Robotti
Value Investors

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Dear Client,

We recently shared our thoughts on the heightened market volatility. We have attached that below for your reference. Since then, the markets have continued to behave erratically, with volatility persisting. While these swings can be unsettling, it's worth reminding ourselves—and you—that volatility often creates opportunity and risks, shaking out those without the right understanding and fortitude. During this period of uncertainty, we've been actively gathering information, speaking with management teams, and reassessing economic conditions on the ground. These efforts are giving us greater clarity on how our investments are being impacted. We do not see critical deleterious development, but instead we see economic progress which should accelerate positive changes.

One topic we didn't address in our previous note, but that I've discussed frequently over the years, is the role of indexation and passive investing during turbulent markets. In periods of broad investor fear, we tend to see indiscriminate selling—not due to company-specific fundamentals, but as part of a general "de-risking" of portfolios. Mr. Market's manic depressive emotions can result in attractively valued businesses being sold off indiscriminately. "Eventually, our economic fate will be determined by the economic fate of the business we own."[1] For discerning investors, these periods of indiscriminate selling can present real opportunities.

We understand the worry and unease that can come with the steady stream of financial headlines in recent months. It's natural for emotions to run high in this kind of environment—our instincts may shift into fight-or-flight mode. That's precisely why it's so important to pause

[1] Berkshire Hathaway 1987 Letter to Shareholders

and re-center around what we know, what we can control, and what lies beyond our control. Remember, Mr. Market is there to serve you, not to guide you!

By focusing on objective facts and grounding our decisions in the discipline of valuation—our North Star—we can stay focused on the signal and not be distracted by all the noise. While some elements of the market will always remain unpredictable, being appreciative of those risks helps us assess them more clearly. Fortunately, Mr. Market often offers opportunities where the potential upside significantly outweighs the perceived risks.

See our thoughts below, including some highlighted portions:

Market Meltdowns Are Recurring Events,

Buckle up! The past few days have seen rampant investor uncertainty and price volatility that we haven't seen since the onset of the COVID-19 pandemic. The new US tariff policy being threatened by the current administration has unnerved and upset Mr. Market, and he has reacted ubiquitously and negatively. In times like these we think it is good to remember Warren Buffett's message in his 1987 letter to shareholders, "Mr. Market is there to serve you, not to guide you."[1] We council you to think through the purpose of the current turmoil and the likely outcome.

The intended purpose of the current tariffs is to bring manufacturing power back to the United States. As we have said in our recent letters, we believe the reshoring process was already underway and is likely to continue with or without the institution of tariffs. We have repeatedly highlighted this outcome due to the competitive advantages North America holds as a cheap energy producer, a structural advantage which is persistent and sustainable. We also note that tariffs are being introduced into an environment which is experiencing inflationary pressure. Elevated and persistent inflation will control interest rates (not fed policy!) Higher inflation and higher interest rates push lower valuations for financial assets. We believe the current development accelerates the threads we identified.

Manic depressive episodes like this are not uncommon for Mr. Market. Broad-based investor fear affects every corner of the market and while certain industries will be affected negatively, it's paramount we focus on the long-term economics and the fundamentals of a business, which will determine its value. We have tangible examples of this fact pattern in response to COVID. Those structural changes persist even now that COVID has passed. Our job as stock pickers is to discern which companies may have impairments and which have become better value.

Our approach has always centered on bottom-up stock selection, focusing on determining the fair value of a business. When prices come in, as we have seen in the past few days, stocks come closer to – or fall significantly below- their intrinsic value. And as always, the most important thing in investing is: "**Valuation Matters!**" The price you pay for a security is the best predictor of the future result. There is one sure, irrefutable difference in the market today, value is further discounted.

Berkshire Hathaway 1987 Letter to Shareholders

Marketable Securities - Permanent Holdings

Whenever Charlie and I buy common stocks for Berkshire's insurance companies (leaving aside arbitrage purchases, discussed later) we approach the transaction as if we were buying into a private business. We look at the economic prospects of the business, the people in charge of running it, and the price we must pay. We do not have in mind any time or price for sale. Indeed, we are willing to hold a stock indefinitely so long as we expect the business to increase in intrinsic value at a satisfactory rate. When investing, we view ourselves as business analysts - not as market analysts, not as macroeconomic analysts, and not even as security analysts.

Our approach makes an active trading market useful, since it periodically presents us with mouth-watering opportunities. But by no means is it essential: a prolonged suspension of trading in the securities we hold would not bother us any more than does the lack of daily quotations on World Book or Fechheimer. Eventually, our economic fate will be determined by the economic fate of the business we own, whether our ownership is partial or total.

Ben Graham, my friend and teacher, long ago described the mental attitude toward market fluctuations that I believe to be most conducive to investment success. He said that you should imagine market quotations as coming from a remarkably accommodating fellow named Mr. Market who is your partner in a private business. Without fail, Mr. Market appears daily and names a price at which he will either buy your interest or sell you his.

Even though the business that the two of you own may have economic characteristics that are stable, Mr. Market's quotations will be anything but. For, sad to say, the poor fellow has incurable emotional problems. At times he feels euphoric and can see only the favorable factors affecting the business. When in that mood, he names a very high buy-sell price because he fears that you will snap up his interest and rob him of imminent gains. At other times he is depressed and can see nothing but trouble ahead for both the business and the world. On these occasions he will name a very low price, since he is terrified that you will unload your interest on him.

Mr. Market has another endearing characteristic: He doesn't mind being ignored. If his quotation is uninteresting to you today, he will be back with a new one tomorrow. Transactions are strictly at your option. Under these conditions, the more manic-depressive his behavior, the better for you.

But, like Cinderella at the ball, you must heed one warning or everything will turn into pumpkins and mice: Mr. Market is there to serve you, not to guide you. It is his pocketbook, not his wisdom, that you will find useful. If he shows up some day in a particularly foolish mood, you are free to either ignore him or to take advantage of him, but it will be disastrous if you fall under his influence. Indeed, if you aren't certain that you understand and can value your business far better than Mr. Market, you don't belong in the game. As they say in poker, "If you've been in the game 30 minutes and you don't know who the patsy is, *you're* the patsy."

Ben's Mr. Market allegory may seem out-of-date in today's investment world, in which most professionals and academicians talk of efficient markets, dynamic hedging and betas. Their interest in such matters is understandable, since techniques shrouded in mystery clearly have value to the purveyor of investment advice. After all, what witch doctor has ever achieved fame and fortune by simply advising "Take two aspirins?"

The value of market esoterica to the consumer of investment advice is a different story. In my opinion, investment success will not be produced by arcane formulae, computer programs or signals flashed by the price behavior of stocks and markets. Rather an investor will succeed by coupling good business judgment with an ability to insulate his thoughts and behavior from the super-contagious emotions that swirl about the marketplace. In my own efforts to stay insulated, I have found it highly useful to keep Ben's Mr. Market concept firmly in mind.

Following Ben's teachings, Charlie and I let our marketable equities tell us by their operating results - not by their daily, or even yearly, price quotations - whether our investments are successful. The market may ignore business success for a while, but eventually will confirm it. As Ben said: "In the short run, the market is a voting machine but in the long run it is a weighing machine." The speed at which a business's success is recognized, furthermore, is not that important as long as the company's intrinsic value is increasing at a satisfactory rate. In fact, delayed recognition can be an advantage: It may give us the chance to buy more of a good thing at a bargain price.

As always, we are grateful for your trust and are here to answer any questions you may have.

All the best,

Bob

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