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Registration Effective August 27th and Now Operational

GOLDILOCKS SCENARIO WANES AS OUTWARD SHIFT OF "PHILLIPS CURVE"

- The August 4,000 job drop in payrolls casts some doubt on rates of GDP growth and the 4.6% unemployment rate. For some time the weightings or adjustments to the CPI called into doubt the 2% inflation trend. Now it appears fundamentals have asserted themselves so strongly in terms of poor housing, remodeling, appliance, auto or related consumer spending that the Feds can't massage the employment or perhaps GDP data to make them look good.
- The metals markets reacted with a vengeance to the expectation of ever more global monetary stimulus in the face of slow growth.
- Gold and silver rose over 4%, foreshadowing a massive surge in inflation expectations. Real interest rates could prove very negative indeed if inflation in fact surges and monetary authorities push nominal interest rates down. Nothing benefits gold, silver, base metals, real estate or other hard assets more than cheap money measured in terms of the size of the negative real rate.
- Nickel, lead and zinc each LOST over 10% last week while the big winners among base metals, copper and aluminum, fell just 4%-5%.
- Combined exchange inventories rose mildly for copper, lead and tin while steel scrap prices inched up for the second week in a row. Nickel inventories rose less than feared by just 1,806 tonnes while MUCH MORE OMINOUSLY aluminum rose by a large 40,134 tonnes in its third straight weekly rise and zinc inventories on the LME and Shanghai rose 4,313 tonnes in their second weekly rise.
- The question is whether the dramatic base metal collapse reflects the expectation of a dramatic global slowdown or that one is arriving. Further, we wonder whether investment fund managers are selling base metals owing to margin calls from their holdings of mortgage bonds or takeover stocks, or whether those selling money managers really think that metals sectors will slow.

REMEMBER THE OUTWARD SHIFTS OF THE "PHILLIPS CURVE"

After energy shocks #1 in 1973-74 and #2 in 1979-80 economic dialogue or textbooks contained something termed the "Phillips Curve," the tradeoff between unemployment and inflation. The large rises in energy costs prompted an "outward shift" of the Phillips Curve in which both inflation and unemployment simultaneously rose. "Stagflation" was another term for the phenomenon, which was a nemesis both to bonds and stocks.

During the Greenspan and Bernanke eras the markets perceived a sort of "economic perfection," or Goldilocks world. One thought was that the BTUs used per dollar of GDP fell so much that energy mattered less. Another was that since we sent our manufacturing to China and immigrant Latinos did the meanial and Asian Phds the real work in America, low wages permitted near zero inflation. Some others thought the policymakers were simply so good that they would prevent cycles. More recently investors thought that Chinese, Asian, Arab or Russian economic leadership was so good that their superior economic judgments would carry the day even if our fraudulent mortgage markets caused a bump in the road over here.

Now the Mexican president declared that his borders extend to wherever his people live, which means that the income taxes from here in Monmouth County, NJ should be paid in pesos and shipped south of the border. Reductions in carbon emissions to 25% or more below 1990 levels will levy a huge "tax" burden that inevitably will slow consumption as the world retools. How many American wives will simply drive up to Nucor's nearest mill to melt down their SUV ??

Gold and silver now have risen three straight weeks, and gold closed above $700 for just the second week ever other than May 15, 2007. The yellow metal is reacting to the global $0.5 trillion liquidity injection made in the past month or so, and we reiterate our August 5th upgrade of Barrick Gold to Overweight.

Things could get so lousy that the Feds simply can't fake good inflation, GDP and employment data any more. Yes more memory and ten times faster electronic devices create productivity gains, and enough "adjustments" to reflect productivity that we do not need negates much of the inflation we all know we pay out in insurance, college tuition, fuel, food or other daily needs.

Clearly the swing benefits gold. There is a chance that economic stimulus benefits base metals too. Moreover, the lack of a universal slowdown in base metals suggests that the world economy is pretty decent even before the stimulus takes hold.

GOLD AND SILVER

The 20% employment cut at Countrywide Financial suggests that many fewer loans will be offered in the coming year. State regulators will require pay stubs, work place visitation, tax returns, minimum down payments and maybe occasional lie detector tests. Use of outside mortgage brokers will decline. Fewer will admit to past, present or future ownership of "mortgage backed bonds."

