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Cabral Resources Ltd (CBS)

Unlocking the infrastructure advantage

Recommendation
Buy (unchanged)
Price
\$0.07
Target (12 months)
\$0.27 (unchanged)
Risk
Speculative

Expected Return

Capital growth	286%
Dividend yield	N/A
Total expected return	286%

Company Data & Ratios

Enterprise value	\$3.3m
Market cap	\$17.9m
Issued capital	259.3m
Free float	92%
Avg. daily vol. (52wk)	380,950
12 month price range	\$0.06-\$0.23
GICS sector	Materials

Disclosure: Bell Potter Securities acted as Lead Manager for CBS' placement of 125m shares at 20 cents in February 2011. Bell Potter was paid fees.

Price Performance

	(1m)	(3m)	(12m)
Price (A\$)	0.07	0.08	0.16
Absolute (%)	11.94	0.00	-53.13
Rel market (%)	11.68	-4.14	-45.41

Absolute Price



SOURCE: IRESS

Drilling to commence in April, maiden JORC resource in Q3

Cabral Resources Ltd (CBS) is fully funded to commence an initial 3,000m drilling programme at its 100%-owned Morro do Gergelim project in Bahia State, Brazil (north of Minas Gerais). CBS is awaiting final environmental approval for drilling and plans to deploy two diamond drill rigs in mid-April for a 32-hole programme targeting 331Mt-644Mt of magnetite (+32% Fe) at Morro do Gergelim. Environmental approval is expected imminently. A maiden JORC-resource estimate is expected in Q3, CY12.

Mine to market route via 15Mtpa rail/port allocation

CBS has signed a Protocol of Intentions (POI) with Bahia State for access to 15Mtpa of capacity on the State-funded FIOL rail line, which is under construction. The plan is to transport iron ore to a proposed bulk shipping port north of Ilheus, ~450km from CBS' tenements. It is expected that the heavy haulage rail line (52Mtpa capacity) will be completed by 2014. **The State and Federal government is funding the \$5bn infrastructure development.** CBS would have a 15Mtpa export allocation at Porto Sul to export concentrate via cape-size vessels in the Atlantic. There is some uncertainty surrounding the timing of the port development, however, expected commissioning in 2014 would accommodate CBS' development schedule for production in 2015.

Investment view – Buy (Speculative), target \$0.27/share

CBS represents an early stage investment opportunity ahead of initial drilling results, metallurgical test work and subsequent de-risking milestones including a maiden resource estimate for Morro do Gergelim in Q3. **CBS is differentiated among its peers** by a strategic foothold in Bahia State. With possible access to government-funded rail and port infrastructure CBS is well positioned to unlock a significant location advantage in an emerging iron ore province. Cash of \$14.6m at December 21, 2011. Our valuation is based on a peer group comparison (see Table1 and page 6).

Catalysts (1) Initial drilling results, regional exploration and metallurgical test work, (2) maiden JORC resource estimate for Morro do Gergelim in August/September, (3) further tenement consolidation/potential transactions in Bahia State in CY12.

Table 1 – Peer group comparison of emerging iron ore companies

Company	EV (\$m)	Resource (Mt)	EV/Resource (\$/t)	EV/Res (\$/Fe unit)
Cabral Resources Ltd (CBS) – Resource target only*	3.8	331*	0.01	0.04
Iron Road Ltd (IRD)	75	2104	0.04	0.22
Sundance Resources Ltd (SDL)	1266	2300	0.55	1.45
Centaurus Metals Ltd (CTM)	47.5	116.5	0.41	1.52
Cape Lambert Resources Ltd (CFE)	338	680	0.50	1.76
South American Ferro Metals Ltd (SFZ)	70	230	0.31	0.69
Equatorial Resources Ltd (EQX)	210	N/A	N/A	N/A
ENRC transaction for nearby BML project in Bahia State, September, 2010	967	1800	0.54	1.58

