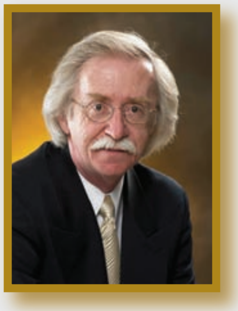
BMG BullionFund

2008 ANNUAL REPORT

BMG

CONTENTS



A MESSAGE FROM NICK BARISHEFF

"I hope for the best but **prepare** for the **worst**.
The **worst is at our doorstep**, and now it is time to
strip away old thinking and plan a **different kind** of strategy.
The next 20 years will not be like the last 20 years."

– Nick Barisheff

The global credit crisis of 2008 heralds the beginning of a deep bear market that is likely to last for years. Why? Because despite the massive financial deleveraging that took place in 2008, huge structural imbalances still remain. Systemic excesses that took decades to build will take decades to unwind.

A credit bubble causes far more devastation when it bursts than a stock bubble. Credit is the lifeblood of the US economy, and when it ceased to function in 2008, the US economy literally seized up. America's problems quickly spread to the rest of the world. Federal Reserve Chairman Ben Bernanke recently said that America's economic system is "critically dependent on the free flow of credit." But healthy economies are not dependent on credit for spending and investment. In most of the world's economies, income and savings drive investment. Not so in the heavily indebted US, whose cash-strapped consumers account for over 20 per cent of world GDP.

Bull market thinking during a secular bear market is lethal to an investor's wealth. But has bull market thinking left the markets as a result of the global financial crisis? Surprisingly, it has not. Old habits die hard, it appears. Even now, far too many institutional and retail investors impatiently wait for the bottom so they can jump into a once-in-a-lifetime buying opportunity. Optimism seems to rule in the consumer market as well. A staggering 71 per cent of American consumers believe the economy will improve during the first year of the Obama presidency, according to a January 2009 Associated Press poll.

President Obama may bring hope, but hope is not an investment strategy. Hope will not preserve wealth during an extended downturn. Investing mantras like 'buy and hold' and 'stay the course' are not only wishful thinking; they are the height of folly in a long-term bear market. History shows us that in a deep recession, stocks fall *below* fair value and can remain there for years. The bear market from the late '60s to the early '80s is the most recent example. In 1979, market sentiment had fallen so low that *BusinessWeek* famously announced "The Death of Equities". Pessimism ruled and stocks were spurned, which sowed the seeds for the next bull market.

Because secular trends last for years, they also take years to break. Included are two charts *(Figure 1A and 1B)* from two secular bear markets in the twentieth century. The dotted lines indicate the length of time in years it took for the markets to recover, or in other words, how long it took to make buy-and-hold investors 'whole' again.

The S&P 500 Index needed until 1954 to surpass the peak it achieved in 1929 (*Figure 1A*). It took a decade (*Figure 1B*) from its peak in 1972 for the market to surpass that mark, in 1982. These charts reveal one of the dirty little secrets of Wall Street and Bay Street: buy and hold doesn't work in a secular bear market. The average recovery time during these two bear markets was seventeen years! Seventeen years is a very long time for an investor to wait to break even, and that doesn't even take into account the effect of inflation.

Figure 1A: S&P 500: 1929 - 1954 Bear Market

Years from bull market peak until recovery

If you are a retiree or a soon-to-be retiree, a secular bear market carries a double whammy: it will not only decimate your wealth but eliminate any chance of recovery. Even if you are much younger than retirement age, buying and holding the wrong asset class during a secular trend change is fatal, because investors are supposed to build nest eggs, not shrink them. But losses get deeper and deeper in a secular bear market, even if you're invested in index funds. The Dow Jones secular bear market lasted even longer. If you bought and held the Dow 30 stocks from 1966 through to 1982 (the last bear market), your nominal returns would have been zero. As Warren Buffett points out: "During these 17 years, the stock market went exactly nowhere."

But that's only part of the story. On an inflation-adjusted basis it would have taken until 1995, nearly 30 years, to break even. And remember, this period was not even considered a depression. Buffett is often portrayed as a proponent of buy-and-hold investing. He actually buys and holds undervalued companies, not stock indexes. Because Buffett is a professional investor and highly skilled valuation analyst, he can recognize when a company is undervalued. He can do enough research to get to know a company intimately.

If you are counting on stock dividends to help you get through this downturn, consider this fact: at the time of writing, dividends are being cut at the fastest pace in at least 50 years. And by many companies that have never cut their dividends.

Common stocks have been available to investors for several hundred years, but few investors realize that until the 1950s, they were considered highly speculative. Bonds formed the core of most investment portfolios and savings were mostly in savings accounts, real estate or jewellery. Mutual funds did not become a popular part of the investment scene until the 1980s, when mass marketing to up-and-coming Baby Boomers helped this new and untested investor generation regard the stock market as a relatively 'safe' but much higher-yielding alternative to boring old savings accounts.

Dreams of early retirement and campaigns like 'Freedom 55' kept hopeful investors in the markets. And they were rewarded. But lax monetary policy led to too much easy money seeking high returns, and bubbles began to form. Dark economic forces were at work, and these forces began to accelerate in the 1990s under Fed Chairman Alan Greenspan's watch. He warned of irrational exuberance, but did nothing about it, and the imbalances grew. Rational investors

Figure 1B: S&P 500: 1972 - 1982 Bear Market would take their money out when the markets became overvalued; so said the economists and market gurus. But the Greater Fool Theory had taken hold, which is to say that as long as a greater fool was waiting in the wings to buy stock, one might as well keep holding.

Reward became the sole focus, risk was ignored. Unfortunately, the wishful thinking that investors embraced was matched in equal amount by people who should know better - government authorities. Fund manager Jeremy Grantham says that the economic establishment "so valued orderliness and rationality that they actually grew to believe (in rational behaviour and efficient markets)".

"It was why Greenspan and Bernanke were not sure that bubbles – outbursts of serious irrationality – could even exist. It was why Bernanke, who had studied the bubble of 1929, could still not see it as proof of irrationality and could still view the Depression (à la Milton Friedman) as a mere consequence of incredibly bad, easily avoidable policy measures."

What's an investor to do? The good news is that these are the best of times and the worst of times, depending on which asset class you are in. If you're in financial assets (stocks and bonds) it will be the worst of times. If you're in precious metals, it is the best of times. As a precious metals investor, you are to be congratulated for taking action to preserve your wealth. But there is much more to do.

In a bear market, rebalancing more and more of your portfolio into negatively correlated assets is crucial. Unless you have already done so, it means reducing your allocation to stocks and bonds and increasing your allocation to bullion. Bullion is an asset class that will maintain its purchasing power as we head into a prolonged period of either stagflation or hyper-inflation. (Why these two scenarios are likely is explained in our Outlook for 2009.)

Ask yourself this question: Is the portion of your portfolio that is allocated to bullion large enough to allow you to withstand the ravages of a long recession or depression? Will you be able to sleep at night if the 2008 decline was just the beginning of a long-term downward spiral? If you are in cash, ask yourself whether cash really is king. In the massive monetary expansion we are now experiencing, cash value will be eaten away by the eventual inflation. If the banking crisis deepens, as many think it will, banks may limit access to your money.

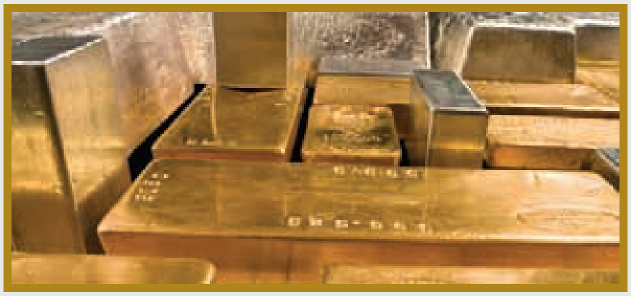
I've always been a realist when it comes to our economic future. I hope for the best but prepare for the worst. The worst is at our doorstep, and now it is time to strip away old thinking and plan a different kind of strategy. The next 20 years will not be like the last 20 years.

Sincerely,

Nick Barisheff, President, Bullion Management Services Inc.
A BMG Company

"What we are **experiencing** is the birth of a new era, **a wake-up call** to overhaul our institutions, our systems and, above all, **our way of thinking.**"

– Karl Schwab, Chairman, World Economic Forum



A LOOK BACK AT 2008

"Our **Ponzi-style economy** and its policy remedies encourage bond investors to **mimic Uncle Sam** and its global compatriots."

- Bill Gross, CEO, Pimco

Markets suffer their worst year since the Great Depression

The precipitous drop in the global financial markets, which had their worst year since the Great Depression, was a painful one for most investors. But it also brought reality back to the land of smoke and mirrors. It is now clear to most investors that the operators of our banking and financial system created an illusion of wealth and never-ending profits that was so masterful they actually began to believe in it themselves. How else to explain their complete shock and bewilderment when the financial house of cards finally fell apart?

The staggering cost of 2008

2008 was a year for the record books. Real estate losses exceeded *$6 trillion, equity losses $7 trillion in the US and $32 trillion globally. The US government and the Federal Reserve spent $3.2 trillion in 2008 bailing out institutions that were "too big to fail", and committed another $5 trillion so far for 2009, for a total of over $8 trillion.

This amount, $8 trillion, is nearly twice as much as was spent on the Korean War, the Vietnam War, the space program, the Savings and Loan crisis and the invasion of Iraq combined. It is over half of total US GDP, and approximately $30,000 for every man, woman and child in America. In contrast, the 1998 bailout of Long Term Capital Management amounted to a 'mere' $3.6 billion, while WorldCom's bankruptcy was $103 billion.

The end result of all this spending will be inflation, not just in the US, but in the UK, Europe, China, Russia and Canada, all of which have adopted similar massive bailout programs.

Of hopes and dreams and pyramid schemes

The global financial system is in some ways an enormous pyramid scheme. The banks rely on a perfectly legal form of leverage – the fractional reserve system. It allows them to use other people's money (OPM) to generate outsized profits. As long as more money comes in than goes out, the scheme works. It breaks down when too many depositors want their money at the same time, which starts a run on a bank.

The owners of a Ponzi scheme keep virtually all the incoming funds for their own use, only returning money when needed for redemptions, which are highly discouraged. Fortunately for us, the banks are not Ponzi artists. But the biggest players in the financial system certainly know how to work the system, and the current rules prevent them from losing. Too-big-to-fail financial institutions have been given carte blanche to use OPM as required – investors' on the way up, and taxpayers' on the way down *(see Figure 2)*. So much for downside risk.

In today's capitalism, gains are privatized and losses are socialized. This is the best of all possible worlds for the globe's largest financial players, but not for taxpayers and investors. Despite hundreds of billions of dollars of capital injections from the Troubled Asset Relief Program (TARP), many US banks are technically insolvent. The world's financial authorities are pretending to be stern with the banks but it would be political and economic suicide to let the banking system actually fail, which means much bigger infusions of taxpayer money are to come. How much is unclear. What is clear is that the losers in this high-stakes game are the taxpayers.

