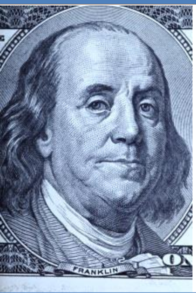


# 3 Empire Profit Plays for Triple Digit Gains in 2015

A Special Research Report from **The Turnaround Stock Report**

Investors Alley

## Introduction

2015 has been a mixed bag so far for investors. Q1 GDP growth came in at a dismal 0.2%. On the other hand, equities have held up quite well through earnings season despite profits and revenues flat lining year-over-year and thew S&P 500 hovering near all-time highs.

Going forward, 2015 will be a stock pickers market. I forsee gains of no more than 10% for the year for the broader markets. More encouragingly, I am finding some remaining bargains in equities within individual sectors and stocks where sentient is more negative then the underlying business fundamentals

The biggest trends this year will be the lasting effects of the rout in energy prices, the begginings of Europe’s quantitative easing, the strong dollar, and the Fed deciding when and how much to raise interest rates in the coming year.

In short, it will be another year for stock pickers as there will be no rising tide to lift all boats.

At The Turnaround Stock Report we are digging through the carnage in energy and specific companies to find stocks that have underperformed the markets over the part year but are poised to deliver outsized returns in 2015 and beyond if sentiment improves for them even slightly. They have many of the dominoes in place for big gains, we’re just getting in before they start moving.

In this report we’ll cover three that seem poised to rip if the dominoes start to fall into place this year.

Bret Jensen
Editor
*The Turnaround Stock Report*

## FelCor Lodging Trust: The Transformation Continues

**FelCor Lodging Trust (NYSE: FCH)**
Irving, TX, USA
http://www.felcor.com
Last: $11.12
Capitalization: $1.6 billion
Market Sector: Lodging, REIT

**FelCor Lodging Trust (NYSE: FCH)** is a real estate investment trust that went public in 1994. FelCor owns a diversified portfolio of primarily upscale and luxury hotels that are located in major and resort markets. FelCor partners with leading hotel companies to operate its hotels, which are flagged under globally recognized names and premier independent hotels such as Marriott and Wyndham. FelCor currently owns interests in over 50 hotels with just over 15,000 rooms.

Near Death Experience:


Like a lot of real estate investment trusts in the lodging and commercial property spaces, FelCor was severely impacted by the financial crisis and the freezing of the credit markets back in 2008 and early 2009. The shares plunged from over $20 a share to under $2 a share at the depth of the crisis. In addition to taking on too much debt the company did not have an overall hotel management strategy with hotels at airports, urban centers as well as non-top 25 markets.

New Focus:

The REIT decided to sell 70% of its hotels in non-primary markets as well as 50% of its airport hotels. When done these efforts will leave FelCor with portfolio of premium hotels in primary urban markets (San Francisco, NYC, Boston, etc….), upscale resorts and high traffic airport hotels that will all benefit from increasing business and leisure travel.

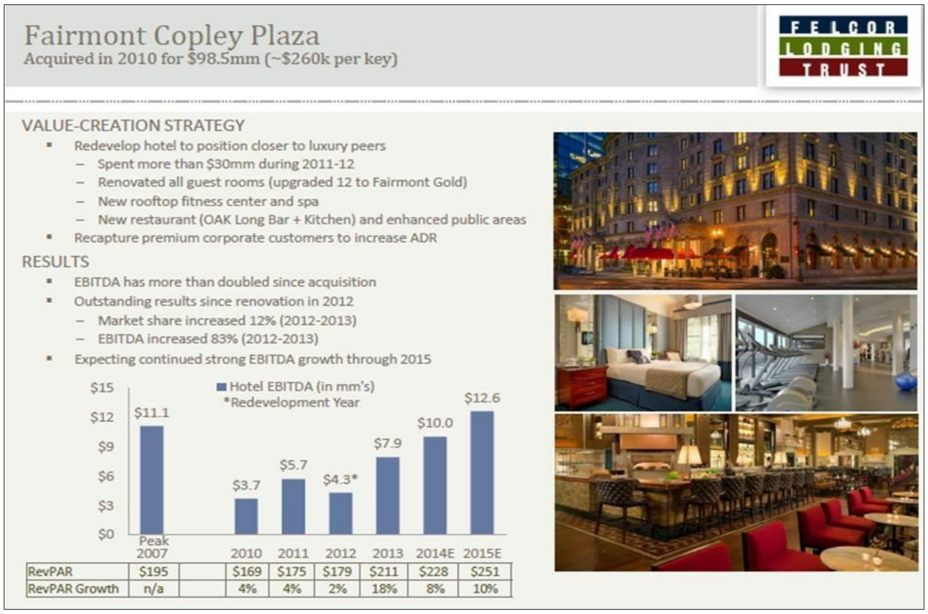
When I last highlighted FelCor in the earlier stages of this transformation on SeekingAlpha in June of 2013 (Notation 1), the REIT had already sold 20 hotels with ~5,000 rooms for a cumulative $429 million. At that point in time the REIT was approximately half way through this divestiture effort.

