

8 September 2011

Baobab Resources

Year End	Revenue (£m)	PBT* (£m)	EPS* (p)	DPS (p)	P/E (x)	Yield (%)
06/09	0.3	(1.6)	(1.9)	0.0	N/A	N/A
06/10	0.0	(2.0)	(1.4)	0.0	N/A	N/A
06/11e	0.0	(6.9)	(4.0)	0.0	N/A	N/A
06/12e	0.0	(2.5)	(1.1)	0.0	N/A	N/A

Note: *PBT and EPS are normalised, excluding intangible amortisation and exceptional items.

Investment summary: Tenge/Ruoni results

In our last update (May 2011), we discussed the prospectivity of Baobab Resources' Tenge/Ruoni target, a crescent-shaped anomaly with 3.5km of potential strike, 7.5km east of the company's projects in the Massamba Group Trend, Mozambique. Yesterday, Baobab announced positive assay results from the first two drill traverses along the northern section of the target (including 73m at 36.6% Fe, 68m at 51.0% Fe and 60m at 41.3% Fe). This news followed last week's announcement of an 113Mt inferred resource at South Zone (within the Massamba Group Trend) – which took Baobab's global inventory to 161Mt at 27% Fe.

Rapid advancement at Tenge/Ruoni

Since the commencement of exploration at Tenge/Ruoni in July 2011, drilling has intersected a mineralised unit varying in thickness from 60-150m. The package appears to be a west-northwest plunging synform – a simple structure to model and interpret, with good depth potential. Our mid-case scenario assumes that this project will host c 300Mt at 41% Fe (±30%) and adds significant value to the company's assets in Mozambique.

Valuation: 44p current, near-term 64p, possibly over £1

Baobab's shares are currently trading at a level that gives the company an enterprise value equivalent to US\$1.65 per JORC-compliant resource tonne of iron based solely on its recently increased resource of 161Mt at 27% Fe (cf an industry average for deposits of this size of US\$3.53/t). On the basis of its drillhole results to date, we estimate that the combination of the remaining resources in the Massamba Group Trend and Tenge/Ruoni may be as large 485.6Mt at 34.7% Fe (mid-case scenario). Valued at the industry average, we calculate that a resource of 161Mt at 27% Fe would support a share price of 43.9p (before dilution). Should the company prove up resources of 485.6Mt at 34.7% Fe, as stated above (as well as retaining further upside potential) Baobab could worth more than £1 per share. The company has sufficient cash to fund the entirety of 2011 exploration.

Price 21.5p
Market Cap £40m

Share price graph



Share details

Code BAO
Listing AIM
Sector Mining
Shares in issue 187.6m

Price

52 week High 53.8p Low 6.9p

Balance Sheet as at June 2011

Debt/equity (%) N/A
NAV per share (p) 0.6
Net cash (£m)* 2.0

* August 2011

Business

Baobab Resources is focused on developing its Tete iron-vanadium-titanium open-pit project in central-western Mozambique. A Pre-Feasibility Study is expected to commence in Q411.

Valuation

	2010	2011e	2012e
P/E relative	N/A	N/A	N/A
P/CF	N/A	N/A	N/A
EV/Sales	N/A	N/A	N/A
ROE	N/A	N/A	N/A

