NAIC Stock to Study
for October 2005
Carnival Corp.

Presented by:

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NAIC DC Chapter
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What is NAIC?

- **National Association of Investors Corporation**
- **NAIC teaches individuals how to become successful strategic long-term investors**
- **NAIC investors use fundamental analysis to study common stocks**
- **Websites:**
  - **www.better-investing.org**
  - **www.naicdc.org**

NAIC Principles

- Invest a fixed amount regularly for the long term
- Reinvest all of your earnings
- Invest only in good quality growth companies
- Diversify (by size and industry)

Carnival Corp. & PLC

- Carnival Corp. is the largest cruise company in the world with 12 brands which include Carnival Cruise Lines, Princess Cruises, Holland America Line, Costa Cruises, P&O Cruises, Cunard Line, Windstar Cruises, Seabourn Cruise Line, Ocean Village, Swan Hellenic, AIDA, and P&O Cruises Australia.
- Operates 78 ships with over 134,000 lower berths.
- Also operates tour companies in Alaska and the Canadian Yukon, Holland America Tours, and Princess Tours.

American Depositary Receipts

- **American Depositary Receipts were created in 1927 to aid US investor who wished to purchase shares of non-US corporations.**
- **An American Depositary Receipt (ADR) is a share of stock of an investment in shares of a non-US corporation. The shares of the non-US corporation trade on a non-US exchange, while the ADRs trade on a US exchange.**
- **Two banks are involved in maintaining an ADR:**
  - **Investment bank purchases the foreign shares and offers them for sale in the US.**
  - **Depositary bank handles the issuance and cancellation of ADRs.**
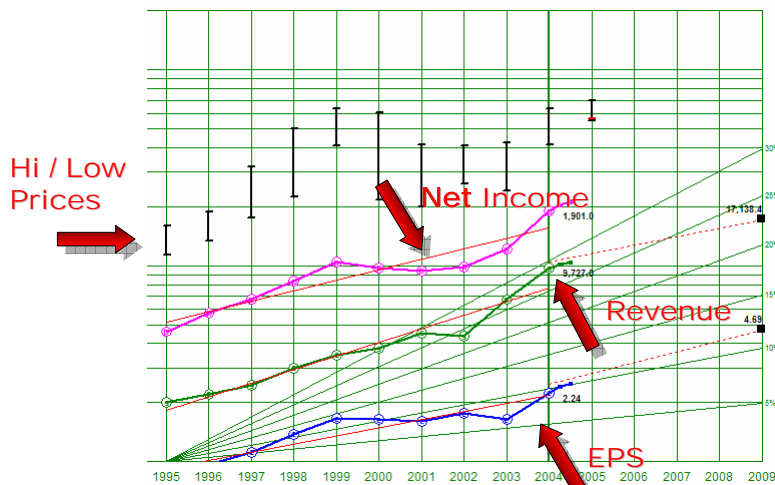
NAIC Stock Selection Guide

- **Section 1 – Visual Analysis (sales, EPS and net profit by year, also, high and low price)**
- **Section 2 – Evaluating Management**
- **Section 3 – Price-Earnings History**
- **Section 4 – Evaluating Risk and Reward**
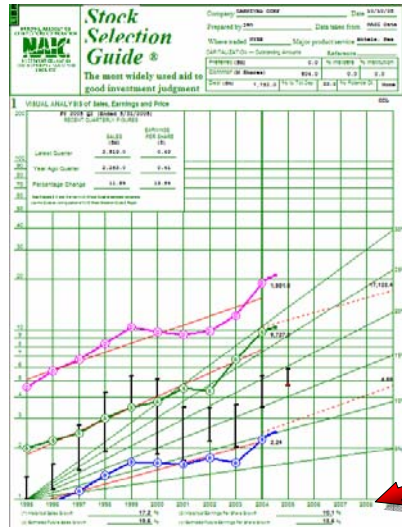- **Section 5 – Five-Year Potential**

