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26 October 2004

The Manager  
Australian Stock Exchange Limited  
Level 4  
20 Bridge St  
Sydney, NSW.

Dear Sir/Madam,

#### **MEDUSA EXECUTES HOA TO ACQUIRE PHILIPPINES JV PARTNER**

The Company advises that it has signed a Heads of Agreement with the principal shareholders of Philsaga Mining Corporation (Philsaga) to acquire their shares and thereby ownership of all of Philsaga's assets in central eastern Mindanao, Republic of the Philippines. These assets include:

- The Co-O CIP plant with a rated capacity of 550 tpd and currently operating at approximately 80 – 100 tpd treating ore averaging 20-25g/t Au. Throughput for the CIP plant is anticipated to rise within 6 months to 150 tpd at similar headgrades with the commissioning of an additional haulage level at the Co-O Mine;
  - Gold production at cash costs of less than US\$200/oz;
  - The Co-O underground mine with vein strike lengths of over 600m and situated approximately 12 km southeast of the mill;
  - Infrastructure including administration buildings, work shops, standby power house, assay laboratory, warehouses and inventories, messing and accommodation facilities, and associated equipment;
  - A work force skilled in all facets of the operation allowing Medusa a seamless transition to a producer with an increasing production profile;
  - A large tenement holding comprising approximately 537 km<sup>2</sup> (53,700 hectares) over an approximate strike length of 70 km of the unexplored but highly mineralised and prospective Diwata Range that has had no systematic modern exploration;
  - The Medusa- Philsaga Saugon Joint Venture to the south of Co-O where Medusa has earned its 50% interest;
  - The Tambis joint venture to the north of Co-O where the JV partner is about to commence spending US\$1.5M to earn a 50% interest;
  - One other joint venture on similar terms under finalisation.
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The purchase price will be negotiated in good faith after completion of an independent valuation and normal commercial due diligence. The Company has appointed various experts both in the Philippines and Australia to undertake JORC compliant Mineral Resource/Ore Reserve calculations, due diligence on Philsaga's accounting aspects, tenements and associated agreements and all legal aspects.

Upon the purchase price being successfully negotiated, full form transaction documents will be drawn to record the acquisition. The acquisition will be subject to all necessary regulatory and statutory approvals.

The Company has mandated Corpac Partners Pty Ltd of Sydney to act as the Company's corporate advisors for the acquisition. Corpac has already satisfied itself with respect to the technical merits of the project.

## **1. BACKGROUND INFORMATION**

Philsaga's assets are located in central eastern Mindanao in the Republic of the Philippines (Fig. 1) and are accessed by the national highway via an approximate 2.5 hour drive north of Davao City. Project areas and the Co-O mill site and mine are located on the eastern side of the highway and are accessible through a network of all weather gravel roads.

The project now comprises approximately 537 km<sup>2</sup> of tenements which cover approximately 70 km of strike length (Fig. 2).

The Co-O Mine was first put into production by Musselbrook Energy and Mines (MEM) in 1989, but due to serious grade dilution problems caused by the inappropriate use of mechanised mining methods for narrow veins, the project closed in 1991 after producing approximately 60, 000 ounces of gold. MEM spent approximately US\$22M to put the project into production, with the majority of the facilities and equipment in good condition when purchased by Philsaga in August 2000 after 9 years of care and maintenance.

MEM developed the mine via an adit which was driven 400m to reach the vein system at the 3150m level (150m above sea level) and extended 600m along the system. Drives were then driven along several sub-parallel veins for the development of stopes above the level. Stoping was planned to recover ore with grades of 10 -14g/t Au, but past records indicate the mill feed grades ranged between 5-8g/t Au.

Philsaga commenced operating the Co-O Project in August 2000 with a different mining approach whereby labour intensive mining methods suited to narrow vein mining have been instituted resulting in minimum dilution and production at low cash costs. Philsaga has very successfully undertaken the ongoing process of developing the project from an essentially care and maintenance basis at the time of acquisition to its current status of being a fully functional and supported gold producer with rising production.

