Idea

CONRAD INDUSTRIES INC (CNRD) - $36.25
Posted on 12/23/13 11:52 AM by bentley883

Description

Investment Overview: Conrad Industries is a classic "Magic Formula" small/micro cap stock (moderately high ROIC and attractive earnings yield), that I believe is sellir option on a legal claim and has a reasonable margin of safety. The Company has: a 16% ROIC, rich cash flow business model, rock solid balance sheet (with cash cons growth prospects and a shareholder friendly management team that has proven to be a good allocator of capital. While the share price has outperformed the recent m at an attractive valuation on a number of measures: including a EV/EBITDA multiple of 4x, a FCF/EV yield of 17% and a cash adjusted P/E of 6.4x, all on ttm results. Wh growth during the next 18-24 months, at current share prices investors are not paying for this growth. I believe the shares are selling about 20%-25% below intrinsic of 25%-35%.

Company Profile: Conrad Industries, established in 1948 and headquartered in Morgan City, Louisiana, designs, builds and overhauls tugboats, ferries, liftboats, barg products for the oil & gas, commercial and government markets. The company provides both repair and new construction services at its five shipyards located in southe and repair, are used primarily in the domestic inland waterways or the intracoastal waters of the Gulf of Mexico.

Statistics:

Symbol: CNRD

Date: 12/23/13

Price: $36.25

Avg. Daily Volume: 6,120 shs.

Market Cap: $216M

Net Cash/(per share): $47M ($7.88)

Enterprise Value: $169M

TTM Revenues: $277.2M

TTM EBITDA: $42.2M

TTM FCF: $28.6M

TTM EPS: $4.43

Key Investment Points: The following points underscore my opinion as to why the share price is attractive and selling below intrinsic value:

A Good & Sustainable Business: Conrad has a ~65 year history of operations and has grown from a single shipyard to five locations through a combination of internal Company has invested heavily and successfully diversified its business to build/repair a broader range of vessels and service a more diversified range of customers. His industry in the Gulf of Mexico. In the 2003/04 time frame the company embarked on an effort to both expand its capacity and diversify its business to new customers. U industry growth slowed significantly during this time. This resulted in the company recording meaningful losses during this period. However, the end result of these effo company with a broader and well balanced customer base. The importance here is that these different customers not only provide more growth opportunities, but they during an industry downturn in a particular sector. This was clearly evident during the recent 2008/09 downturn, helping the company remain profitable and able to ge diversification efforts in the last few years to target the inland waterways market and commercial customers has been a major catalyst to the Company’s growth.

Conrad Industries, Inc
Customer Segments

	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	9 Mths. 2013
Revenues:													
Oil & Gas	31,332	24,368	12,369	12,658	14,610	55,429	72,976	52,349	28,262	14,439	17,252	37,848	60,239
Government	5,488	8,164	16,447	13,995	25,341	19,492	10,955	27,130	26,964	19,577	42,637	17,990	648
Commercial	10,084	8,492	4,613	10,468	24,695	46,902	84,605	111,576	88,966	104,825	186,566	177,792	155,024
Total Revenues	46,904	41,023	33,429	37,121	64,646	121,823	168,535	191,054	144,192	138,841	246,454	233,630	215,911
% of Total Revenues:													
Oil & Gas	66.8%	59.4%	37.0%	34.1%	22.6%	45.5%	43.3%	27.4%	19.6%	10.4%	7.0%	16.2%	27.9%
Government	11.7%	19.9%	49.2%	37.7%	39.2%	16.0%	6.5%	14.2%	18.7%	14.1%	17.3%	7.7%	0.3%
Commercial	21.5%	20.7%	13.8%	28.2%	38.2%	38.5%	50.2%	58.4%	61.7%	75.5%	75.7%	76.1%	71.8%
Growth:													
Oil & Gas		-22.2%	-49.2%	2.3%	15.4%	279.4%	31.7%	-28.3%	-46.0%	-48.9%	19.5%	119.4%	193.8%
Government		48.8%	101.5%	-14.9%	81.1%	-23.1%	-43.8%	147.7%	-0.6%	-27.4%	117.8%	-57.8%	NM
Commercial		-15.8%	-45.7%	126.9%	135.9%	89.9%	80.4%	31.9%	-20.3%	17.8%	78.0%	-4.7%	14.3%
Total Revenues		-12.5%	-18.5%	11.0%	74.1%	88.4%	38.3%	13.4%	-24.5%	-3.7%	77.5%	-5.2%	25.3%

While the business is somewhat cyclical and impacted by general economic conditions in the region as well as business conditions in the oil & gas markets. The Compa region and has "Jones Act" protection from foreign manufacturers. Conrad has a history of healthy growth and conservative management. The Company has an attract healthy FCF generation.

