



# Highfield Resources Limited (ASX: HFR)

Speculative Buy

**UPDATE:** Hola Javier, Bienvenido Aboard! PFS Highlights Pamplona Potash Potential

\$0.66

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## Capital Summary

Issued Capital <sup>1</sup> :	200.5m ords
	100.0m perf
	23.3m opts
Share Price (23/07/14)	\$0.66
52 week low/high	\$0.325 / \$0.68
<b>Market Capitalisation</b>	<b>\$132.3m</b>
Market Capitalisation (fully dil.)	\$213.7m
Cash (est.) <sup>1</sup>	\$32.9m
<b>Enterprise Value<sup>2</sup></b>	<b>\$99.5m</b>

<sup>1</sup> Post-placement

<sup>2</sup> Enterprise Value = market cap. + debt – cash

## Directors & Key Management

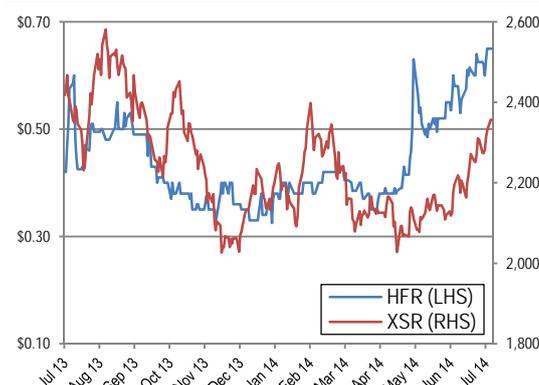
Derek Carter	Non-executive Chairman
Anthony Hall	Managing Director
Pedro Rodriguez	Development Director
Richard Crookes	Non-executive Director
Owen Hegarty	Non-executive Director
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John Claverley	General Manager
Gonzalo Mayoral	Mining Engineer
Helena Mazo	Head Corporate Affairs
Donald Stephens	Company Secretary

## Major Shareholders\*

EMR Capital	65,000,000	32.4%
Derek & Carlsa Carter	5,510,752	2.7%
Raul Hidalgo Fernandez	5,510,752	2.7%
Jose Manuel Prada Fernandez	5,510,752	2.7%
Pedro Rodriguez Fernandez	5,510,752	2.7%

\* Post-placement; Non-diluted; Top 20 Shareholders hold 70.0%.

## Share Price Graph (A\$)



## Our View

Highfield has rapidly advanced the Javier Project to PFS level since its acquisition in June 2012. The experienced, in-country management team has been able to synthesise abundant historical data from the project region and complete new studies on all facets of the proposed mining operation. Development of the Javier Project would be competitive on a global scale when compared to other proposed potash projects, primarily benefiting from established infrastructure in the region, conventional underground mining at relatively shallow depths and cost competitiveness amongst Spanish contractors. In conjunction with high operating margins, the project has the potential to deliver a competitive return on capital. Our 12 month price target based purely on Javier is \$1.18/share (50%-risked). We maintain our recommendation for Highfield Resources as a Speculative Buy.

## Key Points

- Highfield Resources Limited (ASX: HFR) is an advanced exploration company with near-term potash development projects in northern Spain.
- Highfield has three 100%-owned projects located in the potash and halite producing Ebro Basin, near Pamplona.
- All projects are located near existing infrastructure, including grid electricity, gas pipelines, water, highways, rail and an industrial port.
- The Company's Javier Project is the most advanced with a JORC Compliant Mineral Resource of 268Mt @ 11.2% K<sub>2</sub>O (17.8% KCl).
- Highfield has released a Prefeasibility Study ("PFS") on the Javier Project which highlights the economics of developing the project. The PFS was prepared by Highfield with input from Spanish and international consultants and contractors. IDOM, a Spanish-based global engineering company, peer reviewed the PFS.
- The Javier PFS has outlined that ~60% of the resource could be extracted by conventional underground room and pillar mining with access via straight line decline. The ore is suitable for processing by conventional flotation.
- A 4.73Mtpa, 20 year mining operation producing 860ktpa of K60 muriate of potash ("MOP" or "KCl") could be developed with a Capex estimate of €230.8m (US\$307.8m). ~90% of Capex estimates have budget pricing support.
- C3 Opex is estimated at US\$162.48/t MOP.
- Fertiliser markets are being targeted in Brazil and NW Europe.
- Highfield has estimated a post-tax, unlevered NPV<sub>10</sub> of US\$1,061m with an IRR of 48.4%.
- Initial discussions with European commercial banks indicate the likelihood of project financing support.
- Additional economic upside could be generated from salt by-product credits.
- The highly skilled board and management team have in-country experience with mining project development.
- The Company recently completed an over-subscribed Placement, raising ~A\$32m. Funds will be used for ongoing DFS studies at Javier, drilling on all projects, ordering long lead items and working capital.
- Our own DCF modelling of Javier using mining production parameters and Capex estimates outlined in the PFS and our own more conservative estimates on potash sales pricing and C3 Opex, generates a post-tax, unlevered NPV<sub>10</sub> of A\$382.9m (50%-risked) with an IRR of 42.8%. This equates to A\$1.18/share on a fully diluted basis (post-placement).
- Estimated EBITDA of A\$228.7m at steady-state production (FY18). Sector peers currently trade at EV/EBITDA multiples of ~10.4x.

# Overview

Highfield Resources Limited ("*Highfield*" or "*the Company*") has released a Prefeasibility Study ("*PFS*") on its Javier Potash Project ("*Javier*" or "*the Project*") in northern Spain (Fig. 1). The Company proposes to develop, construct and operate a conventional underground potash mine at Javier. Highfield has been able to expedite the PFS since project acquisition in October 2012 by capitalising on abundant historical exploration data acquired on the project area. The PFS was prepared by Highfield's highly experienced in-country management team with support from Spanish and international consultants and contractors. The PFS was peer reviewed by Spanish-based global engineering specialists IDOM.

Potash mineralisation at Javier is composed predominantly of sylvinitic, a mixture of potash (KCl) and salt (NaCl), with negligible amounts of carnallite. Independent geological and mining consultants Agapito Associates Inc ("*Agapito*") have estimated a **JORC Compliant Mineral Resource at Javier of 268.9Mt @ 11.2% K<sub>2</sub>O (17.8% KCl)**. Potash mineralisation is contained within four potash beds over an area of 18km<sup>2</sup>. Agapito also estimated a **high-grade resource component** from 2 potash beds (PAB and P2) from which **154Mt @ 12.9% K<sub>2</sub>O (20.5% KCl)** was identified with a **Measured and Indicated component of 83.3Mt @ 13.3% K<sub>2</sub>O (21.1% KCl)**.

The PFS proposes to access potash mineralisation via a straight line decline and extract it by conventional room and pillar mining methods. An extraction ratio of 60% is assumed. The **base case assumes an extraction rate of 4.73Mtpa of sylvinitic ore** at a constant mining grade of 12.9% K<sub>2</sub>O over a 20 year mine life. Ore would be **processed using conventional flotation producing K60 muriate of potash ("MOP" or "KCl")**. At a recovery rate of 84.6% and 90% plant utilisation, **860ktpa of K60 MOP will be produced over the life of mine**. Production would ramp up from an initial rate of 430ktpa to the full production rate over 18 months. **Equal proportions of granular (compacted) and standard MOP would be produced on site for Brazilian and NW European markets, respectively**. The product would be transported by road and rail to the Port of Bilbao for export, or by road to domestic markets. Salt (NaCl) that is produced as a by-product has not been incorporated into the PFS as sales and marketing strategies have not been sufficiently advanced but offer the opportunity for additional credits if successfully commercialised.

Highfield has estimated **capital expenditure ("Capex") of €230.9m (US\$307.9m)**, including 20% contingency, for the aforementioned operation with budget pricing support for over ~90% of physical costs. This places Javier in the lowest quartile of current proposed global MOP developments at a Capex per annual production rate of US\$358/t. Construction is estimated to take 15 months, commencing in 1H CY15. **An all-in sustaining (C3) operating expenditure ("Opex") of €121/t (US\$162.48/t)** has been estimated. Highfield's DCF modelling of the Javier project generates a **post-tax, unlevered NPV<sub>10</sub> of €796.44 (US\$1,061.9m)** with an IRR of 48.4%. This IRR is the highest of global MOP developments currently proposed. The Company forecast steady state EBITDA in the first full year of production (2018) of €175.8m (US\$234.4m).