The origin of the crisis

The biggest factors behind the US-driven global financial crisis of 2008 were easy money, leverage, debt and denial. Easy money, in the form of artificially low interest rates, led to the unconstrained growth of mortgage credit by non-banks and encouraged governments, consumers and businesses to spend and borrow like there was no tomorrow. Excessive leverage allowed financial institutions to make record profits on their 'easy money'. Excessive debt helped deepen the crisis by allowing the party to go on too long. And finally, regulatory authorities, governments, central bankers and investors went into denial, which allowed the merrymaking to continue unchecked until the music stopped. Let's look at each of these four factors in depth.

"It's a **proprietary strategy**. I can't go into it in great detail."

- Bernard Madoff

Factor 1: Easy money

Easy money is the root cause of the problem. Soon after the US Federal Reserve was created in 1913, the members of that elite group decided to break from their defined role. Instead of being passive lenders of last resort, they took a more active role in the global economy and over time became the world's most aggressive interventionists.

Alan Greenspan and Ben Bernanke have perfected that role. At the first hint of recession, the floodgates are opened and cheap money is poured into the system. Twenty years of this type of monetary policy have shaped America's economy and made it what it is today: flabby, undisciplined and vulnerable.

In 1971, when the US abandoned the gold standard, total M3 money supply stood at $800 billion. Since then, the Federal Reserve has continuously increased the money supply in excess of GDP growth. In 1987, newly appointed Fed Chairman Greenspan took monetary policy to an entirely new level and expanded the money supply from $3.5 trillion to $10 trillion – more than all of the previous Fed chairmen combined. Ben Bernanke came along in 2006 and added another $4 trillion in just three years.

At the time of writing, Bernanke has dropped interest rates to zero, and the rest of the developed world is following suit (with the notable exception of Iceland, a country whose banking system has virtually collapsed). But low rates cannot cure structurally unsound economies. They simply open the gates to a bigger problem – inflation.

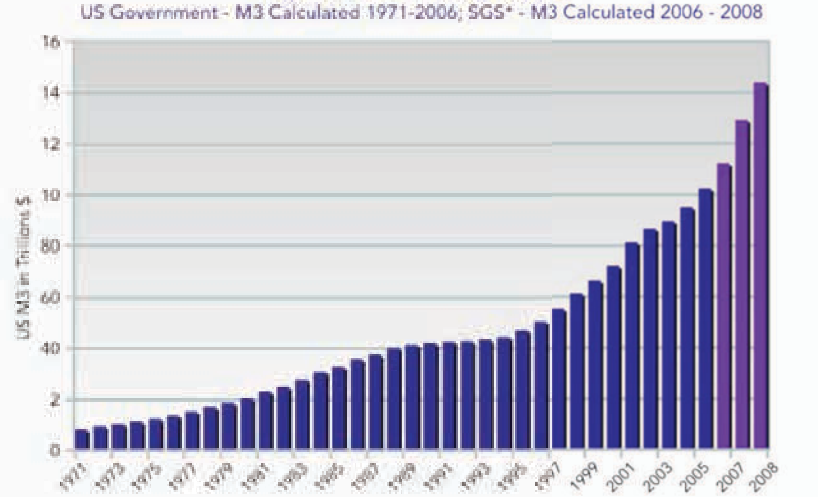
According to economist Milton Friedman, ***"Inflation is always and everywhere a monetary phenomenon, in the sense that it cannot occur without a more rapid increase in the quantity of money than in output."***

When central banks print money in excess of GDP growth, prices rise because too much money chases too few goods. Inflation is caused by banks, not by supply and demand imbalances. Once the inflation genie is out of the bottle, it is impossible to put it back in. As central banks drop rates in unison this coordinated approach will just accelerate money supply growth and inflationary pressure.

When credit-based economies severely contract, as in the Great Depression, debt compounds and defaults accelerate, causing economic collapse. The recent bout of deleveraging and the consequent plunge in asset values could send us into a deflationary spiral. But

Figure 3: US Money Supply

US Government - M3 Calculated 1971-2006; SGS* - M3 Calculated 2006 - 2008



*SGS is Shadow Government Statistics, a private economics firm specializing in calculating US money supply and consumer price inflation figures, using government supplied data. SGS has calculated the M3 Money Supply figures since the Federal Reserve stopped publishing this figure in 2006.

Bullion Management Group Inc. © 2009

again, the Fed has clearly stated that it will print as much money as needed (as measured by M3) to avoid that scenario. Governments around the world are also printing money in unprecedented quantities to try to inflate their way out of this mess. The process has already begun. US money supply increased by over 11 per cent in 2008 (*see Figure 3).*

Factor 2: Excessive leverage

Thanks to the Fed's decision to slash interest rates to 1 per cent in 2003, literally trillions of dollars' worth of easy money seeking the highest possible return began to slosh around the globe. High returns are always difficult to achieve in low-interest environments, but investors and institutions realized that they could boost returns by ratcheting up their leverage. Sure, there was risk to doing so, but if the markets or the economy began to crumble, Bernanke would come to the rescue. At the peak of the housing market, for example, lenders were offering home buyers up to 120 per cent of the value of the home they were about to purchase.

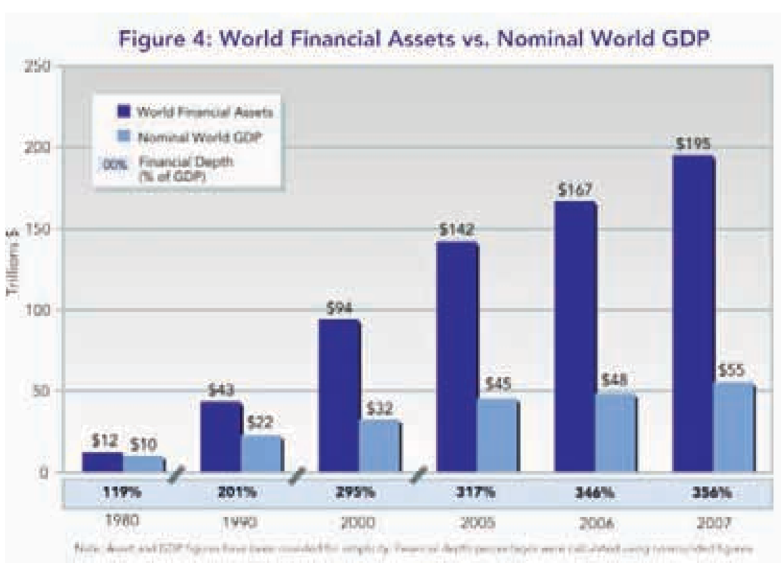
Dangerously high leverage combined with financial engineering turned an already overheated financial system into a cauldron, sending the prices of financial assets soaring to unsustainable levels. By the end of 2007, total global financial assets were valued at an absurd four times total global GDP *(see Figure 4)*. By contrast, in 1980, financial assets were about equal in value to world GDP.

Even the massive compensation packages that many Wall Street investment bankers and traders enjoyed were built on leverage. Former Wall Street trader Shah Gilani said that "in order to keep paying out big bonuses to keep the big rainmakers at the firm, in order to increase earnings per share, the volume of capital applied toward profit-making gets heavily leveraged."

Factor 3: Excessive debt

Businesses took on unprecedented levels of debt because the cost of capital was so low and so readily available. Homeowners took out lines of credit on their always-appreciating homes so they could continue their spending sprees. But the biggest culprit of all was government.

There was a time when the US was a responsible economic power. Not any more. In the past eight years, total US credit market debt-to-GDP has exploded, and in the past three months the budget deficit has doubled. With Obama pledging to add $1 trillion to the deficit combined with the unfunded liabilities for Social Security and Medicaid , there is no limit in sight for government debt.

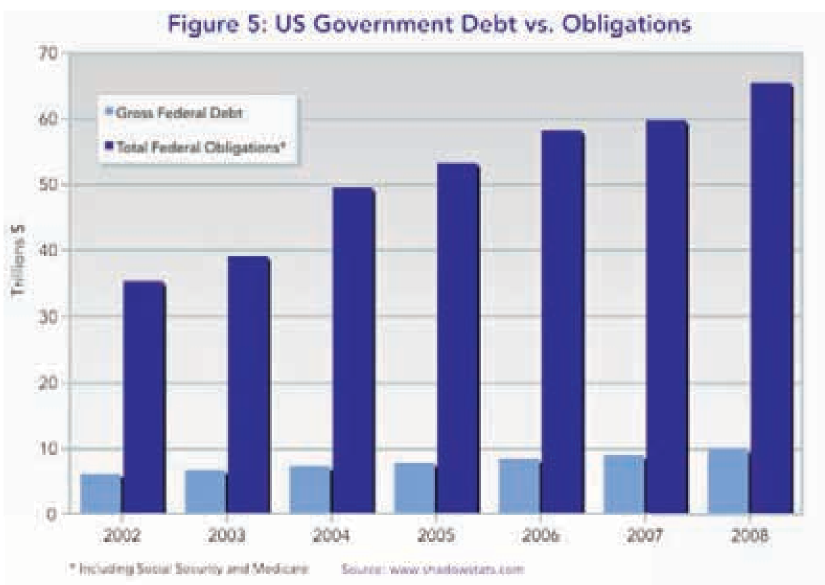


The US has also created a massive unfunded liability for itself. Money the government promised to taxpayers for Social Security has instead been borrowed for its own use. Money the government promised to fund future Medicare and Medicaid benefits, and for military/government pensions, has not been set aside at all. These unfunded liabilities total $40 trillion dollars; combined with the debt of nearly $11 trillion, US government commitments total over an astonishing $50 trillion, or nearly four times the total US GDP. Richard Fisher, a member of the Federal Open Market Committee (FOMC) says the total US debt – including Medicare and Social Security – is more than $99 trillion! The chart below (*Figure 5*) helps put things in perspective.

Factor 4: Denial

Even after all that happened in 2008, many investors remain in denial, just as Bernanke was when he famously said, "The impact on the broader economy and financial markets of the problems in the subprime market seems likely to be contained." But given the colossal mistakes that were made at Bear Stearns, Lehman Brothers, Fannie Mae, Freddie Mac, IndyMac, Washington Mutual, AIG, Citigroup and other formerly world-class financial institutions, it is unlikely that denial has left the markets. The remaining counterparties within the unregulated $600-trillion derivatives market are just as likely to make even greater mistakes.

Investors have enjoyed such a long bull-market run that it is difficult for them to change their behaviour. But change they must. Although GDP is falling, few investors realize how fast it is going to drop in the



"Why the **SEC allowed investment banks** to go from 12-to-1 (leverage) to **40-to-1** is beyond me."

- Jim Puplava, FinancialSense.com

next year. For years, GDP has been overstated by a multi-billion-dollar ‘stealth’ contribution from mortgage equity withdrawals (MEWs). As we know, since the stock crash of 2002 wiped out much of their paper stock wealth, investors and consumers have used their homes as glorified ATMs so they could keep spending and stay in denial about the true state of their finances.

MEWs accounted for hundreds of billions of GDP. Without MEWs, GDP growth since 2001 would have been abysmal. And now, TARP and countless other capital infusions will replace MEWs as a key ingredient in overstating GDP growth, because GDP includes government spending.

