

Americas | Mining | MIO | MIO

10 April 2007

Tequila Sunrise

Recommendation **BUY**

Update

Price **8p**
Target **14p**

Yr to Dec US\$m	2004A	2005A	2006A	2007E	2008E
Sales	.0	.0	.0	.0	.0
EBITDA	.0	1.4	1.4	1.4	1.4
adj. EPS (\$)	-0.01	0.00	-0.01	0.00	0.00
EV/EBITDA (x)	545.5	10.8	17.2	23.8	25.9
P/E (x)	n.a.	n.a.	n.a.	n.a.	n.a.
Div. Yld (%)	0.0	0.0	0.0	0.0	0.0

Market Cap:	£21m
EV:	£17m
Shares issued:	160m
Daily ave. volume:	<1m

■ Minco is focused on zinc and silver exploration

Minco is focused on exploration for zinc and silver and has a portfolio of projects in Mexico and Ireland. The most advanced of these is the Bilbao polymetallic project located in the Mexican state of Zacatecas, where the company has just completed a pre-feasibility study. Minco should complete a full feasibility study at Bilbao over the next 12 months. If brought into production the project should produce concentrate containing 10kt/y of zinc, 7kt/y of lead and 700koz/y of silver from an underground mine. The company has an interest in a number of other exploration projects in the area that could be a source of additional ore, which could extend the mine life.

■ Pallas Green JV could develop into a major zinc deposit

Minco holds a 23.6% interest in the Pallas Green project in Ireland, the balance is owned by Xstrata. It is likely that the deposit hosts a resource of at least 3Mt at a grade of approximately 10% Zn and 1.4% Pb.

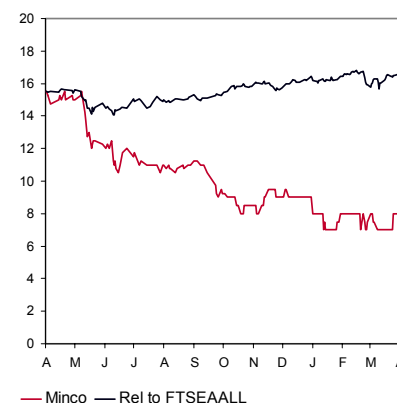
■ Zinc set to remain strong over the medium term

Although the zinc price has fallen back from the high levels touched towards the end of 2006 it remains comfortably above US\$3,000/t and LME stocks remain at below two weeks' consumption. Supply of the metal is likely to remain in deficit during 2007 and 2008 and we forecast a long-term zinc price of US\$0.64/lb.

■ Bilbao provides new direction after Laguna disappointment

Minco's share price has suffered over the past year due to the uncertainty surrounding the development of the Laguna tailings reprocessing project, which has stalled because of environmental concerns. The completion of the pre-feasibility study at Bilbao draws a line under this and provides a clear direction for the company moving forward. We set a 12-month price target of 14p.

Stock Performance



Performance	1m	3m	12m
Absolute %	0	0	-48
Relative* %	-6	-3	-52

Source: Datastream

*Rel to FTSE AALL

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Valuation

We value Minco on a sum of the parts basis and assume that the company brings the Bilbao project into operation over the next three years. The company will need to raise additional funds to complete the bankable feasibility study and to continue to explore its other projects. It will also need to raise further funds to develop Bilbao, although we have assumed that a portion of this can be funded through a debt facility.

Our core NPV for Bilbao sulphides suggests a value of 19p/share. We would value a project where the BFS should be completed over the next 12 months at 50% of NPV and therefore set a target value of 10p/share. The company's other projects, including the oxide portion of the Bilbao resource, have been valued on the basis of their in situ metal value, where a resource has been delineated. Those projects that are at an earlier stage, including the highly prospective Minera Sisa project, have been attributed a nominal value. This suggests a target price of 14p/share, 85% above the current share price.

Table 1: Minco Valuation

	Value p/share
Bilbao Sulphides	£0.10
Bilbao Oxides	£0.01
Pallas Green	£0.01
Laguna	£0.01
Other Exploration	£0.01
	£0.14

Source: CS

Key Assumptions

Bilbao

- Enters production 2010, throughput 330kt/y
- Resource base can be extended by five years through ore from other projects in the surrounding region
- Recovery 88% silver, 90% zinc, 87% lead
- Produces 10.7kt/y of zinc, 7.6kt/y of lead and 760koz/y of silver
- Company is paid 70% of metal value from concentrate
- Tax rate of 28%
- Capex funded through US\$22m debt and US\$20m of equity

Commodity assumptions

- Zinc fades back to long-term price of US\$0.65/lb
- Lead fades back to a long-term price of US\$0.36/lb
- Silver fades back to a long-term price of US\$10/oz

