

# The Man Who Saw It Coming

Sounding the Subprime Alarm -- in 2005

By JASON DEAN in Beijing and PETER STEIN in Hong Kong

August 29, 2007; Page C2

(\*)

"Investors should sell all exposure to the American mortgage securities market," advised Greed & Fear, a weekly note to clients from stock strategist Christopher Wood.

Pretty conventional advice these days? Yes. But this warning from Mr. Wood was sounded in October 2005.

The collapse of prices for U.S. mortgage-backed securities has sent a jolt through global financial markets in recent weeks. Among the people who shouldn't have been surprised: those familiar with the writings of Mr. Wood, the stock strategist for Hong Kong-based brokerage CLSA Asia-Pacific Markets, majority-owned by French bank Cr dit Agricole.

In 2005, he was warning that U.S. mortgage debt was "where the credit risk lies in the American and global financial system."

*NICE ONE.*

*IT WAS EARLIER THIS YEAR I HEARD OF PEOPLE GETTING BORED BY THE ONEVENTFUL/UNPROBLEMATIC US HOUSING + CREDIT ISSUE HE'D BEEN TALKING ABOUT FOR OVER A YEAR - I'M SURE THEY AREN'T BORED NOW.*



Chris Wood

After urging investors to cut their exposure to securities related to U.S. mortgages in late 2005, he continued to warn about securitization through last year. In August, as the U.S. housing market was slowing, he warned that "the markets have yet to focus on the resulting inevitable credit problems. ... This credit aspect to the housing problem will come later in the cycle, and will provide the stress test of securitization."

Then, this January: "It is increasingly clear that the Achilles' heel of the U.S. housing market lies in the subprime mortgage area. This might seem a niche segment, but it is actually rather large and has potentially macro consequences." In late February, global stock markets first caught up with that idea. Worsening problems among subprime-mortgage lenders led to a sudden selloff on Wall Street that pushed the Dow Jones Industrial Average down 416 points.

*Now*

Mr. Wood's take on the current crisis isn't encouraging.

"In the credit world I think we've been in a bubble every bit as big as the one in technology in 2000 and in Japan in the 1980s," he says. The chief culprit, Mr. Wood believes, is securitization, which he thinks "has been basically running amok" in the U.S. in recent years. Securitization in the housing market, he says, has led investors to ignore legitimate financial risk by pretending that it is too spread-out to matter.

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Still, Mr. Wood doesn't think all bubbles are bad. Another one is brewing in the asset prices of Asia and other emerging markets, he believes, adding that it is still early in a cycle that will run for years.

While stock prices in Asia may continue to be volatile because of the U.S. credit-market and housing-market issues, in the long term "we're going to go into new bubble territory in these markets," he says. "In the big picture it's a buying opportunity."

From: Jim Walker (Dr.), CLSA  
Sent: 08/30/2007 6:09 AM  
To: Sales - All; Research - All; Economics Team  
Subject: Econs Wrap

*ANOTHER WHO HAS SEEN A LOT OF THIS COMING*



U.S. EQUITY MARKETS

\* Talk about headless chickens! US equity markets were up 2% overnight after their 2% fall the day before. There was no economic data out to give them guidance so presumably they just thought everything is bound to be OK. Doh!

\* Currency gyrations too! The yen went from Y114/\$1 to Y116/\$1 in a day. This doesn't signal the return of the carry trade, volatility is the death of it.

\* In the all-important debt markets mortgage backed securities (Markit's ABX indices) fell from depressed levels. All categories (AAA to BBB-) fell in price with A-rated paper falling more than 1% on the day. Asset-backed commercial paper interest rates remain at elevated levels of over 6%. The global credit contraction is underway, equity markets just haven't figured it out yet. Sell cyclicals, sell Asian financials.

*AND BOY?*

DR JIM

But buy gold As panic stricken central banks demonstrated so adequately last week, they have no answer to the problems they have created over the last five years but to debase their paper currencies even more. The yellow metal is the safest store of value we can all own.

