

## HOT CHILI LTD (HCH)

### Positioned for gold exploration potential

Hot Chili Ltd has announced an exploration program at the Sierra Zapallo prospect, which has potential to host a high grade gold deposit. It is located in the southern extent of the flagship Productora copper-gold project in Chile. The Company drilled the deposit in 2012 (10<sup>th</sup> October) but focused on the copper potential. Subsequent attention has been focussed on Productora development. Sierra Zapallo has historic workings and the reefs outcrop at surface. The gold reefs are sub-vertical, and are believed to be range between 300-400m in strike length, are generally 0.5-2 metres in true width, and average over 5g/t Au. The Company intends to map the width, grade and nature of individual gold-bearing quartz veins (gold reefs) to identify drill targets. We expect drilling to commence in late August/early September.

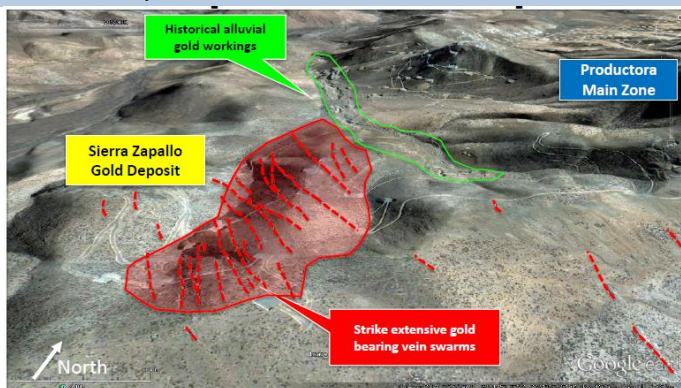
### Productora – very large, but marginal copper project

Productora is a very large copper project. The Company has a completed PFS which is modelled for average annual production of 66kt copper and 25koz gold over first 8 years of production. Our valuation is modest on expected copper projects, but as recent announcements by BHP & RIO highlight, there is a shortage of large copper projects. This suggest that at some point in the future, Productora will be an economic deposit. This probably explains the interest that CAP has in continuing to increase its exposure to Productora. On our copper price estimates, we estimate Productora would generate an average of ~US\$130m pa EBITDA, and based on capex of US\$725m, that means our valuation is low. However, using copper prices of US\$4.00/lb, we estimate EBITDA is closer to \$265m pa, and it becomes a very viable mine.

### Move to Speculative Buy (from Neutral)

Based on an 80% interest in Productora, the recent transaction (US\$60m) implies HCH is worth ~10cps, pre-tax, post debt repayment. That transaction was done when HCH was distressed, and hence we wouldn't be surprised to see future sales at higher prices. The recent capital raising removes near term risk, while the exploration potential at Sierra Zapallo suggests there is potentially a near term positive catalyst. If HCH can define a small high grade gold deposit, it would materially change the investment proposition from being based on speculation on copper prices, to being based on near term gold production earnings. We move to a Speculative Buy.

Fig. 1: Sierra Zapallo



Source: HCH

	25 Jul 2016
<b>Share Price</b>	\$0.052
<b>Valuation</b>	\$0.05
<b>Price Target (12 month)</b>	\$0.08

#### Brief Business Description:

Gold exploration. Also has very large, low grade, bulk tonne, Copper developer in Chile

#### Hartleys Brief Investment Conclusion

Gold exploration potential for high grade deposit. Copper project is very large and advanced, but marginal at current copper prices.

#### Chairman & MD

Murray Black (Chairman & Non-Exec Director)

Christian Easterday (Managing Director)

#### Top Shareholders

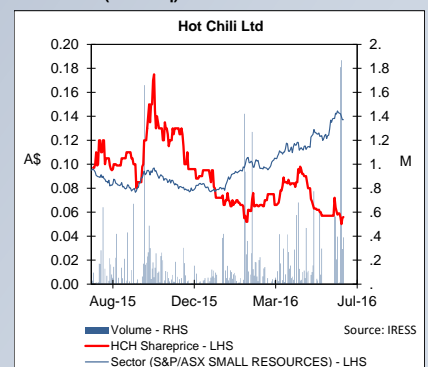
Kalgoorlie Auto Services (assoc M Black & C	15.0%
Cap S.A. (Port Finance)	14.7%
Taurus Funds Mgt	13.9%
Megeve	7.1%
Exploration Capital Partners (affil. Sprott)	5.2%
Blue Spec Sondajes Chile (assoc M Black)	4.4%

