

Avoca BUY

Current Price: **\$2.26**
Target: **\$2.87**

Ticker: AVO
Sector: Metals & Mining

Shares on Issue (m): 221.1
Market Cap (\$m): 499.6
Net Cash (Debt)(\$m): -49.2
Enterprise Value (\$m): 548.8

52 wk High/Low: **\$2.91** **\$1.26**
12m Av Daily Vol: 710,000

Key Metrics

	09F	10F	11F
P/E (x)	23.7	16.5	14.0

Financials:

	09F	10F	11F
Revenue (\$m)	140.5	179.0	175.9
EBIT (\$m)	36.1	49.6	57.0
NPAT (\$m)	22.1	31.9	37.6

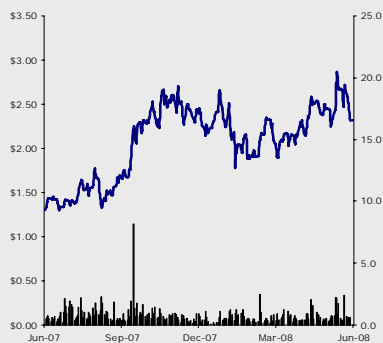
	09F	10F	11F
Net Assets (\$m)	113.8	145.7	183.3

	09F	10F	11F
Op CF (\$m)	42.6	55.2	51.2

Per Share Data:

	09F	10F	11F
EPS (cps)	9.5	13.7	16.2
DPS (cps)	0.0	0.0	0.0
Div Yield	0.0%	0.0%	0.0%
CFPS (cps)	18.3	23.8	22.1

Share Price Graph



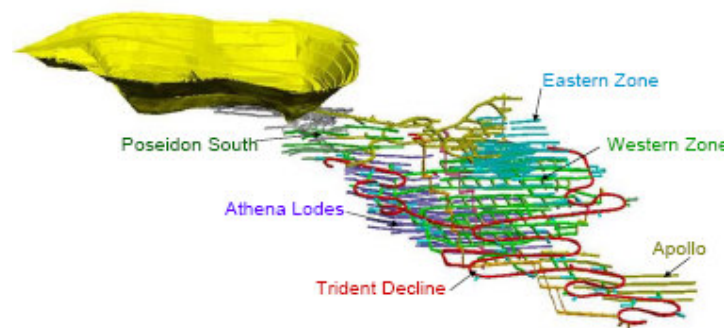
Higginsville Site Visit

The stand-out Aussie gold story

Argonaut considers AVO to be the stand-out Australian gold story over the past three years. Higginsville continues to shape up well. The argument has always been simple – good people developing the high grade Trident ore body (5.3g/t reserve).

Argonaut visited one of the early narrow Eastern Zone stopes. The ground conditions are terrific (shallow depth and competent rock types) with limited water to manage. Mine production will be ramped up when the first of the large Western Zone stopes comes on line in October / November.

Figure 5. LOM development layout



Source: AVO

Plant commissioning on time and on budget

The highlight of the tour however was the opportunity to climb all over the brand new 1Mtpa Higginsville CIL treatment plant. Commissioning is underway with completion expected by the end of June 2008 (on time and on budget with commencement of high grade feed anticipated in early July).

Figure 6. Gleaming new plant



Source: Argonaut

High quality facilities attracting key personnel...

AVO has had tremendous recruitment success, with all key on-site positions filled. The architecturally designed camp is a big draw card, with high quality messing facilities for the FIFO workforce.

... but costs may be come under pressure...

AVO's April 2008 presentation at the Paydirt Gold Conference lists a reserve life cash cost estimate of \$369/oz (from the December 2006 Feasibility Study). Given recent cost pressures this figure could rise significantly unless the grade surprises strongly on the upside. Until a track record of steady state production of 170kozpa is achieved it will be difficult to know how the costs are performing.

... as power station is diesel fired

One expense item to monitor is energy. Higginsville is not on grid power and electricity is supplied from a 10MW diesel fired power station. The cost of power is expected to be at least 30c/kWh, depending upon diesel prices. The power station is gas capable however the price of gas at the mine gate offers no current advantage over diesel. Trident ore has a work index of 18kWh/t.

Figure 7. Higginsville diesel power station



Source: Argonaut

Unhedged exposure to the gold price

AVO offers an unhedged exposure to the gold price. The company recently purchased put options for 438,933 ounces at a strike price of \$830/oz (guarantees a minimum gold price for a 34 month period).

