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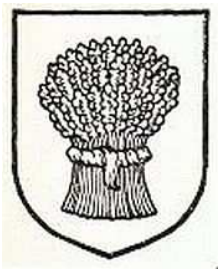

HALLGARTEN & COMPANY

Coverage Update

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Silvercorp (SVM.to, SVM:NYSE)

Diversifying Risk

Key Metrics		
Price (CAD)	$	12.74
12-Month Target Price (CAD)	$	14.50
Upside to Target		14%
12mth hi-low CAD	$6.21	-$14.89
Market Cap (CAD mn)	$	2,103.5
Shares Outstanding (mns)		165.1
Fully Diluted (mns)		168.0

	FY10	**FY11e**	**FY12e**	**FY13e**
Consensus EPS		$0.38	$0.52	n.a
Hallgarten EPS		$0.49	$0.63	$0.66
Actual EPS	$0.238			
P/E	53.6	26.0	20.4	19.3
Dividend	0.08	0.09	0.12	0.24
Yield	0.6%	0.7%	0.9%	1.9%

Silvercorp

Diversifying Away from China Risk

- + Production continues to uptrend and the company is aggressively bolting on acquisitions (at low prices)
- + The recent BYP acquisition makes Silvercorp, a small but growing gold producer and brings (from FY13) more base metals output
- + The company is moving forward fast with its Canadian silver property, Silvertip that will mine-ready within the next 18 months.
- + The GC property is also being moved rapidly towards production which keeps the upward momentum going in earnings with a particularly big step-up in FY14
- + The company has a very siezable cash position of over $220mn at the current time with capex requirements over the next two years that might, at a stretch, use up one third of that amount
- + A dividend payer, which potentially makes attractive to the heavyweight institutional audience
- ✘ Meritorious as the Silvertip move might be we wonder what relevance it has to shareholders who have followed Silvercorp for its China exposure
- ✘ We remain bearish on Silver, which we regard as vastly overpriced at current levels.
- ✘ The valuation is a tad rich at current levels thus limiting the immediate upside

Stepping up as the flagship

The disappearance from the scene of Sinogold has made Silvercorp Metals the major foreign-listed China-only mining player. This categorisation may soon also be shed if the company's ambitions to become a producer in Canada bear fruit. This prominence is not merely by default as the company is China's largest primary silver producer in its own right.

The company is a TSX- and NYSE-listed primary silver producer with mining, development and exploration projects located in the People's Republic of China.

Dominant or domineering?

China is one of the world's great mining nations, indeed in a number of metals its dominance is almost total (Rare Earths, Tungsten, Antimony for example), and in others its role is key, not as a dominant producer, but as a leading processor, a good example being in the production of electrolytic manganese.

Precious metals extraction is one of the very few mining activities where the Chinese have given clear signs that they are amenable to foreign mining companies participating in the activity. Other metals have overt, or tacit, prohibitions on non-Chinese companies operating in their extraction.

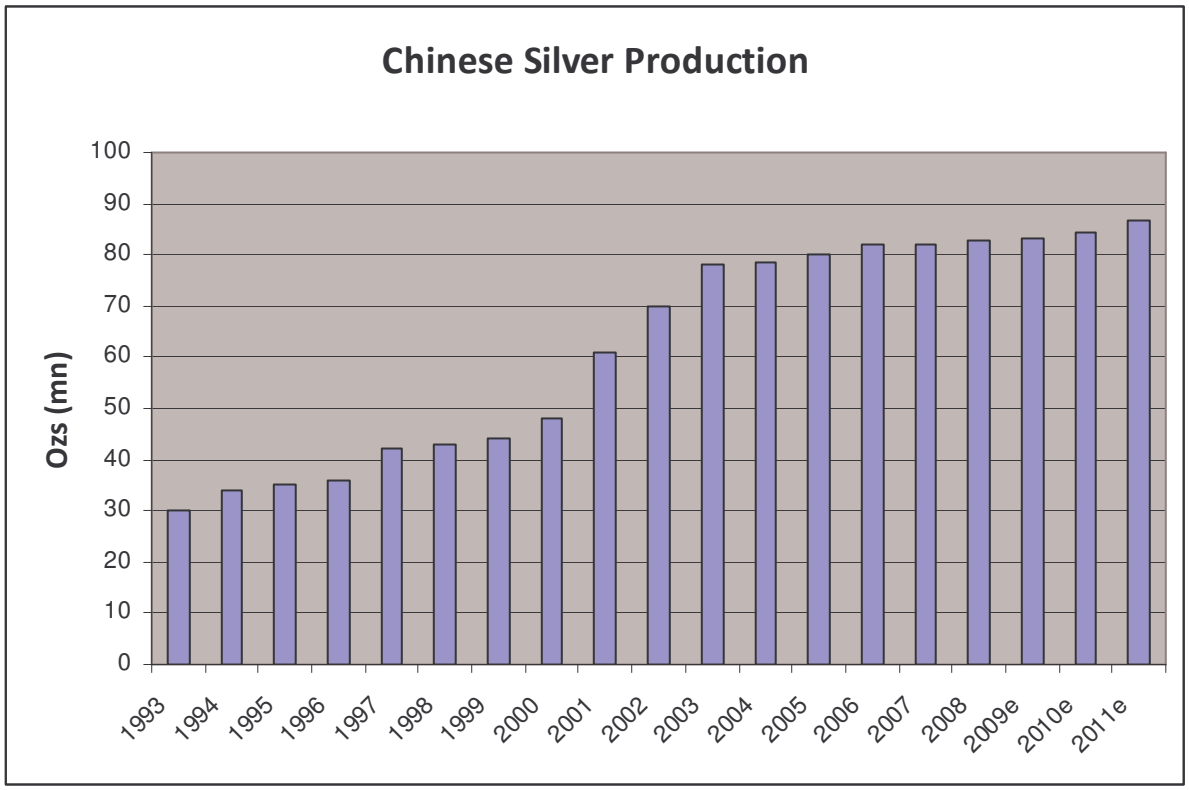
Recent years have seen China go from being resource self-sufficient (and an exporter) in a number of key metals to being a frantic importer (and moreover stockpiler). An important sea-change in Chinese thinking has occurred in recent years. For a good while after the 1970s opening of China to the West the prime category of exports from China was raw materials. Textile and other quotas in the West long blocked the type of low-cost value-added export categories in which China could compete. However over the last 15 years as the rise of the WTO and globalisation of industrial activities has eroded tariff walls China has moblised its low-wage workforce to conquer world-markets.

The "raw material phase" of Chinese exports (which we might tentatively pin down as the late 1970s until around 2005) overlapped with the "industrial phase" which began in the late 1980s and is now running at full flood. Eventually the needs of the domestic market (or moreover the use of Chinese raw materials as their own source of intermediate goods) choked off the flow of exports in metals and brought about the rising tide of imported metals.

Chinese Silver Production

While China's rising status as a gold producer is often noted, its rapid rise is the silver production stakes in not so well known. This is particularly relevant as most of the major accessible plays (which we shall discuss further on) are silver-, rather than gold-oriented. Having a major zinc industry also implies strong silver by-product credits by its very nature. The main provinces for silver production are Hunan, Henan, Yunnan and Jiangxi.

The top four producers in 2008 were Yuguang Gold and Lead Group, Yunnan Copper, Xinda Silver Industry, Chenzhou City Jingui Silver Industry.



Again we see that despite being the third largest silver-producing nation, China's silver production comes principally from a considerable number of small mines as opposed to a few large ones. High fragmentation is the norm, with none of the top 20 silver producing companies operate in China, and none of the world's top 10 silver producing mines are in China. Approximately 162,000 ounces of silver was mined in 1949 and 15 million ounces in 1980. The annual output of silver reached 36 million ounces in 1995 and now stands at 82 million ounces as of 2007.

In 2008, there was no significant change in domestic Chinese silver consumption compared with 2007. The consumption reached 4,500 tons. This was after a prolonged period in which growth rate of consumption exceeded 10% per annum.

While 2009 statistics are not yet available, output of Chinese silver in 2008 ranked the first in the world with 9,587 tons, an increase of 5.45% YOY. The growth rate decreased compared to the annual growth rate of over 20% in the previous five years. The Silver Institute estimated production at 82.8mn ozs in 2008, placing the country third behind Peru and Mexico.

