ROBOTTI & COMPANY ADVISORS, LLC
Investment Securities
6 East 43rd Street
New York, NY 10017
(212) 986-4800
Fax: (212) 986-0816

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Dear Partner,

Good things happen to stocks that are cheap.

It's a simple thought that has served us and you, our clients, well for years. Bad news is often already reflected in the market price of cheap stocks and upside potential is frequently obscured, if not completely forgotten. Negative sentiments can goad investors into second-guessing their investment thesis, but our experience has shown that controlling emotions and focusing on the business pays off. The implicit cost of waiting for clarity, while difficult to quantify, can severely harm an investor's returns as the investment opportunity dissipates.

At Robotti & Company we strive to deliver results, net of fees, which exceed the general return of the stock market and to protect our invested capital from permanent loss; we do not wish to forecast the future. Fortunately for cyclical businesses, the future is highly predictable – the cycle will turn – although when is more uncertain.

Through patient, long-term investing in fractional shares of good companies selling at an appropriate discount, we have been able to meet our investment goals. Both the quality of the business and the risk of being an equity owner are carefully considered. Not only has this strategy worked for us over the past 30 years, but we continue to believe that it represents the best way to achieve our goals over the next 30 years as well.

A Timely Letter

In the third quarter of 2014, we explained why we believed shares of Builders FirstSource, Inc. (Nasdaq:BLDR) were cheap and how a 30+% pullback in the stock presented an interesting opportunity.

> *"While others 'wait on the sidelines' for the 'future to become more certain,' we ask- which future? If your definition of the future is 3 to 6 months, our response is the future is never certain. If you definition of the future is 3 to 5 years, our response is that we are just as certain as we were 6 months ago."*
>
> – Q3 2014 letter to clients

Our timing was opportune. Less than six months after writing our Q3 2014 letter a transformational merger resulted in the shares of BLDR nearly doubling in a day.[1] These recent moves within the building supply industry are a great example of the advantage of thinking long-term and not waiting on the sidelines even if short-term events lack clarity.

We spoke about how the sentiment linked to housing swings presents us opportunities within that volatility. Over our time with this investment we were able to watch the company improve and business begin to

[1] BLDR closed at $6.90 on April 10, 2015 and closed at $11.57 the next market day on April 13, 2015

recover, albeit not in a straight line, while the share price fell. We didn't know what the 'right price' was, but we did know that the economic worth of the business was much more significant than the market price, due to industry dynamics, the company's competitive position and its normalized earnings power.

Back in 2009 our long-term premise on BLDR was (and remains) simple, although we never had certainty on when it would prove out:

- The business was significantly depressed below normalized levels in a sector critical to the US economy – new home construction.
- The housing market was, and is, deeply cyclical.
- BLDR would be a survivor in the depression that its industry was undergoing, and that collapse would provide excellent opportunities to the survivors.
- BLDR was trading at a fraction of the valuation implied by the normalized environment.

Included in this mailing is an excerpt from the letter in which we discuss BLDR.

Transformation
On April 13, 2015 Builders Firstsource, Inc. acquired ProBuild Holdings LLC for $1.63B. This is a transformational acquisition for BLDR specifically and the industry in general. This combined company will clearly be the largest LBM (lumber & building materials) company in America, with a truly national footprint. Another recent merger between BMHC and Stock Building Supplies (NASDAQ:STCK) further

($ in millions)	Builders FirstSource	ProBuild	Cost Savings	Pro Forma Total
Sales	$1,660[1]	$4,430[2]		$6,090
Adj. EBITDA	$76[1]	$190[2][3]	$110[4]	$376
% Margin	*4.5%*	*4.3%*		*6.2%*

Acquisition of ProBuild Is a Transformative Transaction for Builders FirstSource

Source: Company filings.
Note: All figures are for the year ended 12/31/2014.
(1) Pro Forma adjustments to include the full-year impact of completed BLDR acquisitions and related cost synergies.
(2) Adjusted for closed operations.
(3) Impact of lease finance obligations included in interest expense. See reconciliation on page 19.
(4) Mid-point of the expected range. Excludes estimated one-time costs of $90 million to $100 million to implement cost savings.

demonstrates the industry is consolidating, which is a catalyst for the opportunity we had identified.
Like most of the industry, the company that BLDR is acquiring has been in a tailspin since 2008, and although it is the largest company in the LBM market, it still struggled to maintain a healthy business. Its owner, The Johnson family of Fidelity, had to invest $100's of millions to keep the business viable in the downturn. Through combining with BLDR, the two should improve their margins and utilization, expand their breadth of added offering to homebuilders, and leverage a larger North American footprint.

