

Colfax Corporation (NYSE: CFX) – Long

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ENOVIS	2021	2022	ESAB	2021	2022
Revenue	1,430	1,570	Revenue	2,430	2,550
<i>growth</i>		9.8%	<i>growth</i>		4.9%
EBITDA	254	280	EBITDA	434	455
<i>margin</i>	17.8%	17.8%	<i>margin</i>	17.9%	17.8%
EBITDA multiple	13.0 x	11.2 x	EBITDA multiple	13.0 x	11.0 x
Enterprise value	3,302	3,136	Enterprise value	5,642	5,005
Stryker	23.1 x	21.7 x	ITW mult	18.4 x	16.8 x
DePuy	20.0 x		LECO mult	14.8 x	13.1 x
Globus	23.2 x	17.0 x			
Medacta	22.8 x	18.7 x			
Ossur	20.8 x	17.6 x			
Zimmer Biomet	13.4 x	14.4 x			
Smith & Nephew	13.3 x	11.3 x			

COLFAX CORPORATION SUMMARY

Share price	40.00	
Shares out	161.3	
Market cap	6,452	
	<u>2021</u>	<u>2022</u>
Enovis value	3,302	3,136
ESAB value	5,642	5,005
Estimated EV	8,944	8,141
Net debt	1,200	1,200
Equity value	7,744	6,941
Implied share price	48	43
12-month IRR	19.7 %	7.5 %

Company: Colfax Corporation is really two different businesses:

- **Enovis (MedTech)** – Enovis is a growing provider of orthopedic devices covering joints and extremities with 2 segments
 - Prevention and rehabilitation (“P&R”) (~70% sales)
 - Reconstructive (~30% sales)
- **ESAB (FabTech)** – ESAB provides welding materials, devices, accessories, and digital platforms with 2 segments
 - Equipment (~31% sales)
 - Consumables (69% sales)

Background / Setup: Colfax Corporation is splitting its business into two separate, pure-play entities by spinning off its FabTech business after a failed merger in 2019. Both businesses are growing and high margin but were hit hard by the pandemic about a year after the purchase of the MedTech business (formerly DJO) closed, which has made the financials of each segment difficult to interpret and the outlook unobvious to sector specialists either in each of industrials or healthcare. The company is under-followed because of the odd marriage between segments

Thesis: The separation of Colfax’s businesses appears likely to unlock significant value as each segment trades at a substantial implied discount to peers. Stabilized financial performance and movement from “whatever-Colfax-is” into pure play companies should be strong catalysts for each segment to re-rate to less egregious discounts within their respective industries

We expect each of Colfax’s segments to re-rate to 13.0x LTM EBITDA respectively within 12 months following the separation of the businesses (scheduled for Apr 4)

Recommendation: Long Colfax Corporation (CFX) with a 12-month price target of \$48 per share, returning a 19.7% IRR

	Base	Bear	Bull
Enovis value	3,302	2,540	3,810
ESAB value	5,642	4,340	6,076
Estimated EV	8,944	6,880	9,886
Net debt	1,200	1,200	1,200
Equity value	7,744	5,680	8,686
Implied share price	48	35	54
12-month IRR	19.7 %	(11.8 %)	34.1 %

Thesis Detail:

Enovis (MedTech) is a stable, growing business in an industry with favorable tailwinds and solid management

- Colfax management suggests low- to mid-double digit revenue growth through 2024
 - P&R segment growing organically at 3%+, reconstructive growing HSD+ organically
 - Meaningful M&A opportunity with \$20B TAM in highly fragmented market for MSD+ inorganic growth
- EBITDA margins are historically 10-20% even through covid, while large industry peers achieve 20-30% at scale
 - Company is targeting 20%+ EBITDA margins by 2024 without consideration for accretive M&A
- Aging population and increased life expectancy bringing favorable tailwinds to target demographic

- Device innovation and outpatient procedure trends are driving procedure volumes, including a potentially large Covid backlog
- Mitch Rales will chair the board—founder of Danaher which is primarily known for its success in M&A roll up strategy

ESAB is a moderate-quality cyclical business with pricing power in an oligopoly and should trade at a soft discount to LECO

- While management expects MSD organic sales growth and the ability to pass through inflation to its customers
 - Russia invasion of Ukraine revised short-term outlook downward as ESAB has meaningful exposure to Russia
- High-teens EBITDA margins with a management target of 20%+ seems achievable based on pre-covid figures
- Consumables business is high-quality compounding business with large expansion opportunities in developing markets
 - Business exhibits high levels of pricing power because of critical nature for construction and engineering
- Meaningful opportunity in welding platform Saas space for management of workers and workflows

Valuation:

- At the current share price of \$40.07, each business is valued at single-digit EV / EBITDA multiples
 - We believe Enovis should trade ~13x LTM EBITDA
 - Implies a significant discount to medical device peers trading at 19x on average
 - Closest peer is likely Medacta group, which focuses on similar portfolio exposures at smaller scale and trades at 22.8x LTM EBITDA
 - ESAB is worth ~13x LTM EBITDA in our view
 - Reflects some discount to higher quality peers Lincoln Electric (LECO) and Illinois Tool Works (ITW)
 - Lincoln Electric is a direct peer and is segmented nearly identically to ESAB, but higher quality than ESAB

