



1 December 2011

\$0.19

BUY

James Brennan-Chong

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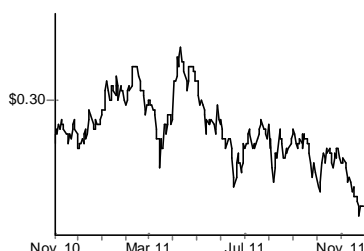
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Price Performance



Security/Capital Details

ASX Code	HGO
Market Cap	\$153 M
Issued Shares (dil)	806.0 M
Avg Mth T'over	39.81 M
12 Mth High – Low	\$0.36 - \$0.18

Key Data/Ratios – FY 2012

EBITDA / Sales	-318.2%
EBIT / Sales	-341.2%
Debt / Equity	26.1%
Interest Cover	-4.5 x
ROE	-2.1%
EPS Growth	70.5%
DCF	\$0.46
12 Mth Price Target	\$0.55

Important Disclosure

Wilson HTM Corporate Finance Ltd acted as Joint Lead Manager and Underwriter for the placement announced by Hillgrove Resources Limited in October 2010 and earned fees for acting in this capacity.

Recommendation

HGO has produced first concentrate and appears on track to record first revenue in mid to late December. Whilst this is a positive, we maintain that the cash outlook remains tight. In our view, ramp up risk and the nature and size of the unexpected claim are likely to continue to limit share price appreciation. The need for a capital raising is not a foregone conclusion as debt financing and deferred payment of the unexpected claim remain possible solutions to the weak near-term cash outlook. We are seeing growing exploration potential at Kanmantoo and look to an updated reserve and resource statement as well as a re-optimised mine plan in CY12 as providing share price catalysts.

Key Points

- **First concentrate:** Kanmantoo has produced first concentrate with initial concentrate grades above company expectations.
- The announcement of first revenue will be the next share price catalyst, and is dependent on 2,500t of concentrate arriving at the port. We understand the mill to be currently operating at +80% of nameplate capacity (~80ktpa concentrate), this implies a current monthly concentrate production rate of 5,333t.
- Although minor 'teething' issues are not uncommon during the ramp up phase for Greenfield mining projects, we remain comforted by the plant's previous operating status as well as the relatively non-complex metallurgy.
- **Contractor claim:** Although details are limited, we understand discussions regarding the unexpected claim to be ongoing, the claim is estimated at ~\$10m. The timing of the payment remains unknown and it is possible that the payment could be deferred into CY2012.
- **Initial resource reconciliation positive:** Initial grade control sampling across an estimated 500kt sample has returned results that have generally met or exceeded the existing resource model.
- **Exploration potential advancing:** Drilling during the quarter focused primarily around the Emily Star satellite pit. Results suggest potential for a single larger and longer life pit compared to a cluster of small pits. A reserve and resource update is expected in the first half of CY2012.
- **Cash outlook remains tight:** Total cash at 31 October was \$34.5m, this includes \$10m that has been ring fenced to Hillgrove's subsidiary at behest of the banks. Cash available to HGO at the end of October was \$24m. Debt at 31 October was A\$30m.
- We continue to estimate a cash burn rate of \$10m per month, and we forecast a cash low point at the end of December of \$4m, which is prior to any expected revenue from the arrival of first concentrate to port. HGO expects to be cash flow positive by February.
- **Valuation:** We rate HGO a BUY, although note the potential for ramp up delays that could add further pressure on an already tight near term cash outlook. Our modelling assumes an additional \$20m of debt financing, although we cannot rule out the possibility of an equity raising. Valuation and target price are unchanged at \$0.46/sh and \$0.55/sh respectively.

Year to Jan	NPAT (Rep) \$M	NPAT (PSig) \$M	EPS (PSig) c	EPS Growth %	PER x	CFPS c	P/CF x	DPS c	Div Yld %	Franking %
2011a	-13.4	-13.4	-1.7	16.2	-11.5	-5.0	-3.8	0.0	0.0	0
2012e	-4.0	-4.0	-0.5	70.5	-38.8	-0.7	-26.4	0.0	0.0	0
2013e	29.3	29.3	3.6	842.9	5.2	6.1	3.1	0.0	0.0	
2014e	52.6	52.6	6.5	79.1	2.9	11.2	1.7	0.0	0.0	

