

BUY

Price Target: \$35.50

Key Statistics as of 03/09/2015

Market Price: \$20.75
Industry: Leisure Products
Market Cap: \$933.35M
52-Week Range: \$16.16-\$24.90
Beta: 2.17

Thesis Points

- Highly experienced management team
- #1 market share in performance sport boats
- Expected market recovery
- Industry-leader in innovation
- International expansion

Company Description

Malibu Boats, founded in 1982, is based in Loudon, Tennessee. It manufactures, markets, distributes, and sells performance sport boats. The company provides boats for use in water sports, including water skiing, wakeboarding, and wake surfing, as well as general recreational boating. It also offers various accessories and aftermarket parts. The company sells its performance boats under the Malibu and Axis Wake Research brands through a network of independent dealers primarily in the United States and Canada, but also internationally. The company is the industry leader in the sale of performance sport boats. The company is publicly traded since January 2014.



Thesis

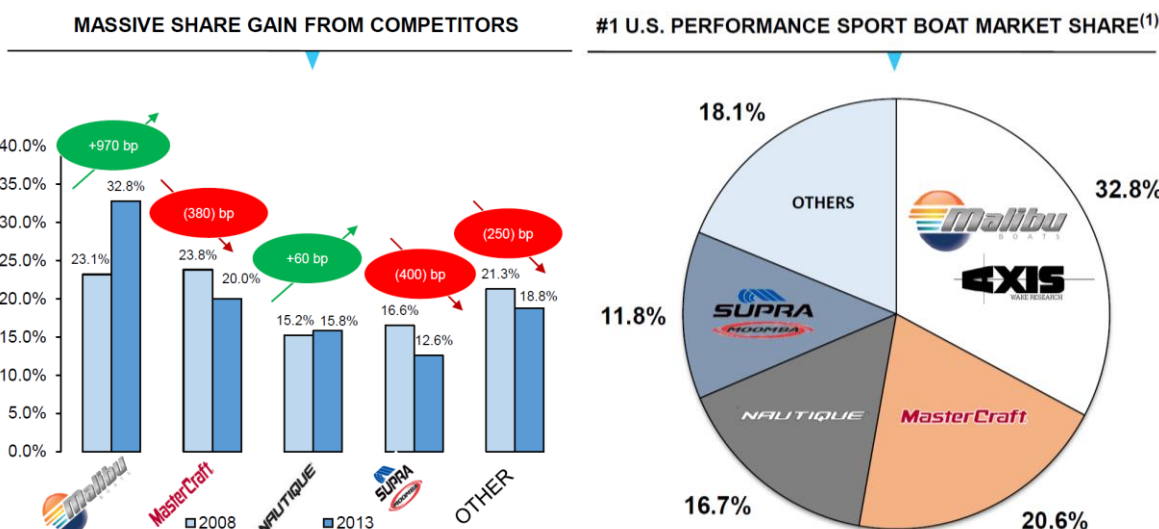
Malibu Boats, founded in 1982, is the leader in performance sport boats (PSP) sales in the United States. Its management team has been able to create enthusiasm for the company, which was reflected in recent financial statements. The company has been innovating a lot to provide customers with high quality boats. With the expected recovery in the industry, the company will capitalize on its leadership and brand recognition to further improve its superiority and its global expansion. The company managed to make economies of scale and has a competitive advantage over its competitors. At a current price of \$20.94, between the 52-week high and low, the company is a BUY.

Highly experienced management team



Almost all of the top executives at Malibu have prior experience in the marine industry. Malibu Boats management believes in “encouraging the creativity of a workforce whose love of the job translates into a superlative product and great customer service”. They consider themselves to be a family. Both the CEO and the CFO have joined the company in 2009. Since June 2010, about one year after they joined the company, revenues have increased at a 15.64% compound annual growth until most of the recent quarterly report. Jack Springer, CEO, has a nine year experience in the marine industry and has worked for several competitors of Malibu Boats. He also served as integration officer for Nautique. When he was appointed as CEO, Malibu Boats has undergone substantial changes including a new brand launch called Axis Wake Research, which provides lower expensive boats to target a higher number of potential customers. Ritchie Anderson, COO, has an impressive thirty-one year of marine industry experience and joined the company in 2011. Finally, Dan Gasper, VP of product design has been employed by the company for twenty seven years. He has a strong experience in manufacturing, quality, engineering and design of sport boats. He knows exactly what customers are expecting from Malibu Boats. This team also led to profitability improvement every year since 2009. The market share of the company has increased since new management took over in 2008. With a complete knowledge of their market, this team is able to take the right decisions for the success of the company.

