

AVOCA RESOURCES LIMITED

MATERIALS
Analyst: Stephen Gorenstein
 Date: 19 March 2007
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All figures in A\$ unless otherwise advised

Initiating Coverage with BUY – Good Small Cap Gold Play

RECOMMENDATION:	S/Term: OUTPERFORM	L/Term: BUY
Stock Code: AVO	S/T Rationale: -ve Neut +ve	L/T Rationale: -ve Neut +ve
Share Price: \$1.30	Earnings Outlook: ✓	Industry Structure: ✓
Base Valuation: \$0.86	Hist Earnings Revision: ✓	EVA™ Trend: ✓
Upside Valuation: \$1.50	Valuation Support: ✓	Growth Option: ✓
	Price Momentum: ✓	Price / Valuation: ✓
	News Flow: ✓	

KEY POINTS:

AVO is developing the Trident Gold Mine in WA

We estimate:

- **155kozpa**
- **5.5years**
- **Cash cost of A\$401/oz**

Base NPV of \$0.86/share...

Upside (with expansion) of \$1.50

Compared to Peers it looks extremely well priced

While not without risks ... BUY

- Avoca is developing the Trident gold mine in Higginsville WA. While the project has a short mine life, we believe exploration potential exists to significantly lengthen this. The key parameters of the operation are:
 - Total production of 792koz (equivalent to indicated resource) over ~5.5year life. Average annual production of ~155kozpa;
 - total LOM capex of \$116m;
 - average cash costs of A\$401/oz; and
 - first production expected June 2007.
- While the share price is currently trading at a premium to our base case NPV of \$0.86/share, it is trading below our upside NPV (\$1.50) and perhaps more importantly on our analysis is trading at a significant discount to its gold peers on nearly every multiple, once it reaches full production:
 - PE's: FY09: AVO 6.5x vs peer average 12.3x
 - P/FCF: FY09: AVO 4.0x vs peer average 12.0x
 - EV/Cost weighted prod: FY09: AVO: \$482/oz vs peer avg: \$1222/oz
- We believe that once funding for the Trident development is secured the market will turn its attention to AVO's production growth, its relatively low valuation multiples and its strong exploration potential.
- We are initiating coverage of AVO with an OUTPERFORM / BUY recommendation. This represents an override to our tick box template. While it is trading at a premium to its base NPV, we feel exploration potential offsets this. In addition, AVO is trading at a discount to its peers, has rapid production growth and excellent exploration potential.
- Please see full report for a more detailed analysis of the company.

INVESTMENT ARITHMETIC

ASX Code:	AVO	12 month Price Range:	151¢-60¢		
Issued Capital:	150.4m ord.	Market Capitalisation:	\$194m		
% of S&P200 Index:	0.01%	Turnover:	\$13m/month		
Debt/Equity:	-17.8%	Interest Cover:	-7.0 times		
Year End June	2006 Actual	2007 Estimate	2008 Estimate	2009 Estimate	2010 Estimate
Net Profit – Reported (\$m)	-1.6	-2.9	14.9	38.7	43.0
NET PROFIT – Adj¹ (\$m)	-1.6	-2.9	14.9	38.7	43.0
- EPS Adj (¢)	-1.2	-1.8	7.7	19.9	22.2
- EPS Growth (%)	N/A	N/A	N/A	158.4	11.6
- PER (x)	nm	nm	16.9	6.5	5.9
Relative PER (%)	nm	nm	24.4	-50.9	-55.1
Dividend (¢)	0.0	0.0	0.0	10.0	11.1
- Yield (%)	0.0	0.0	0.0	7.7	8.5
- Franking (%)	0	0	0	0	0
FCFPS (¢)	-1.2	2.2	15.2	58.0	61.4
P:FCFPS (x)	nm	59.1	8.6	2.2	2.1
EV/EBITDA	nm	-103.2	7.4	2.8	2.1
BV (\$)	0.18	0.43	0.43	0.53	0.64
P/BV	7.2	3.0	3.0	2.5	2.0
Avg. Fully Diluted Shares (m)	133.0	160.2	194.2	194.2	194.2
Relative Price Performance		1 month	3 months	12 months	
vs. S&P 200:		6.2%	1.6%	70.5%	
vs. MSCI - World (Ex Aust):		9.7%	9.3%	88.4%	

Source: Company data, IRESS, and GSJBW Research estimates. For non Dec. year end stocks, 2004 data is AGAAP based.

⁽¹⁾ Net Profit - Adjusted is after share based compensation and pref dividends, and before goodwill amortisation, NRI's and other non-operating AIFRS adjustments.

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*All figures in A\$ unless otherwise advised***What Is Avoca's Business**

Avoca is currently developing the Trident Gold Mine at its 100% owned Higginsville Gold Project in WA. Higginsville is located 150km south of Kalgoorlie and 55km north of Norseman. Shortly after acquiring Higginsville in 2004, AVO made the significant Trident gold discovery located only 180m north of the Poseidon South open pit (300Koz produced). Trident will be accessed via a decline extending from the existing underground workings at the base of the Poseidon South pit.

The Trident deposit is the 'jewel in the crown' at Higginsville and is due to begin production in mid 2007 with an initial 4 year mine life.

While initial production is to be toll treated by a 3rd party, AVO is planning to build a standalone 1mtpa plant during CY08. Once complete this plant should produce between 160-190kozpa.

We believe it is extremely likely the life will extend well beyond 5.5 years once further drilling is completed. We believe cash flow generated from the operation will be put back into the ground in the form of exploration to help extend the life.

Recommendation ... Our Thinking – BUY

We are initiating coverage on Avoca with an OUTPERFORM / BUY recommendation. The key attractions of the stock are:

- 1) it is developing a gold operation in WA and will soon move from being an explorer to producer;
- 2) once it reaches full production rates, AVO is the most attractive gold stock (in our gold universe) on almost all the main multiples. Some of the key multiples are:
 - **PE's**: FY09: AVO 6.5x vs peer average 12.3x
 - **P/FCF**: FY09: AVO 4.0x vs peer average 12.0x
 - **EV/EBITDA**: FY09: 2.8x vs peer average 8.3x
 - **EV/production oz**: FY09: AVO: \$1270/oz vs peer avg: \$3594/oz
 - **EV/Cost weighted prod. oz**: FY09: AVO: \$482/oz vs peer avg: \$1222/oz;
- 3) the Trident deposit is a typical gold deposit with standard mining and processing technology and hence lower development risk than some other developing operations;
- 4) we see significant exploration potential in the Higginsville area and believe success in this area will lead to a life extension and perhaps expansion.

