

UPDATE:

29th July 2011

Carbon Conscious Limited (CCF)

Price: \$0.30
 Mkt Cap: \$19.0m

Speculative Out Perform

Summary Information:

Capital Structure:

Share Price	\$0.30
Ord Shares	63.3m
Market Capitalisation	\$19.0m
Options	9.2m
Market Capitalisation (dil)	\$21.0m
Net Debt (June 2011)	\$3.0m
Enterprise Value	\$24.0m
52 week Low/High	8.5¢ / 38¢

Directors:

Exec Chairman	Steve Lowe
Chief Executive	Peter Balsarini
Non-Exec Director	Trevor Stoney
Non-Exec Director	Andrew McBain
Non-Exec Director	Kent Hunter
Non-Exec Director	Dr Robert Payne

Major Shareholders:

Broadacre Asset Management	8.9%
Stoney Pastoral Co	7.9%
Yall Super Fund	3.8%

Top 20 Shareholders hold 52.6% of the issued stock

Simplified Profit & Loss

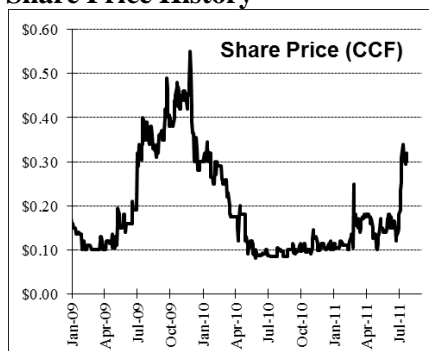
	FY12	FY13	FY14	FY15
Planted Ha	6,500	15,000	25,000	35,000
Revenue	\$14.5m	\$28.0m	\$50.0m	\$70.0m
EBITDA	\$4.5m	\$12.0m	\$23.8m	\$35.0m
NPAT	\$3.1m	\$7.5m	\$15.0m	\$17.5m

Margins

EBITDA	31.0%	42.8%	47.5%	50.0%
NPAT	21.4%	26.8%	28.5%	25.0%

FY12, 13 & 14 assume Origin exercise their option
 FY15 first full year at full tax payable

Share Price History



Company Description:

Carbon Conscious Limited (CCF) is an Australian company producing accredited carbon offsets in Australia and New Zealand by planting trees and establishing "Carbon Sinks".

This is achieved through the Carbon Capture Program™ which involves sourcing land, planting trees and generating carbon credits for businesses that are large emitters of carbon. Carbon is captured via Bio-Sequestration which is the process where the carbon in the atmosphere is stored during photosynthesis by trees in their stems, leaves, twigs and roots.

CCF has announced two large scale projects in Australia and one in New Zealand: 1) contract with Origin Energy for the "planting of millions of native Mallee Eucalypt trees" on 30,000 – 40,000 hectares, 2) contract with BP for the planting of up to 10m trees, and 3) \$11m contract with major Australasian energy company expanding the company's operations in the New Zealand market.

Investment Highlights:

- An investment in CCF is speculating that industrial carbon dioxide emissions will be priced either through a carbon tax or an emissions trading scheme.
- Ideally positioned in the fast growing carbon offset, and carbon trading sectors, which recently received a large boost with the announcement of the Governments Carbon Tax plan, which includes a fixed carbon price of \$23/t commencing 1 July 2012 until 2015 to be followed by a floating price.
- Carbon Conscious' business model is very straight forward, i.e. to produce carbon offsetting options (carbon credits) at a lower price than are available on the open market i.e. \$23/t.
- Have signed three significant contracts since July 2009 with major energy companies. Origin Energy and BP in Australia and an unnamed "Major Australasian energy company" in New Zealand. The calibre of these companies should provide investors with confidence in the Carbon Conscious product and business model.
- CCF is the only ASX listed company in the sector with an existing client option on commercial terms (\$190m) likely to come into play on passing of Australian carbon price legislation. These contracts combined with an extensive pipeline of further deals expected once carbon price legislation is passed provide an exciting future for the company.
- The carbon offset market is forecast to reach between \$4.0 - \$10.0 billion per annum by 2020, providing ample opportunity to grow the business.
- CCF has an established operations team with access to vast tracts of land and farmers and the capacity to scale up to approximately 40,000 hectares of annual planting per annum in Australia.
- CCF is trading at a large discount compared to the only other comparable ASX listed company, CO2 Group, which has a fully diluted market capitalisation in excess of \$100m, compared to CCF's market capitalisation of approximately \$20m.
- On approval of a carbon pricing system (estimated Sept / Oct 2011) and exercise of client contract options (\$190m), we would target a rerating of the company of between \$0.60 - \$1.00. However if a carbon pricing scheme fails to get approval we would expect a significant decrease in price.

