Edison investment research

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Frontier Mining

Year End	Revenue ($m)	PBT* ($m)	EPS* (c)	DPS (c)	P/E (x)	Yield (%)
12/08	0.0	(4.8)	(2.4)	0.0	N/A	N/A
12/09	2.9	(5.3)	(0.6)	0.0	N/A	N/A
12/10e	13.2	0.0	0.0	0.0	N/A	N/A
12/11e	48.8	22.3	2.4	0.0	3.1	N/A

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

Investment summary: FML steams ahead

On the back of the recent gold pour at the Koskuduk heap leach operation, Frontier has moved from explorer to producer during the past 12 months. However, we believe the value of the company lies in the much larger Benkala copper-gold project, where an updated JORC resource is expected on the smaller oxide portion of the orebody later this year. On current resources we value the company at 12p per share, although we expect a positive re-rating on the announcement of the revised JORC resource statement.

Commencement of 2010 gold production

The first gold pour for 2010 was announced on 14 July. The Koskuduk production facility produced doré of 113oz Au and 341oz Ag from the Koskuduk heap leach operation, while 176oz Au and 541oz Ag were produced from 2009 Naimanjal stockpiles. Koskuduk is a small heap leach operation that aims to produce 10koz of gold per year from a total (Soviet) C1 and C2 oxide gold resource of approximately 250koz. The cashflow generated from Koskuduk is to go toward development of Frontier's larger operations.

Benkala infill drilling suggests oxide grade improvement

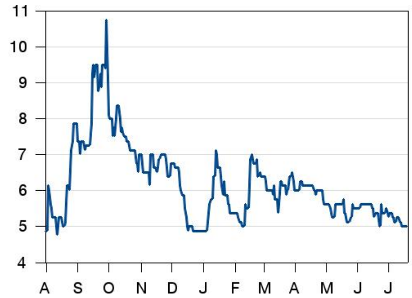
In late 2009 to early 2010, Frontier undertook a 54-hole drill programme, primarily to confirm the oxide zone of the Benkala copper project, which contains less than 10% of the total contained copper metal of the deposit. Results from eight drill holes were announced in May 2010 and indicate a marginal improvement in copper grade to 0.63% Cu, compared to the historical soviet grade, which averaged 0.55% Cu for the entire deposit. Results are imminent for the remaining holes and, on receipt, Frontier will be able to calculate an updated JORC resource estimate and confirm whether the increase in grade is representative of the copper oxide zone as a whole.

Valuation: Shares discounted at 56%

Our initial valuation of 12p per share based on an EV per resource value ratio remains unchanged. However, as Frontier completes its development plans at Benkala we expect our applied 80% discount factor, mainly for execution risk, to decrease creating upside to our initial valuation.

Price	5.0p
Market Cap	£46m

Share price graph



Share details

Code	FML
Listing	AIM
Sector	Mining and metals
Shares in issue	917.3m

Price

52 week	High	Low
	10.75p	4.00p

Balance Sheet as at 31 December 2009

Debt/Equity (%)	244
NAV per share (c)	0.6
Net borrowings ($m)	12.9

Business

Frontier Mining holds two mining licences in Kazakhstan. Its flagship 50% owned Benkala copper-gold project is moving towards production, targeted for H211, while its smaller 100% owned Koskuduk heap leach operation has started to produce gold and is expected to yield approximately 10koz per year.