In February, FelCor announced that it sold its 225-room Embassy Suites Hotel – Raleigh and 536-room Westin – Dallas Park Central for aggregate gross proceeds of $63.6 million in separate transactions. FelCor has also agreed to sell the 261-room Embassy Suites Hotel – San Antonio Airport for $29.5 million. With these latest sales, the company only has a few non-core hotels left to divest and mostly done with the first part of its transformation effort.

Using Sale Proceeds Wisely:

*Renovations:*

If done correctly, renovations make hotel properties much more valuable. The revamped hotels produce higher occupancy levels, rising RevPARs (Revenue Per Available Room), ADRs (Average Daily Room Rates) and most importantly significantly improve FFO from those facilities. FelCor has executed its renovation strategy extremely well.




*Reducing Debt:*

The REIT has made substantial progress over the past few years of refinancing high cost debt, staggering its debt maturities, reducing debt overall and most importantly becoming a much less levered company with substantially more interest coverage reducing its risk premium substantially. This also gives the company more financial flexibility to acquire attractive additional hotels in core markets and/or continue to initiate and complete renovations to existing properties to increase FFO.

*The Knickerbocker:*

In 2011, the company spent $115 million to acquire The Knickerbocker Hotel on one of most desired hotel locations in the world at 42nd & Broadway in New York City. FelCor spent another $240 million redeveloping the property for a total cost of $725,000 per room. Similar hotel construction in the area has come in at over $900,000 a key.

Earlier the month the company proudly announced the grand re-opening of its new flagship property. The newly redeveloped hotel will 330 spacious and luxurious guest rooms, including 27 Junior Suites and four Tribute Suites, a state-of-the-art fitness center, a 2,200 square-foot event space, upscale food and dining options, and a 7,500 square-foot rooftop bar and terrace with unrivaled views of New York City's effervescent skyline.

The redevelopment of the Knickerbocker obviously took a good portion of FelCor's focus as well as cash flow over the past few years. Combined with the renovations at core properties, deleveraging of its balance sheet, the reopening of the Knickerbocker is going to make major differences to the company's cash flow, FFO, dividend payouts and the way the REIT is perceived over the next 12-18 months.

The Best Lies Ahead:

The shares now go for just over $11 a share. I still hold and intend to continue to hold these shares for the foreseeable future as the company has kept its promises to investors and executed impressively against its well thought out turnaround strategy which is probably in its sixth or seventh inning.

However, the next year or two is going bring the benefits of all of FelCor's efforts in recent years in focus. FFO is going to increase substantially over the next few years with $1 a share of FFO likely in FY2015 or soon thereafter. This REIT reinstituted its dividend in the second quarter of 2014 and then doubled its dividend payouts to start 2015. The shares now yield 1.5%. Given how much FFO is going to increase over the next year or two, I expect the company to be paying a dividend of at least three to four percent over the next 18-24 months based on the current price of its shares. This would put it in line with peers and easily doable given its projected cash flow increases.

