

What Metrics Matter?

A Public Equity Investor's Perspective

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About Me

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<https://github.com/chris-lundberg/measure-what-matters>

Public vs. Private Markets

Similarities	Differences
fiduciary duty	liquidity
impact of macroeconomic conditions	data availability
impact of capital market conditions	reporting requirements
impact of investor risk appetite	investor universe
same competitive environment	investor motivations and constraints
importance of expectations	relationship between management and investors

Investment Decision Making

Three Paradigms

- Qualitative
- Quantitative
- ESG

Qualitative: Competition and Execution

Porter's Five Forces

Dimension	High	Low
threat of new entrants	food truck	regulated utility
threat of substitutes	cable TV	cloud computing
bargaining power of customers	AAPL suppliers	Lululemon
bargaining power of suppliers	oilfield well integrity services	Amazon
competitive rivalry	ride sharing	oncology drug development

A Culture of Success

Characteristic	Comments
relevant metrics	is management focused on a small, concrete list of objectives?
customer focus	does management understand the customer deeply?
vision	does the CEO have high expectations and a compelling vision?
agility	is the company willing and able to change direction quickly if necessary?
attitude	does the company value curiosity and experimentation?

*borrowed heavily from *The Lean Startup* and *Measure What Matters*

Quantitative: Return Predictive Signals

Common Metrics: Valuation

Metric	Comments
trailing P/E	popular in the financial press
forward P/E	useful for assessing duration expectations
price to sales	useful for high growth companies
EV/EBITDA	accounts for capital structure
free cash flow yield	important long term, but places emphasis on past performance
dividend yield	useful for capital intensive companies with low growth expectations

Common Metrics: Quality

Metric	Comments
ROIC	what are you doing with what you have?
earnings information ratio	how consistent are your profits?
incremental ROIC	what can you do with an additional unit of investment?
debt to equity	is debt service an issue or is WACC too high?
operating leverage	how does top line growth impact margins?
cash conversion cycle	do you have leverage over your suppliers and customers?

Common Metrics: Timing

Metric	Comments
12 month trailing return	commonly used momentum factor
earnings revisions	good indicator of changing expectations
margin expansion	operational momentum indicator
estimates dispersion	divergent expectations can offer opportunities
growth inflection	this is great, but the new growth rate must persist
relative valuation	does the asset look cheap vs. history on a relative basis?

Common Metrics: Capital Deployment

Metric	Comments
dividend yield	is the company returning the capital it can't invest above it's WACC?
share buybacks	is the company buying back shares? if so, is the valuation low or high?
management compensation	is there a large option pool for management?
capex vs. depreciation	is the company reinvesting adequately to sustain current revenues?
acquisition terms	cash or stock? what are the synergy expectations?
reinvestment rate	what proportion of the company's profits are being reinvested?

ESG: Environmental, Social, Governance

Principles of Responsible Investing

Category	Example
Governance	Is the CEO's compensation in line with industry peers?
Social	Is the company aware of how its products and operations affect the communities in which it operates?
Governance	Are the majority of board members independent?
Environmental	Does the company have a reputation of careless or short sighted operating practices?
Governance	How are the voting rights distributed? Does the CEO have voting control?
Social	Does the company make an effort to develop a diverse workforce?

References

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The New Tycoons - Jason Kelly

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United Nations Principles of Responsible Investing