RESEARCH REPORT

Farallon Resources

(FAN-T, $0.18)

Farallon Closes $5m Equity Financing

Financial Summary (C$)

(end-Dec)	Revenue (m)	CFPS	P/CF (x)	EPS	P/E (x)
2007	0.1	-0.03	nm	-0.02	nm
2008e	35.9	-0.00	nm	-0.03	nm
2009e	159.2	0.13	1.3	0.12	1.6
2010e	226.4	0.28	0.6	0.24	0.8

All figures in C$ unless otherwise noted

- Farallon recently completed a $5m equity financing to supplement its working capital as it moves towards commissioning its high grade G9 mine.
- Farallon should be in a position to commission G9 within the next 3 months. The company's enterprise value is less than the capital invested to construct G9.
- Our revised NAV is $0.86, which is down from $1.04 due to dilution and a more conservative set of operating assumptions. Our target is now $0.65 and we maintain our Buy recommendation.

Farallon Closes $5m Equity Financing

On February 26th, Farallon announced it had completed an initial closing of $5 million of the previously announced private placement financing by issuing 25m common shares at a price of $0.20. The funds will be used for working capital and general corporate purchases.

G9 Commissioning On Schedule for Q2

We expect G9 will be fully commissioned in Q2. We understand that the mine and mill have both been operating near the designed level of 1,500 tonnes per day for most of the first quarter. Additionally, the mill recoveries and concentrate grades have been steadily improving throughout the quarter. We have lowered our expectations for most parametres for the mine to take a more conservative approach in our valuation. The changes to our parameters are illustrated in Figure 1. In short, we have lowered our production and increased our cost estimates. Despite these more conservative parameters, Farallon should still be well within the lowest quartile of cash costs to produce a pound of zinc globally.

Stock Rating:

Buy

12- target (C$)	↓ $0.65
Potential ROR	261%

Company Profile

Sector	Base Metals
Ticker	FAN-T
Shares O/S, basic (m)	377.84
Shares O/S, diluted (m)	419.12
Mkt cap, basic (C$)	$68.0m
Mkt cap, FD (C$)	$75.4m

Key Metrics

NAV/sh (C$)	$0.86
Cash (C$)	$10.0m
Debt (C$)	$32.75m

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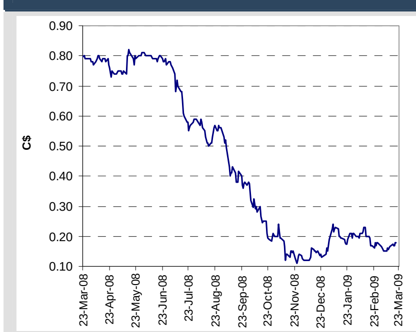
1-Year Stock Chart



03/24/09 Target lowered ($0.65)
11/21/08 Target lowered ($0.75)
10/08/09 Target lowered ($1.20)
05/21/08 FY08/09 EPS lowered, target raised ($1.25)
01/21/08 FY08-09 CFPS & target lowered ($1.15)
03/14/07 Initiating target price ($1.10)

Source: Bloomberg

Figure 1: Revised Parameters in Our Model for Farallon

		OLD			NEW		
		2009	2010	2011	2009	2010	2011
Throughput	t / day	1,525	1,700	2,000	1,450	1,700	2,000
Total Cost	$ / t	$131.3	$120.3	$115.2	$152.1	$144.1	$140.3
Net Cash Cost	$ / lb	$0.16	$0.08	$0.13	$0.19	$0.12	$0.16
Recoveries							
Zn	%	92	91	88	85	85	85
Cu	%	83	82	79	70	70	70
Pb	%	51	51	51	40	40	40
Au	%	25	25	25	42	42	42
Ag	%	32	32	32	60	60	60
Conc. Grade							
Zn	%	55.0	55.0	55.0	52.5	52.5	52.5
Cu	%	23.0	23.0	23.0	21.0	21.0	21.0
Pb	%	34.1	34.1	34.1	34.1	34.1	34.1
Production							
Zn	m lbs	123.0	130.0	142.0	108.0	122.0	138.0
Cu	m lbs	13.0	15.0	17.0	11.0	13.0	15.0
Pb	m lbs	8.0	8.0	8.0	6.0	6.0	6.0
Au	k oz	12.9	14.4	16.6	20.7	23.7	27.9
Ag	k oz	1,104	1,231	1,430	1,968	2,308	2,692

