Independent wealth manager Samuel Weber presented his investment thesis on Lanxess (Germany: LXS) at European Investing Summit 2021.

Thesis summary:

Lanxess is a leading specialty chemicals company with sales of EUR 6.1 billion in 2020. The company has 14,800 employees in 33 countries. The core business of Lanxess is the development, manufacturing and marketing of chemical intermediates, additives, specialty chemicals, and plastics.

The company is in the middle of a multi-year transformation and should in a few years generate around EUR 1.5 billion in EBITDA from highly attractive segments that are characterized by significant barriers to entry, high returns on capital, and long-term growth potential. Furthermore, side projects may create significant value in the future.

Mr. Market values the company based on its past economic profile and systematically ignores its far more profitable future. Lanxess can be bought at around 4x 2025 EBITDA, excluding any value from the aforementioned projects. The management team is capable, honest, and shareholder-oriented and may create far more value than is envisaged even by optimistic market observers.

The following transcript has been edited for space and clarity.

Samuel Weber: As always, I am happy and honored to participate in one of MOI Global's many phenomenal events. This year is quite special because my presentation doesn't entail one investment idea but four. The reason I am sharing so many ideas is not that I am overly generous but that the stock price of my last three ideas developed below my expectations.

Considering the operating performances of these companies, however, I definitely think they offer much better value today than when I first presented them. This is why I have almost 70% of my personal investment account in these companies.

Maybe I just get it all wrong because of severe confirmation bias and reality neglect, and you would be better advised not to listen to anything I'm going to say. This brings me directly to the standard disclaimer: I'm not your advisor, and you have to make your investment decisions by applying your own judgment based on your own analysis. Don't blame me if those ideas don't turn out the way I expect them to.

Having said this, let's take a look at one of my past ideas – Deutsche Bank. As I said last year in my presentation on Swatch Group, I continued buying Deutsche Bank well into 2019. Therefore, I have an average entry price of around 10 euros per share in my personal portfolio, or much lower than the almost 15 euros at the date of my presentation four years ago. Deutsche currently trades at around 11 euros.

When I discussed this idea in 2017 as a possible investment case, most people thought I was crazy – and I'm not talking about a slight majority of 51%, more like a sizable majority of

99.9%. I'm not talking about the light form of craziness, either. As it turned out, the bank needed another two years to find its footing. In 2018, Christian Sewing replaced John Cryan as CEO and announced a new strategy in mid-2019.

Since then, all key metrics have delivered a very positive performance. Core bank profits increased consistently in the past four quarters, while the losses in the capital release unit decreased during that time, allowing the bank to grow its last 12-month profits 15 times in the last two years. In the first half of 2021, core bank return on tangible equity was above 9%, taking into account a few adjustments, even above 10%. Group return on tangible equity stood at above 6% and 9%, respectively. Those are very good numbers that almost nobody thought possible a few years ago.

This strong operating performance has been reflected in a good share price development. Since the announcement of the new strategy, Deutsche Bank's stock price outperformed European peers and German stock companies in general and ranked among its US peers. Given its targets for the next year and considering its massive valuation discount – not only to its US but also its European peers – I consider it only logical that there is much further upside in this stock. Overall, I was over-optimistic regarding the speed of the turnaround, but I think I was right in the fundamental analysis, and I believe I will get a nice return on this investment over the full holding period.

The stock price of Holcim stands at practically the same level as it did when I presented the idea in 2018, including the after-tax dividend yield of almost 5%. We even get to a somewhat positive performance. However, this is much worse than what would be indicated by the company's fantastic operating performance improvements in the last three years. Holcim will reach all its 2022 strateg targets one year earlier than planned despite the corona crisis.

One year after my presentation in 2018, the company almost doubled its cash flow from operations while keeping a tight grip on capex. This led to massive improvements in free cash flow to 3 billion Swiss francs in 2019 and 3.25 billion in 2020, showing a further increase of around 10% in the first half of 2021. Free cash flow includes growth investments. To calculate true status quo owner earnings as defined by Warren Buffett in one of his past shareholder letters, we only have to subtract maintenance capex from operating cash flows, not the whole capex figure.

