



STOCKTRADES PREMIUM COMPANY SUMMARY

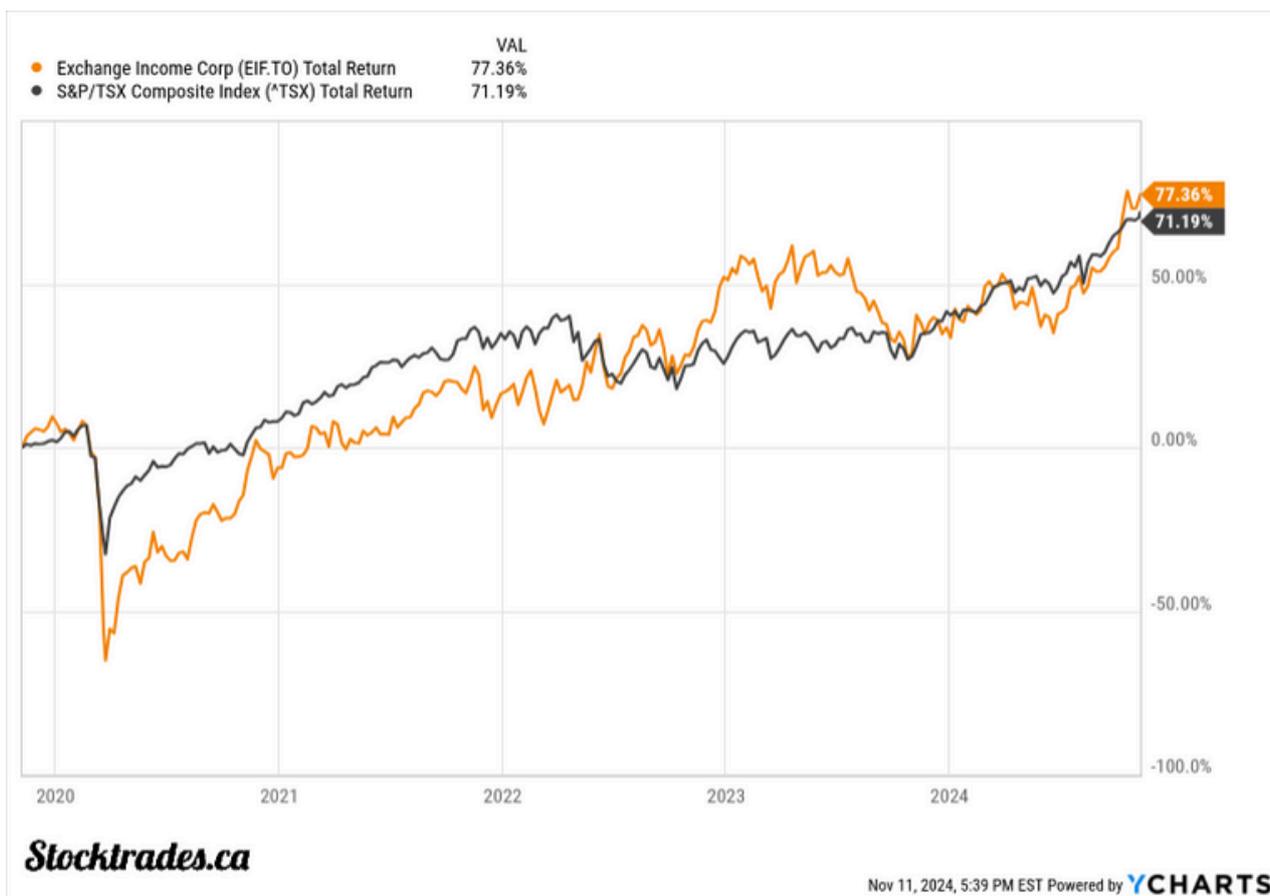
EXCHANGE INCOME CORP.

EIF.TO

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Stocktrades Premium



Exchange Income Corp is a diversified, acquisition-oriented corporation focused on opportunities in three sectors: aerospace, aviation services and equipment, and manufacturing. The corporation's business plan is to invest in profitable, well-established companies with cash flows operating in niche markets. Its Aerospace and Aviation segment is a key revenue driver, recognizing revenue from the provision of aftermarket parts sales, aircraft and engine sales, aircraft and engine lease revenue, surveillance and aircraft modification services, software development and sales of software licenses, charter, passenger flight, medevac, and cargo services. The Manufacturing segment recognizes revenue from the sales of manufacturing products and services.

Focus Areas	Score (0/100)	Focus Areas	Score (0/100)
Valuation	69	Dividend	41
Profitability	42	Outlook	92
Risk	54	Debt	30
Returns	28	Growth	60
Overall	54		

*Our Risk Rating: Our opinion of the overall risk an investment presents. Can be shown as Defensive (DEF), Moderate (MOD), or Aggressive (AGG). By no means is this an indication of future potential gains or lower volatility.

