

# Mossberg's Investor Digest

## From the Editor...

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

Headquartered in Los Angeles, 30+ year-old **Universal Electronics Inc. (Nasdaq: UEIC)** is the dominant worldwide provider of universal remote-control devices.

With 35%+ global market share for home entertainment device controllers (80% market share in the U.S.), UEIC has an impressive competitive moat which includes more than 400 patents and an extensive device control code database that covers more than one million individual device functions and approximately 8,100 individual consumer electronic equipment brand names.

In the same way that UEIC's technologies automatically detect, identify and enable control commands for the wide variety of devices that connect to home entertainment systems, UEIC has recently expanded its technologies (primarily through acquisition) to control the growing number of internet connected devices in the home. Turns out that many of the chipsets and technologies used in home entertainment controllers are the same ones used in home-connected devices. The Company is now providing chips, modules, remotes, sensors, and software for security and HVAC applications. While not broken out, we estimate home automation represents approximately 18% of revenue and is growing faster than 30% per year.

Currently the stock trades at just 10.5x 2018 implied EPS guidance. We expect that as margins improve and as more investors become aware of the Company's position in the smart home, the multiple could expand significantly. Assuming just a 15x multiple of 2020 and 2021 earnings, yields a valuation of \$49 and \$58, respectively.

Dave Mossberg  
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## December 2018

Issue #126

Every month we hear ideas suggested from our large network of professional investors. Here are a few of the ideas we heard this month.

**IRIDEX Corporation (Nasdaq: IRIX)**- Is a worldwide leader in developing, manufacturing, and marketing innovative and versatile laser-based medical systems, delivery devices and consumable instrumentation for the ophthalmology market. They maintain a deep commitment to the success of their customers, with comprehensive technical, clinical, and service support programs. IRIDEX products are sold in the United States through a direct sales force and internationally through a combination of a direct sales force and a network of approximately 70 independent distributors into over 100 countries.

**Verso Corporation (NYSE: VRS)**- Is the turn-to company for those looking to successfully navigate the complexities of paper sourcing and performance. The leading North American producer of printing and specialty papers and pulp, Verso provides insightful solutions that help drive improved customer efficiency, productivity, brand awareness and business results. Their printing papers are designed primarily for commercial printing, media and marketing applications, including magazines, catalogs, books, direct mail, corporate collateral and retail inserts. Their specialty papers are used primarily for label and converting, flexible packaging and technical paper applications.

**GreenSky, Inc. (Nasdaq: GSKY)**- GreenSky's proprietary technology platform addresses a large and growing opportunity in mobile, online and in-store point of sale finance, driving significant value for their constituents: merchants, banks and consumers. Their efficient go-to-market strategy leverages a B2B2C customer acquisition model resulting in strong recurring revenues, low customer acquisition costs and high merchant retention rates, delivering both growth and profitability to their shareholders.

**Central Garden & Pet Company (Nasdaq: CENT)**- Is a leading innovator, producer and distributor of branded and private label products for the lawn & garden and pet supplies markets. Committed to new product innovation, their products are sold to specialty independent and mass retailers.

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Best Idea Profile:

Universal Electronics Inc. (Nasdaq: UEIC)

## DESCRIPTION:

Headquartered in Los Angeles, 30+ year-old **Universal Electronics Inc. (Nasdaq: UEIC)** is the dominant worldwide provider of universal remote-control devices.

With 35%+ global market share for home entertainment device controllers (80% market share in the U.S.), UEIC has an impressive competitive moat which includes more than 400 patents and an extensive device control code database that covers more than one million individual device functions and approximately 8,100 individual consumer electronic equipment brand names.

In the same way that UEIC's technologies automatically detect, identify and enable control commands for the wide variety of devices that connect to home entertainment systems, UEIC has recently expanded its technologies (primarily through acquisition) to control the growing number of internet connected devices in the home. Turns out that many of the chipsets and technologies used in home entertainment controllers are the same ones used in home-connected devices. The Company is now providing chips, modules, remotes, sensors, and software for security and HVAC applications. While not broken out, we estimate home automation represents approximately 18% of revenue and is growing faster than 30% per year.

