

## **Summary**

- I am placing a BUY recommendation on Baldwin Technology Company with a 12- month price target of \$6.34.
- Baldwin is the market leader in the offset print cleaning equipment market and will solidify its market position due to the recently acquired Oxy-Dry and Hildebrand Systeme GmbH.
- The company is in the process to successfully integrate and consolidate Oxy-Dry and Hildebrand Systeme GmbH. The restructuring plan will lead to estimated cost savings of \$3.7 million.
- Baldwin's strong sales presence in Asia will enable the company to address that rapidly growing market and the high demand for brush cleaning systems.
- Baldwin's sales will continue to profit from the weak dollar

## **Financial Situation and Prospects**

Baldwin's net sales for FY07 increased by 12,3%, or \$22 million to \$201.5 million, compared to \$179 million in FY06. A big portion of this sales increase is due to the stronger offshore currencies, like the euro, yen and the Swedish krona.

The company reported a net income of \$6.6 million compared to 6.3 million in 2006. The partial release of Baldwin's deferred tax asset valuation allowance of 2.5, which had a favourable impact on the tax provision, was included in the company's net income. Without the allowance, the company's net income would have been \$4.1 million. Baldwin states, that it released a portion of the valuation allowance "due to the sustained and projected profitability of its domestic operations".

For the fourth quarter of 2007, Baldwin's net sales rose 20%, or \$9.4 million, to 56.9 million, compared to \$47.5 in the fourth quarter 2006. Again, currency exchange rates had a favourable impact of about \$1.2 million on the company's net sales. Baldwin's net income rose from \$1.9 million a year earlier, to \$3.6 in the fourth quarter of 2007. Without the allowance of \$2.5 million, Baldwin's net income would have been \$1.1 million.

However, the respectable sales increase for the fourth quarter of 2007 can primarily be attributed to the sales from the acquired businesses Hildebrand Systeme GmbH and Oxy-Dry. While an estimated \$10.1 million in net sales were generated by the new businesses, Baldwin's net sales alone decreased by \$700 000.

Compared to the fourth quarter 2006, orders went up by 6%, to \$45.6, in 2007. Year to date, orders went up by 9% to \$196 million, compared to the prior period's \$180.4 million.

Baldwin's gross profit margin for the year were 32.6%. Before the acquisitions, Baldwin had an average of 34.6% in gross profit over the past two years. However, once the acquisitions are completely integrated and consolidated, gross margin improvements can be expected.

Since the end of the previous fiscal year cash & equivalents increased by \$2.4 millions to \$17.37 million, inventories, which can be attributed to Baldwin's acquisitions, rose by \$7.7 million to \$30.4 million. Baldwin's net cash position, which is cash & equivalents minus long- and short term debt, has currently a deficit of \$15.3 million, due to the recent acquisitions expenses.

After the acquisition of Hildebrand Systeme GmbH this year, Baldwin announced a restructuring plan. The company estimates the initial total costs of implementing the restructuring and integration plan at \$4.6, but expects annual savings of about \$3.7 million.

I predict, a successful integration and consolidation of the recently acquired companies, Oxy-Dry and Hildebrand Systeme GmbH, and concurrently strengthening offshore currencies until the third quarter 2008, will significantly increase Baldwin's net income over the next year.

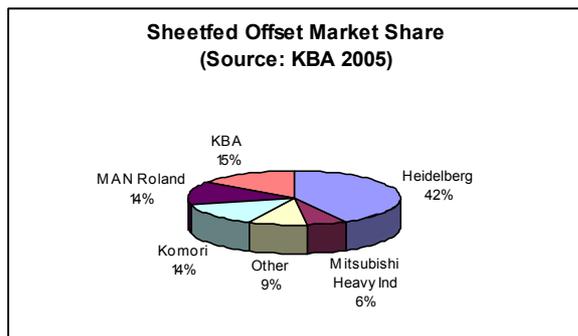
## **Industry and Competitive Analysis**

Baldwin Technology Company, Inc. engages primarily in the development and manufacturing of printing press accessories and control equipment.

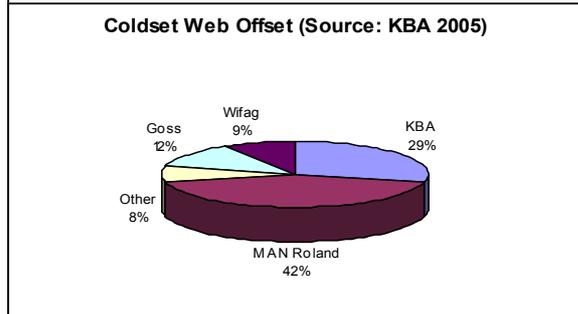
There are three different stages in the printing process: prepress, on-press, and postpress. Baldwin's production line is focused on the actual printing operation, the on-press stage. It offers press cleaning-, fluid management-, web protection-, and ink control systems. The Company's products are designed to improve the printing process in terms of quality, the environment, safety, productivity and reduction of waste.

According to KBA(Koenig und Bauer AG), newspaper markets in North America and Europe are going to stagnate or shrink. As the need for information increases in line with economic power and prosperity, the demand in Brazil, India and China is increasing. In 2005, China and Brazil had a growth rate of 15.9% and 27.3%, respectively.

