

## TALISON LITHIUM LIMITED



### MANAGEMENT'S DISCUSSION & ANALYSIS OF THE FINANCIAL CONDITION AND RESULTS OF OPERATIONS OF TALISON LITHIUM LIMITED AS AT AND FOR THE THREE MONTHS ENDED SEPTEMBER 30, 2011

NOVEMBER 10, 2011

This document provides management's discussion and analysis ("**MD&A**") of the financial condition and results of operations of Talison Lithium Limited ACN 140 122 078 ("**Talison**" or the "**Company**") as at September 30, 2011 and for the three months ended September 30, 2011. This MD&A is prepared as at November 10, 2011 and is current to that date unless otherwise stated.

This MD&A should be read in conjunction with the unaudited condensed consolidated interim financial statements of Talison as at September 30, 2011 and for the three months ended September 30, 2011 (collectively, the "**Financial Statements**"). The financial information contained in this MD&A is derived from the Financial Statements, which were prepared in accordance with International Financial Reporting Standards ("**IFRS**"). All amounts in this MD&A are expressed in Australian dollars ("**A\$**") unless otherwise identified. References to "**C\$**" are to Canadian dollars and references to "**US\$**" are to United States dollars.

The following discussion contains forward-looking statements that involve numerous risks and uncertainties. Actual results of Talison could differ materially from those discussed in such forward-looking statements as a result of these risks and uncertainties, including those set forth under the heading "Cautionary Notes — Forward-Looking Statements" and under the heading "Risk Factors" in Talison's annual information form for the year ended June 30, 2011 dated September 23, 2011 (the "**Annual Information Form**"), which risk factors are incorporated herein by reference and can be found on Talison's SEDAR profile at [www.sedar.com](http://www.sedar.com).



Readers of this MD&A are cautioned that certain statements in this MD&A may relate solely to the debt and capital structure of Talison Minerals Pty Ltd ("**Talison Minerals**") before the Reorganization (as defined below) and may be of no consequence to the ongoing operations of Talison.

Additional information about Talison and its business activities is included in Talison's continuous disclosure documents, which are located on Talison's SEDAR profile at [www.sedar.com](http://www.sedar.com). Readers are cautioned not to rely solely on the summary of such information contained in this MD&A, but should also read the Annual Information Form and subsequent press releases which can be found on Talison's SEDAR profile at [www.sedar.com](http://www.sedar.com).

## 1. Overview

Talison was incorporated under the *Corporations Act 2001* (Commonwealth of Australia) (the "**Corporations Act**") as a public company on October 22, 2009 and was listed on the Toronto Stock Exchange (the "**TSX**") under the trading symbol "TLH" on September 22, 2010.

Talison mines and processes lithium bearing mineral spodumene at its operations located at Greenbushes, Western Australia (the "**Greenbushes Lithium Operations**"), located approximately 250 kilometres from Perth, Western Australia. Talison acquired the Greenbushes Lithium Operations by acquiring Talison Minerals on August 12, 2010 in connection with a substantial debt and equity restructuring of Talison Minerals (the "**Reorganization**").

Management of Talison believes that the Greenbushes Lithium Operations host the world's largest known reserves of lithium minerals with a current mine life of 22 years. Talison produces a range of lithium concentrates which are distributed to a well-established global customer base. Talison has a leading position in the growing Chinese lithium concentrates market.

Talison produces two categories of lithium concentrates: (i) technical-grade lithium concentrates which have low iron content for use in the manufacture of, among other applications, glass, ceramics and heat-proof cookware; and (ii) a high-yielding chemical-grade lithium concentrate which is used to produce lithium chemicals which form the basis for manufacture of, among other applications, lithium-ion batteries for laptop computers, mobile phones, electric bicycles and electric vehicles. Talison does not currently produce lithium chemical products itself. Instead, it sells lithium concentrate to customers for processing into lithium chemicals, primarily lithium carbonate.

Following the Reorganization, Talison completed a statutory plan of arrangement under the *Business Corporations Act* (British Columbia) ("**Plan of Arrangement**") on September 22, 2010, pursuant to which Talison acquired, directly and indirectly, all of the outstanding securities of Salares Lithium Inc. ("**Salares**"). Upon completion of the Plan of Arrangement, Salares became an indirect wholly-owned subsidiary of Talison. In connection with the Plan of Arrangement, Salares undertook a private placement financing to raise gross proceeds of C\$40 million (the "**Financing**"). Further details regarding the Plan of Arrangement and the Financing can be found on Talison's SEDAR profile at [www.sedar.com](http://www.sedar.com).

Through its acquisition of Salares, Talison has an extensive lithium brine exploration project in Region III, Chile (the "**Salares 7 Project**"). The Salares 7 Project is made up of seven salars (brine lakes, and the surrounding concessions) that are prospective for sub-surface lithium and potassium. Five of the seven salars are clustered within 155 kilometres. Talison and its Chilean partner own 100% of five of the salares, Grande, Aguilar, Agua Amarga, La Isla and Las Parinas and hold a portion of the remaining two salares, Piedra Parada and Maricunga.

Talison completed a bought deal financing on February 10, 2011 ("**Bought Deal Financing**") for gross proceeds of C\$69.6 million which together with the exercise of a related over-allotment option resulted in the total gross proceeds of C\$80.0 million. Net proceeds from the Bought Deal Financing will be used primarily to fund the Stage 2 expansion of the Greenbushes Lithium Operations, exploration of the Salares 7 Project, and for general corporate and working capital purposes.

Talison is currently completing the Stage 2 expansion of the Greenbushes Lithium Operations at a total capital cost of A\$65-70 million which will see production capacity more than double to approximately 740,000 tonnes per annum of lithium concentrate (approximately 110,000 tonnes per annum lithium carbonate equivalent ("**LCE**")). Commissioning of the Stage 2 expansion is anticipated to commence in the second quarter of calendar 2012.



## 2. Highlights for the First Quarter ended September 30, 2011

- In anticipation of sustained growth in lithium consumption, driven primarily by the secondary lithium battery market, Talison continued to aggressively pursue its three growth projects encompassing its Australian capacity expansion, proposed lithium minerals conversion plant and its South American salar exploration program.
- Construction of the Stage 2 expansion of the Greenbushes Lithium Operations to double production capacity continued during the quarter in line with budget. The foundations and civil works are nearing completion and off-site fabrication is well advanced with significant plant component parts delivered to site in preparation for the commencement of on-site construction.
- The preliminary engineering and location study in relation to the proposed construction of a lithium mineral conversion plant is nearing completion and the project is expected to move into the detailed studies phase in 2012 with an investment decision anticipated by the end of calendar 2012. During the quarter, Talison engaged with key stakeholders on the potential locations for its proposed plant receiving favourable responses.
- Offices in Shanghai and Santiago were opened to strengthen relationships with customers and facilitate the development of the Salares 7 Project respectively.
- Lithium concentrate production for the first quarter of 90,708 tonnes (approximately 13,500 tonnes LCE), representing a 12% increase over the corresponding period in the prior year.
- Lithium concentrate sales for the first quarter of 80,315 tonnes (12,000 tonnes LCE), representing a 53% increase over the corresponding period in the prior year.
- Operating cost per tonne for the first quarter reduced by 6% and the average sale price increased by 5% compared to the corresponding period in the prior year.
- Earnings before interest, income tax, and depreciation and amortization ("**EBITDA**") for the three months ended September 30, 2011 of A\$6.1 million on revenues of A\$25.9 million, representing a 28% and a 23% increase, respectively, over the corresponding period in the prior year. (The term "EBITDA" is a non-IFRS financial measure. For a reconciliation of EBITDA to its IFRS-compliant income statement, see "Non-IFRS Performance Measures").
- EBITDA as a percentage of sales revenue increased to 24%, despite a 16% increase in the A\$/US\$ exchange rate compared to the corresponding period in the prior year which had an adverse impact on profitability. The average A\$/US\$ exchange rate for the three months ended September 30, 2010 was 0.90. A constant A\$/US\$ exchange rate of 0.90 for the three months ended September 30, 2011 would have resulted in EBITDA, as a percentage of sales revenue, increasing to approximately 33% reflecting the increase in the average US\$ sale price and reduction in the average A\$ cash operating cost of goods sold compared to the corresponding period in the prior year.

