

21 May 2014

Alara Resources

AUQ A\$0.08/share

Zinc prices on the rise

BUY

Following the strong price rises in nickel, we believe the scene is set for zinc to be the next metal to run. Driven by strong fundamentals, the key drivers comprise (i) ongoing market deficits due to significant mine closures (ii) falling LME stockpiles - down 39% in the past 18 months and (iii) demand support from China (net importer) coupled with improving demand from the US and Europe. The lack of choice for investors to play zinc (on the ASX) highlights Alara as a standout in our view. AUQ's Khnaiguiyah project is expected to produce 80-90ktpa Zn at low cost over an initial 13 year mine life. We maintain our BUY recommendation with NPV of A\$0.54/share.

Zinc fundamentals are strong (Figs.1-4, 7-8)

- Price has risen 11% over 6 months to US\$0.95/lb.
- LME stockpiles have fallen 39% this year to 751kt.
- Demand driven by auto, infrastructure and housing.
- China consumes ~45% (6Mt) of global zinc supply.
- China is a net importer of zinc at ~0.3Mtpa.
- Global supply is reducing due to mine closures:
 - Brunswick 175ktpa (closed 2013)
 - Perseverance 145ktpa (closed 2013)
 - Lisheen 170ktpa (closing 2014)
 - Century 500ktpa (closing mid 2015)
 - Paragashu 45ktpa (closing 2015)
 - Skorpion 160ktpa (closing 2016)
- Market deficits are forecast over the long term.
- CRU forecast zinc price rising to US\$1.73/lb in 2016.

Very few ways to play zinc on the ASX (Figs.5-6,9-10)

- Alara – low cost (46c/lb) project in Saudi.
- Ironbark – high cost (90c/lb) project in Greenland.
- Terramin – Angas zinc mine depleted and closed 2013.
- Perilya – taken over by the Chinese in 2013.
- Kagara – went into administration in 2012.
- CBH Resources – taken over by Japanese in 2010.
- Zinifex/Oxiana – zinc mines bought by Chinese 2009.

Khnaiguiyah Zinc - Copper Project (60%)

- EBITDA of A\$100Mpa (first 7 years).
- Free cashflow (after payback of capex) of A\$467M.
- Capex – US\$257M based on a fixed price (EPC).
- Three year capital payback with a 13 year mine life.
- First production estimated Q1 2017.
- Production – 80-90ktpa Zn, 5.8ktpa Cu (years 1-7).
- Cash costs – US46c/lb (years 1-7) after copper credits.

Company Data

Shares – ordinary	308.7M
Options (\$0.10-0.70/share – out of the money)	36.8M
Market Cap	\$24.1M
12 month low/high	\$0.04 / \$0.14
Average monthly turnover	\$0.8M
Average monthly volume	11.5M

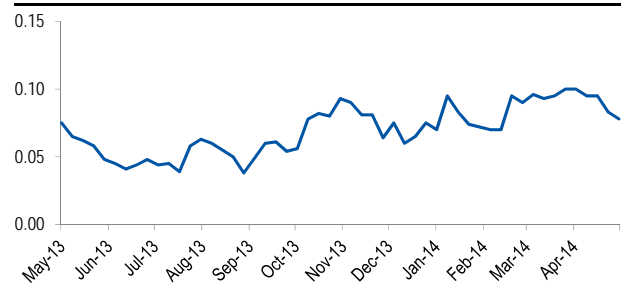
Financial Summary (fully diluted/normalised)

Year end June	2013A	2014F	2015F	2016F	2017F
Revenue (\$M)	0.0	0.0	0.0	22.8	152.2
Costs (\$M)	6.9	6.3	6.7	19.0	84.4
EBITDA (\$M)	(6.9)	(6.3)	(6.7)	3.9	67.8
NPAT (\$M)	(6.7)	(6.5)	(11.1)	(8.0)	34.6
EPS (¢ps)	(2.9)	(2.1)	(3.6)	(2.6)	11.2
EPS Growth (%)	na	na	na	na	>100
PER (x)	na	na	na	na	0.7
Cashflow (\$M)	(3.6)	(6.5)	(11.1)	(6.0)	57.2
CFPS (¢ps)	(1.5)	(2.1)	(3.6)	(1.9)	18.5
PCFPS (x)	na	na	na	na	0.4
Enterprise Value (\$M)	6	30	159	238	184
EV / EBITDA (x)	na	na	na	61.5	2.7