In addition, lodging continues to be one of the strongest parts of the real estate investment trust space. Little if any room construction took place during the financial crisis and in the years afterward. Business travel has returned to peak pre-crisis levels and consumer travel is rapidly recovering. This has resulted in more demand than supply as well as increasing occupancy levels and RevPAR growth in the high single digits annually over the past few years. These trends are expected to continue for at least a couple of more years as new room supply is still growing much slower than pre-crisis levels.

FelCor was selling for north of $20 a share before the crisis. The company has shrunk its room count some 20% to 30% since then, but it is operating in better and more valuable core markets. Over time I think the REIT can achieve its previous levels and investors can expect significant capital appreciation and dividend increases over the next 2-3 years.

Given its growth prospects, paying around 11 times forward FFO is an attractive entry level despite the significant rise in the shares over the past 18 months. Based on a price to sales basis, FelCor is selling at a substantial discount to competitors like Hospitality Properties Trust (NYSE: HPT) and Host Hotels & Resorts (NYSE: HST).

**Recommendation: Buy FCH up to $11.50 a share, hold as long as company continues to execute well against its transformation plans.**

Notation 1: http://seekingalpha.com/article/1583722-felcor-lodging-trust-transformation-will-unlock-significant-gains

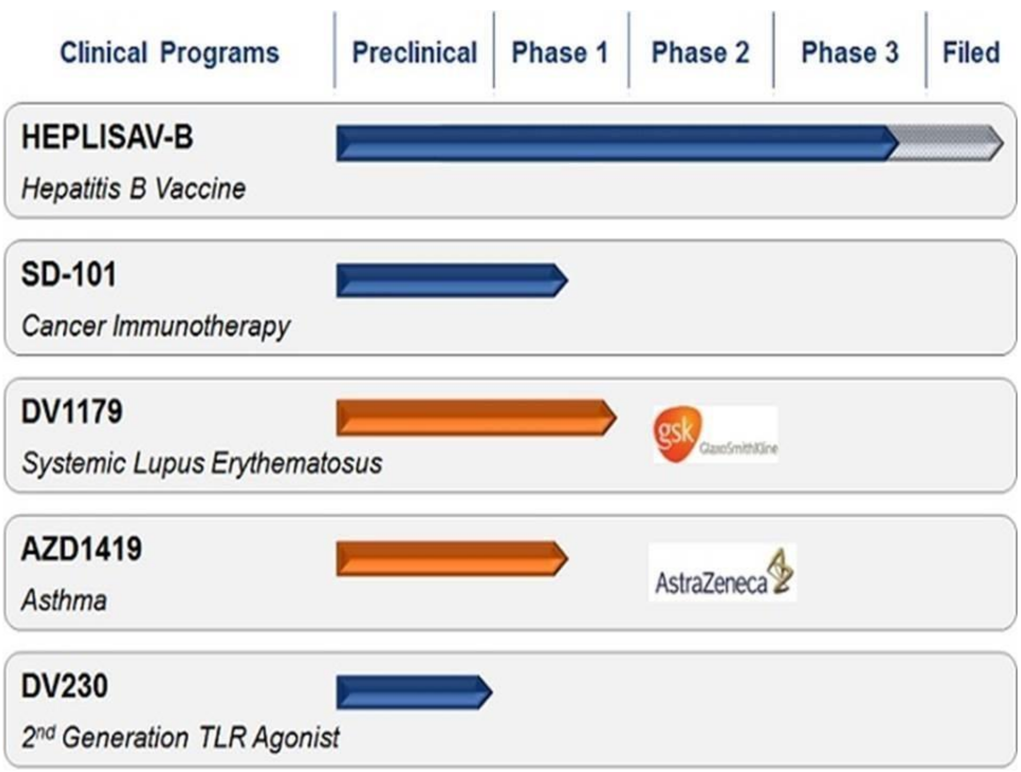
## Stocks from Spring's Unloved Sector Pick Up Steam

**Dynavax (Nasdaq: DVAX)**
Berkeley, CA, USA
http://www.dynavax.com
Last: $20.51
Capitalization: $600 million
Market Sector: Healthcare, Drugmaker

With a market capitalization of about $650 million, Dynavax focuses on pioneering a new approach to therapies for multiple autoimmune and inflammatory diseases including lupus, psoriasis, and rheumatoid arthritis. The company's technology looks to inhibit Toll-like Receptors (TLRs). TLRs are key receptors of the innate immune system that can induce strong inflammatory responses.

