Manager Commentary: On the Gold Market

Gold market finds some strength despite continued soaring dollar

By: Joe Foster, Portfolio Manager

Fund Review

The International Investors Gold Fund's Class A shares returned 4.34% for the one-month period ending November 30, 2014 (excluding sales charge), while the NYSE Arca Gold Miners Net Total Return Index (GDMNTR)[1] returned 5.88% for the same period. The Fund is actively managed and invests mainly in gold-mining equities. Geologist Joe Foster has been part of Van Eck's gold investment team since 1996. The Fund is managed by a specialized investment team that conducts continuous on- and under-the-ground research to assess mining efficiencies and opportunities.

Average Annual Total Returns (%) as of November 30, 2014

	1 Mo^	1 Yr	5 Yr	10 Yr
Class A: NAV (Inception 1/1/56)	4.34	-10.06	-13.68	3.25
Class A: Maximum 5.75% load	-1.61	-15.21	-14.70	2.64
GDMNTR Index	5.88	-15.72	-17.39	-2.86

Average Annual Total Returns (%) as of September 30, 2014

	1 Mo^	1 Yr	5 Yr	10 Yr
Class A: NAV (Inception 1/1/56)	-20.10	-8.66	-7.91	5.61
Class A: Maximum 5.75% load	-24.72	-13.88	-8.99	4.99
GDMNTR Index	-19.78	-13.58	-12.87	-0.99

^Monthly returns are not annualized.

Expenses: Class A: Gross 1.46%; Net 1.45%. Expenses are capped contractually until 05/01/15 at 1.45% for Class A. Caps exclude certain expenses, such as interest.

Please note that precious metals prices may swing sharply in response to cyclical economic conditions, political events or the monetary policies of various countries. Investors should be aware that recent market conditions resulting in high performance for the gold sector may not continue. The tables present past performance which is no guarantee of future results and which may be lower or higher than current performance. Returns reflect applicable fee waivers and/or expense reimbursements. Had the Fund incurred all expenses and fees, investment returns would have been reduced. Investment returns and Fund share values will fluctuate so that investor's shares, when redeemed, may be worth more or less than their original cost. Fund returns assume that dividends and capital gains distributions have been reinvested in the Fund at NAV. Index returns assume that dividends of the Index constituents in the Index have been reinvested.

Market Review

Gold held its own through most of November, even though U.S. dollar strength and gold bullion exchange-traded product (ETP) redemptions continued. Early in the month, gold fell to its yearly lows in the wake of the Republican victories in the U.S. Senatorial elections amid hopes that a newly Republican-controlled Congress and the Administration could deal with tax reform, debt, regulations, and many other issues that generally stifle the economy. Unfortunately, hopes were dashed and it was business as usual in Washington, D.C. when President Obama bypassed Congress to launch immigration reforms unilaterally and the House sued the President over the Affordable Care Act (Obamacare).[2]

The International Monetary Fund (IMF) reported that Ukraine sold 14.3 tonnes of gold in October. This was more than offset by Russian buying; however, Russia likely sourced its gold from domestic production, whereas Ukraine probably sold into international markets. This could help explain gold's weakness in October and possibly early November. Ukraine ended October with 26 tonnes in reserves. The World Gold Council estimates that central banks bought 92.8 tonnes in the third quarter and are on track to purchase roughly 400 tonnes (net of sales) for the year.

Gold bounced off its November 7 low of $1,131 per ounce and was on track to post gains for the month. However, on November 27, the Organization of the Petroleum Exporting Countries (OPEC)[3] surprised the market by announcing no cuts to its oil production ceiling. This caused West Texas Intermediate (WTI) crude prices to fall below $70 per barrel for the first time since 2010. The oil sell-off sparked a contagion across commodities and gold fell $32 on the day to end the month with a $6.07 (0.5%) loss at $1,167.41 per ounce. Since the OPEC decision seems to have had little to do with gold's fundamentals, the metal reversed its losses and gained $45 on December 1 to close at $1,212 per ounce.

