Manager Commentary: On the Gold Market

Gold off to a strong start in 2012, ended month at $1,737.70/ounce

By: Joe Foster, Portfolio Manager

Fund Review

The Fund's Class A shares gained 12.68% for the one-month period ending January 31, 2012 (excluding sales charge), while the NYSE Arca Gold Miners Index (GDM) gained 9.78% for the same period.

Average Annual Total Returns (%) as of January 31, 2012

	1 Mo[1]	1 Yr	5 Yr	10 Yr
Class A: NAV (Inception 2/10/56)	12.68	0.20	14.58	11.09
Class A: Maximum 5.75% load	6.23	-5.56	13.23	10.97
GDM Index	9.72	5.62	8.53	--

Average Annual Total Returns (%) as of December 31, 2011

	1 Mo[1]	1 Yr	5 Yr	10 Yr
Class A: NAV (Inception 2/10/56)	-13.30	-21.52	11.90	24.24
Class A: Maximum 5.75% load	-18.27	-26.04	10.58	23.50
GDM Index	-14.37	-15.48	6.36	--

[1]Monthly returns are not annualized.

Expenses: Class A: Gross 1.25%; Net 1.25%. Expenses are capped contractually until 05/01/12 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 is off to a strong start on the year, ending the month on its highs at $1737.60 per ounce for a gain of $173.90. Gold had been consolidating since September 2011 and a combination of transitory factors (discussed in our December Market Update) drove gold lower in December.

The new year brought a rebound from oversold conditions, which turned into a bullish break-out on January 25 when the Federal Reserve Bank (the "Fed") announced it would hold the targeted federal funds rate near zero "at least through late 2014". This was an unexpected change from previous Fed guidance of mid-2013. Gold advanced $45 on the day and the dollar fell, as the US Dollar Index (DXY) declined 1.2% for the month.

One of the primary drivers of a secular gold bull market is negative real interest rates, which is when the rate of inflation exceeds interest rates. During the gold bull market of the '70s, real rates on one-year treasuries turned negative in November 1970 and remained negative 56% of the time until October 1980. Real rates then stayed positive for 22 years until October 2002. Since October 2002, real rates have been negative 53% of the time. Real rates on one-year U.S. Treasuries were -2.86% at yearend 2011. In addition, real rates have turned negative across Treasury durations, such that five- and ten-year treasuries now carry negative real yields as well.

Erosion of wealth occurs when returns on fixed income fails to outpace inflation. Low real rates typically impact conservative investors the most, such as retirees, pension funds, money market funds and insurance funds. Low rates discourage savings and encourage investors to take on more risk in order to obtain adequate returns. Low rates may also feed asset price inflation, as risk pricing becomes distorted. The integrity of the financial system may become impaired. Low rates in combination with easy credit proved toxic for the subprime mortgage market. All of this is behind gold's reaction to the Fed's implicit assurance that real rates will remain low or negative for nearly three years to come.

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Market Outlook

Gold seems to have established a positive trend in January that may continue through the spring. At work are various efforts aimed at injecting more liquidity into the global financial system to stimulate growth. In addition to the Fed's January 25 rate announcement, the Fed also continues to voice the possibility of a third round of quantitative easing. Many emerging nations are now easing monetary policies. The Bank of England has recently finished another round of gilt buying and may still buy more. In February, the European Central Bank is expected to offer another massive round of bank loans through the long-term refinancing operation (LTRO). These actions potentially increase the supply of money, which effectively debases paper currencies. In addition, low or negative real rates are now common around the globe. Gold may serve as a sound currency alternative and financial hedge in such conditions.

High metals prices have created a global exploration boom and gold is at the forefront of this activity. Metals Economics Group estimates that exploration budgets increased by 50% to $18.2 billion in 2011; gold accounts for about half. Much of this exploration happens in remote corners of the world where the geology is favorable, but the infrastructure or geopolitical environment is less than optimal. An old miner's adage says "gold is where you find it". Unfortunately, it 'ain't' found in Ohio. It is usually found far from an educated work force, grid power or flat ground. There are few places where a mine cannot be developed, provided a deposit is rich enough and large enough. While places like Burkina Faso, Colombia, or Papua New Guinea, may not be a good location for many businesses, they can be very favorable jurisdictions for mining. Once a gold deposit is discovered, the process of de-risking and value creation begins.

Our research takes us to places that are mostly off the beaten track in search of projects that will become profitable mines that create value for shareholders. Recent destinations include Bulgaria, Guatemala, Guyana, and the Democratic Republic of Congo (DRC). Each have significant challenges, but all contain gold properties that we believe will be very profitable. Gold companies must develop honest relationships with communities and political leaders from the local to the national level. Bulgaria probably has more corruption than other eastern European countries. We invest in companies who strictly prohibit the taking or paying of bribes. This can create costly delays, mainly in permitting and moving materials by road or sea. In Bulgaria and elsewhere, with persistent company policies, the local chain of gatekeepers eventually learn not to expect special treatment.

Guatemala and Guyana had presidential elections in November in which pro-business candidates won. Both see gold mining as a promising source of jobs and tax revenue. Mexican drug cartels have infiltrated Guatemala and one of the new president's mandates is to provide greater security. We felt quite safe visiting the Escobal project to find Tahoe Resources busy driving two large declines (tunnels) to access their world-class silver deposit. With the recent approval of its environmental impact statement, the company is now in full construction.

A visit to the eastern DRC showed what a profoundly positive impact mining can have on a region. The geology of the country hosts incredible potential; however, civil war, militias and insurgents have prevented modern exploration and development. The past several years have seen a tentative peace prevail in the DRC and Randgold Resources is now developing the Kibali joint venture with Anglogold. Kibali is a multi-million ounce gold deposit that is expected to become a profitable long-life asset. While the robust geology of the property was confirmed as expected, the main reason for our visit was to see if this war-torn area would be secure for mining. We saw a large United Nations presence at airports, and the main rebel group in the area had been driven across the border by the Congolese army.

Randgold has determined that to be successful they would have to create a more peaceful environment for all. We saw no guns. The company had established a 200 kilometer security zone where they maintain an intelligence network for early warning of any threat to the operation. The company helped create a local police force and convinced the Congolese army their efforts were needed elsewhere. Roughly 16,000 people in 2,600 households across 14 villages agreed to relocate to make way for mine construction. There are no paved roads in eastern Congo and most people live in mud and grass huts (averaging 6 per hut/household) that are typically no bigger than my New York office. The company is replacing each hut with a small brick house with an enclosed cooking/washing area and outhouse. Each village will get a school and a clinic. A new church will also be built for the community.

People have survived by artisanal gold mining and subsistence farming. Artisanal (aka "illegal" or "conflict") miners use pans or sluice boxes to collect gold from stream soils. The disturbed soils wash into the stream system, staining the water orange. Gold is often extracted using mercury, which also washes into the environment. The Dodd-Frank Financial Reform Act contains conflict minerals legislation aimed at preventing the purchase and use of "conflict" gold and other minerals originating from the DRC. While some artisanal operations are run by warlords, in this area people were simply mining to earn a living. They also use slash and burn methods to farm. A small plot is burned to clear for planting; however, with no way of controlling fire, an entire hillside burns as well. Much of the rain forest is now gone. It was the dry season and the air was hazy with smoke. The new Kibali mine development is providing alternative jobs for the artisanal miners and gardens where women learn new farming practices. Here, education and commerce are creating a cleaner environment. As we walked through a village to reach an exploration property, it seemed we would be intruding, but people were genuinely happy. Perhaps the sight of outsiders carrying maps and compasses is a comforting sign of change from those wielding guns and machetes.

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