Applied Investment Management (AIM) Program

AIM Class of 2014 Equity Fund Reports
Fall 2013

Date: Friday, October 25th | ***Location: AIM Research Room (488)***
Presentation Times 3:00-5:00 p.m.

Join us in person, or considering joining us live at:
Connect to the LIVE meeting via Blackboard web-based conferencing tool

Student Presenter	Company Name	Ticker	Price	Page No.
Joe Bachmann	Halcón Resources Corporation	HK	$5.46	2
Charlie Hoover	Prestige Brands Holdings, Inc.	PBH	$31.28	5
Nick Kerger	Orbotech Ltd.	ORBK	$11.98	8
Axel Sjoberg	Adidas A.G.	ADDYY	$55.88	11

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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Halcón Resources Corporation (HK)
October 25, 2013

Joseph Bachmann — Domestic Energy

Halcón Resources Corporation (NYSE: HK) is an independent energy company that engages in the acquisition, production, exploration, and development of oil and natural gas properties in the United States. The company's principal resource plays include the Bakken/Three Forks Formations with an area located in North Dakota and Montana (150,000 net acres), the El Halcón portion of the Eagle Ford Formations in east Texas (60,000 net acres), and the Utica/Point Pleasant Formations comprising a leased area in Ohio and Pennsylvania (142,000 net acres). As of December 31, 2012, the company had estimated proved reserves of approximately 108.8 million barrels of oil equivalent (MMBoe), consisting of 87.4 million barrels (MMBbls) of oil, 5.4 MMBbls of natural gas liquids, and 96.1 billion cubic feet (Bcf) of natural gas. The company was formerly known as RAM Energy Resources, Inc. and changed its name to Halcón Resources Corporation in February 2012. HK is headquartered in Houston, Texas.

					FY: Jun. 30	2012A	2013E	2014E
Price ($): (10/18/13)	5.46		Beta:	1.45				
Price Target ($):	6.92		WACC	8.61%	Revenue (Mil)	247.95	964.19	1108.82
52 WK H-L ($):	4.41-8.28		M-Term Rev. Gr Rate Est:	5.00%	% Growth	139.12%	288.87%	15.00%
Market Cap (mil):	2,228.17		M-Term EPS Gr Rate Est:	4.00%	Gross Margin	35.68%	48.14%	49.00%
Float (mil):	215.20		D/E	109.35	Operating Margin	-11.01%	20.48%	22.00%
Short Interest (%):	22.89%		ROA:	0.40%	EPS (Cal)	-0.91	0.28	0.16
Avg. Daily Vol (mil)	6.74		ROE:	0.90%	FCF/Share	-56.06	-14.44	-0.99
Dividend ($):	0.00		Debt/EBITDA	4.71	P/E (Cal)	79.17	21.59	11.84
Yield (%):	0.00%				EV/EBITDA(Cal)	45.09	8.37	4.35

Recommendation

Until recently, HK has been primarily interested in creating an asset base through acquisitions, focusing on unconventional and oil-rich plays. Rather than limiting their purchases to one specific area, HK has made purchases across several geographically separated, but geologically similar shale formations, allowing substantial production flexibility. Now, with a strong, diversified asset base and access to the latest fracking techniques, HK ready to create several years of profitable production growth. Production in Bakken/Three Forks portion of their holdings has considerably improved, organically growing 10% from 1Q13 to 2Q13 to consist of 56% of 2Q13 production. Although most of the company's current production is in the Bakken, they have also begun increasing their production in the El Halcón portion of the Eagle Ford shale, a 94% oil play with a 119% quarter over quarter production growth. That area accounts for 6% of 2Q13 production and should continue to expand as capital allocation to the area increases. Furthermore, the company's exploratory acreage in the Utica/Point Pleasant shale formations hold strong, untapped, liquid-rich upside potential. Overall, the company is poised to enter a high growth phase driven by efficient exploitation of a substantial, diversified asset base. Because of these reasons and a favorable valuation, it is recommended that HK be added to the AIM Equity Fund with a target price of $6.92, which offers a potential upside of 26.8%. HK does not pay a dividend.

Investment Thesis

- **Extensive Growth of Production and Revenues.** Since 2012, HK has experienced rapid growth in their daily production. Daily production in Q3 of 2013 was approximately 35Mboe per day, compared to 22.4 Mboe per day for the same quarter in 2012, a 56% increase. These production increases have proven lucrative, with triple digit revenue growth since 2012. With currently only 48% of their proved reserves developed, the company still has substantial room for organic production growth solely through their existing asset base. This production ramp up has also been accompanied by increased operational efficiencies. This includes the increasing use of newer batch drilling techniques, which allow for an average of $1.3 MM in savings over comparable single well drilling, facilitating margin improvement going forward.

