PILBARA MINERALS LIMITED

$100m Raised; Increasing Price Target to 95c

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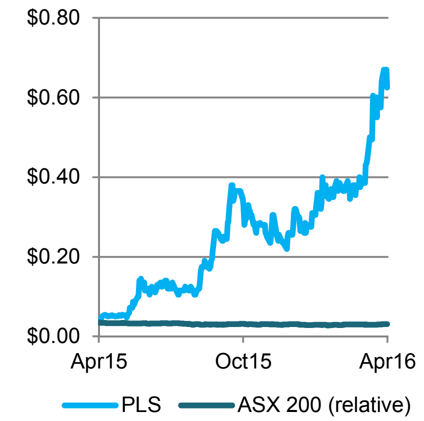
Date 27 April 2016

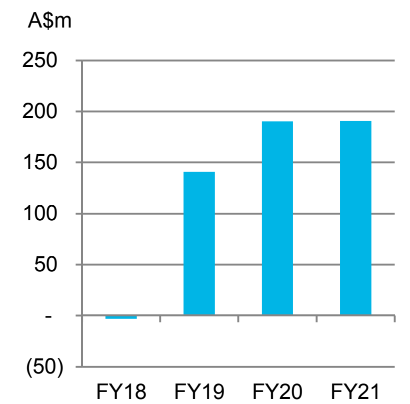
We say	Price	Target	Strategic Target
BUY	**0.63**	**0.95**	**2.20**

Earlier this month Pilbara raised $100m in new equity at 38c, securing ~50% of the funds required to build its world class Pilgangoora lithium project in WA. We expect the balance of project funding to come from debt and offtake finance, likely to be finalised in Q4 2016. Pilbara is on track to complete its DFS at Pilgangoora in Q3 2016 and remains our top pick in the ASX lithium space and we increase our price target to 95c (from 80c) an implied return of over 50%.

PLS SHARE PRICE (A$)



FORECAST EBITDA (VS. CAPEX $185M)



COMPANY DATA

Enterprise value	A$642m
Diluted market cap*	A$748m
Diluted shares*	1,187m
Free float	100%
12 month price range	0.03-0.70
GICS sector	Materials

Management holds ~9% (fully diluted)
* Diluted for 56m options

IMPLIED RETURN

Total expected return	51%

FUNDING & DEVELOPMENT

We estimate a funding need of A$210m to build Pilgangoora: A$185m initial capex and A$25m working capital. With its $100m raising complete, we expect the remaining $110m in funding to come from debt and offtake finance. A DFS for Pilgangoora is due in Q3 CY16 and plant construction is due to begin in Q1 2017. Post a 12-month build, first production is due in Q1 2018.

VALUATION SENSITITVITY

Our 95c base case valuation has an implied return of 51% and is based on a 2mtpa throughput rate, a spodumene price of US$600/t and 20% discount to NPV for development risk.
Our $2.20 Strategic Target has an implied return of ~250% and is based on an expanded 3mtpa plant (for additional capex of A$90m) spodumene prices of US$800/t and no discount to NPV.

THE GO-TO ASX LITHUM NAME IN OUR VIEW

Given the sheer *scale* advantage of the Pilgangoora resource compared to its ASX spodumene peers, PLS's low-risk jurisdiction in WA, and the lower technical risks associated with spodumene projects (compared to their brine counterparts), we believe Pilbara Minerals is likely to have *superior appeal* with global institutional investors.

PLS: OUR TOP PICK IN THE ASX LITHIUM SPACE

MACRO: WHY LITHIUM?

In our view, the outlook for lithium demand is very promising, driven by the accelerating uptake of Electric Vehicles (EVs) and static power storage for both grid and domestic applications.

