MAEDEL'S
EQUITY MARKET ANALYST

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Special Situations

Tough market or not, Lynas Corp., Ivanhoe Mines and Independence Group have every reason to move higher.

One of the positive things about declining markets is that the really good stocks are easy to spot. Take **Lynas Corporation**, I have mentioned it often and followed it for years. It has been in the Maedel's portfolio (added at $0.51) since late 2009. I like its rare earth oxide projects (REO) advanced stage of development, projected high margins and what looked like an imminent tightening of the rare earth oxide (REO) market.

But care must be taken as the longer term outlook for REO prices and the thus the outlook for the many small REO explorers is not as bullish as many believe. **Molycorp LLC's,** imminent $450 million IPO in the US, is to fund its planned modernization and production expansion. It has one of the world's largest REO reserves at its Mountain Pass deposit in Southern California where at its peak production in the mid 1980s, it used to produce a third of global supplies.

The Mountain Pass reserves exceed 30,000,000 tons of ore (cut-off grade of 7.6%) or roughly 150 years worth of current US demand for lanthanum and samarium. At least for these two rare earths, a substantial supply already exists, which could put a cap on any their respective price rises.

Molycorp's $450 million raise is for upgrading and ramping up production and hopefully turning around the currently loss making operation.. Unlike Lynas its current development may have more to do with establishing a secure US supply of strategic metals such as neodymium, the main component of rare earth magnets which are used for example in electric cars, missile guidance systems and, electric generators used in wind power systems.

Molycorp was almost owned by a Chinese company when, in 2005, **National Offshore Oil Corporation** offered $US 18.5 billion for Molycorp's former owner Unocal. The deal was blocked by the US Government and Chevron ended up the buyer. The money losing mine was mothballed in 2002 after years of losses related to its relatively low grades, tailings disposal issues and permit delays meant it was unable to compete with cheaper chinese imports.

In 2007 a private group bought it and it resumed very limited loss-making production. In Q1 2010 it lost $2.92 million on $7.75 million revenues. The IPO is priced to perfection as the cost of ramping up and making profitable the money loser is $511 million, $61 million short of the money being raised. Any problems with the development - which is often the case, will mean raising more money.

Lynas may not have the biggest deposit but it does have the richest known deposit of rare earths (1.2 million tons measured at 15.6%) in the world at its Mount Weld mine which is near Laverton, Western Australia. Currently almost 97% of rare earths are produced in China and prices are rising as "available" supplies continue to tighten at least in the short term. The company is on track to be selling REOs next year making it the next rare earth oxide producer to begin production outside of China.

Similar to Molycorp a Chinese company tried to buy Lynas too. Last year Lynas just about became a subsidiary of **China Nonferrous Metal Mining Group (CNMC)** in an AUD 505 million deal that would have financed the construction of its Mt. Weld concentrator and advanced materials plant in Kuantan, Malaysia. The deal was terminated when Australia's Foreign Investment Review Board demanded CNMC reduce its ownership to below 50 per cent and take a clear minority of board seats in Lynas.

To develop the project, Lynas then rushed to complete a AUD 450 million financing (announced September 29th and completed November 11th). Production of rare earth oxides at a rate of 11,000 tons annually is expected to begin in Q3 of next year and to double to 22,000 tons annually by 2013. In a recent bulletin I commented how its share price had barely reacted to the ongoing correction - a very bullish sign. Since then its shares have rallied more than 50% as brokerage giant **J.P. Morgan** initiated coverage

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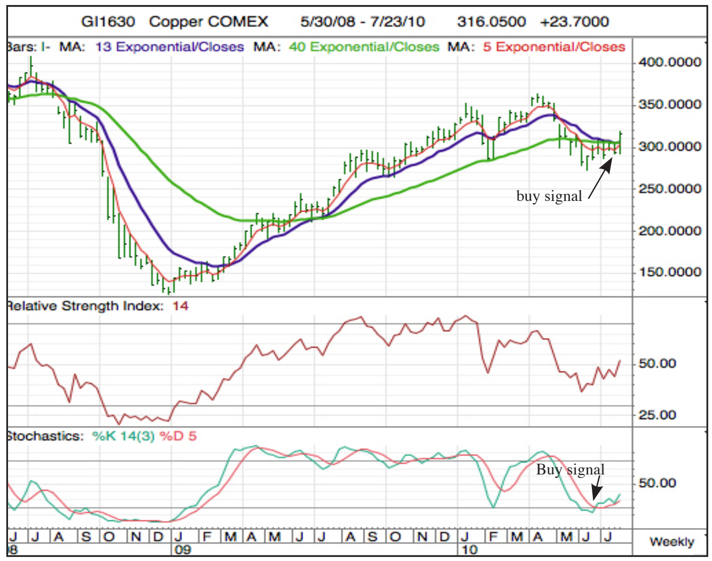
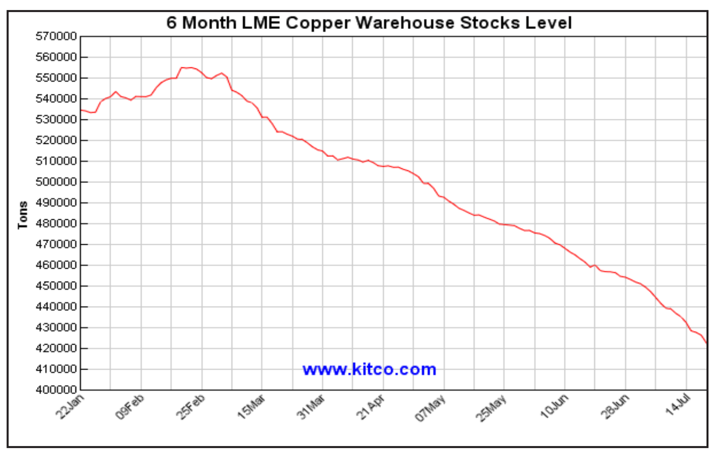
giving the company's shares a $0.91 price target - nearly double its then $0.50 price.