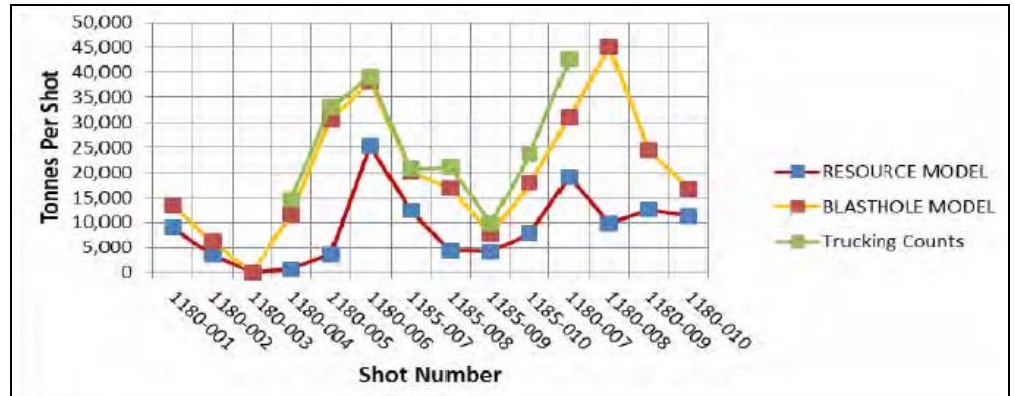


Resource reconciliation

Results from an initial resource reconciliation sample have generally met or exceed the existing resource model. The charts below comprise data taken from one upper bench located at 1180RL and cover an area that is expected to represent 500kt of resource.

Generally, the Kanmantoo ore body demonstrates higher-grade ore towards the bottom of the pit coinciding with primary ore.

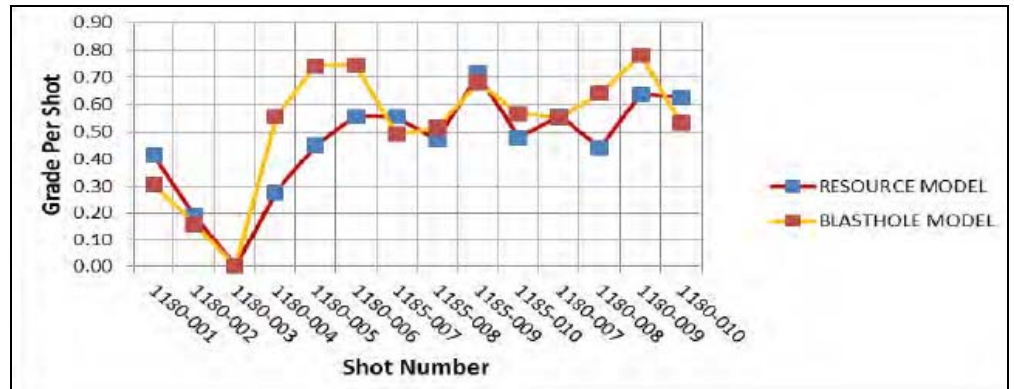
Reconciled primary ore tonnes per production shot



Source: HGO

Initial Blasthole model results have recorded an average ~20% increase in ore tonnages compared to the existing resource model over the sample area.