# YELLOW METAL

CHRIS & JIM AGREE ON THIS ONE

## **GREED & FEAR** - CHRIS Wood

This growing evidence of slowing growth is also why it is wrong to be increasing equity weightings and reducing bond allocations as a result of applying Fed model methodology. In *GREED & fear's* view, the current environment of falling government bond yields and rising credit spreads is negative for equities since it is deflationary market action. The recent initial signs of a US dollar bounce is also a deflationary signal in the sense that it suggests speculators and borrowers are buying back borrowed dollars to repay debts. *GREED & fear's* guess is that the dollar strength will persist, including against the Asian currencies, until Fed chairman Ben **(\*)** Bernanke commits to aggressive easing. At that point, gold's time may well come.

### ✓ HIS 816 PENSION FUND PORTFOLIO

No change in the global portfolio for US-dollar-based, long-term global investors, such as pension funds, was made during the past quarter. The weighting in the Japan absolute-return portfolio was maintained at 20% and the weighting in the Asia ex-Japan absolute-return portfolio at 15%. A five-percentage-point weighting was retained in German physical property, as was the 15% weighting in Asian physical property (including Japan). Finally, the investments in gold and gold-mining stocks (10% and 15% of the portfolio) are maintained. A long-term bullish view is maintained on gold bullion with the price target by the end of this decade held at US\$3,700 per ounce.

A 5+ BAGGER

"GOLD PRICE TARGET BY END OF DECADE HELD AT US\$3,700 PER OUNCE"

### Recommended long-only asset allocation for US-dollar-based pension funds

Weight (%)	Investment type
20	Singapore government bonds
5	German physical property; commercial and residential
20	Japanese equities, weighted according to the Japan thematic portfolio
15	Asia ex-Japan equities, weighted according to the long-only thematic portfolio
15	Asian physical property, including Japan; commercial and residential
15	Unhedged gold-mining stocks
10	Gold bullion

25% IN GOLD.

Source: CLSA Asia-Pacific Markets

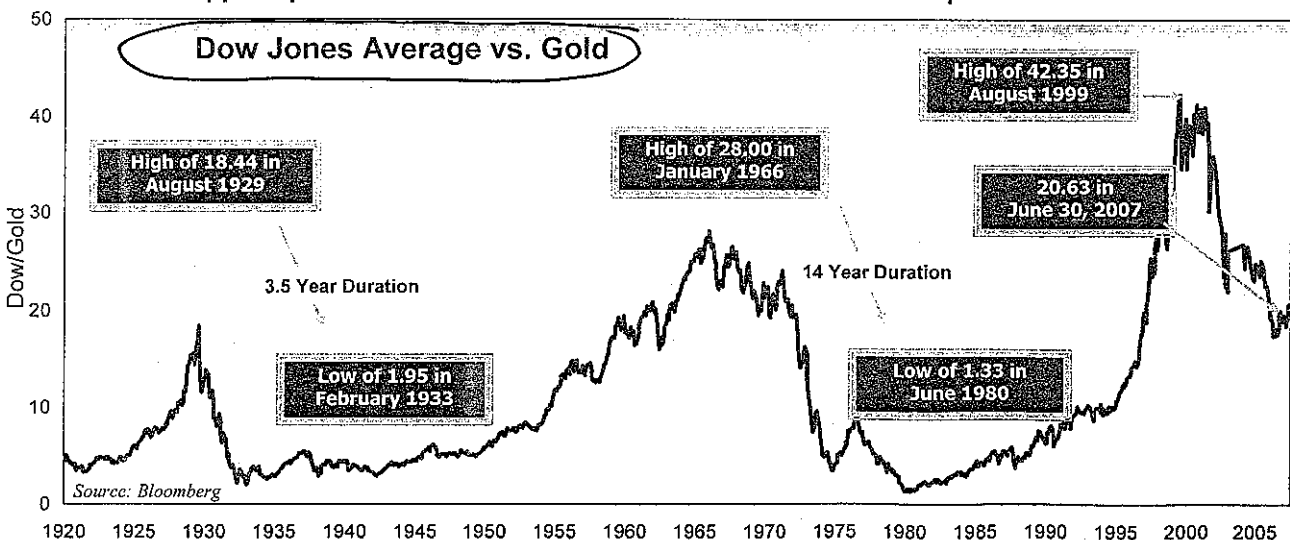
A FEW INTERESTING CHARTS FROM A PRESENTATION BY NEWMONT AT THIS YEAR'S DIGGERS + DEALERS MINING CONFERENCE IN KALGOORLIE (WESTERN AUSTRALIA) - ASK IF YOU'D LIKE THE FULL THING

