

# Territory Resources Ltd

## (TTY \$0.39) Buy

### Comments

**Price Target:** \$0.61/sh

The board restructure and corporate re-alignment is now clearly focussed on optimising the Frances Ck operation by way of growing production, reducing costs and increasing resources. This is in contrast to the diversified investment strategy of the prior management.

Francis Ck production is now on track to meet the ramp-up schedule of 2.0mtpa rate by end of 2008. The budget for the FY'09 year is 2.0mt at a cash cost of A\$60/t. We understand that production is meeting the schedule which is obviously skewed in volume and costs toward the 2nd H. Production in the Dec Q and beyond will be aided by development of the low W:O ratio ore in the Ochre Hill pit. We anticipate Sep Q production of ~300ktpa.

We continue to estimate iron ore price received at ~A\$90-100/t net. While the spot CIF iron ore price has dropped markedly, this has been partially offset by the weaker currency and lower freight rates. We expect Frances Ck product may eventually secure qualification for benchmark related contracts which may yield more certain pricing.

Territory is planning to spend \$8.5m on exploration during FY'09, and maintains its objective of doubling the resource inventory to 20mt within 2 years. The updated resource and reserve statement shows that ore reserves have grown by 10% to 5.6mt over the year net of mining depletion, ensuring a minimum life of 3 years hereon. Resources have replaced depletion and remain static at 10mt.

Installation of a \$15m wet plant has been deferred as it was unlikely to be available during the upcoming wet season. A smaller mobile wet plant has been secured to augment the existing crushing/screening plant which is expected to maintain production rates throughout the wet season. Other civil works have also been completed in anticipation of the wet season. An \$8m upgrade for stockpile capacity at the port is underway.

It is important to note that the port of Darwin, and the connecting railway line, is not constrained by volume unlike virtually all bulk commodity logistics chains in Australia. Both have the capacity to handle more volume. Accordingly users do not incur demurrage at the Darwin Port. Territory is also lobbying for dredging of the Darwin port to allow more cargo onto the vessels. Currently Panamax ships can load to about 70kt with tidal assistance.

The financial results for FY'08 have shown an underlying loss of \$4.5m on the sales of 640kt of product over the nine months of operation, from \$14m in EBITDA. Writeoffs of \$44m relating to the Monarch and Matilda investments were also recorded. Further impairment of the Matilda investment is flagged following closure of its operations, and future uncertainty of Olympia Resources is also noted by auditors. In total the investments are now a negligible component in our valuation.

Territory's balance sheet shows total borrowings of \$34.7m of which \$26.9m is an unsecured short term loan from Noble. Territory is negotiating to replace this with a larger conventional secured debt facility.

### Investment Case

We are now confident that the new Territory management has set the company on a steady course. Our modelling suggests the company is now profitable and generating cashflow. Some uncertainty will persist until Territory secures the replacement term debt facility.

We forecast territory to make \$26m NPAT in the FY'09 year based on the 2.0mt of sales. The stock is priced at an inexpensive PER of 4x. Our NPV based valuation is \$0.61/sh.

The real driver of value will be through exploration success. The recent ore reserve upgrade while modest was actually ahead of expectations.

