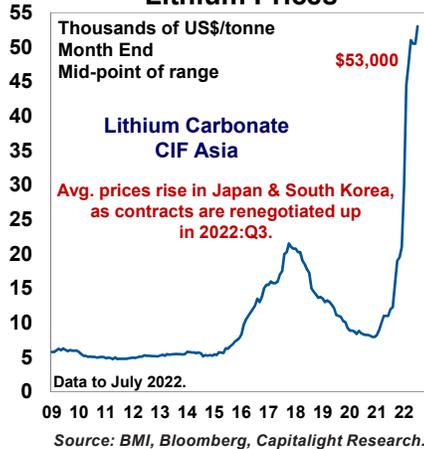


## Lithium Prices



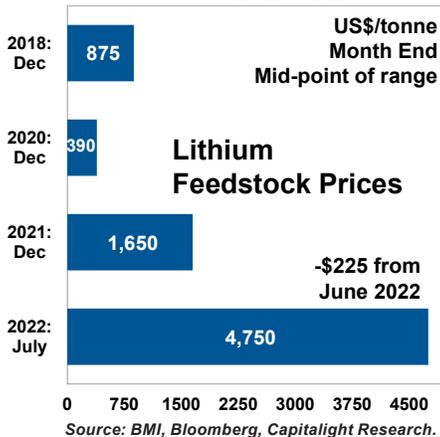
- Canada's 'critical mineral' & auto industries – from mining-to-cathode materials-to-EV manufacturing – are big winners from the U.S. 'Inflation Reduction Act' (IRA).
- The IRA represents largest investment in 'clean energy' in U.S. history.
- China's exports of 'rare earth permanent magnets' remain strong, though domestic orders have softened.

## U.S. 'Inflation Reduction Act': The Big Picture

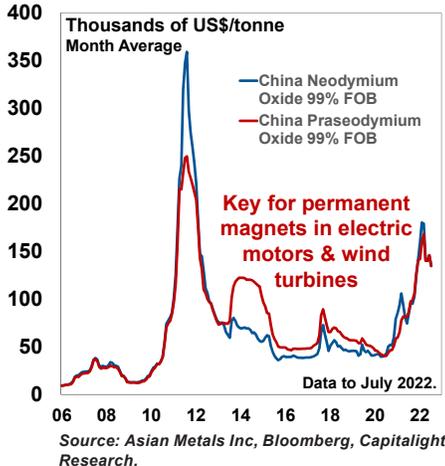
This landmark bill – a package of climate change, health care and deficit reduction measures – was passed by the U.S. Senate in a 50-50 vote by Democrats and Republicans, with the tie-breaking vote cast by Vice-President Kamala Harris on August 7, under 'budget reconciliation' rules. The Bill was subsequently passed by the House of Representatives and will now proceed to President Biden for signature – likely by mid-August. The bill is a scaled-back version of the 'Build Back Better Act' which failed to pass.

The main elements of the IRA include around \$300 bn of tax credits, grants & loan guarantees to incent the transition to

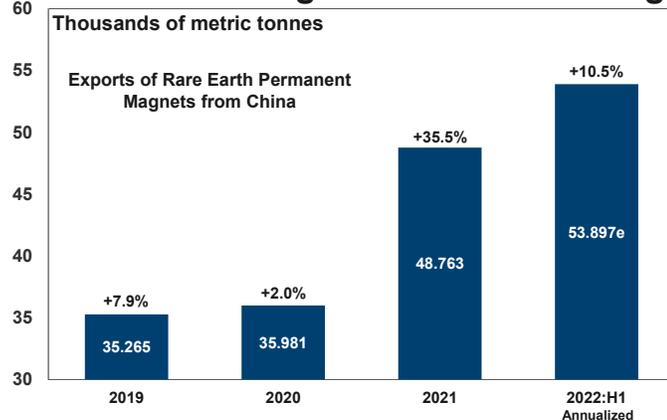
## Spodumene Concentrates 6% FOB Australia



## Rare Earth Prices



## Overseas Demand for China's Permanent Magnets Remains Strong



China's exports totaled 26,948 thousand tonnes in 2022:H1 (26,948 x 2 = 53,897 annualized). Actual exports for 2022 as a whole are likely to be higher. In June 2022, the top three export destinations were: Germany (15% of the total), South Korea (15%) and the United States (13%) = 43% of total exports.

Source: SMM, China Customs, Capitalight Research.

