MILESTONE BULLION SERIES - I

- Investment Opportunities into Bullion Companies
- Reliable Hedge against Inflation

MILESTONE
PRIVATE EQUITY ADVISORY

Milestone Bullion Series – I: A Synopsis

Series Synopsis		as on 1st October, 2013
Commitment Received		₹ 330 Cr
Corpus Received		₹ 330 Cr
	Original Holding	Current Holding
Net Corpus Invested in OFCDs of Portfolio Companies linked	₹ 315 Cr	₹ 191 Cr
– Physical Gold (through Gold Deposit Scheme)	₹ 87 Cr	₹ 5 Cr
– Physical Silver	₹ 131 Cr	₹ 101 Cr
– Capital Protected Gold Linked Debenture	₹ 97 Cr	₹ 85 Cr

Market Snapshot

Bullion prices saw a sharp rally in the third quarter after setting their two year lows in the month of July. Gold and Silver prices spiked by 25% and 35% for a brief period before consolidating near Rs 29,000/10Gms and Rs 49,000/Kg respectively. This rally came as U.S. Fed announced a delay in its widely expected trim back of the bond purchase program which prompted investors to hedge against inflation.

Most industrialized economies are reporting slow but steady growth after a season of debt crisis and local recessions. This could lead to lesser investment demand for bullion. However, industrial and consumer demand of these metals should be able to provide a fair support for the prices. Other than the U.S. debt ceiling deadline which could again spur a safe-haven demand for bullion metals, traders around the world will be closely following the Federal Reserve policy meeting later this month for clues on whether the U.S. central bank will begin trimming its stimulus this year.

Quarterly Activity

Bullion prices have been registering the kind of volatility which is unprecedented for the metals that boasts as a safe-haven investment instrument. This phenomenon in particular demands that traders and investors around the world to become opportunistic in their investments decisions.

The recent sharp rally in bullion prices provided a timely opportunity for fund managers to liquidate yet another tranche of the physical Gold and Silver holdings. Proceeds from the liquidation have been processed and passed on to the investors in from of the fourth payout in September. Valuation reports for the same have also been sent out. The portfolio managers will continue to monitor the bullion markets actively and will systematically liquidate the remaining assets based on prevailing market conditions.

Key Communications & Future Strategy

The fund managers have liquidated a significant proportion of the physical metal holdings till date. However, to accommodate the maturities in GLDs and a systematic liquidation of remaining physical stock, fund will be exercising the option of 1 year extension.

Gold Linked Debentures (GLD) held by the portfolio companies will see their maturity starting as early as in October and will continue through the remaining life of fund. The proceeds from the same shall be passed on to investor along with the proceeds of quarterly liquidation of physical investments

Unlike Gold, Silver has not been able to attract much of safe haven demand in recent months, however slowly but surely improving economic data from around the world, a stable ETF outlook and historically high Gold/Silver ratio suggest that silver prices could turn around in near future as the investment demand picks up again. Fund managers would be looking for such opportunities and will follow a systematic liquidation plan for exit from physical metal holdings.

Major Economies Slow on Recovery – Outlook Brighter for Emerging Markets

In its latest global economic snapshot, the IMF cut its world growth forecasts and now expected global output to expand at just 2.9 percent this year, down from its July estimate of 3.1 percent. However, it sees a modest pickup in next year to 3.6 percent. The United States is currently driving much of the global recovery in terms of gross output but the IMF forecasts showed that emerging markets will be constituting much of the global growth, with their economies forecast to expand nearly four times as fast this year as advanced economies.

In United States, the political deadlock and partial government shutdown have left the world pondering over a possibility of seemingly unlikely default on its debt should the government fail to raise the nation's $16.7 trillion borrowing limits. This has led to a downgrade of the U.S. credit rating "AA+" from "AAA" by Standard & Poors. The outlooks from Moody's and Standard & Poor's, the only agency so far to have lowered its rating on U.S. debt, are both at "stable," but Fitch Ratings has indicated a negative outlook for the U.S. debt rating.

