

LSGI Advisors Report

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Art's Way Manufacturing Co. (ARTW) Annual Shareholder Meeting

Last month LSGI Fund holding Lindsay Corporation (LNN), a provider of irrigation systems and infrastructure products, announced that second quarter revenues decreased 40 percent from the prior year period. The Lindsay CEO noted that “general economic conditions and agricultural commodity prices remained unfavorable during the quarter adversely affecting the willingness of farmers to make investments in capital goods.” He did not expect demand to recover in 2009.

The CEO of Potash Corporation (POT) (not a LSGI Fund holding) also made a comment last month about the lack of demand for potash so far this year. He expressed concerns that if farmers failed to apply the requisite amount of fertilizer the yields might be disappointing, which may support higher grain prices later this summer.

Coupled with the continuing slowdown in the retail, real estate, manufacturing, and banking sector, we decided to attend our first shareholder meeting for the LSGI Fund in a decade to gauge first hand the health of the agricultural sector and Art's Way Manufacturing Co.

The shareholder meeting was well done. Held in the company offices in rural Armstrong, Iowa (population 979) we may have been the first institutional analyst to ever attend an Art's Way shareholder meeting. Four other shareholders were present, all small individual investors. The LSGI Fund owns 3.2% of the company, and we hold additional shares in other accounts we manage.

There were no surprises at the meeting. From our discussions with management, board members, company employees, and fellow shareholders we came away with the following impressions:

- Management appears to be relatively confident that the company will grow revenues this year. The Auger division shipped its' first product last week – a month ahead of schedule. Orders and interest in the auger product continue to grow. The Vessels division has seen slow growth, from almost nothing last year, but it is expected they will begin to become more viable in their new building. Sales from the Vessels group this quarter is expected to be the best in two years.

Interest in the modular scientific laboratories has skyrocketed with the Obama stimulus plan. Projects bid several years ago



but never funded by state or federal governments are being re-submitted as stimulus funds become available for these projects. The swine flu may also increase interest in these products as the modular labs can be operational in one-half the time, at two-thirds the cost, of a traditional lab. And they are transportable to anywhere in the country and possibly overseas. The two latest ARTW projects are being installed at Texas A&M University and the University of Virginia.

- With regard to profitability, the company is still working its way through the high cost steel purchased last summer. Margins should improve now that the Miller Pro products promised at historical prices have been delivered. Company employee levels have declined slightly from earlier levels. The company is also exploring in-sourcing some products now being purchased elsewhere unless the suppliers cut their prices.

We think the company may cut its' dividend to preserve cash for operational and corporate expansion purposes. We noted the fact that it is unusual for a company the size of ARTW to offer a dividend and did not think such a cut will have a major impact on the stock price. The company appears to be committed to telling its story to potential investors with conference calls and an updated website.

- Diversification of ARTW product offerings should be a real plus in this economy. The demand for agricultural equipment is not as robust as it has been in the past, however it has not fallen off the cliff either. The farm economy is still viable and for the most part strong. Local farmland has not gone up in price in the last year but has not fallen in value either. Grain prices might be below year ago levels but futures prices are still well above those of several years ago, which should support activity.

- The management team has been substantially strengthened over the last several years. Gene Tonne has been named the new production manager at the Armstrong plant. We were told by another shareholder who toured the plant several years ago that the difference in the plant efficiency was like night and day – Tonne has done wonders with regard to increasing the efficiency of the production process which ultimately will be reflected in the bottom line. The plant appeared to be staffed with well trained and highly skilled tradesmen who were producing quality farming equipment.

- The plant has been upgraded over the last several years with laser and plasma computerized steel cutting machines that increase accuracy and efficiency while reducing waste. The new paint booth used a powdered paint formulation that was attracted to the metal surface by an electrostatic charge than fused onto the metal. The process is very environmentally friendly, and the final product looked impressive. The older paint spraying facility was still in use. The company had also just completed an enclosed storage area running the entire length of the building.



- When you have a small, closely held company, in a small rural town, the ability to attract quality directors to the Board of Directors can be an issue. In many cases these boards will lack depth, or expertise. We had a chance to visit with all seven ARTW Board members and were impressed with the various expertise they bring to the table and the experience they have in the manufacturing sector. We are also pleased at the amount of stock held by the directors as a group.
- Both the auditors and legal counsel from Minneapolis were present for the meeting. One of the concerns we always have with small firms is the fact that the cost of compliance with the increasing requirements of being a public company will impact the bottom line – the question is how to best manage these costs. If ARTW continues to grow their assorted businesses we think these costs will not be a major impediment in the immediate future.

Fortune magazine called us two weeks ago about Art's Way. They are preparing a potential follow up article for the Fortune Small Business 100 list for 2009 and asked for our comments.

