



## RealCap Uranium Research Report

# Toro Energy Limited

# Toro Energy – Strong Balance Sheet, Improved Uranium Resources

**RECOMMENDATION: BUY**

**TARGET PRICE: A\$0.21**

Toro Energy continues to be an exceptionally well-managed pre-mining uranium exploration company. The combination of a strong balance sheet, prudent financial management, institutional shareholder base and enviable reserves and permitting advancement will allow Toro Energy to participate significantly in a uranium price rerating.

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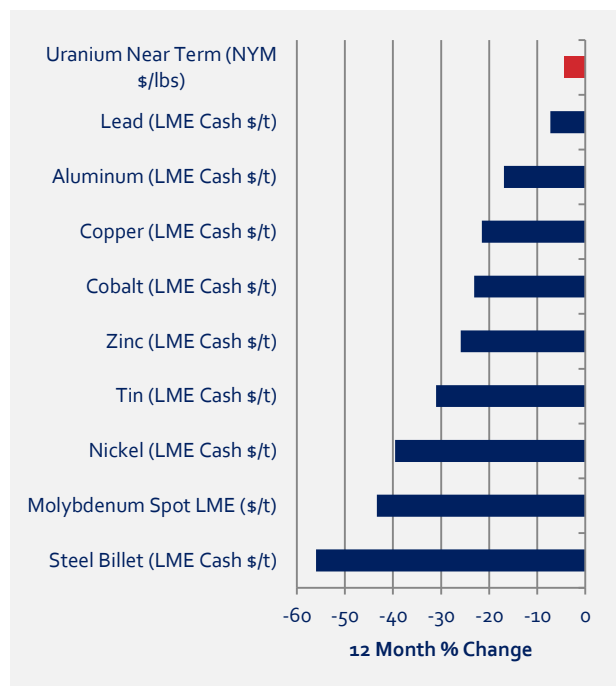
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## Industry Overview

Industrial commodity prices and those of the companies that produce them have been decimated over the last few years. Although not strictly true to compare uranium, a very specific input into the nuclear power industry, to the industrial commodity group, the market tends not to be discerning. However, when reviewing price performance over the prevailing 12 months, it can be seen from the chart below that uranium spot prices have held up remarkably well given the commodity bear market.

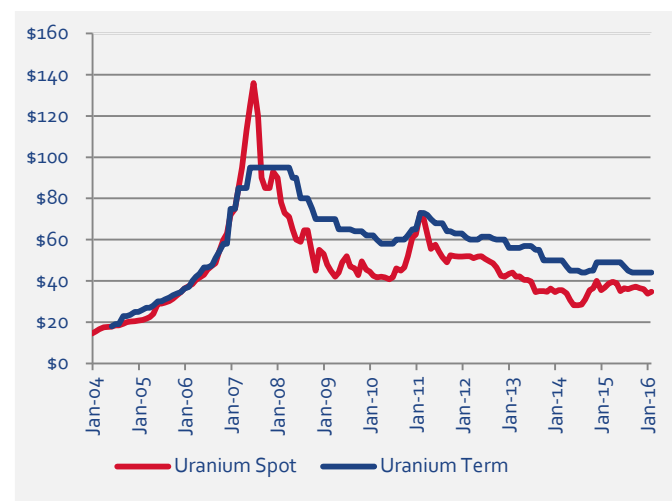
Uranium spot is the best relative performer in this industrial group, losing 4.5% over the last 12 months which is in sharp contrast to copper (-22%), zinc (-26%), nickel (-40%) and steel (-56%).

### 12 Month % Change – Industrial Metals



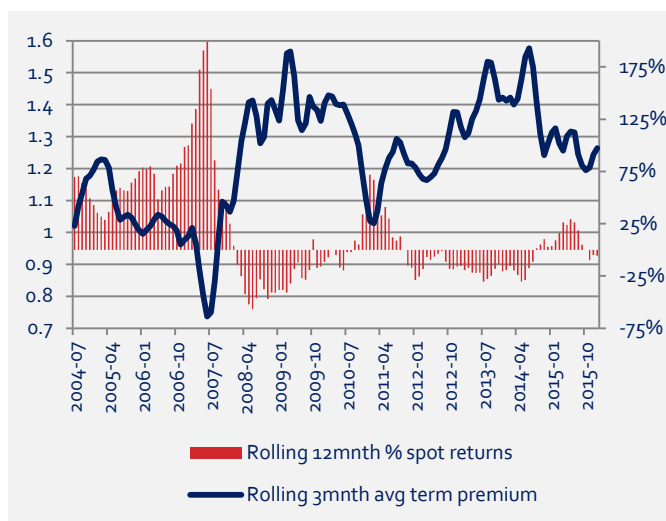
The uranium price itself has hovered around the \$36/lb mark over the last 12 months with the term price at around \$44/lb.

