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New Rec: Diamond Foods (DMND: $90.37) Sept. 25, 2011

Position: Sell **Target: $43**

$MM	FQ411a	FQ112e	FQ212e	FQ312e	FY11a	FY12e	FY13e
Revs	232.8	271.9	515.0	563.0	965.9	1,934.8	2,552.6
EPS $	$0.52	$0.70	$0.83	$0.55	$2.61	$2.75	$3.18
Y/Ygr	55%	8%	-9%	6%	36%	5%	16%
PE	na	na	na	na	34.7	32.9	28.4
PSR	na	na	na	na	2.1	1.1	0.8
Consen	na	$0.74	$0.94	$0.72	Na	3.14	3.73

Shares Out: 22.6M **Market Cap: $2.0B** **FYE: July 31**

Concept:

1. Diamond appears to be losing its dominant position in the walnut industry. As a result, its business model is deteriorating and its profitability is under pressure.

2. Company profitability also appears to be overstated due to accounting treatment of a prospective "momentum payment" paid to walnut growers in September of 2011, which may be in lieu of a retrospective payment.
3. As purchase agreement with walnut suppliers signed at the time of the IPO expire, DMND risks losing suppliers due to its practice of paying discounted walnut prices, or its cost of goods sold will rise.
4. Integration risks inherent in Pringles acquisition.
5. Earnings estimates appear to be too high. We estimate the company will earn non-GAAP EPS of $2.75 in FY 2012 and $3.18 in FY 2013, which compared unfavorably to the "street's" estimates of $3.14 for FY 2012 and $3.73 for FY 2013.
6. On a P/E and EV/EBITDA basis, we think the shares might trade at about $43.

Summary: Diamond of California was founded in 1912 as a walnut cooperative. In 2005, the members of the cooperative elected to IPO the entity, which then became Diamond Foods. At the time of the IPO, the company was buying about 300 million lbs of walnuts and selling about 150 million lbs of walnuts. Note that as a walnut "handler," Diamond sells a portion of its walnuts "in-shell" and a portion of its walnuts "shelled," which means the nut has been broken and the meat has been extracted. Typically, a lb of walnuts in shell is processed into about 0.4 lbs of shelled walnuts. After the IPO, the approximately 1,700 members of the cooperative became Diamond Foods' primary walnut suppliers, the vast majority of which entered into supply agreements for either 3, 5 or 10 years. Since going public, Diamond has grown revenue at a CAGR of 15% from FY 2006 to FY 2011, mainly through acquisition. The company has diversified its product offering by buying Pop Secret and Kettle Foods, adding microwave popcorn and potato chips.

By our account, pro-forma revenue CAGR would have been only about 3.6% if Pop Secret and Kettle Foods had been acquired at the beginning of FY 2006. Despite diversifying, walnuts still remain a significant component of both sales and expenses. Based on our discussion with industry participants, we think Diamond bought about 277 million pounds of walnuts in its FY 2011.

Diamond's supply agreements stipulate that Diamond must, in good faith, pay its walnut growers fair value for their crops. Since the walnut market is transparent to the participants, growers think fair value equals the market clearing price. However, we are told that from the time it became a public company through its FY 2010, Diamond paid its growers about $0.10-$0.15/lb less than fair market price for walnuts. When selling walnuts for about $1.00/lb, a $0.10-$0.15 difference is very significant to growers. Some of Diamond's growers explored the possibility of filing a class action suit in 2007, but their agreements with Diamond stipulated that any disagreement on price would have to be settled in arbitration. Most of the growers run small operations, and, as such, do not have the resources to hire attorneys and go through the arbitration process. Some observers

think Diamond relied on this dynamic to enable it to take unwelcome discounts from the growers.

Diamond has enjoyed a very dominant position in the walnut business. That dominance appears to be coming to a close, and Diamond should be increasingly challenged to make money in the walnut business. Management undoubtedly understands the problem. As a result, management has been acquiring companies to diversify and grow its business. However, we think that the diversification will be unable to compensate for increasing challenges Diamond will face in its core walnut business. This difficulty may also be behind some potential accounting issues, which we discuss, below.

Importantly, many grower contracts signed after the IPO have either recently expired or will expire in the next few years. Some growers have already stopped supplying Diamond. However, due to increased crop yields over the last several years, it appears Diamond's walnut supply has remained relatively consistent. Sources tell us that while Diamond bought about 40% of the walnut harvest around the time it went public, but now only buys about 28% of the harvest. Unfortunately for Diamond, crop yields are forecasted to decline for its FY 2012. Unlike years ago, when farmers relied on the ability of Diamond to ensure they could sell their entire crops, today there are countless companies going door to door, offering to buy crops at favorable prices and favorable terms (i.e. fast payments). In addition, it appears that some growers, themselves, are becoming handlers of their own crops and are eliminating middlemen by going more directly to buyers. This is indicative of how the industry is changing and of how Diamond is losing some of the control it had over its supply. Walnut demand is skyrocketing due to increased consumption in the US, China, the Middle East, and Europe. Yet, Diamond has continued to treat its farmers as if they need Diamond more than Diamond needs the farmers. This appears to be damaging its grower relationships.

For its FY 2011, sources tell us that Diamond increasingly leveraged its market position. For walnuts harvested in the fall of 2010 (and sold over the next year), we are told that the market price was about $1.45/lb on average. However, sources tell us that Diamond paid its growers only about $1.00/lb, or $0.45/lb less than the market price. Understandably, the growers were upset when they found out in August of 2011, the month in which growers receive notice on the final value adjustments for their Fall 2010 harvests. To put this in perspective, this means DMND may have paid about $125 million less than fair market value for its walnuts, based on an estimated 277 million lbs of walnuts. This compared to Diamond's FY 2011 reported operating profit of $109 million and reported pre-tax income of $86 million. Had the company paid market prices for its walnuts, it may have made only about $0.18 of EPS in FY 2011. Had Diamond paid a $0.10/lb

discount to market value, close to its historical discount, we estimate it would have made only $1.14 in FY 2011.

In September or 2011, Diamond's walnut growers received an unusual so-called "momentum payment." This payment amounted to an estimated $0.30-$0.40/lb, and appeared to be calculated based on walnuts delivered to Diamond during its FY 2011, based on our discussions with industry sources. There was significant consternation in the walnut community about this payment, which none of the growers expected, but the consensus is that, even though it was called a "momentum" payment," implying that it was for some benefit to be received by Diamond in the future, in reality it was to mollify and to compensate the growers in arrears for the crops delivered to Diamond in late 2010. Some think this payment has prevented growers from pursuing market enforcement to get fair value for their crops. Even after the momentum payment, growers assert they still did not receive fair value for their prior year harvest.

