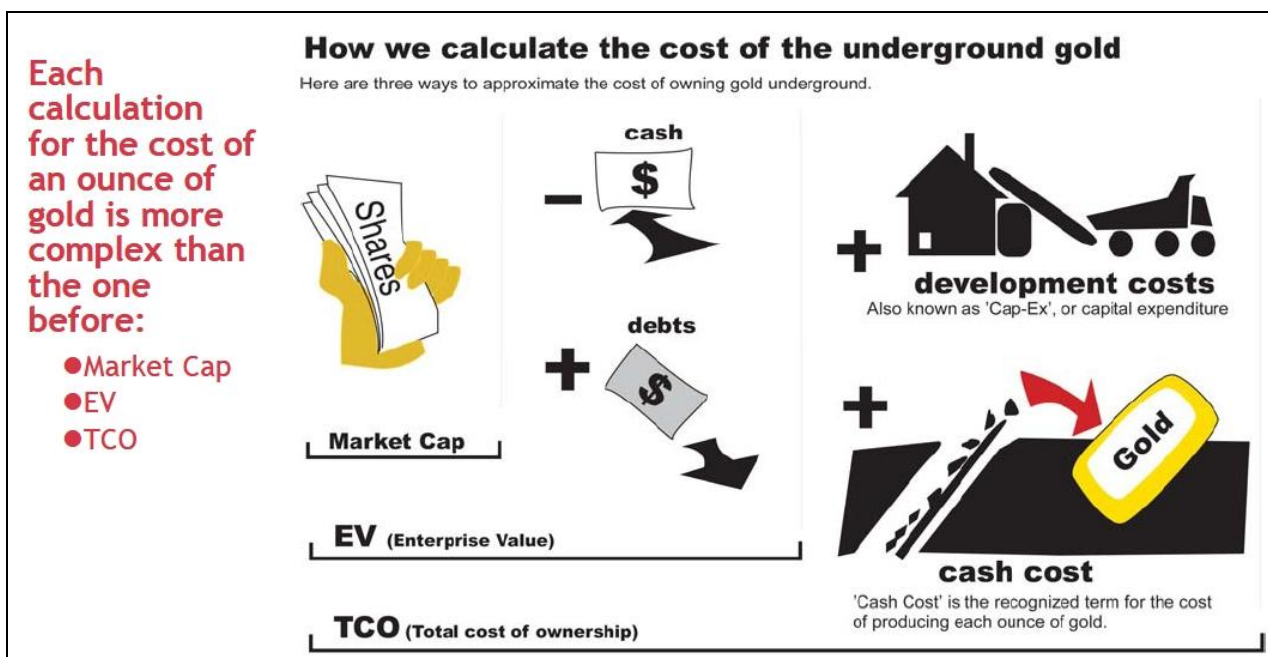


## GOLD STOCK SUMMARY – USERS GUIDE

The following is an overview of how to use and interpret the new Gold Stock Summary report. As in the past, it is built around the GoldNerds **Total Cost per oz (TCO)** concept. Companies eligible for inclusion must have a project with at least a scoping or preliminary assessment study. Categorization is by the development stage of key projects. Producers are further sub-categorized by market capitalization. A new financial strength indicator called **Net Financial Assets (NFA)** has been included to complement and reinforce the findings derived from our TCO analysis. We finish off with a look at share price performance data.

