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Gold Will Start Shining Again: An Interview with Rob McEwen, U.S. Gold

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Legendary mining executive Rob McEwen (U.S. Gold Corporation (UXG:AMEX, UXG:TSX) and Goldcorp Inc. (GG:NYSE, GG:TSX)) talks with The Gold Report about the plight of the junior miners. Rob shares some names he thinks are well positioned to weather the storm, and perhaps find that "big discovery" that will help jump-start the sector. He's optimistic that the price of gold will rise again, believing we're in a seasonal slump, and the fundamentals remain strong.

TGR: The junior mining stocks have taken a beating lately. Some people believe there should be a turnaround in the juniors in the fall... do you agree with that, and if so, what is the catalyst that's going to get them moving?

RM: I do agree with it, although I'm not sure if it will be in the fall, but it should be coming soon. Since last August we have seen all the speculative money come out of the market because of the sub-prime issues. Then, despite the price of gold going up, none of the gold stocks followed until February, when money started going into the senior producers that were generating positive cash flow. And people were avoiding the junior exploration companies in droves because they're negative cash flow, spending money to find a deposit.

It's all about security and safety of capital, and our sector is unfortunately not viewed as a safe place to be putting money in. But at the same time, with the higher metal prices, the producers are just watching their treasuries bulge with cash, but their reserves are going down, so they're going to have to replace their reserves. So, I think you're going to see the majors feeling more confident, looking at the juniors and saying, "These represent bargains," and start buying.

The catalyst, as it's been in most situations like this in the past, is going to be a major discovery, something that wakes investors up and shakes them out of their lethargy. You never know when that's going to happen, but discoveries often happen at bottoms of markets when everybody's given up and said, "Well, that's a sector that I don't want to put my money into."

TGR: With reserves going down, essentially we have a supply and demand issue.

RM: They have to replace their reserves.

TGR: Would we actually need a major gold discovery for the producers to come in and start buying? Wouldn't they be in essence be speculating on some type of discovery?

RM: I think they're very cautious. Liquidity in the juniors is very, very limited, so if someone wants to get out, it's not always that easy, and the same is true if someone wants to buy. There are not a lot of buyers out there. When it does turn, it's rapid and you will see a 20% to 30% move before you can really realize what's happening.

A lot of the juniors have brought properties into production that have disappointed the market. The cost escalation in the industry has caught everybody off guard. Projects are being finished, but they're over

budget, they're delivering less than they promised, and so the shares aren't performing the way investors expected. There has been a big disappointment when the promises haven't been realized.

TGR: Is it the amount of gold that's disappointing, or the production costs?

RM: There are two elements, disappointment and economics. Say someone has gone way over budget; they're producing less gold than they said there would be and at higher cost. So rather than reacting positively when they go into production, the market comes along and pans that story. Investors move on to a better story.

The other factor is the cost escalation, which is gigantic right now. When I was running Goldcorp we built the Red Lake Mine in '99 and 2000. Then, you could go to a supplier and get your capital goods on short lead times. The consumables were in ready supply and reasonably priced. Drilling and assay costs were all quite predictable, but in the last three to four years, the cost of everything has gone through the roof.

So, say a company says it has a deposit with a feasibility study. If the study is more than four or six months old, you have to increase the cost estimate by at least 25%. And in some cases, it's much more than that.

TGR: Is there a geographic area that we should focus on where you would expect a discovery to come from?

RM: Discoveries come usually from the most unexpected quarters. The market is so sensitized to governments stepping in and taking a bigger piece of the deposit or withdrawing permits, or there is some trouble in the area that is obstructing the company from doing anything with the deposit once they've found it. Certain parts of the world might be very prospective for minerals, but not very good from the standpoint of a shareholder continuing to own what they have in the property. I haven't been a big fan of Africa and certain parts of the former Soviet Union. There are very few places in South America I would want to go.

TGR: You've focused mainly on Cortez Trend in Nevada?

RM: I am up and down North and South America. I like the Cortez Trend in Nevada because of the infrastructure in place and the size of the gold deposits there and the currency. It's in dollars and I expect the dollar to fall further against gold. So, the cost of exploring is going to be less in Nevada than, say, in Canada or in Australia or other parts of the world where the currencies are appreciating against the dollar.