'clean energy'; changes to Medicare, capping annual drug costs for recipients & allowing the negotiation of pharmaceutical prices with drug makers; and tax changes to reduce the deficit (introduction of a new 15% minimum tax on corporate financial income, affecting corporations with more than \$1bn in annual income, and a 1% excise tax on corporate stock repurchases). Democrats expect the tax provisions to lower the federal deficit by \$300 bn over ten years, an objective of Senator Manchin (Democrat from West Virginia), whose support was needed to pass the Act. Deficit reduction should go some way towards mitigating inflation, though initial analysis by the Congressional Budget Office indicates little impact in 2022 (between a 0.1% decline and a 0.1% increase).

Rhodium Group estimates that the Act will contribute to a 40% reduction in U.S. net GHG emissions from 2005 levels by 2030, (moving the U.S. closer to meeting its 50-52% commitment under the Paris Accord). Under current policy, the GHG reduction would have been 30%.

The Act uses tax cuts & incentives to spur the transition to clean energy rather than 'carbon taxes' or a 'cap-and-trade system' (both of which are political non-starters in the United States). This is an important distinction compared with other countries. Senator Manchin has also made minimum oil & gas lease sales (onshore and offshore) a prerequisite for issuing rights-of-way for wind & solar development on federal lands and leases for offshore wind. This reflects Mr. Manchin's interest in 'energy security' and the recent negative experience in Germany, where over-reliance on imported oil & gas from Russia and the ill-advised closure of nuclear power plants have become quite a challenge.

### **Changes to U.S. Tax Credit for EV Sales Are a 'Big Win' For Canada**

The IRA has introduced changes to the tax credit for electric vehicle purchases, which will greatly benefit the Canadian mining & battery

sectors over the next ten years (the term of the credit). While it will take time for noticeable benefits to emerge, the provisions will likely spur stepped-up investor interest in the Canadian mining, processing & auto sectors almost immediately (from foreign mining companies & private equity).

Under the Act, the maximum tax credit on the purchase of qualified new 'clean energy' vehicles remains at \$7,500. However, in order to qualify for the credit, FINAL ASSEMBLY OF VEHICLES MUST TAKE PLACE IN NORTH AMERICA (Canada, the United States and Mexico) and the 'critical minerals' in batteries must contain a threshold value extracted or processed in a country with which the United States has a free trade agreement or recycled in North America. 'Critical minerals' from Australia and Chile will qualify, but minerals from Argentina (lithium) and Indonesia (a major source of nickel) will not. The threshold on 'critical minerals' is high – increasing from 40% for vehicles placed in service through 2023 to 80% after 2026.

The definition of 'critical minerals' used in the Act is probably similar to that set by the U.S. Geological Survey and includes nickel, lithium carbonate & hydroxide, cobalt, manganese, graphite, neodymium & praseodymium in various forms, terbium, dysprosium, tungsten, samarium and aluminium (among others). In the United States, copper is not considered to be a 'critical mineral' because of domestic supplies (though output will be insufficient to meet U.S. demand).

In the case of batteries, the percentage of the battery's components manufactured or assembled in North America must also meet threshold amounts. As in the case of 'critical minerals', these thresholds are aggressive – rising from 50% for vehicles placed in service through 2023 to 100% after 2028.

Qualifying vehicles exclude those with battery components or 'critical minerals' in the battery from a 'foreign entity of concern' (for

## Modification of Tax Credit for Electric Vehicle Purchases Inflation Reduction Act of 2022

Under current U.S. law, buyers of qualifying 'plug-in electric vehicles (EVs)' are able to claim a non-refundable tax credit of up to \$7,500. There is a cap of 200,000 on the number of vehicles which qualify for the credit from an individual OEM (e.g. Ford, Tesla...).

Current law also allows (through 2021) a tax credit of up to \$8,000 for 'fuel cell vehicles' (the base credit amount is \$4,000, with up to an additional \$4,000 based upon fuel economy). Heavier fuel cell vehicles qualify for up to a \$40,000 tax credit.

**NEW RULES:** the 'Clean Vehicle Credit' (plug-in EVs with battery capacity of at least 7 kWh & fuel cell vehicles); **QUALIFYING VEHICLES ARE THOSE WITH FINAL ASSEMBLY IN NORTH AMERICA** (Canada, the United States and Mexico).

**1) \$3,750 for any qualifying 'clean vehicle' meeting the 'CRITICAL MINERALS' requirement:** the vehicle's battery must contain a threshold percentage in value of critical minerals that were extracted or processed in a country with which the United States has a 'free trade agreement' or recycled in North America. The threshold percentage is 40% (for vehicles placed in service through 2023); increasing to 50% in 2024, 60% in 2025, 70% in 2026 and 80% after 2026.

