

Company Description:

Ducommun is a global provider of manufacturing and engineering services, developing innovative electronic, engineered and structural solutions for complex applications in aerospace, defense and industrial markets. Our full-service collaborative approach, broad capabilities and value-added services like new product introduction, supply chain strategies and program management deliver value for our customers and innovative solutions for their complex electronic and structural needs.

BUY

Current Price: \$36.93

Target Price: \$42.12

Market Cap: 0.4211 M



Key LTM Data		
	DCO	Peers
NOPAT Margin	3.84%	5.40%
Adj. NI Margin	2.57%	1.25%
ROIC	3.82%	22.51%
ROE	3.82%	-28.15%
Total Debt/Capital	35.44%	8.88%
Kd	5.06%	5.00%
Default Rating	1.38%	0.17%
Ke	12.10%	12.46%
WACC	7.68%	11.67%

Thesis:

The aerospace and defense market is not looking to slow down. With current administration and a larger defense budget, improvement are always looking to be made. While Ducommun will not revolutionize the industry at less than a billion dollars of market cap, they hold a prime spot in this industry. Ducommun understands this and has leveraged their company in order to take full advantage of an expanding market. Moving forward, Ducommun will see a steadily growing revenue flow and increased efficiencies with newly acquired companies which will create value for DCO.

Catalysts:

- Short Term: 2018 Q3 Revenue announcement
- Midterm elections and political landscape until 2020
- Ducommun's customer's growth and their ability to reduce capex while maintaining steady growth

Earnings Performance:

In 2015, due to a shrinking outlook on defense, the aerospace industry took a hit and DCO went down with it. They are heavily reliant on Boeing and Airbus as their main source of revenue and in a receding industry, larger companies were not pushing growth and expansion which hurt DCO. However, they have been rebounding and fueling a new growth due to an expanding market. They have made several cuts to their business lines, focusing on a core model which helped them cut out underperforming segments. They recently acquired Certified Thermoplastics to expand on their end line market. They have specialized resin material that has a wide range of aerospace applications. CTP has expanded their market portfolio and has increased revenues with their proprietary capabilities. This was shown as the merger went through in late April of this year and the earnings for that quarter had already beat expectations. This should be expected to continue, especially as they have made such large Capital expenditures, investing in the business to allow for organic growth of the new segment. Also looking at their growth in Net Income, the company has positioned itself well to see a significant bottom line increase due to their financial leverage. To date, Ducommun has provided an astounding bounce back and looks to continue revenue growth and see positive changes to net income in years to come. As the table above shows, a 1.4%v increase in revenues was shown during a year with 12.7% growth in Market Cap. In the last twelve months a 6.1% growth in revenue led to a 30.6% increase in Market cap. DCO needs revenue to thrive in their industry. Lucky for them the political party in power favors a strong military which will benefit the company, and major consumers of DCO's products including Boeing and Airbus are showing similar growth which can only mean good things for Ducommun.

DCO US Equity		9% Actions		9% Export		9% Settings		Financial Analysis	
ADJ Ducommun Inc		Periodicity		Annuals		Cur		USD	
Key Stats		T/S		B/S		C/F		Ratios	
Segments		Addt		ESG		Custom			
10 Adj Highlights		12 GAAP Highlights		13 Earnings		14 Enterprise Value		15 Multiples	
16 Per Share		17 Stock Value							
In Millions of USD		2014 Y		2015 Y		2016 Y		2017 Y	
12 Months Ending		12/31/2014		12/31/2015		12/31/2016		12/31/2017	
		Current/LTM		2018 Y Est		2019 Y Est			
		06/30/2018		12/31/2018		12/31/2019			
Market Capitalization		276.9		179.8		286.1		322.4	
- Cash & Equivalents		45.6		5.5		7.4		2.2	
+ Preferred & Other		0.0		0.0		0.0		0.0	
+ Total Debt		290.1		245.0		166.9		216.1	
Enterprise Value		521.3		419.4		445.6		536.3	
Revenue, Adj		742.0		666.0		550.6		558.2	
Growth %, YoY		0.7		-10.2		-17.3		1.4	
Gross Profit, Adj		140.3		100.8		106.2		102.8	
Margin %		18.9		15.1		19.3		18.4	
EBITDA, Adj		80.8		43.8		52.8		55.1	
Margin %		10.9		6.6		9.6		9.9	
Net Income, Adj		18.2		8.1		14.7		14.4	
Margin %		2.5		1.2		2.7		2.6	
EPS, Adj		1.64		0.74		1.31		1.25	
Growth %, YoY		11.8		-55.1		77.5		-4.4	
Cash from Operations		53.4		23.7		43.3		35.4	
Capital Expenditures		-18.1		-15.9		-17.0		-87.4	
Free Cash Flow		35.3		7.8		26.3		-52.0	

