

**prospector asset management**

1415 Sherman Ave. #504  
Evanston, IL 60201

Phone: (847) 733-8400  
Fax: (847) 733-8958  
E-mail: lkaplan@prospectorasset.com

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For markets of June 1<sup>st</sup>

INDICATIVE LEASE RATES  
Based upon 30 day maturities

CLOSES

JUNE GOLD	\$394.90
JULY SILVER	\$ 6.11
JULY PLATINUM	\$829.20
JUNE PALLADIUM	\$259.45

GOLD	.00/.50%
SILVER	.50/2.00%
PLAT	1.00/4.00%

**MARKET COMMENTARY**

**GENERAL COMMENTS:**

**Taking their cues from the USD in foreign exchange markets, along with a goodly dose of fear and trepidation from geopolitical events, the precious metals were rather sharply higher last week, as the USD fell by 1.7%.** The gold market managed a steady rise to close \$9 higher, apparently near the top of its recent trading range. Silver, now enslaved to the movements of other markets, rose by 23 cents. As recent fears of the possible slowdown in demand for metals by China subsided somewhat in the marketplace, platinum and palladium also enjoyed rather sharp rallies, up some \$12.00 for the former, and \$8.45 for the latter.

While many analysts in the industry discuss the forecasts for gold in terms of the fundamental supply/demand considerations, the worsening geopolitical terrorism, and perhaps the prospects for oncoming inflation in the United States, **the truth is that the gold market is, and has been, a negatively correlated proxy for the Dollar.** A recent report by RBC Capital Markets disclosed that the correlation between these two was -.95 for the three years between March 2001 and 2004. It is most evident by such research that **the overwhelming driver for the price of gold is the value of the Dollar, and little else.** Even though global jewelry demand has fallen by some 20% over the recent years, even though many gold producers have been aggressively repurchasing previously sold forward positions, even though global terrorism has escalated, even though crude oil is now at 20+ year highs, these considerations have had less importance to determining the gold price than one might imagine.

Perhaps it is the case that both gold and the USD respond to the same stimuli in opposite directions, but it is difficult to convincingly make that case when one considers that fundamental considerations in the gold market SHOULD have created more of a disconnect with the value of the Dollar. While it is clear that terrorist acts, or elementary macroeconomic situations such as the huge bulging twin deficits of the USA, tend to affect both the gold market and the USD similarly, it seems that considerations endemic strictly to the gold market SHOULD have created more of a disparity between the two. To my mind, this relationship portrays just the first few years of the recent secular bull market in gold. The continuation of the bull is going to be conditioned upon the

fact that one day; perhaps months or years from now, gold must start rising in value against all, or most, currencies. **But for now, gold investors/traders are simply foreign exchange traders in disguise.**

**This commentary has repeatedly commented that the markets are now about perception than reality, more about the psychology of the markets rather than fact.** Over the past few weeks, the financial markets have become less fearful of both a forced economic slowdown in China and the fear that the Federal Reserve will aggressively raise interest rates. As such, both the precious metals and industrial metals have rebounded sharply. It seems the pendulum has swung from one extreme to the other in rather rapid and volatile fashion, as yesterday's fears become today's forgotten emotions. The truth is probably in the middle.

Markets are more about expectations than about facts. As an example, I have one client who was recently lamenting the rise in the USD saying that it was totally impossible as this currency was in terrible shape. With the governmental deficits rising, with inflation imminent, with the gun barrel of terrorism pointed directly at the head of the USA, how is it possible that the USD could rise? **The answer is easy, in that the market KNOWS all of these facts, discounts them, and subsequent price movements are due to the CHANGE in psychology, not a change in the underlying facts.** This is an important lesson for investors/traders who sometimes stubbornly refuse to either enter or exit a position based strictly and solely upon their interpretation of the facts. They are looking in the wrong place.

In an article published by Mineweb.com, Mr. Jeff Christian of the CPM Group, dashed the hopes of many gold bulls by stating, "a price over \$400 is not sustainable in the long run...the average long-term clearing price of gold is between \$320 and \$380". He did concede, however, that prices over \$400 could prevail from time to time but that over a 4-5 year period of time fundamental considerations would reassert themselves and drag the price back into the price ranges he indicated. Naturally, he strongly recommends that gold producers once again begin to hedge their production. My view is different, in that I still see more upside to the gold market, but perhaps not right away. But Mr. Christian and I share one view, in that it seems quite prudent for gold producers to begin some hedging, at current levels, because no one really knows what the future holds. There exists a HUGE difference between the imprudent and aggressive hedging strategies utilized by some gold miners in years past, and careful and targeted hedging which would protect current profit margins.

Barclays Capital, the investment banking division of the same named bank, has purchased the "fixing" seat in gold, left vacant by the departure of Rothschild's some weeks ago. The price of the seat was rumored to be \$1 Million British Pounds. The fix is no longer conducted face to face, but is now done by phone.

The passage of the new tax bill in Washington would have considerable import to the precious metals markets as it might change the tax rate on "gold, silver, platinum, and palladium coin or bullion". Presently, these commodities are considered "collectibles", and as such, are taxed at the highest possible rates. If the current bill is passed by our administration, the precious metals would begin to be taxed similarly to the sales of stocks and bonds. A level playing field would be created and some investors who previously shunned the precious metals may begin to take a second look. This change in the law would also have a profound effect on any Exchange Traded Fund dealing in gold, and make its success in the USA a lot more likely.