### PLUS

**2) \$3,750 for any vehicle meeting the 'BATTERY COMPONENTS' requirement:** the percentage of the battery's components manufactured or assembled in North America must meet threshold amounts – for vehicles placed in service through 2023 the percentage is 50%; increasing to 60% for 2024 and 2025, 70% for 2026, 80% for 2027, 90% for 2028 and 100% after 2028.

Qualifying vehicles exclude those with battery components (after 2023) or critical minerals in the battery (after 2024) from a 'foreign entity of concern' (as defined in 42 U.S.C. 18741).

The current cap on tax credits involving individual OEMs is removed.

Credits are only allowed for vehicles that have a manufacturer's suggested retail price of no more than \$80,000 for vans, SUVs and Pickup trucks and \$55,000 for other vehicles. (It should be noted that the average cost of an EV often exceeds these levels.)

Higher-income taxpayers are not eligible for the tax credit: a credit is not allowed for married taxpayers with 'adjusted gross income' of more than \$300,000; \$225,000 for heads of households and \$150,000 for others.

Expiry date for Clean Vehicle Credits: December 31, 2032 (in ten years).

A new tax credit has also been created for second-hand clean (plug-in electric and fuel cell) vehicles. The credit is up to \$4,000 limited to 30% of the vehicle purchase price – available for vehicles with a sale price of below \$25,000. Other qualifications apply.

A new tax credit for qualified commercial clean vehicles has been created: credit is the lesser of 1) 15% of the vehicle's cost (30% for vehicles not powered by a gasoline or diesel internal combustion engine) or 2) the incremental cost of the vehicle relative to a comparable vehicle. Credit amounts cannot exceed \$7,500 for vehicles weighing less than 14,000 pounds or \$40,000 otherwise. Eligible vehicles have a battery capacity of not less than 15 kWh (7 kWh for vehicles weighing less than 14,000 pounds).

Source: Congressional Research Service, Capitalight Research.

vehicles placed in service after 2023 and 2024 respectively). This provision will almost certainly exclude Russia and Russian nationals. Please see the insert on page 3 for details.

### **Impact of EV Tax Credit Modifications**

Changes to the EV tax credit are obviously meant to develop a 'secure' supply chain for EVs and their batteries in the United States and trusted trading partners, as well as spurring the adoption of EVs by U.S. consumers. U.S. sales of EVs have advanced strongly this year, but are only a fraction of sales in China and the EU. However, few vehicles assembled in the United States or across North America are likely to qualify for the tax credit in 2023, in view of only limited current supplies of appropriately sourced 'critical minerals' and battery components. EV sales could actually drop once the Act comes into force. Nevertheless, over time, the content rules will help to develop 'critical minerals' & the battery sector in Canada as well as the United States.

The Canadian Government and others should be congratulated on their successful lobbying efforts for content & assembly rules in line with the terms of the 'United States-Mexico-Canada-Agreement' or USMCA. The modifications also recognize the highly integrated nature of the Canada-U.S. auto industry, since the Auto Pact of the 1960s. The 'Build Back Better Act' would have restricted part of the tax credit to U.S.-assembled vehicles and to batteries meeting U.S. content requirements; by 2027 even the base credit would have required U.S. assembly.

Auto assemblers (such as General Motors, Ford & Toyota) had hoped that specific content rules would be dropped in the IRA. However, those lobbying efforts were never going to be successful, because Senator Manchin was against providing subsidies to foreign supply chains.

Canada is very prospective for nickel and the United States is not. At least five early-stage nickel deposits are currently available for

development in Canada; the U.S. tax credit, for which Indonesian nickel does not qualify, may be another factor spurring ultimate finance for them. Comparatively low CO<sub>2</sub> emissions for Canadian nickel projects – in contrast to high emissions from Indonesian nickel – are another competitive factor in favour of Canadian mines. The nickel properties of Vale and Glencore in Canada will become even more valuable.

It should be noted that the EV tax credit provisions do not mention electric vehicle 'motors' for which permanent magnets are required. The United States currently imports a large number of permanent magnets from China. Please see the chart on the front cover and the text below.