In situ valuations

- Zinc 4c/lb
- Lead 2c/lb
- Silver 1% of in situ value at US\$10/oz
- Mercury US\$600/flask
- Gold USD\$500/oz

Asset Summary

Mexico

Mexico has been a major source of base and precious metals since the pre-Colonial era and today the country produces substantial quantities of copper, silver, gold, lead, zinc and a variety of industrial minerals and speciality metals. Much of the country remains unexplored using modern techniques as there was little incentive for overseas companies to invest there prior to a new mining law being enacted in 1996. Under this law foreign companies and the private sector were allowed to take 100% ownership of projects to encourage new investment into the mining sector.

Bilbao

The Bilbao project covers 1,407Ha of the Mexican silver belt, 50km to the east of the city of Zacatecas and is near to Capstone Mining's Cozamin mine. Previous owners have mined 1Mt of high-grade near surface ore at the deposit from an open pit. Bilbao is in a good position from an infrastructural perspective as the project is located relatively near to a highway and electricity can be drawn from the main grid. Water is scarce although the rights may be obtained from local farmers.

Bilbao is a polymetallic massive sulphide deposit that underlies an oxide cap, which occurs in the contact zone between Cretaceous limestones and a Tertiary age granodiorite. Minco is evaluating the feasibility of an operation that would initially focus on the underground mining of sulphide ore. Studies have also been completed on the open pit mining and vat leach of the oxide ore although this is not currently in the development plan.

Table 2: Bilbao

		2009	2010	2011
Resource	t	2,117,000	1,967,220	1,637,220
Silver Grade	g/t	85.40	85.40	85.40
Zinc Grade	%	3.64%	3.64%	3.64%
Lead Grade	%	2.66%	2.66%	2.66%
Mining Rate	t	0	149,780	330,000
Operating Costs	\$/t	35.40	35.40	35.40
Operating Costs	\$	-	173,507	382,277
Recovery Silver	%	88%	88%	88%
Zinc Recovery	%	90%	90%	90%
Lead Recovery	%	87%	87%	87%
Silver Production	oz	-	360,200.53	793,605.12
Zinc Production	t	-	4,901	10,799
Lead Production	t	-	3,466	7,637

Source: Minco

The sulphide resource is currently 2.1Mt at a grade of 4.25% zinc, 0.25% copper, 2.66% lead and 85.4g/t silver. The oxide resource is 3.6Mt at a grade of 3.28% zinc, 0.34% copper, 2.61% lead and 85g/t silver.

Bilbao would be developed with access using a decline and trackless mining equipment. Mining will be carried out at 1,000t/d (330kt/y) using sublevel stoping with cemented backfill on the majority of the orebody. Ore will be processed using a standard flotation circuit that will produce a zinc concentrate and a second silver-lead-copper concentrate, both of which will be sold on for further refining. The initial capital expenditure estimate for Bilbao is US\$43.3m that would be funded through a combination of project debt and new equity.

Our model suggests that Bilbao has an NPV of US\$116m, £61m, which is equivalent to 19p/share, once the additional equity dilution to bring the project into production is taken into account. This model assumes that the company delineates other sources of ore to extend the mine life by five years. We have made no assumption about the commercial development of the oxide resource. Bilbao is a technically straightforward starter project for Minco that has the potential to develop into a medium-size mine drawing ore both from the known orebody, that may extend to the south, and other satellite deposits in the region. Once the mine is operational it will generate between US\$10m and US\$15m of free cash flow per year for Minco.

Laguna Zacatecana

The Laguna project is located in Central Mexico near to the state capital of Zacatecas. The deposit is a man-made reservoir formed in the early eighteenth century when the Mexican government dammed a depression to provide a source of water for local agriculture. The lake covers an area of 200 hectares with an average water depth of 1.2m. The tailings that make up the lake-bed were created during the Colonial period from nearby mine workings. The process that was used involved mercury and was fairly inefficient and therefore left significant quantities of unrecovered silver, mercury and gold that was washed into the nearest watercourse and then washed down into the depression.

The majority of the resource is located in the lake-bed with additional material in the land surrounding it. It is likely that additional resources will be identified allowing the company to process at a rate of 1.3Mt/y over a mine life of at least 10 years. The BFS envisaged mining using a simple suction cutter dredge and then later using an excavator. Once mined, the ore would be stockpiled and then transported to the plant by road.