Brief History:

Formed in Jan 2008	Carbon Conscious was incorporated in January 2008 to take advantage of opportunities in the domestic and international carbon credit or carbon offset markets.
Raised \$7.25m at 40¢ via IPO in mid 2008	CCF lodged a prospectus in March 2008 to raise up to A\$8m (A\$10m with over subscriptions) via the issue of up to 20m shares at an issue price of 40¢ per share. The group successfully commenced trading on the Australian Stock Exchange (ASX) on the 16 May 2008 after raising A\$7.25m via the issue of 18.1m shares at 40¢ per share. Signs its first carbon forest sink deal in May 2009 with leading Australian energy company Origin Energy, with a value of up to A\$169m (if all options exercised) over the 15 year life of the project. Fully executed the parties believe the deal is the largest carbon bio-sequestration deal in Australia to date.
Operating profit in FY10 and expected operating profit in FY11 pre-legislation	Following first payments from the Origin Energy deal, the group reports its first positive cashflow quarter for the September 2009 period. Signs a strategic "Tree Planting Carbon Offset Deal" during Oct 2009 with BP that involves the planting of up to 10m trees to absorb carbon from the atmosphere. BP's initial investment of A\$2.5m is considered a pilot stage of what could become a very significant part of BP's carbon management program in Australia. On 31 March 2011 CCF signed a deal with a "Major Australasian Energy Company" for \$11m involving planting pinus radiata (pine) trees over two planting seasons commencing in 2011 in New Zealand. The deal was the culmination of two years of work by the company to establish a NZ operation to take advantage of the established (since 2008 with the inclusion of forestry) NZ Emissions Trading Scheme.

Business Model

Business model to produce carbon credits significantly cheaper than the \$23/t fixed price

Carbon Conscious' business model is to produce carbon offsetting options (carbon credits) at a lower price than are available on the open market.

CCF aims to produce these carbon credits through "carbon farming", via the planting of Mallee Eucalypt trees in Australia's wheat-belt regions. Carbon farming has a unique role in the proposed Australian Government's Emission Trading Scheme as credits generated offer the only current domestic opportunity for large emitters of carbon to offset their emissions other than through the Government issuance of carbon certificates.

Three main business segments

Operates three main business segments

- 1) **Mandatory Clients**, which includes the 500 companies identified as having to pay the carbon tax. CCF acts as the Project Developer which includes land identification, carbon credit generation, ongoing monitoring and carbon inventory auditing. This option is designed for businesses seeking to own their own carbon estate asset, delivering a future stream of carbon credits. CCF generates income via initial project development fee, plantation fee, maintenance fee, and ongoing management fees. This option is targeted at clients e.g. Origin and BP who will have a liability under the emissions trading scheme and are looking to hedge the carbon price by investing upfront to gain access to a stream of carbon credits.
- 2) **Carbon Bank**, which involves CCF investing its own capital to generate carbon credits that can be either sold on the open market or held until such time as carbon prices warrant their sale. CCF generates income by selling credits in the spot market as they are generated or by holding and speculating that carbon prices will be higher than the cost to generate a carbon offset.
- 3) **Voluntary Clients**, enables individuals and commercial entities to offset their carbon emission footprint in the voluntary market. Notable clients include Wesfarmers Insurance, The City of Perth, iinet, and Homeloans. It is expected that the Voluntary segment of the business will be a minor part compared to the mandatory.

Key assumptions for business success

- 1) There will be a market through which to sell carbon credits
- 2) Able to produce carbon credits at a competitive price to the open market
- 3) Access to suitable land to enable the establishment of "carbon farming".

Major Economic Assumptions - Australia

Figures used below should be used as a rough guide only, and are designed to give a broad indication of the economics of the industry in Australia.