Substantial Shareholders (FPO)

	Shares (M)	(%)
Acorn	26.6	11.0%
Northcape	21.8	9.0%
Antares	17.2	7.1%

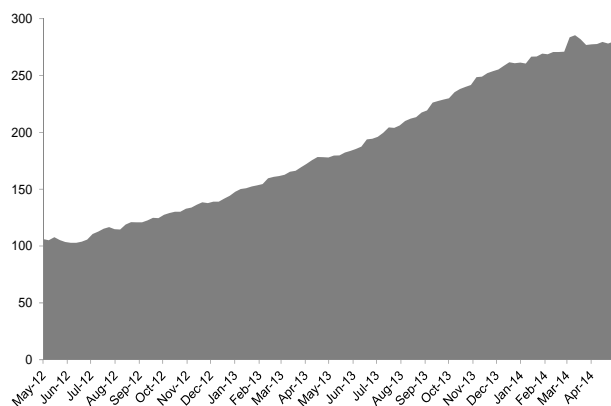
AUQ (A\$/share) – performance over one year



This report must be read with the disclosure and disclaimer on the final page of this document.

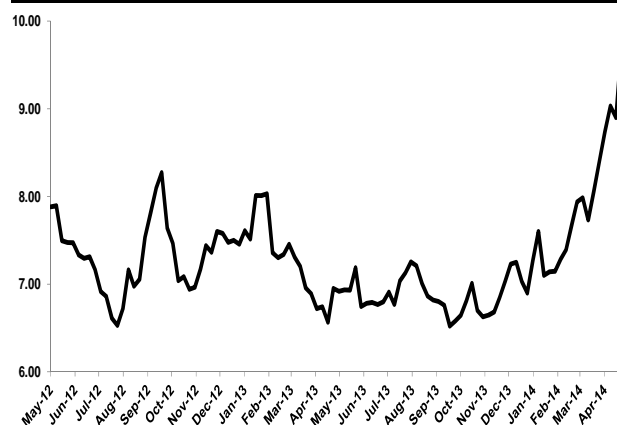
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Figure 1: Nickel LME Stocks (kt) – 2 years



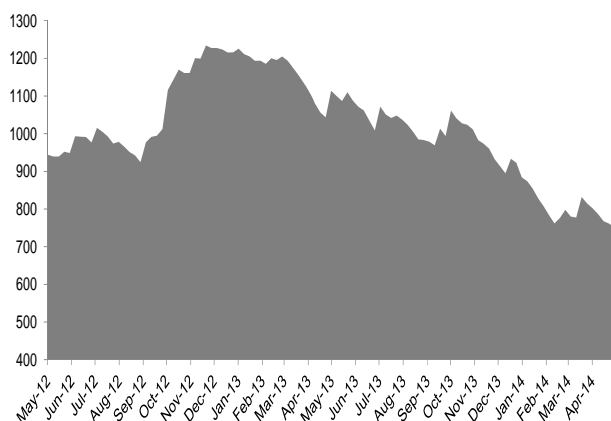
Nickel stockpiles have almost tripled since 2012.

Figure 2: Nickel Price (US\$/lb) – 2 years



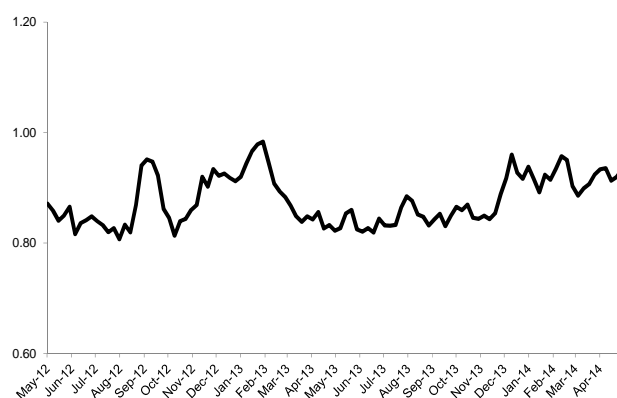
Nickel price has risen 43% in the past 5 months, reflecting expected market deficits in the coming years.

