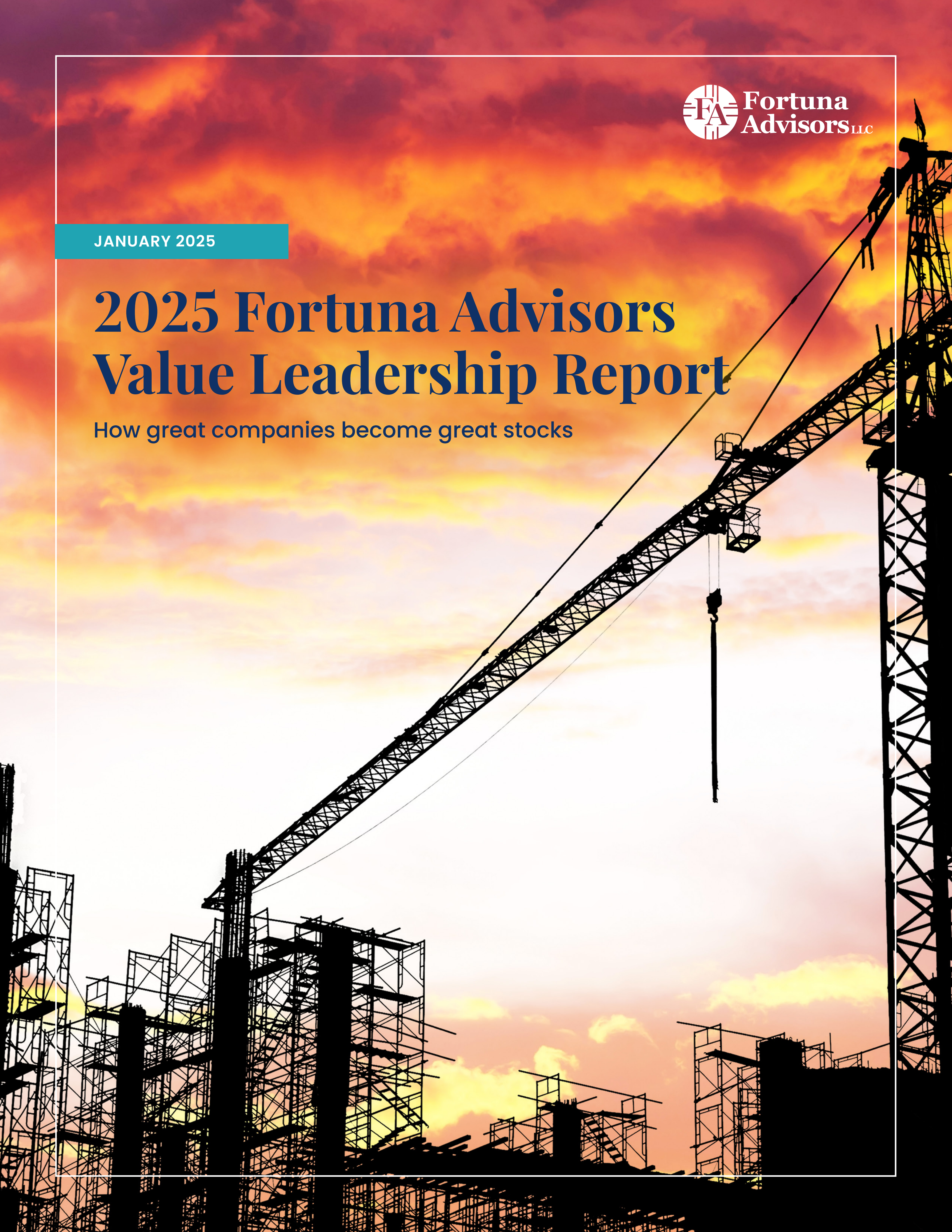

JANUARY 2025

2025 Fortuna Advisors Value Leadership Report

How great companies become great stocks

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Thank you to Chris Moore and Michael Chew of Fortuna Advisors for their contributions to this report.

ABOUT FORTUNA ADVISORS

Fortuna Advisors collaborates with leaders to transform decision-making throughout their business to achieve exceptional results. Our management playbook delivers measurable outcomes through:

1. **Better Insights**: See the truth about where value is created or destroyed.
2. **Better Decisions**: Drive faster, better and enduring results.
3. **Better Behaviors**: Align incentives and processes to drive execution.

We serve as a catalyst to create a culture of ownership, where everyone from the board to management and employees embraces a long-term investor perspective to unlock the organization's full value creation potential.

CONTACT US

Email: *info@fortuna-advisors.com*

Tel: 631-478-5670

www.fortuna-advisors.com

Charting a Path to Value Creation

2024 was a year of tremendous value creation, strong earnings growth, and high returns on capital for US stocks. Combined with the tailwinds of AI enthusiasm and a declining federal funds rate, this made for another blockbuster year for equity investors.

Indeed, in 2024, the S&P 500 index notched 57[1] successive all-time highs. The Nasdaq and Dow Jones Industrial indices, not to mention more speculative assets like bitcoin, also followed suit with their own records. Needless to say, it was a good time to be a bull.

Our annual Fortuna Advisors Value Leadership Report analyzes how some of the world's best public companies produced outsized shareholder returns not just in 2024, but over the last five years. We evaluate Total Shareholder Return (TSR)* as an indicator of value leadership in the S&P 900, excluding financials and real estate,[2] to analyze how key financial measures related to TSR performance over the period.

The findings explain capital market trends to help leaders deliver better shareholder returns. These insights are also vital for managements and boards that are charged with selecting performance measures to gauge and motivate the success of their leadership teams. Additionally, we offer industry insights that examine sector trends and performance beyond the index level and offer more tailored recommendations.

Lastly, we highlight some of the common obstacles managements should address and overcome, along with best practices, to improve shareholder return performance.[3]

VALUE CREATION HIGHLIGHTS

1 PROFITABILITY AND EFFICIENCY OUTPERFORM GROWTH
Despite spectacular gains in speculative assets, data shows investors favored strong economic profit, returns on capital, and earnings over high revenue growth. This shift away from a pure growth focus is a multi-year trend that first emerged in 2022 as inflation intensified, suggesting higher interest rates may have affected investor behavior. *Read more.*

2 ECONOMIC PROFIT DRIVES SHAREHOLDER RETURNS
For the fifth straight year, through multiple bear and bull cycles, Fortuna's unique cash-based measure of economic profit remained the top proxy for TSR outperformance. Market trends fluctuate, so be sure your performance measures reliably relate to shareholder returns. *Read more.*

3 A SURGE OF CAPITAL INVESTMENT
Capital Goods companies' dominance reflected high business and consumer confidence as US companies aggressively built homes, factories, and data centers, among other capital-intensive investments over the last five years. *Read more.*

4 SOFTWARE SUPREMACY
In 2024 the AI enthusiasm continued—but as clearer applications for the technology arose, Software and Services replaced Semiconductors and Semiconductor Equipment as the main benefactor of this trend. *Read more.*

5 PAST PERFORMANCE IS NO GUARANTEE
Value leaders in the prior five years were as likely to be top or bottom quartile in the recent period. Winners must constantly reinvent themselves, and underperformers should always strive to turn their fortunes around. *Read more.*

***Total Shareholder Return (TSR)** combines share price appreciation and dividend yield to reflect shareholder value creation.

