TAGLICH BROTHERS

MEMBER: FINRA, SIPC | WWW.TAGLICHBROTHERS.COM

# Research Report – Update

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

## UFP Technologies, Inc.

**Rating: Buy**

John Nobile
March 29, 2018

### UFPT $29.05 — (NASDAQ CM)

| | 2016A | 2017A | 2018E | 2019E |
|---|---|---|---|---|
| Revenues (millions) | $146.1 | $147.8 | $194.0 | $208.7 |
| Earnings per share (diluted) | $1.10 | $1.26 | $1.78 | $2.55 |

| | | | |
|---|---|---|---|
| 52-Week range | $31.50 – $24.05 | Fiscal year ends: | December |
| Shares outstanding as of 3/5/18 | 7.3 million | Revenue per share (TTM) | $20.15 |
| Approximate float | 6.0 million | Price/Sales (TTM) | 1.4X |
| Market capitalization | $219 million | Price/Sales (2019)E | 1.0X |
| Tangible book value/share | $15.92 | Price/Earnings (TTM) | 23.1X |
| Price/tangible book | 1.9X | Price/Earnings (2019)E | 11.4X |

*UFP Technologies, headquartered in Georgetown, Massachusetts, designs and manufactures packaging and custom products for the medical, automotive, consumer, electronics, industrial, and aerospace and defense markets using foams, plastics, composites, and natural fiber materials. (www.ufpt.com)*

***Key investment considerations:***

***Reiterating Buy rating on UFP Technologies and increasing our twelve-month price target to $37.00 (from $30.00) per share based on strong earnings growth to 2019.***

***On February 1, 2018, UFPT acquired Dielectrics, Inc. for $80 million in cash. Dielectrics designs, develops, and manufactures medical devices using thermoplastic materials. This acquisition should provide a significant increase to UFPT's sales and earnings throughout our forecast horizon.***

***In 2017, Dielectrics generated sales of approximately $43 million. We anticipate Dielectrics to contribute sales of at least $39.4 million in 2018 and $46.4 million in 2019 to our forecast driving UFPT's medical sales to over 60% of total sales in 2019. This increase in high margin medical sales is projected to boost margins through our forecast horizon.***

***We project gross margins of 27% in 2019, up from 25.7% in 2018 and 24% in 2017.***

***4Q17 revenue (10K released on 3/16/18) increased 2% to $37.2 million with EPS of $0.37, up from $0.20. In the current period, net income included a $0.20 per share tax benefit related to the 2017 tax reform act. We projected sales of $36 million and EPS of $0.23.***

***For 2018, we project revenue growth of 31.2% to $194 million and EPS of $1.78, an increase from our prior revenue forecast of $161.2 million and EPS projection of $1.76. Our higher expectations reflect the acquisition of Dielectrics and a lower effective tax rate.***

***For 2019, we project revenue growth of 7.6% to $208.7 million and EPS of $2.55. Accelerated EPS growth should be driven by a full year of higher margin medical sales from Dielectrics and lower interest expense as the company pays down debt.***

***Please view our disclosures on pages 12 - 14.***

## *Recommendation and Valuation*

**Reiterating Buy rating on UFP Technologies and increasing our twelve-month price target to $37.00 (from $30.00) per share based on strong earnings growth to 2019 driven by the acquisition of Dielectrics.**

Shares of UFP Technologies continue to trade at a forward discount to its direct competitors (see chart below) due arguably to a lack of recognition of the company's growth potential. With the acquisition of Dielectrics and continued strong growth in medical market sales, we project 43% EPS growth versus 14% for its competitors in 2019.

| Name | Symbol | Price | Market Cap $M | Trailing P/E | 2019 P/E | Average Projected EPS Growth to 2019 |
|---|---|---|---|---|---|---|
| Packaging Corp of America | PKG | 111.18 | 10,490 | 18.4 | 12.9 | 13% |
| Sealed Air | SEE | 42.22 | 7,067 | 22.5 | 15.0 | 15% |
| Graphic Packaging | GPK | 15.23 | 4,717 | 23.8 | 15.1 | 17% |
| Bemis | BMS | 42.77 | 3,891 | 17.9 | 13.8 | 11% |
| Greif | GEF | 50.75 | 2,574 | 17.0 | 13.3 | 14% |
| **Peer Average** | | | | **19.9** | **14.0** | **14%** |
| Company | | | | | | |
| **UFP Technologies** | **UFPT** | **29.05** | **212** | **23.1** | **11.4** | **43%** |
| Source: Taglich Brothers estimates, Thomson Reuters | | | | | | |

UFP Technologies 2019 PE multiple is 11.4X based on our EPS projection of $2.55 while its direct competitors trade at a 2019 multiple of 14X. We believe UFPT's P/E multiple should expand above its competitors as strong sales and earnings growth is recognized. We applied a multiple of 17X (unchanged) to our 2019 EPS projection of $2.55, discounted to account for execution risk, to obtain a year-ahead value of approximately $37.00 per share.

