

Farallon Mining

(FAN-\$0.32)

Positive Cash Flow in First Quarter of Commercial Production

Financial Summary (C\$)

(end-Dec)	Revenue (m)	CFPS	P/CF (x)	EPS	P/E (x)
2007	0.1	-0.02	nm	-0.03	nm
2008	35.9	-0.01	nm	-0.03	nm
2009e	120.2	0.07	5.1	0.05	7.2
2010e	213.1	0.22	1.5	0.21	1.6

All figures in C\$ unless otherwise noted

- ▶ Farallon continues to make progress at G9, mill availability is improving, metallurgical results (recoveries and concentrate grades) are improving and management is confident they can reach guidance levels.
- ▶ G9 generated positive cash flow from mining operations of \$5.7m in its first quarter of commercial production, based on current base metal prices, we should see cash flow from operations continue to grow in the second half of the year.
- ▶ Our revised NAV is \$0.78, which is down from \$0.82 based on balance sheet adjustments and changes to share capital. Our target remains \$0.80 based on 1.0x our NAV. We maintain our Buy recommendation.

Q2 Financials – First Quarter of Commercial Production

Farallon reported a Q2 net loss of \$8.0m or \$0.02 per share, excluding a non-cash foreign exchange loss of \$3.9m, the Company had a net loss of \$4.1m or \$0.01 per share. Revenues were \$20.1m compared to \$6.7m last quarter while costs of sales were \$14.4m resulting in positive cash flow from operations of \$5.7m and net operating profit of \$1.4m for the quarter. During the quarter, Farallon completed a private placement financing for gross proceeds of \$6.6m issuing 41.7m shares and a further 8.8m shares to settle debt with two of the company's suppliers. In addition, Farallon secured a \$30m, four year term loan facility with Credit Suisse (6.97% fixed rate), at June 30th, the facility had been drawn down by \$29.2m. The first payment is not due until the second half of 2010. At quarter end, cash and equivalents stood at \$13.2m and working capital was \$13.7m. After only one full quarter at commercial production the company has proven its ability to generate positive operating cash flow, with base metal prices and operations at G9 continuing to improve, we expect operating profits to grow for the remainder of the year.

Stock Rating:

Buy

12- target (C\$)	\$0.80
Potential ROR	142%

Company Profile

Sector	Base Metals
Ticker	FAN-T
Shares O/S, basic (m)	426.0
Shares O/S, diluted (m)	443.6
Mkt cap, basic (C\$)	\$140.6
Mkt cap, FD (C\$)	\$146.4

Key Metrics

NAV/sh (C\$)	\$0.78
Cash (US\$)	\$13.2m
Debt (US\$)	\$29.2m

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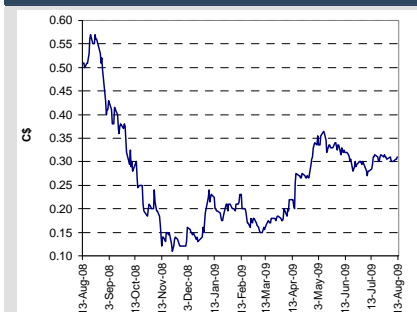
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1-Year Stock Chart



06/23/09 Target raised (\$0.80)
 03/24/09 Target lowered (\$0.65)
 11/21/08 Target lowered (\$0.75)
 10/08/09 Target lowered (\$1.20)
 03/14/07 Initiating target price (\$1.10)

Source: Bloomberg

G9 – Time & Focus Should Pay Off in Q4

Despite lingering recovery problems in the mill, a situation that requires time and focus to rectify, operations continue to show improvement. Engineering with respect to the water treatment plant is expected to take the better part of the next quarter, as a result, significant improvements to recoveries and concentrate grades are not expected until Q4 2009. The plan is to age process water in the tailings pond as opposed to recovering it in the process tank, this should allow the reagents to dissipate reducing reagent carryover and improving metallurgy. The current pumping system is not currently set-up to pull process water up to the plant and engineering work for pumping systems and pipelines will be completed during Q3.

The mine reached design of 1,500 tpd in April with production from three separate zones within the G9 ore deposit. In late June ore production came from the South East zone, which will be the source of approximately 30% - 45% of the production for the next three years. Total ore processed during the quarter was 114,644 tonnes averaging 1,260 tpd, up 7% from last quarter. Head grades and recoveries were essentially all improved over Q1. Production included 21.3m lbs of zinc, 1.7m lbs of copper, 0.6m lbs of lead, 284,350 ounces of silver and 4,400 ounces of gold.

Maintain Target and Buy Recommendation

We believe the next quarter will be critical for Farallon as engineering work continues on the water treatment plant. The results of the engineering work will not prove a success until Q4 but we anticipate the work will achieve recovery and concentrate goals.

We have adjusted our model to reflect the recent private placements, debt financing and slightly reduced output for 2009. Our NAV has been reduced from \$0.82 to \$0.78 due to the above changes and working capital adjustments, Figure 1. Our target remains \$0.80, based on approximately 1.0x our NAV.

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)	\$299.6	\$342.4	\$0.77	
Total	\$299.6	\$342.4	\$0.77	
OTHER ASSETS				
Working Capital (of which cash is \$13.2m)	\$13.7	\$15.6	\$0.04	
Other Properties	\$13.1	\$15.0	\$0.03	
Cash from Exercise of Options and warrants	\$1.6	\$4.5	\$0.01	
Other Investments (Marketable securities)	\$0.9	\$1.0	\$0.00	
Total	\$29.3	\$36.1	\$0.08	
TOTAL ASSETS	\$328.8	\$378.5	\$0.85	
LIABILITIES				
Long term debt	\$29.2	\$33.3	\$0.08	
Convertible Debentures	\$0.0	\$0.0	\$0.00	
Environmental/Other	\$0.7	\$0.8	\$0.00	
Long term leases	\$0.0	\$0.0	\$0.00	
Total	\$29.9	\$34.1	\$0.08	
TOTAL LIABILITIES	\$29.9	\$34.1	\$0.08	
NET ASSET VALUE	\$299.0	\$344.4	\$0.78	
Exchange Rate				
US\$ /C\$	1.14			
US\$	2009	2010	Longterm	Shares Outstanding
Zn	\$0.75	\$1.05	\$0.80	Basic 426.03
Cu	\$2.25	\$3.00	\$1.75	Warrants 6.59
Pb	\$0.75	\$0.95	\$0.70	Options 17.60
Au	\$925	\$925	\$925	Convertible Debs 0.00
Ag	\$5.30	\$5.30	\$5.30	Fully Diluted 443.62

Source : Company, Paradigm Capital

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