

Goldletter INTERNATIONAL

the international independent information and advice bulletin for gold and related investments

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China world leader in gold production since 2007



China has been a producer of gold for centuries and also has a history of usage that stretches back to antiquity. The gold industry has depended entirely on State investment since 1949, when the People's Republic of China was founded. Domestic private and foreign investors were excluded from the industry.

Driven by domestic demand the government invested heavily in the mining industry in the 1990s and as a result output doubled in six years. China's gold production for the first time reached 100 tonnes in 1995. In 2007, China passed the United States and South Africa as the second largest and largest gold producer, respectively.

South Africa dominated the gold mining industry more than a century since the discovery of the Witwaters reef in 1886, considered the "greatest goldfield in the world" on the edge of what is now Johannesburg. The country became the biggest gold producer since 1905, passing the United States.

According to China Gold Association, **China produced 340.88 tonnes of gold in 2010**, up 8% on the previous year (more than 26 tonnes).

According to the National Development and Reform Commission, from 2006 to 2010, China's gold production target was 1,300 tonnes. During that period, China also aims to increase its gold base reserve by 3,000 to 3,500 tonnes

China's top gold producing provinces are Shandong, Henan, Jiangxi, Yunnan and Fujian.

China's 10 largest gold mines include China National Gold Group, Zijin Mining, Shandong Gold Mining, Shandong Zhaojin Group, Lingbao Gold, Eldorado Gold (China), Shandong Zhongkuang Group, Hunan Jinxin Gold Group, Yunnan Geology and Mineral Resources, and Shijiazhuang Jinyuan Mining.

The 2010 industrial output value of China's gold industry amounted to approximately RMB 220 billion yuan (US\$ 33.8 billion) an increase of more than 70% compared with 2009.

According to China National Gold, China's **gold consumption** rose by about 4% to **430 tonnes**, with growth in the country's gold consumption staying intact in the coming years, but on a smaller scale than expected by the World Gold Council.

Official trade data from Hong Kong, Asia's biggest bullion trading centre and a main conduit for gold flows into the mainland, showed its gold exports to the mainland in the first nine months of last year more than doubled from a year earlier to 88.06 tonnes.

On an annualised basis that would translate into 117 tonnes of gold from Hong Kong alone in 2010.

China is finding new gold reserves at a fast enough pace to avoid exhausting supplies with production capacity holding pace with growing demand.

China's expansion process will be enhanced by the introduction of new ore processing technology like the application of bio-leach technology, a major subject of China's 10th 5-year Plan for key projects, and a new cyanidising technique (Thermal Chemical Pre-Oxidation Process) by normal pressure.

According to the China Geology Survey Bureau (CGS), 5 major gold mines were discovered in 2007, with a combined gold reserve of some 600 tons. These include the Ghandu Gold Mine in Tibet (reserves 120 tons), the Dachang Gold Mine in Quinghai Province (reserves 115 tons), the Yuangshan Gold Mine in southern Gansu Province (reserves 258 tons), the Sizhuang Gold Mine in Shandong province (reserves 52 tons) and the Baolun Gold Mine in Hainan Province (reserves 55 tons).

Early 2008, it was reported that a new gold deposit with an estimate reserve of 24 tons has been found in Xinjiang Uygur Autonomous region.

Geologists of the Shangdong Provincial Bureau of Geology and Gold Resources claimed to have found a gold deposit with a reserve of 103 tons. It is the second gold mine found just south of the famous Jiaojia Gold Mine strip of Laizhou near Sizhuang, where provincial geologists found another gold mine in 2007 with a deposit of 51.83 tons.

Not only China's national gold industry, led by its three publicly traded major gold groups Zhongjin Gold (HK code 3330), Zijin Mining (HK code 2899) and Zhaojin Mining (HK code 1818) is expected to get a strong boost, but also successful foreign exploration/development companies active in China will contribute to growing production in the years to come.

Some of these companies have been taken over by Chinese gold groups, including Sino Gold, continental Minerals and a 41.2% controlling interest in China Gold International (formerly Jinshan Gold Mines).

In 2010, Eldorado (ELD – TSX.V) contributed 11 tonnes (358,000 ounces) to China's gold production, equal to approximately 3% of the country's total gold output.

