
Selected Insights and Ideas by Bob Robotti

Prepared exclusively for participants of Ideaweek 2018, St. Moritz, Switzerland

*CONFIDENTIAL – may not be shared or otherwise distributed
without express written permission by john@moiglobal.com*

Table of Contents

Robotti & Company Annual Meeting Highlights

(edited transcript of remarks by Bob Robotti in November 2017)

The Role of Active Management in the Modern World

(edited transcript of conversation with Shai Dardashti in 2017)

Latticework Panel on Active Management

(edited transcript of discussion featuring Bob Robotti, Michael van Biema, and Andrew Burns, moderated by Jim Basili, held in September 2017)

The Supply/Demand Dynamics of Oil

(Q&A with Bob Robotti, dated November 2015)

Presentations at MOI Global Online Conferences

SEACOR Marine, 2017

Finning International, 2017

Subsea 7, 2015

LSB Industries, 2014

This article is shared by MOI Global instructor Robert Robotti, the founder, president and chief investment officer of Robotti & Company Advisors, based in New York City. Bob is an instructor at [Best Ideas 2018](#), the fully online conference featuring more than one hundred expert instructors from the MOI Global membership community.

On November 13, 2017 Robotti & Company Advisors, LLC hosted its annual investor meeting at The Yale Club in New York City. The highlights below, delivered by Bob Robotti, have been edited for clarity.

“Thirty four years ago, a handful of us here in the room started a business with the concept that by doing fundamental bottom-up stock research, we could identify companies that would outperform the market. That is what we have done and it has always been the mandate of the business. Now this is a concept that is simple to say, but is not necessarily so easy to achieve. We believe now, as then, opportunities still exist in the marketplace.

By focusing on the longer-term prospects of a business and not just looking at the short-term, immediate outlook, we think we can identify companies that are substantially mispriced and mis-valued by the market. This takes us to places that are not typical, so there is very little-to-no overlap between what we own and what is found in the popular indices.

Of course, we know that over the long-term there will be periods when we will underperform the market. We think an important component of long-term success is the appreciation and realization that during these periods of underperformance you must remain consistent, and stay true to what you understand and the variant view you have developed versus the market.”

Investing in building distribution companies

“One of the things that we do is invest in cyclical businesses. We think that cyclical businesses often provide us with an opportunity to buy when the price per share is significantly less than the normalized earnings power value of the business. Back in 2003-2004, which is where we have to go to understand our housing related investments, we invested in manufactured housing. This was a mistake and didn’t work out in the short-term. Our visits to manufactured housing plants informed us that this is an efficient way to build a home. If you use the same materials that you do on a site built home, the quality ends up better because you have a controlled environment, which includes supervisors making sure the laborers didn’t go out for 3 beers at lunch and forget to install the insulation. Since the quality was better and the cost per square foot was lower we figured manufactured housing was an out of favor industry that would have a revival.

The problem was that in 2005-2006 the federal government stopped buying mortgages for manufactured homes. So a homebuyer could buy a \$200k site built home for less money down, with a reverse amortization mortgage leaving them with a lower monthly payment for that site built home than for an \$80k manufactured home. This meant a recovery would be

significantly forestalled. In 2009, Alan Weber, a long-time colleague of ours said, 'Go visit Builders FirstSource - a distributor to the homebuilders.' We first invested in Builders FirstSource back in 2009 estimating that we were paying 2x normalized EBITDA for a business that was not a buggy-whip business - so it wasn't going away. Yes, it did have significant financial headwinds, so from 2009 to 2011 we looked wrong. The stock traded from \$3.40 down to \$1.70, so we bought more.

As value investors we often purchase too soon but we continued to have conviction in our investment thesis. The industry had gotten closer to a recovery while the valuation had gotten dramatically cheaper. In the meantime, there was a competitor that was coming out of bankruptcy. By 2010 we had accumulated a 15% position in the equity of that post-bankruptcy because its valuation was a fraction of Builders FirstSource's and it also had better cash flow characteristics. In 2012 I joined the board of that company and was a director of BMC over the time that sales grew from \$650 million to \$1.3 billion. The company reverse-merged into a competitor, Stock Building Supply (which interestingly generated roughly the same revenue as BMC but only ½ the EBITDA). That window is an important part of our process - we get involved with our investments, we are shareholders for a long period of time and we become active with the company as friendly, cooperative shareholders which sometimes leads to becoming a director of the company.

The base premise of our investment in this sector is that single family homebuilding is dictated by irrefutable demographic trends. While there are plenty of headwinds that still persist for the business, we think those long-term demographic trends will win out over time. So you have an industry that today will build about 800k single family homes while the 50 year average is between 1.1 - 1.2 million single family homes or 40% - 50% above the current level of activity. For 10 years single family homes built have been significantly below that long-term average. There were definitely too many single family homes built in 2006 and 2007 but those have all been absorbed into the marketplace while inventory continues to come down. So we ask: What is the normalized level of activity in this business? And that is really what we are looking to do - invest in cyclical businesses at low points in the cycle when you can buy the business at a significant discount to its normalized earning power value and then hold the business for a long-period of time.

Of course, what you really have with cyclical businesses is that they often go through a catharsis. The competitive landscape winnows down through industry consolidation. At the same time internal processes improve lowering cost structures. This results in growth of the normalized earning power of the survivors. We believe the long-term mid-cycle earning power of Builders FirstSource, for example, is between \$4 and \$5 while the stock price is currently in the high teens. So it trades at a single digit P/E multiple of our estimate of the normalized earning power of the business. Demographic numbers continue to grow meaning that a reversion to the historical mean is really a modest expectation."

Energy

"You shouldn't believe everything that is written in the newspaper! Articles in the newspaper are written by someone who may have above-average writing skills, but probably doesn't understand the core tenets of a business. So if you are a journalist and you are

writing about the energy business, you end up reporting what people tell you and they usually tell you about what is in the news or what might make a good headline. We think there are huge misunderstandings about what the real dynamics are in the energy industry. I'm referring to conventional energy, though we closely follow renewable energy as well.

An important fact is that natural gas accounts for half of the hydrocarbons produced in the world today. And while natural gas doesn't grab headlines, the fact is that natural gas is a growing source of energy, it is a bridge fuel and it is less carbon unfriendly. This means that oil is not necessarily the only driver of energy anymore as natural gas consumption grows.

Natural gas also represents a tremendous opportunity for America. North America has a 10 to 20 year oversupply of natural gas which has caused a disconnection between the price of energy in North America and energy prices worldwide. The price of natural gas is roughly \$3 per MMBtu in the U.S. and \$2 per MMBtu in Canada. This translates to an energy equivalent price of \$12 - \$18 per barrel of oil. So even at today's oil prices in North America there is a huge arbitrage opportunity. This is a very important driver and is also extremely positive for the U.S. economy given that energy intensive businesses in North America are competitively advantaged against other energy intensive businesses anywhere in the world. We think these dynamics will continue to play out for at least the next decade.

We also think energy markets will continue to come into balance as oil consumption continues to grow - even though we don't know what the longer-term future holds. My nephew recently tried to get me to buy an electric car. In fact, I don't own a car anymore and I primarily use shared vehicles - I am a part of the new millennial economy! These are examples of what is coming and will clearly be an important factor that eventually enter the equation. In the meantime, older wells which represent 1/3 of North American production have been declining at double-digit rates for the past two years. So U.S. onshore shale oil producers are depleting reserves while telling everyone that they are economic at \$50. We believe that this is not only false but is also exacerbating the problem. Instead, our contrarian view is that over the next year or two the risk is that we are actually short oil which would lead to a spike in its price.

In our portfolio we own companies' related to offshore production because the other general perception is that onshore is economic at \$50 and therefore offshore is dead - both of which are false. Offshore is not dead. Just like onshore, offshore economics have dramatically and significantly improved as a result of technological advances and cost reductions. We have already seen signs of increased activity although investors don't seem to be buying into it yet. Over the next year we will see offshore activity continue to pick-up. For now, investors continue paying high prices for uneconomic onshore stocks while shorting the stocks of offshore companies because "offshore is dead." We believe these investors will be wrong on the long and wrong on the short."

Are there any risks that keep us up at night?

"There are two risks that everybody seems to be thinking about. The first is that the markets keep hitting new highs every day. Of course, the other is that we all know that the two of us (Bob referring to himself and Isaac Schwartz) are dinosaurs because we pick stocks in a

market where passive investing reigns and active management is dead. Of course we don't believe this and we think this actually creates an opportunity for us. It is true a tremendous amount of capital has flowed out of active strategies and into passive ones where there is no regulator since valuation is irrelevant to this process. As a result, fewer and fewer companies have higher and higher valuations driving higher market levels that are no longer constrained by valuation.

What we do as investors is very different because our philosophy is all based on valuation. Valuation is our real litmus test for whether or not an investment makes sense. Is this a good business? Does it have a good balance sheet? Is there an owner operator? These are all very important questions but only so far as they help determine valuation. We look for companies where the valuation can be understood and appreciated and we can therefore determine whether there is a margin of safety and an opportunity to profit. We believe that the fundamentals of a company is what really drives performance over time which is why it is so important to stick to what you know.

I don't think there is much risk of a 2008 event, which was a worldwide financial crises where there was really no safe haven and everything was at risk of being worth a lot less. I think what we have now is a valuation issue which causes a lot less concern for us. Yes, there could be an event that is perhaps analogous to 1987 where you had portfolio insurance that was touted as a guaranteed way to make sure you don't lose money while you get a great rate of return, similar to the way many perceive passive investing today. We believe the markets are laying the groundwork for future opportunity. As more money goes into things without regard to valuation, active managers will have an easier time identifying stocks that really are disconnected from their underlying economic opportunities. That is exactly what we look for as an active manager."

The above text is an excerpt of certain comments made by Robert Robotti at the 2017 Annual Meeting of Robotti & Company Advisors, LLC ("Robotti Advisors") with respect to its separately managed account and business and private fund business. The above excerpt should be read in conjunction with the following disclosure information: This information is for illustration and discussion purposes only and is not intended to be a recommendation, or an offer to sell, or a solicitation of any offer to open a separate account managed by Robotti & Company Advisors, LLC, nor should it be construed or used as investment, tax, ERISA or legal advice. Any such offer or solicitation will be made only by means of delivery of a presentation, prospectus, account agreement, or other information relating to such investment and only to suitable investors in those jurisdictions where permitted by law. Further, the contents of this letter should not be relied upon in substitution of the exercise of independent judgment. The information is furnished as of the date shown, and is subject to change and to updating without notice; no representation is made with respect to its accuracy, completeness or timeliness and may not be relied upon for the purposes of entering into any transaction. The information herein is not intended to be a complete performance presentation or analysis and is subject to change. None of Robotti & Company Advisors, LLC, as investment advisor to the accounts or products referred to herein, or any

affiliate, manager, member, officer, employee or agent or representative thereof makes any representation or warranty with respect to the information provided herein. In addition, certain information has been obtained from third party sources and, although believed to be reliable, the information has not been independently verified and its accuracy or completeness cannot be guaranteed. Any investment is subject to risks that include, among others, the risk of adverse or unanticipated market developments, issuer default, and risk of illiquidity. Past performance is not indicative of future results. If interested, please contact us for additional information about our performance related data. The attached material was provided to investors in a specific Robotti Advisors vehicle at a specific past point of time, advice that may no longer be current or timely. References to past specific holdings of that specific vehicle and matters of related historic fact must be seen in context (as would have been apparent to investors in that vehicle) and are not intended to refer directly or indirectly to specific past recommendations of Robotti Advisors (other than as an indication of language sometimes found in the newsletters). Any reference to a past specific holding or outcome is not intended as representative. None the less, for individuals actively interested in investing in such vehicle, a list of recommendations made by Robotti Advisors with regard to the vehicle in question will be made available on request. Note: certain statements on the attached material, including but not limited to (a) statements of things that "are well known" to be the case (other examples include: "In hindsight people often say, "I should have known better," and more often than not, they did."), (b) statements with the phrase "always", and (c) certain similar statements, are not intended to represent absolute literal fact, but rather represent certain colloquialisms/mannerisms expressed by select market participants (but not necessarily individuals associated with Robotti Advisors). Opinions contained in this letter reflect the judgment as of the day and time of the publication and are subject to change without notice and may no longer represent its current opinion or advice due to market change or for any other reason. Robotti Advisors provides investment advisory services to clients other than the separately managed accounts, and results between clients may differ materially. Robotti Advisors believes that such differences are attributable to different investment objectives and strategies between clients. The information provided herein is confidential and proprietary and is, and will remain at all times, the property of Robotti Advisors, as investment manager, and/or its affiliates. The information is being provided for informational purposes only. A copy of Robotti & Company Advisors, LLC's Form ADV, Part 2 is available upon request. Additional information about the Advisor is also available on the SEC's website at www.adviserinfo.sec.gov

In an episode of the [Latticework Podcast](#), presented by MOI Global, Shai Dardashti speaks with Robert Robotti about the role of active management in the modern world.

Bob is president of Robotti & Company. Prior to forming the firm in 1983, Bob was a vice president and shareholder of Gabelli & Company, Inc. He worked in public accounting before coming to Wall Street and is currently an inactive CPA. Bob holds a BS from Bucknell University and an MBA in Accounting from Pace University. Some of Bob's areas of coverage include special situations, energy, property-casualty insurance, and banking.

Bob is an instructor at [Latticework 2017](#).

The Latticework Podcast is on [iTunes](#), [Soundcloud](#), [Stitcher](#), and [TuneIn](#).

The following transcript has been edited for space and clarity.

Shai Dardashti, MOI Global: Before we talk about the Latticework 2017 conference, please tell us more about your background.

Bob Robotti: I graduated from college and worked for a small accounting firm. I did both audits and taxes; therefore, I had a breadth of different kinds of knowledge. It was interesting to see many different businesses, and to understand the limitations of what auditing can tell you and not tell you, and to learn accounting, because accounting is the language of business. Understanding financial statement construction enables you to better deconstruct financial statements, to understand what the economic reality is that's underlying a business. I was also very fortunate that the accounting firm actually audited a number of investment advisers. Early on, I used to work on the audit of Tweedy, Browne. Of course, Tweedy, Browne is a legendary firm that's been in the value investing space since its inception; it is part of the genesis of this segment of the investment community.

When Ben Graham closed up shop, half the people from Graham-Newman walked into Tweedy's office. Therefore, what I knew when I first got out of school was what Tweedy owned, what they bought, what they sold. It was not only the Tweedy people. In talking with them, it's a smaller firm – therefore I knew Ed Anderson, who ran the firm at the time. I knew John Spears, who was new to the firm, and Chris Browne. In addition, I also knew Eddie Schloss well – he's Walter's son. We're about the same age, and I think the first stock I've ever bought was something that Eddie suggested to me.

We were also fortunate enough to audit Gabelli & Company; for three years, I worked for Mario Gabelli – and that's what I tell everybody. Back then, the focus of the firm was really his brokerage business, because he was originally a sell-side research analyst. Every morning we had a meeting and he went through his favorite investment idea. So, I say I had an executive MBA program that was taught one-on-one by Mario Gabelli to me, and he paid me to attend his class. I didn't have to pay him.

So, of course I had been bitten by the bug, and I had the right orientation. Fortunately, I didn't take finance in college and find out about efficient markets and all kinds of misinformation. I wasn't in any way corrupted through that process. And of course I really wanted to pick stocks, because all of us who get a passion for that, that's what we want to do. I went out and started my own firm, since Gabelli didn't need me to pick stocks when he was managing, when I left, \$77 million dollars – only. He very clearly had the capability to pick whatever he needed to fill up his portfolios. That's how I got into investing. I also think that formed how we've thought about investing, because Tweedy very much is more a Ben Graham, balance-sheet oriented, cheap-stock kind of purchaser, as was Walter Schloss. And that's what we did. We bought cheap stocks.

Having done this for over 30 years, what you realize is that many cheap stocks are cheap for a reason – and the reason is that they can't generate a return on the capital they have. Book value is an accounting number, it's not an indicator of future economic values. Therefore, there's a lot of misleading information, and there's a lot of companies that you end up investing in that are not particularly good investments. That's the evolution we've had over time, having invested in cheap stocks and having some that did work out.

Why did some work out, and why did some not work out?

There are two classes that we found. One of them is controlled by somebody who was a smart capital allocator; therefore, not only were the assets cheap, but management was constantly looking at moving those assets and reinvesting those assets to get higher returns – to grow value – because there was an alignment between management's ownership and our ownership.

And the other group of what has worked: we often found that we invested in cyclical businesses that were at depressed valuations because the outlook of the business, in the short term, was extremely negative. Therefore, a lot of what we do today is focused on trying to identify cyclical industries – cyclical companies, cyclical businesses – and identify who's going to be the survivors in the business, who potentially has product differentiation, and who understands the cyclicity of their business and therefore can work with the advantages of that. There clearly are advantages, absolutely, in the bottom points of the cycle; there is the opportunity to acquire significant assets that have high earnings power at very modest valuations. Therefore, to deploy capital at the right time is potentially a huge positive.

Dardashti: 'The Role of Active Management in the Modern World' – how do you begin to think about that question?

Robotti: Well, clearly we've always come from a bottom-up stock-picking culture, and we continue to believe that there is value in that and the markets' inefficiencies are there because of human nature. We don't think that any of those rules have changed. Therefore, the fundamental underlying reason why markets are not efficient is the intervention of people, and we think that people today have all the same biases they've always had. We think there's plenty of ways, potentially, that's playing out today. And that's causing valuations to significantly diverge from the intrinsic values of businesses, potentially

businesses that are valued today at significantly less than what their intrinsic value is. We actually think that as the market becomes more institutionalized, and whether it's indexed directly or indexed indirectly, what you really have is people picking stocks not based on any kind of fundamental analysis. In our minds, the role of active management – stock selection and differentiation – is inherently more logical, and that it should be the right tool to differentiate performance over time.

Dardashti: What do you think about the overlay of mechanical trading, computer algorithmic trading, even artificial intelligence? How do you think through that challenge?

Robotti: A month and a half ago when Blackrock came out and said, “we’re going to do all this AI, a lot of artificial intelligence,” a friend of mine said, “Bob, you’d better watch out because they’re going to have a computer that will invest just like you, so you’ll be displaced.” I said, “I don’t know why Blackrock would waste money trying to figure out how I invest and try to replicate what I’m investing in. There’s a lot more ways that they could deploy capital much more intelligently; they can deploy and allocate significant dollars of capital as opposed to the small amounts we do.”

In terms of stock selection and the companies that we’re looking at, I just don’t see artificial intelligence coming into play any time in the foreseeable future. Of course, I’m not a technology person, so maybe I’m misunderstanding and misstating and being naive about that process.

Recently, someone who I do respect was talking about a very large firm who clearly must have some kind of institutionalized process, because when he looks at the companies in his universe – a lot of them we jointly own – he said, “It’s amazing how often they show up in those companies. They’re doing something that’s like what we’re doing.” So, there is some capability, and there is clearly something that people are attempting to do, but a lot of what we do is also industry specific.

Energy is an industry that I’ve invested in for over 40 years. I think I have an understanding of how the business works. What the perception is and what the reality is are frequently very different in that business, and especially at the tops of cycles and bottoms of cycles. I think I have some industry-specific knowledge about how those businesses work, and therefore which businesses are well-positioned and should do well over time. Even if there’s some computer that’s figuring out something that I’m doing, I think I still have enough specific information.

Also, we manage a modest amount of capital – there’s not a lot of things we have to pick differently; just a few things can really move the meter for us, but it’s not going to move the meter for somebody else who’s got a large amount of capital that they’re looking to deploy.

Dardashti: From your vantage point, do you find that history rhymes?

Robotti: Rhyming, of course, is exactly right. It doesn’t repeat – it rhymes. There’s some similarities, but there’s probably a lot of disparities between today’s markets and where they were in 1998 and 1999. The number of companies that had no economic model and had

valuations that were extremely expensive was easier to see. Today that's not nearly as pervasive, or that there's as much capital flowing into things that are as separated from fact and reality, in terms of valuation.

Dardashti: With the advent of the Internet, people might have said the same thing in the 1990's - "there's going to be a much more efficient market, there's no more easy opportunities."

Robotti: That brings up the question, what's your analysis? What's your time horizon? What are you looking for? And I would think that there's more time spent on how to outperform the market in the short-term than on how to outperform the market in the long-term. Therefore, stock selection is also different. What metric are you using? Is it a three- to five-year time frame, or is it a one-year time frame? How you would pick a portfolio is different based on whether I want to outperform in the next year or whether I want to outperform over the next five years. Although, I guess you could model a computer to do the same thing, to think "OK, I don't want an immediate reaction." The fact of the matter is that it won't attract much capital because it's going to potentially underperform in the short term; it's really not focused on short-term performance.

Dardashti: Are you finding there is more efficiency in smaller territories?

Robotti: In certain cases we see more inefficiency, because what you do see is one or two companies that are in indices, and that occasionally have real volatility where the stock price is. Of course if someone wants to buy the index, and it's a member of the index and it has limited liquidity, that doesn't matter, because you need to fill up that allocation in those proportions. We do see, occasionally, that some of our securities have very high volatility, which provides opportunities for us to sell some stock and buy some stock.

Dardashti: If we invert the question, what is not the role of active management in the modern world?

Robotti: Of course, I fundamentally do believe that over the long-term the idea of indexation is an extremely valid thing for the average investor. Because, on average, active managers are still going to be large institutions who are still going to have next quarter's performance, next year's performance, and bonuses on their minds - they'll lose their job if they don't outperform. So the institutionalization - which has always been the case - of investment means that the focus you have to have if you manage a large amount of money actively, is still "what's the short-term performance going to be?" Whether your computer is designed to look at what the short term is, or whether it's not, you're too focused on job preservation to be concerned about the short term.

Most active managers, of course, over time have underperformed the index, and that's because of all those factors. And, if anything, these factors are stronger today than they were before. So, the idea that you're going to be able to pick the active manager who's going to outperform the other active managers and outperform the market is difficult. For the average investor, I would think there's a concern that someone who's indexing today is potentially indexing at a time when there's so much indexation that's moving, it's moving

valuations. And therefore, what are you buying? You're tending to buy things that are more expensive – in an expensive market. Therefore, it would seem that buying the more expensive companies in a more expensive market is not, potentially, a formula for long-term investment success. It may be the wrong time to move from active management to indexing – but over time I think there is a real role for indexing. It makes a lot of sense, and probably for most people it is, probably, a better option.

Dardashti: I know you're far too humble to bring this up yourself, so let me raise the point: You've made quite a bit of money by actively investing in certain cycles. Can you share a brief case study of intelligent active investing done right?

Robotti: I think it's pretty well determined that you don't need a lot of winners. You just need the right winners in the right size that therefore have a big impact on performance. One of the ones that I've have talked about in the past is the biggest loser I've ever had – my investment in what was then called Ethyl Corporation. We bought it originally in 1998, and the reason we bought it in 1998 was because in 1997 the company did a significant buyback of stock. The Gottwald family has a long record of significant insider ownership, and allocating capital intelligently. What we had seen in the company was that they had acquired one or two competitors. The industry had consolidated down to an oligopoly, and they didn't see any opportunity to buy out the other three remaining people. They therefore bought back a piece of their own business, as an opportunity they believed in at the time. The facts worked out in the short-term; in the intermediate-term they were wrong. They levered up the company and they bought back stock.

So a year later when it was down 20%, we bought some stock and said, "Hey this is interesting; the right kind of people, the valuation is less than what they think the intrinsic value is." But when they did buy it back, A, there was the leverage, but B, there were also the market dynamics. Chevron had built the plant, the 1997 Asian financial crisis had happened, and the demand for the product had slowed. So the supply-demand got out of balance, and supply was greater than demand. Therefore, the industry had no pricing power even though it was an oligopoly. So, cyclically it was at the wrong part of the cycle – when they had levered up.

We bought the stock consistently as it continued to go down, figuring every time it went down, "Yes, but the intrinsic value of the business is still significantly higher than where it is, and who cares about where we got in; we only care about where we are today." And we continued to be wrong, because the business continued to get more difficult. The business didn't get more difficult in the later years, as it continued to dwindle down because the debt was getting paid down and because it was generating significant cash, and they were deleveraging the balance sheet.

As I said, I think our original purchase was \$35, and it did get down to \$3 a share, so we bought more stock at \$3 a share. Three dollars a share, it had 17 million shares outstanding, so the market cap of the company was less than their annual spending on R&D. We thought that there was something significantly out of whack with the value of the business and what it was being valued at. Of course, in the meantime, nobody would have bought the stock. There would have been no indicators for it. There was no analyst coverage. Who cared

about a company that had a \$50 million market cap? And then, as it played out, the stock actually started to recover. The debt had been significantly paid down, but the important thing that had happened was that the leader in the business was Lubrizol.

Lubrizol always said, "We're going to grow the business." The problem was that this is not a growth business, it's a 1-2% growth business; and since they were trying to grow, that limited the cash flow and the profitability of the business. They acquired another the company that made, I think it was hair care product chemicals - and suddenly that business had growth. So, they didn't need growth in this business, and they said, "We're going to manage this business for cash returns." Fundamentally, the price leader in the industry changed. In the meantime, in supply-demand, the demand had grown slowly over time but there was no new capacity that came online, so you had balance. And then you had one year to see that, where the earnings were flat. They would raise prices, led by the result of the price leader - but immediately the cost of oil went up and that was a key raw material, so the margin never went up.

They raised the price again; oil prices went up again, so once again the margin was compressed. This happened four times in a row. The fifth time, I'm like, "This industry has pricing power. One of these times oil is not going to go up again and therefore the margins are really going to expand. And if you look at where it is today, this company is going to generate \$4 in cash, and it's a \$15 stock, and the debt now was down from \$700 million to \$150 million. So therefore it's a manageable amount of debt, with free cash flow generation, and a \$15 per share valuation on it."

That's when I doubled up on the stock I owned. I became a 13-D holder in the company. I think I owned about six percent of the company. That was a huge turnaround. So along those lines, it would be difficult for anybody to see how they could replicate that purchase pattern that I would do. And then I also bought a lot more, at \$15.

I remember speaking to the CFO, telling him, "You can earn \$4 next year." And his concern was, "From your lips to God's ears. I just lived through the last seven years. There were times where we weren't so sure we were going to come out the other end, so it's been a difficult time." His attention span had also been shortened dramatically, he couldn't look out; his conviction that things would play out was reduced, because he's probably been wrong multiple times over the last eight years on what his projections were, he knew he had no reliance on his own capability to generate those ideas. And then, of course, that's where it became the biggest loser for us. Fifteen months later, stock was trading at \$38 and so nine and a half times free cash flow. It seemed to me like a low-growth business. Maybe it's not a bad sale.

And of course, I sold out the rest of my stock at the end of 2013 after we got a \$25 dividend. I think it earned 16 dollars a share that year, at \$275 a share. The sales that I made continually up to that on - and of course, today it trades at \$470 dollars a share. I forget what the earnings are. Today it's not a cheap stock. But still, how that all worked out, how that played out, how our ability to identify something and then stay with it and have that conviction - it ended up being a really great return for us. That was really important to our performance.

Dardashti: If I heard correctly, you started at \$30 share, it went down to \$3 at one point; approximately what years are we talking about?

Robotti: 1998 to 2003. Then, 2005 is when we made the big investment. We bought a lot of stock at \$15 when it had started to recover.

Dardashti: On the question of rhyming, would you say your housing investments have been a similar narrative?

Robotti: The 2008 financial crisis was definitely exacerbated, but it created what was the worst housing environment in the history of post-war times. You had 450,000 single-family homes constructed in 2009, and the previous low was about 800,000 homes, and that was back in 1982. In 1982, we had 220 million people in America and maybe had 70 million households. In 2009, you have 315 million people in America and you have 110 million households – to do, really, half the volume or two-thirds of the volume in terms of new home construction. That's off the map, and it stayed there for three years. This was an unprecedented depression in that business, and the industry therefore has evolved and changed. I would suggest today it is, in many ways, a different industry. That is really interesting, we think.

And therefore you can't look at past cycles, because the past cycles were not like this cycle, and to think the recovery will be like those cycles, I think, is a mistake. I think it's in uncharted territory, but there's still a cycle. How do cycles work? What does capacity shrinkage look like? What does it look like for the survivors? What differentiation is there? How does that all work? We have a five-year view.

People are always talking about housing starts, and housing starts are both multi-family and single-family, and so we really focus on the single-family housing starts. That's because a single-family housing start is really three times the volume, at least, of wood or any of the other products that go into a home. Therefore, if you say we're at 1.2 million home starts today, well, okay; but if you look behind it, there's 400,000 multi-family homes. That means the single-family number is still off the charts in terms of low activity levels. We think it'll get back to the normalized number of 1 million, 1.1 million. I believe we'll probably get to even higher levels. So, even though household formation is more difficult to track, and that's the real leading indicator, it's still somewhat population and household based.

The idea is that the new generation of people are different, and millennials are all going to rent in urban areas. I kind of think – having gotten out of college in 1975 – we all wanted to live in urban areas and rent. Therefore, seeing how people change, and they meet someone, and then they don't have the roommate, and then, if it's a male and a female you end up – and even if it's not – people want to have children, therefore you end up with children. You like to stay in the city; but the next thing you know, you'd like to have a backyard, and the cost of living in the city is really expensive. The cost of living, even in a suburban area around the New York area, is significantly less than living in the city, and they've got fine schools, and whatever else.

I think that evolution happens every place, and I think it applies even more so in the rest of

the country as opposed to New York. So, I think that there's a big cycle. And there are implications of that, and how we think that applies for who sells what product, or who distributes what product, and what the implications are for the earnings, what the operating leverage is in each of those businesses, and therefore, what the free cash flow generation is. When I look at Builders FirstSource, I say that you can't look at the historical numbers because there's no historical number that's of relevance to the way the business is today. You need to come up with what you think the number is going to be in five years' time.

Dardashti: I would love to explore how you think knowledge becomes wisdom.

Robotti: There is no such thing as someone who has all the wisdom or has none of the wisdom. I'm getting more wisdom every day. Irving Kahn was someone I knew reasonably well; he lived to be 109, and he came into the office every day to 107. I hope to emulate Irving and be in the office, and therefore I've got 40 years of experience to go. I would expect that 40 years from now I'll have a lot more wisdom than I do today, because I still do things I shouldn't. I'm foolish about things. Wisdom is a continuum. It's not attaining some state of full wisdom. I'm not there, for sure.

Dardashti: We are very grateful that you're going to be attending Latticework 2017. You're sharing your wisdom with our community. Why are you sharing so much of your time, and why are you so committed to this endeavor?

Robotti: The main reason I think I do it is because I think it's pretty obvious that I love what I do, and so talking about things that you do, and you love, is kind of exhilarating. Therefore, I love to talk about what I do. That's one of the main reasons.

It would be great if something came out of it. The one thing that I would hope most to potentially come out of is to identify someone who has the same kind of passion for our business that we do. Because the growth of the business has really been predicated on compounded returns of the capital we've had. I am 63, and my capital is also people who are my age, and older. There is some generational kind of attrition that I'm expecting in the business, so therefore to have more capital would be an opportunity, mainly for the people who were here, who were part of the process with me. Therefore, there's a real future in a career for them.

Dardashti: If I could clarify this - financial capital, human capital, or both?

Robotti: I'm looking for people. I'm looking for a person who could help us market, and raise assets from the right kind of investor, because that's really important. I've also had the benefit of knowing that the huge advantage we've had is that the capital we've had has been with us for a long time and is extremely patient. So when we have a year or two when we're underperforming, and we're looking stupid, they have fortunately been with us long enough to know, "No, they know what they're doing and we've been through this before, he's had periods of underperformance." Having capital that aligns with how you invest is clear and fundamental to executing a long-term investment strategy, right? You can't have short-term capital and execute a long-term investment plan. You only want the right people who are aligned with how you think about investing.

Dardashti: Bob, you have shared your perspectives with us at ValueConferences and with MOI interviews. I hope you've received quality feedback over the years.

Robotti: That's an interesting question. I don't know if I've gotten enough feedback from the entire world. I don't know if I get honest feedback. I think people are basically kind, especially if they meet me and they say, "He's really not too bright, so let me be kind to him." I think they're kind to me.

Dardashti: If I could turn the tables, what kind of feedback would you suggest is most value-add?

Robotti: Different ideas are, clearly, the most valuable thing that you can have, right? For me to think expansively – because I do get into a rut and therefore develop a strong opinion on something – to add pieces together, and therefore continue to incorporate the right kind of information. Because plenty of information in the short term will say, "Oh, you're wrong for this, that, or the other reason." It's the people whose views are informed views. That's going to come from, probably, a management – who really understands the business. Also, you can look at their track record and know what this person's history is, and therefore how informed are they, and therefore how informed is the opinion they're giving me back. And it's like, "He's been doing this for 40 years, he knows this industry really well, and if he thinks that my view here is troubling, then that's a really great piece of information for me to have to retest my thesis."

Dardashti: In terms of international audiences who might be hearing this conversation, what type of feedback or communication would you welcome?

Robotti: Fortunately, Isaac Schwartz who runs our Global Fund, in 2006 convinced me to go to Asia, and said we should be investing outside of the United States. At the time I'm like "Ah, that doesn't make any sense to me – but he's young, he's smart, let me go try this."

Dardashti: Why don't we back up and introduce Isaac Schwartz in more detail?

Robotti: Isaac Schwartz runs our Global Fund. Isaac, today, is 34. We started the Global Fund ten years ago when he was 24. I met him when he was 19. He was working at an investor conference on insurance, and he worked for us that summer and pretty much every summer after that. So he's been working for us for the last 15 years. He's 34 today. Isaac, on graduating, traveled to Asia, came back and said, "There's is a great opportunity to invest with the approach we have in Asia. Since foreign markets are more volatile, the domestic market is more manic-depressive, the idea that valuations become further misaligned from a fundamental value is greater, so therefore..."

Initially, I'm like, "I don't know how to do that, I don't speak foreign languages." I was feeling very limited, but he convinced me that it made sense. He took me to Thailand, and Thailand was great at the time, it was in 2006. That was nine years after the Asian financial crisis. The balance sheets were pretty much – all the Thai companies had been significantly repaired; all the debt had been paid off, they'd collected cash on the balance sheet, they had earnings and they were trading it mid-to-high single digit P/E multiples with significant

dividend yields. So, in the valuation, it became extremely easy to say “Yes, these are really cheap stocks; I understand what you’re saying now.”

That was the original entry point. And then he lived for one year in Singapore, and then five years in Hong Kong. Since he was on his own there – of course he had a network of people that he developed that are local – and he could still have contact with the home office; I took five trips each year out to Asia to visit with him. We traveled, and he took me all over the place. It’s been hugely beneficial to me in thinking about investing, because the world is flat.

It’s clear we’re in an interconnected-world, so to understand that has been extremely helpful to me in having a better view of what business is, how does business work, and how do countries work, and having a different view on what the world looks like.

Dardashti: And just to be clear on “global” – we’re discussing Mongolia, Kazakhstan.

Robotti: That’s right, we are discussing Kazakhstan, Mongolia, Slovenia, so therefore, out of the way places. In addition to in-way places too; we’ve also been to Hong Kong and many parts of China. I’ve been to 12 different cities in China. We’re also in Indonesia, we’re also in Singapore. So, therefore we’re not just in the funky places –although we’ll do funky too.

Dardashti: Returning to this question of how our global community could be helpful to you, if anyone is listening in these more interesting geographies they can reach out to you, perhaps?

Robotti: Just yesterday I got a distribution from a fund that I had. After Isaac took me to Thailand in 2006, the next trip we took was two months later, in March 2006. We went to a Euro money investor conference in Vietnam. We spent the week in Vietnam, half of it in Ho Chi Minh City, Saigon, and half of it in Hanoi. I walked away thinking I’m a bottom-up stock picker, but when I went to Vietnam, the financials at the time were – there was an income statement and a balance sheet with no footnotes. When you talked to the management and you asked them some questions about inventory turns, they’d come back and tell you what the payable policy was. There was a clear lack of communication between us, as investors – and the management teams. The financials were not fully expanded. And all the companies have been SOEs, state-owned enterprises, that had privatized with all of the warts that came from that.

I met a guy there who had a private equity fund, and thought, “Vietnam is self-sufficient in food and energy. It has 100 million people who are extremely industrious, I would think as industrious as the Chinese, and has a lower cost compared to the Chinese, so it’s significant. And it is a country that needs to have a great relationship with the United States because they always want to have a counterbalance. They have a neighbor who’s right next to them who has 1.3 billion people instead of 100 million people, who over the centuries and decades they’ve always been at war with. So to have the United States as a counterbalance against China means you need to have access to American capital, and they have a great relationship with America. Therefore, an investor from America in Vietnam is going to be protected.”

That investment we made in 2007. I've already gotten back 3.3 times my money from it. So, I've had an affinity in trying to find something to do in Vietnam, because I do think it is an interesting place to invest.

We went on another trip once we were in Rwanda, Kenya, Zimbabwe, South Africa, and again - I think that part of the world is extremely interesting. The problem is that we have limited bandwidth. So therefore, over time, we would hope the bandwidth grows and our core capacities grow.

So today I think we know a lot about home-building in America; before 2003 we didn't know much about it. You always hope to, as time goes on, gain more experiences, gain more competencies, broaden out both geographically and with an understanding of the industry. I don't know what the next three things we'll do in the next five, next seven years. But I hope we'll be doing more things, because that's part of what makes it so much fun and so energizing, and I'm so passionate about it.

Dardashti: We just stumbled into the theme of Latticework 2017, 'Intelligent Investing in a Changing World.'

Robotti: I'm an energy investor, and it's a changing world. Energy, and energy consumption, is definitely going to be different thirty years from now. Someone asked me a question recently, "If you had to do it over again, what would you do differently?" I said, "I would have spent more time looking at Gabelli's entertainment stocks when I worked for Gabelli - and not doing energy - because entertainment will always be something that sells and is an industry, and you can make money and you can invest in." Energy, and oil definitely, is more problematic. So how does that work? That's an interesting dynamic because it moderates the idea that "Oh, I've been through eight energy cycles and I know how it works; and what goes down goes back up." The next "back up" may be different, or, at some point, the next back up is going to be different than what it was thirty years ago. Therefore, it's rhyming, but it's definitely not repeating. There are new paradigms that are coming into the energy field.

Dardashti: I'd love to stay on this point for a moment. As you talk about the world changing, what changes get you most excited?

Robotti: I can't give you the exact answer to that. The answer is that things that are changing - in areas where you have the most knowledge. You maybe have the best understanding to identify what that change is; clearly being able to understand the change gives you an opportunity to get great returns. As bad as it may be in energy, to understand how that changes, and to appreciate that and to identify what the opportunity is, is definitely something that should work for us over time.

A trio of thought-leaders explored *The Role of Active Management in the Modern World* with the MOI Global community at the Latticework 2017 summit, held at the Yale Club of New York City in September.

The expert panel featured: Robert Robotti, president of Robotti & Company, Michael van Biema, founder of van Biema Value Partners, and Andrew Burns, associate at Global Endowment Management.

Jim Basili, managing partner of Blacktree Capital Management, moderated the conversation.

The following transcript has been edited for space and clarity.

Shai Dardashti, MOI Global: I am honored to have Jim Basili hosting our next panel conversation. Jim is a longtime friend; we met a decade ago, if I recall correctly. He is the managing partner of Blacktree Capital Management, a family office he established in November 2007. I am also very excited to announce that, in January 2018, Jim will launch a new fund called Lightsail Capital, making long-term investments in a group of small growing public companies. We could talk more privately, but Jim has a history of investing in smaller companies in various contexts and what he's doing now is very interesting.

Jim Basili, Blacktree Capital Management: It is my pleasure to be with such a distinguished panel here, and I am going to introduce them to you guys, and then we will launch into a conversation, which we are all going to enjoy.

Andrew Burns works at Global Endowment Management. Global Endowment Management is a multi-endowment, multi-institution firm, managing about seven billion dollars as an outsourced chief investment office for its clients, letting them aggregate their capital so they can benefit from the scale that some of their larger peers have. Andrew focuses on public markets for Global Endowment Management. He joined the firm in 2008, so he got there just in time to have a full market cycle of education in about two years. We will talk a lot about the changes that he has seen at Global Endowment Management since.

Bob Robotti is the president of Robotti & Company. He got his start in public accounting before coming to Wall Street, and that start was an incredibly auspicious one because he audited Tweedy Browne, the legendary value firm. If that is not pedigree enough — I've heard you tell, Bob, that the first stock you ever bought was a recommendation from Walter Schloss's son, Edwin. On top of that, he also audited Gabelli & Company's books, and then went on to work for Mario Gabelli before starting Robotti & Company. Robotti & Company have now been around for over thirty-five years, which is a very long time to have a market-beating track record, and their track record has beaten the market by a wide margin in that period.

Also here is Michael van Biema of van Biema Value Partners, a multi-strategy allocator, and Michael, before forming the firm, was a professor at Columbia Business School for about a dozen years beginning in 1992. In that time he taught at the vaunted value investing program for both M.B.A.'s and executive M.B.A.'s and he also managed to find time to co-

write a book which many of you are probably familiar with and have enjoyed, 'Value Investing: from Graham to Buffett and Beyond.' Despite his finance and value pedigree, Michael's own education was not in finance or value. He was an electrical engineer as an undergrad and got a Ph.D. in computer science. His first jobs after graduation were in the IT field, not in the investing field; perhaps, we will get to talk a little bit about the way those two fields are converging.

I would like to start by interrogating the title of this panel, which is, "The Role of Active Management in the Modern World". We are going to break down that title a little bit and ask some questions about what that title means. The first thing that we are going to do is talk about that word 'active' — because there was a time when there was no other kind of management than active management. It is a sign of where we are today that we have to make a distinction between active management and something else. That something else, obviously, is indexation or passive investing. By some accounts, that now equals about a third of investor capital the United States, up from roughly nothing in the 1960s; it has been a very dramatic change.

I would like to ask each of you guys as panelists, "How do you feel about the ways passive indexation can be done right, and maybe more interestingly, the ways it can be done wrong?" Before we got on stage I spoke to each of you, individually, and you all said you felt there was a place for passive investing — and you all had some interesting comments on what that might mean in terms of the way it is done right and done wrong. Talk about what is good and bad, what is right and wrong about passive in the way it is done today.

Bob Robotti, Robotti & Company: There is absolutely a role for passive index investing. It makes a lot of sense and most people who invest with an active manager over time probably underperform because the human element is, of course, a thing that is always grounding. It does not change and humans follow good performance, whether that is active or passive. They are going to follow it and they are going to do it at the wrong time. Therefore, if someone is disciplined and only does the same thing and does it with the same active manager through down-cycles and up-cycles, or does it with a passive index, they probably will do well.

Passive investing is interesting because that is what the rage of the day is and I would say that it is neither 'passive' nor 'investing.' Today what are not index funds are ETFs. I do not know why someone needs to have an ETF. That means they can trade instantaneously and be subject to their human emotions on an instantaneous basis as opposed to an index fund where you can only do it once a day. Therefore, it moderates all the wrong intuitions that people have. Of course, the ETFs themselves turn over multiple times during the year. Therefore, that is not investing; it is speculating. Today's ETF is an act of speculation that enables people to make all the wrong decisions at the wrong time and, I think, a great opportunity for active investors to compete against.

Andrew Burns, Global Endowment Management: I would agree. There is nothing inherently wrong with passive investing if done correctly. Warren Buffett is a very well-known proponent of investing passively, and he recommends that people just buy an index

fund. The trouble comes in, as Bob mentioned, if people do not stick to it — if people are expecting sustained double-digit returns similar to what we been experiencing for a long time now.

Buying an index is just not a through-cycle number. When things turn south, they lose conviction — and that is probably not going to be the experience for them. Passive investing is a tool that can have a place in more of an active mindset like ours — but it is just generally much harder to take a view on a market, at least in our opinion, than it is to find a great active manager who we can trust to outperform the full cycle.

Michael van Biema, van Biema Value Partners: Passive investing is a terrific thing for investment advisors. It has been a wonderful development for investment advisors because it guarantees them average performance across cycles, and most clients are quite satisfied with that. It is an easy product to sell, and an easy product for their clients to at least *think* they understand. Most clients do not fully understand what passive means and what is involved. All of us here still believe that the only way you are going to significantly outperform the markets, over time, is by practicing some form of active investment.

The other thing interesting is that, over time, we are now developing a continuum from passive to active. There is true passive investing, which is just a fixed algorithm that does not change over time and allocates capital according to that specific algorithm. Then you have more dynamic forms of passive, where you are doing the so-called smart data — a term which I despise, but I will use it anyway. Then, the nearest forms of true active investing, which are passive algorithms or semi-passive algorithms, which use artificial intelligence for things like neural networks, and where the underlying algorithms actually change and develop over time — each have their advantages and disadvantages. The only way I still think that you are going to get superior outperformance over the long-term is by investing in active management.

Basili: I like that you had the courage to talk about something you despise because I am going to try and coax some of that out of you guys as we go through this panel here, Michael. But in particular, I want to highlight something you said, which is that most people do not necessarily know what they are getting when they are involved in a passive product. I wonder if you might mention a feature or two of some of these passive strategies that you think people are not aware of when they invest in them.

van Biema: The basic thing that they do not understand is the risk involved. There is a huge amount of risk, particularly these days, which relates to, as you said, the enormous amounts of capital that are flowed into these ETFs and the other “passive” forms of investing. The risk is, quite frankly, that people are actively trading these things on a day-to-day basis. When the market does go south, which it will sometime in our lifetime, you are going to see enormous capital outflows.

The biggest problem is that if you invest in a passive form, the onus of making active investment decisions falls on the investor himself. In spite of all the evidence, academic and so on, to the contrary, people still believe they can time markets. It is a well-proven fact that they can't time markets, but they are going to attempt to time markets. The

underperformance of the average investor is a direct result of the thought process that one can time these markets. Therefore, not only are you going to perform averagely with ETFs and passive investment but you are probably going to perform, over time, sub-averagely as you try to trade in and out of the market. Constraining people from bad behavior is an important function of active management, including things that people hate like longer lock-ups, but it is a very good discipline for investors to operate under.

Basili: We are still on the title. I am going to interrogate the other keyword in the title, which is looking at the role of active investing in the *modern* world. Saying that word implies, almost in secret, that something has changed in the current world versus the world that maybe we grew up in, or the world we were educated in.

I want to ask each of you what things you focus on that you think are different now, aside from what we just discussed, which is obviously the rise of passive investing. There are a lot of other features of the investment environment that maybe have changed in 2017 versus when you began your careers, or earlier.

Burns: One thing that has been a big change from when I first started, in 2008, was, for us, hedge funds were a much larger allocation at that time. If you looked at the returns that were generated from those investments for the five to ten years prior, they were truly exceptional. But there have been several changes that have led us to meaningfully decrease our allocation in that area. It is not completely gone; we still have a very healthy allocation, but it is a lot less. The main rationale behind it is leverage. Many of those strategies were using leverage in order to generate returns with extremely attractive financing. You can say that is bad, but they were around for a long time and made great returns doing that, so maybe the overall risk-reward, as long as you were thinking about it appropriately, was decent. That is just not there today.

The other thing is a lot of hedge fund strategies will typically hold a high cash balance, and cash has been yielding zero for a long time. It has been a huge headwind to the types of returns that those strategies can generate — and you see that in the numbers if you look at the Credit Suisse hedge fund index. The annualized trailing ten-year return, if you look at a chart of over the last twenty years it is literally just straight down — from double-digit for the industry to probably below five percent annualized. I just saw a study referenced in a book by Ben Carlson that said, from 1998 to 2014, in a survey of pension funds, hedge funds were the lowest returning asset class — aside from cash that those people held. Hence, the returns just are not there and we have reduced our exposure to that area dramatically.

