

## Equities

25 July 2011 | 8 pages

# Resource Generation (RES.AX)

## NEMA delayed but other permits slowly creeping forward

- NEMA delayed** — the key takeaway from the June Q report is environmental approval for the company's 36km rail link to Transnet mainline, which was due July 2011, will be delayed until later this year. While the consultation process has concluded without major objections, bureaucracy could add "several months" to finalization. We do not think the approval is at risk but are now more cautious with respect to timing, anticipating an award in the Dec Q.
- IWULA expected Sept Q** — more positively, the Integrated Water Use Licence permit is progressing well with approval expected in the Sept Q 2011. We had been more cautious on the IWULA relative to the NEMA but it is now possible that water rights will be awarded before the environmental approval for rail.
- Transnet and Eskom agreements would be transformational** — the real game-changer for RES would be signing of rail and domestic coal offtake agreements. These agreements would significantly de-risk the project and confirm the long-term viability of Boikarabelo. Export off-take for Stage 1 is in place and commences at the end of 2013.
- We increase our capex estimate** — the June Q report noted that final engineering designs were completed in July. Planning for the on-site power plant has not been finalized due to financial failure of the contractor. Given unrelenting pressure on costs, we increase our capex estimate from A\$620m to A\$650m. Cash on hand is A\$25m but we believe the market is anticipating a major capital raising in the current half-year.
- Valuation & Recommendation** — due to higher capex and lower cash balance, our NPV is reduced slightly to A\$1.94. Our target, which is 75% of NPV, is also lower at A\$1.45. Delays in a project of this size and scale are not uncommon and we still believe first coal at the end of 2013 to meet off-take contracts is achievable. We maintain a Buy/Spec rating on RES and believe patience will be rewarded.

- Company Update
- Target Price Change
- Estimate Change

|                              |               |
|------------------------------|---------------|
| <b>Buy/Speculative</b>       | <b>1S</b>     |
| Price (25 Jul 11)            | A\$0.72       |
| Target price                 | A\$1.45       |
|                              | from A\$1.50  |
| Expected share price return  | 101.4%        |
| Expected dividend yield      | 0.0%          |
| <b>Expected total return</b> | <b>101.4%</b> |
| Market Cap                   | A\$189M       |
|                              | US\$205M      |

### Price Performance (RIC: RES.AX, BB: RES AU)



| RES.AU revisions (Y/E Jun) | 2009A  | 2010A | 2011E | 2012E | 2013E  |
|----------------------------|--------|-------|-------|-------|--------|
| Sales (A\$m)               | 0.0    | 0.0   | 0.0   | 0.0   | 0.0    |
| % revision                 | 0.0%   | 0.0%  | na    | na    | na     |
| EBIT (A\$m)                | -15.5  | -4.2  | -4.0  | -6.0  | -4.1   |
| % revision                 | 0.0%   | 0.0%  | 0.0%  | 0.0%  | 0.0%   |
| Core Net Profit (A\$m)     | -15.1  | -3.3  | -3.9  | -5.4  | -19.1  |
| % revision                 | 0.0%   | 0.0%  | 0.0%  | 1.2%  | 0.2%   |
| Core EPS (A¢)              | -19.7  | -2.1  | -1.6  | -2.3  | -8.0   |
| % revision                 | 0.0%   | 0.0%  | 0.0%  | 1.2%  | 0.2%   |
| EPS Growth (%)             | -164.4 | 89.5  | 21.2  | -40.5 | -251.6 |
| PE Ratio (x)               | -3.7   | -35.0 | -44.4 | -31.6 | -9.0   |
| Dividend Yield (%)         | 0.0    | 0.0   | 0.0   | 0.0   | 0.0    |

Source: Company Reports and dataCentral, CIRA.

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See Appendix A-1 for Analyst Certification, Important Disclosures and non-US research analyst disclosures.

