

## Hillgrove Resources Ltd

Initiating coverage of near-term copper producer

**Recommendation:**  
**Buy**

Risk: High

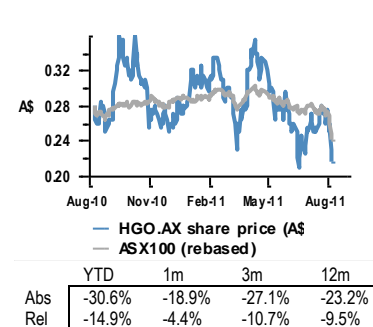
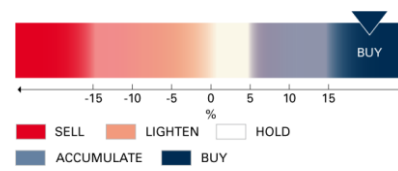
HGO.AX

\$0.25

Price Target: \$0.43

We initiate coverage of Hillgrove Resources Limited (HGO) with a Buy recommendation, a high risk rating and a July 2012 price target of \$0.43. Hillgrove is currently constructing its Kanmantoo copper-gold mine in South Australia. The company has indicated that first production remains on track for November 2011 and that construction is 'on time and on budget'.

- Hillgrove should produce around 19kt of payable copper per annum as well as about 8koz of gold and about 150koz of silver. Though the reserve grade is relatively low at 0.85% copper, average cash costs of around US\$1.61/lb after credits allow for solid margins at current copper prices, highlighting Kanmantoo's leverage to copper prices. Reserve life is around 6.5 years, though the deposit remains open along strike and at depth. Drilling is currently testing these extensions which may lead to either mine life additions and/or production expansions.
- We expect HGO to be rerated as it transitions from a developer to producer and becomes cashflow positive during the first half of the 2012 calendar year. Such a rerating can be evidenced by the average enterprise value per resource tonne of copper for producers of c.\$485/t versus \$375/t for developers. HGO is currently trading at \$410/t.
- Our July 2012 price target of \$0.43 per share is dominated by our discounted cashflow for Kanmantoo of \$0.41cps. We have a conservative production profile, though we assume an extra two years' mine life for likely resource conversion. Based on our modelling, Hillgrove should have steady state operational cashflow of +\$70m over the initial years, falling to +\$50m as the copper price falls. Peak PER is 6.0 in 2018.
- HGO also has two exploration projects in Indonesia. Though in the early stages, work to date has indicated that the projects appear to have good potential to host a sizeable copper/gold deposit. We include \$20m of value for these projects in our net present value.
- Key risks for HGO include, but are not limited to, changes in exchange rates and commodity prices, ore body risk, cost escalation, and to a lesser degree, construction risk.
- For further information, please contact your adviser.



### Hillgrove Resources Ltd (Reuters: HGO.AX, Bloomberg: HGO AU)

| Year-end Jan (\$)            | FY10A  | FY11A   | FY12E  | FY13E   | FY14E |
|------------------------------|--------|---------|--------|---------|-------|
| Total Revenue (\$ mn)        | 96     | 4       | 26     | 167     | 194   |
| EBITDA (\$ mn)               | 90.3   | -27.5   | 7.3    | 78.0    | 96.7  |
| Net profit after tax (\$ mn) | 55.59  | -14.17  | -1.86  | 41.19   | 55.49 |
| EPS (\$)                     | 0.116  | -0.017  | -0.002 | 0.052   | 0.070 |
| P/E (x)                      | 2.1    | NM      | NM     | 4.7     | 3.5   |
| Cash flow per share (\$)     | -0.024 | -0.080  | -0.004 | 0.082   | 0.134 |
| Dividend (\$)                | 0.00   | 0.00    | 0.00   | 0.00    | 0.00  |
| Net Yield (%)                | 0.0%   | 0.0%    | 0.0%   | 0.0%    | 0.0%  |
| Normalised* EPS (\$)         | 0.125  | -0.020  | -0.002 | 0.052   | 0.070 |
| Normalised* EPS chg (%)      | -      | -116.3% | 88.5%  | 2312.1% | 34.7% |
| Normalised* P/E (x)          | 2.0    | NM      | NM     | 4.7     | 3.5   |

Source: Company data, Bloomberg, Ord Minnett estimates.

| Company Data                  |             |
|-------------------------------|-------------|
| 52-week range (\$)            | 0.37 - 0.20 |
| Market capitalisation (\$ bn) | 0.19        |
| Market capitalisation (\$ mn) | 0.20        |
| Fiscal Year End               | Jan         |
| Price (\$)                    | 0.25        |
| Date Of Price                 | 11 Aug 11   |
| Shares outstanding (mn)       | 793.7       |
| ASX100                        | 3,375.5     |
| ASX200-Ind                    | 5,404.2     |
| NTA/Sh^ (\$)                  | 0.35        |
| Net Debt^ (\$ bn)             | -0.00       |

## Executive Summary

We initiate coverage of Hillgrove Resources Limited with a **Buy** recommendation and a July 2012 price target of \$0.43/share. Our price target is a 12 month roll forward of our sum of parts valuation of \$0.41/share. Our sum of parts valuation is dominated by our DCF (WACC: 10%) valuation for the Kanmantoo copper-gold project of \$0.36/share, with the remainder consisting of exploration (\$0.05/share), corporate costs (-\$0.05/share), net cash (\$0.05/share) and investments (\$0.005/share).

The company is trading at a 47% discount to our \$0.43/share price target and we can see HGO being rerated as it moves into production towards the end of CY2011, and then proves itself a consistent producer.

### Reasons for our Buy recommendation

1. We believe HGO offers good exposure to copper via production from its Kanmantoo mine. The company is currently on track for first production in November 2011 from an open pit operation.
2. The company is one of only a handful of Australian copper focused developers and should be the next ASX listed copper producer. Life of mine average annual production is c.19kt of payable copper metal, 8.0koz of gold and c.150koz of silver. HGO is indicating that average life of mine C1 cash costs should be c.US\$1.61/lb of copper after US\$0.25/lb in gold and silver credits, which whilst towards the higher end of the cost curve, still provides for +US\$2.50/lb margins at current prices.
3. The Kanmantoo deposit has moderate potential for expansion, and is still open along strike and depth. We also view the surrounding area as prospective for additional discoveries, with exploration success potentially leading to either mine life extensions and/or production increases.
4. The Company also has two exploration properties in Indonesia, which whilst early stage, have indications of potential copper and/or gold deposits. We do not believe that the market attributes much value to these assets, partially because work completed on these projects to date has been somewhat slow.

### Risks

The key risks facing HGO are similar to most other mining project developments. These include, but are not limited to:

1. Ore Body Risk - The behaviour of an ore body compared to expectations is often one of the biggest risks facing a mining company and is reduced mainly by detailed drilling and metallurgical test work. Kanmantoo has been mined previously and the deposit is relatively well understood, reducing the risk of the ore body underperforming. However, the low grade nature of the deposit, credits notwithstanding, allows for less room for error.
2. Construction Risk - Risks associated with the construction process including cost escalation in capital items as well as delays in the construction also impacting on costs. As the construction at Kanmantoo is at an advanced stage, the likelihood of significant delays and cost overruns should be relatively low.

3. Commissioning Risk - The commissioning of the processing plant can often take longer than planned. However, the plant is relatively simple, with only one extraction process to produce the copper concentrate. Hillgrove has budgeted approximately six months to complete commissioning.
4. Commodity Price and Exchange Rate Risk – HGO has somewhat mitigated commodity price and exchange rate fluctuations over the first few years of production from Kanmantoo by hedging approximately half its copper output in \$. The hedge book involves flat forwards totalling c.40kt of payable copper, delivered at a rate of c.10kt per annum at c.\$8,320/t.
5. Permitting Risk – All necessary construction and operating permits have been received and construction is underway.
6. Financing Risk – Barring any significant capital cost blowouts, HGO has sufficient funding to complete construction for Kanmantoo via cash and a debt facility.

## Company overview

### Background

Hillgrove is an advanced developer, focusing on the construction of its Kanmantoo mine, located 55km from Adelaide in South Australia, with a view to commencing production before the end of CY2011.

The company also has two highly prospective exploration projects in Indonesia, as well as a number of other gold and base metals projects in South Australia. In addition, HGO holds c. 85% of ASX listed junior explorer InterMet Resources Limited [ASX: ITT].

Figure 1: Main HGO Projects



Source: Hillgrove Resources Limited

### Kanmantoo (HGO 100%)

#### History

The Kanmantoo copper project is located in the Adelaide Hills region. The region has a long history of copper mining and prospecting. Small scale mining first occurred in the mid 1840's, continuing for approximately 30 years until copper prices fell significantly, forcing operations in the region to cease.

The area saw periodic prospecting through to the late 1960s, when Kanmantoo Mines Limited (KML), discovered the main Kanmantoo deposit. Production from the mine began in 1970 via an open pit, continuing through to 1976. Production from the pit was 4.05Mt at an average grade of 0.9% copper, yielding 39,000t of copper metal. Low copper prices, industrial disputes, as well as high costs saw the operation close in 1976.

#### Initial Hillgrove Work

Hillgrove acquired the Mining Lease which covered the Kanmantoo Mine in 2004. In addition, HGO earned into, or acquired 100% of, a number of tenements covering c.500km<sup>2</sup> along strike and surrounding Kanmantoo between 2003 and 2008.

The project has a number of infrastructure benefits including being close to mains power, use of recycled water from the township of Mt Barker, as well as being only c.50km from port and 3km from the main highway.

The Company commenced field exploration in early 2004, and announced a resource for Kanmantoo in late 2004. The Indicated and Inferred Resource of 18.4Mt at 1.1% Cu and 0.2g/t Au more than doubled the previous estimate of 8.5Mt. With ongoing drilling, HGO steadily increased the resource base to its current level of 32.2Mt at 0.9% copper and 0.2g/t gold for 292.2kt of contained copper metals and 191.1koz of gold.