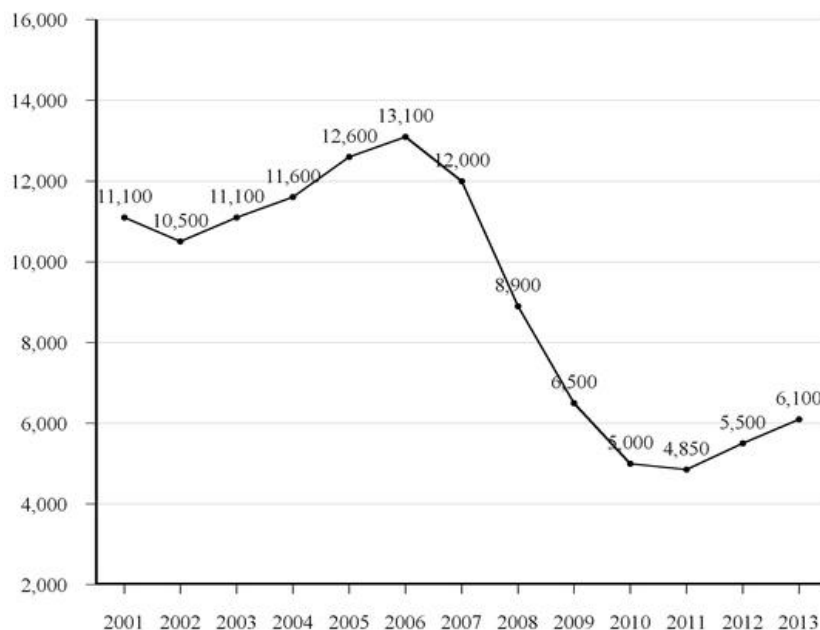
#1 market share in performance sport boats



The company is the industry leader in number of performance sport boats sold in the United States from June 2010 to June 2014. It will continue at least for the next several years. Sport boats are used in water skiing, wakeboarding and wake surfing. They are also widely used for recreational purposes. In 2008, a year prior the arrival of the new CEO Jack Springer, the company had a 23.1% market share. This number increase to 32.8% for the fiscal year ended June 30, 2014 thanks to innovative and diverse product offering. This 970 basis points increase corresponds to a cumulative 725 increase in the number of units sold over the past 6 years, as stated in the bar chart on page 2. The pie chart in the previous page also shows that the company is facing little competition. There are only three significant competitors to the company: Mastercraft, Nautique and Supra. There are also plenty of smaller performance sport boats producers. None of them have been able to remove Malibu Boats from its industry leadership. All of its competitors have seen their market share shrink in that period (except Nautique with a slight increase in market share). It means that Malibu strengthened its domination in the market. To respond to the increasing demand 19 dealer locations were converted from selling competitors' product's over this 6 year period. Moreover, Malibu and Axis brands have been for over 30 years widely recognized in the powerboat industry. Since its creation in 1982, Malibu Boats has received a total of 19 "Boat of the Year Awards". In 2012, Malibu sponsored the wakeboarding's biggest event to date: the "Red Bull Wake Open". This is the first time the company had such an important media and people exposure. This marketing campaign highly contributed to increase their brand awareness with dealers and with consumers in the past two years, which will eventually further boost sales and market share. In order for Malibu Boats to strengthen its market leadership, it has developed a vertical integration program. The company acquired a boat tower manufacturer in 2009, which makes it less dependent on suppliers. The company also planned to start the production of boat trailers by 2016. This activity will require capital expenditures under \$1million but is expected to generate high return on investment.