Since 2000 Philsaga has produced approximately 80,000 ounces of gold at the rate of 20-25,000 ounces per year in a co-operative manner with all local stake holders.

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## **2. THE PHILSAGA ASSETS**

### **2.1 The Co-O Gold Mine**

The Co-O underground mine (Fig 3.) is developed on a series of low sulphide, epithermal quartz veins which strike west over a length of at least 600 metres and have been explored to a depth of more than 200 metres from surface so far. The veins are open to the west and at depth, and until recently had been truncated in the east by the northerly trending Oriental Fault. Recent diamond drilling has intersected vein extensions on the east side of the fault which are being traced by further drilling to the east.

Below the 3150m level where Philsaga commenced operations and are now at the 3050m level, some of these veins coalesce into one vein which averages 2.5-3m in width and contains an average grade of +20g/t Au.

New veins sub-parallel to and immediately to the north of the known Co-O system have been recently discovered at surface and are currently being tested by drilling.

At the surface, being approximately the 3300m level, the veins are generally very narrow veinlets within an extensive clay-pyrite alteration envelope with minor accessory barite with low 3-5g/t Au gold values. The gold values start to increase significantly from about 80m below the surface.

Figure 3 also shows the underground development work already completed by Philsaga as well as the planned mine development. Philsaga has undertaken a considerable amount of rehabilitation work on the old drives for access and ventilation and have produced most of their ore from below the 3150m level. The new Tinago shaft near the western end of the vein system will break through into the 3150m level in early November 2004. Additional driving to link the shaft with the 3150 level workings is in progress as well as work in progress to equip the shaft to produce 150-200tpd of ore and waste.

At the 3050m level, which is 100m below adit level, Philsaga is developing a main haulage level and to date has driven west on the main vein over a strike length of 200m with advancing continuing. Planning has also commenced for an internal inclined shaft at the eastern end of the vein system and to develop another main haulage level at the 2950m level which is 200m below adit level.

Currently the mine is producing ore of approximately 20-25 g/t Au at approximately 80-100 tonnes per day from development and stoping. With the completion of the Tinago shaft, production will start to rise in the second quarter of 2005 to a total of approximately 150 tpd or 4500 tpm at anticipated head grades of +20g/t Au.

Mining and exploration drilling services are carried out by contracting companies which will continue to provide services to Philsaga. Philsaga owns a fleet of dump trucks for ore transport and road maintenance, as well as graders, loaders and other earthmoving equipment.

### **2.2 The Tenement Holdings and Joint Ventures**

Since taking ownership of the Co-O mine and plant, Philsaga commenced consolidating the region north and south of the plant by acquiring a number of tenements through direct ownership or effective ownership via agreements.

As shown on Figure 3, this tenement holding is strategically located north and south of the Co-O milling facility and covers part of the highly prospective Diwata Range.

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Philsaga has also adopted a policy of joint ventures for some of its exploration areas and has entered into a joint venture with Continental Goldfields Ltd to explore the Tambis project to the north of the Co-O plant, whereby Continental will earn a 50% interest by spending the first US\$1.5M. This work will commence shortly. The Tambis project has a long history of artisan mining on high grade veins but workings have all stopped near the water table where individual miners have not had the capital to undertake dewatering. The potential to find additional mineralisation is regarded as high due to the presence of extensive alteration zones and the occurrence of gold in many drainages in other areas away from the main workings.

Philsaga is negotiating a second joint venture on similar terms and conditions as the Tambis joint venture, and has also received expressions of interest from other companies. Each joint venture is expected to bring with it the initial expenditure of US\$1.5M before Philsaga is required to contribute.

### **2.3 Infrastructure and facilities**

The Co-O Mine is independent of the mill site in that it is separated by a 12 kilometre distance and has its own diesel generators, workshops and workforce, the majority of which live at the mine. Ore is transported by dump truck to the mill.

