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THE WALL STREET TRANSCRIPT

Questioning Market Leaders For Long Term Investors

Investing in Underfollowed Small Cap Stocks

ARNOLD URSANER started CJS Securities, Inc., in 1997, named after his three children, and it has grown to 10 analysts. Clients of CJS include leading institutional mutual funds, banks and investment advisors. He has over 30 years of brokerage industry experience. Before starting CJS, he worked at Bear Stearns as a Managing Director in Equity Capital Markets, responsible for the marketing and distribution of IPOs and follow-on transactions. Earlier in his career, he was in institutional sales at Smith Barney, and then First Boston. CJS Securities has enjoyed growing recognition. Mr. Ursaner received the 2002 Nasdaq-Starmine Analyst Award for Top Stock Picker in Commercial Services and Supplies. In 2003, he received the "Best of Wall Street" Award, given out by the Wall Street Journal, for general industrial services. Institutional Investor magazine, arguably the top publication for professionals in the industry, presents its Home Run Hitters Award for analysts who had some of the top performing ideas for the previous year. In 2003, it recognized CJS for having two of the top five small-cap ideas of 2002. For relaxation, Mr. Ursaner is an avid golfer.

(ZBS503) TWST: Would you give us a brief background on CJS Securities and an overview of your investment philosophy?

Mr. Ursaner: Our firm was founded eight years ago and from that time continuing to the present our focus has been on small cap ideas that, for various reasons, may have slipped through the cracks on Wall Street. We have three criteria that must be met for us to consider a name. One is that the company must initially be a small cap. Two, we have to be confident we can add value in terms of the research coverage and, finally, we want our clients to have a reasonable chance of making money.

Beyond the must-have criteria we look for quality businesses where there is typically little if any industry analyst coverage, stocks that are misunderstood or misperceived perhaps due to changes that have distorted reported financials and caused the stock to not screen well, challenging stories turning into good stories, good stories turning into excellent stories, or any positive delta that may not be reflected in the stock market, such as disposing of a problematic subsidiary. That's where we're trying to go.

TWST: Are you looking for niche players that have fallen through the cracks, that are dominant within a small area?

Mr. Ursaner: Frequently that's where our work will lead us. Many of our companies are clear market leaders in a small niche where there may be specific barriers to new entrants or it may be a narrow enough market where another company trying to enter the space would have difficulty gaining enough market share to make it worthwhile. Another thing we find is that many of the companies we keep an eye on don't fit into the natural industry categories. In other words, companies like **Paxar** (PXR), which is a dominant company in label manufacturing, or **Quixote** (QUIX), which is a dominant provider of crash barrier cushions, don't tend to fit easily under industry analyst coverage very often.

TWST: What is the investment climate like for these underfollowed small cap stocks at this time?

Mr. Ursaner: It's actually very, very positive for a number of reasons. One of the drivers for the small cap segment is that even though many of the largest funds have been closed to new investors for years, they're continuing to get significant inflows of new money from existing investors. Let me give you a specific example. The T. Rowe Price Value Fund has been closed to new investors since 2002. Since that time, although closed, its assets have grown from $2 billion to over $5 billion. That dynamic creates constant demand for new ideas.

There are two other major drivers of demand for small cap stocks currently. The new ETFs (exchange traded funds) have become sizable buyers of small cap names. The final factor is the growth of the hedge fund community. In what is generally expected to be a flattish environment for larger cap names, funds are able to get significantly better performance by targeting smaller cap ideas, so we see increasing demand for our product from these funds.

TWST: I assume it doesn't make sense for the larger brokerage firms to focus on these small cap stocks unless they can get investment banking.

Mr. Ursaner: It's a catch-22. If a firm is providing research only because it's hoping to win investment banking, it's not viewed as independent research. The research has traditionally been viewed as having a positive bias. It is interesting to note that investment banks have little if any influence on the research. We have seen examples where a banking firm initiating research coverage will have a negative opinion and a target price below where the investment bank priced the transaction. To me that has to send a confusing signal to the client.

