Applied Investment Management (AIM) Program

AIM Class of 2011 Equity Fund Reports
Date: April 23, 2010, *Location:* Cortina Asset Management
Spring 2010

Student Presenter	Company Name	Ticker	Price	Page No.
Ethan Matter	Patni Computer Systems Ltd.	PTI	$25.22	2
Benjamin Hariri	World Fuel Services Corp.	INT	$27.56	5
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Aaron Socker	Neutral Tandem Inc.	TNDM	$16.74	14

The following seniors in the Class of 2010 served as mentors to juniors:

Ticker	Senior Mentor(s)
PTI	Daniel Widjaja, Sarah Finneran, Sarah Clasing, Amy Klemme
INT	Danny Knight, Sarah Clasing
HWKN	Nate Novak
CPK	Mike O'Carroll
TNDM	Ross Michler

Thank you for taking the time today and participating in the AIM 'road show' at Cortina Asset Management. 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. Today, each student will spend about 5-7 minutes presenting their formal recommendation, which is then followed by about 8-10 minutes of Q & A. Again, thank you for allowing us the opportunity to present at Cortina.

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Patni Computer Systems Ltd. (PTI)
April 23, 2010

Ethan Matter — International Software Sector

Patni Computer Systems Ltd. (NYSE:PTI) is a leading Indian provider of information technology services. PTI delivers a comprehensive range of IT services through globally integrated onsite and offshore delivery locations. The company offers its services to customers through industry-focused practices, including insurance (29.7% of 2009 revenue), manufacturing (29.0%), financial services (12.8%), communications, media and utilities (13.5%) and product engineering (15.0%). Within these practices, PTI operates several different service lines including application development, application maintenance and support, packaged software implementation, infrastructure management services, business product outsourcing and quality assurance services. The company derives its revenues primarily from the United States (78.9%), but also has customers in Europe (12.7%), Japan (3.5%), and India (1.0%). PTI went public in 2004, and is headquartered in Mumbai, India.

				FY: Aug	2009A	2010E	2011E
Price ($): (4/16/10)	25.28	Beta:	0.86	FY: Aug	2009A	2010E	2011E
Price Target ($):	31	WACC	10.18%	Revenue ($Mil)	655.9	734.6	822.8
52WK H-L ($):	26-6	L-Term Rev. Gr Rate Est:	9%	% Growth	-8.76%	12.00%	12.00%
Market Cap (mil):	1,684.0	L-Term EPS Gr Rate Est:	7%	Gross Margin	35.77%	36.00%	36.00%
Float (mil):	64.6	Debt/Equity:	0.1%	Operating Margin	15.34%	18.00%	18.00%
Short Interest (%):	2.3%	ROA:	12.1%	EPS ($Cal)	1.84A	1.88E	1.86E
Avg. Daily Vol (thou)	66.87	ROE:	15.7%	FCF/Share	$1.84	$1.85	$1.94
Dividend ($):	0.12			P/E (Cal)	13.7	13.4	13.6
Yield (%):	0.5%			EV/EBITDA	12.4	9.9	8.8

Recommendation

Since its IPO in 2004, Patni Computer Systems Ltd. has developed into India's sixth–largest software exporter. Despite heavy spending cuts in company IT budgets in 2009 (8.2% decline), Patni mitigated revenue declines and grew EPS by 23% through a revamped cost structure which decreased COGS by 14.3% yoy. With cash and short-term investments of $6.64/share, which is well above peer averages of $2.51/share and no long-term debt on its balance sheet, management's goal of doubling revenues in the next five years through organic growth and EPS neutral or accretive acquisitions is obtainable. The end of PTI's Indian Tax Holiday and slowly increasing salary costs may put a slight pressure on the company's margins. Current estimates, however, show that PTI can absorb almost 50% revenue growth without an increase in SG&A expenses, holding net margins in the desired 14-16% range. Despite recent stock price momentum, PTI continues to trade at a compelling valuation in comparison to its peers at 13.4x Forward P/E, 2.2x P/S, and 12.4x EV/EBITDA vs. peer averages of 20.9x, 3.2x, and 14.7x respectively. Due to PTI's above average financial flexibility and compelling valuation, it is recommended that Patni Computer Systems be added to the IAIM fund at a target price of $31, an upside potential of 22.6%.

Investment Thesis

- **Business Investment and IT Spending Recovery.** PTI's qoq revenues have a significant correlation with US GDP Business Investment (r^2=0.87). Current economic consensus indicates that business investment will accelerate through 2011, encouraging growth in PTI's top line. Forrester Research's revised March forecast predicts 8.4% worldwide IT spending growth in 2010. Increased corporate IT budgets will also assist in expanding revenues as pent-up demand fuels a spending recovery.
- **Insurance Vertical and BPO Micro-Vertical Outlook.** PTI's largest and most profitable industry segment, insurance, is poised to grow into a $400 million business (19.7% CAGR) in the next four years. The BPO (Business Product Outsourcing) micro-vertical will be the main driver for this growth. The Indian BPO Market is expected to grow by 19% through 2013,

becoming a $1.8 billion market. PTI plans to decrease exposure to its maturing application development and maintenance micro-vertical and increase BPO portfolio mix 10-15% through strong pipeline prospects in the US healthcare insurance area.

