

Applied Investment Management (AIM) Program

AIM Class of 2013 Equity Fund Reports Fall 2012

Date: November 9, 2012 | Time: 3-4:00 p.m. | Location: AIM Research Room

Student Presenter	Company Name	Ticker	Price	Page No.
Jillian Morrissey	Hain Celestial Group, Inc.	HAIN	\$57.25	2
Mark McCanna	Home Loan Servicing Solutions	HLSS	\$19.67	5
Timothy Maturo	Innophos Holdings Inc.	IPHS	\$47.91	8
Catie Collins	Sanofi	SNY	\$44.86	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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Hain Celestial Group, Inc. (HAIN)

November 9, 2012

Jillian Morrissey

Consumer Staples

Hain Celestial Group engages in the manufacturing, marketing, and sale of natural and organic products under brand names which are sold as “better-for-you” products, providing consumers with the opportunity to lead A Healthy Way of Life™. HAIN’s brands are very well diversified and recognizable to the organic, healthy shopper. With grocery products composing 68% of their revenue in 2012, HAIN also has exposure in snack lines (15%), tea (8%), personal care (8%), and fresh products (1%). In addition HAIN revenue streams from the U.S. (72%), Europe (14%), and the United Kingdom (13%) with recent acquisitions being made to move into Canada and Eastern Europe. Since HAIN’s inception in 1993, through strategic acquisitions, they have become the leading marketer, manufacture and seller of natural and organic products by anticipating and exceeding consumer expectations in providing quality, innovation, and convenience. Headquartered in Melville, NY, HAIN employs 3,720 people.

Price (\$) (11/04/12):	\$57.25	Beta:	0.85	FY: Jan	2011A	2012 E	2013 E
Price Target (\$):	\$79.39	WACC:	8.66%	Revenue (\$mil)	1108.6	1378.3	1779.3
52 WK H-L (\$):	73.72-32.85	Mid Term Rev Gr. Rate	25%	% Growth	20.84%	24.33%	29.01%
Market Cap (mil):	2587.1M	Mid Term EPS Gr. Rate	22%	Gross Margin	28.85%	27.75%	27.84%
Float (mil):	43.8M	Debt/Equity:	0.40	Operating Marg	10.03%	10.51%	10.92%
Short Interest (%):	11.66%	ROA:	6.19%	EPS (Cal)	\$1.27	\$1.79	\$2.41
Avg Daily Vol (K):	755.21K	ROE:	10.29%	FCF/Share	\$1.09	\$2.29	\$3.05
Dividen (\$):	\$0.00			P/E (Cal)	25.27	28.23	23.75
Yield (%):	0.00%						

Recommendation

With 500 million obese people worldwide today and 2.8 million deaths each year due to individuals being overweight, there is obviously a need for consumers to eat healthier food. The highest rates of obesity are in the Americas (26%) with two-thirds of all US adults being overweight or obese. To combat this serious problem a plethora of people are turning to healthy foods that are natural and organic. Since 2010 HAIN has experienced tremendous growth with net sales growing at a 24.4% CAGR alone. HAIN has created five initiatives to provide a ‘Healthy Way of Life’ and maintain the company’s competitive edge. First, HAIN has plans to reduce calories as well as sugars and sweeteners per serving in all products worldwide by 2016. Next, as part of the National Salt Reduction Initiative, HAIN will reduce sodium by 20-30% over the next two years. To clearly communicate with the consumer HAIN is continuing to improve labels for clear on-pack information. Finally, HAIN has promised to keep high standards in terms of the company’s source of natural ingredients as well as processing the ingredient minimally. HAIN has been able to build an economic moat by creating such a strong brand image which has led to them outperforming broader food peers with net sales growth of 24.3% compared to 10.3% industry average. With all the potential drivers that will be realized and with the strong financial possibilities it is recommended that HAIN be added to the Domestic AIM Fund at a target price of \$79.39 which offers a 38% upside.

Investment Thesis

- **Consumer Shift to Healthier Lifestyle** - In order to live a healthier lifestyle and combat some of the unfavorable statistics mentioned previously, there is a consumer shift towards natural and organic foods. With Net Sales growing at a CAGR 24.4%, EPS at a 58.3% CAGR and Sales/EBITDA at a 24.4% CAGR since 2010, HAIN is capitalizing on this trend. As more consumers recover with improving economic conditions, HAIN’s customer base will grow as more people are willing to pay a slight premium for much higher quality ingredients.
- **Strong Innovation and New Product Pipeline** – For 2013, HAIN has over 80 new products that will become available for sale. These products range from teas such as green, herbal, k-cups to

snacks such as sweet potato chips, veggie straws and cinnamon spice chips. In the frozen and dairy section HAIN will also release non-dairy items such as coconut milk and almond milk as well as infant and toddler items such as Greek yogurt smoothies and fish nuggets. Finally HAIN will also come out with ingredients and meal prep products as well as supplements and personal care items such as hair products and sunscreen. Combine these new products with the recent acquisitions of Daniels UK, and Cully & Sully in Ireland - which will allow HAIN to tap into new territory with market leading brand of 20 chilled products - and HAIN can expect strong growth during 2013 and on. For 2013 alone, these added products are expected to add at least \$180 million in sales which offers over a 13% increase.

