Metal Markets Outlook

Long Term Minerals Price Expectations

Stephen Allen

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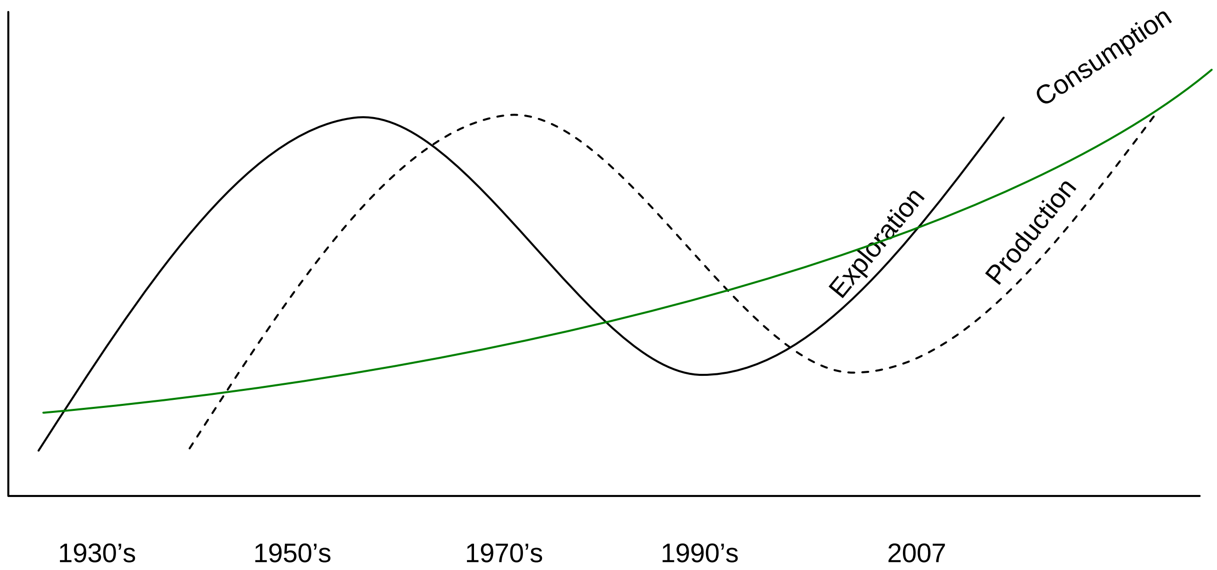
The current boom

