



Small Cap Research

ESCO Technologies' Diverse Businesses, Growth Opportunity Attractive for Long Haul

Details: ESCO Technologies (ESE), Tech - Technical Instruments, \$38.04, Earnings Aug. 2nd

Recommendation: Buy at \$38 with a \$47.50 Target, Add at \$35 on Weakness

Thesis: ESCO Technologies is a simple case of a very favorable reward/risk profile. The \$1B Company is placed in the Technology sector on many sites, but I consider it more of an Industrial with its exposure to Aerospace, Utility, and Industrial applications. ESCO has substantial growth opportunities Internationally and is also experiencing strong organic growth. A low penetration rate for the 2.7 Billion Meters Worldwide leaves an opportunity to improve the current 14% CAGR. Valuation is also attractive at current levels and the \$1B market cap could lead to an eventual buyout. Growth in the RF shielding business will be driven by new wireless devices and technologies and also the increased usage of MRI's and other medical technologies. Metering contract awards should become to come in Internationally in late 2011 and drive 2012 visibility.

Overview: ESCO Technologies is a supplier of Utility Solutions, Engineered Filtration and Fluid Control Products, and a Leader in RF Shielding and EMC Test Products and Solutions. Revenues were broken down as 57%, 20%, and 23% for the previously mentioned business lines, in the respective order.

Fundamentals: ESCO shares trade 16X earnings, 1.46X sales 1.75X book value and 15.4X cash flow with a PEG of 0.93. Sales are growing 25% Q/Q and EPS at 120% Q/Q. The P/E, P/Sales, and P/Book are all near 5 year lows, while gross margins have been steadily rising since 2007, and ROE is near a 5 year high. ESCO beat EPS estimates by 32.4% last quarter and by 110.5% the prior quarter.

Analyst Coverage: ESCO's website lists 15 Analysts covering the stock, with JP Morgan, KeyBanc, Needham, Pac Crest, RBC, RW Baird and Wedbush the more familiar Companies. The average price target is \$44 with a high of \$47. Keybanc initiated shares a Buy with a \$45 target on June 28th and OpCo initiated with an Outperform and \$46 target on May 23rd.

Short Interest, Ownership and Options Analysis: ESCO has 3.8% of the float short, or 8.6 days to cover, up 33% since May. There is minimal Open Interest in options, and nothing to read from any action. Institutions owns 93.53% of shares, with Columbia Wanger, Waddell & Reed, BlackRock, and Vanguard owning 13.75%, 11.62%, 7.15%, and 5.11% of shares outstanding respectively. Newton Investment Mgmt. sold more than \$2M in shares recently.

Technical: The weekly chart of ESCO Tech (ESE) shows that a break above \$40 would be a key move to get shares moving strong. The RSI broke a downtrend on the weekly and MACD nearing a bullish crossover along with ADX. Shares are currently overbought on the daily and entry around \$36.50 may be possible on a pullback.

