11 April 2011

Ariana Resources

Year End	Revenue (£m)	PBT* (£m)	EPS* (p)	DPS (p)	P/E (x)	Yield (%)
12/08	0.0	(0.6)	(0.7)	0.0	N/A	N/A
12/09	0.0	(0.4)	(0.3)	0.0	N/A	N/A
12/10e	0.0	(0.4)	(0.1)	0.0	N/A	N/A
12/11e	0.0	(2.3)	(0.5)	0.0	N/A	N/A

Note: *PBT and EPS are normalised, excluding intangible amortisation and exceptional items.

Investment summary: Red Rabbit jumps on

We increase our valuation of Ariana to 6.15p per share based on the release of a revised scoping study on the Kiziltepe project, and the company's eventual 50% share of the Red Rabbit joint venture with partner Proccea. Although cost estimates remain unchanged since our May 2010 outlook note, the inclusion of the updated resource at Kiziltepe (released October 2010) provides greater confidence in the resource categories and increased tonnages for extraction in the final year of mining. We have also updated our long-term gold and silver prices to US$1,350/oz and US$25/oz, respectively. Consequently Ariana's shares trade at a discount of 27% to our revised valuation.

PFS to use higher gold price, therefore more gold…

A pre-feasibility study (PFS) on Red Rabbit (due H211) will incorporate much of the data within the scoping study, but will also use higher gold and silver prices of US$1,058/oz (vs US$800/oz) and US$16.57 (vs US$14/oz) respectively. This will essentially increase the amount of gold and silver to be mined. We will look to this PFS as the next catalyst to re-visit our valuation.

Red Rabbit – targeting a regional 1Moz resource

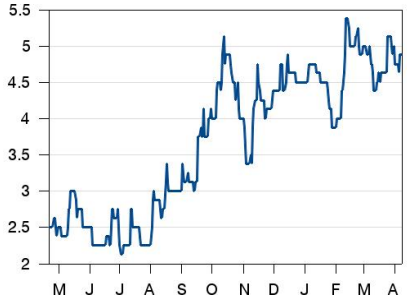
A 1Moz resource target has been set by Ariana for the Red Rabbit region. To achieve this goal Ariana recently entered into a heads of agreement (HoA) with KEFI Minerals to purchase four projects in Western Turkey for £50k in shares and a nominal cash payment. Two of these projects are strategically located close to Red Rabbit.

Valuation: Shares at 27% discount

The revised scoping study details a combined pit resource of 1.034Mt at 3.6g/t Au and 41.6g/t Ag mined over a period of 6.9 years. The current pit models have used a conservative US$800/oz base case gold price, consistent with the company's previous internal study. Unit costs and capex remain unchanged from our initial valuation (see May 2010 outlook note, *Untying the Gordian knot*). On this basis and using our long-term gold and silver prices of US$1,350/oz and US$25/oz we now value Ariana's 50% share of the Red Rabbit project at 6.15p per share.

Price	4.86p
Market Cap	£12m

Share price graph



Share details

Code	AAU
Listing	AIM
Sector	Metals and Mining
Shares in issue	250.5m

Price

52 week	High	Low
	5.4p	2.1p

Balance Sheet as at 31 December 2010e

Debt/Equity (%)	N/A
NAV per share (p)	2.6
Net cash (£m)	3.0

Business

Ariana is a gold exploration company focused on exploration and development projects in the Republic of Turkey.

Valuation

	2009	2010e	2011e
P/E relative	N/A	N/A	N/A
P/CF	N/A	N/A	N/A
EV/Sales	N/A	N/A	N/A
ROE	N/A	N/A	N/A

Geography based on revenues

UK	Europe	US	Other
0%	0%	0%	0%

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Scoping study parameters

The March 2011 scoping study has been based on the October 2010 resource update as shown in the table below.

Exhibit 1: Summary JORC resource estimate for Kiziltepe (at 1g/t Au cut-off)

Note: [1] Includes additional indicated mineralisation from the satellite Kepez prospect.
[2] Includes mineralisation classified as Inferred from the Arzu South, Arzu North, Banu and Derya veins.
[3] Includes mineralisation classified as Inferred from the subsidiary Derya West, Aybor, Arzu Far North and Ceyalan veins.

