

**Today's Notes:**

**1. Endeavour Silver (Chris Berry, MBA)**

Last week, Vancouver-based Endeavour Silver (EDR:TSX, EJD: Frankfurt, EXK: NYSE-AMEX) hosted a group of analysts (yours truly included) on a mine tour of their Bolanitos mine in Guanajuato, Mexico. This trip was a first-hand opportunity to meet with senior management, get a feel for how the operation is run, and witness a company executing a plan to achieve their goal of becoming a mid-tier (5 to 10 million ounces per year) silver producer. I have always believed that there are two prerequisites for any mining investment. They are potentially world-class properties and world-class management. Endeavour Silver excels in each of these categories. A closer look at their business model and plans for the future cements this as a compelling investment opportunity. After yesterday's icy blast from the world's markets Endeavour looks especially cheap. We think it has held its value quite well.



Endeavour was founded in 2004 by Brad Cooke and Godfrey Watson, professional geologists with years of experience in mining exploration, financing, and development. The company is a silver / gold producer with an impressive track

record of five years of consistent growth in silver production and reserves and resources. The company has operating mines in Mexico (Guanacevi and Guanajuato), plans to increase production, and grow organically through acquisition. I like this stock for four reasons:

1. LOCATION: Endeavour's operating mines are based in two districts in Mexico, historically one of the top silver-producing countries on Earth. The Bolanitos mine is located near the Veta Madre, a famous silver belt. Hugh Clark Endeavour's Director of Corporate Communications describes the Veta Madre as "the backbone of the Spanish Empire" for the decades of wealth from created silver mining. The Cebada mine, located near Guanajuato is practically on top of the Veta Madre. Endeavour's Guanacevi mine, which we did not visit, is north of Guanajuato in Durango.
2. BUSINESS MODEL: Endeavour has pursued high-grade silver projects where permitting and mine building has already occurred. This saves time in achieving production and allows the company to keep cash costs down. This is not to say that the company disregards safety. Endeavour takes safety seriously – as evidenced by the shut down of operations in Guanajuato for five months in 2008 for repairs and upgrades. Additionally, the company believes in organic growth from their existing mines as well as acquisitions of strategic properties near their mines. A closer examination of recent acquisitions and mine expansion proves this and demonstrates the success of the business model. Endeavour plans to increase capacity at their Guanajuato plant from 550 tonnes per day to 800. This will increase recoveries and generate higher cash flows. Operating Cash flows can then be recycled to fund additional mine/plant expansion or strategic acquisitions.
3. RESERVES and RESOURCES: According to discussion with the company and a review of recent press releases, Endeavour has 2,025,000 tonnes of ore containing 13,574,000 ounces of silver, and 129,700 oz of gold in reserve/resource at Guanajuato.

The company has 3,833,000 tonnes of ore, containing 42,472,000 ounces of silver and 76,000 ounces of gold at Guanacevi.

Total reserves and resources include 56,046,000 oz of silver and 205,700 of gold. Incidentally, this translates to a "silver-equivalent" of 69,434,700 ounces. The company also has a high-grade silver project in Chihuahua called Parrall that has a completed 43-101 and adds indicated and inferred resources of approximately 2.5 million ounces of silver and 67,000 ounces of gold. The "silver equivalent" at Parall is 6,956,600 ounces.

One very important consideration is Endeavour's growth rate in reserves/resources.

The accumulation of reserves / resources will ultimately translate into increased production. This can be seen in the first quarter of 2010's production results. Endeavour reported a silver production increase of 34% to 766,210 ounces and a gold production increase of 62% to 3,775 ounces. Below I include my photo of silver concentrate from the Guanajuato processing plant.



4. **SILVER LEVERAGE:** This is a most important differentiator when comparing Endeavour to its peers. The company has focused on producing silver – viewing gold as a by-product in silver-equivalent ounces. As the price of silver increases, Endeavour becomes a much more valuable company. We think silver has significant upside from its current price level.

For example, using the silver resources numbers discussed above, we assume the 56 million ounces of silver that Endeavour has identified are economic. Management indicates that they achieve an 85% recovery rate. This provides a potential for 48 million ounces of production over twelve years. The company indicates that cash costs of production should return to the norm of about \$5.50 per ounce. So with silver trading for about \$17+, the operating profit per ounce to Endeavour is ~\$12.00. On this price basis Endeavour's silver yields an undiscounted profit of \$580 million over the next decade.

To estimate a current share valuation for Endeavour we used an average silver price of \$15.50 silver over the twelve year production horizon of 4 million ounces of silver per year, Endeavour's likely average annual production. The present value of this scenario is approximately \$245 million on an undiluted basis or about equal to its current market capitalization.

Even at \$15.50 silver there is significant value creation for EDR shareholders and significant free cash flow. However we believe that silver has a higher average price potential going forward over the next decade. At the current level of \$18.00 silver, Endeavour's Net Present valuation soars to ~\$300 million, well above its current market capitalization.

Please bear in mind that this is an approximate NPV calculation based on a discount rate of 10%, 4 million silver ounces produced annually for twelve years, taxes of 30%, management's estimate of necessary capex and long term average cash costs of \$5.50 per ounce. On the other hand the analysis does not recognize Endeavour's upside potential for expanding resources in its current mines through exploration or acquisition. The current market cap of Endeavour is ~\$240 million on an undiluted basis. We think the shares are undervalued. Endeavour could be a very interesting target to a larger silver company such as Coeur or Hecla.

There is much more to know about this discovery company (2010 drilling plans, mine development, acquisitions, and resource discovery potential from exploration). I will be writing in more detail soon.

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