Figure 2: Historic Kanmantoo Open Pit



Source: Hillgrove Resources Limited company presentation

Hillgrove completed a positive prefeasibility study (PFS) into recommending mining at Kanmantoo in mid 2006. Following on from the PFS, HGO undertook a definitive feasibility study (DFS), which was completed in November 2007.

The DFS indicated a base case NPV of \$72m based on copper forward curves at the time, US\$780/oz gold price and \$16.70 for silver price, yielding a project IRR of 21%.

The mineralisation was to be extracted via open pit mining using conventional truck and shovel, and drill and blast methods. The open pit would be a cutback and expansion of the existing pit as well as a number of new smaller open pits. The plant was envisaged to be a conventional flotation system.

The operation was modelled to have a six and a half year mine life, based on a 2Mtpa plant and 11.1Mt ore reserve, producing a copper concentrate product to be shipped out through the Adelaide port. Preproduction capital costs were \$130m. First production was envisaged to commence in 2Q CY2009.

### **Development Plan**

After the completion of the DFS, the global financial crisis and consequent reduction in financing options, as well as the collapse in the copper price, the plans to develop Kanmantoo were put on hold and the company sought a development partner to help progress the project.

Post the DFS, the company continued near mine exploration and continued to increase the size and confidence of the Kanmantoo resource. In addition, the company continued the permitting process for the project.

In August 2009, Hillgrove acquired the Lennard Shelf Pillara Mine's process plant and equipment from Lennard Shelf Pty. Limited (Teck Resources Limited/Xstrata plc). The purchase price for the plant was c.\$10.5m. The cost to dismantle, transport and reconstruct the plant at Kanmantoo is estimated to be c.\$57m.

The Pillara Mine was a lead/zinc operation in the Kimberley region of WA that operated between 1998 and 2008 then placed on care and maintenance. The throughput rate was 2.7Mtpa. The plant had treated lead-zinc ore via a standard flotation process in two lines (zinc 80% and lead 20%). Hillgrove deemed the plant suitable to treat the Kanmantoo copper ore using a similar flotation process. The purchase included all of the plant and equipment including the float circuit, ball and SAG mills, offices, as well as crusher, spares and other infrastructure.

Figure 3: Pillara Processing Plant at Lennard Shelf, Pre Removal by HGO



Source: Hillgrove Resources Limited company presentation

Both the flotation lines have been installed at Kanmantoo, however, only the former zinc line (80% of the plant capacity) will be initially utilized. The former lead line (20%) allows for a potential cost effective expansion of capacity. However, this expansion is subject to the addition of further reserves.

The company received all relevant approvals for Kanmantoo in April 2010. With the strong recovery in the copper price and financial markets, HGO looked to commence the redevelopment of the project by itself and no longer sought a development partner.

Post the DFS, the company also updated operating and capital costs, re-optimised the open pits and refined the designs, reviewed mining rates, head grades, and cut-off grades ahead of the planned final investment decision (FID). Following these refinements as well as additional drilling, the company reached FID in October 2010.

With the new plant and updated resources and reserves, Hillgrove is now looking at 2.4Mtpa of ore throughput, generating c.70kt of copper concentrate per annum. The planned concentrate grade is 27.5% copper, 3.5g/t gold and 66g/t silver. Payable metal production should be c.19kt of copper, c.8koz of gold and c.150koz of silver per annum. Hillgrove has a life of mine concentrate off take agreement with J.P Morgan Metals & Concentrates LLC. Terms have been set for the first 80kt of copper in concentrate, and then terms will be market based.

The treatment plant has a 2.4Mtpa throughput capacity, however, Hillgrove believes that by debottlenecking the plant, mainly in the crushing and grinding circuits, the plant should be able to achieve up to 2.7Mtpa. In addition, Hillgrove believes that the plant can be expanded further to 3.5Mtpa for a capital cost of \$12m. However, this is dependent on further resource and reserve additions.

**Table 1: Kanmantoo project Parameters**

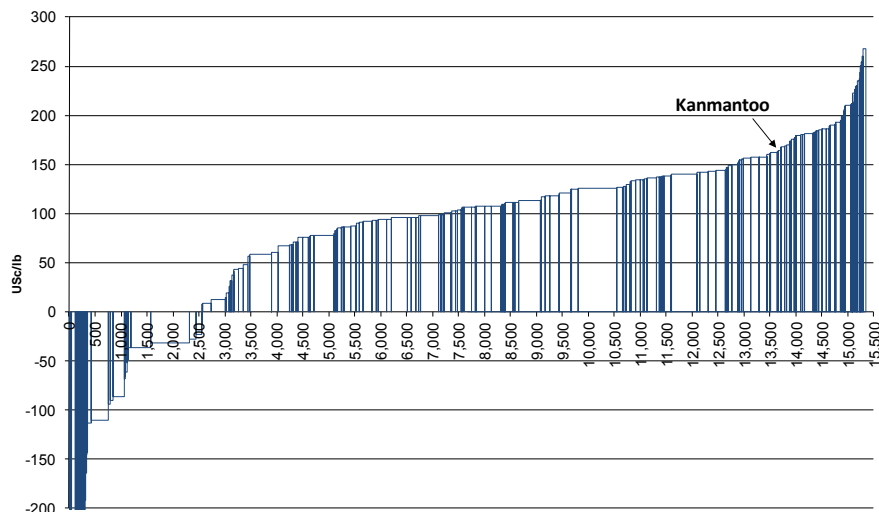
| Parameter                          | Value |
|------------------------------------|-------|
| Annual Plant Throughput (Mtpa)     | 2.4   |
| Reserve Grades                     |       |
| Copper (%)                         | 0.85% |
| gold (g/t)                         | 0.17  |
| silver (g/t)                       | 3.10  |
| Annual Concentrate production (kt) | 70.5  |
| Annual Payable Production          |       |
| Copper (kt)                        | 19.4  |
| gold (koz)                         | 7.9   |
| silver (koz)                       | 160   |
| Unit costs ore milled (\$/t)       | 41    |
| Cash Costs (\$/lb)                 | 1.90  |
| Cash Costs (US\$/lb)               | 1.61  |
| Prestart Capex (\$m)               | 144   |
| Mine Life (yrs)                    | 6.5   |

Source: Hillgrove Resources Limited, Ord Minnett estimates.

Proposed capital and start-up costs are \$144m. Hillgrove has indicated that average life of mine operating costs are c.US\$1.61/lb of payable copper, after c.US\$0.25/lb of by-product credits. These credits are calculated using US\$900/oz gold and US\$13/oz silver.

As can be seen, Kanmantoo sits at the upper end of the world production cost curve. This is primarily due to its low grade and moderate by-product credits.

Figure 4: Copper Mine Cost Curve (Q1 2011 annualised)



Source: AME

We understand that Hillgrove has a State Government net smelter return royalty of 1.5% for the first five years, which then increases to 5%.

Table 2: Capital Budget and Expenditure as at 31 May 2011

|                             | Budgeted<br>Total Capex (\$m) | FID Capex                             |                     | Construction Period Costs               |  |
|-----------------------------|-------------------------------|---------------------------------------|---------------------|---|--|
|                             |                               | Capex spent to FID<br>(31/8/10) (\$m) | Capex for FID (\$m) | Spend Period 1/9/10 to<br>31/5/11 (\$m) | Capex Remaining as at<br>31/5/11 (\$m) |
| Pre-strip                   | 26.7                          | -                                     | 26.7                | 14.5                                    | 12.2                                   |
| Mining, TSF & Grade Control | 17.1                          | 0.1                                   | 17.0                | 10.1                                    | 6.9                                    |
| Pillara processing plant    | 67.9                          | 21.3                                  | 46.6                | 33.1                                    | 13.5                                   |
| Other infrastructure        | 9.3                           | 0.4                                   | 8.9                 | 7.6                                     | 1.3                                    |
| Project management costs    | 13.2                          | 1.1                                   | 12.1                | 6.1                                     | 6.0                                    |
| Contingency                 | 10.0                          |                                       | 10.0                |   | 10.0                                   |
| <b>Total</b>                | <b>144.2</b>                  | <b>22.9</b>                           | <b>121.3</b>        | <b>71.3</b>                             | <b>50.0</b>                            |

Source: Hillgrove Resources Limited

### Project Finance Secured

To fund the budgeted \$144m costs, HGO undertook financing at the time of FID. This involved a \$30m project finance facility and \$20m in bonds and guarantee facilities; as well as a \$65m institutional equity raising. The company also had c.\$65m cash (as at the end of October 2010).

As part of the project finance facility, the company also entered into a 40kt hedging package. The hedges are flat forwards and require the delivery of c.10kt of copper metal per annum at c.\$8,320/t from 2H CY2012.

### Construction on Track

Mining commenced in early 2011 with ore being stockpiled ready for the completion of the processing plant, which is scheduled for the end of September 2011. Practical completion is targeted for the start of November, and first concentrate production shortly thereafter.

