RIO Professional Investors Fund Limited

20 March 2009

Summary

The RIO Professional Fund's current weighting in assets, based outside the US Dollar, have lead to a -20% loss in currency terms, since the Fund is valued in US Dollars. The assets themselves are undervalued and, as such, are well positioned to see upward movement soon. I also believe that the Dollar is overvalued; the recent Fed moves have clearly shown the currency's vulnerability and this underlines my resolve. The Fund will further benefit from any US Dollar weakness looking forward; I have traded Dollar/Sterling/Dollar positions within this Fund during 2006/7/8 with almost all trades posting good gains.

Last week the Fund gained on the Fed's move. The Uranium positions held by the Fund will also benefit from ongoing shortages in this commodity as 2010 is approached. I will add to our position in Gold on lows, and continue to trade this metal within the Fund. This metal went down last week and then quickly bounced back over $930. The Fed's announcement last week created frenzy in the Gold market. In fact the price of Gold shot up $50 per ounce less than 2 hours after the Fed meeting. Further detail on the Gold market now follows.

Gold surges on Fed move

Gold slipped more than 1 percent to briefly dip below $930 on Thursday last week after surging late the previous session to a two week high, following the Federal Reserve's surprise move to buy long-dated U.S. government debt. It rose as high as $945.05 after the Fed's move, its highest since March 2nd. Gold was at $931.20 per ounce at 0649 GMT after earlier sinking to a low of $925 per ounce, down 1.6 percent from New York's notional close of $940.0 on Wednesday last week.

I predict that traders will be watching to see whether Gold will be able to consolidate and hold above the $930-$940 level. I believe that Gold will continue to be driven by the performance of the U.S Dollar. Decline in the U.S. currency often boosts Dollar denominated Gold, which becomes cheaper for overseas traders, in addition to enhancing its appeal as a safe-haven investment instrument. This is a strong reason why I continue to trade this holding within the Professional Investors Fund.

The price of Gold topped $1,000 an ounce on March 13th, and the number of Americans who are taking delivery of Gold coin and bars is still rising. According to the World Gold Council, Americans bought 600 tons of Gold bars and coins in 2008, a 42% increase over 2007.

That is less than in Europe, where Gold mania has become epidemic, but significant given the metal's high price. Analysts say that if stock markets continue to spin out of control and real estate values continue to sink, more people will want to take shelter in an investment with a reputation for being safe, reliable and not dependent on governments for its value.

Well, ultimately the Fed are printing paper, the UK are printing paper, the Swiss are printing paper and the Japanese are printing paper!

Commodity markets were cheered on a glimmer of hope that the Federal Reserve's move would revive the global economy, boost industrial activity and increase demand for oils and metals.

Something I noticed was that the last time Gold sales spiked so dramatically was the year before Y2K. For much of modern history, until the 1920s, government currencies were backed by Gold, an economic practice meant to limit inflation, known as the **Gold Standard.**

The US Market

U.S. Bonds are perhaps the Riskiest Safeguard in Financial History

Under cover of the AIG scandal, the Fed did something foolhardy last week. "Fed plan stuns investors," was the headline in the Financial Times this morning.

In response to the Fed's latest move, the yield on 10-year Treasuries fell more than at any time since they started keeping records in 1962. From 3.01% it had fallen to 2.48% when last checked.

Yields fell because the Fed said it would buy $300 billion worth of government debt. Stocks rose, with the Dow up 90 points, and the dollar fell heavily.

It is interesting to note that, when Richard Nixon cut the link between the Dollar and Gold, the world entered a money system that is, to put it in its best light, experimental. The last experiments of this sort, on anything like this scale, were conducted in the 18th century. The *Banque Generale* was set up by the rogue, John Law, to buy up the debt of France, of which there was plenty. And a similar plan was set in motion in England soon after what was later known as the South Sea Bubble. It was similar in that the Bank substituted pieces of paper stock in the South Sea Company for government debt; many people lost their shirt!

In the U.S. version, circa 2009, the Fed uses pieces of green paper called 'Dollars' to buy up the government debt.

Dollars are normally produced from government authorized printings of bank notes!
With this latest move no printing is required. When the Fed buys U.S. debt, it merely makes an electronic notation, like an IOU, that disappears as soon as the power is switched off.

When those 18th century debt buy-up schemes were put in place, at first their stock rose. Shares in the South Sea Company went up 10 times in a single year.

U.S. bonds rose strongly yesterday too; of course, the richest investors in the world just entered the marketplace - announcing that they would buy $300 billion dollars worth.

If that does not work well they will buy more? “Fed to buy $1 trillion in securities to aid economy," reports the New York Times.

"The Fed is engaging in massive quantitative easing," said William Poole, former head of the St. Louis Fed.

The central banks of England, Japan and Switzerland are all buying their government bonds. The IMF has also entered the buying.

From what I can see, all the bailouts and stimulus plans so far have not worked. At least this latest plan makes a little more sense. Buying up the securities of Fannie and Freddie, the Fed will lower the cost of mortgage debt. This will give homeowners an opportunity - probably the last one of their lifetimes - to refinance their houses at low interest rates. The target range, we have heard, is between 3% and 4%.

