Speculative
See key risks on Page 3. Speculative securities may not be suitable for retail clients

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Highfield Resources(HFR)

Sierra del Perdon scoping study

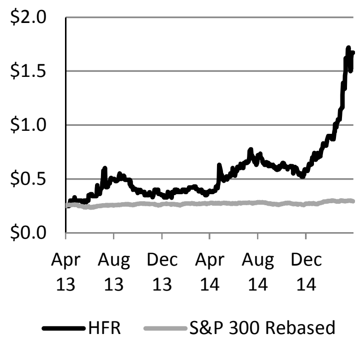
Recommendation
Buy (Buy)
Price
$1.76
Target (12 months)
$2.31 (previously $2.13)
Risk
Speculative

Expected Return	
Capital growth	31%
Dividend yield	0%
Total expected return	31%
Company Data & Ratios	
Enterprise value	$496m
Market cap	$535m
Issued capital	304m
Free float	51%
Avg. daily val. (52wk)	$285k
12 month price range	$0.38-$1.77
GICS sector	Materials

Price Performance

	(1m)	(3m)	(12m)
Price (A$)	1.05	0.73	0.36
Absolute (%)	59.05	130.34	370.42
Rel market (%)	59.18	122.44	362.28

Absolute Price



SOURCE: IRESS

Second project signals potash production basin potential

HFR has released a scoping study for its second potash project, Sierra del Perdon, located approximately 50km from its flagship Muga potash project in northern Spain. The emergence of a second viable project with relatively low CAPEX reinforces the investment thesis of HFR having control of a former potash production basin which may deliver further projects in addition to Muga and Sierra del Perdon.

Sierra del Perdon scoping study results

The scoping study envisages 3.15Mtpa of ore production over a twenty year mine life from an Indicated Resource of 41.8Mt @ 10.7% K_2O and an Inferred Resource of 40.3Mt @ 10.5% K_2O. This will produce 520ktpa of K60 granular potash product for both the European domestic market and for export. Based on CAPEX of US$233m, C3 production costs of US$178/t and FOB Vancouver prices averaging US$376/t over the five years to 2020, the company estimates an NPV of US$527m and IRR of 38.5%.

Reinforces investment case, diversifies risk

The advancement of Sierra del Perdon provides a further positive catalyst for the stock and points to the potential of the former potash production basin that HFR now controls. Although the grades are lower and the returns not as high as for the flagship Muga project, it de-risks the longer term outlook for HFR, opens the way for infrastructure and administration synergies and increases its corporate appeal.

Investment thesis – Speculative Buy (unchanged)

We derive an un-risked NPV for the Sierra del Perdon project of A$430m to which we have applied a risk discount of 80%. This is to account for the early stage of development and the inclusion of Inferred Resources and Exploration Target tonnage estimates in the mine plan. Due to its early stage we do not yet include its cash flows in our forecasts. We increase our otherwise unchanged valuation by $86m or 25cps to $2.31/sh and retain our Buy (Speculative) recommendation.

Earnings Forecast

Year ending 30 June	2015e	2016e	2017e	2018e
Sales (A$m)	-	-	-	208
EBITDA (A$m)	(7)	(14)	(7)	73
NPAT (reported) (A$m)	(5)	(9)	(9)	30
NPAT (adjusted) (A$m)	(5)	(9)	(9)	30
EPS (adjusted) (¢ps)	(2)	(2)	(2)	7
EPS growth (%)	na	na	na	na
PER (x)	(87.5)	(60.4)	(72.0)	21.2
FCF Yield (%)	-2%	-19%	-29%	-3%
EV/EBITDA (x)	(58.9)	(30.8)	(59.8)	5.9
Dividend (¢ps)	-	-	-	-
Yield (%)	0%	0%	0%	0%
Franking (%)	0%	0%	0%	0%
ROE (%)	-50%	-47%	36%	36%

SOURCE: BELL POTTER SECURITIES ESTIMATES

Sierra del Perdon potash project scoping study released

Demonstrates potential for second viable project

The Sierra del Perdon project is located 50km from HFR's flagship Muga project in northern Spain. The emergence of a second viable project with relatively low CAPEX reinforces the investment thesis of HFR having control of a former potash production basin which may deliver further projects in addition to Muga and Sierra del Perdon.

Typically a scoping study works to levels of accuracy of +/-30%-50%. However the recent completion of HFR's Definitive Feasibility Study (DFS) with accuracy levels of +/- 10%-20% and the reliance of the scoping study on some of these inputs the estimates are likely more robust.

