Investor Quarterly

Preparing for a More Challenging Year

ROCKINGSTONE ADVISORS LLC

Stock and Bond Divergence, Commodity Declines Warrant Caution

After six years of rising equity and bond prices, recent sharp declines in commodities, currencies and interest rates create short-term dislocations to large segments of the economy, including energy producers, financial institutions and U.S. multi-nationals. Adjustments take time and are rarely smooth; with corporate profit margins at record levels, S&P 500 earnings forecasts too high and financial asset valuations stretched, we have re-positioned portfolios for a more challenging year.

Introducing a New and Updated *Investor Quarterly* for 2015

We introduce an updated *Investor Quarterly*. In this edition, we recap 2014 by asset class and provide detailed 2015 forecasts for a variety of key metrics we track, including: GDP, S&P 500 earnings and price target, 10-year yields, gold, oil and the dollar. We also introduce a new Chart Book (pp 18-25), which presents historical charts covering a wide array of business, labor, economic and financial indicators. This will be a regular feature of our Quarterly.

2014 in Review

Our forecast was directionally accurate on stocks, currencies, commodities and inflation, as we forecast a rise in stocks, a stronger dollar, declines in commodities and a decline in inflation. We were directionally wrong on bonds, however, forecasting a 30 bps rise in the 10-yr U.S. Treasury yield; instead, yields declined about 90 bps to 2.17%.

4Q14 Asset Class Performance

Commodities were the sole asset class to record declines in 4Q14 as oil prices plummeted. Stocks, bonds and Preferreds recorded material gains. REITs were the top performing asset class.

Rockingstone Posts Solid 4Q14 and 2014 Returns, but with Elevated Risk

We posted a fourth quarter return of +4.2% and a full year return of 10.0%. After a disappointing third quarter we managed the fourth quarter volatility quite successfully, making money short the market in October and then capturing the rally. However, we missed the huge rally in Treasuries and in bonds in general.

About Us

Rockingstone Advisors LLC is a New York-based boutique asset management and corporate advisory firm founded by Brandt Sakakeeny.

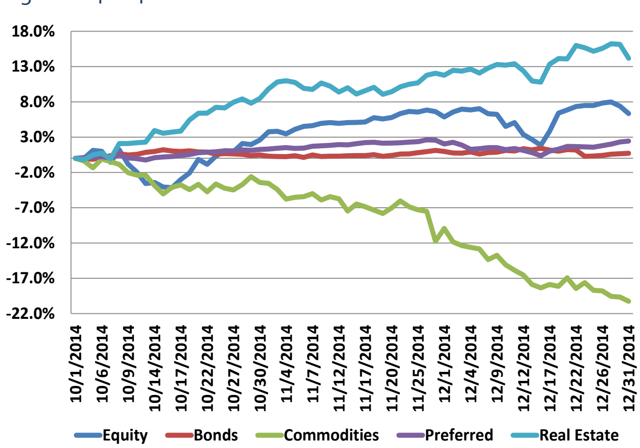
As an SEC-registered investment advisor, we provide multi-asset investment strategies to individuals, families and small institutions through separate accounts.

Our investment strategies attempt to capitalize on pricing inefficiencies across broad asset classes and then across individual securities, with a strong emphasis on fundamental research and analysis.

Thank you for your interest. You can find more information (and some very interesting articles) at:

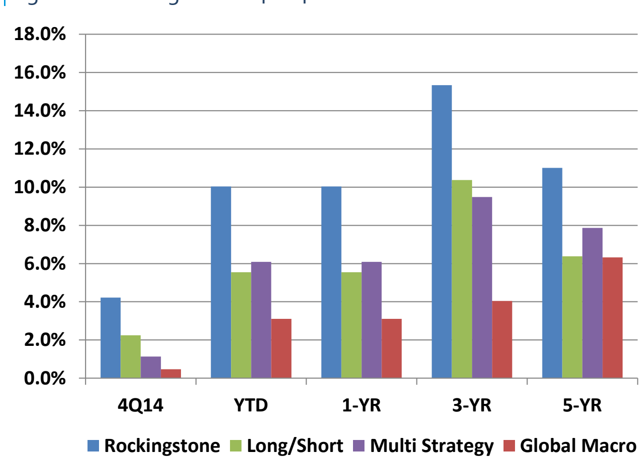
www.rockingstoneadvisors.com

Figure 1: 4Q14 Asset Class Performance[i]



Source: NYSE Arca

Figure 2: Rockingstone's 4Q14 and Historical Returns[ii]



Source: Rockingstone Advisors, Morningstar, DJ Credit Suisse Indices

Please see our End Notes and Disclosures (pages 26-27 of this Investor Quarterly) for important information regarding performance measures. Form ADV available upon request.

Table Of Contents

Detailed Asset Class Performance 3
Real Estate Top Performing Asset Class in 4Q14 and Full Year 3

Equity Performance 5
Surprisingly Strong Year for U.S. Large- and Mid-Cap Stocks 5

Fixed Income Performance 6
Bonds Rally Amid Fall in Interest Rates; Quality Outperforms 6

Commodity Performance 7
Oil Tanks; Precious Metals Begin to Shine 7

2014 Forecast Assessment 8
Key Calls Directionally Right 8
2014 Portfolio Positioning 8

2015 Forecast 10
A Tricky Year: Forecast Masks Intra-year Volatility 10
2015 GDP Forecast 10
2015 S&P 500 Earnings Estimates 11
2015 S&P 500 Price Target 11
2015 US 10-Year Treasury 12
2015 Euro/Yen Forecast 12
2015 Oil Forecast 13
2015 Gold Prices 14
2015 Inflation 15

Five Year Asset Value Forecast 16
Future Real Returns Appear Limited 16
2015 Portfolio Positioning - Equities 16
2015 Portfolio Positioning – Fixed Income 17
2015 Portfolio Positioning – Commodities 17

Chart Book 18
Leading Indicators 18
Labor Market Indicators 19
Production and Business Activity Indicators 20
Consumer and Housing Indicators 21
Price Indicators 22
Valuation and Volatility Indicators 23
Bond Market Indicators 24
Liquidity Indicators 25

Appendix 26
Important Regulatory Disclosures and End Notes 26

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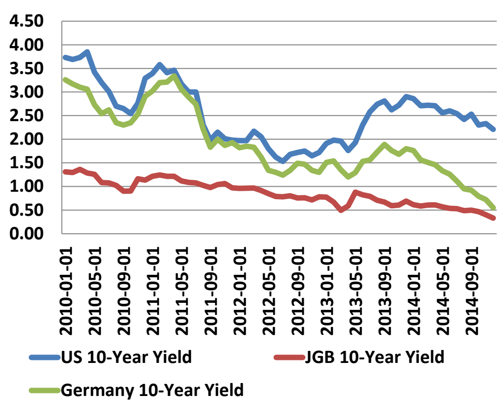
Detailed Asset Class Performance

Real Estate Top Performing Asset Class in 4Q14 and Full Year

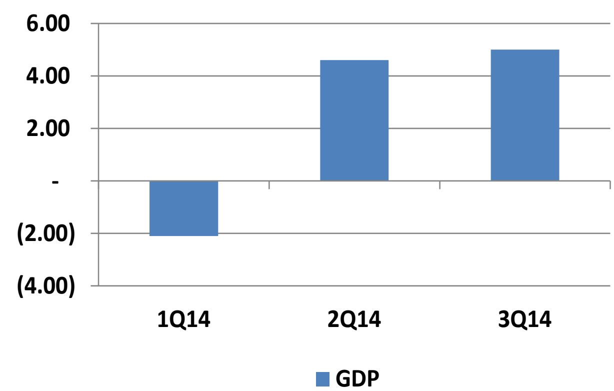
Macroeconomic factors generally set the tone for asset class performance in 2014. U.S 10-year rates followed the decline in European and Japanese sovereign bond yields throughout the year (Figure 3), despite accelerating GDP growth after a surprise drop (weather-related) in the first quarter (Figure 4).

Figure 3: 10-Year Yields, Constant Maturity



Source: St. Louis Federal Reserve, FRED Database; The Economist

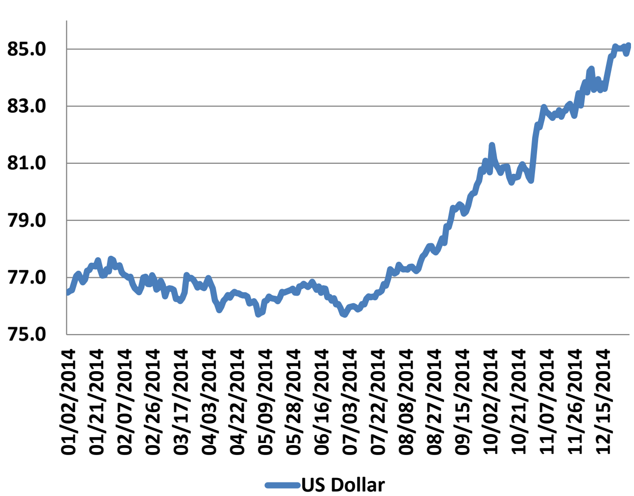
Figure 4: U.S. Quarterly GDP



Source: U.S. Bureau of Economic Analysis, The Economist

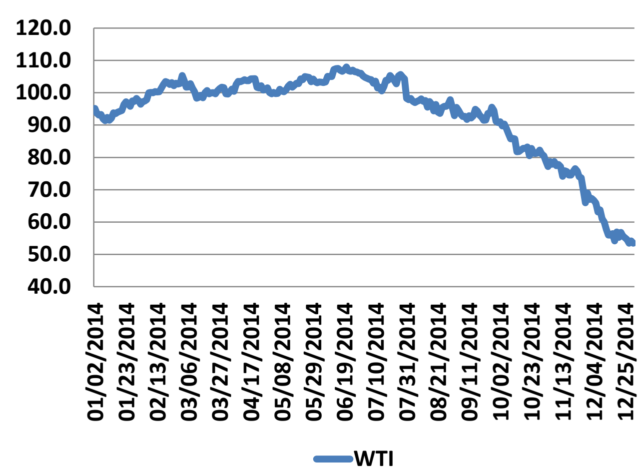
As the U.S. economy improved, European and Japanese growth rates slowed; the differential in the relative outlooks, plus prospects for higher rates in the U.S. and lower rates in Europe and Japan added a substantial tail-wind to an already-rising dollar (Figure 5). The combination of slowing global growth, a stronger dollar and continued supply gains from U.S. oil production forced a sudden re-assessment of the price of oil (Figure 6).

Figure 5: U.S. Dollar, Trade-Weighted



Source: St. Louis Federal Reserve, FRED Database

Figure 6: 2014 West-Texas Intermediate (WTI)



Source: St. Louis Federal Reserve, FRED Database

After rising steadily through 1H14, West-Texas crude (WTI) peaked on June 20, 2014 at $108/bbl, and then fell dramatically, ending the year at $53/bbl. Falling commodity prices lowered inflation expectations and put further pressure on global yields, particularly as the European Central Bank (ECB) contemplated adopting a policy of buying sovereign bonds, much like the Federal Reserve, Bank of England and the Bank of Japan.

The year ended with surprisingly strong U.S. GDP growth (up 5.0%), surprisingly weak rest-of-world growth (flat to down), record stock market levels and lower interest rates.

2014, By Asset Class

Real Estate was the top-performing asset class in both the fourth quarter and the full year (Figures 7 & 8, respectively). REITs were up 14.2% in 4Q14 and a stunning 30.4% in 2014, fueled by improved job growth and a decline in interest rates. REITs, and other high-yielding securities, have benefitted from the abnormally low interest rate environment as investors have sought higher-yielding instruments beyond government bonds.