Figure 3: Zinc LME Stocks (kt) – 2 years



Zinc stockpiles have fallen 39% (485kt) since Dec 2012.

Figure 4: Zinc Price (US\$/lb) – 2 years



Zinc Price has risen 11% over the past 6 months and set for strong gains with forecast market deficits.

Source: IRESS

Source: IRESS

Figure 5: Nickel – several companies to invest in

Company	ASX	Status
Western Areas	WSA	Producer
Panoramic Resources	PAN	Producer
Independence Group	IGO	Producer
Mincor Resources	MCR	Producer
Poseidon Nickel	POS	Emerging Producer
Sirius Resources	SIR	Emerging Producer

Source: Petra Capital

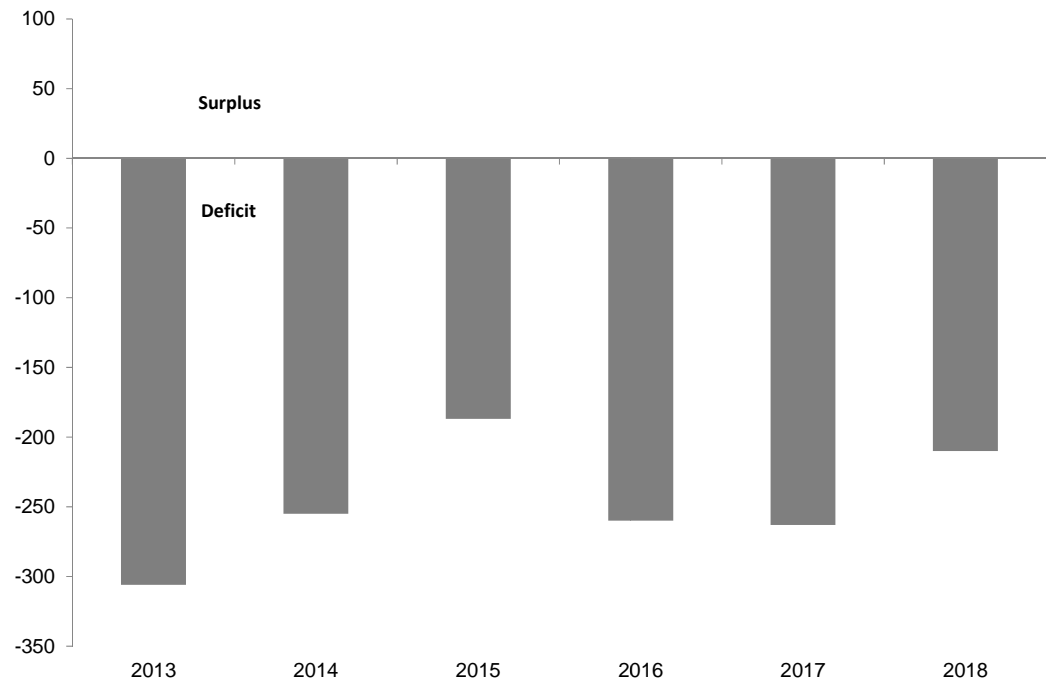
Figure 6: Zinc - very few companies to invest in

Company	ASX	Status
Alara Resources	AUQ	Emerging Producer
Ironbark Zinc	IBG	Emerging Producer
Blackthorn Res	BTR	Perkoa mine sold 2014
Terramin	TZN	Angas mine closed 2013
Perilya	PEM	Taken over by Chinese 2013
Kagara	KZL	Administration 2012
Jabiru Metals	JML	Taken over by IGO 2011
CBH Resources	CBH	Taken over by Toho 2010
Zinifex/Oxiana	ZFX/OXR	MMG buys zinc mines 2009
Herald	HER	Taken over by Bumi 2008

Source: Petra Capital

Figure 7: Zinc Market Deficits (kt)

Wood Mackenzie
forecast significant
market deficits over
the next 5 years.