Basili: Two follow-ups to that. Firstly, you talked about how leverage was a driver of some of these strategies and it is just not there anymore. Obviously, rates are very low, so if you want to borrow as a hedge fund manager and get leverage, you certainly can and it is cheaper than it ever was. What is driving the fact that it is not producing returns for people anymore? Is it risk tolerance changing after 2008 or is it something else?

Burns: People are not willing to take on the leverage, or less willing — maybe it is more on the investor side. They are not doing it, and most of it was not that prudent — so it's probably for the best. The other thing is, with rates also being low, a lot of the opportunities

that are investable via leverage are maybe credit-related things, and the yields – absolute yields – are very low on those as well. Hence, the spreads are not as good and the fee generally remains as high. I would say those are the two reasons.

Basili: Bob, what has changed about this modern world versus the world of ten, twenty or thirty years ago?

van Biema: Bob has a much longer perspective than all of us, you should listen to him.

Robotti: The one thing that has not changed is that the underlying decision makers in all of this are still individuals. Individuals are all the same. They are wired the same way; they make all the same mistakes. They are allocating capital to the wrong things, at the wrong time. It is based on performance because they cannot understand the *driver* of the performance. That is inevitable. But one thing that probably is interesting is where interest rates were when I started to invest and what has happened with interest rates. Last year was, of course, the all-time lowest interest rate ever in recorded history. We have never had interest rates as low as they were last year. It is off the charts; in five thousand years of data, this has not happened. People do not think about that, enough. Over that period of time leverage clearly has been your friend. Of course, multiples have increased, because in a low interest-rate environment, you can pay a lot bigger numbers.

All those things are happening. There are many people who will learn lessons *post*-financial crisis. Those are not lessons because this is *not* the new normal — in spite of the fact people may say that it is the new low, it is the new this, or it is the new that. It is not a new thing or the new this; it is something that is transitory. There have been many lessons learned, amplified by eight years of post-financial crisis.

Interest rate movement has been thirty years of straight down. I do not know when it will go up, but clearly it is the wrong number. Low-interest rates and the Fed have been terrible things. Someone asked me when I was in Omaha, “What do you think about interest rates? Do you pay attention to what the Fed does?” I said, “No, I pay no attention to what the Fed does. Who cares what they do because it is bad policy.” Hopefully, they are getting away from bad policy. It does nothing to incentivize good behavior, rather only incentivizes bad behavior and bad allocation of capital. Bad allocation of capital is always bad. Allocating capital is not inherently good; it is good or bad, depending if it’s well-invested. Those are some thoughts on the current environment.

Basili: I would love to talk a little bit about how interest rates are affecting all three of you, going forward, because there are two general schools of thought; the traditional value school says, “Rates are lower than they should be, which means P/Es are higher than they should be, which means P/Es are going to fall, and maybe we should be nervous about that.” Then, there is the non-traditional value school, espoused by none other than Warren Buffett, along the lines that “P/Es are normal given where rates are, and are not very expensive.” I would be curious how each of you think – knowing that P/Es are higher than they have historically been and that interest rates are a purported reason, which may or may not make sense, for these elevated market valuation multiples.

van Biema: We invest with a large number of small managers, all value-focused managers. The way we do our “macroeconomics” is by talking to our underlying managers and seeing what they are finding and what they have to say. It is clear that people are not finding a lot of cheap stocks, in the United States anyway. The situation is certainly different in other countries, China being one of them and Japan another, where there are a large number of interesting value opportunities — but the United States is pretty slim pickings at the moment. And that is definitely, in my view, a result of the long-term low interest-rate environment we’ve had. We are in a very weird market situation. If you think about it, at no time in my lifetime certainly, have we have seen a market which reacts by less than a couple of percentage points when we are on the verge of nuclear war — which we have been at least a couple of times in the last few weeks. The market is at a point where nobody wants the party to end.

There is a lot of risk in the world, political and other. People have had a good thing for so long that they do not want the ‘Ring Around the Rosy’ situation we are in to change. But I am pretty confident that at some point, that overconfidence, or continued confidence, is going to go away and we are going to have a significant downward movement. It will probably be triggered in the United States, but it will be a global situation and it will be great for our investors in the long-term, and it will probably cause some pain in the short-term. We weathered 2008 nicely; we think that the concept of value — the concept of focus on a margin of safety — will help our investors through. It will probably end up being a relatively precipitous downward movement in the markets, but do not ask me when that is going to happen.

Burns: One of the big lessons I have seen post-crisis, even though my career is relatively young especially compared to these guys, I was around a little bit before the last crash: people have lost a lot of opportunity by waiting for the next shoe to fall in the market. That is a comforting thing to be doing. Plus, interest rates are definitely too low; nobody can deny that. It does seem that there will be another time when the market crashes, but at the same time — if you are investing with concentrated active managers, can they really not find ten, fifteen, twenty stocks to be invested in?

I definitely agree with Warren Buffett that starting where we are today, stocks are definitely going to do better than bonds. Those are your two basic choices and you can say it is easy to sit around and wait for the market to crash, or wait for a better time to buy. But, at least from what I have seen, the track record of people sitting around waiting in 2008 and that is when they bomb it in, or 2011 is when they bomb it in, and even 2016; it does not happen. In our perspective, it is more or less what I said; find the guys that we have a lot of confidence in. They can pick ten stocks over the next five to ten years that will produce. It is obviously not the best buying opportunity, but it should produce acceptable results for us especially compared to alternatives.

Robotti: First off, there are plenty of things to buy today. We have a fully invested portfolio. I wish I had more cash; I’ve got things that I think are great investments over the next three to four to five years. I do not think that is a problem. I am not invested in the S&P 500 and I do not own bonds and I do not own a lot of the asset classes that are too expensive today. I

do think interest rates, over time, kind of move up — but I do not think they move up dramatically, and therefore Ps are not crazy. To not invest given the '08 financial crisis, I would say that that is, hopefully, a once in a lifetime event that I will not get close to again.

I would think it is more analogous to what did happen in 1998/99 when I underperformed and I was down thirteen percent and six percent and I felt like an idiot, while everybody else was making money like crazy and investing in things that I would never invest in and did not understand. What I did was I stayed consistent with what I do, what I understand, and what I know. I have a portfolio of securities that are well-positioned, that are well-priced, that should do well in the next number of years. Interest rates will probably move over time; I do not think they move dramatically. I do not think the world falls apart because the financial crisis is something that is not going to recreate — the banking environment today is extremely strong and well-financed. It is a fundamentally different situation. To think that that is going to happen, and that is what permeates a lot of people's minds; we all know it is going to happen and it is going to happen because after seven years of recovery, it's got to stop.

I was mentioning earlier today, we do a bunch of things in housing and housing has had seven years of recovery and it can't go on forever. Well, when you go from 800,000 was the single-family home — lowest number in the last forty years — and you go down to 450,000 homes, and now you get back to 800,000, which is still the lowest number in fifty years — why can't it continue on? It absolutely will. The demographics would argue that; the population would argue that. And if I am wrong, I am not talking from a high rate that I am paying a huge price. There is still a modest situation that I am invested in today. If I am wrong, I do think I have a huge margin of safety and I do not think I am wrong because the demographics, the numbers, the statistics would all say that there is plenty of room to go from where we are today.

Basili: Fantastic. Andrew, you talked a little bit about a change that you made at Global Endowment's portfolio, moving away from hedge funds. You did not talk about what you moved towards; I am going to ask you what you have moved towards. Bob, you talked about a lot of things that you are doing the same that has not changed. But there are quite a few things that the firm is doing differently than, say, ten years ago. I thought it would be interesting to ask all of you, what are things that you, internally, in your businesses, are doing differently from ten years ago — whether it is moving into a different asset class or something else that you can talk about? If I can maybe prod you a little bit in the direction of controversy, although you do not have to take the bait, something that may have involved letting go of an idea that you held sacred or that people in your field generally believed to be true. Andrew, maybe to start with, where did you move towards — when you moved away from hedge funds?

Burns: We have moved incrementally. Some into our long-biased — and some of our long-biased or long-equity managers some might consider hedge fund strategies with the structures similar to a hedge fund — we moved some there. We have also increased our allocation to some of our private assets, most particularly on the private equity side where we do a lot of work. We have a team, it is not my specific area, but we have a team of people

who focus entirely on doing deals with independent sponsors and finding off-the-radar small deals, not the huge mega-buyout funds. It has been very good for us. Just continuing the philosophy of accepting what the realities of the opportunity sets are and allocating to the best ones that we can, because we are not going to sit around in cash. Maybe give me one second to think about an idea that I have killed.

Basili: That is fine. You can think while Michael maybe tells us about a change that has happened at the firm, if there have been some.

van Biema: We really have not changed anything that we do. We invest with small, deep value managers that manage typically under a few hundred million dollars, which we think is a terrific evergreen niche that is underserved, and under-invested in, by most family offices and larger institutional clients. That is what we try and bring to the table. As I have said before, nobody knows what the environment is going to be going forward. But, whatever it is — historically, that particular niche has generated very good returns with very low downside risk and it captures typically seventy-five percent of up-markets and less than fifty percent of down-markets. If you do that for a long period of time, consistently, your returns and your clients should feel very happy.

Robotti: The biggest question is stock picking, right? That is what it is all about. The more people that come into your universe, that more that is great for you. One of the things that did happen ten years ago, Isaac Schwartz — somewhat similar to First Manhattan's experience, too — I met him when he was nineteen years old. We sat at a dinner and I was chatting with him; Ajit Jain does not say very much and Isaac talks a lot. As a nineteen-year-old, he knew more about investing than most forty-year-olds who invested in the business. I was fortunate to meet him early on; Isaac worked for us when he was in college. He graduated, he went to Asia. He said we should be investing overseas. I am like, "Investing overseas? I am a guy from Queens and I do not even speak English that well. Fine, but I will do it. You are smart; let me try this."

We went to Thailand. It was '06, it was after the Asian financial crisis — nine years later, Thailand had cleaned up the balance sheets, they had collected cash and they had turned the businesses around. The ones that were survivors clearly were great businesses; the valuations were extremely cheap. They had very high dividend payments. A lot of cash on the balance sheet. I was like, "I guess even a guy from Queens can figure this out." They have all the financial statements translated into English. The management teams can even speak English and I can understand them. Of course, not nearly as well as you think they do; just because they said the words does not mean they think like you do. It does not mean they think that differently because people say, "How do you invest in an Asian company? How do you invest? How do you trust the financials?"

Having invested in America I was the named plaintiff in twenty-five class action lawsuits. American companies steal money all the time. Managements are distrustful. United States companies do all kinds of things — so the idea that it is different overseas: it is not; it is the same thing here. Anyway, Isaac was great because he was there by himself but I would have to come a couple times a year, just to have comfort and whatever else. I came to visit with four hundred or five hundred management teams of companies in the ten year period of

time. It was great for me because I have been to twelve different cities in mainland China. I have been through a litany of places that Isaac takes me, including Ulaanbaatar in Mongolia, and some other strange places. It was great because now I have a better understanding of the United States economy, where we fit in.

One of the things we do, a core competency, is energy; that is a huge differentiator and an element which frames my macro view. The world does not understand that there are no more energy resource available in America, at any time in my lifetime, other than now. Everybody talks about fracking, and the impact on oil — we all see that because that happened in the oil price. But the bigger thing is natural gas, the resource that is in America today has never been, in my lifetime, available and known. That's huge — because for the next ten years we are going to have so much natural gas in North America that the United States economy, and the energy-intensive businesses in America, will be competitively advantaged against anybody else in the world. Because we can make steel, we have iron ore and we have metallurgical coal, you have low-cost energy. Energy-intensive businesses tend to be less labor-intensive. Since natural gas prices cannot be exported, that competitive advantage will stay here for at least ten years. You have already seen that; the chemical business has grown up — we have seen a few problems in the last week, what happens with the floods — but that will continue to happen, that means it gets consumed, and that gets into the cost of goods sold. It is a huge opportunity given, I think, in American securities. It also means, in my view I do not know anything about monetary policy, but I also think that inflation does come — because what has happened, my visits have confirmed, is that Asia has sucked all of the inflation out of the world. Because they made everything so cheaply, everything moved to China.

China is today a different place than where it was. They have very few competitive advantages. I would argue the only competitive advantage they have is the government. If they want to do something, it gets done because there is no 'not-in-my-backyard' in China. However, when it comes to making something like steel, they have to import the iron ore and they are importing more of it, because the iron ore is not so good in China. They are importing more metallurgical coal. Labor costs more money because there are no more people coming into the labor force. China's sucking and bringing prices down and keeping inflation away — is gone. Therefore, it is going to be a force for inflation over time — and that is why inflation happens; when the costs of goods go up, you've got to pay more for it — and that is the environment we are going to be in. Energy prices move higher.

Copper is something that is a basic commodity; everybody says the super cycle's dead, I do not think the super cycle is dead — it took a nice hiatus over the last number of years — because the economy is not going to be in a low growth rate environment forever. That is going to change. And when that changes, it is going to change the drivers behind so many businesses and it is going to lead to limitations in goods and services, which leads to inflation, which means higher interest rates. But that is not happening overnight, maybe in the next five to ten years. I just cannot see how that is not the way it plays out.

Basili: That brings to mind maybe one of all of our favorite value investing pontificators, who is Jeremy Grantham at GMO. He has been talking for a very long time about how high

corporate profit margins are and how if capitalism is not broken, they are destined to fall. Some of the things that you are saying, Bob, sound to me like drivers of lower profit margins for corporations — because you've got to pay more for your inputs and you've got to pay more for your wages. Interestingly though, you are saying this at a time when Mr. Grantham has maybe abandoned some of that reasoning and he has written recently that, maybe, things have changed. Maybe it has to do with the shifts in the economy to different sectors that are higher margin sectors and to the shift in the United States economy to international investing, which means our relationship of profits to GDP is not the proper ratio anymore. I am curious what you gentlemen think about the notion that profit margins are at a peak and are destined to come down or whether we are in a new normal.

Burns: I definitely think this would be something that qualifies for an idea that I've changed my mind on. I have read Grantham pretty much my whole career and it is interesting to see him throw in the towel on this idea. But, if you think about it, there does not seem to be an iron law that says that profit margins themselves should mean revert. It seems much more likely to me that return on capital, or a return on equity or something like that, would be potentially more of a mean-reverting measure. That being said, if you had a very small equity market dominated by one or two companies that were able to defend extremely high return on equity positions — maybe that does not revert either. Luckily these are not the kinds of things that we usually have to take a view on. We just find our guys who can find a couple stocks that we do think have a defensible return on equity, so that would be my answer.

van Biema: My thinking is that it depends on what happens in the labor markets, since labor is the main input to production. We have also been in a relatively unique labor situation in that employment levels have increased dramatically over the past few years but wages have not moved up at all. There will be a mean reversion in wages and I think that will have an effect, ultimately, on profit margins. However, Bob makes a terrific point about the reduction in the cost of energy — and that is a countervailing movement to the cost of labor. However, energy is a much smaller component of production in most industries than labor is. We are still a heavy service-sector focused economy.

Robotti: I am going to bail out and say I have no macro view. Instead, we look at companies in which we think we understand the drivers in the business; what the supply and demand is and what we expect margins will be in the next three to five years. Therefore, we expect margins in the profitability of their business to be significantly higher than the current valuation the stock reflects today; I do not know what happens across the entire spectrum. I would imagine there are plenty of companies that are going to have issues in terms of costs increasing and not being able to capture back profit margins from it.

Latticework Participant: I am a startup guy. I am always thinking about the modern investing world, having been an investor in the value space since '91 or so — but now we live in this world of AI and machine learning. You've got a company called Wealthfront coming online that is pitching, "Pick your style of investment, and then we will take care of it, and tax efficiency, and all that." Google has done some experiments on this as well. Could you guys comment on some of the projects that might be going on here in Wall Street that

could compete with that or what do you guys think of their these new modern ways to invest?

van Biema: I can't give you any competitive intelligence. But there are lots of companies that are trying to build machine learning platforms for doing investing for people. They are going to have, at least some of them anyway, are going to have terrific success because there is a lot you can do. It takes a while; if you go back to the history of computing and look at Big Blue, it took them a long time. Deep Blue, for those of you who do not know and I imagine that is not many people, was IBM's original AI chess-playing computer. Everybody knew that the computer had the capability to beat humans at chess. Yet, it took it a surprisingly long time to actually get to that point.

The reason is that people are much better at thinking in non-algorithmic ways and non-linear ways than computers are. But ultimately, you can mimic those thought patterns and therefore build truly intelligent algorithms to do the investing. We are at a similarly early-stage in terms of AI platforms and investing. It is going to take a lot longer and a lot more time and effort than people think it will take to build things that are actually on par with human beings. I also think that chess is, in many ways, more simple than investing. There are so many more human-based factors that go into it that are going to complicate the situation.

Robotti: I have two thoughts. Firstly, I have no concern in the short-term because no one is going to use artificial intelligence to try to figure out how to underperform the market. Over the last three to five years I have underperformed the market. I know a lot of smart investors that also have been active managers that have underperformed the market. We are all kind of safe for the short-term, because they are not going to try to replicate that. In five years' time, when we have outperformed the market — because the indices have not done nearly so well and stock-picking has worked — then, they are going to start to think about what we do and try to emulate that.

In the meantime, fortunately, many of us probably are smaller; why would you want to emulate that model if you cannot put capital to work and deploy it effectively? So, they are not going to be doing it. And the other huge advantage that I have is that everybody keeps saying how I am the old guy, so by the time they figure it out, I would not have to worry about it because I am clearly going to be wealthy enough and it would not be my problem; it will be their problem.

Basili: Bob, I've heard you say you want to work as long as Irving Kahn did. I hope it turns out not to be the case, and you'll be having to worry about it with the rest of us.

Latticework Participant: This is a question for Michael and perhaps Andrew. You spoke about finding small managers running a couple hundred million dollars and the question is if they are small and they are compounding at a healthy clip — they are doubling assets pretty quickly, and they are probably attracting some other investors. At what stage are they not small enough for you and what do you do about the fact that they've made you lots of money, and you have gained lots of faith and trust in them in that time?

van Biema: That is a great question. We try and stay with our managers for as long as possible — and what possible means depends on their style. Some managers have a style where, let's say, they are investing in tiny micro-cap companies — and large amounts of capital are a real negative for them; we may stay with them up to the point where they have a couple hundred million dollars, and then we will leave because we do not think they will continue to compound at the high rates they have been compounding. Other managers have a more diverse skill-set. We have some managers that do both well; they invest across the capital structure, they do bankruptcy liquidation workouts, special situations and a bunch of different things. Those managers can grow a lot.

Just to give an example: we have one manager who I invested with when he had under ten million dollars in capital and he is now at \$1.6 billion. Every day I go to work and I question whether he has gotten too large. So far, I have not pulled the trigger on deciding that he is too large because he is an exceptionally talented guy, and a very versatile guy, but it is a tough decision in some cases. I would say that our performance would have been better had we pulled money from some of the larger managers we have, more quickly. The good news on this front is that there are tons, these days, of really good small managers — so we have no problem replacing managers who we think have gotten too big. I mean, it is exciting. My biggest complaint in life is I have more good managers than I have money to dole out, and that is my biggest frustration — so they definitely are available.

Burns: First of all, it is a great problem to have and it does depend on the strategy. One way we do try to mitigate that is to put controls on how quickly people can raise outside money because — as good as we think we are at finding exceptional managers who can grow through returns — it is much more common that they grow through raising assets. If they grow through returns, it is still going to be a pretty long runway for us to be partnered with them. A lot of times, they will still have a lot of headroom even if they are doubling their asset base — at least that is our experience.

Latticework Participant: Since no one's brought up this can of worms, I thought I would get us into politics and would like to ask your opinions of what you think the risks of the market are in regards to the Trump agenda of tax cuts and cash repatriation not being passed.

Bob Robotti: I would like to comment on that. The most overvalued thing in the world today is Donald Trump. He just drives everybody's attention, and part of it is because of the nature of who he is; I try not to read anything that says Donald Trump. I do not listen to any story that mentions Donald Trump because, first off, you have no idea what is going to happen. Therefore, there is total unpredictability. You are not going to be investing based on what you think he is going to do. It is such a distraction and a waste of time. There are many other factors that are much more important to any business you are looking at. That is, what you can figure out, what you can make determinations on, and what is valuable — and what is a waste of time.

Basili: I did hear someone mention nuclear war earlier, so I think there are some considerations beyond tax cuts that are happening...

Robotti: I will tell you, because I am old enough, I heard that and I thought about that and

you cannot discount that. But the fact of the matter is, in our lifetime — in 1963, when I was in Queens at St. Regis grammar school — we did duck and cover underneath our desk; there was a larger risk of that. In our lifetime we have had that before, and it was right here in Cuba. It was not in Korea. And, yes, today you probably get from Korea to here as quick as you can from Cuba to there. But, that risk — it happens and it is has happened in the past, and it will happen again. Those things will happen and you cannot somehow make determinations on how you want to invest the next three to five years based on that.

Latticework Participant: Over the past three years, we have seen a growth in a lot of these market-neutral and multi-strategy firms, employing a lot of leverage and running on a market neutral basis. Do you think this is like a secular trend that will continue to go on or do you think it is more of a cyclical trend? And then, what will the impact of the eventual rate rise be on such a strategy?

Burns: I can take that since I touched on it a little bit earlier; I have not seen a huge rise in that. It may be because it is an area that we are not that focused on anymore. I think those strategies just tend to be inherently fragile. They are usually liquidity mismatched in some way, and I do not know the specific ones you are talking about — but, probably, it will not wind up ending well and it probably will be cyclical. That would be my view.

van Biema: Our view is that anything that uses a significant amount of leverage is ultimately going to be toxic. We stay away from any of these firms that run a highly-leveraged book.

Robotti: I know nothing about it. But all the phrases — market-neutral, leverage; you said about three or four things about it. Well, one of those, alone, is going to be a guarantee that it is going to be a disaster.

Latticework Participant: It seems to me that there might be two offsetting forces and I would love to get your opinion on it. The first; clearly we have seen a ton of money go into indexing and since indexing is primarily market cap-based, it is causing stocks that go up to be bought and stocks that go down to be sold. For value investors, that is putting selling pressure, possibly, on the types of stocks that you, and the managers that you utilize, are investing in. The flip side of that is we have seen a lot more interest in factor investing — the recognition that things like size, value, and momentum are real factors that firms like Dimensional Fund Advisors have built a tremendous business out of. Those funds are raising hundreds of millions of dollars in capital and we are seeing more money go into factors like value and size. As you look at your businesses and are talking to managers, are these forces offsetting? What perspectives and what kind of impact is that having on the types of companies that you are looking at?

Robotti: I see the first one happening. I do not necessarily see the impact of the second one. The first one is of course that indexes are doing extremely well. Therefore, that is causing fallout — and the flip side to fallout is that it's a great opportunity, right? What you are saying is it is creating companies that are significantly mis-priced and mis-valued. For a stock-picker that is what we love, we all may be grouching — but I would suggest that today is probably a great environment for stock-pickers, because the opportunity is being created.

That is my quickest response.

van Biema: I would say there is definitely a push to the larger cap end of the spectrum. That is a result of, actually, both of these factors — to some extent. I think that is one of the reasons you are seeing a lot of appreciation in some of the larger cap stocks and a lot of neglect in smaller cap value stocks. We have seen historically that, usually, at some point it switches around — but, again, it's hard to predict when it will switch around. Definitely, money is flowing into the larger cap segments of the market — and that is not just in the United States, it is happening across the world, interestingly.

Robotti: But it is more in the United States. It is interesting, right? The best performing stock index and stock market over the last five years has been the United States, in the large cap stocks in the United States. It is the most overvalued, best performing class. How is that going to end? Trees do not grow to the sky, right — and that is what you are putting money into; it's been the best performing market over the last five years.

van Biema: A fellow who was on my board and unfortunately passed away a number of years ago was Peter Cundill, a famous Canadian investor. One of his rules of thumb was he would always go and visit and look at the stocks in the stock market of the worst performing market from the previous year. That is not a bad idea.

Exclusive Insights into the Energy Industry

The Supply/Demand Dynamics of Oil

WITH ROBERT ROBOTTI, PRESIDENT, ROBOTTI & COMPANY

“We focus on oil and gas services companies – the ‘picks and shovels’ of the oil and gas industry.”

The Manual of Ideas: Natural gas prices have been depressed for several years due to abundant supply of shale gas, but oil and gas have historically been cyclical commodities. Do you believe the long-term supply equation for crude oil has changed, or is a substantial oil price rebound only a matter of time?

Bob Robotti: When thinking about the long-term supply function oil and the effect on the supply/demand equation (and therefore oil prices) there are a few facts to keep in mind. First, every existing oil and gas well drilled is depleting. That’s a physical fact. As prices remain low, capital invested in new wells around the world continues to decline. Inevitably the production decline will accelerate. At the same time, lower prices are encouraging demand.

We focus our energy investing on oil and gas services companies – the “picks and shovels” of the oil and gas industry. As volatile as it is, these are 30-40 year assets with better long-term predictability whereas the E&P companies have to remake themselves every 5-6 years. As a result, the level at which the price of oil or natural gas settles is not nearly as important to us as the level of activity.

As for the price of oil I do believe a substantial rebound in oil prices is only a matter of time. The question is how long a period of time? The other extremely pertinent question for us is what equilibrium price is needed to bring on incremental supply. The price that is needed is predicated on the ROI for that incremental production and the commodity price is only part of the equation. The full equation must consider the finding and development costs of incremental barrels of production versus the operating margin realized on the production. So two things will drive future oil and gas prices: (1) the finding and development cost (F&D costs) and (2) the operating cost on the wells developed (lifting cost).

In the current period, drilling and completion costs have declined dramatically (at least temporarily). At the same time, well operating costs have also declined. So in the current environment the oil price needed for economic wells is below where it was a year ago but still higher than the price of oil today.

The tipping point for the recent price decline has been the incremental production from North American shale oil. The intermediate-term questions that will determine how high oil prices need to appreciate is predicated on the size of the production opportunity from North American based shale oil. How many new fields can be identified and developed in the next few years? Can the recovery per well significantly increase in the next two years? My sense is that incremental production from known fields will be moderate. Remember, even the known developable shale oil fields today are being heavily drilled in the core area - that’s the lowest cost, highest productivity, and highest recoverable wells. The depletion of this high quality resource means that future production even in the known shale plays will be less productive and therefore higher cost. This requires higher prices to be economic.

“...substantially higher oil prices are likely in the next two years.”

Further, I’m of the belief that lower F&D costs and lower operating costs are more transitory than many argue today. Specifically, when you look at the high-quality drilling rig fleet in North America, the supply is tighter than currently perceived and the competitive, well-maintained pressure pumping fleets are being run down. When a recovery in drilling and completion activities arrives it will drive drilling and pressure pumping rates up dramatically. Lower F&D costs and well operating costs won’t last for long as activity starts to pick up.

All of these factors lead me to think that substantially higher oil prices are likely in the next two years.

Lastly, no discussion of the price of oil can be devoid of consideration for what certain producers might do differently than what they are doing today. A specific example would be a change on the part of OPEC (specifically, Saudi Arabia) in terms of its market strategy. We all know well that last November Saudi Arabia embarked on its renewed strategy to retake market share at any cost. I don't think the Saudis anticipated how low the price would go. OPEC, the Saudis and all major oil producers have been significantly hurt financially by this decision. Before the Saudis embarked on this new strategy, they appealed to other OPEC and non-OPEC producers to join with them to curtail production. After all, the world's excess productive capacity of 2 to 3 million barrels per day is no more than 3% of the world's demand. A similar fact pattern existed in the 1998 time period. With the same protestations by March 1999 certain non-OPEC producers joined with all of OPEC (including the Saudis) and agreed to curtail production to stabilize and boost the price of oil. This would be an extremely rational decision on the part of every oil producer. All too frequently, however, fighting and rhetoric over economic interests influence decisions.

MOI: When valuing an oil and gas company, how do you weigh reserves vs. production vs. other factors affecting intrinsic value?

Robotti: The value of an E&P company is the discounted value of its future production which is its economic reserves today plus the reinvestment of those reserves. The unpredictability of that, due to so many company specific facts, make investing in E&P companies a minefield.

In my view, evaluating the reserves is synonymous with intrinsic value. Production is historical information and the past is only somewhat helpful in estimating future producible reserves. Those reserves lead to tomorrow's production which generates future cash flows which of course determine intrinsic value. Of course, estimating a future event, in this case the economic developable future reserves, is rarely simple.

A critical element in properly evaluating reserves is a critical assessment of the honesty and integrity of management. Unfortunately, to make this evaluation properly there is no substitute for industry knowledge and experience.

MOI: What is your favorite current investment idea in the energy sector?

Robotti: As we discussed, our favorite investment ideas in the energy sector are not the producers but the servicers — the guys “selling the picks and shovels”. I don't have to worry about who finds the gold or what price they sell the gold for, all we have to worry about is whether they are out mining. As I pointed out previously, the production from existing wells will continue to deplete reducing supply which will inevitably lead to new wells that need be drilled and completed. This means the service guys will be out there working. It's harder to have certainty on the commodity price required. That price is all important to the owners and investors of that commodity but as important for those selling the “picks & shovels.”

Among the oil service companies we own, most compelling is **Subsea7** (SUBC.OB). Subsea7 is the company that installs all of the plumbing necessary to bring offshore discoveries into production. Subsea 7's valuation is heavily discounted - it's currently trading at 3x to 4x last year's earnings. The company maintains an extremely strong balance sheet with cash approximately equal to total debt and generates strong cash flows. The long-term outlook for the business is strong with a significant inventory of undeveloped deep-water fields while the complexity and scope of the work is increasing. The business possesses significant barriers to entry with the current downturn proving that point as would be competitors are starting to fall by the wayside. Subsea 7 has significant insider ownership increasing the likelihood the company will be opportunistic during the market downturn. All this translates into a per-share long-term earnings outlook meaningfully higher than last year's results. And an extremely mispriced security.

“Among the oil service companies we own, most compelling is Subsea7”

Bob Robotti
President & CIO

Best Ideas Conference 2018
January 11, 2018

What Makes Robotti Different

Analytical Edge

Within the context of a longer-term perspective and 30+ years of experience, we have the ability to develop a different conclusion than that of the market.

Informational Edge

Our network of industry relationships, focus on deep primary research, and experience serving on company boards, provides us with more pieces for building our information mosaic.

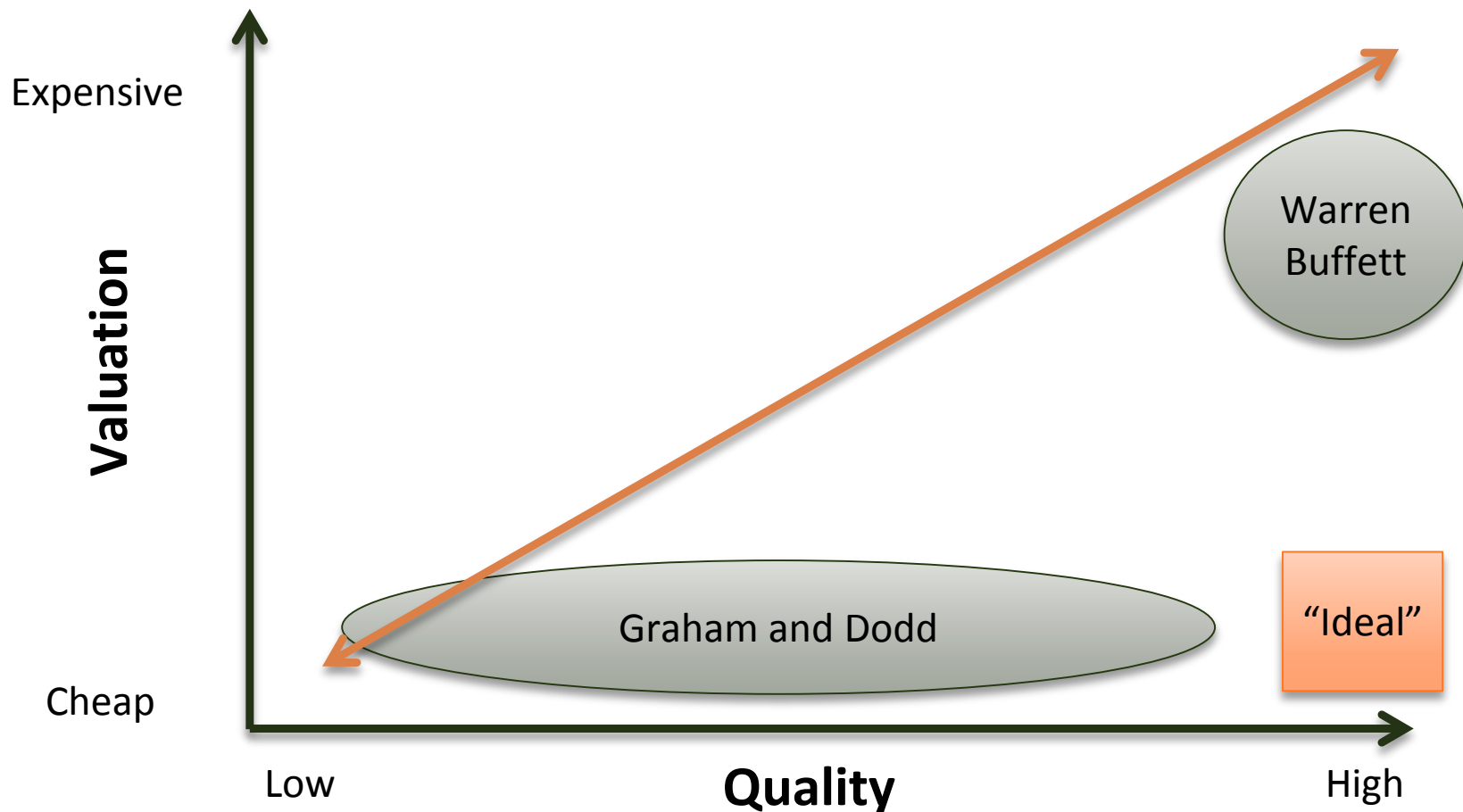
Leads Us To

Behavioral Edge

We take a longer-term view and have the ability to tolerate market swings.

Our behavioral edge comes from our ability to tolerate market volatility. As a result, our investment process concentrates on understanding the long-term normalized earning power of a business well before the “investing herd” gains interest.

Commonalities Among Value Investors

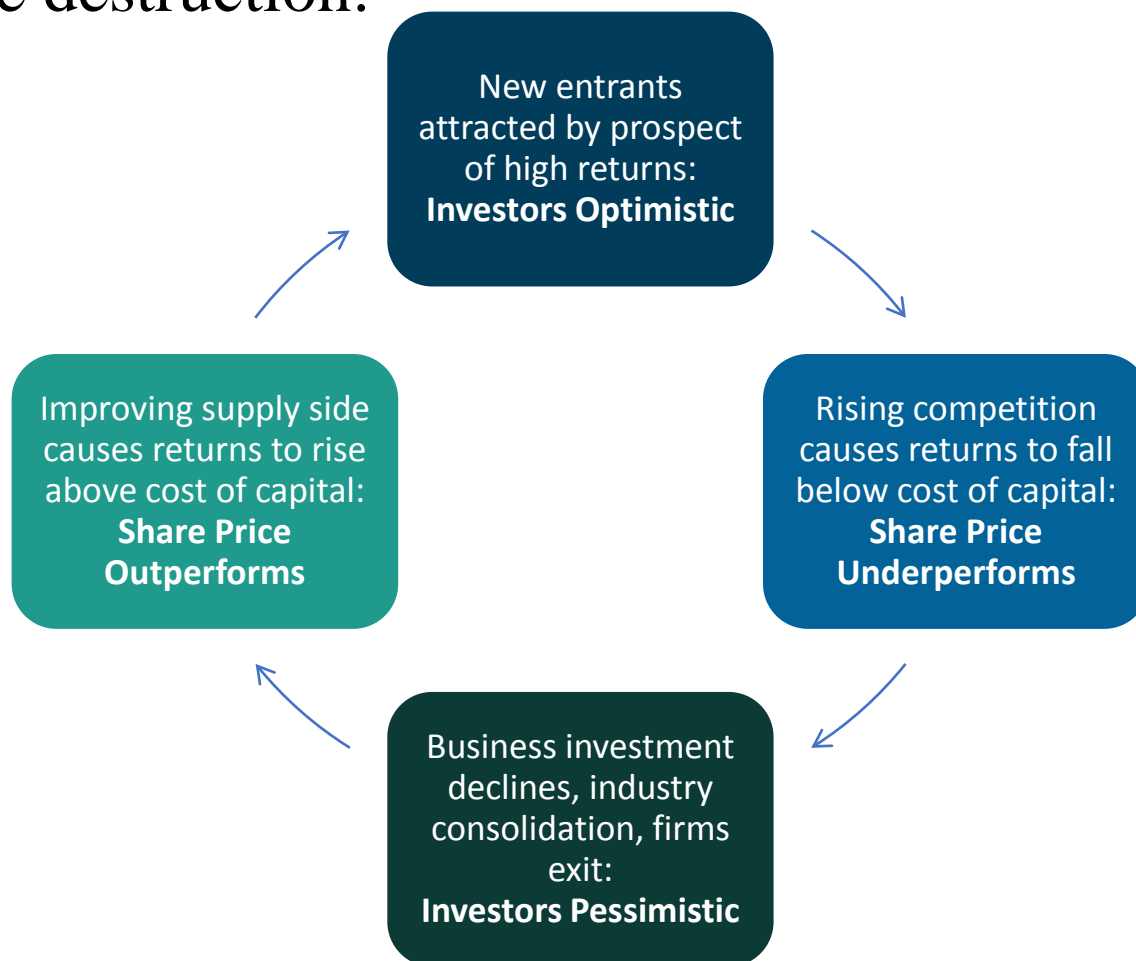


“To me, value investing is a big tent that accommodates many different people. At one end of the tent there is Ben Graham, and at the other end of the tent there is Warren Buffett, who worked with Graham and then went out on his own and made adjustments to the teachings of Ben Graham.”

- Jean-Marie Eveillard (*Graham and Doddsville* – Winter 2007 Ed.)

Understanding the Value of Economic Cycles

Economic cycles resemble Schumpeter's process of creative destruction:



Simple But Not Easy

- Opportunities created by capital cycle analysis often have long gestation periods as the timing of the pay-off can be highly uncertain.
- Holding a contrarian view is difficult – even for a value investor.

“A business which sells at a premium does so because it earns a large return upon its capital; this large return attracts competition; and generally speaking, it is not likely to continue indefinitely. Conversely in the case of a business selling at a large discount because of abnormally low earnings. The absence of new competition, the withdrawal of old competition from the field, and other natural economic forces should tend eventually to improve the situation and restore normal rate of profit on the investment.”

Security Analysis (1934 Edition)
Benjamin Graham and David Dodd



No Shortcut For Experience

“Good investing comes from good judgement. Good judgement comes from experience. Experience comes from bad judgement.”

-Chuck Akre



SEACOR Marine (NYSE: SMHI)



- SEACOR Marine was formed in June 2017 when SEACOR Holdings (CKH) spun-off its Offshore Marine Segment.
- SEACOR's fleet is highly specialized.
- Management has an exceptional track record of financial and operational management while being excellent stewards of capital.
- With the stock currently trading at <50% of tangible book value, we believe the stock is well positioned to benefit a recovery in the offshore energy market while also providing investors with a margin of safety.

Market Capitalization	
Price	\$12.92
+Dil Shrs	17.6
Market Cap	\$228
+LT Debt	142
+Carlyle Convert	175
+MI / Other	16
- Cash	130
Enterprise Val	\$430
P / Tangible Book	0.47x
Net Debt	\$187
52 Wk Hi	\$30.40
52 Wk Lo	\$11.66

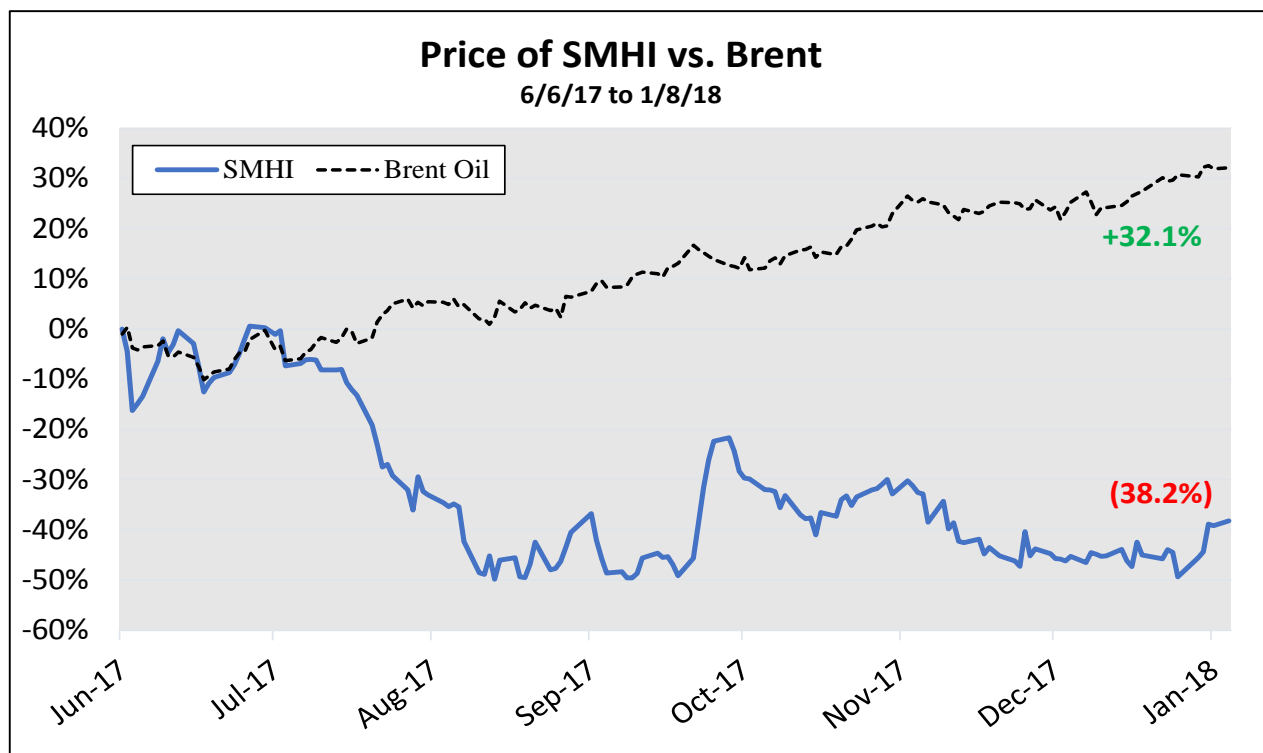
USD millions (except share price) as of 1/10/18

With a strong balance sheet and an exceptional track record of value creating capital allocation, we believe SEACOR Marine provides investors with an excellent opportunity to benefit from a recovery of the offshore energy industry.



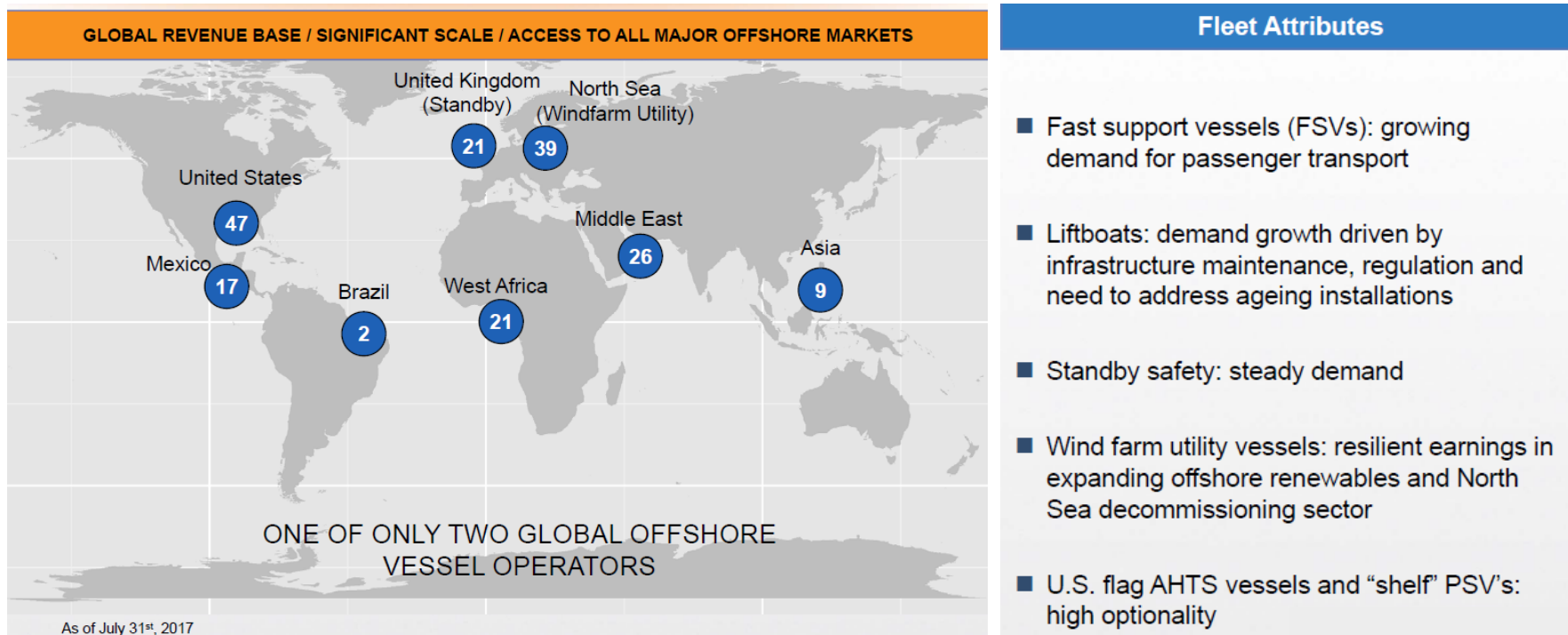
Spin-Off from SEACOR Holdings

- SEACOR Holdings' Offshore Marine segment was historically the primary earnings driver for SEACOR Holdings, contributing 45% of total revenue and more than half of total EBITDA in 2013-14.
- The idea of a spin-off surfaced at the time Carlyle Group announced an investment through the purchase of a \$175 million convertible note.



SEACOR Marine: The Business

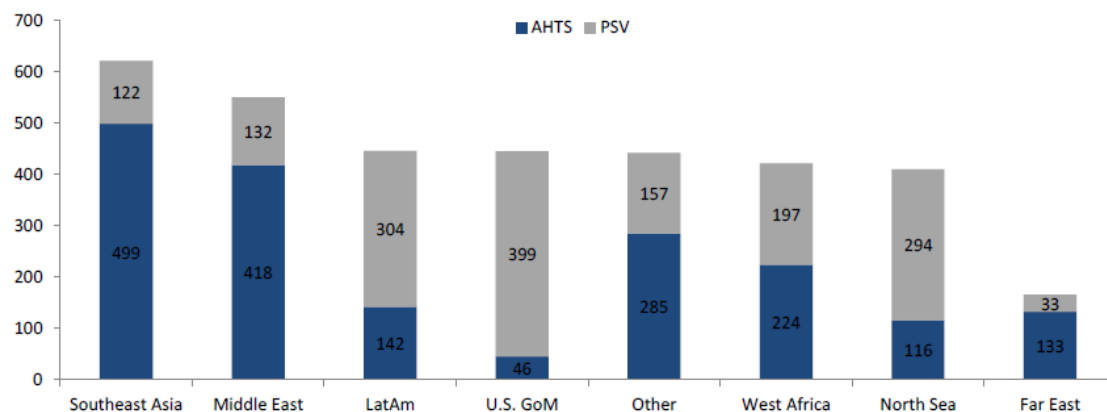
- Leading provider of global marine & support transportation services to the global offshore oil & gas industry.
- Distinctive and non-commoditized fleet support and specialty vessels.



