

## A Message from the CEO

May 15, 2019



Peter Grosskopf  
Chief Executive Officer,  
Sprott Inc.

### Why We Need Gold

#### Peter Grosskopf

Chief Executive Officer, Sprott Inc.; Managing Director, Sprott Resource Lending

It has been nearly a decade since I made a career change from investment dealer to asset management. Throughout that time, the asset management industry has continued to change dramatically, bringing many benefits to investors. These include overall fee compression, the ability to own almost every conceivable segment of the market through ETFs, some increased participation in “alternative” investment strategies, much-improved access to information and risk disclosure and the proliferation of fee-based accounts providing tailored investment advice. The markets have delivered strong overall returns globally and those who have not been fully invested have been punished as asset classes of all descriptions rose in tandem, fueled by reasonably strong economies and low-interest rates.

That backdrop underpins the advice of almost all conventional asset managers today — to allocate capital mostly to broad, liquid equity and bond indices, with perhaps some participation in real estate and other dividend-paying asset classes. The global giants in our industry are no longer active investment managers; rather they resemble operators of licensed technology platforms that offer computer-generated models, packaging this robotic advice to their clients in easy-to-swallow bites.

### The Cinderella Story Will End

There are ominous signs that dangers lie ahead for this Cinderella story, which has worked for investors lately but will not last forever. For one thing, all of the strategies described above have become increasingly correlated and have benefited from once-in-a-lifetime interest rate reductions. For another, global debt levels are at record levels and can no longer be serviced by the productive engines of the economy and normal tax levels. Many pensions and entitlement programs are past the point of broken and government deficits are out of control. A spate of recent IPOs based on ludicrous price-to-sales valuation multiples are eerily reminiscent of the dot-com bubble of 2000.

From a top-down perspective, there is no question that the combination of the increasing polarization of classes and politics will drive governments globally to adapt populist-leaning policies, rather than those that require moderation. It is clear to me that these dovish policies will now require financing through the hand-in-hand partners of massive deficits and direct currency printing, as justified by some version of Modern Monetary Theory (i.e., “helicopter money”). While inflation, as calculated by the misleading CPI (consumer price index) measure, is currently seen as low, there is simply no precedent by which to predict what might occur as this macroeconomic thriller plays out. An apt summary is that all of the above can be described as a tightly coiled spring which is becoming more loaded every year.

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We understand that it is hard to resist the siren song of the solid track record that has been created by the investment industry in the past ten years, and the three decades which preceded it as the boomer generation propelled the markets and the economy. There is also ample logic to suggest that when helicopter money drops one must have some allocation to solid growth and value stocks, as well as dividend-paying real assets. These positions should broadly benefit from the growth and inflation that is initially generated as governments print more money.

## Time to Add Portfolio Protection?

A reasonable question to ask is what happens if investors cool to Treasuries, or lose confidence in the purchasing power of their cash, or start to price in the multiple risks that appear to be lurking on the edges of “consensus” expectations? The crowded trade is to do nothing but that is yet another harbinger that the right thing to do is to begin to add some portfolio protection. As we see them, the existing liquid alternatives for insurance would, with U.S. Treasuries losing much of their appeal, be limited to (a) moving to cash; (b) purchasing portfolio protection options or moving to market-neutral funds; or, (c) buying gold or gold equities.

On the personal side, I accepted the position as CEO of Sprott because I felt, after more than 30 years of experience financing the mining industry, there was an opportunity to establish an industry-leading investment firm specializing in precious metals. I believe that investors will require our expertise as protection against a highly probable pullback in the markets. Lately, my patience has been tested by the markets’ resilient faith in government monetary policies and their proxies — the paper currencies.

## Gold is Unmatched as a Diversification Tool

Most investors do not realize that gold is one of the world’s most liquid currencies and assets, trading with volumes equivalent to those of the euro or U.S. Treasury bond benchmarks. Although similar in philosophy, gold blows Bitcoin away on any measure by which the two can be compared. Gold bullion is easy to purchase and the principal risks are timing, fees and expenses. There are significant new developments in vaulting, ETFs and the digitization of gold, which are helping to improve access for all investors.

The digitization of gold is particularly important because it has ushered in the technology and platforms that address the final frontier for gold: allowing gold to be used within the financial system as a viable household-level payment currency which can credibly replace cash. Put yourself in the headspace of a citizen of most countries and you can understand why gold is immediately superior to holding local currency-denominated cash at the bank, which is an almost guaranteed loser of principal value over time. All of this underpins the conclusion that gold is a must-own cash diversification tool that provides a defense against fiat currency devaluation. Gold should be held in the account of every investor at some appropriate percentage. Sprott is exceptionally well qualified and able to assist individual and institutional investors in executing this allocation.