Taylor Collison Limited ("*TCL*") DCF modelling of the Javier project, adopting Capex, mining sequence and production rates outlined in the PFS and our own conservative estimates on C3 Opex (US\$176.49/t) and potash sales prices (approx. ~10% that of Integer's), highlight the economic strength of the project. We estimate a **post-tax, unlevered, 50%-risked NPV<sub>10</sub> of A\$382.9m** with an IRR of 42.8%. This equates to an NPV/share of A\$1.18 (*fully dil.*).

**Our valuation has only taken into account the Javier project and extraction of ~90Mt or ~33% of the total Mineral Resource (269Mt) defined. We view there to be realistic upside to our valuation when taking into account the entire Mineral Resource, higher production rates, higher potash price assumptions, potential de-icing salt or high purity salt credits, upgraded Mineral Resource and the progression of feasibility studies on the Pintano and/or Sierra del Perdón Projects. For these reasons, we maintain our Speculative Buy recommendation for Highfield Resources Ltd.**

\* Assuming 323.8m shares on issue (post-placement & fully diluted).

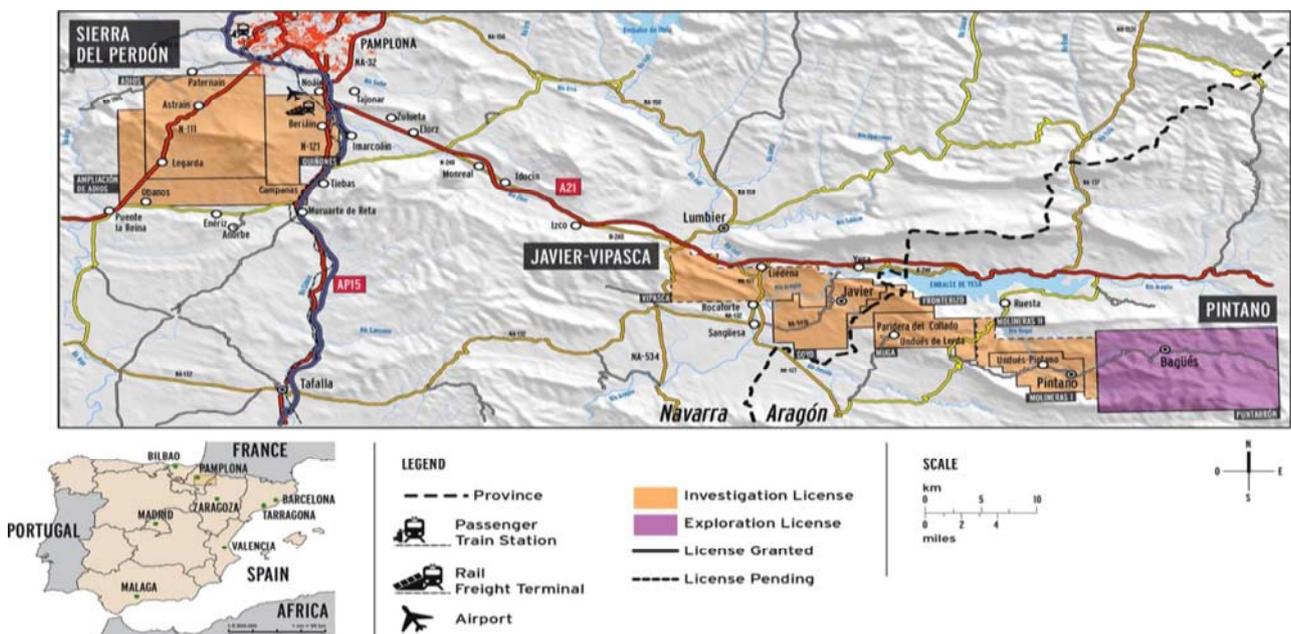


Figure 1. Location map of Highfield's potash projects in northern Spain (Source: Company release).

## Spanish Potash Projects

In June 2012, Highfield announced the option to acquire a 100% interest in potash projects located in northern Spain. The projects are proximal to the northern centre of Pamplona in the Provinces of Navarra and Aragon (*Fig. 1*). Highfield's licences are situated within the Navarra sub-basin of the broader Ebro basin. The Ebro basin hosts numerous potash and salt deposits and prospects and has been mined for these products for several centuries.

Highfield's Spanish Potash Project consists of three distinct projects. The Sierra del Perdon Project includes the former Sierra del Perdon operating potash mine (*Potasas de Navarra and Potasas de Subiza*). The Javier and Pintano Projects are high-quality advanced exploration opportunities adjacent to the Sierra del Perdon project. The Javier Project is the most advanced and the focus of this report.

### Acquisition Terms

As consideration for the acquisition of the Spanish projects, Highfield approved the allotment and issue of the following to KCL Resources Ltd shareholders for 100% interest in the projects:

- (a) 50,000,000 Ordinary Shares for 100% of the Spanish Projects (issued in October 2012);
- (b) 50,000,000 Class A Performance Shares upon successful completion of a JORC Indicated Resource of:
  - (i) 150 million tonnes of potash at or above 13% K<sub>2</sub>O by content; or
  - (ii) 125 million tonnes of potash at or above 14% K<sub>2</sub>O by content; or
  - (iii) 100 million tonnes of potash at or above 15% K<sub>2</sub>O by content; or
  - (iv) 75 million tonnes of potash at or above 17% K<sub>2</sub>O by content; or
  - (v) 50 million tonnes of potash at or above 20% K<sub>2</sub>O by content, on the Navarra Potash Project.
- (c) 50,000,000 Class B Performance Shares upon successful completion of all approvals and utility contracts required to construct and operate a 500,000 tonnes of potash per annum potash mine on the project (including all required Government approvals, water and energy contracts).

TCL assumes the current drilling programme will result in a resource upgrade later in CY14 and the Class A Performance Shares being issued. We also assume the Class B Performance Shares will be issued in late CY15 or early CY16.

### Javier Project

*Javier is 100% owned by Highfield*

The Javier Project is 100% owned by a Spanish subsidiary of Highfield, Geoalcali. Javier covers an area of ~97km<sup>2</sup> and is comprised of 4 permits: Goyo, Fronterizo, Muga and Vipasca. The first three licences are granted Investigation Permits while the final licence is under application. The PFS primarily considers the Goyo and Fronterizo permit areas as this is where the majority of drilling has occurred, the JORC compliant Measured and Indicated Resource defined and where the potash beds are shallowest (*Fig. 2*).

### Historical Exploration

*Extensive historical exploration data exists for the projects*

Highfield has benefited from a substantial amount of historical exploration and mining data collected over its Spanish potash projects. At Javier, ten drill holes and seven seismic lines were completed on the project in the 1980s. Highfield has subsequently completed an additional ten drill holes on the Investigation Permits (*Fig. 2*). These drill holes have confirmed historic intersection thickness and grades and expanded the spatial extent of the prospective sequences. Additional drill holes and seismic profiles are planned in the next 12 months over what is proposed to be the initial mine production area.

