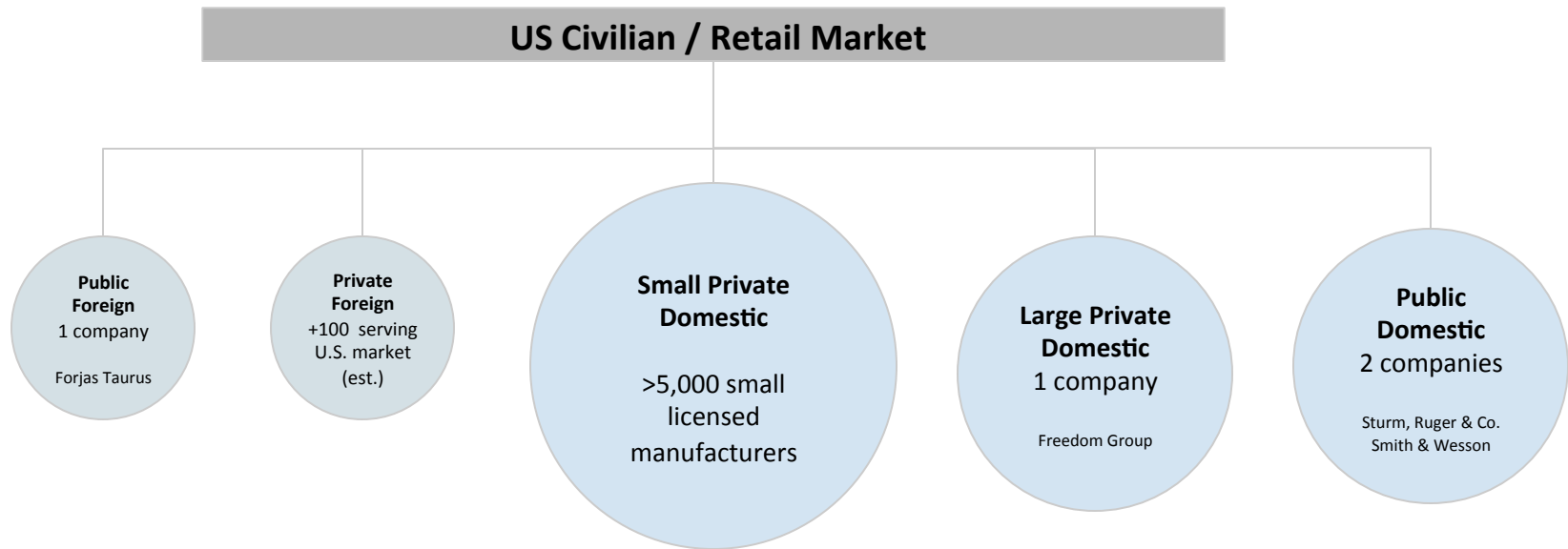


Advisory Committee on Socially Responsible Investing
Firearms Industry Research
February 11, 2014

Firearms Industry Research

Firearms Industry Overview



- Aerospace and defense companies (defense contractors) do not serve the civilian firearms market.
 - i.e. large public companies like Raytheon, Lockheed Martin, Northrop Grumman, General Dynamics, etc.

