

10 December 2009

Red Rock Resources

Year End	Revenue (£m)	PBT* (£m)	EPS* (p)	DPS (p)	P/E (x)	Yield (%)
06/08	1.3	(0.2)	(0.1)	0.0	N/A	N/A
06/09	0.1	(0.8)	(0.2)	0.0	N/A	N/A
06/10e	6.2	3.8	0.6	0.0	2.3	N/A
06/11e	0.0	(0.8)	(0.2)	0.0	N/A	N/A

Note: *PBT and EPS are normalised, excluding goodwill amortisation and exceptional items.

Investment summary: New Kenyan investment

In a move executed in two stages, Red Rock announced last week that it has taken an effective 35.2% interest in Canada's Kansai Mining Corporation, from which it had previously bought a 15% interest in the Mid-Migori Mining Company for US\$725,000. The investment increases Red Rock's effective interest in Mid-Migori to 44.92% with the potential to rise to 74.08% in the event that Red Rock completes a bankable feasibility study within six years and exercises of its right to take a direct 60% interest in the company.

Deal structure

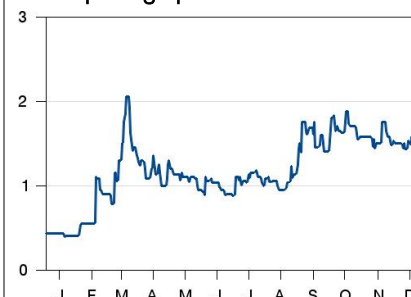
The Kansai deal was effected in two stages. In the first, Red Rock subscribed for 10m shares (an 8.86% stake) in Kansai for a consideration of C\$100,000 – ie C\$0.01 per share. In the second, it acquired an option to purchase an additional 29.629m shares for an option price of C\$360,000 (equivalent to 1.2 cents per share). The option is then exercisable "at any time prior to the earlier of 11 March 2011 or twenty business days after the Kansai Shares become freely tradeable on the Toronto Venture Exchange" for a total consideration of C\$10.

Valuation: Potential 81% discount to NAV

On the basis of its resources of 9,164 measured ounces and 1,229,878 indicated ounces of gold, we have previously put a value of US\$41.3m on the assets of the Mid-Migori Mining Company. We calculate that Red Rock is trading at a discount of at least 30% to its NAV of 2.26p, based purely on the market values of its listed assets. Taking into account its other assets, valued under a variety of circumstances (see over), this NAV has the potential to rise to 8.20p, in which case Red Rock's discount rises to 81%.

Price 1.58p
Market Cap £9m

Share price graph



Share details

Code RRR
Listing AIM
Sector Mining
Shares in issue 542m

Price

52 week High Low
2.1p 0.4p

Balance Sheet as at 31 December 2008

Debt/Equity (%) N/A
NAV per share (p) 1.8
Net cash (£'000s) 49.4

Business

Listed on AIM in July 2005, Red Rock Resources is now a combination of a junior gold explorer and a mineral property investment company focused on the discovery and development of iron ore, manganese, uranium and gold, primarily in Australia and Africa.

Valuation

	2008	2009e	2010e
P/E relative	N/A	18%	N/A
P/CF	N/A	N/A	N/A
EV/Sales	89.3	1.4	N/A
ROE	N/A	31%	N/A

Revenues on geography

UK	Europe	US	Other
2%	0%	0%	98%

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Red Rock's estimated net asset value

Taking into account Red Rock's effective acquisition of a 35.2% stake in Kansai Mining Corporation, our updated valuation of the company in terms of its net asset value is as follows:

Exhibit 1: Red Rock Resources' forecast company balance sheet

Note: * Estimated.

£000's	Worst-case scenario	Low-end scenario	Median scenario	Top-end scenario
Current assets				
Investments in associates				
– Jupiter Mines	11,887	11,887	11,887	23,403
– Resource Star			911	1,195
– Cue Resources	543	543	1,499	2,454
– Kansai		7,488	3,524	3,524
Cash and cash equivalents*		360	360	360
Trade and other receivables		275	275	275
Investments in subsidiaries		964	964	964
Available for sale financial assets*		368	368	368
Exploration properties		3,754	12,107	12,107
Total current assets	12,430	25,639	31,895	44,650
Total assets	12,430	25,639	31,895	44,650
Liabilities				
Trade and other payables	(181)	(181)	(181)	(181)
Total liabilities	(181)	(181)	(181)	(181)
Net assets	12,249	25,458	31,714	44,469
Shares in issue (millions)	542.3	542.3	542.3	542.3
NAV per share (pence)	2.26	4.69	5.85	8.20
Share price discount to NAV (%)	(30.3)	(66.5)	(73.1)	(80.8)

Source: Edison Investment Research estimates

The four scenarios considered above may be summarised as follows:

- The worst-case scenario considers only listed assets, valued at their market values.
- In addition to listed assets, the low-end scenario considers Red Rock's 15% interest in the current Kenyan resource base (under exploration assets) plus its 35.2% interest in Kansai, which has an 85% interest in those same assets; it ascribes no value to its holding in Resource Star.
- The median scenario values Red Rock's holding in Resource Star at 17 Australian cents per share (being the last price at which Red Rock accepted an equity for debt swap relating to its ongoing funding of Resource Star's working capital requirements). It also assumes a 60% direct interest in the Kenyan gold assets (against which US\$8m has been deducted as the estimated expense of the bankable feasibility study), as a result of which Kansai's interest in the same assets has reduced to 40%. The Cue Resources stake has been valued at the mid-point between its market value and our estimate of its value based on its resource base (see below)
- The top-end scenario considers the effect on the Red Rock holding in Jupiter in the event that the Mount Alfred Bonus option is exercised and the maximum number of shares are allocated to Red Rock. Its Cue Resources stake is valued at 15.78% of US\$25.7m (being the value of 9.5m lbs of U₃O₈ indicated and inferred resources at US\$2.70/lb).

