

# Hillgrove Resources Ltd

HGO : ASX : A\$0.077

**BUY**

**Target: A\$0.131**

Reg Spencer

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## COMPANY STATISTICS:

Share Price (A\$)	0.077
12 Mth Hi-Lo (A\$)	0.094-0.061
Market Cap (A\$m)	91
Enterprise Value (A\$m)	104
Issued Shares (m)	1,178
Options (various)	128
Cash (31/7/14)	A\$12m
Debt (31/7/14)	A\$25m
<b>Major Shareholders</b>	
Perennial Value Mgt	12.5%
Platinum Partners	8.4%

## EARNINGS SUMMARY:

Dec Yr End	2014e	2015e	2016e
Cu Prod'n (t)	21	19	20
C1 Costs (A\$/lb)	2.32	2.17	2.10
AISC (A\$/lb)	2.86	2.56	2.52
Copper (US\$/lb)	3.18	3.23	3.15
EBITDA (A\$m)	47.0	47.0	49.6
EV/EBITDA	1.9x	1.1x	0.5x
P/CF	1.9x	1.8x	1.9x
NPAT (A\$m)	7.4	16.6	17.5
EPS (A\$)	\$0.01	\$0.01	\$0.01
PER	12.3x	5.5x	5.2x

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 & Minerals

## Q2'14 REPORT

### Investment Perspective

Hillgrove Resources' (HGO) Q2'14 report showed another solid quarter, beating our production estimates despite the impact of wet weather on operations. We are impressed by HGO's operational turnaround over the last 12 months, and now look to incremental improvements to operating costs and the potential for dividends in 2015 as the next steps for the company. We continue to see value on both multiple (CY15e EV/EBITDA 1.1x) and DCF valuation metrics (P/NAV 0.61x), and maintain our BUY rating.

### Investment Highlights

- Q2 production was reported at 5.9kt Cu in concentrate, a 7% beat on our estimates of 5.5kt. Rain impacted mining and mill feed grade during the quarter, but this was offset by record quarterly milling volumes. Production costs continue to trend down with C1 costs of A\$2.07/lb, below our estimates of A\$2.30/lb due to higher Cu production and inventory adjustments. We estimate AISC of A\$2.74/lb, a 10% QoQ drop after incorporating deferred mining adjustments.
- Cash at period end was reported at \$12.5m, below our forecasts of \$14.5m. The variance is explained by higher than modelled debt repayments and capitalised pre-strip costs. Cashflow during the quarter included a further \$8.2m in debt repayments, with HGO's net debt at period end \$13.1m (31% QoQ improvement). HGO has moved to December year-end reporting, and have revised guidance to cover the 11 month period from Feb-Dec'14, to 20.5-22.5kt Cu, in line with our revised CY14 estimates of 21.3kt. The revision represents no major change to our expectations.
- HGO recently announced that it would seek shareholder approval for a 1:8 consolidation of its share capital and unmarketable sale facility at a meeting in Sep'14. Such capital management initiatives follow on from last quarters' announcement where HGO would assess the potential for dividends.
- With Kanmantoo operations performing well, HGO also announced that it is to re-commence exploration activities, focusing on near mine opportunities and other regional targets including the recently acquired Kitticoola prospect. The company's Indonesian projects remain on care and maintenance while discussions with interested parties for the possible sale/JV of these projects continue.

### BUY rating and \$0.13/share target maintained

Our target price (NAV comprising Kanmantoo NPV<sub>8%</sub>, net debt and other adjustments) is unchanged at \$0.13/share.

**FINANCIAL SUMMARY**

**Hillgrove Resources Limited**

HGO:ASX

Analyst :

Reg Spencer

Date:

25/08/2014

Year End:

December\*

Rating:

**BUY**

Target Price:

**\$0.13**

**Market Information**

Share Price	A\$	0.077
Market Capitalisation	A\$m	90.7
12 Month Hi-Lo	A\$	0.094-0.061
Issued Capital	m	1178
Options	m	128
Fully Diluted	m	1306