Based on our analysis, we question whether Diamond included this "momentum payment" in its cost of goods sold for its FY 2011, which ended on July 31. At $0.35/lb, the momentum payment may have amounted to about $97 million of additional costs related to the CY 2010 walnut harvest, at least half of which we think would be sold in Diamond's FY 2011. If included in FY 2011 results, we estimate this "momentum payment" would have reduced Diamond's FY 2011 reported non-GAAP reported EPS from $2.61 to only about $1.14. Interestingly, Diamond waited until September to make this payment, which is the 2nd month subsequent to the end of its fiscal year. Typically, auditors conduct cut-off procedures for about a month subsequent to a fiscal period. Cut-off procedures are designed to ensure payments made subsequent to the end of a fiscal period are expensed in the prior fiscal period, if applicable. While it appears that most growers of whom we are aware think that this payment should go towards the 2010 harvest, it is unclear that Diamond included this payment in its costs of goods sold for FY 2011. There maybe good reason for that, as we discuss below.

Interestingly, Diamond is in the process of buying Pringles from Proctor & Gamble. In the most recent S-4, which was filed around the time Diamond sent the "momentum payments" Diamond increased its estimate for integration costs by $50 million from $100 million to $150 million, or by about the amount of the estimated momentum payments. Could there be a relationship between the momentum payments and the increase in the integration cost estimate, which will probably be labeled "one time costs?"

In April of 2011, Diamond announced a deal to acquire the Pringles operation from Proctor & Gamble. The deal is being structured as a "Reverse Morris Trust" transaction, which is tax favorable for P&G shareholders, who can

elect to receive Diamond shares in exchange for their P&G shares. The purchase price was set at 29.1 million Diamond shares, plus an assumption of debt from P&G of between $700 million and $1.05 billion, depending on Diamond's share price during a period prior to the commencement of the exchange offer. At Diamond's current share price of about $90, the value of the deal is about $3.3 billion, or nearly 14X Pringles' EBITDA for the FY ended June 30 2011.

There are numerous risks to the Pringles transaction. Most importantly, Diamond investors appear to be willing to pay up for earnings growth. Yet, Pringles is not a growth company. Pringles revenue was up 6% for its recently reported fiscal year on a volume increase of 7%. However, this was against easy comparisons from 2010, when Pringles revenues were down -2% and volumes were down -5%. Comps should get more difficult and Pringles annual revenue growth is likely return to its long-term average of just 2%-3%. For investors focused on profits, Pringles' gross and operating margins have recovered to about peak levels, so margin expansion will likely be difficult to achieve. Pringles is a small player with a mature product, participating in a very competitive snack market dominated by Frito Lay. Apart from weak growth prospects, we think there may be significant risks to integrating the companies, both from a logistics standpoint and a cultural standpoint.

Earnings estimates appear too high. We think Diamond will be unable to pass through the much higher than reported walnut costs that we think it will experience in the future, resulting in much lower margins. With the company trading at 29X FY 2012 and 24X FY 2013 consensus EPS, we think even small earnings misses should mean major downside for the shares. If we are correct in our assessment of these "momentum" payments, the company conceivably might even be forced to restate its FY 2011 financial statements and possibly report a revised EPS of only around $1.14. In our opinion, whatever the outcome of this particular issue, there are many red flags flying, and we think our estimate of $1.14 EPS reflects the real underlying earnings power of the existing business. And, regardless of the accounting, we think Diamond as it stands today is worth only about 15X its real economic EPS of $1.14, or about $17/share.

Including Pringles, we think Diamond will only make about $2.75 in FY 2012 and $3.18 for FY 2013. This compares unfavorably to the "street" which thinks Diamond will make $3.14 in FY 2012 and $3.73 in FY 2013. Based on our analyses, it appears both Diamond as it exists today and Pringles are growing revenues in just low single digits on a pro forma basis over the long term. As such, long term earnings growth will likely be unimpressive as well, and we think the shares should trade at about a market multiple of 13X our FY 2013 EPS estimate, suggesting a share value of about $41. When valued at 10X EV/FY 2013 OWS

estimated EBITDA, the shares should trade around $45. Using the blended average, we recommend investors sell Diamond shares with a $43 price target.

Borrow Information: Below is reported data. However, our discussions with stock loan professionals indicate that substantially more shares may be available to borrow.

Supply Quantity	Quantity On Loan	Available to Borrow	Date
21.4	8.0mm	1.3mm	9/25/11

Source: Data Explorers

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Background:

Diamond Foods, Inc. was incorporated in Delaware in 2005 as the successor to Diamond Walnut Growers, Inc., a member-owned California agricultural cooperative association. In July 2005, Diamond Walnut Growers, Inc. merged with and into Diamond Foods, Inc., converted from a cooperative association to a Delaware corporation, and completed an initial public offering of Diamond Foods' common stock.

When Diamond was operating as a cooperative, it would seek to sell walnuts on behalf of the growers with the intent to maximize gross revenue. From gross revenue, Diamond took a cut to cover marketing and administrative expenses, and on average returned Diamond growers about a $0.03/lb premium to the market price for walnuts (over the last ten years prior to becoming a public company). In conjunction with the conversion to becoming a public company, Diamond offered the cooperative's members 3, 5, and 10 year purchase agreements. Under these agreements, the growers are obligated to deliver their entire walnut crop to Diamond during the fall harvest season and Diamond determines the minimum price for this inventory by March 31, or later, of the following calendar year. The final price is determined no later than the end of the Company's fiscal year, which ends July 31. Since the ultimate price, which Diamond is to determine in good faith, will be determined subsequent to receiving the walnut crop, Diamond makes an estimate of price for interim financial statements. Sources tell us that Diamond makes its first payment toward the crops in November, in the middle of the harvest (September-December), and makes the remainder of the payments through August of the following calendar year. We have been told that at least 95% of former cooperative members opted into marketing agreements with Diamond, most of which appear to be for five years.

At the time of the conversion to becoming a public company, Diamond's only business was nuts. It was purchasing nearly 300 million lbs of nuts annually, some that it sold in-shell (unprocessed) but most that it de-shelled, or "shelled", to be sold the meat. As a general rule, each lb of in-shell walnuts yields about 0.4 lbs

of walnut meat. The processor of the nut is known as a "handler". There are about 70 handlers in the Central California valleys, which account for nearly all of the domestic walnut production. Since going public, Diamond has expanded its brands through acquisition. In September 2008, Diamond acquired the Pop Secret brand of microwave popcorn products. In March 2010, Diamond acquired Kettle Foods, a premium potato chip company in the two largest potato chip markets in the world, the United States and United Kingdom.

