

## Higher Nickel Prices Could Provide Impetus for Restart

### Investment Highlights

Poseidon Nickel Limited (POS) is examining options to fast track development of its 100% owned Mt Windarra Nickel mine in Western Australia. The Company is in the process of negotiating a potential ore-tolling arrangement that could allow for the low cost restart of the mine. Under this scenario the mine would generate good cashflows (~\$28mpa) which should provide a portion of the upfront capital to move the project into full production (9.6ktpa Ni). With nickel prices up 14% since the beginning of February, this provides further impetus for the restart. We maintain our Speculative Buy rating.

- Ore-Tolling Negotiations continuing:** POS has indicated that negotiations are continuing with an unnamed party for an ore-tolling arrangement which could allow for the low-cost restart of the historic Windarra nickel mine. Given that the ore would need to be trucked to a concentrator for processing, BHP's Leinster concentrator is the closest and would likely be the most economically viable. We see potential for a profitable low upfront cost toll-treating arrangement processing circa 500ktpa of 1.7% Ni ore. POS is also examining the commencement of treating surface gold tailings which could add further cashflows.
- Low Cost Development Proposition:** POS completed a DFS on the full restart of the Mt Windarra nickel mine in April 2013. The study indicated that despite the projects relatively low grade (avg 1.55% Ni), POS has the potential to mine at a similar cost per pound to the Long Nickel mine. The main reason is the vertical geometry and orientation of the Mt Windarra orebody, which allows for bulk sub-level caving. We believe that through further optimisations, the upfront capital cost of \$200m can be further reduced given the recent reduction in cost pressures in the resources market (wages, equipment, drilling etc).
- Valuation of \$0.24/sh:** The recent increase in nickel price could provide further impetus for the development of the Mt Windarra nickel mine. POS is highly leveraged to nickel price, a 10% increase in the nickel price results in a 25.6% increase to our valuation.

31 March 2014

12mth Rating

SPEC BUY

Price	A\$	0.075
Target Price	A\$	0.24
12m Total Return	%	215.3

RIC: POS.AX

BBG: POS AU

Shares o/s	m	466.3
Free Float	%	58%
Market Cap.	A\$m	35.0
Net Debt (Cash)	A\$m	39.0
Net Debt/Equity	%	96.3
3m Av. D. T'over	A\$m	0.02
52wk High/Low	A\$	0.24/0.07
2yr adj. beta		0.98

Valuation:

Methodology		DCF
Value per share	A\$	0.24

Analyst:

Simon Tonkin

Phone:

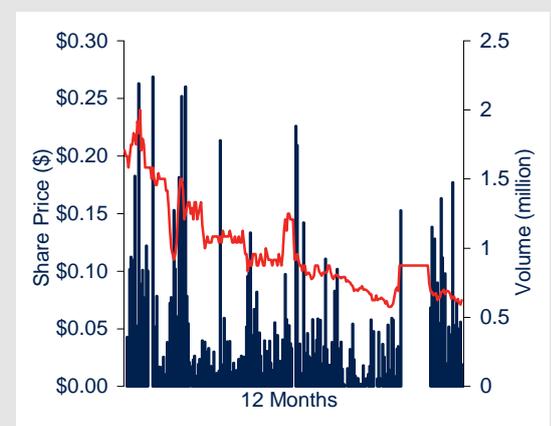
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Year End June 30	2013A	2014F	2015F	2016F
Reported NPAT (\$m)	(13.6)	(11.1)	(1.1)	(0.4)
Recurrent NPAT (\$m)	(13.6)	(14.0)	(1.1)	(0.4)
Recurrent EPS (cents)	(3.3)	(3.0)	(0.1)	(0.0)
EPS Growth (%)	na	na	na	na
PER (x)	(2.3)	(2.5)	(65.7)	(244.2)
EBITDA (\$m)	(6.7)	(4.8)	38.0	47.8
EV/EBITDA (x)	(8.9)	(14.0)	3.6	4.5
Capex (\$m)	0.0	25.3	14.5	168.8
Free Cashflow	(29.4)	(33.5)	16.2	(129.4)
FCFPS (cents)	(7.2)	(7.2)	1.6	(9.1)
PFCF (x)	(1.0)	(1.0)	4.6	(0.8)
DPS (cents)	0.0	0.0	0.0	0.0
Yield (%)	0.0	0.0	0.0	0.0
Franking (%)	0	0	0	0

### 12 Month Share Price Performance



Performance %	1mth	3mth	12mth
Absolute	-13.3	4.0	-61.0
Rel. S&P/ASX 300	-5.4	5.7	-61.1

## Key Highlights

**Offtake Arrangement to Provide Cashflow:** We see the recent announcement by POS that it is looking to negotiate an offtake agreement as positive. Based on our nickel price assumptions we estimate that the operation would generate in the order of \$28m per annum in cashflow. This would provide sufficient funding to cover corporate costs, drilling and should provide some of the upfront funding needed to move the project into full production.

Figure 1, shows the proximity of Mt Windarra to each of the West Australian nickel concentrators. The Leinster concentrator owned by BHP is the closest processing option, at 250km by sealed road, and would make the most economic sense. The Perseverance underground mine near the town of Lenister was recently placed on care and maintenance meaning there would be sufficient capacity at the concentrator to treat ore from Mt Windarra. We estimate cashflows from the ore-toll treatment arrangement could be in the order of \$28mpa based on a 500ktpa operation processing 1.7% Ni ore at our nickel price assumptions. Additional funding could also come from the processing of gold tails to produce 50koz of gold which should generate \$12-16m per annum.

Figure 1 : Proximity of Mt Windarra to Nickel Concentrators



Source: SNL Metals and Mining

**Higher Nickel Prices Provide Impetus for Development:** Nickel prices have increased 14% since the beginning of February. A sustained robust nickel price provides a greater probability that funding will be achieved and the project will be developed. Based on the DFS in April 2013 the project requires \$200m in upfront capital to develop the project. That said, costings would have been calculated at near peak levels of the resources cycle and we believe there is scope to reduce costs. However, we do see the need for working capital requirements of circa \$50m to cover the inventory supply chain as well as interest payments.

**Nickel Leverage Play:** POS has excellent leverage to nickel price with each 10% move resulting in a 25.6% movement in our valuation. Despite this POS's share price has remained relatively flat as it continues to negotiate a potential offtake arrangement. POS has completed an independent feasibility study on the restart of its 100% owned Mt Windarra Nickel project.

**Low Capital Intensity:** The capital intensity for the Mt Windarra Nickel project is relative low (US\$8/lb) when compared to other new nickel operations (US\$10-50/lb). This is due to the fact that the project has significant established infrastructure already in place. We have assumed a 70:30 debt to equity ratio for the \$200m required. We also note that POS has \$43m in debt via two convertible notes (\$35m) and an \$8m loan from its largest shareholder Andrew Forrest. The \$8m loan is due in October 2014 (although it could be extended) and the convertible notes mature in 2017.

**Low Cost Mining; Compares Favourably to West Australian Nickel Producers:** The key differentiating feature for POS in comparison to the other West Australian nickel producers, is the low cash costs considering the projects lower grades. The reason that POS is able to achieve comparatively low cost mining is due to the vertical orientation of its Mt Windarra deposit which can be mined using bulk tonnage sub-level caving. In Figure 2, we have compiled a comparison between the West Australian nickel producers/developers. Based on an EV/Margin multiple POS is trading below the average (1.47 vs. 1.80). This is favourable considering that POS has the lowest rock value of all the producers, yet its project stacks up. POS also trades at a discount to its peers on an EV/resource basis (\$0.26/lb vs. the average of \$0.41/lb).

