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Aspire Mining Ltd (AKM)

Ovoot PFS released

Recommendation
Buy (unchanged)
Price
\$0.13
Target (12 months)
\$0.27 (previously \$0.55)
Risk
Speculative

Expected Return

Capital growth	108%
Dividend yield	0%
Total expected return	108%

Company Data & Ratios

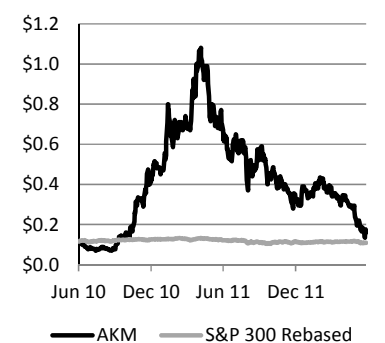
Enterprise value	\$52.0m
Market cap	\$80.7m
Issued capital	620.6m
Free float	31%
Avg. daily vol. (52wk)	1.3m
12 month price range	\$0.13-\$0.67
GICS sector	Materials

Disclosure: Bell Potter Securities acted as as co-manager in a \$33m placement in October 2011 and received fees for that service.

Price Performance

	(1m)	(3m)	(12m)
Price (A\$)	0.29	0.36	0.68
Absolute (%)	-43.86	-55.56	-76.30
Rel market (%)	-36.18	-50.55	-63.07

Absolute Price



SOURCE: IRESS

Ovoot prefeasibility study completed, positive outcomes

AKM's Ovoot Project prefeasibility study supports the two stage development of its 185Mt ROM coal inventory. Stage 1 is expected to ramp up from 2016 to produce 6Mtpa of high quality coking coal. Stage 2 should follow two years later and increase production to 12Mtpa. We had previously modelled a much smaller Stage 1 development commencing in FY14. Changing our model to the scope of the Ovoot PFS has removed operational earnings from our forecast period. Our target price has also been reduced to \$0.27/sh (previously \$0.55/sh) on modelling changes.

Next steps: De-risk 406km of required rail infrastructure

The Ovoot project requires a 406km (\$1.1b) rail line linking the project to existing rail infrastructure. The PFS assumes that this rail link is funded by a separate infrastructure vehicle, Northern Railways LLC. In order to de-risk the entire Ovoot project, AKM must now demonstrate that this rail link is feasible and can provide adequate returns to attract funding from infrastructure investors.

Recognising the project and funding risks

The PFS suggests that capex for Stage 1 and Stage 2 will be US\$1.3b. An additional US\$1.1b will be required for the 406km rail link. If a multi-user rail link solution can be established, this capex could be shared with other participants. We conservatively risk our Ovoot project valuation by 50% and assume that AKM fund 100% of the rail (with some return from tariffs on third party users). We believe that this risking more than reflects project specific risks and the significant capital required for development.

Investment thesis – Buy (Speculative) TP\$0.27/sh

Ovoot is one of the largest undeveloped coking coal projects globally. Its strategic appeal is evidenced by the AKM-Noble Group alliance. At our long term coking coal price forecast (US\$180/t), the Ovoot project could generate annual EBITDA of over US\$700m. AKM is Speculative as it carries significant infrastructure risk.

Earnings Forecast

Year end June	2011a	2012f	2013f	2014f
Sales (A\$m)	0	1	0	0
EBITDA (A\$m)	-5	-5	-7	-6
NPAT (reported) (A\$m)	-4	-3	-3	-2
NPAT (adjusted) (A\$m)	-4	-3	-3	-2
EPS (adjusted) (cps)	-0.9	-0.5	-0.4	-0.3
EPS growth (%)	na	na	na	na
PER (x)	-14.0x	-23.9x	-30.4x	-50.2x
FCF Yield (%)	-46.2%	-14.2%	-2.5%	-2.0%
EV/EBITDA (x)	-14.3x	-14.1x	-10.9x	-12.7x
Dividend (cps)	0.0	0.0	0.0	0.0
Yield (%)	0%	0%	0%	0%
Franking (%)	0%	0%	0%	0%
ROE (%)	-25%	-9%	-5%	-3%