When a credit bubble bursts

The full effects of the global financial crisis are yet to be felt. Since the bailouts began and the printing presses started to run at full tilt, economic conditions have worsened, corporate earnings have fallen, defaults and bankruptcies have risen, house prices have crashed and job losses have skyrocketed.

Credit is the heart of the financial system, and when it crumbles, the system crumbles. Consumers accustomed to easy money now face a lethal combination of rising unemployment, plummeting personal wealth and a rapidly slowing economy. Canada’s economy contracted at an annualized rate of 3.4 per cent in the fourth quarter of the year. But if Canada’s economy has the flu, the rest of the world is on life support.

US GDP decreased a staggering 6.2 per cent (annualized) in the fourth quarter of 2008. The European Union suffered a 5.9 per cent fourth quarter GDP drop, Q4 GDP growth in Hong Kong, Singapore, South Korea and Taiwan was negative 15 per cent, while Japan's gross domestic product dropped 12.7 per cent in the October-December quarter, and Japanese exports plunged 45 per cent from year ago levels. Behind this global economic slowdown is an unmistakable fact: the US consumer, who represents 20 per cent of world GDP, is strangling in debt and being laid off in record numbers.

> “Like gold, **US Dollars** have value to the extent that they are strictly **limited in supply**. But the US government has a technology, called the **printing press** that allows us to **print** as **many dollars** as it wishes at essentially no cost.”
>
> - Ben Bernanke, Federal Reserve Chairman

Although Canada's economy and its banks were in good shape, in 2008 the country quickly became engulfed by the recession sweeping in from south of its border. Statistics Canada reported that Canadian exports plunged 9.7 per cent in December, and almost every sector was affected. Canada's exports to the US amount to an enormous $350 billion per year (only China exports more). So it is not surprising that Canadian manufacturing sales dropped over 8 per cent in December alone, and have declined for five straight months - a trend that is accelerating. As US consumers and businesses continue to retrench, the numbers will only get worse.

Employment keeps shrinking

Canada lost 100,000 jobs in the last two months of 2008, and that number exploded to 129,000 in January 2009. The US lost over 3,000,000 jobs in 2008, and 500,000 jobs in December alone. While the US unemployment rate is a dismal 7.2 per cent and getting worse, if a category called 'discouraged workers' were added in, the rate would jump to a staggering 13 per cent. The Bureau of Labour Services defines discouraged workers as "persons not currently looking for work because they believe no jobs are available for them." In the Great Depression, these people were included in the unemployment rate. Not so today. Consequently, only another 12 per cent rise in the unemployment numbers and we will reach the Depression-era unemployment level of 25 per cent. And let us not forget, the 'recession' has barely begun.

Total employment peaked in December 2007and has been declining ever since. Those who believe unemployment will bottom out soon should note that in an average recession, unemployment numbers continued to rise for almost five years. We are currently only one year into the downward cycle.

Consumer confidence keeps sinking

Given the employment numbers it is not surprising that consumer confidence is falling in Canada. But what is surprising is how fast it dropped. A long-term trend in which confidence rose steadily for 18 years between 1990 and 2008 abruptly ended and the bottom dropped out, sending it to all-time lows in a single year.

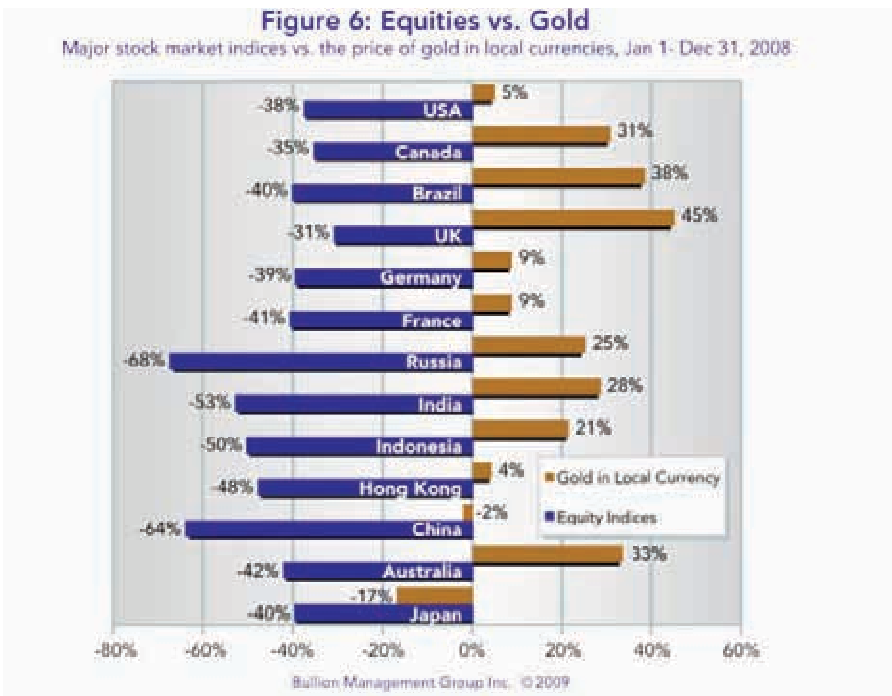
"The excesses of the **Age of Leverage** – the deluge of paper money, the **asset-price inflation**, the explosion of **consumer and bank debt**, and the **hypertrophic growth of derivatives** – were bound sooner or later to **produce a really big crisis**."

- Niall Ferguson, Historian and Author, Ascent of Money

Through the turmoil, gold and precious metals remained a pillar of strength

Through the deepening gloom, gold shone brightly in 2008. It fulfilled its role as a store of value and a safe haven, preserving investor wealth during months of financial turmoil. Gold outperformed every other asset class except bonds. Over the past five years, gold has been the best performing asset of all, and its long-term uptrend remains intact. The chart below (*Figure 6)* shows how well gold in different currencies performed versus equity markets in 2008.

To understand why gold performed so well, it is crucial to understand that it is primarily a monetary asset and not simply a commodity like copper or zinc. Central banks hold over 29,000 tonnes of gold as part of their currency reserves because they recognize its monetary value. The net turnover of physical bullion in London is over $20 billion a day, while volume is estimated at 7-10 times the turnover rate. In addition, it is important to note that precious metals trade on the currency desks of most banks rather than the commodity desks. Gold should be compared to other currencies – not commodities.



"The **vast riches** being earned in our bloated financial industry **undermined our sense of reality** and **degraded our judgment**."

- Paul Krugman, Professor, Princeton University, London School of Economics, Nobel Memorial Prize in Economics

Gold's performance was somewhat muted in US dollars, largely because of the extraordinary demand for dollars caused by massive deleveraging. But even so, compared to the S&P 500, which lost 38 per cent of its value in 2008, gold's 5 per cent increase in US dollars was remarkable. Its performance against other major currencies was exceptional. While global equity markets lost between 30 per cent and 70 per cent, gold rose 31 per cent in Canadian dollars, 9 per cent in euros, 45 per cent in British pounds, 25 per cent in Russian roubles and 38 per cent in Brazilian reals. Only the Japanese yen rose against gold, but this was due to the exceptional demand for yen produced by the unwinding of the Yen Carry Trade.

By the end of 2008, physical gold bullion was in short supply. Gold bullion coins, gold ingots and small bars were difficult to buy. In contrast, there is an unlimited supply of paper money along with trillions of dollars in paper bonds and equities.

Silver made a 28-year high in March at $20.92, and fell as low as $8.80 in November before ending the year at $10.79, down 27 per cent. A victim of the same investment deleveraging that ailed almost every other investment asset in 2008, silver experienced volatility often seen with precious metals in other years. The silver lining could be that silver did not decline as much as most equities, and that many analysts suggest that silver appears to be poised to outperform gold as precious metals continue their long-term bull market.

Platinum in 2008 saw a year to remember. Reports of South African electricity problems drove the price to $2,273 per ounce. South African platinum miners struggled but found ways to mine the metal by producing their own electricity with generators, which led to platinum correcting down to near the $2,000 level before falling victim to the market-wide losses caused by deleveraging. Although news of

"If the American people ever allow **private banks** to control the issue of their **currency**, first by inflation, then by deflation, those banks and the corporations that will grow up around the banks **will deprive the people** of all property until their **children wake up homeless** on the continent their fathers conquered."

- Thomas Jefferson

North American auto sales plunging in September caused some analysts to suggest this caused platinum's declines in 2008, most of the damage was done before auto-sector bad news. The good news is of course that platinum is also poised for strength going forward.

The currency of last resort

With world governments emptying their fiscal and monetary coffers to help countless financial institutions facing liquidity and solvency problems, all currencies appear risky. Experts say the recent US dollar rally has been driven more by declining confidence in other currencies than by increasing confidence in the US dollar. As global governments competitively depreciate their currencies in the vain hope of softening the deepening recession, gold is becoming the second reserve currency. The long-term uptrend in gold and precious metals has continued.

Precious metals have successfully preserved wealth for thousands of years because, unlike stocks and bonds and paper (fiat) currencies, they are not someone else's promise of performance and they are not subject to the whims of the printing press. Even though silver and platinum suffered through a price correction in 2008, BMG BullionFund still outperformed the TSX by 35 per cent, and is outperforming again in 2009. While a minimum 10 per cent to 15 per cent allocation to precious metals bullion is considered adequate in a bull market, a much larger allocation is needed today. Precious metals will possibly be the only currency that survives intact, because while governments may be able to print infinite amounts of money, they cannot increase the supply of hard assets with intrinsic value.

** All amounts in US dollars, unless otherwise noted.*

2009 OUTLOOK

"We can **evade reality**, but we **cannot evade** the **consequences** of reality."

- Ayn Rand, Novelist, Philosopher, Developer of Objectivism

Advice for investors

While most of the world's financial experts failed to see the global financial crisis coming, we have been warning about it for years. Government response to the crisis has been massive and haphazard, and will prove to be highly inflationary. Early estimates suggest it will cost upwards of *$10 trillion to mitigate the damages, but the true figure will become clearer as time unfolds. What is clear right now, however, is that global currencies are rapidly depreciating against precious metals as truckloads of fiat money are printed to cover all the stimulus and bailout programs.

As the financial system unravels, gold is becoming the world's second reserve currency, which means its 6-year upward trend should continue, while real estate, equity markets and even bonds will likely decline. Gold's rise will be spurred by the imbalance in value between money supply and aboveground bullion. This year, total global supply of aboveground gold is expected to increase by about $75 billion, while global money supply will increase by more than $10 trillion. This enormous disparity cannot continue without a significant upward price adjustment in gold as well as silver and platinum.

The crisis that keeps on giving

The year has begun with near-depression-level economic numbers. Canadian auto sales fell 25 per cent in January, and in the US they dropped to the lowest level since 1963. Job losses in Canada rose from 70,000 in December 2008 to over 129,000 in January 2009. The Toronto-Dominion Bank predicts Canada's unemployment rate will reach 8.8 per cent by the end of 2009, pushed upward by an expected loss of 325,000 jobs from the economy. These numbers may prove conservative.

