NYU STERN
NEW YORK UNIVERSITY · LEONARD N. STERN SCHOOL OF BUSINESS

EQUITY INSTRUMENTS AND MARKETS
FINAL VALUATION PROJECT

			DCF Valuation		Relative Valuation		
Analyst	**Company**	**Price**	**Model**	**Value**	**Multiple**	**Value**	**Recommendation**
Domingo Alonso	Brinker Intl.	$33.80	FCFF Gen	$44.13	PS	$45.65	Buy
Steve Vasquez	Millennium Pharmaceuti	$8.70	FCFF Gen	$6.42	VS	$30.74	Sell
Rafael Arteaga	Publicis Groupe	$28.50	FCFF Gen	$29.99	VS	$27.84	Hold
Malcolm Bosse	Taser Intl.	$8.64	FCFF Gen	$10.97	PEG	$9.47	Moderate Buy/Hold

May 2, 2005

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1. Company Overview

Brinker International, Inc, (EAT) is a company engaged in the ownership, operation, development and franchising of restaurant concepts. The Company's restaurant concepts includes Chili's Bar & Grill, which features Tex-Mex cuisine, Romano's Macaroni Grill, Maggiani's Little Italy, On the Border Mexican Grill & Cantina, Corner Bakery Café, Big Bowl and Rockfish Seafood Grill. EAT employs 96,600 people and has a market capitalization of $3.13 billion. As of June 30, 2004, the Company owned, operated, franchised or was involved in the ownership of 1,476 restaurants.
Services Company

2. DCF Valuation

I implemented a one stage stable growth discount model since the firm is in a highly competitive and mature industry. Moreover, the firm has been growing at a rate close to that of the economy.

The assumptions used to build the DCF model are:

	Stable Growth
Length of Growth Period	Forever
Growth Rate	3%
Debt Ratio	10%
Beta	0.8
Riskfree Rate	4.25%
Risk Premium	4.00%
Cost of Debt	5.10%
Tax Rate	35.20%
Return on Capital	16.74%
Reinvestment Rate	17.92%
Cost of Equity	7.25%
Cost of Capital	11.71%

Based on these inputs the valuation was as follows:

EBIT	$733.598 million
Equity Value	$9,103.648 million
Firm Value	$10,425.169
Value/Share	$44.13
Current market Price	$33.80

Sensitivity Analysis

The key drivers for EAT are the stable growth rate.

3. Relative Valuation

21 companies were used as comparables. Since EAT derives a majority of its revenue from the US, the comparables were all firms from the US deriving most of their income form the US. Additionally, I also selected firms with similar business plans, size and growth to best reflect EAT's value. As such, my comparables included such firms as Outback Steakhouse, Applebees, Darden Restaurants, Cracker Barrel and Ruby Tuesday.

The regression was completed on a Price-to-Sales ratio. I selected this ratio since EAT is the restaurant business and a PS multiple is suitable for such firms.

Regression Analysis:PS

The regression equation is

PS=-1.08 +0.776*Payout+9.89*Growth-0.096*Beta+16.2*Net Margin

Predictor	Coef	SE Coef	T	P
Constant	-1.0842	0.5702	-1.9	0.074
Payout	0.7759	0.7723	1.0	0.329
Growth	9.888	3.151	3.14	0.006
Beta	-0.0958	0.3717	-0.26	0.800
Net Margin	16.205	5.497	2.95	0.009

S=0.540421 R-Sq=55.5% R-Sq(adj)=45.0%

Based on this regression, EAT's predicted PS ratio is 1.10 resulting in a predicted stock price of $45.65. This is similar to the discounted cash flow model price. Moreover, as we can see the main driver of the regression is Net Margin. The higher the net margin the higher the PS ratio will be.

The average PS for the comparables was 1.34, lower than EAT's PS ratio.

4. <u>Market Valuation</u>

The market regression equation is

PS=0.0516*Growth-0.0069*Payout-0.0705*Beta+0.2198*Net Margin ($R2$=61.3%)

Based on this equation the predicted PS is 1.24, resulting in a stock price of $51.60.

