

# Stanmore Coal Limited

ABN 27 131 920 968

## Notice of annual general meeting & explanatory memorandum

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### Meeting information:

Date: Thursday, 29 November 2012

Time: 10:00am (Brisbane time)

Place: Brisbane Polo Club, Naldham House, 193 Mary Street (cnr Eagle and Felix Streets), Brisbane, Queensland

This document contains important information regarding the Annual General Meeting of Stanmore Coal Limited and should be read in its entirety. If you are in doubt as to how you should vote at the General Meeting, you should seek advice from your accountant, solicitor or other professional adviser without delay.

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# Notice of annual general meeting

## Stanmore Coal Limited

Notice is given that the Annual General Meeting of Shareholders of Stanmore Coal Limited ABN 27 131 920 968 (**Company**) will be held at the Brisbane Polo Club, Naldham House, 193 Mary Street (cnr Eagle and Felix Streets), Brisbane, Queensland, on 29 November 2012 and will commence at 10:00am (Brisbane time).

### ORDINARY BUSINESS

#### Financial Reports

To receive and consider the Company's Annual Report comprising the Directors' report and auditors' report, Directors' declaration, statement of comprehensive income, statement of financial position, statement of changes in equity, statement of cash flows and notes to and forming part of the financial statements for the Company and its controlled entities for the financial year ended 30 June 2012.

#### Resolution 1: Re-election of Mr Viv Forbes as a Non-Executive Director

To consider and, if thought fit, pass the following resolution as an ordinary resolution:

*That Mr Viv Forbes, who retires in accordance with Rule 38.1 of the Company's constitution and, being eligible, offers himself for re-election, be re-elected as a Non-Executive Director.*

#### Resolution 2: Re-election of Mr Neville Sneddon as a Non-Executive Director

To consider and, if thought fit, pass the following resolution as an ordinary resolution:

*That Mr Neville Sneddon, who retires in accordance with Rule 38.1 of the Company's constitution and, being eligible, offers himself for re-election, be re-elected as a Non-Executive Director.*

#### Resolution 3: Election of Mr Chris McAuliffe as a Non-Executive Director

To consider and, if thought fit, pass the following resolution as an ordinary resolution:

*That Mr Chris McAuliffe, who was appointed by the Board as a Non-Executive Director of the Company on 17 July 2012 be elected as a Non-Executive Director in accordance with Rule 36.2 of the Company's constitution.*

#### Resolution 4: Adoption of Remuneration Report

To consider and, if thought fit, pass the following advisory resolution:

*That the Remuneration Report for the year ended 30 June 2012 (as set out in the Directors' Report) is adopted.*

The vote on Resolution 4 is advisory only and does not bind the Directors of the Company.

## SPECIAL BUSINESS

### Resolution 5: Approval for issue of Shares to Greatgroup on conversion of the Convertible Notes

To consider and, if thought fit, pass the following resolution as an ordinary resolution:

*That for the purpose of Item 7 of section 611 of the Corporations Act, and for all other purposes, the Company be authorised to issue 13,373,377 Shares on conversion of the Convertible Notes to Greatgroup in accordance with the terms of the Subscription Deed and otherwise on the terms set out in the Explanatory Memorandum.*

### Resolution 6: Approval of the Share Issue Mandate

To consider and, if thought fit, pass the following resolution as a special resolution:

*That for the purposes of Listing Rule 7.1A and for all other purposes, the Company be authorised to issue up to 10% of the issued share capital of the Company (at the time of issue), calculated in accordance with the formula in Listing Rule 7.1A.2 and on the terms and conditions summarised in the Explanatory Memorandum.*

#### VOTING EXCLUSION STATEMENT – Resolutions 4, 5 and 6

The Company will disregard any votes cast on:

- Resolution 4 by any member of Key Management Personnel and any Closely Related Party of such a member;
- Resolution 5 by Greatgroup and its Associates; and
- Resolution 6 by:
  - (i) a person (and any Associates of such a person) who may participate in the proposed issue; and
  - (ii) a person who might obtain a benefit, except a benefit solely in the capacity of a holder of ordinary securities, if the resolution is passed.

However, the Company will not disregard a vote if it is:

- cast by a person as proxy for a person who is entitled to vote, in accordance with the directions on the proxy form; or
- cast by the person chairing the meeting as proxy for a person who is entitled to vote, in accordance with a direction on the proxy form to vote as the proxy decides.

#### Important information – Resolution 6

At the date of this Notice, the proposed allottees of the securities are not yet known or identified. For a person's vote to be excluded, it must be known that that person will participate in the proposed issue. Where it is not known who will participate in the proposed issue, Shareholders must consider the proposal on the basis that they may or may not get a benefit and that it is possible that their holding will be diluted.

**Please refer below to the important information about the appointment of proxies in relation to Resolution 4.**

To consider any other business as may be lawfully put forward in accordance with the constitution of the Company.

Specific comments relating to the Resolutions are set out in the Explanatory Memorandum.

**By order of the Board**

**Doug McAlpine**  
Joint Company Secretary

Date: 31 October 2012

# Shareholder information

## Proxy voting – Corporations Act

In accordance with the Corporations Act, a person appointed as a proxy must not vote, on the basis of that appointment, on Resolution 4, being connected directly or indirectly with the remuneration of a member of Key Management Personnel if:

- the proxy is either:
  - a member of Key Management Personnel; or
  - a Closely Related Party or a member of Key Management Personnel; and
- the appointment does not specify the way the proxy is to vote on the Resolution.

If the proxy form appoints the chair of the meeting as the proxy, but does not specify the way the proxy is to vote on the Resolution, and the appointment expressly authorises the chair to exercise the proxy even if the Resolution is connected directly or indirectly with the remuneration of a member of Key Management Personnel, the chair may vote the proxy. Further details regarding the appointment of the chair are included on the proxy form.

### How to vote

You may vote at the Meeting in person, by proxy or authorised corporate representative.

### Voting in person

To vote in person, attend the Meeting on the date and at the time set out in the Notice. The Meeting will commence at 10:00am (Brisbane time).

### Voting by proxy

A Member who is entitled to attend and cast a vote at the Meeting is entitled to appoint a proxy. A form of appointment of proxy is enclosed with this Notice.

The proxy need not be a Member of the Company. A Member who is entitled to cast two or more votes may appoint two proxies and make specified a proportion or number of votes each proxy is appointed to exercise. If the appointment does not specify a percentage or number and two proxies are appointed, each may exercise half of the votes to which that Member is entitled (in which case any fractional votes will be disregarded).

All proxy forms will need to be lodged with the Company no later than 48 hours before commencement of the Meeting, being 10:00am (Brisbane time) 27 November 2012. Any proxy form received after the time will not be valid for the Meeting.

If you wish to appoint a proxy and are entitled to do so, then complete the enclosed proxy

form in accordance with the instructions on it and return it to the Company's share registry by the deadline for lodgement as follows:

- by using a replied paid envelope enclosed with this Notice;
- by posting the proxy form to:  
**Computershare Investor Services Pty Limited**  
**GPO Box 242**  
**VICTORIA 3001 Australia;** or
- by faxing the proxy form to:  
**Computershare Investor Services Pty Limited**  
**(within Australia) 1800 783 447**  
**(outside Australia) +61 3 9473 2555**

Proxies given by corporate Shareholders must be executed in accordance with their constitutions, assigned by a duly authorised attorney.

A proxy may decide whether to vote on any motion, except where the proxy is required by law or the company's constitution to vote, abstained from voting, in their capacity as proxy. If a proxy is directed how to vote on an item of business, the proxy may vote on that item only in accordance with that direction. If a proxy is not directed how to vote on an item of business, a proxy may vote as he or she

thinks fit. If a Shareholder appoints the chair of the Meeting as a Shareholder's proxy and does not specify how the chair is to vote on an item of business, the chair will vote, as proxy for that Shareholder, in favour of the item.

### **Voting by corporate representatives**

A corporate Shareholder wishing to appoint a person to act as its representative at the Meeting must provide that person with an authority executed in accordance with the company's constitution and the Corporations Act authorising him or her to act as a company representative. The authority must be sent to the Company or its share registry in advance of the Meeting or hand it in at the Meeting when registering as a corporate representative.

### **Right to vote**

The Board has determined that, for the purposes of the Meeting, Shares will be taken to be held by the persons who were the registered holders of those Shares at 7.00pm (Sydney time) on 27 November 2012. Accordingly, the Share transfers registered after the time will be disregarded in determining entitlements to attend and vote at the Meeting.

### **Shareholder questions and comments**

The chair of the Meeting will provide Shareholders with an opportunity at the meeting to ask questions and make comments.

# Explanatory Memorandum

## Stanmore Coal Limited

This Explanatory Memorandum has been prepared for the information of Members of the Company in connection with the business to be conducted at the Annual General Meeting of the Company to be held at the Brisbane Polo Club, Naldham House, 193 Mary Street (cnr Eagle and Felix Streets), Brisbane, Queensland, Brisbane, Queensland on Thursday 29 November 2012 commencing at 10:00am (Brisbane time).

The purpose of this Explanatory Memorandum is to provide information that the Directors believe to be material to Shareholders in deciding whether or not to pass the Resolutions set out in the Notice. The Directors recommend Shareholders read the accompanying Notice and this Explanatory Memorandum in full before making any decision in relation to the Resolutions.

This Explanatory Memorandum forms part of and should be read in conjunction with the accompanying Notice. A number of words and terms used in this Explanatory Memorandum have defined meanings, which are set out in the glossary at the end of this document.

### ORDINARY BUSINESS

#### Financial Reports

The Corporations Act requires the financial report, the Directors' report and the auditor's report to be laid before the Annual General Meeting. There is no requirement either in the Corporations Act or in the constitution of the Company for Shareholders to approve the financial report, the Directors' report or the auditor's report. The Company's Annual Report is placed before the Shareholders for discussion. No voting is required for this item.

#### Resolution 1: Re-election of Mr Viv Forbes as a Non-Executive Director

In accordance with rule 38.1 of the constitution, Mr Viv Forbes, a Non-Executive Director, will retire at the Annual General Meeting and being eligible, has offered himself for re-election.

Mr Forbes was initially appointed as a Non-Executive Director on 5 October 2009.

Rule 38.1 of the constitution provides that at every Annual General Meeting of the Company one third of the Directors, other than the Managing Director, must retire from office. If the number of Directors is not a multiple of three, rule 38.1 of the constitution requires that the number of Directors nearest to, but not less than, one third of the Directors (other than the Managing Director) must retire from office.

Mr Forbes is a Bowen Basin pioneer with more than 40 years coal-industry experience including government service, field exploration, mine valuation and acquisition, financing, development, operations and successful asset sales. Mr Forbes has been involved in various capacities at Burton Coal, Dalrymple Bay Coal Terminal, South Blackwater Coal Mine, Tahmoor Coal Mine, Newlands/Collinsville Coal Mines, MIM, Utah Goonyella/Saraji and Gold Fields. Mr Forbes has a degree in Applied Science Geology and is a Fellow of the Australasian Institute of Mining and Metallurgy.

Mr Forbes is a member of the Audit and Risk Management Committee.

The Directors (with Mr Forbes abstaining) recommend that you vote in favour of this ordinary Resolution.

#### Resolution 2: Re-election of Mr Neville Sneddon as a Non-Executive Director

In accordance with rule 38.1 of the constitution, Mr Neville Sneddon, a Non-Executive Director, will retire at the Annual General Meeting and being eligible, has offered himself for re-election.

Mr Sneddon was initially appointed as a Non-Executive Director on 5 October 2009.

Rule 38.1 of the constitution provides that at every Annual General Meeting of the Company one third of the Directors, other than the Managing Director, must retire from office. If the number of Directors is not a multiple of three, rule 38.1 of the constitution requires that the number of Directors nearest to, but not less than, one third of the Directors (other than the Managing Director) must retire from office.

A mining engineer with over 37 years experience in most facets of the Queensland and NSW resource sectors, Mr Sneddon brings substantial Board and industry knowledge to Stanmore Coal. He has developed and operated both underground and open cut mines working for Coal & Allied in the Hunter Valley and from 1997 worked in a senior role in the NSW Mines Inspectorate, covering operations in all forms of mining in the state.

Moving to Queensland in 1999, Mr Sneddon accepted the position of Chief Operating Officer with Shell Coal, which was acquired by Anglo American's Australian coal operations the following year. Leaving as CEO in 2007, he held several Board positions with mining and infrastructure companies including Chairman of the operating company at Dalrymple Bay Coal Terminal near Mackay and Director of Port Waratah Coal Services, a major coal export facility at Newcastle.

Mr Sneddon has also been a member of the Boards of the Queensland, NSW and National Mining Councils. His expertise has been sought by several government committees such as the NSW Mine Subsidence Board, the NSW Mines Rescue Board, Queensland Ministerial Coal Mine Safety Advisory Committee and the joint federal/state advisory committee that is developing nationally consistent mining safety legislation. Mr Sneddon is presently on the Board of Envirogen and is the Chairman of CSM Energy and has recently stepped down from the Board of Centennial Coal.

Mr Sneddon is a member of the Audit and Risk Management Committee.

The Directors (with Mr Sneddon abstaining) recommend that you vote in favour of this ordinary Resolution.

### **Resolution 3: Election of Mr Chris McAuliffe as a Director**

In accordance with rule 36.2 of the constitution, Mr Chris McAuliffe, a Non-Executive Director, will retire at the Annual General Meeting and being eligible, has offered himself for re-election.

Mr McAuliffe was appointed as a Non-Executive Director on 17 July 2012. Mr McAuliffe was nominated by Greatgroup in accordance with its right to appoint a nominee Director under the Subscription Deed.

Rule 36.2 of the constitution provides that where a director is appointed to fill a causal vacancy or as an addition to the Board, they shall hold the office only until the next Annual General Meeting of the Company, and shall then be eligible for re-election.

Mr McAuliffe has more than 20 years' experience in private equity and investment banking with significant relationships across Asia. Prior to co-founding Sprint Capital in 2008, Mr McAuliffe was a Managing Director and co-head of Asia-Pacific Industrials Group at Citigroup in Hong Kong, prior to which he was a Managing Director and head of Asia Industrials and Services Group at Credit Suisse in Singapore.

The Directors (with Mr McAuliffe abstaining) recommend that you vote in favour of this ordinary Resolution.

### **Resolution 4: Remuneration Report**

The Remuneration Report is set out in the Directors' report section of the Annual Report. The Annual Report is available to download on the Company's website, [www.stanmorecoal.com.au](http://www.stanmorecoal.com.au).

In summary the Remuneration Report:

- explains the Board's policy for determining the nature and amount of remuneration of executive directors and other Key Management Personnel;
- explains the relationship between the Board's remuneration policy and the Company's performance;
- sets out remuneration details for each Director and the other most highly remunerated Key Management Personnel; and
- details and explains any performance conditions applicable to the remuneration of executive Directors and other Key Management Personnel.

A reasonable opportunity will be provided for discussion of the Remuneration Report at the Meeting.

Shareholders should be aware that any undirected proxies given to the Chairman will be cast by the Chairman and counted in favour of the Resolution.

Noting that each Director has a personal interest in their own remuneration from the Company as set out in the Remuneration Report, the Board unanimously recommends that Shareholders vote in favour of adopting the Remuneration Report. Under section 250R(3) of the Corporations Act, the vote is advisory only and does not bind the Directors or the Company.

## **SPECIAL BUSINESS**

### **Resolution 5: Approval for issue of Shares to Greatgroup on conversion of the Convertible Notes**

#### **(a) Background**

On 10 October 2012, Shareholder approval was obtained for the issue of various securities totalling \$36.04 million to Greatgroup Investments Limited (**Greatgroup**), an investment vehicle managed by Hong Kong based private equity investment manager Sprint Capital. Funds raised from Greatgroup were used by the Company, along with its Credit Suisse AG debt facility, to meet the Company's financial obligations leading up to execution of the take or pay arrangements for the Wiggins Island Coal Export Terminal, Surat Basin Rail and QR National Moura rail system infrastructure projects.

As a result of the Shareholder approvals, Greatgroup currently holds the following securities:

- 40.02 million Shares, comprising a Relevant Interest in 19.99% of the Company and
- 13.37 million Convertible Notes, which, following conversion, would increase Greatgroup and its Associates Relevant Interest in the Company to 25%.

The Company also obtained Shareholder approval to issue Investor Options to Greatgroup, which provide anti-dilution protection to Greatgroup to allow it to preserve its interest in the Company by subscribing for additional Shares and Convertible Notes upon the exercise of Incentive Options and CS Options. Further details about the Incentive Options and CS Options are included in the notice of general meeting dated 10 September 2012.

The Company is seeking Shareholder approval at this meeting for Greatgroup and its Associates to increase their Relevant Interest in the Company on conversion of the Convertible Notes to 25% without making a takeover bid for all of the Shares. Effectively, Greatgroup will be able to convert all of the Convertible Notes representing a further 5.01% Relevant Interest (assuming no further Shares are acquired by Greatgroup or its Associates and no dilutive new Shares are issued by the Company), during the 12 month period from 27 June 2014, being the first date on which the Convertible Notes become capable of conversion.

#### **(b) Advantages and disadvantages**

The Board considers that the advantages of approving the Resolution include the following:

- providing the Company with the ability to convert the Convertible Notes to equity rather than creating the need to repay the Convertible Notes out of cash reserves. This will allow the Company to preserve cash and avoid the need to make a payment of \$9.03 million to redeem the Convertible Notes at their maturity; and
- the Convertible Notes conversion price of \$0.675 per share is at a significant premium to both the VWAP at which Shares traded prior to the announcement of the funding arrangements with Greatgroup and the prices at which the Shares have traded since the announcement.

The Board considers that the disadvantages of approving the Resolution include that if the Convertible Notes conversion terms are approved and subsequently converted, the interests of non-associated Shareholders will be diluted.

A summary of the advantages and disadvantages of the proposed Resolution is contained in paragraph 12 of the Independent Expert's Report, a copy of which is included as **annexure A**. Shareholders are encouraged to read the Independent Expert's Report in full before making a decision about how to vote on this Resolution.

(c) Shareholder approval under item 7 of section 611 of the Corporations Act

Pursuant to section 606(1) of the Corporations Act, a person must not acquire a Relevant Interest in issued voting shares in a listed company if the person acquiring the interest does so through a transaction in relation to securities entered into by or on behalf of the person and because of the transaction, that person's or someone else's Voting Power in the Company increases:

- from 20% or below to more than 20%; or
- from a starting point that is above 20% to below 90%.

The calculation of a person's Voting Power in a company involves determining the voting shares in the Company in which the person and the person's Associates have a Relevant Interest.

Item 7 of section 611 of the Corporations Act provides an exception to the prohibition under section 606 of the Corporations Act. This exception provides that a person may acquire a Relevant Interest in a company's voting shares if Shareholders of the company approve the acquisition.

(d) Information required by the Corporations Act

For the exception in item 7 of section 611 of the Corporations Act to apply, Shareholders must be given all information known to Greatgroup or their Associates, or known to the Company, that is material to the decision on how to vote on the Resolution.

The following information is provided in compliance with the Corporations Act and ASIC Policy Statement 74:

|                                                                                                                                            |                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                        |
|--------------------------------------------------------------------------------------------------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <b>Identity of the person who will hold the Relevant Interest</b>                                                                          | Greatgroup.                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                            |
| <b>Maximum voting power of Greatgroup and its Associates as a result of the issue</b>                                                      | 25%.                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                   |
| <b>Maximum increase in the voting power of Greatgroup and its Associates as a result of the issue</b>                                      | 5.01%.                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                 |
| <b>When the proposed acquisition of Shares will occur</b>                                                                                  | <p>Under the terms of the Convertible Notes, the conversion period does not commence until 27 June 2014. This is subject to there being no change of control in the Company, in which case the Convertible Notes will automatically convert into Shares.</p> <p>The Convertible Notes mature:</p> <ul style="list-style-type: none"><li>• for those Convertible Notes issued on exercise of Investor Options as a result of the exercise of the CS Options on or after 15 June 2015, ten Business Days after the relevant CS Options are exercised; and</li><li>• otherwise on 27 June 2015.</li></ul> |
| <b>Agreements between the Company and Greatgroup or any of its Associates that are conditional on Shareholders passing this Resolution</b> | Nil                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                    |
| <b>Future intentions of Greatgroup</b>                                                                                                     | <p>The Company has been advised that Greatgroup's future intentions are as follows:</p> <p><i>Intention to change the business of the Company</i></p> <p>Greatgroup has no intention to change the nature of the business of the Company.</p> <p><i>Intention to inject further capital into the Company</i></p> <p>Greatgroup currently has no defined plans to inject further capital into the Company but, would consider capital raising opportunities should they arise.</p> <p><i>Future employment of present employees of the Company</i></p>                                                  |

|                                    |                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                           |
|------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
|                                    | <p>Greatgroup does not envisage any material changes to the employment of the present employees of the Company.</p> <p><i>Proposals where assets will be transferred between the Company and Greatgroup or their Associates</i></p> <p>Greatgroup does not currently have any defined plans to transfer assets between the Company and Greatgroup or its Associates.</p> <p><i>Intention to redeploy the fixed assets of the Company</i></p> <p>Greatgroup has no intention to redeploy the fixed assets of the Company.</p> <p><i>Intention of Greatgroup to significantly change the financial or dividend distribution policies of the entity</i></p> <p>Greatgroup has no intention to significantly change the financial or dividend distribution policies of the Company.</p>                                                                                                                                                       |
| <b>Independent Expert's Report</b> | <p>The Company engaged Lonergan Edwards &amp; Associates Limited to prepare an Independent Expert's Report in relation to Greatgroup and its Associates increasing their Relevant Interest to 25%.</p> <p>The Independent Expert was asked to consider whether, in its opinion, the Convertible Notes conversion terms are fair and reasonable to the Shareholders of the Company not associated with Greatgroup.</p> <p>The Independent Expert's opinion is that the Convertible Note conversion terms are not fair but are reasonable to Shareholders. The Independent Expert formed this view primarily because the Independent Expert considered the advantages to non-associated Shareholders on a conversion of the Convertible Notes significantly outweigh the disadvantages.</p> <p>The Company strongly recommends that you read the Independent Expert's Report in full, a copy of which is included as <b>annexure A</b>.</p> |

(e) Effect on control

Greatgroup currently has Voting Power of 19.99% and an economic interest of 25% of the Company through the Convertible Notes. This means that in the event of a control transaction for 100% of the Company, any bidder would need to engage with Greatgroup to obtain their support.

Greatgroup's current level of Voting Power is also likely to give Greatgroup the ability to block a special resolution of Shareholders (which requires 75% approval), depending on the number of Shares which are voted on the resolution.

If Resolution 5 is approved, Greatgroup's Voting Power will increase from 19.99% to 25% when the Convertible Notes are converted, which cannot happen before 27 June 2014. In practice, Greatgroup will have significant influence on the Company because of its Voting Power of 19.99% prior to that time.

While a conversion of the Convertible Notes will increase Greatgroup's voting interest in the Company, it does not provide Greatgroup with any additional rights regarding Board representation. Following conversion, Sprint Capital will not control the Board (at either an executive or total member level), nor will it control the day-to-day operations of the Company.

(e) Consequences if Shareholder approval is not received

If approval to increase Greatgroup's relevant interest is not obtained, Greatgroup will still be entitled under the statutory "creep" exemption in section 611(9) of the Corporations Act, to increase its Relevant Interest and Voting Power in the Company in every six month period from the date of the 25 October 2012 by a further 3% over the Voting Power Greatgroup held in the six months prior to that increase, provided they had Voting Power in the Company of at least 19% through the prior six month period as required by section 611(9) of the Corporations Act.

If the conversion terms of the Convertible Notes are not approved it is likely that (at the time) the Company would need to undertake an institutional placement and/or rights issue to fund redemption of the Convertible Notes. Such a placement or rights issue would be likely to be priced at a discount to the market price of the Shares at the time.

(f) Directors recommendation

As Chris McAuliffe was appointed by Sprint Capital he has declined to make a recommendation on this Resolution.

The remaining Directors recommend that all non-associated Shareholders vote in favour of the Resolution. This recommendation is based on the information available, including that contained in this Explanatory Memorandum and the Independent Expert's Report. In the opinion of the remaining Directors, the approval of this Resolution is in the best interests of the Company, particularly as the Convertible Notes would need to be repaid in cash at maturity if Shareholder approval is not obtained.

## Resolution 6: Approval of the Share Issue Mandate

### (a) General

ASX Listing Rule 7.1, subject to certain exceptions (none of which are relevant for the present purposes), requires prior approval of Shareholders for an issue of securities if the securities will, when aggregated with all other issues during the previous 12 months, exceed 15% of the number of securities on issue at the commencement of that 12 month period.

Listing Rule 7.1A provides that eligible entities may seek Shareholder approval to issue equity securities up to 10% of the entity's issued capital at the time of issue or agreement, through placements<sup>1</sup> over a 12 month period after the date that Shareholders approve the mandate to issue further securities (**Share Issue Mandate**).

An eligible entity for the purposes of Listing Rule 7.1A is an entity that is not included in the S&P/ASX 300 Index and has a market capitalisation of \$300 million or less.

As at 25 October 2012, the Company's market capitalisation was \$52.2 million, based on the closing price on that date. The Company is not included in the S&P/ASX 300 Index as at the time of this Notice. The Company is therefore an eligible entity for the purposes of ASX Listing Rule 7.1A.

The Share Issue Mandate is in addition to the Company's 15% placement capacity under ASX Listing Rule 7.1, and can provide the Company with capacity to issue up to 25% (in aggregate) of its issued share capital in any 12 month period.

The ability to issue securities under the Share Issue Mandate is subject to Shareholder approval by way of a special resolution. This requires the approval of 75% of the votes cast by Shareholders present and eligible to vote.

In accordance with ASX Listing Rule 7.1A, for Resolution 6 to be effective, a special majority, being 75% of votes cast by Shareholders present and eligible to vote (in person, by proxy, by attorney or, in the case of a corporate Shareholder, by a corporate representative), must be voted in favour of the resolution.

