

19 March 2010

Produced by: RBS Morgans Limited

Buy

Important: The above recommendation has been made on a 12 month view and may not suit your investment needs or timeframe. The basis it is prepared on is summarised on the last page of this report. **PLEASE CONTACT YOUR ADVISER TO DISCUSS THIS GENERAL RECOMMENDATION BEFORE ACTING ON IT.**

High Volatility

Target price
A\$0.23

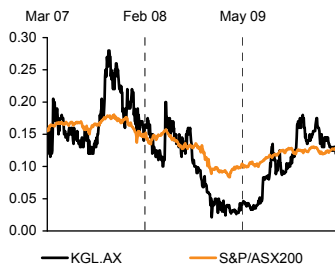
Price
A\$0.12

Short term (0-60 days)
n/a

KGL100319

Price performance

	(1M)	(3M)	(12M)
Price (A\$)	0.14	0.14	0.03
Absolute (%)	-17.2	-11.1	344.4
Rel market (%)	-20.8	-15.0	215.0
Rel sector (%)	-20.5	-14.6	131.4



Market capitalisation
A\$47.16m (US\$43.55m)

Average (12M) daily turnover
A\$0.12m (US\$0.11m)

Sector: BBG AP Mining
RIC: KGL.AX, KGL.AU
Priced A\$0.12 at close 18 Mar 2010.
Source: Bloomberg

Analyst

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Kentor Gold

Site works to start

KGL has extensive tenements in the Kyrgyz Republic. It is developing the Andash gold-copper project (80%) to produce 60koz gold and 5kt copper pa in concentrate, and it is evaluating other Soviet-era gold and copper prospects.

Key forecasts

	FY07A	FY08A	FY09F	FY10F	FY11F
EBITDA (A\$m)	0.97	-1.63	0	0	11.6
Reported net profit (A\$m)	0.98	-5.24	0.13	0.13	10.6
Normalised net profit (A\$m) ¹	0.98	-4.83	0.13	0.13	10.6
Normalised EPS (c) ¹	-1.6	-5.08	0.03	0.03	2.7
Normalised EPS growth (%)	n/a	217.5	n/a	0.1	7,886
Dividend per share (c)	0	0	0	0	0
Dividend yield (%)	0	0	0	0	0
Normalised PE (x)	n/m	n/m	354	354.4	4.44
EV/EBITDA (x)	n/m	n/m	n/a	n/a	3.06
Price/net oper. CF (x)	10.2	-5.41	354	354.4	4.03
ROIC (%)	0	-30.8	0	0	126.8

1. Pre non-recurring items and post preference dividends
Accounting standard: IFRS
Source: Company data, RBS Morgans forecasts

year to Dec, fully diluted

Andash Zone 1 gold-copper – the immediate focus (KGL 80%)

A 2007 feasibility study evaluated development of an open pit mine producing a sulphide concentrate containing 60,000oz of gold and 5,000t of copper per year. Well sited for logistics, power, water and workforce, the capital cost was estimated at US\$55.4m. Andash has been extensively drilled, and an adit driven through the deposit in Soviet times, providing a high degree of confidence in the reserve and process metallurgy. KGL owns the mining and production fleet, and the construction camp, with an estimated replacement cost of US\$9m. The projected site operating cost of US\$9.60/t ore translates into our estimate of US\$250/oz of gold equivalent, including marketing, transport and processing charges. AMEC Minproc is updating and optimising this study, due for delivery in the March-quarter 2010.

The broader Andash tenement (KGL 80%)

The ML covering the Andash Zone 1 extends 2km by 1.5km within the Andash licence, which extends 10km along the prospective trend, and includes Andash zones 2 and 3, as well as four other Soviet-era discoveries. The Nakhodka gold deposit has reported intersections of 9.9m at 7.9g/t and 8.0m at 6.0g/t gold in trenches, while the other prospects are gold-copper. We expect exploitation of these deposits to extend the mine life well beyond 10 years, with a realistic expectation that the licence will support a larger-scale operation.

