
Opportunity for More Value at Coffey?

The board of directors at Coffey International (COF) have done a good job obtaining a \$0.425 per share offer for the company from Tetra Tech, Inc (NasdaqGS TTEK). But we think the business is worth more.

Whilst it's true that the offer is at a 130% premium to the prior share price, that price was itself at a *huge* discount to fair value (thus our original investment). This is in fact an excellent deal for Tetra Tech. There is huge strategic worth in Coffey's business, within both the geoservices consulting segment and the government international aid development business, and Tetra Tech are getting it for a very attractive price. Excluding corporate overheads, Tetra Tech are paying just 6 times EBITDA for Coffey's business at a low point in its earnings cycle. Tetra Tech itself trades on 10 times EBITDA.

That's some difference, and Tetra Tech's valuation multiple doesn't factor in any premium for control, which is typically 20-30%.

We are also disappointed that the deal doesn't involve distribution of \$0.054 per share in available franking credits to Coffey shareholders. Those tax credits have enormous value to shareholders, as Coffey management have themselves pointed out to us many times, and our understanding from previous correspondence with the finance director is they can be paid out. Retained earnings in the parent entity of Coffey are sufficient to cover the required dividend.

The excuse being put forward for not paying out the franking credits is that consent would be required from Coffey's unsecured lenders. That sounds like a small hurdle to us that a motivated corporate adviser could overcome. It's also been suggested to us that Tetra Tech may value the franking credits. If this is indeed the case, then shareholders should be paid for them (we didn't notice any recognition of this value in the expert's report).

We recognise the business has its challenges, and that it may be worth more as part of a larger corporation, but we own a valuable asset. Weighing up the offer price and the lack of franking credits, we think more value should be attained for shareholders.

There are risks to not accepting this offer, of course. If we don't accept it and Tetra Tech walk away, the business might need more shareholder capital. It has too much bank debt and a raising might be required to realise value in the long term.

If we don't accept the offer and Tetra Tech waive their minimum 90% acceptance condition, we could end up minority holders in an illiquid company. Given the turnaround we foresee in Australian infrastructure spend, that may be no bad thing for long term investors, but it is not ideal.

We are weighing up all of these issues and will posit some more concrete thoughts next week. If you are a fellow Coffey shareholder, feel free to get in touch.