BEYOND OIL

The EV pioneer in the running for a $110bn bonanza

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The EV pioneer in the running for a $110bn bonanza

By James Allen

Editor and Publisher, *Exponential Energy Fortunes*

On the first day of his presidency, Joe Biden announced a 100-day plan to reopen schools.

And by this autumn, all American schools could be fully in action.

Which means that 26 million American kids will be back in classrooms.

To move all these boys and girls between school and home you need a lot of buses.

550,000 to be exact.

In fact, school buses are the United States' largest mass transit system.

But this year, some of these buses will be a little different.

And soon, all of them will be different.

They will also be better.

They will be more environmentally friendly.

You see, President Biden has announced a plan to replace every single school bus with a zero-emission one.

And this fleet upgrade will be completed within five years.

If you're an investor, this should be music to your ears.

Because with a $200,000 minimum cost per bus… this is a $110 billion bonanza.

You read that correctly: there's $110 billion up for grabs for the companies that will supply the new buses.

And I think I've uncovered the company that could benefit the most from this policy.

I believe that the company is set to dominate the upcoming electric vehicle (EV) school bus manufacturing boom – and it is already ramping up capacity.

To my mind, it has some huge competitive advantages in the marketplace that put it above its competitors.

It's a high-risk play but, even by our standards, this is very exciting stuff.

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It's not an exaggeration to say that this company's EV school buses could soon be seen in almost every major city and town in the United States…

But right now, it appears as if most investors simply don't realise that the company even exists.

In fact, the firm operates in a market not really talked about by any mainstream analyst…

Which is *great* news for us.

There is a knowledge gap here – and that's our window of opportunity.

So without further ado, let me introduce you to our latest *Exponential Energy Fortunes*' recommendation: Blue Bird Corp (NASDAQ:BLBD).

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Blue Bird is looking to become the dominant manufacturer of EV school buses in the United States.

It's hoping to achieve that feat from a running start.

That is because rather than being a start-up or a special purpose acquisition company (SPAC), it's a 94-year-old company that's already the number one school bus manufacturer in North America.

And now, it's moving aggressively towards alternative fuels and electric motors. To me, that makes it the best investment in the sector, as it has developed a number of competitive advantages along the way.

I'll get into those in a minute. First, though, is a brief overview of the business.

Blue Bird manufactures school buses – that much is clear.

It sells four classes of school buses, and it sells four major fuel types as well – petrol and diesel, propane and electric.

It's the electric segment that we are most interested. It's currently the smallest, but it's growing fast, and is the future of the company.

In terms of its fuel mix, it sells only around 10-20% diesel buses, while most competitors in the United States are at around the 50% mark.

It's much more focused on its alternative fuels business.

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At the moment this is mostly to do with propane, a lower emission, cleaner burning fossil fuel than petrol or diesel.

It's not the worst solution in the world, and Blue Bird is clearly a market leader in selling propane school buses with 76% market share of US propane bus sales in 2020.

But it's the EV segment that we're really interested in.

Blue Bird is the only manufacturer that has produced and deployed every type of electric-powered school bus: Types A, C, and D. These are the two, large, long yellow school buses that you traditionally see in North America, plus a smaller version.

Having launched its electric line in 2018, it already holds more than 50% share of the US and Canadian market for electric school buses.

It has 500 electric school buses sold or on order.

And recently, it delivered the first operational DC fast charge V2G (vehicle-to-grid)-capable school bus. Vehicle to grid is a key emerging technology that I believe will have a growing presence in the EV market.

It basically means that your vehicle can act as an energy storage unit as well. By allowing two-way flow of current, vehicles can send electricity back to the grid, rather than just charging off it.

So, if there's a blackout, you can power your home with your vehicle.

Or, more commonly, the vehicle will be able to generate revenues by selling back the grid when demand (and therefore price) is high. At a fleet level, this is a key technological addition to an electric vehicle, especially one with a large battery like a bus.

This therefore allows operators to store clean electrical energy in the bus, and generate revenue by reselling unused energy back to the grid during peak demand.

Being the first company to get a V2G capable school bus on the road highlights a strength of Blue Bird.

Just because it's almost 100 years old, that doesn't mean it's resting on its laurels or relying on what has served it well historically.

The opposite is true with Blue Bird. It's innovating vigorously, with the intent to transform itself radically for the new electric age.

And one interesting development for the coming years, hinted at in the recent note from the CEO in the annual report, is that Blue Bird will offer its electric chassis to other segments of the vehicle industry.

So freight/trucking, or coach builders, for example, could all put different bodies on top of a Blue Bird chassis.

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And then there's Joe Biden's plan to electrify all 500,000 school buses in the United States, as mentioned above.

At roughly $200k per bus, it's an enormous opportunity for Blue Bird to leverage its existing leadership to benefit from this $110 billion opportunity.

A "start-up" with an existing defensive moat

So it's already a leader in the small but growing electric school bus space, but that only forms a tiny part of the overall business. Why not go for a pure play?

To my mind, its long history and impressive history of operating in the school bus sector gives it some key competitive advantages over a smaller start-up.

