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Aeon Metals Limited (AML)

Drilling program ticks the boxes

Recommendation

Buy (unchanged)

Price

\$0.335

Target (12 months)

\$0.53 (previously \$0.54)

Risk

Speculative

GICS Sector

Materials

Expected Return

Capital growth	58.2%
Dividend yield	0.0%
Total expected return	58.2%

Company Data & Ratios

Enterprise value	\$198.2m
Market cap	\$196.3m
Issued capital	586.0m
Free float	69%
Avg. daily val. (52wk)	\$401,268
12 month price range	\$0.155-\$0.45

Price Performance

	(1m)	(3m)	(12m)
Price (A\$)	0.35	0.37	0.16
Absolute (%)	-2.9	-8.2	109.4
Rel market (%)	0.2	-3.0	106.8

Absolute Price



SOURCE: IRESS

Extensional drilling shows exceptional upside

Extension drilling at AML's 100% owned Walford Ck copper-cobalt project in QLD has continued to deliver impressive results, with the latest hole released today, WFDH378, drilled 5.7km west of the current Resource and intersecting 13m @ 3.73% Cu, 0.27% Co and 49g/t Ag from 300m. This was contiguous to high grade lead-zinc intersections of 19m @ 4.84% Pb, 4.23% Zn and 87g/t Ag and 4m @ 24.1% Pb, 4.57% Zn and 209g/t Ag. These results are consistent with the geological model and are 1.1km along strike from the widest and highest grade hole drilled on the project to date, WFDH352, 42m @ 2.55% Cu, 0.29% Co and 41g/t Ag. These holes add significant weight to evidence pointing to the continuity and significant growth potential of the deposit. Should portions of this be classified into the Inferred Resource category, it would likely result in a material increase to the Walford Ck Resource base.

Infill drilling underpins the base-case

Infill drilling has also made excellent progress and delivered impressive results. Initially targeting 30,000m of drilling for the 2018 program, we estimate that when drilling finishes up at the end of October, AML will have completed in excess of 34,000m. Cost efficiencies should see the program finish in-line with the initial budget of \$8m. The program has returned results consistent with the known Resource, demonstrating strong continuity along strike through the Vardy and Marley zones. Increased drill density should see the bulk of an updated Resource classified into the higher confidence Measured and Indicated categories, making them available for conversion to Ore Reserves, a key milestone towards completing a Definitive Feasibility Study.

Investment thesis – Speculative Buy, valuation \$0.53/sh

AML's drill program is emerging as a success on several fronts and the ~\$8m spend has been hugely value accretive with more newsflow and a key Resource update to come. Our valuation drops marginally on the latest capital structure and AML remains one of our Top Picks for 2018. We retain our Speculative Buy recommendation.

Earnings Forecast

Year end 30 June	2018a	2019e	2020e	2021e
Sales (A\$m)	-	-	-	62
EBITDA (A\$m)	(14)	(4)	(3)	27
NPAT (reported) (A\$m)	(14)	(5)	(4)	11
NPAT (adjusted) (A\$m)	(14)	(5)	(4)	11
EPS (adjusted) (cps)	(3)	(1)	(1)	2
EPS growth (%)	na	na	na	na
PER (x)	(11.9)	(39.1)	(44.6)	17.6
FCF Yield (%)	-5%	-5%	-8%	-9%
EV/EBITDA (x)	(14.1)	(56.6)	(73.4)	7.3
Dividend (cps)	-	-	-	-
Yield (%)	0%	0%	0%	0%
Franking (%)	0%	0%	0%	0%
ROE (%)	-33%	-9%	-8%	20%

SOURCE: BELL POTTER SECURITIES ESTIMATES

Drilling program ticks the boxes

Extensional drilling shows exceptional upside

Extension drilling at AML's 100% owned Walford Ck copper-cobalt project in QLD has continued to deliver impressive results, with the latest hole released today, WFDH378, drilled 5.7km west of the current Resource and intersecting:

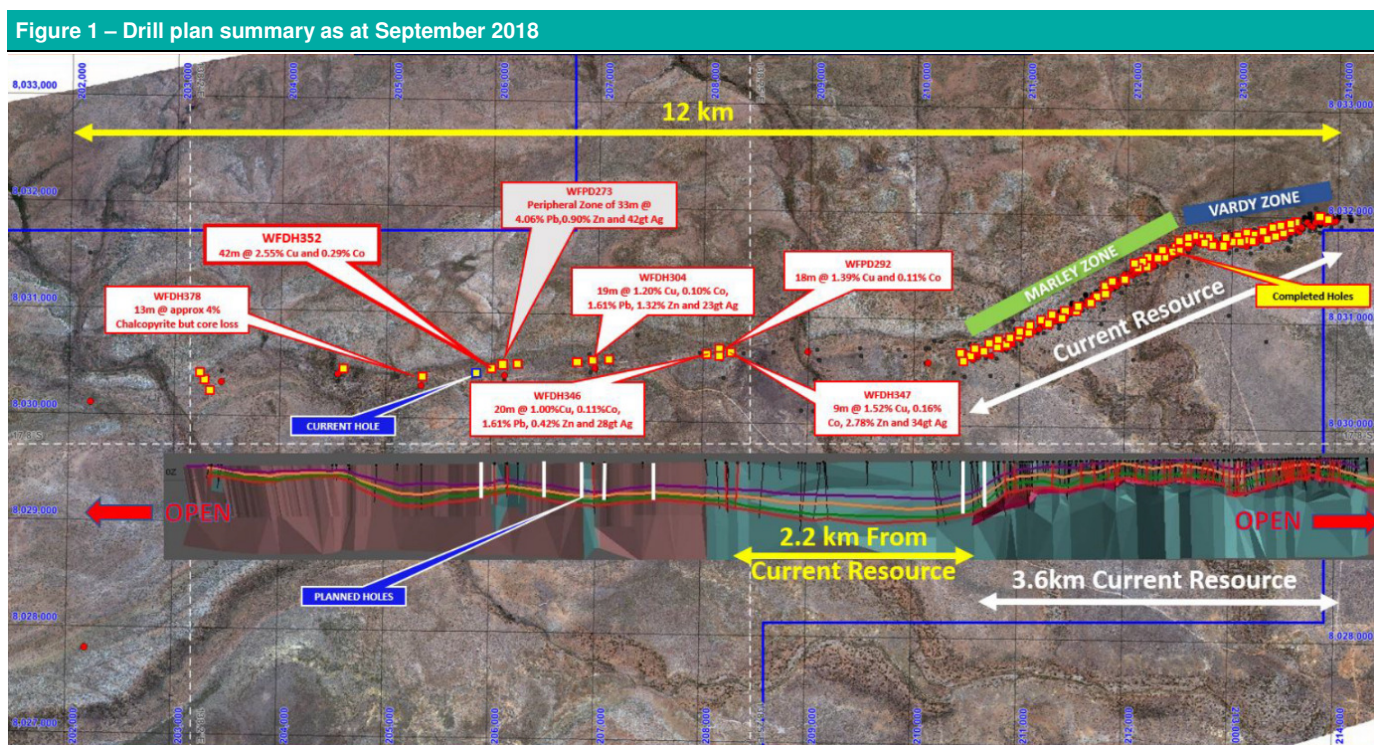
- 13m @ 3.73% Cu, 0.27% Co and 49g/t Ag from 300m; This was contiguous to
- 19m @ 4.84% Pb, 4.23% Zn, 0.06% Co and 87g/t Ag; and
- 4m @ 24.1% Pb, 4.57% Zn, 0.08% Co and 209g/t Ag

We estimate in-situ, copper equivalent grades (at spot prices) for these intersections of 13m @ 6.8% Cueq, 19m @ 4.7% Cueq and 4m @ 12.3% Cueq. We do point out that process recoveries and metallurgical testwork remains ongoing, but these results illustrate the strong mineralisation present in the system.

These exceptional results are consistent with the geological model and are 1.1km along strike from the widest and highest grade hole drilled on the project to date, WFDH352, drilled 4.6km west of the current Resource:

- 42m @ 2.55% Cu, 0.29% Co and 41g/t Ag

These holes provide further evidence of the continuity and significant growth potential of the deposit. Should portions of this be classified into the Inferred Resource category, it would likely result in a material increase to the Walford Ck Resource base.



Assays are pending, but the 2018 drill program has identified mineralised cobalt stratigraphy over ~12km of strike length, showing excellent continuity and potential for Resource growth.

2D seismic data showing potential as a targeting tool

We note that hole WFDH378 was planned using recently acquired 2D seismic data which suggested an anticlinal structure along the mineralised Fish River Fault. In correlating this data with the known Resource, a hypothesis is emerging that these anticlinal structures may be “traps” for high grade fluids in the deposit.