- **Utica/Point Pleasant Shale Resource Potential.** HK currently holds approximately 142,000 net acres in the Utica/Point Pleasant shale formation. This area has high potential profitably, but currently only accounts for less than 1% of HK productions. Although the company is still in the early stages of exploring and evaluating these assets, the area is already considered liquids-rich for the region, with test wells indicating 70% liquids and greater. With over 500 potential drill areas identified, this currently untapped play could lead to substantial proved reserve and production growth for the company, improving future profitability.

Valuation

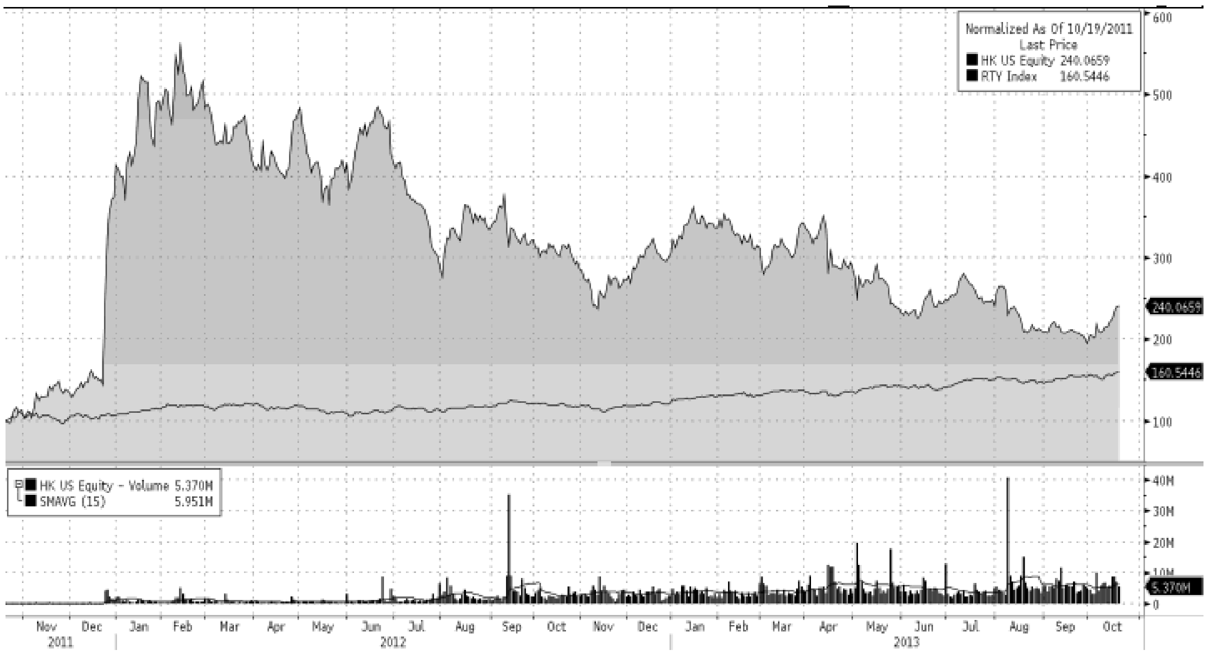
In order to reach an intrinsic value for HK, a ten year discounted cash flow model was conducted. Using a short-term growth rate of 15%, a terminal growth rate of 2%, and a WACC of 8.61% resulted in a valuation of $7.04. Additionally, an EV/EBITDA comparison valuation was used. Using an EV/EBITDA multiple of 9.50, consisting partially of an industry average, and using a 2014 expected EBITDA of $557M, a price of $6.77 was obtained. Finally, a NAV of proved and unproved reserves yielded a per share price of $6.95. Weighing each valuation equally, a price target of $6.92 was reached.

Risks

- **Commodity Price Risk.** The market prices for oil and gas are highly volatile, especially in the current geopolitical and economic environment. If future oil and gas prices move unfavorably, HK future revenues could be materially hurt. HK employs an active hedging program consisting of swaps and cost collars to help mitigate this risk, but this hedging structure could also hinder HK's gains in rising price environment.
- **Governmental and Environmental Regulation.** Hydraulic fracturing, or "fracking", a process by HK and other energy companies of injecting water, sand and chemicals into rock formations to stimulate oil and gas production, has come under intense public scrutiny due to its potentially negative effect on water supplies and the environment as a whole. Federal or state legislation that hinders or prohibits fracking could cause material adverse effects on HK's production, reducing future profitability.
- **Substantial Debt Position.** In the process of acquiring their asset base, HK has entered into substantial indebtedness: as of June 2013, the company has approximately $2.7B in long term debt. Although it is expected that production growth will be sufficient to cover these liabilities, production decline could force untimely or unfavorable selling of assets, which could hurt the company materially.