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**Resource Generation (RES.AX)**

25 July 2011

| <b>Fiscal year end 30-Jun</b>   |              |              |              |               |               |                               |             |             |              |              |              |
|---------------------------------|--------------|--------------|--------------|---------------|---------------|-------------------------------|-------------|-------------|--------------|--------------|--------------|
| <b>Profit &amp; Loss (A\$m)</b> | 2009         | 2010         | 2011E        | 2012E         | 2013E         | <b>Per share data</b>         | 2009        | 2010        | 2011E        | 2012E        | 2013E        |
| Sales revenue                   | 0.0          | 0.0          | 0            | 0             | 0             | Reported EPS (¢)              | -19.7       | -2.1        | -1.6         | -2.3         | -8.0         |
| Cost of sales                   | -0.1         | -0.1         | na           | na            | na            | Core EPS (¢)                  | -19.7       | -2.1        | -1.6         | -2.3         | -8.0         |
| Gross profit                    | 0.0          | -0.1         | na           | na            | na            | DPS (¢)                       | 0           | 0           | 0            | 0            | 0            |
| <b>EBITDA</b>                   | <b>-15.5</b> | <b>-4.1</b>  | <b>-4.0</b>  | <b>-6.0</b>   | <b>-4.1</b>   | CFPS (¢)                      | -1.5        | -0.1        | -1.6         | -2.8         | 4.6          |
| Depreciation                    | -0.1         | -0.1         | 0            | 0             | 0             | BVPS (¢)                      | 74.2        | 54.3        | 44.2         | 31.8         | 26.8         |
| Amortisation                    | 0            | 0            | 0            | 0             | 0             | Wtd avg ord shares (m)        | 77          | 159         | 239          | 239          | 239          |
| <b>EBIT</b>                     | <b>-15.5</b> | <b>-4.2</b>  | <b>-4.0</b>  | <b>-6.0</b>   | <b>-4.1</b>   | Wtd avg diluted shares (m)    | 77          | 159         | 239          | 239          | 239          |
| Net interest                    | 0.4          | 1.0          | 0.1          | 0.6           | -15.1         |                               |             |             |              |              |              |
| <b>Earnings before tax</b>      | <b>-15.1</b> | <b>-3.3</b>  | <b>-3.9</b>  | <b>-5.4</b>   | <b>-19.1</b>  | <b>Valuation ratios</b>       | <b>2009</b> | <b>2010</b> | <b>2011E</b> | <b>2012E</b> | <b>2013E</b> |
| Tax Recurring                   | 0            | 0            | 0            | 0             | 0             | PE (x)                        | -3.7        | -35.0       | -44.4        | -31.6        | -9.0         |
| Non-op/Except/Extraord          | 0.0          | -0.1         | 0            | 0             | 0             | EV/EBIT (x)                   | -12.0       | -43.4       | -43.2        | -54.4        | nm           |
| Minority interests              | 0            | 0            | 0            | 0             | 0             | EV/EBITDA (x)                 | -12.0       | -44.3       | -43.2        | -54.4        | nm           |
| Associates                      | 0            | 0            | 0            | 0             | 0             | FCF yield (%)                 | -2.8        | -21.2       | -5.6         | -178.3       | -139.0       |
| <b>Reported net profit</b>      | <b>-15.2</b> | <b>-3.4</b>  | <b>-3.9</b>  | <b>-5.4</b>   | <b>-19.1</b>  | Dividend yield (%)            | 0           | 0           | 0            | 0            | 0            |
| Core NPAT                       | -15.1        | -3.3         | -3.9         | -5.4          | -19.1         | Payout ratio (%)              | 0           | 0           | 0            | 0            | 0            |
| <b>Half year data (A\$m)</b>    | <b>1H10</b>  | <b>2H10</b>  | <b>1H11</b>  | <b>2H11E</b>  | <b>1H12E</b>  | <b>Growth rates</b>           | <b>2009</b> | <b>2010</b> | <b>2011E</b> | <b>2012E</b> | <b>2013E</b> |
| Sales revenue                   | 0            | 0            | 0.1          | 0             | 0             | Sales revenue (%)             | -91.2       | 35.0        | nm           | na           | na           |
| EBIT                            | -1.6         | -2.6         | -3.8         | -0.2          | -3.0          | EBIT (%)                      | nm          | 72.7        | 5.1          | -50.4        | 32.6         |
| Core NPAT                       | -1.0         | -2.3         | -3.5         | -0.2          | -2.7          | Core NPAT (%)                 | nm          | 78.3        | -18.1        | -40.5        | nm           |
| Core EPS (¢)                    | -0.6         | -1.4         | -1.5         | -0.1          | -1.1          | Core EPS (%)                  | nm          | 89.5        | 21.2         | -40.5        | nm           |
| <b>Balance Sheet (A\$m)</b>     | <b>2009</b>  | <b>2010</b>  | <b>2011E</b> | <b>2012E</b>  | <b>2013E</b>  | <b>Operating performance</b>  | <b>2009</b> | <b>2010</b> | <b>2011E</b> | <b>2012E</b> | <b>2013E</b> |
| Cash & cash equiv.              | 5.1          | 6.1          | 25.3         | 25.6          | 13.6          | Gross margin (%)              | -245.0      | -240.7      | na           | na           | na           |
| Accounts receivables            | 0.5          | 1.7          | 1.7          | 1.7           | 1.7           | EBIT margin - Group           | na          | na          | na           | na           | na           |
| Inventory                       | 0            | 0            | 0            | 0             | 0             |                               |             |             |              |              |              |
