

Labrador Iron Mines Holdings Limited

(LIM-T C\$6.62)

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Rating: 1-Sector Outperform	Target 1-Yr: C\$14.50	ROR 1-Yr: 119.0%	Est. NTM Div. C\$0.00
Risk Ranking: Caution Warranted	2-Yr: C\$14.50	2-Yr: 119.0%	Div. (Current) C\$0.00
Valuation: 0.9x NAV (8%)			Yield 0.0%

Key Risks to Target: Commodity price, operating and technical risks, environmental and legal risks

Successful Startup Demonstrated Before Winter Event

- Labrador Iron Mines reported a loss of C\$0.13 per share in fiscal Q2/12 (July - September 2011), below our estimate of a C\$0.02 loss and the consensus estimate of a C\$0.02 loss.

Implications

- Although commercial production not yet declared, two shipments completed. Subsequent to the fiscal Q2/12 quarter, two shipments of iron ore were sold on the spot market in China. Labrador Iron Mines expects a third and possibly fourth shipment to depart before year-end.
- Seasonal operations are wrapped up for the year. The Silver Yards beneficiation plant was shuttered for the season in early November, as per the designed seasonal operation of the facility. We do not expect any material catalysts over the next few months, but we look forward to 2012, which we expect will be a milestone year for the company.
- Calendar 2011 and 2012 production and sales guidance was lowered slightly, while costs are better than expected. We have revised our estimates in accordance with the company's latest guidance.

Recommendation

- We maintain our 1-Sector Outperform rating our C\$14.50 one-year target price.

Qtly Adj EPS (FD)	Q1	Q2	Q3	Q4	Year	P/E
2010A	\$-0.01 A	\$-0.01 A	\$0.06 A	\$-0.01 A	\$0.03	n.m.
2011A	\$-0.01 A	\$-0.02 A	\$-0.02 A	\$-0.03 A	\$-0.09	n.m.
2012E	\$-0.09 A	\$-0.13 A	\$-0.02	\$-0.02	\$-0.25	n.m.
2013E	\$-0.02	\$0.70	\$0.14	\$-0.02	\$0.81	8.17
(FY-Mar.)	2009A	2010A	2011A	2012E	2013E	
Adj Earnings/Share	\$-0.01	\$0.03	\$-0.09	\$-0.25	\$0.81	
Cash Flow/Share	\$-0.01	\$-0.06	\$-0.08	\$-0.21	\$0.85	
Price/Earnings	n.m.	n.m.	n.m.	n.m.	8.2	
Revenues	\$0	\$0	\$0	\$0	\$161	
EBITDA	\$-2	\$-3	\$-5	\$-13	\$63	
Current Ratio	42.9	21.1	5.1	3.1	3.0	
IBES Estimates	BVPS12E	\$5.67				
EPS 2012E: \$0.28	NAV	\$16.33				
EPS 2013E: \$1.43	P/NAV	0.42x				



Source: Global Insight, Inc.

Capitalization	
Shares O/S (M)	54.0
Total Value (\$M)	357.8
Float O/S (M)	21.7
Float Value (\$M)	143.7

Next Reporting Date Feb-12

Pertinent Revisions

	New	Old
EPS12E	-\$0.25	-\$0.10
EPS13E	\$0.81	\$1.07

[ScotiaView Analyst Link](#)

Historical price multiple calculations use FYE prices. Source: Reuters; Company reports; Scotia Capital estimates.