The Size of the Prize

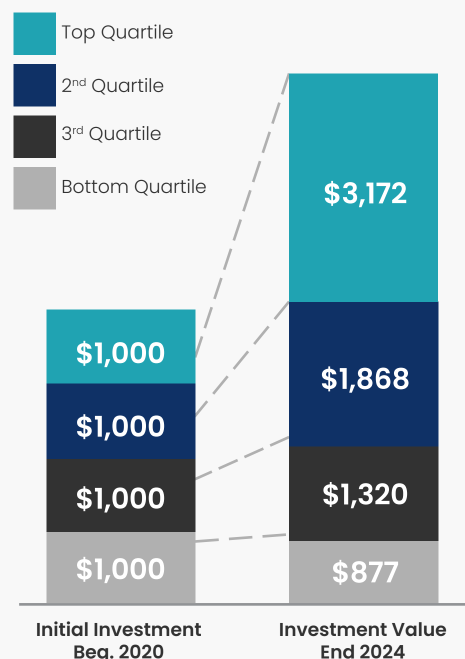
Top-quartile TSR performance in the S&P 900[4] over the five years ending in 2024 meant more than tripling your share price. The median top-quartile company delivered TSR at an annualized rate of 26.0% (versus the sample median of 9.4%), for a cumulative return of 217.2%. At this pace, $1,000 would have been worth $3,172 after five years, as shown in *Figure 1*. To illustrate the gap between top- and bottom-quartile performance, consider that the median of the top group created over 17 times as much value, per dollar invested, as the median of the bottom quartile destroyed.

As we all know, the past five years have been characterized by an abnormally high concentration of returns at the top of indexes. Indeed, the 166 top-quartile companies in our sample were responsible for 88.1% of the increase in market capitalization, or $19.2 trillion of $21.8 trillion, as shown in *Figure 2*. Taking this as step further, the "Elite Eight"—Alphabet, Amazon, Apple, Broadcom, Meta, Microsoft, Nvidia, and Tesla—delivered $13.4 trillion, or 61.5% of the total market value creation.

The yawning gap between winners and losers, not to mention the narrow leadership of the Elite Eight, highlights, at an individual company level, the importance of strategically focusing resources on your best projects, segments, geographies, and product lines—similar to investors concentrating capital in their top-rated stocks. Leaders of multi-business companies should be sure to focus on their top performers, as each dollar reinvested in these typically delivers a better outcome versus trying to turn around poor performers.

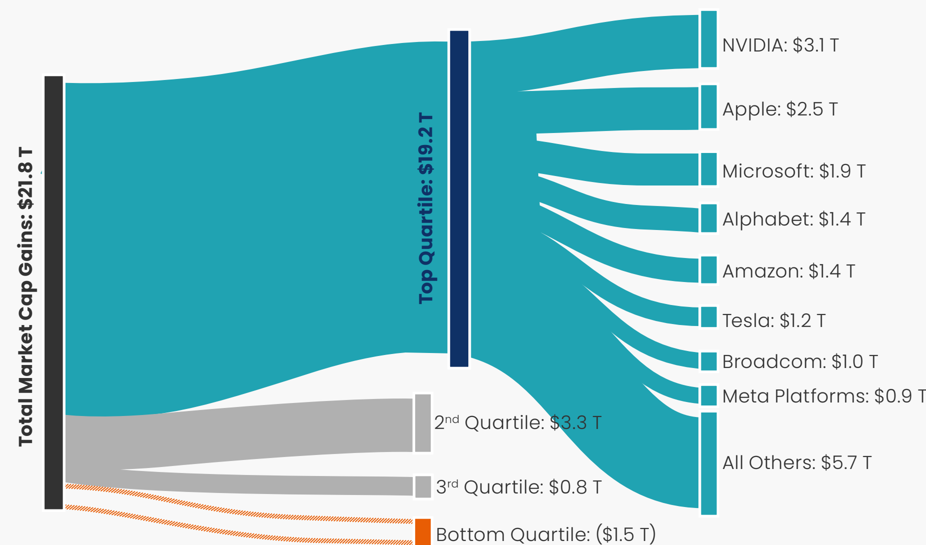
Making the top quartile isn't easy, by definition. But the value at stake is immense and the rewards well worth the effort. Developing a fact-based plan and implementing *value management* processes that foster sustained shareholder returns are key tools that can result in a strong competitive advantage and moat versus peers, which is key to attracting long-term investors. In some cases, organizational efforts to improve corporate governance practices may be your best bet. In some of the sections that follow, we'll discuss a few best practices for setting positive changes in motion.

FIGURE 1
Five-Year Value of $1,000 Invested in S&P 900* Quartiles (Median)



Excludes real estate and financial companies and companies that were not public for the full five-year period.

