

Fundamental

Research Corp.

Investment Analysis for Intelligent Investors

Siddharth Rajeev, B.Tech, MBA
Analyst

Vincent Weber, B.Sc
Research Associate-Mining

Yan Lan, BBA
Research Associate

May 20, 2010

Rio Alto Mining Ltd. (TSXV: RIO, BVL: RIO) – US\$24.25 Million Accessed to Develop the La Arena Gold Oxide Project

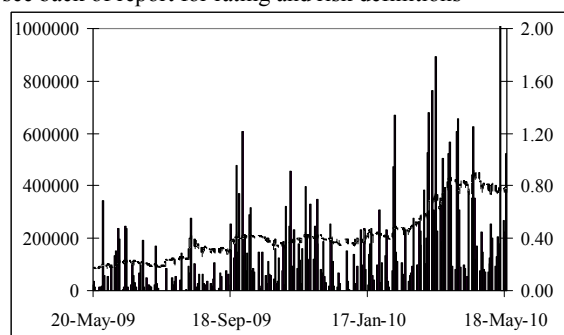
Sector/Industry: Junior Exploration/Mining

www.rioaltomining.com

Market Data (as of May 20, 2010)

| | |
|---------------|-------------------|
| Current Price | C\$0.72 |
| Fair Value | C\$1.69 |
| Rating* | BUY |
| Risk* | 5 (Highly Spec) |
| 52 Week Range | C\$0.17 - C\$0.92 |
| Shares O/S | 103.12 mm |
| Market Cap | C\$74.25 mm |
| Current Yield | N/A |
| P/E (forward) | N/A |
| P/B | 2.94 |
| YoY Return | 323.5% |
| YoY TSXV | 38.0% |

*see back of report for rating and risk definitions



Investment Highlights

- The company has entered into terms for a gold prepayment agreement in the amount of US\$24.25 million. The US\$24.25 million will be repaid by the delivery of 36,800 ounces of gold over a 40 month period from first gold production.
- The deal allows company to minimize dilution from project related equity financing and avoid interest payments associated with traditional bank debt financing.
- The company anticipates the first ore to be placed on the leach pad in December 2010, with **gold recovery starting in January of 2011**. Production of 50,000 ounces of gold is projected for year one.
- On May 20, 2010, the company announced it has closed the first tranche of a private placement by issuing 10.10 million shares (at \$0.75 per share) for gross proceeds of \$7.51 million.
- We have maintained our BUY rating and fair value.

Key Financial Data (FYE - May 31)

| (C\$) | 2009 | 2010 (9 mo) |
|-----------------|-------------|-------------|
| Cash | 5,702,661 | 4,989,820 |
| Working Capital | 5,344,759 | 4,577,500 |
| Mineral Assets | 8,145,252 | 20,902,359 |
| Total Assets | 15,051,240 | 27,315,717 |
| Net Income | (1,450,870) | (2,915,629) |
| EPS | (0.04) | (0.04) |

Note: An FRC analyst has visited RIO's property in the past 12 months; see the back of this report for additional disclosures

Rio Alto Mining Limited is focusing on acquisition and development of its flagship property, La Arena in Northern Peru. The La Arena deposit at the project has indicated resources of 58 Mt containing 0.91 Moz Au in an oxide gold cap. Underlying copper/gold sulphide resources are: 220 Mt indicated containing 1.9 Moz Au and 1.74 billion lbs Cu; 170 Mt inferred containing 1.2 Moz Au and 1.19 billion lbs Cu.

La Arena

The company entered into terms for a gold prepayment agreement in the amount of US\$24.25 million. The funding was acquired through a New York-based, private institutional investor and will be used specifically to develop the La Arena gold oxide project. The US\$24.25 million is to be repaid by delivery of 36,800 ounces of gold over a forty month period from first gold production.

