# RESEARCH REPORT

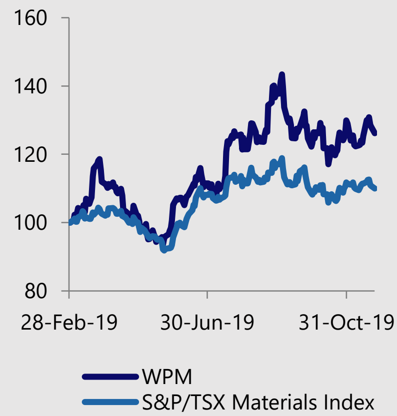
November 25, 2019

| | |
|---|---|
| Stock Rating | HOLD |
| Price Target | $37.30 |

| Bear Case | Price Target | Bull Case |
|---|---|---|
| $32.32 | $37.30 | $44.95 |

| | |
|---|---|
| Ticker | WPK |
| Market Cap. (MM) | $2,993 |
| EV/EBITDA LTM | 9.4x |
| P/E LTM | 19.6x |

## 52 Week Performance





## Metals & Mining

Inaara Panjwani
ipanjwani@quiconline.com

Sebastian Weersink
sweersink@quiconline.com

Alice He
ahe@quiconline.com

Shivam Aggarwal
saggarwal@quiconline.com

Matthew Kampe
mkampe@quiconline.com


# Winpak Ltd.

# Packed with Potential

Winpak is one of the leading North American plastics packaging companies, with what appears to be a strong and defensible business model at first glance. The Metals & Mining team was originally drawn to the name as a top player in our packaging universe, a subsector that we see as providing attractive diversification away from commodity pricing risks. In this report we will analyze and investigate our initial investment theses for the company, namely:

(1) The Company's entrenched position as a market leader with a blue-chip customer base selling into the highly attractive food and healthcare end markets

(2) Winpak's tangible competitive advantages it has generated over time through superior R&D spending

(3) A strong runway for both organic and inorganic future growth, backed by a rock-solid balance sheet

(4) A unique ownership structure that gives them some of long-termism advantages of a private company

We also look at several key risks that could threaten Winpak's business and perform a valuation of the business.

## Table of Contents

## Company Overview

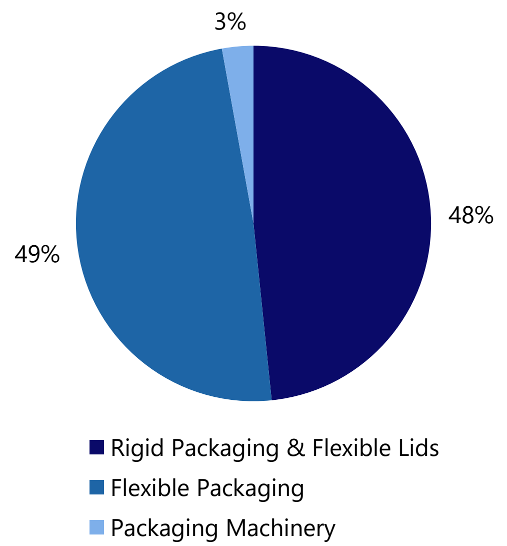
Winpak Ltd. ("Winpak" or "the Company") is a Winnipeg-based manufacturer and distributor of plastic packaging materials and machines. Their products are primarily used in the production of perishable food and beverages as well as in the healthcare industry. Winpak was founded in 1978 in Winnipeg, originally as Wihuri. The company operated a single flexible packaging facility in Winnipeg and was a wholly owned Canadian company when it IPO'd on the Toronto Stock Exchange (TSX:WPK) in 1986. The company has three main operating segments: Rigid packaging and flexible lidding, flexible packaging, and packaging machinery. The Company's products are primarily used for the packaging of perishable foods and beverages, which accounted for more than 90% of its sales for FY 2018 and FY 2017. The other segments including medical, pharmaceutical, personal care, industrial, and other consumer goods.

The rigid packaging and flexible lidding segment is further segmented into the rigid containers and lidding product groups. This segment creates plastic cups, trays and sheets, retort and customer containers, as well as flexible lidding materials, daisy chain, die-cut, and rollstock lidding. This business segment operates principally in the United States and Canada, accounting for 97% of its revenue. Rigid packaging and flexible lidding accounted for $430mm of revenue for FY 2018, with a negligible decrease in volumes.

The flexible packaging segment includes the modified atmosphere packaging, specialty films and biaxially oriented nylon product groups. This segment creates barrier shrink bags, modified atmosphere bags, specialty films, zipper stand-up pouches, vacuum pouches, and foil lamination. Flexible packaging generated $433mm of revenue during 2018, with an increase in volumes.

**Exhibit I**

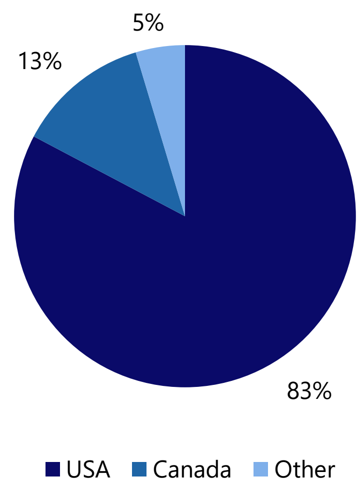
Business Mix




Source: Company Filings

**Exhibit II**

Geographic Breakdown of Sales




Source: Company Filings

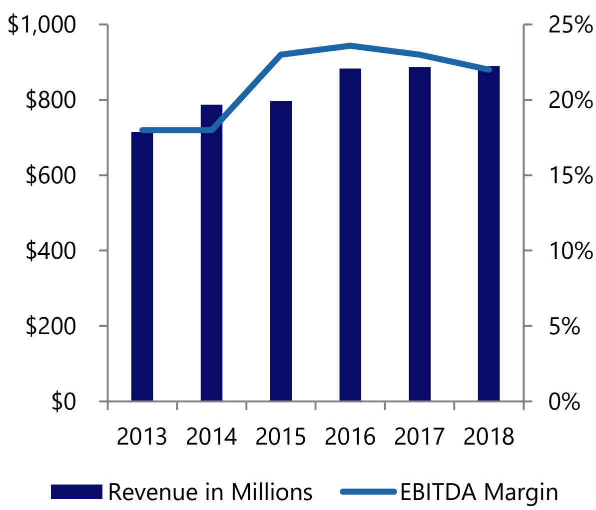
## Company Overview

The packaging machinery segment is the smallest reporting segment for Winpak. This segment creates pouch and cup machines, unifill, packaging systems, replacement parts and unifill press release. Packaging machinery drove $25mm in sales, accounting for only 2.85% of sales and accounting for 3.3% of its plants, property, equipment and intangible assets.

Winpak between its IPO in 1986 to 2000, undertook significant merger and acquisition (M&A) activity, acquiring more than five major companies for a total of $122mm. This series of M&A activity enabled Winpak to expand its production facilities and give it scale to compete internationally. Since 2000, Winpak has slowed its M&A activity, only making two major acquisitions. In 2002, the Webkote division of Fleming Packaging was purchased and the Walsroder Packaging division of Dow Chemical was bought in 2008. These two aforementioned deals were made to expand Winpak's product portfolio.

**Exhibit III**

Revenue Growth




Source: Company Filings

Winpak has an unconventional ownership structure as they are majority (52.5%) owned by Finnish conglomerate Wihuri International Oy. Wihuri also owns the European based Winpak company. This ownership structure creates operational and financial advantages for Winpak as they gain an international exposure and larger client base via Wihuri as well as financing options. Winpak shareholders on the other hand face significant downsides to this governance structure as it is unfriendly to institutional investors, leading to difficulty in improving the valuation. Furthermore, there are large barriers to entry for any financial sponsor looking to acquire the firm as they will have to negotiate with both public shareholders and Wihuri.

