Research Report – Update

Investors should consider this report as only a single factor in making their investment decision.

Orchids Paper Products Company

Rating: Speculative Buy

John Nobile
December 22, 2015

TIS $30.47 — (NYSE MKT)

	2013A	2014A	2015E	2016E
Revenues (millions)	$116.4	$142.7	$171.5	$198.8
Earnings per share	$1.67	$1.11	$1.39	$1.82

52-Week range	$32.00 – $21.42	Fiscal year ends:	December
Shares outstanding as/of 10/31/15	10.3 million	Revenue per share (TTM)	$17.71
Approximate float	9.4 million	Price/Sales (TTM)	1.7X
Market capitalization	$314 million	Price/Sales (FY2016)E	1.6X
Tangible book value/share	$10.67	Price/Earnings (TTM)	23.4X
Price/tangible book value	2.9X	Price/Earnings (FY2016)E	16.7X
Annual dividend	$1.40	Dividend Yield	4.6%

Orchids Paper Products, headquartered in Pryor, Oklahoma, manufactures bulk tissue paper, known as parent rolls, and converts parent rolls into a full line of tissue products, including paper towels, bathroom tissue and paper napkins for the private label segment of the consumer, or "at home," market. The company has focused its product design and manufacturing on the discount retail market, primarily the dollar store retailers. (www.orchidspaper.com)

Key investment considerations:

Reiterating Speculative Buy rating. Raising 12-month price target to $34.50 (from $29.00) due to increased earnings expectations.

The company's five-year growth potential is substantial due to geographic expansion: the 2014 acquisition of Fabrica's business in California, Nevada, Arizona, New Mexico and Utah, upgrading machines at its Oklahoma facility in 2015, and a new integrated facility in South Carolina.

With a full year of shipments from Fabrica and recent new business (shipments started in August 2015) bringing Orchids' Oklahoma converted run rate to 67,000 tons annually, we project a 24% increase in converted products being shipped in 2015 to approximately 84,200 tons.

In 2016, total converted tonnage (from Oklahoma, Fabrica and South Carolina) is projected to increase 17% to 98,400 tons, higher than our previous projection of 92,800 tons due primarily to a full year of shipments from new orders in Oklahoma which started in August 2015 and shipments from the South Carolina facility which are expected to start in 1H16.

We project 2015 revenue of $171.5 million and EPS of $1.39. The change in our projections (previously $173 million revenue and $1.35 EPS) primarily reflects 3Q15 results. We project 2016 revenue of $198.8 million and EPS of $1.82. The change in our projections (previously $192.4 million revenue and EPS of $1.75) stems primarily from increased shipments of converted products.

Orchids reported (10Q released 11/9/15) 3Q15 revenue of $46.8 million and EPS of $0.45. We projected 3Q15 revenue of $47.5 million and EPS of $0.41. In the year earlier quarter, Orchids generated revenue of $44.4 million and EPS of $0.44.

Please view our disclosures on pages 14 - 16.

Recommendation and Valuation

Reiterating Speculative Buy rating and raising 12-month price target to $34.50 (from $29.00) due to increased earnings expectations.

Shares of Orchids currently trade at a TTM EPS multiple of 23X, up from 19X three months earlier, due arguably to strong earnings growth. Based on our projected EPS growth, the market should value the stock at 19X estimated 2016 EPS. Applying a multiple of 19X to our 2016 EPS estimate gives us a price target of approximately $34.50 per share.

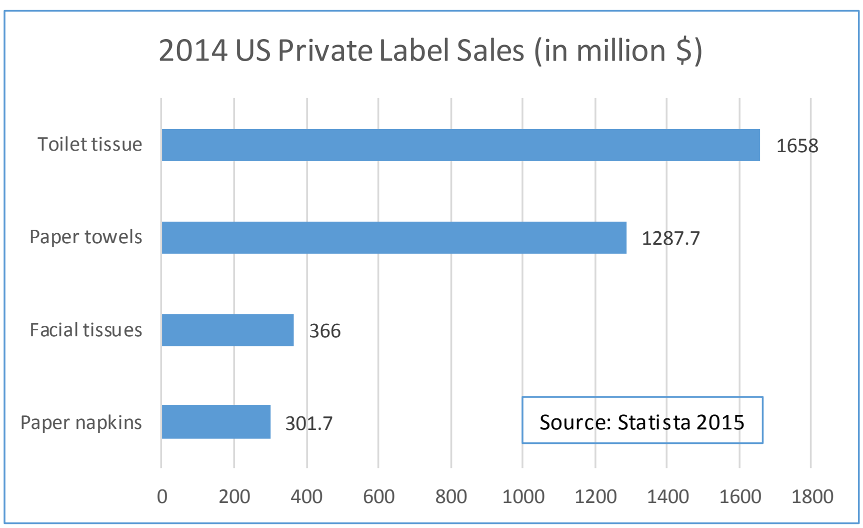
Business

Orchids Paper Products, headquartered in Pryor, Oklahoma, manufactures bulk tissue paper, converting it into a full line of tissue products, including paper towels, bathroom tissue and paper napkins for the private label segment of the consumer or "at home" market. The company targets the discount retail market, primarily dollar store retailers, due to their consistent order patterns, limited number of stock keeping units (SKUs) and the growth in this channel of the retail market. Orchids has customers throughout the US, but its sales efforts are currently focused within a 500-mile radius of its northeast Oklahoma facility, a cost-effective shipping area.

The company's products are sold primarily under its customers' private labels and, to a lesser extent, brand names such as Colortex® and Velvet®. Orchids does not have supply contracts with any of its customers. Orchids' products are daily consumable items so order streams are fairly constant with no significant seasonal fluctuations. Changes in the national economy do not materially affect the market for Orchids' products. However, local conditions might.

Private Label Market and Outlook

In October 2015, the Private Label Manufacturers Association (PLMA) said that private label brands had accounted for nearly $3 billion in incremental US sales in 2014, an increase of 2.5% over 2013 and more than twice the gain recorded by national brands. The PLMA said that the growth in private label sales was driven by the rising quality and value of private label products.



In October 2015, the statistics website Statista.com reported that US sales of private label paper products were approximately $3.6 billion in 2014. Toilet tissue accounted for the greatest percentage of sales at 46%, followed by paper towels at 36%, facial tissue at 10%, and paper napkins at 8% (see chart at right).