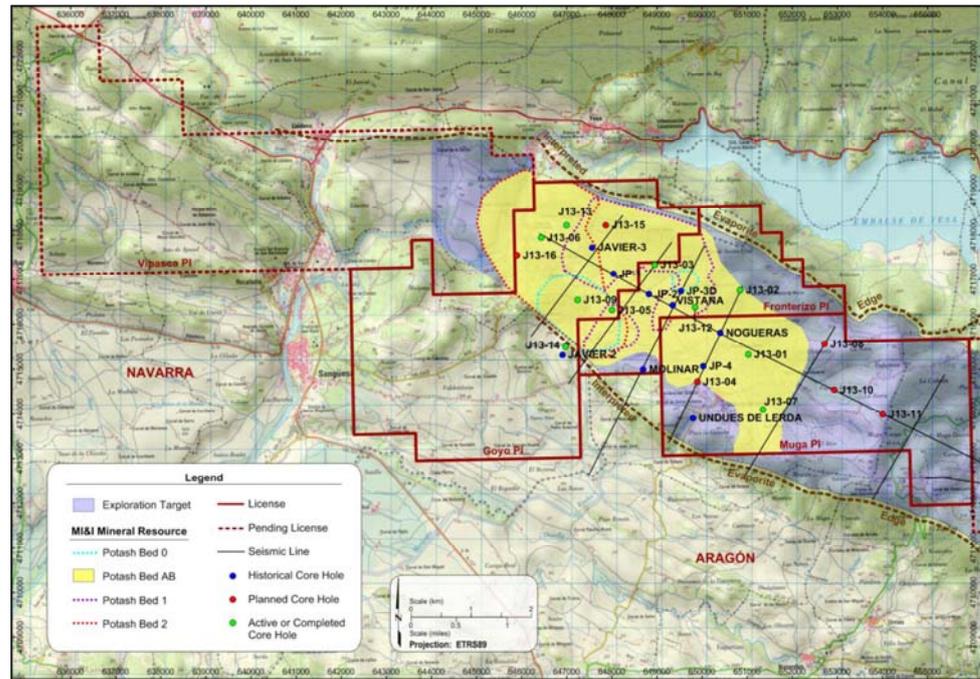


Figure 2. Javier Project location map showing JORC Compliant Mineral Resource Estimate (Source: Company release).

### Updated JORC Resource

*Javier has a JORC Compliant Total Mineral Resource of 268Mt @ 11.2% K<sub>2</sub>O (18% KCl)*

Independent geological and mining consultants Agapito have prepared an updated JORC Compliant Mineral Resource estimate for Javier (Table 1). The Total Mineral Resource is now 268Mt @ 11.2% K<sub>2</sub>O (17.8% KCl) which includes Measured and Indicated Resources of 157Mt @ 11.3% K<sub>2</sub>O (18.0% KCl). This represents a ~65% increase on the Maiden Mineral Resource.

The Mineral Resource occurs in four potash beds over ~18km<sup>2</sup>. Depth from surface to the mineralisation is less than 300m. The JORC Mineral Resource includes a 15% reduction to account for geological uncertainty. Importantly, the resource contains a higher-grade Measured and Indicated component of 83.3Mt @ 13.3% K<sub>2</sub>O (21.1% KCl) within beds PAB and P2. This area could be targeted early in the mine’s life thereby improving the overall economics of the proposed mining operation (Fig. 3).

*Recent drilling continues to highlight resource upside*

Recent drilling has highlighted the resource upside that still exists at Javier. Drill hole J13-07, the first in the Muga permit area, intersected a 4.5m sylvinitic seam at a depth of 282m and J13-08 intersected over 7m of mineralisation at a depth of less than 250m (Fig. 2). Importantly, these drill holes are not included in the recent upgraded Mineral Resource and are ~1.5km and ~2km from the nearest drill hole, respectively. Additional drill holes and seismic studies will be necessary to estimate a Mineral Reserve and final mine design. The Company is encouraged that mineralisation appears to get shallower in the saddle between the Javier and Pintano Projects.

Table 1. Javier JORC Compliant Mineral Resource estimated by Agapito (Source: Company release).

	Potash bed	Tonnes (Mt)	K <sub>2</sub> O (wt%)	KCl (wt%)	MgCl <sub>2</sub> (wt%)	Insolubles
Measured & Indicated	P0	11.9	9.4	14.9	1.62	22.7
	PAB	89.7	11.6	18.4	0.68	16.8
	P1	17.3	9.5	15.1	0.40	13.4
	P2	38.3	12.2	19.3	0.44	8.3
		<b>157.3</b>	<b>11.3</b>	<b>18.0</b>	<b>0.66</b>	<b>14.3</b>
Inferred	P0	5.1	9.1	14.4	1.70	22.4
	PAB	65.1	11.4	18.1	0.73	16.8
	P1	3.4	9.3	14.7	0.38	12.5
	P2	37.6	11.0	17.4	0.42	8.2
		<b>111.3</b>	<b>11.1</b>	<b>17.6</b>	<b>0.66</b>	<b>14.0</b>
Total M+I+I	P0	17.0	9.3	14.8	1.64	22.6
	PAB	154.8	11.5	18.3	0.70	16.3
	P1	20.7	9.5	15.0	0.40	13.3
	P2	75.9	11.6	18.4	0.43	8.3
		<b>268.4</b>	<b>11.2</b>	<b>17.8</b>	<b>0.66</b>	<b>14.2</b>

*Resource has a higher-grade Measured & Indicated component of 83.3Mt @ 13.3% K<sub>2</sub>O (21.1% KCl) across 2 potash beds*

Cut-off: true thickness ≥1.5m; grade cut-off ≥8.0% K<sub>2</sub>O; or true thickness <1.5m; grade-thickness cut-off of ≥12.0 K<sub>2</sub>O-m. Drill hole radii-of-influence (ROI): Measured – 250m; Indicated – 250–1,000m; Inferred – 1,000–2,000m.

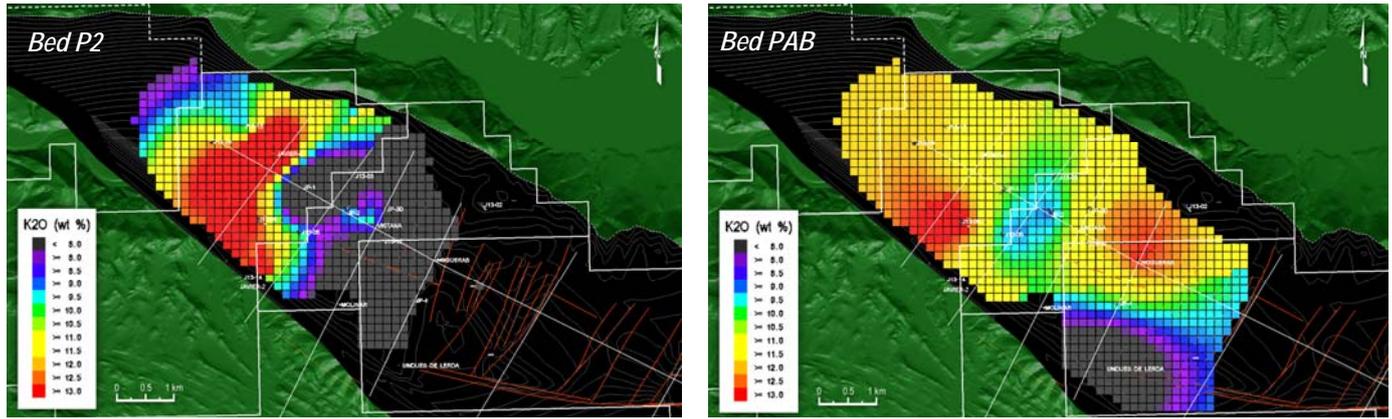


Figure 3. Javier Mineral Resource block model composite K2O grade, plan views. Bed P2 (LHS) and Bed PAB (RHS) (Source: Company release).

**Prefeasibility Study (PFS)**

In May 2014, Highfield released the results of a PFS on its Javier Project which was prepared by the Company with input from local and international consultants and contractors (Table 2). It was also peer reviewed by the Spanish based global engineering firm IDOM. The PFS considered alternative options relating to, but not limited to, mining style (underground conventional vs solution); mineralisation access (decline vs shaft); mine design (room and pillar vs long wall); processing (flotation vs crystallisation); and transport to port (road vs road/rail).

*Javier ore is suited to conventional underground mining and flotation with access via decline.*

The PFS determined that the most suitable extraction method for Javier would be an underground conventional mine accessed via a straight line decline with extraction by room and pillar. Ore would be returned to surface by a conveyer belt and then processed via a flotation circuit producing K60 muriate of potash (MOP or KCl). Potash mineralisation is bounded by thick halite hangingwall and footwall sequences which is positive for mine stability.

Table 2. Summary of key consultants and contractors (Source: Company release).

Component	Organisation	Base
Mining resource estimate	Agapito Associates	USA
Mine engineering	SADIM	ESP
Process engineering	Advanced Mineral Processing	ESP
Process engineering peer review	EngComp	CAN
PFS Peer Review (ex Underground)	IDOM	ESP
Metallurgical testing	AGO Mining	ESP
Assay lab	ALS Global	IRE
Transport study	IDOM	ESP
Environmental studies	Provodit/CRN	ESP
Buildings and facilities	Bovis Lend Lease	ESP
Potash market research	Integer	GBR
Socio economic study	IDOM	ESP

*Domestic and Brazilian markets are being targeted*

The Company is planning on compacting 50% of the MOP into a granular product to target Brazilian markets with the remaining 50% as a standard product targeting NW European markets. Transport of product to Brazil would be by short haul trucking and rail to the Port of Bilbao (total distance of ~300km) and by truck to local markets.

