# INVESTING AMIDST THE DISRUPTION

## TECHNOLOGY THROUGH THE LENS OF A VALUE INVESTOR

FOR A COPY OF TODAY'S PRESENTATION AND ADDITIONAL INFO, PLEASE SCAN

CAMBIAR INVESTORS

PROFILE

# JOSEPH CHIN, CFA

Joe Chin is an Investment Principal at Cambiar Investors with over 23 years of industry experience. Mr. Chin's primary analytical responsibilities include U.S. company coverage within the technology sectors. Prior to joining Cambiar, Joe worked at Obermeyer Wood Investment Counsel, where he was a Portfolio Manager and Senior Analyst.

Mr. Chin received a BA in Economics from Wesleyan University and holds the Chartered Financial Analyst® designation.

## AGENDA

### TECHNOLOGY AND VALUE ARE NOT MUTUALLY EXCLUSIVE

### QPD INVESTING IN TECHNOLOGY

### THREADING THE NEEDLE OF VALUE & QUALITY

### DISRUPTION IS BREAKING OUT

# VALUE INVESTING IS NOT THE SAME AS THE VALUE FACTOR

## VALUE INVESTING

Buying an asset for less than it's worth

*"The value of a business is the present value of the cash they can distribute to owners over time."*

*– Michael Mauboussin (8/2021)*

## TECHNOLOGY

Defined by disruptive innovation with important implications for cashflow growth/durability

*"Intangible assets are more scalable than tangible assets. That means successful companies that rely on intangible assets can grow faster than companies built on tangible assets…On the other hand, obsolescence means that companies that rely on intangible assets can decline more rapidly than those built on tangible assets…This means that we should also expect to see slower growth rates, or a greater rate of decline, for the losers than the base rate data reflect…*

*This provides investors with good and bad news. The good news is there will be some businesses that grow in excess of what history would suggest, creating opportunity. The bad news is some businesses will lose their positions of prominence and decline more rapidly than their predecessors did. Base rates remain extremely informative, but we must have the mental flexibility to acknowledge how the population of companies has changed over time."*

**Michael Mauboussin**
Investment Strategist
(June 2021 – Impact on Intangibles on Base Rates)

# CHEAP IS NOT VALUE, ESPECIALLY IN TECHNOLOGY

A company with above average growth can sustain if it is on the right side of history.

Conversely, cheap tech stocks can often be value traps.

It requires a strong understanding of technology trends and “where the puck is going” in order to accurately make this judgement.

# IN OUR VIEW, A SUCCESSFUL VALUE INVESTOR IN TECHNOLOGY SHOULD EMBRACE THE CONCEPT OF DISRUPTIVE INNOVATION WHILE STAYING GROUNDED IN A CASH FLOW VALUATION FRAMEWORK


- Identify companies where market expectations of FCF generation underestimates true potential
- Identify the secular mega trends (disruption) along with winners/losers
- Rigorous bottom-up analysis of real growth potential (TAM analysis, unit economics, competitive risks, and long-term base rates)
- Enhance risk/reward by identifying second order beneficiaries or market structure inefficiencies

# CHANGES WE ARE MONITORING...

- Cloud/SaaS
- Robotics
- 5G Wireless
- Streaming Media
- Artificial Intelligence/ Machine Learning
- Energy Transition
- Electric Vehicles/ADAS
- Blockchain
- Quantum Computing

# COMMON CHARACTERISTICS OF DISRUPTIVE INNOVATION

- **Simpler, more convenient, and more affordable (tech enables efficiency and is inherently disinflationary)**
- Initially viewed as inferior by historic standards
- Technology is often paired with a Business Model change that allows it to be sustainable
- Innovations start slow but increase exponentially (gradually, then suddenly)
- **Incumbents are economically motivated to ignore the disruption (Innovators Dilemma)**


