THE EXCLUSIVE

Confidential*

October 2018

THE VALUENTUM TEAM

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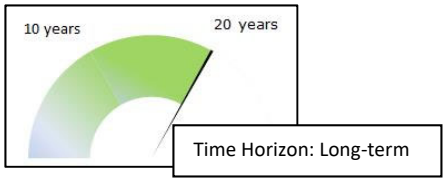
We're celebrating a very special event this week, and we expect to return to the regular newsletter format for the Exclusive in November.

Congrats Kris!

Stay tuned for updates of previous ideas in future emails and editions of the Exclusive!

Image Source: Fayes4Art



Veolia Environnement (VEOEY)

"The first half of 2018 finished once again in a rhythm of sustained growth of both activity and results. The commercial momentum that began two years ago continues. Revenue benefited from the additional efforts we engaged in 2017, growing 6%, along with a notable increase of 4% in waste volumes. Results also revealed sustained growth, with EBITDA up 5.8% and current net income Group share excluding capital gains up 13%, thanks to the revenue growth and the cost savings achieved during the first semester. These strong first half results demonstrate once again the relevance of the two levers of our strategy, growth and operational efficiency, and allow us to be confident in the achievement of our objectives for the full year." – CEO Antoine Frerot, first-half 2018 results

Thesis

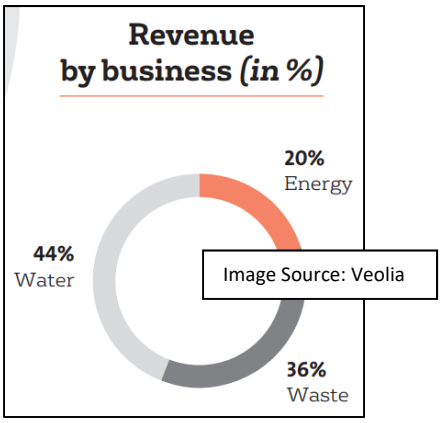
There's just something that gets us excited about a garbage hauler with a ~5% dividend yield. You won't find many high-yielders in the environmental-services space in the US, but one is present in France in Veolia Environnement (VEOEY). The company trades over the counter and on the EN Paris, but it is a massive company with sprawling operations from our favorite in waste services to power operations to its largest exposure, water services (~45% of revenue).

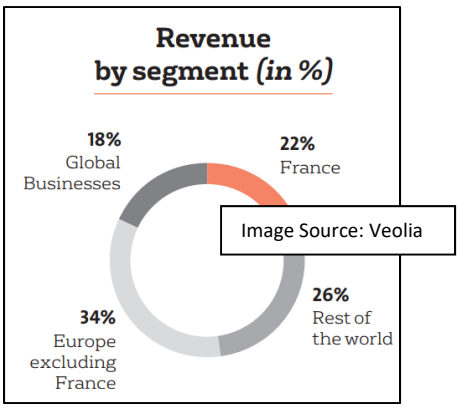
When it comes to companies that provide the necessities of life, Veolia is one of them, and that's why we think it has staying power. The company manages over 4,100 water production plants and nearly 2,900 wastewater treatment plants. It provides 40 million people with waste collection services, treating 47 million metric tons of waste each year. Veolia manages nearly 600 heating and cooling networks. When you talk about a company that is at the core of providing the necessities of life, Veolia is it.

What draws us to the company? For starters, we're huge fans of the waste industry, and Veolia is one of the biggest players on the global stage. Waste collection is something of an indispensable service, and while demand may ebb and flow with the economic cycle, waste generation is not going to go away. As such, we'd view Veolia's waste business as relatively recession-resistant. The near-600 waste-processing facilities the company operates are a key source of pricing power, in our view.

Corporate Profile

Veolia Environnement provides water, waste and energy management solutions around the world. The company supplies nearly 100 million people with drinking water and produces 55 million megawatt hours of energy. It has three primary business activities: Water, Waste and Energy. Veolia employs over 168,000 people across the globe. Its history dates back to 1853 in France.





2018-2019 outlook

- **2018 objectives (at constant exchange rates):**
  - ✓ **Continuation of sustained revenue growth**
  - ✓ **EBITDA growth greater than that of 2017**
  - ✓ **More than €300M in cost savings**
- **2019 objectives[1]:**
  - ✓ **Continuation of revenue growth and full impact of cost savings**
  - ✓ **EBITDA between €3.3Bn and €3.5Bn (excluding IFRIC 12), i.e. between €3.5Bn and €3.7Bn including IFRIC 12**
- **Dividend growth in line with that of current net income**

(1) At constant exchange rates (based on rates at the end of 2016)

Image Source: Veolia

Key metrics continue to move in the right direction, too. EBITDA has advanced to €3.28 billion in 2017 from €3.18 in 2015, and the company expects to achieve the range of €3.3-€3.5 in 2019, as shown in the image above. Post-tax return on capital employed (ROCE) isn't as strong as we would like, but the metric has always been improving in recent years, advancing to 8.4% in 2017 from 7.4% in 2015. Though we'd like to see this return measure in the double-digits, given the relatively low borrowing cost of its utility-like structure, we'd say Veolia is still generating economic profits for shareholders (i.e. ROCE > WACC). The company's dividend per share (in €) has also advanced to 0.84 in 2017 from 0.73. That implies a nice near-5% dividend yield, backed by utility-like operations.