**Figure 2 : West Australian Nickel Producer/Developer Comparatives**

Company Name	ASX Code	EV (\$m)	Main Nickel Deposit(s)	Resource (Contained Ni Eq)	Grade (Ni Eq. %)	EV/lb Res	Reserve (Contained Ni)	Grade (Ni Eq%)	EV/lb Reserve	Annual Production (Ni ore)	Mine life Reserves	Mining Method	Rock Value (\$/t)	C1 Costs (A\$/t ore)	C2 Costs (A\$/t ore)	Margin (A\$/t ore)	C1 Cost A\$/lb payable	EV/ margin (x)
Independence Group NL	IGO	914	Long	74,160	5.37%	1.63	41,900	3.7%	2.89	10,753	3.9	Long-hole open stope with paste fill as well as narrow hand	550	202	233	317	3.66	0.84
Mincor Resources NL	MCR	66	Mittel, Mariners	117,000	3.69%	0.26	21,536	3.2%	1.40	9,000	2.4	Narrow vein mining/Long-hole open stope with paste fill	471	202	282	188	4.55	0.35
Panoramic Resources Limited	PAN	104	Savannah/Lanfrachi	213,598	1.94%	0.22	79,854	1.9%	0.59	20,000	4.0	Long-hole open stope with paste fill	281	125	147	135	4.90	0.77
Poseidon Nickel Limited	POS	90	Windarra, Cerberus	156,442	1.55%	0.26	24,754	1.4%	1.16	10,323	2.4	Sub Level Cave	212	123	150	61	3.56	1.47
Sirius Resources NL	SIR	732	Nova/Bollinger	414,426	2.20%	0.56	358,027	2.6%	0.65	30,000	11.9	Sub level opening stoping with backfill	379	133	140	239	3.20	3.06
Western Areas Limited	WSA	783	Flying Fox/Spotted Quoll	461,694	2.01%	0.77	202,292	4.2%	1.75	18,280	11.1	Long hole & airleg hand held mining	615	266	379	236	3.21	3.32
<b>Average</b>				<b>239,553</b>	<b>2.32%</b>	<b>0.41</b>	<b>121,394</b>	<b>3.00%</b>	<b>1.11</b>	<b>16,392</b>	<b>6.4</b>		<b>391</b>	<b>170</b>	<b>220</b>	<b>172</b>	<b>3.89</b>	<b>1.80</b>

Source: Patersons Estimates

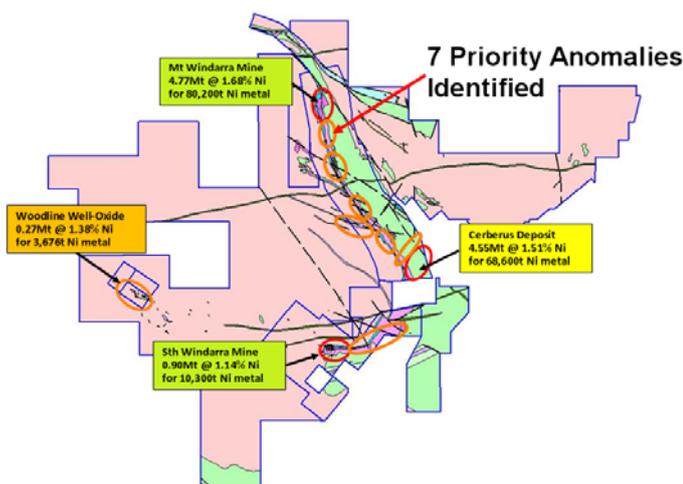
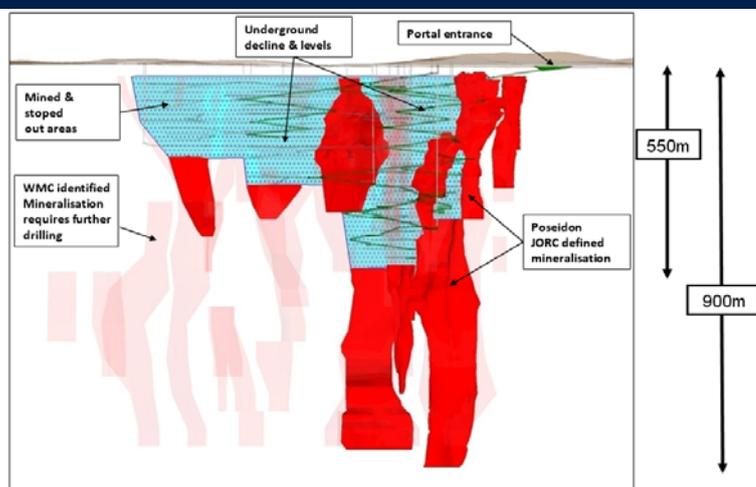
**Long Life Nickel Operation; Resource Growth 24%pa:** POS has significantly increased the mineral resource base since it acquired the Windarra Nickel project in 2006. We calculate an average annual increase of 24% per annum. The biggest growth has come from the discovery of the Cerberus satellite deposit located 10km to the south of the Mt Windarra mine. This rate of growth is equivalent to many of the nickel sulphide producers in WA. Overall, POS has identified approximately 10 years of mining inventory in its feasibility study released in April 2013. This is based on the assumption of a historic conversion of resources to reserves of over 80% during Mt Windarra's production from 1973 to 1991. Based on reserves there is only 2.4 years of material with further drilling needed to convert inferred into measured and indicated and then subsequently into reserves. The drilling will need to be conducted from underground once the mine is in production. Whilst this is a risk it appears the ore bodies are very contiguous and recent drilling by POS has potentially shown a positive reconciliation. Finally, there are 8 drill holes at Mt Windarra which have not been included in the resource/reserves estimates. Results of these drill holes have been received including the previously announced WUG0046 (17.53m true width (tw) at 3.52% Ni in D shoot, 3.57m (tw) at 2.77% Ni in F shoot, 1.2m (tw) at 5.54% Ni) which returned some of the best intersections seen to date.

**Brownfields Development; Existing Infrastructure:** The Windarra nickel project is a brownfields development with historic production of almost 20 years. It has existing infrastructure including: underground development, vertical shaft and headframe, power plant, tailing ponds, airstrip and core yard. An independent valuation in early 2013 of \$58m was placed on the infrastructure. In addition, POS has access to the extensive historical data from previous owner Western Mining Corp (WMC) which reduces start-up and operational risk substantially, provides resource extension and conversion confidence and includes an exploration database which led to the discovery of the Cerberus satellite ore body in 2009.

**Solid Management/Development Team:** POS has a strong management team with in-house development/production experience. The Company is headed up by Managing Director David Singleton, who is a mechanical engineer and was formerly CEO of Clough. Rob Dennis (Non-executive Director), with 35 years of experience which includes time at WMC where he worked at the Mt Windarra nickel mine from 1980-1986 as the underground mine manager. Neil Hutchison is GM Geology, with extensive experience which included time at the Jubilee's Cosmos mine where he developed a solid understanding of the nickel and ultramafic forming processes as well as the associated modern exploration techniques required to explore the Windarra Nickel Project.

**Significant Exploration Blue-Sky:** We see significant blue sky from exploration both near mine, and regionally. At Mt Windarra where mining was stopped at the 550m level, POS has defined the majority of its JORC resource to 900m (Figure 3). We see significant near mine upside to the north and south of the G, D and C shoots. We note that WMC previously identified mineralisation to the south and this is a high priority target for further drilling. At Cerberus, there is good potential for reserve replacement at depth. Finally, we see good regional exploration upside with 7 high priority targets identified along the Mt Windarra ultramafic Belt over a strike length of circa 13km.

**Figure 3 : Exploration Upside Mt Windarra (Top); Regional Exploration Targets (Bottom)**



Source: Poseidon Nickel

## Valuation

We estimate a target price of \$0.24/sh for Poseidon Nickel Limited (POS) (Figure 4). Our price target is based on our sum-of-parts whereby we conducted DCF models for Mt Windarra, Cerberus and processing of the gold tailings. We have not included any processing of the nickel oxide from pre-mined material and historic tailings material, which has a reserve of 12.92Mt at 0.38% Ni for 49.1kt of contained nickel.

