Minutes of the Advisory Board Meeting
Austrian Economics Golden Opportunities Fund
October 5, 2015

Is the Fed in the corner?

Highlights of the conversation:

Heinz Blasnik:

- We should see a few more elevated CPI readings over the next few months due to the base effect.
- It seems to me that there is now a great danger of a credit crisis in China that will be really difficult to control. I expect it to weaken the yuan further.
- If the yuan, the dollar, and the yen are set to become weaker next year, then it's going to be the euro that is going to rise.
- Nowadays, 40 dollars per barrel of oil is roughly what 10 dollars used to be in the mid-70s and the late 90s – it's an important support level.
- Commodity prices can rise even while the economy isn't doing very well. So, I would be careful with betting on the decline continuing in the short term.
- The biggest economic sector (gross) in the US is manufacturing. So, in light of the fact that the manufacturing sector is weakening now, we have to assume that a recession has become more likely.
- All the money supply growth that has happened since the Fed ended QE has been credit expansion by commercial banks. And the sector in which the biggest expansion has taken place is corporate debt. But I suppose that commercial banks will be very reluctant to continue to extend more credit to the corporate sector due to defaults in the fracking industry.
- I focus on gold and gold mining stocks and also some Treasury bonds. One could also consider Russian stocks – this is a market that has a lot of upside potential in terms of percentage gain.

Jim Rickards:

- Inflation and inflationary forces have been roughly balanced but they both exist. The danger of course is that in an unstable equilibrium it could kick out one way, so you have to be prepared for inflation and deflation at the same time. Your indicators are working so well because they are detecting this dynamic equilibrium.
- Right now the deflationary forces are getting the upper hand.
- Taper talk, tapering, removing forward guidance and talking tough is tightening! So, we've seen this tightening, which means it's not a surprise to see capital abandoning emerging markets, emerging markets' currencies are falling and emerging markets' stock markets are going down.
- I expect the Fed's next step will be easing, not tightening – which of course is very bullish for gold!
- Perhaps in March or April of 2016 I think the Fed will deliver some kind of easing: The Fed has 5 ways to ease: helicopter money, forward guidance, QE4, currency wars and negative interest rates.
- I do not expect them to go to negative interest rates, because we have a very large money market industry, and negative interest rates would destroy the money market industry – it's a trillion dollar industry.
- I think we can exclude negative interest rates, QE and helicopter money for various reasons. That leaves only two instruments: one is currency wars, the other is forward guidance.
- The economy is not in too great shape, corporate earnings are going to continue to be lousy, because so many of the large US corporations' earnings stem from overseas and because of the strong dollar weak local currencies are getting translated back into dollars at previously cheaper dollars. That's not fully priced in yet.

Zac Bharucha:

- It's remarkable that in the US – we haven't actually had an interest rate hike for nine years, and the recovery has been going on for four years – the Fed is still not pulling the trigger on interest rates. Could it be the case that we have been running through a whole economic cycle with no Fed action?
- I think the market is really confused, because it doesn't really know what the Fed's looking at – but we suspect that the Fed remains nervous about global deflation.
- Will the Fed raise interest rates? It seems less and less likely to me. I believe that gold as a currency will start to perform.
- In commodities, I believe the sharpest losses are now behind us, particularly in the energy complex – oil, heating oil, natural gas. We could still see lower prices, because the weakened demand side has met a supply side that was increasing capacity, the steepest declines should be over. Again, this is one of the

malinvestments, an obvious malinvestment area – since the whole metals, mining and energy complex received far too much investment capital due to false price signals.

- I think it's evident that something is going disastrously wrong within the EU, first with the North-South divide and now with the migrant crisis. I think the EU will be under serious pressure in 2016.
- If the EU changes shape and nations impose border controls the EU will drift further away from the initial idea (the humanist idea of trading and traveling within a region), Germany would actually be a massive loser because of it's export-dependence and aging population.
- The world is on the edge of chaos – political and economic chaos! It will remain like this.

Frank Shostak:

- Currency wars – I don't really see it at present. The US dollar is strong and I think it will probably be strong for many months to come.
- I agree with Ronni, that there is a very low likelihood that they raise rates this year. If they have a subdued 2016, then obviously an interest rate hike is unlikely.
- There are some signs in manufacturing and industrial activity which are possibly surprising various analysts – the ISM manufacturing index fell close to 50 – the reference between booms and busts, or recession and expansion.
- Recently, monetary growth in America has collapsed – it currently stands at 3.9 % against 9.6 % in August.
- Europe may have a certain recovery, a false recovery because of the money supply – but the real stuff is not made by the printing press.
- From my monetary perspective, China looks set to remain stable. I don't see any tendency for depreciation.
- We are currently at a stage where the so-called bubble cycle is accelerating.
- I would still prefer to have a reasonable weighting in treasury bonds. I would probably have certain positions in stocks. I would probably stay away from commodities and commodity-related stuff. And probably more than just a little cash.

Ronald Stöferle:

- The English version of our book "Austrian Investing Between Inflation and Deflation" is very close to being published. John Hathaway wrote a brilliant foreword!
- It seems that the whole market turmoil and this huge sell-off, especially in commodity markets, was actually really good for our fund and the whole concept because we are currently down 5%, which is a tremendous performance relative to all inflation-sensitive assets.

- We're in the process of launching two new funds. One will be a distressed mining fund, so will only invest in those miners that are having a hard time at current gold prices, because these companies will offer the highest leverage as soon as gold rises.
- The second fund that we're close to launching is a fund that is based on Harry Browne's Permanent Portfolio concept.
- We are holding a long position in a Eurodollar futures, because when we initiated the positions the markets were suggesting that the Fed would raise rates to 1% by June 2016 – and from our point of view this is not going to happen.
- If you look at the breakdown of Wednesday's ISM manufacturing report, there was one ratio that really caught our eye – it was the weakness in *new orders* vs. the strength in *inventories*. It seems that new orders are basically collapsing. So, this could also imply that industrial production growth could cross into negative territory in the coming months and would also mean that there might be a recession looming.
- The total amount of credit in China in the last two decades increased 54 fold. You don't have to be a great economist to see that a massive amount of malinvestment has taken place due to this enormous credit expansion.
- I don't think that many market participants actually realize that there is just a normal credit cycle turning down in China now, and this credit cycle has probably been more dramatic than anywhere else in the world in the last few decades.
- I think one very interesting point is – and this is kind of overlooked by the media – that there was one FOMC member actually mentioning negative interest rates at their September meeting.

Mark Valek:

- The two new products [the distressed mining fund and the Permanent Portfolio fund] are different strategies. In terms of volatility, one is more aggressive, most of the time we'll concentrate on the mining sector only. On the contrary in this fund we'll like to be invested in diversified inflation-sensitive assets, energy equities and so on. Apart from being more concentrated, the new fund is actually a scheduled investment scheme where we will increase our investment level during the first 24 months.
- Most market participants view Germany as a safe haven country. But the bloated, export-oriented capital structure of their economy makes them very vulnerable. Apart from that, the broader implication of the emerging VW case will have to be evaluated.
- Ben Bernanke in a private speech commented on the possibility of negative interest rates: he said that he was afraid of introducing negative interest rates back in 2008/09, but now he would feel more confident to do so. So, this topic has entered the discussion.

Transcript of the conversation:

Ronald Stöferle:

Welcome gentlemen to the Advisory Board of our Fund. I'm very pleased to have you with us!

Mark and I will begin with some housekeeping just to let you know what's happening on our side.

First of all, we are very excited that the English version of **our book "Austrian Investing Between Inflation and Deflation" is very close to being published.** We are in the final process of editing and proofreading. But we're very happy that the book will be ready very soon! We already set up a webpage where you can order it. The German version has been a huge success in the German-speaking world. It was nominated as the best finance book in 2014.

