Mortgage Madness

A. Woke Mortgages[1]

In 2020, the Smithsonian Institute, proponents of Critical Race Theory (CRT), created a chart that was meant to condemn what it called "white dominated culture", or "whiteness", and listed a number of characteristics it claimed were essential to the "white culture" in the United States. Among the characteristics were delayed gratification, saving, planning for the future, hard work, rugged individualism, use of the scientific method and strong nuclear families headed by a biological male. What is shocking about this list is that only a few years ago, these same characteristics were viewed as virtues to be admired and taught to the next generation. Tragically, in our woke culture, these virtues, which have nothing to do with "whiteness" and skin colour, are now viewed as defects to be repressed and punished by the State. What really upsets the woke crowd more than anything is that these characteristics which they despise reflect the historic values of Western Civilization, derived from Biblical Christianity.

Interestingly, the Smithsonian Institute withdrew their chart after widespread protest, but never disavowed the subject matter. Today, the contents of the chart have been adopted by our educational institutions and are being systematically instilled into all areas of our culture. Given the pervasiveness of these ideas, they are now impacting our economic policies and increasingly, the allocation of investment capital within the economy. The most significant example of this is seen in the current push for companies to fall in line with the latest ESG[2] policies which we discussed in our last newsletter. More recently, the Biden administration is ramming these woke ideas into how U.S. mortgages are priced. Although the financial costs are relatively small, what we should be most concerned with is the logic of the argument being used to justify what is clearly unjust and immoral.

In an effort to show its commitment to equity (which translates into equal outcomes, not equality of opportunity), the Federal Housing Finance Agency (FHFA) recently implemented a new pricing policy on May 1, 2023, that **punishes** homebuyers with high credit scores and large down payments by making them pay higher interest rates and extra fees on their mortgages. In a recent Wall Street Journal editorial, it was recorded:

> "According to calculations by Evercore ISI, buyers with strong credit scores between 720 and 739 who make 15%–20% down payments will see their rates increase by 0.750%. Borrowers who put down 20%–25% will see rates increase by 0.500%. The winners are borrowers with weak credit scores—that is, riskier borrowers. Under current FHFA policy, a borrower with a weak credit score below 620, who is borrowing more than 95% of the value of their home, pays 3.75%. Under Ms. Thompson's new plan, those borrowers will see their fees decrease by 1.75%."[3]

Are you kidding me? The short answer is no! Driven by woke ideology, the U.S. government is proposing a damaging change to its mortgage rules. This change will punish borrowers who have worked hard, saved money for a substantial downpayment and made sure they paid all their bills on

[1] Anderson, William L, "Biden's New Intersectionality: Where Equity Policies Meet Bad Economics", Mises Institute, May 1, 2023.
[2] ESG – stands for Environmental, Social & Goverance. (See our First Quarter 2023 Newsletter entitled, "Profiting from the ESG Religion" for more information.)
[3] The Editorial Board (2023, April 28). Spinning Federal Mortgage Fees. *The Wall Street Journal*.

time, in order to subsidize those who have not saved for a large downpayment and have a bad credit history.

Not surprisingly, author and commentator James Bovard has attacked this policy as one that imposes perverse incentives, turning the rewards for creditworthiness upside down. Bovard writes: "Starting May 1, The Post exposed last week, a Biden administration decree will require adjusting mortgage calculations to penalize homebuyers with a FICO credit score of 680 and above—almost two-thirds of the population."[4]

This levy on those with a high credit score will be used to reduce costs for people with low credit scores—i.e., risky borrowers more likely to default on mortgages. However, this is not merely another version of the Law of Unintended Consequences, in which well-meaning government officials implement a policy without looking at the so-called bigger picture. The consequences here are deliberate. The Biden administration officials know the implications of this new policy and are sending a clear message that the idea of creditworthiness itself, according to their woke minds, is implicitly racist since racial gaps in homeownership exists. According to the White House, only 25% of loans held by the FHFA are with people of colour. Black and Hispanic people, on average, have fewer savings to use as a down payment on a home and tend to have lower credit scores, according to David Stevens, former CEO of the Mortgage Bankers Association (MBA) and a former FHA commissioner during the Obama administration.

