NEARING PRODUCTION

RECOMMENDATION : POSITIVE

Kanmantoo remains on schedule for practical completion by 1 November, and also within budget. In addition, Hillgrove is reporting excellent near mine exploration results which are hoped to further extend the Kanmantoo mine life. Progress at the highly prospective Bird’s Head project in West Papua is stymied by red tape, but exploration continues at Sumba. We retain our POSITIVE recommendation.

- Kanmantoo construction is 80% complete, and on schedule for ore commissioning during October and first concentrate shipment planned for late November/early December. Sulphide ore is currently being stockpiled. Cost to complete the construction is currently estimated at AUD120-125m vs. FID estimate of AUD 121.2m.

- Hillgrove has reported excellent near mine exploration results at Kanmantoo from the 48 holes drilled to July 31, with every hole returning visible chalcopyrite. The results suggest a re-optimised mine plan undertaken next year should result in an extension of the current mine life.

- Whilst exploration at Bird’s Head has been stymied due to delays in awarding drilling permits, Hillgrove is making steady progress at Sumba. Within the Sumba project area, at the southern project (Masu), 800m strike length of significant gold mineralisation has been delineated. A 3,300 line km aeromagnetic and radiometric survey over the bulk of the Sumba IUP was also completed during the quarter.

- Hillgrove remains in a strong position, with AUD55.3m cash on hand, and undrawn debt facilities of AUD 18m.
FURTHER DETAILS
Exploration at Kanmantoo ramped up significantly in late May. The initial program consisted of 7,500m RC drilling in and around the current planned open pits. The long sections below show the progress brought by first drilling. Drilling at Emily Star yielded similar results (with a total of 48 holes drilled to the end of July), which prompted expansion of the initial program to 10,500m, with an additional RC rig brought on site.

Source: Hillgrove
FINANCIAL SUMMARY

Hillgrove Resources HGO

Recommendation: Positive

Year end Jan 2010A 2011A 2012F 2013F 2014F

INCOME STATEMENT

Total Revenue $m 98.2 9.0 25.0 169.2 203.2
Operating Costs $m -0.9 -1.7 -19.1 -92.3 -87.8
Royalty $m 0.0 0.0 -1.3 -10.5 -12.7
Exploration W/off $m -1.9 -2.7 -3.2 -2.8 2.8
Total Op. Costs $m -2.8 -4.4 -16.0 -105.7 -103.3
D&A $m -0.1 0.0 -2.1 -16.7 -20.3
Interest Exp. $m -1.47 -0.4 -1.0 -1.5 -0.8
Corporate $m -7.3 -7.4 -13.7 -13.8 -13.9
Other $m 4.5 -20.1 0.0 0.0 0.0
Total Costs $m -20.4 -32.2 -33.9 -137.6 -138.4
Pre-Tax Profit $m 77.8 -23.3 -7.9 31.5 64.8
Tax Provision $m -22.2 9.1 2.8 11.0 -22.7
Net Profit $m 55.6 -14.2 -5.1 20.5 42.1
Minorities $m 0.0 0.0 0.0 0.0 0.0
Attrib Net Profit $m 52.4 -14.2 -5.1 20.5 42.1
Abnormal $m 0.0 0.0 0.0 0.0 0.0
Reported profit $m 52.4 -14.2 -5.1 20.5 42.1

CASH FLOW

Operating Cashflow $m -8.4 -40.7 6.1 46.2 71.4
Capex $m -7.2 -41.8 -111.4 -2.2 -2.2
Exploration $m -4.4 -8.7 -12.9 -11.1 -111.1
Free Cashflow $m -20.1 -91.2 -118.2 32.9 58.0
-dividends $m -8.3 0.0 0.0 0.0 0.0
+Equity Raised $m 32.8 73.7 0.0 0.0 0.0
+Debt Drawdown $m -47.3 -2.5 47.0 -35.0 0.0
-Other (incl asset sales) $m 165.1 7.8 1.6 0.0 0.0
Net Change in Cash $m 122.3 -12.2 -69.5 -2.1 58.0
Cash at End Period $m 130.0 117.8 48.3 46.1 104.2

