Equity | Australia | Metals & Mining

The Royal Bank of Scotland

3 October 2011

Produced by: RBS Equities (Australia) Limited

Iron Road

Ironing out the plan

Initiation of coverage

Buy

Target price
A$0.77

Price
A$0.66

Short term (0-60 days)
n/a

Iron Road is developing the Central Eyre Iron Project, targeting 12.4Mtpa of magnetite concentrate. The project is still in the early stages, with feasibility studies and funding solutions yet to be concluded. We believe IRD offers significant potential upside to our valuation and we initiate coverage at Buy.

Key forecasts

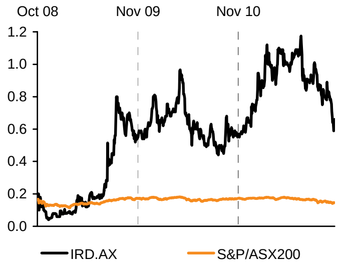
	FY09A	FY10A	FY11F	FY12F	FY13F
EBITDA (A$m)	-4.79	-11.4	-6.00	-16.0	-12.0
Reported net profit (A$m)	-4.60	-11.3	-7.72	-22.4	-22.2
Normalised net profit (A$m)[1]	-4.60	-11.3	-5.94	-17.2	-17.1
Normalised EPS (c)[1]	-7.16	-11.8	-4.59	-12.1	-12.1
Normalised EPS growth (%)	n/a	65.10	-61.1	165.2	-0.58
Dividend per share (c)	0.00	0.00	0.00	0.00	0.00
Dividend yield (%)	0.00	0.00	0.00	0.00	0.00
Normalised PE (x)	-9.21	-5.58	-14.4	-5.42	-5.45
EV/EBITDA (x)	-19.1	-7.92	-15.5	-6.46	-12.5
Price/net oper. CF (x)	-89.5	-58.1	492.9	-5.85	-7.06
ROIC (%)	0.00	-2,437	685.5	-3,593	-56.8

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

year to Jun, fully diluted

Price performance

	(1M)	(3M)	(12M)
Price (A$)	0.81	0.84	0.62
Absolute (%)	-18.0	-21.4	6.5
Rel market (%)	-12.7	-9.7	21.7
Rel sector (%)	-6.2	4.7	41.5



Market capitalisation
A$93.18m (US$90.48m)

Average (12M) daily turnover
A$0.15m (US$0.16m)

Sector: BBG AP Steel & Others
RIC: IRD.AX, IRD AU
Priced A$0.66 at close 30 Sep 2011.
Source: Bloomberg

Targeting 12.4Mtpa of magnetite concentrate production

IRD's primary asset is the Central Eyre Iron Project (CEIP) in South Australia. The company has completed a prefeasibility study on the asset, which indicated 12.4Mtpa of magnetite concentrate as a viable development option, with capex of A$2.6bn and cash operating costs of A$59/t (FOB, South Australia). We estimate first production could be as early as 2016, assuming offtake partners, a funding solution and construction progresses without major delays. The CEIP resource is large at 1.3bn tonnes, with the company outlining an exploration target of 2.8-5.8bn tonnes. Iron (Fe) content at about 17% is low relative to the majors (62%), although the strip ratio for the deposit is also low at 0.8:1. Key hurdles to move from concept to production include securing offtake agreements and a funding solution.

Looking for a partner for offtake and with funding capacity

Management has outlined a development path that could see 50% of the project sold to a larger partner that could bring offtake and debt solutions to the table. Once a development partner is introduced, IRD has suggested an overall financing structure of 70% debt/30% equity is a reasonable target. If we assume A$3bn in costs for development, and half the project is sold; we estimate IRD's equity funding obligation would be A$450m. We believe this is likely to be financed through the issue of new shares.

We initiate with a Buy recommendation and target price of A$0.77ps

There are still significant challenges ahead to move the CEIP into production. As well, the current negative sentiment related to macro economic growth concerns is likely to weigh on the stock in the near term. However, from a valuation point of view we believe the stock looks attractive. IRD offers exposure to a large resource base with significant upside potential and medium-term production opportunities. Near-term positive catalysts include potential further exploration success and the introduction of an offtake and development partner. We initiate coverage with a Buy recommendation and an NPV-based target price of A$0.77ps.

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The basics

Catalysts for share price performance

- The introduction of a JV partner to share in the development costs.
- Securing off take agreements for concentrate sales.
- The completion of a definitive feasibility study, including assessment of Stage 2 expansion options.
- Agreement on a port solution.
- Exploration success with potential upside to resources and mine life.

