January 1st, 2008
Volume 6, Number 1A

Geoshares Newsletter

A warning about junior markets and buying stocks,

It's a time to be very cautious and selective.

When in doubt, stay in cash.

Don't be afraid to take profits. They may not stay around long.

Cut losses fast! Don't hang on hoping for better days.

Question everything. Take nothing for granted.

Preserve your capital. Once lost, it's very hard to regain.

Welcoming in 2008…... with fingers crossed.

Writing this newsletter has become increasingly difficult. Hopefully the following notes may partially explain why.

To write effectively, you have to believe in your subject. In this case, the subject is speculative investing in mining stocks. Unfortunately, events of the past year have tempered my enthusiasm. It's not the volatility which bothers me. That's always been around and part of the attraction. It's the overall health of the market which most concerns me and I don't see any sudden change in the near future.

Let's put it this way. If someone new to investing asked if they should buy some junior mining stocks, I'd strongly suggest they stay far away and save their money and time. The deck is now so stacked against them and the dice so loaded they have little chance of winning. This is what I've said to my own kids (now in their 30's and 40's) and it's what I've said to a few subscribers of this newsletter. It's far better to focus your efforts on your job or profession and concentrate on building your business or career than fiddle around risking hard earned money on doubtful companies hustling a story.

A word about cycles….

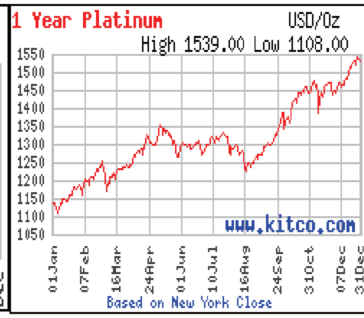
We all know markets run in cycles. Usually they are gradual and roll in and out like ocean swells often unnoticed. Occasionally we get big ones like the tech cycle which everyone notices and many jump into. As stocks rise, more money enters the market pushing prices even higher. People with no knowledge whatsoever about technological devices start throwing around buzz words and sounding like experts. In reality they are only parroting what they've been told but who cares - their stocks are going up and money is being made.

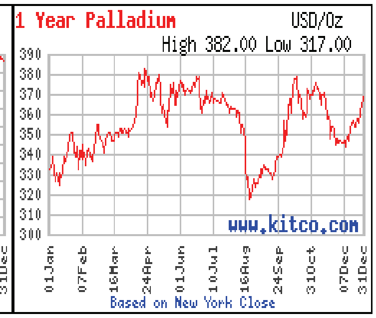
These cycles are not limited only to stock markets. They can and do occur in all types of markets including real estate, antiques and art, but they all have one thing in common. Eventually they end and the higher the rise, the greater the eventual fall.

As we all know, the tech cycle (bubble) collapsed. In the aftermath, we learned about some of what had transpired. For example, we learned of one analyst with a bank-owned brokerage firm who was paid an incredible $20 million to write bogus reports about the splendors of Worldcom. The objective was to keep the price up while the bank attempted to dump their heavy position. Talk about a conflict of interest and we learned about many others. Remember the (*continued on Page 4*)

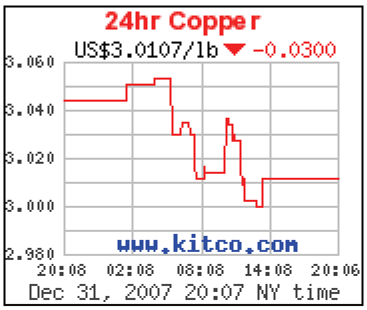
Metal Prices and Inventories

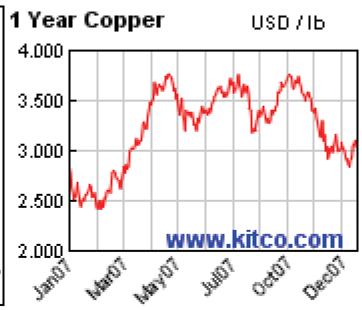
Spot Prices, Monday at close, **December 31st……. (Prices in brackets are as of last issue, 2 weeks prior)**
Gold— $833.30 ($794.40) Silver— $14.77 ($14.34) Platinum— $1528.00 ($1455.00) Palladium— $368.00 ($346.00)

