Covid-19 A License to Print!

A. Fourth Quarter Review

US Market

US equities gained over the quarter. The majority of the move was in November due to the positive vaccine news which had markets looking ahead to a time when economies would be reopened and back to "normal". Talk of a $900 billion stimulus package announced in late December also had a positive impact on equity markets. The Federal Reserve continued to reinforce its supportive message, by stating it will maintain the current levels of money printing at approximately $120 billion per month and hold interest rates at near zero for as far as the eye can see! COVID-19 has provided the Fed with a license to print! During the quarter, economically sensitive sectors made the strongest gains, while more defensive sectors, which had performed strongly earlier in the year, made modest progress.

Looking forward, following a winter slowdown, widespread vaccination should allow U.S. growth to rise later in 2021, precipitating a relatively fast rebound from a deep and self-inflicted recession. However, the recoveries for GDP, jobs and inflation are all on different timetables and will be influenced by different policy decisions. A 50-50 US Senate could imply less fiscal stimulus but that remains to be seen given the reckless spending habits of both Republicans and Democrats. One thing is certain, federal debt will continue to grow sharply, threatening greater fiscal stress within the next few years.

International growth will depend on regional pandemic trends early in the year but should broadly accelerate once vaccines are distributed and herd immunity is reached. In addition, weaker trade policies coming from the Biden administration coupled with stronger international economic growth should cause U.S. dollar weakness. Earnings should rebound, but overall U.S. equity returns will be constrained by high valuations and extraordinary levels of debt. With returns constrained, investors need to proceed with caution and pay greater attention to valuations and quality of company balance sheets.

Eurozone

European equities gained sharply during the fourth quarter, driven largely on the news of effective vaccines. As in the US and around the world, sectors that had previously suffered the most from the economic impact of the "pandemic", such as energy, financials, retails and travel related businesses, were some of the top gainers. However, as the quarter drew to a close rising Covid-19 infection rates saw many European countries begin to tighten their restrictions again. Given the economic damage of the lockdowns, EU leaders approved the landmark €1.8 trillion budget package, including the €750 billion recovery fund, after overcoming opposition from Hungary and Poland. Of course the EU does not have this money and will do what every country is doing which is relying on its central bank, in this case the ECB, to print the money! COVID-19 has given the ECB a license to print! At the very end of the quarter, the EU finally agreed to a Brexit trade deal with the UK, four and a half years after the UK voted in favour of Brexit.

United Kingdom

UK equities performed well over the quarter reversing some of the underperformance that they had suffered versus other regions during the global pandemic's initial stages. The market responded well to November's vaccine news and then again to the Brexit trade deal, with domestically-focused areas of the market outperforming. At the time of writing this update Britain has imposed yet another lockdown which will hinder economic growth during the first quarter of 2021 and drive the country further into debt. But no worries, the Bank of England will grease the system with lots of new money, spun out of thin air. COVID-19 has given them a license to print.

Japan

Japanese equities rallied in the quarter, driven by vaccine-related news, which had many market commentaries pricing in a return to normalcy sometime in mid 2021. The results of the US presidential election also led to some positive gains. It appears that the new administration in the US will focus less on what is best for the US and return to the pre-Trump days of allowing abusive trading practices that harm the US and favour large trading nations like Japan. The style reversal seen in most markets (shift from momentum stocks to value stocks) has not yet materialized in Japan, with only a brief outperformance for value stocks. In Japan small caps/businesses underperformed sharply in the quarter. The focus now is on the vaccine roll out, Japan's general election timetable and the timing of a full corporate earnings recovery which will depend largely on the strength of the overall global economy.

Asia (ex-Japan)

The MSCI Asia ex-Japan Index rallied strongly with the Japanese index, reaching levels not seen since 1990! The South Korean index was the best-performing in the region, aided by strong gains from the technology sector. Indonesia, Taiwan, the Philippines and India also finished ahead of the index. Malaysia, China and Hong Kong generated more modest gains and underperformed. In China, ongoing tensions with the US, coupled with anti-trust moves weighed on sentiment. The Trump administration continued to keep maximum pressure on the Chinese government along with several Chinese companies.