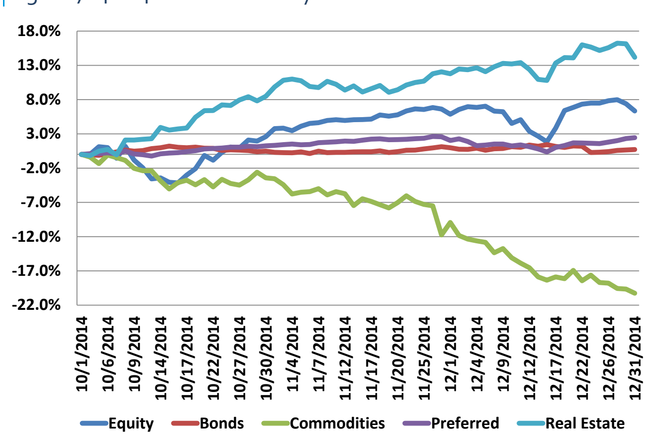
Equities were the second best performing asset class, recording total gains of 6.3% in the quarter and 14.6% for the full year. U.S. Large-Cap equities outperformed Small-Cap, International Developed and Emerging Markets shares as U.S. large-cap companies benefited from a robust domestic economic environment, low interest rates and limited wage inflation, which fueled record profit margins. Earnings for the S&P 500 most likely rose 8.8% to $116.77 from 2013's $107.31. U.S. stocks were also aided by a stronger dollar, which made U.S. assets relatively more attractive for non-dollar denominated investors.

Preferred securities recorded solid fourth quarter and full year gains, up 2.4% and 13.4%, respectively. Like REITs and other high yielding securities, Preferreds tend to outperform in an environment of falling interest rates.

Bonds returned just under 1% in 4Q14 and 5.5% for the full year. Higher quality bonds outperformed lower quality bonds, with 30-year U.S. Treasuries leading the pack, recording gains of more than 25%, the best risk-adjusted returns of any asset class.

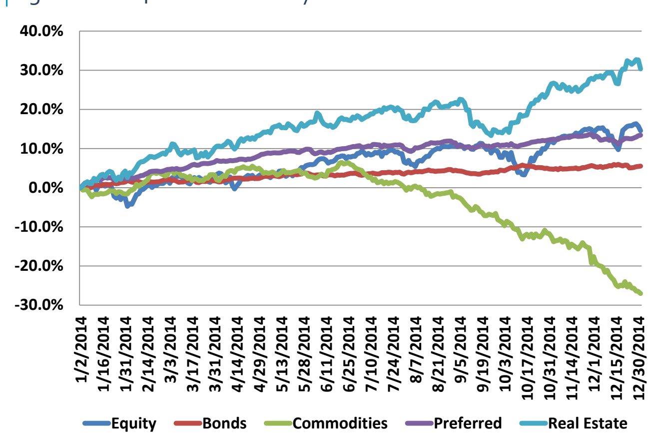
Commodities were the only asset class to record declines, and they were substantial: broad-based commodities declined 20.3% in the fourth quarter and 27.0% for the full year, primarily on a 50% decline in the price of oil.

Figure 7: 4Q14 Performance by Asset Class



Source: NYSE Arca

Figure 8: 2014 Performance by Asset Class



Source: NYSE Arca

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Equity Performance

Surprisingly Strong Year for U.S. Large- and Mid-Cap Stocks

During the fourth quarter, U.S. small-cap stocks outperformed U.S. large-caps and mid-caps, as well as Foreign and Emerging indices, recording gains of 11.4% in the quarter, vs. 6.3% for large-caps and 8.2% for mid-caps (Figure 9). The outperformance was probably attributable to the fact that (i) small-caps had lagged their larger-cap brethren throughout the year, (ii) the fourth quarter is typically a seasonally strong period for small-caps, and (iii) investors may have been trying to minimize exposure to slower-growing Europe as well as currency translation risk as small cap stocks generally have less international exposure than large-cap stocks.

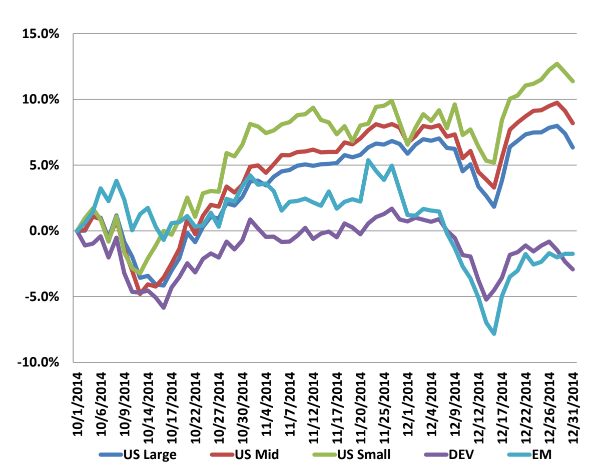
Foreign Developed equities and Emerging Markets equities both posted declines in dollar terms given currency erosion and a flight to quality. Foreign Developed fell 2.9% in dollar terms while Emerging Markets equities fell 1.7% in dollar terms during the quarter.

2014 Full Year

For the full year 2014, U.S. large-cap and mid-cap stocks performed exceptionally well, delivering total returns of just under 15% (Figure 10). Small-caps lagged, recording full year returns of 6.2%. Small-caps had been relatively over-valued compared to large-caps, in our view, so we were not surprised to see the relative underperformance. That said, as we were short small-caps we would have preferred to see an absolute decline in the index.

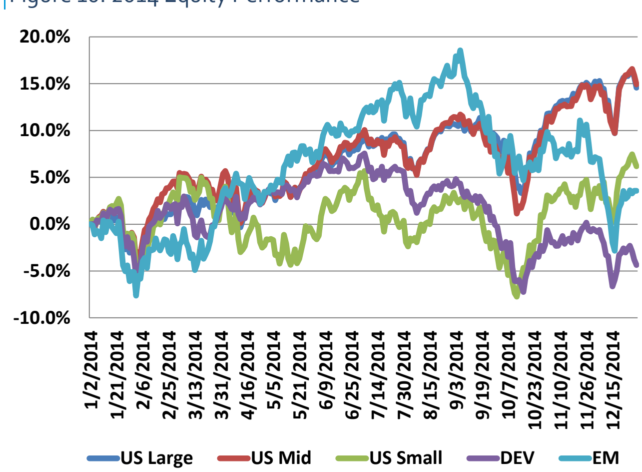
Despite a stronger dollar, Foreign Developed recorded full year gains of 3.6% on a dollar basis, while Emerging Markets posted a decline of 4.4% on a dollar basis. Among top foreign developed markets, Japanese equities (Nikkei) posted gains of 8.8% in Yen terms and declines of 5.1% in dollar terms; the Euro area rose approximately 2.7% in Euro terms but was down 9% in dollar terms. Among Emerging Markets, Chinese A shares rallied sharply, up 49% in local currency terms and 46% in dollar terms. Russia was the big loser: its market recorded losses of 5% in local currency terms but lost 45% in dollar terms due to the crash in the Russian Ruble, which is closely correlated to the price of oil.

Figure 9: 4Q14 Equity Performance[iii]



Source: NYSE Arca

Figure 10: 2014 Equity Performance



Source: NYSE Arca

Fixed Income Performance

Bonds Rally Amid Fall in Interest Rates; Quality Outperforms

During the fourth quarter, high quality bonds (U.S. high grade corporates and U.S. Treasuries) rallied on a flight to quality (Figure 11). U.S. Treasuries recorded gains of 2.1% in the quarter while U.S. high grade corporates gained 1.5%. U.S. high yield bonds declined 2.3% in the quarter on investor concerns that the large decline in oil prices could potentially lead to higher default rates among issuers from the energy sector, which constitutes approximately 20% of all outstanding high yield debt issuance. CCC yields rose from roughly 9.5% at the beginning of the quarter to 11.2% by the end of the quarter, while BBB yields rose from 3.6% to 3.8%.

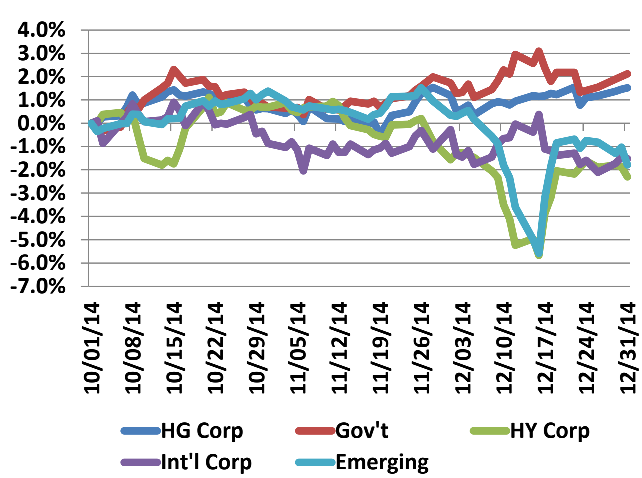
As in the equity complex, Foreign high-grade and Emerging Markets bonds posted 4Q14 declines in dollar terms though gains in local currency. Foreign Developed corporate bonds declined 1.5% and Emerging Market sovereign bonds declined 1.8% in the fourth quarter, both in dollar terms.

2014 Full Year

Fourth quarter results were in line with full-year trends: a flight to high quality bonds and dollar-denominated assets (Figure 12). U.S. Treasuries were the top-performing fixed income security (among those we track), gaining 8.6% (8-10 year paper), a phenomenal risk-adjusted return; longer-dated Treasuries performed even better: up 25% for 20-30 year paper! High grade corporates also performed well, posting full year returns of 8% in 2014. Lower quality bonds suffered: high yield bonds ended the year roughly flat on concerns surrounding energy exposure and the price of oil. CCC bonds began the year at just over 9% yields, rallied to 8% and then finished the year at 11.2%. BBB bonds began the year at effective yields of just over 3.9% and rallied down to 3.4% before ending the year at 3.8%.

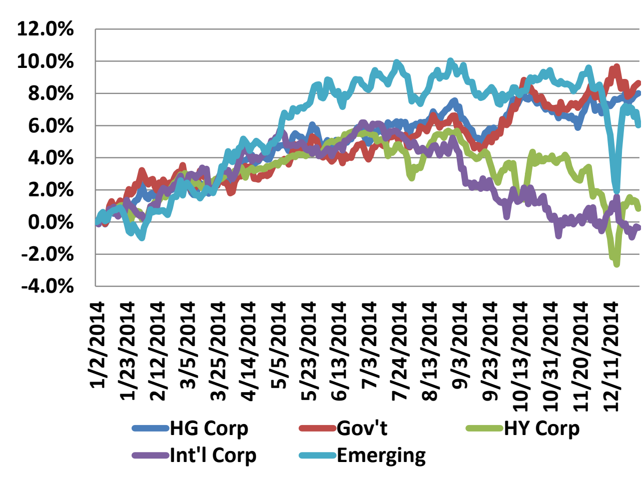
Outside of the U.S.: foreign currency bonds underperformed given the strong dollar. International corporates posted a decline of 0.4% in dollar terms, while Emerging Market sovereign bonds were the one exception: they gained 6% for the year.

Figure 11: 4Q14 Fixed Income Performance[iv]



Source: NYSE Arca

Figure 12: 2014 Fixed Income Performance



Source: NYSE Arca

Commodity Performance

Oil Tanks; Precious Metals Begin to Shine

During the fourth quarter, Oil, Precious Metals, Agriculture and Base Metals all declined (Figure 13). While each of these commodities has a different and distinct driver, the common theme across the commodity complex is that they are typically priced in U.S. dollars, and as the dollar strengthened through the quarter, each witnessed varying declines in price.

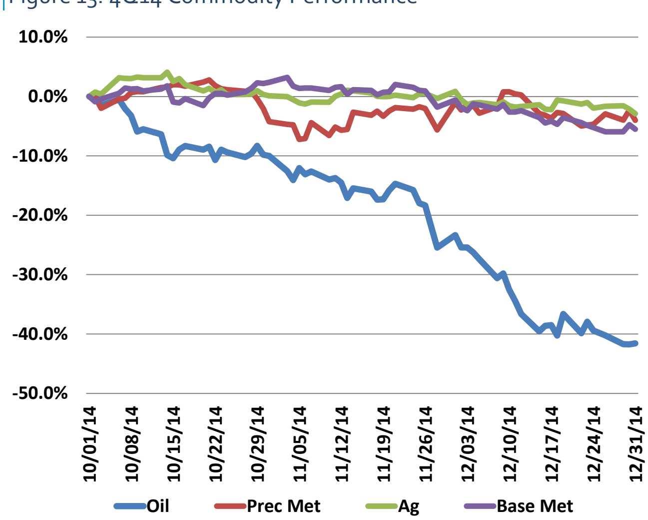
Oil was clearly the standout decliner (down 40%) in the quarter, suffering from slower global demand coupled with ongoing increases in U.S. production. With no curtailment of production by the Saudis, the oil market is currently perceived to be over-supplied by roughly 1.5-2.0 million barrels per day.

