

Mossberg's Investor Digest

August 2016

Issue #98

From the Editor...

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

For the past 90 years, **Ampco-Pittsburgh (NYSE: AP)** has been a key supplier of hardened steel rolls used in the production of rolled steel and aluminum products. For lack of a better analogy, these "hardened steel rolls" are like giant rolling pins. Instead of being used to make pie crusts, they are used to make sheet metal, or other rolled steel products at an industrial scale. For perspective, finished rolls come in weights of 2 kg to 71 metric tons, the same weight as 40 average-sized automobiles. In addition, the company uses its large-scale cast and forging capabilities to provide other hardened and machined parts for use in oil and gas, aluminum and plastic extrusion industries.

With its acquisition of the leading European provider, Åkers Group, earlier this spring, effectively the number one and two players have combined making Ampco the largest producer of cast and forged hardened steel rolls in the world, which should provide greater market discipline, as well as efficiencies of scale and scope.

Based on our assumptions we believe the company could earn \$1.50 per share in 2018. Given AP's diversification strategy, potential for further growth, improvement in margins, improvement in returns, and dominant market position, we believe shares should easily be able to command a mid-teens, or higher multiple of earnings. At 15x 2018, shares would trade at 2x current levels.

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 a few of the ideas we heard this month, but have not reviewed in detail...

OMNOVA Solutions (NYSE OMN) – OMNOVA Solutions is a specialty chemical company that has undergone significant restructuring in the past several years. The company focuses on small and niche markets that provide opportunities for growth, differentiation and higher margin and returns. The restructuring plans have already produced an improvement in operating margin from 6.9% to 10.3%, and further improvement to mid-teens margin is expected.

NovoCure Limited (Nasdaq: NVCR) - NovoCure Limited has developed and begun selling a medical device that uses tumor treating fields (TTFields) for use as a treatment for adult patients with glioblastoma brain cancer. TTFields non-invasively disrupt the growth of cancer by emitting electric fields in cancer cells. The company is developing technology incorporating its similar proprietary TTFields technology for other hard body cancers. Commercialization is ramping nicely and the company has plenty of cash to fund growth to cash flow positive contribution levels, as well as development of technology for treatment of other cancers.

Triumph Bancorp, Inc (NYSE:TBK) – Triumph Bancorp is a community bank, uniquely diversified for its size. Its community bank is focused on small town markets, in IL and CO, where it can be the dominant bank in the area. In addition, the company has a rapidly growing commercial finance business that does asset based lending and factoring primarily to smaller transportation companies. And finally, the bank earns fee income as an asset manager of CLOs. Because of its commercial finance business, the company is able to garner a net interest margin in excess of 5%, which is far greater than the 3% that most community banks earn.

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Best Idea Profile:

Ampco-Pittsburgh Corp. (NYSE: AP)

DESCRIPTION:

For the past 90 years, **Ampco-Pittsburgh (NYSE: AP)** has been a key supplier of hardened steel rolls used in the production of rolled steel and aluminum products. For lack of a better analogy, these "hardened steel rolls" are like giant rolling pins. Instead of being used to make pie crusts, they are used to make sheet metal, or other rolled steel products at an industrial scale. For perspective, finished rolls come in weights of 2 kg to 71 metric tons, the same weight as 40 average-sized automobiles. In addition, the company uses its large-scale cast and forging capabilities to provide other hardened and machined parts for use in oil and gas, aluminum and plastic extrusion industries.

With its acquisition of the leading European provider, Åkers Group, earlier this spring, effectively the number one and two players have combined making Ampco the largest producer of cast and forged hardened steel rolls in the world, which should provide greater market discipline, as well as efficiencies of scale and scope.

