Norwegian Cruise Line Holdings Ltd. (Nasdaq: NCLH)

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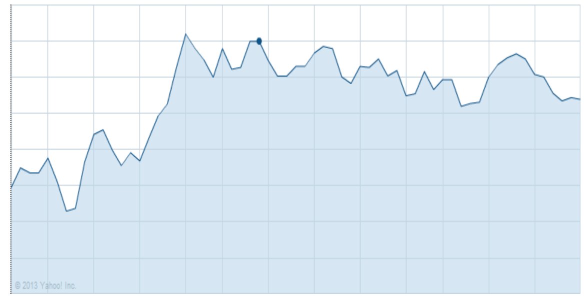
Important Company Financial Data

Share Price: 29.38
P/E: 31.26
Forward P/E: 13.26
Dividend yield: N/A
Cash: 45.5M
ROE: 8.73%

Market Cap: 5.99B
Beta: N/A
EPS:0.94
Volume: 210,727
Total Debt: 2.99B
ROA: 3.88%



Thesis / Key Points

- **Weak member of a competitive industry**: Norwegian Cruise Line Holdings currently is the smallest company, per industry share, in the cruise liner industry putting it at a disadvantage when the other companies in the same industry expand. Since its IPO in January 2013, NCLH has managed to acquire 8% of the cruise line industry. This percentage is minimal compared to the 73% market share controlled by Carnival Corporation (NYSE: CCL) and Royal Caribbean Cruise Ltd. Co. (NYSE: RCL). Currently NCLH controls 11 cruise ships with the hopes of having 14 ships in total in the next 5 years. CCL anticipates aggrandizing their fleet to 109 ships while RCL anticipates their fleet size in 2015 to be 42 ships. With 58% of the industry focused in North America, RCL and CCL control nearly 90% of all the cruises that originate in this market. Along with this, the two largest cruise ports, Miami Florida and Nassau Bahamas, both have exclusive deals with RCL and CCL thus allowing only so many cruise ships from other companies to use the ports. On top of that, RCL has recently signed a deal with Disney thus removing another large portion of the market. Ultimately in North America, though NCLH has developed some headway, it will prove hard to continue expanding especially when RCL and CCL are both entering growing phases too.
    - **Weak Opportunities outside of North America**: Outside of North America, the second largest share of NCLH's business (11%) is conducted in Europe which consists of 29% of the global cruise liner industry. However, currently, while estimates show the cruise liner industry growing by 5.6% in worldwide, growth in Europe will only increase by 2.4%. Thus, though competition remains less fierce in Europe than in the United States, austerity measures coupled with the Costa Concordia incident in 2012 mean there will be few changes in the market that will benefit NCLH
- **Unviable business model**: NCLH's business model is not viable based on the changing trends of the cruise liner industry which focuses on cutting prices while providing the same level of service. Norwegian Cruise Line Holdings finds their competitive edge by allegedly offering a higher level of luxury on cruises than RCL and CCL along with charging a higher price for the service. Along with this, NCLH, since 2000, has instituted a "Freestyle Cruising" policy which allows passengers to order ahead of time which activities they would like to do with them being ultimately provided along with the activities being available at whichever times the passengers so choose for them to occur. As a result of higher prices and a steady flow of passengers, NCLH enjoys a gross margin of 35% which is relatively higher than any of the competition. However, this business model is not viable if NCLH seeks to expand or afford the new ships that it recently purchased.
    - **Changing Demographics:** Though cruise passengers worldwide in 2013 is forecasted at 20.9 million, a 3.3% increase, the mean income of passengers is expected to drop from $102k to $90k due a general decrease in the prices for cruises with RCL and CCL. In fact, while NCLH offers, on average, $175 per night for their cheapest accommodation, CCL is currently offering rooms for as cheap as $38 per night. Furthermore, based on customer reviews, it appears that NCLH luxury rooms compare evenly with their CCL and RCL cheaper counterparts. At the same time, NCLH faces competition from other, more established luxury cruise brands such as Celebrity Cruises, Holland America Line, and Princess Cruises. Norwegian Cruise Line Holdings cannot hope to expand and will most likely shrink if they cannot cater to the new demographics which seek cheaper cruises at the same level of luxury.
- **Highly Indebted:** In a bid to expand its market share, Norwegian Cruise Line Holdings has made financial decisions that rely on steady growth to pay of the means of expanding. Currently, prior to purchasing 4 new cruise liners, NCLH's Net Debt to EBITDA stood at 5.0x. With the new purchases this year, cash flows are not expected to be positive again till 2016 especially since private equity sponsors are seeking to cash out in the next year based on the

stock price remaining stagnant. This predicament presents two issues. With only $45 million in cash along with $2.99 billion in debt, NCLH cannot afford many liabilities or a decrease in revenue. However, the cruise liner industry has experienced a wave of lawsuits and increases in insurance prices due to cruise line crashes and malfunctions. Furthermore, NCLH, being the smallest publicly owned Cruise Liner Company, faces steep competition which can prevent the company from gaining the necessary revenue to afford the intended expansions.