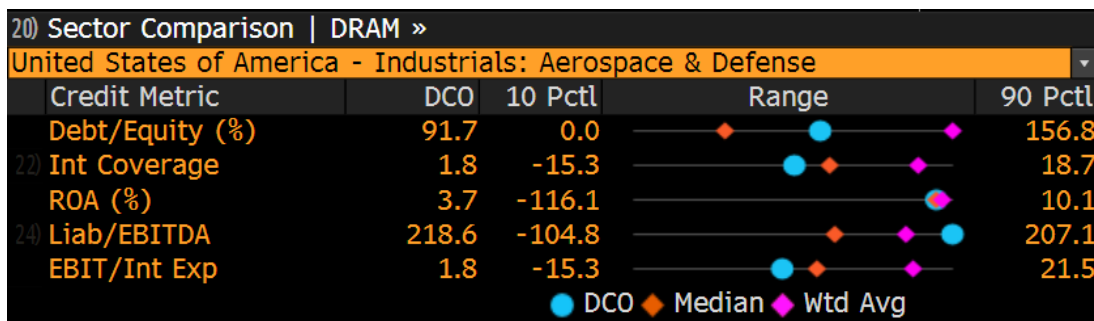
Cost of Capital:

An important aspect to look at when accessing DCO is their capital structure which sits at 53% debt and 47% Equity. While this may seem troubling for

	Adj. Market Value	INT	Maturity (years)	Implied Cost	Tax Rate	Weights
DEBT	\$475.00	5.06%	1.65	5.06%	21.31%	53.01%
PREF	\$0.00	0.00%		0.00%		0.00%
MI	\$0.00			11.42%		0.00%
Equity	\$421.06			11.417%		46.99%
WACC				7.475%		

a small company, you must first look at industry norms. This level of debt is concerning, but they have managed it well, and have kept a relatively low WACC.

The diagram below shows a sector comparison for DCO's debt. The orange mark is the industry median, which DCO fits into, with it's only outlier being Liabilities / EBITDA. This should come as a relief to some skeptical investors because aerospace is a specific industry that requires substantial financing to undergo capital projects. As a measure of interest coverage they are right about at the median, which shows that even though they have taken on debt, they haven't moved to junk ratings because this is an industry standard.



ROC and ROIC:

Ducommun has simply not been as effective in years past as it's primary competitors have been. With that being said, Ducommun has pushed past competition in the past 12 months. This was fueled by new management and several investor friendly projects that have lead to innovative, and value creating segments for DCO. If you look at the first diagram NOPAT / Invested Capital is at 7.3%. We have already looked at the amount of money DCO is dumping into their company, so this shows how their after tax profit has

ROIC/WACC Decomposition		
ROIC (NOPAT/IC)		
	History	LTM
DCO	4.6%	7.3%
Competitors	5.3%	6.8%
Target	6.7%	

soared to keep the measure so high. DCO however does not have to continue high priced investments and acquisitions to create value. They will do so by working with suppliers and consumers to provide a better supply chain process and a more stable one, Both which will benefit investors.

The next diagram shows ROC/WACC. This number is 0.8 which will not necessarily good for DCO, is better than it has been in years past. Over double. The last twelve months has shown a significant increase in the return on their capital and they haven't had a significant increase in their WACC that would take away from this. I know the hardest part to see about the potential in this company is their amount of debt, but every metric I have shown supports the fact that DCO has been responsible with their debt. And that they know how to handle the industry that demands risk in the form of financial leverage in order to be able to sustain themselves.