Precious metals declined 4% in the quarter, bottoming on December 22nd and then rallying through year-end and into 1Q15. Agriculture was down 2.1% in the quarter on strong harvests of corn and wheat and better weather in Brazil. Base metals declined 5.5% in the quarter, mainly fueled by concerns over global growth and deepening concerns about Chinese demand.

2014 Full Year

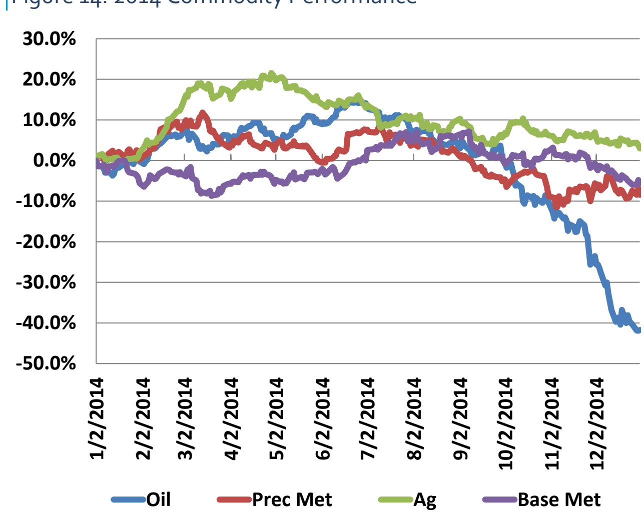
It was the tale of two calendar halves: the first half of the year witnessed generally rising commodity prices in Ag (Ukraine tensions, Brazil weather), Oil and Precious Metals (ISIS gains, Dollar/Yen/Euro debasement). Base metals were the rare underperformer as prices declined in the first half (slower global growth, China concerns). It was only when the dollar started to rally at the end of June that the entire complex simultaneously lost its footing and began a steady decline that persisted throughout the second half of 2014. In fact, only Ag was able to post full year gains (up 3%), while base and precious metals were down mid-single digits and oil down more than 40%. Prices for precious metals, unlike base metals, appeared to bottom in mid-December and rallied into year-end (Figure 14).

Figure 13: 4Q14 Commodity Performance[v]



Source: NYSE Arca

Figure 14: 2014 Commodity Performance



Source: NYSE Arca

2014 Forecast Assessment

Key Calls Directionally Right

In January 2014 we introduced our Key Metric Forecast for year-end (December 31, 2014). We re-evaluate our forecasts mid-year and highlight any changes to our outlook. The following table (Figure 15) outlines our performance against our forecasts:

Figure 15: 2014 Key Metric Forecast vs. Actual

Metric	Jan 2014 Est.	July 2014 Est.	YE Actual
US GDP	2.8%	NC	2.3%
2014 S&P 500 EPS (RSA/Street)	$117.51/$119.99	NC/$119.99	$116.77 (est.)/$119.99
2015 S&P 500 EPS (RSA/Street)	$128.22/$137.26	NC/$134.10	NC/$131.01
S&P 500	1925	2050	2058
DJIA	17,350	17,500	17,823
10-Yr. U.S. Treasury Yield	3.30%	2.60%	2.17%
Euro/USD	1.25	NC	1.22
USD/Yen	115	NC	121
Oil (WTI)	$98	$75	$53
Gold	$1,210	$1,110	$1,206
Inflation	1.7%	NC	1.6%

Source: Rockingstone Advisors, The Economist, Standard and Poors, NYSE Arca, St. Louis Federal Reserve

In January 2014 we expected solid GDP growth would drive higher corporate earnings, a higher stock market and help to contribute to a stronger trade-weighted U.S. dollar. We expected lower oil prices, lower gold prices and lower inflation, due in part to the stronger dollar. By year end, these forecasts were directionally accurate, though stocks outperformed our initial expectations and oil materially underperformed our expectations.

GDP, gold prices and inflation were fairly close to our expectations, though 1Q14 GDP was hampered by poor weather. Our S&P 500 EPS estimate was slightly high, but directionally closer than the Street's estimate, though not all companies have reported 4Q14 EPS. Based on current reporting of 4Q14 results, we see little likelihood that S&P 500 earnings will beat our number and come in closer to Street expectations.

We were directionally wrong on our 10-year Treasury forecast, which is obviously a fairly critical metric. After starting the year at 3.0%, we expected a 30 basis point rise through the year to end at around 3.3%. To the contrary, not only did rates fall rather than rise, but the move was particularly sharp: declining 113 basis points to end the year at 2.17%.

We completely missed the sharp decline in sovereign bond yields across Japan and the Eurozone, and the fact that U.S. rates would not doubt follow other global rates given historical spreads. The rapid decline in oil is adding to the deflationary pressures already being felt most acutely in Europe and Japan given their lackluster growth, poor demographics and the structural challenges to their economies.

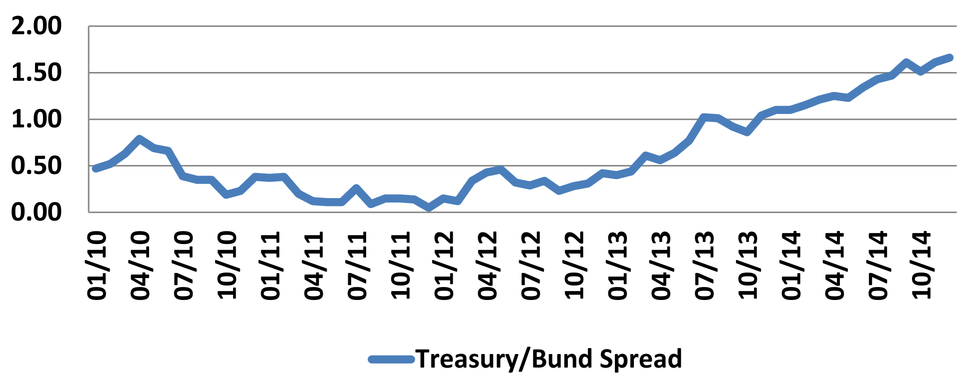
2014 Portfolio Positioning

From a portfolio positioning standpoint, our forecasts led us to overweight U.S. equities (and large-cap over small cap), hedge our European and Japanese equity exposure, overweight tech, industrials and discretionary and underweight energy, materials and utilities. We were short oil in the mid-$70s but covered that short in the mid-$60s.

We were underweight high quality bonds (though fortunately not short) and overweight lower quality bonds, so while our absolute 2014 returns of 10% were solid, we could have generated similar to higher returns with a lot less risk if we had properly forecast interest rates and junk bond spreads. In addition, a long position in U.S Treasuries and a short position in spread products (BBB or CCC) would have produced higher returns with lower risk.

(We now have a position in intermediate and long-term Treasuries (a clear sign of a top!) based primarily on the spread between German and U.S. bonds that seems historically wide to us (Figure 16), though we assume some of this differential may be attributable to expectations of ECB sovereign bond purchases as the Fed has wrapped up its purchases of U.S. Treasuries and continues to signal interest rate increases later this spring or summer).

Figure 16: Spread between 10-Year U.S. Treasury and 10-Year German Bund



Source: St. Louis Federal Reserve, FRED Database

Our sector allocations were generally neutral to slightly negative to our 2014 returns, as we were generally overweight more cyclical sectors and generally underweight more defensive sectors, especially utilities as we did not expect interest rates to fall. Off-setting our sector selection, to some extent, was our large over-weight in REITs and Preferreds, which we have used a bond proxy in light of the low yield environment.

Stock picking definitely helped us in 2014, as some of our largest positions posted significant annual gains. Our best performers were Apple, Delta, Facebook, Home Depot, Micron, Northstar Realty Finance, JetBlue, Robert Half and Walmart.

Our worst performers were AdecoAgro SA, ExxonMobile, and Las Vegas Sands.

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2015 Forecast

A Tricky Year: Forecast Masks Intra-year Volatility

We introduce our 2015 Forecast for key market metrics. The one caveat we highlight— aside from the fact that predicting outcomes is inherently difficult— is that the nature of our forecasts are for year-end, which can mask intra-year volatility.

Our current view is that the severe dislocation in commodities, currencies and interest rates witnessed over the past several months may put near-term pressure on financial assets as companies adjust to an economic environment that appears quite different from the one they faced this time last year. It takes time for companies to re-position assets, streamline operations and adjust their sales resources to target segments that may differ materially today from where they were focused last year. Over time, companies do make these adjustments, and lower commodity prices and lower interest rates are generally a good thing as we believe they are more disinflationary than deflationary for most consumers and businesses. Our potential concern arises from the fact that the impact of market dislocation is immediate whereas the benefits somewhat deferred. Hence, we expect the first half to be more challenging than the second half, but in general we are more cautious in our outlook for financial assets than we have been since the Eurozone crisis in 2010.

On the plus side, markets frequently over-shoot both ways; if oil prices rebound to the $55 - $65 level that may lessen the impact of dislocation and would reduce near-term stress oil patch lenders, for instance, in our view. The same may be said for interest rates and the dollar, both of which may witness a reversal of recent trends.

Figure 17: 2015 Key Metric Forecast

	Year Ended December 31, 2015		
Metric	**Directional**	**Band**	**Point**
US GDP	Up	3.2% - 3.5%	3.3%
2015 S&P 500 EPS (RSA/Street)	Up	$125.00/$131.01	$125.00/$131.01
S&P 500	Flat	1975 - 2125	2050
10-Yr. U.S. Treasury Yield	Flat	1.8% - 2.2%	2.00%
Euro/USD	Down	1.15 - 1.00	1.05
USD/Yen	Up	120 - 130	125
Oil (WTI)	Up	$45 - $65	$57
Gold	Up	$1,325 - $1,450	$1,385
Inflation	Flat	1.5% - 1.7%	1.6%

Source: Rockingstone Advisors, The Economist, Standard and Poor's, NYSE Arca, St. Louis Federal Reserve

2015 GDP Forecast

We are forecasting an improvement in US GDP growth to +3.3% in 2015, within a band of 3.2% - 3.5%. We expect growth to accelerate for two reasons. First, the first quarter's 2014 GDP was adversely affected by horrible winter weather as GDP declined 2.1%, so 1Q15 comps are easy. Second, the trend over the last two quarters has been quite strong: +4.6% in 2Q14 and +5.0% in 3Q14 as private investment spending accelerated and sequestration ended, boosting government spending. However, we believe the recent trend is unsustainable through 2015 as a slowdown in energy investment may adversely affect private investment and export growth may slow due to economic weakness overseas and a stronger dollar. Lower interest rates should aid residential fixed investment, but the early signs (from homebuilders like KB Homes) are not especially encouraging.

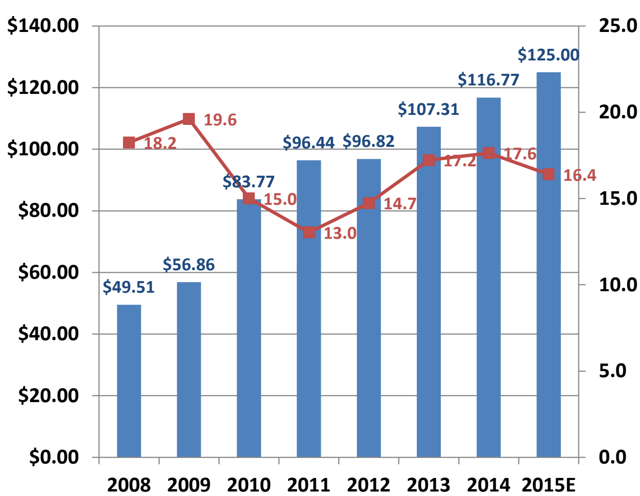
2015 S&P 500 Earnings Estimates

It appears that the S&P 500 will record operating earnings of $116.77 for 2014, yielding a growth rate of 8.8% from 2013, and about a dollar less than we had forecast and several dollars worse than the Street's estimate. As we noted in prior Investor Quarterlies, Street estimates have been declining steadily; at this time last year Street estimates were approximately $121.50. Assuming actual results are closer to $116.77, this figure might imply that current Street estimates of $131.01 for 2015 are also inflated by about 4%. Applying this discount to the current Street estimate yields a target EPS of $125.