In September 2015, international consulting and engineering company Pöyry said that private label tissue market penetration in North America was currently 27%, up from 18% a decade ago. Pöyry cited increased availability of high quality private label tissue products and recession awakened frugality as some of the key factors driving the success of private label tissue products.

In a June 2015 sanitary paper product manufacturing industry report, IBISWorld said that large discount retailers such as Walmart (accounted for 9% of Orchids' converted product sales in 2014) and Target were increasingly focusing on private-label goods that can provide higher margins. IBISWorld expects this trend to continue over the next five years. However, competition from lower-priced imports is expected to attenuate US growth resulting in moderate industry growth averaging 1.9% annually in the six years to 2020.

Economic Outlook

In October 2015, the International Monetary Fund (IMF) raised its economic growth estimate for the US to 2.6% in 2015 from 2.5% previously (July 2015), but lowered it to 2.8% in 2016 from 3%. The IMF said that US economic growth in the first half of 2015 was weaker than expected, despite a strong second quarter. This reflected setbacks to activity in the first quarter, notably harsh winter weather and port closures, as well as much lower capital spending in the oil sector. The IMF expects the recovery to continue in the US, supported in part by lower energy prices and an improving housing market.

The second estimate of US GDP growth (released on November 24, 2015) showed the US economy grew at an annual rate of 2.1% in 3Q15, up from 1.5% growth in the previous estimate in October 2015. The 3Q15 US GDP growth estimate primarily reflects a rise in consumer spending. Spending on nondurable and durable goods also rose. Partly offsetting these contributions to GDP growth was falling private inventory investment, mainly in manufacturing.

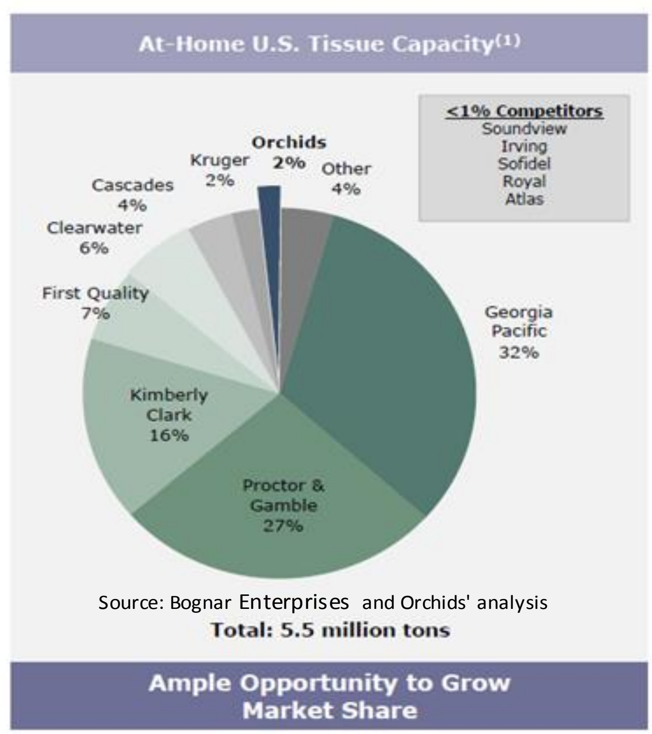
In October 2015, the Federal Reserve Bank of the Tenth Federal Reserve District, which includes the Oklahoma area, released its survey of manufacturing activity. The survey reported that the region's manufacturing activity steadied somewhat in October, 2015, and was expected to remain largely unchanged heading forward. Modest increases in new orders and production nearly offset declines in employment, supplier delivery time, and inventory indexes.

Market and Competition

In June 2015, IBISWorld estimated the 2015 US sanitary paper product market at $13.3 billion with the tissue segment (paper towels, bathroom tissue, and paper napkins) at $2.8 billion. The overall industry is projected to grow at an average annual growth rate of 1.9% to $14.9 billion by 2021.

Dollar and variety stores, Orchids' primary target markets, realized sales of $67 billion in 2014. In September 2015, IBISWorld projected dollar and variety stores' average revenue growth to decline 1.3% annually to $61.5 billion by 2021 as competition from rivals such as Walmart, Target and Costco increases.

Competition in the value-end of the market is significantly affected by proximity, as freight costs represent a material portion of delivered product costs. Over the past five years, competitors (Clearwater Paper, Georgia-Pacific, Cascades, and Pacific Paper) have moved into Orchids' market areas, arguably drawn by attractive margins. The increased competition has reduced Orchids' competitive cost advantage and reduced gross margins from 29.2% in 2009 to 17.0% in 2010, and



Source: Bognar Enterprises and Orchids' analysis

16.3% in 2011. Orchids was able to reverse this downward trend as growing sales of higher margin converted products increased Orchids' gross margins to 22.4% in 2012, 24% in 2013. However, in 2014, gross margins fell to 18.7% due primarily to lower overhead coverage as the company shut down two of its older paper machines in September 2014 and started the construction and installation of a new paper machine. This reduced the absorption of fixed costs at Orchids' Oklahoma plant and required the company to purchase parent rolls in the open market.

Clearwater Paper and Cascades are the only publicly held direct competitors. Revenue and gross margins for Orchids and its competitors are shown at right. These competitors' lower gross margins versus Orchids' could drive them to expand in Orchids' market, increasing pressure on Orchids' prices and margins.

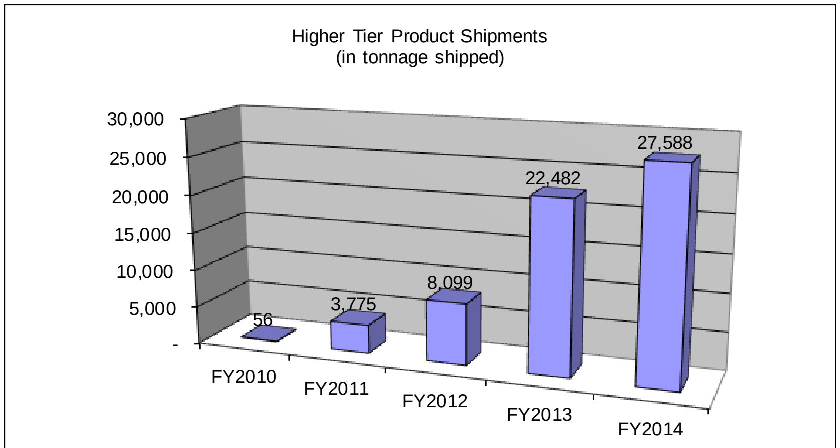
	Clearwater Paper	Cascades	Orchids Paper
TTM Revenue (9/15)	$1.8B	$2.8B	$167.9M
TTM Gross Margin	14.4%	15.1%	15.9%