#### Company Address

First Floor, 768 Canning Highway  
Applecross, WA, 6153

<b>Issued Capital</b>	527.1m
- fully diluted	527.1m
<b>Market Cap</b>	A\$27.4m
- fully diluted	A\$27.4m
<b>Cash (30 Jun 16p)</b>	A\$3.6m
<b>Debt (30 Jun 16e)</b>	A\$9.0m
<b>EV</b>	A\$32.8m
<b>EV/Resource Cu eq lb</b>	A\$0.05/lb
<b>EV/Reserve Cu eq lb</b>	A\$0.09/lb

	Prelim. (A\$m)	FY17e	FY18e	FY19e
Prod (kt Cu Eq)	0.0	0.0	36.2	
Op Cash Flw	-4.1	-12.9	56.0	
Norm NPAT	-8.4	-26.1	25.3	
CF/Share (cps)	-1.6	-3.2	2.4	
EPS (cps)	-2.2	-4.4	3.2	
P/E	-3.3	-1.6	2.1	
	Mt	grade	Cu Eq	
<b>Resources (Mt CuEq)</b>	287	0.5%	1.5	
<b>Reserves (Mt CuEq)</b>	167	0.5%	0.8	



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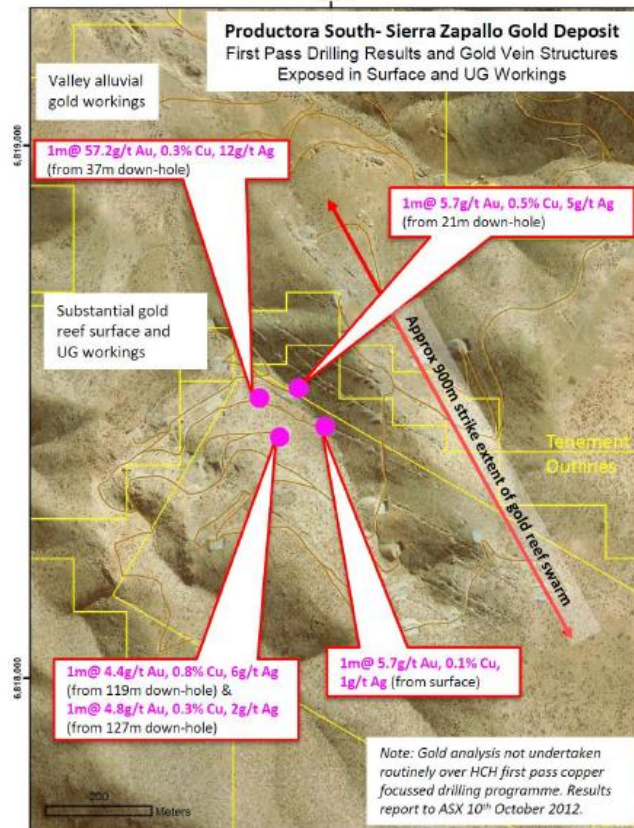
Hartleys has completed capital raisings in the past 12 months for Hot Chili Limited ("HCH") for which it has earned fees. Hartleys has provided corporate advice within the past 12 months. Analyst has a beneficial interest in HCH.asx.

