Quiksilver Inc. (ZQK)

November 18, 2002

As of close 11/18/2002:

S&P 500:	**901.77**
10-Year Bond:	**4.05%**
ZQK	**24.96**

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Surf's Up for ZQK

Recommendation ……….**Buy**
Target Price…………………..**$31**
Timeframe…………………..**6 months**

Definition of Ratings

<u>Buy</u>: Equity is at least 20% undervalued.
<u>Hold</u>:Equity is approximately fairly valued.
<u>Sell</u>: Equity is at least 20% overvalued.

Summary

- European sales up more than 25% for 2001. With 36% of revenues coming from international markets, this bodes well for future growth prospects.
- Quiksilver will continue this international trend and will also continue to supplement this growth with respectable domestic sales figures. 2001 domestic sales were up 6%.
- Costs are stable, and are not projected to increase, even given the aggressive branding campaigns that the Company utilizes.
- 5-year historical CAGR is 15%, largely as a result of management's expertise at identifying and capitalizing on trends.
- Bookings (orders placed by retailers) are significantly up, reflecting the underlying trend in interests in board-riding sports. Quiksilver is currently the leading player in a growing niche, by virtue of its strong branding and awareness with boardsports enthusiasts.
- Further, our bullish projection has precedence as the Company has seen P/E ratios above 23x.

Business Overview

Industry Leader in the Surfing Business

- Quiksilver, Inc. was incorporated in Delaware in 1976. It designs, produces and distributes clothing and accessories with a casual style. It is the market leader in the surfing industry and its success is driven by its ability to identify and follow the core of boardsports.

Growing Sports Apparel Industry Despite the Recession

- Consumer spending for active sports apparel exceeded $6 billion in 2001. It is expected to grow in 2002, despite the recession, as some consumers move away from fashion-inspired purchases and opt instead for functional clothing with multiple purposes. [1]

Surfing Image as the Sales Driver for All Product Lines

- Industry-wide, boardsports represent $9.9 billion in annual revenue, with roughly 80 percent of that coming from sales of related clothes, shoes and accessories. Though skateboarding counts as the dominant action sport in terms of the number of participants in it, boardsports are still driven by the image and influence of the surf lifestyle.

[1] Source: the 2002 SGMA State of the Industry Report, which was released on January 20 during The Super Show®/20-02 in Las Vegas, Nevada.

- Quiksilver's product line includes shirts, walkshorts, t-shirts, fleece, pants, jackets, snowboard wear, footwear, hats, backpacks, sportswear, swimwear, etc. Watches and eyewear are produced by licensees. Its main customers are young men and young women (4-20 years old) with brands under Quiksilver, Roxy, Raisins, Radio Fiji, Hawk Clothing and Gotcha (Europe) labels. Snowboards, snowboard boots and bindings are under the Lib Technologies, Gnu, Supernatural Manufacturing and Bent Metal labels.

Being One of the Few Apparel Companies Successfully Tapping into the Growing *Female* Sports Apparel Markets

Indications of strength and growth in female boardsport market:

- Between 1997 and 2000, spending for women's sports apparel rose 20% to $15.86 billion, while men's spending inched ahead by just 1%, according to the Sporting Goods Manufacturers Association. [2]

- Women spend about 80% of all money that goes to sportswear and control 60% of the money spent for men's sports apparel. [3]

- In 1996, the nation's first all-female surfing school, Surf Divas of Encinitas, California was launched. In the same year, the first all-women's surf shop, Watergirl, opened north of San Diego. *(Outside Magazine)* [4]

- 2002, October – The recent release of the Walt Disney Pictures animated hit "Lilo and Stitch" and the success of Universal Pictures "Blue Crush," a film about a group of female surfers, has created a groundswell of women who want to surf. [5]

- Females account for some 9 percent to 11 percent of the skateboard market, 22 percent to 25 percent of the snowboard market and 20 percent to 23 percent of the surf market. Quiksilver, Billabong and Rusty have successfully built junior labels for these customers. [6]

Acquisition Focused in

Acquisitions History –
1994 – The company acquired The Raisin Company, a swimwear

[2] Source: http://216.239.53.100/search?q=cache:SVbHTbhZL6wC:www.wsjclassroomedition.com/archive/01dec/MKTG_nike.htm+women+apparel+market,+2002,+growth&hl=en&ie=UTF-8
[3] Source: http://216.239.39.100/search?q=cache:SVbHTbhZL6wC:www.wsjclassroomedition.com/archive/01dec/MKTG_nike.htm+women+apparel+market,+2002,+growth&hl=en&ie=UTF-8
[4] Source: *http://www.ewowfacts.com/wowfacts/pdfs/women/31sports.pdf*
[5] Source: http://216.239.37.100/search?q=cache:pEPFa9MLnyEC:www.iht.com/articles/72727.htm+female+sport+apparel+market,+growing,+2002&hl=en&ie=UTF-8

[6] www.apparelnews.net

the Core Sportswear Industry

business.
1997 – The company acquired Mervin Manufacturing, a snowboard business.
2000 – The company acquired Hawk Designs, which owns the rights to use Tony Hawk, a skateboarding icon.
2000 – The company acquired Freestyle, S.A., the European licensee of the Gotcha trademark.
2000 – The company acquired John Ashworth, a startup business in golf apparel.
2001– The company acquired Quiksilver International, an Australian company that owns the worldwide trademark rights to the Quiksilver brand name other than in the United States and Mexico where those rights were already owned by the company.

