

# Mossberg's Investor Digest

## From the Editor...

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With a history spanning more than 150 years, Philadelphia headquartered, **CSS Industries, Inc. (NYSE: CSS)**, designs, manufactures and sells a wide variety of products used in sewing and crochet crafts, gift wrapping, holiday and party decorations, scrap booking, and floral decorations. The company has the #1 or #2 position in most of its categories.

CSS is gaining competitive advantage by adding scale and scope through an active consolidation program, completing 6 acquisitions in the past 4 years. Since its markets are highly fragmented, the Company has been able to make deals at low multiples, in some case recording gains from bargain purchase accounting.

In our back of the envelope calculation, we use a 4.5x multiple of FY21 and FY22 EBITDA to derive an enterprise value of \$177 and \$207 million, respectively. We believe there may be upside to the valuation multiple and multiples may expand as the company proves its ability to reach 10% EBITDA margin in the coming years. Working backwards from enterprise value, we calculate a share price of \$20.27 per share in FY21, which represents more than 100% upside from current levels.

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Issue #127

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

**Avid Technology, Inc. (Nasdaq: AVID)** - Avid creates the digital audio and video technology used to make the most listened to, most watched and most loved media in the world - from the most prestigious and award-winning feature films, music recordings, television shows, live concert tours and news broadcasts, to music and movies made at home.

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**TechTarget, Inc. (Nasdaq: TTGT)** - Is the global leader in purchase intent-driven marketing and sales services that deliver business impact for enterprise technology companies. By creating abundant, high-quality editorial content across more than 140 highly targeted technology-specific websites, TechTarget attracts and nurtures communities of technology buyers researching their companies' information technology needs. By understanding these buyers' content consumption behaviors, TechTarget creates the purchase intent insights that fuel efficient and effective marketing and sales activities for clients around the world.

**Axcelis Technologies, Inc. (Nasdaq: ACLS)** - For thirty-five years, Axcelis Technologies has delivered vital equipment, services and process expertise to the semiconductor manufacturing industry, helping customers reach higher levels of productivity with each new technology generation. Chipmakers from around the globe rely on Axcelis tools and technology insights to produce the transistors that power all electronics - from desktops and servers to cell phones, cameras, personal music players and more. Their equipment portfolio comprises a powerful suite of manufacturing technologies for ion implantation - one of the most critical and enabling steps in the IC manufacturing process. Axcelis customers include all of the 20 largest semiconductor manufacturers in the world.

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Best Idea Profile:

CSS Industries, Inc. (NYSE: CSS)

## DESCRIPTION:

With a history spanning more than 150 years, Philadelphia headquartered, **CSS Industries, Inc. (NYSE: CSS)**, designs, manufactures and sells a wide variety of products used in sewing and crochet crafts, gift wrapping, holiday and party decorations, scrap booking, and floral decorations. The company has the #1 or #2 position in most of its categories.

The Company breaks revenue into three categories, each of which represents 30% to 40% of revenue.

- 1) **Seasonal** – Includes items for wrapping gifts including ribbon, bows, wrapping paper, bags, boxes, tags; as well as greeting cards and holiday items such as Easter egg dyes, and Valentine's Day classroom exchange cards.
- 2) **Gift** – Includes decorative packaging, stationery and party items for celebrating life events such as weddings, birthdays, anniversaries, graduations, birth of a child etc. Products include ribbons and bows, floral accessories, infant products, journals, gift card holders, greeting cards, memory books, scrapbooks, stationery, stickers and other items.
- 3) **Craft** – Includes items used in sewing and knitting such as sewing patterns, ribbons, trims, buttons, and kids crafts.

The majority of sales are generated in the United States and Canada. The Company has more than 30 offices in the U.S., India, China, U.K. and Australia, including more than three million square feet of manufacturing and distribution space in 19 locations. CSS has approximately 2,000 employees.

### CSS Industries, Inc. (NYSE: CSS) Investment Data (as of 1/31/19)

<b>Recent Price</b>	<b>\$8.91</b>
52-Week Range	\$8.40 - \$26.56
Fiscal Year End	March
Dividend	\$0.80
Yield	9.0%
Shares Outstanding*	8.8 M
Average Trading Volume (3 mos)	35,000
Market Capitalization	\$78M
Cash & Equivalents	\$15M
LT Debt	\$62MM
Enterprise Value (EV)	\$125M
TTM Revenue	\$389 M
EV/ Revenue	0.3x
Adj-EBITDA FY19 (guidance)	\$26MM to \$29MM
EV/ EBITDA	4.3x to 4.5x
Book Value/ Share	\$25.16

CSS is gaining competitive advantage by adding scale and scope through an active consolidation program, completing 6 acquisitions in the past 4 years. Since its markets are highly fragmented, the Company has been able to make deals at low multiples, in some case recording gains from bargain purchase accounting.

