Continued from page 1

Macroeconomic Overview

All major U.S. indices increased on a weekly basis during the past week. The Dow Jones Industrial Average and S&P 500 closed with record highs after positive market news from Europe. Additional driver of stock prices in the past week were positive earnings reports, and investors speculation that the Federal Reserve will keep interest rates low for a longer period than expected. In effect, the Dow Jones Industrial Average and the NASDAQ Composite, which increased for now eight days in a row, gained 0.51% and 1.16% respectively, while the S&P 500 increased by 0.47% during the last week. Small cap stocks measured by the Russell 2000 index followed their trend of the past week with returns of 0.55%, closing also with a record high. The VIX week-to-date change of -9.49% indicates that volatility levels start to decrease at a slower rate during the past week compared to its year-to-date change of -19.61%. The yield on the 10-year U.S. T-note increased by 11 basis points to 2.13%, indicating that investors' demand for safer investments decreased during the week. The price of oil declined to $50.34 a barrel, after announcements of rising U.S. oil production.

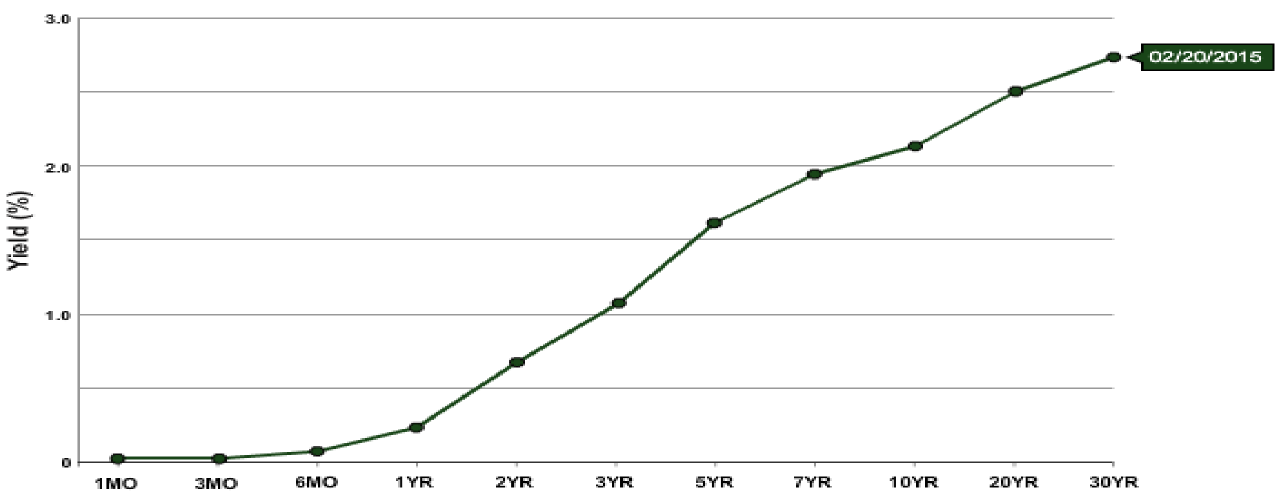
U.S. Stocks		
Index	**% Change Week-to-Date**	**% Change Year-to-Date**
DJIA	0.51%	1.78%
S&P 500	0.47%	2.50%
NASDAQ Composite	1.16%	4.64%
Russell 2000	0.55%	2.10%
VIX	-9.49%	-19.61%

This week's stock price momentum was primarily driven by Greece's debt negotiations. The market reacted positive to reports that Eurozone finance ministers announced a four month extension of Greece's debt maturity, temporarily reducing the risk of Greece defaulting on their loans. In addition, companies keep surprising on the upside and beating earnings in the fourth quarter. The analytics firm FactSet increased their estimates of fourth quarter earnings again from previously an overall earnings growth of 3.1% in the S&P 500 to now 3.5%. The U.S. manufacturing sector grew at a faster rate in February than in the previous month. The Federal Reserve reported about talks to keep rates lower for a longer period than previously expected. Reasons for that are the strong dollar combined with slow U.S. wage growth as well as the global market situation with continuing concerns about Greece and the Ukraine in Europe. Although overall wages in the U.S. are not improving, the labor market sent out positive signs in the past weeks. Less Americans than expected have filed for unemployment benefits in the past week. The Conference Board's index of leading economic indicators increased by 0.2 percent in the month of January, indicating a positive outlook about the economy. However, this increase remained lower than analysts' expectations of 0.3%. Data reports throughout the week indicated a greater than forecasted decline in wholesale prices during the month of January, signaling no increase in inflationary expectations.

Next week, investors will be looking forward to see data from different economic reports that will have an impact on the markets. On Monday 23rd, the Ifo Institute for Economic Research will report on the German Ifo Business Climate Index which rates future expectations of the country's economic outlook. On Tuesday 24th, Germany will report about their Q4 percentage change in GDP. The same day, the Eurozone will release CPI data (YoY) and European Central Bank President Draghi will speak about the economy. On Thursday 26th, Germany will release changes in the country's unemployment rate for February. The same day, the United Kingdom will release GDP data and Canada will report on the country's Core Consumer Price Index.

Bond Report

U.S. government bonds have continued to sell off and prices have fallen for the third week in a row. This comes as the financial ministers of the Eurozone have approved a four-month extension of Greece's financial bailout which has postponed any debt negotiations to take place in the near future. As a result of this, investors continue to sell off their "safe-haven" assets to put their money in to riskier assets. This has continued to push U.S. stock indexes to record highs. Just this past month the yield on a 10 year treasury note has increased 0.457 percentage points, the largest three-week increase since July 2013. On Friday, the 10 year yield closed at 2.02%, it opened on Tuesday at 2.14%. This past Friday it remained relatively flat, closing at 2.13%. U.S. 30-year bond yields have risen to 7-week highs, hitting 2.73% on Tuesday and remaining there until close on Friday. Foreign bond yields continue to fall relatively short to U.S. bond yields. The 10-year yield on German government bonds has declined to 0.350%, as well as declining in the U.K. to 1.766%. The European Central Bank is set to start buying bonds in March, in their latest attempt to stimulate the Eurozone economy as well as limit deflation risks. The Federal Reserve continues to show signs of an interest rate hike this coming June.



What's Next & Key Earnings

On Monday, February 23rd, the Existing Home Sales report will be released. Existing Home Sales measures the change in the annualized number of existing residential buildings that were sold during the previous month. This report helps to gauge the strength of the U.S. housing market and is a key indicator of overall economic strength.

On Tuesday, February 24th, the Conference Board will release the Consumer Confidence report. Conference Board (CB) Consumer Confidence measures the level of consumer confidence in economic activity. It is a leading indicator as it can predict consumer spending, which plays a major role in overall economic activity. Higher readings point to higher consumer optimism.

On Tuesday, February 24th, Janet Yellen will testify to Congress on the economic outlook as well as recent monetary policy actions. The testimony is in two parts; the first is a prepared statement, then the committee conducts a question and answer session. The Q&A portion of the testimony can see heavy market volatility for the duration. She will continue to testify on Wednesday.

On Wednesday, February 25th, the New Home Sales report will be released. New Home Sales measures the annualized number of new single-family homes that were sold during the previous month. This report tends to have more impact when it's released ahead of Existing Home Sales because the reports are tightly correlated. Pending Home Sales will be released on Friday.

On Thursday, February 26th, the Core Durable Goods Orders figures will be released. Core Durable Goods Orders measures the change in the total value of new orders for long lasting manufactured goods, excluding transportation items. Because aircraft orders are very volatile, the core number gives a better gauge of ordering trends. A higher reading indicates increased manufacturing activity.
On Thursday, February 26th, the Core Consumer Price Index figure will be released. The Core Consumer Price Index (CPI) measures the changes in the price of goods and services, excluding food and energy. The CPI measures price change from the perspective of the consumer. It is a key way to measure changes in purchasing trends and inflation.
On Friday, February 27th, the GDP QoQ figure will be released. Gross Domestic Product (GDP) measures the annualized change in the inflation-adjusted value of all goods and services produced by the economy. It is the broadest measure of economic activity and the primary indicator of the economy's health.

Symbol	Company	EPS	Forecast	Prev.	Imp.	Period End
	Monday, February 23, 2015					
AGU	Agrium		1.21	0.60		12/2014
DISH	DISH Network		0.43	0.31		12/2014
ESRX	Express Scripts		1.38	1.29		12/2014
AG	First Majestic Silver		0.05	-0.04		12/2014
ASR	Grupo Aeroportuario Sureste		1.75	1.44		12/2014
OKE	ONEOK		0.36	0.31		12/2014
THC	Tenet Healthcare		1.18	0.74		12/2014
	Tuesday, February 24, 2015					
AMT	American Tower		0.51	0.5		12/2014
AWK	American Water Works		0.51	0.92		12/2014
CMCSA	Comcast		0.78	0.73		12/2014
CMCSK	Comcast Special A		0.78	0.73		12/2014
ECL	Ecolab		1.2	1.21		12/2014
EIX	Edison		0.83	1.52		12/2014
EXPD	Expeditors Washington		0.49	0.53		12/2014
FSLR	First Solar		0.76	0.61		12/2014
HPQ	Hewlett-Packard		0.91	1.06		01/2015
HD	Home Depot		0.89	0.73		12/2014
M	Macy's Inc		2.4	0.61		01/2015
MATX	Matson		0.58	0.5		12/2014
NFX	Newfield Exploration		0.44	0.52		12/2014
OIBR	Oi		0.17	0.00		12/2014
PLL	Pall		0.87	0.89		01/2015
PBR	Petroleo Brasileiro- Petrobras		0.33	0.41		12/2014
QEP	QEP Resources		0.25	0.41		12/2014
RRC	Range Resources		0.28	0.37		12/2014
SKM	SK Telecom		7,893.92	-		12/2014
VRX	Valeant		3.21	2.11		12/2014
VRSK	Verisk		0.63	0.64		12/2014
WIN	Windstream		0.03	0.03		12/2014

Wednesday, February 25, 2015				
ABEV	Ambev SA	0.3	0.18	12/2014
AEE	Ameren	0.13	1.2	12/2014
AVGO	Avago	1.93	-	01/2015
CVC	Cablevision Systems	0.19	0.26	12/2014
CPB	Campbell Soup	0.66	-	01/2015
CHK	Chesapeake Energy	0.25	0.38	12/2014
KOF	Coca Cola FemsaB	1.7	1.20	12/2014
DLTR	Dollar Tree	1.15	-	12/2014
ESV	ENSCO	1.36	1.87	12/2014
ECA	Encana	0.34	0.38	12/2014
GGAL	Grupo Financiero Galicia	-	0.85	12/2014
TEG	Integrys Energy	0.77	0.35	12/2014
LB	L Brands	1.8	-	01/2015
QVCA	Liberty Interactive	0.48	0.25	12/2014
LMCA	Liberty Media	0.16	0.10	12/2014
LMCK	Liberty Media Co	0.16	0.10	12/2014
LVNTA	Liberty Ventures	0.45	0.50	12/2014
LOW	Lowe's	0.44	-	12/2014
MGA	Magna	2.83	2.22	12/2014
RY	Royal Bank Of Canada	1.58	1.27	01/2015
CRM	Salesforce.com Inc	0.14	0.14	01/2015
SPNS	Sapiens	0.09	0.08	12/2014
TJX	TJX	0.9	-	01/2015
TGT	Target	1.46	-	12/2014
RIG	Transocean	0.78	0.96	12/2014
UGP	Ultrapar Participacoes	0.64	0.30	12/2014
VIP	VimpelCom	-	-	12/2014

Thursday, February 26, 2015				
ADSK	Autodesk	0.24	0.25	01/2015
BFR	BBVA Banco Frances	-	-	12/2014
CTRX	Catamaran	0.78	0.58	12/2014
CNP	CenterPoint Energy	0.26	0.30	12/2014
FMX	Fomento Economico Mexicano	1.78	1.24	12/2014
GMK	GRUMA	2.01	0.76	12/2014
GPS	Gap	0.74	-	12/2014
KSS	Kohl's	1.8	0.7	12/2014
MNST	Monster Beverage	0.59	0.70	12/2014
PKX	POSCO	6,722.03	-	12/2014
RBA	Ritchie Bros Auctioneers	0.38	0.13	12/2014
ROST	Ross Stores	1.11	-	12/2014
SBAC	SBA	0.02	-0.13	12/2014
SRE	Sempra Energy	1.09	1.39	12/2014
SWN	Southwestern Energy	0.5	0.5	12/2014
AES	The AES	0.34	0.28	12/2014
UHS	Universal Health Services	1.5	1.36	12/2014
VALE	VALE	-	0.13	12/2014
Friday, February 27, 2015				
ICA	Empresas Ica Soc Contrladora	0.16	-	12/2014
HDB	HDFC Bank	13.57	-	12/2014
LUK	Leucadia National	-	-	12/2014
NRG	NRG	0.52	0.62	12/2014
POM	PEPCO	0.2	0.46	12/2014
TEO	Telecom	1.01	0.62	12/2014

Ardmore Shipping Corp (ASC: NYSE)

Financial Analysis By: Hugo Perrin – Industrials

<u>Company Profile as of 02/18/2015</u>

Market Price: $10.66
Industry: Oil and Gas Transportation
Market Cap: $277.66M
52-Week: $8.25 – $14.97
Beta: 12.7

Source	Target Price	Recommendation
Siena College	13.86	BUY
Capital IQ	15.50	BUY
Yahoo Finance	15.92	BUY
Bloomberg	16.07	BUY

<u>Thesis</u>

-Positive Industry Outlook
-International Presence
-Growing Fleet
-Organic growth

Ardmore Shipping Corporation currently operates a fleet of 18 vessels and will operate an additional 10 tankers during the year 2015. The firm has always operated likewise, leading to a meaningful yearly increase of its revenues since its inception in 2010. Presently, the firm focuses on growing its fleet with brand new vessels that are cost efficient and that will generate higher revenues; therefore, enhancing margins. The growing fleet is a key aspect considering the future of the firm as it is the main reason that drives the firm's value. The current oil market is favorable for Ardmore due to the relative volatility. Additionally, the current experienced firm management team is captivating every opportunity to take advantage of the current commodity market and will continue to increase its operations with the overall world's economic recovery, especially in the US.

<u>Company Overview</u>

Ardmore Shipping, created in 2010 by Anthony Gurnee, owns and operates a fleet of mid-size product and chemical tankers ranging from 17,500 Dwt (Deadweight tonnage) to 50,300 Dwt. The deadweight tonnage is a measure of how much weight a ship is carrying or can safely carry. The company provides seaborne transportation of petroleum products and chemicals worldwide to oil majors, national oil companies, oil and chemical traders, and chemical companies, with their modern, fuel-efficient fleet of tankers.

Ardmore's core strategy is to develop a modern, high-quality fleet of product and chemical tankers, build key long-term commercial relationships, maintain its cost advantage in assets, operations and overhead, while creating significant synergies and economies of scale as the firm grows. The company provides its services to customers through voyage charters, commercial pools and time charters and enjoys close working relationships with key commercial and technical management partners. The firm views the continued development of these relationships as crucial to its long-term success. The firm is currently based in Hamilton, Bermuda; this allows an exemption of income taxes. Since its creation, the firm has not paid income taxes; it is only in 2014 that the company paid as low as 2% of income tax.

Management

Anthony Gurnee, the founder and currently Ardmore's CEO has spent his entire career on the naval industry. He graduated from the US Naval Academy and holds a MBA degree from Columbia Business School. He is also a Chartered Financial Analyst (CFA). Gurnee started his career as a shipping banker with Citicorp, prior to which he served for six years in the US Navy as a surface line officer and as an intelligence analyst on merchant shipping activity. Prior creating Ardmore Shipping Corporation, he was the CFO OF Teekay Shipping Corporation, where he led the firm's financial restructuring and initial public offering. He also co-founded Navigation Finance Corporation, a shipping-focused investment fund.

Reginald Jones, the Chairman and Director of Ardmore Shipping Corp. earned a BA from Williams College and an MBA from the Harvard Business School. Prior coming to Ardmore, Jones spent thirteen years at Goldman Sachs & Co., where he was a Managing Director and Group Head of global transportation investment banking. Jones is also the co-founder and Managing Partner of Greenbriar Equity Group LLC, a firm focused on making privately negotiated investments within the global transportation industry, closely linked to Ardmore Shipping Corporation.

Ardmore's operation segmentation:

Ardmore Shipping Corp. operates two distinct services. The first one is the shipping of oil through the company's product tankers and the other one is the shipping of organic chemicals through chemical tankers

Product tankers:

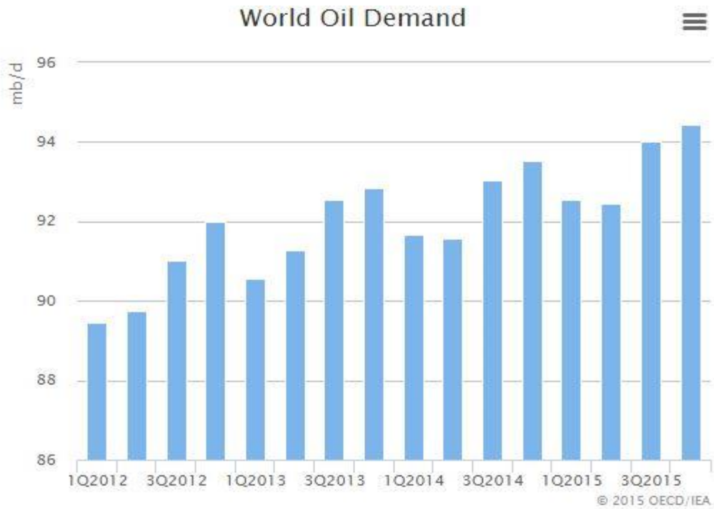
Ardmore is transporting a wide variety of refined petroleum products. It comprises gasoline, jet fuel, kerosene, fuel oil and naphtha. This segment of the company's operation is the most profitable and the one where most of the fleet is dedicated to.

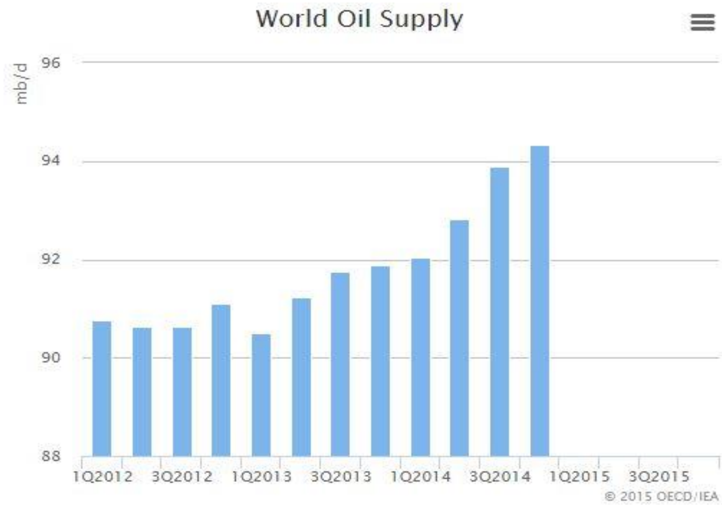
Chemical tankers:

The firm is also carrying organic chemicals, inorganic chemicals and vegetable oils. Also, those vessels designed for the transport of chemicals and also be used for less sophisticated cargos such as molasses, lube oils and refined petroleum products. It is interesting to consider that such vessels can be used for the other type of transportation that Ardmore Shipping Corp, refined oil. In case of an opportunity in the oil sector, the firm could requisition some if its chemical tankers to benefit from an upside demand in the market. However, as explained later, the firm is constantly making deliveries of vessels every year.

Oil Demand:

Since Q3 2014, the price of oil declined by more than 50%, coming from around $100/bbl to currently $46/bbl as of Q1 2015, a level that has not been reached since 2009. This sharp decline in oil price could translate potential difficulties for the firm; however, it is rather beneficial for Ardmore Shipping Corp.





The chart on the left provided by the International Energy Agency (IEA) states the World Oil Demand during the last quarter and shows a forecast for the coming year. The decline in the oil price was driven by higher than expected supply, which has consequently; cut the price of the commodity, as proven by the chart on the right, picturing the World Oil Supply.

As a result, the company's fourth quarter 2014 "has added an extra layer of demand" as reported by the Q4 2014 Earning Call. It is also due to the high volatility of the crude oil that the firm has increased its revenue. This has resulted in more refined products moving at sea and an increase in long-haul arbitrage trade. As most of the firm clients' are oil traders, they want to take to best opportunity for cheap oil. The volatility has been more extreme on a regional scale, which has forced oil traders to favor long-haul trading activity for Ardmore Shipping Corp. The firm is specialized in long-haul products thanks to its fleet. It is to be underlined that the firm is taking advantage of the current situation mainly because of the volatility in oil prices.

Since Q3 2014, the volatility of oil prices has constantly increased from the 20% level to currently around 60% implied volatility. Several reports predict to oil price going in the range of $20 to $75 during the year 2015, proving at least the same volatility as what the market experienced during the last two quarters; a positive aspect for the firm activities.

As for the production sites, the USA is the biggest producer, after overtaking Saudi Arabia and Russia, with 12.34 millions of barrels per day, versus 11.70 and 10.76 million barrel per day. Forecasts predict that U.S Gulf exports will grow in the near future. This is particularly convenient for the firm as its mitigate the risk for piracy acts or terrorists attacks against the firm's vessels in the costs of Somalia, Guinea, South China Sea and the Gulf of Aden.

However, the firm predicts that the growth in exports for refined products is happening in Middle East and India. Due to the international environment of the company, operating in promising markets and geographic areas would be feasible due to the current policy of Ardmore of increasing its fleet.

<u>The Fleet:</u>

As of Q1 2015, the firm is scheduled to increase its fleet by 10 new tankers. Four of them will be tankers and will enter in a proprietary spot trading arrangement with a leading oil firm. The remaining six vessels will be hybrid, meaning that they will be able to exploit both markets depending on their strengths at the time.

On the current operating vessels, the majority is exclusively dedicated to product transportation, 2 of the 20 vessels can be considered as hybrid where they can transport both products and chemicals, and the remaining are chemical transportation vehicles. The current fleet has an average age of 4 years, meaning that all of them are relatively modern, fuel-efficient and reliable. Ardmore is not currently considering selling off its oldest vessels (2005) as they are still performing well, but it is not something that the firm is considering. This will logically ease the firms' free cash flow.

One of the vessels set to be delivered in 2015 is already in service, and will boost revenue days by approximately 70% by the end of the year; which will boost earnings and cash flow capacity.

In Q4 2014, the MR (Medium Range) product tankers delivered earnings of $18,500 per day versus an average of $16,000 prior year, a 16% increase. This increase was mainly due to seasonality but also, the drop and volatility in oil prices.

The firm's existing fleet of chemical tankers has increased their earnings per day on Q4 2014 versus Q4 2013 from $10,473 to $11,456, or 9.4%. The chemical tankers fleet carries roughly equal thirds refined products, vegoils and bio-fuels, and commodity chemicals. This segment's performance lagged versus the oil segment but it is set to increase rapidly due to the strengthening global economy that will normally boost chemical tanker demand. According to the American Chemistry Council, the petrochemical exports from US Gulf are expected to increase 45% by 2018.

In less than 5 years of operations, the firm is successfully managing 10 vessels and will double to 20 by the end of 2015, showing the relative growing opportunities in this market that proves not to be saturated.

The firm is focused on vessel deliveries, which will boost its earnings capacity by 70% by year-end if forecasted are set to realize. All vessels that are currently under construction are financed through bank loans, which enables the firm some financial flexibility in executing its growth strategy.

The new vessels coming in 2015 will be more cost efficient, whether in terms of maintenance or fuel-efficiency. By combining the idea that its will increase the capacity of the firm by 70% in daily earnings, and the cost efficiency of those same boats, Ardmore Shipping Corporation will have better margins in the future.

Ardmore Shipping will not continually increase its fleet on that percentage basis every year, meaning that the CapEx will decrease overtime, but the revenue increase should sustain for a longer period of time if all new vessels will boost the firm's earnings capacity by a double digit number, as it is currently the case.

A positive consequence of the addition of 10 new vessels during FY 2015 will lead to a decrease in operating costs. As more tankers will be deployed around the world, the likelihood that one of them to be around a location where Ardmore will do an operation will be higher, and therefore, will reduce the costs of operation. The current low price of oil is also another factor that will drive the operating costs to be lower that year. By combining the idea that the firm will be delivered fuel-efficient tankers and the cheap price of oil, this will also reduce the firm's costs of running those tankers and increase its margins.

Key Statistics:

In Millions of USD	FY 2010	FY 2011	FY 2012	FY 2013	FY 2014	Current/LTM	FY 2015 Est	FY 2016 Est
12 Months Ending	2010-12-31	2011-12-31	2012-12-31	2013-12-31	2014-12-31	2014-12-31	2015-12-31	2016-12-31
Revenue	3.5	22.4	25.2	35.9	67.3	67.3	115.4	144.6
Growth %, YoY	--	546.8	12.5	42.5	87.7	87.7	71.4	25.3
Gross Profit	0.3	2.7	1.9	6.7	16.0	16.0	74.1	
Margin %	9.4	12.1	7.5	18.8	23.8	23.8	64.2	
EBITDA	0.4	5.5	4.7	10.2	23.6	23.6	60.9	80.1
Margin %	12.5	24.4	18.5	28.5	35.1	35.1	52.8	55.4
Net Income Before XO	-1.2	-3.0	-4.5	-3.8	1.7	1.7	20.8	33.1
Margin %	-33.8	-13.3	-18.0	-10.7	2.5	2.5	18.0	22.9
Adjusted EPS	--	--	--	-0.31	0.07	0.05	0.97	1.26
Growth %, YoY	--	--	--	--	--		1,284.3	30.1
Cash from Operations	--	0.4	4.0	8.1	12.4	12.4	46.1	63.8
Capital Expenditures	--	-56.8	-14.9	-144.6	-209.7	-209.7	-213.5	-2.0
Free Cash Flow	--	-56.4	-10.9	-136.4	-197.3	-197.3	-167.4	61.8

The table above shows the firm's key statistics since 2010. Ardmore Shipping Corporation has been able to significantly increase its revenue since inception. However, it is to be considered that as the firm in is development mode, so it is rather logical for it to have such figures.

Nonetheless, the firm is constantly increasing its margins due to the acquisition of more cost-efficient vessels. Every time the firm increases its revenues, it is also significantly increasing its margins in the meantime.

The firm's revenue growth has been conducted without any acquisitions, highlighting the idea that Ardmore has the know-how to operate organic growth and taking advantage of the current market opportunities. The current CEO claims that "it is an interesting time to consider acquisitions", but does not put that as his top priority, rather focusing on the growth into the actual fleet.

It has to be noted that the insiders do not held any outstanding shares. However, GA Holdings, which currently hold 32% of the shares outstanding is a firm held at 98.6% by Greenbriar Equity LLC, founded by Reginald Jones, the Chairman and Director of Ardmore. This means that Jones, with two other persons have the voting and investment power with respect to shares of the company held by GA Holdings LLC.

Ardmore Shipping profitability versus the industry average:

	Name	Trailing 12M Sales Growth	Trailing 12M Operating Margin	Trailing 12M Gross Margin	Capex/Sales	Return on Assets	Return on Equity	Return on Capital
	Average	11.64%	10.13%	26.40%	46.83%	1.00%	3.30%	3.19%
100)	ARDMORE SHIPPING CORP	87.71%	8.63%	23.79%	95.63%	0.36%	0.59%	1.24%

On the chart above, Ardmore seems to be less profitable compared to its competitors. However, as stated above, this will rapidly change as soon as this current fiscal year. The firm's gross margin will be more than two times higher as the average industry. Ardmore's return on assets is still low but is increasing on a yearly basis, coming from negative 2.36% in 2012 to positive 0.36% in 2014. The path was the same for the return on equity. It is the first year that the return on capital is computed, being two times lower than the industry average, but is set to increase significantly increase due to the reasons stated above.

Also, the CapEx over sales ratio is significantly high, due to the current purchase of new product and chemical tankers. However, it seems that this policy will not be in place for the coming years. As the firm is not going to sell its oldest vessels and is accumulating new ones, the CapEx will decrease overtime. Consequently, a smaller CapEx with a constant improvement in the firm EBIT will rapidly add value to the firm. Currently, the firm has a high EBIT/Interest expense at 1.41, but it should logically decrease considering the future continuing growth in EBIT margins.

The outlook for Ardmore seems solid for the long-term if the firm can continue to grow its revenue by keeping a significant EBIT margin as this should be the case for the next two years. With a fleet that will almost double in size, the firm will generate a significant increase in revenues while cutting its costs. The overall current economic and commodity market is in favor of Ardmore Shipping Corp which will help the firm to post positive net income for the second consecutive year after 2013.