- **Greater Distribution Possibilities** - Relatively low distribution levels, compared to other Consumer Packed Goods groups, present HAIN with an opportunity to increase sales through greater distribution. HAIN aims to drive average All Commodity Volume (ACV) for top 100 SKUs to over 50% from the 32% where the company is today. HAIN has recently restructured sales organizations internally to better capitalize on this growth. Instead of having regional sales team HAIN has restructured to create sales teams for each large client. This allows for better relationship management and a more effective sales effort thus will only help aid in HAIN's growth.

Valuation

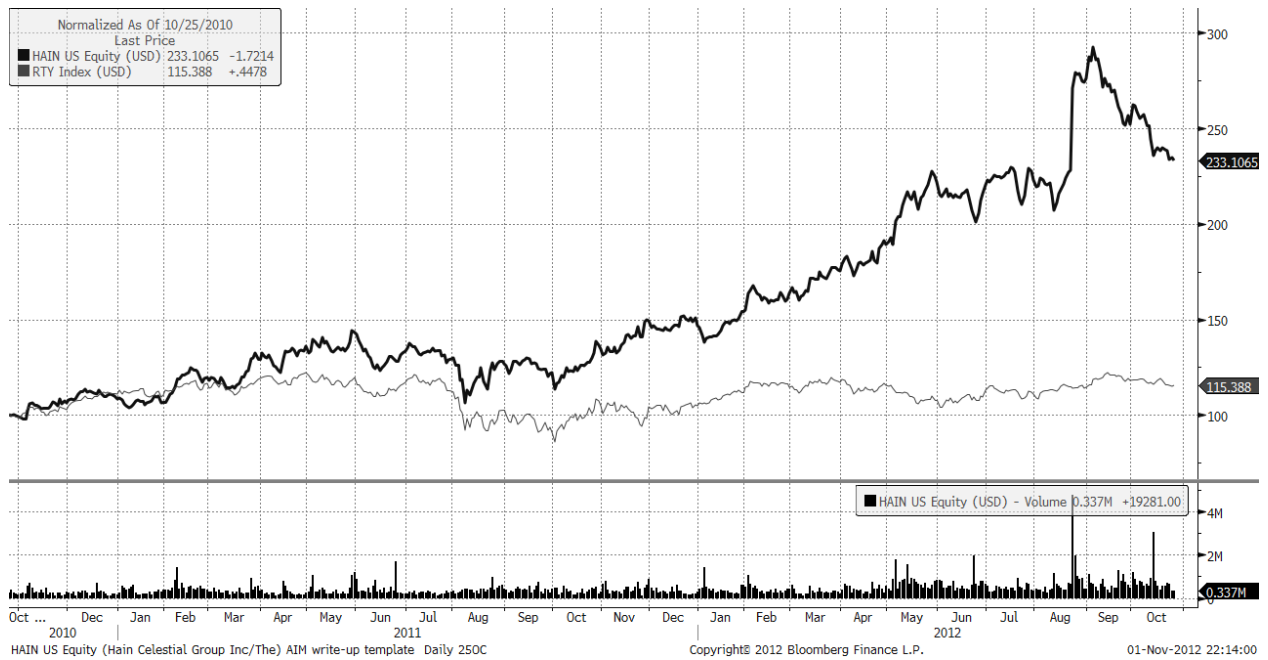
HAIN was valued using a ten-year DCF model. Based on a calculated WACC of 8.5% and perpetual growth rate of 2.50%, the DCF analysis yielded an intrinsic value of \$84.87. A sensitivity analysis was also conducted on the DCF adjusting the WACC, the long-term growth rate and next year's cash flow from. From this a target price range of \$63 to \$87 was obtained. An EV/Sales multiples approach was also conducted using a multiple of 1.88X. The approach yielded an intrinsic value of \$73.91. Weighting the DCF at 50% and the EV/Sales at 50% and intrinsic value of \$79.39 was found which offering a 38.67% upside. The company does not pay a dividend.