Industry Tailwinds Driving Growth: While general economic conditions influence demand for the Company's products and services, there are two significant tailwinds of the on-going oil & gas boom in the Midwest and the transportation of product inland via barges. An aging US inland barge fleet (some reports indicate the average a focused on retiring old vessels and upgrading the fleet to new double hulled and larger capacity barges. The research I have done suggests that this factor should con next 12-18 months. Noteworthy in this regard are the comments from senior executives of Kirby Corp (KEX), a leading provider of marine transport services for the inla

Joseph Pyne - Chairman, President and Chief Executive Officer: *"The marine business is a cyclical business. I've been in it over 35 years and I am seeing not a number of c it's different because, for about 30 of those years, we were essentially in a very slow growth business, business that would grow at about GDP and maybe a little less GDP. Wi oil, gas condensate and the significant improved compatibility of the chemical business on a global basis, you have demand that frankly I don't think that we've seen in this bu to be different here because you've got volumes that are actually growing. Now, with respect to which inning you're in, I think that you could make a pretty good argument tha maybe a little further along on the inland business, the only qualifier I'd put there is that on the coastal side, you're really not building much equipment, on the inland side you absorbed as we speak."*

Gregory Binion - President, Marine Transportation Group: *"In terms of announced construction….. even, if we were to start tomorrow, you're talking almost two years, befo this."*

The second tailwind that the Company is benefiting from has been the recent resurgence in business from oil & gas customers (primary for higher margin repair work). permit restriction in the Gulf of Mexico following the BP Deepwater Horizon oil spill in April 2010. Following the accident, permitting for new deep water exploration was restrictions were adopted. Data from the US Bureau of Safety Environmental Enforcement (which was formally established on October 2011 as part of a major reorgani structure), show the number of revised new deepwater (>500 feet) exploration permits in The Gulf of Mexico were 3, 127, 283 & 319 in the years 2010, 2011, 2012 & 2

http://www.bsee.gov/Exploration-and-Production/Permits/Status-of-Gulf-of-Mexico-Well-Permits/

In addition, data from the Baker Hughes Offshore Rig Count Report shows the increase in exploration activity in the Gulf of Mexico. For the full year to date, the averag basis. The following is a link to the report/chart:

http://gis.bakerhughesdirect.com/Reports/YearToYearCompChart.aspx?chrtName=rigOffshoreChrt

The impact of this increase in oil & gas exploration in the Gulf of Mexico has had a favorable impact on Conrad's revenues from this segment of customers, which until r Revenues from oil & gas customers, which had dropped to ~5% of revenues in 2011/12, now constitute ~25%-30% of revenues during 2013. These customers tend to business, which tends to have higher margins than it's new construction business.

As a result of these favorable tailwinds to demand, Conrad has seen a significant increase in its order backlog, which as of the latest report, is up ~50% y/y and now s the domestic economy, another potential driver of future demand would be rule changes to allow barge transportation of fracking waste, which the U.S. Coast Guard is

Conrad Industries
Backlog vs. Revenue Trends

Date	Backlog ($M)	ttm Backlog ($M)	ttm Revenue ($M)	ttm Bklg./Rev.
11/13/13	188.3	162.0	69.3	234%
Q3 -2013	152.3	145.1	69.3	209%
Q2 - 2013	181.8	133.1	64.3	207%
Q1 - 2013	125.5	100.7	60.8	166%
Q4 - 2012	120.7	87.0	58.4	149%
Q3 - 2012	104.4	68.6	58.8	117%
Q2 - 2012	52.2	64.5	58.5	110%
Q1 - 2012	70.8	73.6	58.8	125%
Q4 - 2011	47.1	84.0	61.6	136%
Q3 - 2011	87.7	94.6	55.8	170%
Q2 - 2011	88.7	94.2	48.7	193%
Q1 - 2011	112.3	82.2	43.3	190%
Q4 - 2010	89.5	66.4	34.7	191%
Q3 - 2010	86.1	53.6	32.4	165%
Q2 - 2010	41.0	46.1	32.4	142%
Q1 - 2010	48.9	45.9	30.8	149%
Q4 - 2009	38.3	42.2	36.0	117%
Q3 - 2009	56.1	50.6	41.2	123%
Q2 - 2009	40.4	55.3	44.3	125%
Q1 - 2009	34.1	68.7	49.4	139%