In order for the FHFA to close the racial gap in home ownership and bring down the cost of borrowing, the agency will compensate for the reduction in borrowing fees by raising the cost of borrowing for those with higher credit scores. Why? Because they tend to be white and credit scores are no longer a just or fair method to evaluate a borrower's risk. According to the leftists, using a scientific approach and mathematical algorithms to determine creditworthiness is racist and reflects "whiteness", so it should all be thrown out the door. Note the average credit score in white communities was 727 in 2021, compared with 667 in Hispanic communities and 627 in Black communities, according to data analyzed by FinMasters, a personal finance blog.

It is no surprise that the Biden administration blames the homeownership gap on racism and as a result, there is nothing wrong if you punish the people who saved their income and engaged in a disciplined lifestyle, something the Smithsonian condemned as a product of "whiteness." However, as Bovard points out, black homeownership rates relative to white homeownership rates are lower today than they were more than fifty years ago: "Federal Housing Finance Agency Director Sandra Thompson testified to Congress last year that the racial homeownership gap 'is higher today than when the Fair Housing Act [of 1968] was passed.'"[5]

> "That is hardly insignificant. In 1968, the United States was just beginning to shed Jim Crow laws, and prospective black homeowners had far fewer financing opportunities than they do today. Furthermore, homebuyers were expected to put at least 20 percent down, with only some exceptions, so one might consider lending policies at that time to have been far less friendly to black borrowers than they are today. Furthermore, the Bill Clinton, George W. Bush, and Barack Obama administrations had policies explicitly aimed at increasing homeownership among blacks and other minority groups. Bush claimed his administration

[4] James Bovard. (2023, April 24). Biden's Mortgage 'Equity' Will Screw Up the Homebuying Market. *The New York Post*.
[5] Ibid.

> had put a record number of black Americans in their own homes by helping to provide down payments and lowering interest rates, among other policies."[6]

Andrew Cuomo, the Clinton administration's Housing and Urban Development Secretary, argued that the homeowning gap between blacks and whites was due to discrimination and told mortgage lenders to make it easier for black households to get access to credit. Cuomo wrote:

> "The American Dream of homeownership is not reserved for whites. We will not tolerate a continued homeownership gap as wide as the Grand Canyon that divides Americans into two societies, separate and unequal. Eliminating housing and lending discrimination is vital to making the opportunity for homeownership a reality for all Americans."[7]

In case you forgot, it was the Bush administration's push to increase black and Hispanic homeownership rates that ended with the 2008-2009 financial crisis. All the efforts on the part of the Bush administration (and the Clinton administration before that) to increase minority home ownership exploded when home prices plunged and millions of homeowners defaulted on their mortgages and lost their homes. The economic result for minorities was disastrous. As a result of the housing crash, the median net worth for Hispanic households declined by 66 percent between 2005 and 2009 and the median net worth of black households declined by 53 percent. So-called 'compassionate lending', that is, bypassing competitive markets and allowing individuals to borrow large amounts of money they cannot afford funded by government aid, seldom ends well and almost always results in financial harm. The last 60 years of government intrusion in the mortgage market is the best evidence of this sad reality. Not holding everyone to the same standards, and subsidizing profligate behaviour has only led to greater financial hardship and poverty for blacks and everyone else who depends on the State for help regardless of the level of melanin in your skin. The focus should be on developing the necessary character traits of success, which include delayed gratification, hardwork and a strong family unit—the exact opposite of what our so-called cultural elites are pushing and what they call "whiteness" and remnants of our "Christian past".

Today, the Biden administration has expanded the use of CRT and "intersectionality" to include the ridiculous claim that whites (along with non-whites who have high credit scores) are to blame for minorities' low credit scores and weak finances. Economically, none of this makes sense, but one must understand that the Biden administration is not looking to promote efficient markets in housing. Instead, they are claiming that the only cause of the gap in homeownership between blacks and whites is white racism and that the government must engage in extraordinary means to eliminate this gap, even if this requires racism and turning economic logic upside down.

