From ValueWalk

Interview one:

## Joseph Boskovich Jr. and team: Old West Investment Management

Old West Investment Management manages two LP's and a long only strategy. Chairman, chief investment officer and portfolio manager Joseph Boskovich, Sr. co-founded the business along with his son, Joseph Boskovich, Jr. and they've been managing investors' money since the end of 2008. The firm runs a concentrated value strategy with around 40% of assets under management in the top ten holdings.

Unfortunately, as value has fallen out of favor, though the firm has struggled over the past three years, however, over the long-term returns are impressive. The Old West All Cap Opportunity strategy has produced an annualized return for investors of 11.3% net since inception (12/01/2008). Meanwhile, year-to-date (28 February) the Old West Income Fund has gained 15% net, eclipsing the S&P 500's total return of 1.8% over the same period.

continue to page 09

Interview two:

## Christine Song Songbird Asset Management

Christine Song, CFA is the founder & portfolio manager of Songbird Asset Management. Christine and her team are focused on finding hidden gems, misunderstood businesses with attractive long-term outlooks that they can hold in a concentrated portfolio. This approach has paid off handsomely for the team as the firm has outrun its benchmark. Last year, Songbird produced a return for investors of 25.6% gross compared to the Russell 2500 benchmark performance of 16.8%. Since inception (01/01/2011), Songbird has produced an annualized return for investors of 25.3%, outperforming its benchmark by 7.4% per annum gross of fees.

continue to page 23

## Contents

P 03
Introduction and Updates

P 07
Returns

P 09
Interview One: Old West

P 15
Old West: Stock Idea One

P 20
Old West: Stock Idea Two

P 23
Interview Two: Songbird Asset

P 25
Songbird: Stock Idea One

P 29
Songbird: Stock Idea Two

P 34
Disclosures

**Songbird Asset Management**
**Representative Portfolio**
Gross of fees

| Annual (inception date of 1/1/2011) | SAM Gross Returns | Russell 2500 Benchmark | Relative Performance |
|---|---|---|---|
| 2011 | 6.81% | -2.51% | 9.32% |
| 2012 | 15.40% | 17.88% | -2.48% |
| 2013 | 32.04% | 36.80% | -4.76% |
| 2014 | 11.59% | 7.07% | 4.52% |
| 2015 | 10.21% | -2.90% | 13.11% |
| 2016 | 10.05% | 17.59% | -7.54% |
| 2017 | 25.57% | 16.81% | 8.76% |

| | SAM | R2.5 | Rel. Perf. |
|---|---|---|---|
| Cumulative annual gross returns | 176.60% | 124.50% | 52.09% |
| Annualized over 7 years (2011 to 2017) | 25.23% | 17.79% | 7.44% |

# Introduction and Updates

A few weeks ago, at hiddenvaluestocks.com we published a roundup of unusual, undervalued small-cap positions as profiled in a select group of value-focused funds' year-end letters. This roundup is available to all premium subscribers.

As part of our mission to help readers uncover hidden value, rather than focus on updates from previous editions at the front of this newsletter, we have included two of our favorite picks from the year-end roundup, which means there are now six hidden value stocks profiled in this issue.

