MORNING NOTES **Monday March 14, 2011**
Michael A. Berry, Ph.D.

Today's Notes:

1. **Talison Lithium (Chris Berry, MBA)**
2. **Rethinking Nuclear**
3. **CGX Energy and Derek Oil and Gas**

1. Talison Lithium: The New Manhattan Project

> "***We remain convinced that EVs powered by lithium-ion batteries will find a place in the consumer market constituting a major driver for demand for lithium carbonate. Demand for lithium batteries will also continue to grow in applications such as laptops, ipads, power tools and cell phones."***
> Cormark Securities Report on Talison Lithium - March 10, 2011

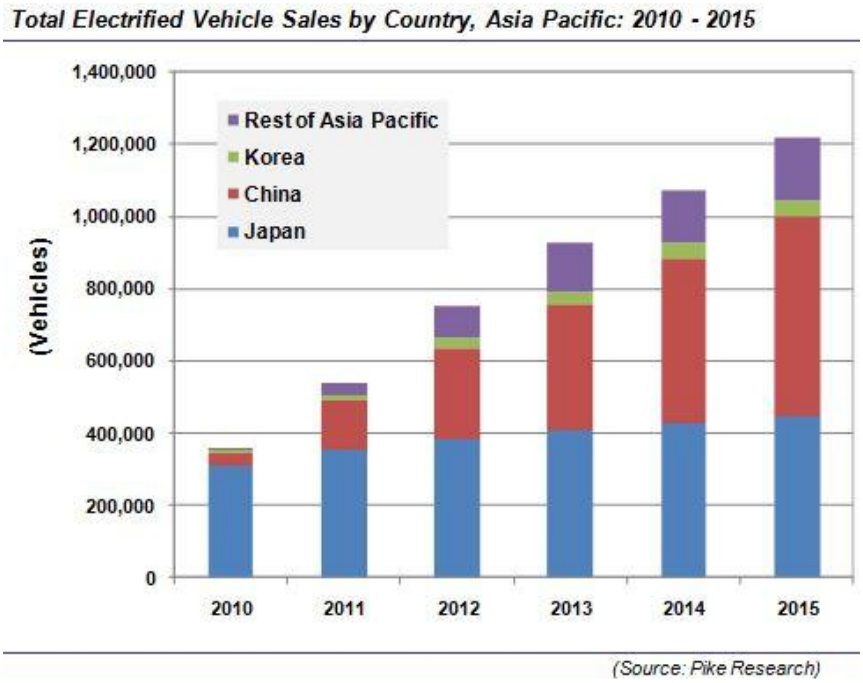
With the recent tumult in the commodities markets, it seems appropriate to take a step back and focus on the long-term fundamentals to make sure the investments you've made are positioned properly. While we could write this morning on any number of commodities – hard or soft – one in particular that we've written about extensively in the past is lithium. We think lithium will become a much more attractive investment opportunity and that Talison Lithium is the way to go.

An investment in lithium is a long term bet on the future of transportation and in particular the electrification of transportation. As recently as ten years ago, there wasn't a great deal of interest in or demand for lithium. Today it's a different story. This is due to the fact that lithium is one of the lightest metals and also due to its ability, in the case of lithium-ion batteries, to store three times the energy of nickel-metal hydride batteries. It's the energy density associated with lithium that is key. Without lithium, the iPhone or Blackberry wouldn't be as small as they are and they wouldn't hold the charge that they currently do – something to think about the next time you pull it out of your pocket and check "the juice" in your battery.

The future of lithium as a critical metal rests with the electric vehicle (EV) movement, though we expect demand for lithium use in chemicals, ceramics, and glass to remain steady going forward thereby providing a solid base. In the past decade lithium demand has increased from 69,000 tons of lithium carbonate equivalent to 117,000 tons in 2008.

