ABN·AMRO Morgans

Thursday 4 January 2007

Initiation of coverage

Copper Strike (CSE)

Are we there yet?

CSE is completing a feasibility study into the Einasleigh copper project, North Queensland, producing 15ktpa of copper, and is evaluating the nearby Chloe zinc deposit. We initiate coverage with a Hold recommendation and a valuation of A$0.50 per share.

Key forecasts

	FY05A	FY06A	FY07F	FY08F	FY09F
EBITDA (A$m)	-1.01	-1.10	-3.00	-3.00	45.7
Reported net profit (A$m)	-0.83	-0.95	-2.21	-2.28	23.0
Normalised net profit (A$m)[1]	-0.83	-0.95	-2.21	-2.28	23.0
Normalised EPS (c)[1]	-1.62	-1.61	-3.38	-3.49	35.3
Normalised EPS growth (%)	n/a	-0.62	110.7	3.13	n/a
Dividend per share (c)	n/a	n/a	n/a	n/a	n/a
Dividend yield (%)	n/a	n/a	n/a	n/a	n/a
Normalised PE (x)	n/m	n/m	n/m	n/m	1.42
EV/EBITDA (x)	n/m	n/m	n/m	n/m	0.65
Price/net oper. CF (x)	-115.4	-61.3	-15.5▼	-15.7▼	0.99▲
ROIC (%)	n/a	-46.0	-64.9	-56.4	54.5

1. Pre-goodwill amortisation and exceptional items
Source: Company data, ABN AMRO Morgans forecasts
Accounting Standard: IFRS

year to Jun, fully diluted

Einasleigh - 30m lb of copper per year?

Copper Strike (CSE) is evaluating development options for the high-grade (+4% Cu) underground Einasleigh deposit, in conjunction with the lower-grade (0.8% Cu) Kaiser Bill open pit deposit. A feasibility study to produce 15,000 tonnes of copper in concentrate per year is scheduled for completion in January 2007. Neither copper deposit has been closed off by drilling, and there is ample scope to increase the size of both, should this be required to improve the robustness of the development. Our valuation of A$0.50 per share incorporates a 25% discount to NPV for the Einasleigh project.

Chloe - a stand-alone zinc project?

Located 20km southwest of Einasleigh, drilling at Chloe is evaluating a zinc-lead-silver prospect. Drilling to date has intersected 6% zinc and 2% lead over widths ranging from 3m to 26m in percussion holes. The size of the resource is open, and it may prove to be a stand-alone project, justifying its own processing plant, or it may prove to be an adjunct for the Einasleigh project. The provision of power and water from Kidston, 40km south, would generate significant cash cost reductions.

Walford Creek - it's remote, but how big is it?

A higher-grade copper-lead-zinc-silver-cobalt zone was now defined in four zones within the 4km long part of the mineralised system drilled to date. Walford Creek is a large polymetallic system, and the recognition of cobalt - the Cu:Co ratio is 4:1 - is significant in terms of financial modelling. The area - 320km northwest of Mount Isa - is remote, and drilling to define a larger resource is now required.

Enough money to do the job

Copper Strike reported A$1.9m in cash at 30 September 2006 and a quarterly burn rate of A$0.8m. It raised A$2.1m with a placement of 5.9m shares at A$0.37 in December 2006. It is well funded to continue the evaluation of Einasleigh and Chloe, and to pursue exploration at its other prospects in north Queensland, northwest Queensland and Tasmania. A decision to develop Einasleigh would require debt and equity funding, or it may be achievable through a joint venture with an industry partner.

Important disclosures regarding companies that are the subject of this report and an explanation of recommendations and volatility can be found at the end of this document.

Priced at close of business 3 January 2007. Use of ▲▼ indicates that the line item has changed by at least 5%.

