Macroeconomic Overview

U.S. Markets

The past trading week was characterized by two distinct parts, with the major indices logging minor losses until Thursday morning, followed by a fierce end-of-week rally that pushed equities 2% higher on average. The biggest gains were recorded by the NASDAQ Composite, which gained 1.14% over the week to settla at $4,886.89 and remains the only major equity index in positive year-to-date territory. The S&P 500 finished the week 0.9% higher at $2,033.11, after closing under the key 2,000 level on Wednesday. The DJIA posted a minor gain of 0.78% and the Russell 2000 Index of small cap stocks was the biggest laggard with a loss of 0.27% over the past five days. The VIX Index of volatility recorded a third week of consecutive declines, losing 11.89% last week and 36.28% over three weeks. Gold settled 1.8% higher at $1,177.30 an ounce, while silver gained 1.3% to close at $16.05 an ounce. Crude oil gave back most of its gains from the previous weeks, with the barrel of WTI finishing the week 4.78% lower at $47.26, after briefly crossing the $50 threshold on Monday. The trading week was marked by several subpar economic releases, with disappointed retail sales dragged down by low gas prices released on Wednesday. September CPI data was released on Thursday and was once again dragged down by low energy prices, with a decrease of -0.2% over the previous month but an increase of 0.2% when excluding food and energy prices, meeting analyst consensus. Industrial production also fell for a second consecutive month in September, with a decrease of -0.2% which still beat the consensus calling for a -0.3% decline. Thursday's positive note was the weekly jobless claims report, which established a new historical low with new claims down 7,000 to 255,000, widely beating the consensus by 15,000. On Friday, the preliminary Consumer Sentiment Index was released for the month of October and showed a large increase from 87.2 to 92.1, beating the consensus of 89.5. In corporate news, Dell and AB Inbev (BUD) announced two major mergers last week for a total of $171 billion. The former will acquire data-storage firm EMC for $67 billion or a 28% premium, while the latter finally obtained approval from SABMiller for its third merger offer, worth $104 billion or £43.50 per share. The price represents a 44% premium over SABMiller's market value before news of an offer first surfaced. The week was also characterized by a flurry of earnings, notably from America's largest employer Wal-Mart (WMT), which issued a worrying guidance for its FY2017 EPs guidance and caused the forecasts for the entire industry to plummet. Many financial companies reported earnings last week, with Wells Fargo (WFC), Bank of America (BAC) and JPMorgan (JPM) all beating earnings estimates. Shares of Netflix (NFLX) lost 8.29% after the company announced weaker than expected subscriber growth guidance. Several economic reports are due next week, with the October Housing Market Index on Monday, September Housing Starts on Tuesday and September Existing Home Sales on Thursday, which are expected to confirm the strength of the U.S. housing market.

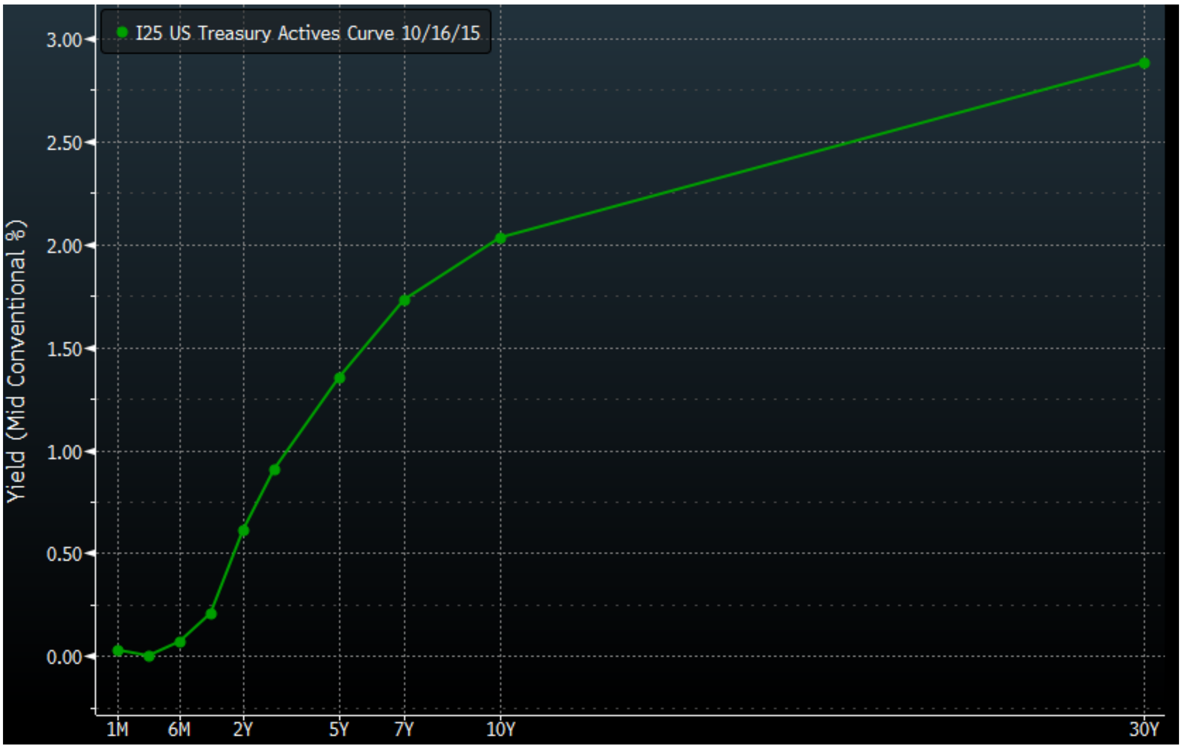
Index	Weekly % Change	YTD % Change
S&P 500	+0.9%	-1.25%
Dow Jones Industrial	+0.78%	-3.41%
NASDAQ Composite	+1.14%	+3.18%
Russell 2000	-0.27%	-3.52%
VIX	-11.89%	-21.61%

International Markets

International equity markets followed the same pattern as their American counterparts last week, with an early-week selloff that turned into a rally on Thursday. However, European equities recorded smaller increases, with the Bloomberg European 500 and Stoxx Europe 600 indices recording gains of 0.18% and 0.09% respectively, while the MSCI Emerging Markets Index gained 1.29%. The lack of strength in international markets might be due to several negative figures that were released during the week, such as weaker than expected Chinese imports and CPI data, slowing European inflation and industrial production, and a sharp decline in the German ZEW Index of Consumer Sentiment attributable mainly to the Volkswagen (VLKAY) emissions fallout. The markets are also preparing themselves for the Monday release of Chinese GDP growth, retail sales and industrial production reports, all expected to confirm the trend of slowing growth in China. Chinese equity markets experienced another week of turbocharged gains, with the Shanghai Composite and Shenzhen Composite gaining 6.54% and 8.57% respectively.

Bond Report:

This week, yields have reached their lowest level in five months. Indeed, the weak economic data provided by the government made investors more confident that the FED will not raise their interest rates before 2016. Indeed, last week release brought doubt about whether inflation will increase enough for the FED to raise its interest rates. According to the CME Group's FedWatch tool, the probability for the FED to increase its rates in October in 6% and 31% in December; This assumption had increased investors' demand for government debt. If we take a look at the two-year maturities, it goes from 0.65% last week to 0.61% this week. The 10-year Treasury note finish the week at 2.03% after falling to its lowest level since April 28 earlier this week. The 30-year edged 0.4 bps to 2.87%.



<u>What's next and key earnings:</u>

On Monday October 19th, the Housing Market index will be released. It is expected to remain at a consensus of 62 as the previous month. The housing supply is low and the low interest rates are two factors that can motivate builders.

On Tuesday October 20Th, the Housing starts indicator will be released. It is expected to increase by 2.0% for the months of September after a decline of 3.0% in August. The main focus will be on whether construction is up for multi-families home where housing permits increase drastically by 3.5% in August.

On Wednesday, October 21st , The EIA Petroleum Status report will be released. This report provides weekly data on the petroleum inventories in the US. This number helps to determine prices of petroleum product.

On Thursday October 22nd, the jobless claims will be released. It is expected to rise to 265,000 in the October 10 week, after reaching last week 255,000, its lowest level in 42 years. On the same day, the Existing house sales report will be released. It is expected to increase by 0.8% for the month of September after a severe drop of 4.8% in August. Finally, The Chicago FED National Activity Index will be released. This is used to measure both the general economic activity and the inflationary pressure. It is expected to reach a consensus of minus 0.05 for the month of September, which is almost at the average growth in the month.

On Friday October 23rd, The PMI Manufacturing Index Flash will be released. Historically, it has been remaining above the breakeven of 50 because of the weak international demand and overall caution among customers.

IRIDEX Corporation

NasdaqGM:IRIX

Analyst: Coralie Cornern
Sector: Healthcare

BUY

Price Target: $12.29

Key Statistics as of 10/15/2015

Market Price:	$8.13
Industry:	Medical Appliances & Equipment
Market Cap:	$81.19 M
52-Week Range:	$6.41-11.28
Beta:	0.68

Thesis Points:

- Ophtalmology is a growing market
- Strong financial position, low debt and share repurchase program
- Overreaction to previous quarter poor performance

Company Description:

IRIDEX Corporation was founded in 1989 and is headquartered in Mountain View, California. The company develops, manufactures, markets, sells, and services medical laser systems and associated instrumentation for the treatment of the sight-threatening eye diseases. IRIDEX also operates for the otolaryngology market with its laser systems to perform stapedectomy. The company offers a wide variety of laser consoles, and ophthalmic delivery devices. They serves ophthalmologists, research and teaching hospitals, government installations, surgical centers, hospitals, and office clinics. Their equipment helps treating very common yet fatal human (and animal) disorders such as glaucoma or Diabetic Macular Edema or all other kind of retinal diseases. IRIDEX also provides solutions to enhance physicians' performance and results on patients. It sells and markets its products through a direct sales force in the United States, as well as through independent distributors internationally. The company was formerly known as IRIS Medical Instruments, Inc. until they went public in 1996.

Thesis

IRIDEX Corporation is among the leading companies in terms of developing, manufacturing, and marketing laser based medical systems. After selling its aesthetics business to Acera in 2012 for approximately $5.1 million, IRIDEX strategy is to focus solely on its ophthalmology business which is the company's core strength as the firm managed to generate net income from its ophthalmology operations in each of the past five years. Ophthalmology is a growing market mainly due to the aging of the population but also due to the widespread of obesity that leads to diabetes. Diabetes causes several eye diseases such as Diabetic Retinopathy, Diabetic Macular Edema (DME) but also cataract and Glaucoma. These diseases are mostly non curable but treatable. This means that people who have glaucoma are going to be treated their whole life. It also mean that demand for IRIDEX laser products is very unlikely to fall. Except for the last quarter, the company is showing growth. As of July 2015, the company recorded $12.2 Million in cash, with a total of $31.9 Million in current assets. The liabilities are $7.9 Million and has almost no noncurrent liabilities ($0.9Million), which leaves IRIDEX room to grow. Moreover the 8.27% Return on invested capital, which is higher than the company's Weighted average cost of capital (8.17%) shows that IRIDEX is creating value. The biotech is currently undervalued after a stock price drop in July due to disappointing earnings. Indeed, net loss for the second quarter of 2015 was $700,000 compared to the prior year period. This decrease is not due to a fall in demand but to supply chain difficulties.