In 2008, the export quota on silver was 4,800 tons. On August 1st, 2008, the 5% export rebate was eliminated. Affected by rebate elimination and prices decrease, export volume was 4,043 tons, 441 tons less than in 2007, and well under the quota. The dramatic rise in exports (and imports) is shown in the table below.

	2000	2001	2002	2003	2004	2005	2006	2007
Exports	10,008,444	11,129,569	14,366,412	18,978,986	23,915,096	47,427,847	128,983,041	204,433,212
Imports	6,751,298	43,223,291	78,109,865	104,424,704	125,546,193	150,943,366	166,203,503	164,976,404
Net Exports	3,257,146	-32,093,722	-63,743,453	-85,445,718	-101,631,097	-103,515,519	-37,220,462	39,456,808

Source: Silvercorp

Silver powder import increased to 1,511 tons in 2008, rising by 54.34% YOY. Import of silver concentrate reached 70,100 tons, declining by 62.84% YOY.

Pick and Choose Your Battlefields

A key factor to divide the waters on any discussion of mining investment into China is to separate precious metals from the industrial metals (base metals, specialty metals, Rare Earths etc). The Chinese do not seem preoccupied by foreigners exploring for and exploiting the former. They are very focused on policy towards retaining control of the latter though and thus discussion of the industrial metals in China is best left to pundits and political strategists.

China is a great mining nation and has been for thousands of years. One of the reasons why foreigners may not be getting much traction in exploring China is that they don't actually bring all that much to the table. China knows very well where most of the mineral potential of its own territory lies. It has spent decades poring over the geological possibilities in a systematic way and millennia exploring and exploiting mineral resources in the more basic ways that preceded the Industrial Revolution. China did not get to be the world's second largest gold producer by starting five years ago with the "comfort of strangers".

With nothing especially new to offer technology/skills-wise, a language barrier to navigate and fairly primitive fundraising markets (yes, we mean Toronto), there is no reason why foreigners should be ahead of locals in the race to Chinese mineral resources.

However, when it comes down to it, mining companies have to stand or fall on their own merits (and that of their mines) not upon the perceived fashionable status of the market in which they happen to be operating. No Chinese precious metal mining story is a consumer/growing GDP story. The price of silver or gold is essentially the same whether mined in Peru, China or Australia. The cost of doing so though may differ greatly and China definitely has a cost advantage over Western economies, though not necessarily over lower wage locations such as Peru.

Country risk is still an important factor. China has been hard going for foreign non-precious miners. If there is any sign that the precious metals miners also are going to be pressured then this country may be put into the "too hard" basket for many investors. Nevertheless a new accommodation seems to have been reached where the players left tend to be run by Mainland, Hong Kong or Overseas Chinese. This seems to help them navigate the passages of power. For foreign miners though that is like saying a miner operating in Mexico needs to be run by a Mexican to have a chance of success or Randgold would need to be run by a Malian. This is patently unworkable at a global scale, but it is seemingly what Chinese "inward" mining investment has devolved into.

Seemingly China is ruling itself off limits for anything more than precious metals miners. This is not enough potentially to deflect criticism that China wants to secure everyone else's industrial metals and wants to keep its own for itself. This complaint will be heard louder and louder in coming years. Thus the investor community are probably best at restricting their China mining forays to companies like Silvercorp for it seems to have passed the test of time (and politics).

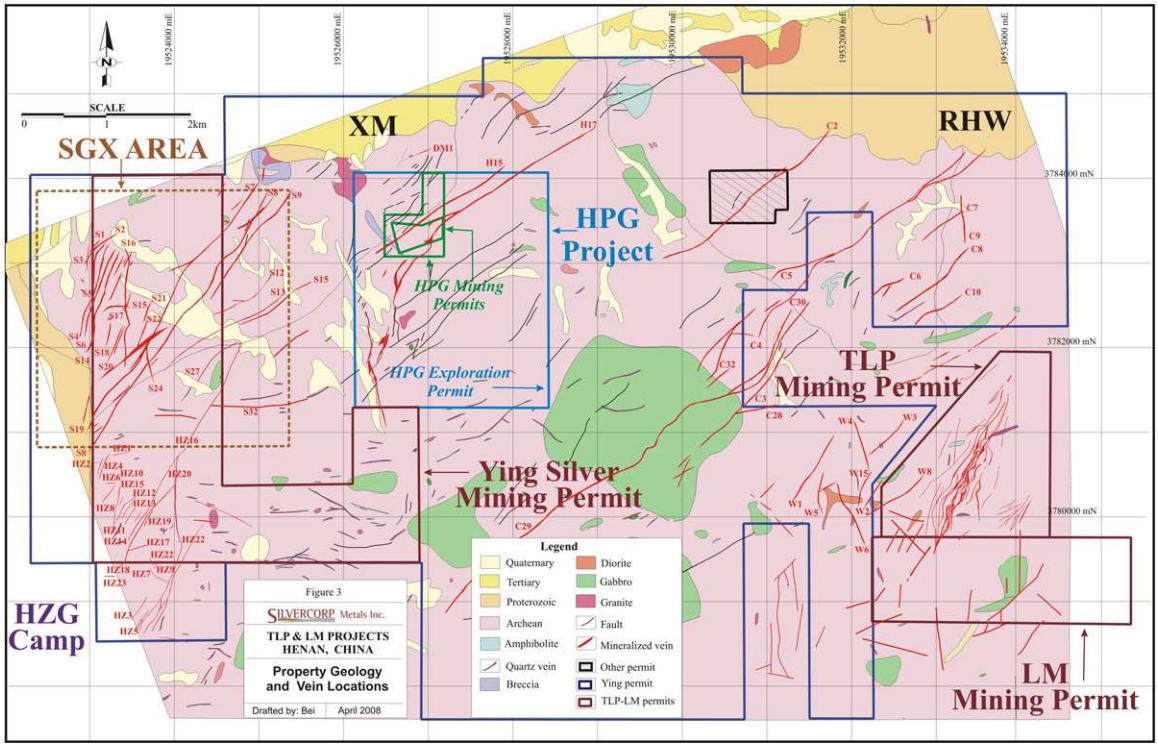
Silvercorp's Chinese Mine Portfolio

The company's asset array consists of both production and exploration assets. The former have been located, up until now, in the central province of Henan. The production asset is located in the Ying Mining District, located near the county of Luoning approximately 240 km southwest of Zhenzhou, the capital city of Henan Province. In March 2004, Silvercorp acquired its flagship Ying silver-lead-zinc project, which came into production in 2006. Later, in 2007, it bolted on, via acquisition, three other adjacent projects (the HPG, TLP and LM mines) in 2007.

The Ying Mining District

This district lies in the Quinling Orogenic belt formed when the Yangtze and the Northern China Plate collided in the Palaeozoic period. The tectonic collision resulted in a number of deep-seated structural thrust faults and shears that provide a host for most of the mineralizing event. The structural event has resulted in widespread silver, lead and zinc mineralization as well as gold in some areas. Although high-grade mineralization has been known for hundreds of years, many areas remained under- explored and untested.

Property Geology and Vein Locations



The zone that has been intermittently mined over the last several hundred years, largely by artisanal miners. Since 1956, extensive geological mapping, airborne magnetic surveys, stream sediment geochemical surveys, local IP surveys and trenching were conducted in the area by provincial geological bureau teams, culminating in the establishment of resource estimates in late 2003 with Silvercorp moving in to secure its position shortly afterwards.

Mining Operations at Ying

The company's four mines in the district are held in two Sino-Foreign Cooperative Joint Venture companies. The flagship Ying Mine and the TLP Mine are held by Henan Found Mining Ltd., owned 77.5% by Silvercorp and 22.5% by the Henan Non-Ferrous Geological & Mineral Resources Co. Ltd. (the local quasi-government owned geological bureau). Then the HPG Mine and the LM Mine are held by Henan Huawei Mining Co. Ltd., a Sino-Foreign Cooperative JV company owned 70% by Silvercorp and 30% by Luoning Huatai Mining Development Co. Ltd. (a private company). The minority interest number in the company's results (discussed anon) are the product of these JV partnerships.