Visualizing the Data
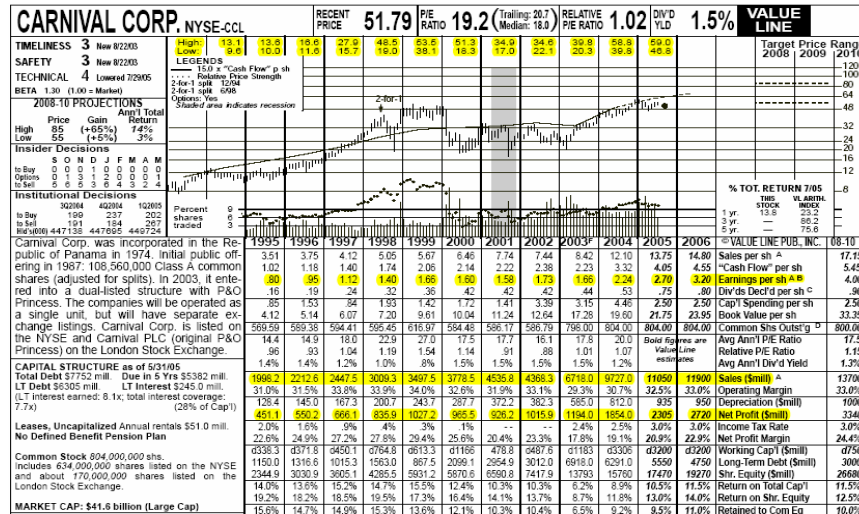
Visual Analysis

Projecting Earnings Growth

- First Call – 15%
- Visual Analysis – 13-15%
- Value Line – 10.5% Sales, 13.5% Earnings

ANNUAL RATES of change (per sh)	Past 10 Yrs.	Past 5 Yrs.	Est'd '02-'04 to '08-'10
Sales	12.5%	13.5%	10.5%
"Cash Flow"	13.5%	9.0%	13.0%
Earnings	12.5%	6.0%	13.5%
Dividends	12.5%	8.5%	12.0%
Book Value	19.0%	16.5%	12.5%

For SSG: 13.5% EPS Growth

Projected 5-Year EPS
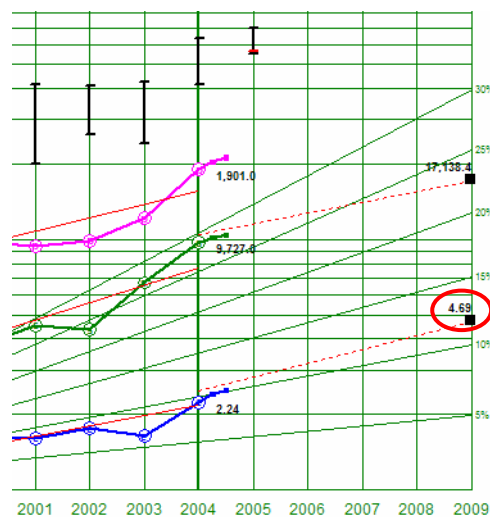
- EPS growth is projected at 13.5%
- $2.24 for last FY
- $2.49 for TTM
- Proj. 5-yr EPS = $(2.49)*(1.135)^5$

Projected 5-year EPS is $4.69

Sec. 2: Evaluating Management

- ■ **Key indicators of management:**
  - ■ **Pre-tax profit margin**
  - ■ **Return on equity**
- ■ **Compare company's ratios with its industry**
- ■ **Caution: The worse a company performs, the better value it may appear to be.**
  - ■ **Trailing and forward PE drops**
  - ■ **Projection at historic growth shows high projected return**

Evaluating Management

- ■ **SSG Section 2**

2 EVALUATING MANAGEMENT   Company   **CARNIVAL CORP**   **(CCL)**   10/10/05

		1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	LAST 5 YEAR AVG.	TREND UP	TREND DOWN
A	% Pre-tax Profit on Sales (Net Before Taxes ÷ Sales)	23.0	26.0	27.5	27.7	29.9	25.9	20.8	22.6	18.1	19.5	21.4		DOWN
B	% Earned on Equity (E/S ÷ Book Value)	19.1	18.8	18.4	19.2	17.3	16.3	14.3	13.9	9.5	11.4	13.1		DOWN