We have assumed two years of a toll treatment arrangement before commencing full production. We believe the key advantage of toll-treatment is it allows the project to get started and generate good cashflows (\$28mpa) and once funding is achieved the project can reach full production more rapidly. Also, the capital used in the restart for toll treatment will reduce the upfront spend when moving to full production.

We have also assumed that the gold tailings start in parallel with the toll-treatment to bring in additional cashflow from the processing of circa 50,000oz over 3 years. We estimate the gold tails could generate \$12-17m per annum and potentially provide funding for the move to full nickel production.

## Net Asset Valuation

Our analysis suggests that the majority of POS's value is contained in the Mt Windarra Nickel project which includes: Mt Windarra, Cerberus and gold tailings. We have applied an 8% discount rate, which we use to value our other nickel sulphide producers under coverage. We have assumed that a short term toll-treatment arrangement is used to process 500,000tpa of 1.7% ore for the first two years of the operation. We estimate the cost to transport ore the 250km to the concentrator at \$30/t, this is based on using estimates from other comparable nickel sulphide producers. The mining, processing, administration costs are based around the Mt Windarra feasibility study. We estimate a total cost for the first two years of production of \$120/t, this reduces to \$91/t once the project moves into full scale production.

Assuming that POS can obtain the necessary financing then we believe the stock is worth 24cps. Further upside could come from processing the low grade nickel oxide tails and regional/near mine exploration which has excellent potential.

**Figure 4 : POS Net Asset Valuation**

<b>Valuation</b>	<b>A\$m</b>	<b>A\$/sh</b>
Mt Windarra	143	0.10
Cerberus	107	0.08
Gold Tails	31	0.02
Investments	0	0.00
Unpaid capital	69	0.05
Tax losses	30	0.02
Forwards	0	0.00
Corporate	(14)	(0.01)
Exploration (inc Resources)	11	0.01
Cash	4	0.00
Debt (incl Convertible Notes)	(43)	(0.03)
NAV @ 8.0% Discount Rate	338	0.24
<b>Price Target (1x NAV)</b>	<b>338</b>	<b>0.24</b>

Source: Patersons Estimates

Following the toll treatment for the first two years we expect the project to move into full production (9.6kt) in late 2016. Our estimates are based on POS's recent feasibility study released in April 2013. The feasibility looked at an average annual production of 9,600t of contained nickel over a 10 year mine life at an average operating cash costs of US\$3.35/lb (net of gold credits). Pre-start project capital cost is estimated at A\$197m with final concentrate expected 16 months after financing. Major capital items are: process plant (\$98m), pre-production costs (\$42m) and mine development (\$27m). Designed plant capacity is 1Mtpa. We estimate the toll treatment restart option will cost ~\$25m which will effectively reduce the capital needed to reach full production rates.

We have assumed an average grade for life of mine of 1.68% Ni with recoveries of 86%. Royalties are estimated at 3.5% comprising of 2.5% standard WA Government royalty and 1% royalty to BHP. Under the original agreement with WMC, who originally sold the property to POS, if the ore was not processed using their concentrator then it would attract a 1% royalty. We have assumed nickel payability of 75% for the life of mine given the low MgO ore which should attract a premium. Overall, we determine a project NPV@8% of \$147m for Mt Windarra. In parallel with the nickel production from Mt Windarra we expect POS to process the gold tails. POS plans to treat 45,000ozpa of gold over the first three years. We estimate cash costs of A\$700/oz. We determine an NPV@8% for the gold tailings of A\$31m.

Production from the Cerberus satellite deposit is expected to occur approximately 2 years after Mt Windarra commences full production in mid-2016. This will allow sufficient time to establish a development decline and production stopes. We estimate a life of mine grade of 1.51% Ni at recoveries of 86%. Cash costs are A\$72/t for mining, A\$35/t for processing, A\$1.61/t for haulage and Administration is \$7.50/t which equates to a cash cost of ~A\$4-4.30/lb. Overall, we determine an NPV@8% for Cerberus of \$107m.

### Financing

We have assumed a 70:30 debt to equity ratio for funding of the project (\$200m). For the toll treating arrangement we have assumed a \$35m raise at a 10% discount to the current share price in the June Q 2014. We have also assumed prior to full production POS raises another \$30m at a 10% discount to the current share price with the remainder a vanilla secured debt facility.

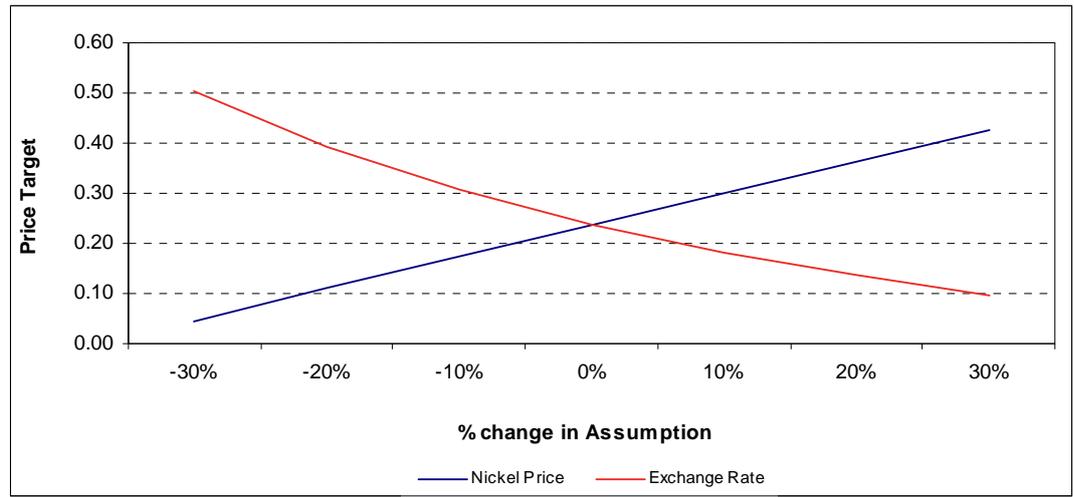
We also note that POS already has \$43m in debt via two convertible notes and an \$8m loan from Andrew Forrest. The \$8m loan is due in October 2014 and the convertible notes mature in 2017. Based on our scenario POS will generate sufficient capital to repay the convertible notes, however, if nickel prices remain lower than expected or financing takes longer than expected this is a key risk for the Company.

### Sensitivities

We have conducted a sensitivity analysis on POS. A 10% move in nickel price results in a 25.6% move in our target price. A 10% increase in exchange rate results in a 23.6% decrease in our target price (Figure 5).

**Figure 5 : POS Sensitivity Analysis**

Price Target of POS	Exchange Rate							
	0.24	-30%	-20%	-10%	0%	10%	20%	30%
Nickel Price	-30%	0.23	0.15	0.09	0.04	0.01	-0.03	-0.05
	-20%	0.32	0.23	0.16	0.11	0.07	0.03	0.00
	-10%	0.41	0.31	0.23	0.17	0.12	0.08	0.05
	0%	0.50	0.39	0.30	<b>0.24</b>	0.18	0.13	0.09
	10%	0.59	0.47	0.37	0.30	0.24	0.18	0.14
	20%	0.67	0.54	0.44	0.36	0.29	0.24	0.19
30%	0.76	0.62	0.51	0.42	0.35	0.29	0.24	



Source: Patersons Estimates

## Peer Comparatives

### Leverage to Nickel Price and Exchange Rate

We have conducted a comparative analysis in terms of nickel price and exchange rate leverage with other West Australian nickel producers/developers. POS has higher nickel price leverage than MCR and WSA (Figure 6).