In April of 2011, Diamond announced a deal to acquire the Pringles operation from Proctor & Gamble. The purchase price was set at 29.1 million Diamond shares, plus an assumption of debt from P&G of between $700 million and $1.05 billion, depending on Diamond's share price during a period prior to the commencement of the exchange offer. At the time the deal was struck, Pringles was valued at $2.35 billion based on Diamond's then share price and the amount of debt it would have to assume from P&G, or at about 9.7X Pringles EBITDA for the FY ended June 30, 2011. The deal will more than double the size of Diamond, with P&G shareholders owning about 57% of the combined company. Since the deal was priced, Diamond shares have appreciated by about 75%. Based on this appreciation, it appears Diamond will have to assume the minimum amount of debt from P&G, or $700 million. At Diamond's current share price of about $90, the value of the deal is now about $3.3 billion.

Diamond sells its products to global, national, regional and independent grocery, drug and convenience store chains, as well as to mass merchandisers, club stores and other retail channels. The company has three produce lines including "Snack," "Culinary and Retail In-shell," and "non-retail." The "Snack" product line sells products under the Emerald, Pop Secret, and Kettle brands. Emerald products include roasted, glazed and flavored nuts, trail mixes, seeds, dried fruit and similar offerings packaged in innovative re-sealable containers. Pop Secret products consist of microwave popcorn offered in a variety of traditional flavors. Kettle Foods products consist mainly of premium potato chips and tortilla chips. The company's snack products are typically available in grocery store snack, natural and produce aisles, mass merchandisers, club stores, convenience stores, drug stores, natural food stores and other places where snacks are sold. Diamond's "Culinary and Retail In-shell" products include culinary nuts sold under the Diamond of California brand. Culinary nuts are marketed to individuals who prepare meals or baked goods at home. "Non-Retail" products include international markets and North American ingredient customers. Diamond market ingredient nuts internationally under the Diamond of California brand to food processors, restaurants, bakeries and food service companies and their suppliers.

Walnuts are the company's most significant raw material. Based on our research, we think Diamond bought about 277 million lbs of walnuts in its FY

2011. All of Diamond's walnuts are purchased from California. Diamond obtains the majority of its walnuts from growers under long-term supply contracts struck at the time of its IPO. A small portion of the company's walnuts is purchased from other California walnut processors. Diamond purchases its other nut requirements from both domestic and international processors on the open market. Diamond buys Brazil nuts from the Amazon basin, cashew nuts from India, Africa, Brazil and Southeast Asia, hazelnuts from Turkey, and pine nuts from China and Turkey. Diamond sources corn from the United States and Argentina and potatoes from the United States and UK for its non-nut products.

Discussion:

1. Walnut growers are increasingly disenchanted, as Diamond has always taken discounts for walnuts, but never as much as in 2011.

Industry sources tell us that, since becoming a public company, Diamond has consistently paid its walnut growers $0.10-$0.15/lb less than fair market values for walnuts. Sources in the grower community tell us that this contrasts with agreements signed between Diamond and the growers around the time Diamond went public, that Diamond must, in good faith, pay the growers fair value for their crops. Grower agreements, which were signed for periods of 3, 5, or 10 years stipulated that any disagreement on price would have to be settled in arbitration. Since most of the growers run small operations, they do not have the resources to hire attorneys and go through the arbitration process. Some observers think Diamond relied on this dynamic to take advantage of the growers. Diamond, on the other hand, may have believed it was entitled to a "volume" discount, and was in a position to take it somewhat unilaterally.

Walnut prices have fluctuated between $0.64/lb and $1.15/lb from 2006 to 2010, based on USDA data, so $0.10-$0.15/lb significantly impacts a grower's income. This discount has allowed Diamond to make handsome returns, which we discuss in detail in discussions point 2. However, also as a result of paying its growers discounted prices for their crops, Diamond has lost significant walnut market share, as growers have opted to sell elsewhere as their contracts with Diamond have expired. Based on discussions with industry participants, we think Diamond's walnut market crop share has declined from about 40% around the time of its IPO to about 28% for the crop harvested between September and December of 2010.

Table 1: Estimated Diamond market share:

	Acres*	Tons/acre*	Change in yield/acre	US production (millions lbs)	**Estimated Diamond walnut demand (millions lbs)	**Est Diamond market share
2001	204,000	1.50		610	289	47%
2002	210,000	1.34	-10%	564	260	46%
2003	213,000	1.53	14%	652	296	45%
2004	214,000	1.52	-1%	650	294	45%
2005	215,000	1.65	9%	710	287	40%
2006	216,000	1.60	-3%	692	279	40%
2007	218,000	1.50	-6%	656	262	40%
2008	223,000	1.96	30%	872	313	36%
2009	227,000	1.93	-2%	874	283	32%
2010	227,000	2.22	15%	1,006	277	28%
2011e	227,000	2.14	-4%	970	246	25%

*- per USDA
**- based on discussions with industry participants

Unlike many years ago when farmers relied on Diamond to ensure they could sell their entire crops, today many companies go door-to-door, offering to buy crops at favorable prices and favorable terms. For instance, Diamond remits the first payment to its growers in the November during the harvest, but most of the payments to the farmers are not remitted until March through August of the following year. With growing walnut demand, we hear that many buyers are now offering much quicker payments, with some even paying up in advance of the harvest. Walnut demand is skyrocketing due to increased consumption in the US, China, the Middle East, and Europe. Yet, Diamond appears to have continued to treat its farmers as if they need Diamond more than Diamond needs the farmers.

For its FY 2011, it appears that Diamond leveraged its market position by an extraordinary amount. For walnut crops harvested in the fall of 2010 (and sold by Diamond during its FY 2011), we are told that the market price for walnuts was about $1.45/lb on average. However, sources tell us that Diamond paid its growers only about $1.00/lb, or $0.45/lb less than the market price. Understandably, growers were very upset when they found out the final price in August of 2011, the month in which growers receive notice on the final value adjustments for their Fall 2010 harvests. It appears that, subsequently, in September of 2011, Diamond paid growers a "momentum payment," which at least partially compensated for this deep discount, and which we discuss in detail in discussion point 3.

