

Gentex, Corp.

Nasdaq: GNTX

Analyst: Matthew Darcy

Sector: Industrials

BUY

Price Target: \$23.04

Key Statistics as of 3/12/2015

Market Price:	\$17.98
Industry:	Auto Parts and Equipment
Market Cap:	\$5.31 B
52-Week Range:	\$13.17-19.06
Beta:	1.319

Thesis Points:

- The Industry is Conducive to Growth
- A Large Number of Patents, Combine with Effective R&D, Gives Gentex a Sustainable Competitive Edge
- A Sustainable Competitive Edge in a Growing Industry Allows Long Term Growth to be Higher than Growth of GDP
- Gentex's R&D Capabilities and its Adaptability Reduces Potential Threats

Company Description:

Gentex Corporation is a global company that designs, manufactures, and sells rear view mirrors, with various high tech safety features, as well as automatic headlights, which adjust brightness as you drive. The company also designs and manufactures dimmable aircraft windows, and smoke alarms and signaling devices, which account for 3% of net income. Dimmable aircraft windows are currently used in Boeing 787 Dreamliners, and are also sold for use in other airplanes. The Smoke alarm systems that Gentex produces can be used in residences, businesses, and hotels. The company has no net debt and a profit margin of 21%.

Note: There is an entirely separate, privately held defense contractor, also known as Gentex Corporation.



Thesis

A company like Gentex, which is constantly developing new technology for the safety of drivers, will be able to grow more quickly than company's in other industries. This is due to the nature of the auto parts industry, where new technologies, and safety features start out in luxury cars, and then build popularity. Gentex is positioned well in this market, with an 88% share. The company will be able to protect their market share, with the competitive advantages described in this paper. Because they have these advantages in such a quickly growing industry, it is justified to value Gentex with a long term growth of 4.5%. This raises the price of Gentex above the current market value. Therefore, Gentex is a BUY.

The Products

Gentex Corp. designs and manufactures internal and external mirrors that dim in proportion to the amount of glare coming from trailing vehicles' headlights. The mirrors come with various combinations of technical features, including a compass, thermometer, rear camera display, frameless, microphones, OnStar compatibility, HomeLink, blind spot sensors and other warnings. HomeLink gives the mirrors the ability for two way communication with garage doors and security gates, home lighting, and security systems, using radio frequency. It has the potential to activate and communicate with any radio frequency compatible system as well.

Gentex was a licensee of HomeLink since 2003, until September 27th 2013, when Gentex acquired HomeLink. Gentex is currently expanding the scope of this product to include vehicles other than cars, such as ATV's, snowmobiles, lawn mowers, etc.

Other upcoming products include a hybrid full display mirror that will allow the driver to view the road behind them through a video camera, as well as the reflective surface. The video display eliminates issues of blocked vision from passengers in the back, and is especially useful in cars with smaller rear windows. However, at the flip of a switch, the product functions as a regular mirror. This ability to switch allows the product to legally qualify as a mirror, and provides a failsafe should the

camera become covered, or have other technical difficulties.

The company sells its products through OEMs only. Its main buyers are, Toyota, Volkswagen/Audi, Daimler AG, and Fiat Chrysler Automotive Group. A customer can also purchase a single mirror through Mito Corporation. Gentex mirrors are suitable for OEMs, because they are a cheap option for adding advanced technology to vehicles. When customers, or governments, want new cars to have a specific technology, for example back up cameras, the car designers have two options. Either they rip open the center console, and re-tool it to make room for the new technology, or they buy a new mirror to replace the old one. It is much cheaper for the OEMs to buy the mirror, than find room for new technology elsewhere in the car.

Growth of the Market

In the auto parts market, new technology often starts out being sold through luxury vehicles, to more wealthy individuals. But as the technology proves its practicality, consumers begin to expect it in all makes and models. This has held true with air conditioners, power locks, and power windows. As this company's products prove their usefulness, there will be a similar effect. The demand for this company's products will grow rapidly, and Gentex has the patents.

