Applied Investment Management (AIM) Program

AIM Class of 2010 Equity Fund Reports
September 23, 2009

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Amedisys, Inc.
AMED
Price: $42.26 ($25.20-59.24)
Fiscal Year Ends: December 31

September 17, 2009
Russell 2000 Index: 600.03 (342.57-761.78)

Anne Mongoven
Healthcare Sector

Amedisys, Inc. (AMED) is a leading provider of home health services to the chronic, co-morbid, aging American population. AMED offers high-quality services and is a low-cost alternative to hospitals, nursing homes and other health care alternatives. AMED provides skilled nursing, pediatric care, rehabilitation care, disease management and home health aide care. AMED has two segments: home health (95% of revenue) and hospice care (5% of revenue). Incorporated in Baton Rouge, Louisiana in 1982, AMED has expanded to own and operate 480 Medicare-certified home health agencies and 48 Medicare-certified hospice agencies, as well as manage the operations of 4Medicare-certified home health and 2 Medicare-certified hospice agencies, in 38 states within the U.S., the District of Columbia and Puerto Rico.

Recommendation

AMED can use health care reform to its advantage as home health services provide a more cost efficient alternative to care than that of facility-based/acute hospitals. Specifically, the government's proposals focused on keeping the elderly in their home longer and providing better care management suits AMED's business model. Additionally, aging baby boomers will require home health services as they become part of AMED's target demographic in 2011. 2Q09 boded well for AMED as EPS increased 28% with revenue increasing $36M. The strong quarter is attributed to (1) growth in volume, an (2) improvement in performance of recent acquisitions and (3) operational efficiencies brought about by a strategic plan to lower expenses. AMED generates significant FCF ($160M in 2008) attributed to low CAPEX, as the firm does not require significant office space or medical equipment. I recommend the addition of AMED to the AIM Equity Fund with a target price of $53.00.

Key Statistics	Sept. 17, 2008
Market Cap	$1,187.60M
Shares Outstanding	27.78M
Ave. Volume (3 month)	1,090,360
Adjusted Beta	1.02
EPS (TTM)	$4.13
2009 Estimated EPS	$4.85
P/E (TTM)	9.55
PEG Ratio	0.46
WACC	8.60%
Debt/Assets	22.31%
ROE	17.19%
ROA	10.46%
Gross Margin	52.62%
Operating Margin	13.23%
Dividend Yield	0.00%
Analyst Coverage	17
Target Price	$53.00

Source: Bloomberg

Investment Thesis

- **Growth: Acquisitions, Start-Ups and Organic**. AMED has a record of successful acquisitions, accurately identifying targets that fit its framework and increase revenue. Its largest acquisition to-date, TLC Health Care Services, Inc. (TLC) in 2008 added 92 home health and 11 hospice agencies. 2Q09 saw mature home health agency margins lower than prior periods due to the TLC inclusion indicating future positive accretion. AMED has a total of 150 start-ups in its pipeline with a 2009 target of 40 new home health locations. Internal growth is driven by continued quality care, referral relationships, and attracting and retaining skilled, experienced employees. AMED posted a 19% 2Q09 organic growth rate figure and forecasts a 15% range for 2009, noting

TLC as the reason for slower same-store revenue growth as they continue to solidify their processes.

- **Hospice Care Potential.** According to the Center for Medicare and Medicaid Services (CMS), the number of Medicare beneficiaries utilizing hospice services is expected to increase 9% per year through 2015. 2Q09 demonstrated strong margins for hospice (28%) which management attributed to TLC's strong hospice locations. Management also voiced optimism that its margin will continue to add to bottom line figures. AMED opened one hospice agency this year and is targeting five startups for 2009. Although hospice care is not AMED's primary business segment, management notes it offers an attractive growth opportunity.
- **Aging American Population.** AMED's typical home health patient is 82 yrs old, takes approx. 12 different medications per day and has multiple co-morbidities. Future health care reform will have a hard time restricting such patients of seemingly required care. In 2004 36.6M people were Medicare eligible at 65yrs+ and estimates it will more than double to 86.7M by 2050 (baby boomers peaking in 2011). The CMS projects health care expenditures to outpace GDP growth over the next decade from 15% GDP today to 20% by 2016. This statistic is favorable to AMED as it continually looks to gain market share through health care consolidation.

Valuation

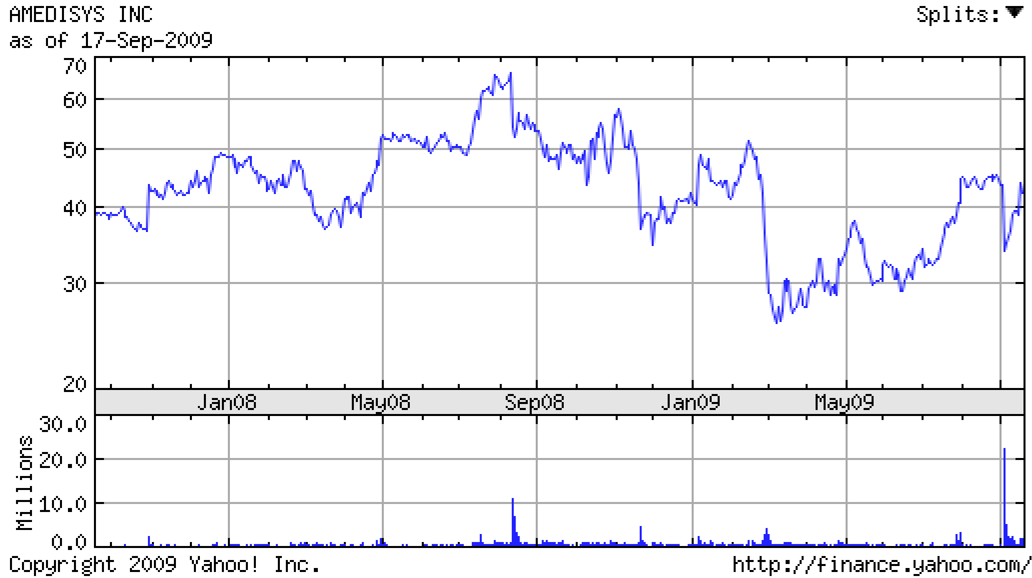
A blended P/E multiples approach using a conservative P/E of 11x 2010 EPS yields a price of $53.58. Based on a 10 year DCF analysis with a WACC of 8.60% and a terminal growth rate of 3%, an intrinsic value of $53.14 was obtained. The DCF assumes a 25% growth rate in 2009 based on management guidance from Q2 earnings call and 12% in 2010 attributed to continued acquisition integration strategies. A sensitivity analysis that adjusts both the long-term growth rate (2-4%) and the WACC (7.60-9.60%) generates a price range of $46.46-89.85. With the stock currently trading at $42.26, the $53.00 price target would yield a 25.41% return.

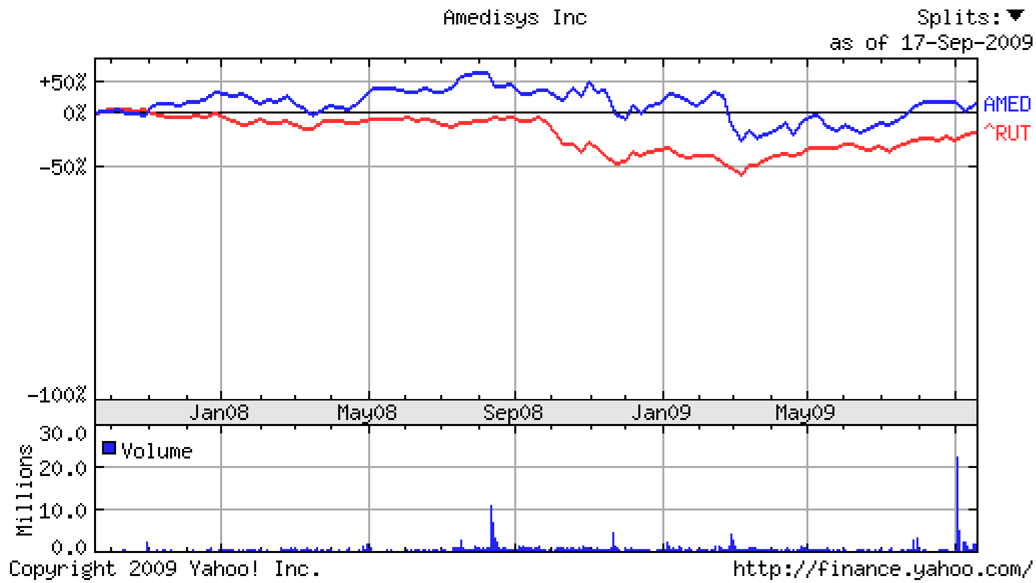
Risks

- **Reliance on Medicare.** The CMS is expected to release the home health payment proposal for CY2010 in the coming weeks. AMED derives approx. 87% of its revenue from Medicare and major changes could greatly reduce AMED's profitability.
- **Management Vacancies.** The recent resignation of Larry Graham and Alice Ann Schwartz could negatively impact AMED in the short term. Graham is a highly regarded senior manager in the home health industry, viewed as one of the best, and has been with AMED for 13 years. His departure leaves AMED with big shoes to fill. The street speculates differences in strategic direction between Graham and the board of directors prompted his resignation.
- **Few Barriers to Entry.** AMED competitors are local privately-owned, hospital-owned and non-profit health care providers. The non-profit organizations receive tax advantages and charitable contributions, which are unavailable to AMED. AMED depends on acquisition and integration strategies to gain market share and lagging in these areas would adversely affect business.

Management

Bill Borne founded AMED in 1982 and assumed the role of Chairman and CEO since its inception. Borne will assume COO and President responsibilities while the firm launches a national search to replace former President and COO Larry Graham.





