**63%**	**26%**	**29%**	2.3	18.9	4	42
Bajaj Finance	**58%**	**32%**	**23%**	5.9	70.5	10	62
Astral	**53%**	**26%**	**23%**	0.6	4.8	14	85
P I Industries	**41%**	**27%**	**12%**	1.0	8.4	18	51
Ratnamani Metals	**39%**	**10%**	**26%**	1.4	3.2	5	38

Clearly, the way to engender Hockey-Stick Returns is to invest in companies with high earnings growth at reasonable valuation. Conventionally, earnings are associated with Accounting Profit. In Section 2, we discuss the concept of Economic Profit, and why we believe it is a superior metric to Accounting Profit.



2. Identifying Hockey-Stick earnings

Look for companies which will move up the Economic Profit Curve

In this section, we draw upon concepts and insights from the book *Strategy Beyond The Hockey Stick* by a team of McKinsey authors, Chris Bradley, Martin Hirt and Sven Smit. The book is targeted primarily towards corporate managers. However, we unearthed quite a few insights for equity investors as well:

1. Economic Profit is (arguably) a superior metric to Accounting Profit
2. All companies can be mapped to an Economic Profit Power Curve
3. Companies which move up the Power Curve generate healthy returns to shareholders, and vice versa.

2.1 Economic Profit vs Accounting Profit

Be it by business managers, bankers, equity investors or who have you, Accounting Profit (AP) is the most widely used metric for various kinds of financial analysis. Sure enough, AP is a highly homogenized metric as it is based on the prevailing accounting principles common to all companies in a given geography. However, one key demerit of AP is the fact that it does not take into consideration the amount of equity (i.e. net worth) invested to generate a certain level of profit.

Consider Exhibit 3. Indian Oil's PAT is 4 times higher than that of Nestle. And yet, its Market Cap is lower than Nestle's. Such anomalies are better explained by the concept of Economic Profit.

Exhibit 3 **Accounting Profit anomaly**

INR bn	Nestle (CY22)	Indian Oil (FY23)	Indian Oil over Nestle
Accounting Profit	24	98	4 times higher profit
Net Worth	25	1,397	56 times higher equity employed …
RoE	96%	7%	… translating to significantly lower RoE
Year-end Market Cap	1,890	1,100	Lower market cap …
P/E (x)	**79**	**11**	**… due to much lower valuation**

2.1.1 Economic Profit – the concept and the math

The main feature of AP is that it incorporates all **explicit costs** to determine a company's profit and profitability. However, it excludes a key item, namely, the **implicit cost of invested equity capital**, **or simply, Cost of Equity (CoE)**.

Academically, based on CAPM (Capital Asset Pricing Model), every company may have a different CoE based on the following formula:

$$\textbf{CoE} = R_F + \text{Beta} \times (R_M - R_F)$$

where

R_F is the Risk-free rate of return

$R_M - R_F$ is the equity risk premium where R_M = Equity market rate of return

Beta is the volatility co-efficient of the company's stock returns vis-à-vis market return

(Mathematically, Beta = Covariance of the security's returns and the market's returns divided by Variance of market returns over the long-term)

For the purposes of this report, **we have considered a uniform CoE of 10%** (more or less equal to the long-period return on Indian equity markets). Thus, based on our methodology –

Economic Profit (EP) = Accounting Profit (AP) minus Equity Charge

Equity Charge = Net Worth x CoE (10% in our case)

Therefore, EP = AP – (Net Worth x 10%) *… Equation 1*

Based on the Equation 1, the 3 determinants of EP are – (1) AP, (2) Net Worth, and (3) CoE.

Now, RoE = AP ÷ Net Worth

Therefore **AP = Net Worth x RoE** *… Equation 2*

Substituting AP in Equation 1, we get –

EP = (Net Worth x RoE) – (Net Worth x 10%)

i.e. EP = Net Worth x (RoE – 10%) *… Equation 3*

Based on the Equation 3, the 2 determinants of EP are – (1) Net Worth, and (2) Spread between RoE and CoE.

We can now revisit Exhibit 3 (see Exhibit 4 below). Nestle earns EP of INR 22 bn whereas Indian Oil actually has an EL (Economic Loss) of INR 42 bn. Thus, EP captures the true profitability of a company.

