

Cape Lambert

Australia | Mining | CLIO.L

26 February 2008

Option overhang

Options to impact value post sale – fully diluted cash value of 45p/sh

■ Considerable number of options outstanding – up to 223M shares

We have reviewed the outstanding options at Cape Lambert to assess the fully diluted impact for the company post transaction. There are currently 223M options at various strike prices and differing expiration dates, which if exercised would raise an additional £35M of new money for the issuance of 223M new shares. Thus total shares outstanding would rise from 281.6M to 504.6M on a fully diluted basis.

■ Impact on valuation – full cash value of 45p/sh

We have assumed a worst case scenario with all options exercised. This would generate £35M of new money in addition to the £188M (A\$400M) of proceeds realised on completion of the sale. With the inclusion of the net cash currently held by the company (£3.4M), the total cash value of Cape Lambert is c.£230M, post transaction. Thus on a fully diluted basis, the cash value of the company is 45p/sh post transaction.

■ Execution risks are moderate

We re-iterate our view of 3 key execution risks; 1) the ability for China Metallurgical Corporation (MCC) to meet its obligations, 2) the discovery of a material issue in due diligence, and 3) management plans for proceeds. MCC is a relatively large Chinese corporate that has sufficient financial and political strength to complete the transaction. The company is a 20% partner in the US\$5.2bn Sino Iron Ore Project (120km south of Cape Lambert) and has experience of the regional geology, infrastructure and legal/social requirements. Cape Lambert has consistently used independent 3rd party consultant to verify their work and thus there is unlikely to be any material issue raised in the due diligence.

In terms of use of proceeds, the sale of the Cape Lambert deposit is a material change in the business requiring both shareholder approval for the sale and use of proceeds. As such, the Cape Lambert board will need to present an investment strategy to shareholders at the time of voting on the iron ore asset sale. This will offer shareholders the opportunity to elect whether to continue with the company's investment plans or to seek a full or partial payout of the sale proceeds.

■ Timing of receipt of proceeds

Payment of proceeds from the sale has been structured with 80% payable within 60 days of completion, however a 20% portion (A\$80M) is linked to the granting of a mining lease at the property. This may lead to a time lag for the full proceeds to be received by Cape Lambert, possible 6 to 12 months, (time value of money impact) and adds risk to this portion of the payment.

We maintain our Buy recommendation up to 45p/sh subject to discount for execution risk. This is a 70% premium to the day's opening price of 26p.

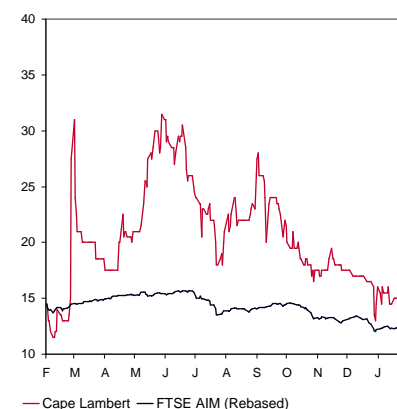
Recommendation **BUY**

Price **31p**
Target **45p**

Market Cap: £87m
EV: £83m

Shares issued: 281m
Daily ave. volume: <1m

Stock Performance



Performance	1m	3m	12m
Absolute %	94	77	114
Relative* %	86	84	142

Source: Datastream

*Rel to FTSE AIM

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Table 1: Option Schedule

Quantity	Exercise Price		Expiry	New money
Issued	(A\$/sh)	(£/sh)	Date	(£'M)
130,968,835	0.277	0.13	31-Oct-08	17.1
50,000,000	0.327	0.15	31-Oct-09	7.7
500,000	0.367	0.17	09-Feb-09	0.1
28,000,000	0.377	0.18	31-Oct-10	5.0
550,000	0.427	0.20	22-Oct-08	0.1
6,350,000	0.490	0.23	30-Jun-08	1.5
3,300,000	0.900	0.42	30-Jun-08	1.4
3,300,000	1.400	0.66	30-Jun-09	2.2
222,968,835				35.0

Source: Company data, Collins Stewart Research

Disclosure. Prices of securities mentioned are as at close of business on 25 February 2008 unless indicated otherwise.

Research Recommendations issued by Collins Stewart Europe Limited in Q4 2007

Recommendations	Buys	Sells	Hold/Neutral
Percentage of Total	49%	32%	19%
Percentage of which in Corporate Client stocks	16%	0%	1%

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