

### Acme United Corp. (ACU)

Company Report – November 5, 2016

Acme United Corporation is a worldwide supplier of cutting devices, measuring instruments and first-aid products for school, home, office, industrial and hardware use.

Acme’s sales in the third quarter, ended September 30, 2016, were \$31.9 million, up 7% compared with the same period last year. Net income for Q3 2016 was \$1.5 million, or \$0.40 per share, a strong increase of 22% in net income and 21% in EPS.

Especially Westcott, the school, home and office products brand, continued to outperform. This year had the best back-to-school performance in the Company’s history. Another strong performer was the first aid business, which gained market share in the industrial and food service segments. There are now SmartCompliance kits in thousands of restaurants in the US. And earlier this year, Wal-Mart equipped each store, warehouse, office, and truck with a first aid kit from Acme United.

Acme United’s brands excel across the board, which lays the groundwork for continued growth in 2017. Acme’s Chairman and CEO, Walter C. Johnsen mentioned during the third quarter conference call that it was a bit too soon for exact projections, but he expects a continued strong performance for the Company.

Based on our outlook and calculations, we reiterate our buy recommendation for Acme United Corp. with a price target of \$30.81, which is 44% above today’s stock price.



- For the second quarter in a row, Acme United increased its sales and earnings guidance for 2016. Thanks to an outstanding performance of all its brands in the first nine months of the year, the Company now expects to generate revenues of \$124 million and earnings per share of \$1.63 in 2016. This is up from the original forecast of \$120 million in revenues and earnings per share of \$1.47.
- The Company continues to execute very well. Distribution is gained both online and off, gross margins are above 35%, the balance sheet is very healthy, and the dividend is increased every six to eight quarters.
- On top of that, Mr. Johnsen again indicated that the Company will be looking for more accretive acquisition candidates in 2017.



Market Data	
Price	\$21.40
Sector	Office Supplies
52-Week Price Range	\$13.01 - \$22.19
Shares Issued (m)	3.58
Market Cap (m)	\$77.92
Listings	ACU (NYSE Mkt)
Website	<a href="http://www.acmeunited.com">http://www.acmeunited.com</a>

## THE COMPANY

Acme United Corporation is a supplier of cutting, measuring and safety products for the school, home, office, outdoors, fishing, hardware, and industrial markets. Its principal products are scissors, shears, rulers, pencil sharpeners, knives and first aid kits.

The Company's products are organized under eight brands: Westcott, Clauss, Camillus, PhysiciansCare, Pac-Kit, First Aid Only, Cuda and DMT. Both the number of products offered under these brands, as well as the number of physical and online stores where these products are available, continue to grow.

For the second quarter in a row, Acme United increased its sales and earnings guidance for 2016. Thanks to an outstanding performance of all its brands in the first nine months of the year, the Company now expects to generate revenues of \$124 million and earnings per share of \$1.63 in 2016. This is up from the original forecast of \$120 million in revenues and earnings per share of \$1.47.

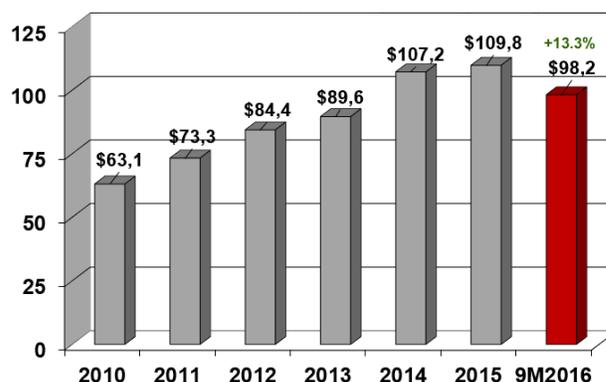
Sales in the third quarter, ended September 30, 2016, reached \$31.9 million, up 7% compared with sales of \$29.9 million in the third quarter of last year. Net income for the quarter ended September 30, 2016 was \$1.5 million, or \$0.40 per diluted share, compared to \$1.2 million, or \$0.33 per diluted share, for the 2015 period, a strong increase of 22% in net income and 21% in earnings per share.

Especially Westcott, the school, home and office products brand, continued to outperform. In fact, this year had the best back-to-school performance in the Company's history. The brand again gained market share in the scissors and pencil sharpeners categories. And its ceramic box openers were an instant success.

Another strong performer was the first aid business, which continued to gain market share, particularly in the industrial and food service segments. For example, there are now SmartCompliance kits in thousands of restaurants in the United States. And earlier this year, Wal-Mart equipped each store,

warehouse, office, and truck with a first aid kit from Acme United. An added bonus to first aid sales is that they're recurrent as products have to be reordered so that supplies never run out.

**As for 2017, Acme's Chairman and CEO Walter C. Johnsen mentioned during the third quarter conference call that it was a bit too soon for exact projections, but he expects a continued strong performance for the Company.**

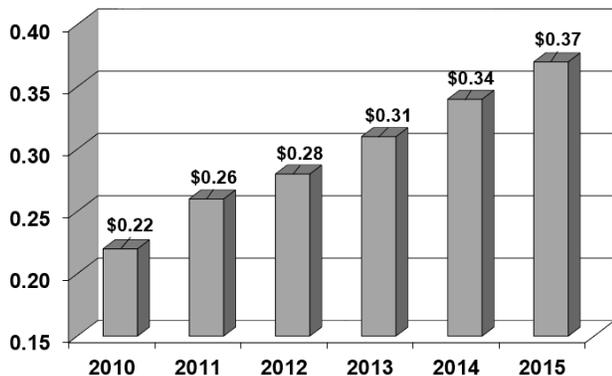


**Acme United's annual sales (in million USD). Sales for the first nine months of 2016 are up 13.3% compared with the same period last year.**

Acme United succeeds in re-inventing everyday products such as scissors, knives and school and office items by applying new and improved materials to them. For example, the blades on many of the Company's products have a titanium carbonitride coating, making them more than three times harder than stainless steel. Or blades get a non-stick coating, making them useful in difficult environments like the floral area for cutting and trimming flowers and bushes, or in the arts and crafts area, where lots of glue and paste is used. Also, some school and office products have Microban antimicrobial protection added during the manufacturing process to prevent the growth of bacteria on the surface.

