Minutes of the Advisory Board Meeting

February 20th, 2024

Finding Value in Gold and Mining Stocks via Active Management

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Key Take Aways:

- **Market Sentiment and Timing: Sentiment the gold and mining industry are at or close to all-time lows. Historically, when sentiment was this low it has been a great entry point into these markets.**

- **There are various opportunities in the gold mining sector, from companies yet to realize their potential to those with promising assets but lacking market recognition, showcasing the potential for contrarian investments in the industry.**

- **There are also lucrative resource opportunities in private markets, particularly in acquiring distressed assets from major companies and improving their production profiles, highlighting the potential for strategic acquisitions.**

- **Incrementum is launching a new, actively managed gold fund. The fund will follow a novel investment approach, resting on three pillars: Strategic allocation from a top-down approach, market timing, and bottom-up analysis.**

Biography of our special guest: Tavi Costa

Tavi is a Member and Macro Strategist at Crescat Capital and has been with the firm since 2013. He is responsible for developing Crescat's macro models as part of our thematic investment process. His research has been featured in financial publications such as Bloomberg, The Wall Street Journal, Reuters, Yahoo Finance, Real Vision, and others. Tavi is a native of São Paulo, Brazil and is fluent in Portuguese, Spanish, and English.

Before joining Crescat, he worked with the underwriting of financial products and in international business at Braservice, a large logistics company in Brazil. Tavi graduated cum laude from Lindenwood University in St. Louis with a B.A. degree in Business Administration with an emphasis in Finance and a minor in Spanish. Tavi played NCAA Division 1 tennis for Liberty University.
Follow Tavi on Twitter here.
Visit Crescat's website, here.

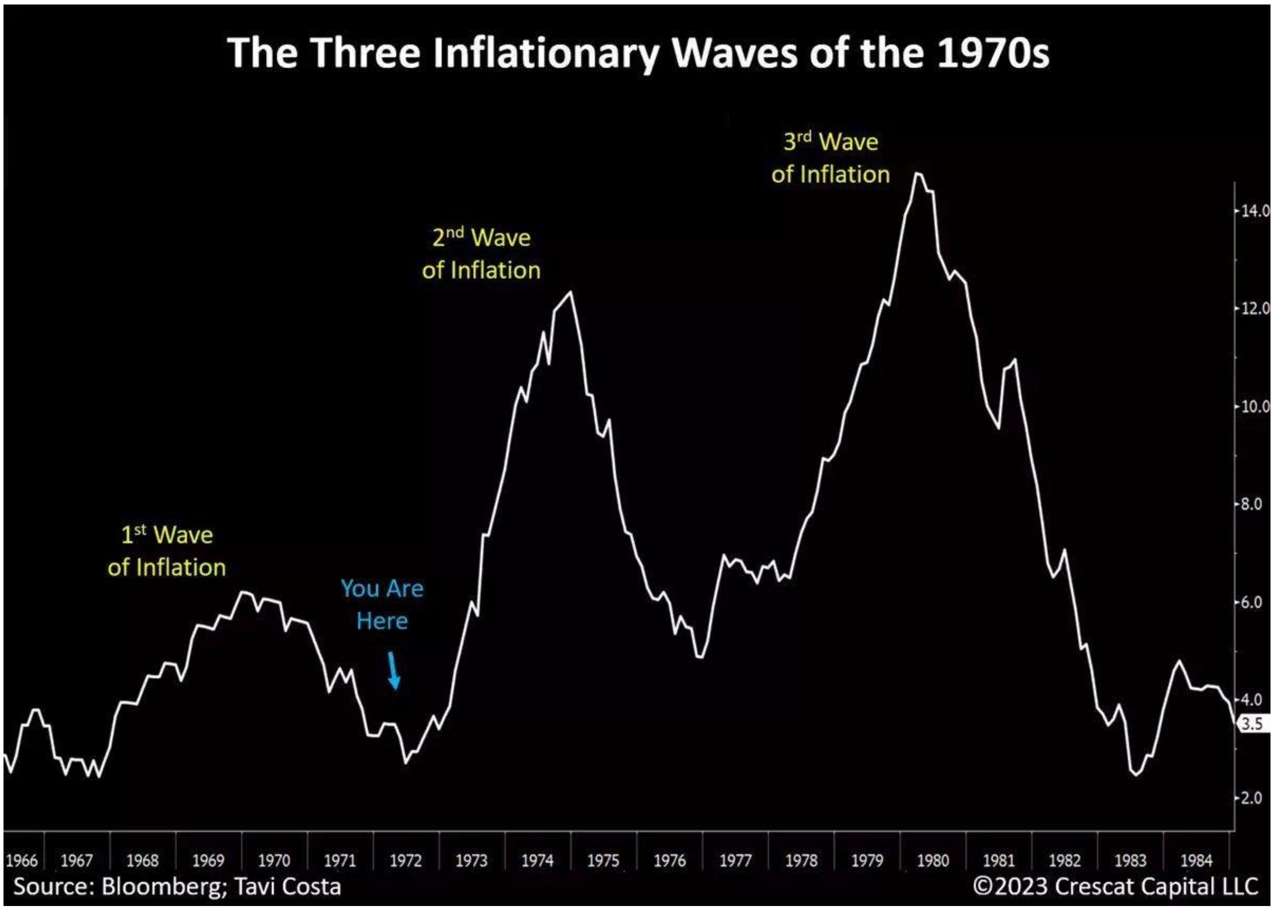
Ronnie Stoeferle

Just some housekeeping to get started. What's going on on our end? **We published a couple of your chart books. We are publishing a quarterly Bitcoin compass now. We also have our monthly gold compass, where we show the most interesting charts from Bitcoin, gold miners, the macro space, and so on; you can download them free of charge on our webpage**.

We're also working very hard on the upcoming In Gold We Trust report; May 17 is the big date. We're now in the part of the process between procrastination and panic, so we're getting into the hot phase and crunch time of this year's report. It will be lots of work, and we'll all be relieved when we can hit the send button on the 17th of May. We genuinely enjoy crunching the numbers, researching, thinking, and writing about gold.

Last week, we launched a new fund, with an active gold strategy. The same week, a really hot CPI print came out, and treasury yields were up significantly, while gold was down significantly, and miners were sold off. So yeah, it was quite a quite a contrarian move, I would say. But the good thing is that Stan Druckenmiller bought quite significant stakes in Barrick Gold, I think 1.7 million shares, and 500,000 shares in Newmont Mining. Still, when compared to the rest of his portfolio, it's not very significant. But he's also been reducing, for example, Nvidia, by roughly 30%. And it seems that he's continuing to buy in full force in the first quarter of this year.