Continued from page 1

CENTER FOR GLOBAL FINANCIAL STUDIES

Ardmore Shipping Corporation	ASC	Analyst	Current Price	Intrinsic Value	Target Value	Divident Yield	Target Return	BULLISH
		Hugo Perrin	$10.70	$12.20	$13.86	4%	33.25%	

General Info

Sector	Energy
Industry	Oil, Gas and Consumable Fuels
Last Guidance	(Invalid Identifier)
Next earnings date	NM

Market Data

Enterprise value	$452.92
Market Capitalization	$279.27
Daily volume	0.11
Shares outstanding	26.10
Diluted shares outstanding	24.55
% shares held by institutions	67.25%
% shares held by insiders	0.00%
Short interest	3.53%
Days to cover short interest	6.62
52 week high	$14.97
52-week low	$8.25
5y Beta	0.00
6-month volatility	38.62%

Peers	Market Cap.
Golar LNG Ltd.	$2,976.10
Scorpio Tankers Inc.	$1,352.86
Nordic American Tankers Limited	$930.17
DHT Holdings, Inc.	$679.95
Frontline Ltd.	$386.51
Teekay Tankers Ltd.	$660.20
GasLog Ltd.	$1,593.13
StealthGas, Inc.	$267.10
Navios Maritime Acquisition Corporation	$541.44
Diana Shipping Inc.	$598.75

Current Capital Structure

Total debt/market cap	51.56%
Cost of Borrowing	2.34%
Interest Coverage	141.05%
Altman Z	0.97
Debt Rating	AAA
Levered Beta	1.83
WACC (based on market value weights)	8.29%

Management

Professional	Title	Comp. FY2012	Comp. FY2013	Comp. FY2014
Gurnee, Anthony	Founder, Chief Executive Office	$ -	$ -	$ -
Tivnan, Paul	Chief Financial Officer, Chief Acc	$ -	$ -	$ -
Cameron, Mark	Chief Operating Officer	$ -	$ -	$ -
Docherty, Gerry	Director of Technical Services	$ -	$ -	$ -
Ruppelt, Gernot	Director of Chartering and Busin	$ -	$ -	$ -
Cogan, Simon	Financial Controller	$ -	$ -	$ -

Historical Performance

	ASC	Peers	Industry	All U.S. firms
Growth	10.7%	-3.1%	8.8%	6.0%
Retention Ratio	0.0%	-32.2%	59.8%	61.6%
ROIC		-3.4%	22.0%	11.8%
EBITA Margin	0.0%	26.8%	17.9%	13.7%
Revenues/Invested capital	12.8%	22.4%	139.1%	202.3%
Excess Cash/Revenue	#DIV/0!	28.2%	10.6%	18.5%
Unlevered Beta		0.76	0.61	0.95
TEV/REV	8.0x	5.6x	3.1x	2.4x
TEV/EBITDA	31.5x	10.8x	14.7x	11.3x
TEV/EBITA	80.1x	18.5x	19.4x	15.4x
TEV/UFCF		11.7x	39.6x	26.8x

Past Earning Surprises

	Revenue	EBITDA	Norm. EPS
Last Quarter	5.1%	9.9%	60.0%
Last Quarter-1	1.4%	7.6%	
Last Quarter -2	-2.2%	7.0%	
Last Quarter -3	0.2%	13.8%	
Last Quarter -4	-5.3%	-41.7%	

Non GAAP Adjustments

Operating Leases Capitalization	100%	Straightline	10 years
R&D Exp. Capitalization	100%	Straightline	10 years
Expl./Drilling Exp. Capitalization	0%	N/A	N/A
SG&A Capitalization	0%	N/A	N/A

Proforma Assumptions / **Forecasted Profitability**

		Period	Rev. Growth	Adj. Op. Cost/Rev	Revenue	NOPLAT	Invested capital	UFCF
Operating. Cash/Cash	0.0%	LTM	88%	67%	$67.33	$5.14	$500.85	$5.14
Unlevered Beta	1.20	LTM+1Y	71%	63%	$115.40	$17.62	$502.62	$15.85
Rev/Invested Capital	100.0%	LTM+2Y	25%	61%	$144.59	$24.63	$503.55	$23.70
Continuing Period Revenue Growth	4.0%	LTM+3Y	9%	61%	$157.05	$27.19	$503.92	$26.82
Long Term ROIC	13.1%	LTM+4Y	10%	61%	$173.20	$30.32	$504.41	$29.83
Invested Capital Growth	Equals to Maintenance	LTM+5Y	8%	61%	$186.63	$32.70	$504.81	$32.31
Justified TEV/REV	3.0x	LTM+6Y	6%	61%	$198.40	$34.62	$505.20	$34.23
Justified TEV/EBITDA	14.7x	LTM+7Y	5%	61%	$209.19	$36.25	$505.55	$35.89
Justified TEV/EBITA	19.4x	LTM+8Y	5%	61%	$219.40	$37.67	$505.89	$37.33
Justified TEV/UFCF	30.0x	LTM+9Y	5%	62%	$229.28	$38.97	$506.22	$38.64

Valuation

	ROIC	WACC	EVA	Enterprise Value	Total Debt	Other claims	Equity	Adjusted Price
LTM	1.0%	8.3%	-$36.38	$507.32	$233.53	-$59.88	$333.67	$13.01
LTM+1Y	3.5%	8.6%	-$25.39	$551.25	$233.53	-$58.71	$376.44	$14.76
LTM+2Y	4.9%	8.7%	-$19.39	$581.88	$233.53	-$84.19	$432.54	$16.82
LTM+3Y	5.4%	8.9%	-$17.59	$607.06	$233.53	-$106.88	$480.42	$18.63
LTM+4Y	6.0%	9.0%	-$15.19	$631.72	$233.53	-$125.29	$523.48	$20.31
LTM+5Y	6.5%	9.2%	-$13.53	$655.99	$233.53	-$150.97	$573.43	$22.29
LTM+6Y	6.9%	9.3%	-$12.32	$680.42	$233.53	-$177.34	$624.23	$24.18
LTM+7Y	7.2%	9.4%	-$11.31	$705.70	$233.53	-$204.11	$676.28	$26.19
LTM+8Y	7.5%	9.5%	-$10.58	$732.27	$233.53	-$233.34	$732.08	$28.34
LTM+9Y	7.7%	9.7%	-$9.87	$760.08	$233.53	-$263.46	$790.02	$30.27

Monte Carlo Simulation Assumptions

	Base	Stdev	Min	Max	Distribution
Revenue Variation	0	10%	N/A	N/A	Normal
Op. Costs Variation	0	10%	N/A	N/A	Normal
Market Risk Premium	6%	N/A	5%	7%	Triangular
Long term Growth	4%	N/A	-3%	11%	Triangular

Monte Carlo Simulation Results

	Intrinsic Value	1y-Target
Mean est.	$13.01	$14.76
σ(ε)	$0.27	$0.30
3 σ(ε) adjusted price	$12.20	$13.86
Current Price	$10.70	

Dominion Diamond Corporation (DDC: NYSE)

Financial Analysis By: Issam Kaisse – Basic Materials

<u>Company Profile as of 02/14/2015</u>

Market Price: $16.55
Industry: Nonmetallic Mineral Mining
Market Cap: 1.41B
52-Week: $11.81 - $18.50
Beta: 0.68

Source	Target Price	Recommendation
Siena	$18.70	BUY
Bloomberg	$20.22	BUY
Capital IQ	$21.40	OUTPERFORM
Yahoo Finance	$20.14	BUY

<u>Thesis</u>

-Attractive Fundamentals
-Production expansion
-Strategic acquisitions and alliances
-International Expansion and Opportunities

As the price of rough diamonds prices are expected to increase by 2018, Dominion Diamond Corporation (DDC) is a company well positioned to benefit from the growing appetite for these precious stones. DDC is a buy at the current price of $16.55 and has a target price of $18.70, a potential upside of 13%. The stock is considered undervalued despite savvy financial management and strategic acquisitions that will enable the company to be the third largest producer of rough diamonds in the world. Dominion Diamond Corporation is well positioned to supply fast growing market for diamond jewelry sales in countries like China and India. Also, the increasing diamond output for DDC and lower oil prices will give the firm a competitive advantage and improve margins starting 2015.

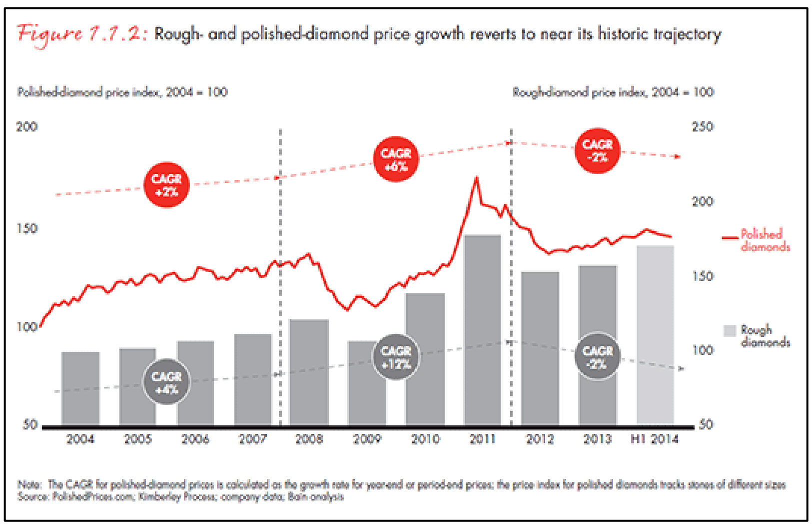
Overall, Dominion Diamond Corporation is a hidden gem because it has ownership interests in two of the world's most valuable diamond mines in Canada with political risk environment.

Company Overview

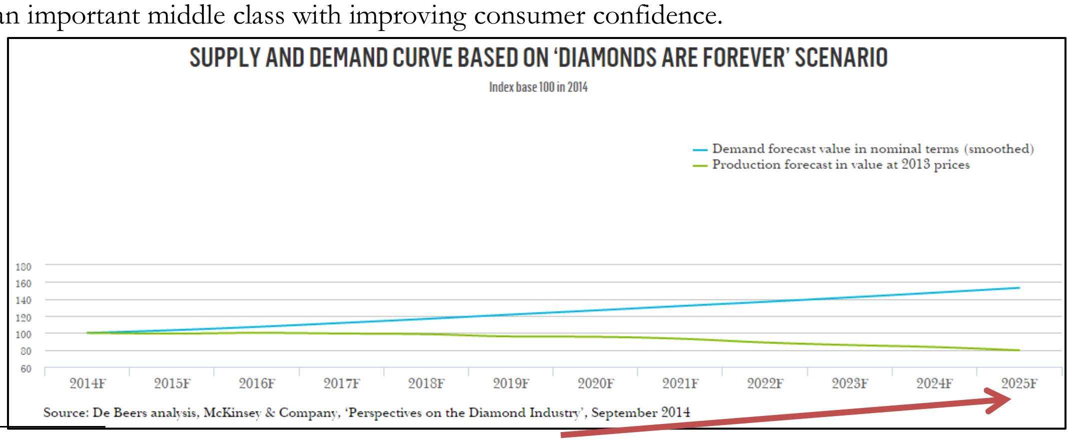
Dominion Diamond Corporation focuses on the mining and marketing of rough diamonds worldwide. DDC is a Canadian diamond mining company with ownership interests in two major producing diamond mines situated in Canada's Northwest Territories. The firm operates the Ekati Diamond Mine with an 80% ownership and maintains 40% of the Diavik Diamond Mine. DDC supplies rough diamonds to the global market through its selling operations in Canada, Belgium and India. The company was formely known as Harry Winston Diamond Corporation and changed its name in March 2013 after it decided focusing on diamond production as well as selling jewellery stores to Swatch Group of Switzerland last year. Dominion Diamond Corporation does not operate the Diavik Diamond mine. The mine is operated by Diavik Diamond Mines Inc., a subsidiary of Rio Tinto, one of the largest and most highly regarded mining companies. Under the joint arrangement, Rio Tinto operates the mine and Dominion Diamond pays 40% of the mine's operating and capital costs while receiving 40% of the mine's diamond output. DDC is keen to buy control of Canada's Diavik mine from Rio Tinto if the global mining group is ready to sell its diamonds business.

Industry Outlook

Starting 2013 the diamond market started to show signs of sustainable growth and developments in the diamond industry. The global production of rough diamond in 2013 jumped by 7% over 2012 levels and consumer demand continues to increase every year and there is a clear opportunity growth. The diamond value chain posted solid growth since demand from countries like China and India is constantly growing. As we can see on the graph below, prices of both rough and polished diamonds show moderate growth in the first half of 2014.



According to McKinsey & Company's report[1] it is expected that diamond prices are going to rise by 5.5% per year over the next 5 years. The report also signals that demand will outpace supply over the next 5 years and projects the rough diamond demand to grow by 5.8% per year over the next 5 years. Demand for rough diamond has recovered significantly since 2012 because the US is leaving the crisis behind and we are seeing pre-2008 levels again. China and India are also experiencing rapid growth in the rough diamond market because there is an important middle class with improving consumer confidence.



[1] http://insightreport.debeersgroup.com/diamond-industry-outlook/index.html

Attractive Fundamentals

Dominion Diamond Corporation is well positioned financially and keeps improving its fundamentals versus its competitors. The company has a strong balance sheet before even taking advantage of the acquisition of the two of the richest producing diamond mines in the world. As the firm slide below indicates, DDC keeps looking for ways to improve its financials.

Fiscal Year 2015 – Third Quarter (in millions of US dollars except where otherwise noted)		
Opening net cash at July 31, 2014		**384.0**
Cash flow from operations for the period		72.3
Capital expenditures for the period (net of Misery pre-production revenue)		(22.8)
Cash tax paid for the period		(1.2)
Net interest paid during the period		(0.5)
Acquisition of additional interest in Ekati		(27.5)
Other		(3.5)
Closing net cash at October 31, 2014		**400.8**
FCF[1] generated during Q3 fiscal 2015		**35**
Debt		46
Diamond Inventory at October 31, 2014		
At cost		235
Estimated market value		**350**

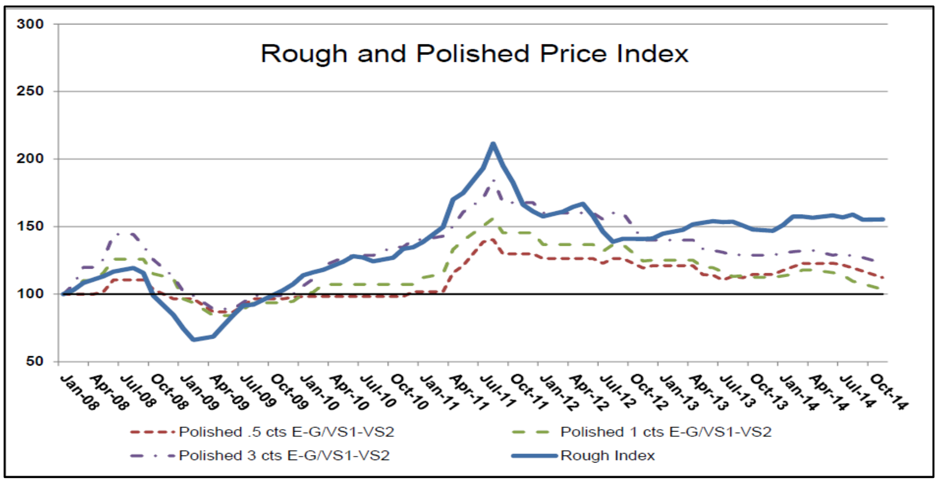
We can clearly see a strong growth potential in this Canadian firm because it has the financial ability ahead of the development of some interesting projects such as Jay project and A21. In fact, the company held $289 million of cash and cash equivalents and $112 million of restricted cash as it wants to develop its mines and secure itself from any financial instability that could occur from the pull back in credit available to the diamond industry from banks. Also, the company has a diamond inventories with a market value of $350 million since they believe that the price of rough diamond will increase in the coming quarters and it is more beneficial to help precious diamond when the price becomes attractive. From a cash flow perspective, DDC was able to generate a consolidated free cash flow of $35 million for the Q3 of 2015 because its existing mines produced high quality carats that increased the revenue. Since the company has enough cash, it allows itself to increase its stake in several mines. As a matter of fact, DDC purchased an additional 16% of two Ekati zones from Chuck Fipke for a total of $70 million. Thus, the sufficient capital on hand will enable the company to fund its capital expenditures and pay its small amount of debt that does not exceed $46 million each year.

	Q3 2015	Q3 2014	YOY Change	Q3 YTD 2015	Q3 YTD 2014	YOY Change
Sales[1]	**222.3**	148.1	50%	**675.2**	518.8	*+30%*
Cost of Sales	**147.0**	136.2	8%	**505.9**	448.8	*13%*
Gross Margin (%)	**33.9%**	8.0%	+2590bp	**25.1%**	13.5%	*+1160bp*
Selling general & administration	**7.9**	7.4	+7%	**24.7**	39.3	*-37%*
Operating profit from continuing operations[1]	**67.5**	4.5	+1397%	**144.6**	30.6	*+372%*
Cash Costs of Production[2]	**121.7**	128.7	-5%	**365.0**	322.0	*+13%*
EBITDA from continuing operations[2]	**115.4**	36.5	+216%	**294.6**	115.5	*+155%*
EBITDA Margin (%)[2]	**52%**	25%	+2700bp	**44%**	22%	*+2200bp*
Earnings per share	**0.30**	(0.06)	631%	**0.78**	(0.18)	*539%*

Sales of DDC increased from $148 million in Q3 of 2014 to $222 million in Q3 of 2015 because the company was able to improve its production and carat extraction. Dominion Diamond is constantly trying to decrease its cost of sales as well as SG&A expenses against peer companies because they are increasing their energy efficiency with new operating approaches such as generators, heat exchangers, and incinerators. Also, DDC continues to improve margins at both production and sales levels as it believe it is the only way to attain its growth potential. Thus, EBITDA for this quarter was $115 million compared to $37 million for the same period last year. The company expects to recover quality rough diamonds from its existing mines in early calendar 2016 and the future looks bright with attractive projects beyond 2019 that will improve the companies' fundamentals. DDC expects a positive fourth quarter because it is the main period for consumption in the world's biggest market, the US. In fact, diamond shops and manufacturers restock their inventory during that period because they are anticipating a positive demand for jewelry. On its recent earnings call, the management team announced to initiate a dividend as they want to send a positive note to the stakeholders that they can both fund their expansion plans for the business as well as sustain regular distribution to their shareholders.

Production Expansion

Dominion wants to start building a new jay pipe at its Ekati mine in the summer of 2016. The Jay project would add 10 years to the mine and is expected to open in late 2019 when the reserves at the existing Ekati operation run out. Currently, the firm will use a pipe called Misery in 2016 until the Jay pipe is achieved. The company sees the Jay pipe as a large scale development asset because in its feasibility study of January 2015 the CEO stated "completing this pre-feasibility study is an important milestone for Jay, a project that we hope will be a significant growth opportunity for the company"[2]. Throughout the feasibility study, DDC expects the Jay pipe to contain more carats of diamonds than any pipe mined at Ekati so far. Hence, the firm will be able to generate a profit of approximately $148 million with an average diamond price of $86 per carat. As you can see on the graph below, there is a huge potential increase in rough diamond prices and DDC will benefit from this prospective increase that could attain nearly the $150 range. As a matter of fact, this acquisition of Ekati mine is important because in 2012 a 78 carat diamond was sold for $6 million. The feasibility study signals that this Jay pipe project has a positive NPV of $113 million and an IRR of 21%. Those elements show the growth opportunity for the company and the long term benefits for Dominion Diamonds will be greater with the Jay project.



Another project that Dominion is eager to develop is the A21 pipe. In fact, this project will resolve the uncertainty surrounding Diavik mine, where Rio Tinto and Dominion has a joint venture partnership. The A21 pipe is expected to start late 2018 and the expansion will ensure output at Diavik sustains at existing levels. Rio Tinto is the one that will construct the pipe and Dominion Diamonds Corporation will share the profit. According to the chief executive of Rio Tinto "our decision to invest in the Diavik A21 project reflects our strong confidence in the diamond sector"[3]. DDC is constantly trying to fully acquire Diavik mine from Rio Tinto as it is near Ekati mine and will enable the firm to create synergies between both of them. Last year Rio Tinto cancelled the talks when Dominion did not agree to purchase its diamond mine in Australia as part of the deal.

Strategic Acquisitions and alliances

There is no surprise that Dominion Diamond Corporation is the third largest diamond producer by value. As a matter of fact, the company has realized strategic alliances by buying 40% stake in the Diavik mine, operated by Rio Tinto, and by purchasing the Ekati mine from BHP Billiton. Thus, the company has interest in two major Canadian diamond mines that could allow it to improve its financial situation versus its competitors. Dominion Diamonds' two mines helped the company earn approximately $498 million in profits last year and they are expected to be producing until 2022 with more than 50 million carats of reserves. Those strategic acquisitions and alliances show the financial ability of the firm to grow and improve its production. Hence, DDC does not need large capex budget in order to improve the production of its mines; however, the company needs to sustain capital if it wants to remain competitive in the diamond industry. The company will not face any risk of idle production because the mines are located in a

[2] http://www.businesswire.com/news/home/20150127005193/en/Dominion-Diamond-Corporation-Announces-Jay-Project-Pre-Feasibility#.VODj9vm-0yo
[3] http://www.bnn.ca/News/2014/11/27/Rio-Tinto-approves-Arctic-diamond-mine-expansion.aspx

politically stable environment. The firm considers Diavik a free cash flow generator of approximately $175 million because a feasibility study proved there are 46 million carats in reserves that will achieve profitability for DDC. The gross margin of Dominion Diamond increased from Q3 2014 to Q3 2015 by 42% and sales improved by 52% for the same period.

Fiscal Year 2015 Third Quarter – Diavik Mine TSX/NY

For the three and nine months ending October 31
(in millions of United States dollars except carat amounts which are in millions of carats) (unaudited)

FISCAL PERIOD	Q3 2015	Q3 2014	YOY Change	YTD 2015	YTD 2014	YOY Change
Sales	$80	$53	52%	$270	$233	16%
Gross Margin	$28	$13	116%	$83	$63	31%
Gross Margin %	34.6%	24.4%	+1020bp	30.5%	27.0%	+350bp
Operating Profit	$27	$12	129%	$80	$59	34%
EBITDA[1]	$47	$24	95%	$146	$113	29%
Carats Recovered[2]	0.67M	0.67M	N/C	2.28M	2.07M	10%
Carats Sold	0.70M	0.45M	56%	2.24M	1.93M	16%

Also, Ekati delivers improvements for DDC as it generates gross margins of approximately 34% in Q3 FY2015 and increases the sales of the company by nearly 49%. Thus, Dominion Diamond will begin improving its situation thanks to two of the richest producing diamond mines in the world. This mine is crucial for the firm since there are more diamonds to extract with the potential growing demand from jewelry store and manufacturers starting 2015.

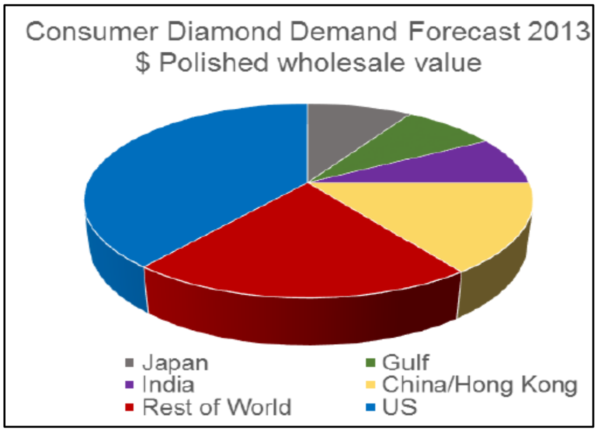
Fiscal Year 2015 Third Quarter – Ekati Mine TSX/NYS

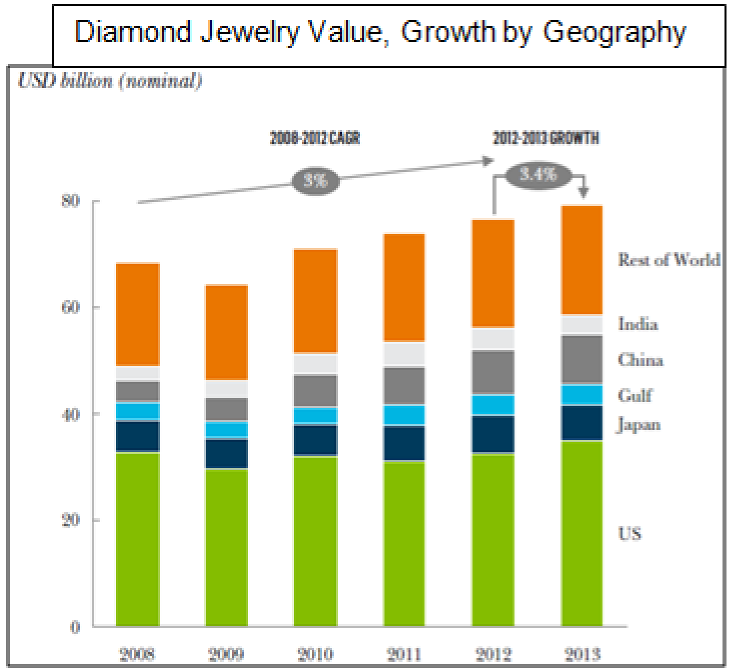
For the three and nine months ending October 31
(in millions of United States dollars except carat amounts which are in millions of carats) (unaudited)

FISCAL PERIOD	Q3 2015	Q3 2014[1]	YOY Change	YTD 2015	YTD 2014[1]	YOY Change
Sales[2]	$142	$95	49%	$405	$286	42%
Gross Margin (loss)	$48	$(1)	NM	$87	$7	NM
Gross Margin % (loss)	33.5%	(1.0)%	NM	21.4%	2.5%	NM
Operating Profit	$47	($1)	NM	$84	$6	NM
EBITDA[3]	$74	$18	317%	$167	$35	373%
Carats Recovered	0.98M	0.61 M	60%	2.34M	1.17M	99%
Carats Sold[4]	0.46M	0.37 M	25%	1.27M	0.97M	31%

International Expansion and Opportunities

Dominion Diamond Corporation is looking for the opportunity to expand its operations in countries other than the U.S. and Canada. The retail markets in both India and the Middle East recovered in the second half of 2014, and the company is looking forward to go overseas in order to improve its competitive advantage. DDC already sells its beautiful stones to manufacturers within the world's major diamond centers such as Belgium, Antwerp, and Mumbai. As the firm sees increasing consumer diamond demand from several countries all over the world, it wants to look for potential countries that will enable it to remain in the top three largest producers of rough diamonds in the world. Dominion Diamond provides desired carat sizes to more than 50 global customers outside the U.S. and Canada, which means that there is an opportunity for an international expansion. Also the company creates customer loyalty and offers an inventory guarantee to its customers in order to eliminate their need to sell unwanted stones. The two mines that DDC owns are internationally recognized as a world-scale supplier of top quality rough diamonds and the firm needs to use this as a way to improve its international exposure. As you can see on the diagram, diamond jewelry value is expected to growth in most of the countries around the globe in the long term. Thus, Dominion Diamond Corporation could benefit from this potential growing demand with an expected increase in prices starting mid-2015.





Best case/worst case

Regarding Dominion Diamond Corporation share price, there are three outcomes that could occur:

I am being conservative if the company cannot take advantage of the two largest mines in the world and the price of rough diamond remains flat in the $90 range. Thus, I believe that if the share price remains in the $16-$17 range in the next few months it means that the company was not able to deliver the promises that it stated in the latest earning calls or 10K before it starts its prospective projects.

I am being neutral if DDC does not extract high quality diamonds that could increase the demand from countries all over the world. The neutral range is between $15 and $16 because I believe that the company has what it takes to improve its position within the industry and become the top producer of rough diamonds.

I am being optimistic as DDC has a strong balance sheet with positive free cash flow and those elements enable the company to acquire additional shares in top mines. Hence, diamond companies will benefit from the potential increase in diamond prices and growing demand. I initiate my buy recommendation at the $16 levels and according to my estimates and assumptions Dominion Diamond Corporation will attain $19 through its projects that will kick start in 2019.

Conclusion

Overall, Dominion Diamond Corporation owns two of the richest producing diamond mines in the world. The experienced management team is confident that the company will be able to improve its fundamentals because it has a strong balance sheet to fund capital expenditures and sustain its credit line commitment. Dominion Diamond appears to be undervalued and investors should not ignore the potential that it could bring in the long term with its profitable projects. Those projects will give the firm the ability to improve its production and would add 10 years to the mine. Thus, the Jay project seems to present an interesting prospect for the company as it will prevent closure of the Ekati mine in 2019. Also, the A21 project gives a positive perspective for the firm because it will ensure the continuation of existing production levels for Diavik mine. The transition from being a jewelry shop to a mining company will certainly give DDC a bright future and the company keeps improving its financial results with its strategic partnerships. Dominion Diamond Corporation will start creating value when its projects start to be finalized and give it a competitive edge versus its competitors. Also, the company will experience a growth between 20% and 15% because the latest additional acquisition of Ekati will improve the production of rough diamonds. Starting 2019 the firm will keep its growth in the 15%-10% range as the projects Jay and A21 will be completed.

