ROCKLINC

Worth.Investing.

Licence to Print Real Money

"I want to be a standup economist, because isn't money funny? Actually, without gold backing our currency, it's all funny money." ― Jarod Kintz, *This Book is Not FOR SALE*

A. Introduction

During the past two decades, the major "Western" economies have changed dramatically. The evidence for this change is readily observed when one considers the massive accumulation of debt during this period, coupled with the decreasing standard of living. As you might expect these factors are inter-related. Any economy that grows its debt beyond its capacity to service it will eventually face a decreasing standard of living.

Let's consider for a moment the concept of one's standard of living. How is a country's standard of living calculated? It is calculated by adding up the total value of output in a country, plus net exports, and then dividing this number by the total amount of labour used. Over time, the standard of living is driven by the productivity of a country, or output per hour of labour. A nation that produces more per hour of labour will experience an increasing standard of living.

What drives productivity and what underpins the ability of a nation or economy to produce more per hour of labour? Ultimately productivity is driven by two key factors: the capital base, and the quality of the labour force. These two productive factors drive long-term economic growth and productivity, which in turn, drives the standard of living! Let's take a brief look at these two productive factors, the capital base and the quality of the labour force.

(a) The Capital Base

For an economy to grow and produce an increasing standard of living it must be committed to savings and making investments in long-term capital! Capital investments include investments in homes, tools, machinery, technology, schools and factories. Economists refer to this as private domestic investment. Any economy that is not committed to savings and capital investments will amputate its long-term ability to increase its standard of living and grow.

The primary problem today is that given the monetary policies of debt, debt and more debt, supported by "zero" interest rates, the focus on long-term capital accumulation has waned substantially in favour of short-term, debt based consumption.

"When the most persistent, most aggressive, and most sizeable actions of policymakers are those that discourage saving, promote debt-financed consumption, and encourage the diversion of scarce savings to yield-seeking financial speculation rather than productive investment, the backbone that

supports a rising standard of living is broken."[1]

John Hussman draws our attention to a point that we have emphasized for over five years, that the debt financed boom, of the past 40 years, (which intensified during the past 15 years) is undermining our long-term capital base! In essence, as an economy, we continue to "run our balance sheet through our income statement" forgetting that consumption in the future requires investments today! If we don't invest today we will be forced to consume much less in the future.

Take the United States as our proxy. Since 1999 the real gross domestic investment has expanded at an annual growth rate of approximately 1.4%. Compare this with a real annual growth in the preceding 50 years of almost 5%! The following chart shows that the total gross domestic investment in the U.S., in 2015, is still no greater than the level reached in 2006 despite a large increase in the U.S. population.

Chart 1. Real Gross Domestic Investment (2009 Dollars)

What is happening? Why are we not committing long-term capital to increase our productive capacity for the future? There are many reasons we could proffer to answer these questions. Here are four reasons looking through the prism of our current monetary policies.

[1] Hussman, John. "The Ponzi Economy" (Advisory Analyst – September 21, 2015)

First, structurally low interest rates feed a culture of instant gratification. Present consumption takes priority over long-term investing (investing in productive capacity). Human behaviour is negatively shaped in an environment of artificially low interest rates and money printing (monetary debasement)! Frugality, thrift and prudence are replaced by debt, dependence and overconsumption. Debasement of money leads to the debasement of manufacturing and production.

We continue to learn the hard way that economics is a metaphysical science not a mathematical one! Moral values are more important than physical assets, because it is the moral and ethical values of a society that will determine the quality and type of physical assets that will be invested in! A society that allows it's monetary authorities to "steal" from savers, reward debtors and debase their money will not be a society that is prudent in it's allocation of scarce capital to productive investments!

Second, it is too easy for governments to promise all the wrong services, even when they cannot afford them and must finance their spending by running large deficits! While government deficits may for a short period maintain the illusion of prosperity, soaring indebtedness will eventually lead to a crash in the value of debt and negatively impact the total economy. **The lack of fiscal discipline imposed by an informed and virtuous electorate on governments leads to increasing government dishonesty, indebtedness, and bureaucracy.** As governments become larger, they consume more of the economy leaving less for judicious capital investments. Worse, large governments undermine personal freedoms and liberties, which leads to stagnation in the economy through the growth of unnecessary rules and regulations.