ABN AMRO Morgans Limited (A.B.N. 49 010 669 726) AFSL235410 A Participant of ASX Group

Hold

Important: The above recommendation has been made on a 12 month view and may not suit your investment needs or timeframe. The basis it is prepared on is summarised on the last page of this report. **PLEASE CONTACT YOUR ADVISER TO DISCUSS THIS GENERAL RECOMMENDATION BEFORE ACTING ON IT.**

N/A Volatility

Absolute performance

n/a

Short term

Materials

Australia

Price

A$0.50

Target price

A$0.50

Market capitalisation

A$32.63m (US$25.97m)

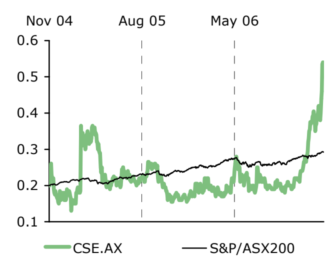
Avg (12mth) daily turnover

A$0.07m (US$0.05m)

Reuters

CSE.AX CSE70104

Price performance	(1M)	(3M)	(12M)
Price (A$)	0.39	0.20	0.19
Absolute %	28.2	150.0	170.3
Rel market %	23.2	129.4	128.5
Rel sector %	30.9	133.0	138.5



Stock borrowing: Hard onshore, Impossible offshore
Volatility (30-day): 83.31%
Volatility (6-month trend): ↓
52-week range: 0.57-0.17
S&P/ASX200: 5649.30
BBG AP Mining: 279.64

Source: ABN AMRO, Bloomberg

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Overview

At Einasleigh, 40km northeast of the now closed Kidston gold mine, CSE is completing a feasibility study into the development of the high-grade underground Einasleigh copper deposit and the open pit Kaiser Bill copper deposit, 8km to the southwest. The study is evaluating treatment through a central flotation plant to produce 15,000-25,000 tonnes per year of copper in concentrate over a five- to six-year life, and is due for completion by the end of January 2007.

It is also evaluating the Chloe zinc deposit (10km southwest of Kaiser Bill) where *Diamond Drilling* and *Reverse Circulation Drilling* to date has reported intersections of around 6% zinc and 2% lead. The objective is to establish a resource at the 6% zinc grade to justify mine development, with processing through a plant co-located with the copper-processing facility. Drilling to date is not adequate to define a resource and is expected to resume by the end of March 2007.

At Walford Creek, 320km northwest of Mount Isa, the initial drill programme by CSE defined an inferred resource of copper/zinc/lead/silver/cobalt. The area is remote, and a substantial deposit – larger than the 6.5Mt inferred resource so far established – would be required to justify the associated infrastructure. Diamond drilling will be undertaken with the objective of increasing the tonnage and better determining the grade of the deposit, and is expected to commence mid 2007.

CSE has a number of other exploration targets that it will advance in 2007. The company has raised A$2.1m with the placement of 5.9m shares at A$0.37 per share in late December 2006. The development of the Einasleigh project would likely require a further equity raising.

Einasleigh – copper in north Queensland

CSE's tenements cover 393km^2, 70km southeast of Georgetown. They incorporate EPM 13072 "Einasleigh" and EPM 12934 "Kaiser North", which comprise the Einasleigh Project, and EPM 13885 "Blackdown" EPM 13767 "Packers Creek" EPMA 14311 "Townley", which are subject to a 1.5% Net Smelter Return to BHP Billiton, capped at A$7.5m.

Einasleigh copper mine

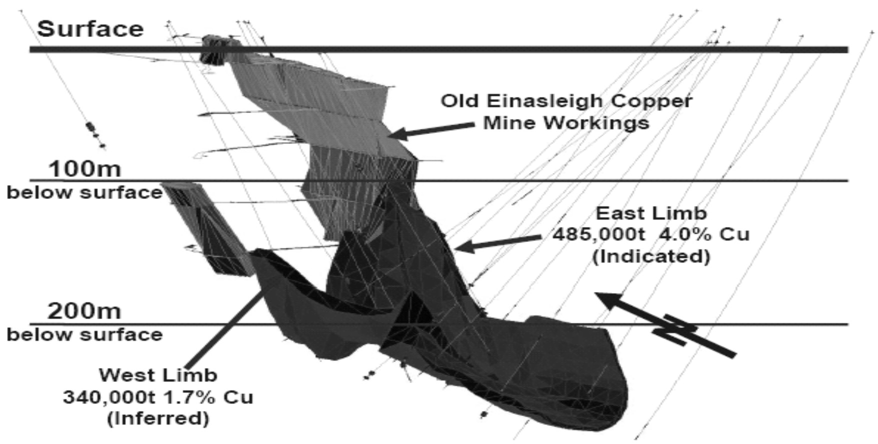
The **Einasleigh Copper Mine** is a past producer of a reported 130,000 tonnes containing about 6% Cu, 0.5g/t Au, 30g/t Ag and 1.2% Zn. It exploited a 5-20m thick high-grade lens of massive chalcopyrite-pyrrhotite-pyrite-sphalerite known as the Big Orebody. Another lens, the New Orebody, was intersected in underground development (15m at 3% Cu in a winze near the Main Shaft) and by drilling. It remained unmined with a grade of 2-3% copper. Previous drilling, and magnetic and electromagnetic surveys carried out by Teck Cominco Australia, indicated a continuation of the Big Orebody mineralisation to the south and at depth.