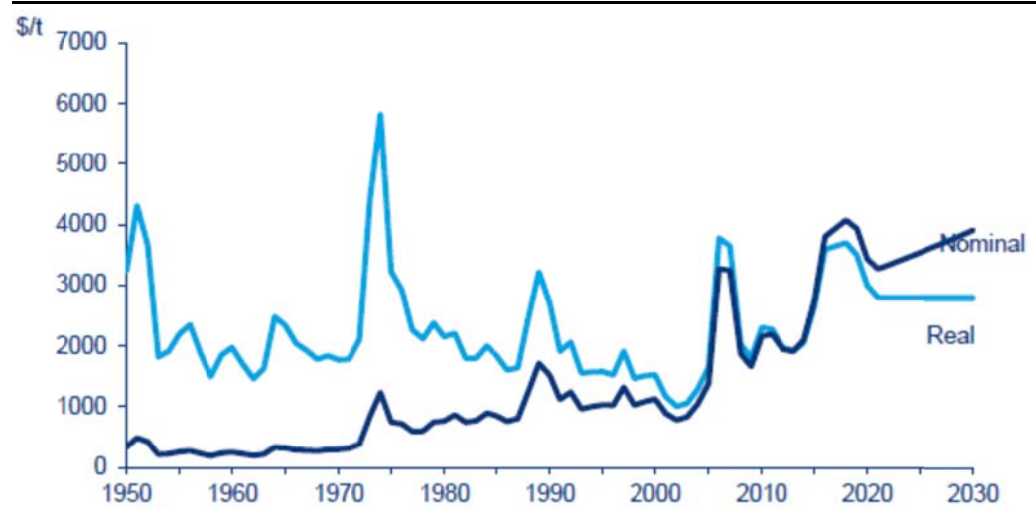


Source: Wood Mackenzie

Figure 8: Zinc price forecasts (US\$/t)

Zinc prices are
forecast to rise
significantly in the
coming years.

In 2006 and 2007,
zinc prices averaged
over US\$3,300/t
(US\$1.50/lb) peaking
at US\$4,600/t
(US\$2.10/lb).



Source: Wood Mackenzie

Figure 9: Zinc (mined production)

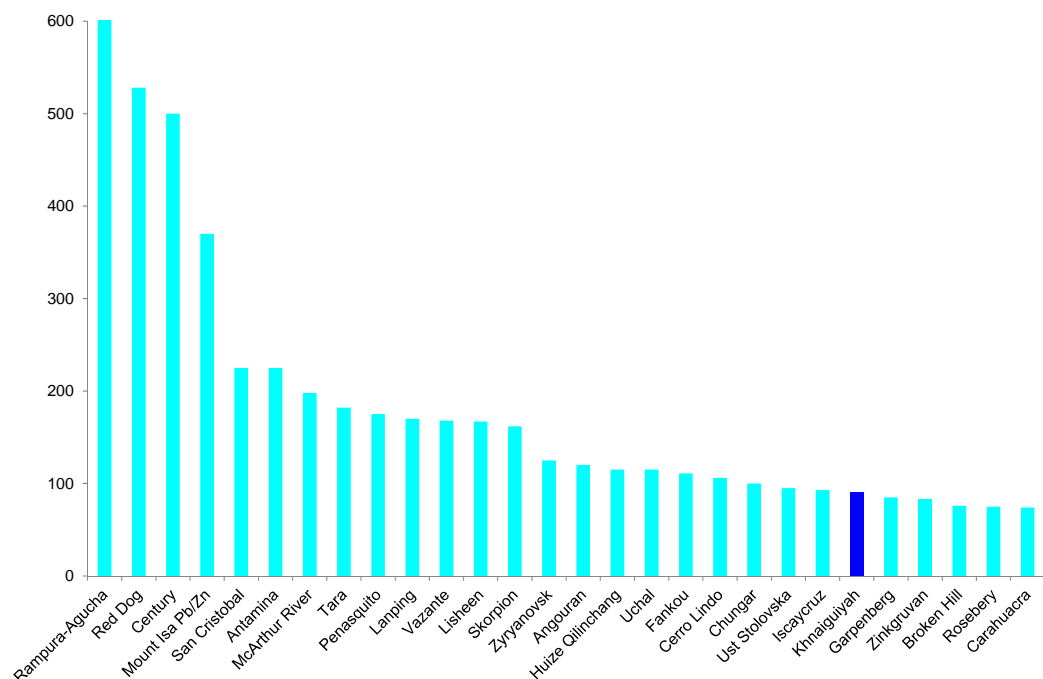
<p>The top 10 zinc miners are dominated by major companies.</p> <p>Global annual production is estimated at ~14Mtpa of which the top 10 make up 32%.</p>	Rank	Company	kt	% World	% Cumulative
	1	Glencore	868	6.2%	6.2%
	2	Hindustan Zinc	827	5.9%	12.0%
	3	Teck	625	4.4%	16.4%
	4	MMG Limited	600	4.3%	20.7%
	5	Votorantim	299	2.1%	22.8%
	6	Xstrata AG	296	2.1%	24.9%
	7	Boliden	272	1.9%	26.8%
	8	Nyrstar	271	1.9%	28.8%
	9	Minera Volcan	251	1.8%	30.5%
	10	Sumitomo	204	1.4%	32.0%

