

**Metalline Mining Company  
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Metalline Shareholders:

Metalline completed a very significant step, November 15<sup>th</sup>, 2001, toward achieving its goal of becoming one of the lowest cost producers of zinc in the world with the signing of an agreement with Minas Penoles to continue the development of Metalline's Sierra Mojada Project. Metalline's Officers and Directors are extremely pleased to have Penoles as a partner and the operator of the Sierra Mojada Project. Penoles is one of the financially strong companies of **Grupo BAL** a diversified group of five Mexico based organizations: **Industrias Peñoles** (natural resources); **Grupo Palacio de Hierro**; (retail); **Grupo Nacional Provincial** (insurance); **Valores Mexicanos-Casa de Bolsa** (financial services); and **Credito Afianzador** (bonding). Grupo BAL has 23,000 employees, over \$4 billion of assets, and over \$2 billion dollars in sales.

Penoles has discovered and put into production 5 major mines in the last 10 years, an exceptional performance for the metals industry. The most recent being Francisco Madero Penoles' new 8,000 metric ton per day zinc, lead, silver and copper mine near Zacatecas, Mexico. Peñoles is Mexico's second largest mining company and the world's largest silver refiner. They operate Fresnillo; the world's largest silver mine, with proven and probable reserves over 400 million ounces silver. For the year 2000 Peñoles produced 298,300 ounces gold, 44.7 million ounces silver, 74,400 metric tons lead and 173,200 metric tons zinc. The Metals Division (MetMex) refined record amounts of gold and silver, 645,700 ounces gold and 74 million ounces silver. For the year 2000 Peñoles reported sales of 9,373,583,000 Pesos and assets of 17,113,584,000 Pesos. The present US dollar equivalent is \$1.02 billion in sales and assets of \$1.86 billion. Peñoles trades under the symbol IPOAF and their web site is [www.penoles.com.mx](http://www.penoles.com.mx).

Penoles is an extraordinary partner and offers many synergies for Sierra Mojada from their current operations. Penoles is building a 250 MW generation plant at San Luis Potosi for the Mexican National grid and consequently have guaranteed power available for their operations and for Sierra Mojada's requirements. High voltage electric power is available 80 km away at Hercules. Electric power is the highest cost component of the Solvent Extraction Electro-Winning process for producing SHG (99.995%) zinc.

Mexico's National power company, Comision Federal de Electricidad (CFE) has generation capacity of 36,100 MW. Mexican demand for the next 6 years will require 13,000 MW of new capacity, 36% of the current generation capacity and an investment of 250 billion pesos about US \$26 billion, which is 25% of the 1999 Mexican Federal Budget and equal to the education plus social security budgets ([www.energia.gob.mx](http://www.energia.gob.mx)).

Penoles has experience designing, building and operating hydrometallurgical zinc extraction and reduction facilities that may be needed at Sierra Mojada. MetMex, Penoles' metallurgical complex located in Torreon, has just completed a 90,000 metric ton addition, raising the annual zinc capacity to 220,000 metric tons. Met Mex produces 180,000 metric tons per year of sulfuric acid, an amount that may be used at Sierra Mojada when in production. This acid could be transported the 250 km (150 miles) to Sierra Mojada on the Coahuila Durango Railroad, which is jointly owned by and operated by Penoles.

At Sierra Mojada, channel sampling, percussion drilling and geologic mapping continue. Penoles is initiating an underground evaluation program consisting of raises, drifts and cross cuts through the mineralization, surface and underground drilling is also planned. Metalline is producing and selling high-grade white zinc ore, plus 38% zinc, for fertilizer use by an American manufacturer. The goal is to produce enough from the white zinc zone to pay for company overhead and generate a reasonable profit.

Metalline has signed an agreement with the B.O.W. Corporation of El Paso, Texas on their property in the Silver Hills District, Otero County, New Mexico. The property contains high-grade andradite garnet deposits that will be developed for the industrial abrasive market, primarily water filtration, sand blasting and water jet cutting applications. Evaluation of the deposit's quality and size are underway. The goal is to determine, during the next six months, if the quality and size of the resource can support a production decision for the deposit. If the evaluation results are favorable the goal would be to put a garnet production facility into operation in an additional twelve months.

