



May 23, 2007

First Metals Inc.
(TSX-FMA \$1.46)

Recommendation: SPECULATIVE BUY
New 12-Month Target: \$1.90
Previous 12-Month Target: \$1.75
Risk Rating: ABOVE AVERAGE

EMERGING COPPER-ZINC PRODUCER IN NORTHWESTERN QUEBEC

THE EVENT:

- On May 7, 2007, First Metals successfully closed a \$20 million debt financing consisting of notes and warrants. A total of 20,000 notes were issued, each having a face value of \$1,000 (and bearing interest at 14% annually, payable on a quarterly basis) plus 100 warrants exercisable at \$1.35 per share. Both the notes and warrants expire in May 2012. Jennings Capital Inc. acted as agent in the financing.

THE IMPACT:

- The completion of the note offering all but eliminates financing risk from the story and allows management to focus on exploration and development...
- ...but the delay has caused us to push our anticipated production startup at **Fabie Bay** out by five months, to August, subject to completion of a custom milling agreement and receipt of a mining permit.
- A 50,000-tonne bulk sample from the bottom of the pit is ready for extraction, and the pace of dewatering the underground workings should enable a smooth transition to underground mining operations once a mining permit is in hand.
- Drilling at **Magusi River** is underway and could be followed by underground development in Q4/07.
- Potential upside to current metal price environment still a significant upside factor in the story. Using recent copper and zinc prices quadruples our NAV and doubles our target.

VALUATION AND RECOMMENDATION

We are raising our target to **\$1.90/share** from **\$1.75/share**, with the biggest driver being an upward revision in our copper and zinc price assumptions. We continue to recommend purchase of First Metals Inc. as a **SPECULATIVE BUY**.

Sector: MINING, GOLD & PRECIOUS MINERALS

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Company Statistics

Market Cap (\$mm)	\$45MM
Basic Shares O/S	31MM
Fully diluted Shares O/S	44MM
52-Week Range	\$0.61 - \$1.76
Dividend	None
Yield	-
Major Shareholders	None
RAB Special Situations (April 2007)	~11.0%
Jaycap Equity Inc. (September 2006)	~10.4%
Cash (03/31/07)	(\$0.5MM)
Working Capital (03/31/07)	(\$1.3MM)
LT Debt (03/31/07)	-
Book Value \$/Share	\$0.29

Financial Summary

FYE: December	2006A	2007E	2008E	2009E
EPS	-\$0.06	\$0.19	\$0.27	\$0.04
CFPS	-\$0.03	\$0.30	\$0.50	\$0.18
P/E	-	7.9x	5.4x	39.9x
P/CF	-	4.8x	2.9x	8.1x

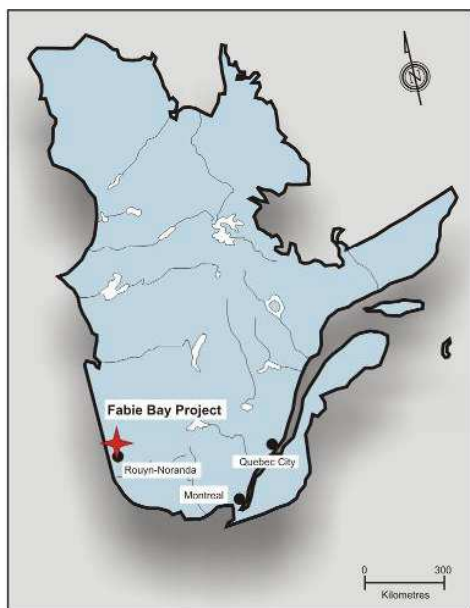


First Metals Inc. is a newly formed public company, created to capitalize on favourable upward trends in metals prices through its Fabie Bay and nearby Magusi River copper-zinc deposits. The properties are located in the historic Noranda Mining Camp of northwestern Quebec.