- ■ **Pre-tax profit over the past five years of 21.4% with a slight <u>downward</u> trend**
- ■ **Return on equity over the past five years is 13.1% with a <u>downward</u> trend**

Industry Comparisons

Management Effectiveness				
Management Effectiveness (%)	Company	Industry	Sector	S&P 500
Return On Assets (TTM)	7.93	6.04	5.45	7.59
Return On Assets - 5 Yr. Avg.	8.28	5.57	4.76	6.34
Return On Investment (TTM)	9.66	7.25	7.89	11.45
Return On Investment - 5 Yr. Avg.	9.76	6.10	7.02	10.02
Return On Equity (TTM)	13.71	12.81	1	36
Return On Equity - 5 Yr. Avg.	13.91	11.99	1	39

ROE

Financial Strength				
Financial Strength	Company	Industry	Sector	S&P 500
Quick Ratio (MRQ)	0.37	0.52	0.88	1.25
Current Ratio (MRQ)	0.50	0.67	1	75
LT Debt to Equity (MRQ)	0.37	0.54		
Total Debt to Equity (MRQ)	0.44	0.62	0.89	0.73
Interest Coverage (TTM)	7.86	6.57	8.56	13.00

Debt

Profitability Ratios				
Profitability Ratios (%)	Company	Industry	Sector	S&P 500
Gross Margin (TTM)	55.27	52.21	41.93	45.74
Gross Margin - 5 Yr. Avg.	54.23	51.69	41.75	45.07
EBITD Margin (TTM)	31.81	29.48	20.12	21.57
EBITD - 5 Yr. Avg.	30.78	28.45	20.92	20.05
Operating Margin (TTM)	23.58	20.98	12.02	20.71
Operating Margin - 5 Yr. Avg.	22.47	19.82	11.25	17.95
Pre-Tax Margin (TTM)	20.73	17.17	1	
Pre-Tax Margin - 5 Yr. Avg.	21.06	17.27	1	
Net Profit Margin (TTM)	20.42	16.33	6.69	13.47
Net Profit Margin - 5 Yr. Avg.	21.18	16.28	6.78	11.07
Effective Tax Rate (TTM)	1.48	6.56	31.39	30.50
Effective Tax Rate - 5 Yr. Avg.	1.65	7.78	33.71	33.17

Pretax Margin
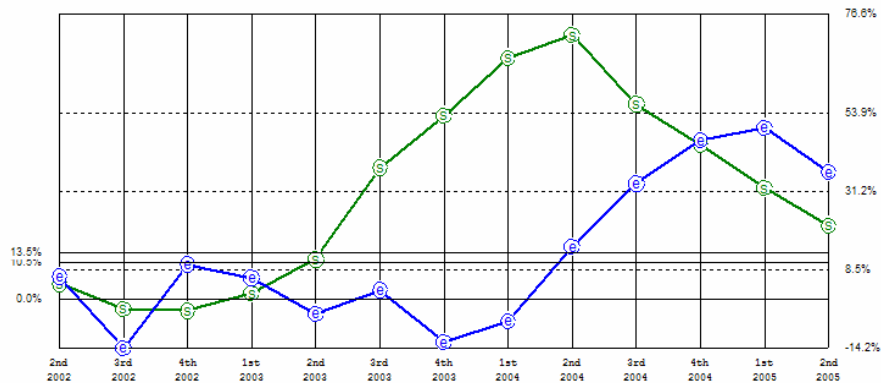
**Industry comparisons:
http://www.investor.reuters.com**

Trailing Pretax Profit Margin and Profit Margin (as % of Sales)
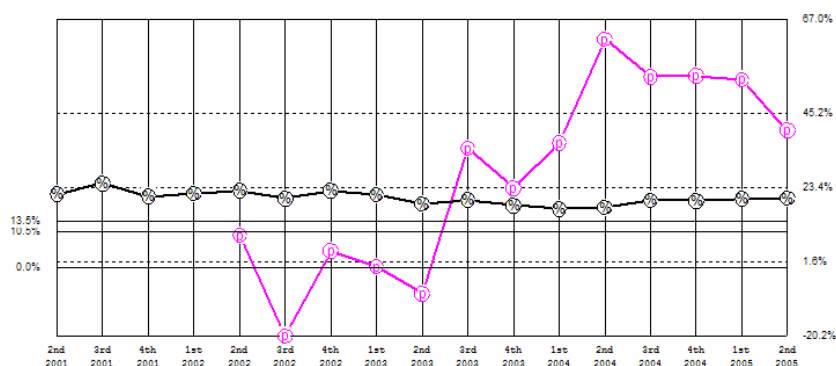
- **Pre-tax profit margin sometimes signals a problem before it is reflected in the EPS. No problem here.**

