

29 Mar 2018

## AVANCO RESOURCES LIMITED (AVB)

### Oz gets a Brazilian

OZ Minerals Limited (OZL) has recently announced a takeover offer to acquire at least 50.1% of Avanco Resources Limited (AVB). OZL will pay 8.5c cash plus 0.009 OZL shares for each AVB share, valuing AVB at 16.8cps or A\$444M as of market open on 27th March 2018 (transaction value now ~ A\$409M). The Board of AVB has unanimously recommended that all shareholders accept the offer, subject to no superior proposal being received.

### Board and major shareholder support

The offer is subject to a 50.1% minimum acceptance condition by AVB shareholders. Of its four substantial shareholders, Appian Natural Resource Funds and BlackRock have shown support for the offer. AVB's largest holder in Appian Natural Resources Funds, which holds 18.5% of AVB, has entered into a pre-bid acceptance deed. Funds and accounts under management by BlackRock, representing 11.6% of AVB, have also stated their intention to accept OZL's offer. AVB's directors and management collectively own 0.57% of AVB. Together, shareholders representing 30.62% of AVB shares have indicated they will accept the offer. It is worth noting that Greenstone (16.7%) and Glencore (8.3%) did not enter pre-bid agreements. The current state of play is that of the 55% of AVB held by substantials, 30% have indicated their support for the deal.

The offer looks like a good deal for AVB, which has had an average weighted VWAP of 9.1cps for the last three years. Equally though, our last valuation (2 March 2017) was 20cps.

### Move to a Neutral Recommendation

Given our valuation, the premium comes as no great surprise (OZL diversifying into Brazil was not expected, although, we do not formally cover it). Our valuation for AVB has ranged between 16cps and 20cps over the past 6 months.

Our price target for AVB is 16.6cps and reflects the current offer price by OZL – 8.5c cash plus 0.009 OZL shares for every AVB share. Every 50c movement in OZL, represents a ~0.5c movement in the offer price for AVB.

Considering the dearth of quality copper projects, this move by OZL may create a sense of urgency for those copper producers looking to acquire further assets; especially those running out of mine life like SFR.asx who has 3.5 years of mine life at Doolgunna. With copper featuring in most EV narratives and recent acquisitions such as Copper Mountain's (CMMC.tsx) takeover of Altona (AOH.asx), we may be on the cusp of a return significant M&A activity in this space.

We move to a Neutral recommendation for AVB assuming at least 90% of shareholders accept the offer.

<b>Share Price</b>	\$0.16
<b>Valuation</b>	\$0.20
<b>Price Target (12 month)</b>	\$0.17

**Brief Business Description:**  
Cu-Au developer and explorer

**Hartleys Brief Investment Conclusion**  
Brazilian Cu-Au miner, expected to produce ~14ktpa Cu & 10kozpa Au from Antas this year, with growth potential at Pedra Branca and further afield.

**Chairman & MD**  
Vernon Tidy (Interim Chairman & Non-Exec Director)  
Tony Polglase (Managing Director)

**Top Shareholders**

Appian Natural Resources Fund	18.5%
Greenstone	16.7%
Blackrock Group	11.9%
Glencore	8.3%

**Company Address**  
Suite 3, 257 York Street  
Subiaco, WA 6008

**Issued Capital** 2456.9m  
- fully diluted 2652.2m

**Market Cap** A\$380.8m  
- fully diluted A\$411.1m

**Cash (31 Dec 17a)** A\$31.8m

**Debt** A\$0.0m

**EV** A\$349.0m

**EV/Resource lb** A\$0.25/oz

Prelim. (A\$m)	CY17a	CY18e	CY19e
Prod (kt Cu)	13.6	14.3	14.3
Op Cash Flw	27.2	48.8	88.1
Norm NPAT	2.7	19.9	50.3
CF/Share (cps)	0.1	1.0	2.4
EPS (cps)	0.1	1.0	2.4
P/E	117.9	16.1	6.4

	Mt	Cu (%)	Au (g/t)
Resources (CentroGold)	32.8	-	2.1
Resources (Carajás)	33.2	2.0	0.5
Reserves (Total)	3.0	2.6	0.6