**Figure 6 : Comparative Leverage Table**

Company Name	ASX Code	EV (\$m)	+10% Move in Nickel Price	+10% Move In Exchange Rate
Independence Group NL	IGO	914	3.0%	-18.0%
Mincor Resources NL	MCR	66	16.5%	-15.4%
Panoramic Resources Limited	PAN	104	43.7%	-53.6%
Poseidon Nickel Limited	POS	90	25.6%	-23.6%
Sirius Resources NL	SIR	732	26.7%	-29.5%
Western Areas Limited	WSA	783	18.2%	-16.2%
<b>Average</b>			<b>22.3%</b>	<b>-26.0%</b>

Source: Patersons Estimates

### EV/Resource; EV/Reserve

Below we provide a comparative with other West Australian nickel producers/developers in terms of EV/Resources and EV/Reserves. Based on an EV/resource POS is trading at 0.26/lb which is below the average of 0.41/lb. Based on an EV/reserve, POS is trading at 1.16/lb which is slightly below the average of 1.11/lb (Figure 7).

**Figure 7 : Comparative Table EV/Resource and EV/Reserve**

Company Name	ASX Code	EV (\$m)	Main Nickel Deposit(s)	Resource (Contained Ni Eq)	Grade (Ni Eq. %)	EV/lb Res	Reserve (Contained Ni)	Grade (Ni Eq%)	EV/lb Reserve	Annual Production (Ni ore)	Mine life Reserves
Independence Group NL	IGO	914	Long	74,160	5.37%	1.63	41,900	3.7%	2.89	10,753	3.9
Mincor Resources NL	MCR	66	Mittel, Mariners	117,000	3.69%	0.26	21,536	3.2%	1.40	9,000	2.4
Panoramic Resources Limited	PAN	104	Savannah/Lanfrachi	213,598	1.94%	0.22	79,854	1.9%	0.59	20,000	4.0
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Sirius Resources NL	SIR	732	Nova/Bollinger	414,426	2.20%	0.56	358,027	2.6%	0.65	30,000	11.9
Western Areas Limited	WSA	784	Flying Fox/Spotted Quoll	461,694	2.01%	0.77	202,292	4.2%	1.76	18,280	11.1
<b>Average</b>				<b>239,553</b>	<b>2.32%</b>	<b>0.41</b>	<b>121,394</b>	<b>3.00%</b>	<b>1.11</b>	<b>16,392</b>	<b>6.4</b>

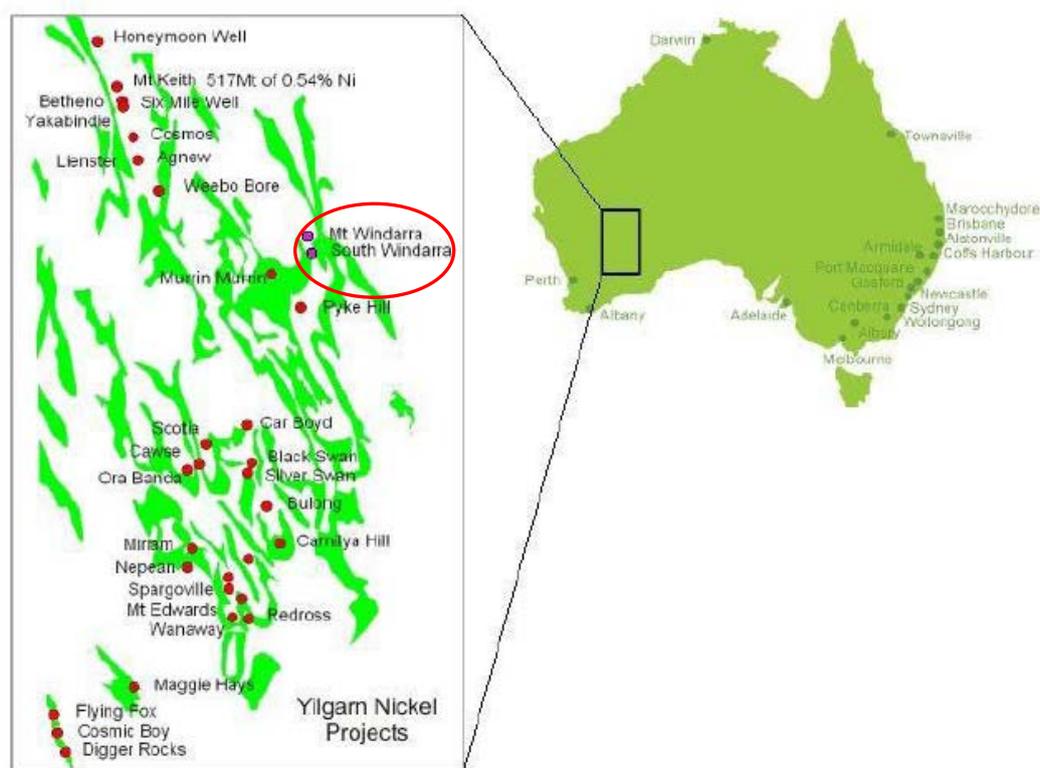
\*Note: IGO Adjusted for Long Ni Mine Only (excludes Tropicana and Jaguar/Bentley)

Source: Patersons Estimates

## Company Background

Poseidon Nickel Limited (POS) is a nickel development Company focused on the restart of the Windarra Nickel Project, located in the North Eastern Goldfields, 260km north east of Kalgoorlie on sealed roads (Figure 8). POS has invested circa \$94m over the last five years in refurbishing the existing mine and facilities and in extending the resource base of the project to support an initial 10 year mine life. The mine has been refurbished to 450m, about 100m above the start of unmined ore. The resource is one of the largest for any West Australian nickel sulphide project that has restarted production in the last decade. In April 2013, POS completed a DFS on the project which looked at restarting the Mt Windarra mine, developing the Cerberus greenfields deposit (10km south) and retreatment of gold and nickel tailings. Pre-production capital is estimated at \$197m. Given the current state of the credit market POS is looking at alternative methods of funding that would allow the reopening at the Windarra nickel project in 2015 to coincide with a widely anticipated nickel supply squeeze.

**Figure 8 : Mt Windarra Project Location**



Source: Poseidon Nickel

### Historical Background of Mt Windarra; First Discovered In 1969

The discovery of nickel at Mt Windarra in 1969 by a prospector with Poseidon Limited sent its share price on an incredible run going from \$1.85/sh to \$280/sh over 5 months. The run was supported by higher nickel prices due to the high demand and low supply. In 1974, the Mt Windarra mine commenced underground production with a second major orebody discovered 18km south (South Windarra) in the early 1970's which was mined as an open pit. By the time Poseidon started producing nickel the price had fallen and the mine went into care and maintenance with the company delisted in 1976. Western Mining Corp. took over the mine and operated it until 1991 when depressed nickel prices forced its closure. From 1973-1991 the Mt Windarra nickel mine processed 8Mt of nickel ore grading an average of 1.59% Ni producing 1Mt of 10% Ni-in-concentrate.

## Capital Structure

POS has 466.3m shares on issue with 7.23m options exercisable at 22c expiring in 2016. The Company has two tranches of convertible notes:

- 1) 36.5m notes convertible at \$0.40 for US\$15m (unsecured) at 5%pa coupon expiring 2017.
- 2) 64.9m notes convertible at \$0.30 for US\$20m (unsecured) at 5%pa coupon expiring 2017.

In addition, the company has an \$8m loan from its major shareholder Andrew Forrest whereby repayment was recently deferred by 12 months to 1 October 2014.

POS had \$0.7m in cash at the end of December 2013 and has since raised \$3.8m (before costs) through a placement to sophisticated investors. We have assumed that under a toll treatment arrangement that POS would look to raise an additional \$25m. It would be unusual for BHP (if it were the preferred party) to provide upfront capital.

POS has made application to the WA MRF Scheme to recover a \$3.5m bond held by the State Government. The application is currently under review as it requires individual approval because the Windarra tenements are subject to the Poseidon Nickel Agreement Act 1971 rather than being managed under the Mining Act of Western Australia.