EBITDA Analysis	Three Months Ended September 30, 2011 (Unaudited)	Twelve Months Ended June 30, 2011 (Audited)	Three Months Ended June 30, 2011 (Unaudited)	Three Months Ended March 31, 2011 (Unaudited)	Three Months Ended December 31, 2010 (Unaudited)	Three Months Ended September 30, 2010 (Unaudited)	Twelve Months Ended June 30, 2010 (Audited)
Sales (tonnes lithium concentrate)	80,315	339,501	92,416	97,001	97,559	52,525	256,767
Average sales price (US\$/tonne lithium concentrate)	US\$330 <sup>(1)</sup>	US\$308	US\$302	US\$303	US\$315	US\$313	US\$281
Sales revenue (\$A'000)	A\$25,879	A\$109,501	A\$26,412	A\$29,207	A\$32,810	A\$21,072	A\$81,278
Cash operating cost of goods sold (A\$/tonne lithium concentrate)	A\$207 <sup>(1)</sup>	A\$200	A\$184	A\$195	A\$208	A\$221	A\$226
General/Administration/ Other (A\$'000)	A\$3,159	A\$13,186	A\$3,680	A\$3,937	A\$3,566	A\$2,003	A\$4,553
EBITDA (A\$'000)	A\$6,126	A\$24,066	A\$5,755	A\$6,308	A\$7,233	A\$4,770	A\$18,661
EBITDA as a percentage of sales revenue	24%	22%	22%	22%	22%	23%	23%

Note:

- (1) Compared to the June 30, 2011 quarter, the average sale price for the September 30, 2011 quarter increased by 9% to US\$330/tonne. This was due to a 5% increase in the chemical-grade price and a change in the sale mix with proportionately more higher value technical-grade product sold in the September 30, 2011 quarter. As a result of the change in sales mix to the higher value technical-



grade product, the cash operating cost of goods sold also increased compared to the June 30, 2011 quarter. Importantly EBITDA, as a percentage of sales revenue in the September 30, 2011 quarter increased to 24%.

### 3. Market Trends and Fundamentals

During the first quarter of the 2012 financial year, the market for technical-grade lithium concentrate remained steady with production fully sold. The market for chemical-grade lithium concentrate continued to grow during the first quarter, with demand remaining strong from both new and existing customers.

During the first quarter, global supply of lithium products from existing producers in South America was impacted by weather conditions and cost increases for raw materials, transport and energy. Supply from new projects is not expected to have a major impact on the global market for several years due to the lower quality of the deposits, high capital costs and time required for development.

There are no terminal markets for lithium concentrates, with the market determined directly by supplier/customer negotiations. Because of this, the lithium market is relatively opaque and therefore pricing trends are not widely published. Generally, statistics on sales volumes and prices are based on global import/export data. Prices for lithium concentrates used for conversion into chemicals are correlated to, and tend to follow the same trend as, lithium carbonate prices. Talison believes the announcements of price increases of up to 25% by two of the three other major lithium producers in mid-2011 are indicative of a tightening in lithium supply leading to an expectation of higher prices in calendar 2012.

### Foreign Currency Fluctuations

Talison's revenues are received in US\$. However, operations are carried out in Australia, with the majority of operating costs and capital expenditures incurred in A\$. The A\$/US\$ exchange rate for the three months ended September 30, 2011 averaged US\$1.04 per A\$1.00, an increase of 16% compared to the corresponding period in the prior year. This has had the effect of lowering A\$ revenues by a corresponding amount. Talison hedges the A\$/US\$ exchange rate to manage its US\$ foreign currency exposure.

### 4. Outlook

For the three months ending December 31, 2011, Talison expects production of lithium concentrate to be in-line with the three months ended September 30, 2011. Sales tonnages of lithium concentrate for the three months ending December 31, 2011 are expected to exceed production for the quarter. Sales are expected to materially match production for the six months ended December 31, 2011.

During the year ending June 30, 2012, Talison expects that sales volume will be limited by the capacity of the processing plants at the Greenbushes Lithium Operations until completion of the expansion of production capacity. As commissioning of the expansion is not due to commence until the fourth quarter of the 2012 financial year, it is not expected to impact results for the 2012 financial year. However a full year contribution from the Stage 1 Expansion of the Greenbushes Lithium Operations is anticipated and, with ongoing process improvements, production and sales tonnages for the 2012 financial year are expected to be consistent with the three months ended June 30, 2011, on an annualized basis.

Talison secured price increases for two shipments of chemical-grade concentrate during the quarter which is reflected in the average sale price for the first quarter and believes this, together with price increases announced by other lithium producers, is reflective of a tightening in global lithium supply. This is expected to enhance Talison's sales prices for its concentrates in the 2012 calendar year.

In light of recent turmoil in Europe, Talison continuously monitors and reviews its sales expectations for the European markets. The company is not highly exposed to European markets, with approximately 10% of sales destined for Europe primarily Germany,



## 5. Operations Overview

### Greenbushes Lithium Operations Stage 2 Expansion

In response to continued strong demand for lithium concentrate, Talison committed to the Stage 2 expansion of the chemical-grade plant at the Greenbushes Lithium Operations. The Stage 2 expansion is currently in the construction phase and upon completion of the expansion, which is scheduled for the second quarter of calendar 2012, the capacity of the Greenbushes Lithium Operations will more than double to approximately 740,000 tonnes per annum lithium concentrate (approximately 110,000 tonnes per annum LCE).

Despite recent expansions Talison's sales volumes remain capped due to the limits on capacity of the processing plants at the Greenbushes Lithium Operations. The completion of the Stage 2 expansion will provide Talison with the ability to sell an additional 60,000 tonnes per annum of LCE from the middle of the 2012 calendar year. In addition to the ability to increase sales volumes, the expansion is expected to substantially reduce Talison's unit operating costs and increase its competitiveness, through improved lithium recovery and economies of scale.

Globally, demand for lithium products remains strong and indications of a tightening in lithium supply are emerging. The increased capacity provided by the expansion will enable Talison to respond rapidly to changing market conditions and this is expected to strengthen Talison's position in the lithium market.

Talison believes that the long-term viability of the lithium market is best achieved by product prices that enable existing producers to justify further capital expenditure to maintain a stable, secure and growing supply of lithium, and Talison intends to pursue a pricing strategy for its lithium products on the basis of this objective.

To this end, Talison is currently engaging in negotiations with its customers with regards to calendar 2012 pricing and volume requirements.

### Salares 7 Project

Following the receipt of outstanding results for both lithium and potassium from the initial drilling at the Salares 7 Project in Chile, Talison is accelerating its exploration program and expects to invest approximately US\$5 million in the 2012 financial year on Phase 2 of the exploration program which is now underway.

A new custom built sonic drill rig with specific capabilities to suit the ground conditions at the Salares 7 Project is being assembled.

The drilling for the Phase 2 exploration program is expected to commence in the third quarter of the 2012 financial year and includes approximately 4,000 to 5,000 metres of drilling focusing on Salar de la Isla. The objective is to define a lithium mineral resource estimate at Salar de la Isla.