Strategy

Orchids aims to increase sales of its converted products, which yield higher margins. In June 2014, Orchids acquired Fabrica's US business, including certain manufacturing assets, and access to 19,800 metric tons of capacity each year to support the value, premium and ultra-premium requirements of the US market. The supply agreement with Fabrica provides access to an additional 7,700 tons in the first two years of the agreement for a total of up to 27,500 tons. The option for the additional tonnage expires at the end of 1H16. In 2Q15, Orchids began construction on an integrated tissue paper facility in Barnwell, SC with paper making capacity of between 35,000 and 40,000 tons per year and converting capacity of between 30,000 and 32,000 tons per year. The first converting line is expected to be operational by the end of 1Q16 and the second converting line is expected to be operational by the end of 2Q16. The paper machine is expected to be operational by the beginning of 2017.

Orchids plans to expand into retail channels such as grocery stores, mass merchandise and other discount retail sectors. Initial efforts to expand into these other channels previously had limited success due to capacity constraints and the inability to produce higher grade products. However, these shortcomings have been overcome by the additional converting line and new product initiatives (higher grade products).

The graph at right shows how shipments of Orchids' higher grade converted products have grown over the past five years. Growth was driven by sales of new higher quality products (with better paper, enhanced graphics, and improved embossing).



Source: Company filings

3Q and Nine-Months 2015 Financial Results

<u>*3Q15*</u> - Sales of $46.8 million were up 5% from the comparable period in 2014. Net income was $4.7 million or $0.45 per share versus net income of $3.8 million or $0.44 per share. We projected 3Q15 sales of $47.8 million and net income of $4.2 million or $0.41 per share.

Converted product (paper towels, bathroom tissue, and paper napkins) sales increased 1% to $43.7 million while parent roll (bulk tissue paper) sales increased 148% to $3.2 million. The increase in converted product sales was due to a 7% increase in tonnage shipped to 23,001, partly offset by a 5% decrease in net selling prices to $1,899/ton. The decrease in net selling price was primarily due to product mix (away-from-home products acquired in the Fabrica transaction have lower selling prices than Orchids' core at-home products). The increase in parent roll sales was due to a 112% increase in tonnage shipped (generated by the new paper machine in Oklahoma) and a 17% increase in selling prices to $998/ton.

Gross margins increased to 21% from 19.8% primarily due to the higher average selling prices of parent rolls.

Selling, general and administrative (SG&A) expenses decreased to $2.4 million from $2.5 million due primarily to a decrease in stock option expense offset in part by increased professional fees. The company recognized $376,000 of amortization expense related to the intangible assets acquired in the Fabrica transaction. Operating income increased to $7 million or 15% of sales from $5.9 million or 13.3% of sales.

Nine-months 2015 - Sales of $126.5 million were up 25% from the comparable period in 2014. Net income was $9.9 million or $1.02 per share versus net income of $7 million or $0.83 per share.

Converted product (paper towels, bathroom tissue, and paper napkins) sales increased 25% to $120.9 million while parent roll (bulk tissue paper) sales increased 30% to $5.7 million. The increase in converted product sales was due to a 32% increase in tonnage shipped to 62,172 (due primarily to a full year of shipments under the supply agreement with Fabrica), partly offset by a 6% decrease in net selling prices to $1,944/ton. The decrease in net selling price was primarily due to product mix (away-from-home products acquired in the Fabrica transaction have lower selling prices than Orchids' core at-home products). The increase in parent roll sales was due to a 15% increase in tonnage shipped (generated by the new paper machine in Oklahoma) and a 13% increase in selling prices to $997/ton.

	9mos15	9mos14	% change
	(in thousands $)		
Net sales	126,542	101,384	24.8%
Cost of sales	104,192	81,092	28.5%
Gross profit	22,350	20,292	10.1%
Intangibles amortization	1,130	430	NMF
SG&A expenses	7,174	9,127	(21.4%)
Operating income (loss)	14,046	10,735	30.8%
Interest expense	289	215	34.4%
Other (income) expense	(507)	141	NMF
Income (loss) before taxes	14,264	10,379	37.4%
Income tax expense (benefit)	4,408	3,360	31.2%
Net income (loss)	9,856	7,019	40.4%
Diluted EPS	1.02	0.83	22.5%
Diluted Shares Outstanding	9,673	8,442	
Margin Analysis			
Gross margin	17.7%	20.0%	
SG&A expenses	5.7%	9.0%	
Operating margin	11.1%	10.6%	
Net margin	7.8%	6.9%	

Source: Company filings

Gross margins decreased to 17.7% from 20% primarily due to lower average selling prices, higher raw material costs, and the company shutting down two of its older paper machines in September 2014 which reduced the absorption of fixed costs at Orchids' Oklahoma plant and required the company to purchase parent rolls in the open market in 1Q15.

Selling, general and administrative (SG&A) expenses decreased to $7.2 million from $9.1 million due primarily to $1.6 million of acquisition costs related to the Fabrica transaction in 2014 and a decrease in non-cash stock option expense. The company recognized $1.1 million of amortization expense related to the intangible assets acquired in the Fabrica transaction. Operating income increased to $14 million or 11% of sales from $10.7 million or 10.6% of sales.

Liquidity - Based on our forecasts, Orchids should need to raise approximately $40 million in additional debt over the next two years in order to meet its financial obligations through 2016. We project increased interest payments through 2016. As of September 30, 2015, Orchids had cash of $8.6 million, a current ratio of 2.1X versus 0.9X for the paper products industry, and a debt/equity ratio of 0.3X versus 0.4X for the industry. Orchids' total debt has more than tripled in a little more than a year to over $46 million in 2Q15 from approximately $15 million at the end of 2013. The increase in debt was to fund the Fabrica transaction and capital expenditures (details provided below).

Cash from operations of $13.2 million in the first nine months of 2015 was primarily due to cash earnings of $18.1 million and a $4.9 million increase in working capital. The increase in working capital was primarily due to increases in accounts receivable and inventory. Cash from operations, a $10.3 million net increase in debt and $32.2 million from a stock offering, were partially offset by capital expenditures of $35.5 million and $10.3 million in dividend payments, resulting in a $7.5 million increase in cash to $8.6 million as of September 30, 2015.