Financial modelling assumptions used by Carbon Conscious (which are similar to assumptions used by other companies in the industry) show that:

Costs per hectare

Planting and land are major expenses	- Land cost (purchased);	\$650 – \$1,100	avg \$875
	- Planting costs	\$750 – \$1,100	avg \$925
	- Maintenance cost (p.a.)	\$20.00 – \$40.00	avg \$30

Therefore total cost per hectare varies between \$1,700 and \$2,800 (average \$2,250), or between \$115 and \$190 per annum (assuming 15 year period of carbon credit generation).

Value created per hectare (per annum)

Carbon valued at \$23 per tonne	- Carbon credit value	\$20/t – \$25/t	avg \$23
	- Carbon generated	10t – 15t p.a.	avg 12.5t
	- Total value created	\$200 – \$450	avg \$312

In Australia 1 hectare generates between 10 and 15 tonnes of carbon offset p.a.

Therefore carbon credits valued at between \$200 and \$450 (average \$312) is generated per hectare per annum for a cost of between \$115 and \$190/t per hectare per annum.

Operating value per hectare per annum of \$135 – \$300, so a 1,000 hectare plantation theoretically produces between \$130,000 and \$300,000 operating profit per annum.

However as always there is a hitch, which in this case is that the cost of the land and planting occurs in the first year so the time value must be taken into account (depreciation), similar to building an office block and then leasing it out for next 15 years.

The likelihood of an increasing carbon price over time is likely to offset the time value of money alluded to above, with Macquarie Bank forecast a price of at least A\$50/t required to achieve the Governments carbon reduction plans, and treasury modelling forecasting a price of \$50/t by 2020 (2005 dollars).

40 – 50% of contract value received in first year

It is for this reason that Carbon Conscious charge a project development and plantation fee that ranges from 40% - 50% of the contract value signed under the **complete package option**.

Rough Financial model

Our rough financial models generate the following operating outcomes, which can be used to forecast potential profitability of the group at the operational level.

1,000 trees = 1ha

Simple rule of thumb: 1,000 trees = 1ha, or 1 million trees = 1,000ha

Operating costs and profitability are based on the average costs mentioned above and a carbon price of A\$23/t.

Per hectare basis

\$800 gross profit per hectare planted in the first year (design and plantation fees, excludes land cost)

\$15 gross profit per hectare per year for 15 years (management fee, includes land cost)

Per tree basis

\$800,000 gross profit per 1million trees planted in first year (design and plantation fees excludes land cost)

\$15,000 gross profit per 1 million trees per year for 15 years (ongoing management fee, includes land cost)

Simple financial model to determine rough value of contracts to CCF

Management expenses running approx. \$2.0mp.a.

Management expenses (salaries, office lease, consumables, etc) have averaged approx. \$2.0 million per annum over the last 12 months, however these expenses are expect to increase going forward as the company grows.

When fully up and running (FY2014 onwards), we would expect an EBITDA Margin of 50% and an NPAT Margin of 25%

Deals signed to Date**Origin Energy Deal**

First major deal for CCF signed with Origin Energy

On the 16 July 2009, Carbon Conscious Limited and Origin Energy Limited successfully completed due diligence and signed contracts for what both parties believe will be the largest carbon bio sequestration project in Australia to date, if fully exercised.

The contract involves Origin paying Carbon Conscious to plant millions of native Mallee Eucalypt trees on less viable agricultural land in the wheat-belt regions of Australia for the production of Carbon Permits tradable under the Commonwealth Government's Carbon Price or Emissions Trading Scheme (ETS).

\$45m initial face value

Origin has engaged Carbon Conscious to establish environmental carbon offset plantings over the first 4 seasons (2009, 2010, 2011 and 2012). These plantings will have a face value of approximately \$45 million and comprise both upfront planting and ongoing licence and management fees payable over the 15-year term of the arrangement.

Potential value in excess of \$200m if Origin exercise all its options

Carbon Conscious has also provided options for Origin to take up further plantings between 2012 and 2015. The face value of these additional plantings is up to \$190 million and would be paid in a combination of upfront planting and ongoing licence and management fees for 15 years post planting. If the options are exercised by Origin in full, the deal would represent what the parties believe will be the largest carbon forest sink development program in Australia to date with a value in excess of \$200 million to be paid over the 15-year life of the project.