Paul How ard  
Resources Analyst  
Ph: +61 8 9268 3045

E: paul.how ard@hartleys.com.au

## SUMMARY MODEL

Avanco Resources Ltd							Share Price		29 March 2018				
AVB							\$0.155		Neutral				
<b>Key Market Information</b>									<b>Company Information</b>				
Share Price									Vernon Tidy (Interim Chairman & Non-Exec Director)				
Market Capitalisation - ordinary									Suite 3, 257 York Street				
Net Cash									Subiaco, WA 6008				
Market Capitalisation - fully diluted									+61 8 9324 1866				
EV									+61 8 9200 1851				
Issued Capital									www.avancoresources.com				
Options													
Issued Capital (fully diluted inc. all options)													
Issued Capital (fully diluted inc. all options and new capital)													
Valuation													
12month price target													
<b>P&amp;L</b>													
	Unit	Dec 16	Dec 17	Dec 18	Dec 19	Dec 20							
Net Revenue	A\$m	66.2	116.7	140.1	231.8	446.7							
Total Costs	A\$m	-62.4	-112.4	-92.7	-135.8	-243.1							
EBITDA	A\$m	3.8	4.3	47.4	96.0	203.6							
- margin		6%	4%	34%	41%	46%							
Depreciation/Amort	A\$m	0.0	0.0	-24.5	-32.6	-47.4							
EBIT	A\$m	3.8	4.3	22.9	63.4	156.2							
Net Interest	A\$m	-4.9	-1.1	0.8	-3.6	-7.0							
Norm. Pre-Tax Profit	A\$m	-1.1	3.2	23.7	59.8	149.2							
Reported Tax Expense	A\$m	0.0	0.0	0.0	-0.5	-23.9							
Normalised NPAT	A\$m	-0.9	2.7	19.9	50.3	125.3							
Abnormal Items	A\$m	-0.2	0.5	3.8	9.0	0.0							
Reported Profit	A\$m	-1.1	3.2	23.7	59.3	125.3							
Minority	A\$m	0	0	0	0	0							
Profit Attrib	A\$m	-1.1	3.2	23.7	59.3	125.3							
<b>Balance Sheet</b>													
	Unit	Dec 16	Dec 17	Dec 18	Dec 19	Dec 20							
Cash	A\$m	30.5	31.5	-0.9	149.1	178.3							
Other Current Assets	A\$m	22.4	24.7	11.5	19.1	36.7							
Total Current Assets	A\$m	53.0	56.2	10.6	168.2	215.0							
Property, Plant & Equip.	A\$m	81.5	64.8	96.1	205.2	303.2							
Exploration	A\$m	28.3	49.9	75.3	89.3	103.3							
Investments/other	A\$m	2.9	5.2	5.2	5.2	5.2							
Tot Non-Curr. Assets	A\$m	112.7	119.9	176.6	299.7	411.7							
Total Assets	A\$m	165.7	176.0	187.2	467.9	626.7							
Short Term Borrowings	A\$m	6.5	3.9	3.9	3.9	3.9							
Other	A\$m	17.4	23.0	10.4	14.1	22.9							
Total Curr. Liabilities	A\$m	23.8	26.8	14.3	18.0	26.8							
Long Term Borrowings	A\$m	-	-	-	108.1	86.5							
Other	A\$m	23.8	31.0	31.0	31.0	31.0							
Total Non-Curr. Liab.	A\$m	23.8	31.0	31.0	139.1	117.5							
Total Liabilities	A\$m	47.7	57.8	45.3	157.1	144.3							
Net Assets	A\$m	118.0	118.2	141.9	310.8	482.4							
Net Debt	A\$m	-24.0	-27.6	4.8	-37.2	-88.0							
<b>Cashflow</b>													
	Unit	Dec 16	Dec 17	Dec 18	Dec 19	Dec 20							
Operating Cashflow	A\$m	16.5	28.5	48.0	92.2	194.8							
Income Tax Paid	A\$m	0.0	-1.5	0.0	-0.5	-23.9							
Interest & Other	A\$m	0.0	0.2	0.8	-3.6	-7.0							
Operating Activities	A\$m	16.5	27.2	48.8	88.1	163.9							
Property, Plant & Equip.	A\$m	0.0	0.0	-43.0	-137.8	-141.5							
Exploration and Devel.	A\$m	-4.2	-11.0	-25.4	-14.0	-14.0							
Other	A\$m	-26.3	-8.5	-12.9	-3.9	-3.9							
Investment Activities	A\$m	-30.6	-19.5	-81.2	-155.8	-159.4							
Net Borrowings	A\$m	0.0	0.0	0.0	108.1	-21.6							
Equity or "tbc capital"	A\$m	0.0	0.0	0.0	109.6	46.3							
Dividends Paid	A\$m	0.0	0.0	0.0	0.0	0.0							
Financing Activities	A\$m	3.2	-5.4	0.0	217.7	24.7							
Net Cashflow	A\$m	-10.9	2.3	-32.4	150.1	29.2							
<b>Shares</b>													
	Unit	Dec 16	Dec 17	Dec 18	Dec 19	Dec 20							
Ordinary Shares - End	m	2457	2457	2457	2458	2458							
Ordinary Shares - Weighted	m	2461	2457	2457	2457	2458							
Diluted Shares - Weighted	m	2461	2457	2457	2457	2458							
<b>Ratio Analysis</b>													
	Unit	Dec 16	Dec 17	Dec 18	Dec 19	Dec 20							
Cashflow Per Share	A\$ cps	0.7	1.1	2.0	3.6	6.7							
Cashflow Multiple	x	23.2	14.0	7.8	4.3	0.0							
Earnings Per Share	A\$ cps	0.0	0.1	1.0	2.4	5.1							
Price to Earnings Ratio	x	-343.5	117.9	16.1	6.4	0.0							
Dividends Per Share	AUD	0.0	0.0	0.0	0.0	0.0							
Dividend Yield	%	0.0%	0.0%	0.0%	0.0%	0.0%							
Net Debt / Net Debt + Equity	%	-26%	-31%	3%	-14%	-22%							
Interest Cover	X	0.8	4.0	na	17.8	22.3							
Return on Equity	%	na	2%	14%	16%	26%							
<b>Directors</b>													
<b>Reserves &amp; Resources</b>													
<b>Top Shareholders</b>													
<b>Company Information</b>													
<b>Production Summary - Antas North</b>													
<b>Production Summary - Pedra Branca East</b>													
<b>Costs</b>													
<b>Price Assumptions</b>													
<b>Hedging</b>													
<b>Sensitivity Analysis</b>													
<b>Share Price Valuation (NAV)</b>													