We're really proud of our strategy in the new fund, and we can talk about that a little bit later. But let's jump into the discussion. Tavi, a while ago you put out a brief and concise summary of what's going on in macro. You said we'd got a trifecta of micro-macro imbalances. We've got a debt problem, reminiscent of the 1940s after the Second World War, we've got a speculative environment, like in the 1920s and 1990s, and we've got inflationary concerns, similar to the 1970s. You wrote that quite a while ago, but it is still super relevant. **What's your take on that and if you could give us a brief overview of all those three topics?**



Tavi Costa

Well, I think that's an important constraint for policymaking in general. It creates the bullishness and likelihood of commodities and hard assets to do very well. Looking at the positioning of investors in terms of not only the traditional portfolios but also large capital allocators, such as central banks, it is not in line with those constraints, meaning, it's highly likely that because we have a problem with the debt, which causes more monetary dilution over time, this becomes almost inevitable. At the same time, I think the genie is out of the bottle when it comes to inflation. Certainly, we're seeing the consumer and businesses being impacted by inflation in different ways. Regardless if it is through shelter cost or auto cost, or, health insurance, and so forth. All that is very deeply ingrained in the economy, and it's changing the way consumers behave. It's causing consumers to ask for higher wages and salaries. We're now unleashing a labor cost trend that tends to be very secular at its nature.

Then, on top of it all, we have this valuation problem that you refer to that is very similar to what we saw, especially in the tech bubble environment, and it can be measured in different ways. I think the **cyclically adjusted P/E ratio is probably one of the most interesting ways to measure that level of frothiness in equity markets**. I think that there are some great opportunities, but places that I would avoid altogether, which are US equity markets today. They look very frothy overall. I think that the outcome of this trifecta of macro imbalances will be that commodities will outperform especially financial assets, long-duration assets like treasuries, and especially the technology space. **And emerging markets could do very well on the back of those trends as well. There are going to be lots of opportunities and some big changes in capital flows and market leadership**, and I have very strong views on how to express that in the markets as well. But it's definitely a big change in the scenario that we've had over the last two to three decades, what we're facing now.

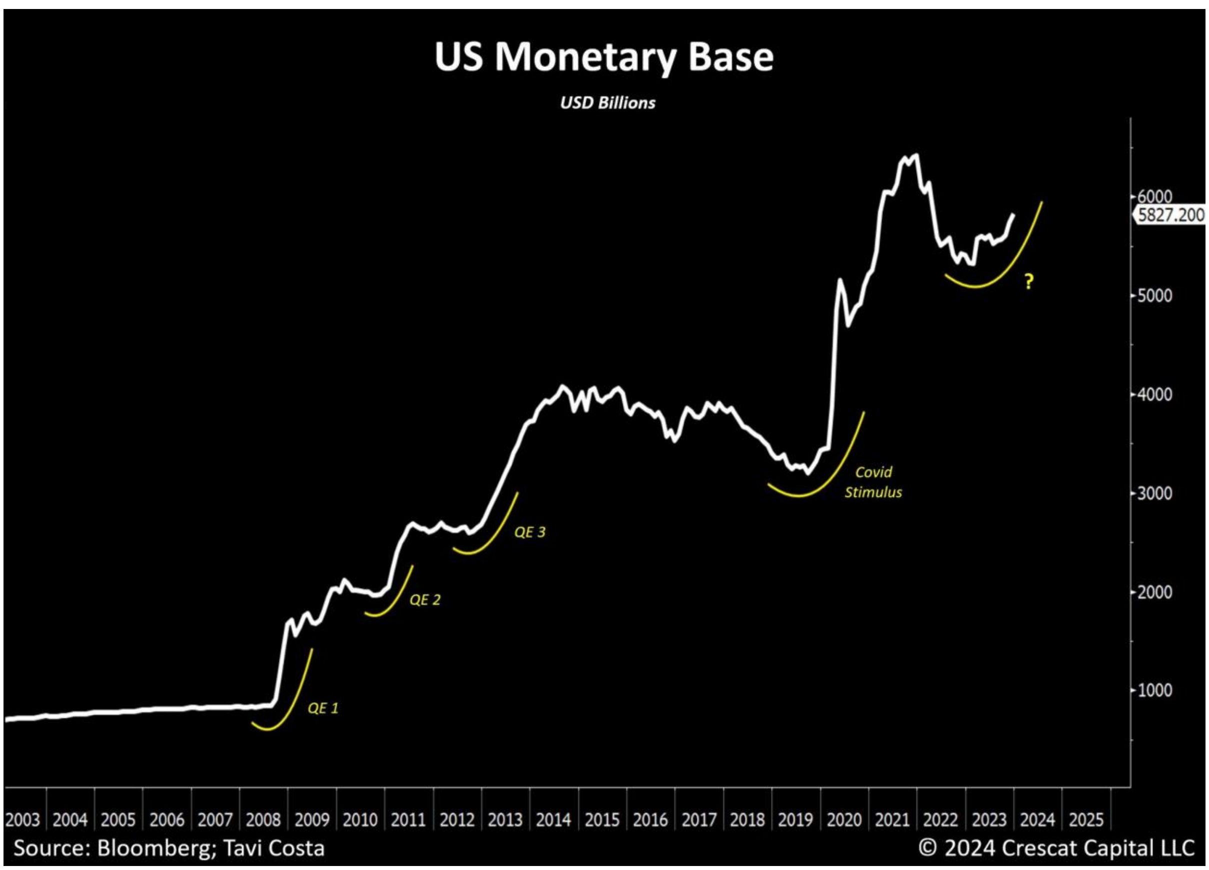
Mark Valek
May I jump in here? I would like to dissect this a little bit. Going into the topic of debt. We've been writing a lot about debt, it's a little bit of an elephant in the room. What are the indicators that you are looking at which tend to it not being sustainable? We all know it's not sustainable, but now the market views it differently than a few years ago. Are we there already? Or what are you looking at? What would have to happen? Would you to say there's really a change in the view on the debt situation?

Tavi Costa
The debt situation has been the major shift in asset correlations, which I believe began after the COVID recession and the subsequent stimulus. This led to significant changes in market behavior. For me, we're already in a new era, where interest rates behave differently in relation to equity markets. This poses a significant question for 60/40 portfolios and traditional portfolio hedging methods. We're certainly observing this phenomenon already, **with the cost of capital remaining higher for longer.**

To address your question specifically about government debt, what caught my attention a few years ago, and what I've been focusing on extensively**, is the issuance of debt.** The magnitude of this issuance is unprecedented, comparable only to periods like World War II when adjusted for inflation and GDP levels. This large issuance exerts downward pressure on treasuries overall and creates an interesting environment regarding the cost of capital.

