

AUSTRALIAN

RESEARCH

INDEPENDENT INVESTMENT RESEARCH

Galaxy Resources Limited (ASX: GXY)

9 November 2010

Key information	
Share price	\$1.47
Valuation range	\$1.48 – \$1.93
Price performance	
Market statistics	
52-Week High	\$1.81
52-Week Low	\$0.91
Avg 3mthly turnover (M)	1.2
Shares Outstanding (M)	191
Market Capitalization (M)	\$281
% of All Ords	0.0
Mining specific information and rating	
Enterprise Value/2P Reserves	\$24
Project financing	****
Off-take agreements	*****
Proximity to infrastructure	*****
Key valuation inputs	
Risk Free Rate	4.5%
Risk Premium	6.0%
Beta	1.7
Cost of equity	14.7%
Cost of debt	SIBOR + 4.5%
Target debt/equity ratio	43/57
Tax Rate	30%
WACC1	0.0%
Company facts	
Major Shareholders	
Creat Resources	19.9%
National Nominees	5.4%
HSBC Custody Nominees (Aust) Ltd	4.5%
Directors	
Iggy Tan	Managing Director
Charles Whitfield	Executive Director
Anthony Tse	Executive Director
Craig Redhead	Non Executive Chairman
Robert Wanless	Non Executive Director

Galaxy Resources Ltd. (ASX: GXY), based in Perth WA, is an emerging mineral exploration and chemical company focused on the development of its primary lithium resource at Mt Cattlin in Ravensthorpe WA.

The Company's current focus is the development of its lithium projects to capitalize on an expected surge of demand for lithium-ion batteries for use in hybrid and electric vehicles in China.

Commencement of mining at Mt Cattlin heralds an important phase in the company's development, which will eventually complement its offshore downstream lithium carbonate chemical plant, currently under construction in Jiangsu Province, China.

We believe Galaxy Resources (ASX: GXY), is well positioned to extract synergy gains from its vertical integration strategy and capitalize on the growing demand for lithium carbonate in the Asian region, as the trend towards lithium battery power gathers momentum. We initiate coverage of Galaxy Resources Limited (ASX: GXY) with a fair value range of between **\$1.48 and \$1.93**.

Key points

Galaxy is the only lithium pure play currently listed on ASX.

Vertical integration strategy underpins potential synergy gains and a low cost position.

Strong Management Team. Four recent appointments add significantly to board's expertise in the Hong Kong and Chinese corporate sector.

Lithium market fundamentals are attractive and strengthening. Increasing consumption of lithium batteries in China is expected to accelerate in the near term given the growth of hybrid and electric vehicles.

Downstream lithium carbonate contracts in place. Off-take contract agreements for the sale of the total output of lithium carbonate to Japanese trading house, Mitsubishi Corporation, and the top thirteen largest cathode producers in China are in place pending the commencement of operations at the Jiangsu lithium carbonate plant (now expected in 2Q11).

Valuation. Our valuation of GXY incorporates a Discounted Cash Flow (DCF) under 3 different scenarios, using a weighted average cost of capital (WACC) of 10.0% to derive a fair value target range of between \$1.48 and \$1.93.

Earnings summary

Yr	Revenue (A\$M)	NPAT (A\$M)	EPS (¢)	PER	DPS (¢)	Cash Balance (A\$M)	ROA	ROE
2H09*	1.20	-12.3	-0.12	na	0.0	83.4	na	na
2010F	55.0	5.9	0.03	47.6	0.0	139.0	5%	6%
2011F	165.6	51.6	0.27	5.4	0.0	114.7	26%	34%
2012F	168.4	53.9	0.28	5.2	0.0	168.9	23%	25