On this basis, Holcim generated almost 4 billion Swiss francs of owner earnings in 2020 – a number that will most probably increase again this year – which equates to a P/E of 8 times, taking into account significant minority interests. Also, the company managed to increase its return on invested capital to above 8% this year. This improvement will likely continue leading to a return on capital employed of more than 15% in the next 5 to 10 years in my own estimates.

In addition, I'm not convinced by the often-leveled accusation that the cement industry can't be sustainable. I recommend to everyone interested in this topic to look at Holcim's credible efforts to become net-zero and nature-positive in the next few decades. The company has set itself ambitious targets supported by the science-based targets initiative. As The Economist

writes, of more than 4,200 firms in the G20 Club of big economies that have disclosed their climate ambitions, only a fifth have committed to so-called science-based targets that will keep the world on track to meet the Paris agreement goal. That requires firms to start slashing emissions within years, not decades.

Furthermore, in 2020, member companies of the Global Cement and Concrete Association came together as leaders in the sector to commit to producing carbon-neutral concrete by 2050 in line with global climate targets, accelerating the CO2 reductions that have already been achieved. The association's recently published 2050 net-zero roadmap sets out in detail how – collectively, in collaboration with stakeholders and policymakers – it will fully decarbonize the cement and concrete industry and provide net-zero concrete to the world. Those efforts are also recognized by independent rating agencies, ranking Holcim among the most sustainable companies, not only in its own industry (building materials) but across all industries.

In my presentation in 2018, I was a little too optimistic with around 10% in my free cash flow and owner earnings estimates for 2020, mainly for four reasons. Of course, COVID played a major role as Holcim is a capital-intensive company that depends on GDP growth to operate successfully. The strong Swiss franc and divestments lowered the absolute level of earnings although the transactions were made at highly attractive valuations. Most importantly, however, my forecast was a linear extrapolation based on a few assumptions, but we know the world doesn't operate that way.

The important thing is that I was more or less right in my endpoint estimates for 2022. In all likelihood, the company will meet my expectations for owner earnings and free cash flows in the next year or at least come very close to it.

The massive operating improvement in cash generation is also reflected in the income statement, with EBIT increasing 66% in the first half of 2021. This helps the company to achieve its return on invested capital target of above 8% this year, which is one year earlier than planned and despite corona. It also allows the company to keep a healthy balance sheet.

The massive free cash flow improvements are sustainable and have been accomplished through lowering the unit capex costs, which will be reflected in the income statement over time. Talking to other investors, I got the feedback that Holcim is a capital-intensive commodity business, and I would miss the train of capital-light, fast-growing, new economy stocks. I disagree with this reasoning for several reasons.

First of all, even though cement is an undifferentiated product, it's not subject to commodity competition. Cement can't be economically transported further than a few hundred kilometers. The distance is even smaller for ready-mix concrete. Licenses to produce aggregates are in short supply. Holcim owns hundreds of local monopolies with significant barriers to entry and pricing power as those basic building products represent only a small percentage of the customers' building costs. Furthermore, structural trends drive significant volume growth. Most importantly, the CEO of Holcim, Jan Jenisch, has an excellent track record of value creation as CEO of the chemical company Sika. He will

continue to transform Holcim away from cement and basic materials.

The company's fourth segment – solutions and products – acquired the global leader of flat roofing systems at the beginning of this year. The segment now represents around 15% of total sales, growing at around 20% per annum. According to my estimates, it will represent 30% to 50% of total sales in a few years. Over the long term, it may even grow to 70% or 80%. Therefore, Holcim isn't a commodity company. It is the global leader in innovative and sustainable building solutions. The combination of decreasing capital intensity, a strong management team, and strong volume growth leads to increasing returns on capital.

What are my key takeaways so far? Over a few years, we can observe significant operating improvements by Holcim and Deutsche Bank that are not yet reflected in the share prices. There is no good reason for this discrepancy to continue indefinitely. This may strike you as a theoretical argument, but I consider it quite practical. We live in a world of entropy. Things that persist for no good reason usually dissolve in one way or another. However, irrationality can prevail for a long time. In the case of Holcim, the current trend towards sustainability clearly stands in the way of a rational valuation of the company. For me, that's fine because I use the tax-free dividend yield of almost 5% to increase my stake in the company. The cheaper the stock price, the more shares I can buy.