### Proposed Minerals Conversion Plant

Responding to growing global demand for an additional secure supply of lithium carbonate, particularly from electric vehicle battery manufacturers, Talison is aggressively pursuing its proposed plant to convert lithium minerals into lithium carbonate ("Minerals Conversion Plant"). Plant capacity is proposed to be 20,000 tonnes per annum LCE in the first stage, and an additional 20,000 tonnes per annum LCE in the second stage.

A location study for the Minerals Conversion Plant is in progress. Potential locations have been narrowed to the Greenbushes Lithium Operations or one other Western Australian location. During the quarter, Talison engaged with key stakeholders on the potential locations and received favourable responses from all parties.

An external engineering consultant is preparing estimates of capital costs and operating costs, which should be completed by the end of this calendar year. Based on initial indications of operating costs, Talison believes that it will be a globally competitive lithium carbonate producer.

### New Offices in Shanghai and Santiago

Talison recently opened an office in Shanghai to support its growing business in China. Talison has been operating successfully in China for over 10 years, and the new office will assist the Company in strengthening relationships with new and existing customers.



Talisson has also established an office in Santiago to facilitate the development of the Salares 7 Project. This office will support the exploration, environmental and process test work currently being conducted by the Company in Chile.

## 6. Results of Operations

The table below summarizes selected financial data for Talisson for the three months ended September 30, 2011, compared to the comparable financial data for the three months ended September 30, 2010. The table below also summarizes selected financial data for Talisson for the twelve months ended June 30, 2011 and for the Greenbushes Lithium Operations for the twelve months ended June 30, 2010. This financial data is derived from the Financial Statements which were prepared in accordance with IFRS.

<b>INCOME STATEMENT</b>	<b>Three Months Ended September 30, 2011 (Unaudited) A\$'000</b>	<b>Three Months Ended September 30, 2010 (Unaudited)<sup>(1)</sup> A\$'000</b>	<b>Twelve Months Ended June 30, 2011 (Audited)<sup>(1)</sup> A\$'000</b>
Sales revenue .....	25,879	21,072	109,501
Operating costs .....	(16,594)	(13,235)	(70,616)
Other income / (expenses) .....	(3,159)	(3,067)	(14,819)
<b>EBITDA<sup>(3)</sup></b> .....	<b>6,126</b>	<b>4,770<sup>(2)</sup></b>	<b>24,066<sup>(2)</sup></b>
Depreciation and amortization.....	(688)	(820)	(3,428)
Net financing income / (costs) .....	857	(3,859)	(3,798)
Net realized US\$ hedging gain.....	2,048	(40)	2,979
Net realized foreign exchange gain / (loss) .....	431	3,449	7,561
Net fair value gain/(loss) on financial assets and liabilities.....	(6,419)	6,067	4,664
Income tax (expense) / benefit.....	(748)	(3,693)	(9,108)
<b>Net profit/(loss) for the period</b> .....	<b>1,607</b>	<b>5,874</b>	<b>22,936</b>
Basic earnings per share (cents/share) <sup>(4)</sup> .....	1.5	11.0	25.7
Diluted earnings per share (cents/share) <sup>(4)</sup> .....	1.5	10.8	24.9
Basic weighted average number of shares .....	107,730,822	53,569,136	89,321,871

Notes:

- (1) The financial results for the three months ended September 30, 2010 and twelve months ended June 30, 2011 are comprised of the results of Talisson for the period from August 12, 2010 to September 30, 2010 and from August 12, 2010 to June 30, 2011 (i.e., post-Reorganization), respectively, and the carve-out results of the Greenbushes Lithium Operations for the period from July 1, 2010 to August 11, 2010 (i.e., pre-Reorganization). Readers are cautioned that the results for the period from July 1, 2010 to August 11, 2010 may not be reflective of the ongoing affairs of Talisson.
- (2) EBITDA for the three months ended September 30, 2010 and twelve months ended June 30, 2011 included A\$1.6 million in non-recurring Reorganization costs.
- (3) EBITDA is a non IFRS financial measure. For a reconciliation of EBITDA to its IFRS compliant income statement, see "Non-IFRS Performance Measures".
- (4) Basic and diluted earnings per share have been calculated based on the weighted average number of shares on issue. For the three months ended September 30, 2011, the weighted average number of shares includes both the outstanding ordinary shares of Talisson adjusted to remove ordinary shares held by the Talisson Long Term Incentive Plan Trust which is consolidated under IFRS, and the exchangeable shares of Talisson Lithium Exchangeco Limited, an indirect wholly-owned subsidiary of Talisson that are exchangeable (on a one-for-one basis) for ordinary shares of Talisson. For the three months ended September 30, 2010 and twelve months ended June 30, 2011, the weighted average number of shares includes the outstanding ordinary shares of Talisson adjusted to remove ordinary shares held by the Talisson Long Term Incentive Plan Trust which is consolidated under IFRS, the exchangeable shares of Talisson Lithium Exchangeco Limited that are exchangeable (on a one-for-one basis) for ordinary shares of Talisson, and the ordinary shares of Talisson Minerals adjusted for the Talisson Minerals share consolidation which occurred as part of the Reorganization. See "Outstanding Share Data".

The table below summarizes selected key operating statistics for Talisson for the three months ended September 30, 2011, as compared to the key operating statistics for the three months ended September 30, 2010.



KEY OPERATING STATISTICS	Three Months Ended September 30, 2011 (Unaudited)	Three Months Ended September 30, 2010 (Unaudited)	Percentage Change
Production (tonnes lithium concentrate).....	90,708	80,729	12%
Sales (tonnes lithium concentrate).....	80,315	52,525	53%
Average sales price (US\$/tonne lithium concentrate) .....	330	313	5%

## FIRST QUARTER OF 2012 FINANCIAL YEAR COMPARED TO FIRST QUARTER OF 2011 FINANCIAL YEAR

Demand for Talison's technical-grade and chemical-grade lithium concentrates continued at robust levels for the three months ended September 30, 2011. Demand remains in excess of current production capacity and Talison is currently producing and selling at capacity.

A total of 90,708 tonnes of lithium concentrate (approximately 13,500 tonnes LCE) were produced during the three months ended September 30, 2011, representing a 12% increase over the corresponding period in the prior year. The strong production results are attributable to a successful production process improvement program that continually targets de-bottlenecking in both the technical-grade and chemical-grade plants and completion of the Stage 1 expansion of the Greenbushes Lithium Operations in December 2010. The volume of ore processed across both plants in the quarter was 8% higher than that in the corresponding period in the prior year and the average product yield improved by 4%.

Sales of lithium concentrate during the three months ended September 30, 2011 of 80,315 tonnes (approximately 12,000 tonnes LCE) represented a 53% increase over the corresponding period in the prior year. This increase was driven by a strong increase in demand for both Talison's technical-grade and chemical-grade products. Lithium concentrate sales for the first quarter of the 2012 financial year were lower than lithium concentrate production during the quarter as a result of Talison's shipment schedule. Talison is currently producing at capacity and selling 100% of its production. The timing of Talison's shipment program will result in variations between production and sales in individual quarters.

The average sales price of lithium concentrates sold during the three months ended September 30, 2011 was US\$330 per tonne, as compared with an average price of US\$313 per tonne during the three months ended September 30, 2010, representing a 5% increase. The increase in average price was due to a combination of underlying average price increases of 13% for technical-grade products and 3% for chemical-grade products and a greater proportion of chemical-grade products sold in the three months ended September 30, 2011 compared to the corresponding prior year period.