Each week's new disclosures suggest the embedded fraud in the U.S. mortgage industry runs deeper. We are trying to track down allegations that Chinese mine safety, food or consumer product safety inspectors actually have been moonlighting as credit managers at major U.S. lenders. Maybe the improving climate in the Congo and Zambia has caused their key bureaucrats to emigrate into U.S. mortgage jobs as they lay down their weapons since corruption in central Africa has grown less fashionable.

The case for gold as a safe haven continues to grow, and the outlook for declining nominal AND REAL interest rates benefits gold. Our $650 per oz 2008 onwards gold price estimate feels too conservative. Gold's $27.80 and silver's $0.53 per oz price rise last week suggests the potential for some upwards acceleration. Gold may be the first metal to set a new all-time record since lead in July, nickel in May, zinc in December or copper in May 2006.

ALUMINUM INVENTORIES SURGE 40,000 TONNES ON LME

Aluminum prices now rest at their lowest levels since March 13, 2006 or 18 months ago. Some producers may suffer actual book losses at their higher cost alumina or smelting locations if these trends continue. We presume the investment fund managers selling aluminum contracts today expect either a 1 mmt inventory build or else they sold aluminum to cover margin calls from losses on other instruments or via reduced credit lines or else their clients withdrew funds from commodities sectors to invest more defensively.

Aluminum fell $0.052 to $1.082 per pound as inventories rose 40,134 tonnes on exchanges to 1.175 mmt. We do not believe it is meaningful to annualize the one week inventory spike into a 2.1 mmt annualized inventory build rate, and note that producer inventories have been falling.

COPPER INVENTORIES FELL

Copper prices fell $0.15 per pound to $3.26 as exchange inventories fell 5,045 tonnes to 220,137 tonnes. This is just 12,408 tonnes above the July 8th low point of copper inventories on exchanges this year, and certainly represents a below average summer buildup.

Codelco continues engineering studies to moving Chuquicamata underground sometime near one decade from now. It aspires to underground output levels matching the El Teniente mine, even though El Teniente mines "sideways" laterally into a large mountain ridge. Targeting El Teniente's volumes translates into a 200,000 tonne-plus output decline target. Several years ago Codelco began reporting the output of "Codelco Norte," which combines Chuqui, Radomiro Tomic and the future producers Gaby, Mansa Mina and others WHICH PREVENTS OUTSIDERS FROM MONITORING CHUQUIS OUTPUT DECLINES SHOULD THEY BE OCCURRING. The conservatism and intensity of the underground planning, combined with Codelco's tests of "autonomous" or manless open pit haul trucks, suggests to us that confidence in the pit wall stability at Chuqui is not very much.

NICKEL INVENTORIES RISE BUT LESS QUICKLY

The potential decline in nickel prices is much less now that their decline exceeds 50% from May peaks. Stainless surcharges in October for the mainstream type 304 (8% ni, 18% cr and 74% fe) will be $1.01 per pound or $2,020 per ton low than for July, which reflects their 60 day lag behind LME spot prices. Distributors might start buying more briskly in November or certainly after January 1.

The $1.45 per pound drop to $12.07 per pound leaves nickel above the $12.04 close four or $11.61 per pound close three weeks earlier. The 1,806 tonne weekly LME inventory rise is similar to the nine week trend of 16,566 or almost 1,800 tonnes weekly driven by three specific 3,000 tonne weekly gains. Inventory buildups should reverse when distributors buy normally.

LEAD INVENTORIES DROP AGAIN

Even though lead prices fell $0.15 to $1.33, inventories fell 900 tonnes to 24,475. The only times lead inventories have been this low in the past generation involved 16 specific weeks in the first-quarter of 1990 or the last few weeks of 1989. No fundamental weakness is evident even though high gasoline moderates global car sales.

ZINC INVENTORIES RISE

Zinc prices fell $0.16 to $1.26, well below the $2.10 peak last December, as Shanghai and LME inventories rose 4,313 tonnes to exceed 100,000 tonnes again.

STEEL SCRAP RISES

U.S.auto auction prices rose $25 per tonne for September, suggesting a further rise above $258.75 for “middle” grades like #1 heavy melt composites. Further, CVRD’s halt in iron ore shipments to a half dozen charcoal blast furnaces on environmental or human rights grounds could drive Midwestern delivered pig iron prices above $400, which gives clean grades of scrap further upward impetus.

