

FUNDAMENTAL VIEW ON METAL MARKETS - Part IV



ARE SPECIALTY METALS NEXT IN SUPER CYCLE?

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In the past few months we have seen how the rising precious and base metal prices have positively affected the future of several well known mining companies. Some of these companies were scrambling to save themselves as profits disappeared and unsustainable debt dragged them down. It appeared as if they would be seeking bankruptcy protection. What a difference a few weeks makes, some of these companies are now returning 2 to 9 times their money for those contrarians that bet on a sustained rise in metal prices. **"We are now in the tenth month of the second leg of the super bull market in metals which should be sustained for at least three more years before a major correction."**

As the Western world fights to avert a major recession, China almost single handed increased the demand for metals. We have yet to feel the effects of infrastructure build-out in the U.S and Western Europe. When and if the build-out and replacement of infrastructure begins, the appetite for metals will rapidly accelerate. Stockpiles of commodities on the LME are increasing with copper being the only commodity to shrink rapidly. The copper price has doubled since November, 2008 to \$2.70/lb and LME warehouse stockpiles have halved since March, 2009. Zinc, lead and nickel are near double from their prior lows even though LME stockpiles have moved up since March, 2009. It would appear that large speculators are once again influencing the metal price direction.

Aluminum stockpiles continue to increase dramatically as shown by the following chart:

Metal	Stockpile T's 1-Mar-2004	Stockpile T's 26-Mar-2009	Stockpile T's 1-Aug-2009	\$/lb. 1-Nov-2008	\$/lb. 1-Aug-2009	Peak Prices
Copper	275k	505k	275K	\$1.30	\$2.60	\$4.00
Aluminum	1,400k	3364k	4550K	\$0.75	\$0.84	\$1.45
Zinc	780k	346k	392K	\$0.50	\$0.78	\$2.10
Lead	76k	59k	109K	\$0.45	\$0.84	\$1.75
Nickel	13k	104k	106K	\$4.00	\$8.10	\$24.00

Metal commodity price strength has also brought idled production back on as well as increased the ability to restructure debt for some of the "list of companies" I have compiled to strengthen the case for supply disruption affecting demand (*View my list of North American companies which have shut down production <http://www.goldrea.com/reacompanies/list/process-disclaimer.php?chc=4>*).

Bought deal financings continue at a lesser degree than previously as most of the advanced producers and projects have been financed for billions of dollars. This is good news for those companies with smaller deposits of gold and base and specialty metal projects of merit. More juniors are able to finance even during the summer months, where it was almost impossible earlier in the year. At this time there is a much greater amount of money sitting on the sidelines than has entered the market in the past few months. Good projects will continue to be financed over the next few months as commodity prices will eventually break their previous highs and corrections, even major corrections will make much higher bottoms than the 2008 bottoms. The metal prices improvements from my March 30 letter is dramatic and is evidenced as follows:

Commodity	June/08	Nov/08	Aug 1/09	Diff %
Gold	\$950.00/oz	\$750.00/oz	\$954.00/oz	0
Copper	\$3.80/lb	\$1.36/lb	\$2.60/lb	-0.32%
Aluminum	\$1.40/lb	\$0.65/lb	\$0.84/lb	-0.40%
Nickel	\$11.00/lb	\$3.95/lb	\$8.10/lb	-0.20%
Zinc	\$0.87/lb	\$0.47/lb	\$0.78/lb	-0.10%
Lead	\$0.85/lb	\$0.41/lb	\$0.84/lb	0
Molybdenum	\$32.00/lb	\$8.75/lb	\$16.50/lb	-0.48%
Manganese Fl.	\$2.00/lb	\$1.05/lb	\$1.10/lb	-0.45%
Cobalt	\$51.00/lb	\$16.00/lb	\$17.00/lb	-0.67%
Magnesium	\$2.70/lb	\$1.51/lb	\$1.20/lb	-54%
Oil	\$145.00/brl	\$41.00/brl	\$69.50/brl	-53%

Even though China does not recognize the benchmark of a 33% reduction in iron ore prices, it is pretty much a foregone conclusion that they will not get the reductions they desire.

