Manager Commentary

Oil Prices Impact Venezuela and the Russian Economy Slides into Stagflation

By: Eric Fine, Portfolio Manager

Executive Summary

- Volatility in oil prices remains critical to Venezuela allocation.
- As has been the case throughout the year, we continue to have zero exposure to Russia.
- Liquid, long-duration, U.S. dollar-denominated government bonds from higher-rated countries look attractive.

Overview

The broad themes that characterize our portfolio remain unchanged, although we continue to monitor the impact of the downward trend of current oil prices on exporting countries, such as Venezuela. We still prefer hard-currency over local-currency debt (a small position in China offshore remains our only exposure in local-currency), have no Russia-/Ukraine-related exposure, and are comfortable with duration. We also continue to limit our corporate debt exposure. We have further increased our selective exposure to duration in steep credit curves of high-rated and most liquid sovereigns, while trimming our corporate exposure below 10%. At the end of the month, long-duration, high-rated sovereigns accounted for approximately 50% of our portfolio, approximately a quarter of our exposure is in idiosyncratic Venezuela and Argentina bonds, and around 6.5% is in offshore China duration.

Given the fact that Venezuela has been such an integral factor this year, we thought we would go into more detail on current views and outlook for the country. We should note that we feel fortunate that there were other sectors within the portfolio (i.e., in general, performance wasn't suffering from anything in particular, like poor local-currency returns or Russia exposure) that allowed us to fully assess the economic forces impacting the country.

At the end of November, there were a number of factors that supported investment in Venezuela, although downward trending oil prices remained a significant influence on our holdings, and one that could prompt an immediate direction change. To our benefit, the Fund's unconstrained investment mandate provides us with the flexibility to react relatively swiftly to developments and trends that may affect our country and currency exposures.

First, there were no big forthcoming sovereign payments by Venezuela (including Petròleos de Venezuela, S.A., or "PDVSA") until October 2015. Second, we believed the current market pricing for Venezuela implied a 70% probability of default within one year. The implied default probability actually increased in the past few weeks, despite the fact that Venezuela had made all prior debt payments and was facing no big upcoming payments for almost a year. Third, Venezuelan bond prices appeared historically low when adjusted for commodity pricing within the Venezuela oil basket. Additionally, long-dated Venezuelan bonds were trading near the recovery value, which we saw in the range of USD$35-$50. This range is lower than previous sovereign emerging markets defaults and accounts for a possible restricting of the debt scenario.

Finally, there were indications that government policy might be improving and becoming a bit more pragmatic. The recent moves worth mentioning include the consolidation of external assets in international reserves, moving more foreign exchange transactions from the artificially low official exchange rate band to a higher (and more market-based) exchange rate band, and another round of talks about possibly increasing gasoline prices. The government's more pragmatic approach was evident in its relations with international oil companies, as new investments are now more closely linked to greater operational control.

In addition to the impact of current oil prices, we are cognizant of risks associated with this position. First, despite a more pragmatic policy stance, in our view, the government has so far failed to push through serious and decisive reforms – such as large-scale foreign exchange liberalization and higher domestic gasoline prices that can significantly improve Venezuela's macroeconomic position (especially the external balance of payments). Second, in our opinion, President Maduro's recent bout of anti-Americanism is another example of a tendency to act irrationally. Recent meetings between Chinese and Venezuelan officials generated vague headlines about "financial cooperation plans" without providing any information about potentially beneficial new credit/swap lines or modifications of existing agreements. Finally, there is much confusion about potential securitization of the Dominican Republic's Petrocaribe debt (estimated at $4B) that could bring Venezuela up to $2B in cash. The total amount of arrears under the Petrocaribe program is estimated to be at least $12B (including payments owed by Jamaica, Honduras and Nicaragua) and any clarity about prospects for its securitization would, in our view, be most welcome.

As has been the case throughout the year, we continued to have zero exposure to Russia. The country's risk/reward profile remains unattractive despite improved valuations. The downside for Russian assets remains significant as the economy slides into stagflation, the probability of corporate defaults increases as long as the Russia-Ukraine conflict remains unresolved, and the international sanctions remaining in place generally stifle growth and restrict capital inflows. We believe the policy reaction of the Central Bank of Russia has been exemplary so far and President Putin's decision to reduce real fiscal spending is, in our view, also orthodox. This leaves some hope that a positive Russia story may eventually emerge, but likely only in a fairly distant future.