Competitive advantages include:

- An existing client network of dealers
- Existing safety record and standards
- Experience with compliance and regulatory framework
- Brand recognition for trust, and safety – especially important for parents and schools
- Proven track record in selling school buses at scale
- Big name partnerships with the likes of Ford and Cummins.

With history comes trust, comes long-standing customer relationships, comes experience with safety regulations, and consumer demands.

The experience means that Blue Bird knows how to deal with all the little technical, operational problems that are associated with running a school bus company.

It's one thing to create an EV product. However, it's quite another to build it out at scale, as Tesla has shown. Tesla is slowly getting there, but it has provided a tale of woe – of cars built in tents, shoddy workmanship, accidents, missed delivery targets, and the rest.

Blue Bird has the opposite problem, a legacy business that may become a burden before too long.

But this gives it other advantages.

It has developed its EV drivetrain and chassis.

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These can simply displace the current, fossil-fuelled models, in the same operational chains: production, dealer networks, compliance, marketing – the works.

Let's take the dealer network, for example.

Pre-pandemic, there were 600,000 school buses ferrying 26 million American children to school each day.

Blue Bird manufactures these buses, but it doesn't sell them. Retailing is done by dealer partners, of which it has an extensive network (there are 10,000 school districts and a few thousand retailers in North America).

In fiscal 2020, Blue Bird sold around 93% of its vehicles through its US and Canadian dealer network, currently consisting of over 50 dealerships. What's more, in their territories, the dealerships are exclusive to Blue Bird with Type C and D school buses.

This is a sector where intermediaries (i.e. dealerships) matter deeply, and when trying to push new products, having that existing relationship will be enormously valuable.

It is the dealerships who are responsible for selling your vehicle, responsible for what happens to the children who use it to get to school each day, and responsible for breakdowns and repair.

You can imagine, as a dealer, what it is like to look at a product from a company that you've done good, profitable business with for decades versus a product from a new upstart competitor.

You know which one you'd trust more. You know which is the one that you believe could deal with any issues.

As noted, the dealerships are responsible for the repair and maintenance of the vehicles.

This requires them to be trained and equipped to deal with any issues with the bus. It also means having an existing framework to access authentic Blue Bird parts and training for mechanics.

Parts are centrally manufactured by Blue Bird in Ohio, and they are typically shipped out the following day for dealer stock orders. Parts are shipped on the same day for urgent customer orders that can be reached on the following day by air.

Alongside its 50 retail dealership partners, Blue Bird has 250 parts and repairs dealers across the United States and Canada.

The dealers are already set up to help purchasers with the EV charging infrastructure needed to incorporate electric buses into their fleet.

That kind of well-oiled system can take a new entrant years, if not decades, to build out so that it works perfectly, with all the kinks ironed out.

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Blue Bird is able to roll out its electric buses out via this network – and that is a huge advantage.

Another competitive advantage to focus on is safety.

Safety is and has for a very long time been the top priority for Blue Bird.

School buses are ferrying 26 million children per day around North America – and the safety of their children is clearly the number one priority for any parent, or school.

The new electric buses benefits from *exactly the same* standards as all other buses in the range.

This is a safety record that people can trust.

Safety is a real issue in the EV space.

Tesla, for instance, has had a lot of bad press recently around the failures of the automatic braking system, and the deaths that have occurred because of the badly understood "full self-driving" feature.

From an investment perspective, we gain much confidence in the fact that Blue Bird has proven that it can be a profitable bus manufacturer.

If it can do it for fossil-fuelled buses, then it makes sense to think it can do it with electric buses too.

The competitive advantages it has in the market are impressive, and I believe, sustainable.

I expect Blue Bird's electric bus network to be one of the top beneficiaries of the federal attempts to overhaul the school bus fleet through the Clean School Bus Act and the Clean Commute for Kids Act.

The $110 billion opportunity for electric bus manufacturers is going to create a few big winners, and I think Blue Bird has the best chance of anyone of being one of them.

Indeed, electric school buses have Buy America regulations, which means US manufacturers such as Blue Bird should be insulated, to a large extent, from competition from overseas.

Blue Bird meets all our EXPO criteria – and some

Blue Bird meets all the EXPO criteria – which act as our informal research guide rather than an overarching entrance requirement – quite easily.

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- *The company is* **Established**

The company was founded almost a century ago. It has sold hundreds of thousands of school buses.

And when it comes to clean energy, it has made more alternative fuel school buses than all of its competitors… combined.

In fact, it owns the majority of EV school bus market share.

Lastly, as a company it has a reputation for safety.

And that is one of the most important factors when it comes to transportation – especially transportation of children.

- *The company has the* **X-factor**

It is the only manufacturer that can make every type of school bus.

This means every school in the United States and Canada buying a new EV bus is a potential client.

Now keep in mind that school buses are a highly specialised product. It will be very hard for newer companies to break into this market.

Not to mention that the company already has an established network of dealers and service centres.

Another X-factor is the company's use of V2G, a technology that will allow schools to reduce operating costs.

You see, thanks to V2G, schools can sell electricity stored in the buses back to the electric grid.