The issue of deglobalization also contributes to the weakness in treasuries over time. Central banks' increasing purchases of gold reduce the demand for treasuries. Although central banks are not yet significant sellers of treasuries on a net basis globally, their buying is not proportional to the increasing issuances. Ultimately, the resolution may lie with the Fed, especially in the U.S., which may have to step in to absorb the excess debt.

One observation worth noting is the recent rise in the U.S. monetary base, reminiscent of levels seen during previous quantitative easing (QE) periods and COVID stimulus measures. This resurgence in the monetary base, to me, indicates inflationary pressures, which might not be immediately evident to everyone. Monetary dilution is a concern, driven not by increased money circulation but by rising banking reserves. This increase in the monetary base, approximately $400 billion annually, is a significant aspect of the overall story of how governments will finance their debts, with the ultimate burden likely falling back on the Fed.



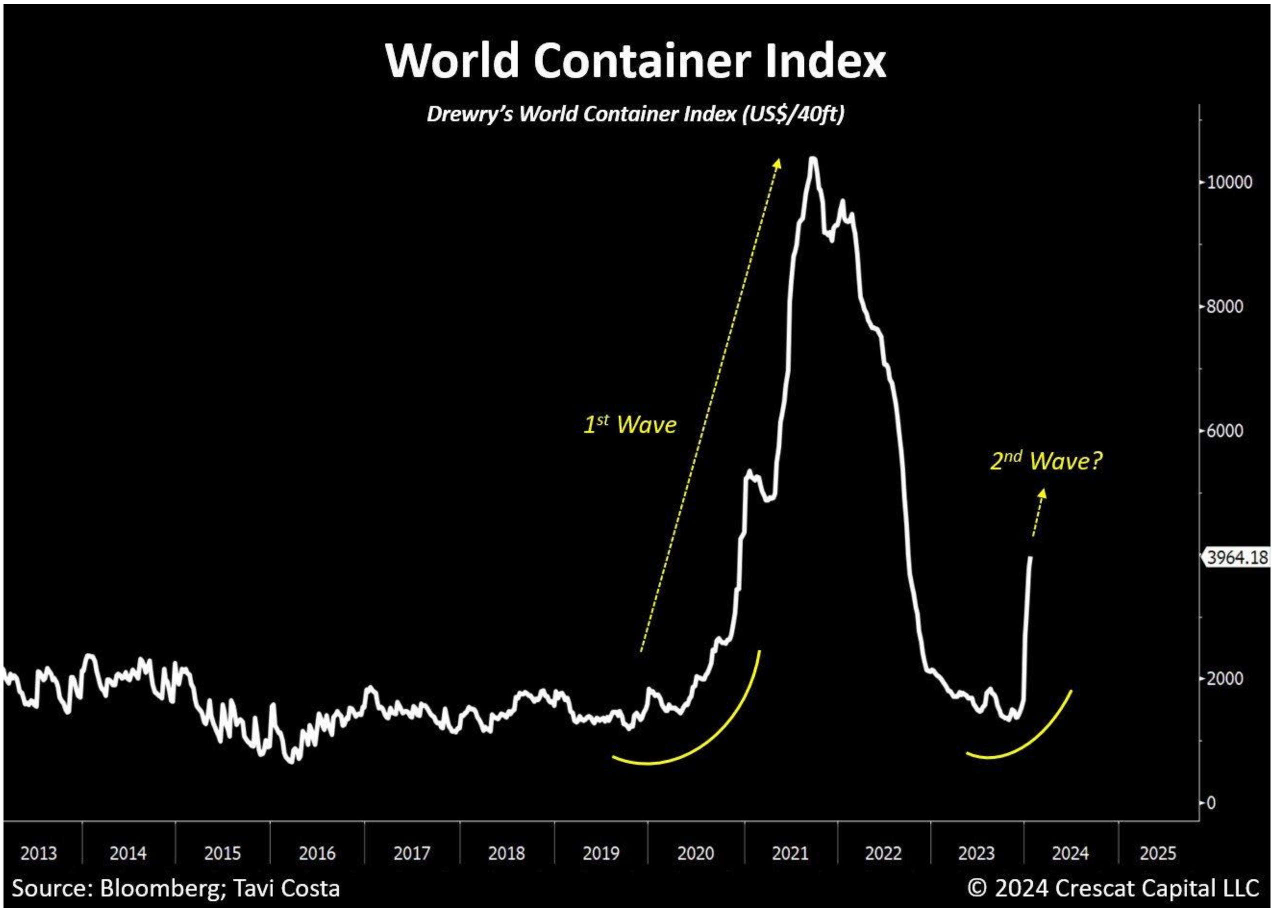
Mark Valek

Okay, thanks for that. Perhaps on the topic of inflation. Currently, according to official statistics, we've seen inflation numbers coming down substantially. In the minds of the average Wall Street investor, at least, the inflation problem isn't as imminent anymore. I think if you talk to people on Main Street, you'll probably get a different reaction and different answers, simply because prices haven't come down, which they probably won't. **Everything is still costly, so prices are still a problem. They're just not rising as fast anymore**. Nevertheless, if one looks at traditional inflation numbers, I guess you would expect these to go up sooner rather than later. Am I correct?

Tavi Costa

I hold the view that a re-acceleration of inflation is likely to occur, **based on the studies we've conducted on the inflation waves of the 1970s, 1940s, and even the 1910s**. It's intriguing to observe how inflation tends to manifest in waves. This happened in the US, as well as in other developed and emerging economies. Despite the deceleration you pointed out, nominal PCE remains at 5.9%, which is not a favorable sign. One factor that has captured my recent attention, and I would like to emphasize here, is the surge in immigration in the US. Academic papers on illegal immigration typically categorize its impacts into three buckets: technological advancements, population growth, and the abundance of natural resources. In the case of the US, the significant growth in population, predominantly driven by illegal immigration, is likely to have an inflationary impact, particularly on shelter costs. We may be entering an inflationary decade on that front. Still, it's difficult to believe that such a trend wouldn't also be highly inflationary for consumers, especially considering that shelter costs heavily influence consumer expenditures.