Table 2: Estimated discounts taken by Diamond for walnuts

Crop harvested Oct-Dec	Est. DMDN walnut offtake (millions lbs)	Estimated discount to fair market value/lb**	Estimated payment discount**	Cumulative estimated payment discount
2006	279	$(0.125)	(34.8)	(34.8)
2007	262	$(0.125)	(32.7)	(67.6)
2008	313	$(0.125)	(39.1)	(106.7)
2009	283	$(0.125)	(35.4)	(142.1)
2010	277	$(0.45)	(124.8)	(266.9)

*- OWS estimated bases on discussions with industry participants
**- calculation based on midpoint of $0.10-$0.15/lb discount growers assert they have been paid by Diamond for crops harvested from 2006 to 2009. Calculation of 2010 based on $0.45/lb discount they assert was taken by Diamond in 2010

Based on our analysis, we think Diamond bought about 277 million pounds of walnuts from September through December of calendar 2010, or during its 1H FY 2011, which began on August 1, 2010. Assuming a discount of $0.45/lb, which is what our sources claim Diamond took in 2011, it would mean Diamond saved up to $125 million for the crop harvested in late calendar 2010 by taking this extraordinarily large discount. Had Diamond taken its usual discount of about $0.125/lb for walnuts, it would have paid $90 million more for the CY 2010 crop, based on our analysis. We think Diamond may have taken discounts totaling about $267 million since its IPO. It is no wonder many suppliers are disenchanted with Diamond. As Diamond loses market power as a result of its contracts with the growers rolling off, and due to increasing walnut demand, it seems that there will come a time, and perhaps soon, when it will be unable to take any discount at all.

2. Were DMND to have to pay full market value, it would have a significant impact on its results.

As detailed above in table 2, our analysis suggests Diamond took discounts for walnuts of $39 million for the CY 2008 harvest, $35 million for the CY 2009 harvest, and, extraordinarily, $125 million for the CY 2010 harvest. The company uses FIFO accounting and sells its walnuts over the following 12-14 months after receiving them. The CY 2008 harvest occurs in 1H FY 2009. Product from the CY 2008 harvest is sold in FY 2009 and FY 2010. For purposes of our analysis, we assume 50% of the CY 2008 harvest is sold in FY 2009 and 50% is sold in FY 2010. We apply the same methodology to the CY 2009 and CY 2010 harvests.

Table 3: Pro forma earnings results assuming Diamond paid fair market value for walnuts, based on OWS analysis:

FYE ended July 31	FY 2010	FY 2011
Reported non-GAAP results M$		
Pre-tax income	54.345	85.932
Income taxes	17.564	26.897
Net income	36.781	59.035
EPS	$1.91	$2.61
Estimated pre-tax net income assuming Diamond paid fair market value for its walnuts		
Adjustment for discount for CY 2008 walnut purchases*	19.55	-
Adjustment for discount for CY 2009 walnut purchases*	17.70	17.70
Adjustment for discount for CY 2010 walnut purchases*	-	62.40
Total est walnut adjustments to fair value	37.25	80.1
Non-GAAP pre-tax net income assuming DMND paid FMV for walnuts	17.10	5.83
Income taxes	5.53	1.83
Estimated earnings as	11.57	4.01
EPS	$0.60	$0.18
Shares	19.215	22.642
Tax rate	32%	31%

*- The CY 2008 walnut harvest, which occurs early in Diamond's FY 2009, is sold during the company's FY 2009 and FY 2010. The CY 2009 harvest, which occurs early in Diamond's FY 2010, is sold during the company's FY 2010 and FY 2011. The CY 2010 harvest, which occurs early in Diamond's FY 2011, is sold during the company's FY 2010 and FY 2011.

Diamond reported non-GAAP EPS of $1.91 for FY 2010 and $2.61 for FY 2011. All in, it appears Diamond may have saved a total of about $37 million in costs of goods sold in FY 2010 and $80 million in costs of goods sold in FY 2011 by paying less than fair market value for its walnuts. This compares to Diamond's reported non-GAAP pre-tax income of $54 million in FY 2010 and $86 million in FY 2011. Our analysis suggests that if Diamond had paid fair market value for walnuts, it would have reported EPS of only $0.60 for FY 2010 and $0.18 for FY 2011.

Overall, the company has about one quarter worth of inventory on hand at the end of each FY, which could suggest up to 75% of the walnut crop may be sold in the fiscal year in which it is purchased. However, we think the inventory of walnuts may be higher as a percent of total inventory at year end, as the company typically does not stockpile other products such as other types of nuts, corn, and potatoes. To the extent the company sells more of its walnuts in the fiscal year in

which it purchases them, it would further reduce our EPS estimate for FY 2011, assuming the company paid fair market value for walnuts.

3. DMND's accounting treatment for an extraordinary "momentum payment" may have obscured real profitability in 2011.

As detailed above, we think Diamond paid its walnut growers about $0.45/lb less than market value for walnuts harvested in late CY 2010. While the growers had been accustomed to receiving discounted prices for their walnuts from Diamond, the magnitude of the estimated $0.45/lb discount stunned the growers. In September of 2011, however, Diamond's walnut growers received an unusual so-called "momentum payment." Industry sources tell us this payment amounted to an estimated $0.30-$0.40/lb, and they believed it to have been calculated based on walnuts delivered to Diamond between September and December of 2010, or during the first half of Diamond's FY 2011.

There was significant consternation in the walnut community about these so-called "momentum payments," which none of the growers expected, but the consensus seems to be that, even though it was called a "momentum" payment," implying that it was for some benefit to be received by Diamond in the future, in reality it seems that it was meant to mollify and to compensate the growers for the crops delivered to Diamond in late 2010. The "momentum payment" of about $0.35/lb appears to have brought the effective purchase price for the CY 2010 harvest to around $1.35/lb, or to within about a $0.10 discount to the market price of about $1.45/lb, which appears to be consistent with Diamond's historical discount.

Interestingly, Diamond waited until September to make this payment, which is the 2nd month subsequent to the end of its fiscal year. Typically, auditors conduct cut-off procedures up to about a month subsequent to a fiscal period. Cut-off procedures are designed to ensure payments made subsequent to the end of a fiscal period are expensed in the prior fiscal period, if applicable. It appears that this "momentum payment" was not included in the cost of the CY 2010 harvest.