Recent Business Development –
2002, September – The company signed a lease to open a company-owned Boardriders Club retail store in the middle of Times Square. The store is scheduled to open next April.
2002, September – The company acquired Beach Street, the operator of 26 Quiksilver outlet stores.

Prices for Main Products

The domestic retail prices for its apparel products range from approximately $18 for a t-shirt and $42 to $47 for a typical short to $200 for a typical snowboard jacket. For its Quiksilver Europe products, retail prices range from approximately $26 for a t-shirt and about $50 for a typical short to $140 for a typical snowboard jacket. As for snowboards, domestic retail prices range from approximately $250 to $475 and in Europe up to approximately $500.[7]

Business Divisions

Focused In-House Design Force

The company designs the majority of its' products. Many of the company's managers, employees and independent sales representatives are involved in surfing, snowboarding, skateboarding and other sporting activities. They serve as product design consultants regarding the customer taste and market trend. Quiksilver's ability to take the pulse of its customer is part of its competitive advantage.

Focused Promotion and Advertising

The company's history is in the sport of surfing and the beach culture, and its casual style is driven from a boardsports heritage. It has always maintained a strong marketing and advertising presence in the surfing world as well as other youth board riding marketplaces. The company's strategy is to continue to promote its core image associated with surfing and other board riding activities. [8]

[7] Source: 10K.
[8] Source: 10K

ZQK's main marketing activities include:

- Magazine advertisements and trade shows: Print images of high profile athletes in surfing, snowboarding, skateboarding and windsurfing;
- Holding surf, snowboard and skateboard contests in the markets where it distributes products. Locations include Hawaii, California, France, and Austria. [9]
- Co-branding arrangements with car producers and video games. For example, Peugeot and Toyota produce cars branded with Quiksilver and Roxy, and the Tony Hawk Pro Skater 3 video game is cross-promoted by both the company and Activision.

The company generally does not offer on-sale programs to its customers.

Manufacture

Over half of the company's domestic products are manufactured in the United States and the majority of its European products are manufactured in Asia. Goods are generally manufactured and processed on an order-by-order basis. During fiscal 2001, no contractor or finished goods supplier accounted for more than 6% of the company's consolidated production.

Competition

The market for beachwear, snowboardwear, skate apparel, casual sportswear and snowboards is fairly competitive. The main competitors include Billabong, Hurley, O'Neill and Volcom. In the department store and specialty store channels, the competitors include brands such as Tommy Hilfiger, Abercrombie and Fitch, Nautica and Calvin Klein. In Europe, the main competitors in the core market include O'Neill, Billabong, Rip Curl, Oxbow and Chimsee. In the snowboard wear and snowboard market, the Company's principal competitors are Burton, K-2 and Morrow.

Although there are several players trying to reach the young consumer with casual, lifestyle-oriented apparel, we feel that Quiksilver is uniquely positioned:

1) Quiksilver currently boasts the most impressive array of celebrity spokespeople in the sector. This lineup assures that the company will maintain its "real" image and continue to attract core customers. Celebrity pitch-people also assure that the company can fetch reasonable margins while fending off lower-quality knock-offs.

[9] Each winter, the Quiksilver in Memory of Eddie Aikau big wave contest is held at Waimea Bay in Hawaii, and the Mavericks Men Who Ride Mountains Big Wave Contest is held at Half Moon Bay in California. The Roxy Pro is held annually at Sunset Beach in Hawaii. In Europe, the Company produces the Quiksilver Masters surfing event in France, the Bowlriders skateboarding event, also in France, and is one of the sponsors of the Air & Style snowboard jumping event in Austria. Other regional and local events are also sponsored such as surf camps and skate park tours. (Source: 10K)

2) The company identifies and acquires small, well-situated competitors before they become large, and then parlays the location occupied by this company into another local presence for itself. By offering a wide variety of clothing and accessories that appeal to the same audience, Quiksilver avoids alienating the local customer base and thus expands its audience through a "guerilla acquisition" strategy.
3) Quiksilver's track record of being able to take the pulse of the boardsports enthusiast shows no sign of dissipating. If anything, the Company has demonstrated that it will become more and more popular as a brand, solidifying its position with loyal customers who are extremely brand- and image-conscious. As we see no reason for the boardsports arena to shrink in terms of spending or enthusiasm, we are confident that Quiksilver can maintain its position for many years to come. We believe that other analysts have taken a more pessimistic view of the company's prospects and have thus undervalued the equity.
4) A significant competitive response would require replicating the Quiksilver model. As the company has painstakingly assembled brands, locations and spokespeople over many years, we feel that dislodging it would require a sustained, multi-year effort by a committed player. We have not observed such an effort by a properly funded competitor thus far, although smaller but established players could certainly make inroads over time.

Revenues

Overview

- Quiksilver's sales are generated within two major markets: The United States (61% of sales in 2002 YTD) and Europe (39% of sales in 2002 YTD). Their products are distributed through a variety of channels that include surf shops, Boardrider clubs, independent specialty stores and specialty chains, depending on the target demographic being served and the geographic location.
- Over 80% of domestic products are manufactured in the United States. The balance is imported. The majority of the Company's European products are manufactured in Asia. Sales are included as either domestic or European based on which division produced and shipped the product.
- The Company also generates revenues from royalties collected from licensing its brand name. However, this has historically constituted less than 1% of their gross revenues. Generally, licensees manufacture and distribute approved clothing, accessories and related products using the Quiksilver and Roxy trademarks. Licensed products include clothing, watches and

eyewear.