Analyst: Paul Howard  
+61 8 9268 3045  
"tbc capital" could be equity or debt. Our valuation is risk-adjusted for how this may be obtained.  
Sources: IRESS, Company Information, Hartleys Research

Last Updated: 29/03/2018

## VALUATION

Our sum of parts valuation for AVB assumes Antas is at full plant capacity (0.7Mtpa), CentroGold commences production in CY19 and Pedra Branca moves into production in early-CY20. We model a nominal exploration value (A\$30M) for the recent Pantera acquisition. We model Antas out to mid-CY25 (8 years remaining) and assume additional resource tonnes convert, and are included in the mining inventory. We have adjusted our Cu recoveries to 97% going forward.

We model a staged 9.5 years at Pedra Branca, and see potential upside at both projects. With the inclusion of Chega Tudo, we model CentroGold as a 10 year, 2Mtpa operation at a head-grade of 1.8g/t but note the recent updated resource grade of 2.1g/t Au. CentroGold is somewhat risked as licensing issues currently remain unresolved but a clear pathway to resolution is apparent and would be a catalyst for an upgrade to a Buy recommendation. We model a nominal A\$120m (\$0.03/share) for exploration upside. We have added A\$30M as consideration for the recent Pantera acquisition and will look to evaluate this as further information is released. We believe AVB is well positioned for brownfield exploration success at both projects and more regionally.