Yet to Declare Commercial Production

- Labrador Iron Mines reported a loss of C\$0.13 per share in fiscal Q2/2012 (July - September 2011), below our estimate of a C\$0.02 loss and the consensus estimate of a C\$0.02 loss. The largest variance to our estimate was a C\$5.6 million (C\$0.10 per share) startup expense which consisted of non-refundable transportation-related expenses incurred prior to establishing full-scale transportation of iron ore from mine site to port. We do not expect these start-up expenses will be incurred on a recurring basis.
- **Two shipments completed to date, another one or two expected in calendar 2011.** Subsequent to the fiscal Q2/2012 quarter, two shipments (total 341,910 wet tonnes) of LIM iron ore have sailed from the Port of Sept-Îles for China where the iron ore was sold on the spot market under Labrador Iron Mines' agreement with the Iron Ore Company of Canada for the sale and shipping of all Labrador Iron Mines 2011 iron ore production. Labrador Iron Mines expects a third shipment of approximately 170,000 tonnes to depart Sept-Îles at the end of November and possibly a smaller fourth shipment to depart in December.
- **Seasonal operations are wrapped up for the year.** The Silver Yards beneficiation plant was shut down for the season in early November, in accordance with the designed seasonal operation of the facility. Ore mining operations are expected to continue during the winter months, and ore will be stockpiled for beneficiation or direct railing in the spring when weather permits.
- **The company has yet to declare commercial production at its Schefferville project.** We had previously expected that Labrador Iron Mines would declare commercial production by October 1, 2011, as per the company's previous informal guidance. However, the company does not yet consider this milestone to have been achieved. We now expect that Labrador Iron Mines likely will not declare commercial production until operations fully restart in spring 2012, and we have revised our estimates to reflect that commercial production will be declared in early Q2/13 (July - September 2012).