Geography based on revenues

UK	Europe	US	Other
0%	0%	0%	100%

Analyst

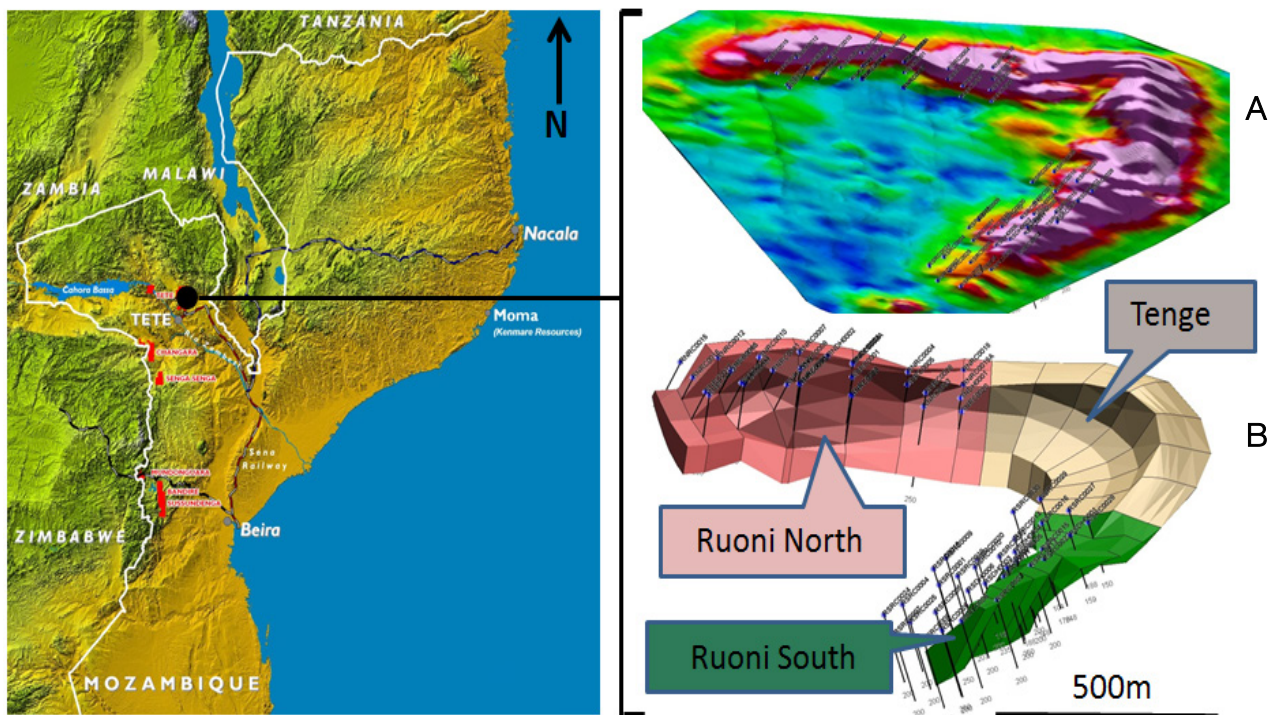
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Tenge/Ruoni delivers the goods

The Tenge/Ruoni target was acquired less than a year ago. After the assessment of geophysical data, drilling and mapping have confirmed the target's prospectively for iron, vanadium and titanium. Exploration work has defined the structure as a west-northwest plunging synform, which has been divided into three resource blocks; Ruoni North, Ruoni South and Tenge (Exhibit 1):

- Ruoni North is a south dipping (25° to 50°) 1.0 km strike along the northern limb of the target; 30 RC holes for 5,750m have been completed across seven traverses. Positive analytical results from the first two drill traverses from this block were announced on 7 September 2011.
- Ruoni South is a north dipping (c 60°) 1.2km strike along the southern limb of the target; 27 RC and diamond holes for 5,200m have been completed across the target. We are expecting extensive mineralised extensions at depth for this block.
- Tenge is the hinge zone of the fold and covers an approximate strike of 1.3km, dips are moderate and range in orientation from southwest to northwest (see image B in Exhibit 1). RC drilling on this block commenced in early September 2011 and a further two diamond rigs will be mobilised during the month. A 3,000m of phase of drilling is planned for Tenge.

Exhibit 1: Tenge/Ruoni: geophysics (A) and drilling (B) have shown the target to be a west-northwest plunging synform



Source: Baobab Resources, Edison Investment Research

Analytical results from five RC holes drilled over two cross sections spaced 170m apart on the Ruoni North block only (Exhibit 1) were announced yesterday, with significant intercepts shown in Exhibit 2.

