



Michael D. Axel, CFA



Jacob D. Benedict, CFA



David J. Manger, CFA

AMI logged many miles in 2013 searching for investment opportunities. We've already chronicled trips this year to Los Angeles, Omaha, Indianapolis, Cleveland, New York City and several local farms. In this issue, we discuss our visits to a local waste facility, a local manufacturing plant, the nation's capital, and Chicago, as well as another trip to New York City. We hope you enjoy.

AMI Does Trash

Jacob had the opportunity to spend a morning with Gregg Walbridge and the folks at Earth First, a Fort Wayne waste disposal company founded in 2009. Gregg and his family previously owned National Serv-all, which was eventually sold to Republic Services, a national publicly-traded waste disposal company.

Trash seems right up our alley – it's a necessary service in a consolidated market that has historically exhibited strong pricing power. But Gregg's efforts in Fort Wayne show that there is room for upstarts. The increasing importance of recycling has allowed innovative folks like Earth First to build trash businesses without the ownership of a major landfill by effectively sorting and selling waste. That's not to say the endeavor is easy – operating a profitable waste enterprise requires local scale and concentration, which is hard to build – but it does create some concern around the value of landfills, which have existed as the key "economic moat" for waste refuse companies for years. Waste volume has been under pressure since 2007, negatively impacting pricing trends. It's also worth considering the doomsday scenario where landfills don't get much use at some point in the future – in that case, landfill operators could be on the hook for large environmental clean-up costs. We recently completed a research project on an operator of trash burning waste-to-energy facilities and while we passed on the investment, it was another interesting lens through which to view the waste industry.

This isn't to say the major waste companies won't operate profitably for some time to come. But their growth could be constrained. In any event, we don't see much opportunity given their current stock prices. But it's an interesting industry to study further though. Meeting with people like Gregg also gives us the chance to discuss ancillary topics, such as the potential for large truck operators to convert their fleets to natural gas, which could have a positive benefit on some of our industrial investments.



Jacob checks out Earth First's recycling and transfer facility, brought online in 2013.

Stock Speed Dating

Jacob and David traveled to Chicago for three days to attend an industrial stock investment conference. The event is analogous to stock speed dating – executives from over 100 companies came and gave 25 minute presentations on their businesses, their industries and their outlooks. This specific conference was focused solely on industrial companies (much to David's excitement – he likes companies that build “machines and stuff”). After each presentation, the management teams retire to “break-out rooms” for another 25 minutes where analysts have a chance to drill into deeper and more controversial issues. This is where we tried to focus our time.

Three of the stocks that we currently own presented at the conference, and we had a chance to visit with each management team to go over our investment thesis and hunt for any unexpected or unforeseen risks. We also had a chance to get a general feel for the overall economic environment (slow and steady continues to be the mantra, although international markets are tough) and screen for new investment ideas. We came back with a handful of exciting ideas that we are working through now. We'd love to get past the “courting” phase with a new stock, but we're a very picky dater.

On the Shop Floor

Chuck Drerup and Tom Walterhouse of Reliable Production Machining and Welding were kind enough to spend some time with us to talk about their end markets and how their business is looking going into 2014. Reliable supplies several major industrial companies, so it was a great opportunity to learn more about how their customers operate and interact with suppliers. We also had a chance to gauge the health of end markets in areas from construction equipment to boats to agriculture. Reliable operates in tough, competitive markets, so they have to run as efficiently as possible. We also took the chance to ask Chuck and Tom about some of their suppliers and cost inflation trends in the Chinese sourcing market.

Mike Goes to DC

Mike recently attended an investment conference in Washington D.C. While most of the sessions focused on investment management, you can't attend a conference in D.C. without hearing one or two major political figures weigh in on the current political landscape. As we've stated before, it is hard to incorporate political speculation into our bottoms-up investment analysis, but we wanted to share what Mike got to hear. The conference's political speakers included recently retired Senator Olympia Snow and former Secretary of Defense Leon Panetta. Given their recent retirements from political office they both offered a very frank take on the current state of affairs (or lack thereof) in Washington.