- **Powerful Deal Pipeline.** PTI is poised to complete two long-term (4-5 yr.) deals within the next two quarters which are larger than any deal in the company's history ($100-200 million). Management statements indicate completion of the deals will result in 3-4+% sustained revenue increases and will improve PTI's ability to participate in large deals. PTI added 20 new clients in 4Q09 and continues to focus on client scalability to drive larger and more profitable contracts ($1.5 million minimum in 18 months, $3 million in three years). PTI has been successful in its initiative; increasing average revenue per client from $0.49 million in 1Q09 to $0.63 million in 4Q09.This is the highest growth rate among larger peers.
- **Financial Flexibility.** PTI boasts a strong balance sheet, holding $63.4 million in cash reserves, liquid mutual fund balances of $357.2 million, and no long-term debt. This financial flexibility will allow PTI to expand through strategic acquisitions in the $100-200 million range. The company's acquisitions will focus on increased geographic presence (specifically, in the Asia Pacific region), vertical/sub-vertical diversification, or obtaining intellectual property.

Valuation

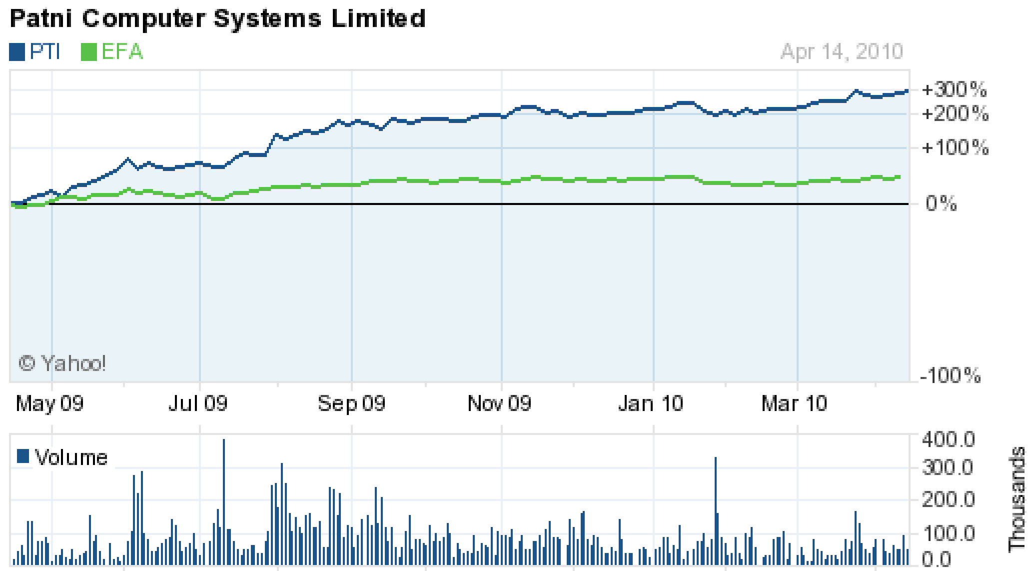
Using a 10-year DCF with a computed WACC of 10.18% and terminal growth rate of 3%, an intrinsic value of $32.26 was obtained. A sensitivity analysis performed on the WACC (9.5-11.5%) and terminal growth rate (2-4%) generated a price range of $25.58-$39.67. In addition, a 15x multiple applied to my 2010 EPS estimate of $1.88/ share yielded a price target of $28.24, and a 2.8x multiple applied to my Sales/Share estimate of $11.48/share yielded a price target of $31.59. Finally, a 13.5x multiple applied to my 2010 EBITDA/share yielded a price target of $33.12. Considering these methods, a price target of $31 was established, representing a 22.6% upside in addition to its 0.5% dividend yield.

Risks

- **Major Contracts.** If one of PTI's largest customers (State Farm, General Electric, or ABN-AMRO) ends its contract, it may have a significant impact on the company's top line. The company's major contracts operate as Master Services Agreements, which can be terminated without cause within 0-90 days of notification. This creates buyer power for customers and may create pricing pressure for PTI. This is a very common agreement in the IT outsourcing industry and is practiced by several of PTI's close competitors.
- **Outsourcing Business Model.** Current or prospective clients could be negatively influenced by unfavorable political attention focused on outsourcing IT services. It is possible that legislation might be introduced if protectionism sentiments (particularly in the United States) continue, which could have an adverse effect on the revenue and growth opportunities for the firm.
- **Significant Private Equity Investment.** General Atlantic Mauritius Ltd, a private equity firm, holds 15.6% of current shares outstanding. If the private equity firm's interests do not align with the interests of shareholders, PTI's stock price might be negatively affected.

Management

Jeya Kumar was appointed CEO and Director of the Company in February 2009. Mr. Kumar is 55 years old and has over 25 years of global industry experience spanning several geographies. Most recently, he served as CEO of MphasiS Ltd. and Senior VP of Sun Microsystems. Mr. Narendra Patni, founder of the company, stepped down as CEO but remains Chairman of the Board.