Unfortunately, this woke policy will only lead to greater gaps in homeownership, more poverty and increased Statism. Why? Because the problem is moral, not structural. Subjugating the free market to Marxist ideology does nothing to deal with the underlying problems; in fact, it only makes it worse—much worse. Homeownership gaps have nothing to do with skin colour and everything to do with human behaviour and morality. Woke and Marxist mortgage policies will end in failure just like all the other housing initiatives aimed at "helping" minorities. In the end, these policies are not rooted in reality and undermine personal accountability and responsibility. They are an attack on the created order and another way to transfer more power to the State.

[6] Anderson, William L. (2023, May 1). Biden's New Intersectionality: Where Equity Policies Meet Bad Economics. *Mises Institute*.
[7] https://archives.hud.gov/news/1998/pr98-385.html

B. North American Equity Market Statistics

During the second quarter, the Canadian equity market as measured by the S&P/TSX increased by .89%. Year-over-year, the index increased by 9.52%, including dividends. The recent performance of the index has been fairly broad with the information technology and consumer discretionary stocks performing strongly. The large increase in interest rates over the past 15 months has dampened the outlook for commodity businesses (materials and energy) as Central Banks around the world try to slow economic growth in order to bring inflation back to what they deem as "acceptable levels". The large rise in rates has weighed heavily on capital intensive businesses that utilize significant levels of debt on their balance sheets such as real estate and utilities/infrastructure companies. This means some of the businesses we own in our portfolios including energy, infrastructure and precious metals have struggled in 2023 to make significant gains. This does not deter us in owning these companies because these same companies continue to grow steadily and are trading at very attractive prices.

At Rocklinc, our focus is on building portfolios of great businesses that can successfully navigate the challenges facing the global economy. We do not market time or attempt to profit from short-term moves in any particular securities or sectors. As the old investment adage goes, it's time in the market, not market timing. Perhaps more accurately we would say, it's time in the market, *in the right businesses*, not market timing! Our mandate is to find the right businesses and be patient.

Canadian Equities

Year-to-date (YTD), our basket of Canadian companies (after all expenses) increased by 3.82% and over the past 5 and 10 years, compounded annually at 9.81% and 9.60%, respectively. While underperforming the index by 1.45% during the first six months of 2023, we have outperformed the index by approximately by 3.01% and 1.98% annually over the past 5 and 10 years, respectively. Our weighting in the precious metals royalty companies, along with our large weighting in infrastructure businesses, added significant value over the last five and ten years despite holding us back so far in 2023. We expect this trend to quickly reverse when interest rate increases peak in the next 3 months. Regardless of the short-term noise, our focus is on the long-term economic fundamentals of the companies we own and we are pleased with our core positions and their favourable long-term fundamentals.

In terms of the S&P/TSX, four of the ten sectors generated positive returns during the second quarter. Their returns from best to worst: Information Technology (+16.5%), Consumer Discretionary (+5.8%), Industrials (+1.8%), Financials (+.9%), Health Care (-.1%), Energy (-1.3%), Telecommunications (-2.4%), Utilities (-2.5%), Consumer Staples (-2.9%) and Materials (-7.4%).

US Equities

YTD, our portfolio of U.S. based companies (after all expenses) increased by 11.51% and over the past 5 and 10 years, compounded annually at 11.0% and 14.17%, respectively. YTD, we have underperformed the index by approximately 5.38%. Over the past 5 years we have trailed the index by 1.30% and over the past 10 years outperformed the index by 1.31% annually. Most recently, the returns in the U.S. markets have been dominated by a handful of businesses which are trading at extremely high valuations. Many of these businesses are being propelled by the latest investment fad, artificial intelligence. Fad or not, we will never chase overvalued securities. It is our long-term discipline that will produce the consistent returns demanded by our investors. Proverbs 21:5 is a great verse to remember when you feel like chasing the latest investment fad, "The plans of the diligent [patient] lead surely to abundance, but everyone who is hasty comes only to poverty."

Major contributors to our long-term performance include businesses operating in the following four sectors; consumer staples, industrial, manufacturing and technology. Given the size of the U.S. market, most of the new holdings we have added to our portfolios over the past 2-3 years have been global businesses domiciled in the U.S. We expect this trend to continue.

Market Statistics

Pertinent market action during the second quarter of 2023 and during the last 12 months is captured in the following table.