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## KEY INVESTMENT CONSIDERATIONS:

### Consolidating a fragmented space to gain category dominance

As shown in the chart below, the markets in which CSS participates are very large and highly fragmented. The Company is an active consolidator in this market, acquiring six companies in the past four years. Acquisitions are focused in areas that are tangential to existing business where there are opportunities for synergies and scale and scope can provide operating leverage to the business. At \$400 million, CSS is one of the largest players in these markets, which illustrates how fragmented the market is and the opportunity for consolidation.

	Seasonal	Gift	Crafts
Total Market Size (at retail*):	\$212.6B	\$46.2B	\$43.9B
CSS Market Segments:	\$159.2B	\$36.2B	\$21.5B
Competitive Dynamic:	Narrow market with leading brands by season for key product segments	Highly fragmented with few category specific brands and no leading national brands	Highly fragmented with category specific brands, but no leading national brands
Key Market Dynamics:	Mass drives the market and most purchases are still brick & mortar focused	Purchases shifting from specialty stores to mass accounts and on-line sales	Increasing direct import focus to address retailer margin pressure

*Source: Company Presentation*

The Company's most recent acquisition in November of 2017, Simplicity, is the Company's largest to date with a purchase price of \$69.6 million. Simplicity is a leading provider of home sewing patterns, decorative trims, knitting and crocheting tools. The purchase price represents a multiple of 0.8x revenue and 4.8x EBITDA (following synergies).

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## Efficiencies of Scale and Scope Provide competitive differentiation

### Primary competitive factors include:

- **Category knowledge:** CSS holds the #1 or #2 position in the categories it serves. In most categories, CSS has decades of experiences.
- **Timely delivery** – The Company has 11 distribution centers across the U.S. and holds significant inventory, so orders can be placed just in time.
- **Price** – CSS has several key brands that substantiate a level of price differentiation. Key brands include: Paper Magic®, Berwick®, Offray®, C.R. Gibson®, McCall's®, Butterick®, Kwik Sew®, Vogue Patterns®, Markings®, Stepping Stones®, Tapestry®, Seastone®, Dudley's®, Eureka®, Stickerfitti®, Favorite Findings®, La Mode®, Simplicity®, Wrights®, Boye®, Dimensions® and Perler®. The company's larger scale and international sourcing ability should give it cost advantage that enable the ability to sell at competitive prices while maintaining adequate profitability and returns.

Below are a list of representative customers by channel. The top 10 customers, which include mass market retailers (Walmart is 25% of rev.), warehouse clubs and national drug store chains, account for about 60% of sales. Sales are also made to specialty chains, dollar stores, office supply stores, independent card, gift and floral shops and retail teachers' stores.



Source: Company Presentation

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## Valuation

(In \$millions)	FY18	FY19	FY20	FY21	FY22
Revenue	362	405	425	447	469
Growth			5%	5%	5%
EBITDA		28	33	39	46
EBITDA Margin		6.8%	7.8%	8.8%	9.8%
FCF		28	33	39	46
Dividends		7	7	7	7
Acquisitions			20	20	20
Cash		25	25	25	25
Debt		42	35	23	4
EV/ EBITDA				4.5	4.5
Enterprise Value				177	207
Market Cap				178	227
Shares Outstanding	8.8	8.8	8.8	8.8	8.8
<b>Share Price</b>				<b>\$20.27</b>	<b>\$25.81</b>

Our back of the envelop model makes the following assumptions:

**Revenue:** Our FY19 (ending March) revenue reflects the mid-point of management's guidance of \$398 million to \$412 million. Our model assumes flat revenue performance organically and approximately \$20 million in acquired revenue (5% growth) per year through 2022.

**Adjusted-EBITDA income:** Our FY19 Adjusted-EBITDA number reflects the mid-point of management's guidance of \$26 million to \$29 million. From an EBITDA margin of approximately 7% in FY19, we assume one percentage point improvement each year through 2022, which reflects expectations for cost synergies from integrating past acquisitions, improving efficiencies and for the operating leverage that can be gained from layering on revenue from new acquisitions. Expanding EBITDA margin to 10% is consistent with recent comments from management... *"We really believe that following our strategic initiatives of acquisitions that we can synergize, growing our omni-channel focus, as well as continuing to drive down our SG&A... over time, we believe that if you go back 2, 3 years ago, that we should be able to achieve EBITDA percentage of sales over 10%, similar to the past."*

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

**Acquisitions:** We would not normally try to forecast acquisitions and certainly they will not happen in regular intervals as our model suggests. However, management has indicated that they are nearing the end of the integration process of their latest acquisitions and we could start to see activity pick up again. For simplicity sake, our model assumes \$20 million per year of acquisitions, which is approximately half of the free cash flow expected to be generated during the next three years. Our valuations assume 1x revenue valuations.

**Cash Flow:** We assume that FCF will approximate EBITDA. Our model assumes that after acquisitions, excess cash generation will be used to reduce debt levels.

