Applied Investment Management (AIM) Program

AIM Class of 2016 Equity Fund Reports
Spring 2016

Date**:* Friday, January 29th | ***Time: *3:00 – 4:30* p.m. | ***Location: AIM Research Room 488***

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These student presentations are an important element of the applied learning experience in the AIM program. The students conduct fundamental equity research and present their recommendations in written and oral format – with the goal of adding their stock to the AIM Equity Fund. Your comments and advice add considerably to their educational experience and is greatly appreciated. Each student will spend about 5-7 minutes presenting their formal recommendation, which is then followed by about 8-10 minutes of Q & A.

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Buffalo Wild Wings, Inc. (BWLD)
January 29, 2016
Avery D. Flyte Domestic Consumer Discretionary

Buffalo Wild Wings, Inc. (NASDAQ: BWLD) is an established and growing owner, operator, and franchisor of sports bar and grill restaurants in the United States and Canada. The company operates Buffalo Wild Wings and Emerging Brands (PizzaRev and Rusty Taco) restaurants, as well as selling Buffalo Wild Wings and Rusty Taco restaurant franchises. As of December 31, 2014, the Buffalo Wild Wings restaurant system was comprised of 1,082 restaurants, of which 487 were owned and operated by the company. The company also franchised an additional 591 restaurants, including 584 Buffalo Wild Wings restaurants and 7 Rusty Taco restaurants. In addition to traditional and boneless chicken wings, Buffalo Wild Wings restaurants feature a variety of menu items including Sharables, Wild Flatbreads, specialty hamburgers and sandwiches, wraps, Buffalito soft tacos, and salads. The Buffalo Wild Wings brand was founded by Jim Disbrow and Scott Lowery in 1982 and is headquartered in Minneapolis, MN.

Price ($): (1/21/2016)	147.78	Beta:	0.93	FY: Dec 31	2014A	2015E	2016E	2017E
Price Target ($):	190.04	WACC	7.17%	Revenue (Mil)	1516.22	1789.03	2085.15	2404.58
52WK H-L ($):	205.83 - 142.76	M-Term Rev. Gr Rate Est:	15.5%	% Growth	19.70%	17.99%	16.55%	15.32%
Market Cap (mil):	2,809	M-Term EPS Gr Rate Est:	18.5%	Gross Margin	17.88%	17.24%	18.40%	19.45%
Float (mil):	18.8	Debt/Equity:	11.7	EBITDA Margin	9.20%	8.24%	8.85%	9.21%
Short Interest (%):	14.8	Debt/EBITDA (ttm):	0.30	EPS (Cal)	$ 4.94	$ 5.17	$ 6.42	$ 7.67
Avg. Daily Vol (mil):	0.40	ROA (%):	10.09	FCF/Share	$ 4.27	$ 4.42	$ 6.56	$ 7.27
Dividend ($):	0.00	ROE (%):	14.95	P/E (Cal)	36.99x	28.62x	23.05x	19.29x
Yield (%):	0.0	ROIC (%):	14.08	EV/EBITDA	12.07x	10.70x	8.18x	7.03x

Recommendation

Buffalo Wild Wings, Inc. is a multifaceted enterprise that is strongly positioned to compete in the highly fragmented and competitive restaurant and casual dining market because of its above average industry total revenue growth (16.5% vs. 0.5% YoY) and net operating cash flow (4.52% vs. -59.32% YoY). With a clearly defined and differentiated brand with which to grow its more sizeable Buffalo Wild Wings and Emerging Brands restaurants segment, BWLD continues to significantly outperform its peers; with 4Q results beating expectations on all key metrics. The company achieved revenue and net income growth of 19.7% and 31.5%, respectively, during the fiscal year 2014, driven by same-store sales increases of 5.9% at company-owned restaurants and 5.1% at franchised locations relative to the same period in 2013. In contrast, their leading competitor, Wingstop, announced in August 2015, that net income in the fiscal second quarter 2015 was $584,000, or $0.02 per diluted share, compared to net income of $2.5 million, or $0.10 per diluted share, in the prior fiscal year's second quarter. In addition, Buffalo Wild Wings has achieved a 25.7% five-year EPS CAGR with lower bad debt expense and leverage from strong revenue growth. Based on strong fundamentals and a recognizable brand, it is recommended that Buffalo Wild Wings be added to the AIM Equity Fund with a target price of $192, representing a 30% upside. The company has never declared or paid cash dividends on its common stock.

Investment Thesis

- **Lower Chicken Wing Prices.** The established market price of food items, particularly chicken wings, sold by BWLD are intrinsically dependent upon the cost of baseline materials used to produce them. During 2012-2015 BWLD saw a drop of 25% in the average price paid per pound for chicken wings at company-owned restaurants. A declining trend in chicken prices is set to continue, as supplies from the world's principal growing regions are set to rise, amid intensifying export competition and sluggish international demand. The United States Department of Agriculture forecasts chicken prices to decline almost 5% in 2016, as the recovery in exports is expected to remain measured. Lower chicken prices will translate into lower sourcing costs for traditional and boneless wings, fueling growth in the wing-based or sports bar restaurant industry.