	June 30, 2022	March 31, 2023	June 30, 2023	3 Month Return	1 Year Return
CAD/USD	$.7768	$0.7399	$.7548	+2.01%	-2.83%
Oil WTI (US $)	$105.93	$75.57	$70.48	-6.74%	-33.47%
Gold (US $)	$ 1,806.60	$1,969.80	$1,918.83	-2.59%	+6.21%
Silver (US $)	$20.26	$24.04	$22.76	-5.32%	+12.34%
S&P/TSX (TR)	18,845	20,099	20,155	+.28%	+6.95%
S&P 500 (TR)	3,785	4,109	4,450	+8.30%	+17.57%
Cdn 10 yr.	3.22%	2.91%	3.27%	+36 bps	+5 bps
US 10 yr.	3.02%	3.47%	3.84%	+37 bps	+82 bps

Source: Bloomberg

During the second quarter, the Canadian dollar increased by 2.01% against the USD and was down 2.83% over the last twelve months. As we pointed out in our first quarter update, the USD has advanced against every major currency in the world over the past three years. While trying to predict the short-term movement in currencies is a losing proposition, we do believe the US dollar will have greater headwinds moving forward and has started to weaken this year. As more and more countries around the world seek to de-dollarize, that is, avoid the U.S. dollar when trading goods in the international markets, the U.S. dollar will come under more pressure and weaken relative to other major currencies. This does not mean that the U.S. dollar will lose its reserve currency status, only that it will continue to be weakened. More importantly, the U.S. dollar along with the Canadian dollar and most other fiat currencies will weaken relative to hard assets such as copper, nickel, oil, gas, gold and silver. Consider the five following global de-dollarization developments that have taken place in the last 12 months.

1. The BRICS[8] nations account for over 40 percent of the total global population and close to one-fourth of global GDP. The fact that they are working to develop a "new currency" backed by gold to avoid the U.S. dollar will have an impact on the value of the dollar.
2. Two of the BRICS nations, China and Brazil, have just "reached a deal to trade in their own currencies".

[8] BRICS – stands for Brazil, Russia, India, China and South Africa.

3. In a move that has enormous implications for the "petrodollar", Saudi Arabia agreed to sell their oil in other global currencies, including the Chinese yuan.
4. The Chinese just completed their very first trade of liquefied natural gas that was settled in Chinese currency instead of U.S. dollars.
5. The government of India is offering their currency as an "alternative" to the U.S. dollar in international trade.

Over time, the best way to minimize 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, which we have held for the past 13 years, is that all fiat currencies will continue to lose value against tangible, or real, assets. This is because governments around the world are fiscally irresponsible (run large budget deficits and accumulate large debts), and through their central banks, continue to print record amounts of money to support their indebted economies.

During the quarter, gold slipped by 2.6% and was up 6.2% over the past twelve months. It finished the quarter at $1,918.83, having reached a peak of $2,070.44 on March 8 2022, very close to its all-time intraday high of $2,075 (August 7, 2020). Silver was weaker during the quarter and decreased by 5.32% over the last three months but was up by 12.34% over the past year. We believe the long-term trends for both of these precious metals are to the upside and we continue to build positions in this sector. Our major positions continue to be royalty companies Franco-Nevada, Wheaton Precious Metals, Royal Gold, Sandstorm Gold, Osisko Royalites and leading miner Agnico Eagle Mines.

During the quarter, oil continued to fall and was down by 6.7%. Year-over-year oil was down a whopping 33.5%. The significant jump in the price of oil back in 2022 due to the Russian invasion of Ukraine and government policies that restrict capital investments in the oil and gas sector (driven by the gospel of ESG), will over the long-term keep oil prices at elevated levels. Currently, oil prices have weakened because markets are anticipating a global slowdown/recession and the U.S. continues to release significant amounts of oil from their strategic reserves. The current weakness in the price of oil is an opportunity to add to some of our positions.

Our direct investments in the oil and gas sector remain relatively small but we continue to look at ways to profit from the "green agenda" which is restricting the new supply of oil, keeping oil prices at higher than normal levels and hence increasing the profitability of our favourite companies. During the quarter, we added to some of our direct oil and gas positions. We maintain a large indirect exposure to the sector through a number of infrastructure firms.