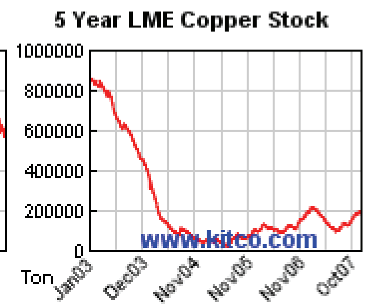


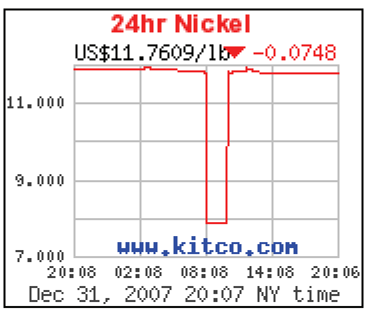


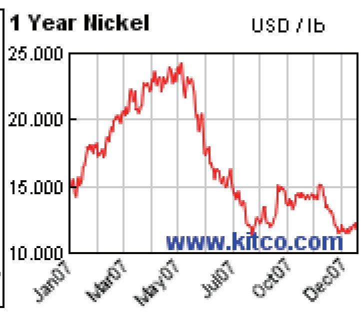
Price **Price** **Price** **Inventory**

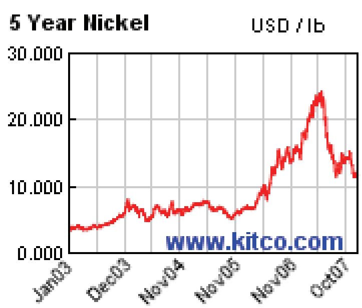


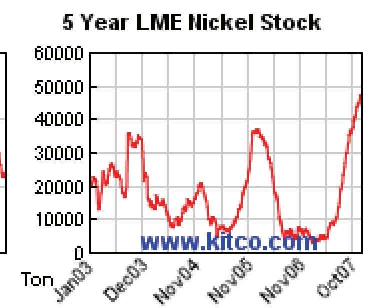


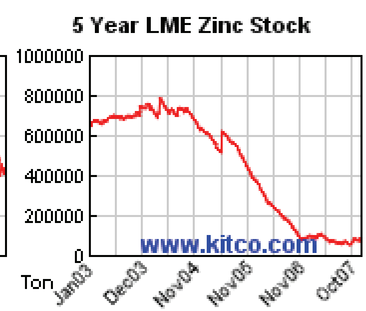


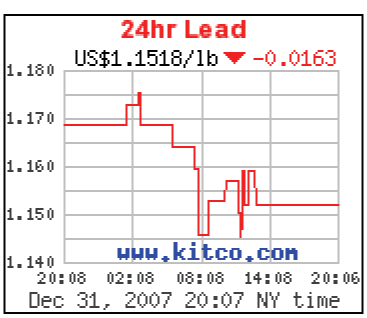


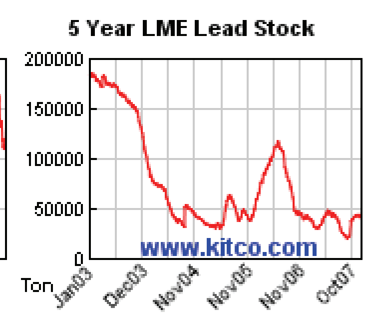












The Markets

The year ended with both the TSE Composite index and the TSX venture exchange showing signs of an upturn. Unfortunately, other markets including the Dow Jones industrial index shown at bottom right, had resumed a downward trend. However, all markets were trading in light holiday volume which tends to mask the their true intentions. It will take the first couple weeks of January with markets back to normal before we get a sense of their direction.

On the previous page, we show metal markets. What's interesting is comparing 1 year and 5 year charts of the 4 base metals shown. It's pretty obvious that all 4 metals have backed well away from their highs. That's not to say prices are now low - by historical standards they are still very high - but they are all past their peak and heading downward. Where these metals will base is anyone's guess but the charts may offer a few clues.

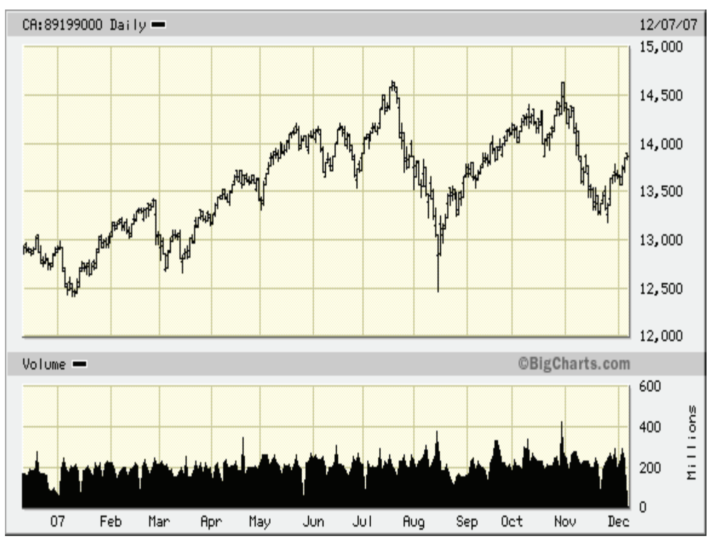
Copper inventories remain low as indicated on the 5 year LME chart. While copper is well down from it's $3.75 high, it appears to be showing support around $3.00 per pound.

