

Worth. Investing.

“Greece-ing the Global Capital Markets – Lending, Extending and Pretending”

Business Update

We continue to expand our business with a steady flow of new clients for which we are very appreciative. Our expectations for growth continue to be exceeded. The first four months have been busy but, at the same time, extremely gratifying. While the markets have not been boring they have provided us with numerous opportunities to take advantage of price volatility. This will work to your benefit over time as we buy exceptional businesses at attractive prices.

We plan to have our new and improved reporting package available to you for the period ending June 30, 2010 by mid July. Currently, we are scrubbing all client statements to ensure that all the “book values” are accurate. In the future, our reporting package will be available to you directly on-line for your convenience. This will assist you in following the progression of your investments. Our reporting package will evolve as we receive feedback from you. Many of you responded positively to our note providing you with direct on-line access to your account. If you have not responded and would like to have direct access to your account, please contact either Doretta or myself and we will have TD Waterhouse send you a password and instructions. This will allow you to view your accounts at any time. Transparency and trust go hand in hand and both are very important to us at RockLinc.

New Phone Number

After some interesting back and forth with Bell Canada (most of you can identify with us here) we were able to secure a phone number that incorporates part of our company name, LINC! Our new office phone number is now 905-631-LINC (5462).

Our old number will continue to work until the end of May 2010. This will make it easier for you to remember our phone number and pass it along to all your wealthy friends, and friends who want to become wealthy!

Investment Update

Watch out for Academics and Politicians

Now to the more stimulating data, the capital markets! It has been a hectic six weeks since our last communication both personally and also within the global capital markets. On a personal note, I had the opportunity in April to speak at Regent College in Vancouver. Regent is located on the campus of the University of British Columbia. I was asked to speak, in my role as senior fellow with Cardus, on the topic of the capital markets from a practitioner’s vantage point. The lecture was framed as a response to a recent papal encyclical written by Pope Benedict XVI called *Caritas in Veritate* (Charity in Truth). It’s always an interesting experience when you juxtapose intellectuals and practitioners. It reminded me of Thomas Sowell’s recent book called *Intellectuals and Society*. In that book, Sowell points out that the problem or risk you encounter with intellectuals is that they are mere “dealers in ideas” and their day-to-day work begins and ends with ideas. Unfortunately, most of their ideas are sealed off from necessary feedback with the external world of reality and, therefore, remain circular in their methods of validation making most of their ideas either useless or simply wrong. After returning from Vancouver, I was more appreciative of my vocation which puts my ideas to a daily test in the crucible of the rough and tumble capital markets! I found

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out, first-hand, how hard it is to argue about the ineffectiveness and overreaching nature of government coupled with the crippling level of taxation to people who live off the public dole in one form or another! It's amazing to me how academia blames everyone else for the problems we experience in the world when most of the bad ideas and theories originate in the halls of our universities!

Take the debt challenges we face today. Most are the direct result of our economic wizards spinning their ridiculous Keynesian ideas. These ideas have been framed within the context of a false or contrived world and then foisted into the real world, aided and abetted by politicians, with devastating consequences. One question we need to always ask is: why do we transfer decision making away from those with personal experience who are the closest to the issues and have a stake in the outcome to those with little personal experience, far away from the issues and little to no stake in the outcome? One example of this was a recent interview on CNBC with James K. Galbraith, son of the "esteemed" economist John Kenneth Galbraith. James earned a B.A. from Harvard and a Ph. D. from Yale University in Economics which makes him particularly dangerous. In the CNBC interview, which pitted him against Peter Schiff, the "practitioner", and a very astute one, Galbraith suggested that the U.S. does not have a debt problem. He stated that since their overall annual interest cost on their debt had dropped year over year (despite their total debt sky rocketing) it showed that investors around the world were more than interested and comfortable in supporting their debt. He said that the U.S. could continue to rack up more debt without any major concern at this time. Galbraith even suggested that if the U.S. could borrow all its money on the short end of the curve at near

zero interest rates they should go ahead and do it!

The obvious question: how can someone with such credentials make such ridiculous statements? The average person knows the obvious - that the U.S., along with every developed country in the world, has a massive debt problem, point period! You literally do not need a Ph.D. in economics to grasp this! Also, no person, no company, and no country with large amounts of debt should ever convert all their debt to short-term debt, and be forced to roll their debt over every 3 - 6 months! Can you image the U.S. having to roll its \$13 trillion debt plus its \$1 trillion plus deficit over in the next 3 - 6 months? Galbraith is suggesting that he sees no problem with the U.S. running their unsustainable finances in the same way the now bankrupt American consumer ran their mortgages, as adjustable rate mortgages! Once rates go up or the lenders figure out you can't pay, you are in trouble! Of course, Galbraith's real presumption is that the government can simply do whatever it wants. For him, this includes counterfeiting or printing its way out of its debt obligations. This is nonsense and academic drivel at its worst. In the end, this is theft on the part of the government as it steals from the owners of wealth in its country either by confiscatory taxes or the creation of inflation and destroying the integrity between creditors and debtors. This brings us to the "Greece-ing of the Global Capital Markets".