Offshore Supply Vessels: A Highly Fragmented Industry

- The OSV industry is highly fragmented with more than 500 vessel operators worldwide and roughly ½ the global fleet controlled by the top 20 operators.

Figure 1. Global AHTS & PSV Fleet by Region, as of May 2017

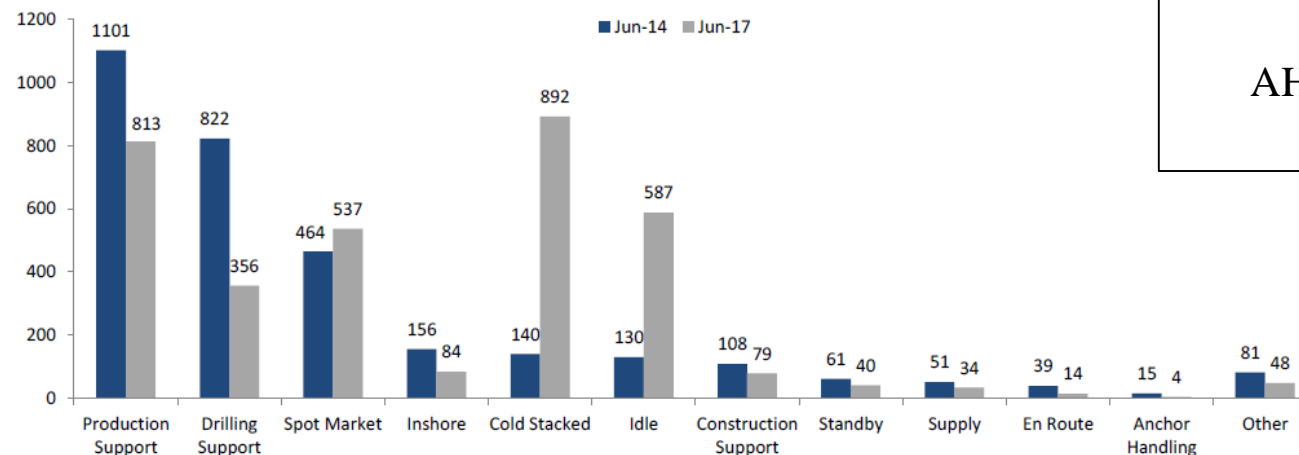


According to IHS, the global PSV and AHTS fleet is ~3,500 vessels:

PSV fleet: ~1,640 vessels
~12 years)

AHTS fleet: ~1,860 vessels
~14 years

Figure 2. Global PSV & AHTS Fleet By Activity

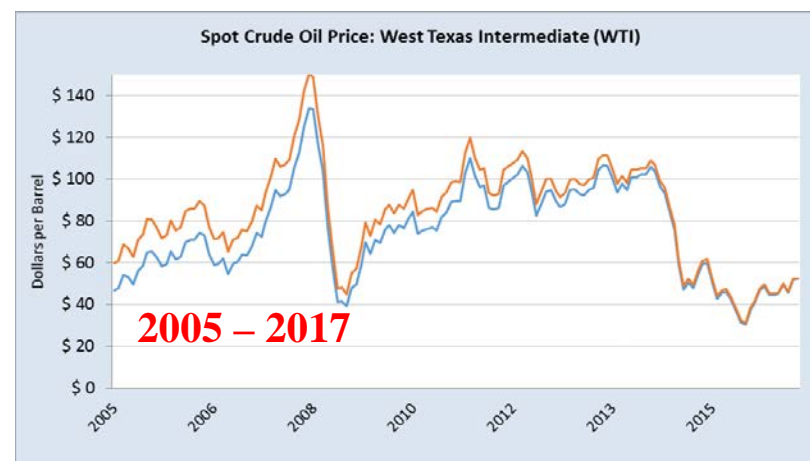
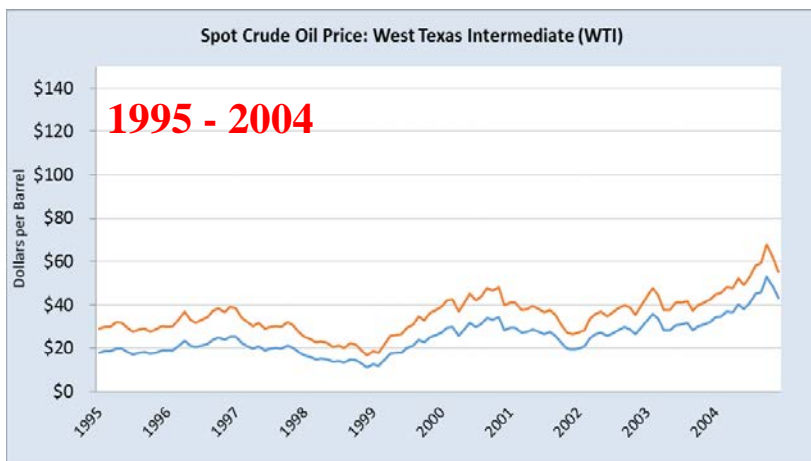
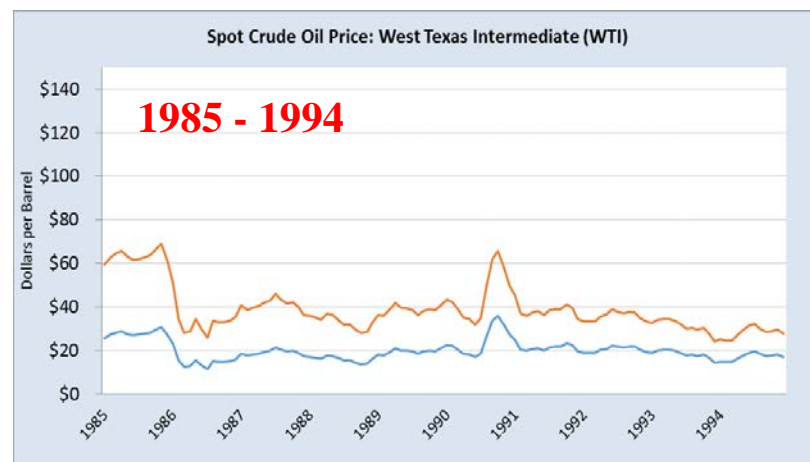
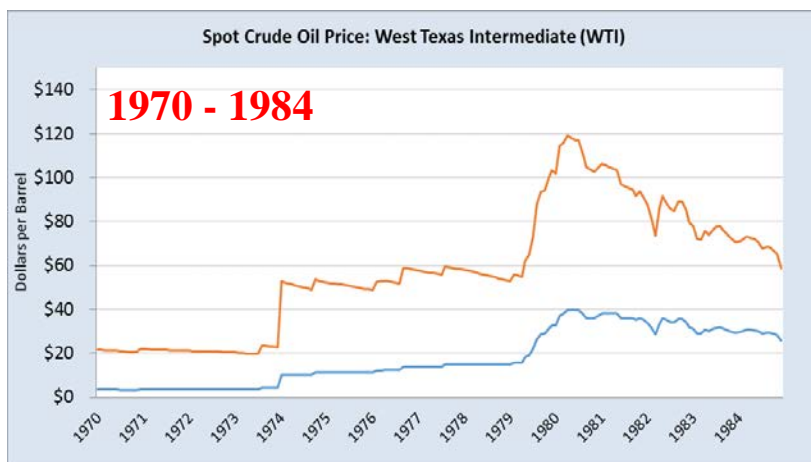


SEACOR Owns and Operates a Differentiated Fleet

- The most commonly cited offshore supply vessel classes are Platform Supply Vessels (PSV) and Anchor Handling Tug Supply Vessels (AHTS).
 - *It is important to note that these two categories of vessels make up less than 1/3 of SMHI's fleet.*
- While the OSV industry is often discussed as being homogeneous, there are very important nuances including:
 - Flag state
 - Location
 - Size
 - Power
 - Capacity
 - Design
 - Technology

How We Got Here: Historical Spot Crude Prices (in USD)

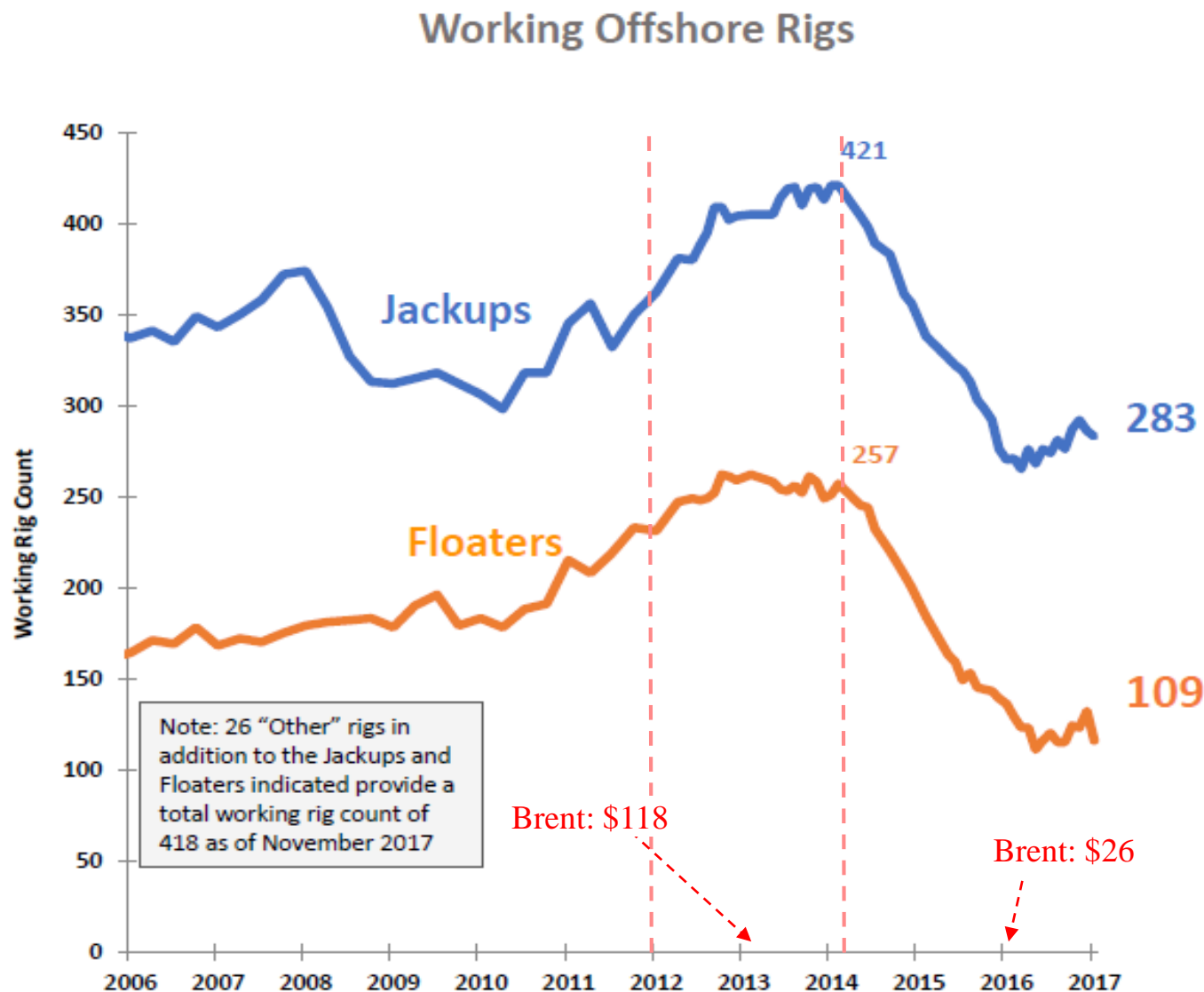
- Demand for SMHI's equipment and services is a first derivative of the price of oil.



WTI Spot, Nominal USD

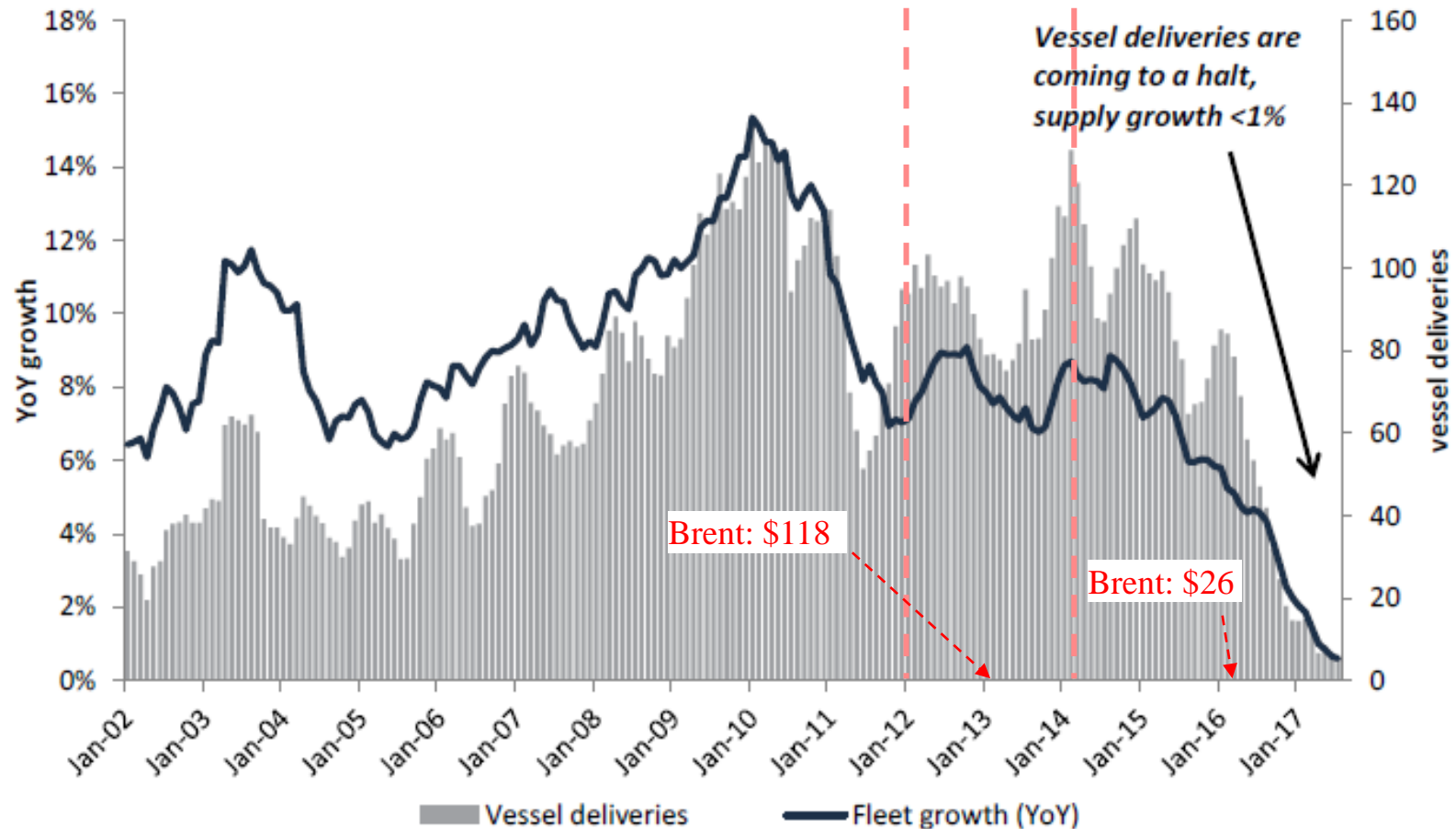
WTI Spot, Real USD

Demand is Driven by Offshore Rig Utilization



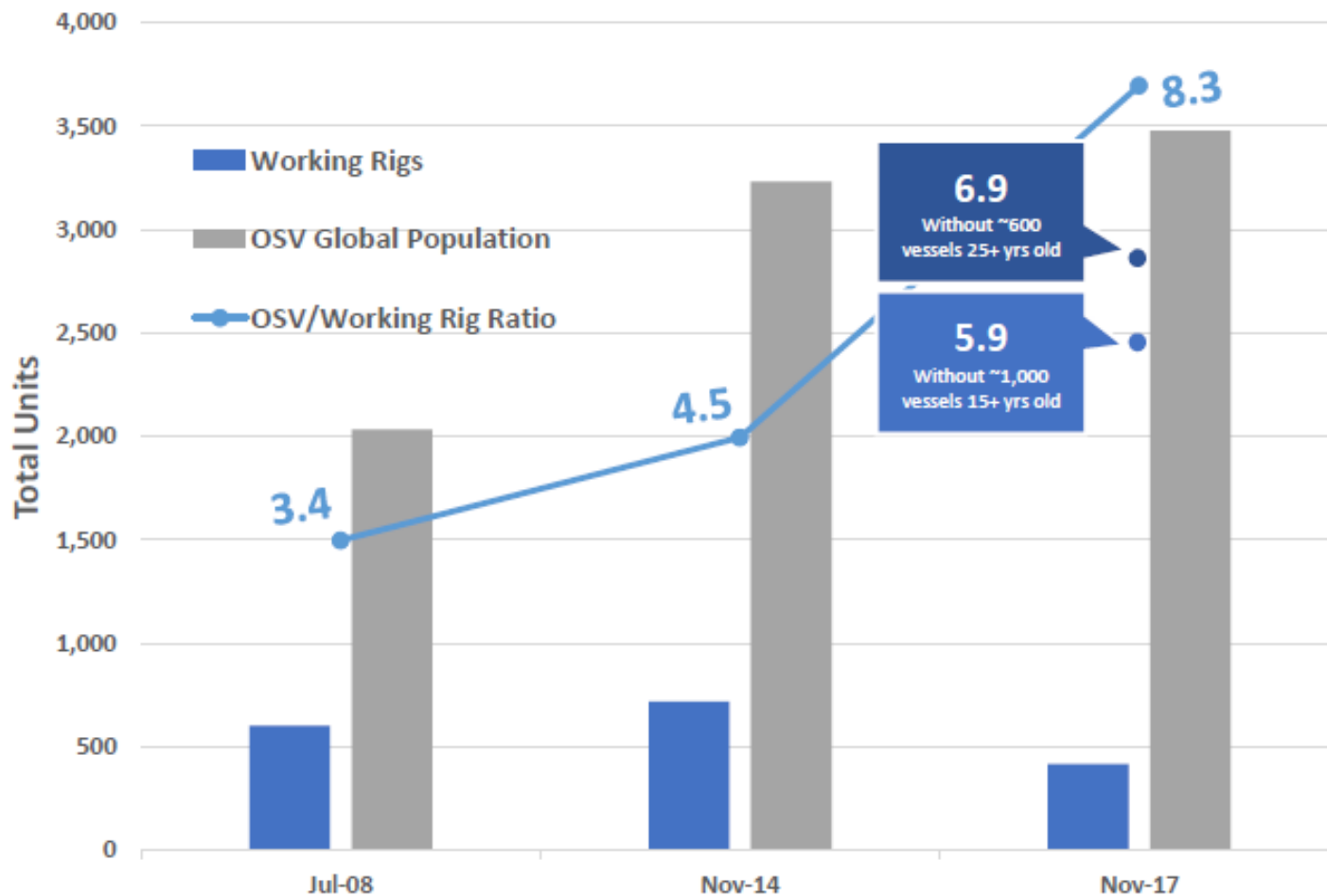
Supply Response to Rising Rig Utilization

OSV fleet growth (YoY) and deliveries (T6M) - Jan 2002 to Aug 2017



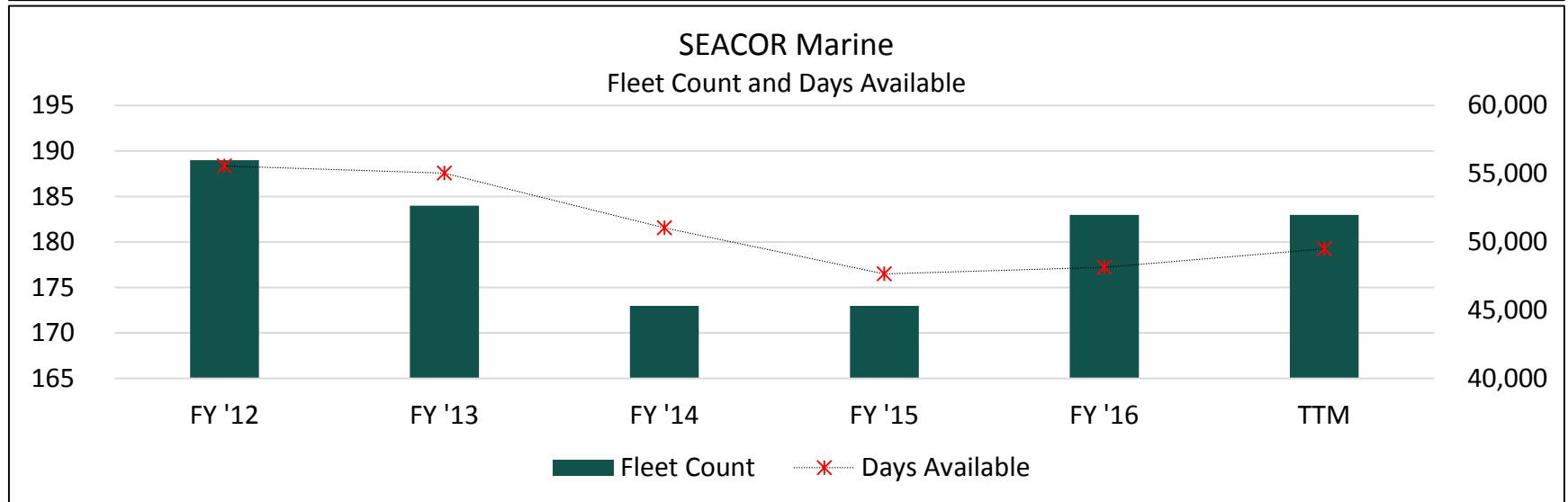
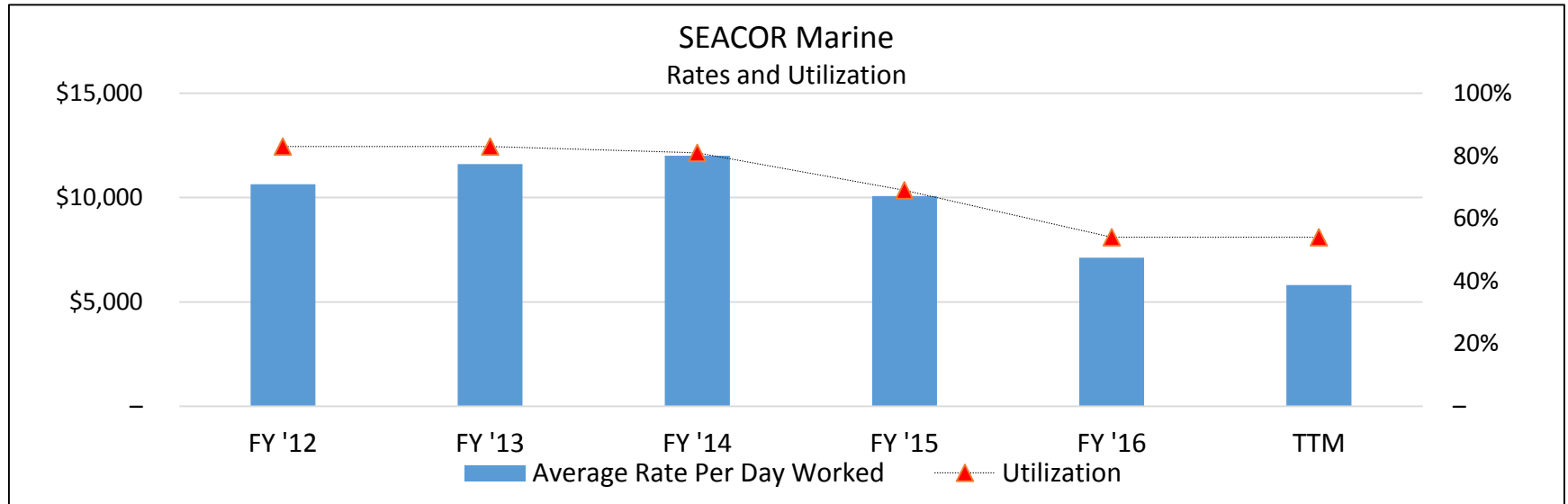
Source: IHS, Clarksons Platou Securities AS | *includes PSVs >50m LOA and >=1000 dwt + AHTS 4-10k bhp

Rising Rig Demand Leads to Vessel Oversupply



Source: IHS Markit and Tidewater

Key Industry Metrics



Institutional Capital Spots an Opportunity

SMHI has a strong financial profile supported by a large Carlyle investment in November 2015

Transaction Overview

- On November 30, 2015, SEACOR announced that its offshore marine subsidiary ("SEACOR Marine") entered into an agreement to issue \$175 million in convertible notes to investment funds managed and controlled by The Carlyle Group ("Carlyle")
- The transaction contemplated the eventual separation of SEACOR Marine from SEACOR's other business lines

Key Terms of Convertible Notes

Coupon / Term

- 3.75% cash coupon / 7 Years

Conversion Price

- \$43.00 (23.26 shares per \$1,000 principal amount of notes)

Ownership

- Implied ownership of 18.7% of the current outstanding shares of SEACOR Marine on a fully-diluted basis

upstream

Gulfmark strikes agreement for major debt restructuring

183 words
1 December 2016

US-based vessel operator Gulfmark Offshore has struck an agreement for major debt restructuring as it tries to stay afloat in a rapidly-deteriorating market.]]>

Gulfmark announced plans for a tender offer of up to \$300 million of unsecured senior notes due in 2022. The all-cash transaction would be financed by MFP Partners and Franklin Mutual Advisors through a \$100 million secured term loan and a \$100 million revolver. The investment also includes at least \$50 million in new equity, GulfMark said. Raging Capital has also committed to tender about \$85 million of the notes. Once the tender offer closes, GulfMark will offer current stockholders a chance to buy stock in the restructured company at the same equity price as the financiers. Gulfmark is "doing all it can to remain a going concern", said analysts at energy investment bank Tudor Pickering Holt. Capital One Southcoast analyst Joseph Gibney was optimistic on the move, saying it is "positive to simply move on, hit the re-set button, and account for a material portion of outstanding debt".

Upstream

Document: UPSTDM0000461320ccc3000kf

'New fund' targets Norway vessel assets

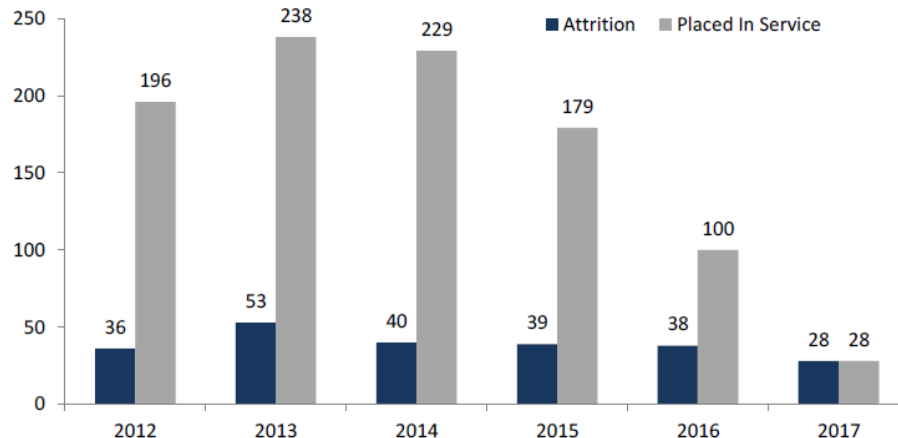
June 1, 2016



Distressed assets in Norway's debt-ridden offshore vessel sector are reportedly being targeted by a newly launched \$250 million fund forged by high-profile Norwegian investor Kristian Siem and US-based Elliott Management Corporation.

Supply: Attrition Lagged New Deliveries

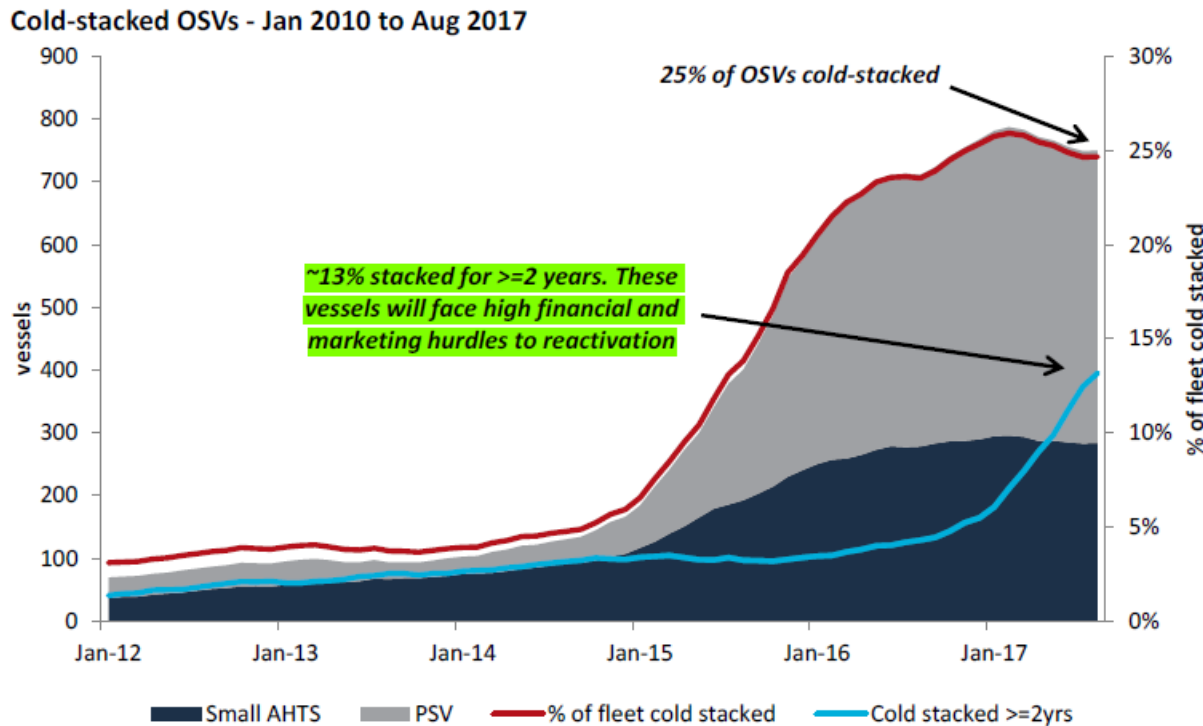
Figure 3. Attrition Has Lagged New Deliveries



Source: IHS Petrodata Marinebase, Evercore ISI Research

- SEACOR Marine is an industry outlier as the industry dataset of PSVs and AHTS vessels account for just 56 of SEACOR's vessels – less than 1/3 of its fleet.
 - Fast support vessels, liftboats and wind farm utility vessels which account for the remaining 2/3 of SEACOR's fleet are specialized in nature and tend to be less cyclical – however industrywide data on these vessels is less available.
- Over the past 5 years SEACOR has avoided investment in large, sophisticated PSVs and favored building its fleet of supply boats, fast support vessels and liftboats.
 - Early phases of an offshore recovery will likely center around deferred maintenance work, decommissioning, personnel support and shelf production.

Supply: Stalling The Inevitable

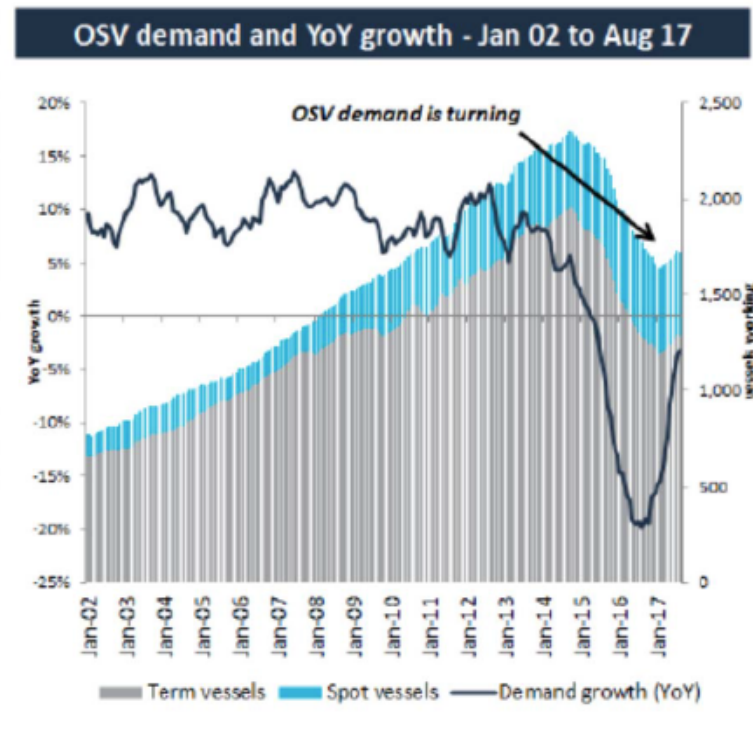


Source: IHS, Clarksons Platou Securities AS

- Scrapping a vessel is a costly endeavor for ship owners given the mobilization costs to remote scrapyards and inherently low scrap value.
- Many cold stacked vessels will not return to service due to the fact that 14% of the global PSV fleet and 20% of the global AHTS fleet is more than 25 years old and approaching 30-year drydocking bills while others will be required to undergo costly special surveys.

Why Now? Sentiment for Offshore Activity

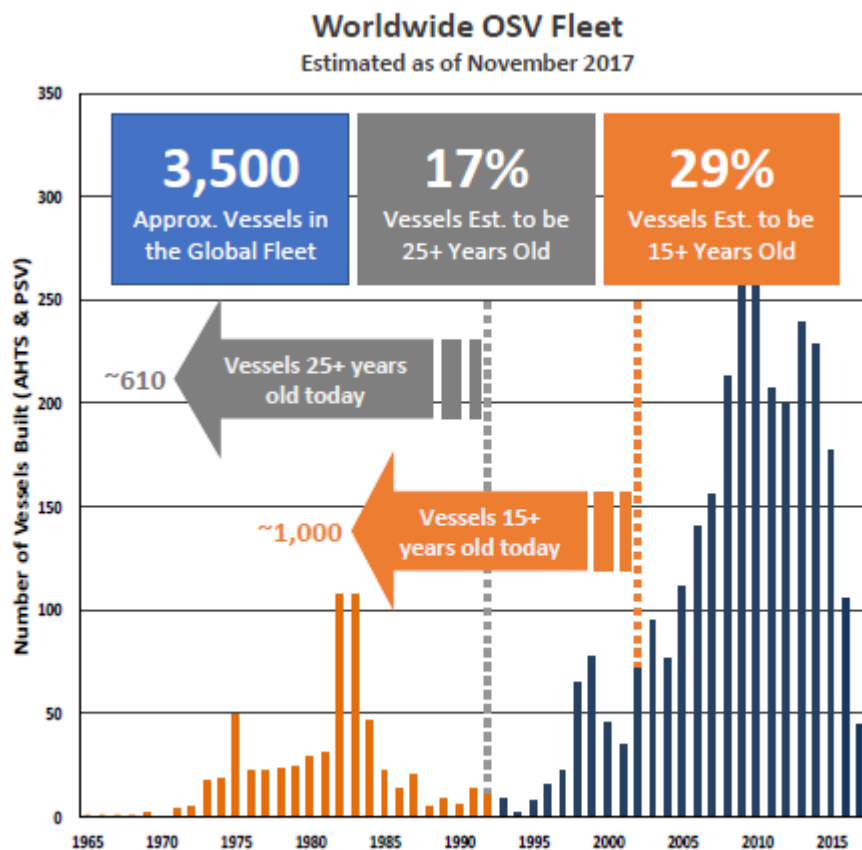
- General distress: numerous competitors have sought bankruptcy protection
- *"Consolidation necessary: will be "forced" due to lack of capital"* (Tradewinds, [Sept. 2016](#))
- *"The challenge: 'Opaque offshore vessel valuations a big hurdle to restructuring work'"* (Tradewinds, [Jan. 2017](#))
- *"Industry backs North Sea amid signs of recovery"* (Upstream, [Sept. 2017](#))
- *"Signs of recovery on horizon for UK Offshore Sector"* (Upstream [Sept 2017](#))
- *"Statoil Johan Castberg break-even at \$30/bbl: Current estimate 3 x lower than original number"* (TPH Energy Research, [Sept.2017](#))
- **The opportunity: "OSV utilisation has bottomed out" and "OSVs moving out of hell into purgatory"** (Pareto, [Aug. 2017](#))
- *"25% of the global fleet is cold-stacked. The fate of this capacity will have profound impact on the market balance"* (Clarkson Platou, [Sept 2017](#))



Source: Clarkson Platou

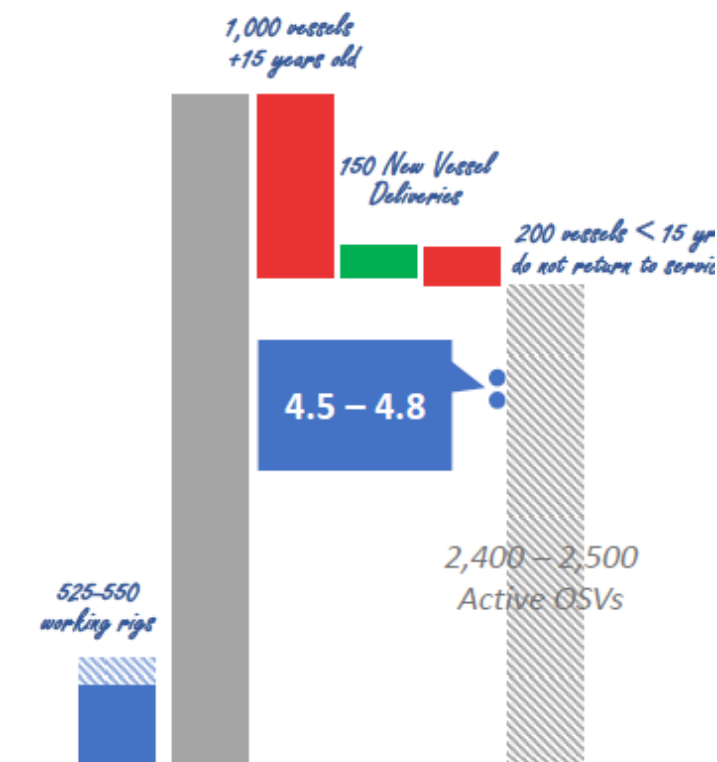
SMHI is ideally positioned to be a leader in **recovering** sector

Industry Drivers – Looking Backwards and Forwards



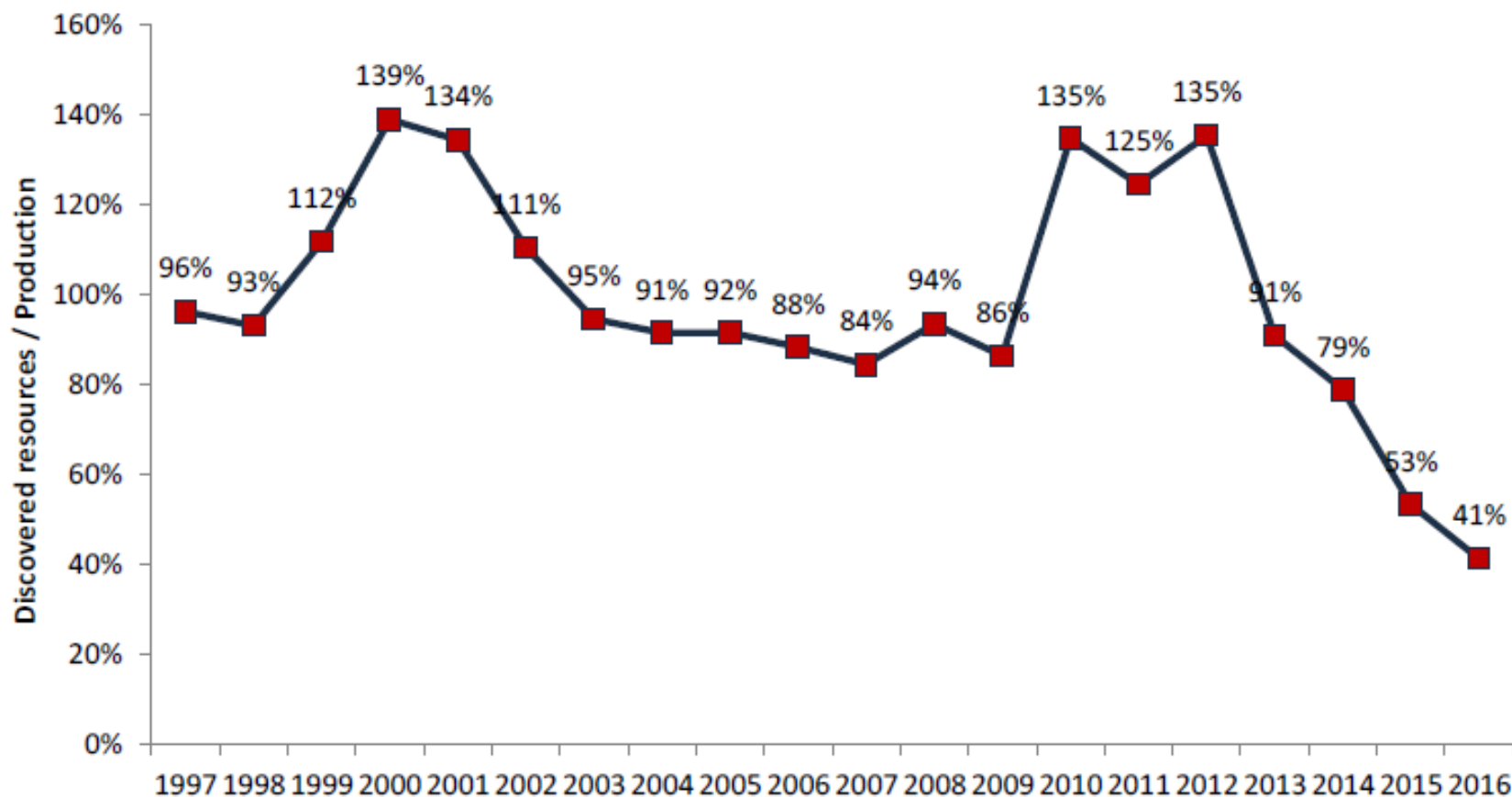
As of November 2017 there are approx. 251 additional AHTS and PSVs (~7% of the global fleet) under construction. In our view, a material number of these vessels will not be completed and delivered.

Market Equilibrium Requires an Increase in Demand and a Reduction in Supply



Offshore Reserve Replacement Ratio Continues to Fall

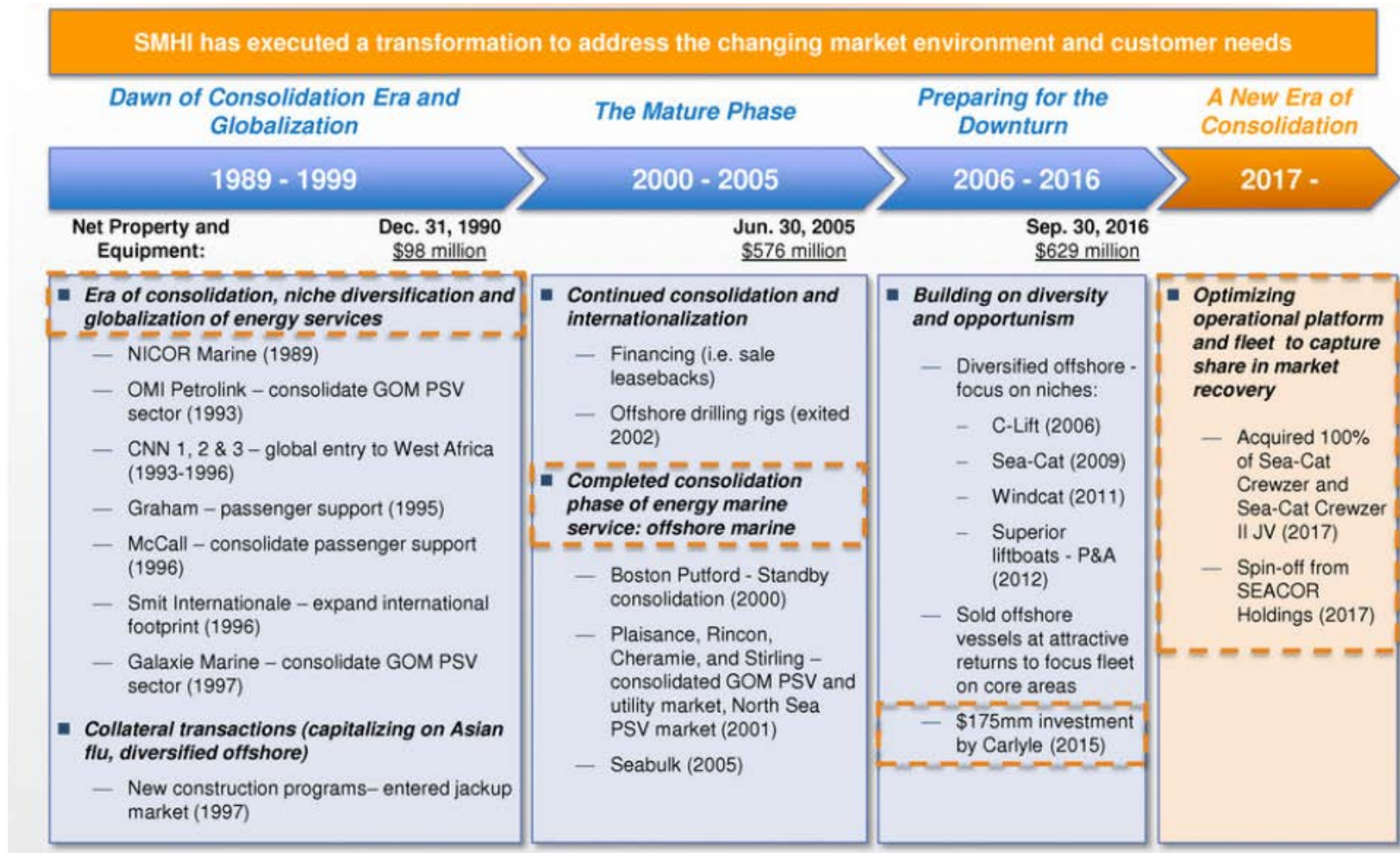
Offshore reserve replacement ratio (trailing 3 year average) - last 20 years



Source: Rystad Energy



SEACOR – A Strong Track Record



Management: Focused on Value Creation

- Experienced Management with demonstrated history of investing in tough times and harvesting in the boom
 - Charles Fabrikant, Founder and Chairman of the Board
 - John Gellert, CEO, over 25 years industry experience with SEACOR, responsible for SEACOR's offshore business since 2003
 - Sold over 500 vessels since 1995
 - \$1.54 billion capex funded with proceeds from asset dispositions of \$1.66 billion since 2005
 - 1992-2003: 13.5% average ROE

Strategic Plan: Thinking Like An Intelligent Investor

SEACOR MARINE

Strategy:

- Focus on niches or regions with limited participants / order book / excess capacity coupled with growing demand
 - Passenger Transfer
 - Decommissioning
 - Offshore Wind
 - Standby Safety
 - Shelf PSV Support
 - Middle East and Mexico
- Consolidation
 - Asset Rationalization
 - Cost Efficiencies
- Opportunistic acquisition of offshore assets at deep value prices.

