

1 PAGE RECOMMENDATION SUMMARY

Screening – In the case of Exco Technologies Limited (XTC.TO), we discovered the following:

P/E Ratio: 10.4, which is less than the benchmark of 13, therefore it passes.

P/B Ratio: 1.4, which is slightly larger than the recommended benchmark of 1.2, therefore it does not pass.

Market cap: CAD \$416 million, which is under the benchmark of CAD \$450 million, therefore it passes.

We decide to investigate further if the stock is potentially undervalued or has growth/franchise value that we would be interested in.

Industry & company analysis – Exco is a global designer, developer and manufacturer of dies, moulds, components and assemblies, and consumable equipment for the die-cast, extrusion and automotive industries. While heavily tied to the cyclical automotive industry, its broad geographic customer and manufacturing base minimizes this risk. The company's target debt structure is 13.1% (including operating leases) but trending upwards. The optimal capital structure is between 30-49%. This puts them in the low financial risk range as their debt levels are quite low, this is supported by its 5yr beta = 0.78, and a bond rating of AA. This leads them to an ERP of 4%. With a tax rate of 26.4%, K_d was calculated to be 6% and K_S at 10%. This leads to a WACC of 9.3%. At this point, we found that the first pass ROIC is 13.1%, which is higher than the WACC. This leads us to anticipate a higher EPV compared to NAV. Detailed calculations are given in the attached exhibits.

NAV & EPV based Price Per Share – NAV-based Price per Share was calculated to be $\$13.6/\text{share}$. EPV-based Price per Share was calculated to be $\$11.9/\text{share}$.

At this point, we found that the *second pass of ROIC is 7.9%*, which is below WACC and our first pass ROIC, and is consistent with the fact that NAV is greater than EPV for this company.

Probability of Catalyst – We feel that the primary reason this company is not attractive currently, is due to management. We believe that they are not efficient allocators of capital: the company is not anywhere near the optimal capital structure, ROA and ROIC have been declining; nor are they operationally efficient as margins have declined across the board. Furthermore, there is constant M&A and divestitures along with reclassification and write-down of assets. It seems like management is trying to optimize capacity, but may not be very good at it. As mentioned previously, the management has a significant ownership stake and has a long and established history with the company. Thus, a change in management may not be imminent. However, with the CEO being older than 70 years of age, there could be a change in the near future. Therefore, we have placed the probability of a catalyst (in this case, a change in management), at 50%.

Intrinsic Value Calculation – As $\text{NAV} > \text{EPV}$, intrinsic value is calculated below:

$$\text{IV} = \text{EPV} + (\text{Catalyst}) * \text{Prob. Sustainability} = 11.85 + (13.6 - 11.85) * 0.5 = \$12.72$$

$$\text{Entry Price} = 2/3 * \text{IV} = 2/3 * \$12.72 = \mathbf{\$8.48} \quad (\text{Current Share Price } \$9.80)$$

Final Recommendation – Since our entry price is well below the current trading price, we **DO NOT recommend buying shares of Exco Technologies at the moment**. Based on value investing principles, the stock would have to fall another 13.4% for Exco to be considered an attractive stock to purchase.

EXHIBITS:

Operating Leases						
Years	2018	2019	2020	2021	2022	2023
Lease Costs	1,422.0	981.5	736.1	245.4	107.3	35.8
Total	1,422.0	981.5	736.1	245.4	107.3	35.8
NPV	3,132.8					
Kd - OL	6.0%					
Implied Interest	187.97					

Debt Structure & WACC												
Years	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2017*	Average
Short-term Borrowings	4.6	0.0	0.0	0.0	0.0	0.0	21.3	10.0	13.5	15.7	10.6	
Curr. Port. of LT Debt	0.0	0.0	0.0	0.0	0.0	0.0	0.6	0.1	4.2	4.0	4.0	
Curr. Port. of Cap. Leases	0.0	0.1	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Current Debt	4.6	0.1	0.1	0.0	0.0	0.0	21.9	10.1	17.6	19.7	14.6	
Long-Term Debt	0.0	0.0	0.0	0.0	0.0	0.0	1.5	0.4	54.5	27.1	31.2	
Capital Leases	0.0	0.1	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Operating Leases	1.1	0.8	0.9	1.1	1.3	1.4	2.0	2.8	3.3	3.2	3.1	
Non- Current	1.1	0.9	1.0	1.1	1.3	1.4	3.5	3.2	57.8	30.4	34.3	
Total Debt	5.8	1.1	1.1	1.2	1.3	1.4	25.4	13.3	75.4	50.0	48.8	
Equity	131.8	114.9	119.2	130.3	143.7	164.1	202.7	244.9	279.4	301.3	305.3	
D/V	4.2%	0.9%	0.9%	0.9%	0.9%	0.8%	11.1%	5.1%	21.3%	14.2%	13.8%	13.1%
E/V	95.8%	99.1%	99.1%	99.1%	99.1%	99.2%	88.9%	94.9%	78.7%	85.8%	86.2%	86.9%
Tax Rate											26.4%	26.4%
Kd											6.0%	
Kd (1-T)											4.4%	4.4%
Ks								ERP	4.0%	10.0%	10.0%	10.0%
WACC												9.3%

