

## Hillgrove Resources Ltd

HGO : ASX

BUY

Target: A\$0.131

Reg Spencer

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## COMPANY STATISTICS:

Share Price (A\$)	0.092
12 Mth Hi-Lo (A\$)	0.145-0.052
Market Cap (A\$m)	109
Enterprise Value (A\$m)	136
Issued Shares (m)	1,179
Options (various)	128
Cash (31/10/13)	A\$17m
Debt (31/10/13)	A\$44m
<b>Major Shareholders</b>	
IOOF	10.4%
Renaissance Smaller Co's	8.4%

## EARNINGS SUMMARY:

Jan Yr End	2014e	2015e	2016e
Cu Prod'n (t)	16,778	20,448	19,490
C1 Costs (A\$/lb)	2.53	2.00	2.12
AISC (A\$/lb)	3.07	2.29	2.36
Copper (US\$/lb)	3.23	3.25	3.21
EBITDA (A\$m)	40.4	59.4	50.1
EV/EBITDA	3.2x	1.5x	1.0x
P/CF	10.6x	2.2x	2.4x
NPAT (A\$m)	8.1	20.6	18.6
EPS (A\$)	\$0.01	\$0.02	\$0.02
PER	12.5x	5.3x	5.8x

Source: Canaccord Genuity estimates

## SHARE PRICE PERFORMANCE:



Source: Interactive Data Corporation

## COMPANY DESCRIPTION:

Hillgrove Resources Ltd (HGO:ASX) is an Australian mining company whose primary asset is the 100%-owned Kanmantoo copper mine, located in South Australia. The mine is capable of producing up to 20,000 tpa copper in concentrate, over a mine life of 8 years

All amounts are in AUD unless otherwise noted.

Metals and Mining – Base Metals &amp; Minerals

## Q3'FY14 REPORT

## Investment Perspective

It was a solid quarter from HGO with key stats mostly in line with our expectations. The significant QoQ improvement is consistent with our thesis that steps taken by the company over the last 12 months plus a move into higher grade/lower strip mining areas are set to drive a turnaround in operating performance and FCF. We will continue to look for further gains to close out the year in Q4'FY14, and re-iterate that the shares continue to offer considerable upside at current levels. We maintain our BUY rating.

## Investment Highlights

- A stronger Q3FY14 copper production figure of 4.3kt was in line with our forecasts of 4.4kt, driven by QoQ improvements in head grades and mill throughput. The move into higher grade/lower strip areas of the Kavanagh pit plus processing plant upgrades is becoming evident, with a similarly strong Q4 expected. As such, we have adjusted upwards our FY14 production estimates to 16.8kt from 16.3kt.
- C1 costs of US\$2.80/lb were higher than expected with the benefits of the recent move to owner operated mining not becoming evident until later in the quarter. Processing unit costs fell by 14% QoQ, but were offset by lower than modelled gold/silver credits. We continue to expect improved costs as grades increase and waste movement falls, with costs for Oct'13 reported at US\$2.07/lb providing a preview of what can be expected moving into 2014
- Cash at period end was steady at \$16.5m, with improved revenue offset by one-off costs associated with the change to owner operated mining, settlement with the previous mining contractor and debt repayments. At the end of Oct'13, outstanding debt was \$44m.

## BUY rating maintained; TP unchanged at A\$0.13/share

We have updated our model following the Q3'FY14 results, including a minor increase in forecast production for the remainder of FY14. Our DCF-based (NPV<sub>8%</sub>) target price remains unchanged at \$0.13/share.

## FINANCIAL SUMMARY

### Hillgrove Resources Limited

HGO:ASX

Analyst :

Reg Spencer

Date:

19/11/2013

Year End:

January

Rating:

**BUY**

Target Price:

**\$0.13**

#### Market Information

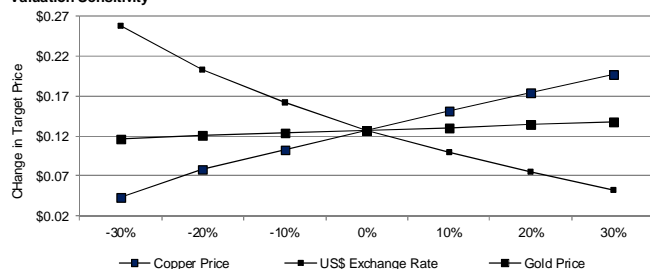
Share Price	A\$	0.092
Market Capitalisation	A\$m	108.5
12 Month Hi-Lo	A\$	0.145-0.052
Issued Capital	m	1179
Options	m	128
Fully Diluted	m	1307