New Additions To Capacity Coming On-line: Over the last 24 months the Company has invested a significant amount of its FCF back into the business in the form of g manufacturing & repair capabilities and increase its efficiency. In the 10 years prior to 2012, cap-ex averaged about $4.5M per year (combination of maintenance & gro $15M in cap-ex and this year the amount should be ~$20M. Highlighting the investments the Company has been making during the last 24 months, cap-ex has been r equipment purchases, refurbishments and enlarging its dry-docks, as well as building an indoor construction facility, the company purchased a new parcel of land adjac While this new facility will add to Conrad's revenue generating capabilities, it will enable the Company to construct and repair bigger vessels and expand its business t on-line in 2H of this year, which should help Conrad turn its growing backlog more rapidly into revenues. While management has not discussed its cap-ex plans for 201 impacting FCF generation.

Cash Rich Balance Sheet: Given the combination of a conservative management team coupled with the Company's healthy FCF generation, Conrad has a rock solid ba investments made in growth cap-ex over the past two years, along with the payment of a special dividend and some share repurchases, the Company's net cash posit September quarter net cash had grown to $9.88 per share; representing ~28% of the current share price. Following the payment of a $2.00 per share special dividenc to $7.88 (excluding potential FCF generation during Q4), or ~22% of the share price.

In addition to a rock solid net cash position, I believe that Conrad's book value could be somewhat understated by the value on the books of the Company's land holdi (in 2003, 52 acres were purchased for $1.3M, while in 2012, 50 acres were purchased for $5.6M) and Conrad's accounting for land dating back a couple of decades on value may be conservative. This would make the Company's assets more valuable to any outside interested party.

Free Call Option On Potential Legal Claim: In December 2012 and February 2013, the Company submitted claims totaling $22.6 million to the BP Settlement Fund in a Settlement Program. Certain of the Company's businesses are located within the economic zones included in the class settlement. The outcome and timing of when the delayed. Originally management had expected a resolution by the end of 2013. Recent indications from press reports suggest that BP has objected to the formula usec from each company filing a claim. Thus, while full or partial payment is uncertain, the potential award ($3.79 pre-tax) could provide a meaningful increase to cash balan management would consider another special dividend to shareholders.

Conservative & Shareholder Friendly Management: The Conrad family owns 47% of the stock and three generations of the family are in the management ranks, with John P. Conrad (age 70) CEO & Co-Chairman. Thus, given that management is not overpaid and does not have a lot of stock options, they are very much aligned with s From my perspective, management is somewhat conservative and backed by past history, not likely to do anything stupid with the cash (i.e. a big acquisition or move a record of capital allocation and being shareholder friendly. In the past the Company has reinvested its cash back into the business or made timely acquisitions of a few returns. Also, management has used excess cash to repurchase shares and pay two special dividends (in 2012 and 2013). The only criticisms that can be made of man reasons) and to not hold quarterly conference calls or give investor presentations (to focus on running the business). However, the Company's financial reports contair open to discussions of the business fundamentals.

A noteworthy point regarding management is the age of both J. Parker Conrad and John P. Conrad. While there is a third generation Conrad working at the Company, management succession plan and if/how soon he would be ready to run the business. This raises the possibility of a potential sale of the Company (something manag the future. Sources I have spoken with indicate that given the Company's excellent reputation and presence in the industry/region, there would likely be interested bu

Financial History & Projections: Conrad's historic annual P&L results along with my forecasts are illustrated in the following table. The numbers show the cyclical natu results were caused by a number of additional factors. From the 1999 period when Conrad operated just two facilities and was focused primarily on the Gulf of Mexico years was driven by: an expansion in the number of facilities, moving its dry docks to larger facilities, broadening the product mix (including a move into the aluminum v expansion efforts coincided to some degree with the post-9/11 downturn in the economy and weakness in the oil & gas industry during the late 2001 thru 2004 period combination of improved economic conditions, higher oil & gas prices and the impact of hurricanes Katrina, Rita, Gustav and Ike combined to create an unusually strong the economy, financial/credit crisis in late 2008 and continued soft following the Deepwater Horizon accident and subsequent weakness in the oil & gas industry in 201 diversification into the inland market and the addition of new capacity has helped fuel a significant recovery in the Company's business beginning in 2011.

Looking out to the future, given the combination of the tailwinds fueling the Company's demand coupled with its record backlog and new capacity coming on-line, it is r current Q3 (September) quarter levels in future quarters. However, in an effort to maintain a conservative posture (and a margin of safety), I have chosen to use a no value investor, I like growth, but don't want to pay for it if possible. Given that the Company's backlog is at record levels on both an absolute basis and as a percent of decline from current levels over the next few quarters. From the standpoint of profitability, both 2013/14 should result in record EPS on both a GAAP and operating cas ~$4.20 per share) as cap-ex spending will likely decline to a level slightly above maintenance cap-ex levels. The following tables illustrate my GAAP and FCF estimated scenario.

