

WPG Resources Limited

WPG to sell its Iron Ore assets to OneSteel for \$346m

- WPG recently announced the intended sale of its Peculiar Knob and Hawks Nest Iron ore projects to OneSteel and is seeking approval for the sale at a General Meeting on 4 October 2011.
- The proposed sale values the iron ore assets of WPG, which includes the fully permitted and fully funded Peculiar Knob project, at \$346m or \$1.40 per share.
- After the accrual of tax to be paid for the capital gains made on the assets, WPG intend to distribute \$1.05 per share in a cash payment to all shareholders.

What do shareholders get?

- Shareholders will receive a cash payment and a franking credit. This includes:
 - (i) Capital Return of 42cps,
 - (ii) Fully franked dividend of 63cps (with an attaching franking credit of 27cps).
- The total package, including the franking credit, totals \$1.32 per share. The capital return and dividend will be paid on 1 November 2011 with the record date set at 14 October 2011.

Veritas view

- Our NAV for the Peculiar Knob operation at 3.3mtpa is \$1.32 per share, which we see as a base case. Our upside NAV scenario of \$1.90 per share is based on the expected 5.0mtpa operation at the end of 12 months and includes reserves from Buzzard and Tui.
- The total cash payment and franking consideration of \$1.32 per share compares favourably to our 3.3mtpa base case NAV. On this basis we see the sale price of \$346m (\$1.40/sh) as fair in the current turbulent equities market.

Recommendation

- The cash payment (\$1.05/sh), franking credit (\$0.27/sh) plus our WPG rump valuation (\$0.15/sh) provides for a combined value of \$1.47 per share. This combined valuation is within our net asset value range of \$1.32 (3.3mtpa) to \$1.90 (5.0mtpa) per share.
- In the absence of a higher offer we recommend that shareholders vote in favour of the transaction at the General Meeting to be held on 4 October 2011.

WPG.ASX

ACCEPT

Monday 19 September 2011

Price	\$1.22
Valuation - 3.3mtpa	\$1.32
Valuation - 5.0mtpa	\$1.90
Valuation Method	DCF
Cash & franked return + rump	\$1.47

GICS sector	Metals & Mining
Market Cap*	\$m 311
Shares on Issue*	m 255.0
Previous rating	BUY

* Fully diluted for assumed option conversion for dividend

WPG Rump valuation

	Equity	A\$m	A\$ps
Southern Coal Holdings JV	50%	23.3	0.09
Port Pirie	100%	5.0	0.02
Cash		10.0	0.04
Liquid assets (EEE shares)		1.0	0.00
Net Asset Valuation		39.3	0.15

WPG Vs ASX 300 (XKO)



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Peculiar Knob bridging Loan

To fund ongoing operations, OneSteel are to provide a A\$140m bridging facility to replace the previous A\$140m Deutsche Bank funding facility. The facility will be in place for 18 months regardless of whether the OneSteel transaction proceeds. The interest rate of 7% to 8% above a floating base is high, however as OneSteel will take over the funding it is immaterial if the transaction goes ahead.

WPG Rump

We value the rump at 15cps

The WPG rump will include the following assets:

1. Cash of approximately \$10.0m.
2. Southern Coal Holdings JV, hosting 622.4mt of low to mid rank JORC coal resources of which 50% are net to WPG.
3. Port Pirie land, purchased for \$1.0m from the SA government for bulk commodity exports.
4. Port Pirie fully permitted bulk commodity export development for receipt, storage and load out facilities.
5. A 3.1% interest in Evergreen Energy Inc, currently worth approximately \$1.0m (plus warrants).

Southern Coal Holdings JV (WPG 50%)

WPG entered into a 50/50 JV in June 2010 with Evergreen Energy Inc. (NYSE Arca: EEE), a green energy technology solutions company, to jointly develop and commercialise EEE's K-Fuel[®] coal upgrading technology throughout Australia. Under the JV Southern Coal Holdings (SCH) will hold the exclusive licence for the first 15mtpa of K-Fuel produced anywhere in Australia, not just from SCH's current portfolio (see Figure 1), and will have the first right of refusal to participate in the production of K-Fuel in excess of 15mtpa on terms to be negotiated in good faith at the time.