SOURCE: BELL POTTER SECURITIES ESTIMATES

Ovoot PFS release: Two stage project

Change in project scope: 2 x 6Mtpa Stages

The Ovoot PFS outlines a project of two 6Mtpa coking coal stages:

- Stage 1 – 6Mtpa production beginning in 2016 whereby coal is trucked 222km from Ovoot to Moron then loaded onto a multi-user rail line for delivery to end markets; and
- Stage 2 – increasing to 12Mtpa production from 2018, with a dedicated rail line between Ovoot and Moron.

Both stages require:

- Onsite infrastructure and utilities including camp, airstrip, power, water and communications;
- Coal handling and preparation plants; and
- A 406km rail line linking the provincial capital of Moron to the nearest rail head at Erdenet.

We'd previously assumed a 1Mtpa ROM Stage 1, with Stage 2 increasing to 12Mtpa

We had previously estimated a two stage project whereby: (1) production and sales would commence at a rate of up to 1Mtpa ROM coal from FY14, with coal trucked to existing rail infrastructure at Erdenet; and (2) a large-scale expansion to 12Mtpa which would include construction of around 600km rail (Ovoot to Erdenet), a 15Mtpa ROM coal preparation plant and site infrastructure and utilities.

The following table outlines the differences between our previous estimates and those delivered in the prefeasibility study.

Table 1 - Project scope: previous estimates versus PFS assumptions

		Previous (Bell Potter Securities assumed) scope		PFS scope	
		Stage 1	Stage 2	Stage 1	Stage 2
Production					
ROM production	Mtpa	0.5-1.0	15.0	7.3	14.5
Yield	%		80%	83%	83%
Product	Mtpa	(ROM) 0.5-1.0	12.0	6.0	12.0
Commencing		FY14	FY17	FY16	FY18
Product delivery					
Ovoot to Moron (222km)		Truck	Rail	Truck	Rail
Moron to Erdenet (390km)		Truck	Rail	Rail	Rail
Rail to end markets		Russia ports	Russia ports	Russia ports & China	Russia ports & China
Capital costs (incl. contingencies)					
Mine & site	US\$m	16	150	235	24
Coal prep plant	US\$m		300	225	238
Transport infrastructure	US\$m	36	510	105	449
Total	US\$m	52	960	565	710
Total (Stage 1 + Stage 2)	US\$m		1,012		1,275
Capital intensity	US\$/tpa	69	85	94	118
Capital intensity (Stage 1 + Stage 2)	US\$/tpa		84		106
Operating costs					
Mine gate cost	US\$/t	19	28		39
Rail & port costs	US\$/t	124	96		79
Total FOB cost excl royalties	US\$/t	143	124		118
Royalties & charges	US\$/t	7	9		
Total FOB cost	US\$/t	150	133		

SOURCE: COMPANY DATA AND BELL POTTER SECURITIES ESTIMATES

Both stages rely on 406km (US\$1.1b) missing rail link

In both our previous estimates and the Ovoot PFS, it is assumed that an “infra-co” provides a rail solution between the Ovoot Project’s provincial capital of Moron, and the nearest rail head at Erdenet. AKM has formed Northern Railways LLC to separately investigate the feasibility study for this infrastructure. We assume:

- it will be a 406km (US\$1.1b) common user rail line;
- AKM will utilise 60% of the capacity; and
- at 20Mtpa (AKM plus third parties) a rail tariff of around US\$12/t (Moron to Erdenet) would provide adequate return to an infrastructure investor (or US\$20/t at 12Mtpa).