A buy of IRIDEX Corporation is therefore recommended with a one-year target price of $12.29. Currently trading at $8.13, it has an upside potential of 51.16%.

Product Mix and Diversification

IRIDEX Corporation is providing products to healthcare professionals. Although they are mainly producing for the ophthalmology market, they respond to two different needs. On one side they have laser delivery devices, which are used to optimize physicians' view and maximize therapeutic capabilities. These are called consumables and account for 60% of the company's revenue. Those lasers are high quality premium products, of which prices are not public and need to be inquired. William Moore, CEO of the company actually declare that IRIDEX was currently shaping their business model to increase the sale of consumables. On most of these lasers, the MicroPulse™ technology, for which they were granted a US patent in 2010 is incorporated. "MicroPulse allows the tissue to cool between laser pulses, minimizing or preventing tissue damage. Treatment risks are reduced or eliminated, with increased patient comfort than with conventional, continuous-wave laser treatment." IRIDEX also sells laser devices which are surgical instruments used to treat patients directly rather than just improving their diagnostic or treatment. These are durable delivery devices and account for the remaining 40% of the revenue stream. One of their best and highest level surgical probe is the Adjustable and intuitive XR probe, that provides full coverage of peripheral retina without removing probe from the eye. Other than this one they have seven other different kinds of retinal surgical probes.

In the latest news, the company announced on October 6th that they added a new eye pressure diagnostic device to their portfolio called tonometer, designed specifically for glaucoma. They partnered with Revenio Group, the corporation who invented the tonometer to ally the tonometer, which monitors intra-ocular pressure to their Cyclo G6 to create a minimally invasive approach of slowing the disease down, it also includes the MicroPulse Technology. Sixty million people are afflicted with glaucoma worldwide so being able to sell this brand new effective and durable option to treat glaucoma is going to add to the company's competitive advantages. Indeed, following the first results shown patients tested with G6, the results were amazing. A woman was tested in Ohio with an intra-ocular pressure (IOP) of 38 and a massive pain, taking heavy medication. After being treated with G6 IOP reduced to 23 in the first day and she felt much better and was reduced of pain from the pressure in her eye. Doctors are also witnessing improvements in their success rate in IOP reduction. The Cyclo G6 system is definitely a growth catalyst. During the last earning call, IRIDEX' CFO and COO mentioned that a new glaucoma probe with illumination

(Containing illumination fiber) was currently sitting with the FDA. It is quite hard to forecast how long the process is going to take but as they are just waiting for the clearance from the illumination concept, managers are believing they could get it shortly. This could again be a catalyst for revenue's growth.

Other than its wide range of ophthalmologic consumable and surgical instrument, IRIDEX offers two different types of ENT lasers that many otologists in the United States use to perform stapedectomy. Finally, IRIDEX offers a range of ophthalmoscopes, probes, and other laser devices to treat animal eye disorders.

Most of IRIDEX' devices are patented. The patents' carrying value as of January 2015 was $120 thousand. The company logically relies on a combination of patents, trade secret, copyright and other intellectual property contracts to remain competitive.

Porter's Five Forces

The bargaining power of suppliers can be classified as relatively high. IRIDEX Corporation has reliable sources in their supply chain, however, since they operate in a very specific area of the healthcare sector, it is not easy to switch suppliers. The problems the company had in its supply chain during Q2 are relatively frequent for this kind of manufacturing companies and can be solved by hiring engineers and experts in the particular field to detect and solve the problem.

The bargaining power of customers on the other hand is low. IRIDEX has the competitive advantage to offer very high quality products, either consumable or durable, that are better than what the competition is offering. Some of their products, such as the Cyclo G6 are unique, the MicroPulse technology also is patented and IRIDEX is the only company to offer this technology. The company does not have to fear a loss in customer numbers, but should rather expect an increase since Cyclo G6 is only at its debut.

The threat of new competitors is low. IRIDEX Corporation holds patents that will protect their products and technologies. The barriers to entry as well as the learning curve are high in the ophthalmology lasers sector. Potential competitors would spent tremendous amount of time and money trying to compete with products such as Cyclo G6 or technologies such as MicroPulse.

The threat of substitute products is extremely low. Today, physicians are willing to use the best technology to better treat or easily diagnose their patients. There is for now no substitutes to retinal surgical instruments or laser delivery services. The only real danger would be another company coming up with a cure for glaucoma.

Management

IRIDEX Corporation is managed by William Moore than serves as Chairman of the board of directors but also as CEO and President of the company. Mr. Moore also currently serves on the board of directors of Natus Medical Incorporated, a public company he co-founded in 1990 and for which he served as CEO until 1993. Natus is also in the Medical Appliances & Equipment industry but does not work for the ophthalmology market. William Moore started as a President of IRIDEX in 2007 and has a very broad and extensive experience in the healthcare sector. However it never is optimal to have the same person, regardless of his or her experience, serving different positions. In this case, William Moore widely contributed to the growth of the company. Since he was appointed CEO in 2012, profit margin rose from 7% to 23% in the period ending in January 2015. Moreover, investors very much like Moore's input in the company and its future strategy of a heavier mix on the consumables to capital equipment. In the last earnings call William Moore announced that the CFO of the company, James Mackaness was resigning. He added that the individual took part in creating tremendous value for the company's shareholders, and that he would continue to serve in the CFO/COO role until the end of August. Even though the CEO mentioned in August that the company was already searching for a world class CFO to "fill Mackaness' shoes", there still has not been any announcement about a new CFO joining the company. As of today, the company's management structure is worrying. Still, there has not been any major stock price decrease since the CFO left the company and the company anticipates an increase in sales for the next quarter and re confirmed its strategy of increasing margins.

Financials

Revenues were 42.8 million in 2014, representing a growth of 12% from 38.03 million in FY 2013.
Gross Margin slightly improved to 50.00% from 48.50% in FY 2013, while the Net Profit margin sky rocketed from 5.83% to 23.45% at the end of 2014, which is partly due to tax benefit.
Similarly to 2013, IRIDEX had $13.30 million cash on hand in 2014 which, secures reserves for future acquisitions (especially patent acquisition) and other growth opportunities. It will also be used for the company's repurchase of its stocks.
IRIDEX has almost no debt, their debt to equity ratio is 0.09x which grants the company an AAA rating as there is absolutely no risk that they will not be able to pay interest payment.
Before the deceiving second quarter of 2015, IRIDEX had ten previous quarters of record revenues. This is actually why the company decided to address the quality issues by reducing the production. Even though gross margin decreased 330 basis points in Q2 2015 compared to Q2 2014, there are opportunities for margins improvement now that the supply chain issue has been addressed and the consumable sales associated with the launch of the new Cyclo G6 system will start kicking in.

Overreaction to Q2 earnings

Since the last earning calls on the 8th June, IRIDEX Corporation's stock price declined by 9% from $8.70 to the current price of $8.13. The stock dropped to $6.51 before the Cyclo G6 was announced, but its price started to increase again right after the announcement. The Q2 disappointing results that led the stock price down were only due to supply chain issue, but not at all about demand as the company's CEO mentioned several times during the earning call. More precisely, there were issues with RFID antenna, a software glitch and a small motor malfunction. The company hired professional to address those issues and then implemented additional quality controls. William Moore is pretty confident that these kind of problems will not arise again. The market overreacted to Q2 results even though the demand for IRIDEX products was not impacted and competitors did not take business away from the company. Additionally, these kind of slight issues can often happen to manufacturing businesses without destroying value. The undervaluation of the stock added to the $12.2 Million in cash gave the opportunity to management to start a massive repurchase program.
They are planning on repurchasing up to $2 million worth of the company's common stock over the next 12 months.

Valuation

The valuation of IRIDEX Corporation is based on a proforma that values the company with a discounted cash flow model and focus on the company's return on invested capital. A summary of the outputs of the valuation is attached to this report and can be found on the last page. A 0.5% premium has been added to the market risk premium consisting of market premium and country risk premium. This 0.5% premium accounts mainly for the small chance of finding a durable cure to retina disease and especially glaucoma.
When valuing IRIDEX Corporation, a slow decay growth rate has been utilized to determine the speed of reversion toward long term stability as the company, together with the ophthalmology market is unlikely to quickly reach long term stability. There is not any analysts' estimates concerning IRIDEX growth but there are other appropriate way of predicting growth: The revenue growth rate for FY 2016 is based on the growth rate in the market for medical lasers, and is an adjusted average of market predictions. In the following years revenue growth has been set to decline year-over-year to reach a revenue growth for the long-term of 3%. Both Net and NOPAT margins are due to increase in the future. From 8.00% to 15.50% and 6.2% to 7.2% respectively in the long term. This seems logical as the company's strategy is to increase margins by 55% at least by using volume and cost reduction drivers but mainly by focusing their sales on consumables that carry better margins.

The below ratios further proves that IRIX is undervalued. The company is traded at lower levels than its competitors.

	IRIX	PEERS	Δ
EV/REV	1.67x	1.82x	8.74%
P/BV	1.50x	2.01x	33.81%

Finally, the Debt to Equity ratio impact on weighted average cost of capital is the same at the end of the explicit period than during the continuing period (8.4%) which shows very smooth and healthy growth. Following the assumptions used in the valuation model, the stock has an upside potential of 51.16% with a one year target of $12.29.

Summary

The recent decline in stock price caused by negative results in Q2 led IRIDEX Corporation's stock to be undervalued. The stock proves to be a good investment as the market for ophthalmology is definitely growing. The investment has more upside than downside risk.
Moreover, IRIDEX Corporation has a healthy balance sheet, without debt, and capital available in order to further invest into the company. The cash available was also used by the company to repurchase large amount of their stocks, due to their current undervaluation. The company plans to further grow the margins but also further invest in innovation and if opportunities come up, in small acquisitions, technology investments and strategic relationships, or improve the pricing of the company's products. In the short-term, revenue, margins and stock price should be driven up by Cyclo G6 sales.

