April 2, 2017

Company Outlook: ECN Capital

Yale School of Management

A strong balance sheet with an uncertain future

Carter Page
+1 (224) 531-8380
carter.page@yale.edu

Ibukunoluwa Adereti
+1 (203) 684-4026
daniel.adereti@yale.edu

We recommend an overweight exposure to ECN Capital with a 3 to 5 year investment horizon.

Our conservative balance sheet valuation yields a per-share value of CA$4.13, representing a 15% upside to the current market price.

Given CEO Steve Hudson's successful track record, we believe the chance to purchase company assets for 74 cents on the dollar is a smart risk for investors to take.

Many Canadian fund managers lost big when Hudson's Newcourt Credit fell from CA$80 in March 1998 to CA$16 in 1999. We believe this ECN mispricing exists in part because a generation of Canadian fund managers loathe Hudson personally for money they lost buying at Newcourt's peak, despite Newcourt's dazzling success for long-term shareholders.

FY 2017 net income will rise from CA$33.0 million to CA$219 million following the CA$140 million gain on the announced C&V sale to PNC and lower restructuring costs.

Recommendation: BUY

Please see the disclaimer at the back of this report for important information.

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Company Overview

Introduction. ECN Capital Corp. (ECN) is a small-cap equipment finance company headquartered in Toronto, Canada, and is traded on the Toronto stock exchange with a current market capitalization of CA$1,410 million (USD $1,060 million). The company has three main divisions that operate in the United States and Canada: 1) Commercial and Vendor finance (C&V), 2) Rail finance, and 3) Aviation finance, with Rail finance being the largest of the three. The company was spun off from Element Financial (now Element Fleet Management) (EFN) on October 3, 2016, and since then has traded at a discount to book value under heavy selling pressure, bottoming at CA$2.60 a share in November 2016. The stock has recovered to CA$3.59, but still trades at a 24% discount to book value.

Element Financial & Newcourt Credit. Prior to the split in October 2016, ECN Capital and Element Fleet together formed Element Financial, a fleet management and equipment finance company founded in 2007 that began publicly trading in 2011. Element Financial was led by CEO Steve Hudson who is the current CEO of ECN Capital. From 2011 to 2015, the annual weighted average share price of Element Financial grew from CA$3.62 to CA$16.43, representing an approximately 46% annualized return for shareholders (excluding dividends).

Hudson has a long history in commercial finance starting with Newcourt Credit, which he founded in 1984 with USD $400,000 and sold to CIT in 1999 for USD $2,520 million. David McKerroll, ECN Capital's current president of Rail & Aviation Finance, ran Newcourt's corporate finance at the time.

Hudson's management style, while incredibly successful in the past, often employs large amounts of debt to make large, headline-grabbing acquisitions. These acquisitions lead to astronomical growth in company assets and high levels of leverage to boost returns. Hudson can be described as aggressive and unpredictable, with quick and sudden shifts into new lines of business when an acquisition opportunity arises. The company entered railcar leasing (the core of ECN capital today) in 2013 with a USD $2,000 million strategic alliance with leading railcar manufacturer **Trinity Industries (TRN)**. Hudson also famously raised CA$2,500 million for Element Financial in 2015 as a "blind pool" for future acquisitions, despite Element not having any definitive acquisition agreements. Most past acquisitions have been from companies wishing to dispose of smaller subsidiaries, and **Hudson has repeatedly said that he plans to continue his acquisition growth strategy with ECN Capital.**

Element Fleet Management. In May 2016, Hudson explained that the Element Financial split was intended to unlock value in Element's fleet management business (EFN), which today trades at a market capitalization of CA$4,800 million. **Investors saw the smaller ECN Capital as the riskier and less desirable spinoff of the larger and more predictable fleet management business.**

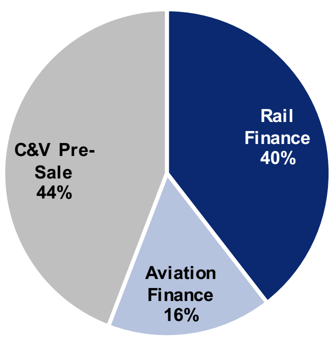
US C&V Sale to PNC. On February 21, 2017, ECN Capital announced that it had sold its US C&V division to PNC Bank for USD $1,250 million, representing a 16.5% premium to book value. Investors should note that this sale is not reflected in the most recent Q4 2016 financial statements, but is expected to close in early April 2017. ECN management has said that they plan to use the proceeds to pay down debt and strengthen the balance sheet **in preparation for an acquisition within the next twelve months.**

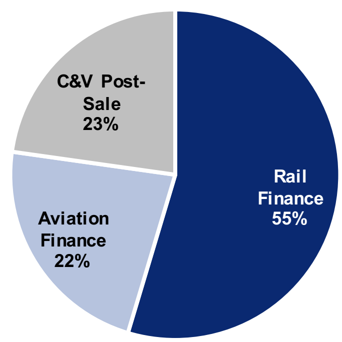
Company Divisions

Overview. Post-sale, ECN will have approximately CA$4,653 million of earnings assets divided between its Commercial & Vendor Finance, Rail Finance, and Aviation divisions. In FY 2016 (Pre-sale), C&V represented 33.9% of ECN's net financial income (revenue), but in terms of net financial income / assets (see Exhibit 3) C&V was the company's lowest performing division.