FIGURE 2
S&P 900* Market Capitalization Added



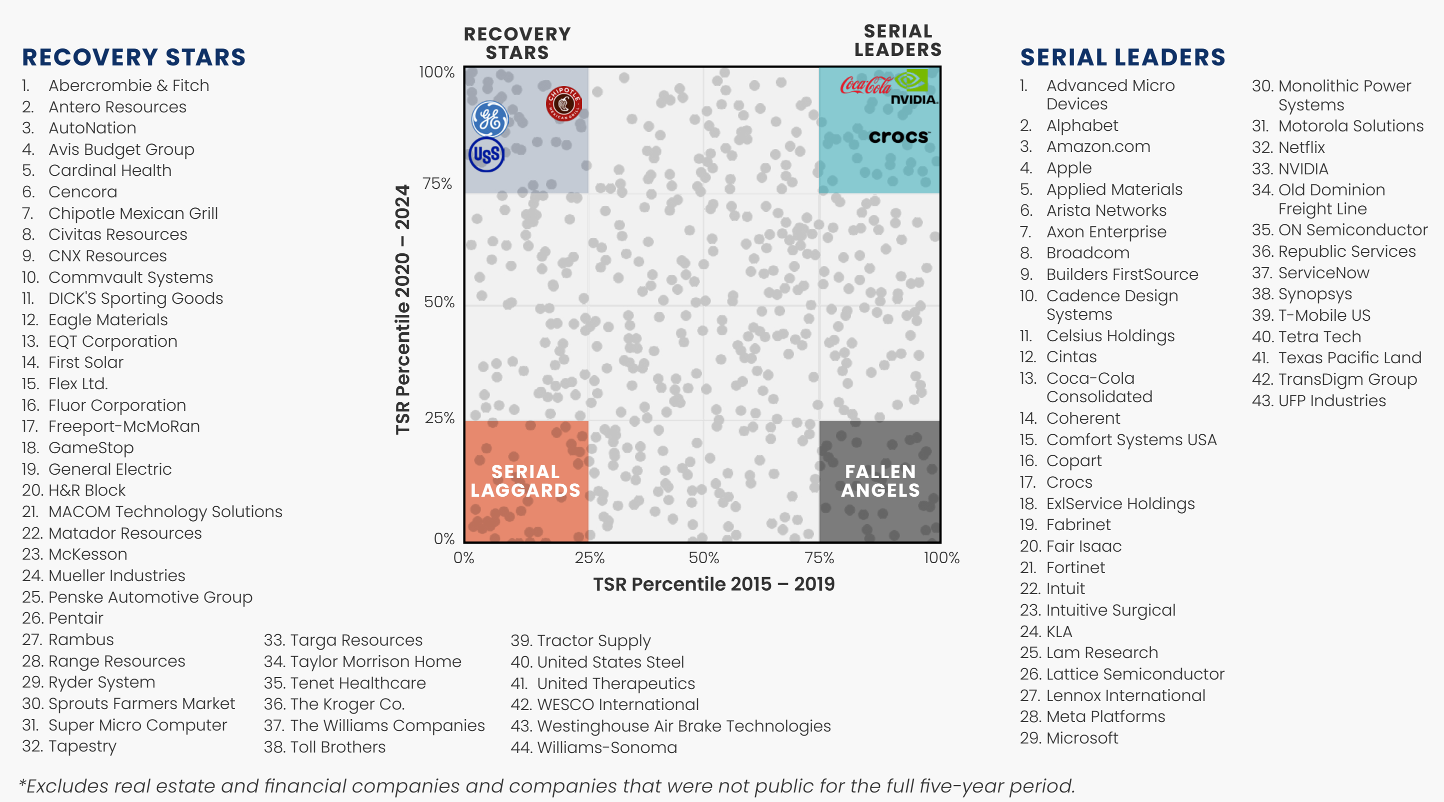
Excludes real estate and financial companies and companies that were not public for the full five-year period.

The scatterplot in *Figure 3* shows company TSR percentile rankings over successive five-year periods, with each dot representing a company in the sample. For instance, General Electric Company was in just the 3rd percentile from 2015 to 2019 (horizontal axis), but jumped to the 88th percentile from 2020 through 2024—and is thus shown in the top-left quadrant of *Figure 3*.

The relatively even distribution of datapoints across the chart suggests that past performance is no guarantee of future performance—virtually any company is capable of reaching the top quartile over the next five years. The data also highlights the difficulty of sustaining superior returns over time. Some companies and industries shift due to business and economic cycles. But there is also a broader influence of market disruption where companies meaningfully gain, or lose, competitive advantage, which can profoundly influence both performance and valuation multiples, and in turn, TSR. Unfortunately, we've observed that far too many companies that become consumed with the quarterly earnings cycle underinvest in innovation and brand building, which often drive such market disruption.

FIGURE 3

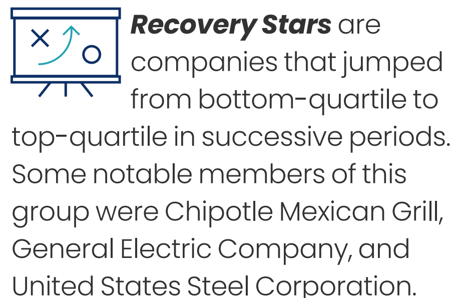
TSR Percentile Rank in Successive Five-Year Periods (S&P 900*)



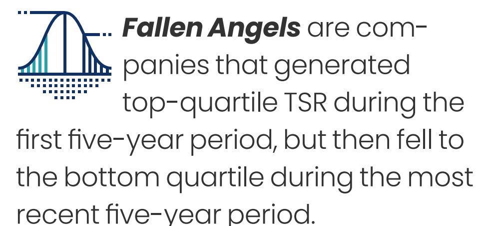
Excludes real estate and financial companies and companies that were not public for the full five-year period.

To add some color to the distribution of companies in *Figure 3*, we developed four TSR "archetypes" for the companies that start and end in either a top- or bottom-quartile position over the two successive five-year periods:

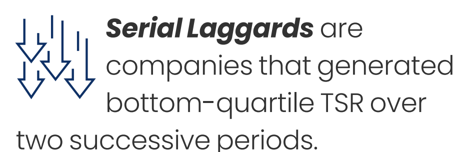
Serial leaders are companies that were top-quartile for both periods. While many industries are represented in this group, tech was the largest constituent. Serial leaders this year included Coca Cola Consolidated, Crocs, and NVIDIA Corporation. Serial leaders focus on improving *constantly* and are never satisfied with the status quo.



Recovery Stars are companies that jumped from bottom-quartile to top-quartile in successive periods. Some notable members of this group were Chipotle Mexican Grill, General Electric Company, and United States Steel Corporation.



Fallen Angels are companies that generated top-quartile TSR during the first five-year period, but then fell to the bottom quartile during the most recent five-year period.



Serial Laggards are companies that generated bottom-quartile TSR over two successive periods.

What stands out in terms of the financial performance of our serial leaders, and how do they consistently outperform their peers and the market? Our data shows a few metrics help explain their success. In *Figure 4*, we looked at the measures that had the highest significance in predicting serial leaders, which include change in revenue, EBITDA, EBITDA margin, return on invested capital (ROIC), and, finally, our cash-based measure of economic profit we call Residual Cash Earnings (RCE).

While revenue and EBITDA growth both show decent correlation to serial leadership, it's RCE growth that demonstrates the strongest linkage, with over 75% of serial leaders above the 80th percentile in the metric and 86% in top quartile of RCE improvement. RCE's utility in predicting value leadership is a function of its ability to capture multiple dimensions of performance. As a modern measure of economic profit (EP), RCE captures growth, profitability, and capital productivity. As such, it is essentially a measure of value creation that improves on the success of generic EP measures like Economic Value Added (EVA). For details on the calculation, click *here.*

