

Mossberg's Investor Digest

From the Editor...

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

Headquartered in Washington D.C., **Liquidity Services, Inc. (Nasdaq: LQDT)**, runs online auction marketplaces that help more than 12,000 retailers, corporations and government agencies liquidate returned merchandise, surplus goods and end-of-life assets. Items from more than 500 different asset categories are auctioned on LQDT's auction sites to thrift shops, flea markets, EBay power users, and liquidators. For sellers, LQDT offers full- and self-service options. Self-service sellers undertake the work of photographing, cataloging, and building auctions. For full-service customers, LQDT can manage each step of the transaction and the reverse supply chain. Sellers make goods available at their facilities, or deliver them to one of LQDT's eight distribution centers, or storage lot.

To derive our 3-year valuation, we use a EV/EBITDA multiple of 11x our forecasted EBITDA, which is a discount compared to peers who are trading with multiples in the mid- to high-teens. Working backwards from enterprise value, our model derives a valuation of \$11.82 per share in three years, 56% above the current valuation.

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Issue #134

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

Enviva Partners, LP (NYSE: EVA) is a publicly traded master limited partnership that aggregates a natural resource, wood fiber, and processes it into a transportable form, wood pellets. The Partnership sells a significant majority of its wood pellets through long-term, take-or-pay agreements with creditworthy customers in the United Kingdom and Europe. The Partnership owns and operates six plants with a combined production capacity of nearly three million metric tons of wood pellets per year in Virginia, North Carolina, Mississippi, and Florida.

Gladstone Land Corporation (NASDAQ: LAND) Gladstone Land owns farmland in Arizona, California, Colorado, Florida, Michigan, Nebraska, North Carolina, Oregon and Washington. As of June 30, 2018 their portfolio has an appraised value of approximately \$537.4 million. Gladstone Land acquires farmland that it rents to corporate and independent farmers on a triple-net lease basis, an arrangement under which the farmer maintains the property while paying rent to Gladstone Land.

comScore, Inc. (NASDAQ: SCOR) is a trusted partner for planning, transacting and evaluating media across platforms. With transformative data science and vast audience insights across digital, linear TV, over-the-top (OTT) and theatrical viewership, they are a powerful third-party source for reliable measurement of cross-platform audiences.

Tuesday Morning Corporation (TUES) One of the original off-price retailers, Tuesday Morning is a leading destination for unique home and lifestyle goods. They specialize in name-brand, better/best products for the home. They are known for irresistible finds at an incredible value and search the world for amazing deals to bring to our customers.

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Best Idea Profile:

Liquidity Services, Inc. (Nasdaq: LQDT)

DESCRIPTION:

Headquartered in Washington D.C., **Liquidity Services, Inc. (Nasdaq: LQDT)**, runs online auction marketplaces that help more than 12,000 retailers, corporations and government agencies liquidate returned merchandise, surplus goods and end-of-life assets. Items from more than 500 different asset categories are auctioned on LQDT's auction sites to thrift shops, flea markets, EBay power users, and liquidators. For sellers, LQDT offers full- and self-service options. Self-service sellers undertake the work of photographing, cataloging, and building auctions. For full-service customers, LQDT can manage each step of the transaction and the reverse supply chain. Sellers make goods available at their facilities, or deliver them to one of LQDT's eight distribution centers, or storage lot.

Revenue is split into four reportable segments...

1) Retail Supply Chain Group (RSCG) (56% of rev) - Marketplaces used by retailers to sell surplus, returned, and salvage consumer goods. LQDT offers a full suite of services including returns management, refurbishment, listing, pricing, payment-processing, customer service and reporting. Marketplace websites include Liquidation.com, and Secondpity.com.

2) Capital Asset Group (CAG) (26% of rev) Full-service marketplaces used by federal government and commercial customers to sell surplus, salvage, and scrap assets. LQDT offers full-service solutions including listing, pricing, payment-processing, customer service and reporting. Marketplace websites include networkintl.com and go-dove.com.