Ownership

% of Shares Held by Insiders:	2%
% of Shares Held by Institutional & Mutual Fund Owners:	113%

Source: Yahoo! Finance

Top 5 Shareholders

Holder Name	Shares Held	Percent of Share Outstanding
FMR LLC	1,988,990	7.27%
Barclays Global Investment UK Holdings Ltd	1,808,434	6.61%
Times Square Capital Management	1,409,065	5.15%
Vanguard Group, Inc.	1,250,135	4.57%
Earnest Partners LLC	1,235,729	4.52%

Source: Yahoo! Finance

Black Box Corporation
BBOX
Price: $27.50 ($16.24-39.53)
Fiscal Year Ends: March 31

September 15, 2009 Rob Mitchell
RUSSELL 2000 INDEX ($342.59 - 761.78) Hardware Sector

Black Box Corporation is a provider of networking products and services for voice and data communication systems. Their products include modems, routers, switches, data storage, testing equipment, cables, and training devices. The services they provide include design, installation, monitoring and maintenance of voice, data and integrated communications systems. They offer clients a single source option to meet all of their networking needs and are a leader in the network infrastructure market estimated at about $60 billion globally. A majority of their revenue comes from corporations, schools, and government agencies in North America. However, they are currently serving over 175,000 clients in over 140 countries and have exposure to all major industries. They manufacture many of their own products under the Black Box brand, and also provide many other solutions that come from original equipment manufacturers when it is more efficient. They have several strong partnerships in place with large communication system providers such as CISCO, NEC, and Polycom that enable them to fulfill their client needs for complex communication systems. Originally founded in 1976, the company has gone through a couple of mergers and had its IPO in 1992. The company is headquartered in Lawrence, Pennsylvania and currently has over 4,500 employees.

Recommendation
BBOX is a well established leader in the network infrastructure market and has a strong business model that gives them an advantage over their competitors. Over the last 4 years they have increased sales by nearly 17% CAGR and are just under $1billion in annual sales. Even in a tough economic environment, they were able to make a few small acquisitions during their last fiscal year that helped increase in net income by15.5%. Earnings will continue to grow due to increased spending by government agencies and schools as well as further market penetration. Their relative valuations are at extremely low levels even as they continue to improve operating cash flows. With the expectations for continual growth and cheap relative valuations, it is recommended that BBOX be added to the AIM Equity Portfolio with a target price of $36 yielding a 30% return. They do pay small annual dividend of $0.24

Key Statistics	Sept. 17, 2008
Market Cap	$482M
Shares Outstanding	17.5M
Ave. Volume (3 month)	153,565
Adjusted Beta	1.21
EPS (TTM)	$2.59
2010 Estimated EPS	$2.78
P/E (TTM)	10.61
Price/Book	0.72
WACC	10.00%
Debt/Assets	20.91%
ROE	7.00%
ROA	4.10%
Gross Margin	35.73%
Operating Margin	8.00%
Dividend Yield	0.90%
Analyst Coverage	3
Target Price	$36.00

Source: Bloomberg

Investment Thesis

- **Increased Public Sector Spending**. A significant portion of Black Box's revenue comes from schools and government agencies. As a result of recent stimulus efforts, the company will benefit from increased spending from some of their top customers. The education sector will receive $48 billion from the stimulus plan, of which a portion will be used towards network upgrades and modernization programs by many public schools and universities. Government agencies will also increase spending on communication systems and Black Box has already been awarded multiple contracts with the U.S.

government. Revenues should continue to remain strong from the Healthcare industry as customers continue to update their networks.

- **New Customers.** Black Box is a U.S. market leader in "one stop shops" for communication system networks due to their size and quality. Their expansive product base gives them the capability to fulfill all of their customers' needs. They offer onsite services such as installation and technical support for all of the products they provide. This gives them an advantage over smaller competitors who are typically either regional or specialized and are only able to provide solutions for some of the market's needs. Some of these competitors have not been able to financially survive the recent economic conditions. Using their business model as a competitive advantage, they will to continue to gain new customers in the networking infrastructure market.
- **Financial Flexibility.** Over the last 5 years they have an average revenue growth of 13.3%. In fiscal year 2009 they were able to increase net income by 15.5% up to $45.3 million. Black Box has a long history of income growth that has been assisted by successful acquisitions. Recent acquisitions' such as Scottel Voice & Data, Inc and ACS Communications, Inc will continue to expand their sales network and customer base. They currently have a healthy balance sheet, sufficient operating cash flows, and a revolving line of credit of $300 million giving them financial flexibility. As a result of this flexibility, they will have the ability to continue their success of acquiring small competitors that would benefit the organization.

Valuation

BBOX is currently trading around 11 x their TTM EPS of $2.59. Using a conservative P/E multiple of 13 x a 2009 EPS estimate of $2.78 yields a $36 price target. A 5year DCF analysis with a computed WACC of 10% and a terminal growth rate of 3%, an intrinsic value of $36.92 was obtained. A sensitivity analysis that adjusts both the long-term growth rate (2.5% - 3.5%) and the WACC (9-11%) generated a price range from $31-$46. The price target was set at $36 which would yield a 30% return for the stock currently trading around $27 in addition to a 0.9% dividend yield.

Risks

- **Legal Issues.** In 2006, a lawsuit was filed against the company claiming an executive improperly backdated stock options for several years starting in 1996. The executive is no longer with the company and current management believes costs are adequately already provided for. However, it is still possible they may incur additional expenses related to this matter.
- **International Risk**. Over 20% of revenues are generated from outside of the U.S. The company is subject to changes in foreign laws, regulations, and political instability that could substantially hinder their operations. In addition to these uncertainties, they are also exposed to fluctuations in currencies. While they take measure to mitigate these risks by entering into currency contracts, they have experienced losses in the past and could incur them again in the future.
- **Dependent on successful integration of Acquisitions.** While past acquisitions have proved successful, there is no guarantee that recent or any future acquisitions will financially benefit the company. If they are unable to successfully integrate companies into their organization, it will affect their future earnings potential.

Management

Black Box has a young management team (average age of 52) with significant industry experience. Terry Blakemore, the current President and CEO, has been working with the company since 1999. He spent numerous years in their business development and was responsible for several successful acquisitions. Michael McAndrew has served the company for over 19 years, becoming the CFO and Vice President in 2002.

Ownership

% of Shares Held by Insiders and 5% Owners:	.1%
% of Shares Held by Institutional & Mutual Fund Owners:	99.9%

Source: MSN Money

Top 5 Shareholders

Source: MSN Money

Holder Name	Shares Held	Percentage of Share Outstanding
Fidelity Management & Research	2,009,225	11.5
Fidelity Low-Priced Stock Fund	1,981,025	11.3
Dimensional Fund Advisors, LP	1,521,629	8.7
Barclays Global Investors	1,242,270	6.9
Vanguard Group	889,165	5.1

Bally Technologies Inc.

Price: $39.02 ($12.21-$42.58)
Fiscal Year Ends: June 30

September 17, 2009 Matthew Pruyn
Russell 2000: 615.47 (342.59-761.78) Business Services Sector

Bally Technologies (BYI) is a leading manufacturer and supplier of casino gaming machines and information systems. The company consists of two business segments, the Bally Gaming Equipment and Systems segment and the Rainbow Casino. Bally's Gaming Equipment and Systems division makes slot machines and video gaming machines for an industry that includes casinos, racinos, video lottery, central determination and Class II markets. BYI's gaming systems (24% FY09 revenue) includes the sale of specialized software designed to track activity on the casino floor. Specifically, the company operates more than 300,000 game monitoring units installed worldwide at more than 225 locations. In addition, the company owns and operates Rainbow Casino in Vicksburg, Mississippi (4% FY09 revenue). The company was founded in 1968 and is currently headquartered in Las Vegas, Nevada.

Recommendation

Within only a few years, management has been able to turn Bally Technologies into one of the dominant suppliers for the casino industry. Through its innovative product offerings, Bally has been able to gain considerable market share from industry leader IGT. Despite the difficult operating conditions, Bally reported EBITDA increased 10% to $300M in FY09 (versus $282M FY08). Bally offset weaker demand through cost cutting, increased prices and sale of higher-margin gaming conversion kits. In addition, Bally's gaming operations business has outperformed its competitors due to pricing model. The majority of its gaming operation revenue (17% YOY increase) is derived from a fixed-fee, which is why Bally is less sensitive to the decline in consumer spending. Also, management expects the replacement cycle to regain steam in calendar 2010. Management also indicated that its systems pipeline is at a record high, which will translate into increased sales activity in 2Q10. Furthermore, the expansion and legalization of gaming in new jurisdictions will create solid revenue opportunities for Bally Technologies. As a result, this stock would be a valuable addition to the portfolio because the target price of $46 represents a potential gain of approximately 18%.

Key Statistics	Sept. 14, 2009
Market Cap	$2,231.91M
Shares Outstanding	54.61M
Ave. Volume (3 month)	820,795
Adjusted Beta	1.64
EPS (TTM)	$2.22
2010 Estimated EPS	2.40
P/E (TTM)	18.50
PEG Ratio	.85
LT Debt/Equity	32.47%
WACC	13.2%
Forward P/E	17.54
ROE	33.25%
ROA	14.11%
Gross Margin	61.09%
Operating Margin	23.97%
Analyst Coverage	13
Target Price	$46

Source: Bloomberg

Investment Thesis

- **Legalization of Gaming in New Jurisdictions**. In order to narrow budget deficits, more states have been forced to legalize gaming. In July, Illinois Governor Pat Quinn approved the legalization of video poker machines at bar, restaurants, vet halls, and truck stops. Specifically, the bill enables the installation of up to 5 video gaming terminals in approximately 15,000 establishments. Given BYI's market share (21%), this legislation alone could boost EPS by over $.40. In addition to Illinois, Bally plans to capitalize on new opportunities in OH, KS, IA, MD and MA.

- **International Sales.** Bally's international sales (16 %of sales FY09) have grown substantially and continue to be a high priority for the company as part of its long-term growth strategy. In a period of only two years, BYI has increased international sales by more than 77%. ($141.9M vs. $80M). Bally Technologies success overseas is important because it has helped offset the sluggish replacement cycle currently in the U.S. Bally continues to penetrate new and existing markets in South Africa, Eastern Europe, Macau, and Australia.
- **Product Development.** Through its innovative product offerings, Bally continues to increase its installed base of machines. As a result, Bally' revenue from its gaming operations has reached an annual record of $275M (17% YOY increase). Furthermore, BYI has drastically improved its market share (21%) and continues to gain share from chief rival International Game Technology. Bally reported replacement sales of 2,850 for 4Q09, which was notably higher than IGT's result of 2,300 replacement units.
- **Strong Systems Pipeline.** Bally's systems division (24% FY09 revenue) continues to be a main driver for the company and remains critical toward its long-term growth strategy. Over 60% of the largest casinos use Bally's software to track player activity on the casino floor. Management noted that its system pipeline began to build in April and is now at record levels. In addition, several of the company's sales have been to casinos that were dissatisfied with competitors' systems. Bally also indicated that these systems are now gaining popularity in international markets, which will also serve as a catalyst for future growth.

