

# Mossberg's Investor Digest

## Best Idea Profile:

## Liquidity Services (Nasdaq: LQDT)

### DESCRIPTION:

Headquartered in Washington D.C., Liquidity Services runs online auction marketplaces that helps corporations and government agencies liquidate surplus goods. LQDT procures product from many top 10 retailers, online retailers, and the U.S. government. After taking possession of the goods at one of its 9 warehouse facilities, the company sorts, barcodes, and palletizes common items. The items are then auctioned on one of its auction sites to eBay power users, thrift shops and back alley liquidators. The company has 2.6 million registered users of its websites liquidation.com, networkinternational.com, govliquidation.com, govdeals.com, truckcenter.com, and liquibiz.com. The company has 1,300 employees across North America, Europe, and Asia.

### KEY INVESTMENT CONSIDERATION:

**LQDT has an attractive "Asset Light" business model** – LQDT's unique business model can generate "negative working capital". This happens because auction winners pay faster than LQDT has to pay for the entire consideration (inventory purchase plus profit sharing distribution) of the product. LQDT has three pricing models.

- 1. Consignment** (13% of revenue) – Under the consignment model, there is no cash outlay for the merchandise sold at auction. Payment is received by LQDT and remits funds to the seller after a few days.
- 2. Profit Share** (16% of revenue) – Under this model, LQDT pays a nominal amount (less than 1% of acquisition value) to the seller, then remits a portion of the profits generated on the sale of the merchandise after selling and other expenses are deducted.
- 3. Purchase** (71% of revenue) – LQDT agrees to a purchase price per item, and sometimes receives terms from the seller that can be as much as 120-180 days. In most cases this is twice as long as it takes LQDT to sell and receive payment for the item.

As a result of this model, LQDT can finance growth without issuing new shares and diluting shareholders. Excess cash can be used to repurchase stock or make acquisitions that further expand the scope and scale. In fact, during the past five years the company's revenue base has more than doubled, while shares outstanding have increased by only 7.5%. It's also conceivable that LQDT could pay a dividend at some point in the future.

**Large Market Opportunity** – The Company estimates that it has only penetrated 2-3% of the

online surplus management market, which may be as large as \$150 billion annually.

**Critical mass and infrastructure create strong value proposition and barriers to entry** – In the auction business, the larger the efficiencies of scale and scope the more valuable the auction is to sellers and buyers. The company has 500,000+ unique items and over 19.2 million auction participants. In addition, the company has built infrastructure to support a \$1B business. Its 19 warehouse/storage facilities with over five million sqft. of usable space, systems, and knowledge base would be significant barriers for any new entrant to duplicate.

### VALUATION:

The stock has fallen near its 52-week low on news of the termination of its Wal-Mart contract along with changes in the company's DoD business which is under volume and margin pressure. Analysts estimates are calling for approximately \$0.60 in earnings for fiscal 2015 (ending September), which is approximately 40% below the prior year. By contrast shares have fallen 60% year over year. While near term revenue and earnings may face difficult comps, the long-term opportunity for this "asset light" business is very attractive. Assuming a recovery back to historical revenue and earnings levels over the next three years, the company has \$1.30 in earnings power, and even a modest multiple yields significant upside for investors with a long-term horizon.

### (Nasdaq: LQDT)

Investment Data (as of 02/23/15)

<b>Recent Price</b>	<b>\$9.77</b>
52-Week Range	7.32 - 27.33
Fiscal Year End	September
Shares Outstanding	30 MM
Average Trading Volume (3 mos)	412,000
<b>Market Capitalization</b>	<b>292 MM</b>
Cash	74 MM
Long Term Debt	0
Enterprise Value (EV)	218 MM
LT Debt/ Equity	0%
Tangible BV/ Share	4.25
TTM Revenue	499 MM
<b>P/ Revenue</b>	<b>0.6x</b>
TTM EPS	-1.33
<b>P/ EPS</b>	<b>N/A</b>
TTM EBITDA	49 MM
<b>EV/ TTM EBITDA</b>	<b>4.5x</b>

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