DJ Carmichael

RESEARCH

RESOURCES

14 June, 2011

RECOMMENDATION:

Buy

VALUATION:

$0.36 per share

Capital Structure

ASX Code	KRL
Current Share price	$0.14
Mkt cap[1]	$480.8m
Ordinary shares on issue	3,434m
Options (various)[2]	145.6m

1 Undiluted
2 Unlisted

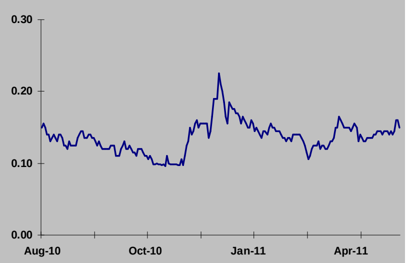
Directors & Management

Peter Richards	Non-Exec Chairman
Mark O'Keeffe	Managing Director
Trevor Butcher	Director
Galih Kartasasmita	Director
Mike Ralston	CFO
Jerko Zuvela	Chief Geologist

Top 5 Shareholders

PT Bayan Resources	56.1%
Jedi Resources Pty Ltd	11.0%
HSBC Nominees	4.0%
JP Morgan Nominees	3.7%
Saxonberg Enterprises	2.9%

12 Month Price Performance



Source: IRESS

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KANGAROO RESOURCES Limited (KRL)

Bayan Transaction Transforms KRL to the Big League

KRL is an ASX listed coal producer and developer that has amassed a substantial project portfolio of up to 8 coal projects through significant locally based Indonesian Joint Venture partners with project development experience and sound Regional and Central Government relationships. The acquisition of the 3.019 billion tonne Pakar Thermal Coal Project by KRL and the subsequent partial takeover of KRL by PT Pakar Bayan Resources Tbk ("Bayan") are both transformational events for KRL, which significantly de-risk the company and will project KRL into the ranks of Indonesia's largest coal producers over the next few years.

Key Points

- In late December 2010 KRL announced a significant company changing transaction involving the Pakar Thermal Coal Project. With the announcement, KRL laid the foundations to transform itself from an up and coming small scale Indonesian coal producer, facing significant logistical difficulties, into a nationally significant coal producer with over 3 billion tonnes JORC resources of coal, backed by one of the most successful and dominant coal producers in Asia. In the deal, KRL agreed to acquire 99% of the large Pakar thermal coal project ("Pakar") in East Kalimantan from Bayan for 2.305 billion shares in KRL. As a result, Bayan have emerged with a 57% stake in KRL and become its largest shareholder.

- The significance of the Bayan deal goes well beyond the size and scale of the Pakar coal project itself. Bayan also assume full operational responsibility for the KRL suite of coal assets, providing the benefit of its operational and logistical expertise and capacity as well as balance sheet strength to rapidly ramp up production to stated objectives and provide an immediate off-take for coal production. This development is very significant in our view and greatly de-risks the company going forward.

- Pakar is a large scale, low ranking thermal coal project in East Kalimantan, adjacent to KRL's existing Tanur Jaya Coal Project and located NE of the GPK Coal Project. Pakar is substantially developed already as an integrated coal mining operation with total coal resources of 3.019 billion tonnes, inclusive of total coal reserves of 442M tonnes. The project has been developed, drilled and evaluated over the past 4 years with substantial infrastructure to support a mining operation already in place, including roads, port facility, crushers, conveyors, mine camp and other infrastructure to allow for rapid start-up of a large-scale mining operation.

- We have updated our discounted cash flow model to derive a new valuation for KRL, using as a base KRL's stated production objectives under the Bayan strategic alliance. We have derived a sum of parts DCF valuation implying a total value for KRL shares of A$0.36 per share, representing a 157 % premium to the current price at $0.14 per share. We therefore place a **Buy** recommendation on KRL, upgrading our recommendation from a Speculative Buy as a result of the improved operational and logistical capacity and the significant de-risking that we believe the Bayan deal has brought to the company.

Introduction

KRL is an ASX listed coal producer with ambition to become a substantial coal producer from their operations in East Kalimantan, Indonesia. Since mid 2009, KRL has entered into a number of transactions that have given the company mining and other rights to several thermal and coking coal projects of various sizes, all in the same region of Indonesia, that provide KRL with a strong portfolio of both development and producing assets over the long term.

KRL currently has one producing asset (Mamahak Project), albeit at a small scale in the ramp up stage, that is currently providing immediate positive cashflow in an environment where the activity and interest in the coal sector is high, given the coal price increases due to continued high demand from China and India, and the supply shock brought about by the Queensland floods