During the second quarter, interest rates continued to rise as inflation settled in at stubbornly high levels. The 10-year Canadian bond increased 36 bps and the US 10-year treasury increased by 39 bps during the second quarter. Year over year, the yields were up 5 bps and 82 bps on the 10-year Canadian bond and the 10-year US bond, respectively. At this point, interest rates are expected to edge up from current levels and remain at these levels throughout the remainder of the year. **As we have pointed out to our investors for many years, global debt is far too high and has reached levels never seen before in world history; the global economy cannot sustain and absorb a sharp rise in interest rates without a significant slowdown in economic growth. While we have been surprised by the resiliency of the global economy, largely supported by the fiscal irresponsibility of national governments, the deficits cannot continue at the current levels and indebted consumers will have to slow down their spending. When this happens, we will see a meaningful slowdown in our economy and a retrenchment in the level of interest rates.**

C. ROCKLINC Investment Update

1. Private Client Assets – Separately Managed Accounts

In terms of our ROCKLINC separately managed accounts, they increased by .30% during the second quarter and increased by 5.44% during the last 12 months (period ending June 30, 2023). More importantly, our average annual compound rate of return over the past 3, 5 and 10 years is clocking in at approximately 3.45%, 7.21% and 7.69%, respectively. Returns are after all fees, and are based on an asset mix of approximately 66% invested in equities, with the remainder invested in short-term deposit accounts, bonds and preferred shares. 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 (Canadian and U.S.) were flat during the second quarter and increased by approximately 6.82% during the past 12 months. Our equities have been compounding by approximately 5.04% per year over the past 3 years, by 10.18% over the past 5 years and by 11.18% over the past 10 years.

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 existing positions at better prices!

Whether the markets are weak or exuberant, there are always opportunities to seize upon. Given the downturn in markets last year (2022), a number of buying opportunities emerged. Expect to see new additions, along with some deletions, from your portfolios over the next few months. **Altius Minerals, Trisura Group and Danaher Corporation** are three of the companies we added to our buy list during the first half of 2023.

2. Rocklinc Partners Fund

We launched our Rocklinc Partners Fund in September 2017. Our goal was to offer our clients a low cost and efficient way to purchase our top 20-30 companies in one portfolio. It is an effective way to gain access to a global diversified portfolio with modest amounts of investment capital.

Our plan is to develop a long-term track record that can be marketed not only to our own private clients but also directly to other Canadian investors. As Rocklinc continues to grow, our number one objective is to create portfolios of excellent companies that produce strong long-term performance.

Quarterly, we provide a performance update to our clients. All performance numbers are after all fees and rates of return beyond one year are annual compound rates of return. Currently, the Fund is approximately 33.1% in cash and short-term money market instruments and 66.9% equities. We continue to let our cash weightings edge higher while we wait patiently for better entry points. During the quarter we took a postion in Trisura Group Ltd. We have more to say about this company in future updates. We also sold all of our position in Becton, Dickinson and Company and replaced it with Danaher Corporation. We believe Danaher has greater growth potential and also trades at a more attractive price when compared to Becton.

After all expenses and fees, the Rocklinc Partners Fund has been compounding at approximately 7.2% per year since inception. When you look through to the equities in the portfolio, the Canadian stocks have been compounding at 11.5% and the U.S. equities have been compounding at 9.2% over the past five years. During the same five-year period, the S&P TSX index compounded at 6.8% and the S&P 500 compounded at 12.3%.

Our top 12 holdings represent 40% of the total portfolio and 60% of the equity weighting in the portfolio. The top 10 holdings are Apple (5.1%), Amazon (4.1%), Brookfield Infrastructure Partners (4.0%), Roper Technologies (3.4%), Franco-Nevada (3.4%), Brookfield Renewable Partners (3.1%), Autodesk (2.9%), MEG Energy (2.9%), Suncor Energy (2.9%) and American Tower (2.8%).

As at June 30, 2023

	1 mo.	3 mos.	6 mos.	1 yr.	3 yr.	5 yr.
RL Partners**	+.9%	+.8%	+6.2%	7.3%	+1.3%	+7.2%

** Inception September 29, 2017 (NBN1212)

3. Rocklinc Kokomo Fund

In order to assist some of our clients and provide them with an investment product that is regulated and registered outside of Canada, we launched our Rocklinc Kokomo Fund in November 2022. Our Kokomo Fund is registered in the Cayman Islands and all funds are held in custody in Grand Cayman. It is important to point out that the Cayman Islands are a British Overseas Territory and the world's number one offshore market for investment funds.