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Dominion Diamond Corporation	DDC	Analyst	Current Price	Intrinsic Value	Target Value	Divident Yield	Target Return	NEUTRAL
		DJ SAM	$16.40	$18.08	$18.72	0%	14.14%	

General Info

Sector	Materials
Industry	Metals and Mining
Last Guidance	Jan-19-2015
Next earnings date	4/2/2015

Market Data

Enterprise value	$1,583.37
Market Capitalization	$1,733.33
Daily volume	0.19
Shares outstanding	85.13
Diluted shares outstanding	85.13
% shares held by institutions	54.39%
% shares held by insiders	1.38%
Short interest	0.00%
Days to cover short interest	0.00
52 week high	$17.42
52-week low	$10.38
5y Beta	0.92
6-month volatility	29.60%

Peers	Market Cap.
BHP Billiton Limited	$173,213.58
Rio Tinto plc	$58,806.25

Current Capital Structure

Total debt/market cap	2.90%
Cost of Borrowing	6.95%
Interest Coverage	8154.43%
Altman Z	2.15
Debt Rating	BB
Levered Beta	1.02
WACC (based on market value weights)	8.19%

Management

Professional	Title	Comp. FY2012	Comp. FY2013	Comp. FY2014
Gannicott, Robert	Chairman, Chief Executive Offic	$ 4,309,294.00	$ 3,888,847.00	$ 4,679,442.00
Bell, Brendan	Acting Chief Executive, Executiv	$ -	$ -	$ 1,159,747.00
Pounds, James	Executive Vice President of Buyi	$ 1,492,379.00	$ 1,673,610.00	$ 1,708,784.00
Lavoie, Chantal	President of Dominion Diamon	$ -	$ -	$ 1,399,494.00
Cameron, Ron	Chief Financial Officer	$ -	$ -	$ -
Chetwode, Richard	Vice President of Corporate Dev	$ -	$ -	$ -

Historical Performance

	DDC	Peers	Industry	All U.S. firms
Growth	5.1%	11.6%	2.8%	6.0%
Retention Ratio	123.0%	43.9%	19.3%	61.6%
ROIC		45.7%	77.7%	11.8%
EBITA Margin	22.0%	33.0%	11.1%	13.7%
Revenues/Invested capital	56.5%	65.9%	79.2%	202.3%
Excess Cash/Revenue	26.9%	12.0%	16.3%	18.5%
Unlevered Beta	1.74	0.84		0.95
TEV/REV	3.4x	2.9x	2.0x	2.4x
TEV/EBITDA	10.2x	7.2x	14.9x	11.3x
TEV/EBITA	16.7x	8.7x		15.4x
TEV/UFCF	11.7x	13.6x		26.8x

Past Earning Surprises

	Revenue	EBITDA	Norm. EPS
Last Quarter	-2.3%	56.9%	42.9%
Last Quarter-1	9.3%	15.2%	55.0%
Last Quarter -2	6.5%	43.6%	112.5%
Last Quarter -3	-10.5%	-12.1%	-73.7%
Last Quarter -4	-21.3%	31.7%	

Non GAAP Adjustments

Operating Leases Capitalization	100%	Straightline	10 years
R&D Exp. Capitalization	0%	N/A	N/A
Expl./Drilling Exp. Capitalization	0%	N/A	N/A
SG&A Capitalization	0%	N/A	N/A

Proforma Assumptions / **Forecasted Profitability**

		Period	Rev. Growth	Adj. Op. Cost/Rev	Revenue	NOPLAT	Invested capital	UFCF
Operating. Cash/Cash	25.0%	LTM	50%	61%	$908.34	$110.41	$1,328.56	$113.72
Unlevered Beta	1.00	LTM+1Y	19%	79%	$1,082.93	$31.82	$1,442.11	-$16.57
Rev/Invested Capital	100.0%	LTM+2Y	17%	79%	$1,269.42	$41.13	$1,498.74	-$15.50
Continuing Period Revenue Growth	8.0%	LTM+3Y	16%	79%	$1,475.34	$51.87	$1,569.34	-$18.73
Long Term ROIC	12.0%	LTM+4Y	15%	79%	$1,699.93	$63.97	$1,649.02	-$15.70
Invested Capital Growth	Equals to Maintenance	LTM+5Y	14%	79%	$1,941.74	$77.13	$1,740.66	-$14.51
Justified TEV/REV	2.0x	LTM+6Y	13%	79%	$2,198.56	$91.29	$1,838.58	-$6.62
Justified TEV/EBITDA	12.0x	LTM+7Y	12%	79%	$2,467.40	$106.07	$1,941.84	$2.81
Justified TEV/EBITA	16.0x	LTM+8Y	11%	79%	$2,744.47	$121.13	$2,048.68	$14.29
Justified TEV/UFCF	25.0x	LTM+9Y	10%	75%	$3,025.25	$207.82	$2,160.09	$96.41

Valuation

	ROIC	WACC	EVA	Enterprise Value	Total Debt	Other claims	Equity	Adjusted Price
LTM	8.3%	8.2%	-$66.82	$1,598.42	$45.89	-$72.33	$1,624.86	$19.04
LTM+1Y	2.3%	8.3%	-$87.38	$1,731.33	$45.89	$74.16	$1,611.28	$19.47
LTM+2Y	2.8%	8.4%	-$83.64	$1,895.65	$45.89	$99.59	$1,750.17	$21.09
LTM+3Y	3.5%	8.5%	-$79.61	$2,074.45	$45.89	$127.84	$1,900.73	$22.94
LTM+4Y	4.1%	8.6%	-$75.00	$2,274.10	$45.89	$153.41	$2,074.80	$25.04
LTM+5Y	4.7%	8.6%	-$70.31	$2,489.57	$56.25	$168.27	$2,265.06	$27.44
LTM+6Y	5.2%	8.7%	-$65.62	$2,724.83	$70.75	$172.49	$2,481.59	$29.98
LTM+7Y	5.8%	8.8%	-$61.14	$2,974.59	$80.43	$173.65	$2,720.51	$32.87
LTM+8Y	6.2%	8.9%	-$56.89	$3,238.82	$82.43	$172.45	$2,983.94	$36.29
LTM+9Y	10.1%	9.0%	$22.27	$3,515.25	$82.43	$91.13	$3,341.68	$39.25

Monte Carlo Simulation Assumptions

	Base	Stdev	Min	Max	Distribution
Revenue Variation	0	10%	N/A	N/A	Normal
Op. Costs Variation	0	10%	N/A	N/A	Normal
Market Risk Premium	6%	N/A	5%	7%	Triangular
Long term Growth	8%	N/A	3%	12%	Triangular
Terminal Value	0	0.1	N/A	N/A	Normal

Monte Carlo Simulation Results

	Intrinsic Value	1y-Target
Mean est.	$19.04	$19.47
σ(ε)	$0.32	$0.25
3 σ(ε) adjusted price	$18.08	$18.72
Current Price	$16.40	
Analysts' median est.		$19.49

Enanta Pharmaceuticals, Inc. (ENTA: NASDAQ)

Financial Analysis By: Pamela Juergens-Healthcare

<u>Company Profile as of 2/18/2015</u>

Market Price: $34.09
Industry: Healthcare
Market Cap: $636.80 M
52-Week: $31.22-52.58
Beta: 0.543

Source	Target Price	Recommendation
Siena	$42.80	Buy
Capital IQ	$41.50	Buy
Yahoo Finance	$43.00	Buy
Bloomberg	$42.50	Buy

<u>Thesis</u>

- Likely approval of Paritaprevir in Japan in early 2015
- Product pipeline
- Contract award from the National Institute of Allergy and Infectious Disease (NIAID) to develop a new antibiotic

<u>Company Overview</u>

Enanta Pharmaceuticals is a research and development focused biotechnology company, which uses a chemistry driven approach to create small molecule drugs for viral infections and liver diseases. They discover and develop novel inhibitor designed for use against the Hepatitis C Virus, or HCV. These inhibitors include members of the direct acting antiviral (DAA) inhibitor classes- protease, partnered with AbbVie, NS5A, and nucleotide polymerase, as well as host targeted antiviral (HTA) inhibitor class targeted against cyclophilin. Enanta also has a preclinical program in non-alcoholic steatohepatitis (NASH), which is a condition that results in liver inflammation and damage caused by a buildup of fat in the liver.

Management

Enanta has an experienced management team with many years combined experience in the biotechnology field. Dr. Jay R. Luly Ph.D. has been the CEO and president of Enanta since July 2003. He has over 20 years of experience in large pharma, mature biopharmaceutical and early-stage biotech environments. Yat Sun Or, Ph.D. is a senior vice president of R&D and the Chief Scientific Officer. He joined Enanta in 1999 and prior to that he worked at Abbot Laboratories. The CFO is Paul J. Mellet; he joined Enanta in Sptember 2003, and prior to that he worked at GelTex Pharmaceuticals. Timothy D. Ocain is the Senior Vice President of New Product Development and Strategy. His focus is on the development activities of Enanta.

Competitors

Enanta is engaged in a segment of the pharmaceutical industry that is very competitive and changing rapidy. Many large pharmaceutical and biotechnology companies are commercializing or pursuing the development of products that target viral diseases, including the same viral diseases that they are targeting. Two products, Incivek by Vertex and Victrelis by Merck were approved by the FDA in 2011 for the treatment of HCV, but by mid-2014 Vertex announce they were discontinuing the sale of Incivek, crediting their decision to competing treatments and diminishing market demand. However, even though HCV is now curable multiple products should be able to survive on the market for many years, due to the prevalence of the disease, as long as they have a competitive advantage. Enanta's main competitor currently is Gilead, with their drug Harvoni. Harvoni is known for it's effectiveness, but along with that comes very high prices, as high as $1,000 per day for many patients. Viekira has the ability to take share from Harvoni by being offered at a discount, which it currently is, at 12% lower than Harvoni. Enanta currently has a pipeline of products to treat HCV, but there is a significant number of other product candidates that are under development, and many competitors, other than AbbVie, have product candidates in Phase 2 or later stage clinical trials, including Achillion and Bristol-Myers.

	Viekira (ABBV)			Harvoni (GILD)		
Patient Population	**Ribavirin Needed?**	**Duration**	**Gross Cost**	**Ribavirin Needed?**	**Duration**	**Gross Cost**
Genotype 1a, without cirrhosis	Yes	12 weeks	$83,319	**No**	**Some Rx naïve* = 8 weeks**; rest = 12 weeks	$63,000-$94,500
Genotype 1a, with cirrhosis	Yes	**24 weeks** (Partial responders and Relapsers **may get** 12 weeks, Nulls need 24 wks)	$83,319-$166,638	Yes	**12 Weeks**	$94,500
Genotype 1b, without cirrhosis	No	12 weeks	$83,319	No	**Some Rx naïve* = 8 weeks**; rest = 12 weeks	$63,000-$94,500
Genotype 1b, with cirrhosis	Yes	12 weeks	$83,319	Yes	12 Weeks	$94,500
Contraindications/ Major Warnings:	Ribarivin combo risks, drug interactions with those that are highly dependent of CYP3A or strongly induce CYP3A and 2C8 or inhibit 2C8. (e.g. generic Zocor). ALT elevations.			**None.**		

Prevelance of Hepatitis C Virus

Hepatitis C Virus (HCV) is a small, enveloped, positive-sense single-stranded RNA, and it is the cause of hepatitis C in humans. HCV is commonly spread through sharing of needles or other equipment to inject drugs. Hepatitis C, in combination with hepatitis B, now accounts for 75% of all liver diseases around the world. There is currently no vaccine available to protect against HCV. Approximately 3.2 million people in the United States have chronic HCV infection. Of those % infected, between 75%-85% develop chronic infection. In the World Health Organization (WHO) European Region an estimated 15 million (2.0%) people are infected. The WHO Health Evidence Network estimates the number of infected people is much higher with prevalence of up to 98% in people who inject drugs. The incidence in Japan was 1.2% of the adult population, or about 2 million people.

Upcoming FDA Approval

Enanta currently has one hepatitis C virus product, Paritaprevir (ABT-450), which was approved by the U.S. FDA on December 19, 2014, and in Europe on January 16, 2014. Paritaprevir (ABT-450) is a NS3/4A protease inhibitor and sold as a component of VIEKIRA PAK, which with dasabuvir is a treatment regimen for genotype 1 HCV patients, in partnership with AbbVie. Enanta announced positive phase 3 trial results, in Japan, in early February 2015, and it is expected that it will be approved in Japan in the first half of 2015. The primary endpoint of the GIFT-1 study was achieved, demonstrating a 95% sustained virologic response rate at 12 weeks post treatment in the sub-group of previously untreated non-cirrhotic adult genotype 1b Japanese patients who were eligible for therapy with interferon and had a high viral load.

Analysts estimate that VIEKIRA PAK could generate approximately 2.9 billion in sales in FY 2015. Enanta's revenues are substantially dependent on the AbbVie collaboration. Enanta can do nothing on the marketing side with the drug,as AbbVie handles that, but AbbVie has proven their ability to sell, with their widely commercially successful drug Humira. Under Enanta and AbbVie's agreement, Enanta stands to earn payments for regulatory and reimbursement milestones as well as annually tiered, double-digit royalties per product on AbbVie's worldwide netsales. Enanta already received $57 million in connection with signing the collaboration agreement, and $95 million in subsequent clinical and regulatory and milestone payments, and is eligible to receive an additional $155 million in payments for regulatory and reimbursement approval milestones. Upon approval in Japan, Enanta is entitled to a $30 million milestone payment from AbbVie. Enanta's stock price strongly reacts to positive regulatory news. Following FDA approval of VIEKIRA PAK in the US, Enanta's stock rose as much as 15% in one week. Approval in Japan should be a catalyst for Enanta's stock price.

Protease Inhibitor-Containing Regimens	Percentage of Annual Net Sales Used for Enanta Royalty Calculation
ABT-450-containing 3-DAA regimen (ABT-450/r, ombitasvir and dasabuvir)	30%
ABT-450-containing 2-DAA regimen (ABT-450/r, ombitasvir)	45%
For any HCV treatment regimen containing ABT-493, net sales for royalty purposes will be determined by dividing AbbVie's worldwide net sales of the regimen by the number of DAAs in the regimen (e.g. 50% of net sales for a 2-DAA regimen and 33 1/3% of net sales for a 3-DAA regimen).	

<u>Pipeline</u>

Enanta currently has a product pipeline, with several HCV treatment options, as well as treatment for liver disease. IN their pipeline for HCV treatment options, they are looking ahead to the future, where they anticipate resistance developing to the current treatments, giving them an edge against the competition in the future. Their pipeline assets are in varying stages of the approval process.

ABT-493: ABT-493 is a next generation protease inhibitor, which is being developed within the Enanta-AbbVie collaboration. AbbVie announced that this protease inhibitor has demonstrated activated in preclinical in vitro testing against a broad range of HCV genotypes, including variants that have shown strong resistance to first generation protease inhibitors. ABT-493 is being developed to be co-formulated with AbbVie's next generation NS5A inhibitor. A Phase 2b clinical trial was initiated in September 2014.

EDP-239: EDP-239 is an NS5A inhibitor for HCV infection. Enanta entered into a collaboration with Novartis in February 2012, granting Novartis the exclusive rights to develop, manufacture, and commercialize EDP-239, however Enanta is in the process of regaining the full rights. EDP-239 has demonstrated potent activity against major genotypes in the replicon assay, which is a common in vitro test for determining the potency of an active compound in reducing HCV replication. Preclinical studies support excellent permeability and absorption potentials in humans, with preferential targeting to the liver, which is the target site of the infection. EDP-239 is currently in ongoing proof-of-concept Phase-1b studies.

Cyclophilin Inhibitors: Enanta anticipates resistance arising to DAA HCV therapy that targets viral proteins. In response to this they are developing an alternative host-targeted antiviral, or HTA, approach that targets the human host protein, cyclophilin, which is essential for the replication of HCV. They have demonstrated in replicon assays that multiple lead cyclophilin targeting inhibitors are potent inhibitors of HCV replication and are more potent in these assays than clinical-stage cyclophilin inhibitors under development by others. They are currently advancing their lead candidates in preclinical studies.

Nucleotide Polymerase Inhibitor: This is a program to develop nucleotide inhibitors to HCV NS5B polymerase, another DAA mechanism considered to have a high barrier to resistance. They have ongoing discovery in this class, but nothing beginning testing yet.

Development of New Antibiotic

Enanta is currently developing a new type of antibiotics, the first in 30 years, called bicyclolides. They are a drug class used for the treatment of methicillin-resistant Staphylococcus aureus (MRSA), vancomycin-resistant Enterococcus (VRE), and other gram-positive infection pathogens. These were previously only a problem for patients treated in hospitals, but now they occurring in the general community, which creates a large need for a new class of antibiotics for use in both the hospital setting and in communities. Enanta's funding partner on the venture is the National Institute of Allergy and Infectious Disease (NIAID). Their partnership with NIAID provides them with the possibility for up to $42 million in research funding. Pre-clinical research on the bicyclolides revealed activity against MRSA and VRE, even against highly drug-resistant strains. The FDA also began special programs for such drugs through the GAIN Act. This act gives drugs under it a five-year exclusivity extension, as well as an expedited approval process. There is currently an urgent and growing threat of resistant strains of these infections, which along with the added benefits from the GAIN Act make the future of their new antibiotic look promising.

Conclusion

Enanta is a buy because of their innovative pipeline of products, as well as upcoming approval of Paritaprevir in Japan in the first half of 2015. They are also receiving funding to develop an antibiotic that will be the first new antibiotic in 30 years. There is a growing need for this because many stains of bacteria are demonstrating resistance to current antibiotics, and the new antibiotic has the potential to be a blockbuster for Enanta.

CENTER FOR GLOBAL FINANCIAL STUDIES

Enanta Pharmaceuticals, Inc.	ENTA	Analyst	Current Price	Intrinsic Value	Target Value	Divident Yield	Target Return	NEUTRAL
		Pamela Juergens	$33.65	$43.95	$42.80	0%	27.2%	

General Info

Sector	Healthcare
Industry	Biotechnology
Last Guidance	(Invalid Identifier)
Next earnings date	5/8/2015

Market Data

Enterprise value	$534.39
Market Capitalization	$636.80
Daily volume	0.21
Shares outstanding	18.68
Diluted shares outstanding	19.52
% shares held by institutions	59.40%
% shares held by insiders	9.94%
Short interest	14.72%
Days to cover short interest	6.57
52 week high	$52.58
52-week low	$31.22
5y Beta	0.00
6-month volatility	48.99%

Peers	Market Cap.
InterMune, Inc	
Vertex Pharmaceuticals Incorporated	$27,494.05
Gilead Sciences Inc	$155,806.06
Pharmacyclics Inc	$12,938.85

Current Capital Structure

Total debt/market cap	0.03%
Cost of Borrowing	0.00%
Interest Coverage	631013.33%
Altman Z	24.49
Debt Rating	AAA
Levered Beta	1.41
WACC (based on market value weights)	10.47%

Management

Professional	Title	Comp. FY2012	Comp. FY2013	Comp. FY2014
Luly, Jay	Chief Executive Officer, Presiden	$ 771,571.00	$ 1,648,841.00	$ 2,519,114.00
Mellett, Paul	Chief Financial Officer and Senio	$ 460,519.00	$ 924,193.00	$ 1,329,622.00
Or, Yat	Chief Scientific Officer and Senio	$ 606,127.00	$ 992,841.00	$ 1,403,437.00
Gardiner, Nathaniel	Senior Vice President, General C	$ -	$ -	$ -
Ocain, Timothy	Senior Vice President of New Pr	$ -	$ -	$ -
Phan, Ly Tam	Director of Medicinal Chemistry	$ -	$ -	$ -

Historical Performance

	ENTA	Peers	Industry	All U.S. firms
Growth	29.1%	27.4%	15.9%	6.0%
Retention Ratio	0.0%	94.1%	107.9%	61.6%
ROIC		25.4%	17.0%	11.8%
EBITA Margin	0.0%	54.7%	19.2%	13.7%
Revenues/Invested capital	57.4%	80.0%	64.4%	202.3%
Excess Cash/Revenue	190.1%	47.3%	82.9%	18.5%
Unlevered Beta		1.19	1.08	0.95
TEV/REV	11.7x	7.8x	6.2x	2.4x
TEV/EBITDA	33.8x	17.7x	16.1x	11.3x
TEV/EBITA	34.5x	18.3x	18.9x	15.4x
TEV/UFCF		84.5x	43.3x	26.8x

Past Earning Surprises

	Revenue	EBITDA	Norm. EPS
Last Quarter	-10.5%	0.0%	-42.9%
Last Quarter-1	62.0%		
Last Quarter -2	1.9%	16.6%	6.4%
Last Quarter -3	-85.4%	0.0%	
Last Quarter -4	-39.5%		

Non GAAP Adjustments

Operating Leases Capitalization	100%	Straightline	10 years
R&D Exp. Capitalization	100%	Straightline	10 years
Expl./Drilling Exp. Capitalization	0%	N/A	N/A
SG&A Capitalization	0%	N/A	N/A

Proforma Assumptions

Operating. Cash/Cash	0.0%
Unlevered Beta	1.40
Rev/Invested Capital	100.0%
Continuing Period Revenue Growth	5.0%
Long Term ROIC	12.4%
Invested Capital Growth	Equals to Maintenance
Justified TEV/REV	5.0x
Justified TEV/EBITDA	15.0x
Justified TEV/EBITA	25.0x
Justified TEV/UFCF	18.0x

Forecasted Profitability

Period	Rev. Growth	Adj. Op. Cost/Rev	Revenue	NOPLAT	Invested capital	UFCF
LTM	94%	10%	$124.35	$95.88	$135.22	$46.82
LTM+1Y	33%	44%	$164.83	$60.95	$279.97	-$86.93
LTM+2Y	19%	46%	$195.42	$64.53	$326.67	$17.83
LTM+3Y	14%	48%	$221.99	$67.80	$368.01	$26.47
LTM+4Y	9%	49%	$242.38	$70.64	$401.80	$36.86
LTM+5Y	7%	49%	$259.35	$74.25	$431.92	$44.12
LTM+6Y	7%	49%	$277.51	$78.63	$464.48	$46.08
LTM+7Y	7%	49%	$296.93	$83.71	$494.77	$53.42
LTM+8Y	6%	49%	$316.14	$88.85	$524.19	$59.43
LTM+9Y	5%	49%	$331.95	$93.14	$550.40	$66.93

Valuation

	ROIC	WACC	EVA	Enterprise Value	Total Debt	Other claims	Equity	Adjusted Price
LTM	111.3%	10.5%	$124.80	$770.22	$0.18	-$73.84	$843.88	$44.91
LTM+1Y	39.2%	10.5%	$78.31	$843.82	$0.18	$36.57	$807.07	$43.55
LTM+2Y	23.1%	10.6%	$40.59	$860.54	$0.18	$21.97	$838.38	$45.43
LTM+3Y	20.8%	10.7%	$36.89	$912.56	$0.18	-$2.58	$914.96	$49.59
LTM+4Y	19.2%	10.8%	$33.58	$962.31	$0.18	-$37.85	$999.97	$54.21
LTM+5Y	18.5%	10.9%	$32.57	$1,014.11	$0.18	-$80.15	$1,094.08	$59.46
LTM+6Y	18.2%	11.0%	$33.28	$1,072.39	$0.18	-$123.91	$1,196.11	$64.80
LTM+7Y	18.0%	11.1%	$34.03	$1,130.65	$0.18	-$174.84	$1,305.30	$70.70
LTM+8Y	18.0%	11.2%	$35.18	$1,190.59	$0.18	-$231.65	$1,422.06	$76.99
LTM+9Y	17.8%	11.3%	$35.36	$1,249.07	$0.18	-$296.23	$1,545.11	$82.71

Monte Carlo Simulation Assumptions

	Base	Stdev	Min	Max	Distribution
Revenue Variation	0	10%	N/A	N/A	Normal
Op. Costs Variation	0	10%	N/A	N/A	Normal
Market Risk Premium	6%	N/A	5%	7%	Triangular
Long term Growth	5%	N/A	3%	29%	Triangular
Terminal Value	0	0.1	N/A	N/A	Normal

Monte Carlo Simulation Results

	Intrinsic Value	1y-Target
Mean est.	$44.91	$43.55
σ(ε)	$0.32	$0.25
3 σ(ε) adjusted price	$43.95	$42.80
Current Price	$33.65	
Analysts' median est.		$42.50

The Hain Celestial Group, Inc (HAIN: NASDAQ)

Financial Analysis By: Remy Fields – Consumer Staples

Company Profile as of 2/12/2015

Market Price: $59.02
Industry: Food Products
Market Cap: $5,864.94M
52-Week: $40.84 – 60.45

Source	Target Price	Reccomendation
Siena	$ 71.15	Buy
Bloomberg	$ 61.49	Buy
Capital IQ	$ 63.75	Buy
Yahoo Finance	$ 63.50	Buy

Thesis

-Positive industry outlook

-Positioning in market
-Strength of balance sheet

-Possible cost cutting

The Hain Celestial Group Inc. is a buy because they are well positioned in an industry that has been and will continue to see rapid growth. Hain Celestial's strong balance sheet will allow them to acquire companies that will help their competitive advantage. The ability to acquire companies allows Hain to leverage their connections throughout the consumer staples industry and create efficiencies. Finally, Hain will be able to cut costs in SG&A that have not been priced into the market yet.

Company Overview

The Hain Celestial Group (Nasdaq: HAIN), is a leading natural and organic food and personal care products company in North America and Europe. Hain Celestial participates in almost all natural food categories with well-known brands that include Celestial Seasonings, Health Valley, Earth's Best, Arrowhead Mills, Hain Pure Foods, Spectrum Naturals, Spectrum Essentials, Imagine Food, Linda McCartney, Grains Noirs, Avalon Organics and many more. The Hain Celestial Group common stock trades on The NASDAQ Global Select Market. Together with its subsidiaries, manufactures, markets, distributes, and sells organic and natural products in the United States, the United Kingdom, Canada, and Europe. Its grocery products include infant formula, rice, non-dairy beverages, frozen desserts, flour and baking mixes, breads, hot and cold cereals, pasta, condiments, and personal care products, including skin, hair and oral care, deodorants, and many more. The company sells its products through direct sales people, brokers, and distributors to specialty and natural food distributors, supermarkets, natural food stores, mass-market retailers, e-tailers, food service channels and club, and drug and convenience stores in approximately 65 countries worldwide. The Hain Celestial Group, Inc. was founded in 1993 and is headquartered in Lake Success, New York.

Management

From a management standpoint The Hain Celestial Group is an experienced management team. The CEO, Irwin Simon, found the company in 1993. Before founding the company he worked in various marketing capacities for Slim-Fast Foods Company. The CFO, Stephen Smith, has been in his position since 2013. Previously, Mr. Smith worked at PricewaterhouseCoopers LLP as a Partner from 1993 until 2001. Another executive to note is John Carroll; he has worked in the Consumer Staples industry for over 15 years. He worked as the managing director of Heinz Frozen Foods from 1995 until 2003. After his stint at Heinz, he consulted for The Hain Celestial group and was brought on soon after in 2004. The management team has expertise in management and the consumer staples industry, which has transpired into the growth of the company.

Industry Outlook

When looking into the consumer staples industry as a whole there are not high expectations of growth, but when considering a smaller part of the industry the growth expectations are higher. Organic foods used to be a niche market, but the growing consumer interest has opened the market to many opportunities. Two out of every three consumers say they buy some sort of organic food. Millennials desire to live a healthy lifestyle that is why we are seeing the frozen food category move more and more to fresh. With millennials moving into the working class, their spending is going to become a large percentage of the spending occurring in the consumer staples industry. Many health risks are associated with the use of conventional food due to the presence of chemicals, such as, pesticides, antibiotics and other drugs. This has resulted in consumers preferring organic food & beverages products that are non-toxic and environment friendly. In addition, we are near-epidemic levels of obesity and the increased occurrence of diabetes, which have stirred a national debate over food policy and diet. This debate has not only influenced consumers, it has caused policy makers to take action. Recently, the FDA has made regulations that have strained food producers to make healthier food. In addition, the FDA has become stricter on their policies for labeling food. In 2013, they set forth a ruling that made it more difficult to label foods gluten-free and non-GMO (Genetically Modified Organisms). This is a good part of the consumer staples industry to be in from a top-down perspective.

One specific area that is growing rapidly is organic personal care market. Sales of organic personal care products are at 7.6 billion dollars and are expected to grow to 13.2 billion by 2018. The popularity of organic personal care products has grown because of the growth of organic food. People care about the different shampoos and lotions they are using on their bodies. They want it to be healthy for their skin without all the chemicals that have come along with skin care products of the past. Consumers have not only become more aware of what they put in their bodies, but they have become more aware of what goes on their bodies.

Another type of product that is expected to see exceptional growth is the gluten-free product line. Gluten-free products were made for the one-percents of human beings who are actually diagnosed with Celiac Disease. At first look, it would appear this is a terribly insignificant niche market, however with further analysis we see that the it appeals to a great deal of the population at large. Eighty-two percent of gluten-free consumers have not been diagnosed. Consumers are eating the gluten-free products because they believe that the products are healthier, so the popularity has risen. Fifty-five percent of gluten-free eaters spend thirty percent of their grocery budget on gluten-free foods. Sixty-eight percent of gluten-free eaters shop at three or more stores a month to find gluten-free foods. These statistics shows that the consumers that eat gluten-free foods believe in it so much that they are willing to go out of their way to find the gluten-free product because it is important to them. Furthermore, 82% of the consumers that shop for gluten-free products have not reached their buying potential in the industry. This leaves more room for improvement just based off the consumers already eating –gluten-free.

Finally, consumers around the world are interested in living healthier lives, a trend that supports companies including athletic apparel and outdoor equipment makers, organic grocery stores, providers of vitamins and nutritional supplements, and fast-casual restaurant chains that offer what are perceived as healthier food options. Nike, Under Armour and many more have marketed active lifestyles, the growth of these companies show that consumers are trying to live healthier lifestyles. One market that has recently emerged is wearable devices. This industry is made up of health trackers from Google, Apple, Microsoft, Fitbit, and more. If these huge names have entered this market, it is because they believe it has great potential. If fitness trackers do become the next "big thing", they will remind people everyday of their health. With this new heightened awareness, many consumers will seek healthier alternatives as they proceed to the check out counter.

Positioning in market

The Hain Celestial Group is positioned very well in consumer staples market with this shift in consumer ideals. The Hain Celestial Group has over 25 brands that range from rice to turkey to personal care. What really differentiates the Hain celestial group from most of their competitors is that they 99% of their food products do not contain GMO's. In addition to having the organic food that consumers are looking for they also have gluten-free brands. Currently, six of their brands produce gluten-free products. They have over 500 gluten-free products on the market today, and expect to release more soon. Again, this positions them in a place that many of their competitors are not in or attempting to move to. Being one-step ahead has allowed Hain Celestial to solidify their buyers from over twenty different sellers. Hain Celestial has big names buying their products, such as, Whole Foods, Amazon, Costco, United Natural Foods Inc., Publix, and many more. Hain Celestial has diversified their portfolio, in which their biggest buyer only makes up 13% of their portfolio. This is a good position because they do not rely on one grocery store too much for their sales. An additional way the Hain Celestial Group has positioned themselves well is in the geographic locations they sell. North America accounts for 48% of the organic food market and Europe consists of 45% of the market. Hain Celestial is positioned well with 60% of their sales in the U.S., 30% coming from the U.K. and 10% being split between Canada and Europe. As mentioned above the organic personal care industry is expected to grow 40% by 2018. Also, the Hain Celestial Group is well positioned in this market. The Hain Celestial Group has six different brands in the organic personal care industry and continues to innovate in that industry.

In addition, Hain Celestial plans to announce 75 new products at the Expo West in March. These products shall be aimed at the high growth potential areas within the industry. They will be announcing products throughout all of their brands, but some key products will include gluten-free, lactose free, and non-GMO coconut bites. They also plan to announce a new beauty treatment for puffy eyes, pimples, under-eye circles, and thin lips in the fast growing organic personal care industry. These innovations have great potential to be huge hits, and are in markets that have high growth expectations in general.

