



Doray Minerals SPECULATIVE BUY

Current Price: **\$0.95**

Ticker: **DRM**
Sector: **Materials**

Shares on Issue (m): **74.6**
Market Cap (\$m): **70.9**
Cash (\$m): **23.0**
Enterprise Value (\$m): **47.9**

52 wk High/Low: **\$1.73** **\$0.56**
12m Av Daily Vol (m): **0.25**

Directors:

Brett Fraser Non-Executive Chairman
Allan Kelly Managing Director
Heath Hellewell Technical Director
Jay Stephenson Non-Executive Director

Substantial Shareholders:

Mr. Allen John Kelly 13.6%
Nedlands Nominees Pty Ltd 8.4%
Debnal Pty Ltd 5.2%

Share Price Graph



Analysts:
Patrick Chang
Troy Irvin
Tim Serjeant

15 April 2011

Bonanza Gold Discovery

Initiation:

Doray (DRM) is an emerging high grade gold explorer that owns strategic tenements in the Murchison Goldfields, WA. The region is well endowed with several large gold deposits (Great Fingall, Mt Magnet, Tuckabianna, Meekatharra, etc) in proximity to DRM's tenements. The Company is well funded (\$23m cash) and is pursuing an aggressive drilling campaign. DRM is managed by Allan Kelly, an ex-WMC geologist.

Impact:

Positive

Wilber (80% DRM) is one of Australia's highest grade virgin gold discoveries:

- Currently drilled to 230m, open along strike and at depth
- Initial resource of 174,000 oz @ 17.5g/t (172,000 @ 24.5g/t quartz vein)

View:

Positive

DRM offers resource upside:

- Potential strike and depth extension at Wilber could increase ounces
- The current drilling campaign is also testing flanking structures at Andy Well that is aimed at increasing the resource as well as ounces per vertical metre.
- The Andy Well resource is calculated using a conservative 75g/t top cut, hence the actual grade mined could be higher
- Strategic tenements in the Murchison Goldfields could host significant gold deposits

Production is targeted for December 2012:

- Andy Well is expected to be a low cost, high margin gold producer, with an expected base case production of 30-40kozpa.
- Argonaut projects modest start up capital expenditure
- The mining lease has been applied for and a mining study has commenced
- High recovery of >98% (>85% from gravity) from initial metallurgy tests

Catalysts include:

- Fully funded drilling campaign to test multiple lodes and depth extent
- Scoping/pre-feasibility study results, expected June 2011
- Resource upgrades throughout the year
- Mining lease application outcome, expected March quarter 2011

Recommendation:

Spec Buy

DRM's premium over its peers is arguably justified by the high grades and the strong likelihood of ongoing exploration success and resource upgrades. DRM's tangible exploration target implies a valuation of up to \$2.18. We initiate coverage with a Spec Buy recommendation.