5. Final Analysis

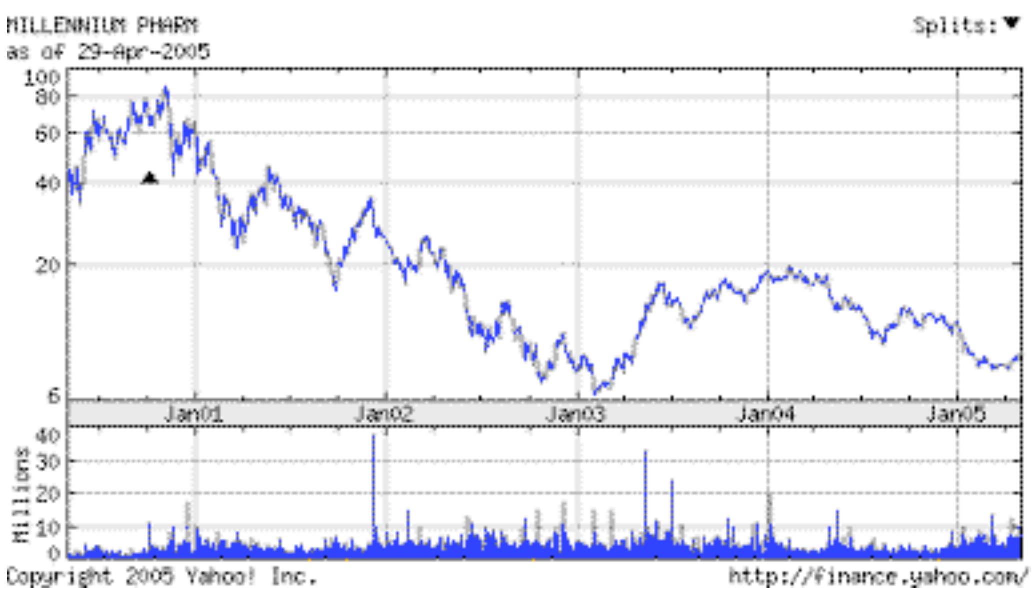
Current Price	$33.80
DCF Price	$44.13
Average PS of comparables	1.34
Average PS regression	1.10
Market PS regression	1.24

I would place most of my valuation weight on the DCF valuation since I believe given where the market currently prices EAT that the DCF most truly reflects EAT's value. As such, I would recommend EAT as a strong buy given that it is undervalued in both the intrinsic and relative valuation analysis.

MILLENNIUM PHARMACEUTICALS

1. Company Overview

Millennium Pharmaceuticals is a biotechnology company concentrating on drug discovery. Since 1993 they have progressed down the value chain of the pharmaceutical industry from basic research to sales and marketing of pharmaceuticals. In the past few years their pipeline has failed to deliver the promised drugs and in order to compensate they acquired a number of companies with drugs already on the market. As their pipeline has failed to deliver viable compounds, their stock price has declined. Currently they are marketing two drugs and hope to broaden the scope of diseases for which they are approved.



2. DCF Valuation

Millennium was valued using a two stage growth model. Growth was projected out for 10 years and a stable period was estimated using industry averages. The key assumption in the valuation was the expected growth for the first 10 years. Millennium was given a growth rate of 20% based on their expected reinvestment rate and future return on capital. A more precise method would have been to project the total market for the drugs that Millennium is developing and estimate its market share. This would require very specific knowledge of the drug industry and was beyond the scope of this valuation.

As Millennium transitions from high growth to stable growth, there are a few key assumptions that affect the valuation. In addition to the growth mentioned earlier, return on capital and reinvestment rate are expected to change significantly. ROC will move from -11% to 7.4%, the industry average. The reinvestment rate will move from 29%, a non-meaningful number given their negative EBIT to 40.5%, the industry average.

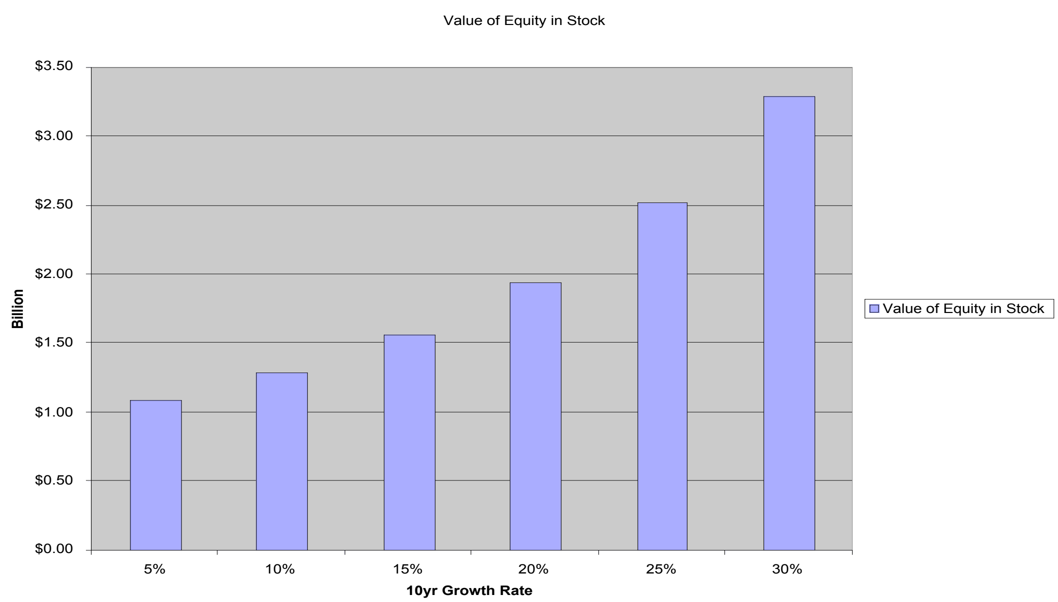
	High Growth	**Stable Growth**
Length of Growth Period	10 years	Perpetuity
Growth Rate	20%	3%
Debt Ratio	3.9%	8.0%
Beta	1.8	1.15
Cost of Debt	8.00%	6.00%
Return on Capital	-11.00%	7.40%
Reinvestment Rate	29%	40.50%
Cost of Equity	12.96%	9.82%
Cost of Capital	12.77%	9.30%

