



**Breakaway
Research**

May 2012

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Capital Structure

ASX Code	ZYL
Share Price	A\$0.140
Ordinary Shares	488.5m
Options	27.0m
Fully Diluted Shares	515.5m
Market Cap	A\$69.4m
Less: Cash	A\$24.5m
Add: Debt	-
Enterprise Value	A\$44.9m

Directors & Management

Executive Chairman	Bevan Tarratt
Chief Executive Officer	Ian Benning
Executive Director	Phillipe Lalieu
Non-Exec. Director	John Beck
Non-Exec. Director	David Greenwood
Non-Exec. Director	Dr. Eric Lilford

Top 5 Shareholders

Macquarie Bank Ltd	8.2%
Sin Tang Dvlmt Pte Ltd	5.6%
Mighty River Intl Ltd	4.5%
HSBC Custody Nom Aust	3.5%
Riverview Corp Ltd	3.4%
Total Top 5	25%

1 Year Price Chart



Source: Bloomberg

ZYL Limited (ZYL)

Near-term producer of anthracite in South Africa

Recommendation: Speculative Buy

Key Points:

- A BFS is nearing completion for the Mbila anthracite project
- Preferred project debt providers have been selected and Mbila is on track to commence production in Q3 2013
- Anthracite is used to process ferro-alloys, steel and mineral sands, and is a low-cost coking coal substitute
- Feasibility assessment of the Kangwane project is also well advanced, providing medium-term growth and diversification
- ZYL has received unsolicited approaches for offtake

ZYL Limited ('ZYL' and the 'Company') is an ASX-listed metallurgical coal exploration and development company with two advanced anthracite projects in South Africa. All of ZYL's projects host large anthracite resources and are in close proximity to key infrastructure, including ports and rail. ZYL is well placed to take advantage of a growing shortfall in South African and international anthracitic coal markets.

Company Overview:

ZYL's objective is to become a leading producer of anthracite for both South African and export markets. It has prioritised development of its Mbila project in KwaZulu-Natal province for the delivery of high-grade anthracite, primarily to South African industrial consumers. Over the medium-term, the company also plans to develop its Kangwane project, consisting of the Kangwane South and Central areas, in Mpumalanga province, which will produce anthracite for export markets.

Mbila is ZYL's most advanced project and is on track to commence producing anthracite in Q3 2013. An interim Feasibility Study outlined a project with high operating margins between A\$82.2/t and A\$59.2/t. The project is located close to critical infrastructure, minimising up-front capital costs to A\$84.5 million. A shortlist of preferred debt providers has been selected. Current reserves of 33.4Mt support a long life operation, as well as providing potential for expansion.



Investment Review

Near-Term Anthracite Producer

ZYL plans to commence production during Q3 2013

ZYL has the right to acquire up to 74% of the Mbila project. The Company plans to develop an anthracite operation at Mbila at a relatively low initial development cost of around A\$85m, commencing production in Q3 2013. The capital requirements of the project will be covered by a combination of cash reserves, debt and new equity. The Company has selected Standard Chartered Bank and Nedbank Capital as preferred debt providers, with indicative debt likely to be in the order of A\$60-75 million. When combined with current cash reserves of around A\$24.5 million, this minimises the risk of significant shareholder dilution during the financing process.

High-Margin Producer

The IFS highlighted strong margins of between A\$82.2/t and A\$59.2/t

An Interim Feasibility Study ('IFS') outlined strong operating margins of between A\$82.2/t and A\$59.2/t for Mbila, depending upon which coal seam is being mined. Using January 2012 coal prices, this would result in annual operating earnings (before taxes, royalties and depreciation) in the order of A\$40m p.a. for the project. This level of earnings is attractive, given the mine (under the first stage) will only produce 580,000t p.a. of saleable product. Being a high-margin producer also mitigates commodity price risk.