Regarding the fund, we are really excited as well! We were able to gain some inflows recently. **It seems that the whole market turmoil and this huge sell-off, especially in commodity markets, was actually really good for our fund and the whole concept because we are currently down 5% since the beginning of 2014, which is a tremendous performance relative to all inflation-sensitive assets**. So, people are realizing that our approach, meaning investments in mining stocks, commodity stocks, energy stocks and so on – but with a timing factor based on our inflation signal –, that this approach actually makes sense, and that we didn't experience any major draw-downs like most of our large competitors. So, that's an encouraging sign!

Besides that, we put out a deflation warning at the beginning of July. In September we published a chartbook, where we discussed the possibility, that the massive deflationary pressure could also have an impact on equity markets, especially on biotech stocks for example and on emerging markets. So, I think that was a pretty good call!

Mark Valek:

Beyond that we're working at two new funds, which we plan to launch rather sooner than later. We cannot complain about a lack of work.

The two new products are different strategies. In terms of volatility, one is more aggressive, most of the time we'll concentrate on the mining sector only. On the contrary in this fund we'll like to be invested in diversified inflation-sensitive assets, energy equities and so on. Apart from being more concentrated, the new fund is actually a scheduled investment scheme where we will increase our investment level during the first 24 months. We will stagger the investment process over a two-year period, beginning with 20% and working our way up. So we'll just start investing slowly and steadily in the mining space regardless of our investment signal. These distressed mining company stocks will benefit the most from a turnaround in gold, which we expect in this time period.

Ronald Stöferle:

So we'll clearly focus on those companies struggling at the current gold price because those offer of course the highest leverage to rising gold prices. We're absolutely sure, it's impossible to predict the low in gold, and therefore we will average into the market with a kind of fixed slices that we are investing every now and then to get some sort of a cost-average effect.

Mark Valek:

On top of that, we'll sell put options to be able to get in a little cheaper, or if they expire, we'll cash in some very nice premiums.

Ronald Stöferle:

And the second fund that we're really close to launching is a fund that is based on Harry Browne's Permanent Portfolio concept: that is 25% equities, 25% bonds, 25% cash, and 25% gold. We made certain adjustments, since obviously cash and bonds do not offer too much upside anymore. The whole concept is that it's rebalanced quarterly on a fixed date. And we're implementing managed futures instead of 25% cash allocation. And instead of holding 25% of gold, we have added diversification to include the entire commodity complex and energy. So, it's based on the Permanent Portfolio concept, but it's our own interpretation. The idea is that the managed futures kick in as soon as there is volatility, they can perform most importantly on the downside, but also on the upside, and they offer a really good diversification. We're marketing the product as a core portfolio as opposed to a kind of satellite investment.

Ronald Stöferle:

So, now we can jump into the discussion. Last Friday was quite an interesting day. In general, it seems that volatility is back in the markets. And we thought we would name this call “Is the Fed in the corner?” We would like to talk about three points, and if there are any other points that you want to discuss, we’ll also talk about them.

The first point regards the status quo of currency wars. **We’re clearly seeing that deflationary pressures are prevailing.** We see for example that the markets are clearly pricing in further disinflation – you can see it from the tips, or in the continued strength of the dollar and weakness in commodities. We also saw (and often twittered about our predicted outcome) that the Fed did not hike rates in September. **We also bought a large position in a eurodollar money market fund, because when we initiated the positions the markets were suggesting that the Fed would raise rates to 1% by June 2016 – and from our point of view this was not going to happen.** It appears that the Fed is a bit in the corner. People do not trust Janet Yellen. I don’t know if you saw the speech that she recently gave when she suffered a kind of collapse. So, I think that there’s enormous pressure on Janet Yellen and the Fed is actually in the corner.

We can go through the other points later – these are emerging market countries, i.e. China, and the US dollar.

But first of all I’d like to hear your opinion on the status quo of currency wars. Let’s start with Jim, Mr. Currency Wars!

Jim Rickards:

Sure, I'd be glad to. You make a very good point. First of all, I completely agree with your idea of the unstable equilibrium, in other words: **inflation, and inflationary forces have been roughly balanced but they both exist.** And **the danger of course is that in an unstable equilibrium it could kick out of the way, so you have to be prepared for inflation and deflation at the same time**. Sounds crazy, but that's the way the world is. And you have your indicators that flip back and forth. A year and a half ago was more deflationary, maybe a year ago or eight months ago you saw a little more inflation, now you're seeing more deflation, that means that **your indicators are working pretty well, because they are detecting this dynamic**

equilibrium; it's not indecision, it's actually a pretty good description of what's going on.

Right now the deflationary forces are getting the upper hand. You look around the world: Russia is in recession, Brazil is in recession with stagflation, Japan is in recession, Canada is in recession, China and the US are not technically in recession but they are both slowing down very abruptly and **a lot of emerging markets are suffering from very dramatic capital outflows**, as I mentioned the situation in South Africa this weekend – so that’s a very powerful story. Now a lot of this is caused by the Fed. The Federal Reserve has been tightening for two years! When I said that to people, they think I’m crazy; they are like: “What are you talking about? Rates have been zero, how could they be tightening?” But it’s about two and a half years ago, all the way back in May 2013, that Bernanke started talking about tapering, he didn't actually taper but he talked about it. Then in December 2013, they began to taper, in November 2014, they finished tapering, and in March 2015, Janet Yellen removed Forward Guidance.

And ever since then, they have been saying over and over again that they are going to raise interest rates. Well, I’m sorry, **rates have been at zero, or close – but taper talk, tapering, removing forward guidance and talking tough is tightening!** It's all about expectations: if we say we’ve got to tighten, the market doesn't wait until you actually tighten, until you actually raise rates. The reaction function is to anticipate raising rates and act as if the raise has already happened. **So, we’ve seen this tightening, which means it’s not a surprise to see capital abandoning emerging markets, emerging markets’ currencies are falling and emerging markets’ stock markets are going down.**
Now what has happened recently is that all of that whole dynamic which goes back almost 2 1/2 years, was based on an assumption that the US economy was fundamentally strong enough to bear the cost of higher interest rates and a stronger currency – those two things go together. Obviously if you even talk about raising interest rates in a world where everyone else is cutting interest rates, then your currency is going to be the strongest currency. And just to shed a little bit more light on that, of course throughout **the last two years until August 2015, China had informally pegged its currency to the dollar**. So, when you peg your currency to another currency, in effect you’re outsourcing your monetary policy to the other central bank, because if they tighten, you have to tighten in order to maintain the peg – that's how pegs work. **So long as the Fed was tightening, the dollar was getting stronger and China had to tighten in order for it to maintain the peg. They were selling dollar assets and using the dollars to buy their own currency – buying the yuan for dollars, reducing the money supply, which is a foreign tightening. And so the Fed not only took the US economy down, they took the Chinese economy**

down with them, because the two central banks are co-dependent and the PBOC is joined to the Fed in this tightening stage, which makes absolutely no sense.

Now, the Fed's blunder was to say that the economy was stronger than it was and strong enough to actually bear tightening and bear a strong currency. That is based on their forecaster models, which are completely obsolete. So, you had their forecast regarding their policy. The forecast showed strength, and they thought they could tighten because the strength would bear it. It turns out that the forecast was wrong, which was not surprising – so, they actually tightened into weakness, which made the US economy even weaker.

Now that all comes tumbling down through the data, it's impossible to deny the data on employment. Job creation in the United States peaked in November 2014. Forget about the monthly noise, go back and look at job creation trends from last November until September, which just came out last week, job creation went down precipitously: it was about 360,000 last November, then it went down to 250, 230, 220, 175, 145 etc. as the months went by. The US job creation stalled last year.