Next steps: Sufficiently funded for BFS completion

At 31 March 2012, AKM had \$28.7m cash. This is sufficient for AKM to progress its project to completion of a Bankable Feasibility Study. AKM’s work program is to:

- continue increasing resources and reserves through exploration and infill drilling;
- continue progressing the Northern Railways (Moron to Erdenet) project through government approvals, licencing, third party partnerships and ultimately a funding solution; and
- complete a BFS on the Ovoot Project by mid-2013.

Changes to valuation: Earnings removed from forecast period

We have changed our modelling to reflect the change in scope of the Ovoot Project. This has removed operating earnings from our forecast period (FY13-15).

Our valuation of AKM assumes a project development as outlined in the Ovoot Project PFS. We assume hard coking coal prices of US\$180/t and currency at US\$0.85/A\$. We have added a further level of conservatism through:

- applying a risk discount of 50% to the Ovoot Project to reflect the relative uncertainties with respect to project development timelines and access to capital;
- assuming AKM raise A\$20m at \$0.20/sh before end-2012 to fund ongoing development expenditures (despite AKM having sufficient cash to mid-2013); and
- assuming AKM fund and own the infra-co for the Moron to Erdenet missing rail link.

Table 2 - AKM valuation

Issued capital		m					
Shares on issue		620.6					
Options		247.2					
New issue at \$0.20/sh		100.0					
Total (diluted)		967.8					
	Present		+ 12 months		+ 24 months		
	A\$m	\$/sh	A\$m	\$/sh	A\$m	\$/sh	
Projects							
Ovoot Project	1,505	1.56	1,655	1.71	1,819	1.88	
Risk discount	50%		50%		50%		
Total Ovoot Project (risked)	752	0.78	827	0.85	910	0.94	
Infrastructure (100%)	-514	-0.53	-565	-0.58	-622	-0.64	
Corporate overheads	-30	-0.03	-33	-0.03	-36	-0.04	
EV	208	0.22	229	0.24	252	0.26	
Net cash + A\$20m issue	54	0.06	50	0.05	49	0.05	
Equity value	263	0.27	279	0.29	301	0.31	

SOURCE: BELL POTTER SECURITIES ESTIMATES

Additional project information

Coking coal: 252Mt resources & 178Mt reserves

In late May 2012, AKM released an initial reserve for its Ovoot Coking Coal Project and an updated resource estimate. We estimate that the project will ultimately yield a reserve of at least 185Mt on the expectation of further conversion of resources to reserves.

Table 3 - AKM resource update and initial reserve

	Mt
Resource ROM	
Measured	156
Indicated	70
Measured + Indicated	226
Inferred	26
Total resource	252
Probable reserve	
ROM	178
Product coal	147

SOURCE: COMPANY DATA AND BELL POTTER SECURITIES ESTIMATES

Reserves: Scope for further increases

AKM has identified several near term opportunities to increase the 178Mt reserve:

- An additional 18Mt of ROM coal in the inferred status was omitted from the reserve due to the density of coal quality sampling. However, resource consultant Xstract will include 8Mt of this coal in the ROM mine plan. Additional drilling should increase the coal quality confidence and bring this material into the reserve.
- Around 20Mt of measured and indicated coal resources below 300m have been excluded from the reserve. Additional geotechnical data is expected to extend the pit beyond 300m to include this additional tonnage.
- The conversion of further exploration upside to resource then reserve categories.