Analyst: Chris Kallos CFA

	A\$m	2H09	2010	2011	2012	Key Ratios	2010	2011	2012	2013
		6months ended 31 Dec 09				Revenue growth (%)	na	201%	2%	2%
						EPS growth (%)	na	4%	4%	4%
Profit & Loss*						EBITDA/Revenue Margin (%)	41%	56%	57%	57%
Total Revenue	1.2	55.0	165.6	168.4		EBIT/Sales Margin (%)	28%	47%	48%	49%
Total costs	13.9	32.5	72.9	73.1		Tax rate (%)	30%	30%	30%	30%
EBITDA	-12.7	22.4	92.7	95.4		ROA (%)	5%	26%	23%	21%
Depreciation/Amortisation	0.0	-6.8	-14.2	-14.2		ROE (%)	6%	34%	25%	20%
EBIT	-12.7	15.6	78.5	81.2		DCF Valuation Inputs				
Interest	0.0	-8.8	-6.3	-5.8		Risk Free Rate	4.5%			
Pre-Tax Profit	-12.3	8.4	73.7	77.0		Risk Premium	6%			
Tax expense	0.0	2.5	22.1	23.1		Beta	1.7			
Net Profit	-12.3	5.9	51.6	53.9		Cost of equity	14.7%			
						Cost of debt	SIBOR + 4.5%			
Cash Flow						Target debt/equity ratio	43/57			
EBITDA	-12.7	22.4	92.7	95.4		Tax Rate	30%			
Working capital	0.0	-5.0	-5.0	-1.0		WACC	10.0%			
Income tax paid	0.0	0.0	-2.5	-22.1						
Interest & other	0.0	-8.8	-6.3	-5.8		Key Model Assumptions				
Operating Activities	-4.5	8.6	78.8	66.5		ROM production rate (mtpa) by 2011	1			
PPE	-7.2	-101.0	-51.0	0.0		Head Grade (%Li2O)	1.1			
Exploration	-2.1	-3.5	-3.5	-3.5		Recovery rate (Li2O)	80%			
Investments	0.0	1.3	1.3	1.3		Head Grade (Tantalite) ppm	135			
Investment Activities	-9.8	-103.2	-53.2	-2.2		Recovery rate (Li2O)	65%			
Borrowings (Drawdown/Repaid)	21.9	153.4	-50.0	-10.0		State royalty % of revenue	5			
Equity	71.9	61.8	0.0	0.0		Capex 2010 (A\$m) ~	101			
Financing Activities	93.8	215.3	-50.0	-10.0		Capex 2011(A\$m) ~	51			
						Depreciation method – straight line				
Net Cash	79.5	120.7	-24.4	54.3		No dividend payment				
Cash at beginning	3.4	18.3	139.0	114.7		A\$/US\$ rate to revert to 10 yr average	0.73			
Cash at end	83.4	139.0	114.7	168.9						
						Pricing Assumptions	2010	2011	2012	2013
Balance Sheet						Spodumene Price (US\$/t 6% Li2O Conc)	400	400	400	400
Cash and cash equivalents	83.4	139.0	114.7	168.9		Lithium Carbonate (US\$/t)	6000	6120	6242	6367
Exploration and evaluation exp.	1.3	5.0	5.0	5.0		Tantalite Price (US\$/lb)	85	85	85	85
Other (inventories & receivables)	1.9	25.0	25.0	25.0		AUD/USD	0.73	0.73	0.73	0.73
PPE	20.8	121.8	157.8	153.8						
Total Assets	109.0	290.8	302.5	352.7		Operating Cost Assumptions(A\$/t)				
Total Debt	22.4	175.8	125.8	115.8		Mining	12			
Total Liabilities	28.6	195.8	150.8	140.8		Processing WA	17.5			
Shareholder Funds	80.4	95.0	151.7	211.9		Transport & Admin	3.5			
Shares on Issue (M)	103	190.6	190.6	190.6						
Options outstanding		24.0	24.0	24.0		Major Shareholders (as at Dec 3, 2010)				
						Great Resources	19.9%			
						National Nominees Ltd	5.4%			
						HSBC Custody Nominees (Aust) Ltd	4.5%			
						Ademsa Pty Ltd	4.0%			
						Super Raya International Ltd	3.5%			
						HSBC Custody Nominees (Aust) Ltd- GSCO ECA	2.4%			
						Citicorp Nominees	2.4%			
						JP Morgan Nominees Pty Ltd	2.1%			
						Equity Trustees Ltd	1.0%			
						Mr Robert James Wanless	0.7%			
						Mineral Administration Services	0.7%			
						Romadak Pty Ltd	0.7%			

* Based on Life of Mine of 11 years

SWOT analysis

Strengths

- ◆ Open pit mining method supports a relatively lower cost of extraction.
- ◆ Off-take contract agreements secure downstream lithium carbonate income streams pending the completion of the Jiangsu facility.
- ◆ Sale of 27,000 tonnes of spodumene concentrate (first two shipments) to another lithium carbonate producer in China has been secured in lieu of the delay in opening of the Jiangsu facility, which provides some interim cash flow.
- ◆ Potential cost advantage associated with vertical integration strategy.
- ◆ Mt Cattlin mine is in close proximity to infrastructure.
- ◆ Lithium market fundamentals are attractive and strengthening.
- ◆ Strong management team.
- ◆ Potential Hong Kong listing may facilitate future capital raisings through access to larger overall investor base.

Opportunities

- ◆ GXY tenements hold other mineral prospects.
- ◆ Burgeoning lithium ion battery market driven by trend towards low emission technologies for vehicles in China and the broader Asian region.
- ◆ Vertical integration strategy increases ability to capture downstream premium for differentiated lithium products.
- ◆ Potential production at Jiangsu facility of higher-grade (99.9% and 99.99%) lithium carbonate to capture associated pricing premium as the market evolves.
- ◆ Potential for lithium ion batteries to store alternative sources of energy such as solar power.

