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January 12, 2009

Oshkosh Corp.

(Buy)

| | | | |
|----------------------|------------------|------------------|--------|
| Price: | \$10.94 | Ticker: | OSK |
| 52-wk. range: | \$3.85 – \$45.99 | Dividend: | \$0.40 |
| Shares out.: | 74.4 mill. | Yield: | 3.7% |
| Market Cap.: | \$813.9 mill. | | |

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Investment Thesis

Oshkosh Corporation, based in Oshkosh, Wisconsin, manufactures a broad range of specialty vehicles and vehicle bodies. The company operates in four segments: 1) Access Equipment, which includes aerial work platforms, telehandlers, scissor lifts, and vertical masts, often used on construction sites to reach elevated heights; 2) Defense, which includes the construction of a variety of military vehicles for the U.S. Department of Defense; 3) Fire & Emergency, which is mostly the manufacture of various apparatuses for fire trucks; and 4) Commercial, which includes the manufacture of refuse collection vehicles for the waste services industry.

Over the past two years, Oshkosh has often been mentioned in the national news media for its pivotal role in the war in Iraq. The U.S. Department of Defense (DoD) estimates that over 60% of U.S. military casualties in Iraq are caused by Explosively Formed Projectiles, or EFPs. EFPs are essentially land mines that discharge specially-shaped metallic discs designed to penetrate armor plating used in military fighting vehicles. EFPs are often placed on the curb of roads so as to be detonated when vehicles or pedestrians pass by, and so are sometimes also known as roadside bombs. In response to this problem, Defense Secretary Robert Gates declared in May 2007 that the U.S. military's highest priority was the design and deployment of military vehicles that would be resistant to EFPs. The ensuing program came to be known as the MRAP (Mine Resistant Ambush Protected) program.

Out of the MRAP program a series of so-called MRAP vehicles was produced and deployed in Iraq to replace the older military vehicle, the "Humvee". These new MRAP vehicles include two important features. The first, and perhaps most obvious feature, is a radically thicker, heavier plate of armor on all surfaces, making it far more difficult for projectiles to penetrate through the vehicle. The second feature is that the bottom of the vehicle is V-shaped (when viewed from the front or rear); the benefit of this feature is that when such a vehicle trips a roadside bomb, the occupants of the vehicle are far less vulnerable to the explosion because of the few extra feet the projectiles travel to meet the bottom of the vehicle.

However, an initial deficiency of this new class of MRAP vehicles was that the additional heavy plate of armor made the vehicles much slower and too heavy. The problem presented by the weight of the vehicles was that an estimated 72% of bridges in the world could not support them. Oshkosh answered this problem by forming a joint venture with Ceradyne, a company involved in the design and manufacture of ceramics. As a material, ceramics are very resistant to EFPs, but have the crucial benefit of being far lighter than armor made with metallurgy. The vehicle Oshkosh and Ceradyne designed with this new type of ceramic armor is known as the "Bull".

Vice President-elect Joe Biden, as the former chair of the Senate Foreign Relations Committee, became an outspoken supporter of the Bull because of its protective capacities

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and lighter weight. However, in his opinion, Congress has been slow to act to authorize funding for further purchases of the Bull, which might lead one to believe that the incoming Presidential administration is committed to purchasing more of these vehicles. Naturally, this might lead analysts of Oshkosh to believe that, in the not too distant future, the company will receive a rather large military contract for the manufacture of the Bull.

However, as evidenced by the recent share price of Oshkosh, the investment community appears largely uninterested in recent developments involving the Bull. Neither do investors appear to be interested in the company's announcement in November that it has broken ground for a new manufacturing facility in Tianjin, China for the construction of access equipment vehicles (largely airport rescue vehicles) for the Asian market. This new facility will be the company's first ever China-based manufacturing facility. Rather, investors appear solely to be interested in one matter – the solvency of the company in the ongoing credit crisis.

Oshkosh has on its balance sheet \$2.7 billion of long-term debt, with shareholders' equity of \$1.4 billion, which gives it a long-term debt-to-equity ratio of 1.93x. However, the company also has on its balance sheet roughly \$2.3 billion of goodwill, which leaves it with negative tangible equity. In FY2008 (fiscal year ended September 30, 2008), the company recorded a goodwill impairment charge related to its refuse collection vehicle business, Geesink. Recently, investors have been concerned with potential write-downs in 2009 in companies across all industries due to the economic downturn. Surely, many are concerned that further write downs for Oshkosh will significantly lower earnings this year, or even lower the company's book value to a level at which it possibly violates a debt covenant related to a minimum leverage ratio.

Over the past 12 months, the Oshkosh market capitalization has collapsed by 75%. As a result, its price-to-book value and price-earnings multiples are far lower than they have been in at least 10 years. The shares are currently priced at 0.6x book value and 6.6x the consensus analyst earnings estimate for 2009. In contrast, its 10-year average price-to-book ratio is 2.7x, and the corresponding average P/E is 15.7x. Therefore, if the shares were simply accorded their 10-year historical average multiple of book value, the appreciation would equal 350%; on a P/E basis, appreciation would amount to 138%.