Resources: Scope for further increases

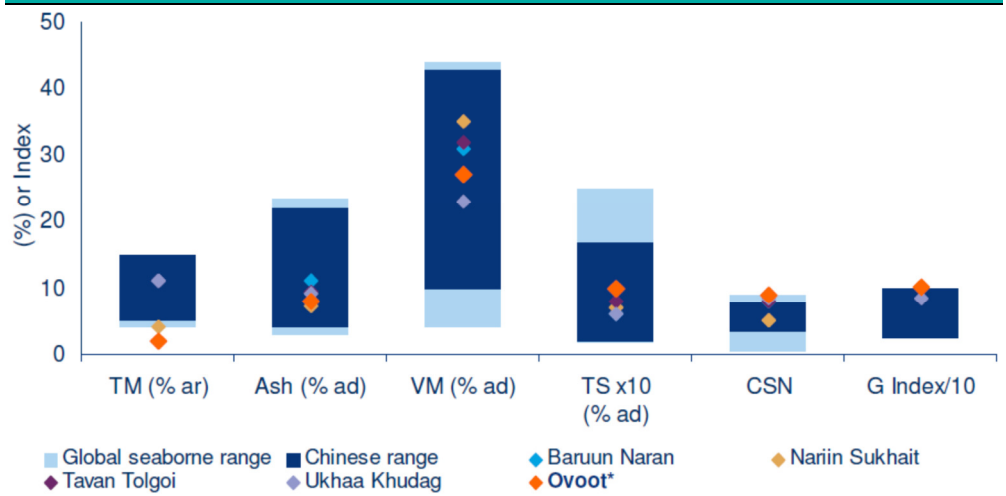
AKM still expects to add significant tonnes to the current resource. Step out drilling has extended coal seams to the south west and to the north east between the current Ovoot resource and the northeast exploration area. The northeast exploration area requires further exploration and remains open to the north and northeast.

Coal quality: Wood Mackenzie analysis

In late August 2011, AKM published the results from consultants Wood Mackenzie's analysis of the Ovoot coal. The analysis confirmed that the Ovoot coal:

- would easily meet global seaborne market requirements;
- had strong caking, hard coking and blend carrying capacity; and
- pricing would be hard coking coal benchmark.

Figure 1 - Ovoot coal quality comparison



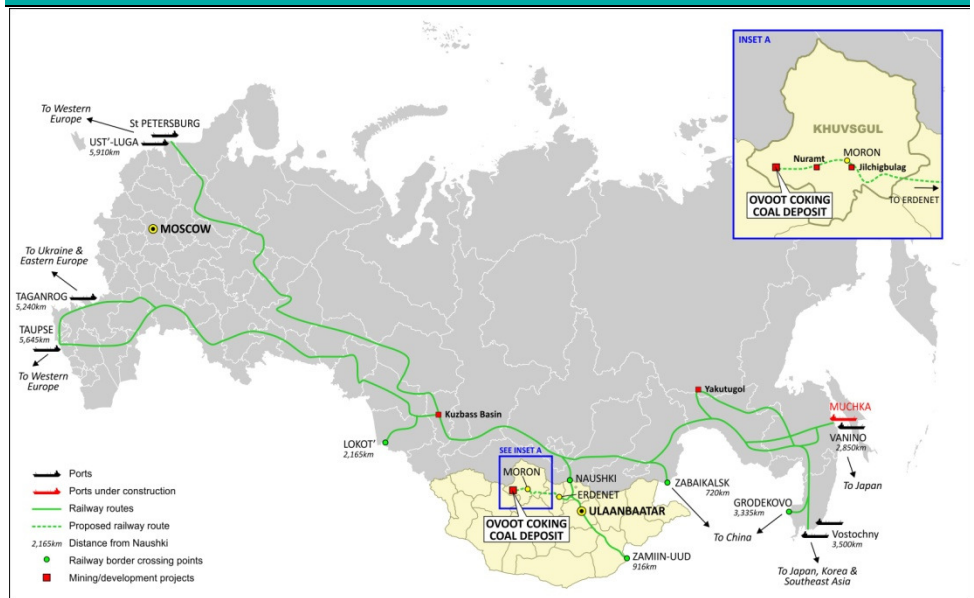
SOURCE: WOOD MACKENZIE, * SUPPLIED BY AKM

Four potential routes to market for Ovoot coal

Through discussions with Russian rail providers and Mongolian infrastructure providers, AKM has identified four potential routes to market.