Nickel is another story so far as their 5 year LME chart is concerned. LME nickel inventories are now at 5 year highs. On that basis, it's reasonable to conclude nickel prices will continue falling.

Countering this argument are both lead and zinc with 5 year LME inventories still extremely low. Their price levels may indicate other factors at work such as Chinese production which is by-passing LME warehouses. Another explanation may be that speculators have been leaving the market due to the general liquidity crisis.

Meanwhile, both gold and platinum have been standouts during this past year. However, these charts are in $US dollars which have dropped badly in the past year. Gold prices viewed in $CA or the Euro don't look quite so attractive and it's a similar story for base metals too.

Consequently, the real story behind metals this past year has been the depreciating American dollar. Because of it's weakness, we may see metal prices stronger than expected well into the future. That means inflationary pressures for America which makes cutting interest rates difficult. Regardless, I'm betting their interest rates will continue lower. Talk about a rock and hard place.



General Notes

(Continued from first page)

auditing firms who had their knuckles rapped for helping to inflate balance sheets. One of the world's largest eventually collapsed. Well it's happening again.

Lots of money - easy credit

Normally an event like the tech bubble collapse would have chilled markets for many years but not this time. The reason was cheap money and lots of it. In part, this cheap money was made available by the American Federal Reserve to help support markets which it was feared might collapse. The results, however, were perhaps a bit different than expected. Stock markets were kept afloat but it also spawned what became a great housing market bubble. It was great while it lasted. It finally got to the point where if you could breathe, you qualified for a big home loan - sometimes for as much as 107% of appraised house value - the appraisal often a loose and generous number.

Naturally with terms this easy, real estate sales boomed and the consequent demand raised prices. In many areas, house prices doubled within just a few years. Suddenly homeowners had a brand new bunch of equity. With banks ready to make cheap loans based on that equity, many decided the wise move was to borrow and play the market. At about this same time, the commodity story was becoming well known so many jumped into it just as others a few years before jumped into the tech and internet story. The result was an unprecedented boom in mining stocks.

The problem with booms...

All booms have a few things in common. On the way up, they lead to eventual excesses, which in turn eventually lead to a bust. The mining boom has been no exception.

Companies which had a hard time placing $500,000 in 2001 were easily doing placements for $5 million by 2005. Money flowed like water over a dam. Some of this money went into worthwhile exploration but a lot also went into enhanced promotion and fancy wine. What went into Hy's Steak House in Toronto will never be known but I doubt the amount was small. However, the biggest beneficiaries of this new largesse were probably the financial engineers who cobbled together a number of lucrative merger deals. When the smoke and dust settled, a number of companies had new names, management and a few inside shareholders had made serious money, but little else really changed. None of the revised companies was likely to produce a pound more of new metal than before and many shareholders lost equity by share dilution.

Meanwhile many excesses that occurred in the later days of the tech boom are now occurring with the mining boom. Lets consider just a couple.

Above is the chart for Southwestern Resources (SWG-V). As you can see the stock suffered a dramatic drop last August. So what happened to cause the drop? Well it appears we have another case of Bre-X type salting but amazingly, not much has been done about it nor is there much interest. The RCMP is supposedly looking into allegations that chief executive officer John Patterson was responsible but who knows? Under the circumstances one would think that regulators and other officials would be all over the situation. Instead, "*Southwestern Resources Corp. has granted options to buy 3,617,000 shares to directors, officers and other key personnel stock options, including options to purchase 2,425,000 common shares*

General Notes

shares to insiders, exercisable on or before Dec. 10, 2012, at an exercise price of 65 cents per share. The options will vest 25 per cent, six months from the date of grant, 25 per cent, 12 months from the date of grant and the remaining 50 per cent, 24 months from the date of grant.."

Consequently, it appears new management isn't crying over spilt milk. They're loading up with cheap options while the going is good. Considering the company's bets in South America, their timing appears excellent. Unlike the cash paying retail investor, they can't lose.

Another situation which deeply troubled me in 07 was placements made by Macdonald Mines (V:BMK). Normally placements are made within a set of rules and guidelines. Depending upon share price, the maximum allowable discount has always been 25%. At times I've seen trading obviously designed to drop a share price so a cheap placement could be announced to fall within the 25% range. However, until MacDonald, I've never seen that 25% rule tossed aside.