Risks

- **High Competition** – HAIN operates in highly competitive geographic and product markets. Numerous brands and products compete for limited retailer shelf space. HAIN's ability to maintain brand awareness while still remaining price competitive is essential to future business. HAIN needs to keep product lines and brand image in the front of competition in order to maintain this competitive edge.
- **Acquisition Integration** – With HAIN continuing to grow business through strategic acquisitions the ability to integrate brands may be difficult. Acquisitions strategy is based on identifying and acquiring brands with products that complement existing product mix as well as exposing HAIN to new geographies for the purpose of expanding business internationally. Failure to meet integration goals may weaken HAIN and the brand image the company has created.
- **Worldwide Economy**-Since HAIN has operations in diverse areas particularly in Europe the company is exposed. With weak economy consumers may shift purchases to lower-priced value offerings during the economic downturns which would adversely affect HAIN's result of operations.

Management

John Carroll has served as CEO in May 2008. Previously he held roles within HAIN such as Executive Vice President of Melville Business, President of Grocery and Frozen and President of Grocery and Snacks. Prior to coming to HAIN Mr. Carroll served as consultant to the firm providing due diligence services with respect to potential acquisitions. Ira Lamel has served as CFO since 2001 and has been the company's Corporate Secretary since 2009. Mr. Lamel is a CPA and was previously a partner at Ernst & Young LLP.



Source: Bloomberg

Ownership

% of Shares Held by All Insider and 5% Owners:	2.86%
% of Shares Held by Institutional & Mutual Fund Owners:	97.14%

Source: Bloomberg

Top 5 Shareholders

Holder	Shares	% Out
Icahn Associates Corp	7,130,563	15.78
Dimensional Fund Advisors LP	2,664,338	5.90
Vanguard Group Inc	2,288,252	5.06
Blackrock Fund Advisors	1,733,420	3.84
Goldman Sachs Group Inc	1,459,892	3.23

Source: Bloomberg

Home Loan Servicing Solutions (HLSS)

November 9, 2012

Mark McCanna

Financial Institutions

Home Loan Servicing Solutions (NASDAQ: HLSS) was formed by William Erbey, the founder and CEO of Ocwen Financial Corp. (NYSE: OCN). OCN is a mortgage servicer that manages the billing, collections, and loss mitigation activities associated with mortgage loans for parties that cannot or do not want to service their mortgages themselves. HLSS was formed to acquire and hold the mortgage servicing rights (MSRs) that OCN holds on its book. Both OCN and HLSS specialize in sub-prime and Alt-A mortgages. By selling their MSRs to HLSS, who then contracts them back to OCN to be the subservicer, OCN can significantly reduce the amount of capital that they need for their operations. OCN receives a portion of the servicing revenue while HLSS retains the rest. Management has the goal of returning 90% of HLSS's income to shareholders through monthly dividends. The remaining cash flow is used to buy more MSRs from OCN, which then further increases HLSS's income. Total servicing revenue is a function of the amount of unpaid principal balance (UPB) that the company services. HLSS had its IPO on February 28, 2012, and used the proceeds to buy \$15.2B of MSRs from OCN. HLSS ended Q3 with an UPB of \$46.5B. HLSS is headquartered in the Cayman Islands and is registered in the US as a passive foreign investment company. The firm had no operations before its IPO date.

Price(\$): (11/1/12)	\$19.67	Beta:	0.71	FY: March	2012E	2013E	2014E
Price Target (\$):	\$23.86	WACC	5.07%	Service Revenue (thousands)	\$99,987,386	\$231,794,227	\$300,473,998
52 WK H-L (\$):	12.80-19.90			% Growth	-	131.82%	29.63%
Market Cap (mil):	\$594.87						
Float (mil):	30.56	Financial Leverage	3.77	Target Price	\$23.86	\$27.07	\$30.08
Short Interest (%):	3.68%	ROA:	2.90%	EPS	\$0.78	\$1.80	\$2.33
Avg. Daily Vol:	694,289,000	ROE:	11.20%	P/E	30.73	15.04	12.89
Dividend (\$):	1.32	Match Funded Advances/Liabilities	1.156	BVPS	13.71	13.89	14.12
Yield (%):	6.80%			P/B	1.44	2.00	2.50

Recommendation

HLSS has an important relationship with Ocwen Financial Corporation, which after its most recent acquisition of servicing rights, is now the fifth largest mortgage servicer in the US and the largest non-bank mortgage servicer. An investment in HLSS provides a vehicle for the AIM portfolio to take advantage of the rapid growth that OCN is undergoing, without the high buy-in price that is associated with OCN. There is also room for further growth, as most banks are becoming wary of increased regulatory scrutiny that comes with servicing their own mortgages, and may divest many of their MSRs to third party servicers, such as HLSS. Macroeconomic trends are also positive as prepayment speeds have softened and delinquencies have decreased, which means that servicing costs have decreased, and servicers keep higher levels of UPB for longer. Based on HLSS's relationship with OCN, which gives them great control over their ability to manage earnings and growth rates, its valuation being relatively low to OCN's, and economic trends, it is recommended that HLSS is added to the AIM Equity Portfolio with a target price of \$23.86, representing a 21.3% upside. HLSS also pays a dividend that is stated to be a 90% payout ratio, which currently equates to a 6.9% dividend yield.

