

Mossberg's Investor Digest

April 2015

Issue #82

From the Editor...

Thank you for your subscription to Mossberg's Investor Digest.

This month's issue highlights premium office furniture manufacturer Kimball International (Nasdaq: KBAL). Having recently spun out a disparate business, the pure play company should garner greater attention from Wall Street. It has an achievable plan to improve operating margins to an industry standard rate of eight percentage points, versus 2.6 percent achieved during the trailing four quarters. To achieve targeted profitability the company needs to grow at a 5% clip for the next 2 ½ years, which will translate into a 20% CAGR in earnings growth. Using reasonable multiples, the company has 50% to 90% upside in the next two years.

As always, I appreciate your feedback.

Dave Mossberg

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Every month we hear ideas suggested from our large network of professional investors. Here are four of the ideas we heard this month, but have not reviewed in detail...

Astro-Med, Inc. (Nasdaq: A LOT) - Astro-Med Inc is a developer, manufacturer, and supplier of hardware and software systems that acquire, process, analyze, store and present data in a variety of useable forms. Astro-Med's mission is to build shareholder value by conscientiously serving their customers in the packaging, avionics, and test & measurement markets. Astro-Med grows by innovation, developing solutions that meet and exceed customer demand for specialty printing and data acquisition equipment and related consumable supplies.

Boingo Wireless, Inc. (Nasdaq: WIFI) - Boingo has built a thriving business on sound fundamentals. With revenue split between retail and wholesale efforts – and augmented with a growing advertising business – the company continues to identify and pursue strategic growth opportunities to enhance shareholder value, while building a leadership position in key markets that support those efforts. Boingo platform is the only monetization engine of its kind, driving revenue through carrier offload, advertising, location-based data analytics, and consumer products like IPTV, high-speed broadband, and Wi-Fi.

Planet Payment, Inc. (Nasdaq: PLPM) - Planet Payment is a leading provider of international payment and transaction processing and multi-currency processing services. The company provides their services and solutions to merchant locations in 23 countries and territories across the Asia Pacific region, North America, South America, the Middle East, Africa and Europe, primarily through their acquiring bank and processor customers, as well as through their own direct sales force.

SuperCom Ltd. (SPCB) - SuperCom has been a leading global provider of traditional and digital identity solutions, providing advanced safety, identification and security solutions to governments and organizations, both private and public, throughout the world. SuperCom also offers a unique all-in-one field-proven RFID and mobile technology product suite, accompanied by advanced complementary services for various industries including healthcare and homecare, security and safety, community public safety, law enforcement, electronic monitoring, livestock monitoring, and building and access automation.

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Best Idea Profile:

Kimball International, Inc. (Nasdaq: KBAL)

DESCRIPTION:

Headquartered in Jasper, Indiana, Kimball International provides furniture for office, healthcare, education, and hospitality industries sold under Kimball Office, National and Kimball Hospitality brand names. Kimball Office is a premium brand, while National is more of a mid-tier brand. As its name implies the Kimball Hospitality brand provides in-room and public space furniture for hotels and condos. The company has 11 production facilities, and eight showrooms in the United States, the majority of which are owned outright by the company. The Company employs approximately 3,000 people.

The Company was founded in 1950 and is well-known for its historic Kimball piano brand. In addition to Pianos, the Company has a long heritage as the furniture, and electronics manufacturer. The Company became public in 1974 with two classes of common stock, which has recently been changed so that both classes have equal rights. In the Mid-90's the company exited the Piano manufacturing business and spent the next 10 years exiting other non-core businesses and restructuring to run under two segments, furniture and electronic manufacturing services (EMS). In October of last year, the EMS business, Kimball Electronics (Nasdaq:KE), was spun off, and Kimball International became a pure play furniture company.

Kimball International, Inc. (Nasdaq: KBAL)

Investment Data (as of 4/29/15)

| | |
|-----------------------------------|------------------|
| Recent Price | \$10.38 |
| 52-Week Range | \$8.38 - \$14.60 |
| Fiscal Year End | June |
| Dividend | \$0.20 |
| Yield | 1.8% |
| Shares Outstanding | 38.9 M |
| Average Trading Volume (3 mos) | 133 k |
| Market Capitalization | \$410 M |
| Cash | \$49 M |
| Long-term Debt | - |
| Enterprise Value (EV) | \$361 M |
| Book Value | \$3.75 |
| TTM Revenue | \$1.3 B |
| P/ Revenue | 0.3 x |
| FY15 EPS (consensus) | \$0.36 |
| P/ EPS | 29x |
| TTM EBITDA | \$97 M |
| EV/ EBITDA | 23x |

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KEY INVESTMENT CONSIDERATIONS:

Unlocking value and improving corporate governance – The Company has made several strategic and operational changes to improve corporate governance and unlock value.