In June 2015, Orchids entered into an amended, five year, $187.3 million credit agreement with US Bank National Association. The agreement includes a $25 million revolving credit line, a $47.3 million term loan, a $115 million delayed draw term loan with a two year draw period, and an accordion feature allowing the revolving credit line and/or delayed draw commitment to be increased by up to $50 million at any time during the credit agreement. Advances under the facility bear interest at a variable rate of LIBOR plus a margin of 1.25% to 2.50% depending on the company's leverage ratio, or a base rate plus a margin of up to 0.25% at the company's option.

The credit agreement contains covenants that require Orchids to maintain specific fixed charge coverage and leverage ratios. As of September 30, 2015, the company was in compliance with those covenants.

In September 2014, Orchids entered into an agreement with the Oklahoma Development Finance Authority (ODFA) whereby the ODFA agreed to provide the company up to $3.5 million to fund a portion of the cost of a new paper production line. The agreement provides for Orchids' Oklahoma state withholding payroll taxes to be placed into a revolving fund held by ODFA. Each year on September 1, beginning in 2015 and ending in 2020, the ODFA will return these state withholding taxes in the revolving fund to the company, up to an amount totaling $3.5 million. These amounts are recognized as a note receivable in other current assets in the balance sheet and in other income in the income statement. The company recognized income of $514,000 in the first nine months of 2015 related to this agreement.

Projections

With a full year of shipments from Fabrica (25,000 tons of converted product) and recent new business (shipments started in August 2015) bringing Orchids' Oklahoma converted run rate to 67,000 tons annually, we project approximately 84,200 tons of converted products being shipped in 2015. For 2015, we project selling prices of $1,933/ton for converted products and $997/ton for parent rolls, consistent with year-to-date pricing.

We have increased our parent roll shipment forecast for 2015 to 8,800 tons (previously 6,900 tons) to reflect recent results as the increased capacity of the new paper machine in Oklahoma which started up in March 2015.

Orchids' agreement with Fabrica provides for the purchase of up to 19,800 tons of converted product annually with the option to purchase an additional 7,700 tons annually in each of the first two years. As the option to purchase the additional tonnage ends in 2H16, we project a reduction in 2016 Fabrica converted tonnage to 22,400 from 25,000 tons in 2015. Helping to offset this reduction in tonnage should be the contribution from Orchids' new plant in South Carolina. Orchids' currently has commitments to

Revenue Model

	Tons Shipped	Selling Price/Ton	Revenue ($,000)
2013			
Converted	52,592	$ 2,084	$ 109,611
Parent Roll	6,726	$ 1,006	$ 6,763
Total	59,318	$ 1,962	$ 116,374
2014	Tons Shipped	Selling Price/Ton	Revenue ($,000)
Converted	67,870	$ 2,039	$ 138,382
Parent Roll	4,922	$ 882	$ 4,342
Total	72,792	$ 1,961	$ 142,724
2015	Tons Shipped	Selling Price/Ton	Revenue ($,000)
Converted	84,200	$ 1,933	$ 162,759
Parent Roll	8,800	$ 997	$ 8,774
Total	93,000	$ 1,844	$ 171,532
2016	Tons Shipped	Selling Price/Ton	Revenue ($,000)
Converted	98,400	$ 1,979	$ 194,734
Parent Roll	4,000	$ 1,021	$ 4,084
Total	102,400	$ 1,942	$ 198,818

Source: Company filings and Taglich Brothers estimates sell out its first converted product line (capacity of approximately 15,000 tons) in South Carolina by the end of 2Q16, at which time the start-up of the second converting line (capacity of approximately 15,000 tons) is expected.

We project Orchids will sell total converted tonnage (from Oklahoma, Fabrica and South Carolina) of approximately 98,400 tons in 2016, higher than our previous projection of 92,800 tons due primarily to a full year of shipments from the new business in Oklahoma which started in August 2015 and the South Carolina shipments. Orchids is currently shipping to customers on the East Coast and the new South Carolina location should reduce overall freight costs. However, as the new paper machine is not expected to be operational until early 2017, Orchids will be buying parent rolls in the secondary market in 2016 which we believe will limit gross margins in that region to approximately 15% (see table at bottom right on this page).

We project 2016 selling prices of $1,979/ton for converted products and $1,021/ton for parent rolls, consistent with the 2.4% increase in paper selling prices projected by IBISWorld. Paper price gains are supported by the fact that falling demand is being outpaced by contracting supply which should result in slowly increasing prices. Our selling price projection may prove to be conservative as Orchids' average selling prices have increased at an average annual rate of 3.6% over the past three years while paper industry selling prices have remained relatively flat.

There are no sales contracts guaranteeing these orders. However, customer order streams are fairly constant and typically last several years.

Construction and installation of a new paper machine, and purchasing parent rolls in the open market had the adverse effect of increasing COGS by approximately $2.1 million in 2014. Excluding these adverse effects, 2014 gross margins would have been approximately 20.2%. The seasonality of higher energy and transportation costs in the Mexicali plant adversely affects gross margins in the second half of a year. The company said that higher energy costs typical in Mexico during the summer months flow through the supply agreement in the trailing quarters (Q3 and Q4). Thus we are projecting gross margins to be lower in the second half of a year than the first half (excluding 2015 with its 1H parent roll purchases).

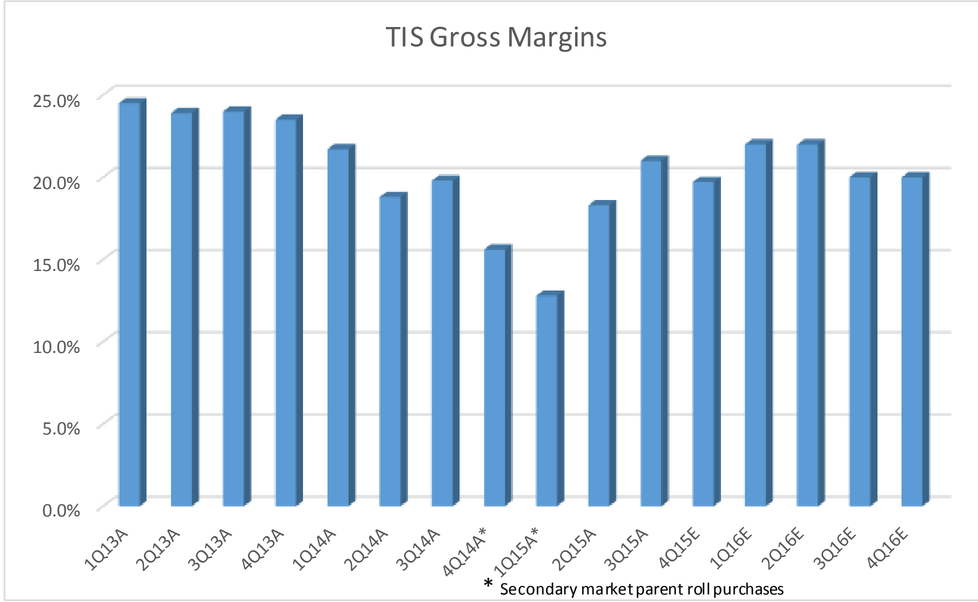
We project 2015 gross margins of 18.2%. Although year-to-date gross margins are 17.7%, the adverse effect of 1Q15's low margin (due to parent roll purchases in the secondary market) will be less of a drag on the full year margin as it will be supported by three quarters of lower cost, company generated parent rolls. We project gross margins increasing in 2016 (see table at right) as converted product sales increase and the higher cost of purchasing parent rolls in the secondary market (as seen in 2014 and 2015 margins) will have been eliminated.