Ronald Stöferle:

Totally agree, Jim. I think the participation rate is at the lowest level since 1977. So, this also confirms this view.

Jim Rickards:

Not only is job creation falling rapidly, the labor force is in decline, the labor market is shrinking, real wages are slumping. By the way, of all the data points – they are all important in different ways, but real wages is the single most important data point because that's where the two sides of the dual mandate come together. The tenets of the dual are price stability and job creation. Other central banks usually have just price stability, a single mandate. The Fed has this dual mandate. Well, **real wages are where the two things converge, because if real wages are going up that means labor market conditions are tightening, labor can demand a raise, a real raise – and when you get a real raise, then it will begin to flow through the supply chain and cause demand inflation**. So, that's really what the Fed is worried about. Minimum wages are flat, minimum wages are not showing any tightness at all, so notwithstanding the fact that the unemployment rate is down to 5.1%, all the other indicators – labor force participation, efficiency of labor force, real wages, job creation –, every other indicator is showing a weakening in the labor market and more slack.

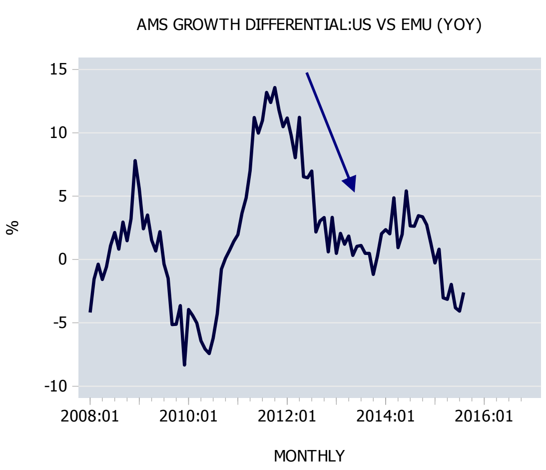
The PCE price inflator year-over-year is declining, it's 1.2%, nowhere near the Fed's 2% goal. So, **take all the data points, apply them to growth and inflation: they're all**

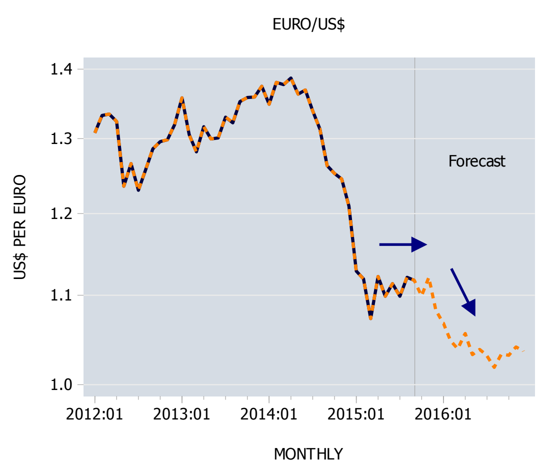
far away from the Fed's forecast and moving in the wrong direction at the same time. So, I see no way the Fed can raise interest rates this year, I think the earliest rate increase is probably the end of 2016. I expect the Fed's next step will be easing, not tightening – which of course is very bullish for gold!

So, the Fed is blundering, and taking the world with them**. I expect a global growth depression in 2016**. I think the next move by the Fed will be some form of easing, probably in the form of a reinstating Forward Guidance, giving the market some words or phrases that make it clear that the Fed is not going to raise interest rates for an extended period of time.

Frank Shostak:

The US dollar is strong and I think it will probably remain strong for many months to come. From my analysis, which focuses on the money supply growth differential, currently the USD is in favor. It's just the beginning of its powerful effect. So, from monetary analysis – which I call the "calm factor" –, we may see more support for the US dollar. Obviously, there could be a more preferable effect, like interest rate differential, there is a noise factor that can have an effect – but the underlying movement still points to a strong American dollar.[1]





Source: AASE – FX Report October 5 2015 EURO

Whether the Fed is in a corner – I'm not so sure, what this means. Obviously, from an Austrian perspective, raising interest rates, to normalize them and to have a normalization of the interest structure would be better for wealth creation. But the Fed doesn't really care about wealth creation, they just care about various funny

[1] See Appendix B for an overview of the AAS Economics currency exchange rate determination model.

indicators like GDP. So, **at the moment, they are scared to upset bubble activities** (they probably don't regard them as bubble activities).

So, I agree with Ronni, that the likelihood of the Fed raising rates this year is very low. If they have a subdued 2016, then obviously an interest rate hike is unlikely to happen. So, the question to ask from my perspective is: "What will happen next year?" **There are some signs in manufacturing and industrial activity which are possibly surprising various analysts – the ISM manufacturing index fell close to 50 – , the reference between booms and busts, or recession and expansion. We forecast with our models that it's not the time for it to fall below 50, which would imply that the manufacturing sector is unlikely to contract.** The contraction could last rather likely until 2016. We could see some improvements here and there, but the underlying trend is down. So, if this is the case, then the Fed is unlikely to raise rates.

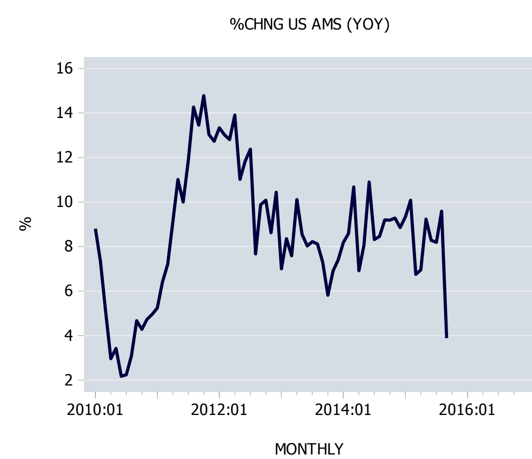
Ronald Stöferle:

Frank, that's a very good point! I think for what it's worth, I would ascribe more confidence to the predictive ability of the ISM service than to the non-farm payrolls for example. I think the non-farm payroll figure is one of the most politicized data on the planet, up there with the Chinese GDP numbers. I would like to add a chart to the transcript, which is very interesting: **If you look at the breakdown of Wednesday's ISM manufacturing report, there was one ratio that really caught our eye – it was the weakness in *new orders* vs. the strength in *inventories*. It seems that new orders are basically collapsing. So, this could also imply that industrial production growth could cross into negative territory in the coming months and would also mean that there might be a recession looming**. Very good to hear that you're also looking very closely at the ISM.

Source: ADMIS – Paul Mylchreest, Bloomberg

Frank Shostak:

And one more point: **monetary growth in America has collapsed – it currently stands at 3.9 % versus 9.6 % in August.**



Source: AAS Economics Weekly Report October 5 2015

Mark Valek:

That is significant!

I just wanted to ask you, Frank, if you know off the top of your head: you were talking about the money growth differential in the Eurozone and the US, which you said is 3.9% for the US. And for the Euro is it obviously much higher?

Frank Shostak:

Yes, it is much higher in Europe! And that makes it inevitable, from a monetary perspective, that the American dollar will gain against the Euro. So, I see a strong American dollar.

Zac Bharucha:

I would like to comment on currencies. There is an iron triangle of central banks, politicians and big corporate leaders – and between them they're doing everything to keep the globalization train moving. This is typical form for a power structure: it must maintain itself rather than undergo radical reform. What happens is that the discredited system struggles on until there is a systemic collapse, a complete breakdown of the ruling order. So, everything that has been done in terms of the monetary policy in the last three years was, I think, an attempt to keep the left-wing parties bound to a corner of politics, and the far-right to the other corner so that there would be no serious upset to the . I think the sense is just to keep the globalisation game running. There have been patch-ups but no significant changes. But obviously, there are cracks appearing all over the place.