While no one really knows when EVs will reach a tipping point into mainstream adoption, most industry participants believe it is likely to be sometime in the next few years, and could be sooner rather than later, driven by:

- The rapidly falling cost of EVs (several models at ~US$30-35k and lower in China)
- The huge number of new EV models in development by car manufacturers
- A rapidly growing list of government policies, tax breaks and incentives for EVs and static storage driven by environmental considerations and the need to reduce emissions
- Complementary applications for static storage in renewable energies like solar and wind power, which have the potential to make these power sources viable as *base-load* power (previously one of the *key* impediments for renewable energy applications)

STOCK SPECIFIC: WHY PILBARA MINERALS?

For investors looking for exposure to this attractive macro thesis, there are relatively limited options on the ASX. In our view Pilbara Minerals (PLS) has all the key ingredients to become to "go-to name" in the ASX lithium space for institutional investors, which it is why it remains our Top Pick in the space.

We believe institutional investors will gravitate towards Pilbara Minerals due to:

1) **Pilgangoora's Best-in-Class Scale**
   - **Pilgangoora is the largest and close to the highest grade undeveloped spodumene deposit globally**. The project has an 80mt resource with an Exploration Target of ~105mt due mid CY16. If the exploration target is achieved Pilgangoora's resource will be ~3x larger than the next largest spodumene resource owned by an ASX lithium company (~36mt)
2) **Low Capex, Low Opex**
   - Spodumene projects are typically lower capex than their brine counterparts
   - While spodumene projects tend to be higher opex, Pilgangoora's scale, low strip and stacked mineralisation mean it is likely to be one of the lowest cost spodumene producers globally. On our estimates Pilgangoora's costs are likely to be around the 50% percentile on the global cost curve and perhaps better
3) **Low-Risk Development**
   - Spodumene projects tend to be lower technical risk than their brine counterparts
4) **Low-Risk Jurisdiction**
   - WA was recently voted the #1 jurisdiction globally for mining investment by the Fraser Institute. Pilgangoora carries considerably lower permitting & sovereign-risk than its brine counterparts in South America (Argentina #71, Chile #11)
5) **Owns 100% of Asset**
   - The ASX lithium space is characterised by fragmented ownership. PLS still owns 100% of its asset, and as such retains considerable corporate appeal in our view.

PROJECT FUNDING

On 7 April 2016, Pilbara Minerals confirmed it had completed an A$100m equity raising at 38c per share comprising:

- A$85m placement to institutional investors (heavily oversubscribed)
- A$15m fully underwritten Share Purchase Plan (SPP)

Post the completion of this raising Pilbara expects to have A$106m in cash.

The table below summarises our revised base case assumptions for the financing plan to develop Pilgangoora:

Pilgangoora Financing Plan (Base Case)

Funding Uses	A$m
Initial Capex	185
Working Capital	25
Total	**210**

Funding Sources		A$m
Equity	48%	100
Offtake Finance	-	-
Debt	52%	110
Total		**210**

Source: Company, Blue Ocean

Given the recent strength in demand for spodumene offtake, we believe offtake finance is also likely to form part of the financing plan for Pilgangoora.

In early March 2016, General Mining (ASX:GMM) confirmed it had locked in offtake for CY16 production from its 50%-owned Mt Cattlin project in WA at US$600/t (for a 5.5% Li_2O concentrate), but more importantly, the two Chinese offtakers paid for 50% of this offtake **upfront**.

We believe PLS should be able to secure offtake finance of *at least A$50m* for Pilgangoora, which would reduce the debt funding need to A$60m or 29% of project funding.

Development Timetable: Pilbara plans to complete a DFS for Pilgangoora by Q3 CY16 and to begin early site works in Q4 2016, with plant construction to begin in Q1 2017. Construction is expected to take ~12 months, leading to first production in Q1 CY18.