Image Source: Veolia

Selected financial information AFR

Figures presented in accordance with IFRS

(in € million)	12/31/2016[1]	12/31/2017
Revenue	24,187.0	25,124.6
EBITDA	3,219.4	3,284.1
Current EBIT	1,460.2	1,519.4
Current net income – Group share	383.1	401.6
Operating cash flow before changes in working capital	2,610.2	2,671.5
Operating income after share of net income (loss) of equity-accounted entities[2]	1,193.3	1,284.8
Net income – Group share	383.1	401.6
Dividends paid[3]	(401.2)	(439.7)
Dividend per share paid during the fiscal year (in euros)	0.80	0.84[4]
Total assets	37,949.2	38,309.1
Net financial debt[5]	7,812	7,841
Industrial investments (including new operating financial assets)[6]	(1,597)	(1,738)
Net free cash flow[7]	940	655

There are a few risks with Veolia, of course. For starters, it is a global operator, so it is not immune to currency fluctuations and economic performance within the countries of operation. We generally feel its operations are relatively recession-resistant, for the most part, but even some of the strongest utilities can face trouble if municipal or sovereign health may wane. We're not thrilled about its net financial debt load, which stood at €7.84 billion at the end of 2017 (and €10.6 billion in June 2018), but the company's net free cash flow of €655 million still easily covered cash dividends paid of ~€440 million during 2017. Its performance with respect to net free cash flow during 2016 was much more impressive, and we expect the executive team to more prudently manage its net free cash flow position on a go-forward basis. Dividend growth is targeted to be "in line with that of current net income."

Revenue has been on the rise in recent years, but cost containment is also an important part of the Veolia story. The company is approaching the end of its efficiency plan for the 2016-2018 period and is targeting €600-€800 million in gross additional savings with respect to the program. Going forward, improving purchasing decisions, organization structure, and optimizing operations will be par for the course to keep net income on the rise. The company's first-half 2018 results, released August 1, showed continued improvement in all the key areas. Revenue advanced 6% on a year-over-year basis, EBITDA advanced at a similar clip, while current net income leapt 13%+ during the half-year period, boding well for the dividend, in our view. Cost savings are progressing as planned. Things are looking good at the moment, but the image below outlines other risk factors that may impact its operations.

