

Panoramic Resources Limited

June Quarterly – Cost Pressures, But Partly One-Off



Wilson HTM
INVESTMENT GROUP

3 August 2008

\$2.25

BUY

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Recommendation

We are retaining our BUY recommendation on PAN. While input costs such as labour, materials, and fuel have all increased sharply, the June quarter cost performance was impacted by poor equipment availability that amongst other things necessitated the employment of a contract miner at Savannah until at this stage September. Certain events and costs in the June quarter should not be a permanent feature of the cost structure and FY2009 will see scale benefits flow to the Lanfranchi operation. We have downgraded our forecasts and now forecast FY2009 NPAT of \$102m (vs. \$117m). Our target price is \$3.80/share (previously \$4.03).

Key Points

- June quarter production was a total of 4.0kt contained nickel for 14.9kt for the year (100% basis). Equity production was 13.1kt. The Savannah mine produced 1.8kt contained nickel in the quarter (7.6kt FY2008), while the Lanfranchi mine produced 2.1kt in the quarter (7.3kt FY2008).
- At the Savannah mine, upward cost pressures were evident, with the payable cash cost increasing from A\$4.84/lb in the March quarter to A\$7.06/lb in the June quarter (+46%). However, this measure exaggerates the increase in costs at the mine level, with the mine gate cost increasing by A\$1.10/lb to A\$5.03/lb (+28%). In turn this measure is further exaggerated by the 8.2% lower level of nickel production and the fixed nature of much of the cost base. In addition, the June quarter and hence June half was impacted by the need to hire McMahon to undertake additional underground development due to poor equipment availability. McMahon has been engaged for six months from 1st April.
- Our reconciliation suggests that for the Savannah mine, total mining costs increased 24%, plant costs 7% and admin costs 15% June vs Dec half, with key volumes (tonnes mined, contained metal produced) comparable. Key inputs such as consumables, steel, fuel and labour related costs all increased.
- At the Lanfranchi mine, upward cost pressures were also evident, although without the need to hire outside mining services, the payable cash cost increased by a lesser (compared with Savannah mine) 14% June vs March quarter, despite 9.2% lower production. However, poor equipment availability also negatively impacted. Viewed half year versus half year, the unit mine gate and C1 cash costs decreased by 15% and 14% respectively and the payable cash in the June quarter was lower than both the Sep and Dec quarters. Importantly, this overall shift to a lower unit cost structure, notwithstanding the June performance, reflects the beneficial impact of the expanding scale of the Lanfranchi mine (2.7kt contained nickel Dec half from 115kt ore versus 4.6kt ore from 170kt ore) half on half. Further scale expansion will occur in FY2009 with 11.8kt contained nickel forecast versus 7.3kt in FY2008.
- Balance sheet remains strong with \$111m cash and \$7m debt at 30th June. FY2008 profit guidance is for \$60m NPAT.

Price Performance



Security/Capital Details

ASX Code	PAN
Market Cap	\$439 M
Issued Shares (dil)	195.0 M
Avg Mth T'over	35.86 M
12 Mth High – Low	\$6.12 - \$2.14

Key Data/Ratios – FY 2008

EBITDA / Sales	53.0%
EBIT / Sales	35.1%
Debt / Equity	5.5%
Interest Cover	130.7 x
ROE	42.4%
EPS Growth	-22.3%
DCF	\$3.57
12 Mth Price Target	\$3.80

BUY: Total return +10% or more over a 12 month period

HOLD: Total return expected to be between +10% to -10% over a 12-month period

SELL: Total return expected to be -10% or more over a 12 month period

TOTAL RETURN OR TSR = capital growth in share price + expected dividend yield in that period

