



Hillgrove Resources (HGO)

Another Solid Quarter. Further Debt Reduction

BUY

Risk: HIGH

Key Information

Price (\$)	0.078
Target Price (\$)	0.115
Net Present Value (\$)	0.117
Market Cap (\$M)	92.11
GICS Sector	Materials
52 week Hi-Lo (\$)	0.10 - 0.06
Daily Vol (M, mth avg)	2.86
Weight of S&P 200 Index (%)	0.88
Cash (\$M) - 01/07/14	12.10
Debt (\$M) - 01/07/14	25.20
Gearing [ND/(ND+E)] (%)	5.42
Forecast Total Return (%)	47.44

Investment Fundamentals

YE 31 Jan	FY13A	FY14A	FY15E	FY16E
Sales (\$M)	109.5	139.2	178.8	170.9
EBITDA (\$M)	3.7	37.3	52.1	31.8
Margin (%)	3.4	26.8	29.2	18.6
NPAT (\$M)	-13.3	1.5	7.3	-1.2
EPS (cps)	-1.1	0.1	0.6	-0.1
EPS Growth (%)	n.a.	n.a.	387.3	n.a.
DPS (cps)	0.0	0.0	0.0	0.2
Franking (%)	0.0	0.0	0.0	100.0

Ratio Analysis

YE 31 Jan	FY13A	FY14A	FY15E	FY16E
PE (x)	-6.9	61.6	12.6	-77.0
Yield (%)	0.0	0.0	0.0	2.2

HGO vs S&P/ASX Market Index



Performance	1 Mth	3 Mth	12 Mth
Absolute (HGO) (%)	-1.3	-3.7	-2.5
Rel to Market (%)	-2.2	-6.3	-12.5

Major Shareholders

	%
Perennial Value	12.5
Platinum Partners	8.4
Renaissance	7.4
Colonial First State	5.5
Freemont Metals & Concentrates	4.7

Directors and Management

Hon. Dean Brown	Non-Executive Chairman
Greg Hall	CEO & Managing Director
Douglas Snedden	Non-Executive Director
Edwin Zemancheff	Non-Executive Director
John Gooding	Non-Executive Director
John Quirke	Non-Executive Director
Russell Middleton	CFO
Shanthi Smith	Company Secretary
Steven McClare	General Manager, Kanmantoo

Event

July quarterly activities report.

Highlights

- Quarterly Mining & Operational Performance:** HGO has delivered another solid quarter of production at Kanmantoo, despite the impact of winter rainfalls. This is the third consecutive quarter of solid production numbers since assuming greater control of mining activities. Quarterly copper production of 5,884t was 6% higher than the April quarter (5,554t) on the back of increased mill throughput (838kt vs 757kt in Apr'14). The mined grade delivered to the ROM for the quarter increased to 0.93%, up from the 0.87% achieved in the April quarter. Milled grade declined from 0.80% to 0.76%, due to increased throughput of lower grade material to maintain the higher throughput rate. Copper sales for the quarter generated revenue of A\$46.9m at an average realised copper price of A\$3.74/lb.
- Cost Performance:** C1 costs (mining/processing/transport/shipping and treatment and refining costs (net of by-product credits)) decreased to US\$1.94/lb, an 8% reduction on the previous quarter (Apr'14 US\$2.11/lb). This cost reduction was achieved despite a reduction in the milled grade due to systematic improvements in the operation.
- Guidance:** FY'15 guidance has been adjusted to reflect the change of reporting date (moving from Jan to Dec year-end), resulting in an eleven month reporting period for FY'15. The revised copper production guidance is proportionally in line with previous guidance at 20,500-22,500t of copper in concentrate, although at higher throughput and lower grade. C1 cash cost guidance has reduced from US\$2.10-2.40/lb to US\$2.00-2.20/lb.
- Balance Sheet:** HGO's net debt declined from A\$19.3m (Apr'14) to A\$13.1m as of end of July 2014. We forecast HGO to be in a net cash position by the end of CY'14 which should enable dividend payments to commence in FY'16, with A\$21.3m of franking credits previously accumulated (1.8c/share). Under its newly adopted dividend policy, HGO will aim to maintain a minimum dividend payment payout of 40% of net profit, excluding non-recurring items.
- Capital Management Initiatives:** HGO intends to complete a one for eight share consolidation to create a more appropriate capital structure, reducing the number of shares on issue to ~148m. In conjunction, HGO intends to implement a sale facility to remove around 1,500 unmarketable parcels of shares.