SOURCE: BELL POTTER SECURITIES ESTIMATES

Morro do Gergelim project

Targeting +1Bt resources in an emerging iron ore province

CBS is fully funded for initial drilling at Morro do Gergelim and will likely deliver a maiden JORC resource estimate for the project in Q3. The company recently completed an aeromagnetic survey and geophysical modelling over 1,720km² in Bahia State. This has assisted with identifying priority targets for a 32-hole drilling programme (3,000m) from mid-April. The Morro do Gergelim project consists of Banded Iron Formation (BIF) interbedded with marble and quartzites and early exploration suggests the possibility of a plunging fold structure. Upcoming drilling is aimed at establishing a JORC resource of up to 644Mt of coarse grained magnetite at +32% Fe in line with CBS' plans to become a 4Mtpa-10Mtpa iron ore concentrate producer by 2015.

- Drilling in mid-April will target outcropping BIF south west of Iguatemi in the Lagoa Real Group of tenements (Figure 2). CBS' total tenement portfolio covers 332km².
- CBS has an initial resource target of up to 644Mt of magnetite at +32% Fe with a relatively coarse grind size of +75 microns estimated at Morro do Gergelim.
- CBS hopes to significantly expand its resource base to include hematite and itabirite ores with further exploration and through potential acquisitions of surrounding tenure.
- Serra do Tigre has similar BIF ridges in close proximity to Morro do Gergelim. This target provides additional scope for resource development and warrants drilling.
- CBS hopes to grow its resource base to +1Bt of beneficiable magnetite. CBS' three main tenement groups include Lagoa Real Group (64.4km²), Itaquarai (50.4km²) and Canabrava (213km²).

Figure 1 – Location of CBS' tenement portfolio in Bahia State, Brazil.



SOURCE: CABRAL RESOURCES LTD

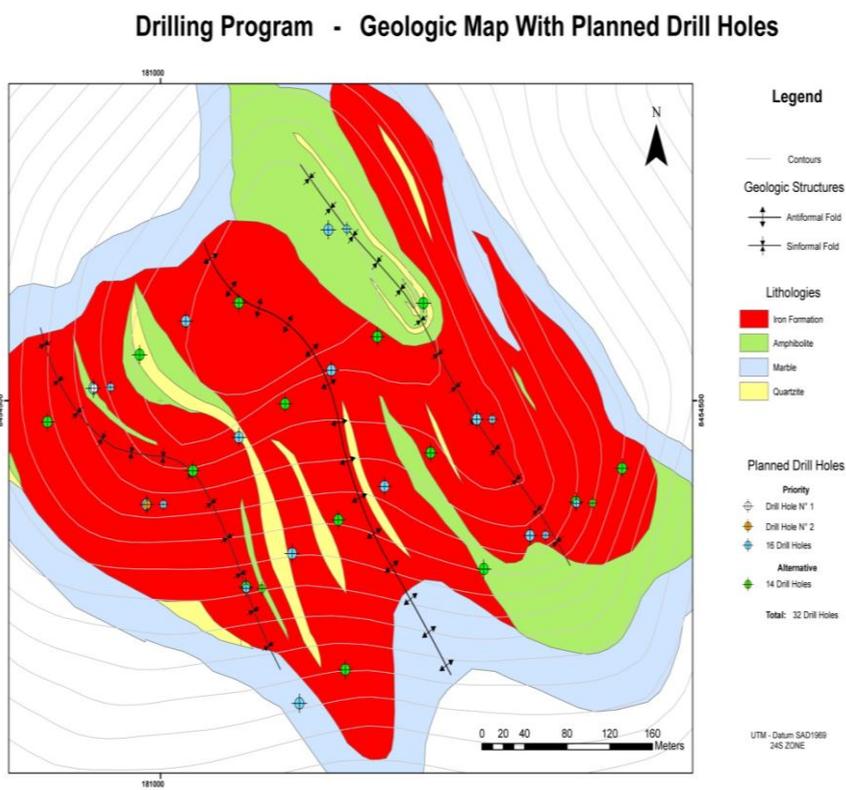
CBS' tenement portfolio in Bahia State, Brazil is ideally located within close proximity to the government-funded FIOCRIL rail line which is in construction.

