

Caledonia Mining

H115 results

FY15 guidance maintained, expansion on track

Metals & mining

24 August 2015

Caledonia's Q215 and H115 results indicate Blanket has met all infrastructure and production milestones on budget or ahead of schedule. Cost pressures relating to increased electricity consumption and a lower gold grade have been partially offset by cost savings made closing its Zambian exploration office.

Year end	Revenue (C\$m)	PBT* (C\$m)	EPS* (c)	DPS (c)	P/E (x)	Yield (%)
12/13	65.1	21.9	18.2	11.4	4.6	13.5
12/14	59.1	12.2	7.5	7.6	11.3	9.0
12/15e	65.2	9.2	13.3	6.0	6.3	7.1
12/16e	78.8	17.9	24.9	6.0	3.4	7.1

Note: *PBT and EPS are normalised, excluding intangible amortisation, exceptional items and share-based payments.

Room for manoeuvre if gold market tightens further

A gold price persistently below the US\$1,100/oz level provides a marginal return off Blanket's Q215 AISC cost of production of US\$1,030/oz (Q215), and turns a loss off its all-in cost per ounce of US\$1,222. The average realised gold price in Q215 was US\$1,174/oz. Blanket's Q215 all-in cost of production included expenditures relating to exploring and developing Caledonia's two main satellite exploration projects, GG and Mascot. If the gold price persists below US\$1,100/oz, we believe Caledonia will be able to maintain profitability through stopping exploration at these two non-core projects. Such a move will not compromise implementing the revised investment plan or affect sustaining capex required to keep Blanket operating efficiently.

Production and infrastructure projects on-track

The Blanket mine produced 10,401oz of gold in Q215, a q-o-q decrease of 7.3%. H115 production is slightly ahead of plan for the quarter and half-year, and Caledonia remains on track for production of 42,000oz of gold for FY15.

Valuation: FY15 and FY16 gold prices revised

Our FY15 gold price forecast is now US\$1,164/oz, down from US\$1,285/oz in our last [update](#) published in May 2015. We also revise our FY16 gold price forecast down from US\$1,397/oz to US\$1,224/oz. This reflects our view of a potential hardening of expectations of a US rate hike by end-2015. With Caledonia's H115 firmly in-line with expectations and capex weighted to H215, we maintain our forecasts (subject to the change in gold price). We also revise our C\$/£ exchange rate from 1.86 to 2.04. On this basis our previous £1.47 valuation becomes £1.36. At a flat gold price of US\$1,100/oz over life-of-mine our valuation becomes £0.43 per share. All valuations use a 10% discount rate to reflect general equity risk. Mainly as a result of our revised gold price forecasts for FY15 and FY16 and changes in the US\$/C\$ exchange rate, our end-year cash estimates are now C\$16.9m (vs C\$21.8m previously) and C\$11.8m (vs C\$23.4m previously) respectively.

Price **41.50p**
Market cap **£22m**

C\$2.04/£, C\$1.31/US\$

Net cash (C\$m) at end-June 2015 23.7

Shares in issue 52.1m

Free float N/A

Code CMCL

Primary exchange TSE

Secondary exchange AIM

Share price performance



% 1m 3m 12m

Abs (8.8) (8.8) (29.7)

Rel (local) (1.1) 2.2 (25.1)

52-week high/low 61.00p 35.50p

Business description

Caledonia Mining mines gold at its main operating asset, the 49%-owned Blanket gold mine in southern Zimbabwe. It is also progressing its understanding of a number of promising satellite projects close to Blanket.