- **Increasing Personal Income.** U.S. personal income in November rose for an eighth straight month on solid wage gains. Internal studies conducted by federal staff at the Bureau of Economic Analysis found that income rose $44.4 billion, or 3.0%, following an unrevised October increase of 4.0%. Economist polled by Reuters had forecasted income advancing 2%; however, wages and salaries actually rose 5%, resulting in a 6% overall gain in October, thanks to strong jobs and pay rate figures. November's increase should support consumer spending and bolster economic growth in quick casual and service segments of the restaurant industry in coming months.
- **Transition to Company-Owned Locations.** Company-owned operations currently comprise 45% + of BWLD's net sales. The company-owned restaurants experienced 10.9% underlying net sales growth over the past 5 years, while franchise operations grew underlying net sales by 6.5% over the same time period. As a result, Sally Smith, President and Chief Executive Officer, announced a system optimization initiative in June 2015. The objective being to increase BWLD's corporate restaurant ownership to 55% of the total system by the middle of 2016. As part of its brand transformation, BWLD exercised its right of first refusal to acquire 38 existing restaurants in Texas, New Mexico, and Hawaii and three restaurants under construction in New Mexico and Hawaii. Franchised units converted to company-owned status experienced enhanced efficiency levels of 40% by reducing labor costs, improving profits, and ensuring customer satisfaction. The acquisition of these restaurants will allow senior management the opportunity to provide shareholders with additional long-term net earnings growth, and the necessary infrastructure and control systems to support the company's disciplined growth strategy.

Valuation

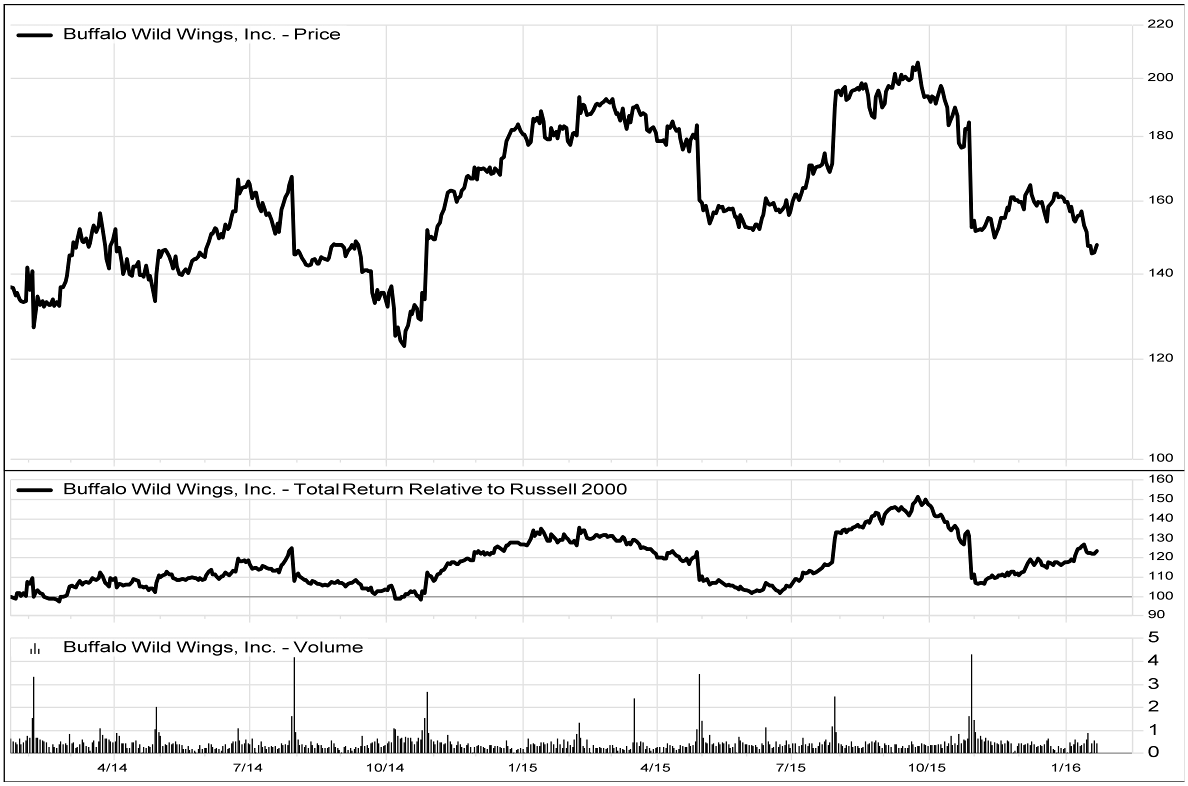
In order to reach an intrinsic value for BWLD, a five-year DCF model was constructed. Using a terminal growth rate of 3.00% and a WACC of 7.17%, an intrinsic value of $190.04 was reached. A sensitivity analysis on the terminal growth rate and WACC ranged from $1652-$222. Additionally, a historical and peer Price/Sales comparison was conducted resulting in a price target of $194. By weighting the two valuation models 50/50, a price target of $192 was reached, which yields a 30% upside.