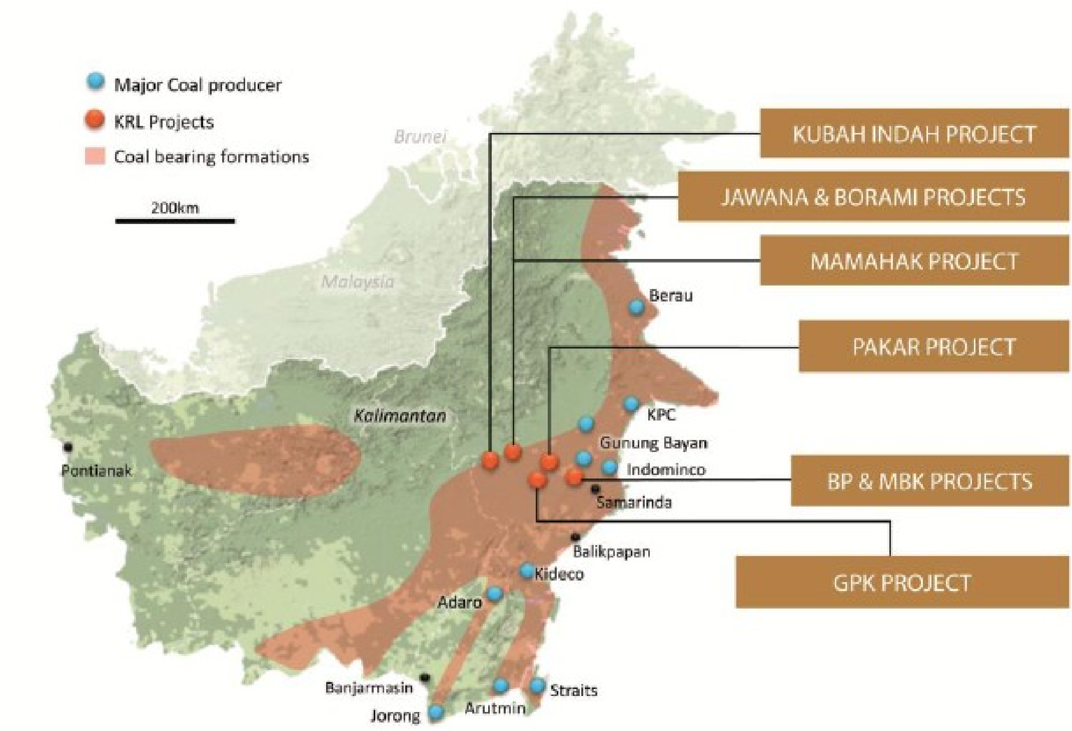


Figure 1. Location Map of East Kalimantan Coal Projects *Source: KRL*

Project Summary

KRL have an interest in eight coal projects in East Kalimantan, comprising 4 coking coal projects and 4 thermal coal projects, of varying in size and quality:

Coking Coal Projects :

- Mamahak (100%) – semi-soft coking coal (SSCC)
- Kubah Indah (100%) – hard coking coal
- Jawana (100%) – SSCC
- Borami (100%) – SSCC

Thermal Coal Projects :

- GPK (84.82%) – low rank thermal coal
- Pakar (99%) – low rank thermal coal, which now includes Tanur Jaya
- MBK (100%) – high quality thermal coal
- BP (100%) – high quality thermal coal

Project	KRL Interest %	2011 Objectives	Conditions Precendent	Concession Status
		Coking Coal		
Mamahak	100	Production	Acquired	Exploitation (Mining License)
Kubah Indah	100	Exploration / Resource definition	Under DD	Exploration Application
Jawana	100	Exploration	Under DD	Exploration Application
Borami	100	Exploration	Under DD	Exploration Application
		Thermal Coal		
GPK	84.82	Under Review	Acquired	Exploitation
Pakar	99	Production / Development	Acquired	Exploitation
MBK	100%	Exploration	Under DD	Exploration Application
BP	100%	Exploration	Under DD	Exploration (Granted)

Table 1. Project Summary and Status *Source: KRL and DJC*

The Pakar Project and the Bayan Deal

In late December 2010 KRL announced a substantial company changing transaction involving the Pakar Thermal Coal Project. With the announcement, KRL laid the foundations to transform itself from an up and coming, small scale Indonesian coal producer, facing significant logistical difficulties, into a nationally significant coal company backed by one of the most successful and dominant coal producers in Asia.

In the deal, KRL agreed to acquire 99% of the large Pakar thermal coal project ("Pakar") in East Kalimantan from Bayan for 2.305 billion KRL shares. In return, Bayan will emerge with a 57% stake in KRL and become its largest shareholder. The deal was subject to a 60 day due diligence process, which completed in May, and shareholder and regulatory approval, which have both recently been granted.

Importantly, Bayan signed an MoU with KRL effectively taking operational control of KRL's other coal assets in East Kalimantan. The Tanur Jaya Project, in which KRL were earning into a 49% interest (and which is one of the 9 concessions within the Pakar Project area) will now be incorporated into the 99% owned Pakar project.

Pakar is a large scale, low ranking thermal coal project in East Kalimantan, adjacent to KRL's existing Tanur Jaya Project and located NE of the GPK Project. Pakar is substantially developed already as an integrated coal mining operation with total JORC coal resources of 3.15 billion tonnes, inclusive of total coal reserves of 442M tonnes.

The project has been developed and evaluated over the past 4 years with substantial infrastructure to support a large scale mining operation already in place, including roads, port facility, crushers, conveyors, mine camp and other infrastructure to allow for rapid start-up of a mining operation.

The Pakar resource has been divided into a 'north' and 'south' project area with resources estimates and coal quality determinations performed separately.

Pakar project Resource Coal Quality Data

PROJECT	AVERAGE COAL QUALITY - RESOURCES						
	TM% (ar)	IM% (adb)	Ash % (adb)	TS% (adb)	CV kcal/kg (adb)	CV kcal/kg (gar)	RD (adb)
NORTH PAKAR	39.1 – 43.1	18.6	5.1 – 5.7	0.13 – 0.14	5,160 – 5,255	3,595 – 3,930	1.36
SOUTH PAKAR	45.5 – 54.3	12.6 – 14.4	4.0 – 14.5	0.17 – 0.28	4,599 – 5,443		1.39 – 1.48

Figure 2. North and South Domain Pakar Resource quality *Source: KRL*

Figure 3. Pakar Infrastructure already in place *Source: KRL*

Who is Bayan?

PT Bayan Resources Tbk is a significant Indonesian-listed coal mining and processing company with a vertically integrated business incorporating mining through to processing, stockpiling, logistics and sales.

With a current market capitalisation of around US$7billion, Bayan is a dominant player in the Indonesian coal market. It has total coal resources of more than 1 billion tonnes and coal reserves in excess of 500Mt spanning eight mining concessions in East and South Kalimantan.

It has interests in both the coking coal and thermal coal markets and sees the agreement with KRL as further enhancing its presence in East Kalimantan. In 2010 it was made revenues in excess of $1 billion from its coal activities.

