

Evidence that the Market Correction is Underway

**Geological Society of Nevada
Silver Summer Series 2009**

**Douglas B. Silver
Chairman and CEO
International Royalty Corporation**



Agenda

- **Thesis I – Great Depression II has arrived**
- **Thesis II – Economic Recovery is underway**
- **Global outlook for the Mining Industry**

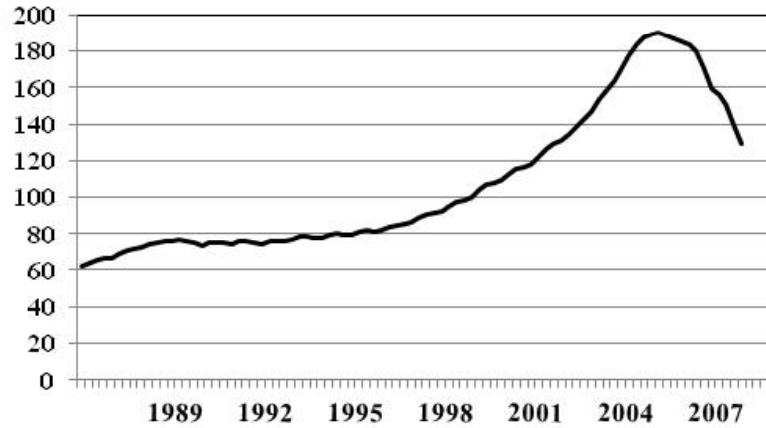
Great Depression II

- **Economic slowdown of massive proportions**
- **US industry used 68.3% of available capacity in May 2009.**
 - **Prior lowest rate was 70.9% in December 1982.**
 - **Similar trajectories to 1929.**
- **32/46 states do not have signed budgets: \$121 B deficit gap**
- **US corporate income tax receipts plunged 57% in 2009 (9 months)**
- **22% drop in individual income taxes paid (9 months)**
- **US government spent \$2.67 T but only collected \$1.59 T**
- **Unemployment rate is double digits (6.9 million people)**
- **6:1 people looking for work wrt job openings (2:1 in 2008)**

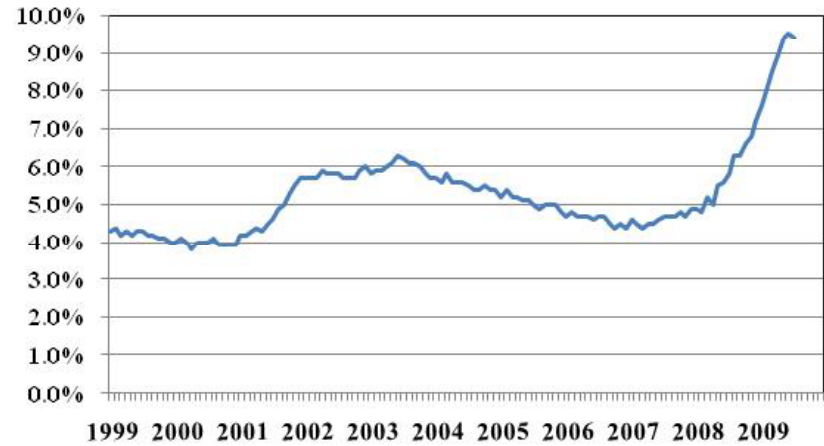
Great Depression II

- **New home sales down 33% (May on May)**
- **New home sales down 73% from all time high in 2005**
- **24% of single-family home mortgages have negative equity**
- **Foreclosures not expected to peak until the end of next year**
- **Foreclosure re-sales made up 22% of all sales in June 2009**
- **Rail car loading down 19.2% YOY (Lots of idled railroad cars)**
- **DJIA retracing the 1929 chart**
- **US Debt currently \$12 trillion on its way to \$20 trillion**
- **IPO of BigGovernment Inc.**