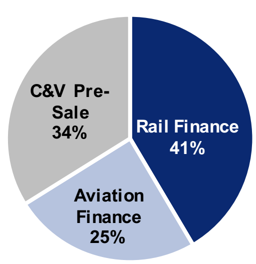
Exhibit 1: Company Divisions by Assets and Net Financial Income (Revenues)
As of December 2016. Post-sale figures estimated.

Company Divisions by Assets





Company Divisions by Net Financial Revenues (Pre-Sale)



Source: ECN Capital 2016 Q4 MD&A, ECN Capital February 2017 Investor Presentation

Exhibit 2: Balance Sheet by Division (Pre- & Post-Sale)

Dollar amounts in thousands CA$. As of December 2016. Post-sale figures estimated.

	Rail	Aviation	C&V	C&V (Post-Sale)	ECN Capital (Pre-Sale)	ECN Capital (Post-Sale)
Assets						
Finance receivables	$ 7,347.0	$ 690,328.0	$ 2,690,304.0	$ 907,304.0	$ 3,387,979.0	$ 1,604,979.0
Equipment under operating leases	$ 2,346,242.0	$ 272,370.0	$ -	$ -	$ 2,618,612.0	$ 2,618,612.0
Total Finance assets	$ 2,353,589.0	$ 962,698.0	$ 2,690,304.0	$ 907,304.0	$ 6,006,591.0	$ 4,223,591.0
Other assets	$ 188,913.0	$ 88,352.0	$ 147,298.0	$ 147,298.0	$ 424,563.0	$ 424,563.0
Goodwill and intangible assets	$ -	$ -	$ 5,200.0	$ 5,200.0	$ 5,200.0	$ 5,200.0
Cash Proceeds from Sale	$ -	$ -	$ -	$ 542,000.0	$ -	$ 542,000.0
Total Assets	$ 2,542,502.0	$ 1,051,050.0	$ 2,842,802.0	$ 1,601,802.0	$ 6,436,354.0	$ 5,195,354.0
Libabilities						
Debt	$ 1,793,583.0	$ 534,053.0	$ 2,176,955.0	$ 815,955.0	$ 4,504,591.0	$ 3,143,591.0
Other liabilities	$ 43,428.0	$ 14,522.0	$ 46,642.0	$ 26,642.0	$ 104,592.0	$ 84,592.0
Total Liabilities	$ 1,837,011.0	$ 548,575.0	$ 2,223,597.0	$ 842,597.0	$ 4,609,183.0	$ 3,228,183.0
Shareholder's Equity	**$ 705,491.0**	**$ 502,475.0**	**$ 619,205.0**	**$ 759,205.0**	**$ 1,827,171.0**	$ 1,967,171.0

Source: ECN Capital 2016 Q4 MD&A, ECN Capital February 2017 Investor Presentation

As an equipment finance company, ECN Capital's current business model depends greatly on the spread between its return on assets and cost of debt, which exposes the company to significant liquidity and interest rate risk. The company finances over 30% of its debt using secured loans that are backed by the assets on the company's balance sheet (such as the company's railcar portfolio). For borrowing, the company relies nearly 40% on a revolving term senior credit facility. Hudson has stressed that he has learned greatly about managing these risks after **Newcourt's implosion following the 1998 Russian Financial Crisis** when the stock fell from almost CA$80 a share in March 1998 to CA$16 a share in 1999 when it was acquired by C.I.T. **ECN received investment grade status BBB (low) from DBRS.**

While the railcar portfolio maintains a utilization rate of 97% (down from 99% during the previous year), the assets across all divisions are also subject to the risk of decline in value, especially in the fallout of the crude-by-rail boom. Management has stated that assets are worth at least book value, if not a premium.

Exhibit 3: Net Financial Income by Division (Pre-Sale)

Dollar amounts in thousands CA$. As of December 2016.

	Rail	Aviation	C&V	Total
Interest income and rental revenue, net	$ 149,302.0	$ 65,891.0	$ 139,498.0	$ 354,691.0
Interest expense	$ 74,240.0	$ 25,668.0	$ 63,688.0	$ 163,596.0
Balance	$ 75,062.0	$ 40,223.0	$ 75,810.0	$ 191,095.0
Syndication and other income	$ 10,928.0	$ 11,294.0	$ 17,999.0	$ 40,221.0
Provision for credit losses	$ -	$ 601.0	$ 23,600.0	$ 24,201.0
Net financial income (revenue)	$ 85,990.0	$ 50,916.0	$ 70,209.0	$ 207,115.0
Interest & rental revenue, net / Assets	5.9%	6.3%	4.9%	5.5%
Interest expense / Assets	2.9%	2.4%	2.2%	2.5%
Net financial income / Assets	3.4%	4.8%	2.5%	3.2%
Interest expense / Debt	4.1%	4.8%	2.9%	3.6%

Source: ECN Capital 2016 Q4 MD&A

Commercial and Vendor (C&V) Finance. Following the sale of the US C&V Finance division to PNC Bank, the company's remaining C&V business represents approximately CA$1,060 million, or 23% of assets. The company relies on its relationships with equipment vendors to provide financing on mid-ticket transactions ranging from CA$10 thousand to CA$10 million. ECN's C&V provides financing for companies in the construction, transportation, healthcare, and technology industries.