TGR: The price of gold fluctuates not necessarily on supply and demand but because of anxiety over the value of the currency. How do you, as someone speculating, exploring, and mining gold, reconcile all that?

RM: The cost of producing an ounce of gold is going up. In 2001, the average price to produce an ounce was \$160. Today, the cost is over \$400. And that's in the space of six years, seven years.

Gold is a monetary metal, and therefore it plays a very different role than most of the other metals that are produced, which are industrial. Gold is a store of value, and at certain times, such as we're in right now where there's a great deal of financial uncertainty, people will seek to protect capital by using gold, as a place to put their money. And I can see much, much higher prices than we have today coming out of that concern about the financial system imploding on itself right now.

TGR: With the risks that come with investing in the juniors, what do you recommend?

RM: You have to diversify your portfolio across a number of juniors. And you have to recognize the very uncomfortable fact that a junior exploration company, despite all they say, can go out and drill in the right place and have the right showings, but it might never find a deposit big enough to be economical.

TGR: Given all the uncertainty—the longer lead time, escalating costs—the prices of gold juniors are down. Do you find them attractive now?

RM: I think they're becoming attractive. They've lost a lot of the appreciation they have had over the last few years. There's a very cyclical aspect to this. Somewhere along the way someone is going to start buying those juniors for what they have.

And I think we're at that point; summer is historically a slow period for mining stocks and gold stocks, and it's certainly very true this year that few people are paying attention. I always like looking at investments when other people are shunning them, and I think we're in that stage right now.

TGR: Someone we spoke with recently claimed that the new gold ETFs are taking away the money that would have gone into the junior mining stocks. Do you agree with that viewpoint?

RM: I do think the new ETFs have taken money out from the seniors and the producers. The gold ETFs were the product of the World Gold Council, which is largely the senior gold producers who really wanted to add some stability to the gold price. Their ambitions weren't very large; they just wanted to generate a small appreciation in the gold price to stabilize their revenues. I have to chuckle somewhat when I look at what happened, because it's cannibalized them. The very people who were doing all the hedging were the ones who created the ETFs, and the ETFs have driven the price of gold up with all the buying and caused these hedgers to run to cover their hedges and incur large realized and unrealized losses.

And if people wanted gold exposure, the juniors offer a different exposure. In the juniors, you're looking for a discovery or a rocket ride, which a senior won't ever deliver.

TGR: Rick Rule (Global Resource Investments) says there are three phases of the market: stealth, the wall of worry, and the mania. He says that we're in the wall of worry phase related to gold. Rule also says he thinks it's going to get to a mania, that this market is going to be a lot more selective in what it does in terms of juniors and seniors. What's your viewpoint on that?

RM: Unless the juniors come back through a discovery or through the seniors dipping into the juniors pool and buying, I would have to agree with Rick. In May of '06 we saw a peak in the mineral junior exploration company prices. All you had to do was say you found gold and you saw your stock running away on the up side.

Investors are now realizing that certain parts of the world aren't as friendly to their investment as others. So they have pulled back. It's just the education of the investor. There is a point where it gets carried away, and that's the mania stage where people forget about the risks that are out there and now I think people are more selective.

TGR: How does one begin to look at the junior markets and find one that's going to give you that rocket ride?

RM: That is what everybody is searching for, and if one had a formula that could pick every winner, you'd be a very wealthy person. I don't think there's a hard and fast rule here. You can get discoveries out of very unexpected quarters, and that's what creates the rocket ride. There's a lot of money being spent on exploration, and it is going to bear fruit but it is just difficult to predict when and where.

TGR: Would you recommend that individual investors invest in gold, which is currently about \$900?

RM: Yes, I believe that by the end of 2010, we'll be seeing \$2,000 gold, and before the gold cycle is out, it will go up and touch \$5,000, and that will be the end of the mania phase.

I don't believe that we're out of the woods on the financial problems, and the economy has quite a bit to shake off before it will start to look good. And there will be more people looking for answers where to put their money so they can protect it. Gold will start shining.

