

Mossberg's Investor Digest

April 2016

Issue #94

From the Editor...

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

35-year-old, **PAR Technology Group (NYSE: PAR)** operates two separate businesses. The Hospitality segment (62% of revenue) is a global provider of point of sale (POS) terminals, software and services to restaurants, grocery stores and specialty retail outlets. This business has deployed 500,000 point of sale terminals in 110 countries worldwide with a global support and services infrastructure.

The second segment is Government, which represents 38% of sales and helps the department of defense and intelligence agencies develop advanced signal and image processing and management technologies on a contract basis. While investors should not be in a hurry for the company to divest this asset, it is a logical step in the transformation process of PAR, which could eventually yield \$35 to \$45 million in a divestiture.

In the hospitality segment, the company offers a system under the SureCheck brand that allows grocery stores, food distributors, restaurants, etc. to more easily track and comply with food safety requirements. This product line should grow dramatically in the coming years as Food industry executives make safety compliance their top priority.

Over the past couple of years, the company has made several strategic moves that better position itself to compete in the POS market. As a result, the company has begun to show significant improvement in financial performance. Initiatives to show further improvement are ongoing and should allow for even greater improvement in operating margin going forward.

In our back of the envelop the sum of the parts calculation, we show a potential value of \$12 to \$15 per share in the next three years, which is more than 2x the current valuation.

As always, I appreciate your feedback.

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

Pure Cycle Corporation (Nasdaq: PCYO) - Is a vertically integrated wholesale water and wastewater service provider that contracts with landowners, land developers, home builders, cities and municipalities to design, construct, operate and maintain water and wastewater systems. As a vertically integrated wholesale service provider, they own all assets necessary to provide water and wastewater services to customers. PCYO designs, constructs, manages, operates and maintains water and wastewater systems. They are vertically integrated which means they own all assets necessary to provide wholesale water and wastewater services to local governmental entities and their end-use customers.

Balchem Corp. (Nasdaq: BCPC) - Balchem Corporation engages in the development, manufacture, and marketing of specialty performance ingredients and products for the food, nutritional, feed, pharmaceutical, and medical sterilization industries in the United States and internationally. Balchem is one of the leading producers of choline. They have a highly skilled management team in place and are well positioned for future growth organically and through acquisitions, JV's and partnerships.

Global Partners LP (NYSE: GLP) - Is a midstream logistics and marketing company that owns, controls or has access to one of the largest terminal networks of petroleum products and renewable fuels in the Northeast. Global also is one of the largest distributors of gasoline, distillates, residual oil and renewable fuels to wholesalers, retailers and commercial customers in New England and New York. The Partnership is engaged in the transportation of crude oil and other products by rail from the mid-continental U.S. and Canada to the East and West Coasts for distribution to refiners and others. With approximately 1,600 locations, mainly in the Northeast, Global also is one of the largest independent owners, suppliers and operators of gasoline stations and convenience stores. Global is No. 180 in the Fortune 500 list of America's largest corporations.

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Mossberg's Investor Digest Idea Performance

The table below shows the relative change in the value of the ideas published since March 2015 and the Russell 2000. **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 2000 Change Since Pub.	Relative Perf. vs. Russell 2000	
M/A-Com Technology Solutions Holdings, Inc. (NASDAQ:MTSI)	28-Mar-15	\$35.81	\$40.66	13.5%	-8.1%	21.6%	
Kimball International, Inc. (NASDAQ:KBAL)	30-Apr-15	\$9.97	\$11.54	15.7%	-6.5%	22.3%	
Ironclad Performance Wear Corp. (OTC:ICPW)	30-May-15	\$0.27	\$0.26	-3.7%	-8.5%	4.8%	
Customers Bancorp, Inc. (NYSE: CUBI)	30-Jun-15	\$26.87	\$25.99	-3.3%	-9.1%	5.8%	
Potbelly Corporation (NASDAQ: PBPB)	30-Jul-15	\$13.43	\$14.15	5.4%	-7.4%	12.8%	
Cosi Inc. (NASDAQ:COSI)	31-Aug-15	\$1.17	\$0.70	-40.2%	-1.6%	-38.5%	
Calloway Golf Company (NYSE: ELY).	30-Sep-15	\$8.39	\$9.30	10.8%	3.6%	7.2%	
New Gold (NYSE: NGD).	31-Oct-15	\$2.47	\$4.67	89.1%	-1.8%	90.9%	
Townsquare Media (NYSE: TSQ)	30-Nov-15	\$11.43	\$10.70	-6.4%	-4.8%	-1.6%	
Build-A-Bear Workshop (NYSE: BBW)	31-Dec-15	\$11.72	\$13.03	11.2%	0.4%	10.8%	
Dycom Industries, Inc (NYSE: DY)	31-Jan-16	\$62.18	\$69.79	12.2%	10.1%	2.1%	
Rackspace Hosting, Inc. (NYSE: RAX)	29-Feb-16	\$21.54	\$22.76	5.7%	10.3%	-4.6%	
Kopin Corporation (Nasdaq:KOPN)	31-Mar-16	\$1.66	\$1.65	-0.6%	2.4%	-3.0%	
				Average	8.4%	-1.6%	10.0%

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Best Idea Profile:

PAR Technology Corporation (NYSE: PAR)

DESCRIPTION:

35-year-old, **PAR Technology Group (NYSE: PAR)** operates two separate businesses.