We are still of the view that we are in a risk-off deflationary environment and, therefore, favor liquid, long-duration, U.S. dollar-denominated government bonds from higher-rated countries. This sector is attractive because it is self-financing and is currently paying in principal and interest more than it is borrowing. Spreads on emerging markets bonds that we own may widen, but we believe that this will be short-lived, and that they will catch up when stability returns. Most of the countries where we invest are net creditors, meaning they have more U.S. Treasuries (USTs)/U.S. dollars than U.S. dollar debt. They are active debt managers with the flexibility to buy back debt, stop issuing it, etc.

We believe longer duration bonds should eventually stabilize and benefit as USTs rally based on the current U.S. dollar strength and a tightening of monetary conditions. Activity data flow remains uneven (still), while long-term inflation expectations continue to edge down. Even when the Federal Reserve finally starts normalizing its target rate, it is likely to proceed at a cautious pace. If this is the case, the policy tightening could predominantly be absorbed by the short end of the UST curve while the long end of the curve remains highly correlated with German Bund yields, which could be anchored by the forthcoming European Central Bank quantitative easing.

The weak growth outlook in systemically important emerging economies and the predominantly orthodox policy responses by emerging markets central banks (e.g., targeting reserves and allowing currencies to absorb shocks) are behind our intention to stay away from local-currency debt for now. Our minimal exposure to offshore Chinese Renminbi appears somewhat different. On the one hand, Chinese authorities have shown their willingness to transition to a different – and more balanced – growth model by monetary easing. On the other hand, a solid current account balance and sizable capital account inflows can provide support for the currency. Our China exposure is concentrated in the longer part of the sovereign curve which, in our opinion, is the best position to benefit from these trends.

Exposure Types and Significant Changes

The changes to our top five positions are summarized below. At the end of November, our top positions were Argentina, Venezuela, Mexico, Vietnam, and Indonesia.

We added exposure to the following:

- China, based on our expectations that the growth slowdown would continue to pave the way to lower local rates, while the People's Bank of China is unlikely to abandon control over the Renminbi.
- Sovereign duration in Mexico, Vietnam, Israel, and Indonesia where we like a combination of strong fundamentals and reform momentum.

We reduced our exposure to the following:

- Brazil to zero, as the election outcome may negatively impact the fundamental story, while corporate results are likely to be weaker in 2015.
- Some positions in Mexico as certain bonds reached our target prices even though our fundamental view remains constructive for the country.
- Sovereign exposure in Venezuela and corporate exposure in Chile due to concerns about the impact of current lower oil prices and weak growth momentum, respectively.

Fund Performance and Allocation Changes

The Fund (Class A shares excluding sales charge) gained 0.06% in November, compared to -1.31% for the J.P. Morgan Government Bond Index-Emerging Markets Global Diversified (GBI-EM) and -0.39% for the J.P. Morgan Emerging Markets Bond Index (EMBI). The Fund's biggest winners were Argentina and Indonesia (in hard-currency denominated bonds) and China (in local-currency denominated bonds). The Fund's biggest losers were India, Brazil, and Venezuela.

Turning to the market's performance, the GBI-EM's biggest winners were Turkey, South Africa, and Indonesia which benefitted from lower commodity prices. The biggest losers were oil-exporting Russia, Nigeria, and Colombia.

The EMBI's biggest winners were Egypt, Argentina, and Turkey, while its biggest losers were Venezuela, Ukraine, and Russia where lower oil prices and local political/economic risks (in the case of Ukraine) were, in general, the main drivers in November.

Please see the next page for standard performance information.

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

	1 Mo	3 Mo	YTD	1 Yr	Life
Class A: NAV (Inception 7/9/12)	0.06	-2.92	6.70	7.27	5.21
Class A: Maximum 5.75% load	-5.72	-8.50	0.58	1.13	2.65
GBI-EM Index	-1.31	-4.89	0.22	-0.33	-0.02
EMBI Index	-0.39	-1.19	8.64	9.28	4.34

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

	1 Mo	3 Mo	YTD	1 Yr	Life
Class A: NAV (Inception 7/9/12)	-2.58	-2.39	7.07	9.14	5.78
Class A: Maximum 5.75% load	-8.18	-7.96	0.93	2.88	3.01
GBI-EM Index	-5.11	-5.66	-0.01	-1.54	-0.13
EMBI Index	-1.81	-0.59	8.02	9.67	4.82

Data Sources: Van Eck Research, FactSet. All portfolio weightings and statements herein as of November 30, 2014. Unless otherwise indicated.