SEACOR HOLDINGS

Objectives:

- Pursue risk adjusted returns on equity
- Pursue long-term appreciation (“real growth”) with capital preservation

Strategy:

- Adhere to capital and balance sheet discipline: we live within our means
- Opportunistically deploy capital into cyclical assets
- Maintain flexibility and leverage off of existing businesses
- Maintain liquidity to buy deep value
- Harvest our gains and not “hug” assets for continuous earnings
- Capitalize on tax efficiency

A DOLLAR OF GAIN IS AS GOOD AS RENTAL INCOME.



Capex Plans

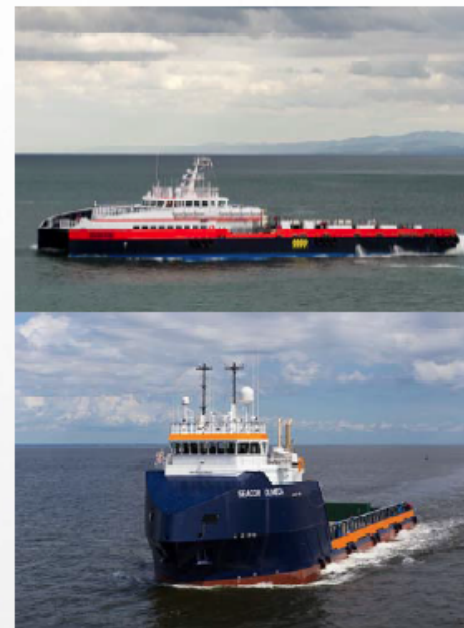
Building Vessels Unique to Market: Capitalizing on Downturn, Strengthening Position in Niche Businesses

■ Six Fast Support Vessels

- Build to meet current and growing demand for efficient and comfortable crew transport
- Grandfathered under US emission requirements. No additional capacity being added
- Deferring deliveries possible: SMHI can adjust CAPEX to demand and liquidity needs

■ Three Handy Size Supply Vessels

- First two vessels of series sold to Mexmar JV and employed on long-term charters with Pemex.
- Underserved market. Good employment prospects



	2017		2018				2019				2020		Total
	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	
Fast Support	2	-	-	-	-	1	-	1	-	1	-	1	6
Supply	-	-	1	-	1	-	1	-	-	-	-	-	3
Wind farm utility	-	1	-	-	-	-	-	-	-	-	-	-	1
Capital Commitments (in millions)	\$10.5		\$51.0				\$13.2				\$1.8		\$76.4

Note: Subsequent to June 30, 2017, the Company committed to acquire one supply vessel and one wind farm vessel for \$19.4 million.

As of June 30, 2017

10

Key Demand Drivers

“Drilling is the sizzle but Production and Maintenance is the meat.”

Oil and Gas									
Vessel type	SMHI vessels	Exploration Drilling	Develop. Drilling	Production	Maintenance	Plug & Abandonment	De-commissioning	Passenger Transfer	Offshore Wind
Liftboat	15			X	X	X	X		X
PSV (<3,500DWT) *	22	X	X	X	X				
PSV (>4,000DWT)	4	X	X	X					
FSV	50	X	X	X	X			X	
AHTS	23	X	X	X		X			
Standby	21	X	X	X	X	X	X		
Windfarm Utility (WFUV)	41			X	X	X	X	X	X
RECOVERY STAGE IN CYCLE		LATE	MID	MID	EARLY	MID	EARLY	EARLY	N/A

Fleet: 177 Vessels

DIVERSIFIED FLEET: POSITIONED TO MEET CURRENT DEMAND AND CAPITALIZE ON EARLY AND LATER STAGES OF MARKET RECOVERY

As of July 31st, 2017. Excludes six specialty vessels.

* Vessels of less than 2,500 DWT in this category are also referred to in this presentation as “shelf PSV’s” or “handy size PSV’s”.

As of September 30, 2017 there was 1 additional PSV in the fleet.

9



Liquidity – Limited Near-Term Maturities

Debt Issue:	Jun-17	Debt Maturities						
		2017	2018	2019	2020	2021	2022	Thereafter
3.75% Carlyle Convertible Notes	175.0	-	-	-	-	-	175.0	-
Falcon Global (Intl. Liftboats) ¹	57.8	4.4	5.9	5.9	5.9	5.9	29.8	-
Sea-Cat Crewzer I & II (Catamarans)	41.7	2.3	4.5	34.9	-	-	-	-
Sea-Cat Crewzer III (Newbuild Cats)	26.1	1.1	2.2	2.2	2.2	2.2	2.2	14.0
Windcat Workboats	24.0	-	-	-	-	24.0	-	-
Liftboat Acquisition Notes	16.5	16.5	-	-	-	-	-	-
Other	10.1	1.0	2.0	3.9	2.0	1.2	-	-
Outstanding Principal	351.2	25.3	14.6	46.9	10.1	33.3	207.0	14.0
Discount/Issuance Costs	(35.7)							
Outstanding Debt	315.5							

As of June 30, 2017

¹ Facility contractually matures in 2022. Falcon Global is currently not in compliance with certain financial covenants in the facility, including its debt service coverage ratio, maximum leverage ratio and minimum liquidity covenant and has received waivers from its lenders for these financial covenants for testing periods through and including December 31, 2017. Given the uncertainties surrounding the future financial performance of the two newly delivered liftboats and Falcon Global's ability to meet its financial covenants for the next twelve months, the Company has classified the outstanding amounts due under the term loan facility as current obligations.

Operating Income and Returns

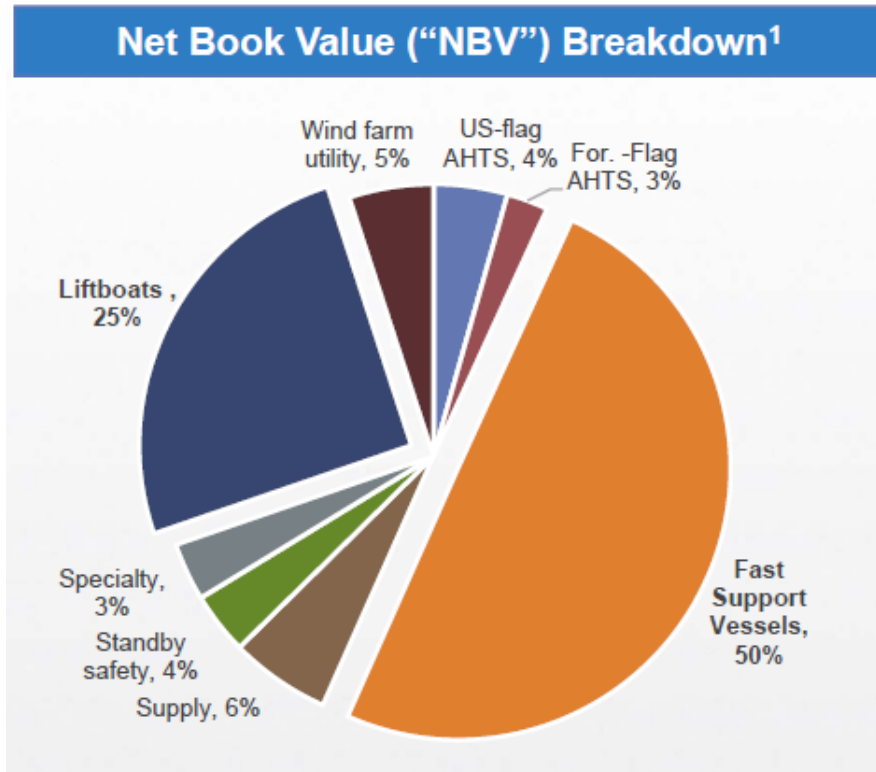
	2012	2013	2014	2015	2016	H12017
Fleet DVP:						
Fast support	33,407	38,507	25,824	18,872	22,478	1,547
Wind farm utility	12,395	12,749	12,755	12,757	11,638	6,306
Liftboats	42,151	45,200	28,258	(3,842)	(5,531)	(5,878)
Standby safety	16,586	12,525	16,567	13,964	10,426	3,677
Anchor handling towing supply	41,442	56,286	61,927	49,322	13,389	(2,168)
Supply	36,544	34,535	32,739	15,298	177	828
Specialty	906	9,191	5,993	7,889	7,026	(722)
Other non-vessel marine services	8,556	5,181	8,268	1,145	6,685	2,457
Consolidated DVP	191,987	214,174	192,331	115,405	66,288	6,047
Less:						
Leased-in equipment expenses	21,850	28,956	27,479	22,509	17,577	7,281
Administration and general expenses	59,253	60,279	58,353	53,085	49,308	33,531
Depreciation and amortization	61,542	65,424	64,615	61,729	58,069	27,136
Operating Income (Loss) before Asset Dispositions and Impairments	49,342	59,515	41,884	(21,918)	(58,666)	(61,901)
Gains (Losses) on Asset Dispositions and Impairments, Net	14,876	28,664	26,545	(17,015)	(116,222)	(1,499)
Operating Income (Loss)	64,218	88,179	68,429	(38,933)	(174,888)	(63,400)

Direct vessel profit (defined as operating revenues less operating expenses excluding leased-in equipment and as presented in the preceding table, "DVP") is our measure of segment profitability when applied to individual segments and a non-GAAP measure when applied to fleets or the combined fleet. We believe that DVP is a critical financial measure to analyze and compare the operating performance of our individual vessels, fleet categories and combined fleet, without regard to financing decisions (depreciation for owned vessels vs. leased-in expense for leased-in vessels). DVP is also useful when comparing our fleet's performance against those of our competitors who may have differing fleet financing structures. DVP has material limitations as an analytical tool in that it does not reflect all of the costs associated with the operation of our fleet, and it should not be considered in isolation or used as a substitute for our results as reported under GAAP.

	2012	2013	2014	2015	2016
Return on Avg Insured Value	10.6%	11.2%	10.5%	2.2%	(12.3%)
Avg Return on Avg Insured Value	7.90%				
CKH Avg ROE (1992 - 2003)	13.50%				



Margin of Safety



- Significant discount to tangible book value.
- Significant discount to insured vessel value.

Risks To Our Thesis

- Oil prices could fall further or remain at current levels for an extended period leading major oil companies to defer capital expenditures and delay deepwater developments.
- Ship owners could delay scrapping older vessels.
- Liquidity could become a concern if the downturn extends even further as the company generated negative free cash flow in the prior two quarters.

Disclosure: Ownership Information

<u>Disclosures</u>	SEACOR Marine (NYSE:SMHI)
Robert Robotti and/or members of his household has a financial interest in the following securities	Yes
Robotti & Company or its affiliates beneficially own common equity of the following securities	Yes
Robotti & Company or its affiliates beneficially own 1% or more of any class of common equity of the following securities	No
Robert Robotti serves as a Director or Officer or Advisory Board Member of the following securities	No

Disclaimer: Analyst Compensation: While this report is not a research report of any broker or dealer, compensation of analysts of the Firm is based on: (1) the analyst's productivity, including the quality of the analyst's research and the analyst's contribution to the growth and development of our overall research effort; (2) ratings and direct feedback from our investing clients, our sales force and from independent rating services. The Firm's management is responsible for establishing these compensation guidelines and for reviewing and approving compensation. Analyst contribution (if any) to the investment banking business of any affiliate of the Firm is not a factor in determining his/her compensation for either entity and compensation is not, directly or indirectly, related to the specific recommendations or views expressed in the report.

Analyst Certification: The author certifies that the views expressed in this financial model accurately reflect his personal views about the subject securities or issuers and that no part of his or her compensation was, is, or will be directly or indirectly related to the specific recommendations or views contained in this presentation. The author, from time to time, may have long or short positions in, and buy or sell, the securities, or derivatives (including options) thereof, of companies mentioned herein. This is not a complete analysis of every material fact regarding any company, industry or security.

Disclaimer

Robotti & Company Advisors, LLC (the “Firm”) is not providing investment advice through this material. This presentation is provided for informational purpose only as an illustration of the firm’s investment philosophy and shall not be considered investment advice or a recommendation or solicitation to buy or sell any securities discussed herein, and does not contain enough information to be considered a recommendation or a research report.

As of the date of this presentation the firm continues to own the securities discussed herein. These opinions are not intended to be a forecast of future events, a guarantee of future results, or investment advice. Past performance is not indicative of future results, and no representation or warranty, express or implied, is made regarding future performance.

Robotti & Company Advisors, LLC or its affiliates may engage in securities transactions that are inconsistent with this communication and may have long or short positions in such securities. The information and any opinions contained herein are as of the date of this material, and the firm does not undertake any obligation to update them.

This material does not take into account individual client circumstances, objectives, or needs and is not intended as a recommendation to any person who is not a client of the firm. Securities, financial instruments, products or strategies mentioned in this material may not be suitable for all investors. The Firm does not provide tax advice. Investors should seek tax advice based on their particular circumstances from an independent tax advisor.

In reaching a determination as to the appropriateness of any proposed transaction or strategy, clients should undertake a thorough independent review of the legal, regulatory, credit, accounting and economic consequences of such transaction in relation to their particular circumstances and make their own independent decisions. By virtue of this publication, neither the Firm nor any of its employees shall be responsible for any investment decision.

This confidential presentation contains information that has been compiled, by the Firm, from sources believed to be reliable; however, there can be no guarantee as to the accuracy or completeness of such information. It also contains statements, estimates and projections made by various third party companies with respect to their historical and projected performance. There can be no assurance that such statements, estimates and projections will be realized and actual results may vary materially from those indicated. Further, in any case, the Firm does not represent nor is affiliated with any of the third party companies and other entities named and makes no representations as to the reasonableness of such assumptions or the accuracy or completeness of the information contained herein. These materials are for the confidential use of only those persons to whom it is transmitted.

This report may discuss numerous securities, some of which may not be qualified for sale in certain states and may therefore not be offered to investors in such states. This document should not be construed as providing investment services. Investing in non-U.S. securities including ADRs involves significant risks such as fluctuation of exchange rates that may have adverse effects on the value or price of income derived from the security. Securities of some foreign companies may be less liquid and prices more volatile than securities of U.S. companies. Securities of non-U.S. issuers may not be registered with or subject to Securities and Exchange Commission reporting requirements; therefore, information regarding such issuers may be limited.

Robert Robotti

President, Robotti & Company

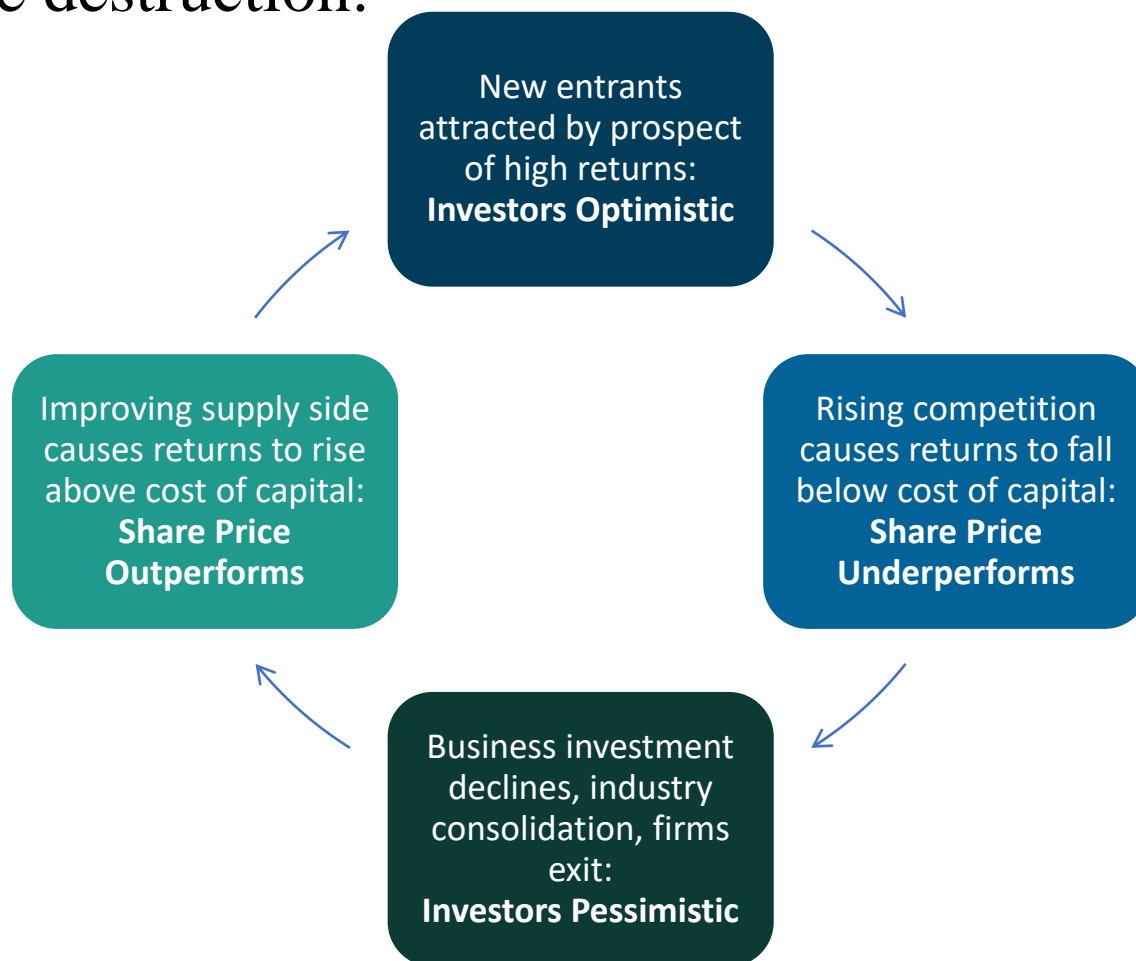


What high-level business characteristics are you conditioned to avoid?

- Cyclical Industries
- Capital Intensive Businesses
- Heavy Exposure to Commodities

Understanding the Value of Economic Cycles

Economic cycles resemble Schumpeter's process of creative destruction:



Cyclicals Amplify Mr. Market's Manic Depressive Nature

“A business which sells at a premium does so because it earns a large return upon its capital; this large return attracts competition; and generally speaking, it is not likely to continue indefinitely. Conversely in the case of a business selling at a large discount because of abnormally low earnings. The absence of new competition, the withdrawal of old competition from the field, and other natural economic forces should tend eventually to improve the situation and restore normal rate of profit on the investment.”

Security Analysis (1934 Edition)

Benjamin Graham and David Dodd



What Makes Us Different

Analytical Edge

Within the context of a longer-term perspective and 30+ years of experience, we have the ability to develop a different conclusion than that of the market.

Informational Edge

Our network of industry relationships, focus on deep primary research, and experience serving on company boards, provides us with more pieces for building our information mosaic.

Leads Us To

Behavioral Edge

We take a longer-term view and have the ability to tolerate market swings.

Our behavioral edge comes from our ability to tolerate market volatility. As a result, our investment process concentrates on understanding the long-term normalized earning power of a business well before the “investing herd” gains interest.

Theory to Practice:
Finding Moats in Cyclical Industries

Finning International (TSX:FTT)

Summary

- Finning International (TSX:FTT) is the world's largest Caterpillar dealer with exclusive territory rights in 6 countries.
- The CAT dealership is a great business with a sustainable competitive advantage and high returns on capital. High margin recurring aftermarket parts & service business helps reduce volatility.
- New management is focused on improving ROIC and free cash flow but results have been masked by weak end markets.
- We believe the company trades at a discount to its normalized earning power.



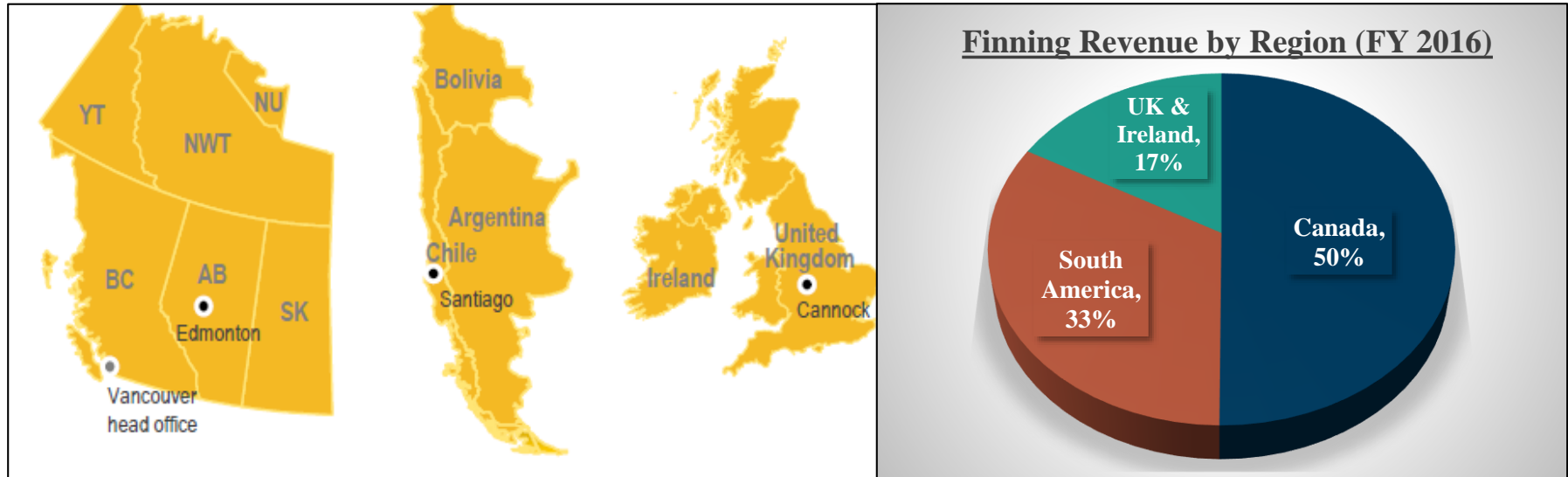
CND \$mm 6/20/17

Market Capitalization	
Price:	\$25.48
Dil Shrs:	168
Market Capitalization	4,290
LT Debt	1,572
Cash	489
Enterprise Value	5,373
Net Debt	1,083
Net Debt / EBITDA	2.0x
Dividend Yield	2.9%
52 Week Hi	\$28.02
52 Week Lo	\$20.53

(Annual)	FY '13	FY '14	FY '15	FY '16	Consensus Est.	
					2017E	2018E
Revenue	6,756	6,918	6,275	5,628	5,757	6,123
growth	2.7%	2.4%	(9.3%)	(10.3%)	(16.8%)	6.4%
Adj EBITDA	736	720	604	465	554	632
margin	10.9%	10.4%	9.6%	8.3%	9.6%	10.3%
Op. Income	645	506	272	193	365	431
margin	9.6%	7.3%	4.3%	3.4%	6.3%	7.0%
Diluted EPS	\$1.94	\$1.84	(\$0.94)	\$0.39	\$1.22	\$1.56

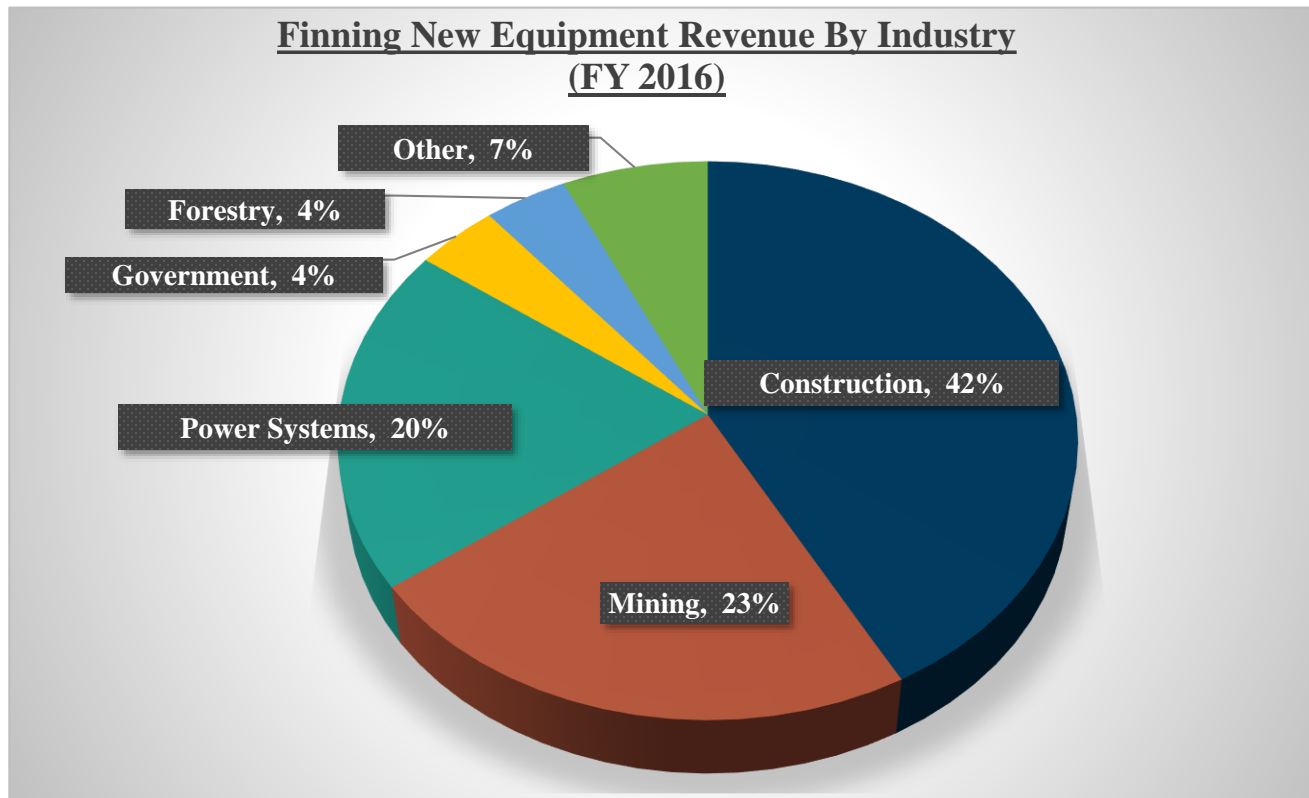
Business Background

- Finning provides sales, rental and aftermarket parts and services for Caterpillar equipment and engines.
- Based in Vancouver, Canada, Finning has operations in 6 countries (Canada, Chile, Argentina, Bolivia, UK and Ireland).
- Finning was founded in 1933 and has 11,900 employees worldwide (~65% technicians / mechanics).

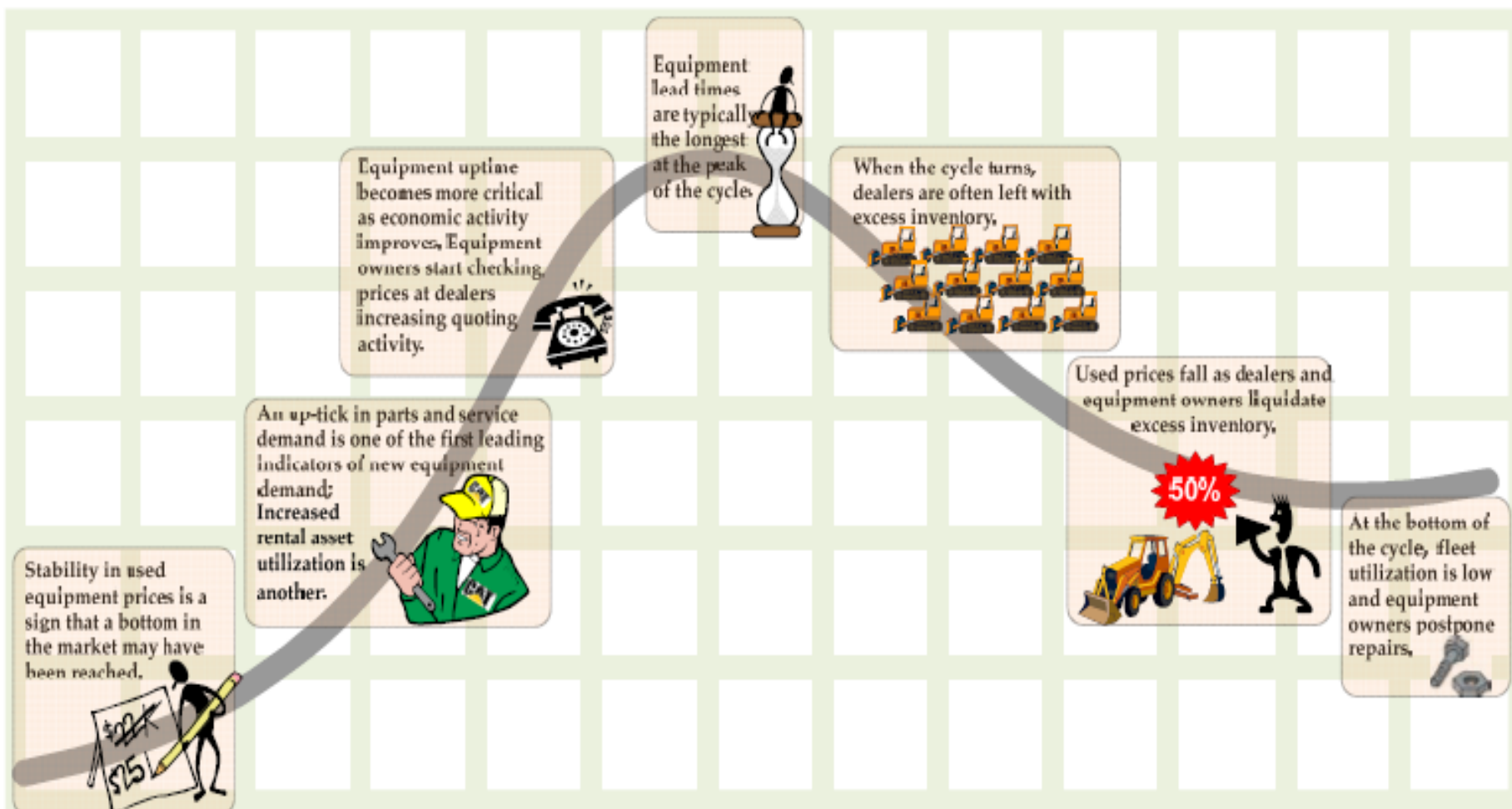


End Markets Served

- **The strength of a dealer's after-market support has become the paramount factor in the equipment purchasing decision.**
 - Finning delivers solutions that enable customers to achieve the lowest equipment owning and operating costs while maximizing uptime.



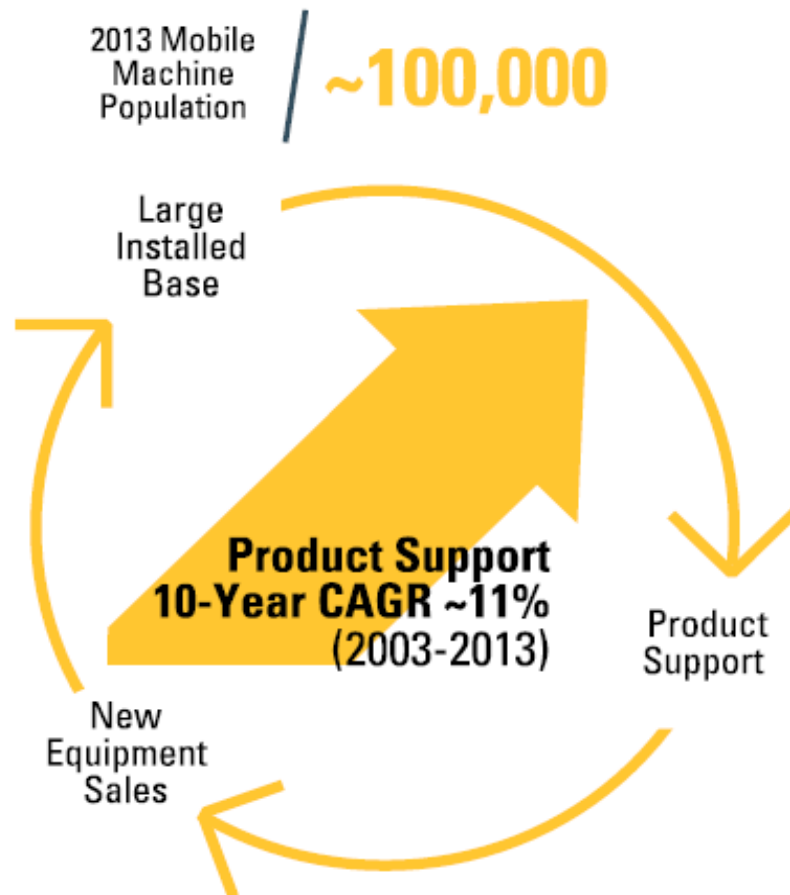
Summary of the Equipment Cycle



Business Model: Equipment Distribution

- **New equipment is the bond between a distributor and a customer that hopefully spans many dollars of aftermarket parts, maintenance and service.**
 - New Equipment sales represented 32% of Finning's revenue in FY 2016.
- **New Equipment sales increase market share for Caterpillar - meaning more dollars for everyone.**
 - While price certainly plays a role in the purchase decision, the strength of a dealer's after-market support is equally, if not more important.
- **The actual sales process varies greatly due to the wide range of equipment sold.**
 - In heavy mining, a Caterpillar 797 truck can cost over \$5 million, is built to spec and can have a long lead time. However, a customer may buy a small skid-steer loader off the lot.

Margins / Aftermarket



2008 – 2014
Machine Population – Canada
Compound Annual Growth Rate: 4%



797 Off-Highway Trucks
172 → 287



Medium Wheel Loaders
3,040 → 3,702



Medium Track Type Tractors
6,624 → 7,940

2008 – 2014
Power Systems



3600 Series Gas Engines
82 → 340

Product Support – Canada Mining Opportunities

Mining Truck
797



Large Dozer
D11 & D10



At Dec 2016

Population⁽¹⁾

316

788

Customers

6

15+

1st replacement of large components

~2 years/
18,000 hours

~1.5 years/
12,000 hours

Component exchange during life span

6-7 times

2-4 times

Expected life span before rebuild

~12 years/
80,000 hours

~8 years/
48,000 hours

Average annual product support

C\$ 1.0-1.2M

C\$ 0.3-0.5M

Average age of population⁽¹⁾

~8 years

~7 years

Purchase price

US\$ 5-7M

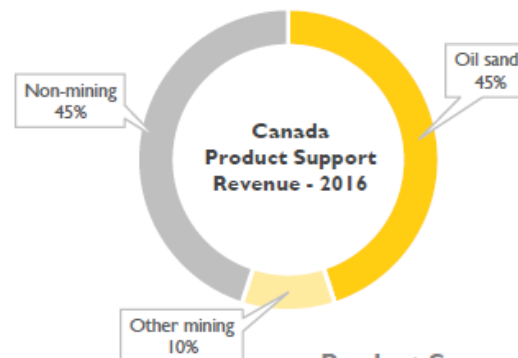
US\$ 1.2-2.4M

Rebuild as % of purchase price

60-70%

60-70%

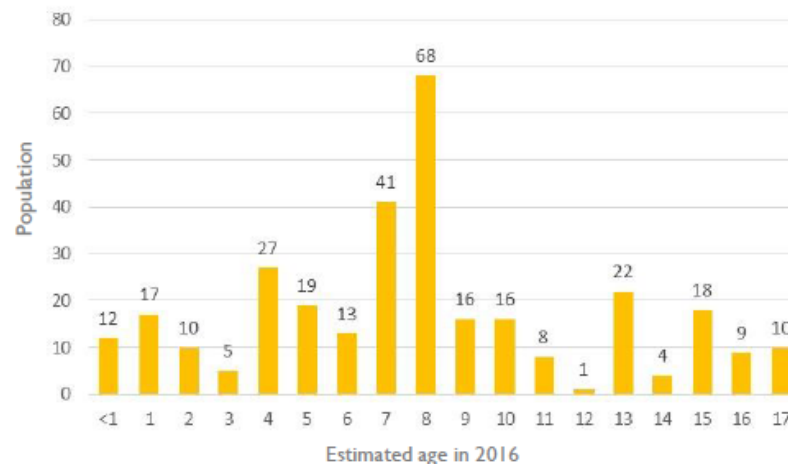
⁽¹⁾ Includes rebuilt machines



Product Support Sweet Spot

Population average age ≥ Expected life span

797 Age Profile



Product Support – South America Mining Opportunities

Mining Truck
797



Large Dozer
D11 & D10



At Dec 2016

Population⁽¹⁾

211

394

Customers

5

25+

1st replacement of large components

~2.5 years/
15,000 hours

~4 years/
18,000 hours

Component exchange during life span

5-6 times

2-3 times

Expected life span before rebuild

~12 years/
80,000 hours

~8 years/
40,000 hours

Average annual product support

~US\$ 1.1M

~US\$ 0.33M

Average age of population⁽¹⁾

~7 years

~6 years

Purchase price

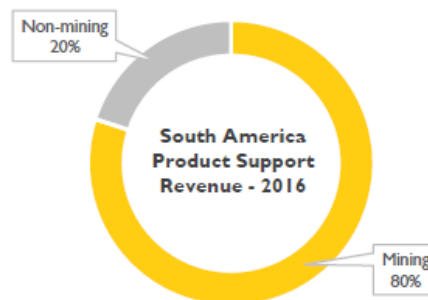
US\$ 5-7M

US\$ 1.2-2.4M

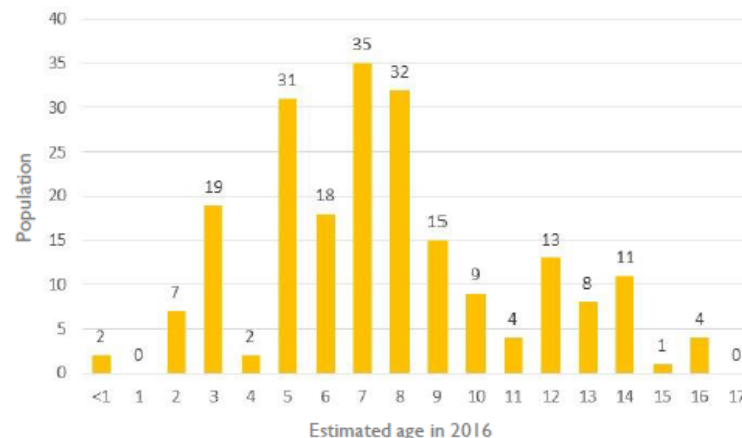
Rebuild as % of purchase price

60-70%

60-70%



797 Age Profile



Competitive Advantages

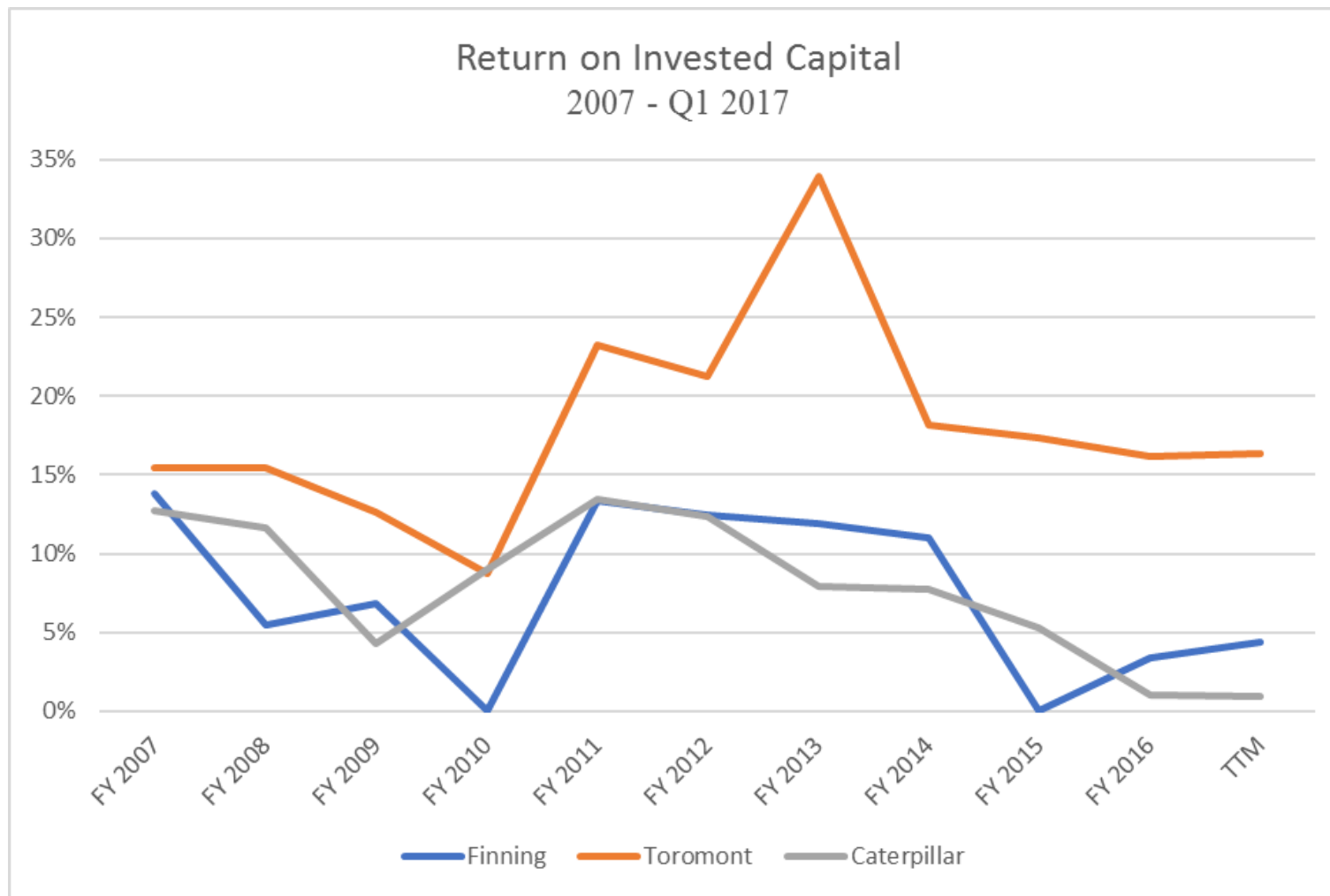
Type	Definition	Source
<u>Supply Advantages:</u>	Cost advantages that allow a company to produce and deliver its products or services more cheaply than its competitors	<ul style="list-style-type: none">• Lower input costs / privileged access to resources• Proprietary technology
<u>Demand Advantages:</u>	Access to customers that rivals cannot match – customer captivity	<ul style="list-style-type: none">• Habit• Switching Costs• Search Costs
<u>Economies of Scale:</u>	Advantage exists if average cost per unit declines as the firm produces more, leaving smaller competitors unable to compete	<ul style="list-style-type: none">• Size - but it is important to remember that pure size alone is not the same thing as economies of scale.

CAT's Competitive Advantage

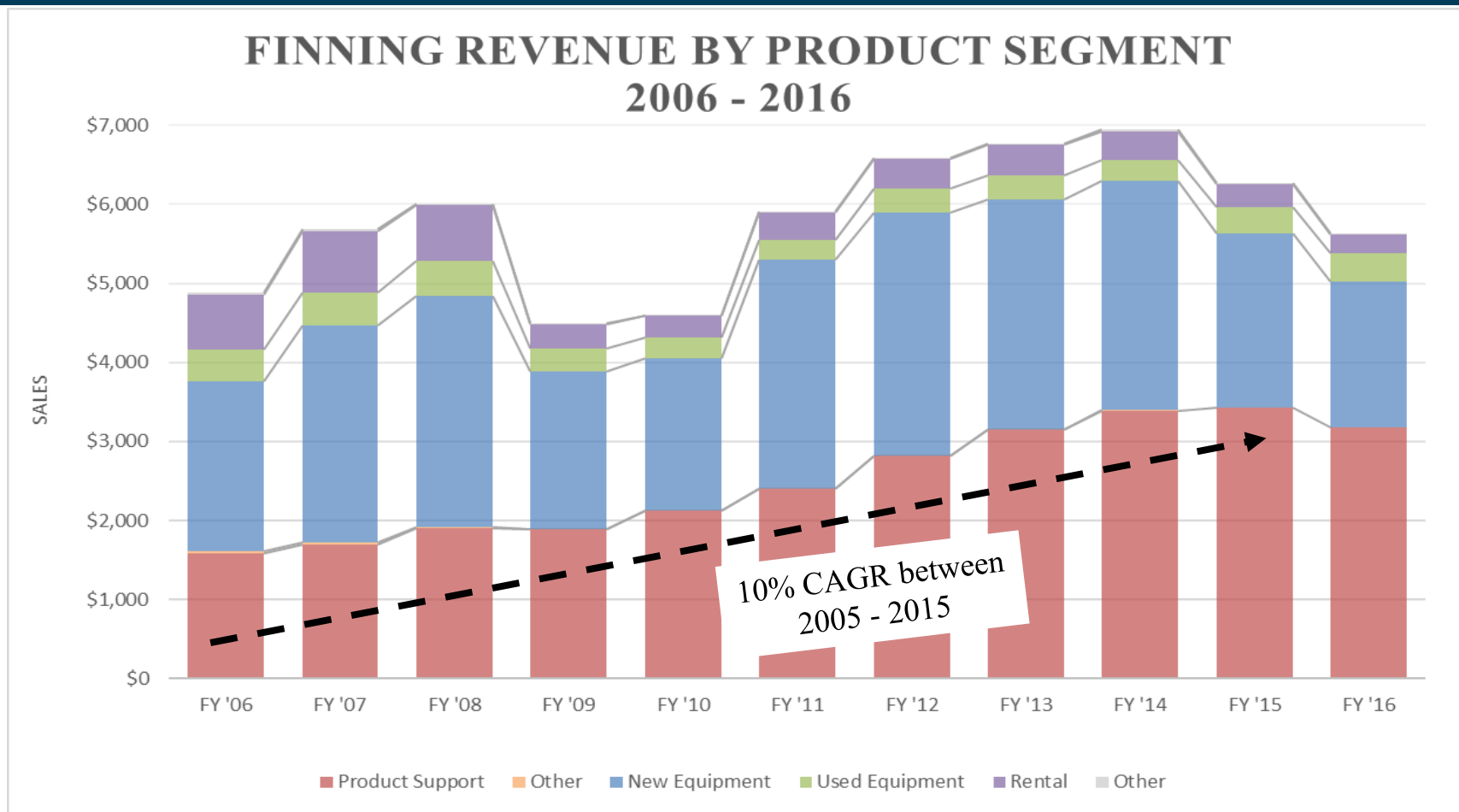
“But the biggest reason for Caterpillar’s success has been our system of distribution and product support and the close customer relationships it fosters. Don’t get me wrong: We think we are better engineers and manufacturers than our competitors. **But we are convinced that our single greatest advantage over our competition was and still is our system of distribution and product support. The backbone of that system is our 186 independent dealers around the world who sell and service our machines and diesel engines.”**

Donald Fites
Former CEO, Caterpillar
Harvard Business Review
March 1996

Competitive Advantage: ROIC



Growth in Aftermarket Parts & Service Revenue

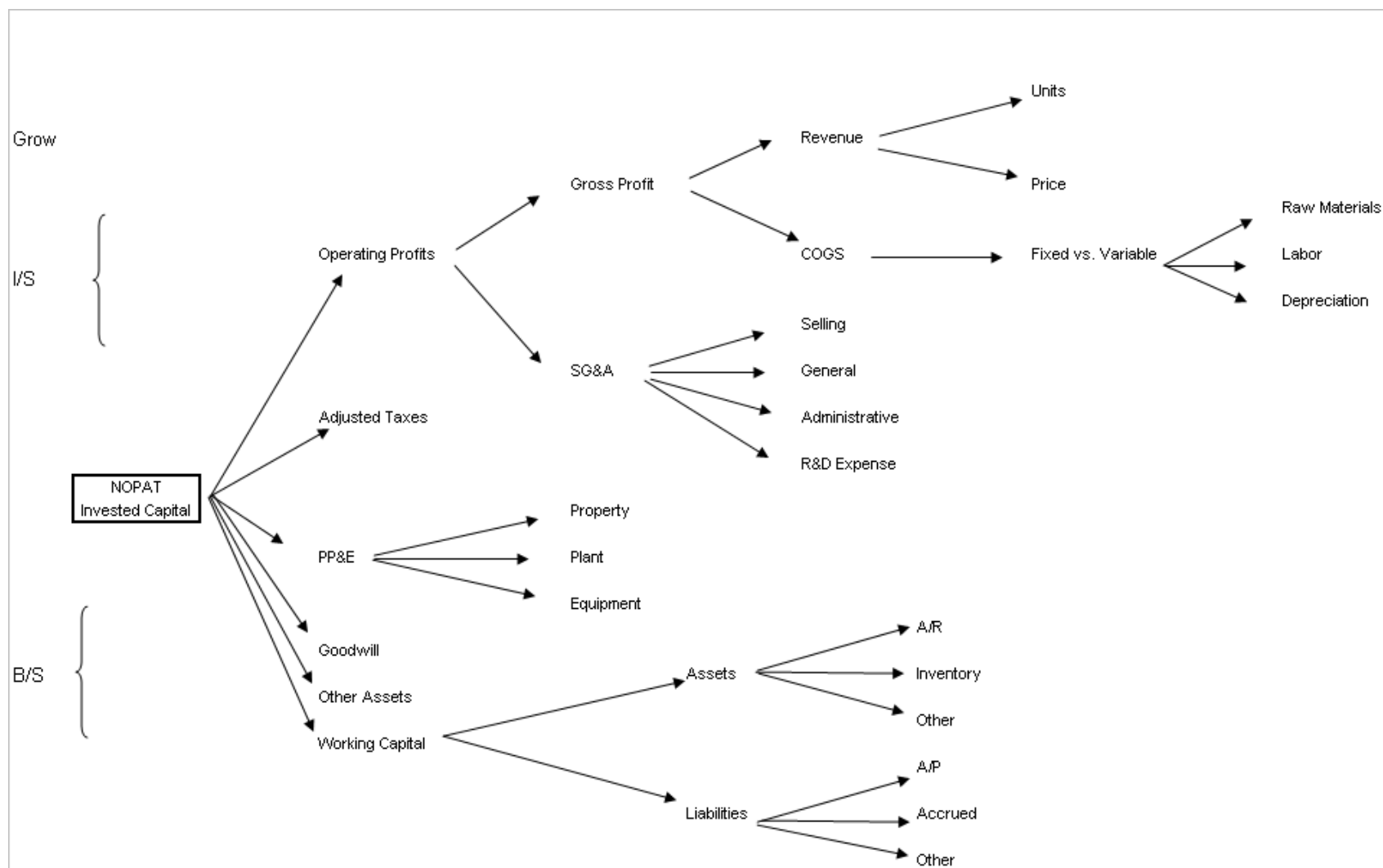


Segment Growth	FY '06	FY '07	FY '08	FY '09	FY '10	FY '11	FY '12	FY '13	FY '14	FY '15	FY '16
New Equipment	13%	27%	7%	(32%)	(3%)	50%	7%	(5%)	(1%)	(24%)	(16%)
Product Support	16%	7%	12%	(1%)	12%	13%	18%	12%	8%	2%	(7%)
Total Revenue	7%	17%	6%	(25%)	2%	29%	12%	3%	2%	(9%)	(10%)

Finning's Competitive Advantage

- The source of Finning's primary barrier to entry / competitive advantage is geographic exclusivity, since CAT must sanction any new dealers.
- Dealers also benefit from some level of customer captivity since they will receive a cut of any Caterpillar part sold in one of their exclusive territories, whether or not they perform the actual service.
- Barriers are also supported by the strength of the Caterpillar Brand.
 - Caterpillar's unmatched geographic network of repair and maintenance locations reinforce Caterpillar's strength, creating a perpetual loop.