The chart below shows expected EV demand in Asia. Though these numbers may seem small relative to total auto demand in Asia, demand for other forms of transportation using lithium-ion batteries such as e-bikes and mopeds is not factored in here. Even the latest power tools use lithium-ion batteries, a testament to the growing ubiquity and critical nature of the supply of the metal. Additionally, demand for EVs across the rest of the world needs to be considered when forecasting lithium demand and deciding where to place investment dollars. Last year, demand for lithium carbonate equivalent (LCE) was approximately 120,000 tonnes. By most forecasts, demand of 200,000 tonnes per year (tpy) is likely by 2015. It's true that electric vehicle propulsion, through full EVs, hybrid (HEVs), or plug-in hybrids (PHEVs), will remain a small part of the overall global vehicle fleet for some time. However we think

advances in battery technology and growing consumer acceptance will propel automotive demand and hence lithium demand going forward.



It is clear from an examination of the chart that the key and critical element to the lithium space is securing supply rather than fomenting demand. In January 2011, we attended the Third Annual Lithium Supply and Markets conference in Toronto. All of the world's lithium participants attended including producers, junior explorers, and end users such as Toyota. One of the themes that emerged was that of developing and owning an entire supply chain. It would appear that this is a critical, but often overlooked necessity for an industry pinning its hopes predominantly on one metal. The following chart shows an example of the supply chain graphic for lithium-ion batteries.

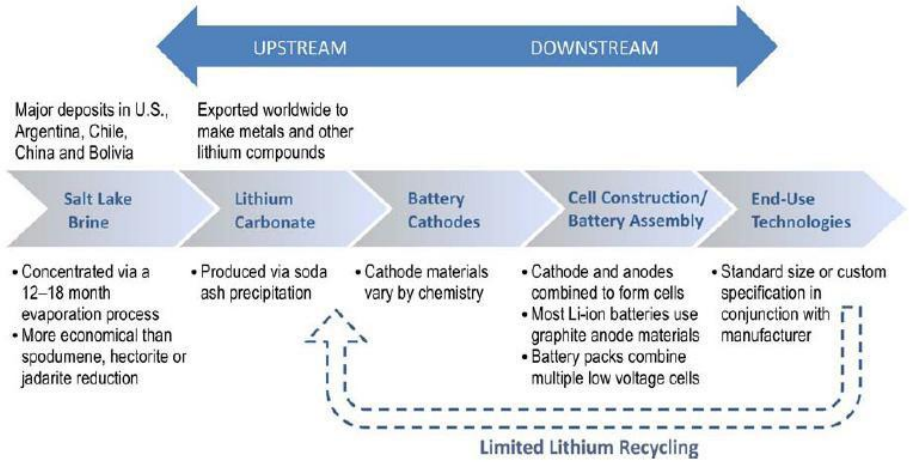


Figure 2-2. Supply chain for lithium-ion batteries

While the race to establish a dominant supply chain in lithium ion batteries intensifies, the real "game" with the lithium/transportation sector surrounds battery chemistry and finding that

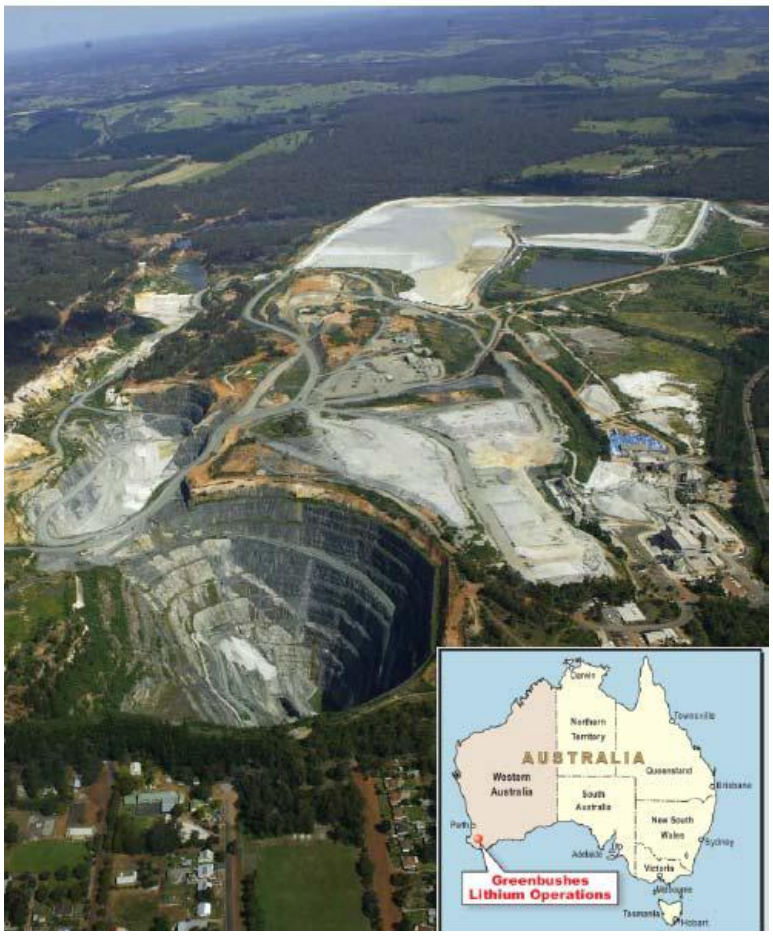
right mix that allows lithium-ion batteries for use in cars to compete economically with the internal combustion engine.
This is the new "Manhattan project" we referred to in the title of this Note. South Korea and Japan are current global leaders in perfecting battery chemistry with the US and, no surprise, China is catching up fast. There are numerous examples of companies joining forces to perfect battery technology and own a supply chain with its associated intellectual property.