In addition to its mines Bayan also owns the Balikpapan Coal Terminal, one of the largest in Indonesia with a throughput of up to 15Mtpa and stockpiling facilities for approximately 1.0mt at any one time across 16 separate stockpiles. Since its development, the coal terminal has handled more than 55 million tonnes and loaded in excess of 1,000 ships.

Bayan also has an interest in coal technology and beneficiation through the ownership of Binderless Coal Briquetting Company Pty Ltd, which upgrades low calorific coal by reducing moisture and compaction to form a briquette that can be handled and transported like normal coal. Hence Bayan are involved all the way through the coal value chain.

Bayan brings to KRL extensive mining and operational ability in the region, logistical expertise, operational synergies, economies of scale, technology and experience. All of these we see as crucial to optimising the KRL asset base and in our view greatly reduces operational, executional and logistical risk and enhances the value drivers to KRL stakeholders. We therefore see this transaction as being very positive for KRL shareholders.

Post Bayan Ownership and Capital Structure

The scrip deal now sees Bayan as the major shareholder, with a 57% stake following the issue of 1.93 billion shares, followed by Jedi Resources Pty Ltd with 380m shares, or 11% (allocated as part of the Pakar acquisition), totaling 2.3b shares issued in return for the Pakar coal project. KRL also received US$18 million in cash as part of the Pakar deal. This now results in there being 3.43 billion quoted KRL shares for a market capitalisation of circa $540 mllion at $0.16 share price, bringing KRL into the ASX 300.

Significant Shareholders	No. Shares	%
PT Bayan Resources Tbk	1,925.0m	57.0%
Jedi Resources Pty Ltd	380.0m	11.0%
HSBC Custody Nominees	136.1m	4.0%
JP Morgan Nominees	129.0m	3.7%
Saxonberg Enterprises	100.0m	2.9%
National Nominees	61.7m	1.8%

Table 2. Major Shareholders *Source: KRL*

Capital Structure

Quoted Securities	
Previous Shares on Issue	: 1,129,430,012
Shares issued to Bayan	: 1,925,000,000
Share issued to Jedi	: 380,000,000
Total Quoted	**: 3,434,430,012**
Unquoted Securities	
Warrants (Jul 2015, 13.3c)	: 128,103,448
Options (Sep 2012, 25c,35,50c)	: 7,500,000
Options (Sep 2012, 25c)	: 1,000,000
Options (Sep 2012, 5c,10c)	: 10,000,000
Total Unquoted	**: 145,603,448**
Fully Diluted	**: 3,580,033,460**

Table 3. Capital Structure *Source: KRL / Iress*

Financing

In December 2010, prior to the announcement of the Pakar acquisition, KRL completed a capital raising of $23.8m through a placement at $0.119c per share for 200m shares. As at the end of the March quarter, KRL had a cash balance of $8.0m. However, a further $18m was paid into KRL from the Bayan deal, resulting in total current cash of circa $26m.

Warrants and options, if exercised, could provide an additional $22.0m in funding through to 2015.

KRL Total Coal Resources, Reserves and Quality Tables

Resources

Project	JORC Resource						
	Measured	Indicated	Inferred	TOTAL	Reserves	Exploration target	Coal Quality
Coking Coal							
Mamahak	6.85Mt	3.11 Mt	0.53Mt	**10.49Mt**		25-40Mt	Coking coal: ~ 7,500 kcal/kg
Kubah Indah						100-140Mt	Coking coal: ~ 7,500 - 8,500 kcal/kg
Jawana & Borami						20-40Mt	Coking coal: ~7,500 kcal/kg
Thermal Coal							
GPK		58Mt	59Mt	**117Mt**		250-300Mt	Thermal coal: ~5,245 kcal/kg
Pakar	111Mt	1,092Mt	1,816Mt	**3,019Mt**	442Mt		Thermal coal: ~5,000 - 5,400 kcal/kg
MBK & BP						20-30Mt	Thermal coal: ~ 6,800 - 7,200 kcal/kg
TOTAL	117.9Mt	1,153.1Mt	1,875.5Mt	**3,146Mt**	442Mt	415-550Mt	

Table 4. Resources and Exploration Targets for KRL Project Portfolio *Source: KRL*

Quality

Project	Coal Quality
Coking Coal	
Mamahak	Coking coal quality: 6,991 - 7,793 kcal/kg, Total Moisture 2.2% - 4.1% Sulphur 0.49% - 3.85% Ash 60.% - 14.9%
Kubah Indah	Coking coal quality: ~7,500 - 8,500 kcal/kg Total moisture 4.6% - 5.7% sulphur 0.49% - 0.83% Ash 2.4% - 12.7%
Jawana & Borami	Coking coal quality: ~7,500kcal/kg No drilling to date, but expected to be similar to Mamahak
Thermal Coal	
GPK	Thermal coal quality: ~ 5,245 kcal/kg Total moisture 39.6% Total Sulphur 0.18% Ash4.9%
Pakar	Thermal coal quality: ~ 5,215 - 5,230 kcal/kg Total moisture 41.1 - 48.6% Total Sulphur 0.14% Ash 5.5% - 5.7%
MBK & BP	Thermal coal quality: ~ 6,800 - 7,200 kcal/kg Total moisture 7.4% Total Sulphur 2.55% Ash 6.29%

Table 5. Coal Quality Table for KRL Project portfolio ***Source: KRL***

Other Project Details

KRL now has one producing operation in East Kalimantan - the semi-soft coking coal project, Mamahak - after KRL decided to review the status of the GPK project post the Bayan acquisition. KRL had been considering a trade sale of the GPK asset prior to the acquisition as a means of gaining further cash in order to develop its other projects. However with the emergence of Bayan as a major shareholder, wanting to produce as much coal within KRL as possible, a trade sale of GPK was immediately shelved and this project will form a third key production hub for the company going forward, with production targeted for early 2012..