Given that the company purchased an estimated 277 million lbs of walnuts from the CY 2010 harvest, we think these momentum payments probably amounted to about $97 million in total (at $0.35/lb). Assuming Diamond would have sold an estimated 50% of the CY 2010 harvest in its FY 2011, treating the "momentum payments" as expenses post FY 2011, likely would have benefited Diamond by about $48.5 million in FY 2011.

Table 4: Pro forma earnings results assuming Diamond included the estimated "momentum payments" in the cost of the CY 2010 harvest:

FYE July	FY 2011
Reported non-GAAP results	
Pre-tax income	85.9
Income taxes	26.9
Net income	59.0
EPS	$2.61
Estimated impact of including the "momentum payments" in the cost of the CY 2010 harvest	48.5*
Non-GAAP results adjusted to account for momentum payment	
Pre-tax income	37.4
Income taxes	11.7
Net income	25.7
EPS	$1.14

*- based on selling 50% of the harvest in the fiscal year Diamond takes delivery. The CY 2010 harvest, which occurs early in Diamond's FY 2011, is sold during the company's FY 2010 and FY 2011.

If the momentum payment had been included in the cost of the CY 2010 harvest, we estimate it would have reduced pre-tax income by about $48.5 million. While the company reported FY 2011 non-GAAP EPS of $2.61 for FY 2011, we think FY 2011 non-GAAP EPS would have been only about $1.14 if the "momentum payments" were accounted for in the cost of the CY 2010 harvest.

4. Description and risks of Diamond's acquisition of Pringles

In April of 2011, Diamond announced a deal to acquire the Pringles operation from Proctor & Gamble. The deal is being structured as a "Reverse Morris Trust" transaction, which is tax favorable for P&G shareholders, who can elect to receive Diamond shares in exchange for their P&G shares. The purchase price was set at 29.1 million Diamond shares, plus an assumption of debt from P&G of between $700 million and $1.05 billion, depending on Diamond's share price during a period prior to the commencement of the exchange offer. At the time the deal was struck, Pringles was valued at $2.35 billion based on Diamond's then share price and the amount of debt it would have to assume from P&G, or at about 9.7X Pringles EBITDA for the FY ended June 30, 2011. The deal will more than double the size of Diamond, with P&G shareholders owning about 57% of the combined company. Since the deal was priced, Diamond shares have appreciated by about 75%. Based on this appreciation, it appears Diamond will have to assume the minimum amount of debt from P&G, or $700 million. At Diamond's current share price of about $90, the value of the deal is now about $3.3 billion, or nearly 14X Pringles' EBITDA for the FY ended June 30 2011.

Table 5: Pringles deal price:

	At time deal was struck	Current
Diamond share price	$51.47	$90.37
Shares to be exchanged	29.1	29.1
Share exchange value	1,498	2,630
Estimated debt assumption	850	700
Total deal value	2,348	3,330
Pringles FY 2011 EBITDA	243	243
Pringles valuation EV/EBITDA	9.7	13.7

Source: company filings and acquisition agreements. Debt assumption of $700 estimated based on current DMND share price.

We think there are numerous risks to the Pringles transaction. Most importantly, Diamond investors have been paying up for growth. Yet, Pringles is not a growth company. Pringles revenue was up 6% for its recently reported fiscal year on a volume increase of 7%. However, this was subsequent to easy comparisons from 2010, when Pringles revenues were down -2% and volumes were down -5%. And although we do not have volume information for FY 2009, Pringles revenue was down -9%, so volume was likely down materially too. Comps should get more difficult and Pringles annual revenue growth is likely return to its long-term average of 2%-3%.

Table 6: Pringles Historical results:

FY end June 30	2006	2007	2008	2009	2010	2011
Revenue	1,298.3	1,339.3	1,534.4	1,396.4	1,367.4	1,455.7
COGS	830.2	890.9	1,077.9	1,049.3	886.9	924.0
Gross Profit	468.1	448.4	456.5	347.1	480.5	531.7
R&D	na	na	na	23.6	22.7	22.3
Advertising costs	na	na	na	66.6	100.5	105.8
Other SG&A costs	na	na	na	189.6	190.9	205.4
SG&A	297.3	301.5	334.9	279.8	314.1	333.5
Other ope expenses	(1.6)	1.0	(0.2)	7.4	(0.5)	0.8
Operating profit	172.4	145.9	121.8	59.9	166.9	197.4
D&A	Na	na	na	74.2	46.5	45.9
EBITDA	Na	na	na	134.1	213.4	243.3
Gross margin	36%	33%	30%	25%	35%	37%
Operating margin	13%	11%	8%	4%	12%	14%
Y/Y rev growth	na	3%	15%	-9%	-2%	6%
Revenue CAGR 2006-2011	na	na	na	na	na	2.3%
Volume	na	na	na	na	-5%	7%
Price	na	na	na	na	2%	-2%
Mix	na	na	na	na	1%	1%

Source: Data per Diamond S-4 related to Pringles acquisition

For investors focused on profits, Pringles' gross and operating margins have recovered to about peak levels, so margin expansion will likely be difficult to achieve. Pringles is a small player with a mature product, participating in a very competitive snack market dominated by Frito Lay. Frito Lay generates about $13 billion of revenue annually and holds an estimated 45% market share. Frito Lay owns upwards of 50 brands, including Lays, Doritos, Tostitos, Cracker Jacks. Based on our research, it appears Pringles has about 8%-10% market share in the snack market.

Apart from weak growth prospects, integrating the two companies could be challenging. The Pringles acquisition will increase Diamond's revenues by about 150%, so there could be significant risks to results if the integration goes awry. Integrating the cultures of Diamond and Pringles could be difficult, with Diamond's entrepreneurial environment possibly clashing with a more institutionalized Pringles' management structure.

5. Pro forma growth analysis shows slow core business growth

Diamond has grown reported revenue at a CAGR of 15% from FY 2006 to FY 2011. However, two major acquisitions have contributed significantly to this growth rate. Diamond acquired Pop Secret on September 15, 2008 for $190 million in cash. Based on Diamond's pro-forma disclosures, Pop Secret would have contributed $103 million to revenue in Diamond's FY 2008, which ended just prior to the acquisition. This means Diamond paid about 1.9X sales for Pop Secret. Diamond acquired Kettle Foods on March 31, 2010 for $615 million in cash. Based on the pro-forma disclosures, Kettle would have added $258 million of revenue to Diamond's FY 2009, had it been acquired at the beginning of Diamond's FY 2009 and not in the middle of Diamond's FY 2010. This means Diamond paid about 2.4X trailing revenue for Kettle Foods.