After testing the \$3.00/share mark just over two weeks ago, the stock has retreated to \$2.26. A target price of \$2.87 (1.5x NAV) is justified by:

- × Quality management
- × High grades
- × Lack of domestic gold competition

BUY

Avoca Resources Limited

Equities Research

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Recommendation BUY
Current Price \$2.26
Argonaut Target Price (1.5x NAV) \$2.87
All Ords (XAO) 5,587

Sector Metals & Mining
Issued Capital (m) 221.1
Market Cap (m) \$499.6
Date 10-June-2008

Profit & Loss (\$m) 30 June	2009E	2010E	2011E
Sales Revenue	140.5	179.0	175.9
Other Income	0.7	2.6	4.6
Operating Costs	72.2	93.2	94.2
Deprn & Amort	25.8	31.6	22.0
Exploration Written Off	2.0	2.1	2.1
Corporate/Admin	5.0	5.1	5.2
Other	0.0	0.0	0.0
EBIT	36.1	49.6	57.0
Interest Paid	4.5	4.0	3.3
Operating Profit	31.6	45.5	53.7
Tax expense	9.5	13.7	16.1
Minorities	0.0	0.0	0.0
NPAT	22.1	31.9	37.6
Normalised NPAT	22.1	31.9	37.6

Financial Summary	2009E	2010E	2011E
Reported Earnings			
Net Profit (\$m)	22.1	31.9	37.6
EPS (cents)	9.5	13.7	16.2
PER (x)	23.7	16.5	14.0
Normalised Earnings			
Net Profit (\$m)	22.1	31.9	37.6
EPS (cents)	9.5	13.7	16.2
EPS Growth (%)		44.0	18.0
PER (x)	23.7	16.5	14.0
Cashflow			
Operating Cashflow (\$m)	42.6	55.2	51.2
GCFPS (cents)	18.3	23.8	22.1
PCF (x)	12.3	9.5	10.2
Dividend			
Dividend (cents)	0.0	0.0	0.0
Yield (%)	0.0	0.0	0.0
Franking %	100	100	100

Cash Flow (\$m)	2009E	2010E	2011E
Operating Cashflow	42.6	55.2	51.2
- Capex	12.0	6.2	4.2
- Exploration & Evaluation	10.1	10.3	10.5
- Asset purchases (+ asset sales)	0.0	0.0	0.0
Free Cashflow	20.5	38.8	36.5
- Dividends	0.0	0.0	0.0
+ Equity raised	0.0	0.0	0.0
+ Debt drawdown (- repaid)	(10.0)	(10.0)	(10.0)
Net Change in Cash	10.5	28.8	26.5
Cash at End Period	39.6	78.7	115.7

Financial Ratios	2009E	2010E	2011E
Balance Sheet Ratios			
Total Debt / Equity (%)	51	33	21
Interest Cover (x)	8.0	12.3	17.4
Acid test ratio (x)	1.4	2.0	2.7
Profitability Ratios			
Net Profit Margin (%)	15.7	17.8	21.4
Return on Assets (%)	22.0	32.1	39.6
Return on Equity (%)	19.4	21.9	20.5

Balance Sheet (\$m)	2009E	2010E	2011E
Total Assets	203.8	233.4	259.8
Total Debt	58.3	48.3	38.3
Total Liabilities	90.0	87.7	76.5
Shareholders Funds	113.8	145.7	183.3

Valuation Summary	A\$m	A\$/sh
Trident	308.5	1.40
Forwards	0.0	0.00
Corporate	-9.3	-0.04
Non Trident Resources	61.3	0.28
Exploration	100.0	0.45
Unpaid Capital	11.1	0.05
Cash	9.1	0.04
Debt	-58.3	-0.26
Total @ 7% discount rate	422	1.91

Production Summary	2009E	2010E	2011E
Trident (koz)	133	172	172
Total	133	172	172
Gold Cash Cost (US\$/oz)	462	444	429
Gold Total Cost (US\$/oz)	627	594	529
Gold Price Realised (US\$/oz)	900	850	800

Directors	
Robert Reynolds	Non-Executive Chairman
Rohan Williams	Managing Director
Stephanie Unwin	Non-Executive Director
David Quinlivan	Non-Executive Director
Jan Castro	Non-Executive Director

	Reserves			Resources		
	mt	Grade (g/t)	Au (moz)	mt	Grade (g/t)	Au (moz)
Trident	3.4	5.3	0.58	5.0	5.8	0.93
Fairplay				3.6	1.8	0.21
Palaeochannels				1.4	2.0	0.09
Chalice				0.5	5.3	0.08
Other				1.3	1.2	0.05
Total	3.4	5.3	0.58	11.8	3.6	1.36

Substantial Shareholders	%
Pala Investment Holdings	17.8%
Commonwealth Bank	8.7%
JP Morgan Chase and Co	6.2%