Key metrics from the study include:

- An Indicated Resource of 41.8Mt @ 10.7% K_2O and an Inferred Resource of 40.3Mt @ 10.5% K_2O.
- An Exploration Target of 150-350Mt @ 9-14% K_2O.
- As the study assumes mining extraction rates of between 60% and 80% it requires a total mining inventory of 91.9Mt, implying full conversion of Resources to Reserves, plus a contribution from the Exploration Target.
- The mine plan assumes 3.15Mtpa of ore extraction over a 20 year period
- Ore production is matched to processing plant capacity of 3.5Mtpa to produce 520ktpa of K60 granular potash product
- 50% of production is envisaged to be sold to European domestic markets, the remaining 50% for export via Port of Pasajes (100km haul)
- CAPEX US$233m (including 20% contingency)
- C1 cost (mining, processing, transport, G&A, sustaining capital) US$134/t
- C3 cost (incl contingency, D&A, royalties currently zero): US$178/t
- Independent expert spot potash prices discounted by 10% for contract pricing and sales and marketing fees

HFR's financial analysis gives the following results:

- Post tax, unlevered NPV of US$527m (10% discount rate)
- Post tax, unlevered IRR of 38.5%
- EBITDA in first full year of production of US$120 million

Bell Potter valuation

Our Sierra del Perdon NPV of A$430m (un-risked) is based largely on the company's scoping study parameters. However, our assumptions include:

- A more conservative potash price outlook of US$300/t, compared with HFR's estimates of around US$370/t (nominal).
- A 80% risk discount applied to the Sierra del Perdon NPV to take into account resource, permitting and development risks. We will roll this discount off as permitting and development milestones are completed.

Highfield Resources Ltd (HFR)

Company description

HFR is progressing its 100% owned Muga-Vipasca project (Northern Spain) through permitting and a definitive study for development from mid-2015. A PFS supported an 860ktpa (K60) potash project, focused on a high-grade section of the company's 268Mt resource. Permitting and a definitive feasibility for Muga-Vipasca are underway, for project financing and the commencement of development from mid-2015.

Investment thesis – Speculative Buy, valuation $2.32/sh

HFR provides unique leverage to an agricultural linked commodity with a solid demand outlook. The company's key project located in a former potash producing basin in Spain is expected to use conventional mining and processing technologies. HFR controls 100% of the project and its offtake, adding flexibility around financing. Our valuation incorporates risked NPVs of HFR's Muga project, Sierra del Perdon project and corporate overheads. HFR has full control of a former potash producing basin with potential strategic value. HFR is a Speculative investment as it carries significant development risk.

Valuation – risked discounted cash flow of key projects

Our HFR valuation is based on the company's Muga project DFS and Sierra del Perdon scoping study. Our assumptions include:

- A more conservative potash price outlook of US$300/t, compared with HFR's estimates of around US$370/t (nominal).
- A 20% risk discount applied to the Muga NPV to take into account permitting and development risks. We will roll this discount off as permitting and development milestones are completed.
- A 80% risk discount applied to the Sierra del Perdon NPV to take into account resource, permitting and development risks. We will roll this discount off as permitting and development milestones are completed.
- A $155m capital raising at $1.20/sh in mid-2015 to take into account project financing dilution.

Key risks: Permitting, development, operation and marketing

Risks associated with an investment in HFR include, but are not limited to:

- **Government approvals and permitting:** To commence development and operate a mine in Spain, HFR must receive a Mining Concession and Construction Approval. HFR must also maintain its license to operate.
- **Mine and infrastructure development:** Project development is a key risk in terms of time and cost over-runs. Delays and cost over-runs can substantially impact the economic returns of its projects.
- **Mining, processing and logistical activities:** HFR will be mining using conventional underground methods. Underground mining, operating of processing plants and haulage equipment carry risks.
- **Potash markets:** HFR will be exposed to price and volume risk. It will be a price-taker in the global traded market for potash.