1. East coast Russian ports: Railing coal north along the trans-Mongolian railway, then across the trans-Siberian railway to east coast Russian ports;
2. South to the Chinese border: Railing coal south along the trans-Mongolian railway for sale at the Mongolian-Chinese border;
3. China via Manzhouli: Railing coal north along the trans-Mongolian railway then east to the Mongolian-Chinese border at Manzhouli (Inner Mongolia); and
4. West to Europe: Depending on freight agreements, it may be viable to rail coal north along the trans-Mongolian railway then west along the trans-Siberian railway to markets in Europe.

Figure 2 – Ovoot Project: distances to markets



SOURCE: AKM

Transport to port a key hurdle

The following table illustrates the freight distances to Vostochny Port (east coast Russia), one of the four routes to market identified by AKM. This route is likely to be the most direct point of access to the seaborne market (and therefore seaborne prices).

Table 4 - Ovoot coal transport distances

	km
Rail Ovoot -> Moron	222
Rail Moron -> Erdenet	406
Rail total Ovoot -> Erdenet	628
Example: Seaborne sales through Russia	
Rail Erdenet -> Naushki (Mongolia-Russia border)	420
Rail Naushki -> Vostochny	3,500-3,800
Rail total Erdenet -> Vostochny	4,070
Total Ovoot Project -> Vostochny	4,692

SOURCE: COMPANY DATA AND BELL POTTER SECURITIES ESTIMATES

Noble to assist with AKM's key challenges

In December 2011, AKM announced that it had entered into an Alliance Agreement with Noble Group to assist with the development of the Ovoot Coking Coal Project. Importantly, the Alliance covers a number of key challenges the Ovoot project will face, namely:

- investigating supply chain logistics to transport Ovoot coking coal to customers in China, north Asia and seaborne markets;
- marketing of Ovoot coking coal and identifying opportunities to develop value added coal products;
- identifying strategic partners to assist with access to rail and port infrastructure;
- identifying strategic partners to assist with funding the Ovoot coking coal project; and
- support the development of AKM's proposed rail link between the Ovoot project and rail infrastructure at Erdenet.

Marketing and logistics: Noble markets 50% of AKM's first 5Mt

For separate marketing and logistics management fees, Noble will:

- market at least 50% of the first 5Mt of saleable coking coal produced from Ovoot; and
- manage the logistics chains between Erdenet and end customers in respect of these sales.

Noble is also entitled to purchase up to 33% of this marketing allocation as principal.

Boost for Ovoot project de-risking

The Noble alliance is a significant positive for the Ovoot project. Noble is a major global commodities trading house with strong trading relationships with logistics providers and commodities end users. These relationships help to mitigate project funding, development and commercial risks.

Aspire Mining Ltd (AKM)

Company description

AKM's key asset is the 100% owned Ovoot coking coal project in northern Mongolia. Ovoot has a resource of 252Mt high quality coking coal. AKM is in the process of completing studies to support the project's development. The company currently expects to develop the project in two stages. Stage 1 is expect to ramp-up 2016 and produce 6Mt/tpa premium quality coking coal. Stage 2 will expand production to 12Mt/tpa.

Investment strategy: Buy (Speculative)

We believe there is strategic value in AKM through its:

- large scale (252Mt), high quality Ovoot coking coal resource;
- potential to partner with major off-take customers (steel producers) to assist with financing the Ovoot Project;
- proximity to other potential minerals deposits, including the Burenhaan Phosphate project (a Mongolian Mineral Deposit of Strategic Importance); and
- implicit relationships/ties with major mining/minerals houses including Ivanhoe Mines/SouthGobi Resources (19.9% shareholder) and Noble Group (5% shareholder).

Valuation: Risked DCF of \$0.27/sh

Our base case valuation of AKM assumes:

- that AKM delivers Stage 1 and Stage 2 of the Ovoot Project as outlined in the June 2012 PFS;
- that AKM funds and owns 100% of the 406km (US\$1.1b) multi-user rail line between Moron and Erdenet, with third party tariff revenues;
- a risk factor of 50% on Ovoot Project to reflect the relative uncertainties with respect to project specific risks and the significant capital required for development;
- Long term hard coking coal prices of US\$180/t and currency at US\$0.85/A\$; and
- AKM raises A\$20m at \$0.20/sh before end-2012 to assist with project development (despite being adequately funded to mid-2013).