## Assets

### Mt Windarra Nickel Project

Poseidon Nickel (formerly Niagara Mining) acquired the historic Windarra nickel assets from WMC Resources Ltd (now BHP) in 2005. The sale price was \$8m with provision for a 1% Net Smelter Return (NSR) royalty, if the offtake arrangements were not with BHP. With nickel prices strong in 2006 Niagara Mining commenced refurbishment and dewatering of the underground mine. In mid-2007, at the peak of record nickel prices (US\$55,000/t), a new Board and management team was appointed and the company was renamed Poseidon Nickel Limited (POS). In mid-2008, POS continued the underground refurbishment and secured \$50m in project funding. Unfortunately, the Global Financial Crisis (GFC) hit and the mine had to be placed on care and maintenance. Nickel prices improved at the back end of 2010 and POS raised US\$20m through a convertible note. The funding was predominately used to expand the existing resource and continue the refurbishment. The infrastructure has been independently valued at \$58m replacement value (Figure 9) and represents a significant saving off capital costs. The development has a capital intensity of US\$8/lb, below the global range for new projects of US\$10-50/lb of annual pound of nickel.

**Figure 9 : Windarra Infrastructure**

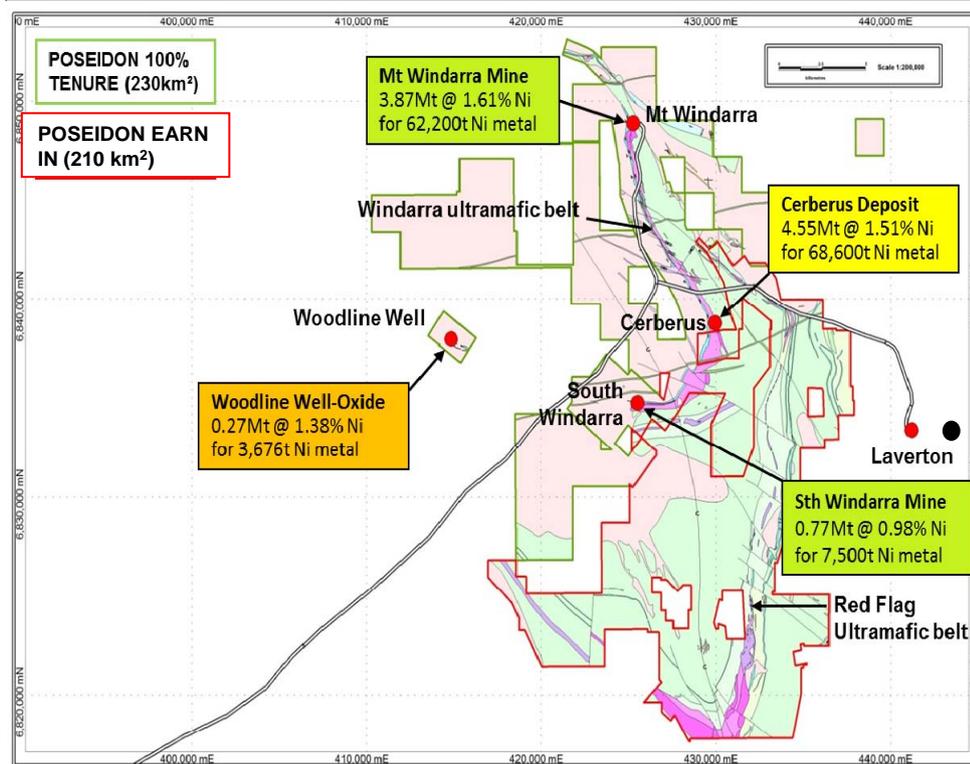


Source: Poseidon Nickel

## Geology

The Windarra Ultramafic Belt has a nickel endowment of 285kt of contained nickel to date (Figure 10). The Windarra region forms part of the Mt Margaret Goldfield. Mafic and ultramafics, metavolcanics and intrusives form important members of the Windarra greenstone belt. Economic nickel mineralisation in the Mt Windarra area is hosted at the base of the Windarra Ultramafics, a 100–300m thick sequence of ultramafic (komatiite) lava flows, overlain by basalts. The Windarra Ultramafics hosts four significant nickel deposits, two of which have previously been mined, the Mt Windarra underground mine and the South Windarra open-pit and underground mine. The third discovery was at Woodline Well which has a small near surface oxide deposit which may contain a deeper sulphide extension. The latest and most significant discovery made by POS was at Cerberus.

**Figure 10 : Geology and Surface Geochemistry**



Source: Poseidon Nickel

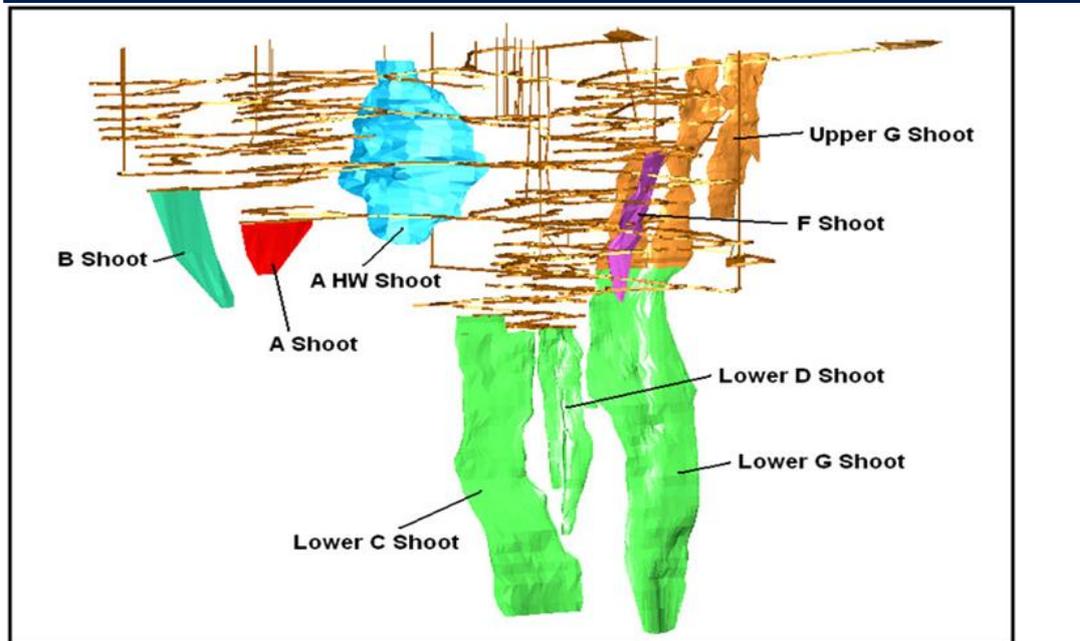
Nickel mineralisation at Mt Windarra is restricted to the sulphide zones at the base of the olivine cumulate ultramafic sequence. Massive sulphides form the dominant ore type and the non-massive sulphide mineralisation can be sub-divided into three different textural types: matrix (25-40% sulphide), blebby (20-30% sulphide) and disseminated (between 5-25% sulphide).

The nickel tenor of sulphides in the ultramafic rocks is normally 8 to 16%, and invariably higher in the disseminated ores than the massive sulphides. The massive ore in A and B shoots rarely assays more than 8% nickel, whereas in the E-C-D and F shoots it may assay up to 12%.

In the primary ore, pyrrhotite, pentlandite, pyrite and chalcopyrite are the most common sulphide phases, in decreasing order of abundance. The pyrrhotite to pentlandite ratio varies from 1:1 in disseminated ore, to up to 8:1 in the matrix hosted ore. The average nickel to copper ratio is 9:1 for most ore types, though may be as low as 4:1 in the copper rich basal matrix hosted ore and remobilised massive sulphide stringers.

The Mt Windarra orebody consists of eight distinct, steeply dipping shoots named: A, A Hanging Wall, B, C, D, E, F and G Shoot as depicted below (Figure 11). These shoots vary from 2m up to 20m in thickness; have a strike length of between 50m and 350m and a down dip extent of greater than 900m.