| Net fixed & other tangibles     | 56.2         | 84.4         | 84.4         | 384.4         | 634.4         | Operating ROA (%)             | -27.9       | -4.3        | -3.8         | -2.1         | -3.6         |
| Goodwill & intangibles          | 0            | 0            | 0            | 0             | 0             | Operating ROE (%)             | -29.2       | -4.6        | -4.0         | -6.0         | -27.3        |
| Financial & other assets        | 0            | 0.0          | 0.0          | 0.0           | 0.0           | Operating ROIC (%)            | -30.7       | -6.0        | -4.8         | -2.6         | -0.8         |
| <b>Total assets</b>             | <b>61.8</b>  | <b>92.2</b>  | <b>111.4</b> | <b>411.7</b>  | <b>649.7</b>  |                               |             |             |              |              |              |
| Accounts payable                | 0.6          | 1.6          | 1.6          | 1.6           | 1.6           | Net debt to equity            | -8.9        | -7.0        | -23.9        | 400.1        | 884.0        |
| Short-term debt                 | 0            | 0            | 0            | 0             | 0             | Debt to total capital (%)     | 0.0         | 0.0         | 0.0          | 81.3         | 90.1         |
| Long-term debt                  | 0            | 0            | 0            | 330.0         | 580.0         | Interest coverage (x)         | na          | na          | na           | na           | -0.27        |
| Provisions & other liab         | 4.0          | 4.1          | 4.1          | 4.1           | 4.1           |                               |             |             |              |              |              |
| <b>Total liabilities</b>        | <b>4.6</b>   | <b>5.7</b>   | <b>5.7</b>   | <b>335.7</b>  | <b>585.7</b>  | <b>Production Volumes</b>     | <b>2009</b> | <b>2010</b> | <b>2011E</b> | <b>2012E</b> | <b>2013E</b> |
| Shareholders' equity            | 57.2         | 86.5         | 105.7        | 76.0          | 64.0          | Thermal (export) (mt)         | 0.00        | 0.00        | 0.00         | 0.00         | 0.00         |
| Minority interests              | 0.0          | 0.0          | 0.0          | 0.0           | 0.0           | Hard Coking (export) (mt)     | 0.00        | 0.00        | 0.00         | 0.00         | 0.00         |
| <b>Total equity</b>             | <b>57.2</b>  | <b>86.5</b>  | <b>105.7</b> | <b>76.1</b>   | <b>64.1</b>   |                               |             |             |              |              |              |
| <b>Net debt</b>                 | <b>-5.1</b>  | <b>-6.1</b>  | <b>-25.3</b> | <b>304.4</b>  | <b>566.4</b>  | <b>Operating Metrics</b>      | <b>2009</b> | <b>2010</b> | <b>2011E</b> | <b>2012E</b> | <b>2013E</b> |
| <b>Cashflow (A\$m)</b>          | <b>2009</b>  | <b>2010</b>  | <b>2011E</b> | <b>2012E</b>  | <b>2013E</b>  | Cash Costs (A\$/t)            | 0.00        | 0.00        | 0.00         | 0.00         | 0.00         |
| EBITDA                          | -15.5        | -4.1         | -4.0         | -6.0          | -4.1          | Cash Costs (US\$/t)           | 0.00        | 0.00        | 0.00         | 0.00         | 0.00         |
| Working capital                 | 0            | 0            | 0            | 0             | 0             | Average Price Received        | 0.00        | 0.00        | 0.00         | 0.00         | 0.00         |
| Net interest paid               | 0.4          | 1.0          | 1.0          | -0.6          | 15.1          | Average Price Received        | 0.00        | 0.00        | 0.00         | 0.00         | 0.00         |
| Tax paid                        | 0            | 0            | 0            | 0             | 0             |                               |             |             |              |              |              |
| Other                           | 13.9         | 3.0          | -0.8         | 0             | 0             | <b>Commodity&amp;FX</b>       | <b>2009</b> | <b>2010</b> | <b>2011E</b> | <b>2012E</b> | <b>2013E</b> |
| <b>Operating cashflow</b>       | <b>-1.2</b>  | <b>-0.1</b>  | <b>-3.8</b>  | <b>-6.6</b>   | <b>11.0</b>   | AUDUSD (analyst)              | 0.74        | 0.88        | 0.99         | 1.06         | 1.00         |
| Capex                           | -0.4         | -24.2        | -5.8         | -300.0        | -250.0        | Hard coking (export) (US\$/t) | 260.8       | 146.0       | 247.3        | 295.0        | 260.0        |
| Net acq/disposals               | -2.3         | 0            | -21.0        | -21.0         | -21.0         | Thermal (export) (US\$/t)     | 98.2        | 84.1        | 109.7        | 138.0        | 136.3        |
| Exploration exp/Other           | -3.9         | -4.3         | 0            | -2.0          | -2.0          |                               |             |             |              |              |              |
| <b>Investing cashflow</b>       | <b>-6.6</b>  | <b>-28.5</b> | <b>-26.8</b> | <b>-323.0</b> | <b>-273.0</b> |                               |             |             |              |              |              |
| Dividends paid                  | 0            | 0            | 0            | 0             | 0             |                               |             |             |              |              |              |
| <b>Financing cashflow</b>       | <b>11.4</b>  | <b>29.6</b>  | <b>49.9</b>  | <b>330.0</b>  | <b>250.0</b>  |                               |             |             |              |              |              |
| <b>Net change in cash</b>       | <b>3.8</b>   | <b>1.0</b>   | <b>19.2</b>  | <b>0.4</b>    | <b>-12.0</b>  |                               |             |             |              |              |              |
| <b>FCF ex acqisns &amp;</b>     | <b>-7.8</b>  | <b>-28.6</b> | <b>-30.7</b> | <b>-329.6</b> | <b>-262.0</b> |                               |             |             |              |              |              |

