

ROYALCO RESOURCES (RCO) IMMEDIATE CASH FLOW FROM REEFTON

Recommendation

Short Term: Spec Buy
Long Term: Outperform
Price: \$0.63
Date: 15th Jan 2007

RCO is set to reap significant cashflows from a royalty it holds over Oceana Gold's (OGD) Reefton Gold project located on the South Island of New Zealand. RCO offers the balance of a royalty bank with identifiable future cash flows from three mining operations and a highly prospective exploration land package in the Philippines.

Capital Profile

ASX Code:	RCO
Issued Capital:	56.4m
Market Cap:	\$34m
Cash:	\$10m
Debt:	\$0m

Augmenting raised funds with royalty streams ensures a well funded ongoing exploration programme and significantly reduces the need to raise further capital for early stage exploration. Royalties are generally low risk as they are based on revenues, not profits. Based on our commodity price assumptions we envisage that RCO will be able to build a significant cash position over time.

Website: www.royalco.com.au

KEY POINTS

Royalco's Board:

Peter Topham: Executive Chairman
David Ogg: Chief Financial Officer
Tom Eadie: Non executive director
Adam Boyd: Non executive director
Peter Lester: Non executive director

- Royalty revenues are expected to commence from Oceana Gold's (ASX code: OGD) Reefton mine in mid 2007 post a 6 month grace period. This royalty is particularly attractive as it is based on the NZ\$ gold price and commencement of production and is not sensitive to profits or revenues.
- Total identifiable royalties to RCO from Reefton are estimated to be A\$24m based on existing reserves and our gold price assumptions.
- RCO holds royalty rights over 10 properties of which 3 have projected cash flows. We calculate a base valuation for RCO of 54cps incorporating the 3 project royalties and the current cash position alone.
- The benefits of royalties to RCO include:
 - Low performance risk as they are based on revenues, not profits,
 - The operator's propensity to optimize mine life and metal recoveries,
 - No requirement of the royalty holder to fund further capital expenditure,
 - Leverage to metal price movements,
 - Minimizes the chance of future RCO shareholder dilution
- RCO has a significant portfolio of prospective exploration assets in the Philippines and RCO's exploration activities are expected to ramp up significantly over the course of 2007. The Philippines has a high level of mineral endowment and the political environment for exploring & mining has improved remarkably over the last 2 years which means there is a stronger chance of recapturing its former eminence as one of the world's top mineral producers.

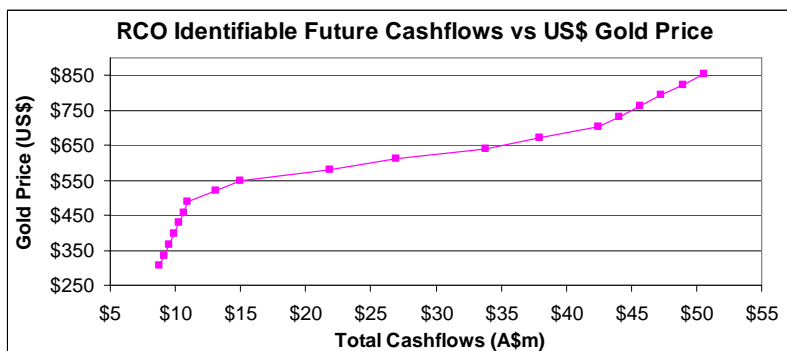
Substantial Shareholders:

Oxiana	17.7%
Topham & Ogg	17.2%
Gasmere	7.4%
Rio Tinto	6.4%
Colonial First State	6.9%
Global Mining Investments	6.2%
Top 6	61.8%

Gold price currently ~US\$610/oz



RCO Identifiable Future Cashflows vs US\$ Gold Price



Analyst: Ted Leschke

RCO Royalties

RCO is set to reap significant cashflows from a royalty it holds over Oceana Gold's (OGD) Reefton Gold project located on the South Island of New Zealand. The Reefton Gold project is currently dry commissioning and is to proceed to wet commissioning with first production expected in mid February. Reefton ore will be concentrated on site with the concentrate treated at OGD's main operations at Macraes. Expected production is 60koz to 65koz for 2007 with annualised rate of 70kozpa. Reefton has an initial 5 year mine life with 548koz in reserves and 1,641koz in resources from the Globe Process open pit.

Strong royalties from Reefton for 5 years.

- Initially RCO is due to receive royalties of 250oz of gold per quarter irrespective of the production rate post a 6 month grace period. There is an incremental addition to this royalty should the New Zealand dollar gold price rise above NZ\$700/oz up to NZ \$900/oz. For each NZ\$10 increment above NZ\$700 equates to a further 50oz/quarter royalty. This royalty is equivalent to total of A\$19m over 5 years using our commodity assumptions. The important thing to note is that this royalty component is not sensitive to profits or revenues, only the NZ\$ gold price and commencement of production.

Reefton royalty is underpinned by a high NZ\$ gold price.