Source: Wood Mackenzie

Figure 10: Top 28 Zinc Mines by production (ktpa)

Planned production of ~90ktpa at Khnaiguayah sees it ranked at number 23.

Potential exists for Khnaiguayah to move into the top 10 should Heavy Media Separation be successful.



Source: Wood Mackenzie, Petra Capital

Analysis

ALARA RESOURCES

(AUQ)

20-May-14

Year End 30 June	A\$					
PROFIT & LOSS						
		2013A	2014F	2015F	2016F	2017F
Sales Revenue	\$M	0.0	0.0	0.0	22.8	152.2
Other Income	\$M	0.0	0.0	0.0	0.0	0.0
Operating Costs	\$M	3.9	6.3	6.7	19.0	84.4
Exploration	\$M	3.1	0.0	0.0	0.0	0.0
Other	\$M	0.0	0.0	0.0	0.0	0.0
EBITDA	\$M	(6.9)	(6.3)	(6.7)	3.9	67.8
Dep. & Amort.	\$M	0.0	0.0	0.0	2.0	17.8
EBIT	\$M	(6.9)	(6.3)	(6.7)	1.8	50.0
Net Interest	\$M	(0.2)	0.2	4.4	9.9	10.6
Pre-Tax Profit	\$M	(6.7)	(6.5)	(11.1)	(8.0)	39.4
Tax	\$M	0.0	0.0	0.0	0.0	4.7
Minorities	\$M	0.0	0.0	0.0	0.0	0.0
Net Profit	\$M	(6.7)	(6.5)	(11.1)	(8.0)	34.6
Abnormal	\$M	(0.2)	0.0	0.0	0.0	0.0
Reported Profit	\$M	(6.9)	(6.5)	(11.1)	(8.0)	34.6
Dividends	\$M	0.0	0.0	0.0	0.0	0.0
Adjustments	\$M	0.0	0.0	0.0	0.0	0.0
Retained Earnings	\$M	(29.3)	(35.8)	(46.9)	(54.9)	(20.3)
CASH FLOW						
Revenue	\$M	0.0	0.0	0.0	22.8	152.2
Costs	\$M	(3.9)	(6.3)	(6.7)	(19.0)	(84.4)
Net Interest	\$M	0.3	(0.2)	(4.4)	(9.9)	(10.6)
Tax Paid	\$M	0.0	0.0	0.0	0.0	0.0
Gross Cash Flow	\$M	(3.6)	(6.5)	(11.1)	(6.0)	57.2
Net Capex	\$M	(10.3)	(2.0)	(118.6)	(74.0)	(2.5)
Exploration	\$M	0.0	0.0	0.0	0.0	0.0
Dividends	\$M	0.0	0.0	0.0	0.0	0.0
Other	\$M	0.0	(6.4)	1.3	0.0	0.0
Free Cashflow	\$M	(13.9)	(14.9)	(128.4)	(79.9)	54.7
Equity Issues	\$M	7.5	0.0	0.0	0.0	0.0
Net Borrowings	\$M	0.0	10.0	140.0	85.0	(50.0)
Net Investments	\$M	0.0	4.4	0.0	0.0	0.0