## *Acquisition of Dielectrics*

On February 1, 2018, UFPT acquired Dielectrics, Inc. for $80 million in cash. Based in Chicopee, Massachusetts, Dielectrics designs, develops, and manufactures medical devices using thermoplastic materials.

Approximately 60% of Dielectrics' customers are customers of UFPT. The company provides complementary – not competing – products and services. In 2017, Dielectrics' sales were approximately $43 million.

In connection with the acquisition, UFPT expects to expense approximately $1.1 million in transaction costs in 1Q18, which are included in our forecast.

## *Business*

UFP Technologies, headquartered in Georgetown, Massachusetts, designs and manufactures packaging and custom products for the medical, automotive, consumer, electronics, industrial, and aerospace and defense markets using foams, plastics, composites, and natural fiber materials.

UFPT's products include automotive interior trim, medical device components, disposable wound care components, athletic padding, air filtration, high-temperature insulation, and military uniform and gear components.

Almost 50% of UFPT's sales are to the medical device industry for applications such as compression-molded foam finger splints, orthopedic foam components, and dental fluoride trays. UFPT's other end markets (automotive, aerospace & defense, consumer electronics, and industrial) each account for approximately 7% to 16% of the company's revenue.


Source: UFP Technologies

The company differentiates itself through the design and production of customized products (such as protective cases and custom foam inserts pictured at right). Through a combination of materials, technology, and engineering, the company is able to produce unique case inserts for surgical instruments, customized repair kits, electronic parts, emergency response equipment, and many other applications.

## *Industry Outlook*

IBISWorld forecasted the urethane foam manufacturing industry to grow at an average annual rate of 1.3% to $12.9 billion through 2022. Industry growth is predicated on strong overall domestic demand and a positive economic outlook.

The company's medical products are used in packaging systems for surgical tools, electronic devices, endoscopes and orthopedic implants. An aging population and technological advancements are among the top factors driving the medical device industry's growth over the next five years. IBISWorld forecasted medical device industry average annual sales growth of approximately 2.8% to $50.6 billion in 2023 from 2018.

IBISWorld projected sales in the US car and automobile industry to be flat through 2023 reflecting demand for new vehicles to slow due to the release of pent-up demand in prior years.

UFP Technologies makes products used in the packaging of consumer electronics. This market is projected to show strong growth over the next eight years. According to research by Future Market Insights, the worldwide market for consumer electronics is anticipated to grow at a compound annual growth rate of 15% from 2016 to 2026 reaching a value of $3 trillion by the end of the forecast period. Growth will be driven by a significant rise in the purchasing power of consumers, stimulated by an increase in their disposable income.

UFP Technologies' aerospace and defense products are used in applications such as protective cases and inserts for military equipment (i.e. tools used for large engine rebuilds), uniform and gear components such as backpacks and duty belts, and explosion suppressant foams used in fuel systems of aircrafts. The US Department of Defense's budget requests $686 billion for US defense spending in 2019, $74 billion higher than 2018 and $80 billion higher than 2017. If the 2018 spending bill is signed into law, the fiscal 2018 defense budget could be almost $43 billion higher than what was originally requested. This potential boost in defense spending over the next two years should bode well for UFPT's sales to this market.

## *Economic Outlook*

Since most of the company's revenue is tied to economically sensitive end markets in the US, increasing economic growth should support our revenue forecast to 2019.

In January 2018, the IMF raised its global economic growth estimate to 3.9% for both 2018 and 2019, up from 3.7% in October 2017. The upward revision reflects increased global economic growth momentum and the positive impact expected from recently approved US tax policy changes.

The IMF raised its economic growth estimate for the US to 2.7% in 2018 and 2.5% in 2019, up from its earlier (October 2017) growth forecast of 2.3% for 2018 and 1.9% for 2019. The upward revision reflects stronger than expected US economic activity in 2017, higher projected external demand, and the positive economic impact from 2018 tax policy changes, in particular the reduction in corporate tax rates and the temporary allowance for full expensing of investments.

The second estimate of US GDP growth (released on February 28, 2018) showed the US economy grew at an annual rate of 2.5% in 4Q17, down from 3.2% growth in 3Q17. The 4Q17 US GDP growth estimate primarily reflects increases in consumer spending, business investment, exports, housing investment, and federal, state and local government spending. These contributions were partly offset by declines in inventory investment.