B. North American Equity Market Statistics

During the fourth quarter, the Canadian equity market as measured by the S&P/TSX increased by 9.0%. Year-over-year, the index increased by 5.6%, including dividends. The S&P/TSX index has lagged many of the world's major stock markets over the past 15 years and over the past 5 years generated a return of 8.5% per year compared to the S&P 500 at 15.2% per year. Despite this mediocre performance, ROCKLINC has successfully generated returns over the past year and for longer periods that have kept us ahead of the overall Canadian equity market index. We have managed to do this by avoiding weaker performing stocks and minimizing our exposure to underperforming sectors.

During 2020, our basket of Canadian companies outperformed the index by approximately 22.7%. Clearly this level of outperformance cannot be maintained, but we will take it when available! This is another reason why we love active investing over passive index investing! Our overweight position

in the gold and silver royalty companies, along with our infrastructure holdings and technology stocks, added significant value over the past year. Our underweight position in banks and energy stocks helped us avoid some of the weaker sectors in the S&P/TSX during the year. Regardless of the short-term noise, our focus is on the long-term economic fundamentals of the companies we own.

In terms of the S&P/TSX, all the sectors except for two generated positive returns during the fourth quarter! Here are their returns from best to worst: Healthcare (29.9%), Consumer Discretionary (20.4%), Financials (15.4%), Energy (13.0%), Real Estate (8.4%), Information Technology (7.6%), Industrials (6.7%), Utilities (4.6%), Telecommunication Services (2.4%), Materials (-4.0%) and Consumer Staples (-6.0%).

Pertinent market action during the third quarter of 2020 and during the last 12 months is captured in the following table.

	Dec. 31, 2019	Sept.30, 2020	Dec. 31, 2020	3 Month	1 Year Return
CAD/USD	$.7698	$0.7508	.7857	+4.65%	+2.06%
Oil WTI (US $)	$61.21	$39.89	$48.52	+21.63%	-20.73%
Gold (US $)	$1,518.20	$1,892.60	$1,898.00	+0.29%	+25.02%
Silver (US $)	$17.87	$23.39	$26.36	+12.70%	+47.51%
S&P/TSX	17,063	16,121	17,433	+8.14%	+2.17%
S&P 500	3,231	3,363	3,756	+11.69%	+16.25%
Cdn 10 yr.	1.70%	.54%	.67%	+13 bps	-103 bps
US 10 yr.	1.92%	.68%	.91%	+23 bps	-101 bps

Source: Bloomberg

During the fourth quarter, the Canadian dollar increased 4.65% against the $USD and was up 2.06% over the last twelve months. Over time, the best way to mitigate currency risk is to buy strong and growing businesses that generate revenue in numerous currencies. As a result, these businesses create a natural currency hedge in your portfolio and mitigate the impact of fluctuating currencies and inflation. Our view is that all fiat currencies will continue to lose value against tangible or real assets because governments around the world, through their central banks, continue to print record amounts of money to support their weak economies. Increasing the supply of paper money can only depreciate its value over time. In a year of record money printing it should come as no surprise that both gold and silver as valued in US dollars increased by 25.02% and 47.51% respectively. We believe this is a trend that has real legs to it and continue to build long-term positions in the precious metals sector.

During the quarter, oil finally stabilized and moved sharply higher increasing by 21.63%. Year-over-year oil is still down by 20.73% given the devastating drop in the price of oil during the first quarter of the year, when much of the world went into lockdown. Fortunately for our investors, our exposure to the oil and gas sector remains miniscule and our interest in the sector remains muted. Commodities in general are very volatile and lack predictability making them poor long-term investments. We would rather gain exposure to the energy sector through businesses that service the sector or provide long-term infrastructure assets (pipelines, storage, cleaning, recycling) to the broader energy sector.

During the first quarter, interest rates collapsed in the face of the economic turmoil resulting from the policy decisions to shut down the global economy in response to COVID-19. What is particularly interesting is that interest rates continued to fall in the second quarter even as economies began

to reopen. It wasn't until the third and fourth quarters that rates began edging higher. In Canada and the US interest rates during the fourth quarter on 10-year government bonds increased by 13 and 23 basis points respectively although they were both down by over a full percent during 2020. The overall trend reinforces what we have been telling our investors for ten years: **we do not expect interest rates to increase significantly for a long time! How could they? With global debt at levels never before seen in world history the global economy could not absorb an increase of 200-300 bps without sinking into a serious and prolonged depression!**

C. ROCKLINC Investment Update

1. Private Client Assets

In terms of our ROCKLINC portfolios, with 69% equities and 31% short-term bonds mix, they increased by 1.1% during the fourth quarter and by 14.7% during the last 12 months (period ending December 31, 2020).