China's Gold occurrence

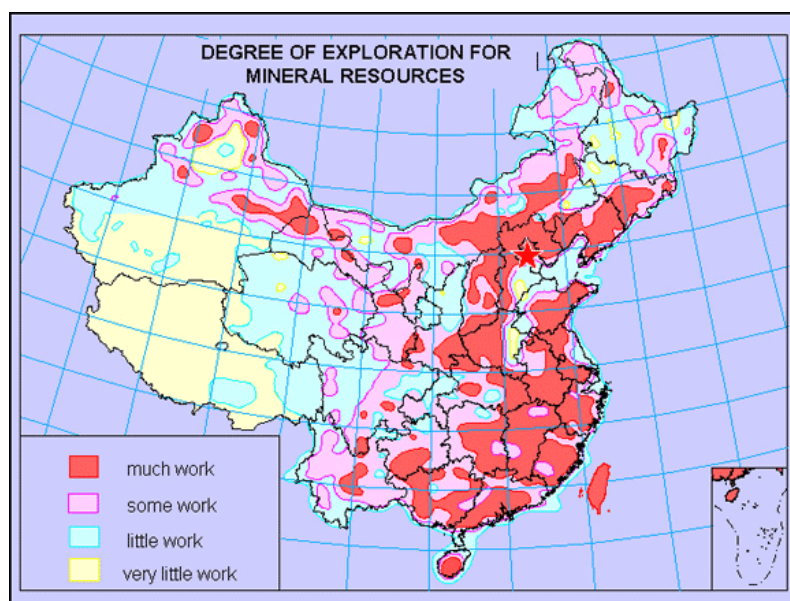
Advanced stage precious metals and base metals projects and large areas of mineral lands with potential exist in China and, as a result, there has been a steady growth in the number of foreign mining companies being active in China.

About 50% of gold in China occurs in quartz-gold vein structures, with another 17% occurring in placer deposits and the remainder is found in polymetallic deposits, often in association with copper. China's gold industry is fragmented, archaic and undercapitalised. Most of the production comes from small, underground mines with little mechanisation.

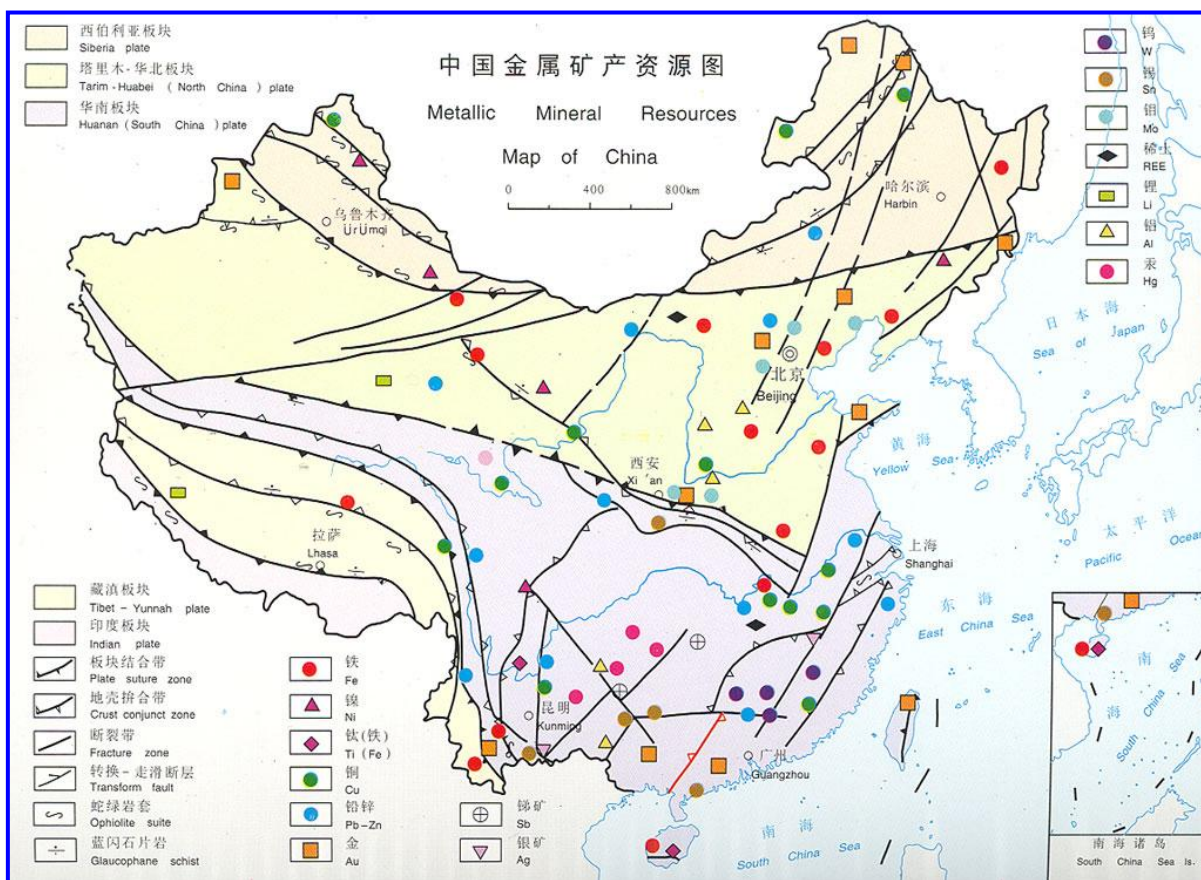
There are thought to be over 1,200 small to medium sized mines in operation throughout the country, equal to approximately 70% of total gold deposits and representing 25-30% of total proven reserves, with only a few mines producing more than 100,000 ounces annually, although the annual average is closer to 16,000 ounces.