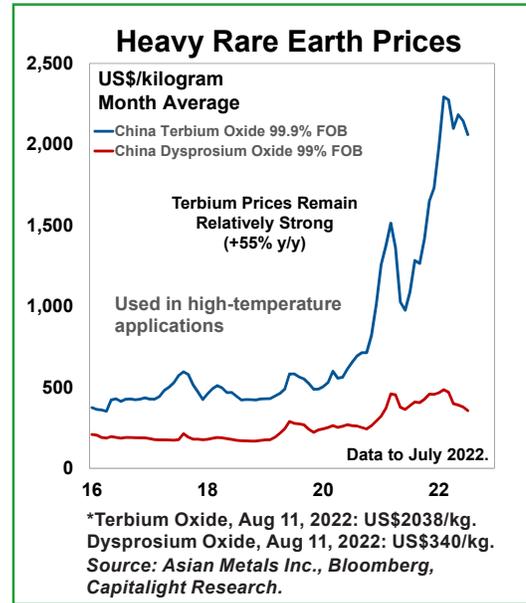
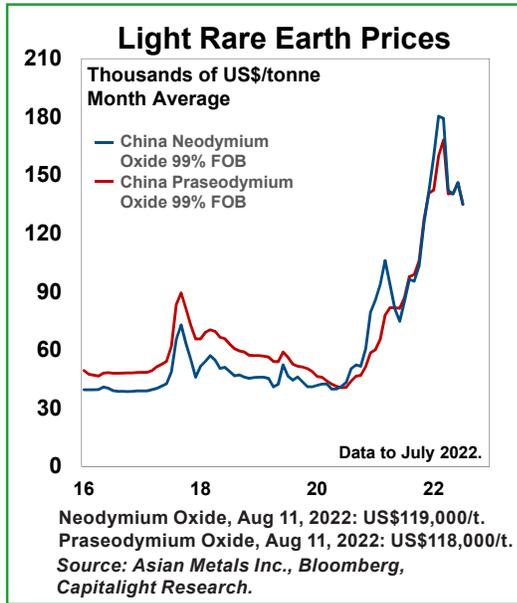
### **Other Clean Energy Initiatives**

The Act provides many tax credits for investment in and production of solar panels, wind turbines, battery cells and other energy-related plant & equipment – all of which will boost demand for 'critical minerals' and copper. These initiatives will be discussed in greater detail in the next report in September.

### **Near-term Outlook For Rare Earths**

Turning to rare earths, the medium-term outlook remains stellar for neodymium, praseodymium & terbium – the three REEs vital for the NdFeB permanent magnets typically used in electric vehicle drive and wind turbine applications. However, in recent months, there has been a noticeable decline in Chinese rare earth prices – important because China is both a major importer of mine concentrates and mixed rare earth intermediate products (including carbonates & chlorides) for 'separation' into individual rare earth oxides and further processing as well as an exporter of rare earth materials (oxides, metals & alloys), permanent magnets and final consumer products containing rare earths.

The price of 'China neodymium oxide' has dropped almost 37% from a peak of US\$190,000 per tonne in mid-February 2022 to US\$119,000