Established Gold Province

Established gold district, well developed infrastructure

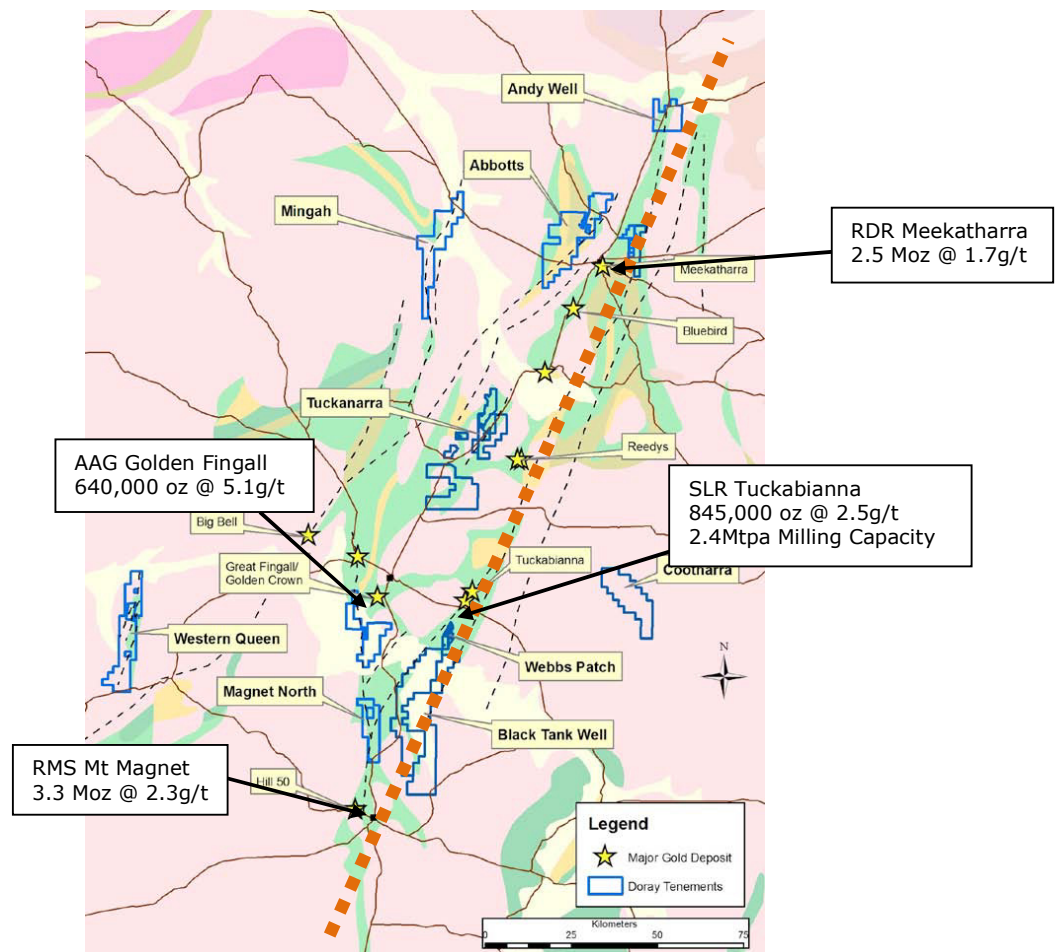
Gold was first discovered in the Murchison Goldfields in the 1880s. Infrastructure is well developed in the region, and there are numerous gold processing facilities nearby. Main developers in the region include Ramelius (RMS), Silver Lake (SLR) and Reed Resources (RDR). Historical production in the region includes 2.5 Moz from Big Bell, 1.2 Moz from Great Fingall, 2.3 Moz from Meekatharra, 1.2 Moz from Blue Bird, and 2 Moz from Hill 50.

Murchison Projects

DRM has an extensive land holding of over 1500km² in the Murchison province. The tenements cover most of the mineralisation structures and extend from Andy Well in the north to Webb Patch (adjacent to SLR's Tuckabianna Project) and Magnet North (north of RMS's Mt Magnet Project) to the south.

DRM is one of the dominant tenement holders in the region

Figure 1: Regional setting, and projects in development



Source: DRM modified by Argonaut

Region hosts numerous large gold deposits including some high grade lodes

The region hosts many large gold deposits, including

- Hill 50 (2Moz)
- Tuckabianna (1Moz)
- Meekatharra (3Moz)
- Golden Fingall (1Moz)
- Mt Magnet (3Moz)

Andy Well Project (DRM 80%)

Andy Well, an ex-WMC tenement, showed promise but was never thoroughly followed up

Andy Well is DRM's most advanced project. It is located 45km north of Meekatharra in WA. Previous owners of the tenement included WMC and BHP. Historic drilling returned promising results (e.g. 10m @ 7.2g/t) that were never thoroughly followed up. In addition, there has been little drilling beyond the first 100m.

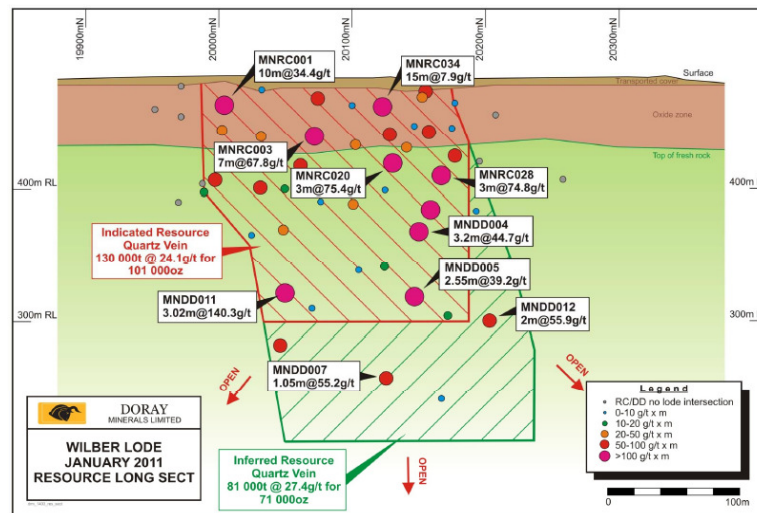
Reserves and resources

Very high grade resource base of 172,000 oz @ 24.5g/t....