	2011A	2012A	2013A	2014A	2015E	2016E
Conv. Tons	39,104	43,661	52,592	67,870	84,200	98,400
Total Tons	55,514	53,995	59,318	72,792	93,000	102,400
Conv. Ton %	70.4%	80.9%	88.7%	93.2%	90.5%	96.1%
Gross Margin	16.3%	22.4%	24.0%	18.7%	18.2%	21.0%

Source: Company filings and Taglich Brothers estimates

The chart at top right on next page illustrates the adverse effect of purchasing parent rolls in the secondary market and can be seen in 1Q15 results, when Orchids purchased approximately 3,000 tons of parent rolls in the secondary market at a cost of approximately $3.4 million resulting in an abnormally low 12.8% gross margin for the quarter. With converted product production ramping in 2Q15 and 3Q15, and the absence of secondary market parent roll purchases, gross margins began to recover and reached 21% in Orchids' most recent (3Q15) quarter. We project continued ramping of higher margin converted product sales should boost margins to 22%, but TIS's need to purchase parent rolls in the secondary market in South Carolina (at 15% gross margins) should result in a weighted average gross margin (WAGM) of 21% in 2016 (see table at right).

	% Total Revenue	Gross Margin %	WAGM
Core	85.0	22.0	18.7%
South Carolina	15.0	15.0	2.3%
Total	100		21.0%



We project 2015 revenue of $171.5 million and net income of $13.8 million or $1.39 per share. The change in our projections (previously $173 million revenue and $13.3 million or $1.35 per share net income) primarily reflects 3Q15 results.

We project SG&A expenses of $9.7 million in 2015 (of which approximately 1% or $1.7 million of sales are commission-related), lower by $2 million from 2014 due primarily to the absence of $1.6 million costs related to the Fabrica transaction and a decreased in stock options granted to management. Operating margins are projected to increase to 11.7% from 10% due primarily to lower SG&A expenses. Interest expense is projected increase to $389,000 from $271,000 due to higher debt levels. The tax rate is estimated at 31.8%.

For 2015 we project Orchids will generate $28.7 million cash from operations primarily from cash earnings. Cash from operations will not cover our projected $60 million in capital expenditures (primarily for South Carolina facility) and $12.3 million in dividend payments requiring the company to raise $32.2 million from the sale of common stock (which it did in April 2015) and a $20.3 million net increase in debt. We project a $6.5 million increase in cash to $7.6 million at December 31, 2015.

We project 2016 revenue of $198.8 million and net income of $19 million or $1.82 per share. The change in our projections (previously $192.4 million revenue and $18.1 million or $1.75 per share net income) stems primarily from increased shipments of converted products.

We project SG&A expenses of $11.1 million in 2016 (of which approximately 1% or $2 million of sales are commission-related). Operating margins are projected to increase to 14.8% from 11.7% due primarily to gross profit gains of approximately $10.5 million. Interest expense is projected to increase to $690,000 from $389,000 due to higher debt levels. Most of the interest associated with the added debt for the company’s South Carolina project will be capitalized and depreciated. The tax rate is estimated at 33.9%.

For 2016 we project Orchids will generate $38.8 million cash from operations primarily from cash earnings. Cash from operations will not cover our projected $80 million in capital expenditures (primarily for South Carolina facility) and $12.3 million in dividend payments requiring the company to raise $50 million from increased debt. We project a $3.2 million decrease in cash to $4.3 million at December 31, 2016.

Risks

Customer concentration

Four customers (Dollar General, HEB, Family Dollar and Wal-Mart) accounted for approximately 72% of total sales in 2014. Any substantial decrease or delay in sales to one or more of Orchids’ key customers would harm sales and financial results.

Competition

Competitors have penetrated Orchids' operating region. More intense competition in the company's market has reduced some of its competitive cost advantages and put pressure on selling prices.

Orchids may not be able to sell the capacity from its expanded converting line

Underutilization of capacity could lead to unabsorbed overhead and gross margin compression.

Fabrica acquisition

In June 2014, Orchids acquired various assets and business operations from Fabrica. There can be no assurance that Orchids will fully realize the anticipated benefits of the transaction. Further, as a result of the Fabrica transaction, Orchids' indebtedness is now greater than it was prior to the acquisition.

South Carolina construction project

Orchids' South Carolina construction project is anticipated to begin in 2Q15 with the first converting line expected to be operational at the end of 2015, the second in 2Q16, and the new paper machine in early 2017. Total cost is estimated at $110 million to $127 million over a two year period. There can be no assurance that the construction, installation, and ramp of production will proceed as scheduled, for the anticipated costs, or at all.

No reliance on contracts

Sales contracts are not the norm in the industry. Although orders typically result in multi-year revenue streams, there can be no guarantee as to their length.

Liquidity risk

Microcap stocks typically have small trading floats and very low trading volume and can lead to large spreads and high volatility in stock price. Orchids has 9.4 million shares in the float with an average daily volume of approximately 48,000 shares.

Miscellaneous risks

The company's financial results and equity values are subject to other risks, including competition, operations, financial markets, regulatory risk, and/or other events. These risks may cause actual results to differ from expected results.