BP Deal

Second deal signed within 6 months

On the 14 October 2009 Carbon Conscious Limited and BP signed contracts for a large scale Australian bio sequestration project involving the planting of up to 10 million trees to absorb carbon from the atmosphere.

The deal signals an important move by BP to secure capacity in the Australian carbon forest sink industry. The contract involves BP paying CCF to create large scale commercial plantings of Mallee Eucalypt trees on less viable agricultural land in the wheat-belt regions of Australia.

BP treating as a pilot program that may lead to significant increases over time

While large scale tree planting will substantially reduce land salinity and erosion problems, the deal is driven by the production of carbon credits tradable under the Australian Government's proposed ETS.

BP's regional director of emissions offsets, Mr Rajeev Suri said: "Our agreement with Carbon Conscious is an important step for BP in this region. We see this contract as potentially the initial stage or pilot of what could be a very significant part of BP's carbon management in Australia. This deal offers BP an investment structure and additional environmental benefits and it provides the foundation for an ongoing and mutually beneficial relationship with Carbon Conscious."

NZ Deal

First deal signed outside of Australia, and provides template for further offshore transactions

On 31 March 2011 CCF signed a deal with a "Major Australasian Energy Company" for \$11m involving planting *pinus radiata* (pine) trees over two planting seasons commencing in 2011. The deal was the culmination of two years of work by the company to establish a NZ operation to take advantage of the established (since 2008 with the inclusion of forestry) NZ Emissions Trading Scheme.

The deal was one of the earliest transactions undertaken in NZ and the first of its type by any ASX listed carbon forest sink developers. This has given the company an excellent platform for further success in the NZ market and has assisted greatly with building a further NZ deal pipeline.

By completing this transaction CCF has proved that it can leverage its knowledge, reputation and experience in a new and exciting market outside its Australian base.

Australian Carbon Price Legislation

Carbon Price legislation goes before Parliament in less than 6 weeks

The Australian Parliament is due to vote on the Government's proposed Carbon Pricing Scheme as early as late August 2011. Below we have summarised the major points of the Carbon Price legislation.

Design of the Carbon Price

Carbon price applies to emitters of 25,000t or more of CO₂ p.a.

The Carbon Price will require any company that owns an industrial facility that emits more than 25,000 tonnes (expected to be approximately 500 companies) of greenhouse gases per year, to pay a fixed \$23 / tonne from July 1 2012 rising by 2.5% p.a. From 2015 the fixed price will switch to a floating price or an Emissions Trading Scheme "ETS" in which the market will decide the price of carbon pollution. The available number of emissions permits will be strictly controlled and it is through controlling the number of permits that Australia will cap its greenhouse gas emissions. Each year the liable business must surrender sufficient permits to cover their emissions. If they do not have enough permits to cover their emissions, they will be subject to penalties. As the ETS rolls forward, fewer and fewer permits will be made available.

The size of the Australian carbon market

By 2020 CO₂ market potentially worth \$5.0 - \$10.0 B per annum.

Through the Carbon Price and ETS the Government intends to reduce Australia's carbon pollution by 5% below 2000 levels (553 Mt CO₂-e) by 2020. In 2020, emissions are projected to be 664 Mt CO₂-e or 120% of 2000 levels.

The 'abatement challenge' is approximately 160 Mt CO₂ under a 5% target option and 249 Mt CO₂ under a 25% target option. Using a \$40/t CO₂ carbon price the size of the abatement challenge is \$5.2B - \$9.9B.

Discharging a liability under the ETS

In managing an organisation's liability under the ETS it is likely that several options will be utilised. The first will be to reduce the organisation's own emissions where possible, thus reducing the required number of carbon permits. Beyond reducing emissions and trading in Government issued permits, carbon credits from activities such as forestry will be tradable under Australia's pending ETS to offset an organisation's liability.

Australian Carbon Credit Units (ACCU's)

Reforestation to be the major source of domestic carbon credits called ACCU's.

ACCU's are Government permits issued under the Carbon Farming Initiative (CFI) generated mainly from activities such as forestry. ACCU's will be used by emitters to offset their liability under the Carbon Price. During the fixed price period a maximum of 5% can be used by emitters to satisfy their liability, this limit becomes unlimited in 2015.