Sources:

- IRIDEX Corporation, 10-K
- Yahoo Finance
- Capital IQ
- Bloomberg
- http://www.IRIDEX.com/
- Seeking alpha
- Bbcresearch.com
- Strategy.com

CENTER FOR GLOBAL FINANCIAL STUDIES

IRIDEX Corporation	irix	Analyst	Current Price	Intrinsic Value	Target Value	Divident Yield	1-y Return: 51.16%	BULLISH
		Coralie Cornern	$8.13	$11.08	$12.29	0%		

General Info		Peers	Market Cap.
Sector	Healthcare	Ellex Medical Lasers Limited	$52.75
Industry	Healthcare Equipment and Supplies	MGC Diagnostics Corporation	$29.36
Last Guidance	August 6, 2015	Utah Medical Products Inc.	$201.82
Next earnings date	November 6, 2015	Misonix, Inc.	$80.54
Market Data		Bovie Medical Corporation	$53.57
Enterprise value	$68.78	Synergetics USA, Inc.	$170.20
Market Capitalization	$77.79		
Daily volume	0.02	STAAR Surgical Company	$341.92
Shares outstanding	10.00	Anika Therapeutics Inc.	$480.96
Diluted shares outstanding	10.10	Carl Zeiss Meditec AG	$2,160.80
% shares held by institutions	21.62%	**Current Capital Structure**	
% shares held by insiders	4.12%	Total debt/Common Equity (LTM)	0.09
Short interest	0.09%	Cost of Borrowing (LTM)	0.00%
Days to cover short interest	0.32	Estimated Cost of new Borrowing	0.00%
52 week high	$11.28	Altman's Z	8.14
52-week low	$6.41	Estimated Debt Rating	AAA
5y Beta	0.70	Current levered Beta	0.97
6-month volatility	44.71%	LTM WACC	8.17%

Management

Professional	Title	Comp. FY2012	Comp. FY2013	Comp. FY2015
Moore, William	Chairman of The Board, Chief Executive Offi	$208,643	$524,391	$0
Steckel, Ronald	Vice President of Operations	$373,037	$226,657	$0
Hardiman, Paul	Vice President of Regulatory & Compliance	$0	$0	$0
Buckley, Timothy	Vice President of Marketing & North America	$0	$0	$0
Rodgers, Stacie	Vice President of Human Resources	$0	$0	$0
Peartree, Kenneth	Vice President of Research & Development	$0	$0	$0

Past Earning Surprises

	Revenue	EBITDA	Norm. EPS	Standard Error of "Surprise"
Last Quarter	-0.30%	0.00%	150.00%	50.05%
Last Quarter-1	1.53%	0.00%	-25.00%	8.60%
Last Quarter -2	3.09%	0.00%	-16.67%	6.14%
Last Quarter -3	0.38%	0.00%	0.00%	0.13%
Last Quarter -4	6.24%	0.00%	25.00%	7.51%
Standard error	1.2%	0.0%	32.0%	10.39%
Standard Error of Revenues prediction	1.2%			
Imputed Standard Error of Op. Cost predictio	NM			
Imputed Standard Error of Op. Cost predictio	32.0%			

Proforma Assumptions

Convergence Assumptions

All base year ratios linearly converge towards the Sub-industry ratios over an explicit period of 10 years

General Assumptions

Money market rate (as of today)	0.28%
Risk-Free rate (long term estimate)	2.94%
Annual increase (decrease) in interest rates	0.1%
Marginal Tax Rate	37.5%
Country Risk Premium	6.0%

Forecast Year	Revenue Growth Forecast	Revenue ($) Forecast
LTM		$41.43
FY2016	11.0%	$46.48
FY2017	10.2%	$52.29
FY2018	9.4%	$58.38
FY2019	8.6%	$64.75
FY2020	7.8%	$71.42
FY2021	7.0%	$78.41
FY2022	6.2%	$85.77
FY2023	5.4%	$93.53
FY2024	4.6%	$101.34
FY2025	3.8%	$109.14
Continuing Period	3.0%	$116.95

Items' Forecast Assumptions

	Base year (LTM)	Convergence period (Sub-industry)	Adjustment per year
Operating Cash/Rev.	0.00%	0.00%	0.0%
NWV/Rev.	30.60%	20.67%	-1.0%
NPPE/Rev.	2.60%	19.30%	1.7%
Dpr/NPPE	41.98%	21.30%	-2.1%
NOPAT MARGIN	8.00%	15.51%	0.8%
Op. Exp./Rev.	93.31%	76.43%	-1.7%
SBC/Rev.	2.55%	1.64%	-0.1%
Rent Exp./Rev.	1.45%	0.91%	-0.1%
R&D/Rev.	11.35%	8.00%	-0.3%
E&D/Rev.	0.00%	0.00%	0.0%
SG&A/Rev.	33.48%	30.78%	-0.3%
ROC	8%	11.78%	0.36%
EV/Rev.	1.67x	2.45x	0.08x
EV/EBITA	18.12x	9.86x	-0.83x
Debt/Equity	9%	64%	5.5%
Unlevered beta	0.92	0.77	-0.01
Cost of Borrowing	0%	5%	0.5%
Dividends/REV	0%	3%	0.3%

Other Assumptions

Tobin's Q	80%
Excess cash reinvestment	Cost of capital
Other claims on the firm's assets	$0.00

Capitalization

100% of all rent expenses are capitalized and amortized 'straightline' over 10 years
100% of all R&D expenses are capitalized and amortized 'straightline' over 10 years
E&P expenses are not capitalized
SG&A expenses are not capitalized

Valuation Focus

DCF Valuation	100%
Relative valuation	0%
Distress Valuation	0%

Monte Carlo Simulation Assumptions

Revenue Growth deviation	Normal (0%, 1%)
Operating expense deviation	Normal (0%, 1%)
Continuing Period growth	Triangular (5.335%, 6%, 5.665%)
Country risk premium	Triangular (2.91%, 3%, 3.09%)
Intrinsic value $\sigma(\varepsilon)$	$0.03
1-year target price $\sigma(\varepsilon)$	$0.03

Valuation

Forecast Year	ROC	WACC	Total Capital	Implied Enterprise Value	Other Claims on Assets and Dilution Costs	Shares Outstanding	Price per Share
LTM	8.1%	8.2%	$60.52	$117.64	$8.29	10.00	$10.84
FY2016	7.8%	8.2%	$65.76	$127.77	$8.03	10.00	$12.01
FY2017	8.4%	8.2%	$71.97	$138.91	$6.64	10.00	$13.32
FY2018	9.0%	8.2%	$79.25	$151.08	$6.35	10.00	$14.66
FY2019	9.6%	8.2%	$87.71	$164.36	$4.15	10.00	$16.18
FY2020	10.1%	8.2%	$97.53	$178.87	$2.30	10.00	$17.78
FY2021	10.5%	8.3%	$108.91	$194.77	$2.01	10.00	$19.40
FY2022	10.9%	8.3%	$122.12	$212.27	$2.05	10.00	$21.11
FY2023	11.2%	8.3%	$132.32	$226.44	$2.13	10.00	$22.64
FY2024	11.8%	8.3%	$143.11	$240.45	$0.00	10.00	$24.16
FY2025	12.4%	8.4%	$155.16	$254.78	$0.00	10.00	$25.55
Continuing Period	11.8%	8.4%	$154.00				

Monte Carlo Simulation Results

The 3σ(ε)-adjusted intrinsic value is $11.08; the 3σ(ε)-adjusted target price is $12.29; and the analysts' median target price is $0

Sensitivity Analysis

Revenue growth variations account for 95.9% of total variance
Risk premium's variations account for 2.5% of total variance
Operating expenses' variations account for 1.4% of total variance
Continuing period growth variations account for 0.2% of total variance

Siena Market Line
3rd week of October 2015

Sucampo Pharmaceuticals, Inc.

NasdaqGM:SCMP

Analyst: Andrew Varone
Sector: Healthcare

BUY

Price Target: $27.83

Key Statistics as of 10/15/2015

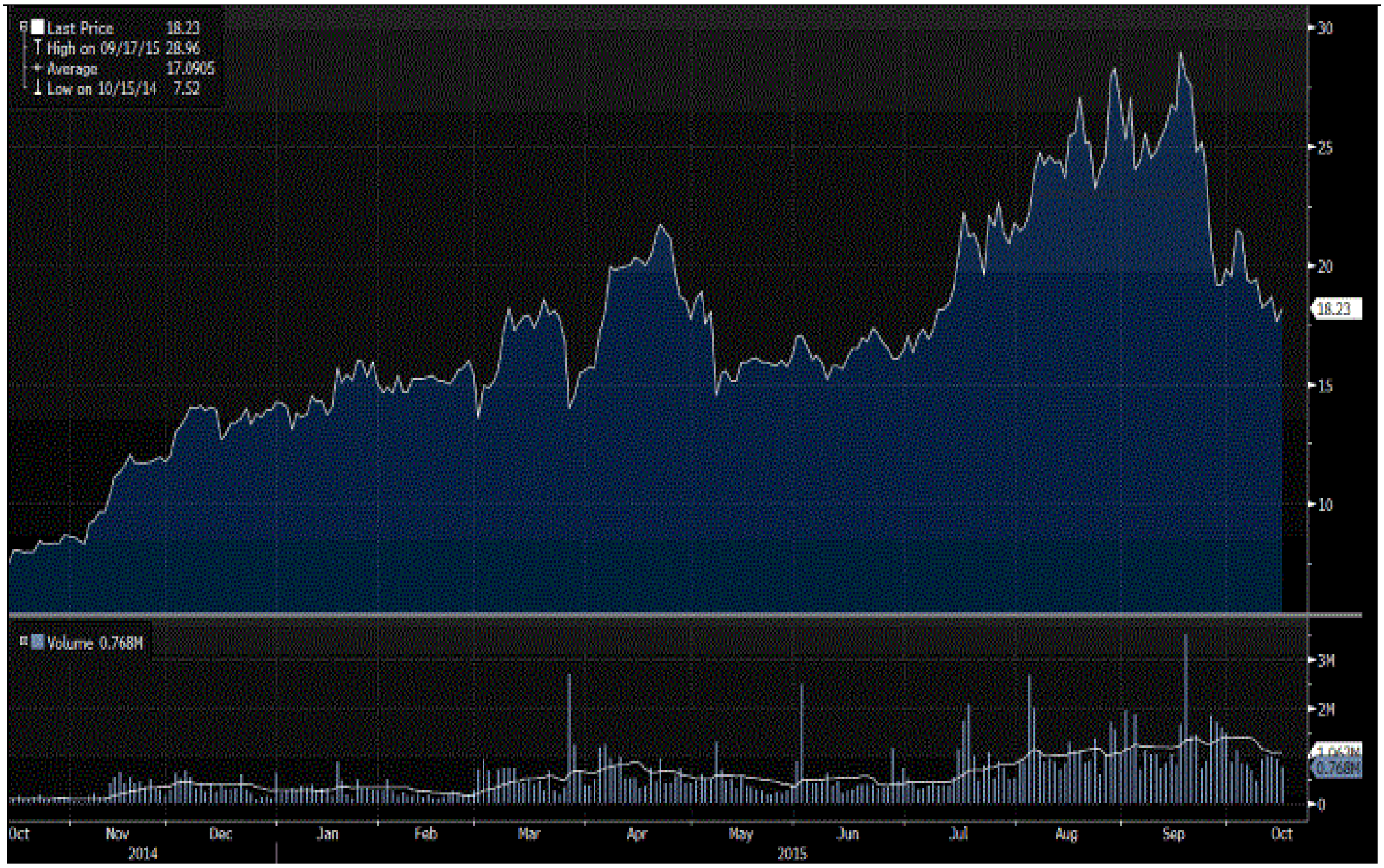
Market Price:	$18.23
Industry:	Pharmaceuticals
Market Cap:	$815.24
52-Week Range:	$6.88-29.67
Beta:	1.06

Thesis Points:

- Short-term losses due to company's industry.
- Opportunity for growth with main drug Amitiza.
- New acquisition could lead to new opportunities.