The **key risks** to our view are:

- a) AVO is trading well above its base case NPV. However we point out this base NPV only encapsulates ~5.5 years of life and we believe exploration success will make this conservative.
- b) AVO still needs to build and commission the Trident gold mine. This is always an element of additional risk – however we note the technology is fairly straightforward and so this risk is somewhat dulled.

On balance – we see this as a BUY.

Timeline

We expect a fairly continuous line of news flow items to help fuel the share price. The key upcoming events for AVO are:

1. Ministerial Approval – Received
2. Commencement of decline – Achieved
3. Exploration results – Ongoing
4. Commencement of ventilation shaft – March 2007
5. Mining development contract awarded – April 2007
6. First gold pour (development ore) – June 2007
7. Re-evaluation of surface resources at current spot prices – 2HCY07
8. Development of standalone plant – during CY07/08
9. First production from plant – early 2008

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Production

Our production profile is shown below. For the most part we see this as a conservative forecast, particularly in relation to the longevity of the mine. We are of the view that further exploration will extend the Trident Gold mine life beyond the current reserve / resource position.

Trident	BASE CASE	>>Forecast						
		2007	2008	2009	2010	2011	2012	2013
Production : mt.		0.08	0.58	1.03	1.15	1.15	1.06	0.00
Grade : g/t		4.26	5.38	5.72	5.33	4.72	4.50	0.00
Recovery : %		95%	96%	96%	96%	96%	96%	96%
Gold Production : oz		10,409	95,152	182,522	189,275	167,286	147,685	0
Cost A\$/t		67.0	63.3	63.0	63.0	63.0	63.0	0.0
Cost A\$/oz (Pre Royalty)		515	383	356	381	432	452	0
Cost A\$/oz (Post Royalty)		536	405	379	406	454	471	0
Capex A\$m		35.9	65.0	4.7	5.0	3.6	3.3	0.0

Source: Company data; GSJBW Research estimates

The key points to take from our production profile are:

- Total production over the life amounts to 792koz (compared to reserves of 581koz and resources of 797koz). This compares to company feasibility study of 581koz. The difference is we have allowed for an additional 18 months of mining to include the recent discovery of Apollo and a small amount of other exploration potential.
- Average annual production of ~155kozpa.
- Life of mine cash costs are A\$401/oz (compared to company guidance of A\$369/oz).
- Life of mine capex is A\$116m (compared to company guidance of \$91-\$103m). We have included capex already spent and sustaining capex post the development of Trident.
- Metallurgical recovery is 96% in line with company guidance.

Upside

We have made our base case valuation achievable. However, this may not fully encapsulate the true potential of the Higginsville area.

The key reasons we feel upside to the area exists are:

- Avoca is still an early stage developer and like many 'similar' companies it has only completed sufficient exploration to complete financing. We expect Avoca will use the cash flow generated to further explore the ground at Higginsville.
- We have focussed our base case valuation on the Trident deposit (797koz resource). However, the Higginsville area has further potential outside the Trident deposit. This includes (but is not limited to):
 - **Recent step-out drilling** – AVO believes it has found a new ore zone in the recently announced Apollo mineralisation. Better intersections include 25m @ 4g/t and 14m @ 4.7g/t. This zone already appears to have a strike length of 350m (longer than the Western zone) and is located only 20m away from the current decline. Should this be moved into resources (and then reserves) as we believe it will it would provide feed for the plant to extend the life of Higginsville.
 - **Near surface resources** – These were deemed uneconomic at A\$450/oz but the current spot gold price is ~A\$800/oz. The table (on page 10 of this article) illustrates that these comprise ~250koz of resource of the Higginsville area.
 - **The Erin ground** which until very recently has been owned and mined by private prospectors. We see this area as very prospective and a possible Trident look-alike.
 - **Further drilling at depth** – In our view the Higginsville area has not yet been appropriately explored at depth. In fact only 1% of all drill holes are to a depth of 250m or more with the average drill hole only 45m deep.
 - **Upgrade to current resource classification** from inferred to indicated (with infill drilling). We also note the very high conversion rate to reserve of 89%.
- We also feel that there is every chance the Athena lodes will produce an overcall on grade given their coarse grade. An overcall on grade is symptomatic of these coarse grade type orebodies. (As an example, the Poseidon South pit (which is only 180m away from Trident) produced a 35% overcall compared to its planned production).

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We have modelled an upside scenario for Higginsville. This assumes:

- extended life at the current 1.0mtpa production rate;
- higher throughput of 1.5mtpa (1.0mtpa in the base case);
- higher annual production of ~195kozpa (~155kozkozpa);
- longer life of ~13 years (~5.5 years). While AVO's stated feasibility study notes a 4 year initial life, the company is building infrastructure for a 10+ year mine life due to its confidence in the exploration potential;
- higher total ounces 2.2Moz (792koz).

Trident (Expanded to 1.5mtpa)	>>Forecast									
	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
Production : mt.	0.1	0.6	1.0	1.1	1.1	1.1	1.1	1.1	1.5	1.5
Grade : g/t	2.13	4.93	5.72	5.37	4.50	4.50	4.50	4.50	4.50	4.50
Recovery : %	95%	96%	96%	96%	90%	90%	90%	90%	90%	90%
Gold Production : oz	10,409	95,152	182,522	189,275	149,213	138,023	138,023	138,023	195,316	195,316
Cost A\$/t	67.0	63.3	63.0	63.0	63.0	63.0	45.0	63.0	50.0	50.0
Cost A\$/oz (Pre Royalty)	515	383	356	381	484	484	346	484	384	384
Cost A\$/oz (Post Royalty)	515	405	379	406	506	502	364	502	402	402
Capex A\$m	35.9	65.0	4.7	5.0	3.6	3.3	2.4	53.3	3.8	3.8

Source: Company data; GSJBW Research estimates

We believe that this scenario is achievable for AVO. However as the current decline can only support a production rate of 1-1.1mtpa, we believe a haulage shaft would need to be sunk in order to increase the throughput rate. We estimate the total capex outlay for this would equate to ~\$50m including upgrading the plant. We expect that a shaft would only be sunk if mineralisation extended below 750-800m which suggests it would not occur before c.2015.