Valuation

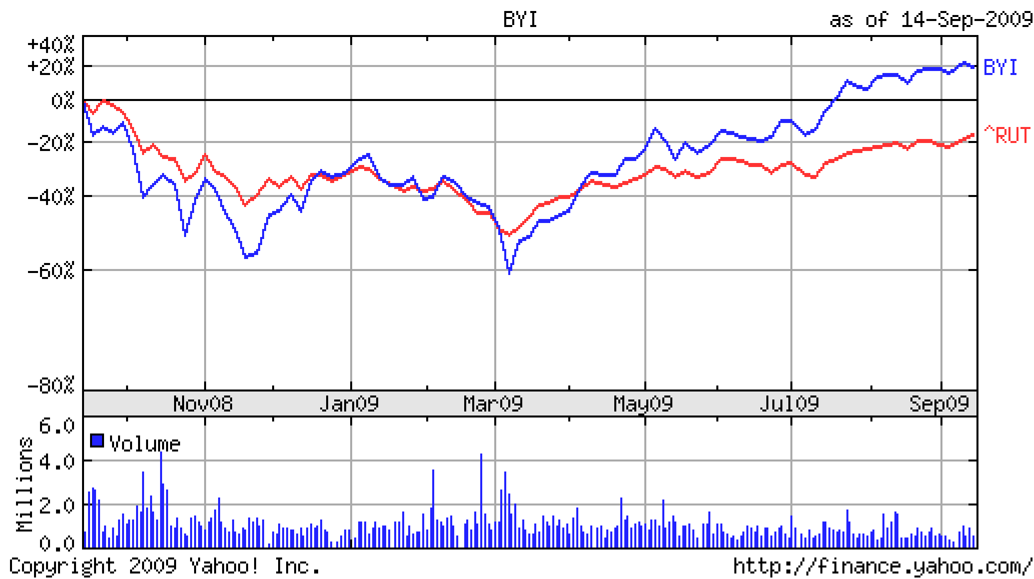
Based on a 10 year DCF model with a computed WACC of 13% and a terminal growth rate of 3%, the model yielded an intrinsic value of $46.16. Adjusting for WACC and terminal growth assumptions, a sensitivity analysis yielded a price range of $40.24 -$51.93. Additionally, BYI is currently trading at 18xTTM EPS of $2.22. A conservative historical P/E ratio of 21 times the 2009 EPS estimate of $2.40 implies in a $50.40 share price. With all metrics taken into account, a target price of $46 has been established, implying a 17% upside.

Risks

- **Highly Cyclical Industry.** A prolonged decrease in consumer spending on leisure activities is detrimental to the casino industry. As a result, the replacement cycle for gaming machines in North America continues to be sluggish. In addition, the current environment could force customers to decrease spending or ultimately declare bankruptcy.
- **Intellectual Property Rights.** Since Bally operates in a highly litigious industry, the company may be subject to claims of intellectual property infringement. Bally is currently involved in an ongoing legal battle with chief rival IGT, who filed a patent infringement lawsuit. An unfavorable court ruling could be detrimental to operations and impact future performance.
- **Change in Gaming Regulation**. Bally's products are subject to extensive federal, state, local and foreign regulation by various gaming authorities. The company's operations could be adversely impacted by unfavorable public referendums, such as referendums to increase taxes on gaming revenues.

Management

Richard Haddrill has been President and CEO of Bally Technologies since 2004. Haddrill previously served as the President and CEO of Powerhouse Technologies, which was a publicly traded gaming company. Robert Caller is the Executive VP, CFO and Treasurer of the company. Caller first joined BYI in 2006; previously he was partner at Ernst & Young. Through its effective management team, Bally has experienced a huge turn around in the past few years is now the fastest-growing supplier in the gaming industry.



Ownership

% of Shares Held by Insiders:	7%
% of Shares Held by Institutional & Mutual Fund Owners:	98%

Source: Bloomberg

Top 5 Shareholders

Holder Name	Shares Held	Percent of Share Outstanding
Columbia Wanger Asset Management, L.P.	5,332,950	9.82%
Eagle Asset Management, Inc.	3,072,578	5.66%
FMR LLC	2,557,734	4.71%
Barclays Global Investors UK Holdings Ltd	2,361,006	4.35%
Vanguard Group Incorporated	2,275,668	4.19%

Source: Bloomberg

New Oriental Education and Technology Group
EDU
Price: $77.08 (38.04-77.50)
Fiscal Year Ends: May 31

September 23, 2009 Sarah Finneran
iShares MSCI Emerging Markets Index: $39.13 (18.22-42.00) International Business Services

New Oriental Education and Technology Group is the largest provider of private educational services in the People's Republic of China based upon number of programs offered, enrollment rates and geographic presence. EDU products and services include language training, test preparation, private primary and secondary schools, online education, and educational content software. Educational programs and services accounted for 91% of EDU's FY2009 revenue stream while the Books and Others segment comprised the remaining 8% of revenue. In FY 2009, student enrollment reached 1.5 million, a 19.5% increase from FY 2008. EDU boasts a network of 48 schools, 270 learning centers, 23 bookstores, and approximately 5,200 teachers in over 40 cities. EDU was founded in 1993 and is headquartered in Beijing, China. 1 ADR constitutes 4 ordinary shares of EDU.

Recommendation

EDU's strong market presence and ability to capitalize on demographic and industry trends position the company for strong top-line growth in light of the continued economic uncertainty. EDU's net revenue has increased at a CAGR of 40.5% from 2004-2009. Further, management forecasts gross margins to expand by 200 basis points in FY 2010. The education industry provides significant opportunity in China as the culture reveres quality education. Over recent years, there has been a significant shift to studying abroad; approximately 200,000 Chinese students studied abroad in 2008. In addition, EDU enjoys premium brand recognition as it is the only language school in China that is authorized to administer the ESOL examinations which are internationally recognized English qualification exams taken by over 3 million people in 130 countries. EDU's growth initiatives include plans to increase student enrollment and course fees at existing facilities as well as pursue opportunities for geographic and facility expansion. Although EDU has experienced a significant run up in its stock price over the past 16 days, the company's solid fundamentals cannot be ignored. It is recommended that EDU be considered as a conditional buy for the International AIM Portfolio at a target price of $75.

Key Statistics	Sept. 16, 2009
Market Cap	$2.91B
Shares Outstanding	38.05M
Ave. Volume (3 month)	342,700
Adjusted Beta	1.10
EPS (TTM)	$1.59
2010 Estimated EPS	$2.30
P/E (TTM)	48.14
PEG Ratio	1.29
Dividend Yield	0.00%
WACC	11.76%
Debt/Assets	0.00%
ROE	18.78%
ROA	14.09%
Gross Margin	61.71%
Operating Margin	24.53%
Analyst Coverage	14
Target Price	$75.00

Source: Bloomberg

Investment Thesis

- **Chinese education industry.** In the Chinese family structure, significant cultural emphasis is placed on obtaining a quality education. In a recent decomposition of Chinese consumer spending, education was the third largest expenditure at 11.6%, preceded only by food and housing.
- **Increased study abroad.** Studying abroad to obtain an overseas degree has become an increasingly popular practice for Chinese college students. In 2008, the U.S. government issued over 53,000 visas to Chinese students, close to 43% higher than in 2007. Students who wish to study abroad often start English courses and other preparation measures over four years in

advance. According to the Chinese Ministry of Education, there will be a 30% increase in the number of students studying abroad in 2010.

- **Strategic movement to younger students.** Mainland China has over 130 million children between the ages of 5 and 12. This largely untapped market provides significant potential for EDU. The company's Kids English program, which targets this age group, has experienced impressive growth with student enrollments growing 50% YoY; management is guiding 35% to 40% enrollment growth in 2010 for this program alone.
- **New Oriental U-Can.** New Oriental recently instituted the U-Can program which targets students preparing to take the gaokao exam. China supports a population of over 120 million middle and high school age students. In FY 2009, the program had 283,000 enrollments; management expects U-Can enrollment to grow by 100,000 students in 2010. If this enrollment goal is achieved, EDU will be the largest gaokao test prep business in China.
- **Strong brand recognition.** EDU enjoys premium brand recognition as the market leader in private educational services. As such, 80% of EDU customers take more than one course through EDU and continue to use EDU for several years. This results in reliable, steady revenue streams and reduced student acquisition costs.

Valuation

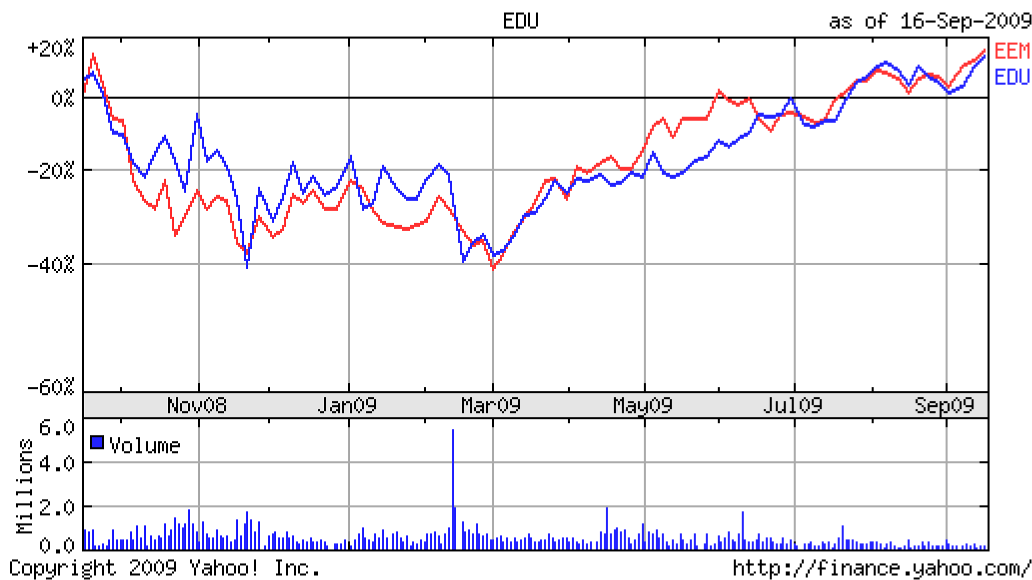
A 10-year DCF analysis using a calculated WACC of 11.75% and a terminal growth rate of 3.5% determined an intrinsic value of $70.66 for EDU. A sensitivity analysis adjusted sales growth for Year 1 (28%-36%) and terminal growth rate (2.5%-4.5%) which produced a price range of $64.04-$78.87. On a relative basis, a P/S multiple of 7.5x my 2010 revenue per share estimate of $10.38 and an add back of $6.70 cash/ADS yields an $84.55 price target. Considering both valuation methods, a target price of $75 is appropriate, representing a 12% upside based on a market price of $67.