- Overall, net Sales for the 9 months ending July 31 were $505,737,000. This represented a 13.6% increase over the net sales for the comparable period in 2001. Domestic net sales for the same period increased 6.2% to $308,358,000 from $290,477,000 in 2000, and European net sales increased 27.5% to $197,379,000 from $154,813,000 for those same periods.
- The company's policy is to sell directly to retailers who merchandise their products in a manner consistent with the Company's image and the quality of its products.

Sales by Region

	% of Sales		
Region	**Domestic**	**Europe**	**Consolidated**
US West Coast	46		30
US East Coast	21		13
Hawaii	5		3
Other US States	18		11
France		46	17
UK and Spain		32	12
Other European Countries		22	7
Other International	10		7

Percentages of fiscal 2001 sales by geographic region (excluding licensees)

- 46% of Domestic sales accrue from sales on the West coast. This is reflective of the huge surf and board sport adherents in the area.
- There is a strong effect of seasonality on the demand for certain products. Quiksilver counteracts this with a strategy of geographically diversifying its customer base.

Sales By Distribution Channel

Distribution Channel	Domestic	Europe	Consolidated
Boardriders Clubs, surf shops, and Quiksvilles	24	39	30
Specialty Stores	52	44	48
Department Stores	14	8	12
Domestic Exports	10		7
European Distributors		9	3
Total Division	64	36	100

- Sales are spread over a large wholesale customer base. In 2001, approximately 22% of the Company's consolidated net sales were made to the Company's ten largest customers. No single customer accounted for more than 7% of the Company's consolidated net sales during the same period.

- A group of 210 independent sales representatives in the United States and Europe, and 61 distributors in Europe are responsible for selling the companies products. The Company's sales representatives are generally compensated on a commission basis.
- There is a strong movement by Quiksilver to build its network of concept stores (Quiksilver's selling space in the retail stores of selected customers). These are referred to as Quiksvilles. There were 203 additional Quiksvilles launched in 2001, representing an increase of almost 20% over the previous year's figures.
- The core of the company's sales is done through surf shops, Boardriders Clubs, and specialty stores where there is a Quiksville. Approximately 30% of the Company's sales were done through this channel of distribution in fiscal 2001. Most of these stores stand-alone or are part of small chains.
- Independent specialty or active lifestyle stores and specialty chains were responsible for 48% of the company's sales in 2001. This category includes chains such as Pacific Sunwear, Nordstrom, Duty Free Shops, and the Buckle, as well as many independent active lifestyle stores, snowboard shops and sports shops.
- The Company also sells its products to a limited number of department stores, including Macy's, Dillards, The Bon Marche and Burdines in the United States; and Harrods and Lillywhites in Great Britain. Sales to the department store channel totaled 12% of consolidated net sales in fiscal 2001. Approximately 3% of the Company's business is done through distributors in certain European countries.10

Brand Acquisition

- In July of 2000, the company acquired Quiksilver International Pty Ltd. Consequently, the company now owns all international rights to use the Quiksilver trademark. This represents a huge potential market opportunity for the company.

Costs

Summary

- In line with others Branded Apparel companies in our universe, Quiksilver also imports a significant percentage of its products from countries with cheaper labor, driving prices down, and

[10] 10K Financial Statement 2002

enabling better margins.

- Management and snowboard production is kept in house.
- A few recent acquisitions in an attempt to vertically integrate will drive up costs, but will be more than offset by the gains in revenue from these acquisitions as reported above in the revenue section of this report.
- Following the recent trend, Royalty Revenue will be larger than Royalty Expense, and this surplus will continue to grow in the quarters to come.
- All of the above factors are already incorporated into the Quiksilver's stock price. What remains speculative, however, are its recent Times Square store purchase and the 26 outlet stores purchases. Due to the decrease in retail spending, the current stock price reflects a poorer than average performance for this store. Our outlook on this store, however, is bullish. In-line with ZQK's store performance all over the country, the Times Square Store will generate in excess of $1000 per square foot, raising revenue by over $3M by this time next year. The Outlet Stores will also add to revenue.
- Adding to our bullish outlook, we further believe that Branding will remain extremely strong. While this costs the Company 5% of sales, the consumer marketplace is highly responsive to this and will remain so for our investment horizon.

Production and Raw Materials

- For fiscal year ended 2001, 53% of apparel products were manufactured by domestic contractors from raw material provided by QuikSilver. 89% of raw materials provided to the domestic contractors were made in the United States. No single fabric supplier accounted for more than approximately 8% of the Company's consolidated expenditures for raw material purchases. There are no long-term relationships with suppliers.
- 47% of apparel products were imported as finished goods from foreign countries: primarily from China, Vietnam, North Africa and Portugal.
- The Company manufactured all of its snowboards in company-owned factories in the United States.

In-House Expertise

- At the end of fiscal 1997, the Company acquired certain assets from two domestic cutting contractors. Since then, all cutting for the domestic subcontractors has been done in-house.
- Quality control is also kept in-house.

Buyer Power

- During fiscal 2001, no single contractor accounted for more than 6% of the Company's consolidated production. The Company reports that numerous qualified contractors are available in the short run to provide additional capacity, should this be needed.

Employees

- The Company reports that it employs approximately 1,950 persons, including approximately 1,180 in production, operations and shipping functions, approximately 730 in sales, administrative or clerical capacities, and approximately 40 in executive capacities.

Unions

- None of the Company's domestic employees are represented by a union, and less than 10% of its European employees are represented by a union. The Company has never experienced a work stoppage and considers its working relationships with its employees to be good.

