

Blackthorn Resources

Base Metals – Speculative Risk

Recommendation	Buy
Last Price	A\$0.50
Target Price	A\$1.10
Forecast Total Return	120%

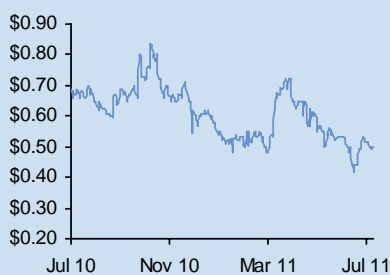
Company profile

Blackthorn Resources (ASX: BTR) is a Sydney-based, diversified mining company with a focus on African projects. BTR has a 39.9% interest with Glencore international (50.1%) in the Perkoa zinc project, under construction, with first production in mid-2012.

The JV is currently investigating potential to add a lead/silver circuit to Perkoa and increase throughput to 1mtpa. With ore grading over 1oz/t Ag, this could provide significant valuation upside.

The company now owns 100% of the Mumbwa Copper project, Zambia with an existing resource containing 1.6mt Cu. Drilling is under way to expand the resource, to coincide with pre-feasibility studies.

Share price performance



	1m	3m	12m
Price	(1%)	(22.5%)	(28.6%)

Source: Iress

Other Information

Iress / Bloomberg	BTR / BTR AU
Market cap (diluted)	A\$61m
Enterprise value (estimate)	A\$55m
Average daily volume (m)	0.10
Free float	72.7%
Number of shares on issue (m)	122.9
Reporting currency	AUD
Quote currency	AUD
Website	blackthornresources.com.au
Analyst(s)	Geoff Muers
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	Source: Iress, Capital IQ

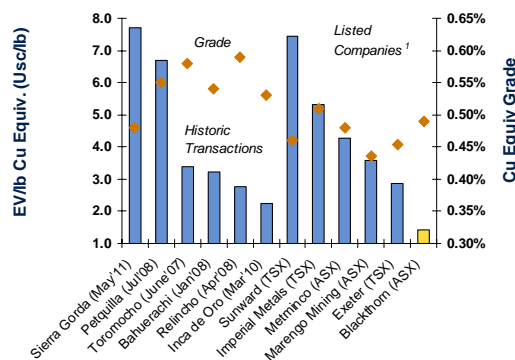
BHP exit paves way for value-add

BHP Billiton recently announced its intention to withdraw from the Mumbwa copper project where a sizeable resource of over 1.6mt Cu has been established to date. BTR will commence drilling in the coming weeks on the 100% owned property, with no shortage of interest from other global copper players. The Perkoa Zinc mine is moving closer to production, with results due shortly on reserve extension drilling with silver grades providing potential upside to cashflow. This stock is rated speculative risk; thus it is suitable only for investors with significant risk tolerance.

- **Recent newsflow:** BHP recently declared it will not continue funding drilling at Mumbwa, and move to the next phase of the project which required a cash payment to BTR and other commitments. BTR's partner in Perkoa, Glencore, is due to report on the progress of potential plant expansion to 1mtpa, and the addition of a silver/lead circuit in coming weeks. BTR recently hired Tony De Santis as COO (ex-Anglo American, BHP) and has acquired new exploration licences in Zambia.
- **Key issues:** The copper project has the potential for further discovery, and to expand the known resource base (87mt @ 0.94% Cu). Whilst valuation of the resource is difficult due to the uncertain economics of a mining project (no scoping or PFS yet conducted) it is clear the market is not factoring in any value-add here, which clearly there is potential for. With production from mid-2012E, the Perkoa project has potential to generate US\$100mpa EBITDA (BTR, 40%); hence at the current share price, investors get exposure to the copper project for free.
- **Value:** We value BTR's 40% of Perkoa at US\$73m, allowing for the expanded case (1mtpa, silver/lead circuit) including a 30% NPV risk discount. Due to reduced equity market valuations, and uncertainty on Mumbwa post the BHP exit, we have reduced our valuation multiple on the resource to US\$0.02/lb (was US\$0.03/lb) which is less than 50% of peers. In summary, our valuation has risen from US\$1.04/share to US\$1.14/share (US\$1.45/share spot) primarily due to a move to 100% ownership of Mumbwa. Our price target of A\$1.10ps (down from A\$1.20) approximates our current A\$ valuation (A\$1.06/share).
- **Catalysts:** Upcoming catalysts may include confirmation of high silver grades and economic attractiveness of the expanded Perkoa mine, and drilling success at the Mumbwa copper project in Zambia.

Market Valuations: Copper projects

Comparable Copper Projects: Metrics*



* Average 4.3c/lb and 0.47% Cu Equiv, excluding BTR. BTR assumes 100% of Mumbwa. Calculations exclude potential value of other assets within listed companies, based on primary asset.

