

Letter to Shareholders
Third Quarter 2018



Karnalyte is transitioning to a brighter future of growth and value creation. This is the first letter to shareholders that we intend on sending to you in connection with our quarterly financial reporting.

Our aim is simple: to keep you apprised of developments that are relevant to Karnalyte, to provide insight into our business and the broader fertilizer industry, and outline the steps we are taking to execute on the strategic plan we announced in May 2018.

We hope that the combination of an update on Karnalyte’s activities, from corporate, to potash to nitrogen, coupled with industry updates and some useful information on the products your Company intends to produce, will lead you to share the enthusiasm that the Board and management has for Karnalyte.

Karnalyte Resources Inc.

Third Quarter Letter to Shareholders – November 14, 2018

Dear Karnalyte Shareholder:

The third financial quarter of 2018 was a busy time for Karnalyte Resources Inc. (“Karnalyte” or the “Company”) as we took steps to advance our strategy to build an independent Saskatchewan-based fertilizer company through the production of potash and the manufacture of nitrogen.

Highlights of the quarter:

- We continued to actively execute our strategic plan to diversify into two fertilizer product lines – potash and nitrogen
- Potash prices continued to improve, as some contracts in key markets reported increases between 20% and 30% from the previous year, which moves Wynyard Potash closer to being economically viable
- Proteos Nitrogen continues to systematically advance through development
- Our recently announced rights offering provides all existing shareholders with an equal opportunity to invest in Karnalyte at an attractive entry price and provides additional working capital to fund our business
- Gujarat State Fertilizer and Chemicals Limited’s (“GSFC”) additional investment in Karnalyte, by way of a backstop of the rights offering, demonstrates GSFC’s ongoing commitment and support of Karnalyte, Wynyard Potash and Proteos Nitrogen

Taken together, these steps forward support our enthusiasm for the opportunities available to Karnalyte in the global fertilizer industry.

Karnalyte’s Strategy: Produce Essential Plant Nutrients

We think fertilizer is a good business to be in. According to the United Nations, world population is expected to grow from the current 7.6 billion to 8.9 billion people by 2050. All of those people will have to be fed, food will have to be grown and produced, and as arable land continues to shrink on a worldwide basis, the challenge is to increase food production per acre to meet the increasing demand.

The only way to increase per acre production is through a combination of increased plant population, fertilizer, crop genetics and technology. Karnalyte’s focus is on the fertilizer component of increased food production.

Developing our fertilizer business is the key to creating shareholder value, as fertilizer is a business that will last generations. Wynyard Potash has a current mine life of approximately 72 years, and Proteos Nitrogen will be able to produce nitrogen fertilizer for as long as we have access to an inexpensive, plentiful supply of natural gas.

Fertilizer: A Fundamental Aspect of Global Agriculture

As we follow an industry trend to diversify into multiple fertilizer products, we felt it would be useful to provide a short primer on fertilizer.

At their most basic, fertilizers are plant nutrients, and plant nutrients simply are plant food. Just like feed provides the carbohydrates, protein, fat, vitamins and trace minerals required to nourish animals, plant nutrient products deliver the essential nutrients needed to nourish plants.

Plants require 17 nutrients for optimum growth and development. Each of these nutrients is a chemical element found on the periodic table. Three of the seventeen elements – carbon, hydrogen and oxygen – are non-mineral elements that are available from the atmosphere or water. The other fourteen are classified as primary nutrients, secondary nutrients and micronutrients. A deficiency of any one of the 17 nutrients will limit plant growth.

Primary Nutrients: The three primary nutrients – nitrogen (N), phosphorus (P) and potassium (K) – are the carbohydrates, protein and fat of plant diets. Plants remove large amounts of the primary nutrients during the growing season and soils become depleted if these nutrients are not replenished after each harvest.