A stock can be sold only once for climate-related reasons. For every stock sold, there is also a buyer. Prices are determined at the margin and react strongly to small imbalances in supply and demand. Ultimately, however, cash matters in the stock market. Stock market participants care about earning money. The Swiss franc paid out by Holcim is worth as much as a Swiss franc paid out by any other company. The attractive dividend yield further strengthens this argument.

Sustainability clearly is an important – if not the most important – trend of the next decades, but it reduces the value of Holcim for its shareholders only if it negatively impacts the company's ability to pay out cash during its remaining lifetime. I'm quite confident this is not the case here.

First, Holcim sells sustainable products. After all, what does a sustainable world look like without building materials? Eventually, we may find a substitute for CO2-heavy cement, but this will take many decades. The innovation also needs to be accepted by the building companies' customers. Holcim makes massive efforts to become net-zero by 2050 by producing sustainable concrete through recycling, among other things. The biggest roadblock is the reluctance of its customers to buy those new products. In some areas of the world, like Switzerland, acceptance is quite high, and the share of sustainable products is therefore set to increase.

Most fundamentally, though, Holcim has the industry's lowest emissions per ton of cement, giving it a significant competitive advantage in a world of increasing CO2 prices. Higher CO2 prices are good for Holcim as the market prices cement based on its cost, and the demand for cement is quite inelastic, increasing the value of the company's relative cost advantage.

However, despite those solid reasons – or at least what I consider solid reasoning – Mr. Market doesn't adequately value the company's cash generation. I think that sooner or later it will. This is not a statement of faith; reality matters. For the stock market, this means that share prices will readjust over the long term to reflect cash flows. In case you doubt this, I ask you to give me one single example of a company with the kind of operating results and entry prices I showed for Holcim and Deutsche Bank that didn't end up being a good investment. I would love to see such an example but as long as I don't, I think those are very rational bets that will pay off handsomely in the not-too-distant future, though it may be longer in the future than we would rationally assume.

This is exactly what Buffett means when he cites Graham's "voting versus weighing machine" metaphor. Over long periods of time, earnings growth and dividends are all that matter for stock returns.

Reviewing quickly the last of the three past investment ideas, Swatch Group trades around 10% higher than at the time of my presentation last year. However, the stock price decreased significantly in the past few weeks, mainly because of worries about the possible reduction in Chinese demand and the general slowdown of the Chinese economy. While it is definitely too early to tell, I am personally not too afraid of the risk that a government crackdown might endanger the luxury goods sector. Both Xi Jinping and his wife are faithful Omega customers. If I am correctly informed, Mao also wore an Omega watch.

Chinese buyers love luxury products. This assessment is supported by recent statements from luxury group LVMH, which sees no impact whatsoever from common prosperity initiatives, but cultural change in China is a risk I consider real and mentioned in my presentation last year. We will see how this develops in the future, but I'm also not too concerned about a slowdown of the Chinese economy as I think the capitalist spirit in China is alive and well and will continue to power the growth of this economy. Charlie Munger recently acquired a significant stake in Alibaba and increased it in the past quarter to around 20% of Daily Journal's US portfolio, so I think he shares this assessment of China and its economy.

Now to the topic of this presentation, Lanxess. This is a leading specialty chemicals company with sales of around 6 billion euros in 2020. It currently has around 15,000 employees in 33 countries. The core business of Lanxess is the development, manufacturing, and marketing of chemical intermediates, additives, specialty chemicals, and plastics. It is listed in the leading sustainability entities – the Dow Jones Sustainability Index and FTSE4Good.

Lanxess operates four segments: advanced intermediates, specialty additives, consumer protection, and engineering materials. It has leading positions in each of these economically attractive and growing niches. The decrease in sales from 2016 to 2017 was due to the divestment of the ARLANXEO joint venture. Overall, we have seen a stable sales development, with a slight drop in 2020 due to the corona crisis. Lanxess is broadly diversified across end markets and industries.

In 2020, Lanxess generated around 50% of its sales in Europe, but this changed quite

significantly this year due to two big acquisitions. The company is production-heavy, employing more than 10,000 of its 14,000 workers in this area. For the most part in the past five years, the return on capital employed stood in the low double digits and decreased to 7.5% last year. These figures are based on pre-tax earnings and therefore have to be lowered by around 30% to arrive at the after-tax figure, resulting in an average return on capital employed of around 5% to 7% in the past few years. There wasn't much EBIT left after subtracting depreciation and exceptions from EBITDA, which is why Charlie Munger calls such earnings bullshit.