Trailing EPS and Revenue Growth

Value Line Quality Indicators

- *Earnings Predictability—*measure of the reliability of an earnings forecast. The most reliable forecasts tend to be those with the highest rating (100); the least reliable (5).
- *Financial Strength Rating—relative* measure of financial strength of the companies reviewed by Value Line. The relative ratings range from A++ (strongest) down to C (weakest), in nine steps.

Value Line Quality Indicators
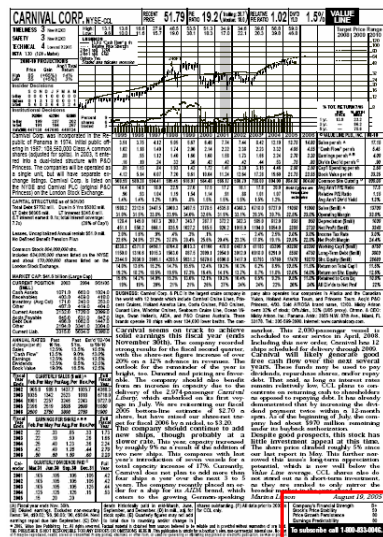
- **Financial Strength (B++ or better)**
- **Earnings Predictability (85 or better)**

Company's Financial Strength	B+
Stock's Price Stability	50
Price Growth Persistence	80
Earnings Predictability	80

Summary of Quality Metrics

| 2 EVALUATING MANAGEMENT | | Company | CARNIVAL CORP | | (CCL) | | | | | 10/10/05 | | |

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B % Earned on Equity (E/S ÷ Book Value)	19.1	18.8	18.4	19.2	17.3	16.3	14.3	13.9	9.5	11.4	13.1		DOWN

Value Line Data

Company's Financial Strength	B+
Stock's Price Stability	50
Price Growth Persistence	80
Earnings Predictability	80

RQR – Manifest Investing

Quality		
Financial Strength	50	12.5
EPS Predictability	80	20.0
Industry Sales Growth Rate	5.7%	12.1
Industry Net Profit Margin	8.8%	25.0
Calculated Quality Rating		69.6

Sec. 3: Price-Earnings History

- **Accept or amend High and Low avg. PEs**
- **Find 5-yr. high PE, low PE and avg. PE**
- **Look for "signature PE" or range**
- **Relative Value**
  - **Current PE / Trailing PE**
  - **Current PE / Projected PE**

Price Earnings History

3 PRICE-EARNINGS HISTORY as an indicator of the future

This shows how stock prices have fluctuated with earnings and dividends. It is a building block for translating earnings into future stock prices.

PRESENT PRICE __47.490__ HIGH THIS YEAR __58.980__ LOW THIS YEAR __46.760__

	Year	A PRICE HIGH	B PRICE LOW	C Earnings Per Share	D Price Earnings Ratio HIGH A ÷ C	E Price Earnings Ratio LOW B ÷ C	F Dividend Per Share	G % Payout F ÷ C X 100	H % High Yield F ÷ B X 100
1	2000	51.3	18.3	1.64	31.3	11.2	0.420	25.6	2.3
2	2001	34.9	17.0	1.61	21.7	10.6	0.420	26.1	2.5
3	2002	34.6	22.1	1.76	19.7	12.6	0.420	23.9	1.9
4	2003	36.0	20.3	1.64	22.0	12.4	0.440	26.8	2.2
5	2004	53.7	35.0	2.24	24.0	15.6	0.525	23.4	1.5
6	TOTAL		112.7		87.4	51.2		125.8	
7	AVERAGE		22.5		21.9	12.8		25.2	
8	AVERAGE PRICE EARNINGS RATIO	17.3			9 CURRENT PRICE EARNINGS RATIO		19.1		