Fundamental Research Corp. Perspective on the Deal

As with most financing deals, there are both pros and cons. Here are some of the positives and negatives of the deal and how we feel they will affect the project and the company:

- The deal allows the company to minimize dilution from equity financing as well as avoid interest payments associated with traditional bank debt financing.
- Gold delivery will be structured as follows: 575 oz per month for 16 months starting month nine after the receipt of capital; and, 1,150 oz per month for the subsequent 24 months. With production estimates of 50,000 oz in year one and 100,000 oz per year for the remainder of the mine life, the monthly payments will average less than 14% of total production per month.
- **Based on our long-term gold price (2012+) forecast of US\$750/oz, we estimate the present value of future cash flows of the proposed gold payments is US\$20.20 million - indicating that the purchase price of US\$24.25 million is favorable for RIO.**
- Most importantly, this deal significantly boosts the company's ability to advance the La Arena gold oxide project to production with minimal need for additional funds.

We should also note how this deal may affect the outstanding ownership payments to IAMGOLD (NYSE: IAG). With the expenditure of US\$30 million on the project – of which US\$4 million has been spent so far – the company will acquire 38.7% of La Arena S.A. (and thus also of the project – see our initiating report for details). The remaining 61.3% may be acquired through a cash payment of US\$47.55 million. This payment can, but is not required to, be made from production cash-flow (of which the company retains 100% during the earn-in process) and is due by June 15, 2011. However, the payment can be extended a total of 18 months with the additional payment of up to \$7.50 million. With ore leaching to begin December of 2010 (first gold recovery expected in January 2011) and the prepayment deal only representing a small portion of production cash flow, we anticipate the deal will not impede the company's ability to acquire the remaining 100% of the project. In fact, **we consider the deal to benefit the company as it expedites the move to production.**

Development Timeline: On April 8, 2010, the company received notice regarding the early completion of metallurgical tests pertaining to a 100 tonne sample of representative material. The details of the leach tests have not been released but the early completion would indicate favourable characteristics. The results are to be independently verified by Coffey Mining Pty. Ltd. who will incorporate the results into an updated NI 43-101 technical report that will also include an updated reserve estimation.

The company is still aiming to initiate production in Q4 of 2010 with the first ore being placed on the leach pad in December. With the acquisition of funding, only environmental approval and construction permits remain as hurdles to production. The company anticipates it will receive environmental approval from the Peruvian Ministry of Energy and Mines by June 2010, and construction permits within the following two months. The company also has to complete minor negotiations regarding local surface rights.

Acquisition of Claims

On March 3, 2010, the company announced that Rio Alto S.A.C., the company's wholly owned Peruvian subsidiary had, through staking, acquired an additional 4,300 hectares in five mining concessions. Three of the concessions are contiguous to, and on the same geological trend as the La Arena project while two are adjacent to Barrick Gold Corporation's (TSX: ABX) Lagunas Norte mining concessions. An additional 1,500 hectares of staked mining concessions were also applied for at the time. Six hundred hectares have been approved; the remaining 900 hectares are expected to be approved in June. All claims were acquired for their geological prospectivity. We remind the reader to distinguish between Rio Alto S.A.C., which is a wholly owned subsidiary of RIO, and La Arena S.A., the holding company of the La Arena project.

Management

On March 15, 2010, the company announced the appointment of Drago Kistic Wagner to the Board of Directors. Mr. Kistic specializes in investment banking, finance and macroeconomics and brings experience working in Peru.

Financials

The company reported a net loss of \$2.92 million in the first nine months in FY2010 (EPS: -\$0.04). We estimate the company had a burn rate (spending on operating and investing activities) of \$0.89 million per month during the first nine months of FY2010, compared to \$0.20 million per month during FY2009 (12 months period).

At the end of February 2010, the company had \$4.99 million in cash. Working capital was \$4.58 million. The table below summarizes the company's cash and liquidity position.

| (in C\$) | 2009 | 2010 (9 mo) |
|---------------------------------------|-----------|-------------|
| Working Capital | 5,344,759 | 4,577,500 |
| Current Ratio | 11.12 | 8.39 |
| LT Debt / Assets | - | - |
| Cash from Financing Activities | - | 5,714,593 |
| Monthly Burn Rate (incl. exploration) | (200,564) | (886,096) |

Stock options and warrants: As of February 2010, the company had 5.47 million stock options (weighted average exercise price: \$0.30), and 15.40 million warrants (weighted average exercise price: \$0.76) outstanding. Based on this information, we estimate about 5.42 million options and 8.98 million warrants are currently 'in-the-money'. **The company can raise up to \$4.95 million if all the 'in-the-money' options and warrants are exercised.**

Subsequent Financings: On May 20, 2010, the company announced it closed the first tranche of a private placement by issuing 10.10 million shares (at \$0.75 per share) for gross proceeds of \$7.51 million. The company expects to pursue additional tranches of the private

placement going forward.