### Uranium Spot & Term Prices (\$/lb) – Source: Ux Consulting Company



The spot-term differential has contracted since 2014 showing a narrowing price gap between spot and term uranium prices. Historically, we have only tended to see “spectacular” price returns from uranium when spot and term price differentials have been very narrow or inverted as we experienced in 2006/07. Much of the demand behind the 2006/07 spot price, which lifted it beyond term prices, was speculative in nature and not a true reflection of the industry demand-supply dynamics. It could be argued that speculators are now out of the market and we are seeing the industry itself drive the term premium.

### Term Premium & Uranium Spot Returns



As utility providers have watched prices fall over 2013 and 2014 in particular, the deflationary environment would have lessened the pressure to contract in uranium. Why buy today when it will be cheaper tomorrow? However, nuclear fuel is a resource which is consumed and perhaps utilities now, tentatively, have to enter the spot market to meet current demand needs that they chose not to secure via a term arrangement in 2013/14.

We can see that ahead of the Fukushima disaster (March 2011) which undoubtedly sent the nuclear power industry into disarray, the term premium had fallen sharply and y/y spot prices had risen sharply.

We will continue to monitor the spot-term price dynamic over the course of 2016 as an indicator of industry demand.

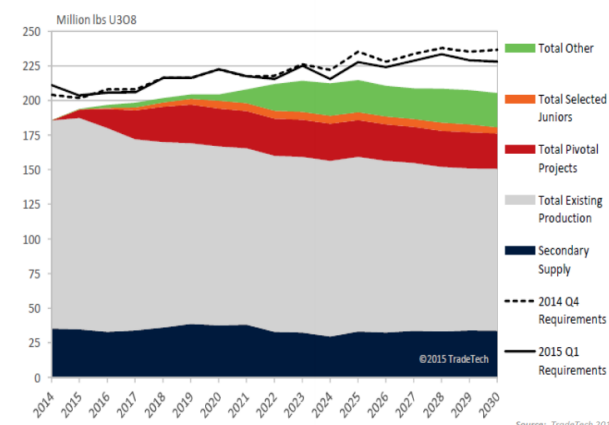
## Demand and Supply

TradeTech, an industry body, has recently published an updated demand and supply forecast for uranium. Demand for uranium to fuel nuclear reactors is estimated by assessing the current generating capacity of global reactors and by reviewing the nuclear power

reactors currently under construction and tabled to begin construction.

Uranium supply comes from a number of sources: secondary supply, current existing production and planned production.

### Uranium Demand-Supply Forecast – Source: TradeTech 2015

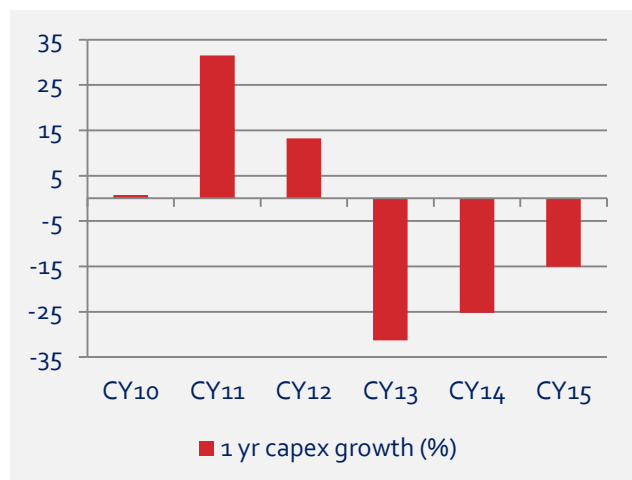


As can be seen from the TradeTech forecast, total existing production, as well as planned production, is insufficient to meet uranium demand requirements now and into the future.

A key reason for declining supply has been the current uranium price environment. Basic economics dictates that planned and prospective mines will only become operational when mining operations are not loss making and the corporate and institutional financiers that mining operations rely on, are comfortable with the creditworthiness and payback probability of their financing.

A lack of profitability with the uranium price below the production cost curve in many key uranium mining geographies has led to a sharp decline in capital expenditure. The chart below shows 1-year CapEx growth for the Global X Uranium ETF – a basket of primary uranium producers.