Next event

Q315 results October 2015

Analysts

Tom Hayes +44 (0)20 3077 5725

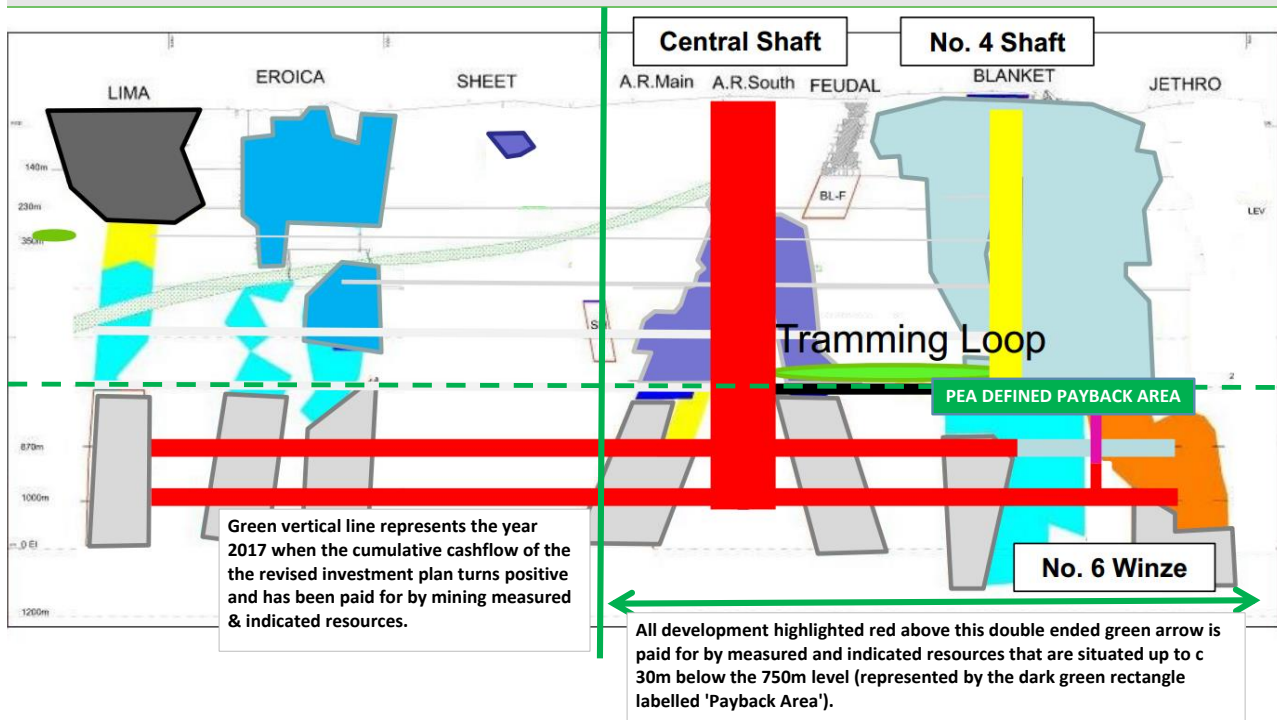
Charles Gibson +44 (0)20 3077 5724

mining@edisongroup.com
[Edison profile page](#)

All expansion projects proceeding as planned

All infrastructure projects being undertaken by Caledonia to increase production and improve mining flexibility at Blanket are on-track and on budget. The tramming loop, which has been completed slightly ahead of schedule (in June) and under budget, will now be used to alleviate previous bottlenecks around the No.4 shaft by doubling haulage capacity along the 22 level. The tramming loop will allow greater amounts of both ore and waste material to be hauled concurrently, therefore freeing up development to finish the No. 6 Winze and Level 22 main haulage way towards the AR Main and Lima orebodies.

Exhibit 1: Long-section view of Blanket showing all main development projects



Source: Caledonia Mining and Edison Investment Research

Completing the No. 6 Winze will allow for production from orebodies below the 750m level. This production is expected to start in January 2016 and will mark the first time Blanket has managed to extract ore from below the 750m level – this type of production is key to extending Blanket's operating life and eventually increasing production to a target rate of c 80koz by 2021. Production will then ramp-up to a daily production rate of 500t by mid-2017. The pre-production cost for the No. 6 Winze is US\$5m and has been funded through internal Blanket cash flows.