Management

Floyd Wilson has served as a Chairman and CEO since its formation in 2012. Mr. Wilson served as Chairman of the Board and Chief Executive Officer of Petrohawk Energy Corporation from May 2004 until BHP Billiton acquired Petrohawk in August 2011. He has over 30 years of experience in the energy sector. President Stephen Herod has also served since HK's inception, and he was previously acted as Executive Vice President at Petrohawk. Mark Mize is the company's CFO, Executive Vice President and Treasurer and served in the same position at Petrohawk. Both men have over 20 years of experience in the energy industry.



Source: Bloomberg

Ownership

% of Shares Held by All Insider and 5% Owners:	55%
% of Shares Held by Institutional & Mutual Fund Owners:	28%

Source: Yahoo! Finance

Top 5 Shareholders

Holder	Shares	% Out
Petro-Hunt Holdings	103,741,278	25.42
Canada Pension Plan	49,099,919	12.03
Kellen Holdings LLC	14,671,666	3.60
Blackrock	10,084,791	2.47
Vanguard Group Inc	9,621,198	2.36

Source: Bloomberg

Prestige Brands Holdings, Inc. (PBH)
October 25, 2013

Charlie Hoover Healthcare

Prestige Brands Holdings, Inc. (NYSE: PBH) is the largest independent provider of over-the-counter products in North America. The firm distributes healthcare and household cleaning products, including oral, eye and skin care; cough, cold, allergy and sinus; and household cleaning appliances, to retail stores in the United States, Canada, and other international markets. Headquartered in Irvington, New York, PBH is a company of brand builders that continues growth by acquiring strong and well-recognized brands from larger consumer products and pharmaceutical companies.

Price ($) (10/15/13)	31.28	Beta:	1.8
Price Target ($):	39.20	WACC	9.0%
52WK Range ($):	16.30-35.98	M-Term Rev. Gr Rate Est:	14.9%
Market Cap:	1.60B	M-Term EPS Gr Rate Est:	18.6%
Float	50.5M	Debt/Equity	199.9%
Short Interest (%):	1.5%	ROA:	3.8%
Avg. Daily Vol:	288,180 K	ROE:	14.9%
Dividend ($):	$ -		
Yield (%):	0.00%		

FY: December	2012A	2013E	2014E
Revenue (Mil)	441	624	717
% Growth	31.08%	41.38%	15.00%
Gross Margin	51.55%	55.68%	53.00%
Operating Margin	23.31%	30.77%	28.00%
EPS (Cal)	$0.74A	$1.30E	$1.59E
FCF/Share	-11.60	2.41	2.86
P/E (Cal)	42.28	24.02	19.66
EV/EBITDA	17.50x	11.05x	11.41x

Recommendation

Prestige Brands Holdings, Inc. sells well-recognized, brand name, over-the-counter (“OTC”) healthcare and household cleaning products largely in North America. The firm utilizes the strength of their brands, their established retail distribution network, a low-cost operating model and an experienced management team in order to maintain their competitive edge in this industry. Originally formed in 1996 as a joint venture of Medtech Labs and The Shansby Group (a private equity group), the firm’s purpose was to acquire certain OTC drug brands from American Home Products. It wasn’t until 2001 where household cleaning products were included in attempts to further diversify their brand portfolio, which is why the OTC Healthcare Segment comprises of 86.1% of net revenues in 2013, as is the core of their business. During 2013, approximately 77.0% of PBH’s net revenues were from brands with a number one or number two market position, consistent with the approximate 67.0% and 73.0% during 2012 and 2011 respectively. Additionally, principal customer relationships include Walmart, Walgreens, CVS, Target and Dollar Tree. Sales of these top five customers accounted for approximately 26.9% of total gross sales in 2013 compared to approximately 40.0% in 2012 and 41.7% in 2011. The continual integration of largely branded products into PBH’s already well diversified product portfolio allow for ample opportunity for future growth amidst those respective markets. In addition to the wide array of products sold, management’s efficient operating model has continually increased their gross margins by upwards of 4% by minimizing general and administrative costs by approximately 4.5% consistently per year as well. Because of these reasons and a favorable valuation, it is recommended that PBH be added to the AIM Equity Fund with a target price of $40.48, which offers a potential upside of 29.41%. The firm does not pay a dividend.

Investment Thesis

- **Diversified Portfolio of Well-Recognized Consumer Brands.** The firm owns and markets well-recognized consumer brands, many of which were established over 60 years ago. The diversified portfolio of brands provides PBH with multiple sources of growth while simultaneously minimizing reliance on any one product or category. The acquisition of over ten core OTC Healthcare brands in the past three years leaves plenty of room for growth in their new respective markets, and the divestiture in Phazyme, a gas treatment brand, in 2013 opened up $21.7M in cash to further grow into these new markets in the next three years.

