

Manager Commentary: On the Gold Market

Gold falls \$104.32 in May, ended month at \$1,560.43/ounce

By: Joe Foster, Portfolio Manager

Fund Review

The Fund's Class A shares declined 10.98% for the one-month period ending May 31, 2012 (excluding sales charge), while the NYSE Arca Gold Miners Index (GDM) lost 5.51% for the same period.

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

	1 Mo ¹	1 Yr	5 Yr	10 Yr
Class A: NAV (Inception 2/10/56)	-10.98	-32.61	6.87	14.03
Class A: Maximum 5.75% load	-16.12	-36.48	5.62	13.36
GDM Index	-5.51	-23.98	3.33	--

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

	1 Mo ¹	1 Yr	5 Yr	10 Yr
Class A: NAV (Inception 2/10/56)	-12.16	-22.65	11.06	19.38
Class A: Maximum 5.75% load	-17.22	-27.11	9.75	18.68
GDM Index	-10.47	-16.92	5.78	--

¹Monthly returns are not annualized.

Expenses: Class A: Gross 1.20%; Net 1.20%. Expenses are capped contractually until 05/01/13 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 took a tumble in May, declining \$104.32 or 6.3% to finish the month at \$1560.43 per ounce. Gold fell through the technically important \$1625 level early in the month, but held its next level of support at \$1530 per ounce. As has been the case for most of the year, gold has traded as a risk asset rather than a safe haven. In May gold correlated with risk assets, as the S&P 500 Index¹, copper, and WTI crude all fell 6.0%, 11.5%, and 17.5%, respectively. As the markets try to figure out the level of economic and financial chaos that may come if Greece exits the monetary union, the dollar has been seen as the safe haven. All of the drama in Europe appears to have diverted the market's attention from the sovereign debt and economic problems in the U.S. that we believe are just as daunting as those in Europe. The U.S. Dollar Index² (DXY) rose 5.5% in May to its highest level in 20 months. Ten-year U.S. Treasuries are now yielding an incredible 1.5% and the five-year is just 65 basis points. However, a weak May jobs report released on June 1 reminded the markets that all is not well in America. The DXY pulled back and risk assets continued to tumble, but gold became the safe haven with a \$63.67 advance on the day.

Gold producers essentially matched gold's performance for the month, with a 5.5% decline in the NYSE Arca Gold Miners Index³. Gold stocks outperformed on the June 1 rally. However, the "risk-off" mood in the markets has been particularly hard on the small-cap gold stocks. The Market Vectors Junior Gold Miners Index⁴ declined 16.8% in May. Exploration spending will probably slow a bit this year as juniors have difficulty tapping the equity markets. However, historic lows in interest rates are providing opportunities for juniors with good projects. On May 16, Allied Nevada announced a corporate debt deal for \$400 million at a coupon of 8.75%. Allied has a low-grade heap leach⁵ mine in Nevada that will be transformed into a world-class milling operation with this funding. Until now, money at single-digit rates was unheard of for a company of this size.

Merger and acquisition activity has been low due to low gold stock valuations, although on April 27 mid-tier producer IAMGOLD (4.31% of Fund net assets) announced the friendly all-cash takeover of Trelawney Mining (position was sold post-takeover) at a 35.2% premium to the previous day's share price. Trelawney has a multi-

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million ounce low-grade gold deposit in Ontario, Canada. We find this acquisition interesting because many juniors are developing large low-grade gold deposits, which we thought may be acquisition targets at higher gold prices. The combination of low stock valuations and a general lack of higher grade (and higher quality) gold projects made Trelawney an attractive target at \$1600 gold. As producers continue to generate cash, we may see more such takeovers if valuations remain low.

Gold has been gaining recognition as a monetary asset since the credit crisis. Recent news indicates the trend is continuing. Okayama Metal & Machinery has become the first Japanese pension fund to make public purchases of gold, initially allocating 1.5% of its portfolio to gold-backed exchange-traded funds. The State of Missouri General Assembly will soon vote on the Missouri Sound Money Act of 2012, which would make gold and silver legal tender within the state. Central banks in countries such as Mexico, Russia, Kazakhstan and the Philippines continue to add to their gold reserves. Meanwhile, China imported a record 103.6 tonnes from Hong Kong in April. Finally, a proposal from the German Council of Economic Experts circulating in Europe calls for European debtor states to pledge their gold reserves as collateral within a so-called European redemption fund, financed mainly by Germany. We doubt such a fund will materialize, as it is hard to imagine a sovereign handing their country's gold over to Germany in a worst-case scenario. Nonetheless, all of these events or proposals point to the continuing loss of faith in a fiat currency system that we believe is based on irresponsible fiscal and monetary policies.