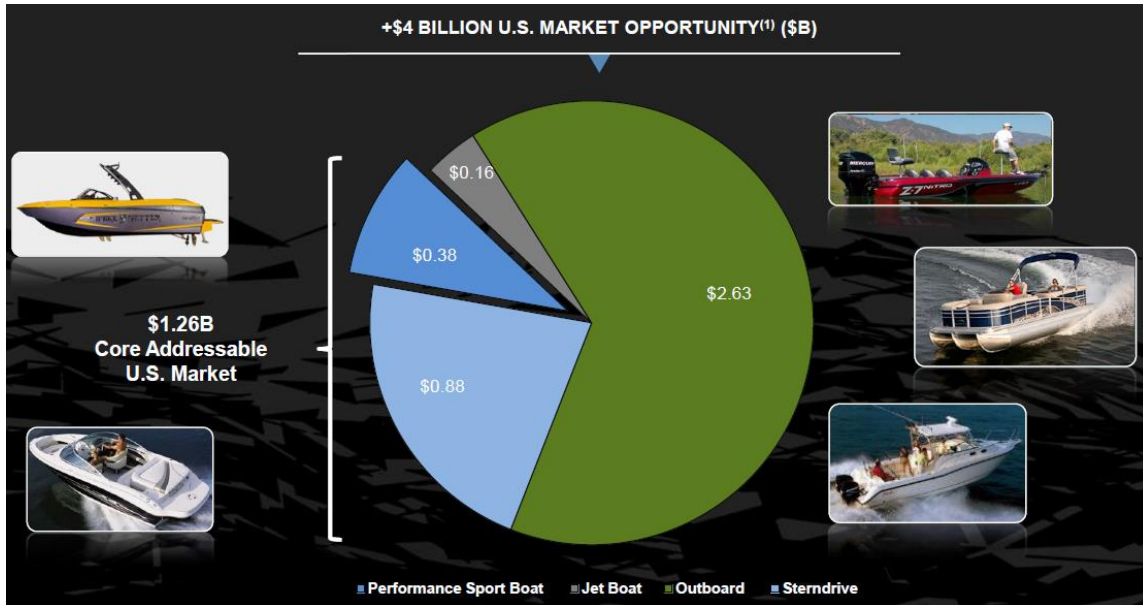
Expected market recovery

U.S. Performance Sport Boat Retail Sales

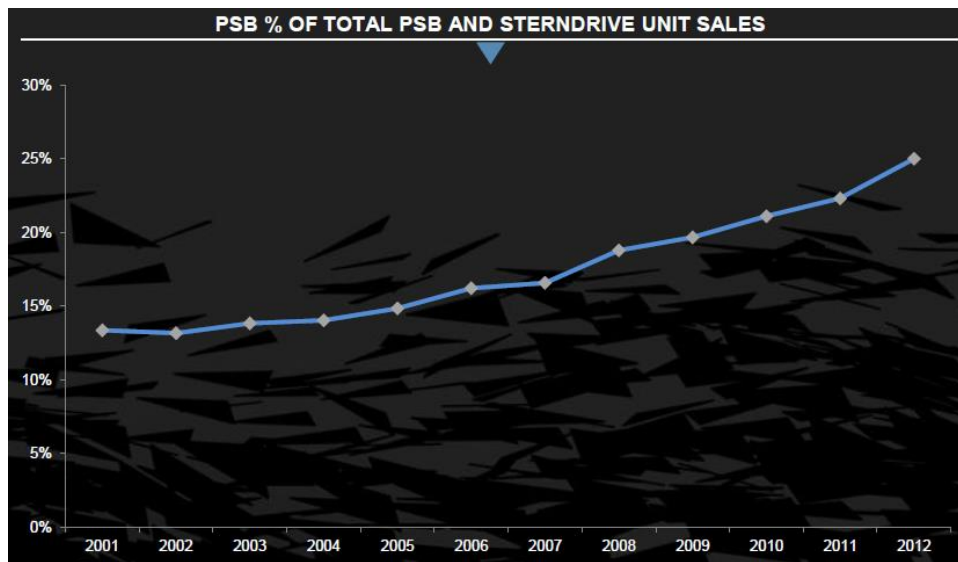


The industry suffered during the recent financial crisis. In 2006, the industry sold a record 13,100 performance sport boats. This number decreased to 4,850 in 2011. However, it steadily increased to 6,100 in 2013. It is expected to improve further to 6,850 by the end of 2014 (data are not yet available but this number based on forecasts presented in the most recent 10K report of the company). The unit sales of performance sport boats in the United States increased by 11% from 2012 to 2013. This is one of the industries that have the highest post-crisis growth rate. The leading and growing market share of Malibu

Boats makes it very well positioned to take advantage of this ongoing recovery. In 2013, performance sport boats sales remained 53% below the average annual new unit sales before the crisis, which leaves a huge space for the market to recover if sales can reach prior levels. Malibu Boats will take advantage of the market growth opportunities thanks to its commitment to innovation, as described later on. Moreover, the average age of performance sport boats was 20 years in the middle of 2014. This is significant higher than the 15 years average life in 1997. This was mainly due to the low renewal rate during the past five years. It suggests that consumers might want to renew their boats anytime soon. It will increase the number of new boat sales, which would confirm the expected recovery of this specific market.



