

CST Brands, Inc. (CST - \$47.45 - NYSE)

Done Deal - Hold

<u>Year</u>	<u>EPS</u>	<u>P/E</u>	<u>PMV</u>		
2018P	\$2.20	21.4x	\$67	Dividend: \$0.25	Current Return: 0.5%
2017P	1.90	24.8	60	Shares O/S: 75.7 million	
2016E	1.75	26.9	55	52-Week Range: \$48.31 - \$29.73	
2015A	2.15	21.9	---		

COMPANY OVERVIEW

Headquartered in San Antonio, TX, CST Brands, Inc. (CST) is an operator of convenience stores (C-stores) in the US and Canada. CST operates 1,225 c-stores in ten US states (~600 in Texas) and 873 retail sites in the Ontario and Quebec provinces in Canada including 305 company operated C-stores, 496 Dealer/Agent sites, and 72 Cardlock (self-serve filling stations) sites. CST was spun-out of Valero Energy and began trading as an independent company on May 1, 2013. In October 2014, CST purchased a 100% interest in Cross America GP LLC, the GP of Cross America Partners LP (NYSE: CAPL). CST currently owns 18.7% of CAPL or 6.2 million units. On February 1, 2016, CST acquired 164 Flash Foods stores located in Florida and Georgia for \$425 million. On March 3, 2016 CST announced that it hired BofA, Merrill Lynch and JP Morgan Chase to commence “an exploration of strategic alternatives to further enhance stockholder value.” On May 8, 2016, CST announced an agreement to sell all seventy-six of its California stores and three Wyoming stores to 7-Eleven for \$408 million, or \$5.2 million per store.

Reason For Comment:

- Monday, before the market opened CST Brands announced it reached a deal to be acquired by Alimentation Couche-Tard for \$48.53 per share in cash.
- On a fully diluted basis, and including the value of CAPL units marked-to-market (\$165 million), the GP interest at cost (\$85 million), as well as the \$390 million in net proceeds from the recently closed CA and WY stores sale, the \$48.53 per share purchase price translates to about \$4.2 billion or 9.7x TTM EBITDA of \$430 million.

Table 1

CST Brands Purchase Price Multiple

(in millions, except per share data)

Fully diluted shares outstanding	77.9
Purchase Price per share	\$ 48.53
Equity Value	\$ 3,780
Net debt as of 6/30/16 (ex-CAPL)	1,105
Net proceeds from CA & WY stores sale	(390)
Value of CAPL LP units (marked-to-market)	(164)
CAPL GP value (at cost)	(85)
Cash proceeds expected from exercise of CST options	(63)
Total Enterprise Value	\$ 4,183
TTM EBITDA as of 6/30/16	430
TTM Purchase Price Multiple	9.7 x

Source: Public data and Gabelli & Company estimates

- The transaction is expected to close in early 2017, and includes Couche-Tard selling part of CST’s Canadian operations to Parkland Fuel Corp (TSE: PKI), we believe in order to appease the Canadian Competition Bureau.

Investment Case

We are changing our recommendation to Hold from Buy based on valuation. Despite the purchase price being below our 2016 \$55 per share PMV, at this time we believe it is unlikely that another bidder will come forth.

Table 2

**CST Brands Earnings Model
2014-2020P**

(in millions, except per share data)

<u>FYE 12/31</u>	<u>2014</u>	<u>2015</u>	<u>2016E</u>	<u>2017P</u>	<u>2018P</u>	<u>2019P</u>	<u>2020P</u>	<u>5-Year CAGR</u>
Revenue	\$ 12,143	\$ 9,372	\$ 9,099	\$ 9,289	\$ 9,719	\$ 10,189	\$ 10,663	3 %
EBITDA	\$ 449	\$ 414	\$ 408	\$ 448	\$ 499	\$ 578	\$ 631	9
% Margin	3.7%	4.4%	4.5%	4.8%	5.1%	5.7%	5.9%	
EPS, continuing operations	\$ 2.46	\$ 2.15	\$ 1.75	\$ 1.90	\$ 2.20	\$ 2.70	\$ 3.35	9
% Growth	27.2%	-12.7%	-18.6%	8.6%	15.8%	22.7%	24.1%	
EBITDA Multiple	9.9 x	10.7 x	10.3 x	9.4 x	8.4 x	7.2 x	6.6 x	
P/E Multiple	19.3	22.1	27.1	25.0	21.6	17.6	14.2	
CapEx	309	361	405	414	414	414	414	
Net Debt	(683)	(703)	(773)	(796)	(777)	(700)	(558)	

