Robotti
Value Investors

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Dear Client,

Often when someone thinks of "Value Investing" they rightly think of analyzing financial data, identifying undervalued assets, and using a systematic approach to evaluate numerous financial metrics, market trends and risk factors. This is true, and much of the work that we do here is through the process of reading financial reports and analyzing the relevant data. While much of our work can be done from behind a desk, there is an important aspect that needs to be done out in the real world. This is why we engage in face-to-face meetings with management teams, visit their facilities, and interact with our portfolio companies beyond the confines of a controlled setting like a conference call or board room.

To that end, through the month of September I traveled extensively and broadened my understanding and appreciation for several key investment factors pertinent to our strategy. My travels commenced in Istanbul, Turkey, where I participated in the 6th annual New Silk Road Forum, expertly orchestrated by my colleague, Isaac Schwartz. Here I was able to broaden my understanding of how trade routes have been impacted by the Russian/Ukraine war. Further I met with fellow investors focused on Africa, Europe, and Asia, which allowed me to test our theses through not just an American focused lens. I was also able to speak with experts on the upcoming graphic cards and chip manufacturing changes that will affect the myriad industries in which we invest. After all, despite the hysteria of deglobalization, the world has been permanently flattened.

Following the conference, my journey led me to Dubai, where I participated in a pivotal board meeting for one of our portfolio companies. This visit allowed me to gain firsthand insights into our business operations in the Middle East, a market of utmost importance to both our company and the global energy markets. Our focus was on delving into the current market dynamics and shaping our outlook for the next few years. Interacting with managers in this strategic market proved to be instrumental, providing deeper insights into the business dynamics that will significantly influence our business strategy and capital allocation decisions. Understanding the intricacies of operation in yet another vital market is critical and impacts our ability to enhance per-share value and drive sustainable growth. This immersive experience informs our strategic decisions, allowing us to effectively navigate the complex landscape of energy markets and capitalize on opportunities that align with our vision for value creation and expansion.

Following this comprehensive exploration of our business landscape, I had the opportunity to attend Pareto's enlightening 2-day conference on offshore energy and shipping in Oslo. The experience of hearing diverse perspectives and engaging with the managements of over 100 companies was incredibly enriching. Moreover, the invaluable networking opportunities with fellow investors provided beneficial insights. It was evident that conference attendance had notably increased compared to the previous year, reflecting a positive shift away from the lingering impacts of the COVID-19 pandemic, both in reality and in our collective mindset. However, amidst this enthusiasm, it's crucial to remain mindful of potential cautionary aspects tied to investor enthusiasm and confirmation biases that can arise from such events. Balancing our own views and insights with these considerations is an ongoing necessity, ensuring our investment decisions remain informed, rational, and aligned with the ever-evolving dynamics of the market and industry landscape. This continuous evaluation is essential for maintaining a prudent and adaptive investment approach.

The final leg of my journey brought me to Chile where my colleague, Theo van der Meer, and I visited with Finning International, the largest Caterpillar dealership in the world. We met with senior management as well as the in-country managers of their operations in Chile, Argentina and Bolivia. We spent a week touring their distribution centers, repair facilities and on-site mining locations. Each night we ate with fellow investors and company management and further developed our "grass-roots macro" view on the industrial, mining and construction industries across the globe. "Grass-roots macro" encapsulates the concept of gaining a profound understanding of macro-level trends within an industry by engaging directly with its fundamental components: customers, suppliers, and competitors. Instead of approaching industry analysis from a top-down perspective and fitting companies into preconceived macro frameworks, this approach involves starting from the ground up. Through extensive interactions and dialogue with industry participants, we allow their experiences and perspectives to guide our comprehension of the broader industry trends. The objective is to uncover diverse incentives and viewpoints across various companies, amalgamating this research to construct a comprehensive and nuanced depiction of the industry. This methodology enables us to transcend the industry's conventional beliefs and dogma, providing us with a clearer and more insightful perspective for strategic decision-making and investment evaluations.

Chile is particularly informative not only for copper markets, as it is the largest copper producing country in the world with 25% of copper production, but it also a critical supplier of the world's growing demand for lithium. And in Chile too, we see the growing advent of increasing application of renewable energy and the role this plays. Finning and Caterpillar will be a beneficiary of the energy transition in so many ways as "new electrical equipment" will displace the existing fleet of diesel powered equipment.

We also met with officials at the state-run Codelco (the largest copper producer in the world) reaffirming our thesis of a severe copper shortage in the coming years. We continued our trip in Chile by meeting with other copper producers and recyclers. I should note just how vital copper is to the world's electrification push. Electric vehicles need 4x the copper of a gasoline car, a single 3MW wind turbine can consume almost 5 tons of copper, and even a simple 12-gauge wire has about 50lbs of copper per mile.