There are times when the government enforces this trend of auto products, especially if the product has safety implications. The most recent example is the backup camera. By May 2018, all new vehicles under the weight of 10,000 pounds will be required to have some form of backup camera. This was announced, by the US National Highway Traffic Safety Administration, in 2014. Although this announcement is already priced in, it is highly likely that the US government will continue to pass safety regulations that will be beneficial to Gentex corporation's growth. All of the products Gentex creates have some safety implication.

Another catalyst for growth is in the exterior mirror segment of the business. Growth of this segment is one of the company's main focuses as of right now. 25% of cars have interior auto dimming mirrors and only 7% have exterior auto-dimming mirrors. The Company sees every car with only interior mirrors, as a potential area

for growth of their exterior mirror business. Gentex believes that the superior quality of their current products will convince OEMs to purchase future products.

Competitive Advantage

Gentex has a significant competitive advantage that allows it to maintain an 88% market share, in the auto dimming mirror industry. This advantage is derived from their use of patents, the company's constant innovation of products, and the company's ability to adapt.

Gentex currently has 495 US patents, 556 foreign patents, and 216 pending patents. The company believes that these patents provide them with a significant competitive advantage, although no individual patent is necessary for the company's operation.

In 1993, the company was awarded \$2.2 Million in damages after suing Donnelly Corporation, for patent infringement. That company is currently known as Magna International, and is Gentex's largest competitor. This event has validated the company's use of patents and has proven its ability to win litigations.

Usually patents would only provide a short term competitive advantage, because they will eventually expire. However, this company is constantly coming up with new technology, which means it will be able to continuously invent and patent new products. The company puts about 6% of its revenue into research and development each year, which allows it to stay ahead with cutting edge technology. Because Gentex is so effective with its R&D, the company's use of patents forms a sustainable competitive advantage.

Gentex was founded in 1974, as a developer and manufacturer of smoke alarm and detection systems. The company has since moved away from the fire protection industry. In 1982, Gentex began selling auto dimming rear view mirrors, and the fire protection industry now makes up less than 3% of income. This is a testament to the company's ability to adapt. When a company can adapt well, it will be less prone to risk of failing markets, meaning the company will be able to adjust its practices, if at all necessary.

All of these factors contribute to the company's ability to maintain its competitive advantage. The company's

current position in the market, its wealth of patents, its ability to use those patents, its ability to continuously generate new patents, and its ability to adapt all give this company a small economic moat. This means that the company has protection from the threat of new entrants.

Long Term Value Creation

Generally speaking, a company cannot sustain a growth rate above GDP or an ROIC above their WACC, because other competitors will enter into their industry, causing growth and returns to be lower. However, Gentex's economic moat will shield this company from the threat of new entrants. This allows the company to sustain a more favorable growth rate, and ROIC.

This justifies the company's ability to grow at 4.5%. The market, on the other hand, is using a long term growth rate of 3.22%, which is equivalent to the 10 year median growth of GDP. The combination, of high growth and ROIC greater than WACC, leads to the creation of value on a long term bases. This explains why the market is under pricing GNTX, and is the main reason that this company is a buy at its current price.

Potential Threats

People who are short on this company believe that governments may, eventually, make it legal to have rear view cameras, instead of mirrors, in automobiles. They believe that people will prefer the cameras over the mirrors, in the event that cameras become legal. Here is the reason that this is not actually a threat to Gentex. The company has recently invented a full display hybrid mirror. This mirror has both a rear view camera, as well as a reflective surface. Users can switch between the two options, simply, by flipping a switch. This means they have created something better than a rear view camera. They have created the option to have both. This is important, because the mirror creates a failsafe, in case the camera is covered, or there is some technical difficulty while driving. Even more importantly, the technology is legal for use, today. Many customers, especially older customers, will be happy to have the safety net of a mirror. Additionally, customers will be able to enjoy the benefits of a full video display.

In the event that rear view mirrors become obsolete, Gentex will be able to adjust their business to be geared

towards cameras. They already have the technology, evident in their new hybrid products, and they have already demonstrated their ability to adapt. This company was originally created to make fire detection systems, a segment of the business that makes up less than 3% of income today.

People who are short on this stock actually see the growth of the market as a threat, saying that this company may need to lower its prices, as the market for its products begins to grow. There are two different scenarios that refute this concern:

1) The company may see lower profit margins, if this is the case. However, this will be offset by the heightened sales volume.