UEIC's customers include almost all of the major pay-TV operators in the world including Comcast, Charter, Dish, Echostar, SKY, Cox, Charter, etc. In addition, the company's technologies are imbedded in several major TV OEM's such as Samsung. Customers for home automation technologies include Daiken, one of the largest HVAC companies in the world, among others.

### Universal Electronics Inc. (Nasdaq: UEIC) Investment Data (as of 12/31/18)

<b>Recent Price</b>	<b>\$24.92</b>
52-Week Range	\$23.46 - \$55.90
Fiscal Year End	December
Dividend	N/A
Yield	N/A
Shares Outstanding*	14.0 M
Average Trading Volume (3 mos)	100,000
Market Capitalization	\$344M
Cash & Equivalents	\$42M
LT Debt	\$104MM
Enterprise Value (EV)	\$406M
TTM Revenue	\$691 M
EV/ Revenue	0.6x
Adj-EPS 2018 (guidance)	\$2.39 to \$2.49
P/E	10x
Book Value/ Share	\$19.70

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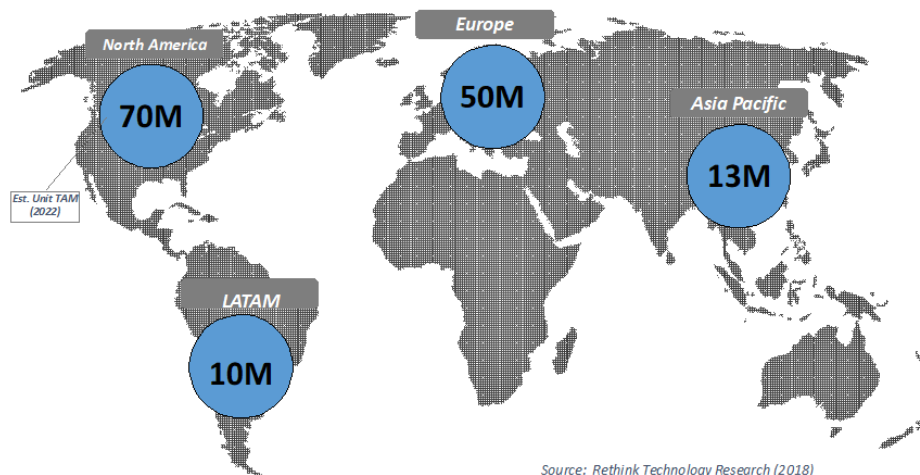
# Mossberg's Investor Digest

## KEY INVESTMENT CONSIDERATIONS:

### Major Growth Driver #1 – Pay-TV providers to upgrade in-home networks

There are two major trends that should drive significant revenue growth for UEIC in the coming years. The first is how pay-TV providers (cable and satellite) are reacting to the growing popularity of streaming television. More than 33 million adults in the U.S. alone have cancelled their cable subscriptions since streaming TV became available (according to eMarketer). This represents about 18% of the 187 million adults that watch traditional pay TV in the U.S. To keep customers from “cutting the cord” and/or to offset the loss of revenue from these subscribers, pay-TV providers are looking to leverage their infrastructure and offer new services, or otherwise differentiate themselves.

- **New service offerings will require new in-home infrastructure and new remote controls** – Service providers are offering new services such home security, lighting/thermostat control, etc. To offer these types of services, pay-TV providers need to upgrade the in-home network infrastructure, including the remote controls. Since many of these connected devices such as door sensors, or HVAC controllers are powered by batteries, they require RF connectivity that includes options for low power and battery efficiency. The next generation in-home infrastructure will include two-way mesh network that is capable of controlling and communicating with all of the devices in your home, not just those that are wired to direct power. Importantly, the ASP for UEIC’s remotes to control these systems will be 2-3x that of previous generation platforms.
- **New infrastructure will enable voice-controlled remotes** – One application that the new in-home infrastructure will enable, is voice-controlled remotes. Users can simply talk into the remote and search results will show up on the screen... with voice, users can search for anything and control other elements of the audio/ visual system or connected home automation devices. This technology is also cross-compatible with other voice products, such as Alexa... essentially the remote becomes the universal voice assistant for the home. This user interface is expected to be very popular. The largest Cable provider in the United States, Comcast, has been deploying this technology for a couple of years now through its Xfinity service and X1 box and UEIC’s XR 15 remote. According to the company, voice-controlled deployments will grow to more than 140 million by 2022. UEIC’s market share is estimated at more than 80%.