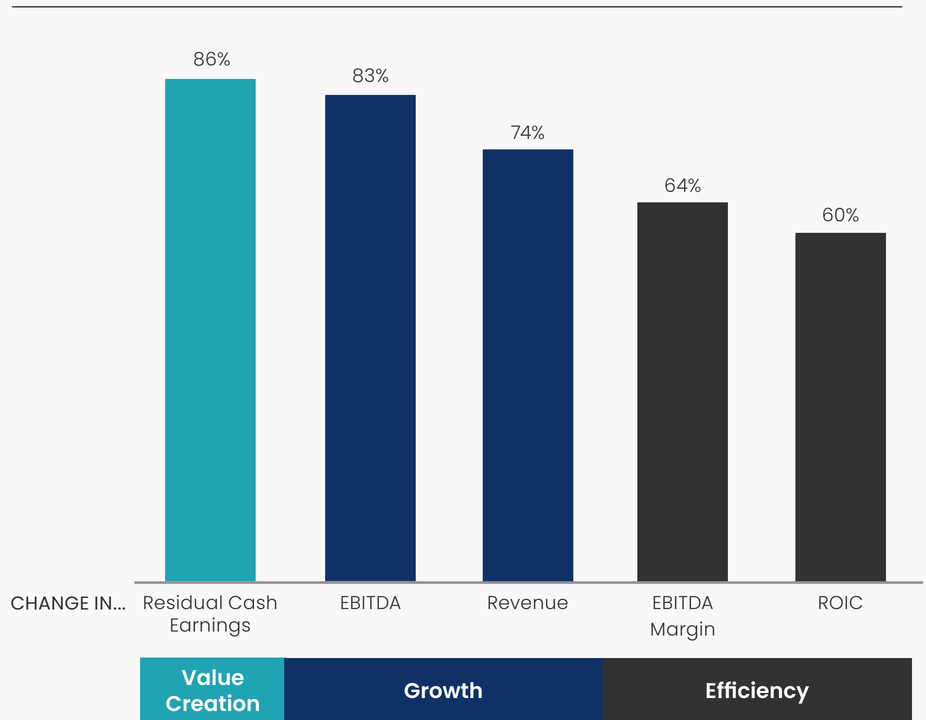
Interestingly, the data also shows that, in our group of serial leaders, revenue and earnings growth measures starkly outperformed "efficiency" measures liked EBITDA margin and ROIC over the last ten years. Bottom-quartile performers in earnings, revenue, and RCE growth yielded zero Serial Leaders underscoring the importance of profitable growth. Conversely, bottom-quartile performers in each of the efficiency measures we looked at yielded at least five serial leaders.

The worst performer among these metrics was change in ROIC. This makes sense to us, since we believe that any investment that outperforms a company's cost of capital is worthwhile—but let's look at an example to make this point. One of our serial leaders was 97th-percentile in ROIC in 2014. Over the next ten years their ROIC eroded by almost 48%; meanwhile they were top-decile in every earnings growth measure and top-quartile in revenue growth. The company in question is Microsoft, and their cumulative TSR over the last ten years is almost 1,000%!

Of course, you may have noticed from our highlights that change in ROIC was one of the top drivers of shareholder returns over the last five years, given the more recent climate of inflation and higher interest rates. But it is scenarios like Microsoft's that demonstrate how incomplete metrics like ROIC can lead management teams astray, especially over longer periods as sources of efficiency improvement become scarcer. Had the software company focused on ROIC over the past decade, its investors would have missed out on massive gains.

The ability to sustain value creation over time requires a flexible approach to financial strategy that constantly reevaluates the optimal balance of growth, earnings, and efficiency. Finding this balance and optimal strategy is the fundamental goal of economic profit measures like RCE.

FIGURE 4
Percentage of Serial Leaders in Top Quartile of Performance Measures



Measurement Matters: How Common Metrics Relate to TSR

Companies adopt performance measures to track and reward performance, which we think should be based on value created for shareholders. In this sense, the north star of performance measurement would be a metric that reliably reflects market value creation, or TSR. When managers try to increase this measure, they are highly likely to be driving higher TSR over the longer term. With this in mind, we set out to analyze how the many common performance measures we see in company executive incentive plans actually related to stock market performance over the last five years.

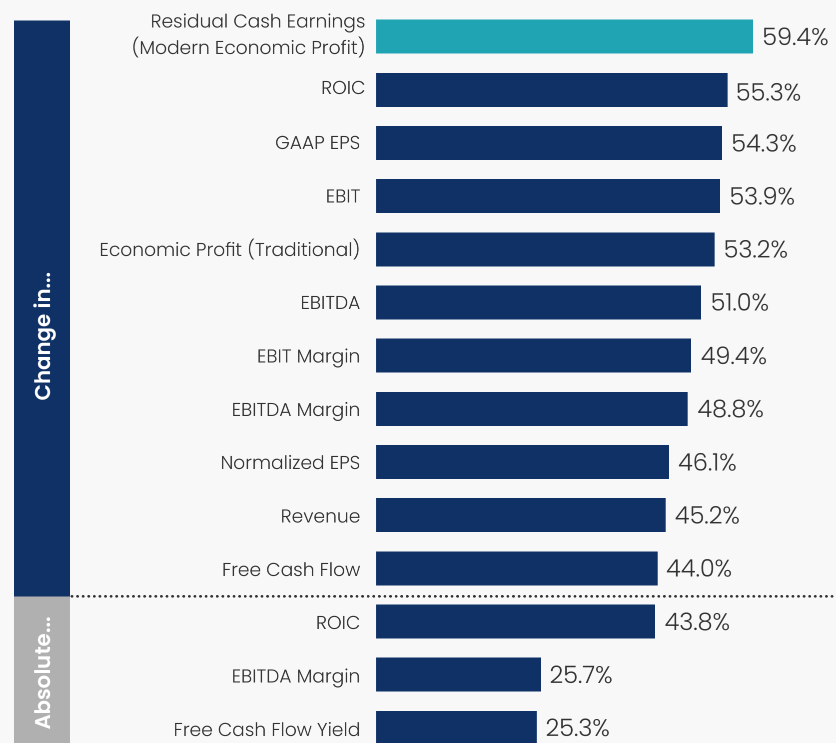
Results & Discussion

The strongest driver of TSR out-performance over the last five years was Residual Cash Earnings (RCE), Fortuna's measure of economic profit. Other top measures included improvement in return on invested capital (ROIC), EPS, and EBIT. Despite stocks' bullish performance in 2024, revenue growth was not a particularly strong driver of shareholder returns. This was in contrast to other strong periods for equities, for example, the five-year period ending in 2021. Instead, investors broadly favored profitability and return measures over high revenue growth. This shift away from a pure growth focus is a multi-year trend that first emerged in 2022 as inflation intensified, suggesting higher interest rates may have affected investor behavior.

A new addition to this year's analysis is a more traditional version economic profit, essentially the generic calculation of an accrual-based economic profit popularized as "EVA" by Stern Stewart in the '90s. In contrast, RCE is simpler, cash-based, and better accounts for value-creating P&L investments like research & development, as discussed later in the report. These differences help explain its ability to better predict TSR outperformance, as shown in *Figure 5*.

FIGURE 5
How Performance Measures Relate to TSR[5]

Probability of Top-Quartile TSR given Top-Quartile Performance



Residual Cash Earnings (RCE) is a cash-based version of economic profit that accounts for growth, profitability, and capital productivity, and capitalizes crucial P&L inputs like R&D to reliably reflect intrinsic value creation.

Economic Profit (Traditional) = NOPAT less a capital charge on net assets (EVA)
EBIT = earnings before interest and taxes
EBITDA = earnings before interest, taxes, depreciation and amortization
EPS = earnings per share
ROIC = return on invested capital

To track how investor preferences fluctuate over time, we aggregated the data over the last four reports to track how these metrics have performed over time in *Figure 6*. Notably, through bull and bear cycles, RCE has reliably related to market outperformance, even as other measures have waxed and waned.