Silvercorp owns and operates two flotation mills in the Ying Mining District. The first mill, with a capacity of 1,000 tpd, was built in 2006 at a capital cost of US$6 million and is currently processing ore from the Ying mine. The second mill, completed in December 2008, has a capacity of 1,500 tpd and cost US$12 million to build. Both are located 15 km by paved road from Silvercorp's mines and are supplied with power from the Henan Province power grid. Currently ore is transported from the mines over a ridge to the processing facilities. The company has been considering however the possibility of putting in a conveyor tunnel between Ying and the mill complex.

The processes used in the mills are typical of polymetallic Pb-Zn ores. There are two stages of ore crushing, from 400 mm to 15 mm, followed by ball milling such that 70% of the material passes 200 mesh (74 microns). The minerals are then separated by a series of flotation circuits, producing a lead concentrate (carrying the silver) which averages 69% lead, and a zinc concentrate which averages 52% zinc. The current capital investment program is directed towards expanding the mine production to 2,500 tpd (from 2,000 tpd) to match the milling capacity available. Thus mine infrastructure investment in FY12 is targeted at $13.8mn, while above ground expenditure (essentially at the mills and tailings facilities) will be $4.7mn.

The concentrates are of a high quality, containing very little arsenic (less than 0.001%) or other penalty elements. Metal recoveries to date have averaged over 96% for lead, 93% for silver and 76% for zinc. The silver and lead recoveries exceed those expected from the design specifications. The concentrates are currently being transported via trucks to custom smelters located 70 to 190 km from the mill site.

In the third quarter results for FY11 (i.e. December quarter) the company provided full year guidance with relation to Ying (which provides 90% of group profits) of a 13% increase in silver production to 5.3 million ounces with production from the TLP, HPG and LM mines continuing to grow as mine development progresses. The company's production plan was to produce approximately 500,000 tonnes of ore at grades of 360 g/t silver, 8% lead and 1.2% zinc, yielding 5.3 million ounces of silver, 83.7 million pounds of lead and 10.3 million pounds of zinc.

Exploration Upside in the District

While Ying appears to be relatively mature as a district there is substantial scope for more work to expand resources. Silvercorp's holdings in the Ying Mining District also include eight exploration permits totaling 59.7 km2 and mining permits covering 16.86 km2. The exploration budget for FY12 at Ying includes 75,000 metres of underground drilling at a cost of $3.3mn and 10,000 metres of surface drilling at a cost of $1.2mn. The lesser deposits will have around another 90,000 metres of drilling (all underground) at a cost of $4mn. Most of the latter is directed towards finding extensions to the currently mined orebodies. The surface drilling at Ying though will be directed towards some territory that is currently not subject to mining. The company offers the interesting statistic that historically extra drilling has tended to add around 110 ozs of silver (or nearly $3,700 in gross revenue value) for every metre drilled. With the underground drilling at Ying costing around $44 per metre that makes a compelling equation.

The goal here is to extend the current mine life of ten years (hopefully by 3-4 years).

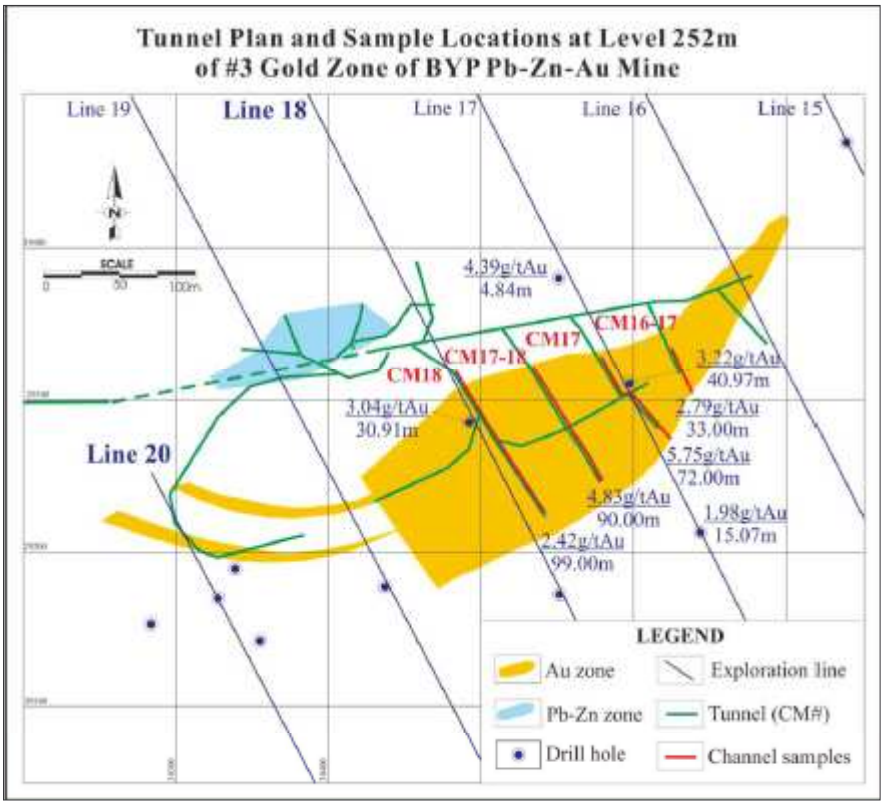
The BYP deal – more China in the mix

While the company's pursuits in the last year seemed to signaling a rebalancing of Silvercorp away from China a surprise transaction in early November 2010 reversed this trend when Silvercorp announced that it had signed a share purchase agreement and a Sino-Foreign cooperative joint venture contract to acquire a 70% equity interest in Yunxiang Mining Co. Ltd. a private mining company in Hunan Province. The cost of the share purchase and the Joint Venture capital investment is approximately US$33 million for Silvercorp, so not overly challenging in capital. The vendor of the majority stake was a consortium of

real estate investors that had got itself involved in something that may have appeared easy at first blush but was clearly more difficult than imagined.

Yunxiang's primary asset is the BYP Gold-Lead-Zinc mine, located 220 km southwest of Changsha, Hunan's capital city. It has a mining permit covering 3.67 km2, a safety production permit, and a 400-tpd flotation mill. The mine and mill has been in production since 2006 and has mined and processed about 300,000 tonnes of "lower grade" lead-zinc mineralization near the surface. No other historical mining and milling activity occurred within the mining permit area.

The mine is capacity constrained with the mill currently not in operation due to the tailings pond being full. A new tailings facility is under construction and is expected to be completed around the end of 1Q11. The mine and mill are easily accessed by paved road and are serviced by the national power grid. Over 4,100m of underground development is completed, including four declines totaling 767m and 2,010m of exploration drifts (shown in green in the plan view below).



At present, gold mineralization (the orange shading) is accessible by underground tunnels at the 252m elevation, about 100m from surface. As the Pb/Zn deposit (the blue shading) is separate from the gold-bearing mineralization the company's plan is to reactivate gold mining in the short term and then they mining shall be extended to the base metal zone.

Silvercorp intends to utilize the existing 400tpd flotation mill to mine and process the gold mineralizations starting from fiscal 2012. Concurrently, Silvercorp will expand the mining and milling capacity to 1,000 tpd gold mineralization for fiscal 2013 then to 2,000 tpd (1,000 tpd gold mineralization and 1,000 tpd lead-zinc mineralization) by fiscal 2014.