There are noticeable signs across the markets, such as rising break-evens, particularly on the short end, **indicating expectations for CPI rising across different durations. Additionally, factors like the de-globalized environment,** conflicts such as the Red Sea conflicts, and increasing freight costs globally are all contributing to inflationary pressures. The rising costs of agricultural commodities, diverging from overall food prices, are also expected to impact food prices worldwide. All these factors are likely to contribute to creating a bottom for inflation over time.



Moreover, while attention is often focused on quantitative tightening (QT) and interest rate policies, it's crucial to acknowledge other policies happening under the radar that offset the restrictive monetary policies implemented by the Fed. The increase in monetary base and other measures of monetary dilution, alongside significant fiscal spending, are all contributing to inflationary pressures. Additionally, the reshoring trend, driven by efforts to reduce reliance on authoritarian regimes and address geopolitical concerns, is expected to drive reindustrialization and bolster manufacturing capabilities, further influencing the inflationary landscape.

Mark Valek
Considering your remarks on inflation, let's address the final aspect of the trifecta: speculative mania, exuberance, or however one may wish to characterize it. From my perspective**, if we do experience an unexpected surge in inflation, it would likely set us on a collision course with this speculative fervor.** I'm unsure about your perspective, but I'm curious about how monetary policy would respond to such a scenario. In my view, it could pose a significant challenge for risk assets. How do you foresee this situation resolving itself?

Tavi Costa

I believe the issue lies in risk assets because one could argue that during inflationary periods, in what could resemble a banana republic environment, equities might soar even higher, leading to an even more severe market concentration. However**, I hold a different view because I see the cost of capital ultimately increasing. It's crucial to recognize that as yields rise, it fundamentally alters the macroeconomic landscape.** Consider recent announcements of dividends by numerous companies; it signals a competition among investors seeking yields. This, in turn, will drive up the cost of capital, not only on the debt side, influenced by interest rates, but also due to companies having to allocate more to dividends.

Reflect on the 1970s, where the majority of returns—about 80%—came from dividends rather than price appreciation. This reality is poised to manifest once again. We're witnessing airlines, despite facing some of the worst margins, announcing dividend payments. This trend, coupled with shareholder pressure on companies across industries, suggests a broader shift towards dividend payouts. Additionally, there's a perplexing skepticism towards natural resource industries from an inflation perspective, alongside an overly conservative approach, hindering capital expenditure on supply. This reluctance poses a risk; without significant capital allocation towards supply now, we won't see substantial changes in supply for the next five to ten years.

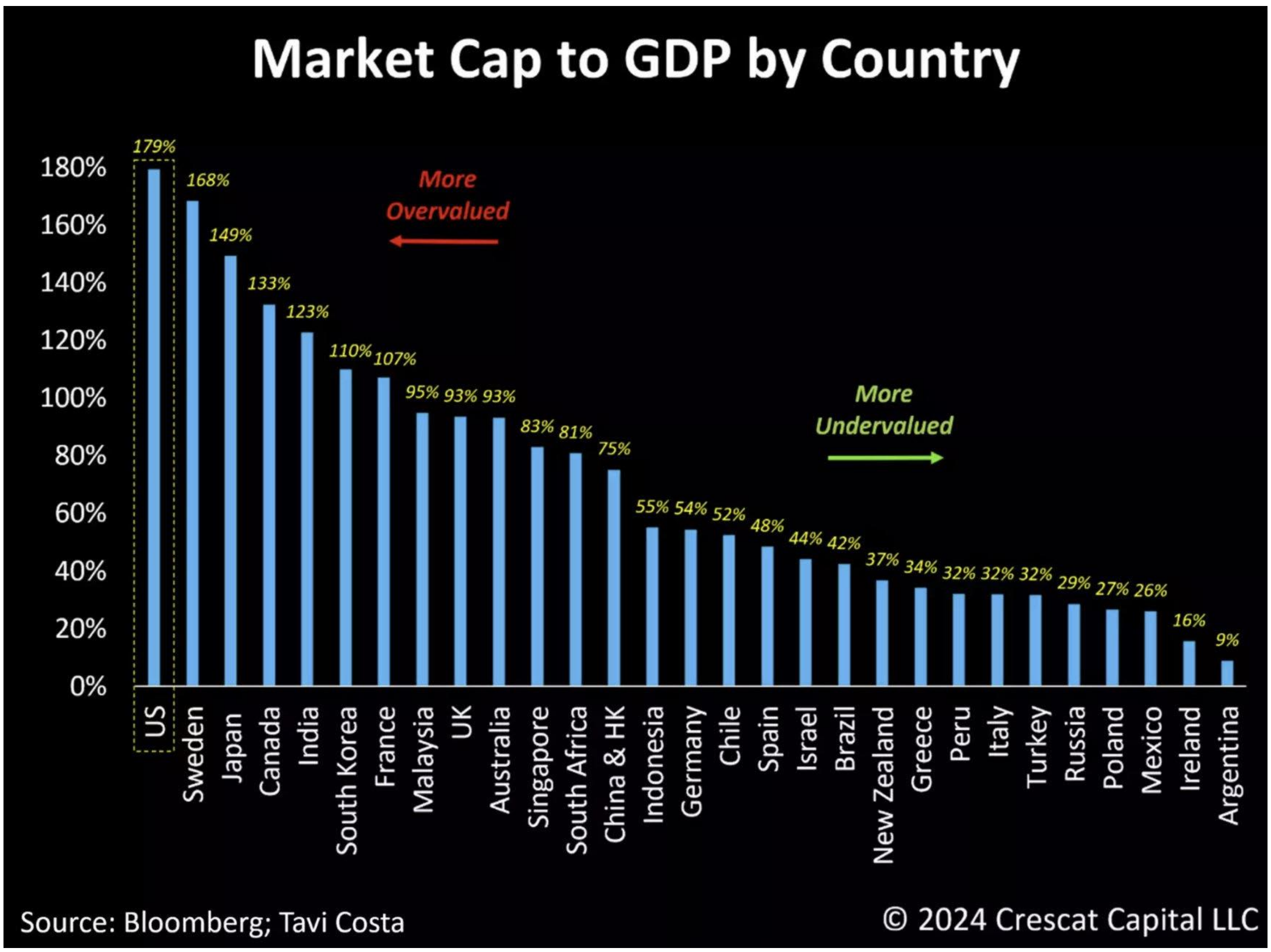
While these developments may seem daunting, they also present opportunities. I don't subscribe to a doom-and-gloom outlook. Instead**, I see tremendous potential to express market views and capitalize on these trends.** The resource space, in particular, holds promise as one such avenue.