Firearms Industry Research

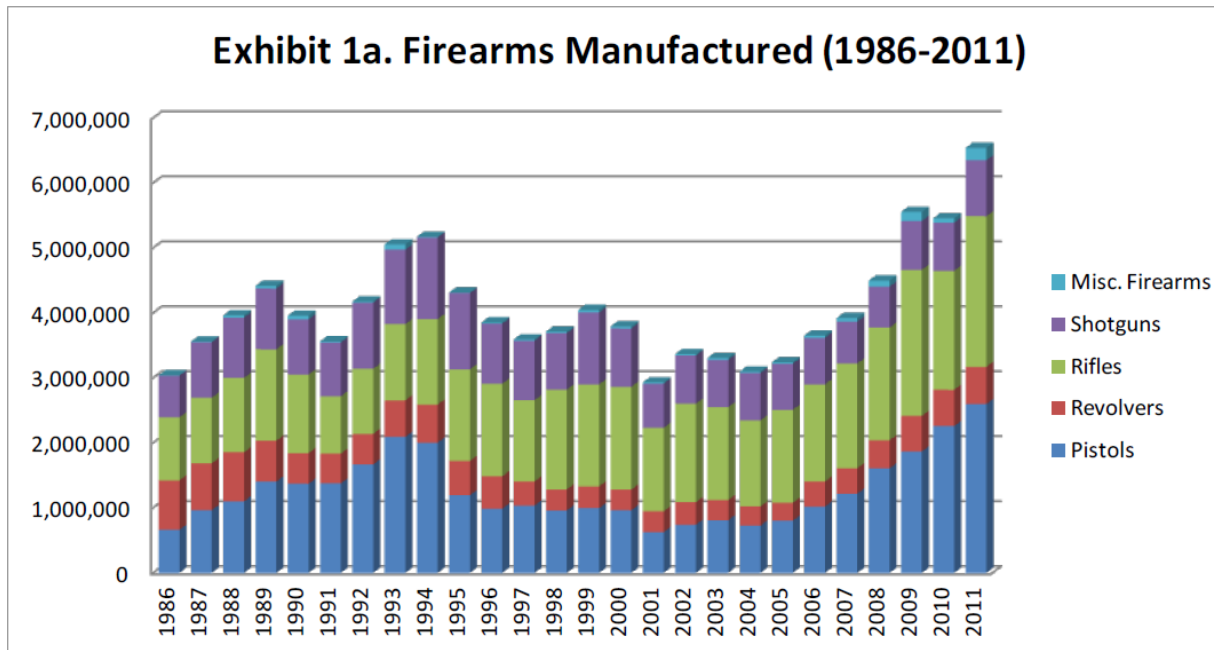
Firearms Industry: Facts & Figures

- According to the Federal Bureau of Alcohol, Tobacco, Firearms and Explosives (ATF).
 - As of 2011, there were approximately 5,400 licensed firearms manufacturers, 950 licensed importers in the US and approximately 51,000 retail gun dealers in the US.
 - 39% of US households owned a gun (according to *The Economist/YouGov* poll).
 - Wal-Mart is the nation's largest gun retailer; Cabela's is the second largest followed by other big-box retailers like Bass Pro Shops, Dick's, Gander Mountain, Academy Sports, and Big Five Sporting Goods.
- The top 25 US manufacturers account for nearly 90% of all guns produced in the US annually.
 - The top 10 manufacturers account for nearly 90% of industry revenue in the US annually.
 - These include the brand names such as Ruger, Smith & Wesson, Remington, Maverick, Sig Sauer, Marlin, Savage, Beretta, Taurus, Browning, Henry, etc.
- In the United States, there are only two publicly traded firearms and ammunition manufacturers serving the retail market:
 - Sturm, Ruger & Co. (NYSE: RGR).
 - Smith & Wesson Holding Corp. (Nasdaq: SWHC).
- Internationally, there is one publicly traded firearms and ammunition manufacturer (based in Brazil).
 - Forjas Taurus SA (BM&F Bovespa: FJTA4).
 - In 2012, the top three importers to the US by country were Brazil, Austria, and Germany.
- The world's largest manufacturer of commercial firearms is the US-based Freedom Group, also known as the Remington Outdoor Company.
 - Currently owned by Cerberus Capital Management.