Moreover, due to rising input costs and lower worldwide demand especially in the second half of 2008, the company's return-on-assets (ROA) declined to its lowest level in over ten years. Its 10-year average ROA of 6.5% is 66% higher than its FY2008 ROA of 3.9%. Therefore, the potential return in the shares becomes far greater if the company can manage the current economic downturn and return to its normalized level of profitability. The valuation section of this report details how, in a so-called "favorable outcome" scenario, the share price could exceed \$80.

In summary, the risk premium accorded by investors to the Oshkosh shares is so substantial that the company trades at price-to-book and P/E multiples not seen in over ten

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years. Although the incoming Presidential administration appears committed to the company's ceramic-plated MRAP vehicle, and although the company recently announced the expansion of its Access Equipment segment in China, the investment community appears solely focused on the damage that might be inflicted by the current credit crisis. Essentially, the Oshkosh share price reflects the widespread belief that the current disequilibrium in the credit markets is at least semi-permanent. However, if one believed that the credit condition as it exists today is unlikely to exist in some future period, the return potential in Oshkosh is quite substantial. Therefore, the Oshkosh shares are recommended for purchase at this time.

Company History

Oshkosh Truck was founded by William R. Besserdich and Bernhard A. Mosling in 1917. The two men had received patents in 1914 and 1915 for improvements on four-wheel-drive capability. Besserdich and Mosling approached several established automobile manufacturers – including Ford, Packard, and Studebaker – about using their designs to produce a four-wheel-drive vehicle. After a series of rejections, they decided to start their own company. In May of 1917, the Wisconsin Duplex Auto Company, located in Clintonville, Wisconsin, was incorporated. Besserdich was the company's president, and Mosling was listed as its manager and secretary.

The prototype vehicle was a four-cylinder, three-speed, 3,000-pound truck called Old Betsy. The success of Old Betsy's four-wheel-drive components attracted investors. Since many of the investors were based in Oshkosh, 47 miles south of Clintonville, the company relocated there toward the end of 1917 and changed its name to Oshkosh Motor Truck Manufacturing Company.

The first Oshkosh Motor truck was the two-ton capacity Model A, priced at \$3,500. After the Model A, Oshkosh began offering the Model B, which could carry 3.5 tons, and soon afterward, the five ton Model F. The four-wheel-drive ability of the Oshkosh trucks quickly distinguished them from conventional trucks already on the market. In 1925 Oshkosh introduced the Model H, a truck with a six-cylinder engine. The Model H proved to be useful for road construction and snow plowing, and therefore sold well to municipalities. Oshkosh diversified its product line further with the introduction of the J-Series in 1935. The J-Series trucks had capacities from two to three-and-a-half tons.

Oshkosh's first major defense contract after World War II was for more than 1,000 WT-2206 vehicles. The WT-2206 was a large, heavy-duty truck capable of plowing snow at much higher speeds than conventional equipment. The Air Force purchased the trucks for clearing runways at its northern-most bases. In 1968 Oshkosh began building the U.S. Navy MB-5, an aircraft rescue and fire-fighting (ARFF) truck capable of carrying 400 gallons of water. The water could expand to 5,000 gallons of extinguishing foam when combined with a specially-concentrated form of the foam.

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In the 1970s, Oshkosh began introducing a number of new trucks including the B-Series, a forward placement concrete carrier. The B-Series truck allowed the operator, seated in a one-person cab over the front axle, to drive to the precise location the concrete was to be discharged, and control the chute without leaving the cab. Despite the company's civilian products, defense contracts continued to provide the majority of Oshkosh's growth through the 1980s. In 1981 Oshkosh was awarded its largest contract yet, a five-year deal from the U.S. Army to produce Heavy Expanded Mobility Tactical Trucks (HEMTT). The contract called for delivery of 2,140 trucks, valued at \$242 million, with an option on the further production of 5,350 additional vehicles. Oshkosh's role in the 1990 Persian Gulf War included pulling the Patriot missile launcher.

In 1985 Oshkosh went public. In 1990 the U.S. Army awarded it the contract for more than 1000 M-1070 Heavy Equipment Transporters, the main function of which is hauling tanks. In September of 1990 Oshkosh won another Army contract for 2,626 Palletized Load System (PLS) vehicles. The PLS truck is ten-wheel driven and can carry 16.5 tons of cargo.

