

John Tumazos Very Independent Research, LLC  
11 Yellow Brook Road, Holmdel, NJ 07733  
732 444 1083 or 732 740 3574 (cellular)

[john@veryindependentresearch.com](mailto:john@veryindependentresearch.com) or

[johnstumazos@comcast.net](mailto:johnstumazos@comcast.net) or [tumazos@monmouth.com](mailto:tumazos@monmouth.com)

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### ***Complimentary Report Not Intended for Compensation***

GENERAL DECLINE IN METALS PRICES REFLECTS A COMBINATION OF WORRIES OF SLOWDOWN OWING TO CREDIT CRUNCH, SPECULATORS' EXIT AFTER PROFIT-TAKING AND EARLY SEASONAL DROP

- The sudden drop in uranium prices to \$110 from \$136 per pound appears to reflect a quick exit by some of the investment funds that reportedly took delivery of 20% of world mine output in 2006. No change in the nuclear plant backlog or global electricity demand trends occurred in the past month.
- The drop to \$1.15 per pound LME aluminum suggests upcoming declining sequential and year-on-year profit comparisons. Our \$1.12 2008 LME spot price estimate, \$2.40 per share 2008 Alcoa earnings estimate or \$5.62 2008 pre-merger 2008 Alcan earnings estimates could prove optimistic. We assign significance to the 2.5-3.0 cent per pound Midwest, Japanese and European producer premiums over LME and late-July 30 cent scrap discounts beneath LME as prima facie evidence of insufficient real demand to absorb record smelter supply. “Relative price demand” in sympathy to much higher copper, zinc or nickel prices provides no floor. The ever-present 1.13 mmt commodity exchange stocks remind markets no aluminum shortage has existed since the 1988 era.
- Combined commodity exchange inventories of copper now have risen three straight weeks to 224,114 from 208,618 metric tonnes. Spot prices fell to \$3.39 from \$3.75 in those same three weeks, but are comfortable in relation to our \$3.20 per pound 2007 and revised \$3.00 per pound 2008 price estimate raised from \$2.75 for 2008. The World Bureau of Metals Statistics (WBMS) reports through May world mine output up 6.0%, refined output up 2.5%, consumption up 2.5% and consumption 145,000 tonnes more than refined output through May. The WBMS data suggests that the increased mine output is “in transit in the pipeline” prior to being refined or else a portion of increased scrap supplies have subsided. Press reports concerning labor unrest grow increasingly irrelevant as concentrate stocks rebound.

- Nickel has turned into an outright rout as LME prices now have plunged more than 50% from mid-May highs to \$12.04 per pound and LME stocks rose to 18,804 tonnes. It is noteworthy that the weeks ended August 12th and July 27<sup>th</sup> saw LME stocks rise 3,666 and 2,754 tonnes, respectively, and any acceleration beyond a 1,000 tonne weekly rise raises the specter of > 50,000 tonne LME inventories by year-end as the seasonally slower second half concludes. The 160 pounds of ni contained within alloy 304 now are worth \$2,000 per ton of 304 less WITHIN A MERE 90 DAYS causing a “buyers strike” until nickel bottoms, and offers hope that a spike rebound could ensue when product buying resumes to permit normal steel mill melt schedules. Our estimates of \$16.00 for 2007, \$12.50 for 2008, \$10 for 2009-10 and \$9.00 for 2011 onwards no longer appear as safe or conservative as previously.
- Gold, silver and platinum have been pillars of stability in recent weeks near \$670, \$12.75-13.00 and \$1,250, respectively. Central bankers’ injections of liquidity, the weak US dollar and the general poor reputation of global banking practices could benefit precious metals going forward. On August 5<sup>th</sup> we upgraded Barrick Gold to Overweight from Neutral.
- Lead and zinc markets appear more stable than other base metals as LME lead inventories have fallen six straight weeks to 32,575 metric tonnes and combined LME and Shanghai zinc inventories have fallen seven straight weeks to 99,971 tonnes. The drop in lead prices to \$1.30 and zinc to \$1.51 represent drops of \$0.28 and \$0.18 per pound, respectively, in three short weeks that appear to reflect investor profit-taking more or perhaps anticipation of first deliveries from the San Cristobal mine in Bolivia.
- Wood markets have reacted to the housing downturn for three years since making peaks in May 2004, while metals traders appear to have just “caught on.” It is noteworthy that forest products prices, which lie in the vortex of the housing collapse, have rebounded from low levels seen during the typical May seasonal “peaks.” OSB rebounded from a \$137 per 000 sq ft five year low on May 7<sup>th</sup> to \$172 August 12<sup>th</sup>, framing lumber has been stable near \$290 up from a \$269 cycle low recorded October 9<sup>th</sup> and November 13<sup>th</sup> last year and plywood rebounded to \$370 on August 12<sup>th</sup> from a cycle low of \$225 at the end of September 2006 or \$265 as recently as February 5, 2007. Wood prices have risen with marginal costs due to the weak US \$, C\$ near US \$0.95, higher energy-based inputs and with anticipation of long capacity shut-ins well before winter sets in.