The Canadian consumer is increasingly drowning in debt. The ratio of household debt to disposable income in Canada has bulged to 130 per cent, higher than in the US according to a recent report by Deloitte & Touche LLP. Meanwhile, outstanding credit card balances have exploded by 40 per cent since 2004, and now stand at $80 billion.

The housing crisis that started it all has not abated. Home prices continue to decline and home-equity loan defaults continue to soar. Meanwhile, Moody's rating agency continues to revise its default numbers downward: it is projecting Alt-A financing deals that originated in the second half of 2007 to experience 25.5 per cent losses of the original balance. That compares to 23.9 per cent for first-half 2007 deals, 22.1 per cent for second-half 2006 deals and 17.1 per cent for first-half 2006 deals. The trend is obvious.

Trying to solve this crisis are policymakers who do not understand how our monetary system really works. Massive bailouts, trillion-dollar stimulus packages and printing money out of thin air are not sound policies but acts of desperation. In 2009, we can expect more layoffs in the retail, travel, hospitality, financial, manufacturing and real estate sectors. Regardless of whether the automakers get another bailout or are forced into bankruptcy, further job losses are likely in the auto sector.

What was once a US credit crunch has morphed into the biggest global economic crisis since the Great Depression. In 2009, 50 million jobs could be lost and 200 million more people around the globe could fall into absolute poverty, according to the International Labor Organization, a United Nations agency.

It's a war out there

In 2009, the secular bear market will intensify. The equity markets may experience a rally during the year, but the deteriorating economy, loss of confidence and loss of jobs will drag down both earnings and share prices. Bond prices seem to have peaked and will likely experience declines in 2009 as interest rates must eventually rise from historic lows near zero per cent. US credit card delinquencies hit a record high in January, and further deterioration is likely as the economy slows and unemployment rises.

If 2008 was the year of the financial institution bailout, 2009 will be the year of the war between states, municipalities and non-financial corporations for their own bailout package. Shell-shocked banks have instituted tighter lending standards that will further hurt distressed consumers whose home prices are still declining. Meanwhile, defaults and foreclosures are now moving from subprime to higher-quality Alt-A and prime borrowers.

Those who think the housing crisis won't affect Canada may be in for a shock. Housing investment (public and private spending on construction and renovation) has plenty of room to fall according to the Organisation for Economic Co-operation and Development (OECD), which indicates that housing spending is likely to contract in several countries including Canada as the recession impacts the construction industry and weakens demand.

"Since last fall, the **global economic** situation has **deteriorated** further and **faster than anyone predicted**."

- Jim Flaherty, Canadian Finance Minister

The next casualty: commercial real estate

The collapse of the residential subprime bubble could be dwarfed by the collapse of the highly leveraged commercial real estate market. According to business analyst James Quinn, billions of dollars in commercial debt needs to be refinanced in the next two years and there is no one willing to make those loans. Shopping mall vacancy rates have already reached 9.4 per cent, and rental income is plunging. Retail chains that have closed or will close include: Circuit City (728 stores), Linens N Things (500 stores), Bombay Company (384 stores), Sharper Image (184 stores), Foot Locker (140) and Pacific Sunwear (153). In all, approximately 700,000 retail jobs are expected to be lost in 2009.

Shopping malls are as American as apple pie, and as long as eager US consumers kept spending, developers kept building. But that bubble is about to burst, visiting a blight of what Quinn calls 'Ghost Malls' upon the urban landscape. Many developers are going to hit a brick wall in 2009 because they borrowed heavily to finance massive mall expansion and obtained their financing through short-term, highly levered CDO loans that are now coming due.

Yet the oncoming collapse in commercial real estate, as with housing before it, could have been prevented. All that was needed was a little foresight and monetary discipline from the Federal Reserve, but it's too late now. Merrill Lynch economist David Rosenberg sees rough sledding ahead for consumers and for the shopping malls that furnish their needs. "This is an epic event; we're talking about the end of a 20-year secular credit expansion that went absolutely parabolic from 2001-2007. Before the US economy can truly begin to expand again… we will probably have to eliminate $2 trillion of household debt." In other words, the process is just beginning.

The final casualty: the US dollar

All of this points to more bank failures, more foreclosures, more bankruptcies, more job losses, and more government deficits. Elevated deficits drive already-high debt loads even higher, and the higher the debt, the faster the depreciation of the dollar. As more and more investors begin to realize how much the US dollar and other currencies have depreciated over the past several decades, they will switch out of financial assets and into precious metals.

In last year's Annual Report, we said that the Fed was caught between a rock and a hard place because if they reduced interest rates to boost the economy, they would fuel inflation and send the dollar down. On the other hand, if they increased interest rates, they might keep inflation in check and boost the dollar, but they would seriously damage the economy. In actuality, they reduced rates to zero, but the dollar did not fall.

We were wrong about the US dollar in 2008 because we did not foresee the effects of sudden, massive and chaotic deleveraging and the weakness of other currencies. Investors bailed out of their highly leveraged positions in stocks and commodities and flocked to the safety of US government bonds and Treasuries. Since these were priced in US dollars, it put tremendous upward pressure on the dollar. But

"The **Government** should **allow** every **distressed bank** to go **bankrupt** and **set up a fresh banking system** under temporary **state control** rather than **cripple the country by** propping up a **corrupt edifice**."

- Joseph Stiglitz, former Senior Vice President and Chief Economist, World Bank.

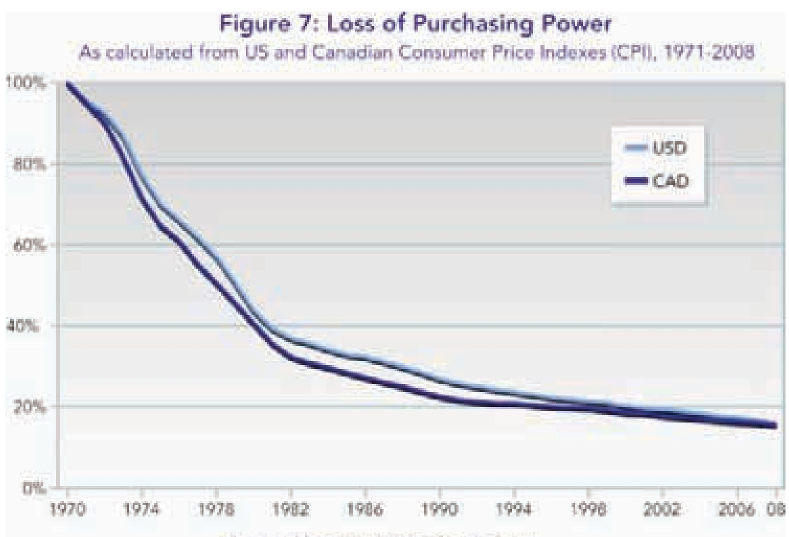
make no mistake: the dollar has never been more vulnerable. As deleveraging slows and government spending ramps up in 2009, the mountain of debt being created by governments around the world will drag the dollar's purchasing power against gold down, accelerating its losing streak.

The world's export-driven countries (America's creditors) are currently engaged in a new round of competitive currency devaluations designed to keep their exports attractively priced, but the retrenching US consumer is too far in debt to care. If global US creditors ever decide to curb their lending to America over fears that it cannot control its debt, it would be the beginning of the end. Without foreigners to finance its debt, the US would be forced into spiralling budget deficits and massive government spending cuts that would be catastrophic for the dollar.

Investors looking for safety will turn to precious metals

This scenario would see gold, silver and platinum surge in value since they are priced and traded in US dollars. In an environment where the dollar is weak and other currencies are weaker, investors seeking to preserve and grow their wealth in 2009 must rethink their investment strategy. The chart below (*Figure 7*) shows how much the Canadian and US dollar have declined in purchasing power since 1970. The world's other currencies have fared no better. It bears noting that in 1971, US President Richard Nixon "closed the gold window".

Along with its two precious metals brethren – silver and platinum – gold is the world's only non-depreciating currency, proven to hold its value in periods of both deflation and inflation.



"**Critical parts** of our financial system are **damaged**."

- Tim Geithner, US Treasury Secretary

Real wealth replaces wishful thinking

We are witnessing a global government spending spree of historic proportions. Coupled with zero per cent interest rates and enormous money supply growth, this will be extremely inflationary. While financial assets will continue to lose purchasing power, precious metals will hold theirs because they are a proven inflation hedge. In fact, they will continue to hold their purchasing power whether we experience deflation, inflation, stagflation or hyperinflation.

Gold in 2009: In 2008, stocks lost 30 per cent to 70 per cent of their value, while gold increased about 5 per cent in US dollars. In addition, during a year of record-setting volatility, gold's volatility was reassuringly low. At its lowest point, gold was down only 14 per cent; at its highest point, gold was up 21 per cent.

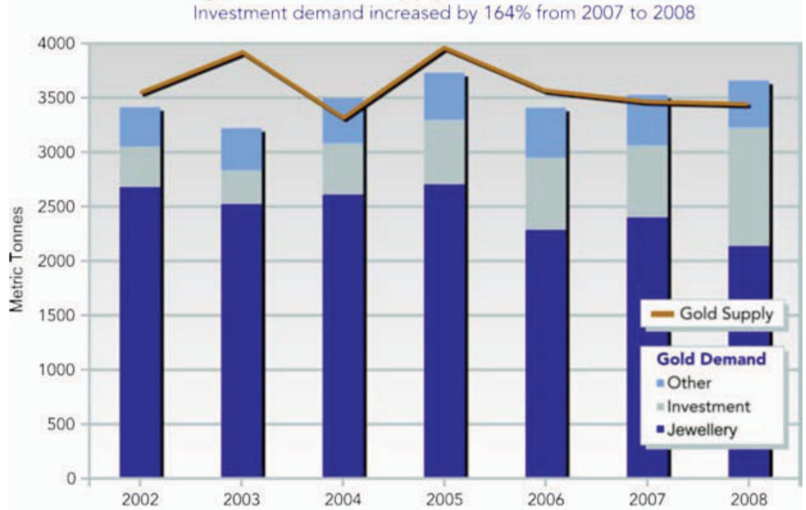
Gold production fell in 2008 and may fall further in 2009, due partly to a lack of exploration success. The gold mining industry discovered only 15 million ounces last year, compared to a production level of 80 million ounces. Both Goldman Sachs and UBS see gold rising in 2009, and UBS expects investment demand for gold *(see Figure 8)* to pull the price of silver and platinum up along with it.

Silver in 2009: The depth of the drop in silver prices in 2008 was surprising, but panic selling by hedge funds and other overleveraged investors may have forced prices to overshoot on the downside. At $13 per ounce, silver is undervalued by any measure, and is certainly underpriced against gold. Silver, along with gold, has a role as monetary metal and as a safe haven, and has been used as money in more regions and countries than gold. Most of the world's silver is now held by individual investors. The turnover rate of silver at the London Bullion Marketing Association (LBMA) has increased from $500 million per day in 2003 to approximately $1.05 billion per day in December 2008.