Beginning in 1995 and continuing through 2007, Oshkosh acquired several different vehicle manufacturing businesses, including (but not limited to): fire truck maker Pierce Manufacturing for \$158 million in 1996; Quebec-based Nova Quintech's firefighting ladder technology in 1997; McNeilus Companies, a maker of concrete mixers and bodies for refuse trucks, for \$250 million in 1998; Kewaunee Engineering, which made parts for aerial devices, for \$6.3 million in 1999; Viking Truck and Equipment, a maker of concrete mixers, in 2000; Medtec Ambulance Corporation in 2000; Geesink Norba Group, a maker of refuse collection bodies, mobile and stationary compactors, and transfer stations, in 2001; Jerr-Dan, a towing equipment manufacturer, in 2004, for \$80 million; 75% of firefighting equipment manufacturers BAI Brescia Antendi International and BAI Tecnica also in 2001; access equipment manufacturer JLG Industries (marking Oshkosh's expansion into the aerial platform market), in 2006; AK Specialty Vehicles, a maker of mobile medical, broadcast, and homeland security command and control vehicles, for \$140 million in 2006.

Overview of Business

Access Equipment

In December 2006, through its JLG acquisition, Oshkosh became a manufacturer of a wide range of aerial work platforms, telehandlers¹, scissor lifts and vertical masts. These

¹ A telescopic handler, or telehandler, is a machine similar in appearance and function to a forklift, with the increased versatility of a single telescopic boom that can extend forward and upward from the vehicle. On the end of the boom the operator can attach one of several attachments, such as a bucket, pallet forks, muck grab, or lift table.

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machines are used in a variety of construction, agricultural, industrial, institutional and general maintenance applications to safely and efficiently position workers and materials at elevated heights that might otherwise have to be reached by scaffolding, ladders, cranes or other means. Prior to the acquisition, in October 2005, JLG had entered into a 20-year strategic alliance with Caterpillar for the design, manufacture and sale of Caterpillar-branded telehandlers.

JLG also arranges equipment financing and leasing, primarily through private-label arrangements with independent third-party financial companies. Financing arrangements that JLG offers or arranges through this segment include installment sale contracts, capital leases, operating leases and rental purchase guarantees. Terms of these arrangements vary depending on the type of transaction, but typically range between 36 and 72 months and generally require the customer to be responsible for insurance, taxes and maintenance of the equipment, and to bear the risk of damage to or loss of the equipment.

The following table details results for the Access Equipment segment since the JLG acquisition in December 2006. Segment revenue increased 21.5% year-over-year and the segment operating margin slightly increased.

Access Equipment Segment Results

| <i>(in millions)</i> | 2008 | 2007 | % change |
|----------------------------------|----------|----------|----------|
| Net sales | | | |
| Aerial work platforms | \$ 1,998 | \$ 1,494 | 33.8% |
| Telehandlers | 747 | 797 | (6.3)% |
| <u>Other</u> | 341 | 249 | 36.9% |
| Total | 3,086 | 2,540 | 21.5% |
| | | | |
| Operating income | 360 | 268 | 34.2% |
| <i>Operating margin</i> | 11.7% | 10.6% | |
| | | | |
| Identifiable assets | 3,999 | 4,160 | |
| <i>Operating income ÷ assets</i> | 9.0% | 6.5% | |

Defense Segment

Oshkosh has sold products to the U.S. Department of Defense (DoD) for over 80 years. Its proprietary military all-wheel drive product line of heavy-payload tactical trucks includes the Heavy Expanded Mobility Tactical Truck (HEMTT), the Heavy Equipment Transporter (HET), the Palletized Load System (PLS), the Common Bridge Transporter (CBT) and the Logistic Vehicle System Replacement (LVSr). The company's military medium-payload tactical trucks include the Medium Tactical Vehicle Replacement (MTVR) and the Medium Tactical Truck (MTT). Oshkosh also exports severe-duty heavy and medium payload tactical trucks to foreign customers.

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The DoD recently awarded Oshkosh a multi-year, firm, fixed-priced requirements contract for production of the Family of Heavy Tactical Vehicles (FHTV). The contract follows an existing FHTV contract awarded in February 2007, and includes the production of the HEMTT, and PLS. As a result of significant usage of the company's heavy-payload tactical trucks in the war in Iraq, it was awarded a five-year follow-on, fixed-price indefinite delivery, indefinite quantity contract in September 2004 to rebuild Oshkosh heavy-payload defense trucks and trailers deployed in Iraq. This contract essentially allows the DoD to contract with Oshkosh to rebuild Oshkosh defense trucks and trailers at fixed prices over a five-year period ending in September 2009.

In May 2006, the DoD awarded Oshkosh a production contract for the LVSR vehicle and associated manuals, vehicle kits, test support and training for the U.S. Marine Corps. The company estimates that this fixed-price contract has a value of \$740 million based on a production quantity of 1,592 units over a six-year period. The contract allows for the purchase of up to 1,900 cargo, wrecker and fifth-wheel LVSR variants. Oshkosh delivered the first units under the contract in fiscal 2007 and expects that full scale production will begin in the second half of fiscal 2009.

In April 2008, Oshkosh entered into an exclusive teaming arrangement for the rights to market and produce the SandCat, a highly mobile, armored light tactical vehicle. This vehicle is designed for high speed operation on or off road, while at the same time providing significant armor protection to its occupants. Oshkosh is currently marketing the SandCat to the DoD and foreign militaries.