It's remarkable that in the US – we haven't actually had an interest rate hike for 9 years, and the recovery has been going on for four years – the Fed is still not pulling the trigger on interest rates. Ok, they've stopped the asset purchases. **Could it be the case that we have been through a whole economic cycle with no Fed action? Market participants are confused, because they don't know what the Fed is looking at in order to set policy– the Fed probably remains very nervous about global deflation because** at every opportunity they've pushed the interest rate hike back down the pipe. So I don't quite agree with Frank regarding the Dollar. I know he's looking at it from a monetary creation point of view and calling the Dollar higher. **I think, a lot of people are looking at the US as being the convoy in the recovery and buying the dollar on the basis of a stronger economy and interest rate rises. Well, I'm just not so sure now, I think that has been rapidly priced out of markets.** A rate **rise seems less and less likely to me. I believe that gold as a currency will start to perform.** Gold did not surge when the stock markets crashed but it held its value. And I think we've put a good base in there. So, my tip for next year: I think there could be a strong run in gold when there's some disenchantment with some other paper money. There are no particularly strong cases for euro, dollar, yen etc., for anything out there really, but I think gold relative to the rest will do well.

The stock market, I think, reflects the economic slowdown and invetory build from earlier this year. Remember from my previous calls – we have been looking at this monetary contraction, thinking the stock market might top out –and there has been a topping out in stocks. Think about it; the Nikkei 225 peaked out in June and then again in August, the Dow Jones Transportation Index, which is pretty sensitive to the economy, peaked out over a year ago – which was a warning signal; the Dow, the S&P all hit peaks between spring and summer of this year, and since then there have been some quite big losses, in particular in the German DAX.

I think there is going to be one more big drop in stocks in the coming 2-3 weeks. That will make fresh flows for the move. And after that, I think, there will be a traditional year-end puff-it-up rally. But looking to 2016, I think that activity could slow down/struggle. The Fed is basically out of the game. And the bear market in stocks will regain its legs again next year.

Ronald Stöferle:

Jim, do you think that a recession in the US might be looming? Do you think the Fed, and especially Janet Yellen, would really be prepared for strong recessionary pressure?

Jim Rickards:

I don't think the Fed is prepared for a recession at all. I don't think the Fed sees a recession as I do. I think that there is a good chance of a US recession that could go last early into next year.

I actually expect oil prices to tend towards the $50-$60 a barrel range, all the way into 2017. So, I do not expect it to go back up to 70 and I don't expect it to go down to 30 either. **That alone would remove some of the deflationary pressure, but you're going to see new problems arising in terms of corporate defaults. Because there are some $5 trillion of mostly junk debt that was issued by frackers that can't pay.** I mean you have to say: "Well okay, the price of oil went down because Saudi Arabia sets the price for the frackers and wants to put the frackers out of business," we understand that. But where did all this oil come from to begin with? Well, they had to borrow money for the exploration. And they borrowed trillions of dollars. All this borrowing was based on the perception that the oil could be sold between $70 and $130 a barrel depending on the project. And we're obviously below that.

Heinz Blasnik:

I agree with that! And I wanted to say something about the connection with the weakness in manufacturing. A mistake is often made because of the way GDP accounting works. People automatically assume: “70% of economic activity consists of consumption.” But that is actually not true, because if you look at the gross economic output tables, then you see that **the biggest economic sector in the US is manufacturing**. Consumer spending represents between 35% and 40% of all activity. The reason this isn’t the same in GDP is because in GDP you only count fixed investments and only final good output – all the intermediary stages of production are left out. So, if you add in the intermediary stages, then it becomes obvious that the biggest amount of spending is actually made in the manufacturing sector. **So, in light of the fact that the manufacturing sector is weakening now, we have to assume that a recession has become highly likely**. Now, what previously helped the manufacturing sector into an uptrend from the 2009-low? Well, that was the money supply extension that took place between 2009 and 2011. There were two peaks in money supply expansion: the first was in 2010 when the year-on-year rate was close to 17% on the broad true money supply. And a secondary peak just above 16% was made in 2011. And since then, **annualized money supply growth has come back down to about 8.3% at the latest reading. Now, when money supply growth slows down, then a lot of the manufacturing activity that had been set into motion because of the money supply growth, is going to come under pressure. And I think this is what we’re seeing now**.

So, in terms of Fed policy: if the Fed is going to rely on Forward Guidance, then this is definitely going to influence the money that is flushing about in the financial markets – because there is a lot of money that is looking for something to do, it always goes somewhere. And where it is going depends a lot on what the Fed is doing or what it is perceived to be doing. But on the other hand, money supply growth is a real data point – it hasn’t got anything to do with perception. And at the moment, **all the money supply growth that has taken place since the Fed ended QE has been credit expansion by commercial banks. And the sector in which the biggest expansion has taken place is corporate debt**. So, if we start seeing a lot of frackers defaulting and players in related industries – it’s not only the frackers, it’s all the suppliers and the suppliers of the suppliers and so on – so this is probably going to have quite a significant impact. So, then **I suppose that commercial banks will be very reluctant to continue to extend more credit to the corporate sector**. And another factor to remember: a lot of money was borrowed for financial engineering purposes, including for share buybacks, even for dividend payments, for mergers and acquisitions. And this kind of borrowing is highly dependent on perceptions of future stock prices and perceptions about how well business is going or what cash flows they’re going to generate in the future. So, there are several reasons why the growth in bank lending could actually decline. And then **if that happens, we will**

have even lower money supply growth. And in my opinion this will definitely bring a recession and possibly quite a severe bear market in stocks.

Mark Valek:

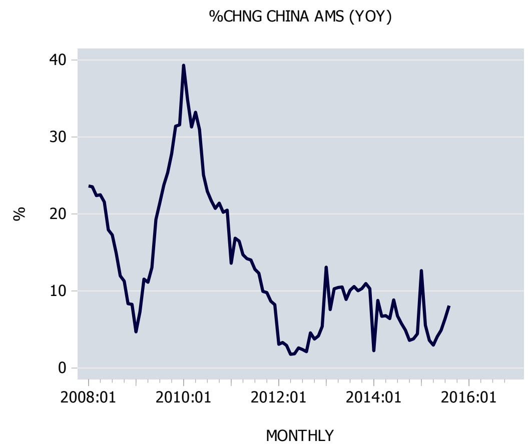
Getting back to the currency perspective – call it "currency war" or "devaluation process" – I think a very important relationship is obviously the US and China, considering they represent the biggest bilateral trading partners. We saw this devaluation in August, pretty surprising for some observers. China isn't having a great time obviously, and I think Frank was pretty accurate when he pointed out China's monetary growth numbers that began a steady decline already one to two quarters ago. So, congratulations for the accurate call! Do you have any views on this going forward? Because China is obviously immensely important for the global

economy…

Frank Shostak:

I look at the money supply for China. At the end of 2010, money supply growth in China was almost 40% year-over-year. Since then it has been falling. It almost collapsed in 2012 and is currently at about 7%. Basically, the effect from this massive rise and massive fall is still 'in progress'. And it takes a long time for the various bubbles to burst. **We'll probably see China suffering a prolonged recession – it may even be something similar to the Japanese disease, because they also resist like in Japan.** So, the world won't look too nice from this perspective. It doesn't mean there won't be any opportunities, there will of course be investment opportunities, but from a Chinese perspective, **China will have a negative effect on commodity prices. And there are countries like Australia and Canada with commodity-related currencies that probably will come under pressure**. China will also play an important role here; and likewise the development in the rest of the world, in particular in the US. **Europe may experience a certain recovery, a false recovery**

because of the money supply growth – but the real stuff is not produced by the printing press.