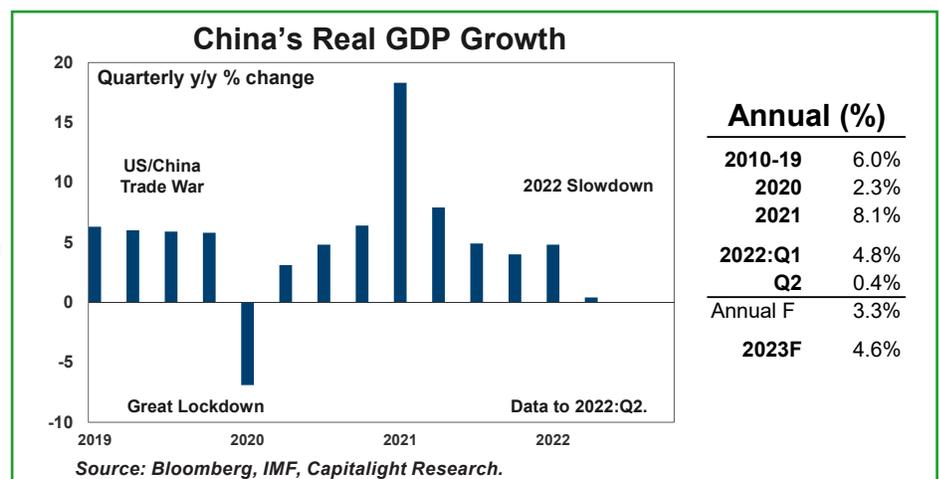


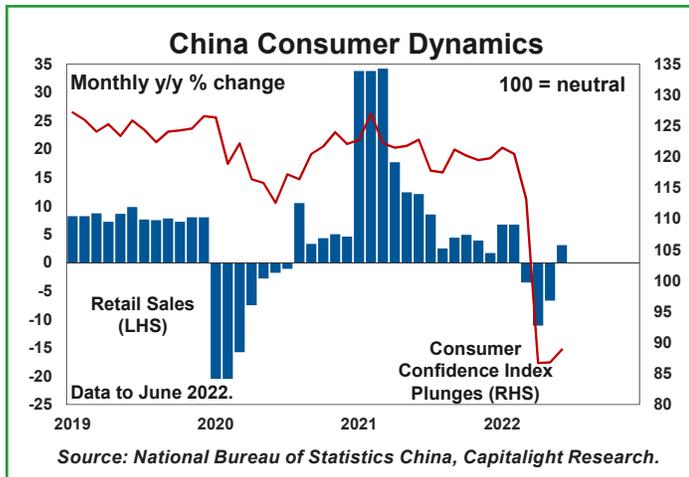
on August 11 – but remains 22.4% above a year ago. Similarly, ‘praseodymium oxide’ has retreated 31.8% from a peak of US\$173,000 in mid-February to US\$118,000 in mid-August (still 20.4% above a year earlier). Terbium oxide – a heavy rare earth in particularly tight supply – has also edged lower from a high of US\$2,370 per kg in early February 2022 to US\$2,038 in mid-August (+ 55% above a year earlier).

In March, China’s ‘Rare Earth Regulation Office’ pressed key market players to forego speculation, probably causing traders to pare inventories and precipitating the price decline. Orders from ‘magnetic material enterprises’ – linked to domestic demand for electric vehicles, wind power generation, home appliances and consumer electronics – turned soft in March, April and May – due to rigid COVID-19 ‘lockdowns’ in many Chinese cities, which prevented consumers from shopping and limited factory operations. The resulting slowdown in China’s economy – with GDP growth receding from 4.8% y/y in 2022:Q1 to a mere 0.4% in Q2 – also reflected a worsening crisis in the real estate sector, with declining residential construction

and property sales (-43% y/y in the first half of 2022) contributing to poor sales of appliances. A number of debt-laden developers have failed to complete pre-sold condominiums, leading to a spate of mortgage payment boycotts by consumers. These developments, combined with higher unemployment, contributed to a plunge in ‘consumer confidence’ to record lows (even below the low levels of early 2020, when COVID-19 first appeared).

China’s electric vehicle sales recovered strongly in June – in fact, to a new record high – contributing to a modest rebound in overall retail sales (+3.1% y/y), though ex-auto sales only advanced 1.8% y/y. EV sales – reported on August 11 – stayed near record levels at





593,000 units in July (representing a 24.5% market share). Nevertheless, orders at magnet producers remained sluggish in July and were still slow in early August. The month of August is usually seasonally quiet in China, with many factories taking vacation downtime.

The slowdown in domestic demand – noted above – has offset ongoing strength in China’s exports of permanent magnets. Exports of ‘rare earth permanent magnets’ climbed by 18.6% y/y in the first half of 2022, though exports dipped slightly in June. **The top three destinations were Germany, South Korea and the United States in June. China dominates global production of rare earth permanent magnets, with a share as high as 90%. Japan accounts for a large part of the remainder, with Hitachi Metals Group owning key patents for technology originally developed by Sumitomo Special Metals.** In 2020-21, the United States produced less than 1% of the world’s NdFeB magnets – now recognized as a key strategic vulnerability both commercially and geopolitically, given ambitious decarbonization goals.

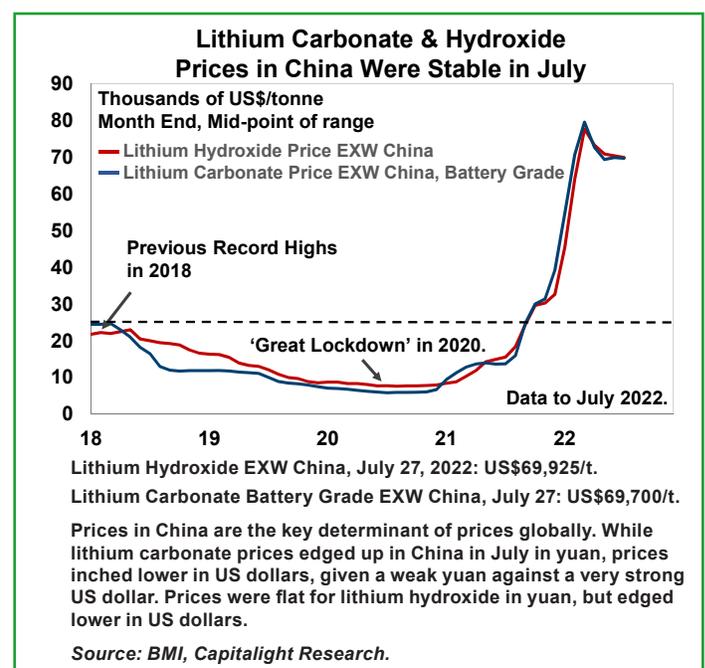
Barring a severe global recession, prospects appear good for a modest rebound in rare earth orders and prices in China in the second half of 2022 (beginning around September). Market sentiment should recover alongside economic stimulus, though China has abandoned its 5.5% GDP growth target for this year. Construction of wind turbines should pick up, after a weak first-

half 2022. Overseas demand for China’s rare earth permanent magnets should also remain strong.

