

## Austock Securities - Research

<b>Event:</b>	Baosteel to take 15% of AQA Funding options now become available, providing a catalyst for value to be recognised The Strategic Co-operation agreement between the two companies should help accelerate the development of many of AQA's projects in coking coal, iron ore and manganese
<b>Impact:</b>	Our share price target has been almost doubled to \$11.0/share. This represents halfway between our risked valuation of \$8.70/share and our unrisksed valuation of \$13.30/share (adjusted for the dilution of the new shares).
<b>Recommendation:</b>	Buy (from Hold)

### Aquila Resources (AQA) - \$7.20

- Subject to approvals AQA plans to issue 43.95 million shares at \$6.50/share to Baosteel. In the process raising \$285.6m. Baosteel will end up with 15% of Aquila.
- The deal is very important as it helps provide the financing pathway for a host of good quality coking coal projects in the Bowen Basin and Iron Ore in WA.
- It therefore reduces that funding uncertainty that has been over-hanging the stock.
- Under the Strategic Co-operation Agreement AQA could offer Baosteel direct equity in properties such as 100% owned Washpool in the Bowen Basin. Baosteel is also a logical partner in the development of the West Pilbara iron ore assets that total almost 600mt of resources grading 57% iron and are approximately 40% owned by AQA and 40% by AMCI who have been attempting to sell their share.
- We valued the company on a risked basis at \$9.15/share. After the issue of new shares and the injection of \$286m of funds into the business this will be diluted to ~ \$8.70/share.
- On an unrisksed basis, for example assuming low cost and readily available debt from Chinese banks, we can see a case for a valuation of \$13.30/share, diluted for the new shares.
- FIRB and Chinese regulatory approvals will be required. We do not envisage any show stoppers.
- We note, if any corporate play were to be made on AQA we expect the Baosteel deal to provide the trigger: although it would be hard to beat the myriad of financing and marketing advantages that the Baosteel deal offers.

- Any new major player would want to make a move before Baosteel got approval to go to 15%. BHP and RIO are most probably fully focused on the Pilbara JV deal. Vale could be a possibility. Xstrata and Anglo American are probably preoccupied with their own corporate tussle. So while a corporate move is not highly likely we would nevertheless be reluctant to dismiss the possibility. The AQA directors are having a bet each way. There is a break fee of ~ \$2.85m in the event a third party control transaction is publicly announced and recommended by a majority of Aquila's directors before the completion of the placement.
- For more company background/details see page 118 of the Austock Quarterly or attachment.

Should you have any queries, please do not hesitate to contact me on 02 9233 9603.

Regards

**Tim Gerrard**

Analyst

31/08/09

Earnings pre Baosteel placement

Y/e Jun (\$m)	FY'08A	FY'09F	FY'10F	FY'11F
Revenue	46.5	93.3	108.0	149.4
EBITDA	(27.2)	(9.8)	(7.0)	37.9
EBIT	(36.2)	(18.8)	(21.0)	19.4
NPAT (reported)	(5.5)	(5.5)	(12.8)	5.6
NPAT (adjusted)	(8.0)	(8.0)	(12.8)	5.6
Adjusted EPS (cps)	(9.9)	(1.3)	(3.0)	3.7
EPS Growth (%)	-62.6%	87.3%	->100.0	+>100.0
DPS (c)	-	-	-	-
Dividend Yield (%)	0.0%	0.0%	0.0%	0.0%
PE adj. (x)	->50.0	->50.0	->50.0	+>50.0
EV / EBITDA (x)	->50.0	->50.0	->50.0	60.7
EV / EBIT (x)	->50.0	->50.0	->50.0	118.6
Gearing (%)	-245.8%	-67.3%	-3.9%	82.2%
EBIT Margin (%)	-77.8%	-20.2%	-19.5%	13.0%
Interest Cover (x)	>50	>50	>50	2.3

## **Recommendation Criteria**

### **Investment View**

Austock Securities Investment View is based on an absolute 1-year total return equal to capital appreciation plus yield.

<b>Buy</b>	<b>Hold</b>	<b>Sell</b>
> 20%	20% - 5%	< 5%

A Speculative recommendation is when a company has limited experience from which to derive a fundamental investment view.

### **Risk Rating**

Austock Securities Limited has a four tier Risk Rating System consisting of: Very High, High, Medium and Low. The Risk Rating is a subjective rating based on: Management Track Record, Forecasting Risk, Industry Risk and Financial Risk including cash flow analysis.

### **Disclosure of Economic Interests**

The views expressed in this research report accurately reflect the personal views of Tim Gerrard about the subject issuer and its securities Tim Gerrard. No part of the analyst's compensation was, is or will be directly or indirectly related to any recommendation or view expressed in this report.

In addition, Tim Gerrard certifies that none of the following persons holds an economic interest in the securities covered in this report or other securities issued by the subject issuer which may influence the report:

- the author of this report;
- a member of the immediate family of the author of this report ;
- Austock Securities Limited;
- an associate of Austock Securities Limited within the meaning of the Corporations Act.

### **Disclaimer/Disclosure**

This publication has been prepared solely for the information of the particular person to whom it was supplied by Austock Securities Limited ("Austock") AFSL 244410. This publication contains general securities advice. In preparing the advice, Austock has not taken into account the investment objectives, financial situation and particular needs of any particular person. Before making an investment decision on the basis of this advice, you need to consider, with or without the assistance of a securities adviser, whether the advice in this publication is appropriate in light of your particular investment needs, objectives and financial situation. Austock and its associates within the meaning of the Corporations Act may hold securities in the companies referred to in this publication. Austock believes that the advice and information herein is accurate and reliable, but no warranties of accuracy, reliability or completeness are given (except insofar as liability under any statute cannot be excluded). No responsibility for any errors or omissions or any negligence is accepted by Austock or any of its directors, employees or agents. This publication must not be distributed to retail investors outside of Australia.

### **Disclosure of Corporate Involvement**

Austock Securities Limited has not in the previous 12 months been involved in a publicly-announced transaction involving the payment of a fee to Austock Securities Limited by the corporate issuer described in this report. Austock Securities does and seeks to do business with companies covered in its research.

**Austock Securities reports are available on Bloomberg, Reuters, FactSet, Capital IQ and [www.austock.com](http://www.austock.com)**