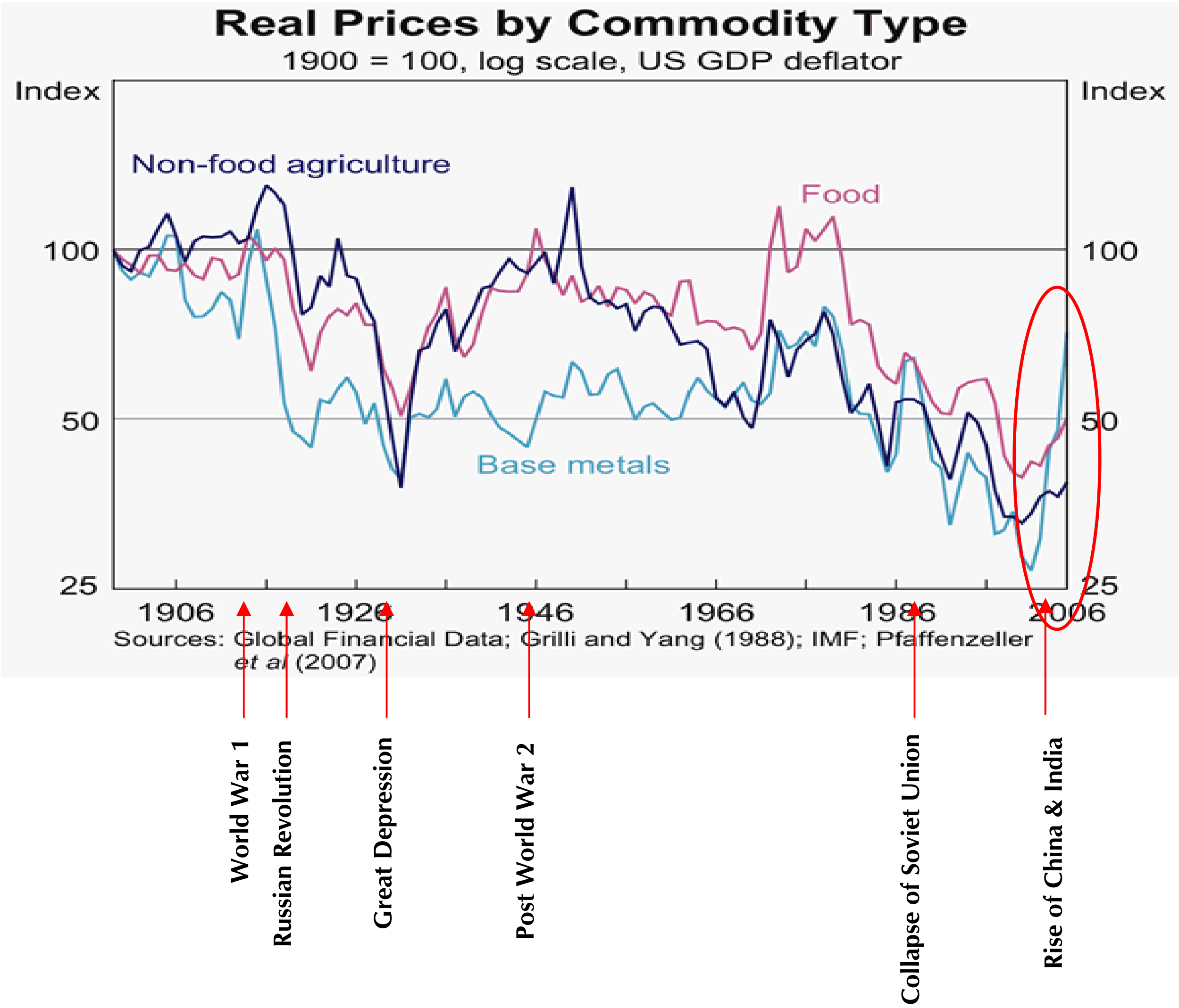
The Lag Effect

- Commodities bear market slowed exploration for 15-20 years in 1980s-2000
- Led to current low production levels
- When combined with escalating demand

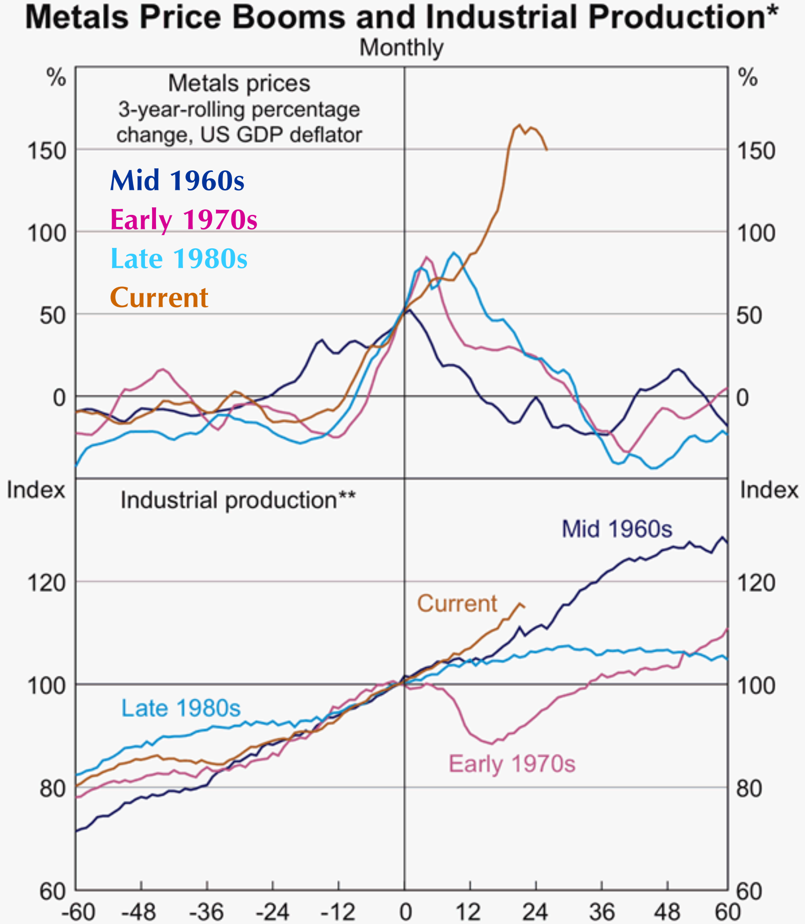
⇨ **Enormity of current boom**



How does it compare?



