



## COMPANY UPDATE | COMMENT

JANUARY 27, 2012

## Resource Generation Ltd. (ASX: RES)

### Approvals process continues to drag; Eskom/Transnet agreements moving forward

#### Outperform Speculative Risk

Price:	0.40	Price Target:	0.80
Shares O/S (MM):	257.9	Implied All-In Return:	100%
Dividend:	0.00	Market Cap (MM):	103
NAVPS:	1.58	Yield:	0.0%
BVPS:	0.52	P/NAVPS:	0.3x
		P/BVPS:	0.8x

Major shareholders: Integrated Coal Mining 11.6%  
Priced as at market close on January 27, 2012.

#### Event

Resource Generation reported its December quarterly.

#### Investment Opinion

RES reported little progress with its Boikarabelo development in the Dec-qr. The environmental (NEMA) and water (IWULA) licence approvals remain outstanding, and the Mining Right remains under appeal. An MoU was signed with Transnet in Oct; the formalisation of an agreement should be a key stock driver. An agreement to secure water supply for the Stage 2 expansion was also signed. Cash balances declined to \$21m (\$24m). Maintaining Outperform.

**Approvals dragging:** The timing for the NEMA (environmental) approval for the rail spur remains early 2012 (originally July) as a second EIA is required due to minor variations to the application. RES had targeted receipt of the IWULA water usage licence by year-end; management commented that this has now reached a 'mature stage'; no timeframe was advised. Delays are not unexpected but continue to be disappointing. The Mining Right (granted in the Mar-11 qtr) remains under appeal; however, RES is confident this will be confirmed.

**Transnet MoU signed:** While not a binding rail haulage agreement, the MoU with Transnet is a positive step in the development of Boikarabelo. The other key commercial agreement required is with Eskom for offtake; there was no update in the quarterly, but we continue to believe discussions are progressing well.

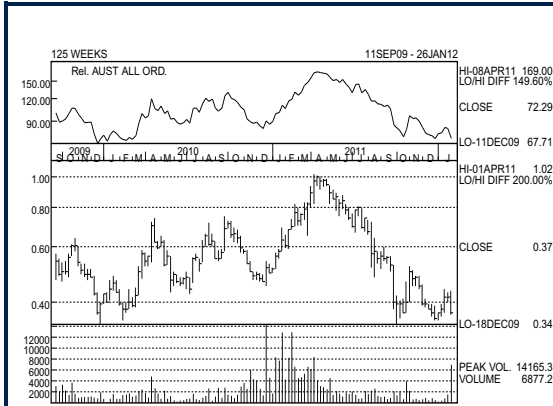
**Funding:** Encouragingly, the company continues to report strong interest from debt funders for the project; however, completion of due diligence requires agreements with Eskom and Transnet.

**Stage 2 water secured:** RES has signed an agreement with the Lephalale Local Municipality to construct, operate, and maintain a wastewater treatment plant at Marapong (~50km from Boikarabelo). This will treat effluent and provide up to 16 megalitres of water per day, which would be sufficient to meet the medium- and long-term needs of Boikarabelo.

**Maintaining Outperform rating and \$0.80 price target:** We continue to see substantial value in the Boikarabelo project. Key drivers of near-term value will be an Eskom offtake and Transnet rail haulage agreement. Our NAV of A\$1.58 incorporates more conservative capex, cost, timing, and price assumptions than management's. Our target of A\$0.80 adjusts our NAV for an equity raising (A\$350m at \$0.75) before applying a 25% risk weighting for development risks.

Priced as of prior trading day's market close, EST (unless otherwise noted).

For Required Non-U.S. Analyst and Conflicts Disclosures, see page 4.



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FY Jun	2011A	2012E	2013E
Adj EPS - Basic	(0.02)	(0.01)	0.00
P/AEPS	NM	NM	NM
Cash Cost	NA	NA	NA
Prod.	0	0	0

All values in AUD unless otherwise noted.