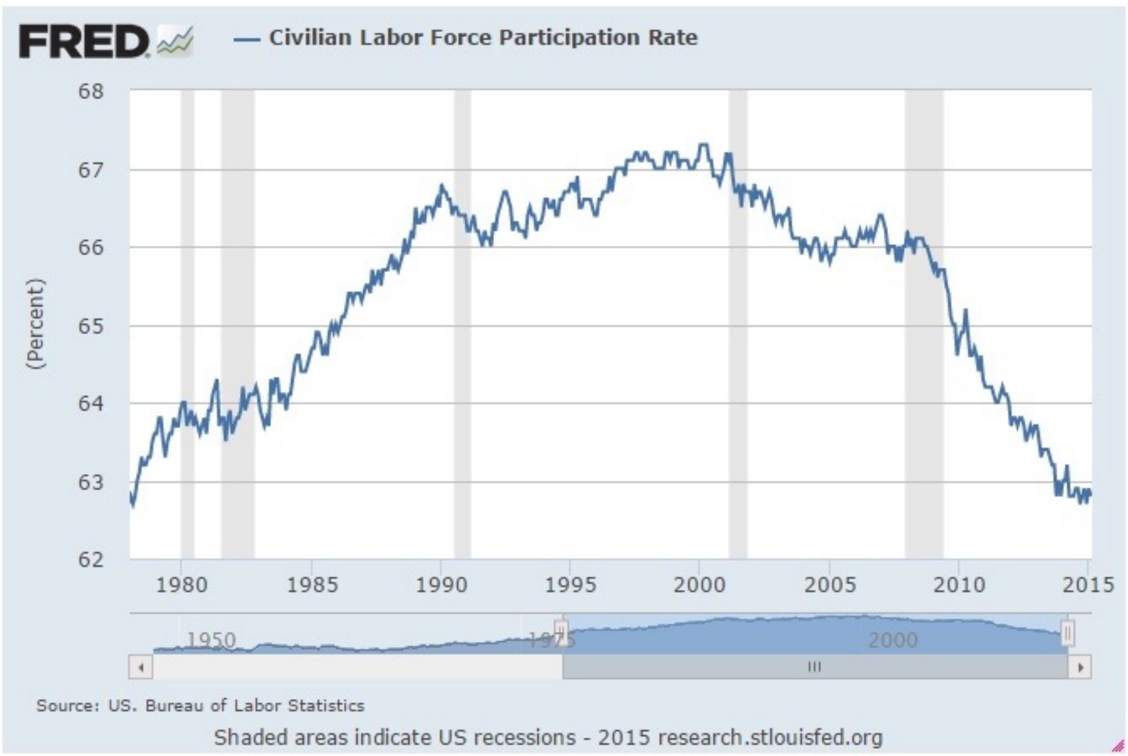
Third, low to zero interest rates punish savers and reward debtors. The longer this goes on, the greater the misallocation of capital. Examples of this misallocation at the corporate level include an inordinate dependency on share repurchases (shrinking the number of shares outstanding) to drive earnings per share, and increasing dividends to unhealthy levels in order to satiate income-starved investors. Corporate resources directed to share repurchases and high dividends often come at the expense of long-term investments in capital.

Fourth, the combination of low interest rates and the printing of money lead to asset price inflation (value of stocks, bonds and real estate increase for a time) while wages and productivity do not grow. This hurts all those who do not already own financial assets and real estate. Over time this leads to an unjust distribution of wealth. Current monetary policies are eviscerating the middle class and increasing their dependence on a growing and increasingly decadent State.

(b) The Labour Base

Using the U.S. economy as our base line and proxy, we see that during that last 15-year period, the U.S. labor force participation rate has collapsed from a record high to the lowest level since the 1970's. (The labour force participation rate is defined as the ratio of the labour force to the working age population, expressed in percentages.)

Wages and salaries have also plunged, over the past 15 years, to a record low share of GDP, with real median household income actually contracting by a cumulative 9%! While we may be surrounded by more "things" too many of these "things" have been debt financed and imported from cheap labour jurisdictions giving us the illusion of ongoing prosperity. But when we look under the surface we see that all is not well, including the massive offshoring of large swaths of our manufacturing, and formerly high paying jobs, to low cost labour jurisdictions.



