

MOI Global Best Ideas 2021

Building an Investment Case

Bob Robotti
Robotti & Company Advisors

January 13, 2021

Traditional Value Investor Bias

Investing **Checklist**

- Is this company cyclical?
- Is the business tied to commodity prices?
- Is the balance sheet levered?

“If you want to have a better performance than the crowd, you must do things differently from the crowd.”

Sir John Templeton



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.

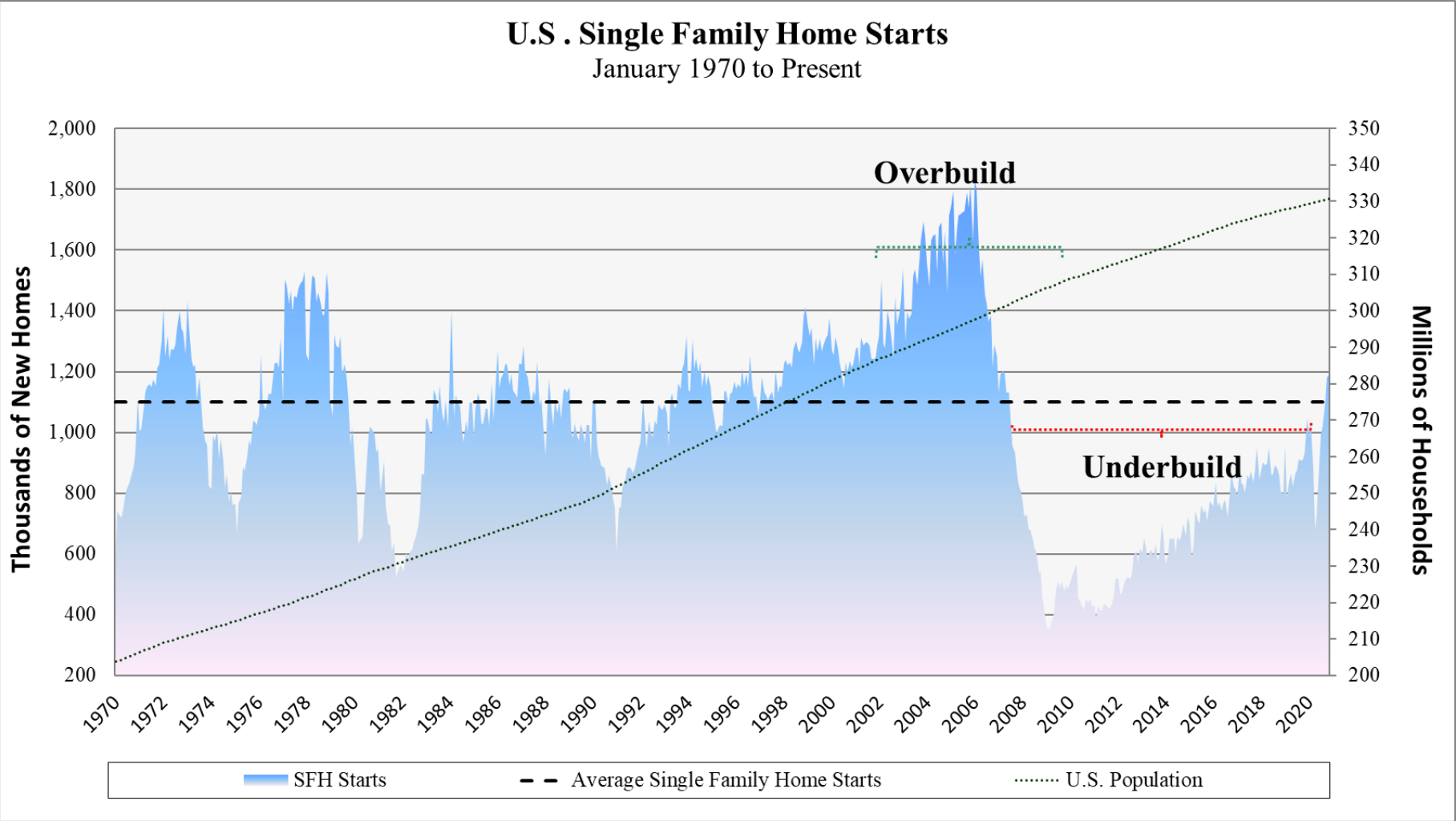
Leads Us To

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.

Capital Cycle: Real-Time Case Study



Source: Federal Reserve Bank of St. Louis, Robotti & Company Advisors Estimates

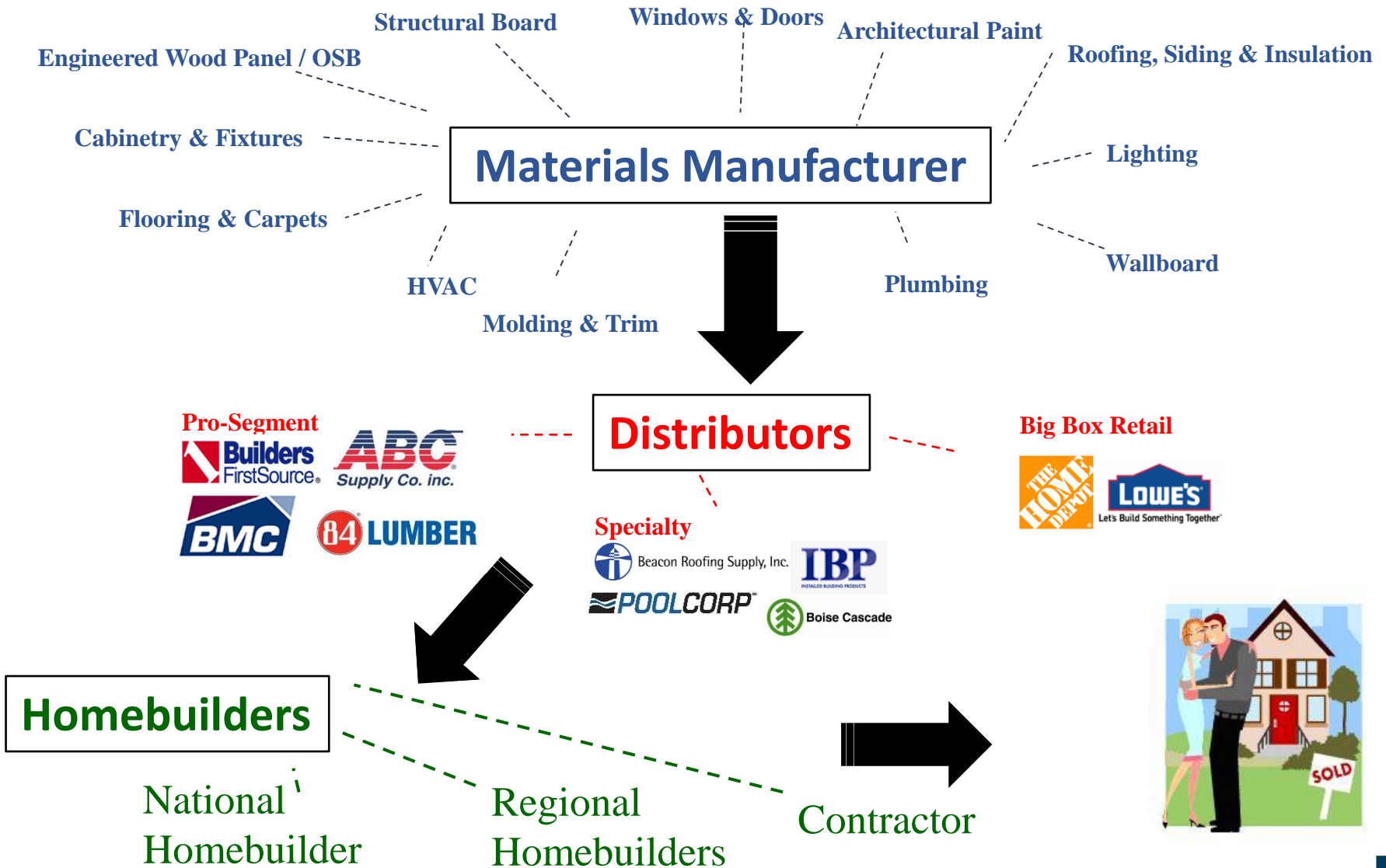


2010 – 2019: A Unique Decade

- Weakest recovery of all-time, so weak it was the only decade without a recession.
 - Government intervention led to the lowest interest rate environment in recorded history.
 - While 2020 was different than any year of our lifetime, economics and securities markets continued their decade(s) long trend.
- Is this the mythical “*New Normal*?”
 - Have governments finally figured out how to eliminate inflation?
 - Interest rates appear to be poised to stay ultra low forever. Will they?