The Kyrgyz Republic

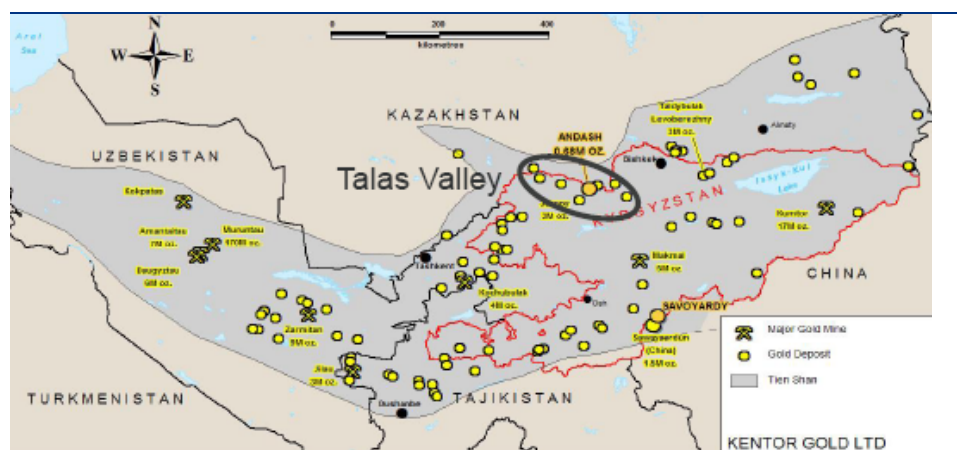
In mid 2009, President Bakiyev, President of the Kyrgyz Republic since 2005, was re-elected with 76% of the vote, although international observers noted "voting irregularities", and corruption is seen to be an issue. However Toronto-listed Centerra Gold's Kumtor mine, producing about 600,000ozpa of gold, has operated uninterrupted since 1997, with its updated resource base now 4.9moz of gold. After a period of dispute with the Kyrgyz Government, it now operates under a new tax regime with gross revenue taxed at 14%. We value the Andash ML at A\$0.28/KGL share, with a discount rate of 12.93%, which we have discounted by 25% for our valuation and target price of A\$0.23/KGL share.

Company overview

Kentor Gold (ASX:KGL) is an Australia-based company with resource exploration and development interests in Central Asia. Its current focus is the development of the Andash gold-copper mine, in the Kyrgyz Republic, in which it has an 80% interest, with the Kyrgyz Government holding 10% and the balance held by UK-based interests. KGL has other interests in the exploration and evaluation of gold and base metals prospects in the Kyrgyz Republic, and in geothermal energy, where ASX-listed Panax Geothermal (ASX:PAX) is earning up to a 61% interest.

Andash is a gold-copper project targeted for production late in 2011 at the rate of 60,000oz gold and 5,000t copper per year. The evaluation of other prospects on the broader licence that were identified in the Soviet era has the potential to deliver a substantially larger resource. Kentor also has an option to purchase 100% of the Savoyardy gold project, located along strike from the 1.5moz Sawayaerdun gold project over the border in China.

Figure 1 : The Andash Licence and the Andash ML



Source: Kentor Gold Presentation – February 2010

The Andash ML

Aurum Mining, listed on the London Stock Exchange AIM, completed a bankable feasibility study into the development of the Andash gold-copper project in January 2007. An ore reserve of 16Mt at a grade of 1.05g/t gold and 0.4% copper was defined to the JORC Code standards. Coupled with detailed drilling, an adit through the deposit at the 2300mRL – slightly above the base of the starter pit (see the section below) – has provided a high level of confidence in both the resource and the process metallurgy. The design documentation for the open pit was approved by the Kyrgyz authorities.

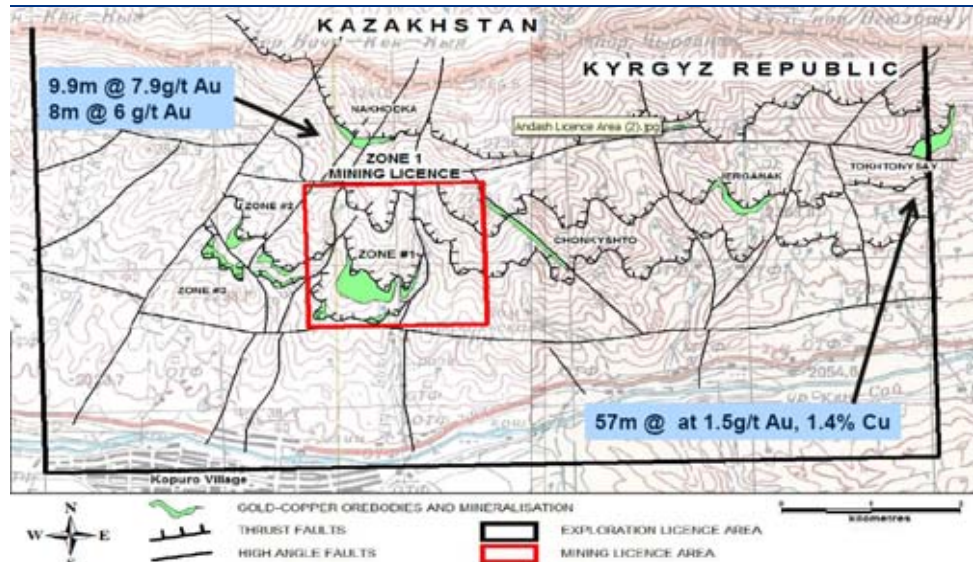
The feasibility study was based on open pit mining at an initial rate of 2Mt of ore per year, moving to 3Mtpy in year 3, with a life-of-mine strip ratio of 0.8:1. A higher-grade starter pit (shown within the final pit in the section below) was designed to reduce the payback period. Processing was to be through conventional crushing, grinding and flotation to produce a clean sulphide concentrate, grading 82g/t gold and 22.3% copper. The LOM production was modelled at 60,000oz of gold and 5,000t of copper per year, with a mine life of eight years.