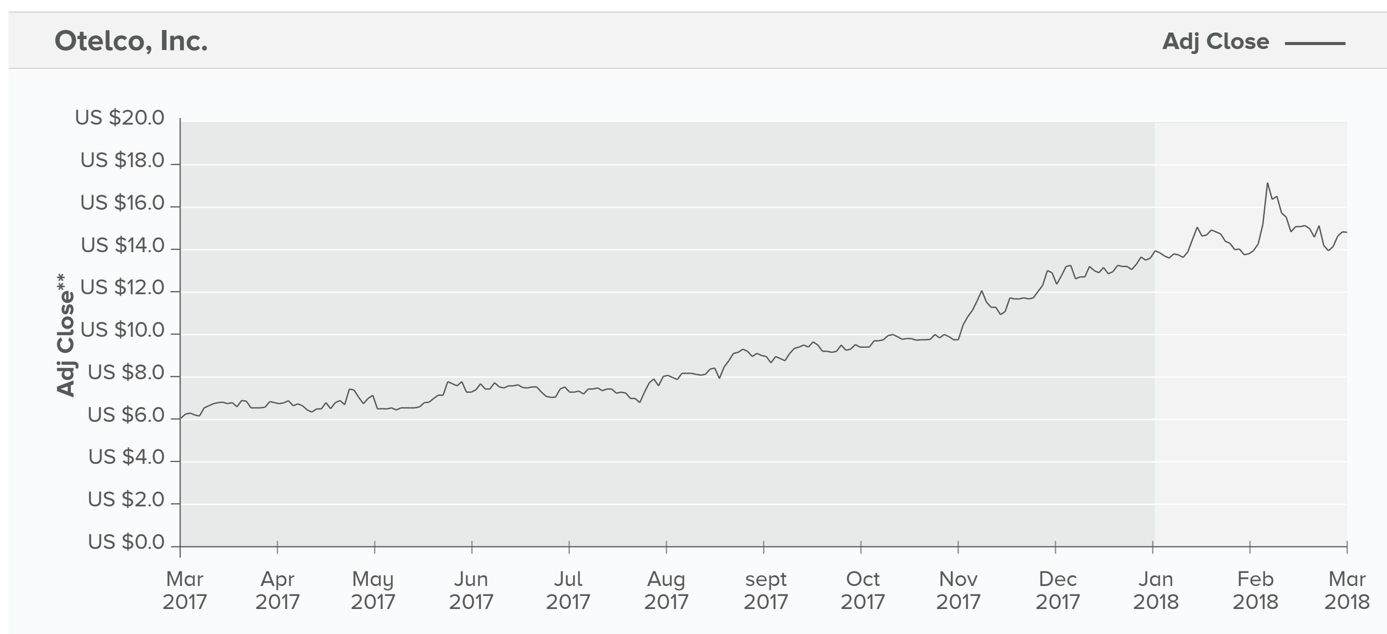
As always, we hope you enjoy Hidden Value Stocks and welcome any comments you may have. If you would like to find out more about any of the funds profiled, feel free to drop us an email.

Sincerely,
Rupert Hargreaves
& Jacob Wolinsky
jacob@valuewalk.com
rhargreaves@valuewalk.com

INTRODUCTION AND UPDATES

# Alluvial Capital Management: Otelco, Inc.

Otelco achieved a new lease on life in November, when it announced a refinancing of all its debt at very attractive terms from a very attractive lender, CoBank. In the transaction, Otelco reduced its cost of debt by more than 400 basis points. The company also gained the ability to distribute increasing amounts of its cash flow to investors, a first since the company emerged from bankruptcy years ago. The refinancing was made possible through a combination ACM of continuing debt reduction and improved earnings visibility thanks to the new federal ACAM funding mechanism.




*Close price adjusted for splits. **Adjusted close price adjusted for both dividends and splits.

| Share Information March 9 2018 | | | |
|---|---|---|---|
| **Market Cap.**<br>$49.5m | **P/E (TTM)**<br>4.3 | **EV/EBITDA**<br>5.3 | **Dividend Yield**<br>N/A |
| **Average Daily Volume**<br>11.8k | **P/B**<br>33 | **ROIC**<br>5.80% | **Debt to Assets**<br>72% |

**Between interest and tax savings, I expect the company to earn at least $3.25 per share in 2018. I also expect the company to pay down at least $10 million in debt and to initiate a dividend. The company's number of access line equivalents will likely continue to decline, but I expect the decline will be largely offset by increasing non-regulated revenue and ACAM income. Looking ahead, I expect one of two outcomes to occur. Either Otelco will begin to trade on its earnings and cash flows, or it will be acquired...Beginning in 2020, Otelco is permitted to distribute 50% of available cash flows as dividends, assuming leverage targets are met. Assuming my earnings targets are met, a 60% earnings payout ratio would mean a dividend of more than $2 per share.**

*As time goes on, Otelco will become a more and more attractive acquisition target. If the company can hold its annual EBITDA decline to 3%, its valuation on an EV/EBITDA basis will fall below 4.0 at some point in 2019.*

INTRODUCTION AND UPDATES

# DG Value: Contura Energy

We remain optimistic about our position in Contura Energy. The company recently paid a $9/share special dividend and completed a $50 million stock buyback through a Dutch auction tender process. In addition, Contura completed a sale of its non-core PRB thermal coal assets in December. Proceeds from the sale include a $50 million royalty stream, the realization of an estimated $425 million NOL, the extinguishment of approximately $115 million in legacy liabilities and $25 million in new unrestricted cash. The valuation of the sale represents a 9x valuation for the PRB business. Pro forma for the sale, Contura becomes more levered to its met coal operations (now nearly 70% of segment EBITDA).