More importantly, our average annual compound rate of return over the past 3 and 5 years is clocking in at approximately 11.7% and 10.9%, respectively. Returns are after all fees, and are based on an asset mix of approximately 69% invested in equities, with the remainder invested in short-term deposit accounts, bonds and preferred shares. This asset mix has varied over the past five years but in general we have averaged approximately 67% invested in equities. Please note that the performance we are disclosing is our **aggregate performance** across all our accounts. Each client's portfolio is unique, and performance will vary, based on your risk tolerance and your specific asset allocation.

When we dig further into our numbers, we find that our basket of equities increased by 1.8% during the fourth quarter and by approximately 25.1% during the past 12 months. Our equities have been compounding by approximately 17.5% per year over the past 5 years and outperforming their relevant indexes. Over the past five years, our Canadian equities have been compounding at 17.9% per year (compared to the index at 8.5%), while our US equities have been growing at 16.5% per year (compared to S & P 500 index at 15.2%)! The higher performing US equity markets point to the reality that there are greater investment opportunities outside Canada although we have been able to invest in a handful of excellent Canadian companies. We continue to allocate capital into global businesses and glean the benefit of global growth and diversification in our portfolios.

Although the markets were very volatile during 2020, our focus has not changed. We continue to fix our attention on the economic fundamentals! This means that we **first,** selectively add companies as our research team ferrets out new opportunities. **Second**, prune underperforming businesses. **Third**, take advantage of market swings and add to our outstanding companies at better prices! Whether the markets are woozy or exuberant, there are always opportunities we can seize upon.

2. Rocklinc Partners Fund

A little over three years ago, in September 2017, we launched our Rocklinc Partners Fund. Our goal was to offer our clients a low cost and efficient way to purchase our top 20-25 companies in one bundle. It is an effective way to gain access to a diversified portfolio with more modest amounts of investment capital.

Our plan was to quietly develop a three-year track record that could be marketed not only to our own private clients but also to the Canadian broker dealer network. By having an investment product that can be marketed to other firms and financial advisors Rocklinc Investment Partners will have a new avenue of growth for the firm. This will provide us with increased revenues that we can use to invest back in the firm as we continue to add professionals to our roster in order to serve all our clients and offer a high-quality investment experience.

Quarterly we will provide our clients updated performance numbers on our Rocklinc Partners Fund. All performance numbers are after all fees and rates of return beyond one year are annual compound rates of return.

As at December 31, 2020 (NBN 1211)

	1 mo.	3 mos.	6 mos.	YTD	1 yr.	2 yr.	Inception
RL Partners	1.73%	-1.56%	4.43%	17.46%	17.46%	21.81%	11.34%

D. Company Update – Church & Dwight Co. Inc.

Often considered a safe haven, consumer staple businesses offer investors down-side protection during economic recessions given the stable consumer demand for basic staples such as household, hygiene and food and beverage products. In North America, the consumer staple industry is concentrated in the hands of a few large companies that compete in a dynamic retail environment with vastly changing consumer preferences. In the last decade, consumers have been more open to try new emerging brands, while also becoming more health conscious in the products they purchase. Although large consumer staple companies can reward investors with a stable dividend and lower stock volatility, they face tremendous growth challenges and most are suffering with stagnant to declining sales. Changing trends in consumer preferences are presenting serious challenges for the large and bureaucratic consumer staple companies given their long innovation and re-formulation cycles.

One company that we believe benefits from a recession-resistant portfolio of products, while offering favourable growth opportunities is Church and Dwight. With a rich history of over 150-years, Church and Dwight has become a leader across many of its product categories. Initially selling Arm and Hammer baking soda, Church and Dwight has proven it can turn a simple baking soda business into a billion dollar-plus business through developing strong brand recognition and investing in product innovation. Overtime, the company has ingeniously infused the Arm and Hammer baking soda brand across many applications, such as laundry detergent, cat litter, tooth paste and deodorant. Over the past twenty years, Church and Dwight has transformed its product portfolio by acquiring a diversified number of leading recession-resistant products that are consumed on a regular basis. Approximately two-thirds of its products are classified under the “premium” category, while the remaining are considered “value” brands. The company has over 80 brands, however it generates over 80% of its revenue and profits from 12 “power” brands: Arm and Hammer (baking soda), Batiste (dry shampoo), First Response (pregnancy test), Flawless (beauty), L’il Critters and Vitafusion (gummy vitamins), Nair (hair removal), Orajel (oral pain reliever), Oxiclean (stain remover), Spinbrush (electric tooth brush), Trojan (condom), Waterpik (oral health) and Xtra (laundry detergent). Each of these brands hold the number one or two market position in their