Earnings momentum

Near-term earnings are likely to be negative, with revenue unlikely to occur until first production (we estimate 2016). After this point, we believe earnings are likely to rise considerably with iron ore sales.

Valuation and target price

We value IRD using a DCF methodology on which we base our target price. We apply a discount rate of 10%, which is consistent with our iron ore coverage. Applying our base-case assumptions we arrive at a valuation of A$0.77ps. Key risks to our target price relate to: 1) changes material movement costs and their impact on total operating costs; 2) changes in capital costs for mine development; and 3) movements in the long-term iron ore price.

Forced ranking*

Company	Rec	Upside/ Downside
GRR	Buy	80%
GBG	Buy	77%
IRD	Buy	17%

* by difference to target price as at time of publication. Recommendations may lie outside the structure outlined in the disclosure page.
Source: RBS forecasts

How we differ from consensus

IRD is in the early development stage. We expect there to be a large spread among consensus estimates due to different assumptions on iron ore prices, funding options and ramp-up projections.

Risks to central scenario

- **Funding risk** – The success of the CEIP depends on a funding solution, which is likely to involve sale of part of the asset to a larger partner.
- **Operating costs** – The low-grade nature of the ore body means a large volume of material needs to be moved to produce 12.4Mtpa of 67% Fe concentrate. Project economics are very sensitive to movements in mining costs assumptions.
- **Development risk** – Delays to the project timing, or increases in the capex budget present risks to our central scenario.
- **Iron ore prices** – We forecast to CEIP to start production in 2016, with name plate capacity reached at our long term iron ore price of US$100/t CFR China. Project economics swing considerably with different iron ore price assumptions.
- **Sovereign risk** – The Australian Government has recently proposed new Mining and carbon taxes. Ongoing increases in tax and royalty obligations could impact our base case scenario.

Key events

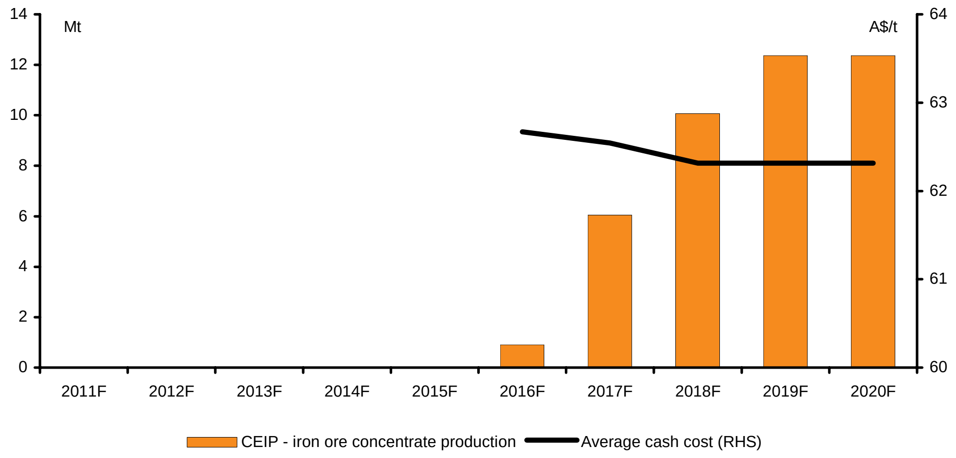
Date	Event
Oct 2011	1Q12 result
DecQ 2011	Exploration update
DecQ 2012	DFS completion

Source: Company, RBS

Key assumptions and sensitivities

We forecast project development capex of A$3bn, cash costs of A$62/t FOB (including royalties), first production in 2016, and a three-year ramp-up to a 12.4Mtpa nameplate capacity. This is more conservative than company guidance to allow for potential delays in securing necessary approvals. We also assume IRD is successful in selling 50% of the project and raising A$450m in equity to finance its share of the development.

Chart 1 : CEIP production profile (RBS est)



Source: RBS forecasts

Every A$1/t change in operating costs changes our NPV by A$48m

Sensitivity to operating costs

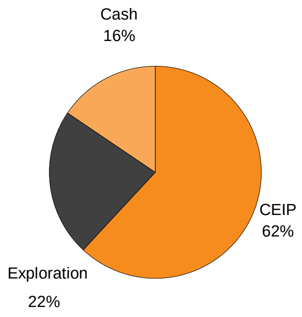
The CEIP is highly sensitive in changes in operating cost assumptions. We assume A$3/t for material movements. If we increase our mining input cost assumption to A$4/t, cash costs increase from A$60/t to A$70/t. Each A$1/t of material moved equates to about A$10/t of concentrate. Processing costs are also critical. We assume A$3.5/t of ore processed. We note that each A$1/t increase in processing cost increases our overall cash costs by A$5.5/t. For every A$1/t change in our operating costs per tonne of concentrate sold, our NPV changes by A$48m.