## Investing in Gold Equities

In contrast to gold bullion, investing in gold mining companies has been difficult given that metals producers are notoriously tough to value. The last several years have exposed these pitfalls and punished investors as mining companies over-bought, over-built and over-promised, and the quest to uncover value suffered due to the ebbing tide of investor sentiment and the corresponding flows to the sector. Partially because of the weak performance record and partly due to pervasive indexation, gold equities are currently suffering from a severe lack of buying interest and many notable specialist funds have been closed or downsized.

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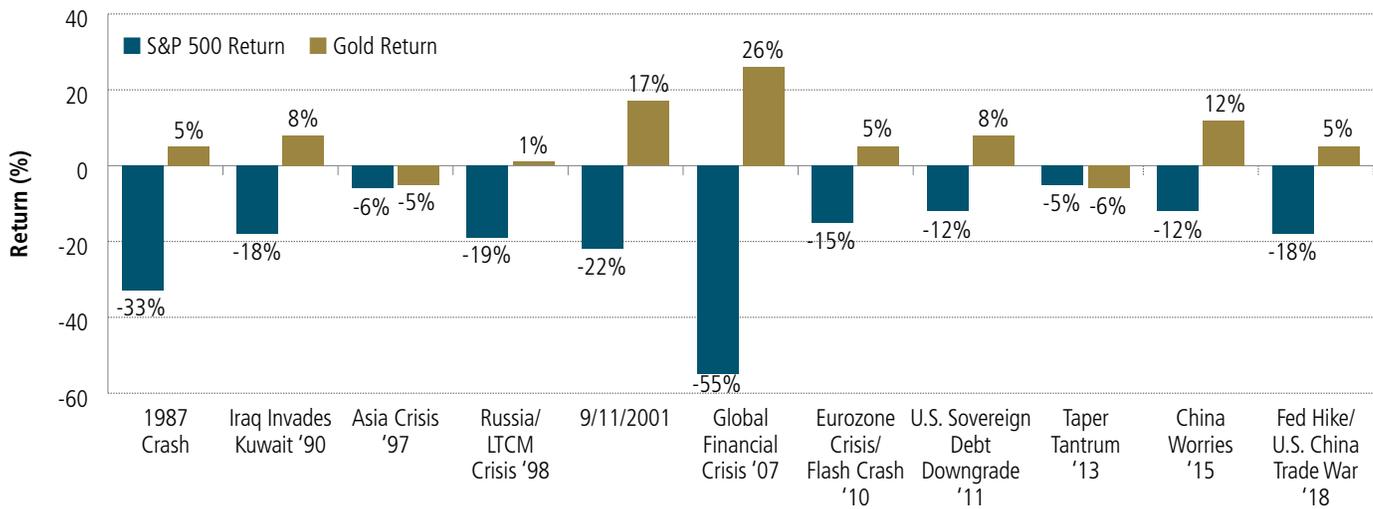
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This leaves Sprott in the position of being stock-picking specialists in an underserved, poorly understood market — in other words, smack in the sweet spot of a contrarian investor. Sprott has developed a solid track record in project lending and our equities team has a sound approach to selecting a focused portfolio of the next tier of successful producers.

Perhaps now is finally the time for investors to benefit from a “life preserver” while others enjoy the card game on the decks of the central bank-piloted Titanic.

Peter Grosskopf, CEO

## Get Ready for the Next Financial Crisis: Gold Provides Proven Portfolio Protection



Source: Tocqueville Asset Management. Dates used: 1987 Crash: 8/25/87-10/19/87; Iraq Invades Kuwait: 7/17/90-10/12/90; Asia Crisis: 10/7/97-10/28/97; Russia/LTCM Crisis: 7/20/98-10/8/98; 9/11: 9/10/01-10/11/02; Global Financial Crisis: 10/11/07-3/6/09; Eurozone Crisis: 4/20/10-7/1/10; U.S. Sovereign Debt Downgrade: 7/25/11-8/9/11; Taper Tantrum: 5/22/13-6/24/13; China Worries: 8/18/15-2/11/16; Fed Rate Hike & China Trade War: 9/20/18-12/24/18.

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**Sprott** is a global alternative asset manager with a defining focus on precious metals and real assets investments. Through our subsidiaries in Canada, the U.S. and Asia, Sprott is dedicated to providing investors with world-class investment strategies that include exchange-listed products, active equity strategies and highly-specialized real asset investments. Our deep sector expertise creates investment and financing solutions unparalleled in the industry.

For more information, please visit [sprott.com](http://sprott.com)

# Sprott

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