respective category. This is an amazing feat given the level of competition within the consumer staple sector.

Unlike many of its larger competitors, Church and Dwight has a relatively nimble corporate structure that enables the company to make faster decisions and adapt to changing consumer behavior and trends. It has a strong track record of maintaining or expanding its market share by making innovative improvements to existing brands. This has been a key source of growth that has helped differentiate itself from larger competitors and establish enduring product brands that consumers love to use on a regular basis. The company has broadened its growth internationally by offering its products in over 130 countries. This has been another lever of sustainable long-term growth that has helped drive the success of the company. Since its first acquisition, the company has developed a successful track record of acquiring, integrating and expanding acquired brands. Management has developed a set of disciplined acquisition target criteria that focuses on choosing the best product categories with opportunity to grow market share. This includes acquiring companies that are asset-light, market leaders, high growth and compatible with Church and Dwight's manufacturing, logistics and purchasing infrastructure. This strategy has guided management in making acquisitions that are accretive to the company's profit. Church and Dwight has created a capital-light business model that is less capital intensive, which means that it is able to generate higher levels of free cash flow. In fact, in 2019, the company had a free cash flow conversion of 124%, which means the company converted 124% of its net income into free cash flow! It is able to convert over 100% due to its disciplined working capital management. The company uses this free cash flow to re-invest into its business, make strategic acquisitions, grow its dividend and make share repurchases.

Since the beginning of government lockdowns and restrictions in March 2020, Church and Dwight has significantly benefitted from consumers stocking up their pantries. Over the course of last year, consumers increasingly purchased more household cleaning products and health products, which helped drive record organic growth. Consumers also flocked to ecommerce to buy the company's products. From 2015 to 2020, e-commerce sales as a percentage of total company sales increased from 1% to 12%. As we enter into 2021, we expect that Church and Dwight will continue to capitalize on its enduring brands and continuous product innovation for many years to come! We started purchasing shares in Church & Dwight back in January 2010 at approximately $15.00 per share. Today the stock is trading closer to $90.00 per share. Without including dividends that equates to an annual compound rate of return of approximately 18% over the past eleven years. Not bad for a "boring" consumer staples business!

E. COVID-19 A License to Print

The major economies have for the moment weathered the "pandemic" and lockdowns with what appears on the surface to be little long-term economic damage. This is in no small measure thanks to the substantial monetary stimulus from central banks and the unprecedented fiscal support on behalf of governments around the world. Programs like wage subsidies and job retention schemes have prevented unemployment rates from rising to unspeakable levels in most developed countries. In the United States, corporate bankruptcies and delinquency rates on consumer loans were actually lower in the third quarter of 2020 than the same quarter in 2019 given all the printed money that is now sloshing around in the economy. Underneath the veneer, the hospitality, tourism, transport and retail sectors have been hit very hard. Aside from these sectors many small businesses throughout the broader economy have also been pulverized by government lockdown policies that have favoured larger corporations at the expense of small private businesses. It is important that we all realize that there is a mounting cost to all this folly. This cost is being inordinately borne by the poor, small business owners and by certain sectors of the economy that have been arbitrarily

deemed non-essential by our omniscience State. The damage done to many Canadians and their businesses will be felt for many years to come and seen most directly in lower economic growth.