#### A MISPLACED “GREENSPAN PUT”

The intervention of the U.S. and EU central banks to inject liquidity into their respective monetary systems helped stock and bond markets to rally as the past week concluded. Gold and silver seemed to benefit, but not the industrial metals.

Certainly central bankers have a legitimate civic duty to encourage full employment without inflation. We feel compassion to homeowners unable to pay their mortgages or job losses in construction, remodeling, furniture, appliance, auto or other consumer-

spending related sectors. Restaurants, retail spending and related discretionary items suffer in hard times.

It is important to remember that “subprime” and “alt-1A” hybrid loan failures stem in part from outright fraud much like the savings and loan crisis 15 years ago. This author vividly remembers the 17 acre “wetlands” parcel behind a former residence that was originally a “buffer” between a residential street and the Jersey Coast commuter rail line. The 17 acres were “zoned” for residential development by the Middletown, NJ planning board on 3 am on a weeknight, pledged as collateral for over \$10 mm in loans and auctioned by the Resolution Trust Company for about \$2 mm in a “high roller” auction. I went hoping to buy the tract for \$100,000 just to maintain privacy and cross-country ski on the deer trails in winter, and was incredulous at the bids made from well-heeled folks shuttled in stretch limousines into an auditorium seating thousands.

False employment data, faulty appraisals, no-money-down, owner non-occupied, third party mortgage broker originations, prompt resale of weak loan packages to Wall Street underwriters, no apparent due diligence, a \$100 billion-plus business repackaging the weaker bonds and reputable foreign banks now finding themselves buried all appear too familiar. It is a good thing that many banks or other lenders are deciding to withdraw from sub-prime lending, terminate relations with third party mortgage brokers, confirm all data themselves, verify proof of employment and require meaningful down payments.

The behavior of state banking regulators in Florida, Arizona, California, Virginia and other “speculator friendly” jurisdictions will prove important. Literally one-fourth of the national housing decline involves Florida, and another one-fourth California, Arizona, Las Vegas, Atlantic City, Virginia or other “second home” markets. In contrast, Houston, Seattle, Salt Lake City, Manhattan and a collection of 15 largely rural states attracted less speculation and demonstrate greater stability. It appears important for Federal laws and regulations to supplement state rules, and for state banking examiners in problem jurisdictions to be taken to task.

*We believe the evolving climate will benefit gold and silver commodity prices, and that large capitalization gold stocks that underperformed both gold bullion and the stock market for several years may be a good place to “hide” in the current unstable period.* There is no reason to be confident in the U.S. dollar or banking system, and political pressures to lower U.S. interest rates will only weaken the dollar more.

It is difficult to determine the extent to which nonresidential construction falls in 2008 and 2009 following the housing slowdown. WalMart’s decision to build 100 fewer stores annually in the U.S. represents a 9% drop in retail square footage built alone. Fewer housing developments will require fewer strip malls or other new shopping areas. The tragic Minneapolis bridge collapse illustrates the vital need to maintain, repair, replace and build new infrastructure as well.

Further, land speculation property bubbles are likely to surface in diverse locations around the globe. Interest rates have been very low around the world, especially in

Japan, since the 9-11-01 tragedies in the U.S. or the Asia Crisis back to 1998. Commercial construction may be due for a pause in other places besides Florida or Arizona. Chinese export product safety suggests that the American mortgage industry has no monopoly on fraud.