Misperception

- **NCLH currently is attaining a growing permanent market share:** Due to the Costa Concordia crashing off the shore of Italy in 2012 and the Carnival Triumph catching fire and stranding passengers in February 2013, NCLH had an IPO much higher than expected with $1 billion gained in the first day. As a result, many have speculated that customers have become disgruntled with CCL (owner of the two above cruise ships) and RCL and have decided to turn to NCLH as the cruise liner of choice; thus leading to NCLH to experience future growth. Though this may be true to an extent, on average most cruise line customers only go on a cruise once or twice in their lives. Furthermore, the demographic of cruise line passengers is spreading to a lower income branch of society. Thus, not only will customers be uninterested in past events but also will be keener on attaining a cheaper price for the cruise line experience. RCL and CCL are expected to regain lost revenue and customers due to their cheap prices along with CCL launching a $200 million redesign project along with RCL placing aside $500 million for ship modernizations. As a result, NCLH in the long run will have virtually no competitive edge to stand up against the larger companies in the industry.
- **The general growth of the Cruise Line Industry will automatically benefit NCLH:** The cruise liner industry is expected to grow by 5.6% annually for the next three years. As a result the market conjectures that NCLH with benefit from this growth. However, industry capacity remains 4% above demand. Thus, instead of new markets, NCLH is stuck fighting CCL and RCL over already heavily controlled markets.

VAR

- **Tim Creeson, Analyst for Port Miami**: “Basically we don’t expect additional Cruise Liner docking space to be available till 2017 especially since the earliest current contracts to do not run out till then… ”
- **Jane Goodson, Critic for Cruise Market Watch**: “The level of luxury that they [NCLH] claim to provide can be matched by the Carnival and outdone by boutique cruise liners like Phoenix Reisen…”

How It Plays Out

- Though NCLH just recently had its IPO, the stock price should remain stagnant with little to no change until the 2013 end of the year report is announced where the company may still have some substantial growth
- NCLH should continue to have 100% bookings for their trips till mid 2014.
- Beginning in 2014 with both RCL and CCL launching new cruise liners, NCLH should lose market share along with stock price as a result
- By the end of 2014, CCL should have regained the market share lost as a result of cruise liner accidents. Based on room prices, their revenue should increase by 15% in North America alone.

Risks / What Signs Would Indicate We Are Wrong?

- **Further Market share increase:** Should RCL or CCL experience any more liability issues in 2013, NCLH could benefit from the bad publicity to further aggrandize their share of the market.
- **NCLH continue to have 100% bookings in their cruise liners**: in 2014 if NCLH continue to experience 100% even though their price remain higher than CCL and RCL, then NCLH could have stronger customer loyalty than expected.

Signposts / Follow-Up

- Track the finances of CCL as they attempt to make a comeback in face of the recent snafus.
- In May 2013, NCLH will announce quarterly earnings which may show early signs of either decay or growth of their company.
- See when private equity sponsors withdraw the funds invested in NCLH.
- Look into anticipated weather for the peak period of cruise liner activity, late July and August.

Company Description

[Nasdaq:NCLH] is a cruise line operator, offering cruise experiences for travelers in North America, the Mediterranean, the Baltic, Central America, Bermuda, and the Caribbean. The company offers cruises ranging in length from 1 day to 3 weeks. As of December 31, 2012, it operated 11 ships offering cruises in Alaska, the Bahamas, Bermuda, the Caribbean, Europe, Hawaii, Mexico, New England, Central and South America, North Africa, and Scandinavia.

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In a nutshell, NCLH is a low ROI, capital intensive, cyclical, and highly indebted enterprise whose private equity sponsor is most likely looking to cash out trading at 16.5x 2012 and 14.4x 2013 Ebitda. It peers, CCL and RCL trade at 10x, which is already pretty rich. NCLH trades well above replacement value despite a weak ROI profile. CCL and RCL trade well below replacement value, which makes sense given the relatively low ROIs. Based on the information, NCLH trades at 150% of replacement value, while CCL and RCL trade at 90% and 80% respectively. As can be seen, CCL is the best operator. It also has the strongest balance sheet and the best cash flow profile. It pays a regular dividend (~2.6% yield) and in late 2012 paid a special dividend. Net debt to 2012 Ebitda stands at 2.6x, while RCL and NCLH show 5.5x and 5.0x respectively. Ultimately, over the next two years, 2013 and 2014, NCLH will significantly add capacity leading to its cash flow will be negative.