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## KEY INVESTMENT CONSIDERATIONS:

### Major Growth Driver #1 – Pay-TV providers to upgrade in-home networks (continued)

- **Why not just use our phones to control the devices... do we need a separate remote control?** - Mobile phones can function as a remote and UEIC offers application software that enables phones with infrared nodes (IR) to operate as such. The problem is that not all phones have IR nodes. Additionally, most consumers don't watch TV with their phones because they don't like to wake up the phone, open the application, and look at the phone to perform the operation. A remote is just easier... it is always on and most consumers don't have to look at the remote for basic functions because they have memorized where the buttons are.
- **The A/V system will be the center of the home** - The center of the smart home will most likely be the A/V system. People do not spend a lot of time setting their thermostats, or adjusting their blinds, or security features. They do spend a lot of time with the AV system... the average person in the U.S. consumes 4.5 hours of live TV or time-shifted (DVR) TV per day. This number has not changed in the last 10 years.
- **Strong value proposition for users** – In addition to voice control capabilities, the setup of these remotes is automatic. Users simply plug in the devices to each other and the software takes over. It identifies the device, blasts the code out to the remote, so that the device just simply works. When it is embedded in TV's, the remote will set up apps that appear on the TV screen such as watch Comcast, xbox and apple TV, etc. The system reconfigures the remote on the fly based on the device the user chooses.
- **We are in the early innings of the upgrade cycle** – The major operators in most of major markets in the world are in the process of rolling out the new in-home architecture, but it is happening a lot slower than originally anticipated. Many have been working on the rollout for the past two years, but only one of the major Cable MSOs, Comcast's Xfinity, has been deploying the new in-home network architecture for any length of time. The good news is that none of them have dropped out and all intend to move forward. While the timing and ramp of these deployments is difficult to determine, based on commentary from the last earnings conference call, it appears several are close to deployment..."I will say some of the projects that we're launching now were supposed to have launched in 2017. We had a few of those that were delayed that long but are now beginning to ramp finally."

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## KEY INVESTMENT CONSIDERATIONS:

### Major Growth Driver #2 –Home automation

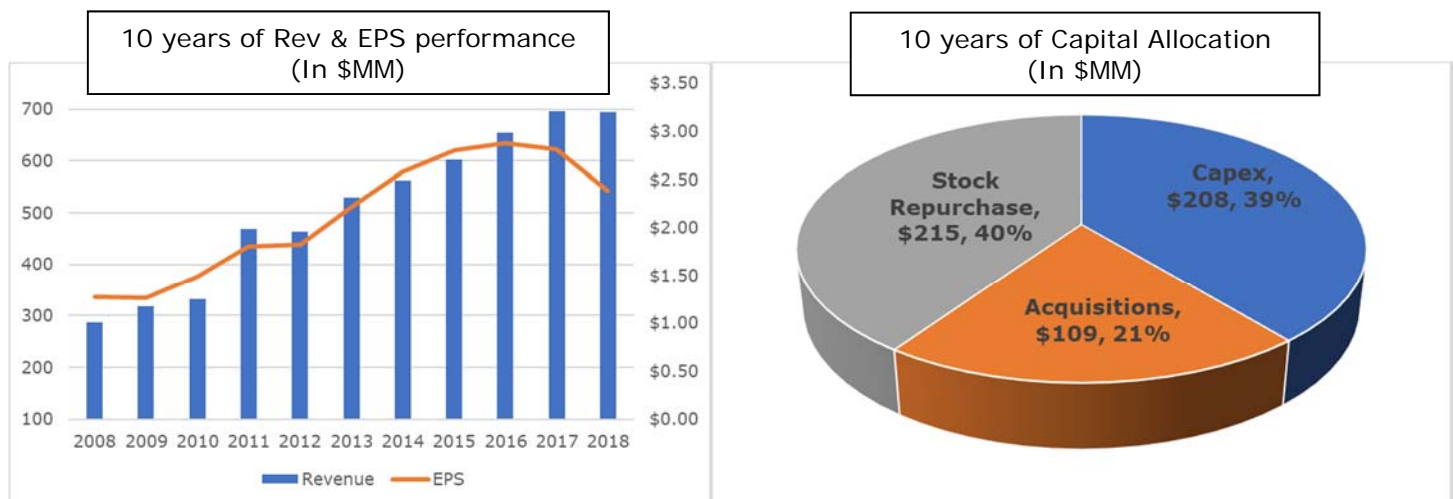
The protocols and chipsets that are being used for audio/visual control are similar, or are the same for home control (lighting, HVAC, sensors for windows/doors, motion sensors). With its scale and experience using these technologies, along with a sizable existing customer base, UEIC is in good position to become a significant player in home automation technologies. This year, the company expects home automation related revenue to reach \$130 million, a growth rate of 30% versus last year.