The Co-O CIP plant is BHP designed and built with a current capacity of 550tpd. Minor alterations are required to increase the throughput to 700tpd and further modifications could maximise the crushing and grinding capacity at 1000-1100tpd.

A second small scale CIP installed post MEM is used to treat tailings acquired from small scale artisan mining operations in the district.

Power to the CIP plant is supplied from the local grid with the high tension power line located approximately 150m from the plant. Back up diesel generators installed by MEM prior to the construction of the transmission line are operational and available.

The other facilities include administration offices and assay laboratory, a warehouse, mechanical and machine shops, messing and accommodation facilities and geological offices and core storage facilities.

## **3. ACQUISITION DETAILS**

Under the terms of the HOA between Philsaga and Medusa, the parties have agreed to use an independent valuation as the basis for agreeing on the final consideration. In preparation for completing the acquisition Medusa has appointed the following experts:

- **Resource and reserve modelling and estimation:** Medusa has assisted Philsaga to complete data entry for all the Co-O Mine data which is currently being modelled and estimated by Cube Consulting Pty Ltd of Perth;
  - **Tenement status, acquisitions, royalty and joint venture agreements:** Medusa has appointed JD Muyco & Associates from Manila to undertake the compilation of the dossier for comment and legal sign off. This work is well advanced.
  - **Project valuation:** Golder Associates Pty Ltd from Perth have been appointed to prepare the Independent Technical Report and to prepare an Independent Valuation for the transaction. This will commence on 1 November and is expected to be received in late November.
  - **Financial and fixed asset due diligence:** Bentleys MRI Perth Pty Ltd has been commissioned to undertake this work in conjunction with their affiliates in
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the Philippines. This work commences on 8 November and is expected to be complete at the end of November.

- **Legal advice Philippines:** Carag, Caballes, Jamora and Somara of Manila have been appointed to draft formal documentation and to provide advice regarding Philippine legal aspects of the transaction;
- **Legal advice Australia:** The Company's legal advisors, Fairweather & Lemonis will provide legal advice on the transaction in Australia.
- **Corporate advisors:** Corpac Partners Pty Ltd from Sydney has been appointed as the Company's corporate advisors for the transaction and will undertake the raising of debt and equity finance to complete the transaction. It is anticipated that settlement will involve a combination of Medusa shares, equity raisings and debt. Technical consultants from Corpac have visited the mine and milling facilities and Corpac has satisfied itself of the technical merits of the project.

The current timetable for the transaction indicate that completion, subject to successful due diligence, is likely near the end of February to early March 2005.

#### **4. BENEFITS OF THE ACQUISITION FOR MEDUSA**

Completion of the acquisition would give Medusa the following benefits:

- Control of a profitable gold mining operation;
  - Access to an immediate cash flow from an initial production of approximately 25,000 ounces on an annualised basis produced at less than US\$200/oz;
  - Production is planned to increase in early to mid 2005 with the commissioning of the additional Co-O Mine 3150m Level haulage level to approximately 35-40,000 ounces;
  - This gold production increase is without anticipated contributions from the Saugon project or other new production projects;
  - Milling facilities which are strategically located and can be expanded as production increases from multiple mine sites;
  - Control over a large, highly prospective tenement holding which will facilitate modern and systematic exploration for the first time ever;
  - An existing workforce, management and infrastructure that are working effectively and co-operatively with local communities;
  - Control of the Saugon joint venture which is currently being explored;
  - Other joint ventures which are funded for the first US\$1.5M of exploration expenditure;
  - A seamless transition from advanced explorer with anticipated initial production in the first quarter of 2005 to a producer with an increasing production profile.
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**Further information**

For further information contact the undersigned on 618-93670601 or by email to [admin@medusamining.com.au](mailto:admin@medusamining.com.au) Detailed descriptions of Medusa's projects can be viewed on Medusa's website [www.medusamining.com.au](http://www.medusamining.com.au)