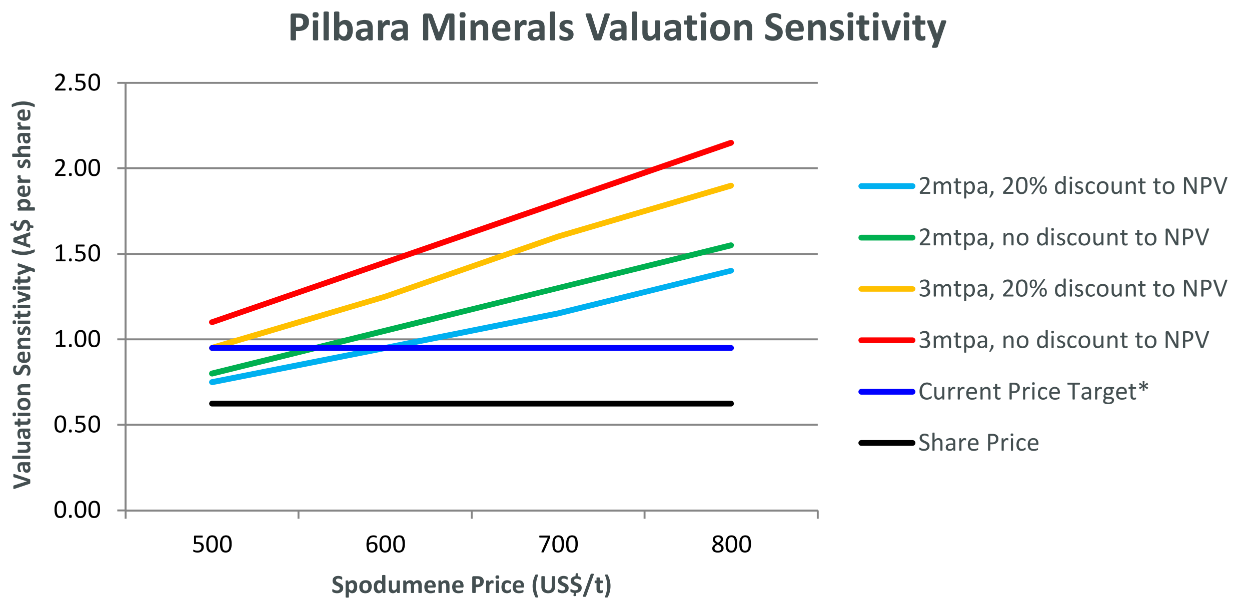
NEAR-TERM CATALYSTS

The key near-term catalysts for Pilbara Minerals are:

(1) **Ongoing drill results**: 15,000m drill programme underway (4 RC rigs + 1 DD rig)
(2) **Mid 2016**: Resource upgrade due. Exploration Target 100-110mt at 1.2-1.5% Li_2O
(3) **Q3 2016**: Definitive Feasibility Study due for Pilgangoora

VALUATION SENSISITIVTY

The chart and table below summarise our valuation sensitivity for Pilbara Minerals at a range of spodumene prices, at throughput rates of 2mtpa & 3mtpa and with and without a 20% discount to NPV for development risk.



Source: Blue Ocean Estimates. Based on NPV using 8% nominal discount rate (or 6% real)
All scenarios use the A$/U$ forward curve from Bloomberg: Spot of 0.77 falling to 0.67 over 5 years
*Current Price Target based on US$600/t spodumene price and 20% discount to NPV for development risks

Pilbara Minerals Valuation Sensitivity and Implied Returns

			With a 20% discount to NPV*		With no discount to NPV	
	Plant	Price (US$/t)	Price Target (A$)	Implied return	Price Target (A$)	Implied return
Base case	2mtpa	500	0.75	20%	0.80	27%
		600	0.95	51%	1.05	67%
		700	1.15	83%	1.30	107%
		800	1.40	123%	1.55	147%
Expanded	3mtpa	500	0.95	51%	1.10	75%
		600	1.25	99%	1.45	131%
		700	1.60	155%	1.80	187%
		800	1.90	203%	2.15	243%

Source: Blue Ocean Equities. *Allowing for development risks

LATEST LITHIUM PRICES

Lithium prices continue to be relatively opaque, but according to Asian Metals, April has seen continued tightness and higher prices in lithium carbonate and lithium hydroxide markets in China. Asian Metals also expects this trend is expected to continue near term. The latest prices according to Asian Metals on 18 April were:

- Lithium carbonate prices: US$26-27k/t for 99.5%, US$21-23k/t for 99%
- Lithium hydroxide prices: US$28-29k/t for battery grade, US$26-28k/t for industrial grade

MARGINS OF LITHIUM CONVERTERS IN CHINA

The slide below, from Orecobre's (ASX:ORE) latest investor presentation, provides an interesting look at the cost of converting a 5.5% Li_2O spodumene into lithium carbonate.