Source : Company, Paradigm Capital

Mine Life – Likely 11 Years with Potential to Double

Currently, we expect the G9 mine to have approximately 11 years of mine life at an average throughput rate of 1,900 tonnes per day. We are modelling a resource of 7.33m tonnes grading 9.1% zinc, 1.2% copper, 1.1% lead, 0.084 oz/t gold and 5.76 oz/t silver. The last published resource by Farallon consisted of 5.98m tonnes grading 7.63% zinc, 1.14% copper, 1.14% lead, 0.089 oz/t gold and 5.73 oz/t silver. However, we would note that the company has experienced significant exploration success since it last reported a resource estimate. Additionally, we believe that there remains significant upside potential to increase the tonnage at G9 above and beyond our estimates. Our resource estimate is currently close to double what the initial 43-101 estimate was back in November 2007. At that time, the company estimated the resource at 3.6m tonnes grading 8.3% zinc, 1.4% copper, 1.1% lead, 0.10 oz/t gold and 6.56 oz/t silver. We believe the resource at G9 could double again from our current estimate. In such a case, the company would likely increase the plant throughput to at least 2,500 tonnes per day. We expect Farallon could be in a position to make a decision in this regard by the end of 2009. Our rough estimate is that such an expansion could be completed with minimal capital expenditures and could increase our NAV by up to 20%.

Maintain Buy, Target Lowered

We believe the next three months will be the most critical for Farallon since its inception. Within the next three months, the company should be operating its first fully commissioned mine. We expect this could remove a huge amount of risk for investors. We would remind investors that the G9 deposit was only discovered June 6th 2005. This means that by the end of Q2, Farallon will have raised over $150m in funding (including a silver off-take agreement with Silver Wheaton), constructed and commissioned a mine and all within four years of the discovery drill hole and without ever conducting a bankable feasibility study. This is an extremely impressive feat and demonstrates the superb quality of the people driving the company. Once Farallon has turned the corner and fully commissioned G9, we expect the management will look to expand the plant's throughput level due to the tremendous exploration success it has had. If by that point, the company has not already been acquired, we believe Farallon will move to secure a second operating mine, most likely within Mexico to grow the company further.

We have adjusted our model to reflect the dilution from the most recent equity financing. Additionally, we have taken a far more conservative approach in our model. We are now expecting the G9 mine to produce 108m lbs of payable zinc in 2009. Our NAV has fallen from $1.04 to $0.86 due to the above changes, Figure 2. We are leaving our NAV multiple unchanged at 0.75x. This gives us a revised target of $0.65.

Figure 1: Revised Net Asset Value for Farallon

	US$ m	C$ m	C$/sh
OPERATING ASSETS			
G9 Campo Morado (8%DCR)	$325.0	$371.4	$0.89
Total	$325.0	$371.4	$0.89
OTHER ASSETS			
Working Capital (of which cash is $10m)	$4.4	$5.0	$0.01
Other Properties	$4.4	$5.0	$0.01
Cash from Exercise of Options and warrants	$11.1	$12.7	$0.03
Recoverable Mexican Taxes	$0.9	$1.0	$0.00
Other Investments (Marketable securities)	$0.9	$1.0	$0.00
Total	$21.6	$24.7	$0.06
TOTAL ASSETS	**$346.6**	**$396.1**	**$0.95**
LIABILITIES			
Corporate Notes @ 15%	$28.6	$25.0	$0.06
Convertible Debentures @ 7.5%	$8.9	$7.8	$0.02
Environmental/Other	$1.2	$1.3	$0.00
Long term leases	$1.4	$1.6	$0.00
Total	$40.0	$35.7	$0.09
TOTAL LIABILITIES	**$40.0**	**$35.7**	**$0.09**
NET ASSET VALUE	**$306.6**	**$360.4**	**$0.86**

Exchange Rate

US$ /C$ **1.14**

US$	2009	2010	Longterm
Zn	$0.75	$1.05	$0.80
Cu	$2.25	$2.75	$1.75
Pb	$0.75	$0.95	$0.70
Au	$875	$875	$875
AG	$5.30	$5.30	$5.30

Shares Outstanding	
Basic	**377.84**
Warrants	**5.09**
Options	**12.70**
Convertible Debs	**23.48**
Fully Diluted	**419.12**

Source : Company, Paradigm Capital

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2. David Davidson does not have an ownership position in Farallon Resources (FAN-T).
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