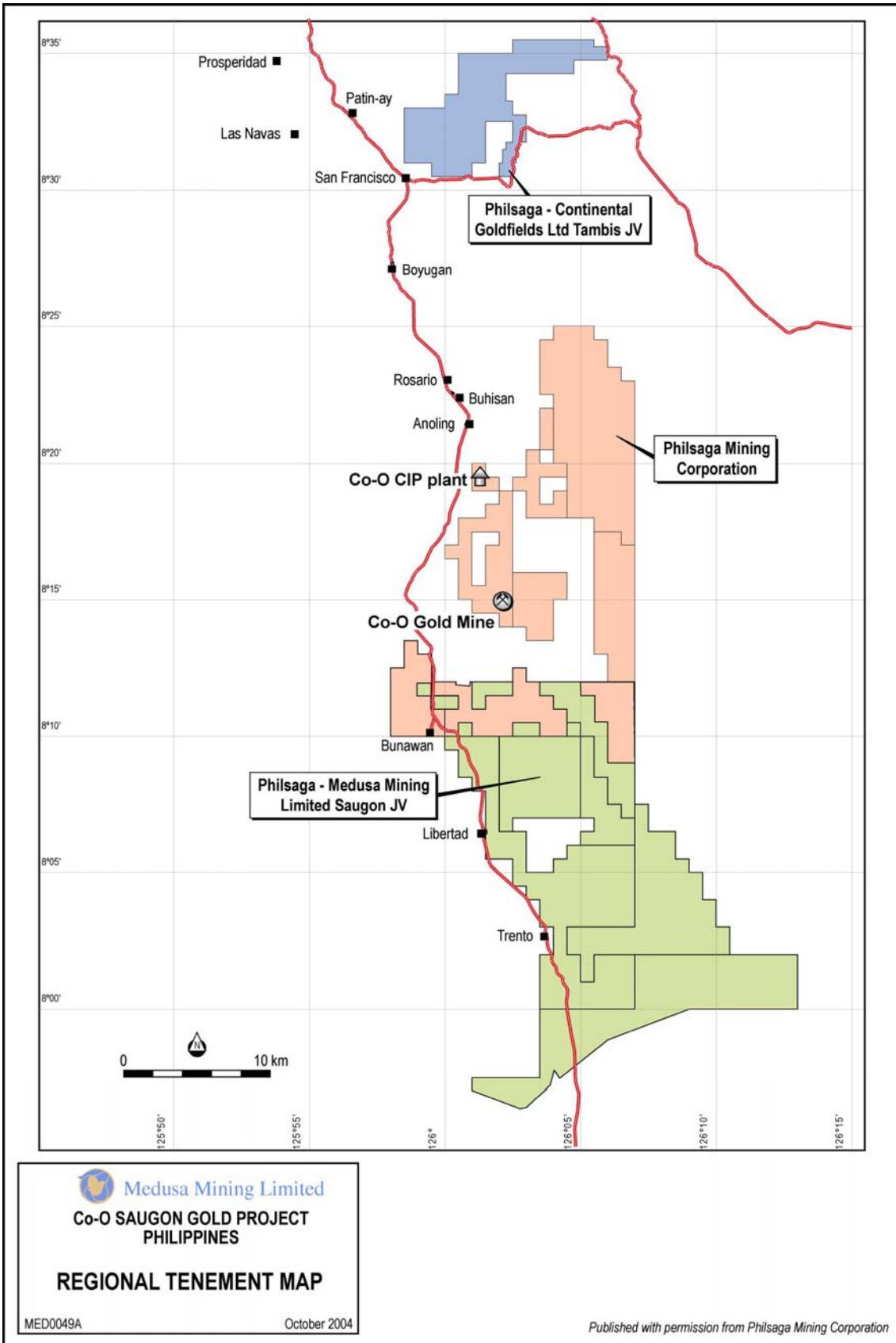
Yours faithfully

Geoff Davis  
Managing Director