1) Hospitality (62% of revenue) - The Hospitality segment is a global provider of point of sale (POS) terminals, software and services to restaurants, grocery stores and specialty retail outlets. This business has deployed 500,000 point of sale terminals in 110 countries worldwide with a global support and services infrastructure. POS customers include well-known fast and fast casual restaurant chains such as McDonalds (19% of revenue), YUM! Brands (10% of revenue), Subway, Baskin-Robbins, Dunkin' Brands, CKE restaurants, Five Guys & Jack in the Box. In addition to its POS offering, the company offers a system under the SureCheck brand that allows grocery stores, food distributors, restaurants, etc. to more easily track and comply with food safety requirements. Significant customers for SureCheck include Walmart and Wegmans Food Markets.

Over the past couple of years, the company has made several strategic moves that better position itself to compete in the POS market. As a result, the company has begun to show significant improvement in financial performance. Revenue from the Hospitality segment increased 8% and operating income margin increased by 100 basis points to 1.2% of sales. Initiatives to show further improvement are ongoing and should allow for even greater improvement in operating margin going forward.

2) Government (32% of revenue) - On a contracted service basis, the Government business helps the department of defense and intelligence agencies develop advanced signal and image processing and management technologies.

PAR Technology Corporation (NYSE: PAR)

Investment Data (as of 4/29/16)

Recent Price	\$6.39
52-Week Range	\$3.80 - \$7.53
Fiscal Year End	December
Dividend	N/A
Yield	N/A
Shares Outstanding	16 M
Average Trading Volume (3 mos)	35,000
Market Capitalization	\$100 M
Cash*	\$2 M
Long-term Debt	\$6 M
Enterprise Value (EV)	\$104 M
Book Value	\$4.31
P/ Book	1.5 x
TTM Revenue	\$247 M
EV/ Revenue	0.4 x
TTM EPS (consensus)	(\$0.25)
P/ EPS	n/a

Headquartered in central New York State (New Hartford) with three U.S. and seven international locations, the company has approximately 1,000 employees.

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KEY INVESTMENT CONSIDERATIONS:

Becoming a Pure play in POS software/ systems/ and services

- **Divest underperforming businesses** – Late last year, the Company sold its hotel and spa management system business, PAR Springer-Miller systems, to Constellation Software for \$16.6 million. While this business had gained significant traction in the luxury spa and hotel market, it was having difficulty transitioning customers and prospects to a cloud-based offering. Divesting this unit allows management to focus on the more successful aspects of their business and removes a significant drag on earnings. During 2014 and 2015, this business lost \$4.9 million and \$3.7 million, respectively.
- **Acquire businesses that accelerate growth, improve margin and create recurring revenue streams** – The Company acquired cloud-based point of sale software provider, Brink, in September of 2014 for \$15 million. Cloud-based solutions are becoming increasingly popular among restaurant chains as they provide several benefits. The cloud solution does not require a server to be in each store, and as such, all software changes can be made in the cloud. Not only does this remove the cost of sever hardware and the corresponding maintenance cost, it eliminates the cost associated with installing updates at each store.

Brink is experiencing significant growth - During 2015, the company deployed Brink software to 700 stores, bringing the total deployed store count to 1,000 at the end of the year. In the past 18 months the company has announced wins with 10 restaurant chains with nearly 2,000 stores, which implies a healthy backlog of new business. As of the last earnings call management said the pipeline of new customers continues to grow in across all restaurant segments including fast casual, quick serve and table service.

Pancheros - 65 stores

Giardino - 12 stores

Tom+ Chee - 50 stores

Bibibop - 10 stores

Modern Market - 15 stores

Five Guys - 1,300 stores

Moose Rocky Mountain Deli - 20 stores

Pita Pit - 250 stores

MOD Pizza - 115 stores

Sonny's BBQ - 119 stores

- **Monetizing the Government Business** – While investors should not be in a hurry for the company to divest this asset, it is a logical step in the transformation process of PAR. The Government business is a stable and highly predictable business with an average contract term of 2.5 years. Over the past several years, revenue has been relatively flat at around \$88 million with a consistent operating margin of 5% to 6%. As such, this business has generated the bulk of the company's profitability over the past several years and it seems unlikely that management would consider divesting this business in the near term. As the hospitality segment continues to show growth and improved margin performance, the likelihood of a divestiture will increase.