Other matters

Exploration

Red Rock has a prodigious amount of historical information relating to its exploration targets in southern Kenya, sourced from (among others) Imperial College. While these are not JORC compliant, they indicate the location of high quality exploration targets and suggest a potential gold inventory at Macalder of 119,736oz (cf the 67,042oz currently reported). As a result, Red Rock is prioritising this exploration at Macalder in particular, focusing on delineating 'measured' ounces in particular in order to maximise the valuation uplift. Note that we value 'measured' ounces at US\$381 each compared to US\$31 for 'indicated' ounces. On this basis, promoting the entire, potential Macalder inventory to JORC-compliant resources in the 'measured' category has the potential to double the value of Red Rock's Kenyan assets with obvious consequences for the NAV calculation above. In addition, the company intends to fly Z-TEM magnetic and gravity surveys (which can penetrate up to 2km down) on 200m lines over the whole area, as soon as practicably possible (ie when the rains permit).

Mount Ida

In addition to its direct interests, there have also been developments at Red Rock's indirect interests – at Mount Ida in particular, at which Jupiter has recently announced the drill hole intersection of magnetite at grades between 20% and 55% Fe. While it is very early stage, a back-of-the-envelope calculation indicates that the total mineralised envelope encompassed by the drill holes could contain of the order of 1.8bn tonnes (which is obviously large). The intersections correlate closely to a previous magnetic survey, which is significant in that previous drilling had focused on haematite, rather than magnetite. In addition to the intersections themselves, preliminary test work suggests that the ore will produce a premium >70% concentrate and that impurity levels are low.

To date, we have taken no account of these results in our valuation of Red Rock. However, insofar as they feed through to the share price of Jupiter, they will eventually have a bearing on Red Rock's net asset value.

Resource Star

Resource Star remains in the process of raising funds prior to re-listing expected on or around 15 January next year. While it accounts for only around 3% of its net asset value, we believe that the successful relisting of Resource Star will improve confidence in Red Rock's assets, while also allowing it to pursue its uranium consolidation strategy with more clarity.

Exhibit 1: Financials

	£'000s	2007	2008	2009	2010e	2011e
		UK GAAP	IFRS	IFRS	IFRS	IFRS
Year end 30 June						
PROFIT & LOSS						
Revenue		535	1,347	68	6,176	0
Cost of Sales		(185)	(1,026)	(108)	(1,590)	0
Gross Profit		350	321	(39)	4,586	0
EBITDA		(310)	(249)	(750)	3,832	(754)
Operating Profit (before GW and except.)		(310)	(249)	(750)	3,832	(754)
Intangible Amortisation		0	0	0	0	0
Exceptionals		85	422	(3)	0	0
Other		0	0	0	0	0
Operating Profit		(225)	173	(753)	3,832	(754)
Net Interest		2	13	(5)	1	0
Profit Before Tax (norm)		(309)	(235)	(755)	3,833	(754)
Profit Before Tax (FRS 3)		(223)	186	(758)	3,833	(754)
Tax		0	0	0	(0)	(0)
Profit After Tax (norm)		(309)	(235)	(755)	3,833	(754)
Profit After Tax (FRS 3)		(223)	186	(758)	3,833	(754)
Average Number of Shares Outstanding (m)		188.2	266.2	389.7	529.9	640.6
EPS - normalised (p)		(0.2)	(0.1)	(0.2)	0.6	(0.2)
EPS - FRS 3 (p)		(0.1)	0.1	(0.2)	0.7	(0.1)
Dividend per share (p)		0.0	0.0	0.0	0.0	0.0
Gross Margin (%)		65.5	23.8	N/A	74.3	N/A
EBITDA Margin (%)		N/A	N/A	N/A	62.0	N/A
Operating Margin (before GW and except.) (%)		N/A	N/A	N/A	62.0	N/A
BALANCE SHEET						
Fixed Assets		0	0	0	0	0
Intangible Assets		0	0	0	0	0
Tangible Assets		0	0	0	0	0
Investments		0	0	0	0	0
Current Assets		2,848	4,364	5,552	10,785	10,616
Stocks		0	0	0	0	0
Debtors		1,080	394	275	508	0
Cash		220	88	49	4	13
Other		1,547	3,883	5,228	10,274	10,602
Current Liabilities		(294)	(413)	(180)	(131)	0
Creditors		(294)	(413)	(180)	(131)	0
Short term borrowings		0	0	0	0	0
Long Term Liabilities		0	0	0	0	0
Long term borrowings		0	0	0	0	0
Other long term liabilities		0	0	0	0	0
Net Assets		2,554	3,951	5,372	10,655	10,616
CASH FLOW						
Operating Cash Flow		(349)	(1,316)	(559)	(974)	(377)
Net Interest		2	13	(5)	1	0
Tax		0	0	0	(0)	(0)
Capex		(260)	(112)	(184)	(837)	(874)
Acquisitions/disposals		0	(11)	(402)	0	0
Financing		727	1,293	1,112	1,764	1,260
Dividends		0	0	0	0	0
Net Cash Flow		119	(133)	(38)	(45)	9
Opening net debt/(cash)		(101)	(220)	(88)	(49)	(4)
HP finance leases initiated		0	0	0	0	0
Other		0	0	0	0	0
Closing net debt/(cash)		(220)	(88)	(49)	(4)	(13)

Source: Red Rock Resources, Edison Investment Research

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