Trade Quotas

- The Company imports finished goods and raw materials under multilateral and bilateral trade agreements between the United States and a number of foreign countries, including Hong Kong, India, China and Japan. These agreements impose quotas on the amount and type of textile and apparel products that can be imported into the United States from the affected countries. The Company does not anticipate that these restrictions will materially or adversely affect its operations since it would be able to meet its needs domestically or from countries not affected by the restrictions on an annual basis.
- Quiksilver Europe operates in the European Union, within which there are few trade barriers. Quiksilver Europe also sells to six other countries belonging to a trade union, which has some restrictions on imports of textile products and their sources. The Company does not anticipate that these restrictions will materially or adversely impact its operations since it has always operated under such constraints and the trend in Europe is continuing toward unification.

Properties & Stores

- The Company's executive offices, merchandising and design, production and warehouse facilities occupy multiple buildings located in Huntington Beach, California, France, and two facilities in the state of Washington. The Company also maintains a sales office in New York and an Australian office in Avalon, New South Wales. The aggregate monthly rental payment for rented facilities is approximately $900,000. The Company believes that its present facilities will be adequate for its immediately foreseeable business needs.
- As mentioned in the revenue section of this report, the Company also own retail space for direct sales through it "Boardriders Club" Stores. In late September, QuikSilver announced the purchase of a store in the heart of Times Square, Manhattan, estimated to be the highest customer foot traffic in the world. In accordance with its Champs-Elysees stores in France which

produce in excess of $1000 per square foot, the Times Square store should also do the same and would be very profitable at this level. The new store will be 3,000 square feet.

- With the purchase of "Beech Street," the past owner-operator of the QuikSilver Outlet Stores, in 2002 for $7.5M QuikSilver will own the entire distribution channel of 26 outlet stores.

Quiksilver, Inc. **Retail Concepts**

	1Q02 (Jan)		2Q02 (Apr)		3Q02 (Jul)		
	Total		Total		Total		
Store Concept	Company-owned	Licensed	Company-owned	Licensed	Company-owned	Licensed	
Boardriders Clubs	36	89	41	93	42	95	
Roxy Stores	4	9	4	11	4	11	
Multibrand Stores	0	2	0	2	0	2	
Gotcha Stores	2	1	2	1	2	1	
Hawk Store	2	0	3	0	3	0	
Youth Store	0	1	2	1	2	2	
Outlet Stores	5	26	5	26	5	26	*
	49	128	57	134	58	137	
licensed territories		98		108		114	
Total	49	226	57	242	58	251	

* Acquired by Quiksilver as per 9/23 announcement.

Source: CIBC World Markets Corp. and company data

Royalties

- The Company has historically received royalties from its watch, sunglass, Mexican and outlet store licensees. These licensees do business in many countries and territories around the world, with headquarters in Australia, Japan, Turkey, South Africa, Brazil, Indonesia, South Korea, Argentina, Chile and Mauritius. As a result, royalty income totaled $5,169,000 in fiscal 2001, up from the fiscal 2000 figure of $3,681,000.
- Much of this income, however, was offset by the royalty expense. In fiscal 2001, Royalty income exceeded royalty expense by $232,000, but the opposite was true in the previous year when royalty expense exceeded royalty income by $3,143,000. This improvement resulted from the Quiksilver International acquisition.

Interest and Tax

- Interest expense in fiscal 2001 increased 69.0% to $10,873,000 from $6,435,000 in the previous year. Of that increase, Expense

approximately $2,200,000 was related to debt resulting from the Quiksilver International acquisition. The rest of the increase came primarily from additional borrowings to provide working capital to support the Company's growth and to continued investments in retail stores.

- The Company's income tax rate for fiscal 2001 decreased to 38.3% from 38.6% in fiscal 2000. This reduction resulted primarily because a higher percentage of the Company's profits were generated in countries with lower tax rates.

Leaving others in the surf, branding is 5% of sales

- Branding and Advertising play a critical role in the Company's success, enabling a pricing premium and sales growth. The brand is built around a strategy of promoting its core image of surfing and other boardriding activities. The Company advertises in magazines such as Maxim, Surfer, Surfing, Skateboard and Transworld Snowboarding in the United States and Wind, Snowboard and Surf Session in Europe. The ad campaign also includes national publications in the United States, such as Spin, Seventeen and Teen People, and mainstream publications in various European countries such as L'Equipe, GQ, Viajes N.G. and Focus.
- The Company also participates in trade shows, which are held throughout the United States and Europe.
- In addition to print media, the Company's core marketing includes surf, snowboard and skateboard contests in the markets where it distributes product. The Company also sponsors an international team of prominent athletes to produce promotional movies and videos featuring athletes wearing and/or using Quiksilver products.
- Co-branding arrangements with independent companies are also used to promote the Company's brands. For example, Peugeot and Toyota produce cars branded with Quiksilver and Roxy, and the Tony Hawk Pro Skater 3 video game is cross-promoted by both the Company and Activision.
- Because of the better than expected results and the strength of the fall and holiday product assortment, Quiksilver increased its domestic advertising spending for the second half of the year (announced on the second-quarter conference call) by $1.5 million, to be spent on a national magazine print campaign for Quiksilver.
- Management reports that Quiksilver will continue to get more aggressive in its domestic marketing, with ads in national magazines. We believe this will enhance the visibility of the brand.
- Advertising as a percentage of sales will be 5% at the end of

2002.