## Gold Market

- Duration of Last Super Cycle Was 14 years (1966 - 1980)
- Base Metal Prices Peaked Before Gold/Oil

NEWMONT™

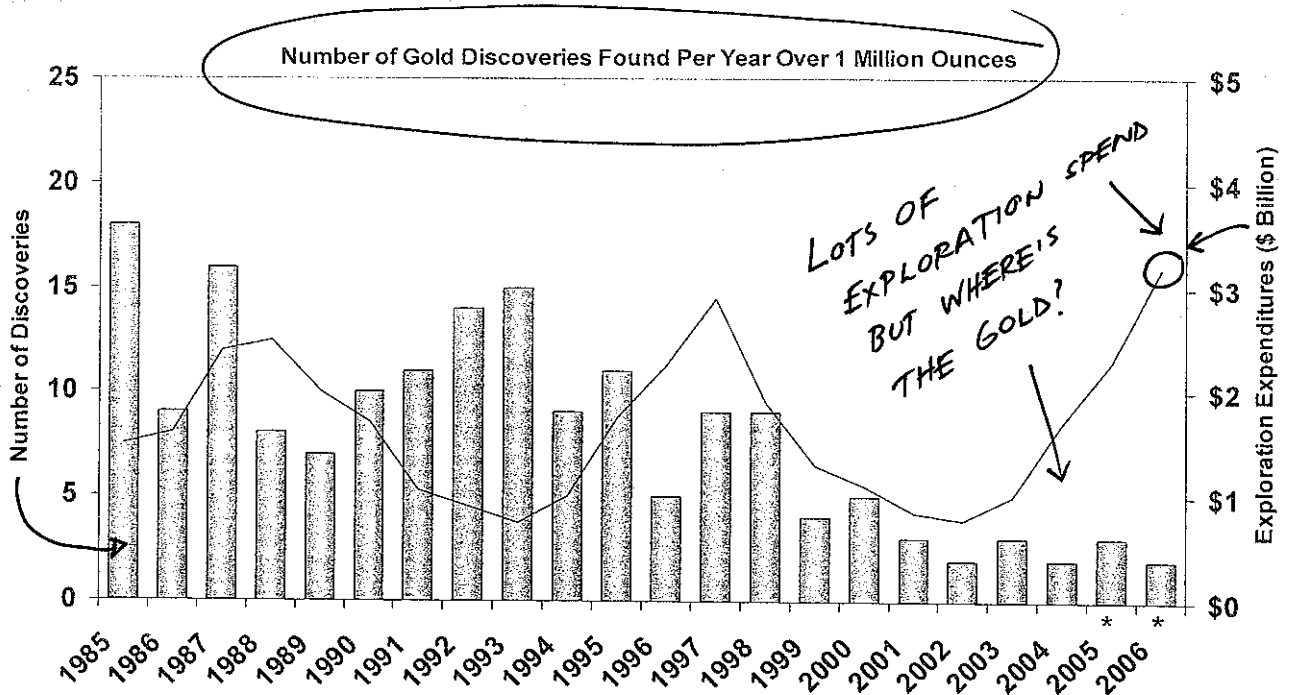
Copper April 1974 - Nickel Feb 1979 - Gold Jan 1980 - Oil April 1980



