Ninepoint Silver Equities Class

Q4 2020 Commentary

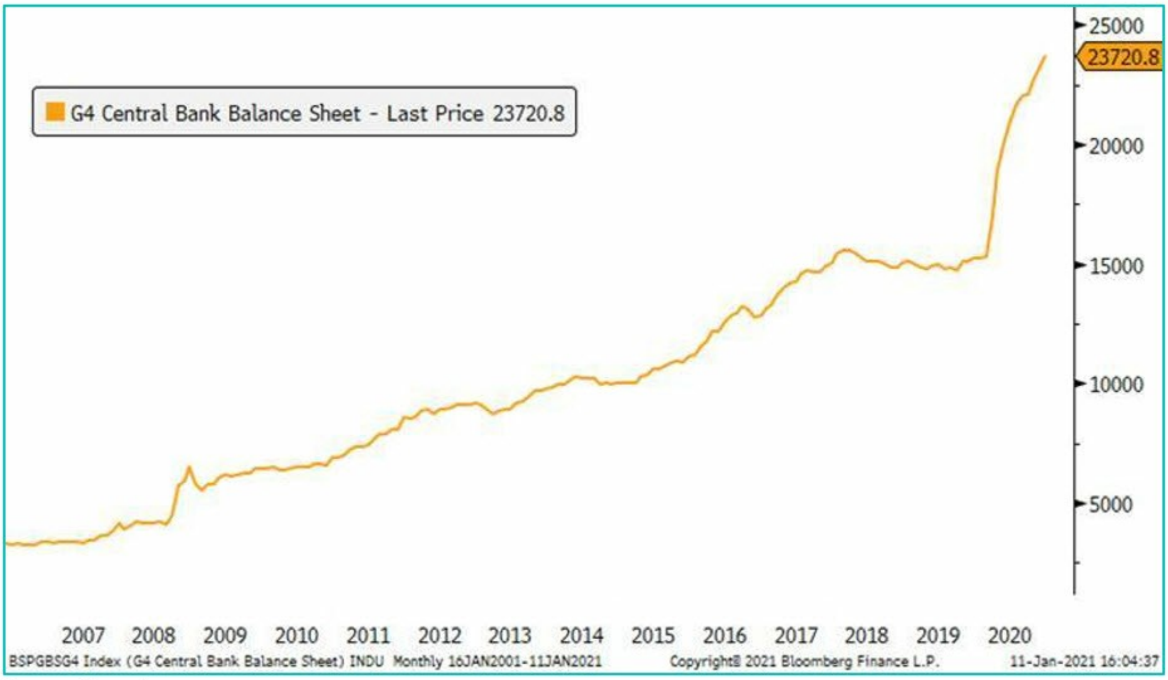
Investment Team

Ninepoint / Sprott,
Sub Advised by Sprott Asset Management (SAM)

The year 2020 was a strong year for precious metal investors despite periods of extreme volatility and continued uncertainty. We are pleased to report that the Ninepoint Silver Equities Class, Series F gained 71.9% over the course of the year. In doing so, the strategy comfortably outperformed the benchmark and was among the best performing actively managed strategies in the precious metals space. We continue to see early signs of increasing investor interest towards precious metal miners who have enormously benefited from the positive price momentum behind gold and silver. We continue to foresee strongest valuations among mid-tier precious metal miners.

Investors face a perilous path heading into 2021. With both the S&P 500 and NASDAQ trading near their all-time highs, the broader market has already priced in a V-shaped recovery. Uncertainty faced by investors on the other hand, continues to rise every day. The approval of vaccines has been timely, but the recent discovery of multiple COVID strains, which are more contagious, has magnified the need for rapid deployment of these vaccines. The issue is that vaccinations have been progressing at a slower pace than anticipated.