The graph above displays the market segmentation of the recreational boat industry. We can see that performance sport boats only represent \$0.38 billion out of the \$4.05 billion of the boat industry in the United States. It means that there is a large and addressable market opportunity for Malibu Boats. The particular PSB segment is also growing faster than the overall powerboat industry, which grew by only 2% from 2012 to 2013. The sterndrive boats represent a \$0.88 billion market. They represent the core addressable market for Malibu in the upcoming years because these boats are very similar to performance sport boats in terms of design and performance. Customers could tend to switch to performance sport boats. Indeed, the next graph shows why this is likely to happen in the foreseeable future.



This graphs show the proportion of performance sport boats (PSB) sales as a percentage of the total PSB and sterndrive unit sales. We can see that PSB represented about 14% of this total in 2001. This market share has been steadily increasing for 12 years to reach about 25% in 2012. This means that there is a shift in demand from customers. They tend to prefer PSB over sterndrive boats. Malibu Boats is currently able to produce about 4,000 boats per year. It has developed an expansion program allowing up to a 5,000 yearly boat production by the end of 2015. The company is also expected to increase its capital expenditures by \$1million next year to be able to produce up to 6,000 boats in 2016. This is a 50% increase within 2 years. This means that Malibu Boats is highly confident that the demand for performance sport boats will increase in the near future.

Commitment to innovation

Malibu Boats is the leading innovator and pioneer of modern wake surfing technology. Innovation in the design of new boat models and new features has been a key to the success of the company. Given that the boats the company produces are equipped with plenty of different features, they are suitable for a wide range of activities. The company currently offers 14 different types of boats, which means that customers can easily select a boat suited for their individual performances. The company has issued 12 U.S. patents and has 14 more U.S. patents applications pending. In 2009, Malibu Boats launched the Axis brand of boat. These boats were designed to be an entry-level product. While Malibu Boats range from \$55,000 to \$125,000, Axis boats only range from \$45,000 to \$85,000. This brand captured 6.4% of the performance sport boats U.S. market share as of December 31, 2013 because new customers can now afford such boats. The most famous and useful innovation of the company is called Surf Gate. This invention was awarded “Innovation of the Year” in 2013 by the Watersports Industry Association during the Surf Expo 2013 and is highlighted in the picture below:

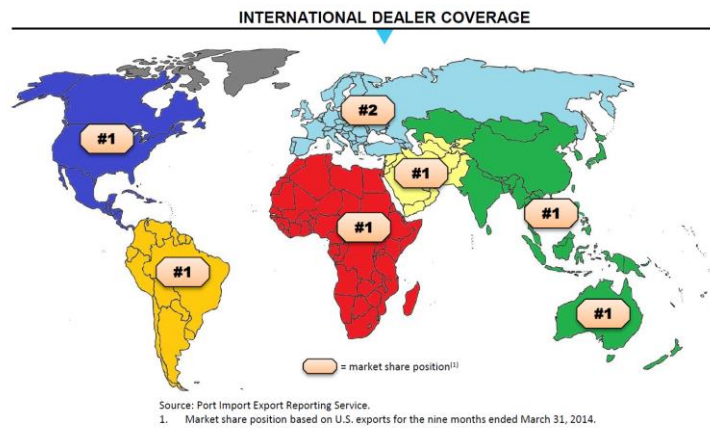


Released in June of 2012, Surf Gate revolutionized the activity of wake surfing. In the past, “participants were forced to lean their boat to one side to create a rideable wave, and wake surfers were limited to surfing on one side of the boat at a time.” Malibu has issue 3 U.S. patents and has 6 pending U.S. patents for Surf Gate itself. Surf Gate allows the driver of the boat to change the convergence of water off the hull by manually articulate a panel located at the stern of the boat, while keeping the boat evenly weighted. It also allows users to surf on either side of the boat’s wake, which makes the surf experience more convenient and enjoyable. Malibu was the first boat company to implement such a solution. Surf Gate has been released to Axis Wake Research boats since 2014. Malibu filed a patent infringement case against Nautique Boat Company in 2014 relating to the unauthorized use of a technology similar to Surf Gate. This patent litigation was settled in February 2015 and won by Malibu Boats. Nautique was required to pay Malibu for this past unauthorized use and was granted a royalty-bearing license for the future. This will generate constant money inflows for the company in the future. Malibu also received a one-time payment of \$2.25 million from Nautique. This means that other companies recognize the value of Malibu’s innovation because it has the ability to create unique and very useful features. For the future Malibu Boats has developed a multi-year product evolution plan to even further improve the functionality and customization of this revolutionary technology. Besides wake enhancement systems (like Surf Gate), Malibu Boats is focused on improving the electronic controls and the design of each new boat. It has developed a fully touch-screen control panel for its boats. It has an emphasis on enhancing

performances, functionality and safety on every boat. By constantly implementing new features, the company encourages its customers to buy new boats. All of this creates a brand differentiation within the performance sport boats segment.

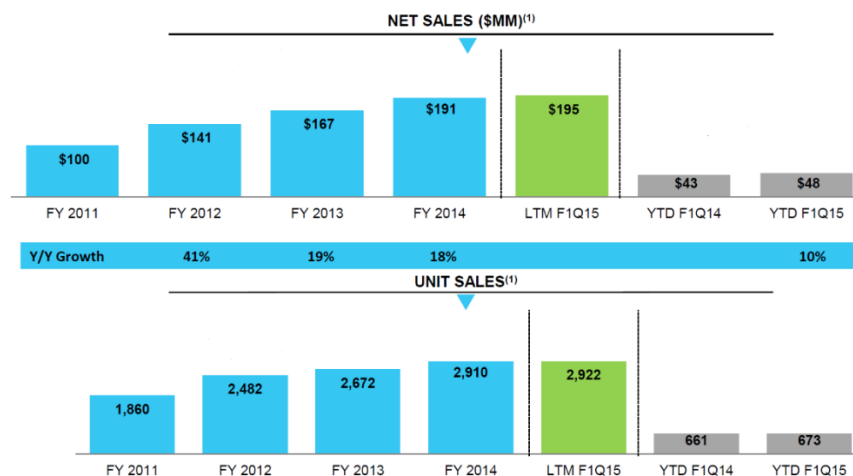
International expansion

The company currently has 52 international dealer locations in Europe, Asia, South America and Africa, which 12 were added in the past 4 years. In October 2014, Malibu finalized a deal to acquire all of the equity interests of its Malibu Boats licensee in Australia. CEO Jack Springer said that "the acquisition of our Australian licensed business represents an important next step in our international growth strategy". This acquisition is expected to generate \$8million in sales and \$1million in EBITDA with 180 units sold per year during the 2015 results. This acquisition is even more important since it will be the first manufacturing location of Malibu and Axis Boats outside of the United States. International expansion became a strategic priority for the company. Malibu Boats wants both to promote products in developed markets and penetrate developing markets, especially Asia, where people are not widely used to this kind of products.



The map above shows the worldwide market share of Malibu based on U.S. exports as of March 31, 2014. From what we can see, the company is the U.S. leader in PSB exports everywhere except in Europe. It is also the U.S. based leader in performance sport boats sales. They have 33% of the PSB U.S. exports market share. Nevertheless, international sales represented less than 5% of the total 2013 unit sales and were not a strategic priority for the company until recently. Malibu Boats recently expanded its direct coverage of important international markets to boost sales. The company is expected to target emerging market thanks to the entry-level Axis Wake Research boats, which are more affordable than Malibu Boats. The company made an important decision by targeting international expansion ahead of its American direct competitors.