Sensitivity to movements in iron ore prices

The project hits full production at our long-term price. Our current long-term forecast for iron ore is US$85/t (62% dry fines, FOB Australia). We estimate each US$1/t change in our long-term iron ore price changes our NPV by 0.53ps.

Company snapshot

Chart 2 : NPV split



Source: RBS estimates

IRD is an iron ore exploration company with projects located in South Australia. Its key project is the Central Eyre Iron Project (CEIP), with a magnetite iron ore resource base of 1.3bn tonnes (16.8% grade Fe). Management is targeting 12.4Mtpa of iron ore concentrate production. Funding and production offtake are currently being sought by IRD. Management has not yet set an official target date for the commencement of construction and initial production, although we assume first iron ore shipment in 2016 is achievable.

The company also has two additional projects, the Gawler Iron Project and the Windarling Iron Project. The Gawler Iron Project is located within 100km of the Central Australia Railway in South Australia, and is a 90% farm-in agreement with tenement holder, Kingsgate Consolidated Limited (through Dominion Mining). The Windarling Iron Project is located 85km to the north of Koolyanobbing, Western Australia, and is a 75% farm-out agreement with Convergent Minerals. Both projects are early stage and are not included in our NPV.

Central Eyre Iron Project overview

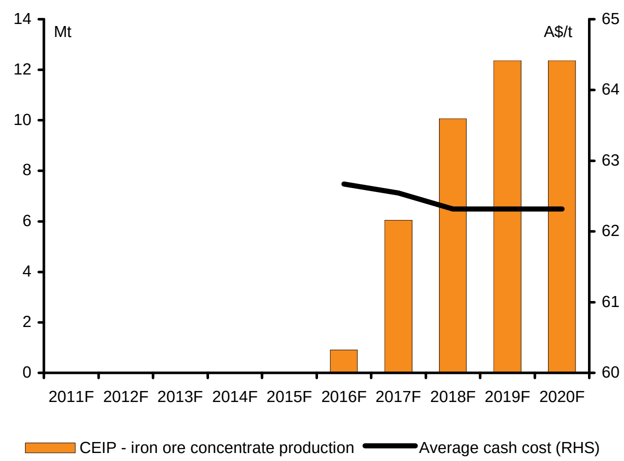
The Central Eyre Iron Project (CEIP) is a large magnetite resource located in South Australia, roughly 200km west of Whyalla and 180km North of Port Lincoln. The project has a 1.3bn tonne magnetite JORC resource (16.8% grade Fe). After processing into an iron ore concentrate product, we estimate this equates into approximately 244Mt of saleable product at 67% grade Fe. Management has a target to expand the size of the resource to 2.8bn to 5.8bn tonnes through further exploration.

A prefeasibility study (PFS) on the CEIP was recently completed based on a 12.4Mtpa iron ore concentrate operation. The study estimates capital costs for the project of A$2.6bn with cash operating costs of A$59/t (FOB, South Australia). Management's current forecasts are based on a Stage 1 scenario. A definitive feasibility study (DFS) will examine the potential of increasing production by 50-100% through a Stage 2 expansion. Our base-case valuation scenario assumes first concentrate production in FY16, with full ramp-up to 12.4Mtpa by FY19.

Chart 3 : Central Eyre Iron Project – location

Source: IRD

Chart 4 : Forecast production profile



Source: RBS forecasts

Operating cost review – mining costs a large swing factor

The most important input cost is material movements; operating costs increase A$10/t for each A$1/t lift material movement

The CEIP is based on conventional open pit mining. The relatively low-grade ore requires beneficiation in order to become a saleable product. Key findings in the PFS were a process rate of 67.6Mtpa @17% Fe to produce 12.4Mtpa of concentrate at 67% Fe. The average strip ratio is 0.8:1 (waste/ore), producing total material movements of 122Mtpa at full production. While the headline strip ratio is modest for an iron ore operation, it equates to about 5:1 on 59% Fe equivalent (FMG's iron ore grade), which is relatively high, in our view. This means operating costs will be particularly sensitive to mining costs. IRD has not broken down the estimated cost of A$59/t (ex-royalty) into mining, processing and transport components, although we estimate the following cost structure:

Table 1 : RBS operating cost assumptions

Description	Cash cost (A$/t)
Mining	30.00
Processing	18.50
Transport (slurry)	3.50
Port handling	3.00
Port fees	6.00
Total (ex-royalty)	**60.00**

Source: Company data, RBS forecasts

We note that if we increase our mining input cost assumption to A$3/t, cash costs increase from A$60/t to A$70/t. Each A$1/t of material moved equates to about A$10/t of concentrate.