Revenue growth	2007	2008	2009	2010	2011	2012
CCL	10%	12%	-10%	7%	12%	-3%
RCL	18%	6%	-10%	15%	12%	2%
NCLH	10%	-3%	-12%	8%	10%	3%

ROI	2007	2008	2009	2010	2011	2012
CCL	12%	11%	8%	8%	8%	6%
RCL	8%	7%	3%	5%	6%	2%
NCLH	n/a	n/a	n/a	6%	7%	n/a

Ebit margin	2007	2008	2009	2010	2011	2012
CCL	21%	19%	16%	17%	14%	11%
RCL	15%	13%	8%	12%	12%	5%
NCLH	2%	-3%	9%	11%	14%	n/a

Ebitda margin	2007	2008	2009	2010	2011	2012
CCL	29%	27%	26%	27%	24%	22%
RCL	23%	21%	18%	21%	22%	20%
NCLH	9%	11%	17%	20%	23%	23%

Net rev yield	2007	2008	2009	2010	2011	2012
CCL	188	195	169	172	179	171
RCL	184	184	158	165	172	174
NCLH	160	170	156	168	173	n/a

Net CCost/albd	2007	2008	2009	2010	2011	2012
CCL	119	129	113	116	126	125
RCL	129	133	120	118	122	129
NCLH	139	144	118	123	120	n/a

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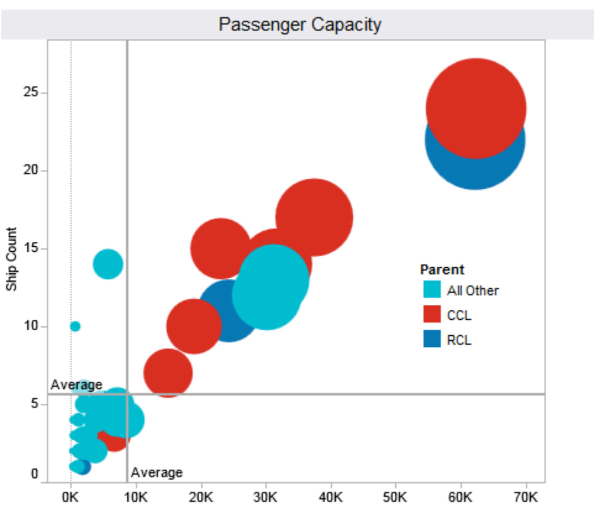
Norwegian Cruise Line Holdings neither has competitive luxury nor competitive price to compete against Royal Caribbean Cruises or Carnival Cruises

NCLH: Norwegian Dawn ~ $175 per night

CCL: Holland Princess ~ $40 per night

RCL: Santa Peri ~ $90 per night



Cruisers as a % of Demo Group

Demo	Demo Detail	
Income	$39k to $50k	9%
	$50k to $60k	10%
	$60k to $75k	39%
	$75k to $100k	19%
	$100k to $200k	16%
	$200k to $300k	7%
	$300k+	1%

Details

Parent	Brand	Passenger Capacity	Ship Count
CCL	Carnival	62,370	24
	Princess	37,470	17
	Costa Cruises	31,640	14
	Holland America	23,110	15
	AIDA	18,970	10
	P&O Cruises	14,970	7
	P&O Cruises Australia	6,910	4
	Cunard	6,690	3
	Ibero Cruises	4,610	3
	Seabourn	1,970	6
	Total	208,710	103
RCL	Royal Caribbean	62,220	22
	Celebrity	24,320	11
	Pullmantur	7,820	4
	CDF	1,830	1
	Azamara	1,420	2
	Total	97,610	40
All Other	MSC Cruises	31,250	13
	Norwegian	30,170	12
	Disney	8,510	4
	Thomson Cruises	7,150	5
	Star Cruises	7,100	4

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Ideas for the Club

The one thing that has truly improved this year is the amount of the social events hosted after meetings. One thing I would like to add to this is "fireside chats" where a small group of MII members sit down with a professor and discuss a certain aspect of investing or business. This would be a good way to supplement the post-meeting gatherings that stimulate debate, conversation, and enlightenment. Ultimately additional social events would help bring the members of MII together.

Also, another idea that I pitched last year which would allow members to further mingle with managers and associates is to conduct a workshop/competition where on a Saturday managers and associates leads teams of regular members to find, research, and present a pitch for a company within a set time limit. Professors in the commerce school would be the judges and the team with best presentation and research would win some reward like an all-expense paid dinner at a restaurant on the corner. This would not only be a relatively short, educational activity but it would also encourage people to make more friends and connections within MII.