Macquarie Research Equities

Tuesday 12 May 2009

PAN AU		**Neutral**
Relative to		ex 100
Volatility index		very high
Stock price as of 11 May 09	A$	1.97
12-month target	A$	1.50
12-month TSR	%	-23.0
Valuation	A$	1.00
- DCF (WACC 12.7%, beta 1.4, ERP 5.0%, RFR 6.5%)		
GICS sector		materials
Market cap	A$m	378
30-day avg turnover	A$m	2.9
Number shares on issue	m	192.0

Investment fundamentals

Year end 30 Jun		2008A	2009E	2010E	2011E
Sales revenue	m	232.4	226.2	258.1	234.8
EBIT	m	66.8	-13.5	24.6	4.9
Reported profit	m	53.3	-5.1	23.9	8.8
Adjusted profit	m	53.3	-5.1	23.9	8.8
Gross cashflow	m	96.0	72.1	69.9	55.3
CFPS	¢	49.0	36.0	33.6	26.6
CFPS growth	%	-39.4	-26.6	-6.8	-20.8
PGCFPS	x	4.0	5.5	5.9	7.4
PGCFPS rel	x	0.59	0.73	0.78	1.10
EPS adj	¢	27.2	-2.7	11.5	4.3
EPS adj growth	%	-53.1	nmf	nmf	-62.9
PE adj	x	7.2	nmf	17.2	46.4
PE rel	x	0.67	nmf	1.33	4.20
Total DPS	¢	13.0	1.0	2.0	0.0
Total div yield	%	6.6	0.5	1.0	0.0
Franking	%	100	100	100	0
ROA	%	21.7	-4.1	7.2	1.4
ROE	%	30.2	-2.2	9.5	3.3
EV/EBITDA	x	3.0	5.6	5.0	6.9
Net debt/equity	%	-44.2	-24.3	-35.8	-43.6
Price/book	x	1.7	1.7	1.5	1.5

PAN AU vs ex 100, & rec history

Source: FactSet, Macquarie Research, May 2009 (all figures in AUD unless noted)

Analysts

Len Eldridge
618 9224 0838 len.eldridge@macquarie.com
Jim Copland
612 8232 0397 jim.copland@macquarie.com

Panoramic Resources

Revisiting Savannah

Event

- We have reviewed our assumptions for Panoramic's (PAN) Savannah operation following the 3Q09 operations results.

Impact

- **Cost cuts kicking in.** Following the 3Q09 operations report we have adjusted our cost assumptions in line with the reduced costs on a A$/t basis. Mining costs were A$45/t (on a P&L basis, excluding underground development) down from A$57/t and A$50/t in 1Q09 and 2Q09, respectively. Underground development costs at Savannah are expected to be ~A$15–20m pa or ~A$1.00/lb (payable). We have reduced our steady state C1 cash cost forecast to average A$5.40/lb (payable) over the LOM with a further A$1.00/lb payable for capital development.
- **LOM extension upside.** Our base case Savannah valuation use a LOM out to FY13 (or a reserve of 37kt) and does not attribute any value for the 20kt resource below the 500 fault. Mineralisation below the 500 fault is offset from the existing Savannah reserve by 100-150m. If we extend the Savannah LOM to FY19, assuming A$20m of incremental development capex (extending the decline and ventilation) our Savannah valuation increases from A$9m (A$0.04ps) to A$45m (A$0.21ps). PAN has flagged a Savannah Deeps resource update in May.
- **Deacon reserve upgrade.** PAN has increased its Deacon resource at its Lanfranchi operations by 29% to 63.1kt contained nickel. The 2.5mt reserve grading 2.52% nickel represents a 92% resource-to-reserve conversion ratio with decline development to the bottom of the new reserve expected to be completed by 2012, thereby providing access to the full ore body and increasing production flexibility. Our Lanfranchi valuation contributes 58% of our PAN DCF valuation and is based on a LOM to June 2016, implying an aggregate Lanfranchi reserve of 77kt compared with the current JORC reserve and resource of 66kt and 140kt contained nickel, respectively.

Earnings revision

- We have reduced our forecast FY09 loss per share by 1.4cps to 2.69cps and increased our FY10 EPS from 5.28cps to 11.5cps on the back of lower cost assumptions.

Price catalyst

- 12-month price target: A$1.50 based on a P/NPV and PER methodology.
- Catalyst: Resource update at Savannah Deeps to extend LOM post 2013.