We believe the main driver of gold price strength through most of November has been improving physical demand from India and China. Weekly withdrawals from the Shanghai Gold Exchange advanced to higher levels last seen in 2013, while UBS reported net inflows to China of 111 tonnes in October—the highest since February. India had strong imports of 98 tonnes in September and press reports indicated they reached their highest monthly level of the year in October. Strong Indian demand could continue thanks to the surprise November 28 removal of gold import restrictions that were imposed in July 2013 by the Reserve Bank of India. As a result of these restrictions, the World Gold Council reckons that roughly 50 tonnes per quarter have

Please note that the information herein represents the opinion of the portfolio manager and these opinions may change at any time and from time to time.

been smuggled into the country, stating: "It's now beyond debate that import restrictions have had little impact on the demand for gold and yet have strengthened the unauthorized supply channels". In October, Switzerland was a net exporter of gold for the first time this year with most of the outflows going to India and China. In addition, the Gold Forward Offered Rate[4] quoted by the London Bullion Metals Association turned negative in November, which is indicative of tight physical markets.

During October, economic weakness and monetary stimulus in Japan and Europe caused the U.S. dollar to soar and gold to sink. Perhaps that dynamic is shifting. On November 21, both gold and the U.S. dollar reached highs for the month when the Bank of China announced a surprise rate cut and European Central Bank President Draghi said "We will do what we must to raise inflation and inflation expectations as fast as possible".

Gold equities rebounded from oversold levels, reversing some of their October losses. The stocks took a hit with gold on the last day of the month, which trimmed their gains. The NYSE Arca Gold Miners Index advanced 5.9%, while the Market Vectors Junior Gold Miners Index[5] gained 1.9% in November. Like gold, the equities also had a sharp rebound on December 1.

In our last update, we mentioned that a supply response to low prices could entail production cuts or mine closures. We met with a number of gold producers recently. With gold averaging $1,177 per ounce in November, lower gold prices (i.e., sub-$1,200 per ounce) are now a reality and companies are articulating plans to deal with prices in more detail than previous encounters. We now believe that it would take prices closer to $1,000 per ounce before we hear of significant cuts in production. The industry should be able to hold the line on mining costs and some companies believe they can make further cost cuts in 2015. Additional savings are likely from lower fuel prices and lower local prices in weak-currency countries. We also expect more cuts to general and administrative (G&A) expenses, exploration, and dividends, as well as more capital deferrals before companies see the need to cut production. The good news is that companies are becoming leaner and meaner. However, while we don't expect global output to increase in 2015, significant cuts to production are probably off the table at current prices.

Market Outlook

By many accounts, the overwhelming victory of Republican senators and governors in the November U.S. election appeared to be a strong indication that a) many people are not happy with public policies of the recent past, and b) many people want policies out of Washington, D.C. that improve an array of economic and social conditions. Unfortunately, hitting Washington between the eyes with the proverbial two-by-four doesn't work, as so far the relationship between the President and Republicans in Congress has not changed.

A recent segment on the 60 Minutes program focused on the decaying U.S. infrastructure in which roughly 10% of bridges are on the brink of failure. There have been a few headlines of bridge collapses and related deaths, but no moves to address the problem on a national scale. The massive amounts of money and manpower spent in Iraq and Afghanistan in the decade following the airliner bombing of the World Trade Center, in my view, shows what government is capable of when motivated.

Unfortunately, in my opinion, a cataclysmic failure seems to be required to generate the consensus and willpower needed to effect overdue change. Forward planning to mitigate known risks is too often the exception, when it should be the rule.

Similar complacency is apparent in monetary policy. At some point during the former chairman Alan Greenspan era, the Federal Reserve Bank (the "Fed") adopted the persistent strategy of cutting rates and enabling credit to expand to unprecedented proportions in order to improve economic growth. Those policies have been taken to the extreme since the 2008 credit crisis by maintaining short-term interest rates near zero and pumping trillions of dollars of liquidity into the system. We believe the post-crisis recovery has so far shown that these policies have not worked as expected. Despite massive stimulus, this recovery has created the fewest jobs relative to the previous employment peak of any prior recovery, while the labor participation rate is at a 36-year low.[6] There are 10 million fewer full-time workers today than six years ago. Mortgage lending is at its lowest level in 13 years.[7] Productivity growth has been less than half of long-term averages and economic growth has been below post-recession norms. Voters have shown their dissatisfaction.