Silver is more volatile than gold, and just as silver out-performed gold on the way up, it has fallen more on the way down. Nevertheless, the underlying fundamentals for silver continue to improve, given its safe-haven attributes. Weak industrial demand in 2009 will likely be more than offset by increased investor demand. UBS has raised its forecast for silver in 2009 because, as gold moves higher, silver tends to follow. As with all three precious metals, the US dollar is a key factor; silver's price could soar if deteriorating financial conditions cause further dollar decline.

Figure 8: Global Supply and Demand for Gold

Investment demand increased by 164% from 2007 to 2008



Source: World Gold Council

Platinum in 2009: Platinum rarely trades at a discount to gold and when it does, the discounts are short-lived, says UBS, which recently raised its 2009 forecast for the metal. According to a study by Wainwright Economics, platinum is the leading indicator of inflation. While gold and silver lead inflation by 12 months, platinum leads by 16 months.

It appears that new demand for platinum may come as a result of new air pollution laws. Many jurisdictions now require diesel trucks be retrofitted with platinum-based particulate filters. Meanwhile, reports from India suggest that the jewellery industry is taking a renewed interest in the metal because of its recent price drop. Signs of safe-haven buying come from Japan where Tokyo-based bullion dealers have been forced to turn away customers because they are experiencing a drought of platinum ingots and coins.

Walking on a tightrope

In an inflationary environment, precious metals are the only currency that cannot be devalued. Governments can print infinite amounts of money, but they cannot increase the supply of gold, silver or platinum. As a result of the global financial crisis, the world's governments and central banks are walking on a tightrope. On one hand, failure to stimulate the economy could allow the deflationary spiral to intensify, leading to another Great Depression, or worse. On the other hand, stimulate too much, and we could be heading for uncontrolled hyperinflation where trillions in bad debt would be propped up by trillions of dollars in fiat money printed wantonly and paid for by taxpayers.

Inflation unleashed

The US government and the Fed have so far pledged $8.5 trillion and have spent $350 billion. When the bulk of its spending is underway, and the banks and other credit originators begin lending again, inflation will be unleashed in full force. Interestingly, inflation is something the Fed secretly embraces, because they know it can inflate away the crushing level of debt.

It is not just the US that is unleashing massive inflation. It will be a long-term problem for the world as a whole. According to a study by CIBC World Markets, a wave of government bailouts around the world combined with a deterioration in existing infrastructure could lead to as much as $35 trillion in public works spending over the next 20 years. Massive amounts of money need to be printed to fund these massive expenditures. And that means soaring inflation.

Today, most people view inflation as an increase in the cost of living as measured by the Consumer Price Index (CPI). However, the accurate definition of inflation is an increase in the money supply that leads to rising prices. Increasing money supply is the cause; increasing prices are the effect. In recent years, most industrialized countries have been increasing M3 by more than double the reported increases in the CPI.

The Fed, the Treasury and central banks and governments around the world are throwing everything at the crisis, which means money supply growth is going to be off the charts. If history is any guide, this will lead to a US dollar currency crisis. The

"A West **addicted to Ponzi credit** has put off the day of reckoning with ever **more extreme** monetary **policy** with each **downturn**."

- Ambrose Evans-Pritchard, former International Business Editor, Daily Telegraph destructive power of uncontrolled money expansion has already been experienced in Mexico, Brazil, Argentina, South-East Asia, Japan and Russia. Each experienced a major currency crisis accompanied by plunging stock markets and collapsing real estate markets, while many bonds and other debt instruments became worthless. However, precious metals prices increased dramatically during these currency crises, acting in their traditional safe-haven role.

If left unchecked, inflation can quickly lead to hyperinflation, generally defined as inflation in excess of a 4-digit annual percentage change. Hyperinflation creates a vicious circle in which the widespread desire to spend rapidly depreciating money results in skyrocketing prices that soon make the currency virtually worthless. In Zimbabwe today, an egg costs $50 billion Zimbabwe dollars. Will that be allowed to happen in the US or Canada? Perhaps not, but as inflation is unleashed by panicky policymakers, you can bet the cost of an egg will be much higher next year.

The quick fix

Just as it took years for the global economy to become imbalanced, it will take years for the economy to heal. There is no quick fix, but governments are trying anyway.

Quick fix I: Stimulus programs

As 2009 unfolds, stimulus packages are sprouting like mushrooms. If one government supports its financial sector, every country must do the same, because the world has become interconnected. That's why countries like Canada, supposedly a bastion of fiscal and monetary responsibility, are dropping interest rates and creating stimulus packages that, in Canada's case, will plunge the country into an $85-billion deficit over the next few years. It is amazing how quickly political strategy can change when economic matters intrude. Every one of Canada's political leaders pledged not to run a deficit during the recent federal election. But when the crisis hit full bore, all bets came off the table and deficits are the order of the day.

Prime Minister Stephen Harper's stimulus package is estimated at CDN$40 billion over the next two years, with much of the money to be spent on infrastructure projects such as roads, as well as incentives to encourage home improvements. In addition, the government is buying CDN$75 billion (increased from CDN$25 billion) of mortgage-backed securities from the banks. Interestingly, these were already government-insured, but the government is buying them outright to try and encourage the bankers to lend. But it is not clear what they are trying to accomplish, or how on top of the situation they really are.

"Whatever **actions** Washington takes **to save** the "**too big to fails**," they will **prove very costly** for the "**too small to saves**" who will be **forced** to foot the bills and **eat the losses**."

- Gerald Celente, Founder, Trends Research Institute

Incredibly, Bank of Canada Governor Mark Carney expects Canada's economy to resume growing in 2010, although he was quick to say his projections could be thrown off by decisions made by the US and other major economies. "There are so many unknowns out there, some positive, some negative... there's an enormous degree of uncertainty," he said. That may prove to be the understatement of the year. Just recently, the International Monetary Fund warned that the recession in Canada this year will be much deeper than the Canadian government is projecting and [2010's] recovery will be "a lot weaker than forecast by either the federal government or Bank of Canada."

European Union governments have so far spent $380 billion to recapitalize their banks and have guaranteed $3.18 trillion in loans of many European banks as well as neighbouring states. The numbers are sure to increase as the year goes on. But no matter how large the stimulus packages become, they will not make right what went so horribly wrong.

To put the rescue packages in perspective, the US bailout commitment of $8 trillion dollars is more than double the entire cost to the US of World War II ($3.6 trillion in inflation-adjusted dollars). See *Figure 9* for comparisons.

Quick fix II: Low interest rates

Conventional economic wisdom suggests that when a recession hits, interest rates should be lowered to stimulate the economy. The problem in 2008 was that interest rates were already low. But that didn't stop the Fed from lowering them further – to an unprecedented near-zero per cent. The effect of low interest rates may work in a conventional recession, but they have little effect in a downturn such as this one.

Quick fix III: Quantitative easing

When interest rates can't go any lower, central banks resort to what is euphemistically termed "quantitative easing": that is, printing money. Will Fed Chairman Ben Bernanke's quantitative easing policy solve the global financial crisis? Not likely. At zero per cent interest, Bernanke has one-upped what former Fed Chairman Alan Greenspan did in 2004 by giving the world the cheapest money it has ever had. But it is a grand illusion to think that the paper

Figure 9: Bailout in Perspective
Inflation Adjusted Costs

Bernanke is giving us – fiat money created by government decree – comes without a cost. The bailout and monetary policies will not work because they don't lower the debt and they don't cleanse the system of trillions in bad debt. Fund manager Jeremy Grantham says that write-downs of $1 trillion to $2 trillion aren't nearly enough to restore the system. He believes "somewhere between $10 trillion and $15 trillion of debt will have to disappear." That is a staggering number.

The consequences of the bailout

The most likely consequence of the bailouts is hyperinflation, although there is always the possibility of something never before encountered. Currently, we are experiencing what some refer to as deflation… not of the money supply but of asset values. The Fed will break this deflationary trend because they have an unlimited ability to print money and need to create trillions of dollars to pay for the huge bailouts. By that time it is entirely possible that we will be in the throes of a full-fledged depression. Many economists doubt the Fed will then be able to turn the money tap off as quickly as they turned it on, leading to a substantial depreciation of the dollar.

It is possible the world is entering an extended period of stagflation. Stagflation happens when slow growth occurs simultaneously with inflation, something which the Keynesians thought impossible until it happened not once but twice in the US, in the 1970s and early 1980s. Stagflationary cycles can be broken, but only by raising interest rates to punishing levels. Former Fed Chairman Paul Volcker did just that, at one point raising the federal funds rate as high as 20 per cent. But we would be very fortunate to have only stagflation.

If foreign creditors of US debt decide to abandon the dollar by selling off their depreciating assets on a large scale, the dollar will collapse and a potentially devastating hyperinflationary depression could set in, perhaps approaching that of Germany's Weimar Republic during the 1920s. At its peak, German inflation reached 3.25 million per cent per month. That means prices doubled every two days.

The only way to protect your wealth against deflation, stagflation, hyperinflation or the great unknown is by investing in non-depreciating assets that have intrinsic value; in other words, precious metals.

"In poker terms, the **Treasury and the Fed** have gone **'all in'**. Economic medicine that was previously **meted out by the cupful** has recently been **dispensed by the barrel**. These once-unthinkable dosages will almost certainly **bring** on unwelcome after effects - (an) **onslaught of inflation**."

- Warren Buffett, Chairman and CEO, Berkshire Hathaway

What percentage of my portfolio should be in physical bullion?

Precious metals not only protect portfolio purchasing power and shield against inflation, they can provide upside growth potential in an unstable economic environment. How much you should have in your portfolio depends on your time horizon and investing needs. Ibbotson Associates, the world-renowned asset allocation specialists, recommend between 7 per cent and 16 per cent just for proper diversification, while Wainwright Economics recommend between 18 per cent and 47 per cent in order to immunize portfolios against inflation.

To make money in these troubled times, you will need an even higher allocation in precious metals than those recommended by Ibbotson and Wainwright. But no matter what your allocation to bullion turns out to be, it should certainly not be zero. A portfolio without an allocation to bullion is not only highly risky but irresponsible.

Also, given the drop in mining stocks in 2008, it is critical for investors to hold actual physical bullion, not pooled accounts, paper proxies or derivatives. Allocated, segregated, physical bullion is one of the only assets that is not someone else's liability and not someone's promise of performance.

Bullion may be the only safe haven in 2009 as conditions are deteriorating even faster than economists expected. What started as a potentially bad recession is now showing signs of turning into a full-blown depression, says investment expert David Chapman. In order to adapt to current global changes, investors need to rethink their investment strategy and their portfolio allocations, because the next 20 years are going to be completely unlike the past 20.

Because gold is above all a monetary asset, over time it will rise as the US dollar weakens. And the US is doing everything in its power to avoid a depression, with zero per cent interest rates, massive fiscal stimulus and quantitative easing. All of these will weaken the dollar.

As noted earlier, precious metals are just a fraction of 1 per cent of the value of global financial assets.

Yet even after eight years of gains from $250 to $900 for gold, from $4 to $13 for silver and from $400 to $1,100 for platinum, most investors have no allocation to precious metals whatsoever. As a result, most portfolios are defenseless against the ravages of inflation, the likeliness of currency declines and further market declines. As investors begin to realize

"The **legacy of 2008** may be an enduring **suspicion – even disgust** – with the financial establishment and the **system's lack** of adequate **safeguards**."