A Few Final Thoughts

An investment in CCF is speculating that carbon will be priced

An investment in Carbon Conscious is speculating that industrial carbon dioxide emissions will be priced either through a carbon tax or an emissions trading scheme.

Carbon Conscious has positioned itself for the eventual pricing of carbon and what is forecast to be a major growth area over the next decade, as carbon emitter's source carbon credits to offset their emissions.

CCF trades at a large discount to ASX listed competitor

The carbon offset market is forecast to reach \$4.0 - \$10.0 billion per annum by 2020 (depending on whether 5% or 25% offset target is used), providing ample opportunity to grow the business.

CCF trades at a large discount compared to the only other comparable ASX listed company, CO₂ Group, which has a fully diluted market capitalisation in excess of \$100m, compared to CCF's market capitalisation of approximately \$20m.

In a relatively short time period, management of CCF have shown an ability to deliver on its prelisting ambitions of: 1) finalising deals with strong counter parties Origin Energy and BP, 2) producing positive free cash-flows and, 3) establishing a New Zealand business. This progress is all the more impressive when considered it was accomplished amidst the global financial crisis and continued uncertainty around the implementation of the Australian carbon price legislation.

Price Targets

Approval to price carbon & exercise of \$190m of contract options: \$0.60 - \$1.00.

It is hard to put a value or price target on Carbon Conscious today due to the largely divided nature of the carbon pricing debate in Australia at present. However, if a carbon pricing system is introduced and clients options worth \$190m exercised, we would expect a price target range of \$0.60 - \$1.00. If the pricing scheme fails to get up we would expect the share price to retreat significantly.

In order for Carbon Conscious' business model to thrive it is reliant on a carbon price (whether through a carbon tax or a carbon trading scheme), without a carbon price, the company will struggle in Australia, although we believe it will still survive and focus on New Zealand and other jurisdictions that already have a carbon price.

Carbon Conscious Limited Directors

Mr. Stephen Lowe Exec Chairman	Mr Lowe has over 28 years' experience in capital and financial markets, with a focus on energy commodities. He previously held the role of General Manager Trading with Integral Energy, a government owned electricity, distribution and retailing company, for over five years. Mr Lowe is the COO of a renewable energy company that will be converting waste to energy. He brings to Carbon Conscious senior relationships with major energy and mining companies, investment banks and fund managers in national and international markets.
Mr. Peter Balsarini Chief Executive Officer	Mr Balsarini holds a Bachelor of Economics and a Masters Degree in Business. He has over 18 years' experience in the financial services industry having spent considerable time both as a public accountant and CFO of a Funds Management business. His experience spans project feasibility, investment analysis, staff management, product development and distribution amongst others. He has significant experience in the development and operation of Managed Investment Schemes, including regulatory and compliance requirements.
Mr. Trevor Stoney Non-Exec Director	Mr Stoney brings more than 48 years of involvement, knowledge and relationships within the agricultural industry to Carbon Conscious. From 1962 until the farm's sale in 2009, Mr Stoney managed his family's mixed farming operations of 70,000 acres which stretched from Dongara in the mid-west, Esperance in the south and Donnybrook in the south-west of Western Australia.
Mr. Andrew McBain Non-Exec Director	Mr McBain was the founder and initial developer of the Carbon Conscious business and has previously served on the Board as a non-executive director. Mr McBain is tasked with assisting Carbon Conscious with investor and shareholder relations, communication and awareness as the Company increases its activities ahead of proposed carbon legislation which is expected to be introduced by the Federal Government in 2011
Mr. Kent Hunter Non-Exec Director	Mr Hunter is a Chartered Accountant with over 17 years corporate and company secretarial experience. He has been involved in the listing of over 20 companies on ASX in the past 9 years. He has experience in capital raisings, ASX compliance and regulatory requirements
Dr. Robert Payne Non-Exec Director	Dr Payne has significant corporate finance and operational experience coupled with technical expertise in the financial, industrial, resources and technology sectors. Between 2000 and 2006 he was Chief Executive Officer of State Development Fund Limited.

The author of this report currently owns shares (personally or by related parties) in CEU, ERA, GFF, IEC, IECO, MUB, MUBO, TAH and WPI.

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