The central shaft will form the main route to surface for the majority of Blanket ore and waste production from mid-2018 onwards. Work started on the central shaft's development in early 2015. To date, a lay-down area has been cleared for site works and delivery of equipment. One winder has been delivered and excavation of a 9m x 9m x 5m void completed to allow concrete to be poured and form the collar to the shaft. Winder base excavations have been completed and the shaft pre-sink excavated to a depth of 8.1m. The target depth for the shaft at the end of 2015 is approximately 90m. Once finished, the shaft's depth will be 1,080m.

Blanket resources upgraded, GG and Mascot advancing

Caledonia announced a resource upgrade on 19 May 2015. The resource upgrade was based on drilling at depth below the AR Main and Blanket ore bodies over the past year. This drilling resulted

in 491kt of inferred material being upgraded to indicated category, as well as the addition of 47kt of new indicated resources. The total 538kt of indicated material is in addition to the 2,934kt of ore reserves and mineral resources in the indicated category that were used to underpin the revised investment plan being implemented at Blanket. The resource upgrade represents a 20.5% increase in contained gold ounces. The main point to highlight is that the resource upgrade from inferred to indicated was achieved at depth below the 750m level, which is crucial to extending Blanket's mine life. It also de-risks our valuation through reducing the amount of inferred resource tonnes (which are highly speculative in nature) that were used by Caledonia to underpin its revised investment plan.

Blanket's resource and reserve statements prior to the above additions are provided in our January 2015 Outlook note [Future-proofing Blanket](#).

Exploration at GG and Mascot progresses

Exploration and development activities at its two main satellite projects, namely GG and Mascot, are showing the potential for additional gold production to be brought on-line for a relatively minimal cost. It is worth noting that these projects are brownfield sites, and other than for GG where a new shaft has been sunk, have existing shaft entry and some historical underground development. These brownfield projects have historical production records, which Caledonia states show GG and Mascot as providing the greatest near-term opportunity to enter back into production. Risks persist and mainly relate to understanding the size and scope of future production and the metallurgical compatibility of processing satellite ore feeds through the Blanket processing plant. Caledonia has stated it could build a small pilot plant (funding and board approval pending) to test ores from GG and Mascot so as not to compromise the high gold recovery rates achieved at Blanket and also to design a commercial process to extract GG and Mascot's gold.

The GG project has mineralisation currently defined to a depth of 300m and along a strike length of 150m. Mineralisation is currently understood to form two zones, called the North and South zones. Caledonia has completed underground development to reach the North zone, which is currently understood to host the most extensive mineralisation. The most significant result of surface drilling into the North zone was an intercept of 3.9g/t over 4m – roughly comparable to the grades and widths seen at Blanket. This drill result has caused Caledonia to suspend lateral development and extend the depth of the shaft to 240m below surface. The main production level is planned for 210m below surface. Locally, widths of 10m have been observed and Caledonia states GG's known mineralisation remains open along strike.

The Mascot project contains three gold prospects: Mascot, Penzance and Eagle Vulture. Mascot has been mined previously to a depth of 250m, and, while at depth Mascot's strike shortened, its width expanded. Further, drilling from surface undertaken by Blanket staff indicates two mineralised zones, one to the south and one to the north. Current underground development comprises levels at 30m vertical spacings to a depth of 180m below surface. Payable mineralisation has been observed along Levels 1 and 2 at 60m and 90m below surface respectively. During Q115 the mine was completely de-watered to expose the shaft bottom and allow for its potential deepening. During Q215, development of a drill cuddy (a location from which drilling takes place) will allow angled drill holes to be sunk at Mascot to investigate the potential continuation of higher-grade mineralisation observed elsewhere in the North zone.