Image Source: Veolia

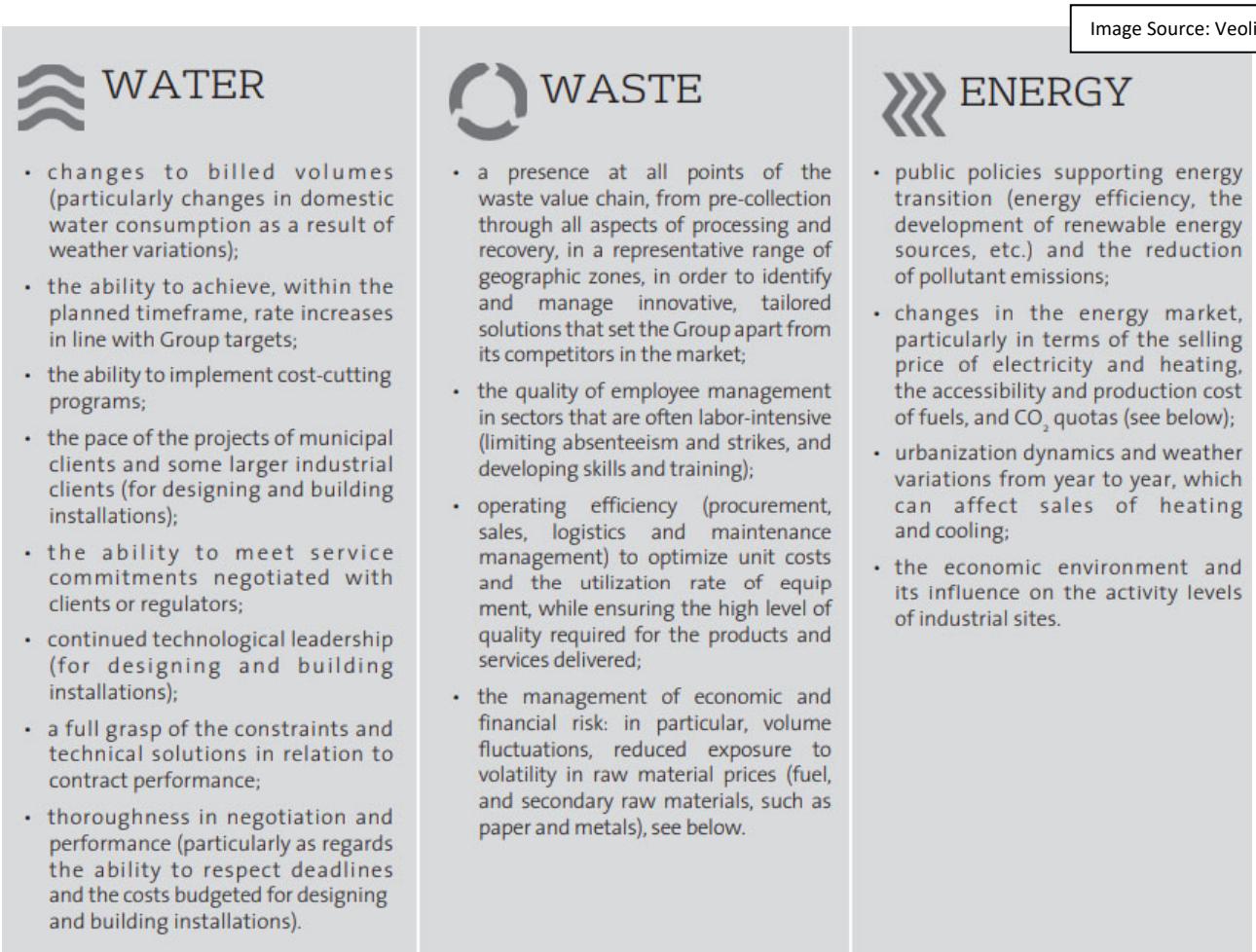


Image Source: Veolia

2.3 Dividend policy

2.3.1 DIVIDENDS PAID DURING THE LAST FIVE FISCAL YEARS

(in €)	2012 Dividend	2013 Dividend	2014 Dividend	2015 Dividend	2016 Dividend
Gross dividend per share	0.70	0.70	0.70	0.73	0.80
Net dividend per share	0.70*	0.70*	0.70*	0.73*	0.80*
TOTAL DIVIDEND DISTRIBUTION**	355,494,245	374,246,447	383,952,678	401,183,799	439,772,185

* *Dividends eligible for the 40% tax rebate.*
** *Amounts paid by the Company.*

A dividend payment of €0.80 per share for each of the Company's outstanding shares carrying dividend rights as of January 1, 2017 was approved by the Combined General Meeting of April 20, 2017. The ex-dividend date was set at April 24, 2017 and the dividend was paid from April 26, 2017. As of December 31, 2016, the share capital comprised 563,364,823 shares, including 15,064,835 treasury shares. The total dividend distribution was adjusted to take account of the number of treasury shares held by Veolia Environnement at the payment date.

A dividend of €0.84 per share for 2017, payable in cash, will be proposed to the Combined General Meeting of April 19, 2018. The ex-dividend date has been set at May 14, 2018 and the 2017 dividend will be paid from May 16, 2018.

For individual shareholders who are French tax residents, a mandatory flat-rate levy of 12.8% will be deducted as payment on account for income tax due in 2019 on 2018 income. This levy will however not be applied to taxpayers whose reference taxable income is less than €50,000 for a single person or €75,000 for couples, if they request exemption in advance.

Social security contributions on dividends paid to private individual shareholders tax resident in France are subject to withholding tax deducted by the paying agent at a rate of 17.2%.

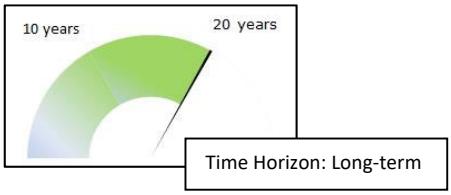
The definitive tax liability for dividends paid by Veolia Environnement will be determined based on information reported in the income tax return filed in the year following receipt of the dividends.

Whether paid in cash or shares, dividends are liable to a flat-rate tax of 12.8% (giving a total tax rate of 30% including social security contributions). Social security contributions are not deductible from income tax.

A taxpayer may make a global election to include dividends in income taxable at the progressive income tax scale. They will therefore be taxed after a 40% deduction. Under this option, social security contributions are deductible from taxable income in the amount of 6.8%.

For beneficiaries who are not French tax residents, dividends are subject to withholding tax at a rate dependent on the country of tax residence.

Veolia is a rather complex entity with far-reaching global operations across diversified end markets. The company has a number of risks, not the least of which are related to municipal/sovereign health across Europe and its own financial leverage, but the company has been around for over 150 years, and we can't envision a situation where Veolia is no longer a part of people's everyday lives. The company's dividend is covered by net free cash flow, and the payout has just started to resume its upward climb, with the company raising it in each of the past three years, per the image above, to the current annual rate of €0.84. Veolia makes the cut for this month's income idea consideration of the Exclusive.



Cigna (CI)

"We believe shares of Cigna are poised to do well in the next few years thanks in large part to excellent cost controls coupled with a well-timed merger. The acquisition of Express Scripts should further allow the company to drive its medical costs ratio lower thanks in large part to rationalizing drug spending. We feel the market is overlooking this high-quality idea as its largest competitors are breaking out to new highs while Cigna consolidates post the announcement of the takeout of Express Scripts."

Introduction to Cigna

Cigna (CI) is a managed care company with a diverse revenue stream thanks in large part to legacy run-off operations from its time as a broad-line insurance entity. Cigna exited the vast majority of its life and reinsurance business in the 1990s, though the company does maintain a division that holds assets in a run-off phase.