## SUMMARY MODEL

Hot Chili Ltd HCH		Share Price \$0.052					Speculative Buy
<b>Key Market Information</b>							
Share Price		\$0.052					
Market Capitalisation - ordinary		A\$27m					
Net Debt (cash)		\$5m					
Market Capitalisation - fully diluted		A\$27m					
EV		A\$33m					
Issued Capital		527.1m					
Options (ITM)		0.0					
Issued Capital (fully diluted inc. all options)*		527.1m					
Issued Capital (fully diluted inc. all options and new capital)*		6583.5m					
Valuation		\$0.052					
12month price target		\$0.083					
<b>P&amp;L</b>							
	Unit	30 Jun 16	30 Jun 17	30 Jun 18	30 Jun 19	30 Jun 20	
Net Revenue	A\$m	0.0	0.0	0.0	154.1	321.2	
Total Costs	A\$m	-3.6	-3.6	-3.6	-82.1	-157.4	
EBITDA	A\$m	-3.6	-3.6	-3.6	72.0	163.8	
- margin		-	-	-	47%	51%	
Depreciation/Amort	A\$m	-0.1	-4.3	-13.2	-25.0	-28.1	
EBIT	A\$m	-3.8	-8.0	-16.8	47.0	135.7	
Net Interest	A\$m	-1.0	-0.4	-9.2	-21.7	-25.1	
Norm. Pre-Tax Profit	A\$m	-4.7	-8.4	-26.1	25.3	110.5	
Reported Tax Expense	A\$m	0.0	0.0	0.0	0.0	0.0	
Normalised NPAT	A\$m	-4.7	-8.4	-26.1	25.3	110.5	
Abnormal Items	A\$m	0.0	0.0	0.0	0.0	0.0	
Reported Profit	A\$m	-4.7	-8.4	-26.1	25.3	110.5	
Minority	A\$m	0.0	0.0	0.0	0.0	0.0	
Profit Attrib	A\$m	-4.7	-8.4	-26.1	25.3	110.5	
<b>Balance Sheet</b>							
	Unit	30 Jun 16	30 Jun 17	30 Jun 18	30 Jun 19	30 Jun 20	
Cash	A\$m	3.6	5.4	171.8	192.0	330.2	
Other Current Assets	A\$m	0.0	0.0	0.0	14.8	30.8	
Total Current Assets	A\$m	3.6	5.4	171.8	206.8	361.1	
Property, Plant & Equip.	A\$m	0.2	5.5	350.0	432.8	404.7	
Exploration	A\$m	76.5	61.6	61.6	64.6	68.6	
Investments/other	A\$m	0.0	0.0	0.0	0.0	0.0	
Tot Non-Curr. Assets	A\$m	76.7	67.2	411.7	497.4	473.3	
Total Assets	A\$m	80.3	72.6	583.5	704.2	834.4	
Short Term Borrowings	A\$m	-	-	-	-	-	
Other	A\$m	0.9	0.9	0.9	21.4	41.1	
Total Curr. Liabilities	A\$m	0.9	0.9	0.9	21.4	41.1	
Long Term Borrowings	A\$m	9.0	1.7	201.7	276.7	276.7	
Other	A\$m	-	-	-	-	-	
Total Non-Curr. Liabil.	A\$m	9.0	1.7	201.7	276.7	276.7	
Total Liabilities	A\$m	9.9	2.6	202.6	298.1	317.7	
Net Assets	A\$m	70.4	70.0	380.9	406.2	516.7	
Net Debt	A\$m	5.4	-3.7	29.9	84.7	-53.6	
<b>Cashflow</b>							
	Unit	30 Jun 16	30 Jun 17	30 Jun 18	30 Jun 19	30 Jun 20	
EBITDA	A\$m	-3.6	-3.6	-3.6	72.0	163.8	
chg in working capital	A\$m	-0.7	0.0	0.0	5.7	3.6	
Operating Cashflow	A\$m	-4.3	-3.6	-3.6	77.7	167.4	
Income Tax Paid	A\$m	0.0	0.0	0.0	0.0	0.0	
Interest & Other	A\$m	-1.0	-0.4	-9.2	-21.7	-25.1	
Operating Activities	A\$m	-5.3	-4.1	-12.9	56.0	142.2	
Property, Plant & Equip.	A\$m	7.2	5.2	-357.7	-107.8	0.0	
Exploration and Devel.	A\$m	0.0	0.0	0.0	-3.0	-4.0	
Other	A\$m	0.0	0.0	0.0	0.0	0.0	
Investment Activities	A\$m	7.2	5.2	-357.7	-110.8	-4.0	
Borrowings	A\$m	4.3	-7.3	200.0	75.0	0.0	
Equity or "tbc capital"	A\$m	0.0	8.0	336.9	0.0	0.0	
Dividends Paid	A\$m	0.0	0.0	0.0	0.0	0.0	
Financing Activities	A\$m	4.3	0.7	536.9	75.0	0.0	
Net Cashflow	A\$m	6.2	1.8	166.4	20.2	138.2	
<b>Shares*</b>							
	Unit	30 Jun 16	30 Jun 17	30 Jun 18	30 Jun 19	30 Jun 20	
Ordinary Shares - End	m	445.7	605.7	1040.2	1040.2	1040.2	
Ordinary Shares - Weighted	m	422.1	525.7	823.0	1040.2	1040.2	
Diluted Shares - Weighted	m	422.1	525.7	823.0	1040.2	1040.2	
<b>Ratio Analysis</b>							
	Unit	30 Jun 16	30 Jun 17	30 Jun 18	30 Jun 19	30 Jun 20	
Cashflow Per Share	A\$ cps	-1.3	-0.8	-1.6	5.4	13.7	
Cashflow Multiple	x	-4.1	-6.7	-3.3	1.0	0.4	
Earnings Per Share	A\$ cps	-1.1	-1.6	-3.2	2.4	10.6	
Price to Earnings Ratio	x	-4.7	-3.3	-1.6	2.1	0.5	
Dividends Per Share	AUD	-	-	-	-	-	
Dividend Yield	%	0.0%	0.0%	0.0%	0.0%	0.0%	
Net Debt / Net Debt + Equity	%	7%	-6%	7%	17%	-12%	
Interest Cover	X	na	na	na	2.2	5.4	
Return on Equity	%	na	na	na	6%	21%	
*tbc capital" could be equity or debt. Our valuation is risk-adjusted for how this may be obtained. Sources: IRESS, Company Information, Hartleys Research							
<b>Directors</b>							