Company Description:

Sucampo Pharmaceuticals, Inc. is a biopharmaceutical company focused on the discovery, development and commercialization of proprietary drugs based on protons, a class of compounds derived from functional fatty acids that occur naturally in the human body. Sucampo is focused on developing protons for the treatment of gastrointestinal, vascular and central nervous system diseases and disorders for which there are unmet or underserved medical needs and significant commercial potential. Sucampo was established in December 1996.



Thesis

Sucampo Pharmaceuticals, behind its drug Amitiza, finished the second quarter on pace to have the highest revenues in their history. Compared to last year, high revenues have caused net income to be up 575.57% though six months. This helped the stock to reach a new record high in mid-September. A few days after reaching its high, the company's stock has faced declines of around 40%. This is due to the large macroeconomic pressures that pharmaceuticals companies have recently been exposed to. There has been a push in politics to lower the price of prescription drugs. This would cut into the profits of pharmaceuticals companies such as Sucampo Pharmaceuticals. There are some concerns with the company in terms of competitiveness. A major competitor has risen in the United States. Despite this, Amitiza's sales are expected to continue to climb in the United States. The biggest area for growth is expected to be in Japan as there has been little competition there. The company's CEO, Peter Greenleaf, has reshaped the company since joining in 2014. Mr. Greenleaf put emphasize into the company's main drug Amitiza. He then furthered his company's position by acquiring R-Tech Ueno for a price of $278 million. Following the announcement of the acquisition, the stock price rose by 2.6%. The acquisition was done to add assets to the company while giving Sucampo the resources necessary to speed up development and better focus in therapeutic areas where needs at unmet. This acquisition also pairs with their drug Amitiza as they gained control over its manufacturing process.

A BUY is recommended for Sucampo Pharmaceuticals, Inc. as the stock is currently priced at $18.23 which opens a window for entry. With a price target of $27.83, there is an upside potential of 52.66%.

Pharmaceutical Industry

The pharmaceutical industry is one that strives off of revenues and competitive edge gained through patents. Last month, there has been a push for a price ceiling to be put in place on prescription drugs from the democratic candidacy party. This has hurt the stock price of pharmaceutical companies as investors became wary of the possibility of such laws. These laws would decrease revenues and future cash flows of these pharmaceutical companies. Because of this, the pharmaceutical industry as a whole has seen the value of their stocks go down. As seen in the graph below, as the index (red) goes down, the stock of SCMP (blue) decreases.

This means that the devaluation of Sucampo has been a macro economy issue. This devaluation has led to an entry opportunity for investors as the stock's price reflects this macro pressure. An election of a democratic president does not ensure that a price ceiling will be put into place. The laws still have to get pass by congress, which itself will be no easy task. Also, Democratic frontrunner, Hillary Clinton, has enjoyed her fair share of money received from pharmaceuticals/health companies. If the democratic party decides to stop making a push, or do not receive the necessary positions in politics, this price laws will not be put into place. If there is any indication that these laws will not be put into place, the stock prices of pharmaceutical companies will increase. For a company like Sucampo, the stock price should return to its previous values before the prescription drug announcement. This is due to the devaluation mainly being a macro issue.

Main Product

Sucampo Pharmaceuticals leading drug is called Amitiza. The drugs main use is to help with constipation and can also be used to treat IBS in women. The drug has had major sales in the United States and in Japan. With lessor sales throughout Europe. Recently, the drug received permission to start distribution in the People's Republic of China.

amitiza
lubiprostone

Behind Amitiza, Sucmapo has reached $0.67 EPS over the past twelve months. This has been the highest EPS that the company has reached over the past five years. The EPS is expected to be up 33% from last year. Though EPS are reaching its peak, the drug has been pulled off the shelves of CVS in favor of a competitor starting in 2016. Despite this, EPS are forcasted to increase through 2016. This is due to the fact that there can still be growth in the United States even without CVS as a distributor. The Chinese market is one that has untapped potential for Sucampo. Overall, sales are expected to be up 44% from a year from now. In their second quarter earnings call, CEO Peter Greemlead had this entrance into the Chiense market was long overdue. Sucampo has received $1.5 million upfront as part of the lienscing agreement. Amizitza can see an increase sales due Japan and now China. If third quarter follows the trends of the second quarter where actual sales outpaced estimated sales by 9%, this could lead to furtther increasing of the price of the stock.

Acquisition

Sucampo has recently announced the results of their tender offer for R-Tech Ueno. By October 20th, they will have control of approximately 98% of R-Tech Ueno. Sucampo believes that this acquisition will give them around $5M operational synergies. These synergies will raise adjusted EBITA by 5% and EPS by 8%. This acquisition also gives Sucampo control over their supplier that makes their drug, Amitiza. This acquisition is already reflected in the stock price as SCMP rose by 2.6% after the announcement of a tender offer.

This acquisition also gives Sucampo access to pipeline drugs. They could eventually add these new drugs to their company, making them less dependent on Amitiza. Currently, they are working on spinoffs of Amitiza that include, one with a new formula and two that are suitable for children. These are currently in Phase III of the development stage. They are also working on new types of drug that deal oral mucositis and non-erosive reflux disease. There two drugs are currently in Phase II of development. Being able to complete these drugs through all three phases of

development will make their stock price increase.

This is due to the new cash flows that will be created and the company will also be less risky. Sucampo was rated at a B3 from Moody's credit rating. This risky rating is not from being overly levered, as their capital structure is 1.7% long term debt. Their risky rating comes from their lack of assets and overreliance on sales from one drug. If the company is able to add another drug to its sales, Sucampo will become less risky as a result. This was increase the value of its stock as the risk premium of the company will decrease due to an increase in their rating.

Financials

The acquisition of their supplier will allow for higher margins and to capitalize on revenues to other drug pharmaceuticals. The operating margin of the company has increased by 49.7% over the past year. For going forward, this level of margin increase can be sustainable through the use of their new acquisition. By increasing margin, EPS will increase as a result furthering increasing the stock price. For the forecasted year 2016, EPS will increase to 1.13 which is a 51% increase.

Despite the company high risk rating, it is not from being over levered. This can be seen from the balance sheet as they have decreased debt by almost half, going from $52.7-25.8M. Also, their recent acquisition was done through cash as they had $108.5M on their balance sheets. If their company is able to acquire more assets and produce more products, Sucampo will become less risky. When they become less risky, they will be able to become more levered increasing EPS.

Porters 5 Forces

The threats of new entrants is relatively low as there is currently seventeen patents put into place on their drug, Amitiza. This will make it hard for new competitors to enter the market as they will have to pay royalties to Sucampo if they want to enter the same dietary market as Sucampo.

The threat of substitutes is also relatively low for this company. The main concern for substitutes comes from the selling of generic pharmaceuticals. Currently, there is no generic brand on Amitiza in the United States making the threat of substitutes low.

The threats of customers is neutral. Since there are no generic substitutes, the consumer has to pay the price that the drugs are priced at. Future laws could change this as movements have been made to try and lower the premiums on pharmaceutical drugs. Since no laws have been passed yet, the threat is neutral.

The threat of suppliers is low. Currently there are five suppliers that supply the compound needed to create Amitiza. Sucampo has acquired a company that supplies them with this drug compound.

The last threat is the threat of rivals. This last threat is neutral as Amitiza has seen some rivalry. Starting in 2016, their drug will be pulled from the shelves of CVS for a competitors. Despite this, sales are expected to rise because there is enough market share that they can still obtain.

Conclusion

The downsides of Sucmpo are macro with the downturn of the pharmaceutical industry. The only micro downside they face is their product taken off the shelves in CVS. On the other side, there are many upsides with their exposure to new drug patents through their acquisition. Since their company has been devalued through macro economy trends, SCMP is at a low price for investors looking for a stock to enter the market.

Sources:

- Capital IQ
- Bloomberg
- www.sucampo.com
- www.drugpatentwatch.com
- www.opensecret.org

CENTER FOR GLOBAL FINANCIAL STUDIES

Sucampo Pharmaceuticals, Inc.	SCMP	Analyst	Current Price	Intrinsic Value	Target Value	Divident Yield	1-y Return: 32.66%	BULLISH
		Andrew Varone	$18.23	$22.46	$24.18	0%		

General Info	
Sector	Healthcare
Industry	Pharmaceuticals
Last Guidance	August 5, 2015
Next earnings date	November 5, 2015
Market Data	
Enterprise value	$728.48
Market Capitalization	$77.79
Daily volume	0.02
Shares outstanding	44.72
Diluted shares outstanding	45.72
% shares held by institutions	21.62%
% shares held by insiders	0.16%
Short interest	11.50%
Days to cover short interest	4.52
52 week high	$29.67
52-week low	$7.34
5y Beta	1.59
6-month volatility	77.12%

Peers	Market Cap.
Pernix Therapeutics Holdings, Inc.	$224.01
Supernus Pharmaceuticals, Inc.	$785.31
Akorn, Inc.	$3,330.00
Sagent Pharmaceuticals, Inc.	$562.26
Nektar Therapeutics	$1,437.55
Avanir Pharmaceuticals, Inc.	
Ironwood Pharmaceuticals, Inc.	$1,633.91
Salix Pharmaceuticals Ltd.	
Cumberland Pharmaceuticals, Inc.	$88.46
SciClone Pharmaceuticals, Inc.	$372.86
Current Capital Structure	
Total debt/Common Equity (LTM)	0.15
Cost of Borrowing (LTM)	3.56%
Estimated Cost of new Borrowing	0.00%
Altman's Z	8.77
Estimated Debt Rating	AAA
Current levered Beta	1.06
LTM WACC	7.52%