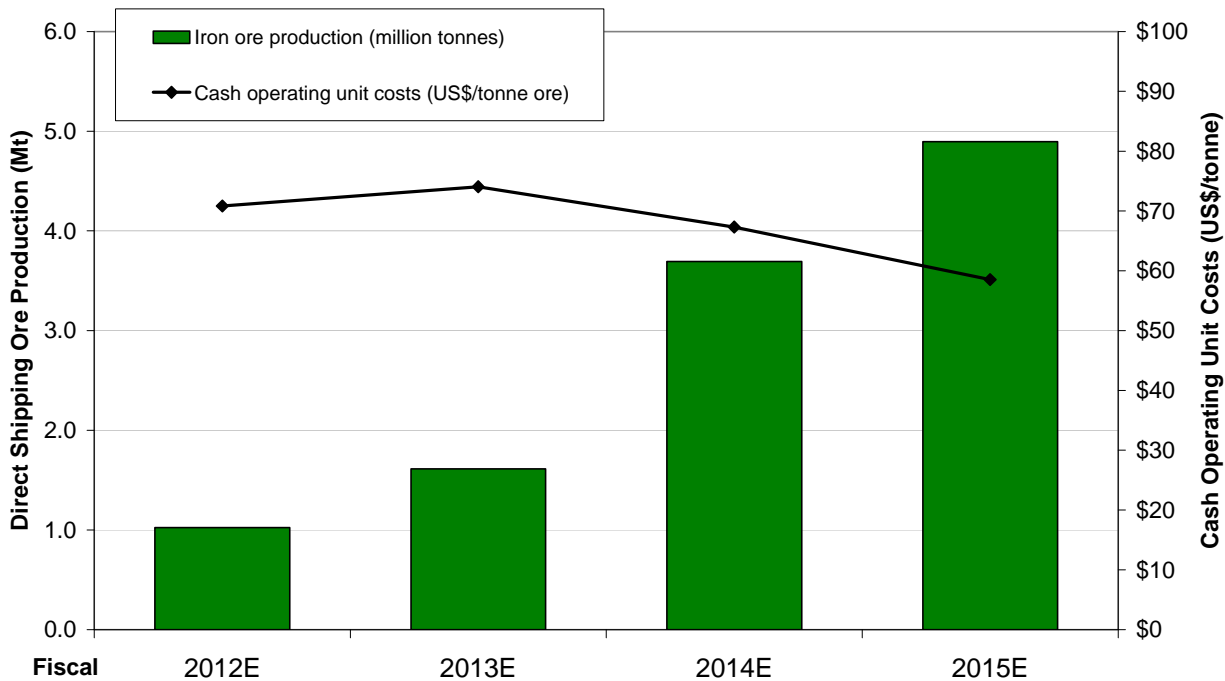
Revising 2011 and 2012 Guidance

- Labrador Iron Mines has re-released guidance for calendar 2011 and calendar 2012. Please see Exhibit 1 for an illustration of our production and sales estimates in the next one and a half years.
 - **The James Mine will produce 1.6 million tonnes raw ore, with sales of 0.6 million tonnes (clean ore) in calendar 2011.** This is down from previous guidance given in the fiscal Q1/12 earnings release, which estimated that the mine would produce 2.2Mt raw ore and would sell 0.75 - 1.0 Mt clean ore in the calendar year. We have revised our estimates to reflect the company's new guidance.
 - The difference between production and sales will be used to build an inventory stockpile, in order to ensure smooth operations on an ongoing basis and to provide material for a quick start-up in spring 2012. We believe that the company has sufficient working capital to finance the inventory build.
 - **2011 operating costs are significantly better than we had expected.** Labrador Iron Mines maintains its long-term cost guidance of C\$50/t, with initial operating unit costs higher due to lower volumes during startup. Yesterday, the company indicated specifically that costs in calendar 2011 would be approximately C\$65/t, below our previous estimate of C\$100/t. We have revised our estimate to approximately C\$80/t, which is conservatively above guidance but below our previous estimate. We note that, as Labrador Iron Mines has not yet declared commercial production, actual operating costs are not yet disclosed in the company's audited financial statements.
 - **Production is expected to be between 2.0 million and 2.5 million tonnes in calendar 2012,** from the previous estimate of 2.5 million tonnes. We have

lowered our production estimate to 2.0 million tonnes (from 2.6 million tonnes), in line with the low end of the company's guidance.

- **2012 sales guidance has dropped to 2.0 million tonnes from 2.5 million tonnes** given in fiscal Q1/2012. Sales in 2012 is expected to include 1.5 million tonnes saleable product treated through the Silver Yards beneficiation plant and an additional 0.5 million tonnes of direct railable ore from the 2011 stockpile and from 2012 mining operations.

Exhibit 1 - Labrador Iron Mines Production and Cost Profile



Source: Company reports; Scotia Capital estimates.

Modular Expansion Remains on Track

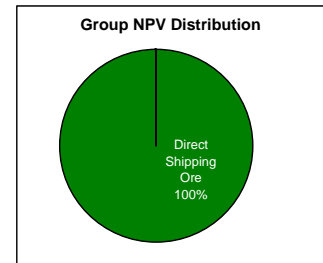
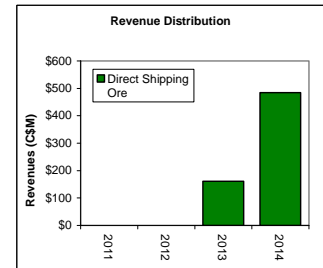
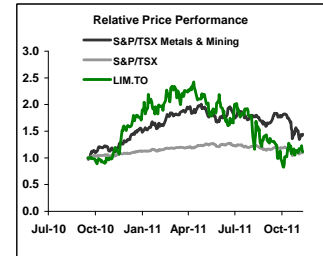
- **The second phase expansion of the Silver Yards plant was completed during fiscal Q2/12.** The company had previously indicated that the Phase 2 expansion will resolve problems with handling fine material and was expected to increase overall recoveries to about 75% (from 62%) and would increase the plant output by approximately 13% (from 1.7Mtpa).
- **Planning is well advanced for the Phase 3 extension** to increase Silver Yards' production capacity to about 2 million tonnes per year. Labrador Iron Mines expects that the planned plant expansion will be in place by mid 2012.
- The company is also evaluating the development of a separate operation for the Houston and Redmond deposits. Some mine development could take place at Houston in calendar 2012, with the first ore processed through a new Redmond plant in the second half of calendar 2013. The company envisions the new plant would have a production capacity of a further 2.5Mtpa.

Recommendation

- **We maintain our 1-Sector Outperform rating and our C\$14.50 one-year target price.** In our view, Labrador Iron Mines remains the most attractively valued iron ore-focused equity in our coverage universe. Our NAV estimate is relatively unchanged at C\$16.33 per share from C\$16.24 per share as our lower near-term production and sales estimates are largely offset by our reduced operating cost estimates. Our fiscal 2012E EPS estimate has decreased to a C\$0.25 per share loss from a C\$0.10 per share loss, largely due to incorporating the fiscal Q2/12 actual results into our assumptions.
- **We do not expect any material catalysts until spring, but 2012 should be a milestone year.** With the seasonal shuttering of operations at Silver Yards and reduced mining through the winter, we do not expect the company will report any material news or will achieve any significant catalysts over the next few months. However, we do expect that calendar 2012 will be a milestone year in the company's development, with the following anticipated events as potential share price drivers:
 - **Commercial production.** We expect that Labrador Iron Mines will declare commercial production in spring 2012.
 - **Commissioning Phase 2 expansion.** We expect that Silver Yards throughput will be improved in calendar 2012 as a result of the recently completed Phase 2 expansion.
 - **Construction of the Phase 3 extension.** We anticipate approval of the Phase 3 extension at Silver Yards, with construction completed by the end of calendar 2012.
 - **Stage 2 decision.** Labrador Iron Mines will likely start mine development on the Houston mine and Redmond beneficiation plant in late 2012.
- Please see Exhibit 2 for a valuation summary.