Murray Black (Chairman & Non-Exec Director)			First Floor, 768 Canning Highway				
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Dr Michael Anderson (Non-Exec Director, Taurus Nom.)			+61 8 9315 5004				
Roberto Adriasola de Andraca (Non-Exec Director)			www.hotchili.net.au/				
Melanie Leighton (exec. alternate director for M Black)							
<b>Top Shareholders</b>							
Kalgoorlie Auto Services (assoc M Black & C Easterday)					15.0%		
Cap S.A. (Port Finance)					14.7%		
Taurus Funds Mgt					13.9%		
Megeve					7.1%		
Exploration Capital Partners (affil. Sprott)					5.2%		
Blue Spec Sondaies Chile (assoc M Black)					4.4%		
<b>Reserves &amp; Resources</b>							
	Mt	% Cu	Cu Kt	g/t Au	Koz	Mo ppm	
<b>TOTAL RESOURCE</b>	287.0	0.46%	1.3	0.12	1.1	111	
M&I	198.1	0.49%	1.0	0.11	0.7	130	
Inferred	88.9	0.40%	0.4	0.13	0.4	67	
<b>Productora Resource</b>	236.5	0.48%	1.14	0.10	0.73	134	
M&I	182.0	0.50%	0.91	0.10	0.59	142	
Inferred	54.5	0.42%	0.23	0.08	0.14	109	
<b>Productora Reserve</b>	166.9	0.43%	0.72	0.09	0.47	138	
- Transitional + oxide	44.6	0.44%	0.19	0.42	0.61	69	
- Fresh	122.4	0.43%	0.52	0.09	0.36	163	
<b>Frontera Resource</b>	50.5	0.37%	0.2	0.22	0.4	-	
M&I	16.1	0.38%	0.06	0.11	0.12	-	
Inferred	34.4	0.36%	0.13	0.11	0.24	-	
<b>Production Summary</b>							
	Unit	Jun 18	Jun 19	Jun 20	Jun 21		
Mill Throughput	Mt		8.9	17.5	17.5		
Mined grade	Cu%		0.5%	0.5%	0.5%		
Mined grade	g/t		0.09	0.09	0.09		
Production - Copper	Kt		32.7	70.9	70.9		
Production - payable - Copper	Kt		31.5	68.4	68.4		
Production - payable - Gold	(koz)		13.9	27.3	27.3		
Production - payable - Molybdenum	Mlbs		1.3	2.6	2.6		
Cu equiv	Kt		36.2	77.3	77.4		
Gold equiv	(koz)		165.6	346.1	346.1		
M&I Resource Conversion	%		77.6%	73.8%	72.0%		
Mine Life	yr	15.00	14.25	13.25	12.25		
Assumed inventory	Mt		222.8	205.3	187.8		
- grade Cu	%		0.5%	0.5%	0.4%		
- grade Au	g/t		0.09	0.09	0.09		
<b>Costs</b>							
	Unit	Jun 18	Jun 19	Jun 20	Jun 21		
Cost per milled tonne	\$/t		18.5	18.0	17.8		
EBITDA / tonne milled ore	\$/t		16.2	18.7	17.5		
Total Cash Costs	\$/lb Cu eq		2.06	1.85	1.83		
C1: Operating Cash Cost = (a)	\$/lb Cu eq		1.83	1.67	1.65		
(a) + Royalty = (b)	\$/lb Cu eq		1.97	1.80	1.78		
C2: (a) + depreciatn & amortisation = (c)	\$/lb Cu eq		1.47	1.37	1.38		
(c) + actual cash for development = (d)	\$/lb Cu eq		2.46	2.00	1.98		
AISC: (c) + Royalty	\$/lb Cu eq		4.61	1.72	1.70		
(d) + Royalty	\$/lb Cu eq		2.59	2.13	2.11		
	Unit	Jun 18	Jun 19	Jun 20	Jun 21		
<b>Price Assumptions</b>							
AUDUSD	A\$/US\$	0.72	0.75	0.76	0.77		
Gold	US\$/oz	1380	1380	1275	1250		
Copper	US\$/lb	2.77	2.90	2.92	2.84		
Molybdenum	US\$/lb	8.00	8.81	9.35	9.32		
<b>Hedging</b>							
		Jun 18	Jun 19	Jun 20	Jun 21		
Hedges maturing?		No	No	No	No		
<b>Sensitivity Analysis</b>							
		Valuation				0.05	
<b>Base Case</b>						110.5	
Spot Prices		0.02 (-65.5%)				55.17 (-50.1%)	
AUDUSD/AUD 0.75, Gold \$1318/oz.							
AUDUSD +/-10%		0.04 / 0.06 (-19.9% / 24.3%)				95.15 / 129.28 (-13.9% / 17.0%)	
Gold +/-10%		0.05 / 0.05 (2.8% / -2.8%)				112.68 / 108.34 (2.0% / -2.0%)	
Production +/-10%		0.08 / 0.03 (44.3% / -44.3%)				142.63 / 78.39 (28.1% / -29.1%)	
Operating Costs +/-10%		0.05 / 0.06 (-8.2% / 8.2%)				104.94 / 116.08 (-5.0% / 5.0%)	
<b>Unpaid Capital</b>							
Year Expires		No. (m)	\$m	Avg price	% ord		
30-Jun-16		0.0	0.0	0.00	0%		
30-Jun-17		0.0	0.0	0.00	0%		
30-Jun-18		0.0	0.0	0.00	0%		
30-Jun-19		0.0	0.0	0.00	0%		
30-Jun-20		0.0	0.0	0.00	0%		
<b>TOTAL</b>		0.0	0.0	0.00	0%		
<b>Share Price Valuation (NAV)</b>							
49% Productora (pre-tax NAV at disc. rate of 12%)		331				0.05	
Frontera		28				0.00	
Other Exploration		5				0.00	
Forwards		0				0.00	
Corporate Overheads		-15				0.00	
Net Cash (Debt)		-5				0.00	
Tax (NPV future liability)		0				0.00	
Options & Other Equity		0				0.00	
Hedging		0				0.00	
<b>Total</b>		343				0.052	
Last Updated: 25/07/2016							