**Figure 11 : Remaining Lodes At Windarra Nickel Mine**



Source: Poseidon Nickel

### Reserves and Resources

Since 2007, POS has continued to grow its resource base through an aggressive underground drill program. The resource base has the potential to support an initial 10 year mine life. The discovery of the Cerberus orebody (located 10km from Windarra) in 2009 has provided the basis for the majority of the resource growth (Figure 12) which has averaged 24% per annum.

**Figure 12 : Windarra Nickel Project Annual Resource Growth**



Source: Poseidon Nickel

In Figure 13, we provide POS's latest reserve/resource statement as at June 2013. The reserve is comparatively small, however, as explained previously, historically there has been a high resource to reserve conversion of >80%. Therefore, POS uses a 10 year mining inventory. This is appropriate as the orebody is continuous from 550 to 900m and demonstrates good consistency.

**Figure 13 : Windarra Nickel Project Reserve/Resource Statement**

#### ORE RESERVE STATEMENT

Windarra Nickel Sulphides	Reserve Category		
	Probable		
	Tonnes	Ni% Grade	Ni Metal t
Cerberus	1,221,000	1.3	15,900
Mt Windarra	498,000	1.78	8,850
<b>Total</b>	<b>1,719,000</b>	<b>1.44</b>	<b>24,750</b>

Table 3: Windarra Nickel Project Reserve Ore Statement

#### MINERAL RESOURCE STATEMENT

Windarra Nickel Project Sulphides	Cut Off Grade	Resource Category								
		Indicated			Inferred			TOTAL		
		Tonnes	Ni% Grade	Ni Metal t	Tonnes	Ni% Grade	Ni Metal t	Tonnes	Ni% Grade	Ni Metal t
Mt Windarra	0.75%	1,217,000	1.39	17,100	3,553,000	1.78	63,100	4,770,000	1.68	80,200
South Windarra	0.80%	772,000	0.98	7,500	-	-	-	772,000	0.98	7,500
Cerberus	0.75%	2,773,000	1.25	34,600	1,778,000	1.91	34,000	4,551,000	1.51	68,600
<b>Total Sulphide</b>		<b>4,762,000</b>	<b>1.24</b>	<b>59,200</b>	<b>5,331,000</b>	<b>1.82</b>	<b>97,100</b>	<b>10,093,000</b>	<b>1.55</b>	<b>156,300</b>

Source: Poseidon Nickel

## Cerberus

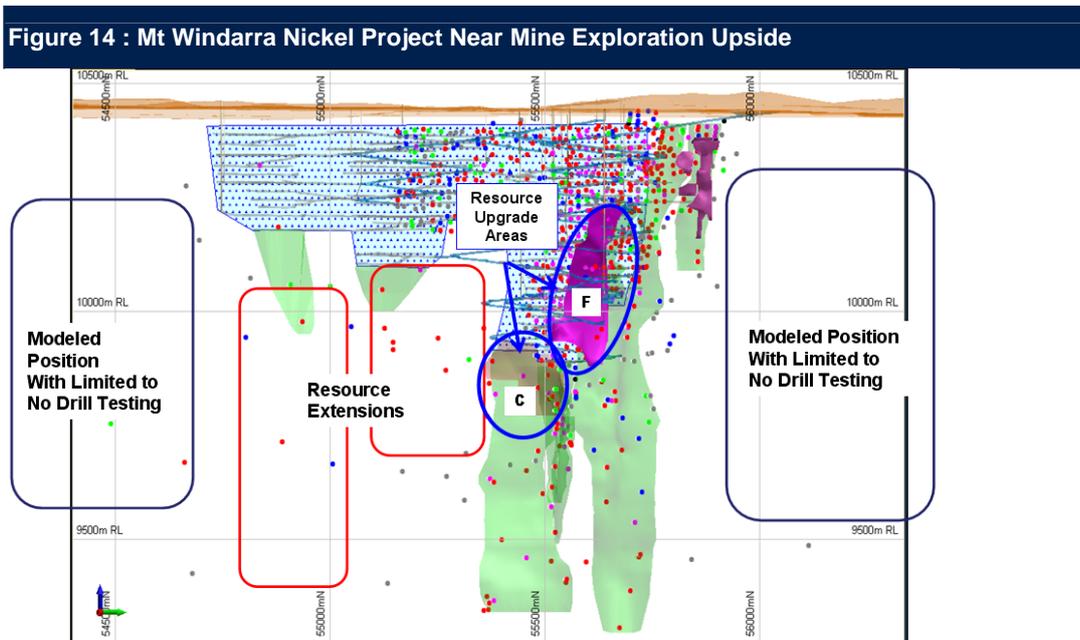
Cerberus is the latest and most significant discovery made by POS. The deposit comprises two lenses of relatively flat lying and north-easterly plunging mineralisation. The deposit is over 1100m long, 450m wide, dips 300m to the east and plunges 450m to the northeast. The Cerberus Deposit is located approximately 10.5km south of the Mt Windarra nickel mine and consists of 3 types of nickel sulphide mineralisation:

- The Main Zone:** Generally consists of massive to stringer nickel and some disseminated sulphides which occurs towards the base of the komatiite lava channel within the Windarra Ultramafic unit. The sulphides have an element of sulphide remobilisation and high grading due to structural overprinting.
- The Hanging-wall Zone:** Occurs as disseminated sulphides and sits around 2-6m above the Main Zone within the lava channel. It is poddier and lower grade than the Main Zone.
- Remobilised Footwall:** Consists of structurally remobilised and high graded nickel sulphides which have squirted off into the footwall. These have not been modelled as they are erratic and cannot be tied together in the current wide spaced drilling.

These may provide additional localised high grade nickel sulphide pods as drill density is increased. Typically drill intersect grades in this zone are between 3.5% and 7% nickel. Recent drilling results have been encouraging and POS has now decided to mine Mt Windarra and Cerberus simultaneously.

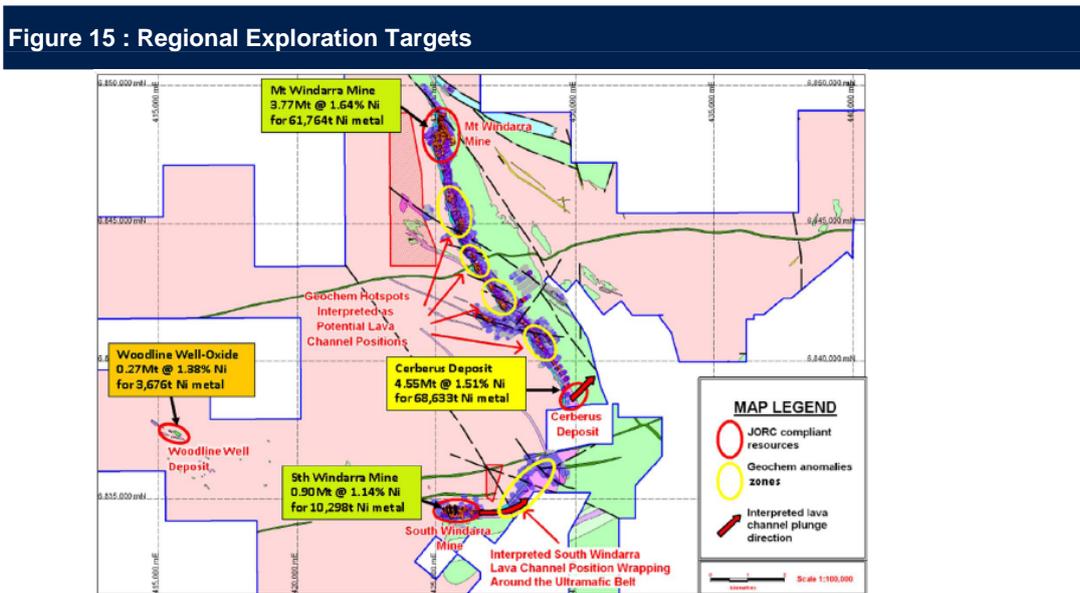
## Exploration Upside

There is both near-mine exploration upside and regional exploration upside which has been identified. At Mt Windarra, there is good potential to increase resources to the north where WMC has previously intersected mineralisation above 1% in a number of positions (Figure 15). In addition, there is potential to the south with limited to no drill testing. Based on this we believe that, with further exploration from underground drilling which allows an improved drill position and is more cost effective, there is good potential to delineate further significant resources. This would likely be done following the restart of production.