### (b) Specific information required by the ASX Listing Rules

For the purposes of ASX Listing Rule 7.3A, the Company advises as follows:

|                                              |                                                                                                                                                                                                                                                                                                                                                                                                                                                                                              |
|----------------------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <b>Minimum issue price</b>                   | The Company's equity securities will be issued at an issue price of not less than 75% of the VWAP over the 15 Trading Days immediately before:<br>(a) the date on which the price at which the equity securities are to be issued is agreed; or<br>(b) if the equity securities are not issued within five Trading Days of the date in paragraph (a) above, the date on which the securities are issued.                                                                                     |
| <b>Type of securities that may be issued</b> | Any equity securities issued under the Share Issue Mandate must be in the same class as an existing quoted class of securities of the Company.                                                                                                                                                                                                                                                                                                                                               |
| <b>Potential risk of dilution</b>            | See the dilution table below in paragraph (c) for further information about the potential risk of dilution from the Share Issue Mandate.                                                                                                                                                                                                                                                                                                                                                     |
| <b>Timing of potential issues</b>            | The Company will only issue and allot the securities during the 12 months after the date of the Annual General Meeting at which the approval is obtained. The approval under the Resolution 6 for the issue of equity securities will cease to be valid in the event that holders of the Company's equity securities approve a transaction involving a significant change to the nature or scale of the Company's activities <sup>2</sup> or disposal of its main undertaking <sup>3</sup> . |

<sup>1</sup> To sophisticated, professional and institutional investors (as those terms are defined in the Corporations Act).

<sup>2</sup> Listing Rule 11.1.2.

<sup>3</sup> Listing Rule 11.2.

|                                    |                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                               |
|------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <b>Purpose of potential issues</b> | <p>The Company may seek to issue the equity securities for cash for the following purposes:</p> <p>(a) meeting port and rail and other infrastructure commitments;</p> <p>(b) continued coal exploration and development activities, including expansion of the asset portfolio; and</p> <p>(c) general working capital.</p>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                  |
| <b>Allocation policy</b>           | <p>The Company's allocation policy will be dependent on the prevailing market conditions at the time of any proposed issue pursuant to the Share Issue Mandate. The identity of the allottees of equity securities will be determined on a case-by-case basis having regard to factors including, but not limited to, the following:</p> <p>(a) the methods of raising funds that are available to the Company;</p> <p>(b) the effect of the issue of the equity securities on the control of the Company;</p> <p>(c) the financial situation and solvency of the Company; and</p> <p>(d) advice from corporate, financial and broking advisers (if applicable).</p> <p>The allottees under the Share Issue Mandate have not been determined as at the date of this Notice but may include existing substantial holders of equity securities who are not related parties or Associates of a related party of the Company.</p> |
| <b>Prior Shareholder approval</b>  | <p>The Company has not previously obtained the approval of its Shareholders for the purpose of a Share Issue Mandate under ASX Listing Rule 7.1A.</p>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                         |

(c) Dilution table

The table below shows the potential dilution of holders of the ordinary Shares on the basis of three different assumed issue prices and numbers of equity securities on issue:

| Issued capital share                                        | Dilution when compared with indicative issued shares (200,492,804) | Issue of 10% of the enlarged share capital        |                                   |                                                   |
|-------------------------------------------------------------|--------------------------------------------------------------------|---------------------------------------------------|-----------------------------------|---------------------------------------------------|
|                                                             |                                                                    | \$0.13 per share<br>(50% decrease in issue price) | \$0.26 per share<br>(Issue price) | \$0.39 per share<br>(50% increase in issue price) |
| <b>200,492,804</b><br>Current issued share capital          | <b>10% dilution</b>                                                | 20,049,280 shares                                 | 20,049,280 shares                 | 20,049,280 shares                                 |
|                                                             | <b>Funds raised</b>                                                | \$2,606,406                                       | \$5,212,813                       | \$7,819,219                                       |
| <b>300,739,206</b><br>50% increase in issued share capital  | <b>15% dilution</b>                                                | 30,073,921 shares                                 | 30,073,921 shares                 | 30,073,921 shares                                 |
|                                                             | <b>Funds raised</b>                                                | \$3,909,610                                       | \$7,819,219                       | \$11,728,829                                      |
| <b>400,985,608</b><br>100% increase in issued share capital | <b>20% dilution</b>                                                | 40,098,561 shares                                 | 40,098,561 shares                 | 40,098,561 shares                                 |
|                                                             | <b>Funds raised</b>                                                | \$5,212,813                                       | \$10,425,626                      | \$15,638,439                                      |

**The table has been prepared on the following assumptions:**

- The issue price is \$0.26 based on the closing price of Shares on 25 October 2012.
- The current issued share capital has been calculated in accordance with the formula in Listing Rule 7.1A(2) as at 25 October 2012.
- The Company issues the maximum number of equity securities available under the Share Issue Mandate.
- No options are exercised or converted into Shares.
- The table shows only the effect of issues of the Company's equity securities under the Share Issue Mandate, not under the Company's 15% placement capacity.

# Glossary of terms

In the Notice and Explanatory Memorandum the following words and expressions have the following meanings:

|                                    |                                                                                                                                                                                                                                                                                         |
|------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <b>Annual General Meeting</b>      | means the annual general meeting of the Members convened pursuant to the Notice for the purposes of considering the resolutions set out in the Notice.                                                                                                                                  |
| <b>Annual Report</b>               | means the annual report of the Company for the year ended 30 June 2012.                                                                                                                                                                                                                 |
| <b>Associates</b>                  | has the meaning given in the Corporations Act.                                                                                                                                                                                                                                          |
| <b>ASX</b>                         | means ASX Limited ACN 008 624 691 or the stock market operated by it, as the context requires.                                                                                                                                                                                          |
| <b>ASX Listing Rules</b>           | the official listing rules of ASX.                                                                                                                                                                                                                                                      |
| <b>Board</b>                       | the board of Directors of the Company.                                                                                                                                                                                                                                                  |
| <b>Closely Related Party</b>       | has the meaning in section 9 of the Corporations Act.                                                                                                                                                                                                                                   |
| <b>Company</b>                     | Stanmore Coal Limited ACN 131 920 968.                                                                                                                                                                                                                                                  |
| <b>Convertible Note Placement</b>  | subject to Shareholder approval under Resolution 3, the issue of \$9,027,029.48 of notes convertible into 13,373,377 Shares at \$0.675 per Share.                                                                                                                                       |
| <b>Convertible Notes</b>           | convertible notes issued by the Company to Greatgroup (each a <b>Convertible Note</b> ) at 100% of their face value, and convertible to Shares.                                                                                                                                         |
| <b>Corporations Act</b>            | <i>Corporations Act 2001</i> (Cth).                                                                                                                                                                                                                                                     |
| <b>CS Options</b>                  | the 11,670,000 CS Options that were issued on 27 June 2012 to Credit Suisse AG pursuant to the Option Deed, which are currently only capable of being cash settled and will, on Resolution 5 being passed, and other conditions being satisfied, also become Equity Settled CS Options. |
| <b>Directors</b>                   | the directors of the Company from time to time (each a <b>Director</b> ).                                                                                                                                                                                                               |
| <b>Explanatory Memorandum</b>      | the explanatory memorandum that accompanies the Notice.                                                                                                                                                                                                                                 |
| <b>Greatgroup</b>                  | Greatgroup Investments Limited, a registered holder and purchaser of securities issued pursuant to the Subscription Deed.                                                                                                                                                               |
| <b>Independent Expert</b>          | means Lonergan Edwards & Associates Limited ACN 095 445 560.                                                                                                                                                                                                                            |
| <b>Independent Expert's Report</b> | means the report prepared by the Independent Expert annexed to this Notice.                                                                                                                                                                                                             |
| <b>Investor Options</b>            | the conditional options granted to Greatgroup to provide as anti-dilution protection, under the Subscription Deed (each an <b>Investor Option</b> ).                                                                                                                                    |
| <b>Key Management Personnel</b>    | a person having authority and responsibility for planning, directing and controlling the activities of the Company and its subsidiaries, directly or indirectly, including any Director (whether executive or otherwise) of the Company or any of its subsidiaries.                     |
| <b>Member</b>                      | means a Shareholder.                                                                                                                                                                                                                                                                    |
| <b>Notice</b>                      | the notice of meeting of Shareholders dated 31 October 2012.                                                                                                                                                                                                                            |
| <b>Relevant Interest</b>           | has the meaning given in the Corporations Act.                                                                                                                                                                                                                                          |
| <b>Remuneration Report</b>         | means the section of the Directors' report contained in the annual financial report of the Company for the year ended 30 June 2012 entitled "Remuneration Report".                                                                                                                      |

|                            |                                                                                                                                                                                                                                    |
|----------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <b>Resolution</b>          | means a resolution to be proposed at the Annual General Meeting.                                                                                                                                                                   |
| <b>Shares</b>              | fully paid ordinary shares in the capital of the Company (each a <b>Share</b> ).                                                                                                                                                   |
| <b>Shareholder</b>         | a registered holder of Shares.                                                                                                                                                                                                     |
| <b>Share Issue Mandate</b> | means the mandate to issue up to 10% of the entity's issued capital at the time of issue or agreement, through placements over a 12 month period after the date that Shareholders approve the mandate to issue further securities. |
| <b>Sprint Capital</b>      | Sprint Capital Partners (HK) Limited, and any of its affiliates and related parties.                                                                                                                                               |
| <b>Subscription Deed</b>   | the Subscription and Cooperation Deed between the Company and Greatgroup dated 27 June 2012, as amended by deed on or about 28 August 2012.                                                                                        |
| <b>Trading Day</b>         | has the meaning given in the ASX Listing Rules.                                                                                                                                                                                    |
| <b>Voting Power</b>        | has the meaning given in the Corporations Act.                                                                                                                                                                                     |
| <b>VWAP</b>                | volume weighted average price.                                                                                                                                                                                                     |

## **Annexure A - Independent Expert's Report**

# LONERGAN EDWARDS & ASSOCIATES LIMITED

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The Directors  
Stanmore Coal Limited  
Level 11, 10 Market Street  
Brisbane Qld 4000

25 October 2012

**Subject: Funding agreement with Greatgroup**

Dear Directors

## Introduction

- 1 On 28 June 2012 Stanmore Coal Limited (Stanmore Coal) announced that it had executed a subscription and co-operation agreement with Greatgroup Investments Limited (Greatgroup), an investment vehicle managed by Sprint Capital Partners (HK) Limited (Sprint Capital) to secure funding totalling \$36.04 million. Pursuant to the funding arrangements Greatgroup agreed to subscribe for:
  - (a) 40.02 million shares in Stanmore Coal at \$0.675 per share to raise \$27.01 million<sup>1</sup> (Placement Shares)
  - (b) 13.37 million zero coupon notes which are convertible into 13.37 million shares in Stanmore Coal at a conversion price of \$0.675 per share to raise \$9.03 million (the Notes)<sup>2</sup>.
- 2 The Notes will be convertible into ordinary shares on 27 June 2014, with conversion rights exercisable by either Greatgroup or the company. The Notes may mature, depending on the circumstances and in accordance with their terms, on a date which may be between 10 business days after 15 June 2015 up until 27 June 2015. Upon maturity, any Notes not converted by Greatgroup or the company will be redeemed for their face value (of \$0.675 per Note).
- 3 Approval of Stanmore Coal shareholders for the issue of the Placement Shares and Notes was obtained at a general meeting held on 10 October 2012. Greatgroup holds 19.99% of the issued share capital of Stanmore Coal, and Notes which on conversion could increase Greatgroup's shareholding in the company by up to 5.01%, to an aggregate shareholding of up to 25% based on issued share capital after the agreed allotment to Greatgroup.

---

<sup>1</sup> The first tranche of 19.23 million shares were allotted on 29 June 2012, raising \$12.98 million. The second tranche share placement was subject to Stanmore Coal shareholders' approval, which was received on 10 October 2012.

<sup>2</sup> The placement of the Notes and related anti-dilution rights were subject to the approval of Stanmore Coal shareholders which was received at the general meeting on 10 October 2012. The Notes have been allotted.

- 4 Greatgroup also holds anti-dilution options to subscribe for new shares and Notes. The issue of the anti-dilution options was also approved by shareholders on 10 October 2012. Greatgroup's anti-dilution rights will trigger on the exercise of a fixed number of board and management options, which were outstanding and in-the-money as at the date of the arrangements<sup>3</sup>. Stanmore Coal has also agreed to use its best endeavours to ensure that Greatgroup has the opportunity to participate pro-rata on any future capital raisings in the two years after the date of the subscription and co-operation agreement.
- 5 Stanmore Coal intends to use the proceeds of the share and Notes placements to provide funding for its short to medium term infrastructure and project development commitments and to fund working capital.

### Stanmore Coal

- 6 Stanmore Coal is a growth focused, pure play coal exploration and development company with a number of prospective coal projects and exploration areas within Queensland's Bowen and Surat Basins. Stanmore Coal is focused on the creation of shareholder value via the identification and development of coal deposits, with a focus on the prime coal bearing regions of the east coast of Australia. Stanmore Coal holds 100% interests in its coal project areas which cover 2,594 km<sup>2</sup>. These projects include significant deposits of open pit thermal coal and coking coal and are typically well located for export infrastructure.

### Greatgroup and Sprint Capital

- 7 Greatgroup is a special purpose investment vehicle which is managed by Sprint Capital.
- 8 Sprint Capital is a Hong Kong based private equity investment manager, focused on undertaking investments in the mining and natural resources sector. Sprint Capital seeks to invest in resources which are in high demand across China and the wider Asian region (including high grade thermal and metallurgical coal, oil and gas, iron ore, potash and copper). Sprint Capital's investment approach is to partner with strong management teams with a proven track record in bringing highly prospective exploration and development-stage projects through to production.

### Scope

- 9 The potential conversion of the Notes and related issue of Stanmore Coal shares may result in Greatgroup acquiring a relevant interest in Stanmore Coal of more than 20%. Accordingly there is a regulatory requirement for Stanmore Coal to commission an independent expert's report (IER).
- 10 Consequently the Directors of Stanmore Coal have requested that Lonergan Edwards & Associates Limited (LEA) prepare an IER stating whether, in LEA's opinion, the Notes conversion terms are fair and reasonable to the shareholders of Stanmore Coal not associated with Greatgroup.
- 11 LEA is independent of Stanmore Coal and Greatgroup and has no involvement with, or interest in, the outcome of the Notes and share placements other than the preparation of this report.

<sup>3</sup> The specific terms and conditions relevant to the anti-dilution rights are detailed in the related agreement.

## Summary of opinion

- 12 In our opinion the Notes conversion terms are not fair but are reasonable to Stanmore Coal shareholders not associated with Greatgroup. We have formed this view primarily because we consider the advantages to non-associated Stanmore Coal shareholders on a related conversion of the Notes significantly outweigh the disadvantages.
- 13 The advantages and disadvantages associated with conversion of the Notes and related approval by non-associated Stanmore Coal shareholders of the Notes conversion terms are summarised below:

### Advantages

- (a) Stanmore Coal has an on-going need for funding for its coal portfolio. The ability to convert the Notes to permanent equity funding, prima facie, preserves funding within the company and avoids the need to make a payment of \$9.03 million to redeem the Notes at a time when annual company operational cash flows have yet to be established
- (b) the Notes conversion price of \$0.675 per share is at a significant premium to both the volume weighted average price (VWAP) at which shares in Stanmore Coal traded prior to the trading halt which preceded the announcement of the funding arrangements with Greatgroup and the prices at which Stanmore Coal shares have traded subsequent to the announcement

### Disadvantages

- (c) the Notes conversion price of \$0.675 per share is below the full underlying value of Stanmore Coal shares and is therefore not fair when assessed under Australian Securities & Investments Commission (ASIC) Regulatory Guide 111 – *Content of expert reports* (RG 111)
  - (d) if the Notes conversion terms are approved, and in the event of a subsequent conversion of the Notes, the interests of non-associated Stanmore Coal shareholders will be moderately diluted. However, non-associated shareholders are likely to be diluted in any event, as Stanmore Coal is likely to require an alternative source of additional equity capital if the conversion terms of the Notes are not approved and the Notes have subsequently to be redeemed. In our view, an alternative equity issue (for example, to redeem the Notes) is likely to be significantly more dilutionary if priced at a discount to the listed market price at the time (consistent with the majority of equity capital raisings).
- 14 Pursuant to RG 111, when assessing the fairness of the Notes conversion terms (including the conversion price), the value of the Stanmore Coal shares to be allotted on conversion must be assessed on a 100% controlling interest basis (notwithstanding that pursuant to the funding arrangements entered into, Greatgroup will only acquire a significant (but not controlling) 25% interest in Stanmore Coal on a subsequent conversion of the Notes).

- 15 Given the circumstances of the proposed conversion of the Notes, in our opinion, it is more appropriate (from a commercial perspective) to assess the conversion price per share based on a value for Stanmore Coal shares which reflects the size of Greatgroup's potential increased shareholding and related proposed voting entitlement (particularly as Greatgroup will not control Stanmore Coal subsequent to a potential conversion of the Notes).
- 16 In our opinion, it is not commercially realistic to expect that Greatgroup would pay a full control premium for the shares in Stanmore Coal to be allotted to it pursuant to a conversion of the Notes. The conversion price of the Notes of \$0.675 per Stanmore Coal share represents a discount of 15.6% to the low end of our valuation range for Stanmore Coal shares on a 100% controlling interest basis. We consider this level of discount to be reasonable having regard to the increased interest of Greatgroup in Stanmore Coal that will arise on a conversion of the Notes. Accordingly we have concluded that the Notes conversion price is reasonable.

### **Implications if the Notes conversion terms are not approved**

- 17 In the event that the Notes conversion terms are not approved there are a number of implications for Stanmore Coal shareholders not associated with Greatgroup including:
  - (a) due to Stanmore Coal's on-going need for equity funding to advance both the development of The Range and related infrastructure together with the rest of its coal portfolio, if the conversion terms of the Notes are not approved it is likely that (at the time) Stanmore Coal would need to undertake an institutional placement and/or rights issue to fund redemption of the Notes at the maturity date
  - (b) such a placement or rights issue would be likely to be priced at a discount to the listed market price of Stanmore Coal shares at the time. In contrast, based on the proposed Notes conversion price, Greatgroup is paying a significant premium to the market price of Stanmore Coal shares prior to the announcement of the funding agreement with Greatgroup
  - (c) to the extent that a capital raising included a pro-rata rights issue, this would be likely to have a negative effect on the subsequent Stanmore Coal share price in the short-term
  - (d) the extent to which investors might be prepared to support an equity raising at the time by a company yet to establish operational cash flows (as is expected to be the situation of Stanmore Coal over the three year term of the Notes) is uncertain.

### **Conclusion**

- 18 As indicated above there are a number of advantages and disadvantages associated with approval of the Notes conversion terms. However, based on the above, on balance we consider the likely advantages of approval of the Notes conversion terms from the perspective of Stanmore Coal shareholders not associated with Greatgroup significantly outweigh the likely disadvantages.
- 19 In addition there are a number of negative implications for Stanmore Coal shareholders not associated with Greatgroup in the event the Notes conversion terms are not approved.
- 20 Accordingly, we have concluded that the Notes conversion terms are not fair but reasonable to Stanmore Coal shareholders not associated with Greatgroup.

**General**

- 21 In preparing this report we have considered the interests of Stanmore Coal shareholders as a whole. Accordingly, this report only contains general financial advice and does not consider the personal objectives, financial situations or requirements of individual shareholders.
- 22 The ultimate decision whether to approve the Notes conversion terms should be based on each Stanmore Coal shareholder's assessment of their own circumstances. If Stanmore Coal shareholders are in doubt about the action they should take in relation to the resolution covering the Notes conversion terms or matters dealt with in this report, Stanmore Coal shareholders should seek independent professional advice. For our full opinion on the Notes conversion terms and the reasoning behind our opinion, we recommend that Stanmore Coal shareholders read the remainder of our report.

Yours faithfully



Craig Edwards  
Authorised Representative



Martin Holt  
Authorised Representative

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## I The Notes

### Background

- 23 On 28 June 2012 Stanmore Coal announced that it had executed a subscription and co-operation agreement with Greatgroup, an investment vehicle managed by Sprint Capital to secure funding totalling \$36.04 million. Pursuant to the funding arrangements Greatgroup agreed to subscribe for:
- (a) 40.02 million shares in Stanmore Coal at \$0.675 per share to raise \$27.01 million<sup>4</sup> (Placement Shares); and
  - (b) 13.37 million zero coupon notes which convert into 13.37 million shares in Stanmore Coal at a conversion price of \$0.675 per share to raise \$9.03 million (the Notes).
- 24 The Notes will be convertible into ordinary shares on 27 June 2014, with conversion rights exercisable by either Greatgroup or the company. The Notes may mature, depending on the circumstances and in accordance with the terms, a date which may be between 10 business days after 15 June 2015 up until 27 June 2015. Upon maturity, any Notes not converted by Greatgroup or the company will be redeemed for their face value (of \$0.675 per Note).
- 25 Approval of Stanmore Coal shareholders for the issue of Placement Shares and Notes was obtained at a general meeting held on 10 October 2012. Greatgroup holds 19.99% of the issued share capital of Stanmore Coal, and Notes which on conversion could increase Greatgroup's shareholding in the company by up to 5.01%, to an aggregate shareholding of up to 25% based on issued share capital after the agreed allotment to Greatgroup. The conversion terms of the Notes are subject to approval by Stanmore Coal shareholders not associated with Greatgroup including Sprint Capital.
- 26 Greatgroup also holds anti-dilution options to subscribe for new shares and Notes. The issue of the anti-dilution options was approved by shareholders on 10 October 2012. Greatgroup's anti-dilution rights will trigger on the exercise of a fixed number of board and management options, which were outstanding and in-the-money as at the date of the arrangements<sup>5</sup>. Stanmore Coal has also agreed to use its best endeavours to ensure that Greatgroup has the opportunity to participate pro-rata on any future capital raisings in the two years after the date of the subscription and co-operation agreement.

### Rights

- 27 The rights attaching (or otherwise) to the Notes include the following:
- (a) the Notes rank at all times *pari passu* with all other present and future unsecured obligations of the company
  - (b) the Notes do not confer any entitlement to:
    - (i) vote at a general meeting of shareholders of the company

<sup>4</sup> The first tranche of 19.23 million shares were allotted on 29 June 2012, raising \$12.98 million. The second tranche share placement, Notes placement and related anti-dilution rights were subject to Stanmore Coal shareholders approval, which was received on 10 October 2012.

<sup>5</sup> The specific terms and conditions relevant to the anti-dilution rights are detailed in the related agreement.

- (ii) receive dividends; or
- (iii) participate in any issue of securities, other than on conversion of the Notes
- (c) holders of the Notes have the same rights as shareholders to receive notices of general meetings, reports and financial statements of the company
- (d) the Notes automatically convert to ordinary shares on a change in control event in respect of the company.

For personal use only

## II Scope of our report

### Purpose

- 28 If the conversion terms of the Notes are approved, a subsequent issue of Stanmore Coal shares on conversion of the Notes may result in Greatgroup holding a relevant interest of 25% in Stanmore Coal.
- 29 Section 606 of the *Corporations Act 2001 (Cth)* (Corporations Act) generally prohibits the acquisition of a relevant interest in issued voting securities of an entity if the acquisition results in a person's voting power in a company increasing from below 20% to more than 20%, or from a starting point between 20% and 90%, unless a permissible exception applies. A permissible exception to this general prohibition is set out in s611(7), whereby such an acquisition is allowed where the acquisition is approved by a majority of securityholders of the entity at a general meeting and no votes are cast in respect of securities held by the acquirer or any of its associates.
- 30 RG 111 sets out the view of ASIC on the operation of s611(7) of the Corporations Act. s611(7) of the Corporations Act allows shareholders to waive the prohibition in s606 and requires that shareholders approving a resolution pursuant to this section be provided with all material information in relation to the proposed transaction including an IER.
- 31 As conversion of the Notes and the related issue of shares may result in Greatgroup acquiring an interest of more than 20% in Stanmore Coal shares there is a regulatory requirement for Stanmore Coal to commission an IER.
- 32 Consequently, the Directors of Stanmore Coal have requested that LEA prepare an IER stating whether, in LEA's opinion, the Notes conversion terms are fair and reasonable to the non-associated shareholders of Stanmore Coal.
- 33 This report has been prepared to assist the Directors of Stanmore Coal in making their recommendation to the shareholders of Stanmore Coal not associated with Greatgroup, and to assist these shareholders assess the merits of the Notes conversion terms.
- 34 Our report should not be used for any other purpose or by any other party. The ultimate decision whether to approve the Notes conversion terms should be based on each shareholders' assessment of their own circumstances, including their risk profile, liquidity preference, tax position and expectations as to value and future market conditions. If in doubt about the resolution in respect of the Notes conversion terms or matters dealt with in this report, Stanmore Coal shareholders should seek independent professional advice.

### Basis of assessment

- 35 In preparing our report we have had regard to ASIC RG 111 and to the VALMIN Code. Under ASIC RG 111 the potential conversion of the Notes is "fair" if the conversion price of \$0.675 per Stanmore Coal share is equal to or greater than the value of Stanmore Coal shares on a 100% controlling interest basis.
- 36 The potential conversion of the Notes is "reasonable" if it is fair. The potential conversion of the Notes may also be reasonable if, despite being "not fair", there are sufficient reasons for securityholders to approve the Notes conversion terms.