ENOVIS						ESAB					
	2018A	2019A	2020A	2021A	2022F		2018A	2019A	2020A	2021A	2022F
Revenue	2,193.1	976.0	863.0	1,426.0	1,492.8	Revenue	2,193.1	2,247.0	1,950.1	2,428.1	2,500.9
<i>Growth</i>			(11.6 %)	65.2 %	4.7 %	<i>Growth</i>		2.5 %	(13.2 %)	24.5 %	3.0 %
<i>CAGR</i>			(11.6 %)	20.9 %	15.2 %	<i>CAGR</i>			(5.7 %)	3.5 %	3.3 %
EBITDA		200.4	153.6	206.1	232.6	EBITDA		379.2	320.7	433.6	445.0
<i>Growth</i>			(23.4 %)	34.2 %	12.9 %	<i>Growth</i>			(15.4 %)	35.2 %	2.6 %
<i>CAGR</i>			614.8 %	288.1 %	439.7 %	<i>CAGR</i>			(15.4 %)	6.9 %	5.5 %
Multiple				13.0 x	11.0 x	Multiple				13.0 x	13.0 x
EV				2,679.7	2,559.0	EV				5,636.8	5,785.0
Net debt				-	-	Net debt				-	-
Equity value				2,679.7	2,559.0	Equity value				5,636.8	5,785.0
Shares out				161.3	161.3	Shares out				161.3	161.3
Stock price				16.6	15.9	Stock price				34.9	35.9

Risks:

- **Covid and elective procedures**– With most of the expected growth and value creation in the MedTech business, a meaningful decline in elective procedures as a secular rather than cyclical trend would suggest that perhaps Enovis should trade at a more meaningful discount to peers
- **ESAB’s emerging markets focus showing geopolitical risk** – ESAB’s growth is predicated on expansion into emerging markets. With Russia’s invasion of Ukraine and geopolitical instability across the globe, the business is facing meaningful risk of extended trough cycles in key markets, and low or negative growth in areas with high exposure
- **Asbestos claims** – While the company is insured, Colfax has a sizable number of asbestos claims sitting in its financials that could materialize to its detriment. It appears that these will be saddled with the FabTech business which generates sufficient FCF to offset any sort of recapitalization event. Asbestos claims also have a long history and are generally actuarially predictable, though changing regulations locally and nationally can drive unpredictable changes in outcomes

MARKET CAP SENSITIVITY

		ESAB NFY multiple						
		7.0 x	8.0 x	9.0 x	10.0 x	11.0 x	12.0 x	13.0 x
Enovis NFY multiple	6.0 x	3,665	4,120	4,575	5,030	5,485	5,940	6,395
	7.0 x	3,945	4,400	4,855	5,310	5,765	6,220	6,675
	8.0 x	4,225	4,680	5,135	5,590	6,045	6,500	6,955
	9.0 x	4,505	4,960	5,415	5,870	6,325	6,780	7,235
	10.0 x	4,785	5,240	5,695	6,150	6,605	7,060	7,515
	11.0 x	5,065	5,520	5,975	6,430	6,885	7,340	7,795
	12.0 x	5,345	5,800	6,255	6,710	7,165	7,620	8,075
	13.0 x	5,625	6,080	6,535	6,990	7,445	7,900	8,355
	14.0 x	5,905	6,360	6,815	7,270	7,725	8,180	8,635
	15.0 x	6,185	6,640	7,095	7,550	8,005	8,460	8,915

IRR SENSITIVITY

		ESAB NFY multiple						
		7.0 x	8.0 x	9.0 x	10.0 x	11.0 x	12.0 x	13.0 x
Enovis NFY multiple	6.0 x	(42.8 %)	(35.8 %)	(28.8 %)	(21.8 %)	(14.8 %)	(7.8 %)	(0.9 %)
	7.0 x	(38.4 %)	(31.5 %)	(24.5 %)	(17.5 %)	(10.5 %)	(3.5 %)	3.4 %
	8.0 x	(34.1 %)	(27.1 %)	(20.2 %)	(13.2 %)	(6.2 %)	0.7 %	7.7 %
	9.0 x	(29.8 %)	(22.9 %)	(15.9 %)	(8.9 %)	(1.9 %)	5.0 %	12.0 %
	10.0 x	(25.5 %)	(18.6 %)	(11.6 %)	(4.6 %)	2.3 %	9.3 %	16.2 %
	11.0 x	(21.2 %)	(14.3 %)	(7.3 %)	(0.3 %)	6.6 %	13.6 %	20.5 %
	12.0 x	(16.9 %)	(10.0 %)	(3.0 %)	3.9 %	10.9 %	17.8 %	24.8 %
	13.0 x	(12.7 %)	(5.7 %)	1.3 %	8.2 %	15.2 %	22.1 %	29.0 %
	14.0 x	(8.4 %)	(1.4 %)	5.5 %	12.5 %	19.4 %	26.4 %	33.3 %
	15.0 x	(4.1 %)	2.9 %	9.8 %	16.8 %	23.7 %	30.6 %	37.6 %