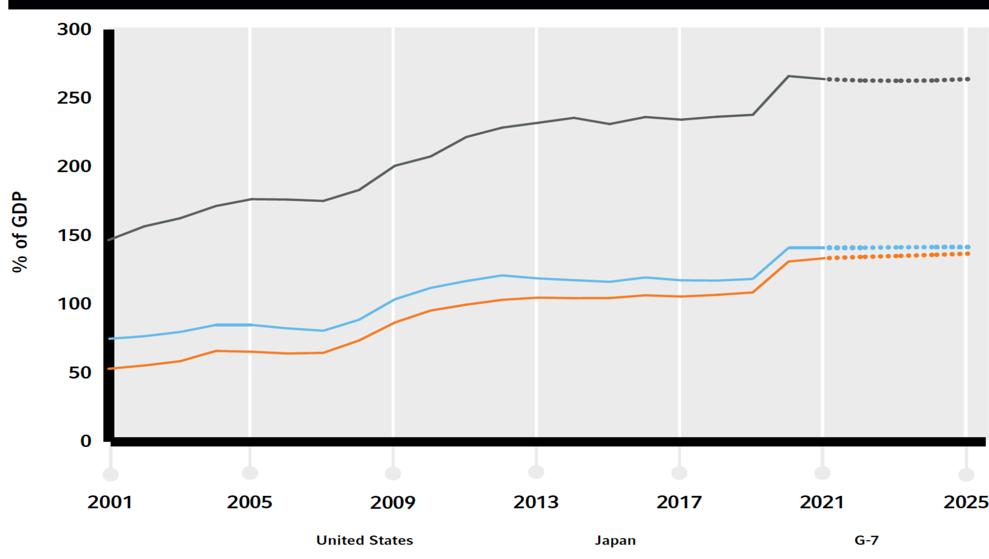
The most notable harm from the pandemic is the rising government debt which has fed the expansion of the State and led to the massive loss of personal liberties and freedoms. The International Monetary Fund (IMF) projects that gross government debt for the G7 economies will rise on average by 23% of gross domestic product (GDP) in 2020! That is an astounding increase in debt never experienced before in a non-wartime period. In Canada, our total debt is expected to increase by 80% of GDP (including household, non-financial corporates and government) the highest level of growth in debt anywhere in the world! See chart below. Note this growth is over a 9 month period.

Normally high debt levels make government finances vulnerable to rising interest rates. This is unlikely to be a significant problem for the foreseeable future as central banks around the world coordinate their efforts to repress interest rates and keep them as close to zero as possible. Some have speculated that governments will soon start to trim deficits through tax hikes and lower spending but this seems highly unlikely given both the voter pressure on governments to spend more along with the misguided promises governments continue to make!

The two charts below show that despite the increase in debt levels, net interest expenses are projected to trend lower for all the major economies. By 2023, Japanese government net interest payments are expected to be close to zero, despite gross debt of approximately 300% of GDP! Let that sink in for a moment. How is that possible? Because two-thirds of Japanese government debt has a negative yield! With negative yields governments could theoretically continue to rack up increasing levels of debt forever! But we know this party will come to an end and when it does it

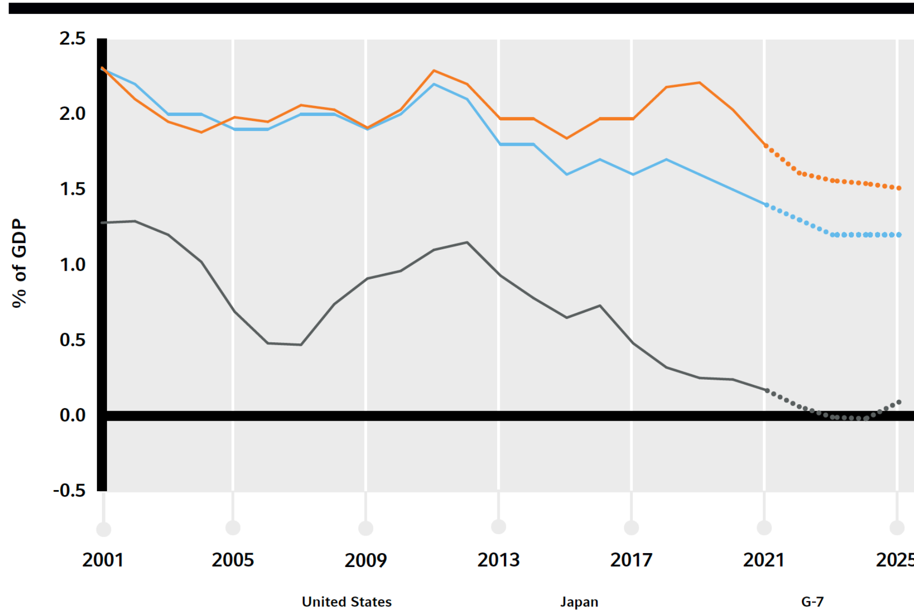
will be very ugly. Governments will come under pressure to reduce deficits only after bond yields rise meaningfully and the markets question debt sustainability. In the interim expect them to keep spending recklessly. Fiscal austerity and tighter monetary policies will never occur until they are literally forced on governments when the financial system crashes or is "reset". We must invest with the full understanding that the current monetary arrangements are not sustainable and we must protect our purchasing power against the decreasing value of fiat currencies.

