Techprecision Corporation (TPCS)

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Disclaimers

- I am not a registered investment advisor and I do not offer any investment advise
- No parts of this talk are suggestions to invest, not invest, buy or sell any kind of securities or other financial instruments

Techprecision Corporation - business

- Metal fabricated and machined precision components and equipment
  - Alternative energy - wind turbine components and components used to produce solar panels **52%** - all to GT Solar
  - Medical - components and assemblies for proton beam accelerators for cancer treatment 6%
  - Nuclear - commercial reactor internal components and temporary heads, spent fuel storage and transportation canisters and casks, and material handling equipment 6%
  - Defense - aircraft carrier steam accumulator tanks, DDX destroyer prototype propulsion equipment, gun and weapons handling equipment, submarine sonar system components, and primary shield tank heads and foundations **26%** - half to BAE Systems
  - Industrial - vacuum chambers, food processing equipment, chemical processing equipment, and pressure vessels 7%
  - Aerospace - delta rocket precision-machined fuel tank bulkheads, F-15 special equipment pods 3%

Techprecision Corporation – business (cont'd)

- 2010 sales 28M (so 1% is 280K, and 3% is 840K order)
- 134 employees - 18 administrative, 9 engineering, 107 manufacturing

- Listed through reverse merger
- RE spinoff with leasing, then rebought

- MA loan

Techprecision Corporation – Misc thoughts

- What can go wrong?
  - Defense and solar energy slowdown
  - Solar energy alternative (cheaper?) suppliers
  - Nuclear energy slowdown
- Opportunities:
  - Chinese solar energy manufacturing

Strategic considerations

- Moat (*switching costs, habit, low cost*):
  - What are the moats? Not much. Contracts?
  - What does it take to sustain the moats?
  - Bargaining power of suppliers/customers? Big: defense contractors, GT Solar
- Is it a low risk business? No.
- Is there high uncertainty? Yes
- How capital intensive is the business? Machines are cap intensive
- Future growth – saturation? Future growth possible
- Are the revenues and cash flows of the business sustainable or overstated / understated due to boom or bust conditions? Possibly understated

Management

- I don’t usually do management analysis. Included for template completeness
- Some dilution (also convertible prefs)
- Can I trust management?
- Management shareholding (> 10%)
- Management incentives?
- Are the salaries too high?
- Is there heavy insider buying?
- Is there heavy insider selling?
- Do I like the management? (Operators, capital allocators, integrity)
- Profitable reinvestment
- What has management done with the cash?
- Where is Free Cash Flow invested? Share buybacks, dividends, reinvested, ROE & ROCE, incremental BV

Piotroski Score

Only applicable to Graham Cos – N/A to TPCS

1. Net Income: Bottom line. Score 1 if last year net income is positive.
2. Operating Cash Flow: Better earnings gauge. Score 1 if last year cash flow is positive.
3. Return On Assets: Measures Profitability. Score 1 if last year ROA exceeds prior-year ROA.
4. Quality of Earnings: Warns of Accounting Tricks. Score 1 if last year operating cash flow exceeds net income.
5. Long-Term Debt vs. Assets: Is Debt decreasing? Score 1 if the ratio of long-term debt to assets is down from the year-ago value. (If LTD is zero but assets are increasing, score 1 anyway.)
6. Current Ratio: Measures increasing working capital. Score 1 if CR has increased from the prior year.
7. Shares Outstanding: A Measure of potential dilution. Score 1 if the number of shares outstanding is no greater than the year-ago figure.
8. Gross Margin: A measure of improving competitive position. Score 1 if full-year GM exceeds the prior-year GM.
9. Asset Turnover: Measures productivity. Score 1 if the percentage increase in sales exceeds the percentage increase in total assets.

- Total: / 9

Is it a good business?

- 3 year history of profits
- ROE:
  - 2009: ?? 2010:17 2011: 19
- Margins
  - 2009: 15 2010:7 2011: 8
- Dropping earnings: 3 year sales growth 0%, earnings growth -9%
- Some dilution (also convertible prefs)
- OK balance sheet
  - Debt ~= cash/short term investments
- ROIC = Earnings / (Equity + Debt – Cash) = Earnings / (Assets – non-debt liabilities - Cash)
  - ~= ROE

Is it a good business? Cash flow

- Weak operating cash flow and FCF:
  - 2011 2.7M earnings, 1.3M operating cash flow, 0 FCF (FCF = OCF – capital expenditures)
  - Free Cash Flow/Share higher than dividends paid

Is business cheap? - Buffettology calculations

- ROE 15%
- Earnings in 10 years = ROE*Equity*$(1+ROE)^9$ = $7M
- Equity in 10 years = Equity*$(1+ROE)^9$ = $49M
- Market cap = 25B x P/E (15) = $110M
- Rate of return = 14.6% after tax (calculations omitted)

- No calculation based on earnings growth

Is business cheap? DCF

- Discounted cash flow
  - Current earnings of 2.7M
  - 5% growth for 5 years, leveling after that
    - 15% discount -> $22M current valuation (if you buy company at <$23.4B, you will get 15% return or higher)
  - 5% growth for 10 years, leveling after that
    - 15% discount -> 24M current valuation
  - 10% growth for 10 years, leveling after that
    - 15% discount -> $26M current valuation
- Owner's yield = earnings / (market cap + debt - cash) = earnings/EV
  - 2.7M / (23.7M+0M) = 11%

- What makes up the margin of safety? Price?
- Is there a sufficient margin of safety? No

Is business cheap? - Graham investment considerations

- N/A for TPCS – included for completeness
- 1.7 P/Book – not a net net
- Altman Z score (http://en.wikipedia.org/wiki/Altman_Z-score)