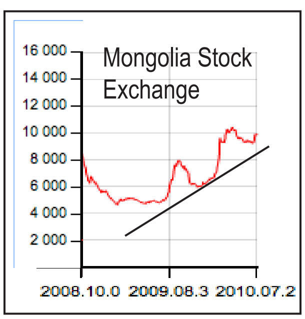
Adding to its bullish outlook, already tight REO supplies then became tighter when on July 9th, China's Ministry of Commerce reduced the second half REO export quota by 72% making the total export quota for 2010 40% less than the total export quota for 2009. At the same time the government is moving to consolidate the industry by eliminating small producers which are notorious for smuggling rare earths out of the country. As much as a third of the REOs available to western companies outside of China are obtained illicitly . Factoring domestic use and exports the total surplus of Chinese REO production is estimated at up to 30,000 tons, an amount expected to shrink as the use of technologically advanced products such a high-tech magnets and ultra efficient lighting grows. But for the near term the reduction in quotas combined with a crackdown on smuggling is bound to lead to shortages and higher prices putting Lynas as the Wests first real producer in a highly advantageous position. We are maintaining our holdings. For American's wishing to invest in Lynas its ADR has just been listed on the OTC Market in the U.S. under the symbol LYSDY.





Ivanhoe Mines

Copper supply is expected to move into a deficit next year a prospect made increasingly apparent by the ongoing LME copper stock reductions and the recent developing technical breakout in the metal's price. In the first 6 months of 2009 copper demand by the OECD was the lowest since 1983 giving little downside in terms of further reductions in copper consumption.



A relevant question today is whether "peak copper" is a reality? That is are sources of cheap to mine, easy to access copper that is in politically safe areas increasingly a thing of the past? With the exception of Mongolia, new major sources are coming from among the world's most dodgy areas. The Democratic Republic of Congo and Zambia are all to typical examples of large but unreliable new supplies.

I have written about First Quantum's problems with its copper and cobalt projects in the Democratic Republic of the Congo. In the mid 1990s, during the civil war, I travelled there numerous times to access its developing potential. On one trip to visit the **Kolwezi** cobalt tailings project our pilots mistakenly landed the airplane in an unsecured zone. The next two days were spent negotiating our release with the area's Mobutu supporters. After losing our plane our Rapport escorts managed to secure a jeep to transport us through the jungle to meet with the local war lord. In one tense moment we ran into a ragtag group of congolese soldiers. They just emerged from the dense jungle as we inched along. We stopped and then a new negotiation began. The first words from the groups leader were not all that encouraging as he told us with a dozen or so guns pointed in our faces "That is my jeep".

So while I can speak from personal experience about some of the world's riskier mining environments and thus attest to the growing precariousness of supply, I also see from my base in Asia how those booming economies are likely to continue needing as much copper as is likely to be produced for years too come.

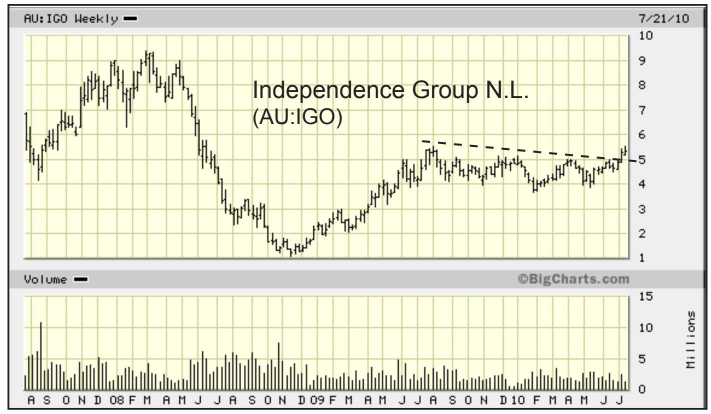
Already China consumes 40% of world copper production and India may be a few years behind in the consumption curve but its growth will also ensure firm copper prices for years to come. I think its reasonable to expect Chinese demand to remain strong in the near term as the government is now wisely discouraging what it views as an unhealthy predominance of high-end home building and speculation, while it instead encourages a massive expansion of entry level housing construction. The government expects to increase its urban population from its current 49% to 60% in less than a decade. That means it plans to build homes for roughly 150 million people over the next nine years . New houses need copper and this is a reality that will support copper consumption.