Valuation

Avoca Resources		DISCOUNTED CASH FLOW VALUATION	
Spot Gold Assumption	A\$/oz	736	
Discount Rate Used	%	10.9%	
Issued Shares	millions	211.9	
		A\$m	\$ per share
Mines			
Trident		137	\$0.65
Sub Total Mines		137	\$0.65
Exploration Assets	389	20	\$0.09
NPV of Tax		(40)	(\$0.19)
NPV of Hedge Book		0	\$0.00
Net Cash		48	\$0.22
Corporate		-3	(\$0.02)
Franking Credits		8	\$0.04
Sub Total Corporate/Other		33	\$0.15
Options Dilution		12	\$0.06
NET PRESENT VALUE		181	\$0.86
	Probability		
Trident expanded to 1.5mtpa	100%	74	\$0.35
Regional Exploration		45	\$0.21
Resources not in base mine plan		17	\$0.08
UNRISKED UPSIDE		317	\$1.50

Source: Company data, IRESS, GSJBW Research estimates

The production profiles shown in the sections above drive this valuation. The base production profile forms the basis of the Base Case NPV of \$0.86/share. The upside production profile (Trident expanded) forms the basis of our upside valuation of \$1.50/share.

The clear point that comes out of our valuation is that it appears the current share price is factoring in all of the base case production plus some potential for expansion. We highlight this is not uncommon in the gold market and should not be seen as a definitive sell signal. Gold companies have a tendency to trade well above their NPV's and we do not see this changing in the near term (particularly with our view of a favourable gold outlook).

Instead we believe investors should compare AVO to its peers in terms of a variety of multiples to see whether it is more or less expensive.

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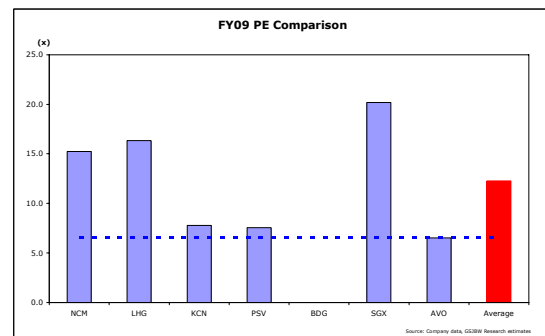
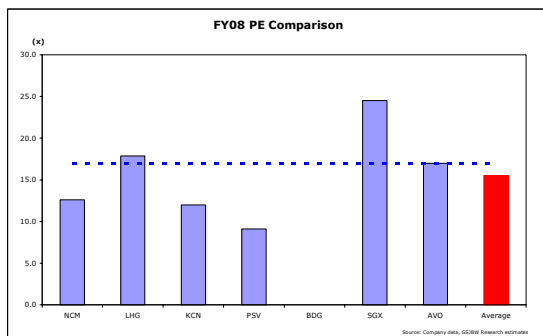
Peers

While on a standalone basis AVO seems fully priced compared to its base case NPV, this is not the case when its gold peers are taken into account.

In fact, once AVO reaches full production rates (FY09), on nearly every multiple it stacks up favourably against the other gold companies. The only obvious exceptions are in terms of EV/ Resource oz and EV / Reserve oz. We note however that in terms of resources and reserves we see considerable scope for AVO to increase its position and so we believe this should be a secondary consideration.

Charting Avoca vs The Sector

PE's

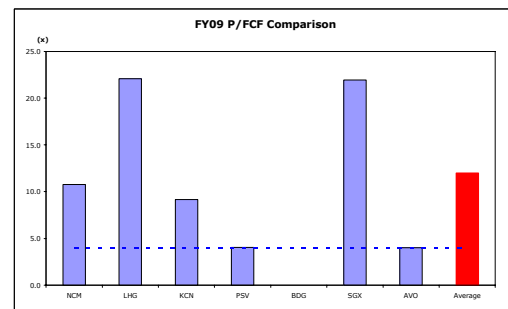
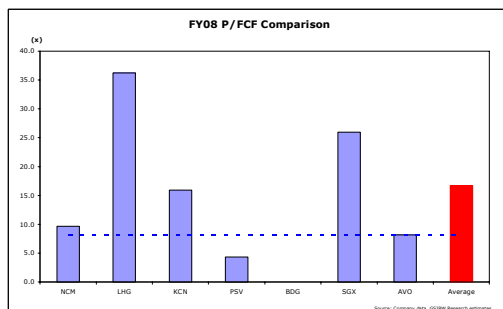


PE (x)	Price	2007	2008	2009	2010
NCM	22.50	37.0	12.6	15.2	15.0
LHG	3.17	24.9	17.8	16.3	14.5
KCN	4.65	n.a.	12.0	7.8	8.1
PSV	0.39	n.a.	9.1	7.6	6.5
BDG	0.30	n.a.	n.a.	n.a.	9.6
SGX	6.52	38.3	24.5	20.2	20.4
AVO	1.30	n.a.	17.0	6.5	5.9
Average		33.4	15.5	12.3	11.4

Source: GSJBW Research estimates

- On FY08 PE AVO is in line with the average of the sector.
- From FY09 AVO is well below the average and in fact stacks up as the least expensive in the sector.
- At a 6.4x forward multiple, AVO is amongst the cheapest stocks in the market.

Price to Free Cash Flow



P/FCF (x)	Price	2007	2008	2009	2010
NCM	22.50	35.6	9.6	10.8	11.0
LHG	3.17	30.3	36.2	22.1	16.4
KCN	4.65	n.a.	15.9	9.2	9.8
PSV	0.39	10.3	4.4	4.0	4.2
BDG	0.30	n.a.	n.a.	n.a.	80.1
SGX	6.52	43.5	26.0	21.9	20.7
AVO	1.30	n.a.	8.2	4.0	3.8
Average		30.0	16.7	12.0	20.9