Exhibit 2 - Labrador Iron Mines Valuation Summary

Labrador Iron Mines (LIM.TO)	Q1/12A	Q2/12A	Q3/12E	Q4/12E	2011A	2012E	2013E	2014E	November 14, 2011
calendar	Q2 2011	Q3 2011	Q4 2011	Q1 2012					
Share data and financial ratios									
Shares outstanding - FD, weighted average (millions)	51	54	54	54	44	54	54	54	
Market capitalization, EOP (C\$ millions)	\$622	\$380	\$380	\$380	\$598	\$380	\$784	\$784	
Enterprise value, EOP (C\$ millions)	\$561	\$343	\$335	\$332	\$518	\$332	\$739	\$593	
Adj. net earnings per share - FD (C\$)	(\$0.09)	(\$0.13)	(\$0.02)	(\$0.02)	(\$0.09)	(\$0.25)	\$0.81	\$2.80	
Operating cashflow per share - FD (C\$)	(\$0.08)	(\$0.11)	(\$0.01)	(\$0.01)	(\$0.08)	(\$0.21)	\$0.85	\$2.89	
Net free cashflow per share - FD (C\$)	(\$0.50)	(\$0.86)	(\$0.21)	(\$0.33)	(\$0.43)	(\$1.87)	(\$0.37)	\$2.72	
Book value per share - FD (C\$)	\$5.39	\$4.97	\$5.31	\$5.67	\$3.97	\$5.67	\$6.82	\$9.62	
Dividend per share (C\$)	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	
Price/Earnings					n.m.	n.m.	17.9	5.2	
Price/Cash flow					n.m.	n.m.	17.1	5.0	
EV/EBITDA					n.m.	n.m.	11.7	2.7	
EBITDA margin					n.m.	n.m.	0.4	0.4	
Net debt/(Total Debt + Equity)					(0.5)	(0.2)	(0.1)	(0.4)	
ROE					-2%	-4%	12%	29%	
Dividend yield					0%	0%	0%	0%	
Key operating parameters									
Iron ore production (million tonnes)	0.1	0.2	0.5	0.0	0.04	0.68	1.61	3.69	
Iron ore sales (million tonnes)	0.0	0.0	0.5	0.4	0.00	0.95	1.61	3.69	
Benchmark iron ore Hamersley fines price (UScents/dmtu FOB)	279	275	250	230	201	259	221	195	
USD/CAD	1.03	1.02	1.08	1.09	0.98	1.05	1.06	0.96	
Average realized price (US\$/tonne)	\$0	\$0	\$0	\$0	\$0	\$0	\$105	\$126	
Unit cost of goods sold (US\$/tonne)	\$0	\$0	\$81	\$82	\$0	\$71	\$74	\$67	
Income statement (C\$ millions)									
Revenues	\$0	\$0	\$0	\$0	\$0	\$0	\$161	\$485	
Operating costs	\$0	\$0	\$0	\$0	\$0	\$0	\$93	\$259	
EBITDA	(\$4)	(\$7)	(\$1)	(\$1)	(\$5)	(\$13)	\$63	\$217	
Depreciation and amortization	\$0	\$0	\$0	\$0	\$0	\$1	\$1	\$4	
General and administration	\$1	\$0	\$1	\$1	\$4	\$3	\$3	\$8	
Other operating expenses	(\$4)	(\$6)	(\$0)	(\$0)	(\$1)	(\$11)	(\$1)	(\$1)	
Operating earnings	(\$5)	(\$7)	(\$1)	(\$1)	(\$5)	(\$14)	\$62	\$214	
Interest income (expense)	\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$0	
Other income (costs)	\$0	\$0	\$0	\$0	\$1	\$1	\$0	\$0	
Total taxes	\$0	\$0	\$0	\$0	(\$1)	\$0	\$19	\$62	
Net Earnings	(\$5)	(\$7)	(\$1)	(\$1)	(\$4)	(\$14)	\$44	\$151	
Adj. Net Earnings	(\$5)	(\$7)	(\$1)	(\$1)	(\$4)	(\$14)	\$44	\$151	
Cash flow statement (C\$ millions)									
Operating cashflow	(\$4)	(\$6)	(\$1)	(\$1)	(\$4)	(\$13)	\$45	\$156	
Cash from operating activities	(\$4)	(\$21)	(\$1)	(\$1)	(\$3)	(\$27)	\$45	\$156	
Cash from investing activities	(\$31)	(\$30)	\$8	\$4	(\$39)	(\$49)	(\$49)	(\$9)	
Cash from financing activities	\$115	\$1	\$0	\$0	\$2	\$115	\$0	\$0	
Increase (decrease) in cash	\$80	(\$50)	\$7	\$3	(\$41)	\$39	(\$4)	\$147	
Net free cashflow	(\$25)	(\$46)	(\$11)	(\$18)	(\$19)	(\$101)	(\$20)	\$147	
Balance sheet (C\$ millions)									
Cash and cash equivalents	\$88	\$38	\$45	\$48	\$8	\$48	\$45	\$191	
Other current assets	\$3	\$25	\$25	\$25	\$2	\$25	\$25	\$25	
Long-term assets	\$215	\$234	\$245	\$262	\$215	\$262	\$327	\$332	
Net debt	(\$61)	(\$37)	(\$45)	(\$48)	(\$80)	(\$48)	(\$45)	(\$191)	
Total debt and capital lease obligations	\$2	\$2	\$1	\$1	\$2	\$1	\$1	\$1	
Other liabilities	\$30	\$26	\$26	\$26	\$49	\$26	\$26	\$26	
Shareholder equity	\$274	\$268	\$287	\$307	\$174	\$307	\$369	\$520	
Net Asset Value									
Direct Shipping Ore	8%	10%							
Exploration properties	\$871	\$758							
Equity investments	\$0	\$0							
Working capital	\$49	\$49							
Total debt and capital leases	(\$1)	(\$1)							
Reclamation Obligations	\$0	\$0							
Corporate SG&A	(\$36)	(\$32)							
TOTAL NAV	\$882	\$774							
NAVPS	\$16.33	\$14.32							
Sensitivity									
fiscal 2012E	EPS	CFPS	NAVPS						
Iron Ore	n.m.	n.m.	37%						
USD/CAD	0%	0%	-28%						
Reserves/Resources (Mt)									
Measured & Indicated	39.6								
Inferred	1.3								
Rating and Target									
Rating	1-Sector Outperform								
Risk ranking	Caution warranted								
Valuation method	0.9x NAV (8%)								
1-yr Target	C\$14.50								
Share price	C\$6.80								
ROR	113%								