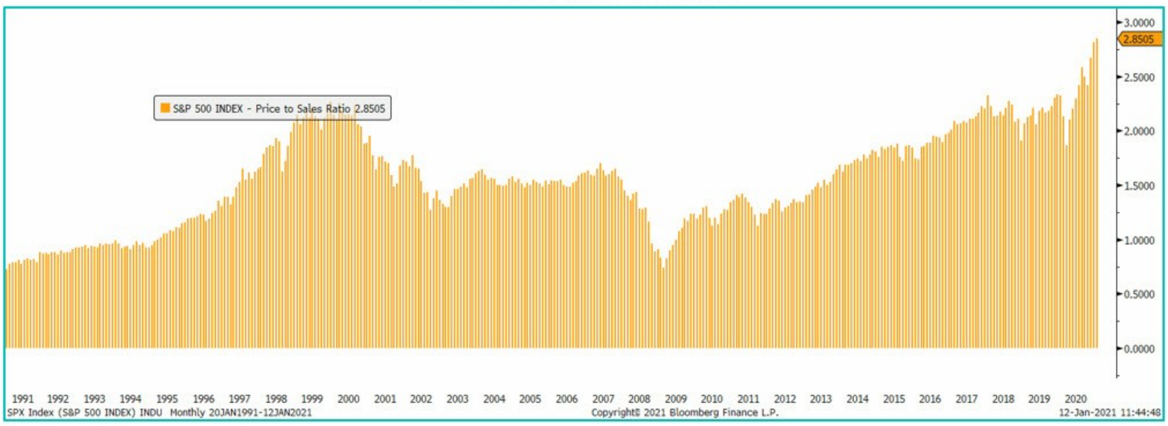
As we have noted before, governments around the world, especially those in developed countries, have gone on a debt binge since the beginning of the pandemic. While we are hopeful that the pace of vaccinations will pick up rapidly in the coming months, the debt burden of the governments and by extension of the people continues to rise rapidly. Central banks around the world have stepped up their respective versions of quantitative easing (QE). The already ballooning balance sheets of the G4 central banks (US, ECB, Japan and the UK) have truly gone into overdrive of late, rising by over 50% in the past 10 months alone. The combined value of the G4 balance sheets was $23,720,800,000,000 ($23.7 trillion). Debts are now in the fourteen-figure territory and they represent over 55% of the combined G4 GDP.



Source: Bloomberg

The rapid expansion of QE has had a two-fold effect. First, the rapid expansion of the balance sheets has severely reduced nominal interest rates on the longer maturity securities. Second, it has succeeded in crowding investors out of government treasuries and into more gnarly areas of fixed income and equities at large. The recent highs for equities were achieved not by earnings expansion, but by multiple expansion. The S&P 500 is trading at 30x earnings, while the NASDAQ's P/E ratio has reached an astronomical 70x. You may have heard whispers of analysts comparing the recent market valuations with those seen in 2000. On this point, we present a chart outlining how just how expensive the S&P 500 has become today. The S&P 500 trades at the highest Price to Sales multiple than it has in over three decades.

S&P 500 Price to Sales

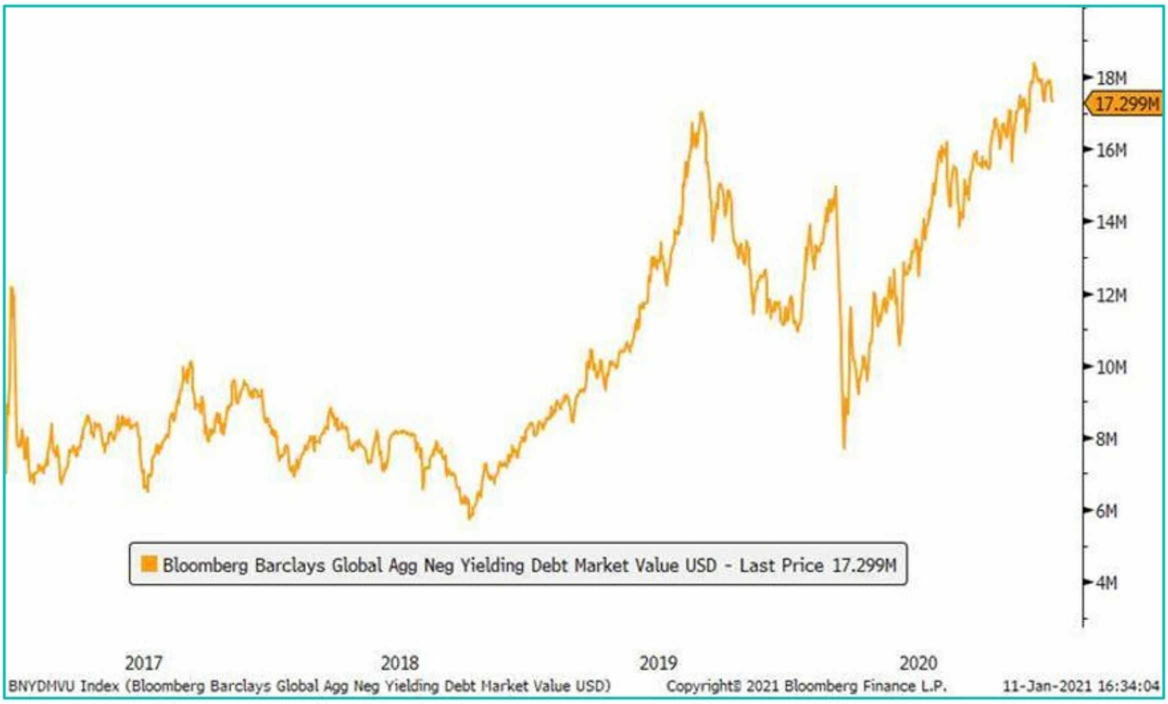


Source: Bloomberg

The concurrent rise of investor complacency in this perilous period is frightening to us. Despite the pandemic doom and a foggy future that lies ahead, 2020 saw a new record be established for new IPOs. 480 IPOs were completed in 2020, which crushed the old high set in 2000.