If there is a silver lining to this whole fiscal fiasco, it's that the Federal Reserve could see fit to wait even longer before reducing its bond buying from $85 billion a month. The Fed had surprised financial markets last month when it voted to maintain its $85 billion monthly pace of bond purchases, saying it wanted to see more evidence of solid economic growth.

In Europe, a better mood more than any change in policy lifted core economies such as Germany and France, and even Italy and Spain should edge into positive growth territory next year. EU officials hope that recovery of Ireland's economy may mark the beginning of the end of the euro zone's debt problems. However as International Monetary Fund has said, the euro zone must still address financial fragmentation, improve the health of banks, and move closer to banking union, as the IMF has urged in past reports.

The Chinese government officially opened a new free-trade zone in Shanghai that is long on promises and short on details about how it will boost the economy. Among other features, the zone is supposed to make it easier for foreign companies to open businesses that ordinarily are restricted to Chinese companies or joint ventures. In all, 18 industries are to be liberalized. Chinese economy grew at an annual rate of 7.6 percent in the first half of 2013, slower than 7.7 percent last year.

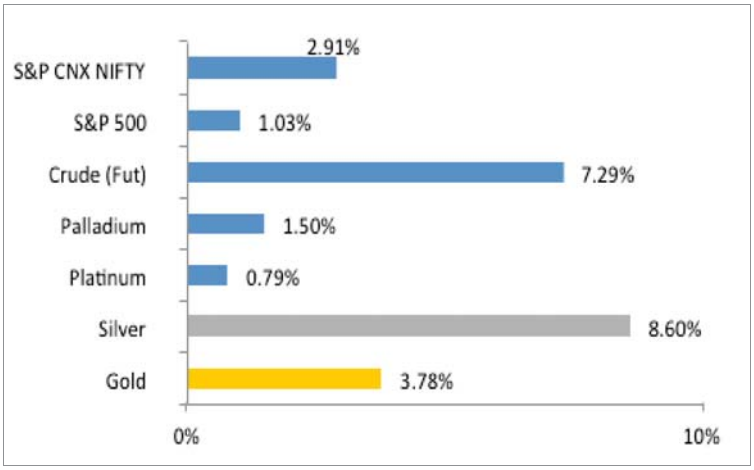
RBI Scrambled to Contain Ballooning CAD Crisis - Rupee under Pressure

Uncomfortably high inflation coupled with supply constraints is impacting India's annual growth that has slowed to 4.4 percent in the April-June quarter this year. This may explain why Raghuram Rajan, the new governor of Reserve Bank of India (RBI), raised the benchmark repo rate by 25 basis points to 7.5 percent in his maiden policy decision. The RBI has also reduced the marginal standing facility (MSF) rate to 9.50 percent, which makes borrowing cheaper for banks. Since mid-July, the MSF is being widely viewed as India's effective policy rate.

India's ballooning CAD crisis seems to be gradually coming under control under the policy measures put in place by RBI. A sharp decline in gold and silver imports has played a significant role in reigning down this deficit crisis. So far, in 2013, the government and Reserve Bank of India (RBI) have taken aggressive measures to curb gold imports. The RBI restricted them on a consignment basis by banks. A transaction tax of 0.01% was imposed on non-agricultural futures contracts including precious metals. India's biggest jewellers' association asked members to stop selling gold bars and coins, and the import duty on gold was raised to 10%.

The rupee slumped to its new record lows near 69 to the dollar lat in August on growing worries that foreign investors will continue to sell out of a country facing stiff economic challenges and volatile global markets. The pummeling in markets sent the rupee reeling 3.7 percent to an all-time low of 68.85. In absolute terms too, the 256-basis-point fall in the rupee was the biggest ever. However, Rupee has since recovered nearly 11% as RBI governor Raghuram Rajan introduced measures to stem the slide. The currency also received help from Federal Reserve chief Ben Bernanke when he announced postponing of the tapering (its liquidity infusion) program.