The Fund Custodian for the Rocklinc Kokomo Fund is FundBank (formerly DMS Bank), the Fund Administrator is SGGG Fund Services (Cayman) Inc., the Fund's legal counsel is Carey Olsen, and Fund's Auditor is Grant Thornton (Cayman). The minimum investment is $100,000 USD. The Net Asset Value (NAV) of the Fund is priced monthly and started at $100.00 per unit. We are managing the portfolio in a similar manner to how we manage all our discretionary accounts. This will include 20-25 stocks, low turnover, a competitive management fee, no performance fees and monthly pricing and liquidity. Offering documents are available on our website or by calling us at Rocklinc.

We started making investments in the portfolio in February and continue to add slowly to our core positions. At the end of the second quarter, the Fund had a total value of $2.52 million USD. The units closed at $103.54 at the end of June giving them a year-to-date return of 3.5%. There has been a consistent flow of assets into the Fund and client interest is strong.

As of July 12th, we have 17 equity positions in the portfolio representing approximately 53% of the total value of the assets. The remaining 47% is invested in a money market fund currently earning approximately 5% per year. Our objective is to slowly increase both the number of equities in the portfolio (up to 20-25 securities) and also take the equity weighting up to 80-90% based on buying opportunities and valuations. We will not chase stocks.

Our top 8 companies in the portfolio are Brookfield Infrastructure, American Tower, Brookfield Renewable, Wheaton Precious Metals, Linde PLC, CoStar Group, Apple Inc and Autodesk.

D. Company Update – CoStar Group

On a warm spring day in May of 1792, underneath an old sycamore tree, a group of twenty-four respected New York merchants came together and placed their signatures on a piece of parchment on what was to become known as the *Buttonwood Agreement*. The significance of this accord is better known not by its name but rather by the location in which it was signed – 68 Wall Street. The agreement laid the foundations for standardized trading in basic commodities, such as wheat and coffee, and it would go on to transform global finance, becoming the home of the New York Stock Exchange and by extension, American capitalism. To this day, the collective finance industry is often referred to as 'Wall Street', an eponymous hat-tip to this locale. The standardization of trading, price transparency, and ease of buying and selling (in trading parlance known as *liquidity*) helped, in part, to catapult the young American nation onto a long road of wealth creation and prosperity, solidifying its superpower status by the end of World War II.

Trailing third behind the global capital markets and residential real estate, global Commercial Real Estate (CRE) represents the world's third largest investable asset class. Despite its size and importance, commercial real estate had been operating in a market of relative obscurity, not unlike wheat and coffee before the signing of the *Buttonwood Agreement*. Commercial real estate data is considerably more difficult to collect, maintain, and update due to the unique nature of its transactions. However, there has been one company at the forefront of bringing this disparate $180 trillion market into the 21st century – **CoStar Group**.

At its core, CoStar Group is an information company. Having started from humble beginnings in an undistinguished basement apartment in Washington D.C., the now $37 billion juggernaut has curated the commercial real estate sector's leading database of proprietary information. Its information and online marketplaces are indispensable to the functioning of this market – a place where industry professionals and other stakeholders continuously interact and facilitate transactions by efficiently accessing and exchanging current, accurate, and standardized real estate-related information. CoStar's proprietary data, analytics, and marketplaces provide insight and services to the entire spectrum of global commercial real estate, from industrial warehouses, hotels and apartment buildings to office towers and beyond. Its granular detail on commercial buildings across this continent and select global markets is unrivalled; the Company has such a large lead over all other data providers that undertaking an effort to develop a comparable database would cost billions of dollars and would be hopelessly time-consuming to pursue. This reality has resulted in no meaningful competition for CoStar's suite of CRE data.