- **Proven Ability to Develop and Introduce New Products.** PBH focuses marketing and product development efforts on identifying under-served consumer needs, designing products to address those needs, and extending their well-known brands to other products. The success of meeting consumer needs has been vital to the continued success of PBH business, and will continue to drive revenue growth moving forward by approximately 6% annually.
- **Efficient Operating Model.** The firm oversees the production planning and quality control aspects of the manufacturing, warehousing, and distribution of their products, while choosing to outsource the operating elements of these same functions to well-established third-party providers. This management strategy allows PBH to benefit from core competencies and maintain a highly variable cost structure, in addition to low overhead, limited working capital, and minimal capital expenditures through business. Specifically, this approach led to a 4.1% increase in gross margin from 2012 to 2013, and a 4.6% decrease in G&A % to total revenues. Management is confident that their strategies will keep these structural changes sustainable moving forward.

Valuation

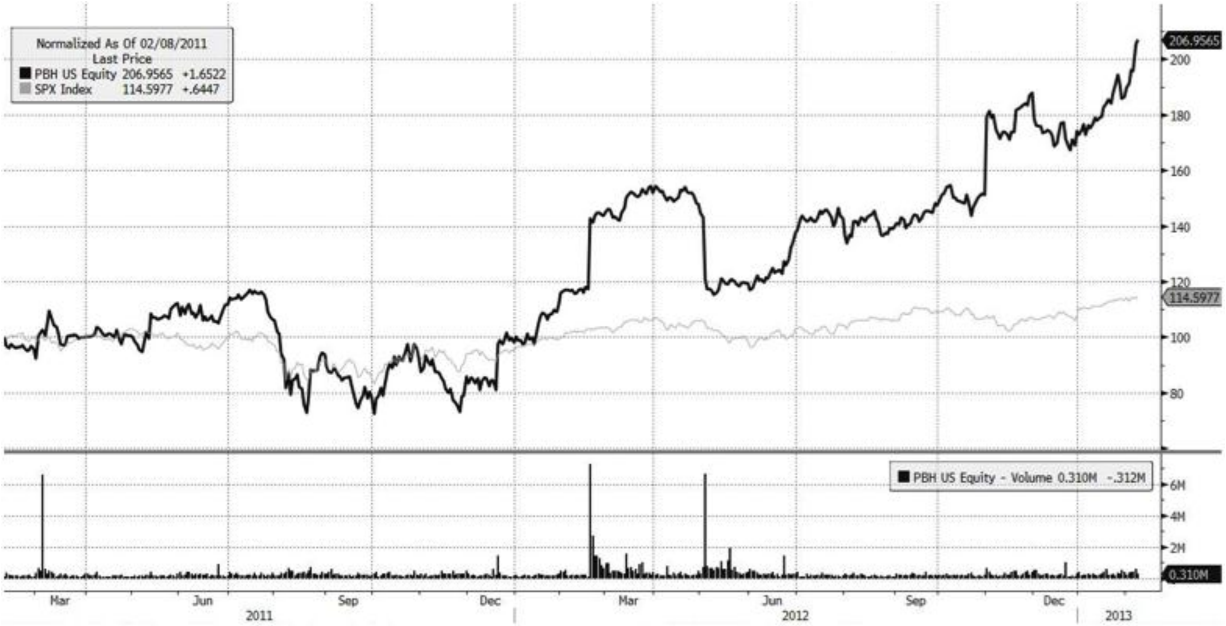
In order to reach an intrinsic value for PBH, a ten year discounted cash flow model was conducted. Using a terminal growth rate of 3% and a WACC of 9.05% resulted in a valuation of $41.87. Sensitivity analysis provided for a range between $28.95 and $50.11. Additionally, relative valuations using P/E and EV/EBITDA ratios were utilized. After calculating respective multiples, estimated P/E and EV/EBITDA values were $29.19 and $45.68, respectively. The total valuation of the firm was calculated by a weighted average of the three projections. First, the intrinsic value, $41.87, was weighted by 50%. Second, the EV/EBITDA valuation of $45.68 was weighted by 30%. Finally, PBH's P/E multiple valuation of $29.19 was weighted by 20% - resulting in an overall price target of $40.48 – a 29.4% upside.