Ownership

% of Shares Held by All Insider and 5% Owners:	32%
% of Shares Held by Institutional & Mutual Fund Owners:	21%

Source: Bloomberg

Top 5 Shareholders

Holder	Shares	% Out
General Atlantic LLC	10,080,933	15.59
Fidelity Management	3,446,133	5.22
Acadian Asset Management	1,046,047	1.62
Renaissance Technologies, LLC	475,300	0.73
Oppenheimer Funds, Inc.	332,831	0.51

Source: Bloomberg

World Fuel Services Corp. (INT)
April 23, 2010

Ben Hariri | Domestic Energy

World Fuel Services Corporation (NYSE: INT) markets and sells marine, aviation, and land fuel products and related services throughout the world. INT provides fuel and services to corporate and commercial aircraft, petroleum distributors, and ships at more than 2,500 locations around the world. The services they offer include quality control, price risk management, logistical support, credit solutions, and transactions processing. In fiscal year 2009, INT's three reportable business segments of marine, aviation, and land accounted for 53%, 36%, and 11% of revenue, respectively. INT serves customers in both North America and internationally (45% and 55% of revenue, respectively) in Singapore, the United Kingdom, and 197 other foreign countries. INT was ranked fourth by Fortune magazine for One Year Total Return to Shareholders and eleventh for Ten Year Total Return to Shareholders. They were also ranked nineteenth by Barron's for ROI and Revenue Growth and thirteenth by BusinessWeek for World's Best Companies. INT was founded in 1984 and is headquartered in Miami, Florida.

					FY: Dec	2009A	2010E	2011E
Price ($): (4/16/10)	27.14	Beta:	1.03		Revenue ($Mil)	11,295.2	15,474.4	18,569.3
Price Target ($):	37	WACC	10.16%		% Growth	-38.98%	37.00%	20.00%
52WK H-L ($):	30-17	L-Term Rev. Gr Rate Est:	15%		Gross Margin	3.33%	3.10%	3.15%
Market Cap (mil):	1,660.0	L-Term EPS Gr Rate Est:	16%		Operating Margin	1.36%	1.12%	1.10%
Float (mil):	56.78	Debt/Equity:	2.3%		EPS ($Cal)	1.96A	2.12E	2.48E
Short Interest (%):	12.6%	ROA:	7.5%		FCF/Share	$3.82	$2.18	$2.61
Avg. Daily Vol (mil):	0.695	ROE:	17.5%		EV/EBITDA	7.61	7.23	6.87
Dividend ($):	0.15							
Yield (%):	0.5%							

Recommendation

INT is a global leader in the downstream marketing and supply of fuel and related services to the marine, aviation, and land transportation industries, having distributed 9.7 billion gallons of fuel during 2009. The global economic downturn depressed the oil and gas operations industry and reduced overall energy demand in 2009. Revenues were lowered because shipping companies lost between $20-30 billion—and the aviation industry lost an estimated $11 billion. Despite these factors, in 2009 INT posted record earnings of $117 million with an EPS of $1.96 per share. They were able to double their dividend year-over-year from $0.07 per share in 2008 to $0.15 per share in 2009. INT also made two strategic acquisitions over the past year to gain market share for their land segment—a segment that has seen significant growth even throughout the recession (269 million gallons in 2007, 454 million gallons in 2008, and 628 million gallons in 2009). In addition, INT's gross profit has grown at a 5-year CAGR of 23.6%. INT has been able to differentiate themselves by offering single-supplier convenience, having access to capital, and maintaining a strong balance sheet. Therefore, it is recommended that INT be added to the AIM Equity Portfolio at a target price of $37, an upside return potential of 36%.

Investment Thesis

- **Well Positioned for Growth Opportunities.** With cash equivalents totaling $307 million and a solid debt-to-equity ratio of 2.27%, INT possesses a strong balance sheet. This sound financial position, coupled with the $900 million of untapped liquidity available to them ($475 million from a revolving credit facility), provides INT with substantial financial flexibility to fund both acquisitions and organic growth opportunities going forward. Furthermore, INT's management has a disciplined approach when it comes to assessing acquisition targets. This discipline has led the firm to make acquisitions and investments that have added significant value for shareholders. INT recently announced plans to acquire assets of Milwaukee-based Lakeside Oil Company. The deal will include assets of Lakeside's wholesale motor-fuel distribution business, increasing

INT's global land volume by 350 million gallons. The transaction is expected to add $0.06-0.08 per share to EPS in the first year. The deal should also provide additional customer and supplier relationships with ExxonMobil Corporation, BP Products North America, and CITGO Petroleum Corporation.

- **Fuel Prices.** INT's revenues are highly correlated with the market price of light crude oil. This was evident when INT had negative revenue growth in 2009 of 39% when average crude oil prices fell from $100 per barrel in 2008 to $62 per barrel in 2009. Using S&P estimates based on data from IHS, the EIA and Bloomberg, spot oil prices are projected to average about $79 per barrel in 2010 and $82 in 2011. This should provide INT room for significant revenue growth moving forward, especially in 2010.
- **Financial Transparency.** Many of INT's direct competitors, including BBA Aviation plc and Sun Coast Resources, Inc. are privately held. Since INT is publicly traded, suppliers may be more inclined to sell to INT rather than to their competitors, since they would have direct access to information about INT's credit and cash availability. Because of this, suppliers may charge INT lower premiums on their products, leading to lower costs and higher margins for INT.