- Once 400,000 cumulative ounces have been recovered the royalty changes to 1% below NZ\$800/oz, 2% between NZ\$800/oz and NZ\$900/oz, and 3% above NZ\$900/oz. This second component of the royalty is equivalent to total of A\$6m over 4 years using our commodity assumptions. This applies until a total of 1.0moz cumulative ounces have been produced, after which royalty reverts to a flat 1.5% of production.
- Total identifiable royalties to RCO from Reefton is estimated to be A\$24m based on existing reserves. Given that there is 1.1moz in additional resources at the Globe Process open pit and that the Reefton royalty also covers the Sams Creek project where OCN has identified a resource 778,000koz, there is significant potential for additional royalty revenues beyond the current reserve.

RCO's royalty bank also includes projected royalties over:

- Kagara Zinc's Mt Garnet zinc deposit where there is a 3% NSR over an open cut reserve of 646kt grading 6% zinc and underground reserve of 618kt grading 10.5% zinc.
- Copperco's Mt Kelly copper deposit where there is a 1% net smelter return capped at \$619,000 after the first 25 million pounds of copper has been produced.

Based on our commodity assumptions RCO's royalties on ratified projects with JORC reserves will support RCO's exploration programme for several years whilst building considerable cash position as shown below. In addition there is always the chance that Reefton's and Mt Kelly's reserves are extended and/or other projects in the RCO's royalty bank come to fruition. This means there is a reduced chance of shareholder dilution and, given the tight share registrar, any exploration success will have very positive share price effect. We calculated a 54cps valuation based on the 3 project royalties and the current cash position alone.

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RCO's Royalty Bank

RCO's royalty bank includes 3 operations with identifiable future cashflows

Company	Description	Commodity	Pre Resource	Scoping Studies	Feasibility	Under Development
Oceana Gold Ltd	Reefton, 1-3% ORR*	Gold				●
Kagara Zinc Ltd	Mt Garnet 3% NSR**	Zinc, Lead, Silver				●
Copperco Ltd	Mt Kelly, 1% NSR	Copper, Gold				●
Silver Standard	Bowdens, 1-2% NSR	Silver			●	
Hydromet Corp Ltd	Stanton, 1% NSR	Nickel, Cobalt		●		
Georgetown Mining Ltd	Dagworth/Huonfels		●			
Perserverance Corp Ltd	Heathcote		●			
Pelican Resources Ltd	Xanadu		●			
Alkane Exploration Ltd	Molong		●			
Copper Strike Ltd	Lake Margaret		●			

*ORR : Overriding Royalty

**NSR: Net Smelter Returns

RCO's Modelled Cashflows (based on ratified project royalties)

RCO Cashflows		Jun-07	Jun-08	Jun-09	Jun-10	Jun-11	Jun-12	Jun-13	Jun-14	Jun-15	Jun-16	Total
Assumptions												
Gold price	US\$/oz	615	593	570	551	551	551	551	551	551	551	
Zinc Price	US\$/lb	1.87	1.70	1.43	1.22	1.22	1.22	1.22	1.22	1.22	1.22	
Copper Price	US\$/lb	3.24	2.58	2.03	1.58	1.58	1.58	1.58	1.58	1.58	1.58	
A\$/US\$	US\$	0.77	0.75	0.74	0.68	0.68	0.68	0.68	0.68	0.68	0.68	
A\$/NZ\$	A\$	1.16	1.14	1.14	1.14	1.14	1.14	1.14	1.14	1.14	1.14	
Reefton Gold Prod.	Koz	0.0	52.5	70.0	70.0	70.0	70.0	70.0	70.0	70.0	28.0	
Mt Kelly Copper Prod.	Kt	0.00	5.67	5.67	5.67	5.67	0.00	0.00	0.00	0.00	0.00	
Mt Garnet Zinc Prod.	Kt	0.00	0.00	26.78	39.41	23.56	0.00	0.00	0.00	0.00	0.00	
Reefton royalty	A\$m	-	2.97	3.57	4.05	4.05	4.05	1.65	1.70	1.70	0.68	24.43
Mt Kelly royalty	A\$m	-	-	0.25	0.20	0.17	-	-	-	-	-	0.62
Mt Garnet royalty	A\$m	-	-	2.65	3.49	2.09	-	-	-	-	-	8.23
Royalty Cashflow	A\$m	-	2.97	6.47	7.75	6.31	4.05	1.65	1.70	1.70	0.68	33.28
Admin Expenses	A\$m	0.60	0.60	0.60	0.60	0.60	0.60	0.60	0.60	0.60	0.60	6.00
Tax expenses	A\$m	0.00	0.00	0.00	0.30	1.03	0.62	0.65	0.04	0.05	0.00	2.69
Interest exp./(inc.)		-0.25	-0.45	-0.42	-0.60	-0.86	-1.07	-1.19	-1.16	-1.17	-1.19	-8.37
Operating Cashflow		-0.35	2.82	6.30	7.45	5.54	3.91	1.58	2.22	2.23	1.27	32.96
Exploration Expenditure	A\$m	1.60	3.30	3.30	3.20	2.00	2.00	2.00	2.00	2.00	2.00	23.40
Net Cashflow	A\$m	-1.95	-0.48	3.00	4.25	3.54	1.91	-0.42	0.22	0.23	-0.73	9.56
Cash Balance	A\$m	9.5	7.55	7.07	10.06	14.32	17.85	19.76	19.34	19.56	19.79	19.06

RCO's Reefton gold royalty has an escalator between NZ\$700/oz and NZ\$900/oz