Management

Professional	Title	Comp. FY2012	Comp. FY2013	Comp. FY2014
Greenleaf, Peter	Chief Executive Officer and Director	$0	$0	$5,650,759
Ueno, Ryuji	Co-Founder, Chairman Emeritus and Scienti	$809,585	$865,632	$183,282
Smith, Andrew	Chief Financial Officer	$0	$405,914	$570,362
Kiener, Peter	Chief Science Officer	$0	$0	$1,812,214
Alder, Matthias	Executive Vice President of Business Develo	$0	$0	$1,700,673
Donley, Matthew	Executive Vice President of Human Resource	$0	$0	$1,117,429

Past Earning Surprises

	Revenue	EBITDA	Norm. EPS	Standard Error of "Surprise"
Last Quarter	9.44%	0.00%	50.00%	15.34%
Last Quarter-1	-2.25%	35.28%	7.69%	11.23%
Last Quarter -2	-1.69%	-21.62%	10.53%	9.37%
Last Quarter -3	21.56%	125.00%	250.00%	66.04%
Last Quarter -4	-1.63%	3.22%	0.00%	1.43%
Standard error	4.7%	25.8%	47.4%	17.91%
Standard Error of Revenues prediction	4.7%			
Imputed Standard Error of Op. Cost predictio	25.4%			
Imputed Standard Error of Op. Cost predictio	39.7%			

Proforma Assumptions

Convergence Assumptions

All base year ratios linearly converge towards the Sub-industry ratios over an explicit period of 10 years

General Assumptions	
Money market rate (as of today)	0.28%
Risk-Free rate (long term estimate)	2.94%
Annual increase (decrease) in interest rates	0.1%
Marginal Tax Rate	35.0%
Country Risk Premium	5.0%

Forecast Year	Revenue Growth Forecast	Revenue ($) Forecast
LTM		$131.31
FY2015	6.5%	$143.79
FY2016	41.7%	$212.22
FY2017	9.7%	$242.77
FY2018	8.0%	$273.50
FY2019	10.4%	$314.05
FY2020	9.6%	$356.54
FY2021	-1.5%	$363.29
FY2022	11.3%	$416.76
FY2023	-2.4%	$417.90
FY2024	0.5%	$431.18
Continuing Period	3.0%	$455.29

Items' Forecast Assumptions

	Base year (LTM)	Convergence period (Sub-industry)	Adjustment per year
Operating Cash/Rev.	0.00%	0.00%	0.0%
NWV/Rev.	2.88%	14.66%	1.2%
NPPE/Rev.	0.40%	41.77%	4.1%
Dpr/NPPE	111.03%	15.40%	-9.6%
NOPAT MARGIN	34.55%	19.58%	-1.5%
Op. Exp./Rev.	59.49%	72.50%	1.3%
SBC/Rev.	3.84%	1.62%	-0.2%
Rent Exp./Rev.	1.07%	0.83%	0.0%
R&D/Rev.	18.85%	11.33%	-0.8%
E&D/Rev.	0.00%	0.00%	0.0%
SG&A/Rev.	26.20%	26.42%	0.0%
ROC	18%	13.29%	-0.50%
EV/Rev.	5.07x	3.75x	-0.13x
EV/EBITA	10.73x	12.45x	0.17x
Debt/Equity	15%	44%	2.9%
Unlevered beta	0.96	0.78	-0.02
Cost of Borrowing	0%	5%	0.5%
Dividends/REV	0%	7%	0.7%

Other Assumptions

Tobin's Q	80%
Excess cash reinvestment	Cost of capital
Other claims on the firm's assets	$0.00

Capitalization

100% of all rent expenses are capitalized and amortized 'straightline' over 10 years
100% of all R&D expenses are capitalized and amortized 'straightline' over 10 years
E&P expenses are not capitalized
SG&A expenses are not capitalized

Valuation Focus

DCF Valuation	100%
Relative valuation	0%
Distress Valuation	0%

Monte Carlo Simulation Assumptions

Revenue Growth deviation	Normal (0%, 1%)
Operating expense deviation	Normal (0%, 1%)
Continuing Period growth	Triangular (5.335%, 5%, 5.665%)
Country risk premium	Triangular (2.91%, 3%, 3.09%)
Intrinsic value σ(ε)	$0.48
1-year target price σ(ε)	$0.50

Valuation

Forecast Year	ROC	WACC	Total Capital	Implied Enterprise Value	Other Claims on Assets and Dilution Costs	Shares Outstanding	Price per Share
LTM	18.3%	7.5%	$250.95	$910.28	$125.19	44.72	$23.37
FY2015	22.3%	7.3%	$271.32	$941.02	$115.72	44.72	$25.20
FY2016	22.8%	7.4%	$361.09	$1,038.43	$115.62	44.72	$26.85
FY2017	17.5%	7.4%	$413.33	$1,104.20	$113.19	44.72	$28.15
FY2018	15.6%	7.4%	$460.99	$1,169.37	$110.13	44.72	$29.50
FY2019	14.7%	7.5%	$511.93	$1,239.59	$106.68	44.72	$30.84
FY2020	14.0%	7.5%	$559.57	$1,307.99	$102.39	44.72	$31.74
FY2021	12.5%	7.5%	$576.16	$1,352.61	$96.01	44.72	$32.89
FY2022	13.6%	7.5%	$623.30	$1,422.90	$90.54	44.72	$33.78
FY2023	12.6%	7.5%	$634.11	$1,461.63	$0.00	44.72	$35.38
FY2024	13.2%	7.5%	$654.14	$1,507.60	$0.00	44.72	$36.59
Continuing Period	13.3%	7.6%	$670.71				

Monte Carlo Simulation Results

The 3σ(ε)-adjusted intrinsic value is $22.46; the 3σ(ε)-adjusted target price is $24.18; and the analysts' median target price is $27.83

Sensitivity Analysis

Revenue growth variations account for 95.9% of total variance
Risk premium's variations account for 2.5% of total variance
Operating expenses' variations account for 1.4% of total variance
Continuing period growth variations account for 0.2% of total variance

Siena Market Line
3rd week of October 2015

U.S. Concrete, Inc.

NasdaqCM:USCR

Analyst: Daniel Bacchi
Sector: Industrials

BUY

Price Target: $58.24

Key Statistics as of 10/15/2015

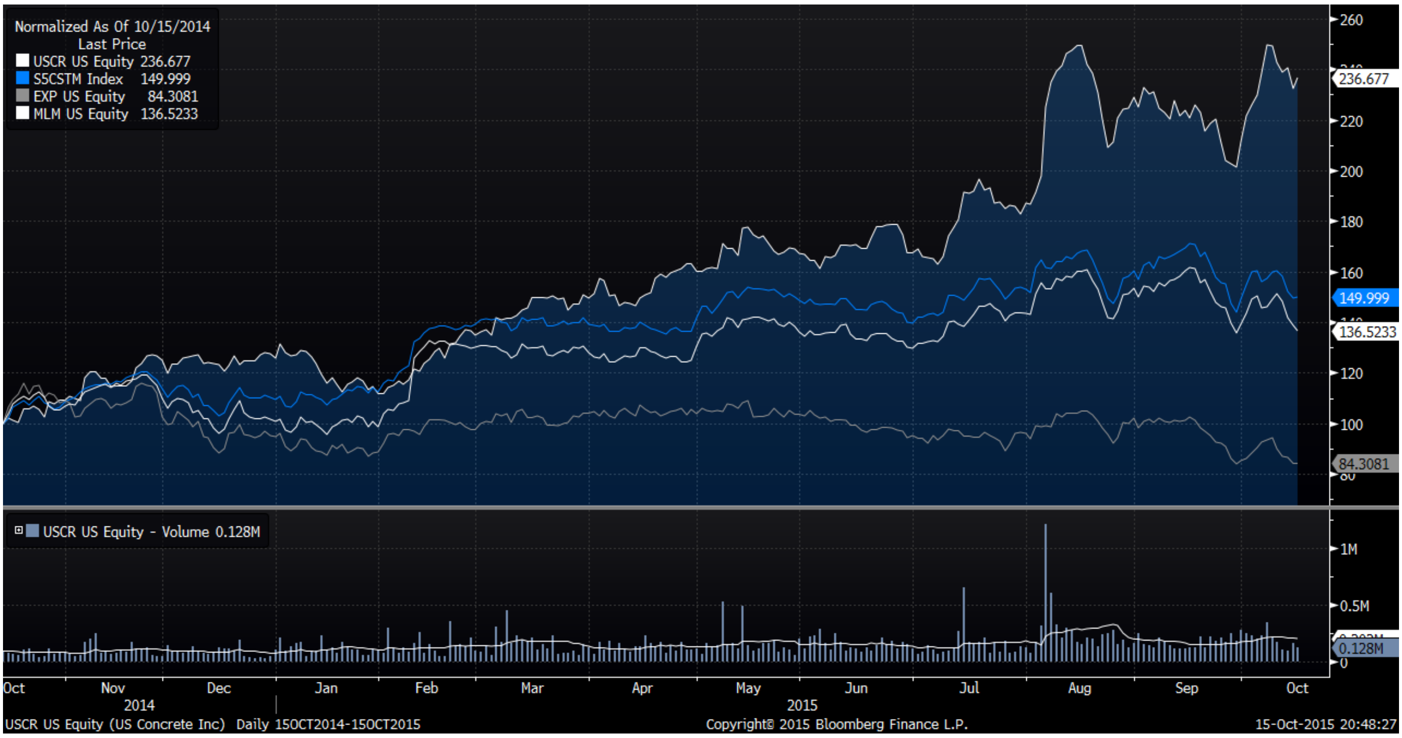
Market Price:	$53.56
Primary Industry:	Construction Materials
Market Cap:	$781.02 M
52-Week Range:	$21.60-57.57
5Y Beta:	1.46

Thesis Points:

- Vertical integration in the industry through key acquisitions in the aggregates market.
- Greater margin potential through reduced materials costs while maintaining or increasing quality.
- The industry strength will be a key factor to continued growth.

Company Description:

U.S. Concrete, Inc., through its subsidiaries, produces and sells ready-mixed concrete, aggregates, and concrete-related products and services for the construction industry in the United States. It operates through two segments, Ready-Mixed Concrete and Aggregate Products. The Ready-Mixed Concrete segment is involved in the formulation, preparation, and delivery of ready-mixed concrete to customers' job sites; and the provision of various services that include the formulation of mixtures for specific design uses, on-site and lab-based product quality control, and customized delivery programs. The Aggregate Products segment offers crushed stone, sand, and gravel for use in commercial, industrial, and public works projects. The company also engages in the operation of building materials stores; provision of lime slurry and Aridus rapid-drying concrete technology; sale of brokered products; hauling and recycled aggregates operation activities; and operation of drum mixer trucks, as well as transfer trucks for transporting cement and aggregates. It primarily serves concrete sub-contractors, general contractors, governmental agencies, property owners and developers, architects, engineers, and home builders in north and west Texas, California, New Jersey, New York, Washington, D.C., and Oklahoma. U.S. Concrete, Inc. was founded in 1948 and is headquartered in Euless, Texas. (From YAHOO! Finance)



Thesis

U.S. Concrete, Inc. is positioned in the top 3 in the major markets the firm serves. The firm has focused on vertical integration through key acquisitions in the ready-mixed concrete segment and the aggregates market. The vertical integration assisted U.S. Concrete, Inc. in reducing cost by using the aggregates as a primary source for the ready-mixed business division. The reduction in cost has produced a greater margin for U.S. Concrete, Inc. in the current financial period along with the increased activity in construction in the U.S. that has increased demand for materials such as ready-mixed concrete. A BUY of U.S. Concrete, Inc. (USCR) is suggested with a one-year target price of $58.24.