- 37 RG 111 also states that the expert should identify the advantages and disadvantages of the proposal to the shareholders not associated with the transaction (i.e. Stanmore Coal shareholders other than Greatgroup), and should provide an opinion on whether the advantages of the proposal outweigh the disadvantages<sup>6</sup>.
- 38 Accordingly, we have also considered the overall impact on Stanmore Coal shareholders and formed an opinion as to whether, on balance, the advantages arising from a conversion of the Notes outweigh the disadvantages.
- 39 Our report has therefore considered whether the Notes conversion terms are fair and reasonable to Stanmore Coal shareholders not associated with Greatgroup, having regard to:

**Fairness**

- (a) the market value of Stanmore Coal shares on a 100% controlling interest basis
- (b) the price at which the Notes convert to shares in Stanmore Coal (i.e. \$0.675 per share)
- (c) the extent to which (a) and (b) differ (in order to assess whether the conversion price of the Notes is fair under ASIC RG 111)

**Reasonableness**

- (d) the conversion price of the Notes relative to the listed market price of Stanmore Coal shares prior to the announcement of the funding arrangements
- (e) the conversion price of the Notes relative to the price at which Stanmore Coal could raise further equity capital in an alternative placement and/or rights issue
- (f) the impact of the potential conversion of the Notes on the ownership and control of Stanmore Coal
- (g) the potential benefits resulting from conversion of the Notes including, for example, access to permanent project development financing
- (h) the implications for Stanmore Coal if shareholders do not approve the conversion rights (e.g. the need to repay the Notes on maturity<sup>7</sup>)
- (i) share market trading in Stanmore Coal shares subsequent to the announcement of the funding arrangements
- (j) other qualitative and strategic issues associated with a potential conversion of the Notes and the extent to which, on balance, they may advantage or disadvantage existing Stanmore Coal shareholders other than Greatgroup and its associates.

**Limitations and reliance on information**

- 40 Our opinions are based on the economic, sharemarket, financial and other conditions and expectations prevailing at the date of this report. Such conditions can change significantly over relatively short periods of time.

<sup>6</sup> RG 111.39.

<sup>7</sup> Pursuant to Stanmore Coal shareholder approval (obtained at the general meeting on 10 October 2012, the Notes will be issued to Greatgroup prior to seeking shareholder approval at the annual general meeting for the attaching conversion rights.

- 41 Our report is also based upon financial and other information provided by Stanmore Coal and its advisers. We understand the accounting and other financial information that was provided to us has been prepared in accordance with the Australian equivalents to International Financial Reporting Standards. We have considered and relied upon this information and believe that the information provided is reliable, complete and not misleading and we have no reason to believe that material facts have been withheld.
- 42 The information provided was evaluated through analysis, enquiry and review to the extent considered appropriate for the purpose of forming an opinion on the proposed conversion terms of the Notes from the perspective of Stanmore Coal shareholders not associated with Greatgroup. However, we do not warrant that our enquiries have identified or verified all of the matters which an audit, extensive examination or “due diligence” investigation might disclose. Whilst LEA has made what it considers to be appropriate enquiries for the purpose of forming its opinion, “due diligence” of the type undertaken by companies and their advisers in relation to (for example) prospectuses or profit forecasts is beyond the scope of an IER.
- 43 Accordingly, this report and the opinions expressed therein should be considered more in the nature of an overall review of the anticipated commercial and financial implications of the proposed transaction, rather than a comprehensive audit or investigation of detailed matters.
- 44 An important part of the information base used in forming an opinion of the kind expressed in this report is comprised of the opinions and judgement of management of the relevant companies. This type of information has also been evaluated through analysis, enquiry and review to the extent practical. However, it must be recognised that such information is not always capable of external verification or validation.
- 45 We in no way guarantee the achievability of budgets or forecasts of future profits. Budgets and forecasts are inherently uncertain. They are predictions by management of future events which cannot be assured and are necessarily based on assumptions of future events, many of which are beyond the control of management. Actual results may vary significantly from forecasts and budgets with consequential valuation impacts.
- 46 In forming our opinion, we have also assumed that the information set out in the Explanatory Memorandum is complete, accurate and fairly presented in all material respects.

#### **Reliance on technical experts**

- 47 Our assessed value of The Range project is based on the pre-feasibility study (PFS) completed in November 2011. The PFS reflected the opinions of mining experts (such as The Minserve Group) on technical mining matters, including the reliability of reserve and resource estimates, recovery rates, mining plans and the appropriate operating and capital cost estimates. Stanmore Coal management have advised that nothing has come to their attention from the on-going feasibility work to suggest a need to change any of the key assumptions contained in the PFS. LEA has relied on the results of the PFS and subsequent work to date when forming our opinion on the value of The Range project.
- 48 In making references to Stanmore Coal’s coal reserves and resources in this report we have relied on publicly disclosed statements of reserves and resources issued by Stanmore Coal. LEA does not certify these reserves and resources for the purpose of the Joint Ore Reserves Committee (JORC) Code.

### III Profile of Stanmore Coal

#### Overview

- 49 Stanmore Coal is an Australian Securities Exchange (ASX) listed coal mining company with advanced development and early stage coal assets located in the Surat and Bowen basins in Queensland, Australia. The company has JORC marketable reserves of 94 million tonnes (Mt), recoverable reserves of 117 Mt and resources of 498 Mt, consisting primarily of export quality thermal coal from its key coal project The Range. A PFS on The Range was completed in November 2011, and a Bankable Feasibility Study (BFS) is currently underway. First production is being targeted for mid 2016, but is subject to the timing and completion of requisite planned rail and port infrastructure.
- 50 Stanmore Coal also recently completed a concept study on the Belview coking coal project, and is undertaking a concept study at its Mackenzie coking coal project. The exploration portfolio also comprises prospective early stage assets located in the Bowen Basin within close proximity to operating mines held by major international coal miners.

#### The Range

- 51 Stanmore Coal's primary development project is The Range, which is an open-cut export quality thermal coal project located 27 km south-east of both the Wandoan project (Xstrata) and the proposed Surat Basin Rail line (SBR) (which will provide a link to the Wiggins Island Coal Export Terminal (WICET) and other Gladstone port infrastructure). Current marketable reserves of 94 Mt and resources of 260 Mt support an initial 20 year mine life, with potential to increase reserves based on current drilling underway<sup>8</sup>. The company is targeting BFS completion by the end of 2012.
- 52 The key features of the PFS include saleable coal production of 5 Mt per annum (Mtpa) assuming required rail and port capacity is available, a recovery yield of some 80% (14.4% ash product) and an average strip ratio of 6.7:1 (over first 17 years of mine life). Both owner mining and contract mining scenarios were evaluated.
- 53 Stanmore Coal is well progressed in securing sufficient infrastructure to support its production plans for The Range, having entered into a Capacity Commitment Deed (CCD) in respect of an allocation of 5 Mtpa port capacity at Wiggins Island Coal Export Terminal Expansion Phase 1 (WEXP1) and being in advanced discussions in connection with related rail capacity via SBR and QR National. Stanmore Coal also has an additional 2 Mtpa of priority access rights for Wiggins Island Coal Export Terminal Expansion Phase 2 (WEXP2).

#### Coal quality

- 54 Surat Basin coals are typically clean burning with low nitrogen, ash and sulphur. The Range coal is suitable for all key markets including Japan, China, Korea and India. The coal is capable of being washed to a range of ash levels from 10.0% to 14.4%. The indicative coal quality for The Range project under different wash scenarios identified in the PFS is as follows.

<sup>8</sup> We understand that the mine plan outlined by the PFS proposes a mine life of 26 years based on a conversion of current JORC resources to JORC reserves.

| The Range – coal quality |                              | 10% ash | 12% ash | 14.4% ash |
|--------------------------|------------------------------|---------|---------|-----------|
| Volatile matter          | % ad <sup>(1)</sup>          | 41.6    | 40.7    | 39.8      |
| Fixed carbon             | % ad                         | 40.4    | 39.3    | 37.7      |
| Total sulphur            | % ad                         | 0.4     | 0.4     | 0.4       |
| Nitrogen                 | % daf <sup>(2)</sup>         | 1.1     | 1.1     | 1.1       |
| Total moisture           | %                            | 14.0    | 13.5    | 13.0      |
| Gross calorific value    | kcal / kg ad <sup>(3)</sup>  | 6,375   | 6,217   | 6,026     |
| Gross calorific value    | kcal / kg daf <sup>(4)</sup> | 7,774   | 7,771   | 7,777     |

**Note:**

- 1 ad is air dried.
- 2 daf is dry ash free.
- 3 kcal / kg ad kilocalorie per kilogram.
- 4 Kcal / kg daf kilocalorie per dry ash free kilogram.

- 55 The coal quality analysis in the PFS indicates that only the energy content of the coal is outside the Newcastle benchmark<sup>9</sup>. This is a common occurrence among coal types and is adjusted in the market with a pro-rata discount to the benchmark price based on the difference (short-fall) of the energy content from the benchmark specification. Based on a 14.4% ash product (as reflected in the PFS) a 9.6% pricing discount would apply. Surat Basin coals with similar specifications are currently exported to the Asian utility market.

**Infrastructure**

- 56 A key issue for Stanmore Coal's The Range project is access to infrastructure and securing access to adequate rail and port capacity, most of which is yet to be built.

**Port**

- 57 As noted above, Stanmore Coal recently executed a CCD for WEXP1 which will provide Stanmore Coal with 5 Mtpa of port capacity for The Range project. The planned capacity for the WEXP1 terminal is 32.2 Mtpa which has been allocated to four coal companies from the Surat and Bowen basins. Stanmore Coal also possesses an additional 2 Mtpa of priority access rights which remain valid for use in the planned WEXP2 expansion.
- 58 Each proponent, including Stanmore Coal, has entered into a CCD supported by a bid bond which sets out their intention to meet their proportionate share of WEXP1's early works costs up to financial close, and upon financial close sets out a framework which would allow those proponents to execute long-term take-or-pay agreements. Stanmore Coal's share of these costs is \$44 million, \$26 million of which was provided at the time of CCD execution. The remaining \$18 million is payable in accordance with the WEXP1 financing plan. The \$44 million bid bond is proposed to be converted to an equity interest in the WEXP1 port expansion at financial close.

**Rail**

- 59 The Range has satisfied the due diligence requirements for the SBR project and expects to sign a SBR CCD for 5 Mtpa capacity. Similar to WEXP1, this commitment is a precursor to executing an SBR Access Agreement (containing take-or-pay obligations) at financial close.

<sup>9</sup> Newcastle coals set benchmark standards for high quality thermal coals.

- 60 In addition The Range is one of four projects that has been invited by QR National to participate in the final feasibility phase of the Gladstone Rail Capacity Expansion process. This will involve funding a detailed feasibility study into a capacity upgrade of the existing QR National Moura line linking the SBR with WICET.

### Project funding

- 61 Current estimated capital expenditure requirements for The Range project total some \$407 million<sup>10</sup> (based on an assumed contract mining scenario). A key challenge facing Stanmore Coal therefore is to raise the necessary funding to finance the project development. In this regard a range of options are available to the company including:
- (a) the sale of a joint venture stake in one (or more) of its projects
  - (b) the issue of shares via a capital raising to existing shareholders or otherwise to new strategic investors
  - (c) the issue of debt and/or project finance.
- 62 The company is in discussions with a number of potential project partners in respect of purchasing a minority interest in The Range project. It is expected that a minority interest sale transaction will involve the investor entering into agreements to purchase a proportional share of project off-take and assist the company in financing its port and rail infrastructure obligations. Post completion of the BFS and identification of a project partner the company will commence discussions with financiers in respect of project / construction finance.

### Other projects

- 63 Stanmore Coal's other projects include:
- (a) **Belview** – an underground hard coking coal prospect in the Bowen Basin currently at the development stage (concept study completed) with JORC inferred resource of 95 Mt. The Blackwater to Gladstone railway line runs some 5 km north of the tenement boundary. The project has the potential to produce low ash coking coal with a high crucible swelling number (CSN). Technical aspects associated with the proposed mining method (including depth of coal deposit) are currently being evaluated
  - (b) **Mackenzie** – an open cut coking coal project located in Bowen Basin on the existing Blackwater railway line to coal ports at Gladstone. The project contains 143 Mt of JORC resources (indicated and inferred status) and is at the development stage, with test work continuing and a concept study underway. A primary focus of the study will be the identification of optimal areas in the deposit where coal liberation techniques can be utilised effectively
  - (c) **Tennyson** – an underground coking and export thermal coal exploration prospect in the Bowen Basin. Initial drilling results support an exploration target of 220 Mt to 290 Mt. Drilling continues targeting an initial JORC inferred resource expected in late 2012
  - (d) **Kerlong** – an exploration project targeting underground coking / pulverised coal injection (PCI) coal. Located 8 km north of the Goonyella rail line to Dalrymple Bay Coal Terminal (DBCT) in the Bowen Basin. Exploration drilling has commenced

<sup>10</sup> In real dollar terms (i.e. before allowance for inflation).

- (e) **New Cambria** – early stage exploration project targeting low-volatile PCI coal with open-cut potential. Adjacent to the Blackwater rail line to Gladstone.

## Reserves and resources

- 64 The reserves and resources held by Stanmore Coal as at 31 August 2012 were as follows.

| Stanmore Coal – reserves and resources |           |               |             |                |          |       |
|----------------------------------------|-----------|---------------|-------------|----------------|----------|-------|
| Project                                | Coal type | JORC reserves |             | JORC resources |          | Total |
|                                        |           | Marketable    | Recoverable | Indicated      | Inferred |       |
|                                        |           | coal<br>Mt    | coal<br>Mt  | Mt             | Mt       |       |
| The Range                              | Thermal   | 94.2          | 117.5       | 184.0          | 76.0     | 260.0 |
| Mackenzie                              | Coking    | -             | -           | 25.7           | 117.5    | 143.2 |
| Belview                                | Coking    | -             | -           | -              | 95.0     | 95.0  |
| Total                                  |           | 94.2          | 117.5       | 209.7          | 288.5    | 498.2 |

## Financial performance

- 65 The financial performance of Stanmore Coal for the period ended 30 June 2010<sup>11</sup> and the two years ended 30 June 2012 is set out below.

| Stanmore Coal – statement of financial performance |                           |                           |                           |
|----------------------------------------------------|---------------------------|---------------------------|---------------------------|
|                                                    | FY10<br>Audited<br>A\$000 | FY11<br>Audited<br>A\$000 | FY12<br>Audited<br>A\$000 |
| Revenue                                            | 101                       | 800                       | 899                       |
| Employee benefits expense                          | (754)                     | (928)                     | (2,993)                   |
| Depreciation and amortisation expenses             | (3)                       | (14)                      | (36)                      |
| Finance costs                                      | -                         | (141)                     | (1,432)                   |
| Legal expenses                                     | (106)                     | (190)                     | (607)                     |
| Administration and consulting expenses             | (805)                     | (790)                     | (1,462)                   |
| Other expenses                                     | (187)                     | (825)                     | (1,969)                   |
| <b>Profit / (loss) before income tax</b>           | <b>(1,754)</b>            | <b>(2,088)</b>            | <b>(7,600)</b>            |
| Income tax expense                                 | -                         | -                         | -                         |
| <b>Profit / (loss) after income tax</b>            | <b>(1,754)</b>            | <b>(2,088)</b>            | <b>(7,600)</b>            |

- 66 As a coal exploration and development company, Stanmore Coal capitalises the majority of its exploration and development expenditure. Reported losses reflect mainly employee benefits and administrative expenses, partially offset by interest and miscellaneous other income.

<sup>11</sup> Stanmore Coal was listed on the ASX on 4 December 2009.

## Financial position

67 The financial position of Stanmore Coal as at 30 June 2011 and 2012 is set out below.

| Stanmore Coal – statement of financial position |                                |                                |
|-------------------------------------------------|--------------------------------|--------------------------------|
|                                                 | 30 Jun 11<br>Audited<br>A\$000 | 30 Jun 12<br>Audited<br>A\$000 |
| Cash and cash equivalents                       | 18,182                         | 23,957                         |
| Trade and other receivables                     | 722                            | 1,700                          |
| Other current assets                            | 20                             | 6,963                          |
| <b>Total current assets</b>                     | <b>18,925</b>                  | <b>32,620</b>                  |
| Plant and equipment                             | 2,039                          | 2,116                          |
| Exploration and evaluation expenditure          | 14,698                         | 28,659                         |
| Capitalised development costs                   | -                              | 5,827                          |
| Other non-current assets                        | 82                             | 2,572                          |
| <b>Total non-current assets</b>                 | <b>16,819</b>                  | <b>39,174</b>                  |
| <b>Total assets</b>                             | <b>35,744</b>                  | <b>71,794</b>                  |
| Trade and other payables                        | 3,743                          | 3,324                          |
| Other current financial liabilities             | -                              | 1,400                          |
| <b>Total current liabilities</b>                | <b>3,743</b>                   | <b>4,724</b>                   |
| Interest bearing liabilities                    | -                              | 4,040                          |
| <b>Total non-current liabilities</b>            | <b>-</b>                       | <b>4,040</b>                   |
| <b>Total liabilities</b>                        | <b>3,743</b>                   | <b>8,764</b>                   |
| <b>Net assets</b>                               | <b>32,001</b>                  | <b>63,030</b>                  |

**Note:**

1 Rounding may exist in the above.

## Cash and cash equivalents

68 As at 30 June 2012 Stanmore Coal held \$23.96 million in cash, including \$12.98 million raised pursuant to the allotment of tranche one shares to Greatgroup on 29 June 2012.

## Debt facility

69 Funds raised from the issue of Stanmore Coal shares to Greatgroup, combined with funds from a \$25 million Credit Suisse AG debt facility (CS Facility), are projected by Stanmore Coal management to be sufficient to enable the company to fund its bid bond and equity contributions associated with securing rail and port infrastructure prior to signing respective take-or-pay contracts.

70 The \$25 million CS Facility is available for drawdown by Stanmore Coal at any time. Draw downs are planned as and when the company requires funding to meet its current commitments to finance WEXP1 early works obligations (prior to execution of the take-or-pay contracts) and its SBR and QR National commitments.

- 71 The CS Facility requires Stanmore Coal to raise additional capital of \$25 million by 31 October 2012, a requirement capable of being met following Stanmore Coal shareholder approval on 10 October 2012 of the various further issues of securities to Greatgroup.

## Share capital and performance

- 72 As at 31 August 2012 Stanmore Coal had 179,409,108 fully paid ordinary shares on issue<sup>12</sup>. In addition the company had 15.9 million options on issue at exercise prices ranging from \$0.15 per share to \$2.50 per share and 11.67 million options to be issued to Credit Suisse AG in connection with the CS Facility.

| Stanmore Coal – options outstanding |                   |                      |             |
|-------------------------------------|-------------------|----------------------|-------------|
| Security type                       | Number            | Exercise price<br>\$ | Expiry date |
| Unlisted options                    | 525,000           | 0.153                | 16 Jan 14   |
| Unlisted options                    | 6,350,000         | 0.193                | 9 Dec 12    |
| Unlisted options                    | 3,500,000         | 0.193                | 31 Dec 13   |
| Unlisted options                    | 100,000           | 0.733                | 31 Dec 13   |
| Unlisted options                    | 100,000           | 0.873                | 31 Dec 13   |
| Unlisted options                    | 100,000           | 1.093                | 31 Dec 13   |
| Unlisted options                    | 75,000            | 1.44                 | 30 Mar 15   |
| Unlisted options                    | 75,000            | 1.68                 | 30 Mar 15   |
| Unlisted options                    | 75,000            | 1.80                 | 30 Mar 15   |
| Unlisted options                    | 500,000           | 1.75                 | 31 Dec 15   |
| Unlisted options                    | 500,000           | 2.00                 | 31 Dec 15   |
| Unlisted options                    | 500,000           | 2.25                 | 31 Dec 15   |
| Unlisted options                    | 500,000           | 2.50                 | 31 Dec 15   |
| Unlisted options                    | 400,000           | 1.75                 | 31 Dec 15   |
| Unlisted options                    | 400,000           | 2.00                 | 31 Dec 15   |
| Unlisted options                    | 400,000           | 2.25                 | 31 Dec 15   |
| Unlisted options                    | 450,000           | 1.75                 | 31 Mar 16   |
| Unlisted options                    | 450,000           | 2.00                 | 31 Mar 16   |
| Unlisted options                    | 450,000           | 2.25                 | 31 Mar 16   |
| Unlisted options                    | 450,000           | 2.50                 | 31 Mar 16   |
|                                     | <u>15,900,000</u> |                      |             |
| Options to be issued                | 11,670,000        | 0.518                | 27 Jun 14   |

<sup>12</sup> Including 19.22 million shares issued to Greatgroup on 29 June 2012. Stanmore Coal shareholder approval for a further issue of 20.79 million shares to Greatgroup was received on 10 October 2012.

### Significant shareholders

- 73 As at 31 August 2012 Stanmore Coal's substantial shareholders held 28.4% of the issued capital of the company, as shown below.

| Stanmore Coal – substantial shareholders                |                  |             |
|---------------------------------------------------------|------------------|-------------|
| Shareholder                                             | Number of shares | % of shares |
| St Lucia Resources International Pty Ltd <sup>(1)</sup> | 31,700,270       | 17.7        |
| Greatgroup Investments Limited <sup>(2)</sup>           | 19,228,887       | 10.7        |
|                                                         | 50,929,157       | 28.4        |

**Note:**

- 1 A company associated with two Stanmore Coal directors.  
2 An investment vehicle managed by Sprint Capital.

### Share price performance

- 74 The price of Stanmore Coal shares from 9 December 2009 (the day the company commenced trading on the ASX) to 31 August 2012 is summarised below.

| Stanmore Coal – share price performance |            |           |             |                                         |
|-----------------------------------------|------------|-----------|-------------|-----------------------------------------|
|                                         | High<br>\$ | Low<br>\$ | Close<br>\$ | Monthly<br>volume <sup>(1)</sup><br>000 |
| <b>Quarter ended</b>                    |            |           |             |                                         |
| December 2009                           | 0.80       | 0.31      | 0.75        | 4,066                                   |
| March 2010                              | 1.02       | 0.63      | 0.88        | 7,067                                   |
| June 2010                               | 0.96       | 0.59      | 0.65        | 2,799                                   |
| September 2010                          | 1.17       | 0.62      | 1.10        | 4,120                                   |
| December 2010                           | 1.53       | 1.04      | 1.40        | 8,449                                   |
| March 2011                              | 1.49       | 1.07      | 1.25        | 3,912                                   |
| June 2011                               | 1.45       | 0.95      | 1.01        | 3,281                                   |
| September 2011                          | 1.30       | 0.72      | 0.75        | 4,624                                   |
| December 2011                           | 1.03       | 0.68      | 0.74        | 4,847                                   |
| <b>Month ended</b>                      |            |           |             |                                         |
| January 2012                            | 0.81       | 0.74      | 0.76        | 4,045                                   |
| February 2012                           | 0.95       | 0.78      | 0.85        | 7,735                                   |
| March 2012                              | 0.85       | 0.75      | 0.80        | 4,514                                   |
| April 2012                              | 0.81       | 0.69      | 0.70        | 3,470                                   |
| May 2012                                | 0.71       | 0.46      | 0.49        | 9,474                                   |
| June 2012                               | 0.50       | 0.33      | 0.43        | 12,873                                  |
| July 2012                               | 0.53       | 0.33      | 0.36        | 6,886                                   |
| August 2012                             | 0.41       | 0.31      | 0.37        | 6,578                                   |

**Note:**

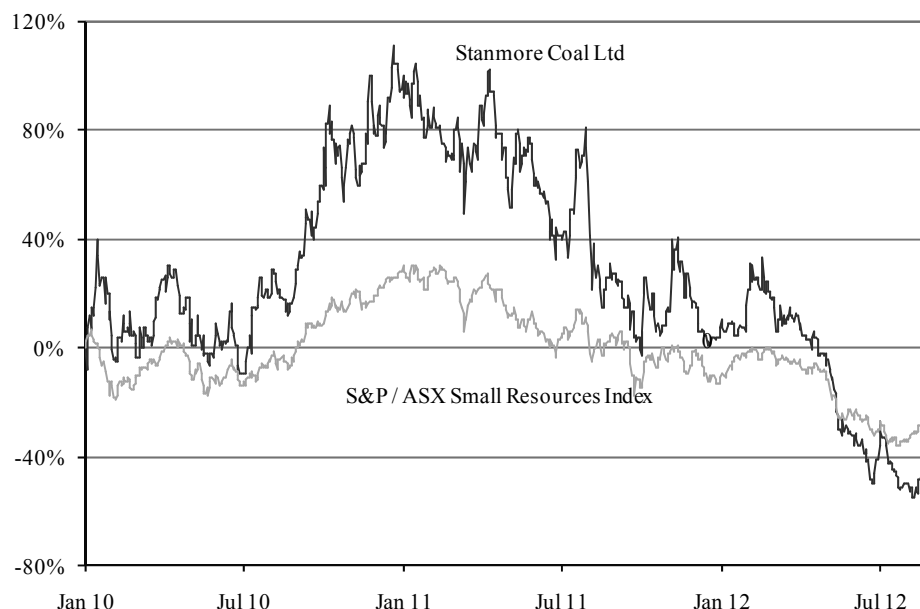
- 1 Monthly volumes for the quarter ended represent average monthly volumes.

**Source:** Bloomberg.

- 75 The following chart illustrates the relative movement in both the share price of Stanmore Coal and the S&P / ASX Small Resources Index from 1 January 2010<sup>13</sup> to 31 August 2012.

**Stanmore Coal – relative price history**

**1 January 2010 to 31 August 2012**



Source: Bloomberg.

- 76 From the date of listing to the share price peak (in December 2010) we note that there were positive dynamics for the coal industry, including the emergence of China as a significant net importer of coal for the first time, increased spot coal prices and high expectations for new coal contract negotiations. Coal development companies such as Stanmore Coal generally out-performed the S&P / ASX Small Resources Index during this period.
- 77 Prior to the share price peak and particularly more recently there has been weakened thermal coal demand due to, inter alia, slowing growth from importers of Australian coal, the substitution effect of all time low gas prices (from abundant US shale gas reserves) combined with increased seaborne coal. US exporters have sought to supply the European coal market forcing Columbia producers to commence the negotiation of new Asian coal export markets (also due to low shipping costs). This has reduced recent thermal coal prices and sentiment for coal stocks generally.

<sup>13</sup> We have shown the relative movements from 1 January 2010 rather than at the initial listing date to eliminate the effects of the initial volatile trading in Stanmore Coal shares post initial public offering (IPO).