The key point is this: the major Western economies have shifted course from one of productive capital accumulation to one of reliance on the continuous expansion of debt. Unfortunately the level of debt throughout the global economy is now unsustainable. This is what some call "the Ponzi Economy" and it is not just Greece's problem (or Puerto Rico)!

"The Ponzi Economy is one where domestic workers are underemployed and consume beyond their means; household and government debt make up the shortfall; corporate profits expand to a record share of GDP as revenues are sustained by household and government deficits; local employment is replaced by outsourced goods and labor; companies refrain from productive investment, accumulate the debt of other companies and issue new debt of their own, primarily to repurchase their own shares at escalating valuations; our trading partners become our largest creditors and accumulate trillions of dollars of claims

ROCKLINC

Worth.Investing.

that can effectively be traded for U.S. property and future output; Fed policy encourages the yield-seeking diversion of scarce savings toward speculation in risky securities; and as with every Ponzi scheme, everyone is happy as long as nobody seeks to be repaid."[2]

If you wonder why the economy "feels like it is fine", despite the undermining of the capital base and the hollowing out of its middle class, it's because we are covering the shortfall with the endless issuance of cheap and perpetual debt that must be rolled over and over and over! There will come a time when the debt is too large to rollover. **A quick glance at Europe and the ongoing challenges surrounding Greece are merely a precursor of what to expect from many more countries in the years to come.**

At some point we must expect the "gradual" or "not so gradual" normalization of interest rates and a return to more fiscal and monetary sanity. **We invest with this backdrop in mind.** Our focus is to find investments that can hedge some of this risk and increase in value despite these challenges. Let's take a moment to discuss one of these areas.

B. Licence to Print Real Money

The ultimate investment is one that produces a compounding cash flow stream that protects and grows your purchasing power, regardless of the economic backdrop. Given the health of the global financial system, which is gasping under the weight of unsustainable levels of debt and government bureaucracy, it is essential that we invest carefully and find such cash flow streams.

We often tell our investors that our goal is to convert their debasing paper money into essential, scarce and tangible assets, with low leverage and limited counterparty risk.

One of the areas we believe is an important area to invest in is the precious metals sector and in particular gold and silver. Both of these precious metals have proven over time to be excellent ways to protect investors from the debasement of money, **particularly at times when debts levels are excessive.** The problem is, what is the best way to gain exposure to these two precious metals? After all, investing in gold and silver mining companies is difficult and can be very risky. Some of the obvious risks of investing in miners include geopolitical risk, capital cost overruns, safety conditions of the mine, estimating the size of the resource base, regulatory and environmental challenges along with the volatility of the underlying bullion prices. Because of these risks many investors stay away from the sector, especially long-term value investors who appreciate the financial reality that few mining companies make any money, and those few that do, seldom return their cost of capital!

---

[2] Hussman, John. "The Ponzi Economy" (Advisory Analyst – Sept. 21, 2015)

ROCKLINC

Worth.Investing.

Fortunately we believe that there is a "sane and sensible" way to get exposure to the gold and silver space and it is through royalty or streaming companies that focus on the financing of gold and silver projects! In essence the royalty and streaming companies provide upfront capital in return for either a portion of the miners revenue stream or the right to purchase a percentage of the mines production at a fixed price. The only difference between a royalty and a stream is that the latter includes a fixed and ongoing payment for every ounce of precious metal purchased. Currently our investors have exposure to the four leading royalty and streaming precious metals companies: Franco-Nevada Corp, Royal Gold Inc., Silver Wheaton Corp and Sandstorm Gold Ltd.[3] Each company is highly profitable, and each one is currently expanding their business, in the midst of one of the worst markets for gold and silver miners in recent history.

One of the reasons we love these business models is that they actually thrive and create their value in the most difficult environments! The current market conditions are wonderful for these types of companies. Given the low gold and silver prices most miners are now cash strapped and in desperate need of capital. In today's environment with banks on the sidelines and equity markets not interested in the miners, royalty and streaming companies are stepping in and cutting wonderful long-term contracts. Deals consummated today will compensate patient long-term investors with extraordinary returns over the next 3-5 years.