Source: Poseidon Nickel

POS has identified a number of regional exploration targets along the Windarra ultramafic belt. These are defined as anomalous geochemical zones which, with additional drilling, have the potential to continue to expand the nickel resources.



Source: Poseidon Nickel

## Risks

We believe many of the risks for POS are relatively low considering that the Mt Windarra nickel mine processed ore from 1974 to 1993. This reduces construction, engineering, permitting and metallurgical risks. The main risks for POS relate to 1) Financing to restart operations, 2) Resource to Reserve Conversion 3) Restart Risks 4) Commodity Price 5) Foreign Exchange 6) Concentrate Sales Agreement.

**Financing Risk:** The largest risk for POS at this time is financing. While nickel prices have improved 14% since the beginning of February debt markets remain tight, making it difficult to achieve funding. Equity markets have improved recently although it remains difficult for junior mining companies looking for development capital.

**Resource to Reserve Conversion:** The DFS uses an assumption of an 80% conversion from inferred resources to reserves to determine an estimated initial mining inventory of 10 years. While there is a good historical reconciliation there is a risk, while low, that this reconciliation may turn out to be lower.

**Restart Risks:** There are a number of risks relating to the restart of the Mt Windarra mine. The key risk is delays to construction, slower ramp-up and/or lower recoveries through plant commissioning.

**Commodity Price:** Assuming financing, moving forward the majority of revenues will be derived from the sale of nickel concentrate. Fluctuations in the nickel price affect the Company's ability to mine at a profitable margin. That said, nickel prices are expected to recover as a lack of quality sulphide concentrates are expected to be available post-2015, which should be positive for prices.

**Exchange Rate:** As an Australian domiciled company, fluctuations in foreign currency exchange rates between the Australian dollar and US dollar have the potential to decrease the profitability of the company. POS has indicated that it could use hedging to negate fluctuations in nickel price and currency.

**Concentrate Sales Agreement:** POS has yet to sign a concentrate sales agreement. BHP does have first right of refusal to match the terms of a competing bidder. Generally, BHP's terms are for a 65% nickel payability, which is considered low compared to terms with Jinchuan and other offtake arrangements.

## Management

### **Mr Christopher Indermaur, Non-Exec Director (Appointed February 2014; Non-Exec Director since April 2009)**

Mr Indermaur has over 30 years of experience in large Australian companies in Engineering or Commercial roles. Amongst these roles he was the Engineering and Contracts Manager for the QNI Nickel Refinery at Yabulu, Company Secretary for QAL and General Manager for Strategy and Development at Alinta Ltd.

Mr Indermaur holds a Bachelor of Engineering (Mechanical) and a Graduate Diploma of Engineering (Chemical) from the West Australian Institute of Technology (now Curtin University). Chris also holds a Bachelor of Laws and a Master of Laws from the Queensland University of Technology and a Graduate Diploma in Legal Practice from the Australian National University.

### **David Singleton, MD & CEO (Appointed February 2008)**

Mr Singleton has a wide range of operational and management experience including as Managing Director and CEO at Clough Limited and CEO of Alenia Marconi Systems based in Rome, Italy. He was also the Group Head of Strategy, Mergers & Acquisitions with BAE SYSTEMS in London, which through consolidation became one of the largest Aerospace and Defence Companies in the world.

He has a degree in Mechanical Engineering from University College, London, is a non-executive director of Austal Ltd and Quickstep Holdings and was formerly a non-executive director of Triton Gold Ltd and a director of PT Petrosea Tbk in Indonesia. He is also the Deputy Chair of the Council for Methodist Ladies College in Perth.

Mr Singleton was appointed as Chief Executive Officer on 2 July 2007

### **Mr Geoff Brayshaw, Non-Exec Director (Appointed February 2008)**

Mr Brayshaw was formerly an audit partner with a major accounting firm in Perth, having been in practice for some 35 years. He has also held a number of positions in commerce and professional bodies including national president of the Institute of Chartered Accountants of Australia in 2002.

He is a director of a number of public and private companies, including independent director and audit committee chairman of both Fortescue Metals Group Limited and AVEA Insurance Limited. He was previously a member of the board of the Small Business Development Corporation

### **Mr Rob Dennis, Non-Exec Director (Appointed February 2014)**

Mr Dennis is a mining engineer with over 35 years experience in the nickel, copper, gold and alumina industries.

In his former role as COO Aditya Birla Minerals Ltd he managed the expansion and development of the Nifty Copper Project in the North West of Western Australia and the Mt Gordon operation in North Queensland. Prior to that, he held positions including General Manager Project Development for Lionore Australia, General Manager Operations for Great Central Mines and Chief Mining Engineer for Western Mining Corporation. During his time with Western Mining Corporation, Mr Dennis worked at the Windarra Nickel Project as underground mine manager from 1980-1986. He joined Poseidon Nickel in June 2007 as Chief Operating Officer and was appointed to the Board in February 2014.

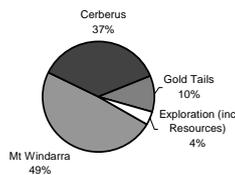
## Poseidon Nickel Limited

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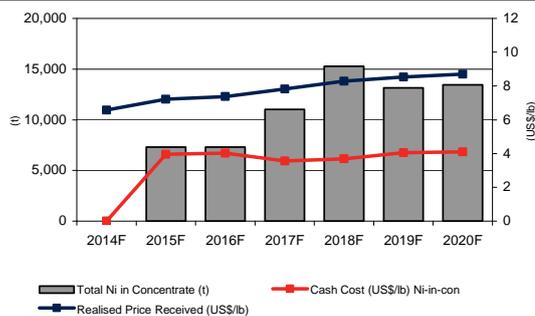
Valuation	A\$m	A\$/sh
Mt Windarra	143	0.10
Cerberus	107	0.08
Gold Tails	31	0.02
Investments	0	0.00
Unpaid capital	69	0.05
Tax losses	30	0.02
Forwards	0	0.00
Corporate	(14)	(0.01)
Exploration (inc Resources)	11	0.01
Cash	4	0.00
Debt (incl Convertible Note)	(43)	(0.03)
NAV @ 8.0% Discount Rate	338	0.24
<b>Price Target (1x NAV)</b>	<b>338</b>	<b>0.24</b>

Patersons base case NPV	\$0.24
Valuation at flat spot NI and AUDUSD	\$0.115
Implied US\$ Ni price at current SP	\$6.71

## Valuation Summary of Operating Assets



## Nickel Production Summary



## Reserves &amp; Resources (as at 30 June 2013)

Reserves (Nickel)	kt	Ni %	Ni kt
Cerberus	1,221	1.3	15.9
Mt Windarra	498	1.8	8.9
<b>Total</b>	<b>1,719.0</b>	<b>1.44</b>	<b>24.7</b>

Reserves (Gold)			
North, Central and South Dams	10,430	0.52	174.1
<b>Total</b>	<b>10,430</b>	<b>0.52</b>	<b>174.1</b>

Resources	kt	Ni %	Ni kt
Mt Windarra	4,770	1.7	80.1
Cerberus	4,551	1.5	68.7
South Windarra	772	1.0	7.6
Central Dam Tailings	9,600	0.3	32.6
South Windarra Dumps	2,976	0.4	12.2
Woodline Well	344	1.3	4.3
<b>Total</b>	<b>23,013</b>	<b>0.89</b>	<b>205.6</b>