- **High PE of 21.9 and Low PE of 12.8**
- **Average PE of 17.3**
- **Steady growth often commands a higher PE**

Selecting High and Low PE with 10-years of Data

- **Toolkit 5 allows you to look back 10 years in calculating high and low PE**
- **[Alt + M] automatically eliminates the five highest of "High PE" and "Low PE"**
- **Using this approach:**
  - **High PE of 19.4**
  - **Low PE of 11.6**
- **Average PE of 15.5**
- **More conservative than using only last 5 years**

Judgment - Average High/Low P/E		
Clear Outliers	High PE	Low PE
1995	17.3	12.2
1996	16.5	11.8
1997	24.3	13.3
1998	30.9	13.8
1999	32.2	21.0
2000	31.3	11.2
2001	21.7	10.5
2002	19.7	12.5
2003	22.0	12.4
2004	24.0	15.6
Average:	19.4	11.6

Use Section 3 Averages

Use Average From Above

Use Median

Estimated Future High P/E Ratio: 19.4
Estimated Future Low P/E Ratio: 11.6

Ok   Cancel

Questions to Ask About PEs

- **Is there a "signature" PE?**
- **How does company's PE compare to industry PE?**
- **Is EPS growth likely to increase or decrease?**
- **Is PE expansion or contraction likely?**
  - **We have higher return with PE expansion – why?**
- **How does PE compare to projected growth? ("PEG" ratio)**
- **Do the quality of earnings (consistency and financial strength) justify a higher PE?**

Sec. 4: Risk and Reward

- **Calculate high price in five years**
  - **(Avg. High PE) x (Est. 5-yr. EPS)**
- **Calculate low price in five years**
  - **(Avg. Low PE) x (Est. 5-yr. low EPS)**
  - **Can use current EPS for 5-yr. Low**
- **Find buy, hold & sell zones**
- **Determine upside-downside ratio**
- **Relative value (Current PE / 5-yr avg PE)**

Risk and Reward

4 Proj. P/E [16.80] Based on Next 4 qtr. EPS [2.83]   Current P/E Based on Last 4 qtr. EPS [2.49]
EVALUATING RISK and REWARD over the next 5 years   PEG=141

Assuming one recession and one business boom every 5 years, calculations are made of how high and how low the stock might sell. The upside-downside ratio is the key to evaluating risk and reward.

A HIGH PRICE -- NEXT 5 YEARS
Avg. High P/E _____21.9_____ X Estimate High Earnings/Share _____4.69_____ = Forecast High Price $ _____102.7_____ (4A1)
             (3D7 as adj.)

B LOW PRICE -- NEXT 5 YEARS
(a) Avg. Low P/E _____12.8_____ X Estimated Low Earnings/Share __2.24__ 2.49__ = $ _____31.9_____
              (3E7 as adj.)
(b) Avg. Low Price of Last 5 Years = _____22.5_____
                                      (3B7)
(c) Recent Severe Market Low Price = _____20.3_____
(d) Price Dividend Will Support   Present Divd. = _____0.800_____ = _____32.4_____
                                  High Yield (H)   0.025
Selected Estimate Low Price   = $ _____31.9_____ (4B1)

C ZONING
__102.7__ High Forecast Price Minus __31.9__ Low Forecast Price Equals __70.8__ Range. 1/3 of Range = __17.7__
  (4A1)   (4B1)   (C)   (4CD)
(4C2) Lower 1/3 = (4B1) __31.9__ to __49.6__ (Buy)   Note: Ranges changed to 25%/50%/25%
(4C3) Middle 1/3 = __49.6__ to __85.0__ (Maybe)
(4C4) Upper 1/3 = __85.0__ to __102.7__ (4A1) (Sell)
Present Market Price of _____47.490_____ is in the **Buy** Range
                                                          (4C5)