Surplus Cash Flow	\$M	(6.4)	(0.5)	11.6	5.1	4.7
BALANCE SHEET						
Cash	\$M	4.5	3.9	15.5	20.6	25.3
Other Current	\$M	1.3	0.0	0.0	0.4	1.5
Total Current	\$M	5.8	3.9	15.5	21.0	26.8
Fixed Assets	\$M	29.5	31.5	150.2	222.1	206.8
Exploration	\$M	0.0	0.0	0.0	0.0	0.0
Intangibles	\$M	0.0	0.0	0.0	0.0	0.0
Other	\$M	5.7	12.1	10.8	10.8	10.8
Total NC Assets	\$M	35.3	43.6	161.0	232.9	217.5
TOTAL ASSETS	\$M	41.0	47.6	176.5	253.9	244.4
Total Debt	\$M	0.0	10.0	150.0	235.0	185.0
Current Liab	\$M	1.8	1.8	1.8	1.8	6.5
Non Current Liab	\$M	1.8	4.9	4.9	5.3	6.4
TOTAL LIAB	\$M	3.6	16.6	156.6	242.1	197.9
NET ASSETS	\$M	37.5	30.9	19.9	11.8	46.5
SH/HLDRS FUNDS	\$M	37.5	30.9	19.9	11.8	46.5
RATIO ANALYSIS						
EPS	¢	(2.9)	(2.1)	(3.6)	(2.6)	11.2
PER	x	na	na	na	na	0.7
EPS Growth	%	na	na	na	na	>100
EBITDA per share	¢	(3.0)	(2.0)	(2.2)	1.3	22.0
EBITDA Multiple	x	(1.5)	(3.8)	(3.6)	6.2	0.4
EV/EBITDA	x	(0.9)	(4.8)	(23.6)	61.5	2.7
CFPS	¢	(1.5)	(2.1)	(3.6)	(1.9)	18.5
PCFR	x	na	na	na	na	0.4
DPS	¢	0.0	0.0	0.0	0.0	0.0
Yield	%	0.0	0.0	0.0	0.0	0.0
Franking	%	0	0	100	100	100
Payout Ratio	%	0%	0%	0%	0%	0%
Gearing D/E	%	na	20	677	1,813	344
Interest Cover	x	30.7	na	na	0.2	4.7
EBITDA Margin	%	na	na	na	17.0	44.6
EBIT Margin	%	na	na	na	8.1	32.8
Return On Assets	%	(16.9)	(13.3)	(3.8)	0.7	20.5
Return On Equity	%	(17.9)	(21.1)	(55.8)	(67.9)	74.5
Eff Tax rate	%	0	0	0	0	12
OTHER DATA						
Share Price	\$/sh.	0.05	0.08	0.08	0.08	0.08
Number of shares	M	231	309	309	309	309
Market Capitalisation	\$M	10	24	24	24	24
EV	\$M	6	30	159	238	184

Share Price	(\$)	0.08
Iss. Shares	(M)	308.7
Iss. Options (unlisted)	(M)	36.8 Ex @ \$0.10-\$0.70
Equity	(M)	308.7
Mkt Cap.	(\$M)	24.1