In Japan, the record is much the same over a longer period. Deficit spending that has raised national debt to 227% of GDP (gross domestic product)[8] has failed to generate sustainable growth since the economy collapsed in 1990. Recently, the Bank of Japan embarked on Fed-style monetary policies, yet Japanese GDP fell at an annual rate of 1.6% in the third quarter, sending the economy into yet another recession.

The Europeans are not having much luck either, as bigger government seems to lead to less growth. Meanwhile, European Central Bank policies have distorted sovereign debt markets such that Spanish 10-year bonds at 1.93% have yields that are 0.33% lower than 10-year U.S. Treasuries.

Central banks alone cannot conjure up jobs and economic growth. In my opinion, the more they try to compensate for inadequate fiscal or overreaching regulatory policies, the more they distort the natural incentives, checks, and balances of the free market. Economic imbalances become excessive, wealth gets misallocated, and asset bubbles form that can disrupt or even cripple the financial system. We now know what a tech stock bubble and a subprime credit bubble look like.[9] History suggests more asset bubbles will form, but this is not a typical cycle and typical recovery. What does a post-credit crisis bubble look like? Last year, art sales in the U.S. were up 25% to $22 billion.[10] Sales at a recent fall art auction in New York set a record at over two billion dollars, while penthouse condos in new Manhattan skyrises approach nine-digit prices. Does the "greater fool theory" apply here? Snapchat, Yik Yak, and WhatsApp are companies with market capitalizations of hundreds of millions to billions of dollars. Do social media apps really create that much value? Are all-time highs in the stock market a function of fundamentals or stimulation from central banks? Has the 33-year bull market in bonds gone too far?

No one knows if these are signs of impending bubbles about to burst, but in my view, fiscal and monetary policy makers cannot keep doing the same things and expect a different outcome. Eventually the cycle will turn and if it happens too soon, central banks may not have the firepower remaining to defend the financial system. Perhaps it will take a cataclysmic failure to generate the will and vision to create a more robust fiscal and monetary system that immunizes the economy from extreme periods of boom and bust. Until such a system is in place, many choose to use gold and gold shares to diversify portfolios and to attempt to help preserve value when tail risk becomes reality.

Any indices listed are unmanaged indices and include the reinvestment of all dividends, but do not reflect the payment of transaction costs, advisory fees or expenses that are associated with an investment in the Fund. An index's performance is not illustrative of the Fund's performance. Indices are not securities in which investments can be made.

[1]NYSE Arca Gold Miners Index (GDMNTR) is a modified market capitalization-weighted index comprised of publicly traded companies involved primarily in the mining for gold. [2]The Affordable Care Act (Obamacare) was enacted in 2010 with the goals of increasing the quality and affordability of health insurance, lowering the uninsured rate by expanding public and private insurance coverage, and reducing the costs of healthcare for individuals and the government. [3]Organization of the Petroleum Exporting Countries (OPEC) is an international organization and economic cartel whose mission is to coordinate the policies of the oil-producing countries. [4]Gold Forward Offered Rate (GOFO) are rates at which contributors are prepared to lend gold on a swap against U.S. dollars; basically the interest rate for borrowing money using gold as collateral. [5]Market Vectors Junior Gold Miners Index (MVGDXJTR) is a rules-based, modified market capitalization-weighted, float-adjusted index comprised of a global universe of publicly traded small- and medium-capitalization companies that generate at least 50% of their revenues from gold and/or silver mining, hold real property that has the potential to produce at least 50% of the company's revenue from gold or silver mining when developed, or primarily invest in gold or silver. [6]The Wall Street Journal, November 19, 2014. [7]The Wall Street Journal, November 25, 2014. [8]Gross Domestic Product (GDP) estimates are commonly used to measure the economic performance of a whole country or region, but can also measure the relative contribution of an industry sector. [9]Tech stock bubble is a pronounced and unsustainable market rise attributed to increased speculation in technology stocks. Subprime credit is a general term for borrowings of subprime debt, or loans made to people with less-than-perfect credit or short credit histories. [10]The Wall Street Journal, November 13, 2014.

vaneck.com | 800.826.2333

Van Eck Securities Corporation, Distributor
335 Madison Avenue | New York, NY 10017