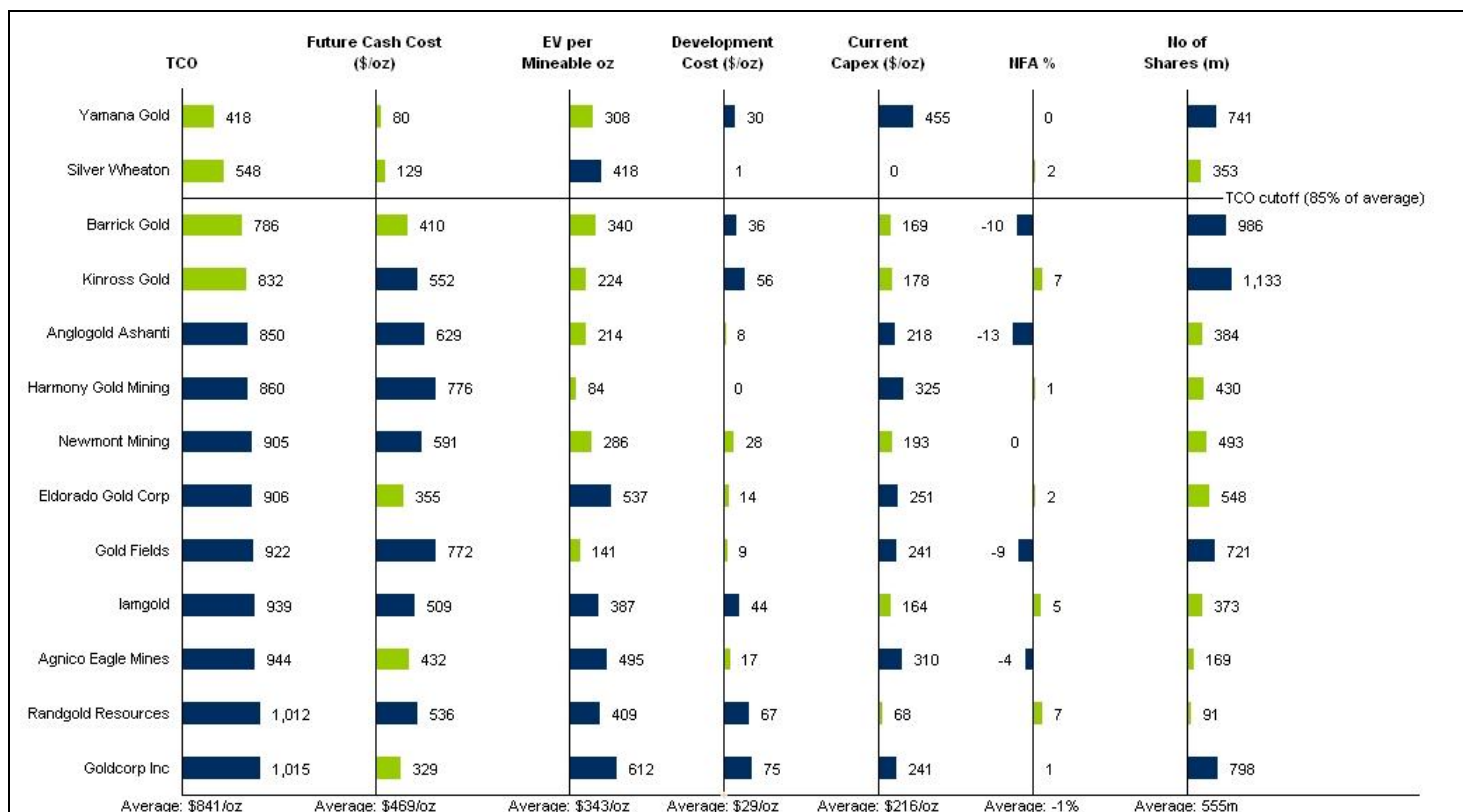
### TOTAL COST PER OZ (TCO)

I'm sure many of you have read or seen gold mining company presentations which include charts comparing the Enterprise Value (EV) per resource oz and or reserve oz for a number of different companies. The company doing the presenting will usually boast a low EV per oz and use this chart to demonstrate how undervalued their company is. If the chart is half reasonable, it will compare companies at similar development stages (apples with apples). I have seen a number of exploration stage companies, however, compare their EV per resource oz with producers! This, as most astute investors are aware, is deeply flawed based on the premise that all gold oz are not created equally. GoldNerds developed the Total Cost per Oz indicator for this reason. It is designed to take these simplistic charts you see in company presentations and add some important components. The result is a much more accurate and complete picture.



We incorporate cash costs and any associated development costs into the above equation. The result is a more indicative number, you the investor are paying, for the estimated **mineable ounces** of gold within a company's portfolio of projects. Combine TCO with some other useful indicators and you can build an accurate picture of the North American gold/silver sector and its various participants. Going to the trouble of building this picture makes it much easier to discover potential undervalued opportunities.