Reconciled primary ore copper grade tonnes per production shot



Source: HGO

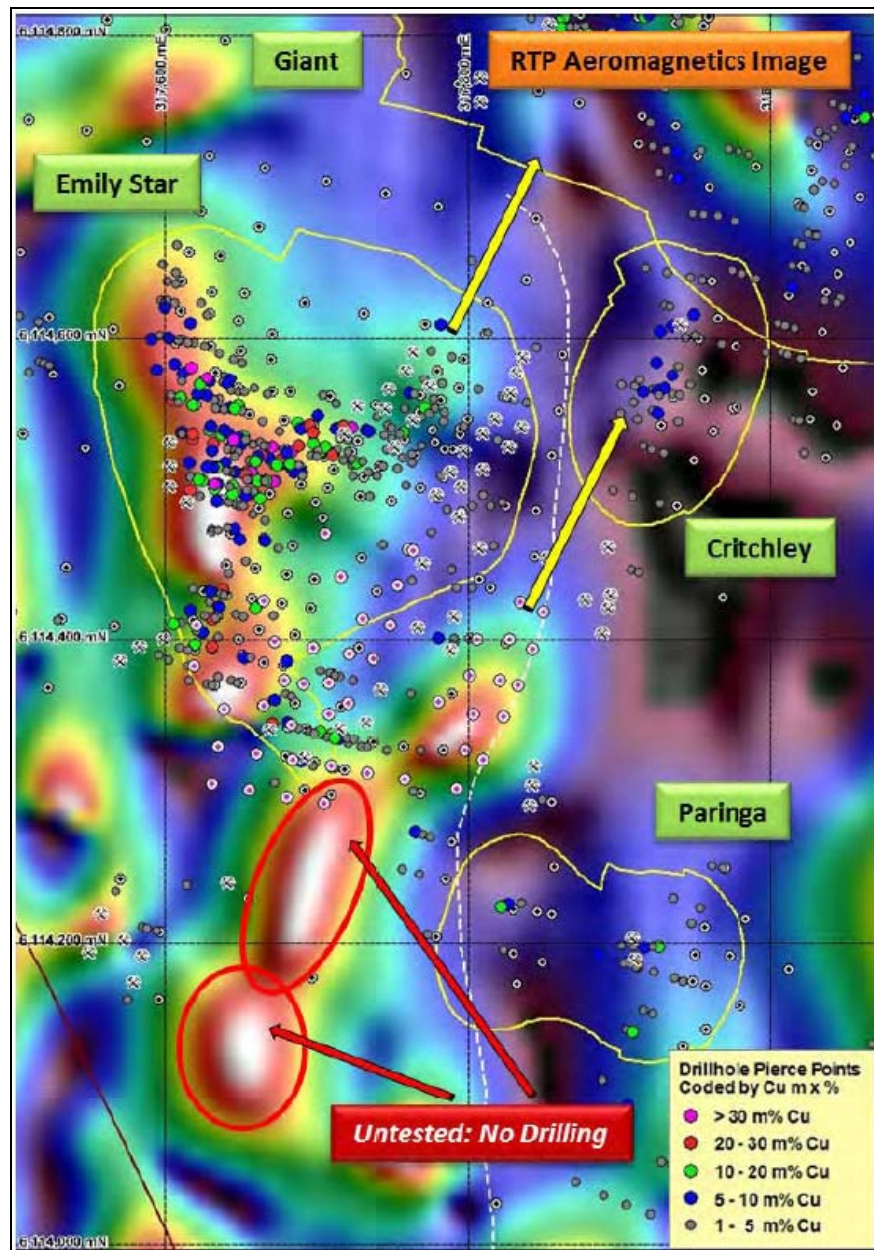
Initial Blasthole model results have recorded primary ore copper grades that have generally met or exceed the expected grade as per the resource model.

The average grade from the above sample is not readily comparable to the reserve grade of 0.85% Cu, as grades at the upper portion of the deposit generally exhibit lower copper grades.



Growing resource potential at Kanmantoo

Emily Star aerial magnetics and drillhole pierce points



Source: HGO

Resource to reserve conversion drilling focused primarily on the Emily Star satellite pit, 20 holes over 3,197m were completed. Key results include;

- 22m @ 1.21% Cu from 128m
- 14m @ 1.56% Cu from 91m
- 17m @ 1.10% cu from 118m

These results are significant as the grades from the drill results are above the existing Emily Star reserve grade, estimated at 1.5mt @ 0.95% Cu for 14.3kt Cu.

HGO is seeing potential for a link zone between Emily Star, Critchley, Giant and Paringa that could potentially result in a single large open pit, compared to a series of smaller satellite pits (existing pit outlines in yellow). Should grades at all locations continue to demonstrate widths and grades analogous to that of Emily Star, we see scope for a combined larger pit that is up to three times the size of the existing Emily Star pit. Such an outcome could potentially add +3 years mine life.