D UP-SIDE DOWN-SIDE RATIO (Potential Gain vs. Risk of Loss)
High Price (4A1) __102.7__ Minus Present Price __47.490__
                                                              = __55.2__ = __3.5__ To 1
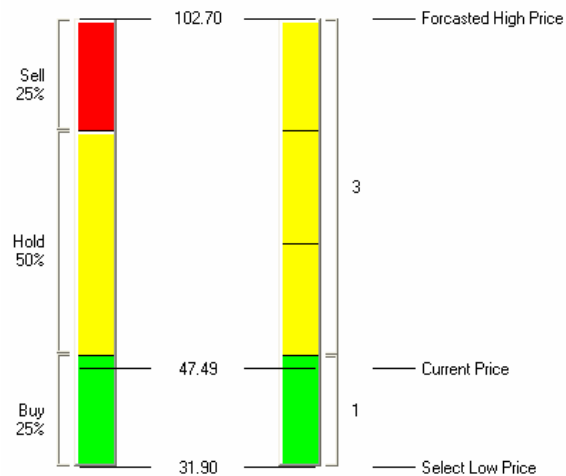Present Price __47.490__ Minus Low Price (4B1) __31.9__   15.6   (4D)

E PRICE TARGET (Note: This shows the potential market price appreciation over the next five years in simple interest terms
High Price (4A1) __102.7__
                            = (__2.163__) X 100 = (__216.3__) - 100 __116.3__ % Appreciation
Present Market Price __47.490__   (4E)

Upside / Downside

Buy – Hold – Sell Range

Sec. 5: Five-Year Potential

- **Average Total Annual Return**
  - **Assumes stock reaches projected <u>high</u> PE in year 5**
  - **Easy to calculate**
- **Compound Total Annual Return***
  - **Assumes stock reaches projected <u>high</u> PE in year 5**
  - **More complex calculation**
- **Projected Average Return***
  - **Assumes stock reaches projected <u>average</u> PE in year 5**
  - **Also a complex calculation**

  * Both Toolkit and Stock Analyst compute these

Five-Year Potential

Relative Value: 110.4% Proj. Relative Value: 97.1%

5 5-YEAR POTENTIAL   This combines price appreciation with dividend yield to get an estimate of total return. It provides a standard for comparing income and growth stocks.

Note: Results are expressed as a simple rate; use the table below to convert to a compound rate.

A Present Full Year's Dividend $ ___0.800___

Present Price of Stock $ ___47.490___ = ___0.017___ X 100 = ___1.7___ Present Yield or % Returned on Purchase Price
(5A)

B AVERAGE YIELD OVER NEXT 5 YEARS

Avg. Earnings Per Share Next 5 Years ___3.64___ X Avg. % Payout (3G7) ___25.2___ = ___91.7___ = ___1.9___ %
(5B)

Present Price $ ___47.490___

C ESTIMATED AVERAGE ANNUAL RETURN OVER NEXT FIVE YEARS

5 Year Appreciation Potential (4E) ___116.3___

	P.A.R.	Tot. Ret.
Average Yield	1.5%	1.2%
Annual Appreciation	11.4%	16.7%
% Compd Ann Rate of Ret	12.8%	17.8%

5 Year Appreciation Potential (4E) 116.3 ÷ 5 = 23.3 %

Average Yield (5B) .... 1.9 %

Average Total Annual Return Over the Next 5 Years (5C) 25.2 %

Return includes 1.5% dividend

- **Projected Average Return of 12.8% is based on average PE**
- **Total Return of 17.8% is based on average high PE**

12 Month Price History

CARNIVAL CORP   as of 7-Oct-2005

CCL
50-day MA
200-day MA

Volume

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Carnival Corp. Conclusions

- **Carnival is a <u>quality stock.</u>**
  - **Value Line financial strength is B+ and earnings predictability is 80, and RQR is 69.6**
- **More likely to go up than down**
  - **Upside/Downside ratio of 3.5**
- **Fully priced**
  - **Relative value = 110**
- **Return:**
  - **Total Return of 17.8%**
  - **Projected Average Return of 12.8% (using average PE of 17.4)**

Conclusion

- **Email: tyhughes@gmail.com**
- **This presentation and SSG can be found at: www.tyhughes.net/moosepond**

Better Investing!