Year to June	NPAT (Rep) \$M	NPAT (PSig) \$M	EPS (PSig) c	EPS Growth %	PER x	CFPS c	P/CF x	DPS c	Div Yld %	Franking %
2007a	88.1	88.1	45.5	315.5	9.1	104.9	3.9	12.0	2.9	100
2008e	60.5	68.7	35.3	-22.3	6.4	53.5	4.2	11.0	4.9	100
2009e	102.1	102.1	52.4	48.2	4.3	88.1	2.6	13.0	5.8	100
2010e	126.5	126.5	64.9	23.8	3.5	88.3	2.5	18.0	8.0	100



Production

- June quarter contained nickel production for both the Savannah (8.2%) and Lanfranchi (9.1%) mines was down on the March quarter. This reflected equipment availability issues at both sites. At the Savannah mine, mining contractor McMahons was brought in at the beginning of April to increase underground development which had fallen behind plan. McMahons are expected to stay on site until the end of Sep at this stage.
- As previously announced, FY2009 is expected to see production of 20,500-21,500 contained nickel tonnes (17,000-18,000 tonnes equity share).

Costs

- Lower production, the employment of McMahons, and upward cost pressures on labour, materials and fuel all impacted in the June quarter.
- The impact was more evident at Savannah due to McMahon's costs and the dependency of the Savannah mine on diesel generated power.
- For the Panoramic Group as a whole, the cash cost per payable pound of nickel increased by 12.5% in FY2008 versus FY2007 to A\$6.65/lb. However, the Savannah mine operated below this level for the Sep 2007 to Mar 2008 quarters and the Lanfranchi mine operated below this level in the Mar and Jun 2008 quarters, reflecting the increasing scale benefits accruing through production ramp up. Further scale benefit should accrue to Lanfranchi in FY2009 as production ramps up further.
- We have back calculated unit costs on a per tonne basis for the June quarter and adjusted our previous forecasts accordingly. Effectively we are not capturing scale benefits which should accrue to both operations in FY2009 (Savannah with Copernicus production), however in turn this provides some measure of comfort should input costs escalate at a higher rate than expected.

Resource Updates

- Panoramic previously advised an updated resource position for the Savannah mine. Contained nickel increased by XX% over the 12 months to 30th June. Resources are included for the first time for Savannah lower, previously known as the Deeps.
- An updated resource position was also released for the Lanfranchi project today – 5.33Mt @ 2.35% nickel for 125.4kt contained nickel. This represents a virtually unchanged position from 12 months prior (5.3Mt @ 2.38% nickel for 125.7kt), although the former is net of production of 0.29Mt @ 2.55% nickel for 7.3kt contained nickel).
- The new Deacon resource statement includes a 3kt increase in contained nickel for the Deacon orebody (2.24Mt @ 2.83% nickel for 63.6kt contained) compared with the April 2007 pre-mining resource. However, the increase has been achieved by significantly lowering the cut-off grade from 1.6% nickel to now 1.0% nickel. PAN indicates this is reflective of the bulk mining method which is supported by a 0.8% nickel economic cut-of grade for reserves. However, the increase in contained nickel looks very small for such a significant change in the cut-off grade. The rationale requires further explanation as on face value, it hardly seems worth the additional risk and may reflect weaker than expected grades during grade control drilling. The average grade of the stated Deacon resource over the 12 months to 30th June has reduced from 3.04% nickel to 2.83% nickel for an increase of 5.5kt contained nickel.
- The Deacon resource is expected to be the subject of a further update in the Dec quarter following further drilling to test down plunge extensions.
- Winner orebody also believed to now have down plunge extension potential



given EM conductor interpreted below the resource.

- Lanfranchi resource also continues to extend down plunge and has increased by a further 10%.

Safety

- PAN had a poor safety performance in the June quarter, with the LTIFR (long term injury frequency rate) increasing from 12.9 at the end of March to 14.1 at the end of June. Five LTIs were recorded in the June quarter. All employees have fortunately returned to either normal or light duties.
- Deteriorating safety performance can in some instances be symptomatic of more deep rooted organisational issues, hence we raise the above in that context as well as an issue in its own right.
- We note that PAN has instituted a number of measures across both sites to increase safety performance and has been open in communicating the deterioration in performance with investors. We view such openness as a sign of management's commitment to fix the problem, but only results will count.
- We recommend investors pay increased attention to this aspect of company performance in the current environment and not only in respect of PAN, given its potential to signal more deep rooted issues that might not otherwise be apparent and that could signal a future deterioration in financial performance.