Source: AAS Economics Weekly Report October 5 2015

Zac Bharucha:

Concerning the China angle, I think the markets have been pretty sanguine as if somehow this whole economy can be controlled by central planners. It's an absurdity that's hanging around in the markets. But somehow these central planners have got knobs and switches with which they can restart the economy at will, and solve this massive post-crash monetary bubble that has been built. And I agree with Frank, **this could be a multi-year recession that now takes place**. You can't then flip the center and back up to the plus side so easily.

In commodities, I believe the sharpest losses are now behind us, particularly in the energy complex – oil, heating oil, natural gas. The same applies for the base metals, with the sharpest year-over-year declines behind us.

We could still get lower, because the weakened demand side has met a supply side that was increasing capacity, but at lower rates of decline. Again, this is one of the malinvestments, an obvious malinvestment area – since the whole metals, mining and energy complex received far too much investment capital due to false price signals. And that's one bust that's unfolding right before our eyes. So, **I think the idea of buying equities in the gold area could work, if gold works as an alternative currency**! But I think there are going to be plenty of bankruptcies in the listed and unlisted industrial metals sector.

Mark Valek:

Frank, I guess you are of the opinion that the Chinese will probably depreciate the renminbi further?

Frank Shostak:

Probably it won't be very much. **From my monetary perspective, China looks set to remain stable. I don't see any tendency for depreciation.** But equally – we're talking about a totalitarian state, they can also do a lot of crazy things – at the end of the day, if you start the currency depreciation train, you end up in a disaster. I don't think it will happen this way. **But a contractive depression or recession will probably hit China and all these Southeast-Asian countries.**

Ronald Stöferle:

Just one number to illustrate the incredible extent of malinvestment that probably took place. **The total amount of credit in China rose 54 times in the last two decades**. That's huge! And of course there have probably been some very positive developments, but **you don't have to be a great economist to see that there's a massive amount of malinvestment that took place due to this enormous credit expansion.** And I think that the market at the moment is very ignorant on this topic. But **I don't think that many market participants actually realize that there is just a normal credit cycle turning down in China now, and this credit cycle has probably been more dramatic than anywhere else in the world in the last few decades**. We're probably on the verge of the bust phase. So, I actually expect sooner or later the People's Bank of China to continue devaluing.

Now coming back to the currency wars, because this is obviously Jim's topic. I think it's interesting because the Fed was not participating in the currency wars recently and we have seen enormous strength especially of the dollar, and especially vs. emerging market currencies. I think it was really interesting that Yellen mentioned the emerging markets' turmoil so often in the last press conference. From my point of view, this – and also last Friday's job numbers – perhaps marked the end of this massive uptrend in the US dollar. However, on the other hand, there is already pressure being put on Mario Draghi to expand (or make it longer or bigger) quantitative easing in the Eurozone. And it seems that the Japanese, at the moment at least, kind of refuse to talk about further easing; perhaps they are taking a time-off from currency wars. How would you see that game currently developing?

Jim Rickards:

Well, **I think the Japanese have to cheapen the yen**, they don't have anything else going for them. I mean their debt to GDP ratio is well over 200%, I guess they could run bigger deficits and sell more bonds, but it seems that they're at the upper limit as to what they can do. The real solution in Japan is of course structural reform. But I don't see any of that happening. It's too culturally embedded and the Japanese don't really want to engage in these types of reforms. So, all they have is a cheap yen and the yen at the current level around 1.24 is not cheap enough to cause inflation. Because as fast as the yen depreciates against the dollar, oil prices were depreciating even faster than the yen was depreciating, so the oil price was falling even in yen terms.

So, all they got was more deflation and they are technically in a recession, so they have to do something. They have no other policy tools, so I guess they can just sort of sink into the Pacific Ocean. But even if they wanted 1% inflation, they'd have to take the yen down to 1.50 to the dollar.

As far as the US dollar is concerned, you're right that the US is not trying to get any inflation with a cheap currency. They have a strong currency, but that was based on their forecasting as I said before (they believed that the economy would grow on its own even without a cheap currency, that turns out currently not to be the case). **They need a cheap dollar!** And I also agree with you that China will devalue again, I agree with that completely – **I see China devaluing once or twice more between now and the end of March**. They might go back to a managed peg or a dirty peg, a dirty floating let's say, next March, because that's when the IMF will announce that China is included in the SDR, and they will be expected to be on their best behavior. But between now and March they can be active. As it gets closer to March, there is going to be ever more pressure to be a good actor in the international monetary arena. But for now, they have some degrees of freedom, because March is still a long way away. So, I would expect some further devaluation down in the yuan in order to get some inflation.
So if you try to cheapen the dollar, Japan's got to get cheaper because it needs the help and China would get cheaper because they actually don't care what the United States think. They might care a little bit about them on the map, but they don't care about the United States. So if the second and third largest economies in the world are cheapening and you wanted a cheaper dollar, **it'll be the Euro that will have to bear this**!

Heinz Blasnik:

I wanted to say something to Japan first. **One of the reasons why Japan has recently sounded a bit reluctant about enlarging QE further is probably the fact that**

there are no ready JGB sellers anymore. The banks want to sell beneath the inventory they have for their repo business. The large Japanese pension fund – its name escapes me now, but you know which one I'm talking about – has already shifted its allocation from JGBs to stocks and foreign investments. So, it's no longer a large seller of JGBs. So, the Bank of Japan has encountered liquidity problems in the JGB market. On some days, there is not even a single trade except for what the Bank of Japan is buying. So, presumably they're now considering what else they might buy. I'm not sure what they will come up with, because they can't buy anything. They have in fact changed the rules several times. Once upon a time, the Bank of Japan was not allowed to hold more JGBs than the amount of currency in issue – that's a rule they overthrew quite some time ago already; and a lot of other rules have been canceled over the course of the past two decades. It will be interesting to see, what else they will come up with! A possibility that occurred to me is that **the Bank of Japan might begin buying foreign securities. This would definitely cheapen the yen very quickly. So, that is one option**. That's all to the Bank of Japan.

And with respect to the euro, I tend to agree that the euro is probably going to be the one taking the strength next. Because as long as the official growth data from the Euro area is okay (and they are at the moment okay, they had something like 0.4% growth quarter-on-quarter), then the ECB doesn't really have a reason to add large QE. They're talking about it, but it's always talked about it in a sense that it's something they might do if necessary. At the moment, they can't really argue that it's necessary. So, it's probably true that, **if the yuan, the dollar, and the yen are set to become weaker next year, then it's going to be the euro that's going to rise**. And I also agree with Jim that in such a scenario we could see a pretty violent snapback in emerging market currencies.

And the same goes for commodity prices. That is something that I wanted to mention as well. Because I've seen your chart where you think about whether commodity prices might actually fall further. There are two reasons why I don't think that's necessarily going to happen, even if a globally synchronized recession sets in. One of the reasons is that the amount of money that has already been created since the year 2000 (looking at the dollar money supply as commodities are priced in dollar) has almost quadrupled from the level it had in early 2000s. Now think about the oil price for instance: the oil price bottomed out in 1998 at 10 dollar/barrel. That is a level the oil price had already seen once before: when it started rising in the early 1970s, it first went from 1.20 dollar to 11 or 12 dollar, then it corrected back to 10 dollar, that proved to be support, then it rose to 40 dollar in 1980. Then over the next 18 years it fell back to that 10-dollar-level that used to be one of the peaks in the 1970s; then in the next move it rose above the 40-dollar-level that was the high in 1980. Now what I'm thinking is that **nowadays 40 dollars per barrel of oil is roughly what 10 dollars used to be in the mid-70s and the late 90s – it's an important support level**; the region between 40 and 30, let's say. Because there's both spread and US taxes intermediate oil, they're drifting about from time to time. Sometimes you might see US taxes intermediate oil at 35, Brent is still over 40. So, that strikes me as a very, very strong support level for oil. I'm actually thinking that the next move in oil and other industrial commodities, and of course also gold, would be a retracement of some of the decline we have seen. And that could very well happen in conjunction with a weakening dollar. And it could happen regardless of economic activity, because if you think back to the 1970s – okay, we are not in the 1970s of course, there are many differences –, however, what it demonstrated: **you can have rising commodity prices even while the economy isn't doing very well. So, I would be careful with betting on that decline continuing in the short term.** For the longer term, that is something that we cannot really say; it's true that deflationary pressures are prevailing at the moment, but if central banks react the way we generally would expect them to, then this doesn't have to be the case next year.