## *Competition*

The packaging industry is highly competitive. While there are several national companies that sell interior packaging, the company's primary competition for its packaging are smaller independent regional manufacturing companies. The company's foam and fiber packaging products also compete against products made from alternative materials, including expanded polystyrene foams, die-cut corrugated, plastic peanuts, plastic bubbles, and foam-in-place urethane. The company's component products compete with smaller companies that typically concentrate on production of component products for specific industries.

Proximity is a key competitive factor in the packaging business. Companies shipping products typically buy packaging from vendors that are relatively close to their manufacturing facilities to increase shipping efficiency and decrease costs. As many US companies move their manufacturing operations overseas, particularly to the Far East, the associated packaging business often follows. UFP Technologies has lost customers in the past and may lose customers in the future as a result of customers moving their manufacturing facilities offshore, then hiring competitors that operate packaging-production facilities perceived to be more territorially advantageous.

Other competitive factors are price, product performance, product reliability, and customer service. We believe the company's ability to custom design proprietary manufacturing equipment in conjunction with its machinery suppliers enables the company to effectively differentiate its products. For example, UFPT has custom-designed its own lamination machines allowing the company to achieve adhesive bonds between cross-linked foam and fabric and other materials that do not easily combine. These specialty laminates typically command higher prices than traditional foam products.

Some of UFPT's public competitors include Graphic Packaging, Packaging Corp. of America, Greif, Bemis Company, and Sealed Air Corp. TTM sales and gross margins for UFP Technologies and its public competitors are shown in the table at right.

| Company | Sales TTM | Gross Margin |
|---|---|---|
| Graphic Packaging | $4.4B (12/17) | 16.4% |
| Packaging Corp. of America | $6.4B (12/17) | 22.8% |
| Greif | $3.7B (1/18) | 19.2% |
| Bemis Company | $4.1B (12/17) | 19.4% |
| Sealed Air Corp. | $4.5B (12/17) | 31.8% |
| UFP Technologies | $147.8M (12/17) | 24.0% |

Source: Yahoo! Finance

UFPT's margins are at the high end of the range for our comparison group, due arguably to the company's ability to differentiate its products. Most of the company's competitors primarily offer conventional shipping and packaging products (i.e. shipping containers and boxes) or flexible packaging products (i.e. plastic bags, films and laminates) whereas UFP Technologies offers products that are custom designed and engineered for specific applications (i.e. customized foam case inserts for the electronics industry).

## *Projections*

The company's February 2018 acquisition of Dielectrics should provide a significant increase to UFPT's sales and earnings throughout our forecast horizon. In 2017, Dielectrics generated sales of approximately $43 million. We anticipate Dielectrics to contribute sales of at least $39.4 million in 2018 and $46.4 million in 2019 to our forecast driving UFPT's medical sales to over 60% of total sales in 2019. This increase in high margin medical sales is projected to boost margins through our forecast horizon.

The company completed the relocation of certain operations in its Georgetown, Massachusetts facility into its Newburyport, Massachusetts facility in 2017. While over $2 million in one-time expenses have occurred in connection with these consolidations, annual cost savings of $1 million are expected due to reduced real estate and labor costs.

*2018 Forecast*

For 2018, we project revenue growth of 31.2% to $194 million and net income of $13.2 million or $1.78 per share, an increase from our prior revenue forecast of $161.2 million and net income projection of $12.9 million or $1.76 per share. Our increased revenue forecast reflects the recent acquisition of Dielectrics. Our EPS forecast reflects a lower effective tax rate stemming from the 2017 tax reform act, offset in part by $1.1 million of transaction costs (in 1Q18) and $1.7 million of interest expense associated with $56 million the company borrowed for the acquisition of Dielectrics.

With an increase in higher margin medical sales and the consolidation of manufacturing facilities ended, we project gross margins increasing to 25.7% from 24% in 2017. SG&A expenses should increase to $29.5 million from $23.8 million due primarily to the acquisition of Dielectrics. SG&A margins should decrease to 15.2% from 16.1% in 2017. We project operating income growth of 64.5% to $19.2 million with margins increasing to 9.9% from 7.9%. We project a tax rate of 25%.

In 2018, we project $17.7 million cash from operations from cash earnings of $27.4 million and a $9.7 million increase in working capital primarily due to increased receivables and inventories. The acquisition of Dielectrics resulted in $56 million in debt. Cash from operations and borrowings will not cover capital expenditures, the acquisition, and repayment of debt ($17 million). We project a $27.1 million decrease in cash to $10.9 million at the end of 2018.

*2019 Forecast*

For 2019, we project revenue growth of 7.6% to $208.7 million and net income of $18.9 million or $2.55 per share. Growth will be driven primarily by a full year of higher margin medical sales from Dielectrics and lower interest expense as the company continues to pay down debt.