Initial tailings, comprised of salt and clays, would be stored above ground after which open rooms in the underground mine would be back-filled. This would also potentially improve the extraction ratio as tailings would provide additional geotechnical support for mined-out areas. The environmental approval process has also commenced with the memoria resumen (preliminary statement of intent) submitted with regulatory bodies. Additional key studies have also been completed including hydrology, geotechnical and socio-economic impacts. Environmental Approval documents and Mining Concession applications are currently being prepared for submission in Q3 CY14.

### Key Parameters

A summary of the key parameters outlined in the PFS are listed in *Table 3*.

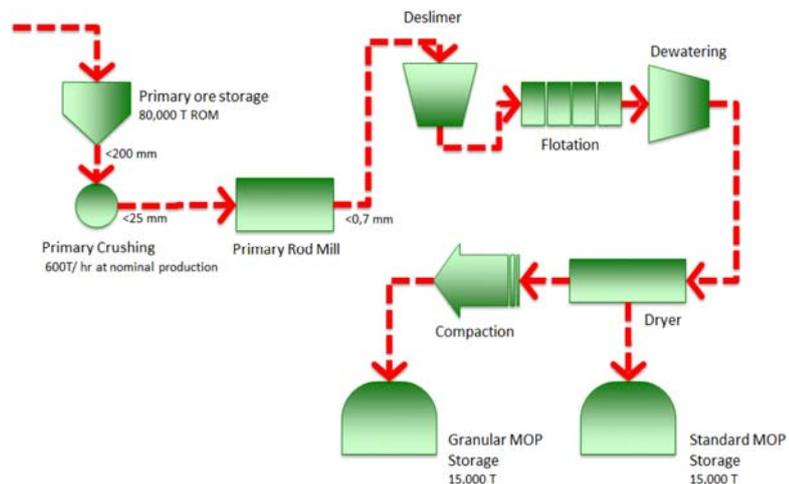
*Table 3. Summary of Javier PFS key parameters (Source: Company release).*

Key Design Elements	Response
Mineralisation	Sylvinitic
Operating assumption	Mine and processing plant as owner operator Transport solution outsourced
Extraction method	Underground conventional room and pillar
Annual ore extraction	4.73 Mtpa
Ramp up	2.365 Mtpa to 4.73 Mtpa over 18 months
Initial mine depth to surface	315m
Mine access	2,100m length decline (15° gradient; 28m <sup>2</sup> section)
Life of mine	20 years
Measured & Indicated Resource	83.3Mt @ 13.3% K <sub>2</sub> O
Inferred Resource	70.7 Mt @ 12.4% K <sub>2</sub> O
Extraction ratio	60%
Average grade	12.9% K <sub>2</sub> O (21.5% KCl product)
Processing method	Conventional flotation
Process plant size	600 tph design capacity (690 tph max.)
Utilisation rate	90% or 7,884 hrs p.a. at 600 tph
Process recovery rate	84.6%
Average annual production (K60)	860kt
Product composition	50% pink K60 granular targeting Brazil markets 50% pink K60 standard targeting NW Europe markets
Logistics solution	50% to Port of Bilbao by 50km road haulage and 205km rail 50% road haulage to domestic market in Spain, France & Portugal
Capital expenditure	US\$307.8m (€230.8m), inclusive of 20% contingency
Sustaining Capex	2% of initial Capex
Rehabilitation/Closure Capex	10% of initial Capex
Operating expenditure	US\$122.31/t K60 MOP (C1), inclusive of 20% contingency US\$162.49/t K60 MOP (C3), inclusive of 20% contingency
Construction time	15 months

### Metallurgy and Processing

*A recovery rate of 84.6% has been estimated*

Preliminary metallurgical test work completed by the University of Barcelona has identified that the ore is suitable for conventional flotation processing. A simple process has been identified whereby potash and salt concentrates could be produced by conventional crushing, grinding, desliming, flotation, dewatering, drying and compaction (*Fig. 4*). The ore has the advantage of containing low levels of carnallite, is relatively coarse in size and has low levels of gangue incursions into the KCl grains. However, the ore is disadvantaged by having relatively high levels of insolubles (clays) which necessitates a desliming circuit prior to flotation. The Company anticipates additional test work conducted as part of the DFS will generate improved recovery rates and lower reagent use. This assumption is based on AGQ Mining's metallurgical test work on a project with similar insoluble contents elsewhere in the Ebro Basin. Based on preliminary metallurgical test work completed to date, a recovery rate of 84.6% has been estimated by EngComp, a Canadian based processing engineering consultant.



*Figure 4. Simple process flow chart (Source: Company release).*

**Logistics & Infrastructure**

Given Spain has First World infrastructure, development of the Javier project would have many advantages over greenfield developments elsewhere in the world. The Company is still assessing the most suitable site for above ground facilities however four 50ha sites have been identified, all of which are within 10km of water, electricity and gas networks (Fig. 5). Highfield proposes to upgrade ~7km of bitumen roads before utilising ~43km of dual-lane highway to the Noain rail freight terminal. It is then ~255km to the Port of Bilbao along an existing rail line.

Energy requirements for the mining operation include electricity, gas, water and telecommunications. Electricity will be accessed from the Spanish grid network and gas for product drying will be accessed from an existing pipeline that transects the project area.

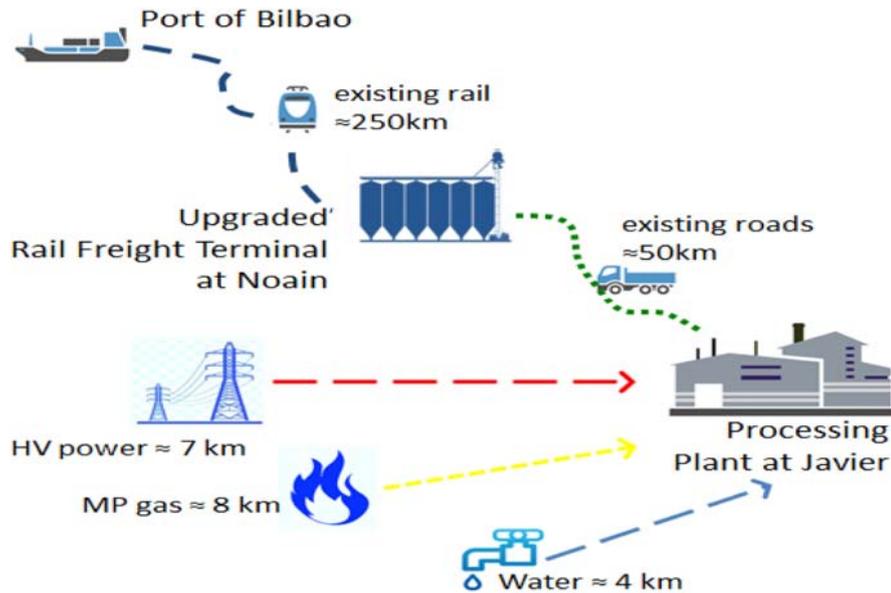


Figure 5. Schematics of utilities and transport solutions for the Javier Project (Source: Company release).

**Capital Expenditure Summary**

Capex is estimated at US\$307.9m

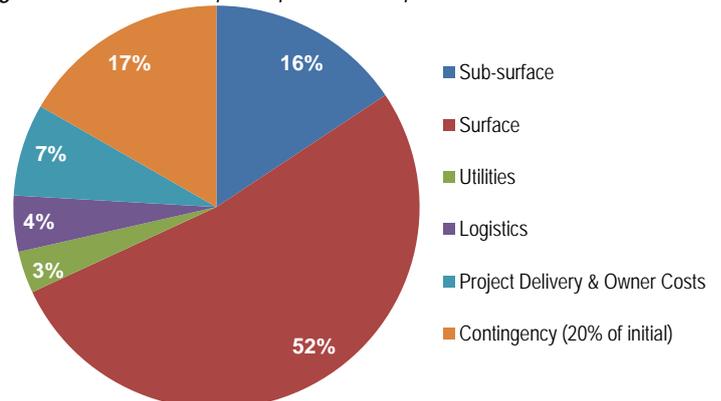
A summary of the capital expenditure items are listed in Table 4 & Fig. 6. Full details are outlined in Appendix A. Capex is estimated at US\$307.9m (CY14 prices), including 20% contingency, with Spanish contractor budget pricing support for ~90% of physical costs (excluding EPCM, owner’s costs and contingency). Underground development assumes straight line decline access to a conventional room and pillar operation. The Capex estimate also includes the first year of galleries required for ore extraction.