Financials highlight



The two charts above represent the net sales and the unit sales of the company. We can see that net sales grew at a 24% CAGR from 2011 to 2014. In the same time Unit sales grew at a 16% CAGR during the same period. It means that the company has been able to generate more money from each boat sale. In 2011, Malibu Boats generated \$53,755 per boat sold. In 2014, their net sales per boat increased to \$65,613. Over the last twelve months this number is even expected to increase to more than \$67,000. It means that the company has been able to make economies of scale while selling more and more boats over the past 4 years.

| In Millions of USD | FY 2011 | FY 2012 | FY 2013 | FY 2014 | Current/LTM | FY 2015 Est | FY 2016 Est |
|-----------------------|------------|------------|------------|------------|-------------|-------------|-------------|
| 12 Months Ending | 2011-06-30 | 2012-06-30 | 2013-06-30 | 2014-06-30 | 2014-12-31 | 2015-06-30 | 2016-06-30 |
| Market Capitalization | -- | -- | -- | 222.4 | 331.2 | | |
| - Cash & Equivalents | -- | 14.8 | 16.0 | 12.2 | 12.0 | | |
| + Preferred & Other | -- | 0.0 | 0.0 | 8.8 | 11.4 | | |
| + Total Debt | -- | 21.2 | 23.6 | 0.0 | 20.0 | | |
| Enterprise Value | -- | -- | -- | 219.0 | 350.6 | | |
| Revenue, Adj | 100.0 | 140.9 | 167.0 | 190.9 | 206.8 | 224.0 | 247.8 |
| Growth %, YoY | -- | 40.9 | 18.5 | 14.3 | 26.3 | 17.3 | 10.6 |
| Gross Profit, Adj | 16.3 | 30.0 | 43.6 | 50.8 | 54.3 | 60.0 | 68.4 |
| Margin % | 16.3 | 21.3 | 26.1 | 26.6 | 26.3 | 26.8 | 27.6 |
| EBITDA, Adj | 7.4 | 18.7 | 25.8 | 33.9 | 35.5 | 41.6 | 48.9 |
| Margin % | 7.4 | 13.3 | 15.4 | 17.8 | 17.2 | 18.6 | 19.7 |
| Net Income, Adj | -0.5 | 11.2 | 18.1 | 13.3 | 13.8 | 23.1 | 29.0 |
| Margin % | -0.5 | 8.0 | 10.8 | 6.9 | 6.7 | 10.3 | 11.7 |

Indeed, the gross margin of the company has jumped from 16.26% in 2011 to 26.30% in 2014. The gross margin increased for several reasons. Malibu Boats used operating leverage, which means that the proportion of fixed costs increased and the proportion of variable costs decreased, which is good in the case of an increase in unit sales. The company has also increased its margins on boats options and features. In the same time, the EBITDA margin of Malibu Boats increased from 7.4% to 17.2% in the same time frame. Finally, net income margin jumped from -0.5% to 6.7%. All of these margins are expected to increase further at least during the next 2 years, even with a less important increase in revenues in 2016.



In the fourth quarter of their fiscal year 2014, Malibu Boats agreed to pay \$20 million in cash to settle an intellectual property rights lawsuit by Pacific Coast Marine. The settlement of this litigation generated a \$20 million debt increase, which was recorded as an abnormal loss. Otherwise, the company would have been debt free, which was the case since 2012. The management team has been able to repay all of the outstanding debt of the company, which accounted for about 50% of the equity in 2011 (at a time the company was not public, which means much lower equity). The current debt level only represents 6.65% of the market capitalization and 10.53% of the net sales. With more than \$12million in cash on hand and growing net income, the company will be able to repay this liability very soon. Finally, Malibu Boats targets a long-term revenues growth of 10%, a long-term EBITDA margin of 20% and a long-term EPS growth of 15%. It is much higher than most of the companies in the market and reflects the growing ambitions of the company.

Conclusion

Malibu is the industry leader in the sales of performance sport sports. The company has strong brand recognition and a competitive advantage over its competitors. The recent management team undergone changes that created value and enhanced efficiency of the company and created economies of scale. With an expected market recovery in the near future, the demand

for performance sport boats will increase. That is why the company will increase its production capacity by 50% within two years. The company will take advantage of this trend by developing new boats and by adding revolutionary features and options that will meet customers' expectations. At a current price of \$20.75, Malibu Boats is a BUY, with a target price of \$35.50.

