TOCQUEVILLE
ASSET MANAGEMENT

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"Tocqueville Fund's Robert Kleinschmidt prides himself on being an independent thinker. In his exclusive interview with WEALTHTRACK he does not disappoint. While the rest of Wall Street has been expecting the Federal Reserve to raise interest rates he says they won't, and while most investors run from troubled stocks he finds gems among them. His deep value approach has generally worked. Under his stewardship, the 4-star rated Tocqueville Fund has delivered market and category beating returns."- Consuelo Mack, WEALTHTRACK, on Public Television

Guest

Robert Kleinschmidt
CEO, President, Chief Investment Officer
Tocqueville Asset Management

CONSUELO MACK: This week on WEALTHTRACK, an exclusive interview with a spelunking stock picker who looks for light where others see only darkness. The Tocqueville Fund's deep value, contrarian portfolio manager Robert Kleinschmidt is next on Consuelo Mack WEALTHTRACK. Hello and welcome to this edition of WEALTHTRACK, I'm Consuelo Mack.

After a long hiatus, market volatility appears to be back. The widely followed VIX, or "CBOE Volatility Index" which measures expectations for near-term market volatility has picked up in the last couple of months, which is a problem as far as financial advisors and their clients are concerned. A recent quarterly survey of advisors by Eaton Vance found that volatility is a top concern for them and their clients right now, followed by generating income, capital appreciation and reducing taxes. One source of market volatility is the prospect of a change in Federal Reserve policy from one of extreme ease over the past five years to possible tightening. But is this fear justified?

In a recent report to clients the street's number one economic research team, ISI Group, wrote: *"Fed Tightening is Not Necessarily Bad for the Stock Market."* They gave two examples. One from 1994 to 2000, when the key Fed funds rate more than doubled from 3 percent to 6.5 percent and the S&P 500 increased three fold. However there was some market drama. There were 5 corrections averaging minus 12 percent in the six year period.

The other example was from 2004 to 2007 when the Fed funds rate skyrocketed from 1 percent to 5.25 percent, and the market increased 30 percent. During that period there were 5 market corrections averaging 7 percent. This week's guest is not worried about the Fed tightening at all.

He is a noted contrarian investor who has appeared exclusively on WEALTHTRACK over the years. Robert Kleinschmidt is the President and Chief Investment Officer of Tocqueville Asset Management, a firm with about 12 billion dollars in assets under management for high net worth individuals and institutions around the world, plus several mutual funds. He has been the Portfolio Manager of the four-star rated Tocqueville Fund since 1992. Under his management the deep value, stock focused fund has delivered 8 percent annualized returns over the last fifteen years, far outperforming the market and its category.

I started our conversation by asking him about one of his most contrarian views. That the Fed was not about to raise interest rates any time soon.

ROBERT KLEINSCHMIDT: The Fed really doesn't control the interest rates. The market controls the interest rates. And so the Fed does control one very short-term rate, and that short-term rate does have an impact on the longer-term rates. There's a relationship between that short-term rate and the longer-term rates, but that relationship is fluid, and it can be different at different times, and you can even have a negatively inverted yield curve, so it's not really clear what the Feds' real role in interest rates actually is. There is a psychological impact, however, to what the

Fed does, and so it is all together possible that by raising this rate, it may change the psychology of the market, which could cause interest rates to go higher. Now, as a matter of fact, higher interest rates are disastrous for the U.S. federal budget.

CONSUELO MACK: And explain why they are so particularly disastrous at this particular time.

ROBERT KLEINSCHMIDT: Well, okay. So we have $18 trillion worth of debt at the Federal level, on which we're paying interest. And the interest we're paying on that Federal debt is about $250 billion, which is less than 1 ½ percent. So think of it this way, at $18 trillion, each 1 percent increase in the interest rate that the government is paying adds $180 billion to the federal deficit.

CONSUELO MACK: Oof.