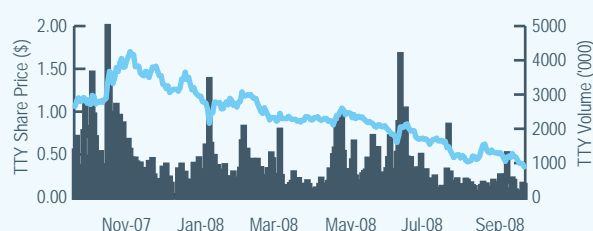
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Top 20 Shareholders		as at 24 September 2008	
Shareholders	Shares (m)	(%)	
1	Crawley Resources Limited	69.99	26.45
2	OM Holdings Limited	29.16	11.02
3	DCM Decometal GMBH	28.18	10.65
4	Zero Nominees Pty Ltd	6.94	2.62
5	Sun Hung Kai Investment Services Ltd	5.00	1.89
6	ANZ Nominees Limited	3.62	1.37
7	Ocj Investment (Australia) + Pty Ltd	3.51	1.33
8	HSBC Custody Nominees (Australia) Ltd	2.85	1.08
9	National Nominees Limited	2.34	0.89
10	UOB Kay Hian Private Limited	1.51	0.57
11	Mr Chunlin Ouyang	1.33	0.50
12	DBS Vickers Securities (Singapore) Pte Ltd	1.25	0.47
13	Tinkler Investments Pty Ltd	1.22	0.46
14	Pegmont Mines Limited	1.00	0.38
15	Mr K Bartley + Mr R Bartley + Mr A Bartley	0.88	0.33
16	Citicorp Nominees Pty Limited	0.86	0.33
17	Mr Phillip Clive Hardcastle	0.85	0.32
18	Mr Keith William Sheppard	0.80	0.30
19	Palazzo Nominees Pty Ltd	0.75	0.28
20	Gibbins Investments Pty Ltd	0.72	0.27
<b>TOTAL</b>		<b>162.77</b>	<b>61.51</b>

### Market Statistics

<b>Share Price</b>	<b>\$0.39 A\$/sh</b>	<b>Directors</b>	
Issued Capital		A Simpson	Chair
FP Ord	264.6 m	A Quadrio	Mg Dir
Opt (@\$0.20/sh)	0.3 m	I McCubbing	NE Dir
Opt (@\$0.25/sh)	0.5 m	R Elman	NE Dir
Opt (@\$0.40/sh)	7.0 m	J Ariti	NE Dir
Opt (@\$0.50/sh)	2.5 m	M Donaldson	NE Dir
Opt (@\$0.60/sh)	1.3 m	F Harris	NE Dir
<b>Total Dil. FPOrd</b>	<b>265.4 m</b>		
Market Capitalisation	\$225 m	<b>Shareholders</b>	
Enterprise Value	\$259 m	OM Holdings	11.0%
Debt	\$35 m	Noble	26.5%
Cash	\$1 m	DECOmetal	10.7%