**Exhibit IV**

Example Flexible Packaging Products


Source: Company Website

## Industry Overview

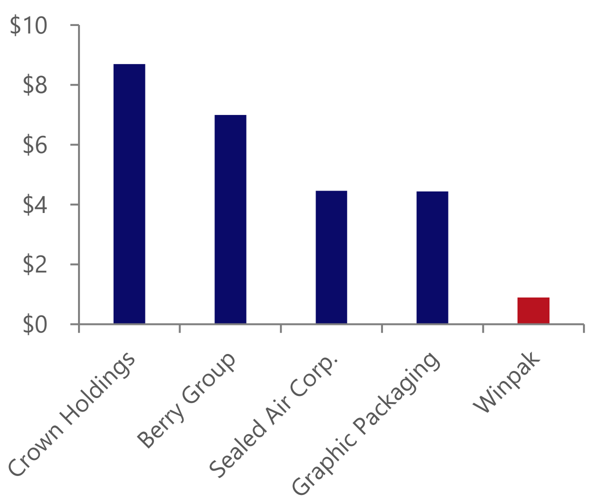
Firms in the packaging industry manufacture and sell materials and equipment used in the packaging process for customers, typically in the food & beverage, industrial, and healthcare industries. The global packaging industry is highly fragmented, with over 10,000 firms in North America alone providing solutions for a wide variety of packaging needs. The largest North American competitors include Crown Holdings, Berry Group, Sealed Air Corporation and Graphic Packaging International, with revenues of $8.69B, $7.0B, $4.46B and $4.4B, respectively. The Canadian packaging manufacturing industry is fairly mature and concentrated among a few leading players. The three major players are also the largest packaging companies in the M&M coverage universe which are Intertape Polymer Group, CCL Industries and Winpak.

The industry's end markets, primarily perishables, is directly tied to overall economic growth and as a result, the packaging industry is too. Winpak has experienced above-GDP growth over the past ten years accomplished by improving market share through cross-selling its products, as well as entering new markets.

The largest packaging companies are generally geographically diversified, with a broad mix of revenue for each region. The large players in this space also tend to be more diversified in their product offerings, rather than specializing in food and beverage packaging such as Winpak. Major companies in this sector are also tend to be internationally based, rather than American dominated. European companies are very prevalent and competitive in this sector, accounting for five out of the top ten largest packaging companies globally. The customers for packaging companies tend to be more concentrated, as large consumer packaged goods (CPG) companies are major customers to many of the players. The customer base of these companies generally are composed of several large CPG companies, followed by hundreds of very small niche companies. Winpak's largest customer for example accounts for 16% of sales in 2018, down from 18% in 2017. This results in packaging companies being very reliant on securing major contracts or else risk major sales declines.

**Exhibit V**

Winpak Revenue vs. International Peers




Sources: Company Filings, S&P Capital IQ

**Exhibit VI**

Example of Winpak's Portion Packing Products

Source: Company Website

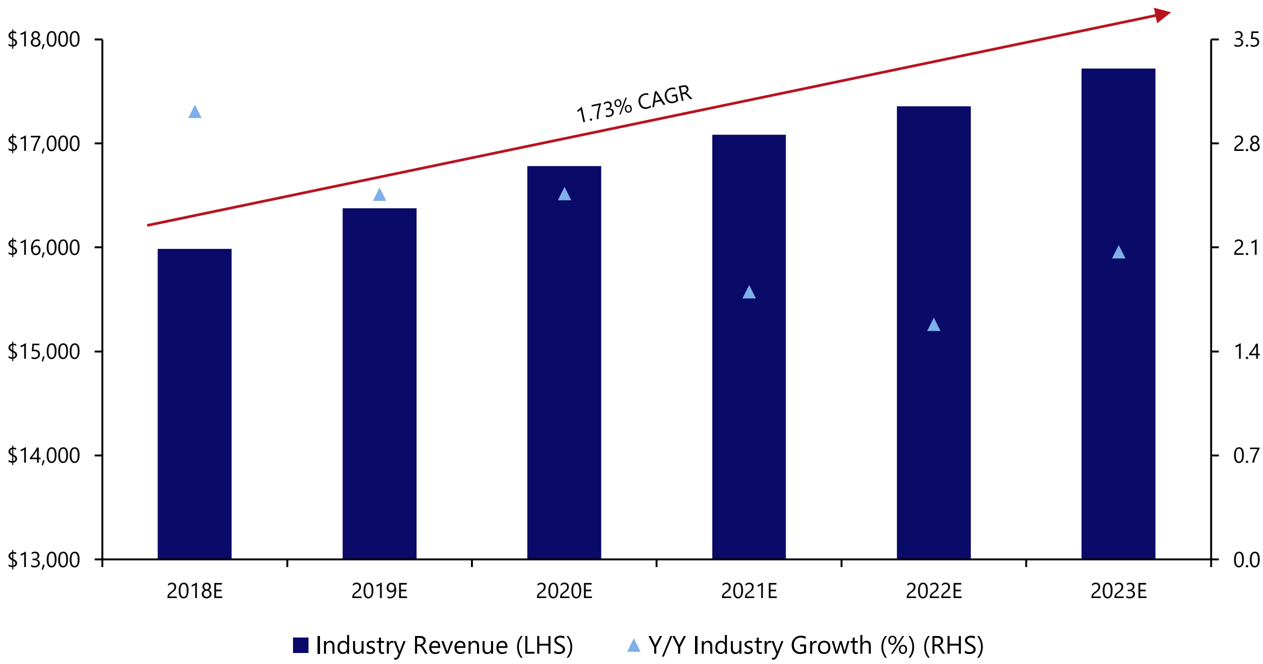
## Industry Overview (cont'd)

Packaging is a highly commoditized and relatively stable industry, with revenues showing little correlation to broader economic trends. Despite being a commoditized business, technology and innovation do play a larger role in certain customers' buying criteria. Healthcare and higher-end products in other categories often demand specific technical requirements for safety and aesthetic reasons. Large amounts of revenues are generated from health care and other non-discretionary items such as packaged foods, where volumes tend to remain stable throughout recessionary periods. Demand for a certain portion of packaging revenues is attributable to more discretionary items and is hence driven by consumer spending patterns. Outsourcing activities from firms subject to heavy regulatory burdens, such as pharmaceuticals and food manufacturing, is a significant growth driver. It is often easier for large firms in these industries to outsource their packaging to specialized firms to minimize risk and costs. Another growth trend is e-commerce. For smaller online merchants, outsourcing packaging is a viable way to reduce costs and maintain a lean physical footprint to optimize overhead.

The firms best positioned to generate outsized returns in this industry will have scale, a technological advantage, and sound management that is aligned with shareholders and experienced. Winpak exerts each of these elements and is well positioned to capitalize on future growth and consolidation.