**1 Year CapEx Growth – Global X Uranium ETF Constituent Basket**



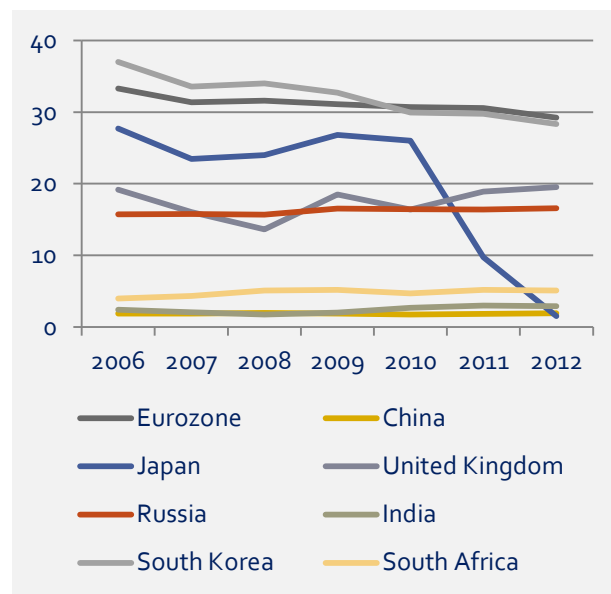
The uranium miners are not alone in the mining industry in showing a sharp decline in capital expenditures. Many prospective and planned exploration projects have been shelved, non-profitable mines mothballed and there has been non-commencement of near production miners. All of these CapEx reductions take future supply out of the uranium market. This lack of supply and the inability to instantly ramp up uranium production, enrichment and delivery – the commencement of a uranium mine is a long and convoluted regulatory and planning process – means that the risks to the uranium price are very much on the upside.

What is important to note, is that demand continues to grow for nuclear energy, particularly in the developing economies of China and India and other emerging markets.

The chart below shows the impact of Fukushima on electricity production from nuclear sources in Japan. Also visible is a declining trend in the Eurozone as a result of Germany abandoning nuclear energy generation. However, what is striking, is how little of overall electricity production comes from nuclear

sources in both China and India (less than 5%). This indicates huge scope for an increase in nuclear power in both these rapidly industrialising and urbanising nations.

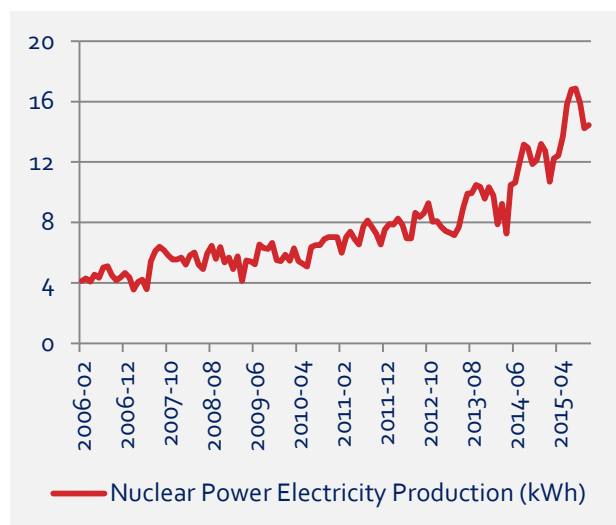
**Electricity Production from Nuclear Sources, Percent of Total**



China has 27 reactors under construction and a further 64 planned, and the scale of their nuclear programme dwarfs that of any other country.

There is undoubtedly commitment by the Chinese State Government to include nuclear energy as a key component of the country's energy mix. According to the Medium and Long-term Development Plan for Nuclear Power (2010-2020) – installed capacity should be 58 GWe by 2020 with a further 30 GWe under construction. A total of 40 GWe needs to be newly built by 2020. The Chief Engineer of the China Institute of Atomic Energy, Xu Mi, stated that nuclear energy should be the first choice for the reduction of carbon dioxide emissions in China. There is a realisation that although “green technologies” of solar and wind generated electricity are important, they cannot be relied upon for large-scale, base-load supply.

**Nuclear Power Electricity Production - China**



India has 6 reactor units under construction. Currently, nuclear energy provides only 3% of India's total electricity generation but the government has stated it intends to lift this to 25% by 2050. 22 reactor units are planned with construction due to start on two reactors in 2015 and a further 35 units are proposed. These are fairly ambitious targets by 2011's fourth largest global energy consumer (behind China, the US and Russia). Given the increasing population size and rapid urbanisation, these energy demands are likely to continue increasing.

As India has been outside the Nuclear Non-Proliferation Treaty due to its weapons programme, its civil nuclear power industry stagnated. However, this is now changing with a recent spate of international deal-making, including deals with the US, France, Russia, Kazakhstan and Australia.

Due to India's previous exclusion from the uranium market, there has been an internal focus on thorium fuelled reactor technology as India has abundant thorium reserves. However, according to the WNA country briefing on India, Indian utilities are still 15-20 years away from using thorium to a major extent as a fuel source. India is, therefore, dependent on strategic

partners to secure a supply of Uranium and their recent deal with Australia in particular builds on the Civil Nuclear Co-operation Agreement between the two countries that has been two years in the making. In addition to securing Uranium, Australian coal and gas are also to be supplied to India.