Processing – coarse grind minimises energy requirements

Table 2 : Input assumptions

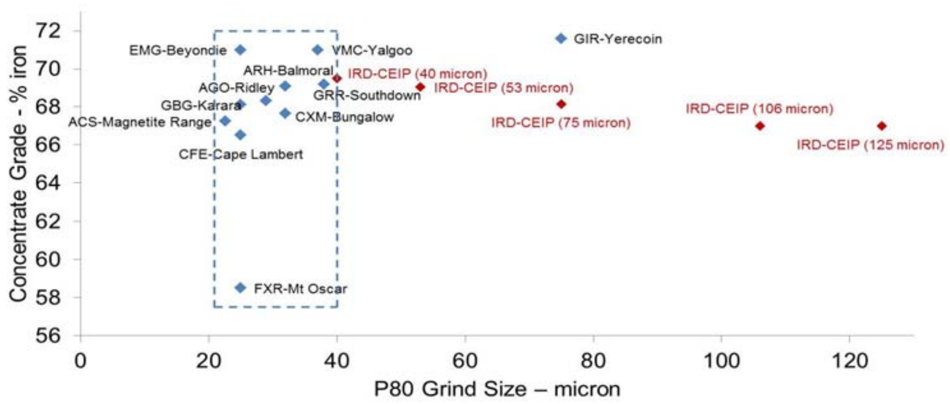
Description	(A$/t)
Mining (A$/t material)	2.00
Processing (A$/t ore feed)	3.50
Slurry (A$/t concentrate)	3.00
Port (A$/t concentrate)	9.00

RBS estimates

IRD has proposed a 67.6Mtpa processing plant to produce 12.4Mtpa of iron ore concentrate grading 67%. The company states the grind size will be relatively coarse 106 microns, which is high relative to peers. IRD believe this coarse grind provides a competitive advantage on the basis that less energy is required than peers. The larger grind size also allows the concentrate to bypass the pelletisation process and be used directly as a sinter blending product. We understand at 106 microns the concentrate can account for up to 10-20% of the sinter blend. IRD is investigating the potential for an even coarser product at 125 microns, which could see our operating cost assumptions decline.

While the processing plant looks relatively efficient compared to peers, it is still quite large due to the significant beneficiation requirement. We note that each A$1/t increase in processing cost increases our overall cash costs by A$5.5/t.

Chart 5 : Concentrate grind size for various projects



Source: Company data

Port access and infrastructure

Construction of a port at Sheep Hill has been proposed by the Erye Iron JV (Wuhan/Centrex)

Based on the findings of the PFS, the project is likely to source power from the grid, with a slurry pipeline to port providing the transport solution. The PFS includes costs and charges to use a third-party port, most likely at Sheep Hill. Construction of the port is currently being proposed by the Eyre Iron JV owned by Wuhan Steel and Centrex Metals. According to the proposed timeline from Centrex Metals, construction of the port would commence in 3Q13 with the port export ready by 3Q14. On 6 January 2011, the proposed Port Project was declared a 'major project' by the South Australian Minister for Urban Development and Planning.

IRD is now commencing the DFS, aimed at expanding the mineral resource base and exploring the option of a Stage 2 expansion. Management estimates if the resources are sufficiently expanded, this could increase production by a further 50-100%. Increasing production to this level could lead to a preference for rail versus slurry transport, and could justify a standalone port development for the project if required. Until completion of the DFS, however, we retain our base case assumptions that relate to the PFS Stage 1 scenario.

Offtake and partnerships

IRD is yet to enter into an offtake agreement for the project, which in our view is likely to coincide with a potential funding solution. In our view, the project may need multiple offtake partners if the concentrate is marketed purely as an sinter blending product. Due to the fineness of the ore, limiting the concentrate to 10-20% of the sintering blend, we do not believe one steel producer would be able to handle all CEIP concentrate alone without pelletisation. We suggest the most likely partnership(s) will occur with a large Asia-based steel producer due to proximity and capacity to receive offtake. We have listed the 15 largest producers in Asia below for reference.