On December 31, 2008, the DoD announced that it awarded a sole source contract to Oshkosh to provide replacement parts for medium and heavy tactical vehicles. This annual contract has a potential duration of 10 years, if all option years are exercised, and a value of up to \$1.12 billion. This follows a one-year contract that included seven option years, each of which were exercised, that ended in December 2008.

Under the contract, Oshkosh Defense will supply the DoD with replacement parts to support Oshkosh's medium and heavy tactical vehicles, which include the MTRV, HEMTT and PLS. Oshkosh also supplies replacement parts for other manufacturers' medium and heavy-payload vehicles. The first contract order is valued at \$17.5 million and is for approximately 2,300 replacement part numbers to support Oshkosh's tactical vehicles.

The following table details results for the Defense segment since 1997. Segment revenue increased at an 18.9% annualized rate over the past 12 years.

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Defense Segment Results

| <i>(in millions)</i> | <u>Revenue</u> | <u>Operating income</u> | <u>Op. Margin</u> |
|----------------------|----------------|-------------------------|-------------------|
| 2008 | \$1,892 | \$265 | 14% |
| 2007 | 1,417 | 245 | 17% |
| 2006 | 1,317 | 242 | 18% |
| 2005 | 1,061 | 210 | 20% |
| 2004 | 774 | 128 | 17% |
| 2003 | 657 | 69 | 10% |
| 2002 | 595 | 41 | 7% |
| 2001 | 423 | 40 | 9% |
| 2000 | 276 | 30 | 11% |
| 1999 | 223 | 23 | 10% |
| 1998 | 248 | 23 | 9% |
| 1997 | 283 | 20 | 7% |

Fire & Emergency

Through its Pierce brand name, Oshkosh manufacturers fire apparatuses assembled on custom chassis, designed and manufactured to meet the specific needs of firefighters. Pierce also manufactures fire apparatuses assembled on commercially available chassis, which are produced for multiple end-customer applications. Pierce primarily serves domestic municipal customers, but also sells fire apparatuses to airports, universities and large industrial companies, and in international markets. In an effort to be a single-source supplier for its customers, Pierce manufactures a line of custom and commercial fire apparatuses and emergency vehicles, including pumpers, aerial and ladder trucks, tankers, light, medium and heavy-duty rescue vehicles, wildland rough terrain response vehicles, mobile command and control centers, bomb squad vehicles, hazardous materials control vehicles and other emergency response vehicles.

Through its JerrDan name, Oshkosh manufactures towing and recovery equipment, including roll-back carriers and traditional tow trucks. In addition to manufacturing equipment, JerrDan provides its customers with one-stop service for carriers and wreckers and generates revenue from the installation of equipment, as well as the sale of chassis and service parts.

The company also manufactures and sells aircraft rescue and fire-fighting (ARFF) vehicles to domestic and international airports. These highly specialized vehicles are required to be in service at most airports worldwide to support commercial airlines in the event of an emergency. Customers include many of the world's largest airports, including LaGuardia, O'Hare, Hartsfield-Jackson and Dallas/Fort Worth in the U.S. and airports located in Montreal and Toronto, Canada; Rome and Milan, Italy; and Shanghai, Hangzhou, and Beijing, China.

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The Fire & Emergency segment also includes the manufacture of its airport snow removal vehicles. These vehicles can cast up to 5,000 tons of snow per hour and are also used by some of the largest airports in the world.

Through its Medtec brand, Oshkosh manufactures custom ambulances for private and public transporters and fire departments. Medtec markets a full line of ambulances including smaller Type II van style ambulances, larger Type I and Type III ambulances, as well as larger “Additional Duty” ambulances. Type I ambulances feature a conventional style, light or medium-duty chassis with a modular patient transport body mounted separately behind the vehicle cab. Type II ambulances are smaller van style ambulance units typically targeted to transport ambulance services. Type III ambulances are built on light-duty van chassis with a walk-through opening into the patient transport body which is mounted behind the vehicle cab.

Through its OSV brand, the company manufactures mobile medical vehicles for North American and European medical centers and service providers. OSV is the only mobile medical vehicle manufacturer certified by all major original equipment manufacturers of medical diagnostic imaging equipment. OSV also designs and manufactures custom vehicles for the broadcast industry through its Frontline brand. These vehicles include television broadcast, satellite news gathering and microwave transmission electronic news gathering vehicles for broadcasters, TV stations, broadcast production, radio stations and NASA. OSV also manufactures mobile command and control centers and simulation units for sale to police, fire and other government agencies in the U.S.

The following table details results for the Fire & Emergency segment since 1997. Although the segment operating margin declined a percentage point from 2007 to 2008, margins have remained remarkably consistent over the past decade.