The assets of the C&V division are almost exclusively classified as finance receivables, and on a post-sale basis represent 57% of the company's outstanding finance receivables. The distribution of ECN's net finance receivables (inclusive of impaired receivables and deferred origination costs and subsidies) before the sale appears below. **Note that construction and transportation assets make up nearly 75% of the portfolio.**

Exhibit 4: Distribution of Net Finance Receivables (Pre-Sale)
Dollar amounts in thousands CA$. As of December 2016.
Inclusive of impaired receivables and deferred origination costs and subsidies.

Construction equipment	$	858,202.0	25.1%
Aircraft (not in C&V)	$	714,327.0	20.9%
Highway Tractors	$	520,122.0	15.2%
Restaurant equipment	$	293,057.0	8.6%
Highway Trailers	$	254,289.0	7.4%
Healthcare equipment	$	220,863.0	6.5%
Inter-city transportation equipment	$	211,393.0	6.2%
Office equipment	$	137,183.0	4.0%
Manufacturing equipment	$	111,733.0	3.3%
Industrial equipment	$	50,867.0	1.5%
Technology equipment	$	22,203.0	0.6%
Other equipment	$	16,136.0	0.5%
Golf carts	$	5,871.0	0.2%
Total	$	3,416,246.0	100.0%

Source: ECN Capital 2016 Q4 MD&A

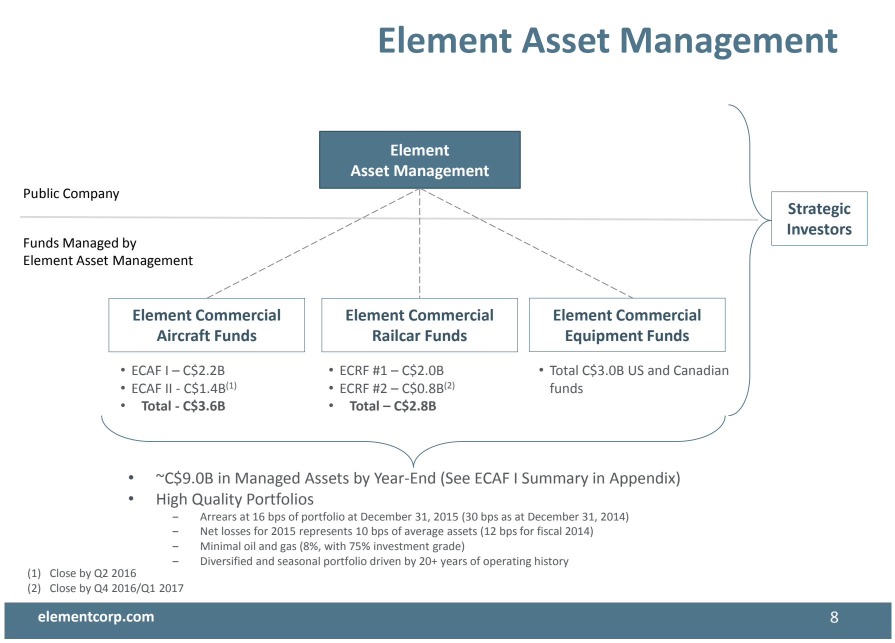
Source: AAR

Aviation Finance. ECN's aviation segment represents CA$1,051 million, or 22% of assets post-sale. In February 2016, Element Financial announced that it would discontinue its on-balance sheet aviation portfolio. ECN has said it would let the aviation portfolio "run off" with no new originations, meaning that the portfolio should gradually fall to CA$350 million by the end of 2019.

In June 2015, Element Financial successfully structured and sold a USD $1,210 million ABS fund (ECAF I. Ltd.) backed by leased aircrafts to over 30 institutional investors, the largest aircraft ABS transaction in a decade. Element collected a syndication fee for structuring the security, as well as yearly management fees that ECN now collects. **The success of ECAF I Ltd. has inspired Hudson to transform ECN Capital into an asset manager that structures and sells asset-backed securities to institutional investors, rather than the current business of ECN owning these assets itself.** Hudson argues that only in syndication and management fees will ECN Capital be able to generate a return on equity closer to 16-18%, as opposed to the current 3.1% ROE for FY 2016 (excluding separation and reorganization costs).

ECN's desired shift to securitizing leases into asset-backed products has been far slower than management's initial estimates. **In February 2016, management predicted that it could close a second commercial aircraft Fund (ECAF II) and two railcar funds (ECRF #1, #2) by Q1 2017. None of these ambitious funds have launched yet**, though in its most recent earnings call (March 7, 2017), Hudson assured that ECN was finding much demand for the assets. Management says it is currently working on either selling the assets through a fund or as a straight sale from the balance sheet.

Exhibit 5: Business Plan for ECN Capital as Asset Manager
Slide from February 2016 Element Financial Investor Presentation.



Source: Element Financial February 2016 Investor Presentation

Rail Finance. ECN's largest segment is rail financing, which represents CA$2,543 million, or 55% of assets post-sale. Element entered rail finance in 2013, when it formed a strategic alliance with Trinity Industries to acquire USD $2,000 million of leased railcars from Trinity over the next two years. Many of these cars were newly manufactured, leaving Element and now ECN Capital with an incredibly young railcar portfolio. Trinity collects fees from servicing these railcars, and the alliance was renewed in 2015 for another USD $1,000 million of railcars over the next four years. ECN Capital has also begun originating its own railcar leases.

