

## Yesterday's Top Story: BMO digs deeper into silver as production and demand constrain physical market

Stronger demand and lackluster supply growth could propel silver to \$20/oz this year and next and maintain silver as an outperformer, BMO Capital Markets forecasts.

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RENO, NV -

BMO Capital Markets predicts silver will average \$20 per ounce this year and next, and is expected to decline to \$15/oz in 2012.

The analysts of BMO Research said they expect "stronger demand and lackluster supply growth to constrain the physical market and maintain silver as an outperformer for the next three years."

The sharp rebound in global and industrial activity this year "should spell good news for silver going forward," the analysts advised.

"BMO Research forecasts a relatively constrained physical supply/demand environment for silver and maintains the view that silver will outperform relative to other metals in the medium term," they added.

"Recent correction notwithstanding, the demand side has turned bullish and should be largely supportive of silver prices," the analysts said.

"Silver's heavy weighting towards the industrial side has convinced investors that it will significantly benefit from the sharper-than-expected global recovery," they noted. "Tightening physical fundamentals are projected to play an increasingly significant role in setting silver prices."

The analysts asserted that mine site development strengthens the argument that silver markets will be "quite tight moving into 2010."

"The sector is projected to operate near capacity, which is consistent with the US\$18-20/oz marginal cost of production," they forecast. However, the largest sources of secondary mined silver, zinc, lead and copper projects have either cutback or suspended production due to hefty inventories, which means "by-product silver supply growth will be somewhat limited for the next two years."

Meanwhile, silver from gold production will increase 3%, but since it only represents 10% of total mine supply, the contribution of by-product silver will be only modest, according to BMO.

The analysts predicted that total primary and secondary silver production is projected to increase 13% annually through 2015 to 243 million ounces and 245 million ounces, respectively.

Based on 2010 estimates, BMO finds BHP to be the largest silver producer based on by-product production while Mexican silver miner Fresnillo is the largest primary silver producer followed by Coeur d'Alene Mines, Pan American Silver, and Peruvian silver miner Hochschild.

By 2015, BMO analysts predict Fresnillo will surpass BHP as the largest silver producer, as significant new mine production growth is projected to elevate Vancouver's Pan American Silver to the second largest primary silver producer.

Barrick's Pascua Lama Project is expected to become the world's largest silver mine by 2015, while Fresnillo would realize 50 million ounces of silver annually from the Fresnillo District in Mexico.

Silver Standard's San Luis project is expected to become the highest grade underground silver producer.

Currently, Fresnillo is the lowest-cost primary silver producer. However, by 2015 BMO projects that junior producers Orko Silver and MAG Silver will join Fresnillo as the lowest cost primary silver producers.

In their research, BMO Capital Markets found Silver Wheaton and Silver Standard have "very large reserve lives, followed by junior developer BCM [Bear Creek Mining]." Meanwhile, Silver Standard, Pan American Silver, Fresnillo and Silvercorp Metals "have large silver resources to support future reserve conversion."

## 2010 WILL CONTINUE SILVER M&A

BMO Research expects more consolidation in the silver sector this year. Central themes could include consolidation of mine and project ownership, and the acquisitions of junior silver developers by senior and intermediate producers to maintain existing production rates or to achieve growth.

For instance, BMO predicts that Orko Silver could be acquired by JV partner Pan American Silver in an effort to consolidate Durango, Mexico's Las Preciosa's potential production and lower cash costs.

Meanwhile, Hochschild has invested \$360 million in two junior developers who are transitioning to producers this year. Hochschild has indicated its intentions to increase ownership of Canada's Lake Shore Gold. BMO anticipates that a comparable strategy will evolve with Gold Resources, which is developing the El Aquila mine in Mexico.

BMO considers MAG Silver and Bear Creek Mining to be prime candidates for acquisition.