This could take place during summer, when school buses are mostly idle, but electricity is in peak demand.

- *The company has* **Potential for Growth**

Like I've said, President Biden plans on replacing the United States' entire fleet of 500,000 school buses with zero emission buses in five years.

That's a great opportunity for the company.

Already, last year its sales of electric buses went up 250%.

And it has plans to increase its production capacity six times in response to surging demand.

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- *The company already has* **Orders, Clients and Partnerships**

Already 10,000 schools are customers of the company.

And with the average school bus being 11 years old, soon these schools could go shopping for a new bus.

The company also has an exclusive partnership that gives it access to alternative-powered engines from one of the biggest car manufacturers in the world.

All in all, it is well-positioned to capitalise on the opportunity arising from the US government subsidies for electric school buses.

Perhaps it is no wonder, then, that a whopping 92% of all stock issued by Blue Bird is held by institutions.

Including some of the most reputable names in finance like:

BlackRock…

Vanguard…

And others…

On top of that, the company's insiders believe that Blue Bird is ready for success.

For example, the CEO of the company holds Blue Bird stock worth $10.5 million.

Financials

For us the financials are a little hard to judge.

There are two stories – one of the legacy business and its decent financials.

But secondly, of its rapidly growing EV business.

Total revenue is up over 50% since 2010, so the trend is one of broadly positive, albeit not explosive, growth. Bus unit sales are up 40% over the same period, and market share in the United States is up 7 percentage points over the decade.

In the last few years though, total company revenues have been pretty flat, at around the $1 billion per year mark. There was a slight dip in 2020 as schools closed and business dried up.

To be honest, it's pretty surprising the hit to the top line in 2020 wasn't worse though. Revenue still came in at $880 million during a national pandemic and lockdown.

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The drop in sales was largely in line with the experience of the broader industry, where bus sales dropped from 33,800 units to 28,500.

Until 2019, although revenues had been flat, margins had been expanding such that net profit grew from $3 million in 2016 to $24.3 million in 2019.

In 2020, although sales fell in unit terms, the average selling price actually rose by 7%. This carried on the margin expansion that had driven improved net income in previous years.

Blue Bird has had a slow start to 2021, with Q2 and Q1 returning $165 million and $130 million in revenues respectively.

However, the EV business delivered nearly 200% growth from 2019 to 2020.

This has taken the company to an incredible 59% market share of electric school bus sales in the United States.

Given that this is a large focus for us, this fits into a fair picture of the company financially.

It's an established school bus manufacturer, earning decent revenues and positive net earnings. However, it is trying to move aggressively into EVs, as it's the key growth area for the market and for the business too.

Going back to margins, the alternative fuels vehicles – propane and electric – deliver higher price points and margins then their petrol and diesel predecessors. Leadership in two sectors with promising impressive growth and higher margins is a very promising combination from a financial perspective.

So there's a lot of promise from Blue Bird's pivot to alternatives.

There are three key risks, though, which should be noted.

Risks

One key risk arises from the fact that electric school buses are relatively new. The company could lose market share fast as a result of an unanticipated change to the market.

It is possible that there's another wave of coronavirus and schools don't reopen. That would result in delayed orders for new buses.

It is also possible that, as a result of the pandemic, education is much more online and at home than in classrooms: this could produce a once-off decline in the number of school buses that are needed.

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Conversely, it may be that the pandemic results in laws and rules mandating more space on buses between children.

With fewer children per bus, more buses would be needed.

Other potentially adverse changes can be imagined.

Furthermore, the propane business is something in which Blue Bird has invested a lot of time and money.

While that business has been successful so far, it's possible that that too could become a burdensome legacy business as the electrification of transport really gathers pace.

But again, I think the company is clearly focused on growing its EV business, and is as well placed as anyone to benefit from that trend too.

The second key risk is that growth of the EV business is not enough to offset a possible contraction in the propane business.

It is also true that the investment case is partly predicated on a massive government initiative to electrify the United States' school bus fleet.

In my mind, that is an initiative that is also backed by the people at large, as well as by the financial system: it is therefore likely to continue.

But it's possible that politics could get in the way and hurt the prospects for Blue Bird's EV business.

That is the third key risk.

In that case though, it has its legacy business to rely on so it's less vulnerable to such a turnaround than a pure-play EV manufacturer.

A plethora of other, more general risks also apply here. In no particular order, these include (and are not limited to): a stock market that is expensive by historic norms; economies' over-reliance on central bank stimulus; potential competition from other established players and new entrants; rising costs of doing business from inflation in commodity and shipping prices; and semiconductor shortages.

But despite all that, I believe that the potential reward outweighs the risk. Blue Bird is well placed to exploit the electric school bus bonanza, and investors in the company should be reaping the rewards.

I'm therefore recommending that you BUY Blue Bird Corp (NASDAQ:BLBD). It trades on Nasdaq and is available from numerous major and smaller brokers, including Hargreaves Lansdown. For more information on possible brokers to use, see here.

Action to take: BUY Blue Bird Corporation

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For full details of current prices and buy up to limits, click here to check the portfolio for details.

James Allen
Editor, *Exponential Energy Fortunes*