Let's zoom in on the different segments. The EBITDA margins vary widely among the different segments and have been influenced differently by the crisis. The consumer protection segment showed a better margin on higher sales in 2020 compared to 2019, making it the shining star last year. This is not surprising as Lanxess bought the Virkon brand in 2016 – the leading powder disinfectant with proven performance against a broad range of viruses.

This segment has been significantly bolstered this year with two major acquisitions worth around 2.5 billion euros and two smaller bolt-ons. Let's take a bird's eye view of how Lanxess transformed itself during the past five years.

Since 2016, Lanxess has sold three major assets for around 2.6 billion euros with an EBITDA margin ranging from 12% to 16%. It has also bought four major assets for almost 5 billion euros, with the post-synergy EBITDA margin ranging from 23% to 30% and generating a total EBITDA of around 600 million euros, implying that Lanxess paid an EV/EBITDA multiple of only 8 times to achieve a significant margin enhancement company-wide. The whole group is currently valued at around 5 billion euros, so this is a highly significant transformation, turning over more than 150% of the company's market cap in the last five years, significantly improving its profitability.

Two of those four acquisitions were announced this year, so their profits aren't included in my overview of the company segments. Also, Lanxess needs time to realize the significant synergies, and there are also three highly significant hidden assets in this portfolio. The value-creating transformation of Lanxess isn't yet reflected in the company's stock price, a familiar topic by now.

The sale of Currenta offers an insightful example of the systematic misevaluation of this company. The asset was sold for almost one billion euros in 2020 and was valued at zero in the company's balance sheet. There was no indication whatsoever that Lanxess would sell this asset or what it would be worth if it would choose to do so and for the market to foresee this significant gain. Yet, the stock market barely reacted to the news despite this gain representing around a quarter of the company's market cap at that time, indicating how the transformation of Lanxess is systematically ignored by investors. Of course, the whole stock market was overshadowed at the time by the impact of the corona crisis. I remember that time well because John hosted the Intelligent Investing in Crisis Mode Conference, where I spoke pretty much at the lowest point of the stock market. I think it was March 17, 2020.

The Lanxess CEO recently said that even though there is no problem child left in the

company, the transformation is far from over, and Lanxess will change in the next three years as much as it did in the last three. Considering how valuable this transformation has been so far, I'm hugely excited about how it will continue.

Let's now focus on the acquisitions Lanxess has made in the last few years, starting with Chemtura. Lanxess created a major global additives business which laid the foundation for its business unit specialty additives with a focus on flame-retardant and lubricant additives. Additives are economically very attractive products. Aside from growing global demand, they have to apply it only in tiny volumes to have a major influence on the qualitative characteristics of customers and products. They represent only a small fraction of the customers total purchasing costs, leading to both pricing power and the capital-light business model.

Furthermore, Lanxess is a highly disciplined and strategic acquirer that profits from strong operational synergies, allowing it to pay an attractive multiple of only 7 times EBITDA for this business. In acquiring Chemtura, Lanxess created a major competitor in the highly fragmented lubricant additives industry. This partly explains why Buffett bought 5% of Lanxess in 2017, a few months after the closing of the Chemtura acquisition. We know that the CEO of Lanxess flew to Omaha to meet Buffett, but we don't know what was discussed during that meeting.

In the flame retardants segment, there is an interesting business called Albemarle, which plays an important part in Lanxess' lithium project. In this segment, Lanxess has also created a leading global company. Access to highly concentrated bromine is a cost advantage, and Lanxess' production site in Arkansas benefits from access to this highly valuable resource. Other competitive advantages of this location include the social license to produce, the established supplier network, and contract contractual clauses to pass on raw material prices – though not energy costs, which is important in this environment given its one-quarter time lag. Many competitors don't enjoy these attractive contractual clauses. The currently exploding energy prices are definitely a headache, but they are manageable as far as I can tell.

The second important acquisition is that of Emerald Kalama Chemical. It is also both financially and strategically highly attractive. Lanxess paid an EV/EBITDA multiple of 9 times for a company with a post-synergy EBITDA margin of 28% and a strong return on capital. Strategically, it bolstered the company's consumer protection unit, which is a highly attractive segment. It not only grew in 2020 but also increased its profitability. The integration of Emerald Kamala is simple as only two production sites have to be integrated. It will increase the business unit's vertical integration.