Expenses: Class A: Gross 1.42%; Net 1.25%. Expenses are capped contractually until 05/01/15 at 1.25% for Class A. Caps exclude certain expenses, such as interest. Please note that, generally, unconstrained bond funds may have higher fees than core bond funds due to the specialized nature of their strategies. The tables above 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 investors' 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 have been reinvested. Investing involves risk, including loss of principal; please see disclaimers on next page. Please call 800.826.2333 or visit vaneck.com for performance current to the most recent month ended.

Duration measures a bond's sensitivity to interest rate changes that reflects the change in a bond's price given a change in yield. This duration measure is appropriate for bonds with embedded options. **Stagflation** is a condition of slow economic growth characterized by relative high unemployment, and inflation. The **Venezuelan oil basket** is a weighted average of prices for petroleum blends produced by Venezuela. The Venezuelan oil basket trades at a discount relative to other oil benchmarks because of its higher content of heavy oil. **Quantitative Easing** by a central bank increases the money supply engaging in open market operations in an effort to promote increased lending and liquidity. **Correlation** is a statistical measure of how two variables move in relation to one other. **Monetary Easing** is an economic tool employed by a central bank to reduce interest rates and increase money supply in an effort to stimulate economic activity.

Emerging Markets Hard Currency Bonds refers to bonds denominated in currencies that are generally widely accepted around the world (such as the U.S.-Dollar, Euro or Yen). **Emerging Markets Local Currency Bonds** are bonds denominated in the local currency of the issuer. **Emerging Markets Sovereign Bonds** are bonds issued by national governments of emerging countries in order to finance a country's growth. **Emerging Markets Quasi-Sovereign Bonds** are bonds issued by corporations domiciled in emerging countries that are either 100% government owned or whose debts are 100% government guaranteed. **Emerging Markets Corporate Bonds** are bonds issued by non-government owned corporations that are domiciled in emerging countries. A **Supranational** is an international organization, or union, whose members transcend national boundaries and share in the decision-making. Examples of supranationals are: World Bank, IMF, World Trade Organization.

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. The **J.P. Morgan Government Bond Index-Emerging Markets Global Diversified (GBI-EM)** tracks local currency denominated bonds issued by Emerging Markets governments. The index spans over 15 countries. The **J.P. Morgan Emerging Markets Bond Index Global Diversified (EMBI)** tracks returns for actively traded external debt instruments in emerging markets, and is also J.P. Morgan's most liquid U.S.-dollar emerging markets debt benchmark.

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 and portfolio managers of other investment strategies may take an opposite opinion than those stated herein. Not intended to be a forecast of future events, a guarantee of future results or investment advice. Current market conditions may not continue. Non-Van Eck Global proprietary information contained herein has been obtained from sources believed to be reliable, but not guaranteed.

Investing involves risk, including loss of principal. You can lose money by investing in the Fund. Any investment in the Fund should be part of an overall investment program, not a complete program. The Fund is subject to risks associated with its investments in emerging markets securities. Investing in foreign denominated and/or domiciled securities may involve heightened risk due to currency fluctuations, and economic and political risks, which may be enhanced in emerging markets. As the Fund may invest in securities denominated in foreign currencies and some of the income received by the Fund will be in foreign currencies, changes in currency exchange rates may negatively impact the Fund's return. Derivatives may involve certain costs and risks such as liquidity, interest rate, market, credit, management and the risk that a position could not be closed when most advantageous. The Fund may also be subject to credit risk, interest rate risk, sovereign debt risk, tax risk, non-diversification risk and risks associated with non-investment grade securities. Please see the prospectus and summary prospectus for information on these and other risk considerations.

Investors should consider the Fund's investment objective, risks, and charges and expenses carefully before investing. Bond and bond funds will decrease in value as interest rates rise. The prospectus and summary prospectus contain this as well as other information. Please read them carefully before investing. Please call 800.826.2333 or visit vaneck.com for performance information current to the most recent month end and for a free prospectus and summary prospectus.