Ronnie Stoeferle

Thanks, Tavi. What's intriguing about central bank policy, especially considering your perspective from Brazil, is the comparison between central bank and fiscal policies in emerging market countries like Mexico and Brazil versus those in most Western nations. **In emerging markets, policies tend to be more orthodox. Reflecting on 2021, central banks were initially pleased to see the return of inflation, dismissing it as transitory and temporary. They were notably slow to respond by raising rates, unlike the Brazilian Central Bank, which increased interest rates by over 12 percentage points**. They have experienced inflation first-hand, which is a valuable lesson. **So, how do you perceive the differences between industrialized developed economies and emerging markets?** I know you've been favoring emerging markets lately. Do you anticipate them repeating past mistakes, eventually?

Tavi Costa

Let's begin with the origins of emerging market policies. Traditionally, their focus has been on achieving a trade surplus, often by depreciating their currency to boost exports relative to imports. This pattern persists despite changes in political leadership every four years, especially in non-authoritarian countries like Brazil. The overarching strategy remains currency depreciation, leading to long-term cycles where commodity price increases are crucial for improving trade surpluses over time. **To me, being right about inflation and commodities is key to understanding emerging markets**. What draws me in is their undervaluation, particularly in comparison to developed economies. I've shared a **chart illustrating the market cap-to-GDP ratios across different markets**, highlighting South America and other emerging markets as significantly cheaper relative to US markets. This valuation disparity extends to metrics like CAPE ratios and other indicators, indicating that emerging market companies appear inexpensive.

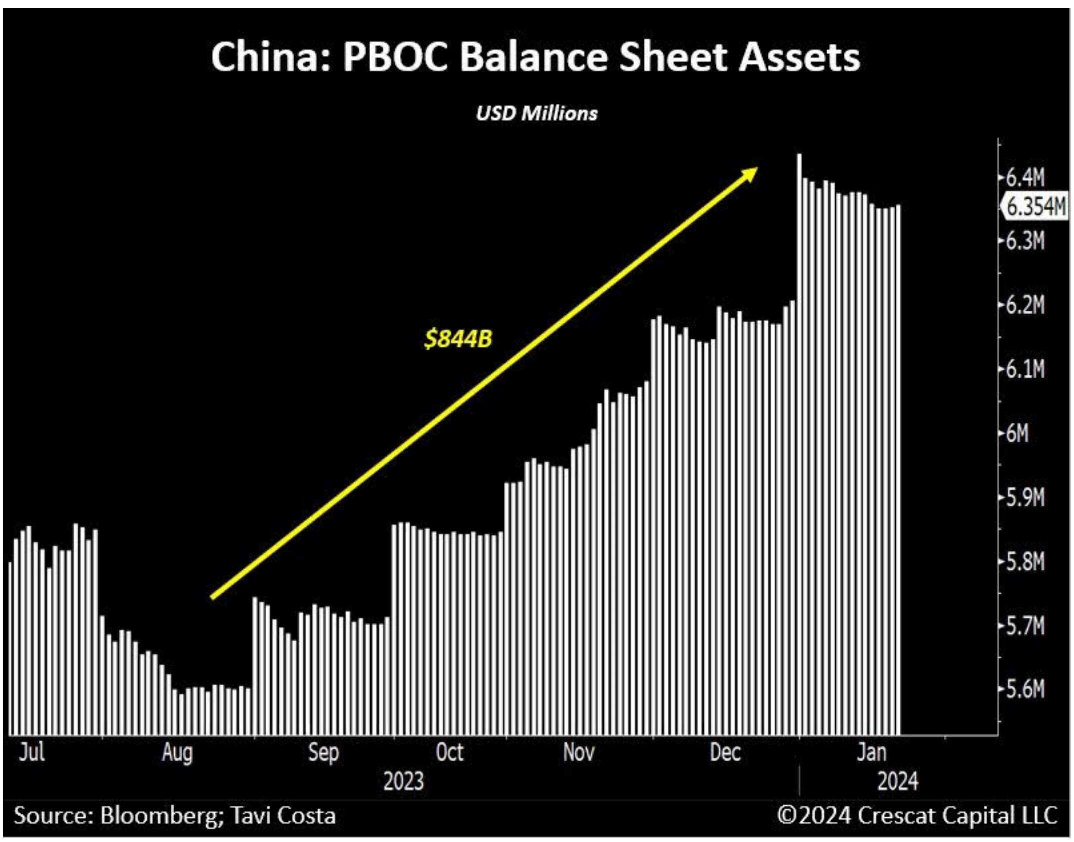


Another factor worth considering is the role of artificial intelligence (AI) in closing the gap in labor quality between emerging markets and developed economies like the US. **The US stands out as**

a true melting pot, fostering competition driven by a diverse labor force. I believe AI will enhance capabilities in emerging markets, thereby improving labor quality and potentially impacting multiples.

Speaking specifically about Brazilian markets, they appear exceptionally cheap in terms of free cash flow yield, reminiscent of the depths of the global financial crisis. These markets offer attractive dividends and growth prospects, particularly in sectors like banking, historically undervalued compared to other regions.

As commodity markets see increased capital deployment, emerging markets are likely to benefit. However, it's essential to differentiate between markets. While I'm cautious about Chinese equities due to moral considerations, I recognize the potential impact of stimulative policies on their market dynamics. **The PBoC just inflated their balance sheet by $850b**. Despite past bearish views, the current environment suggests a shift in perspective, with stimulative policies potentially influencing inflation and commodity markets.



Ronnie Stoeferle

Let's shift our focus to gold now. Many people have been somewhat disappointed with its performance. Despite reaching new all-time highs in US dollar terms last year, peaking around $2150, it didn't sustain the breakout as expected. We've consistently highlighted the impact of opportunity costs and real rates, which have posed significant headwinds for gold prices. If you had told me two years ago that interest rates in the US would exceed 5% while experiencing significant disinflation, and the price of gold would surpass $2000, I wouldn't have believed it. So, from our perspective, the best is yet to come for gold. Once the Fed begins lowering rates, although with the recent CPI print and strong economic indicators, it's challenging to gauge. The GDP forecast by the Atlanta Fed is around 2.7-2.9%, suggesting we're still far from a recession. However, we maintain our recession call.

Looking at the sentiment shift over the past year, from anticipating a hard landing to now a Goldilocks environment, I'm skeptical. **How do you see gold performing in this environment of high opportunity costs and a resilient economy?** Do you believe gold is already signaling that the Fed will eventually panic and lower rates, as they've done before?