Valuation

We evaluated Quiksilver's equity value using two methods:

1) Comparable Companies
2) Discounted Cash Flows Available to Equity Holders

Comparables

- Quiksilver seems pricey with respect to earnings, but very much in line when considering cash flows.
- As a fast grower, we would expect Quiksilver to fetch a higher multiple to earnings than its slower growing counterparts in our coverage universe.
- Our target price of $31 is only 18 times consensus 2003 earnings estimates of $1.75/share, which we think is cheap given the near-term growth potential of the company.

Company	Price/ Earnings	Price/ Book	Price/ Sales (ttm)	Price/ Cash Flow (ttm)
Quiksilver	22	2.3	0.9	13.8
Coverage Universe Median	15	2.3	0.9	13.3
Columbia Sporstwear	17.5	3.7	2.0	16.6
Liz Claiborne	15	2.7	0.9	10.2
Jones Apparel Group	15	1.9	1.1	13.3
Polo Ralph Lauren	14	2.0	0.9	9.3
Tommy Hilfiger	5	0.6	0.4	2.8
VF Corporation	24	2.4	0.8	24.0

Source: Multex, Marketguide

Discounted Cash Flow

WACC

- We discounted Cash Flows using the WACC. Net Debt as a percentage of Firm Value has remained relatively constant over the past few years, so the WACC approach appears reasonable.
- A range of market risk premiums was used to generate multiple WACCs in order to simulate varying assumptions/preferences used by investors in the market.

Assumptions for WACC/DCF

Beta	1.12
Mkt. Value Equity	569,000,000
Equity Proportion	88%
Mkt. Value of Debt	74,564,740
Debt Proportion	12%
Firm Value	643,564,740
Avg. Cost of Debt	8%
Shares Outstanding	24,365,000

WACCs for given Market Risk Premium

Market Risk Premium	WACC
4.5%	8.6%
5.5%	9.6%
6.5%	10.6%
7.5%	11.5%
8.5%	12.5%
9.5%	13.5%

Equity Value Per Share

- By discounting firm values using the range of WACCs and subtracting the value of debt, we produced an array of possible equity values.
- In the table below, we averaged the equity values for each of our growth scenarios (Worst, Best, Base) and also averaged the column values across all of the cases for different terminal growth rates.
- We see that the Base case returns an equity value that is better than 20% higher than the current stock price, and the Worst case is less than 20% off the current stock price.
- The column result for terminal growth equaling 4%, which is the long-run growth rate for the sector, returns a value that is also better than 20% higher than the current stock price. We think the market may not have properly taken into account the sustainable upside potential of Quiksilver, and thus we feel that the aggressive terminal growth rate is warranted.
- We arrived at a target price of $31 for the stock, which is more than 20% higher than the current trading price.
- We have included detailed assumptions about how free cash flows to the firm were derived later in the report.

NPV of Discounted Cash Flows to Equity given Growth Assumptions and WACC

		Terminal Growth Rate			
Case	**WACC**	**2%**	**3%**	**4%**	**5%**
Worst	13.5%	12.20	13.81	15.76	N/A
Avg. 20.38	12.5%	13.63	15.56	17.94	N/A
	11.5%	15.36	17.72	20.70	N/A
	10.6%	17.49	20.44	24.29	N/A
	9.6%	20.18	23.99	29.16	N/A
	8.6%	23.69	28.79	36.14	N/A
Best	13.5%	19.97	21.99	24.42	27.43
Avg. 33.39	12.5%	21.89	24.30	27.27	31.04
	11.5%	24.18	27.12	30.84	35.70
	10.6%	26.97	30.65	35.46	41.99
	9.6%	30.47	35.22	41.68	50.96
	8.6%	34.99	41.37	50.53	64.83
Base	13.5%	18.85	20.72	22.98	25.77
Avg. 31.34	12.5%	20.64	22.88	25.64	29.13
	11.5%	22.78	25.51	28.97	33.48
	10.6%	25.39	28.81	33.27	39.33
	9.6%	28.65	33.06	39.05	47.67
	8.6%	32.86	38.78	47.29	60.56
		22.79	**26.15**	**30.63**	**40.66**

Calculation of Free Cash Flow to the Firm Over a Five-Year Horizon

Assumptions:

- Each free cash flow case (Base, Best, Worst) refers to Pro Forma calculations of Net Income, which are each included in subsequent tables.
- CAPEX ramps down from current level of 4% of sales to 3% of sales over the 5-year horizon. As the company achieves density in its target markets, we believe less investment will be required in PP&E. International growth will come more slowly than in the U.S.
- Working Capital levels remain constant at 25% of sales. This is a conservative assumption as the company will likely become more efficient with operations as it matures.

BASE CASE	Y1	Y2	Y3	Y4	Y5
NET INCOME	47,250	51,975	54,573	56,756	58,459
POST TAX INT	6,092	6,701	7,036	7,318	7,537
NOPAT	53,342	58,676	61,609	64,074	65,996
DELTA WC	26,465	20,290	11,159	9,374	7,312
CAPEX	32,464	33,478	32,809	31,684	30,124
DEPRECIATION	16,232	17,855	18,748	19,498	20,083

FREE CASH	10,644	22,762	36,389	42,514	48,643

BEST CASE	Y1	Y2	Y3	Y4	Y5
NET INCOME	47,250	52,920	57,682	61,143	62,978
POST TAX INT	6,092	6,823	7,437	7,883	8,120
NOPAT	53,342	59,743	65,119	69,026	71,097
DELTA WC	26,465	24,348	20,452	14,862	7,877
CAPEX	32,464	34,087	34,678	34,133	32,453
DEPRECIATION	16,232	18,180	19,816	21,005	21,635
FREE CASH	10,644	19,487	29,805	41,036	52,403