- **Nitrogen (N)** is often required in the greatest quantity by crops, primarily for vigor and yield. Nitrogen plays a key role in chlorophyll production and protein synthesis. Chlorophyll is the green plant pigment responsible for photosynthesis. When nitrogen is deficient, plants develop yellow or pale leaves and their growth is stunted.
- **Phosphorus (P)** is a vital component of adenosine triphosphate (ATP) which supplies the energy for many processes in the plant. Phosphorus rarely produces spectacular growth responses, but is fundamental to the successful development of all crops. For example, maize or other corn crops that lack phosphorus during the growing season achieve lower yields.
- **Potassium (K)** is needed by virtually all crops and often in higher rates than nitrogen. Potassium regulates the plant's water content and expansion. It is key to achieving good yield and quality in cotton and critical for increasing the size, juice content and sweetness of fruit.

The three numbers on fertilizer represent the value of these three primary nutrients or the NPK values. The higher the number, the more concentrated the nutrient is in the fertilizer. A fertilizer that contains only one plant nutrient will have a “0” in the other values.

Karnalyte's Projects: Potash and Nitrogen

Karnalyte's projects are designed to produce potash and manufacture nitrogen. They are both at an advanced stage of development, are both located in Saskatchewan in the heart of the Canadian farm belt and are adjacent to the major US Midwest agriculture industry.

Wynyard Potash Project

The Wynyard Potash Project (“Wynyard Potash”), our flagship project, is a 100% owned conventional solution mining potash project located in Wynyard, Saskatchewan, approximately 175 kilometres from Saskatoon. Wynyard Potash has been designed to be developed in three phases:

- Phase 1: 625,000 million tonnes per year (MTPA)
- Phase 2: 725,000 MTPA
- Phase 3: 725,000 MTPA

Wynyard Potash is well advanced. We have completed a final feasibility study, basic engineering, obtained all necessary environmental approvals, and entered into an offtake agreement with GSFC for approximately 50% of Phase 1 production. The only thing lacking is favourable market dynamics.

Awaiting a Recovery in Global Potash Prices

We are encouraged by the continuing improvement in potash prices, and in particular by the recent contracts entered into by China and India. While potash prices continue to improve, they have not yet reached the level where Wynyard Potash is an economically viable and financeable mining project. In the current industry conditions, it is simply impossible to finance and build Wynyard Potash.

International financial markets, and in particular the debt markets, remain very tight, very restrictive and increasingly expensive as interest rates continue to rise. We are committed to taking a prudent and disciplined approach to the development of Wynyard Potash, and we will continue to closely monitor potash prices and market dynamics in deciding when to re-activate development of Wynyard Potash.

Proteos Nitrogen Project

The Proteos Nitrogen Project (“Proteos Nitrogen”) is a compelling part of Karnalyte’s future. Moving into the manufacturing of nitrogen will provide valuable diversification away from a reliance on potash, and give us another market in which to do business. Proteos Nitrogen also has the potential to provide a source of free cash flow to assist in funding the development of Wynyard Potash. We see great potential in this area.

Proteos Nitrogen is a proposed small-scale nitrogen fertilizer plant to be located in central Saskatchewan, with a nameplate capacity of 700 mtpd (metric tonnes per day) ammonia and 1,200 mtpd urea. Our primary target market is local, independent wholesalers within a ~400-kilometre radius of Saskatoon, with a secondary target market of Midwest USA wholesalers near the Canadian border.

Our investigation of the technical and economic viability of Proteos Nitrogen includes identification and acquisition of an appropriate project site which is in close proximity to the required infrastructure of natural gas supply, power supply, water, and railway and highway access. In addition, we have received a positive independent marketing study, as well as numerous responses to our request for expressions of interest to develop Proteos Nitrogen on a lump sum turn key basis. Next steps include preparation of a feasibility study, including initial capital and operating costs, and project economics.

Why Nitrogen Fertilizer?

Saskatchewan has a number of competitive advantages for nitrogen fertilizer production, including:

- Plentiful natural gas
- Some of the lowest global natural gas prices
- Higher urea usage rates
- Premium pricing in local markets
- Proximity to local markets

We feel our regional scale design will provide farmers with local supply, while at the same time allowing them to reduce transportation costs and associated risks. As with any industrial material, the ultimate consumers are always looking for local, alternate and independent sources of supply. We are pleased and encouraged by the continuing interest shown in Proteos Nitrogen by participants in the local agricultural industry, and those inquiries confirm our regional scale approach to nitrogen.