Financials

Caledonia's Q215 and H115 results are in-line with expectations. We reiterate our underlying cost and capex forecasts, and adjust our revenue line, which is revised for new FY15 and FY16 gold prices and exchange rates. In light of the current lower gold price, Caledonia has made cost

reductions a key focus. During H115 the company closed its Zambian exploration office, which resulted in US\$0.5m in legislated retrenchment costs but will result in a saving of approximately US\$1m per annum; no further material expenditures are expected. Caledonia fully impaired its Zambian asset (Nama) in 2014.

Earnings estimates reduced due to revised gold price

Caledonia's FY15 EPS figure has been affected by our mid-year gold price revisions, which has been necessary to reflect a hardening of sentiment towards a US rate hike by end-2015. Previously we forecast FY15 EPS at 19.4c, rising to 34.0c in FY16 as the effects of increased haulage capacity and access to ore bodies below the 750m level becomes available via the No. 6 Winze, resulting in gold production increasing from 42koz (FY15) to 50koz (FY16). On adjusting our financial model for our new gold prices of US\$1,164/oz (FY15) and US\$1,224/oz (FY16), our EPS figures reduce to 13.3c and 24.9c respectively.

FY16 dividend governed by the gold price

We maintain our assumption that Caledonia will pay a dividend in FY16 similar to the 6c total dividend paid quarterly through FY15. However, FY16's dividend is not guaranteed, and in light of the current lower gold price we expect Caledonia to firm up its commitment to a dividend in FY16 by the end of the current calendar year. Dividend payments will also be sensitive to Caledonia providing financial support to the Blanket mine and its implementation of the revised investment plan. Caledonia has guided it can provide such support during periods of increased gold price weakness. Its current C\$3.1m FY15 dividend is c 8x covered by its end-June 2015 cash balance (C\$23.7m).

Applying our revised FY15 and FY16 gold prices, results in end-year cash, after all expenses and capex, of C\$16.9m and C\$11.8m respectively. Therefore, if a 6c dividend was paid during FY16 it would only be c 5x covered by cash. Caledonia has no formal dividend policy, but such a reduction in dividend cover (cf 2015) and the potential need to financially support Blanket if the gold price decreases further from its current level of c US\$1,100/oz, could put a dividend as high as 6c in doubt. Caledonia currently yields 7%, compared with the FTSE Mining Index average of 5.7% and an average dividend cover of 2x.