Source: Public data and Gabelli & Company estimates

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Table 3

CST Brands, Inc. Private Market Value Analysis 2015-2020P

(in millions, except per share data)	2015	2016E	2017P	2018P	2019P	2020P
Retail US						
Revenue	\$ 5,978	\$ 6,125	\$ 6,350	\$ 6,733	\$ 7,154	\$ 7,579
EBITDA	380	377	415	466	545	598
Valuation Multiple	10.0 x	10.0 x	10.0 x	10.0 x	10.0 x	10.0 x
Segment Value	3,805	3,773	4,149	4,658	5,448	5,980
Retail - Canada						
Revenue	\$ 3,394	\$ 2,966	\$ 2,932	\$ 2,980	\$ 3,029	\$ 3,078
EBITDA	152	156	160	162	164	167
Valuation Multiple	10.0 x	10.0 x	10.0 x	10.0 x	10.0 x	10.0 x
Segment Value	1,520	1,563	1,601	1,623	1,645	1,667
Corporate						
EBITDA	\$ (118)	\$ (125)	\$ (127)	\$ (129)	\$ (131)	\$ (133)
Valuation Multiple	5.0 x	5.0 x	5.0 x	5.0 x	5.0 x	5.0 x
Segment Value	(590)	(627)	(637)	(647)	(657)	(667)
Total Private Market Value	4,735	4,709	5,113	5,634	6,436	6,980
Plus: CrossAmerica GP interest (at cost)	85	85	85	85	85	85
" CrossAmerica LP units (marked-to-market)	164	164	164	164	164	164
Less: Net Debt	(703)	(773)	(796)	(777)	(700)	(558)
" Options Payment	(15.4)	(14.3)	(18.2)	(23.7)	(32.5)	(39.5)
Equity Private Market Value	4,266	4,171	4,548	5,082	5,952	6,632
Basic Shares Outstanding	76	76	76	76	76	76
PMV per share	\$ 56	\$ 55	\$ 60	\$ 67	\$ 79	\$ 88
Current Market - Discount to PMV	16%	14%	21%	29%	40%	46%

Source: Public data and Gabelli & Company estimates

Other Companies Mentioned:

7-Eleven	(SE - Z)	CrossAmerica	(CAPL - NASDAQ)
Alimentation Couche-Tard	(ATD - TO)	JPMorgan Chase	(JPM - NYSE)
Bank of America	(BAC - NYSE)	Parkland Fuel Corp	(PKI - Toronto)
		Valero Energy	(VLO - NYSE)

CST Price Performance



Source: Public data. As of August 23, 2013 CST had a BUY recommendation.

I, **Damian A. Witkowski** the Research Analyst who prepared this report, hereby certify that the views expressed in this report accurately reflect the analyst's personal views about the subject companies and their securities. The Research Analyst has not been, is not and will not be receiving direct or indirect compensation for expressing the specific recommendation or view in this report.

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Important Disclosures

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Analysts' ratings are largely (but not always) determined by our "private market value," or PMV methodology. Our basic goal is to understand in absolute terms what a rational, strategic buyer would pay for an asset in an open, arms-length transaction. At the same time, analysts also look for underlying catalysts that could encourage those private market values to surface.

A **Buy** rated stock is one that in our view is trading at a meaningful discount to our estimated PMV. We could expect a more modest private market value to increase at an accelerated pace, the discount of the public stock price to PMV to narrow through the emergence of a catalyst, or some combination of the two to occur.

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