Acme's quest for innovation is reflected by its on-going goal of generating at least 30% of its sales from products developed in the last 3 years. Therefore, the Company works with new, often proprietary, materials and adds new user-friendly features to existing tools (also read Culture of Innovation under Growth Drivers).

The Company's products are available at Staples, Office Depot, Office Max, United Stationers, SP Richards, W.B. Mason, Home Depot, Target, Wal-Mart, Walgreens, Grainger, McMaster Carr, Meijer, Fred Meyer, WH Smith, and many other major chains all over the world.



**Since 2010, Acme United's annual dividend has increased each year.**

Acme United pays a quarterly dividend and traditionally increases the amount by 1 cent every 6 to 8 quarters. Late last year, the quarterly dividend was increased from 9 to 10 cents per share. The 11% dividend increase was justified as the Company generates lots of cash and expects to continue to do so in coming years.

## BRANDS

**Westcott** began as a ruler company more than 140 years ago. It sells between 60 and 80 million scissors, and between 15 and 18 million rulers annually. It truly is the leading scissors brand in the United States and one of the leading ruler brands in North America.

The Company's infamous grey/yellow Titanium Bonded Non-Stick scissors are known all over the globe. The blades are lightweight, stay sharper longer, and are five times harder than steel. Also, they have a non-stick coating that resists adhesives.

Westcott is also known for its line of iPoint electric pencil sharpeners. Their award-winning design and ease of use make the iPoint one of Acme United's best selling products. In 2013, for example, the sharpener's revenues reached about \$11

million. The iPoint continues to do amazingly well.

Other main Westcott products include TrimAir paper trimmers with a titanium coating and a proprietary blade change system for rotary and personal trimmers, Westcott Ultra Soft Handle scissors with anti-microbial protection and True Professional sewing shears.

In addition, the brand constantly innovates and brings new products to the market. The new ceramic box cutters, for example, are hitting the shelves of large retail chains in the US, Canada and Europe. They feature rugged ceramic blades that are much safer than traditional metal cutters.

Or the new scissors for kids, coined Ergo Jr, which are specifically designed for ages 4 to 6. These are the first and only scissors developed with the United States Ergonomics organization.

The Westcott scissors business continues to become stronger. In fact, Mr. Johnsen mentioned during a recent conference call that a large retailer tried a different scissors supplier a few months ago, and now returned to Acme because sales of the other brand were disappointing. A true validation of the Westcott brand.



**The Westcott Ergo Jr. kids' scissors line are certified by a professional ergonomist & kid tested.**

**Clauss** has its roots dating back to 1877 as a scissors, razors and kitchen knives manufacturer. Today, Clauss offers a

substantial line of quality cutting tools for professionals in the hardware & industrial, lawn & garden, food processing, sewing, and housewares channels.

When the brand was re-introduced, shortly after it was acquired by Acme in 2004, it was a simple scissors business, available in only a handful of stores. A decade later, Clauss has gone through a complete transformation and has become an established name in the industry. It has developed into a broad hardware line and is now available at Lowe's, Home Depot, Sears, Granger, McMaster-Carr and many others.

Similar to Acme's other brands, Clauss applies its proprietary coatings to everyday tools. The brand, for example, markets the SpeedPak Utility Knife. It features a cartridge with 10 titanium bonded double edged blades that allows for quick, easy and safe blade changes.

Another unique product is the Clauss chef shear that detaches for easy cleaning. The shears have a micro-serrated blade, making them ideal for cutting and trimming poultry, meat, fish, herbs, and more.

**Camillus** is one of the oldest and best known knife manufacturers in the United States. It has roots dating back to 1876 and has always been a synonym for the finest knives available. Acme purchased the Camillus brand name and intellectual property rights in 2007 and re-launched the brand in 2009. Since then, numerous new knives have successfully been brought to the market.

Late 2011, Acme United signed an agreement to manufacture and sell Camillus survival knives and tools, co-designed and promoted by Les Stroud, the star of the hit TV series *Survivorman*.

The initial four knives under the Les Stroud Signature name, were introduced in 2012 and immediately sold well. Since then, the Les Stroud line has grown to 25 knives, tools and first aid kits. Some of them are actually used in the *Survivorman* shows.

Next to Les Stroud, Camillus joined forces with ten other so-called Pro Staffers. The Camillus Pro Staff consists of former Green

Berets, expert hunters, Special Forces, adventurers, firemen and survival experts. These are true American heroes and the best of the best at what they do.

Grady Powell, for example, is a former U.S. Army Green Beret. He is now the host of Discovery Channel's *Dual Survival*. Or Jared Ogden, a Navy SEAL who spent eight years in the Naval Service. Jared was star of the National Geographic Television program, *Ultimate Survival Alaska*.



**The Camillus M-13 Machete, featuring a 13" titanium bonded blade with gut hook.**

The Pro Staffers have quickly become an invaluable part of the Camillus team. With their help, the Camillus tools truly stand out in regards to design, performance and durability. As many of them have been in extremely dangerous, and often life-threatening situations, they give information that Camillus' designers could never know about. In addition, these well-known stars have thousands of followers on social media, which is ideal to promote all the new tools.