- Financial Post

and understand this, even a small shift from the $195 trillion of financial assets into the $3 trillion of bullion will result in dramatic price increases, and may ultimately lead to shortages of even the largest bullion bars.

The Dow:Gold ratio confirms gold's rise

The Dow:Gold ratio shows the cost of the Dow divided by the price of an ounce of gold. When the ratio is falling (as it has been since 2000), it is time to increase allocations to gold and other hard assets and to sell stocks. When it is rising, it is time to increase allocations to stocks and sell gold. As you can see from *Figure 10* below, the Dow:Gold ratio approached parity (1:1) in 1932 and in 1980. In 2000, it took 44 ounces of gold to "buy the Dow". Today, it only takes 8.4 ounces, as the purple line clearly indicates. This means we are in a long-term bear market for stocks, and a long-term bull market for gold.

Whether Dow-to-gold parity is $5,000, $20,000, or some other price point is not important. All that matters to gold investors is the purchasing power of their gold investment. And gold's purchasing power continues to rise.

Gold surpasses the S&P 500

For the first time in 17 years, the price of gold has risen above the S&P 500 index, further evidence that gold is in an uptrend and stocks are in decline. On January 20, 2009, the London PM fix for gold was $853 while the S&P 500 closed at 805. The chart on the next page *(Figure 11)* show the two trend lines intersecting.

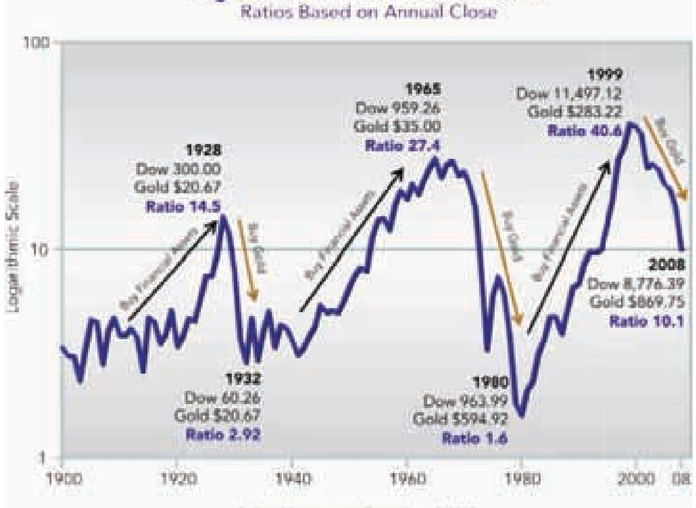
The beginning of the end

It is the beginning of the end of wishful thinking for most investors – all except those who are invested in real wealth: gold and precious metals. The banking system is broken, the credit markets are not working and the system needs to be replaced. Is recovery around the corner? Not even Treasury Secretary Tim Geithner thinks so. "Instead of catalyzing recovery, the financial system is working against recovery," he announced in his inaugural speech.

Now that we are in the throes of the crisis, don't expect any objective advice from Wall Street. Even at the end of 2008, after the markets crashed by the worst percentage since the Great Depression, analysts had a sell rating on only 5.9 per cent of stocks.

Figure 10: The Dow:Gold Ratio

Ratios Based on Annual Close



Precious metals investors understand that for true portfolio protection in a secular bear market, their asset allocation strategy must be diversified to include a sizeable portion of gold, silver and platinum.

It is very hard to see change when we are right in the middle of it, but wrenching change is happening all around us. Over the next few years, soaring inflation will send the US dollar into rapid decline, but precious metals will continue to hold their purchasing power.

Global investors looking to currencies that are stronger than the dollar will realize there are none. Most foreign central banks will follow the US lead and debase their currencies in a vain attempt to spend their way out of recession. The result will be an ongoing round of competing currency devaluations where all paper currencies will decline relative to gold, silver and platinum.

Precious metals will be the only currency that survives intact because while governments can print infinite amounts of money, they cannot increase the supply of hard assets with intrinsic value. Eventually, the threadbare financial system will be revealed to all as a fragile house of cards. Investors, institutions and central banks will turn in droves to the historical safe haven of precious metals as real wealth replaces wishful thinking.

** All amounts in US dollars, unless otherwise noted.*

"Investors seeking to **preserve and grow** their **wealth** in 2009 must **rethink** their investment **strategy**. In an inflationary environment, **precious metals** are the **only currency** that **cannot be devalued**."

- Nick Barisheff

FINANCIAL STATEMENTS

AUDITORS' REPORT

To the Unitholders of BMG BullionFund

We have audited the statements of net assets and investment portfolio of BMG BullionFund as at December 31, 2008 and the statements of operations and changes in net assets for the year then ended. These financial statements are the responsibility of the Fund's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these financial statements present fairly, in all material respects, the net assets and investments held by the Fund as at December 31, 2008 and the results of its operations and the changes in its net assets for the year then ended in accordance with Canadian generally accepted accounting principles.

The comparative figures for December 31, 2007 were reported on by another firm of chartered accountants.

KPMG LLP

Chartered Accountants, Licensed Public Accountants
Toronto, Canada
January 16, 2009

STATEMENTS OF NET ASSETS

As at December 31	2008 $	2007 $
ASSETS		
Gold, silver and platinum bullion, at market value	**203,662,863**	124,039,219
(Average cost: $190,525,136; 2007 - $98,265,397)		
Cash	**2,313,810**	1,613,902
Subscriptions receivable	**466,737**	176,229
Accounts receivable	**615**	–
	206,444,025	125,829,350
LIABILITIES		
Management fees payable	**355,088**	225,358
Accounts payable and accrued liabilities	**374,065**	354,328
Redemptions payable	**93,427**	264,210
	822,580	843,896
Net assets represented by unitholders' equity	**205,621,445**	124,985,454
Class A	**156,147,446**	92,851,312
Class E09	**136,851**	322,159
Class E10	**423,239**	–
Class E11	**4,179,370**	4,298,173
Class E15	**2,456,620**	–
Class F	**11,990,640**	8,937,600
Class G01	**15,067,975**	9,001,835
Class G05	**998,332**	1,362,608
Class G09	**4,425,875**	1,370,581
Class G10	**1,513,573**	1,115,657
Class G11	**8,281,524**	5,725,529
	205,621,445	124,985,454
Net assets per unit		
Class A	**8.07**	8.41
Class E09	**8.45**	8.72
Class E10	**8.46**	–
Class E11	**8.53**	8.77
Class E15	**8.56**	–
Class F	**8.46**	8.72
Class G01	**8.13**	8.48
Class G05	**8.73**	9.05
Class G09	**8.37**	8.62
Class G10	**8.32**	8.57
Class G11	**8.39**	8.62

See accompanying notes

On behalf of the Board of Directors of Bullion Management Services Inc.,
Trustee and Manager, BMG BullionFund:

Nick Barisheff,
Director

Larry Gamble,
Director

STATEMENTS OF OPERATIONS

Year ended December 31	2008 $	2007 $
REALIZED AND UNREALIZED GAIN (LOSS) ON INVESTMENTS		
Net realized loss on investments	**(101,667)**	–
Net realized gain (loss) on foreign exchange	**257,278**	(23,620)
Change in unrealized appreciation (depreciation) of investments	**(12,622,997)**	7,032,291
Net gain (loss) on investments	**(12,467,386)**	7,008,671
INVESTMENT INCOME		
Early redemption fees	**337,723**	37,937
Interest income	**10,054**	7,679
	347,777	45,616
EXPENSES		
Management fees *(note 4)*	**3,652,096**	2,180,365
Securityholder reporting costs	**752,755**	565,698
Bullion storage fees	**644,616**	342,765
Goods and Services Tax	**263,575**	193,230
Other administrative expenses	**50,257**	41,704
Legal fees	**77,528**	77,516
Audit fees	**87,095**	52,317
Interest and bank charges	**2,628**	754
	5,530,550	3,454,349
Net investment loss for the year	**(5,182,773)**	(3,408,733)
Increase (decrease) in net assets from operations	**(17,650,159)**	3,599,938
Increase (decrease) in net assets from operations per class		
Class A	**(12,478,775)**	2,380,865
Class E09	**36,669**	2,159
Class E10	**(100,965)**	–
Class E11	**(118,803)**	159,208
Class E12	**(64,823)**	–
Class E15	**(1,767,901)**	–
Class F	**(815,773)**	320,348
Class G01	**(1,414,632)**	395,724
Class G05	**(246,628)**	22,510
Class G09	**(341,877)**	42,958
Class G10	**(146,829)**	13,436
Class G11	**(189,822)**	262,730
Increase (decrease) in net assets from operations per unit		
Class A	**(0.83)**	0.24
Class E09	**1.69**	0.06
Class E10	**(2.02)**	–
Class E11	**(0.24)**	0.32
Class E12	**(0.34)**	–
Class E15	**(2.77)**	–
Class F	**(0.68)**	0.33
Class G01	**(1.03)**	0.53
Class G05	**(1.42)**	0.12
Class G09	**(1.11)**	0.27
Class G10	**(0.88)**	0.11
Class G11	**(0.26)**	0.44

See accompanying notes

STATEMENTS OF CHANGES IN NET ASSETS

Years ended December 31	Class A		Class E09	
	2008	2007	**2008**	2007
	$	$	**$**	$
Net assets, beginning of year	**92,851,312**	66,299,404	**322,159**	–
Increase (decrease) in net assets from operations	**(12,478,775)**	2,380,865	**36,669**	2,159
Capital transactions				
Proceeds from issuance of units	**98,532,265**	34,954,436	**302,227**	320,000
Redemption of units	**(22,757,356)**	(10,783,393)	**(524,204)**	–
	75,774,909	24,171,043	**(221,977)**	320,000
Net assets, end of year	**156,147,446**	92,851,312	**136,851**	322,159

	Class E10		Class E11	
	2008	2007	**2008**	2007
	$	$	**$**	$
Net assets, beginning of year	**–**	–	**4,298,173**	4,138,965
Increase (decrease) in net assets from operations	**(100,965)**	–	**118,803**	159,208
Capital transactions				
Proceeds from issuance of units	**524,204**	–	**–**	–
Redemption of units	**–**	–	**–**	–
	524,204	–	**–**	–
Net assets, end of year	**423,239**	–	**4,179,370**	4,298,173

	Class E12		Class E15	
	2008	2007	**2008**	2007
	$	$	**$**	$
Net assets, beginning of year	**–**	–	**–**	–
Increase (decrease) in net assets from operations	**(64,823)**	–	**(1,767,901)**	–
Capital transactions				
Proceeds from issuance of units	**1,679,242**	–	**7,955,303**	–
Redemption of units	**(1,614,419)**	–	**(3,730,782)**	–
	64,823	–	**4,224,521**	–
Net assets, end of year	**–**	–	**2,456,620**	–