- **Spin off of Electronic Manufacturing Services Segment** – At the end of October 2014, the company spun off its Electronic Manufacturing Services segment into a separately traded public company, Kimball Electronics (Nasdaq: KE). The two disparate businesses had little if any overlap. The company has only one analyst, likely due to the past complexity of analyzing the disparate businesses. Post transaction, Kimball International became a pure-play furniture company, making it easier for furniture-focused analysts and investors to follow, understand and value properly, which may attract greater analyst coverage and broader ownership. In addition, the pure-play allows management to focus attention and capital allocation decisions on one segment, and as a result will most likely improve shareholder returns.
- **Removing the distinction between Class A&B common shares** – Late last year, the Class A and B shares were essentially assigned equal voting and dividend rights and there no longer remains a distinction between them...management and the board are now 100% accountable to shareholders. Many companies have historically issued A & B classes of common in order to protect their companies against a takeover or other corporate actions. It has since been proven by academic study that having a dual-class structure where one class has super voting rights often hinders corporate performance. It is also a disqualifier for some institutional investors, so removing the distinction not only provides more accountability, but also encourages broader potential ownership.
- **Habig Family** - The Company was founded by Arnold F. Habig in 1950 and was led and ultimately controlled by the Habig family up until long-time CFO, Robert Schneider was named CEO and Chairman in 2014. Coinciding with the changing of the guard, several other members of the board retired or otherwise resigned. Today 5 of the 7 members of the board are independent and the company established a lead independent director of the board.
- **Selling a corporate plane** – Whether there is a viable business case or not, having a corporate jet for management's use is often viewed as a red flag by corporate governance watchdogs. Last year, the Company sold the plane that was used by management, which is expected to generate \$800,000 in annual pretax savings. The Company maintains a corporate-owned plane that is used to transport customers to visit showrooms and manufacturing locations that are located in smaller towns away from major metropolitan areas.
- **Other opportunities for value creation** – When reviewing the last 10K, which includes a breakout of the amount of property that is owned by the furniture division, it shows that 98% of the facilities that are used by the Company, post spin, are owned instead of leased. Relative to the \$98 million in value assigned to property plant and equipment (PP&E) after the split, it equates to about \$28 per foot in value. This number includes the value of the land, building and equipment per square foot. A quick search in the Jasper, Indiana area shows the value of industrial/ commercial properties value of \$45 to \$50/ sq. ft. If you add a value for KBAL's equipment, I think it is reasonable to make the case, even without a more thorough comparable analysis, that there is significant hidden value in KBAL's PP&E. If the company did a sale lease back on half of their facilities, and were able to garner \$20 per sq. ft. incremental value, it would equate to approximately \$34 million or \$0.90 per share in incremental value.

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KEY INVESTMENT CONSIDERATIONS: (continued)

Attractive trends in office and Hospitality furniture markets – There are several cyclical and secular trends that should drive mid-single digit growth in office and hospital furniture for the next several years.

- **Traditional economic indicators of demand are strengthening** - Economic indicators, such as corporate profits, record levels of corporate cash, lower vacancy rates, and improved job growth show that spending on office furniture should continue to be positive for the next several years. BIFMA (Business + Institutional Furniture Manufacturers Association) is calling for the U.S. office Furniture market to grow by 4.5% in 2015 and 6.4% in 2016.
- **Collaboration, newer technologies and mobility drive furniture upgrade cycle** – Several secular drivers are causing growth in office furniture. Key among these trends is the growth in collaborative work, distributed teams and disruptive technologies, all of which have significant implications for making changes in the workplace environment.
- **RevPar rates are strong across the board for the hospitality industry** - The hospitality market is strong with the latest industry statistics forecasting RevPAR, (revenue per available room) to increase 7% in calendar year 2015, on top of a 7% increase last year.

Well positioned for above market growth – KBAL is well-positioned to achieve mid- to high-single-digit growth for the next several years. Quarterly revenue growth has averaged over 6% during the past five quarters and order backlog was up 20% entering the fiscal third quarter, which will be reported next week.