Bottom line: This is one of the best opportunities we have seen in years! This also helps to explain why some investors refer to royalty companies, (especially in this market), as the "mafia of the precious metals industry". They literally have a licence to print real money! The power and profitability of their business models will be fully revealed when precious metal prices improve! In the interim they are building amazing value in a market that for the moment has turned its back on the miners. Today is a perfect opportunity to build positions in these financiers!

In order to better appreciate the quality and power of their business models we have listed five key advantages of the royalty and streaming model.

First, portfolio diversification: companies over time build can build large numbers of interests in high-quality, long-life mines, development projects and exploration properties. In some cases the companies in our client portfolios have interests in more than 100 producing properties. No miner can provide this level of diversification.

Second, no cost exploration upside: firms enjoy the benefit of reserve growth, as mine operators seek to extend mine lives by exploring for additional reserves at their existing mine sites. Royalty companies are not required to participate in the exploration expense or pay any additional compensation when operators discover or add additional reserves at existing mines. Royalty and streaming companies have a long-term call option on all new reserves discovered at a mine site, even 50 years down the road!

[3] Rocklinc investment team conducted a conference call with the CEO of Sandstorm Gold, Nolan Watson, on June 11, 2015. This call confirmed many of the points made in this quarterly report in regards to the current deal flow and opportunities for the royalty and streaming companies.

Third, less geopolitical risk: not only can country risk be diversified it can be minimized, by focusing on the safest jurisdictions. The firms we are invested in derive the majority of their revenue from "safe countries."

Fourth, fixed-cost investments: companies do not have to contribute to capital or operating costs at the mining operation in which they have an interest beyond their original investment. Therefore, companies are not exposed to inflationary pressures that can erode the rate of return expectations and profit margins of operating mining companies. The business model of a royalty company is amazingly scale-able and highly efficient. Firms can double and triple in size without needing to add any new employees. The profit margins and revenue per employee within these firms are some of the highest when compared to all other industries.

Fifth, strong balance sheets, substantial cash flows and consistent dividend payments.

While most investors are shying away from the precious metals sector, despite the monetary instability, we are bargain hunting and selectively dollar cost averaging in the leading royalty and streaming businesses. If there was every a time to be building a substantial position in these companies it is now. There are virtually no other businesses that provide investors a compounding revenue stream tied directly to precious metals prices. You need to let that sink in for a moment. If there is a financial "mishap" or "debt reset" in the future, gold and silver prices will adjust to reflect the debasement of money. This means that they will protect your long-term purchasing power! When we invest in royalty and streaming companies their cash flow not only compounds through the building of excellent contracts with miners, it will skyrocket and adjust immediately to rapidly rising gold and silver prices in the event of a currency crisis! Because of this, there is no other business that can be said to have a license to print "real money" since no other business derives their direct cash flow stream from the ultimate real time currencies, gold and silver!

What is most exciting today is that these businesses can be purchased at terrific prices based on some of the lowest precious metals prices in years. If we are correct and gold and silver move up substantially as the global economy is forced to deal with the debt overhang the values of the royalty and streaming companies should rise "big time"! In the interim, we must have intestinal fortitude to go against the masses.

C. The First Half of 2015

Since our last quarterly update, the S&P 500 and the TSX Composite both moved lower. For the first half of the year both indexes are largely flat with less than 1% moves from where they began the year. On a price/earnings basis, the S&P 500's valuation remains rich by historical standards. The index closed at 2,063 at the end of June and has continued to weaken earlier in July. This implies a price/earnings ratio of approximately 19.0, using trailing-12-month operating earnings. According to data collected by Morningstar markets have traded below this level over 65% of the time since 1989. Such high valuation levels can only be justified in an environment of very low interest rates and high profit margins. The problem, as we see it, is that interest rates will eventually move up and profit margins of companies will come under pressure. To assume otherwise would reject long-term historical valuations and leave our investors without an adequate margin of safety. As a result we remain cautious with cash on the sidelines ready to take full advantage of any market weakness.

Across all of our ROCKLINC clients we averaged a 4.1% gain during the first half of the year and have progressed by 8.1% since July 1, 2014 (last 12 months). These numbers include an allocation of approximately 65% equities and 35% fixed income and cash. Please note that portfolios and hence returns will vary by client based upon risk tolerance and each client's respective asset mix.

