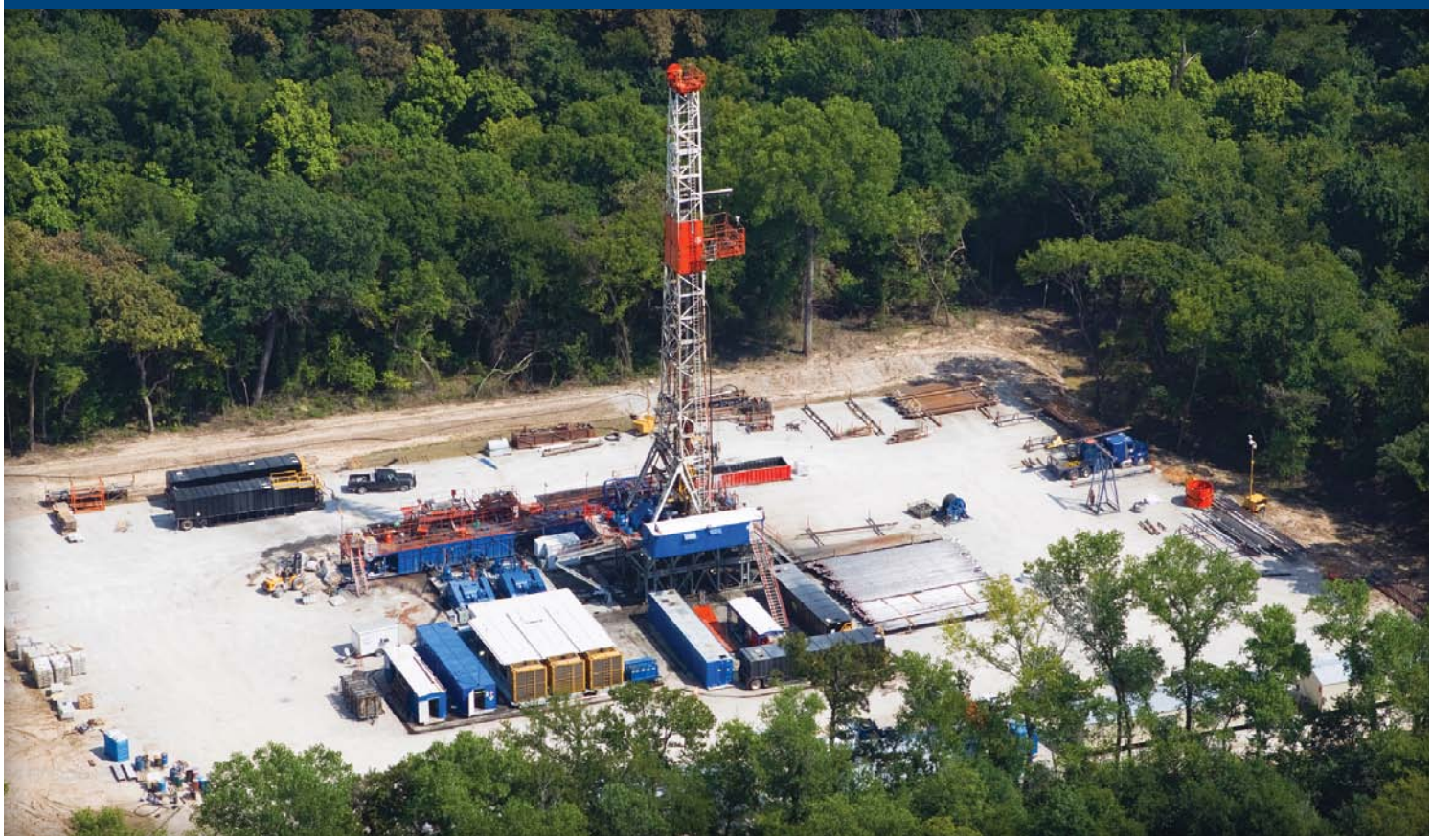
U.S. Global Investors

SPECIAL ENERGY REPORT



An American Energy Renaissance

Due to the disruptive shale technology, U.S. crude oil production reached just over 8 million barrels a day in December 2013. This is the highest number in 25 years, according to the Energy Information Administration. What does this newfound surge in oil and natural gas mean for investors? In this special report on U.S. energy, we take a look at direct shale plays, as well as other companies likely to benefit.

