Fortuna Advisors LLC

Learn About RCE

Gross Cash Earnings

EBITDA, after-tax, with R&D treated as an investment

Residual Cash Earnings (RCE)

Capital Charge

Gross Operating Assets x Required Return %

What is Residual Cash Earnings (RCE)?

RCE is our take on economic profit. It starts with Gross Cash Earnings (GCE), which is tax-adjusted EBITDA plus P&L investment (R&D expense, Operating Leases, etc.). We then deduct a capital charge on Gross Operating Assets as a representation of the required return investors expect on that capital. The difference is RCE – the value created beyond the firm's cost of capital.

What are the benefits of RCE?

As a comprehensive value creation signal, RCE tracks Total Shareholder Return better than any conventional measure. RCE is also a more reliable period performance measure, since we remove distortions that can be caused by depreciation and GAAP accounting treatment. While EVA and other economic profit measures can unwittingly stifle long-term investment, these adjustments result in a healthier balance of short- and long-term performance outlook, fueling sustained growth and improvement.

What are the Five Tools of Value Creation?

The Five Tools of Value Creation is a short list of metrics that, in aggregate, explain value creation. It is helpful for companies to compare their performance across the Five Tools to the performance of their peers to know where they can improve and whether their forecasts are reasonable. Long-term improvement in these metrics reliably drives value creation. The table below explains each of the Five Tools:

		Measure	Description	Calculation
Current Performance	Growth	**Revenue Growth**	Reflects a company's ability to grow, as measured by the percentage change in sales over a specified period.	Revenue Compound Annual Growth Rate (CAGR)
Current Performance	Profitability & Efficiency	**Gross Cash Earnings Margin**	An indicator of P&L efficiency and pricing power. Gross Cash Earnings (GCE) is calculated as after-tax EBITDA with R&D added back. To arrive at a margin estimate, we divide this value by revenue.	Gross Cash Earnings/ Revenue
Current Performance	Profitability & Efficiency	**Asset Intensity**	Reflects capital productivity. The lower the Asset Intensity, the more capital-efficient a company is. Gross Operating Assets (GOA) refers to a company's undepreciated operating asset base.	Gross Operating Assets/ Revenue
Future Performance	Reinvestment	**Reinvestment Rate**	Measures the level of reinvestment relative to the cash generated by a business Includes CapEx, R&D, Net Cash Acquisitions, Δ Net Working Capital, Rent, and Δ Operating Leases.	Reinvestment/ Gross Cash Earnings
Future Performance	Reinvestment	**Reinvestment Effectiveness**	Indicates efficiency of reinvestment by measuring the revenue generated per dollar of reinvestment.	Change in Revenue/ Reinvestment

*Note that *Annualized TSR* and *Δ RCE / Beg. GOA* are already normalized for multi period measurement.