Quarterly Movement in Commodity Prices
(Crude and Silver gained on better Economic Outlook)

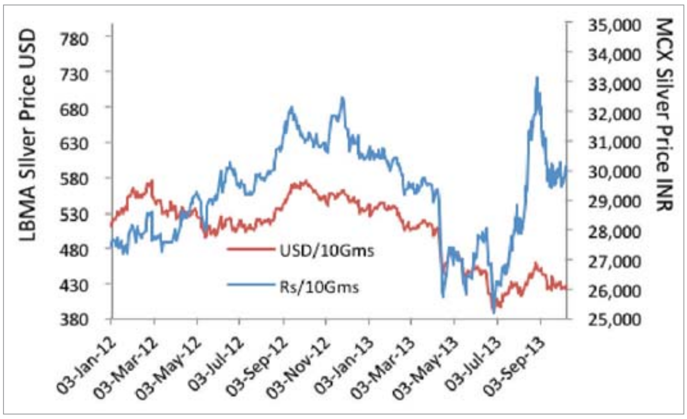


Source: Bloomberg, Internal Research

Gold: Performance and Future Outlook

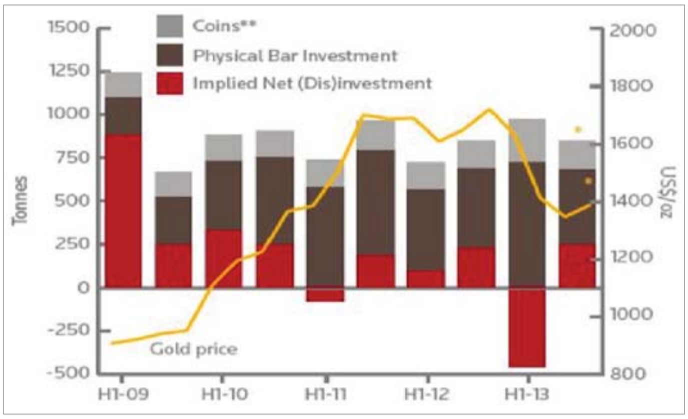
After the rebound to $1,433.95/oz on 28th August, from a low of $1,180/oz on 28th June, a move of 21.5 percent, prices spent September consolidating. The yellow metal was trading at $1309.5/Oz on October 9th. After the August high, prices dropped back to a low of $1,291.40/oz, before stabilising above $1,300/oz. There was a brief spike up to $1,375.65/oz following the FOMC's decision not to start tapering its bond purchase program, but prices soon fell back again into consolidation mode.

Gold under Consolidation after a Short-lived Rally
Price Movement (USD vs INR)



Source: MCX, London Bullion Market Association

World Investment in Gold Weakens



Source: Thomson Reuters GFMS

India's trade deficit narrowed to a two-and-half-year-low in September, data showed on Wednesday, indicating that the government's bid to curb gold imports, and reduce the deficit, by raising import duty (currently at 10%) on the precious metal several times this year was having an impact. Non-oil imports likely eased on lower gold purchases as their volumes came under pressure on account of fresh import restrictions and lack of clarity in the RBI trade regulations.