#### Valuation

	A\$m	A\$/share	
Kanmantoo	NPV @ 8%	191.0	0.16
Exploration		10.0	0.01
Corporate	(26.4)	(0.02)	
Copper Forwards NPV	3.3	0.00	
Cash	16.6	0.01	
Debt	(44.5)	(0.04)	
<b>Total NAV/Price Target</b>	<b>150.0</b>	<b>0.13</b>	
Price/NAV		0.72x	

Assumptions	2013a	2014e	2015e	2016e
Gold Price (US\$/oz)	1,638	1,321	1,326	1,344
Copper Price (US\$/lb)	3.51	3.23	3.25	3.21
AUD:USD	1.03	0.92	0.92	0.91

#### Valuation Sensitivity



Production Metrics	2013a	2014e	2015e	2016e
<b>Kanmantoo</b>				
Cu Prod'n (t)	13,743	16,778	20,448	19,490
C1 Costs (A\$/lb)	2.64	2.53	2.00	2.12
All in Sust. Costs (A\$/lb)	3.28	3.07	2.29	2.36

#### Group Reserves & Resources

	Mt	Grade Cu	Tonnes Cu
<b>Reserves (100%)</b>			
Kanmantoo	22.10	0.71%	156,730
<b>Resources (100%)</b>			
Kanmantoo	31.29	0.78%	242,529

#### Directors

Name	Position
Hon. D Brown	Chairman
G Hall	CEO & MD
J Gooding	NED
J Quirke	NED
D Snedden	NED
E Zemancheff	NED

#### Substantial Shareholders

	Shares (m)	%
IOOF	122.14	10.4%
Renaissance Smaller Co's	98.86	8.4%
Platinum Partners	83.31	7.1%

#### Company Description

Hillgrove Resources Limited (HGO:ASX) is an Australian mining company whose primary asset is the 100%-owned Kanmantoo Copper mine located in SE South Australia. The mine was commissioned in 2012, and is capable of producing 20,000 tpa of copper in concentrate, over a mine life of +8 years.

Profit & Loss (A\$m)	2013a	2014e	2015e	2016e
<b>Revenue</b>	115.4	139.5	172.4	165.0
Operating Costs	92.6	106.5	106.8	107.3
Royalties	1.6	1.8	2.3	2.2
Corporate & Oheads	4.4	3.8	4.9	5.0
Exploration (Expensed)	0.0	0.0	0.0	2.0
<b>EBITDA</b>	10.8	40.4	59.4	50.1
Dep'n	26.5	26.6	30.0	23.5
<b>EBIT</b>	-15.7	13.7	29.4	26.6
Net Interest	-1.3	0.8	1.0	1.6
Tax	8.8	4.6	8.8	8.0
<b>NPAT</b>	-16.5	7.1	20.6	18.6
Abnormals	-4.8	-1.0	0.0	0.0
<b>NPAT (reported)</b>	-11.7	8.1	20.6	18.6

Cash Flow (A\$m)	2013a	2014e	2015e	2016e
<b>Cash Receipts</b>	106.7	129.1	172.8	165.3
Cash paid to suppliers & employee	-75.7	-105.3	-114.0	-114.5
Tax Paid	0.0	-2.4	-8.8	-6.8
Net Interest	-3.1	-2.7	-0.9	1.4
Other costs	-0.9	-8.5	0.0	0.0
<b>Operating Cash Flow</b>	<b>26.9</b>	<b>10.2</b>	<b>49.0</b>	<b>45.4</b>
Exploration and Evaluation	-8.6	-3.2	-4.7	-4.1
Capex	-38.1	-13.3	-8.2	-1.7
Other	1.1	0.1	0.0	0.0
<b>Investing Cash Flow</b>	<b>-45.7</b>	<b>-16.4</b>	<b>-12.9</b>	<b>-5.7</b>
Debt Drawdown (repayment)	6.1	-11.3	-17.8	-21.6
Share capital	18.6	10.8	0.0	0.0
Dividends	0.0	0.0	0.0	0.0
Financing Expenses	-0.8	-0.5	0.0	0.0
<b>Financing Cash Flow</b>	<b>23.9</b>	<b>-1.0</b>	<b>-17.8</b>	<b>-21.6</b>
Opening Cash	22.1	27.4	20.2	38.5
Increase / (Decrease) in cash	5.2	-7.2	18.3	18.1
FX Impact	0.0	0.0	0.0	0.0
<b>Closing Cash</b>	<b>27.3</b>	<b>20.2</b>	<b>38.5</b>	<b>56.7</b>