### Liquidity in Stanmore Coal shares

- 78 The liquidity in Stanmore Coal shares based on trading on the ASX over the 12 month period prior to 31 August 2012 is set out below.

| Stanmore Coal – liquidity in shares |            |           |                 |               |                    |                             |
|-------------------------------------|------------|-----------|-----------------|---------------|--------------------|-----------------------------|
|                                     | Start date | End date  | Value<br>A\$000 | Volume<br>000 | As a % of<br>WANOS | WANOS <sup>(1)</sup><br>000 |
| 3 months                            | 01 Jun 12  | 31 Aug 12 | 10,534          | 26,337        | 15.2               | 172,901                     |
| 6 months                            | 01 Mar 12  | 31 Aug 12 | 21,933          | 43,795        | 26.3               | 166,609                     |
| 1 year                              | 01 Sep 11  | 31 Aug 12 | 46,341          | 73,071        | 48.0               | 152,273                     |

**Note:**

1 WANOS – Weighted average number of share on issue.

**Source:** Bloomberg, LEA analysis.

- 79 Trading in Stanmore Coal shares in the 12 months to 31 August 2012 was equivalent to 48.0% of the weighted average number of shares on issue during the period, representing a reasonable level of market liquidity in Stanmore Coal shares.

## IV Coal industry overview

### Overview

- 80 Stanmore Coal is currently developing a number of coal projects, the most advanced of which is The Range project in the Surat Basin, which is expected to produce export quality thermal coal. The Range project plans to utilise export capacity at WICET and is also dependent on the construction of the Surat Basin Rail (SBR). The other projects owned by the company contain deposits of metallurgical and thermal coals and are in the exploration stage and located primarily in the Bowen Basin.
- 81 This section therefore discusses the dynamics of the global and Australian coal industries with particular emphasis on the types of coal expected to be produced by Stanmore Coal and the coal mining regions in which Stanmore Coal operates (i.e. the Bowen Basin and the Surat Basin).

### Global coal markets

- 82 Global coal production is expected to total 7.9 billion tonnes in 2012, providing for industry revenue of US\$1.4 trillion<sup>14</sup>. Approximately 87% by volume and 97% by value of coal output is black coal and the remainder the lower energy and value brown coal. Global trade in coal at US\$207.5 billion by value and 1.2 billion tonnes<sup>14</sup> by volume (2012 estimate) is modest in comparison to total production, reflecting the broad distribution of the resource and the use of coal mined in the country of origin. The global seaborne coal market is split essentially between the Atlantic market, representing imports by Europe and the Pacific market representing imports by Asia.
- 83 There are two primary types of black coal, metallurgical coal and thermal coal. Metallurgical coals are used in the production of iron and steel due to their particular characteristics, high carbon and lower moisture content. Prices for metallurgical coals are at a premium to thermal coals. Thermal coal is used in power generation to produce energy via steaming. Thermal coals generally have low coking properties making them unsuitable for steel making.
- 84 Coal is mined via surface / open-cut mining or underground mining, with the geology of the coal deposit (thickness of the overburden and depth and thickness of the coal seam) generally dictating the mining method. Open-cut mining can be conducted by excavator and truck, via a dragline or a combination of both. This mining method involves the sequential removal of overburden to reach the coal and recovers a higher proportion of the coal deposit (typically around 90%) than underground mining. It is usually economic when the coal seam is near the surface.
- 85 Underground mining is the predominant form of global coal production. However, approximately 80% of Australian coal is produced via open-cut mines, in part due to the geology of Queensland topography where the depth and thickness of coal has made it more economic to mine by open-cut. The primary forms of underground mining are longwall mining and bord-and-pillar mining. Longwall mining involves mining a long wall of coal in a single slice. It typically allows around 75% of coal to be extracted from panels of coal that can extend long distances through the coal seam. In comparison (once established) the bord-and-pillar method leaves up to 40% of the total coal in the seam, initially retained as pillars to

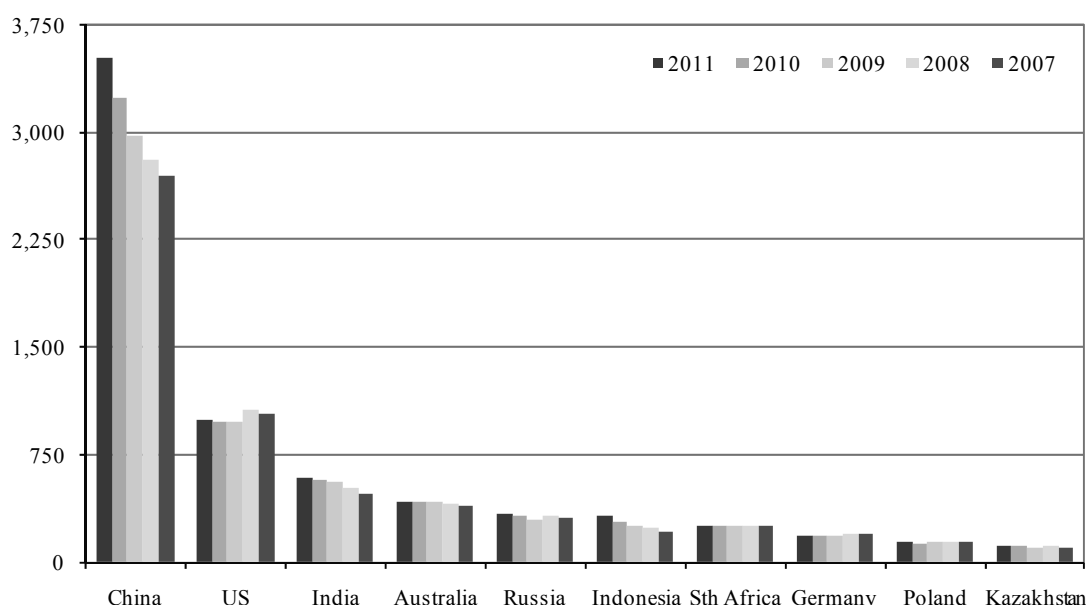
<sup>14</sup> Source: IBISWorld (June 2012) *Global Coal Mining*.

support the roof of the mine. These pillars are usually recovered using pillar extraction methods as part of this mining method.

- 86 Coal consumption in China represents around 46% of global coal output, with the four next largest consumers of coal (USA, India, Russia and Japan) accounting for a further 29% of global coal consumption. All of these countries boast large coal resources except Japan, which is reliant on imports. Total production by the top 10 coal producing countries is set out in the graph below, with Australia the fourth largest producer globally.

**World annual coal production**

**Mt**



Source: BP (June 2011) *Statistical Review of World Energy*.

- 87 Worldwide, the reserve-to-production ratio for coal is estimated to be 118 years (Australia's reserve to production ratio is 186 years)<sup>15</sup>. In comparison the reserve-to-production ratio for oil is 46 years and natural gas 63 years, making coal one of the most abundant carbon fuels<sup>15</sup>. In a number of countries coal production is also subsidised.

### Thermal coal

- 88 Thermal coal is the most common coal type and is used in the production of electricity by power stations. The coal is first crushed or pulverised, and then burnt in large boilers. These boilers create steam, which drives the turbines that create electricity. Thermal coal is also used as a fuel in the manufacture of cement, bricks and tiles and other energy intensive industries. As a result, thermal coal prices are generally traded by reference to energy content.
- 89 Coal currently accounts for about 26% of global energy requirements and generates some 41% of the world's electricity. Thermal coal's use in the production of electricity places it in direct competition to other sources of electricity production, including natural gas (20% of

<sup>15</sup> Source: World Coal Institute.

global electricity), hydro (16%), nuclear (15%), oil (6%) and minor sources such as solar, wind and geothermal (2%).

- 90 Thermal coal demand is linked to power generation, which fluctuates according to the economic state of global industrialised nations (particularly those in Asia in Australia's case) and the overall health of the global economy. Accordingly, the faster the growth in the global economy the higher the demand for thermal coal and vice versa. This situation is further exacerbated by the growth of electricity consumption in developing countries, which tends to outpace economic growth.
- 91 Demand for thermal coal accelerated following the energy crisis in the 1970s and led to an increased reliance on coal as opposed to oil for power generation and cement manufacturing. Historically, annual and longer term price negotiations have also served to provide a more stable pricing regime compared to other carbon energy sources. Despite the recent trend of rising coal prices, coal remains one of the lowest-cost sources of energy for electricity generation.
- 92 In recent years supply of thermal coal has been constrained in Australia and South Africa (the major exporting nations historically) while Russia, Colombia and particularly Indonesia have taken the opportunity to expand their export markets. Infrastructure problems have hindered Australia's coal export growth, however a number of new export port and transport initiatives have the potential to boost exports substantially.

| Thermal coal trade (source: ABARE / BREE) |      |      |      |      |      |       |       |
|-------------------------------------------|------|------|------|------|------|-------|-------|
|                                           | 2007 | 2008 | 2009 | 2010 | 2011 | 2012F | 2013F |
|                                           | Mt   | Mt   | Mt   | Mt   | Mt   | Mt    | Mt    |
| <b>Thermal coal exports</b>               |      |      |      |      |      |       |       |
| Indonesia                                 | 189  | 193  | 233  | 285  | 302  | 308   | 319   |
| Australia                                 | 112  | 126  | 139  | 141  | 148  | 164   | 192   |
| Russian Federation                        | 88   | 86   | 84   | 95   | 97   | 99    | 99    |
| Colombia                                  | 65   | 74   | 63   | 69   | 75   | 76    | 82    |
| South Africa                              | 65   | 61   | 67   | 68   | 66   | 69    | 72    |
| China                                     | 51   | 43   | 22   | 20   | 13   | 12    | 12    |
| Other                                     | 127  | 121  | 117  | 116  | 134  | 143   | 143   |
| Total                                     | 697  | 704  | 725  | 795  | 835  | 871   | 919   |
| <b>Thermal coal imports</b>               |      |      |      |      |      |       |       |
| European Union                            | 182  | 185  | 170  | 149  | 160  | 160   | 163   |
| China                                     | 41   | 35   | 92   | 129  | 139  | 145   | 151   |
| Japan                                     | 128  | 128  | 113  | 129  | 125  | 128   | 129   |
| Republic of Korea                         | 66   | 76   | 82   | 91   | 97   | 99    | 102   |
| India                                     | 31   | 34   | 49   | 60   | 78   | 89    | 104   |
| Taiwan                                    | 61   | 60   | 59   | 65   | 67   | 68    | 69    |
| Other                                     | 188  | 186  | 160  | 172  | 169  | 182   | 201   |
| Total                                     | 697  | 704  | 725  | 795  | 835  | 871   | 919   |

- 93 In 2009 China became a net importer of thermal coal (net imports increased some 78 Mt), and India's imports rose by 15 Mt. These increases offset the volume falls recorded in the other major coal importing countries as the global financial crisis (GFC) took hold, but were not enough to offset large falls in benchmark thermal coal prices. The fall in prices in 2009

should also be viewed in the context of the 2008 coal price, which reflected a rise unprecedented historically in terms of the size of the increase recorded.

- 94 In the first three months of 2010 Chinese thermal coal imports were a record 34 Mt, a level more than three times the corresponding period in 2009. This was due to high domestic Chinese coal prices as domestic demand from electricity generation outpaced available supply<sup>16</sup>. However, in the first quarter of 2011, low delivered domestic Chinese coal prices reduced Chinese coal imports by 35%. The price differential between domestic and international thermal coals subsequently narrowed and Chinese coal imports overall increased by approximately 8% in 2011. China has therefore become an arbitrage trader (albeit a very large one) importing thermal coal when international coal prices landed in China are below domestic Chinese thermal coal prices and relying more on domestic sourced coal when imports are unattractive<sup>17</sup>. The BREE is forecasting modest growth in Chinese coal imports in 2012 and 2013. At the same time the fastest growing coal import market India, increased imports by 30% in 2011, with expectations for continued import growth of 14% and 17% in 2012 and 2013 respectively, as new investment in India's coal fired electricity generation capacity is commissioned.
- 95 As is apparent from the above, China both exports and imports coal. This situation generally arises where domestic production, non-proximity to the end user, makes transport costs prohibitive. As noted above, thermal coal trade in China moved from a net export to net import position in 2009, notwithstanding an increase in Chinese coal production. This was the result of domestic supply being unable to meet demand (as some mines were closed for safety reasons), prices in the Chinese market being above those in international markets (particularly in the southern regions), weak demand in the Japanese market (China's largest coal export market) and lower international freight rates.

### **Metallurgical (or coking) coal**

- 96 The metallurgical coal market is segregated based on coking properties into hard-coking coal, semi-hard and semi-soft coking coals and pulverised coal injection (PCI) coal. Hard-coking coal commands the highest price owing to its high levels of coking properties. Semi-hard and semi-soft coking coals are lower in coking properties and thus attract a price discount. They are often blended with hard-coking coal in order to meet blast furnace specifications. Semi-soft coking coal can also be used in the PCI process.
- 97 Some 800 Mt of metallurgical coal is used by the steel industry annually, with 70% of steel production dependent on coal<sup>18</sup>. In comparison to thermal coal, a higher proportion of metallurgical coal is traded globally which is due to its relative scarcity versus thermal coals<sup>19</sup>. Metallurgical coal, or coking coal as it is often called, is a vital ingredient in the steel making process. As a consequence the health of the global steel industry sets the demand for metallurgical coals.

<sup>16</sup> In response to the prevailing market conditions new higher cost coal mines in China are being developed.

<sup>17</sup> R.K. Morse, G. He, "The World's Greatest Coal Arbitrage: China's Coal Import Behavior and Implications for the Global Coal Market".

<sup>18</sup> The remaining steel production is from recycled steel, which in many cases requires electricity generated from thermal coal. Source: Based on interpolated data from the World Coal Association.

<sup>19</sup> Approximately 25% of metallurgical coal is traded globally versus around 14% for thermal coals.

- 98 Metallurgical coal is much less common than thermal coal and therefore commands a price premium. Premium hard and other hard coking coals are the most scarce, which contributes to their price premiums over the other more available metallurgical coal types. While many countries hold significant deposits of thermal coal the same cannot be said about coking coal, where Australia (or more specifically Queensland) has a substantial market share due to its competitive deposits of high quality coal. Australia is by far the largest supplier of metallurgical coals with approximately 55% to 60% of the global market, as shown in the table below.

| <b>Metallurgical coal trade (source: ABARE / BREE)</b> |             |             |             |             |             |              |              |
|--------------------------------------------------------|-------------|-------------|-------------|-------------|-------------|--------------|--------------|
|                                                        | <b>2007</b> | <b>2008</b> | <b>2009</b> | <b>2010</b> | <b>2011</b> | <b>2012F</b> | <b>2013F</b> |
|                                                        | <b>Mt</b>   | <b>Mt</b>   | <b>Mt</b>   | <b>Mt</b>   | <b>Mt</b>   | <b>Mt</b>    | <b>Mt</b>    |
| <b>Metallurgical coal exports</b>                      |             |             |             |             |             |              |              |
| Australia                                              | 138         | 135         | 135         | 159         | 133         | 149          | 163          |
| United States                                          | 29          | 39          | 34          | 51          | 55          | 51           | 46           |
| Canada                                                 | 26          | 27          | 22          | 28          | 30          | 33           | 35           |
| Russian Federation                                     | 10          | 16          | 13          | 14          | 17          | 18           | 20           |
| Other                                                  | 24          | 16          | 6           | 21          | 36          | 35           | 32           |
| World                                                  | 227         | 233         | 210         | 273         | 271         | 286          | 296          |
| <b>Metallurgical coal imports</b>                      |             |             |             |             |             |              |              |
| Japan                                                  | 54          | 57          | 45          | 58          | 55          | 55           | 56           |
| European Union                                         | 56          | 56          | 41          | 45          | 46          | 46           | 46           |
| China                                                  | 6           | 7           | 34          | 48          | 46          | 53           | 56           |
| Republic of Korea                                      | 23          | 24          | 15          | 28          | 34          | 34           | 35           |
| India                                                  | 22          | 29          | 23          | 30          | 32          | 34           | 36           |
| Other                                                  | 66          | 60          | 52          | 64          | 58          | 64           | 67           |
| Total                                                  | 227         | 233         | 210         | 273         | 271         | 286          | 296          |

- 99 In 2009 steel production in Japan, Korea and Europe declined due to struggling domestic economies in the wake of the GFC, with a consequent impact on the level of metallurgical coal imports. However, China steel production increased with an associated increase in demand for metallurgical coals. In part, this was attributable to a government stimulus programme aimed largely at infrastructure, which raised demand for metallurgical coals at a time when domestic supply failed to keep up. Prior to 2009, China was largely self-sufficient in metallurgical coals and imported only modest tonnages. Subdued domestic coal production, increasing production costs and lower international freight rates, as well as arbitrage opportunities similar to those for thermal coal have since increased demand for imported metallurgical coals into China.
- 100 Similar to the situation with thermal coal, high international prices for metallurgical coals in the first quarter of 2011 increased the competitiveness of China's domestic coals and encouraged the drawdown of Chinese coal stocks. This reduced imports by 24% compared to the previous quarterly period in 2010, however on an annual basis Chinese imports only reduced by 4% for 2011. BREE is forecasting minimal growth from the traditional markets of Japan and the European Union, with the Chinese and Indian economies expected to account for the majority of forecast growth in metallurgical coal trade in 2012 and 2013 (notwithstanding the recent weakness of demand in the Chinese steel industry).

## Australian coal industry

- 101 Australia is the fourth largest coal producer globally and holds the fifth largest recoverable reserves of coal. However, due to its relatively small domestic needs, Australia is the world's largest coal exporter. The industry is also one of Australia's largest export sectors, worth almost A\$44 billion in FY11 with BREE forecasting export earnings of A\$47.7 billion in FY12, as shown below.

| Australian coal statistics (source: ABARE / BREE) |                |                |                |                |                |                  |
|---------------------------------------------------|----------------|----------------|----------------|----------------|----------------|------------------|
|                                                   | Actual<br>FY07 | Actual<br>FY08 | Actual<br>FY09 | Actual<br>FY10 | Actual<br>FY11 | Forecast<br>FY12 |
| <b>Australian production</b>                      |                |                |                |                |                |                  |
| Metallurgical coal (Mt)                           | 132            | 137            | 125            | 157            | 140            | 142              |
| Thermal coal (Mt)                                 | 112            | 115            | 136            | 135            | 143            | 159              |
| Total exported (Mt)                               | 244            | 252            | 261            | 292            | 283            | 301              |
| Total domestic (Mt)                               | 82             | 75             | 78             | 71             | 62             | 64               |
| Total (Mt)                                        | 326            | 327            | 339            | 363            | 345            | 365              |
| <b>Value of exports</b>                           |                |                |                |                |                |                  |
| Metallurgical coal (A\$bn)                        | 15.0           | 16.0           | 36.8           | 24.5           | 30.0           | 30.3             |
| Thermal coal (A\$bn)                              | 6.8            | 8.4            | 17.9           | 11.9           | 13.9           | 17.4             |
| Total                                             | 21.8           | 24.4           | 54.7           | 36.4           | 43.9           | 47.7             |
| <b>Coal exports - implied price per tonne</b>     |                |                |                |                |                |                  |
| Metallurgical coal (A\$/t)                        | 114            | 117            | 295            | 156            | 214            | 213              |
| Thermal coal (A\$/t)                              | 61             | 73             | 131            | 88             | 98             | 109              |

- 102 Australian coal exports in the March 2011 quarter were hampered by heavy rains in Queensland, which flooded a significant number of mining pits and closed rail corridors. This flooding was the primary reason that metallurgical coal exports reduced 32% in the March 2011 quarter (compared to the previous quarter), with as much as 37 Mt of coal (coking and thermal coals) due for delivery in FY11 lost<sup>20</sup>. Due to continued excess water remaining in the mining pits and the inability of miners to release this water due to environmental regulations, mining in Queensland is likely to be impacted for some time yet. As such Queensland's coal industry is still operating below full capacity.
- 103 Australian coals are high in energy content and tend to be relatively low in impurities such as sulphur. The consistent quality, volume, diversity of suppliers and security of supply add to demand for Australian sourced coals and provides impetus for investment in Australian coal projects. Notwithstanding this, coal price volatility is prevalent for all coals, including Australian coals.

## Australian coal infrastructure

- 104 Seaborne coal trade has been negatively impacted by inadequate infrastructure in Australia and South Africa. Indonesia in particular has capitalised on this situation by expanding coal exports three-fold over the past 10 years. However, future growth of Indonesia's coal industry may be capped by (market driven) requirements to divert exports to Indonesian industries and domestic power stations. Furthermore, Indonesian coals generally have lower energy content than Australian coals, translating to lower prices.

<sup>20</sup> Source: QR National Limited.

- 105 Australian infrastructure bottlenecks such as inadequate port and rail capacity and shortages of rolling stock (trains and coal wagons) have hindered the growth of Australian exports. This situation is expected to progressively improve going forward as major initiatives at key ports as well as additional rail capacity and rolling stock add significant capacity to Australia's coal infrastructure. Current and planned theoretical capacity output at Australian coal ports is set out below.

| Australian port capacity – actual and forecast |                 |              |                             |              |                     |
|------------------------------------------------|-----------------|--------------|-----------------------------|--------------|---------------------|
| State / port                                   | Export loadings |              | Theoretical annual capacity |              |                     |
|                                                | 2010            | 2011         | 2010 (A)                    | 2012 (F)     | 2015 (F)            |
|                                                | Mt              | Mt           | Mt                          | Mt           | Mt                  |
| Abbot Point                                    | 17.4            | 13.7         | 50.0                        | 50.0         | 80.0 <sup>(1)</sup> |
| Brisbane                                       | 7.4             | 6.8          | 10.0                        | 10.0         | 10.0                |
| Dalrymple Bay (DBCT)                           | 62.7            | 49.3         | 85.0                        | 85.0         | 85.0                |
| Gladstone <sup>(2)</sup>                       | 60.3            | 52.6         | 76.0                        | 76.0         | 103.0               |
| Hay Point                                      | 36.5            | 30.8         | 44.0                        | 44.0         | 55.0                |
| <b>Total Queensland</b>                        | <b>184.3</b>    | <b>153.2</b> | <b>265.0</b>                | <b>265.0</b> | <b>333.0</b>        |
| Newcastle (PWCS) <sup>(2)</sup>                | 95.7            | 98.1         | 113.0                       | 133.0        | 145.0               |
| Newcastle (NCIG)                               | fno             | fno          | fno                         | 30.0         | 66.0                |
| Port Kembla                                    | 13.4            | 13.9         | 18.0                        | 21.0         | 28.0                |
| <b>Total NSW</b>                               | <b>109.1</b>    | <b>112.0</b> | <b>131.0</b>                | <b>184.0</b> | <b>239.0</b>        |
| <b>Total Australia</b>                         | <b>293.4</b>    | <b>265.2</b> | <b>396.0</b>                | <b>449.0</b> | <b>572.0</b>        |

**Note:**

- 1 Assuming one 30 Mtpa terminal is built by 2015, noting port expansion targets in excess of this.  
 2 Ports with two coal loading terminals.  
 fno – facility not operational.

- 106 In total, planned theoretical coal port capacity in Australia is forecast to reach 572 Mtpa by 2015. In addition, further capacity is in the planning and development stages in Queensland from a combination of proposed expansions at Gladstone and Abbot Point and a development at Dudgeon Port<sup>21</sup>, while in NSW an expansion at PWCS is also envisaged<sup>22</sup>. Given the high capital costs of these port developments and the likelihood that the projects will be seeking funding at, or around the same time, the probability of all these developments taking place concurrently is low. Further, it is highly probable that actual coal exports will be lower than the theoretical capacity due to available infrastructure capacity / usage being lower than nameplate capacity. For example, despite recent port expansions and related rail corridor improvements at PWCS and DBCT, the actual port and rail deliveries in these coal chains have not yet achieved theoretical expanded capacity. In addition, a lack of coal production close to Abbot Point has meant that historically some of its port capacity has gone unused. However, with the recent commissioning of the Northern Missing Link this situation is likely to change<sup>23</sup>.

<sup>21</sup> A site located 15km south of Hay Point coal terminal.

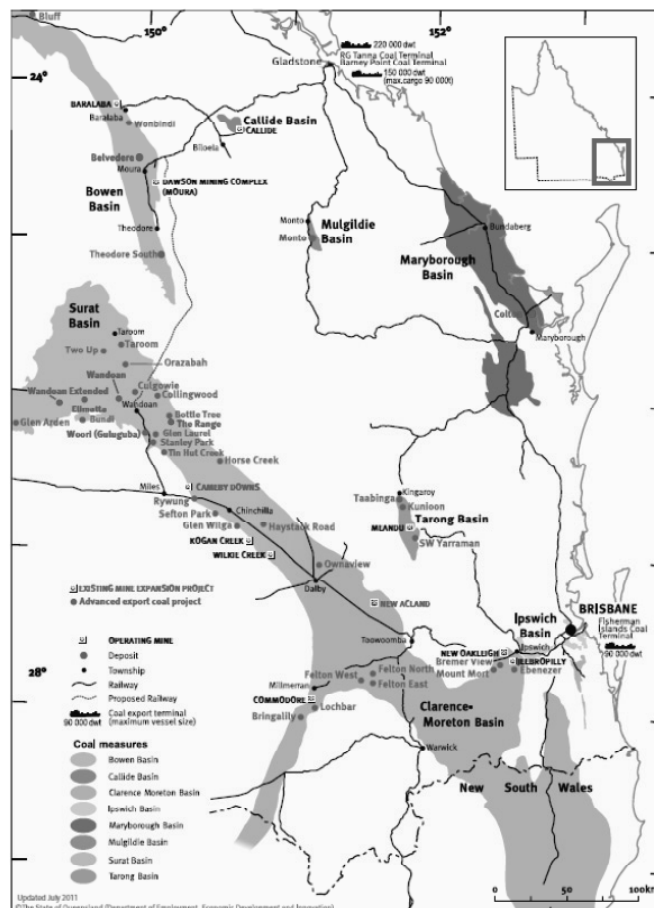
<sup>22</sup> Given the recent fall in coal prices, the anticipated timing and size of these expansions is under review.