The JV provide exclusivity for the first 15mtpa of K-Fuel product anywhere in Australia

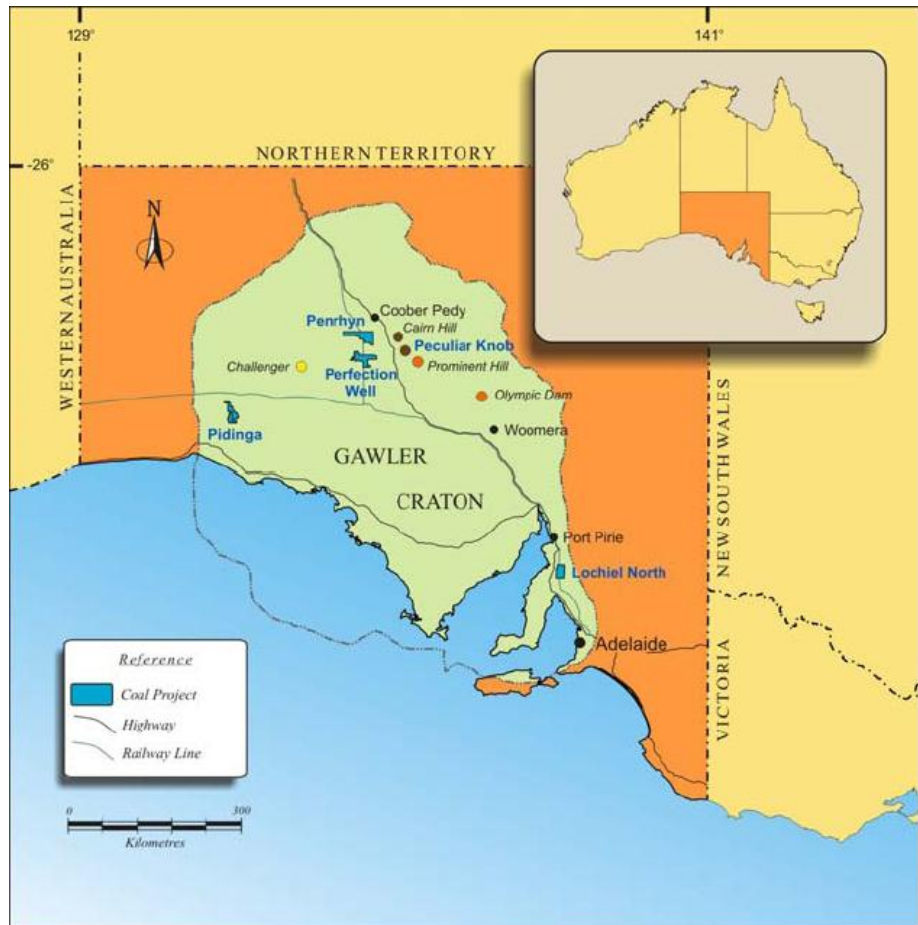
The K-Fuel approach increases the heating value (calorific value) of low-rank fuels while decreasing the environmental impact of coal energy production. This is accomplished by refining coal before it is burned to increase energy densities and combustion efficiencies and reduce greenhouse gas emissions. EEE's 750,000 tpa demonstration plant at Fort Union in the Powder River Basin (PRB) in Wyoming operated from December 2005 to March 2008. Operations were idled as part of EEE's response to the global financial crisis. Based on the feedstock, testwork has shown that PRB coals can be upgraded from a calorific value of 4,500 kcal/kg and 31% moisture to 5,600 kcal/kg and 15.5% moisture. Generally similar upgrading results have also been achieved with Indonesian coals. Test burns of the K-Fuel product in several US power stations have also validated the process.

The process upgrades typical low rank coal to +5,000kcal/kg GAR suitable for export

WPG's South Australian coal portfolio, held in SCH, consists of: its Penrhyn deposit in the Arckaringa Basin south west of Coober Pedy; its granted Pidinga exploration licences in the western part of the state and at Lochiel North near Port Pirie; and an application for an exploration licence at Perfection Well south of Coober Pedy. The locations of these tenements are shown in Figure 1 below.