Plenty of new exciting knives and tools were launched at the 2016 SHOT Show. Amongst them was the Camillus Camtrax, a 12" 3-in-1 hatchet with a hammer and triple-edge folding saw; the M-13 Machete, featuring a 13" titanium bonded blade with gut hook; and the extremely attractive Les Stroud Heritage Collection, which includes a folding knife, two fixed blades, a machete, and a slingshot.

Also, the Heat2, Sizzle2 and Wildfire2 knives, were relaunched. These knives continue to be popular thanks to their "Robo-Assist" quick launch technology.

The SHOT Show is Acme United's biggest marketing event of the year, and as such a

good indicator of how well the Company's new products are received by distributors and consumers. Rick Constantine, Acme's Vice President of Marketing & General Manager, was quoted saying: "SHOT Show 2016 was a huge success". So it's fair to assume that we could see another year of solid growth at Camillus and Western with increased distribution and sales.

Acme intends to further expand the number of Camillus distributors in Europe, Canada, the US, but also in countries like Australia, South Africa and the Philippines.

**PhysiciansCare** offers a wide assortment of first aid kits, emergency and disaster kits, kit refills, hearing, eye and head protection, and ergonomic supports and braces. It also carries a successful branded line of over-the-counter medications, including the active ingredients aspirin, acetaminophen and Ibuprofen, etc. PhysiciansCare's products are sold at Staples, Office Depot, United Stationers, Office Max and many more.

**Pac-Kit** sells first aid kits, industrial stations and refills, emergency medical travel and recreational kits for the industrial, safety, transportation and marine markets. The brand has a long and vivid history dating back to the 19th century. Its early first aid kits were chosen by global explorers like Captain Robert Scott, Admiral Peary and Theodore Roosevelt on their expeditions.

Although Pac-Kit's products are somewhat similar to PhysiciansCare's, Pac-Kit is especially known for tailoring its products to meet user requirements and for rapid turnaround.

**First Aid Only (FAO)** is a supplier of SmartCompliance first aid kits, refills, and safety products that meet regulatory requirements for a broad range of industries.

The business was founded in 1988 and pioneered consultative selling and support of first aid items to large corporate customers. It has since become a recognized industry leader.

It was acquired by Acme in June 2014 for \$13.8 million, after reaching revenues of

\$17.4 million and operating income of \$1.1 million the previous year.

FAO operates out of a modern 54,000 square-foot facility in Vancouver, Washington where well over 100 people are employed. All of FAO's first aid kits are produced in the United States.

First Aid Only is especially known for its SmartCompliance kits. Most businesses are federally mandated to have first aid solutions that are compliant with OSHA as well as ANSI standards. These SmartCompliance first aid supply cabinets ensure that a business is covered.



**The SmartCompliance kits are now placed in thousands of restaurants in the US. And earlier this year, Wal-Mart equipped each store, warehouse, office, and truck with a first aid kit from Acme United.**

The innovative design of the SmartCompliance first aid cabinet eliminates disorganized and missing supplies often seen within traditional first aid cabinets. As first aid products are used, the SmartTab ezRefill reminders notify a user when it's time to reorder so that supplies never run out when it matters most.

The SmartCompliance cabinets are very successful. A few months ago, FAO received an order for 40,000 kits from Wal-Mart. They were installed in the chain's stores, trucks and warehouses. More recently, Saudi Airlines was landed as a new customer. In addition, tests with SmartCompliance kits are ongoing at other corporations, such as food chains, large manufacturers and banks. One such order is potentially worth several hundreds of thousands of dollars (also read Growth Drivers).

**Cuda** markets a line of knives and tools dedicated to fresh and saltwater fishing. The brand was launched in July 2014 in Orlando, Florida at the International Convention of Allied Sportfishing Trades (ICAST), the largest sportfishing trade show in the world.

The Cuda tools are created with a breakthrough design that allows the angler to actually see that the knife has a full tang construction. Moreover, the tools are manufactured with Acme's patented Titanium Bonded technology making them three times harder than untreated options, and they're equipped with Aluminum Alloy and Tungsten Carbide, guaranteeing the ultimate in performance.

As a demonstration of the tools' outstanding design, Cuda won six GOOD Design awards earlier this year from the Chicago Athenaeum, Museum of Architecture and Design. This is one of the oldest and most important design competitions worldwide.

Similar to what Camillus did with Les Stroud, Cuda attracted several well-known fishermen to design, test and represent the brand. The stars of the National Geographic hit show "Wicked Tuna", star of the "Real Fishing Show" Bob Izumi, Mariko Izumi from "Hooking Up", and David Dudley two-time FLW Bass Champion all tested the initial tools extensively.



**A patented stainless steel hook on a Cuda gaff.**

In fact, the original 32 Cuda tools were used for nearly two years before the first product was released to the public. Often the pros will suggest small improvements, but when the products finally go into production, they are

the best on the market. It was the most extensive test program in Acme's history. But it paid off in providing numerous product improvements and usages.

Since then, the Cuda Pro Staff has continued to grow to about 30 ambassadors today.

Also the promotion, which the Pro Staff provides is priceless. One pro has close to 300,000 Twitter followers. So when he tweets information about Cuda, all his followers get to see it. The Pros also use the Cuda tools during tournaments, and they attend Cuda customer meetings to provide testimonials directly to the buyers.

### **RECREATIONAL FISHING MARKET**

Despite increased urbanization and on & offline sales, recreational angling remains one of the largest outdoor activities in the United States.

