February 20, 2005

March 2005 Market Update

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Hi gang,

There were several questions concerning the Wheaton tendering process. I decided to come out with a shortened update as there were more things to talk about.

General Market Commentary:
Broader markets began to tank in mid-January and have since come back up to break even. I remain bearish on the market as it is over priced and the news going forward has been yielding soft economic numbers.

Last April I brought to the group's attention of pending inflation. It appears those comments were prophetic as now the talk of Wall Street is concern over inflation. Back in 1980-82 the Commodity Research Bureau (CRB) index hit a high of around 330. The CRB is a basket of some 17 commodities, all equal weighted so that no single commodity could set a trend by itself. Inflation at the time was ragging in the 12% area and my favorite commodity, gold, was making lifetime highs. The following is a recent chart of the CRB.

Notice we are a mere 10% away from an all time high. The index has been pushed up by oil, copper, gold, silver, natural gas and heating oil. Grain prices have kept the index in check for nearly a year. Now Brazil is going through a drought, soybeans are beginning to take off. Increasing prices of soybeans influences other grain markets. This will add upward pressure to the CRB index.

Increasing oil prices cause heating oil and natural gas to go up. Like soybeans, oil moves up and causes two other index members to also increase in price. Thus far, oil has not been able to go above $50/barrel but it soon will. The next

chart is of oil futures. Head and Shoulders patterns are fairly reliable indicators of where prices will go. The oil futures chart has a well defined Reverse Head and Shoulder pattern. Presently it looks like oil will go to $60/barrel in coming months.

I have been touting the tightness in the supply of copper for over a year now. The consumers of copper have manipulated the price since last September. Every time copper challenged $1.50, a China slow down story would hit the presses. I have shown on the chart below how many times the China story worked. The first time they did it copper dropped 25 cents, #2 was good for 20 cents, #3 was good for 14 cents and #4 hit copper for just 7 cents. Storage of copper has been dwindling all this time and now the China story doesn't seem to have any effect. I am looking for $1.80 copper sometime this summer.

My last chart to bring to your attention is for Gold. I pointed out last time the government was going after the price of gold with a vengeance. Shortly after my last Market Update, they hit gold real hard. Like copper, I have outlined the number of times gold was hit. Price hit #1 smashed gold down over $12. Attack #2, the gold cartel took advantage of thinly traded holiday markets and scalped the price for $8. The third price attack started again when most markets were on holiday except the US markets. Another $8 was shaved off with attack #3 ending in a rout of $20 by week's end. The last attack, #4, was a concerted effort to drop the price of gold down before the G7 meeting so everyone would think all is well in the world. Foreign and domestic leaders have been trying to talk up the price of the dollar and talk down gold. They tried hitting gold by suggesting selling all of the IMF's (International Monetary Fund) gold to pay off third world debt. They float this idea about once per year to give gold a hair cut. The problem with the idea of selling IMF gold is there a numerous third world countries relying on mining gold for income. You dump gold to pay off their debt and cause the mining workers to lose their jobs: Great Idea! Notice over the last six months of the chart how many times gold has lost over $6 in a day (answer: 7 times). Now count how many times it has closed over $6 in a day (answer: zero). Gold may have only closed up over $10 in a day, twice in the last 9 years. Welcome to manipulated markets.

Gold has broken out of a falling wedge, which is very bullish. It is possible, since the market is beginning to ignore all of the hot air out of politicians, that gold will challenge its high of $456 in coming months. Gold stocks are beginning to get some life and are on the verge of a breakout. I am quite bullish today. Once gold does hit the $455, be prepared to take profits out of your gold stocks. I'd suggest selling 1/3rd to ½ of your position. The government will take out all of its resources to make sure gold does not take out the high of early December. I may change my mind if gold closes one day up over $10 and/or something bad occurs in the world.

It certainly looks to me like Sir John Templeton's statement the US is entering a period of stagflation is coming true. Stagflation is last occurred in the 1970's. Stagflation is where the Fed has to raise interest rates because of inflation, not growth. As the Fed increases rates, our economy slows down. A slowing economy causes the US dollar to drop raising our costs for commodities and imports. This causes inflation to increase whereby the Fed has to raise interest rates. You get the picture. Only commodities do well in this type of environment. As you have observed from all of the above charts, commodities are poised for much further gains. There are too many consumers and not enough resources to go around. The result is higher prices and consequently inflation (whether the government acknowledges it or not).