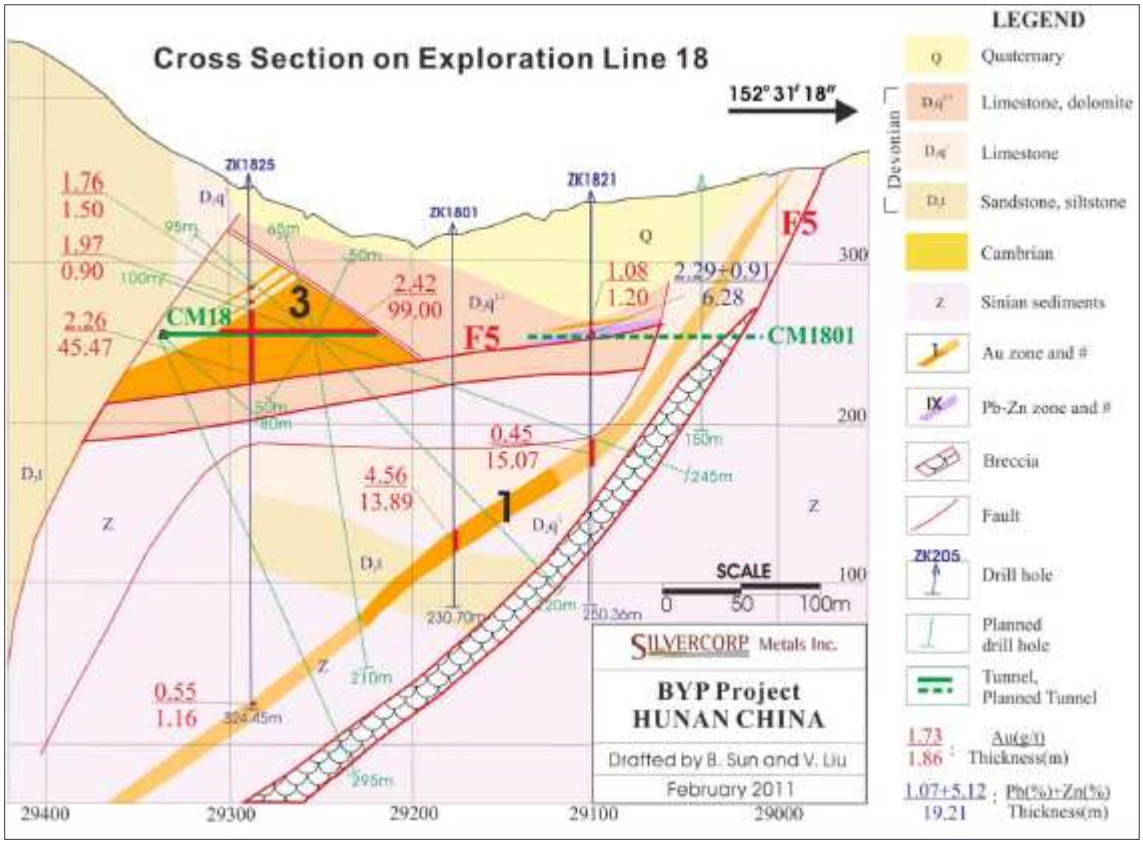
Within 200 km there is one gold refinery and seven lead & zinc smelters with ample capacity ready to take these concentrates.

BYP – Geology & Resource

Not unsurprisingly the new asset does not come with a NI 43-101. A geological report on the property was completed by the Chinese government geological team in 1992. Based on 36,151m of diamond drilling in 105 holes, the report defined:

- 5.44 million tonnes of gold mineral resources grading 2.76 g/t Au,
- Containing 482,000 ounces of in situ gold, and
- 3.12 million tonnes of "higher grade" lead and zinc mineral resources grading 2.45% Pb and 5.26% Zn.

This resource does not measure up to NI43-101 standards as a "qualified person" has not done sufficient work to classify the historical estimates as current mineral resources, and thus Silvercorp is not treating the historical estimates as current mineral resources.



Geologically, the project area is underlain by Devonian limestone, mudstone, and sandstone units that were intruded by Mesozoic granites within the prominent Central Hunan gold-tin-lead-zinc-antimony polymetallic belt. Gold mineralization up to 41m in true thickness as defined by surface drill holes occurs in the sandstone while lead and zinc mineralization zones up to 53m in true thickness are hosted in the limestones. Gold mineralization is mainly related to fine quartz veining and disseminated pyrite developed along joints and fractures in sandstones. Lead and zinc is usually very fine-grained and is associated with silicification and pyrite in limestone. Gold, lead and zinc mineralization zones appears

from surface to a depth of about 350m based on the deepest drill holes. As drilling to date has been widely spaced (100m to 400m between holes) it is possible that additional mineralization will be proven through future extensive exploration of underground tunneling and closely spaced diamond drilling, as the recent underground tunnels have intercepted several new gold and lead-zinc mineralization zones.

As part of the due diligence review, extensive gold mineralization defined by previous drilling was confirmed by Silvercorp geologists who carried out a systematic channel sampling program in four newly developed underground tunnels that cross-cut through the #3 gold ore (see table below).

Underground Channel samples

	Tunnel cross-cut interval (m)	**Gold grade (g/t)**	
CM 16-17	33	2.79	
CM17	72	5.75	(including 15.08 g/t over 12 meters)
CM17-18	90	4.83	(including 14.13 g/t over 9 meters)
CM18	99	2.42	(including 7.67 g/t over 6 meters)

Silvercorp will carry out an extensive exploration program to upgrade and expand the current resources. In the short-term it is undertaking a 50,000 m drilling campaign at a cost of $3mn. The goal here is to:

- upgrade the main #3 mineralisation zone,
- to extend alonmg strike and downdip of the F5 fault
- probe several orher gold and lead/zinc/gold mineralisations
- complete a NI 43-101 report on the project within 3-6mths (Wardrop have been engaged to do this)
- engage a Chinese engineering firm to design a full plan for mining development.

The target is to lift the gold resource to one million ozs.

Silvercorp has used a metallurgical laboratory in Changsha City to conduct metallurgical tests on gold and lead-zinc mineralization from the BYP mine. The preliminary test results and previous production records show that gold can be recovered at about 90% recovery rate by conventional floatation to produce a gold-sulfide concentrate. Lead and zinc can also be recovered by conventional flotation with 80% lead and 90% zinc recoveries.

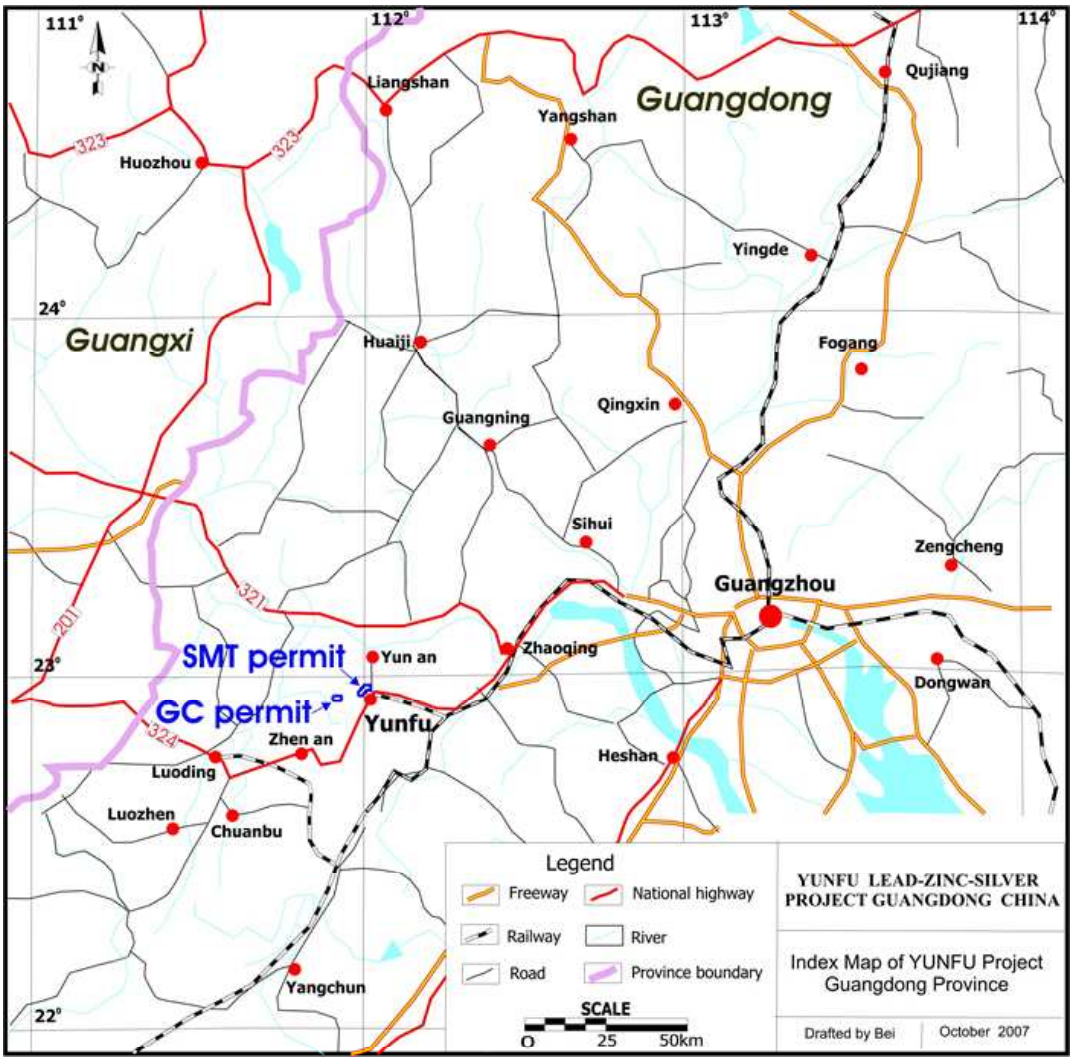
The production plan at the current time is to restart operations with the gold only at the rate of around 24,000 opa. The gold deposit will be high-graded at beginning with an average grade of 7g/t (compared to the resource grade average of 2.7g/t). The mill will then be expanded in increments to 1,000tpd and then 2,000 tpd. The company claims that gold production will only be 30,000 opa even with the higher throughputs due to the average grade veering back towards the deposit norm and a greater proportion of the output is base metals from FY13 when mining resumes in the lead/zinc part of the deposit.