Sales revenue for the three months ended September 30, 2011 was A\$25.9 million. In US\$ terms, sales revenue was 61% higher than that of the corresponding period in the prior year. However, including the sale of crushed ore in 2010 (which was a one off sale) and as a result of the adverse effect of a 16% increase in the value of the A\$ against the US\$ between the two periods, sales revenue in A\$ terms was only 23% above the corresponding period in the prior year.

Operating costs for the three months ended September 30, 2011 were A\$16.6 million, an increase of 25% over the corresponding period in the prior year, as a result of the increase in sales. The operating cost per tonne of lithium concentrate sold decreased by 6%, due to the new ore reserve announced in May 2011 which substantially increased the mine life and lowered the life of mine strip ratio of the ore body, and economies of scale as a result of the high production and sale volumes.

Other income and expenses for the three months ended September 30, 2011 of A\$3.2 million included A\$2.2 million in corporate administration costs and A\$1.2 million for share option expenses and is comparable to the amount in the corresponding prior year period.

EBITDA achieved by Talison for the three months ended September 30, 2011 of A\$6.1 million was a A\$1.4 million or 28% increase over the corresponding period in the prior year. This was due to a 53% increase in sales volumes and A\$1.6 million in non-recurring Reorganization costs incurred in the prior year partly offset by a 16% increase in the value of the A\$ against the US\$ between the two periods. (The term "EBITDA" is a non-IFRS financial measure. For a reconciliation of Talison's EBITDA to its IFRS-compliant income statement, see "Non-IFRS Performance Measures").



Depreciation and amortization charges for the three months ended September 30, 2011 were A\$0.7 million, a decrease of 16% over the corresponding period in the prior year. The majority of Talison's depreciation and amortization charges are determined by reference to production levels as a proportion of remaining lithium mineral reserves. While production levels increased during the period, the substantial increase in lithium mineral reserves announced on May 4, 2011, resulted in a reduction in depreciation between the two periods.

The net finance expense of Talison for the three months ended September 30, 2011 was A\$0.9 million consisting of the net interest income on cash deposits of A\$1.4 million, and finance expenses of A\$0.5 million, mainly in relation to Talison's senior debt. These amounts are not comparable to the amount in the corresponding period in the prior year as that amount reflected the debt levels of Talison Minerals which were significantly higher than the debt levels of Talison. Talison's ongoing debt levels and their terms are discussed under the heading "Discussion of Financial Position, Capital Resources and Liquidity — Interest Bearing Liabilities".

Talison managed its A\$/US\$ exchange rate risk by hedging. The net realized US\$ hedging gain / (loss) reflects the net gain / (loss) on those hedging activities. It is calculated as the difference between the A\$/US\$ exchange rate realized on delivering into the hedge and the spot exchange rate on the day of delivery less any net realized US\$ hedging gain / (loss) recognized in sales revenue and any costs incurred in establishing the hedge.

The net realized foreign exchange gain of \$0.4 million relates to gains realized on US\$ denominated cash deposits and trade debtors. The corresponding prior year period includes a large foreign exchange gain realized as a result of the Reorganization of Talison Minerals.

The net fair value loss on financial assets and liabilities for the three months ended September 30, 2011 of A\$6.4 million represents mainly an unrealized loss in the mark to market value of Talison's US\$ hedge book (A\$4.8 million) and an unrealized loss on the revaluation of Talison's US\$ senior debt (A\$2.7 million) as a result of a 9% reduction in the A\$/US\$ exchange rate from 1.07 at June 30, 2011 to 0.97 at September 30, 2011. The A\$/US\$ exchange rate at November 10, 2011 is 1.02 and consequently part of the net fair value loss on financial assets and liabilities of A\$6.4 million has reversed.

The income tax expense is based on Australia's corporate income tax rate of 30% after allowing for any non-deductible expenses.

## 7. Summary of Quarterly Results

Selected financial data from the time the Company became a reporting issuer is included in the table below.

FOR THE THREE MONTHS ENDED	September 30, 2011 A\$'000	June 30, 2011 A\$'000	March 31, 2011 A\$'000	December 31, 2010 A\$'000	September 30, 2010 A\$'000
Sales revenue	25,879	26,412	29,207	32,810	21,072
Cost of sales	(17,282)	(17,613)	(19,887)	(22,489)	(14,055)
Gross profit	8,597	8,799	9,320	10,321	7,017
Net profit	1,607	7,891	3,874	5,297	5,874
Gross Profit Margin	33%	33%	32%	31%	33%
Basic earnings per share (cents)	1.5	7.3	3.8	5.6	11.0
Diluted earnings per share (cents)	1.5	7.1	3.7	5.4	10.8

The Company's results for September 30, 2011 are discussed throughout this document, with the results for prior periods discussed in the respective quarterly financial statements and related management's discussion and analysis located on [www.sedar.com](http://www.sedar.com).



## 8. Discussion of Cash Flows

The table below summarizes selected financial data of Talison for the three months ended September 30, 2011, as compared to the comparable financial data for the three months ended September 30, 2010. This financial data is derived from the Financial Statements which were prepared in accordance with IFRS.

<b>CASH FLOW STATEMENT</b>	<b>Three Months Ended September 30, 2011 (Unaudited) A\$'000</b>	<b>Three Months Ended September 30, 2010 (Unaudited)<sup>(1)</sup> A\$'000</b>
Operating Activities .....	8,214	8,010
Investing Activities.....	(19,076)	(3,713)
Financing Activities .....	(638)	33,399

Note:

- (1) The financial results for the three months ended September 30, 2010 are comprised of the unaudited results of Talison for the period from August 12, 2010 to September 30, 2010 (i.e., post-Reorganization) and the carve-out audited results of the Greenbushes Lithium Operations for the period from July 1, 2010 to August 11, 2010 (i.e., pre-Reorganization). Readers are cautioned that the results for the period from July 1, 2010 to August 11, 2010 may not be reflective of the ongoing affairs of Talison.

### FIRST QUARTER OF 2012 FINANCIAL YEAR COMPARED TO FIRST QUARTER OF 2011 FINANCIAL YEAR

The Company's cash inflow from operating activities for the three months ended September 30, 2011 of A\$8.2 million was consistent with the three months ended September 30, 2010 despite a 23% increase in sales revenue, an increase in receipts from the settlement of derivatives and lower interest charges, as the three months ended September 30, 2011 included a A\$4.1 million increase in working capital compared to a A\$8.1 million reduction in working capital in the corresponding prior year period. Working capital does fluctuate from quarter to quarter depending on the timing of shipments.

The cash outflow from investing activities for the three months ended September 30, 2011 was A\$19.1 million, A\$15.4 million greater than the three months ended September 30, 2010 as costs associated with the Stage 2 expansion of the Greenbushes Lithium Operations were paid.



## 9. Discussion of Financial Position, Capital Resources and Liquidity

The table below summarizes selected financial data for Talison as at September 30, 2011, compared to the comparable financial data for Talison as at June 30, 2011, and for the Greenbushes Lithium Operations as at June 30, 2010. This financial data is derived from the Financial Statements, which were prepared in accordance with IFRS.