## THE NEXT BIG THING WILL START BY LOOKING LIKE A TOY

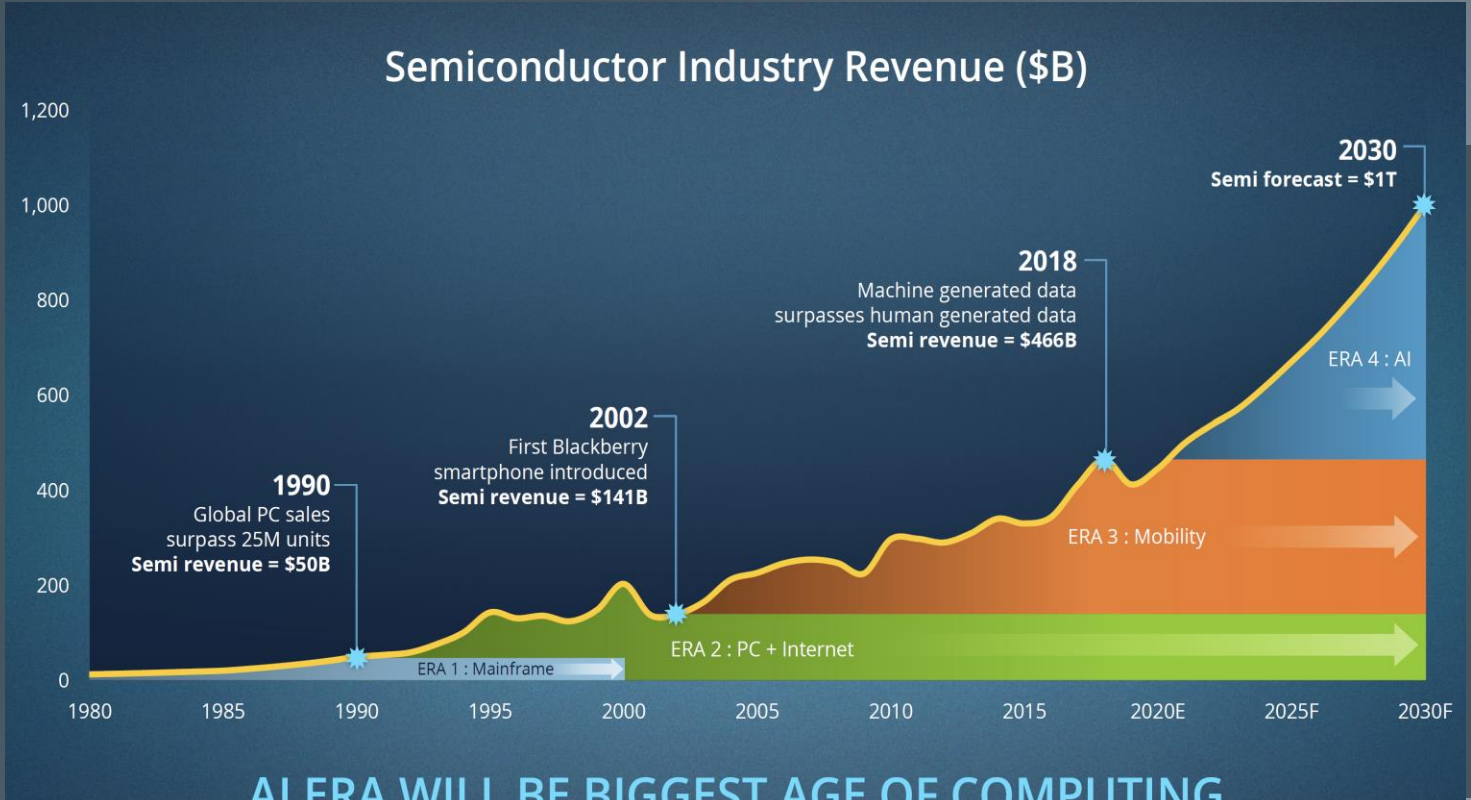
# APPLIED MATERIALS®

- Disruption has positively impacted supply/demand equilibrium in semiconductor industry
- Industry data confirms increasing criticality of semiconductor manufacturing and future architectural direction increases conviction
- Cambiar doesn't believe current market value reflects the company's multi-year FCF potential