Source: GSJBW Research estimates

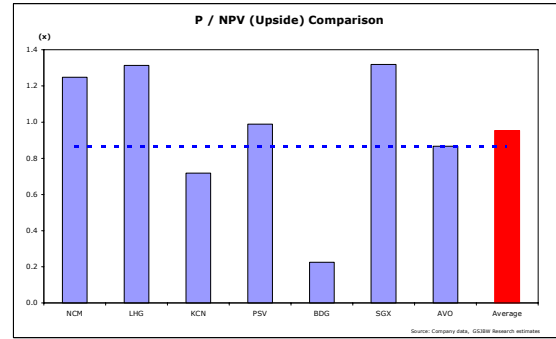
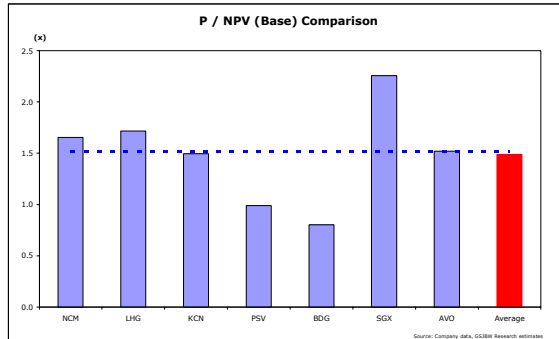
- We define Free Cash Flow as net cash after sustaining capex but pre expansionary capex.
- On this measure AVO is more attractive than its peer group as soon as production starts in FY08.
- From FY09 AVO's ~4x multiple is also low, particularly if it can find more material to extend its life.

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Price to NPV (Base case and Upside)

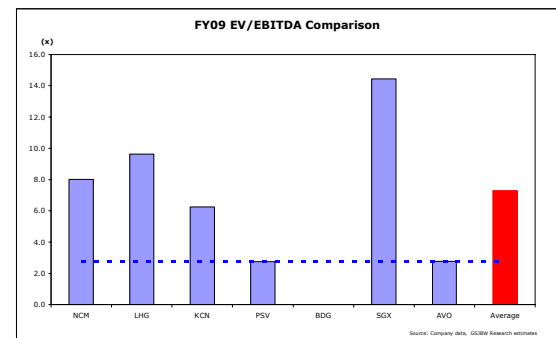
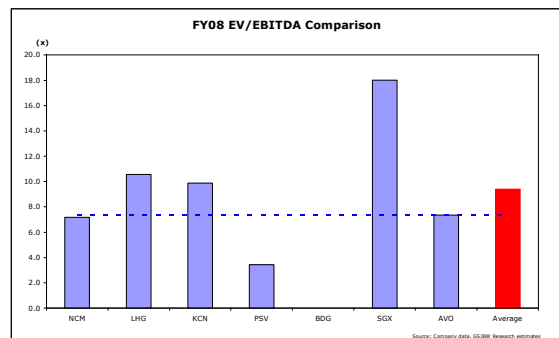


P/NPV (x)	Price	P / Base NPV	P/ Upside NPV
NCM	22.50	1.7	1.2
LHG	3.17	1.7	1.3
KCN	4.65	1.5	0.7
PSV	0.39	1.0	1.0
BDG	0.30	0.8	0.2
SGX	6.52	2.3	1.3
AVO	1.30	1.5	0.9
Average		1.5	1.0

Source: GSJBW Research estimates

- As discussed above AVO is trading at a price between its base case NPV and its Upside NPV.
- In other words, the market is suggesting there is more production than the mere feasibility study suggests. We concur with this view.
- In addition we note, when compared to its PEER group, trading above the base NPV is not uncommon (in fact no company is trading below its base NPV).
- As AVO has fewer company specific issues than many of its peers we believe a premium to NPV is justified.

EV / EBITDA



EV/EBITDA (x)	Price	2007	2008	2009	2010
NCM	22.50	15.6	7.2	8.0	7.7
LHG	3.17	13.8	10.6	9.6	8.6
KCN	4.65	n.a.	9.9	6.3	5.4
PSV	0.39	6.8	3.4	2.8	2.1
BDG	0.30	n.a.	n.a.	n.a.	5.3
SGX	6.52	29.7	18.0	14.4	14.1
AVO	1.30	n.a.	7.4	2.8	2.1
Average		16.5	9.4	7.3	6.5

Source: GSJBW Research estimates

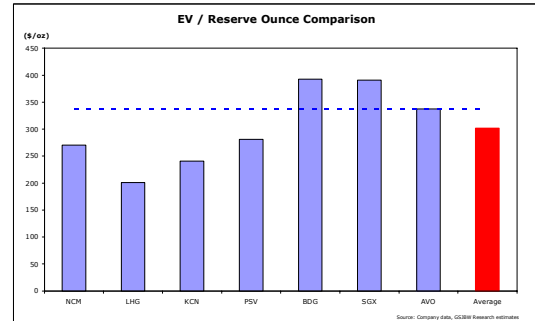
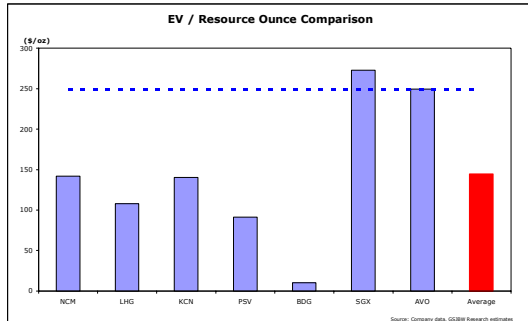
- Like the other earnings / cash flow multiples AVO appears inexpensive on this measure compared to the peer group.
- From FY09 AVO is the least expensive in the sector.

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EV / Resource Ounce and EV / Reserve Ounce

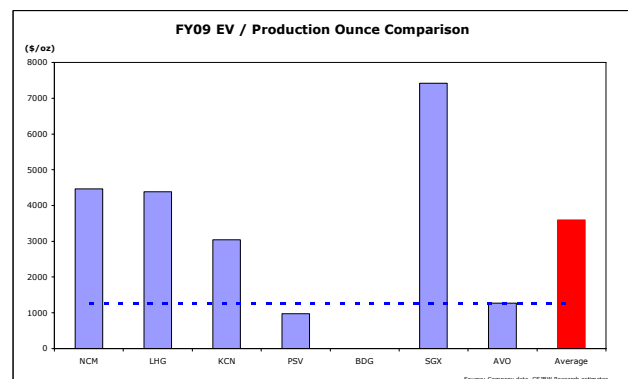
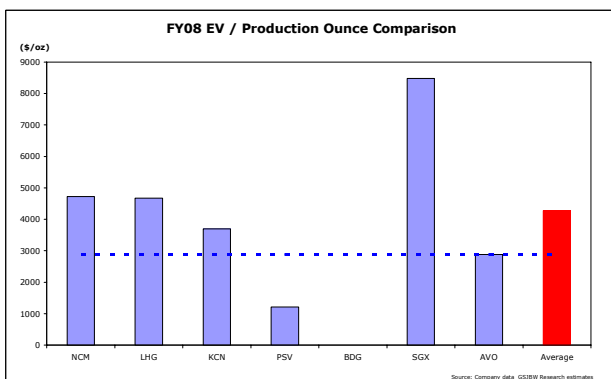