Table 3: Mbila – Indicative Annual Operating Parameters

	Ecca Seam	Beaufort Seam	Total
ROM Production (Mt)	0.42	0.42	0.84
Saleable Product (Mt)	0.27	0.31	0.58
Mine Gate Price* (A\$/t)	135	112	123
Revenue (A\$m)	36.5	34.7	71.2
Cost (A\$m)	14.3	16.4	30.6
Operating Profit (A\$m)	22.2	18.4	40.5

**Based on anthracite prices as at Jan 2012*

Source: ZYL and Breakaway Research

Anthracite – A Growth Industry

Anthracite is highly sought after by South African industry

Anthracite is the most-altered and highest-ranking form of coal. It has the highest level of fixed carbon, and also has low levels of volatile matter and impurities. While traditionally used as a source of heating, anthracite now is highly sought after by South African and international ferro-alloy and mineral sands industries and is in demand globally as a substitute for coking coal (metallurgical coal).

Anthracite is a low-cost substitute for coking coal

Unlike coking coal, anthracite does not require processing to reduce volatile matter and impurities; a process that can cost as much as US\$140/t. The price of anthracite, currently around US\$130/t, trades at a significant discount to coking coal (currently ~US\$230/t), making it a low-cost substitute.



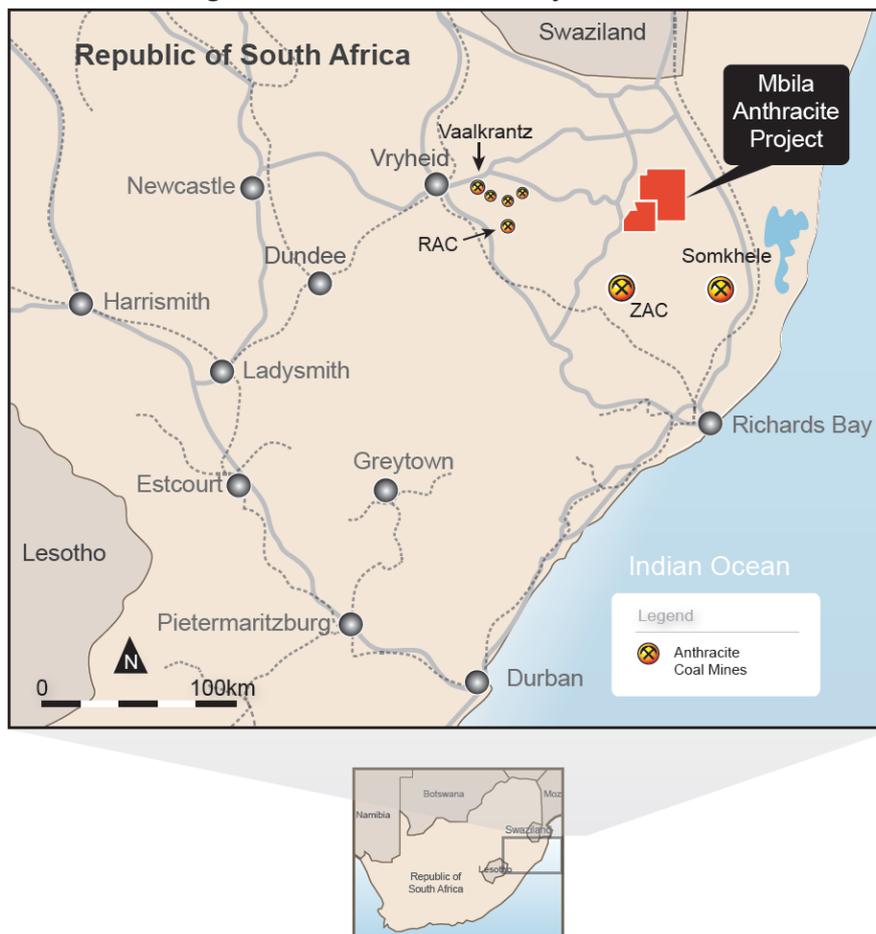
Project Review

The Mbila Anthracite Project

Mbila is located just 150km northwest of Richards Bay

The Mbila Anthracite project is located in the KwaZulu-Natal province of South Africa, just 150km northwest of the major South African coal export terminal of Richards Bay (see Figure 1). The project, which consists of a 19,120Ha Mining Right Area ('MRA') and a 53,000Ha Prospecting Right Area ('PRA'), is also located in close proximity to rail infrastructure and coal processing plants.