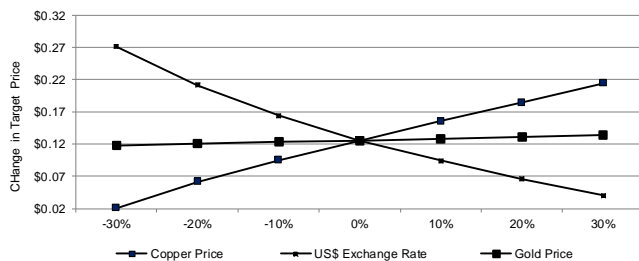
**Valuation**

	A\$m	A\$/share	
Kanmantoo	NPV @ 8%	167.0	0.14
Exploration	10.0	0.01	
Corporate	(21.3)	(0.02)	
Copper Forwards NPV	5.7	0.00	
Cash	12.1	0.01	
Debt	(25.2)	(0.02)	
<b>Total NAV/Price Target</b>	<b>148.2</b>	<b>0.13</b>	
Price/NAV		0.61x	

**Assumptions**

	2014a*	2014e	2015e	2016e
Gold Price (US\$/oz)	1,300	1,317	1,337	1,367
Copper Price (US\$/lb)	3.19	3.18	3.23	3.15
AUD:USD	0.91	0.93	0.92	0.88

**Valuation Sensitivity**



**Production Metrics**

	2014a*	2014e	2015e	2016e
<b>Kanmantoo</b>				
Cu Prod'n (kt)	17.2	21.3	19.5	19.8
C1 Costs (A\$/lb)	2.62	2.32	2.17	2.10
All in Sust. Costs (A\$/lb)	3.29	2.86	2.56	2.52

**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
M Loomes	NED
D Snedden	NED

**Substantial Shareholders**

	Shares (m)	%
Perennial Value Mgt	147.71	12.5%
Platinum Partners	98.86	8.4%
Renaissance Smaller Co's	87.20	7.4%

\* - moved to Dec Yr-end reporting from Jan Yr - end as at August'14

Source: Company reports & Canaccord Genuity estimates

**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)**

	2014a*	2014e	2015e	2016e
<b>Revenue</b>	139.2	174.3	160.2	163.4
Operating Costs	107.9	120.9	105.3	104.5
Royalties	1.6	2.1	2.1	2.2
Corporate & O'heads	3.2	4.8	4.9	5.0
Exploration (Expensed)	0.0	0.0	1.7	4.1
<b>EBITDA</b>	39.4	47.0	47.0	49.6
Dep'n	29.2	35.6	23.3	24.6
<b>EBIT</b>	10.3	11.4	23.7	25.0
Net Interest	0.8	0.5	0.8	2.0
Tax	0.8	4.0	7.1	7.5
<b>NPAT</b>	-6.4	7.4	16.6	17.5
Abnormals	-7.9	0.0	0.0	0.0
<b>NPAT (reported)</b>	1.6	7.4	16.6	17.5

**Cash Flow (A\$m)**

	2014a*	2014e	2015e	2016e
<b>Cash Receipts</b>	121.3	176.6	161.5	162.4
Cash paid to suppliers & employees	-107.5	-127.9	-112.3	-111.7
Tax Paid	0.0	0.0	0.0	-5.7
Net Interest	-2.8	-1.0	0.8	2.0
Other costs	0.0	-0.2	0.0	0.0
<b>Operating Cash Flow</b>	<b>11.0</b>	<b>47.6</b>	<b>50.0</b>	<b>46.9</b>
Exploration and Evaluation	-3.8	-0.8	-2.9	-2.1
Capex	-19.0	-20.8	-8.8	-10.0
Other	0.4	0.0	0.0	0.0
<b>Investing Cash Flow</b>	<b>-22.3</b>	<b>-21.6</b>	<b>-11.7</b>	<b>-12.1</b>
Debt Drawdown (repayment)	-9.8	-31.4	-9.5	0.0
Share capital	10.8	0.0	0.0	0.0
Dividends	0.0	0.0	0.0	-8.2
Financing Expenses	-0.6	0.0	0.0	0.0
<b>Financing Cash Flow</b>	<b>0.4</b>	<b>-31.4</b>	<b>-9.5</b>	<b>-8.2</b>
Opening Cash	27.4	16.5	11.1	40.0
Increase / (Decrease) in cash	-10.9	-5.4	28.8	26.5
FX Impact	0.0	0.0	0.0	0.0
<b>Closing Cash</b>	<b>16.5</b>	<b>11.1</b>	<b>40.0</b>	<b>66.5</b>