## Industry Dynamics

As discussed, the mining industry as a whole has been out of favour with investors and many companies are pricing in continued distress and bankruptcy. A large degree of the negative sentiment has been the ending of China's fixed asset binge and slowing growth. Demand-supply dynamics have been pushed out of alignment and excess supply, or perceived excess supply, in many commodities – oil, in particular, has driven down prices.

While many may argue a "lower for longer" state for oil which then makes the argument for more costly renewables less compelling, we believe the same argument cannot be made in the case of nuclear energy. As highlighted above, demand for base-load energy continues to increase and even a slowing China will impact very much at the margins of that energy requirement growth.

At the Paris United Nations Climate Conference (COP21) held in mid-December 2015, a historic deal was struck between nearly 200 countries to commit to a variety of goals and targets. Global warming on average is to be kept below two degrees compared with pre-industrial levels and greenhouse gas emissions are to stop rising and begin declining rapidly. Individual nations can decide how best to manage their compliance with these newly ratified targets and funding will be made available to help poorer countries

overhaul energy generation and industrial processes to diminish reliance on pollution-intensive fossil fuels. COP21 now has countries committed to a reduction in greenhouse gas emissions as the direct mechanism to provide further rises in global temperatures. The China Post (14 December 2015) reported:

*"The burning of those fossil fuels releases invisible greenhouse gases, which cause the planet to warm and disrupt Earth's delicate climate system. Ending the vicious circle requires a switch to cleaner sources, such as solar and wind, and improving energy efficiency. Some nations are also aggressively pursuing nuclear power, which does not emit greenhouse gases."*

In the World Energy Outlook from the IEA, they state:

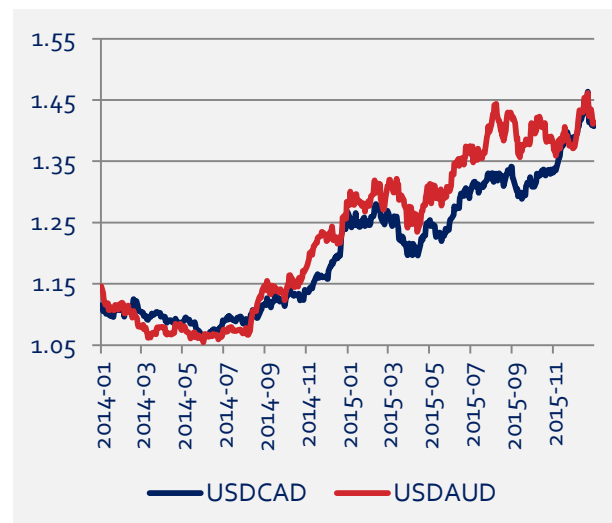
*"Nuclear power is one of a limited number of options available at scale to reduce CO<sub>2</sub> emissions. It has avoided the release of an estimated 56 Gt of CO<sub>2</sub> since 1971, or close to two years of emissions at current rates."*

Thus, while cheap fossil fuels (oil and natural gas) may make the cost per kilowatt hour of clean-air alternatives look relatively more expensive; ultimately, clean-air technology has to win out and this very much includes nuclear energy.

US Dollar strength has also been a significant factor in current market sentiment and pricing. However, US Dollar strength introduces an interesting and advantageous profile for a number of commodity producers as their cost base and operations tend to be in depreciating currency geographies. The chart below shows the move relative to the US Dollar for the Canadian and Australian Dollars – two key uranium mining jurisdictions. The competitiveness of operations in both Australia and Canada has increased improving

the margins and potential margins of mining operations.

#### Canadian and Australian Dollars relative to US Dollar



## Summary

- Uranium as a metal commodity has held up well relative to other industrial metals.
- The demand-supply imbalance continues to widen – there is insufficient existing and planned mining production to meet future energy demand.
- China, India and other emerging nations remain committed to nuclear power electricity generation.
- COP21 has served to ratify the need for clean air, base-load energy supplies.
- Foreign exchange dynamics are increasing the global competitiveness of many mining operations.



## Toro Energy

Toro Energy (ASX: TOE) is a Western Australian, Perth-based Uranium development and exploration company focussed on being a leading mid-tier global uranium company. Toro Energy has a suite of development and exploration assets within their business structure – the key flagship project being the Wiluna Project.