This event obviously accelerated, but more importantly increased, our expected return from our investment in BLDR. Specifically, I wrote back in our Q3 2014 letter that normalized (not peak) levels for BLDR should be $2.5B in revenues and at least $150m in EBITDA with 100m shares outstanding ($1.50/share). The impact of this combination changes those projections materially. I now expect, though nothing is for certain, normalized revenues and EBITDA to be at least $10 billion and $800m respectively with 110m shares outstanding. So the new proforma merged company should have 5 times the EBITDA with only 10% more shares outstanding.

The average cost across the entirety of the managed accounts is just under $2.50. The closing price on June 30, 2015 was $12.84, up almost 100% from when we wrote back in Q3 2014 and 5x our initial average investment. To reiterate, this transformative acquisition sets the backdrop for BLDR to appreciate dramatically from here.

Simplify the matter

We approached our investments in the building supply companies as simply as possible. The U.S. was building fewer homes than it needed, and pent up demand was (and still is) a significant tailwind going forward. While a rising tide rises all boats, it does not do so equally. Through our expertise in identifying good capital allocators and management that is able to navigate cyclical industries we were able to find an exceptional investment opportunity. Our patience and commitment to our investment thesis paid off this year with the consolidation of the industry.

In addition to the specifics of BLDR this story has implications throughout our entire portfolio. We have identified other companies in the housing industry like Norbord (TSX:NBD) that have a similar opportunity set that have yet to manifest. Outside of BLDR, our portfolio is chock full of companies that are also in that consolidation phase, with dramatic appreciation potential yet to be realized.

The investments we have in energy are prime examples. Our conviction is that over the next three years the recovery in energy should be in full bloom. We expect the survivors we have identified should be ready, willing and able to opportunistically grow the earnings power of their businesses and provide strong returns to their owners. We do not believe that these well positioned companies can continue to trade at the extremely large discounts to the value of their businesses they currently do. After identifying these companies we believe it to be a matter of continued scrutiny, time and patience.

Conclusion

When the difference between price and value is wide, precision is not a prerequisite for investment. This latest event does not exist in a vacuum, and is indicative of the style of investing that we have employed for 30 years. By identifying those companies with a large margin of safety and a substantial disparity between economic value and market value we should and hope to, over time, continue to outperform the market. Just identifying the companies is half the battle; we also need to have the temperament to stay true to our beliefs (and clients that share the same disposition) while the market does everything it can to scare us away from our thesis. The best way to insulate ourselves from the noise? Keep it simple.

All the Best,

Bob Robotti

Excerpt from October 15, 2014 letter to clients.

Are You Mr. Market's Master (or vice-versa)?

The word "volatility" has taken on a negative connotation for investors. Conventional investment dogma states that more volatility means more risk, and we all know that risk is bad. In tune with our contrarian nature, we disagree with this assertion. The preoccupation with short-term news can sometimes have an outsized and disproportionate effect on stock prices, creating opportunities for investors who are able to tune-out the noise and focus on the long term.

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. For example, 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 confidence[3].

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 $5.10[4]. 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 Jeanna Smialek and Lorraine Woellert | May 28, 2013 4:20 PM ET
Bloomberg

ECONOMIC REPORT
Home-builder confidence hits seven-year high
Published: June 17, 2013 10:56 a.m. ET
MarketWatch

BloombergBusinessweek
Markets & Finance
The Housing Rebound Stalls
By John Gittelsohn and Prashant Gopal | May 01, 2014

Housing market could be facing another bubble: Shiller
Tuesday, 31 Dec 2013 | 9:54 AM ET
CNBC

Price is What You Pay, Value Is What You Get

Let's take a step back for a moment and reframe the question, putting aside the very important, but more difficult problem of determining Builders FirstSource's true economic worth.

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[3] Federal Reserve Bank of St. Louis
[4] Capital IQ

Excerpt from October 15, 2014 letter to clients.

On April 4, 2014, Builders FirstSource had 97.6 million diluted shares outstanding and $290 million of net-debt (long-term debt *minus* cash)[5]. In other words, if you happened to have an extra few billion dollars lying around, you could have bought the entire business for $1.2 billion (share price *multiplied by* shares outstanding *plus* net debt).

Just six months later, on September 29th, Builders FirstSource had 100.8 million diluted shares outstanding and $319 million of net-debt. Now, even if you didn't have a few extra billion handy, you could buy the same business for just $830 million[6]. Between April and September earnings had *improved* and the company made three acquisitions *adding $43 million of revenue*[7]. Yet the price one had to pay to buy the entire business fell by 31%!