FABIE BAY AND MAGUSI RIVER PROJECTS

HISTORY

The Fabie Bay and adjoining Magusi River base metal properties consist of 13 unpatented, contiguous mining claims covering approximately 508 hectares located 35 kilometres northwest of Rouyn-Noranda, Quebec. Infrastructure is excellent, with access being gained from a network of gravel and forestry roads branching off provincial highways 117, 101 and 388. First Metals recently upgraded and widened the main access road and commissioned Quebec Hydro to construct a 31-kilometre power line to both properties.



Source: First Metals Inc.

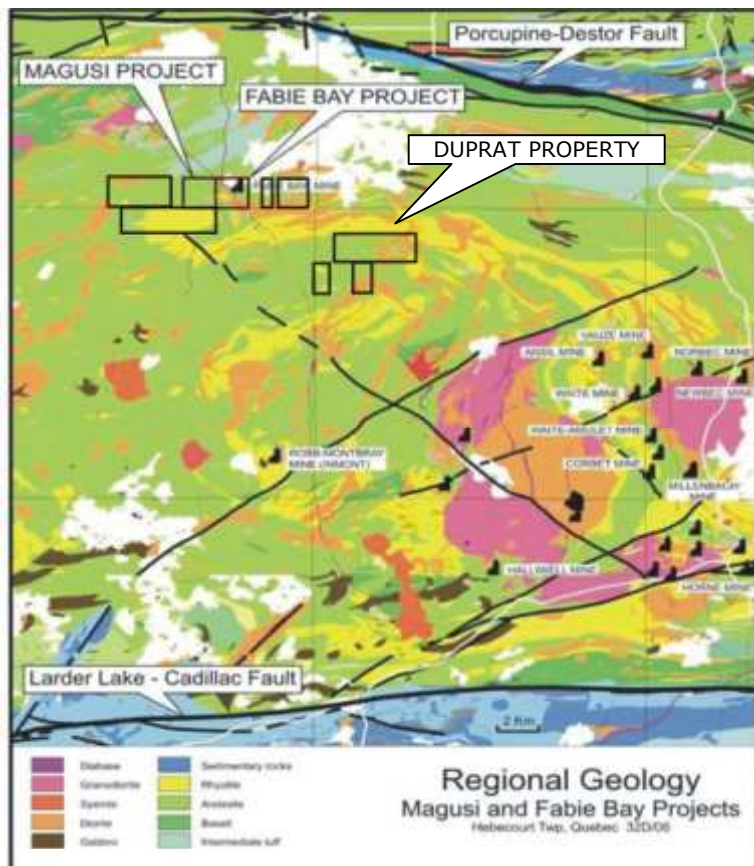
In April 2006, First Metal acquired 100% interests in the properties and an additional 2,366 hectares, in return for paying Globex Mining Enterprises Inc. \$1 million in cash (\$250,000 remains unpaid and is due in six months of achieving commercial production), a 10% equity interest once commercial production is achieved and royalties on future production. The royalties consist of a 2% interest on metal sales and a 10% net profits interest, net of recovering \$10 million of capital. Two private placements totaling \$3.1 million and an Initial Public Offering totalling \$10.2 million were subsequently completed.

In November, First Metals received a Certificate of Authorization (C of A) for Fabie Bay, essentially permitting site preparation and extraction of a 50,000 bulk sample. Since then, the Company has drilled off 80,000 tonnes of mineralized material at the bottom of the pit, signed a Letter of Intent for a custom milling agreement with Xstrata Copper Canada and submitted an application for a mine permit that would allow for the start of commercial mining operations. Both the custom milling agreement and mine permit are expected shortly. In addition, definition drilling has begun at the Magusi River deposit, and a C of A application is expected to be filed during the summer, possibly enabling the start of underground development later in the year.

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GEOLOGY

Fabie Bay and Magusi River are volcanogenic massive sulphide deposits (VMS) hosted by a folded sequence of Archean-aged volcanic flows and sills forming part of the Blake River Group. The deposits lie at what is generally considered the northern limits of the Noranda Complex, a caldera-like structure bounded to the north and south by the mineral-rich Porcupine-Destor and Larder-Cadillac structural breaks.