## Recent Announcements

On the 8th of March 2016, Toro Energy released an important announcement confirming that the revision in their available uranium resources will lead to improved processing grades to above 1 000 ppm. Work conducted on the design and optimisation of the mining pits at Centipede and Millipede, the first deposits to be mined at Wiluna, will significantly reduce mining costs. Costs reductions are achieved due to the ability to significantly reduce the total ore tonnes mined, a 36% reduction, combined with an increase in uranium that is milled.

This follows announcements made in October 2015 and February 2016 concerning the increased mineral resources. Following on from extensive geological and geochemical work, the estimated total resources at the Wiluna Project site have increased by approximately 20% together with an increase in the estimated grade of the deposit.

## Conference Call with Management

On the 19th of February, RealFin Capital Management had a one-on-one conference call with the Toro Energy executive management team including Chief Executive Officer, Vanessa Guthrie and Chief Financial Officer, Todd Alder. The purpose of the call was to provide an update on Toro Energy current activities, plans and

outlook for 2016 as well as respond to specific questions posed by RealFin Capital Management.

The highlights of that call are provided as follows.

### Mine Planning & Testing

- Toro intend to release their mine plan in 1H16
  - The revised mine plan will be based on more resource and an improved resource grade

*We have a very good understanding  
of the [Wiluna] resource | Vanessa  
Guthrie, Feb 2016*

- The revision is being conducted in two stages:
  - Benchmarking the existing plan given the new grade
  - A new plan with the improved grade metrics
- The current mine plan head grade figure is approximately 880 ppm whereas the new plan will use an updated head grade figure above 1 000ppm
- For every 100 ppm improvement in head grade, a reduction of \$2/lb in operating costs (opex) is anticipated

### Financial Management

- Currently A\$14 million cash on hand to be applied as follows:
  - Compliancy
    - Approvals
    - T.O. agreements
    - Technical studies
  - Tenements

- People
- Toro could recoup the proceeds of the loan made to Strateco (a function of the Sentient Deal)
  - Strateco have a preliminary hearing set for April 2016 (in addition to a hearing date set for January 2017)
  - Strateco are working towards an out of court settlement with the Quebec government and given recent precedence within Quebec, the probability of a settlement agreement being reached is quite high
  - Strateco need C\$50 million in order to settle with their creditors, Toro is such a creditor, and would receive the sums due for the loan and convertible note extended to Strateco
  - A settlement with the Quebec government would likely involve the return of the Matoush asset owned by Strateco

### Offtake Partners

- Update on relations in India:
  - Toro is exploring a two-pronged approach:
    - An off-take agreement with the Indian government
    - Investment by private Indian companies who will then sell to Indian government

*"India is open for business" | Vanessa Guthrie, Feb 2016*

- No other Australian uranium development miners are pursuing "India" as there is a

general perception that agreements move too slowly

- An agreement with delivery in 2022/2024 would suit Toro perfectly

### Strategic Steps and Objectives

- Cameco Corporation's (TSE: CCO) Yeelirrie asset lies just 70kms south-west of Wiluna and there would be definite synergies in a degree of cooperation and asset alignment between the two companies

*Shareholders have a long-term upside belief and are not looking to exit | Vanessa Guthrie, Feb 2016*

- Toro have been trimming exploration assets in an effort to reduce holdings rental expenses and are not looking for further exploration assets
- Toro are "keeping an eye open" for growth opportunities
  - There is consolidation within the uranium mining and while "good assets" are still being held onto; the time may come where such "good assets" are available
  - Toro will look to create leverage for themselves by considering M&A deals with companies to create a larger end-company with a greater and potentially more diverse resource base
- Vanessa Guthrie will be visiting Abu Dhabi in April 2016 and meeting with several Sovereign Wealth Funds and the nuclear energy commission

## Mineral Resources

Listed mining and minerals companies in Australia and New Zealand are obligated as part of the exchange listing rules to comply with the JORC Code. "The JORC Code provides a mandatory system for the classification of minerals Exploration Results, Mineral Resources and Ore Reserves according to the levels of confidence in geological knowledge and technical and economic considerations in Public Reports" ([www.jorc.org](http://www.jorc.org)).

Toro Energy, as a listed Australian entity complies with all aspects of the JORC code and as part of extensive geological work, has published an updated JORC resources schedule.

The estimation of the underground resources has been achieved through an extensive sample drilling programme funded by the some of the proceeds Toro Energy received from investment by the Sentient Group.

By conducting this ongoing research work, Toro Energy has been able to generate a comprehensive understanding of the grade and deposit geography of the U<sub>3</sub>O<sub>8</sub> deposits at Wiluna. This R&D work not only allows for a rigorous estimation of the mineral deposit, but also importantly allows for in-depth mining economic planning and budgeting to be conducted.

While the uranium resources have increased, so too has the grade of those resources. A high head grade means the ability to develop a high-grade mining plan which will allow for improved mining economics.