The processing plant consists of a conventional flotation circuit with initial capacity of 300tph ramping up to 600tph over an 18 month period. Budget pricing support for the processing plant, which represents ~40% of overall costs, is estimated by the Company to be at a ±15% level to that of final estimates. Associated surface infrastructure includes site works, perimeter protection, a tailings dam for 12 months of production and all required buildings.

Table 4. Summary of capital expenditure from Javier PFS.

Expenditure item	€m	US\$m
Underground development & machinery	36.0	48.1
Process plant & assoc. infrastructure	121.1	161.4
Utilities & logistics	18.2	24.2
<b>Sub-total</b>	<b>175.3</b>	<b>233.7</b>
Mining permits	0.9	1.2
EPCM & owners costs	16.2	21.6
<b>Sub-total</b>	<b>192.4</b>	<b>256.6</b>
Contingency (20% on all costs)	38.5	51.3
<b>Total</b>	<b>230.9</b>	<b>307.9</b>
<b>Pre-production Capex</b>	<b>187.1</b>	<b>249.5</b>

Figure 6. Breakdown of capital expenditure components.



### Operating Expenditure Estimates

A breakdown of estimated operating costs are listed in *Table 5*. Operating costs per tonne of product are listed in *Table 6*. A contingency of 20% has been added to estimated underground, above ground and transport Opex. There is no allowance for royalties as Spain currently does not have a royalty regime (*Source: Company release*).

*Table 5. Summary of operating expenditure (Source: Company release).*

Expenditure item	€/t	US\$/t
Underground operations (per tonne of RoM)	5.69	7.59
Above ground operations (per tonne of RoM)	5.15	6.87
Transport to port (per tonne of product)	16.85	22.47
Contingency (20%)	5.54	7.38
Sustaining capex (per tonne of product)	6.71	8.95
G&A (per tonne of product)	10.00	13.33
Depreciation (per tonne of product)	13.42	17.89

*Table 6. Summary of operating costs per tonne of product (Source: Company release).*

Components	€/t MOP	US\$/t MOP
<b>C1 costs</b>		
- Mining	31.28	41.71
- Processing	28.31	37.75
- Logistics	16.85	22.47
Sub Total	76.45	101.93
- Contingency (20%)	15.29	20.39
Sub Total	91.74	122.31
- G&A	10.00	13.33
- Sustaining Capex	6.71	8.95
<b>Total C1 Costs</b>	<b>108.44</b>	<b>144.59</b>
<b>C2 costs</b>		
- Depreciation	13.42	17.89
- C1 costs	108.44	144.59
<b>Total C2 Costs</b>	<b>121.86</b>	<b>162.48</b>
<b>C3 costs</b>		
- Royalties	-	-
- C2 costs	121.86	162.48
<b>Total C3 Costs</b>	<b>121.86</b>	<b>162.48</b>

C3 Opex is estimated at US\$162.48/t of product

### Potash Price Forecasts

Potash price assumptions utilised in the PFS financial model were prepared by UK based Interger Research Group, a specialist provider with over 10 years experience in research, data, analysis and consultancy services across a range of commodity markets. Potash prices are based on FOB Vancouver references for standard K60 MOP. Marketing costs and shipping costs were also incorporated into net sales prices. Price assumptions are listed in *Table 7* and current as of February 2014.

*Table 7. Potash price assumptions per metric tonne of product (US\$/t, nominal) (Source: Company release).*

	2016	2017	2018	2019	2020
FOB Vancouver Reference	384	398	407	410	408
CIF NW Europe	445	460	471	475	474
CFR Brazil	438	453	463	467	466
Avg. of NW Europe & Brazil	441.50	456.50	467.00	471.00	470.00
Less					
Shipping from Spain to Brazil (50%)	7.96	8.20	8.44	8.69	8.96
Sales Commission (5%)	22.08	22.83	23.35	23.55	23.50
<b>Avg. Net Price</b>	<b>411.47</b>	<b>425.48</b>	<b>435.21</b>	<b>438.76</b>	<b>437.54</b>

Potash sales price assumptions based on FOB Vancouver reference

### Additional Financial Model Assumptions

Additional assumptions utilised in the PFS financial model are listed in *Table 8*.

### Key Financial Metrics

The Company completed a detailed financial model as part of the PFS. Key valuation metrics were calculated on a post-tax, unlevered basis (*Table 9*). Project economics benefit from an accelerated depreciation regime enabling Capex to be depreciated within the first 10 years. Highfield's model

assumes straight line depreciation of 25% p.a. over the first four years. Project economics also benefit from delayed Capex relating to the ramping up of production over 18 months. Based on the financial metrics, the Company's preliminary discussions with European commercial banks suggest the likelihood for project finance support.

*Table 8. Additional financial model assumptions (Source: Company release).*

Assumption	Item
Marketing fee	5% of sales price
Pricing year	2014
Escalation	3% on expenses from 2015 3% on revenue from 2021
Corporate tax rate	30%
Tax depreciation rate	25% p.a. over 4 years
Exchange rate	EUR 0.75:USD 1.00
Remediation costs	10% of full upfront capex escalated

*Javier Project as proposed in the PFS generates a highly attractive return*

*Table 9. Summary of key financial metrics (Source: Company release).*

Metric	Output
Post-tax, unlevered NPV <sub>10</sub>	US\$ 1,062m (€ 796.4m)
IRR	48.4%
EBITDA in 1 <sup>st</sup> year of full prod. (2018)	US\$ 234.4m (€ 175.8m)

*Project economics are most sensitive to potash sales prices*

### **Sensitivity Analysis**

Project economics are most sensitive to potash price assumptions. Economics are less sensitive to Capex due to the low capital intensity.

### **Economic Upside**

The Javier PFS has identified additional economic upside relating to the project but not incorporated into the financial model. Common salt (NaCl) that would be produced as a by-product of MOP recovery could be sold as de-icing salt which currently sells for -€55/t (*Source: K+S Ag company presentation*). Spanish law also enables 15% of tax paid to be applied against future Capex. This would provide upside to the project economics if Highfield were to develop its other potash projects.

*Highfield has commenced work programmes towards completion of a DFS by the end of CY14*

### **Definitive Feasibility Study (DFS)**

Highfield has sufficiently demonstrated the commercial potential of the Javier project such that it has now moved into the preparation of a DFS. Key activities required for completion of the DFS include:

- The completion of an additional six hole drilling programme and up to an additional six hole infill drilling programme.
- The completion of metallurgy tests to inform detailed process plant design and reagent use.
- The acquisition of surface sites.
- Detailed underground engineering including mine planning.
- Lodgement of mining concession application including the Environmental Impact Assessment (EIA).

### **Project Timeline**

The Javier Projects timeline envisages construction commencing early in 2015 and initial production in mid 2016. Major milestones from the Company's base-case scenario include:

- Initial drill programmes assays finalised in Q3 CY14.
- DFS finalised in Q1 CY15.
- Environmental Approval document submitted Q3 CY14 and finalised by Q1 CY15.
- Mining Concession application submitted Q3 CY14 and finalised by Q1 CY15.
- Detailed design and engineering by Q1 CY15.
- Financing programme finalised by Q1 CY15
- Construction commencing Q2 CY15 and completed by Q2 CY16.
- Production of up to 300tph by Q3 CY16.
- Full production up to 600tph by Q1 CY18.

## Board & Management

The Board and Management team are highly experienced in the resource sector, with backgrounds in exploration and mining. Crucially, the Company has a strong proven capability in the mining industry in Spain in the fields of project feasibility and development. The in-country office and management team are adequately equipped to progress the Javier project towards finalisation of the DFS.