According to the 2011\* National Survey of Fishing, Hunting and Wildlife-Associated Recreation, the U.S. counts more than 40 million licensed anglers. To put this number in perspective, more Americans fish than play golf (21 million) and tennis (13 million) combined.

The anglers generate over \$46 billion in retail sales with a \$115 billion impact on the nation's economy creating employment for more than 828,000 people.

*\* The survey is conducted every five years by the U.S. Fish and Wildlife Service.*

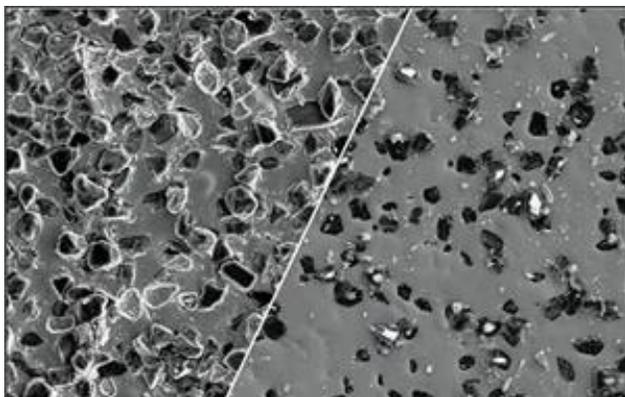
A major advantage of Acme United entering the fishing tools market a couple of years ago, is that fishing is popular in many parts of the world. Europe, for example, counts 25 million recreational anglers, while Canada has over 3 million. These are impressive statistics that immediately give an indication of Cuda's potential.

When Cuda was launched in 2014, it had 24 different tools. Now, only two years later, it has about 70, and by next year, the brand plans to have 100.

Cuda continues to exceed expectations in both brand acceptance and placement at retail stores. This is largely thanks to the innovative design and quality of the tools.

Acme's Rick Constantine has been an avid fisherman for over 40 years. All his knowledge, combined with the use of the best materials on the market, and Acme's patented coating technologies, have created a family of tools that provide consistent, high-end performance.

**Diamond Machining Technology (DMT)** is the world's leading innovator of manual diamond sharpening technology. It currently has 28 employees and sells its products at chains such as Home Depot, Bass Pro Shops, Grainger, Fastenal, and Amazon. DMT manufactures all its products in the United States and exports worldwide to nearly 50 countries.



**The DMT sharpening surface (left) exhibits full coverage and the diamonds show striking consistency in size to ensure peak performance and durability. The copycat surface (right) carries a sparse, patchy coating made from a jumble of different sized diamonds.**

The company was acquired by Acme United in February 2016, and is renowned for its polka dot pattern diamond surface products. It offers sharpening solutions for virtually every user, from do-it-yourselfers to professionals and large commercial operations.

DMT's products differ significantly from those of its competitors. For example, DMT makes certain that each sharpening surface carries the most diamonds per square inch in the industry to guarantee long-lasting performance.

The uniformity of the diamond is also key to a sharpener's performance. DMT uses a proprietary process that ensures near-perfect consistency in grit size. The result is a micronized monocrystalline diamond that covers evenly across the sharpening surface to prove effective with every use, year after year.

By attending several trade shows after DMT's acquisition, the Acme team learned that the diamond sharpening tools brand has plenty of growth opportunities, both in the number of market segments where the products are offered, as well as in the number of customers (Also read Growth Drivers).

## FINANCIALS

### Third Quarter and Nine Months 2016 Results

Net sales for the third quarter ended September 30, 2016 were \$31.9 million, compared to \$29.9 million in the comparable period of 2015, an increase of 7%. Net income for the quarter ended September 30, 2016 was \$1.5 million, or \$0.40 per diluted share, compared to \$1.2 million, or \$0.33 per diluted share, for the 2015 period, a 22% increase in net income and 21% in earnings per share.

For the nine months, ended September 30, 2016, Acme's net sales were \$98.2 million, compared to \$86.7 million in the same period in 2015, an increase of 13%. Net income for the nine months ended September 30, 2016 was \$5.3 million, or \$1.49 per diluted share, compared to \$4.4 million, or \$1.18 per diluted share, in last year's comparable period, a 22% increase in net income and 26% in earnings per share.

The Clauss, Camillus, and Cuda brands added new products and customers. Clauss, for instance, introduced new high performance shears with a carbo-nitrite coating. And Camillus hunting knives sales benefitted from new distribution in the camping area.

Also, the new ergonomic Ergo Jr. kid scissors were well received. We expect a lot more

from them during next year’s back-to school season. In addition, the new Westcott Carbo line of scissors and trimmers, with a carbottitanium coating, exceeded expectations.

Finally, sales at DMT, which was acquired in February of this year, increased more than forecast due to successful placement of the sharpeners in Acme’s existing global distribution network. Also Acme’s online sales, especially at Amazon, continued to increase rapidly.

Amounts in \$000's	09/30/16	09/30/15
Net Sales	31,913	29,903
Cost of Goods Sold	20,050	19,578
S, G & A Expenses	9,723	8,334
<b>Income From Operations</b>	<b>2,140</b>	<b>1,991</b>
Pre-Tax Income	1,828	1,750
Income Tax Expense	355	542
<b>Net Income</b>	<b>1,473</b>	<b>1,208</b>
Diluted Shares Outs.	3,641	3,699
Diluted EPS	0.40	0.33
<b>Most important income statement data for the quarters ending September 30, 2016 and September 30, 2015. Source: Company Press Release</b>		

Gross margin was 37.2% in the three months ended September 30, 2016, compared to 34.5% in the same period in 2015. The higher gross margin was primarily due to a favorable product mix. Also, in the third quarter of last year, the Company incurred approximately \$150,000 of one-time moving and severance costs associated with consolidating its first aid facilities. Gross margin was 36.4% for the nine months ended September 30, 2016 compared to 36.1% for last year’s period.