Exhibit 4 **Nestle's Economic Profit vs Indian Oil's Economic Loss**

INR bn	Nestle (CY22)	Indian Oil (FY23)
Accounting Profit (1)	24	98
Net Worth (2)	25	1,397
Cost of Equity (3)	10%	10%
Equity Charge (4) = (2) x (3)	3	140
Economic Profit (5) = (1) - (4)	**22**	**-42**
RoE (6) = (1) ÷ (2)	96%	7%
Alternatively, Spread between RoE & CoE		
(7) = (6) - (3)	86%	-3%
Economic Profit (8) = (2) x (7)	**22**	**-42**

Based on the above methodology, we present below the EP of companies constituting Nifty 50.

Exhibit 5 **Economic Profit of Nifty 50 companies**

INR bn	2023					INR bn	2023				
	AP	NW	EC	EP	RoE		AP	NW	EC	EP	RoE
TCS	421	904	90	**331**	47%	IndusInd Bank	74	550	55	**19**	14%
Coal India	281	572	57	**224**	49%	Bajaj Finserv	64	464	46	**18**	14%
SBI	557	3,589	359	**198**	16%	Adani Ports	63	457	46	**17**	14%
HDFC Bank	459	2,894	289	**170**	16%	Britannia Inds	20	35	4	**17**	58%
Infosys	240	754	75	**164**	32%	Eicher Motors	29	150	15	**14**	19%
O N G C	408	2,806	281	**127**	15%	Bharti Airtel	88	776	78	**11**	11%
ICICI Bank	340	2,145	214	**125**	16%	Hero Motocorp	27	167	17	**11**	16%
ITC	191	692	69	**122**	28%	Larsen & Toubro	100	893	89	**10**	11%
HCL Technologies	146	654	65	**81**	22%	UPL	37	298	30	**7**	12%
Power Grid Corpn	156	830	83	**73**	19%	Hindalco Inds	101	948	95	**6**	11%
Bajaj Finance	115	544	54	**61**	21%	Maruti Suzuki	67	618	62	**6**	11%
Hind. Unilever	102	503	50	**51**	20%	Divi's Labs	18	128	13	**5**	14%
Axis Bank	181	1,298	130	**51**	14%	Cipla	28	234	23	**5**	12%
Kotak Mahindra	149	1,123	112	**37**	13%	SBI Life Insurance	17	130	13	**4**	13%
M & M	93	564	56	**36**	16%	Apollo Hospitals	8	62	6	**2**	13%
Wipro	114	777	78	**36**	15%	HDFC Life	14	130	13	**1**	11%
Bajaj Auto	60	294	29	**30**	20%	UltraTech Cement	50	543	54	**-4**	9%
Sun Pharma	86	560	56	**30**	15%	Tata Consumer	11	163	16	**-6**	7%
LTIMindtree	44	166	17	**27**	27%	Adani Enterprises	27	331	33	**-6**	8%
Asian Paints	41	160	16	**25**	26%	Grasim Inds	68	788	79	**-10**	9%
NTPC	170	1,470	147	**23**	12%	Tata Steel	86	1,031	103	**-17**	8%
Dr Reddy's Labs	46	233	23	**23**	20%	Tata Motors	25	453	45	**-20**	6%
Nestle India	24	25	2	**21**	97%	B P C L	33	535	54	**-20**	6%
Titan Company	33	119	12	**21**	27%	JSW Steel	38	657	66	**-28**	6%
Tech Mahindra	48	279	28	**20**	17%	Reliance Industries	668	7,159	716	**-48**	9%

NW – Net Worth; **EC** – Equity Charge @ 10% of NW

2.1.2 Economic Profit is a superior metric compared to Accounting Profit

Many equity investors consider AP and RoE before making their investment decision. However, juxtaposing the two can be somewhat fuzzy. Unlike this, EP offers a composite metric, capturing the interaction of AP and RoE. To assess the efficacy of EP vis-à-vis AP, for every year beginning 2014, we observed the return profile of the top 500 companies, classified into equal-weighted portfolios as tabled in Exhibit 6.

Exhibit 6 **Economic Profit portfolios have significantly superior performance compared to Economic Loss portfolios**