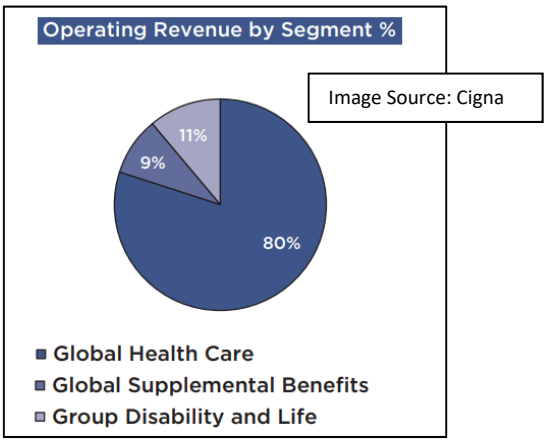
The bulk of Cigna's business is focused on health care needs with a niche in employee benefits including health, supplemental benefits, disability, and life insurance. While accounting for an ever-increasingly smaller percentage of overall revenue, the legacy lines of business have saddled Cigna with a below industry multiple, as Cigna operates as a hybrid versus industry bellwether United Healthcare (UNH) which operates as a pure play managed care entity.

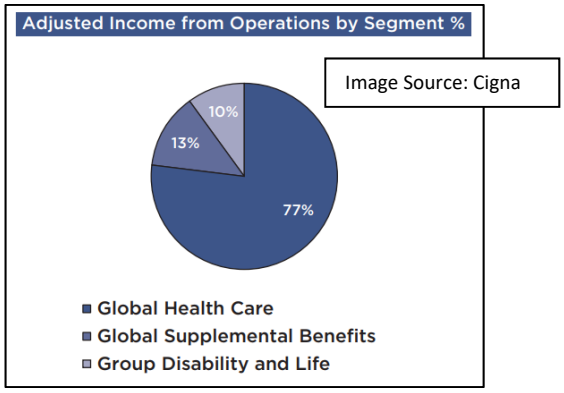
Industry Consolidation

The managed care industry continues to undergo a wave of consolidation in order to lower overall costs while maintaining margins. Cigna had struck a deal to be acquired by Anthem (ANTH) in June 2015, a combination that would form a new managed care colossus on par with United Healthcare. The combination was doomed when the US Department of Justice sued on July 21, 2016 to block the merger, claiming it was anti-competitive. Not to be outdone, rival Aetna (AET) announced its intention to acquire Humana (HUM) in July 2015. The narrowing of the field from 5 national providers down to 3 drew the ire of the DOJ as the organization feared the narrowing of choice would lead to even higher premiums for policy holders and employers.

Corporate Profile

Cigna is a global health service company that works with employers and organizations to develop programs that improve their health and lower medical costs. Some of its products include medical, dental, behavioral health, vision, and prescription drug benefits. It offers Medicare Advantage and Medicare Part D plans through its Government operating segment. Its headquarters is located in Bloomfield, Connecticut.





The DOJ has not slowed down the pace of consolidation, however, instead allowing the reshaping the industry. For example, vertical integration has been allowed rather than the horizontal integration attempted in 2015. The M&A wave has continued, as Aetna, itself, was acquired by CVS Health (CVS) as a way for CVS to stem the expected decline in its PBM business. Humana has been the subject of numerous rumors, most linking the managed care organization with Wal-Mart (WMT), an interesting rumor we feel in large part born out of the numerous deals in various other capacities between the two entities.

United Healthcare, on the other hand, managed to avoid a costly horizontal merger attempt in large part due to to its size in the market. We feel United correctly surmised a takeout of a smaller rival would not be viewed highly be the DOJ. Instead, it moved downstream by building out its provider network via the acquisition of DaVita Medical Group. The wisest move, in our view, is Cigna's acquisition of Express Scripts (ESRX) to augment its existing pharmacy operations, thus taking a page out of United Healthcare's uber-successful playbook, which has seen its Optum Division power the shares significantly higher (well-outpacing the performance of the major markets).

Why Did Cigna Buy Express Scripts?

The days of the pure-play PBM (pharmacy benefits manager) are coming to an end, in our view, as the industry dynamics tend to favor the increase in costs to the healthcare system thanks in part to the profit motive on the part of the PBMs. An area of notable controversy is in the area of negotiated rebates with drug manufacturers. Pfizer's CEO Reed publicly stated his company only sees 58% of the list price of a drug.

> ***"At the moment in time, about 40% of the pharmaceutical prices are subsidies to the rest of the health care system. We realized some 58% of our list price. The rest goes to subsidize profitability of PBMs; insurance companies; and frankly, premiums for those that are healthy.*** *This is not a sustainable position. And so removal of the rebates, I believe, will be very beneficial to patients and our industry, especially those companies that are -- who are at launching -- those companies who are launching new products over the next 5 years or so would remove the rebates, will remove the sort of what we call the rebate trap, whereby access is denied to innovative products because of a strong position of another product with its rebates."*
>
> Quote Source: Pfizer Q2 2018 Earnings Conference Call.

The PBM industry does serve a vital role in cost containment via the use of strict product formularies, which forces the drug manufacturers to compete on price to prevent the loss of market share (as the plan locks out its patient base from utilizing the treatment). The most notable example is Express Scripts' great job in controlling costs on Hepatitis C treatments. The problem, however, is the lack of transparency coupled with the need for profitability, which adds costs to the overall delivery of healthcare in the US.

We believe one of the easiest solutions would be for the PBM industry to become absorbed into the managed care industry, thus allowing managed care to ring out some redundant costs while retaining the cost control initiatives (formularies, prior authorization, etc.) that the PBM industry does so well.

