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RED ROCK RESOURCES* **6 October 2016**

BUY*

Price Target 2.8p

(prev. 4.2p on 20/01/16)

Price Data

Share Price:	0.38p
Shares in Issue:	467.3m
Warrants in Issue:	220.8m (ex. 0.8p to 1.625p)
52 Week High/Low	0.70/0.35p

Profile

Market:	AIM - London
Sector:	Resources
Ticker:	RRR.L
Weblink	rrrplc.com

Key Data

Market Cap:	£1.8m
Cash *(est. Oct 16):*	£0.2m
Est Net Asset Value:	£13.3m

Activities

Investment, exploration, development of natural resource projects with a focus on oil, gold, along with manganese and iron ore.

Directors

Andrew Bell (Exec Chairman)
Scott Kaintz (Exec)
Michael Nott (Non-Ex)
Sam Quinn (Non-Ex)

Main Shareholders > 4%

Metal Tiger plc	17.4%
Barclayshare Nom'	12.0%
Hargreave Hale Nom'	7.2%
Huntress (CI) Nom'	4.6%

Est. Valuation Summary

	Oct '16	Jan'16
Kenya	£4.1m	£3.6m
Colombia	£3.3m	£1.7m
Jupiter Mines	£3.2m	£3.5m
Shoats Creek	£1.1m	£0.2m
Greenland	£0.8m	£1.5m
Ivory Coast	£0.3m	£0.3m
Elephant Oil	£0.3m	£0.3m

Dowgate Capital Stockbrokers act as Broker to Red Rock Resources plc.

In this updated note for **Red Rock Resources** (RRR) we have used a similar 'sum of the parts' asset valuation methodology to our previous note (20 Jan '16) to derive a 2.8p value per share, which is a reduced target price (prev. 4.2p) due to dilution from recent equity placings.

Although we use an asset valuation approach, the Group is positioning itself towards generating cash flow from producing assets and investments. The first cash flows are being generated from its Colombia Milling Ltd **royalty interest**, as gold production is ramped up at the facility. Assuming gold at near current levels of US$1,200 per ounce, the royalty interest could provide a cash flow to Red Rock of between US$0.15m and US$0.76m p.a. over the next three years. Another emerging cash flow producing asset is the US onshore **Shoats Creek** oil and gas interest. Net cash flow to RRR from Shoats Creek could be between US$0.20m and US$0.93m p.a. in 2017 and 2018, depending upon how fast or not the field development plan is executed and based on oil prices in the range US$30 to US$50 per barrel. A third, but smaller cash flow source within the next year could come via the 1.2% stake held in Jupiter Mines, which could be on the cusp of paying a dividend, thanks to improved operational performance at its open pit manganese mine in South Africa. Along with these income streams, the Group itself is now on a much better financial footing, following the reduction in plc running costs, with overheads now thought to be at just £30K per month, compared to £100K per month back in 2013. With improved finances and cash flow income, Red Rock could be in a position to self-fund its own asset and project purchases and development, instead of relying upon dilutive equity placings.

The asset with the largest valuation uplift is the Colombian gold mine investments, which we estimate are now worth £3.3m (prev. £1.7m). This includes an estimated discounted royalty value (US$1.9m) and also a risked value for the **promissory note** interest (US$2.28m). The value of the note depends upon the result of current negotiations with CML and Para Resources on whether RRR had the right to convert the note into shares of TSX listed Para Resources and at what price it should be converted. The value of the converted note could be between £1.5m and £2.9m, an amount that could exceed the current market cap of Red Rock Resources.

Another more highly valued asset is the Shoats Creek oil interests, which have increased from £0.2m to £1.1m, due to a higher and more robust oil price of US$40 per barrel (prev. US$25) and more expansive field development plans. We have maintained our licence risk of 30% for the **Kenya** gold project, which has risen in value from £3.68m to £4.06m due to the stronger US dollar. A positive outcome to any judicial review and restoration of title over the properties could eliminate the asset's licence risk.

Our estimated asset valuation has improved by 19% from £11.2m to £13.3m due mainly to the higher valuation for Colombia and Shoats Creek and also the enhanced value of US dollar denominated assets. On a price per share basis, our valuation drops to 2.8p from 4.2p. Nevertheless, a price target of 2.8p represents considerable upside from the current share price of 0.38p. A favourable resolution to the issue regarding the promissory note conversion terms, could move the shares significantly in the short term, as investors re-adjust their assumptions on the Group. To this end we continue to recommend **Red Rock Resources** plc as a '**Buy**'.

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VALUATION RATIONALE

Although the **Shoats Creek** hydrocarbon interests are being pursued to generate cash flow, rather than held as an asset that can be traded in the future, we have valued it on an asset basis to aid our valuation of the Group. The net asset value for RRR's interest in the first 6 wells to be drilled and reworked comes to US$1.38m (prev. US$0.24m for 3 wells), based upon a total CAPEX of around US$600K, oil price of US$40 per barrel, production profile of 10 years with declining production rates, costs per barrel of between $3 and $10 and a discounted cash flow rate of 10%. Net cash flow from Shoats Creek could range from US$0.2m to US$0.9m in 2017 and 2018 p.a. (Table 2) depending upon the field development plan and assuming an oil price in the range US$30 to US$50 per barrel. The valuation does not include any further new wells or additional reworks that could be drilled and exploited on the acreage and in the existing field, which could total up to 16 over the next few years.