AP operates two segments. 1) **Forged and Cast Engineered Products** segment, which encompasses the products described above and makes up approximately 2/3 of revenue, and 2) the remaining revenue is generated from the **Air & Liquid Processing** segment, which is further separated into three divisions. *Aerofin* manufactures custom-designed specialty heat exchanges used by the oil & gas, nuclear power, automotive, industrial process and HVAC industries, air handling systems, and centrifugal pumps. *Buffalo Air Handling* manufactures large customer air handling systems used in commercial, institutional and industrial buildings. And, *Buffalo Pumps* manufactures centrifugal pumps for the refrigeration, power generation and marine defense industries.

Headquartered in Carnegie, Pennsylvania, Ampco-Pittsburgh employs 1,800 people and has 15 manufacturing facilities in the U.S., Europe and China. (12 in Forged and Cast Engineering Products segment, 3 in Air & Liquid Processing segment)

Ampco-Pittsburgh Corp. (NYSE: AP) Investment Data (as of 8/30/16)

Recent Price	\$11.12
52-Week Range	\$8.88 - \$19.22
Fiscal Year End	December
Dividend	0.54
Yield	4.1%
Shares Outstanding	12.3 M
Average Trading Volume (3 mos)	57,000
Market Capitalization	\$135M
Cash	\$46 M
Long-term Debt	\$44 M
Enterprise Value (EV)	\$133 M
Book Value	\$18.04
P/ Book	0.7 x
Proforma Revenue 2016	\$390 M
EV/ Revenue	0.34 x
TTM EPS	-0.69
P/EPS	N/A
2018 EPS Est.	\$1.50
P/2016E	7.3x

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KEY INVESTMENT CONSIDERATIONS:

Transitioning from a "private/public" company

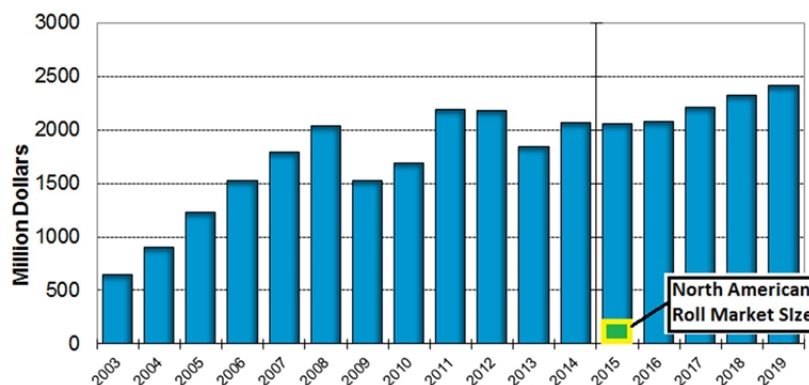
Since its founding, the CEO position and several board seats have been occupied by AP's founder, Louis Berkman, his son (Marshall Berkman), son-in-law (Robert Paul) and grandsons (Stephen & Laurence Paul). While the family still owns a 12% stake and occupies two board seats, since Louis Berkman's passing in 2013 (at the age of 104), control has been transitioning into independent hands. The first outside CEO, John Stanik, has been hired and Robert Paul (son-in-law of the founder) retired from the Board and Chairman position in May of 2016. The independence of the board has also increased with two board seats added at the request of long-time investor GAMCO, and a new board member joined from the recent acquisition of Åkers.

New Leadership has been there and done that – Joining the company in January of 2015, 62-year-old John Stanik, came out of retirement to apply a turnaround strategy that was similar to the one he used to successfully lead the turnaround of Calgon Carbon Corporation (NYSE: CCC). During his 9-year tenure as CEO of Calgon (from 2003 till 2012), annual revenue doubled from approximately \$275 million to \$550 million, losses turned to consistent profits, returns were consistently 8% to 12%, and shares appreciated 150%+. That is a compound return of 11% per year, which is more than 2x the 4.5% return of the Russell 2000 during that same time period.

Implemented Strategic Plan – November of 2015

Upon joining Ampco-Pittsburgh, CEO, John Stanik began implementing a strategic plan to deliver organic annual top line growth of 15% for Forged and Cast Engineered Products segment, and 7%, and the Air & Liquid Processing segment. Profitability goals of the plan are to restore net margins to 4%, which is consistent with levels achieved as recently as 2013.

