ISIN: LU0344810915/ WKN: A0ND6Y/ BLOOMBERG: SUNARES LX / WWW.SUNARES.COM

Patience is bitter; but the fruit is sweet!"
Rob McEwen CEO McEwen Mining

Money Printing Kicks Off Again

We have said for a long time, in this report, that central banks will continue to crank up the printing presses to increase the monetary base so as to avoid the pain of a deflationary collapse. After all, central bankers are only human and human nature means that we all like the easy option. More easing/ stimulus was always inevitable in our view. Quantitative easing (QE) has become the accepted route to attempt to stimulate economies even though it has not been able to boost the global economy so far. Will this time be any different? The main thing that can be said in defence of QE is that economic hardship and collapse would have already occurred if monetary easing had not happened, so QE is the policy that pushes the structural problems further into the distance. The world is not yet ready to accept that the current system is reaching breaking point and will need to be reset at some point – the reset therefore lies ahead of us.

The real surprise from the massive and unprecedented central bank stimulus is the position that the US Federal Reserve has taken, as they are following on from the head of the European Central Bank, Mario Draghi's comments about doing *"whatever it takes"*. The Fed is, in fact, taking QE further than anyone expected at this point, a sign that things are worse than we feared. The relevant part of the statement from the Federal Reserve follows:
"The committee is concerned that, without further policy accommodation, economic growth might not be strong enough to generate sustained improvement in labour market conditions….If the outlook for the labour market does not improve substantially, the committee will continue its purchases of agency mortgage-backed securities, undertake additional asset purchases and employ its other policy tools as appropriate."

The Fed intends to buy US$40bn of mortgage security debt every month from now on and they also extended the period for zero interest rates by six months to the middle of 2015. It should not be forgotten that Operation Twist, where the Fed sells shorter-dated securities and buys longer-dated papers, is also continuing, so this increases the Fed's longer term bond holdings by some US$85bn every month. The market is already speculating that the Fed will move on from mortgage papers and get going with a Treasury paper purchase programme soon. In other words, full debt monetisation. With tax receipts falling and spending continuing unabated this should not come as any great surprise.

Of course, QE has benefitted the banking sector more than any other and this round will be no different from the rounds that have gone before. Investors, however, should take careful note of these facts:

1) The latest QE programme is open-ended. This means that the Fed can adjust policy and introduce new measures as they see fit without all the speculation that has surrounded QE3. There may never be a QE4 or 5 announcement, as they have afforded themselves flexibility to do what they deem necessary.
2) The last part of the statement mentions the possible use of *"other policy tools"*. This could see the Fed buying whatever they see fit to keep the economic ball rolling.

It means that the bank is now all-in and fully committed to the path it has taken and there is likely to be an acceleration in the scale and types of measures used from now on. The significance of this policy announcement should not be underestimated and it will have far-reaching consequences for all markets.

If readers are in any doubt about the path the Fed has taken we offer the following 2 charts of 803 years of inflation – no prizes for guessing when the Fed was founded!

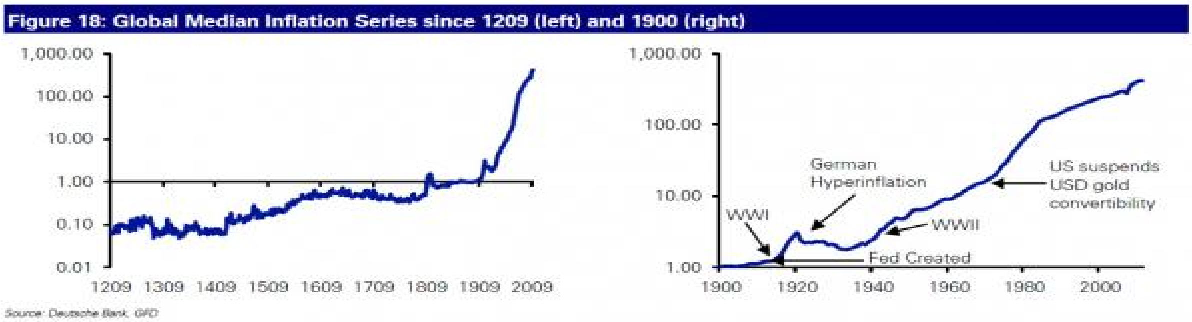
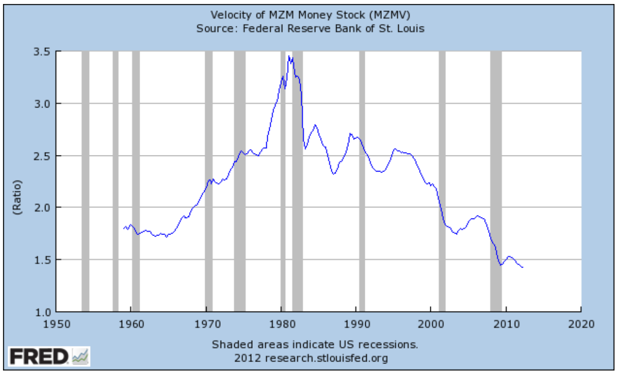