In the short run, if the homeowner is able to refinance at such low rates, he reduces his monthly cash-flow burden and frees up cash for other things (such as paying down his credit card debt). In the long run, if he is able to lock-in those low rates, he will almost certainly see the debt burden itself significantly eased - thanks to rising inflation rates.

RIO's research indicates that it is time for Lenders to beware!

U.S. Treasury bonds are attractive because they are safe, but they could turn out to be the riskiest safeguard in financial history. This is a moment when it is probably better to be a borrower than a lender. Refinancing your house at 5% fixed rate in the USA and 3.2% in the UK is so attractive; I am tempted to do it myself.

The US Dollar

Dollar oversupply concerns are beginning to show.

The Fed move stirred worries that the sharp expansion of the Fed's balance sheet, which has already doubled in size in the past six months, could lead to an oversupply of the world's main reserve currency.

The U.S was not alone in the buying of government debt. The Bank of England is buying 75 billion pounds of gilts and the Bank of Japan on Wednesday announced it would increase its purchases of Japanese government debt. The Swiss National Bank surprised the market last week with an intervention to weaken the Swiss franc as well as an interest rate cut to fight a deep recession. In addition, the European Central Bank may also eventually turn to non-standard policy measures after cutting interest rates to a record level of 1.5% in March.

How desperate is the economic and financial situation in the US? More importantly, how bad is the situation compared to the rest of the world? Considering the dollar's (and nearly every other currency and asset class's) reaction to the Fed's policy announcement last Wednesday, the outlook is bleak and growing worse.

A Closer Look At Financial And Consumer Conditions

My comment on recent events would be that, despite the bailouts, guarantees and stimulus packages from US and other officials around the globe, financial conditions are still on the edge of panic. Despite the effort that is being made to improve the flow of money and credit around the world, the presence of toxic debt, the continuing over-abundance of leverage, and development of the worst recession in nearly six decades is preventing the various medecines administered from taking effect. Sentiment was further depressed when the G20 meeting last Saturday ended without a much needed coordinated response to what are obviously global problems. A more formal summit is scheduled for April 2nd, but should we expect anything more?

The US economy is falling deeper into recession; but most market participants have long realized that the slump is far from finding a bottom any time soon. Nevertheless, confirmation that a brake on such an aggressive contraction has not yet taken place will leverage pessimism. Considering the consistency of deterioration in economic activity, the surge in unemployment and the unique troubles in banking and lending, the USA are perhaps nearing the point when economists and market commentators begin using the term 'depression.' With recent data showing consumer sentiment holding near a 28-year low and factory activity dropping the most in 75 years, it probably seems warranted.

The following tables summarize the movements of Credit Market and Economic Indicators over the period

Credit Market	Previous	Current	Change	% Change	Outlook*
Credit Card Delinquencies	5.15	5.52	0.37	0.37%	Deteriorating
Mortgage Delinquencies	8.99	7.88	0.89	0.89%	Deteriorating
US 3 Month Libor Rate	1.320	1.227	-0.09312	-7.05%	Deteriorating

Economic Indicators	Previous	Current	Change	% Change	Outlook*
GDP (Annualized)	2.8	-6.2	-6.2	-6.20%	Deteriorating
Initial Jobless Claims	631	646	15	2.38%	Deteriorating
Consumer Confidence	37.4	25	-12.4	-33.16%	Deteriorating
ISM Manufacturing	35.6	35.8	0.2	0.56%	Deteriorating
ISM Services	42.9	41.6	-1.3	-3.03%	Deteriorating
ISM Services - Employment	34.4	37.3	2.9	8.43%	Deteriorating

The Financial and Capital Markets

The Fed’s decision to join the Bank of England by adopting a policy of quantitative easing was taken initially as a sign that the government has not run out of options for turning the economy around. However, the purchase of $300 billion in longer-dated government notes helps little more than just the Treasury market at this point. A rebound from the capital markets is more than likely a mixture of sentiment and traders taking advantage of burgeoning inefficiencies. From a confidence perspective, the bullish drive in the market is a necessary rebound that breaks the pace of an otherwise consistent decline - there are certainly rallies in bear markets. Another factor in the rebound for equities specifically is the action of savvy investors and traders taking advantage of the government’s presence in the markets. With so much money floating around, it is bound to trickle down to speculators.

While the government’s additional steps may placate some investors, it generally highlights how dire the situation truly is. If the next G20 meeting doesn’t produce a promising global policy, momentum will inevitably carry growth and sentiment much lower.

The Economy and The Credit Market

Are US Treasuries still the risk-free assets that they were 10 years ago? This is a question that can redefine the dollar's trend for weeks or months. It seems the safe haven status that has supported the world's most liquid currency for nearly eight months now is starting to meet resistance. Growth forecasts for the United States continue to diminish, as policy efforts fall short of a consumer and credit-led plunge in economic activity. In contrast, the FX market's typical high yielders are actually finding economic projections that point to a quick recovery, making such currencies attractive because of both sound fundamentals and comparatively high returns. However, sentiment following growth projections and sentiment based on liquidity come under two very different conditions of fear and risk. The US has the deepest markets in the world; but with the pressure of an accelerating global recession and/or the emerence of another financial crisis, the American economy will be exposed to its struggling policy efforts and an economic trend towards a possible depression.

Reports to follow this week's investment report: RIO Prestige Performance Fund and a general update.

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