CSE prosecuted a drill programme to explore for extensions to the mineralisation, drilling to depth and south of the Einasleigh underground mine workings. Work to date has outlined a deposit folded along a north-south axis, cut by a cross fault. The old workings are in the area north of the cross fault and the recent drilling is in the block south of the cross structure. The higher-grade intersections – about 4% copper – are close to the keel of the fold and on the East Limb. This appears to be the offset extension of the Big Orebody – the source of historical production. The West Limb intersections are thinner and lower grade, around 2% copper, and may represent an extension of the New Orebody.

Work to date has defined an indicated resource of 485kt at 4.0% copper, 0.22g/t gold and 18g/t silver, and an additional inferred resource of 260kt at 2.1% Cu.

Drilling to date has not closed the mineralisation to the west or down plunge to the south, although it appears to be getting weaker in both directions. Of greater immediate significance, it has failed to test the structure to the north of the offsetting cross-cut fault. Success in this area could add tonnage at good grade. Of longer-term significance, geophysical anomalies with comparable signatures remain untested in the immediate area.

Figure 1 : Einasleigh copper deposit



Source: Copper Strike

Kaiser Bill copper prospect

The Kaiser Bill deposit, some 7km southwest of Einasleigh, was explored in the 1960s by MIM, and the shallow oxide copper potential was evaluated. Within the 800m strike length drilled in the 1960s, MIM reported a resource of 6.7Mt at 0.45% Cu to 90m depth. This work also identified numerous narrow intervals of higher-grade copper sulphide. Results from the two holes drilled by Teck Cominco confirmed this interpretation, with 58m at 0.86% Cu and 0.21g/t Au in KBD 01, and three intercepts of 2m each, with 1.29%, 1.15% and 0.79% copper in KBD02.

CSE completed a programme of 31 holes at Kaiser Bill to confirm the previous work and has defined an inferred resource of 13Mt at 0.80% copper, 0.13g/t gold and 6.3g/t silver. The drilling also provided samples for metallurgical testwork.

A seven-hole programme was then completed to evaluate the geotechnical conditions and mineability of the resource. The results of this work are shown in Table 1. The best hole – KBRC 081 – reported 18m at 1.26% copper. It was sited outside the initial pit shell, to the northeast of the area containing the inferred resource, and it is likely that the resource will be extended to the northeast. Drill holes 082 and 084 were drilled outside of the proposed pit.

Table 1 : Kaiser Bill drill results

Hole	From (m)	To (m)	Int (m)	%Cu	g/t Au	g/t Ag	Comments
KBRC080	10	23	13	0.42	0.05	1.7	oxide
KBRC080	23	25	2	0.80	0.27	2.6	supergene
KBRC080	27	40	13	0.60	0.09	3.3	
KBRC080	42	48	6	0.54	0.03	13.0	
KBRC081	0	23	23	0.30	0.01	4.0	oxide
KBRC081	34	52	18	1.26	0.15	7.2	
KBRC082	0	14	14	0.40	0.09	3.9	oxide
KBRC082	19	24	5	0.20	0.10	2.2	oxide
KBRC083	10	22	12	0.31	0.03	1.0	oxide
KBRC083	22	27	5	1.10	0.05	3.1	supergene
KBRC083	36	44	8	1.02	0.11	2.1	
KBRC083	47	48	1	0.81	0.09	2.3	
KBRC083	50	52	2	0.62	0.07	1.7	
KBRC083	62	64	2	1.28	0.54	4.0	
KBRC084							No significant results