How does it compare?



* Months before and after 50 per cent increase in real base metals prices
** OECD area prior to 1994; includes China, India and Russia thereafter
Sources: Global Financial Data; IMF; Thomson Financial

- **1960s:** Demand for metals did not rise, but production escalated
- **1970s:** Growth of demand for metals fell while supply was boosted by investment in base metals production from '60s
- **1980s:** The oversupply created during post World War II led to a 25 year bear market between the '80s and early 2000
- **2007**: Rapid and prolonged recent growth in prices has been met by relatively modest supply response to date
- After large price declines in '80s and '90s, global investment in base metal production stayed low, and the rate of significant discoveries of new resources slowed
- This lack of current supply capacity, and long gestation period for new investments to begin production has resulted in the magnitude of the current price boom

How long can it last?

Are the right ingredients there?

Brazil

Russia

India

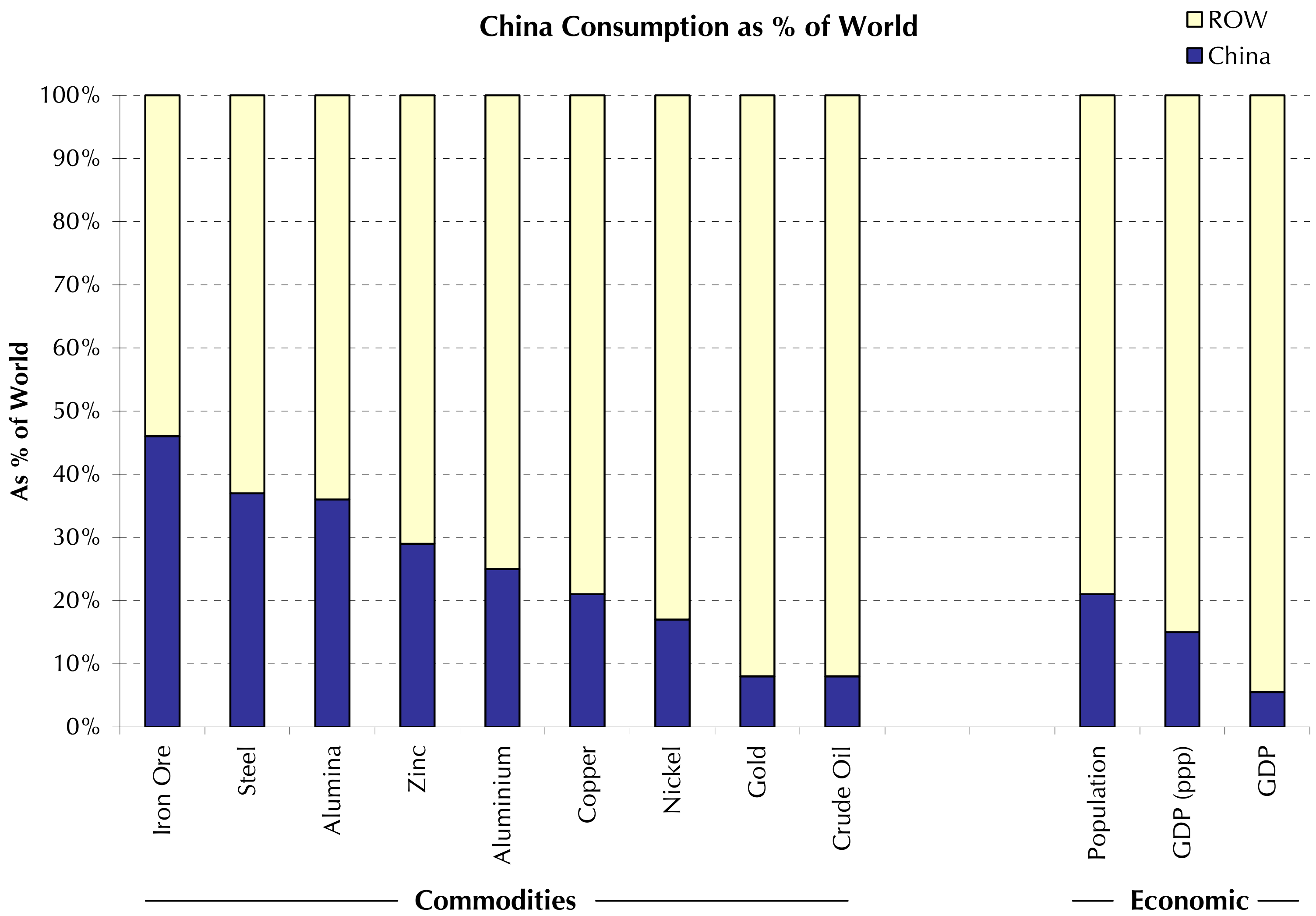
China

Growth of the BRIC countries is the key

- 2006: real GDP rose 10.7% for China and 9.2% in India
- Forecast that China will continue to grow at >11% for at least next 2 years
- Market expectations are that by 2050 the BRIC countries will have combined GDP of $196 trillion (2006: $18 trillion)
- Population Growth
  - BRIC countries now account for over 40% of world population

Share of Global GDP

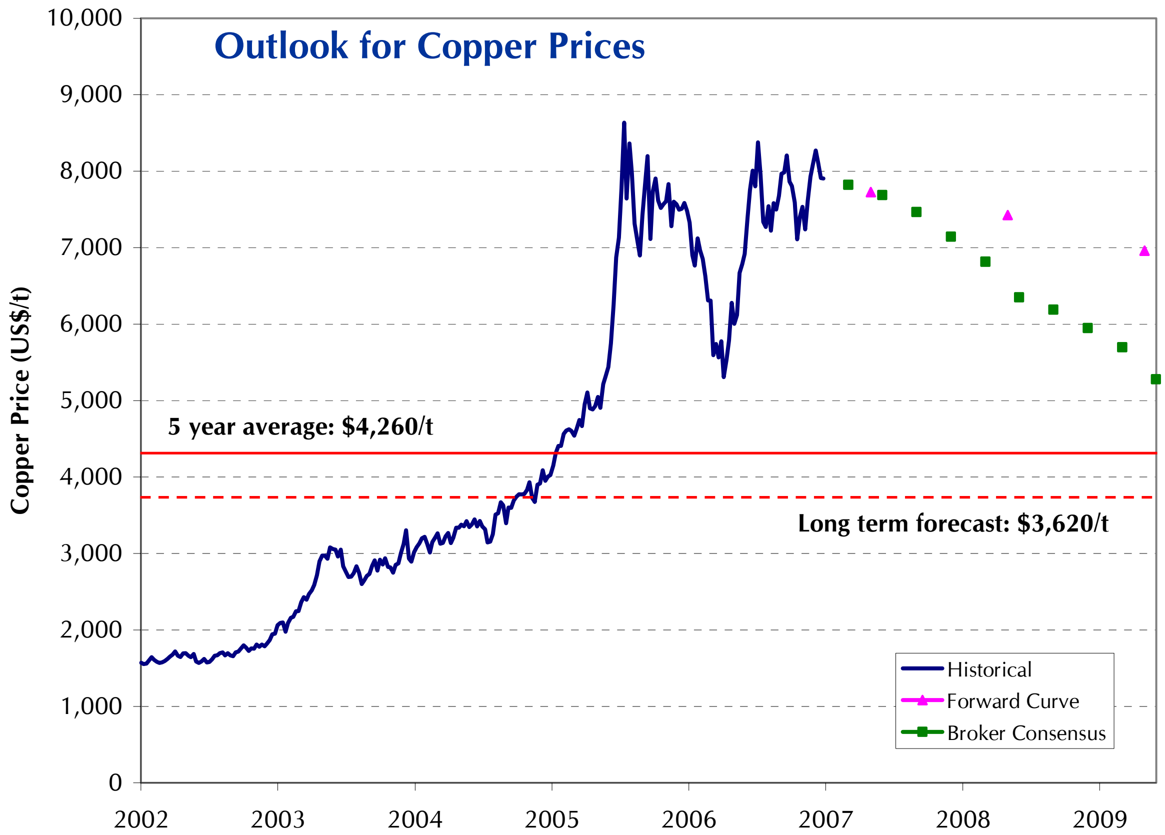
How long can it last?
Influence of China alone



How long can it last?