<sup>23</sup> Due to the commissioning of the Northern Missing Link railway, coal can now be moved from the Goonyella rail system to Abbot Point and hence the surplus capacity at Abbot Point is expected to reduce.

## Queensland port and rail infrastructure

- 107 Queensland currently has around 55 coal mines located principally in the Bowen Basin. The coal is exported via five rail systems which each link to port terminals. A map of south-east Queensland (where Stanmore Coal's The Range project is located) is shown below.

### Queensland coal infrastructure – south-east Queensland



Source: Queensland Government.

- 108 Mines located in the north of the Bowen Basin are linked to the Abbot Point (Newlands system) and Dalrymple Bay and Hay Point ports (Goonyella system). The mines in the southern Bowen Basin can either export from the Dalrymple Bay and Hay Point ports via the Goonyella system, or otherwise the Barney Point and RG Tanna ports via the Blackwater system. The Moura system and Western (Brisbane) systems also service mines located to the south of the Bowen Basin.
- 109 The Northern Missing Link was completed in December 2011, with first coal railed in January 2012. The Northern Missing Link joined the Goonyella and Newlands rail systems and has the potential to significantly expand coal exports through Abbot Point (where surplus coal export port capacity is currently available and significant additional capacity is envisaged).
- 110 Notwithstanding that wet weather and flooding significantly lowered coal production in Queensland during 2011, theoretical or nameplate capacity of the Queensland ports is

substantially higher than actual coal exports. This is primarily the result of a lack of investment in the rail network capacity and specifically a lack of rolling stock capacity. In response to these constraints the Queensland Coal Rail Infrastructure Master Plan (Master Plan) has been progressively rolled out since 2006. The Master Plan has developed expansion paths for each rail system, based on specific rail infrastructure expansion projects needed to meet future demand predictions. Expansion plans include a combination of:

- (a) the construction of additional lines, including
  - (i) the Northern Missing Link (now completed)
  - (ii) the SBR that will link to the Moura rail system and the Surat Basin
- (b) additional trains and rolling stock, including increased operational performance from longer trains, heavier payloads and improved maintenance practices
- (c) new spur lines to service new mines; and
- (d) train line duplications and extra passing loops.

#### **Wiggins Island Coal Export Terminal**

- 111 The Queensland Government has granted WICET the mandate to own and develop the terminal located at Golding Point, Gladstone, to the west of the existing RG Tanna and Barney Point terminals. The A\$5 billion industry-funded terminal is expected to provide up to 84 Mtpa in additional export coal capacity through the Port of Gladstone after completion of a three stage construction process. The Stage 1 WICET consortium includes eight owners (existing and potential coal exporters located in Queensland), with the objective of providing increased long-term export coal capacity to the industry<sup>24</sup>. Upon completion of Stage 1 of WICET (expected in late 2014) the Barney Point terminal with current export capacity of 7 Mtpa is planned to be phased out as an export coal terminal.
- 112 WICET Stage 1 is expected to deliver up to 30 Mtpa export capacity at an estimated cost of A\$2.5 billion. Stage 1 port allocations were made to Bowen Basin coal developers / producers. Following agreements from the eight coal companies involved for capacity totalling 27 Mtpa, financial close took place in September 2011 which enabled construction to commence. WICET is planning to operate on a cost plus pass through basis to recover both operating and financial costs incurred. Access to the terminal is to be based on long-term take-or-pay contracts (supported by bank guarantees).
- 113 Plans for the expansion of WICET (initially WEXP1) are currently underway. WEXP1 is scheduled to provide additional capacity of around 32 Mtpa. This capacity has been allocated to four coal development projects, three of which are located in the Surat Basin including The Range project owned by Stanmore Coal. Each of the companies involved has signed a CCD for its proportionate share of the costs to fund the early works of WEXP1 ahead of financial close. The CCDs also oblige the respective parties to (subsequently) execute WEXP1 take-or-pay agreements (supported by a bond / guarantee).

<sup>24</sup> The WICET Stage 1 consortium includes Aquila Resources Ltd, Bandanna Energy Ltd, Caledon Coal Pty Ltd, Cockatoo Coal Limited (Cockatoo Coal), Northern Energy Corporation Ltd, Wesfarmers Curragh Pty Ltd, Yancoal and Xstrata Coal Queensland Pty Ltd (Xstrata Coal).

- 114 WEXP1 construction timing is being managed to coincide with the development of the SBR. Given the integrated nature not only of WEXP1 and the SBR, but also the underlying coal projects on which use of the infrastructure is dependent, a significant level of overall funding is required. This will likely involve capital markets in both Australia and overseas, the status of which will therefore be a key determinant in funding availability and hence timing. Based on prevailing market conditions financial close is unlikely prior to late 2013, with completion of the facilities in late 2016 following a three year construction phase.

### **Surat Basin Rail**

- 115 The SBR involves the construction and operation of a 214 km rail line connecting the Western rail system (near Wandoan) to the Moura rail system (near Banana). The Surat Basin Rail Joint Venture (SBRJV) is an unincorporated joint venture between the Australian Transport and Energy Corridor, a subsidiary of QR National and Xstrata Coal, formed to develop the rail infrastructure. As noted above, development of the SBR is being programmed to coincide with completion of WEXP1.
- 116 Current plans are to build a multi-user, open access single line track (with seven passing loops) to facilitate the export of coal from the Port of Gladstone. Under the first stage of development the line will be capable of moving approximately 32 Mtpa of coal, using trains of up to 2.5 km in length. Further upgrades and expansions are envisaged that will progressively increase rail capacity.
- 117 The project has currently received indicative annual tonnage requirements from the three companies owning the Surat Basin coal projects that have received the WEXP1 port allocations, the largest of these being Xstrata Coal in connection with its Wandoan project (which has initial plans for a 22 Mtpa mine). During 2012 development of the Wandoan mine gained traction, with the Queensland Land Court endorsing the project in March 2012 and environmental approval granted in August 2012. CCDs in respect of the SBR (containing similar obligations for the coal companies to the corresponding WEXP1 deeds) are expected to be entered into shortly. The estimated construction costs of the SBR are in excess of A\$1 billion.

### **Moura system upgrade**

- 118 Moura system capacity is currently 17 Mtpa and requires a significant upgrade in order to meet increased future tonnage, primarily from the SBR. Planning for the upgrade of the Banana to Wooderson track is well progressed with a study completed during 2010. The study identified and costed the individual projects (including track duplication, passing loops and improved logistical support) required to provide up to 71 Mtpa of additional capacity across this line. These upgrades will be required in order to meet capacity for the proposed SBR tonnage, in addition to extra demand from the Moura region itself.
- 119 In addition to Stanmore Coal a number of participants with interests in the region have lodged support for the Moura system upgrade including Xstrata Coal, Vale, Cockatoo Coal, Northern Energy<sup>25</sup> and Syntech Resources Pty Ltd. Feasibility studies on the Moura system commenced in early 2011, with the additional rail capacity scheduled to be completed in line with WEXP1 and the SBR.

<sup>25</sup> Now a subsidiary of New Hope Corporation Ltd.

### Australian operating costs and royalties

- 120 Coal royalties represent a significant cost to Australian coal miners. The Queensland and NSW Governments have taken advantage of stronger coal prices to increase royalties (primarily to address respective state budgeting issues). According to the Queensland 2012-13 State Budget, recently revised Queensland royalty rates are 7% up to a sales value of A\$100 per tonne, 12.5% on revenue above A\$100 per tonne and 15% on revenue above A\$150 per tonne. While mining companies have been promised no further increases for 10 years, this is the second increase in Queensland coal royalties in four years.
- 121 Royalties in NSW are 6.2% (deep underground), 7.2% (underground) and 8.2% (open cut) of coal sales values. In its 2011 budget announcement, the NSW Government indicated that it was looking to cover the cost imposed on it by the Federal Government's carbon tax by raising coal mining royalty rates. While the proposed new royalty rates have not been released, and consultation with the industry is currently taking place, the government has announced it was seeking to raise A\$950 million over four years.
- 122 Coal miners are increasingly in competition with other Australian mining sectors for skilled mining labour. As a result and partially due to a national skills shortage, mine wage inflation has been high. Costs for equipment have also increased as shortages and long lead times result in higher total costs. Australian coal production costs have also been impacted by high demurrage costs, caused by shipping vessels queued at Australian coal ports due to congestion in recent years. In combination, these factors have contributed to a significant increase in the cost of producing coal over the past five years, with the marginal cost of production (impacting on mine profitability) now significantly above historical levels.

### Coal prices

- 123 NSW and Queensland set world benchmarks for their respective coal types, with coal mined in NSW primarily being thermal coal and in Queensland primarily metallurgical coal. Benchmark prices which were typically negotiated annually between Japanese customers and major Australian producers (Japanese benchmark prices) represent the highest class of coal. While benchmark pricing has been the predominant form historically, there have been some recent moves towards contracts related to spot coal markets. In addition, metallurgical coal prices are now primarily based on quarterly based contracts, having regard to spot prices.
- 124 The hard coking coal benchmark price is generally set by Australian suppliers and most often by the largest supplier of hard coking coal, the BHP Billiton / Mitsubishi Development Alliance (BMA Alliance). Most other hard coking coals are then sold at a minor discount to this benchmark price, depending on quality relativities to the benchmark coal. Semi-hard, semi-soft and PCI coal prices are also negotiated at a discount to the hard coking coal price depending on market dynamics at the time. Rio Tinto and Xstrata Coal, the significant exporters of Australian thermal coals, tend to lead negotiations on behalf of Australian thermal coal producers.
- 125 In a bid to add flexibility to the coal contract process, quarterly based contracts indexed to spot prices were introduced by BHP Billiton for its metallurgical coal contracts beginning 1 April 2010, and replaced annual contracts from this date. This move was quickly embraced

by other Australian metallurgical coal producers and quarterly contracts are now the primary contract form for metallurgical coals<sup>26</sup>.

### Historical coal prices

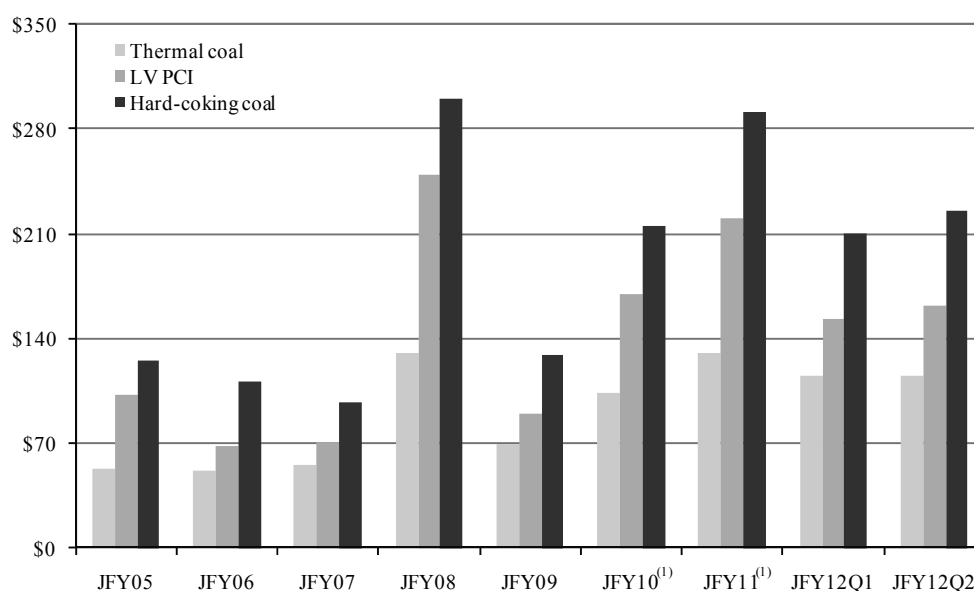
126 As discussed above, demand for coal is primarily influenced by the power generation and steel industries. Whilst power generation is more stable than steel production, both industries are reflective of the general health of the global economy. Supply is dependent on mine production and adequate coal infrastructure (rail, port etc.). In recent times supply has been constrained due to both a lack of infrastructure and a lack of historical investment. In addition, a number of other factors also impact coal prices, such as:

- (a) the quality of the coal (and energy content of thermal coal), which may result in the price received being a premium or discount to benchmark prices
- (b) the availability and price of alternative fuels and energy sources (thermal coal)
- (c) adverse weather and natural disasters
- (d) the proximity, capacity and cost of transportation
- (e) domestic and foreign government regulations and taxes, including those establishing air emission standards for coal-fuelled power plants.

127 Metallurgical coals have recently moved to a quarterly pricing system, while thermal coals are still based on annual negotiations. Japanese benchmark coal prices that have resulted from the price negotiations are set out below:

#### Coal prices<sup>(1)</sup>

Japanese fiscal year (US\$/t)



**Note:**

1 Represents the average quarterly prices for hard coking and PCI coals for JFY10 and JFY11.

<sup>26</sup> In late August 2011 however, BHP Billiton indicated that it had progressed around 50% of its coking coal sales from quarterly to monthly pricing, with work continuing on a derivative (futures) pricing market.

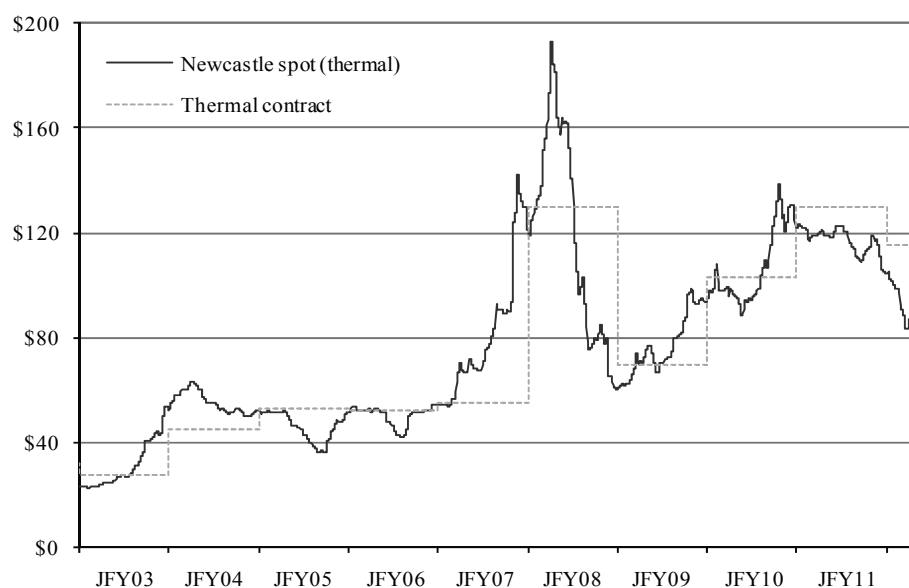
- 128 The most notable developments in recent years were the pricing outcomes for the Japanese fiscal years JFY05 (to 31 March 2006), JFY08, JFY09, JFY10 and JFY11. In JFY05, a strong global economy and increased Asian imports combined with limited supply, raised prices significantly above the previous year. In subsequent years the volatility in coal prices rose markedly.
- 129 During JFY08 strong demand and supply side constraints such as those listed below provided the impetus for the most substantial and unprecedented coal price rise in history. Supply constraints included:
- (a) severe blizzards in China forcing China to suspend all coal exports in order to guarantee local supply
  - (b) electricity black-outs in South Africa that took mining equipment offline, hence impacting production. The Government power monopoly also re-directed coal destined for export to domestic use
  - (c) floods in Australia (Northern Queensland), the largest export coking coal source in the world.
- 130 The GFC and the reduction in coal demand that followed resulted in a large fall in Japanese benchmark prices for JFY09, as was the case for most commodities. However, as the year progressed coal imports into China increased significantly whilst its coal exports reduced. Chinese total coal imports were 84 Mt higher than in 2008, with thermal and metallurgical coal imports increasing 57 Mt and 27 Mt respectively. As demand from developing economies began to return, demand for seaborne coal once again outpaced supply and resulted in significantly higher JFY10 coal prices.
- 131 Coal prices, particularly metallurgical, spiked in 2011 due to severe flooding in Queensland. Prices have since reduced with the latest hard coking coal quarterly price (September 2012) negotiated at US\$225 per tonne. Notwithstanding the reduction, this price was partially supported by industrial action at BMA Alliance coking coal mines in Queensland, which limited production from these mines. More recently, over production of steel in China in a period of weak demand has impacted the spot price of hard coking coal (and also iron ore), with prices dropping to around US\$150 per tonne, just above current production costs. Implications for the next round of quarterly hard coking coal negotiations (and other metallurgical coals) are therefore for a significant reduction in prices, with a price of US\$170 per tonne mentioned in press reports.
- 132 The thermal coal contract price for JFY12 (commencing 1 April 2012) settled at US\$115 per tonne. However, as the year has progressed spot prices for benchmark thermal coals<sup>27</sup> have gradually reduced and are currently trading at a significant discount to the annual benchmark price (at around US\$90 per tonne). The reason for such weakness is due to a mild northern hemisphere winter, with thermal coal burn rates low and mining allowed to continue longer than normal, combined with an oversupply of coal in the US, where significant increases in shale gas production have reduced gas prices considerably and encouraged substitution of gas over coal for power supply. A proportion of US excess coal supply has been redirected towards the European coal market and in the process put downward pressure on coal prices

<sup>27</sup> Newcastle benchmark, 6,700 Kcal gross air dried (GAD) FOB thermal coal.

internationally. Columbian coal producers, who primarily export to Europe (Atlantic coal market), are consequently facing increasing competition from US producers. Columbian producers are low cost, and due to prevailing low shipping rates are now targeting sales to the Pacific (Asian) coal market. The situation has been magnified by recent slower growth in China's economy, which has lead to increased coal stockpiles and a reduction in imports.

- 133 Spot thermal coal prices, as compared to historical JFY contract prices are shown below.

**Thermal coal prices – contract and spot (US\$/t)**  
**Japanese fiscal year (JFY)**



Source: ABARE, Bloomberg.

### Coal price outlook

- 134 China now accounts for almost half the global demand for coal and hence changes to Chinese coal supply and demand can have a profound effect on world coal prices. Furthermore, Chinese coal traders are likely to engage in arbitrage opportunities when international coal prices are below domestic Chinese coal production costs. Hence China's production and consumption levels, as well as its future coal production costs (including transport costs) are important considerations for future coal prices. Whilst China remains the single most important market for coal, demand for coal from India and other Asian markets is expected to grow progressively stronger over the medium to longer term.
- 135 In 2011 global steel production increased 5.6% to 1.5 billion tonnes<sup>28</sup> (with 74% of this growth attributable to China) following growth of 15% in 2010. The high rate of growth in 2010 was due to the rebound in industrial demand in developed nations as government stimulus programmes impacted positively on economies and consumer demand increased off previously low levels. Steel production levels in China are currently declining, however the relative scarcity of metallurgical coals as well as infrastructure constraints are likely to provide impetus for price recovery in the medium term.

<sup>28</sup> World Steel Association.

- 136 While coal is under pressure in the short-term, the longer term growth prospects for both metallurgical coal and thermal coal are likely to remain strong. The International Energy Agency (IEA) forecasts that coal demand will grow 40% over the next 20 years, while in the short to medium term demand is also likely to remain strong on the back of Asian demand, in particular from China and India. In addition, on-going mine development will be required to replace existing production capacity as resources are depleted at existing mines. Furthermore, many of the large global coal exporters (including Indonesia, China and Russia) are diverting increasing proportions of production to domestic uses.

## **Regulation and taxes**

- 137 The resource industry and in particular the coal industry in Australia is facing ever increasing regulation for environmental management. By way of example carbon emissions, mineral taxes and restricting mining on strategic cropping land are all issues that have recently been publicly debated. The lead time from securing mine leases to commencement of production is now in excess of five years, with the environmental permit process becoming more complex due to an increase in requirements to evaluate and mitigate both social and environmental impact. For example, the introduction of stricter water management requirements for mine sites in Queensland has not only increased capital expenditures, but also increased the risk associated with maintaining a licence to operate.

## **Carbon pricing and environmental issues**

- 138 Coal mining releases methane, one of the major greenhouse gases. Some methane gas emitted from mines is converted to electricity and used to power mines or on-sold to electricity grids. Coal power stations also emit high levels of greenhouse gases like carbon dioxide, nitrogen dioxide and sulphur dioxide. While there are technologies being advanced that have the potential to lower emissions from coal power stations, such as carbon capture technologies that store the carbon underground rather than releasing it into the atmosphere, these technologies have not been widely used to date generally due to cost.
- 139 The Federal Government previously sought to implement a carbon reduction system consistent with the accords of the Kyoto Protocol. In December 2009 the Government released its Carbon Pollution Reduction Scheme (CPRS) White Paper in which it set out the design of the CPRS that it intended would take effect from 1 July 2010. The CPRS White Paper confirmed the Government's commitment to the long-term goal of reducing Australia's greenhouse gas emissions by 60% of 2000 levels by 2050. The medium term targets were a reduction in greenhouse gas emissions by 2020 of between 5% and 15% of the 2000 level.
- 140 The White Paper allocated A\$2.15 billion over five years to the Climate Change Action Fund (CCAF) to assist businesses to adjust to the CPRS. The CCAF had four streams, one of which was assistance for coal mining involving the promotion of emissions abatement and specific transitional assistance. Adjustment assistance of up to A\$250 million over five years was proposed to be provided to affected coal mining operators to promote emissions abatement. A further A\$500 million over five years was allocated as direct assistance to gassy coal mines to assist them adjust while they explored abatement opportunities.
- 141 In April 2010 the Government announced it would delay the implementation of the CPRS until after 2013 when the current Kyoto Protocol commitment period ends. By this time it was expected that there would be greater clarity on the actions of other major economies including the US, China and India.

- 142 On 31 May 2011 an update of the Garnaut Climate Change Review was released. This review was followed on 10 July 2011 by the release of the Federal Government's Clean Energy Future Agreement and on 28 July 2011 by the Clean Energy draft legislation. These policies outlined a two stage carbon pricing policy mechanism comprising a fixed price carbon period effective 1 July 2012, with a transition to an emissions trading scheme from 1 July 2015. The draft legislation was subsequently approved by the Federal Parliament on 12 October 2011 and was effective from 1 July 2012.
- 143 In the first stage the proposed fixed price is A\$23 per tonne of emitted CO<sub>2</sub>, rising by 2.5% in real terms for each of the years ending 30 June 2014 and 2015. In the second stage the carbon pricing mechanism will move to a flexible, market-driven approach where a "cap and trade" system<sup>29</sup> will be adopted. For the first three years of the flexible pricing stage there will be a ceiling price of A\$20 above the "expected international price"<sup>30</sup> (rising by 5% per annum in real terms). The previous carbon permit floor price of A\$15 was removed on 28 August 2012.
- 144 The point of obligation is a threshold of "covered" emissions (being emissions in respect of which carbon permits must be surrendered) greater than 25 kilo-tonnes of CO<sub>2</sub> from a single facility. The covered emissions produced by a facility (that is, the mine site) will primarily be fugitive emissions being mainly methane gas from open cut or underground coal mines. Other covered emissions relate to those from landfill mine site facilities and those associated with waste water treatment. The carbon tax legislation does not tax combustion of liquid petroleum fuel, or other transportation fuels that have previously been subject to a duty or excise<sup>31</sup>, but emissions arising from these sources will be taxed via adjustments to the relevant duty or excise.
- 145 The carbon pricing scheme includes structural adjustment assistance to the mining industry as follows:
- (a) **Coal Sector Jobs Package** – to provide A\$1.3 billion over six years to gassy coal mines (that is, mines with fugitive emissions that account for more than 0.1 tonnes of CO<sub>2</sub> per tonne of saleable coal). The Government will cover 80% of fugitive emissions from these mines above the threshold
  - (b) **Coal Mining Abatement Technology Support Package** – to provide A\$70 million of grants over six years to assist mines implementing abatement technology (on a co-contribution basis).

<sup>29</sup> The Government will set annual caps on the number of carbon permits to be issued and the price of those permits will be determined by the market forces of supply and demand. Liable entities will be provided with the scheme cap five years beforehand on a rolling basis.

<sup>30</sup> We understand this refers to the price of certified emissions units under the Kyoto Protocol Clean Development Mechanism. The starting price will be set by 31 May 2014.

<sup>31</sup> Emissions exclude use of diesel for on-site electricity generation, off road transport, explosives and LPG or CNG as a fuel source for generation.

## Minerals Resource Rent Tax

- 146 The Mineral Resource Rent Tax (MRRT) was proposed by the Australian Federal Government on 2 July 2010, after the Resource Super Profits Tax (RSPT) failed to gain widespread support. The Federal Government established a Policy Transition Group (PTG) that provided a report on the detailed technical design of the new resource tax arrangements in December 2010. On 24 March 2011 the Federal Government accepted all recommendations of the PTG, which formed the basis of the design of the MRRT draft legislation that was released for consultation on 10 June 2011.
- 147 After a consultation process involving the Resource Tax Implementation Group, which comprised representatives of industry, the tax profession and government officials, a second exposure draft was released on 18 September 2011. On 2 November 2011, the MRRT bills and associated Explanatory Memorandum were introduced into Parliament in a form largely consistent with the second exposure draft. On 19 March 2012, the legislation for the MRRT passed through the Senate, taking effect from 1 July 2012.
- 148 The MRRT targets only coal and iron ore projects, as opposed to all mining resources as was proposed for the RSPT. The MRRT purports to tax the resource as close as practically possible to the point of extraction (i.e. at the “mine gate”) to ensure only the value of the resources extracted is taxed (less all “mining expenditure”<sup>32</sup> to that point). Conceptually, any value added processing or coal and iron ore mining unrelated activities (such as downstream processing or infrastructure) are not taxed under the MRRT.
- 149 The tax will commence with a headline rate of 30%. However, an extraction allowance of 25% is applied to acknowledge the mining expertise and know-how required to extract the resource, which effectively reduces the MRRT rate to 22.5%.
- 150 The other key features of the MRRT are as follows:
- (a) with the policy intent of recognising investments made prior to the announcement of the MRRT, existing investments receive a “starting base” of either:
    - (i) the market value of the existing investment as at 1 May 2010 (including the value of the mining rights) plus any capital expenditure incurred from 2 May 2010 to 30 June 2012. This starting base is depreciated over the remaining effective life of the asset (up to a maximum period of 25 years). Unused deductions are uplifted at CPI
    - (ii) the written down book value of the project assets as at the latest reported date prior to 1 May 2010 (excluding the value of the mining rights), plus any capital expenditure incurred from 2 May 2010 to 30 June 2012. This starting base is uplifted at the Government Bond rate plus 7% to 1 July 2012 and is depreciated over a period of five years using an accelerated declining balance depreciation method<sup>33</sup>

<sup>32</sup> Being expenditure on moving the resources to the run-of-mine stockpile, expenditure on managing and maintaining the stockpile and preliminary crushing for the purpose of moving the resource to the stockpile.