A Map of the Homebuilding Industry



Builders FirstSource, Inc. (BLDR)

- Builders FirstSource is a leading supplier of building products, prefabricated components and value-added services primarily for new residential construction and repair & remodeling.

Financial Summary			
Price:	\$39.50		
Dil Shrs:	207.7		
Market Cap	8,204	52 Week High	\$42.84
LT Debt	1,969	52 Week Low	\$9.00
Cash	637		
Enterprise Value	9,536		

Prices as of 1/12/21 in \$ millions (except share price)

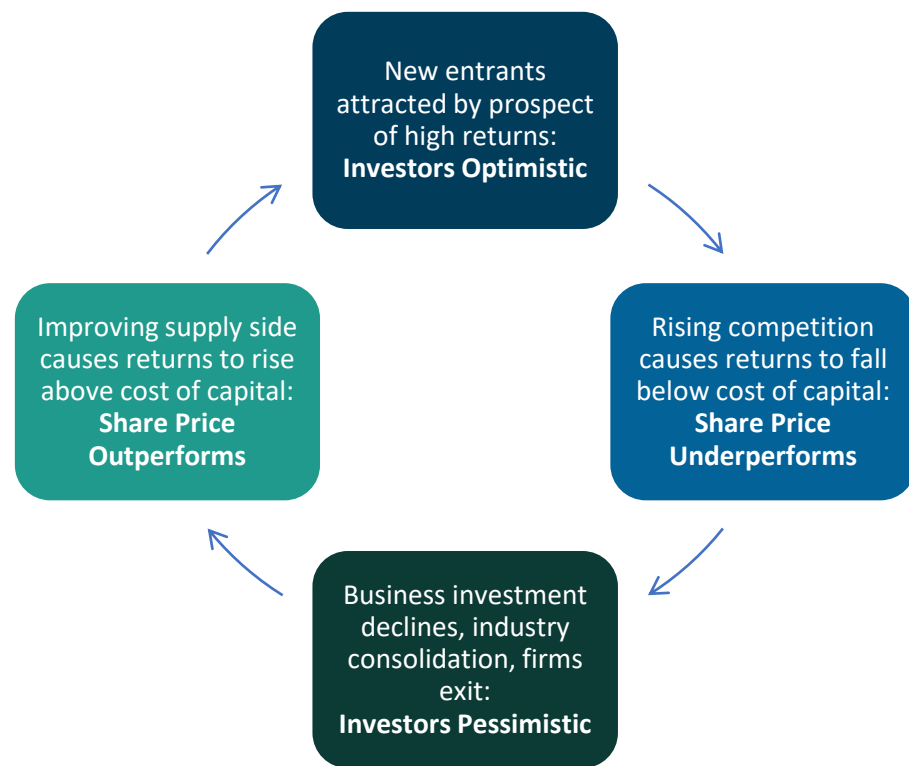
- With the second largest North American LBM distribution network serving the professional market BLDR benefits from regional economies of scale.
- After a period of industry consolidation, expense reduction and balance sheet improvement BLDR is poised to benefit from the reversion of single family home starts to a normal level.
- We believe BLDR trades at a low single-digit multiple of normalized earnings power.



Understanding the Value of Capital Cycles

“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)



Economic cycles resemble Schumpeter’s process of creative destruction.

Source: Capital Returns, Edward Chancellor, editor (2015)

Cyclical Downturns: A Bumpy, Yet Cathartic Ride

- Poor competitors go out of business or are acquired
- Consolidation
- Recapitalization
- Elimination of unprofitable assets
- Strong competitors take advantage of undervalued opportunities

Robotti & Company Advisors, LLC – Q3 2014 Letter
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When stock prices fall sharply, we often find opportunity - *so long as our conviction in our long-term view remains solid*. Opportunity is exactly what we see today in a number of our portfolio investments. This holds particularly true for our housing-related investments, including Ainsworth Lumber, Norbord, Gibraltar Industries, Cavco Industries and UMH Properties. Builders FirstSource provides us with a timely example to illustrate what we mean.

For the better part of 2013, investors were feeling confident about a recovery in the domestic housing markets. News headlines echoed this optimism and by November 2013, single-family housing starts reached an annualized pace of 710,000, the highest level since March 2008.

But the recovery did not continue on a straight path up. Economies rarely progress in a linear fashion – a fact that does not sit well with many academic theories and formulas. Single-family housing starts dropped 4.9% in December and another 13.6% in January, falling to an annualized level of 583,000 units and rattling investor confidence¹.

In early 2014, shares of Builders FirstSource hit a 52-week-high of \$9.40. By the end of September, less than six months later, Builders FirstSource's stock dropped 45% marking a 52-week low of \$5.10². A prescient headline from CNBC.com on September 22 read "Investors Leaving Housing High and Dry." Clearly, investors are running for the exits. The obvious question is: Should we be running along with everyone else?

Housing in 'Early Stages' of Multiyear Recovery: Trulia

Paul Toscano | @ToscanoPaul
Wednesday, 1 May 2013 | 1:45 PM ET

CNBC

Confidence at Five-Year High as U.S. Housing Climbs: Economy

By Inessa Smolok and Lomena Winkler | May 29, 2013 4:00 PM ET

Bloomberg

Home-builder confidence hits seven-year high

Published June 17, 2013 10:56 am ET

Marketwatch

Bloomberg Businessweek Markets & Finance

The Housing Rebound Stalls

By John Gittelsohn and Prashant Goyal | May 01, 2014

Housing market could be facing another bubble: Shiller

Tuesday, 31 Dec 2013 | 9:54 AM ET

CNBC

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Stock Building Supply Merger Creates a \$1.5 Billion Company

LOU WHITEMAN · JUN 3, 2015 11:53 AM EDT

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BUSINESS

Builders FirstSource to Buy ProBuild Holdings for \$1.63 Billion

Deal will position company to capitalize on the housing market recovery

By *Chelsey Dulaney*
Updated April 13, 2015 8:40 am ET

THE WALL STREET JOURNAL.

Norbord to Buy Ainsworth Lumber in All-Stock Deal

Transaction Represents 15% Premium to Ainsworth's 20-Day Volume Weighted Average Price

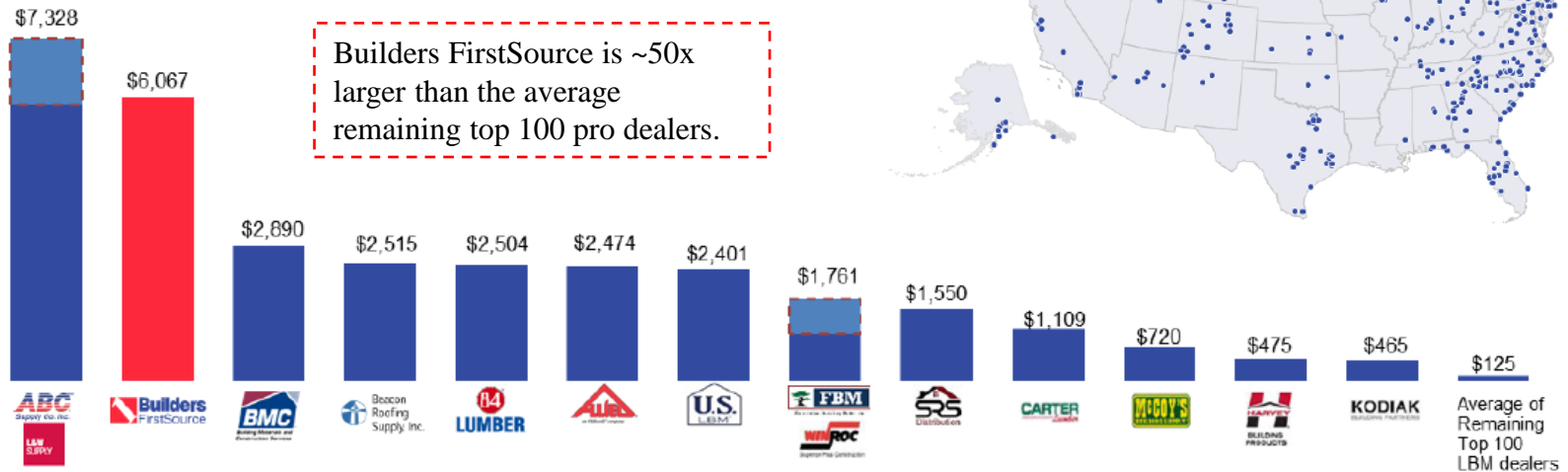
By *Carolyn King*
Dec. 8, 2014 8:59 am ET

