Initiating Coverage:

Advanced Drainage Systems

Rebound not a Pipe Dream

Key Take-away: Strong performance for tanks and advanced treatment products in the infiltrator division buoyed recent earnings but ultimately were not enough to hide poor performance in non-residential markets, leading to a 2.3% decrease in Net Income per Diluted Share. Regardless, we maintain a positive outlook on the stock, under the guise that the residential market is currently experiencing a prolonged cyclical downswing poised to revert soon and that the Infiltrator and Allied Products divisions will be beneficiaries of climate change induced events.

Valuation: We initiate coverage with a $150.00 PT.

Company Description: Advanced Drainage Systems is the nationwide leader in the production of HDPE (High Density Polyethylene Piping). They also acquired Infiltrator Technologies in 2019, a leader in the onsite wastewater treatment solutions, mostly providing septic tanks. They have three main divisions: Pipes, Infiltrator, and Allied Products. Combined with their fourth division, International, representing their small presence in Canada and Mexico, ADS provide a comprehensive suite of water solutions to any build site or municipality.

Investment Theses

Water Management Market is Overlooked Climate Play: While EVs and solar may be the stocks traditionally packaged in a green ETF, wastewater management will take on the legitimate burden of keeping residential and non-residential areas alike safe from flooding and other water damage. With a 6.5% CAGR, the market is more than accommodative to ADS's growth story, and this will play out with its key driver being municipal spend. This will be through more dollars allocated to the drainage of parks, intersections, transit stops, and more. With a lot of infrastructure potential priced out following Trump's victory, a window has opened to buy on the thesis that municipalities will be forced to spend, whether federally or not, as catastrophes worsen, and options dwindle.

Short Term cyclical rebound of Residential End market in View: $WMS, with a 1.41 unlevered, unadjusted beta is market sensitive both due to its nature as an industrial player and its exposure to the residential end market. Its products are often chosen during the housing construction process, thus making it a stock dependent on the new residential starts indicator. That number has shown some weakness for quite some time, and the 82 bp rise in the US 30 Yr Mortgage since the first Fed cut in September has only weighed on the stock. However, the potential remains that the promises made by the incoming administration regarding slashing federal housing regulation and opening up reserved land are realized, which would put positive pressure on the starts number.

CONSORTIUM EQUITY RESEARCH

Consortium Equity Research
Industrials | Construction Materials
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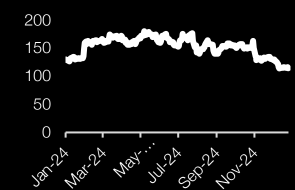
Stock Rating:	Overweight
Price Target:	$150.00
Price:	$115.02
Potential Upside/Downside:	30.4%
Ticker(s):	$WMS
Market Cap:	$8.92b
Shares Outstanding:	77.54mm
Free Float (%):	73.91%
Dividend Yield:	0.56%

1 Year History



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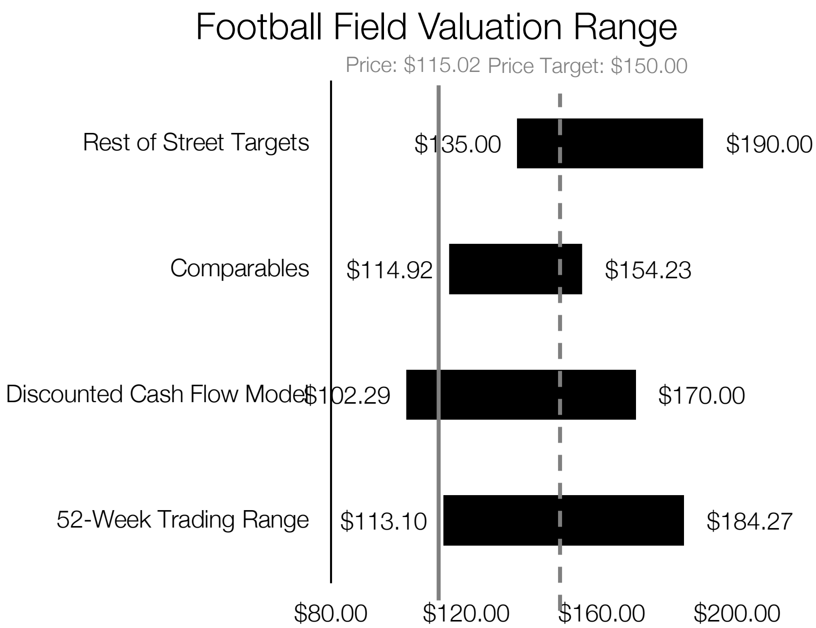
Price Target & Valuation

Our analysis gives ($WMS) a price target of $150.00 and an overweight weight rating.



Potential Downsides to Our Rating

Downside 1 - Interest Rate Exposure:
The stock is only so tied to its fundamental operating ability and assets before it trades purely on interest rates, both short and long, leaving risk if unhedged in a portfolio.

Downside 2 - Administration Challenges:
The main negative catalyst would be a repeal/claw back of money disbursed by the Infrastructure and Jobs Investment Act, vital to ADS.

Catalyst 1 - Potential Trade War:
A trade war, while bearish for the market, would likely lead to ADS outperformance, given its low exposure to foreign inputs, labor, and end markets.

Catalyst 2 - Continued Strong Hurricane Seasons in Southeast:
Storms are a negative short term pressure, as they pause construction activity, but they elevate the need for water management.

Catalyst 3 - Sea Level Rise:
Sea level rise will continue to buoy the need for the Infiltrator division, as septic tanks are disproportionately located in exposed areas, needing servicing and repairs, which justifies the recent Orenco acquisition and its advanced onsite treatment services.

Our Price Target: $150.00

Our PT is based on a 7.5% Pipe and 6.0% Allied Product growth number for ’30 and a 26% EBIT% on a 14.5x EV/EBIT exit multiple, supporting both ends of our thesis

Our Upside Case: $170.00

Our upside case is based on an 8.0% Pipe and 8.0% Allied Product growth number for ’30 and a 27% EBIT%. To support an enhanced realization of our long term thesis, we model a 7.0% infiltrator growth with a 15.5x EV/EBIT multiple.

Our Downside Case: $100.00

Our downside case is based on modest 6.5%, 3.0%, 3.5%, and 4.0% divisional growth numbers, but we project greater downside comes from production weakness, pricing power loss, and a weakened terminal value, hence a 22% EBIT% and a 12.0x EV/EBIT multiple.