GALAXY meeting a lithium future

GALAXY RESOURCES LIMITED

CHAIRMAN'S LETTER TO SHAREHOLDERS AND FUNDING UPDATE

20 May 2013

Dear Shareholder,

On behalf of the Board of Galaxy Resources Limited, we would like to provide an update of your Company and its capital raising plans. We have launched a 1 for 1 pro rata entitlement issue at $0.08 per share to raise up to $47 million. We believe it is very important to provide you with some context and background to this significant decision and the decisive actions we have taken within the business.

Galaxy's strategic plan has always been to become the preeminent producer of very high grade lithium carbonate to meet the demand of the rapidly growing lithium-ion battery market.

In the last four years, Galaxy's Management and Board have built a global lithium company on four continents by:

- Funding, constructing and commencing operations at the Mt Cattlin spodumene mine in Western Australia on time and budget;
- Funding, constructing and commencing operations of one of the world's largest and most advanced battery grade lithium carbonate plants, in China's Jiangsu province;
- Producing battery grade lithium carbonate that ranks as some of the best quality globally;
- Developing strong relationships within the key markets of China, Japan and Korea;
- Merging with TSX-listed Lithium One Inc. to acquire a low cost brine development project;
- Completing the Definitive Feasibility Study on the Sal de Vida Lithium Brine & Potash Project in Argentina on time and on budget.

Galaxy has taken all of the above projects from feasibility stage, right through construction and development to production and market establishment. No other lithium company has achieved this advanced penetration into the market over such a short space of time. In four years, Galaxy has built a global lithium business on the verge of being operationally cash flow positive (subject to sales and the progress of the Jiangsu Plant ramp-up to full production).

Galaxy's key asset, the Jiangsu Lithium Carbonate Plant is in production and is on schedule to become operationally cash flow positive by Q3 2013, subject to sales and the progress of the ramp-up to full production. The tragic pipeline rupture accident at Jiangsu in late 2012, and subsequent withdrawal of the proposed investment of $66 million by East China Mineral Exploration & Development Bureau, caused a significant financial and operational setback for the Company, resulting in a temporary shutdown of the Plant, loss of revenue and a considerable recovery process. The Jiangsu Plant is now producing at 60% of design capacity and daily production rates and sales of lithium carbonate continue to increase month by month. The Company's budget scenario, assuming it meets its Plant ramp-up and sales profile, is to achieve an operational EBITDA in 2014 of

$20 million to $30 million and to potentially increase further in future years as the product mix changes to higher value EV grade product.

The event at the Jiangsu Plant, however, has placed a significant burden on our working capital position, and we now require an injection of new equity during this production ramp-up phase.

Galaxy now presents its shareholders with an equitable opportunity to support the Company in this capital raising as we find ourselves in a very exceptional and very challenging period in our Company's history. Given the difficult equity raising environment and therefore the discount being offered, we consider that the appropriate course of action is to offer the equity raising to our 10,000 strong shareholder base, in order to provide the Company with the necessary working capital to achieve our vision of reaching positive cash flow status and becoming a major player in the lithium industry. This will enable existing shareholders the opportunity to maintain or increase their holding in the company on attractive terms.

On behalf of the Board of Galaxy, we would like to invite you to participate in the Company's upcoming capital raising. The capital raising is a one (1) for one (1) pro-rata entitlement offer (Entitlement Offer or the Offer) at an offer price of $0.08 per New Share. Applicants will also receive three (3) free attaching New Options for every two (2) New Shares subscribed. Galaxy intends to raise up to approximately $47 million through the Offer to raise funds for working capital (including interest payments), to reduce debt levels and a re-structure of the Company's balance sheet. The Entitlement Offer price of $0.08 per New Share represents an approximately 65% discount to the closing price of Galaxy Shares on 24 April 2013, being the day the Company's Shares last traded on ASX before announcement of the Entitlement Offer, an approximately 48% discount to the TERP (theoretical ex-rights price or TERP) and an approximately 66% discount to Galaxy's 5 day volume weighted average price on the ASX on 24 April 2013.

Patersons Securities Limited has been appointed Lead Manager to the Entitlement Offer. Deutsche Bank has been appointed Corporate Adviser leading debt re-arrangement and non-core asset sale initiatives.

The discount level and free attaching options are necessary in these very difficult financial markets but most importantly, being a pro rata offer, it is offered to give you an opportunity to maintain your level of holding in the Company. If shareholders do not support the Entitlement Offer, we will unlikely be able to achieve our plans to become cash flow positive. Ultimately, it will call into question the ability of the Company to continue.

We understand the frustrations shareholders are likely to have experienced in recent times and that in order to consider a further investment, will want to know, we have taken significant action.