Risks

- **Changes in testing materials and admission standards.** Test preparation constitutes a significant portion of EDU's revenue stream. When United States assessment exams added the essay component, EDU was forced to equip faculty with the skills and training necessary to analyze essays. In 2005, the PRC Ministry of Education reformed the CET 4 and CET 6 exams by offering them only to college students. This significantly reduced enrollment in CET exam preparation courses. If assessment tests or admission standards are altered, this could have a significant impact on EDU's top line growth going forward.
- **Margin contraction.** EDU could face margin pressures going forward as the company is not raising its prices as aggressively as in the past. However, this move has spurred increased enrollment. Management has confirmed that price freezes are only a temporary measure in response to the weakened economic conditions.
- **Highly fragmented industry.** The Chinese education market is ripe with competition as it is such a highly fragmented industry. Foreign competitors like Princeton Review and Kaplan are able to penetrate the market as barriers to entry have diminished significantly in the face of online course offerings. Furthermore, competitors are actively consolidating the space while EDU has not seen a great deal of M&A activity.

Management

Current CEO and Chairman of the Board Michael Yu founded EDU in 1993 with the goal of becoming the trusted educational partner for Chinese students throughout their lifetimes. Mr. Yu has over 20 years of experience in the Chinese education industry, starting as an English instructor at Peking University in 1985. He facilitated the impressive growth EDU has experienced and continues to bring innovative ideas to the company. He is supported by Louis Hsieh who is president and CFO.



Ownership

% of Shares Held by Insiders:	24.03%
% of Shares Held by Institutional & Mutual Fund Owners:	25.10%

Source: MSN Money

Top 5 Shareholders

Holder Name	Shares Held	Percent of Share Outstanding
Morgan Stanley	2,643,030	6.95%
Waddell & Reed	2,142,547	5.63%
Baillie Gifford and Company	2,021,800	5.31%
Lloyd George Management	1,374,260	3.61%
Emerging Markets Management	1,370,210	3.60%

Source: Bloomberg

HQ Sustainable Maritime Industries Inc.
HQS
Price: $9.10 ($3.29-$10.31)
Fiscal Year Ends: December 31

September 17th, 2009 — Tiffany Roberts
Russell 2000 Index: 600.03 (342.59-761.78) — Business Services

HQ Sustainable Maritime Industries Inc. is a multinational firm engaged in the aquatic product producing, processing, and farming of toxin free tilapia, other aquatic products, and marine bio and healthcare products. HQS has three reportable revenue segments: Aquaculture Product, Health & Bio-Products (Nutraceuticals), and a newly introduced Feed segment (2008 revenues: 67%, 33%, and 0%, respectively). Its main aquaculture products include tilapia and shrimp that are exported to the United States, Canada, Japan, and European countries. The company's principal health and bio-products consists of shark cartilage capsule, shark liver oil, and shark liver, all sold in the People's Republic of China (PRC). HQS also produces nutraceuticals, manufactured from palm oil or other natural organic matters which enrich feed formulations for tilapia and shrimp. The company was founded in 1989, and it is headquartered in Seattle, Washington with primary operations in the Hainan Province of China.

Recommendation

HQ Sustainable Maritime Industries Inc. prides itself on being a vertically integrated company, focusing on producing quality toxin-free tilapia and shrimp products. HQS has proven its resilience during the current economic downturn, which is evident through their extensive intercompany expansion. The performance of the Aquaculture Product and Health & Bio-Products both saw significant revenue gains y-o-y in Q2 '09 (9% and 12%, respectively). Overall, the company experienced top line growth of over 10% y-o-y. HQS has maintained impressive gross and operating margins (41.64%, 22.22%, respectively) allowing for any top line growth to ultimately flow through to the bottom line (net margin). Furthermore, HQS boasts a strong capital position with $63.09M in cash and no long-term debt. As a result, HQS will continue to improve production capacity through 2011 with the introduction of two filet processing lines, an additional production plant, as well as expanding into pond ownership and potential cage farming. Therefore, because of HQS's expanding product line and production capabilities, strong financial position, and an opportunity to gain future market share, it is recommended that HQ be added to the AIM Domestic Equity Portfolio at a target price of $12.50, allowing for a potential upside of 37%.

Key Statistics	September 17th, 2009
Market Cap	$127.89M
Shares Outstanding	13.664M
Ave. Volume (3 month)	79,816.90
Adjusted Beta	.80
EPS (TTM)	$1.02
2009 Estimated EPS	$.88
P/E (TTM)	8.71
PEG Ratio	.36
WACC	8.67%
Debt/Assets	0
ROE	12.79%
ROA	10.88%
Gross Margin	41.64%
Operating Margin	22.22%
Dividend Yield	0%
Analyst Coverage	4
Target Price	$12.50

Source: Bloomberg

Investment Thesis

- **On-going Expansion in Chinese Operations.** In 2009, management added two additional filet processing lines (increasing the total to 6) to its existing plant. This addition is expected to be completed by year end at a total cost of $3M, and is projected to increase plant capacity by over 30% (10,000 metric tons). HQS management has also entered into negotiations to buy a parcel of land to build a new production plant, 100 meters from the existing plant in China. This new plant

is expected to benefit from numerous efficiencies as a result of the sharing of resources and labor management at a cost of $15M. It is anticipated to be complete in 12-15 months with the expectations to generate an extra $30M of annual aquaculture product revenue (an increase of over 50%) once operational. Lastly, HQS will also enter into pond ownership and management late next year, progressing toward a sustained effort to improve the quality of HQS's fish products as well as full vertical integration.

- **Rise in Tilapia Demand.** According to the National Marine Institute (NMI), per capita tilapia consumption has grown significantly in the United States, increasing by over 300% since 2000. Also, according to the NMI, tilapia is the fastest growing segment of the seafood market in the United States. HQS management expects Europe to replicate this shift towards tilapia and plans to capitalize on this change in consumer preferences through vertically integrated production and increased consumer awareness of the benefits of organic, aquaculture products.
- **New Chinese Nutraceutical Legislation.** On September 1st, 2009, all Chinese companies were required to comply with a new food safety law. This legislation raises nutraceuticals standards which HQS has been in compliance with since 2005, evident through Good Manufacturing Practice (GMP) certification. Management expects to benefit from this new legislation, as it should bring about a serious reduction in the subpar producers of nutraceutical products.

Valuation

Based on a 10 year DCF analysis with a computed WACC of 8.67% and a terminal growth rate of 3.5%, an intrinsic value of $12.34 was obtained for HQS. A sensitivity analysis that adjusts both the long-term growth rate (2.5-4.5%) and the WACC (7-10%) generates a price range of $9.41-22.92. Applying an historical P/E average of 12.5x to my 2010 EPS estimate of $1.16 yields a $14.50 price target. Taking into consideration these two methodologies, a price target of $12.50 was obtained. With the stock currently trading at $9.10, this target provides for a 37% upside. HQS does not pay a dividend.

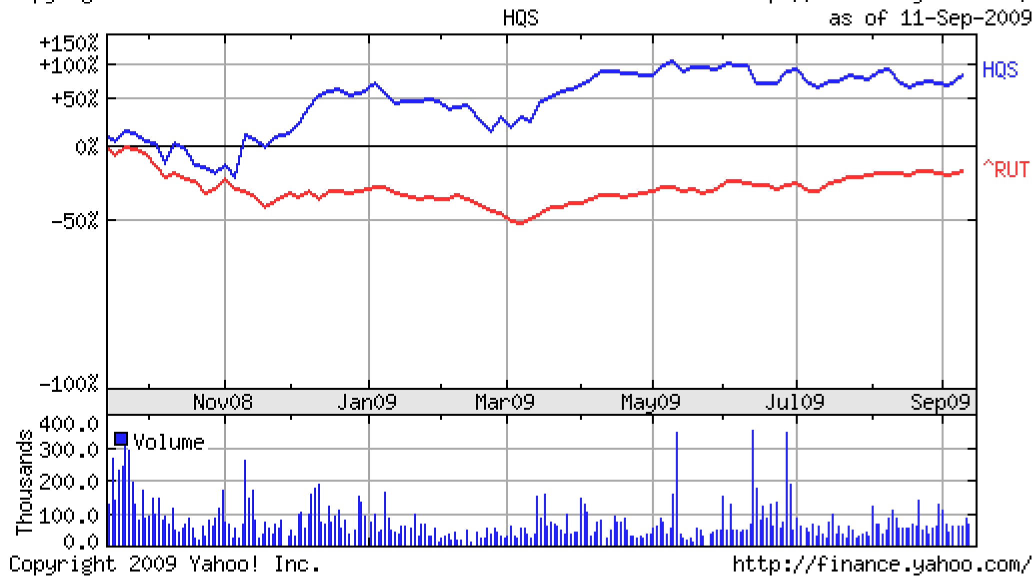
Risks

- **Concentrated Customers.** In 2008, HQS's five largest customers constituted almost 40% of net sales and 46% of trade receivables, all relating to the company's aquaculture segment. A loss or nonpayment from any one of these five customers could negatively and materially affect the company's results in terms of operations and financial position.
- **Potential Export Regulation.** HQS exports most of its aquatic products to the United States, Canada, Japan, and European countries. Countries importing HQS's products could impose tariffs or duties, potentially making the company's products less competitive. The U.S. has previously imposed anti-dumping duties on certain seafood imports, such as shrimp, which if raised or expanded to include tilapia, could also negatively affect the company's competitive position.
- **Exposure to the Chinese Government.** HQS's operations take place mainly in China. The exposure to the Chinese government could adversely affect the company as the government has significant control over the economy, including foreign direct investment, tax policies, foreign currency conversion, or the nationalization of private enterprises.
- **Input Costs.** HQS depends on a variety of raw material inputs, including tilapia and shrimp. The costs of tilapia and shrimp could be affected by the climate, the supply of clean rainwater, disease, or pollution, which could constrict HQS's margins and put pressure on the company's ability to meet consumer demand.

Management

Norbert Sporns is the co-founder, President, Chief Executive Officer, and Director of HQS. Sporns boasts more than 20 years of experience in global project development and investment consulting. Since

1997, Sporns has successfully led the company with an objective to become the world leader in vertically integrated production, processing, and farming of toxin-free tilapia products.