Weaknesses

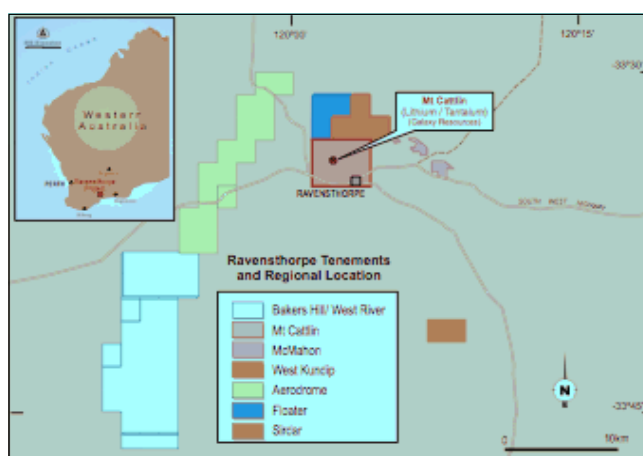
- ◆ Relatively short history of operations.
- ◆ Jiangsu lithium carbonate facility completion date originally set for 4Q10 was recently revised by management to 2Q11 due to the addition of a further purification step in the production process relating to the higher-grade lithium carbonate.
- ◆ Competition from a concentrated group of larger existing lithium producers in both brine and hard rock sourced deposits.
- ◆ Lack of diversification given single metal focus and inherent commodity price volatility.
- ◆ Negative cash flow to date.
- ◆ Lack of transparency inherent in the pricing of lithium, which is subject to individual agreement negotiations.
- ◆ Potential Hong Kong listing possibly dilutes existing shareholders holdings and adds to compliance requirements given the two sets of accounting standards.

Threats

- ◆ The company's downstream operations in Jiangsu Province, China, expose investors to some degree of country risk. That said, China's current sovereign rating by The Economist Intelligence Unit (EIU) stands at BBB, which is on par with Australia.
- ◆ Any further delays in completion of Jiangsu facility will negatively impact downstream production and sales of lithium carbonate, a key value driver for the company.
- ◆ Operating costs of extracting spodumene exceed original forecasts given low head grade when compared to major competitor Talison.
- ◆ Lithium prices remain flat or decline given weak global economic environment and company's price taking position.
- ◆ Emergence of alternative energy sources and new technologies.

Company Overview

GXY is an emerging mining and chemical company, based in Perth WA, currently focused on the exploration and production of lithium and a tantalite by-product. The company holds an interest in several projects in Western Australia with the most advanced being the Mt Cattlin lithium/tantalum project in Ravensthorpe, Western Australia; and a downstream processing plant in Jiangsu Province, China, which is currently under construction and due for completion in 2Q11. In addition to lithium, the company's other exploration projects cover a range of commodities, including copper, zinc, gold, iron ore, manganese, talc, rare earths, and uranium. The company listed on the ASX in 2007.



Company Project Location

The Mt Cattlin lithium tantalum project, which contains the majority of the spodumene ($\text{LiAlSi}_2\text{O}_6$) resource identified to date, is a hard rock lithium mine and processing facility located approximately 2 km north of the town of Ravensthorpe in WA. Spodumene is a pyroxene mineral consisting of lithium aluminium inosilicate, $\text{LiAl}(\text{SiO}_3)_2$, found in pegmatite ore which is open-pit mined and processed using gravity separation techniques to produce a concentrate containing approximately 6% lithium oxide. On January 20, 2010, GXY reported the following ore reserves and ore resources in accordance with the JORC (Joint Ore Reserves Committee) Code and guidelines.

Ore Resource

Category	Tonnes	Ta2O5 ppm	Li2O%
Inferred	3,573,757	146	1
Indicated	9,628,958	171	1.09
Measured	2,672,447	150	1.17
Total	15,875,162	162	1.08

Ore Reserves

Category	Tonnes	Ta2O5 ppm	Li2O%
Proved	2683000	135	1.08
Probable	8684000	151	1.04
Total	11,367,000	147	1.05

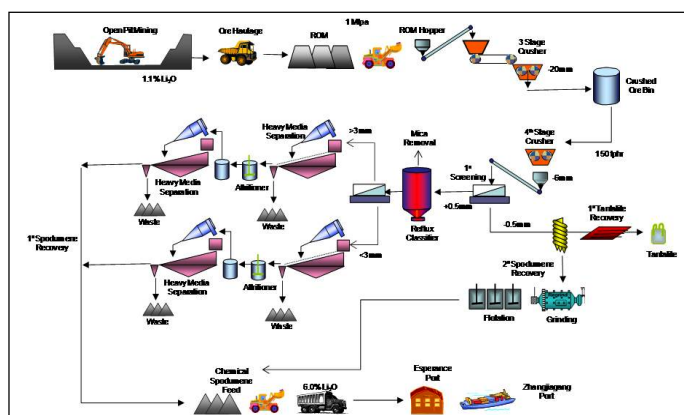
Operations

During 3Q10 GXY commenced production of spodumene concentrate at Mt Cattlin. According to management, ROM stripping ratio will be approximately 2.8:1 and processing of the ore once at steady state will be at a rate of 1 million tons per annum (tpa) at an average grade of 1.1% Li_2O to produce approximately 137,000 tpa of spodumene concentrate at 6.0% Li_2O and 56,000 lbs pa of tantalite contained concentrate. The spodumene concentrate will subsequently be transported to Esperance for shipment to China. Tantalite concentrate, essentially a by-product, on the other hand will be transported to Perth for packaging in 200 litre drums and then shipped from Fremantle to potential customers. We note, Talison Minerals (Western Australia) currently holds first right of refusal to approximately the first 4 years of tantalite production by GXY.