Fire & Emergency Segment Results

| <i>(in millions)</i> | <u>Revenue</u> | <u>Operating income</u> | <u>Op. Margin</u> |
|----------------------|----------------|-------------------------|-------------------|
| 2008 | \$1,193 | \$94 | 8% |
| 2007 | 1,142 | 108 | 9% |
| 2006 | 962 | 90 | 9% |
| 2005 | 842 | 80 | 9% |
| 2004 | 600 | 55 | 9% |
| 2003 | 535 | 52 | 10% |
| 2002 | 476 | 49 | 10% |
| 2001 | 464 | 46 | 10% |
| 2000 | 391 | 33 | 8% |
| 1999 | 336 | 27 | 8% |
| 1998 | 301 | 26 | 8% |
| 1997 | 292 | 29 | 10% |

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Commercial

Through McNeilus and Geesink, Oshkosh manufactures refuse collection vehicles for the waste services industry. The Commercial segment also includes the manufacture of front and rear-discharge concrete mixers and portable and stationary concrete batch plants for the concrete ready-mix industry. Through its IMT name, the company manufactures field service vehicles and truck-mounted cranes for the construction, equipment dealer, building supply, utility, tire service and mining industries.

In March 2002, Oshkosh introduced the rear-discharge Revolution concrete mixer drum, which is constructed of lightweight composite materials. In 2006, it launched the sale of front-discharge Revolution drums. Since the introduction of the first concrete mixer drum about 90 years ago, drums had been produced utilizing steel, until the launch of the Revolution. The Revolution was the first composite concrete mixer drum ever produced.

The following table details historical results for the Commercial segment.

| <u>Commercial Segment Results</u> | | | |
|-----------------------------------|----------------|-------------------------|-------------------|
| <i>(in millions)</i> | <u>Revenue</u> | <u>Operating income</u> | <u>Op. Margin</u> |
| 2008 * | \$1,037 | (\$29) | (3)% |
| 2007 | 1,248 | 245 | 20% |
| 2006 | 1,190 | 242 | 20% |
| 2005 | 1,061 | 210 | 20% |
| 2004 | 774 | 128 | 17% |
| 2003 | 657 | 69 | 10% |
| 2002 | 595 | 41 | 7% |
| 2001 | 423 | 40 | 9% |
| 2000 | 276 | 30 | 11% |
| 1999 | 223 | 23 | 10% |
| 1998 | 248 | 23 | 9% |
| 1997 | 283 | 20 | 7% |

** 2008 operating income excludes a goodwill impairment charge of \$167.4 million and a long-lived asset charge of \$7.8 million related to its refuse collection vehicle business, Geesink.*

The FY2008 operating loss (even excluding the charges related to Geesink) for the Commercial segment were due to a \$37 million operating loss for Geesink and significantly lower concrete mixer sales as a result of the slowdown in the U.S. residential construction market. Geesink incurred an operating loss of \$19 million in FY2007. Although Oshkosh expects to improve the profitability of Geesink, the recent losses led the company conclude that a non-cash impairment charges of \$175.2 million were required.

Liquidity and Capital Structure

At the end of Oshkosh's fiscal year ended September 30, 2008, the company had \$88.2 million in cash on its balance sheet and long-term debt totaling \$2,681 million. Shareholders' equity equaled \$1,389 million, which results in a long-term debt-to-equity ratio of 1.93x. However, this ratio is a bit misleading as the company also recorded \$2,274 million of goodwill related to its various acquisitions over the past decade. Therefore, Oshkosh has negative tangible book value.

| <i>(in millions)</i> | at Sept. 30, 2008 |
|----------------------|-------------------|
| Cash & equivalents | \$ 88.2 |
| Total debt | 2,680.5 |
| Shareholders' equity | 1,388.6 |
| - <u>Goodwill</u> | <u>2,274.1</u> |
| = Tangible equity | \$ (885.5) |

The long term debt is almost entirely bank debt. Specifically, the company has a syndicated senior secured credit agreement with various banks which consists of a five-year \$550 million revolving credit facility and two term loan facilities, Term Loan A and Term Loan B. The \$500 million Term Loan A requires principal payments of \$12.5 million, plus interest, due quarterly through September 2011, with a final principal payment of \$262.5 million due December 6, 2011.

The \$2.6 billion Term Loan B requires principal payments of \$6.5 million, plus interest, due quarterly thru September 2013, with a final principal payment of \$2,424.5 million due December 6, 2013. In its recent efforts to reduce leverage, Oshkosh paid all of the remaining quarterly principal payments on this Term Loan B facility, as well as \$110.5 million of the final principal payment.

The future maturities under the senior secured credit agreement are as follows:

| | |
|---------------|---------------|
| December 2009 | \$ 50 million |
| December 2010 | 50 million |
| December 2011 | 263 million |
| December 2012 | - |
| December 2013 | 2,314 million |

As is typical of bank debt, these loans have variable interest rates equal to LIBOR plus a specified margin. At September 30, 2008, the weighted average interest rate on these borrowings was 4.58% and 4.32% for the Term Loans A and B, respectively.