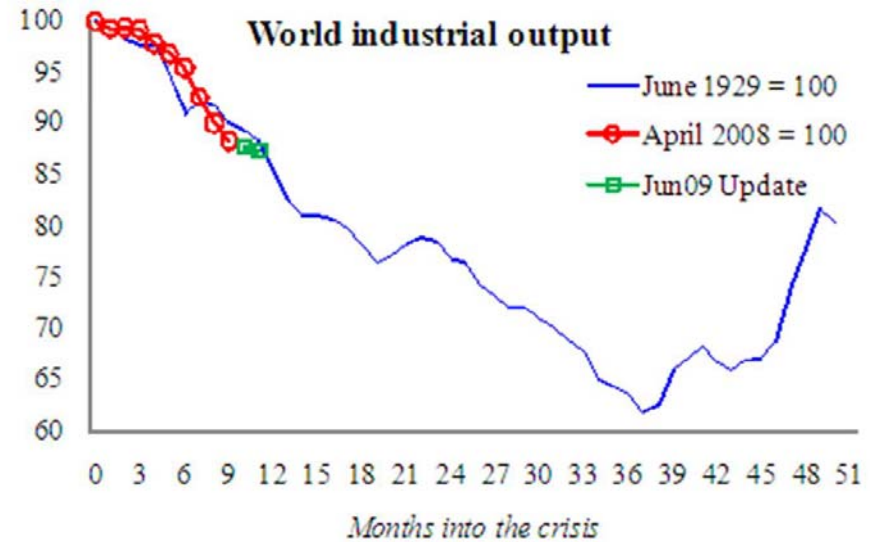
Case-Shiller House Price Index



Unemployment Rate

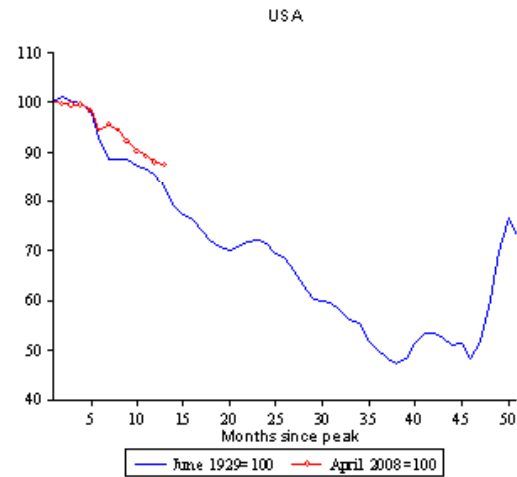
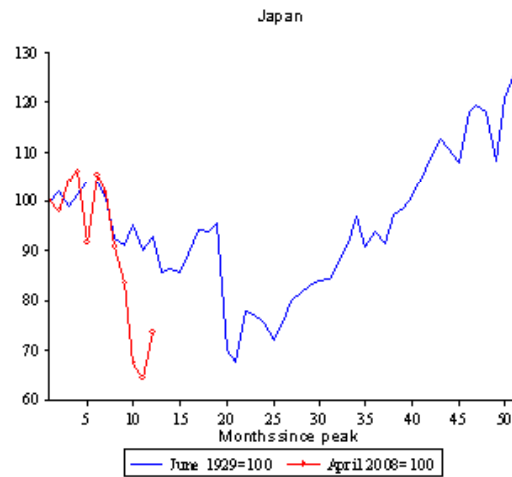
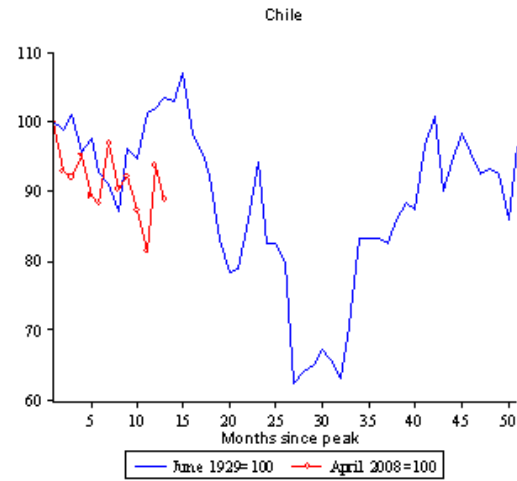
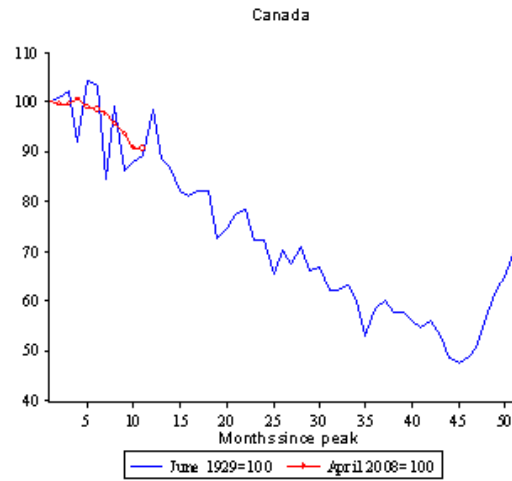


Michigan Sentiment Index



MSI requires a 90 to be in a growth phase

1929 Versus 2008



What shape will the Recovery take?