The capital cost was estimated at US\$55.4m. The Andash project is well located, largely eliminating the requirement to house the workforce. It is also well located for road access, water supply and grid power. Current metal prices would deliver a payback in less than one year.

Kentor Gold has acquired from Aurum the mobile plant and equipment that Aurum had purchased for the mine development and operation of the Andash open pit. Recommissioning of this new plant has now commenced at the railway siding where it is stored 150km west of Andash.

The mining and processing cost was estimated at US\$9.60/t of ore processed, with power costs based on the then current Kyrgyz hydro-power cost of US3 cents/KWh. We have modelled marketing costs and concentrate transport charges, together with standard treatment and refining charges to estimate a C1 cash cost close to US\$300/oz of gold equivalent. The gold equivalent is based on converting the value of copper contained in the concentrate to the weight of gold, which would generate comparable revenue based on our projected gold and copper prices for 2011.

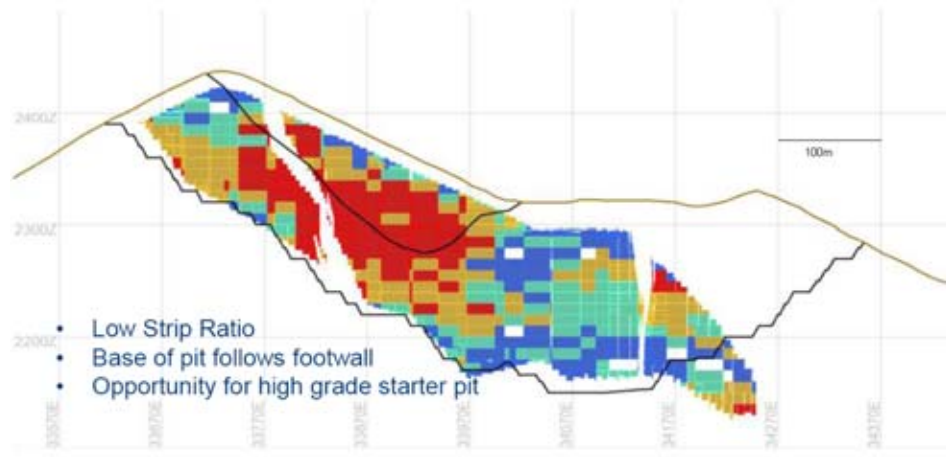
Figure 2 : The Andash Licence and the Andash ML



Source: Kentor Gold Presentation – February 2010

The mining and processing cost was estimated at US\$9.60/t of ore processed, with power costs based on the then current Kyrgyz hydro-power cost of US3 cents/KWh. We have modelled marketing costs and concentrate transport charges, together with standard treatment and refining charges to estimate a C1 cash cost close to US\$300/oz of gold equivalent. The gold equivalent is based on converting the value of copper contained in the concentrate to the weight of gold, which would generate comparable revenue based on our projected gold and copper prices for 2011.

Figure 3 : Andash Pit cross section



Source: Kentor Gold Presentation – March 2010

A refreshed feasibility study is due for completion in the March-quarter 2010, updating capital and operating costs.

The Andash Licence

As Figure 2 (The Andash Licence and the Andash ML) shows, a number of other gold prospects identified during the Soviet era have been followed up by Aurum Mining with sampling and trenching. The Tokhtonsay project, 6km east of the ML, reported a diamond drill intersection of 57m at 1.5g/t gold and 1.4% copper, while at Nakhodka, 2km north of Zone #1 in the ML, trenching has reported high-grade gold, with the best results 9.9m at 7.9g/t gold, and 8.0m at 6.0g/t. Evaluation of these and the four other known prospects in the licence will be undertaken together with development of the Andash project in its current configuration.