FIGURE 6

Performance Measures' Relation to TSR over Time[6]

Probability of Top-Quartile TSR given Top-Quartile Performance

Performance Measure (Change in...)	**5 Years Ending... 2021**	**2022**	**2023**	**2024**	**Avg.**
Residual Cash Earnings (Modern EP*)	61.0%	52.0%	56.2%	59.4%	57.1%
Traditional EP*	58.2%	49.1%	54.2%	53.2%	53.7%
ROIC	49.0%	51.0%	54.8%	55.3%	52.5%
EBIT	52.0%	49.0%	53.1%	53.9%	52.0%
EBITDA	53.0%	48.0%	47.5%	51.0%	49.9%
GAAP EPS	46.0%	45.0%	51.0%	54.3%	49.1%
EBITDA Margin	52.0%	46.0%	47.8%	48.8%	48.6%
Normalized EPS	43.4%	47.0%	52.9%	46.1%	47.3%
Revenue	56.0%	39.0%	42.9%	45.2%	45.8%
EBIT Margin	48.5%	33.0%	50.6%	49.4%	45.4%
ROIC (Absolute)	43.0%	43.0%	43.7%	43.8%	43.4%
Free Cash Flow (Absolute)	38.0%	37.0%	43.2%	44.0%	40.5%
Free Cash Flow Yield	15.0%	42.0%	22.2%	25.3%	26.1%
EBITDA Margin (Absolute)	26.0%	25.0%	23.5%	25.7%	25.1%

*EP = economic profit

Methodology

To identify which measures best explain market outperformance, we calculated the percentage of companies that were top-quartile in both TSR and the respective metrics displayed in Figure 8 over the last five years. For example, 59.4% of companies that achieved top-quartile TSR performance also achieved top-quartile RCE performance from 2020 - 2024. The data is based on the S&P 900 less financials, real estate, and companies without full data.

Recommendations

Our advice to boards and managements is to carefully consider their approach to internal performance measurement, as it has lasting effects on decision-making and shareholders returns over time. Generally, companies tend to use too many measures and fail to adequately understand how they relate to each other and to overall value creation. Oftentimes with this "balanced scorecard" approach, measures conflict, and this leads to indecision and "*analysis paralysis*."

Another problem is that most measures are incomplete—that is, they don't tell the full value creation story—and this leads to predictably adverse outcomes. For example, companies focused on revenue growth risk lowering profitability to the point of value destruction. Those guided by EBIT or EBITDA growth may not pay sufficient attention to capital productivity. Meanwhile, those occupied with return on capital might sacrifice attractive growth investments that bring down average ROIC but still earn more than the cost of capital, leading to market underperformance.

Economic profit measures like RCE are a reliable proxy for TSR because they clarify tradeoffs between growth, profitability, and capital productivity to send an unambiguous value creation signal. RCE simplifies decision-making to the point where, "up is good and down is bad"—no need for endless analyses of the new plant, product or whatever investment management may be considering. As Ball Corporation's CFO Scott Morrison described their use of economic profit in a 2021 webinar, "[I]t makes the meetings shorter … [and] takes away a lot of the *BS that happens in the budgeting process*."

As market trends and investor preferences for various aspects of performance fluctuate over time, RCE remains a reliable tool to track market value, as evidenced by 86% of our *serial leaders* placing in the top quartile of RCE improvement over the last ten years.

Problems with Common Measures

ROIC

In 2024 investors showed a strong preference for companies with high returns on capital. As mentioned above, this emphasis on capital efficiency likely reflects the higher cost of capital over the last two years as interest rates moved up. The drawback of measuring performance with ROIC is that it unintentionally stifles long-term growth and innovation, putting companies at risk of being leapfrogged by competition in years to come. Too often we see managements pass up value-accretive investments for the sake of boosting ROIC. It may take time for market underperformance to materialize, but in the long run insufficient reinvestment will eventually drag on a company's share price.

EBIT & EBITDA

EBIT and EBITDA growth are some of the most common measures we see linked to internal performance measurement. While an excellent gauge of your bottom line, the fundamental issue with these metrics is that they don't account for the capital required for each dollar of earnings. While this problem generally leads to a suboptimal allocation of capital, in our work we have seen it affect one increasingly vital source of growth in particular: M&A. Again and again, we see companies effectively "buying" EBITDA through acquisitions, with little regard to whether capital spent actually achieves a decent ROI—much to the dismay of their shareholders.

Free Cash Flow

In recent years, it has become increasingly common for companies to use *free cash flow* (FCF) as a period measure of performance. It may seem desirable, since free cash flow over time is used in the discounted cash flow net present value (NPV) model, which is a cornerstone of modern corporate finance. But unless an investment has a return over 100% in its first year, which is rare in our experience, FCF will be negative—and may remain negative for several years if a company is in a growth stage, or modernizing older assets over that period. As a result, free cash flow can motivate underinvestment, which harms shareholders and other stakeholders over the long term.

Earnings Per Share

EPS is perhaps the most common measure we see companies focus on. Despite its merits, managements can feel pressured to maximize EPS over short-term cycles to the extent that they forgo good investments that may pay off handsomely over time. Additionally, GAAP EPS requires R&D investments to be charged as an annual expense. So unless the lion's share of the benefits of R&D is expected during the current fiscal year, which is typically not the case, this distorts EPS by making it look worse. Unfortunately, this tends to discourage R&D investments to meet earnings expectations—often at the cost of future earnings.

Another problem stems from the fact that share repurchases create the appearance of earnings improvement when looking at profitability on a per share basis. So using EPS as an incentive may unintentionally encourage managements to prioritize share repurchases over investing in their businesses to build earnings power.

Don't see your company's performance measure(s) on this list? Reach out and we'd be happy to take a look for you. (info@fortuna-advisors.com)

Managements should carefully consider their APPROACH TO PERFORMANCE MEASUREMENT as it has lasting effects on decision-making and shareholders returns over time.

Residual Cash Earnings (RCE)

There are many business attributes that lead to high total shareholder return (TSR). When it comes to performance measurement, executives are often tempted to layer measures on measures. But this introduces **unnecessary complexity**, and worse, creates **adverse incentives.** So how can management teams effectively balance performance drivers to maximize long-term TSR?

Economic profit, whose most well-known iteration is Economic Value Added (EVA), was developed to serve as a comprehensive performance measure.

Fortuna's partners spent many years implementing Stern Stewart's EVA and applying Credit Suisse HOLT's cash flow return on investment (CFROI). In different ways, these two frameworks aimed to combine growth, profitability, and capital productivity to relate performance to valuation and share price performance.

Unfortunately, both of these measures are fairly complex, and EVA also has been found to discourage long-term growth investment. To arrive at a simpler measure that better balances growth and return, Fortuna conducted extensive capital market research to create Residual Cash Earnings (RCE).

More than any other performance measure, RCE provides a reliable value signal. To put it simply: up is good, down is bad. And most important, it shows a stronger relationship to TSR than EVA, or generic economic profit (see "*Beyond EVA*").