Competitive Advantage Indicator: ROIC



Finning's Priorities: ROIC

All priorities are linked directly to **EBIT** or **Invested Capital**



2013 Operational Priorities

Service Excellence

- Drives lowest equipment owning and operating costs
- Maximizes equipment uptime and improves customer loyalty
- Increases service profitability
- Attracts and retains technical talent

Service Excellence

Target Δ 2013-2016

Consolidated EBIT \$

\$40 – 60M↑

Supply Chain

- Competitive advantage as a world-class distributor
- Efficient supply chain drives customer loyalty
- Reduces costs and invested capital
- Improves cash generation

Supply Chain

Target Δ 2013-2016

Working Capital Reduction

Inventory Turns

0.5 – 0.9x ↑

0.1 turn = \$50M inventory ↓

Market Leadership

- Builds machine population and drives future product support
- Aligns with Caterpillar's focus on market share growth
- Expands focus to entire product line

Market Leadership

Target Δ 2013-2016

Revenue Opportunity*

Core Equipment Market Share

2-4% ↑

1% share = \$35M

Parts Market Share

2-4% ↑

1% share = \$45M

Power Systems Revenue (Canada)

10-15% ↑

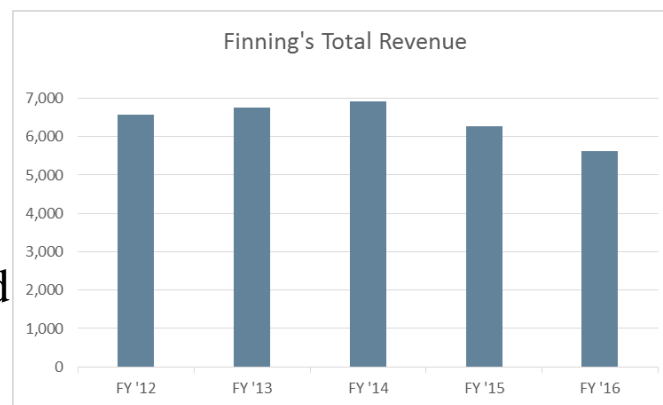
5% growth = \$20M

* Assumes no industry growth

Asset Utilization

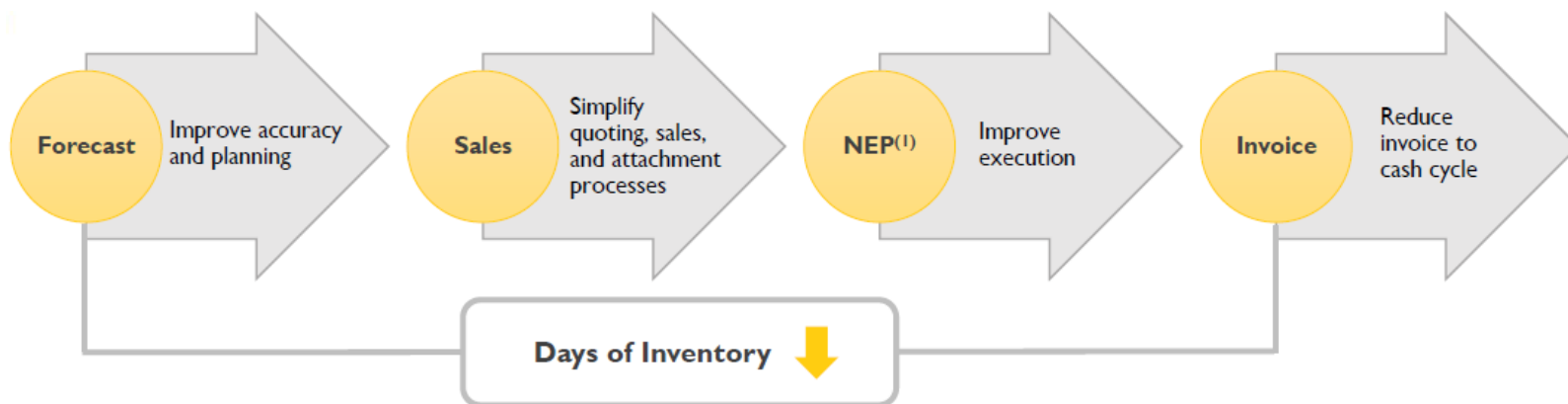
- Optimizes footprint and distribution of activities
- Maximizes return on investments made
- Improves service delivery
- Reduces costs and invested capital

- Improvements have been masked by cyclically weak end markets.

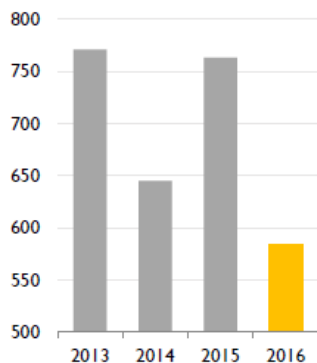


Equipment Supply Chain Transformation

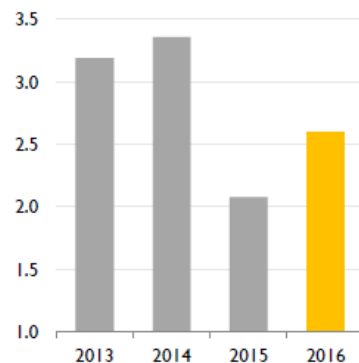
- Machine population drives stable product support business



New Equipment Inventory (\$m)



New Equipment Turns (times)



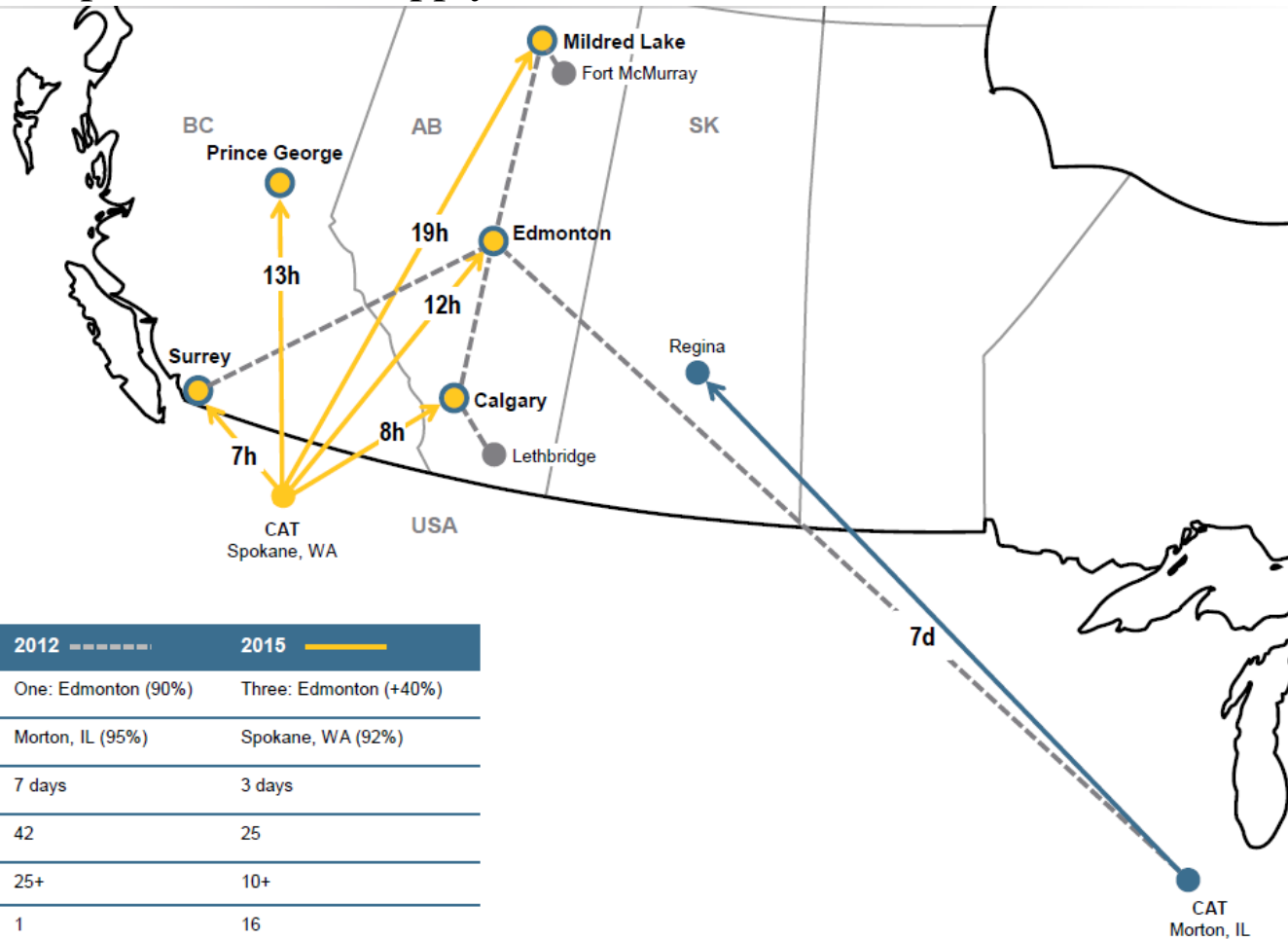
Equipment Turns → Free Cash Flow

↑ 0.1 times = \$30 million

⁽¹⁾ New equipment preparation

Parts Network Transformation

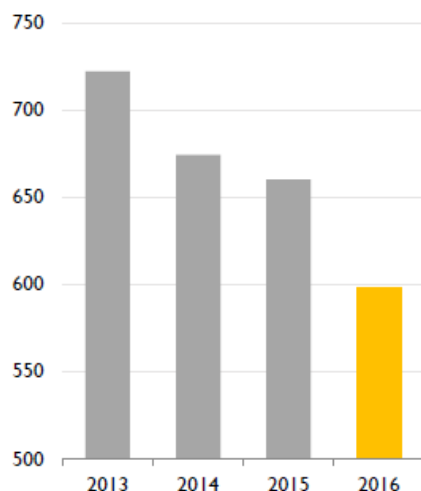
- Simplified and Optimized Parts Supply Chain



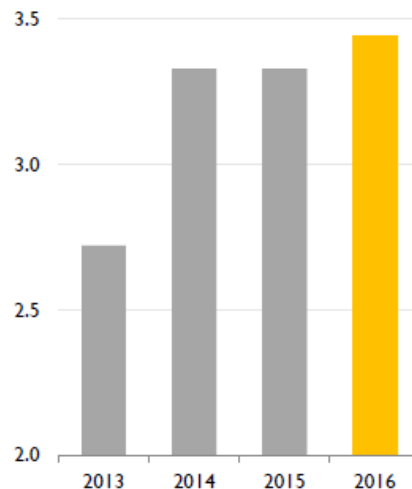
	2012	2015
Centers of Gravity	One: Edmonton (90%)	Three: Edmonton (+40%)
Sourcing	Morton, IL (95%)	Spokane, WA (92%)
Average Transit Time	7 days	3 days
Network Routes	42	25
Network Touches	25+	10+
Branch Direct Shipments	1	16

Parts Supply Chain Improvement

Part Inventory (\$ millions)



Parts Turns (times)



From 2013 to 2016

Parts Turns ↑ 0.7 times

Customer Loyalty ↑ 13 points

Key Improvement Drivers

- Centralized inventory management
- Simplified and optimized network
- Reduced network routes and touches
- Increased direct shipments to customers

Embracing the Trough

Embracing the Trough

Decisive actions to navigate downturn and improve business for long-term

FINNING

Canada

- Workforce ↓ 1,100 people or 20% in 2015
- Accelerated facility optimization
 - 27 closures / consolidations by late 2016
 - Footprint ↓ ~20%
- Operational excellence agenda is transforming the business to deliver improved financial and customer results
- Permanent SG&A cost reductions to achieve sustainable cost model

South America

- Workforce ↓ 1,200 or 16% since mid 2013
- 11 branch closures / consolidations by end of 2016
- Expect further inventory reduction

UK & Ireland

- Workforce ↓ 200 or 9% in 2015
- 2 branch closures
- Continued focus on inventory management and supply chain efficiencies

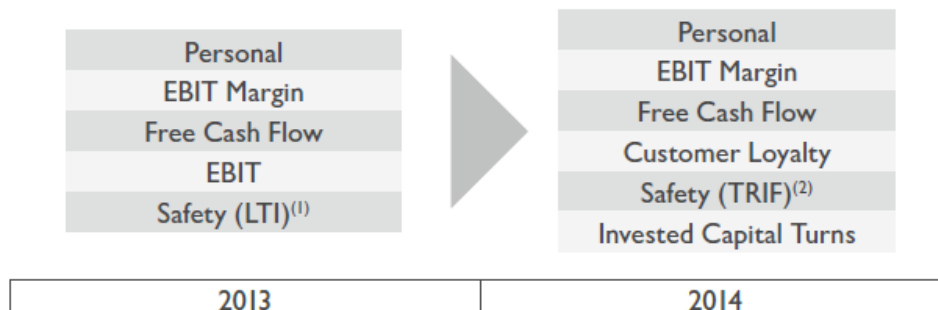
Reduced Cost Structure Canada (2014 – 2016)

Workforce ⁽²⁾	↓	25%
SG&A ⁽³⁾	↓	22%

Driving business transformation by staying the course on operational priorities

Management Incentives - Operational Priorities

Short-Term Incentive Program



(1) LTI is defined as the number of lost time injuries per 200,000 exposure hours worked by employees.

(2) TRIF is defined as the number of total recordable injuries per 200,000 exposure hours worked by employees

Long-Term Incentive Program



Why ROIC?

ROIC is aligned with our operational priorities, which are directly linked to improving profitability and capital efficiency and places a clear focus on factors we can control. Improvements in ROIC correlate well with TSR and provide a comprehensive measure of Finning's performance.

"I think I've been in the top 5% of my age cohort all my life in understanding the power of incentives, and all my life I've underestimated it. And never a year passes but I get some surprise that pushes my limit a little farther."
-Charlie Munger

3-Year Operational Priorities Performance Scorecard

Service Excellence

- Drives lowest equipment owning and operating costs
- Maximizes equipment uptime and improves customer loyalty
- Increases service profitability
- Attracts and retains technical talent

Supply Chain

- Competitive advantage as a world-class distributor
- Efficient supply chain drives customer loyalty
- Reduces costs and invested capital
- Improves cash generation

Market Leadership

- Builds machine population / drives future product support
- Aligns with Caterpillar's focus on market share growth
- Expands focus to entire product life

Asset Utilization

- Optimizes footprint and distribution of activities
- Maximizes return on investments made
- Improves service delivery
- Reduces costs and invested capital

2013 Commitments

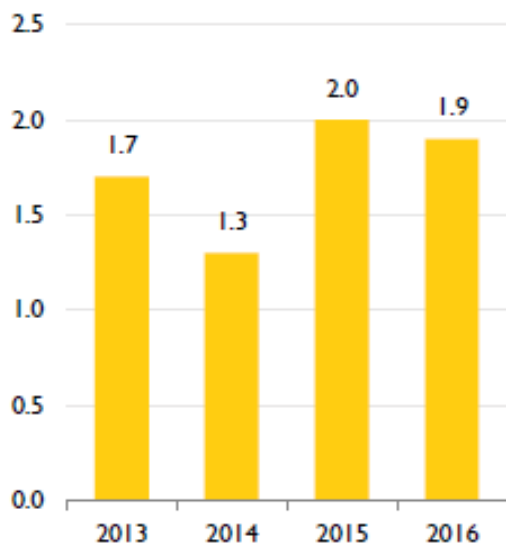
Assuming no industry change

2016 Outcome

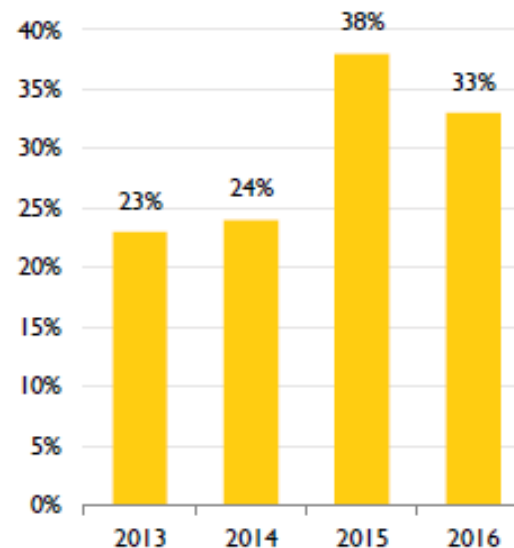


Capital / Free Cash Flow

Net Debt to Adjusted EBITDA⁽¹⁾



Dividend as % of FCF



“We'll make capital allocation decisions when (we) start to see the Canadian free cash flow generation, which I expect to be in mid-year. I'm extremely confident... that by the end of 2015 we'll look back, and Finning will have allocated at least a portion of its excess capital to repurchasing shares, and particularly if the share price stays at this level.”

Scott Thomson, CEO
Q4 2014 Conference Call (2/19/2015)

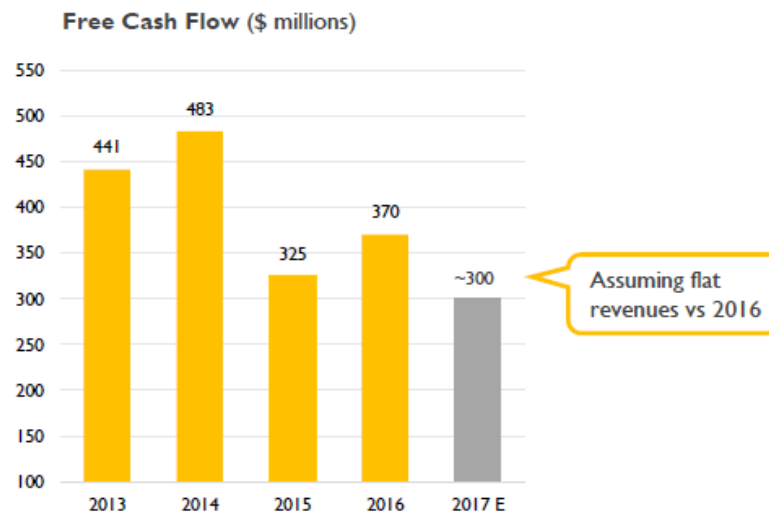
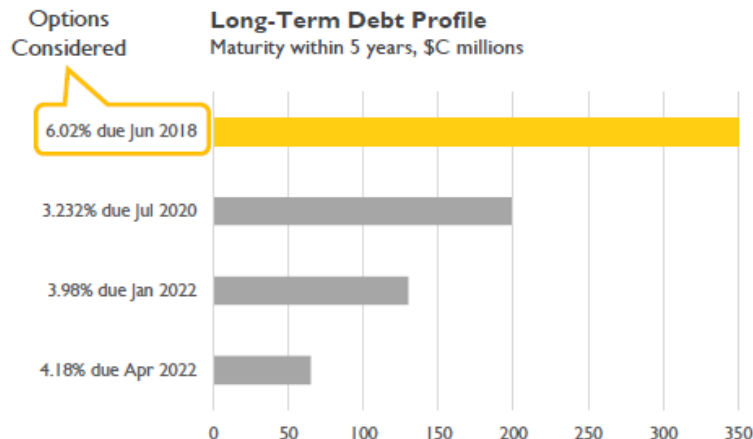
Capital / Free Cash Flow

Capital Allocation Priorities

- Dividends
- Debt reduction
- Targeted investment in technology
- Share repurchases
- Disciplined complementary acquisitions

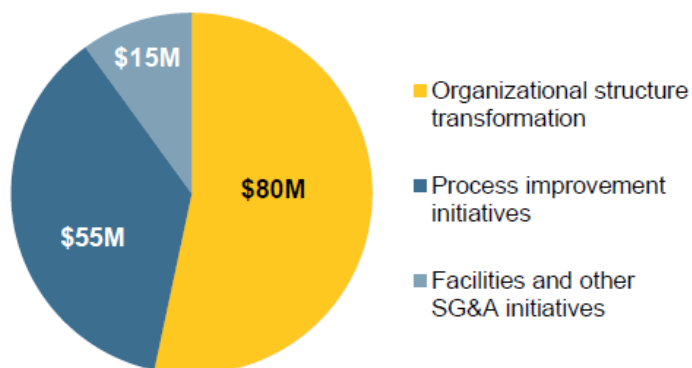
Positive Free Cash Flow

- Higher EBITDA driven by reduced cost structure and operating efficiencies
- Working capital improvements
- Capital expenditures up ~\$40 million vs 2016 mostly due to ERP implementation in South America
- Rental investment flexible to market demand; lower disposals vs 2016

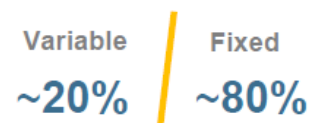


Canada's Sustainable Cost Model

\$150M SG&A Cost Savings
Non-volume related (2014-2016)



Canada's SG&A Costs
2015




Permanently reducing fixed SG&A costs

- Optimized organizational structure
- Changing the way we do business through process improvements
 - Supply chain - structurally improved (e.g. reduced freight costs)
 - Service excellence - improved profitability (e.g. increased labour recovery)
 - Procurement
 - Service vehicle fleet
- Reduced facility footprint

Significant Infrastructure Opportunities


Announced Government Infrastructure Spending

C\$ billions		US\$ billions		£ billions / € billions	
British Columbia	24.5 (2017-2019)	Chile	61 (2016-2020)	UK	300 (2017-2021)
Alberta	32.8 (2017-2020)	Argentina	48 (2016-2020)	Ireland	38 (2017-2021)
Saskatchewan	1.6 (2017-2018)	Bolivia	19 (2016-2020)		
Federal	~141 (2019-2027)				




Selected Projects

- George Massey Tunnel (BC)
- Southwest Calgary Ring Road (AB)
- Regina Bypass (SK)



Selected Projects

- Subway Line 7 (Chile)
- Railroad Belgrano Cargas (Argentina)
- Highways and roads (Bolivia)



Selected Projects

- Hinkley Point Nuclear Plant (UK)
- High Speed Rail 2 (UK)
- Road Investment Strategy (UK)
- Dublin Metro Link (Ireland)

Digital Strategy

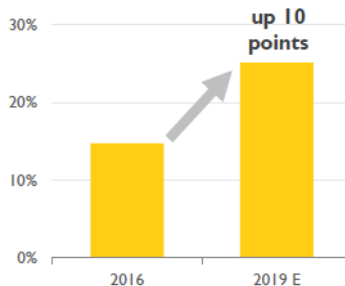
E-COMMERCE - Parts⁽¹⁾

Customer Parts Share⁽²⁾ ↑ 11 points
Transaction Cost ↓

⁽¹⁾ Caterpillar study covering 11,700 e-commerce and integrated procurement customers between 2010-2014

⁽²⁾ Parts purchases from Finning as a percentage of total parts opportunity

Online Parts Revenue Projections % of total



SITECH

Technology to maximize machine productivity on job sites

Revenue Growth
CAGR (2013 – 2016)

↑ ~15 %

Predictive analytics drive improved maintenance and increased productivity

Insights drive improved equipment performance, market visibility, and lower costs

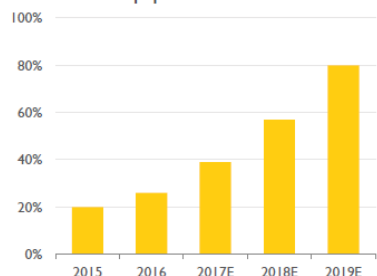


Drive Parts Share⁽¹⁾ ↑ ~10 points⁽²⁾ | Enable Performance Solutions

⁽¹⁾ Parts purchases from Finning as a percentage of total parts opportunity

⁽²⁾ Caterpillar study covering >37,000 connected customers vs 174,000 non-connected between 2010 and 2013

Connected Assets Projections % of total population⁽¹⁾



⁽¹⁾ Assumes constant numbers of active equipment population

Key Data & Services

Customer Benefits

Hours and location

- Tracking by job site and fleet; security
- Invoice automation

Utilization, fuel and production

- Idle time and fuel consumption
- Asset optimization and fleet production

Machine health

- Preventative maintenance
- Lower operating costs

Training and site development

- Operator training
- Haul road analysis

Data analytics

- Optimization recommendations
- Site & management performance reporting

Fatigue management

- Improved safety performance

Key Performance Indicators

For years ended December 31	2016	2015	2014	2013	2012
Return on Invested Capital (ROIC) ⁽¹⁾⁽²⁾ (%)					
Consolidated	5.6%	(3.0)%	15.3%	15.7%	16.5%
Canada	5.3%	5.5 %	17.1%	15.9%	15.7%
South America	13.3%	(12.8)%	14.6%	17.6%	19.7%
UK & Ireland	(4.5)%	(1.4)%	16.3%	16.4%	16.3%
EBIT ⁽²⁾ (\$ millions)					
Consolidated	165	(105)	504	521	489
Canada	87	98	284	263	231
South America	137	(174)	196	249	239
UK & Ireland	(12)	(5)	50	43	45
EBIT Margin (%) ⁽²⁾⁽³⁾					
Consolidated	2.9%	(1.7)%	7.3%	7.7%	7.4%
Canada	3.1%	3.1%	7.8%	7.8%	7.1%
South America	7.4%	(8.4)%	8.8%	9.9%	9.9%
UK & Ireland	(1.1)%	(0.5)%	4.8%	4.9%	5.0%
Invested Capital ⁽¹⁾ (\$ millions)					
Consolidated	2,797	3,240	3,106	3,138	3,131
Canada	1,595	1,760	1,475	1,488	1,589
South America	996	1,122	1,348	1,391	1,298
UK & Ireland	216	321	284	265	260
Invested Capital Turnover ⁽¹⁾⁽³⁾ (times)					
Consolidated	1.90x	1.78x	2.10x	2.04x	2.22x
Canada	1.70x	1.74x	2.19x	2.03x	2.22x
South America	1.80x	1.52x	1.66x	1.78x	1.98x
UK & Ireland	3.54x	2.93x	3.43x	3.37x	3.25x
Inventory (\$ millions)	1,601	1,800	1,661	1,756	1,930
Inventory Turns ⁽¹⁾⁽³⁾ (times)	2.49x	2.38x	2.81x	2.74x	2.43x
Working Capital to Sales Ratio ⁽¹⁾⁽³⁾	30.4%	32.2%	26.1%	26.5%	24.5%
Free Cash Flow (\$ millions)	370	325	483	441	(37)
Net Debt to Invested Capital Ratio ⁽¹⁾	32.0%	36.7%	31.4%	40.8%	50.0%
EBITDA ⁽²⁾ (\$ millions)	357	126	720	737	701
Net Debt to EBITDA Ratio ⁽¹⁾⁽²⁾	2.5	9.5	1.4	1.7	2.2

Risks To Our Thesis

- Commodity prices (copper, oil, natural gas, coal and gold, among others) could fall further or remain at current levels for an extended period leading major customers to delay large projects and defer capital expenditures.
- Continued foreign currency fluctuations could impact Finning's earnings.
- Unforeseen issues at Caterpillar, Finning's sole supplier, could have adverse effects on its business.
- Chinese OEMs continue attempts to enter international markets. Successful penetration could drive down profitability.

Disclosure: Ownership Information

<u>Disclosures</u>	Finning International (TSX:FTT)
Robert Robotti and/or members of his household has a financial interest in the following securities	Yes
Robotti & Company or its affiliates beneficially own common equity of the following securities	Yes
Robotti & Company or its affiliates beneficially own 1% or more of any class of common equity of the following securities	No
Robert Robotti serves as a Director or Officer or Advisory Board Member of the following securities	No

Disclaimer: Analyst Compensation: While this report is not a research report of any broker or dealer, compensation of analysts of the Firm is based on: (1) the analyst's productivity, including the quality of the analyst's research and the analyst's contribution to the growth and development of our overall research effort; (2) ratings and direct feedback from our investing clients, our sales force and from independent rating services. The Firm's management is responsible for establishing these compensation guidelines and for reviewing and approving compensation. Analyst contribution (if any) to the investment banking business of any affiliate of the Firm is not a factor in determining his/her compensation for either entity and compensation is not, directly or indirectly, related to the specific recommendations or views expressed in the report.

Analyst Certification: The author certifies that the views expressed in this financial model accurately reflect his personal views about the subject securities or issuers and that no part of his or her compensation was, is, or will be directly or indirectly related to the specific recommendations or views contained in this presentation. The author, from time to time, may have long or short positions in, and buy or sell, the securities, or derivatives (including options) thereof, of companies mentioned herein. This is not a complete analysis of every material fact regarding any company, industry or security.

Disclaimer

Robotti & Company Advisors, LLC (the “Firm”) is not providing investment advice through this material. This presentation is provided for informational purpose only as an illustration of the firm’s investment philosophy and shall not be considered investment advice or a recommendation or solicitation to buy or sell any securities discussed herein, and does not contain enough information to be considered a recommendation or a research report.

As of the date of this presentation the firm continues to own the securities discussed herein. These opinions are not intended to be a forecast of future events, a guarantee of future results, or investment advice. Past performance is not indicative of future results, and no representation or warranty, express or implied, is made regarding future performance.

Robotti & Company Advisors, LLC or its affiliates may engage in securities transactions that are inconsistent with this communication and may have long or short positions in such securities. The information and any opinions contained herein are as of the date of this material, and the firm does not undertake any obligation to update them.

This material does not take into account individual client circumstances, objectives, or needs and is not intended as a recommendation to any person who is not a client of the firm. Securities, financial instruments, products or strategies mentioned in this material may not be suitable for all investors. The Firm does not provide tax advice. Investors should seek tax advice based on their particular circumstances from an independent tax advisor.

In reaching a determination as to the appropriateness of any proposed transaction or strategy, clients should undertake a thorough independent review of the legal, regulatory, credit, accounting and economic consequences of such transaction in relation to their particular circumstances and make their own independent decisions. By virtue of this publication, neither the Firm nor any of its employees shall be responsible for any investment decision.

This confidential presentation contains information that has been compiled, by the Firm, from sources believed to be reliable; however, there can be no guarantee as to the accuracy or completeness of such information. It also contains statements, estimates and projections made by various third party companies with respect to their historical and projected performance. There can be no assurance that such statements, estimates and projections will be realized and actual results may vary materially from those indicated. Further, in any case, the Firm does not represent nor is affiliated with any of the third party companies and other entities named and makes no representations as to the reasonableness of such assumptions or the accuracy or completeness of the information contained herein. These materials are for the confidential use of only those persons to whom it is transmitted.

This report may discuss numerous securities, some of which may not be qualified for sale in certain states and may therefore not be offered to investors in such states. This document should not be construed as providing investment services. Investing in non-U.S. securities including ADRs involves significant risks such as fluctuation of exchange rates that may have adverse effects on the value or price of income derived from the security. Securities of some foreign companies may be less liquid and prices more volatile than securities of U.S. companies. Securities of non-U.S. issuers may not be registered with or subject to Securities and Exchange Commission reporting requirements; therefore, information regarding such issuers may be limited.

July 8-9, 2015



Bob Robotti
CEO & Chief Investment Officer

6 East 43rd Street
23rd Floor
New York, NY 10017
Tel: (212) 986-4800
Fax: (212) 986-0816
www.robotti.com

What Makes us Different

Analytical Edge

Within the context of a longer-term perspective and 30+ years of experience, we have the ability to develop a different conclusion than that of the market.

Informational Edge

Our network of industry relationships, focus on deep primary research, and experience serving on company boards, provides us with more pieces for building our information mosaic.

Leads Us To

Behavioral Edge

We take a longer-term view and have the ability to tolerate market swings.

Our behavioral edge comes from our ability to tolerate market volatility. As a result, our investment process concentrates on understanding the long-term normalized earning power of a business well before the “investing herd” gains interest.

Investment Thesis

- Subsea 7 is a global leader in a niche industry with a sustainable competitive advantage.
- The market underestimates the barriers to entry shared by the 3 Tier-1 competitors.
- The dislocation of oil prices should accelerate consolidation opportunities and further differentiate the Tier-1 competitors.
- Backlog dynamics are in place to create a runway for significant growth.
- Shares of the business today trade at a single-digit multiple of current and normalized earnings.

Subsea 7 is our highest conviction investment idea. We believe that shares will more than double within 2 – 3 years.

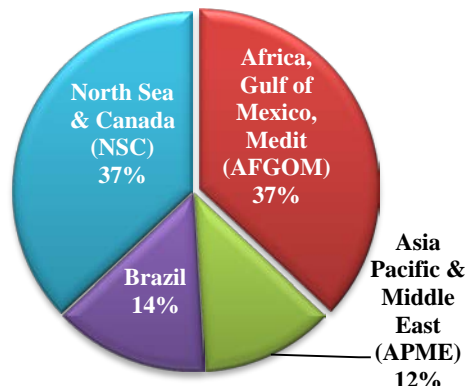
Business Summary

- Subsea 7 is a global leader in seabed-to-surface engineering & construction services to the offshore industry.
- The company provides integrated services for projects of all sizes, complexity and water depth.

Market Capitalization	
Price	\$9.71
Adj Dil Shrs:	348.4
Market Cap	3,382
LT Debt	662
Minority Interest	(26)
Cash	373
Enterprise Value	3,644

Trading Summary	
52 Week High	\$15.09
52 Week Low	\$8.00
Net Debt	(14.5)
Net Debt / EBITDA	(0.0x)
Price / Book Value	0.6x
Price / Tangible BV	0.7x
Avg Daily Volume	1,466,250
Listing Exchange	Oslo Bourse

Revenue by Geographic Segment



(in thousands USD)

Valuation Summary	Consensus Est.				
	FY2012	FY2013	FY2014	2015E	2016E
Revenue	6,296.6	6,297.1	6,869.9	5,130.2	4,454.1
<i>growth</i>	15.0%	0.0%	9.1%	(25.3%)	(13.2%)
<i>ev/sales</i>	0.6x	0.6x	0.5x	0.7x	0.8x
Adj. EBITDA	1,139.0	981.0	1,439.0	950.9	774.5
<i>margin</i>	18.1%	15.6%	20.9%	18.5%	17.4%
<i>ev/EBITDA</i>	3.2x	3.7x	2.5x	3.8x	4.7x
Adj. Op. Income	808.2	573.4	929.5	522.4	334.3
<i>margin</i>	12.8%	9.1%	13.5%	10.2%	7.5%
<i>ev/EBIT</i>	4.5x	6.4x	3.9x	7.0x	10.9x
Adj. Diluted EPS	\$2.18	\$1.00	\$2.32	\$1.12	\$0.69
<i>p / e</i>	4.4x	9.7x	4.2x	8.7x	14.2x

Company reports diluted shares assuming conversion of all convertible bonds regardless of current share price. Diluted shares assumes that no convertible bonds are converted since the share price on 6/29/15 was significantly below conversion prices.

Core Business Segments

SURF (77%)

Engineering, construction, installation and procurement of subsea umbilicals, risers and flowlines

Life-of-Field (10%)

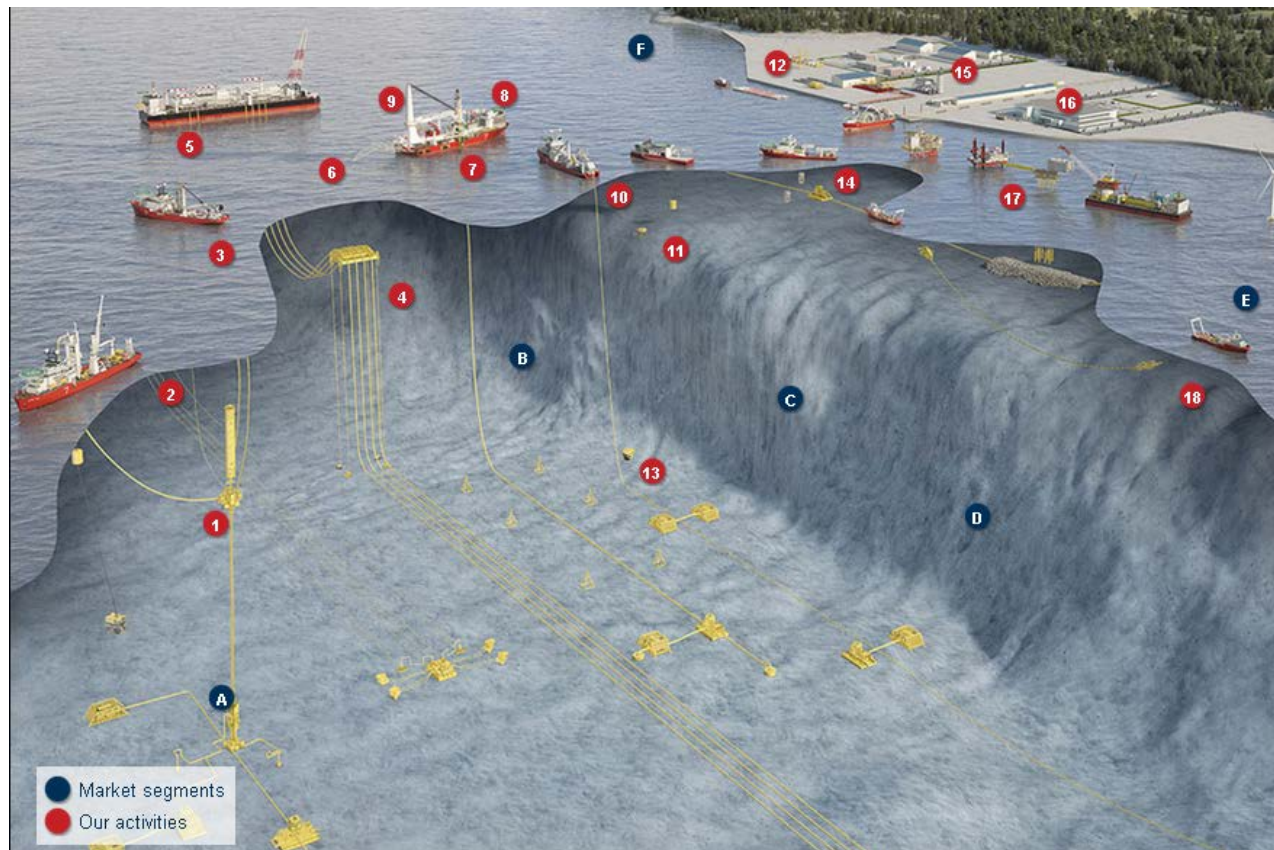
Services over the life of a field's production, including inspection, repair and maintenance

Conventional / Hook-up (10%)

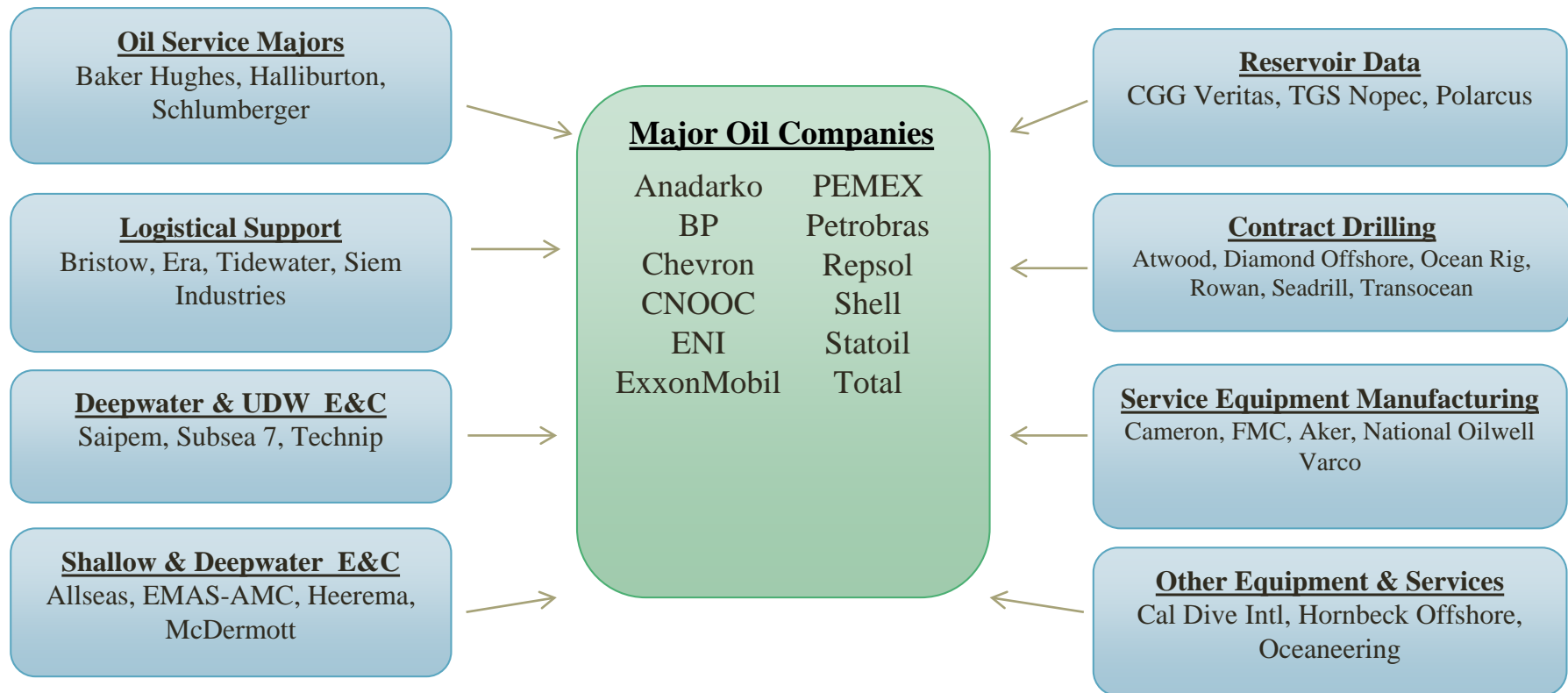
Fabrication and installation of fixed platforms and associated pipelines. Addition of modules on new platforms and refurbishment of topsides of an existing platform or FPSO.