Terms of the Deal

Image Source: Cigna

Delivers Meaningful Shareholder Value

- Significantly broadens and strengthens Cigna's growth profile
- Strong EPS[1] profile with double digit accretion in first full year post-close, excluding the impact of Express Scripts' transitioning clients
- Greater than ~$600 million of retained synergies, primarily reflecting the benefit of administrative efficiencies
- Meaningful opportunities for additional synergies to be realized through integration of complementary platforms over the longer term
- Generates significant cash flow from service-oriented business to support strategic growth initiatives
- Financial strength and flexibility to delever and maintain investment grade debt ratings

Enhancing Cigna's revenue and earnings growth

Image Source: Cigna Investor Presentation

Under terms of the deal, Cigna has proposed to acquire Express Scripts via a combination of cash and stock. Shareholders of Express Scripts will receive cash in addition to shares of the new combined company. The deal is subject to review with numerous regulatory bodies needing to sign off on the transaction, and while there have been obstacles thus far, **Cigna expects the deal to close by the end of 2018**, as it pushes to gain the necessary regulatory clearance to make the deal happen.

It hasn't been easy though. Through the course of the deal process, famed investor Carl Icahn had thrown his hat in the ring to try to potentially scuttle the deal. In typical Icahn fashion, he claimed the deal didn't make strategic sense. Instead, he had advocated for Cigna to utilize its cash hoard to repurchase shares while striking a partnership with Cigna.

Icahn may have been partially correct that the PBM industry is facing an "existential crisis," but the crisis also extends to the freestanding PBM's as consolidation will force them to lose independence. By striking a deal with Express, Cigna may forgo significant profit advancement in the near term, in our view, as evidenced by Anthem's (ANTM) belief that Express had systematically overcharged them for years, but it may be the right move for CI-ESRX in the long haul.

Icahn eventually backed down, and Cigna now has received shareholder support for the deal along with clearance from the US Justice Department. We feel more confident the deal will go through (scheduled for completion by the end of 2018), now that the DOJ has signed off, and but let's further examine the parameters of the expected deal to gain a better insight into why Cigna wanted to make this move.

From our perspective, the accretive nature of the Express deal from year one stands in sharp contrast to the dilutive nature of CVS's move to acquire Aetna. The Aetna transaction is targeted to be accretive after the second full year after the deal, a sharp contrast to the Express deal, which is expected to be accretive in the first full year. Also, the debt levels are far different with debt to capitalization for Cigna

less than 50% versus the 60% level for the Aetna deal.

The more-telling statistic is the composition of the leadership team post completion of the acquisitions, however. We were happy to see that Tim Wentworth, the current CEO of Express, will stay on post the acquisition to run the Express division of Cigna, unlike in the case of the CVS-Aetna deal, where Mark Bertolini, the CEO of Aetna, has plans to join the board of directors and relinquish his day to day oversight of the business.

Express+Cigna Earnings Guidance for 2021

The managed care industry continues its upward ascent as it remains one of the hottest sectors in the equity market today. The stellar growth of the industry underscores the robust nature of the underlying business trends, which capitalize on the greying of America coupled with the increased demand for insurance coverage. The Express deal will aid Cigna in increasing its revenue growth through 2021 with management's initial guidance of a 6-8% annual revenue increase.

We view the increase in revenue as one part of the puzzle, with margin expansion necessary for fundamentals to continue to support the share price. Management's initial projection is for earnings per share to fall within a range of $20-21 in 2021 versus an actual base of $10.47 in 2017. While we are impressed with management's lofty projections, execution is critical to ensuring the projections are attainable.

Earnings Guidance for 2018

The managed care industry derives the majority of its profits by controlling medical costs in a similar vein to the business dynamics of the property and casualty industry. The key metric to follow for the managed care industry is the Medical Loss Ratio (MLR). A figure below 100% indicates the underlying profitability of the business.

We were impressed with the most recent second-quarter 2018 earnings report from Cigna, where the managed care giant beat and raised guidance off the back of favorable medical cost trends. Cigna reported second-quarter 2018 Commercial MLR of 76.3% with the Government MLR coming in at 83.7% (expected as the older population tends to utilize medical services at a higher rate than commercially insured patients). The Commercial MLR of 76.3% is 70 basis points lower than the second quarter of 2017, underscoring Cigna's effective control of costs. The MLR in the Government line of business decreased 240 basis points versus the second quarter of 2017.

The disciplined cost controls allowed Cigna to increase its 2018 earnings guidance to $13.60-$13.90 per share versus prior guidance of $12.85-$13.25, an increase of 65-75 cents in earnings. Cigna increased its revenue forecast for 2018 to 8% versus a prior range of 7-8% underscoring improving demand for its products relative to the midpoint of the prior range. The MLR outlook brightened with Commercial MLR decreasing by 50 basis points to 77-78% and Government decreasing 50 basis points to 83-84%.

Medical Cost Trend

Tackling the skyrocketing cost trends involved in the delivery of care is Cigna's largest opportunity to drive profitability for its shareholders while delivering quality care. In this regard, Cigna lowered its projected Medical Cost Trend, which may be generally viewed as the yearly inflation rate for the cost of medical care, to 3.5%-4% versus the prior range of 4-5% before the completion of the Express deal.