Mamahak Project (100%) – Production Update

The Mamahak semi-soft coking coal project was acquired from TSX-listed South Gobi Energy Resources Ltd (TSX:SGQ) ("South Gobi") in December 2009. The agreement, covering all the South Gobi's assets in Indonesia, involved a US$1.0m cash payment and 50.0m shares in KRL, escrowed for 12 months. KRL initially acquired only 85% of Mamahak but announced the acquisition of the remaining 15% for $1 in 2011 thus bringing its interest in the project to 100%.

The project has an existing JORC resource of 10.5mt estimated by KRL, on exploration licenses comprising 22,976 hectares, with an option over 5 additional concessions totalling 24,501 hectares in the Haloq Formation, which hosts other coking coal projects in East Kalimantan. The concessions are located contiguous with KRL's existing Jawana and Borami Projects providing significant potential operational synergies.

Production started in February 2010 with pre-stripping of over-burden and exposure of approximately 15,000 to 30,000 tonnes of coal in thin coal measures, 30cm to 1.70m thick. Coal is being stockpiled on site at a 'run-of-mine' (ROM) facility and will be transported to KRL's stockpile facility at a barge loading port on the Mahakam River and then to the coast. The operation is utilising a 'dozer push' mining method, thereby reducing operating costs.

KRL is now pushing production towards 30,000 tonnes per month now that Bayan has assumed responsibility for the operations. We expect the Mamahak Operation to reach production rates of in excess of 500,000 tonnes per annum next FY and slowly ramp up towards a rate of 1.0Mtpa by 2014.

Figure 4. Barge Loading Facility at Mamahak with stockpile *Source: DJC*

Medium term Off-take Contract over Mamahak Secured

KRL finalised a significant coal off-take contract with Bayan during the March quarter, for coal sales up to 300,000 tonnes at market price, free-on-board (FOB) from the Mamahak jetty. This agreement allows for KRL to get paid for coal immediately at port site which means quicker cash into the business and zero logistical challenge of barging coal downriver, stockpiling and loading onto mother vessels. KRL can concentrate on mining coal which is where the Company's strengths lie. Additionally this deal allows for 70% payment of coal on stockpile and 30% on barge loading, which means KRL can continue to produce coal and be paid for it even if river levels are low and no barging is able to take place. This is very advantageous to KRL and secures constant sales and cash flow from operations 365 days per year. The scale up of operations at the project is continuing with additional haul trucks and other mobile equipment, the upgrading of the capacity of the barge loader, recruitment of additional staff and submission of additional forestry applications to open up new areas for mining.

As the ramp up continued coal sales for the 1Q2011 totalled 35,000 tonnes with an additional 9,500 being delivered to on-site stockpiles by mid April. KRL are now delivering approximately 30,000 tonnes per month. The capital expenditure made in increasing the capacity of Mamahak has enabled year round transportation, via the upgraded haul roads and additional trucking capacity, of the coal to generate revenues year round. The seasonal nature of the river at Mamahak had previously meant that transportation could only occur when the river was navigable, out of the dry season. This greatly effected cashflow and the ability of Mamahak to operate at an efficient level.

KRL has successfully sought and acquired extensions to its mining permits and licenses at Mamahak and has also successfully completed the mandatory transfer of licenses from KP status to the new IUP status, which will ultimately allow for direct foreign ownership of the concessions. KRL is in the process of moving to direct ownership of all Indonesian coal assets via new Mining Laws and expects that this will be in place around mid-2011.

GPK (Graha Panca Karsa) Thermal Coal Project (84.82%)

KRL originally entered into an agreement with the concession owner - PT Graha Panca Karsa, under which it was granted the exploration, mining and selling rights to an 84.82% interest in the GPK Project - a significant thermal coal project in East Kalimantan. Under the terms of the agreement a US$2.0m cash consideration was paid and an additional US$8.0m spent in-ground to move the project into production to earn the 84.82% interest in this project. A share-based payment totalling 150.0m shares was issued to parties nominated by KRL's significant shareholder PT Energi Surya Abadi, as a finder's fee for the GPK project.

As part of the due diligence on the Bayan transaction these mining rights at GPK have been upgraded to an 84.82% KRL direct share interest in the company PT Graha Panca Karsa, thus giving KRL a much stronger position of control in this project than it ever held before,

The GPK project includes 4 concessions covering 22,976 hectares located 15km from the Mahakam River. Average coal seam thickness of 4.5m with shallow dips mean low strip ratio (average 3:1, dependent on coal price) and ease of mining, with over 60% of the total resource lying within 60m of the surface. An existing JORC resource totalling 117m tonnes provides the basis for a long term mining operation at GPK. KRL and its mining consultants are very confident in a strong resource to reserve conversion and work is underway to secure a first JORC reserve for GPK in 2011.

Operations commenced in December 2009 with KRL clearing the site for the establishment of the main port loading facility and the commencement work on pre-stripping the designated coal mining areas. The barge loading facility will be used to barge coal down the Mahakam River for sale to the export market as GPK coal is sought after for power generation in India in particular. KRL will be utilising 5,000 tonne barges for this purpose.

Although production continued for some time, operations ceased last year as KRL considered a trade sale of the asset to a number of parties. At the time the GPK project was not a significant value driver for the company. However, leveraging Bayan's logistical and operational expertise under the present structure will result in improved economics for the project. KRL now has the project under review and we expect that production could again be started in FY2012.

KRL will look to a sale-at-mine-gate offtake agreement with Bayan for GPK coal, similar to that already in place at Mamahak, whereby the Company does not get involved in the logistical challenges of barging, stockpiling and loading coal, and concentrates on mining as much coal as possible. Such agreement would be done at market prices to ensure KRL received fair value for this coal. The two parties will discuss a potential offtake agreement later in 2011 once GPK is closer to re-starting operations.