In Jiangsu Province, China, the spodumene concentrate will be converted to lithium carbonate, using a conventional bicarbonate purification process, at the Company's lithium carbonate plant, which is due for completion by 2Q11. As an interim measure, GXY has secured the sale of its first two shipments of spodumene concentrate. Once operational, the chemical facility will have the capacity to produce a total of 17,000 tonnes per annum (tpa) of battery grade lithium carbonate (commencing with mostly 99.5% grade product). We note, given that the current global demand for lithium carbonate equivalent is approximately 110,000 tpa (*Roskill Information Services: The Economics of Lithium*), GXY has the potential of becoming a significant global lithium carbonate producer provided production targets are met.

Furthermore, management believes the demand for higher purity lithium carbonate will increase as the market for electric vehicles evolves and plans to incorporate an additional bicarbonate purification step, which, once the plant is commissioned, will facilitate the production of both 99.9% and 99.99% grade product.

Flow Diagram - Mine & Concentrator



Products

In 3Q10, GXY launched two high-grade lithium carbonate products tailored specifically for lithium batteries used in the production of electric vehicles. These new categories will be branded 'EV Grade' (99.9% lithium carbonate) and 'EV Plus Grade' (99.99% lithium carbonate) representing a key niche product offering for the electric vehicle market.

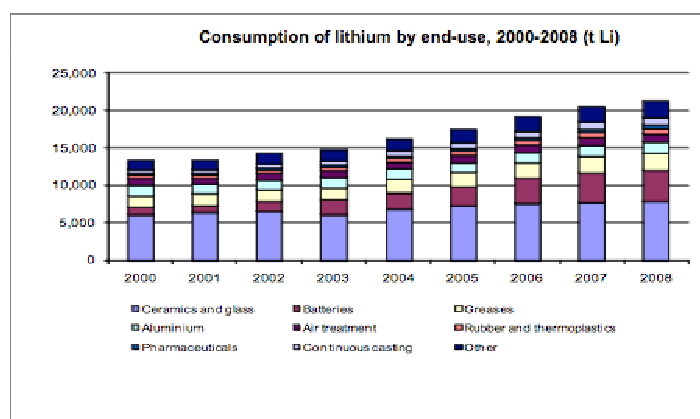
Industry Outlook

The market dynamics for lithium are positive. Lithium demand has grown steadily over the past decade driven largely by the use of lithium in batteries for mobile phones and computers; and in the manufacture of fine chemicals, rubbers, plastics, glass, ceramics and lubricating grease.

That trend is expected to gather momentum significantly in the near term as the move towards alternative energy sources and technological advances increases the consumption of lithium batteries used in the manufacture of hybrid and electric vehicles, with China, India, Japan and South Korea. That said, forecast growth estimates as high as 15% pa of lithium consumption in the battery market (*Roskill Information Services: The Economics of Lithium*) have been cited assuming the push towards plug-in hybrid and electric vehicles by major automotive manufacturers such as Chevrolet, Hyundai, Mercedes and Mitsubishi gains traction as expected. Consensus growth of overall lithium consumption overall is currently estimated at 5.8% pa, notwithstanding further economic slowdowns over the medium term, which equates to an increase in annual global consumption by end users of approximately 7,000t by 2013.

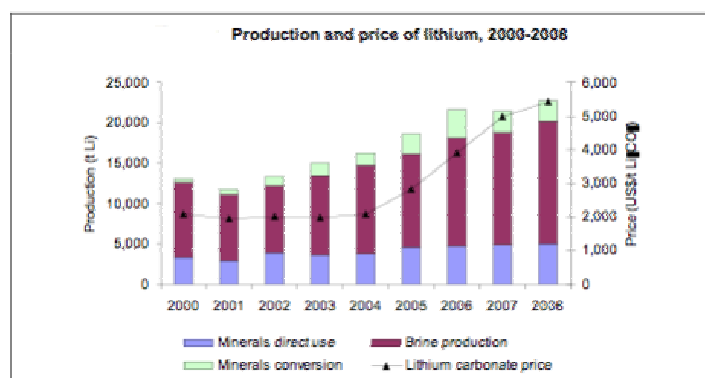
Supply

The two major sources of the world's current supply of lithium are: extraction from brine pools and brine deposits; and, separation from other elements found in igneous minerals such as granites. Brines currently account for most of the world's supply with Argentina and Chile representing 90% of world lithium output derived from brines (2008).



Source: Roskill

Hard rock lithium sources such as granites (granitic pegmatite providing the greatest concentration of spodumene) account for the remainder of supply, with Australia providing 70% of world production of lithium minerals, followed by China and Zimbabwe, which contribute an additional 20%. The two major sites in Australia of hard rock lithium mineral deposits are found at Greenbushes and Cattlin Creek in Western Australia.



Source: Roskill

Current global production of lithium is highly concentrated, both geographically and in terms of corporate ownership with more than 85% of world production generated by four relatively diversified listed producers:

Company	Lithium interests	Ticker	Mkt Cap	Share
Sociedad de Quimica Minera de Chile S.A.	Chile	NYSE: SQM	US\$14B	26%
Talison Lithium Ltd *(merged with Salares)	Australia	TSX: TLH	C\$533M	23%
Rockwood Holdings Inc.	USA	NYSE: ROC	US\$3B	22%
FMC Corp.	Argentina	NYSE: FMC	US\$5B	14%

Unlike Australian-based Talison Lithium, which owns the largest pegmatite source of Lithium in Australia and recently acquired TSX Venture Exchange-listed Salares and its brine based operations in Chile, all of the major global producers are not exclusively focused on lithium production per se.