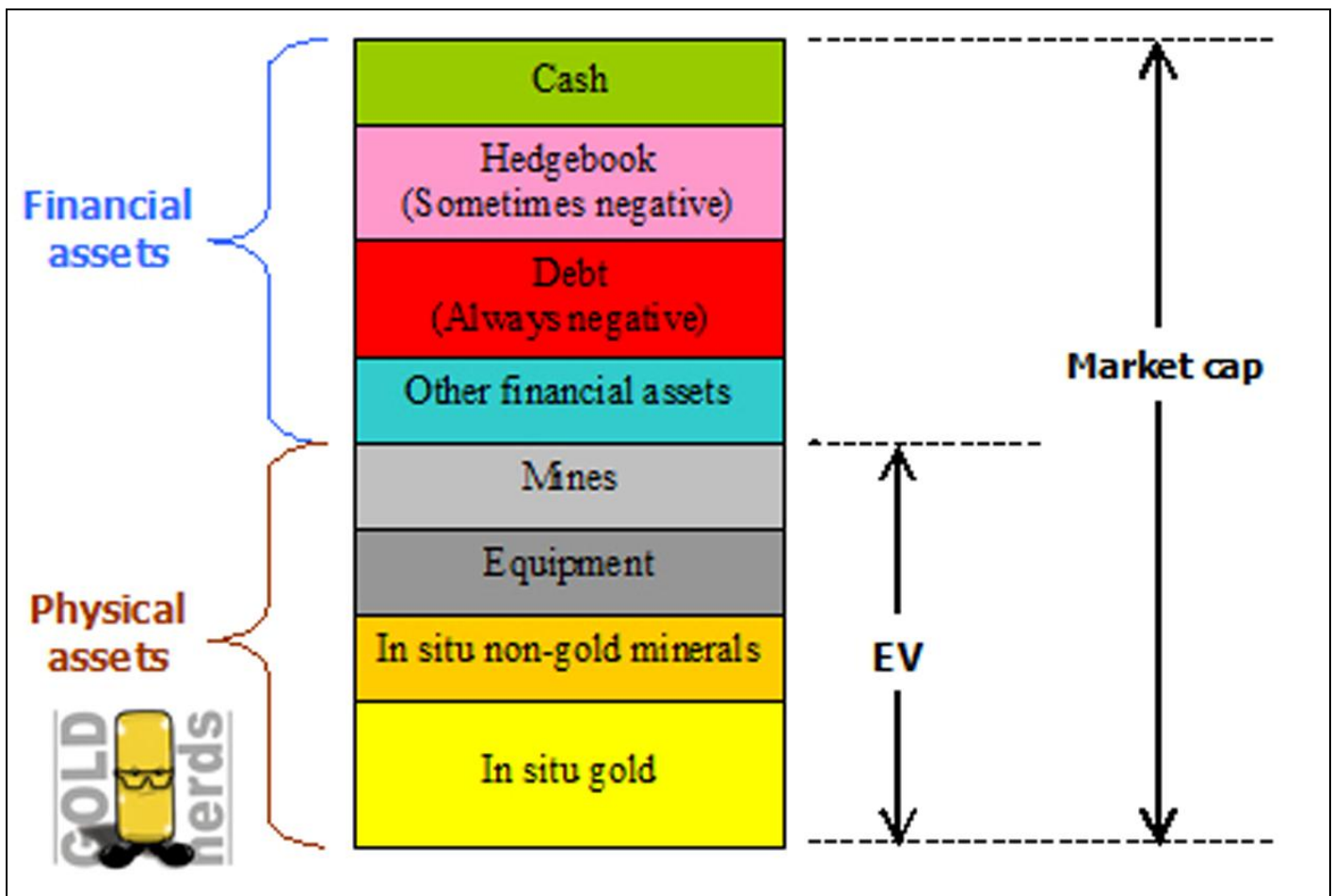
## PRIMARY TCO GRAPH (EXAMPLE: MAJOR PRODUCERS)



Each company category has the above chart along with a share price performance chart, which we will touch on later. We will now step you through each of the indicators from left to right.