Above is the chart for Macdonald Mines. Lets look at what happened. With the stock trading as high as 40 million shares a day between 85 cents and a $1, the company announced: *"IBK Capital Corp. acting as agent, for gross proceeds of $10-million, such offering to be completed through the sale of 25 million units of the company. A total of 15,625,000 units of the company will be sold on a "hard dollar" basis at a price of 40 cents per hard unit, for gross proceeds of $6.25-million. A further 9,375,000 units of the company will be sold on a flow-through basis at price of 40 cents per flow-through unit, for gross proceeds of $3.75-million. Each hard unit will comprise one common share and one common share purchase warrant. Each flow-through unit will comprise one flow-through common share and one-half of one non-flow-through common share purchase warrant."*

In reality, the placement was already sold to Sheldon Inwentash, chairman and chief executive officer of Pinetree Capital Ltd., Robert McEwen, chairman and chief executive officer of US Gold Corp., Pierre Lassonde, chairman of Franco-Nevada Corp., and Randall Oliphant, chairman of Western Gold Fields Inc.

There was a little ruckus raised by a few shareholders but once the hype machine went into gear, they were soon silenced. A couple "respectable" newsletters endorsed the deal after supposedly hearing "in confidence" the details behind it. It was even turned into a supposed positive for the share price which actually rose temporarily.

That incident more than anything else made me realize just how absurd the market had become. Not being a shareholder I was not personally effected yet indirectly I knew I was. It raised the question, if companies can get away with this amount of favoritism, what chance has the retail investor who is paying cash on the barrel head? The next question had to be, is it even worth playing this game?

With the above in mind other questions arose. For example, I am now writing Geoshares. Many readers are new to the market. Is it right to advocate mining stocks to these people if you personally believe the market has become sick? If I tell my own kids to avoid the market, is it right to suggest stocks to others?

I'm not sure what the right answer is to these questions. What I do know is these thoughts should be spelled out for readers to see and consider. I really do believe the market has become sick - too many lies and too many liars telling them for too long. Hell even the banks don't trust each other any more. What a mess.

Where we stand.

I believe we are living in very dangerous times. I suppose that can be said of almost any time in history but in particular, right now, it's very true. We have not seen a truly severe market correction in many years. By a severe market correction I'm referring to one which sees a drop of 10 or 15 or 20% or more within one day. Many people believe that can't happen anymore. I believe they are wrong. That's not to say it will happen, but that it could happen.

If we did have a serious market correction, what would happen to the junior mining market? We've already seen that when the big boards in Toronto and New York go down, the drop is magnified in the junior market index. Therefore, imagine what would happen if we saw a truly serious market correction on those big boards. I believe junior markets would be devastated.

With this in mind, I therefore suggest anyone playing junior markets should only be playing with money they can afford to lose at least 50% of. I know such warnings are often given but usually only by those wishing to cover their ads. In my case, at this time, I'm deadly serious about it. This truly is a time for real caution.

Notes from subscribers

From time to time I receive notes from subscribers. Sometimes I receive a lot of them. Over the past while, I've come to know some subscribers quite well. Often they ask questions and I attempt to answer as best I can. In some cases they have sent pictures of their family and in time I've come to know quite a bit about their lives.

Some of these people have a lot of money committed to the stock market. Going further, some have committed large amounts of money to just one or two stocks. While not knowing their overall financial position, I get the feeling they are way over- exposed and taking severe risks. To be blunt, it's my concern about their risk and exposure to a market turn down or a bad stock call that scares the hell out of me. It's what has prompted this issue.

Money can be easily lost. It can happen while running your own business, making a bad loan to a friend, or any other number of ways. That's life. It's unfortunate but it's to be expected. Not everything in life is predictable.

Losing money in the market is something else. As an investor, you control the money up to the point at which you invest. After you have invested, the use and control of your money is gone. You have given it to others. That's something to think about when you buy any stock. It's something to really think about when buying an over-priced, over-hyped penny mining stock. If you decide to do it, don't compound the possible error by putting all your eggs in one basket. That is just plain nuts so be aware and spread the risk.

The Next Issue, etc

This issue is being labeled 1A. Within a week I'll send the second half. We can call that 1B. It will contain some meat about individual stocks and situations of interest.

This issue has just one purpose. It's to warn readers to be careful. We've all just come off a holiday. It's a good time to rethink what we are doing and where we are going. Markets will return in earnest next week. There are some interesting situations on the horizon and I like writing about them.

But I'll be damned if I want to see someone lose a bundle over anything I've written. Therefore, question everything you read. That includes what comes from Geoshares.
We may be honest and can't be bought but we aren't infallible…. and that's a fact.

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