More aggressively entering other segments of open die market, which is 7x larger than roll market alone – As the chart below shows, the North American market for steel rolls is approximately \$300 million. Comparatively, the North American market size for open die products is more than \$2 billion. Existing manufacturing assets can be leveraged to make products for these new segments. Although currently representing a small portion of company's revenue, sales of ingot and open die forged products outside of steel rolls are expected to grow and become a more significant portion of overall revenue. New targeted markets include blow-out preventers, gears, mining bits, mud pump blocks and crankshafts, shafts, wellhead forgings and wye blocks. Not only will these new markets provide growth opportunities, they will also diversify the Company's end markets, which should reduce fluctuations in revenue and earnings trends due to steel industry cycles.

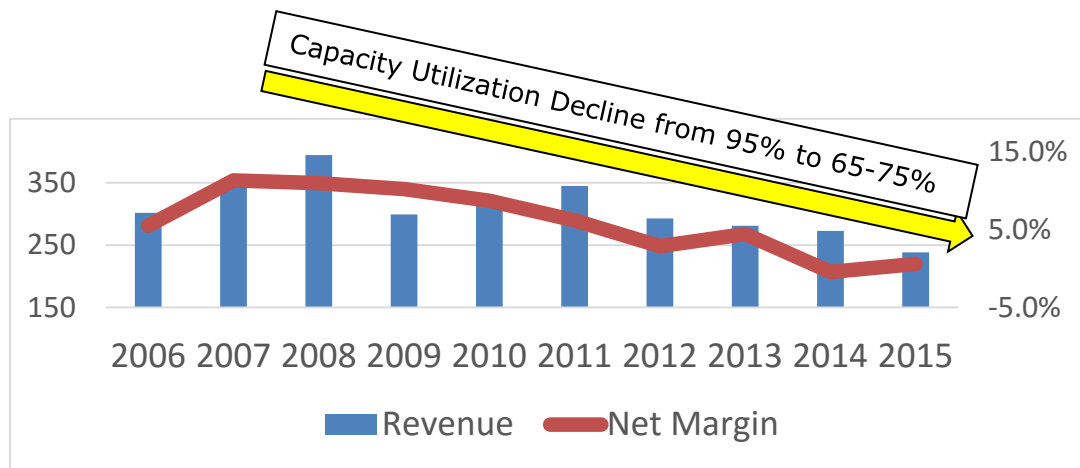


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Strategic Plan (Continued)

Increase capacity utilization – Due to an extended weakness in the steel industry, AP's utilization rates have fallen from a level of 95% to 65-75% over the past several years, which among other factors including pricing, has caused a drop in revenue and an even more significant drop in net income margin. As shown in the chart below, at the peak of the last cycle in '06-'08, AP was operating near capacity and producing net income margin in the high single digits. By adding incremental revenue from new end markets, management plans to fill the unused capacity, significantly mitigate the traditional cyclical "roller coaster" ride of the steel industry, and allow the company to return to mid-single-digit net margin on a more consistent basis.



\$10 million corporate-wide cost reduction program – The strategic plan includes a cost reduction effort of centralizing overhead functions, 10% reducing the work force (100 employees), and freezing the defined pension plan. Part of the cost reduction also includes a relocation of the corporate headquarters, saving \$0.5 million annually.

An opportunity not to be passed

Acquisition of Åkers at bargain prices - Part of the Strategic plan also includes acquisitions. Due to the length and severity of the most recent downturn in the steel industry, there are some valuable companies that can be purchased at bargain prices (picking up debt, very small amounts of cash, etc.). It was anticipated that most M&A opportunities would be with relatively small "tuck-in" acquisitions, it was not anticipated that there would be an opportunity to buy Åkers, which has historically been AP's largest competitor and largest player in Europe.