The current resource on Wilber is 311kt @ 17.5 g/t (174koz), of which 139koz is attributed to DRM. The higher grade quartz vein component of the resource is 211kt @ 24.5 g/t (172koz), of which 137 koz is attributed to DRM. The resource is only drilled to a depth of 230m and is still open at depth. The quartz vein is about 2-3m thick and consistent in grade.

...drilled to 230m and open at depth...

Figure 2: Long section, Wilber Lode



Source: DRM

Geology

Andy Well is located on a greenstone belt that is folded and cross cut by younger intrusive dolerite dykes, quartz veins and metamorphosed porphyry. The area is largely concealed, but subcrops of banded iron formation, weathered schistose sedimentary and felsic rocks including quartz-sericite schist are present. Gold at Andy Well is predominantly hosted in a very thin unit of quartz vein. Andy Well was a blind discovery.

Proximal Prospects

...several adjacent lodes that have returned promising hits are being tested

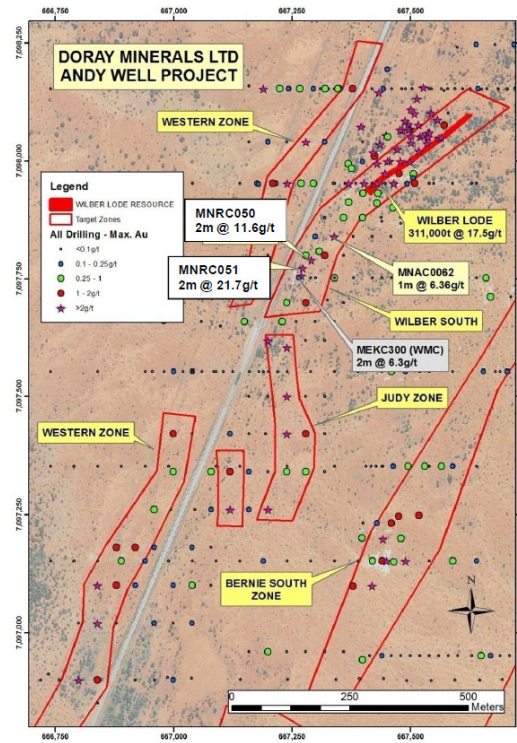
Structures along strike from Wilber and up to 7 parallel shear zones proximal to Wilber have been identified, with little drill testing beyond the first 100m. The company has planned an extensive drilling program to test these structures. Some encouraging results from these targets are listed below:

- Wilber South (along strike):
 - 2m @ 11.6 g/t
 - 2m @ 21.7 g/t
- Judy Zone (along strike):
 - 2m @ 18.7 g/t (EOH)
 - 5m @ 8.9 g/t, including 1m @ 46.9 g/t
 - 4m @ 3.23 g/t
- Bernie South (parallel)
 - 8m @ 13.9g/t including 2m @ 51.1 g/t

Structures adjacent to Wilber yet to be fully tested

Figure 3: Other local prospects

Shallow drilling around Wilber has identified several prospects yet to be fully tested.