In addition, we would expect some deceleration from recent trends based on several of the factors discussed earlier: a stronger dollar, lower energy prices and lower interest rates. It is tough to see how Energy and Financials will record YoY earnings growth. In addition, corporate profit margins are at record highs and hence there seems to be limited room for material increases from current levels.

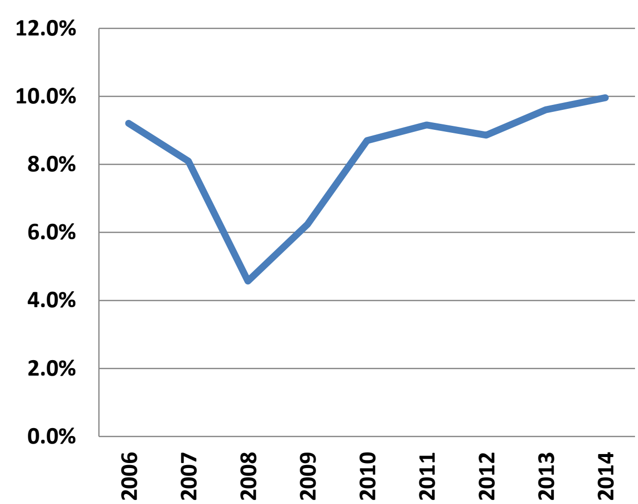
Thus we would expect earnings growth to decelerate from 8.8% in 2014 to a figure roughly in the mid-single digits in 2015, something like 4-6%; applying this growth rate to $116.77 yields an EPS range of $122 - $124 for 2015. This figure assumes while energy and financials may be hampered by lower oil prices and interest rates, respectively, sectors like consumer discretionary and homebuilders should expect a tailwind from these developments over time.

Figure 18: S&P 500 EPS EPS (LHS) and P/E (RHS)



Source: Standard and Poor's, Rockingstone Advisors

Figure 19: S&P 500 Profit Margins



Source: Standard and Poor's

2015 S&P 500 Price Target

We are forecasting a potential range of the S&P 500 by year end of 1975 – 2125, with a point target of 2050, which assumes a flat year. We are assuming a decline of just of one multiple point due to anticipated slightly higher interest rates and slightly lower EPS growth rates. Note that even our assumption of 16.4x is above the market's traditional multiple of approximately 15x. We think that is probably fair given the abnormally low interest rate environment; but it does worry us to apply a premium multiple to late-cycle earnings. Investing with a margin of safety typically implies applying a premium multiple to early cycle earnings and a discount multiple to late cycle earnings.

The lower end of the range would be achieved if our expected multiple of 16.4x is applied not to our $125, but rather to $120, which is certainly within the range of expectations, implying low single-digit EPS growth vs. our current mid-single digit assumption and a down market YoY.

On the upper end, however, we could see 2125 or possibly more if one of two things occurs: earnings exceed our figure and are closer to the Street' $131, or our assumption for a lower multiple proves to be too conservative. We think it's unlikely to see both (a higher multiple on higher EPS, which would yield 2290 on the S&P 500). That said, we have underestimated the S&P 500 price in each of the last two years.

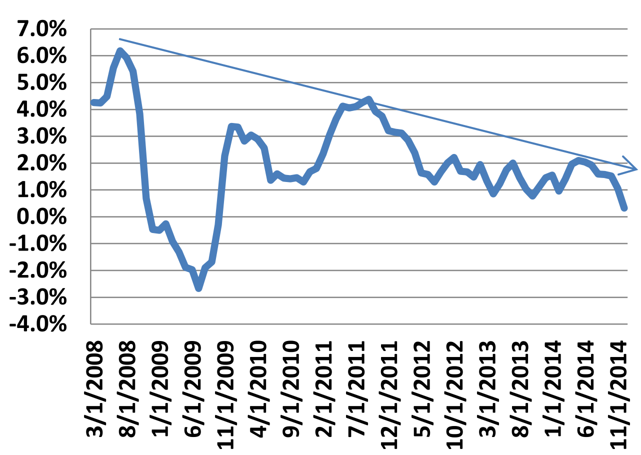
2015 US 10-Year Treasury

With the caveat that we were not able to get even the directional call correct in interest rates in 2014, we are trying again. Based on flat to declining inflationary pressures, anemic global growth, new regulatory rules on the holding of risk-free assets, and exceptionally low European sovereign rates, we expect 10-year U.S. Treasury yields to fall from current levels, bottoming around 1.3% - 1.5% in 1H15 before ending the year roughly where they started at around 2.0%.

Wage inflation continues to be muted (Figure 20) and falling, not rising; capacity utilization (Figure 21) has risen from its 2008 lows, but still below historical levels. Most importantly, a stronger dollar is at the very least disinflationary, and potentially deflationary.

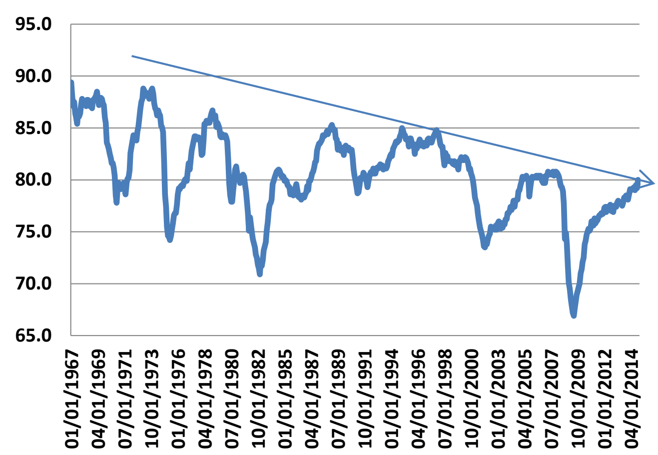
The factors that would endanger our forecast would be (i) a correction or reversal of recent dollar strength (but this would most likely be the result of slower U.S. growth), (ii) a correction or reversal in the price of oil (certainly logical given the likelihood of an overshoot, but given the current supply glut it's unlikely oil makes a major move back into the $70s), or (iii) a rapidly accelerating economy, of which presently there is little evidence.

Figure 20: Wage Inflation YoY



Source: St. Louis Federal Reserve, FRED Database

Figure 21: Capacity Utilization



Source: St. Louis Federal Reserve, FRED Database

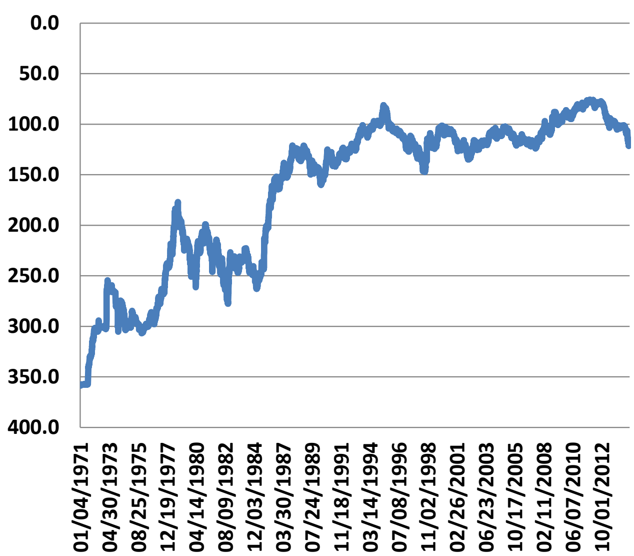
2015 Euro/Yen Forecast

The dollar has rallied sharply against most major currencies on improving economic growth in the U.S. and the prospect for higher interest rates sometime in 2H15.

Currencies typically make multi-year moves, and in our *3Q13 Investor Quarterly* we outlined the factors behind what we believed was the beginning of a multi-year period of a rising dollar: "A Case for a $trong Dollar." While we were a little early, our view was predicated on the following factors: (i) improving current account deficit as U.S. households paid down debt and government deficits declined; (ii) improving trade balances due to U.S. energy production; and (iii) the likelihood for higher U.S. interest rates as the U.S. economy outperformed Europe and Japan.

We continue to believe that the factors we outlined remain in place. That said, the dollar has made a fairly significant move in a relatively short period, and it seems that everyone is on the same side of the trade: long U.S. dollar, short Euro and Yen. For this reason, we may very well see a correction or at least a partial retracement of the sharp move witnessed over the last six months. We believe, though, that a stronger dollar is the most logical longer-term outlook.

Figure 22: $/Yen (Inverted Scale)



Source: St. Louis Federal Reserve, FRED Database

Figure 23: Euro/$

Source: St. Louis Federal Reserve, FRED Database

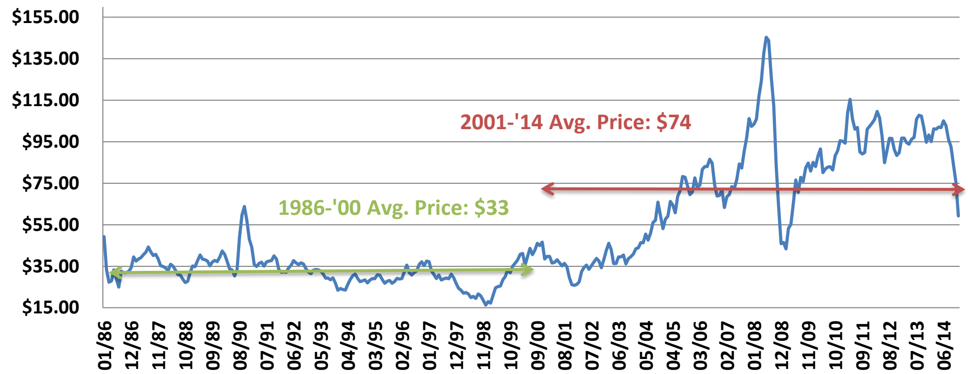
Based on current central bank policies, we believe the Euro may most likely finish the year in a range of between 1.15 and 1.00, with a point estimate of 1.05. We believe the Yen may most likely finish the year in a range of between 120 and 130, with a point estimate of 1.25.

2015 Oil Forecast

While we were directionally correct in our call for lower oil prices, we grossly mis-forecast oil prices. We were not alone, but in hindsight given the massive increase in U.S. supply the speed of the decline should not have surprised us. It was just surprising that it took a move in the currency markets to get oil moving.

Looking back in history, from 1986-2000, WTI prices averaged $33/bbl in constant (inflation-adjusted) 2014 dollars. The price of oil then "re-rated" in early 2000. In the subsequent 15 years, WTI prices averaged $74/bbl (Figure 24) in inflation-adjusted 2014 dollars, more than 2x their historical average!

Figure 24: Inflation-Adjusted WTI Price/Barrel (2014 Prices)



Source: St. Louis Federal Reserve, FRED Database, Rockingstone Advisors

The key question is: Have oil prices "re-re-rated" back to the historical norm of $33 (inflation adjusted) that existed from 1986-2000, or have they simply fallen in the short-term in response to near-term excess supply, and within a period of 6-18 months as the market responds to current price signals, will recover back to the "re-rated" range of around $74/bbl?

Our best assessment is that the answer lies somewhere between the two price levels. From 1985-2000 (i) geopolitical risk was reasonably muted (with the exception of Dessert Storm in 1990-91), (ii) the trade-weighted dollar flat to rising (1987-2000), and (iii) oil adequately supplied amid growing demand. Conversely, from 2001-14, (i) geopolitical risk was heightened, (ii) the trade-weighted dollar declining, (iii) oil inadequately supplied amid growing demand; hence, the re-rating in price from $33 to $74 that occurred. Presently, geopolitical risk remains high, but the trade-weighted dollar is rising, oil remains adequately supplied, and yet demand trends are softer, due in part to slow global growth, but also due to the impact of alternatives.