This will swing the focus on specialty and critical metals which follows the fortunes of the steel industry. In my March 30 letter I mentioned that molybdenum followed closely on the heels of copper prices. Since March 30 the price of molybdenum has doubled from \$8.00/lb to over \$16.00/lb. As molybdenum leads the way other specialty metals will strengthen in price. It is my belief that as "Moly" (molybdenum) became the darling of the investment community in 2007, specialty metals will become the investment of choice in late 2009 early 2010. Over the last several decades those metals were the sole do-

main of major miners and very little was known about them until recently. In some cases during the last run up specialty and critical metals such as moly and manganese accounted for a large portion of these majors' profits. Specialty metals include molybdenum, manganese, magnesium, niobium, cobalt, chrome, tungsten, vanadium, etc.

Why these metals will become the darlings are as follows:

1. China is the major producer of these metals and has imposed export duties;
2. Other producers such as Russia and India have announced that they will impose similar duties;
3. Most countries consider these metals strategic and in the case of manganese critical, you will not have a steel industry without it, as a combination of iron and manganese is require to produce steel.
4. Western Europe has begun serious discussions on stockpiling these metals in the near future. The United States cannot be far behind.
5. There will come a time when China's appetite consumes these metals internally and the rest of the world will suffer without them. Examples of these are electrolytic manganese where China produces 95% of the world supply and magnesium where China produces 78% of the world supply.

The metals I watch are the "THREE M's": Manganese, Molybdenum and Magnesium. Production and prices are as follows:

Metal	Price Aug 06	Price Nov 08	Peak Price	Price Aug 09	Production
Manganese*	\$0.70	\$1.10	\$2.85	\$1.10	2.5 billion lbs
Magnesium	\$1.20	\$1.10	\$2.70	\$1.20	1.6 billion lbs
Molybdenum	\$26.00	\$7.50	\$39.00	\$16.50	460 million lbs

* Manganese production of electrolytic manganese only. Total production is approximately 29 billion lbs.

It was only five years ago that very little was known about molybdenum (moly) and today it is almost as well known as precious and base metals having moved from one company developing a moly project in early 2004 to several hundred companies today. The same statistics exist today in manganese/magnesium explorers and developers around the world.

Major companies dominate the exploration and production of the "Three M's" and have done so for decades with little fanfare on discovery or reports on profits although molybdenum and manganese have been huge contributors to their bottom line. Some of the attributes of these metals are as follows:

Molybdenum: A high demand specialty metal that strengthens and has high anti-corrosive abilities. Used in all aspects where strength and anti-corrosion elements are required. Large usage in nuclear power plants, oil and gas pipelines, drill steel and saline plants.

Manganese: 90% of its usage is in the manufacture of steel. For every tonne of steel 10 to 20 lbs of manganese is required this makes it a critical rather than a specialty metal. Manganese is the fourth largest produced metal at 29 billion pounds behind iron, aluminum and copper. The western world produces less than 5% of electrolytic manganese.

Magnesium: The fastest growing demand for magnesium is the automobile industry where recent studies have magnesium replacing plastics for strength, cost and weight. China produces 78% of the world's magnesium.

As the demand for iron and steel continues to rise so goes the demand for these specialty and critical metals. A handful of junior companies are active in the exploration and development of manganese and magnesium similar to molybdenum in 2004 and I predict that within two years they will be numbered in the hundreds.

The Super Cycle is a metal commodity bull market which will last for over 30 years. As India begins to play catch-up with China the impact can only push commodity metal prices higher as these two mega countries come into the twenty-first century. There will be major corrections along the way but the Super Bull will remain intact as the transfer of wealth moves from the west to the east. Gold more than ever will become the currency of choice and necessity.

In conclusion, from time to time, I'll be updating this article, and if you'd like to receive those updates, please send an email to: lwreaugh@rdminerals.ca.

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