Tavi Costa

Yeah, you had a great chart showing the change in Fed interest rates and the corresponding appreciation of gold. I think you're onto something with that because that's probably what will ultimately happen. The problem here is certainly the change in correlations that we're seeing. I was at a dinner recently with a JP Morgan roundtable event, and this guy was pounding the table on Bitcoin, which I have nothing against, by the way. He was saying that gold is losing its value and status as a reserve currency. I've heard this so many times, yet the very next day, gold made new highs in six different major currencies.

So, we know that central banks are buying gold, especially in Eastern societies, as you guys cover very well. It's hard to believe that this will change, given the imbalances we see in the treasury

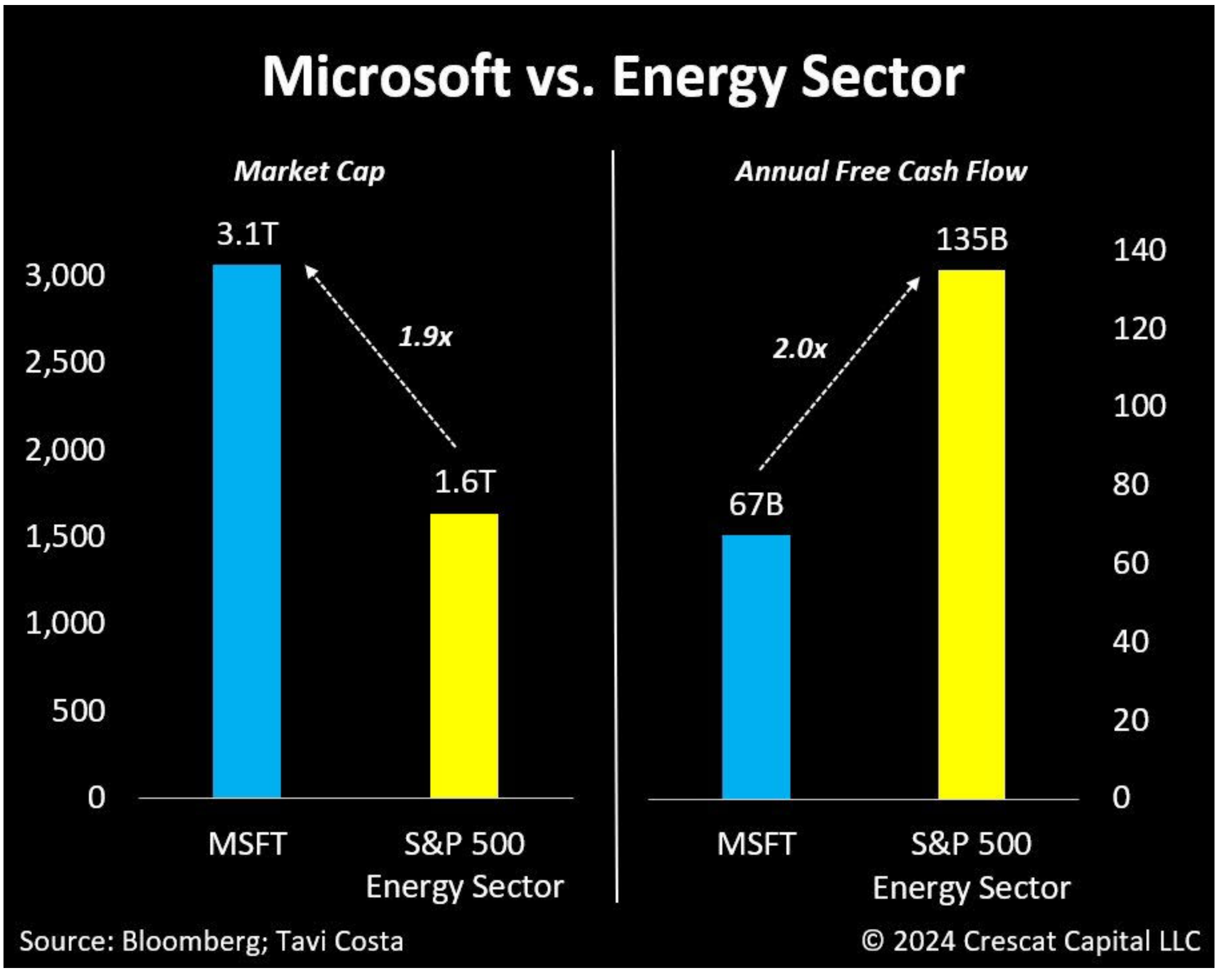
market with issuances and inflation. What we haven't seen yet is this movement towards hard assets. With inflation problems persisting, I've always been of the view that instead of interest rates staying higher for longer, it's actually inflation staying higher for longer, and that's yet to be the case. When we look at how much financial advisors own of gold, there was a survey from Bank of America that was really interesting. About **71% of them actually own zero to 1% allocation towards gold.** So, that 60/40 portfolio allocation, when you think about how expensive it has been historically, it's one of the most expensive levels we've seen. I think that's also in line with the fact that most of those institutions are going to have to diversify away from the 40% that has been ultimately all treasuries into some other things like gold. **Even if it's a 5% allocation, it would be a big change in terms of the drivers for the demand for gold overal**l. So yeah, I think that's the big story that's likely to come.