ROBERT KLEINSCHMIDT: Now, this is a government which nearly shut itself down twice over $30 billion worth of spending cuts that they couldn't find, so how in the world are they going to deal with another $180 billion, or if it's 2 percent, $360 billion, or if the national debt starts to carry a 4 percent interest rate, you know, you're up to $720, $700. So it's a half a trillion dollar increase in the amount that we would have to pay, so it's really disastrous if these rates begin to go up. Now, there are all kinds of reasons perhaps on the monetary side where you may feel like it makes sense to raise rates, but if I'm Janet Yellen, the very first female Fed Chairman, do I really want to be saddled with a legacy that says that I was the Fed Chairman that raised the rates and caused the eventual bankruptcy of the U.S. government? And that's the size of the problem that we're talking about, because $18 trillion compounds pretty quickly at 1 percent. And since we would simply be adding to the deficit, rather than paying for these increases, next year would be $19 trillion, and the year after that it would be $20 trillion. And so the runaway expenses of interest rates, if they begin to ... is a real fiscal problem. So if I were Janet Yellen, I'd wait, I'd sit and hope that the Federal FISC gets their act together, and somehow they come up with a way of dealing with this, or I'll wait until economic growth becomes so powerful that it can overcome the deficit problem that we have. From a legacy point of view, it's just too powerful an argument to try to do anything else.

CONSUELO MACK: From an investment point of view, what difference does it make if, in fact, the Fed does keep short-term rates 1 percent or so for a very long period of time?

ROBERT KLEINSCHMIDT: Well, so, it continues to favor the equity markets over the bond markets because most bond investors, certainly casual bond investors, are scared to death that they're going to own something, and rates are going to go up, and their bond prices are going to collapse.

CONSUELO MACK: There is no alternative argument – "TINA", as it's been called on Wall Street?

ROBERT KLEINSCHMIDT: Well, I think so. There are companies that you can buy that generate 3 to 4 percent kind of dividend yields, and that's not terribly bad, and usually dividend yields over very long periods of time represent about half of the return that you get from holding stocks in the first place. And they can grow. So there is a way that you can be compensated and generate a yield these days, even in a 0 interest rate environment, but it's not in the fixed income markets.

CONSUELO MACK: One of the other contrarian calls that you have made on WEALTHTRACK, one in 2012 when everyone thought sequestration and the fiscal cliff was going to destroy the stock market, was that you were very bullish. You were bullish again in 2013. We have had substantial rallies since then in the stock market. As a value investor, what is your view of values in the stock market now?

ROBERT KLEINSCHMIDT: They're not as good. They're not as good.

CONSUELO MACK: Right. Are they bad?

ROBERT KLEINSCHMIDT: No. I mean, well, we're going to talk about stocks in a little bit...

CONSUELO MACK: We will.

ROBERT KLEINSCHMIDT: And I think you can find things that are still reasonably priced, and that you feel comfortable holding for the longer term, and you shouldn't be an investor unless you're looking at the longer term anyway. But the kind of returns that we've had since the bottom in 2009, you know, I think are not likely. And you shouldn't plan on that as an investor. And by the way, you also shouldn't plan on it if you're running a pension plan, you know, and are assuming that you're going to get 9 or 10 percent returns over the next five years, because I don't think that's in the cards.

CONSUELO MACK: Therefore, expectations would be if you're running a pension plan ... ?

ROBERT KLEINSCHMIDT: You know, I think 5, 6 percent is the number, I should think.

CONSUELO MACK: Total return?

ROBERT KLEINSCHMIDT: Yeah, I think so. I think that's a reasonable number.

CONSUELO MACK: Ratchet down your expectations.

ROBERT KLEINSCHMIDT: Yeah. And I think if it remains the case, and this is a very large if, but if it remains the case that you have low inflation - 5, 6, 7, 8 percent kinds of returns, they're pretty attractive.

CONSUELO MACK: You are a global investor at Tocqueville, are there any areas where the markets have sold off significantly, or have underperformed significantly that it's a place that you would go and look for individual securities?

ROBERT KLEINSCHMIDT: We do look for individual securities, and so we're sort of driven ...

CONSUELO MACK: Yes, you do. You're stock pickers. Right.

ROBERT KLEINSCHMIDT: We're driven by, you know, the bottom up rather than the top down. And so we rarely make the case that, oh, geez, Japan is attractive, we have to be there. Or China is attractive, we have to be there. Or Brazil is attractive, we have to... It's more the case that we find a company that we think is a good company and is trading at a substantial discount to what we think its intrinsic value is, and then we'll buy it regardless of where it is in the world. That being said, the companies that very often represent the best international plays are traded on the New York Stock Exchange. You don't really have to go far off field to find companies that benefit from emerging market growth, as an example, or benefit from China's growth. So you don't have to travel around the world, necessarily, to find them.

CONSUELO MACK: I will ask you one more theme question, because we actually did talk about a theme a year ago, and that was cheap energy, being a phenomenon that you were very, very interested in. Well, guess what? Energy's gotten a lot cheaper.