TWST: Has there been growth in independent firms that are looking for these type of stocks?

Mr. Ursaner: We've seen a dramatic change in the competitive environment for small cap research. There are an increasing number of independent firms targeting this space.

TWST: What do you mean by small cap? Does it go down into micro cap?

Mr. Ursaner: It's a constantly changing definition. Most of our clients today define small cap as being anything contained within the Russell 2000. But there has been a lot of blending of these numbers. We're also seeing specific micro-cap funds, which are basically market caps under $500 million, and nano-cap funds, which are under $250 million. So you're really seeing an increasing differentiation even within the small cap arena, out of necessity. The problem we have is that unless a money manager intends to file a 13-D on nearly every position he owns, it's almost a necessity to move up the market cap curve. In any case, clients will not sell winners that grow larger in market cap unless they run the risk of style drift issues from the consultants.

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TWST: Would you tell us about your research team, which must be essential to your finding these stocks that you're discussing and it probably differentiates you from the competition.

Mr. Ursaner: We are a team of nine professionals with varying levels of experience. They range from someone like me with an excess of 25 years' experience down to college graduates with three years or less of experience. The most senior analysts on my staff joined me from the buy side. They had experience as money managers in small cap. We've also had to train people out of business school, so it's a mix of different levels of experience.

Robert Labick functions as my formal Director of Research. He has a very hands-on approach to the product. It's very research-intensive, to the extent that there's a differentiation between ourselves and some of the other firms we compete with directly. We tend to do fewer names, but we try to do them in a lot more detail and really drill down to both the key elements of the story and the financial modeling. It's just a different level of intensity that I would argue is one of the differentiating factors in our product. We tend to function as the screen by doing fewer names in greater detail rather than providing six page reports on a larger number of names to our clients. We're trying to do more detailed work, more thorough work and be more selective in our names.

TWST: Where do you go to find these ideas and what is your decision-making process involves?

Mr. Ursaner: Ideas come to us from a multitude of sources. We have found that the best sources of ideas are our clients. Once they have established a position in a company that is underfollowed or misunderstood, they're anxious to have us pick up coverage. We are viewed as a good source of research that will fairly lay out a balanced story so this can be a win/win situation.

The second source for ideas is top-tier investor relations firms. We understand they're being paid by clients to get in front of us, so we have a challenging screen to eliminate the firms that don't demonstrate reasonable selectivity.

A third way we find ideas is simply experience. I've been involved with stocks for 25 years and you always have names on an informal watch list. Sometimes it's a competitor to a name that we're interested in. For example, if we are following an aggregate company, we typically will find a competitor interested in explaining to us why their company may be better at what they're doing. We've had a number of examples where we initiated on a single company and were almost immediately contacted by a competitor, and in several cases, we broadened our coverage.

Our overall screening process is pretty straightforward. We start by looking at the market cap, to be sure it's the right size. We look at current ownership of the stock, to see if there has been shift from value to growth clients or vice versa. Some of our most interesting names are owned by both types of firms. What did the stock do over the last year or so? If it was dramatically higher or dramatically lower, we attempt to identify what caused that performance. We like to ask, "Was the issue investor expectations or some material business change?" Another great place to find attractive ideas is carve-outs from larger companies.

An excellent example that we recently initiated coverage on is **ACCO Brands** (ABD), which was a carve-out of **Fortune Brands** (FO). **Fortune Brands** was a Fortune 500 company and all of a sudden their shareholders, which are large cap or index funds, inherit a small cap position with complex financials, minimal coverage and short-term uncertainties. This combination can lead to volatility and opportunity for our clients.

Another thing we look for, which may be a competitive advantage for us, is for stocks that don't screen very well. Most of Wall Street is extremely busy and some firms have moments when they're lazy. An organization may run a basic screen but will almost never attempt to really go through the numbers to identify why a stock may not screen well. If you're doing simplistic screens, you're not going to capture some of the most attractive ideas because it may involve a simple financial or write-off issue that traditional Wall Street screens would not catch.