**Exhibit VII**

Packaging Materials and Machinery Industry Growth




Source(s): Company Filings, S&P Capital IQ

## Management Overview

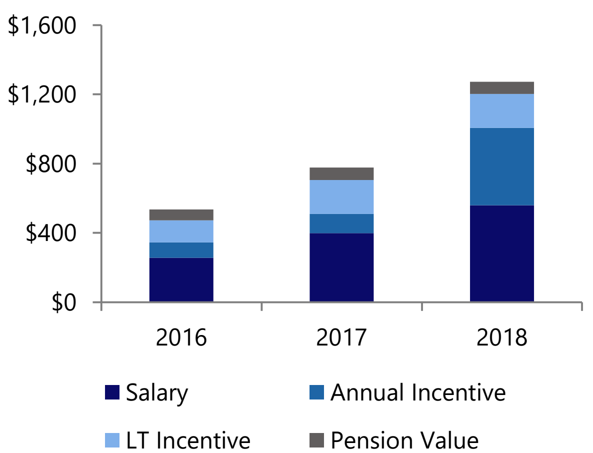
The family-owned Finnish conglomerate Wihuri Oy holds a 52.5% stake in Winpak, giving them effective complete control of the Company. As a result, the majority of the Board of Directors, six of nine members, is made up of high-ranking executives from Wihuri. In part owing to the unique stability at the Board level, Winpak has only had three CEOs since it's founding in 1977. Bruce Berry served as Winpak's President and CEO for over 13 years before retiring in 2017 and is now a member of the Board of Directors. Upon Bruce's retirement, Olivier Muggli was appointed President and CEO, roles that he continues to hold. Prior to being appointed President and CEO, Mr. Muggli had worked at Winpak for six years and was most recently the COO. Additionally, Mr. Muggli has significant experience in the packaging and CPG industries, having worked in various senior management roles at a variety of firms,

Other notable executives include CFO Larry Warelis, who has worked at Winpak in the corporate accounting and treasury division since 1997. Winpak's other key Named Executive Officers are the Presidents of the Company's three primary business lines: James Holland, Timothy Johnson and David Stacey, who are Presidents of Winpak Division, Winpak Heat Seal and Winpak Portion Packaging respectively. All division Presidents have been with the Company for at least 14 years and have been promoted internally within their respective divisions.

Executive compensation at Winpak is unique in the Company's lack of use of equity awards as a compensation method. This is due to the unwillingness of Wihuri to issue the additional shares required to award stock options. Thus, for all NEOs, all compensation is cash based, with around half of compensation derived from base salaries. The majority of bonuses take the form of an annual incentive plan based on management's ability to hit yearly EBT targets, with remaining compensation based on achievement of a 4-year EBT CAGR target of 6%.

**EXHIBIT VIII**

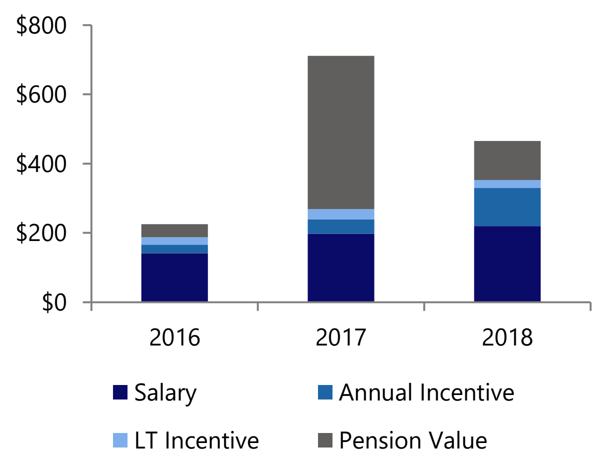
Oliver Muggli Compensation Mix (USD '000s)




Source(s): Company Filings

**EXHIBIT IX**

Larry Warelis Compensation Mix (USD '000s)




Source(s): Company Filings

## Thesis I: Non-Cyclical and Captive End-Markets

Whereas other players in the industry such as CCL Industries and Intertape Polymer offer a breadth of products (see EXHIBIT X), Winpak has strategically narrowed its focus to provide niche products in the plastics packaging segment. The result is that, despite not being the largest player in the packaging industry by market cap or revenues, Winpak has developed strong customer relationships in favourable plastics packaging end-markets.

Across North America, Latin America, Pacific Rim, and Europe, Winpak operates three key segments of rigid packaging and flexible lidding, flexible packaging, and packaging machinery (see EXHIBIT XI). The company's products across these segments are primarily utilized by two distinct end markets: perishable foods and beverages companies looking to preserve with packaging (accounting for 90 per cent of sales during 2018 and 2017), and the healthcare industry (including medical and pharmaceutical end uses). The remainder of its sales are comprised of end users in personal care, industrials, and other consumer goods industries.

The fact that the majority of Winpak's end-users belong to the perishable food and beverage industry, as well as the healthcare industry presents a major advantage in demand-stability, pricing power, and recurring revenue potential. Since Winpak is predominantly exposed to inherently non-cyclical end-markets such as food and beverage and healthcare, its demand is relatively stable across economic cycles. Additionally, both packaging for medical and perishable food products must meet stringent requirements and stringent regulatory approvals, given that patient and consumer safety, respectively are major concerns. Global regulatory bodies in the medical and perishable foods space, such as Health Canada, the US FDA, and European Medicines Agency require sophisticated labels that disclose significant amounts of potential information; as well, any packaging used by either sector must be sterile.

Barriers to entry for healthcare or medical products is typically significantly increased by the lengthy regulatory approval processes. Ultimately, for end users, it becomes a challenge to find suppliers who can reliably and cost-effectively fulfil these strict regulatory requirements. Thus, upon finding a plastics packaging supplier such as Winpak, who can deliver these end-users are limited in their ability to easily switch packaging companies; in turn, suppliers enjoy stickier customer relationships, and higher pricing power. Finally, in examining the perishable food and beverage industry in particular, Winpak's end-users are mainly comprised of "blue-chip" companies (see EXHIBIT XII), which are multinational firms that have been in operation for a number of years and have sustainable cash and revenue flows. This greatly reduces the risks associated with unstable demand.

**EXHIBIT X**

Winpak Versus Competitor Product Portfolio

| | Product Category | | | |
|---|---|---|---|---|
| ***Company*** | Plastic | Labelling | Metal & Glass | Paper |
| Winpak | YES | NO | NO | NO |
| CCL Industries | YES | YES | YES | NO |
| Intertape Polymer Group | YES | YES | NO | YES |

Source(s): Company Filings

**EXHIBIT XI**

Winpak Product Mix

| ***Operating Segment*** | End Market |
|---|---|
| Rigid Packaging and Flexible Lidding | Food, Dairy, Beverage, Healthcare and Industrial |
| Flexible Packaging | Food, Beverage, Healthcare and Industrial |
| Packaging Machinery | Food, Beverage, Healthcare |

Source(s): Company Filings

## Thesis I: Non-Cyclical and Captive End-Markets (cont'd)

In examining the nature of Winpak's customer relationships, there are other favourable characteristics worth noting. First, Winpak works closely with and embeds itself into its customers' operations through customized resin blends and its proprietary co-extrusion process. By integrating itself into client operations, Winpak can increase its ability to capture recurring business. In addition the majority of Winpak's revenue is comprised of customer contracts spanning two to five years, which include volume clauses or price incentives for higher volume. The result is that Winpak can lower customer turnover and enjoy relatively predictable revenues. It is important to note the risk that Winpak faces owing to the significant customer concentration of its contracts. Specifically, Winpak's ten largest customers accounted for around 35% of revenues in 2017; in 2018, its largest customer comprised 16% of revenues. Significant customer concentration holds the potential to limit pricing flexibility or hurt operating performance if the customer faces its own business or financial challenges.