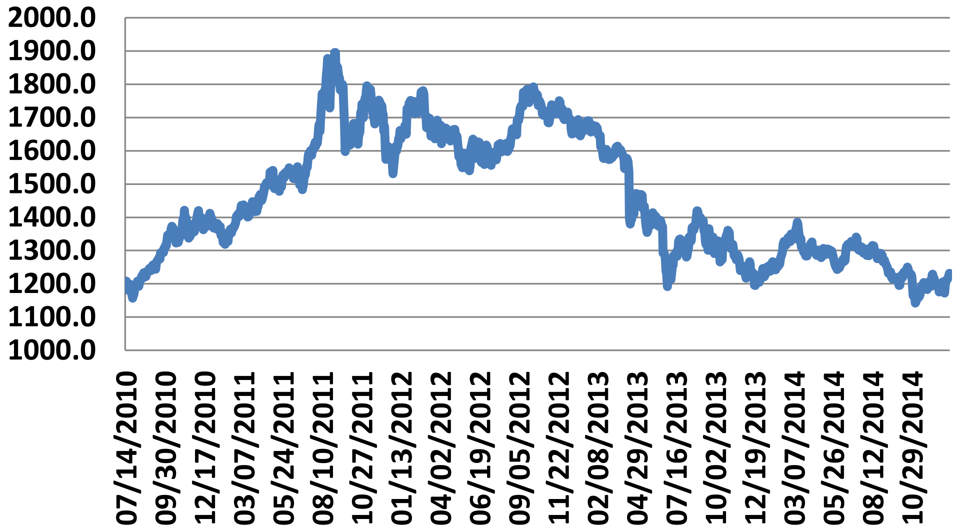
For these reasons we do not believe oil prices return rapidly to the low-$70s; rather, we believe that after testing the high $30s or low $40s they will most likely end the year higher than current levels but not back to the mid-$70s. So if the median price is $53 from 1986-2014, we have calculated a weighted average that yields our target of $57 within an anticipated range of between $45 to $65.

2015 Gold Prices

Gold began the year at $1,225/oz, which was a sharp decline from 2013's beginning price of $1,663/oz. We expected gold prices to be flat to slightly down, and our initial target was $1,210/oz, but which we trimmed to $1,110 in our July *Investor Quarterly* based on the stronger dollar. During the year gold peaked at about $1,378/oz in March and hit its intra-year low at $1,142/oz in November before ending the year at $1,206/oz (Figure 25 on the following page).

Looking forward, gold appears to have bottomed and has started to rally along with silver. While it is unclear how sustained the rally may be, given the ECB's newly-announced bond buying program, coupled with ongoing Bank of England (BoE) and Bank of Japan (BoJ) actions, as well as a potential Greek exit fears, we are inclined to think the direction will be up this year, and are forecasting a year-end range of $1,325/oz to $1,450/oz with a point forecast of $1,385/oz. Lower inflation may act as a drag on pricing, but we think gold's role as a surrogate currency (rather than an inflation hedge) is what supports 2014 price appreciation.

Figure 25: Gold Prices (USD/London Close)

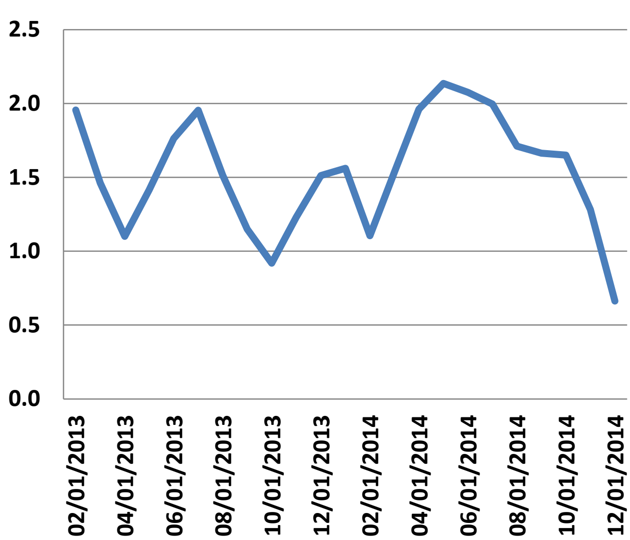


Source: St. Louis Federal Reserve, FRED Database

2015 Inflation

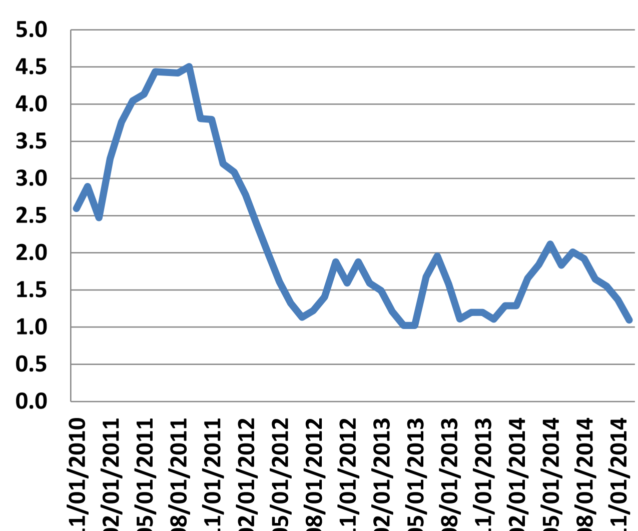
We had forecast inflation to decline slightly based on our expectations of lower commodity prices and a stronger dollar. While we believe oil prices will stabilize around current levels and should finish the year higher, the short-term move in energy prices could very easily be lower until supply/demand find equilibrium. This, plus the stronger dollar, record low employee participation rate in the labor market, slowing Chinese demand for commodities, and slower global growth should limit inflationary pressure. We are forecasting a range of 1.5% to 1.7% with a point estimate of 1.6% for CPI.

Figure 26: Consumer Price Index (CPI - % change YoY)



Source: St. Louis Federal Reserve, FRED Database

Figure 27: Producer Price Index (% change YoY)



Source: St. Louis Federal Reserve, FRED Database

Five Year Asset Value Forecast[vi]

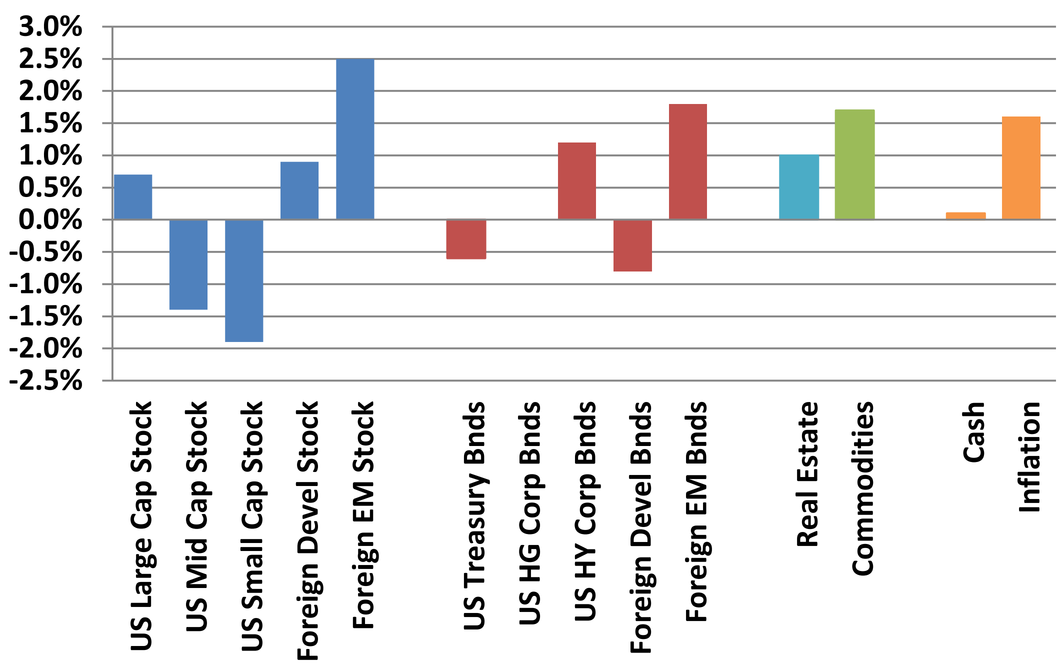
Future Real Returns Appear Limited

We present our five-year asset value forecast below (Figure 28). We are forecasting limited real long-term returns on financial assets as we believe the discount rates applied to these assets is abnormally low due to central bank intervention.

Our forecasts are predicated on the assumption that asset values mean-revert over time. In essence for equities, corporate profit margins and P/Es will decline (if currently above their historical mean) or expand (if currently below their historical mean) over the longer-term. Given our expectations of flat to down total returns, we expect the "give" of earnings and dividends to be exceeded by the "take" of mean-reverting margins and multiples, both of which are above their historical mean. In fixed income we expect the "give" of coupons will be exceeded by the "take" of mean-reverting inflation and real rates, both of which are below their historical mean.

Of course short-term returns may not necessarily match our longer-term return predictions; markets are significantly more random over the short-run than the long-run.

Figure 28: Five-Year Asset Class Forecast



Source: Rockingstone Advisors

2015 Portfolio Positioning - Equities

As we see limited gains in the indices, our priorities are on (i) capitalizing on relative value across the various indices (large vs. small, Japan vs. Europe); (ii) capitalizing on relative value across sectors (financials vs. utilities); (iii) finding relative value in individual securities; and (iv) shorting indices, sectors and names that appear materially over-valued with operational or structural challenges (we rarely short value alone).

From an index standpoint, we think there is still some value in large-cap names, and continue to be over-weight large-caps and short the small-cap index. We are now also short the mid-cap index, but remain net long overall. We are neutral weight the U.S., under-weight Europe and over-weight Japan. While we like Emerging Markets longer-term, we believe there are some short-term struggles adjusting to lower commodity prices and a stronger dollar, so are currently under-weight EM.

Across sectors, we are now less over-weight Financials, Technology and Industrials, but we still find some value in all three sectors. We think Financials are the longer-term winner as margins remain constrained and values still close to book. Tech and Industrials are probably both hampered by a stronger dollar and Industrials by latent oil exposure. We are less under-weight Energy (but not yet neutral) as we have been scaling into the sector very cautiously, believing that oil still has further to fall before it recovers. We continue to be neutral-weight Discretionary and Healthcare, and under-weight Staples and Utilities. We thought Discretionary would be acting better in light of lower oil prices; however, the initial commentary coming out of the retailers was not overwhelming positive. Healthcare has been the place to be; unfortunately we are now neutral, though we have owned the biotech ETF for some time. We are increasingly worried about the healthcare sector as (i) the trade seems crowded, (ii) there appears to be growing price pressures in the pharma market; and (iii) we think there is a very high likelihood that the Supreme Court overturns Obamacare. Utilities and Staples both strike us as quite expensive given their role as bond proxies and given where interest rates are.

Our largest individual holdings are The Advisory Board Company, Apple, Delta, General Dynamics, Home Depot, KKR, Morgan Stanley, New Mountain Capital, Northstar Asset, Northstar Realty, Precision Cast Parts and Walmart. Our largest individual shorts are on IBM and Prosperity Bancshares.

2015 Portfolio Positioning – Fixed Income

For 2015 we have added new positions in Treasuries (more of a trade than a long-term commitment), reduced some of our high yield exposure, but generally maintained our fixed income orientation to one of slightly higher yields by the end of the year.

We are long (intermediate and long-term) Treasuries, agencies, high grade corporates, high yield, floating rate debt, bank debt and emerging markets debt. We have no shorts in the asset class, having learned that painful lesson last year.

We continue to be long converts and preferreds for hybrids.

2015 Portfolio Positioning – Commodities

We have recently added to our silver holdings, which were quite minimal, and are contemplating creating a new long position in gold (most likely denominated in Yen or Euro). Central bank actions, we believe, should continue to add price support for both metals, as well as geopolitical issues in Russian and in Greece. We continue to own Stillwater Mining (SEC) as a platinum/palladium play. We have added some ag stock plays, though we do not own ag outright in size.