*Hartleys models Antas to 2025, CentroGold to 2029 & Pedra Branca to 2029*

**Fig. 1: Hartleys Sum of Parts Valuation for AVB**

Share Price Valuation (NAV)	Risked Est. A\$m	Est. A\$/share
100% Pedra Branca (pre-tax NAV at disc. rate of 12%)	258	0.07
100% Antas (pre-tax NAV at disc. rate of 8%)	259	0.07
100% CentroGold (pre-tax NAV at disc. rate of 14%)	191	0.05
Other Exploration	120	0.03
Forwards	0	0.00
Corporate Overheads	-60	-0.02
Net Cash (Debt)	32	0.01
Tax (NPV future liability)	-104	-0.03
Options & Other Equity	18	0.00
Hedging	-2	0.00
<b>Total</b>	<b>711.5</b>	<b>0.20</b>

Source: Hartleys Estimates

*Hartleys sum of parts valuation for AVB has increased to A\$0.20/share*

Fig. 2: Earnings Changes

	Unit	31 Dec 16	31 Dec 17	31 Dec 18			31 Dec 19		
		Actual	Actual	Old	New	% diff	Old	New	% diff
Cu Production (payable)	kt	10.3	13.6	14.3	14.3	0.0%	14.9	14.3	-3.8%
Au Production (payable)	koz	7.4	10.8	10.6	10.6	0.0%	10.0	10.6	6.5%
Cash costs (C1)	A\$/lb Eq	2.06	2.31	2.04	2.03	-0.3%	1.89	3.18	68.2%
Total operating costs (AISC)	A\$/lb Eq	2.99	3.76	3.58	3.70	3.3%	3.00	3.32	10.7%
<b>Net Revenue</b>	<b>A\$m</b>	<b>66.2</b>	<b>116.7</b>	<b>139.8</b>	<b>140.1</b>	<b>0.2%</b>	<b>136.3</b>	<b>231.8</b>	<b>70.1%</b>
<b>Total Costs</b>	<b>A\$m</b>	<b>-62.4</b>	<b>-112.4</b>	<b>-87.6</b>	<b>-92.7</b>	<b>5.8%</b>	<b>-82.9</b>	<b>-135.8</b>	<b>63.8%</b>
EBITDA	A\$m	3.8	4.3	52.3	47.4	-9.2%	53.4	96.0	79.8%
- margin		6%	4%	37%	34%	-9.4%	39%	41%	5.7%
Depreciation/Amort	A\$m	0.0	0.0	-23.4	-24.5	4.9%	-24.0	-32.6	35.8%
<b>EBIT</b>	<b>A\$m</b>	<b>3.8</b>	<b>4.3</b>	<b>28.9</b>	<b>22.9</b>	<b>-20.6%</b>	<b>29.4</b>	<b>63.4</b>	<b>115.9%</b>
Net Interest	A\$m	-4.9	-1.1	0.6	0.8	37.7%	-10.8	-3.6	-67.1%
<b>Norm. Pre-Tax Profit</b>	<b>A\$m</b>	<b>-1.1</b>	<b>3.2</b>	<b>29.4</b>	<b>23.7</b>	<b>-19.5%</b>	<b>18.6</b>	<b>59.8</b>	<b>222.2%</b>
Norm. Tax Expense	A\$m	0.2	-0.5	-4.7	-3.8	-19.5%	-3.0	-9.6	222.2%
- rate		16.0%	16.0%	16.0%	16.0%	0.0%	16.0%	16.0%	0.0%
Reported Tax Expense	A\$m	0.0	0.0	0.0	0.0	n/a	0.0	-0.5	n/a
<b>Normalised NPAT</b>	<b>A\$m</b>	<b>-0.9</b>	<b>2.7</b>	<b>24.7</b>	<b>19.9</b>	<b>-19.5%</b>	<b>15.6</b>	<b>50.3</b>	<b>222.2%</b>
Abnormal Items	A\$m	-0.2	0.5	4.7	3.8	-19.5%	3.0	9.0	203.8%
Reported Profit	A\$m	-1.1	3.2	29.4	23.7	-19.5%	18.6	59.3	219.2%
Minority	A\$m	0	0	0	0	n/a	0	0	n/a
<b>Profit Attrib</b>	<b>A\$m</b>	<b>-1.1</b>	<b>3.2</b>	<b>29.4</b>	<b>23.7</b>	<b>-19.5%</b>	<b>18.6</b>	<b>59.3</b>	<b>219.2%</b>
capex + exploration	A\$m	-4.2	-11.0	-70.4	-68.4	-2.9%	-108.8	-151.8	39.6%
Net Debt	A\$m	-24.0	-27.6	-8.6	4.8	-155.6%	-65.9	-37.2	-43.6%
Dividends Per Share	cps	-	-	-	-	n/a	-	-	n/a