We would be surprised if first-half global demand growth rates in the 8%-10% for steel or aluminum continue. Looking ahead to 2008, the U.S. nonresidential construction industry, world auto demand as fuel prices remain firm, the conclusion of Chinese Olympic construction and a possible 90 day Beijing regional manufacturing slowdown to reduce air pollution look as risks to metals demand. *Zero to 5% global industrial metals growth rates appear to be the outlook for next year.*

#### ALUMINUM PRICES WELL LOWER WHILE COSTS MORE

Quarterly average LME prices appear poised for a fall sequentially from \$1.27 in March 2007, \$1.25 in June 2007 and now nearer to the recent \$1.15 level for the second-half. First-half 2008 fabricated aluminum prices important to Alcoa's earnings reports probably will be at least \$0.10 per pound less than first-half 2007 levels. The U.S. Aluminum Association reports a roughly 7% drop in ytd consumption and 11% drop in mill product orders. There will not be any relief from cost increases from the weaker US \$, stronger C\$ or A\$ or euro or higher energy or other inputs.

On a worldwide basis outside of the U.S. nothing is wrong with aluminum demand. The market problems involve a more than 3 mmt increase in Chinese smelter output this year, the construction of ultra low cost smelters in eight Mideastern nations, Rusal's program to double output and new smelters in Iceland and a sprinkling of other venues around the world. Demand is good, but output is more plentiful.

#### COPPER INVENTORIES NORMALLY RISE SEASONALLY FROM AUGUST TO DECEMBER AS MINE OUTPUT GAIN OVER TWICE THE CONSUMPTION GAIN

Press reports and market commentary about mine output and copper supply suggest a greater level of mine output disruptions than do the WBMS statistics report of a 6% mine output gain through May 2007. We tend to dismiss most strike reports as they tend to settle quickly "much as a Latin lover would change moods."

We can identify three specific output disruptions that prevented 80,000 tonnes of refined output - - the December 10 Chuquicamata pit wall remediation over 25 days that prevented 45,000 tonnes from being mined, the planned Collahuasi March grinding mill repair that prevented 35,000 tonnes from being milled and the Newmont Mining first-half 2007 emphasis upon stripping for which milling of stockpiled ores permitted reasonable copper concentrate shipments without mining much new ore.

Rio Tinto had almost 10% lower ore grades at Kennecott in Utah, BHP Billiton produced less than expected at Olympic Dam in Western Australia, and Newcrest's Telfer in Western Australia each produced less than expected. Freeport-McMoRan Copper and

Gold's Grasberg enjoyed its highest scheduled ore grades output in the March 2007 quarter.

There are more mines that have produced smoothly. World mine output up 364,900 tonnes or 6% stems mostly from the Americas and Asia, and it is noteworthy that the mine output gain of 6% was much more than the global demand gain reported at 2.5%. While refined output only grew 2.6%, it is possible that refined output will improve with a three to six month time lag as more concentrates become available or reach smelters and refineries or give the smelter/refinery industry confidence to improve throughput. Through May mine output in Oceania is down 1,400 tonnes, Europe down 22,900 tonnes and Africa is up 9,600 tonnes due to a 31,000 tonne South African gain offsetting drops in Congo, Zambia, etc.

The 207,000 tonne Asian gain may not be sustained as Grasberg's ore grades moderate. Through May it stems 165,300 tonnes from Indonesia, 24,200 tonnes from China and a net 17,500 tonnes from all other nations.

The 172,500 tonne output gain in the Americas is more broadly based. Chilean output rose 107,600 tonnes, Mexico 30,500, Peru 32,100 and Brazil 28,400 tonnes.

#### STEEL MARKET REGISTERS SOME SHORT-TERM SIGNS OF HEALTH

The August more than \$10 uptick in scrap steel prices, the drop to 13.9 million tons of distributor inventories just 1.0 million tons above late-2005 lows and prognosis of steel imports to trend no better than 3.0 million tons each month or possibly drop towards 2.5 million tons each are positives.

However, the trend of auto and construction activity in the U.S. gives no indication of a short-term upturn. Minimills have cut rebar and other bar product prices nearly \$40 per ton as summer subsides and winter approaches. SeverCorr offers new molten output in the fourth-quarter, and by 2010 expansions loom from ThyssenKrupp, Minnesota Steel, possibly Magnitogorsk in Ohio and incremental expansions at Severstal Rouge in Michigan or California Steel.

