



Patient Capital... Positioned for Profit

A PEEK AT THE WEEK THAT WAS - March 01, 2014

“Armaments, universal debt, and planned obsolescence - those are the three pillars of Western prosperity. If war, waste, and moneylenders were abolished, you’d collapse. And while you people are overconsuming the rest of the world sinks more and more deeply into chronic disaster.”

Aldous Huxley (1894 - 1963)

Aldous Huxley was a bit out there but the author of "Brave New World" hit it spot on with the above quote. In the developed west we are armed, indebted and increasingly obsolescent...and it seems like the rest of the world is sinking into chronic disaster. And yes, get rid of war, waste and banks and the world would unquestionably be a much better place. Sadly, all three are part of the human experience and they are not going away anytime soon. So best that we be aware of what is going on around us. And there is a lot going on.



The charge of the light brigade....old school

In the Ukraine, they are talking another Crimean war. And why not, the last decent stoush in the region was way back in 1853 when the orthodox Christian Russians took on an unusual consortium of Catholics, Protestants and Muslims from France, Britain and Turkey. Don't see that very often anymore. Oh yes, you do...it's call NATO.

The unlikely consortium won and the Russians were routed when....*into the valley of death charged the light brigade*...at least according to the famous poem by Alfred Lord Tennyson.

***Half a league half a league,
Half a league onward,
All in the valley of Death
Rode the six hundred:
'Forward, the Light Brigade!
Charge for the guns' he said:
Into the valley of Death
Rode the six hundred.***

Click [here](#) for the full version of this classic poem by one of the masters.

Sevastopol fell and the Russians lost their Black Sea port...but they would be back...as Bolsheviks. Poor old Crimea has been a very "popular" spot over the millenia and has shed more than its fair share of tears as invader after invader has imposed its iron will and

forlorn legacy. Just in the last 100 years, this region was sequestered by the Soviets in 1921, overrun by the Hun in 1942 and then restored by the Russian army in 1944. In the process, the ruthless, recriminating reds ran off the Crimean collaborators (which they identified as pretty much the entire Crimean Tartar population) to Central Asia. Then they moved in themselves.

A decade later, in 1954, the Soviet Big Boss, Nikita Khrushchev, decided to give the region to the Ukraine...probably because he himself had come up through the ranks of the Ukrainian Communist party. And why not? In 1954, the Soviet Union was just one big happy family, so it was a bit like dad giving the bottom 40 acres of the farm to his brother. Of course, the brother would always hold it for the benefit of "all the kids". Unfortunately the big happy family split apart in 1991 and the Crimea, now largely Russian, remained with the Ukraine.

Nevertheless, the Russian navy once again calls Sevastopol home and that's where it gets interesting. Why do you think that the saga in Syria continues? And why were the Commies so concerned about Caesar's capers against Assad back in September last year?

It's simply because the Russians also have a naval base in Tartus, Syria, which gives them a great Club Med access pass in that part of our lonely planet. And a fleet on the Black Sea is just a quick dart through the Bosphorus to the Sea of Marmara. Pop across the Dardenelles to the Aegean and voila...Club Med. And trust us when we tell you that Eurasia is very important to a lot of potential world dominators, not just the Russkies.

Little wonder then that Barackus Caesar is on his chariot.

From the [New York Times](#), February 28, 2014:

Obama Warns Russia Not to Intervene in Crimea

From [NPR via The Associated Press](#), February 28, 2014 8:12 pm

Obama Warns Russia Over Military Moves In Crimea

From [CNN](#) February 28, 2014 8:43 pm

Obama warns Russia against Ukraine intervention, says 'there will be costs'

Czar Vlad is not taking this Crimean thing lightly. Barry might be barking but we suspect that Vlad has already bitten.

From [Fox News](#), February 28, 2014:

Ukraine official: Russia has launched 'armed invasion' in Crimea

This could get very interesting, very quickly.

Meanwhile, on the other side of our lonely planet.

From the [Brookings Institution](#), February 2, 2014:

Is China Preparing for a "Short, Sharp War" Against Japan?