The assets of the Rail Finance division appear almost exclusively as equipment under operating leases (meaning the company retains the railcars on its books). **The company charges depreciation against lease payments received** in order to arrive at the figure "rental revenue, net" which appears in Exhibit 3.

The Rail division depreciates railcars "up to 50 years from the date of manufacture to an approximate 10% salvage value", in line with the useful life of the young fleet. Rail division depreciation expense was CA$46.8 million in 2016.

As mentioned earlier, management is seeking to sell much of its railcar portfolio to institutional investors through structured ABS funds or as straight asset sales. In Q4 2016, management reported "ECN Capital sold a small portion (~2%) of its railcar portfolio at a 20% premium to asset NBV in the second half of 2016", **implying an approximate CA$47 million sale at a premium to book value. Information on this railcar sale was not segmented in either the 2016 Financial Statements or the 2016 Management Discussion & Analysis.**

ECN does not disclose the number of railcars that it owns or any fleet breakdown by car type. Since these railcars serve as collateral for some of ECN's secured loans, we were able to construct a sample of ECN's railcar portfolio using S&P Pre-Sale Reports for the ABS securities. This analysis revealed a high exposure to tank cars (approximately 50%) that when presented to management, we were told the following information: 1) approximately 35% of the railcars owned by ECN Capital are tank cars, and 2) nearly half of those tank cars (or 17.5% of the total cars outstanding) are leased to companies operating in the depressed crude-by-rail market. Despite the tank car and crude-by-rail exposure, management stated in our call and in the Q3 2016 earnings call that the railcar assets are worth at least book value, if not a 3-5% premium. Any losses in tank cars have been offset by gains on other car types in the portfolio.

The company's financial statements are audited by Ernst & Young.

Competition. ECN faces fierce competition in all lines of its business. In the C&V business its largest competitors are other independent lessors. The company depends on its relationships with vendors rather than approaching the business as a strict independent lessor competing against captive company lessors (subsidiaries of the vendors selling the product). In aviation, the company competes against many private aircraft lessors, though this competition risk has been minimized now that the company is unwinding its aircraft portfolio.

In Rail Finance, the company faces considerable competition from a number of railcar lessors and financing groups, including **GATX, Trinity Industries, CIT, Wells Fargo Rai**l, and **Union Tank Car** (subsidiary of **Berkshire Hathaway**). The asset management group **Napier Park Global Capital** also embarked on a similar joint-venture with Trinity Industries to acquire USD $2,100 million of railcars in order to package them into funds for institutional investors. Napier Park successfully closed a USD $259.84 million railcar ABS in April 2016, and has also structured several railcar and aircraft lease funds.

Investment Recommendation

Current Landscape

Taking into account the recent P&V Sale to PNC Bank, ECN shares are trading at a 34.6% discount to book value available to common shareholders (CA$4.83 per share). Though shares have gained much since bottoming at CA$2.60 in November 2016, the gap between price and book value represents an attractive risk-reward payoff for value-oriented investors with longer time horizons (3 to 5 years).

Consensus analyst estimates predict FY 2017 net income rising from CA$33.0 million to CA$219 million following the CA$140 million gain on the announced C&V sale to PNC and lower restructuring costs. FY 2018 earnings are expected to then fall to CA$72.8 million with lower revenues and fewer one-time gains on asset sales.

Any investment in ECN faces three major risks: 1) Acquisition risk arising from management's 12-month self-imposed deadline to make an acquisition, 2) Asset impairment risk resulting from a decline in the value of ECN's railcar portfolio, and 3) Earnings power risk if the company's planned asset sales and transformation do not materialize. Despite these significant headwinds, we believe that the market price provides an adequate margin of safety to protect the investor.

Our Recommendation

Despite significant risks facing ECN Capital, the current market price presents an opportunity to buy the company for 74 cents on the dollar, which provides an adequate margin of safety to protect the investor. We believe that the market is put off by the uncertainty surrounding management's plans for transforming ECN as well as the company's dismal return on equity. An attractive value play exists for long-term investors willing to ride out the volatility in the coming years.

Our Analysis

For our analysis, we perform a rigorous review of the company's balance sheet to calculate a conservative value for the company's assets. By providing a fundamental analysis of the various risks facing the company, we make clear potential downside that investors face.

Our final valuation aims not to calculate the precise intrinsic value of ECN Capital, but rather to demonstrate that the company's deep discount to book value provides an adequate margin of safety to protect investors. For this reason, we believe an overweight exposure to ECN Capital would be a smart risk for investors to take.

Exhibit 6: ECN Capital Stock Performance
Share price listed in CA$. Shares have recovered their losses after bottoming in late 2016, but still trade at a 24% discount to book value.

Balance Sheet Analysis

With 81.3% of the company's total post-sale assets in Finance receivables and Equipment under operating leases, we see that the book value of the company is largely determined by the value of these two accounts. We arrive at the current market price of ECN Capital if we suppose that both accounts lose 10% in value. Since the company is levered on a 1.6 Debt to Equity Ratio, a 9% fall in value of the assets leads to a 26% drop in shareholders' equity attributable to common shareholders. We do not, however, believe the market is pricing in this fall in book value. Rather, the market is more concerned with the uncertainty tied to the desired transformation of the company and the poor earnings prospects in the short-term.