Table 7: OWS estimates for pro-forma revenue assuming Pop Secret and Kettle Foods were acquired at the beginning of Diamond's FY 2006:

FY	2006	2007	2008	2009	2010	2011	5 Year CAGR
Reported revenue	477.2	522.6	531.5	570.9	680.2	965.9	15.10%
Pop Secret	85.4**	94.0**	103.4*	13.5*	-	-	na
Kettle Foods	245.1**	269.6**	296.6**	257.9*	174.4*	-	na
Estimated pro forma revenue	807.8	886.2	931.5	842.4	854.6	965.9	3.64%
Y/Y %	2006	9.7%	5.1%	-9.6%	1.4%	13.0%	na

*- calculation based on Diamond Foods pro-forma disclosures

**- OWS estimated revenue for Pop Secret and Kettle Foods in years prior to available financial information.

Based on our analysis in Table 7, we think Diamond's 5 year revenue CAGR would have been only about 3.6% if it had owned Pop Secret and Kettle Foods since the beginning of 2006. This would likely surprise investors, who generally regard Diamond as a growth stock. It appears much of the recent revenue growth may be due to easy comparisons. While pro-forma revenue was up 13% for FY 2011, we think cumulative pro forma revenue growth was only about 3.5% from the time that our pro forma revenue estimate last peaked in FY 2008 at $932 million, again assuming Diamond and Pop Secret had been owned the entire time.

6. Recent results

Diamond recently reported FQ4 and FYE 2011 results. Diamond reported $2.61 of non-GAAP EPS for the year, which compares to GAAP EPS of $2.22. The company excludes acquisition and related expenses to get to its non-GAAP EPS. The company issued revenue guidance of $1.85-$1.95 billion for FY 2012, which includes about 2.5 quarters from the Pringles acquisition, expected to close in mid December. The company raised its earnings guidance for FY 2012 from $3.00-$3.10 to $3.05-$3.15. Guidance for EBITDA (excluding integration costs) is for $300mm-$310mm. Guidance excludes integration and acquisition related costs, which will be $150 million, an increase from $100 million previously. We wonder about this increase, which was disclosed at around the same time as the momentum payments were made. The company will argue that this $150million is a one-time charge that investors should ignore.

The company guided to operating margins of 11.5%-12% for FY 2012 (excluding acquisition and integration costs), which appears to be below most sell side estimates of 12%-13%. Advertising spend is expected to be higher than the "street" anticipated. The company guided to interest expense of $40-$45 million which was less than "street" estimated, which appears to have been $50M-$55M. Most importantly, in our opinion, a lower assumed tax rate appears to have added $0.10-$0.12 to earnings. Investors chose to ignore this lackluster guidance, and instead appeared focused on accretion from the Pringles transaction.

7. Risks to thesis:

The biggest risk to our thesis is if the company is able to increase its market share in the walnut business and continue to buy its walnuts at significant discounts to market prices. However, we think the walnut business is structurally changing and consider this to be an unlikely outcome.

A secondary risk to our thesis is if the company can generate materially higher operating margins than we are modeling. Given the level of competition in the company's industries, we also consider this to be unlikely.

8. OWS valuation & model

Earnings estimates appear too high. We think Diamond will be unable to pass through the much higher than reported walnut costs that we think it will experience in the future, resulting in much lower margins. With the company trading at 29X FY 2012 and 24X FY 2013 consensus EPS, we think even small earnings misses should mean major downside for the shares. If we are correct in our assessment of these "momentum" payments, the company conceivably might even be forced to restate its FY 2011 financial statements and possibly report a revised EPS of only around $1.14. Under this scenario, depending on the timing of such a reassessment, we wonder whether the Pringles deal could be affected? In our opinion, whatever the outcome of this particular issue, there are many red flags flying, and we think our estimate of $1.14 EPS reflects the real underlying earnings power of the existing business. And, regardless of the accounting, we think Diamond as it stands today is worth only about 15X its real economic EPS of $1.14, or about $17/share.

Fortunately for Diamond, it is using its shares, which are very expensive, to buy Pringles, so Pringles will be materially accretive to both earnings and Diamond's share value. However, our estimates post-merger, with Pringles, are materially lower than the "street's" estimates. This is mainly due, as we have explained, to the lower than recently reported earnings power that we think the core Diamond business will have in the future. Including Pringles, we think Diamond will only make about $2.75 in FY 2012 and $3.18 for FY 2013. This compares unfavorably to the "street" which thinks Diamond will make $3.14 in FY 2012 and $3.73 in FY 2013.

Based on our analyses, it appears both Diamond as it exists today and Pringles are growing revenues in just low single digits on a pro forma basis over the long term. As such, long term earnings growth will likely be unimpressive as well, and we think the shares should trade at about a market multiple of 13X our FY 2013 EPS estimate, suggesting a share value of about $41.

Assuming the Pringles deal closes, the consolidated company will have about $1.3 billion of debt outstanding. The deal will result in Diamond having about 52 million shares outstanding, putting the total value of the company at about $6 billion, based on Diamond's current share price. The company's guidance for EBITDA is $300-$310 million for FY 2012, so the current enterprise

value is about 20X EBITDA. At 10X the company's EBITDA, shares would be valued at only about 1/3 of today's share price. We estimate EBITDA of $367 for FY 2013, the first full year after Diamond acquires Pringles, implying EV/EBITDA multiples of 16.3X. As the company misses "street" earnings estimates, we think maintaining a 10X multiple might prove very difficult. At 10X our estimated FY 2013 EBITDA, the shares should trade at about $45. We recommend investors sell Diamond shares with a target of $43, the midpoint between our two valuation methods.