What what's the Government Business worth? - A \$35 to \$45 million valuation would imply a multiple of 7-9x EBITDA, which seems reasonable for stable business with consistent financial performance.

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KEY INVESTMENT CONSIDERATIONS: (Continued)

Food Safety – When the CEO is at risk of going to jail

Outbreaks of foodborne illness are shockingly high – While hurting your brand, or your making your customers sick should be reason enough for food retailers and restaurants to follow food safety guidelines, the reality is that these reasons are not enough. An estimated 1 in 6 Americans get sick from foodborne illness every year, resulting in 128,000 hospitalizations and 3,000 deaths. Young children, the elderly, pregnant women and their expected children are especially susceptible to foodborne pathogens such as Salmonella, E. coli and Listeria.

Strong Selling Tool... We can help you NOT go to jail - The Food Safety Modernization Act (FSMA) is putting pressure on food retailers and restaurants. FSMA was signed into law in 2011, but has just begun to be implemented over the past year. Among a long list of other rules related to Food, the Act essentially mandates continuous monitoring of food handling and preparation in compliance with Hazard Analysis and Critical Control Point (HACCP) guidelines. Basically the "guidelines" are now "the law" and not following the law offers serious consequences not only in terms of civil liability, but also criminal liability. Under Supreme Court case law, the "Park Doctrine" provides that corporate officials can be held criminally liable (second time offense is a felony) and there does not have to be proof that the corporate official acted with intent, or even negligence. The number of criminal prosecutions is just beginning to increase, and as we start to see food industry executives in orange jump suits, the food safety will become the top priority for every industry executive. [Read more here...](#)

SureCheck – Food safety automation system – SureCheck is an integrated hand-held device that records and stores temperature and other data in the cloud. The system is easy to use and mostly competes against a thermometer, pens, and legal note pads. Besides costs saving through efficiencies gains, the system can help monitor and ensure safety procedures are being followed.

One of the first customers for SureCheck was Walmart, who has deployed the system in its domestic locations and has just begun to deploy the system in its 7,500+ international locations. Other customers include Wegmans, Festival Foods, and Lunds & Byerlys supermarket chains.

Management Changes

A new CEO – Daughter of the Company's founder and current board member, John Sammon, 51-year old Karen Sammon was appointed to CEO and the board on January 1, 2016. Collectively, Ms. Sammon has 20 years of experience at various senior level management positions at the company, including most recently President of Hospitality unit since 2013. Ms. Sammon's experience also includes leading strategic planning and management of CBORD's US and Asia/Pacific operations.

A CFO mistake – After being named to the position in late July 2015, former CFO, Michael Bartusek, was terminated for cause in March of 2016 in connection with making unauthorized investments. The funds, which totaled less than \$900,000 were invested in contravention of the Company's policies. The company charged off \$776,000 related to the inappropriate fund transfer, but continues to pursue recovery. The Company is currently searching for a new CFO. While this likely has spooked investors, the issue was handled and communicated to investors well.

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Valuation

(\$ in millions)	Assumptions	2015	2018
Product Revenue	5% Growth Rate	94.4	109.3
Service Revenue	15% Growth Rate	46.8	71.1
Total Revenue		141.2	180.4
Product Gross Profit		26.2	30.6
Product Gross Margin	Unchanged	28%	28%
Service Gross Profit		13.9	27.0
Service Gross Margin	+800 basis points	30%	38%
Total Gross Profit		40.1	57.6
Operating Expenses	5% Growth Rate	38.4	44.5
Operating Profit		1.7	13.2
Operating Margin		1.2%	7.3%
Tax	35% Tax Rate		4.6
Net Income			8.6
EPS			\$ 0.53
Shares Outstanding			16

In our back of the envelop calculation, we break out the hospitality segment from government division and value each separately.

Back of the envelope assumptions for hospitality segment:

Revenue Growth: We assume that average annual product revenue growth will be 5% while service revenue will grow at 3x that pace (15%), which will be driven by the adoption of Brink and SureCheck software-as-a-service sales.

Gross Margin: We expect product margins will continue to face pressure and remain near levels achieved in 2015. Due to the mix shift to higher margin software sales, we expect an 800 basis points improvement in services revenue.

Other: Operating expenses are expected to increase at 5%, tax rate is assumed to be 35% and share count is assumed to increase modestly to 16 million

Based on these assumptions, we believe the hospitality segment has roughly \$0.50 in earnings power during the next three years. Given the potential to accelerate growth and improve margins, we believe this business could reasonably command a P/E multiple of 20x to 25x, which would yield a valuation of \$10 to \$12. Based on a \$35 million to \$45 million (\$2 to \$3/share) valuation for the government business described earlier, the sum of the parts would be \$12 to \$15 per share in the next three years, which is more than 2x the current valuation.

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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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