



GOLD WORLD

Zinc prices have increased a whopping 187.6% in the past twelve months alone.

But because of severe supply constraints and skyrocketing demand, I still think zinc is . . .

The Most Undervalued Metal on the Market Today

Dear Fellow Investor,

After centuries of use, zinc has become one of the most important and functional metals known to man. And while this largely ignored mineral may not be as sexy as gold, silver, or platinum, zinc plays a fundamental role in a wide range of the industrial and consumer products that keep our society moving.

In fact, the bluish-white mineral is now the fourth most common metal in use today—trailing behind iron, copper, and aluminum in global consumption. And this exactly why we as investors should be interested. Zinc is a vital cog in the modern economic machine.

So, what the heck are we using all this zinc for, anyway?

Well, without a doubt the single biggest use of zinc is for galvanizing steel. Galvanized steel is simply standard, cold-rolled steel coated with a thin layer of zinc. The zinc layer protects the steel from rust and corrosion, making it ideal for construction.



Galvanized Steel

Galvanized steel is used virtually everywhere. As a matter of fact, it's most likely that you're completely surrounded by the protected metal right now. That's because galvanized steel is one of the most widely used metals in residential construction today in the form of beams, floor joists, nuts, bolts, studs, trusses,



Zinc Ingot

roofing nails, HVAC ducts, etc.

As you can image, demand for galvanized steel is nothing short of astonishing. The United States alone consumes nearly 40 billion pounds of the stuff each year for a multitude of different applications. And that's nothing. Worldwide, galvanized steel consumption was estimated at 418 billion pounds in 2005!

Now, galvanized steel is only half the zinc story. It currently accounts for about 50% of the world's zinc consumption. But what most folks don't realize is that zinc has a multitude of other uses as well.

Zinc is also used for making die-cast components from door knobs to car parts, along with tens of thousands of other products that you need in your everyday life, such as casings for electronic components. And, of course, zinc is alloyed with copper to make brass, which is used in a vast array of products. The myriad other uses for zinc include sun screens, phosphors for TV screens, medicines, fireworks, paints, cosmetics and plastics . . . the list goes on and on.

This rapidly growing catalog of applications is progressively adding to zinc's importance in our modern, industrialized world.

So, it's no wondering that global demand for zinc has increased well over 250% in the past 45 years.

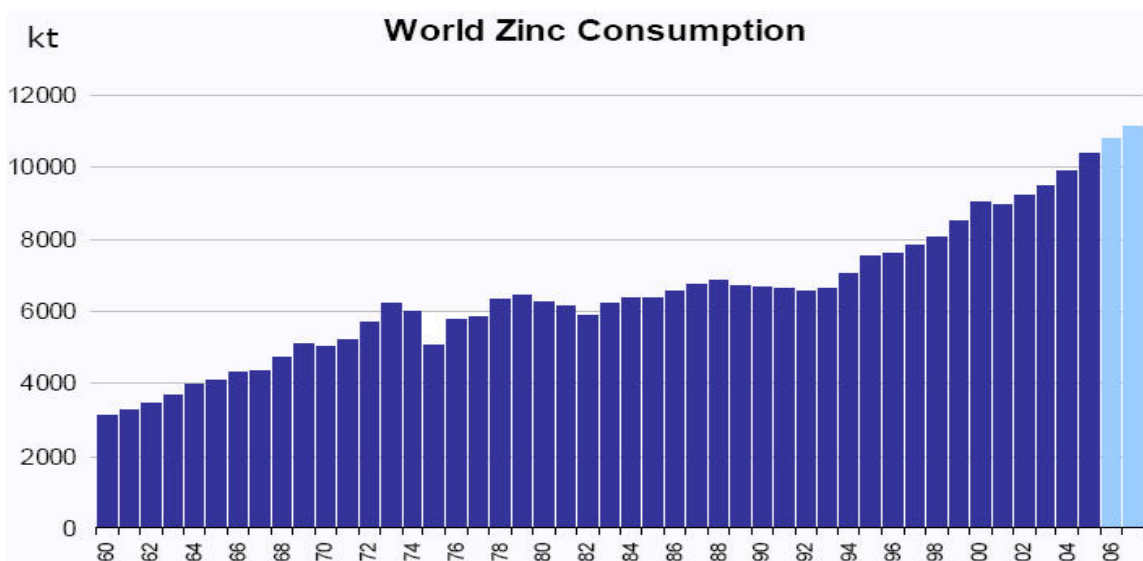
Take a quick look at the chart at the bottom of the page. As you can see, worldwide zinc consumption grew at an average annual rate of about 2% between 1960 and 1990. But since 1993, annual worldwide demand has been growing by roughly 3.2%. And by all accounts, this is just the beginning.