	June 30, 2015	Quarterly Returns	Year-To-Date
S&P/TSX Composite Index	14,553	-2.30%	-0.50%
S&P 500 (USD)	2,063	-0.20%	0.20%
Dow Jones Industrial Average	17,620	-0.90%	1.10%
FTSE TMX Canada Universe Bond Index	984	-1.71%	2.37%
CADUSD	$0.8014	1.08%	-6.91%
Brent Crude Oil Spot	$61.20	12.20%	9.60%
NYMEX Gas - 12 month	$2.82	-2.73%	-34.26%
Gold (USD/Oz.)	$1,169	-1.50%	-1.40%
Silver Spot (USD/Oz.)	$15.69	-5.00%	-3.60%
Copper Spot (USD/lb.)	$2.61	-5.10%	-9.70%

Source: Canaccord Genuity, FTSE TMX Canada Universe Bond Index, Google Finance

Other important price changes during the first half of 2015 included the decrease in our Canadian dollar against the US dollar of approximately 6.9%. As we have stated in previous reports we expect our dollar to continue to trade within a range of 75-85 cents. When adding US dollar investments to our client portfolios we will be very sensitive to currency moves and attempt to buy US dollars at the best prices based on our range. Overall oil has rebounded from the lows reached early in 2015 and seems to be largely range bound. Our holdings in the energy space (oil and gas) remain relatively small, approximately 4% of our total investments, and we are not looking to add to our positions given the overall outlook for supply and demand. As we have communicated previously, our oil and gas holdings are well positioned geographically, vertically integrated, lower cost producers and pay healthy and sustainable dividends.

ROCKLINC

Worth. Investing.

Lastly, while industrial metals continue to be shellacked by the weak global economy, precious metals were little changed over the first half of the year. In US dollar terms gold was down 1.4% and silver gave back 3.6%. Both gold and silver were up in Canadian dollar terms given the drop in our dollar. We continue to believe strongly that a position in gold and silver businesses, particularly in the royalty and streaming companies, is an important hedge or protection against the unsustainable levels of debt around the world. What is most exciting about these companies is that they are trading at very attractive prices in the midst of a market that remains priced to perfection. There is only one problem with investing in the gold and silver space in 2015 and that is the market sentiment! Currently it is one of the most hated places to invest! The good news is that this is the sector where we will make the best returns going forward! Buying despised businesses can be very profitable!

Moving forward we will continue to prudently add to our positions in Franco-Nevada, Royal Gold, Silver Wheaton and Sandstorm as opportunities emerge and within strict weighting allocations in your portfolios. Currently we have approximately 5.5% of our total assets in the foregoing businesses. If prices remain weak and global instability continues to rise we will slowly take this weighting up.

D. Summary

Given the challenges ahead we will remain conservatively invested in strong companies, operating in strong long-term growth industries. We are prepared to take advantage of market swings and welcome volatility! We continue to compile a list of exceptional companies we would love to own, but most at lower prices. Over the past three months we have either met with or talked on the phone with over a dozen companies. We are pleased to add new companies, from time to time, that are attractively priced and at the same time, have significant capital growth potential. Currently we are building a significant position in an innovative finance company providing much needed capital to the agricultural industry. We will have more on that topic in an upcoming report.

As we have stated in other communications, the best offence is a good defense, and we have some great companies to provide us cover in a world that is increasingly under the influence of “monetary insanity”. We also own a handful of companies that are growing very quickly and finding wonderful opportunities to deploy their capital. We continue to carry significant cash positions that can quickly be put to work! We appreciate your support and are committed to providing the highest levels of return consistent with a disciplined approach to risk management!

ROCKLINC INVESTMENT PARTNERS INC.

Contact Information

ROCKLINC INVESTMENT PARTNERS INC.

4200 South Service Road, Suite 102

Burlington, Ontario

L7L 4X5

Tel: 905-631-LINC (5462)

Fax: 905-333-9116

Jonathan Wellum	jwellum@rocklinc.com	(ext. 2)
Paul Farrugia	pfarrugia@rocklinc.com	(ext. 3)
Doretta Amaral	damaral@rocklinc.com	(ext. 1)