Exhibit 2: Preliminary drill results from two traverses along the Ruoni North block at Tenge/Ruoni

HOLEID	Depth		Length	Mass		Davis Tube Recovery (DTR) product						
	(From)	(To)		Fe	Recovery	Fe	V2O5	TiO2	Al2O3	P	S	SiO2
(m)	(m)	(m)	(m)	(%)	(%)	(%)	(%)	(%)	(%)	(%)	(%)	(%)
RNRC0001	87	160	73	36.6	48.2	57.0	0.8	13.1	3.8	<0.001	0.07	0.98
RNRC0002	22	90	68	51.0	36.2	57.0	0.8	13.7	3.6	<0.001	0.06	0.79
RNRC0003	135	159	24	30.8	41.4	57.9	0.8	13.3	3.6	<0.001	0.06	0.77
RNRC0004	5	17	12	39.2	51.1	57.7	0.8	13.3	3.5	<0.001	0.04	0.84
RNRC0005	82	142	60	41.3	55.3	58.1	0.8	13.0	3.5	<0.001	0.13	0.73
and	168	180	12	37.6	43.5	60.6	0.9	9.1	2.9	<0.001	0.5	0.78

Source: Baobab Resources

While our previous spread of tonnage estimates for Tenge/Ruoni (see May 2011 note) remain essentially the same the assay results from Ruoni North produced higher than expected grades over longer intervals. Our mid-case scenario assumes that this project will host c 300Mt at 41% Fe ($\pm 30\%$) and adds significant value to the company's assets in Mozambique.

South Zone resource announced – 113Mt at 26.8% Fe

On 30 August 2011 Baobab announced a 113Mt resource for South Zone – at 28% Fe, 0.2% V₂O₅ and 10% TiO₂ this represents a c 130% increase on the company's global inventory from 47.7Mt at 25% Fe to 161Mt at 26.8% Fe (Exhibit 3). Based on c 20,000m of drilling and open along strike and at depth, the estimate was completed by international consultants Coffey Mining. A follow-up drill programme is being planned for 2012.

Exhibit 3: Baobab Resources' global JORC-compliant resources

	Tonnage											
	(Mt)	Fe%	V2O5 %	TiO2 %	SiO2 %	Al2O3	P %	CaO %	MgO (%)	Mn (%)	S (%)	
Chitongue Grande	47.7	25.3	0.2	9.7	27.9	12.32	0.023	4.44	4.19	0.19	0.26	
South Zone	113.0	27.5	0.2	10.1	25.85	8.00	0.29	5.22	6.87	0.31	0.31	
Total	160.7	26.8	0.2	10.0	26.46	9.28	0.21	4.99	6.07	0.27	0.30	

Source: Baobab Resources, Edison Investment Research

Initial metallurgical results suggest that the material will be amenable (at 23% mass recovery) to a concentrate in the order of 61% Fe, 0.66% V₂O₅ and 7.7% TiO₂ (cf 64% Fe, 0.68% V₂O₅ and 4.9% TiO₂ at mass recoveries of 20% for Chitongue Grande) and neither resource shows evidence of elevated levels of deleterious elements.

2011: a year for accelerated exploration for Baobab

Baobab's flagship asset is the Tete project (85% owned, 15% IFC), consisting of three areas of magnetite-ilmenite mineralisation: the Massamba Group Trend in the north and the satellite deposits of Tenge/Ruoni to the east and Singore to the south. Tenge/Ruoni is the focus of current work, with 11,000m of drilling already completed at Ruoni and a programme of approximately 3,000m underway at Tenge. We expect the announcement of a maiden resource over the area (covering the Ruoni zones) during Q411, followed by an update including Tenge by early Q112. A 30,000m drilling programme was planned for Tete in 2011, and despite minor setbacks in timing through the middle of the year, the company has expanded the programme to c 40,000m and is on target to complete campaigns on time and on budget. In addition to the c 31,000m already drilled (and on going) at South Zone and Tenge/Ruoni, Baobab has carried out the following work during the first three quarters of 2011:

- Drilling at the Chitongue Grande resource extension area was completed in August, with 36 RC holes for 6,275m – a resource announcement is expected during October.
- A 2,000m drilling campaign has been completed at the Monte Muande magnetite/ phosphate project with first assay results due within eight weeks. Trench sampling has also been completed to assess direct shipping ore (DSO) potential.
- The company is receiving tenders for the completion of a variety of aspects for the Pre-Feasibility Study (PFS) for Tete.
- Drilling is underway at the Mundonguara nickel / copper / gold project.