The 2011 key KRL operational strategy is therefore:

1. Commence immediate ramp up of existing Mamahak semi-soft coking coal operation
2. Initiate some Pakar coal production, likely in the Pakar 'south' region and look to get Pakar 'north' into production by late 2011
3. Target GPK into initial production in late 2011 or early 2012

This means that KRL will aim to have three production hubs in operation selling coal by late 2011, or early 2012, which all have the ability to ramp up quickly and place the Company in the position of becoming Indonesia's newest large coal producer.

Kubah Indah Coking Coal Project (earning 100%)

The Kubah Indah Project is a coking coal project with KRL earning 100% subject to shareholder approval, with exploration leases located 100km from the Markham River. This is a potentially large project for KRL with premium quality export hard coking coal. Previous exploration consists of over 5,000m of drilling identifying seven main coal seams. The project has an exploration target of between 100Mt and 140Mt and KRL has estimated that production could start as early as FY2013 with a target production rate of approximately 1.5 – 2.0Mtpa. Start up capex has been estimated at approximately $100m.

However, in the 2010 Annual Report KRL stated that after KRL had completed its due diligence in May 2010, the company received notification from a large multinational third party alleging that part of the initial three exploration licences for the Kubah Indah Coking Coal Project overlap licenses held by the third party. These allegations also claim that the licenses held by the third party have a priority right to the licenses granted to the Company's Indonesia partner. While overlap issues are fairly common in Indonesia the Company is confident in the position held by its Indonesian partners and is conducting further due diligence as necessary to resolve this issue.

KRL will continue to push for closure in the Kubah Indah issue as a priority now that the Pakar/Bayan transaction is complete. The Company is confident that it will ultimately hold a significant concession area with coking coal and it will move to develop that as a priority thereafter. In the meantime no shares will be issued for Kubah Indah until all due diligence is completed.

Minor Projects

Other projects include the Jawana and Borami coking coal and thermal coal projects, both of which are neighbouring KRL's Mamahak Project next to the Markham River, and the smaller MBK and BP Projects. All these projects are greenfield exploration targets but have substantial coal outcropping and therefore potential to add to KRL's portfolio of coal assets. They are all still subject to deal completion, due diligence and ultimately shareholder approval, and have therefore not been modelled separately in our analysis.

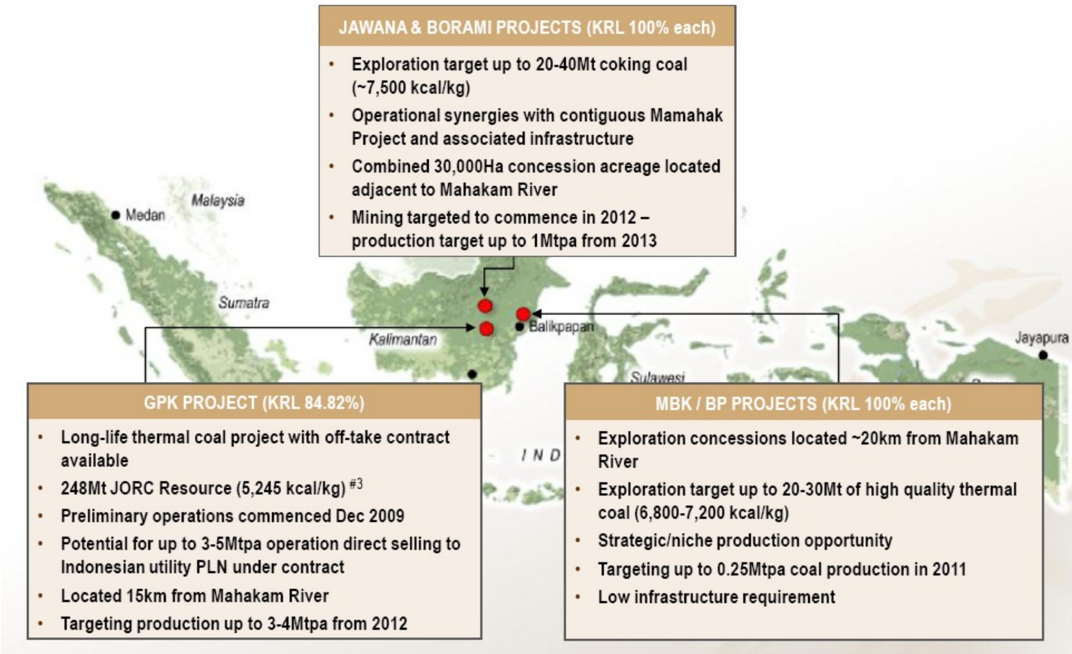


Figure 5. Project Summary (ex Mamahak, Pakar, Kubah Indah) *Source:KRL*

Valuation

Indonesian Coal Pricing Supply and Demand Dynamics & Price Assumptions

Commodity prices are based on the assumptions made by KRL but backed by DJ Carmichael's current knowledge of coal prices and forecast growth statistics. The current pricing for the global COAL Newcastle Index, seen as a benchmark for Asia, rose to around US$120 per tonne. The Mamahak semi-soft export coking coal asset analysis used $100 per tonne and the low grade thermal coal coming from the Pakar and GPK projects uses prices set around US$35 per tonne. The current price for low grade Indonesian sub-bituminous coal is currently selling for between US$33 and US$35 per tonne for quality in the range 5,300 – 5,500 kcal/Kg adb, FOB Kalimantan.

Continued bad weather in Queensland has affected global supply and in a few months time, the Queensland rainy season will commence again. Indonesia has also had its fair share of poor weather this year with high rainfall levels recorded in Kalimantan, crimping production.