The commercial opportunity is quite large. Over 20 million individuals just in the U.S. and Europe have autoimmune diseases such as lupus, psoriasis, and rheumatoid arthritis. Key biologic drugs used to treat these conditions generate over $15 billion in worldwide sales each year.

The company has several compounds in development. However, near-term prospects will be driven by the development of Heplisav-B which is a vaccine in Phase III trials that is targeted at hepatitis B. Hepatitis B is the most common serious liver infection in the world. It comes in two varieties: acute and chronic. Most individuals have the acute version of this disease which affects the individual for 1-4 months presenting symptoms like fatigue, appetite loss, nausea, as well as itching, jaundice, and aches in the liver region. This version of the disease is usually defeated without drugs over a few months.



The chronic version of this type of hepatitis does not go away by itself and can cause a form of liver cancer and death. Children are particularly at risk if they are infected with this type of hepatitis.

The company also has early stage development for treatment of Lupus within a partnership with **GlaxoSmithKline (NYSE: GSK)** and an early stage asthma compound is being developed in conjunction with **AstraZeneca (NYSE: AZN).** Dynavax will receive milestone payments as both compounds reach successive successful endpoints as well as royalty payments should they attain approval and market distribution.

The Turnaround Story:

The stock ran up to almost $50 a share in late 2012 on the anticipation of the approval of Heplisav-B. Unfortunately that is where the company ran into a roadblock. Even though results from its Phase III trials were encouraging, neither the FDA nor its European equivalent would grant approval of the compound. Both agencies cited that there were not enough test subjects in these studies to provide confidence in the efficiency and safety needed to approve Heplisav-B.

It is important to note that the FDA **did not** say this compound was ineffective, just that it needed a larger sample size for Phase III trials to be approved. Dynavax has spent the better part of a year enrolling more than 8,000 patients in a new Phase III study for Heplisav-B which should be completed by October of 2015.

The enrollment for the study was completed in late 2014 and the stock has behaved more strongly as a result. Also helping the shares is the news that **Arrowhead Research Corporation (Nasdaq: ARWR)** just posted disappointing results with that company's experimental hepatitis B drug in Phase II trials.

Obviously the biggest catalyst for Dynavax would be the approval of Heplisav-B. The stock ran up to $50 a share in anticipation of approval previously so logically a floor if approved would be $50 a share. I like the risk/reward of this stock at current levels and want to overlay my own risk mitigation strategy on this position as well.

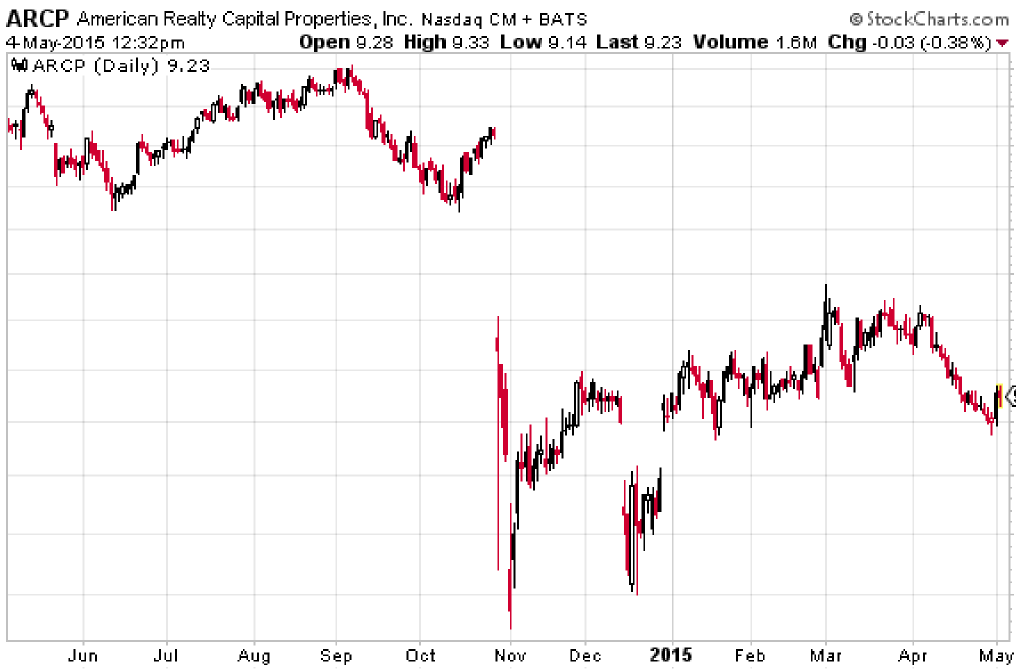
We are not putting a price target on Dynavax Technologies Corp., but "Jensen's rules" for biotech investing do apply. This strategy consists of selling 10% of your original stake once a 50% gain has been achieved, 20% if the stock doubles off your entry point and 20% more if the stock triples. This way one books a guaranteed profit while retaining half their original stake riding on the "house's" money. I have found it to be prudent way to invest in this inherently volatile space.