Consolidation Continues: Competitive Landscape 2015

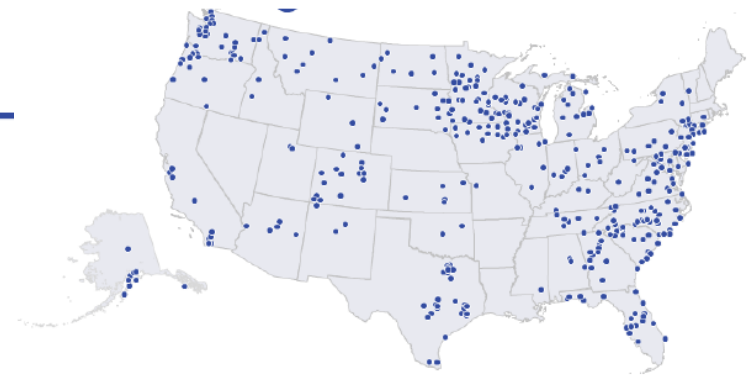
- The 2015 ProBuild Acquisition created ~\$100 million of synergies through procurement savings, general & administrative cost reductions and network consolidation.
- With its leading network of distribution facilities BLDR is able to benefit from **regional economies of scale**.

2015 Pro Forma Sales of Top Distribution Pro Dealers

(\$ in mm)



Broad U.S. coverage with 400 locations in 40 states



Q3 2020: BLDR + BMC = Four Competitors Become One

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Builders FirstSource, BMC Stock to Combine in an All-Stock Deal
By [Cara Lombardo](#)
Updated Aug. 27, 2020 7:47 am ET

The companies, which manufacture products used in residential construction, would have a combined market value of about \$5.5 billion

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1 Scale

- Expanded customer reach nationwide
- Greater economies of scale

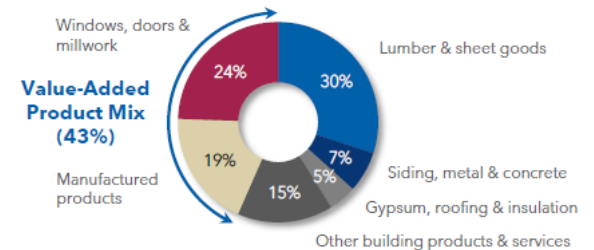
2 Depth and excellence

- Enhanced customer value proposition
- Integrated product and service offering

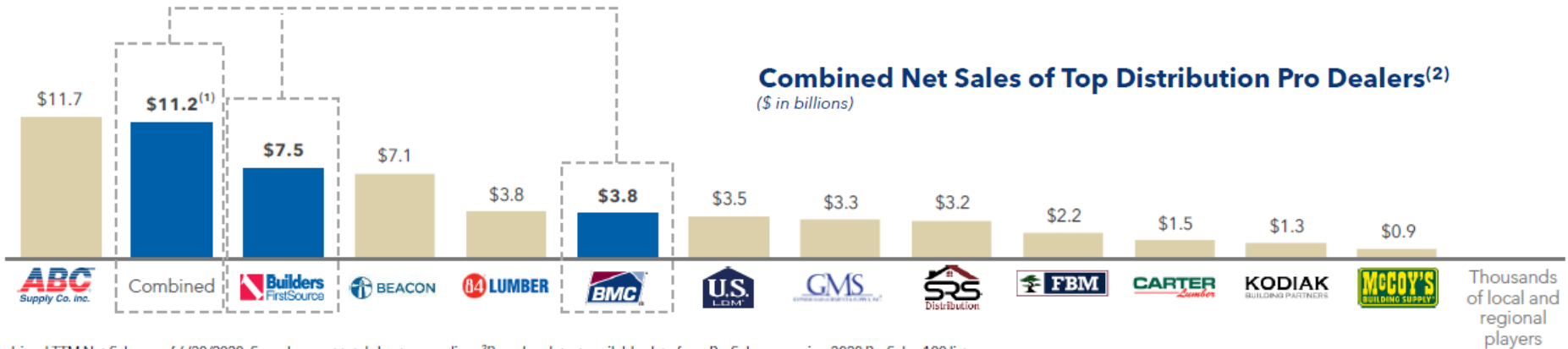
3 Diversity and range

- Exceptional geographic, customer and end market diversity
- Full suite of structural and related building products and services

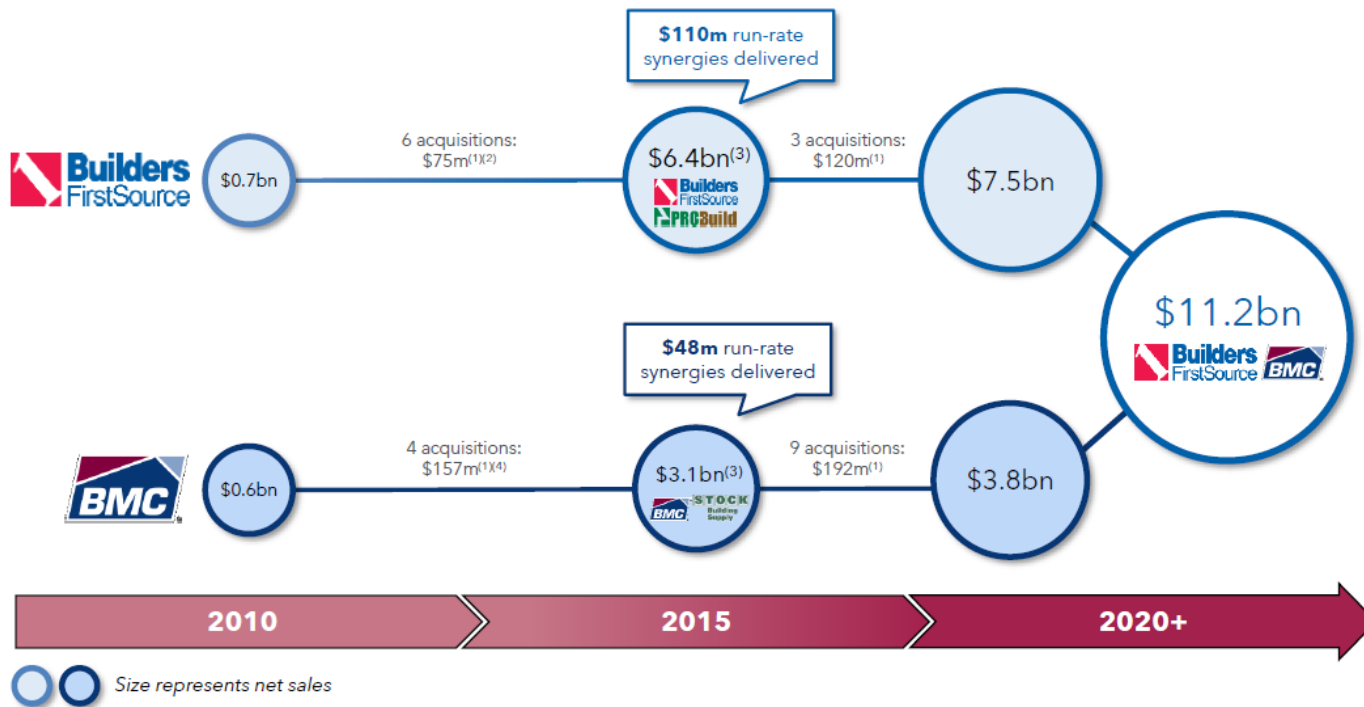
Combined Net Sales by Product⁽¹⁾



Transformative Acquisition: Competitive Landscape 2021



¹Combined TTM Net Sales as of 6/30/2020. Sum does not total due to rounding. ²Based on latest available data from ProSales magazine 2020 ProSales 100 list.