Based on the DCF the value of Millennium as a firm is $2.048B with $1.942B in common stock. This differs significantly from MLNM's market cap of $2.67B which is not unexpected considering the difficulty in projecting growth and returns for a biotech company.

The Valuation	
Value of Firm =	$2,048,733,790
- Value of Outstanding Debt =	$105,667,216
Value of Equity =	$1,943,066,575
- Value of Equity Options =	$86,552
Value of Equity in	$1,942,980,023

Common Stock =	
Value of Equity per share =	$6.42

One way to compare the DCF value to its market cap is to examine how changes in assumptions would change Millennium's value. Comparing the value of equity in stock to growth rate illustrates how sensitive the analysis is to the underlying assumptions. To justify Millennium's current market cap of $2.67B, it would require a growth rate greater than 25%. One way to improve the DCF would be to get revenue projections for drugs that are currently on the market as well as ones that are being developed. From the estimates we could tailor the growth rate over the next 10 years to more accurately reflect expectations.

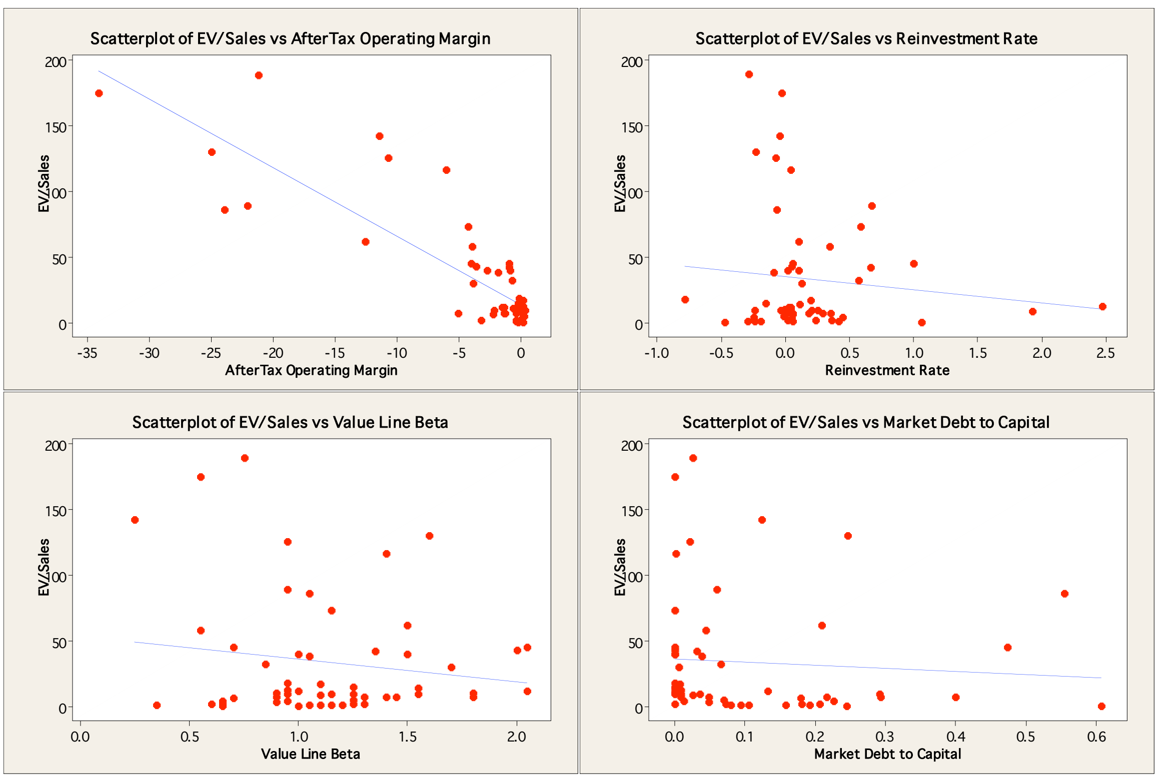


3. **<u>Relative Valuation</u>**

Millennium's comparable companies were defined as publicly traded companies that were categorized with a "Biotechnology" SIC. The group of 57 companies contained domestic and foreign, positive and negative earnings and large and small companies.