- **Offtake relationships:** HFR will likely need an offtake partner to market and distribute its potash products. These arrangements typically carry a level of commercial and working capital risks.
- **Foreign exchange risks:** HFR will have operations in Spain (Euro), likely be selling product in US dollars, and be reporting to Australian investors.
- **Infrastructure access:** HFR's project requires access to infrastructure and purchase agreements with infrastructure providers. Infrastructure includes roads, rail and ports.
- **Sovereign risks:** HFR's assets are located in Spain, the company is listed in Australia and will have customers from a broad range of foreign jurisdictions. HFR is subject to the sovereign risks of those countries.
- **General capital and operating cost fluctuations:** Markets for exploration, development and mining inputs can fluctuate widely and cause significant differences between planned and actual operating and capital costs. Key operating costs are linked to energy and labour markets.
- **Financing and capital management risk:** Financing and capital management includes access to debt and equity finance, maintaining covenants on debt finance, managing dividend payments, and managing debt repayments.
- **Corporate/M&A risk:** Risks associated with M&A activity including differences between the entity's and the market's perception of value associated with completed transactions.

Highfield Resources
as at 21 April 2015

Recommendation	Buy, Speculative
Price	$1.76
Valuation	$2.31

Table 1 - Financial summary

PROFIT AND LOSS

Year ending June	Unit	2014a	2015e	2016e	2017e	2018e
Revenue	$m	-	-	-	-	208
Expense	$m	(6)	(7)	(14)	(7)	(135)
EBITDA	$m	**(6)**	**(7)**	**(14)**	**(7)**	**73**
Depreciation	$m	(0)	(0)	(0)	(0)	(11)
EBIT	$m	(6)	(7)	(14)	(7)	62
Net interest expense	$m	0	1	1	(6)	(14)
PBT	$m	**(6)**	**(7)**	**(13)**	**(13)**	**48**
Tax expense	$m	-	2	4	4	(18)
NPAT	**$m**	**(6)**	**(5)**	**(9)**	**(9)**	**30**

CASH FLOW

Year ending June	Unit	2014a	2015e	2016e	2017e	2018e
OPERATING CASHFLOW						
Receipts	$m	-	1	-	-	197
Payments	$m	(4)	(7)	(6)	(7)	(109)
Tax	$m	-	-	-	-	(6)
Net interest	$m	0	1	1	(6)	(14)
Other	$m	-	-	-	-	-
Operating cash flow	$m	**(4)**	**(5)**	**(5)**	**(13)**	**69**
INVESTING CASHFLOW						
Capex	$m	(0)	(0)	(92)	(167)	(81)
Exploration & evaluation	$m	(4)	(5)	(5)	(5)	(5)
Other	$m	(4)	(5)	(5)	(13)	69
Investing cash flow	$m	**(8)**	**(10)**	**(102)**	**(184)**	**(17)**
FINANCING CASHFLOW						
Share issues/(buy-backs)	$m	14	21	147	-	-
Debt proceeds/(repayments)	$m	-	-	288	-	-
Dividends	$m	-	-	-	-	-
Other	$m	-	-	-	-	-
Financing cash flow	$m	**14**	**21**	**435**	**-**	**-**
Change in cash	$m	5	11	333	(184)	(17)

BALANCE SHEET

Year ending June	Unit	2014a	2015e	2016e	2017e	2018e
ASSETS						
Cash & short term investments	$m	12	23	356	172	155
Accounts receivable	$m	1	0	0	0	10
Property, plant & equipment	$m	0	0	92	259	328
Exploration & evaluation	$m	37	42	47	52	57
Other	$m	2	4	8	12	-
Total assets	$m	**53**	**70**	**503**	**495**	**551**
LIABILITIES						
Accounts payable	$m	2	1	1	1	27
Borrowings	$m	-	-	288	288	288
Other	$m	-	-	-	-	-
Total liabilities	$m	**2**	**1**	**289**	**289**	**315**
SHAREHOLDER'S EQUITY						
Share capital	$m	35	57	212	212	212
Reserves	$m	25	25	25	25	25
Retained earnings	$m	(9)	(14)	(23)	(32)	(2)
Total equity	$m	**51**	**68**	**214**	**205**	**236**
Weighted average shares	m	236	278	365	430	430

CAPITAL STRUCTURE

Shares on issue	m	203.5
Performance shares	m	100.0
Total shares on issue	**m**	**303.5**
Share price	**$/sh**	**1.72**
Market capitalisation	$m	520.5
Net cash	$m	25.0
Enterprise value (undiluted)	**$m**	**495.5**
Options (in the money)	m	43.5
Issued shares (diluted for options)	m	347.0
Market capitalisation (diluted)	m	595.1
Net cash + options	$m	50.4
Enterprise value (diluted)	**$m**	**544.7**