But buyers are turning to Indonesia to fill the supply gap left by Australia and more expensive landed coal costs from South Africa. We predict world demand for coal will be strong for the short to mid-term as weather events and other supply constraints keep pricing firm. In addition China has its own supply constraints and domestic coal prices have been rising strongly as utilities have stockpiled coal ahead of the summer months. This is making imported coal more attractive.

There will be intense competition between India and China for imported coal tonnages and Indonesian coal, given its geographic advantage to both markets, will be highly sort after. India has now surpassed China as the lead buyer of Indonesian coal with sea-borne coal demand into India likely to be high throughout CY2012 with a domestic supply deficit recently announced of 112Mt, up from 88Mt a few months ago.

		FY	2010	2011	2012	2013	2014
Revenues	**GPK Project**	**US$/t**	0	0	38	38	38
	Mamahak Project	**US$/t**	0	100	100	100	100
	Pakar	**US$/t**	0	0	30.8	32.6	33
	Kubah Indah	**US$/t**	0	0	0	250	250
	MBK	**US$/t**	0	0	0	0	0

Table 7. Commodity Price Assumptions for KRL Project Portfolio *Source: KRL*

DCF Analysis

We have updated our discounted cash flow model to derive a new valuation for KRL, using as a base, KRL's stated production objectives under the Bayan strategic alliance.

Progress on production ramp up has been slow since April 2010, partly due to the decision to sell the GPK asset and issues with transport logistics at Mamahak. However, we now expect to see rapid growth in production capacity over the next 2 to 3 years as the full benefit of the strategic alliance with Bayan takes effect.

		FY	2010	2011	2012	2013	2014
Attributable Production	GPK Project	t	-	-	763,380	2,722,722	3,358,872
	Mamahak Project	t	-	134,828	510,000	800,000	950,000
	Pakar	t	-	-	4,455,000	10,098,000	11,880,000
	Kubah Indah	t	-	-	-	-	500,000
	MBK & BP	t	-	-	-	-	-
	Total		**-**	**134,828**	**5,728,380**	**13,620,722**	**16,688,872**

Table 6. Production Profile for KRL Project Portfolio *Source: DJC*

Other assumptions we have made to derive our valuation include:

- USD : AUD rate — $1.00 (first 3 years, $0.95 LT)
- Discount Rate — 12% - 18%
- Mine Life — to 2025
- Depreciation — Straight line over LOM
- Corporate tax Rate — 25%
- Total CAPEX — US$148m (including sustaining capital)

OPEX costs for each operation have been based on data provided by KRL. Operating costs include royalties and Government levies. The CAPEX estimates is mostly composed of costs incurred with the Kubah Indah Project and therefore represents the higher, more conservative expenditure and assumes that the Kubah Indah Project proceeds to production by 2014.

			US$	AU$	A$ / per share
NPV	GPK Project	14%	$89,663,553	$93,874,750	0.03
	Mamahak Project	12%	$139,840,296	$145,553,925	0.04
	Pakar	14%	$804,048,653	$838,891,941	0.23
	Kubah Indah	30%	$108,532,128	$116,645,021	0.03
	Total		**$1,142,084,630**	**$1,194,965,637**	**0.33**

Table 8. Project NPV for KRL Project Portfolio *Source: DJC*

Discount Rates

In our project NPV determinations we have used different discount rates to reflect the status of each project. As Mamahak is in production but continuing its ramp up to full capacity we have elected to use a discount rate for our DCF analysis of 12% whilst the Pakar and GPK projects have been analysed using a discount rate of 14% reflecting near-term, but as yet un-commenced production.

Kubah Indah, whilst a potential major project for KRL, has some uncertainty with regard to the outcome of the tenure issues on some its concessions. We have decided to include Kubah Indah in our DCF analysis but have assigned a discount rate of 30% to reflect this uncertainty. As this issue gets resolved we will revisit the discount rate to take into account the de-risking of the project.

Sum of Parts Valuation	Item	A$ (m)	A$ per share
	GPK	93.9	0.03
	Mamahak	145.6	0.04
	Pakar	838.9	0.23
	Kubah Indah	116.6	0.03
	Exploration	50.0	0.01
	Options	22.0	0.01
	Cash	26.0	0.01
	Corporate	-5.0	0.00
	Total	**1,288.00**	**0.36**

Table 9. Sum of Parts Valuation for KRL *Source: DJC*

Recommendation

Using the above assumptions we have derived a sum of parts DCF valuation for implying a total value for KRL shares at A$0.36 per share, representing an 157 % premium to the current price of $0.14 per share. We therefore place a **Buy** recommendation on KRL, upgrading our recommendation from a Speculative Buy as a result of the improved operational and logistical capacity, and the significant de-risking that we believe the Bayan deal has brought to the company.

Investment Risks

Commodity Price and Currency Risk : As with all resource based companies, fluctuations in commodity prices has a major influence on the outcome of a DCF valuation. The current environment for coal and coal companies is favourable, and over the long term, we believe that coal prices will be reasonably well supported, providing robust economics for future projects. However, the prices received for projects supplying thermal coal to local power stations will vary depending on local conditions and margins for these projects are not generally high. Fluctuations in exchange rates will also have an influence on the A$ denominated profits.

Operational Risk : We view the Bayan deal as being highly beneficial to KRL in its expansion plans in Indonesia. Having a group such as Bayan with its local operational and logistical expertise including its vertically integrated value chain, is a large mitigator in risk in our view, especially when local knowledge and capable, dependable strategic partners are almost a pre-requisite for success in Indonesia. However, external factors such as third party suppliers and the unpredictability of the weather will all play a part in effecting future cash flows. To a degree, future funding issues have been lessened by Bayan's balance sheet strength.

Third Party Risk : KRL are currently supplying their Indonesian JV partners' funds to continue operations, until KRL can convert these loans to equity under the new mining law. Given the local partners are also major shareholders in KRL, and the added security of exchangeable bonds in the local PT companies for these funds, the interests of KRL are protected to a degree.