Savoyardy – KGL 100%

The Savoyardy gold project in the Kyrgyz Republic is about 8km along strike from the 1.5moz Sawayaerdun project, Xinjiang Province, China. As with Sawayaerdun, the Savoyardy project contains a number of high-grade gold and gold-antimony lodes within a large mineralised system. Previously evaluated during the Soviet era by drilling and underground development, Kentor Gold undertook a drilling program to successfully evaluate the potential for a small, high-grade underground mine at Savoyardy. With the focus on development of the larger Andash project, this proposal has been mothballed. Kentor Gold plans to continue drilling the project to build the size of the resource. The area retains potential for a larger gold project to be evaluated.

Geothermal JV – Panax earning 51%

After a six-month technical evaluation Panax Geothermal (ASX:PAX) committed to a regional exploration program to identify commercially attractive exploration targets in Kentor Gold's geothermal tenements in the Kyrgyz Republic. It has agreed to spend A\$5.0m to earn a 51% interest, and may earn a further 10% interest with the expenditure of another A\$1.0m. It currently has an application for a grant of US\$5.4m before the World Bank's "GeoFund".

Valuation and risks

In our simple DCF valuation of the Andash Zone 1 project we use the Kyrgyz Republic's 5% royalty on gold revenue, 3% royalty on copper and a 10% net profits tax rate, resulting in our valuation of about US\$140m. We value KGL's 80% equity at US\$110m, using the 12.93% discount rate. We expect that while some debt will be employed to fund development, further equity will also be required above the current 393.0m shares on issue. We have discounted the value by 25% to allow for an increased equity requirement. After adding in the valuation of non-core assets and exploration upside, we reach a valuation of A\$0.23 per KGL share, in line with the table below.

The share price currently values Andash at A\$60/oz of gold in reserves. Realisation of the Andash Zone 1 development would be expected to see the share price move towards our DCF valuation, and close to US\$200/oz of reserves, which would support a trebling in the share price from current levels based on current issued capital.

Successful evaluation of the other Andash licence targets outside the ML and delivering an increased resource base would add value, as would successful exploration at Savoyardy and in the other exploration tenements. Positive outcomes from the Panax Geothermal JV would also add value.

Downside risk lies with delivering the Andash project in line with current expectations, and with downward moves in the gold and/or copper prices. A strengthening of the Kyrgystani "som" against the dollar, and a rise in Kyrgystani costs would also prove to be negatives for Kentor Gold and for our valuation.