**Sizable and fast-growing market** – The Company's current smart home technologies are being sold into a \$5.3 billion annual market, which is growing at a CAGR of 19%. Current markets include smoke alarms, security sensors, smart lighting, smart thermostats, and garage door sensors. Because the technology architecture is similar, UEIC believes there are adjacent market opportunities in wireless cameras, smart blinds, hubs smart plugs, and smart door locks. These adjacent markets represent an addition \$4.8 billion in addressable market size.

**Strong relationship with existing customer base** – UEIC already has a large base of operators that are looking to deploy home automation technologies and services. As the cable and satellite companies deploy their new in-home technology platforms, they will increasingly begin to deploy new smart home services.

### Solid Track record of creating shareholder value

The CEO, Paul Arling, has been with the company for 20 years and is a proven operator. While there have been some up and down years (such as they are experiencing now), during the course of his tenure, the company has created tremendous shareholder value. Recent years' have included significant incremental investments in CAPEX as well as \$25 million in acquisitions. These investment along with other factors have created some near-term disruption in earnings growth, but have positioned the company well for the next leg of growth and an expansion in profitability and returns.



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## Valuation

	2018	2019	2020	2021
(In millions)				
Revenue	694	746	802	862
Revenue Growth		7.5%	7.5%	7.5%
Net Income Margin	4.8%	5.3%	5.8%	6.3%
Adjusted - Net Income	34	39.5	46.5	54.3
Diluted Shares	14.1	14.1	14.1	14.1
EPS	2.38	2.80	3.29	3.85

Our back of the envelop model makes the following assumptions:

**Revenue:** 2018 revenue reflects the mid-point of management's guidance. Our model assumes 7.5% annual growth for 2019 through 2021, which is within the range of management's long-term target of 5% to 10%. We believe our growth assumptions could be conservative. Many operators have delayed projects to upgrade their in-home network architectures, sometimes for more than a year. As such, there could be some pent-up demand as others look to catch up to Comcast and/or offset the negative impacts of streaming television.

**Net income margin:** Net income margin for 2018 reflects the mid-point of management's guidance. Margins have been depressed recently with changes manufacturing and increasing component costs driven by tariffs. We expect these factors will normalize, and along with operating leverage, will allow net margin to return 6.3%, which is the average during the last 10 years. Our model expands margin by 50 basis points for each year through 2021.

**Diluted Share count:** We assume no change in the diluted share count and expect that equity compensation will be offset by share repurchases.

**Valuation:** With 7.5% top line growth and modest expansion in margin, our model produces approximately 15% annual growth in earning over the next three years. Currently the stock trades at just 10.5x 2018 implied EPS guidance. We expect that as margins improve and as more investors become aware of the Company's position in the smart home, the multiple could expand significantly. Assuming just a 15x multiple of 2020 and 2021 earnings, yields a valuation of \$49 and \$58, respectively.