Source: Hartleys Estimates

12-month price target of \$0.17, which is the offer price.

## PRICE TARGET

Our price target for AVB is 17cps and reflects the current offer price by OZL – 8.5c cash plus 0.009 OZL shares for every AVB share. Every 50c movement in OZL, represents a ~0.5c movement in the offer price for AVB.

Fig. 3: Price Target

Price Target Methodology	Weighting	Spot	12 mth out
NPV base case	0%	\$0.20	\$0.23
NPV at spot commodity and fx prices	0%	\$0.17	\$0.21
Net cash backing	0%	\$0.01	\$0.01
NPV upside (5 yrs added to Antas + Pedra Branca West)	0%	\$0.19	\$0.23
OZL takeover: 8.5c + 0.009 OZL shares	100%	\$0.17	\$0.17
<b>Risk weighted composite</b>		<b>\$0.00</b>	
<b>12 Months Price Target</b>		<b>\$0.17</b>	
Shareprice - Last		\$0.16	
<b>12 mth total return (% to 12mth target )</b>		<b>7%</b>	

Source: Hartleys Estimate

## RISKS

**Fig. 4: Key assumptions and risks for valuation**

Assumption	Risk of not realising assumption	Risk to valuation if assumption is incorrect	Comment
0.7Mtpa Antas, 1.2Mtpa Pedra Branca & 2Mtpa CentroGold	Moderate	Meaningful	AVB is highly leveraged to the success of the Antas Copper project. We model a 0.7Mtpa 'starter' project followed by a 1.2Mtpa project at Pedra Branca. Meanwhile, we model CentroGold commencing operations in CY19. If either project varies from our modelled scenarios our valuation will be at risk to the downside
Model parameters	Moderate	Meaningful	We have made a number of large assumptions in our valuation of AVB, changes in these assumptions can change our valuation to both the upside and downside.
Exploration potential	Moderate	Meaningful	We assume exploration upside at all projects and throughout the region. We believe this assumption is reasonable given the geological prospectively of the world class Carajás province.
Funding	Moderate	High	We model Pedra Branca to be funded with new conventional debt (70%) and equity (30%), and CentroGold to be funded with 60% debt and 40% equity. We believe this assumption is acceptable given the Antas 'starter' project is fully funded.