Consolidated Balance Sheets
(in thousands $)

	2012A	2013A	2014A	9/15A	2015E	2016E
Cash	5,734	7,205	1,021	8,550	7,556	4,348
Accounts receivable	5,406	6,585	10,195	13,795	12,253	14,202
Inventories	10,275	10,921	9,650	12,047	11,675	13,071
Short term investments	5,027	5,035	-	-	-	-
Income taxes receivable	607	-	634	-	-	-
Prepaid expenses	637	863	1,285	1,626	1,626	1,626
VAT receivable	-	-	1,734	1,735	1,735	1,735
Other	44	146	899	157	157	157
Deferred income taxes	393	552	614	592	592	292
Total current assets	28,123	31,307	26,032	38,502	35,594	35,431
Property, plant and equipment	91,188	95,745	119,720	148,229	167,630	231,213
Intangible assets	-	-	17,237	16,107	15,737	14,237
Goodwill	-	-	7,560	7,560	7,560	7,560
Deferred debt issuance costs	47	40	190	872	872	272
Total Assets	119,358	127,092	170,739	211,270	227,393	288,713
Bank overdrafts	-	-	1,706	-	-	-
Accounts payable	3,685	3,685	11,391	9,551	13,781	15,429
Accrued liabilities	2,832	4,030	3,747	5,668	4,503	5,220
Current portion of long-term debt	1,152	1,152	2,700	3,025	3,025	3,025
Total current liabilities	7,669	8,867	19,544	18,244	21,309	23,674
Long-term debt	15,079	13,927	33,662	43,600	53,600	103,600
Deferred income taxes	19,432	19,449	17,020	16,175	16,175	16,175
Total liabilities	42,180	42,243	70,226	78,019	91,084	143,449
Total stockholders' equity	77,178	84,849	100,513	133,251	136,309	145,264
Total liabilities & stockholders' equity	119,358	127,092	170,739	211,270	227,393	288,713

Source: Company filings and Taglich Brothers' estimates

Income Statements for the Fiscal Years Ended
(in thousands $)

	2012A	2013A	2014A	2015E	2016E
Net sales	100,819	116,374	142,724	171,532	198,820
Cost of sales	78,253	88,494	115,985	140,319	157,104
Gross profit	22,566	27,880	26,739	31,213	41,716
Intangibles amortization			753	1,507	1,200
SG&A expenses	8,456	9,471	11,675	9,674	11,140
Operating income (loss)	14,110	18,409	14,311	20,032	29,376
Interest expense	407	371	271	389	690
Other (income) expense	302	(173)	181	(507)	-
Income (loss) before taxes	13,401	18,211	13,859	20,150	28,686
Income tax expense (benefit)	4,144	4,892	4,394	6,403	9,725
Net income (loss)	9,257	13,319	9,465	13,747	18,962
EPS	1.18	1.67	1.11	1.39	1.82
Shares Outstanding	7,832	7,937	8,539	9,882	10,425
Margin Analysis					
Gross margin	22.4%	24.0%	18.7%	18.2%	21.0%
SG&A expenses	8.4%	8.1%	8.2%	5.6%	5.6%
Operating margin	14.0%	15.8%	10.0%	11.7%	14.8%
Net margin	9.2%	11.4%	6.6%	8.0%	9.5%
Tax rate	30.9%	26.9%	31.7%	31.8%	33.9%
Year / Year Growth					
Total Revenues	3.0%	15.4%	22.6%	20.2%	15.9%
Net Income	49.4%	43.9%	(28.9%)	45.2%	37.9%
EPS	47.3%	41.3%	(33.6%)	25.5%	30.7%

Source: Company filings and Taglich Brothers' estimates

Quarterly Income Statement for the Fiscal Years Ending December 31, 2014, 2015, and 2016
(in thousands $)

	3/14A	6/14A	9/14A	12/14A	2014A	3/15A	6/15A	9/15A	12/15E	2015E	3/16E	6/16E	9/16E	12/16E	2016E
Net sales	27,759	29,196	44,429	41,340	142,724	37,415	42,295	46,832	44,990	171,532	46,520	51,100	51,890	49,310	198,820
Cost of sales	21,741	23,706	35,645	34,893	115,985	32,629	34,576	36,987	36,127	140,319	36,286	39,858	41,512	39,448	157,104
Gross profit	6,018	5,490	8,784	6,447	26,739	4,786	7,719	9,845	8,863	31,213	10,234	11,242	10,378	9,862	41,716
Intangibles amortization		108	322	323	753	377	377	376	377	1,507	300	300	300	300	1,200
SG&A expenses	2,179	4,407	2,541	2,548	11,675	2,497	2,240	2,437	2,500	9,674	2,610	2,860	2,910	2,760	11,140
Operating income (loss)	3,839	975	5,921	3,576	14,311	1,912	5,102	7,032	5,986	20,032	7,324	8,082	7,168	6,802	29,376
Interest expense	13	112	90	56	271	214	64	11	100	389	150	170	185	185	690
Other (income) expense	1	(7)	147	40	181	(186)	(152)	(169)	-	(507)	-	-	-	-	-
Income (loss) before taxes	3,825	870	5,684	3,480	13,859	1,884	5,190	7,190	5,886	20,150	7,174	7,912	6,983	6,617	28,686
Income tax expense (benefit)	1,182	324	1,854	1,034	4,394	648	1,312	2,448	1,995	6,403	2,432	2,682	2,367	2,243	9,725
Net income (loss)	2,643	546	3,830	2,446	9,465	1,236	3,878	4,742	3,891	13,747	4,742	5,230	4,616	4,374	18,962
EPS	0.32	0.07	0.44	0.28	1.11	0.14	0.39	0.45	0.37	1.39	0.45	0.50	0.44	0.42	1.82
Shares Outstanding	8,153	8,346	8,824	8,823	8,539	8,824	9,853	10,425	10,425	9,882	10,425	10,425	10,425	10,425	10,425
Margin Analysis															
Gross margin	21.7%	18.8%	19.8%	15.6%	18.7%	12.8%	18.3%	21.0%	19.7%	18.2%	22.0%	22.0%	20.0%	20.0%	21.0%
SG&A expenses	7.8%	15.1%	5.7%	6.2%	8.2%	6.7%	5.3%	5.2%	5.6%	5.6%	5.6%	5.6%	5.6%	5.6%	5.6%
Operating margin	13.8%	3.3%	13.3%	8.7%	10.0%	5.1%	12.1%	15.0%	13.3%	11.7%	15.7%	15.8%	13.8%	13.8%	14.8%
Net margin	9.5%	1.9%	8.6%	5.9%	6.6%	3.3%	9.2%	10.1%	8.6%	8.0%	10.2%	10.2%	8.9%	8.9%	9.5%
Tax rate	30.9%	37.2%	32.6%	29.7%	31.7%	34.4%	25.3%	34.0%	33.9%	31.8%	33.9%	33.9%	33.9%	33.9%	33.9%
Year / Year Growth															
Total Revenues	4.3%	(0.1%)	49.3%	34.3%	22.6%	34.8%	44.9%	5.4%	8.8%	20.2%	24.3%	20.8%	10.8%	9.6%	15.9%
Net Income	(14.5%)	(82.6%)	2.9%	(27.2%)	(28.9%)	(53.2%)	NMF	23.8%	59.1%	45.2%	283.7%	34.9%	(2.7%)	12.4%	37.9%
EPS	(17.3%)	(83.4%)	(6.4%)	(34.0%)	(33.6%)	(56.8%)	NMF	3.4%	34.6%	25.5%	224.8%	27.5%	(2.7%)	12.4%	30.7%