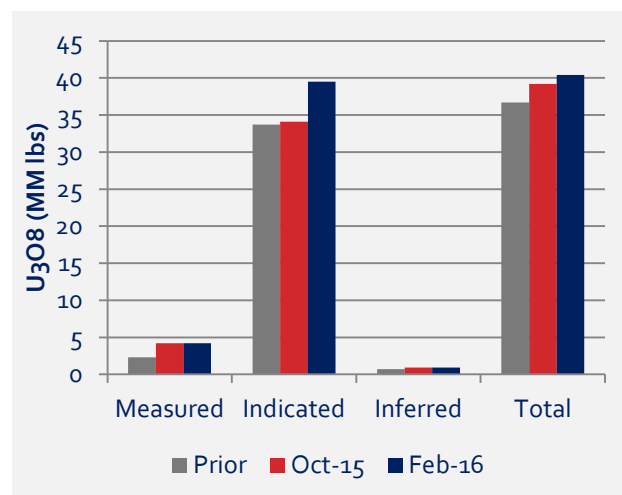
SRK Consulting (Australia), independent consultants who assisted Toro Energy in conducting the geological sampling process in conjunction with geochemical

laboratory work, are now going to assist in revising the mine optimisation plan.

The chart below indicates the change in resources at Wiluna based on sampling work conducted by Toro Energy, enhancing the resources of the Wiluna Project.

It is important to note that these figures include the Centipede/Millipede, Lake Maitland and Lake Way deposits. They exclude Dawson Hinkler and Nowthanna. As part of the recent geochemical and sampling work, a resource increase has also been advised for Nowthanna bringing the total resource inclusive of Nowthanna and Dawson Hinkler to 84.0 Mlbs at a 200 ppm cut-off.

**Wiluna Project Resources: U<sub>3</sub>O<sub>8</sub> (MM lbs), 500ppm cut-off**



## Impact on Valuation

An increase in resources, both in terms of quality and quantity allows Toro Energy to revisit the mining economics and mining schedule. Using the new resource information, Toro Energy has the ability to:

- Maintain the currently projected mine life, but effectively increase the quantity of uranium mined per year, or
- Maintain the currently projected annual output

but extend the life of the mine, or

- Work on a combination of the two – increased output and a mine life extension – in order to optimise output and longevity and thus economic value.

We have updated our DCF valuation model to account for the increased resources and have assumed an increase in production output for the Wiluna Project and improved mining economics given the higher grade of the deposits.

The CapEx requirements to commence mining operations are clearly a large driving factor in the projected NAV of the project. Our valuation model assumptions use an equal-weighted debt-equity mix for the financing of the CapEx component. An off-take contract with nuclear utility (potentially an Indian partner) could readily be used as security against debt financing. By securitising a long-term purchase contract, we believe Toro Energy will have the ability to blend their capital requirements which would be to the benefit of existing and new shareholders.

#### *Toro Energy Valuation Model Summary*

	Equity Issuance Price per Share	Future Uranium Spot Price	Toro Energy Valuation per Share
<b>Current Base Case</b>	A\$0.176	US\$55/lb	A\$0.21
<b>Prior Base Case*</b>	A\$0.148	US\$55/lb	A\$0.18
<b>Current Upper Case</b>	A\$0.288	US\$70/lb	A\$0.36
<b>Prior Upper Case*</b>	A\$0.248	US\$70/lb	A\$0.32