22
Total Acquisitions Completed Over the Last 10 Years Delivering Enhanced Value to Customers

17,500+
New Team Members Successfully Integrated

100%+
of Target Identified Synergy Value Delivered

Industry Consolidation

We are the fifth Largest Building Products Provider⁽¹⁾ in an Estimated \$304 Billion Industry⁽²⁾



	2007 Pro Sales (Millions)	Primary Business
1 Pro-Build	\$ 4,500.0	M
2 Stock Building Supply	4,417.0	M
3 84 Lumber Co.	3,007.0	M
4 BMHC	2,285.0	M
5 Builders FirstSource, Inc.	1,560.2	M
Total Top 5 Distributors	\$ 15,769.2	
Total Top 5 Market Share	5%	

M - Professional Dealer/Lumberyard with Manufacturing Capabilities

(1) ProSales magazine's 2007 ProSales 100 list

(2) National Association of Home Builders single family residential construction as of December 31, 2007

We are the fifth largest building products provider⁽¹⁾ in an estimated \$105 billion industry⁽²⁾

	2009 Pro Sales (Millions)	Primary Business
1 Pro-Build	\$ 2,784	M
2 Stock Building Supply	1,303	M
3 84 Lumber Co.	1,283	M
4 BMC Select	665	M
5 Builders FirstSource, Inc.	664	M
Total Top 5 Distributors	\$ 6,699	
Total Top 5 Market Share	6%	

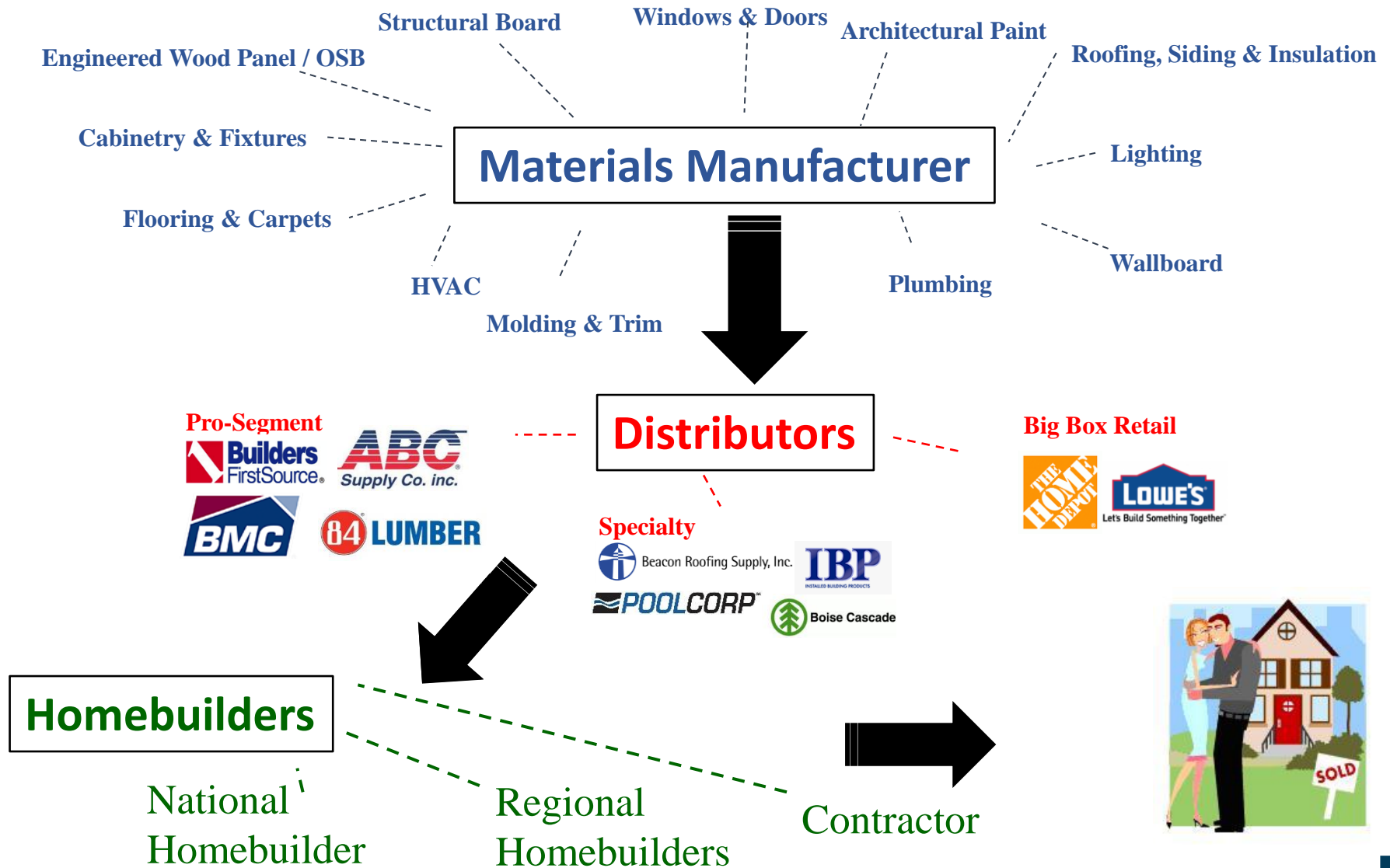
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Active Engagement Provides Deeper View of an Industry



- Norbord is the world's largest producer of oriented strand board (OSB) with 14 mills in North America and 3 mills in the UK and Europe.
- As the leading low-cost producer Norbord is well positioned to take advantage of the North America's continued housing recovery.
- A focus on value-added and specialty products, favorable geographic exposure and a history of prudent capital allocation.
- A period of industry consolidation has created favorable supply / demand dynamics that will allow for a period of above average free cash flow generation.

Financial Summary			
Price:	\$40.81	Net Debt	705
Diluted Shares	81.8	Net Debt/EBTIDA	1.4x
Market Cap	\$3,338		
LT Debt	725	Dividend Yield	2.0%
Cash	20	52 Week High	\$45.62
Enterprise Value	\$4,043	52 Week Low	\$8.92

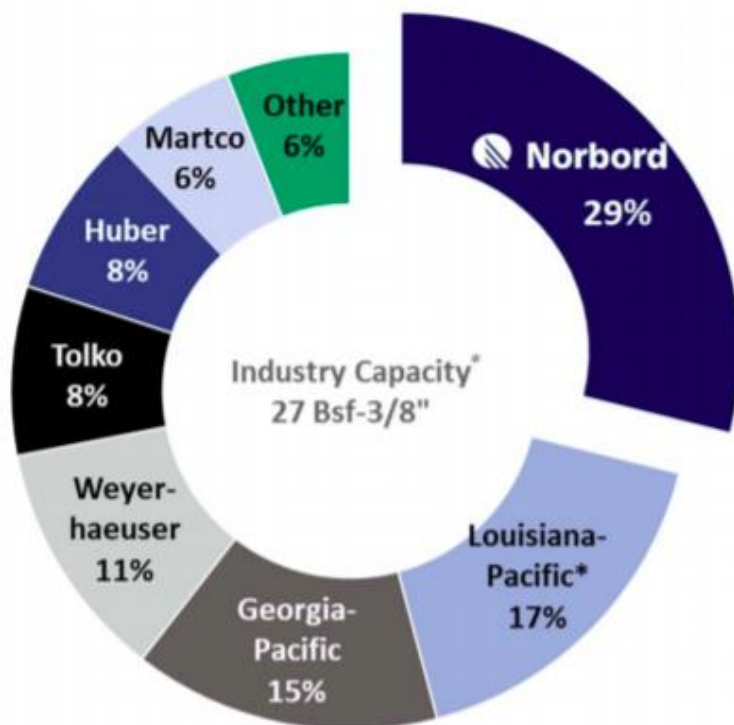
(in USD as of 1/12/21)

(Annual)	Consensus Est.			
	FY '18	FY '19	FY '20E	FY '21E
Revenue	2,424	1,731	2,339	2,427
<i>growth</i>	11.3%	(28.6%)	7.5%	3.8%
	1.5x	2.2x	1.6x	1.5x
EBITDA	724	138	806	703
margin	29.9%	8.0%	34.4%	29.0%
<i>ev/ebitda</i>	5.1x	27.0x	4.6x	5.3x
Op. Income	586	(1)	659	598
margin	24.2%	(0.1%)	28.2%	24.6%
	6.4x	na	5.7x	6.2x
Diluted EPS	\$4.27	(\$0.51)	\$5.67	\$4.84
	9.6x	na	7.2x	8.4x

Source: Norbord Financial Statements, S&P Capital IQ

Cyclical Downturns: A Cathartic Process

North American OSB Industry



In 2002 the top 5 North American Producers accounted for 69% of North American Capacity.