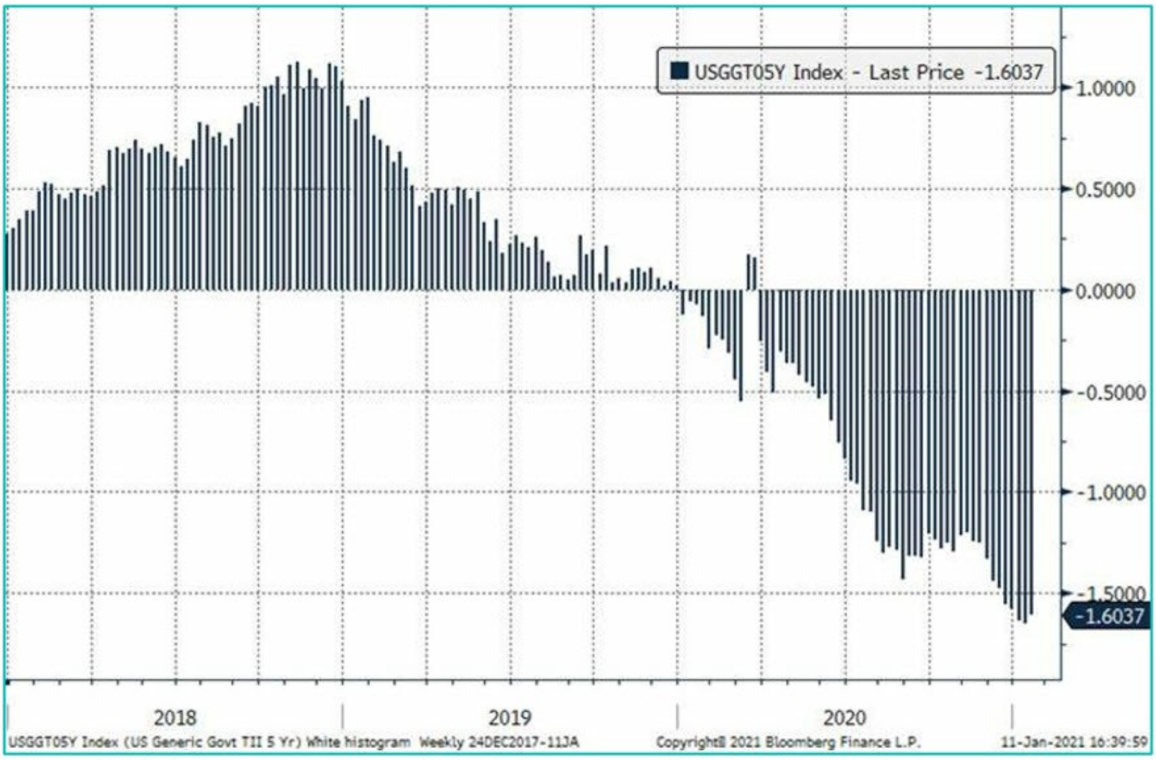
Source: stockanalysis.com

Another confounding development we have come across is the gross value of negative yielding debt in the world. Not negative yielding on an inflation-adjusted basis, but negative yielding on an absolute basis. Paper which if bought today and held to maturity is guaranteed to lose you money. Today, nearly $17,300,000,000,000 ($17.3 trillion) worth of debt trades at a negative nominal yield. To put this into context, the US GDP is ~$20.5 trillion.



Source: Bloomberg

Besides this $17.3T pile of debt that features return-free risk, treasuries worth trillions of dollars around the world trade with a negative real yield. Real yields are calculated by subtracting inflation expectations from nominal yields. We just witnessed the U.S. 5 year real yields declining to a five-year low. With real yields at -1.6%, investors are being charged 1.6% annually to own U.S. 5-year Treasury bonds after adjusting for expected inflation. With the U.S. Federal Reserve and other central banks pinning interest rates to the floor, real yields will likely continue their trend downward.