V shaped?	Lasting 8 months with quick rebound
U shaped?	Long (24 months) and deep with a slow recovery
W shaped?	Multiple setbacks before Recovery can gain traction
Q shaped?	Round and round with no sign of recovery and then suddenly recovery
Square root shaped?	Big collapse, rebound, flatten out at lower level than prior level
L shaped	Cynics only

Pimco – “The New Normal”

The New Normal Economy – a new equilibrium is being established

- **Lower potential growth for the global economy**
- **Lower export demand**
- **Reversal of global capital flows**

Professor Nouriel Roubini

Roubini believes this is the worst recession in 60 years

- **3 X longer than the previous 2 recessions**
- **5 X deeper (cumulative decline in output) than the previous recessions)**
- **Believes the recession will bottom out in 2H 2009**
- **Believes recession could be a U or W shape.**

Professor Nouriel Roubini teaches at the Stern School of Business at NYU

The Next Shoe to Drop?

- **Increase in commercial building loan defaults?**
- **Weakened US dollar could lead to double recession**
- **China asset bubble?**
- **California goes bankrupt**
- **Eased banking stress tests / slacker accounting standards hides the problem leading to another bank(s) blowup.**
- **European banks contemplating suspending preferred dividends**
- **Federal policy changes – Do they get the timing right on tightening interest rates (they didn't in 1937 and needed a war to recover)**
- **Every major economic crisis uses war to change the rules.**
 - **US invasion of Iran?**

The Great Recovery is Underway

Wall Street Survey, published August 12, 2009

- 27/47 Economists surveyed said the recession was over**
- 3Q growth projected to be 2.4% (Cash for Clunkers is working)**
- Unemployment fell in July; first time in 15 months**

**“The United States economy is now out of the emergency room and appears to be on a slow path to recovery”
-- Warren Buffett**

Reference: Warren Buffett, “The Greenback Effect,” Op-ed piece in the Wall Street Journal, August 18, 2009

The Great Recovery is Underway

Second quarter GDP results

China	+14.9%
France	+1.4%
Germany	+1.3%
Euro Zone	-0.4%
United States	-1.0%
Italy	-1.9%
United Kingdom	-3.2%

Other Recovery Indicators

- **US durable goods orders rose 1.9%, largest gain since December 2007.**
- **US construction has increased three months in a row (March – May)**
- **Several TARP borrowers have repaid their loans.**
- **Rate of home value declines has slowed: 1st time since Fall 2007**
- **Association of American Railroads reports increase in month-to-month carload gains (albeit still less than normal)**
- **China stimulus package appears to be working**
- **Lots of indices have stopped dropping: flattening out**

12 Indications that the worst is over for the global metal industry

- 1. Fund money is back: Investors risk appetite is back!**
- 2. Credit is starting to flow; cost of financing declining**
- 3. Government stimulus packages starting to kick in.**
 - China's \$586 billion program is the largest and bearing fruit**
 - Most packages biased towards infrastructure development**
- 4. China stockpiling metals for next boom**
- 5. Mines starting to reopen**
- 6. Car sales are up, especially in China (+34% YOY, 14% YTD)**

12 Indications that the worst is over for the global metal industry

- 7. Steel mills and copper cable makers gearing back up.**
- 8. Chinese bank lending for property development up 28% YOY**
- 9. Manufacturing purchasing managers' indices bottomed out and is in recovery.**
- 10. Inventories have been depleted.**
- 11. EU 27s manufacturing sector reports an increase in new orders in March – first month-on-month increase since September 2008**
- 12. Base metal prices are up!**