Figure 5: Planned Development and Construction Timetable

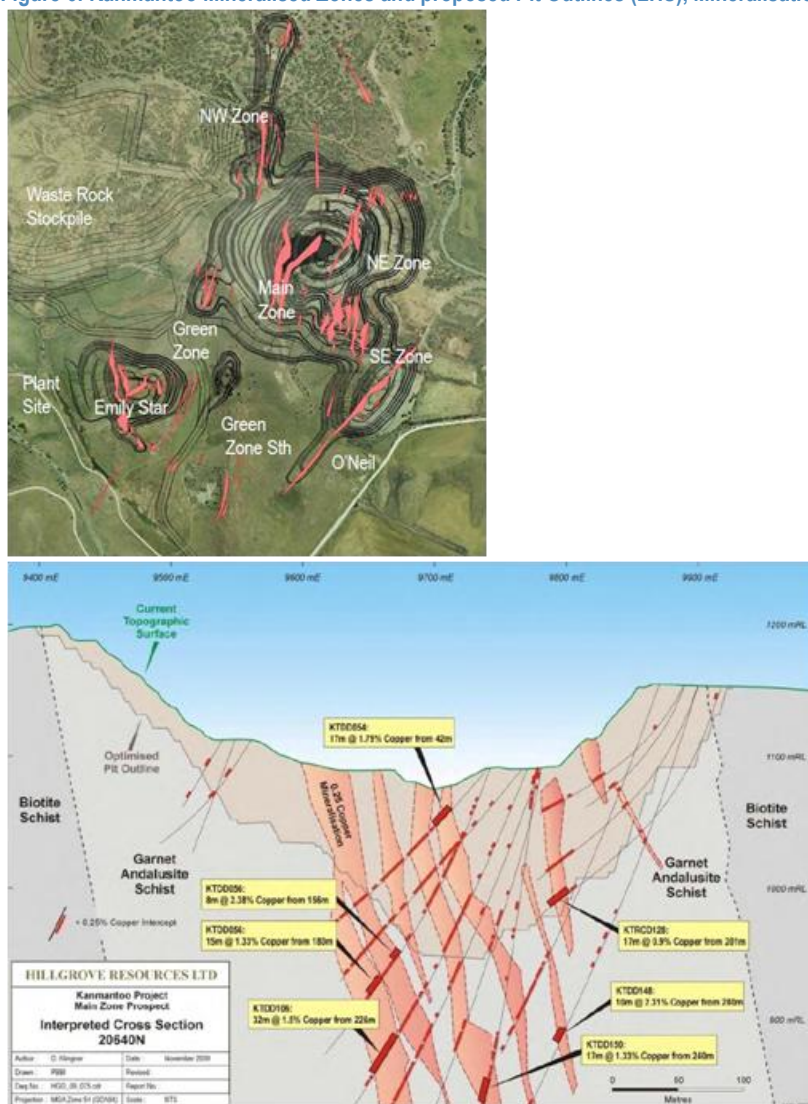


Source: Hillgrove Resources Limited company presentation

### Exploration Ongoing

The region is considered to be prospective for additional copper-gold ore bodies, however, most exploration to date has focussed on the area immediately around Kanmantoo. Hillgrove holds c.500km<sup>2</sup> of tenements in the area.

Figure 6: Kanmantoo Mineralised Zones and proposed Pit Outlines (LHS), Mineralisation Cross Section (RHS)



Source: Hillgrove Resources Limited company presentation

The company is currently reviewing exploration completed to date with a view to prioritising targets within the Kanmantoo mining lease. \$1.5m has been budgeted for near-mine exploration in 2011, with a priority to increase resources and reserves. The Company believes that the deposit remains open along strike and down dip and c.5,000m of RC and 400m of diamond drilling have been planned to target these extensions. The company is also using geophysical techniques to refine both near mine and regional targets. Following the drilling, the next resource and reserve update will be in early in 2012.

Table 3: Kanmantoo Resource (calculated as at 8/12/2008 using 0.25% Cu cut-off)

| Class        | Tonnes<br>Mt | Cu<br>%    | Au<br>g/t  | Ag<br>g/t  | Cu Metal<br>kt | Au Metal<br>Koz | Ag Metal<br>koz |
|--------------|--------------|------------|------------|------------|----------------|-----------------|-----------------|
| Measured     | 2.3          | 0.9        | 0.2        | 3.5        | 21.7           | 12.1            | 255.3           |
| Indicated    | 22.5         | 0.9        | 0.2        | 3.3        | 204.4          | 139.9           | 2,381.2         |
| Inferred     | 7.4          | 0.9        | 0.2        | 2.9        | 66.1           | 39.1            | 677.1           |
| <b>Total</b> | <b>32.2</b>  | <b>0.9</b> | <b>0.2</b> | <b>3.2</b> | <b>292.2</b>   | <b>191.1</b>    | <b>3,313.6</b>  |

Source: Hillgrove Resources Limited

**Table 4: Kanmantoo Reserve (calculated as at 4/5/2010)**

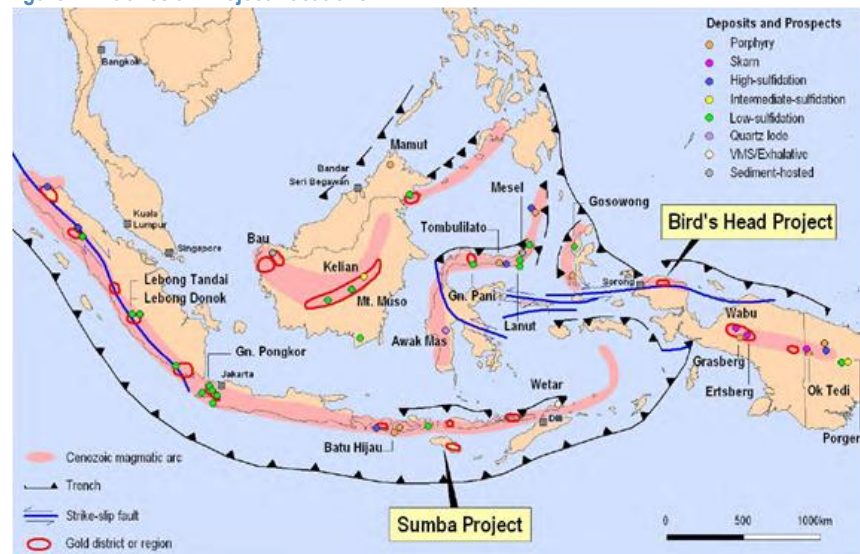
| <b>Class</b> | <b>Tonnes<br/>Mt</b> | <b>Cu<br/>%</b> | <b>Au<br/>g/t</b> | <b>Ag<br/>g/t</b> | <b>Cu Metal<br/>kt</b> | <b>Au Metal<br/>koz</b> | <b>Ag Metal<br/>koz</b> |
|--------------|----------------------|-----------------|-------------------|-------------------|------------------------|-------------------------|-------------------------|
| Proven       | 2.3                  | 0.87            | 0.13              | 3.20              | 20.0                   | 9.6                     | 236.6                   |
| Probable     | 12.5                 | 0.84            | 0.18              | 3.10              | 105.0                  | 72.3                    | 1,245.8                 |
| <b>Total</b> | <b>14.8</b>          | <b>0.85</b>     | <b>0.17</b>       | <b>3.10</b>       | <b>125.8</b>           | <b>80.9</b>             | <b>1,475.1</b>          |

Source: Hillgrove Resources Limited, Ord Minnett estimates

## Indonesian Exploration Projects

Hillgrove has two projects in Indonesia, Bird's Head and Sumba, covering a total of c.1990km<sup>2</sup>. The Indonesian companies were awarded the permits for both projects in 2008. The Bird's Head Project is on the north western tip of the eastern Indonesian province of West Papua. The Sumba project is located on the island of Sumba, west of Timor.

Figure 7: Indonesian Project Locations



Source: Hillgrove Resources Limited company presentation

### Bird's Head

The Bird's Head Project licence is an Eksplorasi Izin Usaha Pertambangan (IUP), held by PT Akram Resources, in which Hillgrove has an 80% beneficial interest, via a JV agreement. The IUP has a term of six years from March 2010 and covers an area of 992km<sup>2</sup>. The license area is sparsely populated.

Hillgrove is currently in the process of corporatising its interest in PT Akram to an 80% indirect interest (as is possible under the new mining law). Hillgrove is responsible for all exploration and development activities and is sole funding the project up to a decision to mine.

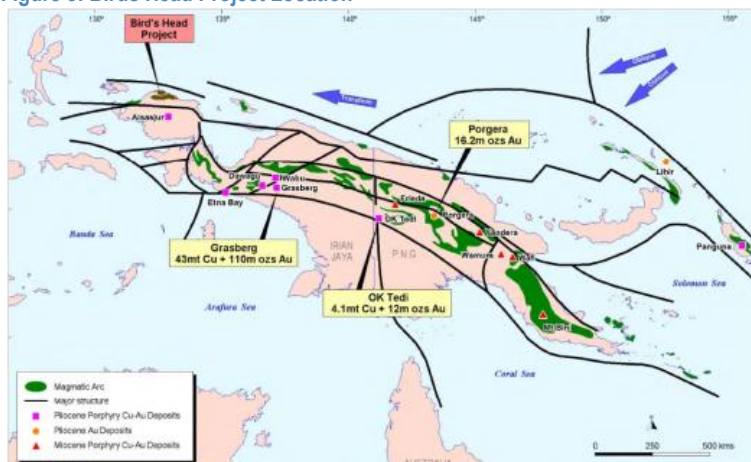
The IUP covers an extensive area of production, protected and conservation forest. However, Hillgrove has limited its surface exploration activities to production and protected forest, and currently has an application to undertake drilling before Indonesian authorities. This drilling will be limited to production forest only.

The company is targeting large scale epithermal and porphyry style gold and/or copper mineralisation. The project covers an area that is interpreted to be the western extension of the New Guinea 'Orogenic Belt'. This orogenic belt contains the world class Ertsberg/Grasberg, Porgera and Ok Tedi copper/gold deposits.

The area was previously explored between 1986 and 1993, during which time, porphyry style copper-gold and epithermal gold mineralisation was identified. This exploration highlighted five major zones. Three zones, Alpha, Bravo and Golf in the southern part of the IUP, are considered prospective for epithermal style gold targets, however, they are located in Conservation

Forest. Two prospects, Foxtrot and Delta in the northern portion of the IUP, are considered prospective for porphyry style copper-gold targets. The current focus is on the Delta prospect.

