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Computer Services & IT Consulting
North America | United States

FleetCor Technologies Inc (FLT)

Transformative Comdata Acquisition; Some Questions Come to Mind, But Clearly a Net Positive; Maintain Buy on FLT

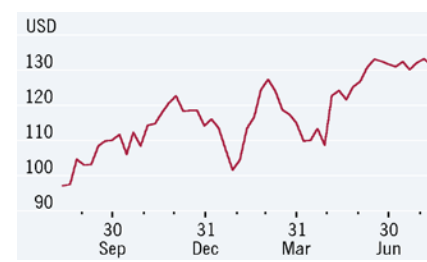
- Key Takeaway(s)** — After recent media speculation, FLT has agreed to acquire Comdata for ~\$3.5 bil. Not surprisingly, the deal is significantly accretive (adds ~9% to 2015 EPS) and mgmt. is optimistic about forward synergy opportunities. However, the deal will raise questions given Comdata's historically lower growth and FLT's long-standing preference for faster growth entities (mostly ex- US). Some may doubt FLT's ability to accelerate Comdata's growth to ~10%, but we do see some near-term opportunities for improvement and it is difficult not to give FLT the benefit of the doubt with their M&A track record. Importantly, this was a unique opportunity for FLT and puts further distance between them and their competitors in terms of size / cash flow, the latter of which should drive further shareholder value through continued M&A. By no means is this acquisition perfect, but the positives certainly outweigh the negatives in our opinion. Maintain Buy on FLT.
- Details of the Acquisition** — FLT announced that it has agreed to acquire Comdata for ~\$3.45 bil (\$2.4 bil in cash, ~\$1 bil in stock) in a deal that is expected to close in December. Comdata is a leading provider of fuel card and corporate payment solutions in the US with 2013 revenues of ~\$580 mil and EBITDA margins of ~50% (~12x EBITDA). The deal will take FLT to just over ~3x leverage at the close, but the company expects to de-lever quickly after the acquisition. The transaction is expected to add \$0.50-\$0.60 to adj. EPS in 2015. Additionally, FLT expect accelerated top-line growth, synergies and de-leveraging to contribute to ~20% EPS growth contributions from Comdata over the next few years.
- Model Impact** — FLT laid out 2015 EPS guidance of \$6.25-\$6.45, which calls for ~25% growth at the midpoint vs. 2014 guidance. This includes 13-15% core organic EPS growth and \$0.50-\$0.60 from Comdata. We believe both of these metrics can potentially prove conservative. We defer our model changes until the deal closes.
- Inside** — Further Comdata thoughts and points from our recent meeting with FLT.

EPS	Q1	Q2	Q3	Q4	FY	FC Cons
2013A	0.90A	1.00A	1.08A	1.08A	4.05A	4.05A
2014E	1.12A	1.27A	1.35E	1.38E	5.12E	5.09E
Previous	1.12A	1.27A	1.35E	1.38E	5.12E	na
2015E	na	na	na	na	5.95E	5.94E
Previous	na	na	na	na	5.95E	na
2016E	na	na	na	na	6.75E	6.55E
Previous	na	na	na	na	6.75E	na

Source: Company Reports and dataCentral, Citi Research. FC Cons: First Call Consensus.

Buy	1
Price (12 Aug 14)	US\$129.44
Target price	US\$154.00
Expected share price return	19.0%
Expected dividend yield	0.0%
Expected total return	19.0%
Market Cap	US\$10,776M

Price Performance (RIC: FLT.N, BB: FLT US)