**EXHIBIT XII**

Winpak's "Blue Chip" Customer Base

| **Winpak Sample Customers** | |
|---|---|
| Cargill | Natrel |
| Dnanone | Parmalat |
| General Mills | Schreiber Foods |
| Heinz | Smithfield |
| Kellogg's | Maple Leaf |
| Keurig Green Mountain | Mars Petcare |
| Kraft Foods | |

Source(s): CIBC World Markets, Company Filings

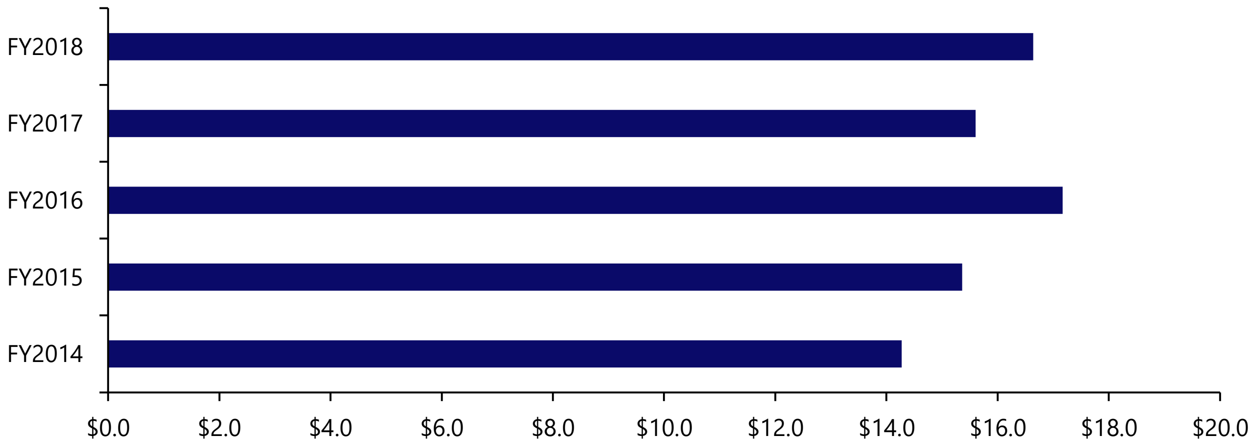
## Thesis II: Continuous Investment in Innovation and R&D

In recent years, Winpak has made sustained and growing investments in research and development. The resulting innovations have generated significant cost savings while increasing Winpak's pricing power in the plastics packaging space through product differentiation. Namely, Winpak has piloted several innovative products such as Semi-Rigid Films and the Horizontal Flowpak for dairy and protein packaging.

However, the most notable of Winpak's innovations is its proprietary conversion equipment and the multi-barrier films that said equipment is able to create. For the proprietary equipment, Winpak has developed in-house, co-extrusion techniques to produce highly engineered, multilayer plastic films. Without the need to bond multiple layers of film, processes can extrude up to 13 layers at a time. The proprietary equipment is thus used to create industry-leading films with thermoforming properties that is useful to perishable foods and beverages packaging as well as medical applications. For Winpak, the business impacts of the proprietary technology are two-fold, the first being that it generates significant cost savings among materials, energy, capital, and labour. In 2018, for example, Winpak's Winnipeg, Manitoba facility utilized the proprietary conversion equipment in its manufacturing process; the step-ups in productivity and quality consistency have been instrumental in mitigating the impact of raw material price increases and maintaining low-costs. Second, the proprietary technology allows Winpak to move beyond the commodity, low-tech product space towards that which is differentiated and has higher-margins. Companies in the perishable foods and beverages space have a clear economic rationale in paying a premium for Winpak's multi-barrier films: the higher cost of superior packaging reduces the costs associated with product foliage.

**EXHIBIT XIII**

Winpak's R&D Investment (In $M USD)




Source(s): Company Filings

## Thesis II: Continuous Investment in Innovation and R&D

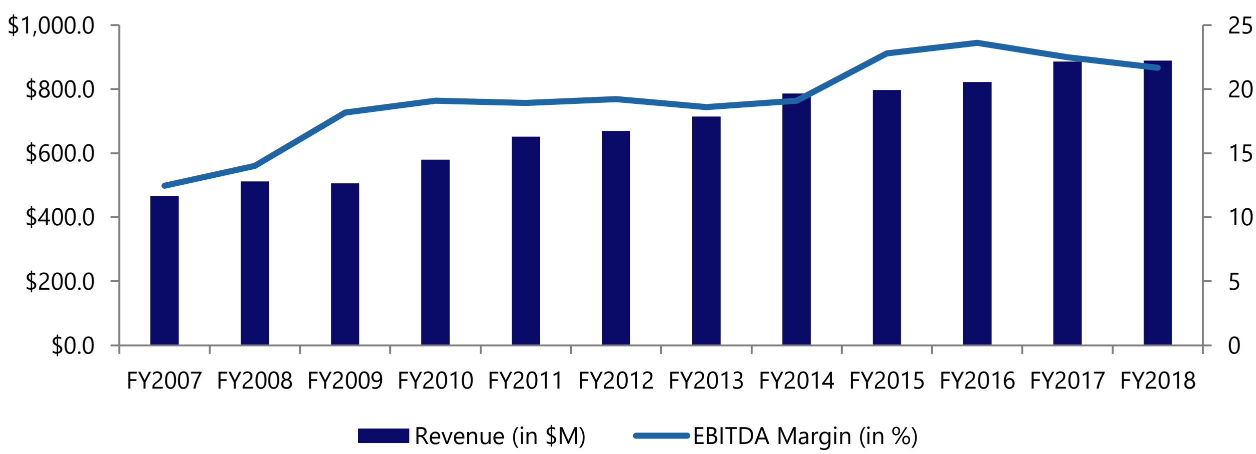
Thus, Winpak is able to command a premium for these packaging products as producers of perishable food, Winpak's primary end-market, prioritize minimizing food waste. In 2018, Winpak invested in additional high-barrier co-extruded blown film capacity at its Winnipeg facilities to keep up with demand; similarly, Winpak's specialty film business in Senoia, Georgia will be proceeding with additional capacity in early 2020 to keep up with demand for sophisticated high-barrier food and medical film.

Arguably, Winpak's ability to continuously innovate as well as command pricing premiums, drive demand, and decrease costs, as a result have yielded favourable results for the company. From 2007 to 2016, the company saw revenues rise at a CAGR of 6%; EBITDA margins too grew at an 11.4% CAGR. Relative to peers in 2018, Winpak's EBITDA margin was noticeably higher, at 21.4% compared to the peer average of 15.5% (see EXHIBIT XIV).

Faced with growing competitive pressures in the packaging space, superior technology provides Winpak with a potential competitive barrier for strong revenue growth, high margins, and robust free cash flow. Further, R&D is extremely capital intensive and requires expertise in a relatively niche sector; Winpak's balance sheet strength and over 30 years of experience builds confidence that ability to continuously innovate can be a sustainable moat for the company. Despite this, in 2018, Winpak cited several key risks surrounding competitive pressures including: changes in pricing, new product development, and increases in capacity; such risks call into question the apparent sustainability of Winpak's competitive advantage.

**EXHIBIT XIV**

Winpak's Revenue and EBITDA Margin




Source(s): Company Filings, S&P Capital IQ

## Thesis III: Runway for Growth

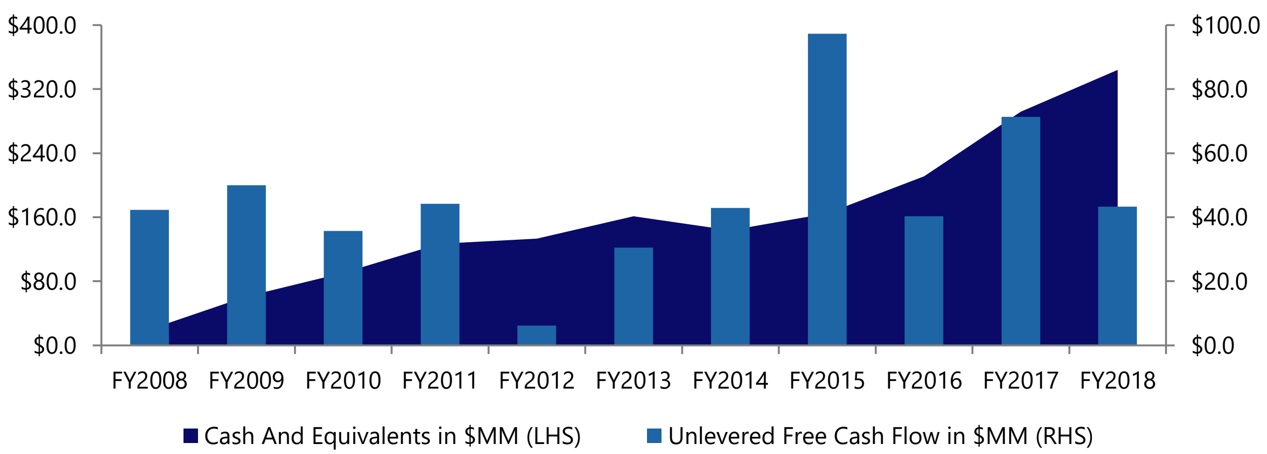
Given its strong balance sheet, Winpak has the capacity to fund future growth; that is, if it can find favourable targets.