Valuation

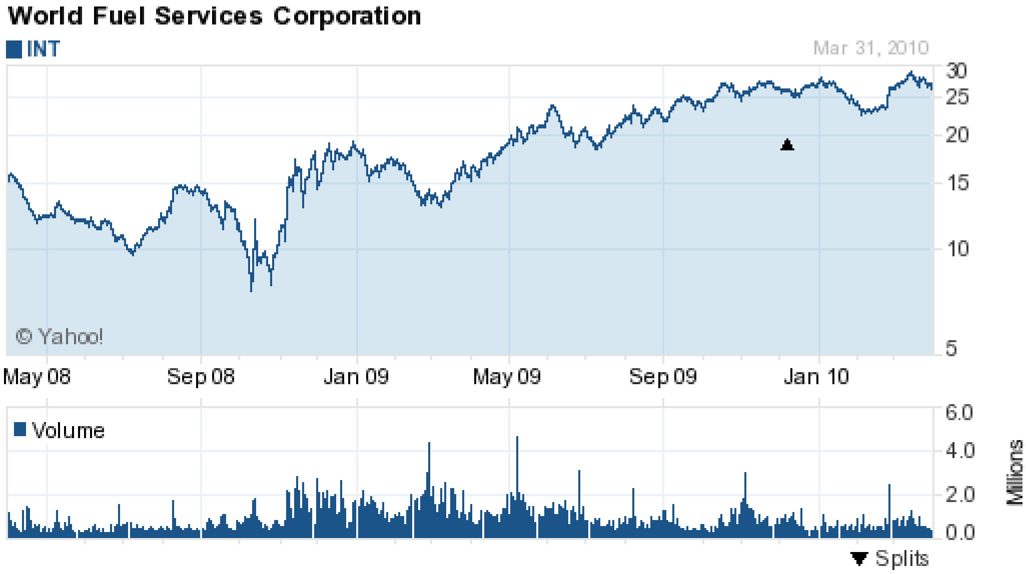
Based on a 5 year DCF analysis with a computed WACC of 10.16% and a terminal growth rate of 3%, an intrinsic value of $35.52 was obtained for INT. A sensitivity analysis that adjusts both the long-term growth rate (2-4%) and the WACC (8.15-12.15%) generates a price range of $25.90-59.07. An EV/EBITDA multiple approach was also used with a multiple of 11.89x, yielding an intrinsic value of $39.11. Taking these into account, a price target of $37 was established. With the stock currently trading around $27, the $37 price target would yield a 36% return. The firm has a dividend yield of 0.5%

Risks

- **Fuel Prices.** Changes in the market price of fuel could have a material impact on INT's business. Fuel prices have been extremely volatile in recent years and will likely continue to be volatile in coming years. Light crude oil prices have ranged from $59 to $87 per barrel over the last year. These prices are out of INT's control and are dependent on factors such as actual and expected supply and demand for fuel, production and pricing controls set by OPEC, political conditions, and weather. Because INT's inventory is valued at LCM, a significant rapid decrease in the price of fuel could cause their inventory to be marked down or sold at lower prices. Alternatively, if fuel prices increase rapidly, INT's customers may not be able to purchase as much fuel from INT due to their credit limits, having a negative effect on both top line revenue and bottom line earnings for INT.
- **Worldwide Political and Economic Risks.** INT operates in emerging markets, including Russia and certain Asian and Latin American countries, which are historically more prone to corruption and uncertainty with regards to regulatory issues. Many of the countries INT operates in may also be susceptible to currency devaluation and/or recessions.

Management

Paul H. Stebbins has served as Chairman of the Board of Directors and CEO since July 2002. He has served as a director of INT since June 1995, and served as President and COO of INT from August 2000 to July 2002. From January 1995 to August 2000, Mr. Stebbins served as President and COO of World Fuel Services Americas, Inc., the principal subsidiary engaged in the marine fuel services business. From September 1985 to December 1994, Mr. Stebbins was an officer, shareholder, and director of Trans-Tec Services, Inc. and its affiliated companies. Mr. Stebbins also serves on the board of directors and on the audit and compensation committees of First Solar, Inc.



Ownership

% of Shares Held by All Insider and 5% Owners:	4%
% of Shares Held by Institutional & Mutual Fund Owners:	>90%

Source: Bloomberg

Top 5 Shareholders

Holder	Shares	% Out
State Street Corp.	3.262.622	5.49
Vanguard Group, Inc.	3,137,231	5.28
Allianz Global Investment of America LP	3,121,900	5.26
Argyll Research LLC	2,880,000	4.85
Blackrock Fund Advisors	2,635,419	4.44

Source: Bloomberg

Hawkins, Inc.
April 23, 2010

Kristin Holzhauer — Domestic Industrial Materials

Hawkins, Inc. (NASDAQ: HWKN) manufactures, blends, and distributes bulk and specialty chemicals. It operates through two segments, Industrial and Water Treatment (70.9% and 29.1% of net sales, respectively). The Industrial segment stores, receives, and distributes bulk chemicals, bleach, agricultural products, and food grade products primarily for the energy, electronics, food, chemical processing, medical device, and pharmaceutical industries. Specializing in providing equipment, chemicals, and solutions for portable water, municipal and industrial wastewater, and non-residential swimming pool water, the Water Treatment segment had the capacity to treat systems ranging from a single well to a multi-million-gallon-per-day treatment facility. Founded in 1938, HWKN's sales are primarily concentrated in the Midwest, while the group's food-grade products are sold nationally.