ROIC	
Years	2017*
First Pass ROIC	
EBIT	57.4
Taxes	15.2
Amort. For GW	0.0
WC	105.2
Net PPE	116.4
Goodwill	61.9
Intangibles	39.0
Invested Capital = WC + Net PPE + Intang + GW	322.5
ROIC (1)	13.1%
Second Pass ROIC	
NOPLATPA	46.0
WC	115.0
Property and Equipment Net	335.5
Customer Relations	38.4
Product Portfolio	28.3
Goodwill	61.9
Intangibles	0.0
Invested Capital = WC + Net PPE + CR + PP + Intang + GW	579.1
ROIC (2)	7.9%

NAV		
NAV Calculation	2017	MV Notes
Cash And Equivalents	33.6	33.6 BV
Accounts Receivable	116.4	122.6 BV / 0.95
Inventory	56.7	60.3 BV / 0.94 - Obsolescence
Prepaid Exp.	2.0	2.0 BV
Other Current Assets	0.0	0.0 BV
Total Current Assets	208.7	218.4
Property and Equipment Net	116.4	335.5 Org. Cost +/- Adj.
Goodwill	61.9	61.9 BV
Other Intangibles	39.0	0.0 Product portfolio
Loans Receivable Long-Term	0.0	0.0 BV
Deferred Tax Assets, LT	1.4	1.2 BV*0.9
Other Long-Term Assets	0.0	0.0 NA
Customer Relations	0.0	38.4 As Calculated
Product Portfolio	0.0	28.3 As Calculated
Operating Leases	0.0	3.1 As Calculated
Total Non-Current Assets	218.7	468.5
Total Asset Value	427.3	687.0
Accounts Payable	44.8	44.8 BV
Accrued Exp.	15.8	15.8 BV
Short-term Borrowings	10.6	10.6 BV
Curr. Port. of LT Debt	4.0	4.0 BV
Curr. Port. of Cap. Leases	0.0	0.0
Curr. Income Taxes Payable	0.0	0.0
Unearned Revenue, Current	5.4	5.4 BV
Other Current Liabilities	3.8	3.8 BV
Total Current Liabilities	84.4	84.4
Long-Term Debt	31.2	15.2 Calculated
Capital Leases	0.0	0.0 BV
Def. Tax Liability, Non-Curr.	6.5	5.9 BV * 0.9
Other Non-Current Liabilities	0.0	0.0 BV
Operating Leases	0.0	3.1 As Calculated
Employee Stock Options	0.0	1.6 Price*# Options Black Scholes Outstanding
Under (Over) Funded PF	0.0	0.0 BV * (1-Tax)
Total Non-Current Liabilities	37.7	25.7
Total Liabilities Value	122.1	110.2
NAV		576.8
# of Shares Outstanding		42.4
Price per Share		13.6

EPV	
EPV Calculations	2017 Notes
Normalized Operating Profit	64.0 Calculated as per formula using Oper. Margin = 11.3%
(-) One Time Adjustment	2.1 Refer to other exhibits
(+) Adjustment for Op Leases	0.2 Implied interest on oper. Leases as calculated
(+)SOE	0.5 Do not take this prior to 2005!
EBIT	62.5
(-)Taxes on EBIT	16.5 Tax Rate = 26.4%
NOPLAT	46.0
(+) Amortized GW (Merger)	0.0 Do not include after 2001
NOPLATPA	46.0
(+) Depreciation of FA	15.6 Given in note on Cap Ex.
(+) Amortization of other Int	4.8 From Cash Flow Statement
Gross Cash Flows	66.4
(-) Zero Growth CapeX	15.6 Replacement Investment = Cap Ex. Depreciation
(-) Zero Growth Inv in Intangibles	4.8 From Cash Flow Statement
Zero Growth FCF from Ops	46.0
Non Operating Cash Flows (Only A/T Income from Investee Companies)	0.0 None
Normalized Zero Growth FCF	46.0
PV of FCFs	496.6 Normalized Zero Growth FCF / WACC
Add	
ECMS	33.6 From B/S
I&A	0.0 None
Excess Real Estate (A/T)	0.0 None
Less	
BV of STD (incl current portion of LTD)	4.0 From B/S
MV of LTD	18.3 As Calculated
Preferred stock	0.0 None
Minority Interest	0.0 None
Underfunded PF (Add overfunded PF) (A/T)	0.0 As Calculated
Employee Stock Options	1.6 As Calculated
Value of OL	3.1 As Calculated
Equity Value	503.2
No of Shares	42.4 Given in case
Price per share based on EPV	\$ 11.85