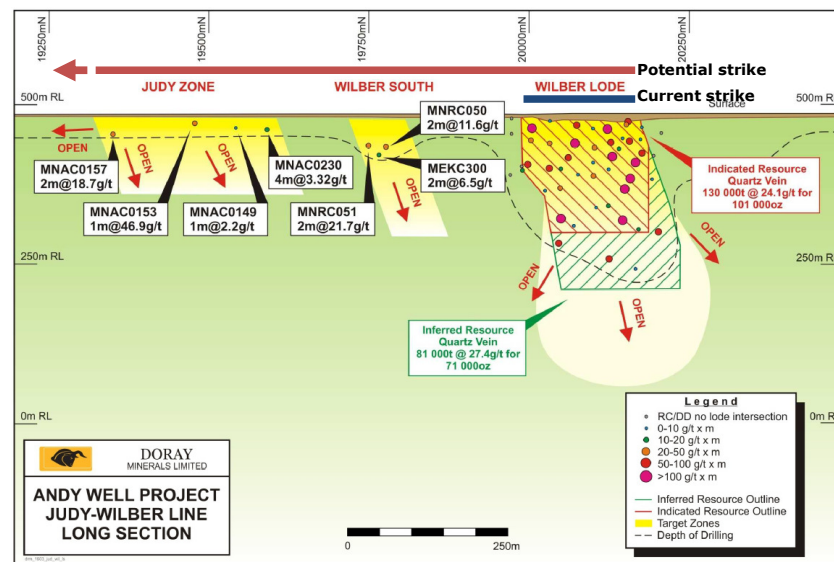


Source: DRM

Results from Wilber South and Judy Zone are considered highly encouraging as they could provide strike extensions and are also open at depth.

Potential to significantly increase strike and increase ounces per vertical metre

Figure 4: Long section, Wilber, Judy Zone and Wilber South



Source: DRM, modified by Argonaut

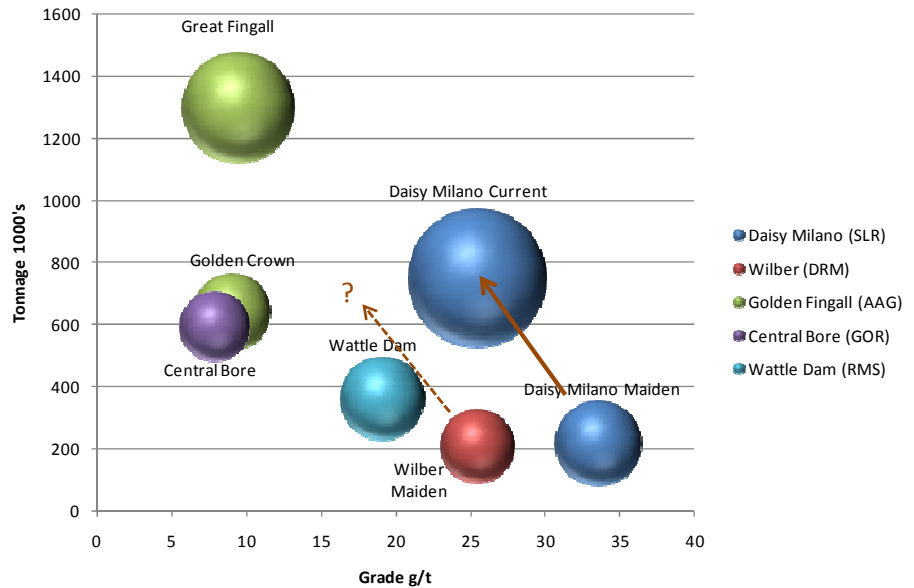
Resource Potential

Extending resources at Wilber along strike and at depth, as well as identifying new mineralisation at Andy Well could add significant ounces to the project. We compare the current resource at Wilber with several well known deposits to demonstrate the resource growth potential. Notably, both Daisy Milano and Wattle Dam started off with a modest resource at shallow depth, that progressively grew with depth extension.

Grade/tonnage comparison with other narrow vein, high grade deposits shows potential

Figure 5: Similar deposit grade tonnage comparison

High Grade Gold Deposit Comparisons



Source: Argonaut

Development Potential

Wilber with its current inventory could sustain small scale production...

Given the current tonnage and grade, Wilber could arguably justify a stand alone, low tonnage production scenario even without any depth extension or upside from other prospects in Andy Well. However upside from exploration is considered likely, given the excellent potential to add ounces from mineralisation along strike and at depth.

...it has comparable parameters with 'successful' high grade narrow vein deposits...

To demonstrate potential project economics, we compare Wilber to Great Fingall and Silver Lake Resource's Daisy Milano. Great Fingall is located in the Murchison region and Daisy Milano is situated east of Kalgoorlie. Both of them are narrow quartz vein deposit.