Pre-Housing Crisis (~2006):

- 11 OSB producers in North America
- **Top 5 = 74% market share**

Today:

- 9 OSB producers in North America
- **Top 5 = 84% market share**
- (Top 6 = 92% market share)

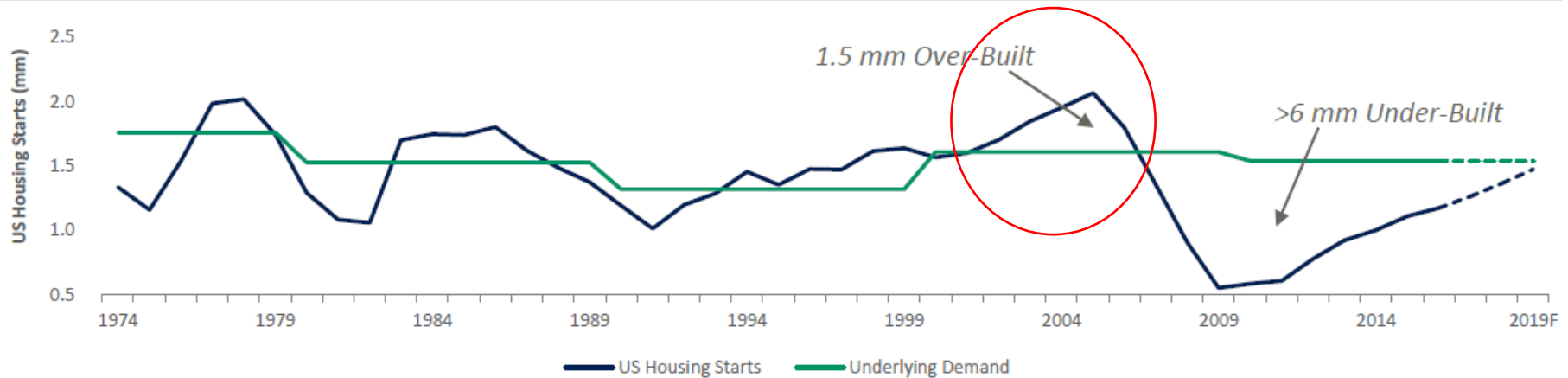
Herfindahl-Hirschman Index (HHI)

