

Charles Oliver: Gold Headed to \$2,000 in Two Years

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Sprott Asset Management's Charles Oliver not only makes some bold predictions in this exclusive interview with The Gold Report, he backs them up. "I expect gold to be at \$2,000 roughly two years from today. . .if I'm wrong I'll shave the hair off my head," Oliver says. As an unwavering believer in the yellow metal, Oliver is well positioned as co-manager of several Sprott investment funds, some of which hold bullion. One of those—Sprott's Gold and Precious Minerals Fund—climbed 114% in 2009, and claimed the 2010 Lipper Fund Award for Best Fund Over One Year in the precious metals category. Oliver shares some of the secrets of his success in this one-on-one interview.

The Gold Report: What's your view on the European bailout?

Charles Oliver: The big problem that's going on is that there's too much leverage, too much debt, and people spending beyond their means. We had the financial crisis in 2008; the banks were bailed out by the governments, and now we see that the governments are in trouble because they've been spending too much and not living within their means. I really don't like the idea of bailing out everybody who breaks the rules. In the case of Greece, as part of the European Union, it was supposed to have a deficit that was less than 3% of its GDP, as part of the rules for getting in. Its deficit is now north of 13%, and it looks like it's going to get bailed out. One of the big problems with bailouts is that other countries see that and say, "You know what? We can be irresponsible, we can keep on spending, and, if we get into trouble, somebody else is going to come and bail us out." I really have some concern about the moral hazards that these bailouts have toward future spending and the way the countries go about their business.

TGR: How would you solve the problem?

CO: You ultimately have to cut back on your spending; you have to increase taxes. There is going to be pain and suffering. The Germans have been quite aggressive in telling the Greeks they don't want to bail them out. In Germany, people retire at the age of 65, and, in Greece, my understanding is people retire at 53. The German people really get incensed when they think that they're going to bail out somebody so they can retire at the age of 53 while they're still working at 65.

TGR: Do you think the euro will survive?

CO: I think the euro survives; I was very skeptical when it first came into being because it's very tough to have a whole different collection of countries living under one set of rules. Having said that, I think they've been very successful over the last decade. Some principles were put in place for the euro, like running a deficit that is less than 3% of GDP. When people drafted that rule, there was a reason, and the reason was that if you have a deficit below 3% of GDP, you are going to be able to pay back your debts. Things like that make the euro a very good currency to have. Also, when you look at Europe, there's a great opportunity to trade and do business. By having the euro, you really facilitate easier transactions.

TGR: The bailout provides a stopgap solution for the European Union. In the United States you have "green shoots" economic data, and there's still economic growth coming from China and India. There are lots of positive signs that the global economy is heading in the right direction. Nonetheless, we're seeing quite a bit of volatility in the markets. Why is this happening?

CO: There are positive signs, but if you dig behind the data, they're not nearly as positive as one might think. Again, if we look at this European bailout, I think that the issues still exist. If you look at Spain, it has a deficit of around 11% of GDP—Portugal, the U.K., all these countries are running big deficits. I might add, too, that the United States, it is going to have a deficit of around \$1.6 trillion on a GDP of \$14 trillion, which means that the U.S. is also running a very large budget deficit. If you look at a lot of the green shoots data out of the U.S., some of the growth numbers have been funded by fiscal stimulus programs—government spending—and that is basically because they're running very large deficits.

If the U.S. was to live within its means, let's say with deficits of less than 3% of GDP, then I would say if you looked at what the GDP numbers are without the government spending, they wouldn't look all that good.

Looking at other countries around the world, such as China, I am a big long-term believer that China is going to have substantially higher growth than the U.S. and other advanced countries. Having said that, it looks like they're sort of pulling back right now; their stock market is down around 20%, so sort of entering a bear market. There are many risks when you look behind some of the finer details.

TGR: The Sprott Gold and Precious Metals Fund received the [2010 Lipper Fund Award for Best Fund Over One Year](#) in the precious metals category; it was up 114% in 2009. Congratulations! With that in mind, what are your short- and longer-term projections for gold?