- **Leveraging existing capacity and competencies to enter new industry segments** – The Company has launched new furniture designed specifically for healthcare and education industries.
- **Strong Balance sheet with ample liquidity to make acquisitions** - The U.S. office furniture market is very fragmented with more than 3,800 companies, and none of the publicly traded manufacturers having more than 15% share of the market. This describes an industry that is well positioned for consolidations. KBAL has ample liquidity with no debt, about \$50 million in cash and a \$30 million line of credit. Combined with the potential for the company to unlock the hidden value in its properties as I described earlier, the company has more than enough liquidity to support its internal growth plans as well as make acquisitions of smaller niche players.

The bottom line should grow much faster than the top line – As a focused pure-play furniture company, there are several areas to improve efficiencies as well as improve utilization to gain operating leverage. The Company has stated that with modest growth to \$640 million in sales (5% CAGR from FY2014), its goal is to increase operating margin to 8 percent of sales, which is in-line with industry standard margins. Comparatively, during the trailing four quarters, the Company's adjusted operating margin was 2.6 percent of sales, which leaves room for 540 basis points of improvement. As margins improve, a 5% CAGR in revenue translates into to 20% CAGR in operating profit over the next three years. Shortly after the spin, management specifically identified that \$5.8 million in annual savings (approximately 100 basis points) should be achieved from the sale of one of its corporate planes (\$800,000 in annual savings), and consolidation of its metal fabrication facilities into a centralized location (\$5 million in annual savings).

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VALUATION:

| | FY 17 | FY 17 | Targets/ assumptions |
|----------------------------|----------------------|----------------------|-------------------------|
| 2014 Base Revenue | \$550,000,000 | \$550,000,000 | |
| 5% Compound Growth Organic | \$90,000,000 | \$90,000,000 | 5% CAGR |
| Acquisitive Growth | | \$90,000,000 | |
| Total Revenue | \$640,000,000 | \$730,000,000 | |
| Operating Profit | \$51,200,000 | \$58,400,000 | 8% |
| Taxes | \$17,920,000 | \$20,440,000 | 35% |
| Net Income | \$33,280,000 | \$37,960,000 | |
| Shares Outstanding | 38,900,000 | 38,900,000 | |
| EPS | \$0.86 | \$0.98 | |

The table above shows our back-of-the-envelope calculation for revenue and earnings for FY17. The calculation assumes approximately 5% organic growth and two scenarios, first a scenario with no acquisitions and second, a scenario with an equal amount revenue contribution from acquisitive growth. Operating margins targets are industry standard and it appears management is already doing the right things necessary to drive margins to 8% of sales. Using a 35% tax rate, yields \$0.86 to \$0.98 earnings power over the next 2 ½ years. This is more than 2x to 2.5x the lone analyst's estimate of \$0.36 for the current fiscal year ending in June.

Comparatively other office furniture focused companies, HNI, Herman Miller and Steelcase trade at approximately 19x, 16x and 22x forward estimates. Therefore, it is reasonable to assume that KBAL could command an 18x to 20x multiple over the next couple of years, which would yield a valuation of \$15 to \$20, or 50% to 90% upside for its current valuation.

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Mossberg's Investor Digest Idea Performance

The table below shows selected ideas published from March 2014 until March 2015. The overall performance number includes all ideas published since July 2008, including those not shown. **Performance data quoted represents past performance and does not guarantee future results.** Current performance of ideas may be lower or higher than the performance quoted.