Pre-Housing Crisis HHI: 1,382

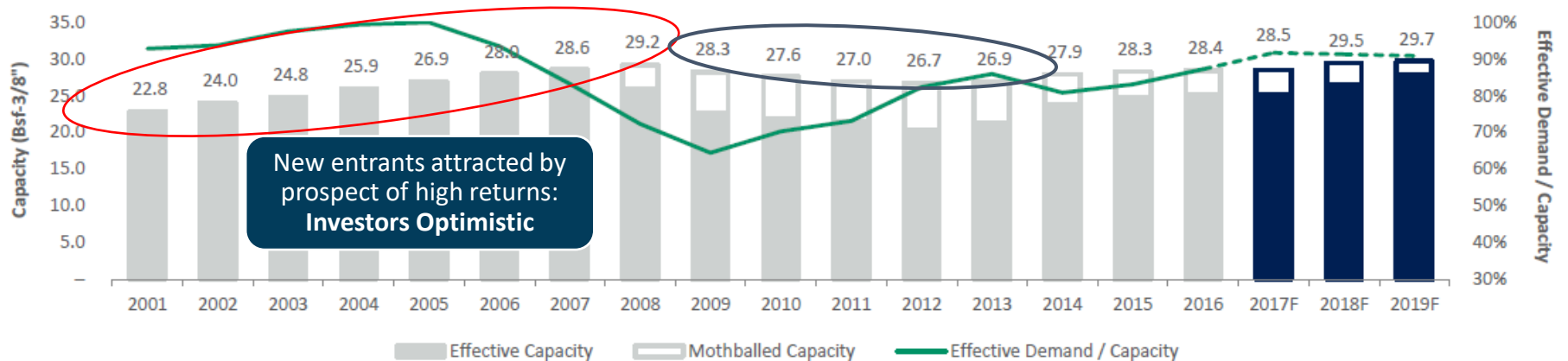
2017 HHI: 1,722

Understanding the Capital Cycle

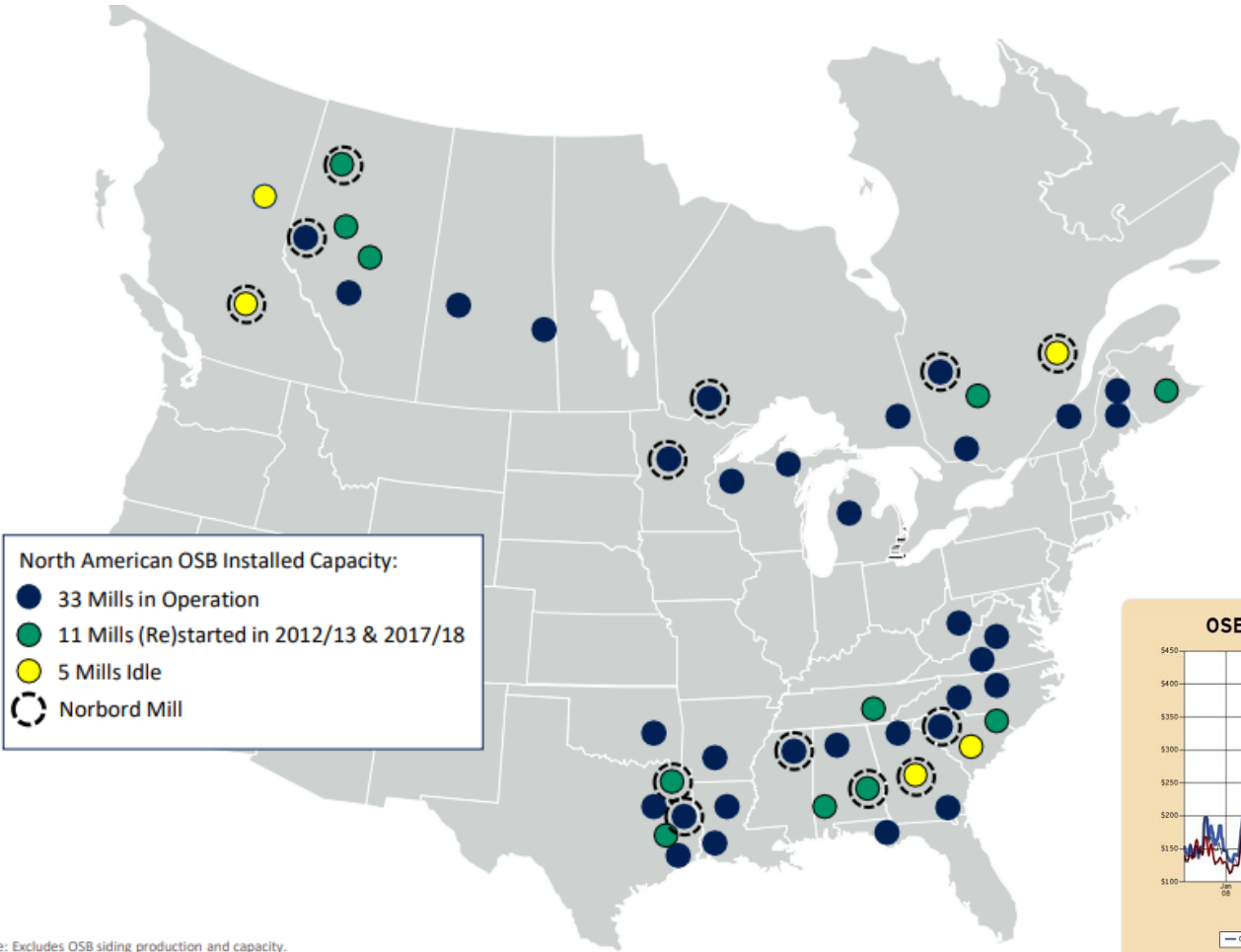
US Housing Starts and Underlying Demand



North American OSB Demand and Capacity



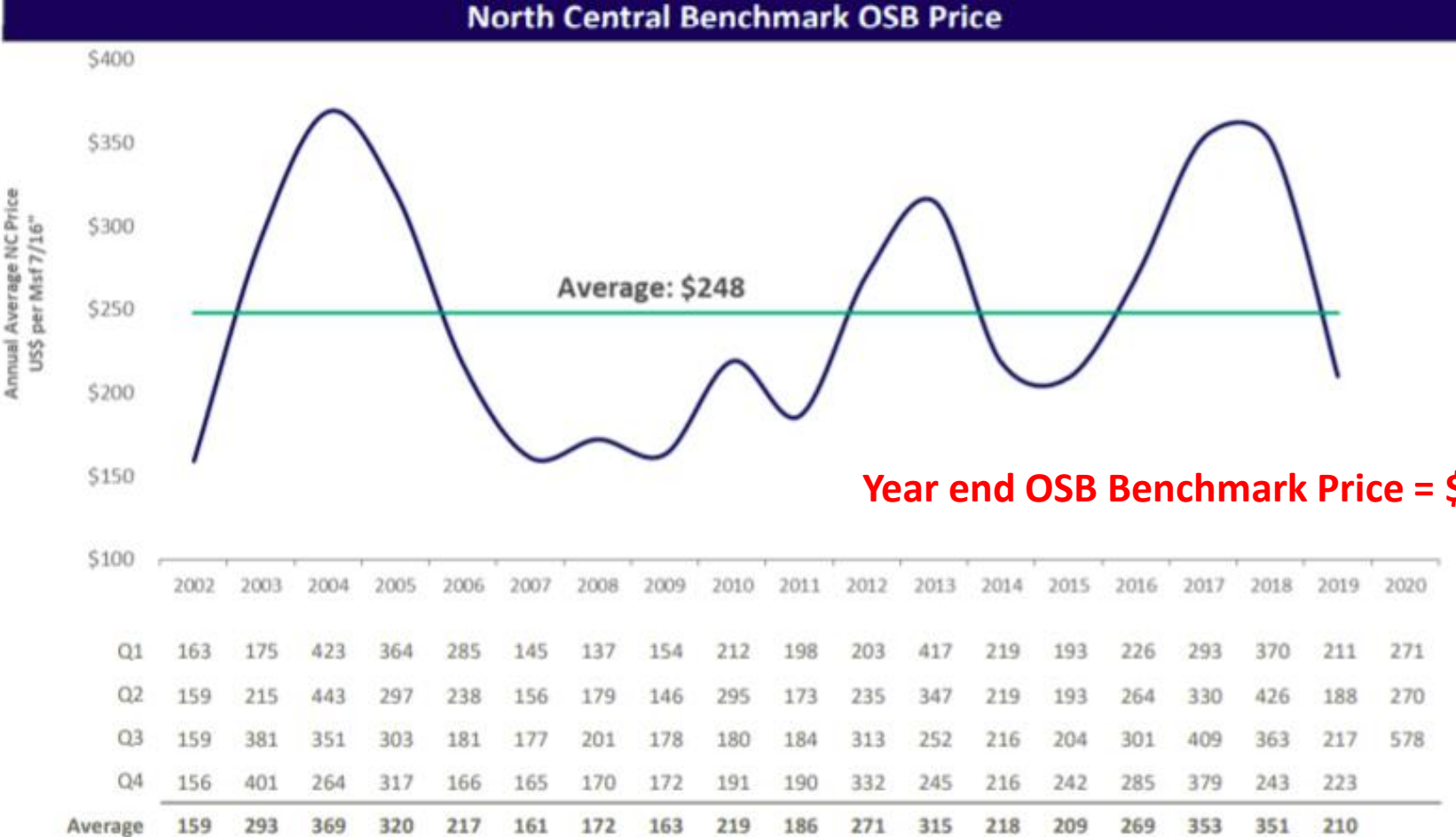
North American OSB Stated Capacity of 27 Bsf



Note: Excludes OSB siding production and capacity.
 Source: APA, company documents and other public filings



North American Benchmark OSB Prices



Source: Random Lengths

Financial Sensitivities



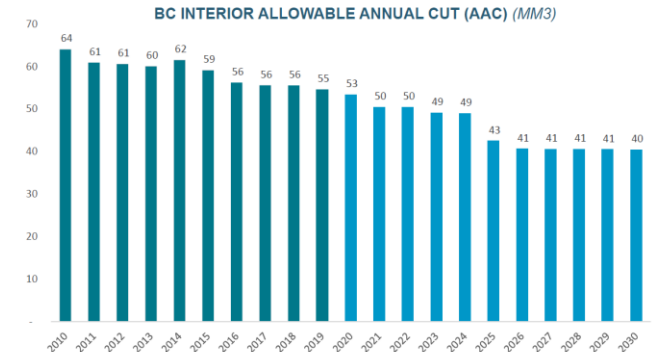
Exposure	Change	Adjusted EBITDA Impact (US\$ millions)
North American OSB ⁽¹⁾⁽²⁾	\$10 per Msf-7/16"	± \$64
European OSB	€10 per 000 m ³	± \$11

West Fraser Acquires Norbord

- On November 19th, 2020 West Fraser, a diversified wood products company, made an all-stock offer to acquire Norbord in a transaction that will value the company at \$37.78 per share. The deal should close in Q1 2021.

BC INTERIOR: REGIONAL FIBRE OUTLOOK

- Allowable Annual Cut (AAC) reductions of approximately 25% between 2019 and 2025

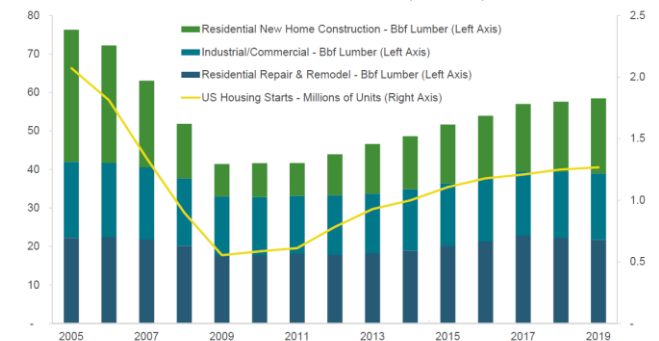


INTERFOR

Source: BC Ministry of Forests 15

LUMBER DEMAND

NORTH AMERICAN SOFTWOOD LUMBER DEMAND BY END-USE (BBF) & TOTAL US HOUSING STARTS (MILLIONS)



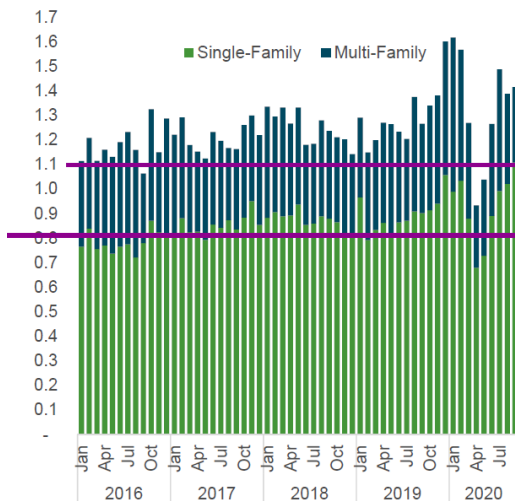
INTERFOR

Source: Forest Economic Advisors (FEA) 9

LUMBER DEMAND: KEY DRIVERS

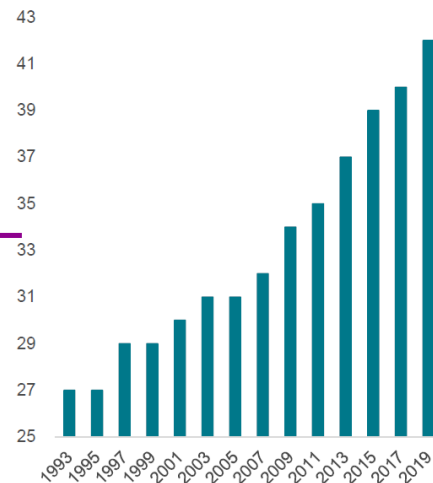
US HOUSING STARTS

(MILLIONS SEASONALLY ADJUSTED)



AGE OF US HOUSING STOCK

(MEDIAN AGE IN YEARS)