Figure 1: WPG coal project location

WPG holds 4 coal projects in South Australia with 2 comprising JORC resources of over 500mt of low to mid rank coal



Source: Company reports

Current JORC resources total 622.4mt which includes:

Figure 2: Southern Coal Holdings global resources

Resources Category	Tonnes (mt)
<i>Penhryn Sub-bituminous coal</i>	
Measured resource	185.4
Indicated resource	150.5
Inferred resource	16.5
Total Penhryn resource	352.4
<i>Lochiel North lignite</i>	
Inferred resource	270.0
Total Resources	622.4
Penhryn additional exploration target	330

Source: Company Reports

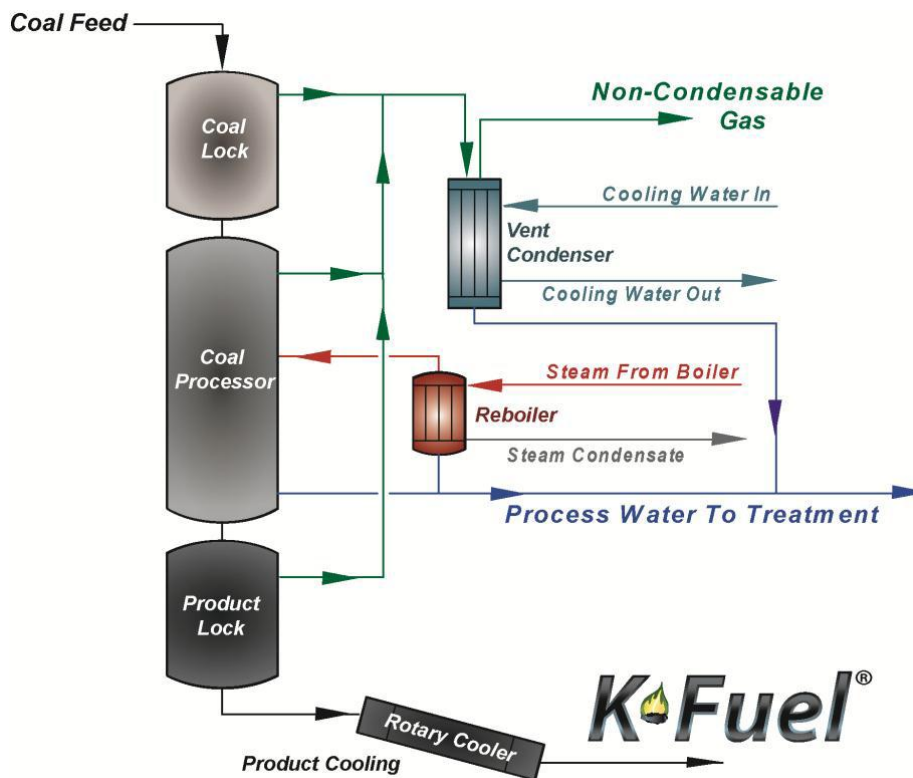
SCH has sufficient resources to commence pre-feasibility work immediately at Penhryn

K-Fuel® Process

The K-Fuel process was developed at the Stanford Research Institute, an independent client-sponsored nonprofit research and development organisation completing studies for government agencies, commercial businesses, foundations and other organisations. Extensive research and development has been undertaken over the past 20 years together with pilot and commercial scale facility design, construction and operation, has resulted in a robust and validated technological process. The process is summarized in Figure 2 below and involves the heating and pressurisation of low value coals, the irreversible removal of the water content and converting the product into a higher energy K-Fuel product.

Figure 3: Schematic overview of K-Fuel Process

The process decreases moisture content and upgrades specific energy



Source: Evergreen Energy

The 0.75mtpa K-Fuel commercial plant and testing lab tested over 60 low rank coal feed stocks during its operation and demonstrated substantial heat value increases. Feed stocks were tested and upgraded from sources such as Inner Mongolia, Indonesia, Russia and the US. In the US, test burns of K-Fuel at multiple power stations validated combustion benefits.

The technology is proven at a commercial scale

Value Potential of K-Fuel to SCH JV

The K-Fuel process is a proven technology for upgrading low rank coal. A development by the JV would be the first since the Wyoming plant shut down in 2008. The major benefit to the JV of a new plant at Penhryn and/or Lochiel North will be ownership of the coal, giving the partners the full value upside from the process.

Initially the JV is seeking to produce 1mtpa of upgraded thermal coals, which based on work to date would see feed stock of 1.2t to produce 1.0t of K-Fuel. Export quality K-Fuel could be delivered through WPG's Port Pirie bulk commodity export option.

Global coal demand increasing

Coal upgrading technologies are becoming increasingly relevant as the supply of low moisture high rank thermal coals are in decline in Australia and Asia. Approximately 465 billion tons of coal or 47% of the world's reserves are sub-bituminous, lignite and brown coals, which are of limited use without being upgraded. The K-Fuel® process of upgrading low value coal allows the SCH JV to take advantage of the significant price arbitrage opportunity.