EV/ Reserve/Resource (\$/oz)	Price	EV/ Reserve	EV/ Resource
NCM	0.00	270	142
LHG	22.50	201	108
KCN	3.17	241	140
PSV	4.65	281	91
BDG	0.39	392	10
SGX	0.00	391	273
AVO	6.52	337	249
Average		302	145

Source: GSJBW Research estimates

- On both EV / Resource Oz and EV / Reserve Oz AVO is more expensive than the majority of its peer group.
- We note however, that AVO is at an earlier stage of development than most of the covered sector and hence has not had the opportunity (or cash) to explore its field as well as the others.
- We believe exploration will increase the size of the reserve and resource for AVO.

EV / Production Ounce



EV / Production Oz (\$/oz)	Price	2007	2008	2009	2010
NCM	22.50	5790	4723	4463	4248
LHG	3.17	5216	4673	4389	4192
KCN	4.65	4694	3701	3046	2885
PSV	0.39	1838	1212	977	1058
BDG	0.30	3405	n.a.	n.a.	1326
SGX	6.52	12869	8476	7422	7264
AVO	1.30	18831	2882	1270	996
Average		7521	4278	3594	3138

Source: GSJBW Research estimates

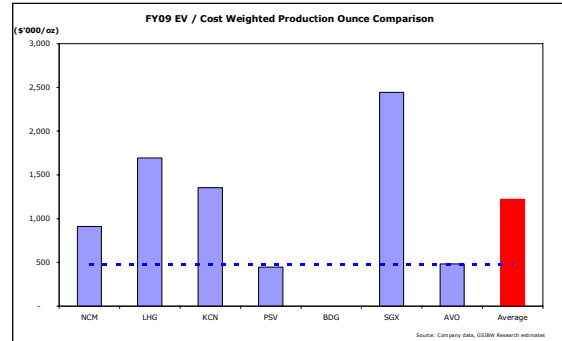
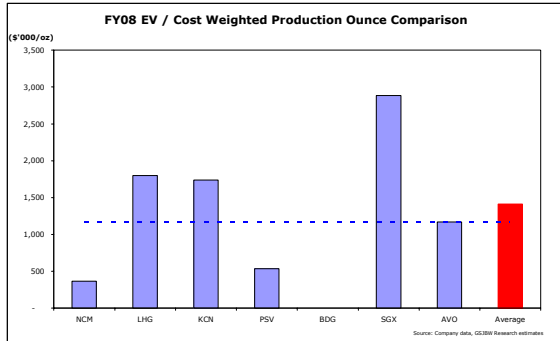
- On this measure AVO (with PSV) is the lowest in the sector.
- On this EV / production ounce measure from FY09, AVO is less than a third of the price of the average sector multiple.

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EV / Cost Weighted Production Ounce*



EV / Cost Weighted Production (\$'000/oz)	Price	2007	2008	2009	2010
NCM	22.50	1,005	365	911	1,121
LHG	3.17	1,863	1,797	1,695	1,631
KCN	4.65	2,567	1,739	1,352	1,321
PSV	0.39	850	532	447	477
BDG	0.30	3,275	n.a.	n.a.	638
SGX	6.52	4,642	2,885	2,444	2,457
AVO	1.30	10,093	1,168	482	405
Average		3,471	1,414	1,222	1,150

Source: GSJBW Research estimates

- * EV/ Cost Weighted Production oz is a GSJBW term based on multiplying the EV / production by the average cash cost of the company. It is used to gauge the relative value (or margin) of each ounce produced rather than just volume against the Enterprise Value of the companies.
- On this measure (like a number of others) AVO ranks 1st in the sector followed by PSV and NCM.

MINING PARAMETERS

Mining Method

The Trident underground gold mine will be accessed and serviced by a 5.2m x 5.5m decline. We understand that the decline can support a production rate of 1.0-1.1mtpa based on 5 trucks in the fleet. The current plan is to extend the decline to ~475m depth.

The mining methods will be a combination of 28 conventional large volume sub-level open stopes (on the Western zone) and a series of narrow (<10m wide) sub-level open stopes (also referred to as bench stoping and occurring predominantly on the Eastern Zone and Athena Lodes). Total development over the period 2007 to 2010 amounts to 26.7km and includes 11.3km of decline development, 1.9km of vertical raises and 13.5km of ore development.

The differences in the stoping methods partly explains why the cut-off grade for the Western zone (2.0g/t) is lower than that of the Eastern and Athena zones (3.0g/t). We estimate the unit costs for the conventional open stoping method to be lower than bench stoping.

Overall, we estimate Mining and Milling costs to be ~\$63/t (including \$5/t administration).

Operating Costs

The company has issued a life of mine cost guidance of A\$369/oz. We have used A\$401/oz over the life of mine in a slightly more conservative approach.

Our break-down of the cost structure is:

Mining:	A\$40/t	
Milling:	A\$18/t	(standalone plant) or A\$22/t (toll treating in year 1)
Administration:	A\$5/t	
Total	A\$63/t	(standalone plant)

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*All figures in A\$ unless otherwise advised***Metallurgy**

Detailed metallurgical studies were carried out to establish gold recovery characteristics. These indicate the Trident ore contains simple free milling gold amenable to processing through a standard CIP/CIL gold processing plant with an installed gravity circuit. Head assaying for gold as well as calculated gold grades showed a degree of variability consistent with ores containing significant proportions of coarse gravity recoverable gold. Importantly, the test work confirmed there are no deleterious elements in the ore.

Gravity recovery produced variable results ranging from 40% - 84%. Leach recovery appears to be excellent and optimum leach residence time is ~36 hours.

Total recoveries for the Eastern zone were calculated at 95.9%, the Western zone at 95.8%, and the Athena Lodes at 97.7%. We have used ~96% recovery in our modelling.

Comminution test work showed the Trident ore has a medium to high Abrasion Index, the rod and ball mill indices are calculated at 18 - 20 kWh/t and the compressive strengths indicate the ore is medium to hard. No excessive consumption of consumables was evident in the test work.