Source: Copper Strike

The Einasleigh copper project

CSE is completing a feasibility study into the development of the Einasleigh and Kaiser Bill copper deposits to produce 15,000-25,000 tonnes per year of copper in concentrate. We have modelled underground mining of 100,000 tonnes per year of ore at a head grade of 4% copper – 4,000 tonnes of contained copper – from Einasleigh and the extraction of 2Mt of 0.8% copper ore – 16,000 tonnes of contained copper – from the Kaiser Bill open pit. Initial studies suggest the Kaiser Bill ore can be crushed and sorted to produce about 1Mt at 1.2% copper. This upgraded material would be blended with the Einasleigh ore and processed through a central mill to produce about 14,000 tonnes per year of copper in concentrate.

There is the potential to develop the required infrastructure at Einasleigh – water supply, power generation etc – however, grid power and water are available at Kidston, 40km south of Einasleigh. A project of sufficient scale to justify the capital cost of the connection to the Kidston infrastructure would generate substantial savings in cash operating costs, with, for example, reticulated power rather than diesel-generated electricity.

While the feasibility study will be available by end January, we think more work will be required to ensure the optimal decisions are taken with respect to the scale of the development and the infrastructure decisions, prior to commitment to development.

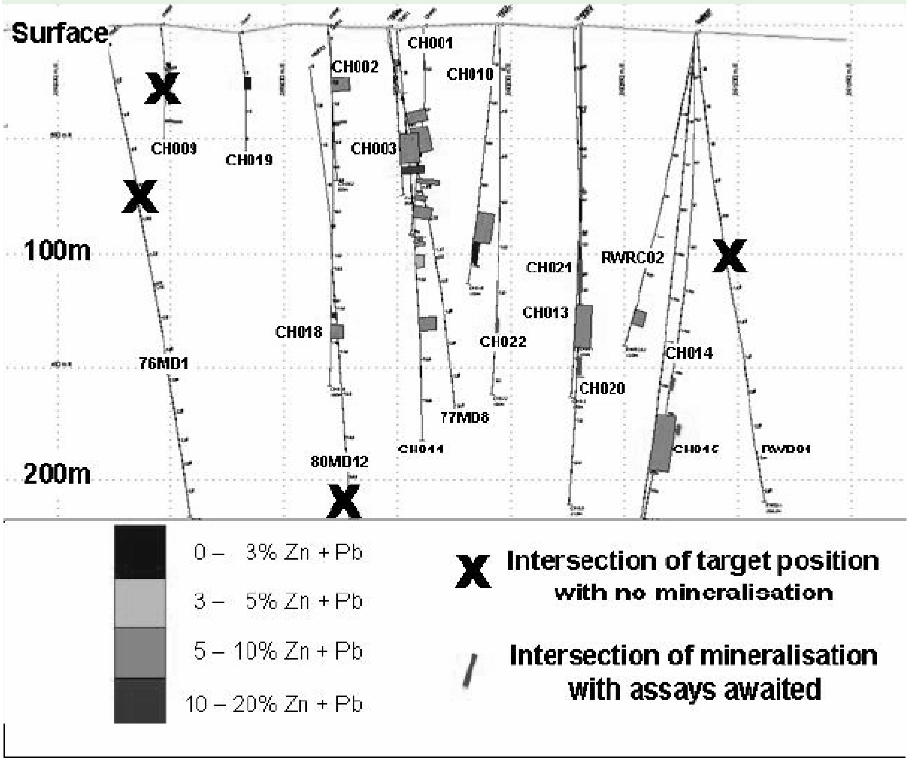
Chloe zinc

The Chloe zinc-lead-silver prospect is 20km southwest of Einasleigh. Should the evaluation of Chloe support mine development, it could be developed in tandem with the Einasleigh copper project, or it could be developed subsequently, and justify the commitment to the power/water/transport infrastructure by extending the life of the process plant.

In 2006, CSE completed a drill programme of 18 diamond and reverse circulation drill holes on Chloe, testing beneath the Chloe East, Central and West gossans. The mineralisation is structurally complex, but the results to date support the interpretation that the prospect has the potential to host a zinc-lead deposit with a grade of 5.5-6.0% zinc and 2% lead, plus 1oz/t silver.