Each real estate transaction has multiple participants and multiple information requirements; in order to facilitate each transaction, each participant must have accurate and current data. Sale prices, tenant information, asset values, lease expirations, vacancy rates, absorption rates, and lien assessments are critical pieces of information provided to consumers of CRE data. Many individuals beyond brokers require detailed CRE information – property owners, managers, developers, bankers, insurers, retailers, hospitality owners, government agencies, appraisers, pension fund managers, reporters, asset managers, and others need comprehensive information on commercial properties. With a commercial lease expiring every 7 minutes in the U.S, the demand for CoStar's offerings is colossal.

For those outside of the CRE industry, it is possibly a company you've never heard of before, but for those in it, CoStar represents an essential provider of databases and marketplaces that the global real estate industry requires to operate efficiently just as the *Buttonwood Agreement* served as the basis of trading in basic commodities in the New York region in the late 1700s. In a survey of commercial real estate professionals conducted in 2019, 98% of respondents indicated that they relied on CoStar for CRE data despite its significantly higher cost. It's this sticky subscriber base and hard-to-duplicate depth, breadth, and scope of data coverage that CoStar's economic moat is built upon, providing near impenetrable barriers to entry. (CoStar's only competitor, Xceligent, went bankrupt in 2017, and to this day, there is no real alternative to CoStar's suite of data and analytics.) Perhaps counterintuitively, times of distress in the commercial real estate sector can reinforce the company's value proposition as market participants require more than ever to have actionable and accurate information crucial in decisions of financing, buying & selling, lease information, and extending insurance, among many other important components to the life cycle of CRE. This value proposition has recently been demonstrated by renewal rates of over 95% in the most recent quarter and the company is expecting double-digit revenue growth in 2023, despite turbulent times in the broader sector.

Leveraging its industry leading database, CoStar has built dominant listing businesses in both the for-lease multifamily and for-sale residential segments of the real estate market. The company's listing platforms generate a high number of leads for listers when compared to its competitors, which gives CoStar strong pricing power, creating a positive feedback loop that enables the company to increase its investment in data, R&D, and advertisement, resulting in increased traffic and thereby reinforcing their competitive position. For example, the company's flagship Apartments.com brand boasts one of America's largest inventories of rental apartment listings in the country, having delivered over 1.2 billion visits to the platform in 2022. With over 20% revenue growth expected in this segment this year, CoStar says it is still in the early innings of growth with an addressable domestic market still largely untapped, continued above-inflation price increases, upsell opportunities, and new international markets to enter. Likewise, CoStar's residential real estate segment is led by its Homes.com brand. Though a newer entrant in the residential multiple-listing service space and facing strong competition from the likes of Redfin and Zillow, CoStar has shown time and time again that it can allocate capital shrewdly, invest judiciously in marketing, and drive superior returns on capital as the businesses begin to dominate their sectors and boast reinforcing network effects. We look forward to seeing repeated success as CoStar continues to invest heavily into the brand.

CoStar is laser-focused on its operational performance. One of the first major publicly-traded companies to require its employees back into the office full-time and also quick to prune underperformers, CoStar is not hesitant to ask of its employees their best effort each and every day. Its driven culture is set at the top, with CEO Andy Florance the captain at the CoStar helm, having founded the company over 30 years ago in his basement. A roommate of Jeff Bezos back at Princeton, Florance has embodied an 'Amazon-like' approach to business building: exceed customers' expectations, plow cash back into the business for reinvestment, and dominate the competition. Winner of numerous awards and accolades including most recently the Globee Visionary and CEO of the Year, there is not a job in CoStar that Andy Florance has not done at one point or another. We like to see competent, honest, and ethical management teams commandeering the businesses we own, and we certainly see these characteristics manifestly displayed throughout the company at CoStar.

Despite the cyclical nature of the real estate industry, CoStar's operational stability is derived from recurring revenue representing 75% of total revenue, with renewal rates typically exceeding 95% (which is particularly impressive given that CoStar does not exclude small-scale companies, such as boutique brokerage firms, that ceased their operations). In the height of the Global Financial Crisis in 2008/09, CoStar saw renewal rates dip to 85%, where they hovered for a few quarters before rising again. This resiliency speaks to the embedded high switching costs for a consumer of CoStar data – data which is often integrated in workflows and business processes, meaning that switching to an inferior product could materially affect the information quality and execution capabilities of a client, resulting in tremendous financial and reputational harm. Compounding at a 20% annual growth rate over the past 10 years, it is no surprise that CoStar has reached a formidable market capitalization and has recently been admitted as the S&P 500's newest member.