RESERVES / RESOURCES		2013A	2014F	2015F	2016F	2017F
Reserves						
Tonnes	Mt	29.96	29.99	29.96	29.59	27.42
Copper	%	0.24	0.24	0.24	0.24	0.23
Zinc	%	3.30	3.30	3.30	3.29	3.17
Resources						
Tonnes	Mt	38.10	38.10	38.10	37.70	35.53
Copper	%	0.27	0.27	0.27	0.27	0.26
Zinc	%	2.98	2.72	2.72	2.70	2.58
PRODUCTION (100%)						
Khnaiguiyah						
Tonnes	Mt	0.00	0.00	0.00	0.40	2.17
Copper	%	0.00	0.00	0.00	0.35	0.40
Zinc	%	0.00	0.00	0.00	4.00	4.80
Metal in concentrate (pre-charges)						
Cu in concentrate	T	0	0	0	1,246	7,812
Zn in concentrate	T	0	0	0	14,560	95,827
ATTRIBUTABLE REVENUE (post smelter charges)						
Project						
Khnaiguiyah	ASM	0.0	0.0	0.0	22.8	152.2
Other	ASM	0.0	0.0	0.0	0.0	0.0
Total	ASM	0.0	0.0	0.0	22.8	152.2
Commodity						
Copper	ASM	0.0	0.0	0.0	5.2	31.8
Zinc	ASM	0.0	0.0	0.0	17.6	120.4
Other	ASM	0.0	0.0	0.0	0.0	0.0
Total	ASM	0.0	0.0	0.0	22.8	152.2
ATTRIBUTABLE COSTS (includes treatment charges)						
Khnaiguiyah	ASM	3.4	3.3	3.7	15.5	80.4
Corporate and Other	ASM	0.4	3.0	3.0	3.5	4.0
Total	ASM	3.8	6.3	6.7	19.0	84.4
Cash Costs (pre credits)	US\$/lb	0.00	0.00	0.00	0.81	0.63
Cash Costs (after credits)	US\$/lb	0.00	0.00	0.00	0.54	0.38
Cash Costs (all-in)	US\$/lb	0.00	0.00	0.00	0.83	0.44
ATTRIBUTABLE CAPEX						
Khnaiguiyah	ASM	8.8	2.0	118.6	74.0	2.5
Other	ASM	1.5	0.0	0.0	0.0	0.0
Total	ASM	10.3	2.0	118.6	74.0	2.5
ATTRIBUTABLE DEPRECIATION & AMORTISATION						
Khnaiguiyah	ASM	0.0	0.0	0.0	2.0	17.8
Other	ASM	0.0	0.0	0.0	0.0	0.0
Total	ASM	0.0	0.0	0.0	2.0	17.8
HEDGING						
Copper hedged	t	0	0	0	0	0
Currency hedged	A\$/US\$	0	0	0	0	0
Hedged price	US\$/lb	0	0	0	0	0
Hedged price	A\$/lb	0	0	0	0	0
Sales hedged	%	0%	0%	0%	0%	0%
Ave. price deliv.-Cu	US\$/lb	3.47	3.19	3.06	2.88	2.75
Ave. price deliv.-Cu	A\$/lb	3.38	3.53	3.47	3.34	3.24
Zinc hedged	t	0	0	0	0	0
Currency hedged	A\$/US\$	0	0	0	0	0
Hedged price	US\$/lb	0	0	0	0	0
Hedged price	A\$/lb	0	0	0	0	0
Sales hedged	%	0%	0%	0%	0%	0%
Ave. price deliv.-Zn	US\$/lb	0.87	0.90	0.95	0.93	0.95
Ave. price deliv.-Zn	A\$/lb	0.85	0.99	1.07	1.08	1.12
ASSUMPTIONS						
Exchange Rate	A\$/US\$	1.02	0.90	0.86	0.86	0.85
Zinc	US\$/lb	0.87	0.90	0.95	0.93	0.95
Lead	US\$/lb	0.97	0.95	0.95	0.95	0.95
Copper	US\$/lb	3.47	3.19	3.06	2.88	2.75
Gold	US\$/oz	1595	1308	1300	1263	1250
Silver	US\$/oz	28.82	20.66	20.00	20.00	20.00
90 day Bank Bills	%	3.15	2.62	2.55	2.63	2.88
10 Yr Bond rate	%	3.29	4.02	3.75	3.38	3.38
Int. Rate Charged	%	4.29	5.02	4.75	4.38	4.36
VALUATION						
Khnaiguiyah - Saudi	ASM				193.1	\$0.63
Washihi - Oman					7.5	\$0.02
Exploration					5.0	\$0.02
Corporate and Other					(32.0)	\$ (0.10)
Net Cash (Debt)					(6.1)	-\$0.02
Total					167.5	\$0.54

Source: Petra Capital

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