Figure 8: Birds Head Project Location

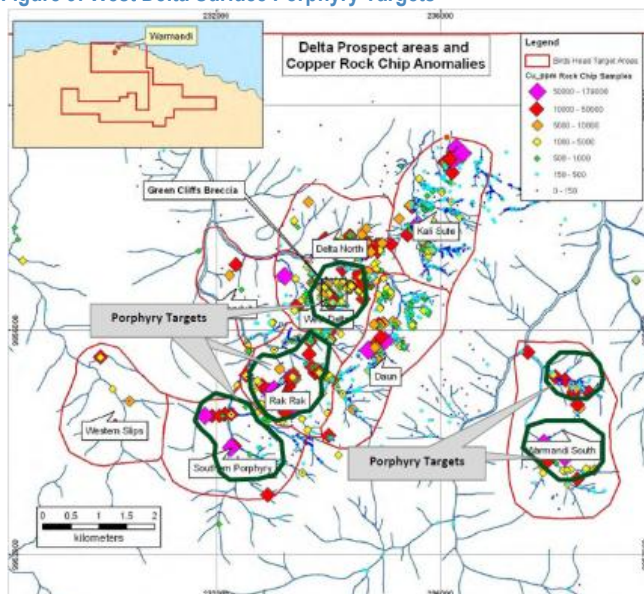


Source: Hillgrove Resources Limited company presentation

At West Delta, Hillgrove has identified strong magnetic anomalies that are associated with intense hydrothermal alteration that may be related to copper mineralisation. The Company has a number of porphyry style targets that it plans to drill. Work to date includes trenching, rock chip sampling and stream sampling which have all identified copper anomalism. Better results from trenching include:

- 32m @ 0.73% Cu incl. 20m @ 0.95% Cu, and
- 52m @ 0.35% Cu incl. 12m @ 0.75% Cu

Figure 9: West Delta Surface Porphyry Targets



Source: Hillgrove Resources Limited company presentation

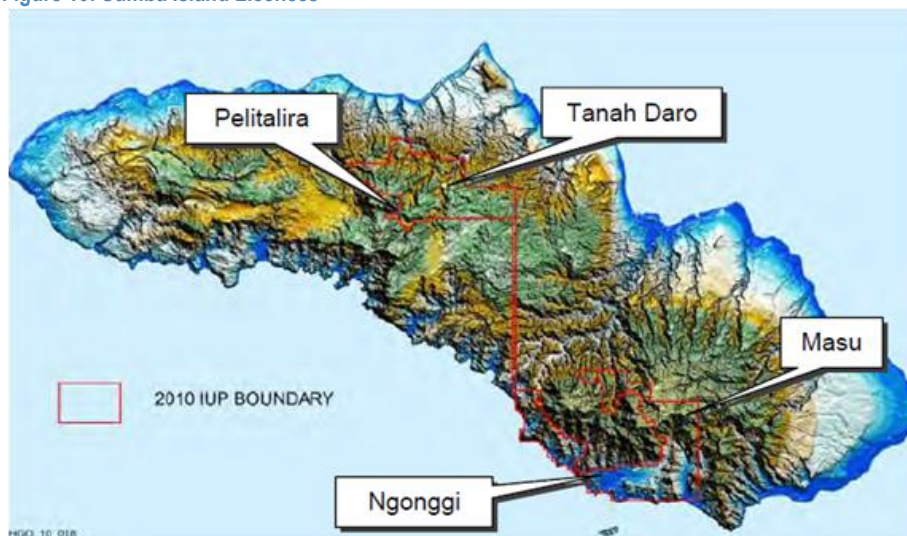
Hillgrove has planned a drilling program to test a number of these targets with drill holes down to c.600m depth. However, the company is currently awaiting the appropriate permitting before mobilising a drill rig to site. In the

meantime, the company is continuing its ground mapping, sampling and trenching in the area.

### Sumba Island

Hillgrove has an indirect 80% interest (via share ownership) in Indonesian company PT Fathi Resources, which holds a ten year IUP on the island of Sumba. Hillgrove is funding all exploration work as well as feasibility studies up to a decision to mine. The IUP covers 999km<sup>2</sup>. The IUP is not located in a forestry area.

Figure 10: Sumba Island Licences



Source: Hillgrove Resources Limited company presentation

Previous work in the area was undertaken by BHP, which combined with work to date by Hillgrove, has identified numerous gold anomalies and occurrences that warranted follow up work. The IUP contains two main project areas; Masu in the south-east and Tanah Daro in the north-central area of the island.

### Masu

At the Masu (South eastern) project area, mapping, sampling, trenching and scout drilling has identified 17 gold targets that require follow up work. Better historical trenching results by BHP include:

- 3m @ 49.38g/t gold
- 4m @ 16.73g/t gold
- 4m @ 6.7g/t gold

More recent trenching has returned:

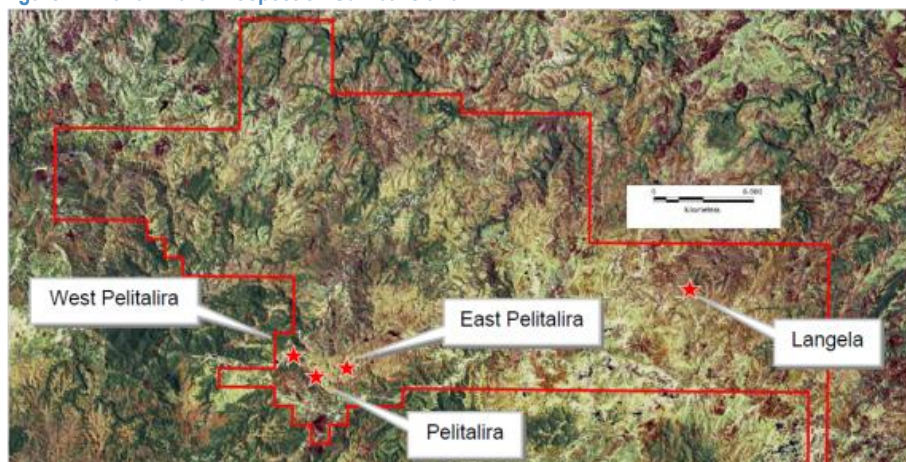
- 22m @ 2.66 g/t gold,
- 80m @ 3.18 g/t gold, and
- 73m @ 4.72 g/t gold

The company has drilling planned to commence soon.

### Tanah Daro

The Tanah Daro project is on the northern part of the IUP. Hillgrove believes that the project is highly prospective for gold and base metals deposits. The company has identified a number of promising prospects at Tanah Daro, including the Pelitalira prospect in the north west of the area.

Figure 11: Tanah Daro Prospect on Sumba Island



Source: Hillgrove Resources Limited company presentation

Recent work by Hillgrove has included soil sampling, trenching, mapping, rock chip sampling of the Waterfall Vein (which returned 72g/t Au, 3.68% Cu and 765g/t Ag), and a 9 hole drill program, as well as geophysical surveys.

The drilling targeted gold and base metal anomalies identified from the trenching and soil sampling. No significant mineralisation was encountered though the drilling intersected zones of hydrothermal alteration, sulphides and brecciation. Such features are often encountered high up in high-sulphidation epithermal mineralised systems. Consequently Hillgrove believes that the potential for mineralisation is deeper than the recent program tested.

Mapping, soil sampling and trenching work is expected to continue over the coming quarters to delineate further drill targets.

### Other Australian Exploration

Outside of the Kanmantoo project area, Hillgrove also has a portfolio of more early stage greenfields exploration projects including:

- Gold exploration at Mt. Rhine, South Australia
- Gold, silver, lead and zinc exploration at Mt. Torrens, South Australia
- Gold, silver, lead and zinc exploration at Aclare, South Australia
- Lead, zinc, copper, gold at Wheal Ellen, South Australia

However, the current focus of the company is on the development of Kanmantoo, and to a lesser extent, exploration in Indonesia.

## Investments

### Eastern Star Gas

In 2003, Hillgrove entered into a 32.5% JV interest in a Narrabri Coal Seam Gas (CSG) project called the Gunnedah Basin Gas Project. In October 2006, Hillgrove swapped its 32.5% interest in the project for 172m Eastern Star Gas Limited [ASX: ESG] shares, equivalent to 19.9% of ESG. In July 2009, HGO then sold this stake to Santos Limited for \$172m in cash. HGO booking a \$94m profit before tax. Hillgrove then used the cash to retire \$49.8m in debt leaving the company with \$127m cash. Following the sale, Hillgrove has no further interest in ESG.

### Intermet Resources Limited

Hillgrove owns 84.8% of Intermet Resources Limited [ASX: ITT]. Intermet is a junior exploration company targeting the identification, exploration and development of bulk commodities in Australia and Indonesia. As at close of business on 5 August 2011, ITT had a market capitalisation of \$1.9m. Hillgrove is reviewing its shareholding in Intermet.

### Silver Swan Group

Hillgrove holds 4.2m ordinary shares in Silver Swan Group Limited [ASX: SWN]. This is approximately 5.3% of SWN's ordinary fully paid shares. SWN is a gold and base metals explorer with projects in the Murchison province, Western Australia and the Gawler Craton, South Australia. As at close of business on 5 August 2011, SWN had a market capitalisation of \$9.0m.

## Financials

Given that Hillgrove is in transition from developer to producer, the previous financials are not representative of the company going forward. Below is our forecast for Hillgrove's P&L and Balance Sheet. Note the company has a January 31 financial year.