Recommendation

Systematic improvements at Kanmantoo continue to deliver unit cost reductions, allowing significant debt reduction and forecast dividend payments to commence in FY'16. **We maintain our 11.5c/share valuation and BUY recommendation.**

Refer to disclaimer on last page



Financial Summary

Market Valuation Metrics

Recommendation	BUY
Risk	HIGH
Price (A\$)	0.078
Target Price (A\$)	0.115
Net Present Value (A\$)	0.117
Issued Capital (M)	1,180.9
Market Cap (\$m)	92.1
Year End	31 Jan

Investment Statistics

YE 31 Jan	FY13A	FY14A	FY15E	FY16E	FY17E
NPAT (Reported)	(11.8)	1.5	7.3	(1.2)	1.9
NPAT (Adjusted)	(13.3)	1.5	7.3	(1.2)	1.9
EPS (Adj \$)	(0.01)	0.00	0.01	(0.00)	0.00
P/E (x)	n.a.	61.6	12.6	n.a.	47.8
P/NPV (x)	n.a.	0.8	0.7	0.6	0.6
Div (cps)	0.0	0.0	0.0	0.2	0.3
Yield (%)	0.0%	0.0%	0.0%	2.2%	4.3%
Franking (%)	0%	0%	0%	100%	100%
(ND/(ND+E)) (%)	9.4%	9.9%	0.0%	0.0%	0.0%
Net Debt/Equity (%)	10.4%	11.0%	0.0%	0.0%	0.0%
ROE (%)	-6.1%	0.7%	3.0%	-0.5%	0.8%
ROA (%)	-4.0%	0.5%	2.5%	-0.4%	0.7%

Profit & Loss Statement (A\$m)

YE 31 Jan	FY13A	FY14A	FY15E	FY16E	FY17E
Revenue	109.5	139.2	178.8	170.9	157.0
Revenue growth (%)	na	27.0%	28.5%	(4.4%)	(8.1%)
EBITDA	3.7	37.3	52.1	31.8	33.0
EBITDA margin (%)	3.4%	26.8%	29.2%	18.6%	21.0%
Depreciation & Amortization	(26.5)	(29.2)	(37.5)	(31.7)	(29.5)
EBIT	(23.5)	8.2	12.7	(2.0)	1.5
EBIT margin (%)	(21.5%)	5.9%	7.1%	(1.2%)	1.0%
Net interest	(6.5)	(5.9)	(2.2)	0.3	1.3
Pretax profit	(19.1)	2.2	10.4	(1.7)	2.8
Tax	8.8	(2.1)	(3.1)	0.5	(0.8)
Reported NPAT	(11.8)	1.5	7.3	(1.2)	1.9
Significant items	(1.6)	0.0	0.0	0.0	0.0
Normalised NPAT	(13.3)	1.5	7.3	(1.2)	1.9
NPAT margin (%)	(12.2%)	1.1%	4.1%	(0.7%)	1.2%

Cashflow Statement (A\$m)