Industry Performance & Outlook

U.S. Concrete, Inc. provides ready-mix concrete and aggregates for the construction materials sector. The past year's market increase of 25.33% due to the growing economy leaves investors with a positive outlook into the future. The construction materials sector is heavily tied to future GDP growth; economists have predicted that, overall, the U.S. GDP will continue to grow, barring any extraordinary events in the economy. Forecasters see a 25% chance of growth over 3%, defined as an economic boom, before election day of 2016. Overall the forecaster have a consensus of 2.8% growth in the period between now and election day. The forecast bodes well for the new construction market.

Economists forecast an average increase in industrial construction, the main driver of change in the construction materials sector, of 10.1% for 2016. Industrial and commercial projects provide the largest opportunity for U.S. Concrete, Inc. to offer value-added products that meet the requirements requested by those projects. Office construction is forecasted to increase 12.0% for 2016, other construction is estimated between 2.5% and 11.5%. The key factor is the strength of the market continuing forward. The Fed and economists look for continued growth that we have seen in 2015. U.S. Concrete, Inc. expects an increase with sustainable construction; a main market segment of the business. They predict green construction at 55% of non-residential construction in 2016. With increases in construction, it can be assumed that competition will be fierce and new entrant may appear as low cost alternatives in the primary construction market. The key to success will depend on the strategies of the competitors in the market.

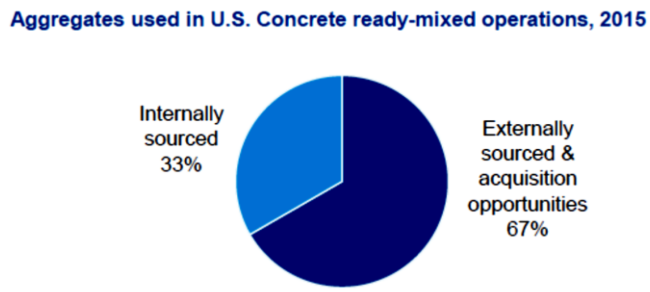
Vertical Integration & Acquisitions

U.S. Concrete, Inc. completed 17 acquisitions of ready-mixed concrete and aggregate firms since 2014, building U.S. Concrete, Inc.'s position within the market and providing cost reductions due to economies of scale along with integrating firms providing the primary material, aggregate (about 60-75%), of ready-mixed concrete. The inorganic growth that has been achieved through acquisitions has expanded U.S. Concrete, Inc. into new arenas and grew market share in current markets. The primary market for U.S. Concrete Inc. is in West Texas where they are currently positioned at #1. The average market share in key regions is about 30%, with an opportunity to grow both organically, through increased sales, and inorganically, through more acquisitions.

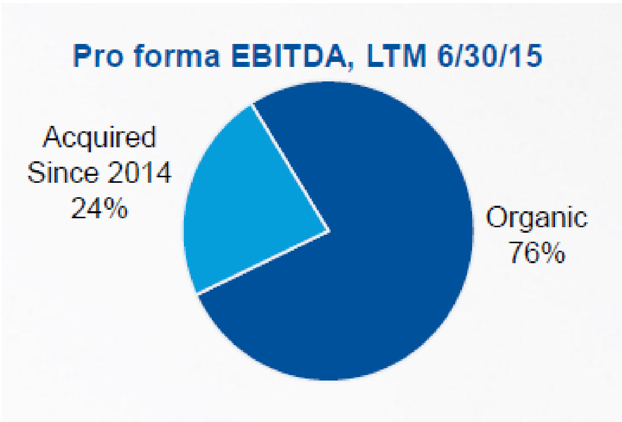
Enhancing the value chain in the NY/NJ region has been achieved through aggregate acquisition of Wantage Stone. A single site of 38 million tons of reserves will reduce costs in the region. Value chain enhancement in the region near Texas has been achieved with the acquisition of E&A Materials in Wichita Falls; that will provide 15+ million tons of reserves.

Along with aggregate acquisitions, U.S. Concrete Inc. has expanded their ready-mixed concrete capacity in the NY/NJ region with the acquisitions of Colonial Concrete Company (NJ) and Ferrara Bros. (NY) providing 10 more ready-mixed plants and 129 mixer trucks allowing U.S. Concrete Inc. to provides a wider range of service and a larger proportion of service in the NY/NJ region. Other recent acquisitions have provided U.S. Concrete with 7 plants and 91 trucks in both the San Francisco Bay Area and Northern Virginia.

The recent acquisitions have proven that U.S. Concrete Inc. has the ability to consolidate markets, integrate their operations, in turn increasing margins and producing attractive returns for the firm.



Increasing Margins



By vertically integrating their operations with aggregate and ready-mixed concrete acquisitions U.S. Concrete has managed to increase revenue and margins, costs of goods sold as a percentage of sales for the LTM have dropped to 80% from the average of 85% in the period from 2010 to 2014. Coupled with revenue growth of 23.5%, U.S. Concrete Inc has managed to produce an EBITDA margin of 7.7%, up from the 3% average in the years from 2010 from 2014. The key consideration is U.S. Concrete, Inc. has beat past estimates for revenue and EBITDA in the last few quarters, and the future of U.S. Concrete looks strong into the following quarters.

		Past Earning Surprises
	Revenue	EBITDA
Last Quarter	7.40%	26.73%
Last Quarter-1	6.62%	45.19%
Last Quarter -2	4.50%	8.47%
Last Quarter -3	3.45%	13.33%

Investors can only expect the margin to increase as the acquisitions and backlog allow for anticipated growth into 2016. U.S. Concrete, Inc. is looking to expand into a 5th geographic area, if they are successful they are looking at more revenue growth and an increase in margins for 2016.

Business Cores

U.S. Concrete, Inc. provides technology and innovations that provide the development of engineered mixes that are able to reduce the carbon footprint, while maintaining the high performance that customers look for in concrete, as compared to traditional concrete. They are able to reduce the material cost by using a low CO_2 level but at the same time offer an equal or higher performing product as compared to traditional manufacturing procedures. Just like competitors, U.S. Concrete, Inc. remains focused on cement production and utilization.

Continuing expansion into current markets through organic growth along with acquisitions and partnerships is a goal of U.S. Concrete, Inc. Along with expansion into new markets that allow for new streams of revenue and supply and to better serve customers. Coupled with optimizing the performance of their ready-mixed concrete they will continue to differentiate themselves from competitors that focus solely on cost and price rather than quality.

Financials

Through the recent year U.S. Concrete, Inc. has grown financially stronger through increases in revenue to reductions in costs. Those do not come without any cost however. In order to expand markets and control supply U.S. Concrete, Inc. required financing; primarily, they used debt in their acquisitions.

Currently the cost of borrowing for the firm is 8.54%, correlating with the debt rating of B+ by S&P. It will be imperative that U.S. Concrete, Inc. is able to wisely use debt to finance their future expansion, management believes that they will use a blend of equity and debt to finance future growth. The key factor is not only how they finance but the return brought on by the asset they finance. At the current period net property plant and equipment as a percentage of sales is well below the industry average of 85.0%, with an NPPE/Rev. of 26.0% it is apparent that U.S. Concrete is able to do more with the assets the firm owns.

For the current period U.S. Concrete produced a NOPLAT margin of 5.5%, forecasts show that by 2022 that margin will reach 7.9% into the continuing period placing U.S. Concrete at a prime position and allowing for future reinvestment through the company's earnings.

Conclusion

It is imperative that U.S. Concrete, Inc. maintains or increases current margins into the next year. The most sensitive aspects to their value are revenue and operating costs.

Sensitivity Analysis
Revenue growth variations account for 42.1% of total variance
Risk premium's variations account for 3% of total variance
Operating expenses' variations account for 32.7% of total variance
Continuing period growth variations account for 24.9% of total variance

The consensus and predictions, along with past performance in the year indicate that the firm will continue to grow revenue and find avenues to reduce costs. That is why I recommend a BUY for U.S. Concrete, Inc.

Sources:

- U.S. Concrete Inc., 10-K
- U.S. Concrete Inc., Investor Presentations
- The American Institute of Architects
- Capital IQ
- Bloomberg
- SEC
- NY Times

CENTER FOR GLOBAL FINANCIAL STUDIES

U.S. Concrete, Inc.	USCR	Analyst	Current Price	Intrinsic Value	Target Value	Divident Yield	1-y Return: 8.74%	NEUTRAL
		Daniel Bacchi	$53.56	$55.16	$58.24	0%		

General Info

Sector	Materials
Industry	Construction Materials
Last Guidance	(Invalid Identifier)
Next earnings date	November 6, 2015

Market Data

Enterprise value	$1,046.52
Market Capitalization	$781.02
Daily volume	0.13
Shares outstanding	14.58
Diluted shares outstanding	13.86
% shares held by institutions	94.65%
% shares held by insiders	7.54%
Short interest	6.02%
Days to cover short interest	4.16
52 week high	$57.57
52-week low	$21.60
5y Beta	1.46
6-month volatility	39.36%

Peers	Market Cap.
Martin Marietta Materials, Inc.	$9,997.93
Eagle Materials Inc.	$3,413.49
Vulcan Materials Company	$12,185.22
Summit Materials, Inc.	$1,023.32

Current Capital Structure

Total debt/Common Equity (LTM)	2.30
Cost of Borrowing (LTM)	8.46%
Estimated Cost of new Borrowing	0.00%
Altman's Z	2.11
Estimated Debt Rating	C
Current levered Beta	0.76
LTM WACC	6.13%

Management

Professional	Title	Comp. FY2012	Comp. FY2013	Comp. FY2014
Sandbrook, William	Chief Executive Officer, President, Chief Ope	$1,350,092	$1,442,889	$2,393,578
Jolas, Paul	Vice President, General Counsel and Corpora	$0	$0	$580,784
Roberts, Jeffrey	Vice President of Ingram Concrete LLC and C	$0	$410,592	$526,494
Poulsen, Niel	Vice President of Redi-Mix LLC and General	$443,443	$454,975	$548,626
Kohutek, Kevin	Chief Accounting Officer and Vice President	$0	$0	$0
Johnson, Wallace	Vice President of Marketing & Sales	$360,386	$0	$0