What the Big Boys\Girls Think

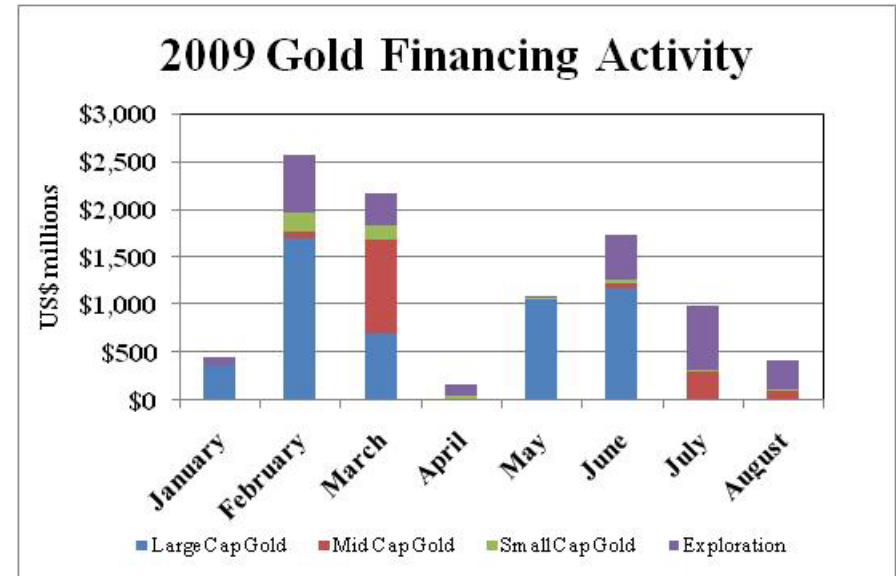
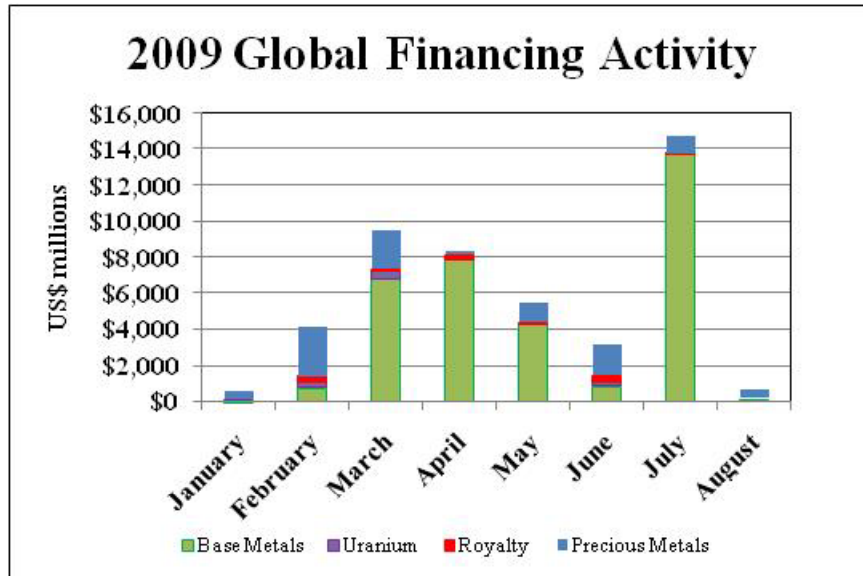
“CEO Marius Kloppers highlighted continued weakness in economic indicators and suggested that “any assumption of a quick return to historical growth may be premature”. He said that “underlying demand will continue to be obscured by movements in inventories until next year” and that price increases in many commodities, particularly iron ore, had probably run their course as more production is brought on line. BHP Billiton estimated that 70% of Chinese iron ore production capacity had been shut down by lower prices.”

– Marius Kloppers, CEO BHP Billiton

“Having said that, however, there are definite signs that things have been improving on the economic front in recent weeks. There has been some easing in the credit markets, with our own bond offerings having been many times over-subscribed. In terms of the industry, prices for most commodities appear to be stabilizing.”

- Cynthia Carol, CEO Anglo American

2009 Financing



More than \$46.5 billion raised in 2009 by 100 companies

60% of the Gold Producers have raised funds in 2009; 18% of the Exploration/Resource companies

Additional funds were raised through asset sales.