Source: Company filings and Taglich Brothers' estimates

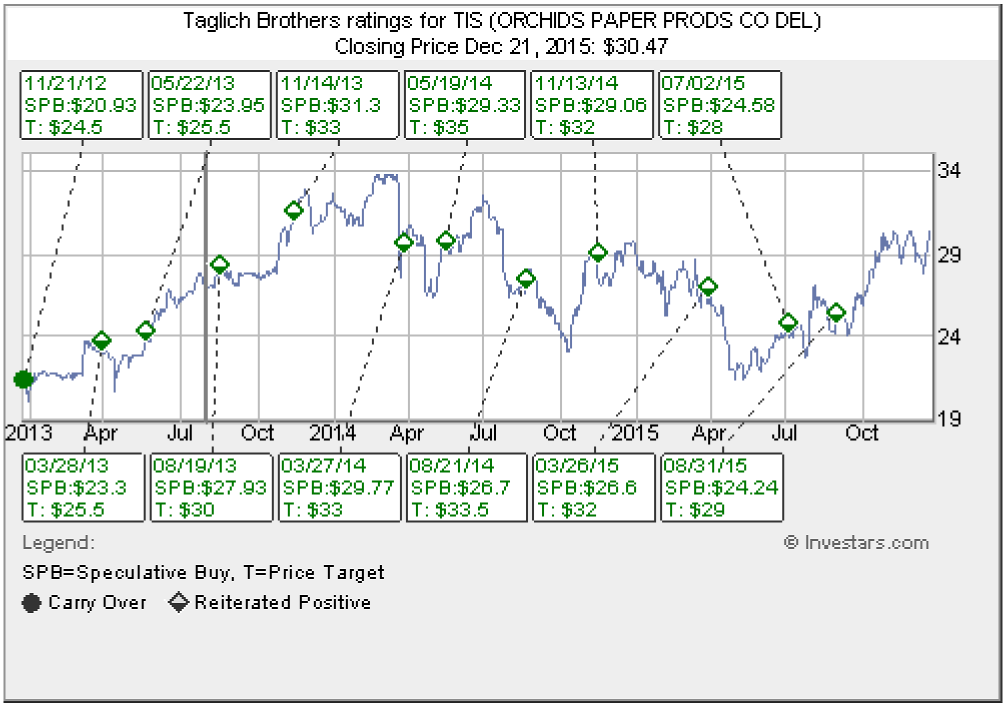
Orchids Paper Products Company

Statement of Cash Flows for the Periods Ended
(in thousands $)

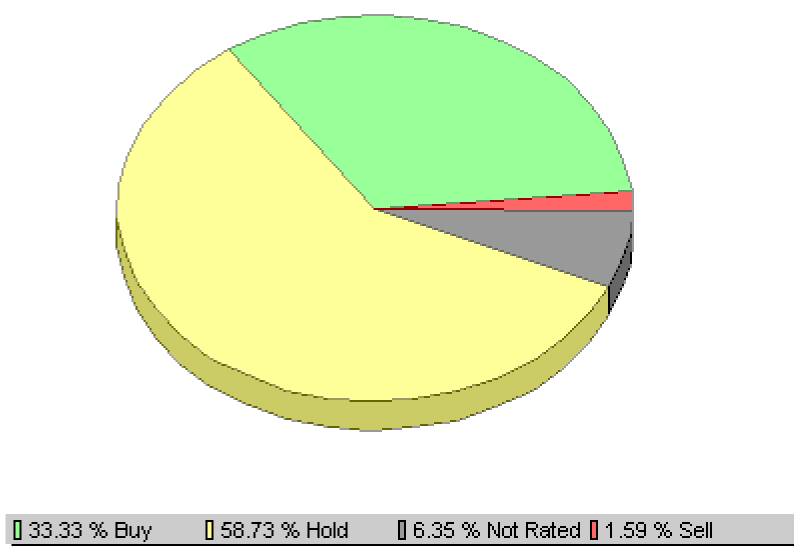
	2012A	2013A	2014A	9mos15A	2015E	2016E
Net income(loss)	9,257	13,319	9,465	9,856	13,747	18,962
Depreciation and amortization	7,548	7,621	9,749	8,255	14,290	19,117
Provision for doubful accounts	(20)	10	20	-	-	-
Deferred income taxes	648	(142)	(2,491)	(823)	(823)	-
Stock based compensation	346	346	1,879	777	2,000	2,000
(Gain) loss on disposal of property, plant and equipment	336	(146)	8	-	-	-
Cash earnings	18,115	21,008	18,630	18,065	29,214	40,079
Changes in assets and liabilities						
Accounts receivable	1,553	(1,189)	(2,556)	(3,600)	(2,058)	(1,949)
Inventories	(2,464)	(646)	1,272	(2,397)	(2,025)	(1,396)
Prepaid expenses	(107)	(226)	(422)	(341)	(341)	-
Income taxes receivable	(322)	607	(634)	634	(18)	(300)
Other current assets	294	44	(3,560)	741	742	-
Accounts payable	165	-	7,706	(1,840)	2,390	1,648
Acrrued liabilities	217	1,198	(284)	1,921	756	716
(Increase) decrease in working capital	(664)	(212)	1,522	(4,882)	(553)	(1,281)
Net Cash Provided by (Used in) Operations	17,451	20,796	20,152	13,183	28,660	38,798
Acquisition of Fabrica's US business	-	-	(16,700)	-	-	-
Proceeds from the sale of investment securities	-	(8)	5,037	-	-	-
Purchase of investment securities	(3,008)	-	(2)	-	-	-
Purchase of property and equipment	(6,780)	(12,171)	(25,769)	(35,485)	(60,000)	(80,000)
Net Cash Provided by (Used in) Investing	(9,788)	(12,179)	(37,434)	(35,485)	(60,000)	(80,000)
Proceeds from the sale of common stock	-	-	-	32,155	32,155	-
Borrowings on long-term debt	-	-	30,000	20,000	30,000	50,000
Principal payments on long-term debt	(1,152)	(1,152)	(16,429)	(2,025)	(2,025)	-
Net borrowings (repayments) on revolving credit line	-	-	7,712	(7,712)	(7,712)	-
Bank overdrafts	-	-	1,706	(1,706)	(1,706)	-
Proceeds from the exercise of stock options	974	3,305	79	210	300	300
Excess tax benefit of stock options exercised	395	1,409	20	(6)	(6)	(6)
Deferred debt issuance cost	-	-	(209)	(831)	(831)	-
Dividends paid	(6,443)	(10,708)	(11,781)	(10,254)	(12,300)	(12,300)
Net Cash Provided by (Used in) Financing	(6,226)	(7,146)	11,098	29,831	37,875	37,994
Net Change in Cash	1,437	1,471	(6,184)	7,529	6,535	(3,208)
Cash - Beginning of Period	4,297	5,734	7,205	1,021	1,021	7,556
Cash - End of Period	5,734	7,205	1,021	8,550	7,556	4,348