The annual production of gold expands the world supply by about 1% a year, whereas the money supply

has been expanding at better than 8% a year around the world, so gold is in short supply. And as we talked about at the beginning, the cost of producing an ounce of gold is going up, and it's going up rapidly while annual production is going down. It's harder to find gold; it's more expensive to produce gold; and it takes longer to build new mines, yet more people want to buy it.

TGR: Are there some gold companies that you are interested in that may see some of this bounce at the end of the summer?

RM: I have conflicts as I have large investments in a number of companies. One that's good is [Minera Andes Inc. \(TSX:MAI;OTCBB:MNEAF\)](#). They have what appears to be a very large copper discovery in northern Argentina. I like that. It's like many others down there, but it also has production, although it hasn't seen any cash flow from its partner yet. Production should be effectively doubled by the second quarter of next year.

TGR: How about some of the other companies you have in McEwen Capital? Can you make any comments on those?

RM: I like [Rubicon Minerals Corp. \(RBY:AMEX, RMX:TSX\)](#), which has recently reported some very interesting high grade gold results. They are the second largest landowner in the world's richest gold district, Red Lake, Ontario, Canada. As you know, this area is my favorite spot because this is where we discovered a fabulous gold deposit that powered Goldcorp's growth and produced fantastic returns for our shareholders. Goldcorp's recent \$1.5 billion takeover bid for Rubicon's neighbor, [Gold Eagle Mines \(GEA:TSX\)](#), dramatically highlights the big potential of the area. Rubicon appears to be at the early stage of making an important new discovery in Red Lake. It has a strong treasury in addition to large land holdings around a new mine and a exciting new gold discovery in Alaska and Nevada, respectively.

TGR: Can you make any comment about [Freegold Ventures \(TSX:ITF\)](#)?

RM: Some very good explorers with good experienced management. They market it well. They've got some interesting projects up in Alaska — one project I bid on myself, trying to joint-venture it. It had some very high-grade assay results, which they're going to be drilling this summer. And they have two other properties they're putting into production as well. It's a good team, and they have the investor very much at heart.

Unfortunately, our government has put so many restrictions in place that from the time you say you have enough mineral resource or reserves to justify a mine, you're three to five years away from generating any revenue. You have to permit it, build it, and start getting a cash flow.

I've met a number of Chinese mining people, and they say, "What's wrong with you people? When we find a deposit, we put into production within a year." That's the competition. We have introduced our too much regulation and at the very time when a lot of our manufacturing jobs have gone off shore. Natural resources are going to be one of the sectors that keeps North America afloat. We need to abbreviate the regulatory and permitting process. The government needs to make it easier to get business done while maintaining all the safeguards for protecting the natural ecosystem.

TGR: Well said. Of course, we have to ask about your own company, [U.S. Gold](#).

RM: We're exploring in Nevada and Mexico; we have a couple of projects there, with two or three resource estimates coming out this quarter. We have 1.7 million ounces in Nevada in the Cortez Trend, which is right next door to Barrick's Cortez Mine, which Barrick has stated is one of its most exciting exploration projects. This deposit has in excess of 35 million ounces of gold and it is next door. So, our drill program is to see if we can find something that looks like the next Cortez Hills deposit.

In Mexico we have about a million acres spread across three states. We have focused our drilling on the site of a historic mine where there is currently a little over a half million ounces outlined on that property by our 43-101 report, which is the Canadian standard and according to the SEC we call it mineralized

material. We have another resource estimate coming out this quarter on nearby property on which are quite encouraged by what we've been finding.

TGR: Great. Rob, thanks for your time. We really appreciate it.

Rob McEwen has been associated with the resource industry for 29 years. Currently Chairman and CEO of US Gold and Lexam Explorations, he was the founder and former Chairman and CEO of Goldcorp. Rob followed his father into the investment industry and developed a passion for gold. In 1990 he jumped into the mining industry, where he transformed Goldcorp from a collection of small companies into a mining powerhouse. At Goldcorp he grew the company from a market capitalization of \$50 million to approximately \$8 billion. During that time Goldcorp's shares achieved a 32% compound annual growth rate, making it one of the best performing gold companies in the world.

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