KEY POINTS:

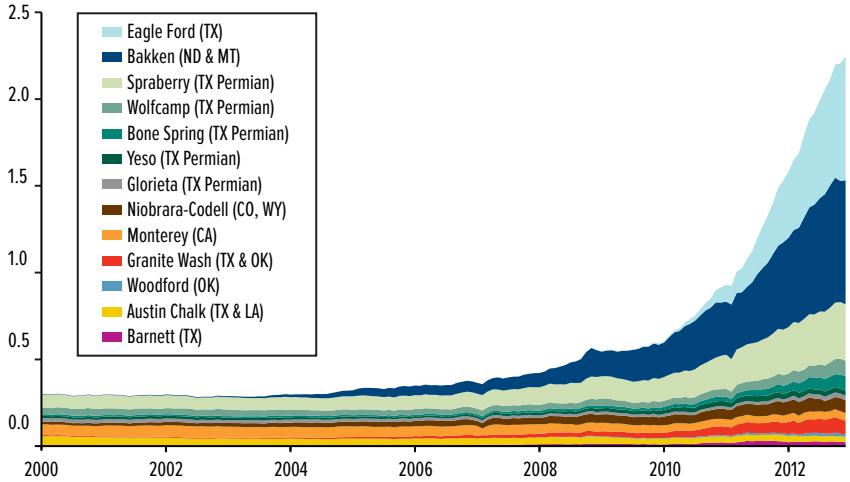
- To benefit from this tremendous growth in oil and gas production, investors should be discriminating.
- Beyond direct shale plays, there are three additional ways to benefit.
- For investors looking for a diversified way to invest in energy and materials, the Global Resources Fund may be an answer.

U.S. Oil and Gas Production On the Rise

Only a few years ago, investors were contemplating the supply constraints facing the petroleum industry, as many major oil fields around the world were facing a decline in production. Now, with the disruptive technology in shale oil and gas taking place in the U.S., we may be looking forward to decades of drilling.

Climbing U.S. Production of Tight Oil

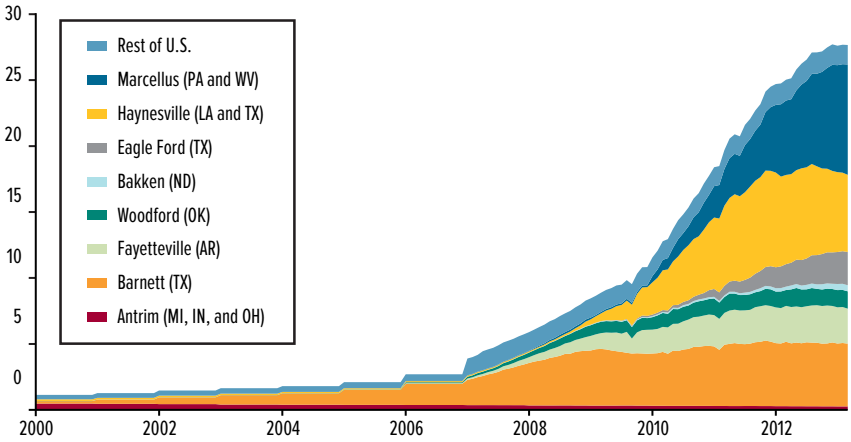
Million Barrels Per Day



Source: Drilling Info, Texas RRC, North Dakota Department of Mineral Resources, EIA, U.S. Global Investors

Dramatic Increase of U.S. Shale Gas Production

Billion Cubic Feet Per Day



Source: EIA, U.S. Global Investors

Note: LCI Energy Insight gross withdrawal estimates as of March 2013 and converted to dry production

Two charts clearly illustrate the incredible growth in oil and gas. While there are many shale areas around the U.S., there are a few notable hot beds of activity. Regarding the domestic production of tight oil, most of the growth has been in the Eagle Ford area that's outside of San Antonio, Texas, the Bakken formation in Montana and North Dakota, and the Permian Basin in West Texas.