The International Lead and Zinc Study Group (ILZSG) says global demand for refined zinc will increase an impressive 3.9% over last year's demand to 11.06 million tons in 2006. Next year the ILZSG expects demand to increase again to 11.35 million tons. According to their figures, after falling in 2005, U.S. demand is expected to recover strongly this year, increasing 7% over last year, followed by flat growth in 2007. Similarly, in Europe, it is anticipated that demand will rise by 3.4% in 2006 but remain unchanged in 2007. Growth will be strongest in Asia, where demand is forecasted to rise over last year's by 9.1% in India, 4.5% in Japan and 4.4% in the Republic of Korea. And we can't forget about the waking dragon, China.

As is the case with every other commodity in China, escalating consumption has been a major factor in the increased demand for zinc. In recent years, China has become the world's largest consumer of zinc, with demand increasing 8% to 10% per year. But it wasn't until very recently that demand really started to pick up.

During the first nine month of 2003, zinc demand grew an amazing 22%. That was just the beginning. Demand grew again in 2004. This time consumption figures were 27.8% over the previous year's. Last year Chinese zinc demand grew another 13%, and figures for this year are expected to be similar. Now, get a load of this: Experts predict that by 2007 China alone will account for nearly 30% of global zinc usage! To put this in perspective, that's more zinc consumption than in all of Europe!

As you would expect, the construction industry is the largest user of galvanized steel in China. And why not? Heck, the country uses enough construction material to build a city the size of Philadelphia each month. However, increasing motor vehicle production is also a substantial source of demand.



This year, China's automobile sales are expected to reach between 6.8 million and 7 million—making up one tenth of the world's total. This figure represents a 100+% increase since 2002. Chinese auto sales are expected to continue to grow by leaps and bounds. Experts predict sales will climb to 10 million in the year 2010 and to 20 million in 2020, at which point China will overtake the United States and become the world's largest automobile market.

And speaking of China, get this: Throughout the 90s, China was a major player in the zinc supply game. In fact, the ancient country accounted for roughly 63% of zinc's global supply growth. But now, because of the country's insatiable hunger for the galvanized metal, China has actually gone from being a significant zinc exporter to a net importer!

Monthly Chinese Net Zinc Exports



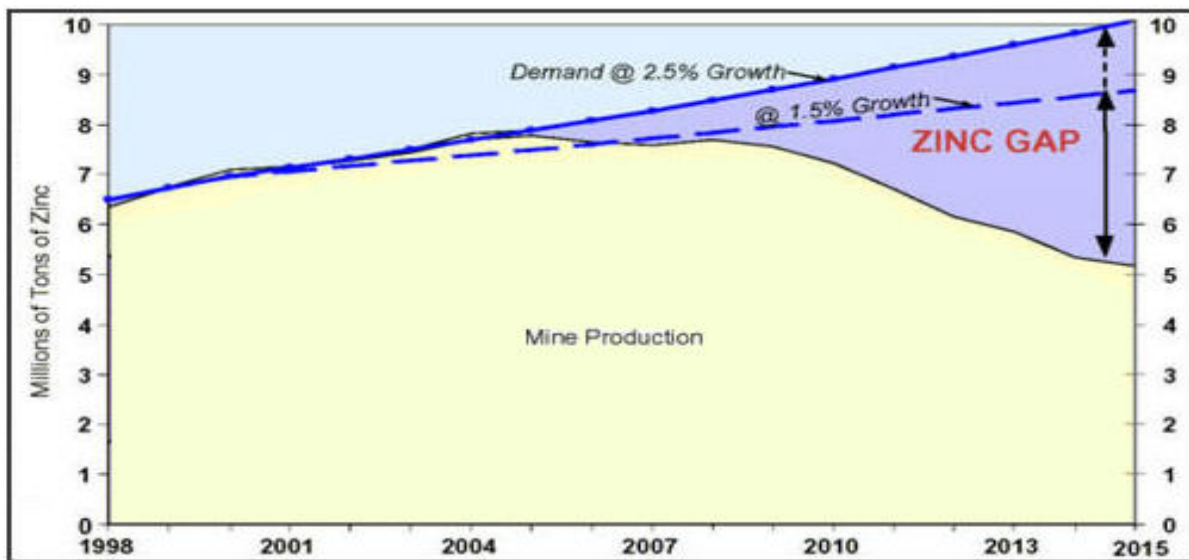
As a result of this ever-growing global demand for zinc, CRU International, an independent business analysis and consultancy group partly focused on the mining and metals, recently forecast that 2.5 million tons of new zinc mine production will be required by 2007 to meet expected demand. Overall, it's projected that in the next few years the zinc mining industry will need to bring *two* brand new 200-million-pound-per-year mines into production each year just to meet the growing demand.