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Of course, these loans also have the standard restrictions and covenants typical of bank debt. The covenants include requirements that the company maintain certain financial ratios and restrictions on the ability of the company to consolidate or merge, create liens, incur additional indebtedness and dispose of assets. In particular, the credit agreement requires:

- (1) Maintenance on a rolling four-quarter basis of a maximum leverage ratio of 4.25x for the fiscal quarters ending on December 31, 2008 through September 30, 2009, and 3.75x for fiscal quarters ending thereafter;
- (2) A minimum interest coverage ratio of 2.50x

In each case these ratios are tested as of the last day of each fiscal quarter. As previously discussed, at September 30, 2008, Oshkosh's leverage ratio (total debt ÷ shareholders' equity) was 1.93x, well under the maximum ratio prescribed by the covenants of 4.25x. One might note that, as Oshkosh has recorded a substantial amount of goodwill on its balance sheet from historical acquisitions, the company is susceptible to write-downs in its shareholders' equity. For example, in FY2008 the company recorded a goodwill impairment (and offsetting decline in shareholders' equity) of \$175 million related to its refuse collection vehicle business, Geesink. However, with total debt of \$2,680.5 million, shareholders' equity would need to decline by at least \$758 million over the next nine months to violate the maximum leverage ratio of 4.25x ($\$2,680.5 \text{ million in debt} \div 4.25 = \$630 \text{ million of shareholders equity}$, versus current shareholders' equity of 1,388.5 million is a difference of \$758 million). Moreover, the company has not recorded negative earnings in over ten years. Therefore, with respect to its leverage ratio, Oshkosh does not appear to be in danger of violating the related debt covenant.

With regard to the minimum interest coverage ratio prescribed by the covenants (2.50x), in FY2008 the company's ratio was 3.06x. This is its lowest interest coverage ratio recorded over the past 10 years, which are detailed here:

| | <u>Interest Coverage Ratio</u> |
|------|--------------------------------|
| 2008 | 3.06x |
| 2007 | 3.27x |
| 2006 | 45.17x |
| 2005 | 33.40x |
| 2004 | 33.83x |
| 2003 | 10.05x |
| 2002 | 5.51x |
| 2001 | 4.96x |
| 2000 | 5.21x |
| 1999 | 3.27x |

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To violate the minimum allowable ratio of 2.50x, which is roughly 18% lower than the 2008 ratio of 3.06x, one of the following three scenarios would have to occur before December 2013: 1) the Oshkosh EBITDA would have to decline by approximately 18% from its 2008 level; 2) interest expense would need to increase by approximately 18% from its 2008 level; or 3) a combination of either of these two circumstances.

Valuation

Historical Method

The Oshkosh share price has declined remarkably over the past year to a level not seen since November 2001. It has declined 75% over the past 12 months and 83% from its high of over \$62 in October 2007. Clearly, the investment community is indifferent towards the U.S. military's continuing demand for Oshkosh's MRAP vehicles, and is far more concerned about the viability of the company in the current credit crisis. This is evidenced by the current price-to-book and price-to-earnings multiples at which the shares trade, versus their historical multiples, as viewed here.

| | <u>Historical Price-to-Book Value</u> | <u>Historical Price-to-Earnings</u> |
|-----------------|---------------------------------------|-------------------------------------|
| 2007 | 3.3x | 14.2x |
| 2006 | 3.5x | 18.3x |
| 2005 | 3.9x | 19.5x |
| 2004 | 3.1x | 18.2x |
| 2003 | 2.6x | 18.6x |
| 2002 | 2.3x | 16.8x |
| 2001 | 1.7x | 12.6x |
| 2000 | 2.2x | 13.1x |
| 1999 | <u>2.0x</u> | <u>10.4x</u> |
| Average: | 2.7x | 15.7x |
| Current | 0.6x | 6.6x |

Oshkosh's current price-to-book multiple of 0.6x is a small fraction of what it was in 2007, and roughly 78% lower than its 10-year historical average multiple ($0.6 \div 2.7 = -78\%$). Similarly, the Oshkosh P/E ratio is at a level far lower than any experienced over the last decade. The P/E multiples shown above are based on the average price for each year, divided by that year's earnings. Not once has this ratio been in the single digits, and since 2000 the P/E has been well over double the multiple of 6.6x (based on 2009 consensus estimates) accorded to the shares today. If the shares were simply accorded their 10-year historical average multiple of book value, the appreciation would equal 350%; on a P/E basis, appreciation would amount to 138%.