Risks

- **Increased Labor Costs.** In the United States, each of Buffalo Wild Wings' company and franchise restaurants is subject to federal and state laws governing such matters as minimum wages, working conditions, overtime, and tip credits. The long-term trend toward higher wages in both mature and developing markets may result in additional expense or in disruption to the company's operations, either of which could reduce gross margins and affect overall profitability.
- **Shortages of Supply of Sourced Goods.** Buffalo Wild Wings and its franchisees are dependent upon third parties to make frequent deliveries of perishable food products and other supplies that meet detailed specifications. An unexpected interruption in any of the supply sources or manufacturing facilities could have a material adverse effect on the company's business, results of operations, or financial condition.

Management

Ms. Sally J. Smith assumed the role of Chief Executive Officer and President for Buffalo Wild Wings in July 1996. Prior to such date, Ms. Smith served as Chief Financial Officer of the company from 1994 to 1996, and has been a director and Executive Vice President since August 1996.



Source: FactSet

Ownership

% of Shares Held by All Insider Owners:	1.20%
% of Shares Held by Institutional & Mutual Fund Owners:	94.00%

Source: FactSet

Top 5 Shareholders

Holder	Shares	% Out
Fidelity Management & Research Co.	2,738,000 ▼	14.40
BlackRock Fund Advisors	1,446,000 ▲	7.60
The Vanguard Group, Inc.	1,291,000 ▲	6.80
SSgA Funds Management, Inc.	593,000 ▼	3.10
Franklin Advisors, Inc.	565,000 ▼	3.00

Source: FactSet

Peer Analysis

Name	Ticker	MarketCap (mil)	Sales (mil)	EBITDA	Dividend Yield	EV/EBITDA
Buffalo Wild Wings, Inc.	BWLD	2,774.70	1,731.41	254.63	0.00	10.93
Jack in the Box, Inc.	JACK	2,543.20	1,540.32	301.54	1.60	10.75
Dave & Buster's	PLAY	1,409.30	839.84	176.74	0.00	9.87
BJ's Restaurants, Inc.	BJRI	1,028.10	900.41	115.88	0.00	9.22
Peer Averages		1,660.20	1,093.52	198.05	0.53	9.95

Source: FactSet

Medidata Solutions, Inc. (MDSO)
January 29, 2016

Daniel Kralovec — Domestic Healthcare

Medidata Solutions, Inc. (NASDAQ: MDSO) is a leading provider of cloud-based Enterprise Resource Planning ERP solutions for all stages of clinical trial developments. MDSO serves most subsectors of the healthcare industry, including large pharmaceuticals firms, biotechs, and academic institutions. Through their web-based software, the firm helps customers plan, run, and evaluate clinical trials by increasing efficiency, centralizing data, and eliminating waste. MDSO derives revenue from two operating segments: Subscription (83.6% of FY14 Revenue, ~ 86% Gross Margin) and Professional Services (16.4%, ~29%). The Subscription segment includes the fees paid to access MDSO's cloud-based solutions. The Services segment aids in product implementation and provides extensive training to end-users. This segment consults with customers on how to optimize the clinical trial process. The firm, located in New York City, has 572 customers, none of which account for more than 10% of annual revenue.

Price ($):	43.11	Beta:	1.18	FY: Dec	12/31/2014	12/31/2015	12/31/2016	12/31/2017
Price Target ($):	53.69	WACC	9.40	Revenue (Mil)	355.1	398.6	473.8	560.6
52WK H-L ($):	61.31 - 35.81	M-Term Rev. Gr Rate Est:	15.8%	% Growth	21.03	18.95	18.88	18.31
Market Cap (mil):	2,387	M-Term EPS Gr Rate Est:	20.1%	Gross Margin	73.27	77.28	78.03	78.04
Float (mil):	52.4	Debt/Equity:	82.7	EBITDA Margin	11.16	23.23	24.66	26.90
Short Interest (%):	9.4	Debt/EBITDA (ttm):	5.94	EPS (Cal)	$0.11	$0.87	$1.08	$1.37
Avg. Daily Vol (mil):	0.3	ROA (%):	1.86	FCF/Share	$0.83	$1.21	$1.59	$1.86
Dividend ($):	0.00	ROE (%):	4.28	P/E (Cal)	434.1	49.6	40.1	32.3
Yield (%):	0.0	ROIC (%):	2.27	EV/EBITDA	69.7	26.1	19.9	15.1