From [The Times \(UK\)](#), February 24, 2014:

China ready for 'short, sharp war' with Japan [wow...that was fast]

Then, of course, you have the usual suspects...Syria, Sudan, Iran, India / Pakistan...not to mention internally conflicted hotspots like the always interesting Venezuela and most recently Egypt, where the whole government recently resigned, probably to make way for Pharaoh Mubarak II.

The world is getting grumpy. The military industrial machine are gleeful.

The rest of us should be glum...and watchful...especially as the big bout unfolds between the current and former champions of the world. Vlad "Czar" Putin is the reigning champ, having made a chump of Barry "Caesar" Obama in their last big "Saga in Syria". Caesar still claims a points victory in that brawl but the rest of the world clearly saw The Czar coming out as champ.

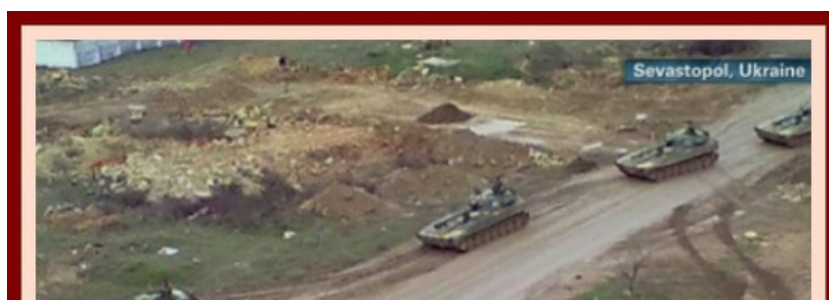
Now we move over to the next re-match, which the sporting pundits have already dubbed the "Pain in Ukraine".



How do we see the match?

Well, we're no boxing experts but we suspect that Vlad will rumble and Barry will crumble. Putin simply cannot afford to lose his Black Sea naval base, the Eurolanders need the Russian natural gas and the US simply does not have the gusto to go "gang ho" at this point. The Reds will probably do to the Crimea what they did to Georgia in 2008...all in the name of protecting the local Russian population. Pity no one was there to protect the Crimean Tartars some 60 years ago.

But politicians can make incredibly stupid decisions, usually for all the wrong reasons. So stay tuned sports fans, this match just might go all 15 rounds. God help us if it does!





So what does Mr. Market think about the big "Pain in Ukraine" bout? Apparently, Mr. Market could care less about geo-political pugilism. He is only concerned about swinging from the 1900 chandelier at Club S&P. And he got so close...with the punters pushing the S&P up tantalizingly close to 1870 before a late Friday afternoon, month end, profit taking...you name it...who cares...sell-off saw it close just shy of 1860.

Everything is good in the world according to Mr. Market. Who are we to argue?

Ms. Bond's 10 year treasury rate dropped from 2.74% to 2.66% during the week, basically back to where it started the month. Ho hum.

Meanwhile, gold started the week around \$1,322 / oz, ran up to \$1,345 before getting slammed down on Wednesday in normal fashion. It closed out the week just shy of \$1,329. The patrons at Bill Bullion's Gold Bar don't care. They are expecting worse. In fact, they are hoping for worse because to them, worse is better. Better pricing at which to buy. They have figured it out. We hope you have too.



We'll start out with an apology that this week's edition is once again dominated by nobles...noble metals, that is. We will be taking a detailed peek at another precious metal...in this case, **platinum**. It's a close cousin of the shiny stuff and part of a tight knit family of precious (and noble) metals which includes gold, silver, platinum, palladium and rhodium.

Why punish you with platinum? Well, simply because we are attracted to aberrational behavior and what is happening in platinum certainly qualifies as unusual, if not aberrational. And aberration is often related to opportunity. And everyone likes opportunity, don't they?

So we are going to make our case for Element #78 and wonder why the price is down, while the market fundamentals are screaming for it to go up.

And while on the elements, we'll share a Financial Times piece that actually suggests that manipulation of the precious metals does take place. Surprise, surprise! But don't go looking for this article by yourself...it's been pulled from the FT site. Surprise, surprise!

And continuing our theme, our chart of the week will give you another reason to cheer (and buy) every time the shiny stuff gets slammed down. We'll explain how their management

may have wised up and why the precious metals miners are poised to play catch up.

