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Fed's Hot Air Could Lift Gold

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For gold, dollar strength overshadows geopolitical maelstrom

The cycle of rising geopolitical risks continued, driving gold to its $1,807 per ounce monthly high on August 10 as China conducted military exercises over and around the Taiwan Region. The show of force was unprecedented. In a Wall Street Journal op-ed, Hal Brands and Michael Beckley argue that China's new military capabilities, combined with the mid-2020's lull in American military power, brings an opportunity for China to reclaim the Taiwan Region. According to the RAND Corporation, one year of fighting over the Taiwan Region would reduce America's GDP by 5% to 10% and China's by 25% to 35%. Logic suggests the human suffering and economic costs of an attempt to force unification are prohibitive. However, many also thought Russia would never attack Ukraine…

Gold trended lower for the rest of August, finishing at $1,711.04 for a $54.90 (3.1%) loss. On August 15, China reported retail sales, industrial output and jobless rates that were all below expectations. This caused a selloff in commodities, including gold. Gold was also pressured by the U.S. dollar, which reached new twenty-year highs on August 29. The dollar gained strength as U.S. Federal Reserve Bank (Fed) Chairman Powell signaled the Fed is poised to continue raising rates and may keep them higher for longer in order to battle inflation

Average Annual Total Returns (%) as of August 31, 2022

	1 Mo†	1 Yr	5 Yr	10 Yr
Class A: NAV (Inception (2/10/56)	-8.04	-26.59	-0.38	-4.71
Class A: Maximum 5.75% load	-13.33	-30.81	-1.56	-5.27
GDMNTR Index	-8.78	-25.28	0.61	-5.62

Average Annual Total Returns (%) as of June 30, 2022

	1 Mo†	1 Yr	5 Yr	10 Yr
Class A: NAV (Inception (2/10/56)	-13.44	-21.98	3.04	-2.60
Class A: Maximum 5.75% load	-18.41	-26.46	1.83	-3.17
GDMNTR Index	-13.80	-17.35	5.76	-3.63

Source: VanEck

The performance data quoted represents past performance. Past performance is not a guarantee of future results. Investment return and principal value of an investment will fluctuate so that an investor's shares, when redeemed, may be worth more or less than their original cost. Performance may be lower or higher than performance data quoted. Please call 800.826.2333 or visit vaneck.com for performance current to the most recent month ended.

The "Net Asset Value" (NAV) of a Fund is determined at the close of each business day, and represents the dollar value of one share of the fund; it is calculated by taking the total assets of the fund, subtracting total liabilities, and dividing by the total number of shares outstanding. Investors should not expect to buy or sell shares at NAV.

† Monthly returns are not annualized. Please note that precious metals prices may swing sharply in response to cyclical economic conditions, political events or the monetary policies of various countries.

Expenses: Class A: Gross 1.34%; Net 1.34%. Expenses are capped contractually until 05/01/23 at 1.45% for Class A. Caps exclude acquired fund fees and expenses, interest, trading, dividends, and interest payments of securities sold short, taxes and extraordinary expenses.

Gold stocks seem to have largely priced in rising costs

Second quarter reporting concluded in August and it wasn't pretty. Companies were hit by the combination of falling metals prices and rising costs—leading to earnings misses and cost revisions. Most companies moved cost expectations to the upper end of guidance or revised them higher. We don't fault the companies because most of the cost pressures are out of their control. A war in Ukraine wasn't factored into anybody's guidance in January. Fuel, energy and consumables that are tied to the petrochemical chain are some of the main cost drivers. Another is tight labor, which is a global phenomenon. Original company guidance called for 3% to 6% 2022 cost inflation, but those estimates have doubled and all-in sustaining costs now average around $1,200 per ounce. Margins remain healthy enough to support dividend policies and many companies continue to buy back stock. The uncertainty of how long this rising cost environment will last appears to be largely priced into gold stocks, as the NYSE Arca Gold Miners Index[1] (GDMNTR) underperformed gold by 15.5% in the second quarter. During August, GDMNTR fell another 8.7% and the MVIS Global Junior Gold Miners Index[2] (MVGDXJTR) declined 11.7%.