Figure 6: Wilber, Daisy Milano and Great Fingall comparison

| High Grade Narrow Vein Deposit Comparison | | | |
|---|---|--|--|
| | Daisy Milano (SLR) | Great Fingall | Wilber (DRM 80%) |
| Stope Width | <2m | 1-12m | ~2m? |
| Mineralisation | Quartz vein | Quartz vein | Quartz vein |
| Mining Method | Airleg | - | Airleg? |
| Cash Cost | ~\$600/oz | - | ~\$500/oz? |
| Strike Length | 400m | 200m | 200m, open along strike |
| Maiden Resource | 235,000 oz @ 33.55g/t (drilled to ~200m) | - | 172,200 oz @ 25.4g/t (drilled to ~230m) |
| Current/Future Resource | 598,000 oz @ 25.8g/t, excluding 14,000 oz @ 10g/t produced, open at depth | 1,610,000 oz @ 17g/t (produced and current), open ? at depth | |
| Oz per Vertical Metre | ~1100 | ~1300 | ~760 |
| Production Rate | 80,000 oz/pa | - | 45,000 oz/pa? |
| Flanking Structures | Daisy East 135,100 oz @ 38.3g/t Emma, Haoma, Rosemary | Golden Crown 482,000 @ 12g/t (produced & current) | Judy/Wilber South? Western Zone? Bernie? |

Source: Argonaut

...and it will get better if Judy Zone or South Wilber mineralisation extends down dip

The economics of the projects could significantly improve should structures along strike from Wilber (Wilber South, Judy Zone) continue at depth. Potential also exists should adjacent parallel structures (e.g. Bernie South, Western Zone) prove to host mineralisation. These discoveries could have a major impact on ounces per vertical metre. The proximity of these structures makes co-development an attractive proposition.

DRM has an internal target of achieving 500koz at the Andy Well project by December 2011. Argonaut considers this target achievable, given the following considerations.

- Wilber is open along strike and down dip. Drilling results suggest that mineralised structures exist south of and parallel to Wilber. These structures were not drilled below the first 100m, and hence remain open at depth
- The region's history of hosting high grade deposits that extend below 800m (e.g. Great Fingall, Golden Crown, Big Bell)

Possible Production Scenarios

Two production scenarios are presented below. Under the base case scenario we assumed no further exploration success. Mine life is 4 years with an average annual production of 45koz. Under the upside scenario we used DRM's internal exploration target of 500koz by December 2011. Mine life is 5 years with an average annual production of 93koz. Under both scenarios we assumed utilisation of Gekko modular gravity recovery plant(s) and toll treatment of concentrate at a nearby plant (e.g. Bluebird).

Under our base case scenario, Andy Well has an NPV of \$52M net to DRM

Figure 7: Preliminary project NPV

| Key Project Assumptions | | | |
|------------------------------------|----------|----------------|------------------|
| Andy Well Project | | Base Case | Upside Case |
| Ownership | % | 80 | 80 |
| First Production | | Dec-12 | Dec-12 |
| Ore milled | ktpa | 72 | 150 |
| Gold grade* | g/t Au | 20 | 20 |
| Gold recovery | % | 98 | 98 |
| Gold production* | koz | 45 | 93 |
| Mine Life | yrs | 4 | 5 |
| Capex | US\$m | 15 | 30 |
| Cash Costs - uninflated* | US\$/oz | 500 | 500 |
| Pricing | | | |
| Gold price | US\$/oz | 1400 | 1400 |
| Exchange rate | A\$:US\$ | 1 | 1 |
| Fiscal | | | |
| Government royalty | % | | 2.5 |
| Tax Rate | % | | 30 |
| Discount Rate | % | | 7.7 |
| *Denotes average over life of mine | | | |
| Summary Valuation | | | |
| Doray Minerals | | Base Case A\$m | Upside Case A\$m |
| Andy Well | | 52 | 135 |
| Murchison Tenements | | 10 | 10 |
| Corporate | | -5 | -5 |
| Cash Estimate | | 23 | 23 |
| Debt | | 0 | 0 |
| Total @ 7.7% Discount Rate | | 80 | 163 |
| A\$ps (undiluted) | | 1.07 | 2.18 |