We project gross margins increasing to 27% from our 2018 forecast of 25.7% as higher margin medical sales continue to grow. SG&A expenses should increase to $30.3 million from $29.5 million due primarily to increased compensation costs. SG&A margins should decrease to 14.5% from our 2018 forecast of 15.2%. We project operating income growth of 35.6% to $26.1 million with margins increasing to 12.5% from 9.9%. We are maintaining a tax rate of 25%.

In 2019, we project $29.8 million cash from operations from cash earnings of $32 million and a $2.2 million increase in working capital primarily due to increased receivables. We project a $23 million pay down of debt and $7 million of capital expenditures will increase cash by $207,000 to $11.1 million at the end of 2019.

## *4Q and Fiscal 2017 Financial Results*

*4Q17* - Sales increased 2% to $37.2 million with net income of $2.7 million or $0.37 per share, up from $1.5 million or $0.20 per share. Net income included a $1.5 million or $0.20 per share tax benefit related to the 2017 tax reform act. We projected sales of $36 million and net income of $1.7 million or $0.23 per share.

Gross profit decreased to $7.8 million from $8.2 million on a decrease in gross margins to 21.1% from 22.4%, respectively. SG&A expenses increased to $5.8 million from $5.7 million for operating income of $2.1 million versus $2.3 million in 4Q16. Operating margins decreased to 5.5% compared to 6.3% in the year ago period. The company had an effective income tax rate of 28.3%.

*Fiscal 2017* - Sales increased 1% to $147.8 million with net income of $9.2 million or $1.26 per share, up from net income of $8 million or $1.10 per share in 2016. 2017 net income included a $1.5 million or $0.20 per share tax benefit related to the tax reform act. 2016 net income included a $2.1 million or $0.29 per share gain related to a material overcharge settlement.

The increase in sales was primarily due to increased sales to the medical, aerospace and defense and consumer markets of approximately 8.1%, 5.2% and 4.4%, respectively, partially offset by decreases in sales to the automotive and industrial markets of approximately 15.1% and 7.4%, respectively.

The increase in sales to the medical market was largely due to increased demand from the company's medical customers. Aerospace and defense market sales rose in large part to increased government spending on defense. Consumer market sales reflect increased demand for molded fiber protective packaging for consumer products. The decrease in sales to the automotive market was largely due to the phase-out of the company's automotive door panel program for Mercedes Benz, which began in 2004, as well as reductions in demand on certain legacy programs. Sales for the company's Mercedes Benz program were approximately $3 million in 2017 and are expected to be modest in 2018, as the program ends in the first quarter of 2018. Following the cessation of the Mercedes Benz program, the company plans to cease operations and vacate its Georgia facility when that lease expires in April 2018.

Gross margins increased to 24% from 23.7% due primarily to improvements in manufacturing efficiencies that began in 2H17. SG&A expenses decreased to $23.8 million from $24.1 million due primarily to cost containment efforts. Operating income decreased to $11.7 million from $12.2 million on operating margins of 7.9% and 8.4%, respectively. The company had an effective income tax rate of 22.3%.

### *Liquidity*

The company has a strong balance sheet. At December 31, 2017, the company had no debt, tangible equity of $116.4 million, and cash (approximately $5.24 per share) exceeds all liabilities.

Cash from operations of $17.5 million for 2017 consisted of $14.9 million in cash earnings and a $2.6 million decrease in working capital. The decrease in working capital was primarily due to lower inventories and higher accruals. Cash provided by operations covered $10.4 million of capital expenditures and a $856,000 repayment of debt resulting in a $6.6 million increase in cash to $38 million as of December 31, 2017.

On February 1, 2018, the company entered into an unsecured $70 million amended and restated credit agreement with Bank of America that matures on February 1, 2023. The credit facilities consist of a $20 million term loan and a $50 million revolving credit facility at an interest rate of LIBOR plus a margin that ranges from 1.0% to 1.5% or, at the discretion of the company, the bank's prime rate less a margin that ranges from .25% to zero.

Under the restated credit agreement, the company is subject to a minimum fixed-charge coverage financial covenant as well as a maximum total funded debt to EBITDA financial covenant. As of March 16, 2018, the company had approximately $56 million in borrowings outstanding under the amended and restated credit facilities, which were used as partial consideration for the Dielectrics acquisition.

In connection with the amended and restated credit agreement, the company entered into a $20 million, 5-year interest rate swap agreement under which the company receives three-month LIBOR plus the applicable margin and pays a 2.7% fixed rate plus the applicable margin. The swap modifies the company’s interest rate exposure by converting the term loan from a variable rate to a fixed rate in order to hedge against the possibility of rising interest rates during the term of the loan.