Ownership

% of Shares Held by Insiders:	25%
% of Shares Held by Institutional & Mutual Fund Owners:	46%

Source: Bloomberg

Top 5 Shareholders

Holder Name	Shares Held	Percent of Share Outstanding
Red Coral Group	1,984,142	14.52%
Sino-Sult Canada	1,421,529	10.40%
River Road Asset Management LLC	821,533	6.01%
Hound Partners LLC	609,520	4.46%
Royce & Associates LLC	454,000	3.32%

Source: Bloomberg

National CineMedia, Inc.
NCMI
Price: $16.83 ($4.79-16.84)
Fiscal Year Ends: December 31

September 17, 2009 — Ross Michler
Russell 2000 Index: $615.47 ($342.59-761.78) — Media Sector

National CineMedia, Inc. is the leading operator of digital in-theatre advertising in North America with over 17,000 screens in its network. NCMI receives 89.4% of revenues from its FirstLook segment, where it develops, produces, sells, and distributes its advertising program and various marketing and promotional products to national, regional, and local theatres. NCMI also operates in two other segments, CineMeetings and Fathom events, through its digital network. These segments consist of facilitating corporate events and meetings at movie theaters, while also distributing live and pre-recorded concerts, sporting events, and entertainment programming. Headquartered in Centennial, Colorado, NCMI was founded in 2005 by the three largest movie theater chains in the country: AMC Loews, Cinemark Holdings, Inc. (CNK), and Regal Entertainment Group (RGC).

Recommendation

NCMI is one of two major players in the North American theatre advertising industry with a 45% market share. This is expected to remain the same because its main competitor, Screenvision, accounts for an additional 45% of the market, creating high barriers of entry for any smaller competitor attempting to enter the market. In addition, NCMI has 30-year exclusive contracts with its founders, the three largest theatre chains, none of which are set to expire before 2037, and it distributes its proprietary DCN technology to these affiliates. NCMI's emphasis on top line revenue growth, (11.3% YoY in 2008) coupled with technological advances, allow the firm to cut costs and maintain steady and improving operating margins at the bottom line (46.87% in 2008), putting NCMI at a advantageous position to take more market share in the forthcoming years. Despite a weak advertising environment, the company has experiences growth due to expanding cinema audiences (56% CAGR since the firm's incorporation). Thus, because of NCMI's unique competitive positioning, strong growth, and high profitability, it is recommended that NCMI be added to the AIM Equity Portfolio with a target price of $21, which yields a potential 24.78% upside. The firm pays a 4.12% dividend.

Key Statistics	Sept. 15, 2009
Market Cap	$708.87M
Shares Outstanding	42.119M
Ave. Volume (3 month)	236,008
Adjusted Beta	1.30
EPS (TTM)	0.89
2009 Estimated EPS	0.80
EV/EBITDA	5.57
ROA (TTM)	19.53%
WACC	9.00%
Debt/Assets	133.40%
PEG Ratio	1.10
Gross Margin	83.55%
Operating Margin	46.87%
Dividend Yield	4.12%
Analyst Coverage	14
Target Price	$21

Source: Bloomberg

Investment Thesis

- **High Barriers to Entry.** NCMI's growing market share of 45% gives it a distinct advantage as theatre advertising industry continues to grow into the future. Only 3 years into its 30-year exclusive contracts with the three largest theatre chains, the current industry consolidation will aid in the firm's growth. These relationships and other multi-year agreements with several other theatre operations, including Hollywood and Cobb, allow NCMI to competitively price their services to force smaller players out of the market.
- **Sale of Screenvision.** As NCMI's strongest competitor and market leader prior to 2008, any alteration in Screenvision is large news. Screenvision was put up for sale by its 50% owner,

Thomson, in February, and any change in management or ownership will affect the company's ability to compete with NCMI's top line growth as it restructures. Furthermore, NCMI has expressed interest in purchasing the firm, which would effectively create a monopoly in the cinema marketing industry, dramatically modifying NCMI's long-term profitability forecasts with a 90% market share.

- **Theatre Advertisement Growth.** Cinema Advertising has been growing (56% CAGR since 2005) as advertisers have begun to appreciate the ability of theatres to deliver not only an engaged and attentive audience, but also their ability to more effectively tailor marketing schemes to a particular demographic. Theatre location, show times, movie genre, and ratings are all advantages of cinema entertainment and advertising that print, radio, and television cannot provide. For instance, despite a weak advertising market, NCMI's Q1 and Q2 advertising revenue grew 11.9% YoY and 11.6% YoY respectively. Furthermore, NCMI operates using digital equipment provided by the movie theatres they serve, thus making expansion less costly, they can expand into new theatres without high capital expenditures (management's CAPEX guidance for 2009 is only $8-10M).

Valuation

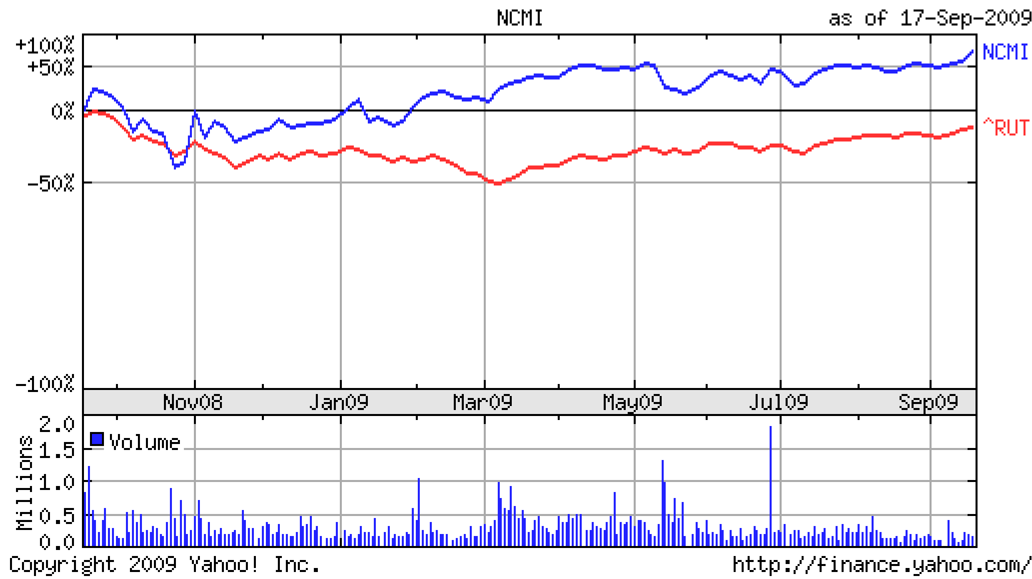
NCMI currently trades at an EV/EBITDA of 5.57x relative to its peer group average of 7.31x. A 5-year DCF analysis with a WACC of 9.0% and terminal growth rate of 3%, led to an intrinsic value of $20.61. A sensitivity analysis adjusting for best and worst case scenarios led to an intrinsic value range of $17-26. Taking management revenue assumptions, industry consolidation, and barriers to entry into consideration, a stock price of $21 was established for NCMI, offering upside potential of 25%.

Risks

- **Industry Cyclicality.** Approximately 90% of NCMI's revenue comes from advertising, a very cyclical and consumer dependent industry. Any change in the current economic recovery or consumer sentiment will directly affect the company's profitability, limiting its ability to pay off its large debt and expand into new theaters. In addition, if the theatres and movie producers cannot deliver an audience, advertisers will pull their ads from NCMI's payroll.
- **Screenvision Purchase.** While the acquisition of Screenvision would be very beneficial by erasing NCMI's only significant competitor, NCMI is already highly levered. The fear of NCMI overpaying for its strongest competitor and their market share is a large concern because it would adversely impact the firm after they have exhibited an ability to organically capture market share from Screenvision since their IPO and restructuring in February 2007.
- **Highly Levered.** The founding companies loaded NCMI with debt in 2005 and when the firm recapitalized it did so by issuing significant amounts of debt to the point where it has more debt than assets. Despite the firm's bottom line growth, this is an alarming risk as any decline in operating margins could make it difficult for NCMI to satisfy its debt covenants. For instance, in 2008 income was only 2 times its interest payments, leaving the firm susceptible to default if its profitability lags.
- **Management and Board Concerns.** NCMI's ownership structure is another risk as the 3 founding companies have a 58% ownership stake. NCMI does not have strong governance, as 6 out of the 10 members of the board are handpicked by AMC, Regal, and Cinemark and the seventh is CEO Kurt Hall, meaning only three are independent of the company. The structure also circumvents minority shareholders as the board requires a supermajority for most decisions and has the power to issue blank-check preferred stock without a shareholder vote.

Management

Kurt Hall has served as Chairman and CEO of NCMI since its founding in 2005, and prior to taking the position, he acted as co-chairman and co-CEO of Regal Entertainment Group. The remaining executives also have extensive industry experience as the majority of them moved to the company from Regal.



Ownership

% of Shares Held by Insiders:	1%
% of Shares Held by Institutional & Mutual Fund Owners:	99%

Source: Bloomberg

Top 5 Shareholders

Holder Name	Shares Held	Percent of Share Outstanding
Times Square Capital Management	3,708,300	8.80%
AXA	3,285,205	7.80%
Wells Fargo & Co	3,208,503	7.62%
FMR LLC	3,000,000	7.12%
Fidelity Mid-Cap Stock Fund	3,000,000	7.12%

Source: Bloomberg

Safety Insurance

Price: $31.99 ($28.16-49.39)
Fiscal Year Ends: December 31

September 23, 2009 — Mike Rice
Russell 2000 Index: $594.90 (342.59-761.78) — Financial Services Sector

Safety Insurance is a property and casualty insurance company located in Massachusetts. SAFT primarily focuses on private passenger automobile insurance (71.7% premiums written), but it also has a small presence in commercial automobile insurance (13.2%), as well as homeowners insurance (11.6%). The remaining 3.5% of premiums written include dwelling fire, umbrella and business insurance. SAFT's insurance products are sold through a network of over 827 independent agents located in 969 locations throughout Massachusetts. SAFT prides itself on its technological platform that is used by its agents which has helped increase the agent base. Currently the state of Massachusetts requires owners of registered automobiles to maintain a minimum level of insurance coverage. SAFT is registered with Commonwealth Automobile Reinsurance (CAR), which passes along insurance policies for car owners that are unable to find their own insurance policies and makes certain all automobile owners are insured. SAFT recently applied for and received the ability to underwrite products in New Hampshire. Safety was founded in 1979, currently has about 600 employees and is headquartered in Boston.