Figure 18: Global Median Inflation Series since 1209 (left) and 1900 (right)

Source: zerohedge, Deutsche Bank

For anyone confused as to why the central bankers have been so active and accommodative with monetary policy over the last few weeks need only look at a chart of the velocity of money:



Source: St Louis Federal Reserve Bank

Velocity is a ratio of nominal GDP to a measure of the money supply. It can be thought of as the rate of turnover in the money supply-that is, the number of times one dollar is used to purchase final goods and services included in GDP.

Until the velocity of money turns higher, policy is going to remain loose. The danger is of course that when it does pick-up it will turn very quickly and will be difficult to control. With commodity prices (food in particular) increasing again how far are we from this turning point?

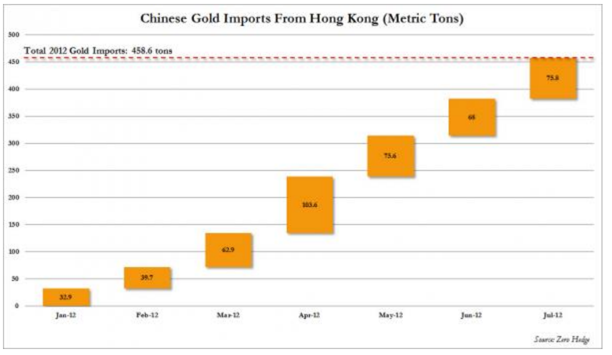
Jeffrey Lacker of the FOMC was a lone dissenting voice and was not in favour of further stimulus. He said about additional QE:

"I dissented because I opposed additional asset purchases at this time. Further monetary stimulus now is unlikely to result in a discernible improvement in growth, but if it does, it's also likely to cause an unwanted increase in inflation.... Channelling the flow of credit to particular economic sectors is an inappropriate role for the Federal Reserve."

The lone voice of reason in Europe comes from the seat of hard money, the German Bundesbank and their head Jens Weidmann. He compares the current path with the scene in the play Faust - when the devil (Mephistopheles) 'disguised as a fool', convinces an emperor to issue large amounts of paper money - which solves the kingdom's financial problems in the short-term but ends rather badly in rampant inflation. However, a lone voice is often drowned out by the noise from the crowd…

Gold As Money

We wrote in last month's report about the amount of gold purchased by China in the first part of the year and we can update this picture with the news that China's gold buying has picked up in pace. In the first seven months of 2012 alone, China has imported nearly as much gold as the *total* holdings of the European Central Bank. There is little doubt that China will have imported more gold in 2012 than the ECB's entire official 502.1 tons of holdings. To place this into some sort of context, gold buying is now replacing buying of US treasury bonds and is about twice the level of US treasury bonds bought this year. Paper is being usurped by gold as real money…



Billionaire Update

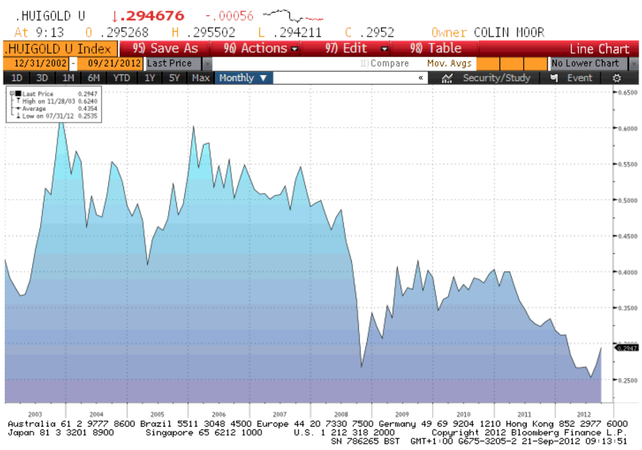
Frank Giustra is a successful mining entrepreneur who is also involved in the film industry and his success makes him worth listening to. He has also been a bull of precious metals since 2002 when he wrote *"A tarnished dollar will put the shine on gold"*. We watched an interview with him and it is well worth taking the time to listen to his opinions on what is happening today. The interview can be accessed at the following link: http://www.youtube.com/watch?v=9o30gNfPq_k

He remains a bull of gold but he also points out the cheapness of many of the underlying companies mining gold and silver:

"People usually connect irrational and stupid market behaviour with peaks of markets, but it takes place at the bottom of markets too. And it's just as bad [at bottoms] … fear is a much stronger emotion than greed, so the sense of hopelessness some people might have about the resource sector right now is something that you know if you're logical about it, it will change. It's not going to stay like this forever. If you lose complete faith, you just have to give your head a shake. [There are] companies developing world-class assets trading at pennies on the dollar."