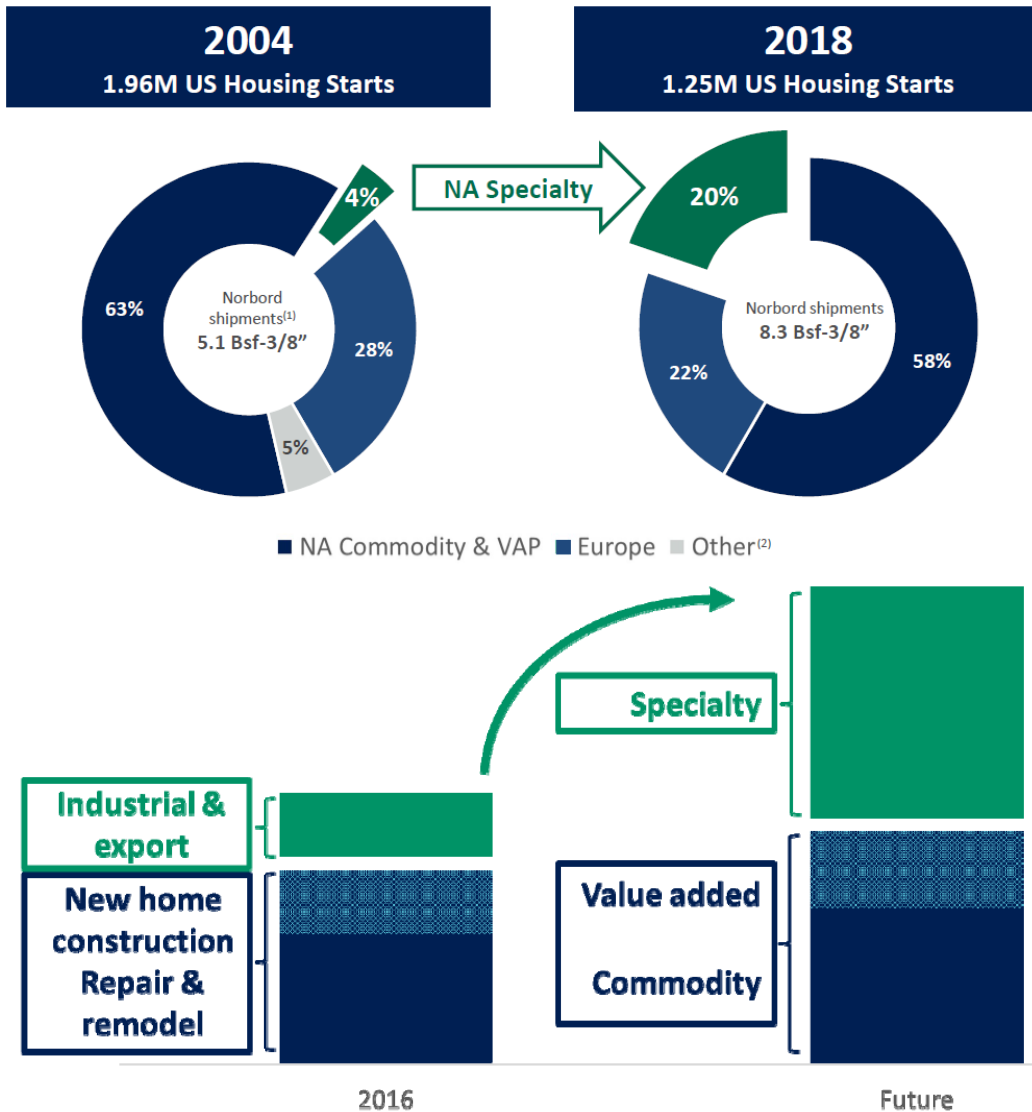


Source: US Census Bureau & Forest Economic Advisors (FEA) 10

INTERFOR



Additional Underlying Shifts: Specialty OSB



- Reduced dependence on new home construction
- Increased supply absorption means higher capacity utilization without any new growth in core homebuilding market
- More predictable, stable margins over business cycle
- Number 2 industry participant converting OSB plants to grow specialty siding business further reducing capacity

Additional Underlying Improvements: Repair & Remodel

Repair and Remodeling – Key Drivers Point to Solid Growth

✓ 2020: COVID Surge in Disposable Income/Time

DIY is an increasingly greater proportion of projects
Despite a decline in spending in 2021 as compared to 2020, we see lumber usage rate per dollar trending higher (reduced labor costs)

↻ 2021: Record Low Existing Home Inventory

Drives spending pre and post-sale ~ 5.4 million units/yr.
Generally lower existing home sales may drag down overall spend as new home sales increase

↻ Aging in Place

Mobility amongst Baby Boomers & Silent Generation Decline
Single family owners likely to resort to improvements over relocation, proportion of lumber usage likely lower

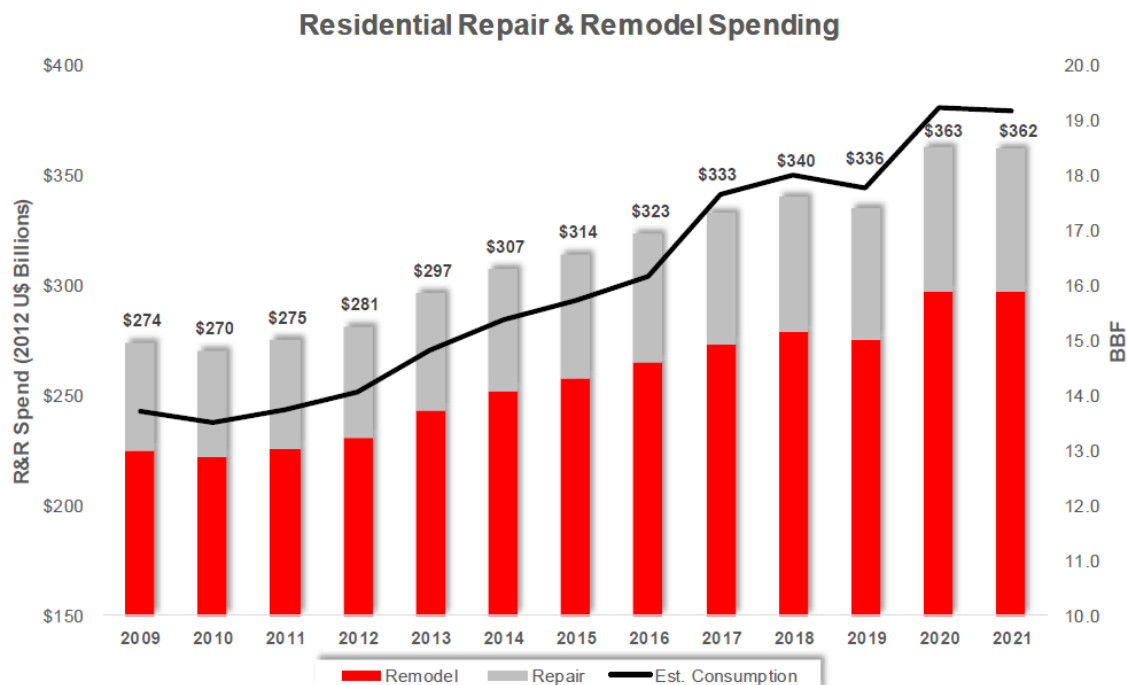
✓ Age of Housing Stock

Demands ongoing repairs (avg. 42 yrs. Old)
16-35 yrs. indoor projects, >46 yrs. outdoor projects

