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QUAY MAGNESIUM LIMITED
ACTIVITIES REPORT TO 30 JUNE 2009

In the Chairman's address delivered at the November 2008 AGM the poor condition of global economic confidence, the automotive industry and demand for magnesium alloys were all touched on. Unfortunately the global economy continues to remain weak with little evidence of recovery and these comments remain relevant today more than six months after they were originally made. There are some signs of economic activity resuming but currently at a level insufficient to underpin the commercial profitability of our plant. As an indication production and sales in August and September from Quay's Nanjing facility are currently forecast to be approximately 20 – 25 % of capacity. Scheduling considerations have resulted in a focus on AM50A and AM60B alloys but this strategy is being continuously reviewed to match our products with market opportunities.

Approximately half of these sales are to domestic customers and the other half are for export. There has been a slight recovery in North America but Europe remains extremely quiet. In both regions customers continue to report overstocking and lack of demand from end users. Chinese domestic demand has remained reasonably firm but margins for alloys have been adversely affected both here and in export markets.

The pure magnesium price also serves to highlight the weak state of underlying economic activity and demand. Anecdotally there are many Chinese primary magnesium plants running at a fraction of their capacity while some have been placed on care and maintenance. At last year's AGM the fall from 36,000 to 24,000 and then to 16,000 Renminbi per tonne (RMB /t) of the pure magnesium price was highlighted. In the six months since then it has remained firmly around this base with no recovery in demand evident. At the time of writing the pure magnesium price is under 15,500 RMB/t. At this price level and on low volumes much of the Chinese pure magnesium industry would be in losses.

In order to survive these conditions Quay has implemented several waves of cost cutting at both the plant in Nanjing and Head Office. Current manning at Nanjing is down to 55 – this was well over 100 at its peak during ramp up. There is a certain minimum level of manpower required to maintain standards and accreditation which enable Quay to sell into the automotive sector. Manning cannot be reduced below this level without impacting on the plant's credentials. The quiet time at the factory has been used to enhance some parts of the production process and carry out essential maintenance. The largest work currently being performed is on the melting furnace but this will not impact on the sales orders that are in hand.

On a positive note Nanjing's domestic working capital loan of 10 m RMB was increased to a 20 m RMB facility with another Chinese bank when the existing facility expired in late June. This new facility was activated on July 1. Investigations are being made into securing further working capital in China to finance working capital requirements when sales eventually recover. Quay believes another 10 – 15 m RMB may be available for this purpose. Another positive was receiving the final payment from our insurer as settlement for the fire of more than a year ago.

In August last year Quay announced that it had secured a line of working capital finance from a European bank. To date this facility has not been used and during the year it was reduced from USD 10.0 million to USD 7.0 m. A decision will have to be made shortly on whether to apply for an extension of this facility as it expires in early August. The facility is expensive to maintain and its usefulness severely restricted by the bank's inability to provide trade finance insurance for many of Quay's customers in the automotive sector.

At this time Quay is in advanced negotiations with two China based groups with the objective of securing equity investments from both. The first of these potential investments is close to completion. The second will require approval of shareholders at a General Meeting but the commercial terms are already broadly agreed in principle. If these investments proceed not only will Quay benefit from the injection of new equity but the company may also benefit from access to the primary magnesium plants that each of these two potential investors is associated with. If share issues are successfully completed Quay's intention is to conduct technical, legal and commercial due diligence on each of the plants associated with these investors with a view to realising Quay's strategy of becoming a more fully vertically integrated producer of magnesium products. While it is too early to speculate on the final form of any commercial arrangements, if any, that are entered into beyond the initial investments it is Quay's intention to pursue these potential opportunities aggressively with a view to finalising one or both by calendar year end.

In summary Quay is still enduring the effects of a savage downturn in the global economy and confidence but unlike many of our customers in the automotive and die – casting sectors we have survived. We remain committed to our vision of production of magnesium alloys of the highest quality, vertical integration and much larger economies of scale.

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