Given the vast amount of sub-bituminous resources in key markets, the K-Fuel process commercialization is in its infancy. This translates to a massive potential upside from a full commercial roll-out of a technology that is proven, unlike some of its competitor technologies.

Global demand for thermal coal is driven by a major new global build out of coal generation capacity, driven by India and China.

Value drivers

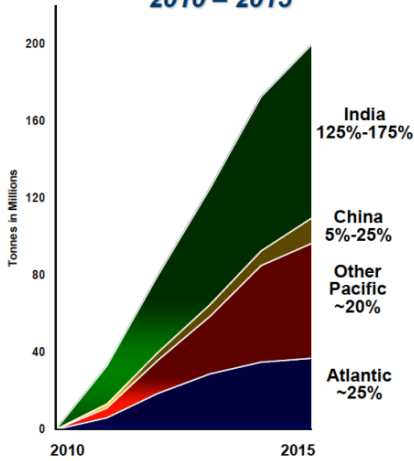
The increase in value that can be derived from the K-Fuel process has been assessed by EEE. Figure 3 shows the EEE sensitivity table comparing the selling price for upgraded coal to the value increase per tonne, using Indonesian coal as an example.

Figure 3: Value increase per tonne of upgraded coal sensitivities.

Value Increase per metric ton (tonne) of upgraded coal sensitivity table (i)					
Kcal/kg	Selling value of Upgraded Coal	Value increase/tonne at cost of:			
		\$10.00	\$12.00	\$14.00	
4200	US\$50	\$22.00	\$18.80	\$15.70	
	US\$60	\$32.00	\$28.80	\$25.70	
	US\$70	\$42.00	\$38.80	\$35.70	
5000	US\$80	\$52.00	\$48.80	\$45.70	
	US\$90	\$62.00	\$58.80	\$55.70	

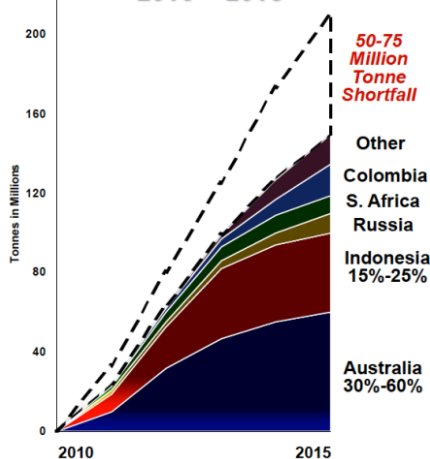
Source: Evergreen Energy

Expected Increase in Seaborne Thermal Demand 2010 – 2015



Source: Evergreen Energy, Peabody

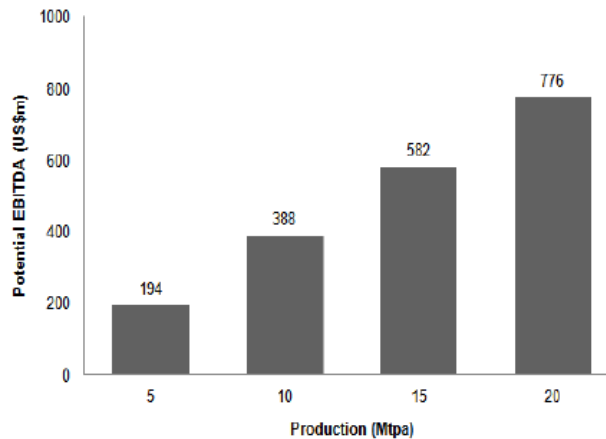
Expected Increase in Seaborne Thermal Supply 2010 – 2015



Source: Evergreen Energy, Peabody

On this 100% basis EEE anticipates that based on Indonesian coal as an example, a \$12.0/t upgrade cost would provide a cash margin of \$38.80/t, or an EBITDA of \$194m to \$776m for a 5mtpa to 20mtpa operation (see Figure 4 below).

Figure 4: Potential EBITDA at various production levels.



Source: Evergreen Energy

Environmental benefits

Upgrading low rank coals also provides environmental benefits

The upgraded coal will be more efficient to burn and is likely to have lower carbon emissions. The upgraded coal has also been shown to reduce Hg, SO₂ and NO_x, further enhancing its more 'efficient to burn' status.