3) GovDeals (15% of rev) – Self-service marketplaces used by state and local government agencies, as well as commercial businesses, to list and sell their surplus and salvage assets. Marketplace websites GovDeals.com and AuctionDeals.com.

Liquidity Services, Inc. (Nasdaq: LQDT) Investment Data (as of 8/30/19)

Recent Price	\$7.57
52-Week Range	\$9.16 - \$5.17
Fiscal Year End	September
Dividend	N/A
Yield	N/A
Shares Outstanding	33.5 M
Average Trading Volume (3 mos)	85,000
Market Capitalization	\$245 M
Cash	\$66 M
LT Debt	N/A
Enterprise Value (EV)	\$179 M
FY19 Revenue (Estimate)	\$220 M
EV/ Revenue	0.8x
FY19 EBITDA (Estimate)	-\$1.2 M
EV/EBITDA	nmf
Book Value Per Share	\$3.62

4) Machinio (2% of rev) – Acquired in July of 2018, Machinio.com aggregates more than 1 million global used heavy equipment listings. There is \$20 billion of used equipment for sale right now on the Machinio website. The revenue model is subscription based with more than 3,000 sellers paying an annual subscription to list on the site. This is the "Craig's list for heavy equipment" with a subscription for sellers.

The Company has 3.5 million registered buyers and completes more than 500,000 transactions annually. LQDT's 700 employees are located across North America, Europe, and Asia.

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KEY INVESTMENT CONSIDERATIONS:

Attractive business model with scale and scope

Critical mass and infrastructure create strong value proposition, ability to take market share and create barriers to entry – While there are a few large auction houses, the market is still very fragmented with about 10k traditional auctioneers, which are mostly small businesses with fixed site locations. In the auction business, the larger the efficiencies of scale and scope the more valuable the auction is to sellers and buyers. LQDT offers sellers access to a global buyer base of more than 3.5 million registered users, along with technology to transact quickly and audit/ reporting capabilities. During the past three fiscal years, LQDT has conducted 1,585,000 online transactions generating approximately \$1.9 billion in gross merchandise volume. In addition, the Company has built infrastructure to support a \$1B annual business. It's nine warehouse/storage facilities with nearly 1.5 million sqft. of space, systems, and knowledge base are significant differentiators and create barriers for smaller players, or any new entrants to duplicate.

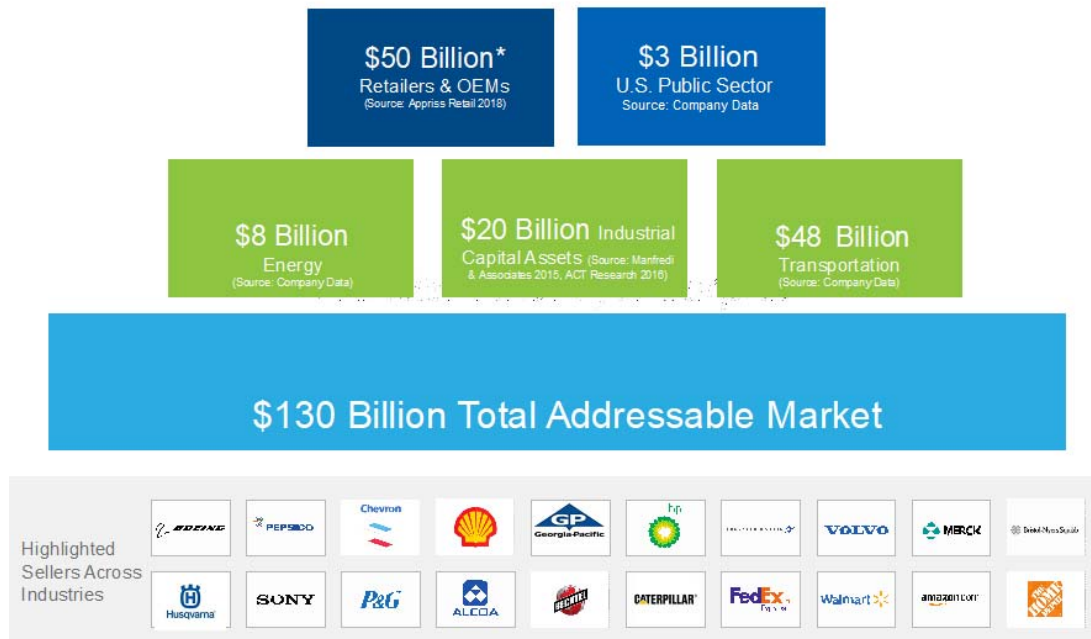
LQDT has an attractive "Asset Light" business model – LQDT's unique business model can generate "negative working capital". This happens because auction winners pay faster than LQDT has to pay for the entire consideration of the product. For example, as of June 30, the company has \$14.6 million of receivables and inventory, versus \$38.1 million of accounts payable and payables to sellers. LQDT has two primary pricing models.