## *Risks*

In our view, these are the principal risks underlying the stock:

<u>Dependence on a small number of customers</u>
The company’s top ten customers represented approximately 29% of total revenues in 2017. The loss of sales to a large customer would have a material adverse effect on projected financial results.

<u>Competition</u>
The packaging and component products industries are highly competitive. The company’s primary competition for its packaging products has been from smaller independent regional manufacturers. UFPT’s component products face competition from smaller companies that typically concentrate on production of component products for specific industries.

<u>Economic conditions</u>
Poor economic conditions could negatively impact sales of the company’s packaging customers.

<u>Environmental considerations</u>
Future government action may impose restrictions affecting the industries in which the company operates. There can be no assurance that any such action will not adversely impact UFP Technologies.

<u>Liquidity</u>
With only 7.3 million shares outstanding and 6 million in the float, liquidity issues must be considered. Average daily volume has been approximately 21,000 shares. Any significant trading in shares of UFPT could result in large swings in the price of the stock.

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

## Balance Sheets
(in thousands $)

| | 2015A | 2016A | 2017A | 2018E | 2019E |
|---|---|---|---|---|---|
| Cash and cash equivalents | 29,804 | 31,359 | 37,978 | 10,873 | 11,081 |
| Receivables | 17,481 | 21,249 | 21,381 | 28,056 | 30,182 |
| Inventories | 14,202 | 14,151 | 12,863 | 16,500 | 17,442 |
| Prepaid expenses | 930 | 2,281 | 1,835 | 2,385 | 2,385 |
| Refundable income taxes | 1,186 | 807 | 1,017 | 1,320 | 1,320 |
| Total current assets | 63,603 | 69,847 | 75,074 | 59,135 | 62,410 |
| Net property, plant and equipment | 46,555 | 48,516 | 53,652 | 106,959 | 103,436 |
| Goodwill | 7,322 | 7,322 | 7,322 | 12,322 | 12,322 |
| Intangible assets | 636 | 318 | - | 15,000 | 13,500 |
| Other assets | 1,834 | 1,931 | 2,159 | 2,800 | 2,800 |
| **Total assets** | **119,950** | **127,934** | **138,207** | **196,216** | **194,468** |
| | | | | | |
| Current portion of long-term debt | 1,011 | 856 | - | 3,000 | 3,000 |
| Accounts payable | 4,598 | 4,002 | 4,180 | 5,362 | 5,668 |
| Accrued expenses | 5,374 | 4,698 | 5,763 | 7,562 | 8,135 |
| Total current liabilities | 10,983 | 9,556 | 9,943 | 15,924 | 16,803 |
| Long-term debt | 859 | - | - | 36,000 | 13,000 |
| Deferred income taxes | 2,883 | 3,459 | 2,440 | 3,170 | 3,170 |
| Other liabilities | 1,653 | 1,866 | 2,112 | 2,740 | 2,740 |
| **Total liabilities** | **16,378** | **14,881** | **14,495** | **57,834** | **35,713** |
| **Total stockholders' equity** | **103,572** | **113,053** | **123,712** | **138,382** | **158,755** |
| **Total liabilities & stockholders' equity** | **119,950** | **127,934** | **138,207** | **196,216** | **194,468** |

Source: Company filings and Taglich Brothers' estimates

## Annual Income Statements
(in thousands $)

| | 2015A | 2016A | 2017A | 2018E | 2019E |
|---|---|---|---|---|---|
| Net sales | 138,850 | 146,132 | 147,842 | 194,000 | 208,700 |
| Cost of sales | 101,397 | 111,482 | 112,355 | 144,125 | 152,351 |
| Gross profit | 37,453 | 34,650 | 35,487 | 49,875 | 56,349 |
| | | | | | |
| Extraordinary items | 1,731 | (1,692) | (51) | 1,100 | - |
| SG&A | 24,009 | 24,105 | 23,845 | 29,540 | 30,260 |
| Operating income | 11,713 | 12,237 | 11,693 | 19,235 | 26,089 |
| | | | | | |
| Non-operating (expenses) income | 27 | 80 | 166 | (1,650) | (900) |
| Income before taxes | 11,740 | 12,317 | 11,859 | 17,585 | 25,189 |
| Income tax (benefit) | 4,147 | 4,347 | 2,649 | 4,396 | 6,297 |
| | | | | | |
| Net Income / (Loss) | 7,593 | 7,970 | 9,210 | 13,189 | 18,892 |
| EPS | 1.05 | 1.10 | 1.26 | 1.78 | 2.55 |
| Shares Outstanding | 7,219 | 7,275 | 7,337 | 7,400 | 7,400 |
| | | | | | |
| Margin Analysis | | | | | |
| Gross margin | 27.0% | 23.7% | 24.0% | 25.7% | 27.0% |
| SG&A | 17.3% | 16.5% | 16.1% | 15.2% | 14.5% |
| Operating margin | 8.4% | 8.4% | 7.9% | 9.9% | 12.5% |
| Pretax margin | 8.5% | 8.4% | 8.0% | 9.1% | 12.1% |
| Tax rate | 35.3% | 35.3% | 22.3% | 25.0% | 25.0% |
| | | | | | |
| Year / Year Growth | | | | | |
| Total Revenues | (0.3)% | 5.2% | 1.2% | 31.2% | 7.6% |
| Net Income | 0.4% | 5.0% | 15.6% | 43.2% | 43.2% |
| EPS | (0.2)% | 4.2% | 14.6% | 42.0% | 43.2% |