<sup>33</sup> The write off rates are 36%, 37.5%, 37.5%, 60% and 100% over the respective five years. Furthermore, unused deductions from this method can be uplifted at the Government Bond rate plus 7%.

- (b) a “royalty allowance” which effectively provides credits for State royalty payments which can only be used to reduce taxable MRRT profit. Accordingly, if no MRRT liability is incurred in the year the royalty is paid and the credit for State royalty payments cannot be used in that year
- (c) unused mining losses<sup>34</sup> and/or unused credits for State royalty payments are uplifted at the Government Bond rate plus 7% for use in future periods
- (d) new capital expenditure occurring after 1 July 2012 is deductible in full in the year incurred (as opposed to being depreciated)
- (e) a low profit offset is available for producers with group mining profits of less than A\$75 million per annum, which is phased out for profits between A\$75 million and A\$125 million (that is, no offset is available for producers with mining profits greater than A\$125 million)
- (f) the MRRT will allow transferability of mining losses between Australian iron ore and Australian coal projects (i.e. but not across other commodities) within a wholly owned group to the extent that the other project has sufficient mining profits to absorb the remaining mining losses once it has applied its own royalty, mining loss and starting base allowances. Unused royalty allowances are transferable if the interests are integrated and unused starting base allowances are not transferable.

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<sup>34</sup> The exception is the portion of the loss attributable to unused starting base allowance.

## V Valuation methodology

- 151 ASIC Regulatory Guide 111 – *Content of expert reports* (RG 111) outlines the appropriate methodologies that a valuer should consider when valuing assets or securities for the purposes of, amongst other things, share buy-backs, selective capital reductions, schemes of arrangement, takeovers and prospectuses. These include:
- (a) the discounted cash flow (DCF) methodology
  - (b) the application of earnings multiples appropriate to the businesses or industries in which the company or its profit centres are engaged, to the estimated future maintainable earnings or cash flows of the company, added to the estimated realisable value of any surplus assets
  - (c) the amount that would be available for distribution to shareholders in an orderly realisation of assets
  - (d) the quoted price of listed securities, when there is a liquid and active market and allowing for the fact that the quoted market price may not reflect their value on a 100% controlling interest basis
  - (e) any recent genuine offers received by the target for any business units or assets as a basis for valuation of those business units or assets.

### Methodologies selected

- 152 The market value of Stanmore Coal shares has been assessed by aggregating the market value of the mine exploration and development projects, together with the realisable value of any surplus assets and deducting net borrowings.

### The Range

- 153 Given the finite life of mining operations and the expectation of increasing coal production over time we have selected the DCF methodology as the primary methodology when valuing the interest of Stanmore Coal in The Range project.
- 154 Under the DCF methodology the value of the mining operations is equal to the net present value (NPV) of the estimated future free cash flows (after tax) including, where applicable, a terminal value at the end of the forecast period. In order to arrive at the NPV the future cash flows and terminal value are discounted using a discount rate which reflects the risks associated with the cash flow stream.
- 155 While we consider the DCF methodology to be the most appropriate valuation methodology to adopt in respect of The Range project, it is important to cross-check the valuation against other valuation methodologies used in both the mining industry and equity markets to assess the price that might be paid for a 100% interest in The Range project. Accordingly, we have also considered the value of The Range project by reference to the value per tonne of marketable reserves and resources implied by the listed coal company values and transactions in the Australian coal industry.

**Other projects**

- 156 The other projects held by Stanmore Coal are in the exploration or early development stage. Separate values on a cents per tonne of resource basis have been attributed to these projects, having regard to factors including the type of coal (and related coal quality), conceptual mining method, their location, availability of infrastructure, as well as the respective stages of exploration and development.

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## VI Valuation of Stanmore Coal

### Methodology

- 157 As set out in Section III Stanmore Coal currently has six coal projects. Of these only The Range is sufficiently advanced to enable a DCF valuation to be undertaken. Accordingly, the primary methodologies adopted to value each project are as follows.

| Valuation methodology                      |                                                                                                                                                     |                                                                                                                                                                                                                                                                                                                                                                                                                                                                                |
|--------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Project                                    | Primary methodologies                                                                                                                               | Reasons                                                                                                                                                                                                                                                                                                                                                                                                                                                                        |
| The Range                                  | <ul style="list-style-type: none"> <li>DCF</li> <li>Value per resource tonne</li> </ul>                                                             | <ul style="list-style-type: none"> <li>Pre-feasibility study completed in November 2011</li> <li>Definitive feasibility study underway</li> <li>Stanmore Coal has received a 5 Mtpa port allocation in WEXP1 and has a further 2 Mtpa of priority capacity rights available for WEXP2</li> <li>Sensitivity of DCF value to long-term coal price assumption requires consideration of implied values per resource tonne in comparison to recent transaction evidence</li> </ul> |
| Mackenzie and Belview projects             | <ul style="list-style-type: none"> <li>Value per resource tonne</li> </ul>                                                                          | <ul style="list-style-type: none"> <li>While there is a JORC resource at both projects, feasibility studies have not yet commenced. As a result a DCF method is inappropriate at this time</li> </ul>                                                                                                                                                                                                                                                                          |
| Tennyson, Kerlong and New Cambria projects | <ul style="list-style-type: none"> <li>Regard had to project expenditure to date</li> <li>Value likely to be low given exploration stage</li> </ul> | <ul style="list-style-type: none"> <li>Early stage exploration projects with no current JORC resources</li> <li>Initial drilling undertaken at Tennyson and commenced at Kerlong</li> <li>No drilling yet undertaken at New Cambria</li> </ul>                                                                                                                                                                                                                                 |

### The Range

- 158 As stated above we have undertaken DCF analyses on The Range project. Under the DCF methodology the value of the project is equal to the NPV of the estimated future free cash flows (after tax). In order to arrive at the NPV the future cash flows are discounted using a discount rate which reflects the risks associated with the cash flow stream.
- 159 Our DCF calculations are based on the free cash flow projections derived from the pre-feasibility study completed in November 2011, which have been adjusted where appropriate to reflect the latest results of the detailed feasibility study currently in progress. These feasibility studies have been undertaken with significant input from technical mining experts such as The Minserv Group.
- 160 The DCF analyses therefore reflect the views expressed in the feasibility studies on technical mining matters and our opinion on future coal prices, exchange rates, discount rates and other economic and valuation parameters.

161 It should be noted that in respect of these projections:

- (a) the major assumptions underlying the projections were formulated in the context of current economic, financial and other conditions
- (b) future profits and cash flows are inherently uncertain. This is particularly so as coal prices have varied significantly in recent years
- (c) the achievability of these projections is not warranted or guaranteed by Stanmore Coal or LEA, as they are projections based fundamentally on predictions of future events that cannot be assured and are necessarily based on assumptions, many of which are beyond the control of management; and
- (d) actual results may be significantly more or less favourable than projected.

162 Free cash flow represents the operating cash flows on an ungeared basis (i.e. before interest) less taxation payments<sup>35</sup>, capital expenditure and working capital requirements. The free cash flow on an ungeared basis is adopted to enable the value of the mining assets to be determined irrespective of the level of debt funding employed. Our DCF valuation has been undertaken in nominal (inflation adjusted) terms using nominal cash flows and discount rates.

#### Production scenarios

163 We have undertaken our DCF analyses under two scenarios as follows:

- (a) **Scenario 1** – assuming production of 5 Mtpa of saleable export thermal coal over a 26 year mine life<sup>36</sup>. This is consistent with the production profile set out in the pre-feasibility study announced in November 2011
- (b) **Scenario 2** – assuming initial production of 5 Mtpa, increasing to 7 Mtpa following commissioning of WEXP2. As stated above, Stanmore Coal has received a 5 Mtpa port allocation in WEXP1 and has 2 Mtpa priority capacity rights available for WEXP2.<sup>37</sup>

164 Under both scenarios total saleable coal production of some 125 Mt is assumed. In comparison the project contains a JORC marketable reserve of 94 Mt<sup>38</sup> and total resources (on a run of mine (ROM) basis) of 260 Mt (184 Mt indicated and 76 Mt inferred). The production scenarios therefore assume approximately 27% of resources outside the current reserve will become marketable reserves, consistent with the assumptions in the pre-feasibility study.

<sup>35</sup> Also calculated on an ungeared basis.

<sup>36</sup> We note that under some long-term thermal coal price assumption scenarios the economic mine life is shortened because of a significant increase in operating costs after an initial 17 years of steady state production (due to a step up increase in the strip ratio and the resulting increase in overburden removal costs).

<sup>37</sup> Based on discussions with Stanmore Coal management, we understand the mine and related mine infrastructure will be developed to a capacity of 7 Mtpa of product coal. We have therefore assumed no change in capital or operating costs under Scenario 2. Essentially the main value benefit will be earlier access to the cash flows arising from the sale of coal, as the amount of coal produced and the margins (in real terms) are largely identical in both scenarios.

<sup>38</sup> The JORC probable reserve (on a ROM basis) is 117.5 Mt.

## Project timing

165 The timing of The Range project (and adjacent coal projects in the Surat Basin) is dependent on access to required rail and port infrastructure, as discussed in more detail in Section III of this report. In summary:

- (a) stage 1 of WICET achieved financial close in September 2011 and on completion will provide initial port capacity of 27 Mtpa (expected in late 2014)
- (b) Stanmore Coal has received a port allocation in WEXP1 of 5 Mtpa, and has a priority capacity right to a further 2 Mtpa available for WEXP2
- (c) the development of Xstrata Coal's Wandoan mine is critical to the development of all (North) Surat Basin coal projects, as it is proposed to be the largest user of WICET and the Surat Basin Rail (SBR), and therefore underpins the investment required in related rail and port infrastructure. In this regard Xstrata Coal has committed \$220 million associated with entering into a CCD in respect of WEXP1
- (d) the proposed funding of WEXP1, SBR and Wandoan are inter-related and financial close on each will effectively be conditional on all the projects proceeding. Due to the significant total level of funding required and the current weak coal market conditions<sup>39</sup>, Stanmore Coal management do not expect financial close in relation to WEXP1 to occur until late 2013
- (e) first coal from The Range is being targeted for mid 2016, after allowing for a WEXP1 construction phase of around three years. For valuation purposes we have conservatively assumed that first coal is not shipped until January 2017
- (f) any increase in production at The Range above the initial 5 Mtpa of product coal is dependent on securing port capacity, most likely from WEXP2. Stanmore Coal management's current view is that it is likely to be a further two years after WEXP1 achieves financial close before financial close on WEXP2. Under our Scenario 2 calculations therefore full production to 7 Mtpa does not occur until 2020.

## Capital expenditure

166 The pre-feasibility study sets out the following upfront capital expenditure costs under both scenarios:

| The Range – development capital costs <sup>(1)</sup> |                      |                            |
|------------------------------------------------------|----------------------|----------------------------|
|                                                      | Owner mining<br>A\$m | Contract<br>mining<br>A\$m |
| Coal handling and preparation plant                  | 134                  | 134                        |
| Surface infrastructure                               | 120                  | 123                        |
| Conveyer and rail loop                               | 113                  | 113                        |
| Mining fleet to first coal production                | 101                  | -                          |
| Mining fleet to ramp up to full production           | 85                   | -                          |
| Contingency                                          | 37                   | 37                         |
| Total                                                | 590                  | 407                        |

<sup>39</sup> Spot thermal coal prices have fallen significantly in recent weeks.

**Note:**

1 Capital costs are shown in 2011 dollar terms.

- 167 As noted a decision to contract mine will significantly reduce upfront development costs, but will however increase annual operating expenses. Due to the significantly higher upfront capital costs and commissioning risks associated with owner mining, in our view, it is more appropriate for current valuation purposes to assume contract mining.
- 168 On-going capital expenditure to sustain mining operations (assuming contract mining) is estimated at, on average, around US\$4 million per annum over the project life under both the 5 Mtpa and 7 Mtpa scenarios.

**Operating costs**

- 169 Excluding state government royalties and the impact of the MRRT, in 2012 dollar terms<sup>40</sup> the weighted average operating costs over the first 17 years of the mine life are estimated at A\$81.70 per tonne of saleable coal (consistent with the operating cost assumptions set out in the PFS). After the first 17 years operating costs increase due to an increase in the strip ratio and the resulting increase in overburden removal costs. Under some long-term thermal coal price assumption scenarios therefore the economic mine life is shortened.
- 170 For the purpose of our DCF calculations we have assumed no difference in weighted average operating costs per tonne between Scenario 1 and Scenario 2. This is consistent with our earlier assumption of the mine being developed to a capacity of 7 Mtpa of product coal, but is likely to be conservative as some costs would reduce on a per tonne basis as a result of the higher saleable production under Scenario 2.
- 171 Coal royalties represent a significant cost to Queensland coal miners. From 1 October 2012 Government royalties in Queensland are 7% up to a free on board (FOB) sales value of A\$100 per tonne, 12.5% on FOB revenue above A\$100 per tonne and 15% on FOB revenue above A\$150 per tonne<sup>41</sup>.
- 172 Allowances have also been made for carbon tax costs<sup>42</sup> (assuming a typical level of Surat Basin fugitive emissions) and the impact of the MRRT (which has no effect on the DCF value assuming real FOB Newcastle benchmark coal prices are \$120 per tonne or less, due to the high level of State royalties paid relative to the cash margins earned).

**Discount rate**

- 173 A (nominal) discount rate of 12.0% per annum (after-tax) has been adopted for the DCF valuation of The Range project, which has been derived using the capital asset pricing model (CAPM) and the weighted average cost of capital (WACC) formulae using the following inputs.

<sup>40</sup> Although the PFS costs are stated in 2011 real terms, we have adopted these costs as 2012 real costs based on advice from Stanmore Coal management that nothing has come to their attention from the on-going feasibility work to suggest a need to change any operating cost assumptions.

<sup>41</sup> In the Queensland State budget (announced on 11 September 2012) coal royalties were increased on FOB sales revenue above A\$100/t from 10% to 12.5%, and to 15% of FOB sales revenue above A\$150 per tonne.

<sup>42</sup> Carbon tax costs are included in the above operating costs per tonne.

| WACC – nominal          |                   |
|-------------------------|-------------------|
| Parameters              | The Range project |
| Risk free rate          | 4.5%              |
| Market risk premium     | 6.0%              |
| Beta                    | 1.3               |
| Cost of equity          | 12.3%             |
| Additional risk premium | 2.0%              |
| Adjusted cost of equity | 14.3%             |
| Cost of pre tax debt    | 7.5%              |
| Tax rate                | 30.0%             |
| Cost of post tax debt   | 5.3%              |
| Gearing                 | 25.0%             |
| After tax nominal WACC  | 12.0%             |

- 174 The currently prevailing 10 year Commonwealth Government bond rate is well below historical levels and reflects, inter-alia, the weak outlook for global economic growth (and its impact on the outlook for the Australian economy) and the effect of quantitative easing measures by major overseas central banks. At the same time credit spreads have generally increased to offset the impact of the lower risk-free rate. Accordingly, in our view the application of current (low) government bond yields and long-term average market risk premiums is inappropriate in the context of determining long-term required equity rates of return (discount rates). As it is difficult to reliably measure short-term movements in the market risk premium we have therefore increased the risk-free rate for the purpose of estimating required equity rates of return only<sup>43</sup>. We note that this approach to assessing the required equity rate of return is consistent with the approach adopted in an Independent Pricing and Regulatory Tribunal (IPART) decision in December 2011.
- 175 The beta estimate adopted of 1.3 reflects our review of the betas for other listed coal companies and the beta for the overall mining sector (which was 1.12 as at 30 June 2012)<sup>44</sup>.
- 176 We have applied an additional equity risk premium of 2.0% per annum when valuing The Range project. This reflects the greater risks associated with mines in development compared to existing mine operations (which is not reflected in our beta estimate).

#### Exchange rate

- 177 Our assessment of the AUD/USD exchange rates that we consider appropriate for the purpose of our valuation of The Range project is based upon a blended analysis of forward market estimates and long-term (and in some instances short-term) historical foreign exchange trends. We set out below the actual AUD/USD forward rates for the years CY16 to CY20 and broker forecasts for the year 2016.

<sup>43</sup> Had a higher risk-free rate not been adopted, in our view, it would be appropriate to adopt a correspondingly higher market risk premium

<sup>44</sup> Sector betas are generally more reliable than individual stock betas.

**AUD/USD forecasts and forward rates as at 7 September 2012**

|                                                 | AUD/USD     |
|-------------------------------------------------|-------------|
| <b>Broker forecasts for CY16 (sample of 10)</b> |             |
| Mean                                            | 0.89        |
| Median                                          | 0.90        |
| Range                                           | 0.79 – 0.95 |
| <b>Forward rates</b>                            |             |
| CY16 <sup>(1)</sup>                             | 0.92        |
| CY17 <sup>(1)</sup>                             | 0.90        |
| CY18 <sup>(1)</sup>                             | 0.87        |
| CY19 <sup>(1)</sup>                             | 0.86        |
| CY20 <sup>(1)</sup>                             | 0.84        |

**Note:**

1 As at 30 June of the respective calendar year.

**Source:** Bloomberg.

- 178 We have adopted a long-term exchange rate (i.e. for CY17 and beyond) of A\$1.00 = US\$0.85<sup>45</sup> to A\$1.00 = US\$0.90. In our opinion, these rates are appropriate long-term rates for valuation purposes over the DCF forecast horizon.

**Inflation rate**

- 179 As stated above our analysis has been undertaken in nominal terms, including allowances for inflation. For the purpose of our valuation we have adopted an inflation rate of 2.3% per annum, consistent with:
- (a) the difference between long-term Australian Government bond yields (which reflect inflationary expectations) and Australian Government indexed bonds yields (which are quoted in real terms excluding inflation) over recent months<sup>46</sup>; and
  - (b) the Reserve Bank of Australia's (RBA) target for inflation of between 2% and 3% per annum.

**Future coal prices**

- 180 As noted above, for valuation purposes we have assumed that initial coal production from The Range is not expected to be shipped until 2017. Accordingly, the relevant coal prices for valuation purposes are the long-term prices. In forming our opinion on the appropriate long-term thermal coal prices to adopt we have considered, inter alia:
- (a) analysts' long-term coal price forecasts
  - (b) industry participants' views as to the short and long-term outlook for coal prices generally
  - (c) China's import behaviour in the coal market, which has significant implications for future coal prices<sup>47</sup>

<sup>45</sup> We note that an exchange rate of A\$1.00 = US\$0.85 was assumed in the PFS.

<sup>46</sup> The long-term inflation rate in the US (based on the yields on 30 year US Government bonds and index bonds of a similar maturity) is also around 2.3% per annum.

- (d) the forward prices quoted on futures markets<sup>48</sup>
- (e) the historical correlation between USD denominated coal and commodity prices and the AUD/USD exchange rate
- (f) the long-term prices (in AUD) for coal used by independent experts conducting valuations of coal projects in Australia in recent years
- (g) the quality and energy content of the coal produced (e.g. calorific value adjustments etc.).

181 Analysts' long-term price forecasts for export thermal coal (FOB Newcastle) are summarised below.

| Long term thermal coal price forecasts (FOB Newcastle US\$/t in 2012 dollar terms) <sup>(1) (2)</sup> |        |
|-------------------------------------------------------------------------------------------------------|--------|
|                                                                                                       | US\$/t |
| Low                                                                                                   | 80.0   |
| High                                                                                                  | 120.0  |
| Mean                                                                                                  | 93.9   |
| Median                                                                                                | 90.0   |
| Number of analysts                                                                                    | 11     |

**Note:**

1 As at 20 August 2012.

2 Long term coal price reflects average analyst forecast for 2017 to 2021.

**Source:** Consensus Economics Inc.

182 The average (and median) long-term price forecasts by analysts (in 2012 dollar terms) reflect a view that:

- (a) the elevated price levels over recent years (prior to the recent fall in spot prices) were largely the result of mismatches in:
  - (i) demand, which has been boosted by the on-going industrialisation of China, India and other developing nations (which industry participants and analysts generally expect to continue in the long-term); and
  - (ii) supply, which has been constrained by, inter alia, under-investment in necessary port and rail infrastructure and adverse weather events
- (b) over the medium and long-term the supply of most commodities will increase.

183 Over the short to medium term (five years) thermal coal markets are also expected to be impacted by increased supply into seaborne markets by US and Colombian producers. In the US low domestic gas prices (due to increasing shale gas production) and weak electricity demand growth has resulted in US thermal coal exports increasing by over 50% (9 million tonnes) during the first half of calendar 2012<sup>49</sup>. Low thermal coal demand in Europe

<sup>47</sup> Chinese thermal coal imports during the first half of 2012 were 110 million tonnes, up by 46 million tonnes or 73% on the same period of 2011. Source: Xstrata plc Half-Yearly Results 2012.

<sup>48</sup> The FOB Newcastle thermal coal benchmark price for CY17 delivery as at 7 September 2012 was around US\$115/t (in nominal terms).

<sup>49</sup> Source: Xstrata plc Half-Yearly Results 2012.

(Colombia's primary market) and low ocean freight rates have also increased the supply of thermal coal from Colombia into the Pacific (Asian) market.

- 184 However, major coal participants remain optimistic about the outlook for thermal coal prices in the longer term, as evidenced by the following recent statements by major thermal coal producers:

*"Current spot market prices are trading significantly below marginal supply costs for Australian, Indonesian, Russian and US supply. Production cutbacks are expected to continue throughout the second half of 2012, returning the market to a balanced position. Further, an expected seasonal slowdown in Chinese hydro electricity generation during the fourth quarter will provide a recovery in Chinese domestic coal burn and renewed Chinese purchasing interest. In the longer term, demand for thermal coal continues to be driven by its position as the lowest cost fuel for power generation in most economies. Combined with the challenge of developing new coal production capacity, future demand growth is expected to result in a strong pricing environment."* [Source: Xstrata plc Half-Yearly Results 2012, announced on 7 August 2012]

*"Thermal coal demand in the traditional markets of Japan, Korea and Taiwan remains strong. Longer term we expect demand to improve, with Asian demand for both thermal and metallurgical coal continuing to grow, particularly in India and China, along with both countries' preparedness to accept more imported coals in conjunction with domestic coal."* [Source: Rio Tinto, Half Year Results announcement dated 8 August 2012]

*"Long term prices for Anglo American's products are expected to be supported by widespread supply constraints and the challenges producers face in bringing new supply into production, leading to increasing capital intensity and tight market fundamentals. In addition, economic uncertainty is likely to lead to a reduction in capital investment further restraining future supply."* [Source: Anglo American Plc (Anglo), Interim Results announced on 27 July 2012].

- 185 Further, coal experts such as Wood Mackenzie expect thermal coal prices in the longer term to increase significantly above the average and median levels forecast by analysts. This view reflects:

- (a) continued strong demand for seaborne thermal coal in Asia, particularly in China and India where coal remains the lowest cost source of energy and domestic demand significantly exceeds domestic supply
- (b) the elimination of oversupply driven by increased coal demand and the rationalisation of excess supply
- (c) the higher costs associated with bringing required additional coal supply to market (driven by higher operating and capital costs, and the costs associated with access to new rail and port infrastructure)
- (d) the possibility that the current weak market conditions will result in the deferral of some infrastructure projects, constraining supply growth.

186 We set out below the value of The Range project based on various long-term prices for export thermal coal (and exchange rate assumptions). While the table sets out the Newcastle benchmark price for thermal coal, a 9.6% discount to the benchmark price has been applied when valuing The Range to reflect the lower energy content of the coal (consistent with the findings in the pre-feasibility study).

187 The values of The Range project under the two scenarios are as follows:

| Sensitivity table                                   |       |       |       |       |       |
|-----------------------------------------------------|-------|-------|-------|-------|-------|
| <b>Scenario 1 – 5 Mtpa</b>                          |       |       |       |       |       |
| Benchmark coal price (US\$/t – real) <sup>(1)</sup> | 95.0  | 100.0 | 105.0 | 110.0 | 115.0 |
| AUD/USD exchange rate (\$) <sup>(2)</sup>           | 0.850 | 0.863 | 0.875 | 0.888 | 0.900 |
| Coal price (A\$/t – real)                           | 111.8 | 115.9 | 120.0 | 123.9 | 127.8 |
| NPV of The Range project (A\$m) <sup>(3)</sup>      | (73)  | (8)   | 54    | 117   | 192   |
| <b>Scenario 2 – up to 7 Mtpa</b>                    |       |       |       |       |       |
| Benchmark coal price (US\$/t – real) <sup>(1)</sup> | 95.0  | 100.0 | 105.0 | 110.0 | 115.0 |
| AUD/USD exchange rate (\$) <sup>(2)</sup>           | 0.850 | 0.863 | 0.875 | 0.888 | 0.900 |
| Coal price (A\$/t – real)                           | 111.8 | 115.9 | 120.0 | 123.9 | 127.8 |
| NPV of The Range project (A\$m) <sup>(3)</sup>      | (48)  | 28    | 117   | 197   | 275   |

**Note:**

- 1 FOB Newcastle benchmark price in real terms (2012 dollars).
- 2 We have assumed the lower end of our adopted exchange rate range occurs at the lower end of the coal price range (and likewise for the high end), given the historical correlation between commodity prices and the AUD/USD exchange rate.
- 3 The above values are in nominal terms and reflect the impact of the recently announced increase in Queensland coal royalties.