\* October 2015

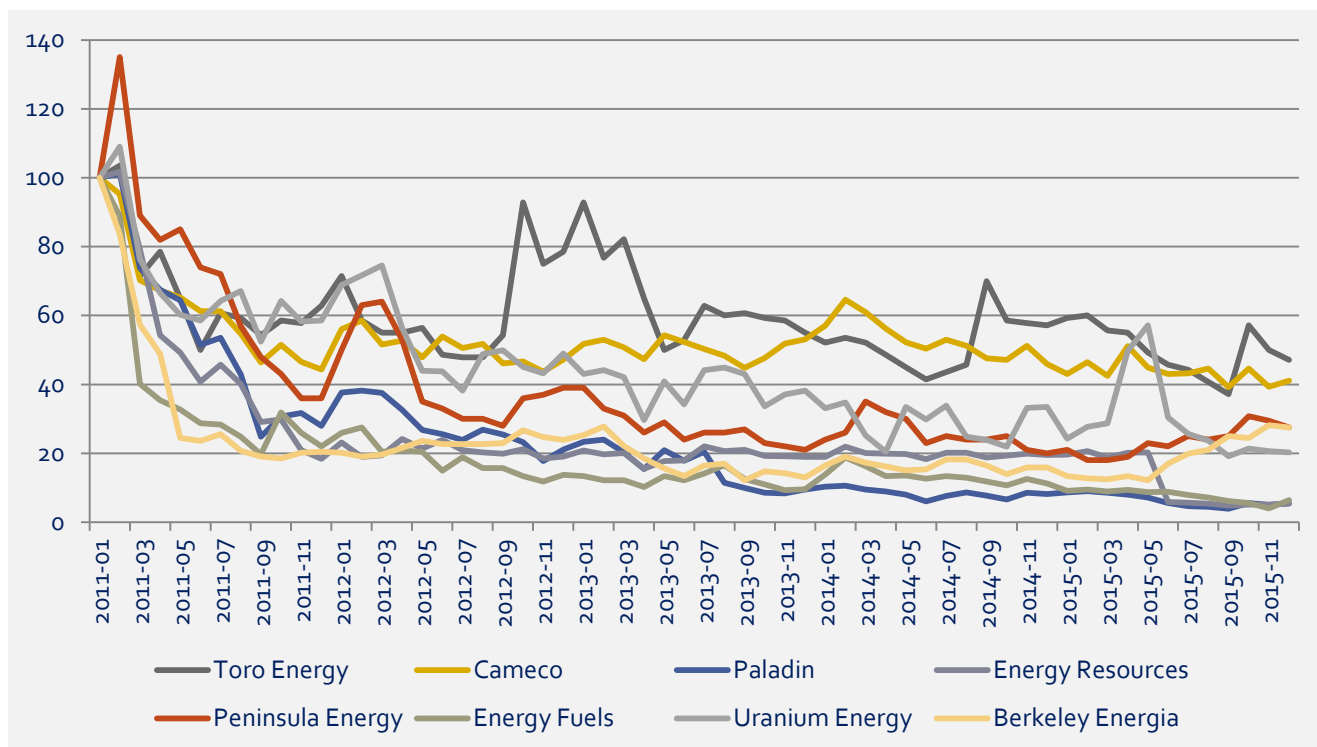
The point at which mining production will commence still remains subject to an anticipated improvement in the uranium price. Such an improvement, or perception of improvement, will put Toro Energy in a stronger negotiating position with potential off-take or financing partners.

## Share Price Performance

As discussed earlier in this report, the uranium spot price has held up well relative to other industrial metals. Equally, Toro Energy's share price has been a relative outperformer in what is a particularly volatile equity market environment, especially in the energy and mining sectors. When measured in US Dollars, Toro Energy has beaten a basket of its peers since 2011 and has behaved more like the industry heavy-weight Cameco rather than a pure exploration player. This US Dollar performance comes despite depreciation in the Australian Dollar relative to the US Dollar.

Select Uranium Mining & Exploration Companies – Indexed share price performance in US Dollars

received in December 2014 and an additional A\$2.5m



## Balance Sheet Strength

Toro Energy has made excellent progress along the regulatory and environmental path to mining commencement over the last several years, but just as importantly, the management team have paid very close attention to the Toro Energy capital structure and balance sheet.

Toro Energy has enviable balance sheet strength coupled with equity partners who are committed, long-term investors and not “hot money” speculators.

On the 4<sup>th</sup> of November 2014, Toro Energy received a cash and asset injection from The Sentient Group, an independent private equity firm specialising in the global resources industry. The Sentient Group manages of \$2.7bn in global resource assets.

In terms of the deal, Toro Energy received A\$10m in placement proceeds (A\$7.5m reflecting tranche 1

as a tranche 2 payment received in June 2015). Also received were A\$10m in unitisation funds earmarked for further development of the Wiluna project.

On the 11th of June 2015, Toro Energy announced a key balance sheet restructuring backed by The Sentient Group. In terms of the deal, Toro Energy paid down the A\$12million debt facility held with Macquarie Bank (ASX: MQG).

The post-deal balance sheet is reflected below until the end of June 2015. Updated financial figures will shortly be made available by the company.

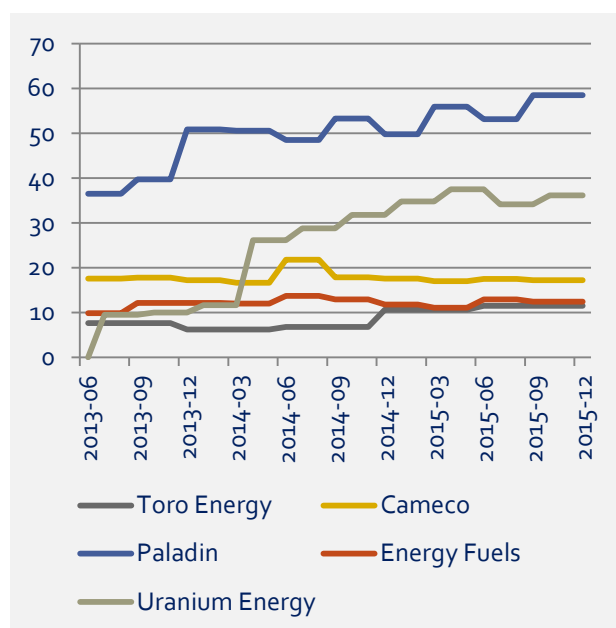
*Toro Energy Balance Sheet (Australian Dollar millions)*