WORST CASE	Y1	Y2	Y3	Y4	Y5
NET INCOME	43,552	45,729	47,559	48,985	50,455
POST TAX INT	5,615	5,896	6,132	6,316	6,505
NOPAT	49,167	51,625	53,690	55,301	56,960
DELTA WC	10,586	9,351	7,855	6,127	6,311
CAPEX	29,923	29,456	28,592	27,346	26,000
DEPRECIATION	14,962	15,710	16,338	16,828	17,333
FREE CASH	23,619	28,528	33,582	38,657	41,983

Source: Yale SOM Team Estimates

Pro Forma Income Statements Over a Five-Year Horizon

Assumptions:

- We assume that expenses will remain constant as a percentage of sales. Common size expense levels can be found in the subsequent income statement table under the column for current fiscal year (ending 10/31/2002).
- For the Base and Best Cases, we assume that sales will continue to grow at the 5-year CAGR of 15% in the first year, and then growth rates will decline towards the long-term range.
- In the Worst Case, sales in the upcoming year do not reach the 5-year CAGR of 15%, and sales then taper off towards the long-term range. See the Sales Growth Factor in the bottom row for each case.

BASE CASE	Fiscal Years Ending					
	10/31/02E	10/31/03E	10/31/04E	10/31/05E	10/31/06E	10/31/07E
NET SALES	705,737	811,598	892,757	937,395	974,891	1,004,138
COST OF GOODS	428,554	486,959	535,654	562,437	584,935	602,483
GROSS PROFIT	277,183	324,639	357,103	374,958	389,956	401,655
SG&A	212,587	243,479	267,827	281,219	292,467	301,241
OPERATING INCOME	64,596	81,160	89,276	93,740	97,489	100,414
OTHER INCOME/EXPENSE	3,770	4,058	4,464	4,687	4,874	5,021
EBIT	68,366	85,218	93,740	98,426	102,364	105,434
INTEREST EXPENSE	9,154	9,739	10,713	11,249	11,699	12,050

EBT	59,212	75,479	83,026	87,178	90,665	93,385
TAXES	22,174	303,537	333,891	350,586	364,609	375,548
NET INCOME	37,038	47,250	51,975	54,573	56,756	58,459
Sales Growth Factor		1.15	1.1	1.05	1.05	1.05

BEST CASE			Fiscal Years Ending			
	10/31/02E	10/31/03E	10/31/04E	10/31/05E	10/31/06E	10/31/07E
NET SALES	705,737	811,598	908,989	990,798	1,050,246	1,081,754
COST OF GOODS	428,554	486,959	545,394	594,479	630,148	649,052
GROSS PROFIT	277,183	324,639	363,596	396,319	420,098	432,701
SG&A	212,587	243,479	272,697	297,239	315,074	324,526
OPERATING INCOME	64,596	81,160	90,899	99,080	105,025	108,175
OTHER INCOME/EXPENSE	3,770	4,058	4,545	4,954	5,251	5,409
EBIT	68,366	85,218	95,444	104,034	110,276	113,584
INTEREST EXPENSE	9,154	9,739	10,908	11,890	12,603	12,981
EBT	59,212	75,479	84,536	92,144	97,673	100,603
TAXES	22,174	303,537	339,962	370,559	392,792	404,576
NET INCOME	37,038	47,250	52,920	57,682	61,143	62,978
Sales Growth Factor		1.15	1.12	1.09	1.06	1.05

WORST CASE			Fiscal Years Ending			
	10/31/02E	10/31/03E	10/31/04E	10/31/05E	10/31/06E	10/31/07E
NET SALES	705,737	748,081	785,485	816,905	841,412	866,654
COST OF GOODS	428,554	448,849	471,291	490,143	504,847	519,993
GROSS PROFIT	277,183	299,232	314,194	326,762	336,565	346,662
SG&A	212,587	224,424	235,646	245,071	252,424	259,996
OPERATING INCOME	64,596	74,808	78,549	81,690	84,141	86,665
OTHER INCOME/EXPENSE	3,770	3,740	3,927	4,085	4,207	4,333
EBIT	68,366	78,549	82,476	85,775	88,348	90,999
INTEREST EXPENSE	9,154	8,977	9,426	9,803	10,097	10,400
EBT	59,212	69,572	73,050	75,972	78,251	80,599
TAXES	22,174	279,782	293,771	305,522	314,688	324,129
NET INCOME	37,038	43,552	45,729	47,559	48,985	50,455
		Y1	Y2	Y3	Y4	Y5
Sales Growth Factor (Bad)		1.06	1.05	1.04	1.04	1.04