However, if the Au resource is expanded to the one million oz level hoped for then we would expect that production of gold would exceed these humble targets.

GC – pushed back in the queue

The arrival in the portfolio of the BYP mine pushed GC into second place as the company's main development prospect in China. The Gaocheng and Shimentou silver-lead-zinc exploration permits (covering an area of 5.54 km2 and 9.49 km2 respectively) are located about 200 kilometres west of Guangzhou City in Guangdong Province (shown on the map on the next page). These are known as GC in the company's practice of abbreviating Chinese project names to acronyms. Since 2001, the permits have been explored for gold, silver, lead, zinc, and sulphur.

The two exploration permits are 100% owned by Anhui Yangtze Mining Co. Ltd., a Sino-foreign cooperative JV company owned 95% by Silvercorp (through a wholly owned subsidiary). It acquired these in April 2008 at the not unsubstantial cost of approximately US$60mn for an exploration property. This was composed of 40% (US$24mn) in cash and 60% in common shares of Silvercorp (4,532,543 common shares at CAD$8.20 per share).



History

Since 1959, extensive systematic geological mapping, airborne magnetic surveys, stream sediment geochemical surveys, local IP surveys and trenching were conducted by provincial geological bureau teams. From 2001 to 2007, a total of 16,819 metres of diamond drilling in 53 drill holes and 13,630 cubic metres of trenching were completed on the properties. Some 13 silver-lead-zinc mineralized veins were identified within an area of 3km long on NW by 1.5km wide on NE. Five mineralized veins are dominant, accounting for approximately 86% of known mineralization, with one vein accounting for approximately 48% of known mineralization. This vein has been outlined along strike for 1,255 m and at down to 466 m depth with thickness ranging from 0.39 m to 9.69 m grading 7.45 g/t to 968g/t silver, 0.03% to 6.81% lead, 0.01% to 10.61% zinc and up to 0.56% tin.

A NI43-101 independent technical report completed by SRK Consulting China Ltd was released in April 2008.

Resource for GC deposit

		Grades			Contained Metals			
	Tonnes	Ag (g/t)	Pb (%)	Zn (%)	Ag (oz)	Pb (t)	Zn (t)	Ag Equiv. (oz)
Measured	374,000	233	1.83	3.19	2,797,000	6,850	11,920	5,383,300
Indicated	6,034,000	132	1.47	3.35	25,690,400	88,710	202,230	65,779,900
Inferred	7,892,000	121	1.45	2.7	30,774,200	114,570	213,380	75,962,400

The silver resource is impressive and indicates that the project may indeed add another leg to the Silvercorp story. Hopefully further work will move more of the Indicated resource into the Measured category. The company initially applied for a mining permit on the GC deposit using the resource estimate done by the Guangdong Geological Survey Institute (GGSI) in 2007 that has been accepted for filing by the relevant Chinese government authorities.

Subsequently, Silvercorp completed a 22-hole, 10,083-meter drill program in 2008, the results of which were incorporated into an updated NI43-101 technical report on the GC Ag-Zn-Pb Project by AMC Mining Consultants Canada that dates from June 2009. The mineral resource was calculated using a 150 g/t recovered Ag Equivalent cut-off. Ag Eq is calculated using US$12/oz Ag, US$0.75/lb Pb and US$0.75/lb Zn.

Development

Silvercorp has completed the environmental permitting process for GC. This process was initially slow as the company was awaiting new environmental regulations compiled by the authorities in Guangdong Province. The new regulations were a response to heavy metal discharge concerns due to several environmental incidents around China in 2009. The company is currently constructing a 1,500 tpd mine and mill. Capex in FY12 will be of the order of $22.5mn (of this the largest portion will be $12mn for the mill construction and tailings dam). It is expected that Capex for FY13 (including around $3mn for ramp

extensions from 1,500 metres to 4,600 metres) will be funded out of cashflow from the early stage production.

Initially production will be of the order of 700 tpd (by the end of FY12) with expected production of one million ozs of silver at that daily run-rate. The mining cost is estimated to be around $25-30 per tonne. When full capacity is achieved (sometime in FY13) the output will be around 2mn opa of Ag and 40mn lbs of lead and zinc. This would give gross revenues of over $120mn per annum at current prices for those metals. The mine life is estimated at around 30 years on the current resource.

As far as the latest resource numbers are concerned, with the weighting towards Indicated rather than Measured, we somehow doubt that Silvercorp needs to prove anything to the market or regulators before it might move forward on this in light of its own strong cashflows and the potential for it to finance any expansion through sources in China.

GC will receive around 20,000 metres of surface drilling, at a cost of $2.5mn, during FY12. This will be focused on a vein that surface outcrops for over 1,500 m, but which has only had four holes drilled into it in the past. The campign will also pursue several Ag/Pb geochem anomalies and undertake some infill drilling in the main zone. At the Shimentou permit, Silvercorp has defined six mineralized veins with strike lengths of between 300 m and 1000 m, defined depths of 100 m to 500 m, vertical thicknesses of up to 7.59 m and grades of up to 344 g/t silver, 8.87% lead, 7.45% zinc, 1.44% tin and 1.79 g/t gold. No NI43-101 resource estimate has yet been established for the Shimentou Permit area and we have not been told of any worked planned there for the immediate future.

Outside China

Several years ago with China-focused miners out of favour (maybe rightly so), Silvercorp struck out to rebalance its business to a broader geographical base. To this end it launched its abortive bid for the wily Klondex and then more recently it secured the Silvertip mine in British Columbia that is now moving towards production.

The Takeover Offer for Klondex

On June 8th 2009, Silvercorp launched an offer to acquire all of the outstanding common shares of Klondex Mines (KDX.to). Its flagship property is Fire Creek in North Central Nevada where it held at that time an NI 43-101 compliant Indicated Mineral Resource exceeding 1.6 million ounces of gold equivalent and an Inferred Mineral Reserve of over 500,000 ounces of gold. The shareholders of the target were offered 0.50 common shares of Silvercorp for each Klondex common share tendered to the offer. This represented a price of around CAD$2.18 per common share based on Silvercorp's closing share price (CAD $4.36) as at the 5th of June 2009. This represented a premium of 59% to Klondex's closing share price (CAD$1.37) as at June 5, 2009. The Silvercorp offer was scheduled to expire on July 21, 2009, unless it was withdrawn or extended.