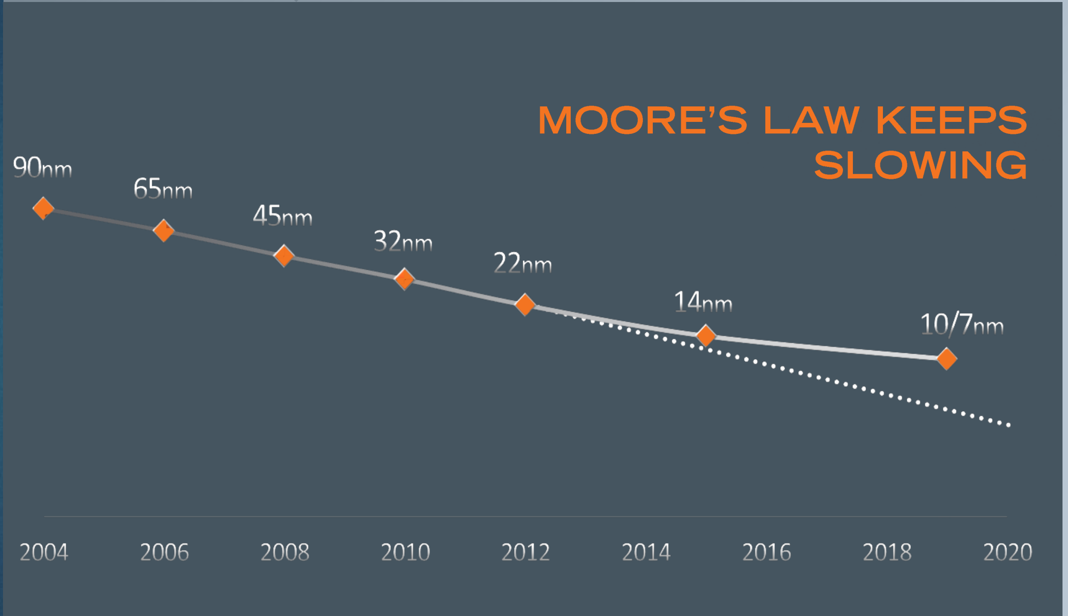
# MOORE'S LAW STRESS

## "TWILIGHT IN THE VALLEY"

- Parallels to other supercycles
- Demand = Fourth Wave of Computing
- Supply = Moore's Law Stress




Source: Applied Materials

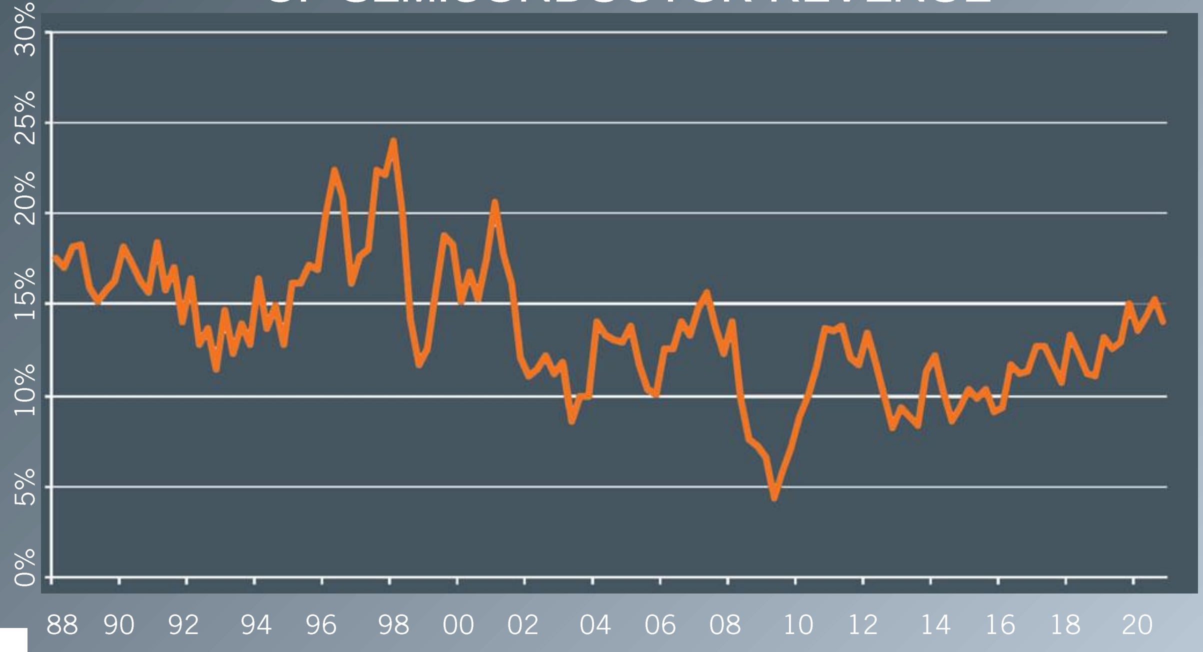



Source: AMD

# ARMS DEALER TO SEMICONDUCTOR INDUSTRY

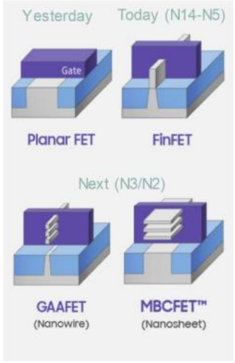
## INCREASING RENT TO MANUFACTURING ECOSYSTEM