- **Bargain Price** – AP paid \$77 million (\$29 million in cash, 1.78 million shares in stock, and \$26 million note bearing 6.5% interest). Relative to the €340 million price paid by Åkers' former parent, Altor, paid in 2008, this appears to be a significant bargain price.
- **\$15 million in acquisition synergies**
- **Gaining efficiencies of scale and scope**
- **Purchase price adjustments** – The purchase price has been adjusted by 10%, to \$72 million and the company is pursuing other claims to further adjust the purchase price. The claims relate to contract margins, which were not disclosed to AP and were underestimated during the due diligence stage of the transaction. Because these margins were lower than estimated, the transaction is now expected to be accretive early next year. Regardless of the delay in accretion, the transaction does not affect the long term value creation of the deal.

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Improving market conditions

In recent years, the global steel industry has been under significant pressure mainly due to overcapacity from China, and slower growth rates. As a result, the profitability of the U.S. and European steel producers fell to the lowest levels seen in more than 20 years. In 2016, several factors are driving improving conditions for U.S. and European producers, which should allow for improved profitability and more demand for AP's products.

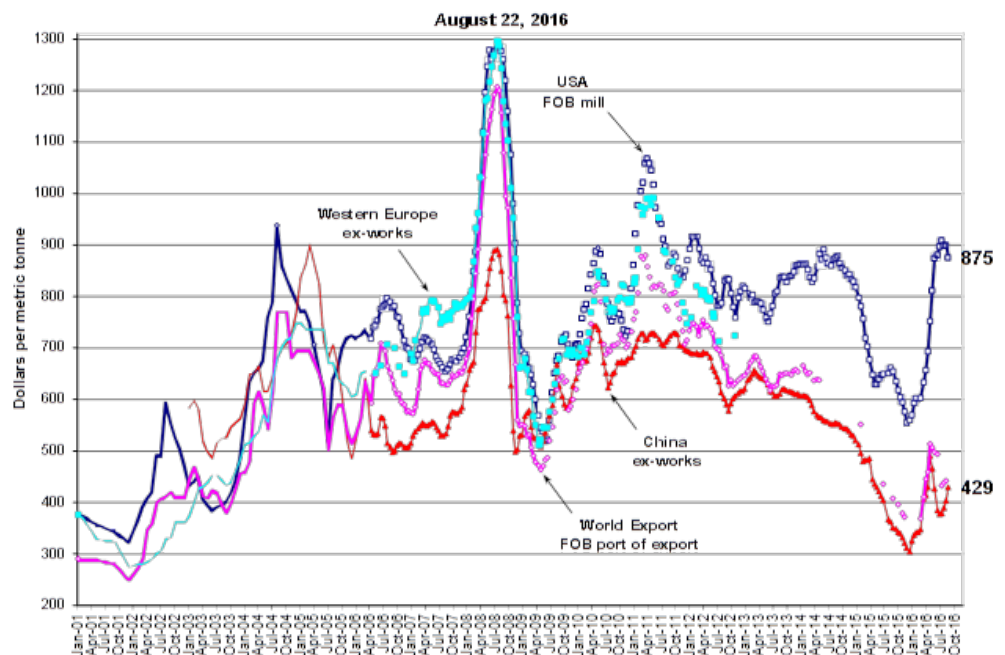
Improved Utilization - U.S. Mills and European mills typically operate at about 85% utilization. Last year, utilization was 62% to 65%. So far this year, mill capacity has improved to 73% to 75%.

Capacity rationalization – China plans to reduce steel capacity by 100 to 150 Metric Tons (12% to 18% of current production) over the next 5 years and there will be no new capacity additions.

U.S. Steel Tariffs – After findings that Brazil, China, India, Japan, Korea, Russia and the U.K. were dumping steel in U.S. markets, the Department of Commerce imposed import tariffs ranging from 7% to 266%. Chinese imported steel, which received the highest tariff, has dropped significantly. Carbon flat roll imports from China have dropped about 1/3 this year, to the benefit of domestic producers.

Improved Pricing – The chart to the right shows the significant increase in steel pricing in recent months.