Exhibit 7: Balance Sheet with 91% of Asset Value

Dollar amounts in thousands $CA. As of December 2016. Post-Sale figures estimated.

	Pre-Sale	Post-Sale	%	Adjusted
ASSETS				
Cash	$ 45,849.0	$ 45,849.0	100%	$ 45,849.0
Restricted funds	$ 136,871.0	$ 136,871.0	100%	$ 136,871.0
Finance receivables	$ 3,387,979.0	$ 1,604,979.0	90%	$ 1,444,481.1
Equipment under operating leases	$ 2,618,612.0	$ 2,618,612.0	90%	$ 2,356,750.8
Inventories	$ 140,019.0	$ 140,019.0	75%	$ 105,014.3
Accounts receivable and other assets	$ 38,212.0	$ 38,212.0	75%	$ 28,659.0
Notes receivable	$ 40,668.0	$ 40,668.0	90%	$ 36,601.2
Derivative financial instruments	$ 11,385.0	$ 11,385.0	65%	$ 7,400.3
Property, equipment and leasehold improvements	$ 3,812.0	$ 3,812.0	50%	$ 1,906.0
Intangible assets	$ 640.0	$ 640.0	25%	$ 160.0
Deferred tax assets	$ 7,747.0	$ 7,747.0	90%	$ 6,972.3
Goodwill	$ 4,560.0	$ 4,560.0	25%	$ 1,140.0
Cash Proceeds from Sale	$ -	$ 542,000.0	100%	$ 542,000.0
Total Assets	**$ 6,436,354.0**	**$ 5,195,354.0**	**91%**	**$ 4,713,804.9**
LIABILITIES				
Accounts payable and accrued liabilities	$ 84,252.0	$ 64,252.0	100%	$ 64,252.0
Derivative financial instruments	$ 2,980.0	$ 2,980.0	100%	$ 2,980.0
Secured borrowings	$ 4,504,591.0	$ 3,143,591.0	100%	$ 3,143,591.0
Deferred tax liabilities	$ 17,360.0	$ 17,360.0	100%	$ 17,360.0
Total Liabilities	$ 4,609,183.0	$ 3,228,183.0	100%	$ 3,228,183.0
SHAREHOLDERS' EQUITY				
Total Equity	$ 1,827,171.0	$ 1,967,171.0	76%	$ 1,485,621.9
Preferred Stock	$ 97,000.0	$ 97,000.0	100%	$ 97,000.0
Equity attributable to Common Shareholders	**$ 1,730,171.0**	**$ 1,870,171.0**	**74%**	**$ 1,388,621.9**
Number of Common Shares Outstanding	387,000	387,000		387,000
Book Value attributable to Common per Share	**$ 4.47**	**$ 4.83**		**$ 3.59**

C&V and Aviation Portfolio. Given that ECN was able to sell its US C&V Finance operation for a 16.5% premium to book value we believe the 10% loss on the remaining Canadian business modeled in Exhibit 7 is unlikely. While the aviation portfolio is in the process of winding down, we have found no cause for alarm in its value among analysts. That being said, the company's existing aircraft lease portfolio suffers from the same lack of disclosure as the railcar portfolio, thus we are more bearish on the aviation assets than the Canadian C&V portfolio.

Railcar Portfolio. ECN's railcar portfolio alone represents 36.6% of assets on a post-sale basis, and apart from a published utilization rate of 97%, average railcar age of 5 years, and average remaining lease term of 4 years, investors are given remarkably little information about the makeup of ECN's portfolio.

Fortunately, we were able to construct a sample of ECN's railcars using S&P ABS Pre-Sale Reports dating back to Element Financial that rely on ECN's railcar portfolio as collateral (these securities became part of the secured borrowings on the balance sheet for ECN Capital).

By our estimates, the three ABS securities that we analyzed, **Element Rail Leasing I LLC (Series 2014-1), Element Rail Leasing II LLC/Element Rail Leasing Canada L.P. (Series 2015-1),** and **Element Rail Leasing II LLC/ Element Rail Leasing Canada L.P. (Series 2016-1),** represent approximately **73.8% of ECN Capital's railcar portfolio. Our sample contains a weighted average of 50.5% tank cars.**

Exhibit 8: Railcar Sample Estimated Portion of Total

We estimate that our sample represents approximately 73.8% of the total ECN portfolio. Percent tank cars in our sample is 50.5%.

	2014	2016*	Total	Adjusted for Depreciation	CA$ (1 USD = 1.33 CAD)
Amount (USD $)	$ 401,544.00	$ 942,719.72	$ 1,344,263.7	$ 1,305,611.4	**$ 1,736,463.1**
# of railcars	4,267	8,578	12,845	-	-
Average age (years)	4.2	3.7	-	-	**Total Portfolio Book Value**
Average remaining lease term (years)	4.8	4.7	-	-	$ 2,353,589.0
Average lease rate (USD $)	$ 799	$ 931	$ 887	-	**Sample / Total**
% tank cars	**48.9%**	**51.3%**	**50.5%**	-	**73.8%**