Calendar Year
Conrad Industries

	2002A	2003A	2004A	2005A	2006A	2007A	2008A	2009A	2010A
Net Sales	$41,023	$33,429	$37,121	$64,646	$121,823	$168,535	$191,054	$144,192	$138,8
Cost of Goods	35,657	32,770	37,104	60,577	107,530	133,282	149,231	119,017	118,09
Gross Profit	5,366	659	17	4,069	14,293	35,253	41,823	25,175	20,749
Gross Margin	13.1%	2.0%	0.0%	6.3%	11.7%	20.9%	21.9%	17.5%	14.9%
SG & A	4,815	4,702	4,296	3,081	3,568	4,791	5,480	6,250	4,780
% of rev	11.7%	14.1%	11.6%	4.8%	2.9%	2.8%	2.9%	4.3%	3.4%
Operating Expenses	4,815	4,702	4,296	3,081	3,568	4,791	5,480	6,250	4,780

% of rev	11.7%	14.1%	11.6%	4.8%	2.9%	2.8%	2.9%	4.3%	3.4%
Operating Profit	551	(4,043)	(4,279)	988	10,725	30,462	36,343	18,925	15,969
Operating Margin	1.3%	-12.1%	-11.5%	1.5%	8.8%	18.1%	19.0%	13.1%	11.5%
D&A	1,861	2,175	2,471	2,395	2,430	2,485	3,020	3,324	3,459
EBITDA	2,412	(1,868)	(1,808)	3,383	13,155	32,947	39,363	22,249	19,428
% of Sales	5.9%	-5.6%	-4.9%	5.2%	10.8%	19.5%	20.6%	15.4%	14.0%
Impairment Goodwill	0	4,000	4,101	0	0	0	0	0	0
Termin. Acq. Costs	350	0	0	0	0	0	0	0	0
Interest Expense	(221)	(435)	(585)	(1,064)	(1,214)	(776)	(484)	(159)	(96)
Other Income (Expense)	39	36	163	172	2	440	173	771	348
Net Income Before Taxes (Reported)	19	(8,442)	(8,802)	96	9,513	30,126	36,032	19,537	16,221
Net Income Before Taxes (Operating)	369	(4,442)	(4,701)	96	9,513	30,126	36,032	19,537	16,221
Income Taxes	23	(1,613)	(1,681)	(15)	3,618	10,917	13,023	6,688	5,936
Tax Rate	121.1%	19.1%	19.1%	-15.6%	38.0%	36.2%	36.1%	34.2%	36.6%
Net Income (Reported)	(4)	(6,829)	(7,121)	111	5,895	19,209	23,009	12,849	10,285
Net Income (Operating)	346	(2,829)	(3,020)	111	5,895	19,209	23,009	12,849	10,285
EPS (reported, basic)	($0.00)	($0.94)	($0.98)	$0.02	$0.81	$2.65	$3.31	$2.00	$1.60
EPS (operating, basic)	$0.05	($0.39)	($0.42)	$0.02	$0.81	$2.65	$3.31	$2.00	$1.60
Shares Out. (FD)	7,230	7,234	7,236	7,236	7,236	7,236	6,949	6,439	6,448
Revenues									
Y/Y % Growth		-19%	11%	74%	88%	38%	13%	-25%	-4%
Operating Income									
Y/Y % Growth		-834%	6%	-123%	986%	184%	19%	-48%	-16%
Net Income									
Y/Y % Growth		170625%	4%	-102%	5211%	226%	20%	-44%	-20%

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Conrad Industries
Cash Flow Analysis & Projections

	2006	2007	2008	2009	2010	2011	2012	2103E	2014E
Net Income	5,895	19,209	23,009	12,849	10,285	19,167	20,842	24,981	26,343
D&A	2,430	2,485	3,020	3,324	3,459	3,619	4,067	4,756	5,963
Adjustments	2,844	334	1,342	324	(1,174)	1,478	(520)	(151)	0
Working Capital	952	(14,573)	3,558	(10,872)	(1,160)	5,327	18,157	121	(980)
Cap-ex	(2,230)	(5,098)	(5,892)	(4,676)	(2,901)	(4,302)	(15,293)	(21,970)	(6,000)
FCF	9,891	2,357	25,037	949	8,509	25,289	27,253	7,737	25,326

