

## Kaiser Bottom Fishing Report

### John Kaiser commentary – June 26, 2008: Avalon gearing up to conduct Thor Lake metallurgical studies

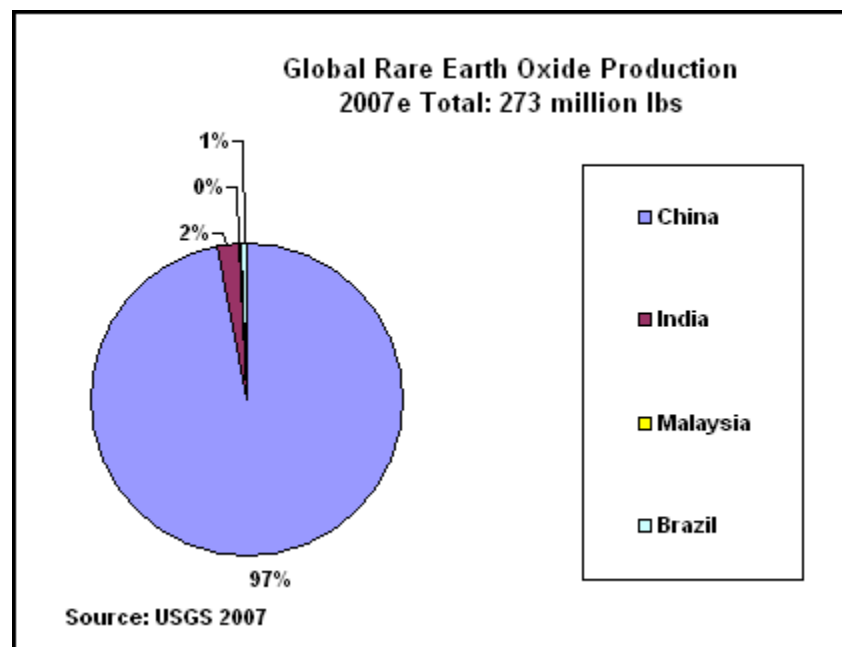
**Avalon Ventures Ltd** has resumed drilling on its Thor Lake rare earth project in the Northwest Territories after a 3 week break for spring thaw. The company has completed 45 core holes representing 8,724 metres, of which 11 holes representing 2,277 m were recently drilled south of Thor Lake on the land-based part of the Thor Lake system. These holes will form the basis for a new resource estimate in Q3 of 2008. Drilling so far has identified several laterally extensive, gently dipping horizons to a depth of 200 metres, with the 10-59 metre thick "Basal Zone" yielding the best total rare earth oxide (TREO) grades (1%-4%). What is special about the Thor Lake system is that 10%-30% of the TREO grade is comprised of heavy rare earth oxides (HREO), which includes the elements europium through lutetium plus yttrium. These numbers do not easily translate into rock value terms, but if we take the grades reported for terbium, europium, dysprosium and yttrium in a 12 metre interval in the Basal Zone from hole L0-89 highlighted by Avalon, and use the FOB China prices recently reported by Metal-Prices for these metals, those HREO's represent a rock value of \$290 per tonne. Avalon thinks it is on track toward establishing an underground mineable resource of 20-30 million tonnes of HREO bearing material, and if I connect the dots, and apply a rock value of \$100-\$500 per tonne to this resource, we are looking at a scenario with a gross metal value range of \$2-\$15 billion.

Avalon has received assays from only 21 of the initial 34 holes (up to L0-91), and when these are received the company will conduct a block model based resource estimate expected in September. **The resource estimate will be an important milestone because it will finally give us a proper basis for estimating rock values and gross metal value for Thor Lake.** The drill is now back at work on the south side of the lake for further definition drilling that will form part of an updated resource estimate in Q1 of 2009. The drill will later move to the western part of the Thor Lake system to follow up hole L0-89 referenced above. This was the westernmost hole drilled by Avalon, and the strength of the grade and total thickness (59 metres) of the Basal Zone in this sparsely drilled area surprised management. **News that rich and thicker HREO zones persist in the western part of this deposit could be a pleasant late summer surprise for Avalon shareholders.**

The real importance of Avalon's June 25 news release lay in details of its plans to deal with the most important milestone that still lies ahead for Thor Lake. The final 11 holes of the winter program were drilled to furnish material for metallurgical studies aimed at establishing how much of the assayed rare earths will report to a concentrate produced through conventional flotation processes. The commercial recoverability of the rare earth elements in Thor Lake is a critical milestone which Avalon hopes to have achieved by the

end of 2008. The rare earth elements are associated with the mineral fergusonite, a yttrium-niobium-tantalum oxide mineral. The Lake Zone was initially explored as a tantalum-niobium deposit during the late seventies, but the tantalum bearing mineral is so fine-grained that tantalum is not yet commercially recoverable. The current focus on the rare earth elements arose from the most recent failed attempt earlier this decade to solve the tantalum recovery problem.