Figure 8 shows the median improvement in RCE normalized as a percentage of starting Gross Operating Assets, for the TSR quartiles. The strong relationship gives us confidence that, if management drives RCE higher over time, TSR will follow.

Figure 9 demonstrates the versatility of RCE in predicting shareholder returns across industries. While traditional economic profit has been criticized as applying only to "old world" companies with tangible assets, RCE is adjusted to capture intangible assets as well, as shown by industries like Software and Pharmaceuticals.

FIGURE 7
RCE Calculation

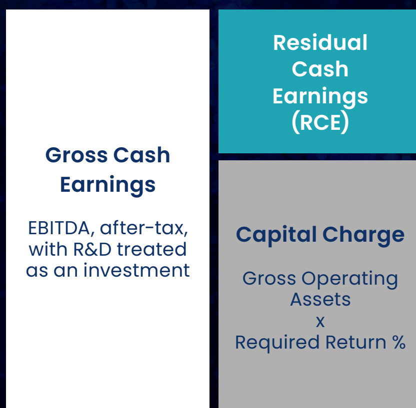


FIGURE 8
Improvement in RCE Relates to Higher TSR[7]

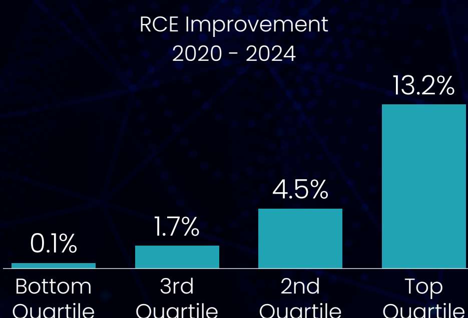
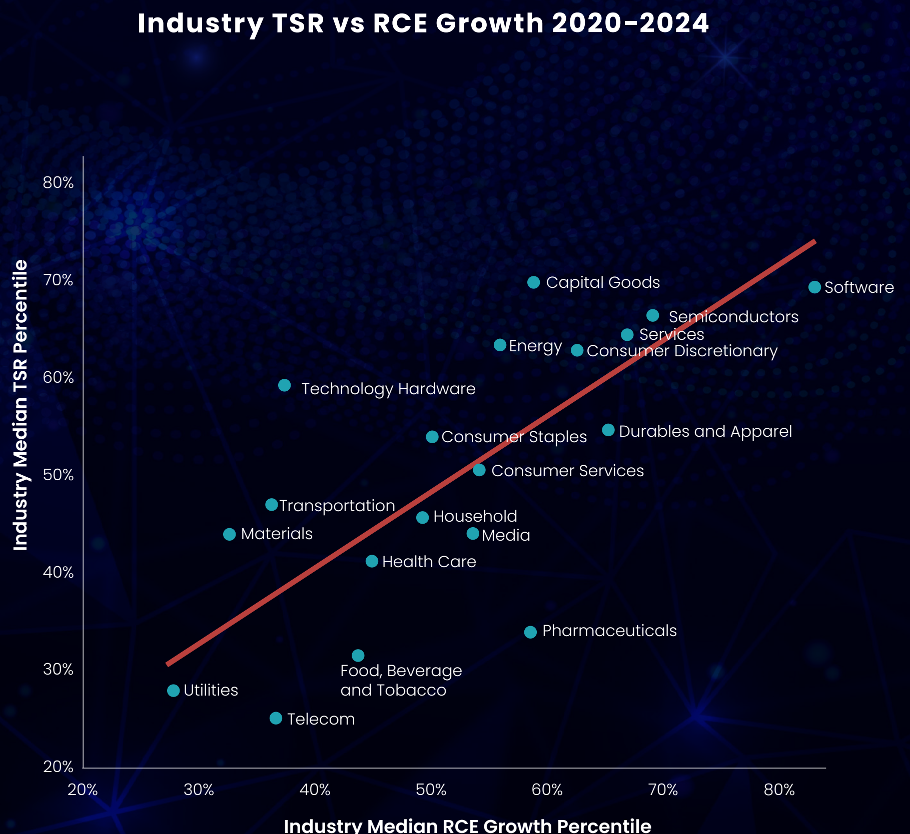
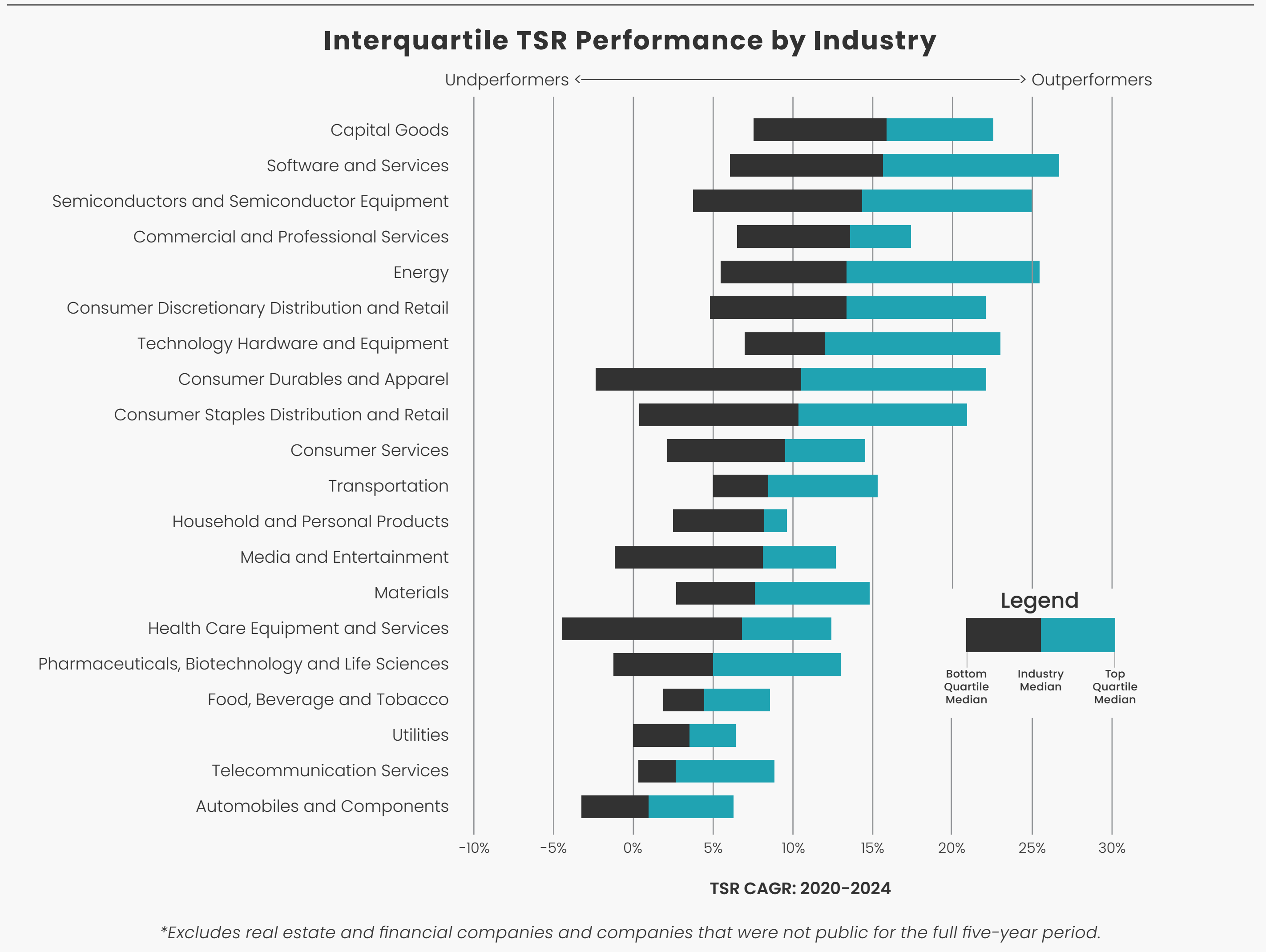