To us this suggests the lithium carbonate convertors are currently making *substantial* margins, suggesting potential for higher spodumene prices. i.e.:

- **Current Margins**: Using General Mining's (ASX:GMM) offtake agreement in early March at US$600/t. If the Chinese lithium convertors are achieving prices of, say US$22k/t (assuming these prices are being achieved for decent volumes) this implies healthy margins of 62% based on a cost to mine gate from the slide below of US$8,440/t.
- **Long Term Prices?** Most investors agree that lithium carbonate prices are likely to pull back at some point from US$22k/t towards US$12-14k/t. But even at US$12k/t, according to the slide below, lithium convertors would still be making 19% margins at a spodumene price of US$750/t. i.e. **On this basis, in our view, a long term spodumene price of US$750/t appears potentially viable**

SPODUMENE CONCENTRATE CONVERSION COST PROVIDES PRICING BENCHMARK

ITEM	USD/TONNE	USD/TONNE	USD/TONNE
US$/t 5.5% Li2O Concentrate	450	600	750
Conversion Recovery	85%	85%	85%
Tonnes of 5.5% Li2O Concentrate at 85% recovery	8.65	8.65	8.65
Input Cost of Concentrate	3,892	5,190	6,487
Freight/insurance etc	250	250	250
Conversion Cost	3,000	3,000	3,000
Cost per tonne of lithium carbonate at plant gate in China	7,142	8,440	9,737

Recently announced spodumene concentrate prices supports Chinese price excluding taxes of >US$8500/t

OROCOBRE LIMITED 16

Source: Orecobre Investor Presentation, 19 April 2016

PRICE TARGET & RATING

We increase our price target to $0.95 (from $0.80) based on ~1.0x our 20% risk-adjusted NPV representing an implied return of over 50%.

The main changes to our forecasts since last publish were:

- Updating our forecasts for the $100m raising at 38c
- Reducing the discount applied to our NPV from 30% to 20% on completion of the major raising (a key de-risking milestone)
- Increasing our spodumene prices ~6% to US$600/t (from US$565/t) on the back of a continued rally in lithium prices since we last published and confirmation that General Mining (ASX:GMM) achieved a CY16 contract price of US$600/t.
- Increasing our notional exploration value from A$50m to A$100m in recognition of the *scalability* of Pilgangoora. Our base case forecasts assume a 20 year mine life at 2mtpa rate, or a 40mt mining inventory – ***representing only <u>half</u> the current 80mt resource***. Pilgangoora also has an Exploration Target of 100-110mt.

STRATEGIC TARGET

Our $2.20 Strategic Target for Pilbara minerals is primarily based on:

- Expanding the Pilgangoora plant from 2mtpa to 3mtpa (for capex of ~A$90m). This assumes lithium demand is sufficient to take this additional product
- Increasing the mining inventory from 40mt in our base case to 54mt (in line with the company's target for the DFS due in Q3 2016)
- US$800/t prices for Chemical Grade spodumene (85% of production)
- US$1,000/t price for Technical Grade spodumene (15% of production)
- We also remove our 20% discount to NPV for development risks

KEY RISKS

Pilbara Minerals is exposed to all the normal risks associated with developing and operating mining projects, including permitting, funding and construction risk.

Given the early stage nature of the Pilgangoora project, other key risks for Pilbara Minerals include metallurgical recoveries as well as a successful infill drilling program.