Table 3: Laguna Resource

	Tonnes	Ag g/t	Au g/t	Hg g/t	Ag oz	Au oz	Hg flask
Measured	558,583	54.56	0.29	341.07	937,732	4,984	5,522
Indicated	7,371,074	59.08	0.31	315.97	13,399,479	70,309	5,116
Inferred	1,246,558	66.67	0.34	261.45	2,557,170	13,041	4,233
	9,176,215				16,894,380	88,334	14,871

Source: Minco

The company has evaluated the use of a thiosulphate-based leach process to recover the metal, which has a lesser environmental impact than alternative cyanide-based processes with recovery levels of 75% for silver and 85% for the mercury, with a far lower recovery rate of 40% for the gold.

The bankable feasibility study for Laguna was completed by independent engineers, Micon International of Canada. However, because of concerns about the environmental impact of the project, the company has not progressed with development and is seeking to identify a third party that would be interested in acquiring the project.

Minera Sisa

Minco acquired a 50% holding and management control of a Mexican company, Minera Sisa, which owns the Santa Cruz project in the Mexican epithermal precious metals belt in Durango State. The agreement gives Minco the opportunity to increase its holding in the company to above 90% through a series of staged investments in the project.

Minco also acts as the project operator and has just completed the first exploration programme at the deposit, which included 3,000m of diamond drilling and surface and underground sampling. The work identified large-scale disseminated silver-gold mineralisation and high-grade epithermal silver-gold and copper-zinc mineralisation. Historical mining was carried out at the site targeting high-grade silver veins with associated gold mineralisation. The underground infrastructure from this period remains at least partially accessible.

The company has also acquired a further 10,000 hectares of contiguous concessions in the area immediately surrounding the project, which occurs in one of Mexico's main mineralised belts. A very preliminary assessment of the project completed in 2002 indicated that the deposit had the potential to host at least 10Mt at a grade of 480g/t silver and 4.2g/t gold. This preliminary analysis may not be regarded as a resource or reserve using any of the main classification systems, such as JORC. However, this does give some sense of the potential scale of the project, which could on that basis host some 15.3Moz of silver and 1.34Moz of gold.

Ireland

Pallas Green

Ireland is a major producer of lead and zinc and Minco holds an interest in a substantial landholding in the country's main mineralised belt. Exploration has progressed slowly and is still at a relatively early stage, however, the Pallas Green project has the potential to yield a significant base metal discovery.

The Pallas Green project, in which Minco has a 23.6% interest, is made up of 10 prospecting licences covering 350 km² in Limerick/Tipperary and is subject to a joint venture agreement with Xstrata. The project, which is similar to other base metal deposits in Ireland, is located on a major regional structure within a sequence of reef limestones with extensive massive sulphide mineralisation hosted in lenses. Drilling has intersected zones of high-grade mineralisation at depths of around 350m.

To date the joint venture has completed more than 100 holes and Xstrata has indicated that it will continue to fund exploration at the project and a five-rig programme is currently underway. It is likely that the deposit hosts a resource of 3Mt from two orebodies at a grade of around 10% zinc and 1.4% lead. Xstrata is likely to require a resource of at least 20Mt to justify the development of the project. It is therefore possible that Minco could be able to negotiate to acquire Xstrata's interest for either shares or cash.

Financials

Minco's financials reflect the fact that the company is an explorer and has no revenues. The company will need to raise additional funds during 2007 to cover G&A, fund further exploration at Pallas Green and to complete the feasibility study at Bilbao. It will also need to fund the construction of Bilbao once the BFS is complete. The company may be able to generate some cash from the sale of its interest in Laguna, however, no assumption has been made about this.

We have restated the company's accounts in US\$ (from euros) as this will be the main operating currency once the mine is developed.

P&L		2005A	2006E	2007E
Revenue	\$m	0.0	0.0	0.0
Other	\$m	0.0	0.0	0.0
Total revenues	\$m	0.0	0.0	0.0
Operating Costs	\$m	0.0	0.0	0.0
Royalty	\$m	0.0	0.0	0.0
EBITDA	\$m	0.0	0.0	0.0
Depreciation	\$m	0.0	0.0	0.0
Amortisation	\$m	0.0	0.0	0.0
Exploration Expenditure	\$m	0.0	0.0	0.0
G&A	\$m	1.4	1.4	1.4
	\$m	1.4	1.4	1.4
EBIT	\$m	-1.4	-1.4	-1.4
Interest income	\$m	0.2	0.3	0.1
Interest paid	\$m	0.0	0.0	0.0
Other income/expense	\$m	0.5	0.0	0.0
Net interest	\$m	0.7	0.3	0.1
Pre tax profit	\$m	-0.7	-1.1	-1.3
Tax	\$m	0.0	0.0	0.0
Abnormals	\$m	0.0	0.0	0.0
NPAT	\$m	-0.7	-1.1	-1.3
Dividend	\$m	0.0	0.0	0.0
Retained income	\$m	-0.7	-1.1	-1.3
Normalised income	\$m	-0.7	-1.1	-1.3
EPS	\$	0.0	0.0	0.0
EPS (Recurrent)	\$	0.0	0.0	0.0
Dividend	\$	0.0	0.0	0.0
Shares OS	m	143.0	160.0	260.0