The International Flavors and Fragrances (IFF) business generates an even higher EBITDA margin than Emerald (30%) but was a little more expensive to acquire, with an EV/EBITDA multiple of 9.6 times, including synergies. We have to take into account here that the multiple is calculated based on normalized earnings, and the synergies will take four years to materialize though the vast majority of synergies will be delivered by 2024. Of course, there is execution risk involved in all of these acquisitions, but the management's track record is very good in this regard, as demonstrated by the successful integration of

Chemtura.

Overall, this is a financially attractive acquisition, but the real excitement comes from looking at its strategic implications. By acquiring IFF's microbial control business, Lanxess creates a market leader in a growing, vertically integrated, asset-light, and high-margin business.

This attractive consumer protection segment will become the company's biggest profit engine, significantly increasing the quality of its earnings due to the decreasing importance of what I consider Lanxess' lowest-quality earnings from the engineering materials segment, which has a lower and more volatile return on capital. The customers of the consumer protection segment care about reliability and innovation, and Lanxess will be able to excel at both. Furthermore, the business is protected by high barriers to entry. To deal with the required regulation, you need lots of data, intellectual property, and significant scale to compete effectively. Quite interesting and positive is the fact that to finance this acquisition, Lanxess recently placed a five-year bond in the European capital markets with an interest rate of zero percent.

Let me now focus on a very important hidden asset with tremendous potential for value creation. Standard Lithium developed a technology to extract lithium from brine. This new way of producing lithium is very different from how it is done conventionally. An overwhelming quantity of today's lithium is extracted from liquid brine reservoirs located beneath Salt Flats (known as Salars), most of which are located in South America and China.

Lithium brine recovery is typically a straightforward but lengthy process that can take anywhere from several months to a few years to complete. Drilling is required to access the underground deposits. The brine is then pumped to the surface and distributed to evaporation ponds. It remains in these evaporation ponds for months or even years until most of the liquid water content has been removed through solar evaporation.

This conventional production method is much different from what Lanxess and Standard Lithium are trying to accomplish. Lanxess manufactures bromine from brine for its flame-retardant additives. This brine can also be used to develop lithium with the technology Standard Lithium has developed. In 2018, Lanxess announced a corporation with Standard Lithium with the aim of establishing a joint venture once the technology has been proven to work. Lanxess is the largest brine operator in North America and owns enormous brine reserves – enough to supply the whole world with the lithium it needs for decades to come – should this new extraction method work. The corporation with Lanxess saves Standard Lithium years of permitting and millions of dollars of capex. Once established, this joint venture will be owned 70% by Lanxess and 30% by Standard Lithium, which may increase its stake to 40% over time.

Lanxess' production facilities are located in South Arkansas, which has a decades-long history of brine production. Therefore, the company benefits from an established ecosystem that includes a social license to produce, an educated workforce, and a supply of cheap energy and specialty ingredients. The bolt-on direct lithium extraction technology that

Standard Lithium has developed to extract and purify lithium from the brine byproduct of existing bromine production facilities is clearly economically and environmentally advantaged vis-à-vis the conventional method of lithium extraction and will allow the joint venture to become a cost leader in the industry, which is extremely important when competing in a commodity business. The joint venture is clearly the most advanced lithium project in the US, with the clearest path to get into production.

During the next few years, profitability shouldn't be a problem even for high-cost lithium producers as the demand for battery-grade lithium for electric vehicles is heating up around the world to an extent that supply won't be able to keep up. Albemarle's plans for the future include annual volume growth of 35% to 40%. This indicates that if Lanxess and Standard Lithium manage to get a low-cost position in this industry via a new technology, the resulting business should be enormously attractive.

Answering my question at the investor call for the full year 2021, Matthias Zachert, the CEO of Lanxess, said, "Battery chemistry is a big field that we see profit and turnover wise only in three to four years to come. But we see there are opportunities, and those opportunities are big. I think, in the next three to four months, we will eventually be able to test the technology live. So far, due to corona, it was very burdensome. There were some improvements here and there, but we need to check the technology."