YE 31 Jan	FY13A	FY14A	FY15E	FY16E	FY17E
EBITDA	3.7	37.3	52.1	31.8	33.0
Working Capital Investment (Inc)/Dec	5.7	(23.1)	0.0	12.6	(0.2)
Gross Cash Flow	9.4	14.2	52.2	44.4	32.8
Net interest (paid)/received	(6.5)	(2.8)	(2.2)	0.3	1.3
Tax Paid	0.0	0.0	0.0	0.0	0.0
Other	28.6	2.4	0.0	0.0	0.0
Operating cashflow	31.5	13.8	49.9	44.7	34.1
Investing Activities	(45.7)	(22.2)	(28.3)	(26.6)	(18.3)
Free Cash Flow	(14.2)	(8.5)	21.6	18.0	15.7
Equity raised/options exercised	17.8	10.8	0.0	0.0	0.0
Debt Raised/(paid)	15.0	(10.9)	(28.5)	(11.1)	0.0
Dividends paid	0.0	0.0	0.0	(2.0)	(4.0)
Other	(11.9)	(2.4)	0.0	0.0	0.0
Financing cashflow	20.9	(2.5)	(28.5)	(13.1)	(4.0)
Net change in cash	6.7	(11.0)	(6.9)	4.9	11.7

Balance Sheet (A\$m)

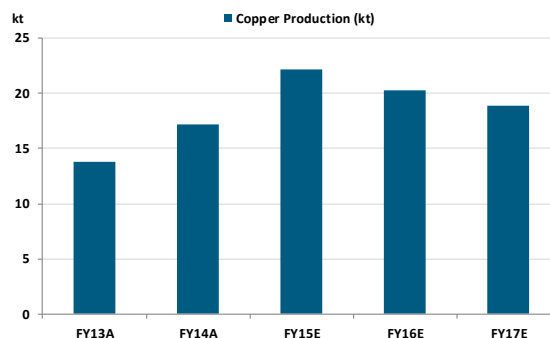
YE 31 Jan	FY13A	FY14A	FY15E	FY16E	FY17E
Cash	27.4	16.5	11.5	16.4	28.2
Property, Plant & Equipment	260.6	256.2	232.3	225.2	211.9
Deferred Tax Asset	12.9	13.8	10.7	11.2	10.4
Other	35.1	35.7	41.0	28.9	27.7
Total assets	336.0	322.2	295.5	281.8	278.3
Debt	50.3	41.7	11.1	0.0	0.0
Other	65.1	52.0	42.9	43.4	42.0
Total liabilities	115.4	93.7	54.0	43.4	42.0
Total shareholders equity	220.6	228.5	241.5	238.3	236.3

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Production (kt)

YE 31 Jan	FY13A	FY14A	FY15E	FY16E	FY17E
Kanmantoo	13.7	17.2	22.1	20.3	18.9
Other	0.0	0.0	0.0	0.0	0.0
Total	13.7	17.2	22.1	20.3	18.9



Cash Costs Summary (US\$/lb)

YE 31 Jan	FY13A	FY14A	FY15E	FY16E	FY17E
C1 Cash Costs	2.19	2.37	2.04	2.28	2.23
Total Costs	3.20	3.15	2.77	2.94	2.89

Total Resources & Reserves

Resources	Mt	Cu (%)	Au (g/t)	Ag (g/t)	Cu (kt)
Total - In Situ	31.2	0.80	0.15	2.2	256.6
Total - Stockpiles	1.6	0.37	n.a.	n.a.	5.9
Total Kanmantoo	32.8	0.80	0.15	2.2	262.6

Reserves	Mt	Cu (%)	Au (g/t)	Ag (g/t)	Cu (kt)
Total - In Situ	20.7	0.73	0.18	1.9	150.3
Total - Stockpiles	1.4	0.46	na	na	6.4
Total Kanmantoo	22.1	0.71	0.18	1.9	156.9

Base Case Assumptions*

YE 31 Jan	FY'13A	FY'14E	FY'15E	FY'16E	FY'17E
Copper Price (US\$/t)	8,068	7,348	6,901	6,867	6,957
A\$:US\$	1.0339	0.9498	0.9000	0.8625	0.8700

