

Resources and Costs Up, Grade Down

Brief Update Note

Stock:	Matrix Metals Limited (MRX 5.5cps)
Valuation:	12cps (Previously 17cps)
Market Cap (Full. Dil.):	\$44.4m (\$44.4m)
Issued Capital (Full. Dil.):	807.5m shares (807.53m)
Cash (as at 31 March 2008):	\$12.9m
Date:	25 June 2008
Resources Analyst:	Andrew Muir



Source: Iress

Detail:

June Quarter Production Underperforms – June 2008 quarter production at Matrix Metals Limited’s (“Matrix”, “Company”) Leichhardt operation will only be at 86% of capacity, producing ~1,180t of copper cathode at cash costs of ~US\$2.50/lb. The underperformance is due to poor equipment availability as well as a once-off re-lining of the leached copper solution drains and several copper solution ponds. Costs were also impacted by the high diesel price due to the Company’s reliance on diesel for all power. Based on an average copper price of ~US\$3.80/lb for the June quarter, we estimate Leichhardt had an operating margin of ~US\$1.30/lb, generating operating cash flow of ~US\$3.5m.

FY2009 Costs Up – The Company also indicated that FY2009 operating costs should average US\$2.40/lb, higher than our previous expectations of US\$2.00 – 2.20/lb. The main culprits are increases in operating expenses, primarily diesel, as well as adverse movements in the AUD:USD exchange rate.

Plant Upgrade Complete by Mid July – The plant expansion to 9,000tpa copper cathode is due to be completed by mid July, with commissioning finalised by mid-August. Construction of the up-scaled plant had originally planned to be finished by the end of June; however, difficulties with contractor availability led to the slight slippage in completion date.

Initial Stage 1 Reserve – Matrix has delineated an initial JORC compliant reserve for Leichhardt Stage 1 of 1.49Mt @ 1.02% Cu. This should allow for a Stage 1 mine life out to early-mid CY2010. The size of the reserve was close to our expectations; however, the grade was slightly lower than our expectations of 1.1 – 1.2% Cu. Mining reconciliations to date indicated slightly higher dilution and ore loss than initially envisaged. This information was utilised in the reserve estimation and were the main contributors to the lower reserve grade.

Stage 2 Resource – The Company has also released the Stage 2 resource for the Leichhardt project of 8.1Mt @ 0.88% Cu. Of this, 5.9Mt @ 0.88% Cu is leachable, with the remainder pertaining to sulphide mineralisation, and not treatable through the current plant. When subtracting the Stage 1 reserve, the remaining resource for Stage 2 is ~4.2Mt @ 0.82% Cu. This would give the Leichhardt operation a total mine life of approximately 5 years. However, as with the Stage 1 reserve, the resource grade is lower than we expected, and will have a detrimental impact on operating costs per pound. Metallurgical testwork on the Stage 2 ore is underway, with a reserve calculation due towards the end of CY2008.

Valuation Downgrade – We have incorporated the Stage 1 reserve, Stage 2 resource as well as higher cost expectations into our model for Matrix. Whilst the life of mine is similar to our previous modelling, stretching out to early 2013, we have reduced the grade and increased operating costs in line with the Company’s guidance. As a consequence, our valuation for Matrix has reduced to 12cps from 16.7cps.

Impact:

Whilst the Company had indicated that it was exposed to the higher oil price, FY2009 costs around US\$2.40 were still higher than market expectations. The reduction in grade for both the Stage 1 reserve, and Stage 2 resource were also disappointing, both having a negative impact on our valuation.

If the operation is working at capacity and with the current US\$1.30/lb margins, Leichhardt will generate ~US\$4m in operating cashflow per quarter (US\$16mpa). The increase to 9,000tpa increases this to ~US\$6.7m per quarter (US\$26.8m pa). As the Company is unhedged, we estimate that a US\$0.10/lb movement in the copper price will lead to a US\$2m change in annual cash flow. Consequently, an investment in Matrix is now heavily leveraged to the copper price, and we have reduced our recommendation for **Matrix Metals Limited** to a **Speculative Buy** from a Buy.