Winpak is in an ideal position for growth with no debt on its balance sheet, consistent FCF and a large cash balance. In 2018, the company stated that it was "confident that all 2019 requirements for capital expenditures, working capital, and dividend payments can be financed from cash resources, cash provided by operating activities and unused credit facilities." Winpak is a highly free-cash-flow generative business and has demonstrated its consistent ability to convert revenue into free-cash-flows. In 2018, Winpak generated approximately 95M of UFCF (~11 per cent of revenue and 49 per cent of EBITDA). Cash and cash equivalents in 2018 ended at $344.4M, even though property, plant and equipment additions of $71.2M represented the second highest annual outlay in the company's history (see EXHIBIT XV). In addition to cash, Winpak has a clean balance sheet with no short term borrowing or long term debt outstanding on it and has not for the past ten years. In the event that Winpak elects to finance with debt, it has access to additional facilities, unused operating lines of $38M and access to relatively low interest rates.

For Winpak, the difficulty lies not in financing growth, but rather determining attractive opportunities in which to deploy capital. While management has mentioned its desire to enter the injection moulding market or expand further into the healthcare and packaging market, few projects seem to meet the company's high hurdle of a 20% IRR. And even as cash on hand accumulates, Winpak's dividend payout ratio has remained below 20%, with exception to fiscal years 2014 and 2015, when a special dividend was issued.

**EXHIBIT XV**

Winpak's Cash and Cash Equivalents and Unlevered Free Cash Flow




Source(s): Company Filings, S&P Capital IQ

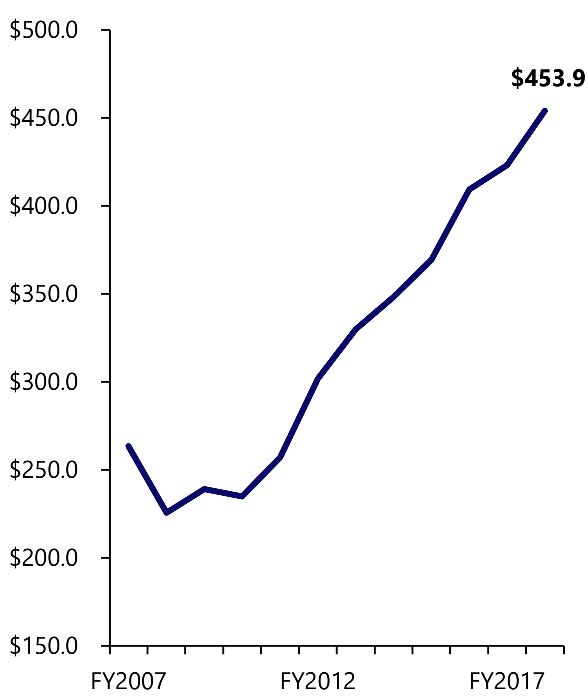
## Thesis III: Runway for Growth

Generally, the projects in which Winpak has chosen to invest remain focused on organic growth opportunities. As of 2018, Winpak has made sizeable investments in capital to expand the manufacturing footprint, reduce manufacturing costs, deploy new technologies, and improve operational performance.

In 2019, as part of Winpak's organic growth initiatives, capital expenditures are forecasted to attain approximately $70M to $80M due to increased in extrusion capacity at the rigid container facility in Sauk Village, Illinois, and a new Mexican plant which will accommodate increased production capacity and new capabilities in printing technology for flexible packaging products. Winpak has additionally invested in building expansion and new biaxially oriented polyamide (BOPA) line capacity in Winnipeg, Manitoba, with an anticipated commercial start-up in the latter half of 2020. In 2018, earlier investments in the same organic growth initiatives totalled $71.6M and in 2017, similar plant and equipment additionals represented $72.2M in capital expenditures.

**EXHIBIT XVI**

Winpak's Net Property, Plant & Equipment (in $M)




Source(s): Company Filings, S&P Capital IQ

There are also apparent opportunities for inorganic growth given the highly-fragmented, largely regional packaging industry in the United States. This highly fragmented and localized market is mainly attributable to the low relative value of packaging materials, which limits the range in which packaging products can be economically transported. As a result, certain packaging materials can be moved longer distances due to lower weights and smaller form factors, but packaging production tends to occur in close proximity to manufacturing production.

Given this fragmented industry structure, it is perhaps unsurprising that Winpak's competitors have pursued M&A as avenues for growth in recent years. Namely, in 2018, Intertape acquired protective packaging solutions company, Polyair, to expand its product offerings and usher in approximately $20M in adjusted EBITDA by 2021. In the same year, Intertape acquired Maiweave, a woven packaging producer, to expand its geographic reach into the Southeast US and consolidate its position in the construction end-market. CCL, the dominant player, has developed a successful acquisition strategy of buying out its smaller competitors or mostly private companies which can expand its product line, geography or customer base. CCL has a track record of profitably integrating these acquisitions, without relying on high leverage or dilution to finance growth; at the same time, it has a backbone of internally generated growth.

## Thesis III: Runway for Growth

Historically, Winpak has relied on inorganic growth opportunities. Between 1986 and 1998, Winpak underwent five major acquisitions for a total value of $122M with the purpose of expanding production facilities and international presence (see EXHIBIT XVII). Since then, it has made three strategic acquisitions, acquiring Webkote (in 2002), Walsroder Packaging division of Dow Chemical in 2008 and most recently Control Group (in October of 2019) for $42.2M, funded from cash resources on hand. The rationale for Winpak's most recent acquisition was the potential it provided in terms of reinforcing Winpak's global service model and product portfolio dedicated to the pharmaceutical and medical markets.

While management has not made any obvious indications that Winpak will be pursuing inorganic growth opportunities, it has stated that they are always looking for acquisition targets that would provide new technologies or capabilities to offer expanded products. With Winpak's strong financial position, the Company will continue to evaluate acquisition prospects that strategically fit and align with its core competencies in sophisticated packaging for food, beverage and health care applications.

