

Quarterly Activities Report and Appendix 5B

For the period
ending
30 September
2012

ASX: ARU



**AN EMERGING
RARE EARTHS
PRODUCER
FOR USERS
WORLDWIDE**

HIGHLIGHTS



Definitive Nolans Rare Earths Project Update completed;



Independent Expert's Report:

- Values the Nolans Project at A\$3,200 million – more than 30 times its current market capitalisation; and
- Validates the advanced progress of the Nolans Project using a discounted cash flow method;



Significant progress made in technical and engineering feasibility work streams;



Share Placement with major shareholder approved;



Tax Refund of A\$22.5 million received for R&D spend

SUMMARY

NOLANS PROJECT UPDATE

A major highlight of the September quarter FY13 was the completion and release of the definitive Nolans Project Update Report in August. This comprehensive document provides a detailed overview of the history and development of the Nolans Project, the accomplishments to date and what is required going forward to bring the Nolans Project to construction and ultimate production.

Through an advanced Feasibility Study, the Company has established a Base Case for the Nolans Project. This includes a mine and concentrator at Nolans Bore in the Northern Territory, and a chemical processing operation at Whyalla in South Australia. The Project's Base Case is expected to produce 20,000 tonnes per annum of Rare Earth Oxide products, generating a Net Present Value ("NPV") of A\$4.3 billion (at a 10% discount rate) and an internal rate of return ("IRR") of 30%, on an after tax basis. The Base Case projects a strong financial return over a 20 year period, with a capital payback within four years of operation.

Key findings disclosed in the Nolans Project Update Report include:

- Arafura's extensive testwork program has provided the Company with a detailed understanding of its resource and mineralogy, as well as the steps required to progress through to the production of separated REO products.
- The Nolans Project process flow sheet has taken the Company and its technology partners approximately seven years to develop. It is based on an extensive laboratory pilot plant and demonstration plant test work program; and has been augmented by detailed process modelling from mine to final products.
- The Nolans Bore resource is low risk and has a long life based on the Project's planned rate of production. It also has the potential for expansion at depth. In addition, the test work program carried out by Arafura has significantly de-risked the process route.

ARAFURA RESOURCES LIMITED

arafura@arafuraresources.com.au www.arafuraresources.com.au ABN 22 080 933 455

PERTH: Level 5/16 St Georges Tce, Perth WA 6000 | PO Box 5773, St Georges Terrace, Perth WA 6831 T: +618 6210 7666 F: +618 9221 7966

DARWIN: 18 Menmuir St, Winnellie NT 0820 | PO Box 37220, Winnellie NT 0821 T: +618 8947 5588 F: +618 8947 5599

WHYALLA: Unit 18, 11 Darling Tce, Whyalla SA 5600 | PO Box 511, Whyalla SA 5600 T: +618 8645 5509 F: +618 8645 1856



- The Company has a clearly defined program through to completion of the Nolans Project.
- The core capital cost, estimated by top tier engineering consultants for the Project's Base Case, is A\$1,395 million, with an ancillary plant estimated to be an additional A\$517 million. This estimate includes provisions for indirect costs and contingencies of A\$502 million.
- The Base Case price assumed for Arafura's REO product range starts at US\$60/kg in 2012, growing at a nominal 2.8% per annum up until 2025. The Project's high value, high-growth Didymium Oxide (mixed Neodymium and Praseodymium Oxide) product is expected to generate 50-60% of total revenue from the Nolans Project.
- Operating costs average A\$20.55/kg of REO products in real 2012 terms, before credits for phosphate, uranium and gypsum co-products.
- Both the Nolans Bore and Whyalla sites have access to existing public infrastructure, services and utilities. Furthermore, environmental studies at both sites are advanced and no significant issues have emerged.
- Arafura has executed a MOU with two multinational companies for offtake and assistance with project development and/or funding. The Company will be seeking to lock these in, and other offtake agreements, prior to arranging funding for further development of the Project.
- The Nolans Project is likely to be one of very few, new sources of rare earths supply this decade. There is expected to be a global shortfall in certain REO products in the medium to long term, particularly Didymium Oxide. In this scenario, the Nolans Project has a strong representation of Didymium Oxide in its product mix.
- The Nolans Project has received positive community engagement and support, as well as government support at Federal and State/Territory levels.

NOLANS PROJECT – TECHNICAL AND ENGINEERING ACTIVITIES

During the quarter the Company made significant progress on a number of Base Case feasibility work streams aimed at achieving the key milestone of raising finance for the Project. This included:

- Scoping for production of a separated Lanthanum Oxide product to 99% purity;
- Refinement of marketing samples and offtake negotiations;
- Progressing Environmental Impact Statement studies;
- Mine and Plant Design engineering to levels of +/- 25% accuracy;
- Transport, logistics and raw material estimates to +/- 25% accuracy; and
- Information Memoranda for potential investors and financiers.