Matrix Metals Limited		Share Price			
MRX		\$0.055			
Key Market Information					
Share Price		\$0.055			
Market Capitalisation		\$44m			
52 Week High-Low		\$0.20-\$0.07			
Issued Capital		807.5m			
Issued Capital (fully diluted inc. ITM options)		807.5m			
Options		23.4m@ \$A0.14			
Hedging					
Yearly Turnover/Volume		\$118.0m/939.4m shares			
Liquidity Measure (Yearly Turnover/Issued Capital)		116%			
Valuation		\$0.12			
Financial Performance					
	Unit	FY2007A	FY2008F	FY2009F	FY2010F
Net Revenue	A\$m	9.6	40.2	75.1	124.2
Total Costs	A\$m	(18.0)	(29.4)	(52.6)	(79.2)
EBITDA	A\$m	(8.4)	10.9	22.4	44.9
Depreciation/Amort	A\$m	(0.1)	(5.4)	(5.1)	(11.0)
EBIT	A\$m	(8.5)	5.5	17.3	34.0
Net Interest	A\$m	0.5	(0.4)	(0.2)	(3.5)
Pre-Tax Profit	A\$m	(8.0)	5.0	17.1	30.4
Tax Expense	A\$m	-	-	(2.5)	(9.1)
NPAT	A\$m	(8.0)	5.0	14.6	21.3
Abnormal Items	A\$m	-	-	-	-
Reported Profit	A\$m	(8.0)	5.0	14.6	21.3
Financial Position					
	Unit	FY2007A	FY2008F	FY2009F	FY2010F
Cash	A\$m	14.2	8.4	23.3	7.4
Other Current Assets	A\$m	0.9	13.2	15.5	23.5
Total Current Assets	A\$m	15.1	21.6	38.8	30.8
Property, Plant & Equip.	A\$m	20.8	24.6	22.0	114.6
Exploration	A\$m	9.8	12.1	13.2	13.2
Investments/other	A\$m	1.5	2.2	2.2	2.2
Tot Non-Curr. Assets	A\$m	32.1	38.9	37.4	130.0
Total Assets	A\$m	47.2	60.5	76.2	160.8
Short Term Borrowings	A\$m	4.8	3.0	2.0	-
Other	A\$m	4.6	4.5	5.0	13.2
Total Curr. Liabilities	A\$m	9.4	7.5	7.0	13.2
Long Term Borrowings	A\$m	5.2	3.0	2.0	50.0
Other	A\$m	0.8	0.8	0.8	0.8
Total Non-Curr. Liabil.	A\$m	6.0	3.8	2.8	50.8
Total Liabilities	A\$m	15.3	11.3	9.8	64.0
Net Assets	A\$m	31.9	49.2	63.9	85.2
Cashflow					
	Unit	FY2007A	FY2008F	FY2009F	FY2010F
Operating Cashflow	A\$m	(2.5)	0.3	20.6	45.2
Income Tax Paid	A\$m	-	-	-	-
Interest & Other	A\$m	0.4	(0.7)	(0.2)	(3.5)
Operating Activities	A\$m	(2.1)	(0.4)	20.4	41.7
Property, Plant & Equip.	A\$m	(12.6)	(9.9)	(0.8)	(101.6)
Exploration and Devel.	A\$m	(3.0)	(3.5)	(2.9)	(2.0)
Investments	A\$m	8.9	(0.7)	-	-
Investment Activities	A\$m	(6.8)	(14.2)	(3.6)	(103.6)
Repayment of Borrowings	A\$m	-	(4.2)	(2.0)	(2.0)
Proceeds From Borrowings	A\$m	10.0	0.2	-	48.0
Equity	A\$m	7.8	12.8	0.1	-
Dividends Paid	A\$m	-	-	-	-
Financing Activities	A\$m	17.3	8.8	(1.9)	46.0
Net Cashflow	A\$m	8.4	(5.8)	14.8	(15.9)
Ratio Analysis					
	Unit	FY2007A	FY2008F	FY2009F	FY2010F
Cashflow Per Share	A¢	(1.2)	1.3	2.4	3.9
Cashflow Multiple	X	(4.8)	4.3	2.3	1.4
Earnings Per Share	A¢	(1.2)	0.6	1.8	2.6
Price to Earnings Ratio	X	(4.7)	8.9	3.1	2.1
Dividends Per Share	A¢	-	-	-	-
Dividend Yield	%	-	-	-	-
Interest Cover	X	13.0	72.0	9.6	-
Return on Equity	%	na	10%	23%	25%