Price YoY ending	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	Avg	CAGR	Alpha yrs	
													+ve	-ve
Nifty 500 Return	**18%**	**34%**	**-8%**	**24%**	**11%**	**8%**	**-28%**	**76%**	**21%**	**-2%**	**15%**	**13%**		
RETURN														
Top 500 by Mkt Cap	19%	58%	-5%	36%	13%	-8%	-33%	102%	28%	-2%	**21%**	**16%**		
All profit-making cos.	21%	62%	-5%	37%	15%	-7%	-32%	101%	26%	-1%	**22%**	**17%**		
With EP	**25%**	**72%**	**0%**	**37%**	**16%**	**-5%**	**-28%**	**98%**	**26%**	**-2%**	**24%**	**19%**		
With EL	14%	41%	-14%	38%	14%	-12%	-44%	109%	24%	1%	**17%**	**11%**		
All loss making	-1%	32%	-6%	28%	-4%	-23%	-44%	112%	43%	-8%	**13%**	**6%**		
ALPHA OVER NIFTY 500														
Top 500 by Mkt Cap	1%	24%	3%	12%	2%	-17%	-5%	26%	7%	1%	**5%**	**3%**	**8**	**2**
All profit-making	4%	28%	3%	13%	4%	-15%	-4%	25%	5%	1%	**6%**	**4%**	**8**	**2**
With EP	**7%**	**39%**	**8%**	**13%**	**4%**	**-13%**	**-1%**	**22%**	**5%**	**0%**	**8%**	**6%**	**8**	**2**
With EL	-4%	7%	-6%	14%	2%	-20%	-16%	33%	4%	3%	**2%**	**-2%**	**6**	**4**
All loss making	-19%	-1%	1%	4%	-16%	-31%	-17%	36%	22%	-6%	**-3%**	**-6%**	**4**	**6**
NO. OF STOCKS														
Top 500 by Mkt Cap	500	500	500	500	500	500	500	500	500	500	**500**			
All profit-making	438	435	446	436	448	453	456	454	451	466	**448**			
With EP	**296**	**286**	**290**	**309**	**311**	**330**	**351**	**322**	**324**	**341**	**316**			
With EL	142	149	156	127	137	123	105	132	127	125	**132**			
All loss making	62	65	54	64	52	47	44	46	49	34	**52**			

Note: EP – Economic Profit; EL – Economic Loss; For EP and EL companies, negative Alpha numbers are highlighted

Two key takeaways:

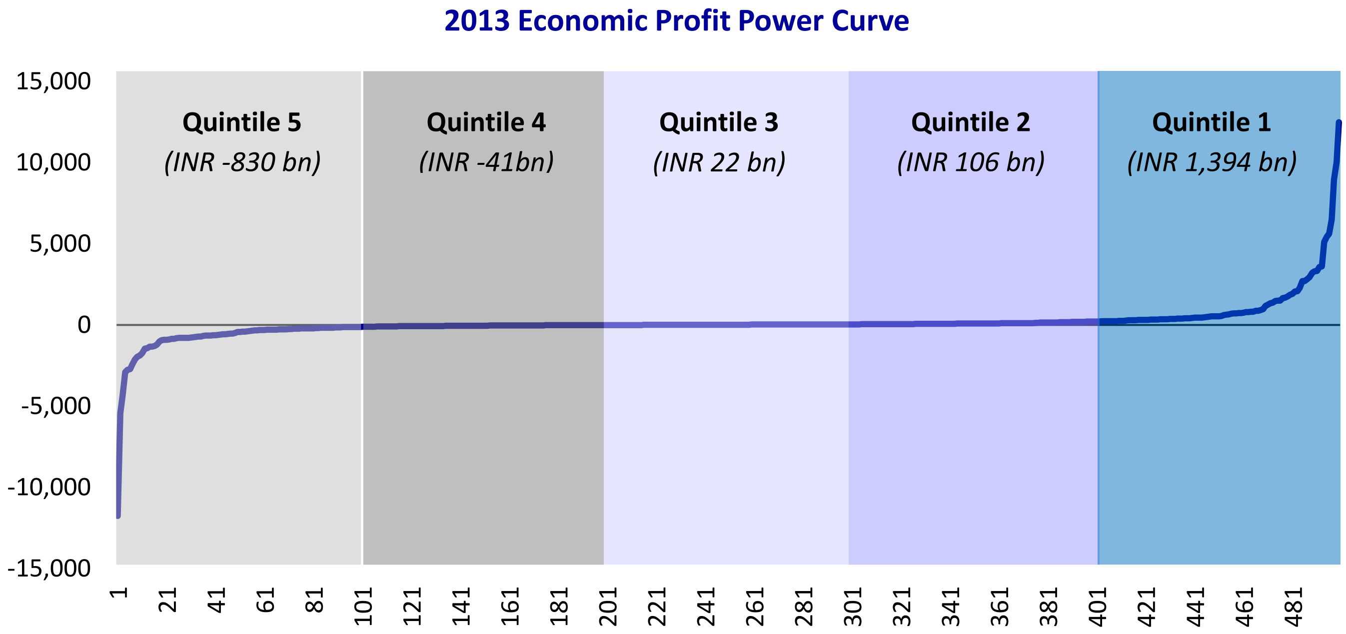
1. On average, the EP portfolio delivered 8% Alpha with a probability of 80% (i.e. in 8 out of 10 observations). In contrast, the Economic Loss (EL) portfolio delivered only 2% Alpha that too with a lower probability of 60% (i.e. in 6 out of 10 observations).
2. On a CAGR basis, the EP portfolio delivered Alpha of 6% whereas the EL portfolio delivered negative Alpha of 2%.