How is Nitrogen Fertilizer Made?

The most common form of nitrogen fertilizer is urea, which is manufactured through a series of chemical processes. The key input is natural gas. The first step is to produce ammonia by reacting nitrogen from the air with hydrogen from natural gas at high pressure and temperature using the Haber process. This ammonia is then stored as a liquid under pressure or refrigerated. Urea is produced by reacting this ammonia with carbon dioxide at high pressure. Urea can be further concentrated or converted into a solid form (prills or granules).

Gujarat State Fertilizers & Chemicals Limited: A Committed Shareholder and Strategic Partner

We receive many questions about GSFC, why it invested in Karnalyte, and how it contributes to the execution of our strategy.

GSFC is a long-term strategic investor. GSFC made its initial \$45 million investment in Karnalyte in January 2013 with the objective of developing Wynyard Potash into an operating potash mine. That objective has not changed. GSFC, as one of India's largest chemical / fertilizer manufacturers, is intent on securing a long term, stable supply of potash from a primary potash producer such as Karnalyte.

How GSFC Contributes to Our Development

Wynyard Potash:

GSFC has had a tangible impact on our business. In 2013, GSFC entered into an offtake agreement with Karnalyte, which provides for GSFC to purchase approximately 50% of all potash produced from all three phases of Wynyard Potash. Offtake agreements are a critical component of project financing of major projects, as they provide security to the lenders of a minimum revenue stream during project debt pay-back periods. Such agreements also provide a stable, certain source of revenue.

In addition, in early 2016, in the face of declining potash prices, GSFC arranged, guaranteed, and backstopped a complete US\$700 million debt and equity project financing package for Wynyard Potash, which would have seen Wynyard Potash built and operating by early 2019. Unfortunately, as the public record shows, this financing did not proceed.

We continue to work with GSFC, and GSFC has continued to state publicly that it is committed to Karnalyte, committed to Wynyard Potash, and committed to assisting Karnalyte in structuring the most effective project financing package for Wynyard Potash when required.

Proteos Nitrogen:

GSFC is also very supportive of Karnalyte's nitrogen fertilizer strategy. We have been able to leverage GSFC's technical, operational and commercial experience gained from manufacturing nitrogen fertilizer in India for the past 50 years. As

Karnalyte's strategic partner and single largest shareholder, supporting the development of Proteos Nitrogen will also provide a series of benefits that will assist us in developing Wynyard Potash.

Raising the Capital to Support Our Development

Wynyard Potash and Proteos Nitrogen are major projects that will require significant amounts of capital to develop to the point where we can finance and build them. While we currently have sufficient cash on hand to keep the Company running for the next two years, we simply don't have sufficient capital to fund the development programs needed to bring our projects to the point where we can make a final investment decision.

We will need to raise this development capital through a series of equity financings in the Canadian capital markets as we achieve development milestones. This approach is designed to balance raising the funds required to advance our business, while minimizing dilution to existing shareholders.

In November, we announced a rights offering to all our shareholders as our first equity financing since 2013. We have specifically chosen a rights offering as it is the most fair and democratic way to raise capital and provides all our existing shareholders with the opportunity to protect themselves from dilution. To incentivise shareholders to participate in the financing, the Toronto Stock Exchange requires that the shares be offered at a deeply discounted price to the current market price.

We are particularly pleased that GSFC will be investing more into Karnalyte through the rights offering and their continuing investment in Karnalyte provides a strong vote of confidence in our strategy and our projects.

An Exciting Time for Karnalyte

We are enthusiastic about Karnalyte's future and the opportunities to execute on our strategy to create an independent Saskatchewan based fertilizer company. We are always happy to talk to shareholders, and we encourage you to contact us with any comments or questions you may have.

Thank you for reading, and for your support of Karnalyte.

Sincerely,

A handwritten signature in black ink that reads "Frank Wheatley". The signature is written in a cursive style with a long horizontal line extending to the right.

Frank D. Wheatley
President