Valuation and Rating

We revised our valuation models to reflect the recently announced gold prepayment agreement and private placement. A summary of our revised valuation is shown below.

| Valuation Summary | |
|--------------------------|---------------|
| DCF | \$1.44 |
| Comparables | \$0.45 |
| Real Options | \$2.90 |
| Average | \$1.60 |

Our revised valuation is \$1.60 per share (from \$1.69 per share). The valuation dropped primarily due to share dilution. The sensitivity of our valuation to changes in long-term gold and copper price assumptions is shown below:

| | | LT Copper Price (US\$/lb) - 2012+ | | | | |
|--|----------------|--|---------------|---------------|---------------|---------------|
| | | \$1.00 | \$1.50 | \$2.03 | \$2.50 | \$3.00 |
| LT Gold Price (US\$/oz) - 2012+ | \$450 | (\$0.40) | \$0.23 | \$0.99 | \$1.69 | \$2.43 |
| | \$600 | (\$0.17) | \$0.52 | \$1.30 | \$1.99 | \$2.74 |
| | \$750 | \$0.10 | \$0.82 | \$1.60 | \$2.30 | \$3.04 |
| | \$900 | \$0.39 | \$1.12 | \$1.90 | \$2.60 | \$3.35 |
| | \$1,050 | \$0.68 | \$1.42 | \$2.20 | \$2.91 | \$3.65 |

*Gold price forecast for 2011 is \$975/oz

We reiterate our BUY rating, and maintain our fair value estimate at \$1.69 per share.

Risks

The following risks, though not exhaustive, may cause our estimates to differ from actual results:

- The value of the company is dependent on commodity prices.
- Access to capital and share dilution.
- The company currently has no operating mines.
- The company has substantial financial obligations up to June 15, 2011, in order to fully acquire La Arena S.A.
- The company has yet to receive all permitting required to construct a mine at La Arena. Delays or failure to obtain such permits may have a material adverse affect on the value of the company and the financial obligations relating to the acquisition of La Arena S.A.

We rate the company's shares a RISK of 5 (Highly Speculative).

Fundamental Research Corp. Equity Rating Scale:**Buy** – Annual expected rate of return exceeds 12% or the expected return is commensurate with risk**Hold** – Annual expected rate of return is between 5% and 12%**Sell** – Annual expected rate of return is below 5% or the expected return is not commensurate with risk**Suspended or Rating N/A**— Coverage and ratings suspended until more information can be obtained from the company regarding recent events.**Fundamental Research Corp. Risk Rating Scale:****1 (Low Risk)** - The company operates in an industry where it has a strong position (for example a monopoly, high market share etc.) or operates in a regulated industry. The future outlook is stable or positive for the industry. The company generates positive free cash flow and has a history of profitability. The capital structure is conservative with little or no debt.**2 (Below Average Risk)** - The company operates in an industry where the fundamentals and outlook are positive. The industry and company are relatively less sensitive to systematic risk than companies with a Risk Rating of 3. The company has a history of profitability and has demonstrated its ability to generate positive free cash flows (though current free cash flow may be negative due to capital investment). The company's capital structure is conservative with little to modest use of debt.**3 (Average Risk)** - The company operates in an industry that has average sensitivity to systematic risk. The industry may be cyclical. Profits and cash flow are sensitive to economic factors although the company has demonstrated its ability to generate positive earnings and cash flow. Debt use is in line with industry averages, and coverage ratios are sufficient.**4 (Speculative)** - The company has little or no history of generating earnings or cash flow. Debt use is higher. These companies may be in start-up mode or in a turnaround situation. These companies should be considered speculative.**5 (Highly Speculative)** - The company has no history of generating earnings or cash flow. They may operate in a new industry with new, and unproven products. Products may be at the development stage, testing, or seeking regulatory approval. These companies may run into liquidity issues, and may rely on external funding. These stocks are considered highly speculative.**Disclaimers and Disclosure**