2) Gentex has been on the forefront of new technology. If the market begins to squeeze its profit margins too much, this company will be able to sell or license some of its patents, and move on to new frontiers. Research and Development of new products has been a strong suit for this company, and the company is always looking to invent and innovate.

Summary

Gentex Corporation is in an industry that is conducive to growth. It also has a sustainable competitive advantage, in that industry. This means the company should be valued with a long term growth rate that is higher than the growth of GDP. Analysts are currently using a long term growth rate equivalent to the growth of GDP, which is why the price of the stock is undervalued. Gentex is a BUY.

CENTER FOR GLOBAL FINANCIAL STUDIES									
Gentex Corp.	gntx	Analyst Matthew Darcey	Current Price \$17.98	Intrinsic Value \$20.57	Target Value \$23.04	Divident Yield 2%	Target Return 29.94%	NEUTRAL	
General Info		Peers	Market Cap.	Management					
Sector	Consumer Discretionary			Professional	Title	Comp. FY2012	Comp. FY2013	Comp. FY2014	
Industry	Auto Components			Bauer, Fred	Founder, Executive Chairman an	\$ 1,588,528.00	\$ 1,708,794.00	\$ -	
Last Guidance	Jan-28-2015		\$0.00	Downing, Steven	Chief Financial Officer, Vice Presi	\$ -	\$ 536,679.00	\$ -	
Next earnings date	4/17/2015	Munkami Corporation	\$208.07	Flynn, Paul	Vice President of Operations	\$ 257,561.00	\$ 322,841.00	\$ -	
Market Data		Motherson Sumi Systems Ltd.	\$6,938.94	Newton, Mark	Senior Vice President, Secretary at	\$ 688,283.00	\$ 741,624.00	\$ -	
Enterprise value	\$5,077.35	Tokai Rika Co., Ltd.	\$1,936.64	Nash, Kevin	Chief Accounting Officer and Vic	\$ -	\$ -	\$ -	
Market Capitalization	\$5,309.15	Idihok Industries Ltd.	\$178.74	Guarr, Tom	Vice President of Chemical Resea	\$ -	\$ -	\$ -	
Daily volume	0.75	Magna International Inc	\$21,512.75	Historical Performance					
Shares outstanding	295.28	Current Capital Structure			gntx	Peers	Industry	All U.S. firms	
Diluted shares outstanding	294.30	Total debt/market cap	5.23%	Growth	10.8%	5.7%	6.4%	6.0%	
% shares held by institutions	92.67%	Cost of Borrowing	0.00%	Retention Ratio	18.1%	42.0%	40.3%	56.6%	
% shares held by insiders	2.79%	Interest Coverage		ROIC	40.1%	22.8%	17.0%	12.9%	
Short interest	1.88%	Altman Z	8.43	EBITDA Margin	22.6%	4.8%	8.8%	13.7%	
Days to cover short interest	3.45	Debt Rating	AA	Revenues/Invested capital	134.9%	291.2%	233.4%	202.3%	
52 week high	\$19.06	Levered Beta	1.46	Excess Cash/Revenue	51.9%	7.8%	9.2%	18.5%	
52-week low	\$13.17	WACC (based on market value weights)	10.45%	Unlevered Beta	1.41	0.71	1.20	0.95	
5y Beta	1.35	Past Earning Surprises			TEV/REV	3.7x	1.0x	2.4x	
6-month volatility	25.75%	Revenue		TEV/EBITDA	12.7x	5.5x	8.7x	11.3x	