Establishing a benchmark for lithium prices remains problematic. Spodumene is not a publicly traded commodity and therefore limited publicly available reference prices are available.

Industry position

Galaxy entered the lithium market with the acquisition of the Mt Cattlin tenements from the receivers of Sons of Gwalia in 2006, and is one of only two other significant lithium projects in Australia after Talison Lithium. The other player, Reed Resources (ASX: RDR), has yet to commence lithium production.

Galaxy is pursuing a vertical integration strategy aimed at leveraging a potentially steady supply of raw materials (spodumene concentrate) with an offshore downstream processing facility to produce battery-grade lithium carbonate. It is anticipated that the demand for a clean energy source will continue to grow and fuel the uptake of electric vehicles and growth of the alternative energy storage market in China. The lithium carbonate will be used in electric vehicles manufactured in China and also supplied to consumer electronics manufacturers in the broader Asian region.

Financial position

The company has \$96.9M of cash on the balance sheet versus total debt of \$114M, as at September 30, 2010. With the commencement of mining at Mt Cattlin and the sale of lithium oxide under the current Off Take agreements, we forecast cash from operations and net profit for FY10 of \$10.2M and \$5.9M (or FY10 EPS of \$0.03) respectively.

Notwithstanding further delays in the commencement of operations at the downstream processing facility in Jiangsu Province, China, and given near term earnings certainty resulting from current agreements and stated working capital requirements by management, coupled with the stronger balance sheet following the recent capital raising of A\$91.5M, we do not anticipate solvency problems in the medium term.

Major Shareholders (as at Dec 3, 2010)

Great Resources	19.9%
National Nominees Ltd	5.4%
HSBC Custody Nominees (Aust) Ltd	4.5%
Ademsa Pty Ltd	4.0%
Super Raya International Ltd	3.5%
HSBC Custody Nominees (Aust) Ltd- GSCO ECA	2.4%
Citicorp Nominees	2.4%
JP Morgan Nominees Pty Ltd	2.1%
Equity Trustees Ltd	1.0%
Mr Robert James Wanless	0.7%
Mineral Administration Services	0.7%
Romadak Pty Ltd	0.7%

Risks

- ◆ **Competition.** Although GXY is only one of only three significant lithium projects in Australia, globally competition from both brine and mineral suppliers is significant (see appendix) Historically, brine producers have had a competitive cost advantage over hard rock producers given the relatively lower operating costs involved in recovering lithium from brine solutions.
- ◆ **Commodity price risk.** The recent weakness in the global economic environment highlighted the pricing risk inherent in less commonly traded commodities, such as lithium, in times of financial uncertainty. We note that this risk is largely mitigated by the Off-take agreements secured with Mistubishi and 13 other Chinese Cathode manufacturers.
- ◆ **Currency risk.** Global lithium carbonate sales denominated in USD will be subject to FX exchange risk.
- ◆ **Execution risk.** Delays or disruptions across any part of the value chain can impact on ultimate cash flow generation and share price. Delays in the completion of the Jiangsu facility, in particular, represent a key risk for the company.
- ◆ **Country risk.** Galaxy's downstream operations in Jiangsu Province, China, expose investors to country risk. That said, China's current sovereign rating by The Economist Intelligence Unit (EIU) stands at *BBB*, which is on par with Australia.
- ◆ **Small-cap risk.** Investors should consider risks common to small-cap stock investments, including: share price volatility, inordinate sensitivity to news flow, and liquidity.
- ◆ **Dual listing on Hong Kong Stock Exchange** may potentially add to short-term share price volatility.

Valuation

Our valuation of GXY incorporates a Discounted Cash Flow (DCF) under 3 different scenarios, using a weighted average cost of capital (WACC) of 10.0% to derive a fair value target range of between \$1.48 and \$1.93.

Our low end case assumes the Mt Cattlin/Jiansgu project has an 11-year mine life, using management's forecast production volumes and our conservative use of reported 2P (Proved and Probable) reserves on an un-risked basis. In this scenario we have not attributed any value in our calculation to exploration assets or current 'inferred' resources. Our second case extends the mine life to 16 years by incorporating total resources (Measured, Indicated, Inferred) as reported by the company in January 2010, and an increase of 1% per annum, year on year, in lithium prices, all else equal. While the high end of our valuation range is derived using a mine life of 16 years and a modest increase of 2% per annum, year on year, in lithium prices achieved, all else equal.