The valuation for **Colombia** includes an estimate of outstanding **royalty** amounts due from Colombia Milling Ltd (CML) for production at the El Limon mine, discounted back by 10% p.a, amounting to a total US$1.9m. This is based upon production rising to 15,000 to 25,000 ounces p.a. from 2018, which could provide RRR with a royalty income of US$400K to US$700K p.a., assuming a gold price of US$1,200 per ounce. The value of the **promissory note** consideration depends upon the result of current negotiations with CML and Para Resources on whether RRR had the right to convert the note into shares of TSX listed Para Resources. If the parties agree that RRR should be issued shares in Para Resources, then the equity value will be much higher (US$1.9m to US$3.8m) than the cash obtained from a simple conversion of US$1m of the note. Our analysis (Table 1) considers four possible settlement outcomes, weighted by risk to derive an estimated risked amount of US$2.28m, depending upon when the equity conversion is deemed to have taken place and the exact structure of any settlement.

	Reference Date	**Potential Amount Realisable** Para Shares 23c C$/US$ 1.32	**Risked Probability**	**Risked Amount US$**
Scenario 1	2018 US$1m Promissory Note Repayment	Cash US$0.86m (10% discounted)	20%	$0.17m
Scenario 2	Jan '16 Stake Offer (Equity & Warrants)	US$3.8m	20%	$0.77m
Scenario 3	October '15 Financing (Equity & Warrants)	US$2.9m	20%	$0.58m
Scenario 4	October '15 Financing (Equity Only)	US$1.9m	40%	$0.77m
Risked Total				**US$2.28m**

Table 1: *Promissory note settlement scenarios.*

In **Kenya**, RRR is still seeking to restore its title over the JV gold exploration properties from the Ministry of Mining, upon which we maintain a 30% licence risk. The asset is also risked at the project level at 50% to reflect development risks, and valued on a per ounce discovery basis, according to resource category, as detailed in previous research notes. Due to the strong US$, the asset value has risen from £3.39m to £4.07m. A positive outcome to any judicial review and restoration of title over the properties would lift all or most of our current licence risk factor.

We have reduced our valuation for **Greenland** to £0.8m, which represents 5% of the value Red Rock was offered for its stake of US$20.9m in 2012. Our previous valuation used a higher percentage of 10%, which now appears too high given the lack of interest in the property from potential suitors.

The Group's equity stake value in **Jupiter Mines** has fallen from A$4.25m to A$2.65m, due to a write down in the value of its 49.9% holding in the Tshipi mine following an independent valuation. The Mt Ida royalty value remains unchanged in dollar terms at US$2.04m. The reduction in asset value does understate the improved value of the asset in terms of potential cash flow for Red Rock, as aggressive cost cutting on Jupiter's Tshipi manganese mine and improved resource prices, has raised the prospect of a dividend being paid within the next 6 to 9 months, which we understand could be worth between A$75K and A$225K to Red Rock.

A new asset since our last note, is the stake in AIM listed **GoldStone Resources**, which is valued at the bid price (£0.17m) and also includes a small warrant value of £30K, calculated using the Black Scholes formula. Both the **Ivory Coast** project and investment in private oil and gas company, **Elephant Oil Limited** remains at cost, which comes to £0.25m for each asset.

CASH FLOW SUMMARY

2017 Est. Main Group Cash Flows	Low Case	Base Case	High Case
Shoats Creek Oil Net Royalty Interests	US$198K ($30 p/barrel) Slow field development expansion	US$440K ($40 p/barrel) Planned field development expansion	US$929K ($50 p/barrel) Fast field development expansion
Colombia Gold Net Royalty	US$146K (5,000 oz p.a. prod, gold price $1,000 p/oz)	US$349K (10,000 oz p.a. prod, gold price $1,200 p/oz)	US$757K (20,000 oz p.a. prod, gold price $1,300 p/oz)
Jupiter Mines Dividend	circa A$75,000	circa A$150,000	circa A$225,000
Total	**US$0.40m**	**US$0.90m**	**US$1.86m**

Table 2: *Cash flow estimates for 2017 calendar year.*

Group Valuation Summary

Asset *A$/£1.67* *US$/£1.28*	**A$ or US$ Valuation**	**£ Valuation 6 Oct '16**	**Comments**
Projects			
Kenya	US$5.19m	£4.06m	*Double risked project value (prev. £3.68m)*
Greenland	US$1.05m	£0.82m	*Risked potential sale value - (prev. £1.46m).*
Shoats Creek	US$1.38m	£1.08m	*NPV for initial 6 well development plan, previously valued at cost £0.17m.*
Ivory Coast	US$0.32m	£0.25m	*Project cost to date – Unchanged.*
Investments			
Colombia	US$4.17m	£3.26m	*Present value of estimated royalty and risked value of promissory note (prev. US$2.6m).*
Jupiter Mines Ltd Equity Stake Mt Ida Royalty	 A$2.65m US$2.04m	 £1.59m £1.59m	*Previously A$4.25m equity and US$2.04 royalty value.*
GoldStone Res' Cash Warrants		 £0.17m £0.03m	*New investment, equity and Black Scholes value of warrants.*
Elephant Oil Ltd	US$0.32m	£0.25m	*Recent investment, valued at cost.*
		6 Oct '16 Valuation	*(15 Jan '16 Valuation)*
Sub Total		**£13.09m**	***£11.14m***
Net Cash (Debt)		Cash £0.2m	*(Debt £30K)*
Total		**£13.29m**	***£11.11m***
Shares In Issue		467m	*241.4m*
Share Adjustment for outstanding debt		n/a	*20.0m* *(£80K)*
Combined Shares in Issue Cash adjustment for debt		467.3m **n/a** **£13.29m**	*264.0m* ***£0.08m*** ***£11.19m***
Price per share		**2.8p**	***4.0p***

Table 3: *Group Valuation Summary.*

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DCS act as Broker to Red Rock Resources PLC. DCS private clients and institutional contacts hold shares in Red Rock Resources PLC.