Price ($): (4/14/10)	26.10	Beta	0.64		FY: Mar	2009A	2010E	2011E
Price Target ($):	32.29	WACC	8.42%		Revenue ($Mil):	284.40	355.50	444.38
52WK H-L ($):	15-27	L-Term Rev. Gr Rate Est:	11%		% Growth	44.80%	25.00%	25.00%
Market Cap (mil):	268.57	L-Term EPS Gr Rate Est:	25%		Gross Margin	22.00%	28.00%	34.00%
Float (mil):	7.93	Debt/Equity	N/A		Operating Margin	13.10%	16.38%	20.47%
Short Interest (%):	N/A	ROA:	17%		EPS (Cal)	$2.32A	$2.90	$3.63
Avg. Daily Vol.:	42,405	ROE:	21%		FCF/Share	$0.99	$1.24	$1.55
Dividend ($):	0.56				P/E (Cal)	11.60	10.77	10.46
Yield (%):	2.20%				EV/EBITDA	3.0	3.8	4.7

Recommendation

The commodity chemicals industry is highly cyclical and competitive with annual revenues of about $1 billion. Consequently, HWKN's annual revenue of $267 million accounts for 26.6% of market share. HWKN has been able to maintain its strong market share because of its efficient operations and strategic storage facility investments. Increased storage capacity over the last several years allowed HWKN to obtain substantial amounts of raw materials when prices were low; consequently, the company was able to expand market share to new and existing customers while competitors were facing materials shortages and an inability to supply their customers. HWKN should be able to retain this business and keep solid gross and operating margins, 8.8% and 14.0%. This is a significant edge relative to the industry's 1.9% gross margin and 3.9% operating margin, respectively. Additionally, HWKN has seen FCF grow 308% with zero debt on its books. Because of these reasons and a favorable valuation, it is recommended that HWKN be added to the AIM Equity Fund with a target price of $32.29, which offers a potential upside return of 17.4%.

Investment Thesis

- **Water Treatment Growth.** The Water Treatment segment normally has higher margins than the Industrial segment due to the higher service component. The first three quarters of FY10 saw gross margins at 33.1%, up 8% from the prior period of FY09, primarily driven by increased sales of higher-margin manufactured and specialty chemical products. In the past two years, HWKN has opened three new warehouses to expand its geographic footprint. This storage advantage allows HWKN to acquire large amounts of raw materials when prices are favorable, and service new customers when competitors cannot meet demand. Because of this, FY09 saw a 52.3% increase in sales over FY08.
- **Customer Service.** HWKN is competitive in the Chemical Distribution industry by maintaining its edge on superior customer service. Although many producers, distributors, and sales agents offer chemicals equivalent to almost all of HWKN's products, the company is often able to leverage long-standing supplier relationships to obtain products when supplies are scarce or to

obtain competitive pricing. HWKN has a vast network of branch offices and warehouses, providing flexibility to respond to special needs and requirements of customers throughout its large delivery area. Many of HWKN's customers have been with the company for over 20 years.

- **Operations Efficiency.** The Industrial and Water Treatment segments utilize delivery routes operated by employees who serve as route drivers, salesperson, and technician to deliver products and diagnose chemical and treatment needs. To accommodate its rapid growth, HWKN contracted Enventis Corp. in March 2010 to upgrade their network and double bandwidth, improving efficiency, productivity, and delivery of integrated applications. Additionally, HWKN was able to decrease SG&A to 8.8% in FY09, down from 14.2% in FY08 after implementing an Enterprise Resource Planning system.

Valuation

HWKN has steadily growing free cash flow and a debt-free balance sheet. Based on a 5 year DCF analysis with a computed WACC of 8.42% and a terminal growth rate of 2.5%, an intrinsic value of $32.29 was obtained for HWKN, providing a potential upside of 17.4% with a 2.2% dividend yield. A sensitivity analysis that adjusts both the long-term growth rate (2.5-3.5%) and the WACC (7.50-9.50%) generates a price range of $20.29-$46.26.

Risks

- **Environmental/Health and Safety Regulation.** HWKN is subject to regulations regarding the discharge of pollutants and management and disposal of hazardous substances. Compliance efforts consume substantial capital and incur large operating costs, and failure to comply could result in litigation, negative public reactions, and material adverse effects on operations. Federal limits on the distribution of hazardous materials are being considered, and bans on movement through certain cities could hinder HWKN's logistical efficiency.
- **Commodity Prices.** The cyclicality of commodity chemical markets—caustic soda, sulfuric and hydrochloric acid, etc.—combined with the price of HWKN's supply contracts and their tendency to lag market prices, has significant impact on cost management and margins. Rapid price escalation in FY09 allowed HWKN to sell at higher market prices, yielding a 52.3% increase in sales over FY08. Both supply constraints and demand have eased as a result of the economic downturn, and a slow recovery could suppress gross profits going forward. HWKN does not enter into futures contracts or hedge the price of commodities chemicals.
- **Expiring Patents on Value-Added Formulation.** In 1995 HWKN developed and patented a process for manufacture and delivery of Cheese-Phos and Citraflo, two ingredients that allow liquid sodium to be stored at room temperature. Allowing for higher quality and more efficient production, these ingredients are the industry standards for processed cheese production. These patents expire in 2013. Failure to renew these patents could materially affect the company's sales and profits.

Management

John R. Hawkins has been the CEO of Hawkins, Inc. for ten years, and previously served five years as Chairman of the Board from 2000 to 2005. Since Mr. Hawkins' appointment as CEO, HWKN has seen a 220% increase in its stock price. Currently serving as Chairman is John McKeon, who has 35 years of experience in senior management roles at ConAgra Foods and Northstar Industries. Patrick Hawkins is the newly appointed President and was promoted from business director of HWKN's food and pharmaceuticals operations, as part of the Board of Directors' succession planning efforts.