Tenure Risk : KRL continue to seek a resolution to the Kubah Indah concession issue arising as a result of a third party contesting the ownership of some of the concessions at the project. There is uncertainty as to the final outcome of this issue and it is possible that KRL could lose some or all of those concessions. Should this occur, it would negatively impact on our valuation. However, if resolved successfully, we would adjust our discount rate for the project downward to account for the lessening in risk to this project, with a consequent increase in our valuation, all else being equal.

Directors

Peter Richards – Non-Executive Chairman
Peter holds a Bachelor of Commerce from the University of Western Australia. He has over 30 years of business and international experience with global companies including BP plc, Wesfarmers Ltd and Dyno Nobel Limited and recently retired as CEO of Dyno Nobel following its successful takeover. After becoming CEO, he expanded the business into China, Southern Africa and Europe while continuing to build upon its core Australian and North American operations. He is currently a non-executive director of NSL Consolidated.

Mark O'Keeffe – Managing Director
Mark has been a successful businessman in the Perth community for the past 18 years and in recent years has become actively involved in the minerals industry. He has provided his services in various corporate capacities, including his direct involvement in a number of private and public company capital raisings. In addition Mark was instrumental at bringing into KRL the Indonesian partners and their coal projects and maintains a close ongoing relationship. Mark's extensive corporate experience and networks in combination with his entrepreneurial skills will contribute significantly to the Company's strategic move into the Indonesian coal sector.

Trevor Butcher – Director
Trevor is an Indonesian-based professional who has spent more than five years working in the Indonesian mining industry, specifically in coal. This industry knowledge and significant Indonesian business relationships with local partners will be invaluable to help guide KRL through the next phases of development. The advantages of being based in Jakarta, as well as his ability to speak the language and understand the local culture are strategically important skills in developing the KRL coal assets.

Galih Kartasasmita – Director
Galih is an Indonesian national with extensive experience in the country's resources market and a strong contact network in business and political circles. Previous experience lies with PT Freeport Indonesia and PT Bakrie and Brothers.

Management

Mike Ralston – Chief Financial Officer
Mr Ralston joined KRL as the Company's Chief Financial Officer in mid-2009 with a mandate to build strong financial discipline within the Company, provide strategic advice based on his resource experience, as well as to assist in fund raising and the management of corporate and ASX matters. He has 12 years experience as a CFO internationally and has been CFO of several ASX listed mining companies over the past 5 years. He worked in the Indonesian coal market as CFO to Fireside Resources for the 12 months prior to joining KRL. Mr Ralston is a member of the Australian Institute of Company Directors, holds a Bachelor of Commerce from University of South Africa and is a Chartered Management Accountant (London).

Jerko Zuvela – Chief Geologist
Mr Zuvela joined KRL in mid-2009 as the Company's Chief Geologist with a mandate to manage, explore and develop all of KRL's projects. He has 14 years resources experience in Australia and internationally, and has been directly involved in the Indonesian coal sector during the past 4 years, during which time he has worked for Strike Resources as General Manager – Operations, and Fireside Resources as Chief Geologist. Mr Zuvela is a member of the Australasian Institute of Mining and Metallurgy and holds a Bachelor of Science in Applied Geology from Curtin University of Technology in Western Australia.

Kangaroo Resources Ltd

$0.14

PROFIT AND LOSS ANALYSIS	($m)	2009a	2010a	2011e	2012e	2013e
Sales revenue		0.0	0.1	13.5	217.2	513.1
Other revenue		0.0	3.6	6.0	2.0	4.0
Total Revenue		0.0	3.6	19.5	219.2	517.1
Direct Operating Costs		-1.2	-9.7	-8.8	-116.2	-262.0
Gross Operating Profit		**-1.2**	**-6.1**	**10.7**	**103.0**	**255.0**
Depreciation & Amortisation		0.0	0.0	-0.3	-2.1	-2.1
Exploration Written off		0.0	-2.7	-2.0	-2.0	-2.0
Other		0.0	0.0	-19.9	0.0	0.0
EBIT		**-1.2**	**-8.8**	**-11.5**	**98.9**	**250.9**
Interest Expense (benefit)		0.0	0.0	0.0	0.0	0.0
Abnormals & Other		-0.8	-39.6	0.0	0.0	0.0
Profit before Tax		**-2.0**	**-48.4**	**-11.5**	**98.9**	**250.9**
Tax expense		0.0	0.0	1.1	25.0	62.7
NPAT		**-2.0**	**-48.4**	**-12.6**	**73.9**	**188.2**
DJC Adjusted NPAT		-2.0	-48.4	-12.6	73.9	188.2

CASH FLOW STATEMENT	($m)	2009a	2010a	2011e	2012e	2013e
Cash from customers		0.0	0.1	13.5	217.2	513.1
Net Interest received		0.0	-0.3	6.0	2.0	4.0
Cash paid to suppliers		-0.4	-5.8	-8.8	-116.2	-262.0
Tax and Other		0.0	0.0	0.0	-0.4	-0.5
Cashflows from Operating Activities		**-0.4**	**-6.0**	**10.7**	**102.6**	**254.5**
Exploration Expenditure		-0.8	-11.7	-25.0	-5.0	-5.0
Property, plant & equipment		0.0	0.0	-1.2	-42.1	-59.7
Other		-0.2	-11.5	0.0	0.0	0.0
Cashflows from Investing Activities		**-1.0**	**-23.1**	**-26.2**	**-47.1**	**-64.7**
Proceeds from issue of shares		1.9	29.0	23.8	0.0	0.0
Dividends paid		0.0	0.0	0.0	0.0	0.0
Other		-0.7	2.6	15.5	32.0	28.0
Cash Flow from Financing Activities		**1.2**	**31.6**	**39.3**	**32.0**	**28.0**
Net change in cash		**-0.2**	**2.5**	**23.9**	**87.5**	**217.8**
Adjusted Cash at end of period		1.1	3.5	27.4	114.9	332.7