Balance Sheet (A\$m)	2013a	2014e	2015e	2016e
Cash + S/Term Deposits	27.4	20.2	38.5	56.7
Other current assets	31.4	33.7	41.6	40.0
<b>Current Assets</b>	<b>58.8</b>	<b>53.9</b>	<b>80.2</b>	<b>96.6</b>
Property, Plant & Equip.	233.2	219.8	198.1	176.2
Exploration & Develop.	27.4	30.6	35.3	39.4
Other Non-current Assets	16.5	24.5	34.7	29.2
Payables	40.0	18.2	22.5	21.7
Short Term debt	29.5	17.8	21.6	0.0
Long Term Debt	20.8	21.6	0.0	0.0
Other Liabilities	25.1	30.8	43.0	42.4
<b>Net Assets</b>	<b>220.6</b>	<b>240.5</b>	<b>261.1</b>	<b>277.4</b>
Shareholders Funds	196.5	207.3	207.3	207.3
Reserves	0.6	1.6	1.6	1.6
Retained Earnings	23.5	31.6	52.2	68.4
<b>Total Equity</b>	<b>220.6</b>	<b>240.5</b>	<b>261.1</b>	<b>277.4</b>

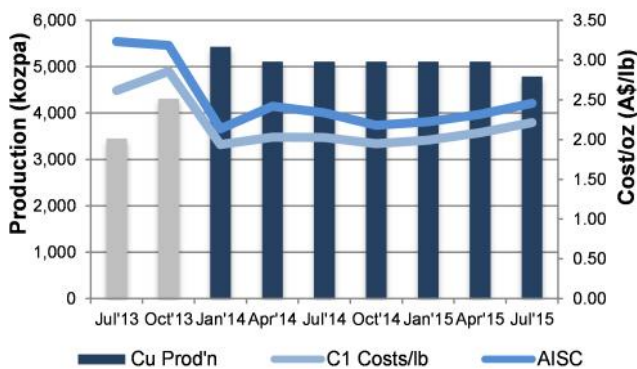
Ratios & Multiples	2013a	2014e	2015e	2016e
EBITDA Margin	9%	29%	34%	30%
EV/EBITDA	10.9x	3.2x	1.5x	1.0x
Op. Cashflow/Share	\$0.03	\$0.01	\$0.04	\$0.04
P/CF	3.5x	10.6x	2.2x	2.4x
EPS	-\$0.01	\$0.01	\$0.02	\$0.02
EPS Growth	nm	-154%	137%	-10%
PER	-6.8x	12.5x	5.3x	5.8x
Dividend Per Share	\$0.00	\$0.00	\$0.00	\$0.00
Dividend Yield	0%	0%	0%	2%
ROE	-5%	3%	8%	7%
ROIC	-11%	8%	18%	17%
Debt/Equity	9%	9%	0%	0%
Net Interest Cover	nm	nm	nm	nm
Book Value/share	\$0.22	\$0.20	\$0.22	\$0.24
Price/Book Value	0.4x	0.5x	0.4x	0.4x

Source: Company reports & Canaccord Genuity estimates

### Q3'FY14 REPORT

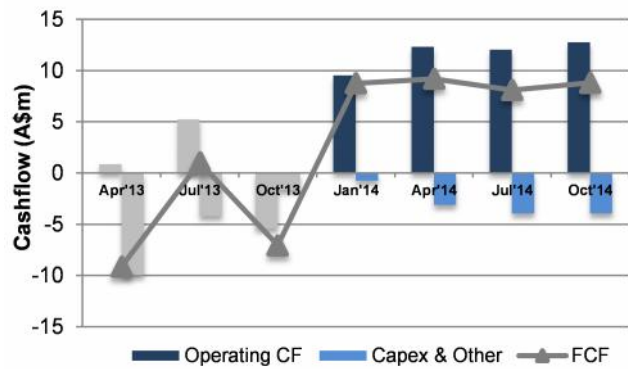
- HGO reported Q3'FY14 copper in concentrate production of 4.3kt (vs CGAu est of 4.4kt), representing a solid 25% increase QoQ. Substantial increases in head grades and milled throughput (annualised at 3 Mtpa vs nameplate of 2.8 Mtpa) contributed to the strong result. The benefits of a move into a lower strip/higher grade portion of the Kavanagh pit plus processing plant improvements are increasingly becoming evident, with grades of 0.79% reported for the month of Oct also very encouraging for the outlook.
- C1 costs of US\$2.80/lb were higher than forecast, with the benefits of the change out from contract mining to owner operated mining not becoming evident until late in the quarter. Lower than modelled gold production (function of lower grades earlier in the quarter) also impacted the result, offset by improvements in processing unit costs. We continue to expect improved costs as grades increase and waste movement falls, with costs for Oct reported at US\$2.07/lb providing a preview of what can be expected moving into 2014. We estimate AISC for the period of US\$2.94/lb.
- No change has been made to FY14 (Jan year-end) guidance of 16.5-18kt copper in concentrate. With further improvements in copper production expected, we forecast a similarly strong Q4, and as a result have made minor adjustments to our FY14 copper production estimates to 16.8kt (up from 16.3kt).