Recommendation

Safety Insurance provides a good value play at its current price and position within the Massachusetts auto insurance industry. Due to the newly passed and implemented Massachusetts Auto Insurance Plan (MAIP), SAFT was forced to cut rates to keep their pricing competitive, which should only affect revenue in the short term. SAFT's premium revenue has been helped by recent expansion into New Hampshire as well as increases in SAFT's other insurance lines, primarily homeowners which had an increase of 3.4% in premiums written during 2Q 2009. These rate cuts will allow SAFT to offer their products at cheaper prices, thus making SAFT appealing to new consumers. This, combined with their strong underwriting discipline, will help SAFT's premium revenue and combined ratio (currently 96%) return to the 2006-07 levels (90%) by 2011. SAFT will also continue to see increasing premium revenue from CAR as a result of the MAIP. SAFT currently trades under its book value of $40.28 and 2009 will mark the 30th consecutive year that the experienced management team has navigated SAFT to profitability. Because of this fundamental analysis, I am recommending SAFT be added to the AIM Equity fund with a target price of $39.00 which represents an upside of about 23%.

Key Statistics	Sept 19, 2009
Market Cap	$490.71
Shares Outstanding	15.34
Ave. Volume (3 month)	75342
Adjusted Beta	.80
EPS (TTM)	$3.64
2009 Estimated EPS	$3.40
P/E (TTM)	8.79
PEG Ratio	.63
WACC	8.77%
Debt/Assets	0%
ROE	11.98%
ROA	4.87%
Gross Margin	12.95%
Operating Margin	9.44%
Dividend (Yield)	$1.40 (5.00%)
Analyst Coverage	1
Target Price	$39.00

Source: Bloomberg, Yahoo! Finance

Investment Thesis

- **Superior Product with Competitive Pricing.** SAFT's market share grew from 10.6% in 2003 to 11.1% in 2008 despite operating in a fully regulated environment with prices established by the Commissioner. After the implementation of MAIP, SAFT cut rates, but did not have to

compromise product quality. The price of SAFT's products will appeal to consumers searching for car insurance and will result in increased premium revenue.

- **Increasing Premiums, Decreasing Losses from CAR.** From 2006-2008 SAFT was forced to take any policy that CAR passed along and share in CAR's losses. MAIP has allowed SAFT to only accept policies that meet the company's standards and has eliminated the sharing of losses. SAFT's premium revenue will continue to increase after the MAIP became fully implemented on April 1, 2009. Also, the new policies from CAR will meet SAFT's strong underwriting standards, thus decreasing losses.
- **Growth in Secondary Product Line and Market.** SAFT has traditionally operated in Massachusetts and focused solely on automobile insurance. Recent organic expansion into New Hampshire has already produced results with 420 policies being written during 2Q 2009. Also, the 2Q 2009 growth of SAFT's homeowners insurance line helped offset some of the effects of the rate decreases. SAFT's business will continue to expand, resulting in an increase in total premium revenue.

Valuation

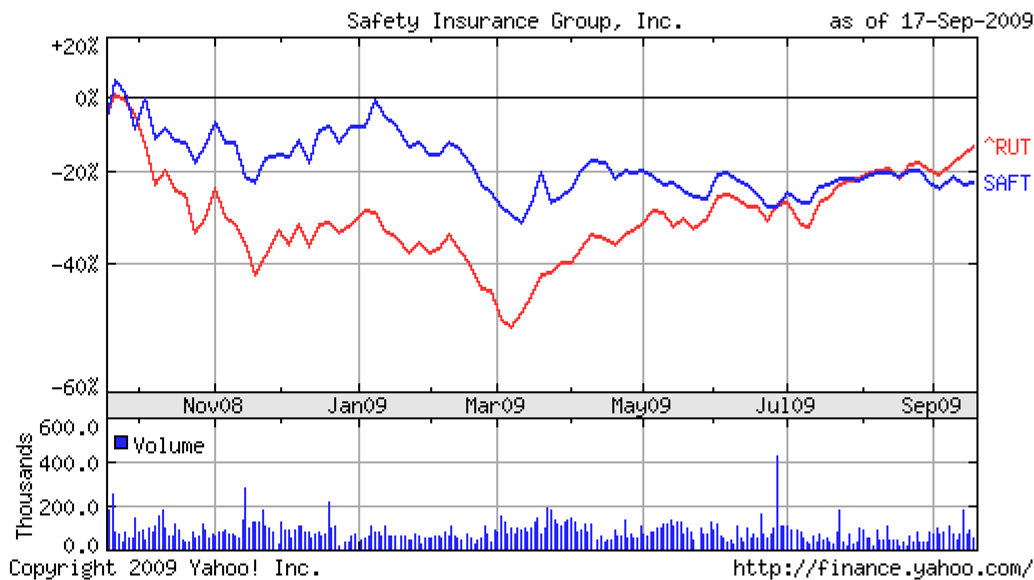
Based on a 5 year DCF analysis, using a computed WACC of 9.71% and a terminal growth rate of 3%, an intrinsic value of $38.86 was found for SAFT. A sensitivity analysis adjusting the WACC (8%-10%) and terminal growth rate (2%-3%) produced a price range of $35.76-$45.88. This model assumes total revenue growth of 5.5% in 2010 and 2011. A blended multiple approach was also used with assumptions of 12x P/E and 5x EV/EBITDA multiples. After applying these to a 2010 EPS of $3.80 an intrinsic value of $39.12 was found. SAFT's current dividend yield is about 5% with a quarterly dividend of $.40. SAFT is currently trading around $32.00 and a price target of $39.00 would produce a return of about 23%.

Risks

- **Competitive Rate Cuts/Regulation Changes.** Safety was forced to take rate cuts of 6.7% as of April 1, 2008. The state of Massachusetts switched its regulation to a "managed competition" style which gives companies the ability to offer residents more product features at lower rates. This new regulation has pushed new premiums lower since Q2 of 2008 and any future rate decreases due to regulation changes could lead to similar results.
- **Massachusetts Weather/Driving Conditions.** SAFT has taken drastic losses in the past due to unexpected weather conditions. Specifically, in 2008, SAFT took a $4 million loss related to an ice storm. Furthermore, Americans are getting in more accidents on a daily basis. Specifically in Massachusetts, which has about 4.6 million drivers, about 159,000 reported accidents occurred in 2006 which is an increase from 138,000 in 2005 and a continuation of an upward trend from prior years.
- **Loss of Independent Agents.** Because SAFT's products are distributed solely through independent agents, SAFT must compete against other insurance companies for agents. Currently SAFT has a strong agent base and obtained approximately 83% of 2008 automobile premiums from these agents. If competitors change commissions or services, SAFT could have trouble meeting these changes, thus losing parts of their distribution channel.

Management

David Brussard was appointed Chairman of the Board in March of 2004. He has been President and CEO since 2001 and has been working for Safety for 33 years. William Begley has been CFO since 2002 and has been employed at Safety for 23 years. Overall the Executive Officers of the firm have been employed over 26 years on average. Each of the Officers serves on various boards within CAR as well as other Massachusetts Insurance industry boards. This 12 person management team owns roughly 7% of SAFT.



Ownership

% of Shares Held by Insiders:	16%
% of Shares Held by Institutional & Mutual Fund Owners:	79%

Source: Yahoo! Finance

Top 5 Shareholders

Holder Name	Shares Held	Percent of Share Outstanding
JZ Equity Partners	1,157,123	7.54%
Dimensional Fund	1,039,873	6.78%
Barclays Global Investors	1,000,269	6.52%
Vanguard Group	706,526	4.61%
Times Square Capital Management	670,400	4.37%

Source: Bloomberg

Companhia de Saneamento Basico do Estado de Sao Paulo
SBS
Price: $38.77 ($13.89-39.43)
Fiscal Year Ends: December 31st

September 17, 2009 — Willie Boucher
iShares MSCI EEM Index: $38.92 ($18.22 – 42.00) — International Utilities Sector

Companhia de Saneamento Basico do Estado de Sao Paulo operates basic and environmental sanitation services in the Brazilian state of Sao Paulo. The company provides water (56.9% of revenues) and sewage services (43.1% of revenues) to a variety of residential, commercial, industrial and government customers in 366 municipalities, including South America's largest city, Sao Paulo. SBS also supplies water on a wholesale level to seven municipalities in the Sao Paulo Metropolitan Region. At the moment, the firm provides 100% of water services, 79% of sewage collection and 72% of sewage treatment in the regions it operates. SABESP was created in 1973 after the passing of the National Sanitation Plan, which fused the autocracies that used to run these services in the area. Currently, the company has nearly 16,000 employees and serves over 25 million customers. Still headquartered Sao Paulo, SBS trades on the BOVESPA and the NYSE (1 ADR represents 2 ordinary shares of SBS).

Recommendation

Companhia de Saneamento Basico do Estado de Sao Paulo is an established utility company in a growing market. Key competitors include Emae, CESP and CPOS, which are all water utilities in the state of Sao Paulo. Being the largest competitor in the industry allows SBS to maintain a gross margin of 55.42% and an operating margin of 33.28%, which are well above it's closest competitors. With billed water and sewage volume up 2.7% and 3.4% in 2Q2009 respectively, SBS has increased penetration to 60% of the state's inhabitants. While doing so, the company has also reduced water loss by 5.9% and has initiated an extensive capital expenditure program to increase efficiency and reduce environmental waste. The firm's debt/equity ratio has been consistently lower than their industry average of 75%. The firm also pays out a semi-annual dividend with a current yield of 3.99%. Therefore, because of Companhia de Saneamento Basico do Estado de Sao Paulo's prominent position in Brazil and its increasing productivity, it is recommended the that SBS be added to the International AIM Equity Portfolio with a target price of $46, yielding a 19% return.

Key Statistics	September 17, 2009
Market Cap	$4,416M
Shares Outstanding	113.92M
Ave. Volume (3 month)	314,289
Adjusted Beta	1.293
EPS (TTM)	$4.55
2010 Estimated EPS	$5.95
P/E (TTM)	7.23
Dividend Yield	3.99%
WACC	12.21%
Debt/Equity	65.43%
ROE	9.94%
ROA	5.15%
Gross Margin	55.42%
Operating Margin	33.28%
Analyst Coverage	14
Target Price	$46.00

Source: Bloomberg, Yahoo! Finance

Investment Thesis

- **Strong Brazilian Growth.** SBS is positioned favorably in an area of rapid population and economic growth amidst a global economic slowdown. According to Banco Central Brasil, the country has seen population growth on average of 1.28% for the past five years, with higher concentrations in larger cities like Sao Paulo. Worldbank believes Brazil's GDP will grow 1.2% in 2009, with 4.4% and 5.7% growth expected for 2010 and 2011, respectively. With a natural monopoly in most of their areas, SBS would benefit handsomely from these growth expectations.
- **New Tariff Increase Procedure**. Working together with the Sao Paulo State Sanitation and Energy Regulatory Agency (ARESP), SBS has been able to consistently increase their water and sewage tariffs every year. The regulatory agency has agreed upon new terms that will set tariffs

based on many factors including inflation, company financial profile, and efforts for improving efficiency and eliminating waste and harm to the environment. These guidelines align perfectly with the company's mission of improving the quality of life for its customers.