Without knowing what the right price is – does it seem rational for the true economic worth of this entire business to have fluctuated >30% in less than six months? Of course, without knowing the true value of the business, this realization would be worthless. If the true value of Builders FirstSource is less than $830 million then the stock price just went from very expensive to just expensive.

Let's investigate further.

Where Are We?

Over 30 years of investing, my team and I have observed that when forecasters agree on the same outcome, that outcome is often the least likely to occur! As the number of single-family housing starts slowly improved throughout 2012 and into 2013, the consensus view assumed that we had entered "rebound mode." But when new home starts began to struggle as we entered 2014, the consensus view reversed. We often find that consensus opinions end up as an "all or nothing" proposition.

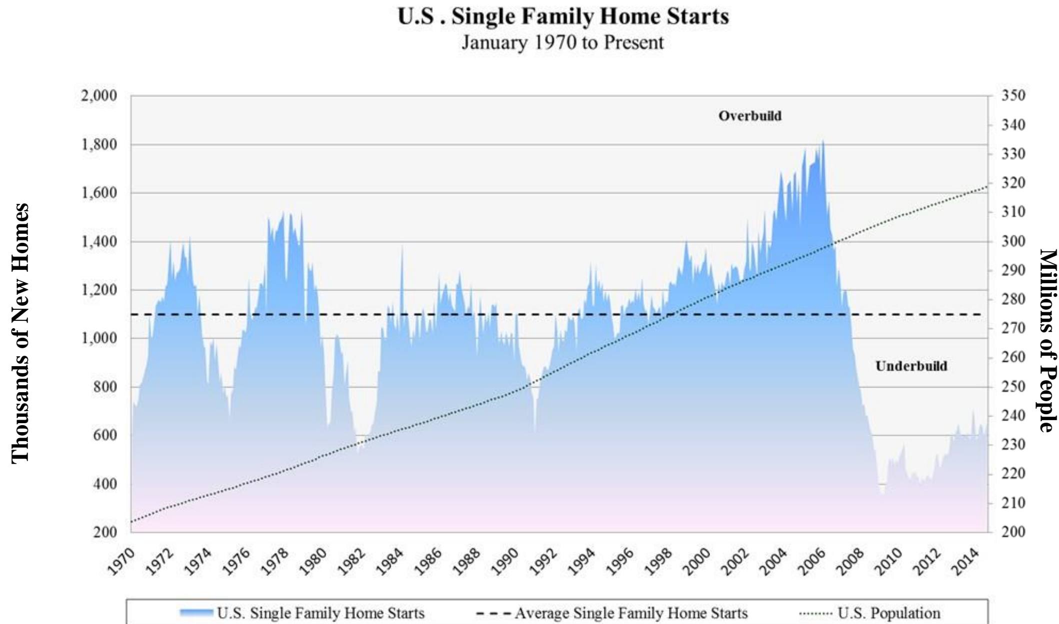
Looking back, the total number of new home starts in the U.S. peaked at an annualized rate of 2.3 million in January 2006 before diving 80% to a low of 478,000 in April 2009. Single-family home starts, which peaked at 1.8 million in November 2005, cratered to 353,000 in March 2009[8]. This is a story that was a long time in the making. The normal economic cycle of the housing industry was amplified by the Federal Reserve's ultra-low interest rate policy, reckless subprime lending, complicated financial instruments such as mortgage backed securities, CDOs, CDO squared, and a host of other variables that led to the collapse of two major investment banks and turned into the worst recession in over 80 years.

Let's consider the longer-term trends as illustrated in the chart below. Since 1970, the annual number of single-family home starts in the United States has averaged 1.05 million units. Over that same period, the population has grown by 115 million people or 56%[9]. Between 1980 and October 2010 (the last official measure) the U.S. added 36.8 million households reaching 117.8 million, an increase of 46%[10].

How many single-family homes will be built this month? This year? These are questions we cannot answer. However, after analyzing the long-term trends, we are comfortable assuming that at present, we are closer to the lows of the normal housing cycle than we are from the highs. Furthermore, within the context of these

[5] Builders FirstSource Q1 2014 Form 10-Q
[6] Builders FirstSource Q2 2014 Form 10-Q
[7] Builders FirstSource Q2 2014 Conference Call
[8] Federal Reserve Bank of St. Louis
[9] Federal Reserve Bank of St. Louis
[10] United States Census Bureau

long-term trends, we believe the normalized level of single-family home starts is more likely to be higher than the 30-year average of 1.05 million.