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FLT.N: Fiscal year end 31-Dec						Price: US\$129.44; TP: US\$154.00; Market Cap: US\$10,776m; Recomm: Buy					
Profit & Loss (US\$)	2012	2013	2014E	2015E	2016E	Valuation ratios	2012	2013	2014E	2015E	2016E
Sales revenue	707,534	895,171	1,102,394	1,233,847	1,363,519	PE (x)	43.3	32.0	25.3	21.8	19.2
Cost of sales	-174,019	-202,173	-228,923	-248,297	-267,606	PB (x)	12.0	8.7	6.5	5.2	4.2
Gross profit	533,515	692,998	873,471	985,550	1,095,914	EV/EBITDA (x)	28.6	22.5	17.6	14.8	12.4
Gross Margin (%)	75.4	77.4	79.2	79.9	80.4	FCF yield (%)	1.0	3.2	3.9	4.6	5.2
EBITDA (Adj)	396,240	520,045	673,416	776,339	881,373	Dividend yield (%)	0	0	0	0	0
EBITDA Margin (Adj) (%)	56.0	58.1	61.1	62.9	64.6	Payout ratio (%)	0	0	0	0	0
Depreciation	-16,395	-20,161	-22,235	-22,420	-22,051	ROE (%)	25.1	26.4	24.2	22.1	20.5
Amortisation	0	0	0	0	0	Cashflow (US\$)					
EBIT (Adj)	379,845	499,884	651,181	753,918	859,322	EBITDA	396,240	520,045	673,416	776,339	881,373
EBIT Margin (Adj) (%)	53.7	55.8	59.1	61.1	63.0	Working capital	-170,609	-21,643	-56,401	-39,802	-42,060
Net interest	-10,738	-13,185	-18,511	-15,608	-13,208	Other	-90,171	-122,717	-159,721	-191,970	-216,928
Associates	0	0	0	0	0	Operating cashflow					
Non-op/Except	-1,121	-602	2,464	4,160	4,160	Capex	-19,111	-20,785	-24,552	-28,000	-28,000
Pre-tax profit	367,986	486,097	635,134	742,470	850,274	Net acq/disposals	-190,447	-728,343	-289,850	0	0
Tax	-111,938	-143,415	-194,916	-226,365	-257,954	Other	0	0	0	0	0
Extraord./Min.Int./Pref.div.	-39,849	-58,181	-84,950	-90,060	-93,334	Investing cashflow					
Reported net profit	216,199	284,501	355,269	426,046	498,986	Dividends paid	0	0	0	0	0
Net Margin (%)	30.6	31.8	32.2	34.5	36.6	Financing cashflow					
Core NPAT	256,048	342,682	440,218	516,106	592,320	Net change in cash	-1,510	54,456	61,587	377,550	458,686
Per share data						Free cashflow to s/holders					
Reported EPS (\$)	2.52	3.36	4.14	4.91	5.69		116,349	354,900	432,742	516,567	594,385
Core EPS (\$)	2.99	4.05	5.12	5.95	6.75						
DPS (\$)	0	0	0	0	0						
CFPS (\$)	1.58	4.44	5.32	6.28	7.10						
FCFPS (\$)	1.36	4.19	5.04	5.96	6.78						
BVPS (\$)	10.83	14.91	19.88	25.05	30.87						
Wtd avg ord shares (k)	83,328	81,789	83,044	83,921	84,871						
Wtd avg diluted shares (k)	85,736	84,651	85,899	86,742	87,692						
Growth rates											
Sales revenue (%)	36.2	26.5	23.1	11.9	10.5						
EBIT (Adj) (%)	40.2	31.6	30.3	15.8	14.0						
Core NPAT (%)	40.9	33.8	28.5	17.2	14.8						
Core EPS (%)	37.5	35.6	26.6	16.1	13.5						
Balance Sheet (US\$)											
Cash & cash equiv.	283,649	338,105	399,692	777,243	1,235,929						
Accounts receivables	823,441	922,351	1,143,769	1,274,232	1,409,951						
Inventory	0	0	0	0	0						
Net fixed & other tangibles	136,043	198,764	323,161	331,267	332,799						
Goodwill & intangibles	1,390,473	2,423,988	2,472,641	2,392,865	2,311,946						
Financial & other assets	88,264	93,056	83,640	87,583	91,474						
Total assets	2,721,870	3,976,264	4,422,904	4,863,191	5,382,098						
Accounts payable	418,609	467,201	573,245	635,431	695,395						
Short-term debt	460,174	1,011,439	931,704	782,171	634,808						
Long-term debt	485,217	474,939	450,207	450,207	450,207						
Provisions & other liab	444,048	778,791	778,617	836,206	899,526						
Total liabilities	1,808,048	2,732,370	2,733,773	2,704,014	2,679,936						
Shareholders' equity	913,822	1,243,894	1,689,131	2,159,176	2,702,162						
Minority interests	0	0	0	0	0						
Total equity	913,822	1,243,894	1,689,131	2,159,176	2,702,162						
Net debt (Adj)	661,742	1,148,273	982,218	455,135	-150,914						
Net debt to equity (Adj) (%)	72.4	92.3	58.1	21.1	-5.6						

For definitions of the items in this table, please click [here](#).

Details on Comdata

- **Business Description** – Comdata operates two main businesses – about half of the revenues are fuel card, mainly for over-the-road (OTR) trucks and national accounts, and the other half is corporate payments, consisting of virtual cards and prepaid card processing.
- **Financial Statistics** – The business generated ~\$580 mil in revenues in 2013 with EBITDA margins around ~50%. Over the past three years, revenues have grown ~7% with the majority of the growth coming from the virtual card product.
- **SVS** – Subsequent to the close of the transaction, FLT may divest the SVS business, which does prepaid card processing. We estimate this business represents ~15% of the profits of Comdata.