What the forecasts look like...

- Strikes keeping supply growth < demand growth
- Global stocks < 2 days global consumption
- Delays in greenfield projects



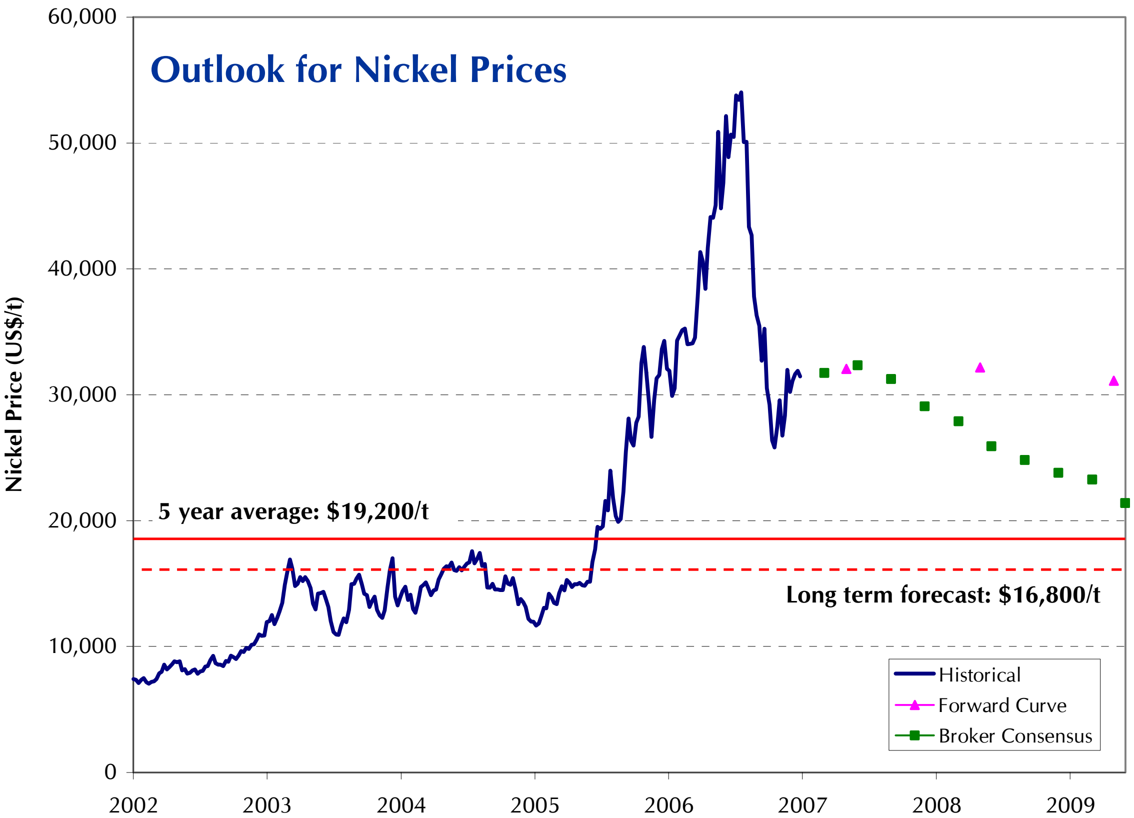
…and Zinc

- Signs of increasing mine supply and steadying global demand
- Large scale projects set to come on stream