- Total Cost per oz (TCO):** **Future Cash Cost + EV per mineable oz + Development Costs per mineable oz.** Companies are sorted from the lowest to highest TCOs. Note the green bars signal better than average and the blue bars below average. The focus stocks we provide commentary on (in the body of the report) have TCOs no more than 85% of the average (note the horizontal line).
- Future Cash Costs:** All our focus companies must have a future cash cost better than the category average (in the above example: US\$469/oz). Unless otherwise stated in the commentary, the cash costs reflect either a company forecast for the next financial year (in this case FY11) or, if not provided, we use the previous rolling 4 quarter average for producing projects. If the company has a development project, the cash cost parameters for these projects are incorporated into an overall average. In most cases the future cash cost heavily reflects that of the previous 12 months. Development projects can bring down the average.
- EV per Mineable oz:** This is the Enterprise Value of the company divided by an estimate of how much gold the company can realistically mine from its projects (Mineable oz). The **Enterprise Value**

is an approximation of what value the market is presently placing on the company's non-financial assets and can best be explained diagrammatically below:



In calculating **Mineable oz**, we count 100% of any reserves (for producing and feasibility study stage projects) and 20% of the resource over and above the reserve in recognition of the capacity for reserve conversion. We also include 10% of any non 43-101 compliant potential. For the development stage companies with scoping study projects, we treat 100% of the mine plan oz (as indicated by the company) as a surrogate reserve. We then add 20% of the resource (over and above the reserves and mine plans) and 10% of any potential as previously explained.

**Typically the companies with the lowest EV per mineable oz also have the highest cash costs and or development costs.** In other words, the market is discounting the value of these ounces due to their marginal nature or development risk. In recognizing this, you start to gain an appreciation of the incomplete nature of what many mining companies provide in their EV per Resource/Reserve oz charts. In addition, for the development stage categories, you will see that a low EV per mineable oz (say less than \$50/oz) usually occurs when the market gives the company little chance of successfully

developing their key projects. Common development barriers which junior companies find particularly challenging include environmental permitting issues (eg. GreyStar Resources, Astur Gold) and huge capital expenditure requirements (eg. Seabridge Gold, Pretium Resources).

- **Development Costs per Mineable oz:** This simply represents any outstanding development costs on new projects or expansion plans on existing production projects divided by the **Mineable oz** for the company. Producing companies, which have key development projects, often tend to trade at a discounted TCO. This reflects the risks associated with bringing a new project into production.
- **Current/Future Capital Costs per oz:** We exclude Ongoing Capital Costs in the TCO calculation due to the variability of this number. We continue to report Ongoing Capital Costs due to its value in explaining why a company with a reasonable cash cost may trade at a significantly discounted TCO. **For the Production categories, we use the rolling 4 quarter Current Ongoing Capital Costs per annual production oz. For the Development Stage companies, we use the Future Ongoing Capital Costs per future annual production oz based on the mining studies.** Note how in the different categories this per oz figure fluctuates markedly. In the Producer categories, you are looking at anywhere from \$250/oz to \$350/oz. In the development categories (mining studies), however, this number is not as comprehensive with the average anywhere from \$20 - \$100/oz. If the number is zero for a company in the development stage categories, this means the information wasn't available.
- **Net Financial Asset Position (NFA):** **This takes the Market Capitalization, subtracts the Enterprise Value and then divides the result by the Market Capitalization.** The resulting figure gives you a % of the Market Capitalization made up of net financial assets (or net financial liabilities if you get a negative percentage).

