SPROTT
ASSET MANAGEMENT

GLOBAL MARKET UPDATE

July 2017 Commentary

MARKET UPDATE

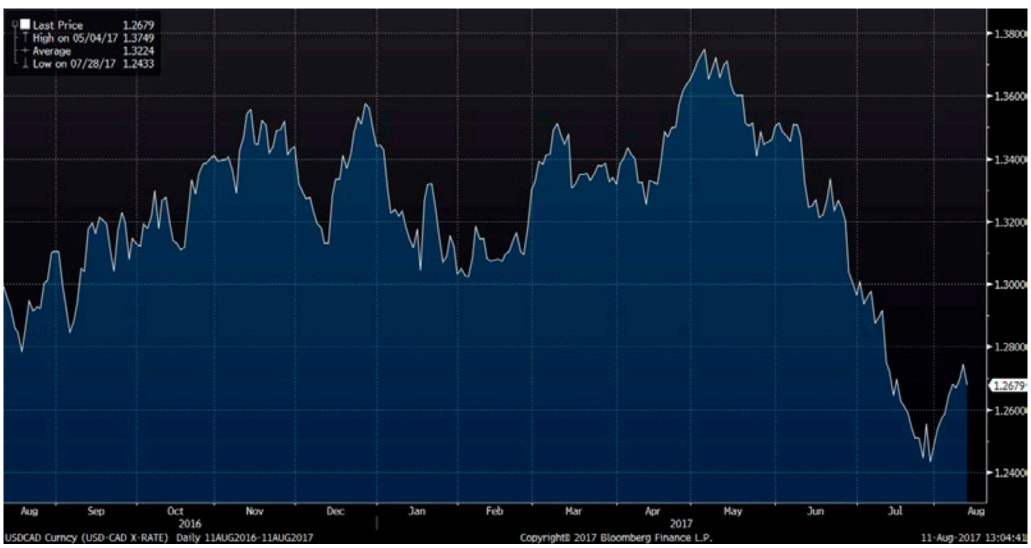
Geopolitical events remain the biggest risk in 2017 and as various concerns were resolved, new ones seemed to materialize.

In June, European markets faced a surprising result in the UK General Election, as Theresa May's Conservative Party lost their working majority and were forced to form a coalition with the Democratic Unionist Party. In July, the US Senate rejected a watered-down proposal to repeal and replace Obamacare, a blow to the Trump administration. Perhaps most concerning, a war of words between President Trump and North Korea escalated to outright threats. The rhetoric was hostile and aggressive but diplomacy looks to have prevailed for now.

Despite these macro risks, earnings growth remains solid. According to Bloomberg data, Q2 2017 earnings growth came in at an average of 12.0% for companies in the MSCI World Index and 10.7% for companies in the S&P 500 Index.

This underlying earnings growth led to decent overall stock market performance year to date, with one major caveat for global investors: US Dollar weakness and Canadian Dollar strength (see Exhibit 1) eroded returns in Canadian Dollar terms.

Exhibit 1: USD/CAD cross rate



Source: Bloomberg.

Specifically, the MSCI World Index gained 13.7% YTD to July 31, 2017 but only 5.2% in Canadian Dollar terms (see Exhibit 2).

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Exhibit 2: MSCI World Index in USD (white line) **and MSCI World Index in CAD** (orange line)

Source: Bloomberg.

Similarly, the S&P 500 Index gained 11.6% YTD to July 31, 2017 but only 3.6% in Canadian Dollar terms (see Exhibit 3).

Exhibit 3: S&P 500 in USD (white line) **and S&P 500 in CAD** (orange line)

Source: Bloomberg.

We would point to a change in the Bank of Canada's messaging beginning in June as the key driver of US Dollar weakness versus Canadian Dollar strength. As a reminder, The Governor of the Bank of Canada, Stephen Poloz, surprised the markets with a sudden pivot in terms of monetary policy, shifting from an easing bias to a tightening bias. He asserted that the Canadian economy is picking up and that "the interest rate cuts we did two years ago have done their job". When the Bank of Canada raised its key interest rate to 0.75%, the first hike in seven years, on July 12, we can't say we weren't forewarned.

PORTFOLIO UPDATE

In response to the Bank of Canada's pivot to a tightening bias in June, we made the decision to hedge our US Dollar exposure across all of the Funds. Although we didn't quite get fully hedged, we were approximately 75% protected against US Dollar weakness over the past couple of months. With the US Dollar now looking to have stabilized and expectations for future rate hikes in Canada perhaps getting too far ahead of the curve, we returned to a neutral position relative to our benchmarks. We plan to continue to tactically hedge our currency exposure as market conditions warrant.

We also raised our cash positions slightly, while waiting for the geopolitical risks to offer more attractive entry points in individual securities. With the MSCI World Index trading at a 2017E P/E multiple of 17.4x compared to the S&P 500 Index at a 2017E P/E multiple of 18.9x, better valuations can be found outside of the United States. Given superior earnings growth coupled with the potential for multiple expansion, we believe that Europe still offers some attractive investment opportunities.