Firearms Industry Research

Firearms Industry: Facts & Figures

- In 2013, the major domestic markets for firearm industry revenue were exports (35.2%), civilians (34.8%), and military and law enforcement (30%).
- Revenue was expected to grow to \$14.7 billion in 2013, with an average five-year annual rate of 8.4% and an increase of 20.2% in 2013 due primarily to:
 - Consumer fear of increasing crime during recession
 - Fear of harsher gun control regulations from the Obama legislation. Concerns were heightened further by mass shootings in Aurora, CO, and Sandy Hook Elementary School in CT.
- From 2008 to 2012, the FBI conducted an increased number of National Instant Criminal Background Checks (NICS) at an average annual rate of 11.4%. After the CT shooting in December 2012, the number of background checks conducted during the following three months increased 44.5% compared to the same time frame in 2012.
- Per the graph below, in 2011, pistols account for 40% of firearms manufactured in the US; rifles 35%; shotguns 13%; revolvers 9%; and misc. firearms 3%.



Firearms Industry Research

Sturm, Ruger & Co. (NYSE: RGR)–Market Cap: \$1.51 billion

- Founded in 1949 in Southport, CT, Ruger is one of the major manufacturers of firearms and ammunition in the United States. The company listed on the New York Stock Exchange in 1990. Ruger employs 1,460 full-time employees as of 2/1/2013.
- For the year ending 12/31/2012, Ruger recorded revenues of \$491.8 million, representing approximately 3% of total US gun industry revenue.
 - Firearms segment net sales were \$484.9 million in 2012. This represents an increase of \$160.7 million or 49.7% from 2011 firearm net sales of \$324.2 million. Firearms unit shipments increased 51.0% in 2012.
- For the nine months ending 9/28/2013, Ruger recorded net sales of \$506.4 million, a 44% increase from \$350.1 million during the corresponding period in 2012.
 - Firearms segment net sales were \$605.9 million, an increase of \$202.4million, or 50.2 %, as compared to the nine months ended September 30, 2012.
- Ruger offers rifles, pistols, and revolvers. As a % of revenue:
 - Pistols: 44%, Rifles: 29%, Revolvers: 19%, Accessories 6%, Castings: 1%.
 - Included in “rifles” are hunting rifles and modern sporting rifles.
- Products are sold to federally licensed, independent wholesale distributors who purchase the products directly from the company. They resell to federally licensed, independent retail firearms dealers who resell to legally authorized end users. Operates an online retail store.
 - End users are sportsmen, hunters, people interested in self-defense, law enforcement, government organizations, and collectors.
- Ruger does not disclose the portion of sales derived from modern sporting rifles.
- The estimated sell-through of the Company’s products from the independent distributors to retailers increased 63% in 2012 from the comparable prior year periods. For the same periods, NICS background checks increased 28%.



TOP HOLDERS RGR	Shares Held	% Total Shares Held	% Total Assets
Capital World Investors	1,685,389	8.71	0.03
Vanguard Group, Inc.	1,620,048	8.37	0.01
NFJ Investment Group LLC	1,183,857	6.12	0.29
BlackRock Fund Advisors	1,064,671	5.5	0.02
James Investment Research, Inc.	751,221	3.88	1.79
Dimensional Fund Advisors, Inc.	469,384	2.43	0.03
Southpoint Capital Advisors LP	413,118	2.14	1.45
State Street Corp	374,203	1.93	0
Northern Trust Investments, N.A.	328,298	1.7	0.01
ARONSON+JOHNSON+ORTIZ	289,280	1.5	0.08
Hays Advisory LLC	244,415	1.26	2.17
ING Investment Management LLC	246,450	1.27	0.04
Morgan Dempsey Capital Management, LLC	204,881	1.06	4.66
Guggenheim Capital LLC	235,464	1.22	0.05
Columbia Management Investment Advisers, LLC	190,010	0.98	0.01
Mellon Capital Management Corporation	189,417	0.98	0.01
Gotham Asset Management, LLC	183,383	0.95	0.37
Schroder Investment Management Ltd.	165,400	0.85	0.04
BMO Asset Management Inc.	141,644	0.73	0.01