Capital Expenditure

Avoca is building an operation with a view to a >10 year mine life. It has estimated the capex for this to be \$91-103m (GSJBW estimate \$116m). This is broken down into:

• Civil Works	\$1.2m
• Services	\$12.1m
• Building and site infrastructure	\$4.7m
• Underground mining capital equipment	\$17m
• Processing plant capital (dependent on installing their own crusher)	\$33m - \$45m
• Mining capital development costs	\$20.7m
• Other	\$2m
Total:	\$93m-\$101m

We believe this is an achievable target, given it would only cost \$40-50m to mine just the current reserve of 581koz.

Geology

The Trident Gold Deposit is comprised of at least three main mineralised zones: the dominant Western Zone; the Eastern Zone; and the Athena Lodes. The Western and Eastern Zones are sub-parallel, approximately north-south oriented steep east-dipping lode arrays comprising shear-bounded high grade arsenopyrite stockwork veins. The two zones lie 60m apart and exhibit a mineralisation style that is broadly similar to mineralisation seen in the St Ives gold camp. The Athena Lodes are located immediately west of the Western Zone and show a style of mineralisation similar in appearance to the veins of the Norseman gold field; that being a series of gold-galena laminated veins.

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Reserves / Resources

The table below shows the overall resources at Higginsville including the Trident deposit as well as the satellite pits.

Higginsville Resources										
	Cut off Grade	Indicated Resources			Inferred Resources			Total Resources		
		Tonnes (kt)	Grade (g/t)	Ounces (koz)	Tonnes (kt)	Grade (g/t)	Ounces (koz)	Tonnes (kt)	Grade (g/t)	Ounces (koz)
Trident		3,521	5.8	655	838	5.3	142	4,359	5.7	797
Western Zone	2.0	2,298	5.0	370	273	2.8	25	2,571	4.8	395
Eastern Zone	3.0	751	4.9	118	-	-	-	751	4.9	118
Athena	3.0	472	11.0	167	565	6.4	117	1,037	8.5	284
Fairplay Area		1,300	2.0	84	1,149	2.0	75	2,448	2.0	160
Fairplay	1.0	1,006	2.2	71	457	1.7	25	1,463	2.0	96
Fairplay East	0.8	293	1.4	13	211	1.3	9	504	1.4	22
Vine (AVO 64%)	0.8	-	-	-	430	2.8	39	430	2.8	39
Pipeline	0.8	-	-	-	51	1.8	3	51	1.8	3
Palaeochannels		845	2.5	68	48	2.7	4	894	2.5	73
Pluto	1.0	535	2.4	40	14	1.2	1	549	2.3	41
Mitchell 3	1.0	219	2.2	16	13	2.7	1	232	2.3	17
Mitchell 4	1.0	91	4.2	12	21	3.7	2	113	4.1	15
Other		89	2.6	7	352	2.2	24	1,085	1.6	57
Mousehollow	0.8	-	-	-	306	2.2	21	306	2.2	21
Pioneer	0.8	89	2.6	7	-	-	-	89	2.6	7
Eundynie	0.8	-	-	-	46	2.2	3	46	2.2	3
LG Stockpiles	-	-	-	-	-	-	-	644	1.2	25
Total		5,755	4.4	816	2,387	3.2	246	8,786	3.8	1,086

Source: Company data

Leverage to Gold Price

Earnings Sensitivity						
	Year end June	2006a	2007e	2008e	2009e	2010e
Gold Price (+/-US\$10/oz)	A\$m	n.a.	0.1	0.8	1.5	1.4
AUD:USD (+/- 1¢)	A\$m	n.a.	0.1	0.7	1.4	1.4

Source: Company data; GSJBW Research estimates

As Avoca has no hedging (at the moment) it has considerable leverage to the gold price. The table above illustrates the sensitivity of each US\$10/oz change to the gold price and 1¢ change to the AUD:USD exchange rate.

On our earnings forecasts this suggests that for a ~1.5% change to either the gold price or exchange rate there is a ~4% change to earnings.

We believe that if AVO were to undertake some debt to help finance the development of Trident, and hedging was a requirement of this, it should only do this by buying put options to secure the downside without limiting the upside.

Balance Sheet & Requirement to Raise Cash

Balance Sheet		(A\$m)				
	Year end June	2006a	2007e	2008e	2009e	2010e
Cash		7	15	15	61	103
Property, Plant, Equip		1	36	71	42	14
Other Assets		18	20	22	24	26
Debt		0	0	20	20	20
Shareholders Equity		24	69	83	101	119
Net Debt / Equity	(%)	n.a.	n.a.	7%	n.a.	n.a.
Net Debt / (D+E)	(%)	n.a.	n.a.	7%	n.a.	n.a.

Source: Company data; GSJBW Research estimates

We have assumed the financing of the project is done via debt and equity with a 50-50 split. This assumes a \$50m equity raising in the June quarter 2007. We have assumed a \$50m equity raising at a share price of \$1.06 (a 15% discount to the current price of \$1.25). This increases the share base by ~47m shares (~30%).

We have assumed AVO organises a \$50m debt facility to fund the remainder of the project.

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Royalties

We believe at some stage AVO may look to buy back a (relatively onerous) royalty from Morgan Stanley (who acquired it from Gold Fields). Under the royalty, after the first 100koz of gold produced from Higginsville, Morgan Stanley is entitled to 10% of the price received above A\$600/oz for the life of mine.

We estimate this to be worth ~\$32m to AVO on a NPV basis. We believe that AVO would need to raise additional money to acquire this royalty.