Figure 1: Mbila Anthracite Project Location



Source: ZYL Limited

Mbila Anthracite Coal Resources

Over 73% of the resources in the MRA are Measured & Indicated

The Mbila project has been extensively drilled, with over 564 holes drilled within the project area by BHP Billiton (439 bore holes) and, more recently, by Mbila (125 bore holes). The data from this drilling has been used to define 125Mt of high-quality anthracite resources compliant with the JORC code ('JORC-compliant'). Over 73% of the resources within the Mbila MRA are in the Measured and Indicated categories. ZYL has also identified additional exploration targets of 20-60Mt within its tenements.

Table 1: Mbila JORC-Compliant Resources

Category	Mbila
Measured	25Mt
Indicated	67Mt
Inferred	33Mt
Total	125Mt

Source: ZYL Limited



Interim Feasibility Study

The IFS confirmed a low production cost of A\$52/t

The Company recently released the results of its interim feasibility study ('IFS') for Phase 1 of production on the MRA at Mbila, which currently hosts 33.4Mt of reserves. The IFS confirmed the potential to produce a high-quality anthracite product at an average cash operating cost of A\$52/t of saleable coal, for an up-front capital cost of A\$84.5m. The IFS assumes a 'mine gate' pricing scenario for the Ecca and Beaufort seams primary products of A\$135/t and A\$112/t respectively.

Table 2: Mbila Project Reserves

Seam	Reserves	Category
Ecca	6.4Mt	Proven
Beaufort	3.6Mt	Proven
Beaufort	23.4Mt	Probable
Total	33.4Mt	

Source: ZYL Limited

The operating margin ranges from A\$82.2/t to A\$59.2/t

Phase 1 is based on run-of-mine ('ROM') production of 0.84Mtpa to produce 0.58Mtpa of saleable anthracite. Using these assumptions, Mbila would generate high operating margins of A\$82.2/t and A\$59.2/t for the Ecca and Beaufort seams respectively. In turn this would support pre-tax operational earnings in the order of A\$40Mpa (see Table 3).

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*Based on anthracite prices as at Jan 2012

Source: ZYL and Breakaway Research

Mbila Product & Off-take

ZYL has received interest for off-take of over 2.3Mt p.a.

The Mbila product has been targeted for the domestic market due to its high-quality, low-phosphorus, low-ash and low-sulphur characteristics. Products with these characteristics are experiencing strong demand from South African producers of mineral sands, ferrochrome, ferromanganese and silicon carbide. ZYL expects to sell this product at the 'mine gate' for premium prices.

Table 4: Mbila Anthracite Product Quality (Washed)

	Ecca Seam	Beaufort primary product	Beaufort secondary product
Coal classification	High Rank B anthracite	High Rank C anthracite	Mid Rank anthracite
Yield %	64.3	51.2	17.3
Phosphorus %	0.008	0.012	-
Ash content %	9.7	14.9	22.0
Inherent moisture %	2.1	1.1	1.0
Volatile matter %	5.1	5.8	5.5
Fixed carbon %	83.1	78.2	71.4
Gross calorific value MJ/kg	31.58	29.45	25.38
Total sulphur %	1.04	0.65	0.84

Source: ZYL Limited



ZYL has received interest for off-take of over 2.3Mt p.a.

ZYL has received a number of non-binding Expressions of Interest ('EOIs') for off-take from Mbila, some of which are from major international coal mining companies. Together, these EOIs account for more than 2.3Mt p.a. of ROM coal, exceeding the full planned output for Phase 1 and 2 of the mine development plan. ZYL is currently seeking to formalise these EOIs and is re-engaging with parties that have previously expressed interest.