General Government Gross Debt



Source: International Monetary Fund (IMF) Fiscal Monitor, as of November 27, 2020
Dashes after solid lines represent IMF forecasts for 2021-25. Gross government debt denotes all accrued external financial obligations.

Interest Expense (Net)



Source: International Monetary Fund (IMF) Fiscal Monitor, as of November 27, 2020.
Dashes after solid lines represent IMF forecasts for 2021-25. The Group of Seven (G7) is an intergovernmental organization consisting of Canada, France, Germany, Italy, Japan, the United Kingdom and the United States.

F. Moving Forward in a Sea of Printed Money!

We continue to keep our eyes fixated on the fundamentals of the businesses we invest in, within the context of a global economy swimming in debt. **We will do our best to take advantage of sharp moves in the market!** As investors, volatility and turbulence are our friends and we will use them to your advantage. It is important that we remain vigilant given the economic and social challenges facing the global economy. Anyone who believes that the market cannot drop sharply in 2021 is mistaken.

As a result, the investment team at Rocklinc is working hard to make sure our existing companies are performing as expected or better and searching for new companies that we can add to your portfolios. Over the past year we have added several new companies to our mix. During the same period, we eliminated several positions. Our most significant asset allocation change over the past 12 months is our increased weighting in the precious metals sector primarily through the streaming and royalty companies but also through several high-quality mining companies. Given the global monetary recklessness we are engulfed in, we view this allocation as a strategic hedge to protect the overall value of your portfolios as discussed in many of our previous updates.

Our basic strategy has not changed and positions strongly to deal with the extraordinary times we are living in. Here is a summary our thoughts as we invest in world awash in debt and money printing.

1. Patience – we need to wait for well-priced opportunities. Today we are in uncharted waters. We have never shut down/locked down large swaths of our economy before and simply filled the loss in economic production with massive amounts of debt and money printing! We do not know when this “lock down insanity” will end so we will be careful not to rush into the market without compelling opportunities. While we are hopeful that vaccines will assist in the process of building herd immunity and the opening up of the global economy we are not betting your accounts on it!

2. Watch the world’s leading Central Banks. The level of money printing is already historic and it is just beginning. **Our collective profligacy is truly historic and without precedent. Using COVID-19 as justification to destroy our country’s balance sheet and print money at nauseating levels is immoral.** This will not end well.

3. Pay attention to the irresponsible decisions of governments around the world. Governments are running massive deficits. These deficits are larger as a % of GDP than during World War 2. Sadly, there does not seem to be any end in sight for this madness. There are even calls for governments around the world to spend more including introducing a universal income benefit.

4. Diversify across asset classes, sectors and geographic regions. At the current time we are focusing on nine sectors. These are agriculture, consumer staples, financial, healthcare, infrastructure, manufacturing, precious metals, technology and water. Our largest weightings are in precious metals, infrastructure and technology. By investing in global businesses we also gain exposure to many different currencies providing a hedge to the Canadian dollar.

5. Invest in businesses with strong balance sheets, backed by hard and tangible assets with limited counterparty risk.

6. Invest in firms that produce essential products and services, in growing industries, with well-established long-term secular growth trends. Our highlighted company this quarter Church & Dwight is an excellent example.

7. Avoid/minimize highly leveraged financialized firms that have incomprehensible balance sheets, loaded with risky derivatives. We continue to minimize our exposure to banks and avoid life insurance companies altogether!

8. Maintain liquidity in our portfolios, in order to take advantage of significant moves in the stock market. **Cash is not trash** when the markets become irrational! We expect our cash allocation to be put to work during the next six months!

9. Remain optimistic and opportunistic seasoned with a dose of reality!

If you have any questions pertaining to your account please call or email for an appointment.

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