Resources (Gold)	kt	g/t	Au (koz)
North, Central and South Dams	10,990	0.52	183.5
<b>Total</b>	<b>10,990</b>	<b>0.52</b>	<b>183.5</b>

## Directors

Name	Position
Chris Indermaur	Chairman
David Singleton	Managing Director & CEO
Geoff Brayshaw	Non Executive Director
Rob Dennis	Non Executive Director

Commodity Assumptions	2013A	2014F	2015F	2016F	2017F
AS:US\$	1.03	0.91	0.87	0.85	0.83
Nickel (US\$/lb)	7.39	6.57	7.21	7.37	7.82
Nickel (A\$/lb)	7.20	7.25	8.30	8.72	9.43

Sensitivities	+10%	0%	-10%
Nickel Price	0.30	0.24	0.17
Exchange Rate	0.18	0.24	0.30

Production Summary	2013A	2014F	2015F	2016F	2017F
<b>Nickel Production (t)</b>					
Mt Windarra	0	0	7,310	7,310	9,413
Cerberus	0	0	0	0	1,598
<b>Total Ni in Concentrate (t)</b>	<b>0</b>	<b>0</b>	<b>7,310</b>	<b>7,310</b>	<b>11,011</b>

Gold Tailings (koz)	0	0	7,203	16,599	18,593
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Cash Cost (US\$/lb) Ni-in-con	0.00	0.00	3.96	4.02	3.56
Cash Cost (US\$/lb payable)	0.00	0.00	5.15	5.16	4.42
<b>Total Cost (US\$/lb) per lb prod.</b>	<b>0.00</b>	<b>0.00</b>	<b>6.10</b>	<b>5.81</b>	<b>5.20</b>

Realised Price Received (US\$/lb)	7.50	6.57	7.21	7.38	7.82
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Profit & Loss (A\$m)	2013A	2014F	2015F	2016F	2017F
<b>Sales Revenue</b>	<b>0.0</b>	<b>0.0</b>	<b>111.5</b>	<b>131.9</b>	<b>202.9</b>
Other Income	0.5	0.3	0.0	0.0	0.0
Operating Costs	(2.3)	0.0	(68.7)	(77.0)	(98.2)
Exploration Exp.	(1.3)	(0.2)	(0.7)	(2.9)	(2.9)
Corporate/Admin	(3.3)	(4.9)	(4.1)	(4.2)	(4.3)
<b>EBITDA</b>	<b>(6.4)</b>	<b>(4.8)</b>	<b>38.0</b>	<b>47.8</b>	<b>97.5</b>
Depn & Amort	(0.0)	0.0	(32.8)	(44.3)	(56.9)
<b>EBIT</b>	<b>(6.5)</b>	<b>(4.8)</b>	<b>5.2</b>	<b>3.5</b>	<b>40.7</b>
Net Interest	(6.9)	(6.3)	(6.1)	(4.0)	(6.7)
<b>Operating Profit</b>	<b>(13.4)</b>	<b>(11.1)</b>	<b>(0.9)</b>	<b>(0.4)</b>	<b>34.0</b>
Tax (expense) benefit	0.0	0.0	(0.2)	0.0	0.0
Abnormals	0.0	2.9	0.0	0.0	0.0
<b>NPAT</b>	<b>(13.4)</b>	<b>(8.3)</b>	<b>(1.1)</b>	<b>(0.4)</b>	<b>34.0</b>
<b>Normalised NPAT</b>	<b>(13.4)</b>	<b>(8.3)</b>	<b>(1.1)</b>	<b>(0.4)</b>	<b>34.0</b>

Cash Flow (A\$m)	2013A	2014F	2015F	2016F	2017F
Adjusted Net Profit	(13.4)	(11.1)	(1.1)	(0.4)	34.0
+ Interest/Tax/Expl Exp	19.5	13.3	13.2	9.8	10.6
- Interest/Tax/Expl Inc	23.0	10.4	9.7	13.1	14.9
+ Depn/Amort	0.0	0.0	32.8	44.3	56.9
+/- Other	12.0	3.4	0.0	0.0	0.0
<b>Operating Cashflow</b>	<b>(4.9)</b>	<b>(4.8)</b>	<b>35.2</b>	<b>40.6</b>	<b>86.6</b>
- Capex (+asset sales)	0.0	25.3	14.5	168.8	21.5
- Working Capital Increase	13.1	(0.1)	0.0	0.0	0.0
<b>Free Cashflow</b>	<b>(18.0)</b>	<b>(30.0)</b>	<b>20.7</b>	<b>(128.2)</b>	<b>65.2</b>
- Dividends (ords & pref)	0.0	0.0	0.0	0.0	0.0
+ Equity raised	0.0	38.6	30.0	0.0	0.0
+ Debt drawdown (repaid)	0.0	0.0	(8.0)	116.0	(63.4)
<b>Net Change in Cash</b>	<b>(18.0)</b>	<b>8.6</b>	<b>42.7</b>	<b>(12.2)</b>	<b>1.8</b>
Cash at End Period	2.6	11.2	53.9	41.7	43.4
Net Cash/(LT Debt)	(40.8)	(32.1)	18.5	(109.7)	(79.9)

Balance Sheet (A\$m)	2013A	2014F	2015F	2016F	2017F
Cash	2.6	11.2	53.9	41.7	43.4
Total Assets	83.8	124.1	247.3	287.2	307.3
Total Debt	31.1	43.4	115.4	151.4	123.4
Total Liabilities	43.2	53.2	147.5	187.9	173.9
Shareholders Funds	40.6	70.9	99.8	99.3	133.3

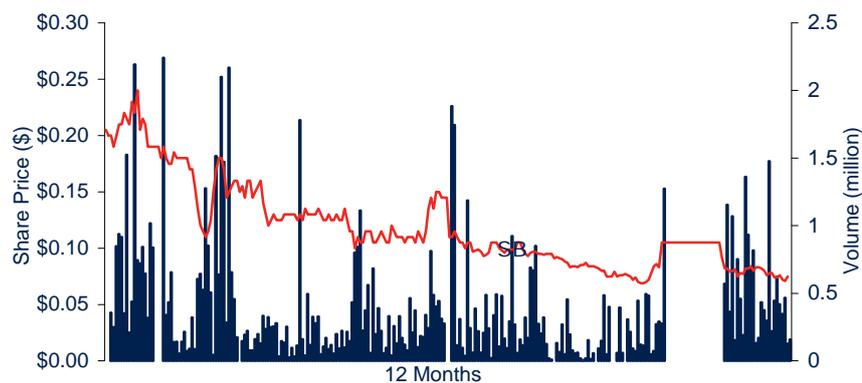
## Ratios

Net Debt/Equity (%)	100.6	45.3	na	110.4	59.9
Interest Cover (x)	na	na	0.9	0.9	6.1
Return on Equity (%)	na	na	na	na	25.5

## Substantial Shareholders

	Shares (m)	%
Andrew Forrest	147.8	31.7
Board / Management	26.1	5.6
Jefferies	22.8	4.9

## Recommendation History



Date	Type	Target Price	Share Price	Recommendation	Return
04 Nov 13	Research Note	0.22	0.10	SB	
	Current Share Price		0.08		-24.2%

**Stock recommendations:** Investment ratings are a function of Patersons expectation of total return (forecast price appreciation plus dividend yield) within the next 12 months. The investment ratings are Buy (expected total return of 10% or more), Hold (-10% to +10% total return) and Sell (> 10% negative total return). In addition we have a Speculative Buy rating covering higher risk stocks that may not be of investment grade due to low market capitalisation, high debt levels, or significant risks in the business model. Investment ratings are determined at the time of initiation of coverage, or a change in target price. At other times the expected total return may fall outside of these ranges because of price movements and/or volatility. Such interim deviations from specified ranges will be permitted but will become subject to review by Research Management. This Document is not to be passed on to any third party without our prior written consent.

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