Targets defined, drilling shortly

Final environmental approval for drilling at Morro do Gergelim is expected imminently and drilling will likely commence in mid-April. CBS has planned 32 diamond holes, including 14 holes on alternative sites. Diamond drilling will provide samples for metallurgical test work in Q3 and RC infill drilling will follow. CBS is confident of drilling some of the higher grade DSO targets within the Itaquari and Canabrava groups of tenements by July. The strategy is to focus on the coarse grained magnetite over the next six months with a view to establishing potential hematite/itabirite resources thereafter. There is a strong presence of both well lithified and fissile itabirite ores in the region. All of the BIF targets are highly metamorphosed and recrystallised (75 micron estimated). Figure 2 outlines the location of the planned 16 diamond holes to establish a maiden JORC inferred resource in Q3.

Figure 2 – Planned diamond drill holes at Morro do Gergelim

CBS has planned an initial 3,000m of diamond drilling to commence at Morro do Gergelim in mid-April.



SOURCE: CABRAL RESOURCES LTD

Serra do Tigre

A similar scale BIF anomaly to Morro do Gergelim and in close proximity, the Serra do Tigre prospect may provide CBS with significant operating synergies. Exploration is at early stage and drilling is required to gain a better understanding of the structural controls. Serra do Tigre is located within 20km of the FIOL railway and grab sample grades have exceeded 38% Fe.

Fazenda da Mata

Fazenda da Mata is a magnetic anomaly, which includes a deep magnetic low in the northern part of tenement area (prospective for hematite) between magnetic highs associated with a cross-cutting BIF. The area is within 10km of the FIOL rail line and may provide an additional source of higher grade concentrate for early cash flow.