## An Accounting Error Gives Us the Entrance We Need

Finally, let's talk about the only high yield play within my personal turnaround portfolio. It is a real estate investment trust (REIT) named **American Realty Capital Partners (Nasdaq: ARCP).** American is the largest single tenant REIT in the country by square footage.

**American Realty Capital Partners (Nasdaq: ARCP)**
Berkeley, CA, USA
http://www.arcpreit.com
Last: $9.23
Capitalization: $8.4 billion
Market Sector: Financial, REIT

The shares plunged some 40% on a combination of announcements all originating from the same event. The REIT announced in late October that it had some accounting misstatements which caused the S.E.C. to open an investigation, a rash of analyst downgrades and **RCS Capital (NYSE: RCAP)** then backed out of its agreement to buy American's private capital-management business Cole Capital for $700 million.



share price: can you spot when the announcement of the investigation was made?

The shares have recovered somewhat recently to around $9.50 a share as lenders have given it some breathing room on existing debt covenants until American can file correct audited statements in early January. Shares had been trading at approximately $12 before this issue came up. It also appears that the restatements will only knock about a nickel a share from first half AFFO (Adjusted Funds from Operations), material but not life threatening.

It is going to be a challenging year as the company works through the ramifications of accounting misstatements. I expect it to settle with the S.E.C. for a minor amount. It is also suing RCS Capital for backing out of the deal to buy Cole Capital and I also expect some negotiated settlement to reach a revised agreement on that sale sometime in 2015.

The REIT was already selling at a 30% to 40% discount to its biggest competitors **Realty Income Corporation (NYSE: O)** and **National Retail Properties (NYSE: NNN)** based on forward AFFO. A good portion of that discount is due to American's Chairman and until recently its CEO. He has been perceived by the street as overcompensated and riddled with conflicts of interest. He is also the chairman of RCS Capital to which Cole Capital was being sold.

I think one positive result as this REIT works through the aftermath of this fiasco is that he will be given the boot and American's new well-regarded CEO will take full charge of the REIT. This will remove a huge overhang from the stock and help start to narrow its valuation discount.

The company's portfolio is in fine shape and is over 99% leased with the average tenant contract running north of a decade with built-in annual rent increases. 46% of its tenant base is investment grade credit quality, higher than peers and the company has a solid balance sheet with staggered debt maturities. After the shares' plunge, the REIT is selling approximately 20% below book value and significantly under its true net asset value as well. The REIT could basically sell properties into a pretty robust commercial market and use the proceeds to buy back shares to drive significant shareholder value.

The shares also yield some 11% annually and the company pays dividends monthly. The market seems to be pricing in a major cut in the dividend payout which I believe is highly unlikely. Over the next year as management works through these recent issues I expect the stock to return to the $12 a share level it sold for before these negative events and move higher. Plus you get a nice double digit yield along the way.

***Positons: Long ARCP, DVAX, FCH***