The China Geological and Mineral Survey Bureau estimates the gold resources of Chinese ten major provinces to be over 11,000 tonnes and the country's prospective gold resources at around 15,000 tonnes.

A joint study by the United States Geological Survey and the Tianjin Geological Academy from 1997 to 2002 identified and reviewed over 160 gold occurrences in China. Within the category of sedimentary hosted gold deposits (a broad category including Carlin style), over 20 million ounces of resources have been identified in China versus over 70 million ounces in Nevada.



The largest deposits of this style discovered to date in China include Lannigou (> 3.2 million ounces) and Baguamiao (> 2.5 million ounces) but exploration has generally been neither well funded nor extensive. Most reserve definition programs are limited.



China's national gold industry

Control and ownership of many of China's largest mines is vested in the State and administrated through the China National Gold Group Corporation (CNGC). First established in 1979 and then reorganised in 1993. GNGC, operating under **China Gold Group**, controls the major gold mines in seven out of eight main producing provinces. The GNGC officially controls 450 mines and has 61 affiliates across China.

Through the biggest gold producer of the Group, Zhongjin Gold, CNGC contributes 20% of total gold production in China, and shares 30% of total Chinese gold resources.

Between 1949 and 1982, China banned personal ownership of gold, not to mention a gold market. In recent years, China gradually lifted its control over the gold market, by allowing the purchase of gold by individual citizens.

The move to bring the local gold price in line with the international price, occurred from recommendations by the World Gold Council (WGC) in 1998 as part of a timetable for deregulation of the market, there motivated by China's acceptance into the World Trade Organisation at the end of 2001.

China Gold Association was formally founded in November 2001, with 70 enterprises as standing directors, and 256 enterprises as directors.

The official opening of the Shanghai Gold Exchange (SGE) on 30 October 2002 heralded the start of a new era in the gold market in China, and is further evidence of the intention of the Chinese government to deregulate the precious metals markets.

In January 2008, China's gold futures made a strong debut on the Shanghai Futures Exchange.

Government investing in gold mining sector

In the 1980's the Chinese government invested heavily in the gold mining sector. This policy continued and was reinforced under the Eight Five Year Plan from 1991-1995. Government spending increased to US\$ 1.5 billion in 138 specific projects. The aim of this initiative was to restrict the informal and smaller sectors and consolidate small mines into bigger and more efficient operations. The policy was not successful and by the end of the 1990 investment had fallen to US\$ 12 million annually.

However, in the last five years China has made new efforts to improve its domestic environment for mining investment. Exploration is intensified by "further exploring the old deposits, prospecting for new areas, and starting special projects", with the emphasis on large and super large mineral deposits. Fundamental geological survey and resource evaluation under the supervision of China Geological Survey have been enhanced and the complete catalogue of geological data is online for query.

CHINA playing prime role in world's gold market

- ▶ Largest gold producer and second largest consumption market

Production 2010: 349 tonnes (2009: 314 tonnes)

- surpassed South Africa in 2009 to become the world's largest gold producer
- estimated annual growth: 5 - 6 %

Consumption 2010 : 430 tonnes (2009: 423 tonnes)

- estimated annual growth: 6 - 8 %

Outlook:

- ▶ **Positive:** → growth in retail and jewellery demand
- ▶ **Negative:**
 - no monetary function as long as RMB is pegged to dollar
 - total monetary reserves \$ 3,000 billion - gold reserves 1,054 tonnes (\$ 46 billion) = 1.6% of total monetary reserves
 - China not buying IMF gold
 - affluent gold reserves (5,000 tonnes) and resources (20,000 tonnes)

Conclusion: Gold price lacks strong support from Chinese demand

CHINA'S MAJOR NATIONAL GOLD PRODUCERS



China National Gold Group Corp. or **China Gold**, is a large-scale state-owned enterprise. As an investment organization authorised by the central government, China Gold directly reports to the central government and it is also a pilot company of which the government is as sole shareholder.