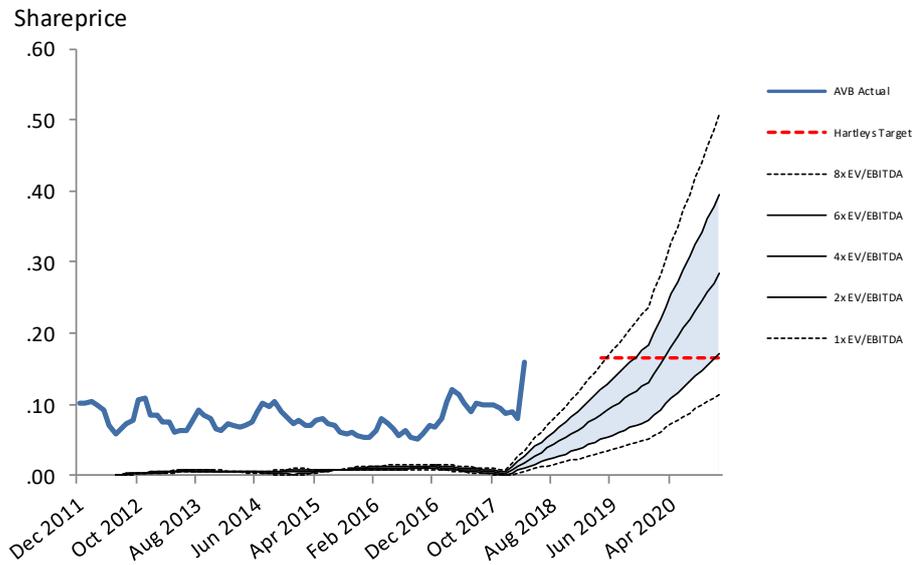
*Conclusion*

*At this early stage we have made significant assumptions but believe these are achievable.*

Source: Hartleys Research

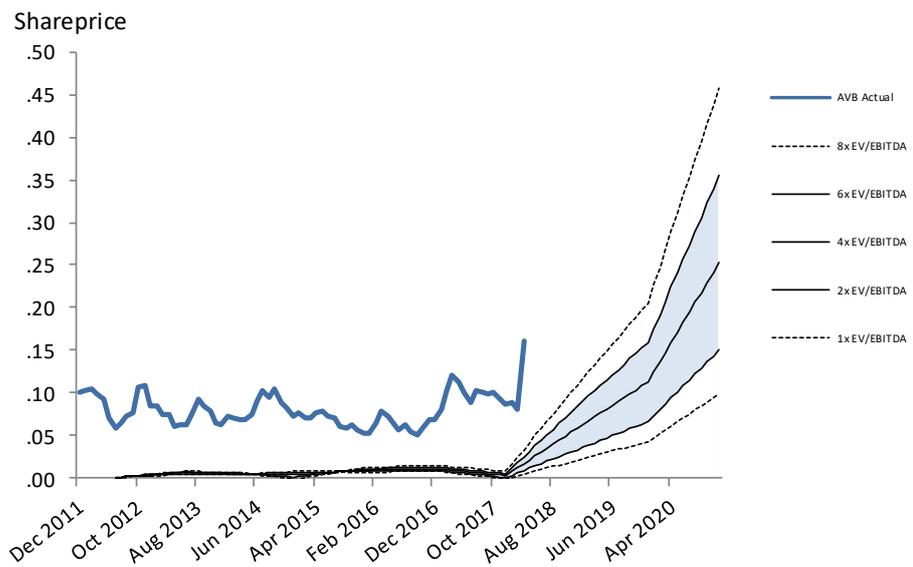
## EV/EBITDA BANDS

**Fig. 5: Using Hartleys base case commodity forecasts**



Source: Hartleys Estimates, IRESS

**Fig. 6: Using spot commodity prices**



Source: Hartleys Estimates, IRESS

# HARTLEYS CORPORATE DIRECTORY

## Research

Trent Barnett	Head of Research	+61 8 9268 3052
Mike Millikan	Resources Analyst	+61 8 9268 2805
John Macdonald	Resources Analyst	+61 8 9268 3020
Paul Howard	Resources Analyst	+61 8 9268 3045
Aiden Bradley	Research Analyst	+61 8 9268 2876
Oliver Stevens	Research Analyst	+61 8 9268 2879
Michael Scantlebury	Junior Analyst	+61 8 9268 2837
Janine Bell	Research Assistant	+61 8 9268 2831

## Corporate Finance

Dale Bryan	Director & Head of Corp Fin.	+61 8 9268 2829
Richard Simpson	Director	+61 8 9268 2824
Ben Crossing	Director	+61 8 9268 3047
Ben Wale	Director	+61 8 9268 3055
Stephen Kite	Director	+61 8 9268 3050
Scott Weir	Director	+61 8 9268 2821
Scott Stephens	Associate Director	+61 8 9268 2819
Rhys Simpson	Associate Director	+61 8 9268 2851