If time and space permit, we'll consider why India may be interesting, especially if you believe the grand manipulator himself, Nathan Rothschild, when he admonished his banking clients to "buy when there's blood in the streets". Old Nathan ran against the herd and now his family rules the world. It pays to be a contrarian. Just ask wise and wily Warren Buffet! He's done OK too.

Let's get rolling...after our customary giggle, of course.



We'll hold this line until Hell freezes over -- Then we'll hold it on ice skates.

Anonymous, picket sign

They're holding the line in South Africa...skates or no skates. For over a month now, striking workers at South Africa's platinum mines have taken out over 40% of the world's output of Element #78. So why should we care? Well, firstly because platinum is in short supply (= opportunity) and demand is increasing (= opportunity) and price is stagnant (= opportunity).

Let's start at the beginning. What is platinum and what is it good for? From [Wikipedia](#) [emphasis ours]:

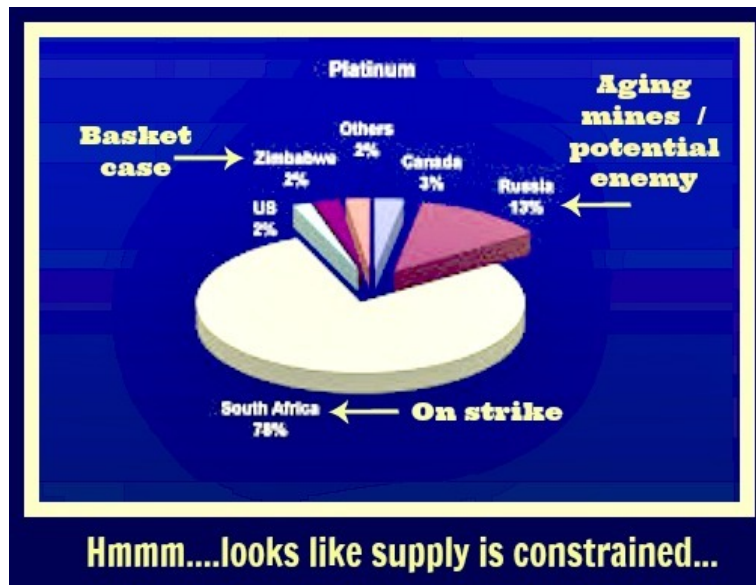
Platinum is a chemical element with the chemical symbol Pt and an atomic number of 78.

*Its name is derived from the Spanish term platina, which is literally translated into "little silver". **It is one of the rarest elements in the Earth's crust and has an average abundance of approximately 5 µg/kg. It is the least reactive metal. It occurs in some nickel and copper ores along with some native deposits, mostly in South Africa, which accounts for 80% of the world production.***

*As a member of the platinum group of elements, as well as of the group 10 of the periodic table of elements, platinum is generally non-reactive. It exhibits a **remarkable resistance to corrosion**, even at high temperatures, and as such is considered a noble metal.*

*Platinum is used in **catalytic converters**, laboratory equipment, electrical contacts and electrodes, platinum resistance thermometers, dentistry equipment, and jewelry. Because only a few hundred tonnes are produced annually, **it is a scarce material, and is highly valuable and is a major precious metal commodity.***

OK...80% comes from South Africa and they are on strike. What about the rest? Where does it come from and can they ramp up production to meet demand? Let's take a look.



Platinum and its close relative, palladium are very different from gold and silver. With gold and silver, most of what's ever been mined is still around. It is stored as value in one form or another....bullion, coins, jewelry, etc. Silver and gold, in particular, are hoarding items. Platinum and palladium are action items. Most of them die in battle. The lucky ones are safely ensconced in high end jewelry worn on a pretty neck or a lovely finger.

Sure, some platinum and palladium is used for high-carat jewelry and similar items but most of it goes up in smoke...up an industrial chimney or in the process of reducing smog from the average car's exhaust system.

Bottom line is that the stuff has to be constantly produced...and that means...mined.

As we see from the illustration above, mining produces some issues, especially now with the South Africans downing tools and upping placards. South Africa is by far the most important of the mix. It produced 73% of the platinum and 37% of the palladium in the world in 2012...but the costs of production keep increasing. As a result, miners have been shutting down mines that operated at less than breakeven at a rapid clip. Since 2006 or so, production of platinum group metals in South Africa has declined 19%. A combination of constantly recurring labor disruptions and the closure of marginal mines has resulted in platinum output from South Africa falling 16% in 2012 to 4.1 million ounces, its lowest since almost the turn of the new century.