Domestic steel markets will rebound sharply if buyers see a "spark" to ignite restocking. Current inventories will not be enough if a major producer suffers a production failure, import prices suddenly rise or scrap steel input costs rise once again in mid-winter.

The International Iron and Steel Institute reports an 8.4% global and 17.8% Chinese gain in steel output through June 2007. China accounted for 35.8 of the 50.4 mmt increase in world output.

The global steel output increase outside of China was very widely dispersed, and gives some comfort or confidence of broadbased global demand. Output grew 1.3 mmt in India, 2.4 mmt in Japan, 1.9 mmt in South Korea, 0.7 mmt in the Mideast, 1.4 mmt in Turkey, 2.8 mmt in the EU 27 nations, 1.5 mmt in Ukraine, 1.6 mmt in Russia and 1.9

mmt in Brazil through June 2007. The collective 14.6 million tonne gain outside China represented a sustainable, non-frothy 3.6% gain outside of China.

If China were to moderate to a 5%-10% steel output slowdown in 2008 as Olympic facilities no longer contribute and it possibly places restrictions on coal-burning emissions in the 90 days prior to the Olympics and if the remainder of the world continues to grow at a 3%-4% rate, a 5% target for a 2008 gain in world steel output appears reasonable. We have the greatest optimism about steel output abroad owing to the large backlog of major infrastructure projects in the Mideast, Russia, Eastern Europe or energy producing regions around the world. Steel has a good chance of outperforming nonferrous metals next year in terms of demand growth.

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Numerous prior investment banking relationships existed prior to three years history to the pre-1997 time frame under the employment of Donaldson, Lufkin and Jenrette or Oppenheimer & Co., Inc. Some of these we can recollect included 14 different gold mine valuations or sales for Barrick Gold, LAC Minerals (later acquired by Barrick), Addington Resources (gold assets in Montana acquired by Canyon Resources), Westworld Industries (Bolivian assets acquired by Battle Mountain Gold later acquired by Newmont Mining), Coeur d’Alene Mines, Crown Resources (acquired by Kinross Gold), Freeport-McMoRan Gold (acquired by Minorco later AngloGold later Queenstake Resources), FMC Gold (later renamed Meridian Gold) and others. Sole managed initial public offerings included Reliance Steel & Aluminum and Huntco. Lead-managed initial public offerings included American Steel & Wire (later acquired by Birmingham Steel) and lead-managed underwritings included Quanex. Co-managed underwritings included the IPO of Century Aluminum and offerings for AK Steel, Kaiser Aluminum, Agnico-Eagle Mines, Cameco and others. Asset sales or purchase advisories, fairness opinion or trusteeships were done for Thypin Steel (sold to Ryerson Tull), Cyclops Corp. (sold to Armco later sold to AK Steel), Allegheny Corp., Bethlehem Steel, the U.S. Dept. of Justice pursuant to the June 1984 merger of LTV and Republic Steel to sell the Gadsden, AL integrated flat-rolled mill, Cobre Copper, and others. Typically more than five investment banking assignments were evaluated, partly executed or “due diligenced” for any completed transaction. Some examples we can recall for which a prospectus was either drafted or partly drafted indicating much work included stock underwritings not completed for Wheeling-Pittsburgh Steel, Steel Dynamics, Atlas Corp., Webco, Sharon Steel, IPSCO, Co-Steel Inc., and others.

#### **ANALYST UNIVERSE COVERAGE:**

John C. Tumazos, CFA: Rio Tinto, Louisiana-Pacific, Nucor Corp., Newmont Mining, U.S. Steel, International Paper, BHP Billiton, MeadWestvaco Corp., Antofagasta PLC, Allegheny

Technologies, Alcoa Inc., Inco Limited, Bowater, Inc., Temple-Inland, Barrick Gold, Abitibi-Consolidated, Weyerhaeuser Co., Alcan Inc., Smurfit-Stone Container, Plum Creek Timber, Worthington Industries, Goldcorp Inc., AngloGold Ashanti, Freeport McMoRan Copper & Gold, Novelis Inc., FNX Mining.

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There is no intention to “balance” the number of Overweight or Underweight ratings, as instances of broad over- or under-performance among basic industrials may occur. JTVIR makes each investment judgment in a “bottoms up” manner based on the assets of each individual company.

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Additional risk factors as they pertain to the analyst's specific investment thesis can be found within the report.

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