



From Accounting to Economics to Valuation

The Applied Finance Group (AFG) helps investment advisors, institutional investment, consulting, corporate firms globally in accurately measuring corporate performance and identifying mispriced equities. AFG developed its proprietary framework, Economic Margin, to correct distortions created by traditional accounting-based analysis. The Economic Margin Framework is more than just a performance metric, as it encompasses a valuation system that explicitly addresses the four main value drivers of enterprise value: profitability, competition, growth, and cost of capital. Unlike traditional valuation approaches that utilize highly sensitive perpetuity assumptions, AFG's approach incorporates company specific competitive advantage periods which identify companies that may lose excess returns over time faster than their competitors.



Helping Investment Managers Make Better Investment Decisions Through Unique Corporate and Valuation Insights

AFG provides its clients a clear and robust set of applications to easily compare valuations and corporate performance over time, firms, industries and countries. By understanding differences between a stock's intrinsic value and market price, management effectiveness, and earnings quality, the firm's recommendations outperform the market regardless of a company's sector, size, or growth/value orientation. AFG's research covers companies traded on U.S. exchanges. Canada, UK, and Japan will be available the second quarter of 2008 and will expand to over 16 countries by the end of the year. To learn more about our global research, visit: www.EconomicMargin.com

AFG's Client Benefits Include:

- Identifying Under/Over Valued Companies
- Ability to evaluate a company's ability to create shareholder value
- Understanding market expectations embedded in stock prices
- Tools and Research to help portfolio managers/analyst focus on investment decision-making.

Why Traditional Accounting-Based Metrics Fall Short

Earnings are a poor proxy for economic profitability because they do not accurately reflect the true cash flow of the firm.

- On average, corporate earnings represent only 45 to 50 percent of a company's cash flow.
- Earnings do not reflect risk.

Accounting ratios mix/confuse many different value drivers.

- Return on Assets/Return on Equity fail to reflect wealth creation or destruction.
- Different Asset Life, Asset Mix, Asset Age, Capital Structure distort ratios across firms.

Accounting rules distort many aspects of economic reality.

- Research & Development costs, which are long term investments, are immediately expensed under GAAP accounting.
- Operating Leases, obligations which must be paid similar to debt never appear on company balance sheets.

Key questions when evaluating any investment:

- How much capital is required? How much capital does the company use in its operations? Is the amount growing or declining through time?
- What is the cash flow? How much cash does the company generate per unit of invested capital? Is the company's cash yield increasing or decreasing?
- What are the opportunity costs of capital? In the current marketplace, what should the average investor expect as a return for an investment given its risk? After accounting for

For More Information please contact us at: (312) 362-9903 or [Visit us at: www.EconomicMargin.com](http://www.EconomicMargin.com)