9. OWS financial model and cash flow model

a. OWS quarterly income statement estimates:

	Q1 11	Q2 11	Q3 11	Q4 11	Q1 12e	Q2 12e	Q3 12e	Q4 12e
Revenue								
Retail	227.8	215.6	181.7	191.0	245.1	229.7	190.3	200.1
International non-retail	21.0	36.8	31.4	29.8	21.6	37.9	32.3	30.7
North American ingredient & food service	3.8	5.2	9.9	12.0	5.1	6.2	10.4	12.6
Pringles	-	-	-	-	-	241.2	330.0	341.6
Total revenue	252.6	257.6	223.0	232.8	271.9	515.0	563.0	585.0
COGS	189.0	186.7	163.4	175.7	203.9	388.8	394.1	409.5
Gross profit	63.6	70.9	59.6	57.1	68.0	126.2	168.9	175.5
Operating expenses								
SG&A	23.1	24.0	24.2	25.7	26.0	45.0	75.2	75.1
Advertising	12.5	10.0	11.9	10.1	13.6	25.1	39.1	34.8
Acquisition & Integration Exp	0.5	0.9	5.9	9.4	30.0	40.0	40.0	40.0
Total operating expenses	36.1	34.9	42.0	45.1	69.6	110.1	154.3	149.9
Operating income	27.53	35.94	17.55	11.96	(1.63)	16.06	14.60	25.58
Interest expense	6.1	6.0	5.9	5.8	5.5	9.0	14.0	14.0
Other expense (income)	-	-	-	-	-	-	-	-
Pretax Income	21.4	29.9	11.6	6.2	(7.1)	7.1	0.6	11.6
Taxes	7.2	10.2	3.9	(2.4)	(2.0)	2.0	0.2	3.3
Net income	14.2	19.7	7.7	8.5	(5.1)	5.1	0.4	8.3
Diluted shares	21.947	22.221	22.341	22.577	22.9	40.2	52.8	53.0
Diluted EPS	0.65	0.89	0.35	0.38	(0.22)	0.13	0.01	0.16
Non-GAAP EPS								
GAAP Pretax Income	21.4	29.9	11.6	6.2	(7.1)	7.1	0.6	11.6
Adjustments to remove loss on ext of debt			-	-	-	-	-	-
Acquisition & Integration Costs	0.5	0.9	5.9	9.4	30.0	40.0	40.0	40.0
Non-GAAP Pretax Income	21.9	30.9	17.5	15.6	22.9	47.1	40.6	51.6
GAAP Income taxes	7.2	10.2	3.9	(2.4)	(2.0)	2.0	0.2	3.3
tax effect of non-GAAP adjustments	0.2	(0.0)	1.9	6.1	8.6	11.4	11.4	11.4
Non-GAAP Income taxes	7.4	10.2	5.8	3.7	6.5	13.4	11.6	14.7
Non-GAAP net income	14.5	20.7	11.8	11.9	16.4	33.7	29.0	36.9
Non-GAAP Diluted Shares	22.357	22.631	22.734	22.963	23.2	40.5	53.1	53.3
Non-GAAP Diluted EPS	$0.65	$0.91	$0.52	$0.52	$0.70	$0.83	$0.55	$0.69

Y/Y %

	Q1 11	Q2 11	Q3 11	Q4 11	Q1 12e	Q2 12e	Q3 12e	Q4 12e
Revenue								
Retail	58%	63%	44%	14%	8%	7%	5%	5%
International non-retail	-9%	2%	399%	693%	3%	3%	3%	3%
North American ingredient & food service	-72%	-68%	56%	143%	35%	20%	5%	5%
Pringles	na	na	na	na	na	na	na	na
Total revenue	40%	40%	61%	32%	8%	100%	152%	151%
COGS	40%	30%	52%	32%	8%	108%	141%	133%
Gross profit	40%	75%	92%	30%	7%	78%	183%	207%
Operating expenses								
SG&A	71%	57%	59%	27%	13%	87%	211%	193%
Advertising	98%	-18%	57%	45%	9%	152%	228%	246%
Acquisition & Integration Exp	na	na	-42%	633%	5912%	4169%	574%	324%
Total operating expenses	82%	27%	27%	58%	93%	215%	267%	232%
Operating income	7%	175%	-1025%	-22%	-106%	-55%	-17%	114%
Interest expense	390%	554%	211%	-5%	-10%	50%	136%	142%
Other expense (income)	na	na	-100%	na	na	na	na	na
Pretax Income	-12%	146%	-305%	-33%	-133%	-76%	-95%	88%
Taxes	-24%	204%	-381%	-195%	-128%	-80%	-96%	-239%
Net income	-5%	124%	-281%	27%	-136%	-74%	-94%	-3%
Diluted shares	32%	33%	16%	2%	4%	81%	136%	135%
Diluted EPS	-28%	69%	-256%	24%	-134%	-86%	-98%	-59%
Non-GAAP EPS								
GAAP Pretax Income	-12%	146%	-305%	-33%	-133%	-76%	-95%	88%
Adjustments to remove loss on ext of debt								
Acquisition & Integration Costs	na	97%	-44%	633%	5912%	4169%	574%	324%
Non-GAAP Pretax Income	-10%	144%	161%	48%	4%	52%	131%	231%
GAAP Income taxes	-24%	204%	-381%	-195%	-128%	-80%	-96%	-239%
tax effect of non-GAAP adjustments	na	-103%	-2%	1149%	5020%	-31767%	497%	88%
Non-GAAP Income taxes	-23%	127%	905%	24%	-11%	32%	100%	299%
Non-GAAP net income	-3%	154%	91%	58%	12%	63%	147%	210%
Non-GAAP Diluted Shares	31%	32%	12%	2%	4%	79%	134%	132%
Non-GAAP Diluted EPS	-26%	92%	71%	55%	8%	-9%	6%	33%

As a % of revenue:

	Q1 11	Q2 11	Q3 11	Q4 11	Q1 12e	Q2 12e	Q3 12e	Q4 12e
Revenue								
Retail	90%	84%	81%	82%	90%	45%	34%	34%
International non-retail	8%	14%	14%	13%	8%	7%	6%	5%
North American ingredient & food service	2%	2%	4%	5%	2%	1%	2%	2%
Pringles	0%	0%	0%	0%	0%	47%	59%	58%
Total revenue	100%	100%	100%	100%	100%	100%	100%	100%
COGS	75%	72%	73%	75%	75%	76%	70%	70%
Gross profit	25%	28%	27%	25%	25%	25%	30%	30%
Operating expenses	0%	0%	0%	0%	0%	0%	0%	0%
SG&A	9%	9%	11%	11%	10%	9%	13%	13%
Advertising	5%	4%	5%	4%	5%	5%	7%	6%
Acquisition & Integration Exp	0%	0%	3%	4%	11%	8%	7%	7%
Total operating expenses	14%	14%	19%	19%	26%	21%	27%	26%
Operating income	11%	14%	8%	5%	-1%	3%	3%	4%
Interest expense	2%	2%	3%	2%	2%	2%	2%	2%
Other expense (income)	0%	0%	0%	0%	0%	0%	0%	0%
Pretax Income	8%	12%	5%	3%	-3%	1%	0%	2%
Taxes	3%	4%	2%	-1%	-1%	0%	0%	1%
Net income	6%	8%	3%	4%	-2%	1%	0%	1%
Non-GAAP EPS	0%	0%	0%	0%	0%	0%	0%	0%
GAAP Pretax Income	8%	12%	5%	3%	-3%	1%	0%	2%
Adjustments to remove loss on ext of debt	0%	0%	0%	0%	0%	0%	0%	0%
Acquisition & Integration Costs	0%	0%	3%	4%	11%	8%	7%	7%
Non-GAAP Pretax Income	9%	12%	8%	7%	8%	9%	7%	9%
GAAP Income taxes	3%	4%	2%	-1%	-1%	0%	0%	1%
tax effect of non-GAAP adjustments	0%	0%	1%	3%	3%	2%	2%	2%
Non-GAAP Income taxes	3%	4%	3%	2%	2%	3%	2%	3%
Non-GAAP net income	6%	8%	5%	5%	6%	7%	5%	6%

b. OWS annual income statement estimates:

	FY 10	FY 11	FY 12e	FY 13e
Revenue				
Retail	570.4	816.1	865.2	905.7
International non-retail	69.2	119.0	122.6	126.3
North American ingredient & food service	40.5	30.8	34.3	36.0
Pringles	-	-	912.8	1,484.7
Total revenue	680.2	965.9	1,934.8	2,552.6
COGS	519.2	714.8	1,367.2	1,815.6
Gross profit	161.0	251.1	567.6	737.0
Operating expenses				
SG&A	64.3	97.0	221.3	302.7
Advertising	33.0	44.4	112.6	147.2
Acquisition & Integration Exp	11.5	16.8	150.0	-
Total operating expenses	108.8	158.2	483.9	449.9
Operating income	52.23	92.98	83.70	287.16
Interest expense	10.2	23.8	42.5	50.0
Other expense (income)	1.8	-	-	-
Pretax Income	40.2	69.1	41.2	237.2
Taxes	14.0	18.9	3.5	67.6
Net income	26.211	50.2	37.7	169.6
Diluted shares	18.8	18.8	42.2	53.0
Diluted EPS	1.39	2.66	0.89	3.20
Non-GAAP EPS				
GAAP Pretax Income	40.2	69.1	12.1	237.2
Adjustments to remove loss on ext of debt	1.8	-	-	-
Acquisition & Integration Costs	12.3	16.8	150.0	-
Non-GAAP Pretax Income	54.3	85.9	162.1	237.2
GAAP Income taxes	14.0	18.9	3.5	67.6
tax effect of non-GAAP adjustments	3.6	8.0	42.8	-
Non-GAAP Income taxes	17.6	26.9	46.2	67.6
Non-GAAP net income	36.8	59.0	115.9	169.6
Non-GAAP Diluted Shares	19.215	22.642	42.2	53.3
Non-GAAP Diluted EPS	$1.91	$2.61	$2.75	$3.18

Y/Y change %

Y/Y %	FY 11	FY 12e	FY 13e
Revenue			
Retail	43%	6%	5%
International non-retail	72%	3%	3%
North American ingredient & food service	-24%	11%	5%
Pringles	na	na	63%
Total revenue	42%	100%	32%
COGS	38%	91%	33%
Gross profit	56%	126%	30%
Operating expenses			
SG&A	51%	128%	37%
Advertising	35%	154%	31%
Acquisition & Integration Exp	46%	793%	-100%
Total operating expenses	45%	206%	-7%
Operating income	78%	-10%	243%
Interest expense	134%	78%	18%
Other expense (income)	-100%	na	na
Pretax Income	72%	-40%	476%
Taxes	35%	-82%	1857%
Net income	92%	-25%	349%
Diluted shares	0%	124%	26%
Diluted EPS	92%	-66%	258%
Non-GAAP EPS			
GAAP Pretax Income	72%	-82%	1857%
Adjustments to remove loss on ext of debt			
Acquisition & Integration Costs	37%	793%	-100%
Non-GAAP Pretax Income	58%	89%	46%
GAAP Income taxes	35%	-82%	1857%
tax effect of non-GAAP adjustments	123%	437%	-100%
Non-GAAP Income taxes	53%	72%	46%
Non-GAAP net income	61%	96%	46%
Non-GAAP Diluted Shares	18%	86%	26%
Non-GAAP Diluted EPS	36%	5%	16%

As a % of revenue

	FY 10	FY 11	FY 12e	FY 13e
Revenue				
Retail	84%	84%	45%	35%
International non-retail	10%	12%	6%	5%
North American ingredient & food service	6%	3%	2%	1%
Pringles	0%	0%	47%	58%
Total revenue	100%	100%	100%	100%
COGS	76%	74%	71%	71%
Gross profit	24%	26%	29%	29%
Operating expenses	0%	0%	0%	0%
SG&A	9%	10%	11%	12%
Advertising	5%	5%	6%	6%
Acquisition & Integration Exp	2%	2%	8%	0%
Total operating expenses	16%	16%	25%	18%
Operating income	8%	10%	4%	11%
Interest expense	1%	2%	2%	2%
Other expense (income)	0%	0%	0%	0%
Pretax Income	6%	7%	2%	9%
Taxes	2%	2%	0%	3%
Net income	4%	5%	2%	7%
Non-GAAP EPS	0%	0%	0%	0%
GAAP Pretax Income	6%	7%	1%	9%
Adjustments to remove loss on ext of debt	0%	0%	0%	0%
Acquisition & Integration Costs	2%	2%	8%	0%
Non-GAAP Pretax Income	8%	9%	8%	9%
GAAP Income taxes	2%	2%	0%	3%
Tax effect of non-GAAP adjustments	1%	1%	2%	0%
Non-GAAP Income taxes	3%	3%	2%	3%
Non-GAAP net income	5%	6%	6%	7%

c. OWS free cash flow estimates:

	FY 10	FY 11	FY 12e	FY 13e
Free cash flow				
GAAP net income	26.2	50.2	37.7	169.6
Depreciation and amortization	17.2	29.5	79.0	113.3
Shareholder compensation expense	3.2	7.0	13.0	17.0
Cash flow from operations	46.6	86.6	129.7	299.9
Capex	11.8	27.7	80.0	85.0
Free cash flows	34.8	58.9	49.7	214.9

d. OWS EBITDA estimates

	FY 10	FY 11	FY 12e	FY 13e
Non-GAAP pre-tax income	54.3	85.9	162.1	237.2
Depreciation & amortization	17.2	29.5	79.0	113.3
Shareholder compensations exp	3.2	7.0	13.0	17.0
EBITDA	74.7	122.4	254.1	367.5