## Corporate

In mid-2013, Highfield brought on cornerstone investor EMR Capital (“EMR”), a specialist resources private equity fund manager. EMR’s investment team is led by Owen Hegarty (Chairman) who is supported by well regarded and knowledgeable industry executives Jason Chang (Managing Director) and Richard Crookes (Investment Director). Hegarty and Crookes subsequently accepted Board positions with Highfield. In June 2014, the Company completed an oversubscribed \$32m (65m shares) placement in order to advance the Javier DFS, order long lead items, complete drill programmes across all its projects and supply working capital. Cornerstone and existing shareholder EMR committed to taking \$12.75m (25m shares) thereby increasing its holding in Highfield to 32% (undiluted) and 20% (diluted for performance shares). We welcome the addition of other resource-focused funds to the register and look forward to the Company continuing to strengthen its board and management as Javier is advanced towards development.

*Highfield raised \$32m in June 2014 to fund the Javier DFS and advance its other projects*

## Valuation

TCL has constructed a DCF model for the Javier Project and conducted a peer review of comparable companies in the potash sector to elucidate the potential value of the Company’s Javier Project.

## Discounted Cash Flow

TCL’s base case DCF model for the Javier Project utilises many of the parameters outlined in the PFS in combination with our own assumptions regarding potash sales prices, operating costs, ongoing costs (e.g. exploration) and capital depreciation profile. As a gauge of how variations to the key parameters impact on our financial model, we have also conducted a sensitivity and scenario analysis.

*We estimated a post-tax, unlevered NPV<sub>10</sub> of A\$382.9m (50%-risked) with an IRR of 42.8%*

Assumptions used in our base-case scenario are listed in *Table 10* with key production and cost parameters displayed in *Fig. 7*. Life-of-Mine movements in revenue, EBITDA and NPAT are displayed in *Fig. 8*. The Javier project as modelled generates a post-tax, unlevered, 50%-risked NPV<sub>10</sub> of A\$382.9m or \$1.18/share (*fully diluted*) with an IRR of 42.8%. At the steady-state production rate (FY18), the project as modelled generates EBITDA of A\$228.7m and NPAT A\$152.1m.

Our post-tax NPV estimate varies from that outlined in the PFS primarily due to our adoption of more conservative estimates of real potash sales prices (approximately -10% to that of Integer’s MOP prices in real dollar terms) and a slightly higher C3 Opex estimate to account for ongoing exploration costs and higher freight rates.

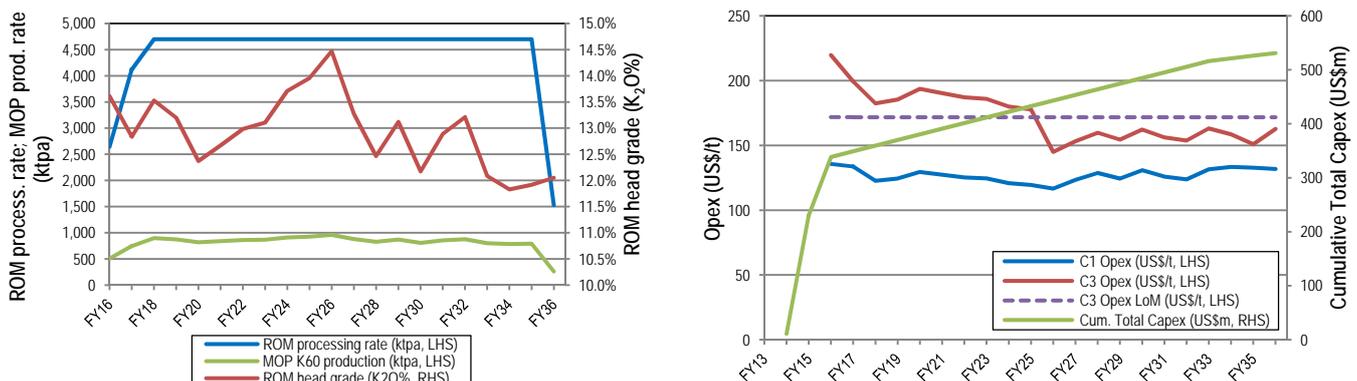


Figure 7. Graphical summary of TCL's DCF life-of-mine parameters for processing and production (LHS) and Capex/Opex (LHS).

Table 10. Summary of key financial metrics used in TCLe base case DCF model.

Mining	2014	2015	2016	2017	2018	2019	2020 <sup>1</sup>
Ore mining rate (Mtpa)			2.64	4.12	4.70	4.70	4.70
Ore grade (K <sub>2</sub> O wt%)			13.6%	12.8%	13.5%	13.2%	12.4%
Life of mine	20 years						

Processing	2014	2015	2016	2017	2018	2019	2020 <sup>1</sup>
Recovery			84.6%	84.6%	84.6%	84.6%	84.6%
MoP K60 concentrate produced (ktpa)			506.6	745.8	896.4	874.7	819.8
Concentrate grade (K <sub>2</sub> O wt%)			60%	60%	60%	60%	60%
Moisture content			8%	8%	8%	8%	8%

Revenue	2014	2015	2016	2017	2018	2019	2020 <sup>1</sup>
Sales price: MoP - CIF NW Europe (US\$/t)			375	380	380	375	366
Sales price: MoP - CFR Brazil (US\$/t)			369	374	374	369	360
Payability			98.5%	98.5%	98.5%	98.5%	98.5%
Shipping (US\$/dmt, Brazil)			17.00	17.00	17.00	17.00	17.00
Shipping (US\$/dmt, NW Europe)			10.00	10.00	10.00	10.00	10.00
USD/EUR	0.77	0.75	0.75	0.75	0.80	0.85	0.85
EUR/AUD	1.43	1.45	1.48	1.41	1.35	1.35	1.35

Capital expenditure	2014	2015	2016	2017	2018	2019	2020 <sup>1</sup>
Exploration & Evaluation (US\$m)	-10.9	-14.7	-5.0	-5.0	-5.0	-5.0	-5.0
Initial Capex, incl. 20% conting. (US\$m)		-205.2	-102.6				
Sustaining capex (US\$m)				-5.8	-5.4	-5.4	-5.4
Rehabilitation & closure (US\$m)							-27.2

<sup>1</sup> 2020 represent long-term values

Operating costs (US\$/t conc., FOB)	LoM
Mining	44.03
Processing	39.84
Transport	23.79
Marketing	17.87
By-product credits	0.00
<b>TOTAL C1 Opex</b>	<b>125.54</b>
D&A	21.47
<b>TOTAL C2 Opex</b>	<b>147.00</b>
Corporate overhead	11.76
Sustaining capex	5.45
Exploration	7.47
Royalties	0.00
Finance interest	0.00
<b>TOTAL C3 Opex</b>	<b>171.69</b>

Finance	
Corporate tax rate	25%
Mining Tax Allowance	15%
NPV discount rate	10%
Depreciation: Initial Capex - straight line	10 yrs

Valuation - Unlevered	
Post-tax NPV <sub>10</sub> (A\$m), 50%-risked	382.9
NPV/share (fully dil.) <sup>2</sup>	1.18
IRR	42.8%
Payback (years)	4.7
EBITDA (steady-state) (A\$m)	228.7
NPAT (steady-state) (A\$m)	152.1

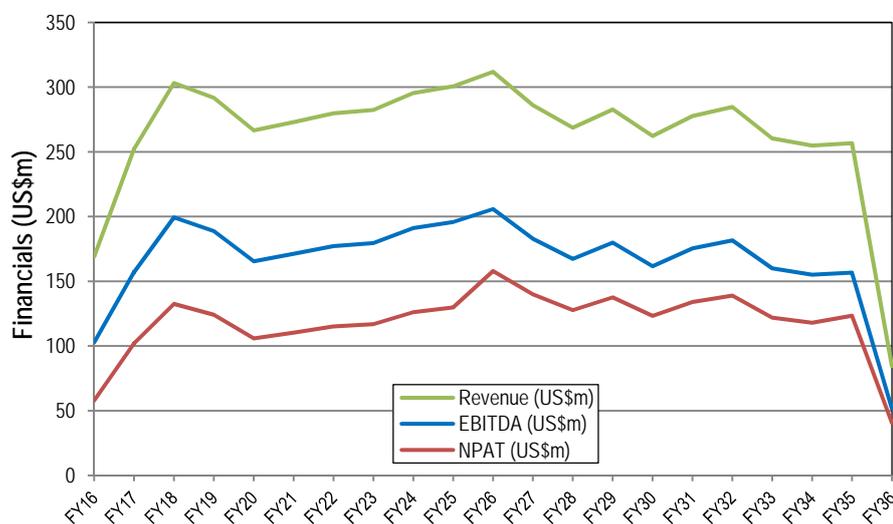
<sup>2</sup> Fully diluted: 323.8m shares on issue

Figure 8. Graphical summary of life-of-mine movements in revenue, EBITDA and NPAT (TCLe, base case).