- **Infrastructure Improvement Plan.** SBS has dedicated over $4.5B in the next five years in order to increase their services and productivity in their markets. Total billable water volume increased this year by 2.7%, while water production stayed constant and water loss decreased by 5.9%. The ultimate goal is to provide 100% of water, 90% of collected sewage and 88% of treated sewage services to their existing markets. With authority from the government to do so, SBS is poised to improve existing infrastructure and implement new technologies to increase efficiency and reduce environmental waste.

Valuation

SBS is currently trading at 8.55x TTM EPS of $4.55. A conservative historical P/E average of 8 times a 2010 EPS estimate of $5.95 yields a $47.60 price target. Using a comparative industry multiple of 10 times the 2009 EPS estimate shows a $59.15 fair value. Based on a 10 year DCF analysis with a computed WACC of 12.21% (including country risk) and a terminal growth rate of 3.5%, an intrinsic value of $46.60 was obtained for SBS. A sensitivity analysis that adjusts both the long-term growth rate from 2.5% to 4.5% and the WACC from 10% to 14% generates a feasible price range of $37.88-60.58. This DCF assumes revenue growth of 8% for the first 3 years of valuation, down from its average of over 20% for the past 5 years, with growth slowing down in the following seven. The company also pays out semi-annual dividends with a current yield at 3.99%. Therefore, I have set my target price at $46. With the stock currently trading around $38.77, the $46 price target would yield a 19% return and a 3% dividend yield.

Risks

- **Foreign Government Issues.** Uncertainty in the role of Brazilian government could play a major role in the operations of SBS. With the State of Sao Paulo owning 50.3% of the company, they have significant control over further operations. Currently there is a dispute between SBS and the state regarding repayment of an employee pension plan. However, external consultants believe this will be resolved to SBS's benefit. In addition, recent polls suggest that Jose Serra and the Party of Brazilian Social Democrats will likely oust President Lula's picked successor of the Workers Party in the October 2010 presidential elections.
- **Exchange Rate Fluctuation**. SBS holds many investments in foreign currency (around 30%) that fluctuate based on their relation to the Brazilian Real. Last year they saw a large exchange rate gain that was the result of the growing strength of the Real versus the U.S. dollar. This relationship is unpredictable and could severely alter the income for SBS in the future.
- **Municipal Concession Contracts.** Beginning in 2010, SBS will be required to have specific concession contracts with every municipality it conducts business with. As of now, 32 of the 367 municipalities are being served with no formal contract. However, SBS does own all of the assets associated with water and sewage services in these areas. If SBS fails to either renew or create concession contracts with municipalities in the future they could lose the right to service certain areas which would severely cripple returns.

Management

Ms. Dilma Seli Pena, chairman of the board since 2007, has been active in the water and sanitation industry in Brazil for many years. She currently serves on the board of other state owned water utility companies in the State of Sao Paulo and is the State Secretariat of Sanitation and Energy. Mr. Gesner José de Oliveira Filho has been CEO since 2007 and has a long track record working for various economic departments for government. Mr. Rui de Britto Álvares Affonso joined SBS as CFO in 2003 and serves as Brazil's seat on the Forum of Federations.

Ownership

% of Shares Held by Insiders:	50.3%
% of Shares Held by Institutional & Mutual Fund Owners:	21%

Source: Yahoo! Finance

Top 5 Shareholders

Holder Name	Shares Held	Percent of Share Outstanding
Allianz Global Investment Partners of America	3,198,432	2.81%
Acadian Asset Management	1,874,290	1.65%
Tradewinds Global Investors, LLC	1,872,316	1.64%
SAM Sustainable Asset Management Ltd.	1,048,300	0.92%
Barclay's Global Investors UK Holdings Ltd.	903,621	0.79%

Source: Yahoo! Finance

Taiwan Semiconductor Manufacturing Company
TSM
Price: $10.89 ($5.80-11.94)
Fiscal Year Ends: December 31

September 17, 2009
iShares MSCI EEM Index: $38.92 (18.22-42.00)

Daniel Widjaja
International Hardware

Taiwan Semiconductor Manufacturing Company is currently the world's largest foundry in the semiconductor industry. As a foundry, it manufactures integrated circuits (IC) based on designs that are provided by either the customers or third parties. The company is divided into two business units: Advanced Technology and Mainstream Technology. Advanced Technology accounts for 52% of total sales in 2008, while Mainstream Technology accounts for 48%. In 2008, TSM's revenue was 51% of total revenue in the foundry industry. TSM's revenue stream can also be divided into the different applications the products serve: Communications accounts for 45%, Computer 28%, Consumer 21%, and Industrial /others 6%. In 2008, the United States was TSM's largest market (73% of revenue), followed by Asia (16%), and Europe (11%). Established in 1987, TSM is headquartered in Hsinchu, Taiwan.

Recommendation

As a manufacturing company, Taiwan Semiconductor differs itself from competitors with its production capability and capacity. TSM currently owns one 6-inch foundry, seven 8-inch foundries, and two 12-inch foundries. Together with UMC, Chartered, and SMIC, TSM forms a group called the Big Four foundries. It benefits largely on its economies of scale as the firm has the largest wafer production capacity among its competitors. For 8-inch wafers, TSM has 52% market share of production capacity among the big four. In the growing 12-inch wafers market, TSM owns 35% of total capacity in the industry, and 59% of the Big Four. Due to its large capacity and capability, the company enjoys strong margins. Operating margin averaged 33.54% the past five years, significantly higher than the Big Four's average of 4.53%. TSM also has a healthy balance sheet. While the group's debt-assets ratio averaged 19.8%, TSM's ratio was only 2.66%. In addition, the company boasts a 4.11% dividend yield. Due to its position as an industry leader, large production capability, and a healthy balance sheet, it is recommended that TSM be added into the International Equity Portfolio with a target price of $12.38.

Key Statistics	Sept. 17, 2009
Market Cap	$56.29B
Shares Outstanding	5179.27M
Ave. Volume (3 month)	14,881,784
Adjusted Beta	0.86
EPS (TTM)	$0.61
2009 Estimated EPS	$0.34
P/E Ratio (Current)	16.27
PEG Ratio	2.42
WACC	11.33%
Debt/Assets	2.66%
ROE	20.74%
ROA	17.69%
Dividend Yield	4.11%
Gross Margin	46.21%
Operating Margin	31.35%
Analyst Coverage	9
Target Price	$12.38

Source: Bloomberg

Investment Thesis

- **Increased Outsourcing.** The semiconductor industry is undergoing significant structural changes. Integrated Device Manufacturers (IDM) are starting to close down their foundries and are increasing outsourcing of IC manufacturing to dedicated foundries, such as TSM. Foundries' share of total logic capacity has increased from just 19% in 2000 to about 45% in 2009. This will not only bring more business to TSM, but it also reduces competition. Management predicts that about 20 foundries, mostly producing 8-inch wafers, will close in 2009 alone. Currently, IDMs have 59% share of total logic production capability for 8-inch foundries, declining from 80% just five years ago.

- **Low Customer Inventory Levels.** 23 of the largest foundry customers see their average inventory level decline 5.4% quarter-over-quarter in 2Q09. Average inventory days are also at its lowest level since 2004 at 68 days, down from 82 in 1Q09. After falling at an average of 54% year-over-year in 1Q09, sales have increased considerably at a monthly average of 18% since March. However, sales year-to-date is still down 27% year-over-year. Customers are expected to replenish their inventory levels this year and in 2010.
- **Well-positioned to Gain Additional Market Share.** While TSM's capex-to-sales ratio is at 17.64% (five year average is 25.2%) in 2008, management plans to ramp up capital expenditures from $1.8bn in 2008 to $2.4bn in 2009, as the firm stated clearly that they are committed to defending their market share. 80% of the capex amount will be spent on advanced technology, primarily on 40nm node technology and adding capacity to 12-inch foundries. TSM currently owns 35% of total capacity for the 12-inch foundries. As the use of 12-inch wafers increases, TSM's increasing capacity will give the firm the ability to accept more orders and customers.

Valuation

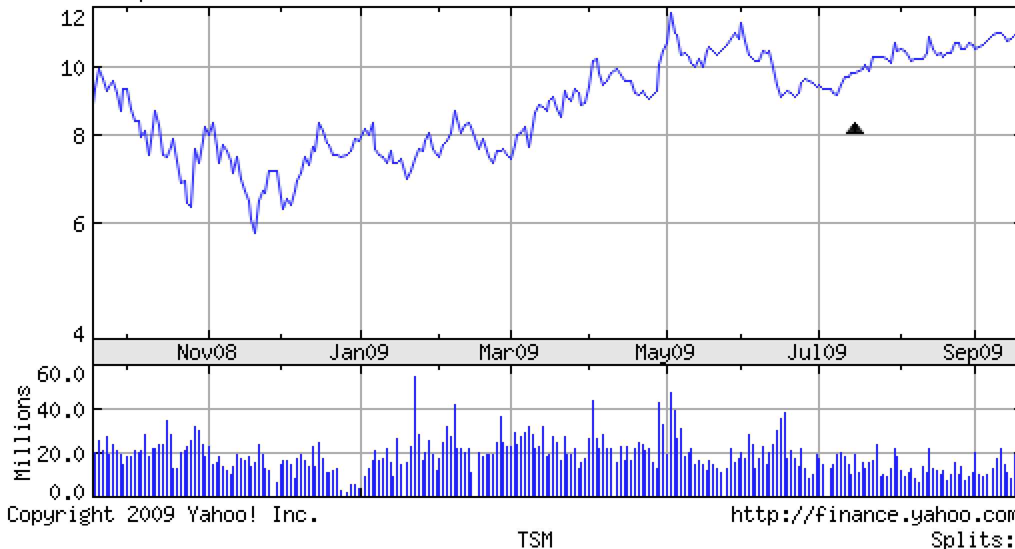
Based on a 5-year DCF analysis with a computed WACC of 11.33% and terminal growth rate of 3.5%, the model yields an intrinsic value of $11.85. The stock is currently trading at 16x earnings. By multiplying a historical P/E (post-tech bubble) of 30.34 with my 2009 EPS estimate of $0.48, a price of $14.50 is obtained. After placing an 80% weight on the intrinsic value derived from the DCF and 20% on the P/E estimate, the calculation yields a target price of $12.38. With the stock currently trading at $10.89, the $12.38 price target represents a 13.7% upside.