The opinions expressed in this report are the true opinions of the analyst about this company and industry. Any "forward looking statements" are our best estimates and opinions based upon information that is publicly available and that we believe to be correct, but we have not independently verified with respect to truth or correctness. There is no guarantee that our forecasts will materialize. Actual results will likely vary. The analyst and Fundamental Research Corp. "FRC" does not own any shares of the subject company, does not make a market or offer shares for sale of the subject company, and does not have any investment banking business with the subject company. Fees of less than \$30,000 have been paid by RIO to FRC. The purpose of the fee is to subsidize the high costs of research and monitoring. FRC takes steps to ensure independence including setting fees in advance and utilizing analysts who must abide by CFA Institute Code of Ethics and Standards of Professional Conduct. Additionally, analysts may not trade in any security under coverage. Our full editorial control of all research, timing of release of the reports, and release of liability for negative reports are protected contractually. To further ensure independence, RIO has agreed to a minimum coverage term including an initial report and three updates. Coverage can not be unilaterally terminated. Distribution procedure: our reports are distributed first to our web-based subscribers on the date shown on this report then made available to delayed access users through various other channels for a limited time. The performance of FRC's research is ranked by Investars. Full rankings and are available at www.investars.com.

The distribution of FRC's ratings are as follows: BUY (72%), HOLD (8%), SELL (4%), SUSPEND (16%).

To subscribe for real-time access to research, visit <http://www.researchfrc.com/subscription.htm> for subscription options.

This report contains "forward looking" statements. Forward-looking statements regarding the Company and/or stock's performance inherently involve risks and uncertainties that could cause actual results to differ from such forward-looking statements. Factors that would cause or contribute to such differences include, but are not limited to, continued acceptance of the Company's products/services in the marketplace; acceptance in the marketplace of the Company's new product lines/services; competitive factors; new product/service introductions by others; technological changes; dependence on suppliers; systematic market risks and other risks discussed in the Company's periodic report filings, including interim reports, annual reports, and annual information forms filed with the various securities regulators. By making these forward looking statements, Fundamental Research Corp. and the analyst/author of this report undertakes no obligation to update these statements for revisions or changes after the date of this report. A report initiating coverage will most often be updated quarterly while a report issuing a rating may have no further or less frequent updates because the subject company is likely to be in earlier stages where nothing material may occur quarter to quarter.

Fundamental Research Corp DOES NOT MAKE ANY WARRANTIES, EXPRESSED OR IMPLIED, AS TO RESULTS TO BE OBTAINED FROM USING THIS INFORMATION AND MAKES NO EXPRESS OR IMPLIED WARRANTIES OR FITNESS FOR A PARTICULAR USE. ANYONE USING THIS REPORT ASSUMES FULL RESPONSIBILITY FOR WHATEVER RESULTS THEY OBTAIN FROM WHATEVER USE THE INFORMATION WAS PUT TO. ALWAYS TALK TO YOUR FINANCIAL ADVISOR BEFORE YOU INVEST. WHETHER A STOCK SHOULD BE INCLUDED IN A PORTFOLIO DEPENDS ON ONE'S RISK TOLERANCE, OBJECTIVES, SITUATION, RETURN ON OTHER ASSETS, ETC. ONLY YOUR INVESTMENT ADVISOR WHO KNOWS YOUR UNIQUE CIRCUMSTANCES CAN MAKE A PROPER RECOMMENDATION AS TO THE MERIT OF ANY PARTICULAR SECURITY FOR INCLUSION IN YOUR PORTFOLIO. This REPORT is solely for informative purposes and is not a solicitation or an offer to buy or sell any security. It is not intended as being a complete description of the company, industry, securities or developments referred to in the material. Any forecasts contained in this report were independently prepared unless otherwise stated, and HAVE NOT BEEN endorsed by the Management of the company which is the subject of this report. Additional information is available upon request. THIS REPORT IS COPYRIGHT. YOU MAY NOT REDISTRIBUTE THIS REPORT WITHOUT OUR PERMISSION. Please give proper credit, including citing Fundamental Research Corp and/or the analyst, when quoting information from this report.

The information contained in this report is intended to be viewed only in jurisdictions where it may be legally viewed and is not intended for use by any person or entity in any jurisdiction where such use would be contrary to local regulations or which would require any registration requirement within such jurisdiction.