**Table 5: P&L**

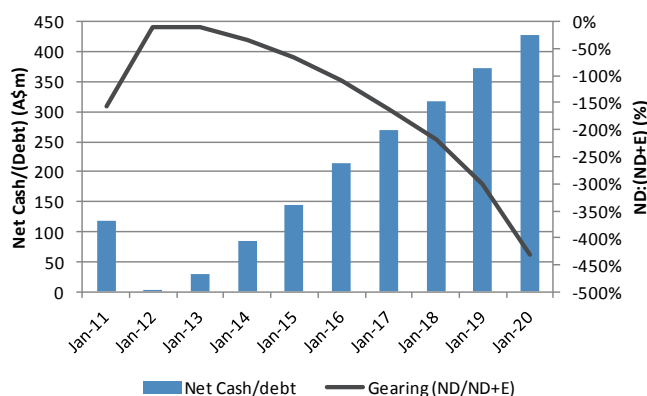
| Profit & Loss (\$m)         | 2011A        | 2012E       | 2013E       | 2014E       | 2015E       |
|-----------------------------|--------------|-------------|-------------|-------------|-------------|
| Revenue                     | 4.3          | 26.1        | 167.4       | 193.6       | 183.7       |
| Costs                       | -31.8        | -18.8       | -89.3       | -96.9       | -99.1       |
| EBITDA                      | -27.5        | 7.3         | 78.0        | 96.7        | 84.6        |
| Depreciation & Amortisation | -0.4         | -10.9       | -17.5       | -18.1       | -18.8       |
| EBIT                        | -27.9        | -3.6        | 60.5        | 78.6        | 65.8        |
| Other                       | 0.0          | 0.0         | 0.0         | 0.0         | 0.0         |
| Interest                    | 4.6          | 0.9         | -1.6        | 0.7         | 3.3         |
| PBT                         | -23.3        | -2.7        | 58.8        | 79.3        | 69.2        |
| Tax                         | 9.1          | 0.8         | -17.7       | -23.8       | -20.8       |
| Minorities & other          | 0.0          | 0.0         | 0.0         | 0.0         | 0.0         |
| NPAT - reported             | -14.2        | -1.9        | 41.2        | 55.5        | 48.4        |
| Exceptional items           | -0.3         | 0           | 0           | 0           | 0           |
| <b>NPAT - adjusted</b>      | <b>-14.5</b> | <b>-1.9</b> | <b>41.2</b> | <b>55.5</b> | <b>48.4</b> |

Source: Hillgrove Resources Limited, Ord Minnett estimates

**Table 6: Balance Sheet**

| Balance Sheet (\$m)           | 2011A        | 2012E        | 2013E        | 2014E        | 2015E        |
|-------------------------------|--------------|--------------|--------------|--------------|--------------|
| Cash and cash equivalents     | 117.9        | 31.6         | 55.3         | 90.6         | 145.4        |
| Trade and other receivables   | 1.9          | 10.3         | 37.3         | 40.5         | 38.7         |
| Inventories                   | 0.1          | 0.1          | 0.1          | 0.1          | 0.1          |
| Other                         | 3.8          | 3.8          | 3.8          | 3.8          | 3.8          |
| Total current assets          | 123.7        | 45.9         | 96.4         | 135.0        | 187.9        |
| Total non-current assets      | 129.8        | 239.1        | 237.0        | 234.4        | 225.4        |
| <b>Total assets</b>           | <b>253.5</b> | <b>284.9</b> | <b>333.5</b> | <b>369.5</b> | <b>413.4</b> |
| Trade and other payables      | 8.7          | 6.6          | 18.0         | 18.5         | 19.0         |
| Other current liabilities     | 0.3          | 0.3          | 0.3          | 0.3          | 0.3          |
| Total current liabilities     | 8.9          | 6.9          | 18.3         | 18.8         | 19.2         |
| Interest bearing liabilities  | 0.0          | 30.0         | 25.0         | 5.0          | 0.0          |
| Other non-current liabilities | 1.1          | 0.3          | 0.3          | 0.3          | 0.3          |
| Total non-current liabilities | 59.7         | 88.9         | 83.9         | 63.9         | 58.9         |
| <b>Total liabilities</b>      | <b>68.6</b>  | <b>95.8</b>  | <b>102.2</b> | <b>82.7</b>  | <b>78.1</b>  |
| <b>Net assets</b>             | <b>184.8</b> | <b>189.2</b> | <b>231.3</b> | <b>286.8</b> | <b>335.2</b> |
| Share capital                 | 178.3        | 184.5        | 185.5        | 185.5        | 185.5        |
| Retained earnings             | 43.2         | 41.3         | 82.5         | 138.0        | 186.4        |
| Minorities                    | 0.3          | 0.3          | 0.3          | 0.3          | 0.3          |
| Other                         | -37.0        | -37.0        | -37.0        | -37.0        | -37.0        |
| Total equity                  | <b>184.8</b> | <b>189.2</b> | <b>231.3</b> | <b>286.8</b> | <b>335.2</b> |
| Net cash/(debt)               | 117.9        | 1.6          | 30.3         | 85.6         | 145.4        |
| Total debt                    | 0.0          | -30.0        | -25.0        | -5.0         | 0.0          |

Source: Hillgrove Resources Limited, Ord Minnett estimates

**Figure 12: Net Cash(Debt) and Gearing Ratio**


Source: Hillgrove Resources Limited, Ord Minnett estimates.

## Valuation

Our sum of parts valuation for HGO is \$0.41 per share. Our Ju1-12 price target of \$0.43 per share is a 12 month roll forward of our valuation.

Our sum of parts valuation is dominated by our DCF (WACC: 10%) valuation for Kanmantoo of \$0.36 per share. We have assigned \$40m (\$0.05/share) exploration value, including \$20m for the Indonesian projects, \$15m for the potential upside at Kanmantoo, and \$5m for the remaining projects. When combining these with corporate costs, net cash and investments, we derive our valuation of \$0.41/share.

**Table 7: Ord Minnett Sum of Parts Valuation and Price Target for Hillgrove Resources Limited**

| Component             | Now         | Jul-12 PT   | Jul-13 | Jul-14 | Jul-15 | Jul-16 |
|-----------------------|-------------|-------------|--------|--------|--------|--------|
| Kanmantoo (cps)       | 35.8        | <b>40.0</b> | 35.2   | 29.8   | 24.0   | 18.5   |
| Investments (cps)     | 0.5         | <b>0.5</b>  | 0.5    | 0.5    | 0.5    | 0.5    |
| Corporate Costs (cps) | -4.6        | <b>-3.4</b> | -2.2   | -0.8   | -0.7   | -0.7   |
| Net Cash (cps)        | 4.6         | <b>1.2</b>  | 7.0    | 14.3   | 22.5   | 31.0   |
| Exploration (cps)     | 5.0         | <b>5.0</b>  | 5.0    | 5.0    | 5.0    | 5.0    |
| <b>Total (cps)</b>    | <b>41.3</b> | <b>43.3</b> | 45.5   | 48.8   | 51.3   | 54.3   |
| Shares on issue (m)   | 793.7       | 793.7       | 793.7  | 793.7  | 793.7  | 793.7  |

Source: Ord Minnett estimates.

Using spot values (AUDUSD: 1.05, copper: US\$4.23/lb, gold: US\$1,645/oz, silver: US\$39/oz), our valuation for Hillgrove is 42cps.

## Key Assumptions and Outputs

Key assumptions in our valuation include:

### Kanmantoo

- Completion of construction of the Kanmantoo plant by November 2011.
- First Kanmantoo production in November 11, production ramping up over 6 months to steady state levels from May 2011.
- Total pre-production capital costs of c.\$150m, which is c.\$16m more than the estimate as at FID (excluding contingencies) to take into account industry wide cost escalation.
- Annual plant throughput and mining rate of 2.4Mt, producing c.70kt of concentrate yielding c.18.7kt of payable copper metal, 8koz of payable gold metal and c.150koz of payable silver metal per year.
- Average life of mine (LOM) unit operating costs of c.\$40/t of ore milled.
- Average C1 cash operating costs of \$1.90/lb (US\$1.62/lb) of copper after gold and silver credits.
- Our modeling uses the May 2010 reserve (14.8Mt) and adds 25% of the resources outside of reserves, to take into account expected reserve conversion over time. Mine life based on reserves yields a 6.25year mine life. Adding the 25% of resources outside of reserves takes total mine life to 8.5 years.
- Total ore mined is 19.7Mt.

Hillgrove has indicated that there is good potential to increase the plant throughput to 2.7Mtpa via debottlenecking of the crushing and grinding circuit. At this point in time we have not incorporated this into our modelling. Beyond the 2.7Mtpa, the company has a target of increasing throughput to 3.5Mtpa, though this is dependant on exploration success. Our model has the plant at 2.4Mtpa for the life of the mine. Were we to increase the throughput to 2.7Mtpa, we would expect to see a slight increase in valuation due to bringing revenues forward, as well as a possible reduction in unit costs.

**Table 8: Ord Minnett Commodity and Exchange Rate Forecasts**

|               |         | CY10A | CY11E | CY12E | CY13E | CY14E | CY15E | LT    |
|---------------|---------|-------|-------|-------|-------|-------|-------|-------|
| Copper (Real) | US\$/lb | 344.8 | 435.0 | 435.7 | 402.4 | 356.9 | 348.2 | 249.5 |
| Gold (Real)   | US\$/oz | 1233  | 1578  | 1642  | 1328  | 1157  | 1084  | 1150  |
| Exchange Rate | AUD:USD | 0.92  | 1.04  | 1.06  | 0.90  | 0.88  | 0.80  | 0.80  |

Source: Ord Minnett estimates.

**Table 9: Assumed Recoveries and Payabilities**

|        | Steady State Recovery | Payability |
|--------|-----------------------|------------|
| Copper | 95%                   | 97%        |
| Gold   | 60%                   | 95%        |
| Silver | 67%                   | 90%        |

Source: Hillgrove Resources Limited, Ord Minnett estimates.

### Financing

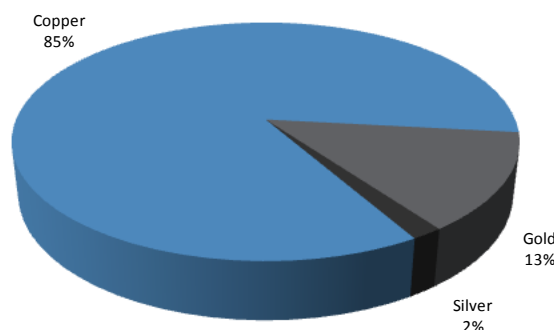
- Cash as of 31 May 2011 was c.\$71m.
- We assume Hillgrove fully draws down the \$30m debt facility.
- We have incorporated hedging of 40kt of payable copper, delivered at 2.5kt per quarter out to April 2016, at \$8,230/t.