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Richard Procter					
Company Information					
June 2008					
SPECULATIVE BUY					
Top 10 Shareholders					
		m shares	%		
Independence Group NL		128.88	16.0		
RBC Dexia Investor Services Australia Nominees		76.55	9.5		
Glencore International AG		41.67	5.2		
HSBC Custody Nominees		22.61	2.8		
National Nominees Pty Ltd		9.53	1.2		
Mr Eugen Schilter		9.21	1.1		
Merrill Lynch (Australia) Nominees Pty Ltd		6.78	0.8		
Standard Bank London Ltd		6.62	0.8		
NEFCO Nominees Pty Ltd		6.22	0.8		
ANZ Nominees		4.85	0.6		
Reserves & Resources					
		Mt	%	000t	Attrib.
Leichhardt					
Mt Cuthbert Resources		1.97	1.10	21.7	21.7
Mt Watson Resources		8.10	0.88	71.3	71.3
White Range					
Cloncurry Area Resources		14.84	1.10	163.3	163.3
TOTAL RESOURCES		24.91	1.10	274.0	274.0
Leichhardt Reserves		1.49	1.02	15.2	15.2
Production Summary					
	Unit	FY2007A	FY2008F	FY2009F	FY2010F
*Attributable					
Payable Copper Metal	000t	-	4.9	8.4	16.1
Cash Cost	US\$/lb	-	2.12	2.41	2.30
Price Assumptions					
	Unit	FY2007A	FY2008F	FY2009F	FY2010F
Copper	US\$/lb	3.21	3.54	3.60	3.13
Exchange Rate	A\$/US\$	0.79	0.88	0.89	0.85
\$A Copper	A\$/lb	4.09	4.01	4.07	3.68
Hedging					
	Unit	FY2007A	FY2008F	FY2009F	FY2010F
Total Forward Sales - Copper	000t	-	-	-	-
Forward Copper Price	A\$/lb	-	-	-	-
Sensitivity Analysis					
	Valuation (\$/s)	NPAT	EPS (¢)	CFPS (¢)	
Base Case	0.120	5.0	0.6	1.3	
Exchange Rate +10%	0.08	3.0	0.4	1.0	
Exchange Rate -10%	0.17	7.6	0.9	1.6	
Copper Price +10%	0.17	7.3	0.9	1.6	
Copper Price -10%	0.07	2.8	0.3	1.0	
Operating Costs +10%	0.08	3.7	0.5	1.1	
Operating Costs -10%	0.16	6.4	0.8	1.5	
*N.B. NPAT, EPS, CFPS forecasts are for FY2008					
Share Price Valuation (NAV)					
		Est. \$m	Est. cps		
Kuridala (NPV @ 8%)		17.8	2.2		
Leichhardt (NPV @ 8%)		39.8	4.9		
Exploration - Uranium		10.0	1.2		
Exploration - Copper		20.0	2.5		
Cash		12.9	1.6		
Forwards		0.7	0.1		
Corporate Overheads		(4.7)	(0.6)		
Total Debt		(7.6)	(0.9)		
Tax Losses		7.9	1.0		
Options & Other Equity		1.0	0.1		
Total		97.8	12.1		
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Sources: IRESS, Company Information, Hartleys Research					
Last Updated: 25/06/2008					

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Hartleys Recommendation Categories

Strong Buy	Significant share price appreciation anticipated
Buy	Share price appreciation anticipated
Speculative Buy	Share price appreciation anticipated but is considered high risk
Accumulate	Buy in periods of weakness
Hold	Take no action
Reduce	Sell in periods of strength
Sell	Significant price depreciation anticipated

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