Market Outlook

When Latin American and Asian nations experienced debt crises in the '80s and '90s, the western establishment insisted on a painful cure of austerity, tax increases and currency devaluation. Ironically, what worked for those countries is now becoming unacceptable to western leaders. There has been a popular backlash against fiscal austerity designed to reduce sovereign debt. France has elected a leftist president who campaigned for growth policies over austerity. In Greece, a left-wing candidate who has vowed to cancel their bailout agreement is a contender for June elections. At Camp David, the Group of Eight nations, led by President Obama, pressed Germany to abandon austerity to back more pro-growth policies. The anti-austerity movement may gain momentum if economies in Europe and the U.S. continue to sink. In a recent report, the Congressional Budget Office concludes that a 2013 recession is inevitable if proposed U.S. tax hikes and spending cuts take effect as planned on the first of January.

Deleveraging cycles have historically averaged about seven years and it appears that this one may not be an exception. Nearly four years of \$1 trillion-plus fiscal deficits, near-0% policy rates, and a historic expansion of the Federal Reserve Bank's (the "Fed's") balance sheet have not generated adequate growth. The U.S. unemployment rate would still be in double digits if not for the decline in labor participation to levels last seen 20 years ago. A report from January 2012 by the McKinsey Global Institute estimates that U.S. households are about halfway through the deleveraging phase, which they believe will take another two years or more. The International Monetary Forum (the "IMF") estimates that European banks plan to shrink their balance sheets by \$2.6 trillion over the next 18 months. The United Nation's International Labor Organization forecasts the global youth unemployment rate will stay at elevated levels for at least four years. The Federal Deposit Insurance Corporation (the "FDIC") reports that U.S. bank lending declined in the first quarter 2012 for the first time in a year. Some banks in Spain and Greece are set to fail without further bailouts. Fitch (ratings) downgraded Japan's sovereign credit rating in May due to the rapid deterioration of public finances. These are all features of an ongoing global deflationary credit contraction.

The fundamental problem with austerity during a deleveraging cycle is that the economy slows or shrinks more than expected. Cutting spending becomes politically unpopular at best and political suicide at worst, so elected officials look for other options, which are extremely limited. One is raising taxes on a minority of wealthy citizens and another is to take on more debt to attempt to fund growth. Each option lacks efficacy as it eventually generates a negative outcome, such as slower growth or sovereign debt downgrades. Without effective policy, central banks are left to somehow solve the problem because they are charged with providing full employment and/or saving the world from financial Armageddon. As a result, in the past four years it has become a conventional policy tool of central banks to print money or monetize debt. The Chairman of the Federal Reserve Bank of Philadelphia warned in a Financial Times article that "Central banks and monetary policy cannot resolve unsustainable fiscal policies. A monetary solution is a bridge to a world of rising and costly inflation and weakening fiscal discipline". However, central banks must honor their mandate and elected officials leave them with little choice. We would not be surprised to see central banks engage in more currency debasement over the term of this deleveraging cycle. We would also not be surprised to see gold rise in stature as a sound currency.

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All company weightings as of May 31, 2012.

¹The S&P® 500 Index consists of 500 widely held common stocks covering industrial, utility, financial and transportation sectors.

²U.S. Dollar Index (DXY) indicates the general international value of the U.S. dollar. It does this by averaging the exchange rates between the U.S. dollar and six major world currencies.

³NYSE Arca Gold Miners Index (GDM) is a modified market capitalization-weighted index comprised of publicly traded companies involved primarily in the mining for gold.

⁴Market Vectors Junior Gold Miners Index is (MVGDXJTR) is a rules-based, modified 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.

⁵Heap leaching is an industrial mining process to extract precious metals, copper, uranium, and other compounds from ore via a series of chemical reactions that absorbs specific minerals and then re-separate them after their division from other earth materials.

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