PROS

- Despite a short stint during the global pandemic, the company has maintained double-digit returns on equity since 2015
- Due to some consolidation, the company is now attractively priced
- The company recently locked in 2/3 of its debt at attractive fixed rates. This should save it around \$8.1M in financing costs annually, and reduce exposure to higher rates
- The company provides a unique blend of high-yield and high-growth
- Analysts expect earnings to grow by 35% through 2025.
- Has a strong history of topping estimates
- Numerous accretive acquisitions and new contracts are fueling backlog growth as management continues to execute

CONS

- The company lost its Aristocrat status during the pandemic
- Although its yield is attractive, dividend growth is sporadic due to the company's growth via acquisition strategy
- Although this should be mitigated moving forward with the company locking in debt, financing costs have ballooned over the last year
- Although right in line with historical averages, debt levels, debt to equity, and interest coverage ratios are just average
- The company is known to frequently issue shares
- The company is volatile, having a beta of 2. It is not uncommon to see double-digit runups/corrections in price in short order
- The company predicts short-term headwinds in terms of expenses

OVERALL THESIS

Exchange Income Corp is a unique blend of income and growth for investors looking for the best of both worlds. Don't make the mistake many do and cast this company aside because it is in the airline industry.

First, it has many other operations outside the airline sector that diversify its revenue base. Secondly, this is not a traditional airline like Air Canada. Although it does provide charter and passenger flights to the more remote regions in Canada, for the most part, it deals with things like medivac services, pilot training, surveillance, and aircraft parts. Outside the aerospace segment, its manufacturing segment contains operations like bridge and mat construction to allow customers to operate machinery in difficult-to-access or environmentally sensitive areas. In addition to this, the company also runs multiple subsidiaries that take care of high-rise window installation and maintenance. Finally, the precision manufacturing segment deals with constructing and maintaining wireless and wireline infrastructure, stainless tanks and vessels, and much more.

Management has proven highly competent over the years in making smaller, tuck-in acquisitions. It never seems to overpay, and there is a bit of a comfort level in knowing that there likely will be a little difficulty when it comes to integrating acquisitions.

The company pays a high-yielding, well-covered dividend. And although this company scores relatively weak inside our dividend screener, this is due to the standardized payout ratios not being the right way to evaluate the dividend. We'll get to more of that in the dividend section. The company recently made the prudent move to enter fixed-rate agreements on most (66%) of its debt. The company states that the move will reduce interest on its \$540M in fixed-rate debt by up to 1.5%. This works out to be around \$8.1M annually.

Overall, we view Exchange Income Corp as a slightly undervalued income and growth play that should grow in line with expected growth rates. The company is by no means a bargain play at this point in time. However, as Buffett has said, it is better to pay a good price for a wonderful company than a wonderful price for a good company.

POTENTIAL RISKS

Although Exchange Income Corporation grows organically, it also relies on acquisitions to fuel further growth. This poses risks on several fronts. First, if competition enters the space and increases the price of these acquisitions, it ultimately cuts into growth figures of Exchange Income. Secondly, although management has proven time and time again to make smart acquisitions that eventually grow the bottom line of the company, it is far from guaranteed that they will continue to do so. Look no further than a company like Enghouse

(TSE:ENGH), which used to have one of the best management teams in the country regarding capital deployment. It seems to have lost its touch in this, so its share price has been impacted. Secondly, the company does have high debt levels. Although its risk of exposure to floating rates has been

Beta	2
Alpha	-1.33
Our Risk Rating	Mod*
Max Drawdown	68%

mitigated with the company locking in approximately 66% of its debt to a fixed rate, its debt to equity is relatively high, interest coverage ratios are sub 3x, and overall an investor has to be comfortable with management navigating routinely high debt levels. Much like the acquisition situation, although it has continually done so in the past, it is never guaranteed to do so in the future, especially with the current rate environment.

In addition to this, the company is also a small-cap Canadian stock with not as much mainstream coverage. Although this can typically keep valuations down and allow investors to accumulate shares cheaply, it can also lead to heightened volatility. Exchange Income has

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a beta of 2, meaning it is twice as volatile as the TSX Index. It is prone to large swings in price over short durations of time, and risk-averse investors will need to know this before purchasing.

VALUATION

	TTM	5 Year Average	Industry Average
P/E	22.67	20.89	2.38
P/S	1.11	1.11	0.41
P/B	2.07	2	2.46
P/FCF	N/A	N/A	N/A
PEG Ratio (FWD)	0.60	N/A	N/A

Exchange Income Corporation doesn't have the slam dunk value it did when we initially added it to the Bull List. However, when we look at how the company has been able to deploy capital through acquisitions and the contracts it has recently added, we view Exchange Income Corporation as a solid GARP (Growth at A Reasonable Price) play that also pays an attractive dividend.