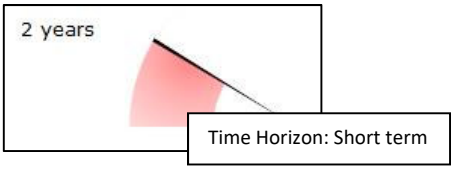
We believe it is very likely Cigna will be able to exert significant downward pressure on the overall costs of the delivery of healthcare upon the consummation of the Express Scripts acquisition. Cigna does not possess significant scale in the pharmacy benefits area, an area ripe for further cost containment. With Express under its wing, we believe Cigna may be better positioned to meet or even exceed future expectations.

Possible Valuation Disconnect

Cigna continues to trade at a significant discount to its peers in the managed care industry, despite the strong underlying business dynamics. The stellar growth numbers posted by the pure-play managed care entities (United Healthcare, Humana, WellCare) may have led to an inflated multiple, well in excess of the current market multiple of approximately 17 times, with WellCare trading well above 30 times 2018 earnings estimates.

While we understand Cigna may warrant such lofty multiples, given the leverage of its business, a market multiple is not out of the question considering its expected earnings growth of 20%+ in 2018 coupled with a well above double-digit earnings growth runway out to 2021. Given favorable market conditions, we think 17 times the high-end of 2018 earnings guidance may offer an optimistic fair value, or ~$235 per share, above 52-week highs.

Independent healthcare and biotech contributor Alexander J. Poulos contributed to this idea. Alex is long Cigna.



Modine (MOD)

Thesis

Trade uncertainty has dominated headlines for a large portion of 2018, and investors have been pulled in a number of directions in hopes of sifting through the seemingly non-stop news flow. This month's short idea consideration looks to capitalize not only on changing trade policies but also the uncertainty that can impact investment decisions from manufacturers around the world. Modine Manufacturing is a thermal management solutions company with a large portion of its sales tied to on- and off-highway vehicle end markets, as well as multiple residential and commercial oriented industrial end markets.

Corporate Profile

Modine Manufacturing is a provider of innovative thermal management solutions to a wide range of markets and customers. It is a leading provider of heat transfer systems and heat transfer components for on- and off-highway vehicle applications. It is also a leader in thermal management technology for a number of HVAC and refrigeration markets. The company was founded in 1916 and is headquartered in Racine, Wisconsin.

While we have our fair share of concerns about the company's near-term operating environment, we expect it to face pressure in the event of a broader economic downturn due to its level of indebtedness and ties to cyclical end markets. One needs to look no further than the Financial Crisis of late last decade for support for this argument. The company was forced to eliminate its dividend in early 2009 as it faced financial distress and defaulted on its debt. Sales fell from more than $1.5 billion in fiscal 2007 to less than $1.2 billion in fiscal 2010, while earnings per diluted share fell from $1.19 in fiscal 2007 to losses of $1.73, $3.25, and $0.50 per diluted share in the following three fiscal years, respectively.

Shares of Modine Manufacturing do not look expensive from a multiple standpoint as they are trading at less than 10 times the midpoint of management's adjusted earnings per share guidance for fiscal 2019 (ends March 31). This may not be all that surprising given the company's ties to cyclical automotive and industrial end markets, but management is also upbeat about its near-term outlook, despite a number of headwinds. It expects fiscal 2019 sales to grow 3%-8% over fiscal 2018 levels, and adjusted operating income is projected to grow 12%-21% year-over-year to a range of $135-$145 million. Adjusted earnings per share guidance is in the range of $1.50-$1.65 compared to $1.54 in fiscal 2018, which is expected to help drive free cash flow generation above fiscal 2018's result of nearly $53 million. It is worth noting, however, that free cash flow was materially suppressed in prior fiscal years and came in negative in fiscal 2017.

Modine has found itself in the midst of changing US trade policies, but the impact of ongoing trade policy uncertainty may also have a material impact on the health of its business as customers may be forced to wait for greater clarity prior to developing investment and production plans. The company may be able to offset a portion of this impact thanks to the shorter purchasing cycles of some of its industrial customers, which may allow for it to more effectively pass through cost inflation. Sales to these customers are approaching 50% of its total business, a result of improved end market diversification in recent years.

However, Modine notes a key risk to its business is continual customer pressure to absorb costs that weigh on its profitability. It often receives requests from customers to pay for design, engineering, and tooling costs that are necessary prior to the start of production and subsequently recover these costs via amortization of the piece price of the product in question. These costs cannot always be capitalized, however, meaning they must be expensed, which ultimately impacts margin performance.

As of its fiscal first-quarter report, released August 2, Modine expects favorable volume trends to help it offset rising raw material costs, but we are not as confident, due in part to the aforementioned potential for order uncertainty from customers. The company's margins will also be impacted by tariffs on imported heat exchanger components, including a number of aluminum and stainless-steel castings it currently imports from China, which will now be subject to a 25% tariff. Management is doubtful it will be granted an exclusion on these items. It also currently imports a specialty aluminum alloy from Europe that it cannot source from the US, and that alloy is now subject to a 10% tariff.

While Modine is able to source a large portion of its raw materials from US suppliers, the tariffs imposed on foreign competitors has significantly impacted demand for these materials. Not only have US suppliers raised prices due to the heightened demand, but freight costs have also been increased as a result of these producers nearing or reaching capacity limitations. The potential for additional tariffs on other portions of its cost structure is certainly real at this point in time given the rhetoric seen from all sides of ongoing trade disagreements, and auto parts may be poised to be a sticking point in trade negotiations as the uncertainty continues to provide an overhang for the sector.

