



# Alaris Royalty Corp. (ALARF)

Updated August 28<sup>th</sup>, 2019 by Aristofanis Papadatos

## Key Metrics

<b>Current Price:</b>	\$15	<b>5 Year CAGR Estimate:</b>	10.0%	<b>Volatility Percentile:</b>	78.5%
<b>Fair Value Price:</b>	\$15	<b>5 Year Growth Estimate:</b>	2.0%	<b>Momentum Percentile:</b>	72.0%
<b>% Fair Value:</b>	98%	<b>5 Year Valuation Multiple Estimate:</b>	0.4%	<b>Growth Percentile:</b>	8.8%
<b>Dividend Yield:</b>	9.2%	<b>5 Year Price Target</b>	\$17	<b>Valuation Percentile:</b>	19.0%
<b>Dividend Risk Score:</b>	D	<b>Retirement Suitability Score:</b>	B	<b>Total Return Percentile:</b>	26.8%

## Overview & Current Events

Alaris provides capital to well-managed private companies in exchange for a monthly cash distribution. These distributions are set 12 months in advance based on the initial agreement and they are adjusted for the performance of the private company. Alaris has 14 employees and trades with a market capitalization of approximately \$550 million.

Alaris creates long-term partnerships with companies that have a successful historical record under various business conditions. Alaris seeks to partner with companies that offer required products or services in mature industries, with low risk of obsolescence, non-declining asset bases (no exploration companies), healthy free cash flows and low amounts of debt. Alaris used to partner primarily with healthcare companies but its current partners are 41% business services, 30% industrials and 29% consumer products and services. Alaris has 83% of its fair value of investments in U.S. companies.

In late July, Alaris reported (7/24/19) financial results for the second quarter of fiscal 2019. Revenue per share decreased 4% but only due to \$4.3 million of one-time distributions in last year's quarter. Adjusted revenue per share increased 14% thanks to distributions from new investments, which were partly offset by contract terminations by some companies. Earnings-per-share decreased from \$0.73 to \$0.60 but exceeded analysts' consensus by \$0.22. In the first half of the year, Alaris earned \$0.90 per share. Thanks to the positive surprise in the results of the second quarter, we have raised our earnings-per-share estimate for this year from \$1.40 to \$1.70.

## Growth on a Per-Share Basis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
<b>EPS</b>	\$1.83	\$0.73	\$1.97	\$0.84	\$1.09	\$1.58	\$1.68	\$1.81	\$0.32	\$1.65	<b>\$1.70</b>	<b>\$1.88</b>
<b>DPS</b>	\$0.99	\$0.93	\$1.04	\$1.17	\$1.35	\$1.47	\$1.56	\$1.62	\$1.62	\$1.62	<b>\$1.38</b>	<b>\$1.50</b>
<b>Shares<sup>1</sup></b>	9.6	13.7	17.6	21.5	26.7	30.4	34.0	36.3	36.8	36.8	<b>37.0</b>	<b>40.0</b>

Alaris aims to grow its revenue streams by adding a few partners every year, with these partners meeting the requirements of Alaris. Within its current revenue streams, the company aims to generate organic growth of 3%-5% per year. Moreover, management expects the short-term variations in the results of individual partners to be outweighed by the strong performance of others.

However, this is much easier said than done. While the business model of Alaris looks strong on the surface and aims to generate recurring and reliable revenue streams, the performance record of the company has been markedly volatile. Even worse, the earnings-per-share of the company in 2018 were lower than those in 2009. In other words, the company has been unable to grow its earnings-per-share in the last decade. We find it prudent to assume approximately 2% annual earnings-per-share growth over the next five years, about in line with inflation.

## Valuation Analysis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	Now	2024
<b>Avg. P/E</b>	5.5	12.3	7.1	26.8	27.9	17.3	14.2	10.5	51.3	8.5	<b>8.8</b>	<b>9.0</b>
<b>Avg. Yld.</b>	9.9%	10.3%	7.4%	5.2%	4.4%	5.4%	6.5%	8.5%	9.9%	9.8%	<b>9.2%</b>	<b>8.9%</b>

1. In millions

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Excluding the outlier years of 2012, 2013 and 2017, in which the depressed earnings resulted in an abnormally high price-to-earnings ratio, Alaris has traded at an average price-to-earnings ratio of 10.8 during the last decade. Due to the volatile earnings record of Alaris, we prefer to be conservative and assume a fair earnings multiple of 9.0. The stock is now trading at an earnings multiple of 8.8, which is very close to our assumed fair value level. If it reaches our fair value estimate over the next five years, it will enjoy a modest 0.4% annualized gain in its returns during this period.

## Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
Payout	54.1%	127%	52.8%	139%	124%	93%	92.9%	89.5%	506%	98.2%	<b>81.2%</b>	<b>79.8%</b>