188 We note that the long-term coal prices adopted are at the higher end of broker forecasts. These higher forecast prices are consistent with the Wood Mackenzie view, recent public statements from major thermal coal producers, factors such as the recent financial close of WICET (which included successful debt financing in excess of \$2.5 billion from both Australian and global capital market providers)<sup>50</sup>, together with funding commitments entered into in respect of new and expansion coal projects requiring the WICET infrastructure. The profitability of these coal projects and therefore the implied economic viability of port infrastructure such as WICET generally rely on long-term real thermal coal prices higher than recent spot prices of around US\$90 per tonne. The risk that the actual long-term thermal coal price (in real terms) may be less than the range adopted has been taken into account when assessing our valuation range.

<sup>50</sup> This provision of debt finance implicitly recognised the long-term economic viability of the Queensland coal projects planned to access the WICET facilities.

### Comparable transactions

189 Given the sensitivity of the value of The Range project to the long-term coal price assumption, we have also had regard to relevant recent transaction evidence regarding coal projects in the development stage. In particular we have had regard to two recent transactions in respect of thermal coal projects in the Surat Basin which require the development of and access to the same rail and port infrastructure as The Range:

- (a) the acquisition by Cockatoo Coal Limited (Cockatoo Coal) in late 2010 of a portfolio of coal assets from Anglo, that included the Collingwood<sup>51</sup> and Taroom projects
- (b) the agreement between Cockatoo Coal and Mitsui Coal Holdings Pty Limited (Mitsui) under which Mitsui acquired (from Cockatoo Coal) a 49% interest in the Woori project, which completed in March 2012.

### *Collingwood, Taroom*

190 Pursuant to the acquisition of the Anglo coal portfolio, Cockatoo Coal acquired a 51% interest in both the Collingwood and Taroom projects (the remaining 49% interests were owned and retained by Mitsui). The consideration paid was \$105.5 million implying a combined value for a 100% interest in the two projects of \$206.9 million.

191 At the time of acquisition total resources of export grade thermal coal at Collingwood and Taroom were 435 Mt, of which 190 Mt were in the measured and indicated categories<sup>52</sup>. The transaction therefore implied a price of \$0.48 per resource tonne and \$1.09 per measured and indicated resource tonne<sup>53</sup>.

### *Woori*

192 The agreement between Cockatoo Coal and Mitsui in respect of the Woori project enabled the parties to align their respective interests in each of the three projects, Collingwood, Taroom and Woori. These projects have since been consolidated into the North Surat Joint Venture (NSJV), managed by Cockatoo Coal.

193 The consideration paid by Mitsui to acquire the 49% interest in Woori was \$37.25 million, implying a value for a 100% interest in the project of \$76.0 million.

194 At the time of the transaction total resources of export grade thermal coal at Woori were 84.3 Mt<sup>54</sup>, of which 40.6 Mt comprised reserves. The transaction therefore implied a price of \$0.90 per measured resource tonne and \$1.87 per reserve tonne.

195 Of further interest in relation to the Woori transaction is that prima facie the NSJV currently plans to develop both the Collingwood and Taroom projects ahead of Woori. The cash flows that will accrue to Mitsui pursuant to the acquisition of Woori are therefore likely to arise later than cash flows expected by Stanmore Coal from development and subsequent mining of The Range.

<sup>51</sup> The Collingwood project is one of three Surat Basin projects (including The Range) subsequently selected to participate in the WEXP1 allocation process.

<sup>52</sup> Measured and indicated resources were 36 Mt and 154 Mt respectively.

<sup>53</sup> At the date of acquisition the Collingwood and Taroom projects did not have a marketable reserve.

<sup>54</sup> All resources were in the measured category.

**Conclusion on comparable transactions**

196 In assessing a value of The Range project based on the two comparable transactions above we note:

- (a) the quantum and ratio of marketable reserves and total resources at The Range is more comparable with the reserve / resource status at Woori at the transaction date, rather than Collingwood and Taroom
- (b) The Range has been selected as a participant in the development of critical rail and port infrastructure (none of Collingwood, Taroom or Woori had this status at the respective transaction dates)
- (c) the Cockatoo Coal acquisition of Collingwood and Taroom was part of a consortium acquisition of the total Anglo coal portfolio offered for sale, with the major consortium membership represented by two significant Korean entities. Primarily therefore both the comparable transactions represented the acquisition of interests in Surat Basin located coal projects by major Asian investors
- (d) based on an analysis of recent transactions in respect of Australian coal projects yet to be brought into production, we note that major Asian investors (and industry participants) in particular have placed higher values on such projects than those attributed by institutional investors in Australia or implied by share market trading.

197 However, subsequent to completion of the two transactions short to medium term investor sentiment towards the coal sector generally has turned negative. As a result the likely timing of required rail and port infrastructure availability for Surat Basin coal projects has been deferred compared with the expectation at the date of the above transactions<sup>55</sup>. In addition, the Queensland State government increased coal royalties effective 1 October 2012, which will have an adverse impact on the profitability and value of coal mining projects in Queensland.

**Assessed value of The Range**

198 As noted above, in assessing a value of The Range we have had regard to both the results of our DCF analyses, together with recent transactions in respect of Surat Basin based thermal coal development projects. For the purpose of our report we have adopted a value of The Range of \$140 million to \$180 million. This valuation range implicitly adopts long-term coal prices which are at the high end of broker forecasts and has regard to the related factors set out in paragraph 188 above.

199 Our valuation range implies the values per resource / reserve tonne set out below. These implied values are lower than the implied values in the Cockatoo Coal transactions (in particular the Woori transaction), reflecting the change in market conditions in the intervening period.

<sup>55</sup> This deferred timing of availability of infrastructure has been reflected in our DCF analyses.

| Implied values per tonne         |       |       |
|----------------------------------|-------|-------|
|                                  | Low   | High  |
| Adopted valuation range (A\$m)   | 140.0 | 180.0 |
| Total resources (Mt)             | 260.0 | 260.0 |
| Total reserves (Mt – ROM basis)  | 117.5 | 117.5 |
| Value per resource tonne (A\$/t) | 0.54  | 0.69  |
| Value per reserve tonne (A\$/t)  | 1.19  | 1.53  |

- 200 The valuation range adopted reflects the current depressed investor sentiment towards the coal sector generally (particularly for coal projects in the development stage) and in our view is representative of the price likely to be realised in the current market conditions.
- 201 However, we do not consider these conditions to be conducive to the sale of a coal development project such as The Range and we note Stanmore Coal has no current intention or (financial) requirement to realise its interest (or part thereof) in the project<sup>56</sup>. As evidenced by the prices paid in coal transactions over recent years (refer Appendix C), in our view, significantly higher values could be achieved in better market conditions.

### Development and exploration projects

- 202 In considering the development and exploration project portfolio of Stanmore Coal we have attributed value to the respective projects primarily on a cents per resource tonne basis. We have had regard to values placed on other development and exploration projects in the Bowen Basin (where the Stanmore Coal projects are located), together with values placed on comparable staged coal projects in the Australian market generally.
- 203 Specific factors we have had regard to include:
- (a) the location of the projects, including proximity to both other mine operations or projects and required infrastructure
  - (b) the availability of required infrastructure (in particular port and rail) and the likely timing thereof
  - (c) the coal types targeted and/or established based on drilling undertaken to date
  - (d) the quantum and nature of established JORC resources and the potential to increase / enhance
  - (e) the respective stage of development of the projects, including the extent to which mining plans have been developed
  - (f) with respect to the (concept) mine plans for the Belview and Mackenzie projects in particular, the extent and nature of the issues that have been identified and the potential for an economic resolution thereof
  - (g) the relatively early stage nature of the Tennyson, Kerlong and New Cambria projects
  - (h) expenditure incurred to date on the projects (by both Stanmore Coal and historically)

<sup>56</sup> Our opinion on the value of a 100% interest in Stanmore Coal has been undertaken for the purpose of considering the conversion terms of the Notes, rather than any proposed change of control transaction in respect of the company.

- (i) recent transaction evidence in the coal sector involving Australian coal projects in development (refer Appendix C)
- (j) the impact on value of the current depressed investor sentiment towards the coal sector generally (particularly for early stage development projects).

204 In comparison with The Range, Stanmore Coal's other coal projects are at a much earlier stage of exploration / development, have not yet secured required rail and port allocations and have long development timelines. As a result they are worth substantially less than The Range on a value per tonne of resource basis. Further, we note that the value of early stage coal projects is inherently more volatile and can vary significantly depending on market conditions. Given the current depressed investor sentiment towards the coal sector generally, our assessed values for the development and exploration project portfolio of Stanmore Coal are as follows:

| Stanmore Coal – valuation of other projects |                             |                                 |                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                   |
|---------------------------------------------|-----------------------------|---------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Project /<br>(JORC resource)                | Value per<br>tonne<br>A\$/t | Assessed<br>value range<br>A\$m | Comments                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                          |
| Mackenzie<br>(143 Mt resource)              | 0.10 – 0.20                 | 14.3 – 28.6                     | <ul style="list-style-type: none"> <li>• Open cut coking coal resource in Bowen Basin</li> <li>• Thin seams requiring two stage wash process</li> <li>• Due to low expected yields (around 30%) project requires high coal prices to be economic</li> <li>• Close to rail line, but need to secure rail and port access</li> <li>• Depressed investor sentiment towards coal sector means value attributed to early stage development projects is low</li> </ul>                                                                                                                                                                                                                                                                                                                  |
| Belview<br>(95 Mt resource)                 | 0.15 – 0.25                 | 14.3 – 23.8                     | <ul style="list-style-type: none"> <li>• Concept study completed</li> <li>• Quality hard coking coal (CSN of 7.0 with low ash)</li> <li>• 5 km from rail line but need to secure rail / port access</li> <li>• Deep seams (560 m to 1,000 m) will require shaft mining and relatively high cash costs envisaged due to depth of resource</li> <li>• Inferred resource based on only six drill holes. Further drilling planned to seek to establish larger resource base required to justify high upfront capital expenditure (of some A\$900 million)</li> <li>• Long development time frame due to establishment of shafts and longwall</li> <li>• Depressed investor sentiment towards coal sector means value attributed to early stage development projects is low</li> </ul> |
| Tennyson,<br>Kerlong and New<br>Cambria     | n/a                         | 2.0 – 5.0                       | <ul style="list-style-type: none"> <li>• Exploration targets only</li> <li>• No JORC resources</li> </ul>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                         |
| <b>Total</b>                                |                             | <u>30.6 – 57.4</u>              |                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                   |

## Corporate costs

- 205 Corporate costs of around A\$4 million (before tax) are incurred annually and are not taken into account in the above project values. After deducting public company costs which would not be incurred by an acquirer of 100% of Stanmore Coal, we have deducted the capitalised value of these after tax costs in our valuation. Based on the DCF methodology and a discount rate of 12% per annum (equal to the rate applied when valuing The Range) we have adopted a value for future corporate costs of negative A\$20 million to A\$25 million.

## Net cash

- 206 As at 30 June 2012 Stanmore Coal had cash balances of \$23.9 million and borrowings of approximately \$4.0 million.
- 207 The cash balance at 30 June 2012 includes the proceeds of \$12.98 million from the first tranche of the placement to Greatgroup. Pursuant to the terms of the funding agreement with Greatgroup a further \$23 million will be received on allotment of the second tranche of shares.
- 208 Together with available debt facilities (which total \$25 million), Stanmore Coal has advised that its cash resources will be sufficient to fund its bid bond and equity contributions associated with the WEXP1 and SBR CCDs. On financial close of these infrastructure projects we understand that the respective financial commitments made by Stanmore Coal pursuant to the CCDs convert to equity, and could be subsequently monetised<sup>57</sup>. In our view therefore, it is appropriate to include the following net cash balances in our valuation.

| Stanmore Coal – pro-forma net cash                                                                         |       |
|------------------------------------------------------------------------------------------------------------|-------|
|                                                                                                            | \$m   |
| Cash as at 30 June 2012                                                                                    | 23.9  |
| Borrowings as at 30 June 2012                                                                              | (4.0) |
| Net cash as at 30 June 2012                                                                                | 19.9  |
| Add further cash to be received pursuant to the issue of the tranche 2 shares and the Notes <sup>(1)</sup> | 23.0  |
| Less: Allowance for estimated cash outflow in quarter ended 30 September 2012 <sup>(2)</sup>               | (7.1) |
| Pro-forma net cash                                                                                         | 35.8  |

### Note:

- 1 Approval by Stanmore Coal shareholders to issue these securities was obtained on 10 October 2012.
- 2 Source: Quarterly cash flow report.

## Dilution

- 209 In addition to the funding requirements associated with the WEXP1 and SBR CCDs, Stanmore Coal will also need to fund the capital costs associated with the development of The Range.

<sup>57</sup> We note that Cockatoo Coal recently announced that it had sold its Wiggins Island Preference Shares (WIPS), acquired as part of the financing for the development of WICET (at a small profit).

- 210 As stated above, the upfront capital costs for The Range (on a contract mining basis) exceed A\$400 million (in 2011 dollar terms). Whilst it is likely that a significant proportion of this capital cost can be debt funded, significant equity capital will also need to be invested. Accordingly, in assessing our valuation range for Stanmore Coal shares we have also considered whether allowance needs to be made for future equity dilution (over and above that implicit in the funding arrangements with Greatgroup).
- 211 In our view it is more likely that in time Stanmore Coal will seek to sell down its interest in The Range in order to fund its equity share of the upfront capital cost, rather than undertake a large (equity) capital raising. In this regard we note that Stanmore Coal currently has a 100% ownership interest in the project and has not yet entered into any off-take agreement<sup>58</sup>. Accordingly, in our view, a future sell down of Stanmore Coal's interest in the project is likely to be of interest to a number of Asian purchasers looking to secure long-term thermal coal supply.
- 212 On the reasonable assumption that any such sell down would be priced at a level (at least) broadly consistent with the pro-rata valuation range attributed by us to The Range, in our opinion, no further allowance for dilution is required.

### **Fully diluted share capital**

- 213 Upon the conversion to ordinary shares of the Notes issued to Greatgroup, Stanmore Coal will have approximately 213.5 million shares on issue<sup>59</sup>.
- 214 In addition the company has a number of "in-the-money" employee options which we expect would be exercised in the event of a change of control transaction for 100% of Stanmore Coal<sup>60</sup>. Accordingly, for valuation purposes, we have included "in-the-money" employee options in fully diluted shares on issue, and have added the cash to be received from the assumed exercise thereof.
- 215 Subsequent to shareholder approval received on 10 October 2012, Stanmore Coal also proposes to issue 11.67 million options exercisable at 51.8 cents per share to Credit Suisse in consideration for providing a debt facility. For the purpose of our report we have assumed that the company will elect to settle these options by the issue of Stanmore Coal shares, and have included in our valuation both the related shares in fully diluted shares on issue and the cash from the assumed exercise thereof.

<sup>58</sup> While Stanmore Coal has appointed Greatgroup as a coal marketing agent with respect to 15% of Stanmore Coal's production, in our view, this will not materially preclude any proposed sell down of an interest in The Range.

<sup>59</sup> While our report is required in connection with a resolution to approve the conversion of the Notes to ordinary shares, in our opinion, it is reasonable and appropriate to assume such an equity issue in any event to ensure Stanmore Coal has sufficient financial resources to meet its WEXP1 and SBR commitments.

<sup>60</sup> While the exercise of some options is subject to the employees meeting various vesting conditions, in our experience, these conditions are usually waived in the event of a change of control transaction for 100% of a company.

### Valuation on 100% controlling interest basis

- 216 Based on the above we have assessed the market value of Stanmore Coal shares on a 100% controlling interest basis as follows.

| Valuation of Stanmore Coal shares – 100% controlling interest basis |               |               |
|---------------------------------------------------------------------|---------------|---------------|
|                                                                     | Low<br>\$m    | High<br>\$m   |
| Value of The Range                                                  | 140.0         | 180.0         |
| Value of other development and exploration projects                 | 30.6          | 57.4          |
| Corporate costs                                                     | (25.0)        | (20.0)        |
| Net cash                                                            | 35.8          | 35.8          |
| Cash from exercise of employee options                              | 2.0           | 2.1           |
| Cash from exercise of financier options                             | 6.0           | 6.0           |
| <b>Equity value</b>                                                 | 189.4         | 261.3         |
| Fully diluted shares on issue <sup>(1)</sup>                        | 235.7         | 235.9         |
| <b>Value per share</b>                                              | <b>\$0.80</b> | <b>\$1.11</b> |

**Note:**

- 1 Includes shares issued on conversion of the Notes and exercise of both the employee and financier options.

### Comparison with listed market price

- 217 We note that even after allowance for a control premium implicit in our assessed value of a 100% interest in Stanmore Coal, our assessed value range significantly exceeds the market capitalisation of the company based on recent trading in Stanmore Coal shares.
- 218 Based on LEA's observation, this level of disconnect is consistent with listed coal companies generally and reflects a situation that has prevailed for some time. Recent transactions representative of this disparity include:
- (a) the announcement in May 2012 by NuCoal Resources Ltd (NuCoal) of the sale of a 10% interest in the Doyles Creek coal development project to Mitsui Matsushima International Pty Ltd at a price that implied a total value for the project of around \$360 million. Notwithstanding a significant net cash position in NuCoal, together with ownership of other coal exploration projects, the market capitalisation of the company remains around 35% of the value of the Doyles Creek project implied by the transaction
  - (b) the arrangements entered into between Stanmore Coal and Greatgroup, in particular in relation to the 19.9% equity interest in the company acquired at a price of \$0.675 per share. Notwithstanding the related announcement in June 2012, shares in Stanmore Coal have continued to trade materially below the Greatgroup subscription price.
- 219 We consider the acquirers of interests in the Australian coal development projects above (and for example in the Cockatoo Coal related Surat Basin transactions) to have taken a long-term view on both the specific projects and the coal sector generally. In contrast a number of market commentators and participants consider the greater influence on current share market trading to be that of investors with a short-term investment horizon.

- 220 In this regard we note that in the six month period ended April 2012, shares in Stanmore Coal traded on the ASX in a range of around \$0.80 per share to in excess of \$1.00 per share. In addition during December 2011 and January 2012 Stanmore Coal successfully raised new equity capital of \$24.1 million at a price of \$0.74 per share. Trading on the ASX reflects portfolio (or minority) interests in a company, whereas our assessed value of Stanmore Coal for the purpose of our report reflects a 100% controlling interest in the company.
- 221 In the circumstances we do not consider recent share market trading<sup>61</sup> in Stanmore Coal shares to be a representative basis on which to form a view as to the 100% controlling interest value of the company.

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<sup>61</sup> Adjusted for a standard premium for control.

## VII Evaluation of the Notes conversion terms

### Evaluation approach

- 222 In LEA's opinion, the most appropriate basis on which to evaluate the Notes conversion terms is to assess the overall impact on Stanmore Coal shareholders not associated with Greatgroup and to form an opinion as to whether, on balance, the advantages associated with conversion of the Notes (and related approval by non-associated Stanmore Coal shareholders of the Notes conversion terms) outweigh the disadvantages. In considering the respective advantages and disadvantages we have had regard to the following factors.

### The need for equity capital

- 223 As set out in Section III Stanmore Coal has a number of mine development (and exploration) projects, the most advanced of which is The Range located in the Surat Basin in Queensland. A PFS in respect of this project was completed in November 2011 and a subsequent BFS is currently underway. Initial coal production from The Range is currently targeted to commence in mid 2016.
- 224 Targeted production from The Range is dependent in particular on the establishment of related infrastructure, including mine infrastructure and associated rail and port facilities. To date Stanmore Coal has met related financial commitments primarily from equity capital raisings, and more recently short-term debt funding. Specific short to medium term financing requirements (both committed and expected) include:
- (a) the provision of bank guarantees in respect of the CCDs for both WEXP1 and SBR (and the related subsequent take-or-pay commitments to be entered into)
  - (b) capital expenditure for the proposed mine development at The Range.
- 225 In summary Stanmore Coal has an on-going need for funding for its coal portfolio. The ability to convert the Notes to permanent equity funding in Stanmore Coal (both the company and Greatgroup have conversion rights), prima facie therefore preserves funding within the company and avoids the need to make a payment of \$9.03 million to redeem the Notes at a time when annual company operational cash flows have yet to be established.

### Comparison with share market prices

- 226 We have set out in section III a summary of share market trading in Stanmore Coal shares. In the three month period prior to the trading halt which preceded the announcement of the funding agreement with Greatgroup (up to 26 June 2012) Stanmore Coal shares traded between \$0.33 per share and \$0.82 per share. The VWAP during this period was \$0.58 per share.
- 227 Accordingly, the price of \$0.675 per share at which Stanmore Coal shares are to be allotted to Greatgroup pursuant to a conversion of the Notes represents a significant premium to the market price of Stanmore Coal shares prior to the announcement, as shown below.

| Conversion premium to recent Stanmore share prices                                |              |                                     |
|-----------------------------------------------------------------------------------|--------------|-------------------------------------|
|                                                                                   | \$ per share | Implied premium <sup>(1)</sup><br>% |
| Price at which shares are to be allotted to Greatgroup on conversion of the Notes | 0.675        |                                     |
| Closing price on 26 June 2012                                                     | 0.36         | 87.5                                |
| <b>VWAP:</b>                                                                      |              |                                     |
| 1 month to 26 June 2012                                                           | 0.43         | 57.0                                |
| 3 months to 26 June 2012                                                          | 0.58         | 16.4                                |
| <b>Note:</b>                                                                      |              |                                     |
| 1 Based on proposed conversion price per share.                                   |              |                                     |

- 228 We also note that the conversion price of \$0.675 per Stanmore Coal share is consistent with the price at which Stanmore Coal shares have been allotted to Greatgroup pursuant to both tranche 1 and tranche 2 of the funding agreement. The tranche 1 allotment price of \$0.675 per share also included product coal marketing arrangements between the parties, under which Greatgroup was appointed as a coal marketing agent with respect to 15% of Stanmore Coal's production. Prima facie therefore the conversion price on the Notes (with no attaching related arrangements) represents a premium to the allotment price on the related equity capital raising.
- 229 As set out above, the Notes have a three year term and are convertible into ordinary shares in Stanmore Coal 24 months after their date of issue. Conversion rights may be exercised by either Greatgroup or the company. Clearly the price of Stanmore Coal shares in the 12 month period in which the conversion rights can be exercised is an unknown at this stage. However as there will be an apparent commercial benefit for the company to exercise its conversion right if the prevailing share price at the time is below \$0.675 per share, and vice-versa for Greatgroup if the price is above \$0.675 per share, it is highly likely that conversion of the Notes will take place. Given the above, together with the zero coupon status of the Notes, the issue of the Notes effectively provides Stanmore Coal with permanent equity funding at a significant premium to the prevailing share price prior to entering into the agreement relating to their issue.
- 230 We also note that the Notes conversion price of \$0.675 per share represents a significant premium to the price at which Stanmore Coal shares have recently traded subsequent to the announcement of the funding arrangements with Greatgroup.

### Assessment of Notes conversion price

- 231 Pursuant to RG 111, when assessing the fairness of the Notes conversion terms (including the conversion price), the value of the Stanmore Coal shares to be allotted on conversion must be assessed on a 100% controlling interest basis (notwithstanding that pursuant to the funding arrangements entered into Greatgroup will only acquire a significant (but not controlling) 25% interest in Stanmore Coal on a subsequent conversion of the Notes).
- 232 As set out in section VI we have assessed the value of Stanmore Coal shares on a 100% controlling interest basis at \$0.80 to \$1.11 per share.

233 Under RG 111 the Notes conversion price is “fair” if the conversion price is equal to or greater than the value of the shares to be allotted on conversion.

234 This comparison is set out below:

| Fairness under RG 111                                                                                                  |           |            |                 |
|------------------------------------------------------------------------------------------------------------------------|-----------|------------|-----------------|
|                                                                                                                        | Low<br>\$ | High<br>\$ | Mid-point<br>\$ |
| Notes conversion price per share                                                                                       | 0.675     | 0.675      | 0.675           |
| Value of Stanmore Coal per share <sup>(1)</sup>                                                                        | 0.80      | 1.11       | 0.955           |
| Extent to which the Notes conversion price per share is less than the value of the Stanmore Coal shares to be allotted | (0.125)   | (0.435)    | (0.28)          |

**Note:**

1 Based on a 100% controlling interest value.

235 Because the value of Stanmore Coal shares on a 100% controlling interest basis exceeds the Notes conversion price per share, the price at which the Notes convert into ordinary shares in Stanmore Coal is not fair when assessed under RG 111. This is because under the Notes conversion terms, Stanmore Coal shares are being issued to Greatgroup at a price which is below the full underlying value of Stanmore Coal shares (being their value on a 100% controlling interest basis).

236 However, given the circumstances of the proposed conversion of the Notes, in our opinion, it is more appropriate (from a commercial perspective) to assess the conversion price per share based on a value for Stanmore Coal shares which reflects the size of Greatgroup’s potential increased shareholding and related proposed voting entitlement (particularly as Greatgroup will not control Stanmore Coal subsequent to a potential conversion of the Notes).

237 Pursuant to a potential conversion of the Notes we note that:

- (a) control of Stanmore Coal would not pass to Greatgroup as Greatgroup’s shareholding would be approximately 25%<sup>62</sup> subsequent to conversion
- (b) Stanmore Coal’s board of six directors includes one director nominated by Greatgroup (which will not change subsequent to a conversion of the Notes)
- (c) Stanmore Coal’s existing shareholders retain all their shares subsequent to a conversion of the Notes and would not be deprived of the potential opportunity to realise a takeover premium in the future<sup>63</sup>.