Investment Thesis

- **Exemption from Regulations.** HLSS thus far only bought MSRs from OCN, which benefits from offloading its MSRs to HLSS to hold. The reason for this relationship is because of HLSS's legal status. Their business operations are carefully structured so that they can rely on an exemption provided in the Investment Company Act that applies to certain structured financing vehicles. This exemption means that HLSS does not need to register as an investment company, and consequently allows them to forego the compliance and capital requirements of OCN.
- **OCN's Effective Servicing.** HLSS uses OCN to subservice the MSRs that they hold, because of this, any success that HLSS has with subservicing their MSRs, is directly correlated to the

effectiveness of OCN's servicing platform. OCN's servicing platform runs on an information technology system that has been developed over 20 years and costing \$150 million, it integrates robust modeling along with artificial intelligence that is driven by behavioral and psychological principles. Their platform is more effective than any other in the industry for effectively modifying loan terms. OCN also believes that their platform is more scalable than any other.

- **Continued UPB Growth.** HLSS's revenue stream is directly purchased from OCN, which means that the ability for OCN to provide a pipeline of UPB that they can sell to HLSS is important for future performance. As of June 30, 2012, OCN had approximately \$91.2B of UPB that HLSS intends to buy. Additionally, on October 24, 2012, OCN successfully bid for the servicing rights of a portfolio that had a UPB of \$374B. To put that into perspective, as of June 30, 2012 OCN only had \$112B of UPB on their books. This ensures that HLSS will not only have the opportunity to grow, but will have the opportunity to grow a lot. If OCN successfully transfers all of its MSR's to HLSS over a period of 5 years, HLSS's UPB could achieve a CAGR of 55.6%.

Valuation

The discount dividend model and price to book ratio approaches were used to find the intrinsic value of HLSS. The WACC for the company was computed to be 5.07%. The discounted dividend model used the most recent monthly dividends, and predicted dividends to grow by \$0.01 per share every quarter for the next ten years. The intrinsic value of the dividend approach was weighted 60%, while the P/B ratio method was weighted 40%. The initial P/B multiple used is the current multiple that HLSS is trading for of 1.44x, but it grows to 2.5x over the next two years. It is worth noting that Ocwen, even with its less efficient capital structure, has been recently trading for a P/B ratio as high as 3.0x, and a P/E ratio as high as 50.0x, and that these are levels that HLSS could also theoretically achieve as OCN tries to realize its goal of selling most or all of its MSR portfolio to HLSS to evolve into a "capital-light" fee-for-service business.

Risks

- **Dividend Tax Policy.** HLSS's high dividend payout ratio makes any future changes in dividend taxation critical for investors to consider. The current dividend taxation rate is 15%, but Congress may increase the tax rate on dividends up to 40%. While this can be problematic to management's current plan to distribute most of HLSS's income as dividends, they are not required to distribute dividends. HLSS's management may consider foregoing dividends and retaining income to grow their UPB balance to further increase revenue.
- **Counterparty Risk.** HLSS's fate is directly tied to OCN's. The MSR agreements that HLSS have with OCN are currently revenue sharing agreements, and HLSS will not gain legal control over the MSR's until various third party consents are given. These third parties include rating agencies and the trustees of the securitization trust that own the mortgages. Until HLSS legally gains control over the MSR's, a bankruptcy could wipe out any claim they have to the MSR's. A bankruptcy of OCN would immediately stall growth, as HLSS relies on them for UPB growth and mortgage servicing.

Management

William Erbey has been the Chairman and CEO of HLSS from its inception, and he is also the founder and Chairman of Ocwen. His role at the company is particularly important since OCN is HLSS's source of revenue. Before working at HLSS, all of the managers of the company were high level employees of OCN, which means that they can continue to capitalize on their expertise and close ties to OCN. Management's close ties with OCN are also important because HLSS uses software provided by Altisource, which was spun off from OCN.