Sources

Malibu Boats

Globenewswire

U.S. Security and Exchange Commission

Statistical Surveys

National Marine Manufacturers Association

Port Import Export Reporting Service

CENTER FOR GLOBAL FINANCIAL STUDIES

| Malibu Boats, Inc. | | Analyst GUILLAUME VALENTIN | Current Price \$20.75 | Intrinsic Value \$31.55 | Target Value \$35.50 | Divident Yield 0% | Target Return 71.07% | BULLISH | | | | | | | | | |
|---|--|--|---------------------------------|---|--------------------------------|---------------------------------|--------------------------------|-------------------|--|-------------------------|--|------------------------|--|-----------------------|--|---------|--|
| <u>General Info</u> | | <u>Peers</u> | <u>Market Cap.</u> | <u>Management</u> | | | | | | | | | | | | | |
| Sector Consumer Discretionary | | Brunswick Corporation \$4,888.99 | | Professional | | | | | | | | | | | | | |
| Industry Leisure Products | | Arctic Cat Inc. \$482.14 | | Springer, Jack Chief Executive Officer and Dires \$ 533,690.00 \$ 661,519.00 \$ 1,952,236.00 | | | | | | | | | | | | | |
| Last Guidance Feb-05-2015 | | LeapFrog Enterprises Inc. \$175.52 | | Wilson, Wayne Chief Financial Officer, Principa. \$ 297,902.00 \$ 371,442.00 \$ 1,264,752.00 | | | | | | | | | | | | | |
| Next earnings date 5/6/2015 | | Marine Products Corp. \$309.69 | | Anderson, Ritchie Chief Operating Officer \$ 310,849.00 \$ 300,084.00 \$ 1,121,051.00 | | | | | | | | | | | | | |
| <u>Market Data</u> | | Hasbro Inc. \$7,703.61 | | <u>Historical Performance</u> | | | | | | | | | | | | | |
| Enterprise value \$346.23 | | Mattel, Inc. \$8,642.39 | | <u>MBUU</u> | | <u>Peers</u> | | <u>Industry</u> | | <u>All U.S. firms</u> | | | | | | | |
| Market Capitalization \$933.35 | | Polaris Industries Inc. \$9,847.41 | | Growth | | Retention Ratio | | ROIC | | EBITDA Margin | | | | | | | |
| Daily volume 0.86 | | BRP Inc. \$2,509.41 | | 0.0% | | 0.0% | | 5.2% | | 35.6% | | | | | | | |
| Shares outstanding 15.61 | | MasterCraft Boat Company, LLC | | 0.0% | | #VALUE! | | 19.8% | | 11.8% | | | | | | | |
| Diluted shares outstanding 13.20 | | SA Catana Group \$19.51 | | 585.7% | | #VALUE! | | 10.1% | | 13.7% | | | | | | | |
| % shares held by institutions 77.02% | | <u>Current Capital Structure</u> | | #DIV/0! | | 1.55 | | 12.4% | | 18.5% | | | | | | | |
| % shares held by insiders 2.83% | | Total debt/market cap 5.78% | | 1.2x | | 1.09 | | 1.1x | | 2.4x | | | | | | | |
| Short interest 4.27% | | Cost of Borrowing 3.23% | | 7.4x | | 10.8x | | 12.1x | | 15.4x | | | | | | | |
| Days to cover short interest 9.94 | | Interest Coverage 2012.49% | | 7.8x | | 28.6x | | 26.8x | | | | | | | | | |
| 52-week high \$24.46 | | Altman Z 4.22 | | <u>Non GAAP Adjustments</u> | | | | | | | | | | | | | |
| 52-week low \$16.16 | | Debt Rating BAA | | 100% | | Straightline | | 10 years | | | | | | | | | |
| 5y Beta 0.00 | | Levered Beta 1.50 | | 100% | | Straightline | | 10 years | | | | | | | | | |
| 6-month volatility 33.86% | | WACC (based on market value weights) 10.13% | | 0% | | N/A | | N/A | | | | | | | | | |