Vein	Tonnage (t)	Grade Au (g/t)	Grade Ag (g/t)	Au (oz)	Ag (oz)	Au Equiv. (oz)
Measured	782,942	4.1	51.4	103,319	1,294,836	123,311
Indicated[1]	619,029	2.3	44.8	46,496	891,368	60,258
Inferred[2]	164,998	1.8	40.9	9,752	217,005	13,101
Inferred[3]	116,000	2	51.30	5,505	191,446	8,457
Halo						
Indicated	352,819	2	25.80	18,430	293,007	22,954
Inferred	76,059	1.4	33.7	3,544	82,341	4,816
Total M&I	1,754,790	3	43.9	168,245	2,479,211	206,523
Global	2,111,847	2.8	43.7	187,046	2,970,002	232,903

Source: Ariana Resources

Consultant Wardrop, author of the scoping study, indicates that further halo material may be mined at Kiziltepe at the end of the current mine life. The amount of additional halo ore will only be known on completion of further technical studies, and likely included in the PFS.

Conventional mining at Kiziltepe

Mining at Kiziltepe will be by open-pit using conventional drill and blast techniques to liberate the rock. A total combined pit resource of 1.034Mt at 3.6g/t Au and 41.6g/t Ag is sufficient for total gold equivalent production of c 20,000 ounces per annum over a mine life of 6.9 years. Mining will be undertaken from one central pit to be developed (Arzu South) with five satellite pits (Arzu North, Banu, Derya and Kepez). An average strip ratio of 11:1 (waste:ore) has been calculated for the open pits, and reflects Kiziltepe's narrow veined ore bodies. The grade will be highest (at 4.7g/t Au and 50.9g/t Ag) in the first four years of operation to maximise cash flow followed by 2.2g/t Au and 50.9g/t Ag in year five. The lowest grade material will be stockpiled separately and processed in years six and seven at a grade of 2.1g/t Au and 28.0g/t Ag.

Processing – cheap and effective

Joint venture partner Proccea has industry expertise in developing mine process plants in Turkey and has aided Ariana in identifying a suitable method of gold and silver extraction. A simple, tried and trusted cyanidation method has been chosen to treat the ore at Kiziltepe. The total cost of the processing plant at Red Rabbit is currently reported at US$11.4m. While this is on the low side compared to other gold projects in development, the ore at Red Rabbit is not refractory. It therefore does not need an expensive roasting unit and more significantly will be built by Proccea, which has a vested interest in sourcing and constructing the plant at a cost effective rate.

As highlighted above, all unit costs for mining, processing and G&A are unchanged from our May 2010 outlook, *Untying the Gordian Knot*.

Ariana targeting 1Moz resource for Red Rabbit

The updated JORC resource (announced October 2010) now forms the back bone of the Red Rabbit project and provides a more robust mining scenario (greater resource confidence and higher tonnages in the final year of mining). Ariana plans to expand its current global 448koz AuE resource base at Red Rabbit with the intention of prolonging the mine life at Kiziltepe. To achieve this goal, Ariana will need to delineate new gold resources to replace reserves depleted as a result of mining Kiziltepe, and therefore recently entered into a heads of agreement (HoA) with KEFI Minerals to acquire four exploration projects in Western Turkey. Two of these projects are located regionally, close to the Red Rabbit project.

Terms of the agreement

The signing of the Heads of Agreement with KEFI Minerals relates to four exploration projects in Western Turkey. It includes:

- A nominal cash payment of 10,000 Turkish Lira to KEFI Minerals.
- The issue to KEFI Minerals of Ariana shares equal to a value of £50,000 based on a 30% premium to the VWAP of Ariana's shares 30 days prior to the date of the completed definitive agreement.
- The grant of a 2% net smelter royalty on all future mineral production from the four licences.

Kizilcukur – another Kiziltepe?

The Kizilcukur project, included in the heads of agreement with KEFI Minerals, is considered strategic insofar as it is located close to Red Rabbit and intended to contribute further gold resources to the operation. A total of 17 drill holes were completed at Kizilcukur by KEFI in 2007, with favourable assay results in six holes returning an average 2.2g/t Au (excluding a high grade intercept of 16.1g/t Au in hole KDTD13) and 47.6g/t Ag (excluding a high grade intercept of 327g/t Ag in hole KDTD04). The style of gold mineralisation is also comparable to that at Kiziltepe, allowing any future gold resource from the project to be treated at the planned Red Rabbit process facility. Following further due diligence as part of the HoA, Ariana will plan to recommence drilling at Kizilcukur in summer of 2011.