Firearms Industry Research

Smith & Wesson Holding Corp. (Nasdaq: SWHC) – Market Cap: \$778.9 million

- Founded in 1852 in Springfield, MA, Smith & Wesson is a major manufacturer of firearms and ammunition in the United States, employing 1,475 full-time as of 5/21/2013.
- At the end of their fiscal year (4/30/2013), S&W recorded revenues of \$587.5 million, an increase of 42.6% from the prior fiscal year. This represents approximately 4% of total US gun industry revenue.
- Manufactures handguns (including revolvers and pistols), long guns (including modern sporting, bolt action, and single shot rifles), handcuffs, and firearm-related products and accessories.
- Customers include gun enthusiasts, collectors, hunters, sportsmen, competitive shooters, individuals desiring home and personal protection, law enforcement and security agencies and officers, and military agencies.
- Sells products under the Smith & Wesson, M&P, Thompson/Center and Performance Center brands.
- Company estimates that domestic non-military firearms market is approximately \$2.0 billion for handguns and \$1.6 billion for long guns (excluding shotguns).
 - Owns market share of approximately 17% and 11%, respectively.
- Sells to distributors who sell to federally licensed dealers who in turn sell to the end uses. Also sells directly to large retailers and dealers. Operates an online retail store.
 - Sales are 89.1% to domestic consumers; 7.6% to state and local law enforcement and federal government; 3.3% international.
- Although attempting to secure military supply contracts, approximately 88% of their net firearm sales are in the sporting goods distribution channel.



TOP HOLDERS SWHC	Shares Held	% Total Shares Held	% Total Assets
Vanguard Group, Inc.	5,376,236	8.58	0.01
Acadian Asset Management LLC	2,349,898	4.2	0.18
BlackRock Fund Advisors	1,969,170	3.14	0.01
Royal Bank of Canada	1,572,023	2.51	0.01
ING Investment Management LLC	1,408,197	2.25	0.04
Quantitative Management Associates LLC	1,296,519	2.07	0.03
ARONSON+JOHNSON+ORTIZ	1,240,100	1.98	0.06
State Street Corp	1,080,979	1.72	0
Trafelet & CO LLC	950,000	1.52	7.54
Northern Trust Investments, N.A.	943,382	1.51	0
Eubel Brady & Suttman Asset Mgmt Inc	914,830	1.46	2.74
Oxford Asset Management, LLC	682,021	1.22	0.28
Olstein Capital Management, L.p.	796,000	1.27	1.34
LSV Asset Management	778,200	1.24	0.02
Millennium Management LLC	676,385	1.08	0.02
Thompson, Siegel & Walmsley LLC	662,100	1.06	0.16
ING Investments, LLC	600,505	0.96	0.32
TIAA-CREF Investment Management LLC	590,415	0.94	0.01
Gotham Asset Management, LLC	575,887	0.92	0.21
Batterymarch Financial Mgmt, Inc.	548,689	0.88	0.13

Firearms Industry Research

Freedom Group International (Cerberus Capital Management)

- The Freedom Group (FGI), based in NC, is the largest manufacturer of firearms, ammunition, and related products in the world with approximately 4,300 employees and 12 manufacturing facilities. It is also known as the Remington Outdoor Company.
- The company was formed through the combination of Bushmaster, Remington, DPMS and Marlin.
 - FGI is a holding company controlled by Cerberus Capital Management, owned since the firm acquired Bushmaster in April 2006.
 - Shortly after the Sandy Hook shooting, on December 18, 2012, Cerberus Capital Management announced its intention to sell its investment in the Freedom Group. To date a transaction has not occurred and new proposals are under way to assist investors who wish to distance themselves from the industry.
- Holds #1 market share position in domestic shotgun sales and commercial AR-style rifles, lever action sales, rimfire rifles, and bolt-action rifles; and the world leader in centerfire rifle hunting ammunition sales. Competitive advantage is gained by leading the US in the manufacture of both firearms and ammunition.
- For year ending 12/31/2012, generated net sales of \$931.9 million. In the first nine months of 2013, generated \$1.0 billion net sales, an increase of 50% as compared to the nine months ending 9/30/2012.
- End customers include police departments, domestic and foreign government organizations, including the U.S. military, and consumers, such as sportsmen, hunters, and recreational shooters.
- Distribution channels include major chain retail stores, major distributors, smaller dealers, gun clubs, and ranges.
 - Sales to Wal-Mart have ranged from 12%–16% of FGI total net sales over the last 3 years, making Wal-Mart, FGI's largest customer.
- Family of companies:
 - Bushmaster
 - Remington
 - Remington Military
 - Remington LE
 - Remington PMPD
 - DPMS Panther Arms
 - Marlin Firearms
 - H&R 1871
 - Dakota Arms
 - Parker Gun Makers
 - Barnes Bullets
 - Advanced Armament
 - Para USA
 - Mountain Khakis
 - Tapco