Fig. 2: Sierra Zapallo was drilled in 2012

# High-grade Gold Drill Confirmed in 2012



- First-pass drilling by Hot Chili in 2012, where limited gold analysis was undertaken, included:

- 1m grading 57.2g/t gold, 0.3% copper and 12g/t silver from 37m down-hole, and
- 1m grading 5.7g/t gold, 0.5% copper and 5g/t silver from 21m down-hole.

- A recent review has highlighted the potential for definition of a substantial at-surface gold deposit

Source: HCH

## PRICE TARGET

Our price target has been increased to 8.3cps (from 11cps previously).

HCH Price Target Methodology	Weighting	Spot	12 mth out
NPV base case	25%	\$0.05	\$0.06
NPV at spot commodity and fx prices	5%	\$0.02	\$0.02
NPV at copper US\$4.00/lb with large dilution	5%	\$0.16	\$0.17
Net cash if sell 30.1% at implied value of \$60m (retain 49%)	5%	\$0.035	\$0.035
HCH valuation based on Productora US\$60m	50%	\$0.11	\$0.11
Net cash today	10%	\$0.00	\$0.00
<b>Risk weighted composite</b>		<b>\$0.079</b>	
<b>12 Months Price Target</b>		<b>\$0.083</b>	
Shareprice - Last		\$0.052	
<b>12 mth total return (% to 12mth target )</b>		<b>60%</b>	