Board & Management

Directors

Non-Executive Chairman:	Mr Robert Reynolds
Executive Director:	Mr Rohan Williams
Non-Executive Director:	Ms Stephanie Unwin
Non-Executive Director:	Mr David Quinlivan
Non- Executive Director:	Mr Jan Castro

Management

Managing Director:	Mr Rohan Williams
Geology Manager:	Mr Chris Newman
Exploration Manager:	Mr Geoff Collis
Senior Project Geologist:	Mr Glen Brown

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Avoca Resources Ltd							Recommendation (ST):		OUTPERFORM		
Current Price A\$: \$1.30		Mkt Cap. : \$191m		Free Float 87%			Recommendation (LT):		BUY		
GSJBW DCF: \$0.86		ASX Code: AVO					Analyst:		Stephen Gorenstein		
Industry: GOLD		Turnover (mth) \$13m					Data as at:		19-Mar-07		
Investments Statistics							Profit & Loss (A\$m)				
Year end June 2006a 2007e 2008e 2009e 2010e							Year end June 2006a 2007e 2008e 2009e 2010e				
Net Profit (reported) (A\$m) -1.6 -2.9 14.9 38.7 43.0							Sales Revenue (excl JV & Assoc.) 0 9 86 172 187				
- EPS (Reported) 1 (¢) -1.2 -1.8 7.7 19.9 22.2							Operating costs 2 11 48 89 98				
- PER (Reported) 1 (X) -108.3 -72.5 17.0 6.5 5.9							Operating EBITDA -2 -2 37 84 89				
NET PROFIT (Adj.) 2 (A\$m) -1.6 -2.9 14.9 38.7 43.0							D&A 0 2 15 28 29				
- EPS (Adj.) 2 (¢) -1.2 -1.8 7.7 19.9 22.2							Operating EBIT -2 -3 23 55 60				
- EPS Growth (%) n.a. n.a. n.a. 160% n.a.							JV & Assoc. 0 0 0 0 0				
- PER (Adj.) 2 (X) n.a. n.a. 17 7 6							EBIT -2 -3 23 55 60				
Dividend (¢) 0.0 0.0 0.0 10.0 11.1							Net Interest Exp./(Rev) 0 0 1 0 -2				
- Yield (%) 0.0% 0.0% 0.0% 7.7% 8.5%							PreTax Profit (pre ab's) -2 -4 22 55 61				
- Franking (%) 0 0 0 0 0							Tax Expense (pre abs) 0 -1 7 17 18				
Free Cash Flow (A\$m) -6 -7 31 63 66							Minorities (after Tax) 0 0 0 0 0				
- P/FCF 4 (X) n.a. n.a. 8.2 4.0 3.8							Prof. Dividends 0 0 0 0 0				
EV(Adj.)/EBITDA 3 (X) n.a. n.a. 7.4 2.8 2.1							NET PROFIT (Pre NRI's) 1 -2 -3 15 39 43				
Avg. Shares (diluted) (mill) 133 160 194 194 194							Abnormal Items (after Tax) 0 0 0 0 0				
							Reported NPAT (post ab's) -2 -3 15 39 43				
							Sales Growth (%) 864% 101% 9%				
							Op. EBITDA Growth (%) n.a. n.a. n.a. 124% 7%				
							NPAT (Adj.) Growth (%) n.a. n.a. n.a. 160% 11%				
							EPS (Adj.) Growth (%) n.a. n.a. n.a. 160% n.a.				
							Op. EBITDA Margin (%) -20.3% 43.6% 48.5% 47.6%				
							Interest Cover - EBITDA (X) n.a. -3.8 39.6 n.a. n.a.				
							Return on Equity 5 (%) -6% -4% 18% 38% 35%				
EV Analysis / DCF Valuation							Cash Flow Analysis (A\$m)				
A\$ DCF Valuation: 0.86		Upside DCF: 1.50					Year end June 2006a 2007e 2008e 2009e 2010e				
Price / DCF: 1.52		Ke: 13.7%		WACC: 10.9%							
Kd: 5.3%		RF: 6.5%									
BETA: 1.20		MRP: 6.0%									
Year end June 2006a 2007e 2008e 2009e 2010e							Year end June 2006a 2007e 2008e 2009e 2010e				
EV (Adj.) 3 (A\$m) 165 196 274 232 189							Operating EBITDA -2 -2 37 84 89				
EV (Adj.) / EBITDA (X) n.a. n.a. 7.4 2.8 2.1							change in working cap. 1 2 2 2 2				
EV (Adj.) / Sales (X) n.a. 22.1 3.2 1.3 1.0							Gross Cashflow -2 0 39 86 91				
EV (Adj.) / Gross CF (X) n.a. n.a. 7.0 2.7 2.1							Net Interest Paid 0 0 -1 0 2				
							Tax Paid (inc. abs) 0 0 -3 -15 -19				
							Exploration -5 -7 -4 -4 -4				
							Operating Cash Flow -6 -7 31 66 70				
							Sustaining Capex 0 0 0 -3 -4				
							FREE CASH FLOW -6 -7 31 63 66				
							Dividends Paid 0 0 0 -19 -22				
							Expansion Capex 0 -36 -65 -1 -1				
							Acquisitions 0 0 0 0 0				
							Asset Sales 0 0 0 0 0				
							Dividends Received 0 0 0 0 0				
							Share Issues/Repurchases 12 50 0 0 0				
							Change in Cash 5 7 -34 42 43				
							Gross CF / Op. EBITDA (X) n.a. 0.00 1.05 1.02 1.02				
							Maint. Capex / Sales (%) n.a. 0.0% 0.0% 1.9% 1.9%				
							Total Capex / Sales (%) n.a. 404.2% 76.0% 2.7% 2.7%				
							Maint. Capex / D&A (X) n.a. 0.00 0.00 0.11 0.12				
							Total Capex / D&A (X) n.a. 22.22 4.41 0.17 0.17				
							Maint. Capex / GCF (%) n.a. 0.0% 0.0% 3.8% 4.0%				
Balance Sheet (A\$m)							ROE Analysis				
Year end June 2006a 2007e 2008e 2009e 2010e							Year end June 2006a 2007e 2008e 2009e 2010e				
Cash 7 12 12 55 98							EBIT/Sales (X) n.a. n.a. 0.26 0.32 0.32				
Property, Plant, Equip 1 35 85 61 37							Pretax Profit/EBIT (X) n.a. n.a. 0.96 1.00 1.03				
Other Assets 18 23 25 27 29							NPAT/ Pretax Profit (X) n.a. n.a. 15.76 -5598.70 -28.08				
Debt 0 0 34 34 34							Sales/Assets (X) n.a. n.a. 0.70 1.20 1.14				
Shareholders Equity 24 69 83 103 124							Assets/Equity (X) n.a. n.a. 1.47 1.39 1.32				
Net Debt / Equity (%) n.a. n.a. 26% n.a. n.a.							Return on Equity (ROE) (%) -6% -4% 18% 38% 35%				
Net Debt / (D+E) (%) n.a. n.a. 21% n.a. n.a.											
Annual Production							ROCE WACC Analysis				
Year end June 2006a 2007e 2008e 2009e 2010e							Year end June 2006a 2007e 2008e 2009e 2010e				
Gold 000 oz 0 10 95 183 189							Adjusted NOPAT (A\$m) -2 -3 15 39 43				
							Adj Cap employed (A\$m) 16 36 81 94 71				
							ROCE (%) -9.7% -7.9% 18.4% 41.3% 60.4%				
							WACC (%) 10.9% 10.9% 10.9% 10.9% 10.9%				
							ROCE Spread (abs) -21% -19% 8% 30% 49%				
							Change in ROCE (abs) n.a. 2% 26% 23% 19%				
Cash Costs											
Year end June 2006a 2007e 2008e 2009e 2010e											
Trident (incl. royalty) A\$/oz 0 536 405 379 406											
Commodity Prices											
Year Average to June 2006a 2007e 2008e 2009e 2010e											
Currency A\$/US\$ 0.75 0.77 0.74 0.73 0.72											
Gold Price Spot US\$/oz 527 826 887 943 990											
Gold Price Received A\$/oz n.a. 839 887 943 990											
Earnings Sensitivity											
Year end June 2006a 2007e 2008e 2009e 2010e											
Gold Price (+/-US\$10/oz) A\$m n.a. 0.1 0.8 1.5 1.4											
AUD:USD (+/- 1¢) A\$m n.a. 0.1 0.7 1.4 1.4											
(1) Net Profit - Adjusted is after share based compensation and pref dividends, and before goodwill amortisation, NRI's and other non-operating AIFRS adjustments.											
(2) Net Profit (Adj.) is before goodwill amortisation, NRI's and after Pref. Divs.											
(3) EV Includes 100% of Mkt. Value of minorities											
(4) ROE excludes Preference Capital.											
Source: Company data, IRESS, and GSJBW Research estimates.											