While this hypothesis is yet to be definitively confirmed, there is potential for this to:

- Further optimise drill hole targeting to hit high grade zones in the deposit; and
- Make a significant contribution to optimising the value of the project by enabling high grade zones to be identified early and prioritised in the mining schedule.

Infill drilling underpins in the base-case

Infill drilling has also made excellent progress and delivered impressive results. Initially targeting 30,000m of RC and diamond drilling for the 2018 program, we estimate that by the time drilling finishes up at the end of October, AML will have completed in excess of 34,000m as a result of good drill productivity. Cost efficiencies achieved due to the good run should also see the program finish in-line with the initial budget of ~\$8m.

The program has been very successful, with infill drilling returning results consistent with the known Resource and demonstrating strong continuity along strike through the Vardy and Marley zones. Increased drill density should see the bulk of an updated Resource classified into the higher confidence Measured and Indicated categories, making them available for conversion to Ore Reserves, a key milestone towards completing a Definitive Feasibility Study.

AML plans to release an upgraded Resource, utilising all of the 2018 drilling, in Q1 2019.

Changes to our valuation

We have made no material changes to our valuation other than updating for the current capital structure. These latest results and developments are consistent with our view that the Walford Creek deposit will exhibit significant growth over the coming 12 months and are reflected in our valuation.

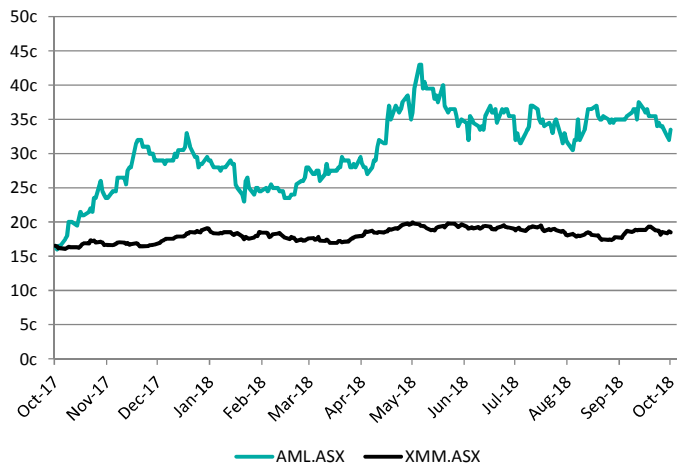
We include a standard assumption for dilution from an assumed equity raise at the current market price, of \$10.0m at \$0.335/sh. This results in incrementally more dilution than previously assumed and lowers our valuation to \$0.53/sh. Our valuation implies a 58.2% return from the last closing share price. We retain a Speculative Buy recommendation.

Upcoming catalysts

Upcoming catalysts for AML include:

- Ongoing newsflow including drilling progress and assay results from the major +30,000m infill and extension drilling program at Walford Creek. Newsflow from this program has the potential to provide strong positive catalysts for the stock price;
- Updates from the ongoing technical studies advancing the larger, upgraded Resource at Walford Creek; and
- Early in Q1 2019, the next Resource updates.

Figure 2 - AML share-price performance vs ASX Metals and Mining (re-based)



SOURCE: IRESS AND BELL POTTER SECURITIES ESTIMATES

Aeon Metals Ltd (AML)

Company description

AML is focused on the exploration and development of its flagship asset, the 100%-owned Walford Creek Copper-Cobalt Project, an advanced exploration stage project located approximately 350km north west of Mt Isa, in Queensland. Since acquiring the project in 2014, AML has completed Resource infill and extension drilling, released updated Mineral Resource estimates, progressed permitting activities and completed a Preliminary Economic Assessment.

In mid-2017 a new understanding of the deposit resulted in the development of a geological model which was subsequently used to target a diamond drilling program testing for high grade extensions of the Vardy Zone. This program was highly successful and defined an upgraded copper-cobalt Resource of 15.7Mt @ 1.24% Cu and 0.15% Co for 194kt Cu contained and 24kt Co contained. Further extension of this Resource will be targeted in 2018 and is a compelling opportunity for AML. A +30,000m diamond core and RC drilling program is underway to test this and will be the single biggest ever undertaken at the project.