*“Even after the price of Contura shares recently increased, the valuation remains attractive at approximately 2.5x EV/’18E EBITDA with a free cash flow yield in excess of 30% to the equity.*

As we look forward, we see a number of catalysts that can close the valuation gap including a renewed IPO process or up-listing on an exchange as the stock currently trades OTC. We also see the opportunity for Contura to participate in further M&A, with public peers trading in the 4-6x range, combined with the opportunity for substantial synergies. Finally, we expect the company to generate significant free cash flow, which will be used to pay down debt or deliver additional distributions to shareholders in the near term.

# Returns

| Edition | Fund | Ticker | Open Price | Date Pitched | Date Closed | Dividends | Current Price (1) (2) | Total Return |
|---|---|---|---|---|---|---|---|---|
| 1 | Foundary Capital | NYSEMKT:VISI | $7.60 | 1/28/2016 | 1/28/2017 | | $8.45 | 11.18% |
| | | NASDAQ:MRVC | $11.21 | 1/28/2016 | 1/28/2017 | | $8.15 | -27.30% |
| 2 | Stanphyl Capital | NASDAQ:MGCD | $5.94 | 3/28/2016 | 3/28/2017 | $0.70 | $8.30 | 51.52% |
| | | NASDAQ:LTRX | $0.90 | 3/28/2016 | 3/28/2017 | | $3.31 | 267.78% |
| | | NASDAQ:ELON | $5.77 | 3/28/2016 | 3/28/2017 | | $6.20 | 7.45% |
| | | NASDAQ:BWEN | $2.87 | 3/28/2016 | 3/28/2017 | | $7.25 | 152.61% |
| 3 | S&C Messina | NYSE:PRA | $51.47 | 06/21/16 | 06/21/17 | $1.24 | $60.15 | 19.27% |
| 4 | Hazelton Capital | NASDAQ:CUI | $5.99 | 09/23/16 | 09/22/17 | | $3.37 | -43.74% |
| | | NYSE:CPS | $106.03 | 09/23/16 | 09/25/17 | | $122.00 | 15.06% |
| 5 | Boyles Capital | LON:SYS1 | 500 | 10/07/16 | 10/07/17 | 45.60 | 537.00 | 16.52% |
| | | ATH:PLAT | €1.69 | 10/07/16 | 10/07/17 | | €2.60 | 53.85% |
| 6 | Livermore | CVE:JSE | $0.50 | 12/21/2016 | 12/21/2017 | | 0.41 | -18.00% |
| | BlueTower | NASDAQ:NICK | $11.10 | 12/21/2016 | 12/21/2017 | | 8.82 | -20.54% |
| | | NASDAQ:EZPW | $10.65 | 12/21/2016 | 12/21/2017 | | 12.30 | 15.49% |
| 7 | Arquitos Capital | NASDAQ:MMAC | $21.45 | 03/15/17 | 03/09/18 | | 28.00 | 30.54% |
| | | NASDAQ:MLNK (3) | $1.87 | 03/15/17 | 03/09/18 | | 2.40 | 28.34% |
| | Alluvial Capital | ASX:CZZ | $14.58 | 03/15/17 | 03/09/18 | 0.57 | 17.10 | 21.19% |
| | | TSE:CRH | $11.33 | 03/15/17 | 03/09/18 | | 3.90 | -65.58% |
| 8 | Verdad | TYO:4028 | ¥1,050 | 06/15/17 | | | ¥1,450 | 38.10% |
| | | TYO:9994 | ¥1,620 | 06/15/17 | | 20 | ¥3,295 | 104.63% |
| | GrizzlyRock | NYSE:RSO | 9.95 | 06/15/17 | | 0.2 | 9.67 | -0.80% |
| | | NYSE:VPG | 17.45 | 06/15/17 | | | 31.40 | 79.94% |

| Edition | Fund | Ticker | Open Price | Date Pitched | Date Closed | Dividends | Current Price (1) (2) | Total Return |
|---|---|---|---|---|---|---|---|---|
| 9 | Logos LP | NASDAQ: AAON | 34.85 | 09/29/17 | | 0.13 | 39.10 | 12.57% |
| | | NYSE: LXFT | 47.80 | 09/29/17 | | | 43.90 | -8.16% |
| | Dane Capital | NYSE: DSKE | 13.05 | 09/29/17 | | | 10.60 | -18.77% |
| | | NYSE: MX | 11.31 | 09/29/17 | | | 10.40 | -8.05% |
| 10 | Hayden Capital | ZO1:GR | €151.90 | 12/22/17 | | | €183.50 | 20.80% |
| | | NASDAQ: CACC | 325.00 | 12/22/17 | | | 337.00 | 3.69% |
| | Avenir Capital | HKG:0100 | 8.20 | 12/22/17 | | | 6.41 | -21.83% |
| | | NYSE: BBX | 7.90 | 12/22/17 | | | 9.21 | 16.58% |
| | | | | | | | Average return | 24.48% |

