

Mossberg's Investor Digest

Best Idea Profile:

Schnitzer Steel Industries (NASDAQ:SCHN)

DESCRIPTION:

Schnitzer Steel Industries collects, processes and sells steel, which is the world's most recycled product. The metals recycling business collects and recycles vehicles, rail cars, home appliances, industrial machinery, manufacturing scrap, and construction and demolition materials. The auto parts business buys used vehicles and sells parts to retail and wholesale customers before supplying the remaining auto bodies to its metals recycling business. This then supplies nearly 100% of the metal used in the steel manufacturing business to produce high-quality reinforcing steel and wire rod used in new construction. Schnitzer was founded in 1906. It operates 116 recycling facilities, including seven deep-water ports. Its corporate headquarters are in Portland, Oregon

KEY INVESTMENT CONSIDERATIONS:

Synergistic Business Model – Schnitzer has one of the largest salvage auto parts providers in the U.S., as well as one of the largest recyclers of scrap metal. It collects used auto parts and scrap metal through 120 facilities located primarily on deep-water ports such as along the east and west coasts of the U.S., Hawaii and Alaska. Schnitzer's own auto parts business is its largest supplier, as it purchases 350,000 cars per year. It sells usable parts, from engine components to windshields and tires, through retail stores that charge an entry fee to the scrap yard. Schnitzer then recycles nonferrous parts and crushes the car body to send to Schnitzer's metals recycling facilities to be sent to customers. It recycles more than four million tons of ferrous metal and more than 500 million pounds of nonferrous metal annually.

Emerging Demand – The U.S. is the largest source of supply for unprocessed scrap metal, yet the largest demand for processed scrap metal comes from emerging economies and industrial hubs, such as China, South Korea, Taiwan, and Turkey. The growing but fluctuating demand is easily accommodated by Schnitzer's broad geographic reach. It can respond to the region with the greatest current demand because of its global footprint. Demand from emerging countries will continue to fuel the need for metal.

Balance Offsets Cyclicity – Higher volumes in operating income in auto parts and steel manufacturing, which is Schnitzer's third line of business, partially offset the impact that declining commodity prices and volumes had on metal recycling. Steel manufacturing is experiencing its highest utilization since 2008 and the

company is beginning to benefit from productivity initiatives, cost reductions, and execution of synergies between its auto parts and metal recycling businesses. Management estimates that capital expenditures for fiscal 2014 will be 50% lower than fiscal 2013.

Return to Shareholders – Schnitzer has paid a dividend every quarter since it went public in 1993. It significantly increased the dividend in 2013 and is currently yielding approximately 2.9%

Supply Trends Favorable – Several economic factors in the U.S. point to a good supply of steel: strong domestic auto sales, increasing appliance shipments, recovering consumer spending, and higher construction spending

VALUATION:

This stock has a lot of upward potential as it benefits from efforts of productivity improvements, more synergies between its businesses, and improved global economic growth and outlook. The almost 3% yield is an attractive incentive to wait on this revival.

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Investment Data (as of 7/25/14)

Recent Price	\$27.35
52-Week Range	\$24.13 - \$33.32
Fiscal Year End	Aug 31
Dividend	\$0.75
Yield	2.9%
Shares Outstanding	27 M
Average Trading Volume (3 mos)	264k
Market Capitalization	\$734 M
Cash	\$29 M
Long-term Debt	\$376M
Enterprise Value (EV)	\$1.1 B
Book Value	\$28.51
TTM Revenue	\$2.5 B
P/ Revenue	0.3x
TTM EPS	\$(10.95)
P/ EPS	NA
TTM EBITDA	\$71 M
EV/ EBITDA	15x

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