**Valuation:** We use a 4.5x multiple of FY21 and FY22 EBITDA to derive an enterprise value of \$177 and \$207 million, respectively. We believe there may be upside to the valuation multiple and it may expand as the company proves its ability to reach 10% EBITDA margin in the coming years. Working backwards from enterprise value, we calculate a share price of \$20.27 per share in FY21, which represents more than 100% upside from 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 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	\$25.15	293.6%	31.5%	262.1%	
Full House Resorts Inc. (Nasdaq: FLL)	30-May-16	\$1.60	\$2.35	46.9%	29.2%	17.6%	
Control4 Corporation (Nasdaq: CTRL)	30-Jun-16	\$7.99	\$20.04	150.8%	29.1%	121.7%	
KapStone Paper and Packaging Corporation (NYSE: KS)	31-Jul-16	\$14.28	\$35.00	145.1%	21.9%	123.2%	
Ampco-Pittsburgh Corp. (NYSE: AP)	31-Aug-16	\$11.12	\$3.43	-69.2%	19.9%	-89.1%	
Select Comfort Corporation (Nasdaq: SCSS)	30-Sep-16	\$22.51	\$32.50	44.4%	18.8%	25.6%	
Northwest Pipe Co. (NWPX)	31-Oct-16	\$13.16	\$22.70	72.5%	24.8%	47.7%	
Mitel Networks Corporation (Nasdaq: MITL)	30-Nov-16	\$7.25	\$11.15	53.8%	12.4%	41.3%	
Black Box Corporation (Nasdaq: BBOX)	31-Dec-16	\$15.25	\$1.10	-92.8%	9.6%	-102.4%	
RadNet, Inc. (Nasdaq: RDNT)	31-Jan-17	\$5.80	\$13.60	134.5%	9.2%	125.3%	
Guidance Software, Inc. (Nasdaq: GUID)	28-Feb-17	\$6.60	\$7.10	7.6%	7.2%	0.3%	
Calgon Carbon Corporation (NYSE: CCC)	31-Mar-17	\$14.25	\$21.50	50.9%	7.3%	43.6%	
LRAD Corporation (Nasdaq: LRAD)	30-Apr-17	\$1.51	\$2.54	68.2%	6.2%	62.0%	
Trecora Resources (NYSE: TREC)	31-May-17	\$10.65	\$8.68	-18.5%	8.5%	-27.0%	
EVINE Live Inc. (Nasdaq: EVLV)	30-Jun-17	\$1.00	\$0.56	-44.0%	5.1%	-49.0%	
LSI Industries Inc. (Nasdaq: LYTS)	31-Jul-17	\$8.38	\$3.22	-61.6%	4.3%	-65.9%	
Cooper Tire & Rubber Company (NYSE: CTB)	31-Aug-17	\$33.80	\$34.54	2.2%	5.8%	-3.6%	
RealNetworks, Inc. (Nasdaq: RNWK)	30-Sep-17	\$4.78	\$2.68	-43.9%	-0.3%	-43.7%	
NCI Building Systems, Inc. (NYSE: NCS)	30-Oct-17	\$15.65	\$8.17	-47.8%	-0.3%	-47.5%	
TransAct Technologies, Inc. (Nasdaq: TACT)	30-Nov-17	\$13.60	\$10.48	-22.9%	-3.7%	-19.2%	
Regis Corporation (NYSE: RGS)	30-Dec-17	\$15.36	\$18.52	20.6%	-3.2%	23.7%	
Team, Inc. (NYSE: TISI)	30-Jan-18	\$16.95	\$14.65	-13.6%	-6.1%	-7.5%	
Andina Acquisition Corp II (Nasdaq: ANDA)	28-Feb-18	\$9.85	\$6.25	-36.5%	-1.7%	-34.9%	
GSE Systems, Inc. (NYSE: GVP)	31-Mar-18	\$3.25	\$2.94	-9.7%	-2.8%	-6.9%	
Telaria, Inc. (NYSE: TLRA)	30-Apr-18	\$4.13	\$3.21	-22.3%	-3.6%	-18.7%	
Avaya Holdings Corp. (NYSE: AVYA)	31-May-18	\$21.57	\$17.15	-20.5%	-9.0%	-11.5%	
Tenneco, Inc. (NYSE: TEN)	30-Jun-18	\$43.96	\$34.58	-21.3%	-9.5%	-11.8%	
Alithya Group Inc. (Nasdaq: ALYA)	31-Jul-18	\$3.40	\$2.78	-18.2%	-11.0%	-7.2%	
Data I/O Corporation (Nasdaq: DAIO)	30-Aug-18	\$5.37	\$5.88	9.5%	-14.2%	23.7%	
TPI Composites Inc. (Nasdaq: TPIC)	28-Sep-18	\$28.55	\$30.36	6.3%	-12.4%	18.7%	
Shiloh Industries, Inc. (Nasdaq: SHLO)	31-Oct-18	\$8.59	\$6.01	-30.0%	-1.6%	-28.4%	
Richardson Electronics (Nasdaq: RELL)	30-Nov-18	\$7.18	\$7.32	1.9%	-3.0%	5.0%	
Universal Electronics Inc. (Nasdaq: UEIC)	31-Dec-18	\$24.92	\$28.32	13.6%	10.3%	3.4%	
				<b>Average</b>	<b>16.7%</b>	<b>5.4%</b>	<b>11.2%</b>

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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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