Ownership

% of Shares Held by All Insider and 5% Owners:	20%
% of Shares Held by Institutional & Mutual Fund Owners:	47%

Source: Yahoo! Finance

Top 5 Shareholders

Holder	Shares	% Out
Royce & Associates, LLC	857,177	8.34
T. Row Price Associates, Inc.	568,431	5.53
Gamco Investors, Inc.	476,370	4.63
Vanguard Group, Inc.	372,593	3.62
BlackRock Institutional Trust Company	334,478	3.25

Source: Yahoo! Finance

Chesapeake Utilities Corporation (CPK)

April 23, 2010

Tom Molosky — Domestic Utilities

Chesapeake Utilities Corporation (NYSE: CPK) is a diversified utility company with a wide array of businesses both regulated and unregulated, operating in Delaware, Maryland, and Florida. It is the sole distributor and marketer of natural gas in its respective local markets. It also produces electricity in Florida through its subsidiary Florida Public Utilities (FPU). Another division of CPK is its propane distribution in Delaware, Maryland, and Florida. Finally, CPK has ventured into business services with an IT division. CPK's regulated energy accounted for 78% of operating income in fiscal year 2009, unregulated energy operations accounted for 24% of operating income, and other business operations accounted for about -2% of operating income. CPK was incorporated in Delaware in 1947 after starting out as Dover Gas Light Company in 1859. The corporate headquarters are located in Dover, Delaware.

Price ($): (4/13/10)	30.51	Beta:	0.788	FY: Aug	2009A	2010E	2011E
Price Target ($):	35.50	WACC	8.39%	Revenue (Mil)	330.00	346.50	363.83
52WK H-L ($):	35-28	L-Term Rev. Gr Rate Est:	2.75%	% Growth	22.77%	5.00%	5.00%
Market Cap (mil):	282.70	L-Term EPS Gr Rate Est:	4.00%	Gross Margin	37.58%	37.45%	37.45%
Float (mil):	9.09	Debt/Equity:	1.94	Operating Margin	10.28%	10.15%	10.15%
Short Interest (%):	2.85%	ROA:	4.39%	EPS (Cal)	2.36	2.44	2.56
Avg. Daily Vol (mil):	24,521	ROE:	9.55%	FCF/Share	($1.02)	$0.76	($0.35)
Dividend ($):	0.32			P/E (Cal)	12.91	12.50	11.90
Yield (%):	4.21%			EV/EBITDA	9.87x	9.40x	8.95x

Recommendation

CPK has been proactive in the current economic environment by increasing levels of spending on capital expenditures; investing $82M in capital expenditures in the last three years. CPK has been hands-on in finding new sources of revenue with its recent merger with Florida Public Utilities which doubled the firm's customer base. CPK has also entered into a preliminary agreement with Texas Eastern Transmission to gain access to new sources of natural gas. As a result of this agreement, Chesapeake's increased access to possible energy supplies will provide renewed reliability towards natural gas reserves and will decrease the firm's need to buy natural gas at the spot rate going forward. Therefore, this strategic preliminary engagement will enhance CPK's budgeting and pricing process going forward. CPK has also increased its liquidity position by entering into two new credit facilities, which were structured to increase the total loan capacity available from PNC Bank, N.A. from $40M to $79.1M. CPK's low price to book ratio of 1.35 as compared to the market mean of 1.71 also helps strengthen the case that CPK is undervalued because of the market's pessimistic view on the CPK's ability to generate earnings towards book value. Because a favorable valuation, agreeable state and local regulation, and strategic geographical growth initiatives, it is recommended that CPK be added to the AIM Equity Fund with a target price of $35.50, an upside return potential of 16%.

Investment Thesis

- **Capital Expenditures.** CPK has budgeted $53.9 million for capital expenditures for 2010. This amount includes $49.2 million for the regulated energy segment, $3.3 million for the unregulated energy segment and $1.4 million for the "Other" segment. This is a 107% increase in capital expenditures year over year from 2009 levels of $26.6M. This improvement in infrastructure will help CPK to promote top line growth in future years through increased distribution capacity. Since CPK is able to maintain quality levels of returns on equity, with such high allocations to capital expenditures, they should be able to return 8-10% on these investments in the future through favorable rate requests to state and local regulators.
- **Rate Increases.** Favorable rate increases for CPK will allow for substantial increased revenue growth going forward. CPK filed a petition recently for a rate increase in Florida which was

approved on a permanent basis for an increase of approximately $2.5 million, applied to all of their meters after mid-January 2010. Meanwhile, FPU's natural gas distribution operation requested and received a permanent rate increase of approximately $8.0 million which will increase net income by $3.84M annually.

- **Merger with Florida Public Utilities.** CPK just recently finished a stock for stock merger with Florida Public Utilities (FPU) costing $75.7M. This merger gives CPK an expanded distribution range in Florida. The merger has allowed CPK to maintain their current business model, but has also allowed the firm to diversify their business model into electrical production. The merger has helped to grow the customer base to 200,000. This is an almost 100% increase from pre-merger levels. The most important part of this merger is that it will not diminish earnings; CPK management has stated that the merger should be neutral to slightly accretive in 2010 and significantly accretive in 2011.