**Table 10: Payable Metal Production**

| Metal        | FY12 | FY13  | FY14  | FY15  | FY16  | FY17  | FY18  | FY19  | FY20  |
|--------------|------|-------|-------|-------|-------|-------|-------|-------|-------|
| Copper (kt)  | 2.3  | 16.6  | 18.7  | 18.7  | 18.7  | 18.7  | 18.7  | 18.7  | 18.7  |
| Gold (koz)   | 1.0  | 7.0   | 7.9   | 7.9   | 7.9   | 7.9   | 7.9   | 7.9   | 7.9   |
| Silver (koz) | 18.4 | 132.5 | 149.5 | 149.5 | 149.5 | 149.5 | 149.5 | 149.5 | 149.5 |

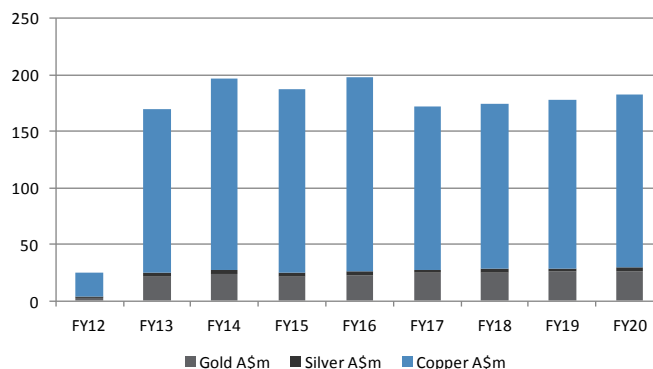
Source: Ord Minnett estimates.

**Figure 13: Kanmantoo Life of Mine Revenue Split**



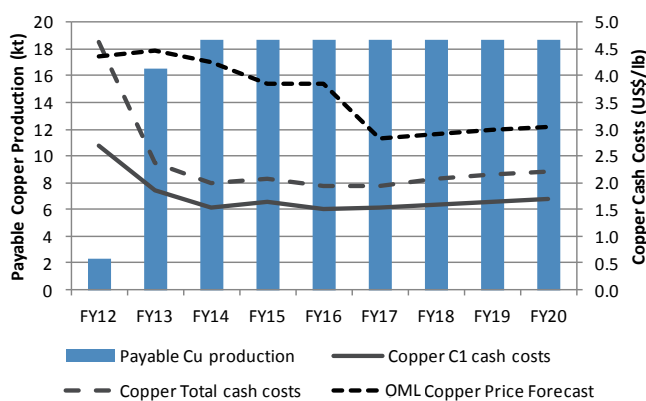
Source: Ord Minnett estimates.

Figure 14: Kanmantoo Annual Revenue Split



Source: Ord Minnett estimates.

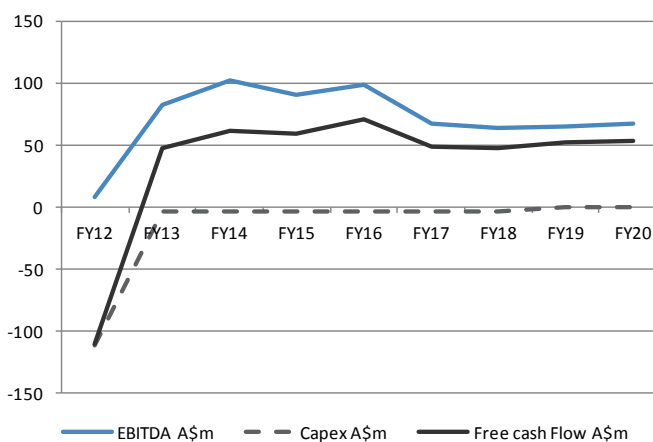
Figure 15: Kanmantoo Copper Production and Costs



Source: Ord Minnett estimates.

As can be seen in Figure 16, peak free cash flow is c.\$70m in FY2016. Note that the difference between EBITDA and net free cash flow is the amount spent on exploration, tax and corporate items.

Figure 16: Project Cash Flows



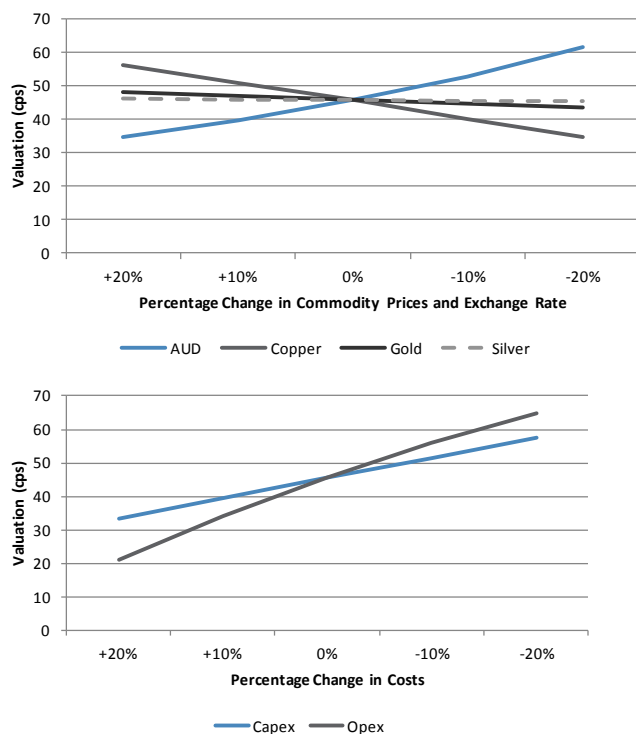
Source: Ord Minnett estimates.

## Sensitivities

### Commodity Prices and Exchange rates

As can be seen from Figure 17, even with the moderate \$ denominated hedge book, our valuation for Hillgrove is most sensitive to changes in the copper price and exchange rates. Changes to the gold and silver price have little effect as expected given their relatively small revenue contribution.

Figure 17: Valuation Sensitivities to Commodity Prices and Exchange Rates (LHS) and Costs (RHS)



Source: Ord Minnett estimates.

### Costs

Our valuation for Hillgrove is moderately sensitive to changes in capital expenditure. However, our valuation is more sensitive to changes in operating costs, given the low grades of Kanmantoo and moderate operating margins.

### Valuation Upside Potential

Given that Kanmantoo remains open in a number of directions, we see potential for HGO to expand on the current resource and reserve, thereby extending mine life or increasing throughput rates, assuming that the additions are economic. The Company is currently undertaking a drill campaign to test this mineralisation.

Given the relatively low grade of the deposit (0.85% Cu), we also expect that any increase in the feed grade to the plant will have a material impact on revenue, cash costs and our valuation. By way of example, if we increase the head grade in our model by 18% to 1.0% Cu with all other aspects constant, our valuation increases by 31% to 63cps.

## Risks

The key risks facing Hillgrove are similar to most other mining project developments and constructions. These include, but are not limited to:

### Ore Body Risk

The behaviour of an ore body compared to expectations is often one of the biggest risks facing a mining company. A mining operation will be designed around an estimate of the ore body, and in particular its size, geometry, grade distribution and continuity, and geotechnical characteristics. If any of these factors is incorrect it may significantly influence the viability of the operation.

To increase the level of confidence in the estimate of the ore body, detailed drilling is required, with typically the more drilling undertaken, the higher the degree of confidence in the shape, geometry and grade of the ore body. Metallurgical test work is also undertaken on drill samples to ascertain the correct treatment methodology for the ore.

Hillgrove has undertaken significant drilling at Kanmantoo to be able to generate a 14.8Mt reserve, of which c.16% is in the proven category, which has the highest level of confidence.

Given that the deposit has been previously mined, the likelihood of the ore body significantly underperforming is relatively low. However, this risk can never truly be discounted until mining and processing has actually commenced.

### Construction/Commissioning Risk

As with the construction of all mines and infrastructure, there are risks associated with this process. These include cost escalation in the capital items as well as the labour completing the construction. Delays in the construction may also impact on costs. Given that Hillgrove is well advanced in the construction phase, and is 'on time and on budget' to meet its November deadline, we see relatively low potential for significant cost or time blow outs during the construction period.

The commissioning of a processing plant, and in particular base metals plant, can often take longer than planned, with the more metals being extracted, the longer the commissioning time due to the interactions between the different processes required. Given that the process at Kanmantoo is relatively straight forward and not a technologically complex one to produce a single concentrate; we see it as unlikely that there are any significant metallurgical and processing issues.

### Commodity Price and Exchange Rate Risk

As demonstrated in our sensitivity analysis, Hillgrove is exposed to movements in the AUDUSD exchange rate as well as the copper price. Even though the company has a moderate degree of hedging, the relatively low grades and therefore only moderate margins results in this leverage.

## Permitting risk

Receiving all required permits is essential for the development of any project. Hillgrove has received all such necessary permits to be allowed to commence operations at Kanmantoo. However, the company must still comply with all necessary environmental requirements to ensure that the mining licence stays in good standing. Key aspects of these requirements are likely to include, but not be restricted to appropriate dust, noise and water management, as well as the containment of any acid mine drainage.

## Financing Risk

Hillgrove has completed all the necessary financing arrangements for the development of Kanmantoo. With cash of c.\$71m as at 31 May 2011 and only moderate debt, we see financing risk as negligible. We estimate that even if preconstruction costs were to increase by 20% above our estimate, HGO would still have c.\$10m surplus cash.