Valuation

- Our DCF valuation (A\$3.57/share) and target price (A\$3.80/share) assume a mine life for the Savannah project until the end of 2012.
- Over the next 6-9 months it should become apparent as to whether Lower Savannah (previously Deeps) is economically viable, as well as the size of the orebody. With a resource of over 20kt contained nickel already established for Savannah Lower and drilling ongoing, there is considerable potential for mine life extension. Should this prove to be the case, there is further upside to our valuation other things equal.

Panoramic Resources Limited (PAN : \$2.25)

PRODUCTION

Yr Ending June	2006A	2007A	2008E	2009E	2010E
Contained Nickel (kt)	9.5	11.9	13.1	17.4	20.1
Contained Copper (kt)	3.9	4.0	4.5	4.6	6.0
Contained Cobalt (kt)	0.4	0.4	0.4	0.4	0.6

PRICES

Yr Ending June	2006A	2007A	2008E	2009E	2010E
AUDUSD (USD)	0.75	0.79	0.90	0.93	0.90
Nickel (US\$/lb)	7.40	17.03	12.95	11.80	10.50
Copper (US\$/lb)	2.42	3.23	3.53	3.78	3.36
Cobalt (US\$/lb)	12.96	21.45	36.78	40.00	30.00

INVESTMENT & VALUATION FUNDAMENTALS

Yr Ending June	2006A	2007A	2008E	2009E	2010E
EPS Before Abs (c)	10.9	45.5	35.3	52.4	64.9
EPS Growth (%)	N/A	315.5%	-22.3%	48.2%	23.8%
PER (x)	10.8	9.1	6.4	4.3	3.5
CFPS (c)	27.3	104.9	53.5	88.1	88.3
P/CF (x)	4.3	3.9	4.2	2.6	2.5
EV/EBITDA (x)	3.5	4.2	2.4	1.2	0.5
DPS (c)	0.0	12.0	11.0	13.0	18.0
Yield (%)	0.0%	2.9%	4.9%	5.8%	8.0%
Franking (%)	0%	100%	100%	100%	100%

DCF VALUATION

Yr Ending June	@	%	%	
	A\$m	A\$ps	A\$m	A\$ps
Sally Malay	185.0	0.95	186.9	0.96
Lanfranchi	261.7	1.34	266.3	1.37
Corporate Costs Capitalised	-25.9	-0.13	-26.4	-0.14
Hedge Book	13.2	0.07	13.3	0.07
Interests - Other Entities	1.2	0.01	1.2	0.01
Exploration/Dev Portfolio	70.0	0.36	70.0	0.36
Franking Credits	86.8	0.44	88.0	0.45
Cash	110.8	0.57	110.8	0.57
Interest Bearing Liabilities	-11.0	-0.06	-11.0	-0.06
Minorities	0.0	0.00	0.0	0.00
Additional Capital - Dilution	5.0	0.03	5.0	0.03
Total Valuation - Diluted	696.7	3.57	704.1	3.61

PROFITABILITY RATIOS

Yr Ending June	2006A	2007A	2008E	2009E	2010E
EBIT / Sales (%)	13.4%	24.5%	35.1%	38.7%	43.8%
ROA (%)	N/A	71.7%	51.5%	72.0%	98.7%
ROE (%)	N/A	103.2%	42.4%	42.1%	37.9%
ROFE (%)	N/A	306.2%	158.6%	150.7%	252.1%

INTERIMS (\$m)