Inflation Reduction Act = Inflation Induction Act?

EInflation decelerated in July as the U.S. Producer Price Index[3] pulled back to 9.8% and the U.S. Consumer Price Index[4] to 8.5%. Hardly cause for celebration, but perhaps it signifies that the peak has passed. Congress passed the Inflation Reduction Act in August. No celebration warranted there either, as the Act's components have us wondering if it might actually stoke further inflation. The bill raises taxes on corporations, which are typically passed on to consumers in the form of higher prices. The bill funds more IRS audits, raising compliance costs for taxpayers. The bill has a number of green energy credits and perks. While this may benefit the environment, green energy costs more than fossil fuels and increases demand for metals, keeping upward pressure on prices. In addition, while the administration claims that the Inflation Reduction Act's lowers deficits can decrease inflation, the last four bills passed by the Administration along with student debt relief will combine to substantially raise the budget deficit.

Inflation is driven by excess demand and/or a lack of supply. Congress and the Administration can address the supply side by enabling companies to produce goods and services more cheaply with incentives to invest in capital, capacity and technology. This comes from reducing taxes, reducing regulations, job training and immigration policies that bring in high quality workers. None of this is found in the Inflation Reduction Act.

Fed balancing act keeps gold waiting in the wings

The Fed can try to control inflation on the demand side by increasing rates and quantitative tightening, which slows economic growth. However, based on the experience of the seventies, the current slow rate of Fed tightening may not be sufficient to return inflation to its two percent target. There might also be a limit to how high the Fed is willing to hike rates. As the Fed raises rates, it must also increase the interest it pays on the trillions of dollars it holds for commercial banks and other depository institutions. As the targeted Fed Funds rate (currently 2.5%) rises above 3%, the interest it pays will exceed the revenue gained from its portfolio assets. In a recent Wall Street Journal op-ed, Judy Shelton estimates a Fed Funds rate of 3.25% to 3.5% would cost the Treasury $195 billion annually to fund the Fed. The Fed might find increasing political pressure to stop raising rates as costs mount. In addition, at the recent Jackson Hole conference, Jerome Powell said, "While higher interest rates, slower growth, and softer labor market conditions will bring down inflation, they will also bring some pain to households and businesses". Will the Fed abandon its inflation fight if the "pain" becomes unbearable?

Last year the Fed said inflation was "transitory" and now Mr. Powell is saying it is a long-term problem. So far, the markets are more concerned with rising rates than they are about inflation. We believe that at some point the markets will lose patience with the Fed's talk and see that inflation is indeed out of control. Such an awakening would benefit gold, and the gold miners cost pressures might be more than offset by a rising gold price.

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All company, sector, and sub-industry weightings as of August 31, 2022 unless otherwise noted.

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[1]NYSE Arca Gold Miners Index (GDMNTR) is a modified market capitalization-weighted index comprised of publicly traded companies involved primarily in the mining for gold. [2]MVIS Global Junior Gold Miners Index (MVGDXJTR) is a rules-based, modified market capitalization-weighted, float-adjusted index comprised of a global universe of publicly traded small- and medium-capitalization companies that generate at least 50% of their revenues from gold and/or silver mining, hold real property that has the potential to produce at least 50% of the company's revenue from gold or silver mining when developed, or primarily invest in gold or silver. [3]The U.S. Producer Price Index (PPI) represents the average movement in selling prices from U.S. domestic production over time and is typical utilized as a measure of inflation based on input costs to producers. [4]U.S. Headline Consumer Price Index (CPI) is a measure of the average change in the price for goods and services paid by urban consumers between any two time periods. It can also represent the buying habits of urban consumers.

Index returns are not Fund returns and do not reflect any management fees or brokerage expenses. Certain indices may take into account withholding taxes. Investors cannot invest directly in the index. Index returns assume that dividends have been reinvested.

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