At the beginning of 2011, the selected shale areas shown were producing less than 1 million barrels of tight oil per day. Now, production is nearing 2.5 million barrels per day.

Shale gas in the U.S. has also taken off in recent years, with the Marcellus shale in Pennsylvania and West Virginia, Haynesville in Louisiana and Texas, and Barnett in Texas contributing to the majority of the growth, according to the U.S. Energy Information Administration (EIA). Since 2010, natural gas production among the many shale areas jumped from under 10 billion cubic feet per day to about 27 billion cubic feet per day.

Active Management is Critical

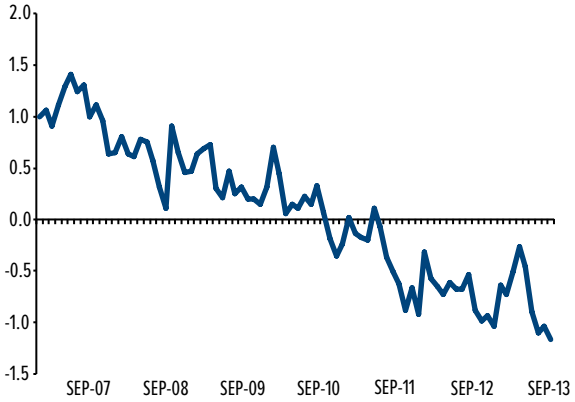
To benefit from this tremendous growth potential, we think investors should be discriminating buyers. We believe great value in today's energy market lies in selectively choosing companies that own high-quality assets in the core basin areas of **Eagle Ford, Permian**, Marcellus and Bakken. What's important to our investment process is owning oil and gas companies that are growing their reserves, production and cash flows on a per share basis.

The new publicly traded **Antero Resources (AR)** is a great example. Antero is an experienced Appalachia producer with an attractive resource base in the Marcellus Shale basin located in West Virginia, Ohio and Pennsylvania. According to research from ISI, the company's acreage in Utica is the "industry's largest" and early leasing in core areas "has created a scalable and 'blocked-up' acreage footprint that would not be possible to replicate today."

U.S. Now Exporting Refined Oil

U.S. Net Imports of Refined Products

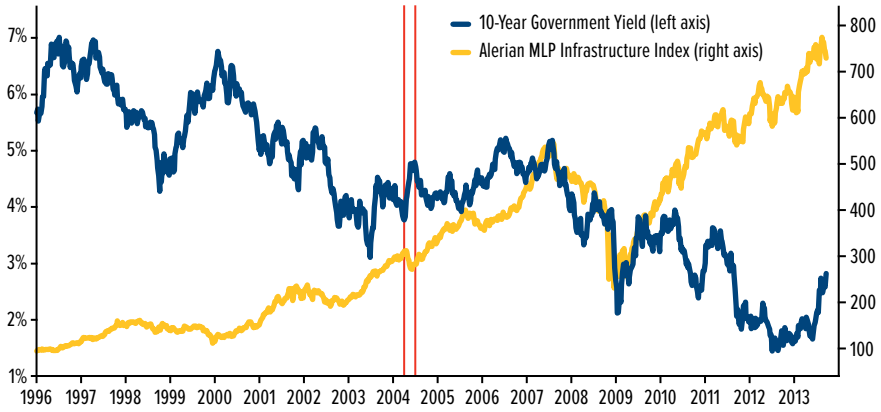
Millions of barrels per day



Source: U.S. Department of Energy, U.S. Global Investors

MLPs Fared Well During Periods of Rising Real Interest Rates

Eighteen-Year Data Shows Only One Period of Decline



Source: Bloomberg Finance L.P and U.S. Global Investors

This company has been impressing its industry peers for years, with its experienced management team that has had "proven success having built and sold three companies prior to AR, with all yielding large financial gains," says ISI.

After the company announced its initial public offering, there was so much demand from eager investors that underwriters increased the amount of available shares and raised the IPO price.