- **Consignment (30% of revenue)** – Under the consignment model, there is no cash outlay for the merchandise sold at auction. Payment is received by LQDT and is then funds are remitted to the seller after a few days. LQDT recognizes revenue based on the commission earned on the sale, not the actual sale amount. While commission revenue from consignment sales represents about 30% of total revenue, the total market value of consignment sales represents approximately 80% of gross merchandise value.
- **Purchase (65% of revenue)** – LQDT agrees to a purchase price per item. LQDT pays either a fixed amount, or a portion of the proceeds from the completed sale based on the sale price, and in some cases, deducting a required return and fees. LQDT receives terms from the seller that can be as much as 90 days.

As a result of this model, LQDT can finance growth without issuing new shares and diluting shareholders. Excess cash can be used to repurchase stock or make acquisitions that further expand the scope and scale.

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Large Addressable Market



Source: Company Presentation

Large Market Opportunity – The Company has only begun to penetrate the online surplus management market, which is estimated to be as large as \$130 billion annually.

Multiple Secular Growth Drivers

- **E-Commerce popularity drives greater demand for returns management** – According to eMarketer (2018), e-commerce return rates comprise 20% of sales, and can grow to 30% of all products ordered online during the holidays. This is 2-3x the rate of normal brick and mortar stores that range from 8%-10%. Brightpearl (2018) found that 51% of all retailers claim their margins are being squeezed by returns, yet 69% are not deploying any technology solutions to help process them. Statista estimates return deliveries will cost U.S. retailers \$550 billion by 2020, 75.2% more than four years prior. Retailers don't want to spend money on technology and infrastructure to handle returns... it just makes more sense to outsource it to companies like LQDT.
- **Technology innovation drives faster product obsolescence**
- **Sustainability** – Environmental sustainability is of growing importance to investors, employees customers and other stakeholders. According to US SIF Foundation, sustainable, responsible and impact investing (SRI) now account for \$12 trillion in assets, representing 25% of total assets under professional management in the United States. The National Marketing Institute found that 58 percent of 53,000 customers surveyed consider a company's environmental impact before buying. As such, sustainability has become a key goal for retailers, commercial and government sellers. LQDT allows sellers to maximize the value form end of life assets and provides tracking data to report on sustainability for stakeholders, as well as for regulatory compliance reasons.

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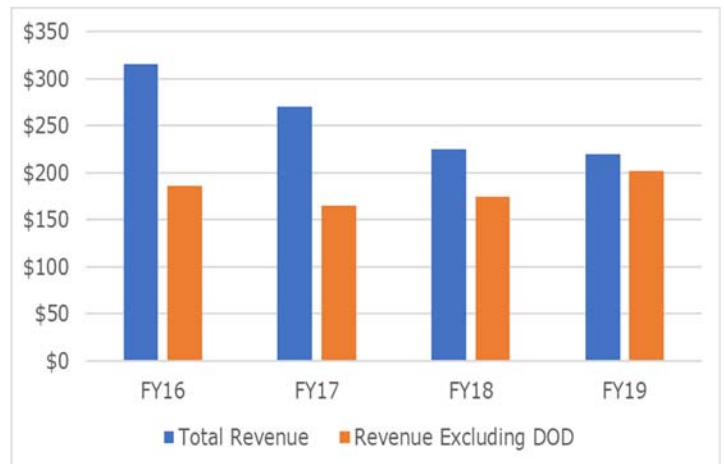
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Early Stages of Turn Around