Considering the high frequency of firms with negative earnings, we chose Enterprise Value-to-Sales to evaluate Millennium. The sector average was an EV/S of 40 but this number is difficult to interpret given the range of size and profitability of the companies.

We also looked at Millennium's EV/S versus reinvestment rate, after-tax operating margin, debt to capital ratio and beta. Our first choice was to use the projected growth in revenues over the next 5 years but this wasn't available for the bulk of companies. Beta was substituted for growth in an attempt to capture the riskiness and possibly serve as a proxy for growth. The graphs below depict the regressions and scatterplots. Again it is very difficult to assess whether Millennium is fairly valued or not based on the charts.



The multiple regression of EV/Sales versus reinvestment rate, after-tax operating margin, market debt to capital and beta produced a more suitable model to evaluate Millennium. The regression produced an equation of

EV/Sales = 20.2 - 0.75 Reinvestment Rate - 5.32 After-Tax Operating Margin

- 52.5 Market Debt to Capital - 1.51 Value Line Beta

The significance for each variable is as follows:

Predictor	Coef	SE Coef	T	P
Constant	20.23	10.29	1.97	0.055
Reinvestment Rate	-0.752	6.422	-0.12	0.907
After-Tax Operating Margin	-5.3188	0.4463	-11.92	0.000
Market Debt to Capital	-52.45	23.04	-2.28	0.027
Value Line Beta	-1.513	8.198	-0.18	0.854

S = 24.0520   R-Sq = 75.0%   R-Sq(adj) = 73.0%

Based on the regression, Millennium has a predicted EV/S of 19.3 and a predicted EV of $9.3B. With an actual EV/S of 6.1 and an EV of under $3B it would appear as though Millennium were undervalued.

4. Market Valuation

Based on the latest market regression, Millennium has a predicted EV/S of -2.32. With an actual EV/S ratio of 6.1, it would appear as though Millennium is over valued. However, it is unclear what a negative EV/S ratio would mean considering the market values of debt and equity and sales are all positive. A better interpretation is that Millennium's fundamentals are significantly different than the average in the market and thus should be compared to the market using a different multiple or should be restricted to comparisons within its sector. Because of Millennium's negative after-tax operating margin, it would be difficult to compare to the market where most firms have much higher after-tax operating margin to revenue ratios.

EV/S Market Regression:

Enterprise Value/Sales = 0.182 g(rev) + 0.0861 After-tax Operating Margin -.0256 (Debt/Capital) - 0.0013 Reinvestment Rate (R^2 = 48.3%)

Expected Growth = 18.9%
After-tax Operating Margin = -65.3%
Debt/Capital = 3.9%
Reinvestment Rate = 29%

Predicted EV/S= -2.32

5. Option Pricing Models

The application of option pricing models to Millennium is not as relevant today as it was 2-3 years ago. Since 2002, their R&D costs have declined from $511M to $488M in 2003 to $402M in 2004. There has been a clear shift from developing drugs from their pipeline to concentrating on 2 drugs that were obtained through acquisitions. As such, the bulk of their future revenue is expected to come from the continued commercialization of already FDA-approved drugs. Although they will continue to develop their drug discovery pipeline, their continued lack of success in organic growth along with their tapering of R&D make it difficult to accurately apply an option pricing model.

6. Final Value Estimate and Recommendation

The DCF and relative valuations paint different pictures of Millennium but this is not surprising considering the difficulty in forecasting revenue and the extremely noisy sample of biotechnology firms. We don't put much confidence in the sector relative valuation considering the number of firms with missing or non-meaningful data. The DCF relies on numerous assumptions but they are clearly stated and can be modified to reflect new information. Overall the DCF valuation is the one that carries the most weight and therefore the recommendation is that Millennium is overvalued.

1. Company Overview

Headquartered in Paris, France, Publicis Groupe (PUB) is the world's fourth largest communications group, as well as the world leader in media buying and media consultancy. Publicis ranks No. 1 in Europe and No. 3 in the U.S. in terms of billings. Its activities span 109 countries on all continents, 229 cities, with 35,166 employees. Publicis is structured around three core businesses: traditional advertising, specialized agencies and marketing services (SAMS), and media services. Publicis serves clients predominantly in North America, including the United States and Europe. Although Publicis experienced significant growth in the past years primarily as a result of M&A activity, this trend is not expected to continue as the industry has reached stability and there are no major advertising networks available for sale. In 2004, Publicis reported revenues of $4.4 billion (€3.9 billion), which represented a 4% organic growth over the previous year. Since Publicis (and the industry) has reached maturity, we expect the company to continue to grow close to 4% in the long-term.