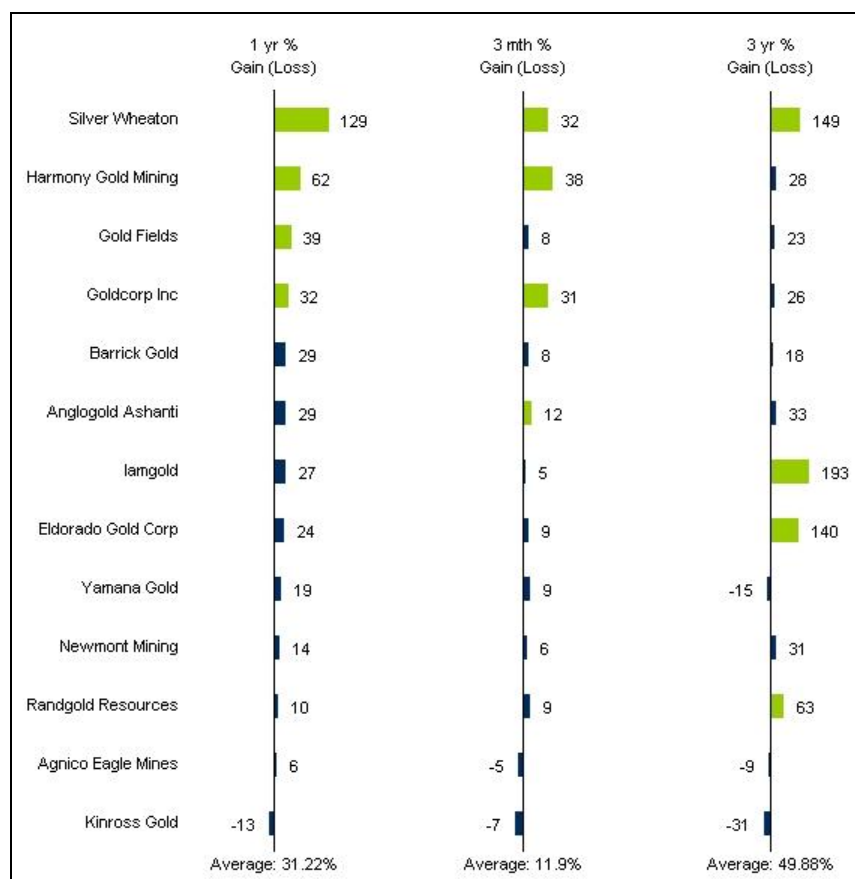
In most cases, if a company is generating surplus cash flow from its operations, this number will be better than average. If this isn't the case, it ought to prompt some questioning. Is the company investing the bulk of its surplus cash flow into value adding exploration and development projects? Has the company recently brought a new project into production or acquired an existing project? It is not uncommon for a balance sheet to be burdened with debt associated with construction costs or the purchase price of a new asset. This needn't be a problem provided the project is performing at a satisfactory level (a better than average cash cost). **Investors need to be mindful of the risks associated with companies with significantly below average NFAs. This NFA % gives you an indicator with which to follow the company's progress. We have found anything generally worse than negative 25% to be a significant risk factor. Especially if the cash costs of the operation continually underperform.**

- **Shares Outstanding:** The last indicator we include allows us to see how many shares it has taken each respective company to achieve its present level of development (relative to its peers). As a rule, the number of shares outstanding for a company needn't matter if the proceeds from capital raised generate company value. Generally, we have found this to be the exception rather than the rule. In reality, much of the valuable investment dollars contributed by shareholders **merely sustain unviable operations and fund the salary, wages and retirements of the company's workforce (this is actually more of an issue in Australia than North America).** We hence find this statistic very valuable in our analysis. Generally speaking, as investors, we prefer this number to be as low as possible, provided the company has the working capital required to sustain and grow its operations.

Any value the company subsequently creates therefore gets spread over fewer shares, meaning greater share price appreciation for you.

Many companies undertake share capital consolidations which can muddy the waters. Share consolidations are akin to re-setting the odometer of a car to 0. The car is no closer to being new again than many (not all) of these companies are to being more disciplined with their share capital. We have added a small note next to the companies in question.

## SHARE PRICE PERFORMANCE CHART



Finally, we take a look at the share price performance of the companies. One needs to be careful when looking at this information in isolation. It is easy to fall into the trap of focusing your attention on the best and worst performing companies over the shorter term (3-12 months). It is then easy to make the assumption that these companies must be “good” or “bad” based on price action alone. There are two mistakes being made here.