CO: My longer-term projection, which I have had for the last two years, is that I expect gold to be at \$2,000 roughly two years from today. On many occasions, on TV and such, I have stated that if I'm wrong I'll shave the hair off my head; so, I firmly believe that. All the fundamentals point to a much higher gold price. The only question is, when?

In the short term, I am very optimistic. I'm hearing about new fiscal stimulus programs out of the U.S. I think there's a call for a mini-stimulus program, which again means high deficits continuing into the future, more printing of money, quantitative easing, and other such things. Everything looks really good for the gold price in the short term. The only thing I have to do is remember to contain my enthusiasm because sometimes these things don't happen the way you expect.

TGR: You said that gold would hit \$2,000 about two years from now. Would you consider that gold mania? Would that be the bump the gold bugs have been looking for?

CO: No, it's not. I'm going to try to avoid picking the top of the market and figuring where a peak will be when it does hit a mania. Really, the \$2,000 target price is based on an inflation-adjusted number for the gold price. The increase in the money supply, relationships of hard assets versus financial assets; some of the targets for those things are actually well above \$2,000. It's more likely, in my opinion, to be something substantially higher, and I don't want to guess what that will be because it's a bit of a game. One thing I would expect is that it will probably surprise a lot of us just how high it can go.

TGR: In a recent commentary, you wrote: "Over the short term we're positive that the current holdings will perform well should gold and the market continue to move sideways." That sounds like you're hedging your position on gold prices.

CO: In the short term, I think you always have to be cautious because things may surprise you and the markets may not act rational. It's usually only over the long term that the true direction gets shown. A lot of the things we talked about earlier make me very concerned for the broad stock market. If we go back to 2008 where there was a very severe correction in the stock markets, we saw that the gold price and gold stocks were also impacted in the short term because when the panic buttons were hit everybody was selling anything they could. In a crisis gold usually goes up in value.

TGR: In Sprott's All Cap Fund, gold bullion ranks second to cash and short-term investments. Do you see a day when bullion is the fund's top holding?

CO: In many respects, it is the top holding. In the All Cap Fund we can short up to 20% of the stocks in the portfolio, so when we sell the stocks, effectively our cash levels go up. But that's money that is required as money on those investments. In my mind, gold is already the largest position in the All Cap Fund. Having said that, that could change too.

TGR: If the gold price does explode, does bullion become a better investment than equities, gold equities in particular?

CO: One of the things that I've been fairly consistent in saying to clients is that it's good to have a combination of both gold bullion and gold stocks. I look at gold bullion as being defensive in nature; it's really preservation of capital, preservation of wealth. It's the insurance against Armageddon in the systems; whereas I look at gold stocks as the ability to get capital appreciation in a bull market, like the one we're in. Having said that, you also have to recognize when you're at a peaking point for gold, which isn't always easy to recognize. There may come a point—and I think we're far from it—when people are not willing to bid up the price of gold stocks because they do not believe that the long-term price of gold is where the current gold price is; they don't believe the increase in earnings power will be long-term in nature.

TGR: How close are we to gold's "peaking point"?

CO: If you look at some of the valuations. For example gold to copper looks like gold is fairly valued. If you look at it relative to stocks, it's far from the peaks that we've seen in the past. In a mania, generally you'll see a number of these ties broken, and probably some irrational exuberance like what happened in the tech sector a few years ago. But that's quite a long way out—maybe it's five years, maybe it's 10. But I don't think it's in the next couple.

TGR: Tell us about the top three holdings in your Gold and Precious Metals Fund: [Barrick Gold \(NYSE:ABX; TSX:ABX\)](#), [Colossus Minerals \(TSX:CSI\)](#), and [Gold Fields Ltd. \(NYSE:GFI\)](#).

CO: Two of them are fairly new. I had not owned Barrick for the last decade because I did not like its hedgebook, as I thought it was quite detrimental to the stock price. If you look at Barrick over the last decade, it was a big underperformer relative to most gold stocks. When it covered its hedge last year, I looked at the valuation of Barrick versus its peers, and could very easily see that because of its decade of hedging, it was trading at a multiple that was almost half of some of its peers. These discrepancies won't last forever, and over the next few years I think you will see Barrick actually outperform its peer group quite substantially. It's a new addition, but I think it's going to be a very good one.