… and Lead

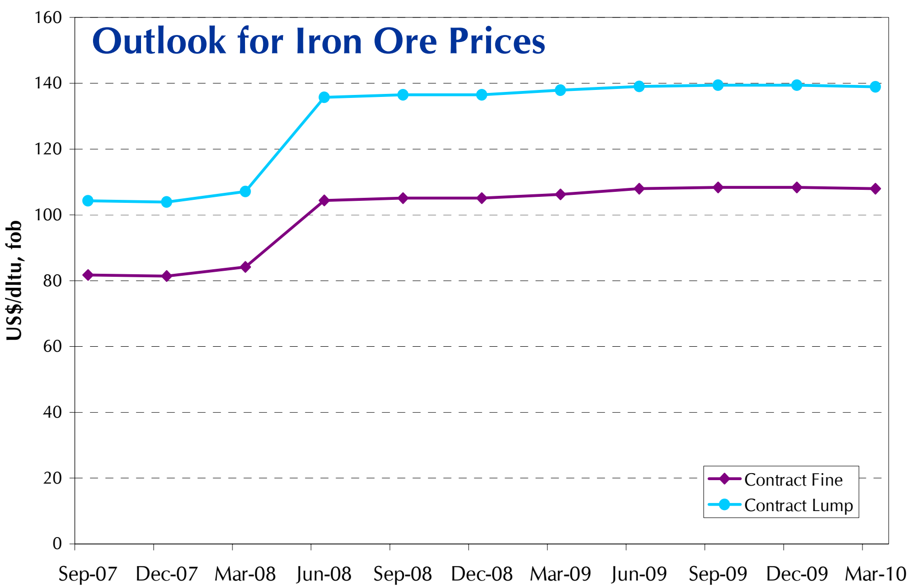
- Suspensions of exports ➔lowest stock levels in 17 years
- Further impending mine strikes in Peru

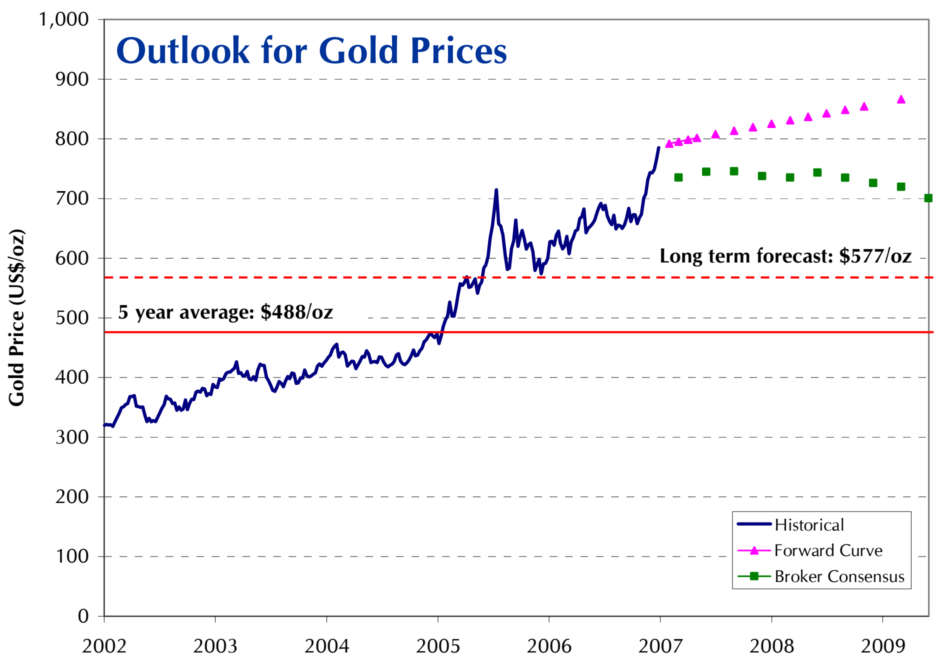
…and Nickel



- Stock levels plummeted in March/July
- Cuts in Chinese stainless steel production July/August