Being the earliest company in doing gold mining in China, China Gold has rich management experiences and strength in both technology and capital. At the advanced level of world standard, China Gold has its gold operations all over China, and contributes 20% of total gold production in China and controls over 30% of the total reserve in China, which guarantees its promising prospects.

China Gold has a 57% controlling interest in Shanghai-listed Zhongjin Gold and controls Hong Kong-listed Zhaojin Mining through a 37.3% interest owned by affiliated company Shandong Zhaojin.

The Yangshan Gold Mine, founded in 2007 in northwest China's Gansu Province, is considered to be the largest Carlin-type gold mine in Asia and the sixth largest in the world. It is estimated to have deposits equivalent to at least 300 tons of gold, in the high-grade "96" vein ore.

In May 2008, China Gold completed the purchase of the 41.2% controlling interest of Ivanhoe Mines in Jinshan Gold Mines for a purchase price of Cdn\$ 217.7 million.

On April 24, 2011, China Gold announced that it plans to inject all of its gold assets in Zhongjin Gold in 5 years.



Zhongjin Gold Co (100549 – Shanghai Stock Exchange) is principally engaged in exploration and smelting of gold, copper, lead, silver and other non-ferrous metals. The Company's major products are standard gold, mineral gold, smelting gold, electrolytic copper, content copper, silver, sulphuric acid and iron ore concentrate, among others.

On July 30, 2003 Zhongjin Gold, 57%-owned by China Gold, became the first listed company in the nation's gold industry after it launched an initial public offering (IPO) on the Shanghai Stock Exchange. The Company issued 100 million shares at a price of 4.05 yuan (US\$ 0.49) per share. The IPO earned 388 million yuan (US\$ 46.7 million) in net proceeds.

Zhongjin Gold, produced 85.82 tonnes (+ 4.3%) of standard gold and 19.7 tonnes (+ 15.9%) of mineral gold from its mines in 2010.

Zhongjin Gold has a current market capitalization of approximately RMB 48 billion (US\$ 7.4 billion).



Zijin Mining Group (2899 – Hong Kong) is China's largest and most efficient gold producer and was the first national gold production enterprise listed overseas (Hong Kong in 2003). The Company and its subsidiaries are a comprehensive mining conglomerate in China engaged in gold production, and specifically engaged in the exploration, mining and sale of gold and other non-ferrous metals.

In 2010, Zijin produced about 69.07 tonnes of gold (including 29.18 tonnes of mine produced gold).

At the end of 2010, Zijin retained resources reserve (audited) of 750.17 tonnes of gold (+5%); 1,827.9 tonnes of silver; 10,578.7 million tonnes of copper; 392,500 tonnes of molybdenum; 5.23 million tonnes of lead and zinc; 173,400 tonnes of tungsten; 184.5 million tonnes of coal; 99,290 tonnes of tin; 607,100 tonnes of nickel and 66.73 million tonnes of sulphur iron (standard ore).

In 2010, Zijin obtained new resources reserve (partially, not yet audited): 71.83 tonnes of gold, 1,014,000 tonnes of copper, 1,782,000 tonnes of zinc and lead, 78,000 tonnes of molybdenum and 3 million tonnes of iron ore.

Zijin owns 275 exploration rights with a total area of 5.52 square km, in which 43 overseas exploration rights with a total area of 314.75 square km, and 63 mining rights with a total area of 154,643 square km, in which 6 overseas mining rights with a total area of 5.68 square km.

Zijin has a current market capitalization of approximately US\$ 10.9 billion (10.5 billion A-shares + 4.0 billion H-shares).



Lingbao Gold (3330 – Hong Kong) is an integrated gold mining enterprise in China which is mainly engaged in gold mining, smelting and refining. The products of the Group are gold, silver, copper products, copper poils and sulphuric acid. Its miner resources are scattered in the region of Henan, Xinjiang, Jiangxi, Inner Mongolia, Gansu and Kyrgyz Republic, with 56 mining and exploration rights covering a total area of 2,222.74 sq km.

