GreensKeeper ASSET MANAGEMENT
a division of LIGHTWATER PARTNERS LTD

The Scorecard

Issue #4 – July 2012

PIIGS and Merde

The Value Fund is up 1.7% year-to-date and 1.1% since inception (after all fees and expenses). To date the Value Fund is ahead of the S&P/TSX total return index but lags the S&P500($CAD) – our two primary benchmarks. More importantly, I am excited by what we currently own and believe that our portfolio of stocks are worth significantly more than what Mr. Market is currently valuing them at. Despite the tough economic climate, these businesses should thrive in the coming years and grow their earnings accordingly. Time will tell. In the meantime I am continuing to reduce our cash balance as I acquire additional stocks that meet my unwavering criteria.

As mentioned previously, I have decided to start disclosing the holdings of the Value Fund in order to provide investors with greater transparency. A full list of the Value Fund's current holdings is provided on page 3. Additional details on the positions (cost basis, position size, etc.) will be provided to clients directly when they receive our June 30 financial statements.

"Investing should be dull. It shouldn't be exciting. Investing should be more like watching paint dry or grass grow."

Paul Samuelson

Nobel Prize-winning Economist

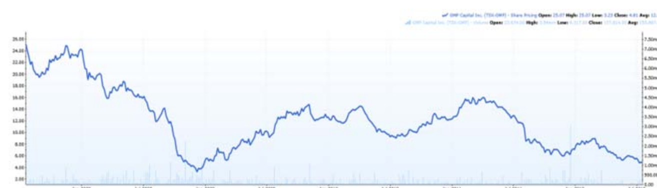
GMP Capital Inc. (TSX:GMP)

One of the keys to being successful at investing over the long term is to stick to businesses and industries within your *circle of competence*. Put another way, you should invest only in businesses that you know and understand. During my investment banking days at Cormark Securities, our primary competitors were the Canadian bank-owned dealers and then GMP Capital Inc. (GMP). They were, and still are, a formidable competitor.

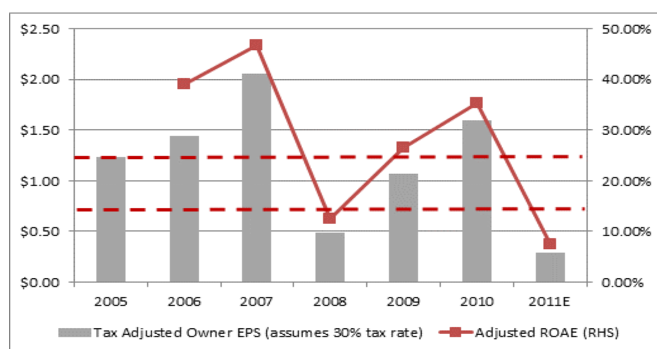
GMP at its core is an institutional investment bank - it acts as agent/underwriter on equity financings and provides advisory services on merger and acquisition (M&A) transactions for Canadian companies. It also facilitates trades for its institutional clients by matching buyers and sellers for blocks of securities. Most of the firm's revenues come from two very cyclical sectors: Energy (Oil & Gas) and Mining. This is a regulated business that is difficult to get right but once you do, it is a license to make money. The business generates a lot of free cash flow and requires very little capital (desks, computers, office space) other than working capital to facilitate its trading and underwriting activities. The real assets of the business are its talented employees.

As illustrated in the charts at right, GMP is a cyclical business with the ability to earn returns on equity of 15-25% and easily earn over $1.00 in earnings per share in good markets.[1]

GMP's business franchise reminds me of a Canadian version of Goldman Sachs *prior* to its initial public offering (IPO) in 1999. Post-IPO, Goldman has become much more reliant on its proprietary trading business which requires significant leverage and is a much riskier (and hence less valuable) business.



Source: S&P CapitalIQ.



Source: Company Reports, GreensKeeper Estimates.

[1] Historical earnings have been adjusted to take into account a number of one-time items and to adjust for GMP's conversion from an income trust to a corporation in 2009.

"Our sustained heavy overweight in quality stocks in 2009 was painful, intellectually and otherwise. Our pain in 2010 was more "business as usual," waiting for the virtues of value to be revealed. The saving grace is that, although value is a weak force in any single year, it becomes a monster over several years. Like gravity, it slowly wears down the opposition,"

Jeremy Grantham,
GMO LLC Quarterly Letter Q1 2011

Going public provides investment banks with a permanent form of capital and access to more if needed. But the downside is that management is tempted to take greater risks once they have access to capital other than their own. I don't believe that Goldman Sachs would have taken the risks that they did in 2008 (leverage of 23 to 1) had the firm been capitalized like they were historically with just the partners' capital on the line.(2) Despite the fact that both are public companies, GMP is a very different business than the Goldman Sachs of today. GMP has largely stuck to its knitting after its IPO and the employees and directors of the firm still own about 25% of the business. They have done a lot of things right and have had a few hiccups along the way.

The Good

One of the keys to success in the investment banking business is the quality of the players on the team. It is hard to retain talent over time as competitors try to poach them or they become wealthy enough to pursue other activities. GMP has dealt with the retirement of a number of its early partners and has successfully managed to attract new talent to the firm and to keep them financially motivated.