Investment thesis – Speculative Buy, valuation \$0.53/sh

AML's drill program is emerging as a success on several fronts and the ~\$8m spend has been hugely value accretive with more newsflow and a key Resource update to come. Our valuation drops marginally on the latest capital structure and AML remains one of our Top Picks for 2018. We retain our Speculative Buy recommendation.

Valuation – risked discounted cash flow of key project

Our valuation for AML is broadly based on the parameters and assumptions the Vardy Zone PEA, which assumes a Mining Inventory of 3.6Mt @ 1.15% Cu, 1.06% Zn, 26g/t Ag and 1,842ppm (0.18%) Co being mined at a rate of 600ktpa. Over a six year mine-life this is planned to produce a total of 38.2kt copper in concentrate, 28.8kt zinc in concentrate and 3.2kt of cobalt in cobalt hydroxide. In addition to this, our valuation assumes further conversion from the existing Resource (15.7Mt) for a total Mining Inventory of ~10Mt. It also allows for higher grades being front-ended in the production profile (as with the PEA). We also include an exploration valuation of \$180m to reflect Resource upside and the prospectivity of AML's tenements and the likelihood of further value being added through exploration success.

NPV premium: In the case of AML, we have taken the step of applying a premium of 25% to our base-case valuation which in some circumstances we believe is justified. We believe this is the case for AML, due to a number of factors including:

- The scarcity of cobalt-exposed projects, particularly advanced stage projects, on the ASX;
- The buoyant, positive market outlook for cobalt demand; and
- A premium being paid by the market, over and above the valuations of exploration companies advancing more 'mainstream' commodity projects as a result of these factors.

Resource sector risks

Risks to AML include, but are not limited to:

- **Funding and capital management risks.** Funding and capital management risks can include access to debt and equity finance, maintaining covenants on debt finance, managing dividend payments and managing debt repayments. As an exploration company with no sales revenues, AML is reliant on access to equity markets and debt financing to fund the advancement and development of its projects.
- **Operating and development risks.** Mining companies' assets are subject to risks associated with their operation and development. Risks for each company may relate to geological, mining and metallurgical performance vs design. These can be heightened depending on method of operation (e.g. underground versus open pit mining) or whether it is a single mine company. Construction and development of mining assets may be subject to approvals timelines, receipt of permits, weather events, access to skilled labour and technical personnel, as well as key material inputs and mechanical components which may cause delays to construction, commissioning and commercial production.
- **Operating and capital cost fluctuations.** Markets for exploration, development and mining inputs can fluctuate widely and cause significant differences between planned and actual operating and capital costs. Key operating costs are linked to energy and labour costs as well as access to, and availability of, technical skills, operating equipment and consumables.
- **Commodity price and exchange rate fluctuations.** The future earnings and valuations of exploration, development and operating resources companies are subject to fluctuations in underlying commodity prices and foreign currency exchange rates. As most metal prices are denominated in US dollars, their translation into Australian dollars are affected by fluctuations in the value of the Australian dollar. Commodity price and foreign exchange rate outcomes may be different from our forecasts.
- **Resource growth and mine life extensions.** The viability of future operations and earnings forecasts and valuations reliant upon them may depend upon resource and reserve growth to extend mine lives. Exploration success is dependent upon a wide range of factors and can deliver a wide range of results. Even once Reserves have been calculated, their economic viability remains dependent upon actual commodity prices and inputs to operating costs.
- **Regulatory changes risks.** Changes to the regulation of infrastructure and taxation (among other things) can impact the earnings and valuation of mining companies. AML's key assets are located in Australia, in the State of Queensland, a politically and socially stable jurisdiction, however changes to business conditions and government policies can and have occurred, with potential for adverse impacts on the economic and social viability of AML's operations.
- **Corporate/M&A risks.** Risks associated with M&A activity include differences between the entity's and the market's perception of value associated with completed transactions, the actual performance of an acquired asset vs its expected performance as assessed by the acquiror and the timing of an acquisition may all have a material impact on the value attributed by the market to that acquisition.