As mentioned last week, the Chicago Board of Trade was making noises about competing directly, through electronic trading, against the Comex for its precious metals business. As expected, Comex has answered immediately by extending its hours for its electronic markets. These markets will now open at 2:00 New York time, instead of 3:15. This is a good beginning but that exchange MUST update its computer system to allow stop orders, which currently are not allowed.

Individual investors in Beijing and Shenzhen will now be able to buy and sell gold bullion through the China Merchants Bank. Price levels will be set by the London Bullion Market and the Shanghai Gold Exchange. Heretofore, individuals had no immediate access to the market as they were unable to trade on either exchange. The liberalization of the gold market continues in China, and many analysts retain great hopes that this nation will become a major demand center. Frankly, in my opinion, I am surprised that the Chinese government has acted as quickly as it has proceeding with the liberalization. This is nothing but wonderful for the gold market but we will have to wait and see how things develop.

And yet another Central Bank wants to sell gold. As part of the newly resigned and extended Washington Accord, the Dutch Central Bank announced that it will be selling 100 tons of gold over the next 5 years, to scale back its reserves to 612 tons, now having sold or committed 1100 tons since 1992.

After a rather shaky start, it would appear the newly reorganized Exchange Traded Fund dealing in gold, titled Gold Bullion Securities in London, has begun to take off. While most of its clientele is admittedly institutional, they have accumulated 52 tons of gold, worth \$640 million USD. Daily volume now averages 575,000 shares, worth some \$23 million USD. The managing director, Mr. Simon Village, now is looking to take it to major markets in Europe and perhaps eventually Asia. Although things are going better for this fund, I remain distinctly unimpressed. The World Gold Council would certainly have been better served promoting already existent and efficient markets rather than to try to re-invent the wheel.

Japanese gold imports rose 133% in April, measured year on year, but the total of 6.8 tons still falls considerably short of significant. The lower price of gold and the improving Japanese economy probably encouraged more jewelry and industrial off take, but we are still far removed from Japan becoming any important demand center.

With the price of silver being quite strong of late, producers are pushing their limits to take maximum advantage. Polimetal, the largest silver producer in Russia increased their production by 80% to 156.6 tons in the first quarter of the year. This has been the story of late, with Mexico, Peru and others clamoring to come to the market with as much metal as they can produce.

On to the Commitment of Traders reports, as of May 25<sup>th</sup>, both futures and options:

GOLD			
Long Speculative	Short Speculative	Long Commercial	Short Commercial
84,464	46,280	137,096	208,046
+960	-2,967	-17,980	-17,253
	Short Small Spec	Long Small Spec	
	65,821	33,055	
	-148	+3,053	

During the reporting period, gold was up some \$12.50 as open interest declined sharply, by almost 36,000 contracts. On its face, this is a classical bearish signal, as open interest should not be falling as prices rise. The commercials traded contracts between them, indicating to me that the long commercials were taking delivery of physical gold, as the short commercials were delivering it, thereby covering their short positions, for a net position of about zero. The ratio of spec longs to spec shorts is now under 2 to 1, down SHARPLY from a high of 7.5 to 1. I also find it most amusing to note that the market rallied sharply just after the small speculators were adding to their positions. They never seem to be right.

Overall, I see gold here as being fully priced, or perhaps a bit overpriced. In my view, gold is still in a trading range between the mid \$370's and perhaps \$400 on the upside, give or take a few Dollars. But all depends on the USD. Look for recommendations below.

## SILVER

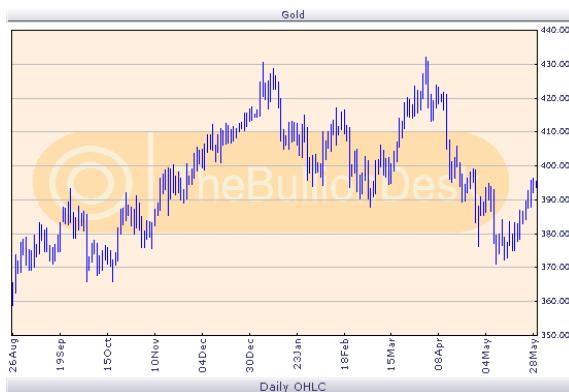
Long Speculative	Short Speculative	Long Commercial	Short Commercial
35,019	8,018	20,712	78,825
-1,084	+347	+77	-1,357
Small Long Spec +955		Small Short Spec +958	

Even though silver prices were up some 40 cents during the relevant period, there was little to no changes in the ownership of contracts on the exchange. **This goes a long way to explain just how thin this market can be at present** and how relatively small orders can move the market in a most exaggerated fashion. Commercials were net buyers, reflecting some demand from the physical market, a minor bullish sign.

My view of silver is that, like gold, it is probably overdone at current levels. There is very heavy technical resistance at the \$6.25 to \$6.30 level basis the July contract and I would expect that to repel any advance. At these levels, I would not want to be long. Recommendations will follow.

## GOLD RECOMMENDATIONS:

**EXPECTED TRADING RANGE: \$382 to \$396**



**(positions and recommendations are available to clients and subscribers only)**

## SILVER RECOMMENDATIONS:

**Expected trading range \$5.75 to \$6.25**

**(positions and recommendations are available to clients and subscribers only)**



## PLATINUM RECOMMENDATIONS:

**Expected trading range \$800 to \$840**

**(positions and recommendations are available to clients and subscribers only)**

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- \*Brokerage of commodity futures and commodity options
- \*Managed and directed speculative accounts in commodity futures and options\*
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- \*Consulting services
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