Ownership

% of shares Held by All Insiders and 5% Owners:	2%
% of shares Held by Institutional and Mutual Fund Owners:	60%

William Erbey's Ownership of Related Companies

Company	Shares	% Out	Latest File Date	Net Change
Ocwen Financial Corporation (OCN)	17,775,005	13.17%	8/21/2012	-
Home Loan Servicing Solutions (HLSS)	342,245	1.12%	8/28/2012	51,000
Altisource Portfolio Solutions (ASPS)	5,935,335	25.40%	3/15/2012	4,988

Top 5 Shareholders

Holder	Shares	% Out
Capital Research Global Investor	1,296,600.00	4.24%
Wellington Management	1,047,800.00	3.43%
Cooperman, Leon	688,000.00	2.25%
FF Plaza LP	520,143.00	1.70%
Citadel Advisors	512,908.00	1.68%

Innophos Holdings Inc. (IPHS)

November 9, 2012

Timothy Maturro

Materials

Innophos Holdings Inc. (NASDAQ:IPHS) is engaged in the production of phosphate based specialty ingredients that are used in food, beverage, pharmaceutical, oral care, and industrial end markets. Applications of products include flavor enhancers in drinks, electrolytes in sports drinks, leveling agents in baked goods, and abrasives in toothpaste. Innophos has the number one market share in nearly all of their targeted specialty phosphate markets. Innophos is divided into two segments: specialty phosphate and GTSP & other products. In fiscal year 2011, specialty phosphates accounted for 87.8% of sales and 84.7% of operating income. Innophos sources its products from the United States, Canada, and Mexico and distributes its products internationally. Innophos was sold off by Rhodia (to Bain Capital) in 2004 and is headquartered in Cranbury, New Jersey. Innophos employs over 1,100 employees.

Price (\$): (11/2/12)	\$ 47.91	Beta:	1.1	FY: Dec	2011 A	2012 E	2013 E
Price Target (\$):	\$ 62.88	WACC	10.0%	Revenue (Mil)	\$ 810.49	\$ 870.62	\$ 914.15
52WK H-L (\$):	41.46-58.50	M-Term Rev. Gr Rate Est:	4.0%	% Growth	13.5%	7.4%	5.0%
Market Cap (mil):	1,050	Terminal Gr Rate Est:	2.0%	Gross Margin	22.4%	21.8%	22.0%
Float (mil):	22.00	Debt/Equity:	74.7%	Oper. Margin	16.9%	13.9%	16.0%
Short Interest (%):	2.70%	Debt/EBITDA:	0.72	EPS (Cal)	\$ 3.85	\$ 3.47	\$ 4.19
Avg. Daily Vol:	119,770	ROA:	12.06%	FCF/Share	\$ 2.77	\$ 4.54	\$ 3.87
Dividend (\$):	\$ 1.40	ROE:	20.01%	P/E (Cal)	12.46	13.82	\$ 11.44
Yield (%):	2.92%			EV/EBITDA	7.50	7.02	6.01

Recommendation

Innophos operates with a tremendous market position in the markets it operates. IPHS operates in essentially a duopoly in each of its markets competing with Israel Chemicals Limited in specialty ingredients (60% of sales), Potash Corp in food and technical grade PPA (17% of sales), and Mexichem in Technical Grade (STPP) and Detergent Grade (11% of sales). The manufacture of PPA and specialty phosphates is capital intensive and requires substantial expertise. Additionally, Innophos generates significant cash flow and substantial return on its assets. With its strong market position, Innophos has superior pricing power able to capture an operating margin in the mid to high teens. IPHS trades at a favorable EV/EBITDA multiple of 7.02 given its solid cash generation and strong market position. More than 60% of Innphos' revenues come from consumer goods providing a stable source of volume. Because of a strong product portfolio and a favorable valuation, it is recommended that Innophos be added to the AIM Equity Fund with a target price of \$62.88, which offers a potential upside of 31.2%. Innophos pays a \$1.40 dividend with a 2.92% yield.

Investment Thesis

- Expanding Margins.** Innophos should experience raw material cost savings in the next fiscal year. In addition, improving margins in GTSP will provide a tailwind in fiscal year 2013. Planned outages and facility improvements in 2012 should drive incrementally improved margins in 2013. In the long-term, management has focused upon specialty consumer products which are higher margin in nature (from ~30% of sales in 2006 to ~60% in 2011). These specialty ingredients are generally highly engineered for specific applications for customers, and generally are a small percentage of the cost of the final product (<1%). Finally, management has focused upon shorter material sourcing contracts which generally lowers the materials cost lag from around 12 months to 3-6 months.
- International Growth Opportunities.** While Innophos has tremendous market share in North America, international markets provide tremendous opportunities (exports ~20% of sales). North America represents only ~30% of the global specialty phosphate market. In August 2011,

Innophos established its first local presence outside of North America just outside of Shanghai, China. This facility will create phosphate solutions for the food industry in China and the rest of Asia. Segments of these markets are growing from 8% to 18%. The local presence of Innophos will accelerate Innophos' exports to Asia. Commercial sales are expected to begin first quarter 2013.