| Company | Pub. Date | Original Price | Recent Price | Change | Russell 3000 Change Since Pub. Date | Relative Perf. vs. Russell 3000 |
|--|-----------|----------------|--------------|--------------|-------------------------------------|---------------------------------|
| Arcos Dorados (NYSE:ARCO) | 7-Mar-14 | \$9.38 | \$6.10 | -35.0% | 11.2% | -45.7% |
| Cimatron Ltd.(NASDAQ:CIMT) | 21-Mar-14 | \$7.85 | \$8.97 | 14.3% | 11.2% | 2.9% |
| Unisys (NYSE:UIS) | 26-Mar-14 | \$29.63 | \$22.12 | -25.3% | 13.2% | -37.7% |
| Mueller Industries (NYSE:MLI) | 28-Mar-14 | \$29.34 | \$35.46 | 20.9% | 13.0% | 8.8% |
| WidePoint Corp. (NYSE MKT:WYY) | 4-Apr-14 | \$1.51 | \$1.41 | -6.6% | 12.5% | -18.2% |
| Allied Motion Tech. Inc. (NASDAQ:AMOT) | 10-Apr-14 | \$12.00 | \$31.52 | 162.7% | 14.6% | 149.2% |
| Ascent Capital Group Inc. (NASDAQ:ASCMA) | 28-Apr-14 | \$68.34 | \$40.00 | -41.5% | 12.8% | -53.0% |
| SWK Holdings Corporation (OTCQB:SWKH) | 29-Apr-14 | \$1.05 | \$1.60 | 52.4% | 12.3% | 41.4% |
| Monitise PLC (OTCPK:MONIF) | 12-May-14 | \$1.08 | \$0.21 | -80.4% | 11.1% | -90.2% |
| Darling Ingredients Inc. (NYSE: DAR) | 27-May-14 | \$19.67 | \$13.73 | -30.2% | 10.2% | -39.5% |
| Radiant Logistics, Inc. (NYSE MKT: RLGT) | 29-May-14 | \$3.09 | \$5.26 | 70.2% | 9.8% | 61.3% |
| Willdan Group, Inc. (NASDAQ:WLDN) | 31-May-14 | \$6.25 | \$14.40 | 130.4% | 9.7% | 121.6% |
| MOCON, Inc. (NASDAQ:MOCO) | 9-Jun-14 | \$15.25 | \$17.90 | 17.4% | 7.9% | 10.2% |
| Global Power Equipment Inc. (NASDAQ:GLPW) | 26-Jun-14 | \$16.52 | \$12.22 | -26.0% | 7.6% | -33.2% |
| Primo Water Corporation (NASDAQ:PRMW) | 30-Jun-14 | \$4.77 | \$5.16 | 8.2% | 7.2% | 1.1% |
| Spectra7 Microsystems Inc. (TSX.V:SEV) | 30-Jun-14 | \$0.44 | \$0.66 | 50.0% | 7.2% | 42.9% |
| Maxwell Technologies, Inc. (NASDAQ:MXWL) | 20-Jul-14 | \$12.77 | \$5.84 | -54.3% | 6.9% | -60.3% |
| Tower Semiconductor Ltd. (NASDAQ:TSEM) | 23-Jul-14 | \$10.90 | \$14.92 | 36.9% | 6.4% | 31.1% |
| Schnitzer Steel Industries, Inc. (NASDAQ:SCHN) | 25-Jul-14 | \$27.42 | \$17.31 | -36.9% | 6.9% | -43.2% |
| Vertex Energy, Inc. (NASDAQ:VTNR) | 31-Jul-14 | \$8.22 | \$2.16 | -73.7% | 9.5% | -82.7% |
| Bolt Technology Corp. (NASDAQ:BOLT) | 5-Aug-14 | \$17.43 | \$22.00 | 26.2% | 10.0% | 16.6% |
| Tribune Publishing Corp. (NYSE:TPUB) | 20-Aug-14 | \$19.55 | \$17.73 | -9.3% | 6.3% | -15.3% |
| Interphase Corp. (NASDAQ:INPH) | 29-Aug-14 | \$3.27 | \$1.34 | -59.0% | 5.3% | -64.1% |
| Richardson Electronics Ltd. (NASDAQ:RELL) | 31-Aug-14 | \$10.19 | \$8.89 | -12.8% | 5.3% | -17.9% |
| Helen of Troy (NASDAQ:HELE) | 15-Sep-14 | \$54.62 | \$87.34 | 59.9% | 6.5% | 53.9% |
| SMTP, Inc. (NASDAQ:SMTP) | 16-Sep-14 | \$6.26 | \$5.62 | -10.2% | 5.8% | -15.5% |
| Mandalay Digital Group, Inc. (NASDAQ:APPS) | 24-Sep-14 | \$4.92 | \$3.68 | -25.2% | 6.2% | -30.5% |
| L.B. Foster Company (NASDAQ:FSTR) | 30-Sep-14 | \$45.94 | \$42.84 | -6.7% | 7.7% | -13.3% |
| Chart Industries, Inc. (NASDAQ:GTLIS) | 13-Oct-14 | \$42.06 | \$42.43 | 0.9% | 13.6% | -11.0% |
| MRI Interventions, Inc. (OTC BB: MRIC) | 16-Oct-14 | \$1.08 | \$1.04 | -4.1% | 13.6% | -16.7% |
