Enpro Uncovered

by Henry W. Schacht, CFA

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In 2002, a small industrial conglomerate called **Enpro Industries (NPO)** began life as an independent company after a hasty spin-off from **Goodrich (GR)**. It was an inauspicious beginning to be sure. Trading started at $8.50 a share and it was downhill from there.

Enpro's decline was more than simple knee-jerk selling after a spin-off. Goodrich didn't want Enpro and neither did its new stockholders. This was fear. The reason: Asbestos. Like many other industrial companies, Enpro used asbestos in some of its products years ago. As a result, Enpro was a hot potato that nobody wanted.

Within six months of its spin-off, Enpro's shares were trading around $2 a share.

Schacht Value stumbled across poor Enpro as it languished on the 52-week low list. At first glance it didn't get anyone all that excited. This changed as we looked deeper. The more we looked, the more we liked.

At its low, Enpro Industries' market value was a paltry $45 million. It seemed a tad low for a company with $700 million in sales, positive cash flow, and earnings of over $40 million a year. The market was pricing Enpro as if it was in liquidation.

But business is good. Enpro subsidiaries manufacture engineered industrial products from engines (Fairbanks Morse) and air compressors (Quincy Compressor) to a host of gaskets, seals, and bearings (Garlock & GGB). These are solid businesses with leading positions in niche markets.

Enpro is now valued at $800 million as shares have increased from $2.25 to $37.50 in four and a half years. Revenue is now over $900 million. With $160 million cash and low debt levels, the company has a solid balance sheet. Free cash flow is around $50 million and that includes some heavy capital spending.

There is a lot to like about Enpro, and Schacht Value is not alone in recognizing it. Steel Partners and Keeley Asset Management own 12.3% and 7.7% of Enpro's outstanding shares respectively. These are names that GuruFocus readers may be familiar with. Nonetheless, Enpro still doesn't seem to get the respect it deserves. It's just too cheap.

Asbestos is the obvious culprit. It is an ongoing problem for Enpro. But the truth is that management has done a great job of managing asbestos claims and liabilities. In court the company has been very successful and insurance coverage is substantial. Indeed, cash flows related to asbestos are difficult to predict. Insurance collections and payments to claimants are mismatched, bumpy, and sporadic. And all timing differences in these cash flows come home to roost in NPO's financial statements.

Enpro will face asbestos costs for years, but this is more than reflected in the current stock price. The general trend in claims is down, providing a tailwind for earnings and cash flow over time. Underlying fundamental strengths will to continue to emerge and this is good news for long-term investors.

Furthermore, Enpro is working hard to help investors understand the extent of asbestos liabilities. In the 4 th Quarter, the firm recorded a $305 million charge to reflect management's estimate of ongoing asbestos liabilities. This concerned some investors, but the liability isn't new. The charge simply was an attempt to make explicit that which was only implicit. The move went a long way towards transparency.

Enpro investors who have been willing to filter out the noise and focus on core fundamentals have been well compensated. Get acquainted with Enpro and it may make a believer out of you.

Disclosure: At the time of publication, the author owns shares of Enpro Industries personally and on behalf of clients.

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