Klondex is a notoriously tough cookie to deal with. Its response to this threat to its independence was to issue shares at a large discount to a "friendly" party, which curiously turned out to be a cooperative of Chinese mining entrepreneurs (though we heard they were actually real estate investors). At the time we indicated our disapproval of this action because of its discriminatory nature towards existing

shareholders. This was a quite blatant attempt to disenfranchise existing shareholders from their right to accept or reject the offer. We were one of the few though to publicly object to this action. Eventually Silvercorp's bid lapsed because in the interim Klondex persuaded Paramount Gold and Silver (PZG.to), a company that we had hitherto been partial to, to launch a competing bid on July 20th, the eve of the expiry of Silvercorp's offer. Once Silvercorp was off the scene, Klondex then turned on PZG, accused them of having misrepresented their own resource and pulled out of the deal with Paramount on the 24th of September 2009.

These shenanigans have left Klondex with a reputation for being radioactive, metaphorically speaking.

Pursuing Canadian assets

Clearly the setback with Klondex did not stifle the appetite of Silvercorp for non-Chinese mining assets because, in late February 2010, the company revealed that it had signed an agreement with Silver Standard Resources (SSRI) to purchase a 100% interest in the Silvertip advanced stage high-grade silver-lead-zinc carbonate replacement deposit system. Total consideration for the project is CAD$15 mn with up to 50% to be paid in Silvercorp common shares and the balance in cash. Further mineral claim staking by Silvercorp has increased the land package to approximately 800 km2.

The Silvertip property hosts an advanced-stage, high-grade silver-lead-zinc. The property covers 216 km2 just south of the Yukon border in northern British Columbia, Canada. The site is readily accessible by a 25-kilometre road from the Alaska Highway. The project was previously explored by various operators/owners from 1955 to 2000 with more than CAD$40mn in exploration work carried out, including 2,400 metres of underground tunnel development and 71,472 metres of surface and underground drilling in 491 holes. The most recent exploration work was carried out by Imperial Metals, which owned the project from 1996 to 2002. No exploration work was conducted by Silver Standard after they acquired the project in 2002.

Silvercorp commissioned a resource evaluation reviewing all available exploration reports and data and compiling a new geological model for the Silvertip project. This model includes exploration results from a 1999-2000 drill campaign designed to test geophysical anomalies discovered in the summer of 1999 by Imperial Metals. In that campaign, drill hole SSD-99-65 intercepted 31.4 metres grading 318.4 g/t silver, 5.52% lead and 8.65% zinc. Subsequently, in the winter of 2000, 22 underground diamond drill holes delineated the high-grade "65 Zone".

This latest NI 43-101 compliant resource dated February 19, 2010, including the "65 Zone" as well as significant drill hole interception readings as follows:

Silvertip 2010 Resource Calculation (Including exploration results up to and including the winter of 2010)

	Tonnes	Silver(g/t)	In Situ Contained Silver (oz)	Lead(%)	Zinc (%)	Gold (g/t)
At >200 g/t Silver Equivalent Cut-off						
Indicated	2,349,055	352	26,556,459	6.73	9.41	0.54
Inferred	459,896	343	5,069,380	6.18	9.81	0.23

At >400 g/t Silver Equivalent Cut-off						
Indicated	1,976,664	398	25,263,518	7.65	10.35	0.58
Inferred	357,713	413	4,747,390	7.50	11.05	0.26
At >1,000 g/t Silver Equivalent Cut-off						
Indicated	705,373	631	14,309,987	12.24	13.18	0.79
Inferred	120,569	739	2,864,647	12.99	14.59	0.51

*Silver Equivalent is calculated using metal prices of US$12.13/oz Ag, US$728/oz Au, US$0.804/lb Pb and US$0.847/lb Zn and metal recoveries of 69.2% for silver, 80.4% for lead, 84.7% for zinc and 50% for gold.
**The increase in the resource is mainly attributed to the inclusion of the "Zone 65" resource. The conversion of tonnes from the Inferred to the Indicated category is based on the drill-demonstrated continuity of the mineralization.

In light of the above, the company claims that "the Silvertip project ranks among one of the highest grade silver-lead-zinc carbonate replacement deposits in North America". We can see why Silver Standard with its focus on very large projects did not pursue this opportunity, but it seems strange that such an advanced (and long explored) asset should have been passed around for so long with so little progress.

Fast-tracking Silvertip

To our knowledge a mine plan is not extant but we would note the presence of a significant tunnel network at the mine that is a legacy of previous exploration efforts. Silvercorp intends to apply for a provincial Small Mine Permit for an operation with a capacity of under 75,000 tonnes per year. Once permitted, Silvercorp plans to start mining those high-grade pockets (those outlined in the resource using >1,000 g/t silver equivalent cut-off grades) that are already accessible from existing tunnels. The cash flows to be generated from these early operations will then be used to finance further exploration programs, a full feasibility study, a full mining permitting process, and future expansion of mining operations.

The first step will be to obtain the necessary permits to de-water the existing underground workings, which is expected to take approximately six months. Once obtained, an underground exploration program, which will include a bulk sample, exploration drilling and a geotechnical assessment, will be carried out.

Preliminary metallurgical testwork was conducted by CSMA Minerals laboratory in the UK back in 1998. These showed that with a lead concentrate grade of 65%, silver and lead recoveries are 69.2% and 80.4%, respectively, and a 61% zinc concentrate grade has a zinc recovery of 84.7%. Silvercorp will perform additional mineralogy study and a metallurgical test program to further increase metal recoveries.

A surface drill program was carried out over the summer months of 2010 where previous drill holes had intercepted extensive mineralized zones that were not included in the 2010 resource estimation as the drill holes were too widely spaced. Furthermore, several geophysical and geochemical anomalies located within five kilometres of the existing resource areas along the same shale-limestone contact zone previously identified to host high-grade mineralization will also be drill tested. The total capital expenditure budget for calendar year 2010 at the Silvertip project was approximately $4-5 million.

Financing

In December 2010 Silvercorp announced that it had closed a bought deal financing. To effect this transaction the company issued 9.2mn common shares at a price of US$12.70 per common share, for aggregate gross proceeds of US$116,840,000 million and total proceeds, net of underwriting fees, of US$110,998,000, including the exercise in full of the underwriters' over-allotment option.

The proceeds from the offering will be used to complete the acquisition of the BYP gold-lead-zinc mine in China, for development at the GC mine in China and development at the Silvertip property in British Columbia, and for general corporate purposes.

New Pacific Metals

It is also worth noting that Silvercorp has a sizeable stake (around 14%, though was over 23% in early 2010) in New Pacific Metals Corp (NUX.v). As such Silvercorp is the company's largest shareholder. The company's historical focus has been exploration and development of gold-polymetallic projects in China though now it is prioritizing its exploration on a gold project in the Yukon.

The Huaiji Gold Project is composed of two gold-polymetallic exploration permits referred to as "HNK" and "XSK" which are located in Guangdong Province's Huaiji and Guangning counties, about 180 kms northwest of Guangzhou, the capital city of Guangdong Province. The concessions have a total area of 160 square kms. The two permits cover two extensive gold, silver, and antimony stream sedimentary geochemical anomalies. New Pacific is currently drilling and tunneling to define mineable high-grade gold reserves at the HNK project.