Thus, not only does EP reflect true profitability of a company, a portfolio of companies with EP has a high probability of outperforming the market. Having established the superiority of EP over AP, we proceed to analyze it further.

2.2 All companies can be mapped to an Economic Profit Power Curve

The book referred to earlier maps leading global companies to what the authors call the Economic Profit Power Curve. We too attempted the exercise on India's top 500 companies by 2013 market cap. We find that the shape of the Power Curve is exactly the same as in the book (Exhibit 7).

Exhibit 7 **Economic Profit Power Curve for India Inc in 2013**



Figures in brackets are the aggregate Economic Profit in the Quintile

The Power Curve can be explained as follows –

- We listed the top 500 market-cap companies in 2013 in ascending order of their EP.
- We divided the companies into 5 EP Quintiles of 100 each.
- The Power Curve captures the above.
- Quintiles 5 and 4 are all companies with EL
- Quintiles 3, 2 and 1 are all companies with EP.
- Bulk of the losses and profits are at the extreme Quintiles.

2.3 Companies which move up the Power Curve generate healthy returns

It is obvious that companies move up the Power Curve only when they generate high incremental EP. Thus, such companies typically generate significant shareholder return (barring the rare cases of exceptionally high opening valuation). For instance, consider Exhibit 8 which captures the inter-quintile moves of the top 500 companies between 2013 and 2023.

Exhibit 8 **Economic Profit Quintile Moves: 2013 to 2023**

Nifty 500 return during 2013-23: 13% CAGR

Return CAGR

	2023 Q					
2013 Q	**1**	**2**	**3**	**4**	**5**	**Total**
1	16%	11%	11%	8%	8%	**14%**
2	**25%**	21%	16%	14%	5%	**19%**
3	**43%**	**26%**	17%	15%	12%	**22%**
4	15%	21%	9%	16%	7%	**14%**
5	17%	14%	16%	6%	3%	**9%**
Total	**21%**	**21%**	**15%**	**13%**	**6%**	**16%**

Number of companies

	2023 Q					
2013 Q	**1**	**2**	**3**	**4**	**5**	**Total**
1	60	13	2	3	22	**100**
2	**21**	27	25	20	7	**100**
3	**5**	**25**	37	23	10	**100**
4	3	21	30	29	17	**100**
5	11	14	6	25	44	**100**
Total	**100**	**100**	**100**	**100**	**100**	**500**

Q – Economic Profit Quintile

Key observations:

- Significantly market-beating performance happens when companies move up the EP Quintiles e.g. companies which moved from Quintile 3 in 2013 to Quintile 1 in 2013 delivered the highest return (43%). However, the number of stocks is only 5.
- Likewise, 25 companies moving from Quintile 3 to Quintile 2 delivered 26% return CAGR and 21 companies which moved from Quintile 2 to Quintile 1 delivered 25% return.
- Performance in Quintiles 4 and 5 is somewhat erratic. As stated earlier, these Quintiles comprise EL companies. So, in such cases, moving up the Power Curve implies lowering EL or turning around into EP. There's no clear pattern here.

Exhibit 9 **Economic Profit Quintile Movers: 2013 to 2023**

Quintile 3 to 1 (5 companies)

	2013-23 CAGR		
Company	**Price**	**EP**	**PAT**
SRF	**53%**	41%	25%
Tata Elxsi	**51%**	46%	37%
TVS Motor	**42%**	36%	26%
G N F C	**21%**	81%	18%
R C F	**10%**	28%	13%

Quintile 3 to 2 (25 companies)