ISIN: LU0344810915/ WKN: A0ND6Y/ BLOOMBERG: SUNARES LX / WWW.SUNARES.COM

The following charts show what he means by comparing the price of gold with the price of the HUI Amex Gold Bugs Index. It is clear that the shares have not kept pace with the price of gold and this highlights how cheap some of the major mining companies are currently. The mid-tier and junior companies operating in this sector are even cheaper. It is likely that this value will attract buyers and the gap in valuation will shrink as the bull market in gold and silver develops.



HUI/ gold ratio monthly chart Source: Bloomberg

HUI/ gold ratio weekly chart Source: Bloomberg

Corn

We all know how important oil is to the global economy but few people appreciate how important corn is and how widely it is used. In fact the National Corn Growers Association lists 4,200 separate uses of corn from aspirin to stamps. A large part of corn produced currently ends up as ethanol (which has questionable economics, a whole separate topic) but corn also goes to produce packaging that is bio-degradable unlike bottles that are petroleum based. One of the most important uses of corn is in livestock feed, a source of food that goes back to the 16th century.

.

However, recent prices have shot higher, which raises questions about the cost of production for meat and a whole string of products that rely on corn. Weather patterns in 2012 have been unhelpful to food production, with drought in the US and crops being impacted by weather patterns in Brazil, China and Australia. In addition to this inventory levels before entering the growing season were at historically low levels and the subsequent lower harvests mean that prices for agricultural commodities have been on the increase across the board.

Farming has long been a tough way to make a living and this is reflected in America where the average age of a farmer is around 58 years of age. As the world's need for food increases, and as population continues to expand, it is obvious that farming needs to be a profession where it is possible to forge a decent living, as the world needs farmers. A recent blog post on the SUNARES website shows that there are signs of the shift starting to happen in the mining world with graduates from Harvard stepping into average salaries of US$54,100 compared to average starting salaries for graduates of the South Dakota Mining and Technology University of US$56,700. Bear in mind that the cost of a Harvard degree comes at about four times the cost of the fees at South Dakota. This shift also needs to happen in agriculture and this will only be the case if agricultural prices go up to a point where good money can be made.

U.S. Deputy Secretary of Agriculture Kathleen Merrigan says: *"If we do not repopulate our working lands, I don't know where to begin to talk about the woes. There is a challenge here, a challenge that has a corresponding opportunity."*

Matt Rush, director of the New Mexico Farm and Livestock Bureau, spoke in April in California at a conference for young farmers and ranchers and he summed up the situation:

"I truly believe we're at a golden age of agriculture. Global demand is at an all-time record high and global supplies are at all-time record lows. Production costs are going to be valuable enough that younger people are going to have the opportunity to be involved in agriculture."

For those readers who are looking at career choices we recommend that you consider farming. The respected commodity investor Jim Rogers said back in 2009:

"Agricultural commodities are the place to be in for investors," and he also said that it will be farmers and not bankers driving Ferraris in the coming decade

SUNARES
SUSTAINABLE NATURAL RESOURCES FUND

ISIN: LU0344810915/ WKN: A0ND6Y/ BLOOMBERG: SUNARES LX / WWW.SUNARES.COM

Hardware is Dead

We were recently forwarded a very interesting article about China's centre for producing leading electronic products in Shenzen and the visit that the author of the article made to the electronic shopping centre in the city's nearby Hua Qiang district. He went specifically to see what sort of tablets were on offer and at what price. After all, the tablet market is growing rapidly with the iPad, Amazon's Kindle and so on.

The shock is that he was able to find a tablet for the equivalent ofUS$45 without having even haggled the price for it! He bought one as a trial and was amazed to see that it ran on the latest Android 4.0 Ice Cream Sandwich, Wifi connected, 4GB of memory, expandable memory, touch-screen and front facing camera.

There are two key thoughts about this – firstly there is very little margin at these prices so hardware producers are under threat. Secondly, and perhaps more importantly, it means that the world will see huge growth in the availability and use of tablets in all sorts of places from schools to restaurants, in fact almost anywhere. The author estimates that these tablets will ship between 20 and 40 million units this year so the hardware revolution is about to take off! This could be a development that helps fuel productivity and growth as well as giving people greater flexibility in the location and means of connecting to the web.

Click here in order to read the full article:
http://venturebeat.com/2012/09/15/hardware-is-dead/

We look forward to receiving any feedback you have and to being in touch again soon.

With kind regards from the SUNARES team,

Colin Moor