ROC /WACC		
	<i>History</i>	<i>LTM</i>
DCO	0.39	0.80
Competitors	0.61	0.65
Target	0.73	

Macro Outlook:

This section is one that holds substantial value in the valuation of Ducommun. They are influenced heavily by external factors that impact their customers, but also the industry as a whole. The good news is that war and defense budget increases do not seem likely to slow down soon, so Ducommun is ready to make the most of a favorable market. A key element though is that I believe with their growth potential and quality leadership Ducommun is severely undervalued currently. There is growth potential, especially if the past 12

months is any indicator of the new DCO. They have improved margins and their bottom line and look to make their operations efficient moving forward which will benefit the company.

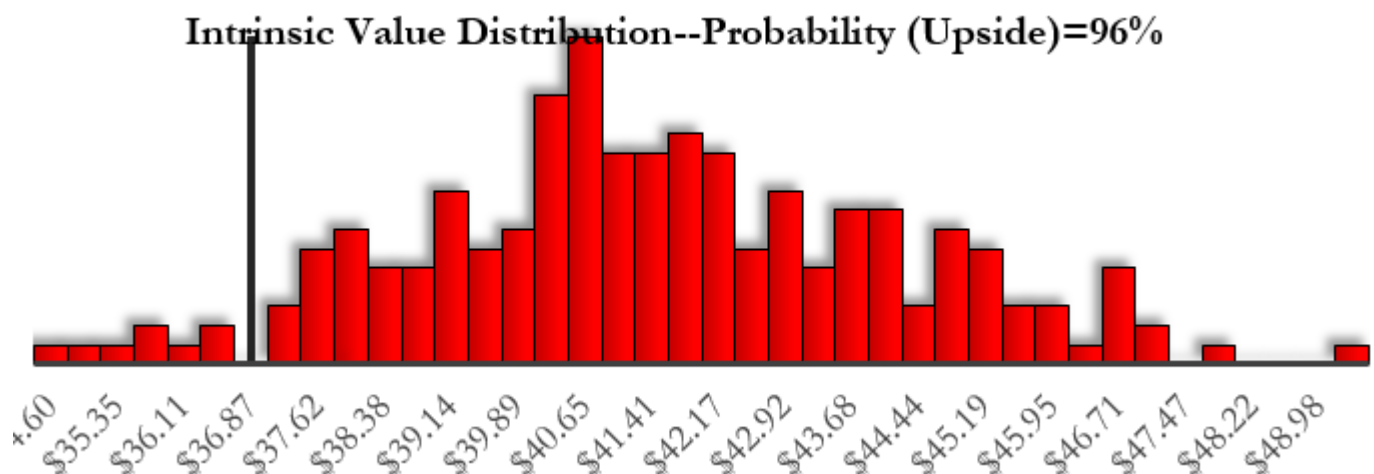
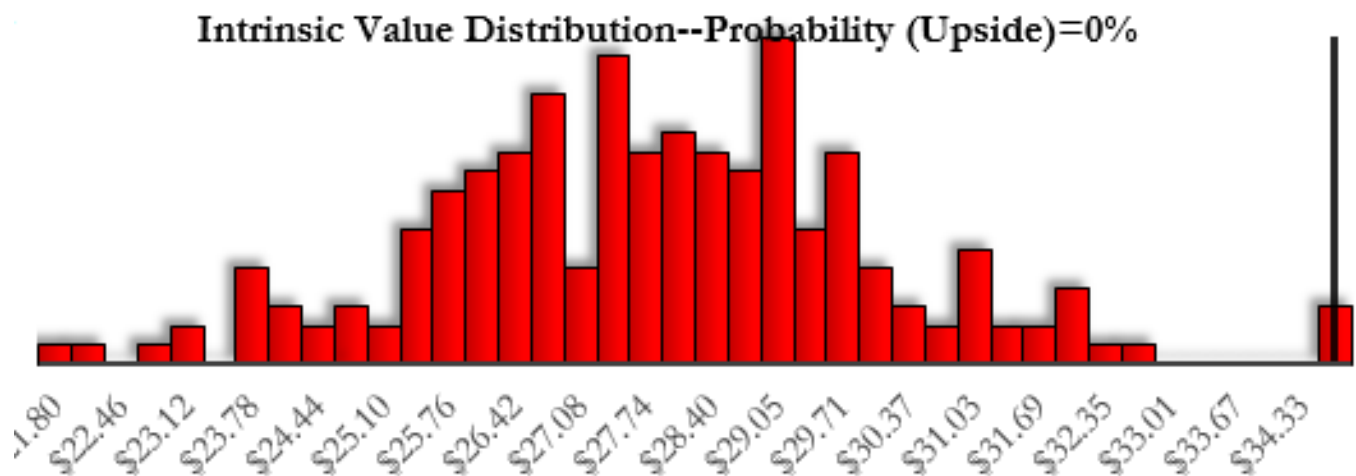
Revenue, Adj	742.0	666.0	550.6	558.2	586.2
Growth %, YoY	0.7	-10.2	-17.3	1.4	6.1
Gross Profit, Adj	140.3	100.8	106.2	102.8	110.5
Margin %	18.9	15.1	19.3	18.4	18.8
EBITDA, Adj	80.8	43.8	52.8	55.1	54.8
Margin %	10.9	6.6	9.6	9.9	9.3
Net Income, Adj	18.2	8.1	14.7	14.4	18.9
Margin %	2.5	1.2	2.7	2.6	3.2
EPS, Adj	1.64	0.74	1.31	1.25	1.63
Growth %, YoY	11.8	-55.1	77.5	-4.4	20.9
Cash from Operations	53.4	23.7	43.3	35.4	45.4
Capital Expenditures	-18.1	-15.9	-17.0	-87.4	-106.0
Free Cash Flow	35.3	7.8	26.3	-52.0	-60.6