Sovereign Debt - A Major Problem

In our last report in March, I stated that the greatest challenge facing the global capital markets is by far the level of sovereign debt and the wrong-headed economic policies being advanced by the majority of governments around the world. When we use

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the expression sovereign debt, we are referring to the debts of governments: federal, state and municipal. The recent financial crisis that hit the world's financial institutions merely shuffled their bad debt to the public sector or sovereigns. The problem is most nations or sovereigns do not have the balance sheets to take this risk. Countries, such as the PIIGS (Portugal, Italy, Ireland, Greece and Spain), will never be able to pay down their debt without writing off substantial amounts of it while, at the same time, reducing their entitlement obligations. Greece is merely the first, or may I say, the tip of the “greasy slope” which will force country after country to begin the process of dealing with their massive debts, colossal deficits and outrageous entitlement promises primarily in the form of pensions and healthcare. The folks who lent these overleveraged countries the money should take the haircut, not taxpayers. In the case of the PIIGS, that is largely European and American financial companies. This is why we own very few non-Canadian financials and have minimal exposure to life insurance companies (who hold vast amounts of sovereign debt and have to make long-term investments to match their long-term liabilities, a horrible business in the face of things to come). We do not want to own any companies that have holdings of European debt from the PIGS, UK or Japanese debt. Japan is on an unavoidable decline given its debt and demographics.

At some point in the future there are going to be some serious write-offs taking place! Greece is simply getting us all ready for the inevitable! According to the proposed bailout announced on May 2, 2010, Greece, in 2014, will still be running a 3% plus deficit as a percent of GDP in a country that is dying (deaths far outnumber births), and where real GDP growth is negative (without government debt) and getting worse. The bottom line is

that Greece will, in the future, have to default and they are not alone. In our new brave world of forced “austerity”, the name of the game will be how to renege on your obligations! This means that financial companies should be purchased with copious amounts of caution and due diligence or simply avoided. When purchasing any financial businesses we only consider well managed and strongly capitalized retail banks, some fee based financials and the occasional property and casualty business. Some examples of financial businesses we own include TD Bank (retail banking), Bank of New York Mellon (fee-based custody) and Market Insurance (property and casualty insurance with an exceptional money manager Tom Gayner).

The current attitude by our intellectual elites that we can somehow keep lending, extending the terms and pretending that the mess will go away is utter nonsense. Only the well trained in econometrics are obtuse enough to put this sort of foolishness forward. We cannot, as investors, take these people seriously. The bottom line is simple: governments around the world are dishonest, and the central bankers are worse than dishonest. Bill Gross, the head of PIMCO, stated it clearly in a recent report, “Don't trust any government and verify before you invest.” The claim that something is “backed by the government”, as Eric Sprott recently wrote, means nothing anymore. Expect to see money continue moving from indebted regions to less indebted regions putting greater and greater pressure on more and more weak countries to either renege on their obligations or inflate them away. This, unfortunately, is the reality we must live with and invest prudently into! This is clearly why more and more money is moving into hard assets. Fiat currencies and financial assets that are not backed by serious and meaningful collateral should be shunned!

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Making Money Despite our Leaders

As we have discussed earlier, our attitude is to take a longer term view and own exceptional businesses that operate in essential industries, with pricing power, scarce assets and with irreplaceable franchises. One example of this type of business is the Canadian Oil Sands Trust which owns 36.74% of the Syncrude Project in northern Alberta. The overall energy needs of the global economy continue to grow. At the same time, cheaper and easier access to energy reserves are becoming harder and harder to find. This means that any business that controls vast amounts of oil reserves in a safe country should see the capital value of those assets continue to grow. Most people do not realize that the Syncrude Project has over 5 billion barrels of proven and probable reserves and another 5 - 6 billion barrels of contingent reserves giving them up to 80 plus years of reserves at the current rate of production of 350,000 barrels per day.

Validation concerning the importance of the Albertan oil sands to the global economy was recently seen in the price paid by the Chinese to buy ConocoPhillips' 9% stake in Syncrude. The Chinese are showing their skepticism when it comes to holding fiat currencies. They would much rather own hard assets! The China Petroleum & Chemical Corporation, Asia's biggest refiner, snapped up ConocoPhillips stake for USD\$4.65 billion. Last year, they spend over USD\$32 billion securing a number of natural resource businesses and it is expected to be even larger this year. What interested most investors, especially those in the Canadian Oil Sands, is the valuation placed on the 9% stake in Syncrude. The price paid by the Chinese is equivalent to approximately \$37.50 for the units of Canadian Oil Sands. That means your units are trading at a significant discount!

The Greece situation and the overall sovereign debt challenges do nothing to change our investment principles. Rather, they merely shape the types of businesses and industries in which we seek to maximize our exposure. In a nutshell, we will continue to buy scarce and essential assets that the government cannot print! The world's debts are not going to magically disappear and at some point in the future will be paid down by either defaults or inflation. We will continue to buy businesses that are least affected by this madness.

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