### Acme’s Largest Customer

Amazon.com is quickly becoming one of Acme United’s most important customers. The Seattle based e-commerce giant will be Acme’s fourth largest customer in 2016, but Mr. Johnsen mentioned that it might move up to become the number three, or even two, as soon as next year.

Westcott, Camillus, Clauss, and DMT sell more products at Amazon almost on a month by month basis. It’s also showing significant strength in the first aid area. **Noteworthy is**

**that internally at Amazon they’re now using Acme’s first aid kits. A true validation of the brand!**

In addition, the Company is working with Amazon on a number of projects to improve sales of first aid refills and SmartCompliance kits.

In Europe, the importance of Amazon.de – the German sister website of Amazon – is significantly growing as well. Part of the DMT product range was recently introduced there and has quickly moved to the top of the retailer’s search results thanks to good ratings and feedback.

Amazon is an increasingly important customer for Acme United. We wouldn’t be surprised if it became Acme’s largest account in a few years.

### Outstanding US Segment

Acme United reports financial information on three separate business segments: the United States (including Asia), Canada and Europe.

Exact revenues per segment for the second quarter will be available in the 10-Q, which will be filed mid-November. However, Acme announced for each segment the percentage by which revenues increased or decreased compared with last year’s third quarter. Based on those numbers, we can give a fair estimation.

Amounts in \$000's	09/30/16	09/30/15
<b>U.S.</b>	28,504	26,160
<b>Canada</b>	1,593	1,669
<b>Europe</b>	1,816	2,074
<b>Estimated sales per segment for the third quarter ending September 30, 2016 (Source: Smallcaps Investment Research) and actual sales per segment for the third quarter ending September 30, 2015 (Source: Company Filing)</b>		

In the U.S. segment, net sales for the quarter ended September 30, 2016 increased 9% compared to the same period in 2015 due to strong sales of Westcott school and office products, and first aid kits. DMT contributed \$1.3 million in sales in the third quarter, and \$3.6 million since February 2016. Net sales for the first nine months of 2016 grew 15% over the comparable period in 2015.

Net sales in Canada for the three months ended September 30, 2016 decreased 5% in U.S. dollars and 4% in local currency compared to the prior-year period. Net sales for the nine months ended September 30, 2016 decreased 2% in U.S. dollars but increased 3% in local currency compared to the same period in 2015. It's clear the business has stabilized in Canada. Growth is again expected thanks to new product introductions.

Net sales in Europe for the three months ended September 30, 2016 decreased 12% in both U.S. dollars and local currency compared to the comparable period in 2015.

The decline in sales was primarily due to the timing of a shipment of promotional products to a mass-market customer. In 2015, the promotion occurred in the third quarter, while in 2016 it occurred in the second quarter. Net sales for the nine months ended September 30, 2016 increased 4% in both U.S. dollars and local currency compared to last year's period.

The European segment has regained its growth and a solid performance is expected going forward.

### Balance Sheet As Of September 30, 2016

The Company's long-term debt less cash on September 30, 2016 was \$33.4 million compared to \$23.9 million on September 30, 2015. By year-end, that number is expected to decline to about \$29 million. This will mainly be achieved by a reduction of bank debt as inventories return back to more normal levels after the back to school season.

During the twelve-month period ended September 30, 2016, the Company paid approximately \$7.0 million for the acquisition of the assets of DMT, spent \$1.4 million on stock repurchases and paid \$1.3 million in dividends on its common stock.

At the end of the third quarter of 2016, Acme had close to \$60 million in working capital and an impressive current ratio of 5.42.

Amounts in \$000's	09/30/16	09/30/15
Cash and Cash Eq.	6,272	4,621
Accounts Receivable	25,909	23,587
Inventories	38,117	34,497
<b>Total Current Assets</b>	<b>72,293</b>	<b>64,877</b>
Property & equipment	7,893	7,343
Intangible Assets, net	16,768	12,023
<b>Total Assets</b>	<b>99,372</b>	<b>86,586</b>
Accounts Payable	6,748	7,206
<b>Total Current Liabilities</b>	<b>13,345</b>	<b>13,965</b>
Bank Debt	39,706	28,551
<b>Total Liabilities</b>	<b>53,625</b>	<b>42,878</b>
Total Stockholder Equity	45,747	43,698
<b>Most important balance sheet data for the periods ending September 30, 2016 and September 30, 2015. Source: Company Press Release</b>		

## GROWTH DRIVERS

### Culture of Innovation Leads to Blockbuster Products

New product development is truly in the DNA of Acme United. The Company's quest for innovation is reflected by its ongoing goal of generating at least 30% of its sales from products developed in the last 3 years.

In order to achieve this goal, well thought-out products are brought to the market almost on a constant basis. The school and office products brand Westcott, for example, this year alone has already launched over 100 new scissors, trimmers, cutters, pencil sharpeners, etc.

The entire process of innovation at Acme United starts with hiring the right people. Many employees have a product development background or gained expertise at the product marketing department of previous employers.

The next step is to "feel" the market by speaking with end-users. In the case of Westcott products, these end-user are teachers, crafters, office people, etc. It's important to speak with them. To find out what they're struggling with, how they feel certain products can be improved upon.

To get a hold of this knowledge, these people are visited where they are using the products. Chris Alagno, Vice President at Acme United, was recently quoted saying, "Great innovative products don't come from the four walls in our office, instead they come from the field".