**EXHIBIT XVII**

Winpak's Acquisition History

| Year | 1992 | 1993 | 1996 | 1997 | 1998 | 2002 | 2008 | 2019 |
|---|---|---|---|---|---|---|---|---|
| Acquisition Target | PNG products Inc. | Consumers Packaging | W.A. Lane Companies | Heat Seal Packaging Inc. | Flex-On Inc. | Webkote Division of Fleming Packaging | Walroder Packaging Division of Dow Chemical | Control Group |
| Business Type/ Product Group | Flexible packaging and material conversion | Rigid plastic packaging and container systems | Packing filling machines | Rigid container systems, heat sealable membranes, and die-cut lids | Flexible packaging, multilayer specialty film extrusion and conversion | Rigid container systems and die-cut foil lidding | Flexible packaging and film packaging | Printing packaging solutions to pharmaceuticals, healthcare, nutraceutical, cosmetic, and personal care markets |

Source(s) CIBC, Company Filings

## Theses IV: Unique Ownership Structure

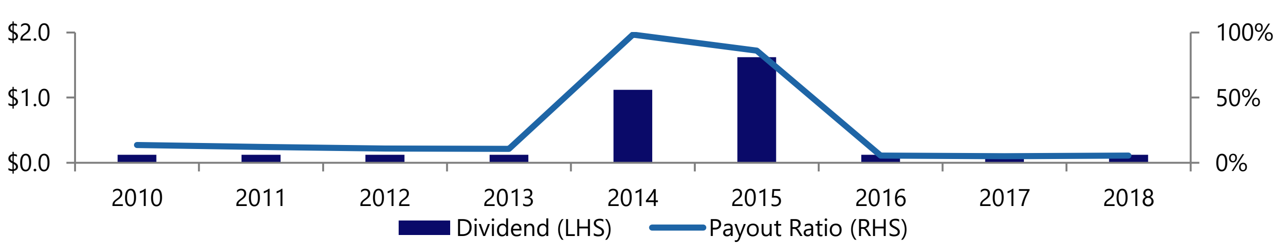
As mentioned earlier, Winpak has an extremely unique ownership and resultant governance structure for a public company. The Company has had 65M common shares issued and outstanding since 2005 when the company completed a ten-for-one share split. Since 2005, Wihuri Oy and its Chairman, Antti I. Aarnio-Wihuri, have owned 34,115,300, or 52.5%, of the Company's shares. Given that every share has equal voting and dividend rights, Wihuri has effective complete control over Winpak through his control of the Board of Directors. Additionally, this means that only 47.5% of the Company's shares are publicly floated and actively traded.

Wihuri is the largest family-owned business in Finland and has four main business lines: (1) Technical Trade, which produces a variety of industrial products, (2) Jetflite, which provides private aircraft services in the EU, (3) Wihuri Oy Aarnio, one of the largest wholesalers of consumer staples in Finland, (4) Packaging, comprised of Winpak and its sister company Wipak. The only business segment that is of any consequence to Winpak is Packaging, as the other business lines are effectively completely removed from the Company. Wipak is functionally a very similar company to Winpak, with both providing high-end solutions primarily to food and healthcare end markets. However, Wipak is located in Europe, with 11 facilities across the EU, Asia and the Middle-East and is additionally not publicly listed. While the two companies do operate separately, they have a strong strategic alliance under the Wihuri umbrella which provides significant benefits to Winpak. This alignment with Wipak allows Winpak to benefit from increased economies of scale and an ability to provide globalized customers a consolidated packaging solution. The latter is especially important as both company's customer base becomes increasingly globalized.

The true uniqueness of Winpak's ownership structure is that it means that the company is effectively run like a private company in that it is relatively free from being forced to respond to market pressures. The Company and its owners have long emphasized the long-term approach that they take to the growth and development of the business. One area that this can be tangibly observed is in Winpak's approach to dividends. The Company has issued the same dividend of C$0.12 per share annually for the past nine years, representing a payout ration of less than 10% most years. Considering Winpak's significant cash balance, it would likely be difficult to pay such an insignificant dividend if they were fully subject to the pressures of the public markets. The Company and its owners believe that it is more beneficial for shareholders if the Company's cash is re-invested in the business.

**EXHIBIT XVIII**

Total Dividend Paid by Winpak and Payout Ratio (2010-2018)




Source(s): Company Filings, S&P Capital IQ

## Theses IV: Unique Ownership Structure

While Winpak doesn't issue a large regular dividend, it has issued several special dividends in the past, most recently in 2014 and 2015. This flexibility in dividend policy allows the Company to return cash to shareholders when it wants to and invest it when there are projects that provide an adequate return. Winpak being part of Wihuri has the added benefit of providing the Company with extra access to capital should it be required.

Winpak has been historically quite effective at allocating capital prudently, due in large part to the long-termism adopted by its owners. Wihuri has done a good job of hiring strong management teams that have been able to grow the business organically. At the same time, these management teams have had the added freedom of stability at the Board level and the knowledge that they will be safe in allocating capital for the long term. This capital allocation has resulted in a 15-year average ROIC of 11.6% and impressive revenue and margin growth over the same period. Thus, we see strong capital allocation at Winpak as the result of this symbiotic relationship between management and Wihuri.

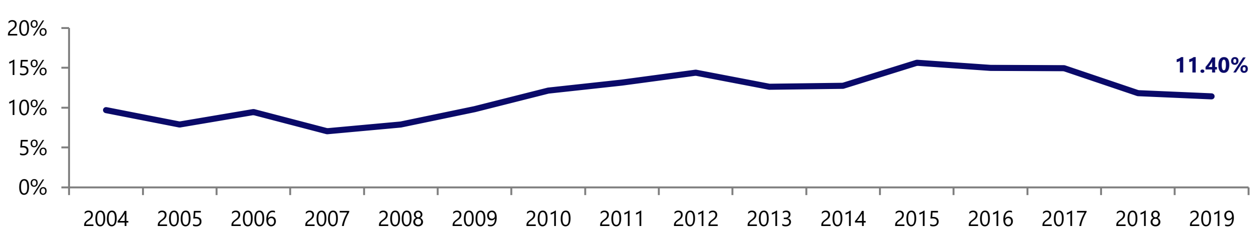
While this ownership structure evidently offers some significant benefits to Winpak, it also has some definitive drawbacks and significant risks. The primary downside of this structure is the reduced public float and the resultant effect on the stock's liquidity. Based on the 3-month average daily volume, 0.06% of Winpak's outstanding shares are traded on a daily basis, compared to 0.16% and 0.18% for Cascades and CCL respectively. The stock's reduced liquidity and the lack of control afforded to shareholders prevents some large institutional investors from investing in the Company, potentially providing a drag on share price performance.

There are other risks that are inherent with such a large single shareholder. The primary concern for shareholders is if Wihuri begins to act in a way that is not aligned with shareholders. While this is unlikely to happen, it could have potentially catastrophic consequences. There is the usual conglomerate risk of excessive meddling in the business by executives with little understanding of what they are doing, something we see as unlikely given Winpak's long history as a part of Wihuri. Last, succession risk is a very real threat given that Antti I. Aarnio-Wihuri is 79 years old. It is expected that his children will take over the family business when he moves on from it, but it is difficult to tell what the business would look like under their stewardship.

On the whole, despite several risks and drawbacks, we believe Winpak's unique ownership structure is a net advantage for the Company.

**EXHIBIT XIX**

Winpak Historical ROIC (2004-2019)




Source(s): Bloomberg, Company Filings

## Additional Risks and Considerations

**Competitive Pressures**

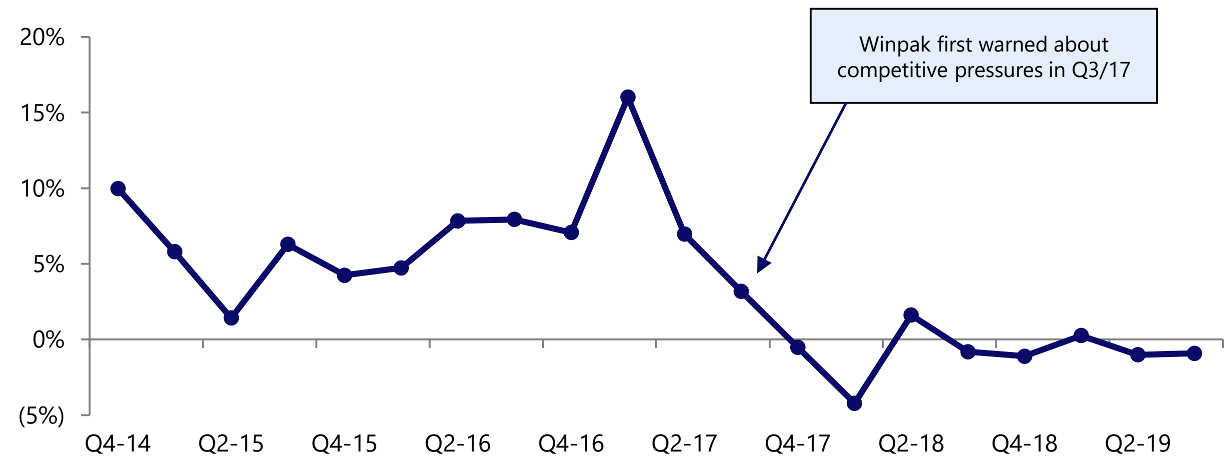
Winpak's management has been warning about an increasingly competitive environment since Q3/17. While they have been highly unspecific regarding the segment and source, sales volume stagnation has been very evident since. This risk is partly limited by Winpak's high customer retention, justified by the customer relationships and switching costs its has established. However, a recently lost retort tray business which has effected results for the last two quarters indicates that these pressures are persisting. Furthermore, this substantial drop in volume growth due to competition raises concerns around the defensibility of Winpak's customer relationships.