Mining is a tough business at the best of times and much of the physical hardship has been replaced through the use of technology and sophisticated heavy equipment. But the South Africans have a set of environmental and labor related challenges which has them in a vice. Firstly, deposits in South Africa are difficult to mechanize from an engineering standpoint because they too thin and too narrow to get the necessary equipment underground. Even if, in certain circumstances, mechanization of the mines would enhance production and reduce costs, management simply cannot do so because of political ramifications. Unemployment is high among a historically disadvantaged and black mining population so the politicians in their infinite wisdom, have blocked wholesale mechanization of mines because it would reduce the need for labor.

So South African mines remain extremely labor-intensive, which creates its own set of problems.

Right now, South African mine workers are arguably underpaid for what they do by

comparative global standards and conditions. As a result, their claims for higher wages are the primary cause of the current strike. So while wages should rise in a perfect world, the mining companies simply cannot afford the added expense. Prices are simply not supporting the cost of extraction.

To make matters worse, the politicians are seeking to increase the government's take in the form of increased royalties, taxes, social sharing, etc.

And let's not forget that miners have to constantly replace inventory, which means that they must consistently invest big sums to discover and develop new ore bodies and new areas of platinum reef in order to replace older mines that have been producing for the last six or seven decades.

So, in technical industry terms, "they are stuffed". OK..so let's look elsewhere, starting with their friendly neighbor to the north.

Zimbabwe is endowed with potential resources but it is also saddled with Robert Mugabe, who decided five years ago that the mining industry had to sell 51% of itself to historically disadvantaged black populations. Half is not enough apparently and since his re-election, Mugabe has made it clear that he will use his best (malevolent) endeavors to take over the entire mining industry, just as he did with agriculture...and of course, that worked out just swell. A veritable bread basket was turned into just a basket through misguided governmental policies, theft and mismanagement. Mugabe managed to turn Africa's largest food exporter into a net food importer. And let's not forget his chief financial man, Gideon Gono who gave us the world's most recent dose of hyper-hyper-inflation. Brilliant. Handle Zimbabwe with extreme care.

Russia has platinum but it has its own challenges and in any event, it produces mainly palladium, as a byproduct from its nickel, cobalt and copper mines. The bulk of their production comes from the Norilsk ore bodies, which are getting deeper with declining grades. More depth, more expense. Lesser grades, lesser productivity, more expense. And with Vlad and Barry setting up to go head to head in the upcoming "Pain In Ukraine" match, getting easy access to Russian platinum may not be all that easy.

We could go on but by now, you've probably got the message. The supply side is limited.

But what about demand? Well, as they say, a picture is worth a thousand words, so let's take a look at Beijing...with and without smog.



Or how about this? From [Time World](#), February 26, 2014:

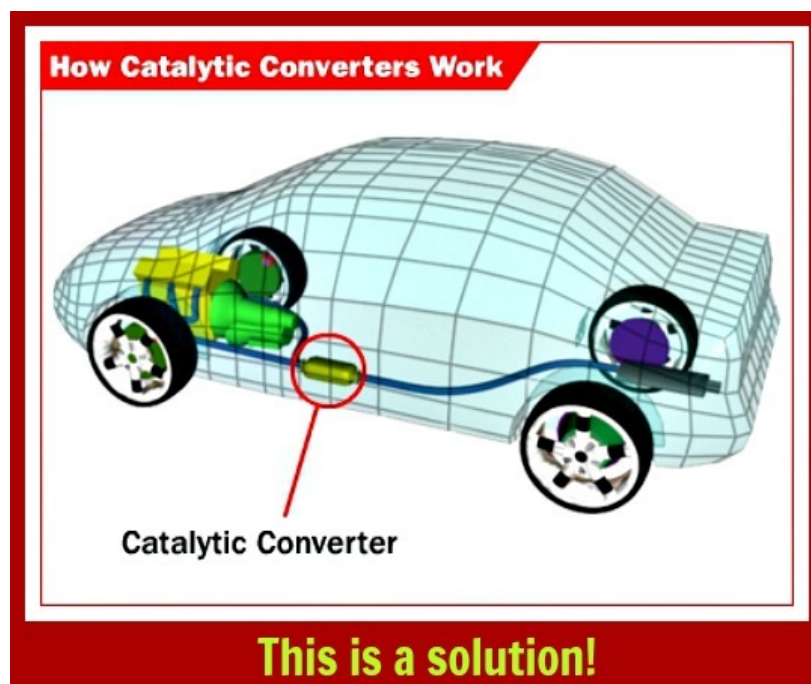
China's Apocalyptic Hellscape

A general view of the pollution covered Beijing CBD on Feb. 25, 2014 in Beijing.