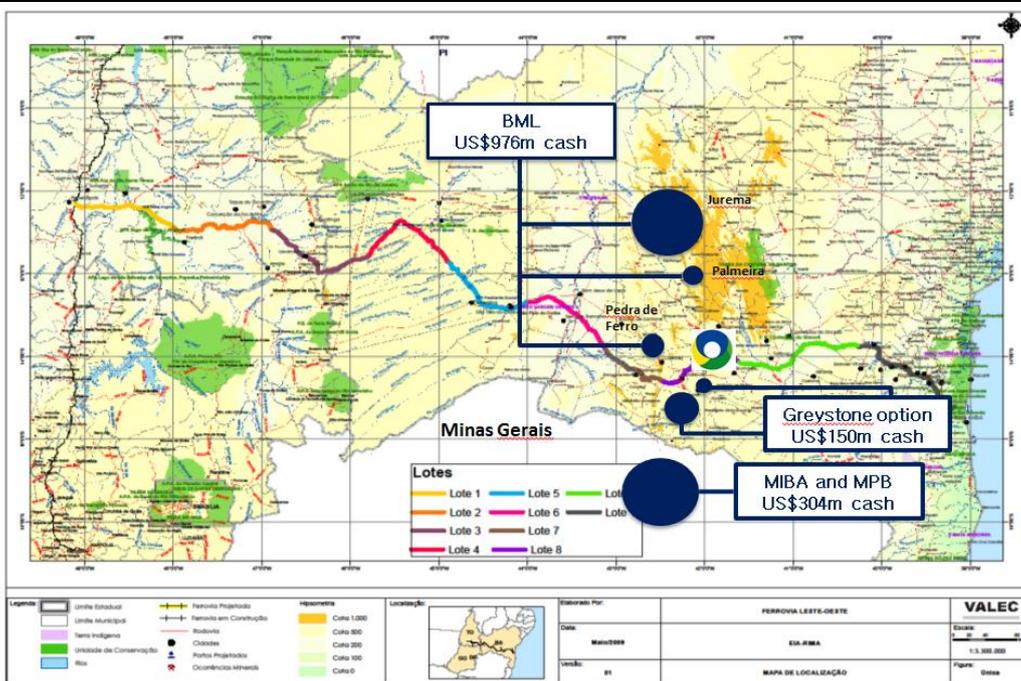
Infrastructure solution

Government-funded rail and port advantage

CBS has moved forward with respect to demonstrating an infrastructure solution to support its strategy to become a 4Mtpa-10Mtpa iron ore producer in Brazil. The planned FIOLE railway would conveniently pass through CBS' tenement portfolio and could provide a transport and export solution to meet CBS' development schedule. In March, CBS signed a Protocol of Intentions (POI) with Bahia State to secure access to up to 15Mtpa of capacity on the FIOLE rail line and at the proposed Porto Sul port development north of Ilheus. The agreement provides for additional assistance with road infrastructure, water, power and project financing from Brazilian agencies. The non-binding agreement is a step towards de-risking CBS' next phase of development and provides a positive framework.

- The FIOLE rail line is in construction and expected to be completed by 2014 at a cost of approximately \$5bn. The commissioning of the port development is expected that year and coincides with CBS plans for export in 2015.
- Initial capacity of the FIOLE rail line will be 52Mtpa with expansion capabilities. The rail line is expected to facilitate the export of higher volumes with debottlenecking and improved operatorship to exceed 52Mtpa in the medium to long term.
- Porto Sul is a proposed open access deep water port development for bulk commodities. It is expected that common user areas would be funded by Bahia State. The development is designed to accommodate cap-sized vessels and would have a 3.5km jetty constructed to allow export through the Atlantic at Ilheus (15Mtpa for CBS).
- Eurasian Natural Resources Corp (ENRC) has established a dominant footprint in Bahia State and invested \$1.3bn in acquiring projects proximal to the East West rail line. ENRC's BML project has a JORC resource of 1.8Bt at 32% Fe and 932Mt measured and indicated at 35.3% Fe (~523km from Ilheus). This development highlights the strategic importance of CBS' landholding and infrastructure capacity.

Figure 3 – Location of planned rail link between CBS' tenements and proposed Porto Sul



ENRC has invested \$1.3bn in acquiring projects proximal to the FIOLE rail line and CBS tenements.

SOURCE: CABRAL RESOURCES LTD

Corporate

Directors and Management

Non-Executive Chairman, Albert Wong

Non-Executive Director, Malcolm Hancock

Non-Executive Director, Bruno Maia

Managing Director and Chief Executive Officer, Michael Bogue

Exploration and Technical Director, Chris Robinson

Head of Exploration, Paul Ribeiro

Executive General Manager – Asia, Jingzhong (James) Li

Country Manager Brazil, Bruno Ribeiro

Major shareholders

Passport Capital LLC Group (9.6%)

Board members (8.2%)

Sun Hung Kai Investment Services Ltd (6.2%)

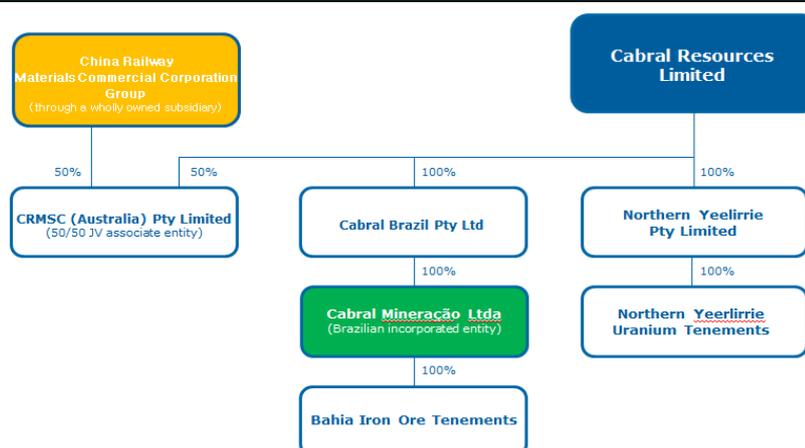
Capital structure

Ordinary shares: 259.3m

Cash: \$14.6m (December, 2011)