Exploration Potential

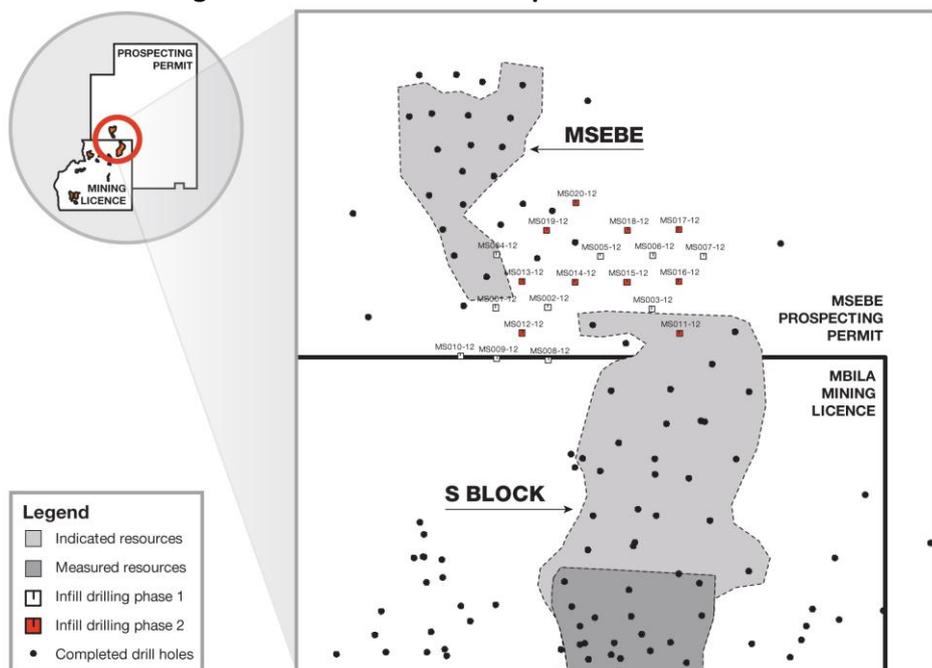
ZYL has outlined significant further exploration potential

ZYL believes that there is considerable potential to define additional open-cut and underground resources within the Mining Right area (beyond the current 125Mt resource). The Company has commenced a drilling program to test the potential for additional coal within the project area, and has an exploration target of 20-60Mt.

An updated resource model is due to be released in June

The Company has commenced Phase 1 and of a two-phase infill drilling program between the Mbila MRA and the Msebe PRA (see Figure 2). Phase 1 is comprised of 10 diamond drill holes for 2,000m of drilling, and Phase 2 will involve an additional 10 diamond for another 2,000m. The results from both programs will be incorporated into an updated resource model and future mine planning. The Company expects to be able to release the updated resource model during June.