### Share Price Performance



Resources Quarterly ▶ October 2008

# Territory Resources Ltd

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# EUROZ

SECURITIES LIMITED

AUSTRALIAN RESEARCH

TERRITORY RESOURCES LTD (TTY)		YEAR END 30 JUNE					
		A\$M	A\$/sh				
<b>ASSET VALUATION</b>							
Frances Creek		152	0.57				
Hedging		0	0.00				
Corporate		-10	-0.04				
Residual Value		5	0.02				
Frances Ck Expl'n		30	0.11				
Other FeO Projects		5	0.02				
Investments (excl MON)		8	0.03				
Investments (MON)		0	0.00				
Loan to MON		0	0.00				
Working Capital		6	0.02				
Unpaid Capital		0	0.00				
Debt		-35	-0.13				
Cash		1	0.00				
<b>Total @ 10% nom</b>		<b>162</b>	<b>0.61</b>				
<b>Total @ 0% nom</b>		<b>199</b>	<b>0.75</b>				
<b>Total @ 5% nom</b>		<b>179</b>	<b>0.68</b>				
<b>Total @ 15% nom</b>		<b>148</b>	<b>0.56</b>				
<b>FORECAST PRODUCTION</b>		<b>2008a</b>	<b>Dec H'08f</b>	<b>2009f</b>	<b>2010f</b>	<b>2011f</b>	
<b>Frances Creek (100%)</b>							
Lump Sales	kt	365	510	1,170	1,350	1,200	
Fines Sales	kt	275	340	780	900	800	
<b>Total Fe Ore Sales</b>	<b>kt</b>	<b>640</b>	<b>850</b>	<b>1,950</b>	<b>2,250</b>	<b>2,000</b>	
Total Cash Costs	A\$/t	67	60	60	58	57	
Net Lump Rec'd	US\$/t	88	109	109	106	-	
Net Fines Rec'd	US\$/t	67	51	51	49	-	
B'mark Lump JFY fob	US\$/dmtu	172.4	201.8	102.7	201.8	201.8	
<b>Foreign Exchange</b>							
Avg Rate Ach'd	US\$:A\$	0.90	0.88	0.86	0.85	0.85	
Ass'd Spot Rate	US\$:A\$	0.90	0.83	0.84	0.85	0.85	
<b>RATIO ANALYSIS</b>		<b>2008a</b>	<b>Dec H'08f</b>	<b>2009f</b>	<b>2010f</b>	<b>2011f</b>	
CF (A\$m)		(49.1)	15.3	46.5	56.2	60.9	
CF / Sh (Ac/sh)		(18.5)	5.8	17.6	21.2	23.0	
CF Ratio (x)		(4.6)	-	2.2	1.8	1.7	
Earnings (A\$m)		(3.1)	11.2	26.2	39.5	32.6	
EPS (Ac/sh)		(1.2)	4.2	9.9	14.9	12.3	
EPS Growth (%)		-116%	424%	990%	1494%	1233%	
Earnings Ratio (x)		-	-	3.9	2.6	3.2	
E'prise Val. (A\$m)		259	118	91	44	(17)	
EV : EBITDA (x)		332.9	2.2	1.4	0.5	(0.3)	
EV : EBIT (x)		(27.0)	4.0	2.4	0.8	(0.4)	
Net Debt / ND+Eq (%)		32%	21%	-4%	-59%	-173%	
Interest Cover (x)		-	-	22	(90)	(20)	
EBIT Margin (%)		-15%	0%	19%	25%	23%	
ROE (%)		-4%	13%	25%	28%	18%	
ROA (%)		-7%	11%	28%	33%	21%	
Div. (Ac/sh)		-	-	-	-	-	
Div. payout ratio		0%	0%	0%	0%	0%	
Div. Yield		0.0%	0.0%	0.0%	0.0%	0.0%	
Div. Franking		0%	0%	0%	0%	0%	
<b>PROFIT AND LOSS</b>		<b>2008a</b>	<b>Dec H'08f</b>	<b>2009f</b>	<b>2010f</b>	<b>2011f</b>	
Iron Ore Sales Revenue		58.0	87.9	199.1	220.9	185.3	
Forex Hedging Revenue		-	(4.7)	(5.0)	0.0	0.0	
Interest Revenue		1.5	0.0	0.1	0.8	3.1	
Other Revenue		4.2	-	-	-	-	
<b>TOTAL REVENUE</b>		<b>63.8</b>	<b>83.3</b>	<b>194.1</b>	<b>221.7</b>	<b>188.4</b>	
Operating Costs		46.2	51.0	117.4	130.9	114.5	
Dep/Amort		8.5	8.8	22.1	28.8	24.8	
Corp O/H		15.3	5.0	10.0	4.0	2.0	
Prov/w'off (expl'n)		0.2	0.5	7.0	1.5	0.5	
EBITDA		0.8	27.2	66.6	86.0	68.8	