2. DCF Valuation

We pursued a one-stage stable growth discount model for Publicis since the company is in a consolidated and mature industry. In addition, Publicis has been growing at a rate close to that of the economy and is expected to continue to do so.

The assumptions used to build the DCF model are the following:

	Stable Growth
Length of Growth Period	Forever
Growth Rate	4%
Debt Ratio	40%
Beta	1.2
Riskfree Rate	4.25%
Risk Premium	4.90%
Cost of Debt	4.75%

Tax Rate	38.60%
Return on Capital	4%
Reinvestment Rate	-35.37%
Cost of Equity	10.93%
Cost of Capital	8.57%

Based on these inputs the valuation was as follows:

EBIT	$523.4 million
Equity Value	$5,457.70 million
Firm Value	$8,003.50 million
Value/Share	$29.99
Current market Price	$28.50

Sensitivity Analysis

As can be seen below, the valuation for Publicis during stable growth is very sensitive to a change in the long-term growth rate or ROC.

Keeping all other variables constant, changing the growth rate of the firm during the stable growth period affects the valuation as follows:

Growth Rate (Stable growth period)	Value per share
3%	$41.27
3.5%	$36.46
4%	$29.99
4.5%	$20.85

Keeping all other variables constant, changing the ROC of the firm during the stable growth period affects the valuation as follows:

ROC (Stable growth period)	Value per share
3%	$9.77

3.5%	$21.37
4%	$29.99
4.5%	$36.73

3. Relative Valuation

For Publicis' relative valuation, we identified 39 companies as comparables. Two groups of companies were selected: Advertising companies and Entertainment companies that generated a significant share of their revenues from advertising. The latter type was included to provide a deeper selection of comparables. Another important criteria in the selection process was market capitalization. Given Publicis' market capitalization of $5.9 billion, companies with a market cap below $500M were taken out of the sample. Since Publicis generates 45% of revenues from the U.S. and 40% from Europe, we are confident the companies selected provide a comparable source of cash flows.

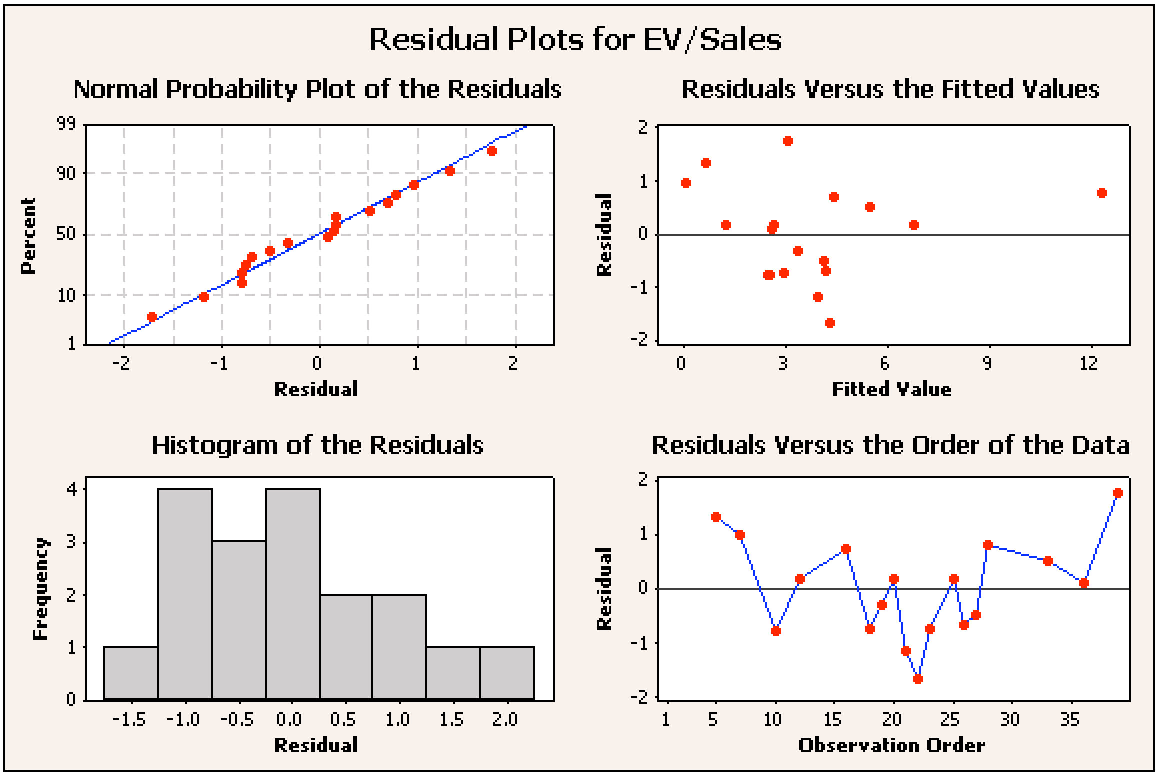
After considerable analysis of the industry (i.e. different leverage ratios) and the company fundamentals, we chose the "Enterprise Value to Sales" ratio to conduct our regression analysis. Following are the regression results:

