

Axial Corporation (AXLL)

Results: Decent 3Q as Building Products Pickup Offsets Weakness in Chlorovinyls; Synergies on Track

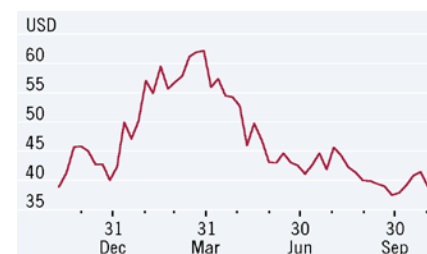
- Citi's Take** — AXLL reported 3Q EPS of \$0.97, above our \$0.93 and in-line with consensus. In 3Q AXLL surpassed its year-one synergy run rate target of \$60mm. The year-end 2014 synergy target remains \$115mm. Despite the profit warning in September, weakness in Chlorovinyls was more pronounced than we expected. However, Building Products grew the top-line more than 1% for the first time since 1Q12 on the highest margins since 3Q09.
- 3Q Highlights** — Adjusted EBITDA of \$175mm was slightly above our \$173.7mm estimate as weakness in Chlorovinyls was offset by strength in Building Products and Aromatics. **Chlorovinyls:** EBITDA of \$151.5mm was below our estimate of \$160.5mm as margins were ~200bps below our forecast. Caustic soda prices have fallen considerably in recent months, and AXLL's planned downtime likely also weighed on results. **Building Products:** 3Q13 EBITDA increased to \$31.1mm, above our estimate of \$24.7mm. Margins of 12.3% expanded 220bps Y/Y and also increased sequentially. Volume rose 10% driven by 26% growth in the US, which offset a 3% decline in Canada. **Aromatics:** EBITDA of \$5.5mm was down 50% Y/Y, but was above our forecast of \$1mm.
- What to Listen for on the Call** — 1) Impact of tightness in the Louisiana ethylene market resulting from the Chevron Evangeline ethylene pipeline disruption and Williams ethylene cracker outage; 2) Outlook for caustic soda prices given the steep recent decline and new US capacity looming; 3) Expected financial impact of ethylene contract renewals for 2014; 4) Status update on securing up to half of the company's ethylene requirements; 5) Additional detail on the pickup in Building Products, and the sustainability of the margin improvement in the segment.
- Call Tomorrow (11/6) at 10AM ET** — Dial-in: 877-312-5406; Passcode: 93520091.
- Implications** — 26% volume growth in US Building Products is positive for VAL.

EPS	Q1	Q2	Q3	Q4	FY	FC Cons
2012A	0.78A	0.52A	1.39A	1.20A	3.90A	3.74A
2013E	0.75A	1.19A	0.93E	0.55E	3.45E	3.67E
Previous	0.75A	1.19A	0.93E	0.55E	3.45E	na
2014E	na	na	na	na	3.70E	4.36E
Previous	na	na	na	na	3.70E	na
2015E	na	na	na	na	4.40E	4.66E
Previous	na	na	na	na	4.40E	na

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

Neutral	2
Price (05 Nov 13)	US\$39.68
Target price	US\$43.00
Expected share price return	8.4%
Expected dividend yield	1.6%
Expected total return	10.0%
Market Cap	US\$2,773M

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



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See Appendix A-1 for Analyst Certification, Important Disclosures and non-US research analyst disclosures.

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Figure 1. AXLL 3Q13 Model Variance

Revenue	3Q13A	3Q13E (Citi)	3Q12A	Y/Y Change
Chlorovinyls	750	718	329	128%
Building Products	253	235	246	3%
Aromatics	194	221	238	-19%
Total Revenues	1,198	1,175	814	47%
EBITDA	3Q13A	3Q13E (Citi)	3Q12A	Y/Y Change
Chlorovinyls	151.5	160.5	84.7	79%
Building Products	31.1	24.7	24.9	25%
Aromatics	5.5	1.0	11.4	-52%
Other	(13.1)	(12.5)	(14.3)	8%
Total Operating Income	175.0	173.7	106.7	64%
EBITDA Margin	3Q13A	3Q13E (Citi)	3Q12A	Y/Y Change
Chlorovinyls	20.2%	22.3%	25.7%	-550 bps
Building Products	12.3%	10.5%	10.1%	220 bps
Aromatics	2.8%	0.4%	4.8%	-200 bps
Total Margin	14.6%	14.8%	13.1%	150 bps

Source: Citi Research

Axiall Corporation

Valuation

Our \$43 target price is the average of our two valuation methodologies, price/forward earnings and firm value/forward EBITDA.

EV/EBITDA

We apply a 6.5x EV/EBITDA multiple to our 2014 EBITDA estimate of \$690 million (subtracting net debt of approximately \$1.4 billion) to arrive at a price of \$44. Over the last 10 years, Axiall has traded between 2x and 17x forward EBITDA with an average of 6x. The multiple we apply is approximately in line with its commodity chemical peers.

Price/Earnings

We apply an 11x P/E multiple to our 2014 EPS estimate of \$3.70, to arrive at a price of \$41. Axiall has historically traded in the range of 5x to 20x forward earnings, with an average of 10.5x. The multiple we apply is approximately in line with its commodity chemical peers.