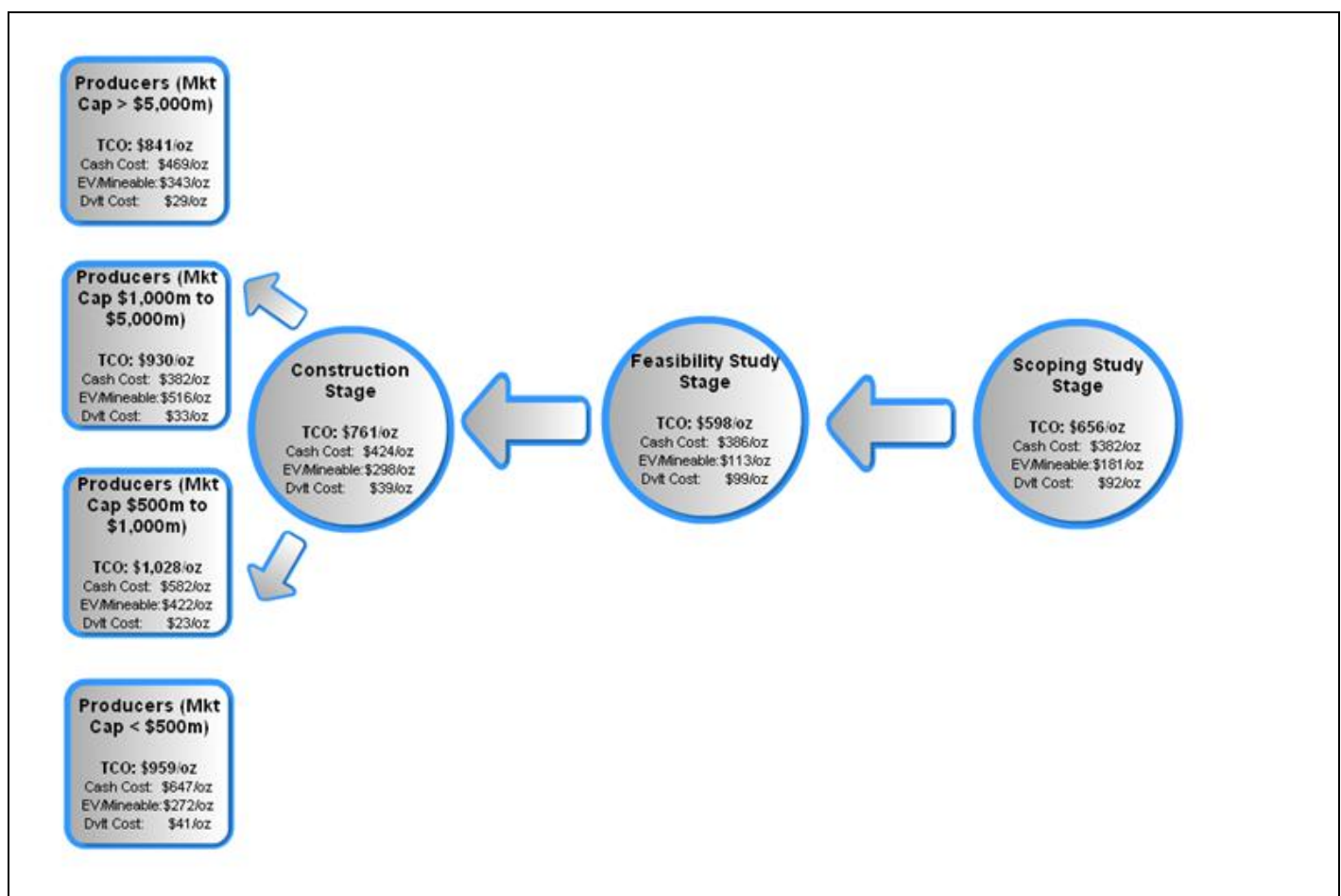
The first is called emotional reasoning and is one of the primary factors of why an overwhelming number of investors in this sector lose money. A company’s share price, over the short term, can fluctuate for any number of reasons. These price movements, more often than not, serve as a distraction. Secondly, there is no

such thing as a “good” or “bad” mining company. Labeling companies as good or bad is far too simplistic. A mining company is forever evolving with many moving parts. The circumstances and conditions under which they operate also constantly change. It is easy to fall into the trap of dismissing poorly performing companies only to see them implement changes which turn their fortunes around. On the flipside, it is equally as easy to become complacent when a company has been operating strongly over a long period of time. A few poor decisions or an event outside of the company’s control (the GFC or a weather event) can change everything! The other important thing to note is all projects have a finite life and will need to be replaced at some point. This creates a serious challenge for mining executives.

Share price performance data becomes useful when combined with the indicators we have discussed above. We typically like to focus on companies with a below average share price performance over the shorter term (3-12 months) coupled with above average indicator readings. This strategy has served us well over time. It is interesting to note that many of the underperforming companies over the longer term (share price wise) also have the worst indicator readings. This is no coincidence and makes our process of elimination that much easier.

## IN SUMMARY

Our indicators are designed to help investors gain an understanding of the interrelationship of different factors which give a gold/silver mining company value. It is a useful exercise to look at the different development stages and see the value added as a project progresses. Note how the average TCO gradually increases.