Recommendation

Economic uncertainty continues to place many challenges on firms within the healthcare sector. We are seeing a change in global demographics, a shift towards emerging markets, market contraction ($354 billion FY14), and increasing amounts new drugs developments coming to market. Global healthcare spending is projected to grow at a CAGR of 4.3% through FY19. Concurrently, R&D expenditures are predicted to grow at about half the aforementioned rate at a CAGR of 2.4%, reaching $162 billion by 2020. Amidst these macro trends, many are optimistic that the industry will continue to invest substantial capital into clinical testing. Pricing pressure remains the foremost challenge facing companies either conducting or planning clinical tests. MDSO offers a unique solution. By centralizing all of a clinical trial's data into the Cloud, MDSO's product, through many applications, allows customers to operate trials more efficiently, which aid in both cost reduction and better resource planning. Their Cloud platform is split into four segments: core (EDC), platform, data analytics, and extended network. While electronic data capture (EDC) remains core to MDSO's business (60% Revenue), firms recognize additional benefits as they adopt multiple MDSO products, such as data analytics. In fact, the platform segment, the base for data planning, monitoring, and test creation, has grown by about 40% this year. The mobile health market remains significantly untapped, but promising looking forward. Medidata allows customers to develop APIs on top of their Cloud software. Similarly, fifteen trials, some completed with other in progress, have used wearable technology to capture data As previously mentioned, MDSO, though data centralization, has created a circular network that connects patients, research teams, and regulators. By increasing the operational efficiency of clinical tests while reducing overall costs, Medidata's single platform software solution gives customers a unique edge in today's contracting healthcare space. In light of the future R&D spending, MDSO's solutions appear attractive and accretive. Due to the aforementioned reasons and the drivers discussed below, it is recommended that Medidata Solutions be added with a price target of $53.69, representing a 25% upside.

Investment Thesis

- **Macroeconomic Environment.** The increasing globalization of healthcare continues to place an enormous amount of pricing pressure on many drug and life science companies. Over the past several months there has been considerable consolidation within this sector. With regard to clinical trials, the focus now lies with innovation with continued emphasis on cost reduction, improved quality and visibility, and quicker results. By centralizing the various facets of a clinical trial, MDSO's cloud software minimizes the inefficiencies associated with traditional testing which enables firms to remain competitive in the changing, regulated, and scrutinized market.

- **Cloud-Based Solution.** MDSO's offers several solutions to its customers, all of which have played significant roles in increasing the company's bottom line. Core to its business is Rave, the cloud-based data capture and platform program (60% of revenue). It allows customers to build, test, monitor, and report clinical results. Contrary to the traditional method, this increases the scalability of tests, making it an attractive solution for global firms. The adoption of multiple products will continue to be accretive as the firm widens their reach, while exuding an increasing sense of confidence in the MDSO's products.
- **Investment in Data and Analytics.** While the firm derives the majority of its revenue from electronic data capture, there is a significant untapped potential within the analytical area of their software. Medidata Insights offers a centralized view of all operational trial data. Having a clear view of all the inputs that go into a trial run, whether costs, results, etc., give test managers a unique opportunity to identify inefficiencies and optimize resources. From an operational perspective, data analytics appears to be a viable value added service protecting against some of the pressures companies face within the healthcare sector.
- **Disruptive Potential.** It is estimated that by 2018, 50% of 3.4 billion mobile device users will have downloaded a mobile health (mHEALTH) app. MDSO allows both customers and third parties to develop APIs on top of their cloud software. Some MDSO based trails been successful in using wearable technology to collect patient data. As the life science industry shifts towards digital health ramps up, MDSO will be in position to capture more market share.
- **Talent Acquisition.** Being primarily a technology firm, human capital is one of MDSO's greatest assets. Over the years, the firm has acquired many talented individuals, both for management and development positions. The new San Francisco office offers a direct pipeline to Silicon Valley. Insider confidence has grown, shown by a 22% increase in shares held by insiders recently.

Valuation

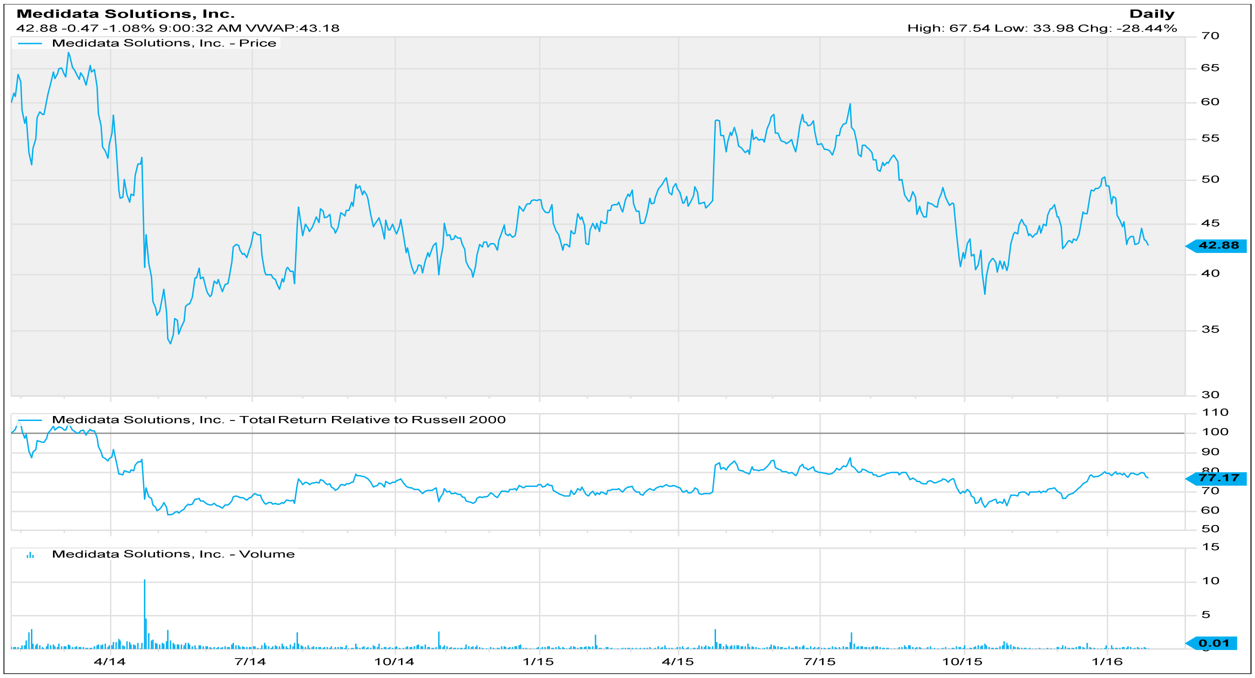
In order to reach an intrinsic value for MDSO, a five year DCF model was constructed. Using a terminal growth rate of 2.5%, WACC of 9.41%, an intrinsic value of $56.74 was reached. Additionally, an EV/SALES multiple valuation was conducted using NTM Revenue of $399.1, a comparables average of 6.7x, resulted in a valuation of $48.27. Finally, an EV/EBITDA multiple valuation was calculated. Using the a similar blended comparables and historical average of 24x and NTM EBITDA of $121.5M, the multiple resulted in a valuation of $53.01. weighting the three valuation models 50/25/25, a price target of $53.69 was reached, which yields a 24.78% upside. MDSO does not pay a dividend.