Source: Company filings and Taglich Brothers' estimates

Price Chart



Taglich Brothers' Current Ratings Distribution



Investment Banking Services for Companies Covered in the Past 12 Months

Rating	#	%
Buy	1	5
Hold		
Sell		
Not Rated		

Important Disclosures

As of the date of this report, Taglich Brothers, Inc. and/or its affiliates, own more than 1% of TIS common stock. Michael Taglich, President of Taglich Brothers, Inc., owns or has a controlling interest in 124,473 shares of TIS common stock. Robert Taglich, Managing Director of Taglich Brothers, Inc., owns or has a controlling interest in 52,232 shares of TIS common stock and 135,413 shares of restricted stock. Richard Oh, Managing Director of Taglich Brothers, Inc., owns 13,864 shares of TIS common stock. Doug Hailey, Director of Investment Banking at Taglich Brothers, Inc. and a Director of Orchids Paper Products Company, owns 44,150 shares of TIS common stock and 33,750 stock options. Taglich Brothers, Inc. had an Investment Banking relationship with the company mentioned in this report. In March 2004, Orchids Acquisition Group, Inc. was formed by Taglich Brothers, Inc. and Weatherly Group, LLC exclusively for the purpose of acquiring all of the outstanding shares of Orchids Paper Products Company, and was subsequently merged into the company. In July 2005, Orchids completed its initial public offering (of which Taglich Brothers, Inc. was the managing underwriter) and began trading on the American Stock Exchange under the symbol TIS.

All research issued by Taglich Brothers, Inc. is based on public information. From April 2008 to December 2012, the company paid a monthly monetary fee of $2,000 (USD) to Taglich Brothers, Inc. for the creation and dissemination of research reports.

General Disclosures

The information and statistical data contained herein have been obtained from sources, which we believe to be reliable but in no way are warranted by us as to accuracy or completeness. We do not undertake to advise you as to changes in figures or our views. This is not a solicitation of any order to buy or sell. Taglich Brothers, Inc. is fully disclosed with its clearing firm, Pershing, LLC, is not a market maker and does not sell to or buy from customers on a principal basis. The above statement is the opinion of Taglich Brothers, Inc. and is not a guarantee that the target price for the stock will be met or that predicted business results for the company will occur. There may be instances when fundamental, technical and quantitative opinions contained in this report are not in concert. We, our affiliates, any officer, director or stockholder or any member of their families may from time to time purchase or sell any of the above-mentioned or related securities. Analysts and members of the Research Department are prohibited from buying or selling securities issued by the companies that Taglich Brothers, Inc. has a research relationship with, except if ownership of such securities was prior to the start of such relationship, then an Analyst or member of the Research Department may sell such securities after obtaining expressed written permission from Compliance.

Analyst Certification

I, John Nobile, the research analyst of this report, hereby certify that the views expressed in this report accurately reflect my personal views about the subject securities and issuers; and that no part of my compensation was, is, or will be, directly, or indirectly, related to the specific recommendations or views contained in this report.

Public Companies Mentioned in this Report

Cascades (OTC PK: CADNF)
Clearwater Paper (NYSE: CLW)
Dollar General (NYSE: DG)
Family Dollar (NYSE: FDO)
Wal-Mart (NYSE: WMT)

Meaning of Ratings

Buy – The growth prospects, degree of investment risk, and valuation make the stock attractive relative to the general market or comparable stocks.

Speculative Buy – Long term prospects of the company are promising but investment risk is significantly higher than it is in our BUY-rated stocks. Risk-reward considerations justify purchase mainly by high risk-tolerant accounts. In the short run, the stock may be subject to high volatility and could continue to trade at a discount to its market.

Neutral – Based on our outlook the stock is adequately valued. If investment risks are within acceptable parameters, this equity could remain a holding if already owned.

Sell – Based on our outlook the stock is significantly overvalued. A weak company or sector outlook and a high degree of investment risk make it likely that the stock will underperform relative to the general market.

Dropping Coverage – Research coverage discontinued due to the acquisition of the company, termination of research services, non-payment for such services, diminished investor interest, or departure of the analyst.

Some notable Risks within the Microcap Market

Stocks in the Microcap segment of the market have many risks that are not as prevalent in Large-cap, Blue Chips or even Small-cap stocks. Often it is these risks that cause Microcap stocks to trade at discounts to their peers. The most common of these risks is liquidity risk, which is typically caused by small trading floats and very low trading volume which can lead to large spreads and high volatility in stock price. In addition, Microcaps tend to have significant company specific risks that contribute to lower valuations. Investors need to be aware of the higher probability of financial default and higher degree of financial distress inherent in the microcap segment of the market.

From time to time our analysts may choose to withhold or suspend a rating on a company. We continue to publish informational reports on such companies; however, they have no ratings or price targets. In general, we will not rate any company that has too much business or financial uncertainty for our analysts to form an investment conclusion, or that is currently in the process of being acquired.