Source: Micon International Ltd.

RESERVES AND RESOURCES

First Metals has not outlined any reserves, but it did complete 43-101 compliant resource studies in June 2006. Combined, the Fabie Bay and Magusi River deposits were estimated with an **Inferred Resource** of 2.74 million tonnes containing 113.0 million lbs copper, 198.1 million lbs zinc, 80,675 oz gold and 2.2 million oz silver, enough to sustain production for 4.5 years at planned production rates. We break the resource estimates out in the next table.

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First Metals Inc.					
Summary of 43-101 Inferred Resource Estimates					
Deposit	Tonnes	Metal Grades			
		Cu	Zn	Au (g/t)	Ag (g/t)
Fabie Bay lens	672,800	2.77%	-	-	-
Magusi Zn-rich lens	1,230,000	0.40%	7.10%	1.89	29.00
Magusi Cu-rich lens	838,860	3.30%	0.30%	0.22	39.10
Combined	2,741,660	1.87%	3.28%	0.92	24.97

Source: Micon International Ltd.

Mineralization at both deposits remains open in several directions and thus, offers good potential for expansion with further drilling and development. We also note that a zinc-rich zone is curiously absent at the Fabie Bay project and suspect this could simply represent a lack of drilling beyond the copper zone or fault displacement.

MINING AND PROCESSING

First Metals proposes to mine the deposits by underground methods at a rate of 1,000-1,500 tonnes per day. Run-of-mine material would be crushed on site and trucked elsewhere for further processing. The current proposed custom milling agreement between First Metals and Xstrata Copper Canada excludes Magusi River thus, would have to be amended if the deposit's feasibility is confirmed. Alternatively, the Company would need to seek other arrangements.

With respect to metallurgy, results from the Fabie Bay zone suggest that upward of 93% recoveries are possible from Fabie Bay, in a concentrate averaging over 24% copper. Historic results provided in a Technical Report by Micon International also suggest favourable results can be expected from Magusi River, subject to further tests.

PRODUCTION AND OPERATING COSTS

Owing to the longer-than-expected completion time of the financing needed to advance Fabie Bay to production, we now expect mining operations to start in August, or five months later than previously anticipated. Against this, we have decided to accelerate the start of operations in the zinc-rich lens at Magusi River, but continue to assume that mining of the copper-rich lens follows the depletion of the Fabie Bay deposit, expected in Q3/09. The adjustments to the Magusi River profile simply reflect further discussions with management, the shallower setting of the zinc-rich lens and recognition of work completed to date, such as an access road and power line from Fabie Bay.