Risks

- **Regulatory Environment.** MDSO serves companies in a highly regulated industry. Any change in the method by which trials are conducted may have adverse effects on the frim.
- **Security/data breaches.** Many recent data breaches have increased awareness over cyber security. This would be detrimental causing health records, test methods, results, etc. to be exposed.
- **Market consolidation.** The industry has seen much consolidation lately. MDSO services both small and large customers and M&A activity may result in the loss of customers.

Management

Tarek Sherif has held the position of CEO since 2001 and Chairman of the Board since 2009. He co-founded the company along with Glen de Vries, the firm's president. Mr. de Vries has held this position since the company's inception. Other executives include: Rouven Bergman (CFO), Mike Capone (COO), Steven Hirschfeld (CCO), David Lee (CDO), Andrew Newbigging (Senior VP of R&D).



Source: FactSet

Ownership

% of Shares Held by All Insider Owners:	5.37%
% of Shares Held by Institutional & Mutual Fund Owners:	>90%

Source: FactSet

Top 5 Shareholders

Holder	Shares	% Out
Sands Capital Management LLC	5,500,277	9.93
Brown Capital Management LLC	5,345,968	9.66
BlackRock Fund Advisors	4,676,541	8.45
The Vanguard Group, Inc.	3,987,693	7.20
Fidelity Management & Research Co.	2,652,867	4.79

Source: FactSet

Peer Analysis

Name	Ticker	Market Cap (mil)	Sales (mil)	EBITDA	Dividend Yield	EV/ EBITDA
Medidata Solutions, Inc.	mdso	2,387	383	42.028	0.00	69.72
Datatrak International, Inc.	DTRK	4	10	-2.7	0.00	#N/A
Oracle Corporation	ORCL	143,346	37,473	16183.0	1.17	10.72
DRS Data and Research Servic	025025	4	#N/A	#N/A	#N/A	#N/A
Merge Healthcare Incorporated	MRGE	#N/A	228	45.6	0.00	12.62
Microsoft Corporation	MSFT	403,230	90,057	32270.0	2.74	9.04
Peer Averages		#N/A	#N/A	#N/A	#N/A	#N/A

**Removed For Relative Valuation Analysis*

Prudential Plc (PUK)

January 29, 2016

Travis Mantel — International Financial Services

Prudential Plc (NYSE: PUK) operates as a holding company with units that provide insurance and financial services. Their retail financial products and services include life insurance, pensions and annuities, and a collective of investment schemes. PUK has international exposure with principal operations in Asia, the United States, and the United Kingdom. Prudential Plc operates out of two segments: insurance (96%) and asset management (4%); they conduct business through its vast network of subsidiaries. Prudential Plc was founded on May 30, 1848 and is headquartered in London, the United Kingdom.

