

ANALYST: PETER KOPETZ

Recommendation

Spec Buy

Stock Type

HIGH RISK

Morningstar Fair Value

\$n/a

State One Valuation

\$0.30c

Consensus Valuation

\$n/a

NTA

\$n/a

Management

J. Dawkins	Chair.
P. Meers	Ex. D/Ch
I. Levy	MD
W. Huang	N/Ex Dir.
K. Boundy	N/Ex Dir.

Substantial Shareholders

Hudson Resources	28.73%
Gleneagle Securities	10.08%
Washington Soul	5.49%

Key Risks

Mining Approvals

Development & Execution risk

Bauxite price

Exchange Rate

Australian Bauxite (ABZ) - \$0.15c

ABZ's strategy has consistently been to identify quality bauxite close to infrastructure and with low socio-environmental impacts. Tasmania emerged in 2010 as a possible destination with the discovery of bauxite similar in nature to Taralga and nearby deposits. With costs being the key, focus shifted to Tasmania where a positive scoping study is being completed on a possible mining operation at Bald Hills. The scoping study will most likely reveal a relatively low cost project underpinned by simple mining methods, short distance to port and existing infrastructure. The plan is to mine Bald Hill, mine nearby deposits and develop a Tasmanian bauxite industry.

1.0 TASMANIAN BAUXITE KEY POINTS

- Tasmanian bauxite is gibbsite rich, which only requires low temperature for processing at an alumina refinery thus aiding in reducing alumina production costs.
- Identified deposits are located close to existing infrastructure such as roads and rail, on land with little to no environmental issues, and free of socio-political opposition.
- With the nation's highest unemployment, Tasmania offers an eager and experienced workforce having a rich mining history.
- Port of Bell Bay is underutilised and spare capacity exists for exports which is advantageous as it could aid in reducing infrastructure spend. A MoU has been executed between ABZ and Tasmanian Ports Corporation for access to Port of Bell Bay.
- Existing rail and road networks are excellent and offer low transport costs as deposits are in close proximity to port.
- Tasmania seems abundant with bauxite and offers great potential to establish a long life bauxite mining industry.

2.0 BALD HILLS

- Bald Hills is the first project for ABZ in Tasmania as it's ideally situated, being close to port, in close proximity to associated infrastructure and 4km from Campbell Town which could provide some of the workforce.
- One of the key reasons Bald Hills was selected as the first mining project in Tasmania was the approvals process, which seems straight forward enabling mining to commence from late 2014. The mining lease application was submitted in early May and a Notice of Intent was lodged with the EPA at the same time.
- Bauxite at Bald Hills is very good quality and ideal for special purpose blending, enhancing final alumina quality at refineries.
- The expected capital cost at Bald Hills is ~\$8-10M, with total operating costs ~\$30/t. Using long term bauxite price assumptions, we expect margins of between \$15-\$17/t.

Possible Products From Bald Hill	Yield %	Al2O3avl %	Rx SiO2 %	avl/rx ratio	Al2O3 %	SiO2 %	A/S ratio	Fe2O3 %	TiO2 %	LOI %	Mix %
DSO from main Bald Hill deposit	100%	36.8	3.1	11.9	42.9	3.7	11.5	24.3	3.2	25.1	
DSO+dry-screened, main deposit	80.5%	36.0	2.9	12.3	41.9	3.6	11.7	26.0	3.0	24.8	70%
Raw bauxite from low grade deposit	100%	26.3	3.7	7.0	34.5	4.9	7.0	34.6	4.6	20.4	
Low grade plus screened layer	83.4%	28.1	3.5	8.1	36.0	4.7	7.7	32.3	4.8	21.2	15%
Raw clay-contaminated bauxite	100%	20.3	6.5	3.1	29.8	9.0	3.3	34.4	7.3	16.8	
Clay-rich bauxite dry-screened	75%	28.2	2.8	10.1	33.9	3.3	10.4	31.5	8.1	19.4	15%
Possible average production	80%	33.7	3.0	11.3	39.9	3.7	10.8	27.7	4.0	23.5	

3.0 MINING

ABZ is planning to start production at Bald Hills at ~500kt per annum. We see this increasing to ~2.5Mtpa as more new mines come on stream. On current numbers we expect a mine life of ~6 years but we are confident that new mines will be added and production extended well beyond 2020. Second mine has already been put forward at Fingal Rail which is in close proximity to Bald Hills and will only require a modest capex to bring into production.

Our modelling (based on 100% ownership) assumes capex of ~\$10M and opex of ~\$30/t which will give ABZ margins of ~\$17/t. Bald Hills project NPV₁₀ equates to ~\$18M or 16c per share.

Mining Parameters Assumptions

Mining	500ktpa
Mine life	6 years
AUD/USD	90c
Bauxite Price (CIF)	US\$62.00/t
Bauxite Price (FOB)	A\$47.20/t
Capex	A\$10M
Opex	A\$30/t
NPV ₁₀	A\$18.2M

Source: State One

4.0 XINFA

Xinfa, a major Chinese aluminium company has signed a term sheet with ABZ on two key Tasmanian bauxite projects, whereby Xinfa can elect to invest in both projects and take an equity position in ABZ. If the agreement is executed, it will see Xinfa fully fund ABZ's first two bauxite projects and be the key off-take partner.