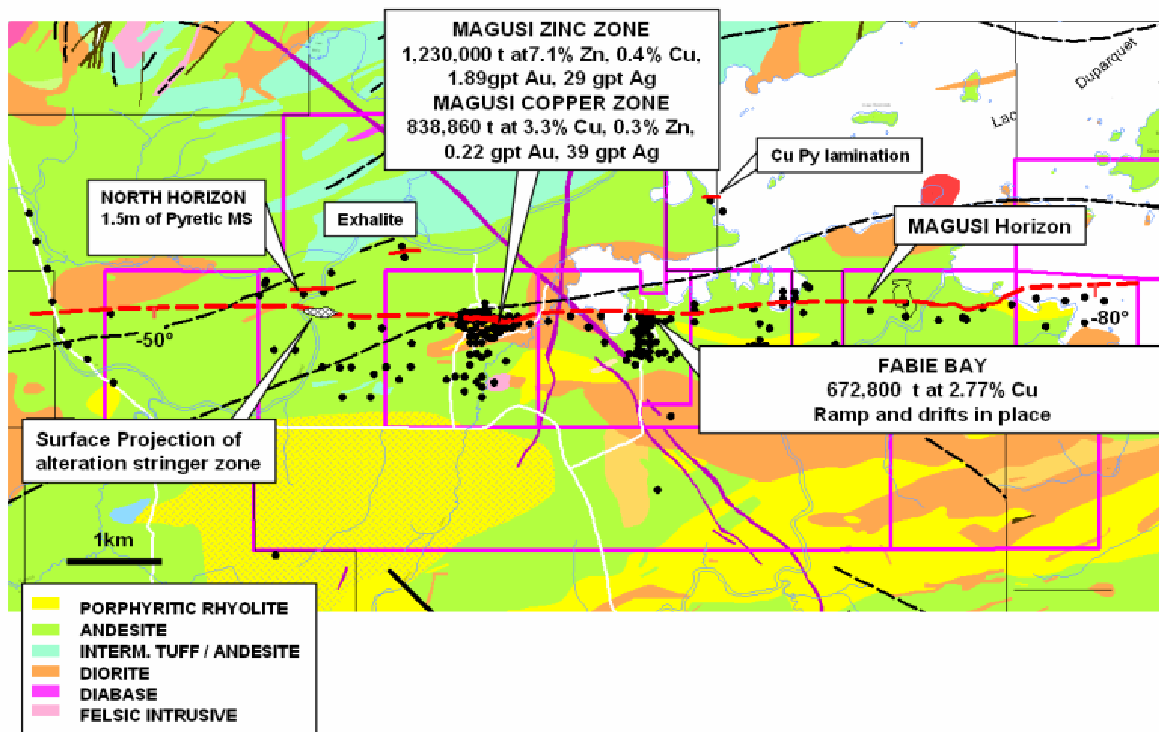
Beyond scheduling, we have adjusted our throughput and cost assumptions to reflect further discussions with management. Our revised estimates are summarized in the next table, but we once again caution investors that our modelling assumptions are necessarily crude in nature, not being based on third-party reserve or economic studies.

First Metals Inc.						
Summary of Production and Cost Projections						
	2007E	2008E	2009E	2010E	2011E	2012E
Annual production rate (tonnes)	176,640	504,000	504,000	504,000	504,000	411,937
Daily	1,140	1,381	1,381	1,381	1,381	1,129
% Fabie Bay deposit	100%	63%	29%	0%	0%	0%
% Magusi River Zn-rich lens	0%	38%	50%	50%	50%	54%
% Magusi River Cu-rich lens	0%	0%	21%	50%	50%	46%
<u>Payable metal</u>						
Copper (000 lb)	8,948	16,581	14,334	14,871	14,871	11,122
Zinc (000 lb)	0	19,010	25,582	25,914	25,914	22,905
Gold (oz)	0	6,346	8,507	8,583	8,583	7,595
<u>Cash costs</u>						
Per tonne milled	\$78.63	\$86.32	\$89.15	\$92.69	\$92.69	\$92.81

Source: Jennings Capital Inc.

EXPLORATION UPSIDE

In addition to Fabie Bay and Magusi River, First Metals has a 100% interest in 1,466 hectares of ground, mostly extending along strike of the deposits. Among the targets of immediate interest are eight geophysical anomalies, half of which are described as characterizing VMS-style mineralization and the other half as gold-style mineralization. Accordingly, we believe that there is good potential for discovering new mineralization in the immediate and surrounding vicinities with additional exploration work.



Source: First Metals Inc.

Beyond Fabie Bay and Magusi River, First Metals owns 921 hectares of claims collectively referred to as the Duprat project. Exploration there is much earlier staged than at the other properties, so we would characterize the project as a loner-term play. Various discoveries by Alexis Minerals Corp. also attest to the camp's exploration potential, particularly the March 2006 preliminary resource estimates for the West Ansil zone. The zone was estimated to host an **Indicated Resource** of 530,000 tonnes grading 3.4% copper, 1.4 g/t gold, 9.2 g/t silver and 0.4% zinc, and an **Inferred Resource** of 600,000 tonnes grading 3.3% copper, 0.3 g/t gold, 5.9 g/t silver and 0.2% zinc.