Since this statement, some good signs have emerged. The final investment decision seems to be imminent. As Standard Lithium recently announced, it is now in the final stages of running the only continuous 24/7 start-to-finish, brine-to-carbonate plant in North America. This explains the stock market's recent excitement about this company, of which Lanxess now owns 5% thanks to the recent preliminary conversion of its bonds into stocks. I'm personally very excited how this will play out in the future.

The cooperation with Standard Lithium isn't the only initiative Lanxess engages in when it comes to lithium-ion batteries. These batteries play a key role in future technology solutions for mobility, energy storage, and consumer electronics. Lanxess is one of the leading manufacturers of hydrofluoric acids and phosphorus chemicals – two important starting materials for lithium hexafluorophosphate, which acts as a conducting salt in electrolytes for lithium-ion cells.

Due to the massive buildup of production capacities for lithium-ion batteries in Europe, the demand for this electrolyte component will also grow strongly. With its integrated raw material base, Lanxess can ensure the supply of lithium hexafluorophosphate and electrolyte production in Europe. It has therefore entered an exclusive bilateral long-term contract with Guangzhou Tinci Materials Technology Co, starting in 2022. This will not suffice to satisfy the projected strong market growth, so we can expect more news to come.

The third exciting hidden asset that is fully owned by Lanxess but operated completely independently is CheMondis. It has nothing to do with batteries. CheMondis is the most active and strongest trading platform for chemicals in the European region, connecting buyers and sellers of chemical products online. This is a significant change from how chemical products are traded traditionally. The number of verified buyers and verified

sellers on the platform both showed very strong growth from 2019 to the beginning of 2021.

The CEO of Lanxess explained that he sees a lot of potential in this startup, but there has been some significant delay in rolling out monetization features due to a lack of suppliers on the platform since the beginning of 2021. There is currently a shortage of many chemical products, so sellers don't look for a digital platform to sell: They sell them directly to their most important customers. There is still a long way to go and a lot of work to do, but the potential is quite big. I am also very excited about this project.

Having looked at the company's operations, let's now try to put a value on it. Some key numbers I've used for this task are maintenance capex and growth capex, financial net debt, and cash conversion. I've also estimated the synergies from the enhanced acquisitions that have yet to be realized. Due to Lanxess' strong track record when it comes to integrating acquisitions, I consider these estimates quite realistic and even conservative.

Putting all of this together, we see that the company will earn around 1.4 billion euros in EBITDA in 2025. I calculate the intrinsic value for the year 2025 with two different methodologies that arrive at almost the exact same result: 12 billion euros. With the first method, I calculate the enterprise value based on the company's EBITDA, applying a conservative multiple of 10 times, and then subtracting estimated net debt to arrive at the intrinsic value. With the second method, I calculate the company's own earnings, which essentially equates to subtracting maintenance capex from operating cash flows. I multiply the result by a conservative multiple of 15 times.

Lanxess currently trades at an EV/EBITDA multiple of around 6 to 7 times. I apply a 10-times multiple on the expected 2025 earnings. Given the qualitative transformation Lanxess has undergone in the last few years (and will continue to undergo in the next few years) and compared to the valuation multiples of competitors, this company seems substantially undervalued even without any benefits from the highly promising initiatives I analyzed earlier.

As the CEO said in the full-year earnings call in response to my question, "We continue working on getting this company to a position that will definitely – a few years from now – be in a completely different league than where it operates today, also cash flow-wise."

I also want to highlight that Lanxess is a leader not only in its industry but across all companies from all industries when it comes to sustainability.

Last but not least, I want to point out the true source of value creation. Warren Buffett famously said that you should only invest in companies that even a fool can lead because someday a fool will. I fundamentally disagree with this statement. I think Buffett does, too. Maybe his eagerness to be funny and entertain got the better of him in this statement. After reading The Beginning of Infinity by David Deutsch – one of the top five books I have read, the other four being books by Steven Pinker – I recognized that the ultimate source of value must lie in human creativity. Of course, competitive characteristics like profit margins, barriers to entry, return on capital, etc. play a big role in estimating any kind of economic value, but in the final analysis, those things can be influenced by management decisions. If a

company is led by a capable, trustworthy, and shareholder-oriented management, there is no limit to the value it can create over the long term.

Considering this, it is a bit surprising that Lanxess' management doesn't own more shares of the company. I think they have this opportunity right under their noses and probably should take more advantage of it.