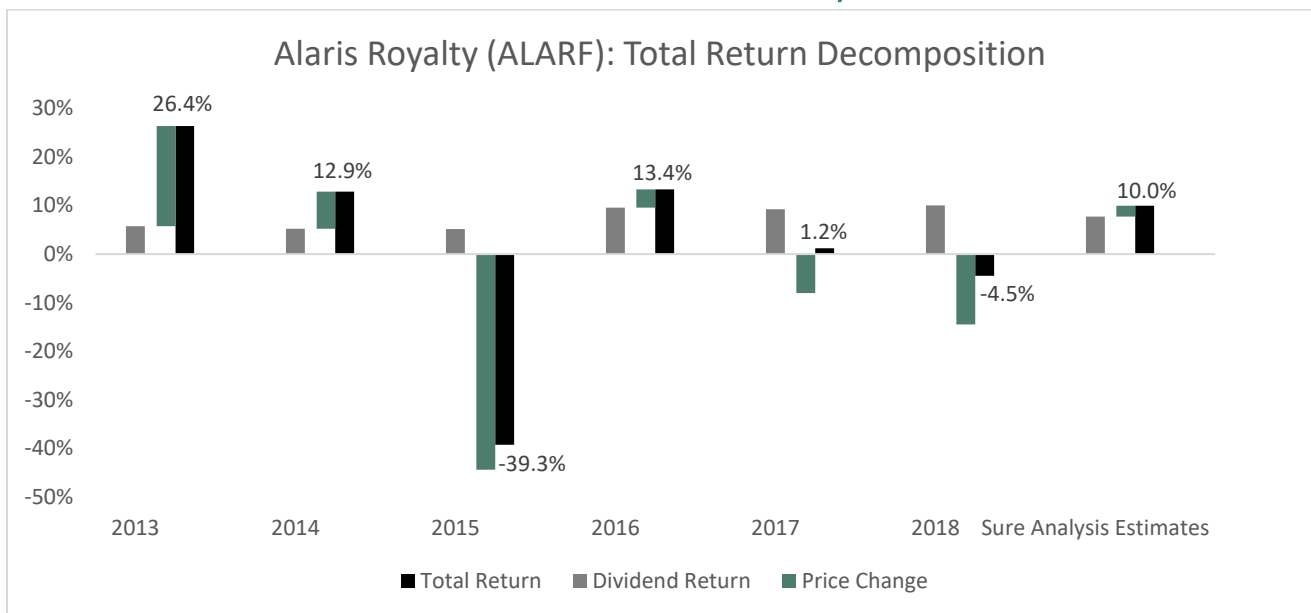
Alaris operates successfully in a niche market, as it partners with companies that have sound business fundamentals but find it uneconomical to borrow funds from traditional channels. Thanks to its strict screening process, Alaris partners only with reliable companies, which have decent free cash flows and low debt levels. As a result, the risk of seeing many of its partners facing liquidity problems is very low.

On the other hand, Alaris has exhibited a remarkably volatile performance record, as many of its partners have opted to terminate their partnership with Alaris. While Alaris makes a profit in such cases, its cash flows experience great variation from year to year. Even worse, Alaris is highly vulnerable to recessions, as companies tend to preserve their cash and reduce their leverage during such periods. Therefore, in the event of a recession, some of the partners of Alaris will probably terminate their partnership and will thus cause a shock in the cash flows of Alaris in the year after the recession shows up.

## Final Thoughts & Recommendation

Alaris has an attractive business model, as it generates cash flows from its partnerships with solid private companies. Moreover, the stock could offer a 10.0% average annual return over the next five years, primarily thanks to its 9.2% dividend yield. However, we are deterred by its volatile performance record and its vulnerability in the event of a recession. We thus rate the stock as a hold.

## Total Return Breakdown by Year



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## Income Statement Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
<b>Revenue</b>	18	17	49	32	50	67	83	100	89	100
<b>Gross Profit</b>	18	17	49	32	50	67				
<b>Gross Margin</b>	100%	100%	100%	100%	100%	100%	0.0%	0.0%	0.0%	0.0%
<b>SG&amp;A Exp.</b>	4	4	5	6	9	12	11	14	11	19
<b>Operating Profit</b>	14	13	44	26	40	54	68	84	77	81
<b>Operating Margin</b>	77.5%	75.2%	89.0%	81.0%	80.9%	81.2%	81.6%	83.7%	86.9%	80.9%
<b>Net Profit</b>	17	7	35	18	30	49	58	67	12	61
<b>Net Margin</b>	96.8%	44.4%	70.4%	56.2%	60.1%	73.6%	69.8%	66.5%	13.3%	60.7%
<b>Free Cash Flow</b>	14	12	15	26	44	50	55	73	67	78
<b>Income Tax</b>	-6	3	8	7	11	11	14	20	10	15

## Balance Sheet Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
<b>Total Assets</b>	164	228	246	333	481	580	788	787	799	891
<b>Cash &amp; Equivalents</b>	4	2	4	4	9	13	21	29	35	23
<b>Accounts Receivable</b>	0	1	3	1	1	6	11	17	9	1
<b>Goodwill &amp; Int. Ass.</b>	13	13	7	7	6	6	6	6	6	0
<b>Total Liabilities</b>	56	32	10	54	51	50	111	133	194	256
<b>Accounts Payable</b>	1	1	2	2	1	1	2	3	2	4
<b>Long-Term Debt</b>	29	29	7	50	45	36	77	99	173	228
<b>Shareholder's Equity</b>	109	196	237	279	430	530	677	655	605	636
<b>D/E Ratio</b>	0.27	0.15	0.03	0.18	0.10	0.07	0.11	0.15	0.29	0.36

## Profitability & Per Share Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
<b>Return on Assets</b>	11.2%	3.8%	14.6%	6.2%	7.3%	9.2%	8.5%	8.4%	1.5%	7.2%
<b>Return on Equity</b>	18.0%	4.9%	16.1%	7.0%	8.4%	10.2%	9.6%	10.0%	1.9%	9.8%
<b>ROIC</b>	13.8%	4.1%	14.8%	6.3%	7.4%	9.4%	8.8%	8.8%	1.6%	7.4%
<b>Shares Out.</b>	9.6	13.7	17.6	21.5	26.7	30.4	34.0	36.3	36.8	36.8
<b>Revenue/Share</b>	1.89	1.22	2.80	1.50	1.81	2.14	2.41	2.73	2.42	2.72
<b>FCF/Share</b>	1.46	0.91	0.83	1.23	1.60	1.59	1.60	2.00	1.83	2.13

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise.

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