CPM Group

Precious Metals and Commodities
Research, Consulting, and Merchant Banking

1 May 2002

Dear Sir:

Much has been written and said lately about the need to regulate OTC derivative markets, worldwide.

This is nothing new: There have been a series of financial debacles involving derivatives since the middle of the 1980s. Every time a financial disaster due to mis-used or abused derivatives threatens the international financial system, regulators in the major market nations talk about the need to regulate these markets, and then do nothing substantial to improve matters. There are several reasons for this. Over-riding this is the complexity of the issue, and the fact that in reality none of the regulatory ideas thrown about by the politicians and regulators would mitigate these problems in the least. Also, the political clout of the major banks and brokerage companies, which as an industry are the major contributors to political campaigns, helps to forestall any regulations that would limit these financial institutions' ability to continue to reap the incredible profits available to them from derivatives sales and trading.

Derivatives, whether they are related to equities, interest rates, currencies, commodities, or other assets, are extremely powerful tools for corporations, financial institutions, and investors. That power can be harnessed in wonderful ways for these corporations. It also can explode in managers' faces, however, as has been demonstrated repeatedly over the past two decades. The ways in which such problems can develop, through misfeasance, malfeasance, or plain incompetence, are manifold, and reach from major, obvious shortcomings in the current practices of corporations in this area, to the most minute details of the contracts underlying these products.

Whether derivative markets ought to be regulated, much less how to do so, remains the focal point of much controversy.

CPM Group has focused on one small, mechanic issue which actually could vastly improve the performance and safety of derivatives markets with little legislative or regulatory involvement in these massive, international markets.

The issue that we are focusing on, regulation-wise, is the fact that many corporations that purchase derivative contracts of various sorts do not fully understand the financial implications of hedges they undertake, regardless of whether they are currency, interest rate, commodity, or other hedges. This is compounded by obfuscatory practices by the issuing banks and financial institutions, which frankly limit the disclosure in their contracts and marketing documents to the minimum required by corporate law. As a result, prior to inception of these positions few purchasers of such derivatives have done the due diligence necessary to be able to know what the credit, revenue, and other financial implications for their companies are under varying market scenarios.

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This could easily be remedied by governments requiring very simple, straight-forward, plain-language reports to be completed before any derivative transactions are entered into by public corporations. Such simple disclosures would illustrate clearly the price and credit implications of the derivatives under varying price and credit market conditions. Regulators could require they accompany all marketing documents from financial institutions, and be attached to all sales, registration, contract, and other documentation.

Attached to this letter are a chart and table CPM Group produced recently showing the revenue implications of various hedges to a gold producer, which was seeking to hedge its metal output. Whenever CPM Group constructs a hedge for a client, it produces a similar chart and table for the client, so that the client can see clearly and easily what the revenue and/or cost implications are for it in choosing various hedge strategies. We know from experience that banks and brokerage companies do not supply similar plain-language analyses to their clients.

Such a chart and table illustrate the price results of various hedges under differing price scenarios. Something this simple would go a long way to assist derivatives purchasing corporations in evaluating the potential implications for their companies of such positions.

CPM Group would be interested in your reaction to this idea. Thank you for any insights you might provide.

Sincerely,

"jeff christian"

Jeffrey M. Christian
Managing Director

Gold Hedges -- Competetitve Analysis

February 2002 examples
US dollars per ounce

This table presents the price a producer would receive at any given market price, depending on which sales and hedging strategy it used. Based with forward price at $280.

Market Price	Spot Sales	Forward Sales	Revenue Relative to Market	Collar $275-$285)	Revenue Relative to Market	Participatory Option	Revenue Relative to Market
$120	$120	$280	$160	$275	$155	$275	$155
$140	$140	$280	$140	$275	$135	$275	$135
$160	$160	$280	$120	$275	$115	$275	$115
$180	$180	$280	$100	$275	$95	$275	$95
$200	$200	$280	$80	$275	$75	$275	$75
$220	$220	$280	$60	$275	$55	$275	$55
$240	$240	$280	$40	$275	$35	$275	$35
$260	$260	$280	$20	$275	$15	$275	$15
$280	$280	$280	$0	$275	-$5	$275	-$5
$300	$300	$280	-$20	$285	-$15	$290	-$10
$320	$320	$280	-$40	$285	-$35	$310	-$10
$340	$340	$280	-$60	$285	-$55	$330	-$10
$360	$360	$280	-$80	$285	-$75	$350	-$10
$380	$380	$280	-$100	$285	-$95	$370	-$10
$400	$400	$280	-$120	$285	-$115	$390	-$10
$420	$420	$280	-$140	$285	-$135	$410	-$10
$440	$440	$280	-$160	$285	-$155	$430	-$10

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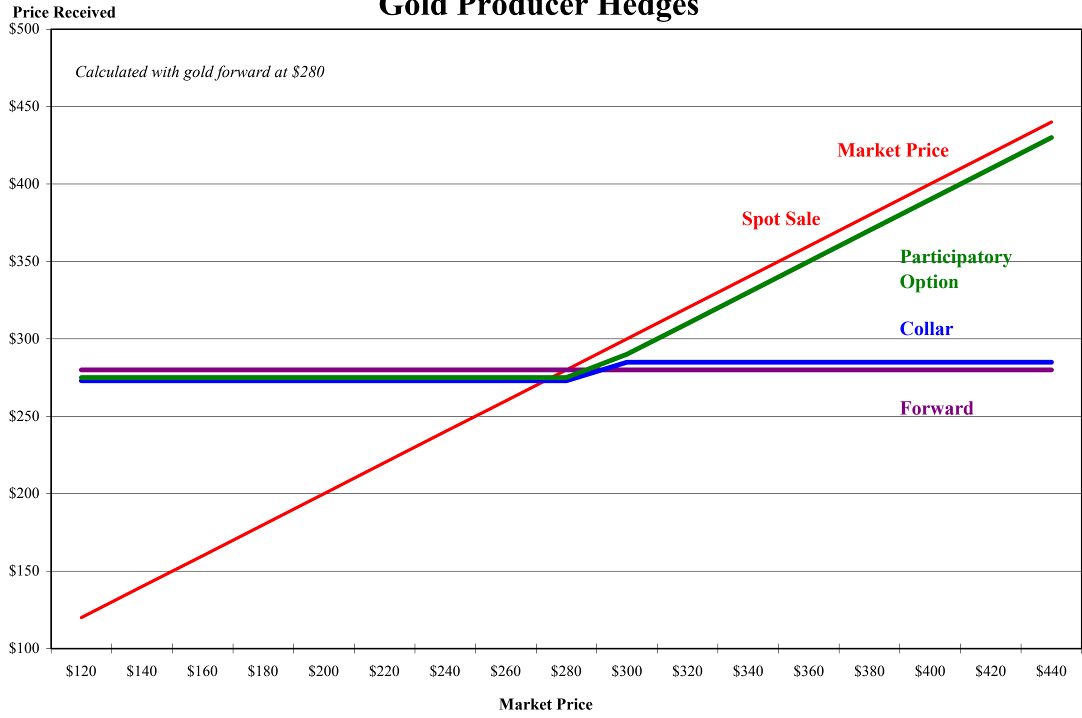

Gold Producer Hedges
Price Received
Calculated with gold forward at $280
$500
$450
$400
$350
$300
$250
$200
$150
$100
Market Price
Spot Sale
Participatory Option
Collar
Forward
$120
$140
$160
$180
$200
$220
$240
$260
$280
$300
$320
$340
$360
$380
$400
$420
$440
Market Price