And that's not all. The industry will also need to bring more mines of that size online to replace their old depleting ones.

It sounds like there's a simple answer to this. Find new deposits, right? Well, there's a catch to that. Because of the thinning supply of geologists who really know how to find a worthy zinc deposit, it's nearly impossible that the industry will be able to meet this goal. And really, the lack of good geologists may be the least of the industry's concerns.

Unlike some other commodities, there are few significant zinc deposits left to be discovered in the world. But for the short-term, it doesn't really matter how many large deposits the world has. Thing is, it requires hundreds of millions of dollars and can take up to 15 years for newly discovered zinc deposits to reach the production stage. No new discovery can supply urgent demand. So finding brand-new deposits won't solve the supply problem. We'll have to make due with the mines we have now. And that's a problem too. Because of decades of low prices, there's has been little serious investment in zinc mining. This has lead to a peak in zinc's global production. Because demand is expected to continue growing, there will be a serious zinc shortfall in the coming years.

Take a look at the chart on the next page. Even if global demand for zinc increases at a modest average rate of 2.5%, it's expected that the shortfall between mine production and demand will be close to 5 million pounds by 2015. In other words, only about half of the zinc the world will be using by then will come from mines. The other half will have to come from recycled materials or stockpiles. And that poses a problem, too.

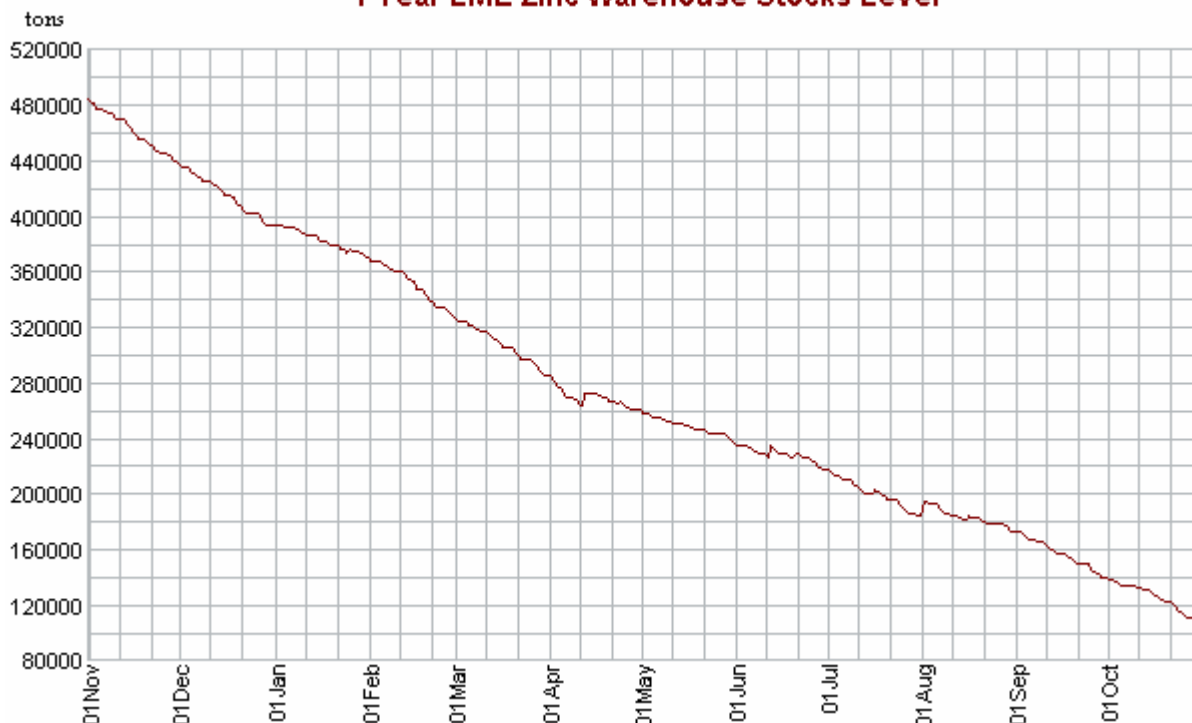


One of the main places we look to gauge base metal supplies, as well as the overall the health of the sector, is the London Metal Exchange (LME), the largest non-ferrous metals exchange in the world.

In April 2004, LME zinc warehouse stocks topped off at about 784,000 tons. Today, only two and a half years later, these stocks have plummeted a whopping 86.5% to about 105,000 tons. In the past 12 months alone these warehouse stocks have fallen 78.1%. Take a look at the chart below:

Now, here's what really knocked my socks off about these stockpiles: The LME supplies are only enough to satisfy the world's total demand for four measly days. Talk about tight! And supply levels aren't even close to stabilizing. It looks like these supplies will continue to knife downwards over the next few months. Rising global demand and concerns over supply have been the driving forces behind the recent rise in zinc prices, which have moved up over 175% in twelve months.

1 Year LME Zinc Warehouse Stocks Level



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Zinc prices rallied late last year, averaging \$0.63 per pound in 2005. Compare that with an average of \$0.48 per pound the previous year and the \$0.35 per pound average of 2002 and early 2003. Recently, zinc has been riding an unparalleled price rally. Zinc prices have skyrocketed **82.7%** since mid July 2005. Compare that to price changes of other major metals over the same time period:

- Aluminum +54.9%
- Copper +102.3%
- Gold +49.4%
- Lead +104.5%
- Manganese +58.7%
- Molybdenum -23.1%
- Nickel +130.6%
- Palladium +77.4%
- Platinum +37.9%
- Silver +81.0%
- Titanium +93.5%

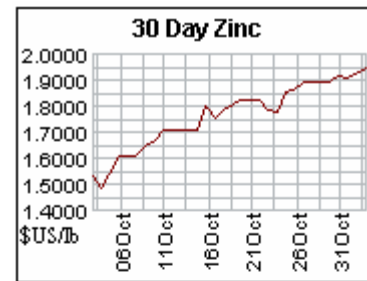
In fact, when I began this report just a few weeks ago, zinc was trading at around \$1.70 per pound. Now it has broken its all-time high and is selling for over \$2.00 a pound. So the obvious question is, have we missed the big moves?

Not likely. The fundamentals that have driven zinc this far are still in place. Production and warehouse stock levels are plummeting while demand is relentlessly marching higher.

I certainly expect zinc to be selling over \$2.50 a pound in 2007. After that, the sky's the limit. With the right conditions I believe we could be looking at \$5 or \$6 zinc within a few short years.

So how can you leverage higher zinc prices?

Personally, I like the upside of junior explorers right now . . . especially those trading on the TSX Venture Exchange. I recommend looking for junior mining



firms with savvy management, a proven track record and a decent land package in a geopolitically safe country. These firms should also have mid- to advanced-stage properties. Historic production and drill results are always a plus. I expect firms like these do to very well over the next three to five years.

The overall metals bull market has once again become stronger than ever. And I know exactly where my money will be. Where will you put yours?

Until next time,

James West
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