Lithium One (LI: TSX-V) and their strategic relationship with KORES, LG International, and GS Caltex is one example. General Motors and LG Chem licensing Argonne Laboratory's lithium-ion battery technology for use in the Chevy Volt is another notable example.[1] From the press release announcing this alliance:
"The unique combination of lithium- and manganese-rich mixed-metal oxides in this stable materials-design approach extends the operating time between charges and increase the calendar life of batteries; improves the inherent safety of lithium-ion cells; and allows charging at higher cell voltages, which leads to a substantially higher energy storage capacity compared to current materials."

Talison Lithium: An Emerging Legacy Investment

So as auto companies and battery producers place their bets, locking up a steady supply of lithium raw material is imperative. This is where we focus our discovery efforts. While there are several promising juniors in the lithium space, our preferred mature discovery company is Talison Lithium (TLH: TSXV). Talison is not a junior, however, but is a major lithium supplier, newly public in the wake of its merger with Salares Lithium. Talison qualifies as a Mature Discovery company rapidly evolving into a Legacy Discovery opportunity. Below you can see its massive, high grade Greenbushes lithium operation near Perth, Australia.

[1] http://media.gm.com/content/media/us/en/news/news_detail.brand_gm.html/content/Pages/news/us/en/2011/Jan/0106_argonne



We have written extensively in past Morning Notes about why we like Talison, but what's interesting to note is that we're no longer the only ones. Last week, Cormark Securities published a major research report from which we extracted the following quote stating their view on the company:

Talison Lithium Limited (TLH - TSX)
Fortifying Its Position As A Top Producer - *Thursday, March 10, 2011*

Over the last 12 months, Talison Lithium has made significant strides in growing its investor base and solidifying its position as the largest producer of lithium concentrate in the world. The company recently completed the first phase of expansionary work at its wholly owned Greenbushes mine near Perth, Australia and has set out to double its production capacity to an estimated 110,000 tpy LCE per by F 2013. Concurrent with its recent listing on the TSX, the company also purchased the Salares 7 lithium brine project in Chile. As such, Talison offers investors exposure to its current and growing spodumene production at Greenbushes, exploration upside from the brine projects at Salares 7 as well as leverage to accelerating lithium demand.