Price ($): (1/26/16)	38.1
Price Target ($):	47.42
52Wk H-L ($):	37-53
Market Cap (mil):	47,730
Float (mil):	2,528.30
Short Interest (%):	N/A
Avg. Daily Vol (mil):	0.28
Dividend ($):	1.17
Yield (%):	2.53%

Beta:	1.44
WACC	8.1%
M-Term Rev. Gr Rate Est:	4.1%
M-Term EPS Gr Rate Est:	4.8%
Financial Leverage	.85x
ROA:	0.7%
ROE:	21.2%
ROIC:	12.9%
Enterprise Value (mil)	53,731

FY: Dec	2013A	2014A	2015E	2016E
Revenue (Mil)	84,729.0	98,656.0	93,250.0	96,453.0
% Growth	-4.11%	16.44%	-5.48%	3.43%
Gross Margin	7.23%	5.35%	6.58%	6.91%
Pretax Margin	3.58%	4.76%	5.58%	5.71%
EPS (Cal)	$1.76	$2.87	$3.08	$3.21
P/E (Cal)	27.2	16.1	16.9	17.2
BVPS	12.5	14.3	14.9	15.3
P/B	3.6	3.2	3.4	3.5

Recommendation

Prudential Plc has seen solid growth over the past five years with a profits increasing by 12% YoY. They have been able to maintain this rate through organic and inorganic means. The management has pushed into emerging markets through acquisition to complement organic growth. PUK has been able to complete these acquisitions while maintaining their debt/equity at 85%. They have a positive cash position ($9 billion) which covers 60% of their long term debt. In addition to growth, Prudential has been able to achieve above average returns, and its ROIC is above most competitors. They posted an ROIC of 12.9% in 2014 while their next closest competitor (Manulife Financial) had an ROIC of 5.9%. PUK has also been able to grow their European Embedded Value (EEV) new business profit by a CAGR of 11% over the past five years. Life insurance is a long term product that produces cash flows over many years. The EEV new business profit reflects the total value of the future profit streams which cannot be recognized in the current period. Nine months through 2015 US life operating profits were up 11%, UK life operating profits were up 19%, Asia life operating profits were up 20%, and their asset management business (M&G) grew operating profits by 11%. With continued profit growth, a strong balance sheet, high returns on their investments, and penetration of Asian emerging markets, it is recommended that Prudential Plc be added to the AIM International Equity Fund with a target price of $47.42, representing an upside of 24.5%. Prudential Plc also pays a dividend that yields 2.53%.

Investment Thesis

- **Emerging Market Exposure.** Over the long term emerging markets are forecasted to outpace the growth of developed economies. PUK is well positioned to take advantage of this growth with 15.2% of their revenues coming from emerging markets. In Asia they have leadership positions in vastly under-penetrated insurance markets such as Indonesia, South Korea, and Taiwan. With a rapidly growing middle class population in Asia demanding protection and savings products, Prudential is well positioned to supply their needs.
- **Acquisitions.** Prudential Plc is very aggressive with acquiring new companies for both investment purposes and for insurance purposes. In 2015 they made four acquisitions. These acquisitions have contributed to operating profit increase of 24% since mid year. This artificial growth is helping PUK penetrate emerging markets. At the end of July, they announced the

purchase of an investment services company called Artmedia. Artmedia is a smaller Slovakian company that will give PUK exposure to a region they haven't been exposed to before. In the past PUK has targeted these smaller companies and used their resources to penetrate the market. These smaller acquisitions continue to add to the recent success of Prudential. Their profits have increased over the past 5 years by a CAGR of 12%.

- **Risk Management.** Many insurance companies in the EU had a difficult time adhering to the new Solvency II regulations which called for higher surpluses. PUK is compliant with the new regulation and has enough liquidity to deal with all obligations through 2019. The new regulation has not been an issue for PUK. Further, they are well capitalized to deal with risk within their insurance operations.

Valuation

To find the intrinsic value of PUK a price to book multiple was used, as well as a dividend discount model. The 5-year average historical price-to-book for PUK was 2.75x while its peers' 5-year historical average was .86x which lead me to an average P/B multiple of 1.81x. Using a BVPS of 13.94, the P/B multiple yielded an intrinsic value of $25.16. The discounted dividend model was used with a WACC of 8.13% and a long term growth rate of 2% which resulted in an intrinsic value of $23.06. Weighting these valuations 25/75 respectively, the final estimated intrinsic value of PUK is $23.59. The ADR on the NYSE represents two shares of Prudential Plc, so we find the true intrinsic value of this security by doubling the single share intrinsic value. This gives us a true intrinsic value of PUK of $47.18 which offers an upside of 27.4%.

Risks

- **Emerging Market Growth.** While PUK is not exposed to any currency trading, the current fluctuations in global currencies have affected emerging market growth. Any slowdown in the emerging markets that PUK is trying to penetrate would greatly affect their growth. All signs are pointing to emerging markets growing faster than developed countries in the near future.
- **Global Regulatory Risk.** The EU has been pushing for a new regulatory framework for insurance companies since 2009. The Solvency II Directive sets out a new framework of regulation that oversees insurance companies more closely. This framework was implemented on January 1, 2016. There have not been any problems yet, but the new regulation could restrict future growth of PUK and will be costlier. There is also more regulation currently being talked about in the EU that could affect PUK.
- **Acquisition Risk.** Every acquisition comes with their share of risks. Prudential has been completing multiple acquisitions throughout the year. While large growth can result from an acquisition, the opposite can be true too if it doesn't go smoothly. There is extra risk when they are acquiring companies outside of the finance industry.

Management

Mr. Michael Wells is the CEO and Executive Director for Prudential Plc. Before being elected as CEO in June of 2015, Mr. Wells was CEO of Jackson National Life Insurance Company (United States subsidiary of PUK). He comes with over 19 years of strategic leadership experience. Mr. Paul Manduca has been the Chairman of the Board of Directors since 2012. Mr. Manduca comes with over 30 years of accounting and management experience. He ultimately retired as the Chairman of JPM European Smaller Companies Investment Trust Plc in 2012.