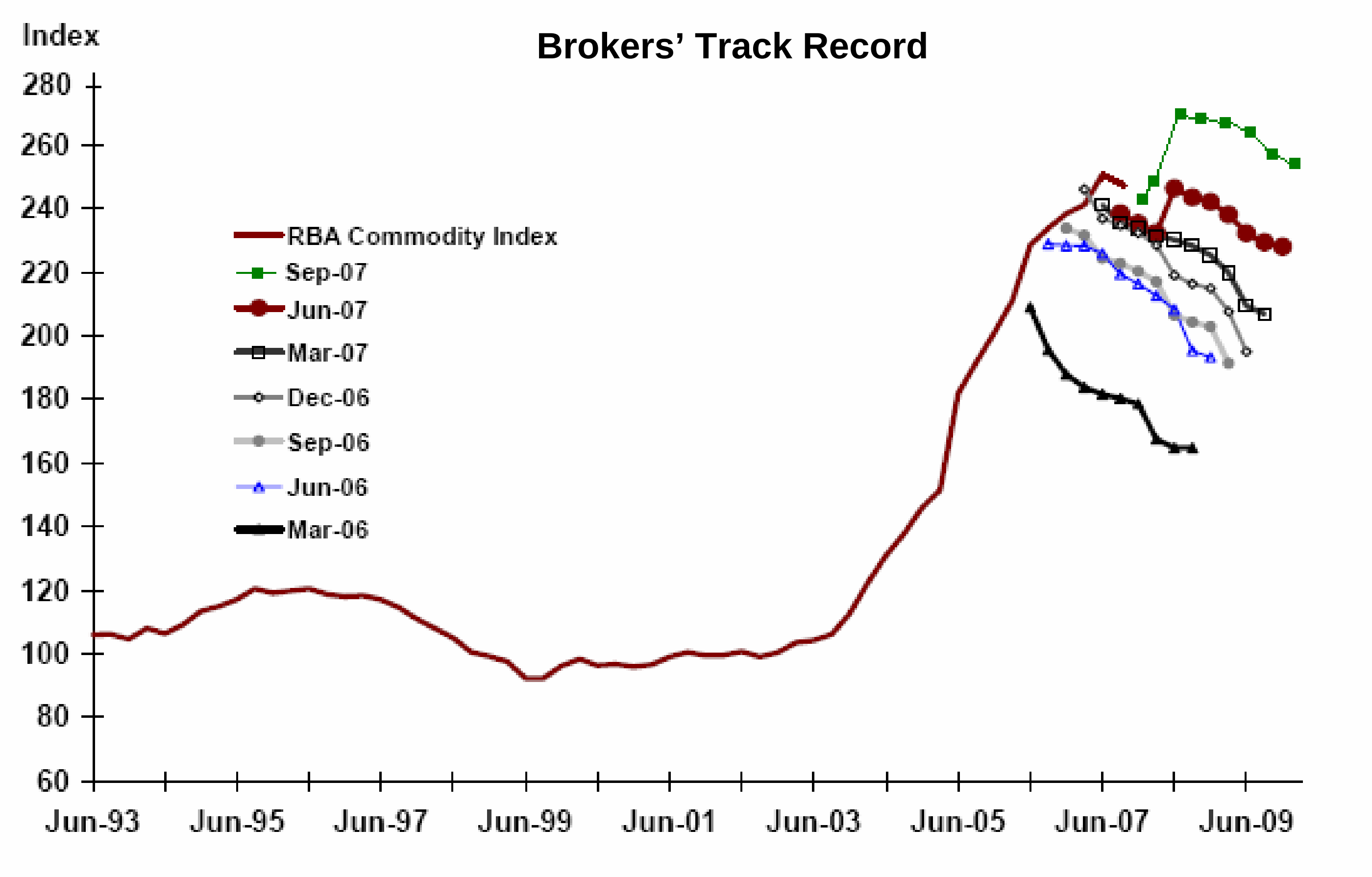
…Iron Ore and Gold





The recent track record of market analysts has been poor

On the whole they are continually seeking to catch up with reality



Summary: reasons for and against

Reasons for…BULL	Reasons against…BEAR
■ BRIC countries show no sign of slowing ■ World economy is still strong ■ Rate of world-class discoveries is declining ■ Majors believe in the Bull market – Paying cash for large businesses • Rio for Alcan • BHP for WMC • Norilsk for LionOre • Xstrata for MIM • Peabody for Excel Coal – Majors can help sustain the Bull market by rational pricing	■ Brokers' forecasts – But are they to be believed? Continue to predict a fall…however, constantly revising when it will commence ■ Technology advances – May cause supply to come on earlier ■ Changing risk profile – Ability to access resources in areas that previously could not ■ Common perception that it is simply not sustainable

Will the resources sector be stronger for longer?

- **RFC believes this cycle will be stronger and run longer than any previous cycle**
  - Although there will be volatile periods along the way
  - When it eventually does weaken, the expectation is that it will be a soft landing
- Current market conditions
  - Combination of low inventories and low production rates
  - Prices above marginal cost of producing industrial commodities
  - Escalating demand
- General consensus is that over the very long term resource prices will weaken from current highs as output catches up with demand. However, higher long term production costs (wages, fuel and equipment costs) and continued growth in demand are likely to keep prices above historical averages.

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