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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 April 2016 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. Date	Relative Perf. vs. Russell 2000	
PAR Technology Group (NYSE: PAR)	30-Apr-16	\$6.39	\$19.97	212.5%	17.8%	194.7%	
Full House Resorts Inc. (Nasdaq: FLL)	30-May-16	\$1.60	\$2.09	30.6%	15.8%	14.9%	
Control4 Corporation (Nasdaq: CTRL)	30-Jun-16	\$7.99	\$17.19	115.1%	15.6%	99.5%	
KapStone Paper and Packaging Corporation (NYSE: KS)	31-Jul-16	\$14.28	\$35.00	145.1%	9.2%	135.9%	
Ampco-Pittsburgh Corp. (NYSE: AP)	31-Aug-16	\$11.12	\$3.03	-72.8%	7.4%	-80.2%	
Select Comfort Corporation (Nasdaq: SCSS)	30-Sep-16	\$22.51	\$32.50	44.4%	6.4%	38.0%	
Northwest Pipe Co. (NWPX)	31-Oct-16	\$13.16	\$22.53	71.2%	11.8%	59.4%	
Mitel Networks Corporation (Nasdaq: MITL)	30-Nov-16	\$7.25	\$11.15	53.8%	0.7%	53.1%	
Black Box Corporation (Nasdaq: BBOX)	31-Dec-16	\$15.25	\$1.09	-92.9%	-1.9%	-91.0%	
RadNet, Inc. (Nasdaq: RDNT)	31-Jan-17	\$5.80	\$10.38	79.0%	-2.2%	81.2%	
Guidance Software, Inc. (Nasdaq: GUID)	28-Feb-17	\$6.60	\$7.10	7.6%	-4.0%	11.5%	
Calgon Carbon Corporation (NYSE: CCC)	31-Mar-17	\$14.25	\$21.50	50.9%	-3.9%	54.8%	
LRAD Corporation (Nasdaq: LRAD)	30-Apr-17	\$1.51	\$2.42	60.3%	-4.9%	65.2%	
Trecora Resources (NYSE: TREC)	31-May-17	\$10.65	\$7.68	-27.9%	-2.8%	-25.1%	
EVINE Live Inc. (Nasdaq: EVLV)	30-Jun-17	\$1.00	\$0.42	-58.1%	-5.9%	-52.2%	
LSI Industries Inc. (Nasdaq: LYTS)	31-Jul-17	\$8.38	\$3.23	-61.5%	-6.5%	-54.9%	
Cooper Tire & Rubber Company (NYSE: CTB)	31-Aug-17	\$33.80	\$31.93	-5.5%	-5.2%	-0.3%	
RealNetworks, Inc. (Nasdaq: RNWK)	30-Sep-17	\$4.78	\$2.14	-55.2%	-10.7%	-44.6%	
NCI Building Systems, Inc. (NYSE: NCS)	30-Oct-17	\$15.65	\$7.24	-53.7%	-10.7%	-43.1%	
TransAct Technologies, Inc. (Nasdaq: TACT)	30-Nov-17	\$13.60	\$9.00	-33.8%	-13.8%	-20.1%	
Regis Corporation (NYSE: RGS)	30-Dec-17	\$15.36	\$16.68	8.6%	-13.3%	21.9%	
Team, Inc. (NYSE: TISI)	30-Jan-18	\$16.95	\$14.70	-13.3%	-15.9%	2.6%	
Andina Acquisition Corp II (Nasdaq:ANDA)	28-Feb-18	\$9.85	\$5.33	-45.8%	-11.9%	-33.9%	
GSE Systems, Inc. (NYSE:GVP)	31-Mar-18	\$3.25	\$2.15	-33.8%	-12.9%	-20.9%	
Telaria, Inc. (NYSE:TLRA)	30-Apr-18	\$4.13	\$2.78	-32.7%	-13.6%	-19.1%	
Avaya Holdings Corp. (NYSE:AVYA)	31-May-18	\$21.57	\$14.43	-33.1%	-18.5%	-14.6%	
Tenneco, Inc. (NYSE:TEN)	30-Jun-18	\$43.96	\$26.95	-38.7%	-18.9%	-19.8%	
Alithya Group Inc.	31-Jul-18	\$3.40	\$2.59	-23.8%	-20.3%	-3.5%	
Data I/O Corporation (Nasdaq: DAIO)	30-Aug-18	\$5.37	\$5.10	-5.0%	-23.1%	18.1%	
TPI Composites Inc. (Nasdaq: TPIC)	28-Sep-18	\$28.55	\$24.43	-14.4%	-21.5%	7.1%	
Shiloh Industries, Inc. (Nasdaq: SHLO)	31-Oct-18	\$8.59	\$5.84	-32.0%	-11.9%	-20.1%	
Richardson Electronics (Nasdaq: RELL)	30-Nov-18	\$7.18	\$8.45	17.7%	-13.1%	30.8%	
				<b>Average</b>	<b>5.1%</b>	<b>-5.7%</b>	<b>10.8%</b>

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## About Mossberg's Investor Digest

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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