	As at September 30, 2011 (Unaudited) A\$'000	As at June 30, 2011 (Audited) A\$'000
<b>STATEMENT OF FINANCIAL POSITION</b>		
<b>Assets</b>		
Cash and cash equivalents .....	91,341	102,605
Trade and other receivables .....	20,884	21,543
Inventories .....	13,955	11,182
Derivative financial instruments .....	3,638	10,205
Deferred tax assets .....	-	-
Property, plant and equipment .....	111,861	95,215
Exploration and evaluation assets .....	62,346	61,714
<b>Total assets</b> .....	<b>304,025</b>	<b>302,464</b>
<b>Liabilities</b>		
Trade and other payables .....	10,377	12,380
Interest-bearing liabilities .....	31,576	29,243
Tax payable .....	2,005	-
Provisions .....	14,246	14,668
Derivative financial instruments .....	1,030	-
Deferred tax liabilities .....	8,043	10,622
<b>Total liabilities</b> .....	<b>67,277</b>	<b>66,913</b>
<b>Shareholders' equity</b> .....	<b>236,748</b>	<b>235,551</b>
	As at September 30, 2011 (Unaudited) A\$'000	As at June 30, 2011 (Audited) A\$'000
<b>Outstanding number of shares</b>		
Ordinary shares of Talison .....	110,987,326	110,527,347
Exchangeable shares of Talison Lithium Exchangeco Limited <sup>(1)</sup> .....	1,083,192	1,494,239
Shares held in trust <sup>(2)</sup> .....	(4,299,367)	(4,299,367)
<b>Total outstanding number of shares</b> .....	<b>107,771,151</b>	<b>107,722,219</b>

### Notes:

- (1) The exchangeable shares of Talison Lithium Exchangeco Limited are exchangeable (on a one-for-one basis) for ordinary shares of Talison. See "Outstanding Share Data".
- (2) On June 7, 2011, Talison Lithium established the Incentive Plan Trust. Talison Lithium issued 3,862,767 ordinary shares to the Incentive Plan Trust and the Incentive Plan Trust purchased 436,600 ordinary shares of Talison Lithium on-market.

### Cash and Cash Equivalents

Cash and cash equivalents at September 30, 2011 were A\$91.3 million, a reduction of A\$11.3 million from the balance as at June 30, 2011 due mainly to the significant investment that the Company made in the Stage 2 expansion of the Greenbushes Lithium Operations.

### Liquidity

As at September 30, 2011, Talison's cash and cash equivalents of A\$91.3 million, together with trade and other receivables of A\$20.9 million and inventories of A\$14.0 million, less trade and other payables of A\$10.4 million, placed it in a strong working capital position of A\$115.8 million.

For the three months ended September 30, 2011, Talison recorded an operating cash inflow of A\$8.2 million. At current lithium concentrate prices and US\$/A\$ exchange rates, management expects its current operations to be



cash flow positive. In the opinion of management, the working capital as at September 30, 2011, together with the expected cash flows from operations, are sufficient to support Talison's normal operating requirements, based on current production capacity, on an ongoing basis. Talison is in the process of expanding its production capacity over the next 9 months. This expansion is fully funded from Talison's existing cash reserves.

Talison's business is such that sales of lithium concentrates are made in large irregular shipments to customers. Consequently, from month to month, Talison's working capital position can fluctuate significantly as product inventories are produced in advance of shipment followed by an increase in trade debtors when the sale is made until sale proceeds are received. Talison sells to its customers on normal commercial trading terms. To accommodate these potential fluctuations at current production capacity, the Company needs to maintain sufficient working capital of approximately A\$10 – \$15 million, which in the opinion of management, it will be able to do so from its current operations. However, the increase in production capacity following the completion of the Stage 2 expansion of the Greenbushes Lithium Operations will require an increase in working capital invested. This increased investment will be funded from Talison's existing cash reserves.

Talison is currently undertaking or planning several growth projects including the Stage 2 expansion of the chemical-grade plant at the Greenbushes Lithium Operations, exploration activities at the Salares 7 Project, as well as various studies relating to Talison's proposed minerals conversion plant. These capital development projects are expected to cost approximately A\$45 – A\$55 million over the next 12 months and will be funded from the Company's existing cash reserves.

In the opinion of management, subject to the occurrence of any unforeseen event and an investment decision to construct a minerals conversion plant, the working capital as at September 30, 2011, together with the expected cash flows from operations will be sufficient to fund Talison's operations for at least the next two years.

As a result of volatility in equity markets, global uncertainty in the capital markets, potential fluctuations in the demand and pricing of lithium concentrates and cost pressures, the Company continually reviews expenditures in order to ensure adequate liquidity and flexibility to support its growth strategy.

All of the Company's existing debt facilities are in good standing. The Company's debt facilities contain certain customary covenants and undertakings in relation to financial performance, minimum liquidity and reporting. Management is not aware of any significant risks that could cause the Company to default on its existing debt facilities in the short term or long term.

### **Trade and Other Receivables**

Trade and other receivables were A\$20.9 million as at September 30, 2011. This amount consists mainly of amounts receivable from customers for the sale of lithium concentrates.

Lithium concentrate sales are made on credit terms and in some cases are secured by letters of credit or alternatively by a commercial trade debtor insurance policy. Given the fact that product shipments can be large in size and irregular in timing, the amount outstanding as trade and other receivables at any point in time can vary significantly.

### **Inventories**

Inventories on hand at September 30, 2011 totaled A\$14.0 million and consisted of finished products, ore stockpiles and spare parts and consumable stocks. Again, given the potentially large and irregular nature of product shipments, inventory levels can also vary significantly at any particular point in time. During the three months ended September 30, 2011, inventories on hand increased by A\$2.8 million in the ordinary course of operations.

### **Derivative Financial Instruments**

Derivative financial instruments represent the mark to market value of Talison's US\$ hedge book, in the form of foreign currency options, collars and forward exchange contracts (see "Financial Instruments and Other Instruments — Foreign Currency Options, Collars and Forward Exchange Contracts"). During the three months ended September 30, 2011, primarily as a result of the depreciation in the A\$ against the US\$, the mark to market value of Talison's hedge book decreased by A\$7.6 million.



## Property, Plant and Equipment

Property, plant and equipment relates to the processing plants, infrastructure and mine development which comprises the Greenbushes Lithium Operations.

Property, plant and equipment increased A\$15.6 million during the three months ended September 30, 2011 mainly due to capital expenditure at the Greenbushes Lithium Operations on the Stage 2 expansion of the chemical-grade plant.

## Exploration and Evaluation Assets

Talisson acquired the sole and irrevocable right and option to acquire up to a 70% ownership interest in a group of concessions in Region III, Chile, known as Piedra Parada, Grande, Aguilar, Agua Amarga, La Isla, Las Parinas and Maricunga (collectively the "**Concessions**") on September 22, 2010. Talisson exercised its option to acquire a 50% ownership interest in the Concessions on September 29, 2011. An additional 20% ownership interest in the Concessions can be obtained upon completion, at Talisson's sole expense, of a feasibility study on the Concessions by September 29, 2013.

## Trade and Other Payables

During the three months ended September 30, 2011, trade and other payables decreased by A\$2.0 million to A\$10.4 million. Trade and other payables fluctuate from period to period in the ordinary course of operations.

## Interest Bearing Liabilities

The interest bearing liabilities consist mainly of a US\$30 million senior secured loan with the Commonwealth Bank of Australia ("**CBA**"). The loan is for a three year term and is repayable in installments of US\$1.5 million on each of December 31, 2011 and June 30, 2012, quarterly installments of US\$1.75 million from December 31, 2012 to September 30, 2013 inclusive, and a final payment of US\$20 million on December 31, 2013. The loan is provided on commercial terms at an interest rate of LIBOR plus a margin of 3.5% and is fully secured over the Australian assets of Talisson.

In addition, Talisson has a bank guarantee facility provided by CBA for A\$5.2 million under which CBA agrees to issue bank guarantees on behalf of Talisson. Talisson pays a fee of 1.5% of the face value of the bank guarantees issued and the facility is fully secured over the Australian assets of Talisson. As at September 30, 2011, the facility was drawn to A\$4.8 million with the majority of the guarantees issued to secure Talisson's rehabilitation obligations in relation to the Greenbushes Lithium Operations. This facility does not constitute an interest bearing liability until a bank guarantee is called; as such, it is not included in the balance of interest bearing liabilities in the Company's Statement of Financial Position.