For further data queries on Citi's full coverage universe please contact CIRA Data Services Australia New Zealand at CIRADataServicesAustraliaNZ@citi.com or +61-2-8225-4848



## Resource Generation

### Company description

RES is a 'concept coal' company with assets in the Waterberg region of South Africa. The main development is the Boikarebelo project. It has 3Bt of coal resources and 745Mt of reserves. RES initially plans an open pit producing c6Mtpa of washed coal with a 50:50 split between domestic and export .

### Investment strategy

We rate RES shares as Buy/Speculative. RES is very high risk but potentially a highly rewarding prospect. The company has a huge resource position in the mainly untapped Waterbank coal region of South Africa. Its resource base, build out of domestic South African power capacity and demand for coal from emerging markets such as India is likely to see RES evolve into a 6mtpa coal producer.

### Valuation

Our target price of \$1.45/share is set as a 75% risk weighting to our NPV of \$1.94 per share. Our NPV is based on DCF analysis using a 14.5% discount rate and a US\$105/t long term thermal coal price. We believe a 75% risk weighting to our NPV is appropriate given the early stage of the project as well as the infrastructure barriers that need to be overcome but recognise that progress is being made i.e. award of a mining right.

### Risks

We rate RES as a Speculative risk given the non producing nature of its assets. Key risks to achieving our target price are as follows:

Commodity price: Coal prices have become more volatile over the past 5 years as the historically bulk traded market has moved to a more terminal market approach. At the same time China has been swinging from importers to exporters to importers of coal which has had a significant effect on the supply-demand balance of the seaborne market. Given the big coal resources that China has, there is always the risk that it could increase domestic production and turn again to a net exporter of coal, having a negative influence on the coal price.

Rail: RES's coal assets are located in the Waterberg region of South Africa. The region is not as well serviced by infrastructure as the coal fields of the Witbank are.

Political Risk: South Africa has had a revolution in its minerals industry in the past decade with the implementation of Black Economic Empowerment.

If the impact on the company from any of these factors proves to be greater than we anticipate, the stock will likely have difficulty achieving our target price. However, should they be less than anticipated, the stock could trade above our target price.

## Appendix A-1 Analyst Certification

The research analyst(s) primarily responsible for the preparation and content of this research report are named in bold text in the author block at the front of the product except for those sections where an analyst's name appears in bold alongside content which is attributable to that analyst. Each of these analyst(s) certify, with respect to the section(s) of the report for which they are responsible, that the views expressed therein accurately reflect their personal views about each issuer and security referenced and were prepared in an independent manner, including with respect to Citigroup Global Markets Inc and its affiliates. No part of the research analyst's compensation was, is, or will be, directly or indirectly, related to the specific recommendation(s) or view(s) expressed by that research analyst in this report.