GMP has also been successful in starting an asset management division from scratch in 2008. The asset management business is a natural extension of their core franchise and requires very little regulatory capital. It is a good business and GMP has capitalized on this opportunity. The division is currently profitable and already has assets under management of $582 million which should continue to grow.

GMP has also extended its core franchise to new geographies, namely the U.S., the U.K. and Australia. Expanding its core business to places where it can leverage its expertise in commodities is a smart and relatively low risk strategy. In early 2011 the firm also raised $115 million of permanent capital via a preferred share issue on what I believe are attractive terms. It should allow them to avoid having to do another dilutive equity issue like the one they did in the depths of the market collapse in 2008. I give them full marks for both of theses initiatives.

The Not So Good

Management teams of great businesses that generate a lot of free cash flow are often tempted to use it to expand their business empire. It is simply human nature. Unfortunately this often this leads to *unforced errors* when management takes the cash generated by the great business and invests it in a less attractive one. It is somewhat ironic that a firm whose primary function is to allocate capital efficiently has been less than stellar when it comes to its own capital allocation. A few examples will demonstrate.

In 2005 GMP decided to start up a wealth management division with financial advisors who would provide advice to retail clients in exchange for advisory fees. In my opinion, the wealth management business is a mediocre one at best. The business requires large scale to operate at a profit and even at scale, the investment advisors often consume most of the business' economics leaving little for the shareholders. In addition, the business brings with it huge regulatory and compliance risks. Unfortunately, to date this division has lived up to my expectations: growth in assets under administration but few profits for the shareholders. It consumes management time and capital that I believe is better used elsewhere.

In 2006 GMP purchased a private equity business (Edgestone) for approximately $152 million. Over the ensuing years, the business was essentially written off *entirely*. This is a significant amount of money for a company that is currently valued by the market at about $340 million.

(2) For an excellent book on the history of Goldman Sachs as a private partnership, I recommend "The Partnership: The Making of Goldman Sachs" by Charles D. Ellis.

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"Of one thing be certain: if a CEO is enthused about a particularly foolish acquisition, both his internal staff and his outside advisors will come up with whatever projections are needed to justify his stance. Only in fairy tales are emperors told that they are naked."

Warren Buffett

Value Fund – Current Holdings

BERKSHIRE HATHAWAY

Cash (US$)

Cash (CAD$)

GMP recently acquired a New York investment brokerage that focuses on institutional sales and secondary trading of high yield and distressed debt. It is a natural extension of GMP's institutional equity franchise. However, the debt capital markets business operates on much thinner margins and I believe is a less attractive business than GMP's core equity-focused franchise. More troubling, GMP paid $48 million (plus a possible future earn-out) for a business with a book value of about $2.1 million that was modestly profitable in 2011 and is unlikely to earn much profit this year.

Finally, GMP's dividend history has been all over the map. The company has increased its dividend, decreased it and paid several special dividends over the past five years. Having been in this business, I know that it is a cyclical one. The key is to keep your costs in check (including employee count and compensation) when things are slow, maintain a fortress-like balance sheet and distribute capital to shareholders in an efficient manner if and when it is available. The idea of a steady common share dividend isn't consistent with the cyclical nature of the business. I applaud GMP's management and board for distributing the excess capital to shareholders. I would just encourage them to do so via special dividends when excess capital is in hand. This strategy has the added benefit of reducing the pressure of earning enough to cover a fixed quarterly amount.

Investment Thesis

In short, I have to give GMP poor marks for its historical capital allocation decisions. My preference would be for the firm to stick to their core institutional equity investment banking franchise and grow their asset management business. That's it. I believe that these two divisions account for 95% of GMP's entire business value. Any excess cash should be returned to shareholders via special dividends and/or share repurchases if and when the shares are significantly undervalued (like now).

Being significant shareholders in the company as well, I suspect that there are many GMP employees that would agree with my conclusions. In this regard, our interests are completely aligned. I am hopeful that management and the board have reflected on the past and will make future capital allocation decisions that will maximize value for all shareholders.

Despite the risks, I believe that the stock is attractive at current levels ($4.90) and I own a position in the Value Fund. The business should continue to generate significant free cash flow and the book value per share of $3.47 (tangible book value - $2.80) should provide some support for the stock. The investment has not been a good one to date as the stock continues to hit new 52-week lows and is trading below my average cost. Obviously I bought too early. However, I am long-term bullish on the Canadian Energy and Mining sectors despite the market's current pessimism. These sectors will turn as they have always done – I just can't tell you exactly when. And when they do, GMP should absolutely mint it as they have done in the past.

Meanwhile, Over in Euroland

Politics makes for strange bedfellows and the political partnership of France and Germany over the past few years has been interesting to watch. Alas the duo better known as "Merkozy" (Merkel and Sarkozy) is no more after the latter lost the French presidential election in May to Francois Hollande. The new celebrity "couple" of Merkel and Hollande has not yet been ceremoniously christened by the European press with a suitable handle. In light of all of Europe's trouble with the PIIGS I think that "Merde" (Merkel and Hollande) seems quite apt. It's catchy n'est-ce pas?