Past Earning Surprises

	Revenue	EBITDA	Norm. EPS	Standard Error of "Surprise"
Last Quarter	7.40%	26.73%	77.03%	20.75%
Last Quarter-1	6.62%	45.19%	NM	19.28%
Last Quarter -2	4.50%	8.47%	60.00%	17.88%
Last Quarter -3	3.45%	13.33%	83.64%	25.24%
Last Quarter -4	0.00%	0.00%	0.00%	0.00%
Standard error	1.3%	7.9%	19.1%	7.98%
Standard Error of Revenues prediction	1.3%			
Imputed Standard Error of Op. Cost predictio	7.8%			
Imputed Standard Error of Op. Cost predictio	17.3%			

Proforma Assumptions

Convergence Assumptions

All base year ratios linearly converge towards the Sub-industry ratios over an explicit period of 10 years

General Assumptions

Money market rate (as of today)	0.24%
Risk-Free rate (long term estimate)	2.84%
Annual increase (decrease) in interest rates	0.1%
Marginal Tax Rate	37.5%
Country Risk Premium	5.4%

Forecast Year	Revenue Growth Forecast	Revenue ($) Forecast
LTM		$793.13
FY2015	19.4%	$943.74
FY2016	17.5%	$1,105.24
FY2017	11.8%	$1,231.25
FY2018	10.7%	$1,358.15
FY2019	9.6%	$1,483.27
FY2020	8.5%	$1,603.69
FY2021	7.4%	$1,716.34
FY2022	6.3%	$1,818.13
FY2023	5.2%	$1,906.05
FY2024	4.1%	$1,977.38
Continuing Period	3.0%	$2,029.74

Items' Forecast Assumptions

	Base year (LTM)	Convergence period (Sub-industry)	Adjustment per year
Operating Cash/Rev.	0.00%	0.00%	0.0%
NWV/Rev.	3.87%	19.18%	1.5%
NPPE/Rev.	26.04%	85.00%	5.9%
Dpr/NPPE	13.37%	11.74%	-0.2%
NOPAT MARGIN	5.50%	9.10%	0.4%
Op. Exp./Rev.	88.73%	78.45%	-1.0%
SBC/Rev.	0.59%	0.79%	0.0%
Rent Exp./Rev.	1.50%	0.00%	-0.2%
R&D/Rev.	0.00%	1.22%	0.1%
E&D/Rev.	0.00%	0.00%	0.0%
SG&A/Rev.	8.59%	9.13%	0.1%
ROIC	13%	9.81%	-0.37%
EV/Rev.	0.97x	1.47x	0.05x
EV/EBITA	11.95x	10.07x	-0.19x
Debt/Equity	230%	-800%	-103.0%
Unlevered beta	0.31	0.51	0.02
Cost of Borrowing	9%	7%	-0.2%
Dividends/REV	0%	4%	0.4%

Other Assumptions

Tobin's Q	80%
Excess cash reinvestment	Cost of capital
Other claims on the firm's assets	$0.00

Capitalization

100% of all rent expenses are capitalized and amortized 'straightline' over 10 years
100% of all R&D expenses are capitalized and amortized 'straightline' over 10 years
E&P expenses are not capitalized
SG&A expenses are not capitalized

Valuation Focus

DCF Valuation	100%
Relative valuation	0%
Distress Valuation	0%

Monte Carlo Simulation Assumptions

Revenue Growth deviation	Normal (-0.00350747037259827%, 1%)
Operating expense deviation	Normal (0%, 1%)
Continuing Period growth	Triangular (5.335%, 5.42593856210061%, 5.665%)
Country risk premium	Triangular (2.91%, 3.00917369157773%, 3.09%)
Intrinsic value σ(ε)	$0.51
1-year target price σ(ε)	$0.34

Valuation

Forecast Year	ROIC	WACC	Invested Capital	Implied Enterprise Value	Net Claims on Assets and Dilution Costs	Shares Outstanding	Price per Share
LTM	13.5%	6.1%	$337.52	$1,185.87	$385.02	14.58	$55.77
FY2015	17.1%	5.5%	$449.47	$1,305.54	$459.43	14.58	$58.91
FY2016	15.4%	6.2%	$602.87	$1,470.00	$584.71	14.58	$60.12
FY2017	13.3%	6.2%	$756.03	$1,634.48	$709.07	14.58	$61.75
FY2018	12.1%	6.4%	$926.86	$1,819.03	$852.76	14.58	$63.20
FY2019	11.2%	6.7%	$1,113.52	$2,022.80	$1,015.94	14.58	$64.44
FY2020	10.5%	6.8%	$1,313.22	$2,244.21	$1,194.52	14.58	$65.55
FY2021	9.9%	7.2%	$1,522.28	$2,484.93	$1,395.38	14.58	$66.46
FY2022	9.4%	7.5%	$1,736.15	$2,742.21	$1,612.83	14.58	$67.32
FY2023	9.0%	7.8%	$1,949.55	$3,012.73	$1,843.55	14.58	$68.19
FY2024	8.6%	8.0%	$2,156.65	$3,292.71	$2,083.49	14.58	$64.11
Continuing Period	9.8%	7.3%	$1,881.86				

Monte Carlo Simulation Results

The 3σ(ε)-adjusted intrinsic value is $55.16; the 3σ(ε)-adjusted target price is $58.24; and the analysts' median target price is $62.25

Sensitivity Analysis

Revenue growth variations account for 42.1% of total variance
Risk premium's variations account for 3% of total variance
Operating expenses' variations account for 32.7% of total variance
Continuing period growth variations account for 24.9% of total varianc

Siena Market Line
3rd week of October 2015

Westlake Chemical Corporation

WLK: NYSE

Analyst: Mark Papuzza
Sector: Materials

BUY

Price Target: $67.26

Key Statistics as of 10/13/15

Market Price:	$58.92
Industry:	Commodity Chemicals
Market Cap:	$7.33B
52-Week Range:	$50.01-93.52
Beta:	1.4

Thesis Points:

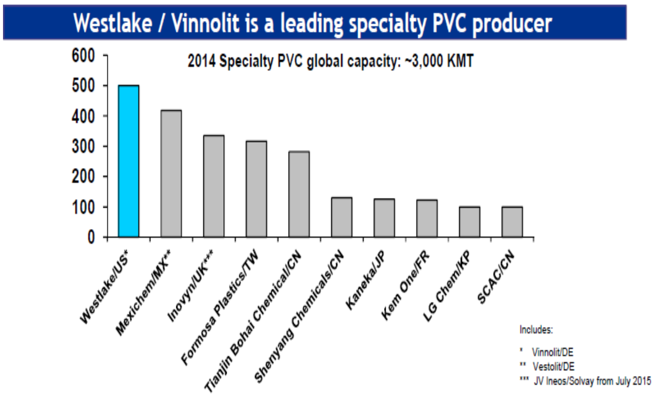
- Product Integration and Acquisitions
- Long-Term Growth Opportunities
- Financials – EBITDA margins, zero net debt, dividends

Company Description:

Westlake Chemical Corporation manufactures and markets basic chemicals, vinyls, polymers, and fabricated products. The company serves a range of consumer and industrial markets, including flexible and rigid packaging, automotive products, coatings, and residential and commercial construction. Westlake Chemical Corporation was founded in 1985 and is headquartered in Houston, Texas.

Thesis

Westlake Chemical Corporation is a producer of chemical and plastic products that enhance the daily lives of people around the world. With their strong history of product integration and acquisitions and future plans to continue both, combined with their long-term growth opportunities, Westlake Chemical will continue to grow their EBITDA margins and continue to create value for the company and increase the price of their stock.



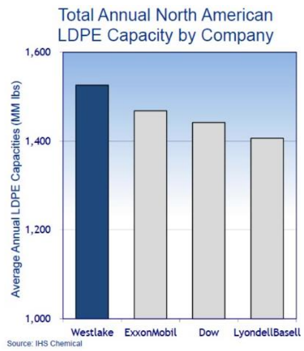
Product Integration and Acquisitions

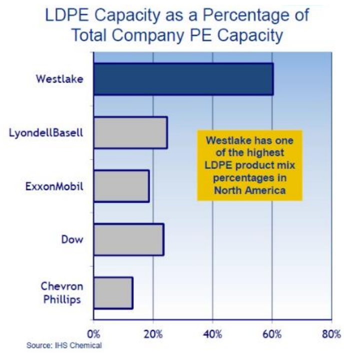
Westlake Chemical President and CEO Albert Chao has over 40 years of global experience in the chemical industry. With the knowledge and familiarity that comes with being a part of an industry for over four decades, Chao possesses the leadership skills this company needs to continue to innovate and grow.

Westlake's core business consists of two product line: Olefins and Vinyls. The olefins product line includes ethylene, polyethylene, polyethylene, styrene, epolene and propylene. The vinyls product line includes caustic, VCM, PVC (Polyvinyl chloride) suspension and specialty resins, and PVC building products such as windows. Westlake continues to focus on finding opportunities that will improve and grow their product line, and have recently made an investment that has helped their PVC product line grow substantially.

In the third quarter of 2014, Westlake Chemical acquired specialty PVC producer Vinnolit. Headquartered in Germany, Vinnolit is a global leader in PVC resins and added significant products and technology to Westlake's current portfolio. It also improved distributions to emerging markets, improved margins and reduced volatility. With the acquisition of Vinnolit, not only did Westlake Chemical earn a record net income from vinyl operations in its most recent quarter, but they are now the global leader in specialty PVC.

On top of being the leading producer of this product, Westlake is also the largest producer of low density polyethylene (LDPE) in the Americas. Their focus on LDPE is to serve the growing demand for the product predominately in Asian and European markets.





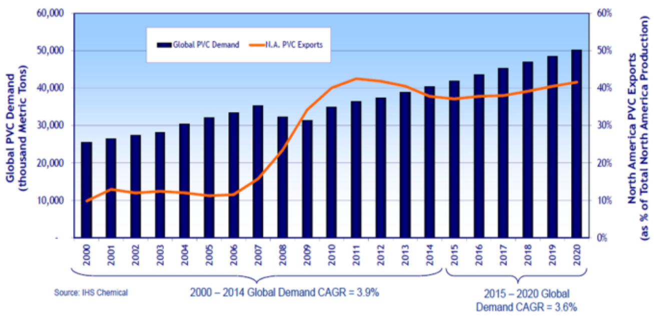
The next key move in place for Westlake is the expansion of their ethylene capacity in Lake Charles, Louisiana. This expansion will cost approximately $330 million, and increase ethylene capacity by approximately 250 million pounds annually.