**Merges railcars from 2015-1 deal*

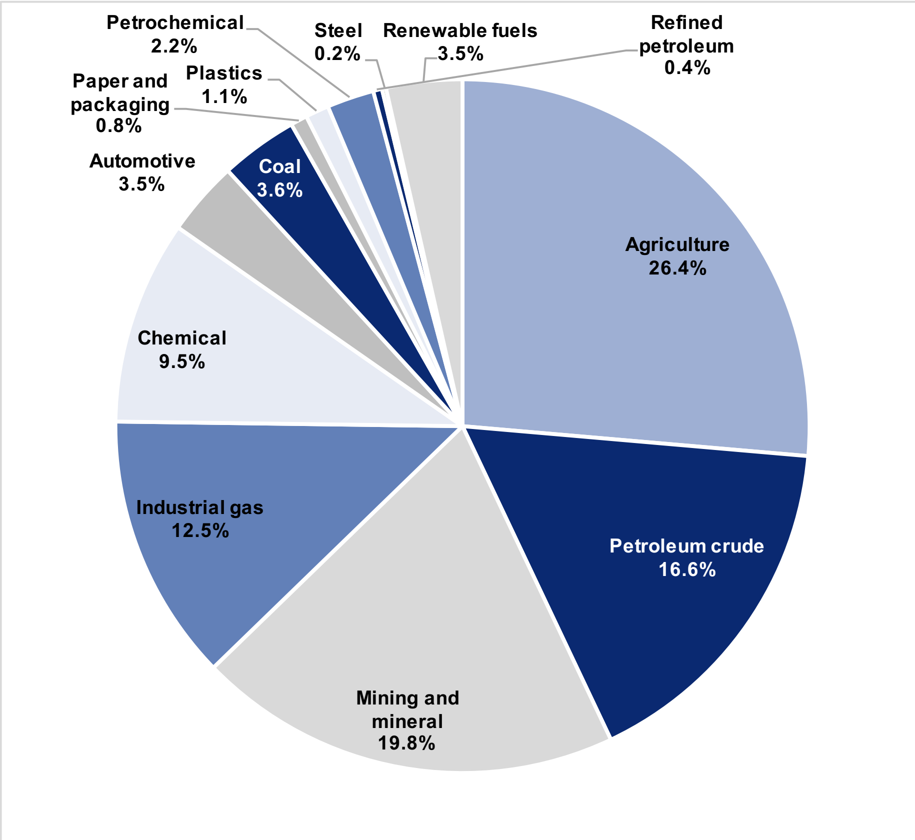
Source: Standard & Poor's

When we presented our sample findings to management, we were told the following information: 1) approximately 35% of the railcars owned by ECN Capital are tank cars, and 2) nearly half of those tank cars (or 17.5% of the total cars outstanding) are leased to companies operating in the depressed crude-by-rail market. The crude-by-rail exposure cited by management appears to match our sample petroleum crude exposure of 16.6%.

Exhibit 9: Railcar Sample Industry Exposure

Sample petroleum crude exposure matches 17.5% number provided by management.

**Note 2016 report merges 2015-1 railcars with 2016 cars*



	Total	2014	2016*
Agriculture	3,388	960	2,428
Petroleum crude	2,131	566	1,565
Mining and mineral	2,540	1,063	1,477
Industrial gas	1,602	423	1,179
Chemical	1,220	289	931
Automotive	446	-	446
Coal	464	227	237
Paper and packaging	100	-	100
Plastics	140	67	73
Petrochemical	282	217	65
Refined petroleum	53	-	53
Steel	24	-	24
Renewable fuels	455	455	-
Total	**12,845**	**4,267**	**8,578**

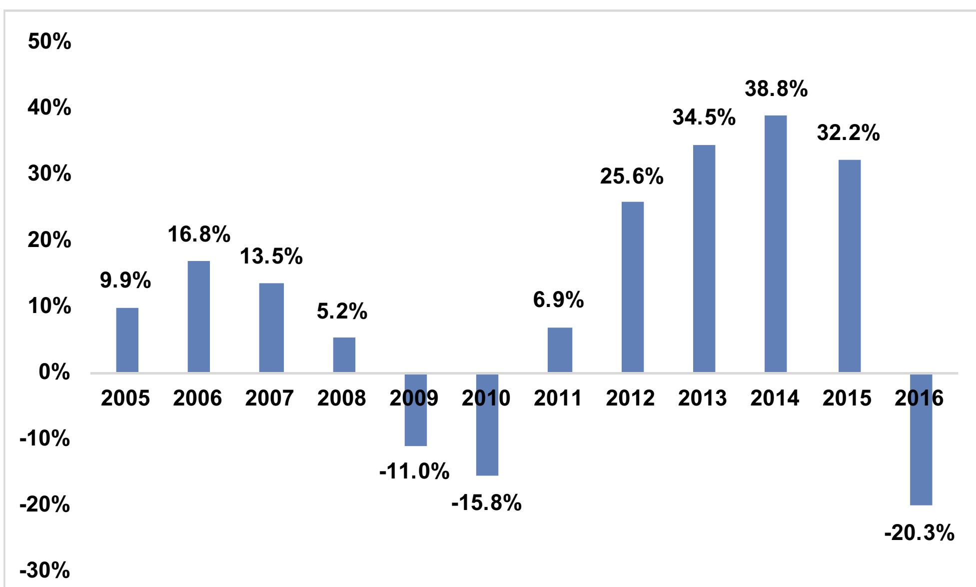
Source: Standard & Poor's

Using our railcar sample portfolio, we can now form a better judgement as to the appropriate value of the total railcar portfolio. Since ECN Capital's railcar portfolio is incredibly young (average age of 5 years), the company has negligible exposure to the DOT-111 railcars under new regulations following several accidents in 2013 and 2014. Generalizing from our sample, we see ECN's fleet also has a small 3.6% exposure to coal, matching management's guidance.