DCF valuation inputs

Risk Free Rate	4.5%
Risk Premium	6.0%
Beta	1.7
Cost of equity	14.7%
Cost of debt	SIBOR + 4.5%
Target debt/equity ratio	43/57
Tax Rate	30%
WACC	10.0%

Key Model Assumptions

ROM production rate 1mtpa by 2011
Head Grade (%Li ₂ O) of 1.1
Recovery rate (Li ₂ O) of 80%
Head Grade (Tantalite) of 135 ppm
Recovery rate (Li ₂ O) of 65%
State royalty of 5% of revenue
Capex 2010 ~ A\$101M
Capex 2011 ~ A\$51M
Depreciation method – straight line
No dividend payment
A\$/US\$ rate to revert to long term average (10yr)

Scenario parameters

	Life of Mine	Lithium Carbonate (US\$/t)	YoY price increase	WACC	Valuation per share
Low	11	6,000	2%	10%	\$1.48
Base	16	6,000	1%	10%	\$1.69
High	16	6,000	2%	10%	\$1.93

	5,500	6,000	6,500	7,000
10%	\$1.20	\$1.48	\$1.76	\$2.05
11%	\$1.10	\$1.37	\$1.63	\$1.90
12%	\$1.01	\$1.26	\$1.51	\$1.76
13%	\$0.92	\$1.16	\$1.40	\$1.64
14%	\$0.84	\$1.07	\$1.29	\$1.52
15%	\$0.76	\$0.98	\$1.20	\$1.41

Key model sensitivities:

- ◆ **Commodity prices.** The price of lithium is a key driver of value for GXY and highly sensitive to the still evolving market dynamics of the most important medium term driver of end-user demand, namely the electric vehicle market in China. Notwithstanding the high concentration of several lithium producers globally, ultimate supply and demand will be a function of both alternative fuel economics and politics. That said, China's stated intention to reduce dependence on oil and curb urban pollution augurs well for stable pricing over the longer term.
- ◆ **Discount rates.** The nominal discount rate adopted for the purpose of this valuation is derived using a weighted average cost of capital (WACC), incorporating a CAPM derived cost of equity of 14.7%, and applied to our estimates of future free cash flows for the period of the economic life of the mine. We note, that WACC used in our valuation methodology is low relative to most junior explorers and largely reflects the company's lower cost of debt through the China Development Bank.
- ◆ **Economic life of mine.** Our low end case scenario assumes an economic mine life of 11 years based on forecast production volumes and our conservative use of reported 2P (Proved and Probable) reserves on an un-risked basis. Management's current 16-year mine life estimate assumes total mineral resource will be converted to 2P categories under JORC guidelines.
- ◆ **Completion of Jiansgu facility.** All three scenarios assume the lithium carbonate plant commences operations in 2Q11. That said, management revised the original opening date of the facility from 4Q10 to 2Q11, due to the addition of a further purification step.
- ◆ **Exchange rates.** Despite the current strength of the AUD we have used a rate closer to the long-term (10 yr) average of AUD per USD of 0.73.

Lithium/Tantalum Project (High end scenario)

Galaxy Resources	YE: December	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025
Lithium																	
ROM Production (mtpa)		0.2	1.0	1	1	1	1	1	1	1	1	1	1	1	1	1	1
Head grade (%Li2O)		1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1
Concentrate Grade required (6% Li2O)		6	6	6	6	6	6	6	6	6	6	6	6	6	6	6	6
Spodumene Concentrate equivalent @ 6% Lithium Concentrate (mtpa)		0.021	0.138	0.138	0.138	0.138	0.138	0.138	0.138	0.138	0.138	0.138	0.138	0.138	0.14	0.14	0.14
Tantalite																	
Ta2O5 Head Grade (Pure - ppm)		135	135	135	135	135	135	135	135	135	135	135	135	135	135	135	135
Recovery (%)		65%	65%	65%	65%	65%	65%	65%	65%	65%	65%	65%	65%	65%	65%	65%	65%
Conc. Grade (@ 25% Ta2O5)		25	25	25	25	25	25	25	25	25	25	25	25	25	25	25	25
Tantalum Conc Production (tpa @ 25% grade)		54	351	351	351	351	351	351	351	351	351	351	351	351	351	351	351
Tantalum Production (Pure - thous.lb Ta2O5 pa)		30	193	193	193	193	193	193	193	193	193	193	193	193	193	193	193
Lithium Carbonate																	
Li2CO3 per ton of Feed	0.12	0.01	0.02	0.02	0.02	0.02	0.02	0.02	0.02	0.02	0.02	0.02	0.02	0.02	0.02	0.02	0.02
Spodumene/Lithium Carbonate Revenue (US\$m)		51.6	143.0	145.9	148.8	151.8	154.8	157.9	161.1	164.3	167.6	170.9	174.4	177.9	181.4	185.0	188.7
Tantalite Revenue (US\$m)		3.4	22.5	22.5	22.5	22.5	22.5	22.5	22.5	22.5	22.5	22.5	22.5	22.5	22.5	22.5	22.5
Total Revenue (A\$m)		55.0	165.6	168.4	171.3	174.3	177.4	180.5	183.6	186.8	190.1	193.5	196.9	200.4	203.9	207.6	211.3
Operating Costs A\$m																	
Operating Costs		19.8	54.6	54.6	54.6	54.6	54.6	54.6	54.6	54.6	54.6	54.6	54.6	54.6	54.6	54.6	54.6
WA State Royalty (5%)		2.8	8.3	8.4	8.6	8.7	8.9	9.0	9.2	9.3	9.5	9.7	9.8	10.0	10.2	10.4	10.6
Corporate Overheads		10.0	10.0	10.0	10.0	10.0	10.0	10.0	10.0	10.0	10.0	10.0	10.0	10.0	10.0	10.0	10.0
	Total cost	32.5	72.9	73.1	73.2	73.4	73.5	73.7	73.8	74.0	74.1	74.3	74.5	74.7	74.8	75.0	75.2
EBITDA		22.5	92.7	95.4	98.1	101.0	103.9	106.8	109.8	112.9	116.0	119.2	122.4	125.7	129.1	132.6	136.1
Depreciation		6.3	9.7	9.7	9.7	9.7	9.7	9.7	9.7	9.7	9.7	9.7	9.7	9.7	9.7	9.7	9.7
Depletion																	
EBIT		16.2	83.0	85.7	88.4	91.3	94.2	97.1	100.1	103.2	106.3	109.5	112.7	116.0	119.4	122.9	126.4
Taxable income		10.5	79.8	83.0	86.4	90.3	93.2	96.1	99.1	102.2	105.3	108.5	111.7	115.0	118.4	121.9	125.4
Income Tax @ 30%	30%	3.2	23.9	24.9	25.9	27.1	27.9	28.8	29.7	30.6	31.6	32.5	33.5	34.5	35.5	36.6	37.6
Net Profit		7.4	55.8	58.1	60.5	63.2	65.2	67.3	69.4	71.5	73.7	75.9	78.2	80.5	82.9	85.3	87.8
Earnings after Tax		7.4	55.8	58.1	60.5	63.2	65.2	67.3	69.4	71.5	73.7	75.9	78.2	80.5	82.9	85.3	87.8
Free Cash Flow		-85.6	13.0	66.1	68.3	70.7	72.7	74.8	76.9	79.0	81.2	83.4	85.7	88.0	90.4	92.8	90.3
Net Present Value @ 10% Nominal		400.9															
Value of Net Assets		366.9															
No of Shares		190.6															
Value per Share		1.93															