Valuation

	2009	2010e	2011e
P/E relative	N/A	N/A	38%
P/CF	N/A	22.0	2.7
EV/Sales	19.0	7.2	1.7
ROE	N/A	0%	81%

Geography based on revenues

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

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Benkala and Maminskoye progress

Technical review on Benkala and Maminskoye

Wardell Armstrong (WA) completed a technical review on Benkala and the Maminskoye gold deposit in Kazakhstan in June 2010. The study included indicative preliminary financial evaluations of the aforementioned projects using Soviet resource figures. WA undertook the Benkala valuation on the secondary oxide copper ore only (which represents less than 10% of the total Benkala resource) based on a US$6,000/t copper price, 5Mtpa operation and average annual production of 5,425t copper between 2010 and 2017. These and other assumptions resulted in an NPV (at 10%) of US$190.8m or 20.8p per share. WA's Maminskoye valuation was based on a 1.5Mtpa operation to produce an average of 2,725oz gold per year at a gold selling price of US$950/oz. These and other assumptions resulted in a preliminary NPV (at 10%) of US$110.9m or 12.1p per share. We will undertake a further detailed assessment of Frontier's flagship Benkala project once a JORC-compliant resource on the oxide zone becomes available (due by end 2010).

New management ushers in more efficient cost control

Frontier installed new management during 2009, including the appointment of Erlan Sagadiev as Chairman and CEO, who immediately took an aggressive stance toward cost management over the company's assets. By year end, his initiatives had resulted in a reduction in operating expense from US$4.5m to US$1.9m, as a result of which overheads are now running at approximately 50% of previous levels. The year was seen as transformational by the company, which sought to move towards producer status and invest in its flagship Benkala project. Results indicated group revenue up US$2.1m to US$2.9m, primarily from production of 2,620oz gold at an average realised selling price of US$1,063/oz, and 13,644oz silver at an average selling price of US$17/oz. This is a marked and expected improvement over the previous year as the Naimanjal licence area (including Koskuduk) re-started gold production. Investment consisted of US$6.2m in Benkala by Frontier's 50% owned subsidiary KazCopper, with US$8m of debt and overdue payables also being retired during the year. However, total loss for FY09 increased markedly to US$30.6m, resulting mainly from an issue of warrants and a re-calculation of their fair value at year-end (US$24.9m).

KazCopper (50% FML) enters engineering contract over Benkala

KazCopper has entered into agreement with Calder Project Services in conjunction with Miller Metallurgical Services over the technical design of the Benkala SX-EW oxide copper process plant. The plant is necessary to fully realise the potential of the Benkala copper oxide ore. Development of the plant will be undertaken in two phases, with phase one having a production capacity of 25tpd (7kt per year) ramping up to 75tpd (21kt per year) as phase two construction is completed. As this is only an initiation of plant design, no definite timelines for the two construction phases has been stated. However, Frontier targets production of the oxide copper-gold at Benkala for H211.

Frontier to move corporate offices to the Cayman Islands

Frontier was originally incorporated in Delaware, US, when it originally aimed to operate in both North America as well as in the wider CIS region. Management has now re-assessed its position as a Kazakhstan-focused mining company and declared its intention to re-domicile to the Cayman

Islands, primarily to make use of a more favourable tax environment. Frontier will effect the change in holding company through a merger (on approval by shareholders), involving a share exchange with a new Cayman Islands company. A timeline to completion of this matter has not yet been issued by the company.

Advances in project development de-risks valuation

We await the outcome of the JORC resource estimate due to be completed by end 2010. Although this, along with the commencement of technical designs for the SX-EW process plant at Benkala, can be seen as positive and de-risk development, no completion of a specific goal at Benkala has yet been achieved. On this basis we re-iterate our valuation of 12p per share based on a market capitalisation to resource value ratio (see our Outlook note published May 2010).