Risks

- **Dependence on Major Customers.** A significant portion of TSM's revenue is derived from a small group of customers. In 2008, TSM's ten largest customers accounts for 53% of the company's sales. TSM's largest customer is responsible for 14% of its sales. A loss of a major customer will have an adverse impact on TSM's revenue.
- **Pricing Pressure.** In the technology industry, average selling price of end products such as computers and cell phones tend to decline over a period of time. Since TSM's customers derive their revenue from end-users in the communication, computer, and consumer markets, their selling prices will decline. This in turn puts pressure on TSM's selling price. Moreover as the players in the semiconductor industry are decreasing, the duration of each technology breakthrough will be longer. This will give major players more time to engage in price wars.
- **Failure to Improve 40nm Node Technology.** Although management mentioned the improvements of yields on their 40nm node technology, they still expressed concerns on the issues that the technology continues to face. In its 2Q09 earnings call, management stated they will continue to place high priority on its success. Currently, it costs about $2 million per 1000 wafers for the 40nm nodes, while it costs $1.67 million per 1000 wafers for the well-established 65nm nodes. If profitability does not improve, it can have a negative impact on TSM's strong margins.

Management

Dr. Morris Chang has been the chairman of the company since its establishment. During the course of his career, he served as Senior Vice-President at Texas Instruments, and President and Chief Operating Officer at General Instruments Corporation. He is now TSMC's Chief Executive Officer. Dr. Mark Liu is the Senior Vice President of the Advanced Technology business and has been with TSMC for 15 years. Dr. C.C. Wei is the Senior Vice President of the Mainstream Technology business and has been with the company for 11 years.



Ownership

% of Shares Held by Insiders:	1.07%
% of Shares Held by Institutional & Mutual Fund Owners:	29.67%

Source: Bloomberg

Top 5 Shareholders

Holder Name	Shares Held	Percent of Share Outstanding
Barclays Global Investors UK	104,002,158	2.01%
Morgan Stanley & Co Inc.	72,298,092	1.40%
Marsico Capital Management LLC	50,472,421	0.97%
Fidelity Management and Research	48,441,230	0.94%
JP Morgan Chase & Co	42,042,774	0.81%

Source: Bloomberg

Contango Oil & Gas
MCF
Price: $47.60 ($31.69-60.00)
Fiscal Year Ends: June 30

September 15, 2009 — Danny Knight
Russell 2000 Index: $342.59-$761.78 — Energy Sector

Contango Oil & Gas (MCF) is an independent oil and gas company that engages in the exploration, development, production, and acquisition of oil and natural gas properties. Contango Operators "COI" and Contango Resources Company "CRC", its fully-owned subsidiaries, act as operators on certain offshore prospects. MCF primarily operates offshore in the Gulf of Mexico. Its revenue segments are divided so that 70% comes from natural gas production, 15% from crude oil, and another 15% from liquid natural gas. MCF depends upon their alliance partner, Juneau Exploration, L.P, for prospect generation expertise. The company is composed of only seven employees that work full time, and they are independent of their partner Juneau Exploration. MCF owns over 30 proven properties in the gulf area. The company is headquartered in Houston, Texas.

Recommendation

MCF is a rapid growing enterprise in a very competitive market. They are in the oil and natural gas market and nearly compete with everyone in the industry. Focusing on natural gas in the current economy puts them at a huge advantage. Natural gas prices were at 7 year lows and have increased dramatically with a switch from coal for electrical purposes due to talks about cap and trade. From a financial standpoint they do not have any debt on hand, however, they do have access to a healthy credit revolver if needed. Their success has been evident over the past year as they outperformed many in their respective industry with an EPS (TTM) of $3.42. Its net revenues grew to $190 million in 2009, up from $116 million in 2008, and $14 million in 2007. Despite a bear market for commodities, MCF was able to maintain a respectable EBITDA margin of 51%. The company has shown their ability to grow and earn revenues in even the hardest economic environment. Due to MCFs strong business plan in natural gas in a recovering economy, it is recommended that MCF be added to the AIM Equity Portfolio with a target price of $75, with a dividend yield of 0.0%.

Key Statistics	Nov. 15, 2009
Market Cap	$753.41M
Shares Outstanding	16.52M
Ave. Volume (3 month)	81,575
Adjusted Beta	1.24
EPS (TTM)	$3.42
2010 Estimated EPS	$3.7
P/E (TTM)	14.68
PEG Ratio	.68
WACC	10.97%
Debt/Assets	0.00%
ROE	16.16%
ROA	10.42%
Gross Margin	87.9%
Operating Margin	48.9%
Analyst Coverage	1
Target Price	$75.00

Source: Bloomberg

Investment Thesis

- **Low Natural Gas, Commodity Prices.** An improvement in the financial markets and the economy has allowed commodity prices to hike as of late. More notably are the prices of natural gas, who have surged double-digit gains over the past few weeks. Natural gas makes up nearly 70% of overall revenues for MCF. As of September 17, natural gas was trading at $3.50. 2010 natural gas futures are trading at a 12-month average of $5.50. Crude oil prices are trading at an average of $76 in 2010, up from their current price of roughly $70, an 8.5% increase.
- **Cap and Trade.** The Obama Administration has made it one of their priorities to impose a cap on carbon emissions. Despite how absurd this proposal may be, it could be a huge positive for a

company like MCF. The cap and trade is designed to target carbon emissions mainly from coal, which will benefit natural gas producers. Natural gas has already seen the effects by being a substitute for companies that used coal in the past, and might see more business if government were to grant a tax benefit to those companies who are more environmental friendly. This probably is not going to be a long-term driver because it's not possible for any country to operate at a competitive level without coal, but in the mean time, this could drive revenues.

- **Improving Economy.** With the expectations that the economy and the markets hit bottom last spring, the potential for energy companies is great. As business operations should improve in time, commodity prices and production should improve. There have already been signs of improvement in markets.

Valuation

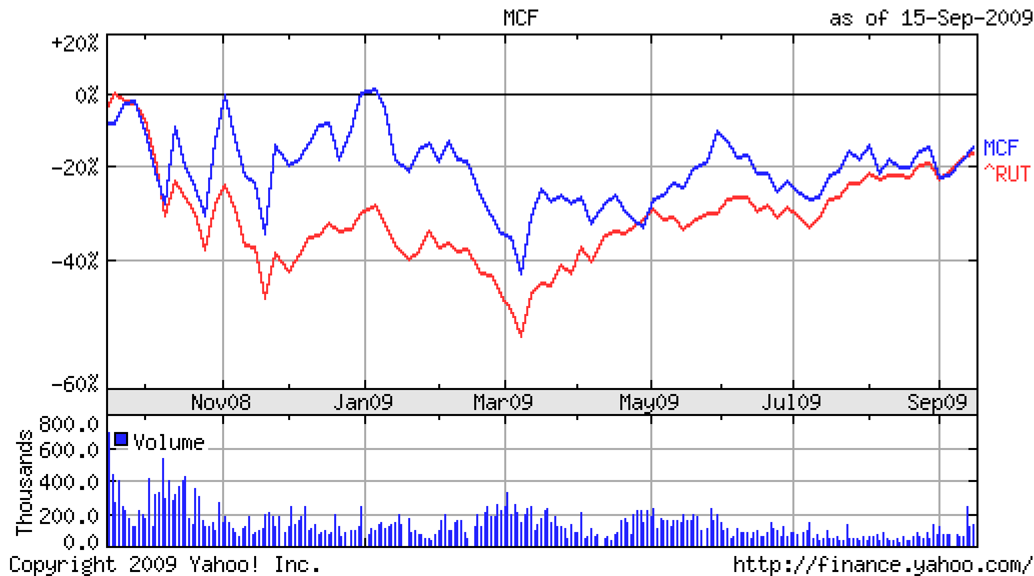
MCF is currently trading at 14.3x TTM EPS of $3.42. A computed forward P/E average of 21.8x 2009 EPS of $3.42 yields a $75 average price target. Based on a 5 year DCF analysis with a computed WACC of 10.95% and a terminal growth rate of 2.25%, an intrinsic value of $79 was obtained for MCF. A sensitivity analysis that adjusts both the long-term growth rate (2-2.50%) and the WACC (9.95 – 11.95%) generates a price range of $70-$90. Using a worst case/best case sensitivity analysis for commodity futures and production, a price range of $58-$98 was found. I think that with the signs that the market is picking up, and commodity prices are rising from near 7-year lows, I am assessing MCF with an intrinsic value of $75. With the stock currently trading around $46, the $75 price target would yield a 53% return.

Risks

- **Government Regulation.** Quite possibly the biggest threat to MCF, and American businesses in general, is government interference. There have been talks about regulating offshore drilling in the U.S. There have not been any dramatic changes thus far, but if government decided to put any constraints on drilling, the future revenue growth could be affected.
- **Drop in Commodity Prices.** Despite seeing commodity prices increase in the past few weeks, a further drop in oil and natural gas prices could further hurt the financial health of MCF. We have seen the effects low natural gas and oil prices have on revenues. There is a strong correlation between commodity prices and MCF's stock price. If the economy goes through another crisis like 2008-2009, the company could see further losses.
- **Dependency on Juneau Exploration.** As long as the relationship between MCF and Juneau Exploration exists, this could be viewed as a tremendous positive because MCF no longer has to incur lease expenses and other title expenses. However, MCF depends greatly on Juneau Exploration to the point that losing them would be catastrophic to their business.
- **Industry Competition.** MCF competes with a broad range of natural gas and oil companies, and because they are much smaller than most of their competition, its operating mobility is limited. In order to compete with the industry leaders, MCF needs to be able to gain access to the same equipment and have quality prospects for acquiring land. Their weaker balance sheet could slow down future growth if land and capital becomes more expensive, or if their competitors make larger bids for superior drilling sites.

Management

Mr. Kenneth Peak is the founder and has been the Chairman, CEO and CFO of MCF since its formation in September 1999. Mr. Peak has been at several different firms within the energy industry since 1972. The company only has seven employees who own roughly 23% of shares.



Ownership

% of Shares Held by Insiders:	26%
% of Shares Held by Institutional & Mutual Fund Owners:	49%

Source: Bloomberg

Top 5 Shareholders

Holder Name	Shares Held	Percent of Share Outstanding
Morgan Stanley	1,476,452	9.33%
Vanguard Group, Inc	664,698	4.20%
Barclays Global Investors	663,388	4.19%
Keeley Asset Management	646,000	4.08%
Dremen Value Management	330,351	2.09%

Source: Bloomberg