The Combined FLT / Comdata

- **Business Mix** – Assuming the divestiture of SVS, Comdata will represent 25-30% of FLT's total revenues in 2015. This is comprised of 15-20% from the fuel card business and ~10% from the virtual card business. FLT's total US revenue exposure should increase to 60-65% from ~50% today.
- **Margin Impact** – Comdata's consolidated margins are ~50%, below the ~60% margins for FLT. FLT has plans to narrow this gap significantly over the next few years through a combination of growth acceleration and synergies.
- **Growth** – FLT is sticking with its ~10% organic growth target for the combined businesses. The company hopes to accelerate Comdata's growth from the ~6% range to ~10% through a combination of strategic actions and greater sales investments.
- **EPS** – FLT expects Comdata to contribute \$0.50-\$0.60 to EPS in 2015 on top of the core business which is expected to grow 13-15%. The company also expects the Comdata EPS contributions to grow ~20% going forward through a combination of accelerated revenue growth, synergies and debt repayment. These building blocks plus the impact of future M&A gets the company to its goals of delivering 20%+ EPS growth per year.
- **Leverage** – At the time of close, FLT's leverage ratio will be ~3.3x. There are opportunities for this to go down quickly if FLT completes the sale of SVS and/or is able to securitize accounts receivable for Comdata. The combined business should generate ~\$600 mil in free cash flow annually according to guidance, so we think a leverage ratio approaching ~2x is possible by the end of 2015.
- **Future M&A** – The debt financing used by FLT gives them access to an additional ~\$400 mil in revolving credit for other acquisition. This combined with the aforementioned cash flow should give FLT plenty of capacity to do its traditional ~\$500 mil in M&A per year beginning in 2015.

Takeaways from Recent Meetings with FLT

We hosted an investor meeting with FLT's CEO Ron Clarke and CFO Eric Dey on Monday at their Norcross, GA headquarters. The main theme of the meeting was a focus on sustaining high levels of growth organically and via M&A. This is consistent with our thesis on the stock that a strong EPS growth rate can provide attractive returns for FLT investors even with no improvement on the premium P/E multiple. Below are some of the key points from the meeting.

- **North America** - FLT believes new partner wins can combine with continued healthy double digit growth in CLC and the direct business to drive sustained gains. Additionally, the Nextraq business is performing very well and should contribute nicely to growth once the acquisition is lapped in 4Q14.
- **International** - New product launches in the UK and Brazil should help growth in the second half and ramping synergies from the late 2013 acquisitions will also contribute. The Russian and Czech businesses remain drags, though a recent mgmt. change at the latter could create some changes. On a longer-term basis, Brazil and Mexico seemed like the greatest opportunities given the secular dynamics of those markets.
- **M&A** - FLT is actively considering multiple M&A opportunities. The strategy for deals remains unchanged - any acquisition, regardless of size, will only be done if there are improvements FLT can make to drive higher profits and that will contribute to the long-term EPS growth goals of 20%+. As previously stated by management, targets include both fuel card and non-fuel card businesses, though the latter should grow in relative size over time. Additionally, FLT remains very interested in acquisitions that can grant them entry into top fuel markets where their current presence is limited (mostly Europe and Asia).
- **Partner Deals** – FLT will begin converting Shell in Germany next month and will prioritize future market deployment by revenue opportunity. While this contract is not hugely material to FLT's revenues today, it is very important strategically as FLT tries to win more business from Shell (in all geographies) and convince more partners to outsource to them.
- **Telematics** – The company is still dipping its toe into the telematics business across the world via its Nextraq acquisition in the US last year and the recent minority investment in Masternaut in Europe. FLT would like to see a more attractive customer acquisition and revenue model before investing more heavily into this product line.

FleetCor Technologies Inc

Company description

FLT is a leading provider of payment products and services to commercial fleets, major oil companies and petroleum marketers, serving more than 530,000 commercial accounts in 18 countries. The company operates in two segments that are broken up geographically – North America (51% of 2013 revenues) and International (49%). In both segments, the company's core offering is fleet vehicle payment processing services for commercial and government fleets primarily for fuel purchases. The company also offers fleet telematics, transportation/toll cards, food cards and lodging/entertainment payment processing services to its clients, which represent a combined ~25% of total revenue.

