

Iron Ore Holdings

Iron Ore – Speculative Risk

Recommendation	Buy
Last Price	A\$1.55
Target Price	A\$2.22
Forecast Total Return	43%

Company profile

Iron Ore Holdings (IOH), established in 2003, is focused on exploring and developing tenements within the Central and Western Pilbara area, targeting direct shipping ore (DSO).

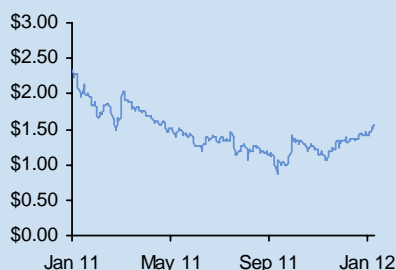
As at Nov'11 the total JORC mineral resource of all IOH projects equated to 934mt, with 450mt located within a 50km radius of existing rail infrastructure.

The key Central Pilbara assets contains multiple deposits; Iron Valley, Lambs Creek and Koodaideri South, over ~570 km² of tenure located adjacent to RIO's Yandicoogina and BHP's Yandi iron ore mines and now FMG's Nyidinghu +2.0bt discovery.

The Western Pilbara project area contains two tenements: Maitland River and Buckland Hills, which is adjacent to the Robe River's Mesa J mine.

All IOH projects are strategically located within close proximity to established rail and currently producing mines, in particular Rio Tinto operations. IOH has no port or rail access.

Share price performance



	1m	3m	12m
Price	17%	17%	(33%)

Source: Iress

Other Information

Iress / Bloomberg	IOH/ IOH AU
Market cap	A\$255m
Enterprise value	A\$213m
Average daily volume (000s)	0.2m
Free float	33.06%
Number of shares in issue (m)	164.6m
Reporting currency	AUD
Quote currency	AUD
Website	www.ironoreholdings.com
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	Source: Iress, Capital IQ

Two assets sold, now for Iron Valley

The early stage of development makes valuation difficult and no earnings are forecast before 2015 at the earliest. Our recommendation is viewed as speculative with the stock suitable only for investors with significant risk tolerance.

We rate IOH as a Buy with a target price of A\$2.22/share, in line with our heavily risked NPV which is indicative of corporate upside potential should Kerry Stokes be a seller of his 50.3% controlling interest or the two main assets.

- Recent news flow:** IOH has increased the resource base to over 900mt over the last two years, including a discovery at Buckland Hills in the West Pilbara (now 263mt at 57% Fe) and including 310mt of magnetite at Maitland River. It has signed a native title agreement with the Nyiyaparti Group covering Iron Valley. In Apr'11 it raised A\$40m for project studies on Iron Valley and Buckland Hills-Bungaroo South (A\$20m) and exploration (A\$14m). The Iron Valley PFS confirmed the technical viability of a staged development of up to 15mtpa at 58.6% Fe for 12 years. IOH has been successful in selling Koodaideri South to Rio Tinto for A\$32m (in line with our in situ value of A\$0.31/t). IOH also received a 2% FOB royalty, which we accord minimal value as RIO is likely to have purchased the tenements for infrastructure space rather than any plans of early development. The key remaining satellite deposits of Phil's Creek and Lamb Creek were sold on 13th Oct for A\$42m, or A\$0.76 per resource tonne to Mineral Resources with payment due in the MarQ'12.
- Key issues:** The timing and the certainty of development remain key issues. The value of the deposits is contingent on trucking, rail and port access. IOH is unlikely to be a developer and there is no clear path to an early cash flow. Iron Valley is high in phosphorous (0.19% versus Pilbara blend 0.09%) and Buckland Hills moderately high (0.15%) which may limit suitors to those with low phosphorous ore looking for a blended product to boost tonnage. Limited market liquidity is also a problem.
- Valuation & Target:** We value IOH at A\$2.22/share (previously A\$2.27/share) NPV based, using an 8% real discount rate and a long-term (2016E) iron ore price of US\$70/t FOB, fines. Our NPV and target price have been risked by an average of 59% to account for the early stage of the developments and the need for funding. At a long-run iron ore price of US\$100/t, our risked valuation increases to A\$4.60/share highlighting the upside for those companies with access to infrastructure and a more bullish view on the long term iron ore price.
- Catalysts:** Any increase in resources is unlikely to be accorded value by the market when IOH has no rail or port access. Upside may be demonstrated by JV deals on Iron Valley and Buckland Hills with parties that do have port or rail access: Wah Nam, Fortescue, Aquila or Atlas - all possibilities.