Risks

- **High Levels of Competition.** Many competitors in this industry have greater resources than PBH. The access to greater resources may provide the ability to spend more aggressively on R&D, advertising and marketing, and may respond more effectively to changing business and economic conditions. Should these conditions intensify, it could have a material adverse effect on the firm's business, financial condition and results from operations.
- **Limited Number of Customers.** The limited number of customers, although credible, have no long-term agreements with PBH. These customers represent a large portion of gross sales. The loss of one or more of these customers could reduce gross sales and negatively effect their financial condition. In particular, Walmart represents 15.9%, 18.9%, and 20.3% of total revenues in 2013, 2012, and 2011 respectively. Should Walmart fail to return as a large customer of the firm, PBH may experience significant decreases in operations and financial conditions.
- **Dependence On Third Party Manufacturers.** PBH relies on third-party manufacturers to produce the products that they sell. The ability to retain current manufacturing relationships and engage in and successfully transition to new relationships is critical to their ability to deliver quality products to customers in a timely manner. As of March, 2013, PBH has relationships with 66 third-party manufacturers. Of those, long-term contracts are established with 22 manufacturers that product items accounting for about 75.3% of gross sales in 2013. Although well diversified, without adequate supplies of quality merchandise, sales may decrease.

Management

Matthew Mannelly is the President and CEO – which he assumed in 2009 after extensive experience in the industry. Ron Lombardi was named CFO in 2010 and has expertise in acquisitions and divestitures among other qualities. Timothy Connor leads as the Executive VP for PBH focused on sales and marketing since 2011. He was appointed to this role after serving as Chief Marketing Officer for years prior for PBH, after having worked for competitors including Matrixx and Clorox.



Ownership		
% of Shares Held by All Insider and 5% Owners:		1%
% of Shares Held by Institutional & Mutual Fund Owners:		99%
		Source: Yahoo! Finance
Top 5 Shareholders		
Holder:	**Shares:**	**% Outstanding:**
Dimensional Fund Advisors LP	4,094,229	8.00%
Vanguard Group, Inc. (The)	3,007,101	5.88%
BlackRock Fund Advisors	2,615,075	5.11%
First Manhattan Company	1,735,820	3.39%
GW Capital, Inc.	1,650,323	3.23%
		Source: Yahoo! Finance

Orbotech Ltd. (ORBK)

October 25, 2013

Nicholas Kerger — International Technology

Orbotech Ltd. (NASDAQ: ORBK) engages in designing, developing, manufacturing, marketing, and servicing yield-enhancing and production solutions for the supply chain of the electronics industry. The company's Production Solutions for the Electronics Industry segment offers automated optical inspection (AOI), automated optical repair, laser direct imaging, digital printing, laser drilling, laser plotters, computer-aided manufacturing, and engineering solutions for printed circuit boards (PCBs) and other electronics component manufacturing; and AOI, test, repair, and process monitoring systems for flat panel display (FPD) manufacturing. Its Recognition Software segment develops and markets automatic check processing and healthcare revenue cycle management solutions to banks, financial and other payment processing institutions, and healthcare providers through system integrators and solution providers. The company is also involved in the research and development of products for the deposition of anti-reflective coating on crystalline silicon photovoltaic wafers for solar energy panels. Orbotech Ltd. primarily serves manufacturers of PCB, FPD, liquid crystal displays, and other electronic components worldwide. Orbotech Ltd. was founded in 1981 and is headquartered in Yavne, Israel.

				FY: Dec 31	2012E	2013E	2014E
Price (10/21/13) ($):	11.98	Beta:	0.71				
Price Target ($):	17.35	WACC	11.01%	Revenue ($, M)	$400.73	$434.92	$472.19
52WK L-H ($):	7.75 - 13.40	M-Term Rev. Gr Rate Est:	8.00%	% Growth	-41.07%	8.53%	8.57%
Market Cap ($M):	519.01M	M-Term EPS Gr Rate Est:	10.00%	Gross Margin	41.30%	42.00%	42.00%
Float (M):	36.6	Debt/Equity:	3.53%	Operating Margin	2.16%	10.00%	11.00%
Short Interest:	0.60%	ROA:	4.60%	EPS (Cal)	-$1.06	$0.93	$1.01
Avg. Vol (3M):	129,509	ROE:	6.40%	FCF/Share	$0.31	$1.16	$1.24
Dividend:	N/A			P/E (Cal)	-	12.87	11.85
Yield:	N/A			EV/EBITDA	23.62	10.20	9.50