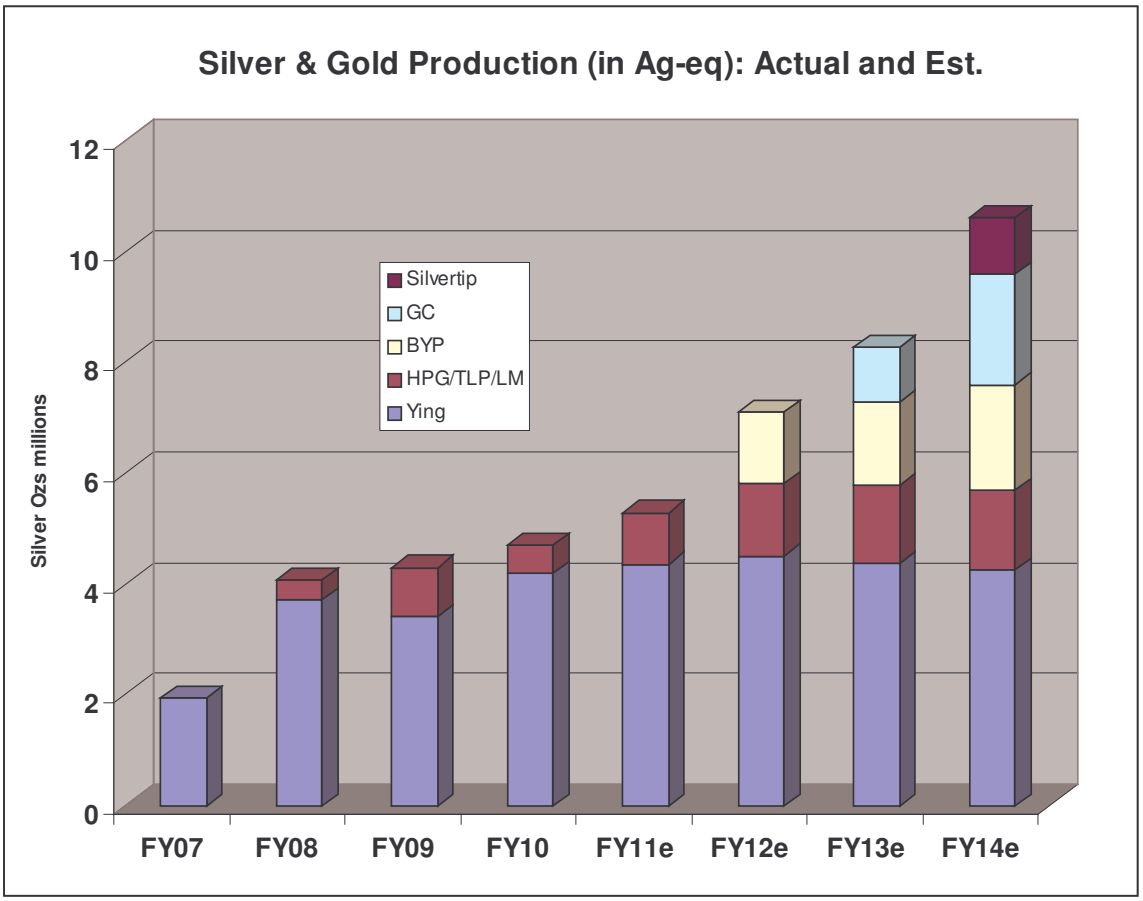
The company's market capitalization is currently around $116mn.

This stake is a perennial wildcard in the Silvercorp results as the larger company continues to mark-to-market the variations in the stakes value. This accentuated the hit from the 2008 meltdown and has positively bolstered Silvercorp's numbers as NUX has undergone a steady upward rerating.

Earnings Outlook

In its full year guidance provided in the third quarter results announcement the company said that, using the average metal prices during the fourth quarter and the above projected production figures, it expected it's mining operations in FY11 to generate revenues of $140 million, resulting in cash flows from mine operations of $95 million to $100 million.

The chart on the below shows the company's estimation of its production by volume and one can note that the advent of BYP significantly changes what would have been a couple of dull years coming up for Silvercorp as Ying (and associated mines) peaked and the company awaited GC and Silvertip for a bumper year in 2014. Now with the addition of BYP the outlook is for FY12 to be another year of substantial additions to production and thus a smoother upward rise in total Ag equivalent production.



It should be noted first that due to its March fiscal year end, the current fiscal year is that of FY2011. Thus the FY to which we refer closes in a matter of weeks.

In our earnings model for FY11 we are looking for:

- top-line revenues of US$177mn in the year shortly to end versus US$107mn in FY10
- gross profits of US$141mn and an operating profit of $113.6mn
- We have then factored in a gain of around $13.4mn, largely for the increase in value of the stake in New Pacific Metals
- This gives a post-tax and minorities result of US$81.3mn or EPS of 49 cts per share
- We would not be surprised to see a fourth quarter dividend of 3 cts per share taking the annual amount to 9cts

This rise has come about through a combination of higher silver (and zinc/lead) prices *vis-a-vis* the depressed levels (particularly of base metals) of the latter half of the previous fiscal year.

Silvercorp Production Summary FY2007 – current

	Year Ended	Year Ended	Year Ended	Quarterly Production Fiscal 2010				Year Ended				Year Ended
	2007	2008	2009	Q1	Q2	Q3	Q4	2010	Q1	Q2	Q3	2011e
Silver (millions of ounces)												
Ying	1.935	3.683	3.408	1.134	1.107	1.086	0.836	4.163	1.147	1.095	1.086	4.400
HPG		0.277	0.209	0.28	0.032	0.044	0.044	0.40	0.091	0.079	0.133	0.43
LM			0.301	0.007	0.007	0.089	0.125	0.23				
TLP			0.271	0.006	0.004	0.001	0.074	0.09	0.149	0.168	0.001	0.40
Total	1.935	3.96	4.189	1.175	1.15	1.22	1.079	4.88	1.387	1.342	1.22	5.23
Lead (millions of pounds)												
Ying	26.26	42.28	42.91	15.01	14.08	14.33	11.097	54.52	14.23	13.486	14.327	57.50
HPG		7.34	5.9	0.88	0.99	1.37	1.228	4.47	1.784	1.02	1.873	7.10
LM			1.32	0.1	0.09	0.51	2.219	2.92				
TLP			2.93	0.05	0.04	0.01	0.377	0.48	2.789	2.522	0.011	6.00
Total	26.26	49.62	53.07	16.04	15.2	16.21	14.92	62.38	18.803	17.028	16.211	70.60
Zinc (millions of pounds)												
Ying	7.14	15.14	12.34	3.58	3.71	4.04	2.747	14.08	3.605	3.275	4.038	13.30
HPG		0.76	0.62	0.16	0.1	0.42	-	0.68	0.209	0.06	0.416	0.80
LM			-	-	-	-	-	-	-	-	-	-
TLP									0.617	0.534	-	1.2
Total	7.14	15.91	12.96	3.74	3.8	4.45	2.747	14.757	3.814	3.869	4.454	14.10
Gold (ounces)												
Ying	249	309	72	-	100	200	300	600	500	200	200	1,150
HPG		1843	1,623	-	200	300	200	700	400	100	300	1,100
LM			103	-	-	-	-	-	-	-	-	-
TLP			82	-	-	-	-	-	200	-	-	200
Total	249	2152	1,880	-	300	500	500	1300	1100	300	500	2,450

In FY12 we are looking for:

- a 27% rise in revenues to $228mn largely driven by higher comparative prices in all metals (over FY11) combined with the onset of gold production from BYP
- This would result in enhanced operating profits (40% higher) of $152mn
- The pre-tax number of $158mn is only 20% better than FY11 as we cannot see a good reason to factor in further massive gains from New Pacific Metals stock price movements
- and net profits up around 25% to $105.67mn representing EPS of 62.5 cts.

Our outlook for FY13 is more subdued because we cannot envision silver prices holding up and GC shall only just start to make a contribution during that period. Thus we are looking for a very modest rise in EPS to 65.9cts per share. However, we do envisage the company raising dividends as capex requirements will be lower leaving the company in a bountiful cash position.