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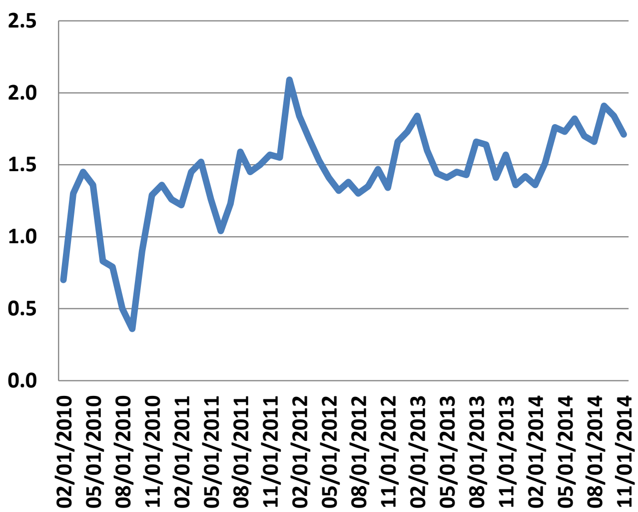
Chart Book

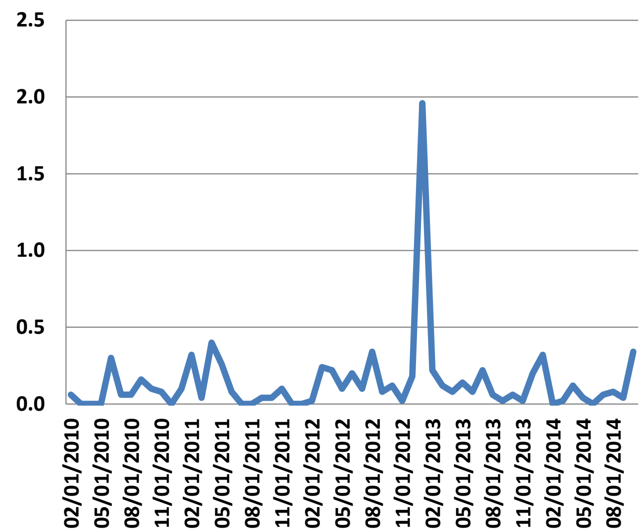
Leading Indicators

Figure 29: Index of Leading Economic Indicators



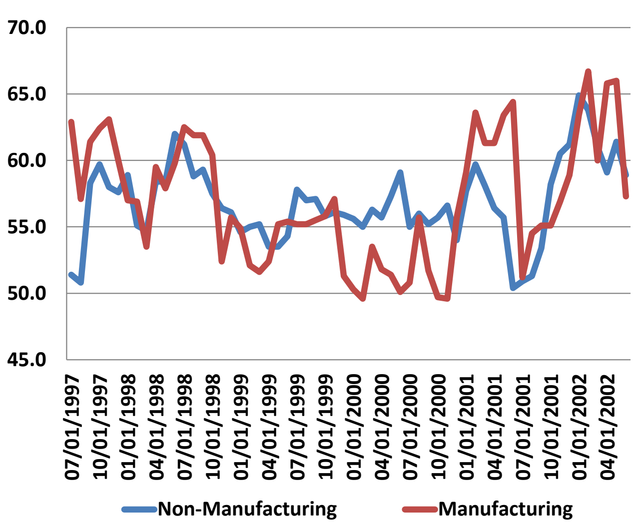
Source: St. Louis Federal Reserve, FRED Database

Figure 30: Recession Probability



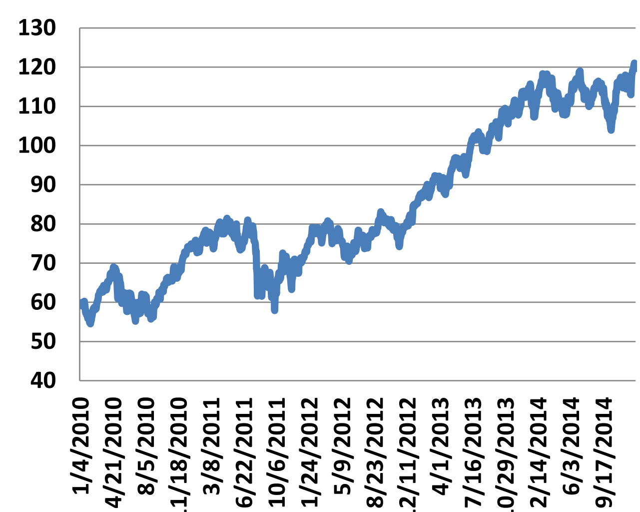
Source: St. Louis Federal Reserve, FRED Database

Figure 31: ISM New Orders



Source: St. Louis Federal Reserve, FRED Database

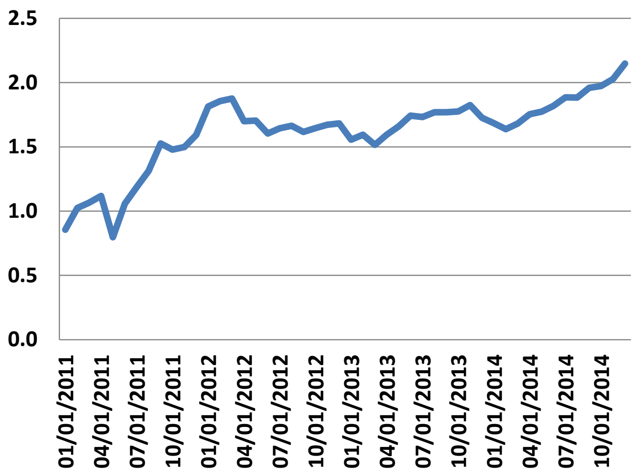
Figure 32: DJ Transports



Source: NYSE Arca

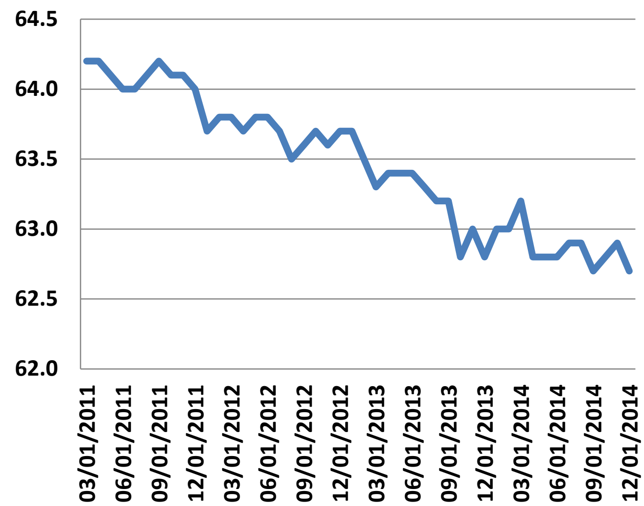
Labor Market Indicators

Figure 33: Payroll Growth (Establishment Survey, % Chg YoY)



Source: St. Louis Federal Reserve, FRED Database

Figure 34: Labor Participation Rate (% of Workforce)

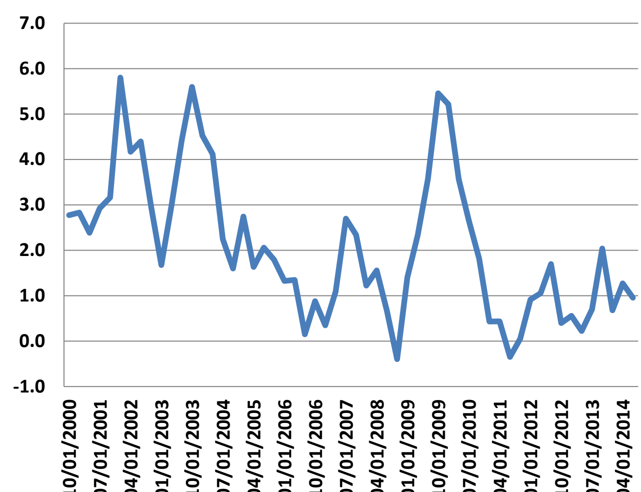


Source: St. Louis Federal Reserve, FRED Database

Figure 35: Initial Unemployment Claims

Source: St. Louis Federal Reserve, FRED Database

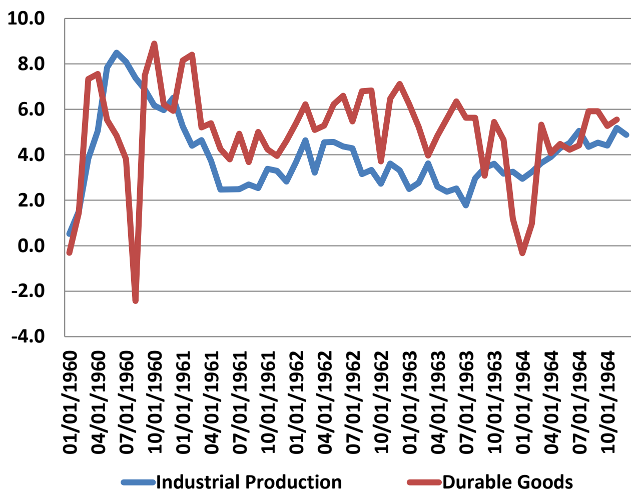
Figure 36: Non-Farm Productivity (% Chg YoY)



Source: St. Louis Federal Reserve, FRED Database

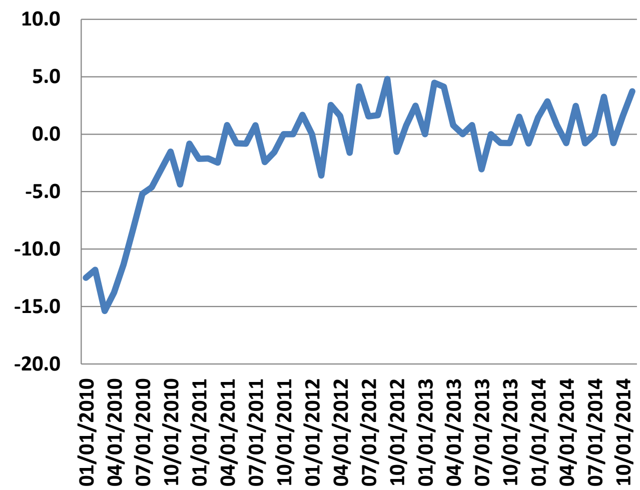
Production and Business Activity Indicators

Figure 37: Industrial Production and Durable Goods (% Chg YoY)



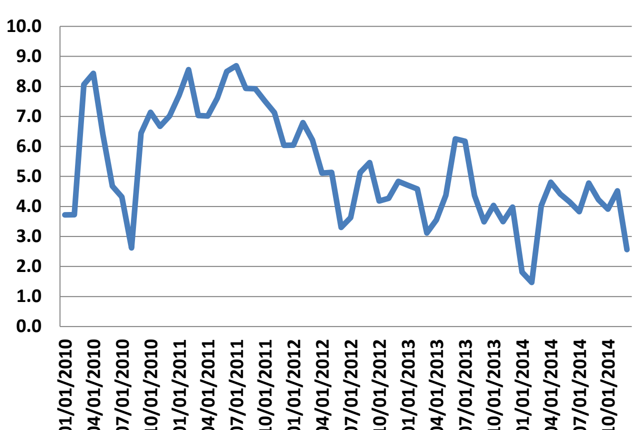
Source: St. Louis Federal Reserve, FRED Database

Figure 38: Inventories to Sales Ratio (% Chg YoY)



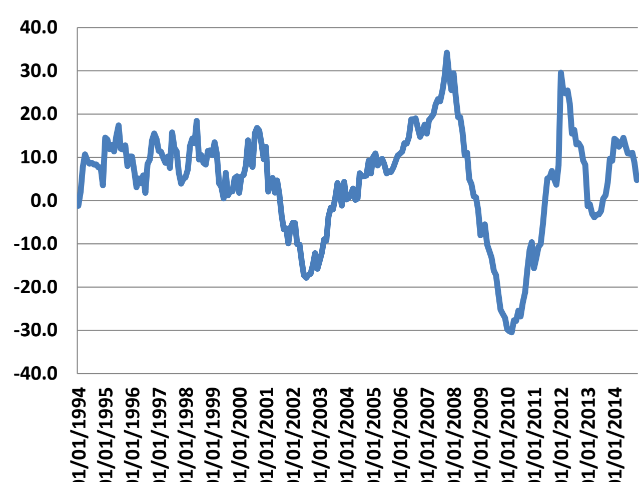
Source: St. Louis Federal Reserve, FRED Database

Figure 39: Retail Sales (% Chg YoY)



Source: St. Louis Federal Reserve, FRED Database

Figure 40: Non-Residential Construction (% Chg YoY)