The regression equation is
EV/Sales = - 0.990 + 0.800 3-yr Regression Beta - 2.82 Book Debt to Capital + 13.6 Pre-tax Operating Margin + 14.8 Expected Growth in Revenues

Predictor	Coef	SE Coef	T	P
Constant	-0.990	0.8949	-1.11	0.289
3-yr Regression Beta	0.7997	0.3232	2.47	0.028
Book Debt to Capital	-2.823	1.03	-2.74	0.017
Pre-tax Operating Margin	13.551	1.816	7.46	0
Expected Growth in Revenues	14.76	7.99	1.85	0.088

S = 1.04760 R-Sq = 89.7% R-Sq(adj) = 86.6%

The regression yielded an impressive R^2 of 89.7% with a strong contribution from the dependent variables selected in terms of T-values. As can be expected, the "Pre-tax Operating Margin" yielded the highest T-Value with 7.46. From the regression we extrapolate that a 1% increase in pre-tax operating margin increases the EV/Sales ratio by 13.5, according to how the market is evaluating advertising companies.



Based on the regression formula, Publicis' EV/S ratio should be 1.24. The predicted EV/S also suggests a stock price for Publicis of 27.84.

4. <u>Market Valuation</u>

When comparing Publicis to the market regression, we chose to use the market EV/S regression equation for large U.S. companies because Publicis generates more revenues from the U.S. market than from Europe and because the equation included "expected growth in revenues", which we found to be a very efficient variable in explaining the y variable. Further, we are using the company's financial ADR information.

The U.S. market EV/S regression equation:

Enterprise Value/Sales = 0.182 g(rev) + 0.0861 After-tax Operating Margin -.0256 (Debt/Capital) - 0.0013 Reinvestment Rate

Based on this equation the predicted EV/S is 1.21, resulting in a stock price of $27.09. This suggests that Publicis' stock price is 16% overvalued.

5. Final Analysis

Current Price (4/29/05)	$28.50
DCF Price	$29.99
V/S Price regression	27.84
Market V/S regression	27.09

Publicis Groupe has been a top performer relative to competitors in terms of new business acquisition, organic growth and operating margin. Despite reporting a negative capex, Publicis has been able to grow its returns through realizing efficiencies and cost cutting. Publicis has developed a core competency of efficiently integrating acquired companies into the network and quickly realizing the synergies. However, no major acquisitions are expected in the future as all global independent networks have already been acquired. Publicis has a major weakness looking forward in its diversification of revenue streams. More than 70% of Publicis' revenues come from traditional advertising and media spending. Thus, the company is underexposed to marketing services, which account for 60% of the global communications industry revenues. Publicis needs to develop its services credentials in the areas of CRM and Interactive Marketing.

The valuation models we conducted for Publicis (DCF valuation and Relative valuation) have suggested opposing target stock prices. The DCF valuation yielded a target stock price of $29.99, 5% higher than the current stock price (4/29/05). The relative valuation suggested a stock price of $27.84, 2% lower than the current stock price. We believe both models to be correct considering the standard error and some of the underlying assumptions of both models. Thus, we can conclude that Publicis Groupe is correctly priced and we suggest a "Hold" strategy.

1. Company Overview

Taser International, Inc. develops and manufactures less-lethal self-defense devices. From its inception until the introduction in 1994 of its first product, the AIR TASER, the Company was in the developmental stage and focused its efforts on product development, raising capital, hiring key employees and developing marketing materials to promote its product line. The Company's primary product lines include the ADVANCED TASER and the TASER X26. The TASER X26 weapon system introduced to the market a new "shaped pulse" technology, and a new smaller form factor. At the close of 2003, Taser had more than 4,300 United States law enforcement agencies deploying one of its Taser brand weapon platforms, with 506 agencies either completed or in the process of implementing a full deployment of one weapon for each patrol or line officer.

2. DCF Valuation

Taser International was valued using a two stage FCFF Valuation Model because the company is a high growth company that has historically used relatively little debt and is expected to increase its use of debt due to its plans for international and product line expansions.

The assumptions used to build the DCF model are:

	High Growth	Stable Growth
Length of Growth Period	10	In perpetuity
Growth Rate	25.06%	4.80%
Debt Ratio	25%	25%
Beta	3.68	1.20
Riskfree Rate	4.25%	4.25%
Risk Premium	4.84%	4.84%
Tax Rate	39%	35%
Return on Capital	34.30%	11.78%
Reinvestment Rate	73.06%	42.44%

Based on these inputs, the valuation is as follows:

Current Revenues	$67,639,879
Adjusted EBIT	$31,566,630
Value of the Firm	$682,609,412
Market Value of Debt	$379,181
Market Value of Equity	$682,230,231
Market Value of Equity/share	**$10.97**
Current Stock Price	**$8.64**

Sensitivity Analysis: The key drivers for the valuation of Taser are its growth rate and length of the growth period.