2009 Metal Prices

<u>Metal Price</u>	<u>Units</u>	<u>Jan. 1</u>	<u>Aug 24</u>	<u>Change</u>
Gold	US\$/Oz	\$870	\$941	+ 8.2%
Silver	US\$/Oz	\$11	\$14	+ 27.3%
Platinum	US\$/Oz	\$934	\$1,239	+ 32.7%
Palladium	US\$/Oz	\$185	\$275	+ 48.6%
Copper	US\$/Lb	\$1.50	\$2.94	+ 96.0%
Lead	US\$/Lb	\$0.68	\$0.99	+ 45.6%
Zinc	US\$/Lb	\$0.59	\$0.85	+ 44.1%
Nickel	US\$/Lb	\$4.67	\$9.48	+103.0%
Molybdenum	US\$/Lb	\$9.25	\$17.25	+ 86.5%

China?

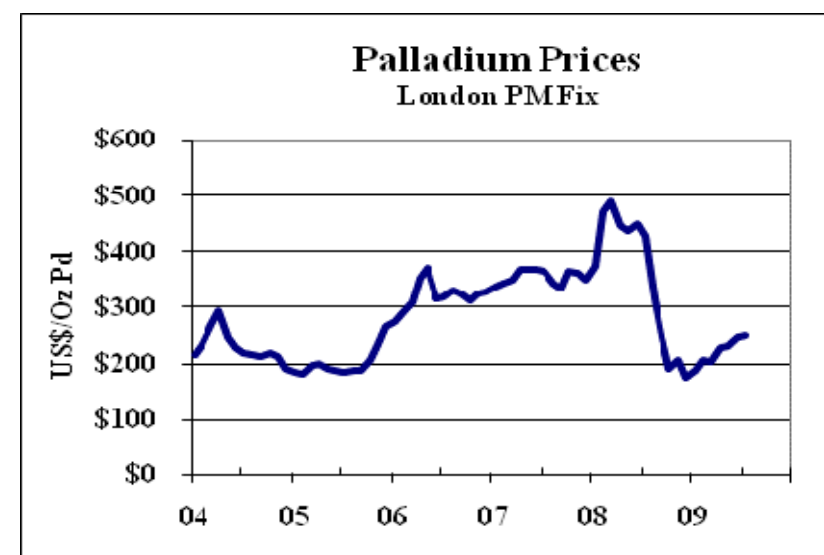
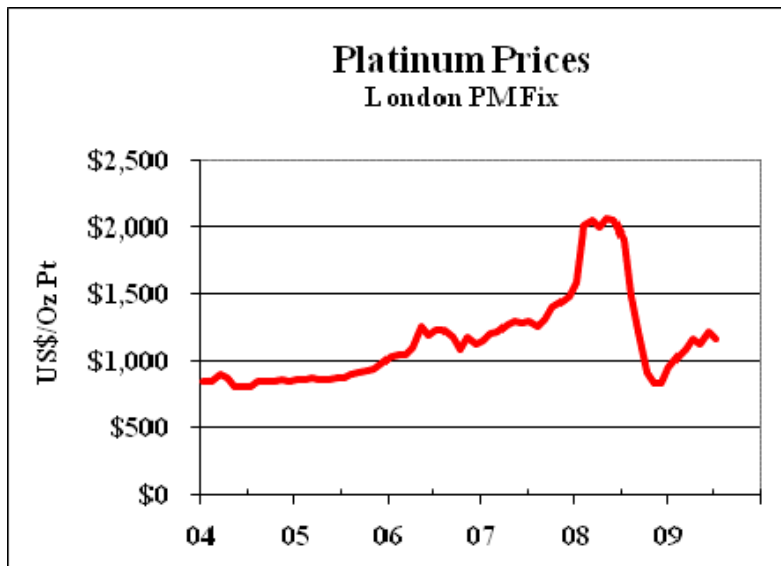
- **7.9% growth in 2Q '09 vs 6.1% in 1Q**
- **Stock market up 64% for this year (recent decline of 14%)**
- **Real estate prices skyrocketing again.**
- **Chinese bank lending for property development up 28% YOY**
- **Rmb 4.0 T (US\$ 585 billion) stimulus package working**
- **Rmb 2.0 B in railroad expansions (20,000 km)**
- **Rmb 0.7 B in highway projects (12,000 km)**
- **Further 180,000 km expansions planned for roads**

- **Follow met coal => iron => nickel => copper, molybdenum prices to track recovery**

Did Rio Tinto Spy?