Source: St. Louis Federal Reserve, FRED Database

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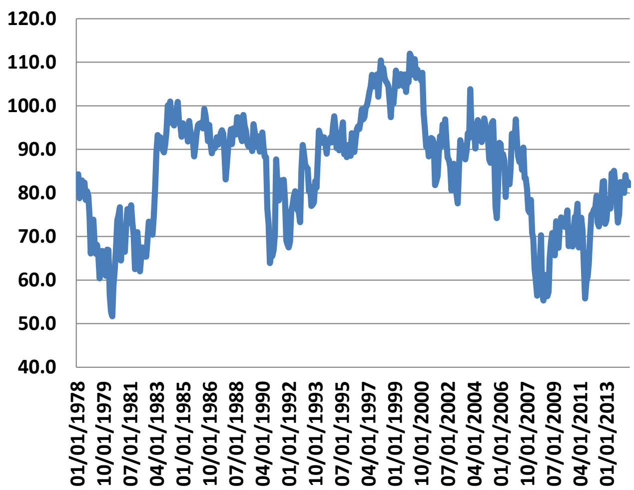
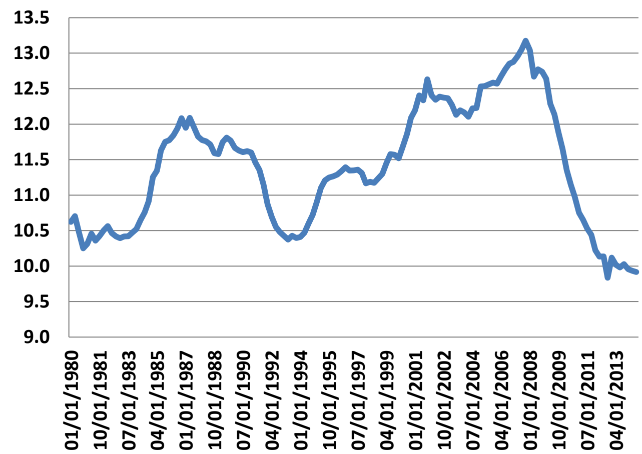
Consumer and Housing Indicators

Figure 39: University of Michigan Consumer Sentiment



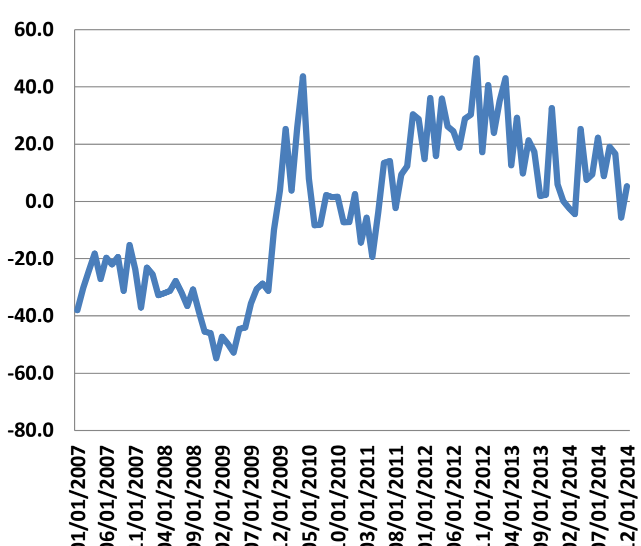
Source: St. Louis Federal Reserve, FRED Database

Figure 40: Household Debt (as % of Disposable Income)



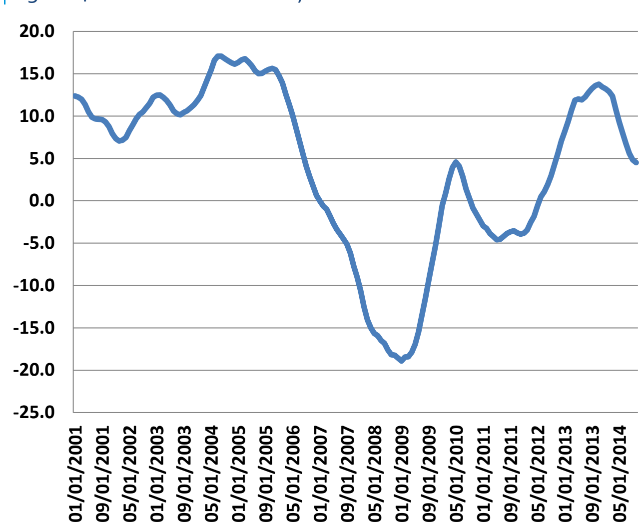
Source: St. Louis Federal Reserve, FRED Database

Figure 41: Housing Starts



Source: St. Louis Federal Reserve, FRED Database

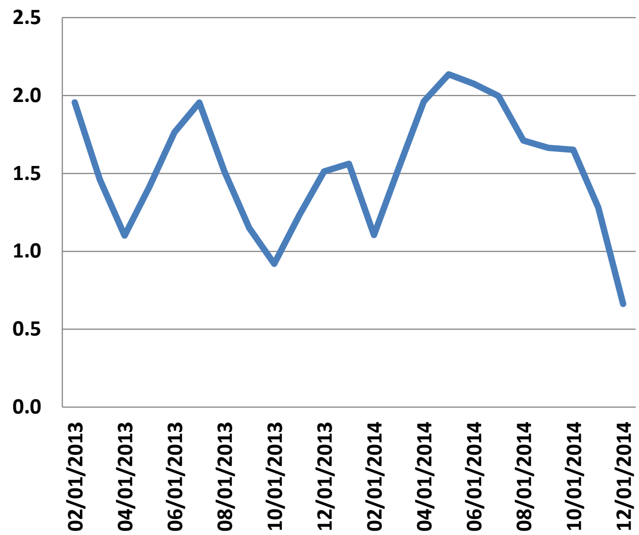
Figure 42: Case-Shiller 20-City Index



Source: St. Louis Federal Reserve, FRED Database

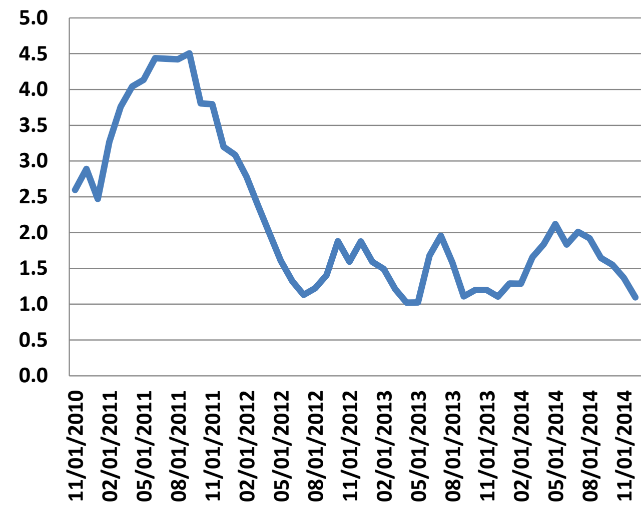
Price Indicators

Figure 43: Consumer Price Index



Source: St. Louis Federal Reserve, FRED Database

Figure 44: Producer Price Index

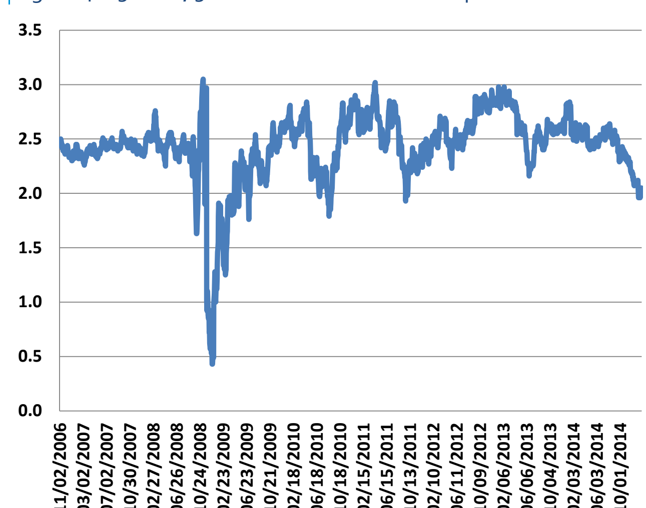


Source: St. Louis Federal Reserve, FRED Database

Figure 45: Employment Cost Index

Source: St. Louis Federal Reserve, FRED Database

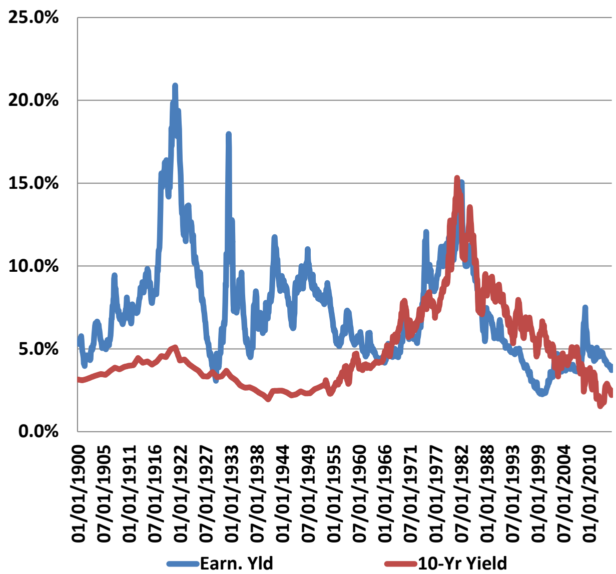
Figure 46: 5-Year, 5-Year Forward Inflation Expectations



Source: St. Louis Federal Reserve, FRED Database

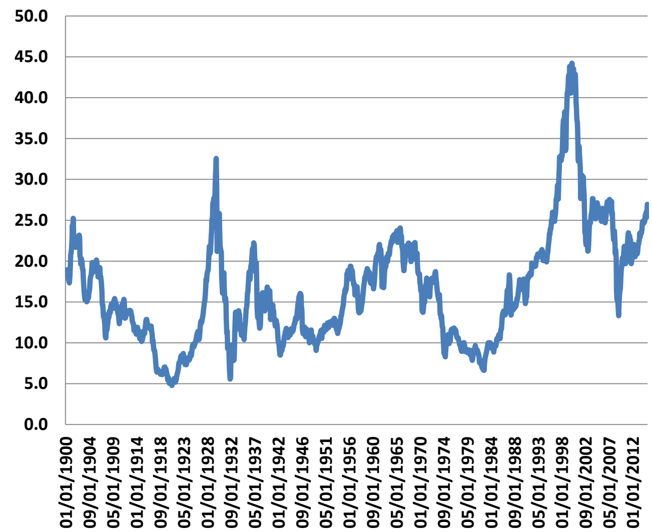
Valuation and Volatility Indicators

Figure 47: 10-year U.S. Treasury vs. S&P 500 Earnings Yield



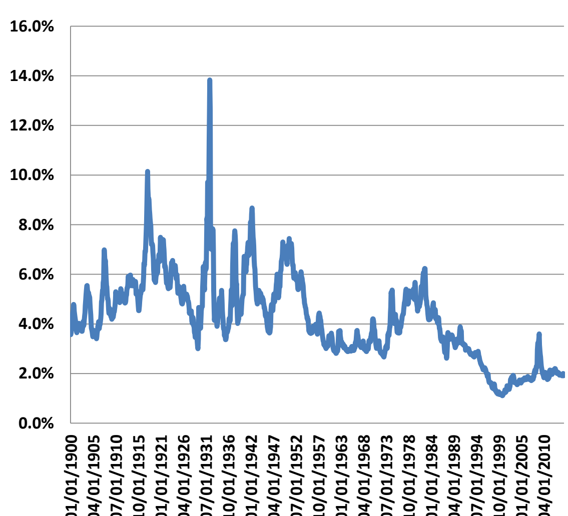
Source: Robert Shiller, Yale University, Rockingstone Advisors, Standard & Poor's

Figure 48: Shiller/CaPE



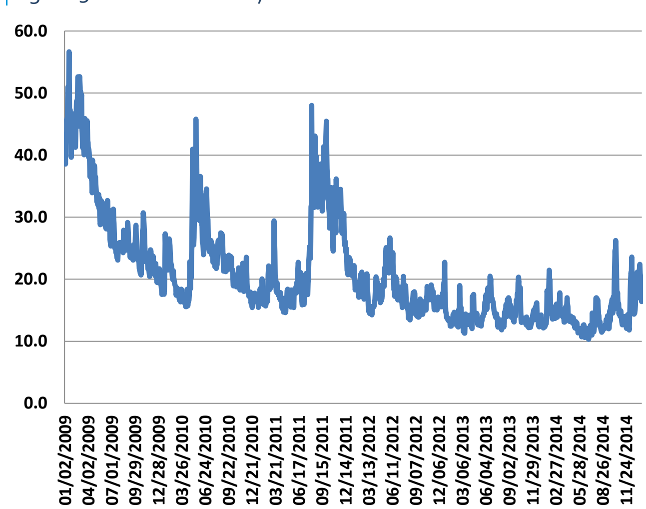
Source: Robert Shiller, Yale University, Rockingstone Advisors, Standard & Poor's

