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Team 6
Cooper Tire & Rubber

Cooper Tire & Rubber Company

Justification for choosing Cooper Tire and Rubber Company: As of March 2018, Cooper Tire and Rubber Company (CTB) has P/E = 15.98; M/B = 1.30; Market Cap=$1,546.08; fair analyst coverage; low growth; and it is not an obscure stock. Market Cap is over than $1.3B USD and other metrics such as P/E and M/B are slightly higher than guideline thresholds. The price is at its 52-week low, after examining the financial statements, we believe that the company might be undervalued in the market. **Decision:** Proceed with valuation.

Industry analysis: CTB is a tire design, manufacturing, marketing and wholesaling company; largely located in the US, Europe, Latin America and Asia. While the industry is dependent on commodity raw material prices and has exposure to cyclical purchasing trends. However, this is offset by the industry's high barriers to entry, due to its capital and labour intensive nature. Overall, CTB has a **High Business Risk**, which gives optimal capital structure of 10-29%.

Company analysis: The Target Capital Structure = **29.76%** is based on last three fiscal years' capital structure. This is on the high side of the optimal capital structure range. CTB has Medium Financial Risk which points to a bond rating of BBB to BB. Given that CTB has a high interest coverage ratio, and high LTD/OCF ratio we chose a bond rating of BB. With a Rf of 2.82%, Kd of 5.20**%**, the ERP is thus at 7.0%. This gives Ks 12.20%. With this capital structure, Kd and Ks gives WACC at 9.7%. The ROIC(1st) **11.36%** is greater than WACC, which indicates that we expect NAV<EPV slightly.

Valuation of chosen company:

($/share)	NAV =	EPV =	Catalyst =	ROIC(2nd) =
	52.97	43.58	9.39	7.69%

The 2nd pass ROIC is lower than WACC supporting the NAV>EPV finding. 1st pass ROIC was much larger than 2nd pass ROIC due to EBIT being adjusted in the 2nd pass.

Strategic valuation analysis: Although there are high barriers to entry, CTB has competitive disadvantage when compared to larger firms such as Michelin or Bridgestone in terms of brand equity and product portfolio. They lack the premium brand image that helps guard against fluctuations to raw material prices. They also lack competitive advantage compared to international low-cost producers because the majority of their manufacturing is US based and the appreciating US dollar is eroding their cost advantages. Therefore: (1) the risk of **competitive disadvantage** is assessed at **medium to high**. CTB's lower unit volume sales in the US suggests overcapacity. Therefore (2) the risk of **overcapacity** is assessed at **high**. Cooper's gross and operating margins are in line with industry performance. This together with the competent management credentials and history (3) the **impact of management** on realizing the catalyst is assessed at **low** as it would be difficult to improve upon. Overall, probability of realization is **low** giving a probability of occurring of **20%**.

Assessing value of growth: Not determined to be a growth stock.

Risk management assessment: This risk here will be accounted for by the margin of safety of **1/3**.

Recommendation: With IV of **$45.46**/share the entry price is $**30.31**/share (1/3 MOS) compared to the current stock price of$ 30.35/share means that CTB is undervalued. **Recommendation: BUY**.