Michael McCloskey
Founder & President

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The GreensKeeper Value Fund

Minimum Initial Investment	$150,000
Eligible for Registered Plans?	Yes (RRSPs, TFSAs, etc.)
Launch Date	November 1, 2011
Type of Fund	Long equity, Long-term capital appreciation
Valuations	Monthly
Redemptions	Monthly on 30 days' notice
Management Fee	1.5% annual - (A series) 1.0% annual - (F series)*
Performance Fee	20% over 3.0% annual hurdle
Loss Carry-forward?	Yes – One year

Service Providers

Investment Manager	GreensKeeper Asset Management (a division of Lightwater Partners Ltd.)
Prime Broker and Custodian	CIBC World Markets
Auditor	KPMG LLP
Fund Administrator	SGGG Fund Services Inc.
Account Administrator	TD Waterhouse Institutional Services

* F series issued generally to purchasers who participate in fee-based programs through eligible registered dealers.

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Corporate Profile

GreensKeeper Asset Management, a division of Lightwater Partners Ltd. is an independent, owner-managed asset management company. We bring a unique offering to the Canadian marketplace based on a value-investing methodology. Our investment approach and our safeguards focus on the safety of our client's capital. We aim to deliver attractive absolute after-tax returns to our investors and invest our own money alongside our clients

GreensKeeper has been over 15 years in the making.   After successful careers as a lawyer at a major Toronto law firm (M&A, Corporate Finance) and an investment banker with Cormark Securities, a leading independent investment bank, Michael McCloskey established GreensKeeper in 2010.

Our Investment Philosophy

At GreensKeeper we practice bottom-up fundamental analysis combined with the value investing methodology taught by our investing heroes: Benjamin Graham, Philip Fisher, Warren Buffett and Charlie Munger. Value investing is all about buying an interest in a quality business for less than its *intrinsic value*. That discount provides us with our *margin of safety* to safeguard our clients' investments.

What We Look For - When selecting investments we scour our universe of stocks that possess the following characteristics:

> Great Businesses*:* We prefer to stick to investments in businesses that we understand, with attractive underlying economics and that possess durable competitive advantages.
>
> Solid Management: We seek investments in companies that are being run by competent and shareholder-friendly management teams.
>
> Margin of Safety: We patiently wait for the stock market to offer us a price that allows us to buy a stock for a sufficient discount to our estimate of its intrinsic value.

Our Best Ideas - The Value Fund will be managed as a concentrated or "conviction" portfolio. The benefits of broad diversification make sense for some but we prefer to make a few large bets on 15-25 situations that we understand well and where we like the risk/reward trade-off.   In other words, *our best ideas*.

Aversion to Leverage - We prefer to avoid the use of leverage.   We believe that doing so provides us with the benefit of never needing to sell when market conditions are difficult.

Eating our Own Cooking - Our founder has a significant percentage of his family's net worth invested alongside our clients.

This is intended for informational purposes and should not be construed as an offering or the solicitation of an offer to purchase an interest in the GreensKeeper Value Fund or any other Lightwater Funds (collectively, the "Funds"). Any such offer or solicitation will be made to qualified investors only by means of a final offering memorandum and only in those jurisdictions where permitted by law. Lightwater Partners Ltd is registered in Ontario, Canada under the categories of Portfolio Manager, Investment Fund Manager, and Exempt Market Dealer. An investment in the GreensKeeper Value Fund is speculative and involves a high degree of risk. Opportunities for withdrawal/redemption and transferability of interests are restricted, so investors may not have access to capital when it is needed. There is no secondary market for the interests and none is expected to develop.

The fees and expenses charged in connection with this investment may be higher than the fees and expenses of other investment alternatives and may offset profits. There is no guarantee that the investment objective will be achieved. Moreover, the past performance of the investment team should not be construed as an indicator of future performance. In addition, the performance of the GreensKeeper Value Fund should not be mistaken for, and should not be construed as an indicator of future performance. The performance figures for the GreensKeeper Value Fund are unaudited, include actual or estimated performance or management fees and are presented for information purposes only.

Certain statements contained in this presentation are based on, *inter alia*, forward looking information that are subject to risks and uncertainties. All statements herein, other than statements of historical fact, are to be considered forward looking. Such forward-looking information and statements are based on current expectations, estimates and projections about global and regional economic conditions as well as industries that are major markets for Lightwater Partners Ltd. There can be no assurance that such statements will prove accurate and, therefore, readers are advised to rely on their own evaluation of such uncertainties. Further, to the best of management's knowledge the information throughout the presentation is current as of the date of the presentation, but management and the agents specifically disclaim any duty to update any forward looking information. The GreensKeeper Value Fund strategy in no way attempts to mirror the S&P/TSX or the S&P500. The S&P/TSX Composite Index and the S&P500 Index are provided for information purposes only as widely followed indices and have different compositions and risk profiles than the GreensKeeper Value Fund.