URANIUM QUIET

Quotations stayed near $90 for the third straight week.

WOOD PRICES FALL AND OUTPUT CUTS TAKE HOLD

Last week the framing lumber composite fell $3 to $282 per 000 board feet, OSB fell $2 to $175 and plywood fell $11 to $357.50 per 000 sq feet. Lumber output fell to 298 from 314 mm board feet in the prior week, which reflects both a reasonable seasonal decline and cyclical drop owing to excess home inventories and reduced credit availability. Further, Louisiana-Pacific and Weyerhaeuser announced OSB output cuts in the past months too.

CHANGE IN THIS RESEARCH OPERATION

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Our investment rating system for securities recommendations is Overweight, Neutral Weight or Underweight. Overweight or Underweight recommendations are estimated to vary from the relative performance of the S&P 500 by more than 10% annually, and the intended time horizon is up to 24 months. Our securities research is intended for institutional investors that might buy up to 10% of a given company, and as such focuses more towards longer-term dynamics impacting the net present value of future cash flows rather than "day trading" sorts of near-term issues.

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Our policy is full disclosure of any advisory relationship or conflict going back three years. None currently exist.

Numerous prior investment banking relationships existed prior to three years history to the pre-1997 time frame under the employment of Donaldson, Lufkin and Jenrette or Oppenheimer & Co., Inc. Some of these we can recollect included 14 different gold mine valuations or sales for Barrick Gold, LAC Minerals (later acquired by Barrick), Addington Resources (gold assets in Montana acquired by Canyon Resources), Westworld Industries (Bolivian assets acquired by Battle Mountain Gold later acquired by Newmont Mining), Coeur d'Alene Mines, Crown Resources (acquired by Kinross Gold), Freeport-McMoRan Gold (acquired by Minorco later AngloGold later Queenstake Resources), FMC Gold (later renamed Meridian Gold) and others. Sole managed initial public offerings included Reliance Steel & Aluminum and Huntco. Lead-managed initial public offerings included American Steel & Wire (later acquired by Birmingham Steel) and lead-managed underwritings included Quanex. Co-managed underwritings included the IPO of Century Aluminum and offerings for AK Steel, Kaiser Aluminum, Agnico-Eagle Mines, Cameco and others. Asset sales or purchase advisories, fairness opinion or trusteeships were done for Thypin Steel (sold to Ryerson Tull), Cyclops Corp. (sold to Armco later sold to AK Steel), Allegheny Corp., Bethlehem Steel, the U.S. Dept. of Justice pursuant to the June 1984 merger of LTV and Republic Steel to sell the Gadsden, AL integrated flat-rolled mill, Cobre Copper, and others. Typically more than five investment banking assignments were evaluated, partly executed or "due diligenced" for any completed transaction. Some examples we can recall for which a prospectus was either drafted or partly drafted indicating much work included stock underwritings not completed for Wheeling-Pittsburgh Steel, Steel Dynamics, Atlas Corp., Webco, Sharon Steel, IPSCO, Co-Steel Inc., and others.

ANALYST UNIVERSE COVERAGE:

John C. Tumazos, CFA: Rio Tinto, Louisiana-Pacific, Nucor Corp., Newmont Mining, U.S. Steel, International Paper, BHP Billiton, MeadWestvaco Corp., Antofagasta PLC, Allegheny Technologies, Alcoa Inc., Inco Limited, Bowater, Inc., Temple-Inland, Barrick Gold, Abitibi-Consolidated, Weyerhaeuser Co., Alcan Inc., Smurfit-Stone Container, Plum Creek Timber, Worthington Industries, Goldcorp Inc., AngloGold Ashanti, Freeport McMoRan Copper & Gold, Novelis Inc., FNX Mining.

Dynatec is a company not continued in the research coverage of JTVIR, LLC that was previously included in the prior June 6, 2007 Prudential Equities Group universe owing to a pending takeover by Sherritt International.

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There is no intention to "balance" the number of Overweight or Underweight ratings, as instances of broad over- or under-performance among basic industrials may occur. JTVIR makes each investment judgment in a "bottoms up" manner based on the assets of each individual company.

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Additional risk factors as they pertain to the analyst's specific investment thesis can be found within the report.

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