"We have been successful with some theme-oriented research. For example, in 2005 we had a theme related to suppliers to commercial aviation. We identified a pickup occurring in commercial aviation in the number of hours planes were flying, utilization, and yield and found a handful of different small cap names that would benefit from this pickup in demand."

TWST: What about financials? What are you looking for there?

Mr. Ursaner: We find that in many cases our companies are self-financed and that's why they don't attract Wall Street attention. They just run their businesses. If you have a company that constantly needs to raise capital, while there's clearly a separation between investment banking and research, you will find analysts at those banking firms following those types of companies hoping to be involved in the next transaction.

In our case, most of our companies generate excess free cash flow and have underlevered balance sheets, in many cases in a net cash position. They focus on managing and growing their business. They're independently run and self-financed. A large number of our companies fit that criterion.

TWST: Do you look for niche areas because there are certain industries where you couldn't add enough value?

Mr. Ursaner: There are several industries we have chosen not to pursue because as generalists, we believe we would not add sufficient value. To be very specific, we don't do anything in the oil and gas area because you need to know the industry. We don't do anything in the financial area because you need specialized accounting skills, so we don't follow insurance or bank stocks. We've generally stayed away from the technology sector, again because while there are interesting things happening in the industry, we have chosen to allocate our limited resources where we can add value.

We have found that if we pick up a small name, for example, in the semiconductor industry, when a money manager is prepared to make a decision on that name, more often than not, even though we may be the only person on the particular company, he will frequently go to an industry analyst, so we lose the competitive advantage.

We have been successful with some theme-oriented research. For example, in 2005 we had a theme related to suppliers to commercial aviation. We identified a pickup occurring in commercial aviation in the number of hours planes were flying, utilization and yield and found a handful of different small cap names that would benefit from this pickup in demand. Another example of theme-oriented research has been the highway construction bill, going back to TEA-21, the previous bill. Another major theme of our firm has been outsourcing. We are convinced this is a trend that is not going away. Most companies we deal with are looking to find expertise outside rather than spending sums in house for non-core competencies.

TWST: What are some of your favorite names, either currently or names that have worked for you in the past?

Mr. Ursaner: I'm asked that question by clients almost every day and I always struggle with it because it's like asking me to choose among my children, in a manner of speaking. One of our best successes over the last two years has been the aggregate space and two names that have been terrific ideas for us have been **Martin Marietta Materials** (MLM) and **Florida Rock** (FRK). In both cases, there's a dramatic secular trend change under way that we believe will continue for several years; specifically, that's the ability to develop an aggregate property. The environmental and permitting issues to develop a new property have gotten dramatically more difficult at the same time that the demand for the product is escalating. That has led to the best pricing environment for aggregates in over 30 years and it is manifest in that traditionally, prices would go up in the low to mid single digits once a year. In 2005, we saw double-digit price increases twice in the course of the year and the industry basically is alerting its clients to expect twice-a-year price increases for the foreseeable future. The barriers to new entry are just enormous and there is no substitute product. This trend change should last for several years to come.

"Kaman Corp. is a leading provider of aerostructures and self-lubricating bearings used in the aerospace industry. We also have been involved with HEICO Corp., which is a dominant provider of PMA parts. We also like Hawk Corp., which is a provider of friction products used in brake linings, and AAR Corp., which is a distributor of parts."