Figure 1: Production & AISC forecasts



Source: Company reports & Canaccord Genuity estimates

Figure 2: FCF forecasts



Source: Company reports & Canaccord Genuity estimates

- Cash at period end was mostly unchanged at \$16.5m, reflecting the one-off costs associated with the move to owner operated mining and settlement with the previous mining contractor. Debt was reduced to \$44m following approximately \$4m in repayments on the Senior Debt facility and the gold loan. With higher grades to drive improved copper production, we continue to forecast stronger FCF moving into 2014.

## INVESTMENT RISKS

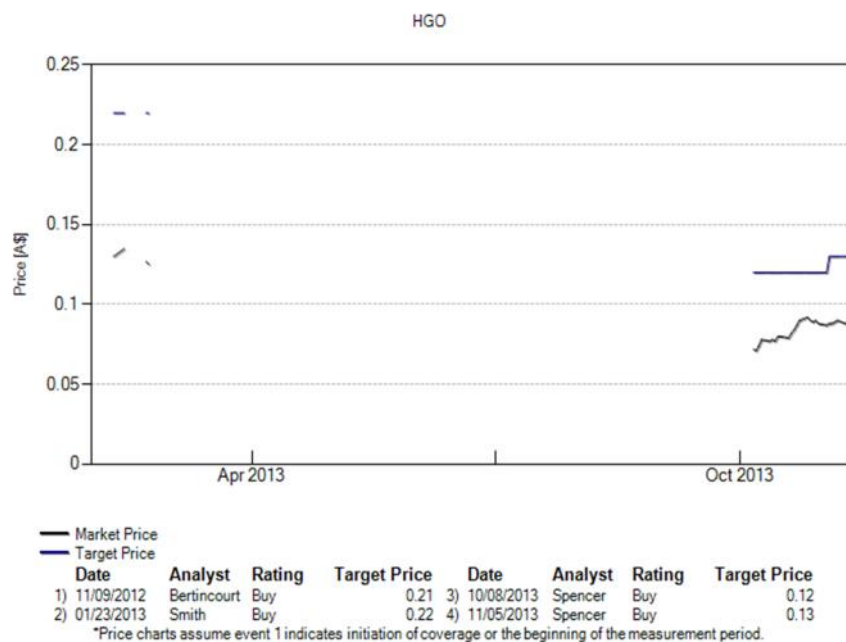
The key investment risks for HGO include:

- Geological & Resource risk – the actual characteristics of a mineral deposit may differ significantly from initial interpretations and expectations. HGO's LOM Plan incorporates Mineral Resources and Exploration Targets whose actual economics are yet to be determined. Grades and tonnages for Exploration Targets are conceptual in nature
  - Operating Risk - As a producer, operating risk is an inherent risk for the company. Halts and or reductions in production due to equipment availability, geotechnical issues, people issues, environmental issues, and weather issues can all reduce and or stop production and therefore revenue and cashflow. Operating risk is a key risk for the company, in particular as HGO is a single asset company.
  - Capital expenditure & operating risk – the risk that capital and or operating costs exceed budget and/or exhaust available funding, reducing the profitability and free cash generation of the project.
  - Commodity price and exchange rate risk: As with all mining and mineral exploration companies, commodity price and exchange rate risk should also be considered.
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**Price Chart:**



**Site Visit:** An analyst has visited the company's material operations in South Australia. No payment was received for related travel costs.

**Distribution of Ratings:  
Global Stock Ratings  
(as of 30 September 2013)**

Rating	Coverage Universe		IB Clients	
	#	%	#	%
Buy	562	57.9%	37	37.7%
Speculative Buy	47	4.8%	31	67.4%
Hold	313	32.2%	11	11.2%
Sell	47	4.8%	7	6.4%
	971*	100.0%		

\*Total includes stocks that are Under Review

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