### **Lithium – ‘North American Lithium’ Project makes progress in Québec**

Lithium market conditions remain steady in China. ‘Lithium carbonate (battery grade) EXW China’ prices were largely flat in July – edging up in yuan, but inching lower in US dollars, given weakness in the yuan against a very strong USD. Prices in late July were US\$69,700 per tonne and US\$69,925 around August 10 (based on BMI price assessments). As with rare earths, converters held the line on prices, following comments by market regulators in March that prices should return to more rational levels. Demand recovered in the electric vehicle sector, but was limited in consumer electronics. On a more positive note, carbonate demand got a boost as some high-nickel cathode makers shifted from NCM 811 to NCM 622 chemistries to cut costs. The technology uses less nickel and usually cheaper carbonate rather than lithium hydroxide, but has the same energy density for high-performance vehicles.

‘Lithium hydroxide EXW China’ also inched lower to US\$69,925 per tonne in late July and was little changed in mid-August.



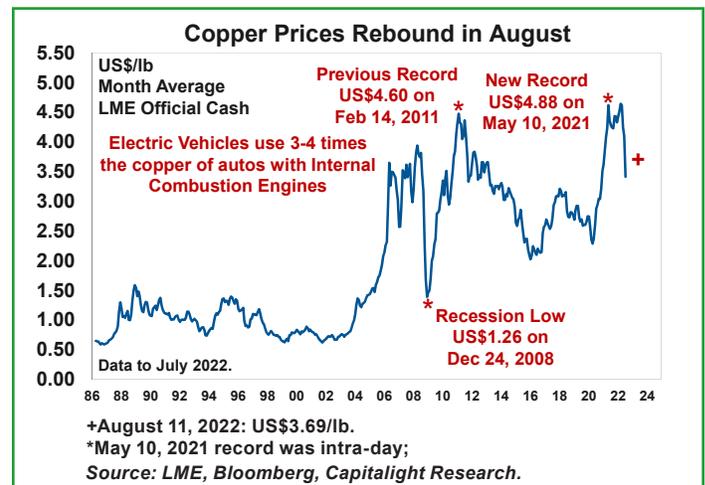
Turning to the spodumene concentrate market, prices edged down from a record US\$4,975 per tonne to US\$4,750 (6% Li<sub>2</sub>O) FOB Australia. This reflects contract re-adjustment at the start of the third quarter to somewhat lower prices in China in the second quarter. In addition, on the high end of the pricing range, a transaction settled on the 'Pilbara Minerals Battery Material Exchange' at US\$6,188 per tonne for 5,000 tonnes of SC5.5 – US\$162 lower than an identical shipment in June 2022. Based on these trends, market participants believe that lithium chemical prices in China will remain high, but largely stable in the third quarter.

Outside China, the price of lithium carbonate (CIF Asia) rose to US\$53,000 per tonne in July (a new record high), after levelling off at US\$50,500 for several months. Japan and South Korea are countries with significant battery production and electronics demand.

Turning to Canadian news, Sayona Québec – a joint venture between Australian lithium producer Sayona Mining and U.S.-based Piedmont Lithium – recently announced that it will restart operations at its 'North American Lithium' (NAL) project at La Corne, Québec (in the Abitibi region) in the first quarter of 2023. The open-pit mine will supply North America's first locally-sourced spodumene concentrates.

### **Copper & Nickel: China's State Reserve Bureau (SRB) plans to replenish inventories in 2022:H2**

LME copper prices rallied back in mid-August to US\$3.69 per pound, after falling as low as US\$3.18 on July 15. Investors reacted positively to signs that inflation is moderating, hoping that the Fed might slow its pace of monetary tightening. The U.S. Consumer Price Index showed little m/m increase in July, decelerating to 8.5% y/y after increasing 9.1% y/y in June. Lower gasoline prices largely accounted for the moderation. The U.S. Producer Price Index – a gauge of final demand wholesale prices – also fell 0.5% m/m, again due to lower energy prices



– but was still up 9.8% y/y. Despite this positive news, we still expect the Fed to implement another 50 basis point increase in the target Fed funds rate in September, after two consecutive 75 bp increases in June and July 2022.

Perhaps more importantly, investors have re-focused on tightening copper supplies in Asia and Europe. A heat wave and drought in China is leading to power cuts affecting several major Chinese smelters – owned by Jiangxi Copper Co. (China's biggest copper producer) and Tongling Nonferrous Metals Group Co. The premium on imports of grade A copper cathode, CIF Shanghai has widened slightly. High power costs in Europe – linked to the Russian conflict – have also halted production at zinc and aluminium smelters.