		EBITDA		TEV/EBITDA	15.1x	8.0x	11.7x	15.4x	
		Norm. EPS		TEV/UFCF	39.2x	16.1x	27.1x	26.8x	
Last Quarter	-4.8%		-4.0%	Non GAAP Adjustments					
Last Quarter-1	3.6%		4.2%	Operating Leases Capitalization	100%	Straightline		10 years	
Last Quarter -2	-0.6%		8.3%	R&D Exp. Capitalization	100%	Straightline		10 years	
Last Quarter -3	3.4%		4.3%	Expl./Drilling Exp. Capitalization	0%	N/A		N/A	
Last Quarter -4	0.9%		14.3%	SG&A Capitalization	0%	N/A		N/A	
Proforma Assumptions				Forecasted Profitability					
		Period	Rev. Growth	Adj. Op. Cost/Rev	Revenue	NOPLAT	Invested capital	UFCF	
Operating, Cash/ Cash	0.0%	LTM	17%	61%	\$1,375.50	\$284.37	\$1,612.99	\$284.37	
Unlevered Beta	1.41	LTM+1Y	10%	60%	\$1,511.68	\$328.02	\$1,689.38	\$251.63	
Rev/Invested Capital	134.9%	LTM+2Y	10%	60%	\$1,665.87	\$372.29	\$1,764.07	\$297.60	
Continuing Period Revenue Growth	4.5%	LTM+3Y	12%	60%	\$1,862.44	\$421.25	\$1,842.23	\$343.08	
Long Term ROIC	16.0%	LTM+4Y	9%	60%	\$2,024.47	\$462.79	\$1,911.71	\$393.31	
Invested Capital Growth	Reverts to Maintenance	LTM+5Y	7%	60%	\$2,158.09	\$494.66	\$1,973.64	\$432.72	
Justified TEV/REV	2.5x	LTM+6Y	6%	60%	\$2,277.86	\$522.72	\$2,030.37	\$465.99	
Justified TEV/EBITDA	8.0x	LTM+7Y	5%	60%	\$2,392.32	\$549.19	\$2,084.22	\$495.34	
Justified TEV/EBITDA	11.0x	LTM+8Y	5%	60%	\$2,506.26	\$575.20	\$2,137.41	\$522.02	
Justified TEV/UFCF	15.0x	LTM+9Y	5%	60%	\$2,622.33	\$601.49	\$2,190.34	\$548.56	
Valuation				Valuation					
	ROIC	WACC	EVA	Enterprise Value	Total Debt	Other claims	Equity	Adjusted Price	
LTM	17.6%	10.4%	\$115.90	\$5,775.29	\$265.63	-\$497.43	\$6,007.10	\$20.81	
LTM+1Y	20.3%	10.6%	\$165.07	\$6,154.89	\$265.63	-\$828.58	\$6,717.84	\$23.31	
LTM+2Y	22.0%	10.7%	\$200.45	\$6,511.66	\$265.63	-\$1,220.51	\$7,466.54	\$25.81	
LTM+3Y	23.9%	10.8%	\$241.32	\$6,865.26	\$265.63	-\$1,674.36	\$8,273.99	\$28.58	
LTM+4Y	25.1%	10.9%	\$272.15	\$7,196.15	\$265.63	-\$2,199.14	\$9,129.66	\$31.50	
LTM+5Y	25.9%	11.0%	\$293.80	\$7,516.18	\$265.63	-\$2,777.00	\$10,027.55	\$34.67	
LTM+6Y	26.5%	11.1%	\$312.51	\$7,839.06	\$265.63	-\$3,401.52	\$10,974.96	\$37.81	
LTM+7Y	27.0%	11.2%	\$330.42	\$8,174.07	\$265.63	-\$4,072.61	\$11,981.05	\$41.25	
LTM+8Y	27.6%	11.3%	\$348.38	\$8,519.88	\$265.63	-\$4,788.53	\$13,042.78	\$44.89	
LTM+9Y	28.1%	11.4%	\$366.69	\$8,877.36	\$265.63	-\$5,551.71	\$14,163.44	\$47.97	
Monte Carlo Simulation Assumptions				Monte Carlo Simulation Results					
	Base	Stddev	Min	Max	Distribution	Mean est.			
Revenue Variation	0	10%	N/A	N/A	Normal	\$20.81			
Op. Costs Variation	0	10%	N/A	N/A	Normal	σ(e)			
Market Risk Premium	6%	N/A	5%	7%	Triangular	3 σ(e) adjusted price			
Long term Growth	5%	N/A	3%	11%	Triangular	Current Price			
Terminal Value	0	0.1	N/A	N/A	Normal	Analysts' median est.			