Current work programme

Recent drilling by the JV at Penhryn and Lochiel North was completed in July/August 2011, with coal samples sent to the EEE lab in Gillette, Wyoming, USA.

K-Fuel test work has shown an export quality thermal coal is produced

Results reported by the JV partners for the Penhryn coal are highly encouraging with the heating value of the coal after it has been upgraded exceeding 5,000kcal/kg GAR. This is an increase of 25% to 40% from the raw coal and ensures an export quality thermal coal can be produced.

Scoping Study: A scoping study has commenced which includes looking at the best option to construct the plant, either on site and utilize K-Fuel coal for power or in Port Pirie where gas fired power is available.

Feasibility Study: As the resource at Penhryn is already at an advanced stage, we anticipate that the all up cost of a full feasibility study will be up \$5m, which is to be funded equally by the JV partners.

The value enhancement of a feasibility study we would anticipate to be reflected in the WPG share price as the project advances.

Veritas WPG rump valuation

SCH JV

The SCH JV advantages which we anticipate will add value are that:

1. the K-Fuel process has demonstrated an increase in the efficiency and heating value of sub-bituminous, lignite and brown coals by 30% on average, accomplished by decreasing equilibrium moisture content by 50%.
2. The K-Fuel product will achieve a higher price for the coal, allowing the product to compete with bituminous coals.
3. The product is handled and transported as FOB feed coal.
4. An average 50% reduced moisture content will lead to lower transportation costs.
5. The K-Fuel product is more efficient than the raw coal which has therefore significant environmental benefits, such as lower carbon emissions and in particular, reduced Hg, SO₂ and NOx.

The K-Fuel process value adds the coal as well as providing significant value upside for WPG

We have based our valuation on the April 2010 acquisition of the adjacent Lake Phillipson coal deposit by White Energy for \$39.3m. This acquisition was made to utilise White Energy's binderless coal briquette's technology on Lake Phillipson coal. The acquisition cost was 7.6 cents per resource tonne.

Using this as a basis to value both the Penhryn and Lochiel North coal Projects, we have concluded an applicable net WPG valuation of \$23.3m. We see the move from a scoping study to a feasibility study as value adding.

Port Pirie

Port Pirie is fully permitted for the development of a bulk commodity export facility which we see as a potential export point for the K-Fuel. Alternatively WPG could sell the land and associated permitting to another budding bulk commodity exporter.

The SA government has a right to buy back the land in 12 months

The land was purchased for \$1.0m from the South Australian government. The SA government has the option to buy the land back after 12 months, if a development has not commenced for \$0.9m.

If WPG show that they are 'developing' the facility in line with K-Fuel, then the option to buy back may not be taken unless a third party knocks on the governments door. However, this would not take into account that the facility is fully permitted and ready to commence construction, which would most likely be attractive to a third party.

Valuation: We have valued Port Pirie land and permitting at \$2.5m, comprising \$1.0m for the land and \$1.5m for fact that it is fully permitted. The potential of a strategic sale to a third party we value at \$2.5m, which includes the time value for the permitting. Therefore we have applied a total value of \$5.0m to Port Pirie.

Cash & liquids

WPG anticipates that after \$71.6m in tax is paid by the end of MQ12, the WPG rump will have approximately \$10.0m in cash as at 30 June 2012. This assumes ongoing administration and corporate overheads of \$3m per annum.

In February 2011, WPG invested US\$2.0m into EEE as part of a larger US\$16.0m capital raising by EEE. This included 0.95 warrants for each share taken, converting at exercise prices between \$2.60 and \$2.80 per share by 1 August 2014. This investment is currently worth approximately \$1.0m.

Conclusion - WPG rump

After a review of the potential of the K-Fuel process we can see significant upside from development of the Penhryn and/or Lochiel North deposits for a K-Fuel plant. However, we await the completion of a pre-feasibility study due in mid-2012 to confirm the economics for such a project.

A peer comparison is likely to be White Energy (WEC.ASX) which is a more advanced with a current market capitalization of \$600m, compared to our WPG rump valuation of \$0.15 per share and a market capitalization of \$39m. A move to a full feasibility is likely to provide a share price re-rating reflecting the value upside and more advanced nature of the K-Fuel process.

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RATING

BUY – anticipated stock return is greater than 10%
 SELL – anticipated stock return is less than -10%
 HOLD – anticipated stock return is between -10% and +10%
 SPECULATIVE – High risk with stock price likely to fluctuate by 50% or more

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