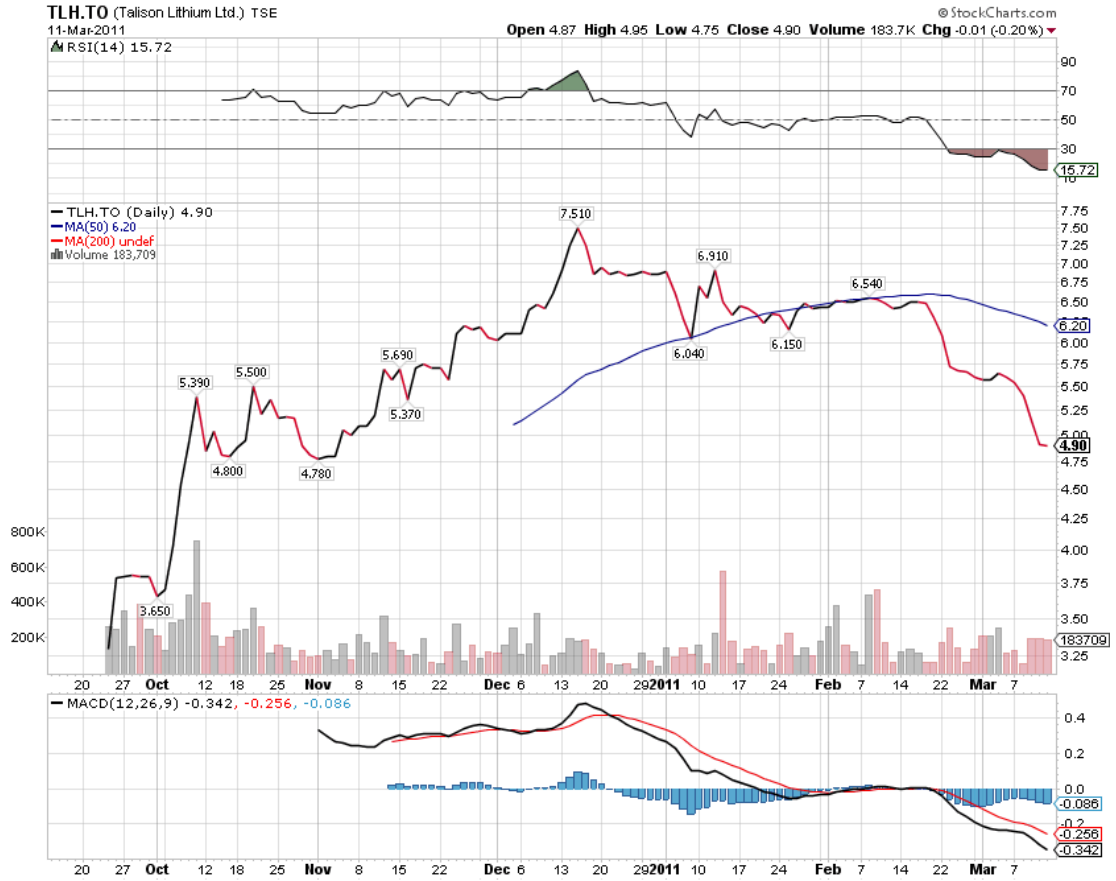
Talison supplies the world with approximately one third of the total lithium market and is in the second phase of an expansion plan to double its production capacity to 110,000 tpy by 2013. The company also produces the highest grade lithium concentrate in the world and satisfies 75% of China's lithium demand. With last year's take-over of Salares Lithium and

their Salares 7 brine assets in Chile, it's clear that Talison plans to cement its current position as a dominant low cost supplier of high-grade lithium. Exploration of its brines in Chile and growth of reserves at Greenbushes (their core asset) should create value for shareholders.

With this new "Manhattan Project" underway surrounding lithium-ion batteries and their use in the electrification of transportation, we think Talison, already a dominant force as a lithium producer, should create significant value for shareholders.

The shares soared to C$7.51 in the three months since listing on the Toronto Stock Exchange and have since fallen back to C$4.90 as you can see in the chart below. The shares more than doubled in the first three months of trading and have now consolidated by 33% since their high in mid-December. With Talison owning a dominant position as a lithium producer, they can exert control over their market and hence, their destiny. We believe that management can expand production at 1/5th the cost of any new greenfield lithium development.

In short, Talison can increase production faster and less costly than any other lithium provider and as we've said before: the lowest cost producer always wins.



We believe that once the global institutional buy side and the retail markets begin to understand Talison's low cost business model and notes its increasing cash flows this will be a stock in demand. It is clear to us that for a company that supplies 75% of China's lithium needs, today's RSI (see chart) is screaming that this stock is undervalued and a value investment. It is time to begin acquiring a position in Talison Lithium.