1-Year Daily Chart of Kaman

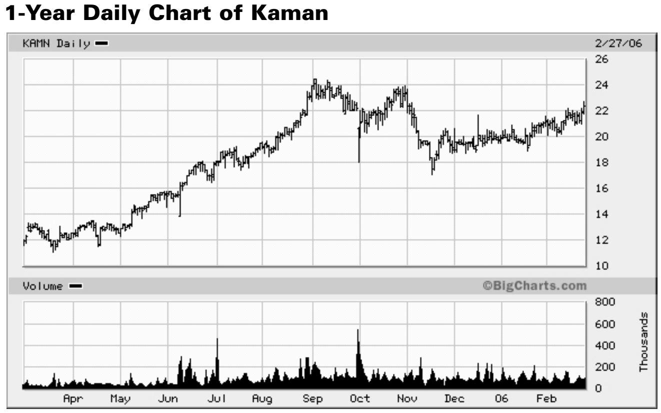

Chart provided by www.BigCharts.com

Another place I mentioned was suppliers to commercial aviation. One of the more interesting names within that space would be **Kaman Corp.** (KAMN). They're a leading provider of aerostructures and self-lubricating bearings used in the aerospace industry. We also have been involved with **HEICO Corp.** (HEI), which is a dominant provider of PMA parts. We also like **Hawk Corp.** (HWK), which is a provider of friction products used in brake linings, and **AAR Corp.** (AIR), which is a distributor of parts, so we have several names within that theme. Again, our view of the commercial aviation cycle is that it has several years ahead of it. We don't view it as a short-term cycle.

And then again, most of the other names are going to be smaller names. I would highlight **ACCO Brands**, which we just initiated on. It was a carve-out from **Fortune Brands** and did a simultaneous merger with General Building I think that illustrates what we look for at CJS. They have absolute brand dominance. 85% of their products are either number one or number two in the office products category. These are products you and I use every day, such as Swingline staplers and Day-Timers. They're very well known, branded products. The challenge for Wall Street was, because it was a carve-out and a simultaneous merger, the company was unable to even provide pro forma numbers until mid-February, so investors had to make decisions with limited financial information, which we view as a positive.

The other driver of that story is outstanding management. The team that's running **ACCO Brands** has proven success running two other public companies, demonstrating their ability to turn around complex operations. We think it's extremely likely this team will be successful in this effort.

TWST: Is a lot of your research focused on management performance and execution?

Mr. Ursaner: In small cap, management is probably more critical than in larger companies. We look for executives whose financial incentives are performance-driven and aligned with public shareholders. We like to see a lot of skin in the game and don't like cronyism on the Board, super voting shares or glaring nepotism. We really dislike executives who, despite the fact they may own significant shares, award themselves a disproportionate share of available options. Compensation overall should be modest; if they own enough shares that rise in price, that's how we want them to create wealth.

TWST: What makes you decide to remove a company?

Mr. Ursaner: There are several reasons. The absolute best way is when one of our names is acquired at a premium. We never count on an acquisition when we initiate on a name but it sometimes enables our price target to be reached in a shorter time frame.

The second reason is that the company has grown to the point where we believe we have little if any competitive advantage. For example, we recently dropped four of our best names because they had become mid-cap names with eight to 10 analysts covering the name. For example, we dropped **R.H Donnelley** (RHD), which we had followed since 1999. At that time it was a complex carve-out and there was no other public Yellow Pages company. RHD is now a $4.2 billion market cap followed by nine industry analysts.

The third reason for dropping a name is the worst one, the realization that we just made a mistake. We may have misunderstood the business or management's goals and no longer have strong conviction or confidence in the story, or management hasn't executed as we had hoped. In the past, we have been a little too patient putting names in this category.

TWST: The merger and acquisition outlook for 2006 seems to be pretty good. That plays well into your line of thinking, I'm sure.

Mr. Ursaner: I would agree. Again, what's interesting is many of our companies can be the target for a larger company or they might be the acquirer of smaller, private companies. In many cases, our companies can be either buyers or sellers. A significant change we see happening now is aggressive hedge funds and venture funds are increasingly competing with strategic buyers for these companies. If I were to look out over the next 18-24 months, I think it's more likely that many of our companies will be acquired by private venture firms rather than strategic buyers, because they have massive amounts of funds to invest.