Strength of Balance Sheet

Another strength that The Hain Celestial Group has in the industry is a strong balance sheet. This is important because, although organic growth has been in the high single digits for the Hain Celestial Group, it can be difficult to find in consumer packaged goods companies today. Having the ability to do this is important because they are less likely to miss an opportunity in the market if they are not able to create it themselves. An example of this would be in the meat, fish and poultry product segment. This product segment has the potential to grow at a 14.6% CAGR through 2020. Currently, The Hain Celestial Group is not in this industry, but there have been talks about moving into it. If they choose to acquire a number two or three in the product segment as they have done in the past in other product segments they will be an instant competitor. The Hain Celestial Group has shown that in the past they will not acquire someone unless they have the ability to help create efficiencies in the company. These efficiencies have made acquisitions, such as Rudi's Organic Bakery and Tilda, well worth the price. Certain synergies that they have used in the past to create value in an acquisition are operational and economies of scale. Operationally they have been able to create value by cutting SG&A of the company they acquire because they have the ability to leverage the SG&A that Hain Celestial already uses. In addition, they have helped smaller companies that they have acquired find and develop more efficient distribution channels. Distribution plays an important role in the success of companies and The Hain Celestial Group has those connections. If they are to buy a company in the meat, fish, and poultry product segment, they will have more places for their product to go.

Possibility of cost cutting

As I have mentioned above Hain Celestial has created operational synergies in the past. Recently, they have had an acquisition of Rudi's Organic Bakery in May and they have already closed their offices and have had them move into their headquarters. This may have already been priced into the stock, but what has not been accounted for as of yet is if Hain Celestial cuts more costs by moving their Canada office into their headquarters as well. At this time, Canada is run as a separate entity, but there is a possibility to create efficiencies by better integrating the operations of Canada and the U.S. In addition, in the U.K Hain Celestial has three different businesses (Tilda, Hain Daniels, and Ella's) running as separate businesses. Hain Europe is also running as its own business, which means that these four businesses have the opportunity to become more strategically integrated to cut costs of operations. This is important because the stock market has not priced this in yet, and there is a possibility to get in ahead of it.

Conclusion

In conclusion, the Hain Celestial Group is a buy because of their positioning in a rapidly expanding market. They are better situated than their competitors are because they have the products that consumers are looking for. They also have the experience of making popular products in the industry, which means they should be able to continue innovating in the fast growing product segments. In addition, they have a strong balance sheet in an industry where organic growth is difficult. Their balance sheet will allow them to buy into a product segment that is growing quickly. Finally, The Hain Celestial Group has been known to cut costs in the past and currently have the ability to do this domestically and internationally. They have multiple businesses running in similar areas, now they must find ways to integrate them together to lower costs.

CENTER FOR GLOBAL FINANCIAL STUDIES

The Hain Celestial Group, Inc.	HAIN	Analyst	Current Price	Intrinsic Value	Target Value	Divident Yield	Target Return	NEUTRAL
		Remy Fields	$59.03	$63.75	$71.15	0%	20.55%	

General Info	
Sector	Consumer Staples
Industry	Food Products
Last Guidance	Feb-04-2015
Next earnings date	5/5/2015

Market Data	
Enterprise value	$6,604.91
Market Capitalization	$5,864.94
Daily volume	0.90
Shares outstanding	101.72
Diluted shares outstanding	102.42
% shares held by institutions	94.53%
% shares held by insiders	2.38%
Short interest	7.82%
Days to cover short interest	7.01
52 week high	$60.45
52-week low	$40.84
5y Beta	0.40
6-month volatility	27.13%

Peers	Market Cap.
The WhiteWave Foods Company	$6,196.65
Treehouse Foods, Inc.	$3,756.10
Post Holdings, Inc.	$2,556.96
Snyder's-Lance, Inc.	$2,122.18
Mead Johnson Nutrition Company	$19,974.71
Boulder Brands, Inc.	$626.00
Monster Beverage Corporation	$19,947.25
Flowers Foods, Inc.	$4,108.27
Pinnacle Foods Inc.	$4,217.07
Keurig Green Mountain, Inc.	$19,312.09

Current Capital Structure	
Total debt/market cap	13.25%
Cost of Borrowing	3.33%
Interest Coverage	959.21%
Altman Z	3.70
Debt Rating	BBB
Levered Beta	1.11
WACC (based on market value weights)	7.95%

Management

Professional	Title	Comp. FY2012	Comp. FY2013	Comp. FY2014
Simon, Irwin	Founder, Chairman, Chief Execu	$ 9,312,869.00	$ 26,493,755.00	$ 11,172,452.00
Smith, Stephen	Chief Financial Officer and Execu	$ -	$ -	$ 1,599,736.00
Faltischek, Denise	Chief Compliance Officer, Execu	$ 1,052,190.00	$ 1,217,315.00	$ 1,586,168.00
Carroll, John	Executive Vice President and Chi	$ 2,224,486.00	$ 2,693,195.00	$ 3,555,529.00
Lamel, Ira	Special Advisor to the Chief Exe	$ 2,030,242.00	$ 2,038,850.00	$ 1,035,147.00
Weiner, Ross	Chief Accounting Officer and Vic	$ -	$ -	$ -

Historical Performance

	HAIN	Peers	Industry	All U.S. firms
Growth	14.8%	12.6%	8.7%	6.0%
Retention Ratio	47.3%	129.3%	59.5%	61.6%
ROIC	48.8%	10.4%	13.5%	11.8%
EBITA Margin	9.7%	15.2%	11.6%	13.7%
Revenues/Invested capital	94.7%	89.2%	178.1%	202.3%
Excess Cash/Revenue	3.9%	8.0%	6.4%	18.5%
Unlevered Beta	0.89	0.67	0.64	0.95
TEV/REV	1.4x	2.4x	1.5x	2.4x
TEV/EBITDA	12.4x	13.6x	12.1x	11.3x
TEV/EBITA	15.3x	16.1x	15.3x	15.4x
TEV/UFCF	18.0x	107.6x	28.3x	26.8x

Past Earning Surprises

	Revenue	EBITDA	Norm. EPS
Last Quarter	-2.9%	1.8%	3.8%
Last Quarter-1	-1.2%	1.0%	0.0%
Last Quarter -2	1.1%	-10.8%	2.3%
Last Quarter -3	0.2%	-2.0%	2.3%
Last Quarter -4	-0.8%	-2.2%	0.0%

Non GAAP Adjustments

Operating Leases Capitalization	100%	Straightline	10 years
R&D Exp. Capitalization	0%	N/A	N/A
Expl./Drilling Exp. Capitalization	0%	N/A	N/A
SG&A Capitalization	0%	N/A	N/A

Proforma Assumptions / **Forecasted Profitability**

		Period	Rev. Growth	Adj. Op. Cost/Rev	Revenue	NOPLAT	Invested capital	UFCF
Operating. Cash/Cash	25.0%	LTM	54%	87%	$2,468.89	$177.61	$2,552.38	$148.23
Unlevered Beta	1.00	LTM+1Y	66%	85%	$4,106.25	$351.41	$2,923.20	$131.73
Rev/Invested Capital	90.0%	LTM+2Y	7%	85%	$4,409.70	$385.38	$3,026.08	$282.50
Continuing Period Revenue Growth	3.5%	LTM+3Y	7%	84%	$4,733.04	$431.49	$3,165.40	$292.17
Long Term ROIC	14.2%	LTM+4Y	6%	83%	$5,040.44	$474.20	$3,313.09	$326.51
Invested Capital Growth	Equals to Maintenance	LTM+5Y	5%	83%	$5,276.31	$504.51	$3,492.77	$324.84
Justified TEV/REV	2.4x	LTM+6Y	4%	83%	$5,485.38	$540.88	$3,681.17	$352.48
Justified TEV/EBITDA	13.0x	LTM+7Y	4%	82%	$5,677.37	$576.97	$3,846.55	$411.58
Justified TEV/EBITA	16.0x	LTM+8Y	3%	82%	$5,876.08	$597.36	$4,019.76	$424.15
Justified TEV/UFCF	30.0x	LTM+9Y	3%	82%	$6,081.74	$618.27	$4,216.56	$421.47

Valuation

	ROIC	WACC	EVA	Enterprise Value	Total Debt	Other claims	Equity	Adjusted Price
LTM	7.0%	8.0%	$65.61	$7,508.23	$875.19	$146.74	$6,486.29	$64.71
LTM+1Y	13.0%	8.0%	$141.88	$8,214.28	$875.19	$126.55	$7,212.54	$71.90
LTM+2Y	13.2%	8.1%	$150.96	$8,587.72	$875.19	-$120.19	$7,832.72	$77.88
LTM+3Y	14.2%	8.3%	$188.43	$9,015.65	$875.19	-$381.13	$8,521.58	$84.69
LTM+4Y	15.0%	8.4%	$217.61	$9,439.47	$875.19	-$679.68	$9,243.95	$91.83
LTM+5Y	15.2%	8.5%	$234.42	$9,892.39	$875.19	-$980.50	$9,997.70	$99.58
LTM+6Y	15.5%	8.6%	$252.63	$10,364.14	$875.19	-$1,313.09	$10,802.03	$107.26
LTM+7Y	15.7%	8.7%	$267.26	$10,821.95	$875.19	-$1,708.53	$11,655.30	$115.70
LTM+8Y	15.5%	8.8%	$269.39	$11,310.01	$875.19	-$2,120.55	$12,555.37	$124.60
LTM+9Y	15.4%	8.9%	$272.12	$11,831.95	$875.19	-$2,534.71	$13,491.47	$132.64

Monte Carlo Simulation Assumptions

	Base	Stdev	Min	Max	Distribution
Revenue Variation	0	10%	N/A	N/A	Normal
Op. Costs Variation	0	10%	N/A	N/A	Normal
Market Risk Premium	6%	N/A	5%	7%	Triangular
Long term Growth	4%	N/A	3%	15%	Triangular
Terminal Value	0	0.1	N/A	N/A	Normal

Monte Carlo Simulation Results

	Intrinsic Value	1y-Target
Mean est.	$64.71	$71.90
σ(ε)	$0.32	$0.25
3 σ(ε) adjusted price	$63.75	$71.15
Current Price	$59.03	
Analysts' median est.		$62.84

Hyster-Yale Materials Handling (HY:NYSE)

Financial Analysis By: Matthew Darcy – Industrials

<u>Company Profile as of 2/19/2015</u>

Market Price: $67.46
Industrial Machinery
Market Cap: $1.04B
52-Week: $108.13 - $62.19
Beta: 1.47

Source	Target Price	Recommendation
Siena	$87.06	Buy
Capital IQ	$75.67	Hold
Yahoo Finance	$75.67	Hold
Bloomberg	$75.67	Hold

<u>Thesis</u>

-Product Innovations will positively impact Sales Price and Warranty Expenses.
-Reducing Cost of Production
-As the company increases Unit Sales, they Increase the market for Replacement Parts.

<u>Recommendation</u>

Hyster-Yale Materials Handling is a BUY. They are focused on Product innovation that will decrease the cost of owning their equipment to the costumers. This will allow for an increase in sales price per Unit as the products become more desirable to customers. The decreasing cost to customers will also decrease Warranty Expenses to Hyster-Yale. They also have focused on Reducing Cost of Production by building a new factory in Brazil, Implementing new IT Systems, and modifying their products to use Common Components. The building of a new factory is an attempt by the company to reach Economies of Scale, at which they will see reduced operating costs in the future. The increase in production has other implications as well. The company is in the business of selling Replacement Parts for their Trucks, which currently makes up 13% of sales. As the company increases its sales of lift trucks, they will create more potential customers for the replacement parts. In this way growth perpetuates more growth.

Company Overview

Hyster-Yale Materials Handling is a designer, manufacturer, and servicer of a large product line of lift trucks, under the brand names, Hyster, Yale, and UTILEV. There are 6 classifications of Lift Trucks with maximum Capabilities of lifting from up to 5.5 tons to up to 52 tons. The company's customers range from Manufacturers, wholesalers, and retailers, to Shipping ports. The company also sells aftermarket parts required for the maintenance of the trucks, under the brand names UNISOURCE, MULTIQUIP, and PREMIER. The parts can be used to service competing brand trucks as well. Hyster-Yale is a global company, with a presence in Australia, Brazil, China, England, India, Italy, Japan, Mexico, Northern Ireland, The Philippines, The Netherlands, The United States, and Vietnam. The company was spun-off from NACCO Materials Handling in 2012, and currently has no net debt. The CEO of Hyster-Yale is CEO of NACCO, but this is not a worry, because his compensation from Hyster-Yale is $4.1 million in Stock awards while his Compensation from NACCO is only $818,989 in Stock awards.

Product Innovation

Hyster-Yale has been focusing on Reducing Cost of Ownership to customers. This means that customers will be willing to pay more for the products as Hyster-Yale continues to make them more fuel efficient, and durable. The company recently acquired Nuvera Fuel Cells Inc. from Hess Corp. The strategy is to integrate Nuvera's clean energy fuel cells into the Hyster-Yale lift trucks. This will optimize the energy efficiency of the lifts, as well as make the products more capable of operating indoors. It also makes the company the soul producer of replacement parts for the newly innovated product line. Another implication of the company's continuous improvement strategy is that the company has been modifying the Products to use as many of the same parts as possible. This will make it cheaper for the parts to be built, decreasing the cost of switching over production lines. The company can produce a bunch of the same part instead of producing small amounts of a variety of parts. This means the parts can be sold cheaper, and therefore the customer will enjoy a lower cost of maintaining the lift trucks.

All of these factors will add to the customer's decision to buy Hyster-Yale products, and will allow the company to increase its sales price. This will help the company realize their desire to increase profit margins.

The reduced cost of Ownership also decreases Hyster-Yale's Warranty expenses, because the company does not need to make good on their promise to fix products as often. This will also help increase profit margins.

Reduced Cost of Production

Hyster-Yale has set a goal for a 7% Operating profit margin, within the next 3 to 5 years. The company will likely not see this margin in 2015 but it has an advantageous position to move towards that goal in the years following. In the proforma forecast a 6% long term operating profit margin was used in order to account for possible failure to reach that goal, and still produced a 31% upside potential. If this company can make good on the 7% margin by 2017 then the company's value would be extremely higher than its current price. The company's main tactics of achieving this goal are the Implementation of new IT Systems in manufacturing, the building of a new plant in Brazil, and the modification of products to use common components.

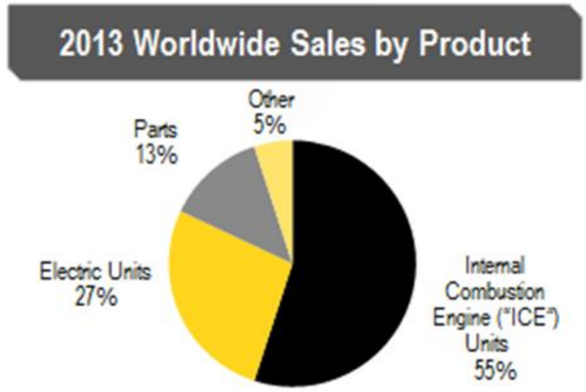
The company began implementing a new IT system throughout the company known as System Applications Products (SAP). SAP is an Enterprise Resource Planning system, which basically means that it helps integrate all aspects of the business, from corporate to manufacturing to retail. The company is already seeing benefits from the program in Brazil and Italy, and has created a Team of employees who are travelling from location to location, setting up the software and helping with change management. It was stated that the previous systems were quit old so the new SAP system should have a very positive effect.

The new Plant in Brazil is an assembly plant for lift trucks. The new factory will be more efficient, as the company strives for its goal to reach Economies of Scale. The factory is already equipped with the updated IT System so they will immediately see the benefits upon startup of production.

The company's plan to integrate Common Components between the product lines is also going to affect the cost of production. It will reduce costs in both the aftermarket parts segment, and the lift truck segment. This will increase profit margins across the board.

Replacement Parts Market

Hyster-Yale is one of the largest manufactures of lift trucks in the world in terms of Units Sold. They have estimated that there are currently 815,000 of their own lift trucks in operation currently, and this number will continue to rise upon completion of the factory in Brazil. As unit sales rise the company increases the number of customers available for its aftermarket sales. This means that, as the company grows, it creates a market for itself with aftermarket parts. The sale of replacement parts is a significant portion of Hyster-Yale's revenue, and it would benefit the company greatly to see growth in this area.



Summary

Hyster-Yale is a Buy with an upside potential of 31%. Even when using conservative Assumptions for Operating margin the proforma still finds the stock undervalued. This mispricing is due to the market overlooking the increasing operating margin that Hyster-Yale will see in the future. This increase will be created through product innovations, and a reduction in costs through improved technology, a new lift assembly plant, and the use of common components in products. In conclusion this company has positioned itself to grow well in the upcoming years, due to the fact that growth in unit sales, driven by the plant in Brazil, will increase growth in aftermarket sales.

CENTER FOR GLOBAL FINANCIAL STUDIES

Hyster-Yale Materials Handling, Inc.	HY	Analyst	Current Price	Intrinsic Value	Target Value	Divident Yield	Target Return	BULLISH
		Matthew Darcy	$67.17	$72.38	$87.06	2%	31.25%	

General Info

Sector	Industrials
Industry	Machinery
Last Guidance	Oct-29-2014
Next earnings date	2/19/2015

Market Data

Enterprise value	$1,034.62
Market Capitalization	$1,082.22
Daily volume	0.05
Shares outstanding	16.26
Diluted shares outstanding	16.80
% shares held by institutions	56.44%
% shares held by insiders	29.20%
Short interest	2.21%
Days to cover short interest	5.45
52 week high	$108.13
52-week low	$62.19
5y Beta	1.14
6-month volatility	29.70%

Peers	Market Cap.
Titan Machinery, Inc.	$311.26
Brady Corp.	$1,417.16
Columbus McKinnon Corporation	$515.23
Deere & Company	$31,404.53
Cargotec Corporation	$2,072.30
China International Marine Containe	$41,147.27

Current Capital Structure

Total debt/market cap	3.77%
Cost of Borrowing	4.73%
Interest Coverage	3494.74%
Altman Z	4.80
Debt Rating	BAA
Levered Beta	1.39
WACC (based on market value weig	9.82%

Management

Professional	Title	Comp. FY2011	Comp. FY2012	Comp. FY2013
Rankin, Alfred	Chairman, Chief Executive (	$ 6,733,740.00	$ 7,474,789.00	$ 7,052,415.00
Schilling, Kenneth	Chief Financial Officer, Prin	$ 619,999.00	$ 821,404.00	$ 1,268,999.00
Prasad, Rajiv	Senior Vice President of Gl	$ -	$ -	$ 1,396,686.00
Wilson, Colin	Chief Executive Officer of N	$ 1,411,134.00	$ 1,593,272.00	$ 2,670,959.00
Bittenbender, Charles	Senior Vice President, Gene	$ -	$ -	$ -
Miller, Lauren	Chief Marketing Officer	$ -	$ -	$ -

Historical Performance

	HY	Peers	Industry	All U.S. firms
Growth	21.2%	7.5%	6.5%	6.0%
Retention Ratio	0.0%	63.8%	44.1%	61.6%
ROIC		18.4%	19.4%	11.8%
EBITA Margin	0.0%	11.9%	11.5%	13.7%
Revenues/Invested capital	358.4%	131.5%	149.3%	202.3%
Excess Cash/Revenue	#DIV/0!	12.6%	12.1%	18.5%
Unlevered Beta		0.89	1.29	0.95
TEV/REV	0.4x	1.3x	1.5x	2.4x
TEV/EBITDA	7.5x	9.2x	10.3x	11.3x
TEV/EBITA	9.2x	10.9x	12.6x	15.4x
TEV/UFCF	20.5x	102.0x	28.1x	26.8x

Past Earning Surprises

	Revenue	EBITDA	Norm. EPS
Last Quarter	3.6%	6.8%	15.6%
Last Quarter-1	-0.8%	-9.2%	-19.5%
Last Quarter -2	0.0%	-4.3%	-6.4%
Last Quarter -3	4.6%	15.2%	-33.6%
Last Quarter -4	-0.6%	0.0%	4.5%

Non GAAP Adjustments

Operating Leases Capitalizatic	100%	Straightline	10 years
R&D Exp. Capitalization	100%	Straightline	10 years
Expl./Drilling Exp. Capitalizatio	0%	N/A	N/A
SG&A Capitalization	3%	Straightline	10 years

Proforma Assumptions / **Forecasted Profitability**

		Period	Rev. Growth	Adj. Op. Cost/Rev	Revenue	NOPLAT	Invested capital	UFCF
Operating Cash/Cash	0.0%	LTM	5%	92%	$2,774.40	$100.83	$745.48	$81.45
Unlevered Beta	1.31	LTM+1Y	2%	92%	$2,829.97	$97.22	$833.51	$52.01
Rev/Invested Capital	131.5%	LTM+2Y	3%	92%	$2,915.04	$101.68	$868.39	$66.80
Continuing Period Revenue Gro	3.0%	LTM+3Y	3%	92%	$3,002.49	$108.65	$904.73	$72.30
Long Term ROIC	13.3%	LTM+4Y	3%	92%	$3,092.56	$112.68	$941.49	$75.93
Invested Capital Growth	Reverts to Maintenance	LTM+5Y	3%	91%	$3,185.34	$115.47	$983.05	$73.90
Justified TEV/REV	0.6x	LTM+6Y	3%	91%	$3,280.90	$118.81	$1,016.21	$85.64
Justified TEV/EBITDA	8.0x	LTM+7Y	3%	91%	$3,379.33	$122.48	$1,044.39	$94.30
Justified TEV/EBITA	9.8x	LTM+8Y	3%	91%	$3,480.71	$126.40	$1,071.32	$99.47
Justified TEV/UFCF	21.0x	LTM+9Y	3%	91%	$3,585.13	$130.34	$1,103.59	$98.07

Valuation

	ROIC	WACC	EVA	Enterprise Value	Total Debt	Other claims	Equity	Adjusted Price
LTM	13.9%	9.8%	$18.91	$1,148.02	$39.00	-$18.40	$1,127.43	$75.59
LTM+1Y	12.2%	10.0%	$18.47	$1,255.63	$31.50	-$164.90	$1,389.03	$90.90
LTM+2Y	12.2%	10.1%	$17.80	$1,318.34	$31.50	-$321.49	$1,608.34	$103.99
LTM+3Y	12.5%	10.2%	$20.37	$1,375.93	$31.50	-$477.84	$1,822.28	$117.42
LTM+4Y	12.5%	10.3%	$19.74	$1,434.35	$31.50	-$644.57	$2,047.42	$131.31
LTM+5Y	12.3%	10.4%	$17.70	$1,495.93	$31.50	-$809.97	$2,274.40	$146.21
LTM+6Y	12.1%	10.5%	$15.43	$1,567.75	$31.50	-$988.95	$2,525.20	$161.43
LTM+7Y	12.1%	10.6%	$14.39	$1,635.01	$31.50	-$1,181.52	$2,785.04	$177.64
LTM+8Y	12.1%	10.7%	$14.24	$1,700.88	$31.50	-$1,385.41	$3,054.79	$194.41
LTM+9Y	12.2%	10.8%	$14.28	$1,768.51	$31.50	-$1,595.41	$3,332.42	$204.94

Monte Carlo Simulation Assumptions

	Base	Stdev	Min	Max	Distribution
Revenue Variation	0	10%	N/A	N/A	Normal
Op. Costs Variation	0	10%	N/A	N/A	Normal
Market Risk Premium	6%	N/A	5%	7%	Triangular
Long term Growth	3%	N/A	3%	21%	Triangular
Terminal Value	0	0.1	N/A	N/A	Normal

Monte Carlo Simulation Results

	Intrinsic Value	1y-Target
Mean est.	$75.59	$90.90
σ(ε)	$1.07	$1.28
σ(ε) adjusted pric	$72.38	$87.06
Current Price	$67.17	
nalysts' median est.		$75.67

Landstar System Inc (LSTR: NASDAQ)

Financial Analysis By: Kevin Akbaraly – Industrials

Company Profile as of 2/18/2015

Market Price: $68.51
Industry: Road and Rail
Market Cap: $3,065M
52-Week: $56.44 - $80.61
Beta: 0.90

Source	Target Price	Recommendation
Siena	$83.70	BUY
Capital IQ	$74.14	OUTPERFORM
Yahoo Finance	$74.00	HOLD
Bloomberg	$74.46	BUY

Thesis

- Favorable macro outlook for the trucking industry
- Well positioned to benefit from expected market conditions
- Increase in operating margins expected through 2017
- Potential share repurchase during the year
- Current stock price offers an entry opportunity

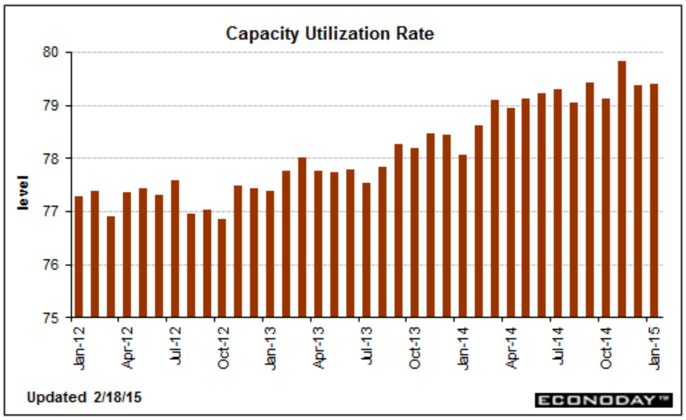
A BUY is recommended on Landstar System Inc. with a 1-year target price of $83.70 representing an upside potential of 24% compared to the current market price. Current market conditions are expected to remain strong through 2015. The company's particular business model could highly benefit from the expected macroeconomic trend, leading to growing revenues and improving operating margins. Also, the company could potentially distribute additional returns to shareholders through a share repurchase around the second quarter of 2015.

Company Overview

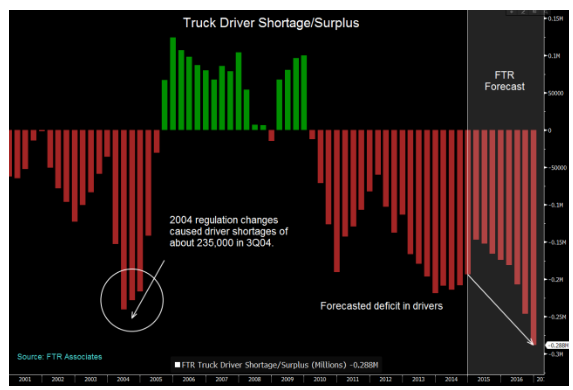
Landstar System Inc provides transportation management solutions within the U.S., Canada, and Mexico. The company offers a wide range of solutions that serves a broad number of customers by using its network of independent agents, third-party capacity owners and employees. Landstar has been founded in 1991 and is headquartered in Jacksonville, Florida.

Macro Outlook

The trucking industry is an essential component of the American economy as it services different sectors that require transportation of raw materials, finished goods, machinery, and other goods across the country and internationally. Since the Credit Crisis of 2008, the U.S. government has continuously aimed at reducing the unemployment rate to help the economy recover and gain in productivity. The BEA reported 2.4% GDP growth in 2014 from 2013, the highest full-year growth since 2010, and is expected to grow around 3% during 2015. The Industrial Production index showed a 4% year-over-year growth in 2014, and the Capacity Utilization rate reflecting the use of the nation's factories, mines and utilities recently reached its highest range with 79%-80% since 2008. The industry is dependent on a wide range of different markets such as the housing, automotive, machinery, retail, materials and oil & gas production. Although the latter is actually experiencing a slowdown due to lower energy prices, other industries are actively participating in the economy's expansion, which should lead to higher demand for goods transportation. Additionally, the expansion of both Canadian and Mexican economies could also lead to higher cross-border opportunities in the future.



One concern that is shared among the trucking industry is the driver shortage that is experienced since early 2010. Indeed, the aging driver workforce coupled with "intrusive" government's regulations has led to a decrease in both the number of available drivers and productivity in recent years. The Federal Motor Carrier Safety Administration has eased the hours-of-service regulation on December 2014, which aimed at limiting the number of hours spent driving and working since 1938. This new measure represents only a small change compared to prior rules, but it is expected to help slightly increase productivity among the industry. However, the deficit in drivers is still expected to exceed 2004 levels by the end of 2016 with 288,200. As a result, an increase in wage expense helps companies to retain their drivers, and related costs are directly transferred to shippers. Also, due to a limited supply, companies have more incentive to raise their prices accordingly in order to meet the demand side. FTR Transportation Intelligence estimates at least 4.4% increase in rates through 2016.



All Sectors	
Sectors vs. S&P 500	1 Year Performance
S&P 500 Index	+16.38%
Transportation	+24.39%
Medical	+19.50%
Retail / Wholesale	+16.59%
Computer and Technology	+16.54%
Business Services	+12.96%
Consumer Staples	+12.46%
Aerospace	+11.52%
Finance	+8.93%
Consumer Discretionary	+6.57%
Utilities	+5.90%
Auto / Tires / Trucks	+4.84%
Construction	+4.53%
Multi-Sector Conglomerates	+4.47%
Industrial Products	+2.72%
Basic Materials	-2.47%
Oils / Energy	-6.12%

Another factor impacting the trucking industry is related to oil prices. The commodity has seen an important downtrend since mid-2014, which led to more than 50% drop in prices. This can impact the trucking industry in two different ways. First, companies operating within the industry could benefit from lower gas prices, which in turn would lead to an increase in operating margins, or lower prices for shippers. Secondly, oil is also a major commodity that needs to be transported all around the world. Lower oil prices could lead oil companies to lower their production, which would therefore lower the needs of oil transportation. Recently, U.S. energy companies have increased their production level; however, a decline in production can be expected due to the number of companies struggling to survive.

Currently, the Transportation sector is the best performer year-to-date with 24.4% increase compared to 16.4% for the S&P500 index. This performance is almost 5% higher than for the Medical sector. Following the recent market environment and 2015 macroeconomic outlook, the

Transportation sector, and especially the Trucking industry could offer investors an attractive opportunity. As stated above, demand is expected to increase; supply is expected to remain limited, which in turn could lead to higher shipping rates and revenues. On the other hand, some attention should be given to the energy industry, which could also impact the demand for oil & gas transportation over the next year.