Firearms Industry Research

Forjas Taurus (BM&F Bovespa: FJTA4)–Market Cap: \$130.9 million

- Forjas Taurus (“Taurus”) is a diversified manufacturing conglomerate, the largest weapons manufacturer in Latin America and one of the largest small arms manufacturers in the world, based in Porto Alegre, Brazil.
 - The company’s main segment, the Defense and Security industry, includes the manufacture of handguns (revolvers and pistols), long guns (rifles and shotguns) for hunting and target shooting practice, and weapons for military and police use (pistols, shotguns, submachine guns, rifles and grenade launchers). Accounts for 77% of net revenue.
 - Also operates in the Metallurgy and Plastics industry, as a market leader in the production of motorcycle helmets, bullet proof vests, antiriot shields, plastic containers and forged and injected parts.
- Is one of the largest importers of handguns to the United States, operating under Taurus USA.
- As of September 30, 2013, net revenues for the year had increased 29% to approximately \$270 million as compared to the first nine months of 2012, due primarily to the increases in exports.
- The US market accounted for 64% of net revenues in the nine months ending September 30, 2013.
- Company’s firearms can be purchased in the US through same channels as US firearms.

Firearms Industry Research

Federal Gun Laws in the United States

- National Firearms Act (1934): earliest federal regulation of firearms; set definitions for classification of firearms; required registration of firearms and imposed an excise tax on manufacturing and transfer of firearms
- Omnibus Crime Control and Safe Streets Act of 1968: allowed federal wiretaps, prohibited interstate trade in handguns, increased the minimum age to 21 for buying handguns, and established a national gun licensing system
- Gun Control Act of 1968: regulation of interstate commerce in firearms, generally prohibiting interstate firearms transfers except among licensed manufacturers, dealers, and importers
- Firearm Owners Protection Act (1986): revised multiple statutes of the Act of 1968
- Gun-Free School Zones Act (1990): prevents possession in a “school zone”
- Brady Handgun Violence Prevention Act (1993): imposed background check requirement
- Federal Assault Weapons Ban (1994–2004) (expired): banned assault weapons

Firearms Industry Research

Public Safety and Recreational Firearms Use Protection Act of 1994 (Federal Assault Weapons Ban, expired 2004)

- ❖ This definition of an assault weapon continues to be the standard definition in context of assault weapon discussions among critics, enthusiasts, politicians, etc., for “military-style” rifles or “modern sporting” rifles
- Passed by President Bill Clinton in 1994, expired in 2004.
- As defined by the 1994 Assault Weapons Ban, an “assault weapon” refers primarily (but not exclusively) to semi-automatic firearms that possess the cosmetic features (see next page for detail) of an assault rifle or “military-style” weapon that is fully automatic.
 - Simply possessing these cosmetic features warrants classification as an assault weapon.
 - Actually possessing the operational features, such as 'full-auto', changes the classification from assault weapons to Title II weapons.
 - Title II weapons are highly regulated by the Bureau of Alcohol, Tobacco, Firearms, and Explosives under the National Firearms Act.
 - Acquisition of these firearms is subject to approval by the Attorney General, and federal registration is required for possession. A \$200 tax is imposed for each transfer or production of a Title II weapon.
- Semi-automatic firearms, when fired, automatically extract the spent cartridge casing and load the next cartridge into the chamber, ready to fire again.
- They do not fire automatically when the trigger is held down.
 - Only one round is fired with each trigger pull.