Turning to nickel, LME prices continued to unwind from the 'squeeze' in March, falling from



US\$11.72 per pound in June to US\$9.75 in July. However, LME nickel prices have moved back over the US\$10 level in August (US\$10.48 on August 11) with the return of some ‘risk-on’ market sentiment.

China’s State Reserve Bureau (SRB) is planning to replenish inventories of copper and nickel in the second half of 2022 – usually a sign that recent prices have been on the low side of expectations (that is, cheap). Actual inventories on the SHFE are very low – particularly for nickel – though only No.1 grade refined product is acceptable for delivery on the LME and SHFE. (The expected ramp-up of Indonesian supplies in 2022 will involve nickel pig iron, MHP and matte.)

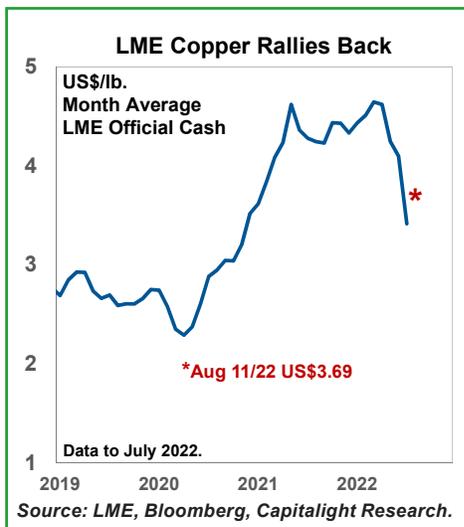
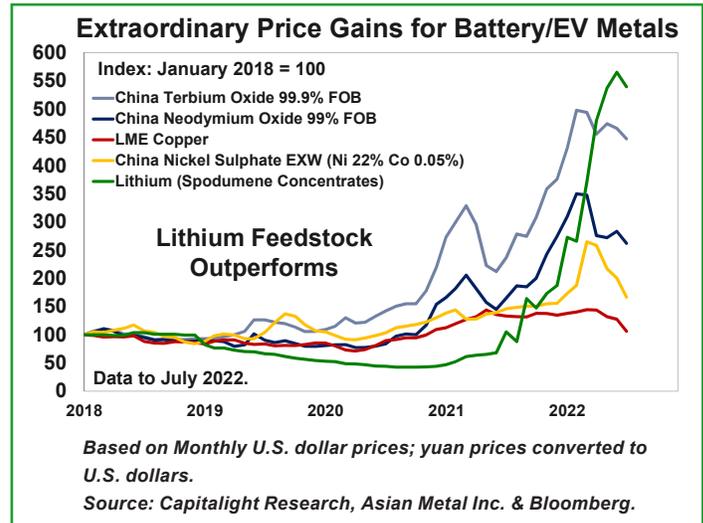