Naturally there is some market skepticism that metals even more exotic than tantalum will not represent a recovery problem, so getting a green light through formal metallurgical studies that identify the most cost effective flow sheet will indeed be a big milestone for Avalon. At the moment SGS Lakefield Research is analyzing the mineralogy of the mineralization in the Basal Zone where Avalon has attained the highest grades for the lucrative heavy rare earth elements which are in short supply and play an important role in the super magnets used by hybrid cars such as the Toyota Prius. This will be followed by flotation testwork during which another shot will be taken at cracking the recovery problem for the niobium and tantalum which have significant grades in the Basal Zone. In fact, if I've done my calculations correctly, the niobium, tantalum and gallium grades reported by Avalon for the above 12 metre interval of L0-89 appear to represent a rock value of \$400 per tonne at current prices. **A metallurgical breakthrough involving niobium, tantalum and gallium would thus be a huge development for which the market is currently making no provision.** Once the flotation tests have produced concentrates Avalon will conduct hydrometallurgical studies to establish the best methods to separate the individual rare earth metals from the concentrate.



Avalon has been among my top recommendations, both as a bottom-fish back in 2005 when Avalon acquired Thor Lake, and last year when I recommended Avalon a Good

Absolute Spec Value Buy at \$1.76 on November 7, 2007. In early January I wrote a long commentary arguing that Barack Obama was emerging as a serious challenger to the Hillary Clinton machine as the Democratic nominee for the presidential elections this November. I suggested that Obama's message of "change" would incorporate footprint consciousness and the push for a green economy, which would be good for Avalon and the exotic metals in its Thor Lake project that are critical for hybrid cars. In early June Obama did indeed wrap up the Democratic nomination, but in the meantime Avalon's stock price had tanked below \$1.00 after the \$16.8 million financing done late 2007 came free trading. On April 2 I commented that with Avalon's stock chart looking like the price was falling off a cliff, and the market wringing its hands over the Bear Stearns fallout, small investors might want to wait for a bottom before stepping into the market, but big investors should step in immediately because Avalon would likely rebound sharply, creating a V-shaped bottom. Some big investors did indeed step into the market, and the stock is back above even my Spec Value Buy price of \$1.76. Obama's victory and the prospects of a booming Green Economy sector, however, are not responsible for the turnaround in Avalon's market. A much bigger factor has been the price of gasoline, which has soared past \$4 per gallon in the United States, and finally forced Americans to give up waiting for a pullback and get serious about fuel economy and alternative means of transportation.

In many parts of California there is a waiting list for the Toyota Prius, and, in defiance of the law that a new car depreciates 20% the instant you drive it off the car lot, used 2007 Prius's are now selling at their new cost and sometimes higher. It is no longer the case that the world needs hybrid cars; it is now the case that the world wants hybrid cars. And China controls almost the entire world supply of rare earth oxides. So if you are a car manufacturer in Japan, Korea or the United States, and you get it that consumers want a lot more hybrids than you are tooled up to produce, and scaling up your production capacity an order of magnitude puts you at the mercy of China and its agenda of being the manufacturing center of the world because China controls the world's rare earth oxide supply, what do you do? One of the slides in Avalon's corporate presentation features a photo of a group of forward-thinking individuals who visited Thor Lake last summer. No, it does not feature Eric Sprott, who much to his regret forward thought about Thor Lake during the eighties. And, no, it does not feature representatives from Detroit. It does, however, feature representatives of the group who joined Detroit in lobbying President George Bush to kill a state based initiative that would have allowed states like California to set their own fuel economy standards, and in doing so force Detroit to give the people what they want.

**The Absolute Good Spec Value Buy recommendation I made six months ago at \$1.76 remains intact, and I continue to believe that Avalon Ventures Ltd will turn into a blockbuster homerun.**