Ownership

% of Shares Held by All Insiders and 5% Owners:	7.00% ▲
% of Shares Held by Institutional & Mutual Fund Owners:	79.80% ▬

Source: FactSet

Top 5 Shareholders

Holder	Shares		% Out
Capital Research & Management Co. (World Investors)	136,702,000	▲	5.30
Norges Bank Investment Management	103,452,000	▬	4.00
Baillie Gifford & Co.	92,728,000	▼	3.60
Capital Research & Management Co. (Global Investors)	82,031,000	▼	3.20
Legal & General Investment Management Ltd.	78,687,000	▼	3.10

Peer Analysis

Name	Ticker	Market Cap (mil)	Net Income (mil)	Div. Yld. %	P/B	D/E
Prudential Plc	PUK	47,730	3,925	2.53	2.5	0.9
American International	AIG	68,481	4,727	2.02	0.7	0.3
AXA	CS	59,009	5,598	4.23	0.88	0.7
AEGON	AGN	15,221	780	4.66	0.38	0.5
Manulife Financial	MFC	25,223	2,104	3.73	0.9	0.2
Peer Averages		41,984	3,302	3.66	0.7	0.4

Source: FactSet

WNS Holdings ADR (WNS)
January 29, 2016

John Grant | International Producer Durables

WNS Holdings (NYSE: WNS) is a leading provider of business process management (BPM) services utilizing an onshore, nearshore and offshore delivery model. WNS seeks to transform clients' businesses by identifying business and process optimization opportunities. The firm has 31,340 employees (+10% YoY) serving 280 clients through 39 different service center locations, with operations primarily in India, the UK, and South Africa. WNS recognizes revenue through two different segments: WNS Global BPM (88.6% of total revenues), and WNS Auto Claims BPM (11.4%). Revenues are primarily generated in the UK (52.8% of total revenues), United States (25.9%) and Australia (6.4%). WNS (Holdings) Limited was founded in 1996 and is headquartered in Mumbai, India.

Price ($):	$ 29.19	Beta:	1.00
Price Target ($):	$ 36.05	WACC	7.98%
52WK H-L ($):	34.37-22.04	M-Term Rev. Gr Rate Est:	8.3%
Market Cap (mil):	1,530	M-Term EPS Gr Rate Est:	21.9%
Float (mil):	50.9%	Debt/Equity:	6.6%
Short Interest (%):	22.4%	Debt/EBITDA (ttm):	25%
Avg. Daily Vol:	156,639	ROA (%):	11.51%
Dividend ($):	$ -	ROE (%):	15.69%
Yield (%):	0.0%	ROIC (%):	14.96%

FY: Dec	2015	2016E	2017E	2018E
Revenue (Mil)	503,016	537,826	582,971	639,424
% Growth	7%	7%	8%	10%
Net Income Margin	12%	12%	13%	15%
EBITDA	$ 104,310	$ 113,611	$ 117,625	$ 142,137
EPS (Cal)	$1.10	$1.22	$1.42	$1.77
FCF/Share	$1.44	$1.43	$1.43	$1.45
P/E (Cal)	26.6	26.0	23.0	20.0
EV/EBITDA	13.9	13.0	12.0	10.0

Recommendation

As a leader in the BPM market space, WNS is advantageously positioned to benefit from many disruptive forces pushing clients to adjust their business models. Some of the major market disruptors are a growing need for digital strategies and value-adding analytics, managing regulatory and compliance related changes, and traditional cost, quality and efficiency requirements. WNS has become increasingly attractive to hyper-growth e-commerce organizations because of a growing reputation of enabling business acceleration by providing essential process expertise, domain knowledge and analytical capabilities. As a result, total revenue expanded 10.4% on a constant currency basis between 3Q15 – 3Q16 ($128.4M – $135.9M) and is expected to expand ~10% YoY by the end of FY16. Management was able to convert strong revenue growth into larger earnings growth - between FY14–15 EPS expanded from $0.78 to $1.10 (41% increase). Management intends to use the high amount of cash WNS has generated towards long-term share buyback programs and M&A opportunities. In FY14 WNS acquired Fusion, a South American BPM company, and management has indicated future M&A is likely to occur. To support the increasing business in the United States, which is now 26% of revenues, WNS opened a new operational center in South Carolina in 2015. Management has recently authorized a repurchase program up to 3.3 million ADRs (~6% of outstanding ADRs) and the program will remain active for 36 months and be funded by internal cash accruals. Due to a favorable valuation, strong financial positioning and promising outlook, it is recommended that WNS Holdings be added to the International AIM Fund with a price target of $36.57, representing a 27% upside.