**Sustainability Issue of Single-Use Plastics**

Trudeau's expected single use plastics ban has not been put into execution yet, however, it appears it will target items outside the scope of pre-packaged goods such as such as grocery bags, straws, stir sticks, and cutlery. Nevertheless, consumer sentiment around reducing plastic waste has been strong and growing in recent years and could influence demand for plastic packaged products or drive producers to seek sustainable alternatives. With its majority investor positioned in Finland, Winpak has a highly detailed sustainability plan and is focused on driving use of scraps and recycled inputs into its production, producing lighter and less material-intensive packaging, using less harmful plastics, and producing a greater mix of commercially recyclable products. It has also experimented with compostable packaging in R&D although the limited facilities in North America that process compostable plastics pose limitations to growth in this field. With these initiatives in place, we believe Winpak is well-positioned against its competitors to offer increasingly sustainable packaging solutions in the future. However, it may face volume pressure if consumer movements towards locally sourced and sustainably packaged goods become substantial.

**EXHIBIT XX**

Historical Volume Growth




Source(s): Company Filings, TD Securities Inc.

## Additional Risks and Considerations

**Raw Material Prices**

Similar to other plastic packaging companies, Winpak is exposed to cyclical raw material inputs which comprise of ~60% of cost of goods sold. Its raw inputs primarily consist of resins which are natural-gas and petroleum based. Winpak has hedging mechanisms in place, such as price-indexing agreements with certain customers enabling them to adjust selling prices with raw input cost changes with a 90 to 120-day delay. These agreements apply to the majority of their products, creating some degree of security, although margins will nevertheless be impacted when there are cost changes. From speaking with a portfolio manager at Sionna Investment Managers in the past about their position in Winpak, we have gathered that resin price fluctuations could represent an opportunity to favourably enter or exit the name, since they are short-term in nature and can influence share price.

**NAFTA and Tariff Exposure**

The majority of Winpak's products are sold to customers in the US followed by Canada and Mexico. Approximately 61% of production costs occur in Canada and export sales from these manufacturing facilities into the US represent ~40% of the Company's revenues. Under the current NAFTA agreement, all packaging materials move across the borders between Canada, the US and Mexico free of duties. However, this high exposure to trade between the US and Canada leaves Winpak vulnerable to border tax adjustments or amendments to NAFTA in the long-run. There are currently no proposed NAFTA changes impacting Winpak that we are aware of but it is important to monitor.

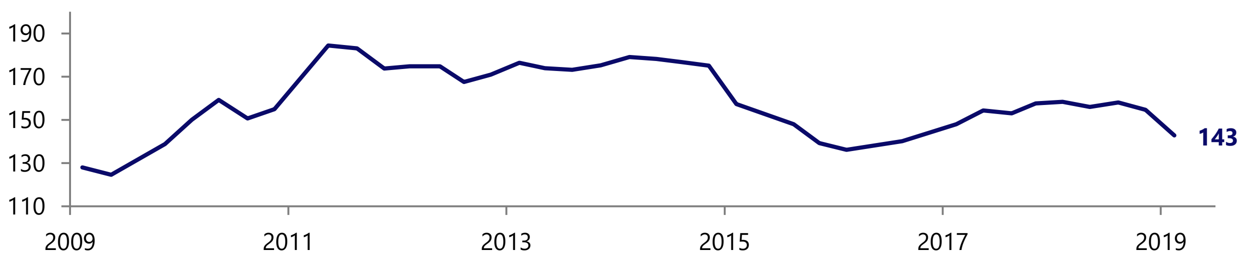
Winpak claims to mitigate this risk through its anticipated ability to increase production capabilities in the US if required, however, the specialized nature of each of its plants appears to limit capacity to do so. For example, Winpak was impacted by the 10% US aluminum tariff increase that commenced in March 2018. The tariff impacted its flexible foil lidding products which are currently exported from Canada to the US. However, no production was reported to have shifted to reduce this impact.

**Customer Concentration**

Winpak has a relatively fragmented customer base compared to its peers, however, impact from a large customer leaving or performing poorly could nevertheless be substantial. Its largest customer contributes ~16% of total revenues and as of 2017, the top 10 customers contributed ~35%. The stable nature of Winpak's customer relations and its long contracts (typically 2-5 years) help to mitigate customer withdrawal risks.

**EXHIBIT XXI**

Index of Prices of Winpak's 8 Most Important Raw Materials




Source: Company Reports

# Valuation Commentary

### Comparables Analysis

A group of Winpak's 3 closest Canadian peers and two similar US peers was used for a comparables analysis of Winpak. As can be seen, Winpak trades at a discounted EV/EBITDA multiple at 8.9x 2019E EBITDA. With that said, they also trade at a slight P/E premium to their competitors, who trade at an average of 17.0x, when Cascades Inc. is taken out of the peer set.

Operationally, Winpak clearly enjoys a couple advantages relative to its peers. They have a debt-free balance sheet providing them with a significant capital structure advantage relative to their peers. Furthermore, they have leading industry margins well above that of their peers. Despite this, Winpak continues to trade at a discount to a company like CCL, likely resulting from a poor near-term growth outlook for Winpak.

### Discounted Cash Flow

This second method used to assess the value of Winpak was a discounted cash flow analysis. A relatively conservative top-line growth rate was used in the DCF with Winpak experiencing a 1% revenue decline in 2019, followed by 3.5% growth for the remainder of the projection period. Also priced in was small margin expansion from 2019 through to 2021, so as to return long-term margins to 2015/2016 levels.

Using a weighted average cost of capital of 6.0% - Winpak has a very low  risk profile due to its lack of leverage and low cyclicality – this valuation returns an implied base case share price of $37.30. This represents a 15.48% discount to Winpak's current share price of $44.13.

At this price, Winpak clearly does not provide value to us as investors. This poor price forecast is largely contributable to stagnant growth from Winpak which sees its future YoY revenue % growth estimates well below historical averages. A bull case projecting 5% annual revenue growth and a 300 bps margin expansion through 2022 only yields a $44.95 valuation, suggesting that the market is pricing in aggressive but unlikely growth in the business.

