

16 November 2007

Metals Exploration

Price: 32.7p

BUY – Target price 45p

Upcoming Events:

Runruno drill results (1Q08)
 Waigeo Island drill results (1Q08)
 Runruno metallurgy (1Q08)
 Full-year Results (Mar 08)

Market cap	£30.0m
Ticker	MTL
Price Target (p)	45
US\$EV/Resource oz	28*
Est. cash in hand (£m)	4.0
52-week (p)	
High	46.0
Low	22.7
3M-avg. daily vol. (000s)	464
3M-avg. daily val. (£000)	172
Shares	
Basic	91.6m
Fully diluted**	97.0m
Top shareholders	
Allianz	10.7%
Williams de Broe	8.1%
Axis Framlington	7.6%
Baker Steel	7.1%
Total	33.5%

*Gold only, excluding molybdenum

**116, 144, 949 on convertible conversion

Share Price Performance (p)



Source: Fidessa

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Main Assets

Project	Resources (Moz)	Interest	Stage
Runruno Gold Project	2.03	100%	Evaluation
Waigeo Island (Ni)	-	100%*	Evaluation

*85% with option to acquire 15%, subject to 10% royalty; Source: Company data

Company Description

Focus and Strategy: AIM-listed Metals Exploration is an exploration and development company focused on the development of its flagship Runruno gold-molybdenum deposit in the Philippines. Acquired in 2005, the company rapidly defined a resource, which now stands at 2.03Moz gold and 34.4Mlbs molybdenum. Ongoing exploration is aimed at proving up a significant multi-million ounce gold resource. In July 2007 the company completed a fundraising of £4.3m in a placement at 40p, with an additional £2m convertible note. The funds are being utilised to buy out the remaining 15% minority interest in Runruno, increase exploration activity there and pursue regional corporate opportunities.

Management: Jonathan Beardsworth (CEO) is a former corporate financier with nearly 15 years' experience in mining and metals, primarily building Standard Bank's mining business in Europe and China. Gary Powell (Technical Director) is a geologist with 23 years' experience in mineral exploration, development & mining in Australia, Southeast Asia and Central Asia, as well as operational and directorship experience. Brian Lueck (Consulting Geologist) is the senior geologist on the Runruno project; he is a porphyry specialist with over 20 years of geological and corporate experience, including over ten years in the Philippines.

Project Summary

Runruno is a gold-molybdenum deposit 300km by road north of Manila. The deposit is hosted in a circular volcanic complex, analogous to the Cripple Creek complex in the US (~23Moz gold production). The resource already stands at 2Moz gold and 40Mlbs molybdenum, with significant scope for expansions. Initial metallurgical test work has been completed, with gold recovery of 94.7% achieved by gravity from pressure oxidation tests. Molybdenum is proving more problematic, but a number of promising options are being investigated. The metallurgical results will form the basis of a scoping study on a 200,000oz pa gold mine, work on which is set to commence in the new year.

Waigeo Island is a recently acquired laterite nickel deposit in Indonesia, purchased for US\$100,000 cash. The deposit has a non-JORC resource of 35Mt @ 1.5% Ni, 0.13% Co and 37% Fe. The objective is to conduct a small-scale drilling programme and commence direct shipping of ore, probably to China, in order to generate short-term cash flow, as is being

done with comparable deposits in the region managed by Rusina Mining (£38m mkt cap) and Toledo Mining (£77m mkt cap). The obvious attraction here is that cashflow should lower dilution associated with capital raising to bring Runruno into production in the future.

Runruno Gold Project						
Category	Tonnes (Mt)	Grade (g/t Au)	Grade (% Mo)	Gold (Moz)	Moly. (Mlbs)	Gold eq. (Moz)*
Indicated	5.4	2.33	0.09	0.4	10.0	0.68
Inferred	28.3	2.23	0.06	1.6	29.5	2.44
Total	28.3	2.3	0.06	2.05	39.5	3.1

*Based on US\$550/oz gold and US\$15/lb molybdenum; Source: Company data

The remainder of the company's assets are early-stage exploration projects on the island of Luzon: Puray, a copper-zinc-silver gold deposit; the Worldwide copper-gold porphyry prospect; and the Dupax zinc-copper-gold massive sulphide deposit.

Key Developments and Price Drivers

Since our review last year, the main developments have been resource upgrades in December 2006 and November 2007, increased ownership of Runruno (to 100%), encouraging metallurgical results, and the recent acquisition of the Waigeo Island laterite nickel deposit. The completion of the acquisition of rights to 100% of Runruno we view as particularly important; completion of a feasibility study and payment of US\$6m is required, but timing of this is at the company's discretion.

Looking forward, we see key price drivers as: (1) Runruno resource upgrades; (2) metallurgical test results, especially on molybdenum which is currently priced at over US\$30/lb compared with long-term prices of <US\$5/lb; (3) drill results from Waigeo Island; and (4) drill results from near-mine targets in the Runruno volcanic complex. In the medium term a further prime objective will be progress feasibility studies for both gold and nickel operations. We estimate the current cash position to be of the order of £4m, such that further funding will likely be required in 1H08.

Recommendation

We are extremely positive on Runruno because news over the next six months will likely address all four of the price drivers outlined above. Resource increases are the typical mainstay of share price appreciation; with control of 100% of Runruno, Metals Ex can now focus heavily on expanding the size of the resource, which may take it over the 3Moz mark. The beauty of the assets now though is that a major re-rating is on the cards if the company can prove up metallurgical methods to capture molybdenum (1Moz gold-equivalent at US\$15/lb), or prove up the economics of the Waigeo Island project.

With so much potential upside, we believe the company's current capitalisation of US\$28/oz undervalues the assets. As such, we retain our **BUY** recommendation, and place a target price of 45p based on an EV/in-situ value of US\$40/oz. We believe a share price in excess of 55p is achievable by the end of 2008, but await results from the events discussed above.

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