Hillgrove Resources Ltd (HGO : \$0.19)

PRODUCTION

Yr Ending Jan	2010A	2011A	2012E	2013E	2014E
Copper In Conc - (kt)	0	0	1.3	16.1	22.0
Gold In Conc - (koz)	0	0	0	10	11
Silver In Conc (koz)	0	0	10	198	226
C1 Cash Cost - (US\$/lb)	0.00	0.00	4.70	1.78	1.29

PRICES

Yr Ending Jan	2010A	2011A	2012E	2013E	2014E
Gold (US\$/oz spot)	994	1250	1617	1900	1783
Silver (US\$/oz spot)	15.02	21.65	36.76	41.08	38.75
Copper (US\$/lb)	2.46	3.51	4.02	4.10	3.95
AUDUSD (USD)	0.82	0.93	1.02	0.97	0.94

INVESTMENT & VALUATION FUNDAMENTALS

Yr Ending Jan	2010A	2011A	2012E	2013E	2014E
EPS Before Abs (c)	-2.0	-1.7	-0.5	3.6	6.5
EPS Growth (%)	N/A	16.2%	70.5%	842.9%	79.1%
PER (x)	-9.6	-11.5	-38.8	5.2	2.9
CFPS (c)	-1.1	-5.0	-0.7	6.1	11.2
P/CF (x)	-17.9	-3.8	-26.4	3.1	1.7
EV/EBITDA (x)	-2.6	-1.7	-28.8	2.2	0.6
DPS (c)	0.0	0.0	0.0	0.0	0.0
Yield (%)	0.0%	0.0%	0.0%	0.0%	0.0%
Franking (%)	0%	0%	0%		

DCF VALUATION

@

11.1%

10%

Yr Ending Jan	A\$m	A\$ps	A\$m	A\$ps
Kanmantoo - Open Cut	393.1	0.49	410.6	0.51
Corporate Items	-29.9	-0.04	-31.2	-0.04
Interests In Other Entities	3.7	0.00	3.67	0.00
Exploration/Development	19.3	0.02	19.2	0.02
Cash collateralised bond	7.5	0.01	7.5	0.01
Franking Credits	31.4	0.04	32.9	0.04
Hedge Book	-18.4	-0.02	-18.8	-0.02
Net (Debt)/Cash	-35.0	-0.04	-35.0	-0.04
Additional Capital - Dilution	0.8	0.00	0.8	0.00
Total Valuation	372.4	0.46	389.6	0.48

PROFITABILITY RATIOS

Yr Ending Jan	2010A	2011A	2012E	2013E	2014E
EBIT / Sales (%)	-710.5%	-670.8%	-341.2%	28.2%	36.0%
ROA (%)	N/A	-19.6%	-3.3%	15.6%	27.0%
ROE (%)	N/A	-7.7%	-2.1%	14.2%	21.2%
ROFE (%)	N/A	-41.2%	-4.8%	20.7%	38.2%

INTERIMS (\$m)

Half Yr	Jul 10	Jan 11	Jul 11	Jan 12	Jul 12
Yr Ending Jan	1H A	2H A	1H A	2H E	1H E
Sales Revenue	1.4	1.7	1.6	0.5	64.1
EBIT	-7.4	-13.9	-2.8	-4.3	15.0
Net Profit	-2.7	-10.7	0.5	-4.5	9.1
EPS	-0.3	-1.3	0.1	-0.6	1.1

BALANCE SHEET (\$m)

Yr Ending Jan	2010A	2011A	2012E	2013E	2014E
Cash	130.4	118.2	15.0	54.9	132.6
Total Assets	211.1	254.4	306.2	346.4	397.7
Debt	2.5	0.0	50.0	47.5	37.5
Total Liabilities	47.3	68.8	114.7	124.7	123.4
Total Shareholders Equity	163.5	185.3	191.4	221.5	274.2
Total Funds Employed	35.9	67.4	226.6	214.2	179.2

LIQUIDITY & LEVERAGE RATIOS

Yr Ending Jan	2010A	2011A	2012E	2013E	2014E
Debt / Equity (%)	1.5%	0.0%	26.1%	21.4%	13.7%
Gearing (%) ¹	1.5%	0.0%	20.7%	17.6%	12.0%
Interest Cover (x)	-0.8	-17.9	3.4	12.0	139.2
Debt / CashFlow (x)	-0.3	0.0	-8.6	1.0	0.4
(Debt+CNNotes) / CashFlow	-0.1	0.0	-11.2	0.8	0.4

PROFIT & LOSS (\$m)