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Moreover, if the company can successfully navigate through the current crisis and emerge relatively unscathed, it will likely see an expansion in profitability towards its historical figures as well. Below, Oshkosh's return-on-assets for the prior ten years are shown.

| <u>Historical ROA</u> | |
|-----------------------|-------------|
| 2007 | 4.2% |
| 2006 | 9.7% |
| 2005 | 9.3% |
| 2004 | 7.8% |
| 2003 | 7.0% |
| 2002 | 5.8% |
| 2001 | 4.6% |
| 2000 | 6.2% |
| 1999 | <u>4.1%</u> |
| <i>Average:</i> | <i>6.5%</i> |
| 2008 * | 3.9% |

** Excluding one-time goodwill impairment charge related to its refuse collection vehicle business, Geesink.*

Oshkosh's 2008 ROA, even excluding the asset impairment charge to its Geesink business, was lower than that experienced in any year over the past ten years, reflecting rising input costs and the slowdown in worldwide demand, particularly in the second half of the year. A return in profitability to the 10-year average of 6.5% would increase the ROA by 66%. Therefore, the return in the Oshkosh shares is a function of potential price multiple expansion as well as earnings expansion. The potential return scenario is outlined below.

| | |
|----------------------------------|---------------------|
| Total assets (at Sept. 30, 2008) | \$ 6,081.5 million |
| × 10-year historical ROA | <u>6.5%</u> |
| = Normalized earnings | \$ 395.3 million |
| × 10-year average P/E ratio | <u>15.7x</u> |
| Potential market capitalization | \$ 6,206.2 million |
| ÷ Shares outstanding | <u>74.4 million</u> |
| = Potential share price | \$ 83.38 |
| vs. current share price | \$ 10.94 |
| <i>Potential return</i> | <i>662%</i> |

The above scenario might be termed a “success scenario”, or “favorable outcome scenario”, in which profitability and price multiples both return to historical levels.

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However, as previously detailed, if either the price multiple or ROA returns to a normalized level, the return potential in the shares is still quite significant. Again, if ROA were to remain at its 2008 level for the foreseeable future, but the shares were simply accorded their 10-year historical average multiple of book value, the appreciation would equal 350%; on a P/E basis, appreciation would amount to 138%.

Comparable Valuation

It is also worth examining how Oshkosh's closest competitors are currently valued by the market. However, as will be shown shortly, this highlights an inherent flaw in the comparable method of valuation. As longtime observers of the stock market are no doubt aware, the fundamental problem with the comparable multiple approach is that if an entire sector is undervalued, an individual company within that sector will appear fairly priced when in fact it is undervalued. A case might be made that at the current time, this problem is apparent in the stock market as a whole, not just with individual sectors. It is this inherent flaw in the comparable multiple approach which leads astute value investors to often employ more than one valuation method when valuing a company, including some type of absolute measure of valuation or by using the historical method as outlined above.

The following table details Oshkosh's competitors by its operating segments.

| | <u>Ticker</u> | <u>Share Price</u> | <u>P/E</u> * | <u>P/Book</u> |
|---------------------------------------|---------------|--------------------|--------------|---------------|
| Access Equipment | | | | |
| Terex Corp. | TEX | \$17.74 | 3.1x | 0.7x |
| Haulotte Group | PIG FP | €4.86 | 4.2x | n/m |
| Linamar Corp. | LNR CN | CAD 3.99 | 3.9x | 0.3x |
| Defense | | | | |
| BAE Systems | BA LN | £390.75 | 10.5x | 2.4x |
| Force Protection | FRPT | \$6.74 | 10.6x | 1.7x |
| Fire & Emergency | | | | |
| Rosenbauer Int'l | ROI GR | €21.39 | 7.6x | 2.2x |
| Commercial (Refuse Collection) | | | | |
| Dover Corp. | DOV | \$33.12 | 9.1x | 1.6x |

**Based on 2009 consensus analyst estimates*

Of the seven competitors listed, five trade at a single-digit multiple of 2009 earnings estimates. In particular, competitors within the Access Equipment industry trade at the lowest valuations, ranging from 3.1x to 4.2x earnings and less than book value.

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Competitors in the defense industry, BAE Systems² and Force Protection, trade at the highest price ratios, yet still only 10.5x and 10.6x earnings, respectively, which are no doubt lower than their historical multiples.

As Oshkosh trades at 0.6x book value and 6.6x consolidated earnings, a sum-of-the-parts analysis based on comparable multiples would only serve the purpose of showing that the company is trading roughly in line with competitors. However, a company trading in line with competitors and a company being fairly valued are not one and the same. The historical valuation method discussed previously shows that, although Oshkosh is valued similarly with its competitors, this does not mean substantial appreciation potential does not exist. On the contrary, the competitor valuations perhaps reveal only that an unusually high risk premium is being placed on equities across most industries.

Investment Summary

The risk premium accorded by investors to the Oshkosh shares is so substantial that the company trades at price-to-book and P/E multiples not seen in over ten years. Although the incoming Presidential administration appears committed to the company's ceramic-plated MRAP vehicle, and although the company recently announced the expansion of its Access Equipment segment in China, the investment community appears solely focused on the damage that might be inflicted by the current credit crisis. Essentially, the Oshkosh share price reflects the widespread belief that the current disequilibrium in the credit markets is at least semi-permanent. However, if one believed that the current credit condition as it exists today is unlikely to exist in some future period, the return potential in Oshkosh is quite substantial. Therefore, the Oshkosh shares are recommended for purchase at this time.