MAJOR SHAREHOLDERS

	%	m
Spanish in-country management	21%	63.7
Australian based management	8%	24.3
EMR Capital	20%	60.7
Other shareholders	51%	154.8
Total	100%	303.5

FINANCIAL RATIOS

Year ending June	Unit	2014a	2015e	2016e	2017e	2018e
VALUATION						
NPAT	$m	(6)	(5)	(9)	(9)	30
Reported EPS	c/sh	(2)	(2)	(2)	(2)	7
EPS growth	%	na	na	na	na	na
PER	x	-73.2x	-100.1x	-69.1x	-82.3x	24.2x
DPS	c/sh	-	-	-	-	-
Franking	%	0%	0%	0%	0%	0%
Yield	%	0%	0%	0%	0%	0%
FCF/share	c/sh	(0)	(0)	(0)	(0)	(0)
P/FCFPS	x	-47.7x	-47.6x	-6.1x	-4.0x	-43.5x
EV/EBITDA	x	-87.2x	-67.8x	-35.5x	-68.8x	6.8x
EBITDA margin	%	0%	0%	0%	0%	35%
EBIT margin	%	0%	0%	0%	0%	30%
Return on assets	%	-13%	-8%	-3%	-2%	6%
Return on equity	%	-29%	-50%	-47%	36%	36%
LIQUIDITY & LEVERAGE						
Net debt (cash)	$m	(12)	(23)	(68)	116	133
ND / E	%	-23%	-33%	-32%	57%	57%
ND / (ND + E)	%	-29%	-50%	-47%	36%	36%
EBITDA / Interest	x	-33.0x	-14.0x	-13.7x	1.3x	-5.3x

RESOURCE

Javier-Vipasca	Mt	K2O %	KCl %	K2O Mt	KCl Mt
Total resource	**269**	**11.2**	**17.8**	**30.1**	**47.9**
Measured	17	11.3	17.9	2.0	3.1
Indicated	140	11.3	18.0	15.8	25.2
Inferred	111	11.1	17.6	12.4	19.6
High grade resource	**154**	**12.9**	**20.5**	**19.9**	**31.6**
Measured	9	13.0	20.7	1.2	1.9
Indicated	74	13.4	21.2	9.9	15.7
Inferred	71	12.4	19.8	8.8	14.0

PROJECT ASSUMPTIONS

Year ending June		2016e	2017e	2018e	2019e	2020e
Currency	US$/A$	0.85	0.85	0.85	0.85	0.85
Potash FOB Vancouver (MOP/KCL)	US$/t	300	300	300	300	300
Potash price realised (FOB Spain)	US$/t	314	314	314	316	316
C1 costs	US$/t		114	117	120	123
Project EBITDA	US$m		0	69	176	217
Mined / milled	Mt		-	3	5	6
Grade	%		13%	13%	13%	13%
Recovery	%		84%	84%	84%	84%
Product grade	%		60%	60%	60%	60%
Production (MOP / K60)	**kt**		**0**	**562**	**898**	**1,123**

VALUATION

Ordinary shares m		252
Performance shares m		52
Options in the money m		44
Diluted m		**347**
	$m	**$/sh**
Muga (risk discount 20%, NPV10)	917	2.64
SdPerdon (risk discount 80%, NPV10)	86	0.25
Corporate overheads	(107)	(0.31)
Total	896	2.58
Cash & options	50	0.15
Total	946	2.73

Project capital raising assumption	
Project capital requirement US$m	354
Project capital requirement A$m	443
Equity / (Debt + Equity) %	35%
Debt requirement $m	288
Equity requirement $m	**155**
Share issue price $/sh	**1.20**
New shares issued m	129
Diluted shares on issue m	**476**

Cash & options	205	0.43
Total	**1,101**	**2.31**

SOURCE: BELL POTTER SECURITIES ESTIMATES

Recommendation structure

Buy: Expect >15% total return on a 12 month view. For stocks regarded as 'Speculative' a return of >30% is expected.

Hold: Expect total return between -5% and 15% on a 12 month view

Sell: Expect <-5% total return on a 12 month view

Speculative Investments are either start-up enterprises with nil or only prospective operations or recently commenced operations with only forecast cash flows, or companies that have commenced operations or have been in operation for some time but have only forecast cash flows and/or a stressed balance sheet.

Such investments may carry an exceptionally high level of capital risk and volatility of returns.

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