Ronald Stöferle:

I think I haven't met a bull on oil for many months. It's actually astonishing that nobody talks about oil prices anymore, because everybody simply expects it to go sideways or get even weaker.

Frank Shostak:

I'd just like to add another point here concerning China, which is a proletarian state – they got fooled by what they earned; and false statistics – you may not even know how bad things are. On the topic of malinvestment: in the former Soviet Union, they had malinvestment for 50-60 years until the Union collapsed. **In China: as long as they have the Fed, they can continue to support malinvestment for a long time.** In freer economies, in Western economies, things would just correct much faster, they would just collapse, not like in a dictatorship like China.

Zac Bharucha:

I think you're absolutely right, but most people think China is integrated in the global trading system and are, even though there is single party rule, essentially they are just like we in the West: they understand markets, they are proto-capitalists. Well, it's an absolute load of rubbish! It's still a one-party-system, where the state wields enormous power, the politicians have enormous wealth and power, and **I believe**

that history will tell that the economic reintegration of China into the global trading system proceeded much too fast; it proceeded way ahead of the political transition and emergence into-the-global-institutions, and I think this was a huge mistake for globalization This had big implications for other countries. But that's the way global capitalism has gone: it has brought China in as a cheap producer. Goods are designed in other countries and then put together there and sent out. And I think it has just been terribly too quick the way it all happened and highly disruptive.

Frank Shostak:

Yes, I agree with that. You can actually bring another analogy here: that the Americans in particular are pressing the American model of democracy on everybody. And that backfires again and again, all the time, everywhere they try to do it in the undeveloped world except maybe for instant results. That's why American foreign policy collapses all the time.

Zac Bharucha:

Yes. As you mentioned, I don't want to stray too far from the agenda. But we should note something Europe... I think the temporary border closures are a highly significant factor in terms of the refugee crisis, because the free movement of people and capital is a key tenet of the EU. Whether these moves are temporary, or not , **I think it's evident that the EU is under strain, first with the North-South division and now with the migrant crisis**, this flow of people coming in who are desperate**. I think the EU will be under a lot of pressure in 2016.**

And as some people criticize governments in general: I have no problem with civil servants per se. If there is a right effort and ethic, the government sector has its role to play! I just think within the EU we have enormous problems.

The other thing that really concerns me is the status of Germany as regional producer/exporter, being able to sell all over with open borders has been a key benefit from open markets in the EU. Can this last? **If this EU changes shape and it starts having border controls and there is creep further away from the initial EU dream** (the humanist idea of trading and traveling within a region), **Germany would actually be a massive loser because it's very export-dependent and has a very aging population**.

Ronald Stöferle:

Actually, Germany has the lowest birth rate on earth, it's not Japan anymore.

I totally agree and I think it's interesting that you are seeing in the German equity market, that the DAX, which is showing the large caps of the multinational companies, is showing relative weakness to the small-cap indices, which are not that dependent on international trade anymore. So, I think it's one of the positions that Mark mentions quite often in his presentations that actually **this whole confidence in the German industry and the German export sector is some sort of a bubble that might pop very soon**.

Mark Valek:

I think they're just very vulnerable, because **most of the market participant view Germany just as a safe-haven-country. But this export-oriented structure of their economy makes them very vulnerable.** I think that is underestimated very much.

Ronald Stöferle:

I think one very interesting point is – and this is kind of overlooked by the media – that there was one FOMC member actually mentioning negative interest rates at their September meeting. And I think these are quite big news for the US, and it's also a position that we're actively playing in our fund with those eurodollar-options. I'm not sure if QE4 will be introduced. I would rather expect that the Fed will kind of continue mentioning the implementation of negative rates and that their verbal intervention will be going forward.

Mark Valek:

You noticed the first time that negative interest rates were mentioned on a press conference – it was a question, but it at least it appeared and surfaced for the first time in the discussion there. And what I also hear is that **Ben Bernanke on a private speech commented on the possibility of negative interest rates: He said that he was afraid of introducing negative interest rates back in 2008/09, but now he would feel more confident to do it. So, this is coming into the discussion a little bit**. But this is something that I am looking at very closely, because first they have to talk about this academically before they are actually going to implement it, I think.

Jim Rickards:

The Fed's next move will be towards ease because of the weakness in the US economy. However, it would not happen right away, I expect it in the first quarter of 2016, so **perhaps in March or April of 2016 I think the Fed will give some kind of easing.** What happened in the last 30 days is exactly what we were expecting, but I think it's come as a shock to them, because their forecasting models are different. And so they're beginning to wake up to the fact that we're going to a global depression and growth depression. But now the Fed is waking up to that, they don't do anything quickly, it's going to take a few months to digest all of this, they're going to hope that things bounce back, but I don't think that they will. Finally, I expect them by maybe the end of the first quarter of 2016 to ease.

The Fed has 5 ways to ease. A lot of people say, how can you ease when you are at zero? But they actually have five different ways to do it. The first I'd like to mention, is negative interest rates; the second one is a cheaper dollar, so back to the currency wars; the third one is helicopter money; the fourth one is reinstating some kind of Forward Guidance, which we also talked about; and the fifth one is setting up QE4. So, you have **helicopter money, Forward Guidance, QE4, currency wars and negative interest rates**. Those are the five policy tools.

Now, **I do not expect them to go to negative interest rates**, and here is why. Actually in the five things that I mentioned that might actually be the most effective one that might deliver the most powerful results. And we've seen negative interest rates in Europe (ECB) and Switzerland. But the US is different **because we have a very large money market industry**, which you really don't have in Europe, **and negative interest rates would destroy the money market industry – it's a trillion-dollar-industry**.

Well, if you put negative interest rates on the money market instruments, these funds are not going to have any money and they would have to shut down, as they really only have a few basis points to pay their expenses. I think this would destroy the industry and that's why the Fed won't do it. I actually don't think they would do QE4 either, only because it's been so discredited and of course 2016 is an election year in the United States and quantitative easing has such a bad flavor, particularly among conservatives and Republicans, that if the Fed went to QE4, they would just be putting themselves in a political crossfire. But independent of politics, the research shows that it doesn't really do anything. So, I don't think they'll go with QE.

I've heard about people's QE from a German program in the UK – people's QE is just another name for helicopter money. The problem there is that the central bank cannot do it alone, they need the corporation and fiscal authority, which in our case would be the Congress and the White House. The Congress and the White House don't even talk to each other; I see now, and again in an election-year, I see no prospects of any cooperation. So **I think we can knock down negative interest rates, QE and helicopter money for different reasons**.