2. Nuclear Technology: Serious Rethinking

The terrible tragedy in Japan worsens. Water levels (seawater) are not increasing in the reactors to cool the core as I write this MN. The legacy of 40 year old nuclear technology and a natural disaster of immense proportion has given us a world class disaster. This has now given cause for a complete rethinking of energy strategy. We need to move more quickly to new nuclear technology in which fuel recycling is eliminated and safety against natural disasters can be assured. Japan produces 30% of its energy from its 17 nuclear reactors. If the situation in Japan is as reported and partial meltdowns are in process the implications for that country as well as longer term world economic growth are ominous.

What does China now do? It is clear that nuclear energy cannot today be totally replaced by alternative, renewable energy technologies such as solar and wind. It is clear that 40 year old nuclear technology must be retired, selectively. China has 23 nuclear reactors under construction currently. Will she halt her development progress to re-examine the technology? What impact will this have on carbon based energy sources such as coal, oil and gas? And what about the nuclear reactor(s) that Iran is ready to start-up? How well designed and protected are those systems? No one knows. There are now many questions to be answered. Perhaps that is the only bit of good news from this terrible tragedy. We will now re-think the nuclear question and move aggressively to standardized and safer fuel technology or throw in the towel on nuclear. We literally cannot afford to follow that course of action,. There are many new and safer nuclear technologies out there.

For example **IBC Advanced Alloys Corp (IB TSXV**) is developing beryllium oxide cladding for uranium fuel rods which appears to be non-reactive with the uranium fuel to 2100 degrees C. This development could reduce temperature and melt down concerns, a key problem now that both standard and emergency cooling mechanisms have apparently failed at two of Japan's Fukushima reactors. Gen 4 technology promises many advances. Let's get serious and move forward with the best energy technology possible.

Our prayers are with the people of Japan as they cope with this tragedy.

3. CGX Energy: Let the Drill Tell the Tale

In response to numerous emails queries, this is a quick review of CGX Energy (OYL TSXV) after meeting the company at PDAC in Toronto last week. I will not tell you what to do (buy/sell) except to say that I am holding my Incubator Discovery position. Here's why:

1) This is what discovery wealth is all about. No guarantee but you gotta be there to be rewarded.
2) CGX is drilling in a highly prospective basin offshore Guyana with a proven hydrocarbon system (Elephant country).
3) CGX is testing for multi-billion (potential world class) barrel resources in Jaguar and Eagle locations.

4) It has legacy and knowledgeable partners in Repsol and Tullow on the Jaguar well where drilling will commence in Q2.
5) Preparations are well underway for drilling on the Eagle target.
6) Oil, particularly sources of oil in the western hemisphere are becoming strategically important.
7) The price of oil is now above $100 per barrel. We think there is upside to this price.

Is this a guarantee of CGX success? No definitely not; but if you have waited this long you probably owe it to yourself to stay to see the CGX drill results, often the most exciting part of the discovery investing process. See www.cgxenergy.com. Kenny Rogers said it best. "Ya gotta know when to hold'em."

By the way the same question may be asked of **Derek Oil and Gas (DRK TSXV).** By the same reasoning as above I think you need to stay to see the results in their Wyoming Lak Ranch resource. Yes, there has been significant dilution to investors but the operating management is a very good team and new high performance boilers are in place. I suggest you consider staying in the Derek investment as well. As always, perform your own due diligence. If you are invested in DRK you have a 6 cent option on Wyoming oil production within a few miles of a refinery at Newcastle, Wyoming.

The material herein is for informational purposes only and is not intended to and does not constitute the rendering of investment advice or the solicitation of an offer to buy securities. The foregoing discussion contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 (The Act). In particular when used in the preceding discussion the words "plan," confident that, believe, scheduled, expect, or intend to, and similar conditional expressions are intended to identify forward-looking statements subject to the safe harbor created by the ACT. Such statements are subject to certain risks and uncertainties and actual results could differ materially from those expressed in any of the forward looking statements. Such risks and uncertainties include, but are not limited to future events and financial performance of the company which are inherently uncertain and actual events and / or results may differ materially. In addition we may review investments that are not registered in the U.S. We cannot attest to nor certify the correctness of any information in this note. Please consult your financial advisor and perform your own due diligence before considering any companies mentioned in this informational bulletin. We own Talison Lithium, Derek oil and Gas and CGX Energy.