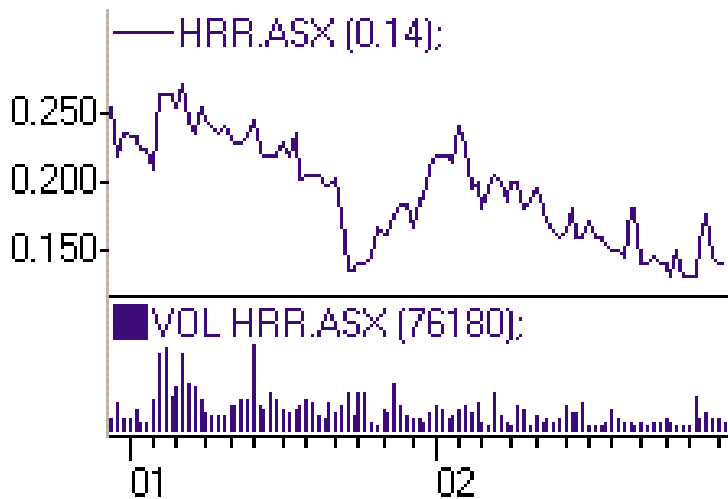


HERON RESOURCES (HRR) \$0.14

Nickel Explorer
No. Shares: 105.1m
Mkt Cap: \$14.7m
52 Week High: \$0.26

Accumulate
Avg. Monthly t/o: 0.9m
Last Reviewed SCG 287
Low: \$0.125

China to enter WA nickel industry?



The Goongarie nickel laterite project continues to be an excellent option on both the nickel price and the future of the Cawse laterite processing plant. Cawse was developed by Centaur Mining and Exploration. While it was the most technically successful of the three Western Australian dry nickel laterite developments, its small size meant there were few economies of scale, so operating costs were stubbornly high. The project quickly entered a vicious circle, where it could not generate enough surplus cash to pay for the large capital investment needed to ramp-up production and

become profitable. With the weakening nickel price two years ago, the plant soon became cash-negative. After Centaur collapsed, Cawse was sold to the OM Group, a US-based metal trader and downstream processor. Now OM is in financial trouble, and non-core assets like Cawse may be on the market. OM also owns 15% of HRR.

HRR has the high grade ore necessary to get the best returns from Cawse. Arguably, this makes Heron the natural owner of Cawse. HRR's management has not lost sight of this strategic advantage and can be expected to make a credible case to OM. Heron appears to have built some relationships with overseas nickel processing groups, particularly in China, which may assist in funding any transaction. The company and a Chinese group have been evaluating the prospects for a stand-alone development based on HRR's nickel laterite resources, however, the availability of Cawse may push these discussions to the background. Chinese smelters and metal traders are currently scouring Australia looking for sources of nickel concentrate and metal - clear evidence that the Chinese economy is powering ahead and that shortages are emerging in commodities where China has little domestic production.

It remains to be seen whether Heron can muster the firepower to mount a bid for Cawse. Despite costing over \$300m, the sale price will probably be closer to \$20-30m. Any new owner will need to invest \$300-500m to expand production, so to some extent the initial purchase is little more than a down-payment. We like HRR's resource base and its position as the natural owner of Cawse and are therefore rating the stock an accumulate.