Resource

Until further updates are received, our estimates for Baobab's overall resource within the Massamba Group Trend and Tenge/Ruoni (see Exhibit 4) are as follows:

Exhibit 4: Edison estimate for Baobab's near-term resource potential

Note: * Edison estimate

	Tonnage (Mt)	Grade (Fe %)
Chitongue Grande Resource (JORC)	47.7	25.3
South Zone Resource (JORC)	113.0	27.5
Sub-total	160.7	26.8
Estimate of additional resources in the Massamba Group Trend and Tenge/Ruoni	486.6	34.7
Grand total (mid-) estimate	647.3	32.8

Source: Baobab Resources, Edison Investment Research

Valuation (diluted and undiluted)

Baobab's shares are currently trading at a level (21p) that gives the company an enterprise value of US\$1.65 per tonne of JORC-compliant iron resource (cf an industry average for resources of this size of US\$3.53/t). Exhibit 5 demonstrates the value that Baobab potentially offers investors (versus the industry average) should the company successfully increase its resource to 374Mt @ 24.4% Fe (including our lower-case inferred resource scenario for the Massamba Group Trend and Tenge/Ruoni) and 648Mt @ 31.4% Fe (including our mid-case inferred resource estimate for the Massamba Group Trend and Tenge/Ruoni – see Exhibit 4). Should the exploration results at Tenge/Ruoni match our expectations, Baobab has an implied (undiluted) value of 141p per share without attributing any value to Mt Muande or the company's Mundonguara project (nickel / copper / gold).

Exhibit 4: Tete valuation summary (not including the IFC stake) at Baobab's current valuation and the industry average

Resource	160.7Mt @ 26.8% Fe	160.7Mt @ 26.8% Fe	374Mt @ 24.4% Fe	374Mt @ 24.4% Fe	648Mt @ 31.4% Fe	648Mt @ 31.4% Fe
EV/t Fe valuation (US\$/t)	1.65	3.53	1.65	3.53	1.65	3.53
Valuation (US\$m)	60.4	129.5	128.0	274.3	285.0	610.9
Per share (US cents)*	33.8	70.6	47.8	102.5	106.5	228.3
Per share (pence)*	21.0	43.9	29.7	63.7	66.1	141.8
Share price (pence)	21.0	21.0	21.0	20.0	20.0	20.0
Discount (%)*	0.0	-52.1	-29.3	-68.6	-69.8	-85.9

Source: Edison Investment Research

Via its £17m equity facility and current cash, we estimate that the company will be able to finance the remainder of the c US\$15m required to complete a high level scoping study at Tete, advance the project through PFS and cover other running costs for 2011. The equity facility enables Baobab the right, but not the obligation, to obtain funding at any time during the next three years by way of subscriptions for new shares in the company, priced at a 6% discount to the market price at timings, intervals and in sizes determined by the company. Baobab's Tete JV partner, IFC, has committed to a pro rata contribution of c US\$1.3m to advancing exploration across the tenement this year. Exhibit 7 shows the effect of share price on Baobab's issuing shares to raise the remaining £15m of the equity facility at a range of prices (the company will draw down money at a minimum share price above 25p):

Exhibit 5: Effect of fund raisings on Baobab equity shares in issue at varying prices

Shares in issue (millions)	187.6	187.6	187.6	187.6	187.6	187.6
Funds to be raised via Dutchess facility (£m)	15.0	15.0	15.0	15.0	15.0	15.0
Additional funds to be raised (£m)	0.0	0.0	0.0	0.0	0.0	0.0
Market price at time of raising (pence)	30.00	35.00	40.00	45.00	50.00	55.00
Discounted price (pence)	28.20	32.90	37.60	42.30	47.00	51.70
New shares issued (millions)	53.3	45.7	40.0	35.6	32.0	29.1
Total shares in issue (millions)	241.0	233.4	227.6	223.2	219.6	216.7
Increase (%)	28.4	24.4	21.3	19.0	17.1	15.5

Source: Baobab Resources

Exhibit 7 shows the effect of such share issues on the valuations calculated in Exhibit 5:

Exhibit 6: Effect of fund raisings on Baobab valuation per share

Note: * See Exhibit 5.