Exhibit 2: Financial summary

	C\$000s	2013	2014	2015e	2016e	2017e
Year-end 31 December		IFRS	IFRS	IFRS	IFRS	IFRS
PROFIT & LOSS						
Revenue		65,113	59,082	65,203	78,785	113,848
Cost of Sales		(35,232)	(38,609)	(48,505)	(53,050)	(61,299)
Gross Profit		29,881	20,473	16,698	25,736	52,548
EBITDA		25,317	16,252	14,004	22,761	49,281
Operating Profit (before amort. and except.)		22,041	12,344	9,029	17,786	44,306
Intangible Amortisation		0	0	0	0	0
Exceptionals		(12,526)	980	(723)	0	0
Operating Profit		9,515	13,324	8,306	17,786	44,306
Net Interest		(108)	(155)	134	85	59
Profit Before Tax (norm)		21,933	12,189	9,163	17,870	44,365
Profit Before Tax (FRS 3)		9,407	13,169	8,441	17,870	44,365
Tax		(9,897)	(6,604)	(445)	(1,823)	(9,832)
Profit After Tax (norm)		12,036	5,585	8,718	16,047	34,533
Profit After Tax (FRS 3)		(490)	6,565	7,995	16,047	34,533
Minority interests		(2,565)	(1,668)	(1,767)	(3,084)	(6,284)
Net income (norm)		9,471	3,917	6,951	12,963	28,249
Net income (FRS3)		(3,055)	4,897	6,228	12,963	28,249
Average Number of Shares Outstanding (m)		52.0	52.1	52.1	52.1	52.1
EPS - normalised (c)		18.2	7.5	13.3	24.9	54.2
EPS - normalised and fully diluted (c)		18.2	7.5	13.3	24.9	54.2
EPS - (IFRS) (c)		(5.9)	9.3	12.0	24.9	54.2
Dividend per share (c)		11.4	7.6	6.0	6.0	0.0
Gross Margin (%)		45.9	34.7	25.6	32.7	46.2
EBITDA Margin (%)		38.9	27.5	21.5	28.9	43.3
Operating Margin (before GW and except.) (%)		33.9	20.9	13.8	22.6	38.9
BALANCE SHEET						
Fixed Assets		33,448	40,388	54,157	70,939	86,013
Intangible Assets		0	0	0	0	0
Tangible Assets		33,448	40,388	54,157	70,939	86,013
Investments		0	0	0	0	0
Indigenisation receivable		0	0	0	0	0
Current Assets		36,154	36,908	27,423	23,858	43,799
Stocks		6,866	7,571	4,810	5,256	5,979
Debtors		3,889	2,151	5,359	6,476	9,357
Cash		25,222	26,838	16,906	11,779	28,115
Other		177	348	348	348	348
Current Liabilities		(7,534)	(5,781)	(5,197)	(6,133)	(11,078)
Creditors		(5,738)	(5,781)	(5,197)	(6,133)	(11,078)
Short term borrowings		(1,796)	0	0	0	0
Long Term Liabilities		(10,094)	(12,980)	(12,980)	(12,980)	(12,980)
Long term borrowings		0	0	0	0	0
Other long term liabilities		(10,094)	(12,980)	(12,980)	(12,980)	(12,980)
Net Assets		51,974	58,535	63,403	75,684	105,754
Minority interests		(51)	(804)	(2,571)	(5,148)	(11,432)
Shareholder equity		51,923	57,731	60,832	70,536	94,322
CASH FLOW						
Operating Cash Flow		22,768	18,859	12,250	21,496	46,159
Net Interest		(108)	(155)	134	85	59
Tax		(7,974)	(4,999)	(445)	(1,823)	(9,832)
Capex		(11,738)	(6,786)	(18,744)	(21,758)	(20,049)
Acquisitions/disposals		0	0	0	0	0
Management Fees		470	0	0	0	0
Dividends		(7,934)	(3,974)	(3,127)	(3,127)	0
Net Cash Flow		(4,516)	2,945	(9,932)	(5,128)	16,336
Opening net debt/(cash)		(27,942)	(23,426)	(26,838)	(16,906)	(11,779)
HP finance leases initiated		0	0	0	0	0
Other		0	467	0	0	0
Closing net debt/(cash)		(23,426)	(26,838)	(16,906)	(11,779)	(28,115)

Source: Company accounts, Edison Investment Research

Edison, the investment intelligence firm, is the future of investor interaction with corporates. Our team of over 100 analysts and investment professionals work with leading companies, fund managers and investment banks worldwide to support their capital markets activity. We provide services to more than 400 retained corporate and investor clients from our offices in London, New York, Frankfurt, Sydney and Wellington. Edison is authorised and regulated by the Financial Conduct Authority (www.fsa.gov.uk/register/firmBasicDetails.do?sid=181584). Edison Investment Research (NZ) Limited (Edison NZ) is the New Zealand subsidiary of Edison. Edison NZ is registered on the New Zealand Financial Service Providers Register (FSP number 247505) and is registered to provide wholesale and/or generic financial adviser services only. Edison Investment Research Inc (Edison US) is the US subsidiary of Edison and is regulated by the Securities and Exchange Commission. Edison Investment Research Limited (Edison Aus) [46085869] is the Australian subsidiary of Edison and is not regulated by the Australian Securities and Investment Commission. Edison Germany is a branch entity of Edison Investment Research Limited [4794244]. www.edisongroup.com