Yr Ending Jan	2010A	2011A	2012E	2013E	2014E
Sales Revenue	1.4	3.2	2.1	162.2	208.7
EBITDA	-9.8	-20.9	-6.5	66.8	104.0
Depn and Amortisation	0.4	0.4	0.5	21.1	28.8
EBIT	-10.2	-21.3	-7.0	45.7	75.2
Net Interest Expense	12.2	1.2	-2.1	3.8	0.5
Pre-tax Profit	-22.4	-22.5	-5.0	41.9	74.6
Tax	-6.4	-9.1	-1.0	12.6	22.0
Tax rate (%)	28.5%	40.6%	19.8%	30.0%	29.5%
Minorities / pref divs	0.0	0.0	0.0	0.0	0.0
Equity accounted NPAT	0.0	0.0	0.0	0.0	0.0
Net Profit	-16.0	-13.4	-4.0	29.3	52.6
Abnormals	71.6	0.0	0.0	0.0	0.0
Reported Net Profit	55.6	-13.4	-4.0	29.3	52.6

CASHFLOW (\$m)

Yr Ending Jan	2010A	2011A	2012E	2013E	2014E
Operating Cash Flow	-8.5	-40.4	-5.8	49.5	90.1
Capital Expenditure	-7.2	-44.2	-141.6	-2.4	-2.5
Expln, Develop, Evaln	-4.4	-8.4	-5.4	-5.4	0.0
Asset Sales/Acquisitions	165.6	12.0	0.2	0.0	0.0
Other	0.0	-0.6	0.0	0.0	0.0
Investing Cash Flow	154.0	-41.1	-146.9	-7.8	-2.5
Share Issues/(Buybacks)	32.8	83.9	0.0	0.8	0.0
Debt Drawdown (Repay)	-47.3	-2.5	50.0	-2.5	-10.0
Dividends Paid	-8.3	0.0	0.0	0.0	0.0
Other Fin. Flows	0.0	-12.7	-0.2	0.0	0.0
Financing Cash Flow	-22.8	68.7	49.8	-1.7	-10.0
Cash Increase (Decrease)	122.7	-12.8	-102.9	40.0	77.6

EARNINGS SENSITIVITIES - % CHANGE

Yr Ending Jan	2010A	2011A	2012E	2013E	2014E
+/-10% US\$ Copper Price	0.0%	0.0%	0.0%	33.9%	25.8%
+/-10% US\$ Gold Price	0.0%	0.0%	0.0%	4.0%	2.3%
+/- 1c Movement US\$/A\$	0.0%	0.0%	0.0%	3.7%	2.8%
+/-10% US\$ Silver Price	0.0%	0.0%	0.0%	1.6%	1.7%

1. Gearing = (Debt + CNotes) / (Debt + CNotes + Equity)



Recommendation Structure

BUY: Total return +10% or more over a 12 month period

HOLD: Total return expected to be between +10% to -10% over a 12-month period

SELL: Total return expected to be -10% or more over a 12 month period

TOTAL RETURN OR TSR = capital growth in share price + expected dividend yield in that period

Other definitions

CS Coverage Suspended. Wilson HTM Ltd has suspended coverage of this company.

NR Not Rated. The recommendation has been suspended temporarily. Such suspension is in line with Wilson HTM Investment Group Ltd policies in circumstances where Wilson HTM Corporate Finance Ltd is acting in an advisory capacity in a merger or strategic transaction involving the company and in certain other situations.

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Disclosure of Interest. Hillgrove Resources Ltd

The Directors of Wilson HTM Ltd advise that at the date of this report they and their associates have relevant interests in Hillgrove Resources Limited. They also advise that Wilson HTM Ltd and Wilson HTM Corporate Finance Ltd A.B.N. 65 057 547 323 and their associates have received and may receive commissions or fees from Hillgrove Resources Limited in relation to advice or dealings in securities. Some or all of Wilson HTM Ltd authorised representatives may be remunerated wholly or partly by way of commission.

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Regulatory Disclosures

Wilson HTM Corporate Finance Ltd acted as Joint Lead Manager and Underwriter for the placement announced by Hillgrove Resources Limited in October 2010 and earned fees for acting in this capacity.

Wilson HTM Investment Group Ltd and its related bodies corporate trades or may trade as principal in the securities that are subject of the research report.

Wilson HTM Corporate Finance Ltd has received compensation for corporate advisory services from this company, its subsidiaries or affiliates during the previous 12 months.

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