ROBERT KLEINSCHMIDT: Well, it just goes to show you that if you make a prediction and stick with it, eventually you'll be right. But, you know, I've been thinking that we were going to have much lower energy prices, much lower oil prices for a long time. And there are lots of reasons for it, but primarily the fracking revolution was the single biggest thing because everybody knows, and everybody has known that there's plenty of oil in the ground, you just couldn't get it out. And under conventional methods, we maybe recovered between 25 and 30 percent, 33 percent of the oil in place, and so you can go back to all these old fields, and you can also go into new fields that you never tried before, and you can produce a lot of oil at a relatively attractive price.

CONSUELO MACK: Great for the country...

ROBERT KLEINSCHMIDT: Great for the country...

CONSUELO MACK: Great for the economy.

ROBERT KLEINSCHMIDT: Great for the country. A few years ago, when I was most worried about some of the increased regulations of the Obama administration, and the increased access, I would say that possibly offsetting all of this was this notion of cheaper energy if it were to come. And now it seems like we're finally here. And, you know, the United States is the largest oil producer in the world and they're not limitless, but there are great possibilities to increase that situation. So that's important from an economic perspective.

CONSUELO MACK: Yes.

ROBERT KLEINSCHMIDT: It's also very important from a geopolitical perspective because, as we've talked about earlier, you know, all of my career the Middle East has dominated the news, and the Middle East ...

CONSUELO MACK: In a negative way. Yes.

ROBERT KLEINSCHMIDT: Yes. Yeah. And the Middle East shouldn't dominate the news. It really shouldn't. It's not that important. With the exception of oil and the exception of Israel, there is nothing that is produced in the Middle East that anybody wants to buy. So, you know, it's simply, it's an underdeveloped area that happens to be sitting on a lot of oil, and it's had a vast geopolitical impact that it probably doesn't deserve to have. It certainly doesn't deserve to have. And by reducing the price of oil, because of this technology, it begins to marginalize these countries in a way that they probably should be marginalized within the entire scope of the global picture. And that has an implication for our defense budget...

CONSUELO MACK: Yes.

ROBERT KLEINSCHMIDT: It has an implication for other people's defense budgets, as well. You know, since 1973, it's been all about the Middle East and all about protecting those sea lanes, and all about protecting that oil, and I am ready for a change. And I think the market is, as well, and I think America is. So I'd be very pleased to see that for reasons that have nothing to do with the stock market and nothing to do with economics. But when it comes to the impact that it has on this economy, I think lower energy prices are much better for the economy than higher ones.

CONSUELO MACK: Oh, absolutely.

ROBERT KLEINSCHMIDT: So, you know, there will be some industries that get hurt. And as a matter of fact, the exploration and production companies, we're going to talk about one, and the oil services companies have gotten hammered during this decline.

CONSUELO MACK: Yes. I was going to ask you, for instance, Schlumberger is one of your holdings.

ROBERT KLEINSCHMIDT: Yeah. Schlumberger is one of my holdings.

CONSUELO MACK: And as a value investor, it's getting more and more discounted.

ROBERT KLEINSCHMIDT: Well, it was cheaper a week ago, but yes. I don't have a lot to say about Schlumberger. It's always expensive relative to the others.

CONSUELO MACK: Because?

ROBERT KLEINSCHMIDT: Because it is a higher technology, higher return, more global company and a better company. It deserves to be more expensive. But, you know, if you're a value investor, you like to buy things on the cheap. But, on a relative basis, it's relatively less at a premium price than usual, but the concept here is that in a lower energy environment, a lower oil environment, technology means more, it doesn't mean less. If you think about it ... Well, from the beginning of the industrial revolution, technology replaced high cost labor with lower cost technology, but over the last 30 years or so what technology has been all about is lowering costs, lowering costs. And the costs are lower, and the technology companies have to deal with lower prices every year, and technology companies have been able to deal with lower prices every year. So that should apply in the energy area, too. And I think that Schlumberger, which has a huge lead in many different areas of technology in this group, is in an ideal position to help out oil producers, now that they really need it. Because how much do you need it when oil prices that are $150 a barrel? You know, you don't have to apply a lot of technology...

CONSUELO MACK: No.

ROBERT KLEINSCHMIDT: Because the margins are so high.

CONSUELO MACK: But at 80...

ROBERT KLEINSCHMIDT: But at 80, or 60 to 80, where we may be for the next five, six years or so, you know, it becomes more important. So I think Schlumberger is very well suited in that situation, and it is also true that they have, by far, the biggest global reach, and countries like Ecuador, and Colombia, and Argentina, and you name it, are going to need help developing their reserves all the more so because they're going to be getting less per barrel for them. So I think Schlumberger is in an ideal position to capitalize on that, too.