Investors have profited handsomely so far. Following its first day of trading, the stock was "up 18 percent after pricing at $44, above their anticipated range," according to the *Wall Street Journal*.

Another company that looks attractive is **Gulfport Energy Corporation (GPOR),** due to its concentrated acreage in the core part of the Utica Shale in Eastern Ohio and impressive well results, which continue to define this play as one of the best natural gas plays in the U.S.

Look Beyond Direct Shale Plays

To make the most out of the energy renaissance, investors should look beyond these direct shale plays. Here are three ways:

1. Companies that Provide Key Ingredients Needed in Fracking

As highlighted in *The Wall Street Journal,* hydraulic fracturing technology is always improving and becoming more efficient and companies that mine key ingredients used in hydraulic fracturing (sand) will likely benefit. The WSJ finds that companies that mine the ideal sand used to crack rocks and allow the oil and gas to flow out have increased substantially. For example, since going public in August 2012, shares of U.S. Silica have doubled, according to the WSJ.

2. U.S. Oil Refiners

There are also U.S. oil refiners that benefit from increased oil production. Crude oil exports are mostly prohibited, so the oil is refined before being shipped to the rest of the world. As you can see in the chart (above, left), in recent years, the U.S. has moved from importing refined petroleum products prior to 2010 to exporting more than 1 million barrels per day as of September 2013.

3. Master Limited Partnerships

With the rapid development of North American oil and gas shale basins such as the Marcellus in Pennsylvania, the Eagle Ford in Texas and the Bakken in North Dakota, infrastructure constraints are being alleviated with new investment in assets to gather, process and transport growing oil and gas volumes. We believe certain Master Limited Partnerships (MLPs) that have the right type of assets in the right geographic locations will allow investors to reap the benefits of the development of shale plays in the U.S. and Canada.

MLPs will likely be attractive even if interest rates continue to rise. According to our research that covers 18 years, there were five longer rising-rate trends and six short-lived spikes. During these times, there was only one four-month period where MLPs declined.

We believe distribution growth, or the ability of MLPs to make distributions to unit holders, is a key driver to consider when determining an investment in MLPs.

To make the most out of the energy renaissance, investors should look beyond direct shale plays.

www.usfunds.com/energyinUSA

Read more about the American energy revolution.

The Importance of Diversification

Energy is only one part of the diverse natural resources sector. What's important for investors to remember is to build a diversified basket of natural resources companies actively managed by professionals who understand the differing seasonal and cyclical trends of these specialized assets.

An investment that covers all the commodity bases is the Global Resources Fund, which selects commodity stocks among 12 themes, including oil services, exploration and production companies, as well as precious metals stocks. We believe this approach offers investors the possibility for better growth with lower volatility.

A Multi-Faceted Approach—12 Themes

Bulk Commodities

Base & Industrial Metals

Precious Metals

Venture Stage Exploration

Oil/Gas Exploration & Production

Resource Transportation

Oil Services

Energy Infrastructure

Agricultural

Food

Forest & Lumber

Renewable Energy

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U.S. Global Investors

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Foreign and emerging market investing involves special risks such as currency fluctuation and less public disclosure, as well as economic and political risk. Because the Global Resources Fund concentrates its investments in specific industries, the fund may be subject to greater risks and fluctuations than a portfolio representing a broader range of industries.

The Alerian MLP Infrastructure Index, comprised of 25 energy infrastructure Master Limited Partnerships, is a liquid, midstream-focused subset of the Alerian MLP Index (NYSE: AMZ). The index, whose constituents earn the majority of their cash flow from the transportation, storage, and processing of energy commodities, provides investors with an unbiased benchmark for the infrastructure component of this emerging asset class. Holdings in the Global Resources Fund as a percentage of net assets as of 3/31/2014: Antero Resources 0.51%, Gulfport Energy 0.00%, US Silica 0.00%. Diversification does not protect an investor from market risks and does not assure a profit. All opinions expressed and data provided are subject to change without notice. Some of these opinions may not be appropriate to every investor. 14-261