Source: Yale SOM Team Estimates

Statements of Income – Actual and Estimated – 1992 through Current FY

ANNUAL INCOME (000s)	Current FY	Quarters Ending				Fiscal Years Ending									
	10/31/2002E	10/31/02E	7/31/02	4/30/02	1/31/02	10/31/01	10/31/00	10/31/99	10/31/98	10/31/97	10/31/96	10/31/95	10/31/94	10/31/93	10/31/92
NET SALES	705,737	200,000	173,962	185,969	145,806	615,452	515,689	443,734	316,115	231,783	193,474	172,787	126,171	94,640	89,319
COST OF GOODS	428,554	120,000	104,691	111,684	92,179	382,762	315,900	268,184	189,399	141,487	117,380	106,741	78,560	60,987	60,071
GROSS PROFIT	277,183	80,000	69,271	74,285	53,627	232,690	199,789	175,550	126,716	90,296	76,094	66,046	47,611	33,653	29,248
SELL GEN & ADMIN EXP	212,587	60,000	53,835	51,569	47,183	181,220	142,888	124,479	91,508	65,424	54,379	46,810	35,014	25,684	26,390
OPERATING INCOME	64,596	20,000	15,436	22,716	6,444	51,470	56,901	51,071	35,208	24,872	21,715	19,236	12,597	7,969	2,858
OTHER INCOME/EXPENSE	3,770	1,000	740	1,043	987	4,815	1,396	-2,728	-1,706	-1,771	-1,651	-1,250	-98	-62	-1,425
EBIT	68,366	21,000	16,176	23,759	7,431	56,285	58,297	48,343	33,502	23,101	20,064	17,986	12,499	7,907	1,433
INTEREST EXPENSE	9,154	2,400	2,039	2,287	2,428	10,873	6,435	3,476	2,734	1,818	785	1,150	743	276	543
EBT	59,212	18,600	14,137	21,472	5,003	45,412	51,862	44,867	30,768	21,283	19,279	16,836	11,756	7,631	890
TAXES	22,174	6,956	5,292	8,009	1,917	17,391	20,026	18,283	12,805	8,639	7,619	6,824	4,618	3,200	519
NET INCOME	37,038	11,644	8,845	13,463	3,086	28,021	31,836	26,584	17,963	12,644	11,660	10,012	7,738	4,431	371
OUTSTANDING SHARES	24,365	24,365	24,365	24,165	23,956	23,890	23,234	22,731	14,552	14,279	6,835	6,776	6,521	6,415	6,364

	Current FY	Quarters Ending				Fiscal Years Ending									
COMMON SIZE INCOME	10/31/2002E	10/31/02E	7/31/02	4/30/02	1/31/02	10/31/01	10/31/00	10/31/99	10/31/98	10/31/97	10/31/96	10/31/95	10/31/94	10/31/93	10/31/92
NET SALES	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%
COST OF GOODS	60.7%	60%	60.2%	60.1%	63.2%	62.2%	61.3%	60.4%	59.9%	61.0%	60.7%	61.8%	62.3%	64.4%	67.3%
GROSS PROFIT	39.3%	40%	39.8%	39.9%	36.8%	37.8%	38.7%	39.6%	40.1%	39.0%	39.3%	38.2%	37.7%	35.6%	32.7%
SELL GEN & ADMIN EXP	30.1%	30%	30.9%	27.7%	32.4%	29.4%	27.7%	28.1%	28.9%	28.2%	28.1%	27.1%	27.8%	27.1%	29.5%
OPERATING INCOME	9.2%	10%	8.9%	12.2%	4.4%	8.4%	11.0%	11.5%	11.1%	10.7%	11.2%	11.1%	10.0%	8.4%	3.2%
OTHER INCOME/EXPENSE	0.5%	0.5%	0.4%	0.6%	0.7%	0.8%	0.3%	-0.6%	-0.5%	-0.8%	-0.9%	-0.7%	-0.1%	-0.1%	-1.6%
EBIT	9.7%	10.5%	9.3%	12.8%	5.1%	9.1%	11.3%	10.9%	10.6%	10.0%	10.4%	10.4%	9.9%	8.4%	1.6%
INTEREST EXPENSE	1.3%	1.2%	1.2%	1.2%	1.7%	1.8%	1.2%	0.8%	0.9%	0.8%	0.4%	0.7%	0.6%	0.3%	0.6%
EBT	8.4%	9.3%	8.1%	11.5%	3.4%	7.4%	10.1%	10.1%	9.7%	9.2%	10.0%	9.7%	9.3%	8.1%	1.0%
TAX RATE	37.4%	37.4%	37.4%	37.3%	38.3%	38.3%	38.6%	40.7%	41.6%	40.6%	39.5%	40.5%	39.3%	41.9%	0.6%
NET INCOME	5.2%	5.8%	5.1%	7.2%	2.1%	4.6%	6.2%	6.0%	5.7%	5.5%	6.0%	5.8%	6.1%	4.7%	0.4%
ANNUAL YOY SALES GROWTH	15%					19%	16%	40%	36%	20%	12%	37%	33%	6%	
CAPEX (ANNUAL)	27,000					22,622	16,420	23,900							
CAPEX/SALES	0.04					0.04	0.03	0.05							
5-Yr Sales Growth	15%														

BALANCE SHEET – EOY 1992 through MRQ

ASSETS (000s)

FY/FQ ENDING	7/31/2002	4/30/2002	1/31/2002	10/31/2001	10/31/2000	10/31/1999	10/31/1998	10/31/1997	10/31/1996	10/31/1995	10/31/1994	10/31/1993	10/31/1992
CASH	26,195	6,916	14,958	5,002	2,298	1,449	3,029	4,103	3,429	3,461	682	3,386	4,613
RECEIVABLES	165,675	171,669	145,021	155,879	136,394	107,619	78,390	54,668	44,554	38,308	29,974	19,315	16,560
INVENTORIES	93,316	76,313	116,364	107,562	90,034	72,207	70,575	48,372	35,668	28,355	21,609	13,599	11,703
OTHER CURRENT ASSETS	25,262	21,965	21,877	19,806	14,647	11,899	8,070	4,614	4,209	3,711	3,385	1,976	1,565
TOTAL CURRENT ASSETS	310,448	276,863	298,220	288,249	243,373	193,174	160,064	111,757	87,860	73,835	55,650	38,276	34,441
NET PROP & EQUIP	67,881	64,580	61,600	61,453	49,834	45,153	31,996	16,436	9,655	7,032	6,133	4,901	5,293
DEFERRED CHARGES	NA	NA	NA	1,837	789	401	264	569	732	660	449	NA	NA
INTANGIBLES	70,310	64,759	64,658	64,840	62,528	18,448	18,970	19,919	16,537	17,293	18,042	14,672	13,275
DEPOSITS & OTH ASSET	4,856	4,593	4,742	2,359	2,218	2,497	1,777	969	796	348	196	799	153
TOTAL ASSETS	453,495	410,795	429,220	418,738	358,742	259,673	213,071	149,650	115,580	99,168	80,470	58,648	53,162
OP WORKING CAPITAL	186,416	172,468	153,271	156,569	128,957	113,438	95,614	68,767	55,887	47,135	32,957	28,232	24,744
OP WORK CAP (% ANNUAL SALES)				25%	25%	26%	30%	30%	29%	27%	26%	30%	28%