Silvercorp

In Millions of USD FY ending March	FY13e	FY12e	FY11e	3Q11	2Q11	1Q11	FY10	4Q10	3Q10	2Q10	1Q10	FY09	4Q09	3Q09	FY08	FY07
Total Revenue	237.02	228.00	177.91	51.84	36.34	36.73	107.16	28.224	31.28	25.09	22.57	83.52	17.39	15.17	108.36	42.79
Cost of Revenue	38.00	42.00	36.88	9.98	8.24	8.66	24.00	7.839	7.05	6	5.9	35.69	6.38	9.93	23.32	9.61
Gross Profit	199.02	186.00	141.02	41.86	28.10	28.07	47.84	20.385	24.23	19.09	16.67	47.84	11.01	5.24	85.04	33.19
SG&A Expenses	19.00	18.00	16.00	4.01	3.27	4.55	11.71	2.835	3.02	2.58	3.37	11.36	2.26	2.69	9.67	5.84
Exploration	7.00	6.00	3.80	0.06	1.11	1.33	4.91	0.702	0.94	0.96	2.31	2.33	0.5	0.2	1.82	0.87
Depreciation/Amortization	9.50	9.00	7.19	1.98	1.68	1.53	3.90	1.108	0.41	0.17	0.2	0.82	0.02	0.35	0.52	0.13
Unusual Expense (Income)			-0.20		0.38	-0.54	0.39	0.243	0	-0.08	0.78	50.71	2.91	47.43	0	0
Other Operating Expenses	1.00	1.00	0.60	0.04	0.46	0.04			0.03	0.03	0.03	0.12	0.04	0.03	0.06	0.07
Total Operating Expense	74.50	76.00	64.27	16.07	15.14	15.56	44.91	12.727	12.24	9.74	11.07	98.14	11.44	61.46	36	16.51
Operating Income	162.52	152.00	113.64	35.77	21.20	21.17	-14.62	15.497	19.04	15.35	11.5	-14.62	5.96	-46.29	72.36	26.28
Gain (Loss) on Assets held/sold	4.00	4.00	13.60	7.16	1.00	0.45	-1.96	-0.24	-0.24	-0.87	-0.26	-1.15	-0.31	-0.83	0.52	0
Net Interest (expense)	3.00	2.00	1.20	0.38	0.32	0.25	0.75	0.206								
Forex gain (loss)			-1.34	-1.34												
Other, Net	0.60	0.50	0.40	0.14	0.09	0.11	0.34	0.52	0.07	0.05	0.16	0.48	0	0.36	4.47	4.18
Income Before Tax	170.12	158.50	127.50	41.98	22.61	21.83	-15.40	15.359	18.99	14.54	11.56	-15.4	5.73	-46.53	79.69	32.05
Tax	28.35	26.42	21.97	5.10	5.61	3.25	8.56	2.135	2.68	2.35	1.39	-0.93	2.48	-6.44	0.56	1.53
Income After Tax	141.77	132.08	105.53	36.88	17.00	18.58	51.89	13.224	16.31	12.19	10.17	-14.47	3.25	-40.09	79.13	30.52
Minority Interest	-28.35	-26.42	-24.18	-7.15	-4.55	-4.48	-13.34	-3.464	-3.9	-3.3	-2.68	-1.53	-2.01	6.4	-19.2	-6.79
Net Income Before Extra. Items	113.41	105.67	81.35	29.74	12.45	14.10	38.55	9.76	12.41	8.89	7.49	-16	1.24	-33.7	59.94	23.72
Net profit	113.41	105.67	81.35	29.74	12.45	14.10	38.55	9.76	12.41	8.89	7.49	-16	1.24	-33.7	59.94	23.72
Diluted Weighted Average Shares	172	169	166	166.965	164.934	164.673	162.287	163.614	163.91	163.36	162.92	152.35	155	151.69	147.66	149.67
Diluted EPS	0.659	0.625	0.490	0.178	0.075	0.086	0.238	0.060	0.076	0.054	0.046	-0.105	0.008	-0.222	0.406	0.158
Dividends per Share	0.24	0.12	0.09	0.02	0.02	0.02	0.08	0.02	0.02	0.02	0.02	0.06	0.02	0.02	0.05	0

The only rain that could fall on this parade would be a revaluation of the yuan and inflationary tendencies. Conservative estimates are talking of a 4% move in the currency against the dollar in calendar year 2011. That would raise costs by an equivalent amount while revenues would remain tied to the dollar denominated silver price (which we feel is in danger of downward correction). A larger in the yuan though move is not out of the question, particularly as a means of dampening incipient inflationary trends, and would certainly be justified in light of the severe cumulative undervaluation of the yuan in recent years. The inflation adds a further twist with costs of workers on the move upwards while energy costs, namely oil inputs, are experiencing a steady rise in recent times.

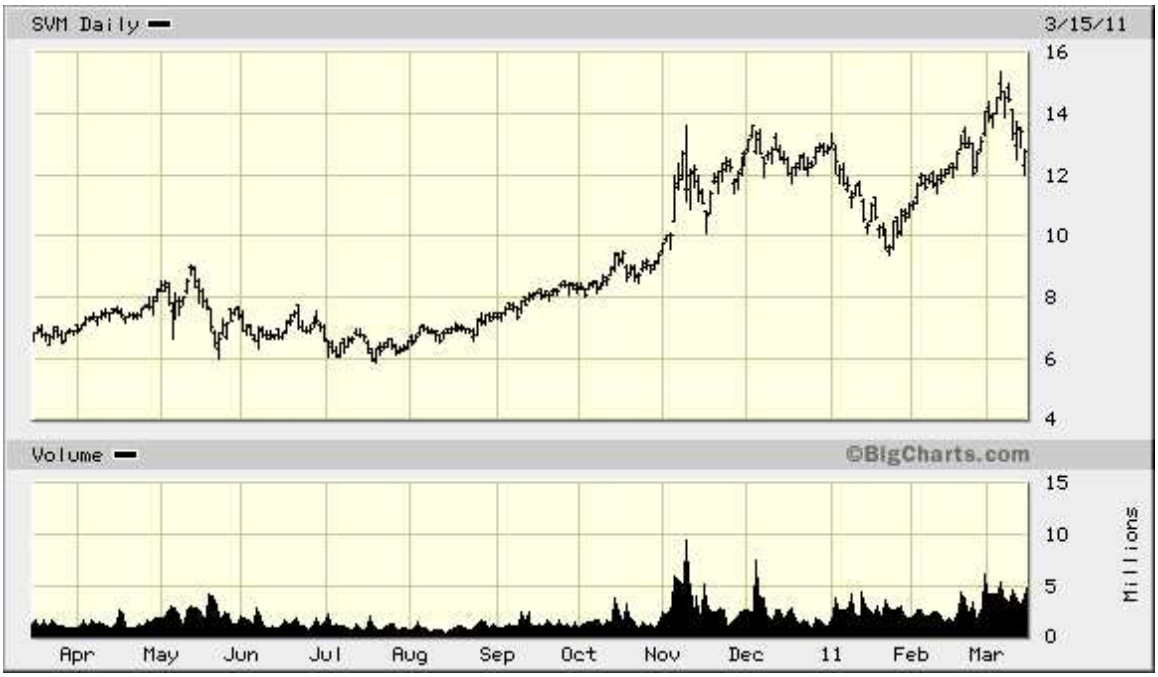
Conclusion

Silvercorp is seemingly doing everything right. In fact, too right, because its valuation is rather rich in our estimation. The ultimate dilemma for a miner in current times is that once the company has a P/E ratio and/or dividend yield, other metrics besides the mining industry's perpetual "trust me we have a great deposit" come to bear. There are plenty more expensive stocks in the mining space than this one but when regarding it is a serious alternative to the whole universe of industrial stocks, the P/E looks high and the company can afford to offer a higher dividend. There is no reason why any, but a dedicated mining investment fund, should not make cross-sector return comparisons.

As a mining company though, Silvercorp excels, with consistent growth in the past and the continual addition of further resources and production over coming years at minimal cost. The surest sign that this company is not of the Canadian mining school of thought is that it pays a dividend. That "fault" is then compounded by seemingly being committed to production. It's a wonder they aren't run out of Toronto for apostasy. On a more serious note we would wonder whether this isn't a company that London managers would seriously fall in love with if it had its listing on the London Stock Exchange, rather than Toronto and Wall Street.

The main drawback of Silvercorp remains that it is very expensive at the current time, but then again so are most silver producers. Even with the rising production, a stable to declining silver price means that the valuation is way out there with a P/E ratio of 26 times for FY11e and 20 times for FY12e. Beyond that one really needs to wait until 2014 for the next big pop in silver volumes to kick up the EPS by a meaningful amount.

The biggest danger to the silver miners is a retreat in the silver price. In this circumstance Silvercorp, while vulnerable due to high valuation, has considerably less downside than its peers due to the solidity of its earnings, its low cash costs and its dividend. To this must be added the consideration that its is amply cashed up and has relatively insignificant expenditure requirements on capex or exploration. This leaves us thinking that Silvercorp is a weak **Buy** with 12 month target price of $14.50 representing ran upside of only maybe 10% from current levels.


SVM Daily
3/15/11
16
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Volume
©BigCharts.com
15
10
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Millions
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