Source: Hartleys Estimate

**Fig. 3: Key Assumptions and Risks for valuation**

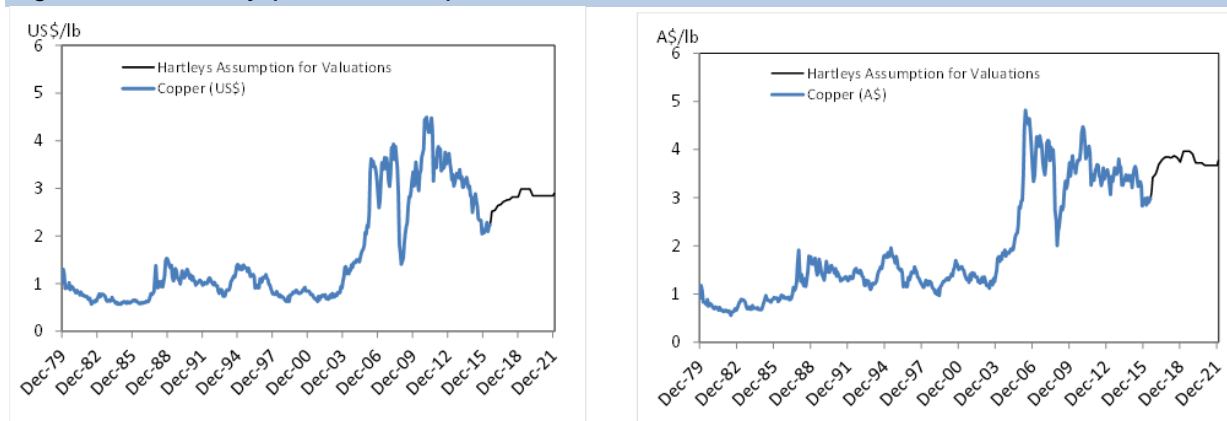
Assumption	Risk of not realising assumption	Downside risk to valuation if assumption is incorrect	Comment
~15 year mine life	Medium	Meaningful	We assume a longer mine life than the PFS, but it appears reasonable based on current resources
~17mtpa processing	Upside/downside	Moderate	We assume a high throughput
Capex slightly higher than PFS	Low	Upside / downside	We assume capex slightly higher than the PFS
Debt/equity funding	High	Upside / downside	We assume the project is mostly equity funded. More debt funding would improve our valuation
Rising copper prices	High	High	Without rising copper prices the project has minimal NPV value.
CAP deal is re-cut	High	High	We assume the CAP option agreement is not exercised
Exploration value	Moderate	Meaningful	We assume modest exploration value.

### Conclusion

Financing and copper prices are the largest risk to our valuation. We believe HCH is very high risk.

Source: Hartleys

**Fig. 4: Commodity price assumptions**



Source: Hartleys Estimates, IRESS

## RISKS

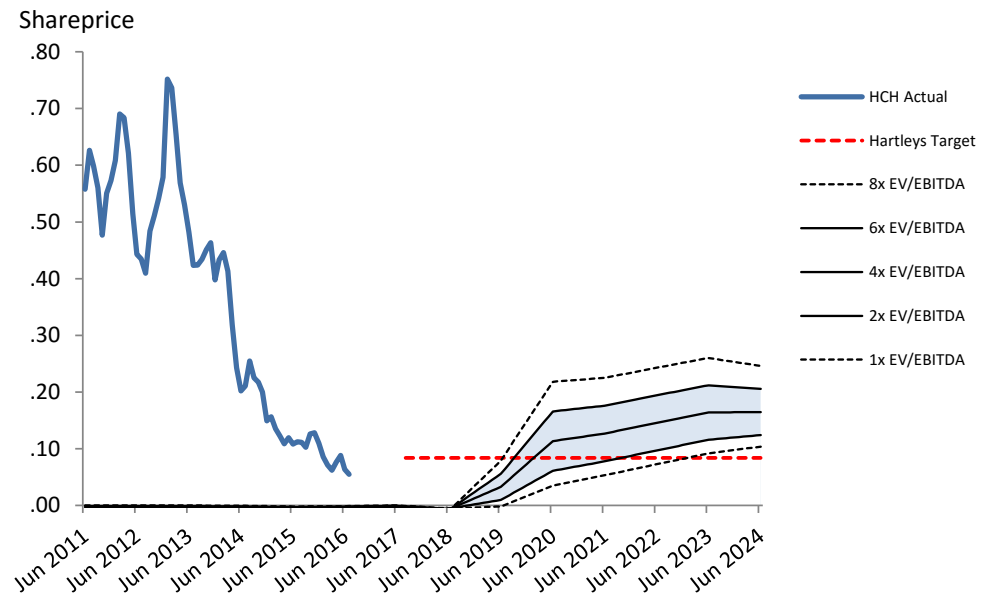
A key downside risk is that if the CMP option were not exercised, it could undermine confidence in the project. The modest net debt position is another short term risk, although it can easily be repaid if CMP exercises the Tranche 1 option.