Both observed that the current environment in Washington is as negative and dysfunctional as it has been in 50 years. They pointed to the lack of leadership in both parties as big contributing factors. Secretary Panetta noted that when he was serving in Congress, President Reagan and Tip O'Neill frequently dined together. During one episode of intense budget negotiations (not unlike today), President Reagan told O'Neill and Congressional leaders on both sides to go into a room and "don't come out until you have a deal!" Everything was on the table.

Senator Snow noted that when she came to Washington in 1979 it was "Country, State and Party," in that order. Today the order has been reversed. She believes a big problem with today's Congress is the adoption of a three day work week. Many members now fly out on Friday and back on Monday, leaving little time for major policy work. There is not enough time to get to know the other members of Congress, making it easier to attack colleagues. This has contributed to the negative tone that plays well to the sound bite hungry, 24/7 news media.

Redistricting of Congressional Districts was another problem mentioned by both politicians. Snow stated that as little as 35 out of the 435 Congressional seats are “in play” in the upcoming election.



Mike in front of the White House. We hoped he could find time to fix the U.S. Budget, but unfortunately he was too busy.

The large number of “safe” Republican and Democratic seats has led to more politicians moving to the extreme left or right, making it harder to find common ground. The 100% purity test being pushed by the GOP limits the party's appeal to moderate voters and shrinks the party's tent, according to Snow. President Reagan, she argued, used to focus on the 80% the country agreed upon and ignored the 20% we disagreed on.

Secretary Panetta summed it up as follows, "If our soldiers are willing to put their lives on the line to defend this country, then our politicians owe it to us to have the courage to make the hard decisions to put the country's best interest ahead of their own political goals." America has always risen to the occasion and it will again. We need party leaders who will work together.

David Heads to the Big Apple

David spent several days in New York City where he had the opportunity to meet one-on-one with an activist hedge fund that manages over \$10 billion and currently serves as a partner to AMI. The fund focuses on investing in a handful of high quality businesses where there are opportunities for structural changes that will serve as a catalyst for the company's stock price. David took the opportunity to drill down into the fund's thesis for its investment in a leading global consumer products company – it's safe to assume you've used the company's detergent, toothpaste, or razors at some point. As we've mentioned previously, because we perform our own research on individual companies, we think we bring an added level of insight to the table when discussing investments with our partners. The fund's analyst highlighted that their much debated view on the potential profitability of the company's branded products was based on numerous conversations with private-label manufactures (i.e. “knockoff brands”). These conversations provided insight into a minimum level of profitability the company should generate given the strength of its brands. Strong brands typically allow companies to increase prices without losing customers, generating a lot of shareholder value. Since making the initial investment earlier this year, the fund's thesis has gained traction. The CEO was forced to resign after the company's board of directors acknowledged the fund's view that the company had underperformed for an extended period of time. With a new CEO at the helm, the company's results have improved, much to the benefit of the fund. That said, things don't always go this smoothly in investing. To keep this idea top-of-mind, the fund showcases a seat from a fighter jet in its conference room to symbolize that in public markets you can always hit the “eject button.”



During his time in New York, David also attended a CFA conference that featured presentations from renowned academics and industry experts on topics such as behavioral biases in stock valuation, potential implications of tax reform, and the changing regulatory landscape for global banks. Far from your leisurely topics, some people may consider these presentations a recipe for a nap. At the risk of portraying ourselves as complete geeks (assuming you haven't already formed that conclusion), we actually find these topics insightful and thought provoking. For example, the presentation on tax reform highlighted potential changes to the treatment of depreciation expense that could impact how we value certain companies. This type of information is a valuable input into our research on individual stocks and investment managers.

A fighter jet seat in the conference room of the hedge fund David visited, which serves as a reminder that investors in public stocks can always hit the “eject button.”