CONSUELO MACK: At what price do you go in? What's your metric that you look at with a Schlumberger?

ROBERT KLEINSCHMIDT: You know, look, lower is always better, right? Lower is always better.

CONSUELO MACK: It's not better when you're owning it.

ROBERT KLEINSCHMIDT: No, no. So it's traded up to the high $90s. I think as an entry price, if you can buy the stock at around $90, which gives you 15 times current year multiple. That is enough of a relative discount so that you can feel comfortable.

CONSUELO MACK: Do you acquire it as it's declining in price? How do you operate at Tocqueville?

ROBERT KLEINSCHMIDT: The way I operate as a portfolio manager...

CONSUELO MACK: Yes.

ROBERT KLEINSCHMIDT: Is that I never take a full position on the first bite. You know, in rare cases, I kick myself for that because, you know, I'm lucky enough to pick the bottom. But for most times, I will get another chance, and I'll get it at a lower price. As you know, I've been a bear on energy prices, and I really do think that the number is likely to be in the $60 to $80 range over the next several years. But a number of exploration and production companies, particularly some of the smaller ones, I think they're the single worst performers in the market this year.

CONSUELO MACK: Yes.

ROBERT KLEINSCHMIDT: I think there are a number of them that have over discounted this lower price. And one in particular is Bill Barrett, which is a $14 stock down from about $25, actually down from $28 earlier this year. And this is a company that's cleaned itself up. It had far too many projects, it sold off most of them, and it's concentrating on just two plays now. They've hedged their production through next year, so you're not going to pay for that, but what that does for them is it gives them the cash flow that they need to develop the two fields that they're focusing on. They're looking at higher production, we think at least for the next ten years, which is a pretty long period of time for an oil company to be able to make that kind of claim, and our guess is that the valuation, even at $70 oil, if the company is maybe $21, $22 a share, if oil prices get up to $80, we think it's closer to $28, and that's before they've really developed some of these prospects that they have in two shale plays in the west.

CONSUELO MACK: Other contrarian ideas, that you and I talked when I did a pre-interview with them, and one of them is Amazon.

ROBERT KLEINSCHMIDT: Right.

CONSUELO MACK: Which has just been slaughtered.

ROBERT KLEINSCHMIDT: Doesn't sound like, you know, like a Tocqueville stock initially, does it?

CONSUELO MACK: It doesn't. Amazon, a value stock?

ROBERT KLEINSCHMIDT: So Amazon is, you know, losing money. But the point is it's losing money for the right reasons.

CONSUELO MACK: Oh, that's nice to hear.

ROBERT KLEINSCHMIDT: Yeah, it is. I don't mind companies that are losing money for the right reasons. So why are they losing money? They're losing money because they're investing in many new avenues, and many new products, some of which won't work, and some of which will work. But they have some very strong businesses. They have 25 percent share of all of e-commerce, they sell about a quarter of the amount that Wal-Mart sells. The e-commerce is growing at 15 percent a year, and they're capturing a larger and larger market share, and I think this is a demographic thing. You and I might not shop a lot online, but my kids don't ever shop in a store.

CONSUELO MACK: Exactly.

ROBERT KLEINSCHMIDT: So I think that e-commerce number is going to continue to grow, and what Amazon is trying to do is to capture as much of what's going on in the web as they can. And they're willing to invest money to do that. Now, this could be simply in a function of antiquated accounting, right? So the accounting grew up in a manufacturing world, and what they allowed you to do, if you were a manufacturer... and I was an accountant... is that if you built a plant, or bought a machine, or something like that, you capitalized it.

CONSUELO MACK: Yes.

ROBERT KLEINSCHMIDT: But in a service world, investing in new services, or new e-services means hiring people, and hiring software engineers, but it's still an investment, although accounting makes you expense it. Right?

CONSUELO MACK: Mm-hm.

ROBERT KLEINSCHMIDT: Because it's not a plant, and it's not a piece of equipment, it's not land, it's not the kind of thing you would do when you're making an investment as a manufacturer. So I sort of think that looking at earnings conventionally described by accounting is sort of wrong for Amazon to begin with. Maybe you should look at relationship to revenues where it trades at about one times sales growth, sales, which is at an all-time low. By the way, the other reason that Amazon is so interesting to me is that the sentiment has never been lower.

CONSUELO MACK: Worse.