Source: Company reports/ Investec Bank (Australia) Ltd estimates

Blackthorn Resources

Risks to valuation, recommendation & target price

- BTR is an early-stage exploration/production company; hence, it is reliant on subjective definition resource valuation
- BTR is exposed to political risks in African countries Zambia and Burkina Faso
- BTR is exposed to construction risk at Perkoa, and commodity price (namely zinc) risk
- Our valuation of the copper asset is high risk, and relatively subjective due to pre-feasibility status

Board members

Bill Cash, Chairman

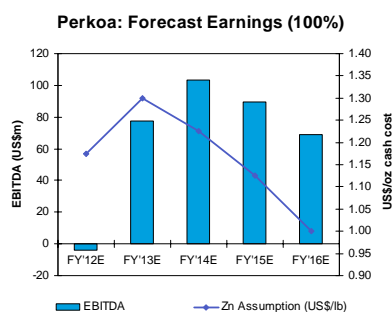
Scott Lowe, Managing Director

Nicki Bowman, Non-Executive Director

Michael Oppenheimer, Non-Executive Director

Major Shareholders

Glencore International	13.0%
North Sound	8.9%
F Brewer	7.0%
JP Morgan	6.2%



Source: Investec Bank (Australia) Ltd estimates

Perkoa Zinc Mine, Zambia (BTR, 39.9%; Glencore, 50.1%)

Glencore as operator has been drilling to extend the known ore reserves, with potential to add high grade silver and lead ore to the mine plan. We believe they are halfway through a 12-hole program, with assays expected in August 2011. Production is scheduled from mid-2012E at a rate of about 90kt zinc metal (720ktpa @ 13.9% Zn); however, throughput expansion to 1mtpa, with addition of a lead/silver circuit is being investigated. This scenario appears probable, and we allow an additional A\$20m in capital. Our Perkoa NPV is US\$235m (unrisked) assuming a US\$1,500/t cash cost (JV hopes to do better than this) and assuming up to 0.5moz of silver per year is payable.

We currently value the mine at US\$164m (8% NPV) allowing for a 30% NPV discount for pre-construction/ramp-up risk, up US\$22m on our last published valuation due to the expanded case being adopted. Applying spot prices, value rises to US\$272m (risky), due to applying a US\$40/oz silver price. Increasing our LT zinc price to US\$1.20/lb increases our current valuation by 44%, indicating strong leverage to the metal.

Mumbwa Project, Zambia (BTR, 100%)

BHP had spent substantial funds on exploration, and was required to make a back-in payment of US\$13m to continue further and would need to fund another US\$20m (estimate) to fund the pre-feasibility required under the agreement. The project may not have met BHP scale criteria and BHP recently advised of its intention to withdraw from the JV. BTR sees scope in untested geophysical targets and potential expansion on the existing resource of 345mt @ 0.47% Cu at Kitumba (including 87mt @ 0.94% Cu and 22mt @ 1.73%). A total of 26 holes were used in the resource calculation. BHP will retain a 2% production royalty, with Glencore having the right to purchase 20% of any production and first right of refusal of any new joint venture BTR may seek to establish.

Whilst large-scale mining economics appear uncertain, the 22mt @ 1.73% may present a smaller scale mining scenario, and the resource is open at depth and along strike. The deposit is of similar grade to Discovery Metals (DML's) Zeta underground deposit (25mt @ 1.7% Cu equivalent). A total of 14 holes are planned in the current A\$5m program, about 7000m of drilling, with 9 infill holes and 4 step-out holes. The aim of the drilling is to upgrade the resource category (potential grade/size increase). Additional scout holes are being considered. We would expect completion of the program in late 2011.

On average, large tonnage projects grading 0.5% Cu equivalent have been changing hands for about US\$0.06/lb (EV) in recent years on our calculations, or including current listed TSX/ASX peers, the average is US\$0.043/lb. Using a conservative value of 50% of this amount (or US\$0.02/lb), we value 100% of the project at US\$72m. BTR is currently trading at US\$0.014/lb Cu (EV) excluding any valuation for Perkoa.

Summary: With drilling results due on both projects this half, and both copper and base metal valuations mostly intact, we see good upside for the BTR share price, particularly as the Perkoa upside case is confirmed, and the future development potential of Mumbwa becomes clearer. Investors in BTR have the benefit of two projects, with the company currently only being valued by the market for one project. We agree a degree of caution is warranted for both projects; however, we feel the current asset quality is not adequately reflected in the share price. We thus expect price appreciation on de-risking.

Strengths

- Production from mid-2012E could enable the company to grow via acquisition or organically
- Conservative and experienced management team appears focused on shareholder value without excess risk

Weaknesses

- Reliance on JV partners to manage project; hence, there is limited control over direction
- Two projects in Burkina Faso, one in Zambia; hence, there is high political risks
- Commercial potential of copper project uncertain; hence, the value is subjective

Opportunities

- Expansion of Perkoa to 1mtpa, and addition of a silver circuit could be a major boost to valuation
- Expansion of resource and potential for grade improvement at Kitumba, Mumbwa project in Zambia
- Completion of scoping/PFS studies to indicate mining potential and economics

Threats

- Minority interests in projects tend to dilute investor interest
- African risk is a consideration
- Significant discount to valuation and peer group comparison means company is vulnerable

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	All countries excl South Africa	South Africa
	Expected total return	
Buy	> 10%	> 20%
Hold	-10% to 10%	10% to 20%
Sell	< -10%	< 10%

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