Many investors may also expect ongoing exploration success (and in our view that is likely) and thus Pilbara Minerals also carries exploration risk.

Assuming the company makes the transition into production, the company's revenues will be derived from the sale of lithium concentrate (spodumene) and tantalum. Fluctuations in the lithium concentrate and tantalum price as well as the Australian dollar could impact the company's cash flow, profitability and share price.

Pilbara Minerals' shares also carry embedded Australian sovereign risk as the company's projects are based in Western Australia.

MODEL SUMMARY – FINANCIALS & VALUATION

Stock Details							
						Enterprise Value	$642m
Recommendation:	BUY					Diluted MCap	$748m
Target	$0.95	Share Price	$0.63	Strategic Target (ST)	$2.20	Diluted Shares	1187m
NAV	$0.96	52 Week High	$0.70	Implied Return to ST	249%	Free Float	100%
Implied Return	51%	52 Week Low	$0.03			Avg Daily Value	$2.2m

Macro Assumptions	FY16E	FY17E	FY18E	FY19E	FY20E
Exchange Rate (A$/US$)	0.73	0.72	0.68	0.68	0.67
Avg Li Conc Price (US$/t)	600	600	600	600	600
Tantalum Price (US$/lb)	55	55	55	55	55
Avg Li Conc Price (A$/t)	821	834	878	885	891
Tantalum Price (A$/lb)	75	76	81	81	82

Profit & Loss (A$m)	FY16E	FY17E	FY18E	FY19E	FY20E
Revenue	6	10	-	235	315
Operating Costs	(3)	(6)	-	(87)	(116)
Operating Profit	**2**	**4**	**-**	**148**	**199**
Corporate & Other	(6)	(1)	(3)	(4)	(4)
Exploration Expense	(2)	(3)	(0)	(3)	(5)
EBITDA	**(6)**	**(0)**	**(3)**	**141**	**190**
D&A	(3)	(5)	(0)	(10)	(14)
EBIT	**(9)**	**(5)**	**(3)**	**131**	**177**
Net Interest Expense	(1)	1	1	(9)	(1)
Pre-Tax Profit	**(10)**	**(4)**	**(2)**	**122**	**176**
Tax Expense	(0)	-	-	(37)	(53)
Underlying Profit	**(10)**	**(4)**	**(2)**	**85**	**123**
Signficant Items (post tax)	1	-	-	-	-
Reported Profit	**(9)**	**(4)**	**(2)**	**85**	**123**

Cash Flow (A$m)	FY16E	FY17E	FY18E	FY19E	FY20E
Operating Cashflow	(2)	3	(3)	144	195
Tax	(0)	-	-	-	(52)
Net Interest	(0)	1	1	(9)	(1)
Net Operating Cash Flow	**(2)**	**4**	**(1)**	**136**	**142**
Exploration	(5)	(3)	(1)	(4)	(5)
Capex	(5)	(2)	(139)	(50)	(6)
Acquisitions / Disposals	(2)	-	-	-	-
Other	-	-	-	-	-
Net Investing Cash Flow	**(12)**	**(5)**	**(139)**	**(54)**	**(11)**
Equity Issue	118	8	7	-	-
Borrowing / Repayments	4	-	110	(110)	-
Dividends	-	-	-	-	(12)
Other	-	-	-	-	-
Net Financing Cash Flow	**121**	**8**	**117**	**(110)**	**(12)**
Change in Cash Position	107	7	(24)	(28)	120
FX Adjustments	-	-	-	-	-
Cash Balance	**110**	**116**	**92**	**64**	**184**

Balance Sheet (A$m)	FY16E	FY17E	FY18E	FY19E	FY20E
Cash	110	116	92	64	184
Other Current Assets	1	1	1	1	1
PP&E	11	9	147	187	179
Exploration & Development	5	5	5	6	6
Other Non Current Assets	1	1	1	1	1
Total Assets	**128**	**133**	**247**	**259**	**371**
Debt	8	8	118	8	8
Other Liabilities	2	2	2	39	40
Net Assets	**118**	**123**	**127**	**213**	**324**