ROBERT KLEINSCHMIDT: The more sells, and more holds, which we all know, is just a sell, but the analyst doesn't have the courage to say it. But only 20 percent of the analysts that are following this company, 19, as a matter of fact, have buys on the company. And that's at an all-time low. So the consensus view is negative. There are losses, but the losses aren't, in my judgment, bad losses. On a sales basis, sales to market cap basis, it's as cheap as it's ever been, and who knows? Some of these things might work out. They've reinvented themselves in the past, and I think that's what they're trying to do again. They're reinventing themselves so they can get their tentacles into more aspects of the e-commerce business. So those are all good reasons to own a stock, in my view, and we think if you do the numbers and apply a margin to it that they have achieved in the past, that you could see a $600 stock in a few years.

CONSUELO MACK: Final question. One investment for long-term diversified portfolio. We ask every guest, what should we own some of?

ROBERT KLEINSCHMIDT: All right, so I thought a lot about this, and I'm going to give you two things, only one of which is an investment. So, first, let me give you the one that's not an investment. I think you should own some gold bullion. But I don't look at gold bullion as an investment. I look at gold bullion as a way to preserve your purchasing power over a long-term period of time. And I don't think you should look at it as an investment, either. You shouldn't buy gold with the idea of selling it later at a higher price because all you're doing is trading it for pieces of paper. If you want to own gold, it's because you don't have faith in pieces of paper. So you should decide how much of your portfolio, or how much of your wealth do you want to have in liquid form, and how much do you just want to sock away where the purchasing power 50 years from now, or 30 years from now, or some long-term period from now will be preserved?

CONSUELO MACK: And your answer to that question for you...

ROBERT KLEINSCHMIDT: Gold.

CONSUELO MACK: For you is how much of your portfolio do you want to have, Robert Kleinschmidt, in gold?

ROBERT KLEINSCHMIDT: I do think it is a function of how much wealth you have, and I think the less wealth you have, the less... But for me it's about 10 percent. And my feeling is that if the world goes to hell in a hand basket, and everything else I own becomes worthless, this thing that was 10 percent will now be worth a lot more to me in purchasing power. I don't view that as an investment because I don't think you buy it to sell it. I think you buy it to have it, and to pass it along to your progeny. So as an investment, to offset that, a very speculative investment is a biotechnology company called Omeros. We own it. It is a pipeline company, it has only one product that's been approved. It has not yet been marketed. But the product that has been approved, it's a pretty exciting product, we think can generate, based on the addressable market, maybe a $30 value for this stock. There's a pipeline of products that address diseases that are sort of orphan-type diseases, that if any one of these pipeline products, which are very early stage, and you can't count on it, can make a $100 stock, a $200 stock. So I would never recommend a stock like that if I didn't feel that there was already a 50 percent discount to what it could be. But the reason that you'd want to put it away for a long-term period of time is if these other things worked out, you could make a lot of money. And if they don't, you still have that gold.

CONSUELO MACK: Perfect. Robert Kleinschmidt from the Tocqueville Fund, thank you so much for joining us.

ROBERT KLEINSCHMIDT: My pleasure. Great to be here.

CONSUELO MACK: Exclusively on WEALTHTRACK...

ROBERT KLEINSCHMIDT: Exclusively here.

CONSUELO MACK: Once again.

ROBERT KLEINSCHMIDT: Nobody else.

CONSUELO MACK: Thank you, Robert.

ROBERT KLEINSCHMIDT: Thanks, my pleasure.

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One-year	*16.18%*
Three-year	*20.89%*
Five-year	*14.00%*
Ten-year	*8.40%%*
Gross Expense Ratio	*1.28%*
Net Expense Ratio	*1.26% **

** The Fund has contractually agreed to "cap" its expense ratio at 1.25% (excluding Acquired Fund Fees and Expenses) until 3/01/15. In the absence of these fee waivers, total returns would be lower.*

Fund holdings are subject to change at any time. As of September 30, 2014, the Fund's top ten holdings were:

Top Ten Holdings	***% of assets***
Microsoft Corp.	3.39
E. I. du Pont de Nemours and Company	2.86
Johnson & Johnson	2.83
General Electric Company	2.72
Schlumberger Limited	2.70
Xerox Corp.	2.64
Exxon Mobil Corp.	2.50
NextEra Energy, Inc.	2.49
Merck & Co., Inc.	2.36
EMC Corp.	2.33

The Fund discloses its top ten holdings on the Tocqueville website no earlier than 15 calendar days after the end of each month. References to other mutual funds should not be interpreted as an offer of those securities.