**(1) For closed positions this price is the price at time of close.**
**(2) Prices as of March 16**
**(3) Name changed to Steel Connect, Inc.**

# Total Compound Returns

| Total HVS Return* | MSCI World | Russell 2000 (Value) |
|---|---|---|
| 52.02% | 29.10% | 42.00% |

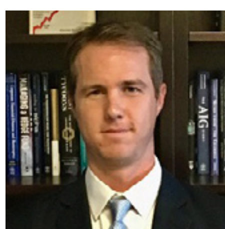
*Return is based on an equal investment in each position profiled and then rolled over at the end of the 12 month holding period.

INTERVIEW ONE:

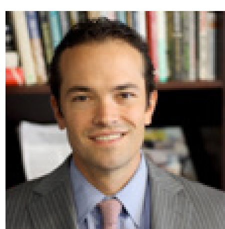
# Chad Cook, Joe Boskovich Sr., Brian Laks and Joe Boskovich Jr. **of Old West**

Chad Cook

Joe Boskovich Sr.



Brian Laks



Joe Boskovich Jr

## To start, could you tell our readers a little about Old West?

We started Old West in 2008, so we recently celebrated our nine-year anniversary. We launched with about $15 million under management, and we've steadily grown our business, mainly through word of mouth and today we are managing about $200 million in client assets.

The genesis of our process originated in the late 1970's when our CIO, my dad, Joe Boskovich Sr., was invited to serve on the board of a small Southern California-based regional bank. For several consecutive quarters, he observed the board Chairman ferociously buying stock in the bank, and he decided to start buying alongside him. Fast forward a few years, and the company was sold to Bank of America for many multiples of his original investment.

He learned a very valuable lesson from that experience, which is that you can never underestimate how much information is known to management that is unknown to everyone else. Although the bank Chairman had never expressed his intention to sell the bank, in hindsight, it was clearly his intention. This lesson is not only deeply ingrained in him, but also greatly informs our investment process: identifying smart owner/managers of companies with track records of success and then closely following their investment activity in the transactions of their own stock.

## So you've built your strategy around this lesson?

I think it would be more accurate to say that our strategy focuses on owner-manager run companies, and that following insider buying is a critical component of our process. Our process focuses on the people in control of our capital and their abilities to efficiently and effectively allocate that capital. As a first principle, we believe that the surest way to protect and grow our capital is by aligning ourselves with management teams who have high stock ownership and smart pay.

One of the first documents that we turn to is the proxy statement, and in the time that it takes us to print out the proxy, study stock ownership, pay levels and the business metrics that drive incentive pay, we are able to intelligently eliminate the vast majority of the potential companies that would otherwise absorb much of our time and resources. Simply, we seek to invest alongside great and proven owner/managers. The process by which business value will grow is a direct function of management's approach to capital allocation, so we also spend a lot of time studying management's historical actions, capital allocation decisions and track records, in an attempt to understand how they think about allocating capital.

As it relates specifically to insider buying and selling, I have found that

many of our best ideas are first sourced from Form 4 filings. We monitor every purchase or sale of stock by insiders, every day. If a CEO and/or several directors purchase millions of dollars of their own stock in the public markets, we will print out the proxy statement and SEC financials to determine if we too think it might be an attractive investment. Likewise, if we see insiders selling stock, it is oftentimes indicative of a situation to avoid.

## What sort of insider transactions are you looking for? Is there a size cut off below which you disregard?

We've spent more than 20 years analyzing insider trading and one of the things we have learned is that every situation is unique. Clearly the size of a transaction is meaningful, but to truly identify when insider buying and selling behavior is an important valuation signal you need understand a variety of factors, including an insider's transaction history, his or her compensation, SEC rules and regulations, and how instruments such as Rule 10b5-1 plans and trading windows work.