## Valuation

Our NAV for the Stage 1, 6mtpa development is A\$1.55. We model a more conservative development path than management forecasts: we incorporate \$850m capex vs. the targeted \$750m, and we also assume a 12-month delay to startup, with first coal from Q2 2015. In setting our price target, we consider the need for an equity raising. We adjust our base case NAV to incorporate the dilutive effects of a \$350m raising at \$0.75 per share. While this is at a premium to the current share price, we consider that by the time a potential equity raising is required RES will have completed its rail agreements, Eskom offtake, approvals, BFS and debt funding, and as such will be materially de-risked, which would be expected to see the share price trade higher. Furthermore, given the degree of risk that remains with the project in terms of timeline, capex, and development hurdles, we set our price target at a 25% discount to our equity-raising-adjusted NAV. This is a greater-than-usual discount for development projects in our bulk commodities coverage universe, reflecting a view that the market is likely to more heavily discount the project given that it is in South Africa.

## Price Target Impediment

As with all mining companies, world economic growth, commodity prices, and currency fluctuations could materially affect Resource Generation's earnings and valuation. There is also material development risk, with a possibility that the project takes longer and costs more to develop than management estimates. Infrastructure access poses a risk for Resource Generation: without rail-haulage agreements, it will not be able to get its product to market, undermining the project's viability. A sales agreement with Eskom will also be key to underpinning the economic viability of the project, and this is yet to be secured. In addition, the mining rights, water usage, and rail development approval are yet to be granted.

## Company Description

Resource Generation is developing the Boikarabelo thermal coal project in the Waterberg coal fields, 300km north of Johannesburg, South Africa. The resource is substantial at 3bt. Stage 1 targets production of 6mtpa, split between 3mtpa export thermal coal and 3mtpa domestic thermal coal sales. Capital costs are estimated at \$552m and at this stage are unfunded. Operating costs are forecast to be extremely favourable; we estimate an overall average unit cost of approximately US\$33/t, benefiting from 0.6:1 strip ratios. The development is at an advanced stage, with the majority of work done and final approvals anticipated over the next three to six months. Offtake has been arranged for 1.5mt of the export coal, a port allocation is in place, and a domestic sales agreement with Eskom is under negotiation as is a rail-haulage agreement with Transnet. Longer-term, RES envisages a substantial expansion to 18mtpa production.

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An analyst involved in the preparation of this report has visited certain material operations of Resource Generation Ltd..

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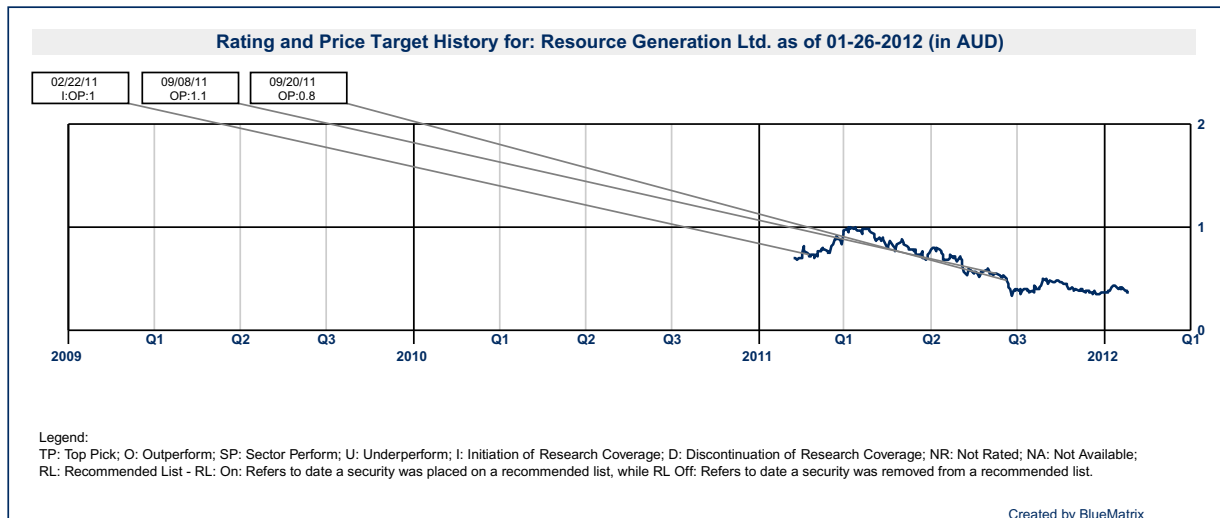
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