## Provisions

Provisions include employee leave entitlements and rehabilitation obligations in relation to the Greenbushes Lithium Operations and have reduced by A\$0.4 million during the three months to September 30, 2011 mainly as a result of payment of the annual short term incentive. The rehabilitation obligations are partially secured by bank guarantees referred to above.

## Contractual Obligations

### Payments due by period as at September 30, 2011

	Total	Less than	1 to 3	4 to 5	After 5
	A\$'000	1 Year	Years	Years	Years
	A\$'000	A\$'000	A\$'000	A\$'000	A\$'000
Senior secured debt.....	33,024	4,179	28,845	-	-
Operating leases.....	2,575	639	744	663	529
Insurance premium funding.....	615	615	-	-	-
Financing leases.....	761	330	340	91	-
Asset retirement obligations.....	16,411	-	-	-	16,411
<b>Total contractual obligations</b> .....	<b>53,386</b>	<b>5,763</b>	<b>29,929</b>	<b>754</b>	<b>16,940</b>



## Shareholders' Equity

Talison's total shareholders' equity as at September 30, 2011 was A\$236.7 million.

Details of the Company's equity instruments are contained in Note 13 of the Financial Statements.

## 10. Financial Instruments and Other Instruments

### Foreign Currency Options, Collars and Forward Exchange Contracts

The sales revenue of Talison is mainly denominated in U.S. dollars. Given the predominately Australian dollar cost base of the business and a main functional currency of Australian dollars, these U.S. dollar sales create a foreign exchange exposure in terms of earnings and cash flow. A one cent movement in the US\$/A\$ exchange rate affects annual pre-tax earnings and cash flows, before the effects of any hedging, by approximately A\$1 million per year. In order to hedge against this exposure, Talison enters into foreign currency options, collars and forward exchange contracts to sell U.S. dollars and receive Australian dollars.

The objective of entering into these derivative contracts is to manage this currency risk and provide increased certainty on earnings and cash flows over the next 36 months. The general strategy employed is to hedge between 50 and 85% of forecast U.S. dollar sales revenues for the next 12 months, followed by a lower level of hedging for the subsequent 24-month period. As at September 30, 2011, Talison has hedged 60% and 44% of its U.S. dollar exposure for the period from October 2011 to September 2012 and from October 2012 to August 2014, respectively, with a combination of purchased currency options at an average exchange rate of US\$0.99, currency collars with an average cap exchange rate of US\$1.06 and an average floor exchange rate of US\$0.87, forward exchange contracts at an average exchange rate of US\$0.93 and offsetting U.S. dollar costs which provide a natural hedge.

These derivative contracts are hedging highly probable forecast sales. The foreign currency options, collars and forward exchange contracts are timed to mature when receipts from customers are expected to be received. Talison purchases the foreign currency options by paying an upfront premium. The foreign currency options give Talison the right, but not the obligation, to sell U.S. dollars in the future. As such, the maximum risk to Talison is that the options will expire unexercised and therefore a loss equal to the premium paid is realized. Talison manages this risk by firstly not hedging 100% of forecast revenues and secondly carefully monitoring and reviewing the maturity date of the foreign currency options to ensure they match the expected timing of future sales receipts.

By entering into foreign currency collars Talison has the right to sell U.S. dollars at a predetermined time and at a predetermined US\$/A\$ exchange rate (the exchange rate cap) and the obligation to sell U.S. dollars at a predetermined time and at a predetermined US\$/A\$ exchange rate (the exchange rate floor). Talison enters into zero cost collars and as such does not pay or receive a premium on entry into the collar.

By entering into forward exchange contracts Talison has the right and the obligation to sell U.S. dollars at a predetermined time and at a predetermined US\$/A\$ exchange rate.

The risk to Talison under both foreign currency collars and forward exchange contracts is that, depending on the US\$/A\$ exchange rate when the instruments mature, Talison may have the obligation to sell U.S. dollars at a US\$/A\$ exchange rate that is less favourable to the prevailing spot US\$/A\$ exchange rate. Also a further risk to Talison is that at the time the instruments mature, Talison may not hold sufficient U.S. dollars to meet its sale obligation. Talison manages this risk firstly by not hedging greater than 30% of forecast revenues by a combination of foreign currency collars and forward exchange contracts and secondly carefully monitoring and reviewing the maturity date of the instruments to ensure they match the expected timing of future sales receipts.

At each reporting date, the outstanding foreign currency options, collars and forward exchange contracts are valued at fair value and reported in the balance sheet of Talison as a current asset or liability. The fair value of the foreign currency options, collars or the forward exchange contracts represents the price at which the foreign currency options could be exchanged or the foreign currency collars or forward exchange contracts could be settled in an orderly market, in an arm's length transaction between knowledgeable and willing parties who are under no compulsion to act. In the case of currency options and collars the fair value is determined using an option pricing model with the key input assumptions being the exercise price of the options and collars, the option and collar period and the market volatility. As the foreign currency options give Talison the right, but not the obligation, to sell U.S. dollars in the future, the fair value of the foreign currency options cannot be negative and will therefore never result in a liability being recorded on the balance sheet.



Talison has adopted hedge accounting for derivatives entered into since March 2011. Where a hedging relationship has been designated between a derivative contract and a highly probable forecast sale, unrealized gains or losses on the effective portion of the derivative are recorded in other comprehensive income as part of net changes in fair value of cash flow hedges and are deferred in equity until the forecast sale occurs, at which point the gain or loss is recognized in the income statement as sales revenue. Gains or losses on the derivative contract that occur after the sale takes place are recognized in the income statement as part of net finance income / (expense).

For derivatives that economically hedge transactions denominated in foreign currencies entered into prior to March 2011 hedge accounting has not been applied and therefore, all changes in the fair value of these derivatives are recorded in the income statement as part of net finance income / (expense).

During the three months ended September 30, 2011, a gain of A\$0.3 million on U.S. dollar hedging was recorded as sales revenue (three months ended September 30, 2010: nil) and a net realized gain on U.S. dollar hedging of A\$2.0 million (three months ended September 30, 2010: realized loss of A\$0.04 million) was recorded as part of net finance income / (expense).

During the three months ended September 30, 2011, in relation to US\$ hedging, Talison recorded a net fair value loss of A\$4.9 million. The net fair value of foreign currency options, collars and forward exchange contracts outstanding at the reporting date and recorded as either a current asset or current liability in the balance sheet as of September 30, 2011 was A\$2.6 million.

## 11. Related Party Transactions

Talison has entered into the following related party transactions:

### Remuneration of Directors and Key Management Personnel

The remuneration of directors and key management are recorded at cost through the income statement as incurred. The remuneration of directors and key management of Talison totaled approximately A\$1.3 million for the three months ended September 30, 2011. This includes the fair value of equity instruments recognised as a share-based payment expense during the period.

### Granting of Equity Instruments to Directors and Key Management Personnel

The granting of equity instruments to directors and key management are recorded at fair value through the income statement over the period in which the equity instruments vest. The following table provides details on equity instruments, in the form of options to purchase fully paid ordinary shares in Talison, issued to directors and key management during the period:

	Three Months Ended September 30, 2011
Options outstanding at the beginning of the period.....	3,114,589
Options granted during the period.....	-
Options forfeited during the period.....	-
Options outstanding at the end of the period .....	<u>3,114,589</u>
Outstanding options which have vested as at the end of the period .....	<u>1,147,922</u>

## 12. Outstanding Share Data

As at November 10, 2011, Talison had outstanding one class of ordinary shares (the “**Ordinary Shares**”) and one special voting share (the “**Special Voting Share**”). As at November 10, 2011, Talison had outstanding 111,462,409 Ordinary Shares. In addition, as at November 10, 2011, 6,455,043 Ordinary Shares are issuable upon the exercise of Talison’s outstanding options, and 500,896 Ordinary Shares are issuable upon the exercise of Talison’s outstanding warrants.