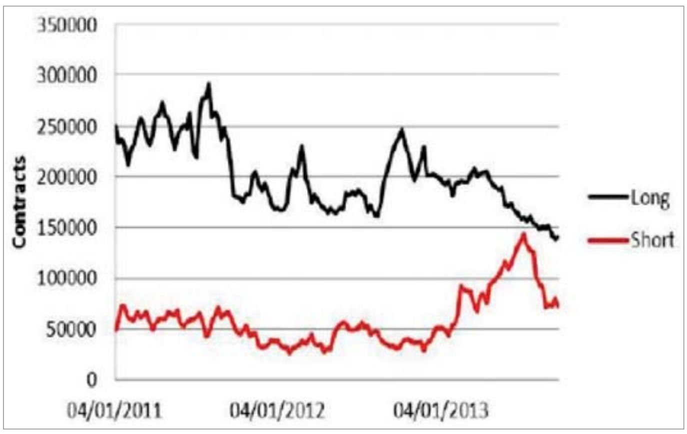
Traders had expected gold prices to get a boost when China reopened on after a week-long holiday in October, but buying in Shanghai has been muted. With the spot gold price around $20 an ounce lower than when the holidays began, the market was hoping for a bit of a bounce, but this didn't eventuate. Data from Hong Kong showed that China imported more than 100 tonnes of gold for a fourth straight month from Hong Kong. But some analysts have questioned whether demand can stay at these levels through the rest of the year.

From fundamentals perspective world's Gold demand has slacken a bit but restrained supply should be able to support the metal prices. According to GFMS report on Gold, the Jewellery fabrication in 2013 jumped by 22.8% in the first half, in response to a marked decline in gold prices but investment demand and net official sector purchases dropped by 28.3% and 32%. In supply side Global scrap supply fell by 14% majorly because of weaker gold prices.

Despite more stable prices after the major sell-offs seen earlier this year and some decent price gains, ETF investors are still cutting exposure. The combined holdings now stands at 1,946 tonnes, the lowest it has been since peaking at 2,647 tonnes. That is a drop of 26 percent.

Other than the U.S. debt ceiling deadline which could spur a safe-haven demand for bullion metals, traders are also looking at the Federal Reserve policy meeting later this month for clues on whether the U.S. central bank will begin trimming its stimulus this year. Analysts expect that the physical demand will make a come-back on account of imminent festival season in India and China and expectations of better central bank purchase data in second half of the year. However, if the metal fails to sustain current price levels of $1300.00/Oz short term speculative buyers will be ready for another round of sell-off.

Investors Exit Short Position, Lowest in September

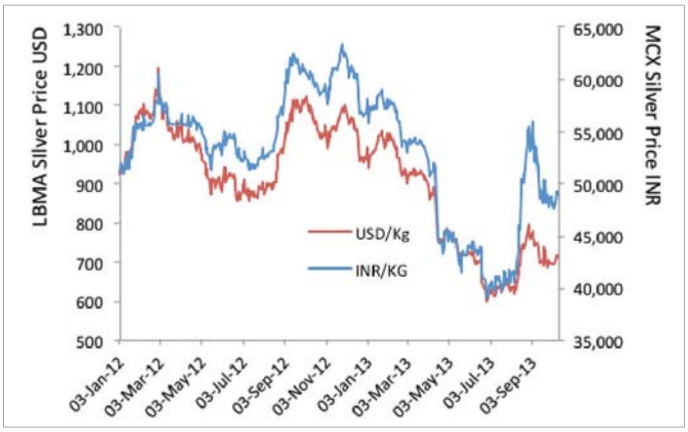


Source: Scotia Metal Matters, October'13

Silver: Performance and Future Outlook

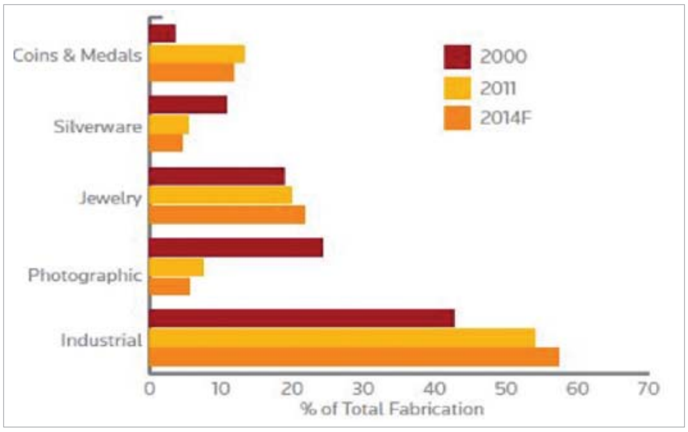
The pull back from the August high at $25.12/oz continues, with prices breaking below $21/oz in early October. Silver was trading at $22.10/oz on October 9th. The post-FOMC rally in mid-September turned out to be a knee-jerk reaction and the fact Silver failed to attract follow through buying did suggest that the market was not ready to get bullish again.