Conclusion:

I believe that for all of the reasons stated above there is substantial grounds for justification in the intrinsic value of the company. However, I ran two other scenarios, one in which revenues were ran at a continuing period assumption starting in 2019. This rate was a 2.5% growth in revenues year over year which led to an estimated target price in one year of \$31.16. I also ran a bull case wear macro trends continued to favor the industry, possible if certain leaders are reelected in 2020, which would favor the continued expansion in aerospace and defense. This stated a similar 5 year revenue growth as my base case did, but growth was higher in later years to reflect the prolonging of a low, but higher than GDP revenue growth.

The discount rate and revenues play a big factor in the pricing of DCO. With that being said, they have taken on the appropriate amount of debt for the industry and they show promising prospects to increase revenues year over year.

Buy DCO.



Ducommun Incorporated

(DCO)

CENTER FOR GLOBAL FINANCIAL STUDIES

NEUTRAL

Analysis by Zachary Girvin
11/21/2018

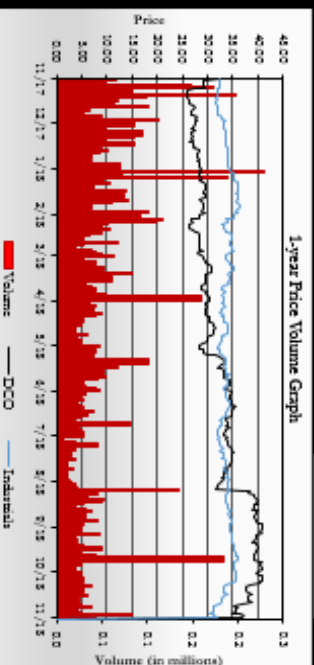
Current Price:
Dividend Yield:

\$36.33
0.0%

Intrinsic Value:
Target Price:

\$37.57
\$42.12

Target 1 year Return: 14.07%
Probability of Price Increase: 72%



Description	
Ducommun Incorporated provides engineering and manufacturing products and services primarily to the aerospace, defense, industrial, natural resources, medical, and other industries in the United States.	
General Information	Industrial
Sector	Aerospace and Defense
Industry	May 8, 2018
Last Guidance	November 5, 2018
Next earnings date	Market Assumptions
Estimated Equity Risk Premium	6.36%
Effective Tax rate	21%