Table 3 : 15 largest steel producers in Asia

Company	Headquarters	2010 crude production (Mt)*
Nippon Steel (incl Sumitomo)	Japan	48
Hebei Iron and Steel	China	45
Ansteel Group (incl Pangang & Sansteel)	China	46
Baosteel Group	China	37
Wuhan Iron and Steel Group	China	37
POSCO	South Korea	35
JFE	Japan	31
Jiangsu Shagang	China	23
Shandong Iron and Steel Group	China	23
Tata Steel	India	23
Maanshan Iron and Steel Company	China	15
Shougang	China	15
Steel Authority of India Limited	India	14
China Steel	Taiwan	13
Valin Steel Group	China	11

* Production figures has been consolidated in situations where mergers have subsequently occurred.
Source: World Steel Association, Company data, RBS

Product quality and pricing

We estimate CEIP will achieve a price equal to benchmark Hamersley fines on a dtmu basis

We believe the high iron content, low impurities and ability to use in the sintering blend add to the appeal of Central Eyre Iron Project concentrate product. Sintering of CEIP concentrate gives IRD access to a larger number of potential customers compared to typical concentrate product and allows customers to blend with lower quality feed stock with the cost advantage of not having to pelletise. We estimate CEIP will achieve an iron ore price equal to benchmark Hamersley fines on a dtmu basis. We have not included a premium for CEIP's low levels of impurities; however, we note that Gindalbie's Karara concentrate achieves a 9-11% premium for its low impurity levels.

Table 4 : Low-impurity magnetite concentrate product

	Fe % (iron)	SiO2 % (silica)	Al2O3 % (alumina)	P % (phosphorus)
CEIP iron ore concentrate	**67%**	**4.0%**	**1.9%**	**0.01%**
Karara iron ore concentrate	68%	4.8%	0.1%	0.01%
Hamersley Pilbara blend	62%	3.6%	2.1%	0.10%

Source: IRD, GBG

Capital expenditure and funding

IRD estimates capex of A$2.6bn for the project. The current market capitalisation of IRD is slightly less than A$100m. Management has outlined a development path that could see 50% of the project sold, with a potential partner bringing offtake and funding. IRD has suggested an overall financing structure of 70% debt/30% equity is a reasonable target. Based on our A$3bn forecast capex assumption, if half of the project was sold IRD would incur a A$450m funding obligation under this structure. We believe this is likely to be sourced through an equity raising of similar size, less any proceeds from the sale of IRD's 50% share.

Our A$3bn capex estimate is inline with Gindalbie and Grange on an A$/t capacity basis

Our base-case scenario for CEIP assumes A$3bn capital cost to build the stage one 12.4Mtpa iron ore concentrate operation about 15% higher than management's A$2.6bn estimate. Based on capital intensity per tonne of annual production, this equates to A$242/t. This is in line with comparable magnetite concentrate developments; including Gindalbie Metals Karara project at A$225/t and Grange Resources Southdown project at A$258/t.

Table 5 : IRD capex budget

Direct Costs	Estimated A$ Millions	Indirect Costs	Estimated A$ Millions	Contingency	Estimated A$ Millions
Crushing circuit	244.1	Field indirect – 12.0%	209.3	Direct and indirect – 15%	337.8
Fine grind & mag sep	152.4	EPCM – 8.0%	139.5		
Milling area & infrastructure	294.1	Vendor reps – 1.5%	26.2		
Tailings handling	59.3	Capital spares – 4.0%	69.8		
Desalination plant	76.9	Commissioning – 0.5%	8.7		
Port facility	117.7	First fills	2.2		
Pipelines, pump stations	463.0	Insurances – 3.0%	52.3		
Plant services	6.1				
Power lines and coms	170.5				
Tailings dam - prework	160.2				
Total directs	**1744.3**	**Total indirects**	**508.0**	**Total contingency**	**337.8**

Source: Company data

IRD share register

Substantial holders appear to be long term supporters, suggesting they may take up an entitlement offer if this were to occur

We believe the IRD register is positive from a funding point of view. The Sentient Group, Columbia University & Duke University appear to be long-term supporters of management and the project, which suggests they may take up an entitlement offer if this were to occur.