Silver follows Gold's Lead-falls after a short rally
Price Movement (USD vs INR)



Source: MCX, London Bullion Market Association

Expected Share of Industrial Demand of Silver



Source: Thomson Reuters GFMS

Fundamentals for white metal are in much better shape than those of Gold. The increase in the sale of silver relative to gold has been especially impressive. The U.S. Mint has sold 60X more one ounce U.S. Silver Eagles than they have one ounce U.S. Gold Eagles. Silver bars and coins now make up a significant portion of the overall annual silver demand. In 2007 silver coins represented less than 40 million ounces of the approximately 666 million ounces of annually mined silver. In 2013 sales of silver coins and bars should exceed over 100 million ounces of the projected silver to be mined in 2013.

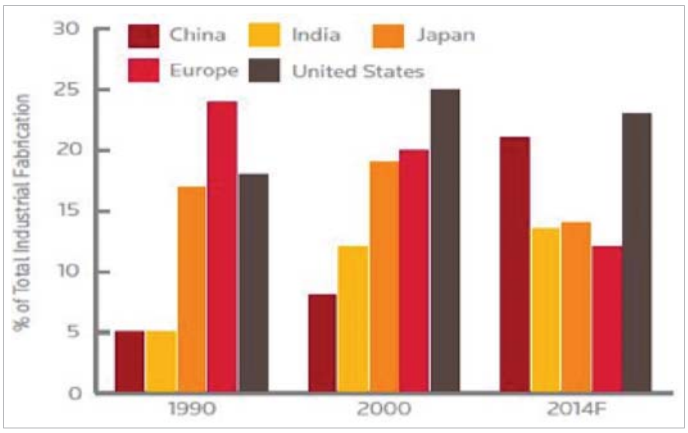
Unlike Gold, the Silver ETF holdings remained high with the amount held just 0.4% below record levels of 19,960 tonne that were seen in mid-March. Quite why there is such a disparity between Gold and Silver holdings is a mystery, but for now analysts believe that it is a sign of extreme confidence in metal's future. The net long fund position in Silver fell during September and most of the movement was accounted for by long liquidation with the gross fund long position dropping to 29,357 contracts, from 34,616 contacts in early September.

In India silver sales are setting records. Silver imports in India were 857 million tonnes from April through July this year, up nearly 260% and totaling approximately one third of the global monthly production of silver. Demand was partly supported by the restrictions put on Gold imports by government of India to curb its hefty import bills of non-essential metals. In China demand for physical silver is also up sharply for investment and industrial use. Approximately 50% of silver's demand comes from industry mostly from electronics (silver is the best conductor of electricity), solar panels and photography. China's silver demand is expected to increase with a recovery in industrial activity.

Historically the prices of silver and gold have been closely tied to each other. However, high investment demand of Gold as a diversifying-safe-haven asset has been keeping this ratio high at 60s levels. Analysts believe that this disconnect will soon be covered by the physical demand generated by industrial demand which has been on the rise.

Silver has been seeing healthy industrial demand in recent months as major global economies remained on recovery tracks. The ETF holdings also suggest that people have not lost their faith in white metal as a safe-haven investment which could eventually bring a positive turn around in its prices -currently near the support of $20/oz levels.

Leading Manufacturers' Share of Industrial Fabrication



Source: Thomson Reuters GFMS

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