Because of the physical impact displayed in pictures like the two above, the demand for platinum and palladium in industrial applications is growing steadily and may explode at some point in the not too distant future. China must tackle one of its biggest issues...smog...much of which is the result of increased car ownership. Those canny Confucians have discovered that driving a car is preferable to riding a bicycle. As a result, car ownership is exploding, along with the smog levels.

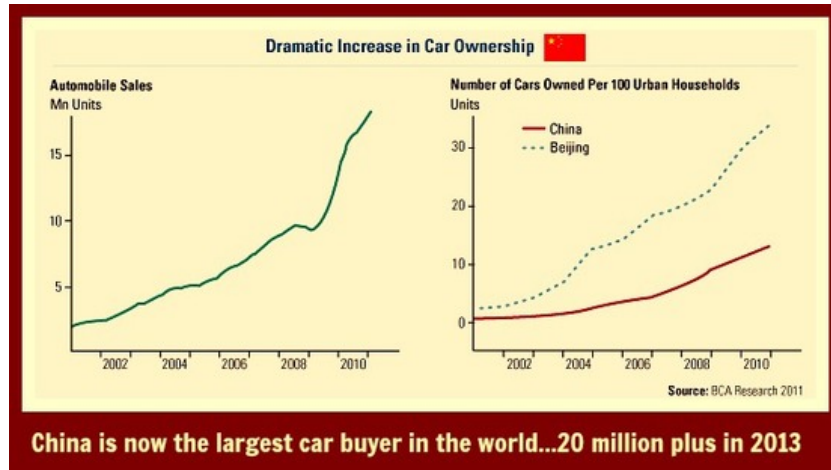
The Chinese government has identified toxicity and cardiopulmonary illness resulting from poor air quality as one of the greatest public health dangers in China....even worse than all those toxic trusts we've recently been writing about. The Confucians love five year plans for some reason, so they have mandated one to substantially improve air quality. In doing so, it will require higher loadings of platinum and palladium in new vehicles.



Most platinum goes out a tailpipe or up a smokestack. Its catalytic properties make many noxious emissions from burning hydrocarbons disappear. This is good. And the cost of adding catalytic converters during the manufacturing process is relatively low...let's say, less than 3% of the overall cost for top coverage on vehicles produced in the west. This is good also, especially when considering the benefits to human health and the environment

generally. The Chinese have been scrimping on the amount of platinum and palladium used in their catalytic converters and they are suffering the consequences.

In 2012, China also eclipsed the United States in auto sales, but they still are not consuming platinum and palladium to the same extent as the US because of their lower level requirements for pollution control. Less than half the amount of platinum used in North America on auto catalysts was used in China in 2012, but this is now changing, The government has "hinted" that they will order manufacturers to have five times more platinum and palladium loadings per vehicle than currently used. In what is now the largest vehicle market in the world, this will invariably lead to a substantially higher demand for platinum and palladium.



And that's just China. Let's not forget India and all the other emerging nations where car ownership is rising dramatically. The prospects for platinum and palladium look good. So the price must have gone up, if only because of the decreased supply resulting from the South African strike. Well...let's take a look.



We suspect that the usual suspects are up to their usual tricks. We will be keeping a close eye on developments in this space. We suggest you do the same. Demand is rising. Supply is falling and the price is stagnant. Something's gotta give.

And speaking of precious metals price manipulation, the Financial Times was unusually candid in an article during the week. From the Financial Times, February 23, 2014 [emphasis and wise cracks in red are ours as usual]:

Gold price rigging fears put investors on alert

Global gold prices may have been manipulated on 50 per cent of occasions between January 2010 and December 2013, according to analysis by Fideres, a consultancy.