238 Accordingly, in our opinion, it is not commercially realistic to expect that Greatgroup would pay a full control premium for the shares in Stanmore Coal to be allotted to it pursuant to a conversion of the Notes. The conversion price of the Notes of \$0.675 per Stanmore Coal

<sup>62</sup> Based on the issued share capital of Stanmore Coal subsequent to the allotment of the tranche 2 shares to Greatgroup.

<sup>63</sup> Given that Greatgroup will have an interest of 19.9% in Stanmore Coal shares subsequent to the allotment of tranche 2 shares, a third-party seeking to make a takeover offer would need to persuade Greatgroup to accept its offer in order to obtain control of Stanmore Coal irrespective of the increased interest of Greatgroup that would arise on conversion of the Notes.

share represents a discount of 15.6% to the low end of our valuation range for Stanmore Coal shares on a 100% controlling interest basis. We consider this level of discount to be reasonable having regard to the increased interest of Greatgroup in Stanmore Coal that will arise on a conversion of the Notes. Accordingly we have concluded that the Notes conversion price is reasonable.

### Strategic tie-up with Greatgroup

- 239 In addition to the funding arrangements entered into, Stanmore Coal and Greatgroup have entered into product coal marketing arrangements, under which Greatgroup has been appointed as a coal marketing agent with respect to 15% of Stanmore Coal's production (effective from the commencement of production for an initial period of five years).
- 240 Stanmore Coal and Greatgroup have also agreed to explore opportunities to co-operate on future growth initiatives, including the funding and support of acquisitions, the development of infrastructure and the arrangement of take-or-pay guarantees.
- 241 Whilst these agreements and undertakings are in place as a consequence of the equity allotments made to Greatgroup, a potential conversion of the Notes whereby Greatgroup increases its interest in the company arguably enhances the positive relationship between the parties.

### Impact on control

- 242 If the conversion terms of the Notes are approved there will be a potential impact on the voting power and ownership of Stanmore Coal. In the event of a subsequent conversion of the Notes and related allotment of shares, Greatgroup (which subsequent to the issue of the tranche 2 shares holds a relevant interest in Stanmore Coal shares of approximately 19.9%) will increase its relevant interest to 25% (assuming no further equity raisings prior to conversion) as follows:

| Shares on issue post conversion of the Notes      |                                                |                              |      |
|---------------------------------------------------|------------------------------------------------|------------------------------|------|
|                                                   | Stanmore<br>Coal shares<br>on issue<br>Million | Shares held by<br>Greatgroup |      |
|                                                   |                                                | Million                      | %    |
| Shares on issue subsequent to tranche 2 allotment | 200.2                                          | 40.0                         | 19.9 |
| Conversion of the Notes                           | 13.4                                           | 13.4                         | n/a  |
| Shares on issue post conversion of the Notes      | 213.6                                          | 53.4                         | 25.0 |

**Note:**

n/a – not applicable.

- 243 Therefore if the conversion terms of the Notes are approved, and in the event of a subsequent conversion of the Notes, Greatgroup will increase its voting interest in Stanmore Coal.
- 244 In respect of the increased interest of Greatgroup which will arise pursuant to a conversion of the Notes, non-associated Stanmore Coal shareholders should note:
- (a) the earliest date for conversion of the Notes is 27 June 2014

- (b) during this period Greatgroup could increase its interest in Stanmore Coal to 25% (and beyond) in any event under the statutory “creep” exemption set out in section 611(9) of the Corporations Act
- (c) the equity funding arrangements entered into provide Greatgroup with anti-dilution rights (under certain agreed circumstances) in respect of both its shareholding interest and the Notes, which effectively enable it to maintain a 25% interest in Stanmore Coal
- (d) conversion of the Notes does not provide Sprint Capital, Greatgroup or any of their associates, with any additional rights regarding Board representation of Stanmore Coal
- (e) by nature, neither Sprint Capital, Greatgroup or its associates are an operator of coal mines and these parties generally seek to be a passive investor in resource projects in which they invest.

245 Accordingly, whilst a conversion of the Notes will increase Greatgroup’s voting interest in Stanmore Coal, it will not control the Board (at either an executive or total member level), nor will it control the day-to-day operations of the company.

246 However, it should be noted that whilst Greatgroup will not control Stanmore Coal, effectively it may be able to veto special resolutions (other than related party transactions in which it has an interest) due to the increased size of its shareholding and voting power.

### **Dilution of existing shareholder interests**

247 If the proposed Notes conversion terms are approved, and in the event of a subsequent conversion of the Notes, the interests of non-associated Stanmore Coal shareholders will be moderately diluted, as they will collectively hold only 75.0 % of Stanmore Coal shares after the related share allotment to Greatgroup<sup>64</sup> (as opposed to their collective shareholding prior to conversion of 80.01%).

248 However, given the coal project equity funding requirements of the company, it should be noted that Stanmore Coal’s non-associated shareholders are likely to be diluted in any event, as Stanmore Coal is likely to require an alternative source of additional equity capital if the conversion terms of the Notes are not approved and the Notes have subsequently to be redeemed.

### **Likelihood of receiving a future takeover offer**

249 If the Notes conversion terms are approved and Greatgroup and its associates increase their interest in Stanmore Coal to 25% on a subsequent conversion of the Notes, in our opinion, the likelihood of Stanmore Coal shareholders receiving a takeover offer in future is unchanged. This is because a potential bidder for the company would need to persuade Greatgroup to accept its offer in any event in order to obtain control of Stanmore Coal<sup>65</sup>.

<sup>64</sup> This voting interest also assumes no further equity issues by Stanmore Coal take place prior to conversion of the Notes.

<sup>65</sup> However, should Greatgroup decide to sell or receive an attractive offer for its interest it is likely that the non-associated Stanmore Coal shareholders will have the opportunity to participate in any takeover premium being offered.

250 Further, there are no restrictions which prevent a third-party making a takeover offer for 100% of the shares in Stanmore Coal either prior to or after the shareholder meeting to approve the Notes conversion terms should they wish to do so.

251 In addition St Lucia Resources International Pty Ltd (a company associated with two Stanmore Coal directors) currently owns approximately 17.7% of Stanmore Coal, which is sufficient to block a full takeover by another party in any event<sup>66</sup>.

## Summary

252 Based on the above we summarise below the advantages and disadvantages associated with conversion of the Notes and related approval by non-associated Stanmore Coal shareholders of the Notes conversion terms:

### Advantages

- (a) Stanmore Coal has an on-going need for funding for its coal portfolio. The ability to convert the Notes to permanent equity funding prima facie preserves funding within the company and avoids the need to make a payment of \$9.03 million to redeem the Notes at a time when annual company operational cash flows have yet to be established
- (b) the Notes conversion price of \$0.675 per share is at a significant premium to both the VWAP at which shares in Stanmore Coal traded prior to the trading halt which preceded the announcement of the funding arrangements with Greatgroup and the prices at which Stanmore Coal shares have traded subsequent to the announcement

### Disadvantages

- (c) the Notes conversion price of \$0.675 per share is below the full underlying value of Stanmore Coal shares and is therefore not fair when assessed under RG 111
- (d) if the Notes conversion terms are approved, and in the event of a subsequent conversion of the Notes, the interests of non-associated Stanmore Coal shareholders will be moderately diluted. However, non-associated shareholders are likely to be diluted in any event, as Stanmore Coal is likely to require an alternative source of additional equity capital if the conversion terms of the Notes are not approved and the Notes have subsequently to be redeemed. In our view, an alternative equity issue (for example, to redeem the Notes) is likely to be significantly more dilutionary if priced at a discount to the listed market price at the time (consistent with the majority of equity capital raisings).

## Implications if the Notes conversion terms are not approved

253 In the event that the Notes conversion terms are not approved there are a number of implications for Stanmore Coal shareholders not associated with Greatgroup including:

- (a) due to Stanmore Coal's on-going need for equity funding to advance both the development of The Range and related infrastructure together with the rest of its coal portfolio, if the conversion terms of the Notes are not approved it is likely that (at the

<sup>66</sup> However, the size of this shareholding would not be sufficient to block the acquisition of a 100% interest in Stanmore Coal if implemented by way of a Scheme of Arrangement.

time) Stanmore Coal would need to undertake an institutional placement and/or rights issue to fund redemption of the Notes

- (b) such a placement or rights issue would be likely to be priced at a discount to the listed market price of Stanmore Coal shares at the time. In contrast, based on the proposed Notes conversion price, Greatgroup is paying a significant premium to the market price of Stanmore Coal shares prior to the announcement of the funding agreement with Greatgroup
- (c) to the extent that a capital raising included a pro-rata rights issue, this would be likely to have a negative effect on the subsequent Stanmore Coal share price in the short-term
- (d) the extent to which investors might be prepared to support an equity raising at the time by a company yet to establish operational cash flows (as is expected to be the situation of Stanmore Coal over the three year term of the Notes) is uncertain.

## Conclusion

- 254 As indicated above there are a number of advantages and disadvantages associated with conversion of the Notes and related approval by non-associated Stanmore Coal shareholders of the Notes conversion terms. However, from the perspective of Stanmore Coal shareholders not associated with Greatgroup, we consider that, on balance, the likely advantages significantly outweigh the likely disadvantages.
- 255 In addition there are a number of negative implications for Stanmore Coal shareholders not associated with Greatgroup in the event that the Notes conversion terms are not approved.
- 256 Accordingly we have concluded that the Notes conversion terms are not fair but reasonable to Stanmore Coal shareholders not associated with Greatgroup.

## Appendix A

### Financial Services Guide

#### Lonergan Edwards & Associates Limited

- 1 Lonergan Edwards & Associates Limited (ABN 53 095 445 560) (LEA) is a specialist valuation firm which provides valuation advice, valuation reports and independent expert's reports (IER) in relation to takeovers and mergers, commercial litigation, tax and stamp duty matters, assessments of economic loss, commercial and regulatory disputes.
- 2 LEA holds Australian Financial Services Licence No. 246532.

#### Financial Services Guide

- 3 The Corporations Act 2001 authorises LEA to provide this Financial Services Guide (FSG) in connection with its preparation of an IER to accompany the Explanatory Memorandum to be sent to Stanmore Coal shareholders in connection with the proposed resolution in respect of the Notes conversion terms.
- 4 This FSG is designed to assist retail clients in their use of any general financial product advice contained in the IER. This FSG contains information about LEA generally, the financial services we are licensed to provide, the remuneration we may receive in connection with the preparation of the IER, and if complaints against us ever arise how they will be dealt with.

#### Financial services we are licensed to provide

- 5 Our Australian Financial Services Licence allows us to provide a broad range of services to retail and wholesale clients, including providing financial product advice in relation to various financial products such as securities, derivatives, interests in managed investment schemes, superannuation products, debentures, stocks and bonds.

#### General financial product advice

- 6 The IER contains only general financial product advice. It was prepared without taking into account your personal objectives, financial situation or needs.
- 7 You should consider your own objectives, financial situation and needs when assessing the suitability of the IER to your situation. You may wish to obtain personal financial product advice from the holder of an Australian Financial Services Licence to assist you in this assessment.

#### Fees, commissions and other benefits we may receive

- 8 LEA charges fees to produce reports, including this IER. These fees are negotiated and agreed with the entity who engages LEA to provide a report. Fees are charged on an hourly basis or as a fixed amount depending on the terms of the agreement with the entity who engages us. In the preparation of this IER, LEA is entitled to receive a fixed fee of \$100,000 plus GST.
- 9 Neither LEA nor its directors and officers receive any commissions or other benefits, except for the fees for services referred to above.

## Appendix A

- 10 All of our employees receive a salary. Our employees are eligible for bonuses based on overall performance and the firm's profitability, and do not receive any commissions or other benefits arising directly from services provided to our clients. The remuneration paid to our directors reflects their individual contribution to the company and covers all aspects of performance. Our directors do not receive any commissions or other benefits arising directly from services provided to our clients.
- 11 We do not pay commissions or provide other benefits to other parties for referring prospective clients to us.

### Complaints

- 12 If you have a complaint, please raise it with us first, using the contact details listed below. We will endeavour to satisfactorily resolve your complaint in a timely manner.
- 13 If we are not able to resolve your complaint to your satisfaction within 45 days of your written notification, you are entitled to have your matter referred to the Financial Ombudsman Services Limited (FOS), an external complaints resolution service. You will not be charged for using the FOS service.

### Contact details

- 14 LEA can be contacted by sending a letter to the following address:
- Level 27  
363 George Street  
Sydney NSW 2000  
(or GPO Box 1640, Sydney NSW 2001)

## Appendix B

### Qualifications, declarations and consents

#### Qualifications

- 1 LEA is a licensed investment adviser under the Corporations Act. LEA's authorised representatives have extensive experience in the field of corporate finance, particularly in relation to the valuation of shares and businesses and have prepared many hundred independent expert's reports.
- 2 This report was prepared by Mr Edwards and Mr Holt, who are each authorised representatives of LEA. Mr Edwards and Mr Holt have over 18 years and 26 years experience respectively in the provision of valuation advice.

#### Declarations

- 3 This report has been prepared at the request of the Directors of Stanmore Coal to accompany the Explanatory Memorandum to be sent to Stanmore Coal shareholders. It is not intended that this report should serve any purpose other than as an expression of our opinion as to whether or not the proposed Notes conversion terms are fair and reasonable to Stanmore Coal shareholders not associated with Greatgroup.

#### Interests

- 4 At the date of this report, neither LEA, Mr Edwards nor Mr Holt have any interest in the outcome of the Notes and share placements. With the exception of the fee shown in Appendix A, LEA will not receive any other benefits, either directly or indirectly, for or in connection with the preparation of this report.
- 5 LEA has had no prior business or professional relationship with Stanmore Coal or Greatgroup prior to the preparation of this report.

#### Indemnification

- 6 As a condition of LEA's agreement to prepare this report, Stanmore Coal agrees to indemnify LEA in relation to any claim arising from or in connection with its reliance on information or documentation provided by or on behalf of Stanmore Coal which is false or misleading or omits material particulars or arising from any failure to supply relevant documents or information.

#### Consents

- 7 LEA consents to the inclusion of this report in the form and context in which it is included in Stanmore Coal's Explanatory Memorandum.

## Appendix C

### Transaction evidence – exploration and pre-development projects

| Date <sup>(1)</sup> | Target                                 | Acquirer                                    | Lifecycle stage <sup>(2)</sup> | OC/UG       | Coal type <sup>(3)</sup> | Project / equity level | Interest acquired % | Consideration ASm | EV <sup>(4)</sup> (100%) ASm | Enterprise value <sup>(5)(6)</sup> / M&I |          |                     |
|---------------------|----------------------------------------|---------------------------------------------|--------------------------------|-------------|--------------------------|------------------------|---------------------|-------------------|------------------------------|------------------------------------------|----------|---------------------|
|                     |                                        |                                             |                                |             |                          |                        |                     |                   |                              | Reserve                                  | resource | Total               |
|                     |                                        |                                             |                                |             |                          |                        |                     | AS / t            | AS / t                       | AS / t                                   | AS / t   | AS / t              |
| May 12              | Doyles Creek project                   | Mitsui Matsushima International             | Pre-development                | UG          | SSCC                     | Project                | 10.0                | 40                | 400                          | na                                       | 2.81     | 0.78                |
| May 12              | Coalworks                              | Whitehaven Coal                             | Pre-development                | OC / UG     | SSCC, TC                 | Equity                 | 100.0               | 184               | 167                          | na                                       | 6.81     | 0.17                |
| Feb 12              | Plasnett Coal project                  | NuCoal Resources                            | Pre-development                | OC          | SSCC, TC                 | Project                | 100.0               | 71                | 71                           | na                                       | na       | 0.36                |
| Dec 11              | Boardwalk Resources                    | Whitehaven Coal                             | Pre development                | OC          | CC, PCI, SHCC, TC        | Equity                 | 100.0               | 463               | 464                          | na                                       | na       | 3.40 <sup>(6)</sup> |
| Sep 11              | MetroCoal                              | DADI Engineering Development Group Co.      | Exploration                    | OC          | TC                       | Equity                 | 15.0                | 24                | 149                          | na                                       | 6.50     | 0.13                |
| Jul 11              | Woori project (Cockatoo Coal)          | Mitsui & Co.                                | Pre-development                | OC          | TC                       | Project                | 49.0                | 37                | 76                           | 1.87                                     | 0.90     | 0.90                |
| May 11              | Lenton project (New Hope Corp.)        | Mai-Liao Power Corp.                        | Exploration                    | OC          | CC, TC                   | Project                | 10.0                | 58                | 580                          | 11.16                                    | 2.95     | 2.06                |
| May 11              | Ellenby Holdings (Monash Coal)         | Gloucester Coal                             | Exploration                    | OC          | SSCC, TC                 | Equity                 | 100.0               | 95                | 95                           | na                                       | 7.31     | 0.33                |
| May 11              | Vickery South (Coalworks)              | ITOCHU Corporation                          | Pre-development                | OC          | SSCC, TC                 | Project                | 49.0                | 11                | 22                           | na                                       | na       | 0.44                |
| Aug 10              | MDL162                                 | Macarthur Coal                              | Pre-development                | OC          | SHCC, PCI                | Project                | 90.0                | 334               | 372                          | na                                       | 2.70     | 1.68                |
| Jul 10              | 5 of Anglo American's coal assets      | POSCO, Korea Electric Power & Cockatoo Coal | Pre-development                | OC / UG     | CC, TC                   | Project                | 100.0               | 580               | 580                          | na                                       | 1.75     | 0.68                |
| Jul 10              | Collingwood & Taroom                   | Cockatoo Coal                               | Pre-development                | OC          | TC                       | Project                | 51.0                | 106               | 207                          | na                                       | 1.09     | 0.48                |
| Jul 10              | Sutton Forest                          | Cockatoo Coal                               | Pre-development                | UG          | CC, TC                   | Project                | 100.0               | 72                | 72                           | na                                       | 0.62     | 0.62                |
| Jul 10              | Bylong & Oxnawiew                      | Korea Electric Power (KEPCO)                | Pre-development                | UG (Bylong) | TC                       | Project                | 100.0               | 403               | 403                          | na                                       | 2.69     | 0.79                |
| Apr 10              | Northern Energy Corporation            | Xinyang Iron and Steel Group company        | Pre-development                | OC          | CC, PCI, TC              | Equity                 | 12.7                | 23                | 181                          | 1.71                                     | 0.73     | 0.35                |
| Feb 10              | Doyles Creek project                   | NuCoal Resources NL                         | Exploration                    | UG          | TC                       | Project                | 100.0               | 94                | 94                           | na                                       | na       | 0.38                |
| Dec 09              | Byerwen project (Q Coal)               | JFS Steel                                   | Pre development                | OC          | CC                       | Project                | 20.0                | 611               | 3,053                        | na                                       | na       | 4.70 <sup>(6)</sup> |
| Nov 09              | Maules Creek                           | Aston Resources                             | Pre-development                | OC          | SSCC, TC                 | Project                | 100.0               | 480               | 480                          | 1.75                                     | 1.75     | 1.21                |
| Nov 09              | Broughton project                      | Resource Portfolio Partners                 | Pre-development                | OC          | CC, PCI                  | Project                | 90.0                | 9                 | 9                            | na                                       | 0.38     | 0.31                |
| Oct 09              | Vickery project                        | Whitehaven Coal                             | Exploration                    | OC          | SSCC, TC                 | Project                | 100.0               | 32                | 32                           | na                                       | na       | 0.11                |
| Sep 08              | Emerald (Terasa) project (Linc Energy) | Xinwen Mining Group                         | Pre-development                | OC          | CC                       | Project                | 100.0               | 1,500             | 1,500                        | na                                       | na       | 1.76                |
| Aug 08              | Yamala (Northern Energy)               | Sojitz                                      | Exploration                    | OC / UG     | TC                       | Project                | 49.0                | 12                | 25                           | na                                       | 0.14     | 0.12                |
| May 08              | Bandanna Coal exploration properties   | Enterprise Energy                           | Exploration                    | OC          | TC                       | Project                | 100.0               | 129               | 129                          | na                                       | 7.31     | 0.20                |
| Dec 07              | Monto Coal (from Macarthur Coal)       | Noble Group                                 | Pre-development                | OC          | TC                       | Project                | 19.6                | 49                | 247                          | 21.46                                    | 3.98     | 0.93                |
| Sep 07              | Anvil Hill project (Centennial Coal)   | Xstrata Plc                                 | Pre development                | OC          | TC                       | Project                | 100.0               | 425               | 425                          | 2.74                                     | 2.29     | 0.81                |

#### Note:

- 1 Date of transaction based on the announcement date or rumoured date, whichever is earlier.
- 2 Definitions of different lifecycle terms are Pre-development – exploration complete and in pre-feasibility or feasibility stage and Exploration – exploration phase.
- 3 Definitions of different coal type terms are CC – Coking coal, PCI – pulverised coal injection coal, SHCC – semi-hard coking coal, SSCC – semi-soft coking coal and TC – thermal coal.
- 4 Enterprise value (EV) is calculated as purchase price divided by percentage interest acquired (i.e. it reflects the EV on a 100% interest basis) and allows for net debt.
- 5 It is important to note that data limitations make some of the calculation relativities unreliable (for example, some projects may have already incurred significant capital expenditure and are thus more valuable relative to others).
- 6 Considered outliers.

**Source:** LEA analysis using data from Bloomberg, Reuters, ASX announcements and company websites. na – not available.

## Appendix D

### Glossary

| Term             | Meaning                                                                                                                                                     |
|------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------|
| ABARE            | Australian Bureau of Agriculture and Resource Economics                                                                                                     |
| ad               | air dried                                                                                                                                                   |
| Anglo            | Anglo American Plc                                                                                                                                          |
| ASIC             | Australian Securities & Investments Commission                                                                                                              |
| ASX              | Australian Securities Exchange                                                                                                                              |
| BFS              | Bankable feasibility study                                                                                                                                  |
| BMA Alliance     | BHP Billiton / Mitsubishi Development Alliance                                                                                                              |
| BREE             | Bureau of Resource and Energy Economics                                                                                                                     |
| CAPM             | Capital asset pricing model                                                                                                                                 |
| CCAF             | Climate Change Action Fund                                                                                                                                  |
| CCD              | Capacity Commitment Deed                                                                                                                                    |
| Cockatoo Coal    | Cockatoo Coal Limited                                                                                                                                       |
| Corporations Act | <i>Corporations Act 2001 (Cth)</i>                                                                                                                          |
| CPRS             | Carbon Pollution Reduction Scheme                                                                                                                           |
| CS Facility      | Credit Suisse AG debt facility                                                                                                                              |
| CSN              | Crucible swelling number                                                                                                                                    |
| CY               | Calendar year                                                                                                                                               |
| daf              | dry ash free                                                                                                                                                |
| DBCT             | Dalrymple Bay Coal Terminal                                                                                                                                 |
| DCF              | Discounted cash flow                                                                                                                                        |
| EV               | Enterprise value                                                                                                                                            |
| fno              | facility not operational                                                                                                                                    |
| FOB              | Free on board                                                                                                                                               |
| FOS              | Financial Ombudsman Services Limited                                                                                                                        |
| FSG              | Financial Services Guide                                                                                                                                    |
| FY               | Financial year                                                                                                                                              |
| GAD              | Gross air dried                                                                                                                                             |
| Greatgroup       | Greatgroup Investments Limited                                                                                                                              |
| IEA              | International Energy Agency                                                                                                                                 |
| IER              | Independent expert's reports                                                                                                                                |
| IPART            | Independent Pricing and Regulatory Tribunal                                                                                                                 |
| IPO              | Initial public offering                                                                                                                                     |
| JFY              | Japanese fiscal year                                                                                                                                        |
| JORC             | Joint Ore Reserves Committee                                                                                                                                |
| Kcal             | Kilocalorie                                                                                                                                                 |
| Kg               | Kilogram                                                                                                                                                    |
| km               | Kilometres                                                                                                                                                  |
| LEA              | LonerGAN Edwards & Associates Limited                                                                                                                       |
| Master Plan      | Queensland Coal Rail Infrastructure Master Plan                                                                                                             |
| Mitsui           | Mitsui Coal Holdings Pty Limited                                                                                                                            |
| MRRT             | Mineral Resource Rent Tax                                                                                                                                   |
| Mt               | Million tonnes                                                                                                                                              |
| Mtpa             | Million tonnes per annum                                                                                                                                    |
| NCIG             | Newcastle Coal Infrastructure Group                                                                                                                         |
| Notes            | 13.37 million zero coupon notes which convert into 13.37 million shares in Stanmore Coal at a conversion price of \$0.675 per share to raise \$9.03 million |
| NPV              | Net present value                                                                                                                                           |
| NSJV             | North Surat Joint Venture                                                                                                                                   |

## Appendix D

| Term             | Meaning                                                                             |
|------------------|-------------------------------------------------------------------------------------|
| NuCoal           | NuCoal Resources Ltd                                                                |
| PCI              | Pulverised coal injection                                                           |
| PE               | Price earnings                                                                      |
| PFS              | Pre-Feasibility Study                                                               |
| Placement Shares | 40.02 million shares in Stanmore Coal at \$0.675 per share to raise \$27.01 million |
| PTG              | Policy Transition Group                                                             |
| PWCS             | Port Waratah Coal Services                                                          |
| RBA              | Reserve Bank of Australia's                                                         |
| RG 111           | ASIC Regulatory Guide 111 – <i>Content of expert reports</i>                        |
| ROM              | Run of mine                                                                         |
| RSPT             | Resource Super Profits Tax                                                          |
| SBR              | Surat Basin Rail                                                                    |
| SBRJV            | Surat Basin Rail Joint Venture                                                      |
| Sprint Capital   | Sprint Capital Partners (HK) Limited                                                |
| Stanmore Coal    | Stanmore Coal Limited                                                               |
| VWAP             | Volume weighted average price                                                       |
| WACC             | Weighted average cost of capital                                                    |
| WEXP1            | Wiggins Island Coal Export Terminal Expansion Phase 1                               |
| WEXP2            | Wiggins Island Coal Export Terminal Expansion Phase 2                               |
| WICET            | Wiggins Island Coal Export Terminal                                                 |