Lastly, management has proven itself to be an excellent allocator of capital; having issued no dividends and not an active repurchaser of its stock, CoStar sees the highest return on its capital from reinvesting into its own business. As interest rates continue to bite into real economic activity and interest-sensitive segments such as commercial real estate continue to be under pressure, CoStar is aptly prepared to take advantage of any opportunities that comes its way. Having abstained from large acquisitions in the past number of years given sky-high valuations in the space, CoStar is patient to wait for the 'fat-pitch'—a well-timed, strategic acquisition to complement and bolster its existing businesses. Sitting on a rock-solid balance sheet of $5 billion in cash and no long-term debt, the company is ready for such an opportunity. We look forward to continuing to own CoStar in client portfolios and to monitor developments as CoStar continues in digitizing the $180 trillion asset class that is commercial real estate.

E. Moving Forward

We continue to keep our eyes focused on the fundamentals of the businesses we invest in, within the context of a global economy immersed in debt. **We will do our best to take advantage of sharp moves in the market!** Given the negative markets last year, we are finding more buying opportunities as we slowly deploy new capital. As investors, volatility and turbulence are our friends. We will do our best to use them to your advantage. It is important that we remain vigilant given the economic and social challenges facing the global economy.

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 started to add several new companies to our mix. These include, Altius Minerals (initiated February 2023), Autodesk, Inc., Canadian Natural Resources, Glencore (initiated January 2023), Intercontinental Exchange, Linde PLC, MEG Energy, Osisko Gold Royalties (initiated February 2023), Progressive Corporation (initiated March 2023) and Trisura Group (initiated June 2023).

During the same period, we eliminated/reduced several positions including Algonquin Power and First Majestic Silver Corp. We continue to add to our weightings in a number of sectors with our largest additions in the areas of the market most impacted by the negative returns in 2022 and the rapid rise in interest rates.

Within the current environment our basic strategy is as follows:

1. Patience – we need to wait for well-priced opportunities. Our patience and cash positions give us the flexibility to buy low. Weak markets in 2022 have opened up a number of new

opportunities for our clients. Some of these opportunities have been reduced by the rise in markets so far in 2023, especially some of the technology stocks.

2. Watch the world's leading Central Banks. The level of money printing has been historic and we do not believe it will be easy to turn off the spigot as 2023 unfolds. Increased rates have started to slow down the global economy and we are preparing for a potential recession later this year. As we enter the third quarter, it looks like Central Banks are nearing the end of the interest rate cycle and rates should start to plateau.

3. Pay attention to the irresponsible decisions of governments around the world. Governments continue to run massive deficits. Sadly, there does not seem to be any end in sight for this madness. At the time of writing, the U.S. debt has exceeded $32.4 trillion. It is up more than $1 trillion in the last 60 days, now that the debt ceiling was raised again. When is the last time you heard a government talk seriously about balancing its budget?

4. Diversify across asset classes, sectors and geographic regions. While we are careful to run focused portfolios (20-30 securities), we are also careful to maintain an appropriate level of diversification.

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 **Costar Group** 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 life insurance companies! We have been sounding the alarm on banks for the past decade and the situation only continues to get worse. We are very concerned with the solvency of many banks. Why? If we are in a global debt bubble and the liabilities of consumers, corporations and governments are the assets of the banks, those are not assets we want to own! We prefer to avoid the banks as much as Pfizer's latest mRNA gene therapy!

8. Maintain adequate 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! With the recent rise in rates the cash we hold in clients accounts is earning approximately 5% per year.

9. Remain optimistic and opportunistic, seasoned with a dose of reality. Do not succumb to fear mongering nor believe that you cannot survive without the "help" of an intrusive State that has proven to be completely inept. How can you trust a government that keeps stealing our money through a rapacious tax system and then sending us meaningless cheques that are supposed to take care of us?

10. Place your faith and hope in God and not the failed State. Remember the words of the psalmist King David in Psalm 118:8-9; "It is better to take refuge in the LORD than to trust in man. It is better to take refuge in the LORD than to trust in princes."

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

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