



**A No-Load Mutual Fund Managed by:  
Front Street Capital Management, Inc.**

June 30, 2019

During the past eighteen months we have been accumulating a meaningful position in The Manitowoc Company (6.12% of Fund holdings). As you know, we select our long-term holdings in the Tarkio Fund based upon a set of management criteria that we believe, if successfully implemented, will create a culture that can unleash the best in human potential. In particular, we generally look for companies that feature:

- Integrity of Management
- A Long-Term Focus
- Purpose and Passion
- Employee Empowerment – Driving Fear Out of the Organization
- Teamwork – Cooperation, Not Internal Competition
- Disciplined Capital Allocation

These criteria are based on the work of W. Edwards Deming, a management consultant who revolutionized manufacturing when he introduced his management concepts to Japan after World War II. He ignited the “quality” revolution led by the Japanese in the 1980’s and most notably the domination and eventual transformation of the auto industry by Toyota. We have been students of this process since 1988 and perform all our analysis through this lens. Over time, we have boiled his process down to a set of core principles in order to identify companies that have created energized corporate cultures, including companies outside of the manufacturing sectors. We think being able to translate these principles to identify companies that may have never even heard of Deming is a testament to the universality of the values around which this process is based. It has been rewarding and fun to use this work to diversify our portfolio beyond the manufacturing sector.

That said, there has been a small portion of the manufacturing sector that have stayed devoted not only to the Deming principles but also to the specific techniques and tools (including specific principles, structures and incentives) he used to motivate individuals and encourage collaboration. In fact, this subset of manufacturers has continually improved upon the Deming model over time. This small group of almost “cult-like” followers have fallen under several labels over the years (Continuous Improvement, Total Quality, Lean Manufacturing, Six Sigma, and Kaizen, among others). We have been fortunate over the years to have benefitted from a handful of these zealots. A few manufacturers we own that are presently doing this are Danaher, Herman Miller and Colfax (5.15%, 4.29% & 1.12% Fund holdings respectively). When we are fortunate enough to find these gems, we believe they can provide us with two powerful advantages:

1. They are easy for us to identify, as they are typically proud of their work in this area and often wear it on their sleeve.
2. If you can find these companies in the early stage of a long-term transformation process you can get a rare, and we believe dependable, look into the future of a company that will be incrementally improving their competitive position in the market place indefinitely into the future.

As such, we are proud and excited to have had the opportunity to allocate a meaningful portion of Tarkio Fund’s capital to The Manitowoc Company last year. Although the Deming method is a model of empowered employees and decentralized decision-making, the essential element in a company’s transition and ultimate success is a total commitment from its leadership. We think this is the reason only a very small number of companies can make this sort of organizational transformation, since a change in culture on this scale typically results in poor short-term performance before the long-term benefits start to accrue. In our opinion, few leaders have the commitment to withstand short-term pressures, particularly in publicly-traded companies, to stay the course and power through the inevitable trough. Even more unique is to be able to find a leader with that type of strong will paired with the humility to delegate decision making away from the executive suite and onto the manufacturing floor. We believe that Manitowoc CEO Barry Pennypacker is that leader!!

The Manitowoc Company was an odd midsized company consisting mostly of an industrial kitchen equipment business and an old line crane manufacturing business. Three years ago, an activist investor forced the company to split itself into two separate companies for short-term gain. The crane business was subsequently left as a stand-alone, publicly traded entity. The consensus investor opinion at the time was that most of the value in the prior combined entity was in industrial kitchen equipment. The crane business had a checkered financial history and was viewed somewhat as the discarded piece in the transaction, and its stock price suffered as a result. Not long after, Barry Pennypacker was hired as Manitowoc’s new CEO. Pennypacker had begun his lean journey with our own Danaher, then took

his learned expertise in “Lean” to transform companies on two subsequent occasions, one being the publicly traded Gardner Denver company. When Barry was hired at Manitowoc, he brought key members of his transformational team from his previous experiences with him. The band was back together for one more gig.