Price at which funds raised (pence)	30.00	35.00	40.00	45.00	50.00	55.00
New total shares in issue (millions)	241.0	233.4	227.6	223.2	219.6	216.7
Valuation of US\$127.96m per share (US cents)*	53.10	54.84	56.21	57.33	58.26	59.04
Valuation of US\$274.32m per share (US cents)*	113.84	117.55	120.51	122.90	124.89	126.57
Valuation of US\$610.90m per share (US cents)*	253.51	261.79	268.36	273.71	278.14	281.87
Valuation of US\$127.96m per share (pence)*	32.98	34.06	34.91	35.61	36.19	36.67
Valuation of US\$274.32m per share (pence)*	70.71	73.01	74.85	76.34	77.57	78.62
Valuation of US\$610.90m per share (pence)*	157.46	162.60	166.68	170.00	172.76	175.08

Source: Baobab Resources

Exhibit 7: Financials

	£'000s	2008	2009	2010	2011e	2012e
Year end 30 June		IFRS	IFRS	IFRS	IFRS	IFRS
PROFIT & LOSS						
Revenue		1	276	0	0	0
Cost of Sales		(2,204)	(1,792)	(2,001)	(6,943)	(2,485)
Gross Profit		(2,202)	(1,515)	(2,001)	(6,943)	(2,485)
EBITDA		(2,202)	(1,515)	(2,001)	(6,943)	(2,485)
Operating Profit (before GW and except.)		(2,259)	(1,570)	(2,040)	(6,957)	(2,499)
Intangible Amortisation		0	0	0	0	0
Exceptionals		0	0	0	0	0
Other		0	0	0	0	0
Operating Profit		(2,259)	(1,570)	(2,040)	(6,957)	(2,499)
Net Interest		68	19	79	46	38
Profit Before Tax (norm)		(2,191)	(1,551)	(1,961)	(6,911)	(2,461)
Profit Before Tax (FRS 3)		(2,191)	(1,551)	(1,961)	(6,911)	(2,461)
Tax		0	0	0	0	0
Profit After Tax (norm)		(2,191)	(1,551)	(1,961)	(6,911)	(2,461)
Profit After Tax (FRS 3)		(2,191)	(1,551)	(1,961)	(6,911)	(2,461)
Average Number of Shares Outstanding (m)		57.0	83.4	142.1	173.3	227.6
EPS - normalised (p)		(3.8)	(1.9)	(1.4)	(4.0)	(1.1)
EPS - FRS 3 (p)		(3.8)	(1.9)	(1.4)	(4.0)	(1.1)
Dividend per share (p)		0.0	0.0	0.0	0.0	0.0
Gross Margin (%)		N/A	N/A	N/A	N/A	N/A
EBITDA Margin (%)		N/A	N/A	N/A	N/A	N/A
Operating Margin (before GW and except.) (%)		N/A	N/A	N/A	N/A	N/A
BALANCE SHEET						
Fixed Assets		114	58	28	14	0
Intangible Assets		0	0	0	0	0
Tangible Assets		114	58	28	14	0
Investments		0	0	0	0	0
Current Assets		937	530	2,318	1,897	14,043
Stocks		0	0	0	0	0
Debtors		74	2	3	0	0
Cash		863	529	2,315	1,897	10,043
Current Liabilities		(228)	(377)	(612)	(675)	0
Creditors		(228)	(377)	(612)	(675)	0
Short term borrowings		0	0	0	0	0
Long Term Liabilities		0	0	0	0	0
Long term borrowings		0	0	0	0	0
Other long term liabilities		0	0	0	0	0
Net Assets		823	211	1,733	1,236	14,043
CASH FLOW						
Operating Cash Flow		(630)	(539)	(1,538)	(6,699)	(2,981)
Net Interest		68	19	79	46	38
Tax		0	0	0	0	0
Capex		(1,554)	(1,011)	(6)	0	(4,000)
Acquisitions/disposals		0	0	0	0	0
Financing		1,795	1,197	3,251	6,235	15,089
Dividends		0	0	0	0	0
Net Cash Flow		(321)	(334)	1,786	(418)	8,146
Opening net debt/(cash)		(1,184)	(863)	(529)	(2,315)	(1,897)
HP finance leases initiated		0	0	0	0	0
Other		0	(0)	(0)	0	0
Closing net debt/(cash)		(863)	(529)	(2,315)	(1,897)	(10,043)

Source: Baobab Accounts, Edison Investment Research

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