ROV (3%)

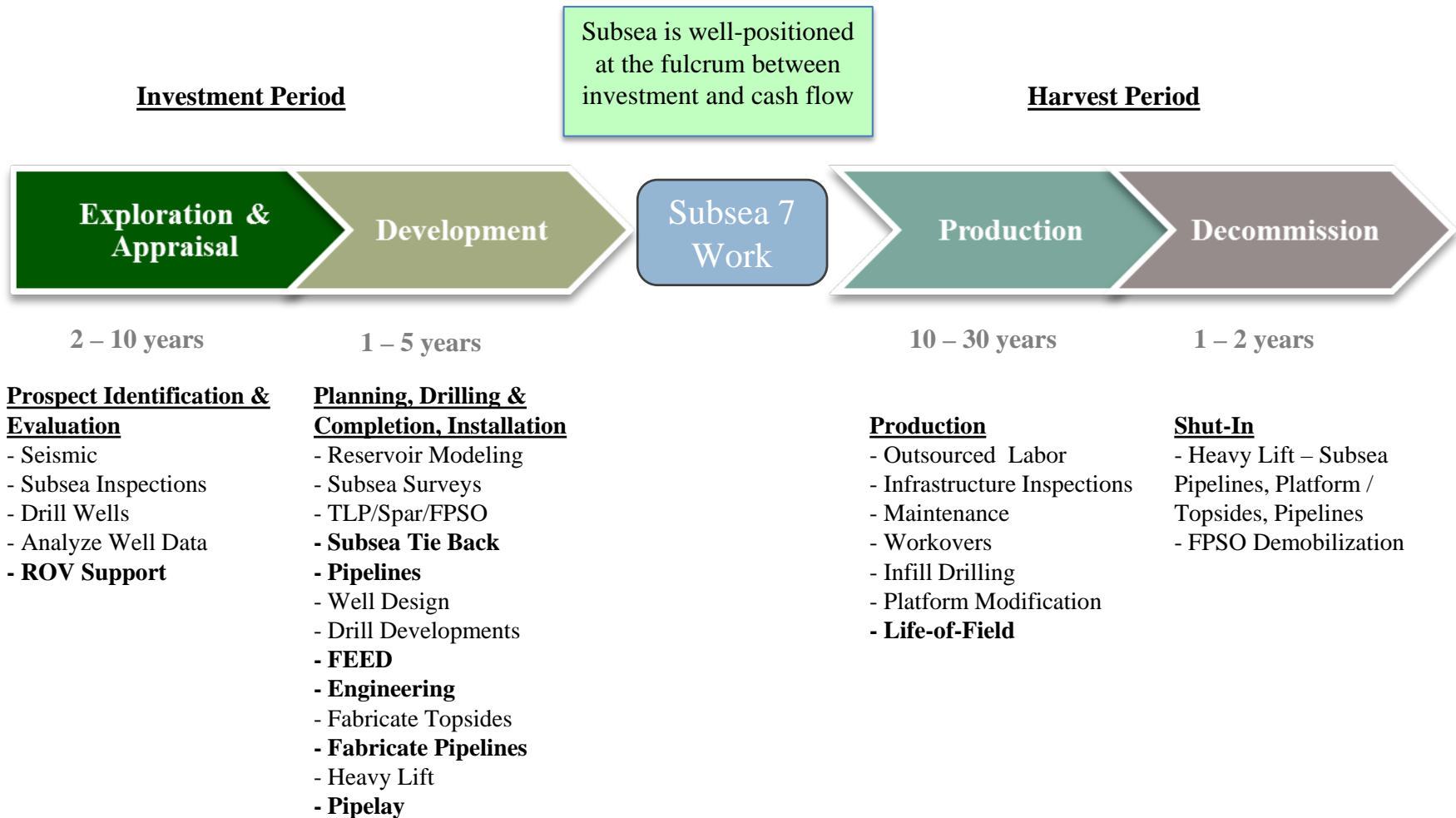
Operation of Remotely Operated Vehicles (ROVs).



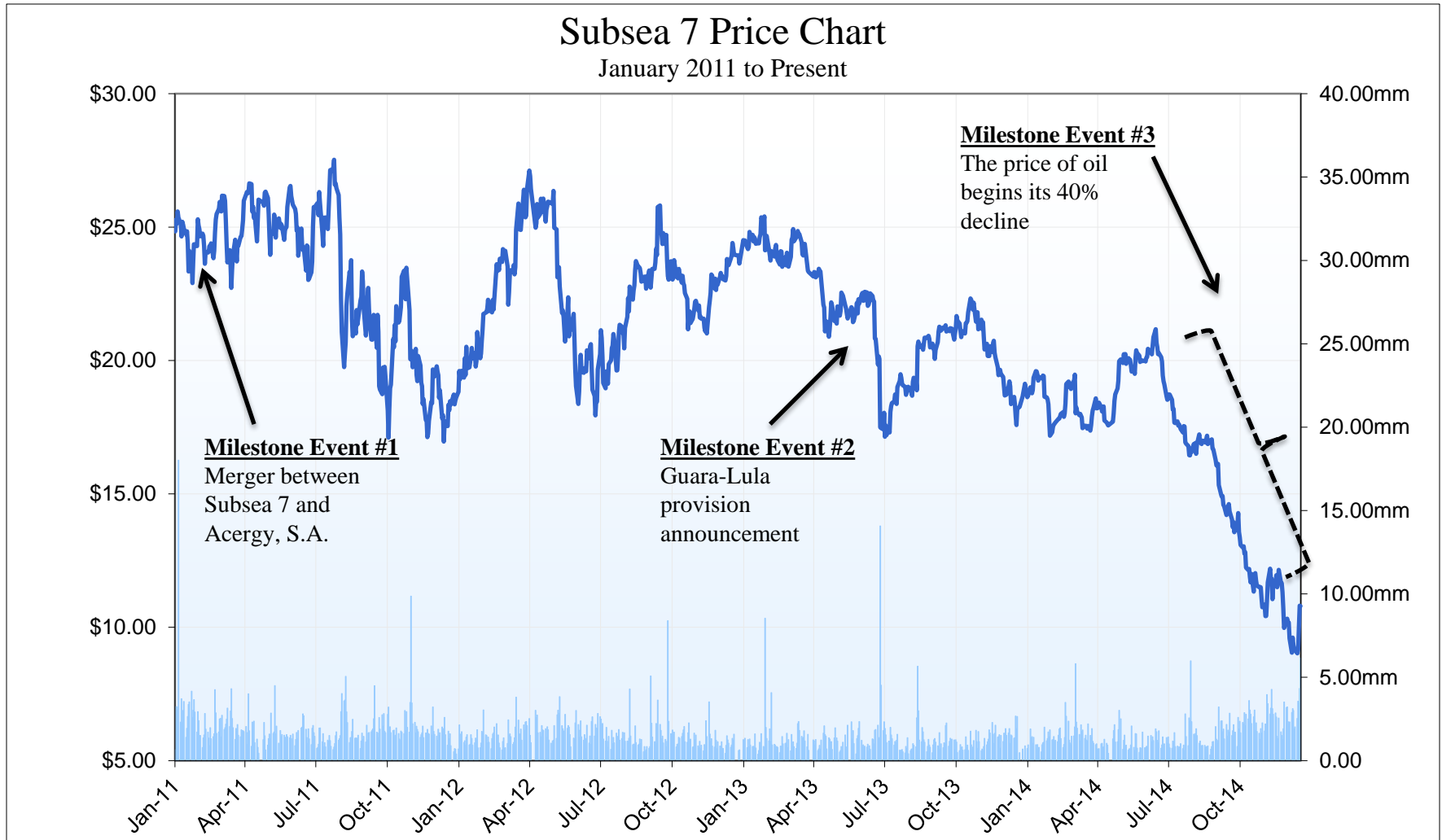
Industry Map



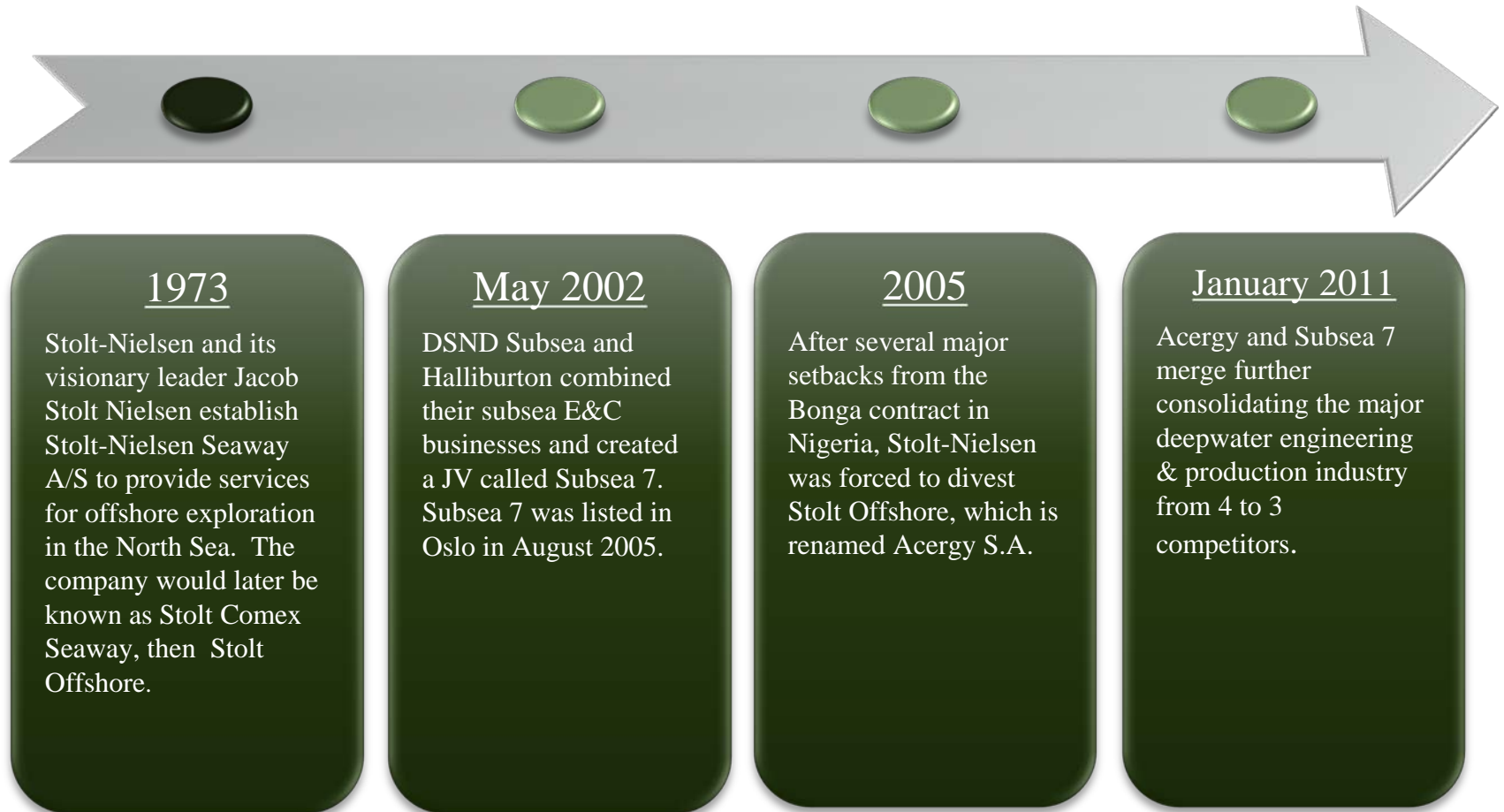
Favorable Position in the Deepwater Lifecycle



Confluence of Events



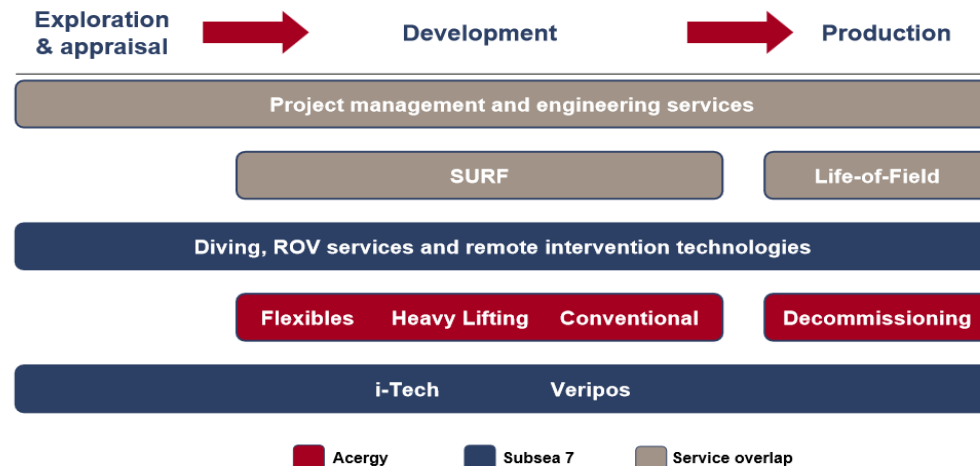
Merger of Subsea 7 and Acergy



Merger Rationale

- Geographic strengths were complementary – especially important for local content offerings in key markets.
- Service offerings and technologies were complementary.
- Kristian Siem – whose interests are aligned with shareholders through large ownership of shares – is named Chairman of Subsea 7.

Complementary fit to provide full spectrum of subsea services

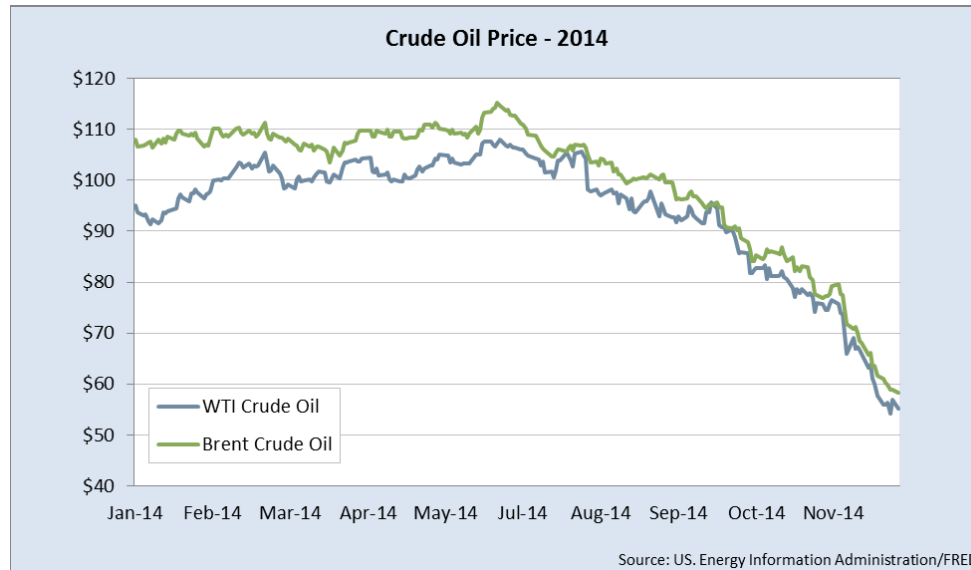


slide 8



Current Energy Environment

- Oil prices collapsed in the second half of 2014, falling > 45% in less than six months.
- Tumbling oil prices have caused oil companies to reassess and begin to cut near-term capex budgets.
- Recent entrants are left with an inventory of idle assets.
 - Potentially reduces the capital investment requirements of the business leading to increased return on assets over the long-term.



The Market View

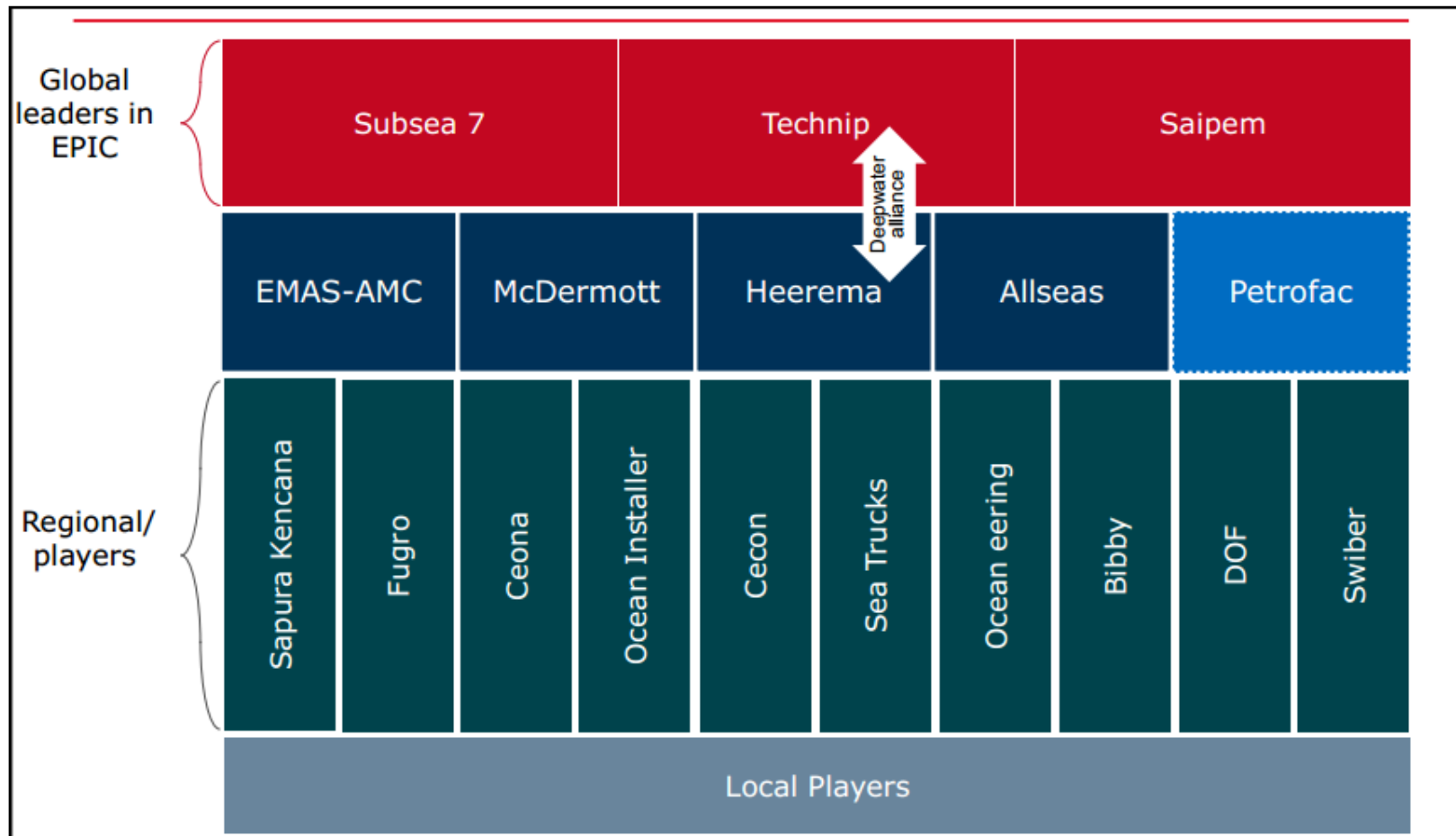
- Beginning in early 2014, major international oil & gas companies embarked on a capex review due to disappointment with investment returns. Since then, the decline of oil prices has further clouded the outlook for major oil project final investment decisions (FID). Deep water projects are considered to be the most susceptible to delay in the current low price environment.
- Ultra-deepwater investments by Tier-2 and Tier-3 competitors will lead to additional pricing pressure and lower profitability across the industry.
- Revenue from important regions such as Brazil are at risk. Petrobras is everyone's, including Subsea 7's, main customer in Brazil. Financial disappointments at Petrobras have resulted in a debt rating of just one level above junk and corruption probes against senior high ranking executives have further complicated matters.

Key Investment Factors / Variant View

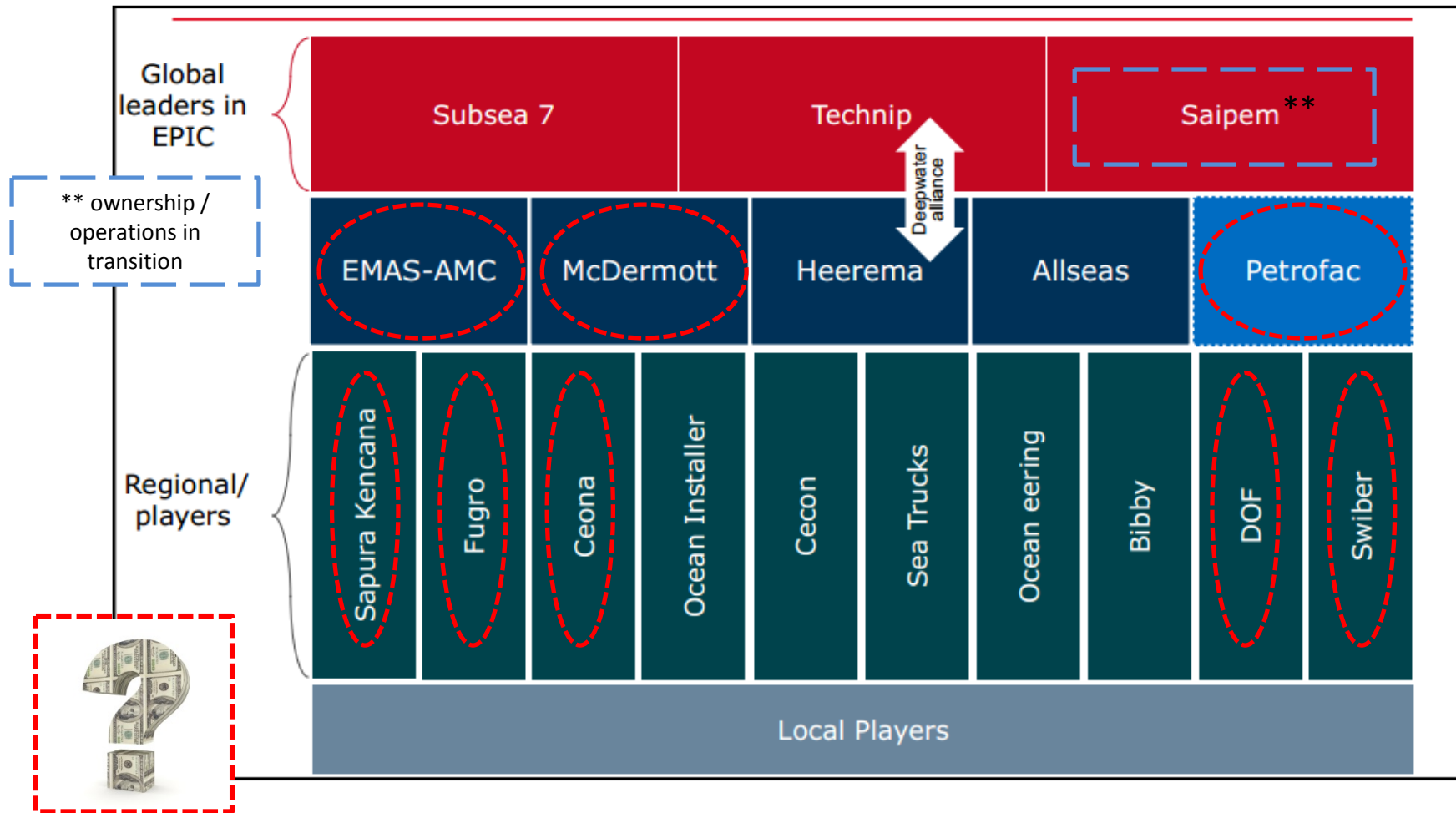
- Industry headwinds from the global financial crisis have resulted in modest industry revenue growth and margin compression in recent years, and have led to an oligopolistic market with barriers to entry that continue to increase over time.
- Shifting contract mix in Brazil will mitigate current macro issues.
 - Oil revenues are vital to Brazil and its economy. As companies increasingly refrain from doing business in Brazil, Petrobras and the Brazilian government will be forced to be more accommodating – participation of majors.
- Current energy prices are below the long-term sustainable price needed, and will likely result in increases sanctioning as the impact of production decline manifests.
- Subsea 7's backlog growth is just the tip of the iceberg. The inventory of deep and ultra-deep water discoveries not yet sanctioned continues to grow creating the potential for significant revenue growth and increased returns on capital.

Subsea 7 is a leading global offshore oil & gas services company with a durable competitive advantage. While near-term challenges persist, long-term dynamics are in place for Subsea 7 to enjoy a long runway of significant growth.

Current Industry Landscape – Core Surf Businesses

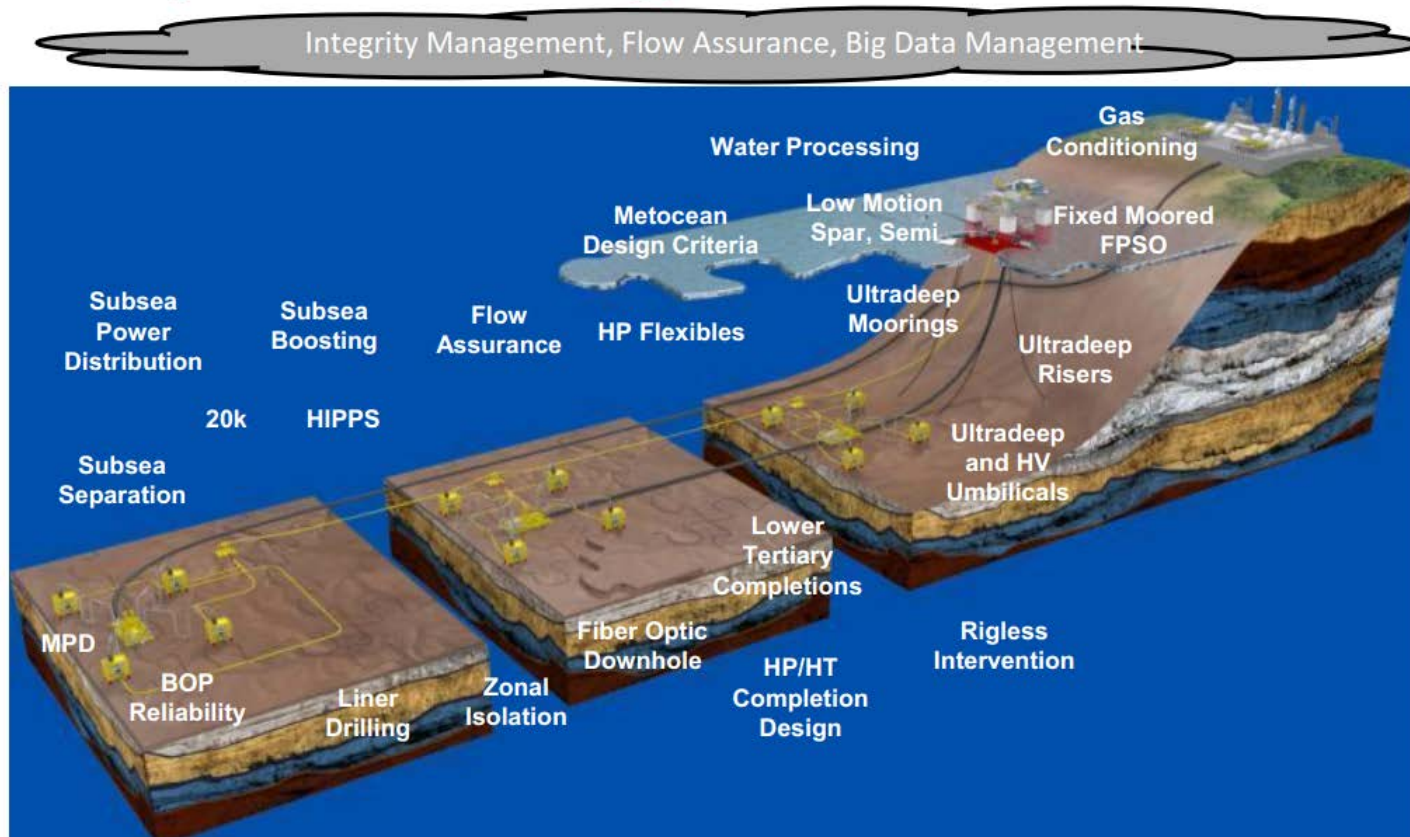


Tier-1 Barriers Continue to Increase – Assets come available



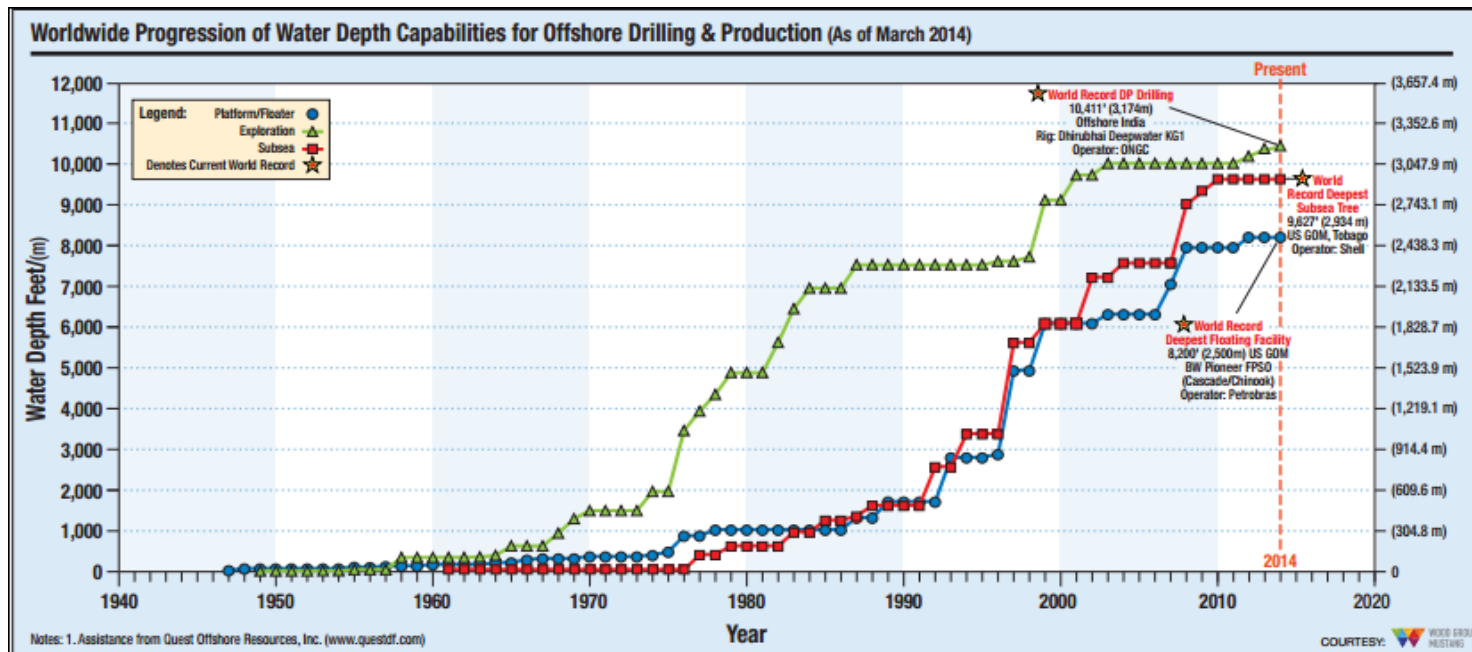
Increasing Complexity

Deepwater Technology Needs



Increasing Complexity

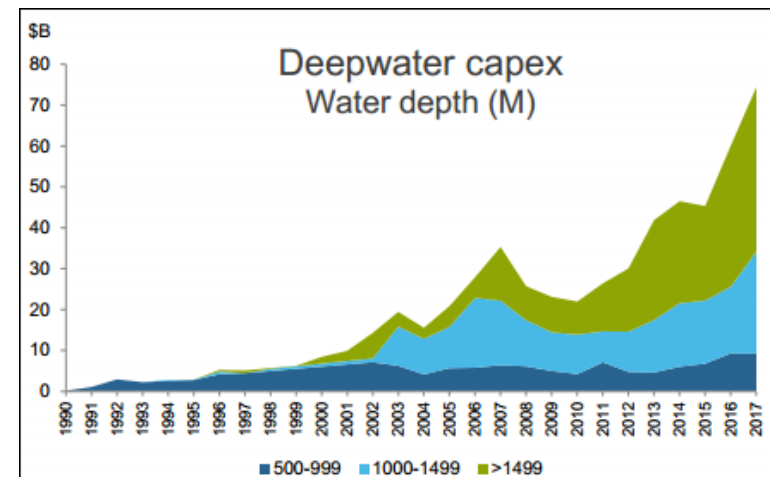
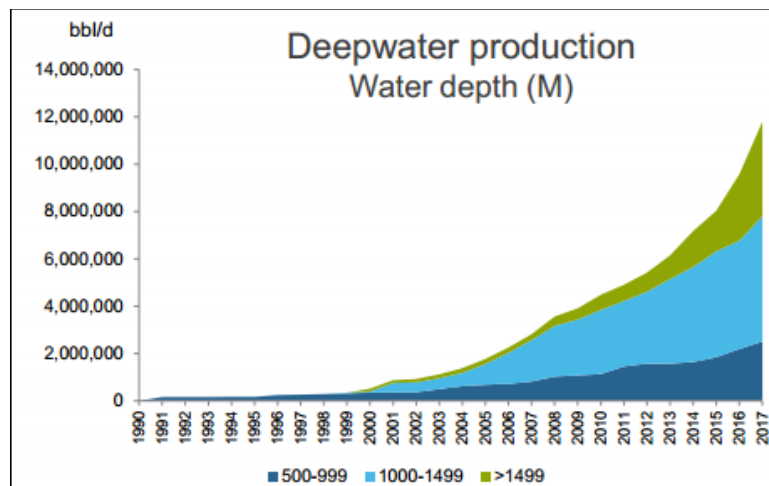
- Declining production profiles of major international oil companies drive demand in the services industry, frequently requiring Tier-1 competitors to bid in consortium.
- Deepwater represents the greatest opportunity to replenish major oil & gas reserves. It also presents greater technical challenges and increases the overall scale and scope of projects. This bodes well for the likelihood of higher exploration & production capital expenditure.
- Technology advances such as subsea separation and compression is increasing the addressable market.



Increasing Complexity



Deepwater Wells Drilled
Greater Distances
from Shore



Geographic Summary

Africa

- Awarded a field development contract in the Ivory Coast by CNR International.
- Local content continues to be a competitive advantage.
- *Potential* market awards over the next 12 months include: West Nile Delta, Bonga Southwest, Zinia Phase II and Chissonga.
- Tendering in West and East Africa remains high, but timing of awards remains uncertain. Significant tender for the Satellite Field Phase II in Nigeria may be awarded in H1 2015.

Asia Pacific & Middle East

- *Potential* market awards for large projects over the next twelve months include: KG-D6 and Vashista in India and Gehem-Gendalo in Indonesia.
- Cost challenges in Australia make large SURF project awards unlikely in the near-term.

Gulf of Mexico

- In December 2014 Subsea 7 was awarded two contracts in the Gulf of Mexico.
- The number of small- and medium-size SURF project awards is expected to increase.

Joint Ventures

- Near-term contribution from SHL and SapuraAcergy JVs expected to be lower than record high 2013 levels.

Geographic Summary

North Sea

- Subsea 7 has very strong market share in the North Sea. Significant existing infrastructure provides recurring revenue and leads to high switching costs.
- Bundle technology remains a key differentiator.
- A number of tendered SURF projects in Norway have been postponed by Statoil until 2015/16. Demand for life-of-field activity is expected to remain strong through 2015.

Brazil

- Guara-Lula riser installation is expected to be completed by year end and the total full-life project loss has been reduced by approximately \$75 million year-to-date. We believe more positive revisions are likely.
- Only Tier-1 participants are capable of the operational responsiveness necessary to complete such large scale projects. Subsea 7 has the breadth of fleet and technical capabilities to ensure successful contract completion.
- Discussions with Petrobras are ongoing to reach an agreement on an acceptable risk profile for large pre-salt EPIC projects. The process established to work through the issues of Guara-Lula has been instrumental.

Brazil PLSV's – Foundation for the Future

- PLSV contracts provide a base of recurring and predictable revenue and cash flow.

(in millions US\$)						As of 9/30/2014	
Vessel	Contract Renewal/Start	Contract End	Duration (years)	Approximate Total Contract	Approximate Revenue / Yr	Revenue Earnings	Remaining Backlog
Normand Seven	12/31/13	09/30/18	4.8	400	84	63	337
Kommandor 3000	06/30/13	06/30/18	5.0	350	70	88	262
Seven Phoenix	09/30/13	09/30/18	5.0	450	90	90	360
Seven Condor	09/30/14	03/31/18	3.5	275	79	–	275
Seven Mar	12/31/13	12/31/16	3.0	290	97	72	218
Seven Seas	09/30/13	03/31/15	1.5	250	167	167	83
Seven Waves	06/30/14	06/30/19	5.0	500	100	25	475
Total:				2,515	686	505	2,010
Seven Sun, Rio and Cruzeiro	Q4 15 - Q4 16	12/31/20	5.0	1,600	320	–	1,600
Total:				4,115	1,006	–	3,610

Subsea 7 should generate > \$1 billion per year of annual revenue when operating all planned contracts in Brazil.

Leadership with Aligned Interests



Kristian Siem
Chairman

- Chairman of Subsea 7 since January 2002
- Assumed Chairman role upon the merger of Subsea 7 with Acergy
- Active in the oil & gas industry since 1972
- Currently Chairman of Siem Industries and Siem Industrikaptial
- Past director of Aker Kvaener and Transocean



Jean Cahuzac
CEO

- CEO of Subsea 7 since April 2008
- Active in the offshore oil & gas industry
- Prior experience as COO and then President of Transocean
- Spent 21 years in various positions at Schlumberger

- Chairman of the Board, Kristian Siem, and other family members own ~20% of Subsea 7's shares through Siem Industries.
- Attractive alignment of interests with leadership that has a long track record of successful capital allocation.

Capital Allocation

2015

- Repurchased \$6.4 million of shares.
- Board did not pay an annual dividend in order to preserve capital for better allocation opportunities including repurchasing shares, repurchasing debt at a discount and/or acquisition opportunities.

2014

- Repurchased \$166 million of shares and paid \$195 million as a dividend.
- Repurchased \$79 million of the \$275 million 3.5% convertible bonds due 13 October 2014 and subsequently redeemed the remaining \$182 million.
- Repurchased \$82 million of the \$700 million 1.0% convertible bonds due 2017.

2013

- Repurchased \$82.6 million of shares and paid \$199 million as a dividend.

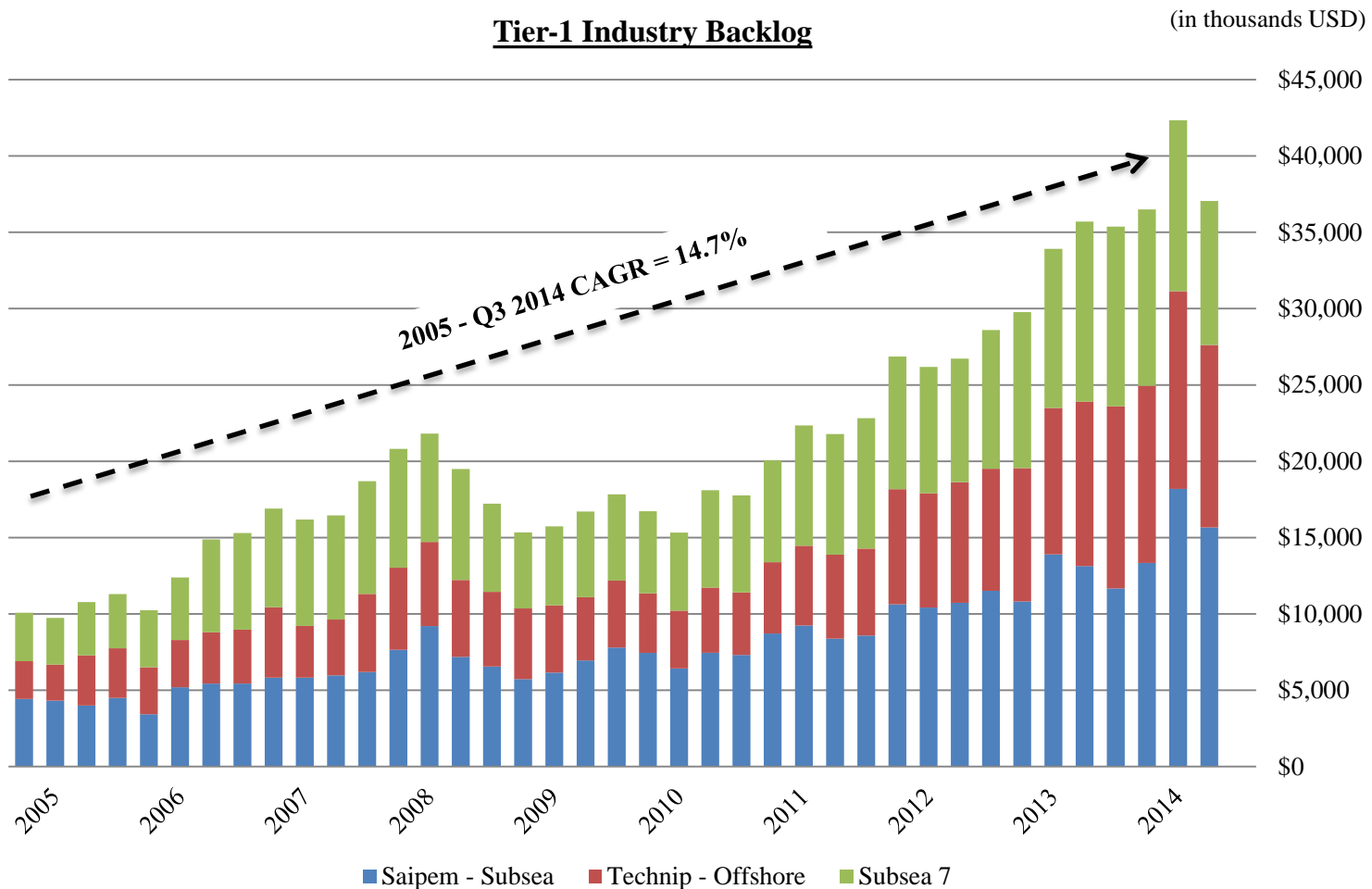
2012

- Exited two non-core businesses:
 - Sold its stake in NKT Flexibles;
 - Spun-off VERIPOS as a dividend-in-kind to shareholders.
- Repurchased \$200 million of shares and paid \$199 million as a dividend.

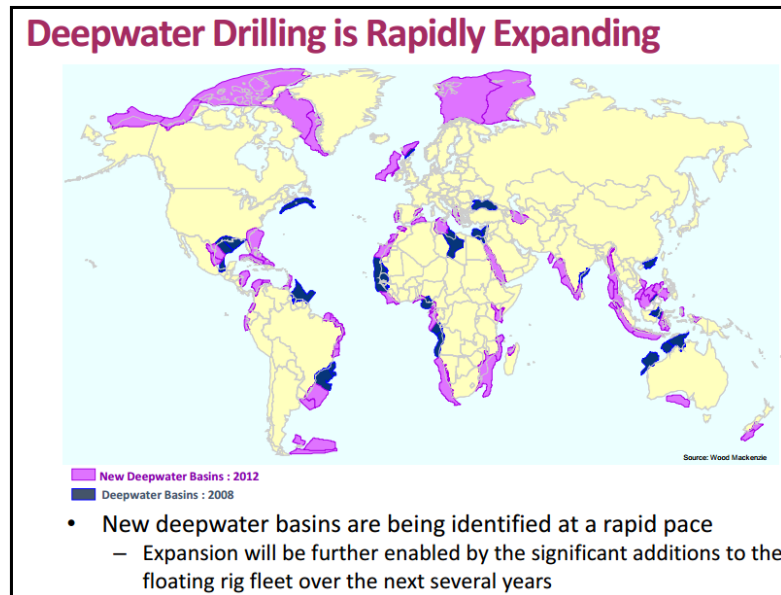
Sources of a Competitive Advantage

Type	Source	Evidence
Supply Advantage:	<ul style="list-style-type: none">• Proprietary Technology• Engineering and Project Management Process• Vessels (especially in certain ultra deep water and arctic areas)	History of increasingly complex engineering needs in deeper water requires a demonstrated track record of successful and safe execution.
Demand Advantage:	<ul style="list-style-type: none">• Market Position• Skilled Engineers• Local Content (Africa, Brazil)	In this case, the resource is skilled engineering talent.
Economies of Scale:	<ul style="list-style-type: none">• Size• Geographic Reach	The tangible and intangible costs of searching for someone who can complete a major ultra deep water project at or above the standard of “the big three” are very high.

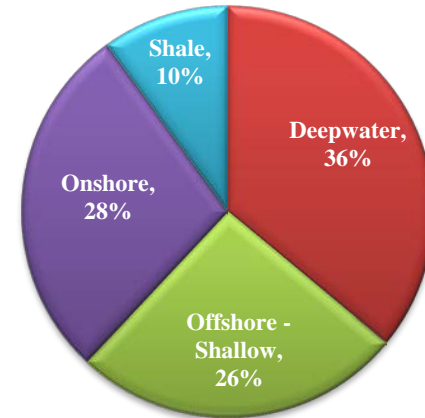
Industry Backlog – The Big 3



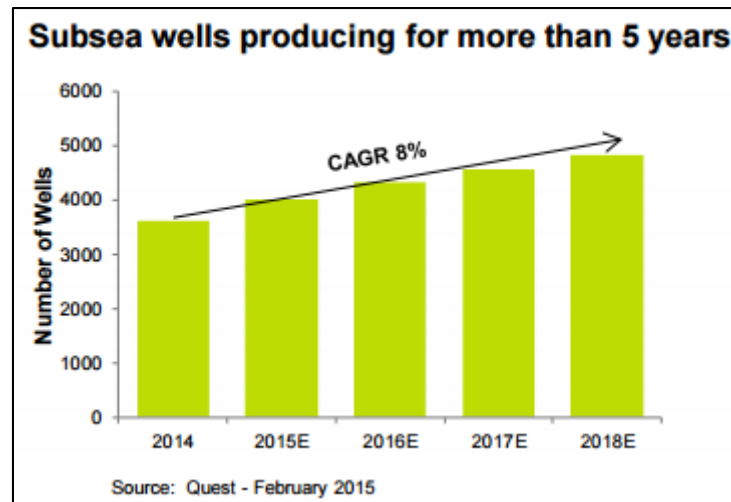
Favorable Dynamics



New Global Supply Sources Needed to Meet Expected World Demand in 2020

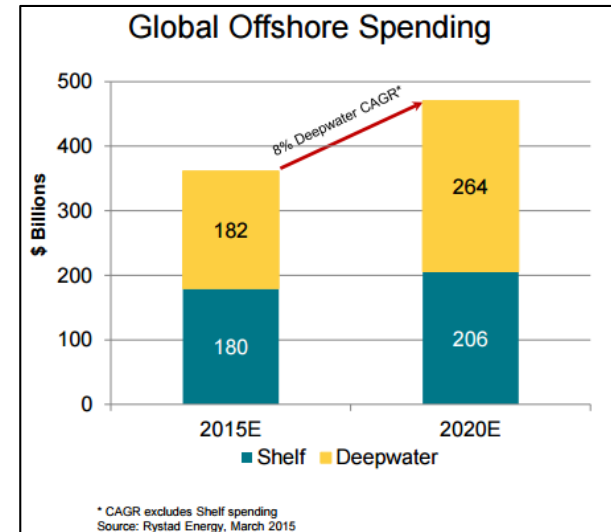


Est. 27 million barrels / day required



Increasing Demand

- Recent larger discoveries have been made in deeper waters and more remote regions.
- Production in these water depths and distances from shore requires large infrastructure investments.
- Deep water gas discoveries have become increasingly economical expanding the size of the addressable market.
- Deep water Subsea Production and SURF Capex are expected to increase 69% over the next 5 years (9.1% CAGR).