Debt: 0

Figure 4 – Company structure



SOURCE: CABRAL RESOURCES LTD

Chinese involvement

CBS has established a strong network of Chinese contacts to assist with development of the Brazilian projects, including access to off-take arrangements, JV partners, infrastructure solutions and project financing. This includes an existing JV with China Railway Materials Corp (CRM), one of the biggest steel users in China (\$20bn revenue in 2009). James Li (Executive General Manager) is well connected in China, has a good understanding of metallurgical requirements for Chinese steel mills and is across Chinese regulations and State-owned enterprises, generally.

Cabral Resources Ltd

Company overview

Cabral Resources Ltd (CBS) is an iron ore exploration company which is focused on resource development in Bahia State, Brazil. CBS is targeting a maiden JORC resource estimate for its Morro do Gergelim coarse grained magnetite project in Q3 CY12 and has a conceptual target of 331Mt-644Mt in addition to several regional targets. A maiden 3,000m drilling programme at Morro do Gergelim is scheduled to commence in mid-April and a maiden JORC resource is expected in August/September 2012. CBS recently signed a Protocol of Intentions with Bahia State to secure access to 15Mtpa capacity on the State-funded FIOL rail line to transport iron ore to a proposed bulk shipping port at Porto Sul, some 450km from Morro do Gergelim. It is expected that the heavy haulage rail line will be completed by 2014 and will support CBS' plans to export 4Mtpa-10Mtpa in 2015.

Valuation commentary

To arrive at a valuation, we use the middle of CBS' lower and upper exploration target for contained iron using 32% Fe content. This is an exploration target of 488Mt for 156Mt of contained iron. We assume that CBS could trade on the EV/Resource \$/Fe unit multiple of \$1.50/t based on several comparisons:

- ENRC transaction in Bahia in 2010 for BML (1.8Bt at 34% Fe) at \$1.58/t
- SDL trading at \$1.45/t (EV/Resource \$/Fe unit) and
- CTM trading at \$1.52/t

(Refer to Table 1 on page 1.)

CBS aims to deliver a maiden inferred resource in Q3. Using \$1.50/t of contained iron for 156Mt, we risk CBS by -70% to reflect the early stage nature of the project (no confirmation of grade and tonnes other than a conceptual target) and considerable execution and operational risk and we arrive at an EV of \$70m. We include \$1m cash at the time of the resource estimate, to arrive at a 12 month price target of 27 cents/share (259m shares).

Risks

(1) Exploration risk – Exploration is at an early stage. CBS has not drilled its targets and no JORC-compliant resources have been established.

(2) Execution/Operational risk – Any potential iron ore resource developments would be subject to further studies and agreements, including metallurgical test work, environmental approval, feasibility studies, project financing, confirmation of rail/port infrastructure access and off-take agreements.

(3) Sovereign risk – Brazil is considered to be a relatively stable mining jurisdiction by global standards, however, changes to regulatory policies or changes to infrastructure development plans could impact CBS' activities.

Recommendation structure

Buy: Expect >15% total return on a 12 month view. For stocks regarded as 'Speculative' a return of >30% is expected.

Accumulate: Expect total return between 5% and 15% on a 12 month view. For stocks regarded as 'Speculative' a return of between 5% and 30% is expected.

Hold: Expect total return between -5% and 5% on a 12 month view

Reduce: Expect total return between -15% and -5% on a 12 month view

Sell: Expect <-15% total return on a 12 month view

Speculative Investments are either start-up enterprises with nil or only prospective operations or recently commenced operations with only forecast cash flows, or companies that have commenced operations or have been in operation for some time but have only forecast cash flows and/or a stressed balance sheet.

Such investments may carry an exceptionally high level of capital risk and volatility of returns.

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