Source: Minco, CS Estimates

Balance Sheet		2005A	2006E	2007E
Fixed Assets				
Property Plant Equipment	\$m	0.0	0.0	0.0
Mineral Interests	\$m	15.8	20.8	22.8
Deferred Tax	\$m	0.0	0.0	0.0
Other Assets	\$m	0.0	0.0	0.0
Receivables	\$m	0.0	0.0	0.0
Other Financial Assets	\$m	0.0	0.0	0.0
	\$m	15.8	20.8	22.8
Current Assets				
Cash	\$m	7.8	1.7	1.4
Receivables	\$m	0.1	0.1	0.1
Other Financial Assets	\$m	0.0	0.0	0.0
Inventories	\$m	0.0	0.0	0.0
Tax Assets	\$m	0.0	0.0	0.0
Other Assets	\$m	0.0	0.0	0.0
	\$m	7.9	1.9	1.6
Current Liabilities				
Payables	\$m	0.9	0.9	0.9
Short-term debt	\$m	0.0	0.0	0.0
Tax liabilities	\$m	0.0	0.0	0.0
Provisions	\$m	0.0	0.0	0.0
Other liabilities	\$m	0.0	0.0	0.0
	\$m	0.9	0.9	0.9
Net Current Assets	\$m	7.0	0.9	0.6
Total Assets less Current Liabs	\$m	22.8	21.8	23.5
Long-term				
Long-term debt	\$m	0.0	0.0	0.0
Deferred Tax	\$m	0.0	0.0	0.0
Provisions	\$m	0.0	0.0	0.0
Other liabilities	\$m	0.0	0.0	0.0
	\$m	0.0	0.0	0.0
Net Assets	\$m	22.8	21.8	23.5
Equity Capital	\$m	6.1	6.1	6.1
Share Premium ac	\$m	24.6	24.6	27.6
Cap Conv Reserve	\$m	0.1	0.1	0.1
P&L ac	\$m	-8.0	-9.1	-10.4
Equity Interests	\$m	22.8	21.8	23.5
Minorities	\$m	0.0	0.0	0.0

Source: Minco, CS Estimates

Cash Flow		2005A	2006E	2007E
Operating profit	\$m	-0.6	-1.4	-1.4
Depreciation	\$m	0.0	0.0	0.0
Amortisation	\$m	0.0	0.0	0.0
Gain on disposals	\$m	0.0	0.0	0.0
Provisions and other	\$m	0.0	0.0	0.0
	\$m	-0.6	-1.4	-1.4
Change in debtors	\$m	-0.2	0.0	0.0
Change in stocks	\$m	0.0	0.0	0.0
Change in creditors	\$m	0.2	0.0	0.0
Other	\$m	0.0	0.0	0.0
	\$m	0.0	0.0	0.0
Operating Cash Flow	\$m	-0.6	-1.4	-1.4
Net Interest	\$m	0.2	0.3	0.1
Tax	\$m	0.0	0.0	0.0
	\$m	0.2	0.3	0.1
Maintenance capex	\$m	0.0	0.0	0.0
Expansion capex	\$m	0.0	0.0	0.0
Pre prod dev expenditure	\$m	0.0	-5.0	-2.0
Assets Purchased	\$m	-6.7	0.0	0.0
Asset Sales	\$m	0.0	0.0	0.0
Investing CF	\$m	-6.7	-5.0	-2.0
	\$m	-7.1	-6.1	-3.3
Shares issued	\$m	5.6	0.0	3.0
+ Loans	\$m	0.0	0.0	0.0
+ Other	\$m	0.0	0.0	0.0
- Loan Repayment	\$m	0.0	0.0	0.0
- Dividends	\$m	0.0	0.0	0.0
Financing CF	\$m	5.6	0.0	3.0
Cash Flow	\$m	-1.5	-6.1	-0.3

Source: Minco, CS Estimates

Disclosure. Prices of securities mentioned are as at close of business on 5 April 2007 unless indicated otherwise.

Research Recommendations issued by Collins Stewart Europe Limited in Q3 2006

Recommendations	Buys	Sells	Hold/Neutral
Percentage of Total	60%	20%	20%
Percentage of which in Corporate Client stocks	22%	2%	6%

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