- **Bolt on Acquisitions.** Innophos acquired Kelatron and AMT in Oct 2011 and July 2012, respectively. These acquisitions give Innophos a leadership position in the attractive bioactive mineral ingredients market. This market is estimated to be growing in high single digits, with key applications including nutritional food & beverages and dietary supplements. Kelatron and AMT contribute \$30 million in revenue at similar margins to existing specialty ingredients. This growth was acquired at a reasonable acquisition multiple of ~7.0-8.0x. Future bolt on acquisitions can provide Innophos with terrific growth into new product areas.
- **New Phosphate Applications.** Innophos has been successful in creating new applications and innovations around their products. For example, Innophos' new leveling agent, CAL-RISE allows a reduction of sodium content in baked goods by as much as 30%. New product innovation will drive volume growth in the future.

Valuation

To find the intrinsic value of Innophos, a ten-year DCF was conducted. Revenue growth of 4.0% was used from 2014-2023. A WACC of 10.0% was used and yielded an intrinsic value of \$61.67. A sensitivity analysis was conducted to account for variations in WACC (9%-11%) and revenue growth (1% - 6%), which yielded a price range of \$48.18 - \$78.22. A forward PE ratio of 15x was used, which gave a value of \$62.83. Additionally, an EV/EBITDA valuation was conducted with a multiple of 8.2x which yielded an intrinsic value of \$66.57. Combining these three methods with 60% weighting on the DCF, 20% on the PE, and 20% on the EV/EBITDA, a composite price of \$62.88 was determined representing a 31.2% upside. A dividend of \$0.35 is paid quarterly.

Risks

- **Regulation.** Innophos' operation involves the use, handling, processing, storage, transportation and disposal of hazardous materials. In addition Innophos' products are ingredients in foods, nutritional supplements, and pharmaceutical excipients. Innophos is subject to extensive regulatory requirements set forth by the EPA, FDA, and other regulatory authorities. Failure to comply with these regulations may result in fines or litigation.
- **Pricing Competition.** In the event overcapacity exists in the market, Innophos may face substantial pricing pressures. Innophos may also experience price competition from import competition. Major customers may utilize this competition to pressure Innophos' prices. Periods of low energy costs will also benefit Chinese producers utilizing a "thermal" method. The "thermal" process is more energy intensive than the "wet" process Innophos utilizes. This would lower their marginal cost and may lead to pricing pressure.
- **Price of Input Costs.** Raw materials are purchased under supply contracts that vary from long term multi-year supply agreement to annual agreements. Pricing is set by formulae dependent upon market prices. The price Innophos pays generally lags the underlying market prices. As a result volatility in input costs may have a negative effect upon IPHS's income statement. In addition a shortage of key inputs could pressure margins.

Management

Randolph Gress is Chairman of the Board, Chief Executive Officer, President and Director of Innophos. Mr. Gress joined Rhodia in 1997 and became Vice President and General Manager of the sulfuric acid business. He was named global President of Specialty Phosphates in 2001. Mr. Gress earned a B.S. in Chemical Engineering from Princeton University and an M.B.A. from Harvard Business School.



Ownership

% of Shares Held by All Insider and 5% Owners:	7%
% of Shares Held by Institutional & Mutual Fund Owners:	94%

Source: Yahoo! Finance

Top 5 Shareholders

Holder	Shares	% Out
Neuberger Berman LLC	2,214,157	10.16
NFJ Investment Group	1,267,807	5.82
Vanguard Group Inc.	1,211,684	5.56
Fiduciary Management Inc.	1,197,060	5.49
Fidelity Management & Research	1,147,240	5.26

Source: Bloomberg

Sanofi (SNY)
November 9, 2012

Catie Collins

International Healthcare

Sanofi (NYSE: SNY), formally Sanofi-Aventis, is a global and diversified health care leader engaging in the discovery, development, and distribution of therapeutic solutions focused on patients' needs. SNY operates under three main business segments: Pharmaceuticals (84%), Vaccines (10%), and Animal Health (6%). Within these segments SNY has carefully diversified their portfolio through seven growth platforms: diabetes solutions, human vaccines, innovative drugs, consumer healthcare, emerging markets, animal health, and the newly acquired Genzyme unit. SNY is well positioned to ward off competition through their commercial presence in over 100 countries and product availability in 170 countries. SNY's strong balance of currently marketed drugs, along with a solid pipeline of new drugs, allows diversified geographical sales throughout the US (30%), Europe (26%), and Rest of the World (44%). SNY was founded in 1970 and is headquartered in Paris, France. They have over 113,500 worldwide employees.