	Growth Period		
Growth Rate	5	10	15
15%	$6.46	$6.33	$6.28
20%	$7.35	$8.34	$9.04
25%	$8.35	$10.97	$12.99
30%	$9.42	$14.25	$18.39
35%	$10.60	$18.45	$25.91
40%	$11.89	$23.75	$36.19

This table illustrates how crucial the length of the growth period and the growth rate are to Taser's valuation. The range presented from this table of $36.19 to $6.46 matches Taser's 52 week high and low of $33.45 to $8.48. Therefore, this trading range reflects the roller coaster ride that Taser's shareholders have been on primarily due to safety concerns of Taser's products.

3. <u>Relative Valuation</u>

58 companies were included in the relative valuation regression. Of these 58 companies, 23 were aerospace and defense companies, 15 were computer software and service firms, 5 computer peripheral companies, 5 internet/e-commerce companies, and 9 semiconductor firms. The criteria for choosing these firms was based on companies with market capitalizations that were less than 10 billion, and companies with growth rates that were higher than 10%. As a result, large aerospace companies such as Northrop Gruman, Boeing and General Dynamics were excluded from the regression. These selections were made to identify companies that were relatively young small to mid-cap and growing at a high rate.

The PEG ratio was selected because it appropriately measures growth relative to market price. The ratio produced the highest R-squared compared to other ratios such as PE and Price to Sales ratios.

Custom Regression:

The regression equation is

PEG = 3.22 – 0.477*LN(grth.) + 0.013*BETA+2.56*PAYOUT RATIO

R-Sq = 47.3%

Based on this regression, Taser's **predicted PEG is 1.65** which results in a **stock price of $9.47** (PEG = PE / Earnings Growth; 1.65 = PE / 30%; PE = .495 so .495 * 19.13 million in net income = $9.47)

U.S. Equity Regression:

The United States equity PEG multiple regression

PEG = 8.530 +– 2.727*LN(grth) +0.730*BETA – 0.0008*PAYOUT

R-Sq = 31%

This regression yields a **predicted PEG of 1.96** which results in a **share price of $11.25** (PEG = PE / Earnings Growth; 1.96 = PE / 30%; PE = .588 so .588 * 19.13 million = $11.25)

4. Market Valuation

Out of the 58 companies that were evaluated, the 5 companies with the highest simple PEGs were mostly technology firms and one aerospace/defense firm. The five lowest simple PEG companies were all technology companies as well. Taser's simple PEG of 1.09 placed it as the 18th company (out of 58) with the lowest PEG. Viewed on a PEG basis, Taser is less expensive than the average company in this group with a PEG of 1.91. This could be because Taser has very high risk which is reflected by an extremely high standard deviation of 137.62% and a lofty beta of 3.71.

Company Name	Industry	Curr. PE	PEG	Growth in EPS: next 5 yrs.	3-yr Reg. Beta	Standard Deviation	ROE	Pre-Tax Op. Margin	Book Debt to Capital
Goodrich Corp.	Aerospace/Defense	101.91	8.49	12%	1.12	37.94%	3.18%	11.76%	64.98%
Supertex Inc.	Semiconductor	130.32	5.79	23%	1.26	35.07%	2.25%	10.68%	0.00%
Sigma Designs	Comp./Peripherals	134.33	4.48	30%	3.38	101.11%	5.77%	6.84%	0.00%
Autodesk Inc.	Comp. Software/Svcs	91.82	4.27	22%	1.08	40.40%	15.51%	13.94%	0.00%
Blue Coat Systems Inc	Internet	149.07	3.73	40%	1.37	97.37%	4.16%	6.37%	0.00%
Aeroflex Inc.	Aerospace/Defense	45.11	3.01	15%	1.83	69.64%	4.80%	15.85%	2.35%
United Industrial Corp.	Aerospace/Defense	32.61	2.96	11%	0.47	35.48%	36.92%	9.67%	0.00%
Armor Holdings	Aerospace/Defense	93.09	2.91	32%	1.46	45.55%	5.75%	13.36%	40.50%
Red Hat Inc.	Computer Software/Svcs	172.49	2.72	64%	1.83	72.87%	3.42%	8.00%	59.51%
Moog Inc. 'A'	Aerospace/Defense	28.15	2.68	11%	0.28	41.80%	10.07%	13.69%	37.70%
Taser International Inc.	Aerospace/Defense	28.40	1.09	30%	3.71	137.62%	16.06%	32.63%	1.08%
Infosys Technologies Ltd.	Computer Software/Svcs	34.64	1.04	33%	1.20	44.48%	28.35%	32.61%	2.21%
Cyberguard Corp	Computer Software/Svcs	30.65	1.02	30%	0.00	0.00%	9.39%	14.87%	0.00%
ARGON ST Inc	Aerospace/Defense	23.79	0.94	36%	0.00	0.00%	6.15%	13.38%	0.19%
Lam Research	Semiconductor Equip	40.22	0.87	47%	3.42	64.35%	10.70%	15.40%	0.00%
Provide Commerce Inc	E-Commerce	22.53	0.83	27%	0.00	0.00%	31.30%	11.04%	0.00%
1-800-FLOWERS.COM	Internet	27.57	0.74	38%	2.45	63.70%	10.78%	6.03%	4.65%
National Semic.	Semiconductor	22.57	0.34	67%	2.75	68.14%	16.83%	27.24%	1.30%
QAD Inc.	Comp. Software/Svcs	20.86	0.47	44%	2.46	77.58%	31.42%	11.18%	29.49%
OmniVision Technologies	Semiconductor	17.21	0.65	27%	3.65	99.58%	19.57%	28.01%	0.00%
Harris Interactive Inc	Internet	16.09	0.64	25%	0.66	49.69%	18.07%	12.55%	0.00%
AVERAGE OF ALL 58 COMPANIES		*46.80*	*1.91*	*26%*	*1.34*	*47.91%*	*12.54%*	*15.81%*	*13.30%*