This fact must be on the minds of **Rio Tinto** executives as they spent US $260 million to increase the company's shareholding in **Ivanhoe Mines**,and then spent another $462 million to exercise warrants in Ivanhoe further increasing its holdings to 29.6 per cent. Ivanhoe has a 66% interest in the Oyu Tolgoi which contains approximately 81 billion pounds of copper and 46 million ounces of gold in measured, indicated and inferred resources. The mine is projected to produce 1.2 billion pounds of copper and 650,000 ounces of gold annually in its first 10 years. Let me be clear Mongolia is nothing like the Congo. In fact it is one of my favourite investment areas and I really enjoy visiting the country and its people. It has one of the world's highest levels of literacy and an economy and stock exchange that is booming because of its business friendly environment.

The Oyu Tolgoi is expected to start producing in 2013, and ramp up to peak production of 450,000 tonnes a year of copper and 33,000 ounces of gold in about 5 years. Rio Tinto has made no effort to dispell rumors it might take over Ivanhoe Mines. The next step would be for it to exercise options and convert debt - thus increasing its interest to 46.6% as previously agreed. Perhaps seeing the writing on the wall that Rio Tinto will eventually want to have control of Ivanhoe, the company adopted a shareholder rights plan, or "poison pill," that allows it to issue more stock should Rio Tinto not offer to buy out all of the shareholders should it move to get control. This adds considerably to the story as investors no longer risk being orphaned as minority holders with RioTinto calling shots once it attains 51% of the shares. The risk, which is considered small, is that Rio Tinto wins an arbitration case regarding the poison pill. In the meantime copper is registering buy signals from its weekly stochastics and moving averages and Ivanhoe's share price looks set to test its old share price high of $18.90 and then move to new highs.

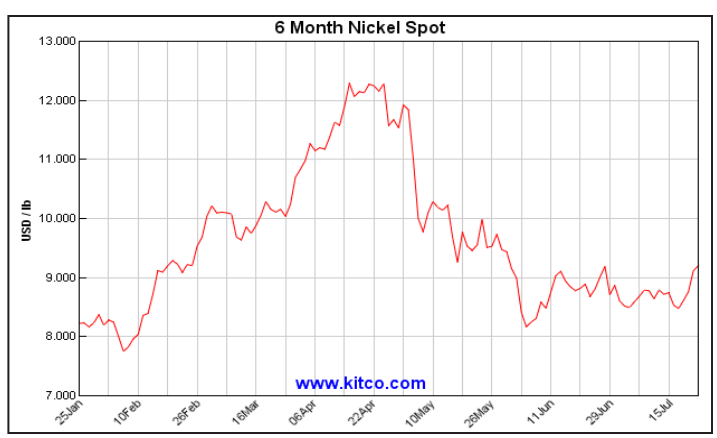
Independence Group

While Ivanhoe and Lynas have been in our portfolio for some time, **Independence Group (AU:IGO)** is our latest speculative buy (at A $4.70). The company was first listed in 2002 beginning with a A $4



million $0.20 per share raise which was quickly followed by a further $7 million raise at $0.42 which went towards the A $15 million purchase of the Long Nickel mine, a move which appeared very aggressive at the time given that the mine had only 26,800 tons of nickle reserves left (over 200,000 tons already produced) and nickel the price was averaging around US $3.38 per pound. The mine has since produced profits to date of $A $268 million. I have followed it and penned a buy recommendation as a consultant for associate CFA Conrad Weise in 2005 when at around A $1.50, its Tropicana gold discovery put it on the radar screen. Now with the resumption of *Maedel's* last year, it has been under close watch. Only in the past few weeks has it broken out of a year long consolidation as further discoveries at the Tropicana look to justify a much higher share price.