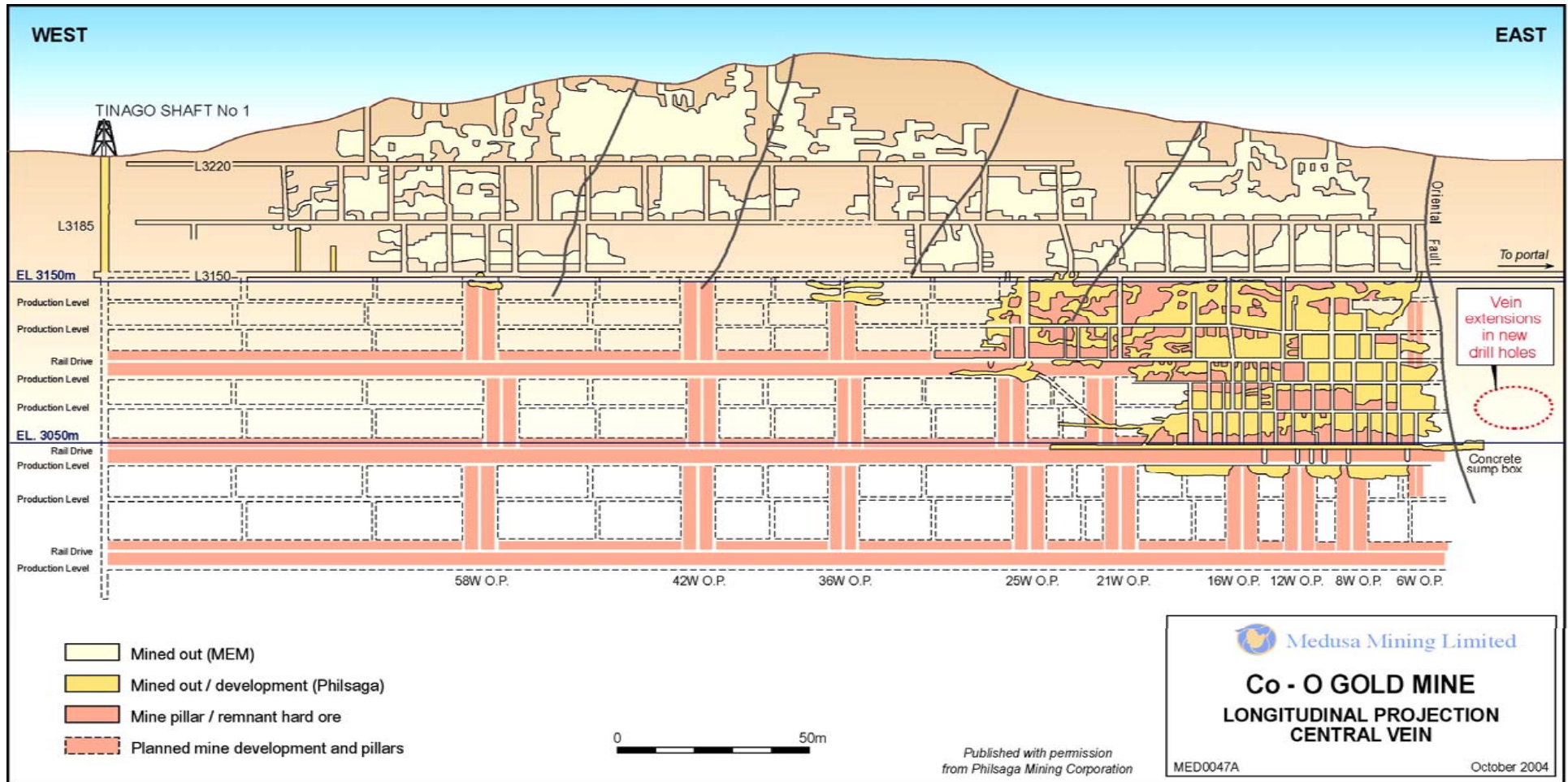
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Fig 1



**Fig 2**



**Fig 3**