Ratio Analysis		FY16E	FY17E	FY18E	FY19E	FY20E
Diluted Shares	m	1,187	1,225	1,243	1,243	1,243
EPS - Diluted	Ac	(1.2)	(0.3)	(0.2)	6.9	9.9
P/E	x	**n.m.**	**n.m.**	**n.m.**	**9.2x**	**6.4x**
CFPS - Diluted	Ac	(0.3)	0.3	(0.1)	10.9	11.4
P/CF	x	**n.m.**	**n.m.**	**n.m.**	**5.8x**	**5.5x**
FCF - Diluted	Ac	(0.6)	0.0	(11.4)	7.5	11.1
P/FCF	x	**n.m.**	**n.m.**	**n.m.**	**8.3x**	**5.7x**
Dividends	Ac	-	-	-	-	2.0
Dividend yield	%	-	-	-	-	3.2%
Payout Ratio	%	-	-	-	-	19%
Franking	%	-	-	-	-	100%
Enterprise Value	A$m	646	639	774	692	572
EV/EBITDA	x	**n.m.**	**n.m.**	**n.m.**	**4.9x**	**3.0x**
ROE	%	(8%)	(3%)	(2%)	40%	38%
ROA	%	(8%)	(3%)	(1%)	33%	33%
Net Debt or (Cash)	A$m	(102)	(108)	26	(56)	(176)
Gearing (ND/(ND+E))	%	n.m.	n.m.	17%	(36%)	(119%)
Gearing (ND/E)	%	n.m.	n.m.	20%	(26%)	(54%)

Lithium (Li_2O)	P&P Reserves			M&I Resources			Inferred
	mt	%	cont(kt)	mt	%	cont(kt)	cont(kt)
Pilgangoora	29.5	1.31%	386	35.7	1.3%	469	539
						Total	**1,008**

Tantalum (Ta_2O_5)	P&P Reserves			M&I Resources			Inferred
	mt	ppm	cont(mlb)	mt	ppm	cont(mlb)	cont(mlb)
Pilgangoora	29.5	134	8.7	17.9	182	7.18	10.98
Tabba Tabba	0.13	1,290	0.38	0.22	1,077	0.53	0.14

Earnings Sensitivity			FY19E	FY20E	FY19E	FY20E
			A$m	A$m	%	%
Lithium conc price	US$/t	+10%	13	18	18%	16%
Tantalum price	US$/lb	+10%	1	1	1%	1%
Exchange Rate	A$/US$	-10%	15	20	20%	18%

Valuation	Discount	Stake	A$m	A$/sh
Pilgangoora (un-risked)		100%	1,150	0.97
Pilgangoora (risk-adjusted)	20%	100%	920	0.77
Exploration / Expansion		100%	150	0.13
Tabba Tabba		100%	5	0.00
Corporate & Other			(41)	(0.03)
Debt			-	-
Cash			106	0.09
Risk adjusted NAV			**1,140**	**0.96**

Source: IRESS, Company data, Blue Ocean estimates

MODEL SUMMARY – OPERATIONAL INPUTS & FCF

Macro Assumptions		FY16E	FY17E	FY18E	FY19E	FY20E
Exchange Rate	A$/US$	0.73	0.72	0.68	0.68	0.67
Chem Spodume Price	US$/t	600	600	600	600	600
Tech Spodume Price	US$/t	-	-	-	-	-
Avg Li Conc Price	US$/t	600	600	600	600	600
Tantalum Price	US$/lb	55	55	55	55	55
Realised Li Conc Price	A$/t	821	834	878	885	891
Realised Ta Price	A$/lb	75	76	81	81	82