Firearms Industry Research

Cosmetic Features of an Assault Weapon

- Semi-auto rifle with detachable magazines and two + of the following:
 - A folding or telescoping stock
 - A pistol grip
 - A bayonet mount
 - A flash suppressor, or threads to attach one
 - A grenade launcher
- Semi-auto pistols with detachable magazines and two + of the following:
 - Magazine that attaches outside the pistol grip
 - Threaded barrel to attach barrel extender, flash suppressor, handgrip, or suppressor
 - Barrel shroud that can be used as a hand-hold
 - Unloaded weight of 50 oz (1.4 kg) or more
 - A semi-automatic version of a fully automatic firearm
- Semi-auto shotguns with two + of the following:
 - Folding or telescoping stock
 - Pistol grip
 - Fixed capacity of more than 5 rounds
 - Detachable magazine

Same Rifle



Same Shotgun



Non-Assault Weapons

Assault Weapons



Firearms Industry Research

Brady Handgun Violence Prevention Act of 1993

(required background checks and defines “prohibited persons”)

- The Brady Act requires that background checks be conducted on individuals before any firearm may be purchased from a federally licensed dealer, manufacturer or importer.
- Prohibits certain persons from shipping or transporting any firearm in interstate or foreign commerce, or receiving any firearm which has been shipped or transported in interstate or foreign commerce, or possessing any firearm in or affecting commerce.
 - Those convicted of felonies and certain misdemeanors, except where state law reinstates rights, or removes disability
 - Fugitives from justice
 - Unlawful users of certain depressant, narcotic, or stimulant drugs
 - Those adjudicated as mental defectives or incompetents or those committed to any mental institution and currently containing a dangerous mental illness
 - Non-US citizens, unless permanently immigrating into the US or in possession of a hunting license legally issued in the US
 - Illegal aliens
 - Those who have renounced US citizenship
 - Minors defined as under the age of 18 for long guns and the age of 21 for handguns, with the exception of Vermont, eligible at age 16
 - Persons convicted in any court of a misdemeanor crime of domestic violence (an addition)
 - Persons under indictment for a crime punishable by imprisonment for more than one year are ineligible to receive, transport, or ship any firearm or ammunition.

Firearms Industry Research

Recent Developments in Gun Control Legislation

On January 16, 2013, in response to the violent shootings in Colorado and Connecticut, President Obama announced a plan of 23 executive actions on gun control.

The following proposed amendments to the gun bill were brought before the Senate. Each amendment needed to clear the 60-vote threshold in the Senate to be approved. Results as follows:

- **BACKGROUND CHECKS** (Manchin-Toomey amendment)
 - Require background checks for online sales and sales at gun shows, but not sales between neighbors and family members
 - **Failed** 54–46
 - Substitute for background check bill that increases enforcement and reporting on mentally ill people
 - **Failed** 52–48
- **ASSAULT WEAPONS**
 - Renew and strengthen a ban on assault weapons and high-capacity magazines
 - **Failed** 40–60
 - Limit magazine sizes to 10 rounds
 - **Failed** 46–54
- **GUN TRAFFICKING**
 - Make straw purchasing and trafficking a federal crime
 - **Failed** 58–42
- **MENTAL HEALTH**
 - Reauthorize and improve mental health programs
 - **Passed** 95–2
- **OTHER**
 - Impose penalties on states for releasing gun ownership data
 - **Passed** 67–30
 - State reciprocity for the carrying of concealed firearms
 - **Failed** 57–43
 - Allow only a judge to deem veterans mentally incompetent to own a gun
 - **Failed** 56–44

More recently, on January 3, 2014, President Obama announced two new executive actions on gun control: the first change by the Department of Defense to further clarify who would be unable to possess a firearm for specific situations related to mental health; and the second by the Department of Health and Human Services, to allow certain entities covered by patient privacy protections to submit additional information to the background-check system.