

WEEKDAY TRADER ■ by Naureen S. Malik

Ready to Be Re-Energized



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Les Engebretson, Ph.D., CEO

The company is a potential takeover target. Some have speculated that Anheuser-Busch, which once attempted to put out an energy drink of its own, might end up buying Hansen.

INVESTORS IN HANSEN NATURAL turned fickle toward the No. 2 energy-drink company in last year's second half. But new growth initiatives could put some fizz back into the shares in 2007.

Hansen enjoyed a monster run from 53 cents at the beginning of 2003 to a record \$52.72 last July 6 (adjusting for stock splits). But its shares slumped after the company reported in-line second-quarter earnings, much to the disappointment of growth investors used to outsized advances, and an options probe.

At its current price of \$37.08, Hansen is 30% below last year's high, though still triple the price (again, on a split-adjusted basis) that it was fetching when *Barron's* published a skeptical piece on it in the summer of 2005. (See *Barron's* feature, "Buzzed to the Max: Why This Drink Is Scary," Aug. 1, 2005.)

Although the stock has bounced back somewhat, there is still upside potential of at least 20%, as Hansen starts to reap the benefits of a deal under which brewer Anheuser-Busch will distribute its Monster Energy Drink, potentially providing deeper market penetration. Hansen also should benefit from new-product introductions, following a pause in its pipeline last year. In addition, the company is likely to emulate energy-drink leader Red Bull's recent decision to boost prices.

Les Engebretson, the founder and chief executive of Engebretson Capital Management in Newport Beach, Calif., started buying Hansen stock in 2004 and says the popularity of the beverage maker's energy drinks isn't a fad. "They have been able to take market share away from the others pretty consistently," he says, adding that the Anheuser arrangement represents "a major shift" in marketing. He expects earnings to grow another 35%-40% in 2007 from the \$1.11 expected in 2006. This compares with 65 cents a share in 2005, 22 cents in 2004 and a mere seven cents in 2003.

Some speculate that the Anheuser relationship ultimately could lead the St. Louis brewing giant to bid for the company.

Hansen's chief executive, Rodney Sacks, declined to comment for this article.

With an initial cost of under \$5 per share, Engebretson's firm sold about half of its stake last May for roughly \$3.56 million at around \$48 per share. But it was a buyer again near the end of 2006, as Hansen shares dipped to around \$30.

Engebretson says that Sacks and Hansen president Hilton Schlosberg manage the company well. The two South Africans purchased Hansen in the 1990s when it was generating roughly \$17 million in annual sales. Last year, it probably had \$530 million in revenue. "It was a sleepy business that they took over and turned into a remarkable growth story," comments Engebretson.

The beauty of Hansen's business model is that the company doesn't own any manu-

facturing facilities or make its own drinks. Instead, it relies on a network of producers and distributors with more efficient economies of scale to make, package and sell its products.

As a result, Hansen has strong cash flow, low capital requirements and costs and can churn out a new product in as little as six weeks, says Engebretson, whose firm calls Hansen's brass monthly and visits its Corona, Calif., headquarters once or twice a year.

Although Hansen sells over a dozen varieties of fruit juices and carbonated natural sodas, about 90% of its sales are generated by energy drinks. Its top sellers are marketed under the Monster label; others, under labels including Lost and Rumba Energy Juice.

In the 13 weeks ended Oct. 28., Monster's 16-ounce cans commanded \$23.4 million of the \$100 million U.S. energy-drink market, narrowing the gap with Red Bull's \$33.8 million, according to AC Nielsen.

Energy drinks are the fastest-growing segment of the beverage world, with sales expanding roughly 50% in 2006. ACNielsen tallied the 2005 wholesale market at \$1.6 billion. A Hansen investor presentation in December estimated that convenience stores account for at least 50% of U.S. energy-drink sales.

Goldman Sachs analyst Andrew Sawyer expects the Anheuser-Busch deal to boost Hansen's penetration to 80% at U.S. food and convenience stores, from 55%-65%. That should help it grab some of Red Bull's market by the horns. Anheuser also will provide some marketing for its new partner.

This deal could also lead Hansen to start selling the Monster label at bars where Red Bull is popularly mixed with vodka, but only if Hansen can create a similar kind of brand image, says Sawyer. Right now, Hansen's core consumers are 18-to-25-year-old males, with more of a "blue-collar skew" than Red Bull's imbibers, he adds. To create a cooler image, Hansen has been sponsoring extreme and motor sports. In 2004, it was also marketing to soccer moms, notes Engebretson.

The Anheuser-Busch arrangement should give Hansen more clout with retailers, such as The Pantry, which did not widely carry the Hansen labels at its 1,500 convenience stores. Stifel Nicolaus analysts Mark Swartzberg and Mark Astrachan wrote in a Jan. 5 note that it was "the swing factor elevating Hansen to effective distribution parity with Coke and Pepsi" with that chain.

Hansen stock could see further upside should the company raise its prices, says Goldman Sachs' Sawyer. He expects Monster sales to climb 45% in 2007.

In the longer term, Hansen could extend its Anheuser-Busch deal to include on-premise distribution. The company also is probing international opportunities, notes Sawyer.

At a Glance Hansen Natural (HANS)

Stock Price:	\$37.08
52-Wk High:	\$52.72
52-Wk Low:	\$19.40
Market Cap:	\$3.37 billion
Est. 2007 EPS:	\$1.60 per share
2007 P/E:	23x
Est. Long-Term EPS Growth:*	36%
Est. ('07/'06) EPS Growth:	38%
Revenue (trailing 12 months):	\$552 million
Dividend Yield:	None
CEO:	Rodney Sacks
Headquarters:	Corona, Calif.

*Based on analyst estimates for three to five years
Sources: Yahoo! Finance, Thomson First Call, Thomson Financial/Baseline

Any good news from Hansen would put pressure on the bears who've shorted 19% of its 70.2 million publicly traded shares. If they had to cover a substantial portion of their bets, that could push the stock higher.

The company, which has just 400 employees, is certainly a potential takeover target. Some have speculated that Anheuser-Busch, which had once attempted to put out an energy drink of its own, may end up purchasing Hansen.

On a valuation basis, the stock is trading at 25 times earnings estimates for the next four quarters, a reasonable multiple given expected earnings growth of at least 20% over that span.

To be sure, Hansen could continue to face downward pressure through the first half of the year during its transition to the Anheuser-Busch distribution system. In some cases old distributors had become complacent about pushing the product, notes Sawyer.

An options backdating probe and class-action suits could weigh on the stock, as well. The investigation has found that 12,000 shares were "inadvertently" awarded to a director in November 2004 after a grant expired, according to a press release earlier this month. Stock options currently held were also amended. Based on independent analysis of Hansen's option grants, Engebretson contends that the class-action suits have little merit.

The good news for investors is that brand extensions and higher market penetration should keep Hansen's sales and earnings growing at a double-digit pace. Shareholders would gladly drink to that.