Exploration risk at the Sierra Zapallo prospect are new risks.

Other risks for HCH are similar to most developers: attaining capital for development studies and construction, the outcomes of more detailed studies, management key-man risk, relevant government approvals, political risk, commodity prices, commissioning success and the asset performance versus nameplate design.

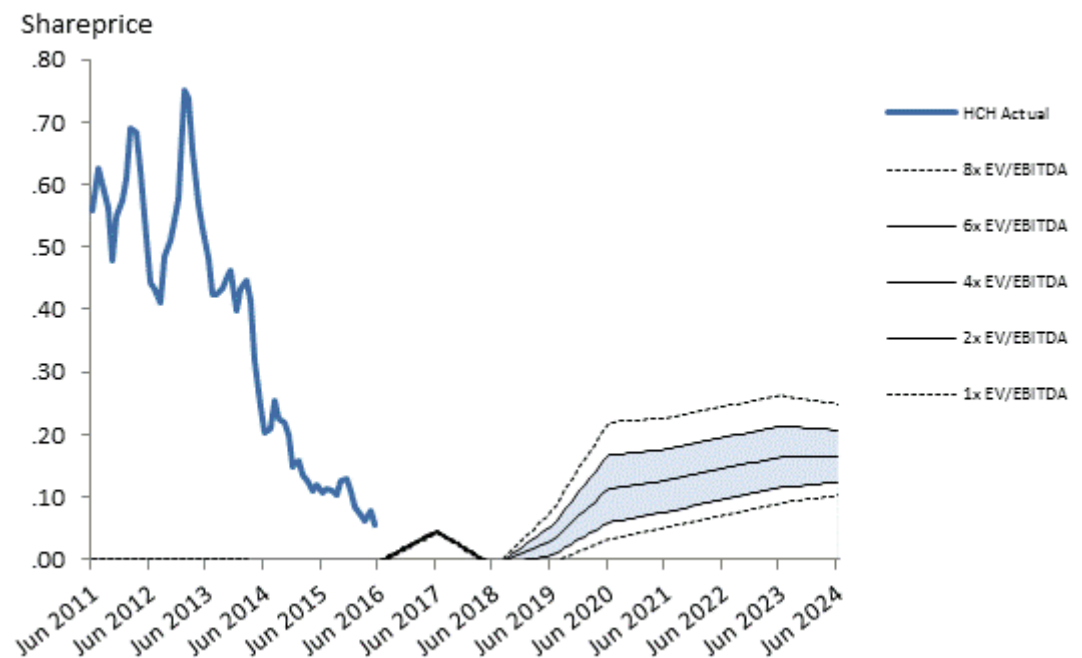
## EV/EBITDA BANDS

**Fig. 5:** Using *Hartleys base case commodity forecasts*



Source: Hartleys Estimates, IRESS

**Fig. 6:** Using *spot commodity prices*



Source: Hartleys Estimates, IRESS

# HARTLEYS CORPORATE DIRECTORY

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*Note: personal email addresses of company employees are structured in the following manner:firstname\_lastname@hartleys.com.au*

## Hartleys Recommendation Categories

Buy	Share price appreciation anticipated.
Accumulate	Share price appreciation anticipated but the risk/reward is not as attractive as a "Buy". Alternatively, for the share price to rise it may be contingent on the outcome of an uncertain or distant event. Analyst will often indicate a price level at which it may become a "Buy".
Neutral	Take no action. Upside & downside risk/reward is evenly balanced.
Reduce / Take profits	It is anticipated to be unlikely that there will be gains over the investment time horizon but there is a possibility of some price weakness over that period.
Sell	Significant price depreciation anticipated.
No Rating	No recommendation.
Speculative Buy	Share price could be volatile. While it is anticipated that, on a risk/reward basis, an investment is attractive, there is at least one identifiable risk that has a meaningful possibility of occurring, which, if it did occur, could lead to significant share price reduction. Consequently, the investment is considered high risk.

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Nathan Bray	+61 8 9268 2874
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Neil Inglis	+61 8 9268 2894
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