Modine also has a degree of customer concentration within its business. Its top ten customers account for nearly half of its total sales as of fiscal 2018, and Daimler (DMLRY) and Volkswagen (VWAGY) each account for more than 10% of total sales. German automaker BMW (BMWYY) recently cut guidance in its 'Automotive' segment as a result of ongoing trade uncertainty related to the strained US-China relationship, and we expect its peers, including Volkswagen, to experience similar pressures, which would likely provide additional pressure on Modine to meet Volkswagen's (and others') changing demands.

In addition to concerns regarding the health of Modine's operations in the event of a downturn in one or more of its end markets, the company's financial leverage is another concern. As of the end of the first quarter of its fiscal 2019, it held $506 million in total debt, including $134 million in short-term debt and the current portion of long-term debt, compared to just $41 million in cash and cash equivalents. Management estimates its net leverage ratio at 2.5x, but investors should note that this comes after multiple years of a relatively benign operating environment.

We currently value shares of Modine Manufacturing at $10 apiece, and this estimate includes the assumption of ongoing improvement in free cash flow generation in the near term. We're still not sold on the company's ability to maneuver a material downturn in its end markets, a notion supported by its significant struggles late last decade. Investors should note that the company's single-digit earnings multiple may be coming near a cyclical peak, suggesting its normalized price-to-earnings ratio might be much higher. In addition, this multiple is on an adjusted earnings basis, and its price-to-GAAP earnings ratio is far lower. For example, GAAP earnings per diluted share in fiscal 2018 came in at $0.43 compared to the adjusted result of $1.54.

All things considered, we expect Modine to face pressure as a result of its cyclical end markets, notable financial leverage, rising input costs, including tariff-related raw materials, and the indirect impact of trade uncertainty. Management will do its best to improve its cost structure and pass rising input costs to consumers, but we are not confident in its ability to do so--or in the impact rising volumes will have on margin performance as a result of heightened uncertainty. The company does not pay a dividend.

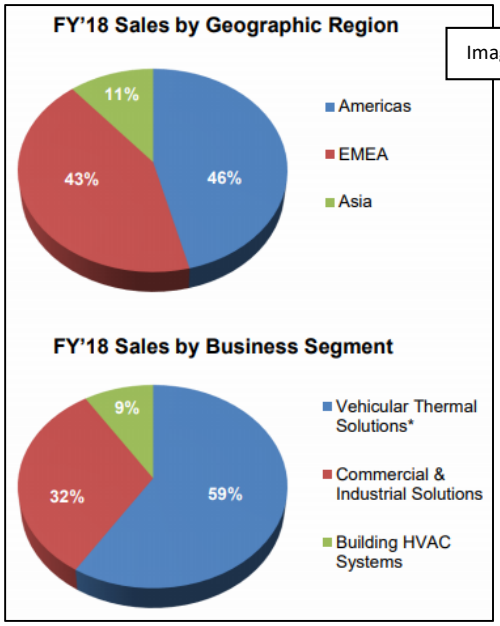


Image Source: Modine

Image Source: Modine

(in millions, except per share amounts)	Years ended March 31, 2018	2017	2016	2015	2014
Net sales	$ 2,103	$ 1,503	$ 1,353	$ 1,496	$ 1,478
Operating income	92	42	37	54	40
Net earnings (loss)	24	15	(1)	23	132
Total assets	1,573	1,450	921	931	1,030
Long-term debt - excluding current portion	386	406	126	130	131
Net cash provided by operating activities	124	42	72	64	105
Expenditures for property, plant and equipment	71	64	63	58	53
Net earnings (loss) per share attributable to Modine shareholders:					
Basic	$ 0.44	$ 0.29	$ (0.03)	$ 0.46	$ 2.75
Diluted	0.43	0.29	(0.03)	0.45	2.72

Image Source: Modine

(in thousands, except per share amounts)	Fiscal Year ended March 31 2011	2010	2009	2008	2007
Net sales	$ 1,448,235	$ 1,162,576	$ 1,406,944	$ 1,603,527	$ 1,525,492
Earnings (loss) from continuing operations	9,227	(19,695)	(104,054)	(55,105)	38,845
Total assets	916,939	840,895	852,506	1,168,283	1,101,573
Long-term debt - excluding current portion	138,582	135,952	243,982	224,525	173,074
Dividends per share	-	-	0.30	0.70	0.70
Net earnings (loss) from continuing operations per share of common stock - basic	0.20	(0.50)	(3.25)	(1.73)	1.20
Net earnings (loss) from continuing operations per share of common stock - diluted	0.20	(0.50)	(3.25)	(1.73)	1.19

Kris Rosemann contributed to this article.

July 1, 2016

Inaugural Letter to Members

Dear Valued Member,

Welcome! You are one of a very limited number of members that will ever bear witness to the pages of this document.

The launch week of the Nelson Exclusive coincided with news that Britain has voted to leave the European Union. The decision, while sending the European banks tumbling violently, does little to muddy the context setting the background of the inaugural edition of this publication.