FIGURE 9
Improvement in RCE Relates to Higher TSR



Industry Tectonics

FIGURE 10
S&P 900* Industry Performance and Quartile Distribution, 2020 – 2024



Excludes real estate and financial companies and companies that were not public for the full five-year period.

A Surge of Capital Investment

Despite the media's entrenched focus on tech companies over recent years, Capital Goods was the top-performing industry in terms of median company TSR. To be clear, as shown in *Figure 10*, outperformers for both Software & Services and Semiconductors & Semiconductor Equipment—the main two components of the tech sector (i.e., Information Technology)—delivered well in excess of Capital Goods' outperformers. But tech's outperformance was concentrated in a narrow group of winners at the top. When you look at industries by median company performance, which we believe provides a more accurate view of the industry as a whole, Capital Goods edged out Software and Semiconductors as the top group.

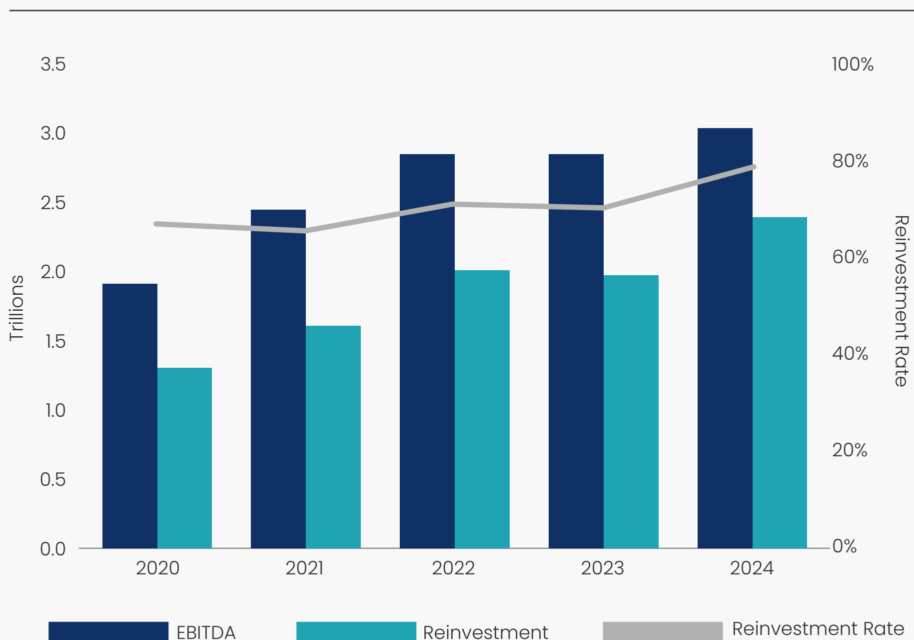
Capital Goods' reign reflects high business and consumer confidence as US companies aggressively built homes, factories, and data centers, among other capital-intensive investments over the last five years. The median company in the group produced a five-year annualized TSR of 15.9%. A broad cross section of subindustries performed well in this group, but Building Products—from home building supplies to HVACs to drainage systems—had an outsized number of outperformers. The top performer of this subgroup was Builders FirstSource, Inc., which manufactures and supplies homebuilding materials. The

next most well represented subindustries were Industrial Machinery Supplies, Construction and Engineering, Aerospace & Defense, and Trading Companies.

A number of trends contributed to Capital Goods' dominance, including immigration-driven population growth, business optimism over rate cuts, as well as an expanding focus on aerospace and defense. Of course, we can't ignore the boom in artificial intelligence development that sparked massive investment in data centers, power sources, and other infrastructure. As a result, Software & Services had the highest increase in reinvestment in 2024, followed by Pharmaceuticals, Biotechnology and Life Sciences, whose reinvestment was likely linked to the rapid deployment of capital to scale production and meet high demand for weight loss drugs.

More broadly, reflecting the boom in Capital Goods was (at least) a ten-year high in corporate reinvestment, which is shown in *Figure 11*. Indeed, the $2.4 trillion reinvested by our sample of S&P 900 companies was 29.2% higher than the average over the last five years. By charting company reinvestment alongside EBITDA, we can trace how a steady rise in earnings has fueled subsequent reinvestment. The rate at which companies reinvested earnings (reinvestment divided by EBITDA) has also steadily risen since 2020 as the economy began to normalize and business confidence improved, following COVID-related supply shocks, as shown by the rising reinvestment rate curve in *Figure 11*.

FIGURE 11
S&P 900* Aggregate Reinvestment, 2020 – 2024



**Excluding financials, real estate, and companies without full data for the period*

Software Supremacy

Turning to tech … In 2024 the AI enthusiasm continued—but as clearer applications for the technology arose, Software & Services replaced Semiconductors and Semiconductor Equipment as the main benefactor of this trend, with a median five-year TSR of 15.7%. Among the top software performers were CrowdStrike Holdings, Fair Isaac Corporation, and Palo Alto Networks, Inc. Not far behind these were common household names like Microsoft, Oracle, and Intuit. Of the 16 top-quartile software companies, 14 (88%) were members of either the Systems Software or Application Software subindustries. The lone standouts of the group were Gartner, Inc. (IT Consulting and Other Services) and GoDaddy Inc. (Internet Services and Infrastructure), which is a testament to these companies' differentiated products, services, and business models.

The bullish tone for 2024 had implications for "safer" sectors. On the other end of the spectrum, non-cyclical industries like Healthcare, Food and Beverage, and Utilities—which had relatively outperformed in 2022 remain at bottom of our industry performance ranking as investors sought more risk and higher returns for their capital.