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

<u>What's It Worth?</u>

The U.S. housing market has just emerged from the most difficult period in its history. During that time the industry went through a cathartic process, one that often takes place during the trough of an economic cycle. Consolidation began, companies were recapitalized, capital structures were improved, unprofitable assets were shed, and costs were removed. Furthermore, the recovery is still in an early stage. In the pro dealer segment of the building distribution industry the top five competitors (ProBuild Holdings, 84 Lumber, Builders FirstSource, BMC, and Stock Building Supply) have emerged with a 25% share[11] of a $169 billion single-family residential home construction market[12]. A long runway of consolidation should help boost revenue growth beyond the level expected from an inevitable industry rebound.

The primary driver of Builders FirstSource's revenue is single-family home starts. As of the August release, the annualized number of U.S. single-family home starts was 643,000[13]. Given our assumption that the normal level of single-family home starts is greater than 1.05 million, we believe that there is *at least 60% upside* from the current level. This translates into approximately 60% more revenue than Builders FirstSource currently generates.

In 2013, Builders FirstSource generated $2,399 of revenue per single-family home start. This number has increased every year since 2009 when it generated $1,534 per single-family home start. Given the likelihood of further consolidation, we believe this number will continue to increase over the long-term.

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[11] Builders FirstSource Second Quarter 2014 Presentation
[12] 2013 National Association of Homebuilders
[13] Federal Reserve Bank of St. Louis

Excerpt from October 15, 2014 letter to clients.

FYE 12/31	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	TTM
U.S SFH Starts	**1,505**	**1,604**	**1,719**	**1,474**	**1,036**	**616**	**442**	**471**	**434**	**537**	**621**	**656**
% growth	*10.4%*	*6.6%*	*7.2%*	*(14.3%)*	*(29.7%)*	*(40.5%)*	*(28.2%)*	*6.6%*	*(7.9%)*	*23.7%*	*15.6%*	*5.6%*
Revenue / SFH	**$1,113**	**$1,283**	**$1,360**	**$1,463**	**$1,417**	**$1,610**	**$1,534**	**$1,487**	**$1,795**	**$1,994**	**$2,399**	**$2,354**
% growth	*1.1%*	*15.3%*	*6.0%*	*7.6%*	*(3.1%)*	*13.6%*	*(4.8%)*	*(3.0%)*	*20.7%*	*11.1%*	*20.3%*	*(1.9%)*

Source: Builders FirstSource Annual Report, Federal Reserve Bank of St. Louis, Robotti & Company Advisors Estimates

Just assuming that the normal level of single-family home starts is 1.05 million (a conservative assumption in our opinion), Builders FirstSource should generate $2.5 billion of revenue. Adjusted EBITDA[14] margin was 4.1% in 2013 and 4.4% over the past twelve months. We think a conservative estimate of a normal EBITDA margin is 6%. That comes out to a low-case, normalized, pre-tax earning power of approximately $1.05 per share or 4.7x the stock's closing price of $4.92 on October 10th, especially modest for a non-capital intensive distribution business.

Conclusion

> *Price fluctuations have only one significant meaning for the true investor. They provide him with an opportunity to buy wisely when prices fall sharply and to sell wisely when they advance a great deal. At other times he will do better if he forgets about the stock market and pays attention to... the operating results of his companies.* Benjamin Graham, The Intelligent Investor

So as you now see, a dramatic move in the price of a stock combined with our conviction as to where we are within the normal housing cycle provides us with a compelling investment opportunity; one we can take advantage of, as long as we are not influenced by the short-term manic moods of Mr. Market.

Of course, we have not revealed a precise estimate of the true economic worth of Builders FirstSource. By doing so, we hope to give you further insight into our way of thinking. The concept of *margin of safety* is fundamental to our investment philosophy and we only invest when the room for error is wide. When the difference between price and value is so wide, precision is not a prerequisite for investment. Lest you think otherwise, we have spent a great deal of time analyzing the value of Builders FirstSource and welcome your call if you would like to discuss further.

There are many who believe that value investing makes so much common sense that it must also be easy. Times like these prove why this is not true. While others "wait on the sidelines" for the "future to become more certain," we ask – which future? If your definition of the future is 3 to 6 months, our response is that the future is never certain. If your definition of the future is 3 to 5 years, our response is that we are just as certain as we were 6 months ago. Time horizon arbitrage, the opportunity created by having a different time horizon than a majority of the market, has frequently been the source of a profitable competitive advantage. Cal-Maine Foods and Skechers, both of which were sold since the quarter end, represent just two of the recent examples where our focus on the long-term value of a business has paid off. (*For a detailed account of our investment in Skechers, please see Robotti & Company Advisors Third Quarter 2013 Letter.*) We continue to take advantage of Mr. Market's manic mood swings and refuse to let his moods drive our view of value.

[14] Earnings before interest, taxes, depreciation and amortization

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