To strengthen its position Galaxy has, with the assistance of our Corporate Adviser Deutsche Bank, undertaken a comprehensive strategic review, with the intention of creating a profitable and robust financial structure through cost reduction initiatives, re-scheduling of debt and non-core asset sales to reduce leverage. Corporate costs will be reduced from $17.6 million in 2012 to $12.2 million in 2013. The 2012 corporate costs were mainly due to Lithium One-related due diligence and merger activities, the Sal de Vida feasibility study as well as the start-up and commissioning of the Jiangsu Plant. A further $4.3 million in cost savings is being targeted to bring corporate costs over the next 12 months to around $7.9 million. Part of the cost reduction initiatives will be a salary cut of 20% for the Managing Director and Board of Directors, and 10-15% for executive management of the Company.

The Company currently has loans ($117 million) with three Chinese banks - China Construction Bank, Industrial and Commercial Bank of China, and Shanghai Pudong Development Bank – all with short term tenor. In addition Galaxy has existing convertible bonds on issue for $62 million which are subject to investor put options in November 2013 where the holder of the convertible bond has a right to require the Company to repay the face value of the convertible bond. The Company is working on various options to term out its debt maturity profile and restructure the convertible bonds. Longer tenor financing will give the Company time to further establish its business, and better match the liabilities to the cash flow profile. The Company has already implemented initiatives in the past 12 months to cut costs, restructure its balance sheet and to streamline business processes. This included the decision to place the Mt Cattlin spodumene mine on care and maintenance in favour of a more cost effective off take agreement from Talison Lithium.

Successful completion of the Entitlement Offer would allow the Company to reduce its gearing levels and, along with debt refinancing, would allow the Company to re-structure its balance sheet. The Company's key objectives in refinancing debt to better terms and conditions, is to achieve an optimised balance sheet structure that better matches its current stage of business and its growth profile going forward.

The Prospectus will include a shortfall application form which will allow shareholders to apply for shares in excess of what their entitlement might actually be and, to the extent that shareholders wish to subscribe for additional shares, we would encourage them to do so on the shortfall application form. Entitlements are non-renounceable. This means the rights to subscribe for New Securities under the Entitlement Offer are not transferable and there will be no trading of rights on ASX.

The issue of three (3) free attaching New Options for every two (2) New Shares subscribed for will enable Eligible Shareholders who take-up their Entitlements to benefit in any increase in Galaxy's share price above the New Option exercise price ($0.08) prior to the New Option expiry date (31 December 2014). Subject to satisfying the requirements for quotation, the New Options will also be tradeable on ASX, enabling New Option holders to realise value for the New Options through selling them on ASX if they so choose.

Shareholders who choose not to take up their entitlement will receive no value in respect of their entitlements and their shareholding in the Company will be diluted.

Galaxy has resolved to maintain the current voluntary suspension from trading in the Company's securities in place, while it seeks to successfully complete the Entitlement Offer and balance sheet re-structuring. The Company hopes trading in its securities will recommence shortly after the close of the Entitlement Offer, when it should have greater certainty as to its financial position and its balance sheet re-structuring.

On behalf of the Board, we thank you for your continued support for Galaxy and encourage you to participate in this investment opportunity.

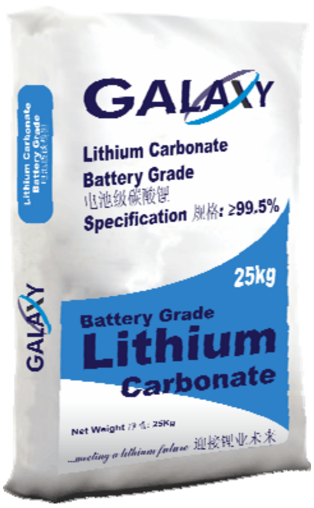
Yours Sincerely

Craig Readhead
Chairman

Iggy Tan
Managing Director

INVESTMENT HIGHLIGHTS

- *Global Lithium Producer and Chemical Business* – Galaxy is an Australian-based global lithium producer and chemical company focused on supply of lithium products for the lithium battery industry.
- *Lithium Battery Focused* – Galaxy's business is focused on the lithium battery sector, which continues to grow strongly from existing applications in consumer electronics, and advancing penetration into sectors such as power tools, electric bicycles, mass energy storage, hybrid and electric vehicles (EVs). The lithium battery sector continues to be one of the fastest growing sectors amongst consumers of lithium.
- *Strong Demand Growth Expected* – According to a wide range of industry analysts, demand for lithium is expected to grow by up to 200% in the next decade from about 140,000 tonnes per annum (lithium carbonate equivalent LCE) to around 250,000-300,000 LCE tonnes per annum. Galaxy is in a strong position to meet this growth. The Company has also strategically located its production capacity in China, which has proven to be the fastest growing market in the last few years.
- *Largest Capacity Producer of Battery Grade Lithium Carbonate in Asia* – Galaxy's key asset is the Jiangsu Lithium Carbonate Plant, one of the first fully-automated battery grade lithium carbonate plants in the world and one of the most technically sophisticated, producing consistent quantity and quality product. At full design capacity the Jiangsu Plant will be capable of producing 17,000 tonnes per annum of battery grade lithium carbonate, making it the largest battery grade plant in the world.