Figure 49: S&P 500 Dividend Yield



Source: St. Louis Federal Reserve, FRED Database

Figure 50: CBOE Volatility Index



Source: St. Louis Federal Reserve, FRED Database

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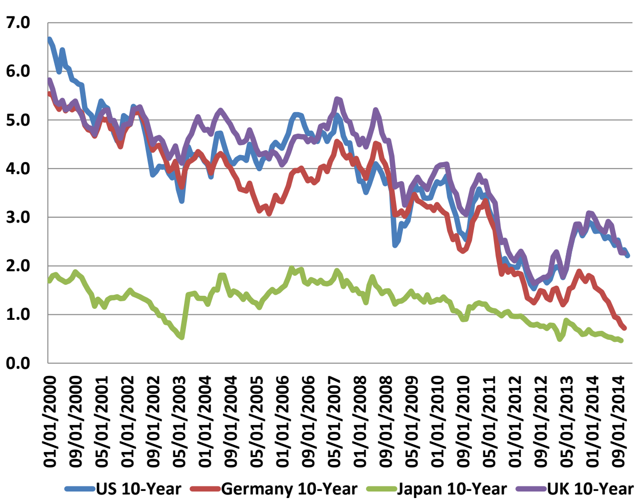
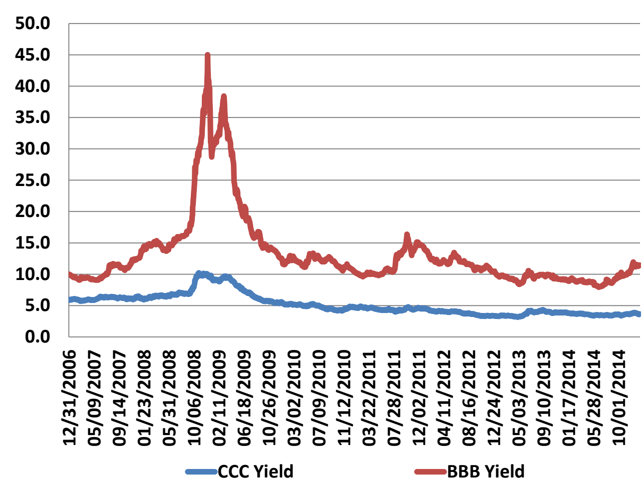
Bond Market Indicators

Figure 51: 10-Year Global Bond Yields



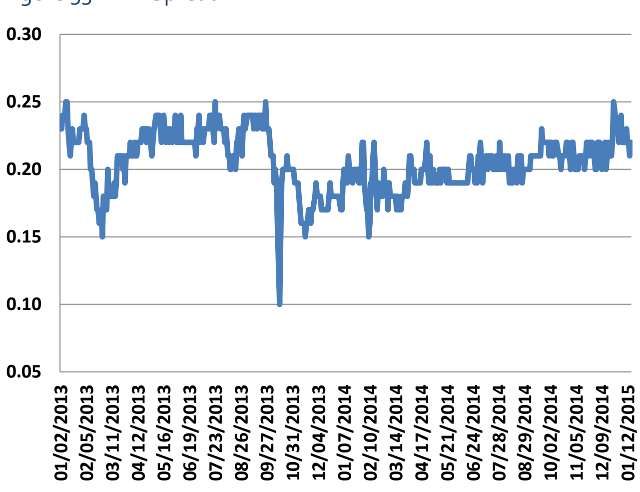
Source: St. Louis Federal Reserve, FRED Database

Figure 52: BBB and CCC Effective Yields



Source: St. Louis Federal Reserve, FRED Database

Figure 53: TED Spread



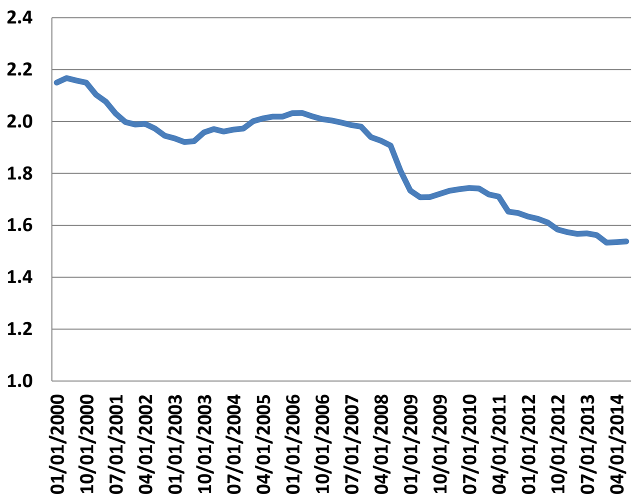
Source: St. Louis Federal Reserve, FRED Database

Figure 54: 10-Year Minus 2-Year Treasury

Source: St. Louis Federal Reserve, FRED Database

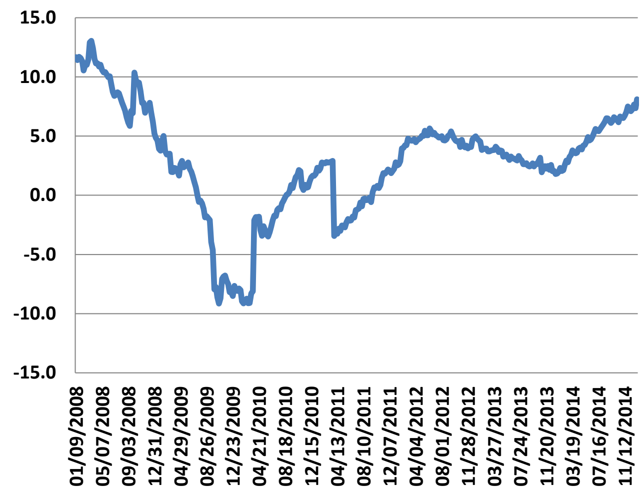
Liquidity Indicators

Figure 55: Velocity of M2 Money Stock



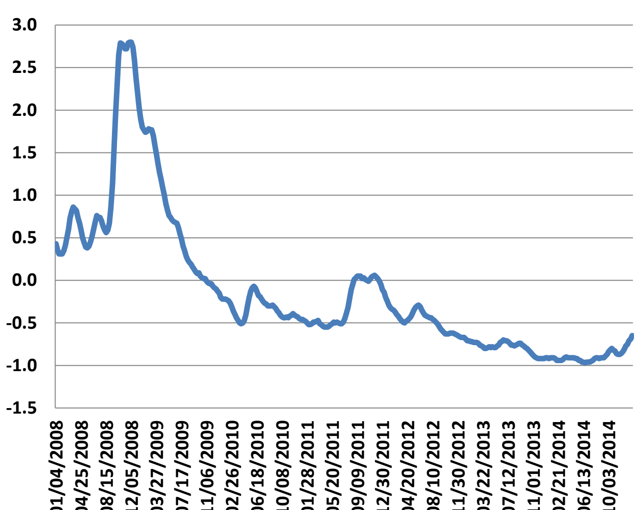
Source: St. Louis Federal Reserve, FRED Database

Figure 56: Loan Growth



Source: St. Louis Federal Reserve, FRED Database

Figure 57: Chicago Fed Financial Conditions



Source: St. Louis Federal Reserve, FRED Database

Figure 58: Financial Stress Index

Source: St. Louis Federal Reserve, FRED Database

Appendix

Important Regulatory Disclosures and End Notes

Form ADV available upon request.

This quarterly is only for informational purposes and not a solicitation to buy or sell securities or as a source of specific investment, legal or tax recommendations.

Rockingstone Advisors is solely responsible for the content of this Quarterly. The information and statistical data contained herein have been obtained from sources we believe are reliable but cannot guarantee.

Rockingstone Advisors performance charts depict the mean aggregate return of all accounts invested with a similar objective and risk tolerance during the entire return period; individual account performance may materially differ according to strategy and portfolio composition. Returns are calculated using time-weighted method (TWM) and are weighted by portfolio assets. Returns can be influenced not only by the actual performance of the underlying portfolios, but by the mix of portfolios in any given year. Public equity returns are calculated by Morningstar based on information received from our custodian(s). Other investment returns, including private equity and real estate investments are calculated based on valuation data from parties other than Rockingstone Advisors. Fixed income returns generated by private notes are recognized when the cash coupon is paid, rather than on an accrued interest basis. Annualized return is based on portfolios invested as of June 1, 2009. The sample set of portfolios within each annual cohort has increased over time. Our investment returns may reflect investment opportunities that are unavailable to all of our clients, for reasons including: (i) certain funds in which we have invested are now closed to new investors, (ii) certain clients may not meet "accredited investor" standards, (iii) certain investments are available only to officers or directors of a business, and /or (iv) we may believe that historical returns most likely will not be generated by a specific security or strategy and thus are no longer allocating new capital to a specific security or strategy. Past performance is not indicative or a predictor of future performance. Mean reversion is a powerful force, meaning periods of outperformance are typically followed by periods of underperformance. All figures are net of fees and expenses. Rockingstone's performance must be assessed in light of not just how we performed relative to the benchmarks, but how much risk we assumed in generating portfolio returns.

Quarterly Data prices are as of December 31, 2014; most other prices and yields are as of January 23, 2015.

We are happy to provide the raw data and source links for any of the charts or tables in this Quarterly. We are also happy to provide individual account performance data. We thank you for your interest and always appreciate any feedback.

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914-481-5050
brandt@rockingstoneadvisors.com

ROCKINGSTONE ADVISORS LLC

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[i] Asset class performance charts depict Equity (SPY ETF), Bonds (BND ETF), Commodities (DBC ETF), Preferred (PFF ETF) and Real Estate (VNQ ETF) price change plus dividends and interest during the selected period.

[ii] Rockingstone Advisors performance charts depict the mean aggregate return of all accounts invested with a similar objective and risk tolerance during the entire return period; individual account performance may materially differ according to strategy and portfolio composition. Returns are calculated using time-weighted method (TWM) and are weighted by portfolio assets. Returns can be influenced not only by the actual performance of the underlying portfolios, but by the mix of portfolios in any given year. Public equity returns are calculated by Morningstar based on information received from our custodian(s). Other investment returns, including private equity and real estate investments are calculated based on valuation data from parties other than Rockingstone Advisors. Fixed income returns generated by private notes are recognized when the cash coupon is paid, rather than on an accrued interest basis. Annualized return is based on portfolios invested as of June 1, 2009. The sample set of portfolios within each annual cohort has increased over time. Our investment returns may reflect investment opportunities that are unavailable to all of our clients, for reasons including: (i) certain funds in which we have invested are now closed to new investors, (ii) certain clients may not meet "accredited investor" standards, (iii) certain investments are available only to officers or directors of a business, and /or (iv) we may believe that historical returns most likely will not be generated by a specific security or strategy and thus are no longer allocating new capital to a specific security or strategy. Past performance is not indicative or a predictor of future performance. Mean reversion is a powerful force, meaning periods of outperformance are typically followed by periods of underperformance. All figures are net of fees and expenses. Rockingstone's performance must be assessed in light of not just how we performed relative to the benchmarks, but how much risk we assumed in generating portfolio returns.

[iii] Equity performance charts depict U.S. large-cap (SPY ETF), U.S. mid-cap (VO ETF), U.S. small-cap (IWM ETF), International Developed (VEA ETF), and Emerging Markets (VWO ETF) price change plus dividends and interest during the selected period.

[iv] Fixed income performance charts depict Intermediate Government (IEF ETF), High Yield Corporates (JNK ETF), High Grade Corporates (LQD ETF), and Emerging Markets bonds (EMB ETF) price change plus interest income earned over the selected period.

[v] Commodity performance charts depict Precious Metals (DBP ETF), Base Metals (DBB ETF), Oil (DBO ETF), and Agriculture (DBA ETF) price change.

[vi] Our Five-Year Forecast is updated quarterly and reflects our best judgment on future performance based on current valuations relative to historical valuations, as well as our outlook for earnings and macroeconomic conditions. We caution that predicting outcomes is inherently risky and subject to change.