BALANCE SHEET	($m)	2009a	2010a	2011e	2012e	2013e
Cash		1.1	3.5	27.4	114.9	332.7
Other		0.1	13.7	11.1	8.0	8.0
Total current assets		**1.2**	**17.2**	**38.5**	**122.9**	**340.7**
Property Plant & Equipment		0.4	0.2	1.4	43.4	103.1
Exploration & development		2.6	11.6	34.6	37.6	40.6
Other		0.2	12.4	16.5	0.0	0.0
Total non-current assets		**3.2**	**24.2**	**52.4**	**81.0**	**143.7**
Total Assets		**4.4**	**41.4**	**90.9**	**203.9**	**484.4**
Payables		0.4	3.8	4.2	4.0	4.0
Borrowings		0.2	1.3	2.4	0.0	0.0
Other		0.0	1.2	4.0	6.0	8.0
Total current liabilities		**0.7**	**6.2**	**10.6**	**10.0**	**12.0**
Non-current debt		0.1	2.7	0.0	32.0	60.0
Other		0.0	0.0	1.0	0.0	0.0
Total non-current liabilities		**0.1**	**2.7**	**1.0**	**32.0**	**60.0**
Total Liabilities		**0.8**	**9.0**	**11.6**	**42.0**	**72.0**
Net Assets		**3.6**	**32.5**	**79.3**	**161.9**	**412.4**

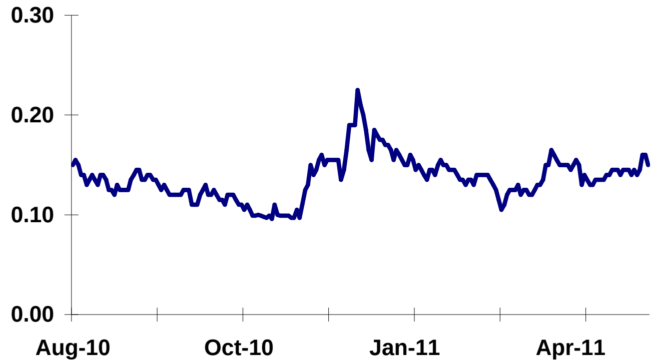
KEY ASSUMPTIONS		2009a	2010e	2011e	2012e	2013e
Commodity pricing						
GPK Project	US$/t	-	32	33	34	34
Mamahak Project	US$/t	-	100	100	100	100
Tanur Jaya	US$/t	-	30	32	35	35
Kubah Indah	US$/t	-	0	0	0	0
FX Rate USD/AUD		-		1.0	1.0	1.0

PHYSICALS		2009a	2010e	2011e	2012e	2013e
GPK Project	t(m)	0.0	0.0	0.0	0.8	2.7
Mamahak Project	t(m)	0.0	0.0	0.1	0.5	0.8
Tanur Jaya	t(m)	0.0	0.0	0.0	4.5	10.1
Kubah Indah	t(m)	0.0	0.0	0.0	0.0	0.0
MBK	t(m)	0.0	0.0	0.0	0.0	0.0

RATIOS		2009a	2010a	2011e	2012e	2013e
Number of shares	m	246.1	567.7	3434.4	3580.0	3580.0
Diluted EPS	cps	-0.01	-0.09	0.00	0.02	0.05
PER	x	- 17.10	- 1.64	- 38.25	6.78	2.66
EPS growth	%	na	na	na	na	255%
FCFPS	cps	na	0	0.00	0.0096	0.04
DPS	cps	0.00	0.00	0.00	0.00	0.00
Dividend yield	%	na	na	na	na	na
EBITDA Margin	%	na	na	35%	46%	49%
EBIT Margin	%	na	na	33%	46%	49%

VALUATION	Value A$	A$ per share
GPK	93.9	0.03
Mamahak	145.6	0.04
Pakar	838.9	0.23
Kubah Indah	116.6	0.03
Exploration	50.0	0.01
Options	22.0	0.01
Cash	26.0	0.01
Corporate	- 5.0	- 0.00
Total	**1288.0**	**$ 0.36**

SHARE PRICE PERFROMANCE (12 MONTHS)



Disclosure RCAN0940

This Research report, accurately expresses the personal view of the Author.

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Declaration:

The Authors of this report made contact with the companies mentioned in this report for assistance with verification of facts, access to industry/company information. DJ Carmichael has produced this research paper on a commissioned basis and has been paid a fee by **Kangaroo Resources Ltd** for this service. No other inducements have been made or accepted.

The recommendation made in this report is valid for four weeks from the stated date of issue. If in the event another report has been constructed and released on the companies mentioned in this report, the new recommendation supersedes this and therefore the recommendation in this report will become null and void.

Recommendation Definitions

SPECULATIVE BUY – 10% outperformance, high risk

BUY – 10% or more outperformance

ACCUMULATE - 10% or more is contingent on entry price and suggests exploiting any share price weakness

HOLD – 10% underperformance to 10% over performance

SELL – 10% or more underperformance

Period: During the forthcoming 12 months, at any time during that period and not necessarily just at the end of those 12 months.

1. Stocks included in this report have their expected performance measured relative to the ASX All Ordinaries index. DJ Carmichael Pty Limited's recommendation is made on the basis of absolute performance. Recommendations are adjusted accordingly as and when the index changes.

Risk Rank is developed to incorporate both market and total risk. The rankings for each category are based on the position of each stock relative to all other stocks covered in ASX300. The risk ranking is based on the following percentages:

1 = best 10%
2 = next 20%
3 = middle 40%
4 = next 20%
5 = bottom 10%

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