Currently, 60% of the print market is dominated by German companies. Japan and UK take a 11.8% and 7% share, respectively(KBA 2007). The total print market is estimated at €9(\$13.23) billion, excluding toner- based technologies, digital print and office print. The biggest share, with a volume of €5(\$7.35) billion, takes the sheetfed offset process, which prints on individual sheets of paper.

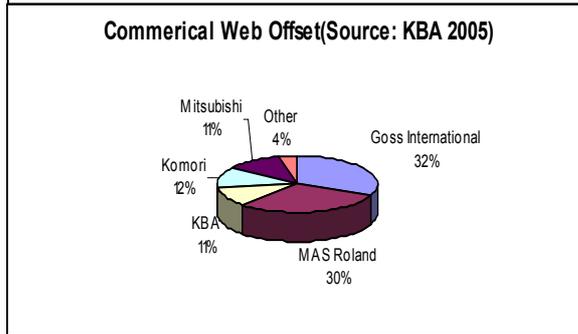


Heidelberger Druckmaschinen AG dominates the market, followed by KBA, MAN Roland, Komori Corporation and Mitsubishi Heavy Industries.

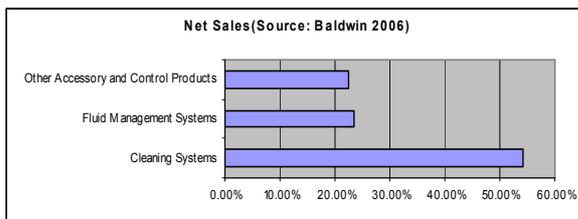


The coldset web offset process takes the second biggest share, with a market volume of €1.1(\$1.62) billion. The coldset web offset process is utilized in the newspaper industry and feeds a continuous role of paper through the printing press. MAN is the market leader in this segment, followed by KBA, Goss and Wifag.

The third major share on the printing market takes the heatset, or commercial web offset process. In the heatset process the ink is dried rapidly by forced air heating. Goss International and MAS Roland are dominating this market.



All the major companies in these three different market segments use Baldwin's components. KBA, with approx. 17% and Mitsubishi heavy industries, with approx. 10% are Baldwin's major customers.



In 2006, cleaning systems were the main contributor to sales, followed by fluid management systems.

In November 2006, Baldwin, which is the world leader in cleaning systems, acquired Oxy-Dry, ranked second in this segment. While Baldwin's system is based on cloth, Oxy-Dry uses a brush solution. In April 2007 Baldwin acquired Hildebrand

Systeme GmbH, another competitor in the web and sheet cleaning segment.

These acquisitions should substantially increase its market power in the U.S. and Europe. Baldwin's already strong sales presence in Asia will enable the company to address that rapidly growing market and the high demand for brush cleaning systems.

In response to Baldwin's Oxy-Dry coup, its biggest rival, Technotrans AG, acquired Rotoclean GmbH, another leading manufacturer of brush cleaning systems for web presses. With this technology, Technotrans seeks to complement its existing cloth cleaning system and hopes to strengthen its position in the global market. However, in 2006, only €10(\$14.7) million or 6% of Technotrans sales were generated in Asia. This weak base in the Asian market will make it difficult for Technotrans AG to compete in this high growth region. In 2006, estimated 70% of Technotrans' net sales of €151.3(\$222.4) million were generated in the printing segment.

## **Investment Risks**

### **Exchange rate risks**

In financial year 2007 roughly 80% of Baldwin's sales were generated internationally. The weakening dollar has increasingly benefited Baldwin's competitiveness over the past few years. However, conditions might change, if the Federal Reserve decides to raise interest rates to strengthen the dollar against the euro, yen and the Swedish krona. Such a scenario could have an unfavourable effect on the company's business results.

### **Reliance on one significant customer**

As in the past year, Baldwin will rely on one significant customer in fiscal year 2007. KBA accounted for about 17% of net sales. A decrease in sales to KBA could have an adverse effect Baldwin's performance.

### **Economic downturn**

An economic downturn could have an adverse effect on the company's results. Growth in the printing industry is highly correlated with GDP growth. The housing meltdown, tighter credit and rising oil prices can be likely to lead to an economic slowdown, or potentially a recession, in the U.S. A slowing U.S. economy could affect global economic growth and therefore not only impact Baldwin's domestic, but also its international sales.

### **New technologies**

The company continues to focus its research and development activities on the offset printing market and expects the demand in this industry to grow. However, new technologies, like digital printing emerge and will increasingly take away market share.

KBA estimates digital print to grow from 4%(2005) market share to 10% in 2015, eroding the offset market.

### **Commodity prices**

Rising commodity prices could increase production costs and thus reduce the company's profit margins. Thus, increasing demand for oil in developing countries and further capital flow out of the stock and housing market into commodity markets, can potentially have adverse effects on the company's profitability.

## **Discounted Cash Flow**

I arrive at a 12- month target price of \$6.34 for Baldwin Technology Company, using a discounted cash flow model with monte carlo simulation.

### **FY 2008:**

Sales growth, costs and interest payments are based on a triangular distribution , taking into account the following:

- The U.S economy slides into a recession, resulting in lower domestic sales.
- The dollar remains weak and benefits Baldwin's exports, but leads to higher interest payments
- Commodity prices surge and increase production costs

### **FY 2009:**

Sales growth, costs and interest payments are based on a triangular distribution , taking into account the following:

- The U.S. economy surprises with strong growth, leading to higher sales domestically
- The FED intervenes and increases interest rates, leading to a stronger dollar and therefore lower interest payments
- Easing commodity prices decrease production costs