Price (11/1/12) (\$):	44.86	Beta:	1.07	FY: Jan 31	2012A	2013E	2014E
Price Target (\$):	58.13	WACC	11.68%	Revenue (\$, M)	\$46,491	\$47,489	\$48,766
52WK H-L (\$):	45.72-31.61	M-Term Rev. Gr Rate Est:	15.0%	% Growth	8%	11%	14%
Market Cap (\$, B):	116.88	M-Term EPS Gr Rate Est:	23.0%	Gross Margin	67.35%	70.00%	70.00%
Float (B):	2.36	Debt/Equity:	27.38%	Operating Margin	22.46%	24.00%	24.00%
Short Interest:	0.11%	ROA:	6.14%	EPS (Cal)	\$5.89	\$5.14	\$6.33
Avg. Daily Vol (B):	2,032	ROE:	10.42%	FCF/Share	4.82	5.36	5.95
Dividend:	\$1.69	Financial Leverage	1.70x	P/E (Cal)	14.26	11.22	11.01
Yield:	3.90%			EV/EBITDA	8.11	8.22	7.74

Recommendation:

Following a challenging patent cliff through 2013, SNY's strategy to move away from traditional drug markets toward less patent-sensitive areas should provide a hedge against the current volatility of long term growth within the market. With over \$45B in revenues projected for 2012, 11 drugs in clinical trial Phase III, and growth platforms rising 6.4% in 3Q12, SNY is well positioned to support its operations in the future. SNY currently maintains a carefully diversified portfolio, meeting the needs of patients facing a wide range of illnesses from cancer to influenza. Alongside this diversification, the recent acquisition of Genzyme provides SNY with a dedicated research team in the U.S. This supplies links to the biotech industry and two additional 2013 potential drug launches, Lemtrada for multiple sclerosis and Mipomersen for cholesterol. Genzyme allows SNY to address biologic rare-disease drugs as well, which holds strong pricing power that will drive steady gains for several years. Despite the expiration losses that are likely to pressure gross margins throughout the industry, SNY will fight competitor R&D pipelines due to their extension into markets such as animal health and travel/endemic vaccines along with emersion into developing markets. As these markets are being spurred by rising standards of living and growing government spending, SNY will increase added patients drastically. As a result of these diverse growth opportunities, it is recommended that SNY be added to the AIM International Equity Fund with a price target of \$58, providing a 30% upside. Additionally, the company offers a 3.90% dividend yield.

Investment Thesis:

- **Blockbuster Diabetes Drug Lantus.** SNY's strong profit margins are attributed to their long-acting human insulin analog, Lantus. With revenue growth in Q312 up 18% YoY, Lantus currently exhibits a 1.7% reduction in sugar levels, while competing products are currently exuding a reduction rate of 1.1%. Lantus is also produced differently than many chemically produced medicines, utilizing E-coli bacteria to produce insulin, a methodology that generic

competition will struggle to mimic. With 366M people currently living with diabetes and an expected 552M before 2030, SNY is strongly committed to improving diabetes management through this integrated treatment.

- **Expansion into Emerging Markets.** According to forecasts from IMS Health, the value of the global drug market is projected to grow 3-5% in 2012, from an indicated \$880B in 2011. SNY's leading position in emerging markets will not only offset patent losses in developed markets, but allow them to significantly benefit from this growth. With aggregate sales expected to advance at a CAGR of 13-16% over the 2011-2015 period, these markets have the potential to carry operating margins around 40%, which is comparable with SNY's current margins.
- **Robust Pipeline and Wide Economic Moat.** SNY's existing product line currently boasts several top-tier drugs, while maintaining an extensive late-stage pipeline as well. With the recent FDA approval of Aubagio for multiple sclerosis and Zaltrap for colorectal cancer, along with a wide line up of orphan drugs, vaccines, animal health, and consumer health, SNY maintains an aggressive business model. With a current pipeline of over 60 drugs that each average a development cost of over \$800M, SNY's large economies of scale derives the necessary cash flows needed for development.