At Chloe East, drill hole CH010 reported 8m of 6.8% Zn, 2.3% Pb and 34g/t Ag. A follow-up hole, CH013, extended the potential strike by 75m, reporting three mineralised zones – 8m at 5.22% Zn, 2.59% Pb, 3m at 5.83% Zn. 3.18% Pb, and 6m at 5.79% Zn, 4.27% Pb. Drill hole CH015 reported 26m at 6.1% Zn and 2.9% Pb at Chloe East. Three subsequent holes into Chloe East – CH021, 024 and 025 – reported intersections comparable with those in holes 010 and 013.

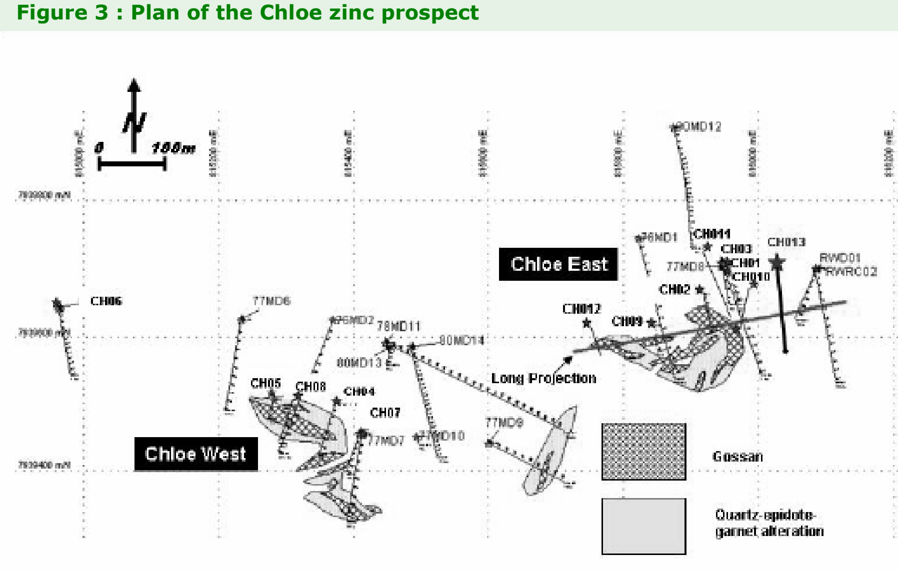
Figure 2 : Long section of Chloe East zinc prospect



Source: Copper Strike

At Chloe West, percussion holes CH023 and 029 reported 11m at 5.0% Zn, 2.5% Pb, 77.7g/t Ag, and 5m at 5.2% Zn, 2.5% Pb, 79.7g/t Ag, respectively. Preliminary interpretation suggests the mineralisation extends at least 200m along strike and to a depth of 200m

Figure 3 : Plan of the Chloe zinc prospect



Source: Copper Strike

We expect drilling to continue at Chloe early in 2007 to better define the resource and to commence metallurgical testwork.

There are a number of other prospects – Teasdale, Bloodwood Knoll – in the general area that are also prospective and where drilling is anticipated in 2007.

Walford Creek potential

In 1989, WMC discovered the Walford Creek zinc-lead deposit. Exploration included airborne EM/magnetics, a gravity survey, Sirotem EM, rock chip/soil sampling and 16.1km of drilling, consisting of 51 diamond core and 42 percussion holes on lines at 400m and 800m intervals over 4km of the 10km-long anomaly. The drilling made several ore-grade Zn-Pb intersections, with the strongest 7.5m at 6.6% Zn, 9.2% Pb and 124g/t Ag.

CSE's initial drill programme at Walford Creek tested the copper potential of the discordant, sub-vertical, 25m- to 100m-wide zone adjacent to the Fish River Fault where the previous widely spaced drilling of the 4km-long Walford Creek zinc-lead deposit by WMC intersected narrow zones of plus 1% Cu (2m at 8.2% Cu, 5m at 3.8% Cu) within broader envelopes of lower-grade mineralisation (eg, 26m at 0.96% Cu).

