RFC Ambrian

Metals & Mining

4 June 2014

Orbis Gold (OBS-AU)

Price: A$0.29 **Recommendation:** Buy **Target Price:** A$0.70 **Market Cap:** A$73m

Hefty Upside Implied by Papillon Agreement

We believe that the merger implementation agreement announced by Papillon Resources has significant positive implications for Orbis Gold, the company focused on the discovery and development of large-scale gold deposits in Burkina Faso.

Papillon and B2Gold have announced an agreement to combine the two companies at an exchange ratio of 0.661 B2Gold common shares for each Papillon share held. The consideration represents a purchase price of approximately A$1.72/Papillon share and values the transaction at approximately A$615m, a 36.5% premium (based on the last traded pricing of B2Gold shares at the time of the offer on 23 May). Since Papillon went into a trading halt on 26 May the B2Gold share price has fallen and at today's share price (at the ASX opening) the offer would be valued at A$1.68/Papillon share and values the deal at approximately A$572m, an 18% premium.

Comment

Given the relatively 'unloved' state of the West African gold sector at the moment, we expected longer-term players in the gold space to move in and make acquisitions. Papillon had previously been flagged by us as a target (as has Orbis). Now that Papillon is on the move we suspect that Orbis could be next. So how does Orbis compare with Papillon?

Comparing Natougou and Fekola

Papillon's flagship asset, Fekola, is an excellent quality 5.15Moz resource in south-west Mali. An impressive PFS has significantly de-risked the project and determined an average life-of-mine production rate of 306,000oz pa of gold over a nine-year mine life at a head-grade of 2.7 g/t Au and a strip ratio of 4.3:1. Metallurgical recoveries are estimated at 92%, with initial capex at US298m.

Natougou, Orbis' flagship asset, is a high-quality 1.8Moz resource in southern Burkina Faso. A scoping study has been completed on the project and we have used this to determine average life-of-mine production of 150,000oz pa of gold over an eight-year mine life at a head-grade of 3.5 g/t Au and a strip ratio of 13:1. Metallurgical recoveries are estimated at 93%, and we forecast initial capex at US$220m.

The table below summarises the valuation per tonne of ore at each project based on mining, processing and general admin costs (outlined in the relevant studies) using a US$1,300 long-term gold price.

Natougou and Fekola Comps (US$)

Project/Value	Natougou	Fekola
Head Grade (g/t Au)	3.5	2.7
Strip Ratio	13:1	4.33:1
Metallurgical Recovery (%)	93	92
Mining Cost per Tonne Mined	2.40	4.07
Mining Cost per Tonne Ore	33.60	21.69
Processing Cost per Tonne Ore	22.31	19.40
G&A per Tonne Ore	7.24	2.50
Total Cost per Tonne Ore	63.15	43.59
Revenue per Tonne Ore	136.05	103.82
Gross margin per Tonne Ore	72.90	60.23

Of course, these costs are before capital, royalties and other costs, but the indication here is that — despite a relatively high strip ratio — the gross margin expected on a tonne of ore from Natougou is US$72.90 vs. US$60.23 at Fekola. This is because Natougou's superior grade generates greater revenue per tonne of ore. While there is a lesser degree of technical risk associated with a PFS as opposed to a scoping study, we would argue that a project in southern Burkina Faso faces less financing risk than one in Mali.

Valuation

Based on the above we feel that it would be reasonable to compare the valuation of Papillon's *in situ* ounces with the current market valuation of Orbis' *in situ* ounces.

Implied Valuation of Attributable *In situ* Ounces

Company	Attributable Resources (Moz)	Valuation/EV (A$m) Before Capex	Valuation/oz (A$)
Papillon	4.63	573	124
Orbis	2.46	65	26

If Orbis was valued for attributable ounces in the ground at the same valuation as Papillon, it would have an Enterprise Value of A$304m and a market cap of A$314m. This represents an implied value per share of A$1.43, a whopping premium of 377% to today's share price and 104% above our target price.

Below we look at the implied valuation of both companies' assumed average life-of-mine production pa.

Implied Valuation of Attributable Forecast Annual Production Ounces

Company	Attributable Production (000oz)	Valuation/EV (A$m) Before Capex	Valuation/oz pa (A$)
Papillon	260	573	2,200
Orbis	135	65	480

If Orbis was valued for attributable ounces of production pa at the same valuation as Papillon, it would have an Enterprise Value of A$297m and a market capitalisation of A$307m. This represents an implied value per share of A$1.40, a premium of 367% to today's share price and 100% above our target price.

Whilst the above is all very interesting, we have always believed that Fekola is a world-class deposit that should be valued at a premium. We are not suggesting that Orbis should be valued at the same premium as Papillon, but Orbis' main asset is a shallow, predictable, high-grade open-pittable resource and we use the above discussion merely to suggest that the market is discounting Orbis by significantly more than it should. We feel this provides additional justification for our discounted NAV valuation of A$153m, or A$0.70/share.

On a simple price-to-NAV metric Papillon's takeover valuation represents a P/NAV of 0.96x, while Orbis currently trades at a P/NAV of 0.41x.

With improved metallurgical studies and an indicated resource due next quarter, we think that the technical risk being applied to the Natougou scoping study will be reduced significantly and anticipate that this will provide greater comfort to potential investors and possible acquirers.

The following table summarises the takeover premium applied to three recent takeover offers in the West African gold sector. If an offer was made today one might expect an average takeover premium of 47% on Orbis' 20-day VWAP of A$0.30, giving a market valuation of A$0.44.

Implied Takeover Premium of Recent Transactions in the West African Gold Sector

Takeover target	Offer price/share	Share price on day (ASX Open)	Premium on day announced	20 day VWAP on day announced	Premium to 20-day VWAP
PMI Gold Corp	A$0.47	A$0.30	57%	A$0.33	43%
Ampella Mining	A$0.16	A$0.08	100%	A$0.10	61%
Papillon Resources	A$1.68	A$1.43	18%	A$1.32	36%

None of the valuation metrics outlined above (with the exception of our discounted NAV) reflect Orbis' significant exploration potential at the Natougou Project (outside the current resource) or the Bantou Project; these could be viewed as additional upside.

Recommendation

We continue to rate Orbis Gold as a **BUY**. We have completed a sum-of-the-parts valuation for the company and determined **a fair value of A$0.70/share** based on current information. We suspect Orbis is a likely candidate for an M&A deal in the West African gold sector and highlight above that on various different valuation metrics Orbis looks undervalued in the sector.

Catalysts going forward include:

- Exploration drilling — Ongoing
- Natougou resource upgrade — Mid-2014
- Natougou metallurgical studies — Mid-2014
- Takeover offer —Potentially ongoing