The second one you mentioned was Colossus Minerals. When I first came to Sprott, Colossus was one of the first two companies that I put into the Sprott Gold and Precious Metals Fund. It has a project in Brazil that is one of, if not the highest, grade precious metals project on the planet. There are spectacular grades; you just won't see anything like it. Just a little bit of ancient history, back in the 1980s—I think it was 1985, 1986—there was a huge gold rush to the area. If you look at some of the old clips of *60 Minutes*, you will see some 60,000 artisanal workers

digging for gold with their shovels and carrying bags of dirt out of these pits. It was quite a sight.

TGR: You're talking about the Serra Pelada project?

CO: That is correct. When 60,000 people descend upon a property, it becomes very difficult to operate it as a commercial business. For the last 20 years, after the artisanal workers left, nothing really happened with it. A couple of years ago the management team at Colossus was able to negotiate a deal with the artisanal workers to go in there and look at commercially mining the remaining gold. Colossus is getting permits; it got some additional land around the area. I think it looks like a spectacular story. I think it's very cheap. There aren't any proper earnings and capital models out because Colossus is still putting together a resource, but I believe that if you sort of take the information that's out there, and apply some general rules of thumb, you will find that this is a very cheap and profitable operation. I believe it won't be long before we see analysts putting those numbers out there.

TGR: Even with the ownership stake from COOMIGASP (a local co-operative representing the interests of artisanal miners)?

CO: Yes, COOMIGASP still has a small stake still in it. But having said that, I think it's good to have a local partner in place. A local partner is good in terms of building and operating a mine.

TGR: And Gold Fields?

CO: If you go back to 2000 to 2002, we were actually buying a significant amount of Gold Fields at my previous company, and we made quite a bit of money. Then the black empowerment rules came in and, to a large extent, I exited South Africa. It was only last year that I added some Gold Fields back to the Sprott Gold and Precious Metals Fund. It was the valuation of Gold Fields on most metrics that makes it one of the cheapest majors out there. I think it is being unfairly punished for some of the issues that have existed in South Africa; we have taken a big position in the last few months.

TGR: In your last interview with your fund's co-manager, Jamie Horvat, talked about the strong balance sheets of [Aurizon Mines Ltd. \(TSX:ARZ; NYSE.A:AZK\)](#) and [IAMGOLD Corp. \(TSX:IMG; NYSE:IAG\)](#). Please give us an update on those companies.

CO: Aurizon Mines still has a very strong balance sheet, and it has actually about \$114 million in cash, and another \$112 million in working capital. Aurizon continues to build a pretty strong war chest and at some point we might see them take out a company with all that cash or maybe they will start to pay a dividend. We continue to be a big shareholder. It hasn't really done much in the last six months, but it's sound, it's safe, and it's in Canada. We like companies that operate in Canada. It's all good.

IAMGOLD is another one of our big shareholdings at Sprott. A year and a half ago you could have bought it for \$6; now, it's in the high teens. It's been a great performer for us; it has a strong balance sheet. IAMGOLD has deployed some of that money because it has been building its newest mine, Essakane, in Burkina Faso, West Africa, which will be commencing production this June. Having said that, IAMGOLD still has roughly \$200 million in cash and cash equivalents in bullion so they're very healthy, and we're looking forward to production from their newest mine.

TGR: What are some countries, or areas, that you're interested in at the moment?

CO: As I mentioned, we do like Canada. We like Canada because of the safety of jurisdiction and it's a safe place to operate. Having said that, I think you're starting to see that you're paying a bit of a premium for owning companies in Canada. One of the other areas that we like is Brazil. Brazil's a great place to operate; you have companies like [Yamana Gold Inc. \(TSX:YRI\)](#)

[NYSE:AUY; LSE:YAU](#)) and [Eldorado Gold Corp. \(TSX:ELD; NYSE:EGO\)](#), which have been quite successful down there. One of the things—I think we've been talking about this for the past several months—a lot of the juniors in Brazil trade at very low valuations on ounces in the ground. I am talking about the companies with significant ounces that might one day be a mine but are not now.