Date: 19 March 2007

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CRF: AU

AVOCA RESOURCES LIMITED

MATERIALS

Analyst: Stephen Gorenstein

Date: 19 March 2007

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Disclosure of Interests:

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RECOMMENDATION DEFINITIONS

Short Term

Underperform (UP) Stock is expected to underperform the S&P/ASX 200 on a 0-6 month timeframe
 Marketperform (MP) Stock is expected to perform in line with the S&P/ASX 200 on a 0-6 month timeframe
 Outperform (OP) Stock is expected to outperform the S&P/ASX 200 on a 0-6 month timeframe

Long Term

Sell (S) Stock is expected to underperform the S&P/ASX 200 for beyond 6 months
 Hold (H) Stock is expected to perform in line with the S&P/ASX 200 for beyond 6 months
 Buy (B) Stock is expected to outperform the S&P/ASX 200 for beyond 6 months

Other Definitions

NR Not rated. The investment rating has been suspended temporarily. Such suspension is in compliance with applicable regulations and/or Goldman Sachs JBWere policies in circumstances when Goldman Sachs JBWere is acting in an advisory capacity in a merger or strategic transaction involving the company and in certain other situations

Research Criteria Definitions

The above recommendations are primarily determined with reference to the recommendation criteria outlined below. Analysts can introduce other factors when determining their recommendation, with any material factors stated in the written research where appropriate. Each criterion is clearly defined for the research team to ensure consistent consideration of the relevant criteria in an appropriate manner.

SHORT TERM (0-6 MONTHS)

Relative Earnings Outlook: Forward looking assessment of risk to consensus EPS estimates relative to estimated EPS risk across the market.
 Earnings Revision: The percentage change in the current consensus EPS estimate for the stock (year 1) over the consensus EPS estimate for the stock 3 months ago. Stocks are rated according to their relative rank, effectively making it a market relative measure.
 News Flow: The consideration of stock specific news flow, market and/or cyclical thematic and other issues such as index changes. Addresses two issues: (1) What is the potential news flow; and (2) What is the share price reflecting?
 Relative Performance: Historic rolling 3 month performance versus the broader market. Stocks are rated according to their relative ranking.
 Valuation Support: Considers a range of valuation methodologies, including discounted cash flow (DCF) valuation, PER, dividend yield and any other relevant measure.

LONG TERM (> 6 MONTHS)

Industry Structure: Based on Goldman Sachs JBWere industry structure ranking. All industries relevant to the Australian equity market are ranked, based on a combination of Porter's Five Forces of industry structure as well as an industry's growth potential, relevant regulatory risk and probable technological risk. A company's specific ranking is based on the proportion of funds employed in particular industry segments, aggregated to determine an overall company rating, adjusted to reflect a view of the quality of a company's management team.
 EVA™ Trend: ¹ EVA™ trend forecast for coming two years. Designed to reflect "turnaround stories" or to highlight companies Goldman Sachs JBWere analysts believe will allocate capital poorly in the estimated timeframe. (An ROE measure is used for insurance stocks in conjunction with an assessment of the strength of an insurer's balance sheet).
 Growth Option: A qualitative and quantitative assessment of a company's long term growth options that the analyst believes should be considered and possibly recognised by the market.
 Price:Base Case DCF: The premium or discount to base case DCF valuation at which the stock is trading relative to the average premium or discount across the market.

¹ EVA™ is a registered trademark of the U.S. consultancy firm Stern Stewart

For Insurers

Return On Equity: Rating taking into account the expected level and trend of ROE over the next two to three years.
 Balance Sheet: Analyst's assessment of the quality and strength of the insurer's balance sheet, including conservatism of provisioning, sufficiency of capital, and quality of capital.

For REITs

EPU Growth: Ranking of Earnings Per Unit growth relative to other listed Real Estate Investment Trusts. Used instead of EVA™ Trend.
 Strategy: Used instead of industry structure as many REIT investors are intra rather than inter sector focussed.
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For NZ Companies

Relevant Index: If a research report is published by the New Zealand affiliate of Goldman Sachs JBWere, the recommendation of a company or trust is based on their performance relative to the NZSX 50 Index (Gross) and not the S&P/ASX 200 index.

Distribution of Recommendations - As at 31 December 2006

Short Term	Overall	Corporate relationship* in last 12 months	Long Term	Overall	Corporate relationship* in last 12 months
Underperform	14%	11%	Sell	3%	3%
Marketperform	61%	63%	Hold	61%	60%
Outperform	25%	26%	Buy	35%	36%

* No direct linkage with overall distribution as the latter relates to the full GSJBW stock coverage (>200 companies). The above table combines the corporate relationships and recommendations of both Goldman Sachs JBWere Pty Ltd and its affiliate in New Zealand, Goldman Sachs JBWere (NZ) Limited.