* Bloomberg & Consensus Economics

Sum of the Parts Valuation

	\$m	/Share
Kanmantoo	159.7	0.135
Hedging	9.7	0.008
Corporate Costs	-23.5	-0.020
Net Debt/Cash	-13.1	-0.011
Other/Exploration	5.0	0.004
Total	137.9	0.117

Sensitivity Analysis - Changes in Copper Price

Copper Price (US\$/t) & Spot FX - In Perpetuity	DCF	/share
Base Case Assumptions	138	0.117
\$6,500	48	0.041
\$6,750	71	0.061
\$7,000	94	0.080
\$7,098 (Spot)	103	0.088
\$7,500	140	0.119
\$8,000	175	0.148

Sensitivity Analysis - Changes in Discount Rate

Discount Rate	DCF	/share
7%	156	0.132
8%	149	0.127
9%	144	0.122
10% (Base Case)	138	0.117
11%	133	0.113
12%	128	0.108
13%	123	0.104

Operational & Cost Performance

HGO has delivered another solid quarter of production at Kanmantoo, despite the impact of winter rainfalls. This is the third consecutive quarter of solid production numbers since assuming greater control of mining activities. Quarterly copper production of 5,884t was 6% higher than the April quarter (5,554t) on the back of increased mill throughput (838kt vs 757kt in Apr'14). The mined grade delivered to the ROM for the quarter increased to 0.93%, up from the 0.87% achieved in the April quarter. Milled grade declined from 0.80% to 0.76%, due to increased throughput of lower grade material to maintain the higher throughput rate. Copper sales for the quarter generated revenue of A\$46.9m at an average realised copper price of A\$3.74/lb.

Table 1: Kanmantoo Production Statistics

	Units	Jan'13	Apr'13	Jul'13	Oct'13	Jan'14	Apr'14	Jul'14
Ore to ROM	kt	639	689	555	656	733	812	680
Waste Mined	kt	3,650	2,728	2,158	1,658	3,483	4,447	3,643
Total Mined	kt	4,289	3,417	2,713	2,314	4,216	5,259	4,323
Milled Grade	% Cu	0.70%	0.67%	0.67%	0.63%	0.85%	0.87%	0.76%
Ore Milled (kt)	kt	601	708	720	756	760	757	838
Milled Grade	%Cu	0.62%	0.57%	0.54%	0.63%	0.85%	0.80%	0.76%
Copper Recovery	%	90.1%	89.1%	89.5%	90.7%	92.4%	92.1%	91.9%
Concentrate Produced	t	15,827	15,510	15,699	19,161	25,053	24,335	25,621
Concentrate Grade	% Cu	22.7%	23.1%	22.0%	22.5%	23.3%	22.8%	23.0%
Contained Metal	Cu t	3,595	3,590	3,450	4,306	5,838	5,554	5,884
Concentrate Sold	t	16,182	16,184	14,134	18,919	24,812	24,425	25,621

Source: Hillgrove Resources & Shaw Stockbroking

C1 costs (mining/processing/transport/shipping and treatment and refining costs (net of by-product credits)) decreased to US\$1.94/lb, an 8% reduction on the previous quarter (Apr'14 US\$2.11/lb). This cost reduction was achieved despite a reduction in the milled grade from 0.8% to 0.76% due to systematic improvements in the operation.

Table 2: Kanmantoo Cost Performance

		Jan'13	Apr'13	Jul'13	Oct'13	Jan'14	Apr'14	Jul'14
Mining	US\$/lb	1.15	1.17	1.02	1.56	0.98	1.11	0.89
Processing	US\$/lb	0.94	0.97	0.84	0.65	0.50	0.47	0.52
Other	US\$/lb	0.19	0.24	0.28	0.25	0.15	0.16	0.19
Total Onsite	US\$/lb	2.28	2.38	2.14	2.46	1.63	1.74	1.60
Transport & Shipping	US\$/lb	0.18	0.18	0.17	0.16	0.16	0.16	0.17
TC/RC	US\$/lb	0.37	0.39	0.44	0.41	0.39	0.42	0.41
Total Offsite	US\$/lb	0.55	0.57	0.61	0.57	0.55	0.58	0.58
Byproduct Credits	US\$/lb	-0.49	-0.54	-0.35	-0.23	-0.18	-0.21	-0.24
Total C1 Costs	US\$/lb	2.34	2.41	2.40	2.80	2.00	2.11	1.94
Royalties	US\$/lb	0.06	0.05	0.04	0.04	0.04	0.04	0.04
D&A	US\$/lb	0.30	0.86	0.75	0.72	0.68	0.71	0.78
Total Costs	US\$/lb	2.70	3.32	3.19	3.56	2.72	2.86	2.76

