Strip out regional jets and Bombardier isn't so bad

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MONTREAL - Bombardier Inc. stock (BBD.SV.B/TSX) has been a meagre investment for shareholders for a few years, and for many analysts, a difficult one to value. Canaccord Capital's Robert Fay hasn't even had a target price since August, 2004 -- it's "under review," with a "sell" recommendation -- due to uncertainty that continues to dog its aerospace business.

But **Anthony Scilipoti** of **Veritas Investment Research** has taken a cold, hard look at the different parts of the business, and put forward some numbers that may be of comfort to investors: the stock has a floor value of $2.30 per share, he says (it has traded between $2.28 and $3.66 in the past year). And it could be worth more than $3 if the company's parts are valued separately. The stock rose 1 cents yesterday to $2.86.

But his analysis comes with no enthusiasm: "Bankers, not shareholders, are in the driver's seat and there is little to look forward to," he surmises in his recent report, adding the company's almost-$2-billion pension deficit, US$2-billion in debt repayments over the next two years and tight-knit control by the Bombardier family are turnoffs. "If faced with a choice," he would invest in the company's preferred shares instead of its equity.

His valuation features one particularly eye-catching point: "Bombardier's segments are likely worth more individually than the sum of the parts." Furthermore, his break-it-up analysis assigns zero value to the flagship regional jet business. "While the assumption is extremely negative, it sets a 'safe' value for the stock," he said.

More on that in a bit. First, the good news. Sales of business jets and turbopropellerpowered airliners are going gangbusters and **Mr. Scilipoti** sees no reason why that business can't churn out operating profit margins similar to the industry's 10% to 15% range. With estimated revenue from those planes at US$3.75-billion for the year ended Jan. 31 (earnings will be released this month), that implies operating earnings of US$375-million. The whole aerospace group currently earns a margin of just 3%.

Similarly, he sees value in the company's other main business, passenger railcar manufacturing, which has earned a 4.2% operating margin in the past nine months and should earn US$295-million on US$7-billion for the year, he said. All told, he figures those two businesses, plus a contribution from Bombardier's shrinking finance arm, add up to $2.30 per share.

And what of the regional jet business? The **Veritas** analyst anticipates a big production cut this fiscal year, up to 2,000 layoffs and an associated payout to meet pension requirements. There could be facility closures and writeoffs. In a worst-case scenario, he estimates a total exit of the RJ business would cost Bombardier US$266-million before tax.

All very interesting. Is Bombardier likely to get out of the commercial jet business? Not likely, if you take everything company officials have said publicly at their word (despite the difficulties financing new jet purchases and the company's recent decision not to develop its CSeries family of 100 to 130-seat jets).

The company's response? It doesn't report on individual analyst reports. But spokesman John Paul Macdonald said its operating businesses "are very solid ... and valid contributors, and that's it."