- **Rio Tinto lead negotiating team on iron prices?**
- **Gathering market intelligence vs espionage**
- **Did consultants bribe?**
- **Did the Chinese government not realize that one of the Chinese arrested was an Australian citizen?**
- **Retaliation for tough iron ore negotiations?**
- **Retaliation for Chinalco-Rio Tinto breakup / rejection?**
- **Did Rio Tinto bribe? Buy classified information?**

Precious Metals Prices



The Future of Gold

Two schools of thought – Both inflation related

School One – Gold price is fine where it is.

- If there was ever a time for gold prices to skyrocket, it is now. But it didn't happen.**
- Are there market mechanisms embedded in the system to mitigate the price?**
 - Fed uses gold price to measure inflationary perceptions**
- Gold mines need a 15% return to be healthy**
 - GFMS projects US\$585/Oz World Total Production Costs**
 - This suggests a US\$673/Oz price is sufficient**
 - Gold prices in the US\$900/Oz range**
 - Plenty of freeboard profit at today's gold price**
- GATA conspiracy theories**
- School One assumes tempered inflation.**
 - The cash infusion nearly offsets the asset value evaporation**
 - Will the US consumer's behavior be modified downward by the Credit Crisis?**

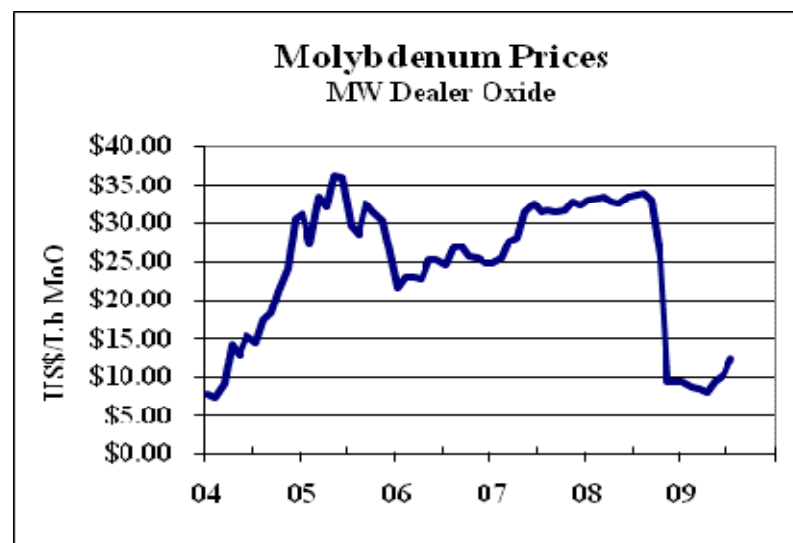
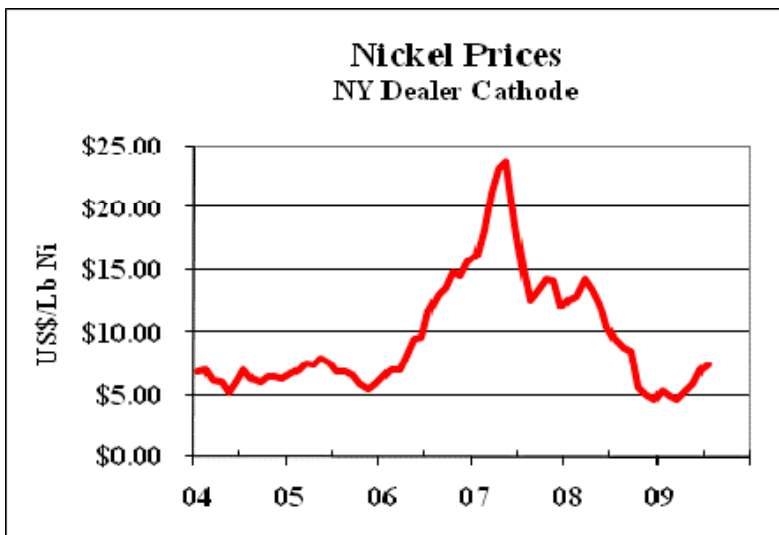
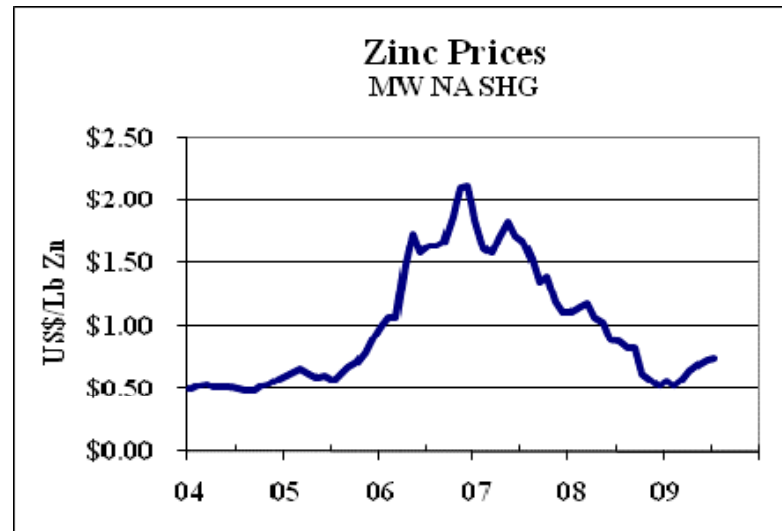
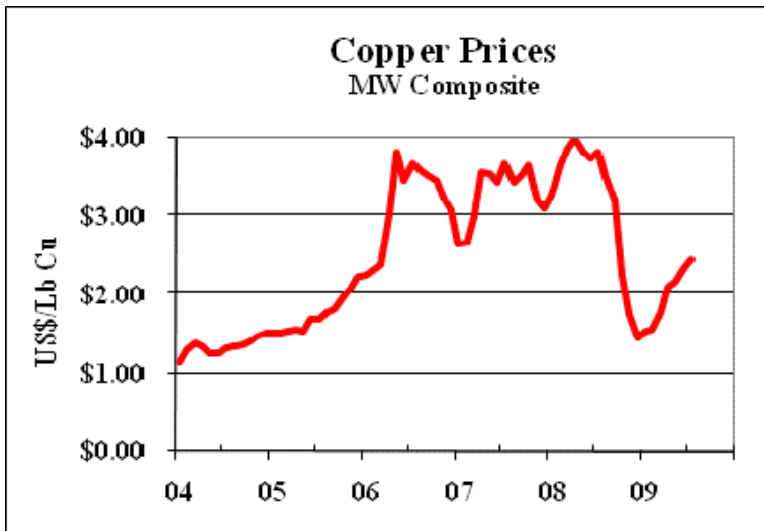
The Future of Gold