LIABILITIES (000S)

FY/FQ ENDING	7/31/2002	4/30/2002	1/31/2002	10/31/2001	10/31/2000	10/31/1999	10/31/1998	10/31/1997	10/31/1996	10/31/1995	10/31/1994	10/31/1993	10/31/1992
NOTES PAYABLE	43,571	46,201	66,690	66,228	49,203	28,619	17,465	18,671	8,211	8,031	10,100	NA	NA
ACCOUNTS PAYABLE	46,600	29,356	48,379	40,554	40,642	31,325	26,340	13,079	12,823	9,257	5,157	4,116	2,239
CUR LONG TERM DEBT	30,996	24,810	24,453	24,153	9,428	3,615	3,293	1,474	240	233	390	1,495	199
ACCRUED EXPENSES	33,861	24,653	29,880	24,898	22,568	19,792	17,269	10,725	10,212	8,834	5,024	4,340	7,450
INCOME TAXES	NA	4,185	NA	NA	2,003	NA	3,376	515	727	578	2,412	1,588	8
TOTAL CURRENT LIAB	155,028	129,205	169,402	155,833	123,844	83,351	67,743	44,464	32,213	26,933	23,083	11,539	9,896
LONG TERM DEBT	43,074	44,187	42,872	46,311	57,284	24,569	27,669	10,178	2,640	3,297	2,449	2,079	2,479
TOTAL LIABILITIES	198,102	173,392	212,274	202,144	181,128	107,920	95,412	54,642	34,853	30,230	25,532	13,618	12,375
COMMON STOCK NET	243	242	239	239	232	227	146	143	70	68	65	64	64
CAPITAL SURPLUS	59,706	56,458	53,281	52,706	42,833	36,780	25,920	22,585	18,971	15,118	11,551	10,364	9,990
RETAINED EARNINGS	206,841	197,996	184,533	181,447	153,426	121,590	95,006	77,043	64,399	52,739	42,727	34,989	30,558
TREASURY STOCK	6,778	6,778	6,778	6,778	6,778	3,054	3,054	3,054	3,054	NA	NA	NA	NA
OTHER EQUITIES	-4,619	-10,515	-14,329	-11,020	-12,099	-3,790	-359	-1,709	341	1,013	595	-387	175
SHAREHOLDER EQUITY	255,393	237,403	216,946	216,594	177,614	151,753	117,659	95,008	80,727	68,938	54,938	45,030	40,787
TOT LIAB & NET WORTH	453,495	410,795	429,220	418,738	358,742	259,673	213,071	149,650	115,580	99,168	80,470	58,648	53,162
NET DEBT FOR WACC	74,565												

Statements of Cash Flow – 1997 to 2001

CASH FLOW PROVIDED BY OPERATING ACTIVITY (000s)	FISCAL YEAR ENDING 10/31/2001	10/31/2000	10/31/1999	10/31/1998	10/31/1997
Net Income (Loss)	28,021	31,836	26,584	17,963	12,644
Depreciation/Amortization	13,877	10,023	7,671	5,621	3,715
Net Incr (Decr) Assets/Liabs	-39,575	-49,185	-30,576	-26,329	-26,319
Other Adjustments, Net	3,524	3,226	966	1,655	2,935
Net Cash Prov (Used) by Oper	5,847	-4,100	4,645	-1,090	-7,025
Depreciation/Amortization (as % of Sales)	2%	2%	2%	2%	2%

CASH FLOW PROVIDED BY INVESTING ACTIVITY (000s)	FISCAL YEAR ENDING 10/31/2001	10/31/2000	10/31/1999	10/31/1998	10/31/1997
(Incr) Decr in Prop, Plant	-22,540	-16,418	-23,601	-19,414	-10,230
(Acq) Disp of Subs, Business	-250	-24,409	NA	-500	-1,900
Net Cash Prov (Used) by Investing	-22,790	-40,827	-23,601	-19,914	-12,130

CASH FLOW PROVIDED BY FINANCING ACTIVITY (000s)	FISCAL YEAR ENDING 10/31/2001	10/31/2000	10/31/1999	10/31/1998	10/31/1997
Issue (Purchase) of Equity	6,102	583	7,583	2,606	2,818
Incr (Decr) In Borrowing	13,781	45,039	10,066	17,371	17,169
Net Cash Prov (Used) by Financing	19,883	45,622	17,649	19,977	19,987
Effect of Exchg Rate On Cash	-236	154	-273	-47	-158
Net Change in Cash or Equiv	2,704	849	-1,580	-1,074	674
Cash or Equiv at Year Start	2,298	1,449	3,029	4,103	3,429
Cash or Equiv at Year End	5,002	2,298	1,449	3,029	4,103

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