"You cannot be in the business of providing small cap research to institutions and not provide clients access to managements. Most small company managements understand this. They allocate a certain number of days every quarter to get out on the road. We're seeing increasing numbers of conferences."

TWST: Do you ever recommend a stock because you think it will be acquired?

Mr. Ursaner: We never will make that a sole basis for a recommendation. We're very comfortable making recommendations strictly on fundamentals, but beyond that, if an acquisition were to occur, the stock might realize value in a shorter time frame, but we would never specifically recommend a stock for a takeover. Remember, takeovers are usually driven because of the positive performance of a company.

TWST: What is your distribution like?

Mr. Ursaner: We distribute our product electronically, through e-mail. We use a service that enables us to hit a single button and distribute to our entire private client base list simultaneously. In addition, we also use electronic services (First Call, specifically) where our product is available. But again, we choose to severely limit access to our product. We have to entitle someone to receive it on First Call. We do not view our product as a commodity and don't treat it like one.

for the entire industry is that at the same time this dynamic is occurring, the overall commissions have been shrinking as rates have been declining.

The biggest issue independent firms will grapple with over the next year or two is the concept of unbundling. We are not very concerned about it. If people really want to unbundle research from the execution capability, we will either get paid fairly for our research or, if not, we will charge a hard dollar fee and get paid that way. But it is clearly a major concern and trend issue we are focused on.

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TWST: Tell us about your clients and their demands. Are these demands changing over time?

Mr. Ursaner: The client base in small cap in general has gone through a pretty significant change. Our core client base has been and remains the small cap money manager within a larger organization. They remain our bread and butter accounts.

Because of what I said before about increasing performance orientation in the hedge fund and the inability to get outsized performance in larger names, we increasingly are being asked to provide our product to smaller hedge funds and it's a challenge because it generally does not fit our longer term orientation, but that's where the growth in the industry is occurring, so over the last two or three years, to the extent that there's a change in our mix, we continue to focus on long-only money managers but are increasingly being asked for our product by the smaller hedge funds and we grapple with how broad our distribution should be.

We have limited distribution today and we will not take on an account for what we call a one-off. If someone calls and is specifically interested in just a single name, we will not take them on as a client. Rather, we're focused on quality relationships.

The other trend I've seen over the last few years is that our best clients are trying to focus more on their revenues with us so that they get better attention and better service. Offsetting this

1-Year Daily Chart of ACCO Brands

Chart provided by www.BigCharts.com

TWST: Do clients want direct access to the management of these companies and is this the way you arrange your conferences?

Mr. Ursaner: It is essential. You cannot be in the business of providing small cap research to institutions and not provide clients access to managements. Most small company managements understand this. They allocate a certain number of days every quarter to get out on the road. We're seeing increasing numbers of conferences. I think if you're a small cap money manager, you can literally go to one or two conferences every single week and as I said, it's absolutely essential. You can't be in business and not do that. We try very hard to differentiate our conferences by deliberately keeping them smaller, not allowing companies to deliver their canned pitches but rather focus on strategic issues, and by customizing clients days.

TWST: You have a unique business at CJS Securities. Do you have any summary statement to wrap things up?

Mr. Ursaner: There are two challenges in running a small cap sellside brokerage firm today. One is the regulatory environment/cost. The regulatory costs are astronomical and the complexity, the amount of time that has to be allocated for this is almost overwhelming. It's one change that it's really difficult to manage through.

The second biggest issue is because the economic model of the hedge funds is so different from the brokerage business, it's increasingly difficult to keep quality people. I've lost three very high quality people in the last year, two to hedge funds, where they became partners, and the third to a commodity firm. That is an increasing challenge that I will have to manage through on a go-forward basis. It's very difficult.

Having said that, we really enjoy what we do and there is still a tremendous feeling when we find a new name that excites us and our clients.

TWST: Thank you.

Note: Opinions and recommendations are as of 2/27/06.

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