Mossberg's Investor Digest

Best Idea Profile: **Quanex Building Products Corporation (NYSE:NX)**

DESCRIPTION:

Quanex Building Products Corporation makes energy-efficient building products, primarily vinyl window and door profiles for residential use. It focuses on providing original equipment manufacturers with products for key end markets of residential repair and remodel and new home construction. Quanex has 22 plants in the U.S., primarily focused in the Midwest and the West Coast, and one each in the U.K. and Germany. Founded in 1927, Quanex sold its steel business in 2008 in order to focus on residential building and construction, growing through internal expansion and acquisitions. The company is based in Houston and employs 2,200.

KEY INVESTMENT CONSIDERATIONS:

Industry Still Chugging – Housing starts for 2014 showed a 7% increase, rather than the original 19% predicted by industry analysts. Consensus says that 2015 should see housing starts increase 17%, although Quanex expects it will be much like 2014. Quanex expects growth in the industry will approach 8%. The company's guidance for 2015 is possibly conservative, given it was burned by its previous optimistic outlook.

Putting Money in Vinyl – Management's number one priority is to correct its laggard investment in the vinyl business. Because of its belief in the long-term future of the vinyl business, it expects nearly two-thirds of its $35 million capital expenditures in 2015 will be in this market, as it is replacing or refurbishing the vast majority of its vinyl extrusion lines. The lack of previous upgrades to its infrastructure and equipment caused a "big bump in the road" for the company, but one that is soon to be resolved. Although a slower than expected process, this investment will allow Quanex to return to its historical levels of profitability in 2016.

Looking for Acquisitions – Management is eyeing domestic and international acquisitions, while also looking to expand its product offerings and market reach. They are looking at acquiring vertically integrated assets from customers and other opportunities within this space; however, there are no transactions in the near horizon.

Hurt by Rising Material Costs – Quanex's contracts last year did not account for the rising cost of resin, and therefore, it was not able to pass on these costs. The company has completed, or has in process, new contracts that will correct this costly mistake. In 2015 it will be able to pass on rising material costs with no expected detriment to revenues or customer retention.

Paying Shareholders – Management indicated its intent to increase its quarterly dividend. It also announced a $75 million stock repurchase program in September, with two-thirds of that spent to date. However, whether this buyback will be extended once it is complete will depend largely on the outlook for its seasonally busy summer months, which will be more apparent closer to mid-year. Quanex also demonstrates its shareholder-friendly governance in its compensation philosophy: mid-range salaries with incentives highly dependent on results.

VALUATION:

Despite the company's expectations of a slow start in the first half of 2015, Quanex holds excellent market position in a recovering market, with expectations for substantial long-term gains in profitability. Management's guidance is for a slow first half with fiscal revenue up 5% to 7%, and EBITDA margins expanding to 9.5%. Longer term margins will likely be closer to 15%. Cash and very little debt can support future acquisitions or an expanded buyback program.

Quanex Building Products Corporation (NYSE:NX)
Investment Data (as of 1/16/15)

Recent Price	**$18.90**
52-Week Range	$16.50 - $21.42
Fiscal Year End	Oct. 31
Dividend	$0.16
Yield	0.8%
Shares Outstanding	37.3 M
Average Trading Volume (3 mos)	258 K
Market Capitalization	$705 M
Cash	$120 M
Long-term Debt	$785 K
Enterprise Value (EV)	$561 M
Book Value	$11.91
TTM Revenue	$595 M
P/ Revenue	0.7 x
TTM EPS	$0.78
P/ EPS	24.4 x
TTM EBITDA	$52 M
EV/ EBITDA	10.9 x

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