School Two – Hold onto your seats. Gold is getting ready to fly

- **Massive unchecked government spending and the massive debt necessary to finance it will cause the purchasing power of the US dollar to melt.**
 - **US dollar getting ready to collapse**
 - **Rampant inflation is a given**
 - **Gold prices will skyrocket when US dollar weakens**
 - **Will the government know when to stop issuing dollars?**
- **US dollar losing credibility as a reserve currency**
 - **There is no other viable currency to use as the reserve currency.**
 - **Will a currency basket replace it? Ask Putin! Or the Chinese?**
 - **Gold has no nationality; safe substitute.**

Will the Chinese unload US dollars to buy hard assets? (Yep!)

Base Metals Prices



Analysts' Projections

	2009	2010	2012	2013
Gold	\$935	\$965	\$935	\$895
Silver	\$13.50	\$14.65	\$14.15	\$13.60
Platinum	\$1,145	\$1,245	\$1,330	\$1,375
Palladium	\$235	\$275	\$315	\$360
Copper	\$1.85	\$2.25	\$2.45	\$2.30
Lead	\$0.58	\$0.67	\$0.70	\$0.68
Zinc	\$0.63	\$0.76	\$0.82	\$0.86
Nickel	\$5.30	\$6.20	\$6.65	\$6.85
Molybdenum	\$10.65	\$13.80	\$15.35	\$14.85

Takeaway Themes

- **Economic recovery is underway but timing and trajectory uncertain.**
- **China is still by far the principal driver for metal demand / metal prices**
- **Commodity prices have rebounded nicely in 2009**
 - **Up about 50% on average for the first 9 months**
 - **China is restocking; rest of the world not yet begun restocking efforts**
 - **Watch out for speculators**
- **Investors have returned**
 - **More money raised in 2009 than in 2008 (\$ going into hard assets)**
 - **Trickle down financing effect underway. Exploration is next.**
- **Credit Crisis was a correction. Economic recovery will return us to the Super Cycle!**