EBIT		(9.6)	14.9	37.5	55.7	43.5	
Interest Expense		0.7	1.7	3.0	-	-	
NPBT		(8.8)	13.2	34.6	56.5	46.6	
Tax		(5.7)	2.0	8.4	16.9	14.0	
Minority Interest		-	-	-	-	-	
<b>NET PROFIT</b>		<b>(3.1)</b>	<b>11.2</b>	<b>26.2</b>	<b>39.5</b>	<b>32.6</b>	
Net Abnormal Gain/(Loss)		(44.6)	-	-	-	-	
<b>NET PROFIT After Abn'l</b>		<b>(47.7)</b>	<b>11.2</b>	<b>26.2</b>	<b>39.5</b>	<b>32.6</b>	
<b>CASH FLOW</b>		<b>2008a</b>	<b>Dec H'08f</b>	<b>2009f</b>	<b>2010f</b>	<b>2011f</b>	
Net Profit		-3.1	11.2	26.2	39.5	32.6	
+ Working Capital Adjustment		-11.8	1.0	2.0	2.0	5.0	
+ Dep/Amort		8.5	8.8	22.1	28.8	24.8	
+ Provisions / writeoffs (explor)		1.9	3.5	7.0	1.5	0.5	
+ Tax Expense		-5.7	2.0	8.4	16.9	14.0	
- Tax Paid		0.0	-0.8	1.2	16.6	14.0	
Operating Cashflow		-10.1	27.3	64.5	72.2	62.9	
-Capex + Development		39.0	12.0	18.0	16.0	2.0	
-Exploration		2.1	4.0	8.5	8.5	0.0	
-Assets Purchased		76.4	0.0	0.0	0.0	0.0	
+Asset Sales		11.4	0.0	0.0	0.0	0.0	
Investing Cashflow		-106.0	-16.0	-26.5	-24.5	-2.0	
+ Equity Issues		66.5	0.0	0.0	0.0	0.0	
+Loan Drawdown/Receivable		0.0	0.0	0.0	0.0	0.0	
+Loans repaid from/(to) other entities		47.5	0.0	0.0	0.0	0.0	
-Loan Repayment		16.0	10.0	34.7	0.0	0.0	
-Dividends		0.0	0.0	0.0	0.0	0.0	
Financing Cashflow		98.0	-10.0	-34.7	0.0	0.0	
Period Sur (Def)		-18.2	1.3	3.3	47.7	60.9	
Cash Balance		1.1	2.5	4.4	52.1	113.0	
<b>BALANCE SHEET</b>		<b>2008a</b>	<b>Dec H'08f</b>	<b>2009f</b>	<b>2010f</b>	<b>2011f</b>	
<b>Assets</b>							
Cash		1.1	2.5	4.4	52.1	113.0	
Current Receivables		12.2	12.2	12.2	12.2	12.2	
Other Current Assets		20.9	20.9	20.9	20.9	20.9	
Non-Current Assets		102.0	105.2	97.9	85.0	62.3	
<b>Total Assets</b>		<b>136.2</b>	<b>140.7</b>	<b>135.4</b>	<b>170.3</b>	<b>208.3</b>	
<b>Liabilities</b>							
Borrowings		34.7	24.7	0.0	0.0	0.0	
Current Accounts Payable		15.6	15.6	15.6	15.6	15.6	
Other Liabilities		14.4	14.4	14.4	14.4	14.4	
<b>Total Liabilities</b>		<b>64.7</b>	<b>54.7</b>	<b>30.0</b>	<b>30.0</b>	<b>30.0</b>	
<b>Net Assets</b>		<b>71.5</b>	<b>86.0</b>	<b>105.4</b>	<b>140.3</b>	<b>178.3</b>	
<b>RESERVES AND RESOURCES</b>							
		<b>Reserves</b>			<b>Resources</b>		
		<b>mt</b>	<b>Fe</b>	<b>P</b>	<b>mt</b>	<b>Fe</b>	<b>P</b>
Helene 6/7		1.83	61.2%	0.03%	2.45	61.6%	0.04%
Helene 5		1.13	59.0%	0.10%	1.38	59.7%	0.13%
Helene 2/3		0.10	65.2%	0.05%	0.68	62.3%	0.08%
Helene 9		0.15	59.8%	0.13%	0.19	59.6%	0.13%
Helene 11		0.14	60.2%	0.12%	0.18	60.0%	0.14%
Thelma/Rosemary		1.08	61.3%	0.20%	1.34	61.1%	0.21%
Jasmine East		0.71	61.8%	0.07%	1.28	61.0%	0.09%
Ochre Hill		0.47	59.8%	0.11%	1.21	59.8%	0.12%
Millers					1.28	53.2%	0.11%
Surface Fines					0.29	53.6%	0.08%
Others					0.44	58.7%	0.12%
<b>Total</b>		<b>5.6</b>	<b>60.8%</b>	<b>0.10%</b>	<b>10.7</b>	<b>59.6%</b>	<b>0.11%</b>

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