Recommendation

After revising its revenue guidance in June 2012, ORBK's sales and earnings have been growing at an impressive pace in 2013, and are positioned to continue growing due to two industry trends: 1) Customer's desire to improve manufacturing efficiency and 2) Growing demand for smartphones and tablets. ORBK's large variety of testing and inspection equipment helps its customers optimize and improve its manufacturing processes. The demand for testing and inspection equipment continues to grow following the great recession. Firms have been looking for ways to become more efficient and productive in their processes in order to reduce costs and hedge the potential downside against future economic downturns. ORBK will continue to lead the way in testing and inspection technology as the company invests between 12-14% of its sales into R&D each year and has more than 500 awarded and patents pending. ORBK will also benefit from the growth of smartphones and tablets over the long run due to the company's market position in inspection and test equipment markets for PCB and FPD applications. The PCB market is expected to grow at roughly 8% annually over the next 5 years, while the FPD market in expected to grow to $110 billion in over the next 5 years, also at around 8% annually. The FPD industry has seen particularly large growth in Asia-Pacific, growing at a projected CAGR of 4.6% over the next 5 years. After their recent organization restructuring, most of the company's revenues coming from the Asia-Pacific region, and a strong amount of net cash holdings ($204M), ORBK is in position to capitalize on these growing trends and garner significant returns from their R&D investments. Due to these reasons and a favorable valuation, it is recommended that ORBK be added to the AIM International Equity Fund with a target price of $17.38, which offers a potential upside of 45%.

Investment Thesis

- **Increasing Demand for Global Internet Devices.** Internet device sales, fueled by tablets and smartphones, continue to increase around the globe. Smartphone sales are expected to grow roughly 70% from 1 billion units a year to 1.7 billion units a year by 2017. Tablet sales are expected to grow to 500 million units a year by 2015, over a 50% CAGR over the next few years. The upward trend in electron device manufacturing provides more opportunities for revenue streams as ORBK's tools test and perform high-end functions in the PCB market.
- **Strong Position in China.** Non-Chinese panel producers have renewed their interest in building capacity on mainland China. Chinese import taxes are giving local producers an advantage, which is beginning to stimulate potential for investment in new capacity in China by traditional panel producers in 2014 and 2015. With roughly 40% of their revenues coming from China, and ORBK's yield tools a part of all new panel construction, the increase in investment will increase ORBK's revenues.
- **Organizational Restructuring.** In July, ORBK announced the creation of two new corporate unites: Strategy and Business Development and Global Product Organization. The new Global Product Organization unit will integrate all the company's R&D activities and better align them with the demands of the Strategy and Business Development, which will focus on capitalizing on growth opportunities in new areas. The reorganization will benefit the company short run, by improving the time to market of new products, and in the long run, by establishing growth and innovation as top priorities for the future.

Valuation

To find the intrinsic value of ORBK, a five-year DCF was computed with a WACC of 11.01% and a terminal growth rate of 2%. Built into the WACC was a 1.05% country risk premium since most of their business comes from Asia. Sensitivity analysis on the WACC yielded values ranging from $11.80 to $17.96, while sensitivity analysis on the terminal growth rate yielded values ranging from $12.72 to $16.66. A P/B multiple of 2.11 was also used, yielding a $19.71 intrinsic value. Weighing both models 50%, an intrinsic value of $17.35 was derived, representing an upside of roughly 45%. The company does not pay a dividend.

Risks

- **Reliance on a Few Customers.** The FPD industry is highly concentrated with a small number of manufacturers producing the majority of the world's LCD In 2012, 55% of ORBK's total FPD revenues were derived from the three largest FPD customers. Revenues could be materially affected should ORBK lose one of those customers.
- **Cyclical Industry.** The electronic device industry is strongly cyclical and demand for the devices fluctuates with capital spending cycles of other firms. If an extended cyclical downturn occurs, ORBK's revenues could be materially affected.

Management

Asher Levy is the CEO of Orbotech Ltd. Mr. Levy brings many years of experience to his position as he has worked for Orbotech in a number of roles including President of Global Business, Executive Vice President for Business and Strategy, Managing Director of Orbotech Technology Ventures, and President of Orbotech Pacific Ltd. Doron Abramovitch is the Corporate Vice President and CFO of Orbotech Ltd. He has been with the company since April 2011 after working as a Senior Vice President and COO of Bagir Group Ltd.

Ownership

% of Shares Held by All Insider and 5% Owners:	9%
% of Shares Held by Institutional & Mutual Fund Owners:	57%

Source: Yahoo! Finance

Top 5 Shareholders

Holder	Shares	% Out
FMR, LLC	2,800,000	6.62
Fidelity Low-Priced Stock Fund	2,388,375	5.65
Price (T.Rowe) Associates Inc.	1,602,684	3.79
Oaktree Capital Management, L.P	1,400,000	3.31
Systematic Financial Management, L.P	1,206239	2.85

Source: Yahoo! Finance

Adidas A.G. (ADDYY)
October 25, 2013

Axel Sjoberg International Consumer Discretionary

Adidas A.G. (OTC: ADDYY) is a German sports retailer. The Retail Business segment comprises the own-retail and e-Commerce activities of the adidas and Rebook brands. The Other Businesses segment comprises the brands Taylor-Made-adidas Golf, Rockport, Reebok-CCM Hockey and other centrally managed brands. They have world-wide operations, with major markets in Europe (27% of sales), North America (24%), Asia (15%), European Emerging markets (12%), Greater China (11%), and Latin America (11%). As of December 2012, Adidas had approximately 41,000 employees around the world. The company was founded in 1920 and is headquartered in Herzogenaurach, Germany.