Broader stock market valuations are at frothy levels, and interest rates continue to hover near all-time lows. The investment-decision landscape is more complicated today than ever before for all types of investors, from those seeking long-term capital appreciation to those that are targeting certain income goals. Cyclicals today are trading at peak multiples on peak earnings, and even consumer staples equities have reached valuation levels that may be more appropriate for aggressive growth equities, not mature operators. *Said differently, the market has laid down the gauntlet.*

The next few years in the markets may be among the most difficult witnessed since the Great Recession. Even a broader market pullback 20% from current all-time highs wouldn't be abnormal given that the collective market valuation of S&P 500 companies has effectively tripled from the March 2009 panic bottom. The launch of the Nelson Exclusive in such conditions can be considered perilous as broader market performance inevitably will act as ballast to the returns of ideas surfaced. In this spirit, I want to remind you that not all ideas in this publication will be successful, and some that are eventually may encounter tough sledding over extended periods of time. As a swimmer cannot achieve his best time swimming against the current, a stock selector cannot achieve his best performance in a down market. Regardless, the value placed on a steady hand during challenging times is priceless.

Let's first cover what the Exclusive is and then we'll talk about what it is not. As you know, the Valuentum investment coverage universe is vast, and what we're seeking to deliver in this publication is ideas that fall outside its reach. We're breaking down the traditional barriers of equity coverage to identify underfollowed gems across the investing spectrum, delivering in each monthly edition one idea for income investors, one idea for readers seeking long-term capital appreciation, and a bonus idea for those looking for a "short" consideration (1). Underfollowed doesn't mean obscure, however, and the ideas that we're targeting will be investable ones, avoiding thinly-traded instruments and penny stock "traps." We'll clearly define our expected time horizon for each consideration, and where applicable, we'll update our theses in subsequent editions. We'll keep score, tracking performance over time.

Let's talk about what the Exclusive isn't. The Exclusive does not constitute individual investment advice, and the ideas within it are not personal recommendations. Each of you reading should always work with your

personal financial advisor who knows your individual goals and risk tolerances. I do not. Only you and your personal financial advisor know what's best for your life circumstances. The personal financial advising markets and what we do at Valuentum via financial publishing are two different verticals in the same industry, but they are different nonetheless. I just want to be very clear about this because I can never tell you to buy or sell anything at any time, even if this may be what you want. It's not that I don't have conviction in my work – it's the rules of the business.

Within the twelve editions of the Nelson Exclusive each year, we'll be highlighting in total 36 ideas for consideration with varying investment parameters. That's a lot. Depending on the time horizon set forth with each idea, fantastic performance might mean a success rate of 60%, great performance might be 55%, average performance might be 50%, while anything below that mark may constituent a poor showing. Obviously, I'm aiming for a 100% success rate, but I also have to be realistic. The great Joe DiMaggio may have hit safely for 56 consecutive games in the last baseball season before the United States was thrust into World War II, but he "only" hit .357 that year. That season of '41, the great Ted Williams would be the last player to hit .400, meaning that one of the best hitters in baseball…ever…was still called out ~60% of the time.

The greatest investors face a similar paradigm. Stock selection is a process where there will be homeruns and strikeouts. You know me. The Exclusive is not a "get-rich-quick" product, and you should keep a close eye on your wallet if you encounter anyone promising anything of the sort. In the inaugural edition of the Nelson Exclusive, we're going to take 36 swings in a year – they are going to be hard and through the zone, and I'm not going to pull my shoulder out or take my eye off the ball. Market conditions are expected to be stormy in coming years as "reversion-to-the-mean" dynamics rain down, and a crafty lefthander with great "stuff" may be on the mound, but we're stepping up to the plate and digging in.

Batter up!

Sincerely,

Brian Nelson, CFA
President, Investment Research & Analysis
Valuentum Securities, Inc.
brian@valuentum.com

Edited October 6, 2018.

P.S. On a very personal note, I wanted to thank you for your continued support. Without you, neither the Nelson Exclusive publication nor Valuentum would exist. This fact is not lost on me. I thank you deeply.

The Nelson Exclusive: Volume 3, Issue 10

The Nelson Exclusive is published monthly. Contact us at info@valuentum.com for more information.

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(1) From the SEC's website: A short sale is the sale of a stock that an investor does not own or a sale which is consummated by the delivery of a stock borrowed by, or for the account of, the investor. Short sales are normally settled by the delivery of a security borrowed by or on behalf of the investor. The investor later closes out the position by returning the borrowed security to the stock lender, typically by purchasing securities on the open market.

Investors who sell stock short typically believe the price of the stock will fall and hope to buy the stock at the lower price and make a profit. Short selling is also used by market makers and others to provide liquidity in response to unanticipated demand, or to hedge the risk of an economic long position in the same security or in a related security. If the price of the stock rises, short sellers who buy it at the higher price will incur a loss.

Brokerage firms typically lend stock to customers who engage in short sales, using the firm's own inventory, the margin account of another of the firm's customers, or another lender. As with buying stock on margin, short sellers are subject to the margin rules and other fees and charges may apply (including interest on the stock loan). If the borrowed stock pays a dividend, the short seller is responsible for paying the dividend to the person or firm making the loan (Source: SEC https://www.sec.gov/answers/shortsale.htm)

Short selling is not for all types of investors, and readers should consult their personal financial advisor that understands their individual goals and risk tolerances before considering any investment or any strategy. Potential losses for an investor engaging in a short selling strategy are theoretically infinite.

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