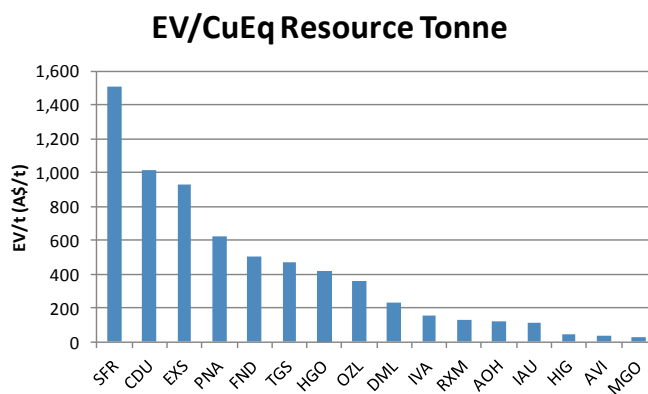
## Peer Comparatives

We have plotted HGO on an enterprise value per copper equivalent resource tonne chart to compare the company to a selection of its peers. We have used copper equivalents to take into account the by/co-product credits typically associated with copper deposits.

Using this metric, HGO has an EV/t of c.\$410/t. This compares to an EV/t for producers of c.\$485/t and c.\$375/t for developers. This implies that, in general, as a company transitions into production, it should be re-rated.

However we also note that the most expensive companies are actually advanced explorers/developers (SFR, EXS, CDU).

Figure 18: Peer Enterprise Value per Resource Tonne



Source: Ord Minnett estimates

## Capital structure

As at 31 July 2011, there were 793.7m ordinary shares on issue. In addition, there were 21.0m unlisted options on issue exercisable at various dates and times, as well as 9.3m performance rights.

Board and management hold less than 1% of the issued capital.

As at 21 April 2011, there were two substantial shareholders:

- JP Morgan Metals & Concentrates: 7.0%
- BT Investment Management: 6.7%

## Board and Management

*Modified from the HGO website.*

**The Hon. Dean Brown, AO** – Chairman. Former Premier and Minister of the South Australian Government and Member of the South Australian Parliament from 1973-1985 and 1992-2006. Mr Brown was also Deputy Premier and Leader of the Opposition. He is Chairman of InterMet Resources Limited, a Director of Scantech Limited, Foodbank SA and the Playford Memorial Trust; the Premier's Special Advisor on the Drought and a member of several advisory boards. Previously he was a Director of AACM International Pty Ltd (1986-92) and a Senior Agricultural Scientist, SA Government.

**Mr Drew Simonsen** – CEO. Mr Simonsen was the Global Head of Energy & Resources, Telecommunications & IT for Westpac Banking Corporation where he worked for over 15 years. Prior to Westpac, he worked for Bank of America in Australia, the USA and Hong Kong for 10 years including roles as Vice President Project Finance, Director of Investment Banking, Director of Corporate Banking and Director of Financial Markets. He has been involved with many energy, resource and infrastructure project and corporate financings in Australia and overseas. Mr Simonsen has also worked for CRA Ltd (now Rio Tinto) in mining engineering roles in Australia.

**Mr Ronald Belz – Non-Executive Director.** Mr Belz has been a Tax Agent since 1978, a member of CPA Australia since 1982 and a Certified Practising Accountant since 1987. He is in public practice in Edgecliff, Sydney. Mr Belz has extensive knowledge and experience in accounting and taxation and corporate law in Australia. He is currently Treasurer and Board Member of the Academy BJE, the New South Wales Board of Jewish Education.

**Mr John Gooding** – Non-Executive Director. Mr Gooding is a Mining Engineer with 30 years' experience in the resources industry. He has held executive management positions with Normandy Mining, MIM, Xstrata (CEO Xstrata Copper Australia), Ok Tedi Mining and Roche Mining. Mr Gooding has extensive experience in gold and base metal mining (both open-cut and underground) through the management and operation of mines in Australia and internationally. He is a former board member of the Queensland Resource Council and has held directorships in a number of companies within the resources industry. Mr Gooding is the Managing Director and Chief Executive Officer at Highlands Pacific Limited.

**Mr John Quirke** – Non-Executive Director. Mr Quirke was previously the Private Secretary to a Federal Senator before being elected the Member for Playford in 1989. In 1997 he became a Federal Senator and then Deputy Chief Whip before resigning in 2000. Mr Quirke gained extensive State and Federal committee experience which included competition policy, public works, social development, economics and finance, and has been an active member of numerous legislative committees specialising in mining and economics since.

**Mr Edwin Zemancheff** – Non-Executive Director. Mr Zemancheff has over 25 years practice experience in all aspects of commercial real estate and land use law having acted for a wide range of major clients on significant

market leading transactions. He has a deep knowledge and understanding of the complex legal, commercial and market issues confronted by leading global and local industry participants in the commercial real estate sector. Mr Zemancheff is a non-executive director of Fortius Funds Management Limited and is currently Chairman of Waratah Rugby.

**Table 11: Board Shareholding as at 31/07/11**

| Holder                          | Shares           | Performance rights |
|---------------------------------|------------------|--------------------|
| Hon DC Brown, AO                | 232,571          | -                  |
| Mr DA Simonsen                  | 750,000          | 3,875,000          |
| Mr RD Belz                      | -                | -                  |
| Mr E Zemancheff                 | 185,000          | -                  |
| Mr JA Quirke                    | 182,955          | -                  |
| Mr JE Gooding                   | 30,000           | -                  |
| <b>Total</b>                    | <b>1,380,526</b> |                    |
| Percentage of Total Issue       | 0.17%            |                    |
| Total shares on issue (31/7/11) | 793,698,575      |                    |

Source: Company Reports

## Private Client Research

### HGO Summary - January 31 year end (A\$m)

| Company Data  |             |
|---|-------------|
| Share Price (A\$)                                       | 0.230       |
| 52 Week range (A\$)                                     | 0.2 - 0.365 |
| Shares on issue (m) (undiluted)                         | 793.7       |
| Shares on Issue (m) (diluted incl ITM options)          | 793.7       |
| Market Capitalisation (A\$m) (undiluted)                | 182.6       |
| Market Capitalisation (A\$m) (diluted incl ITM options) | 182.6       |

| Substantial Shareholders    |      |
|-----------------------------|------|
| OML - Metals & Concentrates | 7.0% |
| BT Investment Management    | 6.7% |

| Profit & Loss (A\$m)        | 2011A | 2012E | 2013E | 2014E | 2015E |
|-----------------------------|-------|-------|-------|-------|-------|
| Revenue                     | 4.3   | 26.1  | 167.4 | 193.6 | 183.7 |
| Costs                       | -31.8 | -18.8 | -89.3 | -96.9 | -99.1 |
| EBITDA                      | -27.5 | 7.3   | 78.0  | 96.7  | 84.6  |
| Depreciation & Amortisation | -0.4  | -10.9 | -17.5 | -18.1 | -18.8 |
| EBIT                        | -27.9 | -3.6  | 60.5  | 78.6  | 65.8  |
| Other                       | 0.0   | 0.0   | 0.0   | 0.0   | 0.0   |
| Interest                    | 4.6   | 0.9   | -1.6  | 0.7   | 3.3   |
| PBT                         | -23.3 | -2.7  | 58.8  | 79.3  | 69.2  |
| Tax                         | 9.1   | 0.8   | -17.7 | -23.8 | -20.8 |
| Minorities & other          | 0.0   | 0.0   | 0.0   | 0.0   | 0.0   |
| NPAT - reported             | -14.2 | -1.9  | 41.2  | 55.5  | 48.4  |
| Exceptional items           | -0.3  | 0.0   | 0.0   | 0.0   | 0.0   |
| NPAT - adjusted             | -14.5 | -1.9  | 41.2  | 55.5  | 48.4  |

|                               |       |      |      |      |      |
|-------------------------------|-------|------|------|------|------|
| Shares outstanding (millions) | 794   | 794  | 794  | 794  | 794  |
| EPS - reported                | -0.02 | 0.00 | 0.05 | 0.07 | 0.06 |
| EPS - adjusted                | -0.02 | 0.00 | 0.05 | 0.07 | 0.06 |
| DPS                           | 0.0   | 0.0  | 0.0  | 0.0  | 0.0  |

| Segmented revenue (A\$m) | 2011A | 2012E | 2013E | 2014E | 2015E |
|--------------------------|-------|-------|-------|-------|-------|
| Copper                   | 0.0   | 21.8  | 146.7 | 172.7 | 166.4 |
| Gold                     | 0.0   | 3.3   | 22.2  | 24.7  | 22.5  |
| Silver                   | 0.0   | 0.7   | 4.4   | 4.5   | 3.9   |

| Attributable Production     | 2011A | 2012E | 2013E | 2014E | 2015E |
|-----------------------------|-------|-------|-------|-------|-------|
| <i>Payable metal</i>        |       |       |       |       |       |
| Copper (kt metal in conc.)  | 0.0   | 2.3   | 16.6  | 18.7  | 18.7  |
| Gold (koz)                  | 0.0   | 1.0   | 7.0   | 7.9   | 7.9   |
| Silver (koz metal in conc.) | 0.0   | 18.4  | 132.5 | 149.5 | 149.5 |

| Cash Costs             | 2011A | 2012E | 2013E | 2014E | 2015E |
|------------------------|-------|-------|-------|-------|-------|
| <i>C1</i>              |       |       |       |       |       |
| A\$/lb (post credits)  | 0.0   | 2.57  | 1.75  | 1.72  | 1.86  |
| US\$/lb (post credits) | 0.0   | 2.68  | 1.86  | 1.55  | 1.64  |

### Resources & Reserves

#### Kanmantoo

#### Resources (8/12/2008)

##### Measured + Indicated

|  | Tonnes | Copper | Gold    | Silver |
|--|--------|--------|---------|--------|
|  | 24.8Mt | 0.90%  | 0.20g/t | 3.3g/t |

|             |         |          |        |
|-------------|---------|----------|--------|
| Cont. Metal | 226.1kt | 152.0koz | 2.6Moz |
|-------------|---------|----------|--------|