Risks

We see the following risks to the stock achieving our target price:

Exposure to Volatile Raw Materials: Axiall is not fully backward integrated into the vinyls or cumene chains, and purchases 100% of its requirements for natural gas, ethylene, propylene and benzene. The US ethylene industry now uses greater quantities of light feedstocks to produce ethylene (i.e. ethane and propane), which correspondingly produce less co-product propylene and benzene, and has led to higher prices of those key raw materials. If Axiall is unable to pass through higher prices of key raw materials, it could be negative for the company. Conversely, if raw material costs remain favorable or if the company is able to successfully pass through higher costs, it would be positive.

Industry Capacity: Axiall operates in commoditized chemical industries, and pricing and profitability can be negatively impacted by new capacity. Several chlor-alkali producers across Asia and North America plan to add new capacity over the next two years, which could have a negative impact on pricing and therefore AXLL's margins. If the new capacity starts up more gradually or later than expected, it would be positive for the company. Conversely, if incremental production commences sooner than expected, it would be negative for the company.

Economic Activity: Several of Axiall's products, including caustic soda, cumene, phenol, and acetone, are generally correlated to global economic activity. Should economic growth accelerate, it would be positive for the company. Conversely, if the economy slows, it would be negative for Axiall.

Weather: Through its building products and PVC businesses Axiall sells into the housing and construction markets, which can be influenced by weather patterns. Unseasonably warm weather would be positive for construction-related activity, while unseasonably cold weather would be negative.

The Valspar Corp

(VAL.N; US\$70.06; 2)

Valuation

Our \$69 target price is based on an average of our two valuation methodologies: price/forward earnings and enterprise value/forward EBITDA:

Price/Earnings: A valuation of \$74 is derived by applying a multiple of 18x to 2014E EPS of \$4.13. Our target multiple reflects moderate industrial demand and some improvement in the architectural paint market.

Enterprise Value/EBITDA: Applying a target multiple of 10x to our 2014E EBITDA of \$681mm produces a valuation of \$64. Our target multiple reflects moderate industrial demand and some improvement in the architectural paint market.

Risks

The following considerations may prevent the shares from reaching our target price:

Raw material costs: The greatest risk facing Valspar is raw material cost inflation. Due to the timing of contracts, there is usually a delay in when the company can pass along price increases, resulting in potential margin squeeze. Should the price of raw materials significantly decrease, this would benefit VAL.

Recovery in housing: Architectural paints, while not the entire focus of the company, remain roughly 40% of revenues. An upturn in the US housing market would benefit Valspar's revenue growth rate.

Acquisition risk: Consolidation is a key feature of the global paints & coatings industry. An acquisition of VAL by an upstream player, or paint competitor, has the potential to significantly boost the share price.

If the impact on the company from any of these factors proves to be greater than we anticipate, the stock will likely have difficulty achieving our target price. Likewise, if any of these factors proves to have less of an effect than we anticipate, the stock could materially outperform our target.

Appendix A-1

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The Valspar Corp (VAL)

Ratings and Target Price History Fundamental Research

Analyst: P.J. Juvekar



	Date	Rating	Target Price	Closing Price
1	22-Nov-10	2M	*35.00	33.70
2	7-Jan-11	2M	*38.00	34.18
3	14-Feb-11	2M	*40.00	38.29
4	10-Aug-11	2M	*32.00	27.59
5	6-Oct-11	2M	*33.00	32.70
6	8-Oct-11	Stock rating system changed		

* Indicates change

	Date	Rating	Target Price	Closing Price
7	8-Oct-11	*2	33.00	32.34
8	26-Oct-11	*1	*40.00	34.57
9	12-Jan-12	1	*48.00	41.55
10	15-Feb-12	1	*53.00	45.52
11	5-Apr-12	1	*58.00	50.00
12	1-Oct-12	1	*65.00	55.57

	Date	Rating	Target Price	Closing Price
13	3-Jan-13	1	*75.00	64.00
14	24-Jun-13	*2	*73.00	62.82
15	13-Aug-13	2	*71.00	66.35
16	3-Oct-13	2	*69.00	65.04

Rating/target price changes above reflect Eastern Standard Time

The Valspar Corp (VAL)

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

Analyst: P.J. Juvekar



	Date	Rating	Target Price	Closing Price
1	14-Jul-11	*ADD LP	-	34.35

* Indicates change

	Date	Rating	Target Price	Closing Price
2	14-Oct-11	*REM LP	-	34.23

Rating/target price changes above reflect Eastern Standard Time

Axiall Corporation (AXLL)

Ratings and Target Price History Fundamental Research

Analyst: P.J. Juvekar

Covered since February 28 2013



	Date	Rating	Target Price	Closing Price
1	8-Oct-11	Stock rating system changed		
2	28-Feb-13	*2	*60.00	56.81
3	12-Mar-13	*1	*69.00	60.07

* Indicates change

	Date	Rating	Target Price	Closing Price
4	9-May-13	1	*60.00	47.47
5	24-Jun-13	1	*52.00	41.06
6	19-Sep-13	1	*46.00	39.81

	Date	Rating	Target Price	Closing Price
7	29-Oct-13	*2	*43.00	40.29

Rating/target price changes above reflect Eastern Standard Time

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

Analyst: P.J. Juvekar
Covered since February 28 2013



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Data current as of 30 Sep 2013

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	Buy	Hold	Sell	Buy	Hold	Sell
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