

Farallon Mining

(FAN-T, \$0.62)

G9 Achieves Profitability in Q4

Financial Summary (US\$)

(end-Dec)	Revenue (m)	CFPS	P/CF (x)	EPS	P/E (x)
2009	89.1	-0.01	nm	-0.04	nm
2010e	196.3	0.16	3.7	0.14	4.2
2011e	254.5	0.19	4.8	0.18	5.0

All figures in US\$ unless otherwise noted

- ▶ **Farallon continues to make progress at G9, mill availability is improving and throughput has exceeded design capacity of 1,500tpd. Mill expansion to 2,000tpd is ahead of schedule and management is now contemplating additional expansion options.**
- ▶ **Metallurgical performance continues to improve with zinc and copper recoveries increasing to 82% and 60%, respectively in Q1/10. Q4 cash costs of \$0.44/lb of zinc are expected to decline in 2010 coinciding with decreased use of outside consultants and contractors.**
- ▶ **Our revised NAV is \$1.03, which is an increase from \$0.74 based on our revised commodity price forecasts and improving throughput and recovery rates at the G9 mill. Our revised target is \$1.00 based on 1.0x our NAV. We maintain our Buy recommendation.**

Q4 Financials

The continued ramp up of operations at the G9 Mine in the fourth quarter resulted in Farallon recording positive earnings of \$0.1m (\$0.00/sh) for the first time. For the full year Farallon reported a loss of \$15.7m (\$0.04/sh). Revenue climbed in the fourth quarter as production of zinc, copper, silver and gold all increased. Net revenue in Q4 climbed 8% sequentially to \$32.3m while cash costs per pound of zinc produced remained stable at \$0.44, resulting in positive cash generated from operations \$4.4m (\$0.01/sh) in the quarter. Farallon's balance sheet continues to strengthen with cash on hand at year end climbing to \$21.6m, working capital increasing to \$14.9m and long term debt falling to \$24.3m.

G9 – Time & Focus Delivering Results

Production at the G9 mine continued to ramp up during the quarter with both throughput rates and recovery rates improving. Fourth quarter zinc production increased 6% sequentially to 23.4mlbs bringing total production for the year to 83.7mlbs. Copper production improved to 2.4mlbs in Q4 compared to 1.8mlbs in Q3.

Stock Rating:

Buy

 12- target (C\$) ↑\$1.00
 Potential ROR 61%

Company Profile

Sector	Base Metals
Ticker	FAN-T
Shares O/S, basic (m)	471.6
Shares O/S, diluted (m)	498.7
Mkt cap, basic (C\$)	\$292.4
Mkt cap, FD (C\$)	\$309.2

Key Metrics

NAV/sh (C\$)	↑\$1.03
Cash (US\$)	\$21.6m
Debt (US\$)	\$24.3m

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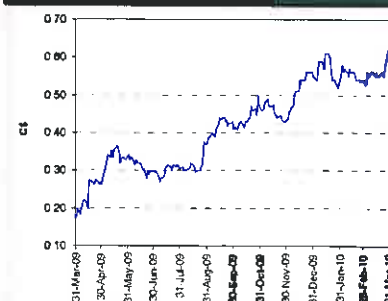
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1-Year Stock Chart



Source: Bloomberg



The mill operated above design capacity at an average of 1,552tpd during the quarter and the expansion to 2,000tpd is progressing approximately one month ahead of schedule. The strong mill performance has continued in Q1/10 with reported average throughput rates further increasing to 1,672tpd including one record day where throughput exceeded 2,400tpd. Mill recoveries have also steadily improved with zinc and copper recoveries increasing to 80% and 56%, respectively in Q4/09. Recoveries have further improved in Q1/10 and have exited the quarter averaging 84% and 68% for zinc and copper, respectively. Farallon will continue to not recover lead until zinc and copper recoveries achieve targeted recovery levels.

The strong performance of the mill in the first quarter has given management reasonable comfort that the throughput rates exceeding the 2,000tpd nameplate capacity are achievable. As such, management has initiated a study to re-evaluate the \$5.3m mill expansion budget to determine if these funds can be redeployed to achieve an even greater throughput capacity. This study is expected to be complete later this month.

Increased mill costs associated with extra staff and consultants employed during the mill expansion and higher zinc treatment charges were offset by increased by-product metal credits during the quarter, resulting in cash operating costs per pound of zinc produced remaining relatively stable at \$0.44. Cash costs are expected to decline throughout 2010 due to increasing production volumes and a decline in the use of outside consultants and contractors who were brought in to assist with the ramp up and expansion of the mill. Additionally, price participation charges associated with Farallon's zinc off-take agreements will decline approximately \$0.05/lb as a result of an increase in the base price stipulated in these contracts.

Since recommencing exploration activities at the start of Q4/09, Farallon has had good success in increasing its ore resources. On March 29, 2010 management announced an updated reserve and resource calculation for G9 which included an 18% increase in measured and indicated resources of 3.0mt grading 9.4% zinc and 1.3% copper. We are expecting additional updates on Farallon's exploration program in late April, 2010.

Maintain Buy Recommendation

We have adjusted our model to reflect the improving recovery rates at the G9 mill, and to incorporate our revised commodity price forecasts introduced in February. Our long term zinc and copper price forecasts increase to \$0.95/lb and \$2.00/lb, respectively. Consequently, our NAV increases to \$1.03/sh from \$0.74/sh and we are increasing our target price to \$1.00. We are encouraged by the progress being made with the G9 mill and expect management will ultimately target throughput rates in excess of the 2,000tpd nameplate capacity. We maintain our Buy recommendation.



Figure 1: Revised Net Asset Value for Farallon

	<u>US\$ m</u>	<u>C\$ m</u>	<u>C\$/sh</u>
OPERATING ASSETS			
G9 Campo Morado (8%DCR)	\$475.5	\$499.3	\$1.00
Total	\$475.5	\$499.3	\$1.00
OTHER ASSETS			
Working Capital (of which cash is \$21.6m)	\$14.9	\$15.6	\$0.03
Other Properties	\$15.0	\$15.8	\$0.03
Cash from Exercise of Options and warrants	\$9.0	\$9.4	\$0.02
Other Investments (Marketable securities)	\$0.0	\$0.0	\$0.00
Total	\$38.9	\$40.8	\$0.08
TOTAL ASSETS	\$514.4	\$540.1	\$1.08
LIABILITIES			
Long term debt	\$24.3	\$25.5	\$0.05
Convertible Debentures	\$0.0	\$0.0	\$0.00
Environmental/Other	\$0.6	\$0.6	\$0.00
Long term leases	\$0.0	\$0.0	\$0.00
Total	\$24.9	\$26.1	\$0.05
TOTAL LIABILITIES	\$24.9	\$26.1	\$0.05
NET ASSET VALUE	\$489.5	\$513.9	\$1.03
Exchange Rate			
US\$ /C\$	1.05		
Shares Outstanding			
Basic		472.6	
Warrants		4.2	
Options		21.9	
Convertible Debs		0.0	
Fully Diluted		498.7	

Source : Company, Paradigm Capital



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