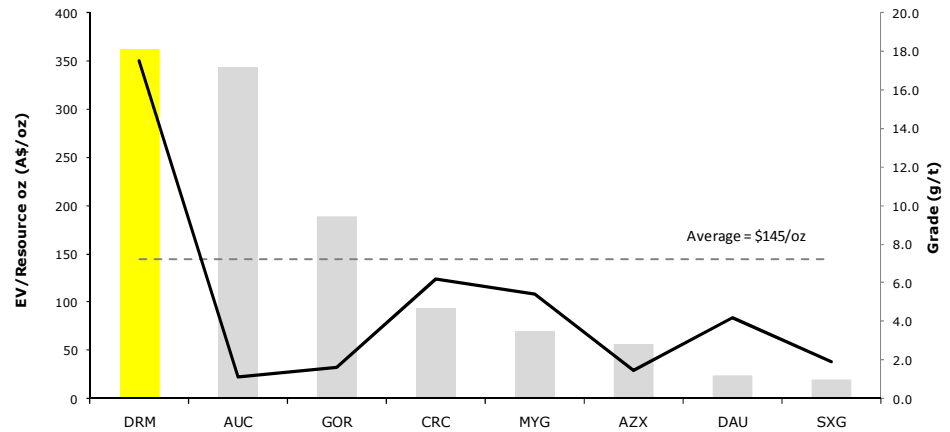
Source: Argonaut

Other production options might include toll treating all ore mined at a nearby plant. Subject to significant regional exploration success, DRM could potentially pursue a higher throughput CIL plant and blend high grade ore with low grade ore.

Peer Comparison

A peer comparison of Australian explorers is presented below.

Figure 8: Australian explorer peers - EV / Resource oz, and grade



Source: Argonaut

DRM is trading on an EV/resource oz of \$362 compared to a peer average of \$145. DRM's premium is arguably justified by the high grades and the likelihood of ongoing exploration success and resource upgrades.

Risks

Technical

The market may be expecting significant resource upgrades

As Wilber is only drilled to a depth of 230m, and significant value is attributed to exploration success, the uncertainty associated with strike and depth extension is the greatest risk.

The company is currently predominantly managed by geologists. Underground mine production expertise would need to be added to the company when DRM goes into production.

Due to its proximity to the current resource, a section of the Great Northern Highway might need to be realigned.

Financing

Low financial risk

Financing is needed to bring Wilber into production. However, given the high grade nature of the deposit an initial small scale production scenario is envisaged, requiring a modest amount of capital.

Permitting

Low permitting risk

The mining lease has been applied for and submitted. Argonaut perceives permitting risk to be low.

Summary

Argonaut initiates coverage with a SPEC BUY recommendation. Potential near term price catalysts include:

- Fully funded drilling campaign testing strike and depth extensions at Wilber, as well as multiple parallel structures, results expected throughout 2011
- Scoping/pre-feasibility study results expected June 2011
- Resource upgrades throughout 2011
- Mining lease application outcome expected March quarter 2011

Contact Details**Research:****Ian Christie**

Director Research
+61 8 9224 6872

Troy Irvin

Director Research
+61 8 9224 6871

Tim Serjeant

Associate Director Research
+61 8 9224 6806

Gianluca Paglia

Analyst
+61 8 9224 6824

Patrick Chang

Analyst
+61 8 9224 6835

Institutional Sales:**Paul Carter**

Executive Director
+61 8 9224 6864

Chris Wippl

Executive Director
Head of Research & Sales
+61 8 9224 6875

John Santul

Consultant, Sales & Research
+61 8 9224 6859

Damian Rooney

Senior Institutional Dealer
+61 8 9224 6862

Ben Willoughby

Institutional Dealer
+61 8 9224 6876

Bryan Johnson

Institutional Dealer
+61 8 9224 6834

Corporate and Retail Sales:**Kevin Johnson**

Executive Director
+61 8 9224 6880

Glen Colgan

Executive Director
+61 8 9224 6874

James McGlew

Director, Corporate Stockbroking
+61 8 9224 6866

Simon Lyons

Director, Retail Stockbroking
+61 8 9224 6881

Geoff Barnesby-Johnson

Senior Dealer
+61 8 9224 6854

Andrew Venn

Senior Dealer
+61 8 9224 6865

Melaney Brans

Dealer
+61 8 9224 6873

Cam Fraser

Dealer
+61 8 9224 6851

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