Half Yr	Dec 06	Jun 07	Dec 07	Jun 08	Dec 08
Yr Ending June	1H A	2H A	1H A	2H E	1H E
Sales Revenue	242.6	267.9	121.0	144.4	193.4
EBIT	47.1	78.0	43.8	49.4	79.2
Net Profit	32.7	55.4	24.4	36.1	57.9
EPS	17.0	28.6	16.8	18.6	29.7

1. Gearing = (Debt + CNotes) / (Debt + Cnotes + Equity)

BALANCE SHEET (\$m)

Yr Ending June	2006A	2007A	2008E	2009E	2010E
Cash	30.6	119.6	110.8	213.8	342.1
Total Assets	215.5	283.7	307.7	398.6	500.0
Debt	48.1	13.1	11.0	11.1	11.1
Total Liabilities	166.6	161.8	106.1	115.4	115.4
Total Shareholders Equity	48.9	121.8	201.6	283.2	384.7
Total Funds Employed	66.4	15.3	101.8	80.6	53.6

LIQUIDITY & LEVERAGE RATIOS

Yr Ending June	2006A	2007A	2008E	2009E	2010E
Debt / Equity (%)	98.3%	10.8%	5.5%	3.9%	2.9%
Gearing (%) ¹	49.6%	9.7%	5.2%	3.8%	2.8%
Interest Cover (x)	6.4	36.3	130.7	2,216.1	2,727.8
Debt / CashFlow (x)	0.9	0.1	0.1	0.1	0.1
(Debt+CNotes) / CashFlow	0.7	0.1	0.1	0.1	0.1

PROFIT & LOSS (\$m)

Yr Ending June	2006A	2007A	2008E	2009E	2010E
Sales Revenue	241.8	510.5	265.4	355.2	385.7
EBITDA	68.9	167.0	140.7	197.9	214.7
Depn and Amortisation	36.5	41.9	47.5	60.5	45.6
EBIT	32.3	125.1	93.2	137.4	169.1
Net Interest Expense	-4.6	-0.1	4.8	8.5	11.5
Pre-tax Profit	28.1	124.6	97.7	145.9	180.6
Tax	7.2	36.5	29.0	43.8	54.2
Tax rate (%)	25.6%	29.3%	29.7%	30.0%	30.0%
Minorities / pref divs	0.0	0.0	0.0	0.0	0.0
Equity accounted NPAT	0.0	0.0	0.0	0.0	0.0
Net Profit	20.9	88.1	68.7	102.1	126.5
Abnormals	-5.1	0.0	-8.2	0.0	0.0
Reported Net Profit	15.8	88.1	60.5	102.1	126.5

CASHFLOW (\$m)

Yr Ending June	2006A	2007A	2008E	2009E	2010E
Operating Cash Flow	52.0	203.3	104.1	171.8	172.1
Capital Expenditure	-8.3	-9.8	-33.2	-23.3	-1.0
Expln, Develop, Evaln	-27.9	-22.8	-42.1	-25.1	-17.6
Asset Sales/Acquisitions	-1.7	-4.2	0.1	0.0	0.0
Other	0.5	-0.8	0.0	0.0	0.0
Investing Cash Flow	-37.3	-37.6	-75.2	-48.5	-18.7
Share Issues/(Buybacks)	20.6	3.9	3.0	0.7	0.0
Debt Drawdown (Repay)	-19.9	-36.6	-5.3	0.1	0.0
Dividends Paid	0.0	0.0	-36.0	-21.1	-25.0
Other Fin. Flows	0.0	-44.0	0.6	0.0	0.0
Financing Cash Flow	0.7	-76.8	-37.7	-20.4	-25.0
Cash Increase (Decrease)	15.4	88.9	-8.8	103.0	128.4

EARNINGS SENSITIVITIES - % CHANGE

Yr Ending June	2006A	2007A	2008E	2009E	2010E
+/- 1c Movement US\$/A\$	0.0	0.0	0.0	3.0	3.2
+/-10% Ni Price Change	0.0	0.0	0.0	27.7	25.4
+/-10% Change In Costs	0.0	0.0	0.0	25.9	22.7

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