In 2010, Lingbao produced approximately 14.58 tonnes of gold (approximately 469,000 ounces).

Lingbao has a current market capitalization of approximately HK\$ 1.8 billion (US\$ 240 million).



Zhaojin Mining Industry (1818 – Hong Kong SE) is controlled by China Gold's affiliated company Shandong Zhaojin Group (37.3% interest). Currently the Company owns 33 subsidiaries, joint venture and associates nationwide, amongst them 6 operating mines within the Zhaoyuan district in the Jiadong peninsula of Shandong Province, namely: Dayingezhuang, Jinchiling, Xiadian, Hedong, Jintinglin and Canzhuang.

According to the China Gold Association, gold resources in the Zhaoyuan district account for approximately 0% of gold reserves in China.

In 2010, Zhaojin's total output of gold amounted to 672,811 ounces of gold (+ 7.4%).

As at the end of 2010, Zhaojin's gold ore resources under the JORC code were approximately 15.9 million ounces (as at year end 2009: 10.86 million ounces), and mineable gold reserves were approximately 8.1 million ounces (7.0 million ounces).

Zhaojin's current market capitalization is approximately HK\$ 13 billion (US\$ 1.7 billion).



Shandong Gold Mining (600547 – Shanghai Stock Exchange) one of China's top-3 gold producers, increased its gold production in 2010 by 18% from a year earlier to 25 tonnes (17.7 tonnes).

The Company's gold production is likely to accelerate in coming years since in the 5-year period ending 2010 Shandong found 800 tonnes of gold resources through exploration with a total investment of 1.15 billion yuan (US\$ 172.6 million).

On April 22, 2011, Shandong announced that it will issue up to 120 million A shares at not less than RMB 46.80 per share to raise approximately RMB 5.62 billion (US\$ 374.5 million) in am private placement. The proceeds raised will be used to extend gold resources.

Shandong Gold Mining has a current market capitalization of approximately RMB 66 billion (US\$ 10.2 billion).

Government encouraging foreign investment

One of the specific aims of the 1990's initiatives was to try and attract foreign investment into the Chinese gold mining industry. However, the lengthy and complex approval process, the limited and poor quality of designed exploration projects, coupled with a legal system that was unclear about ownership and without guarantees of tenure, was enough to deter most candidates. In addition, the mining taxation code did not encourage investment. However, changes in regulation adapted by the Chinese government have encouraged provincial mining bureaus to source capital from mineral exploration companies.

In 1996 China passed the mineral resources law on mineral exploration and development by which The State shall safeguard the national development and utilisation of mineral resources under the responsibility and supervision of the Ministry of Land and Resources ("MLR").

By this legislation MLR has promised to reform the approval process and the costs associated with securing exploration rights in China, and in doing so to encourage foreign investment in an industry yet to experience the transformation brought in other sectors of the nation's economy. The laws and notices issued in 1998 and 2000 clarified the exploration process and the transfer and assignment of exploration rights.

In 1999, China's Ministry of Land and Resources announced a total of 16 projects be recommended for international investment.

In February 2006, the MLR published the "Selected laws and regulations of the People's Republic of China on Mineral Exploration and Development".

The Chinese Central Government has granted Provinces the autonomy to approve Sino – Foreign Joint Ventures for mineral exploration and mining. This provision of the law has attracted a number of mainly Canadian public companies that have been entering into Sino - Foreign Joint Ventures.

The Provision on Guidance for Foreign Investment issued by the State Consul, highlights the protection of investors' legal rights and interests.

In the new Guidance Catalogue of Industries for Foreign Investment revised by the National Department and Reform Commission, the exploration and mining of special and scarce types of coal, precious metals such as gold, silver and platinum metals, precious non-metallic minerals such as diamonds, as well as phosphorus, barite, borax and celistite, is categorised as the restricted category.

The form is China-Foreign Joint-Venture and cooperation and the requirement of the Chinese side's holdings are articulated in specific catalogue of encouraged and restricted categories.

Various policies to encourage investment in Western China will also have impact on the proposed structure of an exploration vehicle. Projects based in Central or Western China (including Sichuan), although listed as "restricted", may in fact be treated as "encouraged". The exploration right granted will typically only be for a particular mineral in the exploration area, and not for all minerals found at the same site.