Market Capitalization	\$42,106
Daily volume (mil)	0.02
Shares outstanding (mil)	11,440
Diluted shares outstanding (mil)	11,558
% shares held by institutions	57%
% shares held by investment managers	67%
% shares held by hedge funds	12%
% shares held by insiders	8.53%
Short interest	0.67%
Days to cover short interest	2.27
52 week high	\$41,140
52 week low	\$25.06
Volatility	43.08%

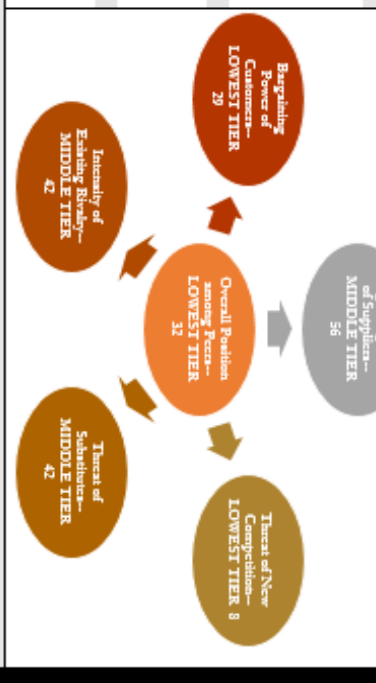
Quarter ending	Past Earnings Surprises
7/1/2017	Revenue
9/30/2017	1.73%
12/31/2017	-2.79%
3/31/2018	-2.11%
6/30/2018	5.21%
Mean	4.26%
Standard error	1.26%
Management	10%

EBITDA	-7.67%
Recommendation (STARS) Value--0	-10.87%
Recommendation (STARS) Description--0	-41.33%
Quality Ranking Value--C	-0.82%
Quality Ranking Description--Lowest	19.56%
Short Score--0	-8.23%
Market Signal Probability of Default % (Non-Ratings)--1.38%	
CreditModel Score (Non-Ratings)--b+	

Position	Total Compensation Growth
Chairman, President & CEO	0% per annum over 5y
VP, CFO & Treasurer	-5.33% per annum over 4y
Senior VP of Operations & Head of Ducommun	-5.28% per annum over 3y
VP & Chief Human Resources Officer	11.78% per annum over 5y
VP, Controller & Chief Accounting Officer	
Vice President of Strategy & Business Develop	

Stock Price Growth During Tense	Peers' Median (LTM)
6.73%	8.94%
0.76	7.1%
4.3%	1.46
Peers' Median (LTM)	6.8%
26.7%	51.0%
15.5%	0.16
Peers' Median (LTM)	5.0%
1.8%	10.1%

Profitability	DCO Historical	Peers' Median (LTM)
Return on Capital (GAAP)	7.3%	4.56%
Operating Margin	7%	4.43%
Revenue/Capital (GAAP)	1.07	1.03
ROE (GAAP)	7.3%	8.2%
Net margin	2.8%	2.3%
Revenue/Book Value (GAAP)	2,606,348.12	2.86
Invested Funds	DCO (LTM)	Peers' Median (LTM)
Cash/Capital	0.2%	4.7%
NWC/Capital	28.2%	27.8%
Operating Asset/Capital	45.2%	42.5%
Goodwill/Capital	26.4%	25.6%
Capital Structure	DCO Historical	Peers' Median (LTM)
Total Debt/Market Capitalization	0.43	0.57
Cost of Debt	5.5%	7.8%
CGFS Rating (F-score, Z-score, and default Probabi	CCC	CCC
WACC	7.2%	9.2%



Forecast Assumptions	Explicit Period (10 years)	Continuing Period
Revenue Growth CAGR	4%	2.5%
Average Operating Margin	12%	12%
Average Net Margin	6%	7%
Growth in Capital CAGR	6%	3%
Growth in Claims CAGR	0%	3%
Average Return on Capital	7%	6%
Average Return on Equity	3%	6%
Average Cost of Capital	7%	8%
Average Cost of Equity	10%	10%