Landstar System Inc's Business Model

Landstar System Inc (LSTR) offers transportation management services to its customers through different transportation modes both domestically and globally. The company's goal is to offer its clients a solution for all their transportation and logistics needs from enterprise-wide to small shipping solutions including logistics and warehousing solutions. LSTR's main solutions include trucking, air and ocean freight, but also include documentation preparation, coordination and insurance (accounting only for 1% to 2% of revenues)

LSTR operations are based through the use of independent agents, business capacity owners and third-party capacity providers. Independent agents represent the company's sales workforce that are not directly employed by LSTR, but who have entered into contractual arrangements with the company. Their role is to market and provide their clients LSTR's transportation and logistics solutions. Once they receive an order from a client, they have to inform LSTR through the use of the company's internet-based application. Independent agents are paid based on a fixed rate of revenue for each deal they provide to LSTR. As of December 2013, the company reported 478 independent agents within their network generating $1 million or more of revenue (referred to as Million Dollar Agents). The average revenue per MDA was $5,081,000, and their contribution represented 91% of LSTR's total revenues. On January 29th, 2015, the company announced that its MDA network increased to 525, and increased their revenues by 18% during the year. Agents are spread all over the U.S. offering LSTR a competitive advantage in terms of geographic location, and do not need the company to increase its capital expenditures to gain market recognition. The company reported in its 2013 10-K that it "believes the company has more independent commission sales agents than any other asset-light integrated transportation management solutions company". Additionally, LSTR is protected by a non-competition agreement that has been agreed upon a contractual agreement with its independent contractors, which limits them to represent exclusively LSTR. The annual termination rate is about 3% or less.

Third-party capacity providers represent the external individuals or entities that provide LSTR with the vehicles needed by the company to perform its services. The company relies on different types of third-parties that are Business Capacity Owner (BCO) independent contractors, Truck Brokerage Carriers (TBC), air and ocean cargo carriers and railroads. Trucks provided by BCO contractors are using exclusive lease arrangements, while TBC and railroads capacity is provided through non-exclusive contractual arrangements. LSTR accounted 8,432 exclusive trucks provided by BCO contractors and 32,000 approved non-exclusive trucks that can be provided by TBCs. On January 29th, 2015, the company estimated its total truck capacity network at over 46,000. The management team stated that it believes LSTR has the highest number of trucks provided by BCO independent contractors within the United States. BCO, TBC and railroads contributes to about 50%, 43% and 3% of company's revenues respectively. Deals involving BCOs generally leads to higher gross profit margins compared to TBCs, but also incurs higher SG&A expenses. These third-parties are also spread all over the country, which increase substantially the company's presence and limits LSTR's capital expenditure requirements. Therefore, the company is able to meet the demand side coming from its independent agent network. All third-party capacity providers are generally compensated based on a fixed percentage of revenue related to the freight they haul.

Landstar's success has been built around its network's entrepreneurial spirit as it does not own tractors or employs drivers itself. This innovative business model provides the company many advantages that allow it to be efficient, and lower fixed costs at the same time. Indeed, an important portion of the company's operating costs are directly linked to the revenues it generates because it uses a compensation rate based on each shipment made. Also, because both agents and capacity providers are independent from LSTR, the quality of services provided to customers remain high in order for them to build a good relationship and continue to work along in the future.

Porter's Fiver Forces

Barrier to New Entrants

The threat of new entrants is considered to be moderate. Indeed, companies entering the trucking industry generally need to invest considerably in capital expenditure including vehicles and warehouses, in marketing and in the development of a network. The high competition could discourage potential entrants. However, due to the industry's fragmentation, one could also take advantage of an underserved sub-market. Another threat would also be related to small companies operating within small geographic areas, but current market conditions would favor global transportation and logistics solutions rather than local ones, emphasizing even more the need of initial capital expenditures.

LSTR's business model helps in the development of its competitive advantage. The use of independent sale agents and capacity providers has enabled the company to expand its presence all over the U.S. by limiting its needs of capital expenditures. Additionally, each member of the company's network often specialize within a specific market area, limiting LSTR's risks related to the industry's operational and geographic fragmentation.

Clients' Bargaining Power

Clients' bargaining power is considered to be low. As stated above, current market conditions show a rebound in productivity and economic expansion. Demand for goods transportation is expected to remain high during 2015, and supply is currently impacted by a driver shortage that is expected to worsen through 2016. Goods transportation is an essential component of economic expansion, and demand should come from various different sectors. Based on the demand and supply theory, shipment rates within the industry are expected to rise by at least 4.4% during 2015, and could see an upward pressure if economic conditions turn to be better than expected.

LSTR has stated during its Q4 earning call that their revenues were generated through a well-diversified client portfolio, and that they would raise prices according to market conditions. The company also expects an increase in operating margins through 2017.

Supplier's Bargaining Power

Supplier's bargaining power is considered to be moderate to high. "Supplier" has to be divided into two components here. First, truck manufacturers do not, and are not expected to put any pressure in terms of supply or increase in prices. Secondly, as stated above, driver shortage is a rising concern for the industry and is expected to worsen through 2016. The reasons that are causing this trend are an increase in the number of driver retiring, but also general complaints about wages and work conditions. Wage expenses are expected to rise over 2015 in order for companies to attract and retain drivers, but costs should be transferred to shippers following current market conditions.

LSTR is limiting its risks related to capacity shortage by its use of exclusive and non-exclusive contractual agreements with third-parties. The company reported that it has more BCO independent contractors than any other companies within the U.S. and that wage rates offered by third-parties were competitive among the industry, which help LSTR maintain a descent level of transport capacity.

Threat of Substitutes

Transportation can hardly be substituted. Indeed, goods transportation is an essential part of any economy, and without it, a country could suffer a brutal downturn in terms of sustainability. Different transportation modes are offered to clients depending on their needs. These solutions include road, rail, air, and ocean transportation.

LSTR is currently offering its services through all possible transportation modes within the U.S. and to a lesser extent to Canada and Mexico. However, trucking represents more than 90% of company's revenues and is the main driver for growth.

Industry Rivalry

The trucking industry is highly competitive and fragmented. Generally, companies operating within this industry specialize in a specific area from small packages or mailing services to massive machinery transportation, but also on a certain geographic area. Currently, there is a tendency to see a consolidation within the industry, helping companies gain in recognition and market share over the long term.

LSTR has been able to develop a business model that offers many advantages regarding current market conditions. Indeed, the company has found a way to limit its need in capital expenditure by expanding its visibility and capacity at the same time. Additionally, the company is able to take advantage of the current industry's fragmentation by offering its clients a portfolio of different solutions that respond to almost all transportation and logistics needs. The company is currently well positioned to benefit from market conditions that are expected during 2015 by increasing its revenues and margins over the year.

Management

Jim B. Gattoni has recently been promoted President and **CEO** of Landstar System Inc in December 2014. Mr Gattoni is a Certified Public Accountant and has joined the company in 1995 as Corporate Controller. He has been promoted as CFO and Vice President in 2007, a position that he held until he has been promoted CEO. Prior to LSTR, MR Gattoni was employed by KPMG within the audit division where he worked from 1987 to 1995. Mr Gattoni is well respected for his experience and knowledge within both the company and the industry.

Kevin Stout has been promoted as **CFO** in December 2014 following Mr. Gattoni's promotion. Mr. Stout joined Landstar in 1997 as Director of Financial Reporting. He has then been promoted as Director of Budget and Planning in 2003, and as President of Finance for the Landstar Carrier Group in 2004. He worked as Vice President and Corporate Controller as well from 2007 to 2014. Mr. Gattoni and Mr. Stout have been working together during 17 years, and he is highly trusted for his integrity, work ethic, and experience within the transportation industry.

Other executive members have been working for the company for more than 10 years in average. The executive team is considered solid and well experienced, which can bring the company forward in the future.

Key Statistics

In Millions of USD	FY 2011	FY 2012	FY 2013	FY 2014	Current/LTM	FY 2015 Est	FY 2016 Est
12 Months Ending	2011-12-31	2012-12-29	2013-12-28	2014-12-27	2014-12-27	2015-12-31	2016-12-31
Revenue	2,650.8	2,772.4	2,666.3	3,186.2	3,186.2	3,456.0	3,710.4
Growth %, YoY	10.4	4.6	-3.8	19.5	19.5	8.5	7.4
Gross Profit	407.8	398.7	380.3	446.7	446.7	793.2	646.8
Margin %	15.4	14.4	14.3	14.0	14.0	23.0	17.4
EBITDA	209.1	226.0	204.3	251.9	251.9	278.7	303.5
Margin %	7.9	8.2	7.7	7.9	7.9	8.1	8.2
Net Income Before XO	112.9	126.6	108.9	138.8	138.8	152.8	167.5
Margin %	4.3	4.6	4.1	4.4	4.4	4.4	4.5
Adjusted EPS	2.38	2.77	2.42	3.07	3.09	3.46	3.88
Growth %, YoY	30.8	16.4	-12.6	26.9	24.6	12.8	12.1

Landstar System Inc. reported $3,1863M of revenue for FY2014 representing an 19.50% growth compared to FY2013. On January 29th, 2015, the company announced $863M of revenue for Q4 2014 representing 25% growth compared to Q4 2013, which also represents the highest revenue reported quarterly, as well as annually for the company so far. Expectations were ranging $820M to $840M for the period. The management team stated that this performance was the result of significant opportunities "based across many industry segments, customers, and geographic regions".

Gross margins represented 14.02% of revenues for FY2014, a slight decrease from 14.26% during 2013, while operating margins increased to 7.04% from 6.62%. Net Income was $38.5M for FY2014 compared to $36.8M for FY2013, representing a 4.4% net margin for both yearly periods. The company stated during its most recent earning call that the company is aiming at improving operating margins through 2017.

The number of Million Dollar Agents has increased to 525 from 478 in FY2013. Also, the number of trucks provided by third parties has increased to more than 46,000, and are both expected to help the company capitalize over expected market conditions in the future. The termination rate of MDAs is still under 3% as of January 2015.

LSTR has discontinued its operations in December 2013 within the "Supply Chain" division that it acquired in 2009. The reason of that strategy was to focus further on its Transportation and Logistics division, which accounts for 98.6% of company's total revenues. The reminder 1.4% goes to the Insurance segment, which generated $36.6M, up from $35.9M in 2013.
The company reported $37M gain from the transaction, and announced a $1 special dividend during the year to shareholders.

Finally, the company also stated that the management was continuously looking for acquisition opportunities to consolidate its operations within the industry. However, LSTR does not foresee any potential target through 2015. It has been stated that the company might distribute some cash to shareholders during the year, which currently accounts for 15% of total assets on the balance sheet. The company bought back 940,000 shares around the second quarter of 2014, and still has 1.8M shares authorized under its repurchase program. Investors can therefore anticipate a potential share repurchase that may be announced around Q2 2015.

Valuation

The valuation of Landstar System Inc. has been made using a proforma that is presented on the last page of this report.
Revenue growth for FY2015 and FY2016 reflects market's expectations with 8.5% and 7.4% respectively. The growth rate has then been reduced to 3% by 1% decrement year over year to reflect an expected long-term growth of 3%. Operating costs over revenues for FY2015 has been estimated at 92% reflecting FY2014 level, and reduced to 90% by 1% decrements year-over-year to reflect management's focus on reducing operating costs. However, this reduction has been made in a conservative manner, and is still well above the industry average representing a 10-year median of 88% to reflect LSTR's particular business model. Unlevered beta has been set at 1.00 even though the 10-year median is about 0.77 only and the company's debt has been reduced to its all-time low. This approach is considered to be conservative in order to do not underestimate WACC levels over the future. Finally, 60% of SG&A expenses have been capitalized over 10 years in order to reflect the company's investments made in its technological applications that are provided to its sale agents network and third-party capacity provider. Indeed, the company launched its new smartphone-enabled GPS tracking tool called Landstar Connect, which provided timely in-transit visibility.

The 1-year target price expected is therefore $83.70, representing 24% upside potential based on current market price.

Conclusion

To conclude, a BUY is recommended on Landstar System Inc. (LSTR) with a target price of $83.70 representing a 24% upside potential compared to current market price. The company shows an innovative business model offering transportation and logistics solutions to its clients within the U.S., Canada, and Mexico. Current market conditions are expected to remain strong through 2015, and LSTR seems to be well-positioned to take benefit of this macroeconomic trend. Growing revenues and improving operating margins are expected over the next years. The company may also distribute some additional return to shareholders through a share repurchase around the second quarter of 2015. Finally, current share price level could offer investors an interesting entry opportunity.

CENTER FOR GLOBAL FINANCIAL STUDIES

Landstar System Inc.	LSTR	Analyst	Current Price	Intrinsic Value	Target Value	Divident Yield	Target Return	BUY
		Kevin Akbaraly	$68.51	$72.47	$83.70	2%	24.04%	

General Info

Sector	Industrials
Industry	Road and Rail
Last Guidance	Jan-29-2015
Next earnings date	4/23/2015

Market Data

Enterprise value	$3,013.87
Market Capitalization	$3,068.87
Daily volume	0.33
Shares outstanding	44.79
Diluted shares outstanding	45.17
% shares held by institutions	105.89%
% shares held by insiders	0.77%
Short interest	4.34%
Days to cover short interest	4.03
52 week high	$81.80
52-week low	$57.28
5y Beta	0.90
6-month volatility	18.21%

Peers	Market Cap.
Werner Enterprises Inc	$2,251.91
Swift Transportation Company	$3,867.47
Con-way Inc	$2,546.74
Knight Transportation Inc	$2,655.16

Current Capital Structure

Total debt/market cap	4.84%
Cost of Borrowing	2.31%
Interest Coverage	7062.39%
Altman Z	9.00
Debt Rating	AAA
Levered Beta	1.03
WACC (based on market value weights)	8.24%

Management

Professional	Title	Comp. FY2012	Comp. FY2013	Comp. FY2014
Gerkens, Henry	Executive Chairman, Member of	$ 2,159,263.00	$ 6,655,121.00	$ -
Gattoni, James	Chief Executive Officer and Presi	$ 2,013,507.00	$ 1,413,014.00	$ -
Beacom, Joseph	Chief Safety & Operations Office	$ 1,496,682.00	$ 1,065,308.00	$ -
Kneller, Michael	Vice President, General Counsel	$ 1,487,992.00	$ 1,074,335.00	$ -
O'Malley, Patrick	Chief Commercial & Marketing (	$ 1,505,442.00	$ 1,085,487.00	$ -
Stout, L.	Chief Financial Officer, Secretary,	$ -	$ -	$ -

Historical Performance

	LSTR	Peers	Industry	All U.S. firms
Growth	1.5%	3.2%	4.6%	6.0%
Retention Ratio	24.4%	50.2%	31.6%	61.6%
ROIC	22.0%	11.6%	20.3%	11.8%
EBITA Margin	7.0%	6.6%	10.0%	13.7%
Revenues/Invested capital	198.2%	172.8%	240.1%	202.3%
Excess Cash/Revenue	4.5%	4.7%	4.8%	18.5%
Unlevered Beta	0.77	1.09	0.87	0.95
TEV/REV	0.9x	0.9x	1.1x	2.4x
TEV/EBITDA	11.7x	7.3x	9.0x	11.3x
TEV/EBITA	12.9x	13.3x	15.5x	15.4x
TEV/UFCF	34.1x	42.2x	32.2x	26.8x

Past Earning Surprises

	Revenue	EBITDA	Norm. EPS
Last Quarter	3.4%	2.6%	6.2%
Last Quarter-1	-0.1%	1.4%	1.2%
Last Quarter -2	3.9%	1.8%	2.6%
Last Quarter -3	3.2%	2.0%	3.4%
Last Quarter -4	3.4%	-14.1%	-16.7%

Non GAAP Adjustments

Operating Leases Capitalization	100%	Straightline	10 years
R&D Exp. Capitalization	100%	Straightline	10 years
Expl./Drilling Exp. Capitalization	0%	N/A	N/A
SG&A Capitalization	60%	Straightline	10 years

Proforma Assumptions

Operating. Cash/Cash	0.0%
Unlevered Beta	1.00
Rev/Invested Capital	200.0%
Continuing Period Revenue Growth	3.0%
Long Term ROIC	13.6%
Invested Capital Growth	Equals to Maintenance
Justified TEV/REV	1.1x
Justified TEV/EBITDA	9.0x
Justified TEV/EBITA	13.3x
Justified TEV/UFCF	32.2x

Forecasted Profitability

Period	Rev. Growth	Adj. Op. Cost/Rev	Revenue	NOPLAT	Invested capital	UFCF
LTM	19%	85%	$3,186.17	$170.91	$1,124.67	$631.84
LTM+1Y	9%	86%	$3,457.71	$201.09	$1,659.33	$127.57
LTM+2Y	7%	85%	$3,713.43	$260.68	$1,740.20	$179.81
LTM+3Y	6%	84%	$3,936.13	$312.06	$1,825.09	$227.18
LTM+4Y	5%	84%	$4,132.82	$335.06	$1,913.38	$246.76
LTM+5Y	4%	84%	$4,298.01	$351.27	$2,002.23	$262.42
LTM+6Y	3%	84%	$4,426.95	$362.07	$2,084.79	$279.52
LTM+7Y	3%	84%	$4,559.76	$372.52	$2,164.57	$292.74
LTM+8Y	3%	84%	$4,696.56	$383.05	$2,241.85	$305.78
LTM+9Y	3%	84%	$4,837.45	$393.94	$2,316.49	$319.30

Valuation

	ROIC	WACC	EVA	Enterprise Value	Total Debt	Other claims	Equity	Adjusted Price
LTM	10.8%	8.2%	$28.95	$3,139.23	$145.95	-$200.95	$3,194.23	$73.10
LTM+1Y	17.9%	8.4%	$157.78	$3,543.43	$145.95	-$338.78	$3,736.26	$84.42
LTM+2Y	15.7%	8.5%	$126.21	$3,604.69	$145.95	-$514.35	$3,973.10	$89.73
LTM+3Y	17.9%	8.6%	$171.04	$3,705.50	$145.95	-$733.11	$4,292.66	$96.78
LTM+4Y	18.4%	8.7%	$185.48	$3,761.79	$145.95	-$970.82	$4,586.66	$103.33
LTM+5Y	18.4%	8.8%	$192.05	$3,800.68	$145.95	-$1,221.28	$4,876.02	$110.07
LTM+6Y	18.1%	8.9%	$192.10	$3,822.23	$145.95	-$1,484.40	$5,160.68	$116.13
LTM+7Y	17.9%	9.0%	$192.61	$3,836.42	$145.95	-$1,758.65	$5,449.12	$122.57
LTM+8Y	17.7%	9.1%	$193.35	$3,842.44	$145.95	-$2,043.87	$5,740.35	$129.08
LTM+9Y	17.6%	9.2%	$194.58	$3,837.46	$145.95	-$2,341.24	$6,032.74	$134.68

Monte Carlo Simulation Assumptions

	Base	Stdev	Min	Max	Distribution
Revenue Variation	0	10%	N/A	N/A	Normal
Op. Costs Variation	0	10%	N/A	N/A	Normal
Market Risk Premium	6%	N/A	5%	7%	Triangular
Long term Growth	3%	N/A	2%	6%	Triangular
Terminal Value	0	0.1	N/A	N/A	Normal

Monte Carlo Simulation Results

	Intrinsic Value	1y-Target
Mean est.	$73.10	$84.42
σ(ε)	$0.21	$0.24
3 σ(ε) adjusted price	$72.47	$83.70
Current Price	$68.51	
Analysts' median est.		$73.46

Reis, Inc. (REIS: NASDAQ)

Financial Analysis By: Mark Papuzza – Information Technology

Company Profile as of 2/18/2015

Market Price: $23.23
Industry: Internet Software and Services
Market Cap: $276.06M
52-Week: $16.36-28.82
Beta: 1.1

Source	Target Price	Recommendation
Siena	$ 28.00	Buy
Capital IQ	$ 30.00	Buy
Yahoo Finance	$ 30.00	Buy
Bloomberg	$ 30.00	Buy

Thesis

-Unique Proprietary Databases
-Subscription Business Model
- Financials: Increasing revenue, increasing EBITDA margins, no debt
- Significant Growth Opportunities

I am recommending a buy on Reis, Inc. because I am confident that these theses will contribute to the growth of the stock to the target price of $28.00. In a real estate market that is growing in size and complexity, Reis offers a carefully constructed and maintained database that provides real estate professionals with up to date and accurate information and analytical tools. Their subscription based business model allows them to maintain their customer base and work with them to improve their services, in turn bringing more subscribers in. Along with their growing revenue margin, EBITDA margin, and potential growth opportunities, the stock price should grow to the target price of $28.00.

Company Overview

Reis, Inc., through its subsidiary, Reis Services, provides commercial real estate market information and analytical tools to real estate professionals in the United States. It maintains an exclusive database which provides information on commercial properties, such as apartment, office, retail, warehouse/distribution, flex/research and development, self-storage, and seniors housing properties in the metropolitan markets and neighborhoods. Real estate investors, lenders, and other professionals utilize the data from the database to make the best buying, selling, and financing decisions possible. The company's products provide online access to their database of commercial real estate information and analytical tools designed to facilitate debt and equity transactions, and ongoing asset and portfolio evaluations.

Management

Reis, Inc. is led by their CEO Lloyd Lynford. He has been in charge since the company's creation over thirty years ago, proving his dedication and commitment to it. Reis co-founder and Executive Vice President Jonathon Garfield has also been with the company since it began. Their experience in the real estate market can be viewed as a huge plus to the value of this company. Rounding out management is Vice President/Chief Financial Officer Mark Cantaluppi, a Villanova graduate and certified public accountant. Besides their long term experience with Reis, perhaps the most notable aspect of the management team is their investment in the company. Management owns 22.41% of the company's stock. They care greatly about the movement of the stock, because it directly effects their own financial situations. Shareholders should feel confident in this stock because of the confidence and trust the management team has in it.

Unique Proprietary Databases

Reis, Inc. maintains three highly developed databases that provide information on property performance, new construction and sales comparables. On a daily basis, Reis surveys and receives data from building owners, leasing agents and managers. The databases are unique due to several key characteristics, such as breadth, geography, depth, history, and frequency. As for breadth, the database covers six property types which include apartments, office, retail, warehouse, research and development and self-storage properties. As for geography, the database covers up to 275 of the largest U.S. metropolitan commercial real estate markets, and over 6,800 isolated market areas with submarket boundaries proprietary to Reis. As for depth, it provides real estate professionals with accurate and up to date information that is essential for their work. This information includes, but is not limited to, occupancies, rents, rent discounts, tenant improvement allowances, lease terms, expenses, buyer, seller, purchase price, capitalization rate, financing details, etc. As for history, the databases contain data from up to 34 years through numerous cycles of economic/market peaks and troughs. As for frequency, the databases provide information in a timely manner. The market reports are available monthly or quarterly, while sales comparables and new, critical information is updated daily. Reis is continually working to expand these databases, specifically by adding more coverage of new areas. Having strong relationships with thousands of data sources, combined with their solid reputation in the industry, the database should continue to improve and fit the needs of real estate professionals everywhere.

Subscription Based Model

Reis, Inc. has approximately 1,000 subscribers to the "Reis Subscriber Edition," which is their primary web-based delivery platform for their market reports. The annual subscription fee costs between $35,000-$40,000, but depending on usage and what the subscriber is entitled too, the fee can surpass $1,000,000. A large percentage of Reis's revenue can be credited to their large subscribers. These large subscribers include banking institutions, property owners, brokers, lessors, builders, pension funds, insurance companies, developers, and government institutions. Reis's revenue model is predominantly based on these annual subscriptions. The contracts they have with their subscribers guarantee steady revenue – and combined with their high renewal rates provides an explanation for their growing revenue year by year. Reis controls more submarket information both by property type and geography than any of its competition. Their information is thorough and accurate, and so subscribers will have an easy decision to make when it is time to renew their subscription. The subscription based model has been very successful for Reis, and they will continue to keep their current subscribers content as well as bring in new subscribers.

Financials

Reis, Inc. has a very attractive balance sheet, especially when viewing their revenue growth, EBITDA growth, and net debt. Their revenue has seen continual growth year by year, as illustrated in the chart below. Their most recent earnings call posted the best third quarter results in the company's history, and reported revenue growth at 19.2% for the quarter, consistent with the growth they have been seeing over the years. Also shown in the chart below is the company's growing EBITDA margin. This proves that Reis is becoming a more profitable company, as they are finding ways to eliminate operating expenses that are eating into their bottom line. The growth in the EBITDA margin has generated value for shareholders, and is expected to continue to do so. In the company's latest earnings call, Lynford acknowledged the historic growth rates they have achieved, and stated that they plan to continue this growth. Another prominent aspect of Reis's financials is their net debt. As illustrated below, the company possesses more cash than debt. The fact that they have enough liquidity to cover their liabilities should be very encouraging to investors. Reis is proud of its debt-free balance sheet, and will work to keep it that way.

In Millions of USD	FY 2011	FY 2012	FY 2013	Current/LTM	FY 2014 Est	FY 2015 Est	FY 2016 Est
12 Months Ending	2011-12-31	2012-12-31	2013-12-31	2014-09-30	2014-12-31	2015-12-31	2016-12-31
Revenue	27.2	31.2	34.7	39.8	40.9	46.3	52.5
Growth %, YoY	12.3	14.9	11.2	16.8	17.8	13.2	13.4
Gross Profit	20.9	24.6	27.7	32.0	32.8	37.5	43.2
Margin %	76.8	78.8	79.9	80.3	80.3	81.1	82.2
EBITDA	6.1	7.7	9.4	12.0	12.1	14.3	16.9
Margin %	22.5	24.6	27.1	30.0	29.6	30.9	32.2

FY 20					
2008-12-					
4.0	-3.3	-8.9	-16.5	-5.0	-10.6

Significant Growth Opportunities

In order to sustain the growth they have achieved, Reis has several plans to adapt to market trends to keep the company moving forward. One of their primary opportunities lies in content expansion. A short-term goal in this field is to take advantage of the senior housing facilities sector. In May of 2015, coverage will expand by an additional 86 submarkets in 53 cities. The new coverage of independent living, assisted living, memory care and skilled nursing senior housing facilities is a sector that is in demand, and Reis will provide the information desired by senior housing investors. Following their expansion into the senior housing sector, Reis's next priority is expanding into the student housing sector. Potential additions after these two sectors include data centers, hotels and land. Reis is confident that no competitors can support better analytical products than they have. In order to increase the gap between themselves and the field they will enhance their products, specifically Mobiuss, in the short-term. They recently updated their Mobiuss product to feature interactive real-time credit and market analytics, and are working to use granular data when analyzing real estate trends and credit risk. The real estate market is growing in size and complexity, and Reis appears to be keeping up with the game.

Conclusion

I am recommending a buy on Reis, Inc. because their consistent financial growth should continue as a result of their unique databases, subscription business model, and their actions to grow and adapt to market trends. Reis is an industry leader in providing real estate information, with a management team that is both experienced and very invested in the company themselves. Owning 22.41% of shares, Reis management demonstrates great faith that their stock price will rise, and investors should feel confident about

Reis, Inc.	reis	Mark Papuzza	Current Price: 23.23	Lower Bound Intrinsic Value: $25.1	Lower Bound 1y-Target: $28	Dividend Yield: 2.35%	22.7%

General Info

Sector	Information Technology
Industry	Internet Software and Services

Description: Reis, Inc., through its subsidiary, Reis Services, provides commercial real estate market information and analytical tools to real estate professionals in the United States. It maintains a proprietary database containing information on commercial properties, such as apartment, office, retail, warehouse/distribution, flex/research and development, self storage, and seniors housing properties in the metropolitan markets and neighborhoods. The company's data is used by real estate investors, lenders, and other professionals to make informed buying, selling, and financing decisions; and debt and equity investors to assess, quantify, and manage the risks of default and loss associated with individual mortgages, properties, portfolios, and real estate backed securities. Its product portfolio features Reis SE, a flagship delivery platform aimed at larger and mid-sized enterprises; ReisReports, aimed at prosumers and smaller enterprises; and Mobiuss Portfolio CRE or Mobiuss, aimed primarily at risk managers and credit administrators at banks and non-bank lending institutions. The company's products provide online access to a proprietary database of commercial real estate information and analytical tools designed to facilitate debt and equity transactions, and ongoing asset and portfolio evaluations; and offer market trends and forecast analysis at metropolitan and neighborhood levels, as well as

Market Data

Enterprise value	$242.31
Market Capitalization	$333.35
Daily volume	0.85851
Shares outstanding	11.14
Diluted shares outstandi	11.53
% shares held by instituti	77.0%
% shares held by insiders	20.8%
Short interest	2.3%
Days to cover short inter	8.54
52 week high	$28.82
52-week low	$16.36
5y Beta	0.73
6-month volatility	30.39%

Peers

Symbol	NAME	Market Cap	TEV/EBITDA	P/B	EBITDA Margin	Total Debt/TEV	EBIT/Int. Exp.	Altman Z
NasdaqGS:CSGP	CoStar Group Inc.	$5,932.01	41.3x	4.0x	27%	1%	8.4x	
AIM:DGS	Digital Globe Servic	$39.05	16.9x	5.7x	10%	3%	662.0x	13.54
IQ1324068	World Energy Soluti			0.0x				1.51
NasdaqCM:MEET	MeetMe, Inc.	$76.29	82.7x	0.8x	2%	6%	(3.2x)	3.27
NasdaqGS:ZIXI	Zix Corporation	$211.94	21.2x	3.1x	18%	0%		
AMEX:GLOW	Glowpoint, Inc.	$37.60	13.4x	3.9x	11%	24%	0.5x	-5.81
TSE:2492	Infomart Corporatio	$58,426.56	21.6x	0.0x	54%	1%	486.5x	23.20
NasdaqGS:RP	RealPage, Inc.	$1,527.34	43.6x	4.9x	3%	3%	(3.2x)	4.22
NasdaqCM:ARIS	ARI Network Servic	$51.37	29.0x	2.6x	6%	17%	2.3x	-1.14
JASDAQ:3633	GMO Pepabo, Inc.	$7,117.29	4.9x	3.4x	19%	0%		3.92
Peers' Median		$211.94	21.6x	3.6x	11%	3%	2.3x	3.59
reis		$258.70	23.8x	2.7x	26%	0%	60.2x	6.01

Management

Professional	Title	Comp. FY2011	Comp. FY2012	Comp. FY2013
Lynford, Lloyd	Chief Executive	$1,130,325.00	$ 1,119,510.00	$ 1,181,662.00
Cantaluppi, Mark	Chief Financial	$ 530,803.00	$ 539,720.00	$ 555,304.00
Garfield, Jonathan	Executive Vice	$ 962,249.00	$ 954,650.00	$ 962,874.00
Sander, William	President of Reis	$ 700,682.00	$ 693,418.00	$ 686,723.00
Richardson, Michael	Executive Vice	$ -	$ -	$ -

Performance

	reis Last	reis 10y Med.	Peers Last	Peers 10y Med.	Industry Last	Industry 10y Med.	All U.S. firms Last	All U.S. firms 10y Med.
ROIC	7.4%	2.8%	7.09%	4.25%	14.88%	11.97%	11.03%	11.85%
EBITA Margin	24.6%	8.5%	23.16%	15.68%	13.91%	14.11%	13.64%	13.67%
Imputed Rev./Invested cap.	0.32	0.33	0.55	0.78	1.32	1.32	1.72	2.02
Excess Cash/Total Cash	10.74%	N/A	23.99%	40.64%	59.99%	54.85%	23.11%	18.48%
Total Cash /Rev.	41.18%	45.95%	31.50%	58.03%	70.45%	67.27%	32.95%	30.26%

Current Capital Structure

Total debt/market cap	0.00%
Cost of Borrowing	0.00%
Interest Coverage	60.20
Debt Rating	AA
5y Beta	2.17
WACC (based on market value weights)	7.3%

Past Earning Surprises

	Revenue	EBITDA	Norm. EPS
Last Quarter	3.3%	11.2%	25.0%
Last Quarter-1	2.9%	7.6%	14.3%
Last Quarter -2	7.5%	24.0%	80.0%
Last Quarter -3	0.3%	11.1%	80.0%
Last Quarter -4	-0.7%	-2.8%	-25.0%

Last Guidance May-01-2014 Next earnings 3/6/2015 Last Earning Call Transcript: www.reis.com

Reis, Inc. announced unaudited consolidated financial results for the first quarter ended March 31, 2014. Income from continuing operations was $1,046,980, or $0.10 per basic share and $0.09 per diluted share, for the quarter ended March 31, 2014. For the quarter ended March 31, 2013, the company had income from continuing operations of $402,066, or $0.04 per basic and diluted share. On a consolidated basis, the company had net income of $669,102, or $0.06 per basic and diluted share, for the three months ended March 31, 2014. For the three months ended March 31, 2013, the company had net income of $250,434, or $0.02 per basic and diluted share. Subscription revenue was $9,946,045 against $8,234,328 a year ago. Income before income taxes and discontinued operations was $1,651,980 against $667,066 a year ago. EBITDA was $2,922,000 against $1,906,000 a year ago. Adjusted EBITDA was $3,357,000 against $2,487,000 a year ago. Cash generation of $5,228,000 in the quarter. During the first quarter, the company had CapEx of nearly $1.1 million, related to the expansion of databases and websites.