Valuation

To find the intrinsic value of CPK, a ten-year DCF was conducted. Sales growth rates were kept nearly steady in line with management's estimates (Years 1-5: 5%, Years 6-10: 2.75%) that sales would stabilize in the near future. Using a conservative WACC of 8.39% and a terminal growth rate of 3.00% yielded an intrinsic value of $35.85. Implementing a sensitivity analysis accounting for variations in the WACC (7.50-9.50%) and long-term growth rate (1.75-3.75%) yielded a price target range of $27.25 to $51.77. Using historical price earnings multiple of 15x a 2010E EPS of $2.36 yields a $35.40 price target. Given the valuations generated by a P/E and DCF approach combined with an attractive dividend yield of 4.50%, a price target of $35.50 was determined.

Risks

- **Weather.** A significant portion of CPK's natural gas and propane distribution revenues is derived from the sales and deliveries of natural gas and propane to residential and commercial heating customers during the five-month peak heating season (November through March). If the weather is colder or warmer than normal, CPK will sell and deliver more or less natural gas and propane to customers, and earn more or less revenue. In 2009 an overall decrease in temperature of 7% occurred versus 2008. This computed into a $1.6M increase in gross margin for CPK's regulated energy and unregulated energy operations on the Delmarva Peninsula in 2009 compared to 2008. Such a deviation from the normal temperature cannot be counted on to reoccur on a regular basis.
- **Collective Bargaining Agreement.** CPK currently employs 757 employees, of whom 162 are union employees represented by three labor unions: the International Brotherhood of Electrical workers, the International Chemical Workers Union and United Food and Commercial Workers Union, all of whose collective bargaining agreements expire in 2010. Given the political and bureaucratic conflicts that could occur when the bargaining agreements expire, substantial operational and financial problems could occur as a result of potential tactics by both parties.
- **BravePoint.** BravePoint is CPK's IT consulting business, responsible for technology-related business services and solutions. It is not a typical addition to a utility's business model. BravePoint has provided negative operating income for the past two years. From 2008 to 2009, income dropped from -$35K to -$1.32M a 3900% decrease. From 2007 to 2008 it fell by -103%. If BravePoint was discontinued or divested it would increase shareholder value by $0.14 per share.

Management

John R. Schimikaitis is the CEO of Chesapeake Utilities Corporation. He also serves as Vice Chairman of the board of directors. He was recently appointed Vice Chairman on Mach 1, 2010, but has been CEO since 1999. He has over 37 years of experience in the utility industry serving for 22 of those years in a multitude of capacities at CPK.

Ownership

% of Shares Held by All Insider and 5% Owners:	4%
% of Shares Held by Institutional & Mutual Fund Owners:	41%

Source: Yahoo! Finance

Top 5 Shareholders

Holder	Shares	% Out
Vanguard Group Inc.	390,438	4.14
Blackrock Institutional Trust Co.	294,493	3.12
Dimensional Fund Advisors, LP	225,328	2.39
Gamco Investors Inc	218,614	2.32
State Street Corp.	217,749	2.31

Source: Yahoo! Finance

Neutral Tandem Inc. (TNDM)
April 23, 2010

Aaron Socker — Domestic Telecomm

Neutral Tandem Inc, (NASDAQ:TNDM) provides interconnectivity services to competitive carriers, including wireless, wire line, cable, and broadband telephony companies. Competitive carriers use tandem switches to interconnect and exchange local and long distance traffic between their networks without the need to establish direct switch to switch connections. TNDM's major customers include Sprint Nextel (23% of revenue) and AT&T (14%). Before Neutral Tandem's services were offered carriers exchanged traffic indirectly through the tandem switches of Incumbent Local Exchange Carriers, ILECs. ILEC's charge per minute rates and access charges for inter and intra-state calls. TNDM enables carriers to exchange traffic between their networks without having to use an ILEC tandem for both local and long distance calling. It is a cheaper and more reliable alternative to the traditional ILEC method, offering increased network efficiency and traffic.

				FY: Aug	2009A	2010E	2011E
Price ($): (4/19/10)	16.81	Beta:	1.00	Revenue ($Mil)	169.00	191.00	208.00
Price Target ($):	21	WACC	10%	% Growth	40.00%	13.00%	9.00%
52WK H-L ($):	14.50-34	L-Term Rev. Gr Rate Est:	3%	Gross Margin	70.00%	68.00%	67.00%
Market Cap (mil):	565.00	L-Term EPS Gr Rate Est:	3%	Operating Margin	37.50%	36.00%	35.00%
Float (mil):	33.6	Debt/Equity:	0.0%	EPS ($Cal)	1.24A	1.3E	1.42E
Short Interest (%):	11.0%	ROA:	17.7%	FCF/Share	$1.10	$1.20	$1.27
Avg. Daily Vol (mil):	0.65	ROE:	19.6%	P/E (Cal)	13.7	13.07	12
Dividend ($):	0.00			EV/EBITDA	9.8x	8.8	7.9
Yield (%):	0.0%						