Source: Company filings and Taglich Brothers' estimates

Quarterly Income Statements 2017A - 2019E
(in thousands $)

| | 3/17A | 6/17A | 9/17A | 12/17A | 2017A | 3/18E | 6/18E | 9/18E | 12/18E | 2018E | 3/19E | 6/19E | 9/19E | 12/19E | 2019E |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Net sales | 37,053 | 37,886 | 35,684 | 37,219 | 147,842 | 44,000 | 49,500 | 50,000 | 50,500 | 194,000 | 51,350 | 51,900 | 52,450 | 53,000 | 208,700 |
| Cost of sales | 27,537 | 27,945 | 27,491 | 29,382 | 112,355 | 33,880 | 36,630 | 36,750 | 36,865 | 144,125 | 37,486 | 37,887 | 38,289 | 38,690 | 152,351 |
| Gross profit | 9,516 | 9,941 | 8,193 | 7,837 | 35,487 | 10,120 | 12,870 | 13,250 | 13,635 | 49,875 | 13,865 | 14,013 | 14,162 | 14,310 | 56,349 |
| Extraordinary items | (5) | (50) | - | 4 | (51) | 1,100 | - | - | - | 1,100 | - | - | - | - | - |
| SG&A | 6,316 | 6,061 | 5,693 | 5,775 | 23,845 | 7,040 | 7,425 | 7,500 | 7,575 | 29,540 | 7,445 | 7,525 | 7,605 | 7,685 | 30,260 |
| Operating income | 3,205 | 3,930 | 2,500 | 2,058 | 11,693 | 1,980 | 5,445 | 5,750 | 6,060 | 19,235 | 6,420 | 6,488 | 6,557 | 6,625 | 26,089 |
| Non-operating (expenses) income | 28 | 29 | 51 | 58 | 166 | (400) | (475) | (425) | (350) | (1,650) | (300) | (250) | (200) | (150) | (900) |
| Income before taxes | 3,233 | 3,959 | 2,551 | 2,116 | 11,859 | 1,580 | 4,970 | 5,325 | 5,710 | 17,585 | 6,120 | 6,238 | 6,357 | 6,475 | 25,189 |
| Income tax (benefit) | 1,062 | 1,329 | 856 | (599) | 2,649 | 395 | 1,243 | 1,331 | 1,428 | 4,396 | 1,530 | 1,560 | 1,589 | 1,619 | 6,297 |
| Net Income / (Loss) | 2,171 | 2,630 | 1,695 | 2,715 | 9,210 | 1,185 | 3,728 | 3,994 | 4,283 | 13,189 | 4,590 | 4,679 | 4,767 | 4,856 | 18,892 |
| EPS | 0.30 | 0.36 | 0.23 | 0.37 | 1.26 | 0.16 | 0.50 | 0.54 | 0.58 | 1.78 | 0.62 | 0.63 | 0.64 | 0.66 | 2.55 |
| Shares Outstanding | 7,297 | 7,323 | 7,353 | 7,369 | 7,337 | 7,400 | 7,400 | 7,400 | 7,400 | 7,400 | 7,400 | 7,400 | 7,400 | 7,400 | 7,400 |
| Margin Analysis | | | | | | | | | | | | | | | |
| Gross margin | 25.7% | 26.2% | 23.0% | 21.1% | 24.0% | 23.0% | 26.0% | 26.5% | 27.0% | 25.7% | 27.0% | 27.0% | 27.0% | 27.0% | 27.0% |
| SG&A | 17.0% | 16.0% | 16.0% | 15.5% | 16.1% | 16.0% | 15.0% | 15.0% | 15.0% | 15.2% | 14.5% | 14.5% | 14.5% | 14.5% | 14.5% |
| Operating margin | 8.6% | 10.4% | 7.0% | 5.5% | 7.9% | 4.5% | 11.0% | 11.5% | 12.0% | 9.9% | 12.5% | 12.5% | 12.5% | 12.5% | 12.5% |
| Pretax margin | 8.7% | 10.4% | 7.1% | 5.7% | 8.0% | 3.6% | 10.0% | 10.7% | 11.3% | 9.1% | 11.9% | 12.0% | 12.1% | 12.2% | 12.1% |
| Tax rate | 32.8% | 33.6% | 33.6% | 35.0% | 22.3% | 25.0% | 25.0% | 25.0% | 25.0% | 25.0% | 25.0% | 25.0% | 25.0% | 25.0% | 25.0% |
| Year / Year Growth | | | | | | | | | | | | | | | |
| Total Revenues | 7.4% | 0.0% | (4.1)% | 2.0% | 1.2% | 18.7% | 30.7% | 40.1% | 35.7% | 31.2% | 16.7% | 4.8% | 4.9% | 5.0% | 7.6% |
| Net Income | 102.0% | (3.8)% | (36.5)% | 82.1% | 15.6% | (45.4)% | 41.7% | 135.6% | 57.7% | 43.2% | 287.3% | 25.5% | 19.4% | 13.4% | 43.2% |
| EPS | 100.8% | (4.5)% | (36.8)% | 80.4% | 14.6% | (46.2)% | 40.3% | 134.1% | 57.1% | 42.0% | 287.3% | 25.5% | 19.4% | 13.4% | 43.2% |