### IMPORTANT DISCLOSURES

#### Resource Generation (RES.AX)

##### Ratings and Target Price History Fundamental Research

Analyst: David Haddad  
Covered since September 22 2010

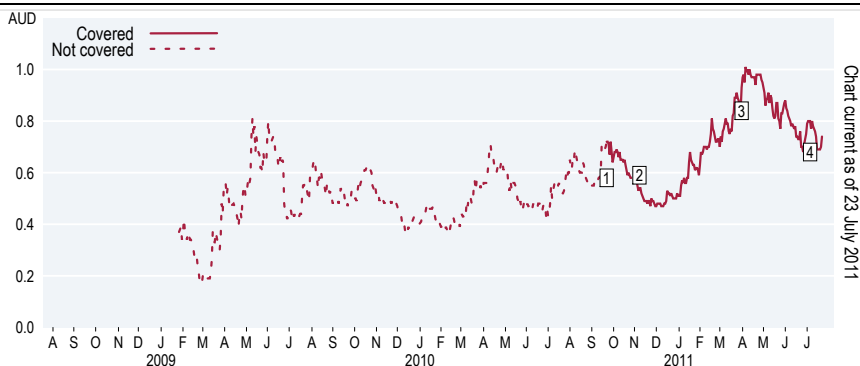


Chart current as of 23 July 2011

|   | Date      | Rating | Target Price | Closing Price |
|---|-----------|--------|--------------|---------------|
| 1 | 22-Sep-10 | *1S    | *1.00        | 0.72          |
| 2 | 8-Nov-10  | 1S     | *0.95        | 0.54          |

|   | Date      | Rating | Target Price | Closing Price |
|---|-----------|--------|--------------|---------------|
| 3 | 31-Mar-11 | 1S     | *1.40        | 0.93          |
| 4 | 6-Jul-11  | 1S     | *1.50        | 0.80          |

\* Indicates change

Rating/target price changes above reflect Eastern Standard Time

#### Resource Generation (RES.AX)

##### Ratings and Target Price History Best Ideas Research Relative Call (3 Month)

Analyst: David Haddad  
Covered since September 22 2010

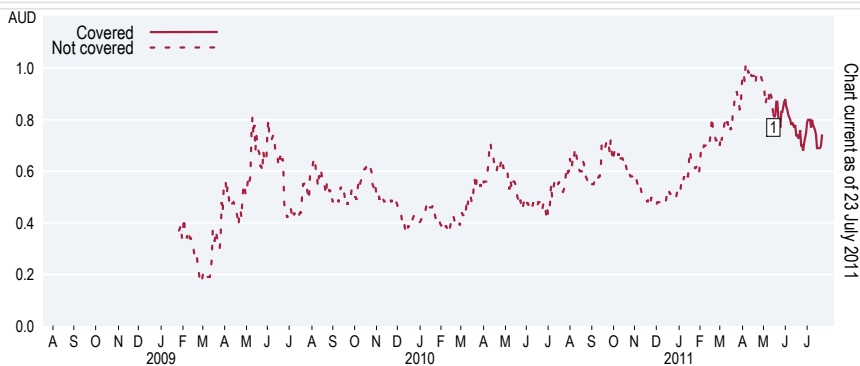


Chart current as of 23 July 2011

|   | Date      | Rating  | Target Price | Closing Price |
|---|-----------|---------|--------------|---------------|
| 1 | 15-May-11 | *ADD MP | -            | 0.85          |

\* Indicates change

Rating/target price changes above reflect Eastern Standard Time

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## Citi Investment Research &amp; Analysis Ratings Distribution

| <i>Data current as of 30 Jun 2011</i>   | 12 Month Rating |      |      | Relative Rating |      |      |
|---|-----------------|------|------|-----------------|------|------|
|   | Buy             | Hold | Sell | Buy             | Hold | Sell |
| Citi Investment Research & Analysis Global Fundamental Coverage                   | 54%             | 36%  | 11%  | 10%             | 81%  | 10%  |
| <i>% of companies in each rating category that are investment banking clients</i> | 45%             | 41%  | 42%  | 50%             | 42%  | 44%  |

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To satisfy regulatory requirements, we correspond Under Review to Hold in our ratings distribution table for our 12-month fundamental rating system. However, we reiterate that we do not consider Under Review to be a recommendation.

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