				FY: December	2012A	2013E	2014E
Price ($) (10/17/13)	55.88	Beta:	1.01	Revenue (Mil)	14,883	15,100	16,233
Price Target ($):	68.42	WACC	8.6%	% Growth	11.72%	1.46%	7.50%
52WK Range ($):	39.69-58.74	M-Term Rev. Gr Est:	4.1%	Gross Margin	49.51%	50.33%	50.00%
Market Cap:	23.38 B	M-Term EPS Gr Est:	19.0%	Operating Margin	7.96%	8.61%	10.00%
Free Float	98%	Debt/Equity	24.2%	EPS (Cal)	$1.26A	$2.02E	$2.79E
Avg. Daily Vol:	26 K	ROA:	4.6%	FCF/Share	1.44	1.66	2.79
Dividend ($):	$ 0.89	ROE:	10.1%	P/E (Cal)	26.72	27.64	20.00
Yield (%):	1.58%	ROIC:	11.1%	EV/EBITDA	9.3	10.99	9.26

Recommendation

Adidas is along with Nike the largest brands within the sports universe. Due to their economies of scale, market capitalization, and strong brand name, Adidas will remain one of the most accepted and loved sport retailers in the world for the foreseeable future. My main driver is based on the FIFA World Cup taking place in Brazil next summer. With Adidas as the main sponsor of the event, they expect additional sales of €2 B. Management has communicated "Route 2015," which is a target for FY15 where Adidas aims for €17 B in sales revenue and achieve an operating margin of 11%. Recently, the stock price has fallen, reflecting worse performance in Q3 than expected. This was as a result of three factors: First, weaker currency exchange rates compared to the EUR was seen in RUB, JPY, BRL, ARS, and off-set the growth achieved (-€40 M). Second, they experienced supply chain issues in Russia caused lost product flow to stores and estimated revenue loss of €15 M. This was a result of closing an old distribution center before their new flagship was ready to handle the Russian market. Last, the golf-market overall underperformed by high single digits (-9% YTD). For these reasons, Adidas lowered its FY13 targets to low single digit sales growth (low-mid SD), EBIT margin of 8.5% (9%), and Net Income to €820-850 M (890-920 M). However, management remain focused on achieving their goals for 2015, and see the factory problems in Russia to be resolved by the start of Q4. Additionally, Adidas launches their World Cup collection in Q4, which can create strong momentum for the stock. The issues in Q3, were in large unavoidable, and I am confident that Adidas will resolve the Russia distribution inefficiency. The lower stock price, makes ADDYY and even more attractive buy as I do not see mentioned issues to continue. In short, Adidas strong brand name, anticipated boost in revenue from the World Cup, renewed focus on margin expansion, and an attractive price makes them a great investment. For these reasons and a favorable valuation, it is recommended that ADDYY be added to the AIM International Equity Fund with a target price of $68.42, which offers a potential upside of 22.45%. The firm also pays an attractive dividend of $0.88 (1.60% yield).

Investment Thesis

- **Attractive Buy.** Adidas strong brand name and the well-known individual brands within the group will keep Adidas as one of the two largest sports retailers in the world. With a strong balance sheet, the company will be able to focus on expanding margins and operational improvement. With the Q3 issues, the company is attractively priced right now. However, management expects the operational issues in Russia to be resolved by Q4. Along with reasons below, the stock is favorably priced right now.
- **FIFA World Cup.** With the company being the main sponsor of the event, they anticipate strong sales of around €2B. We should see the company benefitting from this starting in Q4 FY13 as they launch the World Cup collection, which includes match jerseys and gear for the national teams they sponsor, official game balls, the World Cup Football Cleat, etc.
- **Route 2015.** Striving to achieve group sales of €17 B and operating margins of 11% in FY15 management has been clear on its ambitions. Main performance categories is running, basketball and outdoor, which they believe will drive profitability in the medium term. Despite issues in Q3 this year, they maintain the conviction that "Route 2015" will be a success. It will be more challenging, but with a stacked and exciting pipeline in many of the product categories and experienced management, I am convinced that Adidas has what it takes.