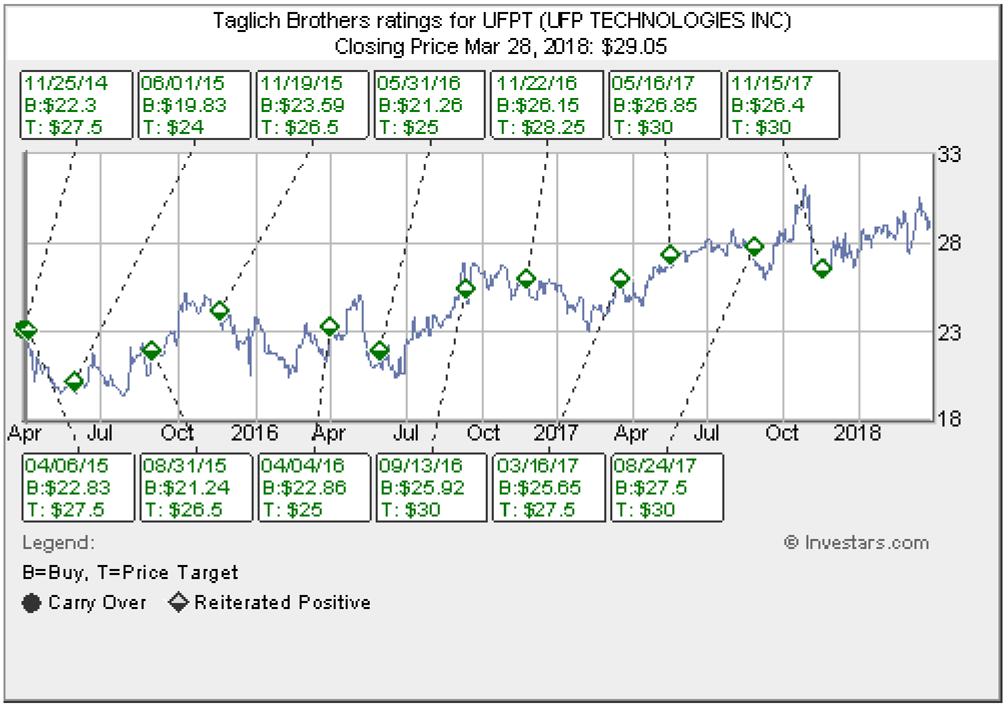
Source: Company filings and Taglich Brothers' estimates