The Importance of Differentiation

Naturally, some industries have a wider interquartile range than others—that is, the difference between the median top- and bottom-quartile companies in each industry group. As in last year's report, in semiconductors we observed a wide distribution of outcomes, as companies like NVIDIA and Broadcom continued to separate from the pack with cutting-edge technology related to artificial intelligence research. A similar situation can be observed in Software & Services, as the likes of Salesforce and Palantir left many of their peers behind. In most growing industries, research and development is a crucial input for success. Companies in these competitive markets need to ensure their corporate governance practices foster and motivate accountable risk-taking, as well as sufficient investment in, and management of, their research and development pipelines.

Consumer Durables and Apparel was another industry with a wide distribution of returns. Indeed, consumer products often require a source of differentiation to reach the top of the pack. Differentiation can come from many sources, including innovation, but it can also arise from strong brands and corporate purpose. In fact, Fortuna's *research* shows that "high purpose" companies achieve 14.1% higher revenue growth, 7.7% better operating profitability, 5.8% higher returns on capital, 6.2x turns higher valuation multiples—and a substantial 34.7% greater annualized TSR—versus their peers. As with innovation, differentiation results from strong company culture and best practices around investment in intangibles.

FIGURE 12
S&P 900* Rolling Five-Year Annualized TSR Trend by Industry

Industry	2020	2021	2022	2023	2024
Capital Goods	17.2%	16.0%	10.1%	18.1%	15.9%
Software and Services	22.7%	28.4%	13.4%	20.4%	15.7%
Semiconductors and Semiconductor Equipment	28.2%	25.5%	15.2%	28.2%	14.4%
Commercial and Professional Services	21.9%	21.2%	15.8%	17.4%	13.6%
Energy	-5.7%	-0.3%	6.7%	13.6%	13.5%
Consumer Discretionary Distribution and Retail	13.0%	20.7%	14.7%	17.7%	13.3%
Technology Hardware and Equipment	19.8%	21.5%	6.7%	12.1%	12.0%
Consumer Durables and Apparel	9.8%	13.7%	3.7%	18.2%	10.5%
Consumer Staples Distribution and Retail	15.5%	12.2%	10.8%	13.1%	10.4%
Consumer Services	16.1%	15.8%	4.6%	10.5%	9.5%
Transportation	13.7%	16.9%	7.1%	14.1%	8.5%
Household and Personal Products	12.6%	9.3%	8.6%	8.7%	8.2%
Media and Entertainment	15.8%	16.8%	3.5%	12.4%	8.2%
Materials	13.2%	14.4%	7.3%	14.1%	7.5%
Health Care Equipment and Services	19.4%	18.7%	11.8%	10.6%	6.8%
Pharmaceuticals, Biotechnology and Life Sciences	17.7%	25.6%	14.1%	14.8%	5.0%
Food, Beverage and Tobacco	6.7%	9.4%	10.2%	9.2%	4.5%
Utilities	9.9%	9.1%	7.1%	4.4%	3.5%
Telecommunication Services	18.9%	9.5%	7.9%	9.6%	2.7%
Automobiles and Components	7.4%	7.7%	-1.4%	10.0%	1.0%

*Excluding financials, real estate, and companies without full data for the period

Overcoming Obstacles to Value Creation

The 2025 Fortuna Advisors Value Leadership Report aims to help executives and investors better understand the factors that influence TSR performance. Our goal is to inspire companies to commit to long-term value creation, and resist the temptation to sacrifice profitable investments in order to meet short-term expectations. This requires a commitment to understanding the sources of value creation, prioritizing the allocation of scarce resources to those sources, and reliably measuring value creation inside the company to drive the desired management behavior. In essence, the goal is for managements to think and act like long-term, committed owners. The following are some of the common obstacles to TSR outperformance facing company managements.

- ***Insufficient portfolio optimization.*** Companies often stay in businesses where they cannot add value and don't commit enough resources to building and growing businesses with significant untapped potential. Shifting cost pressures from inflation, and a rising a cost of capital, only heighten the importance of regular *strategic resource allocation* and portfolio optimization activities.

- ***Misguided incentives.*** Using too many, or incomplete, performance measures means constant negotiation of budget targets. Worse, it often leads to suboptimal investment decisions.

- ***A use it or lose it mindset.*** Many managements overspend because it's "in the budget." In turn, this can lead to underinvestment in new attractive ideas that arise between budget cycles.

- ***Risk aversion.*** Company culture matters. We all want to avoid failure, but excessive risk intolerance can prevent experimentation and innovation, which harms long-term competitiveness.

- ***The team doesn't think it's possible.*** Visualizing and charting a roadmap for achievement is the first step.

- ***Lack of aspirational goals.*** Aiming high is unwittingly discouraged at many companies where performance is measured against plans and budgets. Such companies pay managers to plan for mediocrity, and that's what they get.

ABOUT FORTUNA ADVISORS

Fortuna Advisors collaborates with leaders to transform decision-making throughout their business to achieve exceptional results. Our management playbook delivers measurable outcomes through:

1. **BETTER INSIGHTS:** See the truth about where value is created or destroyed.
2. **BETTER DECISIONS:** Drive faster, better, and enduring results.
3. **BETTER BEHAVIORS:** Align incentives and processes to drive execution.

We serve as a catalyst to create a culture of ownership, where everyone from the board to management and employees embraces a long-term investor perspective to unlock the organization's full value creation potential.

CONTACT US

to learn how your company may be inadvertently facing obstacles to value creation.

Email: *info@fortuna-advisors.com*

Tel: 631-478-5670

www.fortuna-advisors.com

NOTES

[1]"S&P 500 Hits 57 All-Time Highs In Record-Breaking 2024: Magnificent 7 Drive 30% Of Nasdaq's Surge", Benzinga; Capital IQ.

[2]Some of the measures we use, such as EBITDA and Residual Cash Earnings, are not suitable for financials companies, where interest cost is thought of as a cost of goods sold and funding debt is generally not considered to be part of long-term capital.

[3]All analyses performed in this report use data from Capital IQ.

[4]Analysis excludes Banks, Diversified Financials, Insurance, & Real Estate Industries.

[5]Note: Fortuna Advisors analysis using data from Capital IQ. FCF Improvement, EBIT Growth, and EBITDA Growth are calculated as the change in the respective measures divided by revenues at the beginning of the period to normalize the metrics for size. RCE improvement is normalized by size, by calculating the change in RCE divided by Gross Operating Assets at the beginning of the period. Growth measures are calculated as CAGRs over the five-year period. EPS Growth is calculated according to GAAP methodology. ROIC is calculated as NOPAT/Net Invested Capital.

[6]Note: Fortuna Advisors analysis using data from Capital IQ. FCF Improvement, EBIT Growth, and EBITDA Growth are calculated as the change in the respective measures divided by revenues at the beginning of the period to normalize the metrics for size. RCE improvement is normalized by size, by calculating the change in RCE divided by Gross Operating Assets at the beginning of the period. Growth measures are calculated as CAGRs over the five-year period. EPS Growth is calculated according to GAAP methodology. ROIC is calculated as NOPAT/Net Invested Capital.

[7]Note: RCE improvement is normalized by size, by calculating the change in RCE divided by Gross Operating Assets at the beginning of the period.