Valuation

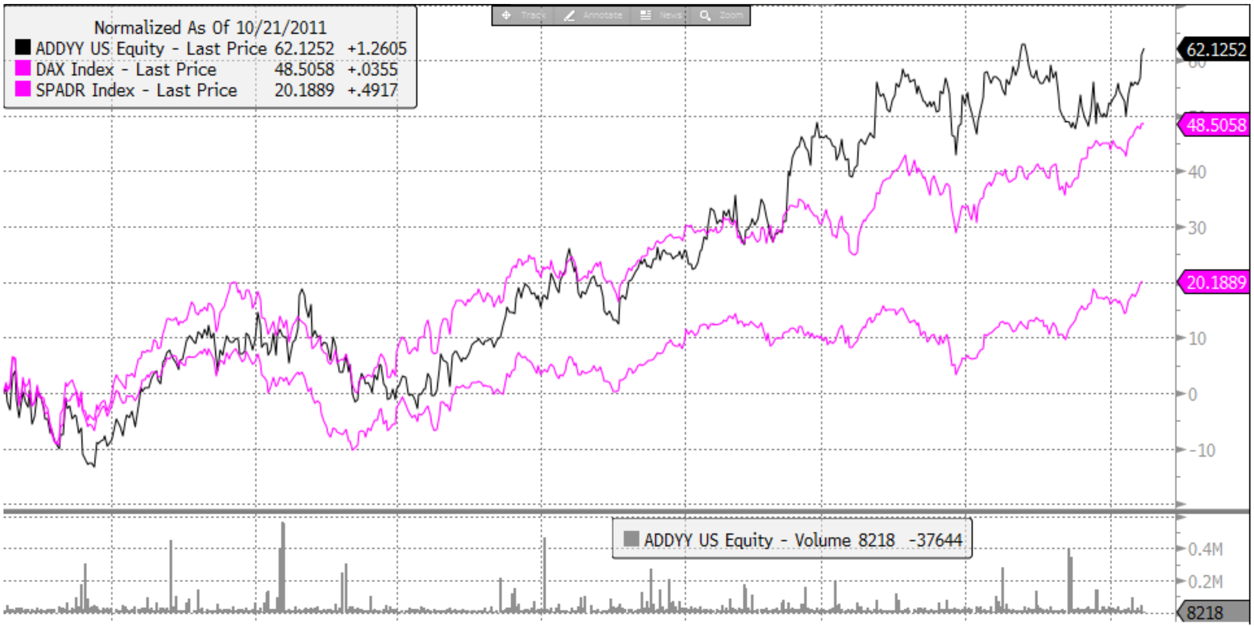
In order to reach an intrinsic value for ADDYY, a ten year discounted cash flow model was conducted. A terminal growth rate of 3% and a WACC of 8.62% resulted in a valuation of $64.59. Sensitivity analysis from a discount rate of 10% provided for a range between $60.41 and $70.17. Additionally, a relative valuation using EV/EBITDA was utilized, providing a value of $79.91. Intrinsic value was weighted 75% and EV/EBITDA 25%, resulting in a price target of $68.42 – a 22.45% upside.

Risks

- **Dependent on Economy.** While the global economy appears to have stabilized recently, there is continued uncertainty of economic recovery. Fiscal policy will drive consumer confidence and disposable income in major economies in the short term. Should the economy face unanticipated setbacks, such as a recurring European sovereign debt crisis, then demand for man of the company's products, and consequently revenues for Adidas, will suffer.
- **Further setbacks to Route 2015.** The announced setbacks in Q3 translates to increasing pressure on management to deliver in terms of margin expansion and sales growth. As long as no major additional issues occur, and they resolve the problem in the important market Russia, I believe they can achieve Route 2015. If they see any further setbacks, I believe it will be too big of a challenge and the stock price could take a hit.
- **Nike.** The main competitor has recently been stealing market share from Adidas especially in North America and Europe. Adidas are looking to respond in 2014, with attractive product launches and World Cup related sales. However, if they do not, Nike will continue to threaten to take market share from Adidas in order to position itself as a clear #1.

Management

Current CEO and Chairman of the Board since March 2001 is Herbert Heiner. German born Heiner has worked within the company for over 25 years. He also sits on the board of F.C. Bayern Munich, Lufthansa, and Allianz.



Ownership		
% of Shares Held by Institutional Owners:		50.8%
	Source: Bloomberg	
Top 7 Shareholders		
Holder	Shares	% Out
CAPITAL GROUP COMPANIES INC	14,632,128	6.99
BLACKROCK	14,512,594	6.94
THORNBURG INVESTMENT MGMT INC	10,057,706	4.81
ROYAL BANK OF SCOTLAND GROUP PLC	9,347,766	4.47
NORGES BANK	4,886,922	2.34
DEUTSCHE BANK AG	3,938,285	1.88
VANGUARD GROUP INC	3,726,800	1.78
	Source: Bloomberg	