Figure 2: Mbila Anthracite Deposits & Tenements



Source: ZYL Limited

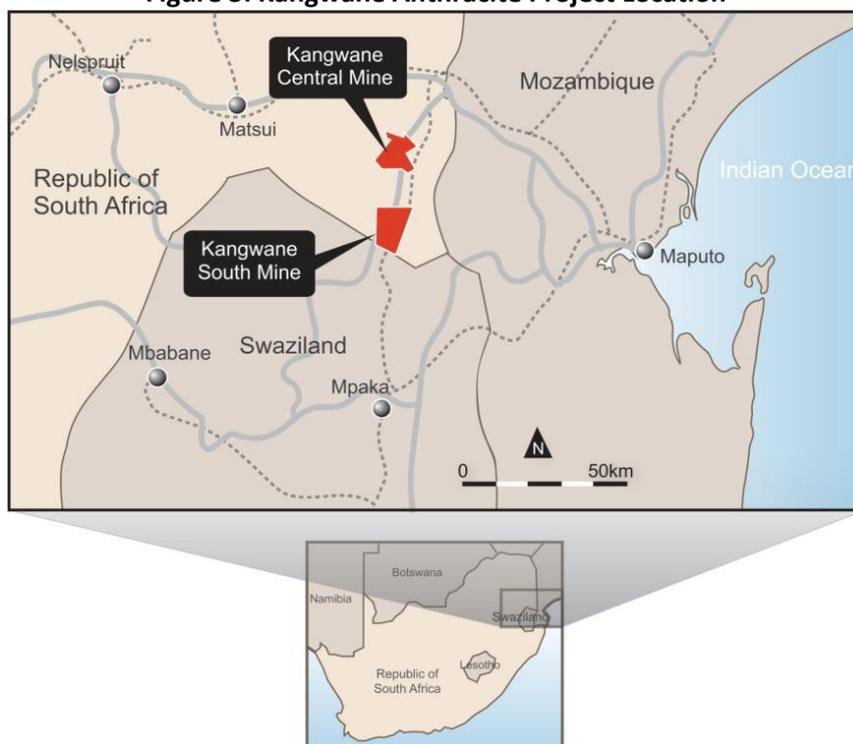


The Kangwane Central Anthracite Project

Kangwane is close to key infrastructure

ZYL has the right to earn a 50.12% interest in the Kangwane Central project. Kangwane is located in the Mpumalanga province of South Africa, around 127km from the coast by rail to the Maputo Port in Mozambique (see Figure 3). The project is strategically located close to key infrastructure, including rail, port, water, electricity, roads, and a semi-skilled workforce. A rail siding at the southern tip of the tenement feeds directly into the main rail network, which continues east to the port at Maputo and west to the established South African industrial coal market.

Figure 3: Kangwane Anthracite Project Location



Source: ZYL Limited

Kangwane Central Anthracite Coal Resources

The project hosts a 136Mt anthracite resource

The Kangwane Central project hosts JORC-compliant resources of 136Mt, including an Indicated component of 54Mt (see Table 3). The global resource includes two open-cut resources (Northern and Southern) that contain a total of 60.8Mt (see Table 6). These near-surface 'open-cut' areas sub-crop on the western side of the project area, and the Southern open-cut area will be the focus of ZYL's BFS for Kangwane Central.

Table 5: Kangwane Central Resources

Category	Resource
Measured	-
Indicated	54Mt
Inferred	82Mt
Total	136Mt

Source: ZYL Limited

Table 6: Kangwane Central Open-Cut Resources

Area	Resource
Northern	11.2
Southern	49.6
Total	60.8

Source: ZYL Limited

Total resources include an open-cut component of 60.8Mt



Exploration and Drilling

Kangwane Central has a 260-315Mt exploration target

The Company has also outlined an exploration target of 260Mt-315Mt with a calorific value of 27.8/MJ-28.1MJ/kg. During Q1, ZYL commenced a 5,000m, 25-borehole (Phase 3) drilling program to follow up on previous exploration, test this exploration target and delineate Reserves. The primary focus of the program is to outline additional open-cut resources. The full drilling programme, analysis and subsequent geological modelling are expected to be completed during Q3 2012.

Route to Market and Off-take

ZYL is looking into a trucking operation to a nearby port

ZYL has made an in-principle decision to proceed with an export operation at Kangwane Central; trucking high-quality anthracite product to the Mozambican port of Maputo. Trucking will utilise an existing tarred road, which will not require upgrading, for a distance of approximately 145km. There is available capacity at the Maputo Bulk Handling Terminal.

Kangwane Central is immediately north of an existing operation

Kangwane Central is located immediately north of an existing anthracite operation that transports a washed product to local industrial consumers, including ferro-chrome, ferro-manganese, vanadium and platinum producers, on the Highveld in South Africa. ZYL has received EOIs for off-take at Kangwane that together account for 1.7Mtpa ROM coal, exceeding the initial planned output for the project.