## Are you looking for CEOs who already own a significant stake in the business?

Definitely, and in these instances, we wouldn't necessarily expect an insider to make a significant open market purchase. That's why following Form 4 buys and sells is an important screening mechanism rather than driving our process. As mentioned, our process often begins with the work that we do on the Proxy Statement and understanding how management's total ownership position relates to net worth and compensation. It's important for us to see that management is largely incentivized and compensated by equity in their respective business.

## Could you give us an example of a recent investment?

Enphase Energy (ENPH) is a recent investment in the portfolio that was uncovered by my partner Brian Laks. Enphase has been a successful position thus far, and we believe that it still represents a great opportunity.

Enphase makes electrical equipment for the solar industry. When solar panels generate electricity, it has to be converted into alternating current before being fed into the grid. This was traditionally done with a central inverter, which is a piece of equipment that takes power from all of the panels as a group and then performs the conversion. A problem with this design is that there is a single point of failure, so if it needs to be repaired or replaced, the entire solar array goes down. Additionally, because the panels are strung together as a group, if any one of the panels has an issue, like too much shade or a malfunction, the entire system can be affected.

Enphase has a different approach to avoid this problem. Instead of a single piece of equipment, each panel receives its own microinverter that processes the conversion. Along with their energy management software, each individual panel can be monitored and operated remotely, which optimizes the output of the entire system. This improved design has seen very rapid adoption since it was introduced.

Quarterly revenue for the company had gone from $1 million in 2009 to over $100 million by 2014. Gross margins increased steadily from single digits to over 33%. The company was profitable, and it had a market cap of over $800 million. Then, in 2014, the solar industry went into a downturn, and falling energy prices made renewables less attractive. Increased competition among the panel makers, especially in China, caused massive supply increases that eroded prices throughout the value chain. Changes in regulatory policies added uncertainty into the market, which had initially been supported by subsidies and other incentives.

Enphase first came onto our radar in May 2016. The stock had fallen to $1.00 per share, the market cap was under $100 million, gross margins had fallen well into the teens, and there were big concerns about the company's survival. With sales levels significantly reduced, Enphase couldn't cover overhead and had to raise debt and equity just to stay afloat. As with any new idea, we always turn to the proxy to better understand insider ownership. Directors

and officers as a group owned over 25% of the company, which we found intriguing. We also saw that a number of notable funds had significant stakes, which we thought unusual for a company that was apparently circling the drain. As we started to study the company more closely, we were impressed that the company had shipped more than 15 million of their microinverters (3 gigawatts of installed power) in over 600,000 residential and commercial systems in 100 countries. Given the popularity of their products and what we saw as long-term tailwinds for renewable energy, we thought that if they could manage to get their costs under control, then the upside potential was pretty large. At that point, we decided to monitor the company and keep an eye out for any large insider transactions which might suggest that the people closest to the operation were gaining confidence in a recovery.

In January 2017, we saw just that. There was a large strategic investment from T.J. Rodgers, who was the Founder and former CEO of Cypress Semiconductor, and as part of his investment, he was appointed to the board of directors. Rodgers has a long history and iconic reputation in the technology industry. He founded Cypress in 1982 and grew it into a multibillion-dollar company before he retired in 2016. He also had experience in the solar industry as Chairman of SunPower during its IPO. Upon joining the Board, Rodgers brought in consultants from McKinsey who he had worked with in the past, and they started to grapple with some of these cost issues and essentially initiated a companywide restructuring.

Then, in April, they brought in another Cypress veteran to the newly created role of Chief Operating Officer. He had a 20-year career with Cypress, including five years as head of Cypress India. His first impression was that the company had great products but lacked a focus on costs. They did not have strong sourcing agreements (which were crucial given their average product contained over 300 components), costs were high for reasons related to warranties, servicing, and freight, and they lacked pricing discipline. To combat all these issues, the company adopted several lean manufacturing practices and accelerated their product development roadmap. They also began partnering with panel manufacturers to incorporate their microinverters directly into the panels themselves. These so-called AC modules reduce costs, simplify installation and give the company a steady high-volume demand.