Investment Thoughts and Overview of Recommended Stocks:
I believe commodity based stocks are the safest way to go forward. Many are still undervalued, particularly since Copper, Nickel and Molybdenum are trading at multi-year highs. Only the most profitable gold stocks I'm recommending with the aforementioned caution in force.

Overview of Recommended Stocks:

Golden Star Resources (GSS): I recommend selling this stock. The company had very bright prospects per their press releases but they have missed guidance several times. I listened to a presentation given late November where they said production would be around 175,000 ounces of gold for 2004. Ten weeks later they came out with earnings showing only 150,000 was produced. They greatly lowered their forecast for 2005. Management at GSS has no credibility and they have way over promised and grossly under delivered.

Northgate Exploration (NXG): I had NXG as a buy in the last update. Northgate will post record earning in a few weeks. My recommendation is to sell this stock. Huh? NXG recently came out with a press release stating 2005 gold and copper production will be less than 2004. NXG will just follow the gold mining sector and not outperform it based on the guidance. If the sector rises, so will NXG. I just think there are better places to put your money at this time.

Taseko Mines (TGB): Taseko was my only new stock recommendation last time and I still have it as a buy today. Its stock price has come down from where I recommended it due mainly to their issuing of stock to raise capital. Their earnings report last week showed they are near producing copper at full capacity. The molybdenum production should be going at full steam by the end of March. Taseko showed a large loss for the quarter but it was due to start up costs and equipment write downs. Their plan is to ship three loads of copper in the first quarter. With copper at 16 year highs and looking to go higher, TGB's stock should go up considerably from where it is today.

Wheaton River Minerals (WHT): Wheaton River is now for all intents and purposes Gold Corp (GG). Gold Corp share holders voted to issue shares to acquire all of Wheaton's stock. Over 66 2/3 % of Wheaton's shares were tendered to Gold Corp and thus making the take over near final.

Most of you use Ameritrade. Ameritrade charges a $20 fee for tendering to Gold Corp. Call Ameritrade up and tell them you want to tender your shares to Gold Corp. They will just verify your intentions and take the $20 out of your account. Once GG receives your shares, they will issue to you 1 share for every 4 you own (i.e. 1000 shares WHT = 250 Shares GG). You can also not do anything and your shares will be automatically tendered to GG in mid-April. Ameritrade will still charge you $20. The problem with waiting is the Wheaton shares available for public trading will dry up and make it more difficult to sell.

Wheaton/Gold Corp is a **MUST HAVE** in your portfolio. The combined company, New GG, will produce over 1.2 million ounces of gold and 140 million pounds of copper in 2005. The CEO, Ian Telfer (Wheaton's CEO) will be the head of New GG. Telfer is a financial genius as far as I can tell. He took a $30 million company and turned it into the envy of the gold sector worth close to $3 Billion in less than three years. He has an eye for value and said he looks to acquire a 500,000 ounce gold producer "very soon". This will make New GG close to a 2 million ounce producer this year. I personally believe he will buy out Cambior (CBJ) as they produce 620,000 ounces per year and will only cost $700 million to buy. Gold Corp pays dividends monthly so you will have a steady stream of cash. Monthly dividends help dissuade short sellers from trying to cap the stock. They have to pay the dividend if they sold the stock short during the dividend distribution, costing them money. New GG should have $0.60-$0.80/share earnings this year. Most of their peers fetch a price to earnings (P/E) ratio between 35 and 50. This means New GG should be trading between $21 - $40/share next year. A handsome gain considering it closed Friday at $13.38.

Indevous Pharmaceuticals (IDEV): IDEV's stock continues to flounder. I had recommended last summer to sell the stock if it went below $6. Now it trades at $3.98. I was wondering why the stock was doing so poorly since it had a block buster drug with a best in class label. It turns out several new urinary drugs came out at the same time as Sanctura. This is delaying market penetration of the drug and sales are not meeting forecasts. One day this stock will explode, but for now either hold for long term or sell and put it somewhere else.

New Stock Recommendations:
I don't have any real strong new recommendations at this time. Please let me know of any you like. Very short term, TOPT and FRO, two oil tanker stocks should do very well. The problem is March-August are seasonal down times.

Final Thoughts:
I believe commodities and inflation will be the talk of the financial press this year. I have positioned my portfolio to take advantage of this bull market. Make sure you let your winners run and sell your losers quickly.

-Toby