| Franklin Electric Co., Inc. (NASDAQ:FELE) | 23-Oct-14 | \$36.99 | \$36.16 | -2.2% | 8.6% | -10.3% |
| Avigilon Corporation (TSX:AVO.TO) | 29-Oct-14 | \$15.30 | \$20.69 | 35.2% | 6.9% | 29.0% |
| Chemtura Corporation (NYSE:CHMT) | 6-Nov-14 | \$23.38 | \$30.24 | 29.3% | 4.4% | 25.9% |
| Hilltop Holdings Inc. (NYSE:HTH) | 11-Nov-14 | \$21.14 | \$20.04 | -5.2% | 3.9% | -8.2% |
| Bravo Brio Restaurant Group, Inc. (NASDAQgs:BBRG) | 24-Nov-14 | \$13.15 | \$14.86 | 13.0% | 2.5% | 11.4% |
| Alamo Group (NYSE: ALG) | 26-Nov-14 | \$48.97 | \$62.80 | 28.2% | 2.3% | 26.8% |
| PGT, Inc. (NASDAQ:PGTI) | 12-Dec-14 | \$9.00 | \$11.35 | 26.1% | 6.0% | 21.1% |
| Unilife Corporation (NASDAQ:UNIS) | 15-Dec-14 | \$2.72 | \$3.40 | 25.0% | 6.7% | 19.4% |
| The Dixie Group, Inc. (NASDAQ:DXYN) | 19-Dec-14 | \$9.21 | \$9.77 | 6.1% | 2.5% | 4.5% |
| Points International Ltd. (NASDAQ:PCOM) | 20-Dec-14 | \$12.86 | \$11.94 | -7.2% | 2.5% | -8.8% |
| Cascade Microtech Inc. (NASDAQ:CSCD) | 19-Jan-15 | \$14.02 | \$13.29 | -5.2% | 4.8% | -9.0% |
| Quanex Building Products Corporation (NYSE:NX) | 20-Jan-15 | \$18.53 | \$19.57 | 5.6% | 4.7% | 1.9% |
| Ballantyne Strong, Inc. (NYSE:BTN) | 27-Jan-15 | \$4.15 | \$4.67 | 12.5% | 4.0% | 8.9% |
| InfuSystem Holdings, Inc. (NYSE:INFU) | 29-Jan-15 | \$2.71 | \$3.13 | 15.5% | 4.4% | 11.6% |
| EXO U Inc. (EXO.V) | 23-Feb-15 | \$1.65 | \$0.99 | -40.0% | 0.0% | -39.6% |
| Liquidity Services, Inc. (LQDT) | 24-Feb-15 | \$9.79 | \$9.41 | -3.9% | -0.2% | -3.2% |
| Smith & Wesson Holding Corporation (NASDAQ:SWHC) | 25-Feb-15 | \$12.89 | \$14.85 | 15.2% | -0.2% | 15.9% |
| Actua Corporation (NASDAQ:ACTA) | 26-Feb-15 | \$16.47 | \$14.67 | -10.9% | 0.0% | -10.3% |
| MA-Com Technology Solutions Holdings, Inc. (NASDAQ:MTSI) | 28-Mar-15 | \$35.81 | \$31.03 | -13.3% | 1.9% | -15.1% |
| Overall Performance since July 2008 | | | | 74.3% | 57.2% | 17.1% |

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The value proposition of the digest is essentially an "Idea Generator". During the course of my 18-year career in capital markets, I've had the chance to meet and work closely with some very smart professional investors who have consistent track records of outperforming the market indexes. Some of these investors, which include mutual fund managers, hedge fund managers, and other professional investors, are kind enough to share their best ideas with me. I conduct my own analysis of their ideas and publish summaries of those ideas I think represent timely investment opportunities. Over time, I trust the majority of these ideas will pan out and help subscribers generate index-beating returns.

The goal of the Best Idea Profiles in this newsletter is to briefly describe the most relevant investment merits and risks of a company. It is not intended to be an exhaustive report including every detail. With limited space available, I am forced to include only those data points that I feel are most important for subscribers to know before they begin their own due diligence. Thank you for your interest in Mossberg's Investor Digest.

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