Source: Bloomberg

We are witnessing the 21st century version of currency debasement. Investors are responding by switching into asset classes that are expected to be store of value. This explains the recent rise in real estate, gold, silver, technology stocks and even bitcoin. Between 2000 and 2020, gold has appreciated by 559%. Between Jan 2000 and Dec 2020, gold has experienced six down years and only double digit down years twice in that period. Gold has been a remarkable store of value not only through antiquity, but in modern times as well. Silver has both investment and industrial demand properties and has risen 391% over the same period. Silver tends to outperform gold in bull markets and its performance has been stronger recently: 2020 saw gold gain 25%, while silver rose an impressive 48%.

Heading into 2021, we expect the U.S. and other Central Banks to maintain extremely accommodative monetary policies and for governments around the world to continue fiscal support of their economies. President Biden is a proponent of “investing in deficit spending in order to generate economic growth” and has said that he will lay out a an economic relief package "in the trillions of dollars”[1]. The can of dealing with financial realities is clearly being kicked down the road in order to stimulate economic growth and employment. We therefore expect deficits to persist, real yields to remain negative and the US Dollar to head lower. There is near-term potential for the US Dollar to stage a rally from its oversold levels, but we would fade any rally in the US Dollar as long as it faces a tepid economic backdrop and negative real yields. This environment should be highly positive for silver and gold.

Biden’s infrastructure and clean energy investment plan envisages $2 trillion of spending and includes initiatives such as accessibility to clean drinking water, expanding 5G networks, installing 500,000 electric vehicle charging stations, purchasing “clean” vehicles for public transport and spurring the installation of millions of solar panels[2]. Silver is used in all these aspects of modern life, particularly in vehicles, solar panels and 5G networks, so its demand will benefit from all of these initiatives.

The strong tailwinds lifting silver and gold higher have been a boon for the miners who have seen their earnings multiply alongside their free cash flows. We have noted the cost discipline of precious metal miners in our recent notes and presentations and this cost discipline has also translated to rising dividend yields for investors. Valuation divergence between the S&P 500 and the GDM index is growing. The precious metal miners today trade at the bottom of their historical EV/EBITDA ratio, while the S&P has rarely been this expensive. The GDM, which has grown its profits by over 444% since 2019, trades at a 60% discount to broader equities today.

Source: Bloomberg

Heading into 2021, we remain optimistic about the precious metal miners at large and more particularly the mid-tier, profitable producers as well as the well-funded explorers that are in the portfolio. Last year saw a number of companies raise capital to explore their properties. The financings demonstrated that there is growing demand for small-cap companies and it is exciting for us to track the progress of these explorers.

Silver averaged just over $22/ounce in 2020, while gold averaged $1707/ounce. We suspect that both metals will trade substantially higher during 2021, powered by the twin tailwinds of negative real yields and currency debasement. 2021 will continue the trend of miners posting strong increases in profits, free cash flows and dividends. Profits have been rising but multiples have not. We believe this is about to change as miners embark into the middle innings of the precious metal bull market where investment gains are created by a sweet combination of rising profits and rising multiples.

[1]https://www.nbcnews.com/politics/white-house/joe-biden-wants-set-aside-deficit-concerns-invest-ailing-u-n1253638
[2]https://joebiden.com/clean-energy/

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NINEPOINT SILVER EQUITIES CLASS - COMPOUNDED RETURNS[1] AS OF DECEMBER 31, 2020 (SERIES F NPP 423)

	1M	YTD	3M	6M	1YR	3YR	5YR	INCEPTION
Funds	21.5%	71.9%	10.9%	31.1%	71.9%	27.5%	28.9%	2.7%
Index	15.7%	53.1%	6.9%	22.7%	53.1%	19.3%	24.9%	-0.4%

[1] All returns and fund details are a) based on Series F units; b) net of fees; c) annualized if period is greater than one year; d) as at December 31, 2020; e) 2012 annual returns are from 02/28/12 to 12/31/12. The index is 100% MSCI ACWI Select Silver Miners IMI (CAD) Index and is computed by Ninepoint Partners LP based on publicly available index information.

The Fund is generally exposed to the following risks. See the prospectus of the Fund for a description of these risks: capital gains risk; class risk; commodity risk; concentration risk; currency risk; cybersecurity risk; derivatives risk; exchange traded funds risk; foreign investment risk; inflation risk; liquidity risk; market risk; securities lending, repurchase and reverse repurchase transactions risk; series risk; short selling risk; small capitalization natural resource company risk; specific issuer risk; sub-advisor risk; substantial shareholder risk; tax risk; uninsured losses risk.

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