Risks

Risks include, but are not limited to:

- The Ovoot project and AKM's exploration tenements are located in Mongolia. With this location carries sovereign risks specific to the region. The company's head office is in Perth, Australia;
- AKM is aiming to develop a large scale mine and associated infrastructure. Ramping up to steady-state production rates is yet to be proven;
- The Ovoot project is in an extremely remote location, making infrastructure very important. There are risks that obtaining the required permits for infrastructure development will be problematic.

- Commodity price and exchange rate fluctuations: Similar to other commodity producers, AKM's earnings and value are subject to fluctuations in commodity price and exchange rates; and
- Major AKM shareholders include: AKM directors; SouthGobi Resources Ltd, Noble Group and the vendors of the Mongolian projects.

Appendix 1: AKM capital structure

AKM issued capital, market capitalisation & enterprise value

Table 5: Issued Capital, Market Capitalisation & Enterprise Value

Total issued shares m	620.6
Share price A\$	0.13
Market cap (undiluted) A\$m	80.7
Net cash A\$m (Bell Potter Securities estimate)	28.7
EV (undiluted) A\$m	52.0
Options m	247.2
Issued shares (diluted) m	867.8
Market cap (diluted) A\$m	112.8
Net cash + options A\$m	41.7
EV (diluted) A\$m	71.2
SOURCE: IRESS	