Mark Valek

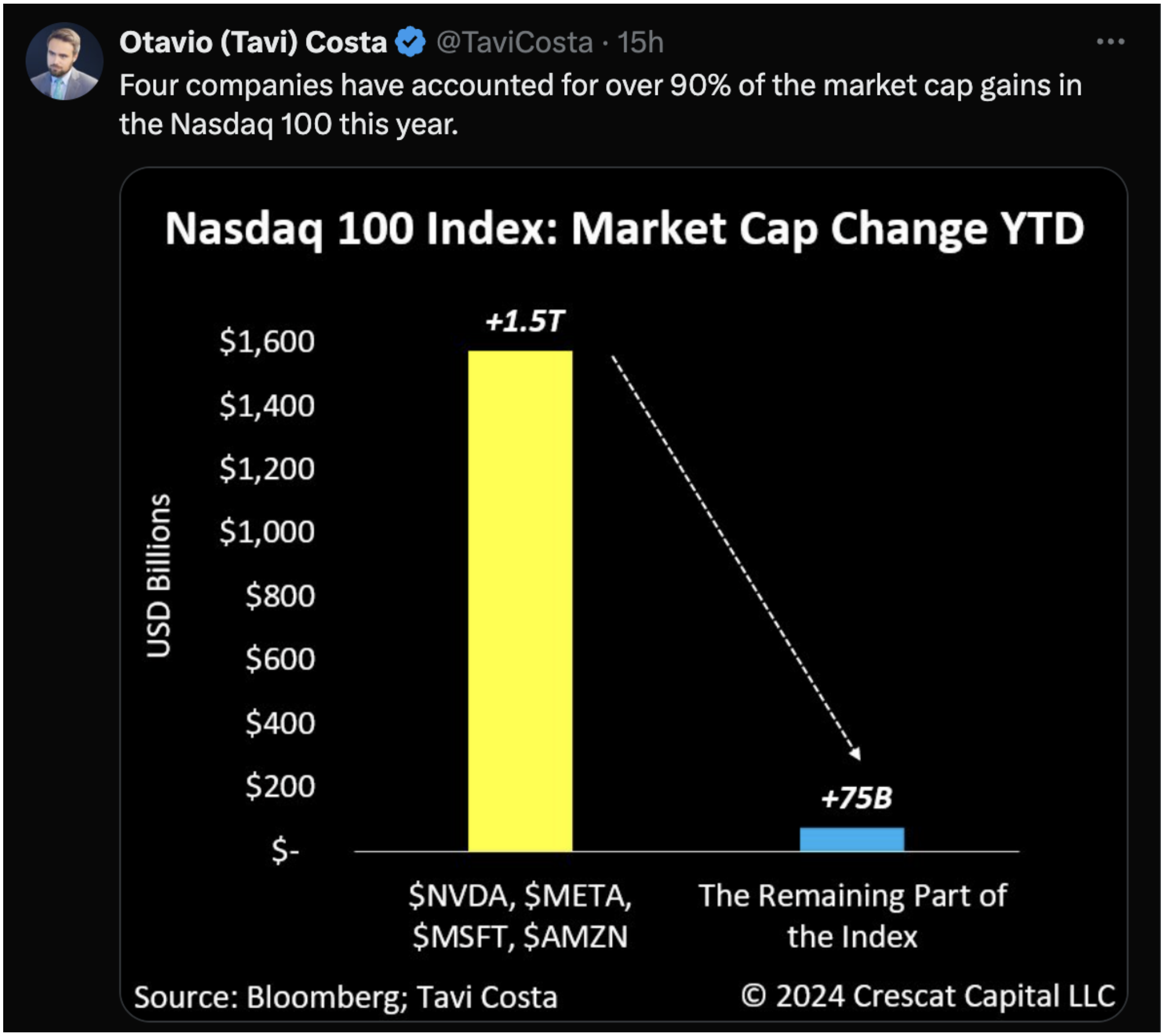
Talking about negative sentiment, we had an internal meeting, and Ronnie came up with a comparison of uranium investments, which was a big darling of commodity investors for years, but nothing much happened for years and years, and the situation got worse and worse. Now, finally, I think people who have invested in uranium stocks are finally seeing some kind of payoff. That's one of the few sectors in the commodity sector which is currently performing pretty nicely. So, is gold, or perhaps silver, the new uranium? And if so, which pockets now are perhaps potentially the cheapest? Where are you looking at when it comes to gold and silver mining?

Tavi Costa

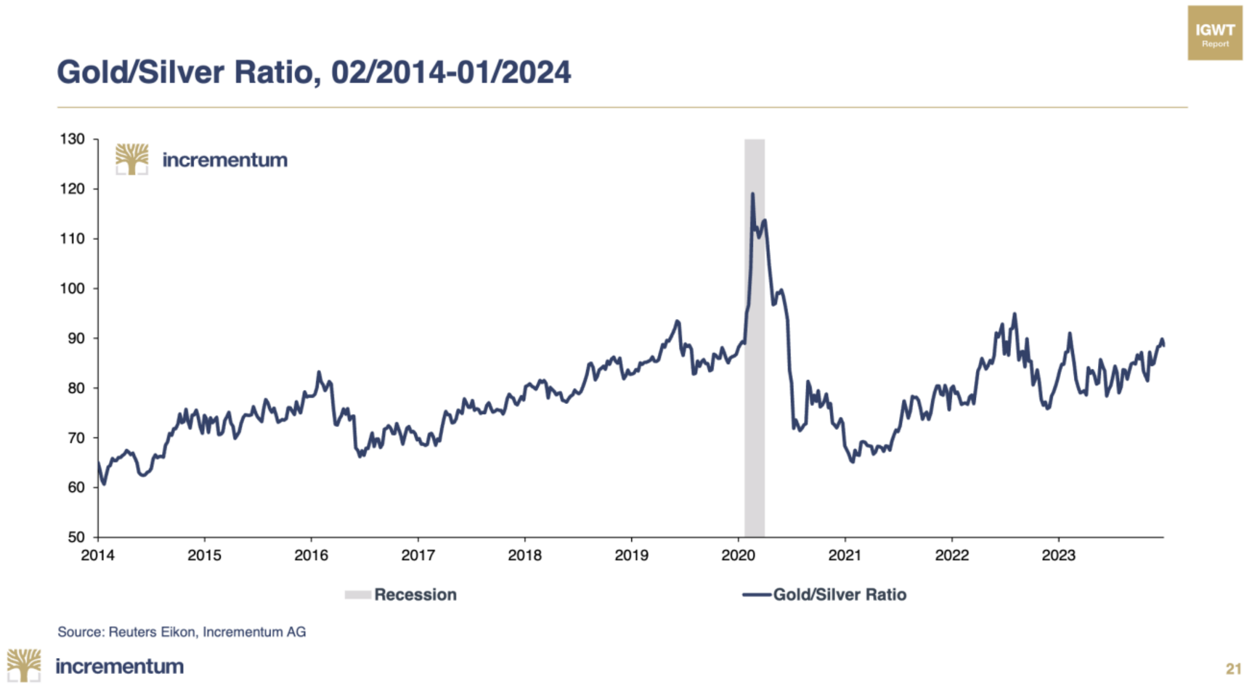
Well, **the overall metals and mining industry is where I see the real opportunity**. When I became more bullish on commodities, I broke it down across all commodities and tried to understand not only from a valuation perspective but also from a growth standpoint, and how those cycles tend to unfold. My understanding is that yes, you want to be long all commodities essentially, and people tend to overanalyze things. What I find interesting is the reshoring of economies, especially developed ones, which we're seeing as a real trend.



The amount of fiscal stimulus going towards infrastructure development is definitely happening. You can see it from many fronts, particularly from exports of steel producers outside of the US to the US, which is really interesting as well. It's hard to believe that were going to see all these trends ongoing, especially the Green Revolution. But I would say that the revamping of manufacturing is even more important than the green revolution itself. It will drive the size of the market in metals and mining much higher. I made a point recently about how Microsoft alone is twice the size, in terms of market cap, of the entire energy space. The energy space today generates twice the size of free cash flow than Microsoft does. If you extrapolate that to the mining space, as you guys have done, it's perplexing, almost. But to me, it just speaks to the opportunity here.