Years ended December 31	Class F		Class G01	
	2008	2007	**2008**	2007
	$	$	**$**	$
Net assets, beginning of year	**8,937,600**	7,758,537	**9,001,835**	559,061
Increase (decrease) in net assets from operations	**(815,773)**	320,348	**(1,414,632)**	395,724
Capital transactions				
Proceeds from issuance of units	**8,417,708**	3,247,296	**8,718,617**	8,739,841
Redemption of units	**(4,548,895)**	(2,388,581)	**(1,237,845)**	(692,791)
	3,868,813	858,715	**7,480,772**	8,047,050
Net assets, end of year	**11,990,640**	8,937,600	**15,067,975**	9,001,835

	Class G05		Class G09	
	2008	2007	**2008**	2007
	$	$	**$**	$
Net assets, beginning of year	**1,362,608**	1,826,636	**1,370,581**	1,307,175
Increase (decrease) in net assets from operations	**(246,628)**	22,510	**(341,877)**	42,958
Capital transactions				
Proceeds from issuance of units	**1,143,585**	199,909	**4,275,846**	287,583
Redemption of units	**(1,261,233)**	(686,447)	**(878,675)**	(267,135)
	(117,648)	(486,538)	**3,397,171**	20,448
Net assets, end of year	**998,332**	1,362,608	**4,425,875**	1,370,581

	Class G10		Class G11	
	2008	2007	**2008**	2007
	$	$	**$**	$
Net assets, beginning of year	**1,115,657**	522,251	**5,725,529**	4,563,824
Increase (decrease) in net assets from operations	**(146,829)**	13,436	**(189,822)**	262,730
Capital transactions				
Proceeds from issuance of units	**544,846**	580,088	**3,523,581**	1,326,333
Redemption of units	**(101)**	(118)	**(777,764)**	(427,358)
	544,745	579,970	**2,745,817**	898,975
Net assets, end of year	**1,513,573**	1,115,657	**8,281,524**	5,725,529

STATEMENTS OF CHANGES IN NET ASSETS *(continued)*

Years ended December 31	**Total**	Total
	2008	2007
	$	$
Net assets, beginning of year	**124,985,454**	86,975,853
Increase (decrease) in net assets from operations	**(17,650,159)**	3,599,938
Capital transactions		
Proceeds from issuance of units	**135,617,424**	49,655,486
Redemption of units	**(37,331,274)**	(15,245,823)
	98,286,150	34,409,663
Net assets, end of year	**205,621,445**	124,985,454

See accompanying notes

STATEMENT OF INVESTMENT PORTFOLIO

As at December 31

Description	Allocated ounces	Unallocated ounces	Total Fine ounces	Average Cost	Market Value	Total
				$	$	%
2008						
Gold Bullion	82,656.657	1,025.090	83,681.747	**63,523,900**	**89,850,130**	**44.11**
Platinum Bullion	41,811.802	2,617.132	44,428.934	**63,360,124**	**49,582,821**	**24.35**
Silver Bullion	4,592,939.112	229,006.941	4,821,946.053	**63,641,112**	**64,229,912**	**31.54**
Total Investment Portfolio				**190,525,136**	**203,662,863**	**100.00**
2007						
Gold Bullion	49,903.242	826.987	50,730.229	**32,617,675**	**41,744,467**	**33.65**
Platinum Bullion	25,750.716	398.662	26,149.378	**32,763,182**	**39,486,536**	**31.83**
Silver Bullion	2,901,938.252	36,689.189	2,938,627.441	**32,884,540**	**42,808,216**	**34.52**
Total Investment Portfolio				**98,265,397**	**124,039,219**	**100.00**

The Fund's gold, silver and platinum bullion is held under a custodial agreement for the Fund by a major Canadian Chartered Bank(or subsidiary thereof) on an allocated, segregated basis.

The allocated bullion is recorded by Refinery, Exact Weight in Ounces and Identification Number.

The Fund's bullion is free and clear of any lien or claim which the major Canadian Bank (or subsidiary thereof) may have, except where the claim arises from any unpaid costs.

Year ended December 31, 2008

1. FORMATION OF THE FUND

BMG BullionFund (the "Fund"), formerly known as The Millennium BullionFund, was established under the laws of Ontario by a master Declaration of Trust and Regulation each dated January 15, 2002, as amended. Bullion Management Services Inc. is the Trustee and Manager of the Fund. The Fund currently offers 11 classes of units. These financial statements pertain to Class A, Class E09, Class E10, Class E11, Class E15, Class F, Class G01, Class G05, Class G09, Class G10 and Class G11. Effective April 16, 2007 Class E01 was renamed Class E11. Effective February 21, 2008 Class E10 units were issued, effective September 18, 2008 Class E12 units were issued and effective April 04, 2008 Class E15 units were issued. All classes share the same attributes from a valuation perspective except that they are subject to different management fee rates.

The Fund is also authorized to issue Class I units, none of which were issued during 2008.

The Fund invests only in equal proportions of unencumbered, gold, silver and platinum bullion, with the objective of providing a secure, convenient, low-cost, low-risk alternative for investors seeking to hold bullion for capital preservation, long-term appreciation, portfolio diversification and portfolio hedging purposes. The Fund's purchase-and-hold investment strategy and fixed purchase allocation to each bullion type eliminates the need for a portfolio manager.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The financial statements have been prepared in accordance with Canadian generally accepted accounting principles and include estimates and assumptions made by the Manager that affect the amounts of assets, liabilities, income and expenses during the reporting periods. The significant accounting policies are summarized below:

Valuation of investments

Gold, silver and platinum bullion are valued at the London PM fix price with the difference between this amount and the average cost being shown as unrealized appreciation (depreciation) of investments.

The market values of investments denominated in foreign currencies are translated into Canadian dollars at the rates of exchange applicable on the valuation date.

Investment transactions, income and expense recognition

Bullion transactions are recorded on a trade date basis.

Purchases and sales of investments and income and expenses are translated into Canadian dollars at the exchange rates prevailing on the dates of the transactions.

The realized gain or loss on sale of investments is calculated with reference to the average cost of the related investments.

The Fund follows the daily accrual method of recording investment income and expenses. Expenses specifically related to each class of units are charged directly to the class. Other expenses are allocated proportionately to each class based on the average net asset value ("NAV") of each class.

Income, and realized and unrealized gains (losses) are allocated to each class of the Fund based on the class's pro-rated share of total net assets of the Fund.

Calculation of Net Asset Value per unit

The NAV of each class of units of the Fund is calculated in Canadian dollars at 4:00 pm (Eastern Time) on each day on which The London Stock Exchange and The Toronto Stock Exchange are open for trading.

The NAV per unit used for purchases and redemptions is the same as the financial statement net assets per unit.

A separate NAV is calculated for each class of units of the Fund by taking the class' proportionate share of the Fund's common assets less that class' proportionate share of the Fund's common liabilities and deducting from this amount all liabilities that relate solely to the specific class. The NAV per unit for each class is determined by dividing the NAV of each class by the number of units of that class outstanding at the valuation date.

Income taxes

Any net taxable investment income and net realized capital gains during the year are distributed to the unitholders such that the Fund is not subject to income tax. Accordingly, no provision for income taxes has been recorded in these financial statements.

Increase (decrease) in net assets from operations per unit
Any increase (decrease) in net assets from operations per unit in the Statements of Operations represents the net assets from operations attributable to a class of units for the period divided by the weighted average number of units of that class outstanding during the year.

Adoption of New Accounting Standards
On January 1, 2008 the Fund adopted CICA Handbook Section 1535, Capital Disclosures. Section 1535 specifies the disclosure of (i) an entity's objectives, policies and processes for managing capital; (ii) quantitative data and qualitative information about what the entity regards as capital; (iii) whether the entity has complied with any capital requirements; and (iv) if it has not complied, the consequences of such non-compliance. The adoption of Section 1535 did not have a significant impact on the Fund's disclosures as (i) the Fund's objectives, policies and processes are described in Note 1; (ii) information on the Fund's unitholders' equity is described in Note 3; and (iii) the Fund does not have any externally imposed capital requirements.

On January 1, 2008, the Fund adopted CICA Handbook Section 3862, "Financial Instruments – Disclosures" and Section 3863, "Financial Instruments – Presentation". The new standards replaced Section 3861, "Financial Instruments – Disclosure and Presentation". These sections establish standards for the comprehensive disclosure and presentation requirements of financial instruments. The standards include new requirements to quantify certain risk exposures and to provide sensitivity analysis for certain risks (see Note 6).

Future Accounting Changes
The Canadian Accounting Standards Board has announced plans to converge Canadian generally accepted accounting principles with those of the International Financial Reporting Standards ("IFRS"), over a transition period expected to end in 2011. The Fund Manager has been reviewing the transitional requirements and comparing IFRS with current Canadian standards as the initial steps in its changeover plan to meet the 2011 timetable. Key elements of the plan include disclosures of the qualitative impact in December 31, 2008, 2009 and 2010 financial statements, disclosures of the quantitative impact, if any, in the December 31, 2010 financial statements and the preparation of the December 31, 2011 financial statements in accordance with IFRS.

Based on the Fund Manager's current evaluation of the differences between Canadian standards and IFRS, the Fund Manager does not expect that net assets attributable to units or net asset value per unit will be impacted by the changeover to IFRS. Currently, the Manager expects that the impact of IFRS on the Funds' financial statements will result in additional disclosures and potentially different presentation of unit interests and certain other items.

3. UNITHOLDERS' EQUITY

Each unit of each class of the Fund represents an interest in the assets of that class of the Fund. All units of a class of the Fund generally have the same rights and privileges. Each unit of each class of the Fund is entitled to one vote at any meeting of unitholders of the Fund. Each unit of each class of the Fund is also entitled, subject to any management fee distributions, to participate equally in any distributions by the Fund. Fractional units of a class of the Fund are proportionately entitled to all the same rights as other units of that class of the Fund, except that they are non-voting. All units of each class of the Fund are fully paid when issued, and are generally not transferable. Units of each class of the Fund are redeemable at the option of the unitholder owning such units. The number of units of the Fund which may be issued is unlimited. The units of each class of the Fund are issued and redeemed at the net asset value per unit of that class of the Fund.