##### Inferred

|  |       |      |         |        |
|--|-------|------|---------|--------|
|  | 7.4Mt | 0.9% | 0.20g/t | 2.9g/t |
|--|-------|------|---------|--------|

|             |        |         |        |
|-------------|--------|---------|--------|
| Cont. Metal | 66.1kt | 39.1koz | 0.7Moz |
|-------------|--------|---------|--------|

|                          |                |                 |               |
|--------------------------|----------------|-----------------|---------------|
| <b>Total Cont. Metal</b> | <b>292.2kt</b> | <b>191.1koz</b> | <b>3.3Moz</b> |
|--------------------------|----------------|-----------------|---------------|

#### Reserves (4/5/2010)

##### Proven & Probable

|  | Tonnes | Copper | Gold    | Silver |
|--|--------|--------|---------|--------|
|  | 14.8Mt | 0.85%  | 0.17g/t | 3.1g/t |

|             |         |         |        |
|-------------|---------|---------|--------|
| Cont. Metal | 125.8kt | 80.9koz | 1.5Moz |
|-------------|---------|---------|--------|

| Key Ratios                   | 2011A | 2012E | 2013E | 2014E  | 2015E |
|------------------------------|-------|-------|-------|--------|-------|
| PE Ratio                     | -12.9 | -98.0 | 4.4   | 3.3    | 3.8   |
| EV / EBITDA                  | -6.6  | 20.9  | 2.0   | 1.8    | 2.2   |
| EBITDA / sales margin        | -644% | 28%   | 47%   | 50%    | 46%   |
| ROA (EBIT/Assets)            | -11%  | -1%   | 18%   | 21%    | 16%   |
| ROE (NPAT/Equity)            | -8%   | -1%   | 18%   | 19%    | 14%   |
| Net debt / net debt + equity | -39%  | -1%   | -12%  | -23%   | -30%  |
| Net interest cover           | 6.0   | 3.9   | 37.0  | -120.2 | -19.7 |

| Cashflow (A\$m)               | 2011A | 2012E | 2013E | 2014E | 2015E |
|-------------------------------|-------|-------|-------|-------|-------|
| <b>Cashflow - Operating</b>   |       |       |       |       |       |
| Receipts from customers       | 3.4   | 17.6  | 140.4 | 190.4 | 185.5 |
| Payments to suppliers & empl. | 29.6  | 20.9  | 77.9  | 96.4  | 98.6  |
| Interest received             | 4.7   | 0.9   | -1.6  | 0.7   | 3.3   |
| Tax paid                      | 19.2  | 0.0   | -17.7 | -23.8 | -20.8 |
| Total CFO                     | -40.7 | -2.3  | 43.2  | 70.8  | 69.5  |

|                             |       |        |       |       |      |
|-----------------------------|-------|--------|-------|-------|------|
| <b>Cashflow - Investing</b> |       |        |       |       |      |
| Purchase of PP&E            | -35.5 | -111.5 | -4.0  | -4.0  | -4.0 |
| Proceeds Sales              | 10.6  | 0.0    | 0.0   | 0.0   | 0.0  |
| Projects & Investments      | -3.2  | 0.0    | 0.0   | 0.0   | 0.0  |
| Exploration & evaluation    | -15.1 | -8.6   | -11.5 | -11.5 | -8.8 |
| Total CFI                   | -43.1 | -120.1 | -15.5 | -15.5 | -9.8 |

|                               |      |      |      |       |      |
|-------------------------------|------|------|------|-------|------|
| <b>Cashflow - Financing</b>   |      |      |      |       |      |
| Proceeds from issue of shares | 79.1 | 6.2  | 0.9  | 0.0   | 0.0  |
| Payment of share issue costs  | -5.3 | 0.0  | 0.0  | 0.0   | 0.0  |
| Proceeds from issue of debt   | 0.0  | 30.0 | 0.0  | 0.0   | 0.0  |
| Repayments of debt            | 2.5  | 0.0  | 5.0  | 20.0  | 5.0  |
| Dividends Paid                | 0.0  | 0.0  | 0.0  | 0.0   | 0.0  |
| Total CFF                     | 71.3 | 36.2 | -4.1 | -20.0 | -5.0 |

|                            |       |       |      |      |       |
|----------------------------|-------|-------|------|------|-------|
| <b>Change in cash</b>      |       |       |      |      |       |
| Opening cash & equivalents | 130.4 | 117.9 | 31.6 | 55.3 | 90.6  |
| FX                         | 0.0   | 0.0   | 0.0  | 0.0  | 0.0   |
| Closing cash               | 117.9 | 31.6  | 55.3 | 90.6 | 145.4 |

| Balance Sheet (A\$m)          | 2011A        | 2012E        | 2013E        | 2014E        | 2015E        |
|-------------------------------|--------------|--------------|--------------|--------------|--------------|
| Cash and cash equivalents     | 117.9        | 31.6         | 55.3         | 90.6         | 145.4        |
| Trade and other receivables   | 1.9          | 10.3         | 37.3         | 40.5         | 38.7         |
| Inventories                   | 0.1          | 0.1          | 0.1          | 0.1          | 0.1          |
| Other                         | 3.8          | 3.8          | 3.8          | 3.8          | 3.8          |
| Total current assets          | 123.7        | 45.9         | 96.4         | 135.0        | 187.9        |
| Total non-current assets      | 129.8        | 239.1        | 237.0        | 234.4        | 225.4        |
| <b>Total assets</b>           | <b>253.5</b> | <b>284.9</b> | <b>333.5</b> | <b>369.5</b> | <b>413.4</b> |
| Trade and other payables      | 8.7          | 6.6          | 18.0         | 18.5         | 19.0         |
| Other current liabilities     | 0.3          | 0.3          | 0.3          | 0.3          | 0.3          |
| Total current liabilities     | 8.9          | 6.9          | 18.3         | 18.8         | 19.2         |
| Interest bearing liabilities  | 0.0          | 30.0         | 25.0         | 5.0          | 0.0          |
| Other non-current liabilities | 1.1          | 0.3          | 0.3          | 0.3          | 0.3          |
| Total non-current liabilities | 59.7         | 88.9         | 83.9         | 63.9         | 58.9         |
| <b>Total liabilities</b>      | <b>68.6</b>  | <b>95.8</b>  | <b>102.2</b> | <b>82.7</b>  | <b>78.1</b>  |
| <b>Net assets</b>             | <b>184.8</b> | <b>189.2</b> | <b>231.3</b> | <b>286.8</b> | <b>335.2</b> |
| Share capital                 | 178.3        | 184.5        | 185.5        | 185.5        | 185.5        |
| Retained earnings             | 43.2         | 41.3         | 82.5         | 138.0        | 186.4        |
| Minorities                    | 0.3          | 0.3          | 0.3          | 0.3          | 0.3          |
| Other                         | -37.0        | -37.0        | -37.0        | -37.0        | -37.0        |
| Total equity                  | 184.8        | 189.2        | 231.3        | 286.8        | 335.2        |
| Net cash/(debt)               | 117.9        | 1.6          | 30.3         | 85.6         | 145.4        |
| Total debt                    | 0.0          | -30.0        | -25.0        | -5.0         | 0.0          |

| Valuation             | Jul-11       |           | Jul-12       |           |
|-----------------------|--------------|-----------|--------------|-----------|
|                       | A\$m         | cps       | A\$m         | cps       |
| Kanmantoo             | 284.0        | 36        | 317.6        | 40        |
| Investments           | 3.8          | 0         | 3.8          | 0         |
| Corporate costs       | -36.3        | -5        | -27.2        | -3        |
| Net cash/(debt)       | 36.5         | 5         | 9.2          | 1         |
| Exploration potential | 40.0         | 5         | 40.0         | 5         |
| <b>Total</b>          | <b>328.0</b> | <b>41</b> | <b>343.3</b> | <b>43</b> |

|                     |       |       |
|---------------------|-------|-------|
| Shares on issue (m) | 793.7 | 793.7 |
|---------------------|-------|-------|

| Price Assumptions | 2011A | 2012E | 2013E | 2014E | 2015E |
|-------------------|-------|-------|-------|-------|-------|
| A\$/US\$ FX rate  | 0.88  | 0.99  | 1.06  | 0.98  | 0.89  |
| Copper (US\$/t)   | 7,601 | 9,636 | 9,875 | 9,875 | 8,500 |
| Gold (US\$/oz)    | 1,233 | 1,587 | 1,688 | 1,400 | 1,250 |
| Silver (US\$/oz)  | 20.40 | 38.52 | 35.73 | 26.90 | 22.70 |

| Sensitivity Analysis | +10% | 0   | -10% | +10% | -10% |
|----------------------|------|-----|------|------|------|
| % change in NPV:     | cps  | cps | cps  | %    | %    |
| AUD                  | 40   | 43  | 53   | -8%  | 22%  |
| Copper               | 51   | 43  | 40   | 18%  | -7%  |
| Gold                 | 47   | 43  | 44   | 8%   | 3%   |
| Silver               | 46   | 43  | 45   | 6%   | 5%   |

## Private Client Research

Please contact your Ord Minnett Adviser for further information on our document.

### Guide to Ord Minnett Recommendations

Our recommendations are based on the total return of a stock – nominal dividend yield plus capital appreciation – and have a 12-month time horizon.

|                        |   |
|------------------------|---|
| <b>BUY</b>             | The stock is undervalued and we expect it to exceed the total return by 15% over the next 12 months..   |
| <b>ACCUMULATE</b>      | We expect a total return of between 5% and 15%. Investors should consider adding to holdings or taking a position in the stock on share price weakness.   |
| <b>HOLD</b>            | We expect the stock to return between 0% and 5%, and believe the stock is fairly priced.  |
| <b>LIGHTEN</b>         | We expect the stock to return less than 0% and possibly as much as 15%. Investors should consider decreasing their holdings.  |
| <b>SELL</b>            | We expect the total return to lose 15% or more.   |
| <b>RISK ASSESSMENT</b> | Classified as High, Medium or Low, denotes the relative assessment of an individual stock's risk based on an appraisal of its disclosed financial information, volatility, nature of its operations and other relevant quantitative and qualitative criteria. |

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