Improved Profitability – Price increases have outpaced costs and positioned steel manufacturers to return to normalized profit levels.



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Valuation

	2015	2017	2018
(in \$millions)			
Revenue	239	289	317
Growth Assumption	10%		
Åkers Incremental Revenue		150	150
Total Revenue		439	467
Net Margin		2.0%	4.0%
Net Income		8.8	18.7
Share Count	12.2	12.35	12.5
Earnings Per Share		\$0.71	\$1.50

In our back of the envelop calculation above, we make the following assumptions for growth and improvement in profitability:

- **Revenue Growth** – Over the next 2 ½ years, we assume base revenue (excluding Åkers) will grow at approximately 10% based on a management's strategic plans and a modest recovery in the steel industry. We assume no growth for Åkers' revenue.
- **Net Margin** – We assume net margin will recover to 4% of sales by 2018, which is conservative relative to margin levels the company has historically reached when operating at 85%+ of capacity.
- **Acquisitions** - We assume no acquisitions, although, we think smaller acquisitions are likely following the integration of Åkers.
- **Share Count** – We expect modest incremental growth in share count related to equity compensation.

Valuation – Based on our assumptions we believe the company could earn \$1.50 per share in 2018. Given AP's diversification strategy, potential for further growth, improvement in margins, improvement in returns, and dominant market position, we believe shares should easily be able to command a mid-teens, or higher multiple of earnings. At 15x 2018, shares would trade at 2x current levels.

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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	\$40.85	14.1%	0.0%	14.1%	
Kimball International, Inc. (NASDAQ:KBAL)	30-Apr-15	\$9.97	\$12.10	21.4%	1.6%	19.7%	
Ironclad Performance Wear Corp. (OTC:ICPW)	30-May-15	\$0.27	\$0.26	-3.7%	-0.5%	-3.2%	
Customers Bancorp, Inc. (NYSE: CUBI)	30-Jun-15	\$26.87	\$25.94	-3.5%	-1.1%	-2.3%	
Potbelly Corporation (NASDAQ: PBPB)	30-Jul-15	\$13.43	\$13.12	-2.3%	0.6%	-3.0%	
Cosi Inc. (NASDAQ:COSI)	31-Aug-15	\$1.17	\$0.23	-79.9%	6.9%	-86.9%	
Calloway Golf Company (NYSE: ELY).	30-Sep-15	\$8.39	\$11.34	35.1%	12.7%	22.4%	
New Gold (NYSE: NGD).	31-Oct-15	\$2.47	\$4.95	100.2%	6.7%	93.5%	
Townsquare Media (NYSE: TSQ)	30-Nov-15	\$11.43	\$9.40	-17.8%	3.5%	-21.3%	
Build-A-Bear Workshop (NYSE: BBW)	31-Dec-15	\$11.72	\$11.72	0.0%	9.2%	-9.2%	
Dycom Industries, Inc (NYSE: DY)	31-Jan-16	\$62.18	\$82.35	32.4%	19.8%	12.7%	
Rackspace Hosting, Inc. (NYSE: RAX)	29-Feb-16	\$21.54	\$31.56	46.5%	19.9%	26.6%	
Kopin Corporation (Nasdaq:KOPN)	31-Mar-16	\$1.66	\$2.21	33.1%	11.3%	21.8%	
PAR Technology Group (NYSE: PAR)	30-Apr-16	\$6.39	\$5.28	-17.4%	9.7%	-27.0%	
Full House Resorts Inc. (Nasdaq: FLL)	30-May-16	\$1.60	\$1.81	13.1%	7.8%	5.3%	
Control4 Corporation (Nasdaq: CTRL)	30-Jun-16	\$7.99	\$11.24	40.7%	7.6%	33.0%	
KapStone Paper and Packaging Corporation (NYSE: KS)	31-Jul-16	\$14.28	\$17.25	20.8%	1.6%	19.2%	
				Average	13.7%	6.9%	6.8%

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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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