The third step is trying to solve the issues that were raised by the users. A solution is sought in cooperation with engineers, product developers, and designers. As soon as a product idea is received from Acme's marketing and brand managers, the New Product Development team starts working on the technical and industrial aspects of the design. It converts sketches into a physical products, and evaluates if the tool will actually function as it's supposed to.

The final step in the process is testing. Before mass production of the new product is initiated, a team of testers evaluates the pre-production samples to ensure the product's quality and functionality. Only when they are satisfied with all aspects of the samples, the go-ahead is given for mass production.

#### **VITALITY INDEX**

The Vitality Index measures new product revenues as a percent of total revenues. It was 3M that first recognized the need for an overall measure of innovativeness. They created the metric named "Vitality Index" in 1988. The actual value differs greatly by company and the market it's in. At Acme United the goal is to reach a products vitality rate of 30%.

It's relatively easy to calculate. The only management decision is how long a launched product remains "new". Most companies, such as Acme United, consider a product as being new when it's less than three years on the market. But, anything is possible. Some software companies only use 9 months.

Amongst the tools that Acme launched the past few months, there are several ones with blockbuster potential. The new scissors for kids, coined Ergo Jr, for example are specifically designed for ages 4 to 6. These

are the first and only scissors developed with the United States Ergonomics organization.

During many months of testing, the specific muscles, which children use while cutting, were researched. As a result, the surprisingly innovative design of the Ergo Jr. reduces stress on a child's arm and wrist by as much as 50% compared with a regular scissor. We expect this to be a good product for next year's back-to-school season.



**The new Westcott carbo-titanium scissors can cut through almost 40 layers of denim.**

Also the new Westcott Carbo line of scissors and trimmers looks and performs exceptionally well. The carbo-titanium coating, makes the blades 8 times stronger than untreated steel. In addition, the handle and scissors are reinforced to withstand the pressure when cutting through thick materials. The carbo-titanium scissors can cut through almost 40 layers of denim fabric!

#### **First Aid Keeps Going Strong**

Before the First Aid Only acquisition in 2014, Acme United already owned two first aid brands, Pac-Kit and PhysiciansCare. Thanks to the combination of the three brands, the Company increased its volumes, and as such was able to negotiate more favorable sourcing prices for products such as bandages, tapes, and pads with its suppliers.

**Acme United has been in the first aid business for over 40 years. Combined, its three brands are among the top-10 producers of first aid kits in the United States, and they generate between 35% and 40% of the Company's revenues.**

And they continue to grow fast. The SmartCompliance business by FAO, for example, is becoming a big success. This is a typical razor/razorblade sales model, as Acme United initially benefits from the placement of the first aid kits, and then as people use the components, there's a strong resale business. In fact, revenues from refills about equal sales of the kits.

Acme's strategy to refill the kits through the internet is contrary to service people in delivery vans who will typically go into different locations to fill the first aid kits and then come back on a regular basis. The latter is obviously a time consuming and very expensive model, as the cost of the individual sales staff, the truck, the employee, and benefits have to be taken into account. Consequently, Acme United is clearly gaining share in this \$600 million market segment.

In addition, the Canadian division has received its Health Safety license, which means it can start to manufacture and assemble its own first aid kits. Also in Europe, Acme received its medical certification, which allows it to import first aid products directly from China.

And finally, a few months ago the Company started shipping products and refills to Fastenal, a large industrial wholesaler for use in vending machines that are placed at facilities throughout the U.S. These are products such as eye wash or to treat burns on the work floor.

To fulfill all orders for first aid products, the Company recently added a second shift at its manufacturing plant in Vancouver, Washington and a full second production line at the Rocky Mount, North Carolina warehouse.

### DMT - World Renowned Sharpening Products Manufacturer

Since the acquisition of DMT, additional orders worth around \$1 million, were received. A large retailer reviewed its sharpener business and ordered \$500,000 worth of products. And another large chain, which was an existing DMT customer, doubled its regular order.

In addition, while DMT has only been a part of Acme United for a few months, plenty of synergies have been discovered. For instance, existing Acme customers are very interested in DMT products for sports & hunting purposes. Also, there are lots of opportunities for DMT in the kitchen area. Consequently, Acme will immediately start to pursue new customers in those areas.

And it works the other way around as well. DMT has plenty of customers in the industrial area where Acme's sales are soft. Consequently, Camillus knives and Clauss industrial tools, such as scissors and cutters, should fit ideally in the DMT customers' range of products.

## RECENT EVENTS

### DMT & Cuda Tools Impress at EFTTEX

In June, we visited Acme's European team at the European Fishing Tackle Trade Exhibition (EFTTEX). We got a good impression of the Company's Cuda and DMT tools, and how well they are being received in the European marketplace.

The 35th edition of EFTTEX was held in the RAI Exhibition center in Amsterdam, the Netherlands, and attracted 215 exhibitors from 35 different countries. Visitors included manufacturers, wholesalers and retailers from all over the world.

The annual event always attracts most of the well-known names in the industry. In fact, over the years, it has developed into the premier European fishing fair and the third largest one in the world.

We saw smiling faces at the Cuda/DMT booth. Although it was only day two of the three-day event when we visited, the Company had already received lots of enquiries and orders.

While walking around at the show, it soon became clear that the Cuda fishing tools truly distinguish themselves for a couple of reasons. First, there were only a handful of competitors that offered knives, which indicates that the playing field is still wide open.

And second, the breakthrough design of the Cuda tools is exceptional. The knives feature Titanium Bonded German 4116 full-tang stainless steel, which is known for its corrosion resistance and edge retention. They have an integrated scale grip pattern for extra grip. All Cuda tools also feature a full-tang window proving the knife blade goes all the way through the handle.