Since the beginning of the year, the Sprott Focused Global Dividend Class initiated new positions in: Credit Agricole, Cellnex Telecom, Interxion, East Japan Railway, Western Digital, Affiliated Managers Group, Xylem and Ferrovial. We exited positions in American Tower, Ameriprise Financial, Bank of America, Carrefour, Cisco, Crown Castle, Discover Financial, Drillisch, Groupe Eurotunnel, Medtronic, Roche, Safran, Starbucks, Sunrise Communications, US Bancorp and Vinci.

Top contributors to the fund YTD include Drillisch (up 48.9%), Cineworld (up 23.6%) and Visa (up 18.8%), while top detractors include Macquarie Infrastructure (down 10.4%), Nextdc (down 10.9%) and Discover Financial (down 8.2%).

Drillisch, the German wireless wholesaler, was the subject of a takeover offer by United Internet and we liquidated our position into the bid. Cineworld benefited from strong UK and Eastern European cinema attendance due to a solid film slate, which should continue through 2018. Visa gained on good consumer spending growth and the continuing successful integration of Visa Europe. We exited our position in Discover Financial as loan growth was offset by rising loan loss provisions due to weaker credit quality.

Since the beginning of the year, the Sprott Focused US Dividend Class initiated new positions in: Affiliated Managers Group, Western Digital and Xylem. We exited positions in Bank of America, Cisco, Crown Castle, Discover Financial, Nike, Starbucks and US Bancorp.

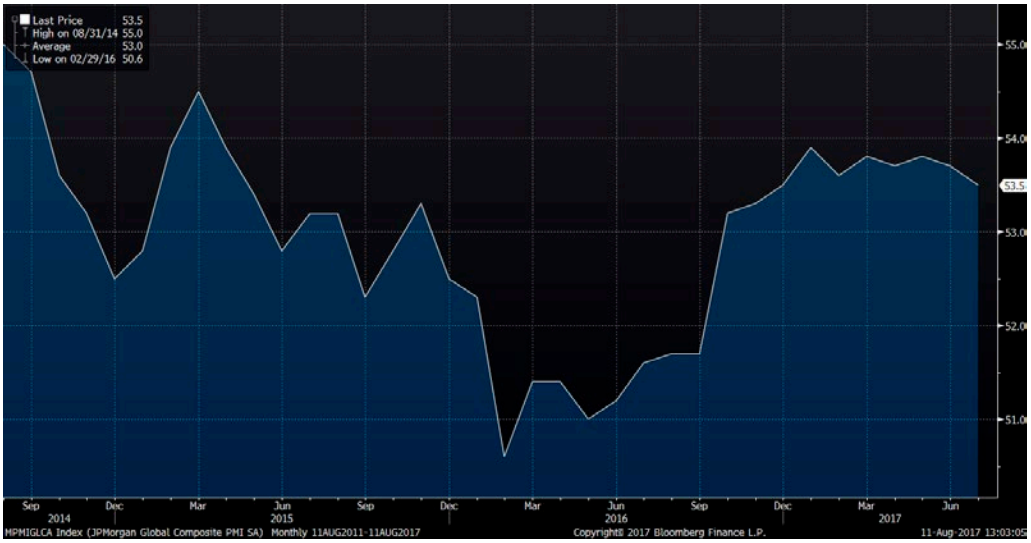
Top contributors to the fund YTD include Visa (up 18.7%), Alphabet (up 11.8%) and Allergan (up 12.2%), while top detractors include Macquarie Infrastructure (down 10.6%), Discover Financial (down 7.9%) and Western Digital (down 4.4%).

Alphabet continues to generate approximately 20% adjusted revenue growth as paid click growth outpaces cost per click declines and traffic accelerates at Google-owned sites. Allergan rallied nicely, as proceeds from the sale of its generic business allowed the acquisitions of several higher-growth companies, including LifeCell (regenerative medicine) and Zeltiq (technology related to plastic surgery).

PORTFOLIO OUTLOOK

The OECD is calling for Global real GDP growth of 3.5% and 3.6% in 2017 and 2018 respectively , with the US growing at 2.1% and 2.4% respectively, the Eurozone growing at 1.8% and 1.8% respectively and Canada growing at 2.8% and 2.3% respectively. The JPMorgan Global Composite PMI Index is still well above the 50 level, indicating continued expansion (see Exhibit 4). These metrics should be supportive of current equity market valuations, excluding brief periods of macro-driven volatility.

Exhibit 4: JPMorgan Global Composite PMI Index, seasonally adjusted



Source: Bloomberg.

We believe that it is possible that we only see one more rate hike out of the US Federal Reserve and only one more rate hike out of the Bank of Canada this year. Long-term rates will likely remain lower for longer, which is positive for equities and income-oriented investments. As we have noted in the past, the US yield curve flattened dramatically through the year and inflation data remains subdued (with July US consumer prices increasing only 1.7% from a year ago), which are both consistent with this outlook.

Jeff Sayer
Portfolio Manager

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Sprott Asset Management LP: Toll Free: 1.866.299.9906. DEALER SERVICES: RBC Investor & Treasury Services: Tel: 416.955.5885; Toll Free: 1.877.874.0899.

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