These initiatives have already started bearing fruit. Gross margins bottomed below 13% and have risen to above 18%, which is the highest level in the last five quarters. Cash burn has been reduced, and the company has posted positive operating and free cash flow. Last August, the CEO stepped down, and the company announced that the successor would be named within weeks. We figured it would be the COO, particularly because they gave a short window for the search, and that guess turned out to be correct. After the announcement of his promotion to CEO, we had a conference call with him, the CFO and Director Rodgers, which gave us a lot of confidence. The newest version of their product, the IQ7, gives the company the ability to offer the same version of the product to all geographies, which further reduces the manufacturing cost, weight and number of components. By the end of 2018, the IQ8 will launch, which is the real blue-sky upside for this company because it’s the first product that can work in both weak-grid and off-grid environments. Surprisingly, most solar power systems only work in tandem with a functioning electricity grid. These so-called grid-tied systems don’t work in places where electricity coverage is spotty or nonexistent, so having a product that can work in those environments really increases the potential market size. During the call, the CEO cited India as an example. The government there has announced plans for 100 gigawatts of grid-tied solar capacity by 2022, of which 40 gigawatts is expected to come from rooftop solar. That’s a massive opportunity for Enphase given their annual run rate is slightly less than 1 gigawatt. The estimated off-grid demand is several additional hundreds of gigawatts.

We think the plan they have outlined to reach a 10% operating margin by the end of 2018 is achievable given the product roadmap and cost reduction initiatives they have put in place. At that rate, we found ourselves buying a company trading at less than five times forward earnings

before giving any credit to the revenue growth just mentioned. Enphase has had quite a run in the last few months as other investors are starting to realize this too, but we think there's still a good deal of upside ahead.

## Aside from insider transactions, what are the other factors you're looking for when analyzing a business?

A second and equally important consideration is valuation. At our core, we are value investors, so not only do we seek to invest in companies where management is among the largest shareholders and incentivized more from their stock ownership than they are from their compensation, but we also want to buy into those businesses at substantial discounts to our assessment of intrinsic value. With that said, it's often not enough to buy something just because it's cheap, so we also spend a lot of time trying to understand what will make a company's stock price appreciate. In general, cheap stocks are cheap for a reason, and there is little insight to gain from basic valuation screens using backward-looking data. As such, we try to identify situations where we believe we have unique insights or can identify catalysts that the market will eventually recognize.

## Are you prepared to overlook your insider dealing criteria if the stock is cheap enough?

No.

> *"We don't try and rationalize owning a company if management interests aren't aligned with shareholders. We always want to invest in companies where management teams are among the largest shareholders and are incentivized more from their stock ownership than from their compensation.*

## On that note, have you ever had any situations where the insider buying has not been a good indicator of value or any situation that has not worked out in your favor?

Of course, and that is why our Form 4 insider buying screen is just a starting point. Although insiders may know their business better than any outsider could, that doesn't mean that they are always right. We still need to build our own investment thesis based on our financial analysis and valuation and an in-depth study of the business at hand.

## Could you give an example?

Overseas Shipholding Group was a company that we bought several years ago because of large insider ownership and continued buying by the founding Recanati family and members of the board of directors. The company got caught off guard during the energy collapse several years ago and eventually filed for bankruptcy. When oil prices plummeted, shipping rates nosedived, and OSG couldn't survive the industry downturn. We sold our stake when it became apparent to us that a bankruptcy restructuring was in the company's future. OSG was run by an iconic shipping family, but the energy downturn was just too sharp and lasted too long. Had it not been for its excessive debt load, the company would have weathered the storm. When investing in commodity or commodity-related companies it's critical to focus on the balance sheet to make sure that a company isn't overleveraged if tough times hit, and that was definitely reinforced to us on this investment. Learning from your mistakes is an important part of becoming a successful investor, and I would say that we put more emphasis on balance sheet analysis today, in large part due to our OSG investment.

## And what's been your best success story following insiders?

Over the years, some of our most successful investments have been in businesses run by owner-managers and capital allocators with demonstrated track records. We've had success in several of the John Malone entities, and more recently have had success and are currently invested in several of the Howard Jonas/IDT spin-off businesses.

## Disclosures

Disclaimer: Any reference obtained from the documents posted on this containing references to products, process, or service does not constitute or imply an endorsement by ValueWalk LLC or its officers, directors or agents of the product, process, or service, or its producer or provider. The views and opinions expressed in this document do not necessarily state or reflect those of ValueWalk LLC.


# Know a friend who would like to subscribe to Hidden Value Stocks?

**If you know someone who might be interested in subscribing to Hidden Value Stocks, we offer a referral program.**

To sign up, click the button below or alternatively, send us an email at **support@valuewalk.com**

**Refer a Friend**

**If you want to learn more, please visit**
**WWW.hiddenvaluestocks.com**