### WAFER FABRICATION EQUIPMENT (WFE) AS A % OF SEMICONDUCTOR REVENUE

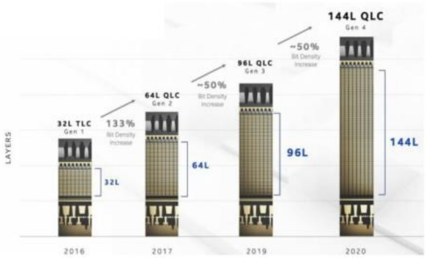



Source: World Semiconductor Trade Statistics

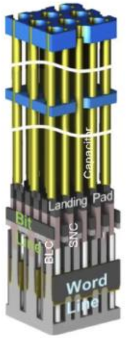
Logic



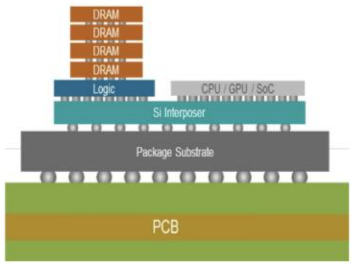

3D NAND Memory




DRAM Memory




Advanced Packaging




Source: Samsung, Intel, AMAT, Semi Engineering

Semiconductor capital intensity today seems neither depressed nor elevated vs. recent history, and is depressed vs. the farther past

CAMBIAR INVESTORS



amazon.com


- Without admitting it, Amazon has copied the Costco business model - Amazon purposefully under-earns in e-commerce (first party) retail in order to cross-sell high margin subscription like B2B services
- Cashflow contribution from high margin services becomes evident when normalizing for business model
- Amazon valuation reflects this inefficiency, especially when considering Amazon Web Services (AWS)

**Breakeven here…**

**..to leverage assets here.**

amazon.com

Retail

| | AWS | Advertising | 3rd Party Commissions | Fulfilled by Amazon (FBA) | Delivery |
|---|---|---|---|---|---|
| **Market Size (2018)** | ~$230B | ~$535B | ~$33B | ~$40B | ~$420B |
| **Market Growth ('18-'22)** | ~20% | ~12% | ~14% | ~35% | ~3% |
| **Incremental Margin (2018)** | ~40% | ~80% | ~80% | ~30% | ~50% |
| **Amazon Share** | ~11% | ~6% | ~75% | ~85% | nil |
| **Competitors** | Microsoft<br>Google<br>Alibaba | Google<br>Facebook | eBay | UPS<br>FedEx | UPS<br>FedEx<br>USPS |

- Amazon's secret is hiding in plain sight: break even in Retail in order to sell high margin services
- AWS, 3P Commissions, Prime, and advertising are today's services
- Investing in logistics, video, and other services



Source: Amazon, Cambiar

Source: Amazon, Cambiar

amazon.com

## BREAKDOWN OF REVENUE

- **First Party Retail** - represents 55% of sales with below corporate average growth and profitability
- **B2B / B2C** subscription - like services represent 45% of sales with above corporate average growth and profitability
- **AWS** - Sum of the Parts Valuation
- **Optionality** - next AWS

# EVERY COMPANY IS A TECH COMPANY

*"Moving forward, companies will need to pursue digital transformation in order to survive, let alone be markets leaders"*

\- Accenture Dig Transformation

CAMBIAR INVESTORS

# CONCLUSION

- In our view, successful value investing in tech:
  - Inflexible around a cash flow definition of value
  - Open-mindedness to change and disruption

- We believe, alpha generated when a differentiated view of the future intersects with analytical rigor

- Disruptive innovation is the result of investment
  - In tech, investments are intangible assets
  - Traditional value factors do a poor job of accounting for intangible investments
  - Income statement / balance sheet heuristics can steer you to companies that are underinvesting and most susceptible to disruption

# THANK YOU

FOR A COPY OF TODAY'S PRESENTATION AND ADDITIONAL INFO, PLEASE SCAN

CAMBIAR INVESTORS

# DISCLOSURE

Certain information contained in this communication constitutes "forward-looking statements", which are based on Cambiar's beliefs, as well as certain assumptions concerning future events, using information currently available to Cambiar. Due to market risk and uncertainties, actual events, results or performance may differ materially from that reflected or contemplated in such forward-looking statements. The information provided is not intended to be, and should not be construed as, investment, legal or tax advice. Nothing contained herein should be construed as a recommendation or endorsement to buy or sell any security, investment or portfolio allocation.

Any characteristics included are for illustrative purposes and accordingly, no assumptions or comparisons should be made based upon these ratios. Statistics/charts and other information presented may be based upon third-party sources that are deemed reliable; however, Cambiar does not guarantee its accuracy or completeness. As with any investments, there are risks to be considered. Past performance is no indication of future results. All material is provided for informational purposes only and there is no guarantee that any opinions expressed herein will be valid beyond the date of this communication.

The specific securities identified and described do not represent all of the securities purchased or held in Cambiar accounts on the date of publication, and the reader/listener should not assume that investments in the securities identified and discussed were or will be profitable. The holdings described may differ by account based on the account's strategy, and other factors. All information is provided for informational purposes only and should not be deemed as a recommendation to buy the securities mentioned.