Investment Thesis

- **Strong Financials to Support Growth.** WNS continues to operate without debt and as of 3Q16 net cash was recorded at $149M (~$2.80 per share), up 15.5% from 2Q16 ($129M). Additionally, FCF/share was $0.46 and adjusted EPS was $0.50 in 3Q16. WNS plans to use cash as the main resource for internal development and M&A. WNS continues to record 10%+ orgarganic revenue growth on a constant currency basis. Net income increased 41.65% between FY14 – FY15 ($41M - $58M) because of increasing revenues in the more profitable segment, WNS Global BPM (8% y/y increase, 23% operating margin). Margins will continue to rise as they have between FY11 – FY15: gross margin (15.03% to 31.19%) and operating margin (4.47% to 12.34%).

- **Increasing Client Base**. Management has indicated in Q3 2016 that the firm added five new clients, expanded six existing relationships, and renewed 21 contracts. Aviva, WNS' largest customer with 11% of revenues, recently extended their contract with WNS to 2022. Employee head count has increased to a historic level of 31,340 in anticipation of three major deals (utilities, travel, and retail), which are expected to significantly increase 2017 revenues. Two of these deals will be with new clients. Travel & leasure is the second largest (20% of total revenues) and fast growing (+11% YoY, +5% QoQ) industry revenue stream in the WNS Global BPM segment.
- **Improving Workforce.** BPM services rely heavily on their talent and WNS has made a major push to improve their workforce through unique training opportunities. Seat utilization at workstations remain above industry average with used seat utilization at 1.63 shifts and built seat utilization at 1.19, both flat with the prior quarter. Consequently, attrition has decreased from 35% to 30% between 2Q16 – 3Q16, a strong tailwind for future talent retention. WNS will launch their joint MBA program in business analytics with NIIT University in Delhi, graduates are placed into WNS research and analytics practice (currently 2,500 employees).

Valuation

In order to reach an intrinsic value for WNS, a five year DCF model was constructed. Using a terminal value growth rate of 2.5% and a WACC of 7.98%, an intrinsic value of $38.56 per share was reached. In addition, a P/E multiple valuation was constructed using five comparable firm's average P/E multiple of 21.28x, WNS P/E of 26.61x and a 2016E EPS of $1.22 an intrinsic value of $35.48 was reached. Lastly, an EV/EBITDA multiple valuation was conducted. The same five comparables produced an average EV/EBITDA of 13.96x, used with WNS's current EV/EBITDA of 13.86x and a 2016E EBITDA of $113.61M produced an intrinsic value of $34.08. Weighing the three valuation models 50/25/25 respectively, a target price of $36.57 was obtained, a potential upside of 27.32%. WNS does not pay a dividend.

Risks

- **Concentration on Top Clients.** Having a high concentration from a small group of clients is common in the BPM market, WNS recognizes ~32% of revenues from top five customers (down from 33% 2Q16). Aviva remains WNS largest client, representing 11% of total revenues as of 3Q16 (down from 15.2% 3Q15). WNS focuses expanding contracts and maintaining relationships with their top clients, however a loss of one major client would have a large impact on revenues.
- **Rising Labor Costs.** On December 31st, 2015 the Indian government passed the India Payment of Bonus Act, consequently creating an unexpected $2.2M expense as it increases employee bonus amounts for certain wage categories. However, an Indian dominated workforce remains attractive to foreign clients as relatively low wages is a cost effective alternative to in house BPM.
- **Currency Exchange Exposure.** Roughly 75% of expenses are denominated in Indian rupees, and about 50% of revenues are denominated in British pounds, WNS is exposed to currency fluctuations that could adversely affect operating results. To minimize the effects of currency exposure WNS hedges most exposure out about a year using options and forward contracts.

Management

Keshav R. Murugesh has been the acting CEO & Executive Director since February 2010. Prior to WNS, Keshav was the President & CEO Syntel, Inc., an American BPM headquartered in Troy, MI. Ronald Gillette, acting COO, has been with the firm since November 2013 and is a graduate of the US Military Academy. Sanjay Puria, acting CFO and Senior Vice President, has been with WNS since January 2010.

Ownership

% of Shares Held by All Insider Owners:	11.68%
% of Shares Held by Institutional & Mutual Fund Owners:	87.70%

Source: FactSet

Top 5 Shareholders

Holder	Shares (000)	% Out
Waddell & Reed Investment Management Co.	10,948	21.4%
Fidelity Management and Research Company	3,686	7.2%
Columbia Wagner Asset Management LLC	2,827	5.5%
Wellington Management Company LLP	2,145	4.8%
TimesSquare Capital Management, LLC	2,138	4.2%

Source: FactSet

Peer Analysis

Name	Ticker	Market Cap (mil)	EPS (LTM)	EBITDA (LTM)	Price/ Earnings	EV/ EBITDA
WNS Holdings	WNS	1,530	1.10	98.7	26.61	13.86
ExlService Holdings Inc.	EXLS	1,451	1.33	93	33.67	15.09
Genpact Limited	G	5,119	1.02	395	24.07	12.09
Infosys Limited	INFY	38,377	0.88	2305	18.84	13.33
Firstsource Solutions	FSL.NS	24,696	3.43	3750	9.58	8.47
The Container Store Group	TCS	4,523	0.18	62	20.28	15.34
Peer Averages		14,833	1.37	1321.0	21.29	12.86

Source: FactSet