# WANING SUPPLY

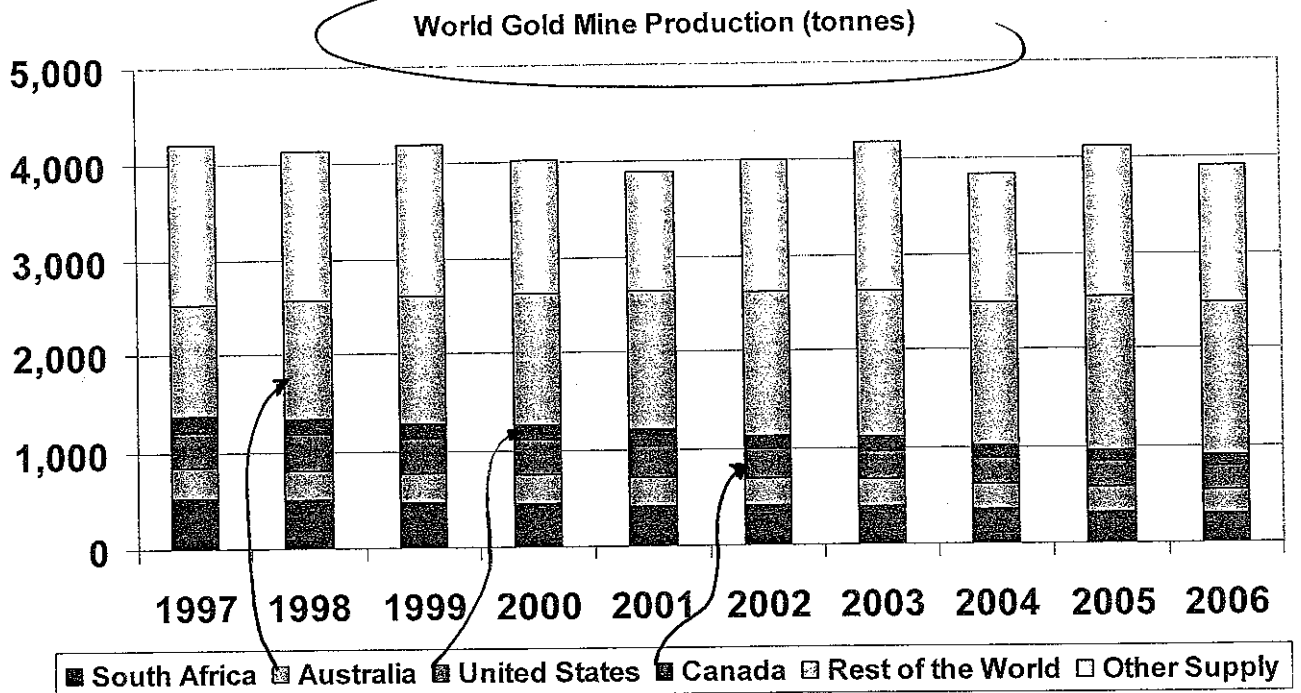
NOT MANY FINDS THESE DAYS

## Discovery Limits



EXISTING MINES - NO GROWTH

## Declining Mine Supply



AND EVEN IF YOU DO FIND IT ✓

9 MONTHS  
IN 1980'S



NOW 6+  
YEARS

**(\*)** *Permitting, Environmental, Political*

Discovery to Production – Increase Permitting Requirements:

Mine Permitting in (1980's)

Mine Permitting in (2006)

**(\*)** Permitting Time = 9 Months

- No Environmental or Social Baseline
- No State Permits
- Federal Environmental Assessment (maybe)
- Public Comment (limited, if any)
- No Legal Challenges

**(\*)** Permitting Time = 6+ Years

- Minimum One Year Environmental Baseline
- 3 to 5 State Permits
- Federal Environmental Impact Assessment (Required)
- Significant, Multiple Public Comment Periods
- 95% Probability of Legal Challenges

IN SUM, THE THEN & NOW FOR GOLD

*Back to the Future*

**Then**

**Now**

- Vietnam War
- Oil: \$2.20/bbl to \$50/bbl
- Falling US \$  
(50% Depreciation to Yen & Mark)
- Growing Current Account Deficits
- Inflation Took Off
- Gold: \$35/oz to \$850/oz (2,300%)

- Iraq/Al-Qaeda War
- Oil: \$12.00/bbl to \$??/bbl
- Falling US \$  
(45% Depreciation to Euro)
- Same but 100x (HA)
- Watch Out!
- Gold: \$250/oz to \$675/oz (170%)  
so far...