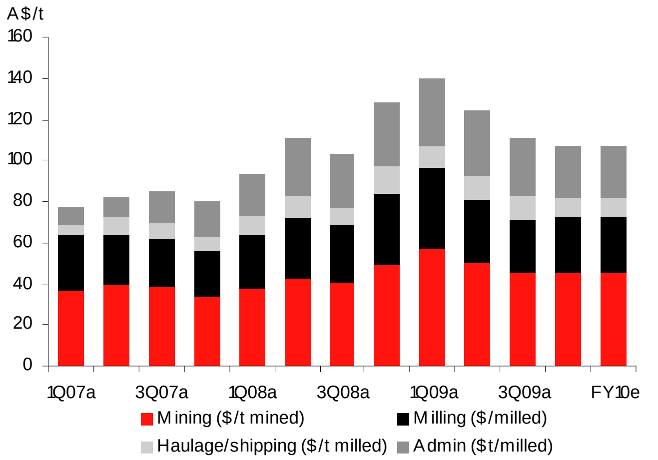
Action and recommendation

- We maintain our Neutral recommendation but raise our target price to A$1.50, representing a P/NPV of 1.5x, from A$0.80. Our upgraded price target is a reflection of the relative trading ranges of our nickel universe. PAN provides investors with strong leverage to any potential spike in the nickel price, with a stable balance sheet (and minimal capital calls on the horizon) to provide investors with a level of comfort.

Update of Savannah parameters

- PAN flagged an aggressive cost saving initiative with the release of the December quarter operation result in January in response to the falling nickel price. PAN has largely maintained production targets at Savannah with the only reduction to date being the suspension of mining at the Copernicus open pit which was expected to contribute ~0.95t nickel (PAN 60% interest).
- On a dollar per tonne basis, costs at Savannah peaked in the 2008 September quarter. Since then, PAN has been able to bring costs down, most importantly at the mining and milling level. Milling costs have been assisted by the fall in diesel prices as the Savannah operation is powered by diesel generators.

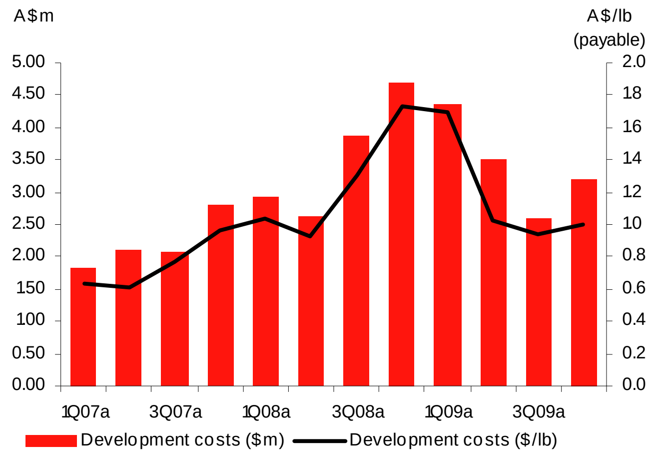
Cost components (P&L)



Source: Company data, Macquarie Research, May 2009

- While not included in C1 cash costs, on a cashflow level we are including underground development costs of A$15m pa or A$1.00/lb (payable) for FY10–12, broadly in line with 3Q09 (A$0.94/lb), with costs coming back in FY13 to A$5m as PAN is currently ~15 months ahead in underground development work.

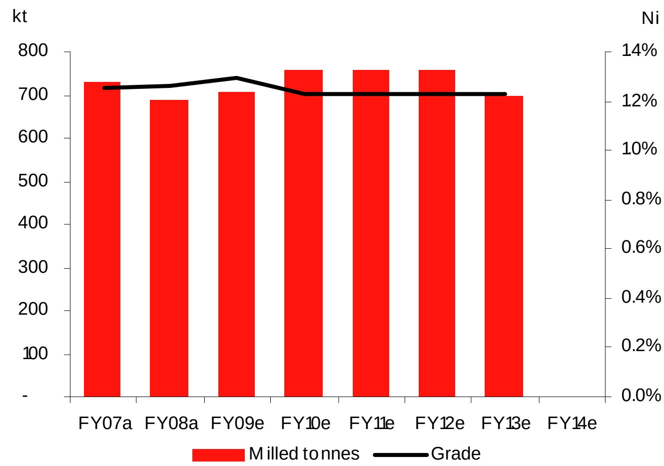
Savannah underground development costs



Source: Company data, Macquarie Research, May 2009

- Our LOM base case milled tonnes and grade profile is based on the 'upper zone' reserve (2.9mt @ 1.29% nickel containing 38kt nickel) and does not include any tonnes below the 550 fault level (Savannah Deeps) which currently has a resource of 20.7kt nickel.

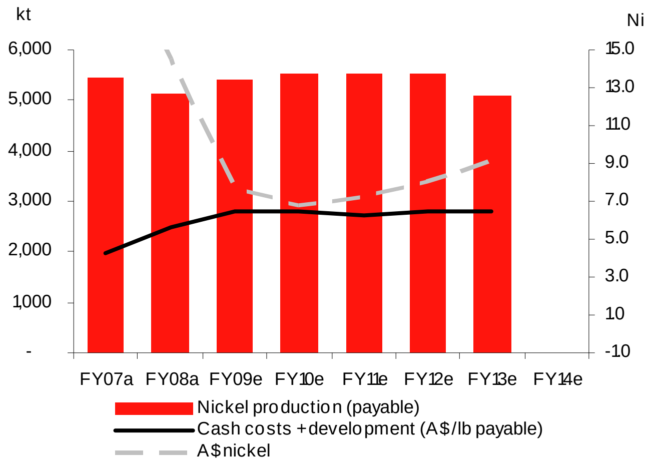
Base case mine parameters



Source: Company data, Macquarie Research, May 2009

- If we incorporate the Savannah Deeps resource in our modelling, assuming A$20m of incremental development capex (extending the decline and ventilation) our Savannah valuation increases from A$9m (A$0.04ps) to A$45m (A$0.21ps).

