Hillgrove Resources (HGO)
First production December 2011
Copper-gold concentrate, SA; Indonesian exploration

Recommendation
BUY

Price
30c

Valuation
41c

ASX / S&P Sector
Metals & Mining

HGO is re-developing the Kanmantoo copper-gold mine in South Australia, which was previously mined 1970 – 1976.

HGO expects to produce 21kt/yr of copper, at a cash cost of $1.61/lb, starting December 2011.

HGO also has highly prospective ELs, near the Kanmantoo mine and in 2 areas of Indonesia.

Intersuisse’s base case valuation of 41c a HGO share gives zero value to HGO’s exploration and also assumes copper prices falling back to $3/lb, and gold back to $1,000/oz.

Intersuisse’s valuation using spot prices, and the planned increase in throughput to 3.5Mt/yr, is 67c.

Snapshot

| Last Price | $0.300 |
| Market Cap. | $234 million |
| Shares on Issue | 794m |
| 52 Week High | $0.515 |
| 52 Week Low | $0.250 |

Price Chart

HGO is currently re-developing the Kanmantoo copper-gold mine in South Australia, which was mined from 1970 to 1976 by Broken Hill South.

HGO’s first date for production was late 2008; some of this delay can be attributed to more conservative financing following the GFC, most of the delay can be attributed to over-optimistic projections. The previous CEO stepped down in June 2010.

After many delays, construction is now taking place.

HGO also has very attractive exploration prospects in Indonesia as well as near the Kanmantoo mine.

See www.hillgroveresources.com.au

Analyst: Pieter Bruinstroop:

Investment Highlights

- HGO has secured finance and on-site project construction has started.
- Kanmantoo is expected to produce 21kt, or 46M lb, of copper, a year, at a cash cost of $1.61/lb, which compares with current copper prices of over $4.50/lb.
- HGO has valuable exploration prospects in the Kanmantoo exploration lease area and for gold in Sumba Island and copper-gold at Brid’s Head, West Papua.
- Assuming successful project delivery and exploitation of existing resources, with current spot prices, Intersuisse’s valuation is 90c.

Review

The HGO share price has lagged the copper price and also its progress in development. In Intersuisse’s view, this is because the market has become dis-illusioned with has over-promising and under-delivering:

- First mine production will be about 4 years later than originally proposed;
- Development costs are much higher; and
- Much more equity has been required.

In Intersuisse’s view, the change in the MD in the middle of 2010 has changed HGO from an entrepreneurial focus to an operations focus, to be able to deliver HGO’s potential value.

Recommendation

Intersuisse initiates research on HGO with a BUY recommendation.

In our view, the current share price is a significant discount to the value of the Kanmantoo mine re-development. Investors get exploration upside that could have significant potential, for nothing.
Hillgrove Resources Limited (HGO)

Hillgrove Resources Limited (HGO) is re-developing the Kanmantoo mine in South Australia that was mined by Broken Hill South from 1970 to 1976, producing 4.05Mt of ore at 1.1% copper. The mine was shut when copper was about $1,500/t ($5,800/t in 2010 terms) due to falling copper prices and also extended industrial action.

Figure 1 shows that Kanmantoo is in South Australia, 55km from Adelaide, along the south-eastern freeway.

Figure 2 shows that Kanmantoo has Resources of 32.2Mt, grading 0.9% copper, 0.2g/t gold and 3.2g/t silver, of which mineable reserves are 14.8Mt at similar grades.

Figure 3 shows the detail of Intersuisse’s valuation of HGO, of 41.2c a HGO share.

Note :
- 31.3c of Intersuisse’s valuation is in the Reserves shown in Figure 2b
- Intersuisse has given some value to the Resources, as we believe that more than 15Mt will be mined.

Figure 3 also shows that Intersuisse has given zero value to HGO’s exploration:
- There are 3 focus areas to HGO’s exploration:
  - Near the Kanmantoo mine, within the exploration leases shown in Figure 1, in which there are many old copper and lead-zinc mines;
  - 80% of an EL on Sumba Island, near Batu Hijau on Sumbawa, west of Timor, which has given good gold grades from rock chip sampling, trenching and some shallow drilling; and
  - 80% of Bird’s Head, an EL on the north coast of West Papua, which contains extensive porphyry style copper-gold and epithermal gold mineralisation and has yielded very good copper-gold grades from trench sampling.

Source: Intersuisse estimates
While Intersuisse believes that each of these projects will add value, we do not ascribe any value to them.

The analysis in the main report shows that Kanmantoo is dominantly a copper project. Figure 4 shows the historical copper price and the projected copper prices used by Intersuisse in deriving our base case valuation of 41c. It shows that Intersuisse’s valuation is based on copper prices falling to $3.00/lb, from present levels over $4.50/lb.

**Figure 4 : Historical copper prices and Intersuisse’s projections**

Intersuisse’s valuation rises to 62c if current spot prices are assumed to last for the mine life

Expanding to 3.5Mt/yr from 2.7Mt/yr raises the valuation to 67c

Intersuisse’s valuation rises further, to 90c, if the risk discount is removed.

Successful project delivery with expanded production, but base case prices, give a valuation of 62c.

HGO’s share price has lagged the copper price, in contrast to most of its peers.

Source: IRESS, Intersuisse

In Intersuisse’s view, the lagging share price was due to “over-promising and under-delivering”

HGO has secured a new CEO to ensure that its valuable are delivered and generate value for shareholders.

In July the original CEO, David Archer, stood down and was replaced by Drew Simonsen, as project development became bogged down, as detailed in Appendix 1, by

- delayed approvals;
- delayed financing, due to the need to do more close spaced drilling; and
- a need for more equity than had been expected

**Conclusions**

The HGO share price has been left behind by the improving copper price. Intersuisse believes that this has been due to over-promising and under-delivering.

Intersuisse’s base case valuation is 41c, which is a significant premium to the current share price of 30c.

There is significant upside potential to Intersuisse’s valuation from:

- successful project delivery;
- metals prices remaining stronger than expected; and
- exploration, both near mine and also in Indonesia.
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Prepared by Pieter Bruinstroop