CSE defined an inferred resource of 6.5Mt at 0.6% Cu, 1.6% Pb, 2.1% Zn, 25g/t Ag and 0.07% Co in four separate bodies within a strike length of 3km along the Fish River structure. About half of the resource lies in the easternmost body, which is open in several directions, while the other three bodies are now completely closed off. The grade of cobalt – 0.07% – is also suspect. About 75% of the holes at Walford Creek were not analysed for cobalt and a zero value was assigned to them in calculating the resource grade.

Walford Creek is a remote location. The objective of future work is expected to be directed to increasing the resource base and refining the grade estimate.

Also in northwest Queensland, CSE holds the Kamarga exploration tenements, 200km northwest of Mount Isa. The Kamarga Dome area hosts several million tonnes of non-economic 2-3% zinc/lead mineralisation. CSE is exploring this large resource to establish if there are higher-grade and economic zones in the larger body. Southeast of Mount Isa and 15km south of the Eloise copper mine, the Levuka tenement of $21km^2$ is prospective for copper.

Valuation & risks

CSE is an exploration company and its share price will move with exploration news – both positive and negative. The Einasleigh project is the most advanced, and we have used the production rate and cost structures from a scoping study to estimate a value. However, the feasibility study is yet to be completed and, until this is done, and the costs are updated for the current high level of demand in the resource industries, and the development decision taken and finance are in place, there is significant risk. Subsequently there is development risk and, ultimately, operational risk. We have addressed this with a 25% discount to the Einasleigh project NPV, which in turn is based on our expectations for the copper price and the AUD/USD exchange rate.

Table 2 : Valuation snapshot

Fair value*	**A$0.58**
Target price	A$0.50
Current price	A$0.50
Upside/downside	(0.0%)
* Methodology	NPV
Assumptions	
WACC	9.16%
Beta	1.2
Equity risk premium	4.50%
Risk-free rate	5.75%

Source: ABN AMRO Morgans estimates

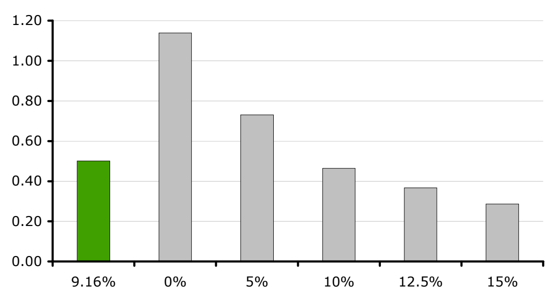
Table 3 : CSE – financial summary

Capital Profile		
Share price - current		$0.50
Share price - 52 wk range	$0.17	$0.54
Number of shares (m)		65.3
Market capitalisation		$32.6M
Avg monthly volume (m)	6.8 M	$2.9 M
Major Shareholders		
Teck Cominco Ltd		14.5%
Geo Discovery Group		9.5%
Acorn Capital Ltd		9.1%

Significant Ratios	
Resources (Mt)	13.84
Reserves (Mt)	4.38
Projected mine life	5 - 6 years
Estimated capital requirement	$80m
Market Cap per Resource tonne ($)	$2.36
Market Cap per Reserve tonne ($)	$7.45
Projected Cash Costs (A$/lb Cu equiv)	$1.15
Projected Total Costs (A$/lb Cu equiv)	$1.50

Valuation		
	WACC	**9.2%**
Asset	**$m**	**$/share**
Einasleigh Copper	19.3	0.30
Chloe Zinc	8.0	0.12
Walford Creek	8.0	0.12
Net cash	2.0	0.03
Exploration	10.3	0.16
Corporate Overheads	-10.0	-0.15
Total Value $m	**32.8**	**0.58**
Mark to Market	0.0	
Premium/Discount to NPV		0%

Valuation sensitivity to discount rate (A$/share)



Earnings Sensitivity (A$m)			
Year to 30 June	**2007F**	**2008F**	**2009F**
Copper Sensitivity 10%	0.0	0.0	5.2
Copper Sensitivity US$10c/lb	0.0	0.0	2.6
Gold Sensitivity 10%	0.0	0.0	0.3
Gold Sensitivity US$10/oz	0.0	0.0	0.0
USD Sensitivity +10%	0.0	0.0	-4.7
USD Sensitivity +1c	0.0	0.0	-6.2