If we turn to the troubled crude-by-rail exposure, we see that 16.6% of the sample (17.5% using management figure) most likely has seen a fall in value given most of the cars were acquired during the crude-by-rail boom. As an added safety, let us assume the deteriorated assets expand beyond the crude-by-rail exposure to all tank cars (~50% sample, ~35% management total). Assuming the rest of the portfolio is worth book value (despite management urging that it has actually gained value), the value of all tank cars in the portfolio would needed to have fallen 20% sample (30% management) to justify a 10% fall in the portfolio value that we model in Exhibit 7. **Given the lack of write-offs across the industry, recent sales at above book value prices, and our faith in the company's auditor, Ernst & Young, we do not believe that a 20-30% fall in the value of these cars has occurred.**

If we examine the GATX Lease Price Index (LPI) for railcar leases, we see that renewal rates fell 20.3% in 2016 and are expected to fall even further in 2017. The LPI tracks GATX's own portfolio of railcars, which are approximately 50% tank car with 30% exposure to petroleum, an even more bearish portfolio than ECN Capital's.

Exhibit 10: GATX Lease Price Index (LPI)
Average renewal lease rate change in percent.



Source: GATX Investor Relations

Since the average remaining lease term is 4 years on ECN's railcar portfolio, we see the company moderately protected from falling lease rates over the next couple years.

We therefore, feel very comfortable with a balance sheet valuation of 95% of assets as a conservative baseline before we consider the more abstract elements of our decision, such as management and acquisition risk. Note that this value is not in our opinion the precise intrinsic value of the company (we feel intrinsic value is all but impossible to calculate for a company with this much uncertainty). Rather, this figure is a conservative baseline of value that we feel comfortable with after our balance sheet analysis.

Insider Activity

We would also like to point to the flurry of buying that has occurred over the past five months by company insiders. Steve Hudson is the largest shareholder of the company, holding 10,241,727 shares, or 2.65% of the total shares outstanding. Although management has been unpredictable, we feel comforted that they are in fact "eating their own cooking."

Exhibit 11: Insider Activity
Insiders have been buying the stock heavily over the past five months.

Trade Date	Net Sell (Shares)	Net Buy (Shares)	Close Price
3/23/17		100,000	$ 3.40
3/15/17		284,200	$ 3.53
3/10/17		12,000	$ 3.47
3/9/17		100,000	$ 3.54
2/13/17		15,000	$ 3.12
12/20/16		15,000	$ 3.17
12/6/16		317,982	$ 3.15
11/25/16		263,500	$ 3.11
11/24/16		92,100	$ 3.11
11/23/16		215,000	$ 3.06
11/22/16		2,358,000	$ 3.10
11/21/16		165,000	$ 3.09
11/18/16		6,821,000	$ 2.94
Totals		10,758,782	

Source: Bloomberg

Currency Exchange Risk

Although ECN is a Canadian company, we believe much of our exchange risk is protected since the majority of the business is in the United States. Our balance sheet margin of safety also provides a source of protection against exchange rate risk.

Earnings Estimates

A Word on Predicting ECN's Cash Flows.

We have shied away from a traditional discounted cash flow (DCF) analysis since we have found that forecasting the future earnings of a company that plans to package and sell its assets to institutional investors in order to fund surprise acquisitions into unpredictable lines of business makes earnings forecasts for ECN incredibly erratic. ECN's future path is uncertain, and management is notorious for sudden moves and reversals as soon as market conditions change. I**n December 2016 management explained to analysts that its secondary goal was to grow in middle market US C&V lending. Less than three months later ECN sold its US C&V division to PNC Bank, and exited the market.** In truth, the earnings of ECN are driven more by the one-time gains from sales of assets than the operating income of leases, and given Hudson's management history we argue it would be foolish to assume capital will be deployed in the same line of business for the next three years, let alone for perpetuity.

We believe that the more prudent analysis begins by treating ECN less as a company, and more as a portfolio of assets. If we can establish a baseline value for these assets by scrutinizing potential risks (which we hope we have done), we can then have a starting point to weigh the various more abstract factors such as future acquisitions and management strategy that are the major drivers for this company going forward.

That being said, we still provide earnings estimates which are simply analyst consensus. Please remember to take these with a grain of salt considering the nature of ECN's business.

Exhibit 12: Consensus Analyst Earnings Estimates

Amounts in thousands $CA. The sharp rise in 2017 net income is due to the CA$140 million gain on sale of US C&V to PNC.

	2016 (Actual)	2017 (Estimate)	2018 (Estimate)
Revenue	$ 207,115	$ 223,000	$ 185,500
Operating Profit	$ 30,689	$ 117,200	$ 132,750
Pre-Tax Profit	$ 134,911	$ 161,800	$ 117,600
Net Income Adj+	$ 106,829	$ 97,600	$ 99,600
Net Income	$ 33,004	$ 219,000	$ 72,800
Book Value per Common Share	**$ 4.47**	**$ 5.02**	**$ 5.20**

Source: Bloomberg

Valuation

Our final valuation of ECN reflects that the key drivers of value for the company will be future acquisitions and management's ability to make sound purchases at fair prices. We begin with a rigorous analysis of the company's balance sheet to establish a baseline value of worth we can use to frame our argument about these qualitative factors.