Operational Summary		FY16E	FY17E	FY18E	FY19E	FY20E
Tabba Tabba						
Ore Milled	kt	50	83	-	-	-
Tantalum Head Grade	ppm	1,200	1,200	-	-	-
Recovery	%	70%	70%	-	-	-
Tantalum Production	**klb**	**93**	**154**	**-**	**-**	**-**
Net Cash Cost	A$/lb	37	37	-	-	-
All-in Sustaining Cost	A$/lb	41	42	-	-	-
% AISC Margin	**%**	***45%***	***45%***	**-**	**-**	**-**
Pilgangoora						
Ore Milled	mt	-	-	-	1.5	2.0
Lithium Head Grade	%	-	-	-	1.31%	1.31%
Recovery	%	-	-	-	77%	77%
Li Conc Produced	**kt**	**-**	**-**	**-**	**251**	**334**
Tantalum Head Grade	ppm	-	-	-	134	134
Recovery	%	-	-	-	47%	47%
Tantalum Production	**klb**	**-**	**-**	**-**	**206**	**275**
Net Cash Cost (post credit)	A$/t conc	-	-	-	296	296
All-in Sustaining Cost	**A$/t conc**	**-**	**-**	**-**	**327**	**328**
% AISC Margin	**%**	**-**	**-**	**-**	***63%***	***63%***

FCF Contribution	A$m	FY16E	FY17E	FY18E	FY19E	FY20E
Tabba Tabba						
Tantalum Revenue		5.8	9.7	-	-	-
Operating Costs		3.4	5.7	-	-	-
Operating Margin		**2.4**	**4.0**	**-**	**-**	**-**
Sustaining Capex		0.2	0.4	-	-	-
Sustaining Exploration		-	-	-	-	-
Corp Overheads		0.4	0.4	-	-	-
All-in Sustaining Margin		**1.8**	**3.2**	**-**	**-**	**-**
Pilgangoora						
Lithium Revenue		-	-	-	222	298
Tantalum Revenue		-	-	-	13	17
Operating Costs (ex credit)		-	-	-	87	116
Operating Margin		**-**	**-**	**-**	**148**	**199**
Sustaining Capex		-	-	-	4	6
Sustaining Exploration		-	-	-	1	1
Corp Overheads		-	-	-	4	4
All-in Sustaining Margin		**-**	**-**	**-**	**139**	**188**
Growth Capex		4	2	139	46	-

Group Operations	A$m	FY16E	FY17E	FY18E	FY19E	FY20E
Revenue		6	10	-	235	315
All-in Sustaining Cost		5	8	3	96	127
All-in Sustaining Margin		**1**	**2**	**(3)**	**139**	**188**
Growth Capex		5	2	139	46	-
Growth Exploration		4	3	1	3	4
All-in Margin		**(8)**	**(3)**	**(142)**	**90**	**184**

Corporate	A$m	FY16E	FY17E	FY18E	FY19E	FY20E
Cash Tax		0	-	-	-	52
Other Items		6	-	-	-	-
FCF pre Debt Service		**(14)**	**(3)**	**(142)**	**90**	**132**
Net Interest		0	(1)	(1)	9	1
Debt Drawdown / (Repayment)		4	-	110	(110)	-
FCF post Debt Service		**(11)**	**(1)**	**(31)**	**(28)**	**132**

New Equity/Dividends	A$m	FY16E	FY17E	FY17E	FY18E	FY20E
Proceeds from Shares/Options		118	8	7	-	-
Dividends Paid		-	-	-	-	12
Change in Cash		**107**	**7**	**(24)**	**(28)**	**120**
Cash Balance		**110**	**116**	**92**	**64**	**184**

Source: IRESS, Company data, Blue Ocean estimates

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DISCLAIMER

DISCLOSURE

Blue Ocean Equities Pty Limited, its employees, consultants and its associates within the meaning of Chapter 7 of the Corporations Law may receive commissions, underwriting and management fees from transactions involving securities referred to in this document, and may from time to time hold interests in the securities referred to in this document.

Blue Ocean Equities Pty Limited and associates hold 756,749 shares in Pilbara Minerals at the date of this report and this position may change at any time without notice.