OSI Systems – OSIS

September 24, 2007

Group 3
Allie Atwood
Peter Curzon
Ryan Ingle
Kirk Smith

Company Overview

- OSI Systems, Inc. is a vertically integrated designer and manufacturer of electronic systems
- Their business has three divisions: security, healthcare, and optoelectronics/manufacturing

OSI SYSTEMS, INC.

Recent News

- Increased revenues by 22% for Q4 to $152.8 million
- Record backlog of $209 million—most coming from the security division
- Significant stock decline after light revenue guidance from management

OSI SYSTEMS, INC.

Company Profile

Market Capitalization	
Shares outstanding	17 million
Stock price as 9/21/07	21.95
Total market cap	**$373.15 M**
Enterprise Value (millions USD)	
Market Capitalization	373.15
Less: Cash	15.98
Less: Minority Interest	8.8
Plus: Debt	48.23
Enterprise Value	**$405.4 M**

APM Portfolio

- Position:
500 shares
- Percentage of the Portfolio:
0.43%
- Average Purchase Price:
$26.02

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Investment Thesis

- The security segment is currently benefiting from a backlog yet historical income margins are currently 3-8%
- The medical devices segment's revenues temporarily propped up by acquisition of Del Mar Reynolds
- Optoelectronics segment will remain unprofitable with projected operating losses of $6.4 million over the next four quarters
- Target Price of $17.01 from Current Price of $21.95

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Risks

- Security Division: Decrease in government spending and increase in competition

- Healthcare Division: Highly competitive market and intense pressure for OSIS to cut costs to remain competitive

- Optoelectronics Division: Escalating long-term contract costs

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Possible Upside

- Possible increase in demand for security segment as Homeland Security regulations intensify
- Improved margins after management restructuring
- Spinoff of Weapons Simulation segment as alluded to by management before end of CY 2007

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Stock Analysis

Pro Forma Income Statement (figures in millions)						
	2005	2006	2007	2008E	2009E	2010E
Revenue	385.0	452.7	532.3	597.8	664.0	737.6
Revenue Growth		*17.6%*	*17.6%*	*12.3%*	*11.1%*	*11.1%*
Gross Margin	141.6	176.7	178.2	217.8	241.1	261.2
Gross Margin %	*36.8%*	*39.0%*	*33.5%*	*36.4%*	*36.3%*	*35.4%*
EBIT	(7.0)	1.0	(42.2)	(23.9)	6.6	14.8
EBIT Margin	*-1.8%*	*0.2%*	*-7.9%*	*-4.0%*	*1.0%*	*2.0%*

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Valuation

- Current Target Price of $17.01
- Range of $13.52 - $26.48

Sensitivity Analysis (share price in dollars)				
	Revenue Growth			
WACC	9.0%	**12.3%**	15.0%	18.0%
9.00%	25.10	25.58	26.00	26.48
10%	20.90	21.30	21.64	22.03
11.42%	16.70	**17.01**	17.28	17.59
12.00%	15.40	15.68	15.93	16.21
13.00%	13.52	13.76	13.97	14.21

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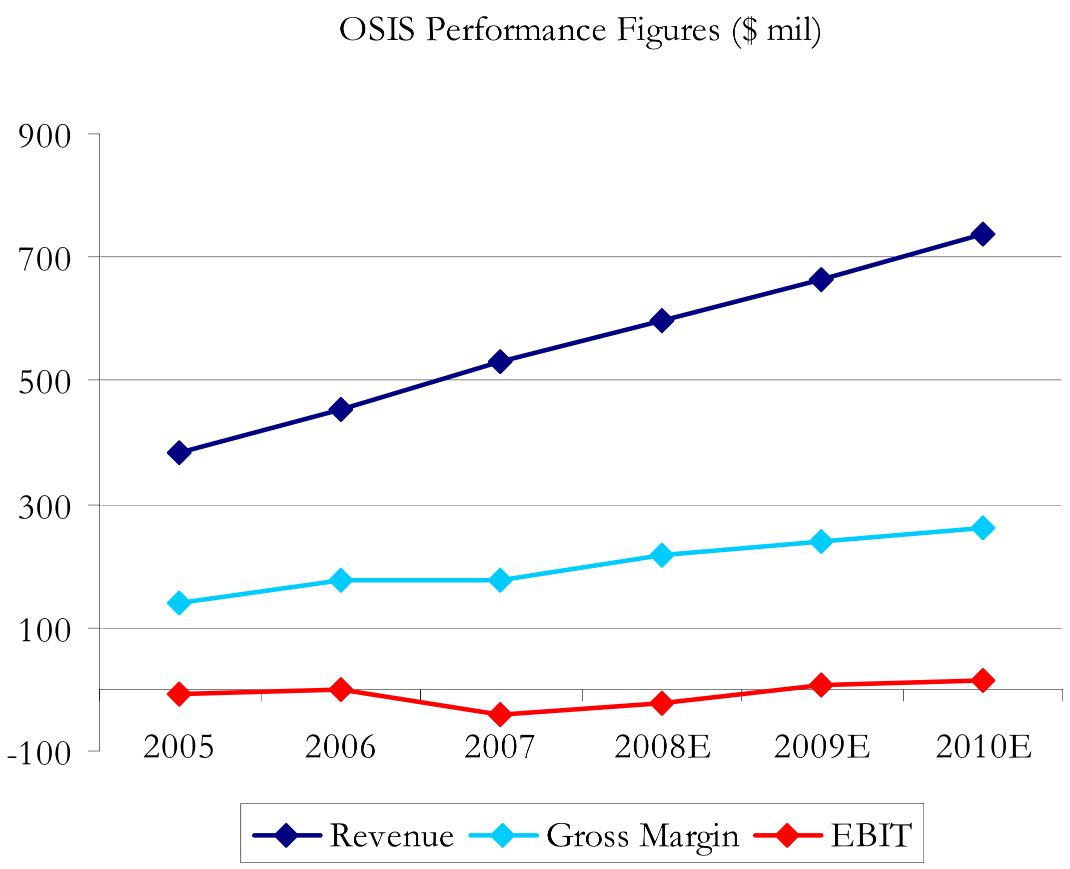
Financial Forecasting



Recommendation

- Mentor Todd Preheim of Campanile Capital Trading recommended **Selling** after most recent earnings call
- We reiterate the **Sell** recommendation due to:
  - Less than 1% profit margins for three years
  - FY 08 revenue guidance of $580 – 595m well below analyst expectations
  - Declining Health Care growth to 10% for FY 08

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