For the zinc industry 2001 closed as one of the most difficult years ever, with metal prices at historic lows and increased zinc inventory on the LME (London Metal Exchange). Zinc prices are at the smelter's cost of producing zinc, \$0.35 per pound, and few mines are profitable. Prices cannot go or remain below the cost of production at the smelter or mines and smelters will have to shut down or reduce capacity to reduce inventory and force prices to increase. The majority of mines have operating total cash costs greater than \$0.50 per pound. Consequently prices will have to increase above \$0.50 per pound or these mines will have to close, restricting supply by up to 50%. This is currently happening, several mines have closed permanently due to exhaustion of reserves and others are operating at reduced capacity, are on maintenance status or closed due to depressed prices, at least 600,000 metric tons of zinc production has been removed from production in the last few months.

During 2001 zinc stocks on the LME increased from 250,000 to 450,000 metric tons, which is still a relatively low inventory. LME inventories for the last 14 years have ranged from a low of 20,000 in 1986 to 70,000 metric tons in 1990 increasing to a high of 1,400,000 in 1994, decreasing to 750,000 for 1995, 580,000 for 1996 and subsequently decreasing to a low of 190,000 in 2000 and increasing to 450,000 presently. Zinc consumption in excess of production accounts for the reduction of the high LME inventories over the last 8 years. Over the last 25 years the uses of and consumption of zinc has increased markedly and continues to do so. The primary use of zinc is corrosion protection as galvanized steel in the automobile industry and in commercial and residential construction, it is also used in alloys with copper, lead, aluminum and magnesium, tires, batteries, paints, the chemical industry and plant and animal nutrition. Zinc is one of our most important and useful metals.

Metalline has strong confidence in the future of base metals, particularly zinc. The uses for and the consumption of zinc continue to increase as new uses for zinc are developed. Of note is the recent increase in galvanized structural steel for commercial and residential construction using galvanized steel beams, trusses, floor joists, studs, exterior covering and roofs in place of dimensional lumber and conventional materials. Zinc fuel cells are under development for generating electricity and could create significant new demand. Zinc consumption is increasing and is projected to continue to increase 3 to 4% per annually.

In regards to future supply, while the uses and consumption of zinc are increasing, discovery of new deposits and reserves is not keeping pace with the depletion and projected depletion of reserves. Century, the new Red Dog discoveries and Antamina have been the latest large additions to reserves and mining capacity. Century, Australia, has annual production of 500,000 metric tons per year and Red Dog, Alaska, 525,000 metric tons per year (International Zinc Association, IZA) and Antamina, Peru 280,000 metric tons per year

(Noranda, BHP Billiton, Teck, Mitsubishi). Reductions in capacity are Sullivan, Canada, 100,000 metric tons per year is mined out and closed, Tara, Ireland, 165,000 metric tons per year has been closed, ASARCO's Tennessee Mines Division, 58,000 metric tons per year is closed, Santa Eulalia, Real de Angeles and San Francisco, Mexico, totaling 91,000 metric tons per year are closed. Polaris, Canada 125,000 metric tons per year, and two large Spanish mines and two large Scandinavian mines are projected to close due to reserve depletion within the next few years. Grupo Mexico owns San Martin 42,000 metric tons per year, Santa Barbara 38,000 metric tons per year and Santa Eulalia 26,000 metric tons per year (closed) in Mexico and mines in Chile and the U.S, Grupo's primary production is copper but they produce significant amounts of zinc and lead. Grupo's financial condition could force mine closures, reduction in production or financial failure.

The recent character of discovery has been the discovery of a few large deposits and a less than historical number of small and medium size discoveries. Numerous small and medium size mines will close due to reserve depletion and low prices have already forced many closures and reduction in capacity. These closures will reverse the production increase of Century and the recent production increase at Red Dog and new production at Antamina, unless new discoveries accelerate. Zinc, unlike copper, has limited known reserves; recent copper discoveries have provided large, high-grade reserves sufficient for decades. There is no shortage of the ability to mine and produce copper, there is for zinc. In addition, there is not large excess zinc smelter capacity.