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

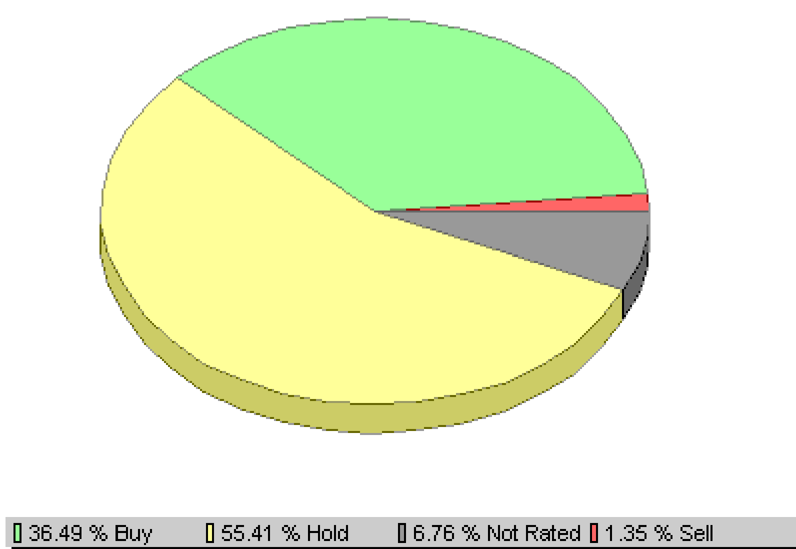
| | 2015A | 2016A | 2017E | 2018E | 2019E |
|---|---|---|---|---|---|
| Net income | 7,593 | 7,970 | 9,210 | 13,189 | 18,892 |
| Depreciation & amortization | 4,846 | 5,634 | 5,635 | 12,393 | 12,023 |
| (Gain) loss on disposal of property, plant and equipment | 27 | 2 | 7 | - | - |
| Share-based compensation | 1,069 | 1,056 | 1,068 | 1,100 | 1,100 |
| Excess tax benefit on share-based compensation | (356) | (145) | - | - | - |
| Deferred income taxes | 437 | 576 | (1,019) | 730 | - |
| Cash earnings | 13,616 | 15,093 | 14,901 | 27,412 | 32,015 |
| *Changes in assets and liabilities* | | | | | |
| Receivables | (1,011) | (3,768) | (132) | (6,675) | (2,126) |
| Inventories | (1,309) | 51 | 1,288 | (3,637) | (942) |
| Prepaid expenses | (266) | (1,351) | 446 | (550) | - |
| Refundable income taxes | 2,362 | 209 | (210) | (1,803) | - |
| Accounts payable | (800) | (596) | 93 | 1,182 | 306 |
| Accrued expenses and other | 152 | (361) | 1,065 | 1,799 | 573 |
| Retirement and other liabilities | 29 | 213 | 246 | 628 | - |
| Other assets | 325 | (97) | (228) | (641) | - |
| (Increase) decrease in working capital | (518) | (5,700) | 2,568 | (9,697) | (2,189) |
| **Net Cash Provided by Operations** | **13,098** | **9,393** | **17,469** | **17,714** | **29,826** |
| Additions to property, plant and equipment | (16,321) | (7,293) | (10,382) | (7,000) | (7,000) |
| Cash paid for acquisitions (net) | - | - | - | (77,200) | |
| Proceeds from sale of fixed assets | 53 | 14 | 7 | - | - |
| **Net Cash Used in Investing** | **(16,268)** | **(7,279)** | **(10,375)** | **(84,200)** | **(7,000)** |
| Proceeds from long-term borrowings | - | - | - | 56,000 | - |
| Repurchases of common stock | (587) | - | - | - | - |
| Tax benefit from exercise of non-qualified stock options | 356 | 145 | - | - | - |
| Proceeds from exercise of stock options | 358 | 529 | 677 | 677 | 677 |
| Payment of statutory withholdings for stock options exercised | (209) | (219) | (296) | (296) | (296) |
| Principal repayments of long-term debt | (996) | (1,014) | (856) | (17,000) | (23,000) |
| **Net Cash Provided by (Used in) Financing** | **(1,078)** | **(559)** | **(475)** | **39,381** | **(22,619)** |
| **Net Change in Cash** | **(4,248)** | **1,555** | **6,619** | **(27,105)** | **207** |
| **Cash - Beginning of Period** | **34,052** | **29,804** | **31,359** | **37,978** | **10,873** |
| **Cash - End of Period** | **29,804** | **31,359** | **37,978** | **10,873** | **11,081** |

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 | 4 |
| Hold | | |
| Sell | | |
| Not Rated | 1 | 33 |

## Important Disclosures

As of the date of this report, we, our affiliates, any officer, director or stockholder, or any member of their families do not have a position in the stock of the company mentioned in this report. Taglich Brothers, Inc. does not currently have an Investment Banking relationship with the company mentioned in this report and was not a manager or co-manager of any offering for the company within the last three years.

All research issued by Taglich Brothers, Inc. is based on public information. Since February 2000, the company has paid a monthly monetary fee of $1,000 (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

Graphic Packaging (NYSE: GPK)
Packaging Corp. of America (NYSE: PKG)
Greif (NYSE: GEF)
Bemis Company (NYSE: BMS)
Sealed Air Corp. (NYSE: SEE)

## 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.