Attractive Valuation: While the stock price of Conrad has outperformed the market during the current rally, the shares are still attractively priced on a number of meas Company's expansion in the past few years, will continue to drive growth over the next 18-24 months and that the capacity additions coming on-line in 2H of 2014 will this period. However, given the cyclical nature of the business and the desire to be conservative, I can make a case that the shares are attractive based on both ttm d are valued at a EV/EBITDA multiple of 4x, a FCF/EV yield of 17% and a cash adjusted P/E of 6.4x. For cyclical companies, it is always helpful to look at how they are valu companies, Conrad was faced with a weak economy and a major financial crisis. In addition, the Company's business (especially vessel repair) was impacted by the BP exploration activities in the Gulf of Mexico and Conrad's oil & gas business. At current prices, the shares are selling at an EV/EBITDA multiple of ~7x and a cash adjuste these attractive multiples on down cycle profitability provide investors a healthy margin of safety.

Conrad Industries
Enterprise Value Calculation

Stock Price	$36.25
+ Shares Out. (mil.)	5,961
= Mkt. Cap. (mil.)	$216.1
- Cash	(60.2)
+ STD	0.3
+ LTD	1.0
+ Special Dividend	11.9
= Ent. Value (mil.)	$169.1

The Share Are Selling Significantly Below Intrinsic Value: I believe the shares are selling at about 20%-25% below intrinsic value of $45-$48 per share. In calculatir assumptions. First, while I believe the combination of a record backlog and additional capacity additions should bode well for some growth over the next few quarters, in forecasting profitability and FCF for my intrinsic value calculation. In addition, a fair amount of my analysis is based using trailing twelve month (ttm) numbers. Thus, a months and estimating the Company can conservatively generate FCF in 2014 of ~$25 million with cash reserves increasing commensurately, and assuming the share an attractive 12.5% yield) would equate to a share price of ~$46.50 per share. Note assuming a multiple of 10x (or a 10% yield) would equate to a share price of ~$5!

Conrad Industries
Potential Share Price Analysis
($ million)

Current Cash	60.2
- Special Dividend	(11.9)
- STD	(0.3)
- LTD	(1.0)
+ Q4 2013 Cash Additions	5.0

+ Cash Additions in 2014	25.0
Net Cash @ 12/2014	77.0
2014 FCF Estimate	25
Assume 8x EV/FCF Multiple	200
+ Net Cash @ 12/2014	77.0
= Market Cap.	277.0
/ Shares Out. (Mil.)	5,961
Share Price	$46.47

Relative to a private market valuation, there are not a lot of comparisons to look at. The closest comparison is the December 2011 acquisition of Seattle based Todd Sh $130 million in cash. This equated to a valuation of about 5.3x EBITDA and 9.4x EPS. However, Todd was primarily in the repair business, with limited manufacturing ca contracts. Additionally, Todd appeared to have about half the number of dry-docks and construction bays and does not appear to have made the investments that Cor financial standpoint, while the revenue base of Todd at the time of acquisition is about similar in size, Conrad has a higher return, richer FCF business model that Todd. of ~9.5% trails the mid-teens margin of Conrad and Todd's three year average FCF is about 1/3rd that of the Company. Applying the same EBITDA and EPS multiples to Noteworthy, these valuation measures were accorded in a depressed market environment, with a subsequent 45% rise in the S&P 500 index since the date of the acq business model, more modern facilities, more diversified customer base, the improved economy and a higher public market, I believe it is reasonable to accord some pr

Thus, when triangulating this data, it leads me to an intrinsic value for Conrad of $45-$48 per share, which represents upside potential of 25%-35%.

Why Are The Shares Mis-Priced?: I believe the shares are mis-priced due to the following: non-SEC filer (due to cost issues, but they release all financials), no confer side analyst coverage (i.e. they don't need investment banking) and that the Company does not screen well due to temporary growth cap-x cycle in 2012/13 (likely en

Risks: Another economic downturn, a significant/prolonged drop in WTI oil prices, a sharp rise in steel prices, competitive pricing pressures, loss of a major customer (t weather event (i.e. hurricane).

I do not hold a position of employment, directorship, or consultancy with the issuer.
I and/or others I advise hold a material investment in the issuer's securities.

Catalyst

- Continued growth in earnings and cash flow.
- A reduction in growth cap-ex, which will aid free cash flow and help the stock screen better.
- A favorable resolution from the Company's legal claim regarding the BP Deepwater Horizon oil spill.
- Possible sell-side analyst coverage.