Peer Comparisons

GXY is unique in the Australian context given its vertical integration strategy and downstream offshore processing facility currently under construction in China. As one of only two ASX listed miners currently focused primarily on hard rock lithium deposits in Australia, and the only one resembling a pure play, defining an appropriate peer group is problematic. That said, we have included a table below of key global lithium producers to provide some perspective of where GXY is currently positioned according to enterprise value.

Peer comparison*

Company	Ticker	Share price	Shares on issue	Market Cap	Net Cash	EV
Sociedad de Quimica Minera de Chile S.A.	NYSE:SQM	50.77	263	13363	-657	14020
FMC Corp.	NYSE:FMC	77.23	73	5602	-368	5970
Rockwood Holdings Inc.	NYSE:ROC	37.50	76	2837	-1874	4710
Talison Lithium Limited	TSX:TLH	5.70	94	533	8	525
Galaxy Resources	ASX:GXY	1.47	191	281	18	263
Orocobre	ASX:ORE	2.78	91	253	25	228
Canada Lithium Corp.	TSX V:CLQ	0.92	150	138	14	124
Reed Resources	ASX:RDR	0.55	192	106	17	89
Western Lithium	TSX V:WLC	1.09	82.8	90	18	73
Lithium One	TSX V:LI	1.18	47	56	5	51
First Lithium	TSX V:MCI	0.09	51	5	1	4

* Denominated in local currencies

Recent News

- ◆ **On November 24, 2010**, GXY announced the signing of a non-binding Letter of Intent (LOI) for the site of the company's proposed lithium ion battery project in China. The site is located close to the company's Jiangsu lithium carbonate project.
- ◆ **On November 8, 2010**, GXY announced it had finalised a capital raising of A\$91.5M comprising a convertible bond issue of A\$61.5M (increased from A\$30M previously announced on October 4, 2010) and an equity placement of A\$30M. Key strategic investors include the Fengli Group (Hong Kong), a major shareholder of Fortescue Metals Group in Australia and one of the major shareholders in Jiangsu Bank; and the private investment company of Mr Li Shu Fu, the founder and major shareholder of Geely Automobile Holdings in China. Geely is a Hong Kong listed company principally engaged in the manufacture and sales of automobiles in China. According to management, the proceeds will be used to fund the completion of construction and ramp-up of its Mt Cattlin and Jiangsu projects, as well as for working capital and the potential acquisition of other lithium-related projects.
- ◆ **On November 4, 2010**, GXY announced it had applied for a dual listing of its shares on the Stock Exchange of Hong Kong (SEHK). The company has submitted its Form A1 listing application, and subject to SEHK approval, anticipates a listing in the first quarter of 2011. The company also announced it was evaluating the potential to construct a manufacturing plant to produce lithium ion batteries for E-Bikes.
- ◆ **On October 5, 2010**, GXY announced commencement of lithium concentrate (spodumene) production at Mt Cattlin. Managing Director, Mr Iggy Tan said Galaxy expects to export its first shipment of spodumene product to China in November 2010.
- ◆ **On October 4, 2010**, GXY announced it had agreed in principle to issue A\$30M in a convertible note to a strategic China based investor. Proceeds of the issue will be used for additional working capital and the ramp up of its Mt Cattlin and Jiangsu projects.
- ◆ **On September 22, 2010**, GXY announced it had received the full US\$105M from the syndicate banks, China Development Bank (CDB) and Austrian bank, Raiffeisen Zentralbank Osterreich AG (RZB), with funds to be used to continue the construction of both the Mt Cattlin and Jiangsu projects and repay any outstanding bridging loans.
- ◆ **On September 9, 2010**, GXY launched two high-grade lithium carbonate products tailored specifically for lithium batteries to be used in the production of electric vehicles (EVs). These new categories will be branded 'EV Grade' (99.9% lithium carbonate) and 'EV Plus Grade' (99.99% lithium carbonate) representing a key niche product offering for the electric vehicle market.
- ◆ **On April 27, 2010**, GXY finalized the issue of 31,000,000 shares to Creat Resources Holdings Limited (CRHL) in April 2010 raising A\$27.28 million. CRHL currently owns 19.9% of the Company

Investment case.