	FY16	FY17	FY18	FY19
Revenue	316	270	225	220
Annual Revenue Growth		-15%	-17%	-2%
DOD Revenue	130	104	51	18
Revenue Excluding DOD	186	166	174	202
Annual Revenue Growth		-11%	5%	16%

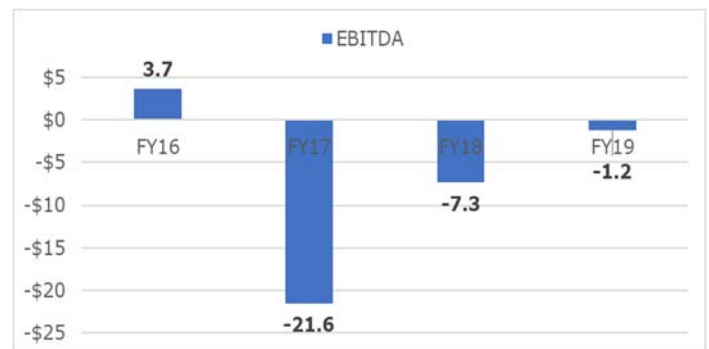
Replacing the DOD business – In 2015 and 2018, respectively, the Company began exiting contracts to sell surplus and scrap for the Department of Defense. After September 2019, LQDT will have zero revenue related to the DOD. This was a significant business for the Company, representing approximately 41% of FY16 revenue. However, the bidding process was highly competitive, and management made a disciplined decision not to bid for renewal. In some cases, the contract winner bid as much as twice as much as the most recent contracts. Management was not willing to compete for this business with the limited potential return. In addition, terms of the new contract required substantial incremental investments in storage and warehouse facilities, along with incremental logistics costs, all of which would have likely resulted in negative returns.



Underlying growth since existing the DOD business – Excluding the DOD-related revenue, the Company began to grow again in FY18, and the pace has accelerated in FY19. During the trailing 4 quarters, the Company's three main segments have grown at the following annual rates..

- o GovDeals Segment – 9.5%
- o Retail Supply Chain Group - 17%
- o Capital Asset Group – 16%

Mix shift to consignment revenue - 100% of DOD-related revenue was booked as GAAP revenue. With less DOD revenue, the revenue mix has shifted to more to consignment, in which the company only books revenue on consignment fee. While this makes revenue comparisons more difficult, greater consignment revenue improves the margin profile and reduces working capital demands.



Improvements in Profitability – The Company has replaced DOD-related revenue with more diverse revenue streams that are more profitable. This has been partially responsible for the improvement in EBITDA. At the right scale, we believe the business is capable of producing greater than 10% EBITDA margins and expect to continue to see significant improvements over the next several years.

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Early Stages of Turn Around (continued)

New Senior management and structural changes – In April of this year, the company reorganized simplifying its leadership structure by creating a new chief marketing officer role to lead service delivery for all of the company's market places. The new CMO was promoted within and succeeded separate Presidents of the CAG/RSCG and the GovDeals business unites.

- **Created Chief Marketing Officer** – In April, LQDT announced John Daunt had been promoted to CMO.
- **New Chief Technology Officer** – Steven Weiskircher joined as CTO in August. Previously he was VP, Omnichannel, Marketing, and Digital Technology Delivery for GameStop (NYSE:GME) and CIO of ThinkGeek.
- **New VP of marketing** – A year ago, the company brought on a new head of marketing with former experience at Hellen of Troy and QVC.

