

Iron Ore Holdings (IOH.ASX, \$1.61/sh, Mkt Cap \$267m) – Deal with Fortescue delivers further cash and de-risks Iron Valley Project.

BUY (PT UNDER REVIEW)

Event:

- Iron Ore Holdings (IOH.ASX) and Fortescue Metals Group Ltd. (FMG.ASX) have signed a binding Memorandum of Understanding (MoU) in respect of IOH's Iron Valley tenements.

Details:

- Fortescue has made a non-refundable \$25m cash payment to obtain a 13 month exclusive option on IOH's Iron Valley tenements.
- If the option is exercised FMG will pay a further cash consideration of \$20m together with 2%-5% royalty based on FOB revenue realised by Fortescue. FMG will pay all costs associated with the development and operations at the Iron Valley tenements.
- FMG also have the right to farm-in to a 50% or greater interest on commercial terms of Maitland River Project should IOH elect to commercialise the magnetite deposit.

Analysis:

- **Fortescue deal on Iron Valley delivers significant shareholder value.** We consider the MoU entered into with FMG to be an excellent outcome for IOH shareholders given significant value will be realised over the life of the asset, whilst eliminating the large level of capital expenditure, dilution and inherent risks of developing a 12-15mtpa iron ore project. Using an assumed royalty of 3.0% (stated range is 2% - 5% dependent upon Fe price), production rate of 12Mtpa commencing in 2015, long term Fe price of \$65/t over a 15 year mine life, cash payments of \$45m (non-refundable \$25m and \$20m upon exercise) derives a NPV¹⁰ of ~\$190m. This equates to an EV/t Fe at Iron Valley of \$1.25/t.
- **Iron Valley deal in line with recent valuation transaction metrics achieved at Central Pilbara.** This is the third deal that management have been able to achieve in a relatively short period of time as part of the Company's ongoing strategy to commercialise the Central Pilbara assets. The previous deals netted >\$70m in cash (plus a 2% royalty on the RIO deal) and were completed at EV/t metrics of \$1.35/t and \$1.16/t respectively with Minerals Resources and RIO.
- **Low risk of FMG not exercising option given \$25m non-refundable deposit and contiguous ore body with 2Bt Nyidinghu deposit:** Iron Valley is contiguous to FMG's Nyidinghu deposit with the mineralisation at Nyidinghu extending into the Iron Valley tenement, providing a logical reason for the projects to be under a single development scenario and mine plan. In our view, FMG could exercise their option well before the 13 month expiry period given the ability to potentially start early production via a low cost trucking operation exploiting the mineralisation at Iron Valley starting at surface and gently dipping towards the FMG tenement boundary, with

approximately 40Mt sitting above the water table and therefore short lead time to production. We estimate 2-3yrs of ore to be available for trucking whilst infrastructure and water management strategies are put in place. We are also confident that FMG have completed extensive due diligence on the synergies and benefits of developing Iron Valley prior to committing a substantial non refundable payment of \$25m.

- **Focus now on Western Pilbara:** With the deal for Iron Valley in progress we expect management to now turn their full attention to commercialising the West Pilbara assets, namely the Bungaroo South Project. Bungaroo South (242Mt) holds strategic value to existing producers/developers with infrastructure capacity coming online in the West Pilbara and/or offshore groups seeking a cheap entry point for a large-scale hematite project that can provide long-term supply. The latest deal will increase the cash balance to ~\$140m (including final tranche payment from Mineral Resources), providing ample cash to fast-track feasibility studies at Bungaroo South and resource definition at the recently discovered large scale magnetite deposit (Dempster).

Recommendation:

- **We reiterate our BUY recommendation with our price target UNDER REVIEW.**
- IOH's market cap is ~\$270m, cash is ~\$140m and the Iron Valley royalty NPV is worth ~\$190m. If we were to apply an EV/t metric of \$1.30/t (in line with recent transactions) at the flagship project at Bungaroo South we would generate an asset valuation of close to ~\$180m, totalling >\$500m which is >\$3/sh and doesn't include any value for the earlier stage assets such as Maitland River and Dempster.
- **We are marketing with MD Alwyn Vorster through Melbourne and Sydney later this month.**

Best regards,
Martin

Martin Carolan
Equity Research Sales



Foster Stockbroking Pty Ltd
D: +61 2 9993 8168 | M: +61 404 809019 | F: +61 2 9221 1031 | E: martin.carolan@fostock.com.au
Level 21, 25 Bligh St SYDNEY NSW 2000
www.fostock.com.au

Disclaimer & Disclosure of Interests. Foster Stockbroking Pty Limited has prepared this report. This document contains general securities advice only. In preparing the report, Foster Stockbroking did not take into account the specific investment objectives, financial situation or particular needs of any specific recipient. The report is published only for informational purposes and is not to be construed as a solicitation or an offer to buy or sell any securities or related financial instruments. Foster Stockbroking is not aware that a recipient intends to rely on this report and is not aware of the manner in which it will be used by the recipient. Investors must obtain personal financial advice from their investment advisor to determine whether the information contained in this report is appropriate to the investor's financial circumstances. Recipients should not regard the report as a substitute for the exercise of their own judgment.

The views expressed in this report are that of the analyst named on the cover page, and no part of compensation of the analyst is directly related to inclusion of specific recommendations or views in this report. The analyst receives compensation partly based on Foster Stockbroking revenues, including any investment banking and proprietary trading revenues, as well as performance measures such as accuracy and efficacy of both recommendations and research reports.

Foster Stockbroking believes that the information contained in this document is correct and that any estimates, opinions, conclusions or recommendations are reasonably held or made at the time of its compilation in an honest and fair manner that is not compromised. However, no representation or warranty is made as to the accuracy, completeness or reliability of any estimates, opinions, conclusions or recommendations (which may change without notice) or other information contained in this document and, to the maximum extent permitted by law, Foster Stockbroking disclaims all liability and responsibility for any direct or indirect loss or damage which may be suffered by any recipient through relying on anything contained in or omitted from this document. Foster Stockbroking is under no obligation to update or keep current the information contained herein and has no obligation to tell you when opinions or information in this report change. Foster Stockbroking, and its directors, officers and employees or clients may have or had interests in the securities of the instruments referred to herein, and may make purchases or sales in them as principal or agent at any time and may affect transactions which may not be consistent with the opinion set out in this report. Foster Stockbroking and its Associates state that they may earn brokerage, fees or other benefits from securities referred to in this report. Furthermore, Foster Stockbroking may have or have had a relationship with or may provide or has provided investment banking, capital markets and/or other financial services to the relevant company.

Specific disclosure: The analyst, Foster Stockbroking and/or associated parties have beneficial ownership or other interests in securities issued by IOH at the time of this report. Diligent care has been taken by the analyst to maintain an honest and fair objectivity in writing the report and making the recommendation.

Specific disclosure: Foster Stockbroking and/or associated parties have received fees in the past 12 months for services provided to IOH in respect of the May 2011 equity capital raising.