So, what are the main takeaways I gained from my month of traveling?

1. **There's no place like home.** Despite the allure of travel, there is truly no place like home. Returning to the vibrant office in New York City and sharing the insights gained from my travels with everyone on our team remains a fulfilling conclusion to my journeys. Our joint follow-up calls with management and the team will further flesh out our learnings.
2. **The world is going to be short copper.** Chile, which is the largest producer of copper in the world, produced 5.3m tons of copper in 2022. By 2032 that number is expected to be 5.3m tons. You don't need an advanced degree to see that those two numbers are the same. Meanwhile the world demand in 2022 was 22m tons and is expected to rise to 40m tons by 2040. That means a likely 8m ton PER YEAR shortfall. Furthering our conviction, Codelco (remember they are the largest copper producer in the world) plans to spend $68 billion dollars over the next 25 years, yet that investment will largely keep the production levels where they are today. That's an awful lot of money to stay in place.
3. **Of course, it's not just incremental copper which will be needed.** In their materials on decarbonizing mining, BHP Properties indicated electrifying its Escondida mine could increase the demand for steel 200% from today. The list of materials includes cement, nickel, lithium, cobalt, etc. These materials have dramatic incremental needs to be both sourced and processed, beyond the depletion of current production.
4. **Picks and shovels remain a great thing to sell.** Whether it's copper or some other mineral, the cost of removing each incremental pound out of the ground is becoming more expensive. What that means is that more equipment is needed per pound, so the number of picks and shovels the world needs will continue to grow.
5. **Globalization 2.0 is in full swing.** From my time in Turkey, Dubai, Oslo and Chile, a constant theme was present. China's deflationary impact on the world has ended, especially as its growing appetite for these same materials exacerbates limited supplies. Further, reshoring of production is present across the globe, both in North America and around the world. Whether it is ensuring computer chip manufacturing is secured, or simply vertically integrating, companies and countries are expanding their facilities outside of China. Still, China's pervasive and critical role in many of these materials supply chains further complicates responses.
6. **The U.S. is structurally advantaged for years to come.** Another constant throughout my trip was the struggle companies have to simply keep on the lights. Whether due to the cost

of electricity or just the access to it, we saw time and again that companies are concerned about power/energy availability. North America doesn't have this problem due to its abundance of stranded, low-cost natural gas reserves. This is a dramatic, sustainable competitive advantage for North American energy intensive businesses. Of course, the accelerant of the Inflation Reduction Act is palpable.

7. **Renewables can't grow fast enough.** I mean this in two senses. One is that the demand for renewables is huge, and everyone is adding them as fast as they can. Two is that the demand for materials to build out renewables is creating bottlenecks and pushing an increase in their cost. They literally cannot grow fast enough, especially with the foreseeable bottlenecks in the demand for so many incremental commodities and materials. Remember, the decade starting in 2000 we experienced a commodity super cycle that was just from China's appetite. What happens when the entire world is hungry?
8. **The demand for energy will prolong the need for hydrocarbons and, with it, accelerate the need to manage down its impacts through substitutions and sequestration.** This leads to opportunities from carbon offsets to natural gas production.

Conclusion

The final thing I *learned* from this trip is something I have *known* for over 40 years. I could not do what I love to do if not for investors such as yourself. The excitement and passion that I have for unraveling the mysteries of our financial world has never been greater, and by having like-minded investors who understand our process, we can conduct our research the right way. I thank each and every one of you for allowing me to continue doing what I love.

All the best,

Bob

Appendix

As I'm sure most of you are aware, I have been on the Board of Directors at several companies over the years. We believe board membership provides invaluable benefits to us and our clients. As Warren Buffet has said, "I am a better investor because I am a businessman, and I am a better businessman because I am an investor." We believe that to be true, and further believe that our position on the board of companies we are invested in allows our voice to be heard at the company. This is one of the ways we are able to help improve our performance, as we have a direct say in how our investment is run. The flip side to board ownership is that from time to time we are restricted from transacting in the company during periods where we have material non-public information or for other regulatory reasons. This will sometimes lead to us not being able to buy or sell shares at certain times of the year. We believe these temporary inconveniences are far outweighed by the benefits of board membership. Further, when a company is on restriction, we are prevented from telling anyone that it is restricted, which can occasionally make communication between ourselves and you, our clients, difficult. That is why we wanted to write this brief note to explain why occasionally stocks that we are on the board of will have strange weightings in your portfolio or transact differently than expected. All this being said, please don't hesitate to reach out to us with questions, but just know that we may be limited in what we can say and/or do in specific companies we own.

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