Source: Hillgrove Resources & Shaw Stockbroking

Guidance

FY'15 guidance has been adjusted to reflect the change of reporting date, resulting in an eleven month reporting period for FY'15. The revised copper production guidance is proportionally in line with previous guidance at 20,500-22,500t of copper in concentrate, although at higher throughput and lower grade. C1 cash cost guidance has reduced from US\$2.10-2.40/lb to US\$2.00-2.20/lb.

Table 3: FY'15 Guidance Summary

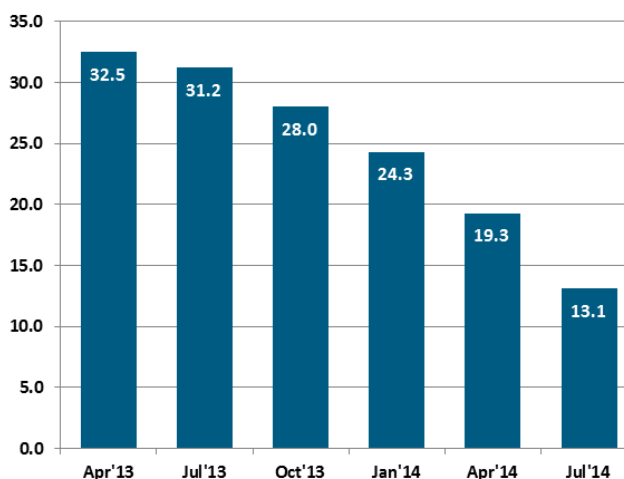
	Units	HGO Guidance	Shaw Estimates
Ore Mined	(kt)	2,850 - 3,000	2,992
Ore Processed	(kt)	2,900 - 3,000	2,995
Processed Ore Grade	(% Cu)	0.76 - 0.81%	0.80%
Copper Recovery	(%)	91.5 - 92.5%	92.0%
Copper Produced	(t)	20,500 - 22,500	22,117
Gold Produced	(oz)	6,000 - 7,800	5,804
C1 Cash Cost	US\$/lb	2.00 - 2.20	2.04

Source: Hillgrove Resources & Shaw Stockbroking

Balance Sheet

HGO's net debt declined from A\$19.3m (Apr'14) to A\$13.1m as of end of July 2014. We forecast HGO to be in a net cash position by the end of CY'14 which should enable dividend payments to commence in CY'15, with A\$21.3m of franking credits previously accumulated (1.8c/share). Under its newly adopted dividend policy HGO will aim to maintain a minimum dividend payment payout of 40% of net profit, excluding non-recurring items.

Chart 1: HGO Net Debt Profile (A\$m)



Source: Hillgrove Resources & Shaw Stockbroking

Shaw Commentary

Systematic improvements at Kanmantoo continue to deliver unit cost reductions, allowing significant debt reduction and forecast dividend payments to commence in FY'16. **We maintain our 11.5c/share valuation and BUY recommendation.**



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Rating Classification

Buy	Expected to outperform the overall market
Hold	Expected to perform in line with the overall market
Sell	Expected to underperform the overall market
Not Rated	Shaw has issued a factual note on the company but does not have a recommendation

Risk Rating

High	Higher risk than the overall market – investors should be aware this stock may be speculative
Medium	Risk broadly in line with the overall market
Low	Lower risk than the overall market.

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