The Special Voting Share was issued to Computershare Trust Company of Canada on September 22, 2010 in connection with the Plan of Arrangement. Computershare Trust Company of Canada serves as trustee in voting matters on behalf of the holders of exchangeable shares (the “**Exchangeable Shares**”) of Talison Lithium Exchangeco Limited (“**Exchangeco**”), an indirect wholly-owned subsidiary of Talison. The Exchangeable Shares were issued on September 22, 2010 in conjunction with the Plan of Arrangement to certain former holders of common shares of Salares that had the right to elect to receive Exchangeable Shares in lieu of Ordinary Shares.



The Special Voting Share provides a mechanism through which the holders of Exchangeable Shares (other than Talison and its affiliates) may exercise voting rights with respect to Talison. The Exchangeable Shares (other than Exchangeable Shares held by Talison and its affiliates) are intended to be substantially the economic equivalent of the Ordinary Shares and (a) have the same voting rights, dividend entitlements and other attributes as the Ordinary Shares, (b) are exchangeable, at each holder's option, on a one-for-one basis into Ordinary Shares, and (c) will automatically be exchanged for Ordinary Shares three years from closing of the Plan of Arrangement and earlier than three years in certain limited circumstances. As at November 10, 2011, 608,108 Exchangeable Shares are exchangeable (on a one-for-one basis) for Ordinary Shares.

### 13. Non-IFRS Performance Measures

Talison uses EBITDA as a key metric in assessing its operating performance. EBITDA represents Talison's profit / (loss) before the effect of interest, taxes and depreciation and amortization. Management of Talison believes EBITDA is a useful measure of the operating performance of the business as it excludes the effect that changes in financial structure has on Talison's performance. EBITDA is not a defined financial measure according to IFRS and does not have any standardized meaning prescribed by IFRS. Therefore, this measure may not be comparable to a similar measure used by other enterprises. This measure should not be considered an alternative to net profit / (loss), cash flow from operating activities or other measures of financial performance calculated in accordance with IFRS. Rather, EBITDA is provided as additional information to complement IFRS measures by providing further understanding of the results of operations from management's perspective.

EBITDA is calculated by adding net finance expense / (income), income tax expense / (benefit) and depreciation and amortization to net profit / (loss). The following table reconciles EBITDA with net profit / (loss) for the periods indicated.

<b>INCOME STATEMENT</b>	<b>Three Months Ended September 30, 2011 (Unaudited) A\$'000</b>	<b>Three Months Ended September 30, 2010 (Unaudited) A\$'000</b>	<b>Twelve Months Ended June 30, 2011 (Audited) A\$'000</b>
Net profit / (loss) .....	1,607	5,874	22,936
Add:			
Net finance expense / (income) .....	3,083	(5,617)	(11,406)
Income tax expense / (benefit) .....	748	3,693	9,108
Depreciation and amortization .....	688	820	3,428
EBITDA .....	6,126	4,770	24,066

### 14. Subsequent Events

No matters have arisen in the interval between the end of the interim period ended September 30, 2011 and the date of this MD&A regarding any items, transactions or events of a material and unusual nature which will significantly affect the operations of Talison in the future years.

### 15. Critical Accounting Estimates

IFRS requires Talison to make estimates and assumptions that affect the amounts reported in the financial statements and related notes.

Accounting estimates and assumptions are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

Talison makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom equal the related actual results. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below.

#### Deferred Waste Mining Costs

Talison capitalizes the costs associated with the removal of waste rock using a life of mine waste-to-ore strip ratio. Costs of mining of waste rock, in excess of the life of mine waste-to-ore strip ratio, are accumulated and classified as property, plant and equipment. Significant judgment is required in determining the life-of-mine strip ratio. Factors that will affect this ratio include future changes in pit design, cost structures, product price, ore



grade and recoveries against modeled grades and recoveries. When these factors change or become known in the future, such differences will impact the deferred stripping costs in property, plant and equipment in the period in which they change or become known.

### Rehabilitation and Mine Closure Provisions

Rehabilitation and mine closure provisions represent the discounted value of the present obligation to restore, dismantle and rehabilitate certain items of property, plant and equipment. The discounted value reflects a combination of management's assessment of the cost of performing the work required, the timing of the cash flows and the discount rate.

A change in any, or a combination of, the three key assumptions used to determine the provisions could have a material impact to the carrying value of the provision. In the case of provisions for assets which remain in use, adjustments to the carrying value of the provision are offset by a change in the carrying value of the related asset. Where the provisions are for assets no longer in use or for obligations arising from the production process, the adjustment is reflected directly in the income statement.

### Reserves

Reserves are estimates of the amount of mineral product that can be economically extracted from Talison's properties. In order to calculate reserves, estimates and assumptions are required about a range of geological, technical and economic factors, including quantities, grades, production techniques, recovery rates, production costs, future capital requirements, short and long-term commodity prices and exchange rates.

Estimating the quantity and/or grade of reserves requires the size, shape and depth of ore bodies to be determined by analyzing geological data. This process may require complex and difficult geological judgments and calculations to interpret the data.

Talison determines and reports ore reserves in accordance with the Australasian Code for Reporting of Exploration Results, Mineral Resources and Ore Reserves (the "**JORC Code**") and the standards prescribed by National Instrument 43-101. The JORC Code and National Instrument 43-101 require the use of reasonable investment assumptions to calculate reserves. Due to the fact that economic assumptions used to estimate reserves change from period to period, and geological data is generated during the course of operations, estimates of reserves may change from period to period. Changes in reported reserves may affect Talison's financial results and financial position in a number of ways, including:

- asset carrying values may be impacted due to changes in estimated future cash flows;
- depreciation and amortization charged in the income statement may change where such charges are calculated using the units of production basis;
- decommissioning, site restoration and environmental provisions may change where changes in estimated reserves after expectations about the timing or cost of these activities; and
- depreciation and amortization of mining assets is prospectively adjusted, based on these changes.



## 16. Accounting Policies

### Hedge Accounting

Under the existing accounting policy applicable to derivatives (AASB 139 *Financial Instruments: Recognition and Measurement*), Talison is able to recognize derivatives at fair value through profit and loss, or apply hedge accounting. Talison has chosen to apply hedge accounting for derivatives entered into from March 2011 onwards. The ability to recognize the change in the fair value of derivative hedging instruments, designated and effective as cash flow hedges, in other comprehensive income, results in the matching of gains or losses on derivative instruments with the underlying hedged transaction being sales revenue, subject to meeting the relevant hedge accounting criteria. During the three months ended September 30, 2011, Talison recognized a loss of A\$2.1 million, net of tax, on the revaluation of designated and effective cash flow hedges in other comprehensive income. Had Talison not adopted hedge accounting for derivatives entered into during the three months ended September 30, 2011 this loss would have been recognized in NPAT.

On initial designation of a hedge, Talison formally documents the relationship between the hedging instrument(s) and hedged item(s), including the risk management objectives and strategy in undertaking the hedge transaction, together with the methods that will be used to assess the effectiveness of the hedging relationship. Talison makes an assessment, both at the inception of the hedge relationship as well as on an ongoing basis, on whether the hedging instruments are expected to be "highly effective" in offsetting the changes in the cash flows of the respective hedged items during the period for which the hedge is designated, and whether the actual results of each hedge are within a range of 80-125 percent. For a cash flow hedge of a forecast transaction, the transaction should be highly probable to occur and should present an exposure to variations in cash flows that could ultimately affect reported net income.