BALANCE SHEET AND CAPITAL REQUIREMENTS

On March 31, 2007, First Metals had a working capital deficit of \$1.3 million and no debt, but has since completed a \$20 million note offering to raise what should be adequate financing to advance Fabie Bay to production and cover working capital requirements until operating cash flow can be generated. A note has a face value of \$1,000, bears interest at 14% annually and matures in May 2012. As part of the financing, a total of 2 million warrants were issued to the note holders and are exercisable at \$1.35/share over the same period. A total of \$3 million was released to the Company upon the deal's closing and the remainder is being held in escrow, pending, among other things, finalization of the custom milling agreement and receipt of a mining permit. Jennings Capital Inc. acted as sole agent for the financing.

First Metals also had 3.5 million options outstanding, with a weighted average price of \$1.00 per share, plus approximately 7.6 million warrants outstanding, priced at \$0.30-\$1.25/share. The options and warrants expire over the next two years and would represent an equity capital inflow of \$9.8 million if exercised.

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To date, First Metals has spent over \$12.5 million on Fabie Bay and is expected to spend a further \$7.5 million before commercial mining operations begin. The bulk of the additional expenditures, being \$4.5 million, are allocated for the refurbishment of the Horne mill. Total capital expenditures for Magusi River are estimated at \$12 million, mostly in 2008.

VALUATION

We have modelled First Metals' projected cash flows at the metal prices summarized in the table below and conservatively determined the 2007 net asset value (NAV) to be \$0.72/fully diluted and fully financed share, discounted at 10%. **Applying a hybrid multiple of 1.25x NAV to reflect the precious metals component, near-term production potential and exploration upside, generates a 12-month target of \$0.90/share.** Our valuation incorporates working capital, options and warrants, plus the short-term debt financing assumptions discussed above.

We have forecast average 2007 and 2008 EPS of \$0.23/share. **Applying a multiple of 10.0x to our average EPS estimate generates a 12-month target of \$2.28.**

We have forecast average 2007 and 2008 CFPS of \$0.40/share. **Applying a multiple of 6.0x to our average CFPS estimate generates a 12-month target of \$2.39.**

Given equal weight to NAV, EPS and CFPS, we generate a blended 12-month target of \$1.90/fully diluted share for First Metals Inc. We also note that First Metals remains highly leveraged to metal prices, with the use of current prices causing our NAV to more than triple and our target to nearly double.

Valuation Method	Parameter	Multiple	Valuation
<u>@ US\$1.50/lb Cu and US\$0.75/lb Zn LT</u>	<i>(\$/shr)</i>		<i>(\$/shr)</i>
NAV @ 10% discount	\$0.72	1.25x	\$0.90
Average of 07E and 08E EPS	\$0.23	10.00x	\$2.28
Average of 07E and 08E CFPS	\$0.40	6.0x	\$2.39
	Average		\$1.86
<u>@ US\$3.50/lb Cu and US\$1.70/lb Zn</u>	NAV	Multiple	Impact on Target
NAV @ 10% discount	\$2.91	1.25x	\$3.63
Average of 07E and 08E EPS	\$0.42	10.00x	\$4.20
Average of 07E and 08E CFPS	\$0.59	6.00x	\$3.54
	Average		\$3.79

Source: Jennings Capital Inc.