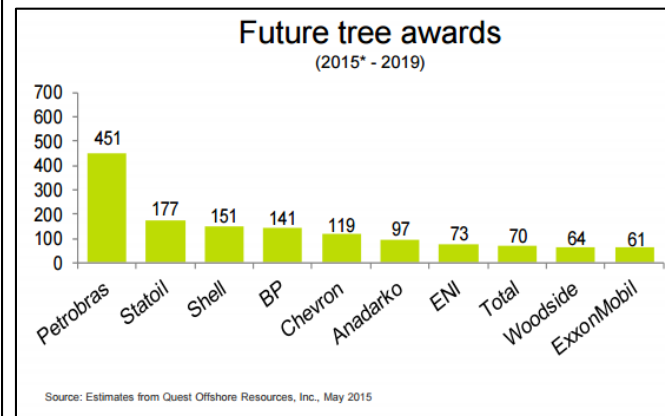
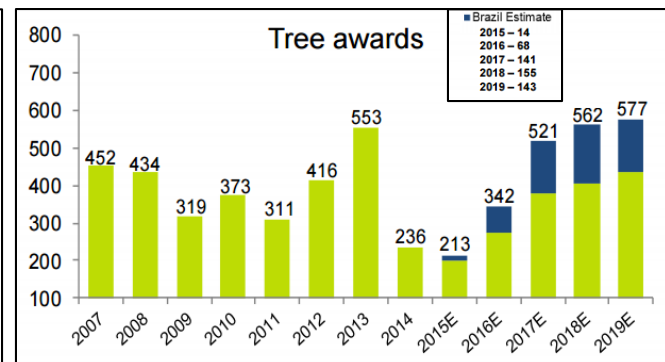


Revenue Drivers

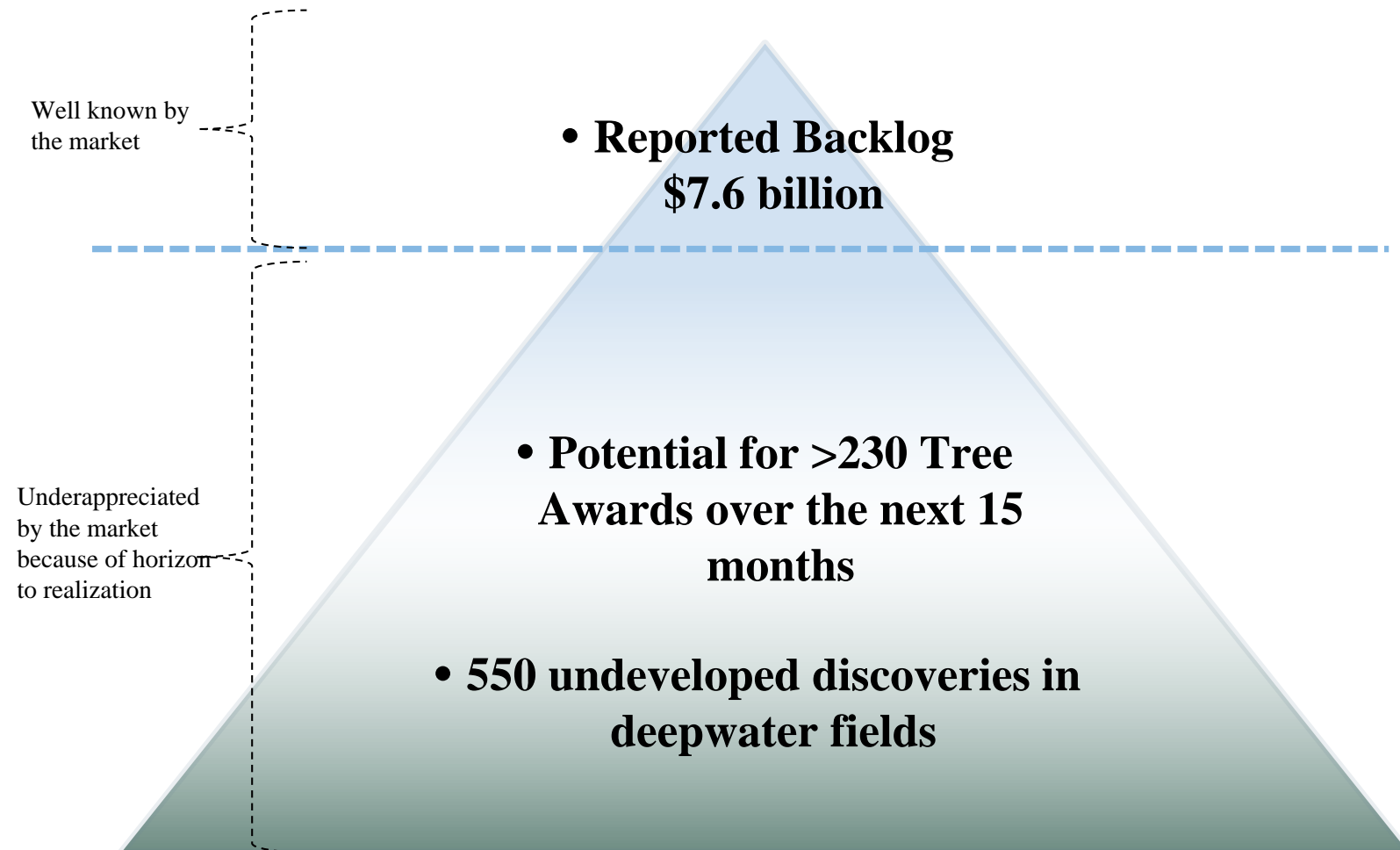
Major subsea project opportunities ahead

Potential \$150M+ subsea production system projects in the next 15 months*

Operator	Project	Location	No. of Trees
Woodside	Greater Western Flank Phase 2	Australia	11
Husky	Liwan Phase 2	China	5
Cobalt	Cameia	Angola	6
Murphy	Rotan Blk H	Malaysia	4
Reliance	R-Series	India	9
Shell	Appomattox	GOM	20
Statoil	Johan Sverdrup	Norway	13
Anadarko	Golfinho	Mozambique	30
Chevron	Buckskin Mocassin	GOM	7
ENI	Etan	Nigeria	11
BP	Mad Dog Phase 2	GOM	6
Shell	Bonga South West	Nigeria	48
Total	Zinia Phase 2	Angola	11
ENI	Mamba	Mozambique	21
Woodside	Browse	Australia	19
Chevron	Gorgon	Australia	8
			229



Revenue Drivers



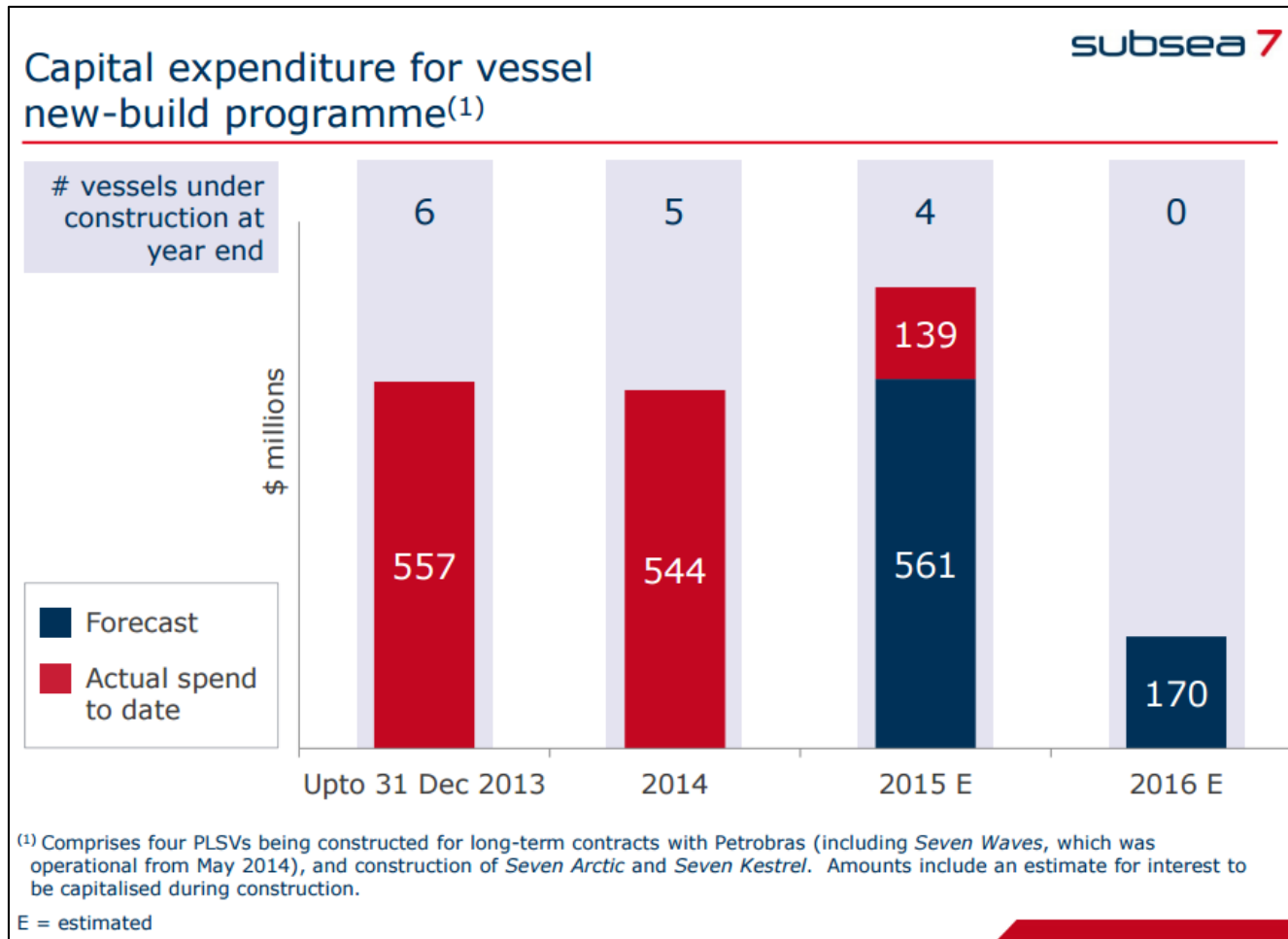
Financial Guidance

subsea 7

Financial guidance for 2015





- 2015 guidance is unchanged:
- Group Revenue expected to decrease significantly from record level in 2014
- Adjusted EBITDA margin expected to decrease compared to 2014
- Other net income related guidance:
 - Administrative expenses: \$280-300 million
 - Net finance costs: \$5-10 million
 - Depreciation and amortisation expense: \$420-440 million
 - Full year effective tax rate 28-31%
- Capex: \$900-950 million
 - \$700 million for the new-build vessel construction programme
 - \$200-250 million for sustaining capex

Financial Guidance



Financial Guidance

Fleet investments to meet growth objectives: vessel new-build programme

Ship	Vessel Type	Rationale	Operational
	Seven Waves Pipelay Support Vessel (PLSV)	Under 5-year contract with Petrobras	2 nd Quarter 2014 <i>(commenced operations mid May)</i>
	Seven Rio Seven Sun Seven Cruzeiro (PLSVs 2, 3 & 4)	Under 5-year contracts with Petrobras	4 th Quarter 2015 2 nd Quarter 2016 4 th Quarter 2016
	Seven Kestrel Diving Support Vessel (DSV)	Fleet replacement investment for growing market	4 th Quarter 2015
	Seven Arctic Heavy Construction Vessel (HCV) 900T crane	Strategic investment; enabling for seabed compression/separation/production module installation	1 st Quarter 2016

Earnings Summary

(USD mm)	2013	2014	TTM	<u>Consensus Est.</u>	
				2015E	2016E
Revenue	6,297.1	6,869.9	6,383.2	5,130.2	4,454.1
<i>growth</i>	<i>0.0%</i>	<i>9.1%</i>	<i>(1.8%)</i>	<i>(25.3%)</i>	<i>(13.2%)</i>
Gross Profit	742.4	1,175.0	1,175.9	776.6	576.0
<i>gross margin</i>	<i>11.8%</i>	<i>17.1%</i>	<i>18.4%</i>	<i>15.1%</i>	<i>12.9%</i>
Adj. EBITDA	981.0	1,439.0	1,456.0	950.9	774.5
<i>ebitda margin</i>	<i>15.6%</i>	<i>20.9%</i>	<i>22.8%</i>	<i>18.5%</i>	<i>17.4%</i>
Adj. Operating Income	573.4	929.5	940.0	522.4	334.3
<i>operating margin</i>	<i>9.1%</i>	<i>13.5%</i>	<i>14.7%</i>	<i>10.2%</i>	<i>7.5%</i>
Adj. Diluted EPS	\$1.00	\$2.32	\$2.35	\$1.12	\$0.69
Diluted Shares	374.7	369.0	348.4	343.8	338.3

Valuation

Implied EBITDA

	<u>Revenue (USD)</u>					
	7,000	7,500	8,000	8,500	9,000	9,500
18%	1,260	1,350	1,440	1,530	1,620	1,710
20%	1,400	1,500	1,600	1,700	1,800	1,900
22%	1,540	1,650	1,760	1,870	1,980	2,090
24%	1,680	1,800	1,920	2,040	2,160	2,280
26%	1,820	1,950	2,080	2,210	2,340	2,470
28%	1,960	2,100	2,240	2,380	2,520	2,660

Implied Stock Price (7x EBITDA)

	<u>Revenue (USD)</u>					
	7,000	7,500	8,000	8,500	9,000	9,500
18%	\$24.56	\$26.37	\$28.18	\$29.99	\$31.80	\$33.61
20%	\$27.38	\$29.39	\$31.40	\$33.40	\$35.41	\$37.42
22%	\$30.19	\$32.40	\$34.61	\$36.82	\$39.03	\$41.24
24%	\$33.00	\$35.41	\$37.83	\$40.24	\$42.65	\$45.06
26%	\$35.82	\$38.43	\$41.04	\$43.65	\$46.26	\$48.88
28%	\$38.63	\$41.44	\$44.26	\$47.07	\$49.88	\$52.69

Implied Margin of Safety

	<u>Revenue (USD)</u>					
	7,000	7,500	8,000	8,500	9,000	9,500
18%	153.0%	171.7%	190.3%	208.9%	227.6%	246.2%
20%	182.0%	202.7%	223.4%	244.1%	264.8%	285.5%
22%	211.0%	233.8%	256.5%	279.3%	302.1%	324.9%
24%	240.0%	264.8%	289.7%	314.5%	339.3%	364.2%
26%	269.0%	295.9%	322.8%	349.7%	376.6%	403.5%
28%	297.9%	326.9%	355.9%	384.9%	413.9%	442.8%

Comparable Analysis

Name	Price	Shares	Market Cap	Enterprise Value	Gross Margin	EBITDA Margin	ROE	ROIC	Net Debt / EBITDA	Debt / Equity
Technip SA	59.81	113	6,740	6,666	14.6%	9.8%	10.3%	6.8%	–	59.7%
Saipem SpA	10.61	440	4,664	11,150	39.1%	9.3%	(5.3%)	2.6%	4.4x	165.8%
Ezra Holdings Limited	0.40	1,013	402	2,228	14.7%	9.0%	8.4%	1.5%	12.0x	131.6%
McDermott International	2.91	238	692	967	8.2%	3.2%	(4.4%)	(0.7%)	0.0x	57.9%
Subsea 7 SA	10.23	326	3,339	3,322	18.4%	19.6%	(6.3%)	8.7%	0.0x	10.4%
Mean:					22.8%	9.4%	4.5%	3.7%	5.5x	119.0%
Median:					14.7%	9.3%	8.4%	2.6%	4.4x	131.6%

Name	EBITDA						Earnings Per Share					
	FY '13	EV / EBITDA	FY '14E	EV / EBITDA	FY '15E	EV / EBITDA	FY '13	Price / Earnings	FY '14E	Price / Earnings	FY '15E	Price / Earnings
Technip SA	1,191	4.6x	1,577	4.6x	1,574	3.7x	4.42	12.2x	7.01	11.2x	6.91	8.5x
Saipem SpA	1,457	7.7x	1,939	6.7x	2,198	5.6x	(0.63)	–	1.26	14.1x	1.72	8.4x
Ezra Holdings Limited	138	12.6x	166	10.5x	226	7.7x	0.04	19.7x	0.05	8.6x	0.06	6.2x
McDermott International	72	NM	174	28.1x	275	6.0x	(0.32)	–	0.09	–	0.30	32.0x
Subsea 7 SA	1,345	3.0x	1,150	2.5x	1,121	3.1x	(1.02)	6.1x	1.47	4.9x	1.36	7.0x
Mean		8.3x		7.2x		5.7x		10.6x		11.3x		7.7x
Median		7.7x		6.7x		5.6x		12.2x		11.2x		8.4x

(in thousands USD)

Risks to Our Thesis

- Oil prices could fall further or remain at current levels for an extended period leading major oil companies to defer capital expenditures and delay deep water developments.
- Ongoing operational and/or financial issues at Petrobras could cause significant delays to deep water development in Brazil.
- Increasing competition in shallower water could result in decreased profitability should well depth not continue to increase.
- The safe and successful execution of large, complex EPIC projects is a primary risk. Supply chain delays can reverberate throughout the entire project.
- Operations in deep water are subject to unpredictable events such as severe weather or harsh ocean environments.
- While management believes the current provision for the Guara-Lula Project in Brazil is sufficient, additional problems could require additional write-downs.

Disclosure

The Firm is not providing investment advice through this material. This presentation is provided for informational purpose only as an illustration of the firm's investment philosophy and shall not be considered investment advice or a recommendation or solicitation to buy or sell any securities discussed herein. As of the date of this presentation the firm continues to own the securities discussed herein. These opinions are not intended to be a forecast of future events, a guarantee of future results, or investment advice. Past performance is not indicative of future results, and no representation or warranty, express or implied, is made regarding future performance.

Robotti & Company Advisors, LLC or its affiliates may engage in securities transactions that are inconsistent with this communication and may have long or short positions in such securities. The information and any opinions contained herein are as of the date of this material, and the firm does not undertake any obligation to update them. Information contained in this presentation has been obtained from sources which we believe to be reliable, but we do not make any representation as to its accuracy or its completeness and it should not be relied on as such.

This material does not take into account individual client circumstances, objectives, or needs and is not intended as a recommendation to any person who is not a client of the firm. Securities, financial instruments, products or strategies mentioned in this material may not be suitable for all investors. Robotti & Company Advisors, LLC does not provide tax advice. Investors should seek tax advice based on their particular circumstances from an independent tax advisor.

In reaching a determination as to the appropriateness of any proposed transaction or strategy, clients should undertake a thorough independent review of the legal, regulatory, credit, accounting and economic consequences of such transaction in relation to their particular circumstances and make their own independent decisions.

Disclaimer

<u>Disclosures</u>	Subsea 7 (OB:SUBC)
Robert Robotti and/or members of his household has a financial interest in the following securities	Yes
Robotti & Company or its affiliates beneficially own common equity of the following securities	Yes
Robotti & Company or its affiliates beneficially own 1% or more of any class of common equity of the following securities	Yes
Robert Robotti serves as a Director or Officer or Advisory Board Member of the following securities	No

LSB Industries: Sowing the Seeds of Value

SMALL-CAP INVESTING SUMMIT 2014
FEBRUARY 12, 2014

Bob Robotti
President & CEO



Disclaimer

The Firm is not providing investment advice through this material. This presentation is provided for informational purpose only as an illustration of the firm's investment philosophy and shall not be considered investment advice or a recommendation or solicitation to buy or sell any securities discussed herein. As of the date of this presentation the firm continues to own the securities discussed herein. These opinions are not intended to be a forecast of future events, a guarantee of future results, or investment advice. Past performance is not indicative of future results, and no representation or warranty, express or implied, is made regarding future performance.

Robotti & Company Advisors, LLC or its affiliates may engage in securities transactions that are inconsistent with this communication and may have long or short positions in such securities. The information and any opinions contained herein are as of the date of this material, and the firm does not undertake any obligation to update them. Information contained in this presentation has been obtained from sources which we believe to be reliable, but we do not make any representation as to its accuracy or its completeness and it should not be relied on as such.

This material does not take into account individual client circumstances, objectives, or needs and is not intended as a recommendation to any person who is not a client of the firm. Securities, financial instruments, products or strategies mentioned in this material may not be suitable for all investors. Robotti & Company Advisors, LLC does not provide tax advice. Investors should seek tax advice based on their particular circumstances from an independent tax advisor.

In reaching a determination as to the appropriateness of any proposed transaction or strategy, clients should undertake a thorough independent review of the legal, regulatory, credit, accounting and economic consequences of such transaction in relation to their particular circumstances and make their own independent decisions.

About Robotti & Company

- Established in 1983 by Robert Robotti.
- Robotti & Company Advisors manages internal and external capital in separately managed accounts and several private partnerships.
- We believe that market prices of securities do not necessarily indicate their true economic worth. Guided by this philosophy, our analysts research and identify equities selling at significant discounts to their “intrinsic value.”
- Our niche is small-to-mid capitalization equities of misunderstood, neglected, or out-of-favor companies around the world.

Behavioral Edge Forms Our Foundation

Behavioral Edge

We take a longer-term view and have the ability to tolerate losing money before we make it.

Leads Us To

Analytical Edge

Within the context of a longer-term perspective and 30+ years of experience, we have the ability to develop a different conclusion than that of the market.

Informational Edge

Our network of industry relationships, focus on deep primary research, and experience serving on company boards, provides us with more pieces for building our information mosaic.

Our behavioral edge comes from our ability to tolerate losing money before we make it. As a result, our investment process concentrates on understanding the long-term normalized earning power of a business well before the market gains interest.

Select Investment Themes

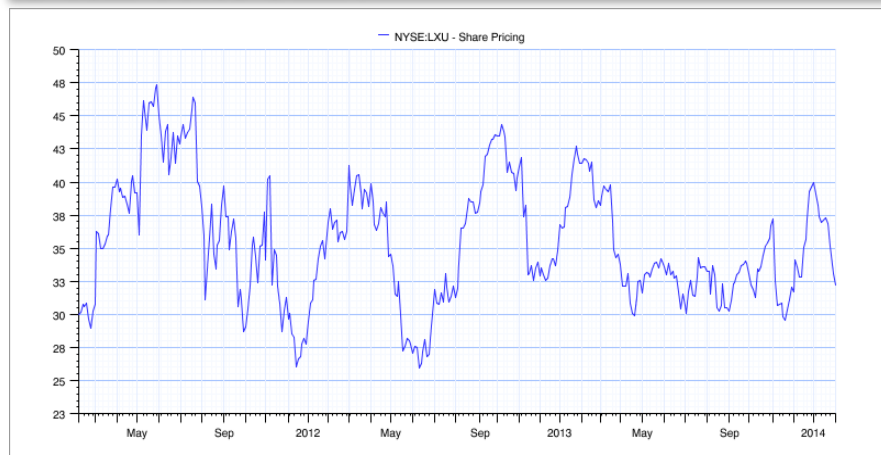
- ✓ Industries facing significant near-term headwinds / “unknowns.”
- ✓ Individual companies that are certainly not immune to the industry-wide issues and may even have more serious complications.
- ✓ Large insider-ownership – managers who ‘eat their own cooking.’
- ✓ The dynamics are in place for very long runways of growth.

LSB Industries, Inc. (NYSE: LXU)

Company Background

- LSB Industries was formed in 1968 and is headquartered in Oklahoma City, OK.
- The company operates two primary segments: (1) Chemical, and (2) Climate Control.
- The chemical business (63% of revenue) manufactures and sells nitrogen based chemicals.
- The climate control business (35% of revenue) manufactures and sells a broad range of HVAC and is a leader in the geothermal & water source heat pump market.

3 Year Price Chart



Market Capitalization (USD mm as of 2/10/14)

Price	\$32.33
Shares	23.6
Market Cap	\$763.0
Long-Term Debt	468.4
Preferred Shares	3.0
Cash	139.7
LT Cash & Equiv	280.0
Enterprise Value	\$814.8

Valuation Summary

(\$ mm)	2011	2012	2013E	2014E
Revenue	805.3	759.0	707.0	800.0
<i>ev/ revenue</i>	<i>1.0x</i>	<i>1.0x</i>	<i>1.0x</i>	<i>1.0x</i>
EBITDA	155.5	116.9	68.0	145.0
<i>ev/ebitda</i>	<i>5.2x</i>	<i>7.0</i>	<i>12.0</i>	<i>5.6x</i>
Diluted EPS	\$3.80	\$2.61	\$0.82	\$2.76
<i>p/e</i>	<i>8.5x</i>	<i>12.4x</i>	<i>39.5x</i>	<i>11.7x</i>

Trading Summary

52 Week High / Low:	\$42.24 / \$28.15
Avg Daily Volume:	165,720
Listing Exchange:	NYSE
Analyst Coverage:	4

Source: Capital IQ, Wall Street Consensus Estimates, Company Filings

ROBOTTI
& COMPANY ADVISORS, LLC

Investment Highlights

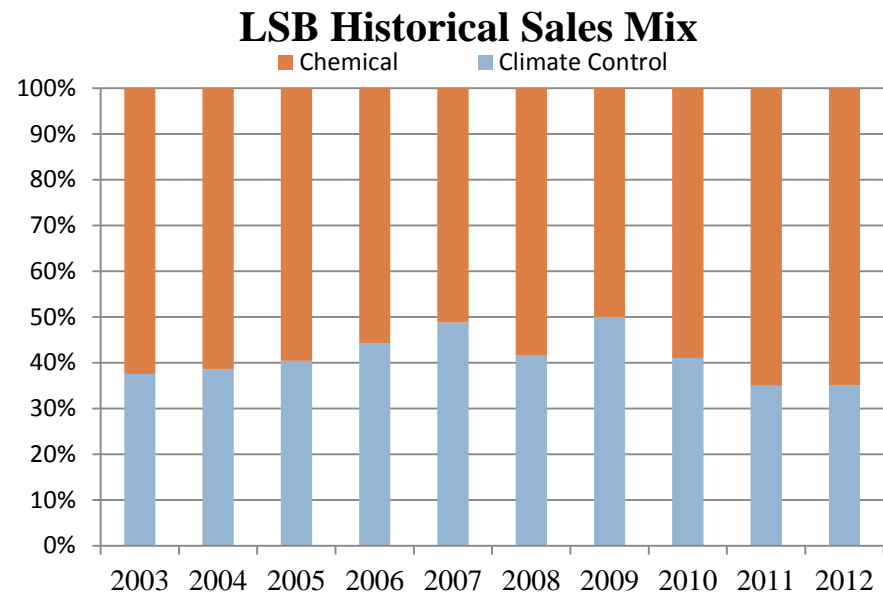
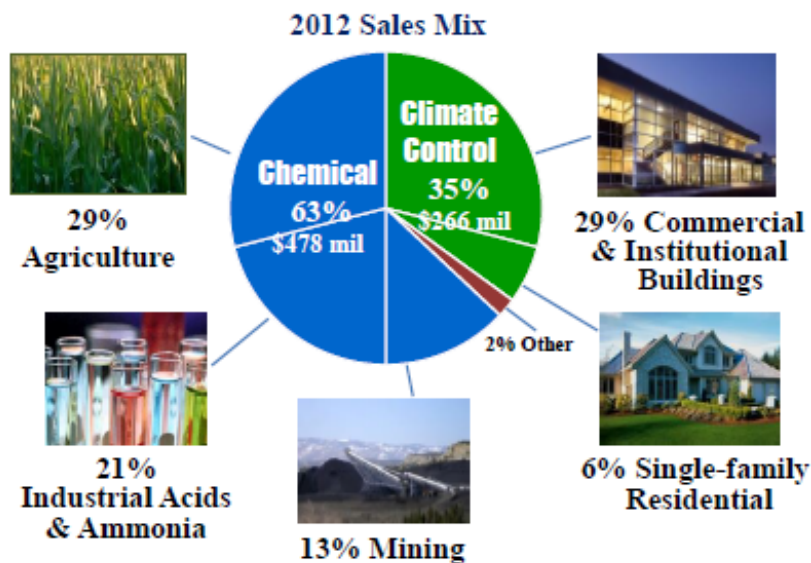
- **Domestic leader in two separate niche businesses**
- **Chemical segment has not demonstrated its true earning power**
 - Several operational issues have weighed on recent earnings
 - Management has opportunistically grown this business
- **Climate control segment positioned for cyclical recovery**
 - Weak residential and commercial real estate markets
 - Consistent revenue / margins even at low utilization rates in recent trough
- **Management team with significant ownership and a history of creating shareholder value**
- **We believe shares trade at a 50% - 100% discount to intrinsic value**
 - Recent developments have forced management to address operational issues
 - Chemical segment is poised to take advantage of a long-term feedstock advantage
 - Climate control segment is poised to benefit from a rebound in residential and commercial construction

Background

LSB operates two primary segments:

Chemical Segment: Manufactures and sells nitrogen based chemicals to North American agricultural, mining and industrial industries.

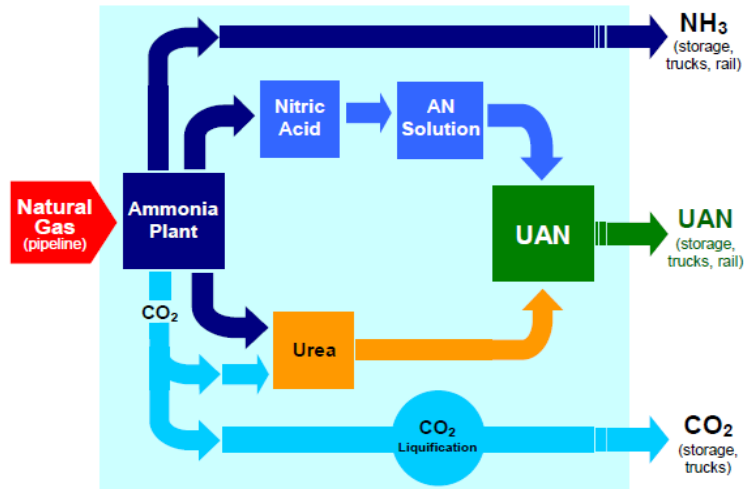
Climate Control Segment: Manufactures and sells a broad range of HVAC products to commercial, institutional, and residential new construction, renovation and replacement with a particular focus on geothermal and water source heat pumps.



Chemical Segment

- Manufactures and sells nitrogen based chemicals to North American agricultural, mining and industrial industries.
- Leading supplier of urea ammonium nitrate (UAN) and ammonium nitrate (AN) fertilizers in key markets.
- Leading merchant marketer of nitric acid in the U.S.
- Nitrogen is required for most crops to grow – corn, soybeans, wheat, forage.

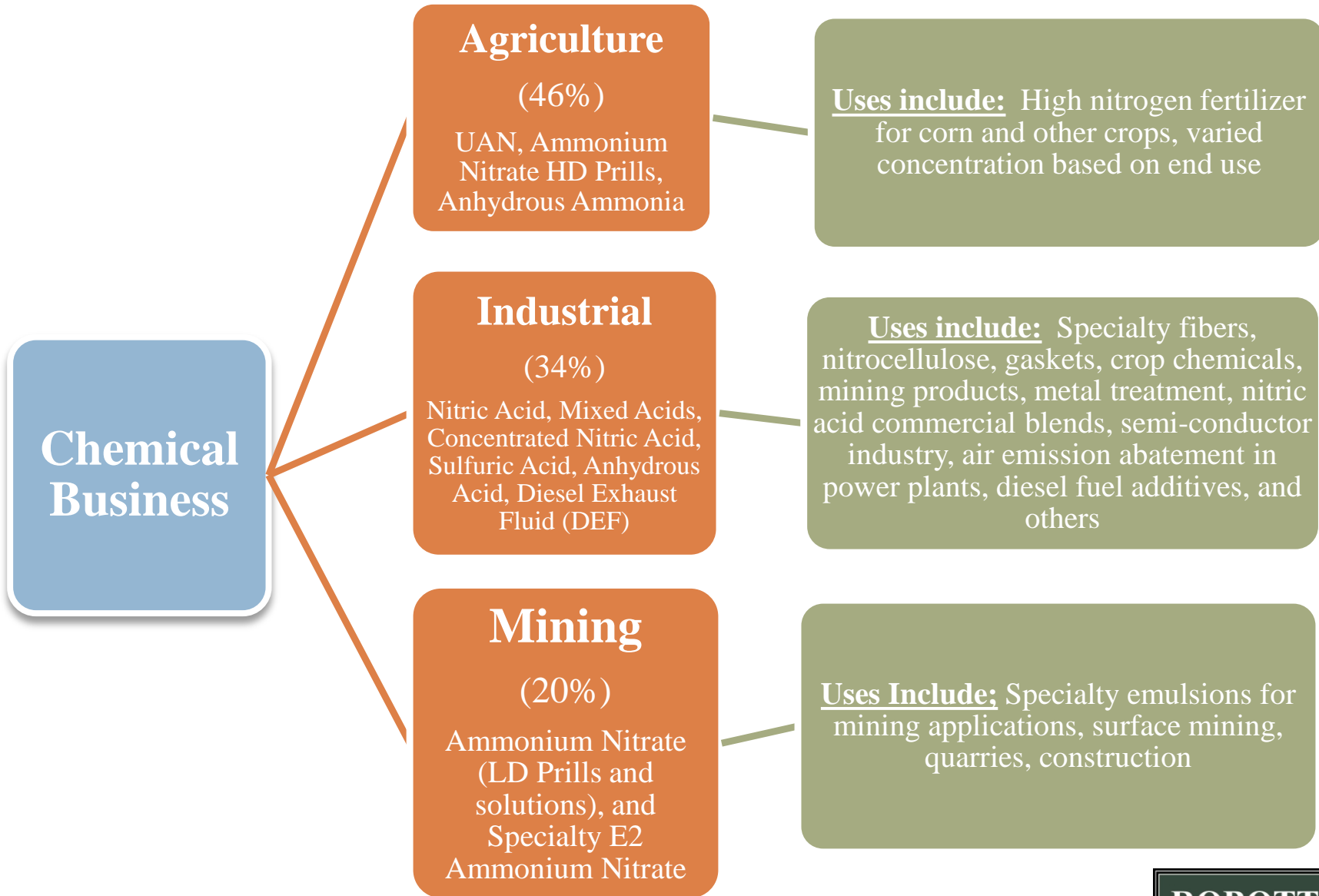
Typical Facility Process Flow (Pryor)



Major Chemical Customers



Chemical Markets

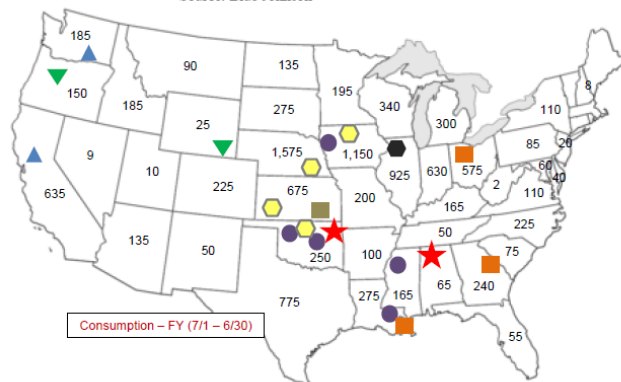


Domestic Capacity

U.S. UAN Plant Locations

2012 UAN Usage = 11.5 Mil. Short Tons

Source: Blue Johnson



U.S. Production Capacity:

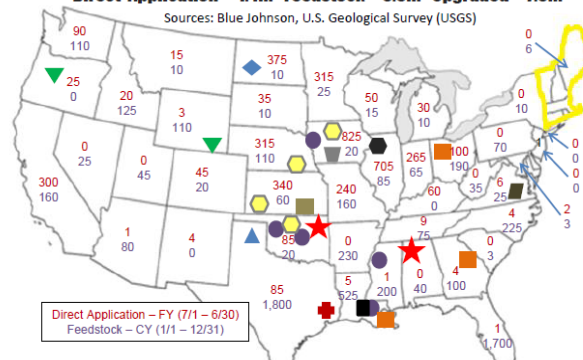
▲	AGRIUM 645,000
▲	Kennewick, WA 430,000
▲	W. Sacramento, CA 215,000
●	CF INDUSTRIES 6,495,000
●	Verdigris, OK 2,050,000
●	Woodward, OK 845,000
●	Port Neal, IA 800,000
●	Donaldsonville, LA 2,275,000
●	Yazoo City, MS 525,000
■	COFFEYVILLE RESOURCES 1,010,000
■	Coffeyville, KS 1,010,000
■	DYNO NOBEL 355,000
■	Cheyenne, WY 290,000
■	KOCH 1,085,000
■	Beatrice, NE 200,000
■	Dodge City, KS 255,000
■	Enid, OK 90,000
■	Ft. Dodge, IA 540,000
★	LSB INDUSTRIES 575,000
★	Pryor, OK 325,000
★	Cherokee, AL 250,000
■	POTASH CORP 1,885,000
■	Augusta, GA 500,000
■	Lima, OH 250,000
■	Geismar, LA 1,135,000
■	RENTTECH 375,000
■	East Dubuque, IL 375,000

U.S. Anhydrous Ammonia Plants

2012 Total Production = 11,309,250 Short Tons

Direct Application = 4.4m Feedstock = 6.5m Upgraded = 7.5m

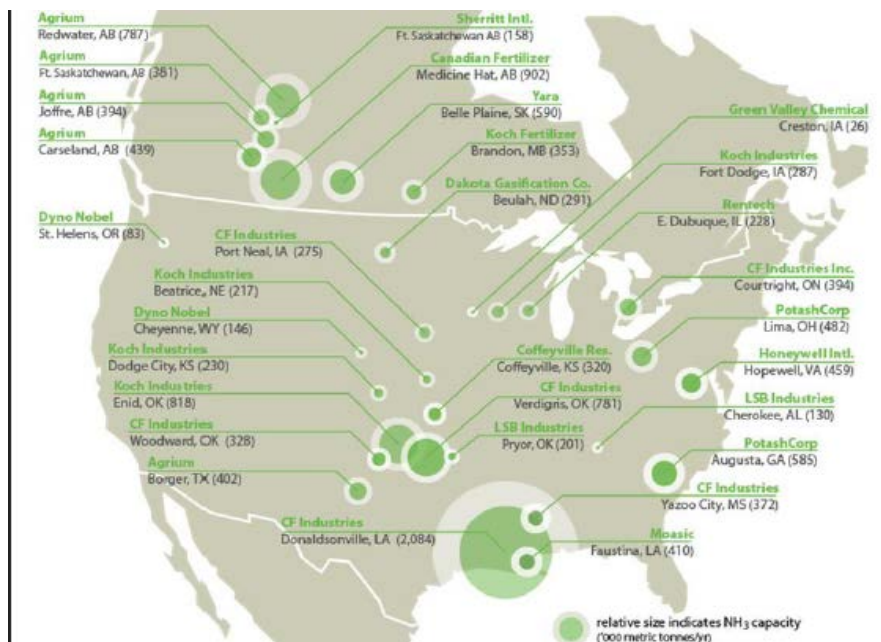
Sources: Blue Johnson, U.S. Geological Survey (USGS)



U.S. Production Capacity:

▲	AGRIUM 540,000	FREE NH3
▲	Borger, TX 540,000	450,000
●	CF INDUSTRIES 5,345,000	FREE NH3
●	Donaldsonville, LA 2,755,000	810,000
●	Port Neal, IA 385,000	45,000
●	Verdigris, OK 1,130,000	305,000
●	Woodward, OK 570,000	145,000
●	Yazoo City, MS 505,000	-0-
■	COFFEYVILLE 400,000	FREE NH3
■	Coffeyville, KS 400,000	-0-
■	DAKOTA GAS 450,000	FREE NH3
■	Beulah, ND 450,000	300,000
■	DYNO NOBEL 300,000	FREE NH3
■	Cheyenne, WY 190,000	-0-
■	St. Helens, OR 110,000	15,000
■	EASTMAN CHEM 250,000	FREE NH3
■	Beaumont, TX 250,000	250,000
■	GREEN VALLEY CHEM 35,000	FREE NH3
■	Creston, IA 35,000	30,000
■	HONEYWELL 580,000	FREE NH3
■	Hopewell, VA 580,000	-0-
■	KOCH 2,095,000	FREE NH3
■	Beatrice, NE 300,000	200,000
■	Dodge City, KS 310,000	200,000
■	Enid, OK 1,100,000	720,000
■	Ft. Dodge, IA 385,000	160,000
★	LSB INDUSTRIES 475,000	FREE NH3
★	Pryor, OK 300,000	100,000
★	Cherokee, AL 175,000	-0-
■	MOSAIC 565,000	FREE NH3
■	Faustina, LA 565,000	190,000
■	PCS 1,935,000	FREE NH3
■	Augusta, GA 785,000	120,000
■	Lima, OH 650,000	300,000
■	Geismar, LA (Q1 13) 500,000	-0-
■	RENTTECH 335,000	FREE NH3
■	East Dubuque, IL 335,000	150,000

- U.S. production capability of 13,305,000 short tons (Blue, Johnson)
- Total free ammonia is approximately 4,490,000 short tons (Blue, Johnson)
- In 2012 ammonia plants operated at 85% of rated capacity (Blue, Johnson)
- Imports in 2012 estimated to be 6,900,000 short tons (TFI)
- 2012 estimated imports as a percentage of consumption = 38%



Demand Drivers: Agriculture

Basic Macro Agro-Economics

World Situation:

- Growing populations
- Developing economies
- Changing dietary habits (from grain to meat)
- Worldwide grain shortages and low stock-to-use ratios

North American Situation:

- World grain shortages impact grain requirements in the U.S.
- During last 3 years U.S. consumed more grain than it produced
- U.S. grain stocks are at low levels

Result:

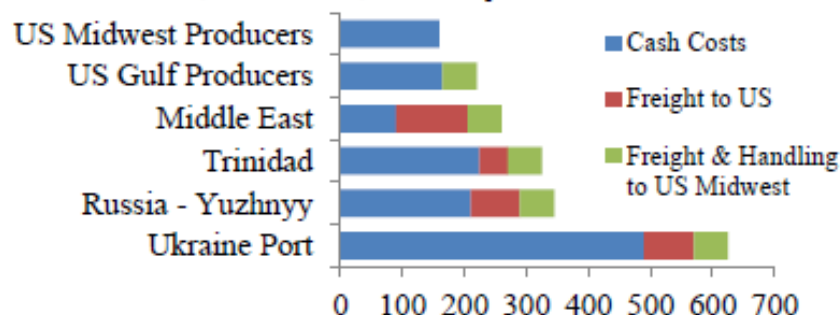
- **High demand for grain expected in 2013 and beyond**

North America is Low Cost Producer of Nitrogen Fertilizers

- Natural gas is the primary feedstock for anhydrous ammonia and all nitrogen fertilizers.
- Due to large shale gas reserves, U.S. has very low natural gas prices vs. most places worldwide.
- Natural gas is expected to average between \$3.50 and \$4.00 per MMBtu in 2013.

U.S. Midwest Delivered Ammonia Cost Forecast (\$US/ton)

Source: Fertecon, Blue Johnson, PotashCorp



Natural Gas Feedstock Advantage

World LNG Estimated November 2013 Landed Prices



Market Realist[®] Source: Waterborne Energy Inc. (Data in \$US/MMBtu Updated October 7, 2013)

Will Natural Gas Prices Fall Further?

Behavioral Edge:

We take a longer-term view and have the ability to tolerate losing money before we make it.

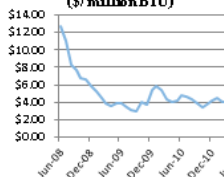
Leads Us To

Analytical Edge:

Within the context of a longer-term perspective and 30+ years of experience, we have the ability to develop a different conclusion than that of the market.

- It comes down to maintaining the proper temperament.

Natural Gas Price – Henry Hub (\$/million BTU)



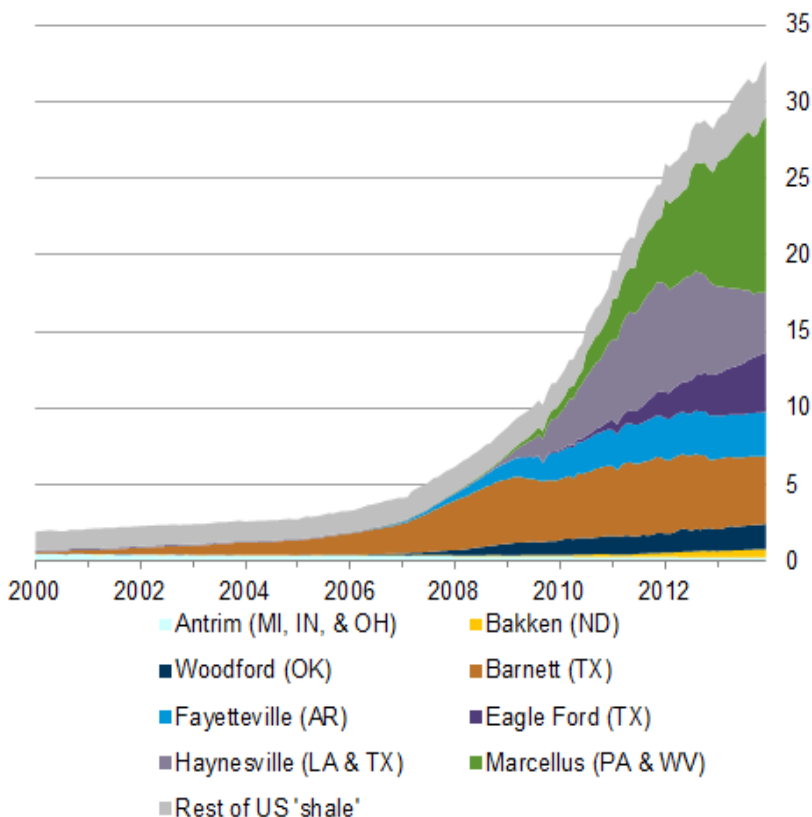
Natural Gas Henry Hub Price: \$2.16 (as of 4/27/2012)

"There are two kinds of forecasters: those who don't know, and those who don't know they don't know."

- John Kenneth Galbraith

ROBOTTI & COMPANY ADVISORS, LLC

Monthly dry shale gas production billion cubic feet per day



Source: EIA derived from state administrative data collected by DrillingInfo Inc. Data are through January 2014 and represent EIA's official shale gas estimates, but are not survey data. State abbreviations indicate primary state(s).