Regarding the stock price, we think Wall Street likes to see improving financial results, even though it’s analysts may not always have an understanding

of what it takes to get there. In fact, a management philosophy that empowers lower level employees to be able to make decisions is often viewed by the consensus investment community as a negative. In fact, we believe that employee empowerment can often be the antithesis of the ego centric Wall Street culture. As a result, despite a revitalized management team at Manitowoc, the stock continued to languish. Probably looking for a fresh start and a complete reset, the company decided to reverse split the stock (each share of stock became a quarter of a share with four times the price). In our experience, these transactions almost always lead to lots of investors bailing out once they see that they are left with what they consider remnants of a former holding in their portfolios. This type of selling also seems to be much more prominent during years of heavy year-end tax-loss selling (as occurred at the end of 2018). Partly because of these phenomena, Manitowoc’s stock price came under heavy selling pressure during last year’s fourth quarter. We took full advantage of this rare opportunity and significantly added to our position during the end of 2018. In an unusual set of circumstances, a similar situation occurred with YRCW last year as they also had a reverse stock split a few years ago. We aggressively and enthusiastically added to our position there as well. This is the primary reason for our short-term underperformance in the fourth quarter of 2018 and, correspondingly, our outperformance in the first quarter of 2019. The valuation metric we like to use in some situations like this is the relationship between stock price and sales (the “price to sales ratio”). Stable industrial companies with average profitability we believe can generally sell at 1.0-1.5 times sales. Manitowoc’s stock currently sells around \$17 per share and the company at this very early stage in its transformation has about \$47.00 of net sales per share.

On May 10, 2019, Manitowoc reported its first quarter earnings, and there was incremental but clear evidence of their progress in the numbers reported. But we got a glimpse of their real progress in January, as Dominic Piazza and Jeremy Brown made a site visit to the company’s Shady Grove manufacturing facility. They could literally see the difference between the manufacturing areas that had already undertaken transformation efforts and the areas that have yet to start the transformation. They likened the experience to visiting two altogether different companies. I’ve personally had experience with this type of lean transformation in the late 1980’s (often known at that time as “total quality control”), as we owned, benefitted from and witnessed a transformation at JLG Industries. In addition, the passion and belief in the transformation process they witnessed at Manitowoc from everyone they interacted with at the company was nothing short of extraordinary and probably a career-changing experience for both Jeremy and Dom (like it was for me at JLG).

Outstanding investment results always include a little bit of good fortune coming your way. Identifying The Manitowoc Company and Barry Pennypacker is smack dab within our circle of competence and, we believe, can be easily duplicated. But finding them at this early stage in their transformation it is nothing short of a miracle, and we welcome our good fortune. As Warren Buffett says, “When it’s raining gold, reach for a bucket, not a thimble.” In this case, we have tried to behave accordingly.

We thank you for your continued confidence and investment in the Tarkio Fund.

Warm regards from our home in Western Montana,

A handwritten signature in blue ink that reads "Russ Piazza". The signature is fluid and cursive, with a large initial "R" and "P".

Russ, Michele, Ginger, Jeremy, and Dominic

The Tarkio Team

***On June 30, 2019, the per share price of MTW was \$17.80. The mention of any investments in this commentary should not be considered a recommendation to sell or purchase the security(ies) mentioned or similar investments. Please consult an investment professional on how the purchase or sale of such investments can be implemented to meet your particular investment objective or goals. Investments in securities and/or similar investments are subject to risks. It is important to obtain information about and understand these risks prior to investing.***

***Mutual Fund investing involves risk. Such risks associated with the Tarkio Fund (including but not limited to Small/Medium Capitalization Risks, Foreign Securities Risk, Fixed Income Securities Risk, Non-Diversification Risk, and New Fund/Adviser Risk) as well as applicable investment objectives, charges and expenses must be considered carefully before investing. This and other important information about the Tarkio Fund is found in the Prospectus, a copy of which or current performance information may be obtained by visiting [www.tarkiofund.com](http://www.tarkiofund.com) or by contacting 866-738-3629. We encourage you to read the prospectus before investing.***

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