KGL – financial summary

Year to 31 Dec (A\$m)	AIFRS	AIFRS	AIFRS	AIFRS	AIFRS	Price target (A\$ps)	0.23
Income statement	2008A	2009A	2010F	2011F	2012F	Valuation (A\$ps)	0.23
Divisional sales	0.0	0.0	0.0	18.4	137.8		
Total revenue	0.0	0.0	0.0	18.4	137.8	Valuation summary	A\$m
EBITDA	-1.6	0.0	0.0	11.6	107.6	Andash Mining Lease	82.9
Depreciation & amortisation	0.0	0.0	0.0	-1.1	-7.9	Andash Licence	16.6
EBIT	-1.7	0.0	0.0	10.5	99.7	Savoyard Licence	5.6
Net interest expense	0.1	0.1	0.1	0.1	0.1	Panax JV	1.1
Pre-tax profit	-4.8	0.1	0.1	10.6	99.8	Net cash	5.0
Income tax expense	0.0	0.0	0.0	0.0	-15.0	Corporate	-22.2
After-tax profit	-4.8	0.1	0.1	10.6	84.8	Total Value \$m	88.96
Minority interests	0.0	0.0	0.0	0.0	0.0		0.23
NPAT	-4.8	0.1	0.1	10.6	84.8		Shares
Significant items	-0.4	0.0	0.0	0.0	0.0	Production (Mt)	2009A
NPAT post abnormals	-5.2	0.1	0.1	10.6	84.8	Gold Production (moz)	0.00
						Copper Production (mlbs)	0.00
							0.98
							5.72
Growth ratios	2008A	2009A	2010F	2011F	2012F	Key assumptions	2009A
Sales growth					6.5	USD / AUD exchange rate	0.75
Operating cost growth		-100%	nm	nm	342%	Copper price (US\$/lb)	2.24
						Gold price (US\$/oz)	874.55
							1027.30
							987.50
							1175.00
Cash flow statement	2008A	2009A	2010F	2011F	2012F	Per share data	2009A
EBITDA	-1.6	0.0	0.0	11.6	107.6	No. shares	392.6
Cash flow from ops (1)	-2.1	0.1	0.1	11.7	92.7	EPS (cps)	0.0
Capex (2)	-3.1	-1.0	0.0	0.0	0.0	EPS (normalised) (c)	0.0
Disposals/acquisitions	0.1	0.2	0.2	-0.8	-7.7	Dividend per share (c)	0.0
Cash flow from invest (3)	-3.0	-0.8	0.2	-0.8	-7.7	Dividend payout ratio (%)	0.0
Incr/(decr) in equity	4.0	0.0	0.0	0.0	0.0	Dividend yield (%)	0.0
Incr/(decr) in debt	0.0	0.0	0.0	0.0	0.0		0.0
Ordinary dividend paid	0.0	0.0	0.0	0.0	0.0	Operating performance	2009A
Other financing cash flow	-0.2	0.0	0.0	0.0	0.0	EBIT growth	n.m.
Cash flow from fin (5)	3.8	0.0	0.0	0.0	0.0	NPAT growth	n.m.
Forex and disc ops (6)	0.0	0.0	0.0	0.0	0.0	Normalised EPS growth	n.m.
Incr/(decr) cash (1+3+5+6)	-1.3	-0.6	0.4	10.9	85.1	Asset turnover (%)	0.0
Equity FCF (1+2)	-1.3	-0.6	0.4	10.9	85.1	EBITDA margin (%)	n.m.
						EBIT margin (%)	n.m.
						Net profit margin (%)	n.m.
Balance sheet	2008A	2009A	2010F	2011F	2012F	Return on net assets (%)	0.0
Cash & deposits	1.2	0.5	0.9	11.8	96.9	Net debt (A\$m)	-0.5
Trade debtors	0.1	0.1	0.1	0.1	0.1	Net debt/equity (%)	-8.2
Inventory	0.0	0.0	0.0	0.0	0.0	Net interest/EBIT cover (x)	n.m.
Investments	0.0	0.0	0.0	0.0	0.0	ROIC (%)	0.0
Other intangible assets	0.0	0.0	0.0	0.0	0.0		0.0
Fixed assets	0.2	1.0	0.7	0.5	0.3	Comparable multiples (x)	2010F
Other assets	5.3	5.3	5.3	5.3	5.3	Kentor Gold	EV/EBITDA
Total assets	6.8	6.9	7.1	17.7	102.5	Year to 31 Dec	PE
Short-term debt	0.0	0.0	0.0	0.0	0.0		354.4
Trade payables	0.1	0.1	0.1	0.1	0.1	Discovery Metals	EV/EBITDA
Long-term borrowings	0.0	0.0	0.0	0.0	0.0	Year to 30 Jun	PE
Provisions	0.0	0.0	0.0	0.0	0.0		-39.9
Other liabilities	0.2	0.2	0.2	0.2	0.2		-21.3
Total liabilities	0.4	0.4	0.4	0.4	0.4	Intrepid Mines	EV/EBITDA
Share capital	17.4	17.4	17.4	17.4	17.4	Year to 31 Dec	PE
Other reserves							-11.1
Retained earnings	-10.5	-10.4	-10.2	0.4	85.2		-16.7
Total equity	6.4	6.6	6.7	17.3	102.2		-16.5
Minority interest	0.0	0.0	0.0	0.0	0.0		-10.5
Total shareholders' equity	6.4	6.6	6.7	17.3	102.2		-4.8
Total liabilities & SE	6.8	6.9	7.1	17.7	102.5		-10.6

Source: Company data, RBS Morgans forecasts

RESEARCH TEAM

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FIONA BUCHANAN	-	Director - Research	TAMARA STRETCH	-	Associate Director - Research
NICK HARRIS	-	Senior Analyst	TANYA SOLOMON	-	Associate Director - Research
MICHAEL KNOX	-	Executive Director - Economic Strategy	REBECCA SULLIVAN	-	Research/Special Projects
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JOSEPHINE LITTLE	-	Associate Director - Research	MARCEL VON PFYFFER	-	Director - Strategy

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For listed property trusts (LPTs) the recommendation is based upon the target price plus the dividend yield, ie total return. A Buy implies a total return of 10% or more; a Hold 5-10%; and a Sell less than 5%.

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