GOLD PLAYS ↗

*NOT MUCH*

Ticker	Mkt Cap (US\$m)	Performance (%)		PE (x)		P/CF (x)		Div yield (%)		EV/Ebitda (x)		EV (US\$m)	EV/Res Oz US\$	
		1W	3M	2007	2008	2007	2008	2007	2008	2007	2008	2007		
Barrick Gold	ABX CT	27,611	(3.3)	8.2	17.2	17.0	13.8	11.2	1.0	1.0	10.4	8.4	28,264	205
Newmont	NEM UN	18,868	2.4	5.4	43.3	26.1	17.7	11.6	1.0	1.0	9.8	7.7	20,328	207
Goldcorp	GG UN	16,545	0.3	1.3	37.3	27.2	18.6	14.7	0.8	0.8	14.2	11.6	16,294	1,087
AngloGold Ashanti	ANG SJ	10,697	(0.4)	(8.9)	24.5	12.5	9.8	6.6	1.7	2.9	9.0	8.4	13,706	141
Gold Fields	GFI SJ	9,768	1.8	(12.6)	19.9	14.1	11.4	6.7	2.3	3.4	8.0	8.5	10,639	147
Zijin Mining	2899 HK	9,357	12.2	59.3	32.0	28.4	11.4	22.2	1.7	1.9	15.3	13.9	9,643	779
Kinross Gold Corp	KGC UN	6,875	2.4	(7.0)	30.9	20.1	17.8	11.7	0.0	4.3	16.6	8.8	7,126	281
Newcrest Mining	NCM AU	6,691	(4.5)	12.8	29.0	23.0	13.0	11.1	0.2	0.2	12.8	10.7	7,670	240
Lihir Gold	LHG AU	4,928	0.0	2.9	38.7	22.5	19.6	14.2	0.0	0.0	20.5	13.1	4,690	239
Harmony Gold Mining	HAR SJ	3,644	(2.5)	(39.9)	20.7	11.3	10.3	6.0	1.0	2.9	8.2	7.7	4,031	67
Shandong Gold	600547 CI	2,736	10.2	170.0	98.3	69.9	64.5	53.8	0.7	2.0	47.1	36.0	2,766	1,077
Meridian Gold	MNG CT	2,683	8.2	11.5	28.6	24.2	18.9	17.5	0.0	0.0	12.5	9.9	2,418	547
IAMGOLD Corp	IAG US	1,987	0.0	0.0	29.2	21.2	13.6	10.4	0.7	0.7	12.2	8.2	2,016	499
Zhaojin Mining	1818 HK	1,325	0.6	(0.8)	24.7	18.2	15.2	13.6	1.2	1.6	9.9	7.8	1,075	319
Sinogold	SGX AU	866	8.1	0.3	-	21.9	139.0	13.6	0.0	0.0	75.5	11.2	882	384
Zhongjin Gold	600489 CI	759	20.3	163.5	111.7	75.7	41.1	25.0	0.5	0.6	21.7	12.0	-	402
Lingbao Gold	3330 HK	518	16.0	(4.9)	15.4	11.7	11.6	11.7	2.3	3.0	8.4	7.6	536	324
Equigold	EQU AU	364	0.0	16.7	19.3	10.6	12.0	7.1	3.3	4.7	8.3	5.2	315	161
Kingsgate	KCN AU	340	(3.6)	(18.3)	-	14.8	41.8	5.4	1.6	5.1	43.9	6.6	387	143
Resolute Mining	RSG AU	249	(7.7)	(5.7)	-	Na	20.0	Na	0.0	Na	11.4	Na	243	93
<b>Weighted Average</b>		<b>126,811</b>	<b>3.4</b>	<b>21.5</b>	<b>76.6</b>	<b>22.1</b>	<b>16.9</b>	<b>12.9</b>	<b>1.0</b>	<b>1.5</b>	<b>13.1</b>	<b>10.1</b>	<b>133,028</b>	<b>234</b>