Table 6 : Material shareholders

Shareholder	Type	Holding
The Sentient Group	Private equity	30.7%
Management	Various management	10.4%
Columbia University	Investment fund	6.6%
Duke University	Investment fund	6.2%
Top Holders		**53.9%**

* Note University holdings are spread through a number of companies.
Source: Company data, RBS forecasts

Investment view

There are still significant challenges ahead to move the CEIP into production. However, we believe the stock looks attractive from a valuation point of view. Further, we note that iron ore prices remain firm despite the downturn in equity markets. IRD offers exposure to a large resource base with significant upside potential and medium-term production opportunities. We initiate coverage with a Buy recommendation. Our target price is set at our NPV-based valuation of A$0.77ps. Key near-term catalysts include the introduction of a development partner, the establishment of offtake agreements and potential exploration success.

Risks to target price

Downside

- Higher capital costs than anticipated.
- Higher operating costs than our forecasts.
- Lower iron ore prices than our forecasts.

Upside

- Lower capital costs than anticipated.
- Lower operating costs than our forecasts.
- Higher iron ore prices than our forecasts.

IRD – financial summary

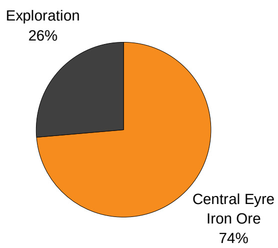
Capital profile			
Number of shares (m)	141		
Market capitalisation (A$m)	93		
Enterprise value (A$m)	93		
Enterprise value (US$m)	93		

Resources			
Magnetite resources (Mt)	1334	16.8%	Fe
Magnetite reserves (Mt)	na		
Concentrate resources (Mt)	244	67.0%	Fe
EV/t conc resource (A$/t)	0.38	0.38	(US$/t)
EV/t conc reserve (A$/t)	na	na	(US$/t)

Valuation

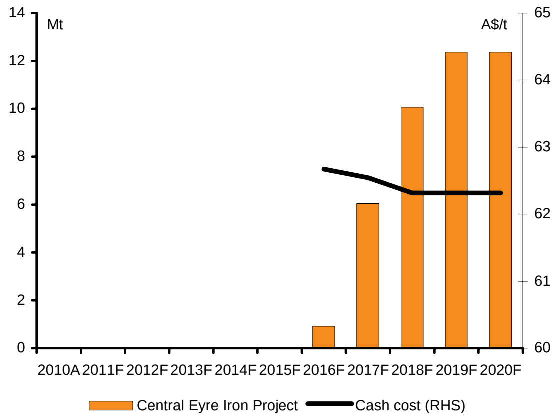
Description	A$m	A$ps
Central Eyre Iron Ore	72	0.51
Exploration	26	0.18
Net cash (debt)	18	0.13
Corporate	-7	-0.05
Total Valuation	**108**	**0.77**
P/NPV		0.86

NPV split



Valuation inputs	
Rf rate	5.3%
MRP	6.0%
Equity beta	1.30
Ke	13%
Kd	7.0%
Gearing	30%
Tax rate	30%
WACC	11%
DCF (A$)	0.77
Prem/disc	0%
Target (A$)	0.77