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Valuation

	FY16	FY17	FY18	FY19	FY20	FY21	FY22
Revenue	316	270	225	220			
Revenue Excluding DOD	186	166	174	202	227	254	284
Annual Revenue Growth			5%	16%	12%	12%	12%
EBITDA	3.7	-21.6	-7.3	-1.2	7.9	17.8	28.4
EBITDA Margin	1%	-8%	-3%	-1%	4%	7%	10%
EV/ EBITDA						11	11
Enterprise Value							313
Cash					60	69	83
Market Cap							396
Shares Outstanding							33.5
Price Per Share							\$11.82

Valuation

The table above shows our back of the envelop calculation for the next three years. We make the following assumptions in our calculation:

- **Revenue:** We assume revenue for FY19, ending in September, of \$220 million, which is within the range of guidance given by management. Thereafter we assume non-DOD related revenue growth of 12% per year. Given the Company's recent growth trajectory and successful growth initiatives, we believe this rate is conservative.
- **EBITDA & EBITDA Margin:** We assume EBITDA loss of \$(1.2) million for FY19, which is in line with management's guidance. We expect EBITDA margin will improve due to fixed cost leverage, management initiatives to improve efficiencies, as well as a mix shift that will include a greater portion of higher margin lines of business. We assume a steady improvement to 10% EBITDA margin over the next three years. Historically, the company has produced EBITDA margins in excess of this level.
- **Share Count –** We assume no growth in the Company's share count.
- **Cash Generation –** We assume 50% of EBITDA will translate into Free Cash Flow.

To derive our 3-year valuation, we use a multiple of EV/EBITDA of 11x, which is a discount compared to peers who are trading with multiples in the mid- to high-teens. Working backwards from enterprise value, our model derives a valuation of \$11.82 per share in three years, 56% above the current valuation.