Key Terms of Xinfa Term Sheet

- Initial \$500k as an exclusivity payment 'EP'
- A MoU to be executed at end of exclusivity period (due diligence) at which time Xinfa will pay an additional \$2m for a 5.8% equity in ABZ through the issue of 6.58M shares at \$0.38c per share. The EP will fully convert to shares as part of this placement.

Agreed Commercial Terms

1. Xinfa is to acquire a 50% interest in the Projects through:

- a. funding all pre-production costs for the first mine of each project including due diligence costs, evaluation costs, feasibility studies costs, lease payments, project development-construction costs and working capital (Development Costs);
- b. providing marketing management with ABx management participation;
- c. taking at least 50% of bauxite production from the Projects (see 3 below); and,
- d. taking up to 100% of bauxite production from the Projects if requested by ABx.

2. ABx will:

- a. provide Australian project management together with Xinfa senior management participation;
- b. manage and operate exploration activities over the project areas;
- c. manage statutory and government relations;
- d. manage land and tenement administration;
- e. repay its proportion of Development Costs through an agreed mechanism that ensures ABx will receive a positive cashflow whilst repaying its proportion of Development Costs (see 3a. below).

3. Until ABx has repaid its proportion of Development Costs, Xinha will have the right to:

a. Continue with its 50% interest in the Project and elect each year to take and market an additional 20% of production by a payment of costs and outgoings plus US\$5 per tonne for the additional 20% of tonnage. Profit earned by Xinha from this additional 20% of tonnage will reduce ABx's outstanding proportion of Development Costs.

b. Take a 70% interest in the Project by purchasing 20% equity in the Project for a payment per tonne of identified bauxite resources at the time of purchase plus the forgiveness of any outstanding ABx proportion of Development Costs. Should resources increase in future, Xinha will pay ABx a further payment per tonne of the additional 20% of increased bauxite tonnages, payable when shipped.

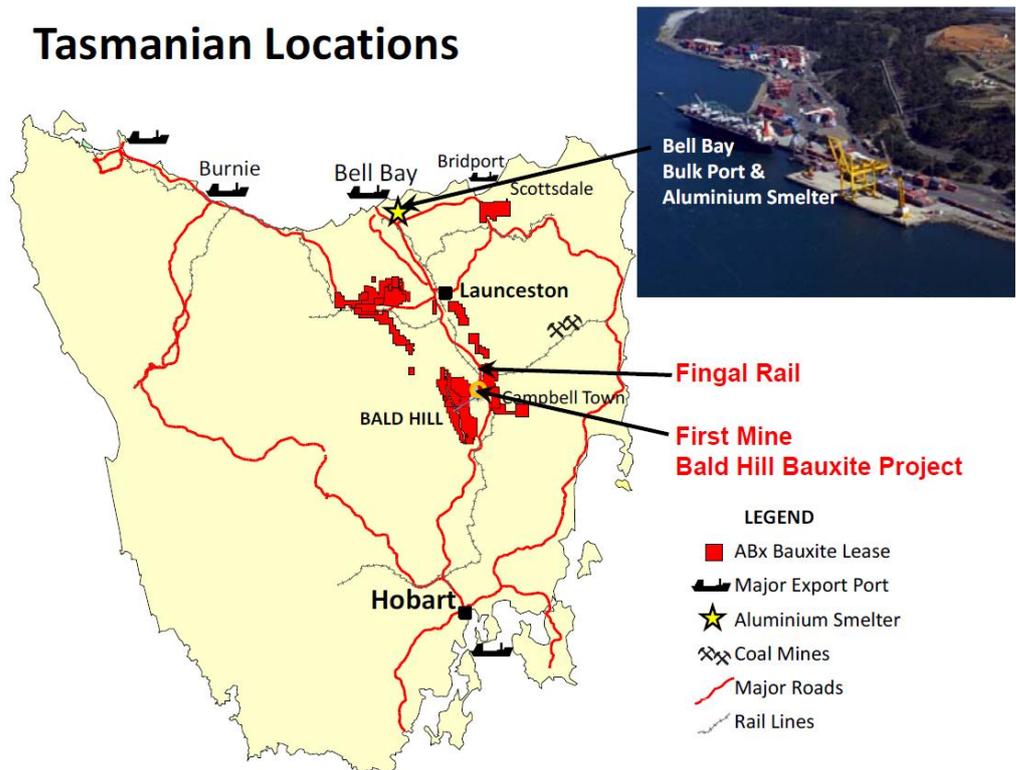
4. Xinha has the right to first negotiation for other ABx projects including the Binjour Project.

5.0 INVESTMENT THESIS

Our modelling suggests that ABZ is grossly undervalued and Tasmania alone, if mining rate of ~2.5mtpa is achieved, is valued at ~50c per share of which we attribute 16c per share to Bald Hills Project. Key risks for ABZ are execution and development risks as well as mining approvals. If ABZ successfully delivers the project on time and budget, risks decrease significantly and we expect truer value of ABZ to be reflected in its share price. We have set a Speculative Buy on ABZ with a valuation of 30c which incorporates Bald Hills and Fingal Rail as the first two mines.

6.0 TASMANIAN LOCATIONS

Tasmanian Locations



Source: ABZ

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