Table 7: Kangwane Central Anthracite Product Quality (Washed)

	@ 20% ash	@ 16% ash
Yield %	79.34	66.36
Ash content %	17.78	15.46
Inherent moisture %	2.43	2.40
Volatile matter %	6.35	6.17
Fixed carbon %	74.32	76.80
Gross calorific value MJ/kg	27.74	28.70
Total sulphur %	0.62	0.61

Source: ZYL Limited

Feasibility Studies

ZYL expects to complete a BFS during 2012

ZYL has completed a pre-feasibility study at Kangwane Central for an operation that mines and processes 1.8Mtpa of ROM anthracite to produce 1.2Mtpa of saleable product for export to international markets. ZYL's share of the capital cost of the project was estimated to be A\$58 million. The project was assessed as an export operation due to its proximity to the Mozambican port of Maputo.

This project is now being advanced through a BFS, which the Company expects to complete during 2012.

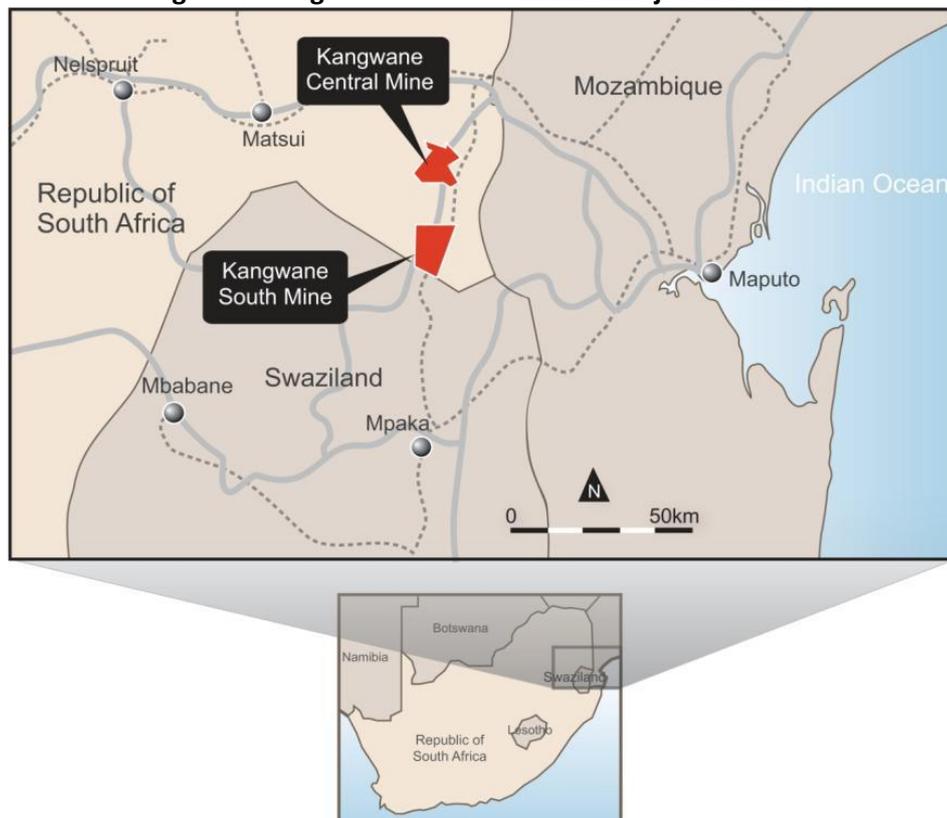


The Kangwane South Anthracite Project

Kangwane South also has excellent infrastructure access

The Kangwane South project (ZYL 70%-owned) is also located in the Mpumalanga province of South Africa and is approximately 25km south of Kangwane Central (see Figure 4). The project has the same close proximity to rail, port, water, electricity and domestic industrial consumers as Kangwane Central.