According to Taser's **given PEG of 1.09 its stock price should be $6.25**, which is significantly lower than the custom regression, U.S. equity regression, and the DCF projected stock prices.

5. <u>Final Analysis</u>

Shares of Taser International have recently tumbled over 15% to a 52-week low of **$8.25** after the stun-gun manufacturer blamed a revenue warning on negative publicity.

On the negative side:

- Critics have tied the company's stun guns, marketed as non-lethal weapons, to dozens of deaths;
- Taser is threatened by an informal probe launched by the Securities and Exchange Commission over Taser's safety claims as well as accusations of channel stuffing;

- In a Jan. 11 open letter to shareholders, the company acknowledged the SEC investigation and admitted that revenues in the first half of 2005 wouldn't gain at the 177% rate seen in 2004;
- The company has admitted that CEO Smith and his brother Tom, Taser's president, sold an average of 22% of their stake in the company. Shareholder lawsuits have followed.

On the positive side:

- The company is a clear leader in its market;
- Taser's balance sheet can self-finance up to three times its capacity with no need for investment banking (although mounting legal costs could negatively affect its cash account);
- Taser could possibly grow its revenue to over 100% in the next three years since it has little competition in the stun gun/defense weapon niche market;
- just 5.2% of the country's individual officers actually carry the weapons;
- there are many relatively untapped markets of the U.S. military, private security firms and consumers that Taser can eventually target.

Therefore for the near term the stock is slightly undervalued and is probably at its low. The question remains when or if it will be able to regain its 52 week high of $33.45. As a result, I recommend a hold/moderate buy on this stock.

1. Value of Control

A common reason why a Firm's stock is undervalued is due to its poor management which can lead to a loss of value. We will now analyze Taser as if it were optimally run. There are three areas that we would chose to modify, they include:

- The debt ratio should be modified from 25% to 30%. We believe that this is a reasonable increase because the company currently has no debt and could use borrowings to fund its product line and international expansion. One concern would be that due to an increase in litigation costs, Taser must be careful in maintaining or increasing its cash holdings which is currently at $15 million.

- Taser has an opportunity to make its product less discretionary to its customers if it is able to weather the current storm over the safety of its stun guns. We believe that it will be able to do this if it fights back against the negative publicity by increasing the effectiveness of its advertising and assurances of product safety. This should reduce the general riskiness of the stock and the risk premium of the stock which will decrease the cost of equity. In addition, we realized that unlike a typical high growth technology stock, Taser is a company that has positive net income of $19 million, no debt, and provides a unique product which has little competition. Therefore, we decided to lower the current beta of 3.71 to a more reasonable beta of 2.5 (which is conservative since Taser's most comparable competitor, Aeroflex has a beta of 2.3.)

- Finally, we increased the growth rate from 25% to 30%. Although we believe that this is a relatively optimistic view of Taser's performance, it is likely that Taser will pursue an acquisition to diversify its revenue streams and expand its product offerings. We also believe that if Taser comes up with a satisfactory response to the safety concerns, it will be able to increase its capital turnover ratio which will result in an increased expected growth rate.

If Taser is able to implement these three actions, Taser's value per share will increase to $19.06 from $10.97.

The resulting value of control is:

Value of the Firm: with Control Change	**$1,176,540,787**
Value of the Firm: Status Quo	**$682,609,412**
Value of Control	**$493,931,375**