Table 1 - Financial summary

PROFIT AND LOSS						FINANCIAL RATIOS							
Year ending June	Unit	2017a	2018a	2019e	2020e	2021e	Year ending June	Unit	2017a	2018a	2019e	2020e	2021e
Revenue	\$m	-	-	-	-	62.0	VALUATION						
Expense	\$m	(8.3)	(14.1)	(3.5)	(2.7)	(34.8)	NPAT	\$m	(8)	(14)	(5)	(4)	11
EBITDA	\$m	(8.3)	(14.1)	(3.5)	(2.7)	27.2	Reported EPS	c/sh	(2)	(3)	(1)	(1)	2
Depreciation	\$m	-	-	(0.0)	(0.0)	(6.0)	EPS growth	%	na	na	na	na	na
EBIT	\$m	(8.3)	(14.1)	(3.5)	(2.7)	21.1	PER	x	-14.1x	-11.9x	-39.1x	-44.6x	17.6x
Net interest expense	\$m	0.1	0.2	(1.5)	(1.7)	(10.0)	DPS	c/sh	-	-	-	-	-
PBT	\$m	(8.2)	(13.9)	(5.0)	(4.4)	11.1	Franking	%	0%	0%	0%	0%	0%
Tax expense	\$m	-	-	-	-	-	Yield	%	0%	0%	0%	0%	0%
NPAT	\$m	(8.2)	(13.9)	(5.0)	(4.4)	11.1	FCF/share	c/sh	(1)	(2)	(2)	(3)	(3)
							P/FCFPS	x	-24.5x	-22.0x	-22.2x	-12.2x	-10.8x
							EV/EBITDA	x	-23.8x	-14.1x	-56.6x	-73.4x	7.3x
							EBITDA margin	%	nm	nm	nm	nm	44%
							EBIT margin	%	nm	nm	nm	nm	34%
							Return on assets	%	-14%	-21%	-7%	-4%	8%
							Return on equity	%	-29%	-33%	-9%	-8%	20%
							LIQUIDITY & LEVERAGE						
							Net debt (cash)	\$m	30	2	11	27	45
							ND / E	%	123%	3%	20%	53%	73%
							ND / (ND + E)	%	55%	3%	16%	35%	42%
							EBITDA / Interest	x	-	-	-	-	-2.7x
							MINERAL RESOURCES						
							Walford Creek, QLD	Mt	% Cu	Cu (kt)	ppm Co	Co (kt)	
							Total resource	73	0.40%	296	813	60	
							Measured	-	-	-	-	-	
							Indicated	16	0.46%	75	914	15	
							Inferred	57	0.39%	221	785	45	
							Vardy Zone						
							Total resource	15.7	1.24%	194.0	1,552	24.4	
							Measured	1.2	1.25%	15.0	1,600	1.9	
							Indicated	3.8	1.19%	45.2	1,400	5.3	
							Inferred	10.7	1.25%	133.8	1,600	17.1	
							PROJECT ASSUMPTIONS - Vardy Zone evaluation						
							Year ending June 30	FY17	FY18	FY19	FY20	FY21	
							Currency	US\$/A\$	0.75	0.78	0.73	0.75	0.75
							Copper price	US\$/lb	\$2.44	\$3.14	\$3.18	\$3.39	\$3.47
							Cobalt	US\$/t	\$75,000	\$75,000	\$75,000	\$75,000	\$75,000
							Zinc	US\$/t	\$1.15	\$1.48	\$1.33	\$1.31	\$1.25
							CAPEX - development	A\$m	-	-	-	(10)	(34)
							CAPEX - sustaining	A\$m	-	-	-	-	(3)
							Ore milled	Mt	-	-	-	-	0.30
							Head grade	% Cu	-	-	-	-	1.35%
								ppm Co	-	-	-	-	1,800
							Production	t Cu	-	-	-	-	3,848
								t Co	-	-	-	-	270
							AISC	A\$/lb Cu	-	-	-	-	\$1.26
							VALUATION						
							Ordinary shares (m)						586.0
							Options in the money (m)						85.0
							Assumed equity raise (m)						29.9
							Diluted m						700.8
							SOTP						\$m
							Walford Ck (unrisked NPV10)						243
							Walford Ck (risk discount 25%, NPV10)						182
							Other exploration						180
							Corporate overheads						(14)
							Net cash (debt)						(2)
							Total (undiluted)						346
							Cash from options						13
							Assumed equity raise						10
							Total (fully diluted)						370
													0.53
							MAJOR SHAREHOLDERS						
													%
													m
							OCP Holdings						30.7%
							Management and Board						4.1%
							Bliss Investments						4.0%
							Washington H Soul Pattinson						2.8%
							Top 4						41.7%

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.

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

Sell: Expect <-5% 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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Disclosure: Bell Potter Securities acted as Lead Manager to the \$30.0m Placement in December 2017 and Manager to the \$5.0m Placement in August 2017 and received fees for that service.

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