SPROTT
ASSET MANAGEMENT

SPROTT ENHANCED EQUITY STRATEGY

April 2016 Commentary

April was a challenging month on a relative basis for our strategy. While we succeeded mitigating further downside during periods where the market declined last month, we also did not participate in the massive upside experienced by materials (up >20% on the TSX) and energy (up 6% and 8.7% on the TSX and SPX, respectively). Uncertainty remains high and investors are chasing market moves, one way or another, for fear of missing out. This is nothing new, as we have been in this rotational market since the oil price collapse in late 2014. As such, our core fundamental stock portfolio, which by design has little exposure to commodity prices (and their derivatives like credit risk/banks, and cyclical industrials), suffers each time money rotates from "safe havens" to "risk-on".

This is partly why we are now using more stock specific hedges to manage our risk; different sectors move up and down with commodity prices sentiment, but the broad based indices (on which our hedges were usually based) do not move much. For example, during the first two months of the year, utilities, staples and telcos performed extremely well (risk-off environment), whereas the last two months have seen energy and materials take the baton, with the other sectors either threading water or actually going down significantly. However, the S&P 500 is only up 1.74% on the year.

Fundamentally, the story remains the same: The U.S. economy continues to muddle through, with economic growth underwhelming but incredibly resilient. While manufacturing and industrial production has remained weak, job and wage growth has been impressive. We think that those looking for a significant acceleration of economic growth are bound to be disappointed, but slow and steady wins the race, and until we see a significant negative shock, talk of recession is simply alarmist.

Similarly, in Canada, fears of a double dip recession were over blown, and the Bank of Canada's strategy of a weaker dollar driving non-resource exports seems to be working. However, in this environment things tend to get ahead of themselves; the rally in the Loonie has been impressive, but is overdone on a fundamental basis. While economic growth in the first quarter of this year was better than expected, the rapid currency appreciation and the consumer hangover from the commodity collapse will likely take more time to flow through the economy. The impact of job losses in Alberta is only starting to show up in credit data, and even with the recent bounce in oil prices, it is unlikely that companies will immediately go back to spending like they used to in the boom years.

Although energy prices are now well off their February lows, it is yet unclear whether or not we are now in a sustained recovery. The massive rally off the bottom has been driven by a combination of oversold market conditions, production outages and then by an epic chase of investors fearful of missing out. Unfortunately this might be "too much of a good thing" as we are already hearing about some shale producers setting up hedges at these levels and ramping up production. Could Libyan and Iranian production surprise to the upside; or could further outages due to geopolitical events drive further price upside? In our view there are too many variables in play on the fundamental side and price movements still appear to be largely an outcome of volatile movements in market positioning.

As discussed in last month's commentary, we have changed our views on the Federal Reserve's monetary policy stance. We now believe that the Fed will be challenged to meaningfully raise rates this year, as their fear of the downside risks to the economy and financial stability significantly outweighs the inflation risks. To us, it feels like Yellen needs a quasi-perfect environment to move the funds rate again, meaning the Fed will stay lower for longer and likely end up behind the curve on inflation. In the meantime, a dovish Fed coupled with increasingly negative rates globally and a perception that central

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banks have "no more bazookas in their bags" has created a very supportive environment for continued positive returns for gold. We have not had any positions related to materials or precious metals in our portfolios for almost four years but started adding gold related equity positions earlier in the first quarter of this year.

We do not see a change in the market narrative of risk-on/risk-off driven by commodities and the resulting wild inter-sector swings. Fundamentals make equity market gains seem less probable over the near to medium term but general lack of participation in the rally since February lows could be reason enough to push to fresh highs as the "pain trade" forces portfolio managers' hands. Accordingly, we will continue to use stock specific option structures such as put spread collars, put selling, etc. to manage volatility. This significantly reduces our volatility, regardless of market conditions. We have also added more names to the portfolio, selectively increasing exposure in core Canadian companies such as Riocan and TransCanada. Consistent with the view expressed above on gold, we have also initiated positions on a few high quality gold miners. Finally, we added a few names in the U.S. exchanges and consumer staples sectors.

Our objective is to continue to find and hold quality companies with strong fundamentals, use option wrappers to improve the risk-reward and somewhat insulate the portfolio from the endemic sector rotation discussed above. Finally, and until stock fundamentals begin to matter more, ETF's are likely to play a bigger role in our portfolio construction. There are many we can use to get theme or sector exposure that offer very deep trading liquidity and often even more liquid option opportunities. We believe that this will help our upside capture in those more cyclical sectors (i.e. materials, energy) where outright stock ownership does not fit with our risk appetite.

Until next month,

The Enhanced Strategy Team:
John, Colin and Etienne

COMPOUNDED RETURNS (%) AS AT APRIL 29, 2016*

	1 MTH	3 MTH	6 MTH	1 YR	3 YR	5 YR	10 YR	ANNUALIZED INCEPTION
SPROTT ENHANCED BALANCED FUND, SERIES A	-0.7	-2.2	-5.9	-5.3	2.3	-	-	3.5
BLENDED INDEX[1]	0.5	2.8	1.8	0.4	9.8	-	-	9.9
SPROTT ENHANCED BALANCED CLASS, SERIES A	-0.6	-2.3	-6.0	-5.5	-	-	-	0.9
BLENDED INDEX[1]	0.5	2.8	1.8	0.4	-	-	-	10.2
SPROTT ENHANCED EQUITY CLASS, SERIES A	-1.4	-4.2	-8.5	-7.9	2.9	-	-	4.4
TSX/S&P 500 BLENDED INDEX[2]	0.3	2.6	0.7	0.0	13.4	-	-	13.1
SPROTT ENHANCED LONG-SHORT EQUITY FUND L.P., CLASS A	-2.2	-7.1	-13.4	-13.3	1.4	-1.7	2.7	9.0
TSX/S&P 500 BLENDED INDEX[2]	0.3	2.6	0.7	0.0	13.4	10.2	6.3	7.1
SPROTT ENHANCED LONG-SHORT EQUITY RSP FUND, CLASS A	-2.2	-7.2	-13.5	-13.5	1.1	-2.0	2.4	4.0
TSX/S&P 500 BLENDED INDEX[2]	0.3	2.6	0.7	0.0	13.4	10.2	6.3	6.9
SPROTT ENHANCED US EQUITY CLASS[3]	-	-	-	-	-	-	-	-

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* All returns and fund details are a) based on Class/Series A shares/units; b) net of fees; c) annualized if period is greater than one year; d) as at April 29, 2016; e) inception date for Sprott Enhanced Equity Class is 04/16/12; f) inception date for Sprott Enhanced Balanced Class is 09/13/13; g) inception date for Sprott Enhanced Balanced Fund is 04/16/12; h) inception date for Sprott Enhanced Long-Short Equity Fund L.P. is 04/07/04; i) inception date for Sprott Enhanced Long-Short Equity RSP Fund is 09/30/05.

[1] 40% S&P/TSX Composite TRI; 30% S&P 500 TRI CAD; 30% FTSE TMX Canada Universe Bond Index™.

[2] 50% of S&P/TSX Composite TRI; 50% of S&P 500 TRI CAD.

[3] In accordance with NI 81-102, we will not publish returns for this Fund until it is one year old.

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