**Balance Sheet (A\$m)**

	2014a*	2014e	2015e	2016e
Cash + S/Term Deposits	16.5	11.1	40.0	66.5
Other current assets	35.4	42.0	38.6	39.7
<b>Current Assets</b>	<b>51.9</b>	<b>53.1</b>	<b>78.6</b>	<b>106.2</b>
Property, Plant & Equip.	225.7	210.8	196.3	181.7
Exploration & Develop.	30.5	31.3	34.2	36.3
Other Non-current Assets	14.1	26.2	24.2	13.1
Payables	23.9	22.7	20.9	21.5
Short Term debt	31.4	9.5	0.0	0.0
Long Term Debt	9.5	0.0	0.0	0.0
Other Liabilities	28.9	53.4	63.4	60.0
<b>Net Assets</b>	<b>228.5</b>	<b>235.9</b>	<b>249.0</b>	<b>255.9</b>
Shareholders Funds	206.9	206.9	206.9	206.9
Reserves	-3.3	-3.3	-3.3	-3.3
Retained Earnings	25.0	32.4	45.5	52.4
<b>Total Equity</b>	<b>228.5</b>	<b>235.9</b>	<b>249.0</b>	<b>255.9</b>

**Ratios & Multiples**

	2014a*	2014e	2015e	2016e
EBITDA Margin	28%	27%	29%	30%
EV/EBITDA	2.9x	1.9x	1.1x	0.5x
Op. Cashflow/Share	\$0.01	\$0.04	\$0.04	\$0.04
P/CF	8.2x	1.9x	1.8x	1.9x
EPS	\$0.00	\$0.01	\$0.01	\$0.01
EPS Growth	-114%	242%	125%	5%
PER	41.9x	12.3x	5.5x	5.2x
Dividend Per Share	\$0.000	\$0.000	\$0.003	\$0.009
Dividend Yield	0%	0%	4%	12%
ROE	1%	3%	7%	7%
ROIC	5%	7%	15%	12%
Debt/Equity	4%	0%	0%	0%
Net Interest Cover	nm	nm	nm	nm
Book Value/share	\$0.19	\$0.20	\$0.21	\$0.22
Price/Book Value	0.4x	0.4x	0.4x	0.4x

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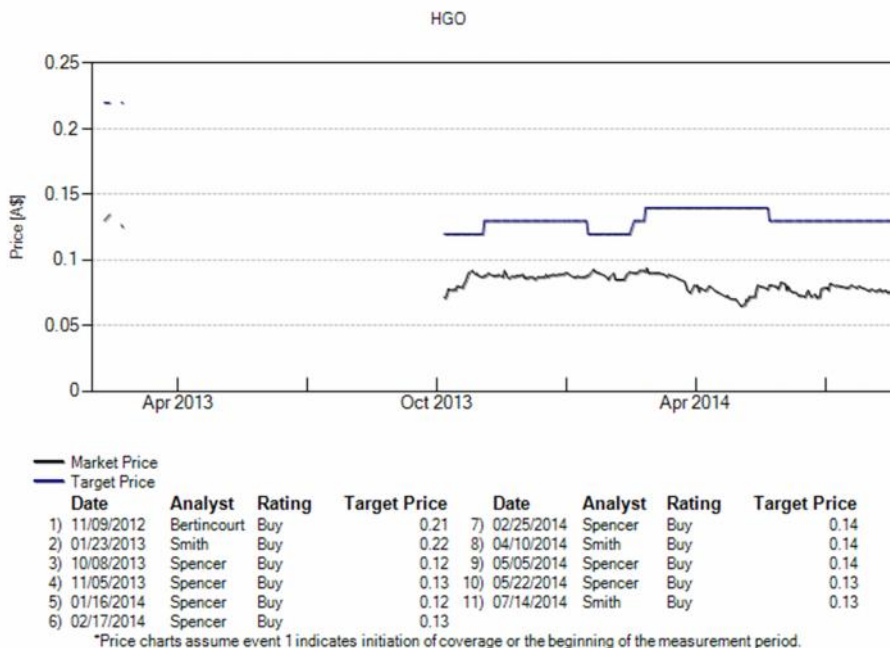
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**Site Visit:** An analyst has visited the company's material operations in South Australia. No payment was received for related travel costs.

**Price Chart:\***



**Distribution of Ratings:  
Global Stock Ratings  
(as of 3 July 2014)**

Rating	Coverage Universe		IB Clients	
	#	%	#	%
Buy	602	61.2%	38	38.2%
Speculative Buy	49	5.0%	32	55.1%
Hold	290	29.5%	17	13.1%
Sell	41	4.2%	3	7.3%
	984	100.0%		

\*Total includes stocks that are Under Review

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**Risk Qualifier:** **SPECULATIVE:** Stocks bear significantly higher risk that typically cannot be valued by normal fundamental criteria. Investments in the stock may result in material loss.

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