² BAE acquired Armor Holdings, Inc. in July 2007. A *Contrarian Research Report* on Armor Holdings was published on January 31, 2006

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OSHKOSH CORPORATION CONSOLIDATED STATEMENTS OF INCOME

(In millions, except per share amounts)

| | Fiscal Year Ended September 30, | | |
|---|---------------------------------|------------|------------|
| | 2008 | 2007 | 2006 |
| | _____ | _____ | _____ |
| Net sales | \$ 7,138.3 | \$ 6,307.3 | \$ 3,427.4 |
| Cost of sales | 5,955.0 | 5,204.5 | 2,819.1 |
| | _____ | _____ | _____ |
| Gross income | 1,183.3 | 1,102.8 | 608.3 |
| Operating expenses: | | | |
| Selling, general and administrative | 532.5 | 446.6 | 274.0 |
| Amortization of purchased intangibles | 69.3 | 65.9 | 8.4 |
| Intangible assets impairment charges | 175.2 | -- | -- |
| | _____ | _____ | _____ |
| Total operating expenses | 777.0 | 512.5 | 282.4 |
| | _____ | _____ | _____ |
| Operating income | 406.3 | 590.3 | 325.9 |
| Other income (expense): | | | |
| Interest expense | (212.4) | (200.8) | (7.4) |
| Interest income | 7.4 | 6.3 | 6.6 |
| Miscellaneous, net | (10.9) | (0.1) | (0.2) |
| | _____ | _____ | _____ |
| | (215.9) | (194.6) | (1.0) |
| Income before provision for income taxes, equity in earnings of unconsolidated affiliates | | | |
| and minority interest | 190.4 | 395.7 | 324.9 |
| Provision for income taxes | 118.1 | 135.2 | 121.2 |
| | _____ | _____ | _____ |
| Income before equity in earnings of unconsolidated affiliates and minority interest | 72.3 | 260.5 | 203.7 |
| Equity in earnings of unconsolidated affiliates, net | | | |
| of income taxes of \$2.7, \$3.1 and \$1.4 | 6.3 | 7.3 | 2.3 |
| Minority interest, net of income taxes of \$0.1, \$0.1 and \$(0.2) | 0.7 | 0.3 | (0.5) |
| | _____ | _____ | _____ |
| Net Income | \$ 79.3 | \$ 268.1 | \$ 205.5 |
| | _____ | _____ | _____ |
| Earnings per share: | | | |
| Basic | \$ 1.07 | \$ 3.64 | \$ 2.81 |
| Diluted | 1.06 | 3.58 | 2.76 |

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CONSOLIDATED BALANCE SHEETS

| | September 30, | |
|--|---------------|--------------|
| | 2008 | 2007 |
| Assets | | |
| Current assets: | | |
| Cash and cash equivalents | \$ 88.2 | \$ 75.2 |
| Receivables, net | 997.8 | 1,076.2 |
| Inventories, net | 941.6 | 909.5 |
| Deferred income taxes | 66.6 | 77.5 |
| Other current assets | 58.2 | 56.5 |
| | 2,152.4 | 2,194.9 |
| Total current assets | | |
| Investment in unconsolidated affiliates | 38.1 | 35.1 |
| Property, plant and equipment, net | 453.3 | 429.6 |
| Goodwill | 2,274.1 | 2,435.4 |
| Purchased intangible assets, net | 1,059.9 | 1,162.1 |
| Other long-term assets | 103.7 | 142.7 |
| | 6,081.5 | 6,399.8 |
| Total assets | \$ 6,081.5 | \$ 6,399.8 |
| Liabilities and Shareholders' Equity | | |
| Current liabilities: | | |
| Revolving credit facility and current maturities of long-term debt | \$ 93.5 | \$ 81.5 |
| Accounts payable | 639.9 | 628.1 |
| Customer advances | 296.8 | 338.0 |
| Payroll-related obligations | 104.8 | 105.0 |
| Income taxes payable | 11.1 | 64.0 |
| Accrued warranty | 88.3 | 88.2 |
| <u>Other current liabilities</u> | <u>228.8</u> | <u>243.2</u> |
| Total current liabilities | 1,463.2 | 1,548.0 |
| Long-term debt, less current maturities | 2,680.5 | 2,975.6 |
| Deferred income taxes | 308.9 | 340.1 |
| Other long-term liabilities | 237.0 | 138.7 |
| Commitments and contingencies | | |
| Minority interest | 3.3 | 3.8 |
| Shareholders' equity: | | |
| Common Stock (\$.01 par value; 300,000,000 shares authorized; 74,545,337 and 74,235,751 issued, respectively) | 0.7 | 0.7 |
| Additional paid-in capital | 250.7 | 229.2 |
| Retained earnings | 1,082.9 | 1,036.3 |
| Accumulated other comprehensive income | 55.7 | 129.0 |
| Common Stock in treasury, at cost (116,499 and 28,073 shares, respectively) | (1.4) | (1.6) |
| | 1,388.6 | 1,393.6 |
| Total shareholders' equity | | |
| | 6,081.5 | 6,399.8 |
| Total liabilities and shareholders' equity | \$ 6,081.5 | \$ 6,399.8 |