For 2014, The company anticipates that 2014 annual revenue growth will exceed 2011 through 2013 compound annual growth rate of 12.8%. In fact, based upon most current view of the year, The company expects that revenue growth will range between 15% and 16% of sustaining an EBITDA margin of approximately 40%. The expectation of additional spending in 2014 may result in margins for future quarters being below the 40.9% 2014 first quarter Services EBITDA margin.

Continuing Period Assumptions

Money market rate as of today	0.49%	Risk-Free rate	2.6%	LT Op. Costs/Rev	70.0%
Annual increase (decrease) in interest rates	0.10%	Op. Cash/Rev.	0.00%	LT WACC	8.3%
Yield Spread acceleration	1.2	Op. Cash/Cash	0.0%	LT Term ROIC	11.1%
Marginal Tax Rate	37.5%	LT Growth	4.5%	Growth in PPE	Equals to Maintenance

: weights are either implied from the stability of each time-series"--i.e., median/(max.-min.), or estimated based on the "uniqueness" of its competitive power--i.e., buyers power, suppliers power, competitive rivalry, threat of substitution,

	Rev./Capital Last	Rev./Capital 10y Median	LT Imputed Growth Last	LT Imputed Growth 10y Median	LT Op. Costs/Rev. Last	LT Op. Costs/Rev. 10y Median	Unlevered Beta Last	Unlevered Beta 10y Median	Multiples (10Y Historical Median Value) TEV/Rev.	TEV/EBITDA	TEV/EBITA	TEV/UFCF
reis	0.32	0.33	2.9%		78.3%	81.60%	0.94	0.85	3.0x	20.0x	19.2x	8.8x
Peers	0.55	0.78	11.0%	16.2%	82.7%	84.01%	0.88	0.99	6.7x	40.2x	53.0x	497.6x
Primary Industry	1.32	1.32	17.2%	12.4%	82.9%	81.37%	1.07	1.14	3.3x	16.7x	19.9x	30.5x
Industry	1.32	1.32	17.2%	12.4%	82.9%	81.37%	1.07	1.14	3.3x	16.7x	19.9x	30.5x
Industry Group	1.46	1.59	11.0%	9.9%	81.5%	80.94%	1.04	1.08	3.4x	14.3x	18.0x	27.3x
Sector	1.44	1.56	3.8%	8.4%	82.7%	82.80%	1.15	1.18	2.8x	13.2x	17.4x	27.1x
All U.S. Firms	1.72	2.02	6.6%	6.0%	80.4%	81.20%	0.98	0.95	2.4x	11.3x	15.4x	26.8x
GDP	N/A	N/A	3.9%	3.2%	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
reis long-run estimate	1.30		4.50%		70.00%		0.85		5.0x	8.0x	18.0x	30.5x

Capitalization

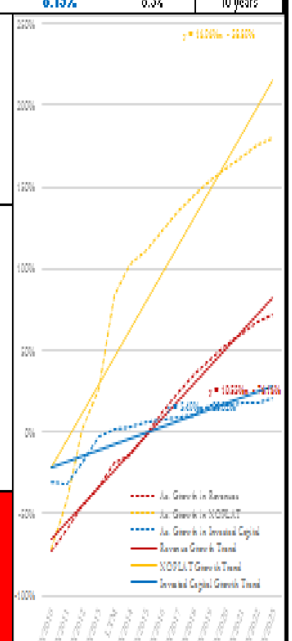
Operating Leases	100%
	Straightline
	10 years
R&D Exp.	100%
	Straightline
	10 years
Expl./Drilling Exp	0%
	Straightline
	10 years
SG&A	0%
	Straightline
	10 years

Explicit Period Assumptions

	FY2013	FY2014	FY2015	FY2016	FY2017	FY2018	FY2019	FY2020	FY2021	FY2022	FY2023	to ∞
Growth	11.2%	17.8%	13.2%	12.5%	12.0%	11.0%	10.0%	8.0%	7.0%	7.0%	5.0%	4.5%
Op.Costs/Rev.	78.3%	70.0%	70.0%	70.0%	70.0%	70.0%	70.0%	70.0%	70.0%	70.0%	70.0%	70.0%
WACC	7.27%	7.33%	7.42%	7.52%	7.62%	7.70%	7.80%	7.90%	8.00%	8.09%	8.19%	8.3%

Valuation

	LTM	LTM+1Y	LTM+2Y	LTM+3Y	LTM+4Y	LTM+5Y	LTM+6Y	LTM+7Y	LTM+8Y	LTM+9Y
NOPLAT	$8.0	$9.4	$10.4	$11.6	$12.8	$14.0	$15.2	$16.2	$17.4	$18.3
Invested capital	$104.3	$117.4	$119.7	$121.6	$123.3	$128.4	$131.1	$132.3	$132.9	$135.8
ROIC	7.4%	8.4%	8.9%	9.7%	10.6%	11.4%	11.8%	12.4%	13.1%	13.8%
UFCF	$12.16	$5.82	$8.21	$9.63	$11.22	$8.89	$12.42	$15.04	$16.81	$15.40
EVA	$0.97	$1.12	$1.66	$2.55	$3.55	$4.62	$5.14	$5.83	$6.74	$7.61
Terminal value										$388.80
Enterprise value (mid-year adj.)	$278.06	$298.57	$314.40	$329.04	$343.49	$359.05	$375.68	$391.62	$406.25	$420.23
Total Debt	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00
Minority Interest	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00
Preferred Equity	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00
Capitalized Operating leases	$15.14	$26.76	$28.95	$31.11	$33.01	$38.41	$41.24	$42.45	$43.18	$46.02
V of Unfunded Pension Plan Liabilities	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00
act of options,warrants, and converts	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00
Other claims on operating assets	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00
Non-operating cash and LT investments	$16.40	$35.28	$49.44	$61.93	$74.11	$87.38	$101.59	$116.75	$133.13	$150.22
Equity value	$279.32	$307.10	$334.90	$359.86	$384.60	$408.02	$436.04	$465.93	$496.19	$524.44
Shares outstanding	$11.14	$11.14	$11.14	$11.14	$11.14	$11.14	$11.14	$11.14	$11.14	$11.14
Price per share as of 2/18/2015	$26.04	$28.62	$30.93	$33.16	$35.34	$37.70	$40.18	$42.87	$45.52	$47.09



Monte Carlo Simulation Assumptions

	Base	Stdev	Min	Max	Distribution
Revenue Variation	0%	10.0%	N/A	N/A	Normal
Op. Costs Variation	0%	10.0%	N/A	N/A	Normal
Market Risk Premium	5.5%	N/A	5.0%	7.0%	Triangular
Long term Growth	4.50%	N/A	3.2%	16.2%	Triangular
Terminal Value	0%	10.0%	N/A	N/A	Normal

Monte Carlo Simulation Results

	Intrinsic Value	1y-Target
Mean est.	$26.04	$28.62
σ(ε)	$0.32	$0.22
) adjusted price	$25.08	$27.96
Current Price	$23.23	
sts' median est.		$30.00

CGFS

Boston Beer Company Inc. (SAM: NYSE)

Financial Analysis By: Nicholas Luca – Consumer Goods

<u>Company Profile as of 2/19/2015</u>

Market Price: $309.61
Industry: Beverages - Brewers
Market Cap: $4.02B
52-Week: $208.82 - $325.00
Beta: 0.25

Source	**Target Price**	**Recommendation**
Yahoo Finance	$316	BUY
Bloomberg	$319	BUY
Siena	$291	SELL

<u>Thesis</u>

-Threat of new entrants in an already competitive market
-Diminishing comparative quality of product to competitors
-Loss of brand loyalty
-Unsustainable growth

Company Overview

The Boston Beer Company produces and sells alcohol beverages primarily in the United States, Canada, Europe, Israel, the Caribbean, the Pacific Rim, Mexico, and Central and South America. The company primarily sells their Samuel Adams or the Sam Adams brand names which contain over 50 different styles. Their portfolio also contains 10 flavored malt beverages under their Twisted Tea brand name and 8 hard cider beverages under the Angry Orchard brand name. It sells its products to a network of wholesale distributors, who in turn sell to retailers, such as pubs, restaurants, grocery stores, convenience stores, package stores, stadiums, and other retail outlets. The Boston Beer Company, Inc. was founded in 1984 and is based in Boston, Massachusetts.

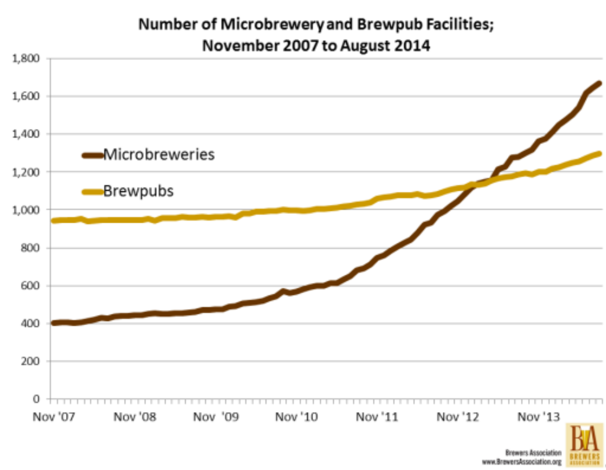
Management

Their management team is led by Founder and Chairman James "Jim" Koch, a graduate of Harvard that left his prior position in a consulting firm to transform a beer recipe, founded by his great grandfather in 1860, into a product. Koch is often credited for popularizing craft beer in the 1980s and 1990s, a time when the alcoholic beverage market was dominated by lighter style, less flavorful beer producers such as Budweiser and Coors. Jim was known as a leader in the marketing aspect of the company, but now at age 65, has less in store presence in retailers and brewpubs. Jim, as a founder of the company, admires the traditional style of craft beer that he grew up on, but unfortunately his ability to adapt to where the market has headed has been relatively slow.

Next on the management team is President/CEO Martin Roper, who recently has been in headlines for selling 10,000 of his shares of the company, lowering his shares of SAM by 90%. Roper has been with the company since 1999, shifting his position from COO to CEO in January of 2001.

New Entrants/Preexisting Competitors

The surge of a richer, more flavorful beer would be said to be started around 2010-2011 in the United States. Although craft beers have been present since the 70's, it wasn't until recently they became a growing percent of the beer industry at roughly 8% currently and expected to be low double digits by the end of 2015, according to founder Jim Koch. A distinction between a craft brewery and a microbrewery is a matter of production numbers, with microbreweries having an annual production of less than 15,000 US beer barrels and craft brewery's producing between 15,000 and 6,000,000 barrels per year. Microbreweries basically have the ability to emerge into craft breweries, a feat that is becoming tougher now because of the increasing competition. The most recent number of microbreweries has been updated to be over 1,700 in the U.S. as of August 2014, a number that is almost double since emergence of craft beer in 2010-2011 which stood at 700 microbreweries.



	2013
Anheuser-Busch InBev	47.5%
SABMiller	14.9%
Molson Coors	14.4%
Constellation Brands	6.8%
Heineken	4.4%
S & P	3.2%
Yuengling	1.6%
Boston Beer	1.4%
Diageo	0.7%
Sierra Nevada	0.5%
Total	*95.4%*

Source: Euromonitor International

The leaders of the industry understand that craft beer is growing and that although they only currently represent a relatively small portion of the beer industry, there is a lot of growth expected in upcoming years. Market leaders want to eliminate this competition through acquisition. Rather than competing for shelf space, they would rather add them to their portfolio through buying them out at a fairly cheap price, figuring they're fairly new companies. These sought after microbreweries have only been around so long, so for brand acceptance is a huge growth figure when it comes to acquiring them. Essentially, these microbrews are creating and perfecting certain styles that connoisseurs love, a task that these light beer developers struggle with. To compensate with that, rather than trying to create a similar recipe or style, they are merely acquiring the breweries. SAM is up against competitors that are in a much better position of acquiring these microbreweries. In a $92 billion U.S. beer industry, SAM represents an inferior percent of the market, as compared to the top three leaders that combined hold 77% of the industry. The top performers are acquiring more and more companies each quarter.

The market leader, Anheuser-Busch InBev has spent the past few years acquiring competing breweries to expand its reach into a growing market. Some of these acquisitions include Chicago's Goose Island for $38.8 million in 2011, the largest craft beer acquisition ever. Another notable acquisition is of Blue Point Brewery of NY, which was a $24 million acquisition in 2013. Adding to the buyout of microbreweries, BUD is also buying stake into craft competitors within the industry. They now have 32% stake in Craft Brew Alliance (NASDAQ:BREW), one of the few public craft breweries. If you add up their more popular acquisitions: Blue Point, 10 Barrel, and Elysian, BUD added about 150,000 bbls to its portfolio.

Even though SAM is in a decent position financially to endure some debt in acquiring microbreweries, any brewery worth pursuing can easily be out-bid by the big contenders like BUD. In an industry filled with partnering, there isn't much discussion along acquiring other breweries or partnering coming from discussion with management.

Loss of Brand Loyalty

Rise of local breweries

While Sam Adams once topped leaders like Budweiser as far as quality goes, with the new fast paced growth of local breweries, Sam Adams is now being outdone in quality. What they used to be able to sell themselves as, the highest quality beer, they are now unable to. As stated before, they are adding more and more styles to their portfolio in hopes of competing with the smaller breweries that create all new styles of beer. But this isn't what craft consumers are looking for. They don't want mass produced, mass marketed beers. Beer snobs want to know the quality in the beer they're ordering is superb to the other choice. The assumption is that the local brewery will always be fresher and better in taste as compared to the Sam Adams that you can order at almost any bar or restaurant now. The issue with Samuel Adams is they wanted to get their name in every bar, and with that they are becoming the Budweiser and Coors Light of craft beer now. Their brand is so well known and recognized, of which is great to new customers to the craft market, but for those that have been consumers of craft beer for quite some time are looking at the Sam Adams as a mass produced, better Bud Lite.

These viewpoints are heavily reflected in the ratings all across the web, more specifically in the table below, of which charts Samuel Adams at only the 39th best brewery in the Northeast region. Of the top 25, there are four Boston breweries higher ranked than Boston's very own, Samuel Adams.

	Brewery	Location	# Beers	Avg ABV	SOLID	SOLID%	Avg BAR	BAR25	BAR
1.	Hill Farmstead Brewery	Greensboro Bend, VT, US	**74**	5.6	68.29	100%	6.0	165.01	**444.08**
2.	Southern Tier Brewing Company	Lakewood, NY, US	**94**	7.5	55.12	97%	1.93	127.57	**181.4**
3.	Jack's Abby Brewing	Natick, MA, US	**52**	6.3	60.56	100%	3.48	81.35	**181.21**
4.	Allagash Brewing Company	Portland, ME, US	**65**	7.7	58.48	100%	2.76	90.06	**179.36**
5.	New England Brewing Co.	New Haven, CT, US	**31**	6.5	61.89	100%	4.78	64.19	**148.21**
6.	Lawson's Finest Liquids	Warren, VT, US	**29**	6.1	61.08	100%	4.14	59.48	**120.04**
7.	Maine Beer Company	Portland, ME, US	**22**	6.6	60.75	100%	4.57	49.69	**100.58**
8.	Brewery Ommegang	Cooperstown, NY, US	**48**	7.3	57.92	100%	2.06	45.89	**98.79**
9.	Brooklyn Brewery	Brooklyn, NY, US	**91**	7.1	54.03	92%	1.06	78.68	**96.4**
10.	Tree House Brewing Company	Brimfield, MA, US	**18**	5.6	69.21	100%	5.18	35.21	**93.15**
11.	Night Shift Brewing	Boston, MA, US	**43**	6.1	58.4	98%	1.93	42.45	**82.78**
12.	The Alchemist Pub & Brewery	Waterbury, VT, US	**14**	7.5	58.46	93%	5.63	46.24	**78.84**
13.	Sixpoint Brewery	Brooklyn, NY, US	**56**	6.0	55.02	96%	1.32	53.36	**73.81**
14.	Clown Shoes	Ipswich, MA, US	**46**	9.1	55.41	100%	1.08	33.03	**49.88**
15.	Barrier Brewing Company	Oceanside, NY, US	**37**	5.6	56.78	97%	1.34	31.08	**49.74**
16.	Pretty Things Beer & Ale Project	Boston, MA, US	**24**	7.6	60.1	100%	2.01	20.94	**48.17**
17.	Smuttynose Brewing Co.	Portsmouth, NH, US	**50**	6.6	53.48	96%	0.79	34.89	**39.37**
18.	SingleCut Beersmiths	East Elmhurst, NY, US	**19**	5.6	59.09	100%	1.89	16.94	**35.89**
19.	Peekskill Brewery	Peekskill, NY, US	**19**	3.5	56.18	100%	1.89	20.78	**35.84**
20.	Relic Brewing Co.	Plainville, CT, US	**18**	6.8	59.1	100%	1.8	15.61	**32.34**
21.	Harpoon Brewery	Boston, MA, US	**52**	6.0	53.47	100%	0.61	27.26	**31.9**
22.	Great South Bay Brewery	Bay Shore, NY, US	**18**	5.8	56.65	94%	1.74	18.3	**31.32**
23.	Cambridge Brewing Co.	Boston, MA, US	**26**	5.9	56.19	100%	1.18	17.73	**30.8**
24.	Portsmouth Brewery (NH)	Portsmouth, NH, US	**30**	6.1	53.65	93%	1.01	30.89	**30.31**
25.	Wormtown Brewery	Worcester, MA, US	**14**	6.5	57.54	100%	2.04	16.58	**28.61**
39.	Boston Beer Company (Samuel Adams)	Boston, MA, US	**133**	6.8	50.73	82%	0.08	133.91	**11.21**

Quality

With these new entrants come new styles of beer. Microbreweries attempt to differentiate themselves from others through developing new styles, or even creating hybrids of two or more styles. This is ultimately leading to thousands of different styles on the market. SAM has been able to diversify, having over 50 barrels of different styles; and also adding the Angry Orchard brand that provides for the new hard cider craved by consumers. They clearly see the rise of new styles, and are attempting to expand their styles rapidly to keep up. However, while SAM is trying to keep up the varieties coming out, they are losing quality within their other styles. They have expanded their Samuel Adams line so much that the quality control is fading. With less focus on each beer individually, they are losing a grasp of their beer quality as a whole. When they first started, Koch with the help of his brew masters perfected their first style, the Boston Lager. This is what got the ball rolling for Sam Adams. They emphasized so much on the precision of making the beer taste great and that was what they were known for. Now, with the vast varieties, the quality just isn't there, and the industries connoisseurs are responding.

Poor Adaption of Popular Styles

On its website, the company writes, "30 years later, we're still brewing for the craft beer revolution with our latest release, Rebel IPA." SAM has realized a demand for the IPA but the authenticity of their IPA is questioned. Koch grew the company through "door to door" sales with his family's coveted recipe. His IPA brand is noted as a "West Coast IPA", with a highly unique and different bottle design. Their addition of a popular style allowed them to compete in the IPA category, but their approach on the style is very questionable compared to what originally grew this company. The bottle also has been critiqued as identical to a competitor's bottle, Punk IPA of BrewDog Brewery. Now even though the IPA segment seems to be gaining popularity at a quick rate, the popularity of Sam Adam's Rebel IPA is actually weakening according to BeerGraphs.com, shifting from 3.5/5 towards a 3.0/5 in 2014.

<u>Unsustainable Growth</u>

Samuel Adams is regarded as the pioneer for craft beer, as it was the first of its kind. Now, after 30 years, they have raised a lot of interest from others, as new entrants are overwhelming the market. In a market where gaining brand acceptance is as easy as developing a good recipe, it is hard for Sam Adams to be the leader in craft beers. Currently, there are record numbers of people entering the craft beer liking. Samuel Adams is almost the stepping stone from light, low-quality beer, to the luxury high end craft beers. They are capitalizing on this shift and ultimately once the number of new consumers starts to slow in pace, they are to suffer severely.

<u>Conclusion</u>

The Boston Brewing Company is a **<u>SHORT</u>** immediately following Quarter 4 earnings of which are released on February 24, 2015, due to historically strong Q4 earnings. SAM is a short because of unsustainable growth due to an immense increase in competitors within the market. Their products are being questioned by the industry's connoisseurs, largely concerning the quality of their product in comparison to their competitors. Although the Better Beer (Craft beer) segment continues to grow, the percent of market share for Boston Beer Company is soon to decline with new competitors establishing acceptance from consumers. With minimal focus on acquiring emerging microbreweries, while market leaders Anheuser Busch InBev (BUD) and Molson Coors (TAP) continue to make acquisitions, SAM is going to have a limited portfolio to sell to distributers, eventually leading to less shelf, cold box and tap space. The reason for past success is heavily due to the rapid growth in the craft beer market, of which they held most of the market share. Now, with over 3,000 breweries in the United States alone, while over half of them are microbreweries, SAM must differentiate themselves, of which will be tough with a fully exhausted product line and limited acquisitions.

CENTER FOR GLOBAL FINANCIAL STUDIES

Boston Beer Co. Inc.	SAM	Analyst	Current Price	Intrinsic Value	Target Value	Divident Yield	Target Return	BEARISH
		Nicholas Luca	$309.70	$271.19	$291.75	0%	-5.79%	

General Info

Sector	Consumer Staples
Industry	Beverages
Last Guidance	Oct-30-2014
Next earnings date	2/24/2015

Market Data

Enterprise value	$3,967.55
Market Capitalization	$4,024.14
Daily volume	0.01
Shares outstanding	13.06
Diluted shares outstanding	13.49
% shares held by institutions	63.36%
% shares held by insiders	29.93%
Short interest	7.60%
Days to cover short interest	12.30
52 week high	$325.00
52-week low	$208.82
5y Beta	0.54
6-month volatility	25.74%

Peers	Market Cap.
Anheuser-Busch InBev SA/NV	
Molson Coors Brewing Company	$14,192.04
Brown-Forman Corporation	$19,434.68
0	
Craft Brew Alliance, Inc.	$235.18
Grupa Zywiec Spolka Akcyjna	$3,937.00
Guangzhou Zhujiang Brewery Co., Ltd	$9,393.03
Royal Unibrew A/S	$12,252.74

Current Capital Structure

Total debt/market cap	0.01%
Cost of Borrowing	0.00%
Interest Coverage	
Altman Z	14.16
Debt Rating	AAA
Levered Beta	0.70
WACC (based on market value weights)	6.83%

Management

Professional	Title	Comp. FY2011	Comp. FY2012	Comp. FY2013
Koch, C.	Founder and Chairman of the Bo	$ 754,163.00	$ 817,949.00	$ 994,313.00
Roper, Martin	Chief Executive Officer, Presiden	$ 933,818.00	$ 1,052,493.00	$ 1,519,541.00
Urich, William	Chief Financial Officer, Principal	$ 3,437,998.00	$ 599,363.00	$ 617,682.00
Lance, Thomas	Vice President of Operations	$ 693,401.00	$ 721,454.00	$ 787,353.00
Geist, John	Vice President of Sales	$ 4,078,189.00	$ 527,448.00	$ 597,441.00
Wade, Kathleen	Vice President of Legal and Corp	$ -	$ -	$ -

Historical Performance

	SAM	Peers	Industry	All U.S. firms
Growth	27.1%	10.9%	14.1%	6.0%
Retention Ratio	6.5%	83.8%	96.1%	61.6%
ROIC	295.2%	11.2%	16.4%	11.8%
EBITA Margin	12.6%	25.0%	12.5%	13.7%
Revenues/Invested capital	348.1%	55.0%	136.1%	202.3%
Excess Cash/Revenue	9.6%	5.2%	11.1%	18.5%
Unlevered Beta	0.72	0.29	0.68	0.95
TEV/REV	1.5x	0.7x	1.8x	2.4x
TEV/EBITDA	12.8x	2.2x	11.8x	11.3x
TEV/EBITA	15.4x	2.7x	22.3x	15.4x
TEV/UFCF	24.1x	2.4x	33.2x	26.8x

Past Earning Surprises

	Revenue	EBITDA	Norm. EPS
Last Quarter	4.3%	0.0%	24.1%
Last Quarter-1	3.1%	0.0%	5.0%
Last Quarter -2	2.6%	0.0%	-8.8%
Last Quarter -3	6.3%	0.0%	-10.6%
Last Quarter -4	8.0%	0.0%	6.5%

Non GAAP Adjustments

Operating Leases Capitalization	100%	Straightline	10 years
R&D Exp. Capitalization	0%	N/A	N/A
Expl./Drilling Exp. Capitalization	0%	N/A	N/A
SG&A Capitalization	0%	N/A	N/A

Proforma Assumptions

Operating. Cash/Cash	0.0%			
Unlevered Beta	0.70			
Rev/Invested Capital	280.0%			
Continuing Period Revenue Growth	3.0%			
Long Term ROIC	26.9%			
Invested Capital Growth	Equals to Maintenance			
Justified TEV/REV	1.0x			
Justified TEV/EBITDA	8.0x			
Justified TEV/EBITA	13.0x			
Justified TEV/UFCF	18.0x			

Forecasted Profitability

Period	Rev. Growth	Adj. Op. Cost/Rev	Revenue	NOPLAT	Invested capital	UFCF
LTM	27%	79%	$890.57	$111.39	$378.05	$8.80
LTM+1Y	14%	75%	$1,013.85	$143.55	$284.43	$140.06
LTM+2Y	10%	75%	$1,111.41	$155.97	$286.49	$153.91
LTM+3Y	9%	74%	$1,206.72	$173.75	$288.37	$171.86
LTM+4Y	5%	74%	$1,272.99	$184.37	$289.89	$182.85
LTM+5Y	4%	74%	$1,326.16	$191.48	$295.69	$185.68
LTM+6Y	4%	74%	$1,376.31	$198.48	$298.89	$195.27
LTM+7Y	4%	74%	$1,424.62	$205.35	$300.39	$203.86
LTM+8Y	3%	74%	$1,471.79	$212.15	$301.49	$211.05
LTM+9Y	3%	74%	$1,518.27	$218.82	$305.07	$215.24

Valuation

	ROIC	WACC	EVA	Enterprise Value	Total Debt	Other claims	Equity	Adjusted Price
LTM	40.4%	6.8%	$90.54	$3,421.22	$0.58	-$28.28	$3,448.93	$272.15
LTM+1Y	47.8%	7.0%	$115.91	$3,445.10	$0.58	-$270.42	$3,714.94	$292.50
LTM+2Y	54.8%	7.1%	$136.36	$3,538.13	$0.58	-$417.56	$3,955.11	$310.57
LTM+3Y	60.6%	7.3%	$153.58	$3,626.97	$0.58	-$585.69	$4,212.08	$330.40
LTM+4Y	63.9%	7.4%	$163.49	$3,707.27	$0.58	-$767.66	$4,474.35	$350.78
LTM+5Y	66.0%	7.6%	$172.60	$3,791.51	$0.58	-$955.50	$4,746.43	$372.94
LTM+6Y	67.1%	7.7%	$177.20	$3,874.26	$0.58	-$1,155.89	$5,029.57	$394.10
LTM+7Y	68.7%	7.9%	$182.39	$3,963.28	$0.58	-$1,368.13	$5,330.82	$417.58
LTM+8Y	70.6%	8.0%	$188.40	$4,055.19	$0.58	-$1,591.21	$5,645.82	$442.00
LTM+9Y	72.6%	8.2%	$196.16	$4,149.16	$0.58	-$1,822.69	$5,971.27	$457.09