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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	\$23.13	262.0%	32.2%	229.8%	
Full House Resorts Inc. (Nasdaq: FLL)	30-May-16	\$1.60	\$2.02	26.3%	29.9%	-3.7%	
Control4 Corporation (Nasdaq: CTRL)	30-Jun-16	\$7.99	\$23.91	199.2%	29.8%	169.5%	
KapStone Paper and Packaging Corporation (NYSE: KS)	31-Jul-16	\$14.28	\$35.00	145.1%	22.5%	122.6%	
Ampco-Pittsburgh Corp. (NYSE: AP)	31-Aug-16	\$11.12	\$3.59	-67.7%	20.6%	-88.3%	
Select Comfort Corporation (Nasdaq: SCSS)	30-Sep-16	\$22.51	\$32.50	44.4%	19.4%	25.0%	
Northwest Pipe Co. (NWPX)	31-Oct-16	\$13.16	\$23.00	74.8%	25.5%	49.3%	
Mitel Networks Corporation (Nasdaq: MITL)	30-Nov-16	\$7.25	\$11.15	53.8%	13.0%	40.7%	
Black Box Corporation (Nasdaq: BBOX)	31-Dec-16	\$15.25	\$1.10	-92.8%	10.1%	-102.9%	
RadNet, Inc. (Nasdaq: RDNT)	31-Jan-17	\$5.80	\$13.91	139.8%	9.8%	130.1%	
Guidance Software, Inc. (Nasdaq: GUID)	28-Feb-17	\$6.60	\$7.10	7.6%	7.8%	-0.2%	
Calgon Carbon Corporation (NYSE: CCC)	31-Mar-17	\$14.25	\$21.50	50.9%	7.9%	43.0%	
LRAD Corporation (Nasdaq: LRAD)	30-Apr-17	\$1.51	\$3.68	143.7%	6.7%	137.0%	
Trecora Resources (NYSE: TREC)	31-May-17	\$10.65	\$9.05	-15.0%	9.1%	-24.1%	
EVINE Live Inc. (Nasdaq: EVLV)	30-Jun-17	\$1.00	\$0.51	-49.2%	5.6%	-54.9%	
LSI Industries Inc. (Nasdaq: LYTS)	31-Jul-17	\$8.38	\$4.37	-47.9%	4.9%	-52.7%	
Cooper Tire & Rubber Company (NYSE: CTB)	31-Aug-17	\$33.80	\$23.49	-30.5%	6.4%	-36.9%	
RealNetworks, Inc. (Nasdaq: RNWK)	30-Sep-17	\$4.78	\$1.61	-66.3%	0.3%	-66.6%	
NCI Building Systems, Inc. (NYSE: NCS)	30-Oct-17	\$15.65	\$4.69	-70.0%	0.3%	-70.3%	
TransAct Technologies, Inc. (Nasdaq: TACT)	30-Nov-17	\$13.60	\$11.83	-13.0%	-3.2%	-9.8%	
Regis Corporation (NYSE: RGS)	30-Dec-17	\$15.36	\$16.17	5.3%	-2.6%	7.9%	
Team, Inc. (NYSE: TISI)	30-Jan-18	\$16.95	\$16.48	-2.8%	-5.6%	2.8%	
Andina Acquisition Corp II (Nasdaq:ANDA)	28-Feb-18	\$9.85	\$4.75	-51.8%	-1.2%	-50.6%	
GSE Systems, Inc. (NYSE:GVP)	31-Mar-18	\$3.25	\$1.79	-44.9%	-2.3%	-42.7%	
Telaria, Inc. (NYSE:TLRA)	30-Apr-18	\$4.13	\$9.98	141.6%	-3.1%	144.7%	
Avaya Holdings Corp. (NYSE:AVYA)	31-May-18	\$21.57	\$14.12	-34.5%	-8.5%	-26.0%	
Tenneco, Inc. (NYSE:TEN)	30-Jun-18	\$43.96	\$8.72	-80.2%	-9.0%	-71.1%	
Alithya Group Inc. (Nasdaq: ALYA)	31-Jul-18	\$3.40	\$2.78	-18.2%	-10.5%	-7.7%	
Data I/O Corporation (Nasdaq: DAIO)	30-Aug-18	\$5.37	\$3.69	-31.3%	-13.7%	-17.6%	
TPI Composites Inc. (Nasdaq: TPIC)	28-Sep-18	\$28.55	\$17.64	-38.2%	-11.9%	-26.3%	
Shiloh Industries, Inc. (Nasdaq: SHLO)	31-Oct-18	\$8.59	\$4.18	-51.3%	-1.1%	-50.2%	
Richardson Electronics (Nasdaq: RELL)	30-Nov-18	\$7.18	\$5.84	-18.7%	-2.5%	-16.2%	
Universal Electronics Inc. (Nasdaq: UEIC)	31-Dec-18	\$24.92	\$45.15	81.2%	10.8%	70.3%	
CSS Industries, Inc. (NYSE: CSS)	31-Jan-19	\$8.91	\$3.86	-56.7%	-0.3%	-56.4%	
Comtech Telecommunications Corp. (Nasdaq:CMTL)	28-Feb-19	\$26.25	\$26.75	1.9%	-5.1%	7.0%	
Landec Corporation (Nasdaq:LNDL)	31-Mar-19	\$12.28	\$10.99	-10.5%	-2.9%	-7.6%	
Dawson Geophysical (Nasdaq: DWSN)	30-Apr-19	\$2.46	\$2.11	-14.2%	-6.1%	-8.2%	
Fortress Transportation and Infrastructure Investors (Nasdaq:FTAI)	31-May-19	\$15.61	\$14.91	-4.5%	2.0%	-6.5%	
Oil-Dri Corporation of America (NYSE:ODC)	30-Jun-19	\$34.04	\$30.76	-9.6%	-4.6%	-5.1%	
Emmis Communications (Nasdaq:EMMS)	29-Jul-19	\$5.53	\$4.95	-10.5%	-4.7%	-5.8%	
				Average	11.2%	4.4%	6.8%

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