DISCLAIMER

Copyright 2015 Edison Investment Research Limited. All rights reserved. This report has been commissioned by Caledonia Mining and prepared and issued by Edison for publication globally. All information used in the publication of this report has been compiled from publicly available sources that are believed to be reliable, however we do not guarantee the accuracy or completeness of this report. Opinions contained in this report represent those of the research department of Edison at the time of publication. The securities described in the Investment Research may not be eligible for sale in all jurisdictions or to certain categories of investors. This research is issued in Australia by Edison Aus and any access to it, is intended only for "wholesale clients" within the meaning of the Australian Corporations Act. The Investment Research is distributed in the United States by Edison US to major US institutional investors only. Edison US is registered as an investment adviser with the Securities and Exchange Commission. Edison US relies upon the "publishers' exclusion" from the definition of investment adviser under Section 202(a)(11) of the Investment Advisers Act of 1940 and corresponding state securities laws. As such, Edison does not offer or provide personalised advice. We publish information about companies in which we believe our readers may be interested and this information reflects our sincere opinions. The information that we provide or that is derived from our website is not intended to be, and should not be construed in any manner whatsoever as, personalised advice. Also, our website and the information provided by us should not be construed by any subscriber or prospective subscriber as Edison's solicitation to effect, or attempt to effect, any transaction in a security. The research in this document is intended for New Zealand resident professional financial advisers or brokers (for use in their roles as financial advisers or brokers) and habitual investors who are "wholesale clients" for the purpose of the Financial Advisers Act 2008 (FAA) (as described in sections 5(c) (1)(a), (b) and (c) of the FAA). This is not a solicitation or inducement to buy, sell, subscribe, or underwrite any securities mentioned or in the topic of this document. This document is provided for information purposes only and should not be construed as an offer or solicitation for investment in any securities mentioned or in the topic of this document. A marketing communication under FCA Rules, this document has not been prepared in accordance with the legal requirements designed to promote the independence of investment research and is not subject to any prohibition on dealing ahead of the dissemination of investment research. Edison has a restrictive policy relating to personal dealing. Edison Group does not conduct any investment business and, accordingly, does not itself hold any positions in the securities mentioned in this report. However, the respective directors, officers, employees and contractors of Edison may have a position in any or related securities mentioned in this report. Edison or its affiliates may perform services or solicit business from any of the companies mentioned in this report. The value of securities mentioned in this report can fall as well as rise and are subject to large and sudden swings. In addition it may be difficult or not possible to buy, sell or obtain accurate information about the value of securities mentioned in this report. Past performance is not necessarily a guide to future performance. Forward-looking information or statements in this report contain information that is based on assumptions, forecasts of future results, estimates of amounts not yet determinable, and therefore involve known and unknown risks, uncertainties and other factors which may cause the actual results, performance or achievements of their subject matter to be materially different from current expectations. For the purpose of the FAA, the content of this report is of a general nature, is intended as a source of general information only and is not intended to constitute a recommendation or opinion in relation to acquiring or disposing (including refraining from acquiring or disposing) of securities. The distribution of this document is not a "personalised service" and, to the extent that it contains any financial advice, is intended only as a "class service" provided by Edison within the meaning of the FAA (ie without taking into account the particular financial situation or goals of any person). As such, it should not be relied upon in making an investment decision. To the maximum extent permitted by law, Edison, its affiliates and contractors, and their respective directors, officers and employees will not be liable for any loss or damage arising as a result of reliance being placed on any of the information contained in this report and do not guarantee the returns on investments in the products discussed in this publication. FTSE International Limited ("FTSE") © FTSE 2015. "FTSE®" is a trade mark of the London Stock Exchange Group companies and is used by FTSE International Limited under license. All rights in the FTSE indices and/or FTSE ratings vest in FTSE and/or its licensors. Neither FTSE nor its licensors accept any liability for any errors or omissions in the FTSE indices and/or FTSE ratings or underlying data. No further distribution of FTSE Data is permitted without FTSE's express written consent.