Commencement of mining at Mt Cattlin heralds an important phase in the company's development, which will eventually complement its offshore downstream lithium carbonate chemical plant, currently under construction in Jiangsu Province, China. We believe GXY is well positioned to extract synergy gains from its vertical integration strategy and capitalize on the rising demand for lithium carbonate, as the trend towards lithium battery power gathers momentum.

We initiate coverage of Galaxy Resources Limited (ASX: GXY) with a fair value range of between \$1.48 and \$1.93.

Appendix: Global Lithium Players

Resource Companies	Country	Resource	Deposit Name
Lithium Americas Corporation	Argentina	Brine	Salar de Cauchari, Olaroz, Incahuasi and others
Orocobre	Argentina	Brine	Salar de Olaroz, Salar de Salinas Grandes, Cauchari, Guyatayoc and others
The Sientient Group	Argentina	Brine	Salar de Rincon
Marifil Mines Ltd	Argentina	Brines	Salar de Antofalla and Salar de Ratones
Galaxy Resources	Australia	Minerals	Mt Cattlin
Reed Resources	Australia	Minerals	Mount Marion
Comibol	Bolivia	Brine	Salar de Uyuni
New World Resources	Bolivia	Brine	Salar de Pastos Grandes
Rock Tech Lithium	Canada	Minerals	Georgia Lake, James Bay
Mineral Hill Industries Ltd	Canada	Minerals	Chubb, International, Athona
Canada Lithium Corporation	Canada	Minerals	Quebec Lithium Project
North Arrow Minerals Inc	Canada	Minerals	Big Bird pegmatite
Nemaska Exploration	Canada	Minerals	Lac des Montagnes
Sirios Resources	Canada	Minerals	Pontax Project
Petro Horizon Energy Corp	Canada	Minerals	Brzail Lake Property
Ultra Lithium	Canada	Minerals, brines	Berland river, Zigzag lake, South Smoke Valley
International Lithium	Canada - USA - Argentina - Ireland	Minerals - Brines	Forgan and Niemi Lake - Fish lake Valley- Mariana
First Lithium Resources	Canada, Alberta	Basinal Brine and Minerals	Valley View (Alberta) and Godslith (Manitoba)
Channel resources	Canada, Alberta	Minerals	Fox Creek Lithium Project
Lithium One	Canada, Argentina	Minerals, Brines	Cyr Property, Sal de vida
Salares Lithium Inc.	Chile	Brine	Salar de Piedra Parada, Grande, Aguilar, Agua Amarga, La Isla, Las Parinas and Maricunga
Pan American Lithium	Chile	Brines	Laguna Verde, Laguna Brava, Rio Salado y Rio Pedernales and others
Lorniko	Chile, USA	Brine	Salar de Aguas Calientes, Clayton Valley
Citic Lithium	China	Brine	West Tajjinair Salt Lake (Xitai)
Zhabuye Lithium	China	Brine	Zhabuye Salt Lake
Sterling Group Ventures	China	Brine	Dangxiongcuo (DXC)
Western Mining Group	China	Brine	East Tajjinair Salt Lake (Dongtai)
Sichuan Ni&Co	China	Minerals	Maerkang Mines
Sichuan Jinchuan	China	Minerals	Jinchuan Mine
China Lithium Products Technology	China	Minerals	Severla Mines in Sichuan
Jiangxi Ningdu Taiyu	China	Minerals	Ningdu, Jiangxi
Sichuan Dexin Mining Resources Ltd	China	Minerals	Lijiagou Lithium Mine
China Lithium Products Technology Co., Ltd	China	Minerals	
Keliber Resources	Finland	Minerals	Länttä Spodumene Pegmatite
Pacific Wildcat Resources Corp	Mozambique	Minerals	Muiane Project
Rio Tinto	Serbia	Minerals	Jadar Lithium Project
Mesa Uranium	USA	Basinal Brine	Green Energy Lithium Project
Simbol Mining	USA	Brines	brines and effluent
American Lithium	USA	Brines	Montezuma Valley
Amerpro Resources	USA	Brines	Smokey Valley in Esmeralda County
Western Lithium Corporation	USA	Minerals	Kings Valley Project
Rodinia Minerals	USA, Argentina	Brines	Clayton Valley, Salinas Grandes
Electric Metals	USA, Argentina	Brines	Big Smokey Valley, Salar Arizaro, Salar Rio Grande
AmeriLithium	USA, Canada Australia	Brines	Paymaster Canyon, Leduc Formation

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