If you look at the valuations of a lot of these companies, you're finding that companies may be trading at \$25 to \$50 an ounce, and then if you go over to a place like West Africa, you find that a lot of similar companies are trading at \$50 to \$100 an ounce or sometimes even more. Why am I saying West Africa? If you go back in geological time, you find that Brazil and West Africa were basically side by side, so a lot of the geology is quite similar. I think this sort of valuation discrepancy in Brazil does not make an awful lot of sense because it is a very good jurisdiction to operate, just like many countries in West Africa.

We highlighted this in our December write-up, and we added a number of Brazilian names, which we think look awfully cheap. Just to mention a few: [Magellan Minerals Ltd. \(TSX.V:MNM\)](#), [Brazauo Resources Corp. \(TSX.V:BZO\)](#), [Verena Minerals Corp. \(TSX.V:VML\)](#), and [Amarillo Gold Corp. \(TSX.V:AGC\)](#).

TGR: Didn't Eldorado make an offer for Brazauro Resources?

CO: Well, we mentioned Brazauro in a writeup not too long ago, and lo and behold, about two weeks ago Eldorado came out with an offer that values Brazauro at \$1.25 a share. Just about a month ago, we were buying some of their shares for \$0.50. We were already one of its largest shareholders, but we were adding to the position because we thought it was a very cheap company. At some point, these cheap ounces will get recognized. I wonder, in light of the Brazauro move, if this process is already starting? I think it is, and we're quite well positioned with a number of our Brazilian names.

TGR: You said that you liked Canada. What are some companies in Canada you like?

CO: We've been big supporters of [Osisko Mining Corp. \(TSX:OSK\)](#) for quite some time and continue to love that story. They just made a bid for another company we own called [Brett Resources Inc. \(TSX.V:BBR\)](#); we're very happy that they're taking them out. Osisko has a joint venture with a company called [Clifton Star Resources Inc. \(TSX.V:CFO\)](#), which we have a small position in, and we're continuing to follow that. There are companies like [PC Gold Inc. \(TSX:PKL\)](#), which is looking at the old Pickle Crow mine, and hopefully coming out with a resource shortly. [Premier Gold Mines Ltd. \(TSX:PG\)](#), Ewan Downie's company, has been doing a wonderful job of building assets and building ounces on those assets. [Detour Gold Corp. \(TSX:DGC\)](#)—they just came out with their feasibility study a couple of days ago. It looks like it might be one of Canada's newest gold mines in the not too distant future.

TGR: The market has been anticipating that feasibility study for some time. What did it determine?

CO: There was a modification of their previous feasibility from last year, and there's a couple of nuances. Detour is going to look at milling about 30% more tons annually than in the past study. They're also looking at a coarser grain size, which basically means it's going to be less energy intensive in terms of the milling process. Detour expects to continue to get good recoveries; they're looking at annual production being around 650,000 ounces with costs being around \$400–\$450 an ounce. It's a big asset. One of the things the market is wondering is whether or not something like Detour, or Osisko for that matter, will get taken out because they represent very attractive companies with good growth in their production.

TGR: Are there any thoughts you would like to leave us with?

CO: Just keep the faith. Governments around the world continue to spend; they continue to print; they continue to quantitative ease. Until the governments take the necessary medicine, the story for gold is going to be very bright.

Bringing more than 21 years of experience in the investment industry, Charles Oliver joined [Sprott Asset Management](#) (SAM) in January 2008 as an Investment Strategist with focus on the Sprott Gold and Precious Minerals Fund. Prior to joining SAM, Charles was at AGF Management Limited, where he led the team that was awarded the Canadian Investment Awards Best Precious Metals Fund in 2004, 2006, 2007, and was a finalist for the best Canadian Small Cap fund in 2007. At the 2007 Canadian Lipper Fund awards, the AGF Precious Metals Fund was awarded the best 5-year return in the Precious Metals category, and the AGF Canadian Resources Fund was awarded the best 10-year return in the Natural Resources category.

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