Base case production & cost forecast



Source: PAN, Macquarie Research, May 2009

Panaronimic Resources (PAN)

Share price **$2.10**

Year End 30 June 1.4

Profit & Loss		2008e	2009e	2010e	2011e
Sales Revenue	**$m**	**232**	**226**	**258**	**235**
+ Other Revenue	$m	0	1	0	0
Total Revenue	**$m**	**232**	**227**	**258**	**235**
- Operating Costs	$m	111	154	178	173
- Corporates/Other	$m	12	9	10	10
EBITDA	**$m**	**109**	**64**	**71**	**51**
- Depreciation/Amortisation	$m	40	47	44	44
- Write-Offs	$m	2	30	2	3
EBIT	**$m**	**67**	**-14**	**25**	**5**
+ Net Interest	$m	5	4	6	8
Pretax Profit	**$m**	**71**	**-9**	**30**	**13**
- Tax Expense	$m	18	-4	6	4
Net Profit	**$m**	**53**	**-5**	**24**	**9**
+ Significant Items	$m	0	0	0	0
Reported Profit	$m	**53**	**-5**	**24**	**9**
Adjusted Profit	$m	**53**	**-5**	**24**	**9**
Shares on Issue	m	192	204	204	204
EPS (adj)	c	27.3	(2.5)	11.5	4.3
DPS	c	13.0	1.0	2.0	0.0
Payout ratio	%	47.7%	-39.9%	17.4%	0.0%

Balance Sheet $m		2008e	2009e	2010e	2011e
Cash	$m	111	61	104	127
Fixed Assets	$m	136	139	117	95
Total Assets	$m	332	329	358	361
Borrowings	$m	8	4	8	8
Total Liabilities	$m	100	92	91	90
Shareholders Equity	$m	232	237	267	271
N'Debt/N'Debt+Equity	%	-79%	-32%	-56%	-77%
Interest Cover (x)	$m	(14.4)	3.2	(4.5)	(0.6)
Return on Equity (%)	%	30%	-2%	9%	3%

Production & Key Assumptions		2008e	2009e	2010e	2011e
Sally Malay (100%)	kt	7.6	8.0	8.1	8.1
Lanfranchi (100%)	kt	5.5	8.5	10.6	9.8
Total attrib. nickel (in-conc)	**kt**	**13.1**	**16.5**	**18.7**	**18.0**
Payable nickel production	kt	10.9	13.3	14.8	14.3
Cash cost (per lb payable Ni)	**US$/lb**	**4.24**	**4.05**	**3.86**	**3.66**
Ni Price Realised (per lb payable Ni)	US$/lb	11.76	6.82	6.13	5.63
Spot Nickel Price	US$/lb	12.93	5.57	4.69	5.63
Exchange Rate	A$/US$	89.7	73.5	70.0	70.0

Cashflow		2008e	2009e	2010e	2011e
Operating Surplus	$m	112	50	71	51
Net Interest	$m	5	4	6	8
Taxes Paid	$m	-22	-20	-1	-5
Other / Dividends Received	$m	0	1	0	0
Operating Cash Flows	**$m**	**96**	**35**	**75**	**54**
Capital Expenditure	$m	-59	-57	-22	-22
Exploration	$m	-6	-13	-10	-5
Acquisitions/Divestments	$m	0	0	0	0
Other	$m	0	0	0	0
Investing Cash Flows	**$m**	**-65**	**-70**	**-32**	**-27**
Increase/(Decrease) Borrowir	$m	-7	-4	0	0
Dividends Paid	$m	-36	-12	0	-4
Other	$m	4	0	0	0
Financing Cash Flows	**$m**	**-39**	**-15**	**0**	**-4**
Net Increase/(Decrease) Ca	**$m**	**-9**	**-50**	**43**	**23**

DCF valuation	$m	$/share
Sally Malay	9	0.04
Lanfranchi	123	0.58
Hedging	53	0.25
Exploration	-	-
Corporate Overheads	(13)	(0.06)
Cash plus net rec. plus options	45	0.22
Debt	(6)	(0.03)
Net Equity Value	**212**	**1.00**
Fully diluted number of shares	211m	

Key investment ratios		2008e	2009e	2010e	2011e
GCFPS	c	49.0	36.0	33.6	26.6
PER (adj)	x	7.7	(83.8)	18.3	49.4
EV/EBITDA	x	2.8	11.1	4.8	6.3
PGCF	x	4.3	5.8	6.3	7.9

Source: Macquarie Research, May 2009

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