That only leaves two instruments: one is currency wars, the other one is Forward Guidance. The easiest, and it would work, is Forward Guidance. It's just put back on with another word for "extended" or "patient". It doesn't matter, they'll come up with some word that tells the market: "Hey, we're not going to raise rates for the foreseeable future. As long as this world is not as good as we like it, we're not going to raise rates. If we change our minds, we'll take the word out and give you some advance warning." It will be a replay of what they did with Forward Guidance in March 2015. The reaction function there has been slaughtered. I mean, people went to do carry trades and they bought dollars, they invested in emerging markets. And to make the interest tighter, because right now all the capital is coming out of the emerging markets, but if the Fed will reinstate Forward Guidance, the capital would flow back into the emerging markets. So, you can see a very final reversal of a lot of the trends that we have been following and it's dangerous to stop. I mean, in that event all of a sudden you will see the Malaysian currency start to rally, in Korea, Asia (but probably not Brazil), if the Fed goes back to Forward Guidance. So, we have to be really careful, I would be watching them very closely.

The last one, currency wars, is another strong probability, so that's where then we just basically call it "driving" and say: "Okay, you've had a drink from the canteen, we're taking the canteen back, we need a drink" – so the US is going to cheapen the dollar. Thus, you might look for Forward Guidance and a cheaper dollar, not now, not before the quarter end, but in the first quarter of next year, if the US economy gets much worse.

Heinz Blasnik:

I'd like to add a few words to that. One thing that might actually delayed the Fed a little bit of moving to the first quarter of 2016 or maybe a little bit later, is that the CPI data are going to readjust upward a little bit in the end of the year, because the base effect from declining energy prices is going to come out of the data from October onward I believe. **We should actually see a few more elevated CPI readings over the next few months; the year-over-year readings are going to be higher**. That might also delayed that a little bit.

And I also wanted to say something about **helicopter money, because that is something that is eventually going to be done**. But in the US – and it's also the case in most other central banks' arrangements, the ECB has it even more strongly formulated in its statutes – the central bank is not allowed to buy bonds directly from the Treasury, because that would theoretically increase the potential for money supply inflation by a multiple of 10. So, if they do something like that, it's going to be very similar to QE. I think they're going to do it through intermediaries again, so the primary dealers – so, such an agreement, if it comes into being, is probably going to be an informal one.

Then I also wanted to say something about the currency war situation. China, as you rightly said, had its monetary policy basically outsourced. And I think for a while they were okay with that, because (it was discussed last time) they wanted the yuan to become a member of the SDR basket. And there were probably also other objectives that they wanted to achieve. One of them is that they get the congress off the neck if they think they aren't strong. The other is that **the new Chinese leadership planned to reorganize the economy. They want to lead the economy out of its "heavy industry and real estate and so on"-orientation toward a more consumer-oriented economy**. They were probably fine with putting some pressure on these industries that are now in trouble. But I think now that trouble has become too big. **Now there seems to be a great danger of a credit crisis in China that will be really difficult to control. I would actually expect it to weaken the yuan further. So, in other words: I would expect it to do whatever it takes to running an independent and looser monetary policy again.**

Ronald Stöferle:

I think, to sum up it would be really interesting to hear your concrete investment ideas for the last quarter but also going into 2016. Frank, perhaps from your side based on your research on monetary aggregates of course; and Zac, from your side based on your technical analysis, sentiment analysis and intermarket analysis.

Frank Shostak:

From my view, **we are at a stage where the so-called bubble cycle is accelerating right now**. At this stage **I would still prefer to have a reasonable weight in treasury bonds. I would probably have certain positions in stocks. I would probably stay away from commodities and commodity-related stuff. And probably more than just a little bit of cash**. That'd be my suggestions for the next quarter.

Jim Rickards:

I think it's an in any case good entry point for gold. I know it has been tough for years, but all good things come to an end and this bear market in gold might be over. So, I do like the entry point for gold! And my favorite trade are 10-yr Treasury bonds.

Heinz Blasnik:

Well, I'm actually doing the same. **I focus on gold and gold mining stocks and also some Treasury bonds. One could also consider here Russian stocks** – I'm saying that again, last time it was a little bit too early.

Ronald Stöferle:

I think one interesting fact that we watched very closely recently is the fact that the gold-silver ratio, which we are following also for our Inflation Signal, was falling quite dramatically. So, **in the last few days silver actually outperformed gold significantly, which is also a very good confirmation indicator not only for gold itself, for the validity of the uptrend, but also for the mining stocks.**

Zac Bharucha:

And from my side, as I said, **I think there'll be another sharp move down in the stock markets imminently. I mean really imminently! And then a rally into year end, but not a very strong rally – we might end the year at the levels where we're up right now at best**. And **in 2016, I think stock markets will trend lower**. I think gold based out and put in a nice low. Concerning currencies, **I think you can play around with currencies for short-term moves, but I can't see any strong trends between the paper currencies**. I think gold is going to reemerge. And I agree also regarding the commodities: you can also pick, but I think although the strongest momentum on the downside is already behind us, I wouldn't be surprised if the lows are revisited. So, **you've got to look at tactical moves in the commodities and commodity stocks, but not view them as long-term holdings because of the macro picture that I'm looking at**! And I think we remain on the edge of chaos – **the world is on the edge of chaos – political and economic chaos! It will remain like this.**

Ronald Stöferle:

That's a very positive end, Zac! *(laughs)*

Appendix A: Members of our Advisory Board:

Zac Bharucha

Zac began his career in finance at the investment bank Kleinwort Benson and later became an equity portfolio manager at Philipps and Drew Fund Management. He then moved to AMP Asset Management where he was responsible for managing more than GBP 1bn of institutional assets. Afterwards, he moved to M&G in London. Since 1998, he has developed absolute return strategies and specialized in equities and commodities. After 25 years in asset management, he retired from professional life in 2011 and wrote his first book about market timing.

Heinz Blasnik

Heinz is an independent trader and market analyst for the consulting firm Hedgefund Consultants Ltd, as well as a regular publisher for the Independent Research House Asianomics in Hong Kong. Heinz primarily is responsible for his blog www.acting-man.com, on which he analyses developments in the financial markets from an Austrian point of view.

James G. Rickards

Jim is the author of the international bestsellers *Currency Wars* and *The Death of Money: The coming collapse of the international monetary system*. He is portfolio manager at the West Shore Fund. During his career, Jim has held senior positions at Citibank, Long Term Capital Management and Caxton Associates.

Dr. Frank Shostak

Frank is chief economist at AAS Economics. He has over 35 years of experience as a market economist and central bank analyst. He holds a PhD, MA and BA honours from South African universities. He was professor of economics at the Witwatersrand University in Johannesburg. He is one of the world leaders in applied Austrian School of Economics and an adjunct scholar at the Mises Institute in the US.