As evidenced by Westlake's history of expansions, product integrations and acquisitions, the company is always assessing opportunities to see how well they fit into their business strategies. With over $1,000,000,000 cash on hand, Westlake continues to stay prepared for a cash acquisition or an expansion for product capacity whenever a worthy opportunity presents itself.

Long-Term Growth Opportunities

Over the past year, the price of a barrel of oil has decreased by approximately half the price. The most recent price for a barrel of oil is recorded to be $46. This significant drop in oil prices has effected many corporations, including Westlake Chemical. Westlake uses oil as an input for their products, so this decline in oil prices has resulted in lower sales prices for many of the company's top products. Despite lower sales prices, sales from the most current reported quarter increased by $38 million over the previous quarter in the Olefins segment as a result of higher sales volumes. On top of this, the decrease in oil prices has resulted in a higher operating income for both the Olefins segment and the Vinyls segment. The Vinyls segment operating income increased by $41 in its most recent quarter compared to its previous quarter. As a low-cost producer of olefins, vinyls and other products resultant from oil, Westlake is in a solid position for future production.

The core reason Westlake still saw strong growth in both sales and operating income in its most recent quarter despite lower oil prices is due to the demand for their products. Global demand for PVC products has returned to pre-recession levels, and this demand is expected to continue growing. As a low-cost producer of PVC, Westlake is in a great position to supply the necessary demand for this product. As the current global leader in specialty PVC, the long-term outlook in this segment looks more than promising for the company.



Based on the company's move to acquire Vinnolit as the global PVC demand continued to rise, it is evident that Westlake aims to be the global leader for each of their products. The company will continue to watch trends in the industry, and make moves to acquire or expand whatever product line is growing globally in demand. Westlake currently has a cash balance of $1,026,600,000. With this substantial amount of cash on hand, whenever the right opportunity presents itself Westlake is in the position to take it immediately. The company also has negative net debt, meaning they currently have more cash than debt. With oil prices so low, this could potentially be the best time for the company to take on more debt to grow. The global demand for the products they produce combined with their current financial situation creates for many long-term growth opportunities.

Financials –EBITDA margins, zero net debt, dividends

One of the most prominent categories on Westlake Chemical's balance sheet is the EBITDA margins. Westlake's EBITDA margins have consistently outgrown their revenue growth in each of the past five years, and is estimated to continue this trend in the upcoming years. This verifies that the company is creating value, and eliminating operating expenses that are eating into their bottom line. The following chart illustrates Westlake's advantage in EBITDA margins compared to their peer average, as well as their advantages in return on assets and return on capital employed compared to peer averages.

Another noticeable category that has already been mentioned is the company's net debt. With a current net debt of -$262,500,000, the company has more cash than they do debt which should look very promising to investors.

This past August, Westlake announced a 10% increase in its quarterly issued dividend. Including this most recent payout, Westlake has paid 44 straight dividend payments dating back to 2004 when the company went public. This provides a strong message about future expectations, and makes the stock more attractive to investors. It also demonstrates the company's solid financial fundamentals.

On top of all this, Westlake recorded a record net income of $205 million this past quarter. The company is proving that they are moving in the right direction, and all signs show that they will continue moving in this direction.

Conclusion

I am recommending a buy on Westlake Chemical Corporation because they will continue to grow financially as a result of their continued product integration, acquisitions, and long-term growth opportunities resulting from being in an industry of growing demand. Westlake will continue to make the moves necessary to position themselves as the global leaders for their products, and in turn will increase the value of both their company and their share price.

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Westlake Chemical Corp.	WLK	Analyst	Current Price	Intrinsic Value	Target Value	Divident	1-y Return: 15.49%	NEUTRAL
		Mark Papuzza	$58.32	$66.41	$67.32	1%		

General Info	
Sector	Materials
Industry	Chemicals
Last Guidance	August 4, 2015
Next earnings date	November 6, 2015
Market Data	
Enterprise value	$7,824.26
Market Capitalization	$7,773.81
Daily volume	0.77
Shares outstanding	131.94
Diluted shares outstandin	133.36
% shares held by institutio	29.08%
% shares held by insiders	0.47%
Short interest	1.56%
Days to cover short interes	2.33
52 week high	$79.25
52-week low	$49.26
5y Beta	2.11
6-month volatility	34.77%

Peers	Market Cap.
The Dow Chemical Company	$53,880.72
Exxon Mobil Corporation	$330,053.56
LyondellBasell Industries N.V.	$42,990.92

Current Capital Structure	
Total debt/Common Equity (LTM	0.42
Cost of Borrowing (LTM)	4.81%
Estimated Cost of new Borrowin	4.31%
Altman's Z	5.62
Estimated Debt Rating	A
Current levered Beta	1.66
LTM WACC	9.32%

Management

Professional	Title	Comp. FY2012	Comp. FY2013	Comp. FY2014
Chao, Albert	Chief Executive Officer, President,	$5,658,046	$5,753,565	$6,791,588
Bender, M.	Chief Financial Officer, Senior Vice	$1,810,994	$1,873,256	$2,327,181
Hansen, David	Senior Vice President of Administra	$0	$1,281,483	$1,428,975
Mangieri, George	Chief Accounting Officer and Vice P	$0	$0	$0
Ederington, L.	Vice President, General Counsel and	$0	$0	$0
Buesinger, Robert	Senior Vice President of Vinyls	$0	$0	$0

Past Earning Surprises

	Revenue	EBITDA	Norm. EPS	Standard Error of "Surprise"
Last Quarter	5.22%	21.13%	16.53%	4.73%
Last Quarter-1	-2.51%	-3.10%	-8.33%	1.85%
Last Quarter-2	-4.60%	2.22%	-0.72%	1.98%
Last Quarter-3	3.06%	6.95%	1.27%	1.67%
Last Quarter-4	-5.04%	-14.52%	-14.86%	3.22%
Standard error	2.1%	5.9%	5.3%	2.56%
Standard Error of Revenues predictic	2.1%			
Imputed Standard Error of Op. Cost pi	5.5%			
Imputed Standard Error of Op. Cost pi	NM			

Proforma Assumptions

onvergence Assumpti

All base year ratios linearly converge towards the industry ratios over an explicit period of 7 years

General Assumptions	
Money market rate (as of today)	0.27%
Risk-Free rate (long term estimate)	2.94%
Annual increase (decrease) in interest ra	0.1%
Marginal Tax Rate	37.5%
Country Risk Premium	5.5%

Forecast Year	Revenue Growth Forecast	Revenue ($) Forecast
LTM		$4,677.63
FY2015	2.4%	$4,836.59
FY2016	2.2%	$5,091.02
FY2017	4.9%	$5,410.07
FY2018	1.9%	$5,740.07
FY2019	2.0%	$6,077.88
FY2020	2.4%	$6,471.27
FY2021	2.5%	$6,899.08
FY2022	2.8%	$7,380.00
FY2023	2.9%	$7,894.38
FY2024	2.9%	$8,440.46
Continuing Period	3.0%	$9,020.06

Items' Forecast Assumptions

	Base year (LTM)	onvergence period (Industr	ljustment per ye
Operating Cash/Rev.	0.00%	0.00%	0.0%
NWV/Rev.	13.34%	17.96%	0.7%
NPPE/Rev.	61.05%	36.10%	-3.6%
Dep/NPPE	7.49%	13.39%	0.8%
NOPAT MARGIN	15.51%	9.12%	-2.2%
Op. Exp./Rev.	70.98%	82.75%	1.7%
SBC/Rev.	0.21%	0.58%	0.1%
Rent Exp./Rev.	1.20%	1.45%	0.0%
R&D/Rev.	0.00%	2.35%	0.3%
E&D/Rev.	0.00%	0.00%	0.0%
SG&A/Rev.	4.88%	14.41%	1.4%
ROIC	18%	14.42%	-2.63%
EV/Rev.	1.97x	0.00x	-0.28x
EV/EBITA	7.99x	13.87x	0.84x
Debt/Equity	42%	116%	-6.0%
Unlevered beta	1.31	0.85	0.00
Cost of Borrowing	4%	6%	0.3%
Dividends/REV	2%	2%	0.0%

Other Assumptions	
Tobin's Q	80%
Excess cash reinvestment	Cost of capital
Other claims on the firm's ass	$0.00
Capitalization	
100% of all rent expenses are capitalized and amortized 'straightline' over 10 year	
R&D expenses are not capitalized	
E&P expenses are not capitalized	
SG&A expenses are not capitalized	
Valuation Focus	
DCF Valuation	100%
Relative valuation	0%
Distress Valuation	0%
Monte Carlo Simulation Assumptions	
Revenue Growth deviation	Normal (0%, 1%)
Operating expense deviation	Normal (0%, 1%)
Continuing Period growth	Triangular (5.335%, 5.5%, 5.665%)
Country risk premium	Triangular (2.91%, 3%, 3.09%)
Intrinsic value σ(x)	$0.13
1-year target price σ(x)	$0.13

Valuation

Forecast Year	ROIC	WACC	Invested Capital	Enterprise Value	laims on Assets and Dilution	hares Outstandi	Price per Share
LTM	18.4%	9.3%	$4,064.10	$9,187.54	$1,166.75	131.94	$66.88
FY2015	17.3%	9.1%	$5,366.77	$10,718.20	$2,157.72	131.94	$66.62
FY2016	12.7%	8.9%	$5,912.65	$11,378.00	$2,167.36	131.94	$70.40
FY2017	11.3%	8.6%	$6,456.70	$12,169.74	$2,202.85	131.94	$74.45
FY2018	10.1%	8.4%	$6,982.04	$13,001.82	$2,250.32	131.94	$78.50
FY2019	9.0%	8.1%	$7,480.38	$13,867.84	$2,305.26	131.94	$82.67
FY2020	8.1%	7.8%	$7,954.55	$14,771.25	$2,371.33	131.94	$86.85
FY2021	7.4%	7.5%	$8,398.45	$15,700.82	$2,445.44	131.94	$92.13
FY2022	7.5%	7.5%	$8,859.35	$16,723.01	$2,503.99	131.94	$98.00
FY2023	7.6%	7.5%	$9,355.04	$17,814.30	$2,566.91	131.94	$104.17
FY2024	7.7%	7.5%	$9,887.09	$18,977.18	$2,633.86	131.94	$110.66
Continuing Period	14.4%	7.5%	$5,703.29				

Monte Carlo Simulation Results

The 3σ(x)-adjusted intrinsic value i $66.41; the 3σ(x)-adjusted target pric $67.32; and the analysts' median targ price is $63.27

Sensitivity Analysis

Revenue growth variations account for 95.9% of tot
Risk premium's variations account for 2.5% of total
Operating expenses' variations account for 1.4% of
Continuing period growth variations account for 0.2