A key final step to validate the process flow sheet and mass balance, as well as the major recycle circuits, is the successful operation of an Integrated Pilot Plant ("IPP"), which will be constructed early next year. The IPP results will also be used to verify the final engineering design.

The Company is also assessing a number of options for process improvements and work on this program is scheduled for completion by the end of 2012. The results may change the Base Case if they deliver benefits to Project economics and satisfy the Company's criteria for inclusion.



Environment, Health, Safety and Community

The flora and fauna reports for the Whyalla site are now complete and these will be presented and discussed with local stakeholders in the near future. Regional ground water surveys have now been conducted in the Nolans Bore area for more than a full seasonal cycle, and have yielded robust information that supports the sustainability of the ground water resource.

During the quarter the Company also achieved the milestone of one year injury free.

The recent Northern Territory elections have resulted in a change of government and subsequently, Arafura has provided ministerial briefings on the Project during which the Company continued to receive support for the development of the Project. Local stakeholder engagement continued during the quarter in the Northern Territory, with organisations such as the Central Desert Shire; the Regional Development Authority and Native Title holders.

In South Australia, the delay of the Olympic Dam expansion and suspension of the proposed ammonium nitrate plant study near Whyalla has increased the focus on Arafura.

INDEPENDENT EXPERT'S REPORT

Arafura engaged BDO Corporate Finance (WA) Pty Ltd as the Independent Expert ("IE") to prepare an Independent Expert's Report ("IER") to determine if the share placement to the Company's major shareholder ECE Nolans Investment Company Proprietary Limited ("ECE Nolans") is fair and reasonable.

The IE estimates the fair market value of the Nolans Project to be in the range of A\$2,400 million to A\$4,000 million, with a preferred value of A\$3,200 million. Notably, even at the lower end of the valuation range, the Net Present Value of the Nolans Project is more than 30 times the Company's current market capitalisation. This is consistent with Arafura's valuation as presented in the Nolans Project Update in August (07/08/12).

In addition, the IE has assessed the value of an Arafura share to be in the range of A\$0.243 to A\$0.404 per share, with a preferred value of A\$0.323. As such, the IE determined that the share placement to ECE Nolans transaction at a cash consideration of A\$0.22 per share was 'not fair but reasonable,' as the advantages of the placement to shareholders are greater than the disadvantages.

Further, the IE notes that the placement to ECE Nolans can assist in providing a part of the significant funds required to complete the Nolans Project feasibility study.

Overall, the IE's valuation using a DCF analysis provides an encouraging third party validation of the strong progress and advanced stage of the Nolans Project. This has prompted the Company to request an independent assessment of whether the Mineral Resource at Nolans Bore can be converted to an Ore Reserve. This process will further underpin the feasibility and valuation of the Nolans Project and, more importantly, has the potential to open up a wider range of funding opportunities.

SHARE SUBSCRIPTION AGREEMENT WITH MAJOR SHAREHOLDER

The Share Subscription Agreement ("SSA") between ECE Nolans and Arafura was formally executed in September. Under the agreement, ECE Nolans agreed to subscribe for 45,266,500 shares in the Company, at an issue price of A\$0.22 per share and totalling A\$9.9 million.



The SSA was subject to a number of approvals including:

- Australian Government Foreign Investment Review Board (“FIRB”);
- People’s Republic of China Government (“PRC”); and
- Arafura Shareholders.

The Extraordinary General Meeting (EGM) to approve the SSA on the terms set out in the Explanatory Memorandum (18/09/12) was held on 18 October 2012, with a successful outcome. The Company has received notification of FIRB approval for the transaction. Approval has similarly been received from the Jiangsu Provincial Government, and PRC approval is expected imminently.

The transaction represents 8.75% of Arafura’s issued capital, whereby following the transaction, ECE Nolans will hold 24.86% (previously 16.27%).

The funds received from the share placement will assist Arafura to meet its short-term funding requirements as the Company progresses towards project finance in 2013.

RESEARCH AND DEVELOPMENT TAX REFUND

The Company has received an amount of A\$22.5 million representing a tax refund for eligible research and development (“R&D”) expenditure in relation to the development of the Nolans Project. The R&D Tax Incentive is an Australian Government program assisting businesses to offset a portion of costs relating to eligible R&D activities and innovation. It aims to boost competitiveness and improve productivity across the Australian economy as well as encourage R&D activities that may not otherwise have been conducted.

Unique aspects of Arafura’s rare earths extraction process, which have been developed over a number of years, continue to be eligible. In 2006, Arafura received an A\$3.3 million AusIndustry Commercial Ready Grant and, since then, eligible R&D expenditure has been carried forward as potential future tax offsets. In 2010 the Australian Government changed the R&D Incentive program to the current scheme. The R&D Incentive is jointly administered by AusIndustry (on behalf of Innovation Australia) and the Australian Taxation Office.