Valuation

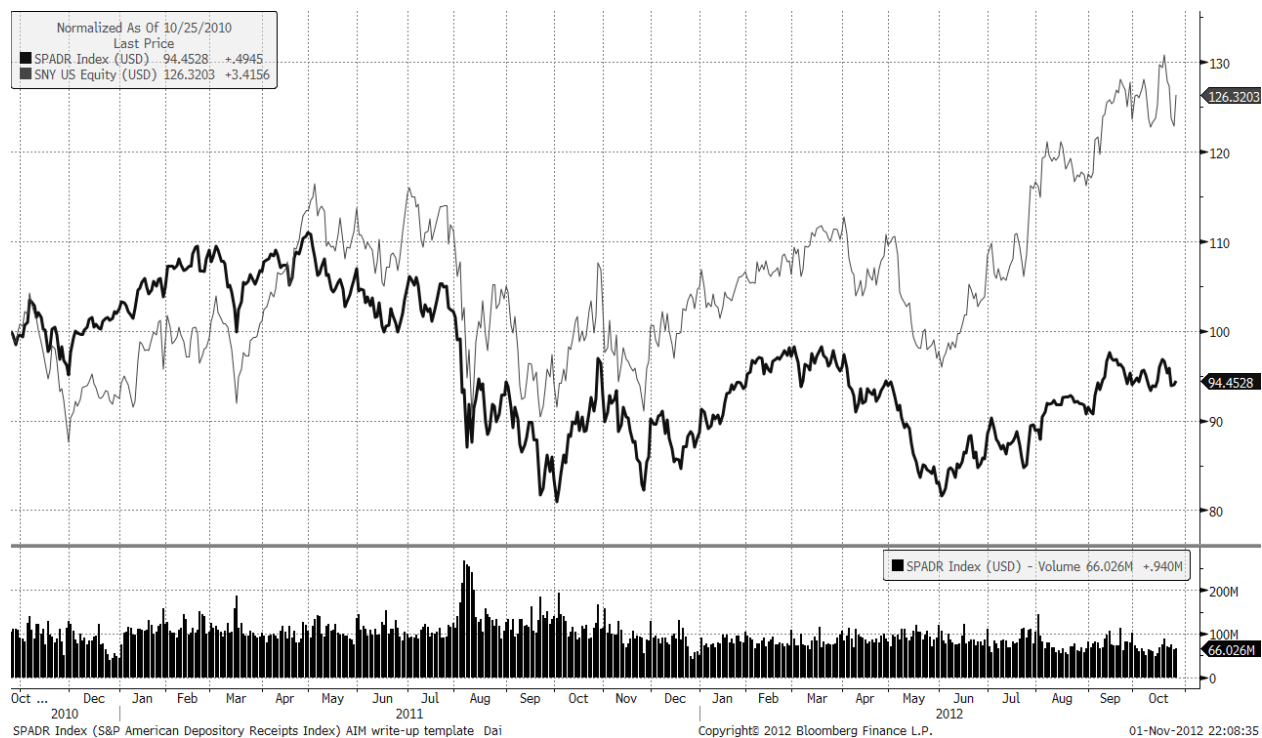
SNY was valued via a five-year DCF analysis in combination with an EV/EBITDA multiple. Based on a calculated WACC of 11.68% and a terminal growth rate of 2.5%, the DCF analysis yielded an intrinsic value of \$60.66. In addition, an 8x EV/EBITDA multiple approach was used, generating an intrinsic value of \$50.55. Weighting the DCF (75%) and EV/EBITDA (25%), a final price target of \$58 was obtained – representing in a potential upside of 30%.

Risks

- **Aggressive Generic Competition.** SNY's products are subject to generic competition in the future as product patents continue to expire. Pediatric exclusivity to Aprovel and Plavix, flagship products that combat blood pressure and prevent blood clots, expired in the United States in March and May 2012, respectively. Following this, the U.S. market exclusivity of Eloxatin expired in August 2012. Approval and market entry of new generic products reduce SNY's sales prices and volumes, adversely affecting operations and financial conditions.
- **Increase in Consolidated Debt.** After digesting the acquisition of Genzyme in February 2011, SNY financed the \$20B acquisition price with a significant amount of debt. Although SNY has already achieved a partial deleverage of the debt incurred, they make significant debt service payments to their lenders. This could limit the ability to engage in new transactions that currently rest in their R&D pipeline.
- **Globalization of Business Units.** Among the pillars of SNY's overall strategy is expansion into Emerging markets. Efforts to expand sales into these markets expose SNY to more volatile economic conditions, political instability, exchange controls, etc. This exposure could impair the current growth opportunities that exist in these markets.

Management

Chris Viehbacher has served as CEO of SNY since 2008. Following his appointment, SNY altered their capital decisions, which included eliminating low probability projects, while focusing on higher pipeline drugs. Viehbacher brings strong management credentials, with 20 years of experience at GlaxoSmithKline. CFO, Jerome Contamine, has served as CEO since 2009, previously serving as the Senior Executive VP of Finance of Veolia Environnement.



Ownership

% of Shares Held by All Insider and 5% Owners:	N/A
% of Shares Held by Institutional & Mutual Fund Owners:	N/A

Source: Bloomberg

Top 5 Shareholders

Holder	Shares	% Out
Dodge & Cox Inc.	48,554,120	1.84
Fisher Investments, Inc.	13,970,779	0.53
NWQ Investment Management Company, LLC	13,631,387	0.52
Franklin Resources	12,338,711	0.47
Invesco Ltd.	10,185,701	0.39

Source: Bloomberg