Price Multiples					
Year to 30 June	**2005A**	**2006A**	**2007F**	**2008F**	**2009F**
PROFIT ($m) after-abnormals	**-0.8**	**-1.0**	**-2.2**	**-2.3**	**23.0**
- EPS (c)	-1.6	-1.6	-3.4	-3.5	35.3
- PE Ratio (x)	-30.9	-11.5	-14.8	-14.3	1.4
CASHFLOW ($m)	4.4	-1.7	-1.0	-2.1	33.0
- CFPS (c)	-1.6	-1.6	-3.2	-3.2	50.6
- P/CF Ratio (x)	0.0	-11.6	-15.5	-15.7	1.0
DIVIDEND (c)	0.0	0.0	0.0	0.0	0.0
- Yield (%)	0.0%	0.0%	0.0%	0.0%	0.0%
- Franking (%)	0%	200%	0%	200%	200%
- Payout Ratio (%)	0%	0%	0%	0%	0%
GROWTH - EPS (%)	n.m.	-0.6%	110.7%	3.1%	#####

Production and Costs					
Einasleigh ore mined (kt)	0.0	0.0	0.0	0.0	100.0
Kaiser Bill ore mined (Mt)	0.0	0.0	0.0	0.0	2.0
Ore milled (Mt)					1.1
Copper production (kt)					13.2
Gold production (koz)					4.5
Cash Costs (A$/lb Cu equiv)					1.15
Total Costs (A$/lb Cu equiv)					1.50

Earnings Forecasts					
Year to 30 June	**2005A**	**2006A**	**2007F**	**2008F**	**2009F**
Currency and commodities					
A$/US$	0.75	0.75	0.76	0.78	0.76
Copper Price (US$/lb)	1.43	2.30	3.11	2.50	2.00
Gold Price (US$/oz)	422.77	527.30	646.00	687.50	650.00
Profit & Loss (A$m)					
Total Sales	0.0	0.0	0.0	0.0	79.3
Other Revenue	0.0	0.0	0.0	0.0	0.0
Total Revenue	0.0	0.0	0.0	0.0	79.3
Operating Costs	0.0	0.0	0.0	0.0	33.6
Operating Profit	0.0	0.0	0.0	0.0	45.7
Depreciation & Amort	1.0	1.1	3.1	3.2	10.0
EBIT	-1.0	-1.1	-3.1	-3.2	35.7
Net Interest	0.2	0.1	0.2	0.2	-5.0
Pre-tax Profit	-0.8	-1.0	-2.9	-3.0	30.7
Taxation	0.0	0.0	-0.7	-0.8	7.7
Profit after Tax	-0.8	-1.0	-2.2	-2.3	23.0
Minorities	0.0	0.0	0.0	0.0	0.0
Net Profit	-0.8	-1.0	-2.2	-2.3	23.0
Abnormal Items	0.0	0.0	0.0	0.0	0.0
Net Profit after Abnormals	-0.8	-1.0	-2.2	-2.3	23.0

Profitability Analysis (%)					
Year to 30 June	**2005A**	**2006A**	**2007F**	**2008F**	**2009F**
Margins - Pretax Profit/Sales	n.m.	n.m.	n.m.	n.m.	38.7%
- EBIT/Sales	n.m.	n.m.	n.m.	n.m.	45.0%
- Operating Profit/Sales	n.m.	n.m.	n.m.	n.m.	57.6%
Effective Tax Rate	0.0%	0.0%	0.0%	0.0%	25.0%
Growth - NPAT	n.m.	n.m.	n.m.	n.m.	n.m.
- EPS	n.m.	n.m.	n.m.	n.m.	n.m.
- Sales	n.m.	n.m.	n.m.	n.m.	n.m.
Return on Funds - EBIT/Assets	n.m.	n.m.	n.m.	n.m.	n.m.
- NPAT/Equity	n.m.	n.m.	n.m.	n.m.	n.m.

Balance Sheet Analysis					
Year to 30 June	**2005A**	**2006A**	**2007F**	**2008F**	**2009F**
Balance Sheet - Debt	-	-	-	30.0	30.0
- Equity	6.8	7.5	7.4	35.2	58.2
- Assets	7.0	7.8	7.7	65.4	88.4
- Cash & Deposit	4.4	2.8	1.8	-0.3	32.7

Source: Company data, ABN AMRO Morgans forecasts

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