BALANCE SHEET

Cash $m 130.4 117.8 48.3 46.1 104.2
Total Assets $m 211.1 253.5 283.8 275.6 323.9
Total Debt $m 2.5 0.0 47.0 12.0 12.0
Total Liabilities $m 47.3 68.6 115.4 80.4 80.4
Shareholders Equity $m 163.8 184.9 168.5 195.2 243.5

Production

Kanmantoo Ore Milled (kt) - 300 2,400 2,400
Head Grade - Cu% (g/t) 0.0% 0.0% 0.8% 0.8% 0.9%
Production - Cu(kt) - 2 17 20
Profit and Loss Cash Cost
Cash Cost ($US/t) 39 37
Cash Cost ($US/lb) 1.91 1.44
Total Cost ($US/lb) 2.25 1.77

RESOURCES

<table>
<thead>
<tr>
<th>T (m)</th>
<th>Zn %</th>
<th>Cu %</th>
<th>Pb %</th>
<th>Au (g/t)</th>
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<td>Kanmantoo</td>
<td>32.2</td>
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<td>0.00%</td>
<td>0.2</td>
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<tr>
<td>Attributable share</td>
<td>32.2</td>
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RESERVES (Contained Metal)

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<tr>
<th>T (m)</th>
<th>Zn</th>
<th>Cu</th>
<th>Pb</th>
<th>Au (G/t)</th>
<th>Au (G/t)</th>
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</thead>
<tbody>
<tr>
<td>Attr share</td>
<td>14.8</td>
<td>0.0</td>
<td>0.9</td>
<td>0.0</td>
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</table>

Valuation Summary

BASE CASE

Valuation Metrics

PER x 2.1 Na Na 10.0 4.9
Dividend Yield % 7.5 0.0 0.0 0.0 0.0
ROE % 32% -6% -3% 11% 17%
Net Debt to Equity % 0% 0% 0% 0% 0%
Debt to Assets % 0% 0% 0% 0% 0%

Directors

Chairman The Hon. Dean Craig Brown
Interim Managing Director Mr Drew Simonsen
Non Executive Director Mr John Quirke
Non Executive Director Mr John Gooding
Non Executive Director Mr Ronald Belz
Non Executive Director Mr Edwin Zemancheff

Substantial Shareholders

JPM Metals and Concentrates LLC 54.0% 7.0%

Assumptions

Copper (US$/t) 2.37 2.30 4.15 4.15 4.12
Average Exchange Rate (US$/A$) 0.74 1.03 1.00 0.99 0.97
Gold Price (A$/oz) 1115 1148 1820 1844 1905
Silver Price (US$/L) 31360 18 41 41 41

Attributable share 14.8 0.0 0.9 0.0 3.1 0.2
RESEARCH RECOMMENDATION DEFINITIONS

Positive Stock is expected to outperform the S&P/ASX 200 over the coming 24 months
Neutral Stock expected to perform in line with the S&P/ASX 200 over the coming 24 months
Negative Stock is expected to underperform the S&P/ASX 200 over the coming 24 months
Speculative Stock has limited history from which to derive a fundamental investment view or its prospects are highly dependent on event risk, eg. Successful exploration, scientific breakthrough, high commodity prices, regulatory change, etc.
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Recommendations are primarily determined with reference to how a stock ranks relative to the S&P/ASX 200 on the following criteria:

Valuation Rolling 12 month prospective multiples (composite of Price-to-Earnings Ratio, Dividend Yield and EV/EBITDA), or long-term NPV for resource stocks.

Earnings Outlook Forecast 2 year EPS growth.

Earnings Momentum Percentage change in the current consensus EPS estimate for the stock (rolling 1 year forward basis) over the consensus EPS estimate for the stock 3 months ago.

Shareholder Returns Composite of forecast ROE (rolling 1 year forward basis) and the percentage change in ROE over 2 years.

Debt Servicing Capacity Rolling 12 month EBIT Interest Cover ratio.

Cyclical Risk Qualitative assessment of the 2 year outlook for a stock/industry's profit cycle.

Industry Quality Qualitative assessment of an industry’s growth/returns potential and company specific management capability.

Financial Transparency If we don’t understand it, we won’t recommend it.

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