Monte Carlo Simulation Assumptions

	Base	Stdev	Min	Max	Distribution
Revenue Variation	0	10%	N/A	N/A	Normal
Op. Costs Variation	0	10%	N/A	N/A	Normal
Market Risk Premium	6%	N/A	5%	7%	Triangular
Long term Growth	3%	N/A	3%	27%	Triangular
Terminal Value	0	0.1	N/A	N/A	Normal

Monte Carlo Simulation Results

	Intrinsic Value	1y-Target
Mean est.	$272.15	$292.50
σ(ε)	$0.32	$0.25
3 σ(ε) adjusted price	$271.19	$291.75
Current Price	$309.70	
Analysts' median est.		$300.75

Stepan Company (SCL: NYSE)

Financial analysis by: Guillaume Valentin

<u>Company profile as of 02/14/2015</u>

Market price: $41.21

Industry: Chemicals

Market Cap: $875.45 million

52-week: $36.34 - $66.51

Beta: 0.19

Source	Traget price	Recommendation
Bloomberg	$55.00	BUY
Capital IQ	$55.00	BUY
Siena	$67.58	BUY
Yahoo Finance	$55.00	BUY

<u>Thesis:</u>

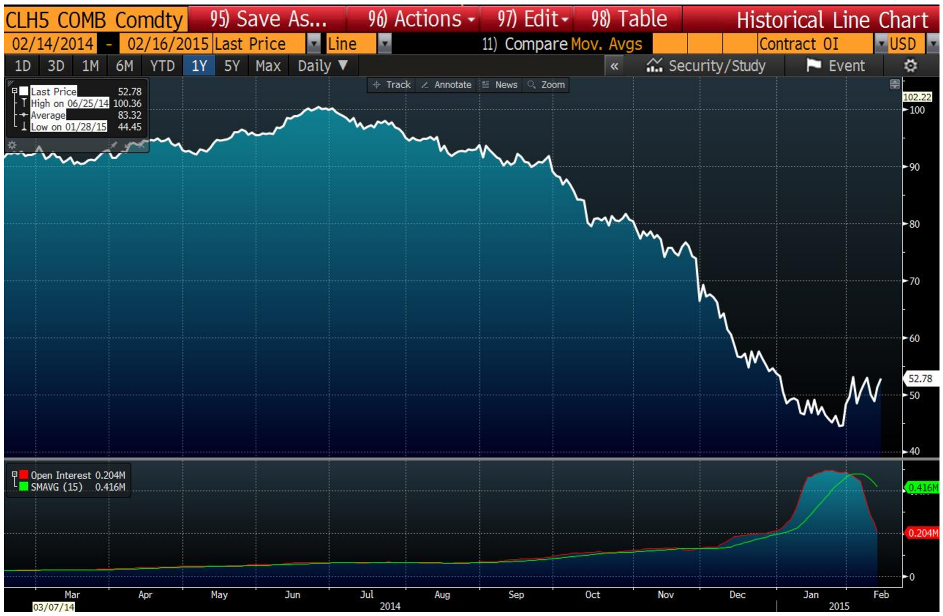
- Leader in the Enhanced Oil Recovery (EOR) technology
- Commitment to innovation
- Growth and global expansion in Surfactants and Polymers segments
- Sustainable advantage
- Healthy Balance Sheet

<u>Company overview:</u>

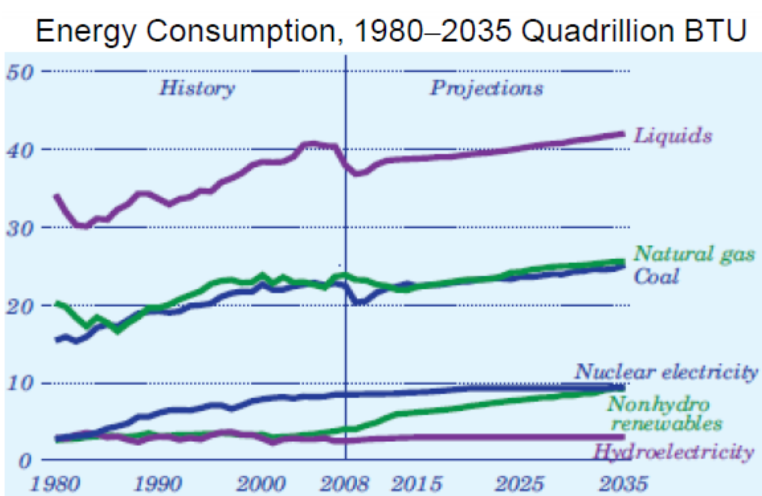
Stepan Company produces and sells specialty and intermediate chemicals to manufacturers in various industries worldwide. The company is divided in three business segments: surfactants, polymers and specialty products. A surfactant is a surface active agent that changes a liquid's surface tension. They are the basic cleaning agent in consumer and industrial cleaning products such as detergents and shampoos and body washes. The polymer product group includes products that are used for thermal insulation in the construction industry and polyester resins that are used in coatings, adhesives and sealants. Stepan also produces specialty products that include flavors and emulsifiers used in the food and pharmaceutical industry. Sales in this segment account for 4% of the total sales of the company. Although Stepan Company is classified with other specialty chemical companies within the material sector, it is unique in the industry and "does not have a competitor or competitors to precisely match its businesses because its products have a specific focus."[4]

Leader in the Enhanced Oil Recovery (EOR) technology:

Enhanced Oil Recovery (EOR) is the implementation of various techniques for increasing the amount of crude oil that can be extracted from an oilfield. The sales in EOR delivered a $5 million increase in operating income improvement in 2014. In September 2008, Stepan and Nalco announced a Joint Venture. In 2008 Nalco bought Tiorco, the global leader in enhanced oil recovery solutions. Since 2008 their technology helped to produce more than 100 million barrels of incremental oil in North American reservoirs alone. Nalco's goal is also to improve recovery in reservoirs throughout the world. To keep up with constant uprising demand in oil, oil producers faces the challenge of producing more oil from their own reservoirs.



The chart above show the crude oil prices from March 2014 to February 2015. Due to a recent huge decrease in oil prices, oil producers tend to have significantly lower margin and are making less profit. This will become a major issue in the foreseeable future. Above is the chart of crude oil prices from March 2014 to present. The oil price dropped 47.48 percent over the past 7 months. If oil priced stays at current levels, oil producers will need to produce more oil in order to remain profitable. Either they manage to increase the output of current reservoirs or they try to find new reservoirs.



In the same time, demand for natural gas and oil continues to grow despite alternate energy sources as states in the graph above.[5] In this sense, the majority of oil companies are focusing on maximizing the recovery factor (RF) from their existing oilfields because it is rather uncommon and hard to find new reservoirs. This is where Stepan comes into play. Oil producer will be more and more interested in their technology since it will be critical for the future of their business. Currently, there are four types of oil extraction methods: Primary production typically recovers about 15% of oil originally in place in oilfields.[6] Waterflooding (or secondary recovery) recovers and additional 20% of oil. This technique is already widely used by oil producers .Waterflooding consists of injecting water to

[4] http://phx.corporate-ir.net/phoenix.zhtml?c=118345&p=irol-homeProfile&t=&id=&
[5] http://www.cacd.ca/files/pdf/AGMPresentations/Frank%20Pacholec_Corporate%20Sustainability.pdf
[6] http://www.nalco.com/applications/enhanced-oil-recovery.htm

increase the reservoir pressure to its initial level so that the oil output increases. However, the effectiveness of this technique decreases over time, which leaves about 65% of oil leftover. The Enhanced Oil Recovery technique (tertiary recovery) targets to extract an additional 20% of oil. Currently, about 10% of the U.S. daily oil production comes from tertiary recovery. Considering the substantial incremental of oil produced in each oilfield, this technique is promising to a bright future. Stepan is specialized in this area thanks to the joint venture with Nalco. In order to boost recovery rates, Tiorco acts as an intermediary that gathers all the necessary products and resources to achieve this goal instead of oil companies trying to solve this problem on their own. Over 30 years ago Tiorco was the first company to recognize this issue. Their field of expertise includes reservoirs engineering, field equipment, chemical formulation and project management. They make sure to use the appropriate tools to fit the specificity of each oil producer and oil reservoir. Tiorco provide oil companies a single resource for their EOR needs so that they can take a full advantage of their oilfields. Stepan Company provides specialty chemicals for use in Enhanced Oil Recovery applications. Tiorco has a competitive advantage in industry thanks to its huge amount of knowledge and experience in this field. Enhanced Oil Recovery is expected to deliver between $3 and $5 million of operating income improvement during the next fiscal year. With Stepan Company, a significant percentage of oilfields have the potential to be more productive.

Commitment to innovation:

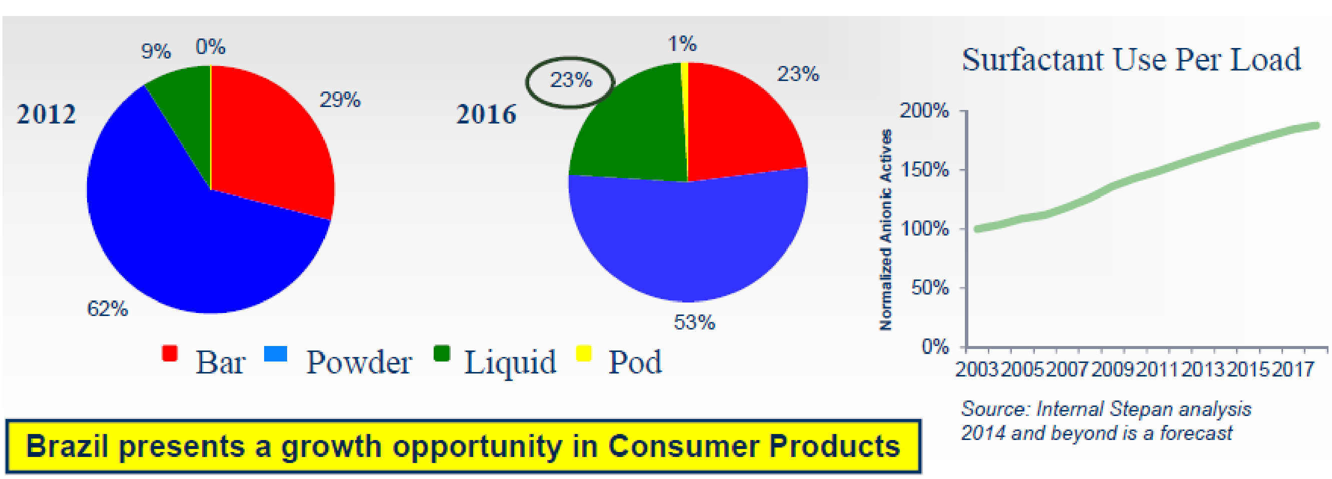
Stephan's innovation initiatives are guided by their Corporate Vision: "Innovative Chemical Solutions for a cleaner, healthier, more energy-efficient world."[7] In June 2013, the Company purchased the North American polyester resins business of Bayer MaterialScience LLC. The purchase included a 21,000-ton production facility in Columbus, Georgia, and a modern research and development laboratory for customer technical support and new product development.[8] This acquisition provides a significant line extension to Stepan's core business. It also increased the operating income of Stepan by $9 million in 2014. Additionally the company exclusively paid this acquisition by cash, which means that it does not believe that tis stock vas cheap and undervalued at that time ($52.25/share, which is higher than the current price). Stepan Company increases its research and development spending each year in order to continuously develop new products and remain competitive in the industry. The company targets to spend at least 2.5% of its revenues in R&D. The company spent $104 million of capital expenditures in 2014. They expect to spend an additional $20 million to $40 million in 2015 with investments in China, Brazil and Poland. The increase will also be attributable to "higher personnel, outside contract service and consulting expenses required to pursue the company's growth and innovation opportunities" Approximately 40% of Stepan's R&D expenses are deployed to support to strategic programs: Novel Feedstocks and Enhanced Oil Recovery (EOR). These two programs will be detailed in the next sections of this report.

Growth and global expansion in Surfactants and Polymers segments:

Stepan Company is divided in three business segments: surfactants, polymers and specialty products. Net sales in surfactants and polymers increased from Q32013 to Q32014. Specialty Products sales volume increased 5% versus prior year due to higher food and flavoring products volume. This segment accounts for about 5% of the company's net income.

Surfactants:

Surfactants are the basic cleaning agent in consumer and industrial cleaning products such as detergents and shampoos and body washes. Surfactants accounts for about 70% of the company's total revenues. Surfactants net sales declined 2% from FY2013 to FY2014. This was attributable to foreign currency translation loss, severe winter and exceptionally higher freights and maintenance costs. However, in the fourth quarter of 2013, the company approved a plan to consolidate a portion of its North American surfactants manufacturing operations in order to reduce future costs and optimize asset utilization. This would increase the short-term profitability of the surfactants division. Stepan Company also continuously develops proprietary processing technology and to meet the rapid changing needs of customers.



[7] http://www.stepan.com/Why-Stepan/Innovation.aspx
[8] http://media.corporate-ir.net/media_files/IROL/11/118345/2013Form10-K.pdf

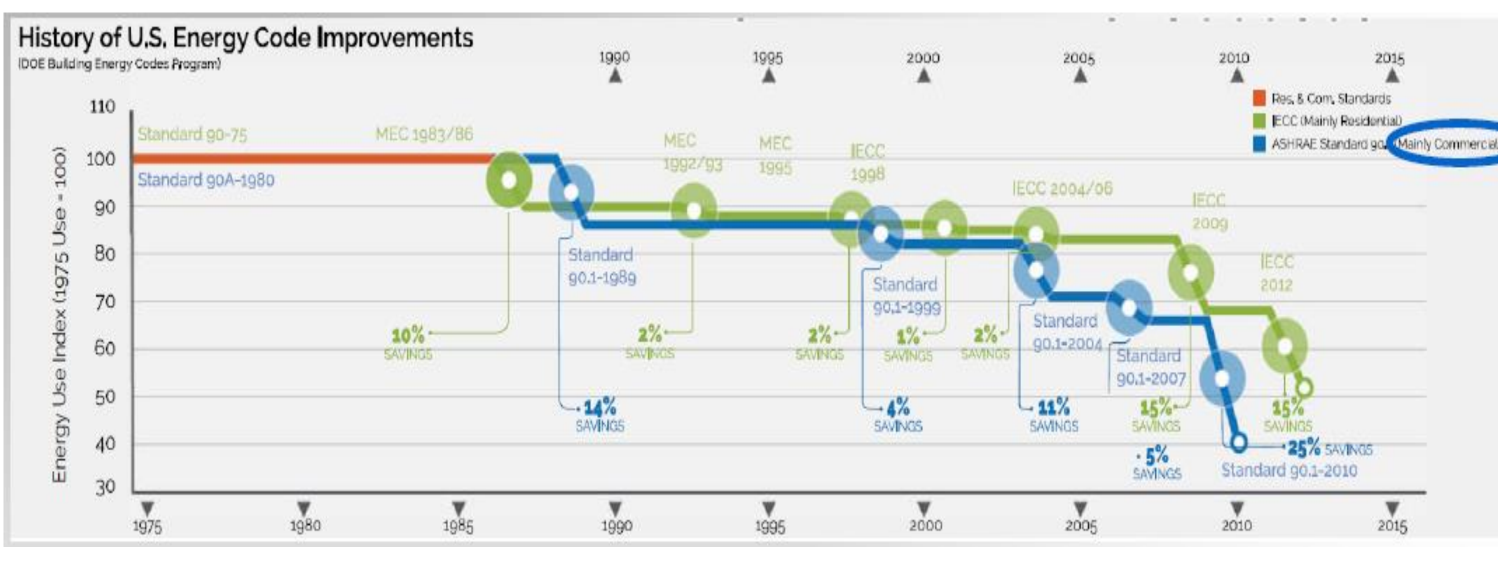
In July 2014, Stepan announced an agreement to acquire a sulfonation production facility in Brazil. This acquisition has recently received anti-trust approval. Brazil, which is the fifth largest country in terms of numbers of inhabitants, has an increasing proportion of middle class people. This would ultimately drive up the usage of liquid laundry products. Liquid laundry products are the ones that that contain the highest proportion of surfactants (compared to powder). As presented on the chart above, by 2016, the market share of liquid laundry products is expected to increase by 12%, which would increase the demand for surfactants. In Brazil, the surfactants use per laundry load is expected to almost double by the end of 2017.

Additionally, Stepan is interested in Brazil because of the opportunity to grow in agriculture. Stepan Company has developed what they call "Novel Feedstock program". The objective of this program is the identification of raw material used in the manufacturing process of chemical products that are produced from non-traditional sources, such as corn and cane. This process is called green conversion process and is illustrated in the picture below. By doing so, Stepan is trying to take advantage of the biotechnology revolution. Stepan has specifically chosen Brazil because it has the moist farmable land in the world and is therefore able to produce far more food than its population needs. The development of these two programs has made Brazil a strategic priority for Stepan in the upcoming year.

Green Conversion Process

Polymers:

The polymer product group includes products that are used for thermal insulation in the construction industry and polyester resins that are used in coatings, adhesives and sealants. Polymers accounts for about 25% of the company's total revenues. Polymers net sales in FY2014 increased 14% over net sales for FY2013 thanks to an 8% increase in organic sales volume, higher average selling price and foreign currency translation gain. This led to a 41% increase in the polymers operating income. The recent acquisition of BMS North American polyester resins accounted for most of the net sales increase in the last fiscal year. It is expected to continue to generate an increase in sales in the future. Because of their broad range of properties, polymers play an essential and role in everyday life. Stepan's comprehensive line of polyester polyols provides for example excellent building insulation. Stepan Company is the global leader in the production and sale of polyester Polyols. The polyester Polyols are frequently used in the construction industry because they have excellent insulation properties. Specifically, Polyol volume sales grew 21% versus prior year as higher energy efficiency standards are adopted. Stepan has been heavily investing in the Chinese market. The Chinese government is currently mandating greater energy efficiency throughout economy and more use of insulation. Therefore, China is a key to Stepan's recent strategy. In Q4 2013, Stepan announced that it would build a Polyol plant is China. The company announced that it signed an EPC (engineering, procurement and construction) contract in order to build the plant. It is expected to be operational by 2016. The company believes that China will be soon the largest Polyol market in the world.



Similarly, the Polyol market in housing insulation is also growing in the United States. The graph above represents the "Energy Use Index (EUI)" from 1975 to 2015. The EUI is expressed as energy per square foot per year (with a 100 value basis in 1975 in this case). Each time the index decreased, it means that the U.S. government has required establishment of new minimum design and construction requirements for energy efficiency. Stepan's unique chemistry leads to the development of superior insulating and fire resistant materials, which are critical requirements in the construction industry, especially in the near future.

In order for Stepan Company to pursue its growth ambition, it has several manufacturing plants all around the world that are able to respond to local and global increase in demand. So that it can meet its global growth expectations, Stepan has a surfactant manufacturing plant in Brazil and a Polyol manufacturing plant in China. This quote, by the CEO of Stepan Company summarizes the future expectations of the company: "There are many projects underway which we expect will reduce our costs and aggressively build our sales. We look forward to improving Surfactant volumes and product mix and continuing to build on the momentum within our Polymer group."[9] To reach this goal, Stepan is currently restructuring some part of its business. The company has agreed in January 2015 to sell its specialty Polyurethane systems business.[10] This aimed to "redeploy resources to further improve growth and innovation in their line of polyols".

Sustainable advantage:
Stepan Company, a member of Responsible Care, is committed to reduce its environmental footprint. Responsible Care is a voluntary initiative developed autonomously by the chemical industry that sets standards for the improvement of health, safety and environmental performance. In 2010, Stepan has agreed on a joint venture with Elevance Renewable Sciences, Inc., the world's leader in transforming natural and renewable oils into high-performing specialty products and materials. Thanks to this partnership Stepan Company has launched in March 2014 a new surfactant called Steposol MET-10U. This product is a cleaning solution derived from natural oils and targets to replace solvents. This product is one of the first commercial products in the market that combines high performance, competitive price and green attributes.[11] The solvent industry is a $45 billion market, which means that chemicals companies have to invest in the "green business" in order to appeal to customers and differentiate themselves from each other's. Therefore, developing innovative products that meet environmental requirements and are still highly effective and affordable for customers gives a great competitive advantage to Stepan Company over its competitors. The company targets to be using 100% certified palm kernel oil and derivatives by 2020. This product is highly suitable for the manufacturing of cleaning agents for laundry purposes. Moreover, not only are the products of the company sustainable. Indeed, in 2013 the company managed to reduce its waste to below 4.1 pounds per 1,000 pounds produced, with a long-term target to 3.0 pounds. Reducing the environment footprint is a core value of the company. Even Stepan's Illinois warehouse was designed utilizing the latest industrial building efficiency systems. It includes a roof insulation containing a similar Stepan polyol that it sold to its customers because the company is a totally confident about the quality and the efficiency of its own products. Sustainability at Stepan Company is noteworthy because most of the chemicals companies tend to have a bad reputation concerning environmental conservation.

[9] http://www.prnewswire.com/news-releases/stepan-reports-third-quarter-results-and-announces-forty-seventh-consecutive-year-of-dividend-increases-190584525.html
[10] http://www.conferencecalltranscripts.org/summary/?id=1394894
[11] http://www.biofuelsdigest.com/bdigest/2014/03/24/the-birth-of-an-affordable-sustainable-more-powerful-gunk-getter/

Healthy Balance Sheet:

The last point of my argument is that Stepan Company has a healthy balance sheet. The company has a 29.8% debt to equity ratio. This ratio has been rather steady over the past few years. I acknowledge that the company is not debt free, but it has plenty of cash on hand. As of December 31, 2013, the company had $133 million in cash. This represented 15% of its market capitalization, which is very high. It could have been able to repay a large portion of its outstanding debt, but by not doing so the company targets the optimal capital structure that offers the ideal debt to equity ratio in order to minimize is WACC. The company has a 7.90% WACC, which is rather low and therefore confirms this theory. The low WACC discounts less the free cash flows, which leads to higher net present values of new projects. All of this leads to a 4.16 Altman Z score. Stepan manages efficiently manages its levels of debt. As it did in the past, Stepan Company can use its cash on hand for horizontal acquisitions purposes, which would reinforce the competitive advantage it has over its competitors.

Best/worst case scenario:

Regarding Stepan Company's stock price, there a three outcomes that can occur:

I am being conservative if the company is unable to pursue its growth operations in the case the Brazilian and Chinese markets turned out to be less promising than expected. Also, the company's net income could be negatively impacted by further foreign currency translation loss or higher freights and maintenance costs. In this case the stock price could decrease to the $38-$41 levels. I evaluate to probability of this scenario to be 15%.

I am being neutral if the company does not maintain a real competitive advantage over its competitors. This would mean that Stepan still invest in Research and Development but does not produce a products that stands out from the others. In this case the stock price would remain in the $41-$44 levels. I evaluate to probability of this scenario to be 25%

I am being bullish if the company successfully performs its international expansion and maintains a strategic competitive advantage over its competitors. If customers keep an interest in the technology of Stepan Company and the sustainability in their products, the company will remain a leader in this industry. In this case the stock price would increase to the $67.58 1-year target price computed by the prroforma on presented on the next page. I evaluate to probability of this scenario to be 60%.

2015 expectations:

	Potential Improvements		Potential Headwinds	
	Net Income	EPS *	Net Income	EPS *
Surf Vol/Mix Items			($6MM) **	($0.25)
Non-Recurring Maintenance and Shutdown costs	+$6MM	+$0.25		
Overall Efficiency Program	+$8MM	+$0.30		
Savings on 2013 Restructuring	+$2MM	+$0.10		
Savings on 2014 Restructuring	+$1MM	+$0.05		
Sale of Polyurethane Systems Business	+$2MM	+$0.10		
Weather	+$2MM	+$0.10		
Special Bad Debt Charges	+$2MM	+$0.10		

Additional $17 million or $0.75 EPS prior to growth and other initiatives

The table above, taken from the Q42014 earnings presentation of the company, summarizes the expectation Stepan has for 2015. The company is expected to increases its total net income by $17 million compared to 2014 thanks to several efficiently and restructuring improvements. Most of this gain in only the result of overall business improvements that should lead to an increase in net income. Concerning the Surfactants Volume decrease, these are known items that will occur in the first two quarters of 2015 (no sales in the biodiesel segments yet and expected lower commodity consumer product sales in North America in Q12015 and Q2015.). Finally, the income growth in the polymers segment and the functional surfactants volumes should both increase in 2015. The company is also expected to benefit from falling raw material prices. Therefore, with these expectations and the thesis points I presented, I initiate a buy recommendation on Stepan Company at a current stock price of $41.21. The company's stock price is near its 52-week low, which makes a good point of entry for a buy opportunity.

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Stepan Company	SCL	Analyst	Current Price	Intrinsic Value	Target Value	Divident Yield	Target Return	BULLISH
		GUILLAUME VALENTIN	$41.23	$60.11	$67.58	2%	65.64%	

General Info

Sector	Materials
Industry	Chemicals
Last Guidance	Apr-29-2014
Next earnings date	2/18/2015

Market Data

Enterprise value	$1,095.21
Market Capitalization	$222.94
Daily volume	0.18
Shares outstanding	22.25
Diluted shares outstanding	22.93
% shares held by institutions	46.52%
% shares held by insiders	13.69%
Short interest	0.94%
Days to cover short interest	2.35
52 week high	$66.51
52-week low	$36.34
5y Beta	0.93
6-month volatility	24.98%

Peers	Market Cap.
	(Invalid Identifier)

Current Capital Structure

Total debt/market cap	24.21%
Cost of Borrowing	4.33%
Interest Coverage	838.10%
Altman Z	4.16
Debt Rating	BB
Levered Beta	1.21
WACC (based on market value weights)	7.90%

Management

Professional	Title	Comp. FY2011	Comp. FY2012	Comp. FY2013
Stepan, F.	Chief Executive Officer, Presiden	$ -	$ -	$ -
Beamer, Scott	Chief Financial Officer, Principal	$ -	$ -	$ -
Mason, Scott	Vice President of Supply Chain	$ -	$ -	$ -
Venegoni, John	Consultant	$ -	$ -	$ -
Servatius, Gregory	Vice President of Human Resou	$ -	$ -	$ -
Eaken, Matthew	Vice President and Corporate Co	$ -	$ -	$ -

Historical Performance

	SCL	Peers	Industry	All U.S. firms
Growth	11.0%		7.2%	6.0%
Retention Ratio	32.9%		49.0%	61.6%
ROIC	36.6%		25.1%	11.8%
EBITA Margin	4.6%	#DIV/0!	12.0%	13.7%
Revenues/Invested capital	241.2%		167.2%	202.3%
Excess Cash/Revenue	4.3%	#DIV/0!	12.8%	18.5%
Unlevered Beta	1.01		1.12	0.95
TEV/REV	0.5x		1.5x	2.4x
TEV/EBITDA	6.2x		9.5x	11.3x
TEV/EBITA	12.0x		13.0x	15.4x
TEV/UFCF	9.2x		28.0x	26.8x

Past Earning Surprises

	Revenue	EBITDA	Norm. EPS
Last Quarter	-0.5%	0.0%	-24.4%
Last Quarter-1	0.8%	0.0%	2.3%
Last Quarter -2	-1.7%	0.0%	-34.9%
Last Quarter -3	2.4%	0.0%	-30.3%
Last Quarter -4	2.0%	0.0%	0.0%

Non GAAP Adjustments

Operating Leases Capitalization	100%	Straightline	10 years
R&D Exp. Capitalization	100%	Straightline	10 years
Expl./Drilling Exp. Capitalization	0%	N/A	N/A
SG&A Capitalization	0%	N/A	N/A

Proforma Assumptions

		Period	Rev. Growth	Adj. Op. Cost/Rev
Operating. Cash/Cash	25.0%	LTM	24%	90%
Unlevered Beta	1.00	LTM+1Y	29%	89%
Rev/Invested Capital	150.0%	LTM+2Y	3%	89%
Continuing Period Revenue Growth	3.0%	LTM+3Y	3%	89%
Long Term ROIC	17.3%	LTM+4Y	3%	89%
Invested Capital Growth	Equals to Maintenance	LTM+5Y	3%	89%
Justified TEV/REV	1.0x	LTM+6Y	3%	89%
Justified TEV/EBITDA	7.0x	LTM+7Y	3%	89%
Justified TEV/EBITA	13.0x	LTM+8Y	3%	89%
Justified TEV/UFCF	20.0x	LTM+9Y	3%	89%

Forecasted Profitability

Revenue	NOPLAT	Invested capital	UFCF
$1,947.31	$51.31	$1,031.61	$2.42
$2,512.33	$104.05	$1,088.79	$62.14
$2,592.58	$113.71	$1,127.11	$75.38
$2,668.12	$120.38	$1,169.42	$78.08
$2,749.22	$126.13	$1,213.70	$81.85
$2,834.15	$131.22	$1,269.07	$75.86
$2,920.95	$136.27	$1,319.96	$85.38
$3,009.83	$141.38	$1,368.52	$92.82
$3,100.95	$146.64	$1,417.69	$97.46
$3,194.42	$151.89	$1,474.15	$95.43

Valuation

	ROIC	WACC	EVA	Enterprise Value	Total Debt	Other claims	Equity	Adjusted Price
LTM	5.2%	7.9%	$1.36	$1,549.62	$265.16	-$8.52	$1,292.98	$61.07
LTM+1Y	9.8%	8.1%	$18.27	$1,654.45	$265.16	-$76.12	$1,465.41	$68.33
LTM+2Y	10.4%	8.2%	$24.80	$1,720.46	$265.16	-$143.37	$1,598.66	$73.99
LTM+3Y	10.7%	8.3%	$27.21	$1,778.72	$265.16	-$210.91	$1,724.47	$79.75
LTM+4Y	10.8%	8.4%	$28.29	$1,840.53	$265.16	-$280.87	$1,856.23	$85.65
LTM+5Y	10.8%	8.5%	$28.55	$1,907.56	$265.16	-$344.45	$1,986.85	$92.08
LTM+6Y	10.7%	8.6%	$27.39	$1,983.75	$265.16	-$417.16	$2,135.75	$98.64
LTM+7Y	10.7%	8.7%	$26.57	$2,060.37	$265.16	-$497.16	$2,292.37	$105.76
LTM+8Y	10.7%	8.8%	$26.17	$2,137.21	$265.16	-$581.80	$2,453.86	$113.03
LTM+9Y	10.7%	8.9%	$25.73	$2,216.51	$265.16	-$664.95	$2,616.30	$117.59

Monte Carlo Simulation Assumptions

	Base	Stdev	Min	Max	Distribution
Revenue Variation	0	10%	N/A	N/A	Normal
Op. Costs Variation	0	10%	N/A	N/A	Normal
Market Risk Premium	6%	N/A	5%	7%	Triangular
Long term Growth	3%	N/A	3%	11%	Triangular
Terminal Value	0	0.1	N/A	N/A	Normal

Monte Carlo Simulation Results

	Intrinsic Value	1y-Target
Mean est.	$61.07	$68.33
σ(ε)	$0.32	$0.25
3 σ(ε) adjusted price	$60.11	$67.58
Current Price	$41.23	
Analysts' median est.		$55.00

Vascular Solutions Inc (VASC: NASDAQ)

Financial Analysis By: Laura Pladys – Healthcare

Company Profile as of 2/18/2015

Market Price: $28.82
Industry: Interventional Cardiology
Market Cap: $495.73M
52-Week: $18.42-30.97
Beta: 0.68

Source	Target Price	Recommendation
Siena	$32.70	BUY
Bloomberg	$32.88	BUY
Capital IQ	$32.88	BUY
Yahoo Finance	$32.88	BUY

Thesis

-International Expansion Opportunity
-Unique Products Development Opportunities
-Promising Financials

Vascular Solutions Inc is a buy because of the factors mentioned above. The company is focused on improving its international sales through distributors and its domestic sales through direct sales. The company has entered a unique partnership with the US Army Combat Casualty Care without having to invest in research and development. They are both working on developing the state and carriage of plasma to heel wounded soldiers on the field. Moreover, the company had an aggressive start in 2015 in its product development in its top selling line of products: catheters. The company's financials are better year over year and the company shows sign of undervaluation compared to its peers in the interventional cardiology industry.