China is the "Wild Card" in world production and consumption. China's mine production is 435,000 metric tons per year and its consumption is 850,000 metric tons per year (IZA). In recent years China has been a zinc exporter. China's production is rumored to have a significant component from small mines and smelters producing concentrates and metal at low cost, by western standards uneconomic mines and smelters. How much production is from these low cost sources and how long can they continue to operate, what is the rate of reserve depletion relative to discovery, how large are China's reserves, what is the discovery rate and the potential for discovery, the increase in world environmental concern and its effect on China's production are the unknowns. China's future consumption is the major unknown, if the Chinese become able to buy cars and appliances and increase their per capita consumption to anywhere near U.S. and European levels, consumption would outstrip their ability to produce and they would become an importer. The Chinese consume 0.67 kilogram (kg, 1.5 pounds) per capita relative to the U. S. of 4.49 kg (9.88 pounds) per capita and Europe of 3.38 kg (7.45 pounds) per capita (IZA for zinc consumption and Population Reference Bureau for population). Doubling China's consumption to 1.34 kg per capita, 30% of U.S. consumption, would require them to increase their mine production by an additional 829,000 metric tons to supply their own needs and would probably cease to become an exporter and become an importer.

In summary, in spite of the recent large discoveries and increasing LME inventories the long-term perspective, in my evaluation, is for increasing use and decreasing ability to supply zinc unless the rate of discovery of zinc increases markedly.

The most significant advantage for Sierra Mojada is that with the development of solvent extraction for zinc Sierra Mojada does not require higher metal prices to be profitable. The development of Solvent Extraction Electro-Winning (SXEW) of oxide zinc ores will revolutionize the zinc industry, as the technology did for copper 25 to 30 years ago. Presently almost all zinc metal production is from smelting of sulfide (sphalerite) concentrates. Consequently the zinc market price is set by the cost through the smelting process, which is about \$0.35 per pound. Anglo American's Skorpion project is under construction with production scheduled for midyear 2002. According to Anglo's feasibility

study Skorpion will produce zinc at \$0.25 per pound. There are only 5 mines with total cash operating costs less than \$0.37 per pound and when overhead is accounted for, a total cost basis, few mines are making a profit today. As stated above, the majority of sulfide mines have operating total cash costs in excess of \$0.50 per pound, on a total cost basis zinc prices will have to increase above \$0.55 or \$0.60 or the majority of the operating mines will close and severely reduce supply necessitating an increase in price to supply world zinc demand.

From 1994 to 2002 inventories on the LME have been reduced a million metric tons as a result of excess consumption over production. Consumption is forecast to increase 3 to 4% annually and a significant reduction in consumption is unlikely, even in difficult economic times, its uses are critical to our way of life and indeed our life, all life forms require zinc. Zinc price has to be at a bottom - no producer can stay in business with prices below the cost of production. Producers will have to require higher prices in order to produce the required, or desired, products and the consumer price will consequently have to increase. The competitive advantage of oxide ore deposits, like Skorpion and Sierra Mojada, with SXEW extraction and reduction is that at the lowest price zinc from concentrates can be produced, the smelter cost, they are profitable and as prices rise all of that increase is additional profit. A very compelling advantage as the average zinc price for the last 40 years has been \$0.61 per pound (IZA) with the most recent high of plus \$0.80 in 1989. Metalline believes that with Sierra Mojada's infrastructure advantages and the abilities and synergies of Penoles to mine and operate the extraction and reduction plant, Sierra Mojada may become one of the world's low cost producers of zinc and possibly the low cost producer.

I wish to thank all of our shareholders for their support and look forward to a productive and profitable 2002.

With Best Regards

Merlin Bingham  
President

This document contains forward-looking statements within the meaning of Section 27A of the Securities Act and Section 21E of the Exchange Act. Forward-looking statements are inherently subject to risks and uncertainties, many of which cannot be predicted with accuracy, and some of which might not even be anticipated.