Figure 4: Kangwane South Anthracite Project Location



Source: ZYL Limited

Exploration undertaken by the project's previous owners outlined a conceptual exploration target of 20Mt-100Mt at a calorific value of 22MJ/kg-28MJ/kg (unwashed). To date a JORC-compliant resource of 99Mt of anthracite has been delineated (73.9Mt Indicated and 25.8Mt Inferred).

Table 8: Kangwane South Anthracite Product Quality (Washed)

	Seams 5 & 6	Seam 3
Yield %	41.20	64.37
Ash content %	17.00	16.81
Inherent moisture %	1.28	1.69
Volatile matter %	8.04	7.68
Fixed carbon %	73.67	73.82
Gross calorific value kcal/kg	6 834	6 725
Total sulphur %	0.62	0.59

Source: ZYL Limited

Kangwane South's anthracite is also export-quality



The Anthracite Market

What is anthracite?

Anthracite is the most-altered and highest-ranking form of coal. It has the highest level of fixed carbon (often up to 98%), and it also has low levels of volatile matter and impurities. Anthracite is the oldest, hardest and cleanest-burning form of coal.

Anthracite is the most-altered and highest-ranking form of coal

What is anthracite used for?

Anthracite was traditionally used as a source of heating, but now is highly sought after by South African and international ferro-alloy and mineral sands industries and is in demand globally as a substitute for coking (metallurgical coal). Anthracite, due to its low levels of volatile matter and impurities, burns cleanly (low sulphur) and produces very little in terms of smoke emissions; this is useful in a closed industrial furnace.

Used in the steel, mineral sands and ferro-alloys industries

Anthracite vs. coking coal

The use of closed furnaces in industrial ovens for the smelting of iron ore, mineral sands and ferro-alloys, means the release of smoke or emissions can be present a major issue; smoke released builds up pressure. To counter this, coking coals are processed to reduce volatile matter and impurities. This process, however, can cost as much as US\$140/t, adding to the cost of the already-expensive coking coal (coking coal is currently trading at around US\$230/t).

Anthracites can be used as a coking coal substitute

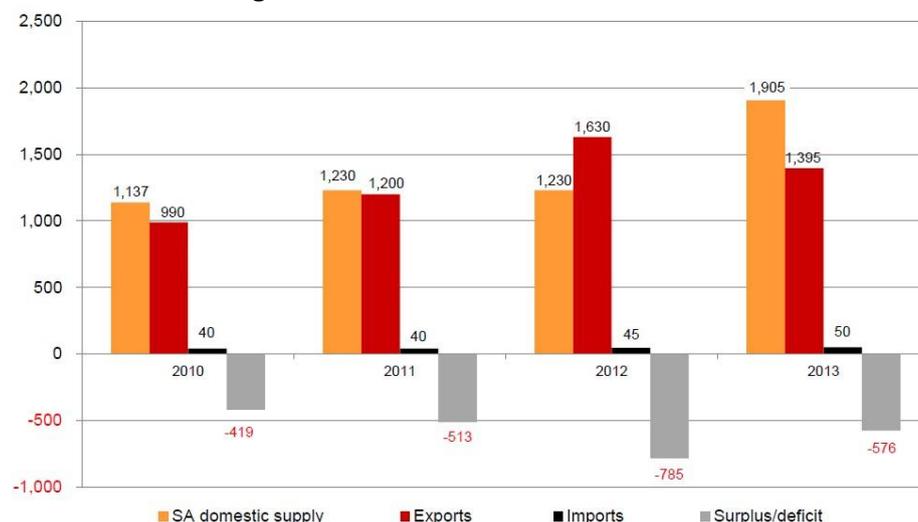
Given that anthracite trades at around US\$130/t (depending upon the quality), it can be used as a coking coal substitute to help reduce costs. One drawback of anthracite is that it does not swell under extreme heat; this is a key property of coking coal that is essential as an oxygen reductant in smelting iron ore. Therefore, in steel production, anthracite needs to be blended with coking coal.