Recommendation

TNDM has a market capitalization of $565 million with 2009 earnings of $41.3 million (YoY increase of 72%), giving shares a trailing P/E of 13. TNDM also has no long term debt and boasts $162 million in cash on its balance sheet, roughly $4.80 in cash per common share. TNDM increased its EBITDA margin in Q4 2009 to 50%, an increase of 200 basis points over the year prior. As increasing competition has arisen in TNDM's line of business, their sheer size, network efficiency, and solid management has helped to offset any decrease in prices, as shown in its EBITDA margin improvement. Furthermore, the company's earnings have increased in each of the past eight quarters despite the downturn in the economy and the company is trading near its 52 week low of $14.50. While TNDM continues to improve its network capacity and attract new customers, management has also embarked on a new Ethernet exchange program by teaming up with Cisco Systems, allowing TNDM to offer and market Ethernet connectivity to current and future customers. The Ethernet market is estimated to be worth $42 billion by 2014, the new product line could eventually dwarf TNDM's current business. Based on TNDM's current business model and bright prospects in its new Ethernet exchange program, it is recommended TNDM be added to the AIM Equity Portfolio with a price target of $21.00, offering a potential upside of 23%.

Investment Thesis

- **Size of Network.** As of Q4 2009, TNDM connects 1,804 competitive carrier switches (a 26% YoY increase), creating up to 3.2 million switch to switch routes serving an estimated 480 million telephone numbers assigned to these carries. The expansion in network capabilities allowed Neutral Tandem to support 23.8 billion traffic minutes in Q4. The increase in network capacity and market share are positively reflected in the company's bottom line as operating income grew by 85% from $35.4 million in 2008 to $64 million for fiscal 09.
- **Wireless Communication Expansion.** In the 2009 CTIA (International Association for the Wireless Telecomm Industry) report, wireless usage minutes exceeded 1.1 trillion in the first half of 2009. As of June 2009 the industry survey recorded more than 276 million wireless users (a

YoY increase of 14 million). With a continuing shift to wireless communications, the traditional ILEC networks are becoming obsolete and telecomm competitors are switching to TNDM's product for reliable network exchange. AT&T, Verizon, Qwest, and Embarq, the four largest ILECs (Incumbent Local Exchange Carrier) in the U.S., reported total access line losses of 11.3 million in 2009, a decrease of 9.4%. The ILEC's are being phased out.

- **Share Buyback Program/International Prospects.** With over $162 million in cash on the balance sheet at end of fiscal 09, the company is embarking on a $25 million share buyback program as management recognizes the undervaluation of its stock and attempts to return cash to its shareholders. Management is also committed to expanding the network to have international capabilities which would include exchanging traffic that originates outside the U.S and terminates in the U.S. to the telephone numbers and carriers they serve. Also, if the company is able to negotiate contracts with international carrier providers, it will be able to expand its network and grow in an untapped market with strong prospects.

Valuation

TNDM is currently trading at 13.55x 2009 EPS of $1.24. Applying a 15x multiple to the estimated 2010 EPS of $1.30 produces a relative valuation of $19.5. A 10 year DCF analysis with a computed WACC of 10.2% and a terminal growth rate of 3%, an intrinsic value of $20.92 was obtained for TNDM. A sensitivity analysis that adjusts for both the long term growth rate (2%-4%) and WACC (9.2%-11.2%) generates a price range of $18.50-$25.39. Based on these calculations, a price target has been set at $21.00. With the stock currently trading at $17, the $21 price target presents an upside potential of 23%.

Risks

- **Regulation.** The telecommunications business is subject to varying degrees of federal and state regulations. Neutral Tandem operates as a common carrier and is therefore subject to the jurisdiction of both federal and state regulatory agencies. These agencies have the authority to review prices, terms, and conditions of service. The regulatory agencies can exercise control over prices and services to varying degrees, and impose various obligations such as reporting payment of fees and compliance with consumer protection and public safety requirements. While these regulations do not impose serious headwinds, it can impact TNDM's pricing benchmarks.
- **New Competitors.** Well funded and well connected competitors could build a similar network to that of TNDM and steal contracts with some of the large scale carriers. Nonetheless, TDNM is very established to manage any competitor threat through its superior technology and breadth of offerings. For example, Neutral Tandems biggest competitor, Peerless Networks, currently operates in 10 markets compared to Neutral Tandems 137.
- **Patent Infringement.** Peerless Networks, a direct competitor, has brought into question the validity of a patent regarding the company's connectivity capabilities. The patent is being revised and may become invalidated. The direct fees TNDM faces are litigation and court costs. However, with potential ethernet and international developments in the works, the company can generate revenues from other areas if their market share is eroded. Furthermore, their competitors would have to offer lower pricing options than TNDM to generate growth. TNDM will be able to counter these price reductions because competitors will need additional capital to expand their networks to operate with the efficiency and reliability of TNDM.

Management

Rian J. Wren, President and Chief Executive Officer, is a telecommunications industry veteran and IP telephony. Before joining Neutral Tandem Inc. in 2006, Mr. Wren served as senior Vice President and General Manager for Comcast Cable where he was responsible for the delivery of telephony services for the country's leading cable and telecommunications provider. He is also a winner of the Ernst and Young Entrepreneur of the year award for 2007.

Ownership

% of Shares Held by All Insider and 5% Owners:	11%
% of Shares Held by Institutional & Mutual Fund Owners:	>90%

Top 5 Shareholders

Holder	Shares	% Out
Wells Fargo & Company	2,670,447	7.94
Next Century Growth Investors LLC	2,352,282	6.99
BlackRock Fund Advisors	1,407,176	4.18
Eagle Asset Management Inc.	1,356,275	4.03
UBS O'Conner LLC	1,265,000	3.76