	2013-23 CAGR		
Company	**Price**	**EP**	**PAT**
Astral	**45%**	18%	22%
Sundram Fasteners	**38%**	32%	19%
Timken India	**35%**	35%	25%
KRBL	**32%**	19%	19%
Honeywell Auto	**29%**	23%	18%
Supreme Petrochem	**29%**	22%	20%
Elgi Equipments	**28%**	26%	17%
TVS Holdings	**27%**	28%	18%
V I P Inds	**25%**	34%	19%
Praj Industries	**25%**	41%	14%
Century Plyboard	**24%**	22%	22%
Esab India	**23%**	23%	14%
P & G Health	**23%**	18%	11%
Natco Pharma	**21%**	24%	24%
Allcargo Logistics	**20%**	57%	14%
Lakshmi Machine	**18%**	16%	11%
Chambal Fertilisers	**18%**	25%	17%
Apollo Hospitals	**18%**	24%	11%
Dhanuka Agritech	**18%**	11%	13%
BASF India	**15%**	L to P	13%
Siemens	**15%**	27%	13%
Pfizer	**13%**	23%	11%
Gillette India	**9%**	27%	15%
Akzo Nobel	**8%**	45%	11%
Styrenix Perform.	**0%**	18%	11%

Quintile 2 to 1 (21 companies)

	2013-23 CAGR		
Company	**Price**	**EP**	**PAT**
P I Industries	**37%**	28%	29%
Solar Industries	**34%**	22%	20%
Persistent Systems	**33%**	20%	17%
IIFL Finance	**32%**	23%	19%
Abbott India	**31%**	24%	21%
Chola. Inv. & Fin.	**30%**	27%	24%
Page Industries	**28%**	17%	18%
Eicher Motors	**26%**	27%	25%
AIA Engineering	**25%**	22%	18%
Britannia Inds	**23%**	25%	24%
Schaeffler India	**23%**	20%	18%
Indraprastha Gas	**23%**	15%	16%
P & G Hygiene	**18%**	16%	13%
Coromandel Inter.	**17%**	19%	17%
Chola Financial	**16%**	16%	16%
Marico	**16%**	18%	13%
Rain Industries	**16%**	11%	12%
Redington	**15%**	16%	16%
Oberoi Realty	**13%**	22%	14%
NLC India	**2%**	32%	5%
Bank of Maha.	**-7%**	23%	13%

We carried out the above inter-quintile exercise for 5 more 10-year periods – 2008-18, 2009-19, 2010-20, 2011-21 and 2012-22. Exhibit 10 is the average of all the above 6 observation periods.

Exhibit 10 **Economic Profit Quintile Moves: Average of six 10-year observation periods between 2008 and 2023**

Nifty 500 average return: 11% CAGR

Return CAGR

	End Q					
Start Q	**1**	**2**	**3**	**4**	**5**	**Total**
1	**16%**	**11%**	6%	8%	4%	**12%**
2	**26%**	**22%**	10%	10%	5%	**19%**
3	**33%**	**25%**	12%	8%	6%	**19%**
4	**34%**	**21%**	9%	8%	7%	**15%**
5	**29%**	**14%**	10%	7%	1%	**14%**
Total	**24%**	**21%**	**10%**	**8%**	**4%**	**16%**

Number of companies

	End Q					
Start Q	**1**	**2**	**3**	**4**	**5**	**Total**
1	53	9	3	7	29	**100**
2	24	28	17	18	13	**100**
3	7	31	30	22	9	**100**
4	5	19	38	26	12	**100**
5	11	13	12	28	36	**100**
Total	**100**	**100**	**100**	**100**	**100**	**500**

Q – Economic Profit Quintile

Key observations:

- Quintile moves from 3 to 2, from 3 to 1 and from 2 to 1 continue to deliver market-beating returns.
- Upmoves from Quintile 4 and 5 also generate handsome returns, albeit they tend to be speculative in nature as they involve mainly turnarounds.
- One significant observation is that on average, almost all market-beating returns happen when companies end up in Quintiles 1 and 2, no matter what the starting Quintile is.
- **The conclusive and actionable observation is that it pays to start from Quintiles 2 and 3.** Any upmove will obviously lead to high returns. Equally important, regardless of the final outcome, on average, investors should expect 19% return (highlighted under Total column).

Having understood the power of EP, we can now delve into factors which drive it.

3. Drivers of Economic Profit

TEM – Trends, Endowment, Moves

In the book, *Strategy Beyond The Hockey Stick*, the authors list 10 key variables which drive EP. They classify the same under 3 heads – Endowment, Trend and Moves – as under.

Exhibit 11 **10 key variables driving Economic Profit**

Endowment	Trend	Moves
• Company size	• Industry trend	• Programmatic M&A
• Debt level	• Geographic trend	• Dynamic reallocation of resources
• Past investment in R&D		• Strong capital expenditure
		• Strength of productivity program
		• Improvement in differentiation

We tweak the above slightly and discuss them as TEM –

- **Trends** – factors external to a company, mostly stemming from the sector; and
- **Endowment & Moves** – factors internal to a company.

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