*Project economics are most sensitive to potash sales price*

### Sensitivity Analysis

Estimates on potash sales price, capital expenditure and operational expenditure were varied by  $\pm 5\%$ ,  $\pm 10\%$  and  $\pm 15\%$  from the TCL base case DCF model. Project economics show the greatest sensitivity to variations in potash sales price, followed by Opex and Capex (Fig. 9).

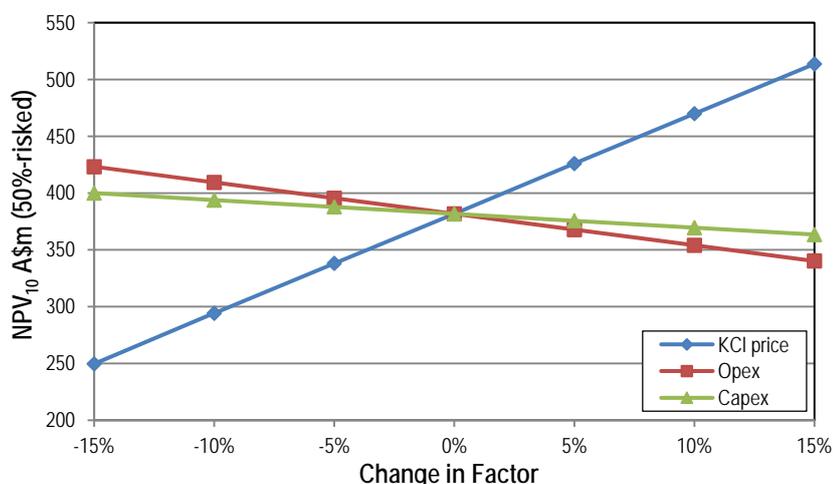


Figure 9. Sensitivity of post-tax, unlevered NPV<sub>10</sub> (50%-risked) to potash sales price, Capex and C1 Opex (TCLe).

### Scenario Analysis

As a gauge to the potential upside (bull case) and downside (bear case) to our base case valuation, we have varied a number of key parameters in our post-tax DCF model. The key parameters for the different scenarios are listed in Table 11. The Javier project economics are robust, even under the bear case scenario. Furthermore, the valuation upside could be significant with higher potash sales prices and lower capital expenditure requirements which we view to be a likely scenario.

Table 11. Scenario analysis for the Javier Potash Project (TCLe).

Parameter	Bear case	Base case	Bull case
MoP K60 LoM prod. rate (ktpa)	851.8	851.8	851.8
De-icing salt LoM prod. rate (ktpa)	-	-	202.3
MoP sales price (US\$/t)	-10%	Table 10	+10%
De-icing salt sales price (€/t)	-	-	40
Operating cost C1 (US\$/t, FOB)	134.5	125.54	122.21
Shipping cost (US\$/dmt)			
NW Europe	+10%	10.00	-10%
Brazil		17.00	
Initial Capex (US\$m)	+10%	307.8	-10%
Sustaining Capex (US\$m/pa)	+10%	-5.4	-10%
Exploration (US\$m/pa)	+10%	5.0	-10%
Rehab./closure Capex (US\$m)	+10%	27.2	-10%
Corporate tax rate (%)	+10%	25	-10%
<b>Key Financials – Post-tax, Unlevered</b>			
NPV <sub>10</sub> A\$m (50%-risked)	239.5	382.9	539.2
NPV/share	0.74	1.18	1.67
# of shares	323.8m	323.8m	323.8m
IRR (%)	30.2	42.8	58.1
Payback (yrs)	5.5	4.7	4.1
FY18 Net Revenue (A\$m)	309.8	347.9	393.8
FY18 EBITDA (A\$m)	178.8	228.7	280.2
FY18 NPAT (A\$m)	107.2	152.1	200.5

*Scenario analysis highlight the economic robustness of the Javier project and its potential economic upside*

### Peer Comparisons

Relative to other global MOP developments proposed, the Javier project is a stand out in terms of Capex per tonne of annual production and IRR (Fig. 10). This highlights the cost competitiveness of the Javier project which is likely to assist with commercial financing discussions.

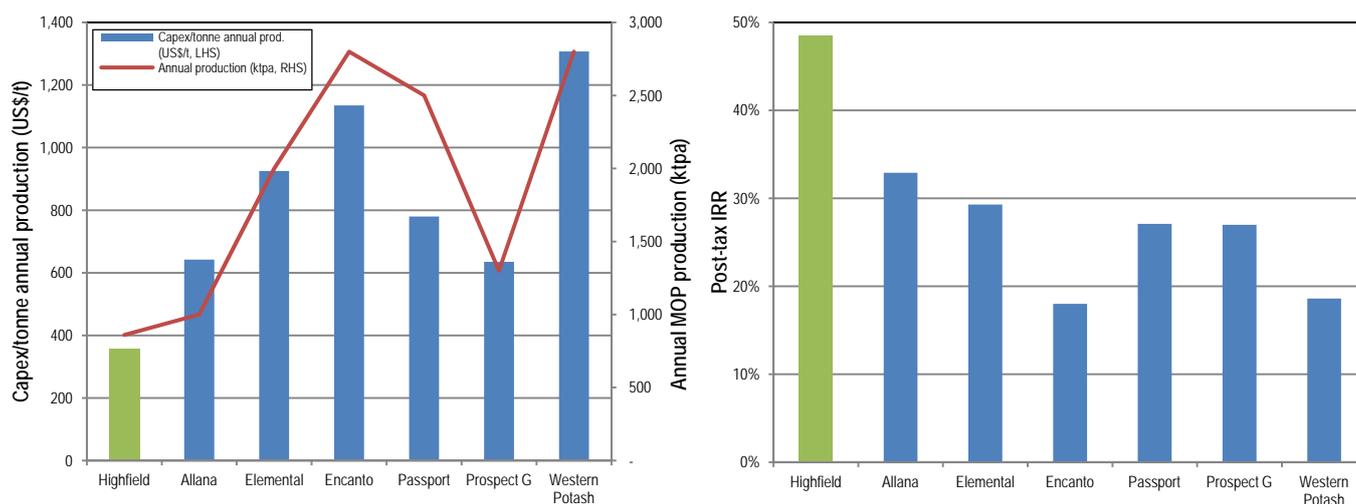


Figure 10. LHS: Company comparison of Capex per tonnes of annual production (US\$/t) and annual MOP production rates for proposed MOP developments (Source: Company releases). RHS: Project IRRs for proposed MOP developments (Source: Company releases).

### Sector Multiples

As a further indication of the potential value that could be realised by Highfield as it reaches steady state production rates in FY18 (896.4ktpa K60 MOP), our base case DCF model generates an EBITDA of A\$228.5m (€169.4m). Global producing peers within the sector currently trade at EV/EBITDA multiples of 7.3x to 14.2x (average ~10.4x) (Table 12). We note that 12 months ago the sector traded at an 8.5x multiple. The increase to its current level is predominantly a function of earnings coming under pressure with the decline in potash price.

Table 12. EV/EBITDA multiples of peers in the sector (Source: <http://www.infinancialsanalytics.com>).