Exploration licences can only be granted to qualified, geological exploration work-units registered in China. Foreign investors will either need to obtain this qualification. Subject to any restrictions set out in the Catalogue and the qualification requirements, a foreign investor registered in China as a representative office, equity or co-operative joint venture, including a non-legal person, co-operative joint venture, or a wholly foreign-owned enterprise, may apply for an exploration licence.

At present, the Geological Survey Department of MLR, which has 26 affiliated organizations and 6 regional centres, is responsible for reviewing and approving exploration applications. Provincial authorities are entitled to issue exploration rights, but they cannot issue them to foreign invested enterprises or representative offices.

In 2003, the MLR issued a circular entitled Administrative Measures of Public Tendering and Auction for the Rights of Exploring and Exploiting Mines. The bidding regulations promulgated by the MLR, effective from August 1, 2003, prescribe three approaches for Chinese and foreign mining companies to obtain exploration and mining rights.

In December 2003, the Chinese Government issued a white paper on China's Policy on Mineral Resources which stresses that China will depend on exploitation of domestic mineral resources to guarantee the needs of its modernisation drive. In future, China will strengthen mineral surveying, prospecting, exploitation, planning, management and rational utilisation of mineral resources.

The policy also highlights the importance of sustainable development, and Sino-foreign co-operation in the exploration and exploitation of mineral resources will be increased.

Comments to activities of foreign exploration companies in China

The suggestion has been made in the past that China does not host any sizeable, continuous gold deposit amenable to commercial production based upon the fact that the largest mine was producing in the region of 100,000 ounces gold annually with the annual average closer to 16,000 ounces. This picture is outdated however, as growing production from its major national mines is demonstrating, and production from a growing number of gold projects developed by foreign companies came on stream.

Missing many of the sophisticated techniques of the western approach including highly sensitive geochemical and geophysical survey as well as high-end interpretation of satellite imagery, China is relatively undiscovered, This offers a high potential for successful exploration.

On the other hand, China's government could be more cooperative by shortening the time of mining licences being approved to foreign companies with a resource base.

FOREIGN GOLD COMPANIES WITH NI 43-101 OR JORC COMPLIANT RESERVES AND RESOURCES					
		Location	RESERVES Proven & Probable	RESOURCES Measured & Indicated Inferred	
Eldorado Gold (Sino Gold)	TJS	Qinghai	0.6	0.8	0.5
	Eastern Dragon	Heilongjiang	2.6	3.6	1.3
	Jinfeng, White Mountain	Guizhou, Jilin	0.8	0.9	0.2
			4.0	5.3	2.0
China Gold Interantional	CHS 217	Inner Mongolia	2.7	3.5	-
Mundoro Capital	Maoling	Liaoning	-	4.8	4.4
Continental Minerals x	Xietongmen	Tibet	0.6	4.3	-
Majestic Gold	Song Jiagou	Shandong	-	3.0	5.1
Corvette Resources xx	Gold Mountain	Xinjiang	-	2.0	0.6
Inter-Citic Minerals	Dachang	Qinghai	-	1.3	1.5
Minco Gold	Changkeng	Guandong	-	0.6	0.4
Dragon Mountain Gold	Lixian	Xinjiang	-	-	2.8
Goldrea Resources	Daye	Shandong	-	0.3	0.3
Total			7.3	25.1	17.1

x acquired as at April 29, 2011 by Jinchuan Group of China for aggregate cash consideration of Cdn\$ 431 million (Cdn\$ 2.60 per share)
xx formerly Tianshan Goldfields

CHINA's taking control over its gold industry

► Zijin Mining Group and China National Gold Group (incl. Zhongjin Gold)

→ Controlling more than 40% of China's gold production (314 tonnes) and more than 50% of total gold reserves (5,000 tonnes)

► Foreign participation in China's gold industry decreasing

→ **China National Gold Group**

acquires 41.2% controlling stake in Jinshan Gold Mines (April 2008) from Ivanhoe Mines for Cdn\$ 217.7 million; Jinshan Gold Mines renamed to China Gold International

→ **Jinshan Gold Mines** sells Dadiangou Gold Project to Zhongjin Gold (April 2010)

→ **Jinchuan Group** acquires Continental Minerals for Cdn\$ 432 million in cash

► Foreign gold producers active in China:

Eldorado Gold * 2010 : 357,947 ounces (2009: 126,299 ounces)

* including Sino Gold, acquired on December 15, 2009

China Gold International ** 2010 : 111,289 ounces (2009: 85,530 ounces)

** 41.2% owned by China National Gold