- *Jiangsu Produces Superior Battery Grade Quality* – The quality of the battery grade lithium carbonate from Jiangsu met the stringent battery grade specifications early in the start-up phase of the Plant. Today the product quality is amongst the best available in the global market. Qualification of the product by lithium cathode producers continues, with strong acceptances and early sales recorded to date.
- *Jiangsu Capable of Producing EV Grade® (99.9% LC) Lithium Carbonate* – While the Jiangsu Plant is designed to produce 17,000 tonnes per annum of battery grade (99.5% Li_2CO_3 purity), it is also capable of producing a higher specification grade product of 99.9% purity, registered by Galaxy as "EV Grade®". This product is used specifically in the manufacture of electrolyte solution for lithium batteries. The higher grade product tends to attract a higher price premium and provides the Company with additional marketing options.
- *Continued Ramp-Up of Production and Sales at Jiangsu Plant* – Galaxy continues to ramp-up production of the Jiangsu Plant, and expects the facility to be operationally cashflow positive during the third quarter of the year, subject to sales and ramp-up progress. The Jiangsu Plant is currently producing at 60% of design output and, at current production rates, is already the second largest lithium carbonate plant in China.

- *Strong Sales Growth* – Lithium carbonate product sales are also growing, with current volumes at approximately 575 tonnes per month, generating revenue of about $3.5 million per month (inclusive of VAT). Galaxy is committed to increasing sales to a range of lithium customers across China, Japan and Korea. Currently, Galaxy's customers are largely battery cathode manufactures, along with some technical grade customers. Customer acceptance of Galaxy's products has been very good to date. Sales commenced in mid-2012 and product qualification processes are ongoing with further customers in Asia. Significantly, the Company has commenced sales to the Japanese market – a market that sets the highest standards for product quality.
- *Jiangsu Records Positive Cash Inflows in April* – Jiangsu's April production totalled 650 tonnes. Average daily production in the month was 28 tonnes per day, representing 60% of the Plant's design output. April's figures included three weeks of production and excluded a one week scheduled outage for improvements and modifications. Product sales in April totalled 575 tonnes of battery and technical grade product. Sales revenue was $3.5 million (including VAT). Production cost for Jiangsu (excluding sunk ore costs) were $2.5 million for April, which means on a purely cash inflow and outflow basis, the operation generated positive inflows for the month.
- *Battery Grade Lithium Carbonate Business Potential* – Galaxy is well positioned both geographically and strategically, to take advantage of the fast growing lithium battery sector in China. The current price of battery grade (99.5%) lithium carbonate in China ranges from US$6,800 –US$7,200 per tonne (inclusive of VAT).[1] Assuming Jiangsu production and battery grade lithium carbonate sales at full capacity, the Company has the potential to generate revenue of US$115 million to US$122 million per annum. The Company expects that the operating costs could range between US$4,900 to US$5,300 per tonne of lithium carbonate. There is a potential upside of selling some product at the higher grade of 99.9% lithium carbonate, which has a current price range of US$7,900 to US$8,250 per tonne (inclusive of VAT).[2]
- *China's Focus on Renewable Energy* – Galaxy's strategy takes into consideration China's 12th 5-year plan for the country, which focuses on development and uptake of renewable energies and lessening reliance on oil. Lithium has a key role to play in China's plans for a lower carbon economy, including a target for 5 million EVs on China's roads by 2020, and 50% ownership EV/hybrids by 2030. Overall, China targets 20% of energy to be from renewable energy sources by 2020.[3]
- *Sal de Vida Definitive Feasibility Study* – Galaxy is advancing plans to develop the Sal de Vida Lithium and Potash Brine Project in Argentina, in which it has a 70% holding. A recently completed Definitive Feasibility Study confirmed robust economics for a low cost, long life lithium and potash project. Potential annual revenues from the Sal de Vida project are in the region of US$215 million, with operating cash flow before interest and tax of US$118 million per annum at full production rates. The capital cost estimate was US$369.2 million, with average operating costs US$2,200 per tonne (net of potash credits). Galaxy sees Sal de Vida as a future flagship asset for the Company.

---

[1] Source: *Asian Metal Ltd – Lithium Market Report March 2013.*

[2] Source: *Asian Metal Ltd – Lithium Market Report March 2013.*

[3] Source: PRC Ministry of Industry and Information's (MIIT) 2012 released policy "*China Energy Efficient and New-Energy Vehicles Industrial Plan 2012-2020*" released 28 June 2012.