Table 6 - Financial summary

PROFIT AND LOSS							FINANCIAL RATIOS						
Year ending 30 Jun	Unit	2010a	2011a	2012f	2013f	2014f	Year ending 30 Jun	Unit	2010a	2011a	2012f	2013f	2014f
Revenue	\$m	-	0	1	-	-	VALUATION						
Expense	\$m	(1)	(5)	(6)	(7)	(6)	NPAT	\$m	(1)	(4)	(3)	(3)	(2)
EBITDA	\$m	(1)	(5)	(5)	(7)	(6)	Reported EPS	c/sh	(0)	(1)	(1)	(0)	(0)
Depreciation	\$m	(0)	(0)	-	-	-	EPS growth	%	-95%	133%	-41%	-21%	-39%
EBIT	\$m	(1)	(5)	(5)	(7)	(6)	PER	x	-32.5x	-14.0x	-23.9x	-30.4x	-50.2x
Net interest expense	\$m	0	1	1	3	3	DPS	c/sh	-	-	-	-	-
PBT	\$m	(1)	(4)	(4)	(4)	(2)	Yield	%	-	-	-	-	-
Tax expense	\$m	-	-	0	1	1	CFPS	c/sh	(1)	(6)	(2)	(0)	(0)
NPAT of associates	\$m	-	-	-	-	-	P/CFPS	x	-12.6x	-2.2x	-7.0x	-39.9x	-50.2x
NPAT (reported)	\$m	(1)	(4)	(3)	(3)	(2)	EV/EBITDA	x	-74.9x	-14.3x	-14.1x	-10.9x	-12.7x
NPAT attributable to MI	\$m	-	-	-	-	-	EBITDA margin	%	0%	-1751%	-879%	0%	0%
NPAT attributable to AKM	\$m	(1)	(4)	(3)	(3)	(2)	EBIT margin	%	0%	-1759%	-879%	0%	0%
Abnormal items	\$m	-	-	-	-	-	Return on assets	%	-9%	-22%	-11%	-6%	-4%
NPAT (adjusted)	\$m	(1)	(4)	(3)	(3)	(2)	Return on equity	%	-11%	-25%	-9%	-5%	-3%
CASH FLOW							LIQUIDITY & LEVERAGE						
Year ending 30 Jun	Unit	2010a	2011a	2012f	2013f	2014f	Net debt (cash)	\$m	(6)	(12)	(33)	(50)	(48)
OPERATING CASHFLOW							ND / E	%	-42%	-42%	-59%	-69%	-68%
Receipts	\$m	-	-	1	-	-	ND / (ND + E)	%	-71%	-74%	-143%	-218%	-209%
Payments	\$m	(0)	(3)	(5)	(2)	(2)	ASSUMPTIONS - Prices						
Royalties	\$m	-	-	-	-	-	Year ending 30 Jun	Unit	2010a	2011a	2012f	2013f	LT Real
Tax	\$m	-	-	0	1	1	Coal prices						
Net interest	\$m	0	0	1	3	3	Hard coking	US\$/t	146	247	260	225	185
Other	\$m	-	-	-	-	-	Semi-hard coking	US\$/t	119	209	214	192	159
Operating cash flow	\$m	(0)	(3)	(2)	2	2	LV PCI	US\$/t	110	196	194	178	149
INVESTING CASHFLOW							Semi-soft coking	US\$/t	102	190	178	160	123
Capex	\$m	(0)	(0)	(0)	-	-	Thermal	US\$/t	77	106	120	118	92
Exploration & evaluation	\$m	(1)	(8)	(8)	(4)	(4)	CURRENCY						
Other	\$m	(1)	(3)	0	-	-	AUD/USD	US\$/A\$	0.87	0.99	1.03	0.96	0.85
Investing cash flow	\$m	(2)	(11)	(9)	(4)	(4)	ASSUMPTIONS - Production						
FINANCING CASHFLOW							Year ending 30 Jun	Unit	2010a	2011a	2012f	2013f	2014f
Equity proceeds	\$m	7	20	31	20	-	Production						
Debt proceeds/(repayments)	\$m	-	-	(10)	(10)	-	Ovoot - Stage 1	Mt	-	-	-	-	-
Dividends	\$m	-	-	-	-	-	Ovoot - Stage 2	Mt	-	-	-	-	-
Other	\$m	-	-	-	(1)	-	Total	Mt	-	-	-	-	-
Financing cash flow	\$m	7	20	21	9	-	Production split						
Change in cash	\$m	5	7	11	7	(2)	Hard coking	%	0%	0%	0%	0%	0%
BALANCE SHEET							Semi-hard coking	%	0%	0%	0%	0%	0%
Year ending 30 Jun	Unit	2010a	2011a	2012f	2013f	2014f	LV PCI	%	0%	0%	0%	0%	0%
ASSETS							Semi-soft coking	%	0%	0%	0%	0%	0%
Cash & short term investments	\$m	6	12	23	30	28	Thermal	%	0%	0%	0%	0%	0%
Accounts receivable	\$m	0	0	-	-	-	VALUATION						
Inventory	\$m	-	-	0	0	0	Issued capital						
Property, plant & equipment	\$m	0	0	1	1	1	Shares on issue						621
Other	\$m	12	17	22	22	22	Options						247
Total assets	\$m	17	29	46	53	51	New issue at \$0.20/sh						100
LIABILITIES							Total						968
Accounts payable	\$m	0	1	-	-	-	Discount rate %						13%
Borrowings	\$m	-	-	(10)	(20)	(20)							
Other	\$m	3	-	-	-	-							
Total liabilities	\$m	4	1	(10)	(20)	(20)							
SHAREHOLDER'S EQUITY													
Share capital	\$m	19	39	70	90	90							
Reserves	\$m	1	0	(1)	(1)	(1)							
Retained earnings	\$m	(7)	(11)	(14)	(17)	(19)							
Total equity	\$m	14	28	56	73	71							
Weighted average shares	m	222	222	580	671	721							

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.

Accumulate: Expect total return between 5% and 15% on a 12 month view. For stocks regarded as 'Speculative' a return of between 5% and 30% is expected.

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

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

Sell: Expect <-15% 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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