Investment strategy

We have a Buy (1) rating on FLT. We like several attributes of the company's business model, including its high barriers to entry, strong margins, prospects for international expansion, and strong M&A track record. We believe the company's recent series of M&A gives it ample opportunity to drive strong synergies, while good financial flexibility will allow it to pursue additional accretive M&A and / or share repurchases. We believe the company's strong EPS growth will deliver good returns for investors.

Valuation

We apply a 25.9x P/E multiple, within our targeted 25x-27x targeted range, to our 2015 EPS estimate of \$5.95 to derive our \$154 target price. The targeted multiple range is consistent with FLT's recent and historical trading multiples.

Risks

The key risks to FLT's business are:

- Fuel Price Sensitivity – Roughly 20% of FLT's revenues are tied to fuel prices, so fluctuations in this commodity can impact the company's financial results. The company does not attempt to hedge this exposure.
- Cyclical Exposure – In addition to fuel prices, which typically fluctuate with economic cycles, FLT's business is exposed to other cyclical factors such as transaction volumes and credit losses. If the economy were to slip into a recession, FLT's earnings would be negatively impacted by these factors.
- Limited Metric Disclosure – Relative to other public competitors, FLT's business metric disclosure is fairly limited. We believe this creates uncertainty surrounding the key drivers of the business, making it more difficult to predict.
- Geopolitical Risk - FLT operates business in many countries around the world and geopolitical events in certain countries (Russia, Czech Republic, Brazil, Mexico) could negatively impact results.

If any of these factors has greater downside effects than we currently contemplate, FLT could fail to reach our target price.

Appendix A-1

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FleetCor Technologies Inc (FLT)

Ratings and Target Price History Fundamental Research

Analyst: Philip Stiller, CFA

Covered since November 7 2011



	Date	Rating	Target Price	Closing Price
1	8-Oct-11	Stock rating system changed		
2	7-Nov-11	*2	*30.00	28.05
3	14-Dec-11	2	*32.00	29.96
4	5-Feb-12	2	*36.00	34.74
5	8-Feb-12	2	*40.00	35.74
6	29-Apr-12	2	*43.00	40.08
7	29-Jul-12	2	*39.00	37.27

* Indicates change

	Date	Rating	Target Price	Closing Price
8	8-Aug-12	2	*41.00	36.70
9	26-Oct-12	2	*49.00	46.64
10	9-Nov-12	*1	*56.00	47.88
11	10-Jan-13	1	*65.00	56.71
12	7-Feb-13	1	*73.00	59.55
13	2-May-13	1	*89.00	77.20
14	29-May-13	1	*97.00	85.91

	Date	Rating	Target Price	Closing Price
15	1-Aug-13	1	*106.00	91.85
16	10-Sep-13	1	*123.00	106.09
17	30-Oct-13	1	*128.00	107.16
18	14-Jan-14	1	*135.00	113.38
19	26-Feb-14	1	*147.00	127.33
20	24-Apr-14	1	*139.00	113.56
21	24-Jul-14	1	*154.00	132.48

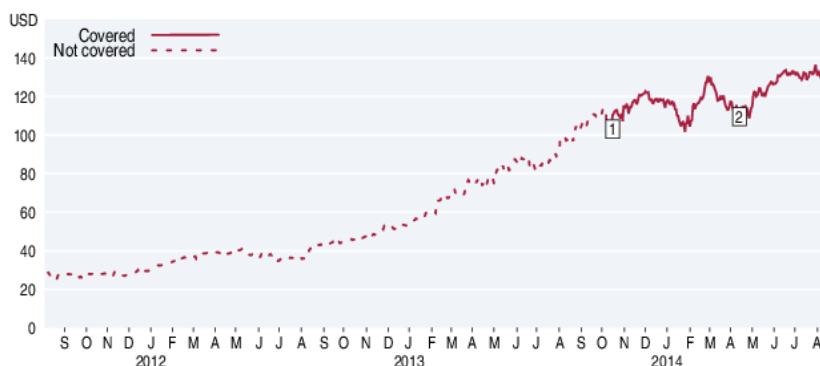
Rating/target price changes above reflect Eastern Standard Time

FleetCor Technologies Inc (FLT)

Ratings and Target Price History Best Ideas Research Relative Call (3 Month)

Analyst: Philip Stiller, CFA

Covered since November 7 2011



	Date	Rating	Target Price	Closing Price
1	16-Oct-13	*ADD MP	-	110.41

* Indicates change

	Date	Rating	Target Price	Closing Price
2	14-Apr-14	*REM MP	-	110.07

Rating/target price changes above reflect Eastern Standard Time

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% of companies in each rating category that are investment banking clients	55%	53%	46%	0%	54%	0%

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