Source: Company reports; Reuters; Scotia Capital estimates.

[ScotiaView Analyst Link](#)

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Company	Ticker	Disclosures (see legend below)*
Labrador Iron Mines Holdings Limited	LIM	G, I, P, T, U

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Labrador Iron Mines Holdings Limited				
#	Date	Closing Price	Rating	Target-1YR
1	17-Mar-11	\$12.65	* 1-Sector Outperform	*\$20.00
2	6-Apr-11	\$14.20	Restricted	Restricted
	27-Apr-11	\$13.46	* 1-Sector Outperform	*\$18.50
3	4-Jul-11	\$12.35	1-Sector Outperform	*\$17.75
	29-Jul-11	\$10.93	1-Sector Outperform	*\$17.50
4	22-Aug-11	\$7.40	1-Sector Outperform	*\$16.00
	30-Aug-11	\$8.72	1-Sector Outperform	*\$15.00
5	26-Sep-11	\$6.45	1-Sector Outperform	*\$14.50
* represents the value(s) that has changed.				

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High

High financial and/or operational risk, low predictability of financial results, high stock volatility.

Caution Warranted

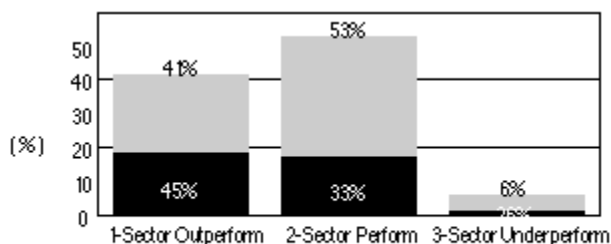
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