Production and costs



June year end	2010A	2011F	2012F	2013F	2014F
NPAT Reported (A$m)	-11	-4	-12	-12	-32
NPAT Normalised (A$m)	-11	-4	-12	-12	-32
EPS (A¢)	-18	-4	-9	-8	-22
CFPS (A¢)	-13	-14	-23	-33	-327
DPS (A¢)	0.0	0.0	0.0	0.0	0.0
P/E (x)	nm	nm	nm	nm	nm
P/CF (x)	nm	nm	nm	nm	nm
EV/EBITDA (x)	nm	nm	nm	nm	nm
EPS Growth	nm	nm	nm	nm	nm
Yield (%)	0.0	0.0	0.0	0.0	0.0
Assumptions FY	**2010A**	**2011F**	**2012F**	**2013F**	**2014F**
AUD/USD	0.88	0.99	1.07	1.10	1.03
Iron ore fines (US¢ dmtu) - benchmark	119	249	260	234	211
Iron ore concentrate (US$/t) - achieved					
Production	**2010A**	**2011F**	**2012F**	**2013F**	**2014F**
Central Eyre Iron Ore (Mt)	0	0	0	0	0
Cash costs (incl royalties)	**2010A**	**2011F**	**2012F**	**2013F**	**2014F**
Average cash cost (A$/t)					
Average cash cost (US$/t)					
Profit and Loss ($m)	**2010A**	**2011F**	**2012F**	**2013F**	**2014F**
Revenue	0	0	0	0	0
Costs	11	6	16	12	6
EBITDA	-11	-6	-16	-12	-6
Depreciation & amortisation	0	0	0	0	0
EBIT	-11	-6	-16	-12	-6
Interest income	0	0	0	0	1
Interest expense	0	0	1	6	40
MRRT	0	0	0	0	0
Pre tax profit	-11	-6	-17	-17	-45
Tax expense (benefit)	0	-2	-5	-5	-14
NPAT - underlying	-11	-4	-12	-12	-32
Significant items	0	0	0	0	0
NPAT - reported	-11	-4	-12	-12	-32
Profitability analysis	**2010A**	**2011F**	**2012F**	**2013F**	**2014F**
EBIT margin	-	-	-	-	-
EBITDA margin	-	-	-	-	-
Effective tax rate	30%	30%	30%	30%	30%
ROA - EBIT / (total assets - cash)	-157%	-407%	-43%	-16%	-1%
ROE - NPAT / equity	nm	nm	nm	nm	nm
Cashflow	**2010A**	**2011F**	**2012F**	**2013F**	**2014F**
EBITDA	-11	-6	-16	-12	-6
Operating cashflow	-1	0	-16	-13	-11
Capex	0	0	-16	-34	-450
Free cashflow	-1	0	-32	-47	-461
Investing cashflow	-6	-16	-16	-34	-450
Financing cashflow	9	13	42	49	465
Net Change in cash	2	-3	10	2	4
Balance Sheet Analysis	**2010A**	**2011F**	**2012F**	**2013F**	**2014F**
Debt	0	0	20	69	534
Equity	2	0	5	-8	-18
Assets	4	1	27	63	517
Cash	3	0	10	12	15
Net debt	-3	0	10	57	519
Gearing - net debt/equity	nm	nm	nm	nm	nm
Gearing - net debt/ (net debt + equity)	nm	nm	nm	nm	nm
Net debt / EBITDA	5.2	5.2	5.2	5.2	5.2
EBIT / net interest	119.4	93.9	-13.3	-2.4	-0.2
EBITDA / net interest	119.3	93.9	-13.3	-2.4	-0.2

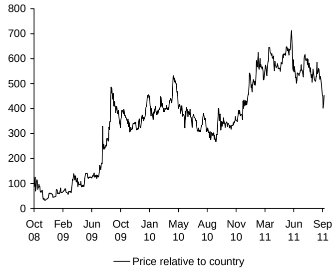
Source: Company data, RBS forecasts

Company description

Buy

IRD is an iron ore exploration company with projects located in South Australia. Its key project, the Central Eyre Iron Project, has a magnetite iron ore resource base of 1.3bn tonnes (16.8% grade Fe). Management is targeting 12.4Mtpa of iron ore concentrate production based on the prefeasibility study findings. Other projects include Gawler Iron Project, a 90% farm-in agreement with Dominion Mining located 100km off the Central Australia Railway in SA, and the Windarling Iron Project, a 75% farm-out agreement with Convergent Minerals located north of Koolyanobbing.

Price relative to country



Strategic analysis

Average SWOT company score: 2

Strengths — 4

A long-life open-pit mining operation, with potential longer-term expansion potential. Larger grind size allows concentrate to be used as a sintering blend, allowing the cost of conversion into pellet to be bypassed. The high 67% Fe grade attracts a premium to benchmark prices.

Weaknesses — 1

Low magnetite grade leads to significant material movements. The beneficiation requirement adds to operating costs. Limitations to the amount of concentrate used in the sintering blend may necessitate multiple offtake partnerships. Port infrastructure relies on a third party for construction.

Opportunities — 3

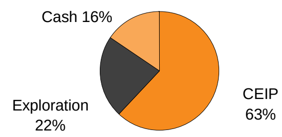
Further exploration may lift the resource base from 1.3bn tonnes to 2.8bn-5.8bn tonnes at CEIP. The DFS may suggest a Stage 2 increase in annual production levels is possible. There is potential for advances at the Windarling and Gawler projects.

Threats — 1

The high capital intensity requirement for magnetite projects leads to the risk of construction cost escalation. The ability to secure offtake agreements and obtain project funding remains uncertain with competition from numerous other prospective Australian magnetite projects.

Scoring range is 1-5 (high score is good)

IRD NPV split



Source: RBS estimates

Market data

Headquarters
35 Havelock Street, West Perth, WA 6005, Australia

Website
www.ironroadlimited.com.au

Shares in issue
141.2m

Freefloat
46%

Majority shareholders
The Sentient Group (31%), Management (10%), Columbia University (7%)

Country view: Australia

Australia underperformed the region during the second quarter, led by declines in the energy, materials, industrials and the healthcare sectors. We expect underperformance to persist given the possibility of further policy tightening (which the market appears not to be pricing in), coupled with likely weakness in commodities.