We also learned that the distribution of Cuda continues to expand. The tools are now available at the largest fishing chain in Germany, and they are doing well in Spain, the UK, the Netherlands and the Scandinavian countries.

**We walked away from the event very satisfied. We saw firsthand that the Cuda and DMT tools are in demand in Europe. We're convinced that the Acme United Europe team will have plenty of work following up on all the leads that were generated at EFTTEX.**

### Cuda Makes Heads Turn at ICAST

Cuda again made heads turn at the annual ICAST show in Orlando, Florida. The event was a phenomenal success. Thanks to the introduction of more than 30 new tools, plenty of existing and potential customers stopped by at the Cuda booth.

The Cuda Pro staff was also well represented at the show. Having such celebrated and respected fishermen at the booth is priceless, as they engage with customers to discuss the product line and they attract lots of curious anglers. The Cuda representatives even scheduled a two-hour meet and great session with the popular Capt. TJ Ott from the hit National Geographic show, Wicked Tuna.

ICAST traditionally is about new gear, apparel and accessories that help make a day on the water both exciting and rewarding. Keeping up with that tradition, Cuda launched a series of new tools at ICAST that are now on the shelves of retailers and sporting goods chains.

For example, Cuda introduced its first ever professional line of knives. The seven different knives feature USA CTS 40A Titanium NonStick Bonded corrosion resistant

Carpenter steel blades and have full tang handles that fit comfortably in the user's hand.

#### ICAST

The International Convention of Allied Sportfishing Trades, better known as ICAST, is the world's largest sportfishing industry trade show. Over 15,000 people attended to learn about the latest products and trends in the domestic and international sportfishing and boating community. The show hosted 1,850 booths with an overall exhibitor count of more than 700.

Cuda's regular knife line for both fresh and saltwater fishing was also expanded with seven new models. Ranging from a marlin spike, to a wide, semi-flex fillet knife, the new line incorporates a number of advanced features, including Cuda's signature visible full-tang construction, non-slip scale pattern grips and titanium-bonded stainless steel.



**Captain TJ Ott with a fan.**

In addition, Cuda introduced four gaffs ranging in length from four to eight feet, featuring carbon-fiber shafts, making them lightweight yet extremely strong. Each gaff featured a patented stainless steel hook with advanced corrosion and adhesion resistance.

Moreover, Cuda presented the new Cuda Fish Measure, designed with a removable straight edge starting point to ensure consistent measurements with each catch. As seen on

Wicked Tuna, the new fish measure features large, easy-to-read-numbers, and is made from durable, waterproof nylon.

Additional new items to the accessory line include the heavy-duty Cuda Sheath & Lanyard, which fits a variety of Cuda pliers and snips; a Cuda Ice Pick; and a Cuda Connect, which connects an action camera, such as a GoPro or WASP to a Cuda Tag Stick or Harpoon.

Finally, Cuda, for the first time, showed a new series of marine first aid kits designed specifically for the unique needs of anglers. Available in three sizes – personal, inshore and offshore – the kits are compact and constructed for easy stowage for a convenient onboard first aid center.

Included in the kit are first aid essentials for burn, CPR and shock treatment, as well as sunscreen, sting relief, aspirin and wound care necessities.

Commenting on the success of the new tools, Capt. Rick Constantine said, “Cuda products are known for quality and performance. We design our tools in cooperation with the Pro Staff and the result is a powerful line, built with anglers in mind. There’s a tool for every task and each one is designed to make life easier and more productive on the water.”

## OUTLOOK & VALUATION

Acme United has a real culture of innovation. New product development is in the heart and soul of its employees. By its constant drive to bring products to the market, the Company continues to gain market share in huge areas, such as the school and office products sector. Consequently, Acme’s guidance for fiscal 2016 was raised for the second quarter in a row to sales of \$124 million and earnings per share of \$1.63.

Acme United’s brands excel across the board, which lays the groundwork for continued growth in 2017. Westcott, for instance, is offering new school, home and office products, such as glue guns with ceramic coatings that are ideally suited for the craft, office and shipping work places. It has new

heavy duty pencil sharpeners with proprietary titanium blades for the school market and it’s expanding the line of ceramic box cutters for heavier duty use.

Next to school and office products, first aid is a second major growth driver for Acme. Production capacity was recently added, and may have to be expanded even further. SmartCompliance kits and their refills have become very popular because they are cheaper and more convenient for businesses. The razor/razor blade model ensures a continual sale of refills once the cabinets are installed.



**The new iPoint Halo heavy duty pencil sharpeners with proprietary titanium blades for the school market ready to be shipped.**

Moreover, the first aid division introduced an app a couple of weeks ago at the National Safety Council Show in Anaheim, California, which allows customers to reorder first aid supplies in a quick, convenient and user-friendly matter. It received lots of positive responses at the conference and will be implemented in 2017.

Also DMT is doing very well. In the United States, Canada and Europe, customers are enthusiastic about the synergies with tools from other Acme brands, such as Clauss, Camillus or Cuda. Only a few months after the

sharpening tools manufacturer was acquired by Acme United, its production had to be expanded to meet demand.

Clauss, Cuda, and Camillus products continue to benefit from expanded distribution in the mass market and specialty stores. For Cuda, new freshwater fishing tools will be launched and several product line extensions, such as carbon fiber gaffs and nets, will be introduced.

On top of all that, Mr. Johnsen again indicated that the Company will be looking for more accretive acquisition candidates in 2017.

The Company continues to execute very well. Distribution is gained both online and off, gross margins are above 35%, and the balance sheet is very healthy.