Unit transactions during the years ended December 31 were as follows:

	Class A		**Class E09**	
	2008 $	2007 $	**2008 $**	2007 $
Balance, beginning of year	**11,038,996**	8,082,540	**36,945**	–
Issued	**10,931,477**	4,292,583	**29,286**	36,945
Redeemed	**(2,616,387)**	(1,336,127)	**(50,043)**	–
Balance, end of year	**19,354,086**	11,038,996	**16,188**	36,945
Average units outstanding	**15,061,426**	9,883,584	**21,675**	36,945

	Class E10		Class E11	
	2008	2007	**2008**	2007
	$	$	**$**	$
Balance, beginning of year	**–**	–	**490,221**	490,221
Issued	**50,043**	–	**–**	–
Redeemed	**–**	–	**–**	–
Balance, end of year	**50,043**	–	**490,221**	490,221
Average units outstanding	**50,043**	–	**490,221**	490,221

	Class E12		Class E15	
	2008	2007	**2008**	2007
	$	$	**$**	$
Balance, beginning of year	**–**	–	**–**	–
Issued	**217,372**	–	**749,620**	–
Redeemed	**(217,372)**	–	**(462,775)**	–
Balance, end of year	**–**	–	**286,845**	–
Average units outstanding	**–**	–	**637,768**	–

	Class F		Class G01	
	2008	2007	**2008**	2007
	$	$	**$**	$
Balance, beginning of year	**1,024,903**	921,562	**1,062,143**	67,630
Issued	**888,439**	388,300	**919,950**	1,082,045
Redeemed	**(495,499)**	(284,959)	**(129,593)**	(87,532)
Balance, end of year	**1,417,843**	1,024,903	**1,852,500**	1,062,143
Average units outstanding	**1,202,402**	985,474	**1,366,948**	747,147

	Class G05		Class G09	
	2008	2007	**2008**	2007
	$	$	**$**	$
Balance, beginning of year	**150,551**	208,083	**158,956**	157,128
Issued	**115,133**	22,721	**458,598**	35,083
Redeemed	**(151,351)**	(80,253)	**(88,487)**	(33,255)
Balance, end of year	**114,333**	150,551	**529,067**	158,956
Average units outstanding	**173,085**	185,691	**307,208**	158,393

	Class G10		Class G11	
	2008	2007	**2008**	2007
	$	$	**$**	$
Balance, beginning of year	**130,190**	63,209	**663,946**	549,106
Issued	**51,698**	66,995	**408,780**	164,535
Redeemed	**(10)**	(14)	**(85,137)**	(49,695)
Balance, end of year	**181,878**	130,190	**987,589**	663,946
Average units outstanding the year	**166,203**	123,767	**741,508**	593,993

4. MANAGEMENT FEES AND SALES COMMISSION

The Manager is responsible for the day-to-day activities of the Fund, providing or arranging for all required administrative services and arranging for the distribution of units of the Fund. For these services, the Fund pays the Manager an annual management fee of 2.25% for Class A, 1.25% for Class E09, 1.125% for Class E10, 1.00% for Class E11, 0.875% for Class E12, 0.50% for Class E15, 1.25% for Class F, 2.25% for Class G01, 1.75% for Class G05, 1.25% for Class G09, 1.125% for Class G10, 1.00% for Class G11 payable monthly in arrears and based on the average daily NAV of the Fund.

A sales commission may be charged by a registered dealer or representative at the time investors buy Class A units, Class E units or Class G units of the Fund. The maximum amount of the sales commission is 5.26% of the net amount invested. The sales commission is negotiable. No sales commission is charged for the other class of units of the Fund.

The Manager paid trailer fees to dealers of $1,341,172 (2007: $607,001).

5. INCOME TAX LOSS CARRY FORWARDS

The Fund has non-capital loss carry forwards of approximately $11,516,000 (2007: $6,489,000) available to offset future years' taxable income.

Non-capital losses expire in the taxation year ending December 31:

Year	$
2009	33,000
2010	365,000
2014	857,000
2015	914,000
2026	888,000
2027	3,432,000
2028	5,027,000

6. FINANCIAL RISK MANAGEMENT

The Fund's financial instruments consist primarily of cash and bullion investments. The Fund's bullion holdings are exposed to various types of risks including market risk, credit risk and liquidity risk. These risks and related risk management practices employed by the Fund are described below:

Market Risk

Market risk is the risk that the fair value or future cash flows of bullion investments will fluctuate because of changes in market prices, currency or transaction timing. The market price of gold, silver and platinum is impacted by a variety of factors including demand, supply, international events and economic events. The Fund employs a purchase and hold investment strategy with purchases allocated one-third to each metal. Since the Fund does not lease bullion the only future cash flows will be from dispositions of bullion. Dispositions of bullion will be necessary to pay redemptions when cash reserves are not adequate.

Bullion is usually quoted and traded in U.S. dollars and, as a result, the Fund is vulnerable to foreign currency risk. The Fund does not hedge its foreign currency exposure.

The Fund holds cash in Canadian and U.S. dollars to pay redemptions and operating costs. The Manager monitors the cash balance on a daily basis and only purchases bullion when surplus cash is available. Normally the cash balance is less than 5 per cent of the assets of the Fund.

Credit Risk
As at December 31, 2008 the Fund had no significant investments in debt instruments and/or derivatives. The Fund limits its exposure to credit loss by placing its cash and cash equivalents in high credit quality issuers. Dispositions of bullion, if any, are with a major Canadian Chartered Bank (or subsidiary thereof) which is a recognized dealer in bullion.

Liquidity Risk
The Fund is exposed to daily cash redemptions of redeemable units. The Fund aims to retain sufficient cash and cash equivalent positions to maintain liquidity. In addition, bullion is readily realizable and liquid. Therefore the Fund's liquidity risk is minimal. All liabilities are payable within a year.

Market Sensitivity
As at December 31, 2008, the impact on the Fund's net assets of a 5% increase, or decrease, in the price of gold, silver and platinum bullion, with all other variables held constant, would be an increase, or decrease, of $10,183,143 or 4.95%. The actual result will vary depending upon the quantity of bullion held and other factors.

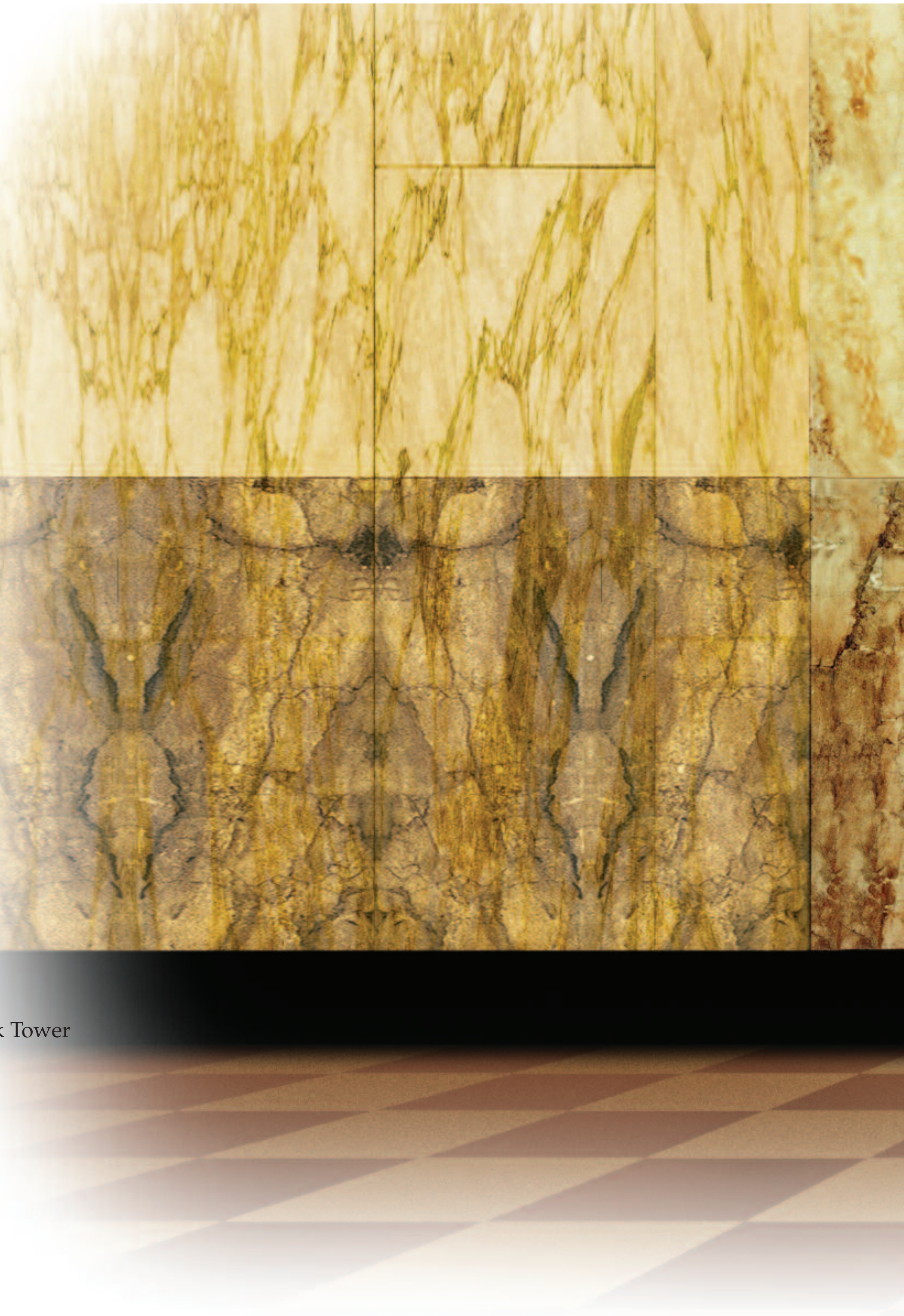
As at December 31, 2008, 99.6% of the Fund's net assets were exposed to U.S. dollars. If the exchange rate with the Canadian dollar increased or decreased by 1%, with all other variables held constant, net assets would have increased or decreased, respectively, by approximately $2,047,390.

The actual result may differ from this sensitivity analysis and the difference could be material as the price of bullion tends to be negatively correlated with the U.S. dollar.

Description	US	Canada	Total $
Cash	1,167,153	1,146,657	2,313,810
Bullion	203,662,863	–	203,662,863
Other net assets	(91,010)	(264,218)	(355,228)
Net assets	204,739,006	882,439	205,621,445
Percent	**99.6%**	**0.4%**	

The forward-looking information, opinions, estimates and projections contained herein are solely those of Bullion Management Services Inc. (BMS) and are subject to change without notice. BMS makes every effort to ensure that the information has been derived from sources believed to be reliable and accurate. However, BMS assumes no responsibility for any losses or damages, whether direct or indirect, which arise out of the use of this information. The information should not be regarded by recipients as a substitute for the exercise of their own judgment. Commissions, trailing commissions, management fees and expenses all may be associated with an investment in BMG BullionFund™. Please read the prospectus before investing. BMG BullionFund™ is not guaranteed, its units fluctuate in value and past performance may not be repeated.

CORPORATE INFORMATION



MANAGER

Head Office

Bullion Management Services Inc.
60 Renfrew Drive, Suite 280
Markham, ON L3R 0E1
Tel: 905.474.1001
www.bmginc.ca
info@bmginc.ca

Vancouver Office

Park Place
Burrard Street, Suite 500
Vancouver, BC V6C 3P6
Tel: 1.888.474.1001 x44

CUSTODIAN

ScotiaMocatta
The Bank of Nova Scotia
Scotia Plaza
40 King Street West
Toronto, ON M5W 2X6

ADMINISTRATOR

RBC Dexia Investor Services Trust
77 King Street West, 7th Floor
Toronto, ON M5W 1P9

AUDITORS

KPMG LLP
Commerce Court West
199 Bay Street, Suite 3300
Toronto, ON M5L 1B2

LEGAL COUNSEL

Fasken Martineau DuMoulin LLP
66 Wellington Street West
Suite 4200,Toronto-Dominion Bank Tower
Box 20,Toronto-Dominion Centre
Toronto, ON M5K 1N6

BMG

BULLION
MANAGEMENT
SERVICES INC.