Changes in the fair value of the derivative hedging instrument designated as a cash flow hedge are recognized in other comprehensive income to the extent the hedge is effective. To the extent that the hedge is ineffective, changes in fair value are recognized immediately in the income statement.

If the hedging instrument no longer meets the criteria for hedge accounting, expires or is sold, terminated or exercised, or the designation is revoked then hedge accounting is discontinued prospectively. The cumulative gain or loss previously recognized in other comprehensive income and presented in the hedging reserve in equity remains there until the forecast transaction impacts the income statement, at which point the cumulative gain or loss is released to the income statement. If the forecast transaction is no longer expected to occur, then the balance in other comprehensive income is recognized immediately in the income statement.

## 17. Additional Disclosures

### Corporate Responsibility and Financial Reports

Talison's Chief Executive Officer and Chief Financial Officer are responsible for establishing and maintaining Talison's disclosure controls and procedures. Access to material information with respect to Talison is facilitated by the small size of Talison's senior management team.

### Disclosure Controls and Procedures

Talison's disclosure controls and procedures are designed to provide reasonable assurance that all relevant information is communicated to senior management, including the Chief Executive Officer and Chief Financial Officer, to allow timely decisions regarding required disclosure.

An evaluation of the effectiveness of Talison's disclosure controls and procedures was conducted as of November 10, 2011. Based on the results of that evaluation, the Chief Executive Officer and Chief Financial Officer have concluded that Talison's disclosure controls and procedures are adequate and effective to ensure that (i) material information relating to Talison is made known to them by others, particularly during the current interim period, and (ii) information required to be disclosed by Talison in its annual filings, interim filings or other reports filed or submitted by Talison under applicable securities legislation is recorded, processed, summarized and reported within the time periods specified in securities legislation. There have not been any changes in Talison's disclosure controls and procedures during the three months ended September 30, 2011 that have materially affected, or are reasonably likely to materially affect, its disclosure controls or procedures.



## Internal Controls over Financial Reporting

Talison's internal controls over financial reporting are designed to provide reasonable assurance regarding the reliability of Talison's financial reporting and the preparation of financial statements in compliance with IFRS. Talison's internal control over financial reporting includes policies and procedures that:

- pertain to the maintenance of records that in reasonable detail accurately and fairly reflect the transactions and dispositions of the assets of Talison;
- are designed to provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with IFRS and that receipts and expenditures of Talison are being made only in accordance with authorizations of management and directors of Talison; and
- are designed to provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or dispositions of Talison's assets that could have a material effect on Talison's annual and interim financial statements.

Management of Talison, including the Chief Executive Officer and Chief Financial Officer, conducted an evaluation of the effectiveness of Talison's internal controls over financial reporting as of November 10, 2011. Based on this evaluation, management has concluded that Talison's internal controls over financial reporting were effective. There have not been any changes in Talison's internal controls over financial reporting during the three months ended September 30, 2011 that have materially affected, or are reasonably likely to materially affect, its internal controls over financial reporting.

## Limitations of Controls and Procedures

Talison's management, including the Chief Executive Officer and Chief Financial Officer, believe that any disclosure controls and procedures or internal control over financial reporting, no matter how well conceived and operated, can provide only reasonable and not absolute assurance that the objectives of the control system are met. Further, the design of a control system reflects the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, they cannot provide absolute assurance that all control issues and instances of fraud, if any, within Talison have been prevented or detected. These inherent limitations include the realities that judgments in decision-making can be faulty, and that breakdowns can occur because of simple error or mistake. Additionally, controls can be circumvented by the individual acts of some persons, by collusion of two or more people, or by unauthorized override of the control. The design of any system of controls also is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions. Accordingly, because of the inherent limitations in a cost effective control system, misstatements due to error or fraud may occur and not be detected.

## Legal Proceedings, Disputes and Regulatory Actions

Talison may be involved in legal proceedings from time to time, arising in the ordinary course of its business. Typically, the amount of ultimate liability with respect to these actions will not, in the opinion of management of Talison, materially affect Talison's financial position, statement of income or cash flows.

In assessing loss contingencies relating to legal proceedings that are pending against Talison (if any) or unasserted claims that may result in any such proceedings (if any), Talison and its legal counsel will evaluate the perceived merits of any legal proceedings or unasserted claims as well as the perceived merits of the amount of relief sought or expected to be sought. If the assessment of a contingency suggests that a material loss is probable, and the amount can be reliably estimated, then a loss will be recorded. If a contingent loss is not probable but is reasonably possible, or is probable but the amount of loss cannot be reliably estimated and may be material, then details of the contingent loss will be disclosed. Loss contingencies considered remote will generally not be disclosed unless they involve guarantees, in which case Talison will disclose the nature of the guarantees. Legal fees incurred in connection with pending legal proceedings will be expensed as incurred.

## 18. Cautionary Notes

### Risk Factors

This MD&A should be read in conjunction with detailed risk factors included under the heading "Risk Factors" in the Annual Information Form, which risk factors are incorporated by reference into this MD&A and which can be found on Talison's SEDAR profile at [www.sedar.com](http://www.sedar.com).



## Forward-Looking Statements

Certain information contained or incorporated by reference in this MD&A, including any information regarding Talison's strategy, projects, plans, prospects, future outlook, anticipated events or results or future financial or operating performance, constitutes "forward-looking statements" within the meaning of Canadian securities laws. All statements, other than statements of historical fact, are forward-looking statements. Forward-looking statements can often, but not always, be identified by the use of words such as "plans", "expects", "budget", "scheduled", "estimates", "forecasts", "intends", "anticipates", "predicts", "potential", "continue" or "believes", or variations (including negative variations) of such words; or statements that certain actions, events or results "may", "could", "would", "should", "might", "potential to", or "will" be taken, occur or be achieved or other similar expressions concerning matters that are not historical facts. The purpose of forward-looking statements is to provide the reader with information about management's expectations and plans for 2012 and subsequent financial years.

Forward-looking statements are necessarily based on a number of factors, estimates and assumptions that, while considered reasonable by Talison, are inherently subject to significant business, economic and competitive uncertainties and contingencies. Such factors, estimates and assumptions include, but are not limited to, anticipated financial or operating performances of Talison, its subsidiaries and their respective projects; future prices of lithium and/or lithium concentrates; the estimation of mineral reserves and resources; the realization of mineral reserve estimates; the timing and amount of estimated future production; estimated costs of future production; the grade, quality and content of the concentrate produced; the sale of production and the performance of offtakers; capital, operating and exploration expenditures; costs and timing of the development of the Greenbushes Lithium Operations and the Salares 7 Project, the costs of Talison's hedging policy; costs and timing of future exploration; requirements for additional capital; government regulation of exploration, development and mining operations; environmental risks; reclamation and rehabilitation expenses; title disputes or claims; the successful integration of Salares; and limitations of insurance coverage. While Talison considers these assumptions to be reasonable based on information currently available to it, they may prove to be incorrect and actual results may vary.

Readers are cautioned that forward-looking statements involve known and unknown risks, uncertainties and other factors which may cause the actual results, performance or achievements of Talison and/or its subsidiaries to be materially different from any future results, performance or achievements expressed or implied by the forward-looking statements. These risks, uncertainties and factors are discussed in the Financial Statements, and in the Annual Information Form, each of which can be found on Talison's SEDAR profile at [www.sedar.com](http://www.sedar.com). Readers are cautioned that forward-looking statements are not guarantees of future performance. All of the forward-looking statements made or incorporated in this document are qualified by these cautionary statements.

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