The country view is set in consultation with the relevant company analyst but is the ultimate responsibility of the Strategy Team.

Country rel to Asia Pacific

Competitive position

Average competitive score: 2-

Supplier power — 1-

Supplier power depends on the construction of a port to support CEIP and the extent to which production is fully contracted out.

Barriers to entry — 4+

Funding, infrastructure and high production costs for magnetite iron ore are likely to keep barriers to entry high for new projects in the medium term.

Customer power — 1-

Customer power will remain strong until an offtake and project development partner is found for production.

Substitute products — 1+

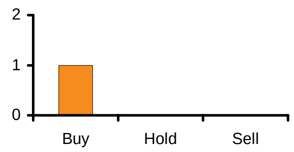
Magnetite iron ore can be substituted for fines or lump iron ore. In the longer term we anticipate the higher-grade and low-impurity qualities of magnetite concentrate to enhance its appeal.

Rivalry — 2-

Competitive rivalry is intense in finding production offtake and funding partners. Once in production we anticipate rivalry to be limited, assuming an offtake partner is found.

Scoring range 1-5 (high score is good) Plus = getting better Minus = getting worse

Broker recommendations



Source: Bloomberg

Recommendation structure

Absolute performance, short term (trading) recommendation: A Trading Buy recommendation implies upside of 5% or more and a Trading Sell indicates downside of 5% or more. The trading recommendation time horizon is 0-60 days. For Australian coverage, a Trading Buy recommendation implies upside of 5% or more from the suggested entry price range, and a Trading Sell recommendation implies downside of 5% or more from the suggested entry price range. The trading recommendation time horizon is 0-60 days.

Absolute performance, long term (fundamental) recommendation: The recommendation is based on implied upside/downside for the stock from the target price and, except as follows, only reflects capital appreciation. A Buy/Sell implies upside/downside of 10% or more and a Hold less than 10%. For UK-based Investment Funds research, the recommendation structure is not based on upside/downside to the target price. Rather it is the subjective view of the analyst based on an assessment of the resources and track record of the fund management company. For research on Australian listed property trusts (LPT) or real estate investment trusts (REIT), the recommendation is based upon total return, ie, the estimated total return of capital gain, dividends and distributions received for any particular stock over the investment horizon.

Performance parameters and horizon: Given the volatility of share prices and our pre-disposition not to change recommendations frequently, these performance parameters should be interpreted flexibly. Performance in this context only reflects capital appreciation and the horizon is 12 months.

Market or sector view: This view is the responsibility of the strategy team and a relative call on the performance of the market/sector relative to the region. Overweight/Underweight implies upside/downside of 10% or more and Neutral implies less than 10% upside/downside.

Target price: The target price is the level the stock should currently trade at if the market were to accept the analyst's view of the stock and if the necessary catalysts were in place to effect this change in perception within the performance horizon. In this way, therefore, the target price abstracts from the need to take a view on the market or sector. If it is felt that the catalysts are not fully in place to effect a re-rating of the stock to its warranted value, the target price will differ from 'fair' value.

Distribution of recommendations

The tables below show the distribution of recommendations (both long term and trading). The first column displays the distribution of recommendations globally and the second column shows the distribution for the region. Numbers in brackets show the percentage for each category where there is an investment banking relationship. These numbers include recommendations produced by third parties with which RBS has joint ventures or strategic alliances.

Long term recommendations (as at 03 Oct 2011)

	Global total (IB%)	Asia Pacific total (IB%)
Buy	851 (11)	552 (3)
Hold	409 (7)	224 (4)
Sell	87 (5)	48 (0)
Total (IB%)	1347 (9)	824 (3)

Source: RBS

Trading recommendations (as at 03 Oct 2011)

	Global total (IB%)	Asia Pacific total (IB%)
Trading Buy	1 (100)	1 (100)
Trading Sell	1 (0)	1 (0)
Total (IB%)	2 (50)	2 (50)

Source: RBS

Valuation and risks to target price

Iron Road (RIC: IRD.AX, Rec: Buy, CP: A$0.660, TP: A$0.768): We value IRD based on a DCF methodology. Key risks to our target price relate to: 1) changes in material movement costs and their impact on total operating costs; 2) changes in capital costs for mine development; and 3) movements in the long-term iron ore price.

Regulatory disclosures

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