Table 1

Critical Metals - Price Trends										
	2018	2019	2020	2021				2022		Latest
	Annual	Annual	Annual	Q1	Q2	Q3	Q4	Q1	July	August 11
<b>Copper</b>										
LME Copper Official Cash Settlement <sup>1</sup> (US\$/lb)	2.96	2.72	2.80	3.85	4.40	4.25	4.40	4.53	3.42	3.69
<b>Nickel</b>										
LME Nickel Official Cash Settlement <sup>2</sup> (US\$/lb)	5.95	6.31	6.25	7.99	7.87	8.68	8.99	11.85	9.75	10.48
SHFE Nickel, Generic First Contract <sup>2</sup> (CNY/tonne)	102,916	110,746	109,054	131,120	128,570	143,708	147,198	185,946	172,624	177,720
China Nickel Sulphate EXW > 22% Ni, 0.05% Co <sup>2</sup> (CNY/tonne)	28,411	30,487	29,874	35,766	35,714	39,276	39,720	41,250	43,160	39,750
<b>Lithium</b>										
Lithium Carbonate, CIF Asia ≥ 99.2% Li <sub>2</sub> CO <sub>3</sub> <sup>3</sup> (US\$/tonne)	17,063	11,675	8,421	9,083	11,000	13,333	19,833	40,667	53,000	53,000 <i>(Data to end July)</i>
Lithium Carbonate, CIF North America ≥ 99.0% Li <sub>2</sub> CO <sub>3</sub> <sup>3</sup> (US\$/tonne)	14,833	11,215	7,746	8,083	9,750	12,375	17,000	38,333	47,500	47,500 <i>(end July)</i>
Lithium Hydroxide, FOB North America ≥ 55.0% LiOH <sup>3</sup> (US\$/tonne)	16,771	13,521	10,629	10,458	11,750	14,333	19,333	37,750	54,500	54,500 <i>(end July)</i>
Spodumene Concentrate, FOB Australia 6% Li <sub>2</sub> O, Lithium Feedstock <sup>3</sup> (US\$/tonne)	886	595	406	472	579	1,048	1,492	2,668	4,750	4,750 <i>(end July)</i>
<b>Rare Earth Elements</b>										
China Neodymium Oxide 99%, FOB <sup>4</sup> (US\$/tonne)	49,918	44,655	48,757	95,147	83,222	92,267	123,356	173,087	135,167	119,000
China Neodymium Metal 99% FOB <sup>4</sup> (US\$/kilogram)	64	57	62	116	102	115	153	210	168	150
China Praseodymium Oxide 99%, FOB <sup>4</sup> (US\$/tonne)	63,627	54,024	45,725	67,818	81,665	94,484	124,540	156,774	134,905	118,000
China Praseodymium Metal 99% FOB <sup>4</sup> (US\$/kilogram)	114	103	91	96	104	110	139	178	187	175
China Dysprosium Oxide 99%, FOB <sup>4</sup> (US\$/kilogram)	177	234	259	384	398	400	447	474	356	340
China Dysprosium Metal 99% FOB <sup>4</sup> (US\$/kilogram)	262	307	341	497	516	516	554	583	474	438
China Terbium Oxide 99.9% FOB <sup>4</sup> (US\$/kilogram)	455	503	664	1,382	1,121	1,213	1,600	2,185	2,060	2,038
China Terbium Metal 99% FOB <sup>4</sup> (US\$/kilogram)	604	655	849	1753	1,430	1,534	2,038	2,761	2,589	2,555

Sources:

1) LME, Bloomberg. 2) LME, SHFE, Asian Metal Inc., Bloomberg. 3) BMI, Bloomberg. 4) Asian Metal Inc., Bloomberg.

Table 2

### Copper Price Outlook - Annual Averages

pre-pandemic						Medium Term
2018	2019	2020	2021A	2022F	2023F	... (2025+)
2.96	2.72	2.80	4.23	4.00	3.70	5.00

### Copper Quarterly Averages

		Actual															
		20-1	20-2	20-3	20-4	21-1	21-2	21-3	21-4	22-1	22-2	22-3	22-4	23-1	23-2	23-3	23-4
		2.56	2.42	2.96	3.25	3.85	4.40	4.25	4.40	4.53	4.32						
Sensitivities	High											3.80	4.00	3.80	4.00	4.20	4.30
	Base											3.50	3.65	3.40	3.60	3.80	4.00
	Low											3.20	3.30	3.00	3.20	3.40	3.70
Probability	High											0.20	0.20	0.20	0.20	0.20	0.20
	Base											0.60	0.60	0.60	0.60	0.60	0.60
	Low											0.20	0.20	0.20	0.20	0.20	0.20
<b>Probability-Weighted Forecast</b>												<b>3.50</b>	<b>3.65</b>	<b>3.40</b>	<b>3.60</b>	<b>3.80</b>	<b>4.00</b>

Source: LME official cash settlement, US\$/lb., quarterly averages.

### Nickel Price Outlook - Annual Averages

pre-pandemic					
2018	2019	2020	2021A	2022F	2023F
5.95	6.31	6.25	8.38	11.30	9.50

### Nickel Quarterly Averages

		Actual															
		20-1	20-2	20-3	20-4	21-1	21-2	21-3	21-4	22-1	22-2	22-3	22-4	23-1	23-2	23-3	23-4
		5.77	5.53	6.46	7.23	7.99	7.87	8.68	8.99	11.85	13.17						
Sensitivities	High											11.50	12.50	11.00	11.00	11.00	11.00
	Base											9.95	10.25	9.50	9.50	9.50	9.50
	Low											8.40	8.00	8.00	8.00	8.00	8.00
Probability	High											0.20	0.20	0.20	0.20	0.20	0.20
	Base											0.60	0.60	0.60	0.60	0.60	0.60
	Low											0.20	0.20	0.20	0.20	0.20	0.20
<b>Probability-Weighted Forecast</b>												<b>9.95</b>	<b>10.25</b>	<b>9.50</b>	<b>9.50</b>	<b>9.50</b>	<b>9.50</b>

Source: LME official cash settlement, US\$/lb., quarterly averages.

Note: The above forecasts assume a significant slowdown in global growth and the possibility of a mild recession, but not a severe recession as occurred in 2008-09.

***Disclaimer***

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