The findings come amid a probe by German and UK regulators into alleged manipulation of the gold price, which is set twice a day by Deutsche Bank, HSBC, Barclays, Bank of Nova Scotia and Société Générale in a process known as the "London gold fixing". [just the name gets you thinking doesn't it?]

Fideres' research found the gold price frequently climbs (or falls) once a twice-daily conference call between the five banks begins, peaks (or troughs) **almost exactly as the call ends and then experiences a sharp reversal, a pattern it alleged may be evidence of "collusive behaviour"**. [banks would never do that, would they...well...maybe with LIBOR rates...oh yeh...and FOREX trades but nothing else...honest!]

"[This] is indicative of panel banks pushing the gold price upwards on the basis of a **strategy that was likely predetermined before the start of the call** in order to benefit their existing positions or pending orders," Fideres concluded.

"The behaviour of the gold price is very suspicious in 50 per cent of cases. [hah...you missed the other 50%] This is not something you would expect to see if you take into account normal market factors," said Alberto Thomas, a partner at Fideres.

Alasdair Macleod, head of research at GoldMoney, a dealer in physical gold, added: "When the banks fix the price, **the advantage they have is that they know what orders they have in the pocket**. There is a possibility that they are **gaming the system**."

Pension funds, hedge funds, commodity trading advisers and futures traders are **most likely to have suffered losses as a result**, according to Mr Thomas, who said that many of these groups were "definitely ready" to file lawsuits. [Where do we sign up for those?]

What was really interesting about the article is that a day after it was published online, it disappeared. Try to find it now and the message below is what you get. We guess those London gold "fixers" also happen to be big advertisers and who cares about objective journalism where client dollars are involved.



But don't worry, we've preserved the entire article for you. Just click the image above to be taken to it...or click [here](#). All these shenanigans will end some day and when they do, the market will have its way...and the world (and the atmosphere) will be a better place for it.

CHART OF THE WEEK

Mining is the art of exploiting mineral deposits at a profit. An unprofitable mine is fit only for the sepulcher of a dead mule.

T.A. Rickard (1864 - 1953)

We have commented more than once that mining is a tough business. After all the work of discovering and developing your resource, you finally get to mine it. As soon as you do, you start draining your limited inventory into a market that you have no control over. That's tough.

The miners have had a nasty habit of spending big and stupidly during the good times.

They routinely depleted their precious capital on overpriced acquisitions while squandering their even more precious ore deposits into an unappreciative and manipulated market. But recently, we suspect that the mining industry is going through something of a catharsis. They have been suffering a death of a thousand price cuts as gold got slammed down in the past 12 months and instead of raking in the dough, they are barely surviving.

Forced fasting will often result in clear thinking and in this regard, it appears as though the industry is in the process of altering its priorities. Profitability, disciplined capital deployment and cash flows per ounce of gold appear to be gaining preference over maximizing gold production. They have gained consciousness and clarity during this dark time. They understand that greater financial discipline and the creation of shareholder value for the true owners of their companies will provide salvation. Instead of the usual squandering, they are now keeping ounces in the ground as they are forced to mothball projects around the globe, reducing supply as demand exorably grows. Therefore, from a sentiment and valuation perspective, gold and silver mining stocks are potentially the ultimate contrarian investment of this decade.

With that in mind, let's hand it over to our chum from last week, Incrementum's Ronald-Peter Stoferle to introduce our chart of the week (which, of course, we borrowed from him):

If the developments in the gold price were already a big disappointment in the past two years, the developments in gold stocks – both in relative and absolute terms – were a complete disaster. It appears as though mining stocks were punished by frustrated shareholders for capital-intensive development projects, risky takeovers and strongly rising production costs. That can be seen in the ratio between gold stocks and gold: The oldest available gold mining index, the Barron's Gold Mining Index (BGMI) currently trades close to the lowest level relative to gold in more than 70 years.



We suggest that you study this chart carefully. Even a reversion to the mean is a substantial gain...and we would submit...and have submitted ad naseum, that there are plenty of reasons for a wild overshoot. Do we have your attention yet?



Til next week...

"Ignorance is the curse of God. Knowledge is the wing wherewith we fly to Heaven."

William Shakespeare

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