	Jun '15	Dec '14	Jun '14	Dec '13	Jun '13
<b>Assets</b>					
Cash & Short-Term Investments	22.89	25.25	7.15	9.21	11.24
Short-Term Receivables	0.90	0.13	0.21	0.25	0.50
Accounts Receivables, Net	--	--	--	0.25	--
Other Current Assets	0.20	0.03	0.03	0.05	0.10
<b>Total Current Assets</b>	<b>23.99</b>	<b>25.41</b>	<b>7.39</b>	<b>9.51</b>	<b>11.84</b>
Net Property, Plant & Equipment	1.45	1.78	2.11	2.69	1.48
Total Investments and Advances	0.04	2.78	--	--	0.00
Intangible Assets	0.00	130.61	0.00	124.98	0.00
Other Assets	133.34	0.00	0.00	0.00	88.71
<b>Total Assets</b>	<b>158.82</b>	<b>160.59</b>	<b>137.56</b>	<b>137.18</b>	<b>102.04</b>
<b>Liabilities &amp; Shareholders' Equity</b>					
ST Debt & Curr. Portion LT Debt	10.96	0.00	0.00	0.00	0.00
Accounts Payable	0.53	1.35	0.24	0.96	0.76
Other Current Liabilities	0.78	0.13	0.57	1.91	0.75
<b>Total Current Liabilities</b>	<b>12.26</b>	<b>1.48</b>	<b>0.81</b>	<b>2.87</b>	<b>1.50</b>
Long-Term Debt	7.36	17.18	9.39	8.61	7.82
Provision for Risks & Charges	0.04	0.06	0.05	0.03	0.08
<b>Total Liabilities</b>	<b>19.66</b>	<b>18.72</b>	<b>10.24</b>	<b>11.50</b>	<b>9.41</b>
Common Equity	139.16	141.87	127.32	125.68	92.62
Common Stock Par/Carry Value	293.81	286.52	260.04	255.08	217.59
Retained Earnings	-160.99	-157.83	-139.19	-135.66	-131.79
Unrealized Gain/Loss Marketable Securities	0.00	1.78	0.00	0.00	0.00
Other Appropriated Reserves	6.34	11.40	6.47	6.26	6.82
Total Shareholders' Equity	139.16	141.87	127.32	125.68	92.62
<b>Total Equity</b>	<b>139.16</b>	<b>141.87</b>	<b>127.32</b>	<b>125.68</b>	<b>92.62</b>
<b>Total Liabilities &amp; Shareholders' Equity</b>	<b>158.82</b>	<b>160.59</b>	<b>137.56</b>	<b>137.18</b>	<b>102.04</b>
Book Value per Share	0.13	0.07	0.08	0.08	0.09
Tangible Book Value per Share	0.13	0.01	0.08	0.00	0.09

The key takeaway from the Sentient deal is a reduction in financing costs and a deleveraging of the Toro Energy balance sheet. This step has reduced any pressure on Toro Energy to service or refinance "expensive" debt and also provides company management with a sufficient cash reserve to keep stepping towards regulatory approval for the Wiluna Project while building on key global relationships with investment and offtake partners.

When compared with some of the uranium mining peer group, as can be seen in the chart below, Toro Energy is unleveraged relative to other exploration companies and is very conservatively structured.

**Uranium Miners Total Debt/Total Assets**



## Conclusions

## Outlook

We echo the outlook posted in earlier reports. Toro Energy continues to be an exceptionally well-managed pre-mining uranium exploration company. The combination of a strong balance sheet, prudent financial management, institutional shareholder base and enviable reserves and permitting advancement will allow Toro Energy to participate significantly in a uranium price rerating.

## Risks

There are undoubtedly risks to investing in a pre-production mining company that we presented in full in a prior publication. We give a summary of the key risks below. Where possible, Toro Energy management has sought to mitigate those risks, but investors must be aware that certain risks are inherent to uranium mining.

- Financing and economic risk
- Permitting risk
- Geology and Metallurgy
- Country risk
- Liquidity risk

## Investor Recommendations

We continue to hold a buy recommendation for Toro Energy and would encourage investors to build a position at current attractive price levels.

# RealFin Capital Partners

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