Source: December Quarter 2010 Gold Stock Summary Report

As an investor, your goal is to ultimately see a better than average portion of the TCO made up by the EV per mineable oz. This component of the TCO is primarily linked to share price activity. **Theoretically, the smaller the costs of getting the gold out of the ground (cash costs and development costs) relative to the gold price, the more value the market will attribute to the mineable ounces.** For example, in the above summary, notice how for the Production categories the EV per mineable oz typically reflects the cash cost. When the cash cost is lower, the EV per mineable oz is higher and vice versa. Also notice how the better economies of scale are largely reflected by a lower average cash cost as the company gets bigger in size. One exception we see is in the largest producer category which can partially be explained by the higher cash costs

of the major South African producers (Examples: Harmony Gold, Goldfields and AngloGold). Another thing of note is how the average TCO declines as the Producer categories get larger. Higher market capitalization companies, given their size, typically experience difficulties in maintaining sustainable growth, which is reflected in a lower EV per mineable oz. We can see in our example category above (The Major Producers) that the companies which enjoy the highest TCOs (over US\$1,000/oz) typically have the strongest growth profiles (Goldcorp and Randgold)

When looking at the Development stage categories, another factor comes into play. Typically we see the EV per mineable oz and consequently the TCO rise as the company gets closer to the production stage. As we enter the construction phase, we start to see more value being attributed to the mineable oz (US\$298/oz). Some of this represents a simple transfer from the Development Cost section (which declines as the mine gets built). The rest is attributable to the market valuing these ounces more as the project advances towards the all important production stage. In the Feasibility and Scoping study stages, a look at the EV per mineable oz for a company will often tell us if the market has any confidence in the development potential. Anything less than US\$50/oz typically suggests very little in the way of market expectation. The mix of companies in each of these categories can therefore largely influence the category averages. For example, we can see in the Feasibility Study category that the average EV per mineable oz is actually less than that in the Scoping Study category (\$113/oz versus \$181/oz). This difference can not be explained by higher average cash costs and or development costs which are more or less the same for both categories. This would suggest that there are more companies in the Feasibility Study category with projects that the market is skeptical about (lower EV per mineable oz). We previously mentioned some examples in the EV per Mineable oz description above.

The average cash costs for the production categories are generally much higher than those under the development stages. **Mining studies nearly always present a project under the best case scenario (it helps with the financing stage).** The reality will usually be somewhat different, with cash costs being anywhere from 30 - 75% higher than the underlying studies (based on the statistics above). This largely explains the discount we often see in a TCO for companies with significant development stage projects.

**The companies which experience development success in terms of emulating their mining studies, will see a larger proportion of their TCO reflected in EV per Mineable oz (not the cash cost). In addition, having less shares outstanding, means this success will translate into much stronger share price appreciation.** Randgold Resources (despite recent weakness) has been a wonderful example of this over the last decade or so.

**As an investor looking for prospective producing stocks, you typically want to look for companies with a better than average cash cost and TCO, not to mention a sound share structure (at least better than average).** It then becomes a simple game of patience. You wait for the market to bid the EV per mineable oz and the TCO up to a level reflecting the operational performance (at least the TCO category averages). If in the mean time the company can build reserves as well as improve the operational performance, this will only serve to further your cause as an investor.

**For development stage stocks there is an additional element to consider. You need to balance development risk with valuation upside potential.** There is no use investing in a company with a low EV per mineable oz and TCO if the key project(s) have very little chance of being developed. As we have discussed already, this may be due to environmental and political risks and or unrealistic capital requirements. When you invest in stocks in the construction category, for the most part you have heavily



reduced this risk but for that you pay a premium in the form of a higher EV per mineable oz and TCO (less upside). When you invest in the scoping and feasibility study categories you are taking on this risk but will be rewarded for it if everything goes according to plan. Osisko Mining is a good example of a company in the Construction category that has successfully progressed through this cycle over the last few years with excellent share price growth to show for it.

We trust you will find this new format of the report a vast improvement. Whilst most of the foundation concepts are in place, it is important to note that this remains a work in progress. We have immediate plans to further strengthen the GoldNerds TCO concept and look forward to sharing the results with you.

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