The following are excerpts of the Q&A session with Samuel Weber:

John Mihaljevic: Thank you so much for another wonderful presentation, Sam. I'm wondering how you think about future capital allocation and what the priorities should be, in your view?

Weber: This question has also been asked of Lanxess in recent analyst calls. I think the next few months – or even the next year – may be used to de-leverage, pay back debt, and integrate the companies acquired this year. They engaged in two major acquisitions, so they have a full agenda.

I also expect some important news when it comes to the joint venture with Standard Lithium. If that joint venture works out, Lanxess will scale conservatively. It will see what the demand for lithium is and will scale the production up quite conservatively over a number of years. There is not a huge capex drain on it, but over the long term, if the company decides to scale up significantly and if it sees the demand for lithium is what it currently expects it to be, this will also take quite some capex – several billion, I guess. Lanxess will have its hands full for the next few years without engaging in any acquisitions.

Mihaljevic: Given the investment case you made, it's amazing that the management team owns so little stock. Can you talk a little more about the key shareholders and anything interesting with regard to the board or engagement by the core shareholders?

Weber: The CEO was asked some time ago about the engagement of Warren Buffett. He said that Buffett is fully in line with the strategy, a long-term shareholder who is very happy with the development of the company.

From what I have seen since then, this happiness must have increased substantially by now. I'm not worried at all about this small stock ownership. I think it's a pity for the management. They should own more stock for themselves.

Matthias Zachert has worked a total of, I think, 13 years for Lanxess. He was the CFO, then he quit to become the CFO of Merck. He came back in 2013 to lead Lanxess as the CEO. If you listen to him and observe his actions, everything shows that he's deeply passionate about this company, and it's his life's work. He will make sure the development will surprise us positively, if that's possible with my expectations.

Mihaljevic: Do you believe that Lanxess could become an acquisition target itself?

Weber: That's an interesting thought. Maybe. I think that's definitely possible. If I had the money, I would absolutely buy the whole company. If you buy it today, the probability of the share price decreasing enough to compensate for any takeover premium is quite low, but the stock has proven very volatile in the past, and Mr. Market associates Lanxess with a basic commodity chemicals company.

We don't know, and this is definitely a risk. Imagine the stock price decreases by 50%, and Lanxess gets a takeover offer with a 30% premium – you lose a lot of money here. That's probably one risk, but I don't see which company would buy Lanxess as it has a leading position in its niches. I don't see a big chemicals company that would get significant operational synergies from this acquisition. Maybe to diversify, but not to get synergies.

Mihaljevic: Would there be anything to stop Berkshire from acquiring the company?

Weber: Zachert met Buffet and they spoke, but I can only speculate about what was discussed there.

I can't explain why the stake is so low. Maybe Buffet just wanted to appear in German newspapers to prove his willingness to acquire companies in other countries, not just in the US. We observed that willingness a few years ago, with Todd and Ted giving interviews for German newspapers. Maybe he wanted to acquire, and there was some reason why that didn't happen. Again, I don't know. I can only speculate.

Mihaljevic: I don't think anyone would turn down a free lunch with Buffett. After all, it's worth millions, as we know. Over the next six to 12 months, what are the key things you will be looking at to gauge how the thesis is playing out and whether the company is meeting or exceeding your expectations?

Weber: The most important thing is that it manages to integrate the acquisitions. I'd watch to see if it does and performs well in a difficult environment. It has contractual clauses to pass on material costs, but it doesn't have such clauses for energy costs. The energy costs have increased massively, and Lanxess needs to work on this contractual setup so that it can also pass on energy costs in the future.

The demand for its product is strong. It should manage just fine, but I'm focusing on how it executes and on its plans. Looking further out – like, two, three, or four years – I'd watch for significantly decreasing expenses that are not part of the operations, exceptionals. These have to go down significantly. It has exceptionals now to finance its hidden assets and its transformation, and that is fine with me. However, over the longer term, those need to disappear so that we can finally see the true cash flows of this company shining through.

About the instructor:

Samuel S. Weber is an independent wealth manager based in Zug, Switzerland. He is a passionate value investor, who is focused on generating long-term, market beating returns by investing in high-quality opportunities in the stock market (samuelsweber.com). Samuel holds a master's degree in strategy and international management from the University of St. Gallen and is a member of the Board of Trustees of HBM Fondation.