The company is trading at only 14x expected earnings and has a price-to-earnings-to-growth (PEG) ratio of 0.6. Theoretically, a PEG of under 1 signals undervaluation by the market, as valuations are not keeping up with expected growth rates.

The company is known to issue shares, which can impact valuation and overall volatility. However, the company has been efficient in growing operating cash flow over the years, and most share issuances do end up accretive, thus adding value.

With the company continually posting record results and double digit growth anticipated in the future, I'd view 14x expected earnings as a very reasonable price to pay for the company. Many analysts have attached high \$60 price tags to Exchange Income, especially after its recent string of attractive results, and I tend to agree with that sentiment.

COMPETITOR ANALYSIS

Exchange Income Corp has relatively little publicly traded competition. If you were to look at the company from a broad industry perspective, many websites compare it to airline companies like Air Canada (TSE:AC), Heroux Devtek (TSE:HRX), and Chorus Aviation (TSE:CHR). However, although Exchange Income Corp has some exposure to the same operations as each of these companies, that being passenger travel with Air Canada and Chorus, along with manufacturing in Heroux Devtek, there is not enough overlap or sole reliance on a single factor to ever label these companies direct competition.

DIVIDEND ANALYSIS

Annual Dividend	Earnings Payout Ratio	5 Year Dividend Growth %	Dividend Growth Streak
\$2.64	90%	2.79%	2

One of the bonuses of Exchange Income Corp is that it provides not only excellent growth but also a strong dividend, paid monthly. There are a lot of misconceptions about the company's dividend. So, we'll aim to walk you through them in this section.

For one, the payout ratio in terms of earnings. Exchange Income Corporation is a lot like a pipeline in that it has extensive maintenance capital expenditures that impact overall earnings and cash flow but not necessarily the ability to pay the dividend. The company uses an internal payout ratio, which compares dividend payments to free cash flow after its maintenance expenses. As of the last quarter, this came in at 60% (up from 55% YoY, but down from 58% QoQ). Of note, it is important to look at Exchange Income Corporation's dividend payout ratio on a trailing twelve-month basis because of the overall seasonality of the company.

Second, the dividend growth rate is on a 5-year basis. Before the pandemic, Exchange Income Corporation was a Dividend Aristocrat. It had increased the dividend from \$0.145 per month in 2014 to \$0.19 monthly in 2020, a mid-single-digit compound growth rate. The pandemic forced the company to stop dividend growth in an effort to maintain the dividend, which it did. This makes the 5-year dividend growth rate look abnormally small, much smaller than typical numbers.

Last year, the company raised the dividend twice for a total of 10.5%, with the last raise coming in August. The company came through with an additional raise of 5% in the third quarter of 2023, bumping the dividend from \$2.52 to \$2.64 annually. This will mark the 2nd consecutive year the company has boosted the dividend.

Finally, Exchange Income Corp is one of the few reliable monthly dividend payers. While this is no reason to buy a stock, for those seeking monthly income, we consider it a bonus.

RECENT EARNINGS

Earnings Estimates	2024	2025	2026
EPS	\$3.01	\$3.77	\$4.58
Revenue	\$2.68B	\$2.99B	\$3.19B
EBITDA	\$626M	\$707M	\$782M
EBITDA Margins	22.36%	23.2%	23.78%

After reporting a relatively soft quarter last report, Exchange Income rebounded in Q3. Although revenue of \$710M missed expectations for \$745M, earnings per share of \$1.29 came in well ahead of expectations for \$1.20.

Adjusted EBITDA grew 25% year-over-year and free cash flow came in 16% higher over the same timeframe.

The company has laid out a lot of capital expenditures over the last few years to improve the efficiency and operations of the business, and we're starting to see those improvements now. The company has won numerous contracts in its Aviation segment that are vaulting results at this point in time. With the investments made in its current and new aircraft, it should be in one of the best positions out of its competitors (there aren't many) to acquire new contracts in the future.

Its manufacturing segment, on the other hand, is lagging a bit. A lot of the businesses inside of this segment are highly cyclical and exposed to the weaker economy. A prime example would be the company's highrise window cleaning business. It witnessed a decline in revenue in this segment, likely attributed to a reduction in spending from many corporations.

It also reported a decline in its Precision Metal and Engineering business, but again, I'd attribute most of that to the cyclical nature of the economy, whereas things like Medivac services are more of an essential need.

Overall, the company is operating quite well, and I'm not overly concerned with the large miss on revenue expectations.

The company stated, with confidence, that its Adjusted EBITDA should come in the range of \$690M-\$730M next year. Considering last year the company reported Adjusted EBITDA of \$556M, this would represent a 24% boost on the low end of that guidance.

The Aviation segment remains strong, while the Manufacturing segment will no doubt pick up on a rebound in economic activity. I'm willing to be patient here.

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