Exhibit 1: Financials

$000s	2006	2007	2008	2009	2010e	2011e
Year end 31 December	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS
PROFIT & LOSS						
Revenue	2,974	0	0	2,925	13,161	48,753
Cost of Sales	(1,969)	0	0	3,891	(6,329)	(17,137)
Gross Profit	1,005	0	0	6,817	6,832	31,616
EBITDA	(2,141)	(3,483)	(4,456)	(2,900)	4,328	29,012
Operating Profit (before GW and except.)	(2,911)	(3,526)	(4,519)	(2,931)	1,601	25,315
Intangible Amortisation	0	(7)	(13)	0	(4)	(4)
Exceptionals	0	(695)	0	0	0	0
Other	164	(5)	(236)	(41)	0	0
Operating Profit	(2,747)	(4,233)	(4,767)	(2,972)	1,598	25,312
Net Interest	103	(89)	(261)	(2,390)	(1,585)	(3,058)
Profit Before Tax (norm)	(2,808)	(3,615)	(4,780)	(5,320)	16	22,257
Profit Before Tax (FRS 3)	(2,644)	(4,322)	(5,028)	(5,362)	12	22,254
Tax	1,051	60	(304)	(302)	0	0
Profit After Tax (norm)	(1,593)	(4,254)	(5,320)	(3,610)	16	22,257
Profit After Tax (FRS 3)	(1,593)	(4,262)	(5,332)	(5,663)	12	22,254
Average Number of Shares Outstanding (m)	132.6	142.4	218.1	567.7	917.3	917.3
EPS - normalised (c)	(1.2)	(3.0)	(2.4)	(0.6)	0.0	2.4
EPS - normalised fully diluted (c)	(1.2)	(3.0)	(2.4)	(0.4)	0.0	2.4
EPS - FRS 3 (c)	(1.2)	(3.0)	(2.4)	(1.0)	0.0	2.4
Dividend per share (c)	0.0	0.0	0.0	0.0	0.0	0.0
Gross Margin (%)	33.8	N/A	N/A	233.0	51.9	64.8
EBITDA Margin (%)	N/A	N/A	N/A	N/A	32.9	59.5
Operating Margin (before GW and except.) (%)	N/A	N/A	N/A	N/A	12.2	51.9
BALANCE SHEET						
Fixed Assets	21,015	47,414	47,717	48,111	59,381	65,381
Intangible Assets	43	1,946	829	539	535	531
Tangible Assets	19,323	6,923	4,650	5,211	16,484	22,488
Investments	1,649	38,545	42,239	42,362	42,362	42,362
Current Assets	5,305	3,115	514	3,653	5,421	25,338
Stocks	2,985	422	264	507	1,330	3,385
Debtors	586	42	0	151	1,330	3,385
Cash	1,253	2,474	15	234	0	15,807
Other	481	176	235	2,761	2,761	2,761
Current Liabilities	(1,827)	(10,623)	(13,496)	(34,605)	(47,627)	(51,286)
Creditors	(1,696)	(3,493)	(6,367)	(31,890)	(32,678)	(33,278)
Short term borrowings	(131)	(7,130)	(7,130)	(2,714)	(14,949)	(18,008)
Long Term Liabilities	(1,048)	(3,818)	(3,967)	(11,827)	(11,827)	(11,827)
Long term borrowings	(940)	(1,963)	(2,096)	(10,543)	(10,543)	(10,543)
Other long term liabilities	(108)	(1,855)	(1,870)	(1,284)	(1,284)	(1,284)
Net Assets	23,445	36,088	30,768	5,333	5,349	27,606
CASH FLOW						
Operating Cash Flow	(4,391)	(1,413)	(535)	(6,009)	3,123	25,507
Net Interest	103	0	0	(89)	0	0
Tax	1,052	0	0	0	0	0
Capex	(8,469)	(2,271)	(1,695)	(2,470)	(14,000)	(9,700)
Acquisitions/disposals	0	(1,033)	0	0	0	0
Financing	0	6,184	0	138	0	0
Dividends	0	0	0	0	0	0
Other	(909)	(89)	(134)	4,618	(1,591)	(3,059)
Net Cash Flow	(12,614)	1,378	(2,364)	(3,812)	(12,468)	12,747
Opening net debt/(cash)	(12,796)	7,751	6,619	9,211	13,024	25,492
HP finance leases initiated	0	0	0	0	0	0
Other	0	(246)	(229)	0	(0)	0
Closing net debt/(cash)	(182)	6,619	9,212	13,023	25,492	12,744

Source: Frontier Mining/Edison Investment Research