Independence Group has a superb management team, but rather than describe them individually I think a short description of IGO's evolution should suffice. Since their purchase of the Long Nickel Mine the company has nearly doubled its existing reserves from 26,800 tons (reserves) to over 50,000 tons with a resource of 93,000 tons while producing a further 61,000 tons at a cash cost (including royalty) of AU $4.44 which is in an impressive bottom third of costs for the industry. The companies current production rate is about 8,000 tons per annum. It has hedged 6,360 tons at an average of A $21,813 per ton. The company plans to increase its production to 9,000 tpa while the potential for a substantial expansion of reserves is very apparent especially from the Moran discovery where significant inter-



cepts to the South (4.7 meters @ 12.2% Ni and 12.9 meters @6.6% Ni) and North (2.6 meters @ 7.9% Ni) indicate considerable room for growth.

In the meantime the Pre-Feasibility study for the AngloGold Ashanti(70%) IGO (30%) Tropicana discovery calculates a measured, indicated and inferred 75.3 MT grading 2.07 g/t for 5.01 million oz/ Au. The proved and probable reserve using a 0.7 g/t cut off is 3.3 million oz Au. Capital costs are a $500 -540 million with gold production of 330,000 - 410,000 oz per year. A bankable feasibility study is expected to be completed by this December.

The development of this large open pit mine is will not be the end of the story as four areas of potential high grade ore shoots have been discovered on the east side of the deposit on both in its north and south which may be exploitable via underground mining, Most notable is the Boston Shaker and Havana Deeps northern shoot which has returned 35 meters of 5 g/t Au and 20 meters of 4.4 g/t Au and remains open. In addition IGO's Tropicana JV with AngloGold encompasses 13,000 square km on which they have already made 8 significant discoveries including the most advanced Tropicana.

IGO also has less advanced gold exploration projects at Karlawinda (100%)Cooberdale (100%) and Holleton (100%) and base metals projects at Mt. Isdell (IGO 100%) Duketon JV (IGO earning 70%) Bungalbin JV (IGO earning 70%) Lefroy JVs (IGO 70 & 100%) and Musgrave JV (IGO 51%).

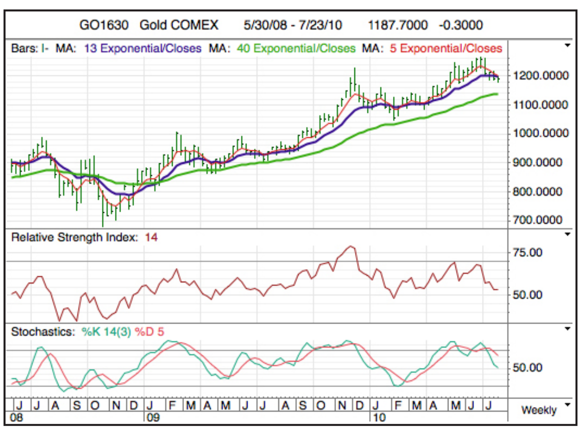
IGO is also in an ideal position for new project gerneration as it also owns an extensive archive of samples taken by DeBeers which includes 2,025 geophysical surveys 2,278 samples reporting visible gold 103,000 analyzed geochemical samples and 198,000 unanalysed geochemical samples covering the entire country. While it develops its current projects the company is analyzing the data base for 57 elements with the objective of finding new Australian mineral camps.

I think it is reasonable to expect a news filled year as the company completes the Moran nickel mine development and tests for extensions to the Moran, Mcleay and long North deposits and increases its production. The Tropicana final feasibility study completion will also be an important catalyst as will be the drill testing of the Havana Deeps high grade zones and drill testing of numerous satellite gold anomalies. IIGO also expects to complete a scoping study of its smaller Rosie Duketon nickel discovery as well as further drilling at Karlwinda and Holleton.

Independence Group has 113.7 million shares outstanding, a net profit after tax (unaudited) of A $9.1 million and has cash and net receivables of A $152 million and no debt. 57% of its shares are institutionally held.

Text Book Traders

I have written in the past how it is really a race to the bottom between heavily indebted OECD countries' currencies. Figuring out who is sinking the fastest at any given point can often be most easily discerned technically. Using the US dollar index below which is essentially the US dollar verses a basket of currencies dominated by the euro and British pound shows that the dollar is near a tipping point. On the below chart it has already peaked as has its RSI which was confirmed by a weekly stochastics sell signal, and later confirmed when the 5 week exponential moving average (EMA) crossed the 13 week EMA. The dollar is now precariously at the 40 week EMA which if the last two times it broke through it are any indication, it will have at least a further 10% to fall. Given that a lower dollar is what the US administration wants in order to stimulate exports, it looks like their wish may being granted.



At the same time the COMEX gold chart also looks weak although unlike the dollar it is comfortably above its 40 week EMA. More worrisome is that its 13 and 5 week EMA's are on the verge of crossing triggering a short term sell signal. A further negative is that its recent high was not confirmed by its RSI just as the stochastics has given a sell signal. It is a seasonally weak time for gold and that looks like what is happening. Again maintaoning high cash levels allows us to take advantage of buying opportunities as they arise and add to our portfolio gems like our most recent pick Independence Group.