### Peer Comparison & Valuation

Acme United competes with many companies in each market and geographic area. The major competitors in the cutting category are 3M and Fiskars Corporation, while Maped and Staedtler are the major competitors in the measuring category. In addition, the major competitor in the pencil sharpener category is Bostitch, and in the safety category Acme faces most competition from Johnson and Johnson.

Although there are many competitors, it's hard to identify a peer group of companies, because there's no other Company in exactly the same line of business as Acme United. Moreover, some of these other companies that engage in the Company's line-of-business do so through divisions or subsidiaries that are not publicly-traded.

For reason of comparison, we have placed the Company in the Housewares & Accessories industry. The average P/E ratio for a Company in that industry is 25.2x, again a bit higher than the average of 24.72x in our previous report. Because we continue to feel that the markets are somewhat overvalued at these multiples, and because we want to remain conservative in our estimates, we are going to apply a 25% discount to the industry's average P/E ratio.

Taking the discount into account, we end up with an average P/E ratio of 18.90x for the Housewares & Accessories industry.

Amounts in \$000's	2014	2015	2016E
<b>Total Revenue</b>	107,222	109,812	124,000
<b>Net Income</b>	4,789	4,794	5,935
<b>Annual sales and earnings FY 2014 – 2016E.</b>			
<b>Source: Company Filings and Smallcaps Investment Research estimates</b>			

**Applying the 18.90x P/E multiple from the peer group to the revised estimated EPS for 2016, we reach the following calculation: \$1.63 estimated EPS multiplied by 18.90 = \$30.81.**

**Based on these calculations, we reiterate our buy recommendation for Acme United Corp. with a price target of \$30.81, which is 44% above today's stock price.**

## SHARE DATA & OWNERSHIP

At the end of the third quarter, Acme United had approximately 3,641,000 common shares outstanding. The principal owners of the Company's common stock are North Star Investment Management Corporation (13.1%), Walter Johnsen (8.4%), Bard Associates Inc. (4.3), Capital Management Corp (3.8%), and Teton Advisors (3.5%).

## MANAGEMENT

### ❑ WALTER C. JOHNSEN - CHAIRMAN AND CEO

Mr. Johnsen has served as director since 1995 and as Chairman and Chief Executive Officer since November 30, 1995. Before joining the Company he was Vice Chairman and a principal of Marshall Products, Inc., a medical supply distributor.

### ❑ PAUL DRISCOLL - VICE PRESIDENT AND CFO, SECRETARY AND TREASURER

Mr. Driscoll has served as Vice President and Chief Financial Officer, Secretary and Treasurer since October 2, 2002. Mr. Driscoll joined Acme as Director International Finance on March 19, 2001. From 1997 to 2001 he

was employed by Ernest and Julio Gallo Winery including two years in Japan as Director of Finance and Operations. Prior to Gallo he served in several increasingly responsible positions in Sterling Winthrop Inc. in New York City and Sanofi S.A. in France.

**▣ BRIAN OLSCHAN - PRESIDENT AND COO**

Mr. Olschan served as Senior Vice President of Sales and Marketing from September 10, 1996 until January 22, 1999. Effective January 23, 1999, he was promoted to President and Chief Operating Officer. From 1984 to 1996, he was employed by General Cable Corporation in various executive positions.

## ANNUAL INCOME STATEMENT FY 2013 – Q3 2016

All numbers in thousands

PERIOD ENDING	FY 2013	FY 2014	FY 2015	Q3 2016
<b>Total Revenue</b>	<b>89,577</b>	<b>107,222</b>	<b>109,812</b>	<b>98,198</b>
Cost of Revenue	57,753	69,037	70,251	62,455
<b>Gross Profit</b>	<b>31,824</b>	<b>38,186</b>	<b>39,561</b>	<b>35,743</b>
<b>Operating Expenses</b>				
Research & Development	-	-	-	-
Selling, General and Administrative	25,945	30,791	32,214	28,008
Non Recurring	-	-	-	-
Others	-	-	-	-
Total Operating Expenses	25,945	30,791	32,214	28,008
<b>Operating Income or Loss</b>	<b>5,879</b>	<b>7,394</b>	<b>7,347</b>	<b>7,735</b>
<b>Income from Continuing Operations</b>				
Total Other Income (Expenses) Net	(35)	(118)	(168)	(38)
Earnings Before Interest And Taxes	5,844	7,276	7,179	7,697
Net Interest Expense	350	473	565	642
Income Before Tax	5,494	6,803	6,614	7,055
Income Tax Expense	1,491	2,014	1,820	1,750
Net Income From Continuing Ops	4,003	4,789	4,794	5,305
<b>Non-recurring Events</b>				
Discontinued Operations	-	-	-	-
Extraordinary Items	-	-	-	-
Effect Of Accounting Changes	-	-	-	-
Other Items	-	-	-	-
<b>Net Income</b>	<b>4,003</b>	<b>4,789</b>	<b>4,794</b>	<b>5,305</b>
Preferred Stock And Other Adjustments	-	-	-	-
<b>Net Income Applicable To Common Shares</b>	<b>\$4,003</b>	<b>\$4,789</b>	<b>\$4,794</b>	<b>\$5,305</b>

Annual Income Statement FY 2013 – Q3 2016. Source: Company Filings



# Acme United Corporation

**NYSE MKT: ACU**

**Company Headquarters**

55 Walls Drive, Suite 201  
Fairfield, CT 06824  
United States

**Company Contact Information**

Paul G. Driscoll, Chief Financial Officer  
Phone: +1 203-254-6060  
Fax: +1 203-254-6019

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Contact: [editor@smallcaps.us](mailto:editor@smallcaps.us)

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