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*The Mining Investment Experts*

# Company Update

28<sup>th</sup> March, 2006

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## Compass Resources NL (“CMR”) *“Running on Uranium as Well as Base Metals”*

When we last wrote up CMR the shares were 30¢. We opined that it was a conservative and reliable company and that the shares were cheap. Since then the uranium card has been played and the shares have excelled to \$2.25 today. It has been a company in the right place at the right time.

### Rum Jungle Was a High Grade Uranium Mine

It is an oft quoted maxim that the best place to look for an orebody is where there was previously a mine. This is exactly the position with Rum Jungle, where historical mining of produced approximately 4,500 tonnes of U<sub>3</sub>O<sub>8</sub> at grades of 0.27-0.36% - very high compared with calcrete and roll-front styles in WA and SA. The mineralisation can be classified as an unconformity style in Proterozoic rocks with similarities to other high grade deposits in the Northern Territory. The uranium is peripheral to the base metal deposits.

### Significant Lower Grade Resources Remain

CMR is unwilling to be drawn on tonnes or grades at this point, even though there are records of about 500 holes that were drilled in the 1950s and 1960s, and the reliability of the data has been confirmed. It would be reasonable to expect that grades will be lower at perhaps 0.1% U<sub>3</sub>O<sub>8</sub> as it will be the material left behind from the first operational phase of the mine. It is not unusual to see intercepts averaging up to 40m at 0.045% U<sub>3</sub>O<sub>8</sub> with higher grade spikes e.g. 12m at 0.15% U<sub>3</sub>O<sub>8</sub>.

The Company will embark upon a \$2-3m drilling program in May, on both the uranium and base metals projects. At the completion of this it may be in a position to quote resources.

Only an open pit operation is being contemplated at present. The old mining widths were historically about 10m, but CMR could be looking at bulk mining of widths up to 50m in a new operation.

Exploration potential for new resources is considered good given the advancement in exploration techniques. There is always the chance that CMR might find another 0.2-0.3% U<sub>3</sub>O<sub>8</sub> orebody, particularly at depth.

### Project Size?

One broker is suggesting a fast track 1,800 tpa U<sub>3</sub>O<sub>8</sub> mine with incremental capital expenditure of only \$5m, as it can use infrastructure common to the base metals project. We believe this is way too optimistic on all counts; timing, capacity and uranium production. It implies a 2 mill. tpa treatment plant (if

the grade estimate of 0.1% U<sub>3</sub>O<sub>8</sub> is accurate). It does not take into account the high environmental compliance capital that will be required. Thus this would have to be seen as an optimistic scenario.

By way of comparison Summit Resources is looking at spending in excess of \$200m for a 2.5 mtpa operation in Queensland. Maybe a \$50m price tag for CMR would still be considered cheap by Summit's standards.

### No State Labor Party Politics

The Northern Territory is the best place to have a uranium orebody as there is no disapproving State government to deal with, such as in Queensland or WA. CMR is in the fortunate position that up to 70% of the known mineralisation is on freehold land and development is not subject to Northern Land Council approval. There is no getting around the strict environmental permitting process though, with very high standards being set by ERA. Fast tracking a project is not something that the Greens are capable of accepting.

### The Oxide Base Metals Project Approaching

CMR is pushing ahead with the development of the Browns Oxide Project, expecting to commission it late 2006 or early 2007. As yet the finance has not been finalised but the Company has had so many approaches from financiers and consumers that it has no concerns on the funding front. There was a \$15m share issue at \$1.25 a share last December, and the Company currently has a cash balance of \$14m.

The 1 mtpa project is expected to produce 10,000 tpa of copper, 1,000 tpa of cobalt and 750 tpa of nickel for a minimum of six years, and maybe even 10 years. Payment terms will probably be about 70% of the contained metal. The capital expenditure estimate has lifted from \$40m back in December of 2004, to \$50m today, with judicious use of second hand equipment e.g. the EW section of the Cause nickel plant.

We previously estimated operating costs of \$25 pt, assisted by low cost free-digging ore, but it would be reasonable to lift this to \$30 pt as a result of energy prices and industry costs.

### Favourable Profit Margins

Back in 2004, when CMR ran the numbers on copper prices of US\$1.10/lb, cobalt prices of US\$12.50/lb and nickel at US\$5.50/lb they showed a cash margin of \$50m p.a. We calculated a prospective PE ratio of 1x on the 30¢ share price. Since then the copper price has been trading at well over US\$2.00/lb. The earnings power is significantly greater. One broker has estimated a pre-tax NPV of \$259m or \$3.30 per share. Though we can't

comment on the accuracy of this, the point is that at least one broking house thinks the shares are worth much more than the current share price.

#### Sulphide Project The Second Leg

As we said previously;

*“Beneath the oxide zone is an 82 mt resource at 0.75% Cu, 2.28% Pb, 0.12% Co and 0.11% Ni. There is the potential for a large scale, \$270m development that could operate for 18 years and more at mill feed grades of 6.2% Pb, 0.7% Cu, 0.18% Co and 0.11% Ni. However, this should be seen as a separate project that needs to stand on its own merits.”*

The higher market capitalisation of the Company, the ability to raise funds more easily and the high metal prices have given CMR the incentive to advance this project more aggressively.

CMR has announced it is looking at a 2 mtpa operation that could commence production in 2009, producing 78,000 tpa of lead, 18,000 tpa of copper, 3,150 tpa of cobalt and 2,250 tpa of nickel.

At current metals prices CMR has calculated a NPV of \$975m and an IRR of 50%. Accepting metal prices at lower, long terms estimates still leads to a NPV of \$700m. Thus it is a serious project.

#### The Bottom Line

Compass is a company which we continue to feel comfortable about, notwithstanding the hype of the uranium market. It would be reasonable to expect some sort of uranium mining operation can be

established, but production would be some years away.

In the meantime it has a solid base metals project that will be coming on-stream at a time of record metal prices. Sensible control of capital costs will ensure that financial risk is minimised.

We believe that CMR will be a topical stock for the foreseeable future and the share price is starting to reflect the entry of sizeable institutional buyers. When this process starts it generates a whole new growth profile for the share price. The market capitalisation of \$167m is much greater than the \$16m tag when we wrote it up last, 16 months ago, but this should not be an impediment to even higher prices.

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