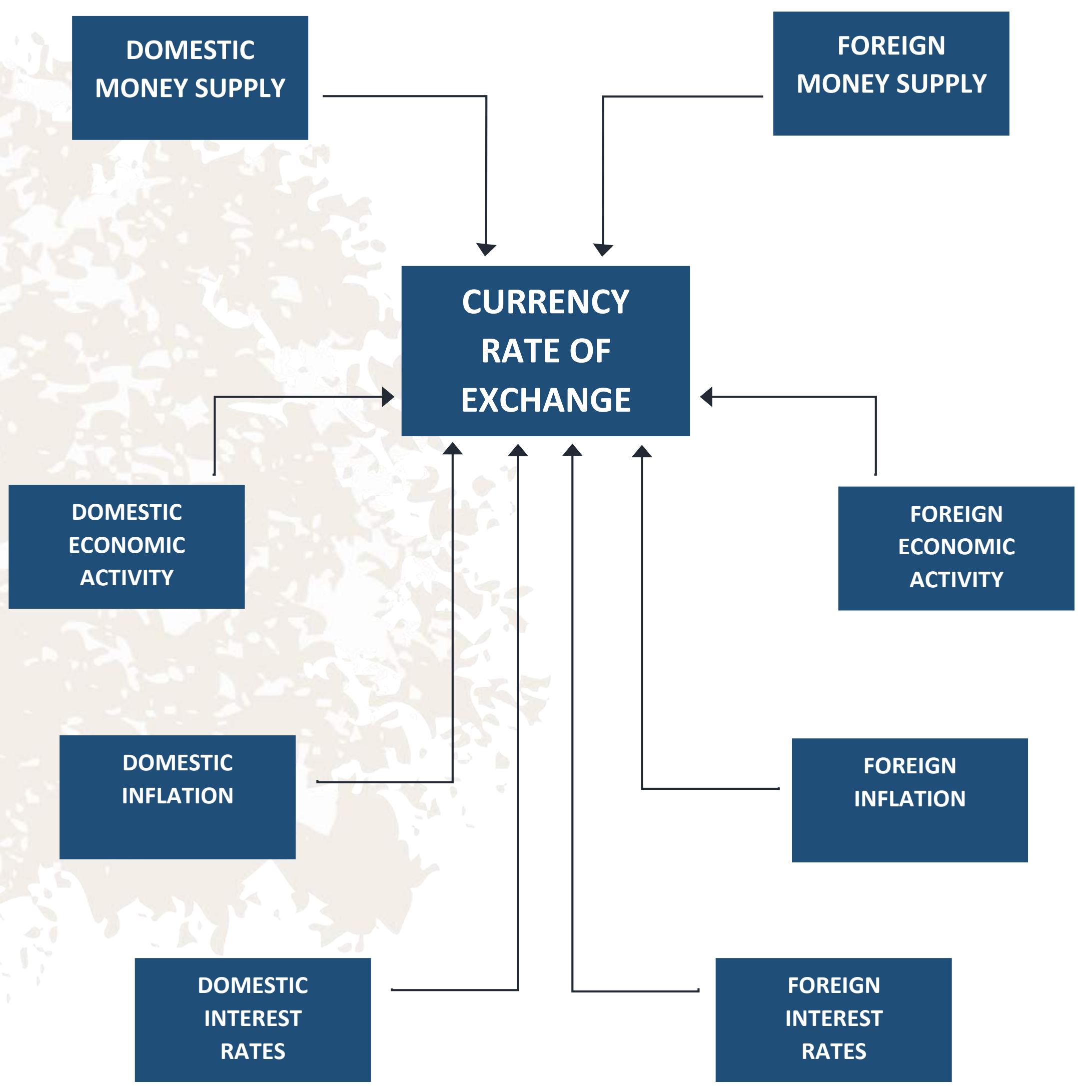
Rahim Taghizadegan

Rahim is the founder and director of the institute for value based economics, an independent research institute in economical and philosophical issues in Vienna. He is bestselling author and a popular speaker internationally. Rahim studied Physics, Economics and Sociology in Vienna and Lausanne. He has worked in the fields of economics, space research and journalism. He has also taught at the University of Liechtenstein, the Vienna University of Economics and Business Administration and the Universität Halle an der Saale.

Appendix B: AAS Economics: Currency exchange rate determination model:

Within the framework of our large scale econometric model the key variable that drives a currency rate of exchange is the relative money supply rate of growth. Over time, if the rate of growth of money supply in country A exceeds the rate of growth of money supply in country B then that country's currency rate of exchange will come under pressure versus the currency of B, all other things being equal. Whilst other variables such as the interest rate differential or economic activity also drive the currency rate of exchange, they are of a transitory and not of a fundamental nature. Their influence sets in motion an arbitrage that brings the rate of exchange in line with the influence of the money growth differential.

Flow chart of currency exchange rate determination

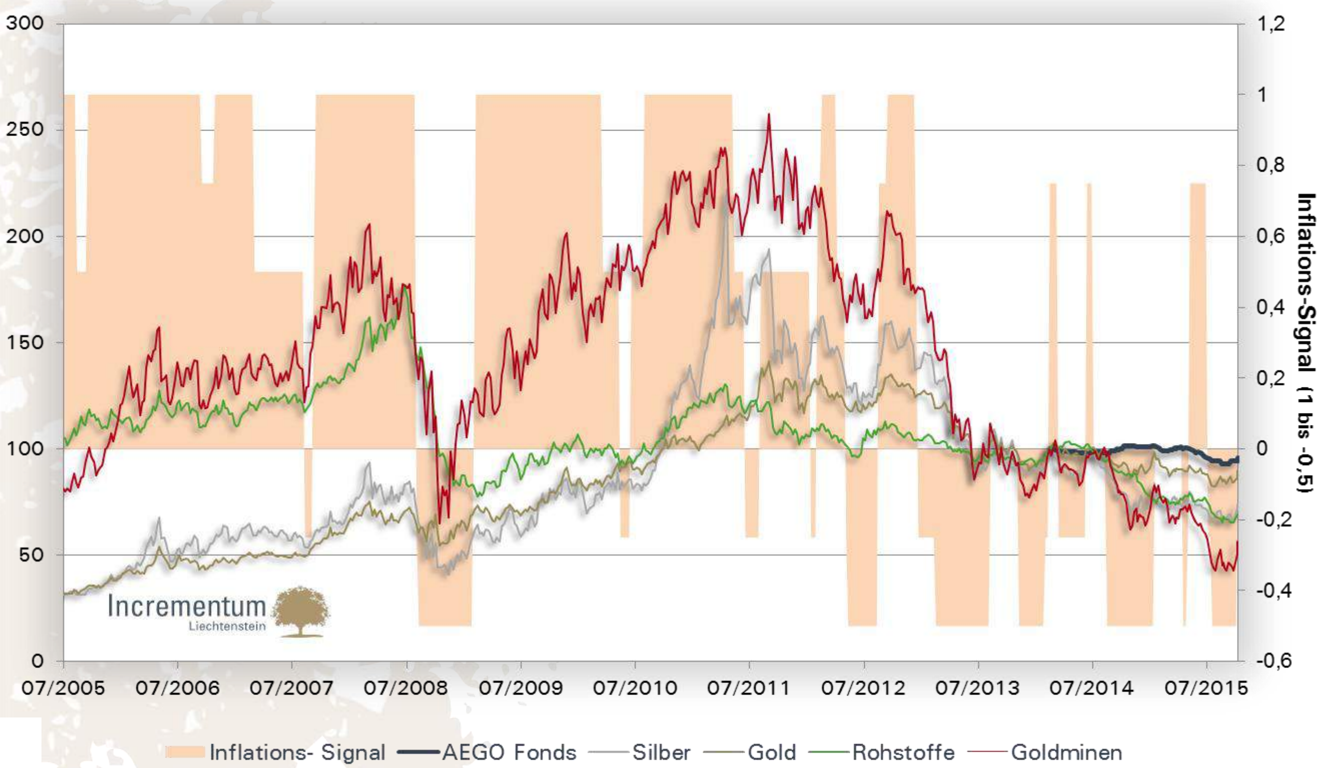


Incrementum Inflation-Signal

At Incrementum, we are convinced that inflation is a monetary phenomenon. Because of the dynamics of "monetary tectonics", inflationary and deflationary phases can alternate. **To measure how much monetary inflation actually reaches the real economy, we utilize a number of market-based indicators** - a combination of various quantitative factors including the Gold-Silver Ratio - which result in a proprietary signal. This method of measurement can be compared to a "monetary seismograph", which we refer to as the **"Incrementum Inflation Signal".**

In the fund we manage, our Incrementum Inflation Signal gauges the inflation trend and we position the fund accordingly. Historically, we observed periods of between 6 and 24 months during which disinflationary forces were dominant. These phases were particularly painful for the holders of inflation sensitive assets. Right now it looks as disinflation might continue for a while. **Our inflation seismograph triggered a "falling inflation signal" in August.**

Inflation sensitive Assets and the Incrementum Inflation Signal



Source: Incrementum AG

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