Iron Ore Holdings: Project Locations



Phil's Creek – Sold
Lamb Creek – Sold
Koodaideri South – Sold

Source: Company reports

Iron Ore Holdings

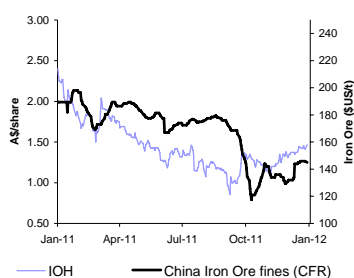
Risks to valuation, recommendation & target price

- Iron ore prices are largely contingent on strong demand being maintained from China
- IOH value depends on third party access to port and rail infrastructure
- High phosphorous nature of the ore adds to valuation uncertainty
- Competing bids required to achieve an optimal valuation for the Company
- Threat of increasing Government tax take, including higher State royalties

Board members

Hon. Richard Court AC, Non-Executive Chairman
 Alwyn Vorster, Chief Executive Officer
 Malcolm Randall, Non-Executive Director
 Ryan Stokes, Non-Executive Director
 Brian O'Donnell, Non-Executive Director

IOH vs China Iron Ore fines



Source: Iress, Metal Bulletin

Strategically located projects – close proximity to infrastructure and the majors

- Iron Valley Project (100% Owned):** The project is located within close proximity to the RIO and BHP Yandi mines, arguably the most profitable mines for each of the majors. It also runs into FMG's new Nyidinghu deposit to the north east. Currently, the JORC resource totals 259mt (indicated and inferred) at average grades of ~58.3% Fe, 5.4% SiO₂, 3.3% Al₂O₃, 0.17% P and 6.9% LOI. The resource includes a high grade component of 143mt at 60.8% Fe. Iron Valley is a low stripping ratio project, largely drilled out, with future work to concentrate on in-fill drilling and Mining and Environmental studies. We value Iron Valley at A\$172m (after risking to 40%) assuming a 7-8mtpa operation beginning mid 2015 and a low capital cost of A\$375m on the assumption of sales at the mine gate. Wah Nam or FMG are likely bidders.
- Buckland Hills Project (100% Owned):** The project is located 35km to the SE of RIO's Mesa J operations and established infrastructure. RIO's Robe River railway was declared by the Australian Competition Tribunal as open to other users until 2018E although this has since been overruled on appeal. Inferred JORC resource: 263mt at 57.2% Fe, 7.0% SiO₂, 2.4% Al₂O₃, 0.15% P and 8.1% LOI. We have applied a value of A\$0.54/t or ~A\$142m. The mine Concept Study envisages a 15mtpa operation over a life of 15 years with a low stripping ratio of 1.2:1 underpinning low operating costs. Aquila is the most likely partner in any JV.
- Central Satellite Deposits (Koodaideri South et al, 100% Owned):** The sale of Koodaideri South for A\$32m to Rio Tinto has been followed by the conditional sale of Phil's Creek and Lamb Creek for ~A\$42m to Mineral Resources with the funds to be directed to progressing the two priority targets, Iron Valley and Buckland Hills.

Stress test in volatile markets

- Assuming iron ore prices decline 15% below our current assumptions through 2016E with no change to our FX, our risked NPV would decline 9% from A\$2.22/share to A\$2.02/share.

Potential suitors

- Fortescue Metals:** Iron Valley dips into FMG's new discovery, Nyidinghu, to the north east and is therefore expected to be of interest as FMG seeks to maximise the utilisation of its rail, port and blending capacity. Iron Valley may act as a good means of access into the larger, but deeper Nyidinghu discovery.
- Other suitors:** As expected, Rio Tinto has already emerged to purchase Koodaideri South. Attracting other suitors depends on whether the incoming party has access to rail and or port. BHP may be tempted in order to keep competitors out of Port Hedland and to consolidate tenements alongside its Yandi mine. Brockman (Wah Nam) and Atlas have potential port access and both are keen to establish rail access: Iron Valley provides meaningful tonnes and blending opportunities. We believe Aquila Resources (AQA) would be unlikely to take over the Company, but is a natural JV partner or buyer of Buckland Hills, as its tenements intersect the mid portion of the deposit.

Strengths

- The Company's projects are located within close proximity to existing rail infrastructure and major existing mines
- New CEO with considerable experience in infrastructure development, marketing and finance. New Chairman with renewed focus
- IOH has relatively high tonnages (500mt) of moderately high grade ore (58%Fe)
- 50.5% owned by Kerry Stokes, strong WA operating base

Weaknesses

- Buckland Hills and Iron Valley have high P impurity levels (0.15-0.18%P versus Pilbara benchmark of 0.09% P)
- IOH has no rights to rail access and no port access.
- Limited ability to force a revaluation unless there is a means of accessing infrastructure

Opportunities

- All tenements are potential JV targets given their close proximity to the major iron ore producers and strategic positioning to rail infrastructure
- Success achieved on asset sales and royalty agreements to monetize stranded assets (in particular the Central Satellite deposits)
- Catalyst for new independent rail option and port access (for instance Korean interests, or China Railway Materials, Wah Nam or Atlas Iron)

Threats

- Assets remain stranded and potential asset value unable to be realized
- Degree of Government tax take, State royalties and carbon taxes
- Now unlikely to secure capacity on the Robe River rail line for the Buckland Hills project

Iron Ore Holdings**Disclaimer**

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	All countries excl South Africa	South Africa
Expected total return		
Buy	> 10%	> 20%
Hold	-10% to 10%	10% to 20%
Sell	< -10%	< 10%

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