Company	Enterprise Value	EV/EBITDAe
Intrepid Potash	US\$ 1.42b	~14.2
Compass Minerals Int.	US\$ 3.44b	~11.5
K+S Ag	US\$ 7.47b	~7.3
ICL-Israel Chemicals	US\$ 13.27b	~8.8
Potash Corp. of Saskatchewan Inc.	US\$ 34.57b	~11.7
Arab Potash Co	US\$ 2.83b	~11.8
Agrium Inc.	US\$ 15.42b	~7.25
Uralkaliy	US\$ 17.94b	~10.9
<b>Average</b>		<b>~10.4x</b>

Producers in the potash sector currently trade at EV/EBITDA multiples of ~10.4x

A comparison to what Highfield is proposing to produce at its Javier Project is Intrepid Potash, a US\$1,264.7m market capitalised pure potash company listed on the NYSE. In 2013, Intrepid Potash produced ~707kt of MOP and 160kt of Langbeinite (potassium magnesium sulphate). Approximately half of Intrepid's production comes from the Carlsbad West conventional underground mine where the main ore body is located 244–335m below the surface. In 2012, the mill feed grade from Carlsbad West was 11.8% with processing recoveries in the order of 72%.

### Economic Upside

As indicated in the scenario analysis, significant upside to our base case valuation would be realised with the inclusion of de-icing salt sales revenue. Although the de-icing salt market in Spain is limited at ~0.5Mtpa, the Javier Project would produce significant salt volumes as a by-product. Minimal additional Opex would be required to prepare the salt for the de-icing market thereby increasing the overall margins of the proposed operation. Highfield has indicated that salt by-product credits will be incorporated into the Javier DFS.

Considerable upside to our economic valuation has been identified

We have also placed no valuation on Highfield's other projects in the region, namely the Pintano and Sierra del Perdon Projects, as JORC Mineral Resource upgrades and feasibility studies are still to be completed. The Pintano Project is contiguous with the Javier Project and therefore offers the potential for dual or staggered development and substantial scale upside. Furthermore, recent drilling to the southeast of the Javier Mineral Resource area has intersected potash mineralisation. This area offers the immediate opportunity for an expanded Javier Mineral Resource and the potential to increase the target production rate above that outlined in the PFS. Highfield has indicated that the Javier process

plant will be capable of being expanded to accommodate additional production from Pintano should an economic resource be identified. Highfield previously announced a JORC Inferred Mineral Resource at Pintano of 187Mt @ 11.2% K<sub>2</sub>O (17.8% KCl) over ~12km<sup>2</sup> of the projects 125km<sup>2</sup> prospective area. Drilling has commenced at Pintano with the view of expanding the total resource.

## Risks

We consider the main risks to be:

- **Exploration/Geological** – potash accumulations can be disturbed by so-called salt “anomalies” and potentially represents an area which is generally not suitable for mining. Salt anomalies can substantially reduce the thickness and grade of the potash mineralised zone resulting in ore of undesirable composition being fed into the mill. Faulting and other structural geology complexities can affect the potash-bearing units. A combination of seismic reflection studies and examination of drill core is often sufficient in identifying potentially anomalous ground. However, unless extremely detailed (3D) investigations are made, the full lateral extent of anomalies may not be known.
- **Resource/Reserves** – resource/reserve estimates depend on many assumptions that may be inaccurate, which could materially adversely affect the quantities and value of resources/reserves. Given that Highfield’s projects are located in a previously potash producing region, we view the risks associated with establishing a resource(s) to be minimal.
- **Funding** – current macroeconomic conditions may impact on the company’s ability to raise additional funds through equity in the short-term. This may impact on Highfield’s future exploration and development activities. However, given the preliminary economics of the project outlined in the PFS and institutional support for the Company, we do not consider fund raising will be an issue. Furthermore, given that European commercial banks have already expressed interest in the project, we do not consider the debt component of the Capex will be difficult to attain.
- **Mining** – the grade of ore that is mined may vary from projections due to complex geology and mineralogy of potash reserves. This could adversely affect potash production and financial results. In addition, mining is complex and hazardous and can experience production disruptions.
- **Processing** – Magnesium concentrations in excess of 0.25% Mg may decrease the efficiency of potash flotation plants. Preliminary recovery estimates of ~85% indicate that the presence of carnallite does not have a major negative impact on processing. The desliming stage is considered critical, as a virtually slime-free product is necessary to feed the potash flotation stage in order to minimise reagent costs and maximise potash recovery.
- **Marketing** – potash sales are subject to price and demand volatility resulting from periodic imbalances in supply and demand. This may impact on project modelling. Aggressive pricing strategies by competitors could also adversely affect sales and profitability. The seasonal demand for potash products and the consequent variations in cash flows may have an adverse effect on operating results and make the share price volatile.
- **Business** – as a potash-only explorer and potential developer, Highfield is not diversified and a decrease in the demand for potash or an increase in potash supply could have a material adverse effect on its financial condition.
- **Permitting** – any mining development will need the appropriate approvals before construction can commence. Furthermore, changes in laws and regulations may periodically affect the mining industry and changes in enforcement practices could have an adverse effect on operations. Permitting is considered to be the main risk to the development of the Javier Project.
- **Liquidity** – Highfield is a tightly held stock which has an impact on trading. Post-PFS, liquidity has improved and is anticipated to improve further with news flow. The granting of the Performance Shares may improve liquidity, although given that several of the recipients are either part of the Company’s Management team or closely associated with them, it is unlikely that a large proportion of these shares will enter the market.
- **Sovereign Risk** – the current economic circumstances in Spain have resulted in social unrest which may result in government changes in the near future. A change in government may potentially result in delays to exploration and development activities on the projects.

*Attaining the necessary environmental approval and mining permits are considered the main risks*

## Recommendation

*We maintain our recommendation for Highfield Resources as Speculative Buy*

Highfield has demonstrated the economic viability of the Javier Project and shown it could be developed as a conventional underground potash mine and the ore processed via a conventional flotation circuit. The rigorous process the Company has gone through in preparation of the PFS will assist it in advancing the project towards completion of the DFS. The Company has also demonstrated that there is considerable upside to the resource potential of the region and the proposed commercialisation of its resources.

Post-placement, Highfield is adequately funded to complete the Javier DFS and advance its other Spanish Projects. Near-term drivers for share price appreciation include: assay results from drilling on all the projects; developments with environmental approvals and mining permits at Javier; resource upgrades at Javier and Pintano; and finally the Javier DFS in early 2015. Announcements relating to off-take and project financing would also promote a re-rating for Highfield. On the basis of the Javier PFS and our post-tax, unlevered DCF model, **we set a price target of \$1.18/share (fully diluted; 50%-risked) and maintain our recommendation for Highfield Resources as Speculative Buy.**

**Appendix A. Detailed capital expenditure summary (Source: Company release).**

Components	Euros (€m)	USD (US\$m)
<b><i>Underground development</i></b>		
Surface infrastructure	0.647	0.863
Decline construction	6.689	8.919
Primary underground infrastructure	5.653	7.537
Initial ventilation raise	0.706	0.941
Initial services installations	0.639	0.852
Machinery – Phase 1	13.115	17.487
Machinery – Phase 2	4.177	5.569
Machinery – Phase 3	4.422	5.896
<b>Sub-total</b>	<b>36.048</b>	<b>48.064</b>
<b><i>Process plant and associated infrastructure</i></b>		
Processing plant	84.543	112.724
Civil works and site preparation	6.481	8.641
General site infrastructure	4.221	5.628
Storage facility	15.955	21.273
Waste management	9.859	13.145
<b>Sub-total</b>	<b>121.059</b>	<b>161.412</b>
<b><i>Utilities</i></b>		
Electrical supply and installation	5.678	7.571
Natural gas supply and installation	1.068	1.424
Water supply and installation	0.858	1.144
Offsite drainage	0.067	0.089
Telecommunications	0.100	0.133
<b>Sub-total</b>	<b>7.771</b>	<b>10.361</b>
<b><i>Logistics</i></b>		
Road connections to highways	0.930	1.240
Local road improvements	1.482	1.976
Rail freight terminal improvements	0.440	0.587
Rail freight terminal staff accomm.	0.534	0.712
Upgrade to port facilities	7.000	9.333
<b>Sub-total</b>	<b>10.386</b>	<b>13.848</b>
<b><i>Project delivery &amp; owners costs</i></b>		
EPCM	9.213	12.284
Owners costs	7.011	9.347
Permit fees	0.936	1.248
<b>Sub-total</b>	<b>17.160</b>	<b>22.879</b>
<b>Contingency (20%)</b>	<b>38.485</b>	<b>51.313</b>
<b>Total</b>	<b>230.908</b>	<b>307.878</b>

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