South African Anthracite Market

South Africa, as well as being the largest producer of high-quality anthracite, is a major consumer; the nation has a large industrial smelting industry. The South African market for anthracite has been in deficit for at least three years (see Figure 5).

South Africa is a major consumer of anthracite

Figure 5: South African Anthracite Market



Source: ZYL Limited



Directors & Management

Bevan Tarrat (Executive Chairman) has over 10 years experience in accountancy and business development

Ian Benning (Chief Executive Officer) has 30 years' mining industry experience in production and mine management, as well as investment banking

Phillipe Lalieu (Executive Director) has extensive experience in the acquisition and sale of Sub-Saharan African mining assets

John Beck (Non-Executive Director) has over 30 years experience in finance and general management

Dr Eric Lilford (Non-Executive Director) holds a PhD in minerals economics and has over 23 years operational and investment experience

David Greenwood (Non-Executive Director) has over 29 years of geological and mining experience

Bevan Tarrat (Executive Chairman) has over 10 years' experience as an accountant, having worked in a various accounting firm and is a former partner at Marlston Taxation & Financial Services. In addition, Mr Tarrat has comprehensive practical business background and an extensive experience in primary and secondary capital raisings and corporate strategic consulting. Mr Tarrat is Non-Executive Chairman of ASX-listed Pura Vida Energy NL (ASX: PVD) and is a Non-executive Director of Minerals Corporation Limited (ASX:MSC) and Stonehenge Metals Limited(ASX:SHE).

Ian Benning (Chief Executive Officer) has 30 years' mining industry experience in production and mine management, as well as investment banking. Ian previously worked for Anglo American. Ian also manages Hemisphere Corporate Services in South Africa, a privately-owned company which is an investment vehicle with a wide range of interests in various mining-related entities. Ian was previously a Non-Executive Director of Noventa Limited (AIM: NVTA, TSX: NTA) and is also currently the Non-Executive Chairman of Segue Resources Limited (ASX: SEG).

Phillipe Lalieu (Executive Director) has extensive experience in the acquisition and disposal of Sub-Saharan African mining assets as well as the raising of exploration and mine development funding for green and brown field mining projects. Phillippe has also given resource specific regulatory and compliance advisory. Phillippe is a co-founder of Opes Capital and has established and managed Growth Partnership South Africa. He also worked for Anglo Platinum in corporate finance and business development roles.

John Beck (Non-Executive Director) has over 30 years experience in finance and general management, with over 10 years, as the CEO of Mineral Technologies International SA, a company actively involved in both South African and International anthracite markets. He is also a former CEO of South African mobile telephone network MTN and is Chairman and CEO at Mbila Resources (Pty) Limited.

Dr Eric Lilford (Non-Executive Director) holds a PhD in minerals economics, a NHD in coal mining, as well as a BSc and MSc Eng in Mining. He has over 23 years operational and investment experience across the global resources sector including the completion of both pre feasibility and bankable feasibility studies in numerous jurisdictions, mine production experience as well as corporate advisory and debt arranging for mining companies. Dr Lilford worked for companies like Deloitte and Touche Tohmatsu, Beny Steinmets Group Resources, Randcoal Limited's Rietspruit and Khutala coal mines.

David Greenwood (Non-Executive Director) has over 29 years of geological and mining experience with a number of coal, precious metal and base metal producers. He is currently the Executive General Manager – External Affairs and Exploration with Straits Resources Ltd where he is involved in investor relations, exploration, marketing and corporate budget development and strategic business planning.



Analyst Verification

We, Howard Humphreys and Grant Craighead, as the Research Analysts, hereby certify that the views expressed in this research accurately reflect our personal views about the subject securities or issuers and no part of analyst compensation is directly or indirectly related to the inclusion of specific recommendations or views in this research.

Disclosure

Breakaway Investment Group (AFSL 290093) may receive consultancy fees and commissions on sale and purchase of the shares of ZYL Limited and may hold direct and indirect shares in the company. It has also received a commission on the preparation of this research note.

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