RECOMMENDATION

Our valuation of First Metals remains entirely dependent on the Company's ongoing drilling and development success. Still, the potential to participate in the current metal price environment and to outline additional tonnage remain very real aspects of the story. **Accordingly, we continue to recommend purchase of First Metals Inc. as a SPECULATIVE BUY.**

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First Metals Inc.							
Summary of Financial Estimates (C\$000)							
	2006A	2007E	2008E	2009E	2010E	2011E	2012E
Copper (US\$/lb)	\$3.05	\$3.19	\$2.70	\$1.90	\$1.50	\$1.50	\$1.50
Zinc (US\$/lb)	\$1.49	\$1.52	\$1.18	\$0.75	\$0.75	\$0.75	\$0.75
Gold (US\$/oz)	\$604.28	\$667.54	\$700.00	\$700.00	\$700.00	\$700.00	\$700.00
Silver (US\$/oz)	\$11.51	\$13.08	\$13.50	\$14.00	\$14.00	\$14.00	\$14.00
Revenue							
Payable copper	\$0	\$33,166	\$52,488	\$30,792	\$25,348	\$25,348	\$18,957
Payable zinc	0	0	24,400	21,803	22,086	22,086	19,521
Payable gold	0	0	5,106	6,767	6,827	6,827	6,042
Payable silver	0	0	732	2,054	3,546	3,546	2,791
Gross Metal Sales	\$0	\$33,166	\$82,726	\$61,416	\$57,807	\$57,807	\$47,311
TC/RCS	\$0	3,176	11,376	11,128	11,436	11,436	9,397
Gross metal royalty (2%)	0	663	1,655	1,228	1,156	1,156	946
Net Metal Sales	\$0	\$29,326	\$69,695	\$49,059	\$45,215	\$45,215	\$36,968
Other income	96	14	0	0	0	0	0
Operating Expenses							
Direct mining costs	\$0	\$10,714	\$32,130	\$33,805	\$35,280	\$35,280	\$28,836
Corporate G&A	339	1,800	1,800	1,800	1,800	1,800	1,800
Stock-based compensation	805	63	0	0	0	0	0
Other	793	75	0	0	0	0	0
	1,937	12,652	33,930	35,605	37,080	37,080	30,636
EBITDA	(\$1,841)	\$16,689	\$35,765	\$13,455	\$8,135	\$8,135	\$6,332
Net profits interest (10%)	\$0	771	3,577	1,345	814	814	633
Interest	6	1,832	2,800	2,800	2,800	2,800	984
Depreciation and amortization	0	5,357	10,601	6,783	3,065	3,210	2,874
EBT	(\$1,847)	\$8,728	\$18,787	\$2,526	\$1,457	\$1,312	\$1,841
Income tax expense (recovery)	\$0	\$0	\$6,106	\$808	\$452	\$407	\$571
Net Earnings	(\$1,847)	\$8,728	\$12,682	\$1,717	\$1,005	\$905	\$1,270
EPS (basic)	(\$0.06)	\$0.28	\$0.41	\$0.06	\$0.03	\$0.03	\$0.04
EPS (fully diluted)	(\$0.06)	\$0.19	\$0.27	\$0.04	\$0.02	\$0.02	\$0.03
Cash Flow From Operations	(\$1,043)	\$14,149	\$23,283	\$8,501	\$4,070	\$4,115	\$4,145
CFPS (basic)	(\$0.03)	\$0.46	\$0.75	\$0.28	\$0.13	\$0.13	\$0.13
CFPS (fully diluted)	(\$0.03)	\$0.30	\$0.50	\$0.18	\$0.09	\$0.09	\$0.09
Shares outstanding, basic	30,862	30,862	30,862	30,862	30,862	30,862	30,862
Shares outstanding, fully diluted	46,966	46,966	46,966	46,966	46,966	46,966	46,966

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Company	Ticker
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Note: *We initiated coverage on **First Metals Inc.** on December 18, 2006 with a **SPECULATIVE BUY** recommendation and a C\$1.75 target price. Share price at that time was C\$1.00.*

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Strong Buy: The stock is expected to provide a total return in excess of 50% over the current trading price over the next 12 months.

Buy: The stock is expected to provide a total return of 10% to 50% over the current trading price over the next 12 months.

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SPECULATIVE BUY	39%
HOLD	3%
RESTRICTED	6%
SELL	11%

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