In terms of understanding the micro developments in the metals and mining space, I get really bullish on precious metals, especially because I think they're out of favor within the sector. Speaking with people who used to be big proponents of the gold space, they've thrown in the towel and are getting into copper, lithium, and uranium. But I don't want to lose focus**. I think that the silver chart and the likelihood of an explosive move in silver is higher than anything I can see in the commodity space.** The last thing I want is to miss that. So I'm looking for assets that are high quality to provide leverage to silver prices as of now. I think it's been the case for me for the last two to three years. Now, I'm building a portfolio of those ideas. It's not easy, and it takes time, but I think there's a lot more to do on that front.



I'm extremely bullish. Now look at the Gold-Silver ratio, which is at about 87 or so. I mean, when was the last time we've seen those numbers? Those numbers usually come when we are at the very bottom of the market for precious metals. I've never seen a bull market in gold that wasn't led by silver. So I'm really bullish. The big surprise for myself has been the resilience of gold that has not been matched by the resilience of the miners. The miners have been destroyed, even with gold prices staying where they are. Some people point to the cost structure of those companies rising relative to gold prices, and that's a fair way to make those assumptions.

Then I've seen somebody saying, "Well, you don't want to be bullish on gold until you start seeing the gold-to-oil ratio rise." That is just crap, I have to say**. If you go back to the early 2000s, the miners had one of the best trends we've seen in history in terms of appreciation. The gold-to-oil ratio was actually falling during that period, meaning oil was outperforming gold, and that cost structure situation still caused gold miners to appreciate significantly**. So now other factors matter even more than those things. Oil is actually an important aspect, and energy costs are an important aspect for the cost structure of the miners, but it's not all you need. You look at the miners, they are usually really difficult businesses to own.

Ronnie Stoeferle

When it comes to mining in general at the moment, we have quite similar views. I think all three of us are pretty bullish. But when it comes to the setup of our funds, we have different views. Mark, perhaps you can briefly describe what we're trying to achieve with the new fund.

Mark Valek

Happy to do so. Well, yeah**, I think we're taking a really innovative approach here, considering the fact that we believe this is a highly top-down asset class**. Dealing with gold mining equities is perhaps one of the most top-down asset classes one can encounter. Obviously, on the bottom-up side, a lot of inputs, as you just named, come into play. But from the top-down perspective, the price of gold, geopolitical factors, and interest rates, among others, all play significant roles. It's a very complex topic that we're dealing with. So, it's very much a top-down approach that we're taking in this fund.

From this perspective, **we wanted to create an approach that captures the significant upside potential while also actively managing the downside risk, because we all know that this is a very risky asset class and the drawdowns can be very brutal**. A purely relative return approach didn't feel sensible to us. So, that's why we put a lot of thought into this approach. **We basically have three pillars to this approach**. Number one is our strategic portfolio composition. We don't only go long on stocks; we also look at bonds and can even consider private placements. We believe there are some exciting opportunities on the bond side, especially if you want to play it safe for top-down reasons. Then, we have our market timing indicator, which gives us top-down input on how much capital we want to allocate towards riskier sub-sectors. And the third, still important pillar, is bottom-up analysis. Obviously, one has to scrutinize the individual names very diligently. That's where Ronnie's expertise in this space, having been in it for a long time, comes in.

This is essentially our very active approach, which we're taking here. We also aim to have a somewhat more conservative approach. Obviously, if we're not fully invested all the time, we will not capture the complete upside potential. However, we want to capture most of the upside while actively managing the downside and providing superior risk-adjusted returns with this strategy. So, this is what we're aiming to do, and we believe we have a good starting point now. It's developing quite well so far.

Ronnie Stoeferle

Absolutely, it's a bit like in sports terms, where offense wins games, but defense wins championships. So, we really aim to avoid the major drawdowns that are often seen in this space.

Ronald-Peter Stöferle, CMT

Ronni is managing partner of Incrementum AG and responsible for Research and Portfolio Management.

He studied Business Administration and Finance in the USA and at the *Vienna University of Economics and Business Administration*, and also gained work experience at the trading desk of a bank during his studies. Upon graduation, he joined the Research department of *Erste Group*, where he published his first *In Gold We Trust* report in 2007. Over the years, the *In Gold We Trust* report became one of the benchmark publications on gold, money, and inflation.

Since 2013 he has held the position as reader at *scholarium* in Vienna, and he also speaks at *Wiener Börse Akademie* (i.e. the Vienna Stock Exchange Academy). In 2014, he co-authored the book *Austrian School for Investors* and in 2019 *The Zero Interest Trap*. Moreover, he is a member of the board at *Tudor Gold Corp*. (TUD), a significant explorer in British Columbia's Golden Triangle and a member of board at *Goldstorm Metals (GSTM).* He is also an advisor to *Matterhorn Asset Management*, a global leader in wealth preservation in the form of physical gold stored outside the banking system.

Mark J. Valek, CAIA

Mark is partner of Incrementum AG and responsible for portfolio management and research.

While working full time, Mark studied Business Administration at the *Vienna University of Business Administration* and has continuously worked in financial markets and asset management since 1999. Prior to the establishment of *Incrementum AG*, he was with *Raiffeisen Capital Management* for ten years, most recently as fund manager in the area of inflation protection and alternative investments. He gained entrepreneurial experience as co-founder of *Philoro Edelmetalle GmbH*.

Since 2013 he has held the position as reader at *scholarium* in Vienna, and he also speaks at *Wiener Börse Akademie* (i.e. the Vienna Stock Exchange Academy). In 2014, he co-authored the book *Austrian School for Investors*.

About Incrementum AG

Incrementum AG is an independent investment and asset management company based in Liechtenstein. Independence and self-reliance are the cornerstones of our philosophy, which is why the four managing partners own 100% of the company. Prior to setting up Incrementum, we all worked in the investment and finance industry for years in places like Hongkong, Frankfurt, Madrid, Toronto, Geneva, Zurich, and Vienna.

We are very concerned about the economic developments in recent years, especially with respect to the global rise in debt and extreme monetary measures taken by central banks. We are reluctant to believe that the basis of today's economy, i.e. the uncovered credit money system, is sustainable. This means that particularly when it comes to investments, acting parties should look beyond the horizon of the current monetary system.

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