EXPLORATION

JERVOIS (Fe-V-Ti)

Arafura executed a farm-in agreement with Rox Resources Limited (“Rox”) during October for Rox to acquire up to 70% of the exploration and development rights to base and precious metals (Cu, Pb, Zn, Au, Bi, Ag, PGEs) on ELs 10215 and 26812. The terms of the agreement include Rox spending:

- A minimum of \$150,000 in the first year before Rox can withdraw;
- \$500,000 in the first two years to earn 51% of the rights, whereupon a JV is formed between the parties; and
- An additional \$1,000,000 during the subsequent two years to acquire 70% of the rights.

The agreement is subject to a 30 day due diligence period and a number of other conditions precedent.

CORPORATE

STRATEGY

Arafura aims to be a recognised leading producer of Rare Earths for users worldwide and has an exploration and development program to grow its position in Rare Earth projects beyond the Nolans Project. The Company will specialise in Rare Earths products and their markets.

GROWTH – DEVELOPMENT

Arafura's primary focus is to develop its 100%-owned Nolans Rare Earths Project. The Nolans Bore deposit has a resource to sustain a mine life of over 30 years and Arafura has developed a processing flowsheet that optimises the extraction of rare earths, phosphate and uranium.

GROWTH – EXPLORATION

Long-term sustainable development and the creation of shareholder wealth can also be realised through exploration success. Arafura has exploration projects in rare earths, gold, base metals and iron-vanadium, and will assess other exploration opportunities that are consistent with additional growth beyond the Nolans Project.

OUTLOOK

Arafura is on track to become one of the world's largest Rare Earths producers and certainly one of the very few new Rare Earth suppliers this decade. The global market outlook continues to provide confidence in the Company's strategy.

The expected Rare Earths supply shortfall within the next decade, particularly in Neodymium, is likely to coincide with Arafura's production and commercialisation pathway, while the growing demand for Rare Earths in the green technology sector is expected to drive the Company's sales.

Arafura is well-placed to capitalise on this market opportunity with the Nolans Project. The project's advanced position is a key point of difference over other Rare Earth development projects and the Company has a clear way forward in the development of the Nolans Project that significantly de-risks the path to production and commercialisation.



Appendix 5B

Mining exploration entity quarterly report

Introduced 1/7/96. Origin: Appendix 8. Amended 1/7/97, 1/7/98, 30/9/01, 01/06/10.

Name of entity

ARAFURA RESOURCES LIMITED

ABN

22 080 933 455

Quarter ended ("current quarter")

30 September 2012

Consolidated statement of cash flows

		Current Quarter \$A'000	Year to date (3 months) \$A'000
Cash flows related to operating activities			
1.1	Receipts from product sales and related debtors	-	-
1.2	Payments for (a) exploration & evaluation	(2,479)	(2,479)
	(b) development	(756)	(756)
	(c) production	-	-
	(d) administration	(1,268)	(1,268)
1.3	Dividends received	-	-
1.4	Interest and other items of a similar nature received	204	204
1.5	Interest and other costs of finance paid	(1)	(1)
1.6	Income taxes paid	-	-
1.7	Other (provide details if material)	-	-
		(4,300)	(4,300)
Net Operating Cash Flows			
Cash flows related to investing activities			
1.8	Payment for purchases of: (a) prospects	-	-
	(b) equity investments	-	-
	(c) other fixed assets	(40)	(40)
1.9	Proceeds from sale of: (a) prospects	-	-
	(b) equity investments	-	-
	(c) other fixed assets	-	-
1.10	Loans to other entities	-	-
1.11	Loans repaid by other entities	-	-
1.12	Other (provide details if material)	-	-
		(40)	(40)
Net investing cash flows			
1.13	Total operating and investing cash flows (carried forward)	(4,340)	(4,340)

+ See chapter 19 for defined terms.

17/12/2010 Appendix 5B

1.13	Total operating and investing cash flows (brought forward)	(4,340)	(4,340)
Cash flows related to financing activities			
1.14	Proceeds from issues of shares, options, etc.	-	-
1.15	Proceeds from sale of forfeited shares	-	-
1.16	Proceeds from borrowings	-	-
1.17	Repayment of borrowings	-	-
1.18	Dividends paid	-	-
1.19	Other – Capital Raising Expenses	(5)	(5)
	Net financing cash flows	(5)	(5)
Net increase (decrease) in cash held		(4,345)	(4,345)
1.20	Cash at beginning of quarter/year to date	19,546	19,946
1.21	Exchange rate adjustments to item 1.20	(19)	(19)
1.22	Cash at end of quarter	15,182	15,182

Payments to directors of the entity and associates of the directors

Payments to related entities of the entity and associates of the related entities

		Current Quarter \$A'000
1.23	Aggregate amount of payments to the parties included in item 1.2	(187)
1.24	Aggregate amount of loans to the parties included in item 1.10	Nil
1.25	Explanation necessary for an understanding of the transactions	
	Salaries, fees, superannuation and consulting services at standard commercial rates.	

