

Mossberg's Investor Digest

Best Idea Profile

Haynes International (Nasdaq: HAYN)

DESCRIPTION:

Headquartered in Kokomo, Indiana (about 60 miles north of Indianapolis), Haynes International is one of the world's largest producers of high-performance nickel and cobalt-based alloys for use in corrosion and high-temperature applications. The company's alloys are used in solar power generators, gas turbine engines, aerospace applications, the chemical processing industry, and other applications. The company has manufacturing in Indiana, Louisiana and North Carolina and worldwide distribution with 15 sales locations in the U.S., Europe and Asia. Geographic revenue split is 54% in North America, 26% in Europe, and 20% in Asia and the rest of the world. The company has approximately 940 employees.

KEY INVESTMENT CONSIDERATIONS:

Well positioned to weather an extended downturn and prosper in an industrial recovery – All three of the company's end markets, aerospace, chemical and power generation have been hit hard by the current economic downturn, resulting in a 26% decline in sales during the first nine months of the company's fiscal year. While sales and profits have declined significantly, the company has cut costs, improved efficiencies and should be able to operate near breakeven at current sales levels. In addition, the company has been pairing down inventory levels, generating strong cash flows and bolstering the balance sheet in the process. Cash flow from operations was \$97 million during the first nine months of the year, largely due to the reduction in inventory. The balance sheet is strong with \$84 million in cash and no long term debt. Capex needs are limited to approximately \$10 to \$12 million this year and should be easily funded through operations. High fixed costs businesses, such as HAYN, underperform during an economic downturn, just as they outperform during good times. The key is to survive during the downturn, which HAYN is more than capable of doing. Investors who buy quality stocks at the bottom of the cycle, should be rewarded as improving utilization and returns generate higher profits and valuation multiples.

Competitive moat – The company's proprietary alloys are protected by 17 U.S. patents and approximately 150 foreign counterpart patents. In addition to its patent portfolio, the company has unique production equipment and process technologies all of which would be very difficult for competitors to duplicate.

Long Product Lifecycles - Safety and performance standards in the aerospace (approx. 40% of revenue) and gas turbine (approx. 20% of revenue) industries require new products to be rigorously tested over long periods of time...eight to ten years in some cases. This long development cycle create significant barriers for competing products. In addition, once designed in, these products have long product lifecycles. Given the safety and performance standards, it is unlikely customers will switch suppliers just to save a few bucks.

VALUATION:

Based on peak earnings power, shares are significantly undervalued. To give a sense of the earnings power of the company, during 2006, 2007 and 2008, the company earned \$3.46, \$5.89 and \$5.22 per share, respectively. Of course this was at the peak of the cycle and utilization rates were much higher. While earnings are not expected to rebound sharply in the near term, for patient long term holders, shares appear attractive. Also, with its balance sheet and strong cash flow generation capability, HAYN could be a buy out candidate for a strategic buyer, or even private equity. (Blackstone owned the company in the late 90's) There should be some downside support for the stock, as shares are trading near par with tangible book value. Also, the company might consider deploying its excess cash to repurchase shares, which would provide further downside support.

(Nasdaq: HAYN)

Investment Data (as of 11/19/09)

Recent Price	\$26.51
52-Week Range	10.92 - 34.99
Fiscal Year End	September
Shares Outstanding	12 MM
Average Trading Volume (3 mos)	75,000
Market Capitalization	318 MM
Cash	84MM
Long Term Debt	N/A
Enterprise Value (EV)	234 MM
LT Debt/ Equity	N/A
BV/ Share	26.72
TTM Revenue	514 MM
P/ Revenue	0.6x
TTM EPS	-2.75
P/ EPS	nmf
TTM EBITDA	25 MM
EV/ EBITDA	9x

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