| <u>Past Earning Surprises</u> | | <u>Proforma Assumptions</u> | | <u>Valuation</u> | | <u>Forecasted Profitability</u> | | | | | | | | | | | |
| | | <u>Period</u> | | <u>Rev. Growth</u> | | <u>Adj. Op. Cost/Rev</u> | | <u>NOPLAT</u> | | <u>Invested capital</u> | | <u>UFCE</u> | | | | | |
| Last Quarter 5.5% | | LTM | | 8% | | 82% | | \$206.84 | | \$17.74 | | \$66.23 | | -\$15.88 | | | |
| Last Quarter-1 0.0% | | LTM+1Y | | 11% | | 78% | | \$229.52 | | \$27.17 | | \$69.91 | | \$8.35 | | | |
| Last Quarter-2 2.2% | | LTM+2Y | | 8% | | 77% | | \$248.63 | | \$32.11 | | \$71.03 | | \$30.98 | | | |
| Last Quarter-3 0.3% | | LTM+3Y | | 7% | | 76% | | \$265.30 | | \$35.79 | | \$72.18 | | \$34.65 | | | |
| Last Quarter-4 0.4% | | LTM+4Y | | 6% | | 76% | | \$280.83 | | \$38.17 | | \$73.28 | | \$37.06 | | | |
| | | LTM+5Y | | 5% | | 76% | | \$296.07 | | \$40.25 | | \$76.47 | | \$37.07 | | | |
| | | LTM+6Y | | 5% | | 76% | | \$311.51 | | \$42.24 | | \$79.62 | | \$39.08 | | | |
| | | LTM+7Y | | 5% | | 77% | | \$327.42 | | \$44.28 | | \$80.56 | | \$43.34 | | | |
| | | LTM+8Y | | 5% | | 77% | | \$343.96 | | \$46.36 | | \$81.15 | | \$45.77 | | | |
| | | LTM+9Y | | 5% | | 77% | | \$361.25 | | \$48.50 | | \$82.82 | | \$46.83 | | | |
| <u>ROIC</u> | | <u>WACC</u> | | <u>EVA</u> | | <u>Enterprise Value</u> | | <u>Total Debt</u> | | <u>Other claims</u> | | <u>Equity</u> | | <u>Adjusted Price</u> | | | |
| LTM | | 10.1% | | \$23.97 | | \$533.06 | | \$20.00 | | \$16.09 | | \$496.97 | | \$32.51 | | | |
| LTM+1Y | | 10.3% | | \$20.74 | | \$557.19 | | \$20.00 | | -\$14.78 | | \$551.97 | | \$36.25 | | | |
| LTM+2Y | | 10.4% | | \$25.20 | | \$584.95 | | \$20.00 | | -\$51.97 | | \$616.93 | | \$40.37 | | | |
| LTM+3Y | | 10.5% | | \$28.73 | | \$610.83 | | \$20.00 | | -\$97.19 | | \$688.02 | | \$44.97 | | | |
| LTM+4Y | | 10.6% | | \$30.93 | | \$635.67 | | \$20.00 | | -\$147.36 | | \$763.03 | | \$49.84 | | | |
| LTM+5Y | | 10.7% | | \$33.78 | | \$663.19 | | \$20.00 | | -\$199.56 | | \$842.75 | | \$55.14 | | | |
| LTM+6Y | | 10.8% | | \$35.33 | | \$690.52 | | \$20.00 | | -\$255.63 | | \$926.15 | | \$60.34 | | | |
| LTM+7Y | | 10.9% | | \$35.95 | | \$718.17 | | \$20.00 | | -\$313.64 | | \$1,011.81 | | \$65.74 | | | |
| LTM+8Y | | 11.0% | | \$37.70 | | \$747.06 | | \$20.00 | | -\$362.91 | | \$1,089.97 | | \$70.68 | | | |
| LTM+9Y | | 11.1% | | \$40.24 | | \$776.61 | | \$20.00 | | -\$405.44 | | \$1,162.05 | | \$74.45 | | | |
| <u>Monte Carlo Simulation Assumptions</u> | | <u>Monte Carlo Simulation Results</u> | | | | | | | | | | | | | | | |
| | | <u>Base</u> | | <u>Stddev</u> | | <u>Min</u> | | <u>Max</u> | | <u>Distribution</u> | | <u>Intrinsic Value</u> | | <u>1y-Target</u> | | | |
| Revenue Variation | | 0 | | 10% | | N/A | | N/A | | Normal | | Mean est. | | \$32.51 | | \$36.25 | |
| Op. Costs Variation | | 0 | | 10% | | N/A | | N/A | | Normal | | σ(e) | | \$0.32 | | \$0.25 | |
| Market Risk Premium | | 6% | | N/A | | 5% | | 7% | | Triangular | | 3 σ(e) adjusted price | | \$31.55 | | \$35.50 | |
| Long term Growth | | 5% | | N/A | | 3% | | 6% | | Triangular | | Current Price | | \$20.75 | | | |
| Terminal Value | | 0 | | 0.1 | | N/A | | N/A | | Normal | | Analysts' median est. | | | | \$26.33 | |