Non-cash financing and investing activities

- 2.1 Details of financing and investing transactions which have had a material effect on consolidated assets and liabilities but did not involve cash flows

Nil

- 2.2 Details of outlays made by other entities to establish or increase their share in projects in which the reporting entity has an interest

Nil



Financing facilities available

Add notes as necessary for an understanding of the position

	Amount available \$A'000	Amount used \$A'000
3.1 Loan facilities	Nil	Nil
3.2 Credit standby arrangements	Nil	Nil

Estimated cash outflows for next quarter

	\$A'000
4.1 Exploration and evaluation	4,855
4.2 Development	3,580
4.3 Production	-
4.4 Administration	2,044
Total	10,479

Reconciliation of cash

Reconciliation of cash at the end of the quarter (as shown in the consolidated statement of cash flows) to the related items in the accounts is as follows.

	Current Quarter \$A'000	Previous Quarter \$A'000
5.1 Cash on hand and at bank	5,182	5,182
5.2 Deposits at call	10,000	10,000
5.3 Bank overdraft	-	-
5.4 Other (provide details)	-	-
Total: cash at end of quarter (item 1.22)	15,182	15,182

Changes in interests in mining tenements

	Tenement reference	Nature of interest (note (2))	Interest at beginning of quarter	Interest at end of quarter
6.1 Interests in mining tenements relinquished, reduced or lapsed	EL 10215	Lease	88 blocks	71 blocks
Interests in mining tenements acquired or increased				

+ See chapter 19 for defined terms.
17/12/2010 Appendix 5B



Issued and quoted securities at end of current quarter

Description includes rate of interest and any redemption or conversion rights together with prices and dates.

		Total number	Number quoted	Issue price per security (see note 3)	Amount paid up per security (see note 3)
7.1	Preference + securities (description)				
7.2	Changes during quarter (a) Increases through issues (b) Decreases through returns of capital, buy-backs, redemptions				
7.3	+ Ordinary securities	396,004,144	396,004,144		
7.4	Changes during quarter (a) Increases through issues (b) Decreases through returns of capital, buy-backs				
7.5	+ Convertible debt securities (description)				
7.6	Changes during quarter (a) Increases through issues (b) Decreases through securities matured, converted				
7.7	Options			<i>Exercise price</i>	<i>Expiry date</i>
	ARUAI	2,700,000	-	\$0.85	31-12-13
	ARUAO	1,100,000	-	\$1.19	31-12-12
	ARUAK	850,000	-	\$0.75	20-07-13
	ARUAQ	750,000	-	\$0.98	31-08-13
	ARUAY	750,000	-	\$1.08	14-09-13
	ARUAD	1,100,000	-	\$1.54	26-11-13
	ARUAU	1,400,000	-	\$0.96	16-07-14
	ARUAM	700,000	-	\$0.81	31-12-14
	ARUAW	2,150,000	-	\$0.70	24-11-14
7.8	Issued during quarter				
7.9	Exercised during quarter				

+ See chapter 19 for defined terms.

17/12/2010 Appendix 5B



7.10 Expired during quarter

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7.11 **Debentures**
(totals only)

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7.12 **Unsecured notes**
(totals only)

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Compliance statement

1 This statement has been prepared under accounting policies which comply with accounting standards as defined in the Corporations Act or other standards acceptable to ASX (see note 4).

2 This statement does give a true and fair view of the matters disclosed.

Sign here:

Date: 30 October 2012

Print name: Gavin Lockyer
(Company secretary)

Notes

1 The quarterly report provides a basis for informing the market how the entity's activities have been financed for the past quarter and the effect on its cash position. An entity wanting to disclose additional information is encouraged to do so, in a note or notes attached to this report.

2 The "Nature of interest" (items 6.1 and 6.2) includes options in respect of interests in mining tenements acquired, exercised or lapsed during the reporting period. If the entity is involved in a joint venture agreement and there are conditions precedent which will change its percentage interest in a mining tenement, it should disclose the change of percentage interest and conditions precedent in the list required for items 6.1 and 6.2.

3 **Issued and quoted securities** the issue price and amount paid up is not required in items 7.1 and 7.3 for fully paid securities.

4 The definitions in, and provisions of, *AASB 1022: Accounting for Extractive Industries* and *AASB 1026: Statement of Cash Flows* apply to this report.

5 **Accounting Standards** ASX will accept, for example, the use of International Accounting Standards for foreign entities. If the standards used do not address a topic, the Australian standard on that topic (if any) must be complied with.

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