**EXHIBIT XXI**

Comparables Analysis

| | Market | Enterprise | EV / EBITDA | | Price to Earnings | | Net Debt/EBITDA | | Dividend | FY2019E |
|---|---|---|---|---|---|---|---|---|---|---|
| **Company Name** | **Cap** | **Value** | **FY2019E** | **FY2020E** | **FY2019E** | **FY2020E** | **FY2019E** | **FY2020E** | **Yield** | **EBITDA %** |
| Berry Global Group Inc. | $9,732.9 | $23,850.9 | 11.8x | 8.4x | 17.3x | 13.8x | 7.0x | 5.0x | - | 19.3% |
| CCL Industries | $9,661.3 | $11,464.3 | 10.7x | 10.3x | 19.8x | 18.4x | 1.7x | 1.6x | 1.2% | 20.8% |
| Sealed Air Corporation | $9,589.6 | $14,255.5 | 11.3x | 10.6x | 16.6x | 15.3x | 3.7x | 3.5x | 1.7% | 20.1% |
| Intertape Polymer Group | $1,096.8 | $1,840.7 | 8.1x | 7.8x | 14.0x | 13.0x | 3.2x | 3.1x | 4.8% | 16.3% |
| Cascades Inc. | $804.4 | $3,798.2 | 6.0x | 5.9x | 9.3x | 8.3x | 4.0x | 3.9x | 2.6% | 11.2% |
| **Mean** | 6,177.0 | 11,041.9 | 9.6x | 8.6x | 15.4x | 13.8x | 3.9x | 3.4x | 2.6% | 17.5% |
| **Median** | 9,589.6 | 11,464.3 | 10.7x | 8.4x | 16.6x | 13.8x | 3.7x | 3.5x | 2.2% | 19.3% |
| Winpak Ltd. | $2,868.5 | $2,356.3 | 8.9x | 8.5x | 18.5x | 18.2x | nmf | nmf | 0.26% | 22.4% |

Source(s) Company Filings, S&P Capital IQ

# DCF Valuation

## EXHIBIT XXII

Base Case Discounted Cash Flow Analysis

| Financials | Historical FY2018 | FY2019E | FY2020E | Projections FY2021E | FY2022E | FY2023E |
|---|---|---|---|---|---|---|
| Revenue | 889,641 | 880,745 | 911,571 | 943,476 | 976,497 | 1,010,675 |
| *YoY revenue growth %* | *0.3%* | *(1.0%)* | *3.5%* | *3.5%* | *3.5%* | *3.5%* |
| *Cost of sales as a % of revenue* | | *(68.4%)* | *(68.0%)* | *(67.5%)* | *(67.5%)* | *(67.5%)* |
| Cost of sales | (619,582) | (602,429) | (619,868) | (636,846) | (659,136) | (682,205) |
| Gross profit | 270,059 | 278,315 | 291,702 | 306,629 | 317,361 | 328,469 |
| *Gross profit margin %* | *30.4%* | *31.6%* | *32.0%* | *32.5%* | *32.5%* | *32.5%* |
| Operating Expenses | (78,830) | (78,169) | (79,082) | (81,850) | (84,714) | (87,679) |
| EBITDA | 191,229 | 200,146 | 212,620 | 224,779 | 232,647 | 240,789 |
| Depreciation | (41,143) | (40,732) | (42,157) | (43,633) | (45,160) | (46,740) |
| Operating income | 150,086 | 159,414 | 170,463 | 181,147 | 187,487 | 194,049 |
| *Operating income margin %* | *16.9%* | *18.1%* | *18.7%* | *19.2%* | *19.2%* | *19.2%* |
| Taxes | (39,572) | (39,854) | (42,616) | (45,287) | (46,872) | (48,512) |
| *Tax rate %* | *26.4%* | *25.0%* | *25.0%* | *25.0%* | *25.0%* | *25.0%* |
| EBIAT | 110,514 | 119,561 | 127,847 | 135,860 | 140,615 | 145,537 |
| Add: Deprecitiation | 41,143 | 40,732 | 42,157 | 43,633 | 45,160 | 46,740 |
| *Depreciation as a % of revenue* | *4.6%* | *4.6%* | *4.6%* | *4.6%* | *4.6%* | *4.6%* |
| Less: Changes to Working Capital | (27,715) | 23,774 | (7,754) | (7,873) | (9,057) | (9,374) |
| Less: Capital Expenditure | (61,474) | (60,859) | (62,990) | (65,194) | (67,476) | (69,838) |
| *Capital Expenditure as a % of revenue* | *6.9%* | *6.9%* | *6.9%* | *6.9%* | *6.9%* | *6.9%* |
| Unlevered Free Cash Flow | 62,468 | 123,207 | 99,261 | 106,426 | 109,242 | 113,065 |
| Discount factor | | 0.971 | 0.916 | 0.864 | 0.816 | 0.769 |
| Present value of unlevered free cash flow | | 119,669 | 90,954 | 91,999 | 89,088 | 86,987 |

| Terminal value Calculation | |
|---|---|
| Terminal year EBITDA | 240,789 |
| Terminal year EV / EBITDA multiple | 10.5x |
| Terminal year enterprise value | 2,528,288 |
| Discount factor | 0.769 |
| PV of terminal year enterprise value | 1,945,137 |

| Implied Share Price Calculation | |
|---|---|
| PV of unlevered free cash flow | 478,696 |
| PV of terminal value | 1,945,137 |
| Implied enterprise (USD) | 2,423,833 |
| (–) Total debt | 0 |
| (+) Cash and cash equivalents | 415 |
| (–) Minority interest | -30 |
| (–) Preferred stock | 0 |
| Implied market capitalization (USD) | 2,424,218 |
| Implied market capitalization (CAD) | 3,224,210 |
| Dilluted shares outstanding | 65,000 |
| Implied stock price | 37.30 |
| Current stock price | 44.13 |
| Implied equity return | (15.49%) |

*$1.00 USD : $1.33 CAD

## Conclusion

Despite operating within a commoditized space, Winpak offers stability and long term competitive advantages through its consistent investments in research and innovation as well as its establishment of modest customer switching costs. Technology investments and vertical integration through in-house film production and resin conversion enable the Winpak to be a margin leader within the industry as well as offer flexibility and personalization to customers. This also positions Winpak well to adapt to a changing packaging environment should sustainability concerns drive further regulatory or demand-based product requirement shifts. Winpak has established barriers to switching for several of its customers through operating in spaces where packaging is mission critical and regulated (e.g. pharmaceuticals and perishables) as well as continuously collaborating with customers in tailored packaging innovations. These economic moats are demonstrated through Winpak's consistently high ROIC and customer retention.

Furthermore, our team has high conviction in Winpak's management team which has longstanding industry and company expertise and has demonstrated exceptional discipline in deploying capital.

However, lacking growth opportunities for Winpak remains a concern. While the most recent acquisition of Control Group is a promising sign, given that it's the first acquisition Winpak has made since 2008, the time taken to make this acquisition despite active searching and available capital demonstrates the scarcity of opportunities available that meet the company's IRR and integration goals. Winpak continues to hold a substantial net cash position as a result. Furthermore, another notable concern is slowing industry growth and increasing competitiveness. Winpak has seen little organic growth over the last two years as a result of this. While we have conviction in their ability to withstand competitive pressures in the long run, this situation places further barriers to their growth.

While Winpak looks attractive on an EV/EBTIDA basis relative to its peers, from an intrinsic perspective we believe it to be somewhat overvalued at this time. The Company's current share price does not make sense to us unless we are willing to underwrite what we believe to be quite aggressive growth assumptions. As a result, we view valuation to be a major sticking point for Winpak right now.

Overall, the QUIC M&M team appreciates the quality of the business and management but is weary about its valuation and barriers to growth. Our team will seek to speak with management or industry professionals covering this company to better understand the nature and extent of competitive pressures that it is facing as well as the growth opportunities at its disposal. Improvement in outlook for these factors may drive up our valuation for the name and prompt entry. However, with our current view of these factors, we believe Winpak is a name worthwhile to keep an eye on and one that we would be comfortable entering should there be a substantial discount to its current price in the future.

## References

1. Bloomberg
2. BMO Capital Markets
3. CCL Industries Company Reports
4. CIBC Capital Markets
5. Company Reports
6. Google Images
7. Google Securities
8. Intertape Polymer Company Reports
9. RBC Capital Markets
10. Seeking Alpha
11. S&P Capital IQ
12. TD