From our balance sheet analysis, we conclude that 95% of asset value is a conservative valuation of the assets on the balance sheet. Note our goal is not to pinpoint the exact intrinsic value of the company, but rather to establish what is a conservative baseline of value. This valuation yields a per-share value of $4.13, representing a 15% upside to the current market price.

Exhibit 13: Balance Sheet with 95% of Asset Value

Dollar amounts in thousands $CA. As of December 2016. Post-Sale figures estimated.

	Pre-Sale		Post-Sale		%	Adjusted	
ASSETS							
Cash	$	45,849.0	$	45,849.0	100%	$	45,849.0
Restricted funds	$	136,871.0	$	136,871.0	100%	$	136,871.0
Finance receivables	$	3,387,979.0	$	1,604,979.0	95%	$	1,524,730.1
Equipment under operating leases	$	2,618,612.0	$	2,618,612.0	95%	$	2,487,681.4
Inventories	$	140,019.0	$	140,019.0	75%	$	105,014.3
Accounts receivable and other assets	$	38,212.0	$	38,212.0	75%	$	28,659.0
Notes receivable	$	40,668.0	$	40,668.0	90%	$	36,601.2
Derivative financial instruments	$	11,385.0	$	11,385.0	65%	$	7,400.3
Property, equipment and leasehold improvements	$	3,812.0	$	3,812.0	50%	$	1,906.0
Intangible assets	$	640.0	$	640.0	25%	$	160.0
Deferred tax assets	$	7,747.0	$	7,747.0	90%	$	6,972.3
Goodwill	$	4,560.0	$	4,560.0	25%	$	1,140.0
Cash Proceeds from Sale	$	-	$	542,000.0	100%	$	542,000.0
Total Assets	**$**	**6,436,354.0**	**$**	**5,195,354.0**	**95%**	**$**	**4,924,984.5**
LIABILITIES							
Accounts payable and accrued liabilities	$	84,252.0	$	64,252.0	100%	$	64,252.0
Derivative financial instruments	$	2,980.0	$	2,980.0	100%	$	2,980.0
Secured borrowings	$	4,504,591.0	$	3,143,591.0	100%	$	3,143,591.0
Deferred tax liabilities	$	17,360.0	$	17,360.0	100%	$	17,360.0
Total Liabilities	$	4,609,183.0	$	3,228,183.0	100%	$	3,228,183.0
SHAREHOLDERS' EQUITY							
Total Equity	$	1,827,171.0	$	1,967,171.0	86%	$	1,696,801.5
Preferred Stock	$	97,000.0	$	97,000.0	100%	$	97,000.0
Equity attributable to Common Shareholders	**$**	**1,730,171.0**	**$**	**1,870,171.0**	**86%**	**$**	**1,599,801.5**
Number of Common Shares Outstanding		387,000		387,000			387,000
Book Value attributable to Common per Share	**$**	**4.47**	**$**	**4.83**		**$**	**4.13**

ECN Capital is not a stock to add to the portfolio and lose touch. It is a company shrouded with uncertainty, in part intentional by management. Before settling down with these shares, be prepared to follow the company diligently as we have seen future plans be reversed one quarter after another and surprising acquisitions be announced and called off with no warning. One thing we are certain of is that the ECN two years from now will be far different than the ECN of today, and we lean on the fact that this company needs to be re-evaluated quarterly when we make our recommendation.

We are concerned when we see management cite "adjusted earnings" that strip out true expenses such as executive compensation. Likewise, we are concerned when management appears reluctant to answer basic questions about the key assets on the company's balance sheet that force piecing together a sample pool from Standard & Poor's to get answers. Yet despite these negatives, we would like to point to the startling success that Hudson has had in building strong companies over the past 30 years. Investors in first Newcourt, and later Element Financial were handsomely rewarded for putting up with Hudson's uncertainty as both companies pivoted and continually surprised analysts.

Thus, when presented with the opportunity to acquire shares in the company at 74 cents on the dollar (after rigorously testing the book value of the company), we believe ECN Capital is a smart risk for the diversified investor to take. The three major risks 1) overpaying for future acquisitions, 2) impairments in asset value, and 3) a current low return on equity create large uncertainties for the stock. Yet investing requires decisions to be made under great uncertainty and with incomplete information.

The market has acknowledged these risks and created a wide gap in price to book value. Our analysis has shown that the book value (or a slight discount to book) of the company is a strong basis to establish a baseline value with an adequate margin of safety. Judging whether management will grow or squander that value, we side with Hudson's performance over the past 30 years to deliver. That being said, we leave the door open to future analyses as ECN Capital continues to evolve.

At this point, we believe the adequate margin of safety that ECN Capital provides makes the company a smart risk for investors to take, and therefore recommend an overweight exposure to the company.

Conclusion

Despite significant risks facing ECN Capital, the current market price presents an opportunity to buy the company for 74 cents on the dollar, which provides an adequate margin of safety to protect the investor. We believe that the market is put off by the uncertainty surrounding management's plans for transforming ECN as well as the company's dismal return on equity. An attractive value play exists for long-term investors willing to ride out the volatility in the coming years. We therefore recommend an overweight exposure to the company with a 3 to 5 year investment horizon.

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