✓ Household Formation

Increase demand
Additional 12.5 million households will form 2015-2025

Strong Spending in the near-term before maintaining at a high level



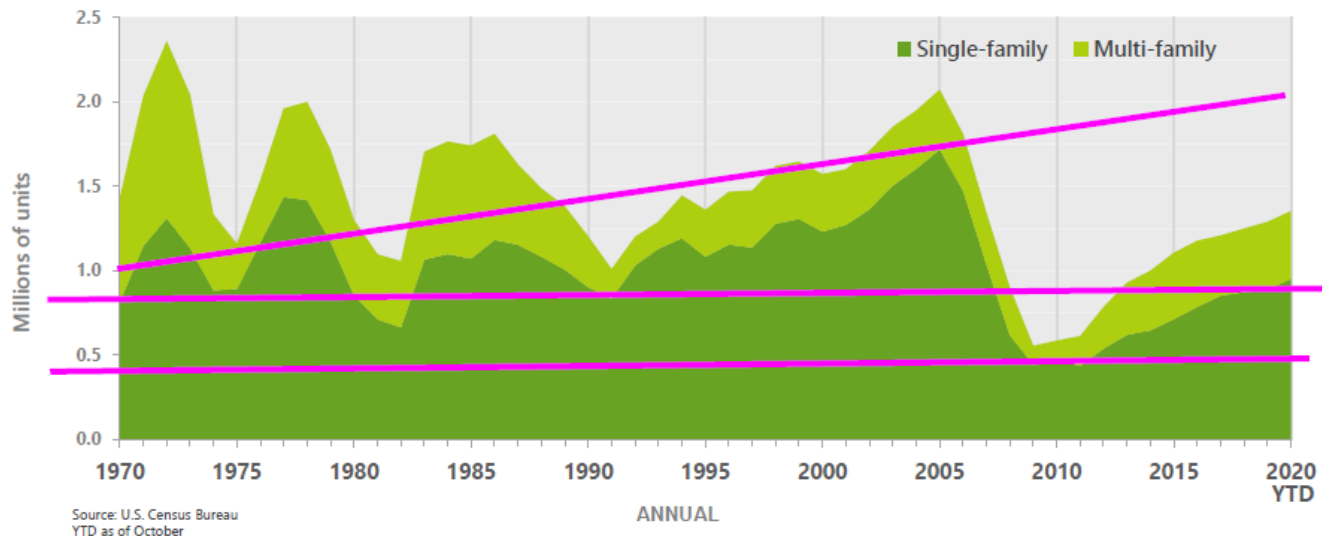
Source: US Census Bureau, Canfor



Long-Term Growth in U.S. Housing

- U.S. housing activity rebounding despite uncertain macroeconomic conditions
- Historically low mortgage rates and growing preference for larger, single-family homes
- Further economic disruptions could dampen near-term housing trajectory
- Expect solid housing growth as economic fundamentals improve

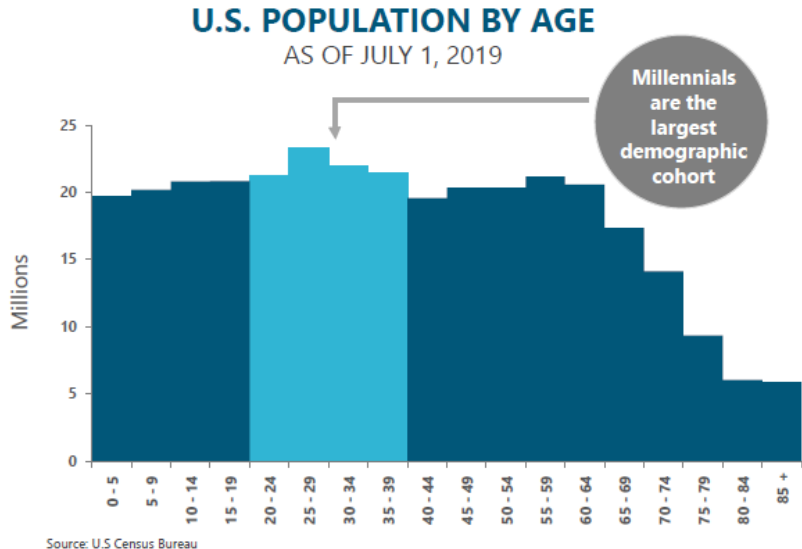
U.S. HOUSING STARTS
SEASONALLY ADJUSTED ANNUAL RATE



Long-Term Growth in U.S. Housing

LEVEL OF CONSTRUCTION REMAINS BELOW HOUSING NEED

- Growing housing “deficit” as current pace of building activity is not sufficient to meet demand
- Favorable demographics with millennials entering prime homebuying years

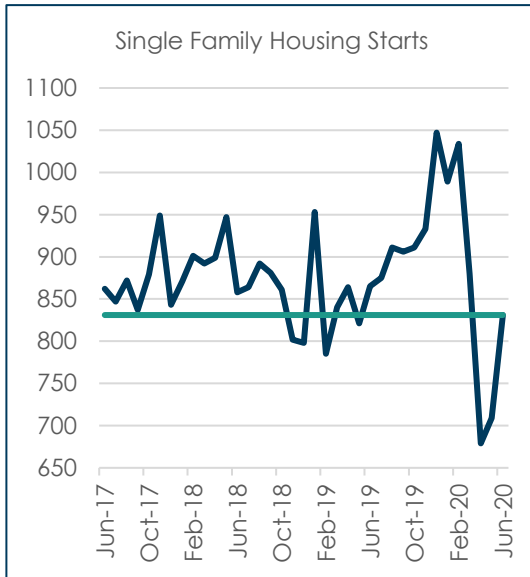


ANNUAL U.S. HOUSING NEED
MILLIONS OF UNITS

DRIVER	BASELINE AVERAGE DEMAND
New Household Formations	1.1
Replace Lost or Obsolete Units	0.3
Second Home Demand	0.1
Natural Vacancy Rate	0.1
ANNUAL NEW UNITS REQUIRED	1.6

Source: Freddie Mac, 2018

Catharsis + New Trends + Demand Boom = Lollapalooza!



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BUSINESS

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By [Cara Lombardo](#)
Updated Aug. 27, 2020 7:47 am ET

The companies, which manufacture products used in residential construction, would have a combined market value of about \$5.5 billion

Homebuyers' Wallets Hammered as Prices for Plywood Substitute Spike

By [Marcy Nicholson](#)
October 21, 2020, 10:30 AM EDT Updated on October 22, 2020, 12:30 PM EDT

- ▶ Prices of oriented strand board surge as lumber, plywood fall
- ▶ Norbord among firms set for windfall as builders' costs rise

- September 2020 Single-Family Starts of 1.415 mm highest since 2011

BNN Bloomberg

Oct 6, 2020

Lumber, panel prices expected to remain elevated despite recent declines

CALGARY - Forest product market analysts expect prices for lumber and building panels in North America will remain strong for several years despite recent price declines after an unprecedented surge to record high levels over the summer.

The New Builders FirstSource

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Range of Intrinsic Value: Valuation is Key!

EBITDA Estimate (10x EV / EBITDA multiple)

		<u>Revenue</u>					
		12,000	13,000	14,000	15,000	16,000	17,000
<u>EBITDA Margin</u>	7%	840	910	980	1,050	1,120	1,190
	8%	960	1,040	1,120	1,200	1,280	1,360
	9%	1,080	1,170	1,260	1,350	1,440	1,530
	10%	1,200	1,300	1,400	1,500	1,600	1,700
	11%	1,320	1,430	1,540	1,650	1,760	1,870
	12%	1,440	1,560	1,680	1,800	1,920	2,040
	13%	1,560	1,690	1,820	1,950	2,080	2,210

Share Price

		<u>Revenue</u>					
		12,000	13,000	14,000	15,000	16,000	17,000
<u>EBITDA Margin</u>	7%	\$34	\$37	\$41	\$44	\$48	\$51
	8%	\$40	\$44	\$48	\$51	\$55	\$59
	9%	\$46	\$50	\$54	\$59	\$63	\$67
	10%	\$51	\$56	\$61	\$66	\$71	\$75
	11%	\$57	\$62	\$68	\$73	\$78	\$84
	12%	\$63	\$69	\$74	\$80	\$86	\$92
	13%	\$69	\$75	\$81	\$87	\$94	\$100

Margin of Safety

		<u>Revenue</u>					
		12,000	13,000	14,000	15,000	16,000	17,000
<u>EBITDA Margin</u>	7%	(14%)	(5%)	3%	12%	20%	29%
	8%	1%	11%	20%	30%	40%	50%
	9%	15%	26%	37%	48%	59%	70%
	10%	30%	42%	54%	67%	79%	91%
	11%	45%	58%	71%	85%	98%	112%
	12%	59%	74%	89%	103%	118%	132%
	13%	74%	90%	106%	121%	137%	153%



Disclosure: Ownership Information

<u>Disclosures</u>	Builders FirstSource (BLDR)	Norbord, Inc. (TSX:OSB NYSE: OSB)	West Fraser (TSX:WFT)
Bob Robotti and/or members of his household has a financial interest in the following securities	Yes	Yes	No
Robotti & Company or its affiliates beneficially own common equity of the following securities	Yes	Yes	No
Robotti & Company or its affiliates beneficially own 1% or more of any class of common equity of the following securities	Yes	No	No
Bob Robotti serves as a Director or Officer or Advisory Board Member of the following securities	No	No	No

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Questions

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