## Registered Office

### Level 6, 141 St Georges Tce Postal Address:

Perth WA 6000 GPO Box 2777  
 Australia Perth WA 6001  
 PH:+61 8 9268 2888 FX: +61 8 9268 2800  
 www.hartleys.com.au info@hartleys.com.au

*Note: personal email addresses of company employees are structured in the following manner: firstname.lastname@hartleys.com.au*

## Hartleys Recommendation Categories

Buy	Share price appreciation anticipated.
Accumulate	Share price appreciation anticipated but the risk/reward is not as attractive as a "Buy". Alternatively, for the share price to rise it may be contingent on the outcome of an uncertain or distant event. Analyst will often indicate a price level at which it may become a "Buy".
Neutral	Take no action. Upside & downside risk/reward is evenly balanced.
Reduce / Take profits	It is anticipated to be unlikely that there will be gains over the investment time horizon but there is a possibility of some price weakness over that period.
Sell	Significant price depreciation anticipated.
No Rating	No recommendation.
Speculative Buy	Share price could be volatile. While it is anticipated that, on a risk/reward basis, an investment is attractive, there is at least one identifiable risk that has a meaningful possibility of occurring, which, if it did occur, could lead to significant share price reduction. Consequently, the investment is considered high risk.

## Institutional Sales

Carrick Ryan	+61 8 9268 2864
Justin Stewart	+61 8 9268 3062
Simon van den Berg	+61 8 9268 2867
Digby Gilmour	+61 8 9268 2814
Veronika Tkacova	+61 8 9268 3053

## Wealth Management

Nicola Bond	+61 8 9268 2840
Bradley Booth	+61 8 9268 2873
Adrian Brant	+61 8 9268 3065
Nathan Bray	+61 8 9268 2874
Sven Burrell	+61 8 9268 2847
Simon Casey	+61 8 9268 2875
Tony Chien	+61 8 9268 2850
Tim Cottee	+61 8 9268 3064
David Cross	+61 8 9268 2860
Nicholas Draper	+61 8 9268 2883
John Featherby	+61 8 9268 2811
Ben Fleay	+61 8 9268 2844
James Gatti	+61 8 9268 3025
John Goodlad	+61 8 9268 2890
Andrew Gribble	+61 8 9268 2842
David Hainsworth	+61 8 9268 3040
Murray Jacob	+61 8 9268 2892
Gavin Lehmann	+61 8 9268 2895
Shane Lehmann	+61 8 9268 2897
Steven Loxley	+61 8 9268 2857
Andrew Macnaughtan	+61 8 9268 2898
Scott Metcalf	+61 8 9268 2807
David Michael	+61 8 9268 2835
Jamie Moullin	+61 8 9268 2856
Chris Munro	+61 8 9268 2858
Michael Munro	+61 8 9268 2820
Ian Parker	+61 8 9268 2810
Matthew Parker	+61 8 9268 2826
Charlie Ransom	+61 8 9268 2868
Mark Sandford	+61 8 9268 3066
David Smyth	+61 8 9268 2839
Greg Soudure	+61 8 9268 2834
Sonya Soudure	+61 8 9268 2865
Dirk Vanderstruyf	+61 8 9268 2855
Samuel Williams	+61 8 9268 3041
Jayne Walsh	+61 8 9268 2828

## Disclaimer/Disclosure

The author of this publication, Hartleys Limited ABN 33 104 195 057 ("Hartleys"), its Directors and their Associates from time to time may hold shares in the security/securities mentioned in this Research document and therefore may benefit from any increase in the price of those securities. Hartleys and its Advisers may earn brokerage, fees, commissions, other benefits or advantages as a result of a transaction arising from any advice mentioned in publications to clients.

Any financial product advice contained in this document is unsolicited general information only. Do not act on this advice without first consulting your investment adviser to determine whether the advice is appropriate for your investment objectives, financial situation and particular needs. Hartleys believes that any information or advice (including any financial product advice) contained in this document is accurate when issued. Hartleys however, does not warrant its accuracy or reliability. Hartleys, its officers, agents and employees exclude all liability whatsoever, in negligence or otherwise, for any loss or damage relating to this document to the full extent permitted by law.