Muratdag – further potential to the south-east of Red Rabbit

Muratdag is another project included in the HoA with KEFI and has been highlighted as prospective for fault controlled gold-silver as well as laterite hosted nickel-cobalt. This project consists of two licences located in the Usak province of Western Turkey. Though only reconnaissance mapping and soil sampling has been undertaken previously by KEFI, a 350m x 250m undrilled gold-silver soil anomaly has been identified on the project. Ariana geologists have also interpreted there to be several geological similarities between Muratdag and its Tavsan and Demirci projects, concluding that all three lie in the same stratigraphic horizon. This latter point is significant in that this horizon is known to be regionally important for gold mineralisation.

Kiziltepe – many veins remain untested and open

Ariana also aims to expand the existing Kiziltepe resource through additional drilling on a number of vein targets including those blind to surface but traceable along strike from outcrop. It is worth noting that surface expressions of vein systems at Kiziltepe can be intermittent and not always a function of a structural break in the vein but a covering of younger rock. Such blind deposits have been identified by Ariana during previous drilling programmes and represent an opportunity to expand the Kiziltepe resource further. Additional resource drilling at Kiziltepe will follow completion of the feasibility studies at end of Q311.

Exhibit 2: Financials

£'000s	2009	2010e	2011e	2012e
Year end 31 December	IFRS	IFRS	IFRS	IFRS
PROFIT & LOSS				
Revenue	18	0	0	21,842
Cost of Sales	0	0	0	(4,341)
Gross Profit	18	0	0	17,501
EBITDA	(405)	(423)	(423)	17,078
Operating Profit (before GW and except.)	(407)	(424)	(424)	14,895
Intangible Amortisation	0	0	0	0
Exceptionals	0	0	0	0
Other	0	0	0	0
Operating Profit	(407)	(424)	(424)	14,895
Net Interest	5	18	60	76
Profit Before Tax (norm)	(402)	(406)	(364)	14,971
Profit Before Tax (FRS 3)	(402)	(406)	(364)	14,971
Tax	0	0	0	(5,240)
Profit After Tax (norm)	(402)	(406)	(364)	9,732
Profit After Tax (FRS 3)	(402)	(406)	(364)	9,731
Average Number of Shares Outstanding (m)	131.9	196.3	236.1	250.5
EPS - normalised (p)	(0.3)	(0.1)	(0.1)	1.9
EPS - FRS 3 (p)	(0.3)	(0.1)	(0.1)	1.9
Dividend per share (p)	0.0	0.0	0.0	0.0
Gross Margin (%)	N/A	N/A	N/A	80.1
EBITDA Margin (%)	N/A	N/A	N/A	78.2
Operating Margin (before GW and except.) (%)	N/A	N/A	N/A	68.2
BALANCE SHEET				
Fixed Assets	4,107	4,906	4,905	17,995
Intangible Assets	3,910	4,710	4,710	4,710
Tangible Assets	197	196	195	13,285
Investments	0	0	0	0
Current Assets	1,226	3,102	3,903	3,741
Stocks	0	0	0	1,820
Debtors	318	126	126	1,921
Cash	908	2,976	3,777	0
Current Liabilities	(450)	0	0	(357)
Creditors	(450)	0	0	(357)
Short term borrowings	0	0	0	0
Long Term Liabilities	0	0	0	(2,841)
Long term borrowings	0	0	0	(2,841)
Other long term liabilities	0	0	0	0
Net Assets	4,883	8,008	8,808	18,539
CASH FLOW				
Operating Cash Flow	(1)	(681)	(423)	13,819
Net Interest	5	18	60	76
Tax	0	0	0	(5,240)
Capex	(477)	(800)	0	(15,273)
Acquisitions/disposals	0	0	0	0
Financing	1,238	3,531	1,164	0
Dividends	0	0	0	0
Net Cash Flow	765	2,068	801	(6,618)
Opening net debt/(cash)	(143)	(908)	(2,976)	(3,777)
HP finance leases initiated	0	0	0	0
Other	0	0	0	0
Closing net debt/(cash)	(908)	(2,976)	(3,777)	2,841

Source: Edison Investment Research, company accounts

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