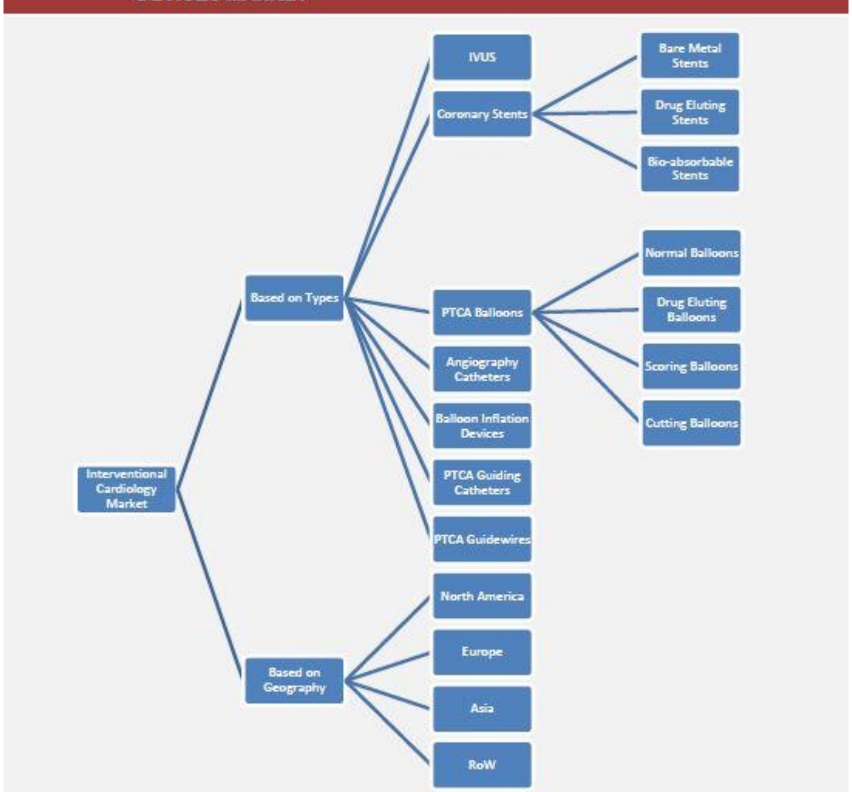
Company Overview

Vascular Solutions, Inc., a medical device company, provides various solutions to interventional cardiologists, interventional radiologists, electro physiologists, and vein practices worldwide. The company's catheter products include GuideLiner catheters for use in various interventions; Pronto extraction catheters for treating acute myocardial infarction; Micro-Introducers for performing arterial and venous catheterization procedures; Langston to measure intravascular pressure gradients for the diagnosis of aortic valve stenosis; and SmartNeedle, a doppler-guided needle device designed to provide auditory ultrasound-guided access to arteries and veins. It also offers Venture, a deflectable tip catheter used for steering guidewires in various interventions; Guardian, a hemostat valve to allow placement of multiple devices simultaneously; SuperCross, a catheter for support and delivery of guidewires during coronary and peripheral interventions; Snares to retrieve or manipulate devices in catheterization procedures; and Minnie, a support catheter used to facilitate placement and exchange of guidewires and other interventional devices. In addition, the company provides hemostat products comprising D-Stat Dry Thrombix, a thrombin-based hemostat bandage used in conjunction with manual compression to control bleeding in catheterizations; D-Stat Flowable, a flowable mixture to control bleeding in the pectoral pockets; Vasc Band, a compression device that utilizes an inflatable membrane to control bleeding; D-Stat Radial, a compression device that utilizes a thrombin pad to control bleeding; and accumed wrist positioning splint. Further, it offers vein products and services, such as Vari-Lase endovenous laser, a laser console and procedure kit used for the treatment of varicose veins, as well as a reprocessing service for the ClosureFAST radiofrequency vein ablation catheter. The company was founded in 1996 and is headquartered in Minneapolis, Minnesota.

Management

Howard Root has held the position of Chief Executive Officer and member of the Board of Directors of Vascular Solutions Inc since he co-founded the company in 1997. Prior to that, he worked as Vice President in the same industry for a company building mechanical heart valves. The Chief Financial Officer James Hennen has a background in audit and control and joined Vascular Solutions in 2004. These two have a very competent team. Charmaine Sutton serves as Senior Vice President of Operations since 2010 and has an impressive background in the medical industry as consultant as well as expert in the medical regulatory environment. Early 2015, the company expanded its US sales management and formed four new American territories for its sales. As a result, three of the regional directors were promoted up. Vascular Solutions Inc prefers to promote existing employees rather than hire external people. The team got bigger with the additional sales region representatives and none of the existing VASC employees left. The CEO believes that promoting existing employees leads to a long-term growth: Vascular Solutions Inc's goal.

FIG. 1 MARKET SEGMENTATION FOR THE INTERVENTIONAL CARDIOLOGY DEVICES MARKET



Interventional Cardiology Devices Overview

Interventional cardiology refers to treatment based on catheters to treat structural heart diseases. Cardiovascular diseases are expected to cause more than 25 million deaths worldwide by 2031. The interventional cardiology industry is much diversified with several segments based on types as well as on geography (see graph on the left for details). The primary factors driving the industry are increasing rates of cardiovascular diseases, the increasing demand of minimally invasive procedures available thanks to new technology, an increased number of interventional cardiologists as well as an aging population. The North American market holds the majority of the industry market share because of higher disposable income than emerging markets but this trend is expected to be reversed in less than a decade. International sales are expected to increase faster than domestic sales and disposable income is increasing in emerging regions, especially in Asia.

Cardiovascular diseases are the first cause of death worldwide and are forecasted to increase because of people's lifestyle: global number of smokers, increasing rates of obesity and dietary irregularities. Patients' rising awareness is expected to increase demand for interventional cardiology devices. Previously valued at $14.9B in 2013, the industry is expected to grow at a CAGR of 7.7% until 2020. In addition, the constant increase in congenital heart disease is a primary factor of this growth. Currently, congenital heart diseases are responsible for 1% of American birth defects per year. The increasing technology helps to boost the growth of the industry with new advanced devices, new products, and existing products enhancement. For the past five years, the industry has been transformed thanks to new techniques and new procedures, forecasted to keep improving. Surgery that would have been considered impossible a decade ago are now performed with a rate of success of 90%. Minimally invasive procedures require less post-surgery complications, pain, and side-effects. Patients' recovery period is also shorter.

Competition

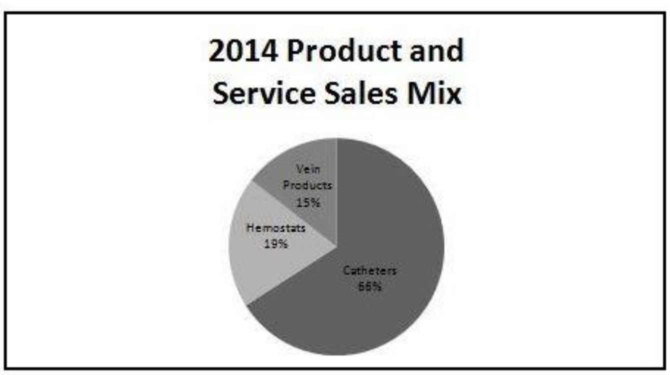
The healthcare sector, especially the interventional cardiology industry, is very competitive; therefore barriers to entry are high. With a market being oligopolistic, any advancement in the industry will impact every company positively or negatively. Despite the nature of the market, companies still succeed at being specialized in a dominant product segment. VASC main competition arises from the following players with several businesses lines as well as small manufacturers with a limited selection of products. VASC biggest competitors include:

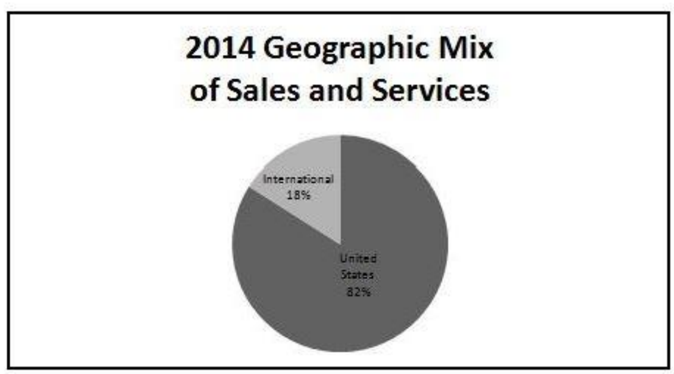
- Medtronic PLC
- Boston Scientific Corporation
- Merit Medical Systems Inc
- Angio Dynamics
- Terumo Corporation

Most of VASC competitors outperform the company in the financial, technological, research and development, marketing, and sales aspects. These companies may also have a greater experience and may have been in business longer than VASC, but the company differentiates itself with its diversified pipeline and focused opportunities in the interventional cardiology industry.

Products Proposed

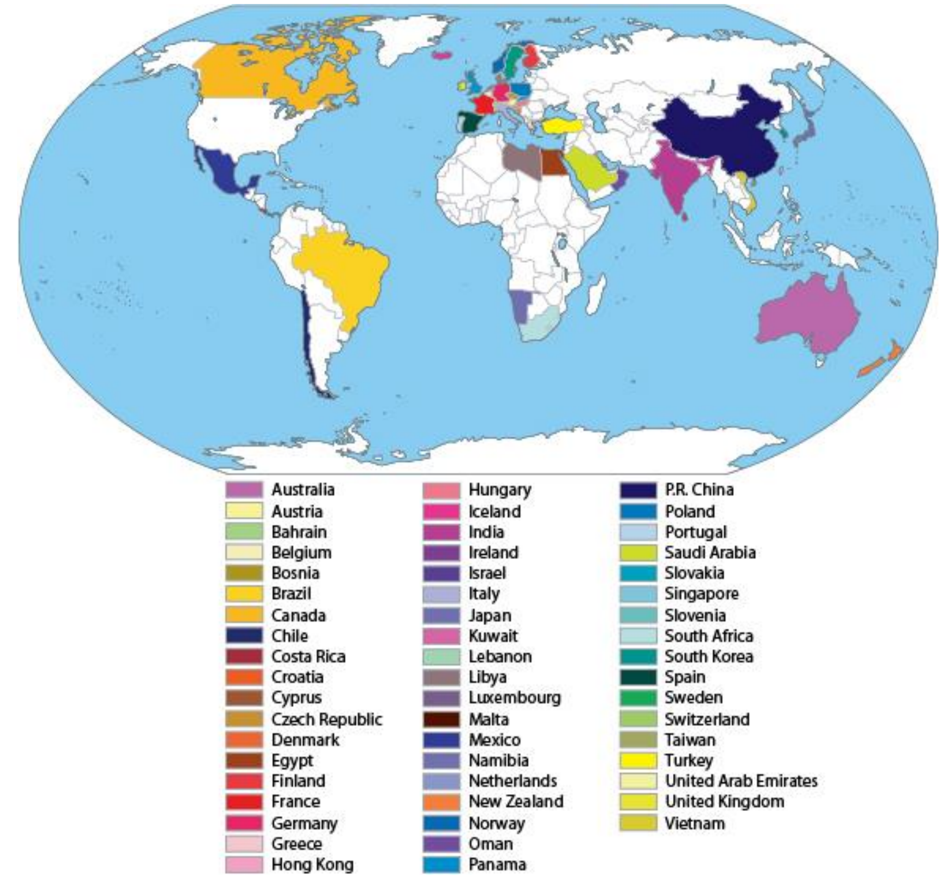
Vascular Solutions Inc started as a single product company in 2000 and now the company's pipeline gathers more than 80 products organized within three different categories: catheter products, hemostat products and vein products. In 2014, catheters products represented 66% of VAS's pipeline (see chart below). The catheters that VASC proposes primarily deal with minimally invasive procedures for diagnostics as well as the treatment of vascular conditions. The hemostat products are blood clotting products as well as radial artery procedures. The vein products and services deal with the treatment of varicose veins and other services related to a vein ablation catheter. VASC geographic mix is represented by 82% of sales directly from the company and 18% of it executed by distributors internationally.





The company believes that the top seller category in 2015 would be their radial products. The radial sheaths represent a market of $50 million and is forecasted to grow substantially. The company expects radial revenues to increase by 30% especially in the second half of 2015. Even though the company is in its early strategy in the radial market, it already anticipates launching several products in the market to drive their hemostat sales forward.

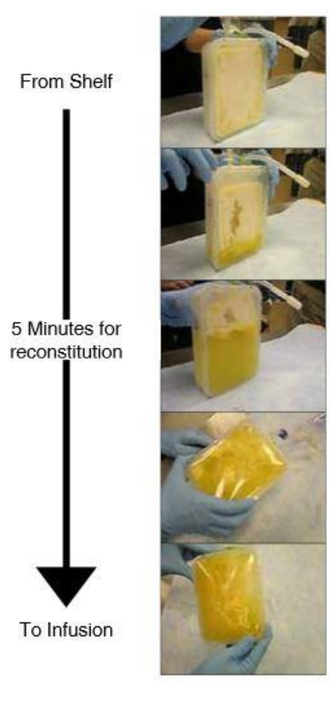
International Expansion



VASC started in 2000 with a single product, Duett sealing device, marketed and sold in the United States by its direct sales organization. As of December 31, 2014, Vascular Solutions Inc partners with 44 independent distributors covering 56 countries (see chart on the left for a detailed list of the countries covered). As stated above, international sales represented 18% of VASC's total sales for 2014. From 2013 to 2014, US sales grew at a rate of 8% while international sales grew at a much faster pace of 59%. VASC executes deals with its international distributors in US dollars except with its Irish subsidiary and its German distributor trading in Euro. With the dollar strongly appreciating against other foreign currencies and its euro transactions representing less than 2%, VASC does not have an important risk exposure on the currency. The company does not have any hedging strategy in place and does not feel like it is required at this point. Though VASC plans on keeping increasing its sales internationally, it does not plan to pursue a direct sales model as it is currently doing in the US. Whether it is short, medium, or long-term, the company refuses to follow direct sales as it would require too much management, currency, and financial risks. On the other hand, the substantial growth driver in the last quarter of 2014 was the company's international sales. It is expected to be the main driver of growth for the year 2015 as well. International sales are forecasted to grow at a faster pace than US sales. International sales carry a lower gross margin but carry as well lower selling expenses.

Product Development Opportunities

In January 2015, VASC launched a new 5 French version of its Pronto LP catheter, the only extraction catheter proposing a 5 French compatibility on the market yet. French version refers to the size of catheters. 5 French versions would represent catheters with a 1.7mm diameter. This new catheter would improve surgeons' rate of success while performing radial artery intervention. This catheter is implemented to complement VASC Pronto V4 Extraction Catheter in order to be even more precise and accurate while removing soft thrombus from arteries.



The company is committed to develop its internal new pipeline since as of December 31, 2014, Vascular Solutions Inc had 40 new medical device projects in various stages of development. One of the most important projects the company has started is the collaboration with the United States Army. This collaboration should result in "freeze-dried plasma for the battlefield management of severe hemorrhage". Plasma is the liquid blood component containing all of the proteins and clotting factors that represent a normal blood flow: hemostasis, the first step in wound healing. An abnormal or deficient blood clotting results in coagulopathy as a consequence of wounding. The replacement of these clotting factors is necessary for a successful healing. The Army currently uses fresh frozen plasma (FFP) but 40% of the FFP sent onto the battlefield breaks before arrival. This represents a consequent waste of plasma, especially for rare plasma like AB type that is only available within 4% of US donors. Since the plasma is currently fresh-frozen, it has to be kept frozen during transfers and weights a lot. Therefore, VASC is currently working on freeze-dried plasma (FDP) that would not require to be shipped on ice and would have a ruggedized container. This would reduce the risk of breakage and waste while saving on power requirement on battlefield. It could also save lives as it should be ready earlier for use in case of severe hemorrhage (see picture on the left). This FDP has been ranked a top priority project by the US Army Combat Casualty Care. FDP has been put out of the market in the 1960's and no company was willing to undertake the R&D expenses and technical challenges until 2014. VASC has been chosen thanks to its expertise in lyophilization of biologic agents and their financial capabilities to undertake the project. By September 2015, an Investigational New Drug (IND) application should be submitted to the Food and Drug Administration (FDA).

In addition, the company announced at its Q4 2014 earnings that 2015 is "off to our best start ever". The company goal was to launch 10 new products per year. On February 3, 2015, the company had already 6 new products in the launch process. Out of these six products, 5 are catheters instruments with Turnpike being another great growing opportunity. Turnpike products are catheters designed to be used in coronary and peripheral interventions. It is the extension of the company's GuideLiner, a "unique coaxial 'mother and child' guide extension that enables deep seating and selective intubation in challenging coronary interventions". GuideLiner has been the stand-out performer in the last quarter of 2014 with quarter sales up by 71%. This increase included 35% growth in the US alone and 172% growth internationally thanks to the adoption of the product in Japan and the consistent adoption by physicians of the products. The turnpike represents a \$20 to \$30 million annual opportunity and is expected to significantly contribute to the 2015 sales growth. It is expected to be launched by the end of the first quarter of 2015. On top of these six products, nine additional products from the company's internal R&D pipeline are expected to be launched by the end of 2015. R&D investment has represented 11 to 12% of net sales in the past three years and is expected to remain at 12% in 2015.

Financials

On February 3rd, 2015, Vascular Solutions Inc held its Q4 2014 earning call. In 2014, the company sustained its double-digit revenue growth for the 11th consecutive year. Revenue increased 14% to reach \$126.1 million. The increase is primarily explained by the 19% increase in catheter products sales, now representing 66% of the company's total sales. The company EV/EBITDA TTM of 18.5 times is 2.6 times lower than the industry average. The company's operating income has been stable for five years around 15% of revenue, showing signs of sustainability. VASC's gross margins has stayed in-between the 66% range since 2006 but is expected to increase primarily due to the agreement signed with the US Army. The US Army is undertaking R&D costs, which should increase VASC revenue without increasing its costs. Their EBITDA growth of 20.93% from 2013 to 2014 is higher than their revenue growth of 14.12%. The pattern has been reversed as in 2013 revenue grew 7% faster than EBITDA, meaning that the company is now creating value. Their \$11.78 million free cash flow for 2014 decreased mainly due to a purchase of PP&E of \$7.1 million from their cash to acquire the company's principal manufacturing facility. The cash as of December 31, 2014 represented 46% of the firm's total assets and the cash ratio was at 2.80. The majority of the cash is kept in their operating accounts. A portion of the company's cash is invested in a money market fund. Most of their investment is short-term money market instruments in US dollars and the company picks them in the highest short term category defined by the S&P or Moody's. The cash provided by their operating activities is driven by the result of their net earnings. 56% of the company's cash in investing activities was used in the purchase of the new manufacturing facility. The cash generated from their investing activities is due to tax benefits from stock based awards and the Employee Stock Repurchase Plan, supposed to expire in 2020. Most importantly, the company expects to keep on having positive free cash flows in the future. Concerning research and development, the company invested 11% of its revenue in order to maintain their new product momentum. The dollar amount increased but the percentage amount declined because of new hiring. The company expects to pursue investing on research and development in order to reach its long term development project goal. In 2008, the company got rid of its short and long term debt and managed to stay debt free until now. VASC's P/E of 33.68 times is significantly lower than the peers' average of 42.75 times. The forward P/E is expected to be 32.20 times, even lower than the peers' average of 47.49 times. The 2 year forward is also expected to decrease to 26.73 times while the peers' average is almost doubling. The bigger decrease in the 2 year expected P/E may be representative of the freeze-dried plasma expected launch in 2016, proving signs of Vascular Solutions Inc capacity to grow and create value. Overall, in the operating segment, Vascular Solutions Inc has outperformed its direct competitors in the past year (see chart below).

13) Op Stats (RV)	Co	Range
Sales Growth Yoy (%)	14.12	-3.68
EBITDA Margin (%)	19.69	-10.77
Gross Margin (%)	66.93	43.28

Most of the company's general and administrative expenses significantly increased as a dollar volume but not as a percentage of sales. The dollar increased is due to legal expenses that the company had last year. The company is currently suing two of its direct competitors, Boston Scientific and Terumo Corporation, for patent infringement. The company's net income of \$1.7 million for the year 2014 was slightly below their expectations of \$2 million because of the Short-Kit litigation. The company had unexpected legal fees because of this lawsuit and expects to have SG&A 3 to 4% higher than the current year in 2015. On November 13, 2014, the CEO Howard Root and Vascular Solutions Inc have been accused of "felony count of conspiracy and eight misdemeanor charges of selling unapproved and adulterated medical devices". This accusation sounds worse than what it actually is. What seems to have happened is that the company marketed a product beyond the approval that the FDA had granted them. The trial is supposed to be held in 2016, with small to no impact on the company next year.

Conclusion

Vascular Solutions Inc is a buy at a price below $27 a share. The company has a bright future ahead. Thanks to its presence in the international market and its expectations of expansion, its products development, and its financials showing signs of undervaluation, VASC is a BUY. The company's current litigation on its Short-Kit should not impact the company's performance in 2015. With its impressive start in 2015 with the launch of 6 new products in only a month and a unique partnership with the US Army Combat Casualty Care, VASC's revenues are expected to significantly improve. Sales internationally are expected to grow faster than domestic sales, representing a real opportunity for the company with recently long-term relationships with its Japanese distributors. Domestically, the company can rely on stable distribution capability. Overall, the company outperformed the industry average in 2014 and currently shows signs of improvement in the near future.

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Vascular Solutions Inc.	VASC	Analyst	Current Price	Intrinsic Value	Target Value	Divident Yield	Target Return	NEUTRAL
		Laura Pladys	$28.82	$29.12	$32.70	0%	0	

General Info	
Sector	Healthcare
Industry	Healthcare Equipment and Supplies
Last Guidance	Feb-03-2015
Next earnings date	NM

Peers	Market Cap.
AtriCure, Inc.	$505.74
ATRION Corp.	$639.73
STAAR Surgical Company	$262.85
AngioDynamics Inc.	$672.90
Merit Medical Systems, Inc.	$759.12

Management

Professional	Title	Comp. FY2012	Comp. FY2013	Comp. FY2014
Root, Howard	Co-Founder, Chief Executive Of	$ 3,134,847.00	$ 1,134,588.00	$ -
Hennen, James	Chief Financial Officer, Senior Vi	$ 484,743.00	$ 511,402.00	$ -
Sutton, Charmaine	Senior Vice President of Operatic	$ 572,312.00	$ 636,009.00	$ -
Rutstein, William	Senior Vice President of Internat	$ 474,554.00	$ 514,564.00	$ -
Powers, Carrie	Vice President of Marketing	$ 411,755.00	$ 462,317.00	$ -
Slayton, Timothy	Principal Accounting Officer and	$ -	$ -	$ -

Market Data	
Enterprise value	$459.30
Market Capitalization	$495.76
Daily volume	0.41
Shares outstanding	17.20
Diluted shares outstanding	17.71
% shares held by institutions	68.19%
% shares held by insiders	4.40%
Short interest	1.60%
Days to cover short interest	3.19
52 week high	$30.97
52-week low	$18.42
5y Beta	-0.04
6-month volatility	46.57%

Current Capital Structure	
Total debt/market cap	0.00%
Cost of Borrowing	0.00%
Interest Coverage	
Altman Z	20.16
Debt Rating	AAA
Levered Beta	0.96
WACC (based on market value weights)	8.03%

Historical Performance

	VASC	Peers	Industry	All U.S. firms
Growth	22.8%	13.4%	14.0%	6.0%
Retention Ratio	23.6%	218.5%	93.0%	60.2%
ROIC	64.4%	5.2%	13.9%	12.1%
EBITA Margin	12.6%	13.8%	15.5%	13.7%
Revenues/Invested capital	63.4%	71.7%	91.8%	202.3%
Excess Cash/Revenue	15.3%	22.1%	36.3%	18.5%
Unlevered Beta	0.33	1.15	0.95	0.95
TEV/REV	2.4x	2.5x	3.4x	2.4x
TEV/EBITDA	16.7x	18.7x	14.7x	11.3x
TEV/EBITA	18.2x	25.6x	16.3x	15.4x
TEV/UFCF	66.8x		39.9x	26.8x

Past Earning Surprises

	Revenue	EBITDA	Norm. EPS
Last Quarter	-0.1%	0.0%	21.1%
Last Quarter-1	2.8%	5.6%	0.0%
Last Quarter -2	0.8%	17.2%	11.1%
Last Quarter -3	0.0%	0.0%	-11.1%
Last Quarter -4	1.6%	0.0%	15.8%

Non GAAP Adjustments

Operating Leases Capitalization	100%	Straightline	10 years
R&D Exp. Capitalization	100%	Straightline	10 years
Expl./Drilling Exp. Capitalization	0%	N/A	N/A
SG&A Capitalization	20%	Straightline	10 years

Proforma Assumptions / **Forecasted Profitability**

		Period	Rev. Growth	Adj. Op. Cost/Rev	Revenue	NOPLAT	Invested capital	UFCF
Operating. Cash/Cash	0.0%	LTM	14%	61%	$124.66	$20.05	$171.81	$48.12
Unlevered Beta	0.95	LTM+1Y	10%	62%	$137.63	$22.82	$215.90	$6.80
Rev/Invested Capital	63.0%	LTM+2Y	9%	62%	$150.18	$26.14	$229.23	$12.80
Continuing Period Revenue Growth	3.2%	LTM+3Y	5%	62%	$158.06	$27.83	$241.13	$15.94
Long Term ROIC	11.9%	LTM+4Y	5%	62%	$165.22	$29.19	$252.26	$18.06
Invested Capital Growth	Equals to Maintenance	LTM+5Y	4%	62%	$171.98	$30.40	$262.69	$19.98
Justified TEV/REV	3.4x	LTM+6Y	4%	62%	$178.54	$31.50	$274.29	$19.90
Justified TEV/EBITDA	14.7x	LTM+7Y	4%	62%	$185.00	$32.64	$283.71	$23.22
Justified TEV/EBITA	17.0x	LTM+8Y	3%	62%	$191.43	$33.78	$292.63	$24.86
Justified TEV/UFCF	39.9x	LTM+9Y	3%	62%	$197.88	$34.95	$301.20	$26.38

Valuation

	ROIC	WACC	EVA	Enterprise Value	Total Debt	Other claims	Equity	Adjusted Price
LTM	10.0%	8.0%	$3.45	$476.41	$0.00	-$19.10	$495.51	$29.30
LTM+1Y	13.3%	8.1%	$11.14	$531.45	$0.00	-$27.66	$559.10	$32.91
LTM+2Y	12.1%	8.2%	$8.91	$558.26	$0.00	-$41.10	$599.36	$35.19
LTM+3Y	12.1%	8.3%	$9.21	$587.47	$0.00	-$56.95	$644.42	$37.82
LTM+4Y	12.1%	8.4%	$9.29	$617.27	$0.00	-$74.16	$691.43	$40.57
LTM+5Y	12.1%	8.5%	$9.28	$648.12	$0.00	-$92.54	$740.66	$43.57
LTM+6Y	12.0%	8.6%	$9.25	$682.28	$0.00	-$110.19	$792.47	$46.48
LTM+7Y	11.9%	8.7%	$9.03	$716.51	$0.00	-$130.64	$847.15	$49.68
LTM+8Y	11.9%	8.8%	$9.03	$753.00	$0.00	-$152.30	$905.30	$53.09
LTM+9Y	11.9%	8.9%	$9.11	$791.59	$0.00	-$175.14	$966.73	$56.20

Monte Carlo Simulation Assumptions

	Base	Stdev	Min	Max	Distribution
Revenue Variation	0	10%	N/A	N/A	Normal
Op. Costs Variation	0	10%	N/A	N/A	Normal
Market Risk Premium	6%	N/A	5%	7%	Triangular
Long term Growth	3%	N/A	3%	23%	Triangular
Terminal Value	0	0.1	N/A	N/A	Normal

Monte Carlo Simulation Results

	Intrinsic Value	1y-Target
Mean est.	$29.30	$32.91
σ(ε)	$0.06	$0.07
3 σ(ε) adjusted price	$29.12	$32.70
Current Price	$28.82	
Analysts' median est.		$32.88