ROBOTTI & COMPANY ADVISORS, LLC

Domestic Fertilizer Capacity Growth

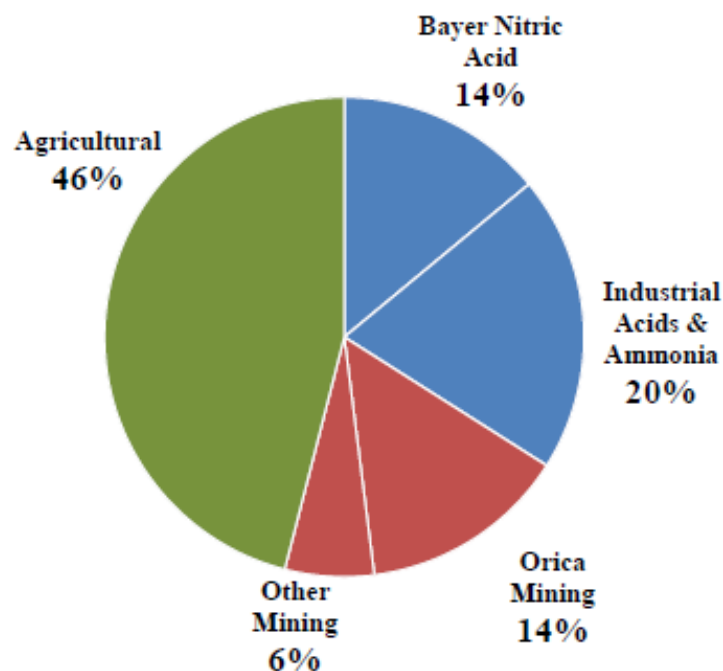
	Plant Location	Est. Capex (US\$B)	Product Mix	Estimated Completion	Incremental Gross Ammonia Capacity (Mst)	Incremental Merchant Ammonia Capacity (Mst)	Incremental Urea/UAN Capacity (Mst)
Expected Brownfields							
PotashCorp. Geismar restart	Geismar, LA	\$0.2	Ammonia/UAN	2013	0.6	0.0	0.8
PotashCorp.	Lima, OH	\$0.2	Urea	2015E	0.1	0.0	0.1
Agrium	Borger, TX	\$0.5	Ammonia/Urea	2016E	0.1	-0.3	0.7
CF	Port Neal, IA; Donaldsonville, LA	\$3.8	Ammonia/Urea/UAN	2015-16E	2.1	0.3	3.8
Koch	Enid, OK	\$1.0	Urea	2016E	0.0	-0.6	1.0
					2.9	-0.6	6.4
Expected Greenfields							
Dyno Nobel (Incitec Pivot)	Waggaman, LA	\$0.9	Ammonia	TBD	0.9	0.9	-
LSB Industries	El Dorado, AK	\$0.3	Ammonia	2015E	0.4	0.2	-
Orascom	Wever, IA	\$1.8	Ammonia/Urea/UAN/DEF	2015E	0.9	0.2	1.6
					2.2	1.3	1.6
Total Expected Brownfields and Expected Greenfields					5.1	0.7	8.0
Potential Brownfields							
Agrium	Redwater, AB	\$0.2	Urea	2015E	0.0	-0.1	0.2
Yara Belle Plaine	Belle Plaine, SK	TBD	Urea	2016E	0.9	-	1.4
Potential Greenfields							
Agrios	Pasadena, TX	TBD	Ammonia/Urea	TBD	TBD	TBD	TBD
Cronus Chemicals	IA/IL TBD	\$1.2	Ammonia/Urea	TBD	TBD	TBD	TBD
Agrium	US TBD	TBD	Urea/UAN	2017E	TBD	TBD	1.8
Dakota Gasification Company	Beulah, ND	TBD	Urea	2017E	-	-0.3	0.4
EuroChem	US TBD	\$1.5	Ammonia/Urea	2018E	TBD	TBD	TBD
IFFCO	Becancour, QC	\$1.2	Ammonia/Urea	2017-18E	0.8	-	1.4
FNA Fertilizer Limited Partnership	Western Canada	TBD	Ammonia/Urea	TBD	TBD	TBD	TBD
Midwest Fertilizer Corp	Posey County, IN	\$2.1	Ammonia/UAN/Urea	TBD	0.8	TBD	TBD
North Dakota Corn Growers / CHS	Spiritwood, ND	\$1.1-1.4	Ammonia/Urea/UAN	2016E	0.8	TBD	TBD
Northern Plains Nitrogen	Dakotas	TBD	Ammonia/Urea	TBD	0.7	TBD	TBD
Ohio Valley Resources LLC	Spencer County, IN	\$1.0	Ammonia/UAN/DEF	2016E	0.8	0.4	1.1
Summit Power	Penwell, TX	\$2.5	Electricity/Urea	2015E	-	-	0.7
Yara/BASF	U.S. Gulf	TBD	Ammonia/TBD	TBD	TBD	TBD	TBD

Note: Capacity figures are slated in millions of short tons

Source: BMO Capital Markets, Company Reports, Industry Reports

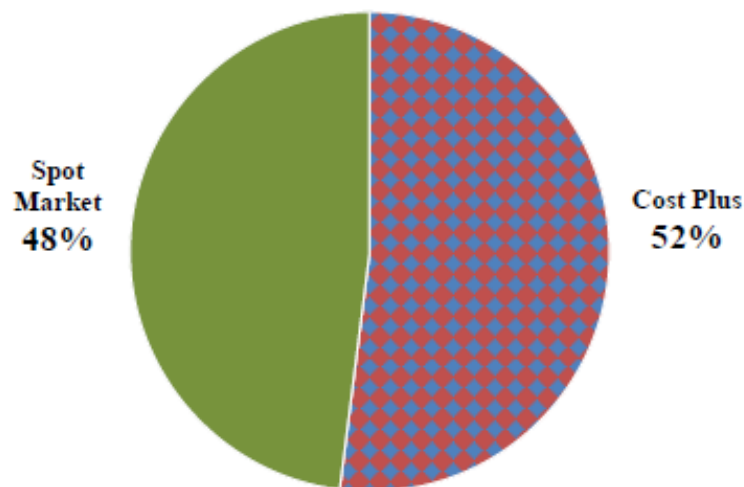
Cost-Plus Sales Agreements

Sales by Market & Key Customer



*A key strategy is to
OPTIMIZE SALES MIX:
industrial vs. agricultural.*

Cost-Plus Agreements vs. Spot Market Sales



*Approximately half our sales
are **NON-SEASONAL**
and priced pursuant to
COST-PLUS agreements.*

2012 Sales Mix

Chemical Facilities

El Dorado, AK

- 150 acre, multi-product facility located on a 1,400 acre site
- Produces high density ammonium nitrate (AN) for agricultural markets and regular nitric acid, concentrated nitric acid, mixed (nitrating) acids, sulfuric acid, and ammonium nitrate solutions for industrial markets
- Products are distributed by truck or rail through third-party distributors, wholesalers, and 17 company owned retailers in TX, TN, and MI
- Feedstock: Ammonia (delivered by pipeline)

Baytown, TX

- Operates one of the newest and most technologically advanced nitric acid plants in North America located within the Bayer Material Science complex
- Produces regular nitric acid used for the polyurethane, nylon fiber and plastics industries.
- Products are distributed by truck or rail
- Feedstock: Anhydrous ammonia (delivered by pipeline)

Source: Company Financials

Cherokee, AL

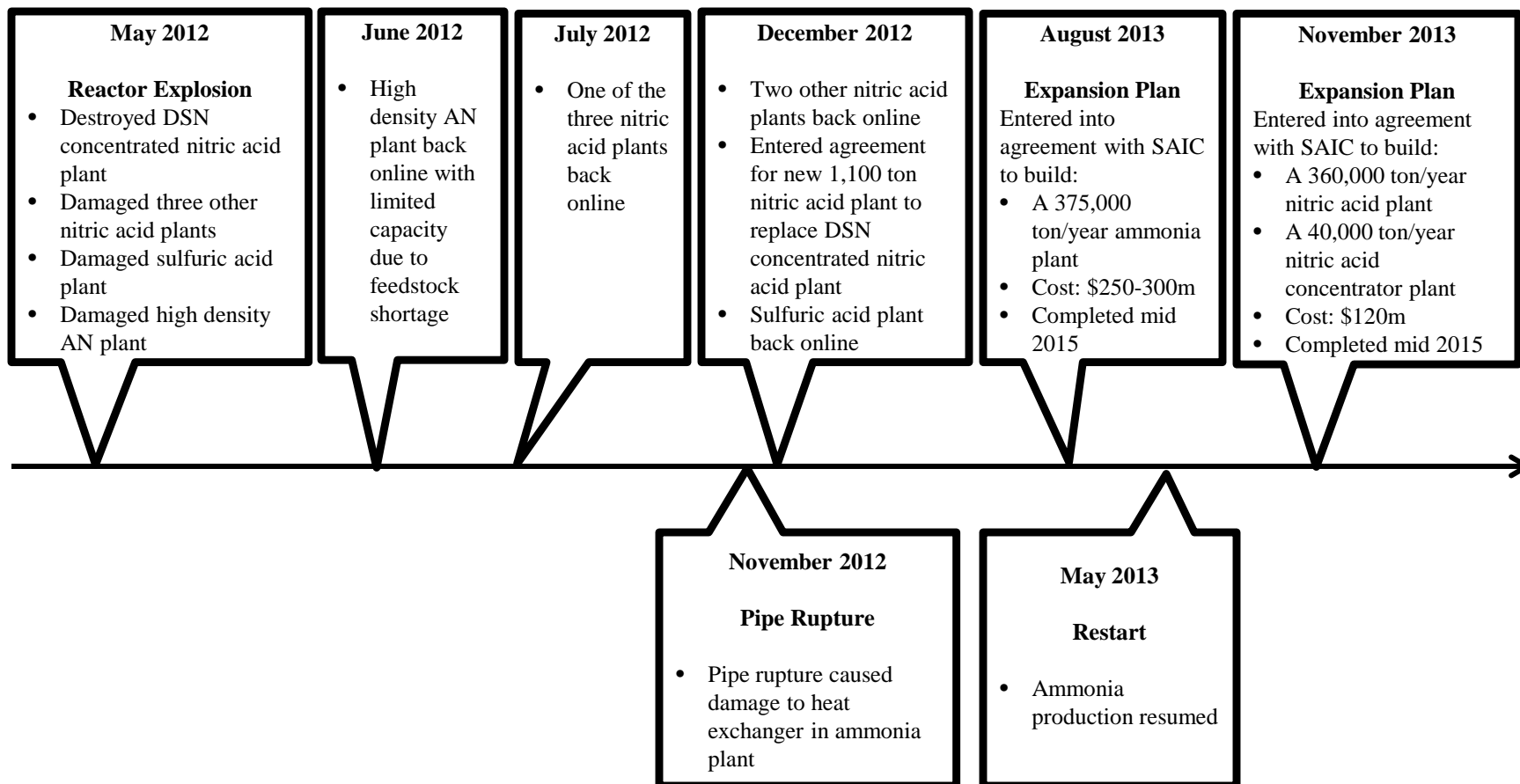
- Operates a 160 acre, multi-product facility on a 1,300 acre site located on the bank of the Tennessee River in Cherokee
- Produces urea ammonium nitrate (UAN), urea and nitrate for agricultural markets and nitric acid, ammonium nitrate solutions, anhydrous ammonia, diesel exhaust fluid (DEF) and carbon dioxide for industrial markets
- Products are distributed by truck, rail, pipeline, or barge
- Feedstock: Natural gas (delivered by pipeline)

Pryor, OK

- Operates a 47 acre, multi-product facility on a 104 acre site
- Produces anhydrous ammonia, urea, and urea ammonium nitrate (UAN) for agricultural markets and nitric acid, and carbon dioxide for industrial markets
- Products are distributed by truck or rail
- Feedstock: Natural gas (delivered by pipeline)

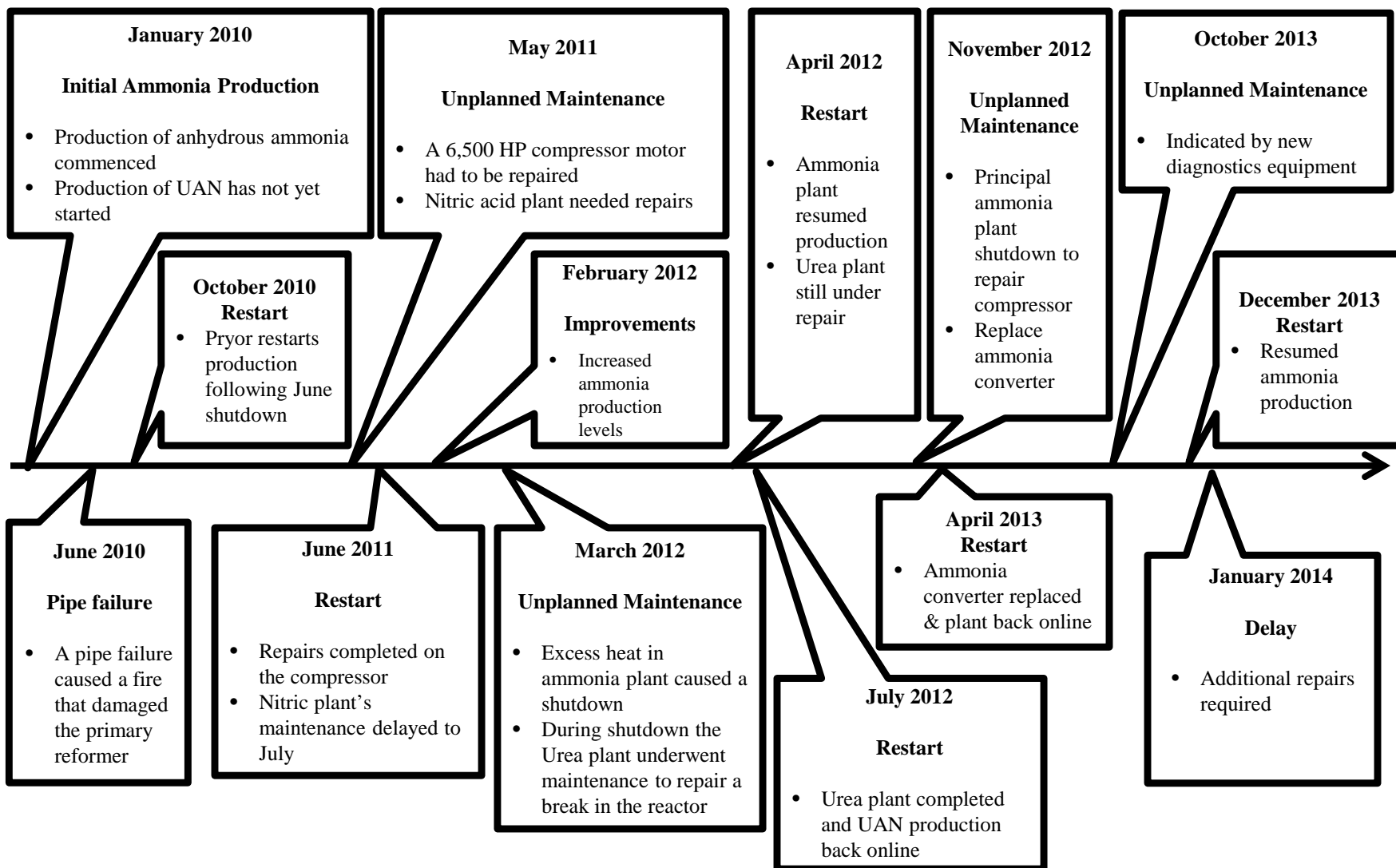
El Dorado and Cherokee Facilities Timeline

El Dorado



Cherokee

Pryor Facility Timeline



Capital Expenditure Plans

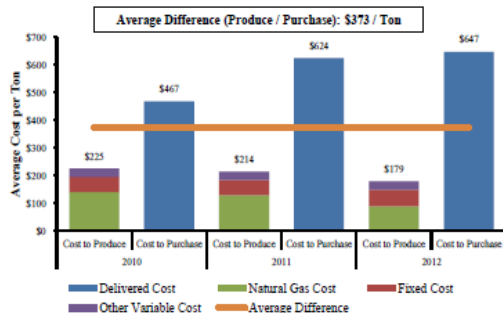
<i>Dollars in Millions</i>	2013 - 2015 (1)	
Chemical		
Nitric Acid Plant (EDC)	-	120
Ammonia Plant (EDC)		270
Infrastructure (EDC)		22
Ammonia Converter (Pryor)		20
Other (reliability, upgrades, growth, environmental, maintenance)		168
Total Chemical		600

(1) Estimates of planned capital expenditure amounts and timing are based on information available at the time of this presentation, are subject to change, and include amounts invested to date for various projects.

El Dorado Ammonia Plant Should Reduce Production Costs

Reduced Production Costs

- Will change with market conditions



Additional Capacity

- Currently use \approx 220,000 TPY
- Planned capacity \approx 375,000 TPY
- Additional capacity \approx 155,000 TPY

Access to Ammonia Pipeline Provides Efficient Access to Market

El Dorado Nitric Acid Plant Will Increase Capacity and Operating Efficiencies

Additional Capacity

- DSN capacity was \approx 90,000 TPY
- Weatherly capacity \approx 370,000 TPY
- Additional capacity \approx 280,000 TPY

Operating Efficiencies

- Higher ammonia conversion rates
- Higher energy efficiency
- Lower maintenance costs
- Higher reliability

Pryor Ammonia Converter Plant Eliminated Bottleneck and Increased Capacity

Additional Capacity

- Previous capacity was \approx 500 TPD
- New capacity \approx 700 TPD
- Additional capacity \approx 66,000 TPY
- Higher energy efficiency and reliability

"...the capital investments in the El Dorado facility, once complete, are expected to contribute approximately \$90 to \$100 million of incremental annual EBITDA, based on anticipated market conditions."

EBITDA Range
 From To
(in millions)

Beginning during 2016:

• Expected Operating Income \$ 70 \$ 80

Plus:

Depreciation and Amortization 20 20

• Expected EBITDA \$ 90 \$ 100

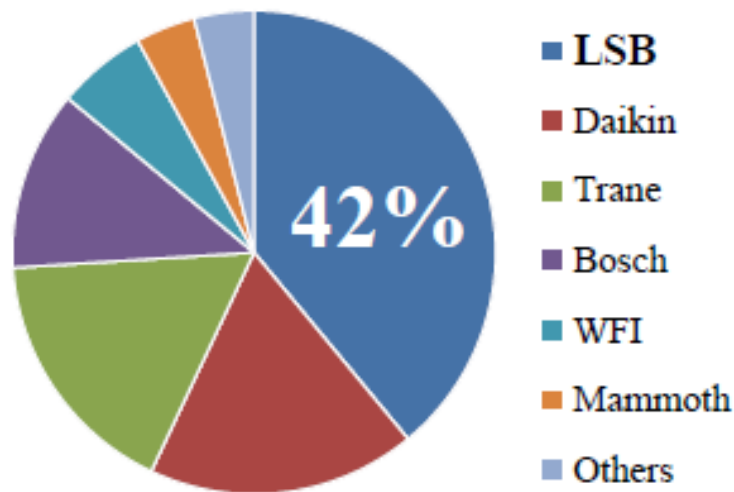
Source: LSB Q3 2013 Presentation, LSB Letter to Shareholders 1/21/2014

ROBOTTI
 & COMPANY ADVISORS, LLC

Climate Control Segment

- Manufactures and sells a broad range of HVAC products to commercial, institutional, and residential new construction, renovation and replacement with a particular focus on geothermal and water source heat pumps.

Leading Market Share



LSB Climate Control Business market shares are according to Air Conditioning, Heating and Refrigeration Institute as of 6-30-13. Market shares of competitors are estimates.

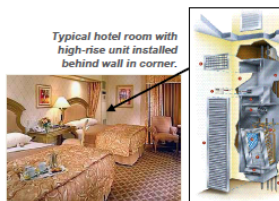
- Leading market share in core niche products
- Leader in geothermal HVAC technology.
- Thousands of premier installations and over four million units installed.

Climate Control Segment

Hydronic Fan Coils



- Leading 32% share
- Energy efficient small air handlers
- Used in central systems – commercial and institutional
- OEM to Carrier®



Modular Chillers

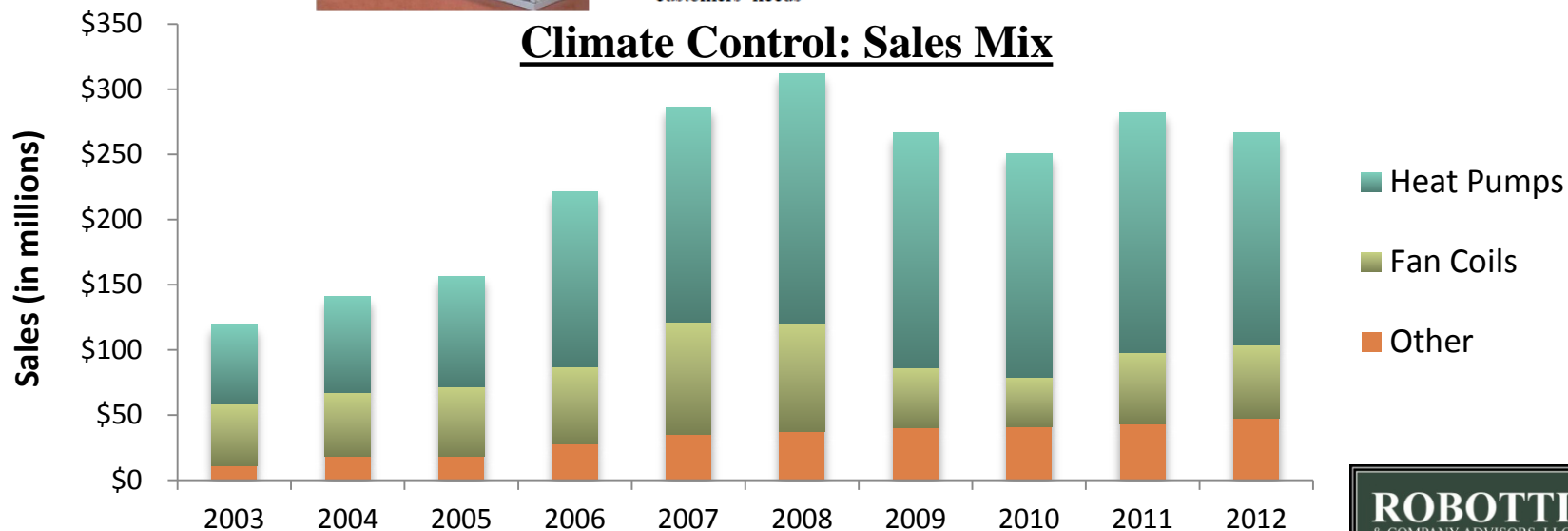
Geothermal Heat Pump, Water Cooled, and Air Cooled

- Large U.S. market (approx. \$1.0 billion)
- Used in central systems with fan coils
- Great for new construction & replacement



Large Custom Air Handlers

- Large U.S. market (approx. \$500 million)
- Healthcare, industrial, pharmaceutical, commercial and institutional uses
- Available with many green features to suit customers' needs



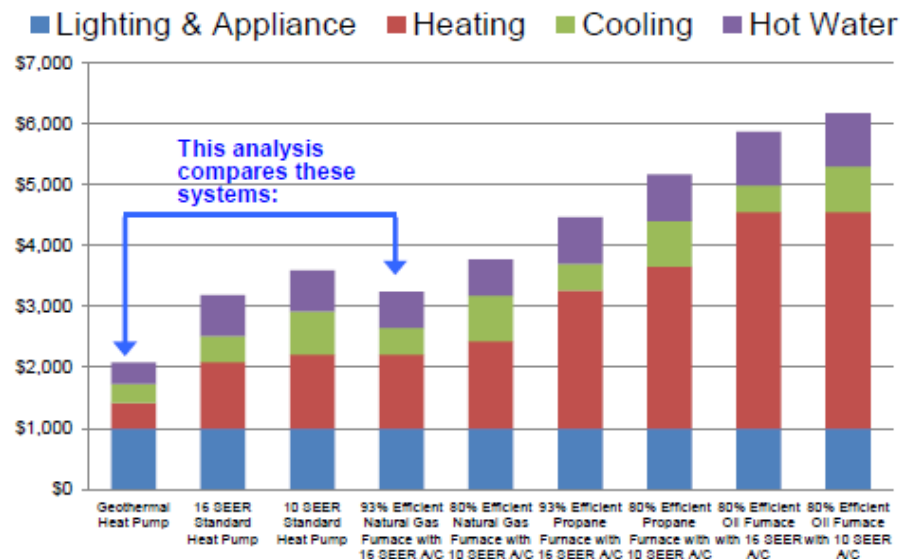
Climate Control Value Proposition

Typical GHP Costs and Savings

For a GHP System in a 2,500 sq. ft. new house in St. Louis, MO (typical middle America)

Installed Cost of a 4 ton GHP System = \$6,000 per ton (12,000 Btu/ton).

System Operating Cost Comparison GHP vs. Conventional Systems



Note: System installed costs are different throughout the U.S due to varying local conditions and labor costs. Savings vary due to weather conditions, user preferences, and local utility rates. Costs and savings in St. Louis are estimates and subject to change.

Payback (GHP vs. Hi-Eff Gas Furn+AC)

Installed cost of GHP	\$24,000
Less: 30% Fed tax credit	(7,200)
GHP cost after credit	16,800
Cost for Hi-Eff Gas + AC	(12,000)
GHP premium cost	4,800
Annual Energy Savings	\$1,162
Payback in Years	4.1

Positive Cash Flow

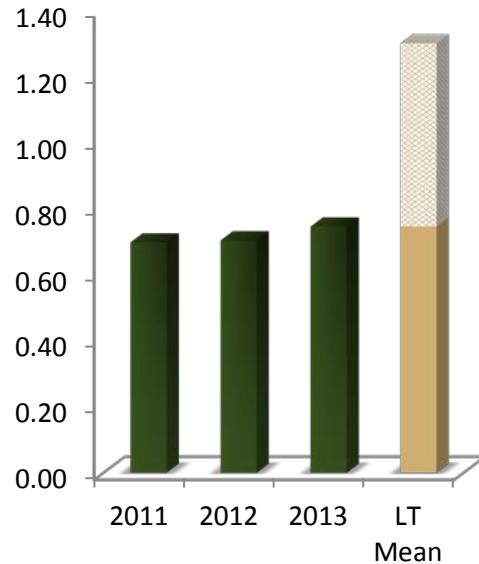
Annual Energy Savings	\$1,162
Annual P&I on GHP Premium (5% int. – 30 yrs.)	(309)
Annual Cash Savings	\$853

Demand Drivers

Commercial Starts

(billion square feet)

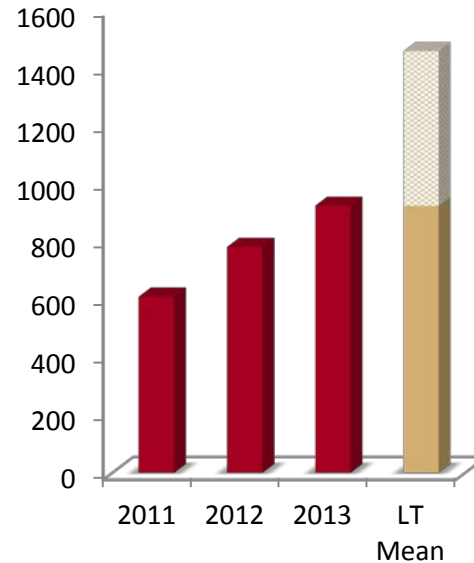
*LT Mean from 1976



Residential Starts

(millions)

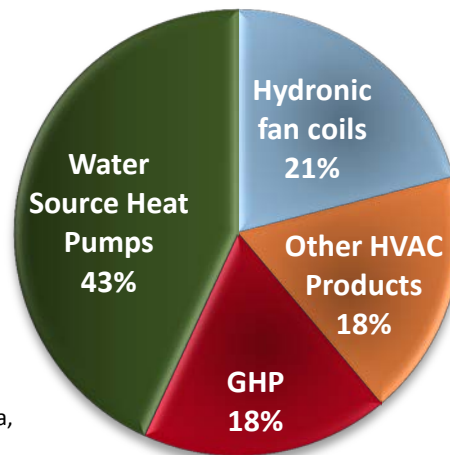
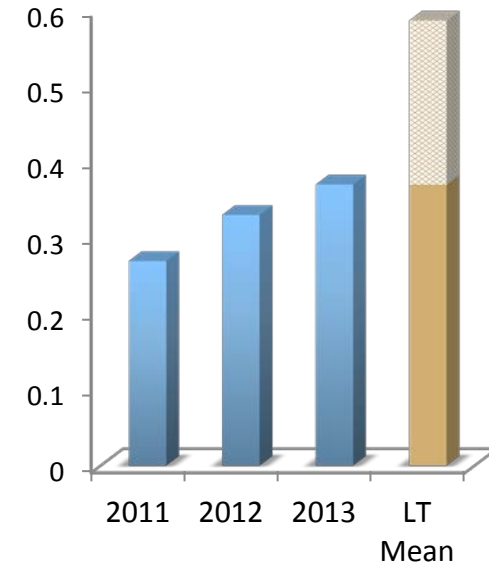
*LT Mean from 1959



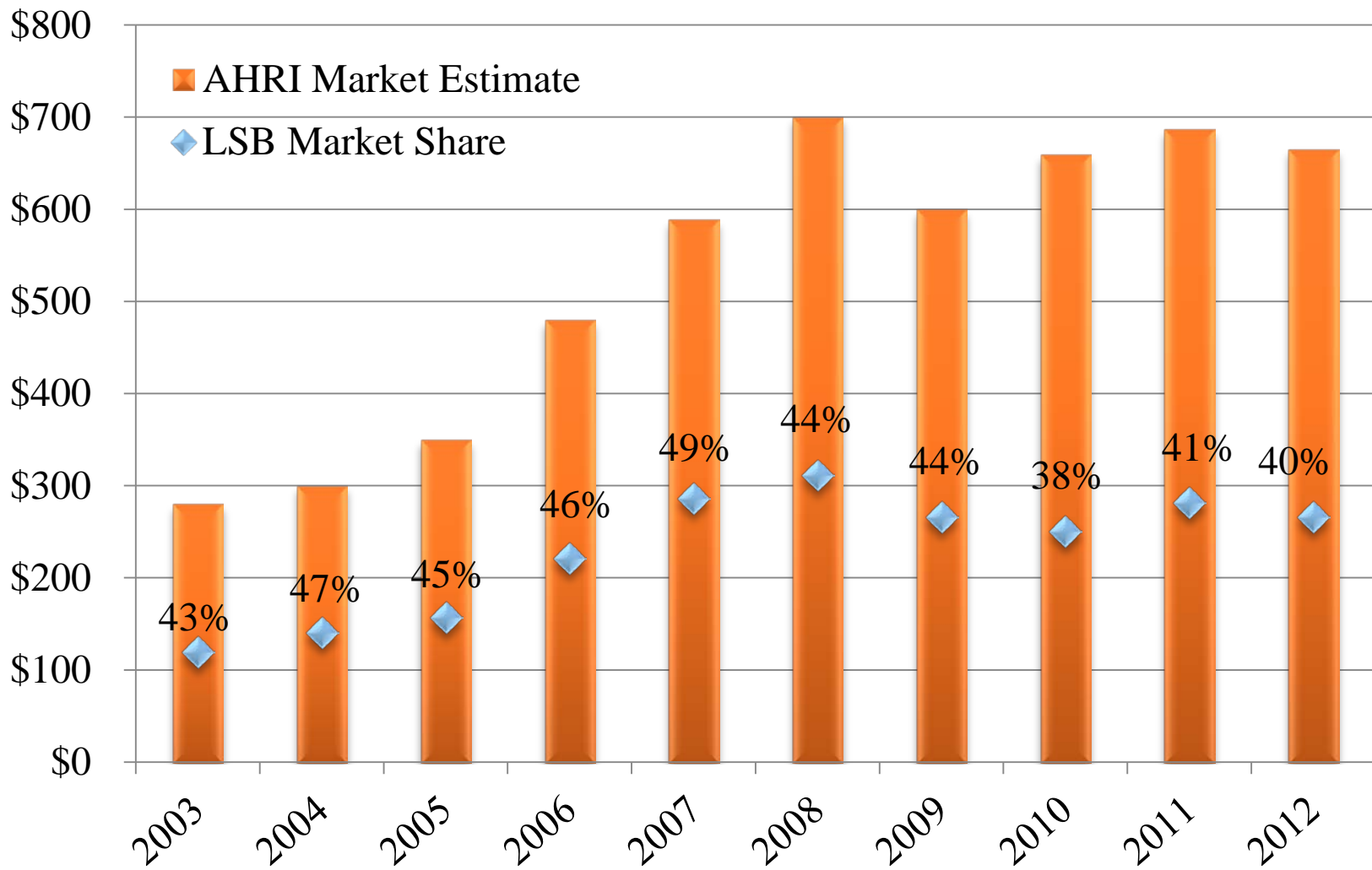
Hotel Starts

(billion square feet)

*LT Mean from 1993

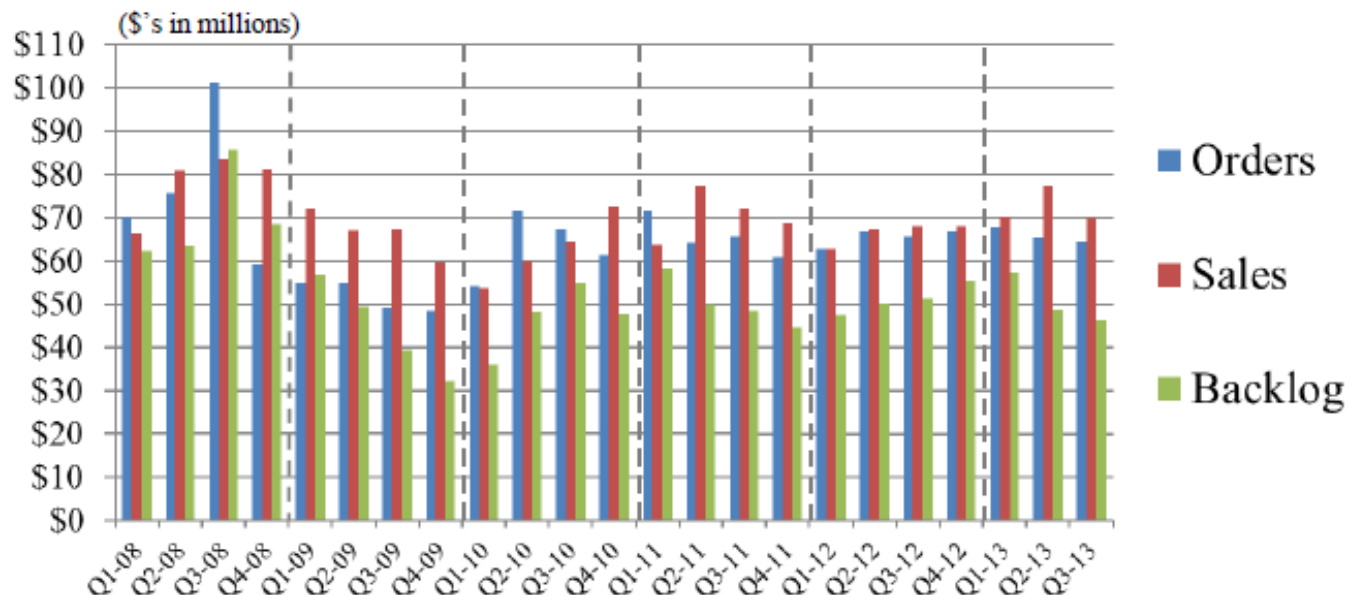


Heat Pump Market Share



*Data Taken from LSB presentations and annual reports and AHRI historical data

Climate Control Orders, Sales & Backlog



Changes from 2012 to 2013	Commercial & Institutional	Single Family Residential	Total
Q3 New Orders	(1%)	(3%)	(2%)
Q3 Sales	1%	10%	3%
Nine Months Orders	1%	2%	1%
Nine Months Sales	12%	0%	10%
Ending Backlog at 9-30	(11%)	9%	(10%)

Management

- LSB was founded by current CEO and Chairman Jack Golsen in 1969.
- Barry Golsen (Jack's son) currently serves as a director (Vice Chairman), President and Chief Operating Officer. Barry joined the company in 1978.
- Jack, Barry, Steven Golson (COO, Climate Control and Jack's son) and family controlled investment vehicle SBL Corp own approximately 12.7% of LSB's outstanding shares.



Jack and Barry Golsen (source: www.newsok.com)

- The board of directors and management team owns roughly 19% of the outstanding shares, including convertible preferred stock.

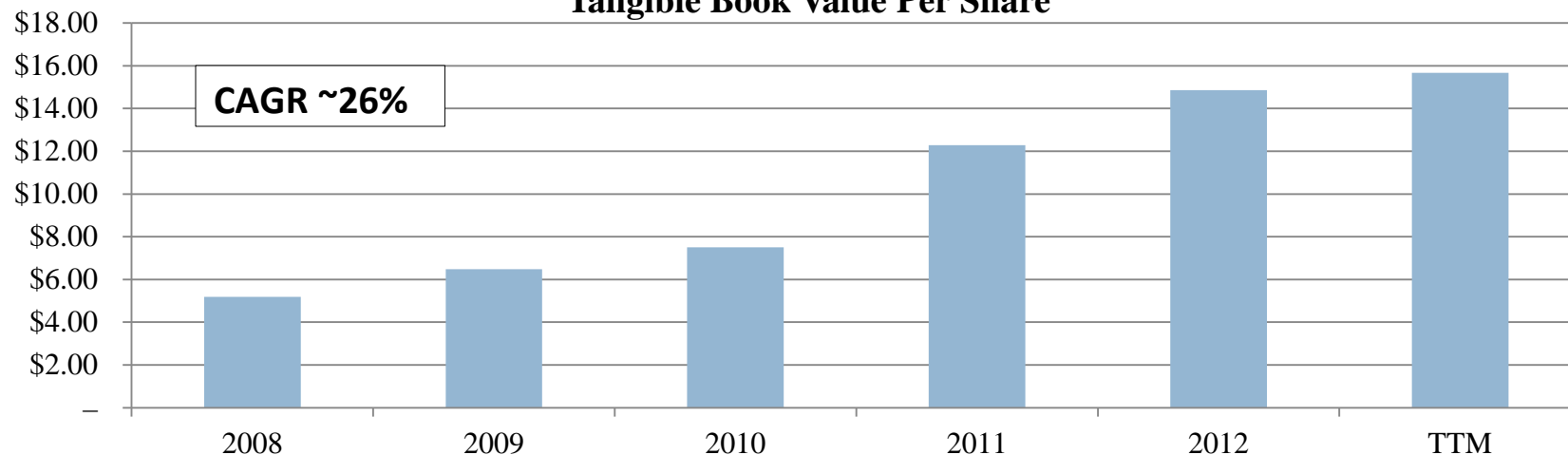
Source: Capital IQ, LSB Letter to Shareholders 1/21/2014

LSB Stock Price / Tangible Book Value

LSB Industries Price Chart 1/1/2008 - Present

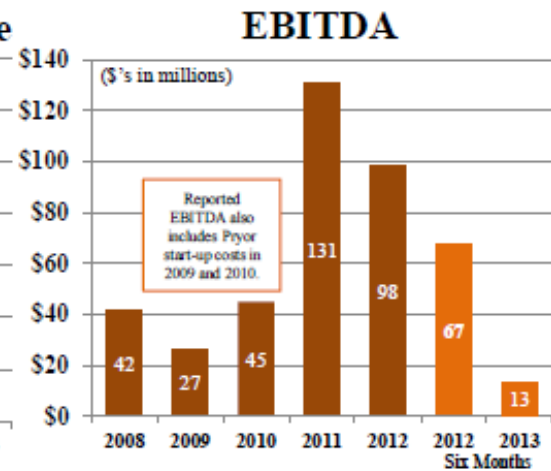
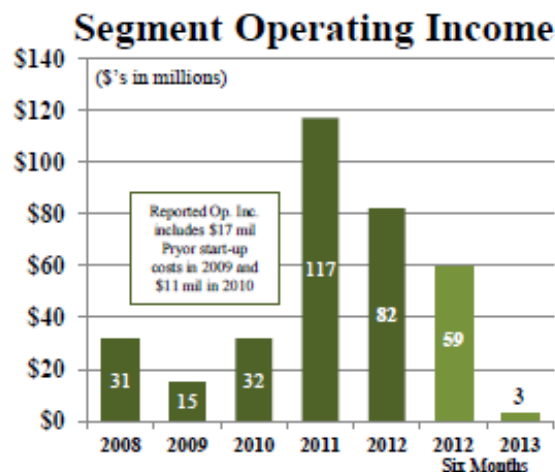
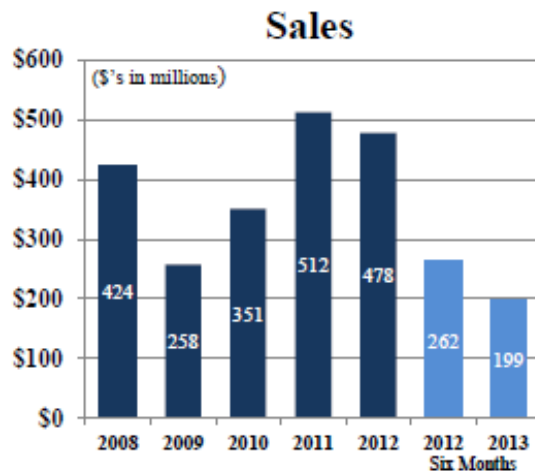


Tangible Book Value Per Share

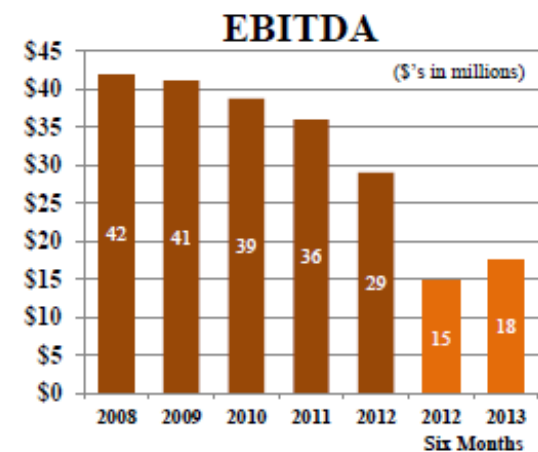
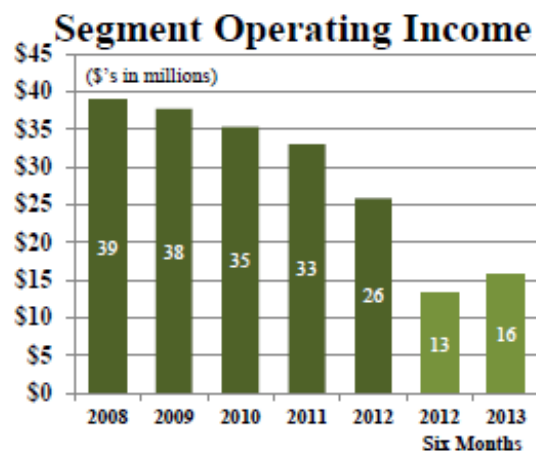
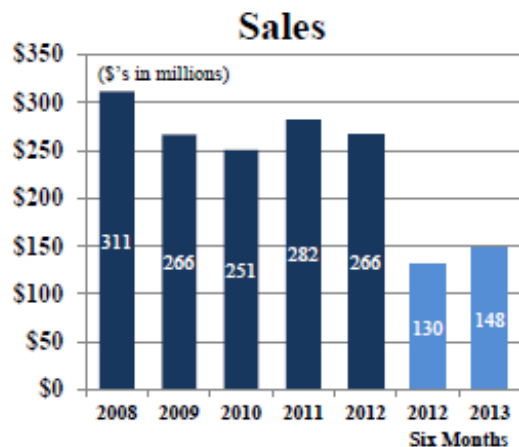


Earning Power

Chemical:



Climate Control:



Capital Expenditure Plan

<i>Dollars in Millions</i>	2013 - 2015 (1)
Chemical	
Nitric Acid Plant (EDC)	- 120
Ammonia Plant (EDC)	270
Infrastructure (EDC)	22
Ammonia Converter (Pryor)	20
Other (reliability, upgrades, growth, environmental, maintenance)	168
Total Chemical	600
Climate Control	
New Equipment, upgrades	17
New Koax Facility	8
Maintenance	15
Total Climate Control	40
Other	10
Total Capital Expenditures	650

(1) Estimates of planned capital expenditure amounts and timing are based on information available at the time of this presentation, are subject to change, and include amounts invested to date for various projects.

Recent Letters

Engine Capital Open Letter to the Board of LSB

Engine Capital Issues Open Letter to the Board of LSB Industries

Critical of Corporate Governance and Corporate Structure
Seeks Change in Board Composition, Sale/Spin of Climate Control Business, MLP of Certain Chemical Assets



Engine Capital LP
December 30, 2013 8:00 AM



NEW YORK--(BUSINESS WIRE)--

Engine Capital LP ("Engine Capital"), a shareholder of LSB Industries, Inc. ("LSB") (the "Company"), released an open letter it sent to the Board of Directors of the Company, critical of the Company's corporate governance, corporate structure, communication with shareholders and repeated operational failures. Engine Capital expressed its belief that the Company's inherent value far exceeds its current stock price, and that such unrealized value could be unlocked through improvement in the composition of the Board, a sale or spin-off of the Company's climate control business, and conversion of a portion of the Company's chemical assets into a publicly-traded master limited partnership.

Full text of the open letter follows:

Engine Capital LP
1370 Broadway, 5th Floor
New York, NY 10018
(212) 321-0048

December 30, 2013

The Board of Directors
c/o Jack Golsen, CEO and Chairman
LSB Industries, Inc.
16 S. Pennsylvania Avenue
Oklahoma City, OK 73107-7024

Dear Board Members:

Engine Capital LP, together with its affiliates ("Engine"), is a shareholder of LSB Industries, Inc. ("LSB" or "LXU" or the "Company"). LSB represents a significant investment for Engine. We invested in LSB because we think that the Company is significantly undervalued and there are opportunities within the control of management and the Board to increase shareholder value substantially. In particular, we think that the Board would be significantly strengthened by adding a number of new members with relevant backgrounds in chemical asset operations, climate control, and corporate finance, and with no ties to the Golsen family. We also urge the Company to establish a special committee of truly independent directors to analyze the Company's strategic alternatives to maximize value, including separating the climate control business from the chemical assets and converting certain of the chemical assets into an MLP structure.

As you probably know, over the last few weeks, we have had discussions with your President and Chief

LSB Open Letter to Shareholders

EX-99-1 Letter to Shareholders from EX-99-1

Exhibit 99.1

LSB Industries Issues Open Letter to Shareholders

OKLAHOMA CITY -- Jan. 21, 2014 -- LSB Industries, Inc. ("LSB") today announced that its Board of Directors, in consultation with independent financial and legal advisors, has reviewed the open letter issued by Engine Capital LP ("Engine Capital") and has issued its response to LSB shareholders. The letter discusses the following topics:

The Board and management team have the right plan in place to deliver value to LSB shareholders.

The proposals from Engine Capital would deliver less value to LSB shareholders than the Company's plan.

The Board and management team are closely aligned with shareholders and committed to effective oversight.

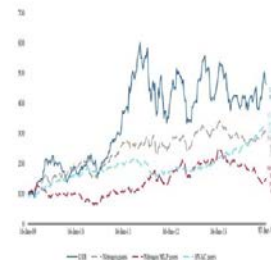
The full text of the letter from Jack E. Golsen, Chairman of the Board and Chief Executive Officer, is below:

January 21, 2014

Dear Fellow LSB Shareholder:

Your Board and management team have a proven track record of value creation. The Board has reviewed the operations of LSB's business and has delivered solid shareholder returns. Our two core Chemical and Climate Control businesses are positioned to benefit from strong demand in the markets they serve over the coming years. Demand for fertilizers is expected to remain steady, mainly as a result of population growth, as increasing global demand for growing natural food crops as people consume more protein and the use of bio-fuels. Nitrogen fertilizers, in particular, are expected to experience robust and sustained demand because they must be applied each year and have a direct impact on farmers' yields, creating an economic incentive for farmers to increase the amount of fertilizer used. LSB's Climate Control business is expected to benefit from the growth in commercial and residential construction as an improving economy. Your Board and management team believe that over three-year operating and capital plan for our Chemical and Climate Control businesses will significantly increase EBITDA.

LSB's stock price has increased by over 300% over the last five years, outperforming the Company's peer groups, coming out of the financial crisis.



The Board and management team believe that we have the right plan in place to deliver value to LSB shareholders.

The Company's existing assets in LSB's Chemical business necessary to drive growth and value creation, and deliver growth to LSB to capitalize on favorable market dynamics. LSB's three-year capital spending plan includes:

\$250 to \$300 million for the construction and completion of an ammonia plant at the El Dorado facility - this investment will significantly increase LSB's costs and eliminate the exposure to fluctuations in the price of ammonia in the open market.

<http://finance.yahoo.com/news/engine-capital-issues-open-letter-130000424.html>

<http://www.sec.gov/Archives/edgar/data/60714/000089882214000037/lettertoshareholders.htm>

Disclosure: Ownership Information

<u>Disclosures</u>	LSB Industries, Inc. (NYSE: LXU)
Robert Robotti and/or members of their households have a financial interest in the following securities	Yes
Robotti & Company or its affiliates beneficially own common equity of the following securities	Yes
Robotti & Company or its affiliates beneficially own 1% or more of any class of common equity of the following securities	Yes
Robert Robotti serves as a Director or Officer or Advisory Board Member of the following securities.	No

As of the date of this presentation, Robotti & Company Advisors, LLC and/or its affiliates owns shares of LSB Industries and does not have any current intention to exit these positions.

Companies have been chosen solely as a case study to illustrate the investment process and approach of Robotti & Company Advisors, LLC. This information should not be interpreted as a performance record or as an indication of future performance results.