SouthGobi Resources Ltd.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Restated)

December 31, 2012

(Unaudited)
(Expressed in U.S. Dollars)

FORWARD-LOOKING STATEMENTS

Except for statements of fact relating to the Company, certain information contained herein constitutes forward-looking statements. Forward-looking statements are frequently characterized by words such as "plan", "expect", "project", "intend", "believe", "anticipate" and other similar words, or statements that certain events or conditions "may" or "will" occur. Forward-looking statements are based on the opinions and estimates of management at the dates the statements are made, and are subject to a variety of risks and uncertainties and other factors that could cause actual events or results to differ materially from those projected in the forward-looking statements. These factors include the Company's expectations of sufficient liquidity and capital resources to meets its ongoing obligations and future contractual commitments; the estimates and assumptions included in the Company's impairment analysis; the outcome of the government, regulatory and internal investigations; the outcome of a review of the dry coal-handling facility and its future contribution to the Company's product strategy; the inherent risks involved in the exploration and development of mineral properties, the uncertainties involved in interpreting drilling results and other geological data, fluctuating commodity prices, the possibility of project cost overruns or unanticipated costs and expenses, uncertainties related to completion results of planned exploration and development programs on the Company's material properties, issuance of licenses and permits and the availability of and costs of financing needed in the future and other factors described in this discussion under the heading "Outlook". Except as required by law, the Company undertakes no obligation to update forward-looking statements if circumstances or management's estimates or opinions should change. The reader is cautioned not to place undue reliance on forward-looking statements.

TABLE OF CONTENTS

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

1. INTRODUCTION AND RESTATEMENT

This restated Management's Discussion and Analysis of Financial Condition and Results of Operations ("MD&A") of SouthGobi Resources Ltd. (which, together with its subsidiaries, is collectively referred to as the "Company" or "SouthGobi") should be read in conjunction with the consolidated financial statements of SouthGobi and the notes thereto for the year ended December 31, 2012 (restated). Details of the restatement referred to below are provided in Note 2 to the consolidated financial statements for the year ended December 31, 2012. SouthGobi's financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") issued by the International Accounting Standards Board ("IASB") and Interpretations of the IFRS Interpretations Committee ("IFRIC").

Financial statement restatement

On November 8, 2013, the Company's Board of Directors approved the decision to restate the Company's financial statements for 2011 and 2012, and the related MD&A. The restatement follows a review by the Company of its prior revenue recognition practices for its coal sales in the fourth quarter of 2010, full year 2011 and in the first half of 2012.

As a result of this review, the Company determined that certain revenue transactions were previously recognized in the Company's consolidated financial statements prior to meeting relevant revenue recognition criteria. The restatement is due to a change in the determination of when revenue should be recognized from its sales of coal previously recognized in the fourth quarter of 2010, full year 2011 and in the first half of 2012. These transactions relate to coal that had been delivered to the customer's stockpile in a stockyard located within the SouthGobi Ovoot Tolgoi mining license area ("the Stockyard"), the location at which title transferred, but from which the coal had not been collected by the customers. The restatement of the Company's consolidated financial statements reflects a correction in the point of revenue recognition from: (A) the delivery of coal to the customer stockpiles within the Stockyard to (B) the loading of coal onto the customer's trucks at the time of collection.

The Company adopted new terms in its sales contracts starting in the second half of 2012 such that title transfers when coal is loaded onto the customer's trucks which results in the latter point of revenue recognition for all its sales starting from the second half of 2012.

As a result of the material effects on the Company's consolidated financial statements, the consolidated financial statements, auditors' reports and related financial information for the affected periods contained in the Company's filings filed prior to November 14, 2013 should no longer be relied upon.

1. INTRODUCTION AND RESTATEMENT (Continued)

Restated financial statement and MD&A presentation

In the consolidated financial statements for the year ended December 31, 2012, the Company has restated the financial position at December 31, 2012, December 31, 2011 and January 1, 2011, the results of operations for the years ended December 31, 2012 and December 31, 2011 and the statement of changes in equity and statement of cash flows for the years ended December 31, 2012 and December 31, 2011. Further information on these adjustments and a reconciliation of amounts previously reported is contained in Note 2 of the consolidated financial statements. The financial information and other affected information presented in this MD&A, including financial information pertaining to selected quarterly data of 2012 and 2011, have been restated to give effect to the correction in the point of revenue recognition.

The Company has updated the disclosure presented in the restated consolidated financial statements and this restated MD&A to reflect events occurring subsequent to the original filing.

The Company has included extensive disclosure regarding the periods affected by the restatement in this MD&A, therefore, the Company has not amended and does not intend to amend the annual filings made for the years ended December 31, 2011 or 2010 or the interim filings of the affected years prior to the interim filing for the three and nine months ended September 30, 2013, although restated balances will be presented as comparatives in future filings where appropriate. Accordingly, this restated MD&A should be read in conjunction with the Company's filings that have been filed on or after November 14, 2013, the effective date of the interim filing for the three and nine months ended September 30, 2013.

1. INTRODUCTION AND RESTATEMENT (Continued)

Summary of key impacts of restatement

	Year ended December 31, 2012			Year ended December 31, 2011		
	As previously reported	Adjustment	Restated	As previously reported	Adjustment	Restated
Raw coal production *(millions of tonnes)*	1.33	-	1.33	4.57	-	4.57
Coal sales *(millions of tonnes)*	1.33	0.65	1.98	4.02	(0.93)	3.09
Average realized selling price *(per tonne)*	$ 47.76	$ (0.27)	$ 47.49	$ 54.03	$ (3.39)	$ 50.64
Revenue	$ 53,116	$ 24,945	$ 78,061	$ 179,049	$ (48,293)	$ 130,756
Cost of sales	(97,118)	(30,289)	(127,407)	(127,343)	35,165	(92,178)
Other operating expenses	(54,345)	12,700	(41,645)	(29,189)	872	(28,317)
Net income/(loss)	(103,019)	5,517	(97,502)	57,745	(9,192)	48,552
Basic income/(loss) per share	$ (0.57)	$ 0.03	$ (0.54)	$ 0.32	$ (0.05)	$ 0.27

	December 31, 2012			December 31, 2011		
	As previously reported	Adjustment	Restated	As previously reported	Adjustment	Restated
Trade and other receivables	$ 17,430	$ (14,138)	$ 3,292	$ 80,285	$ (64,051)	$ 16,234
Inventories	53,661	6,074	59,735	52,443	52,418	104,861
Deferred revenue	-	8,181	8,181	-	17,653	17,653

	Year ended December 31, 2010		
	As previously reported	Adjustment	Restated
Raw coal production *(millions of tonnes)*	2.79	-	2.79
Coal sales *(millions of tonnes)*	2.54	(0.81)	1.73
Average realized selling price *(per tonne)*	$ 34.61	$ 3.63	$ 38.24
Revenue	$ 79,777	$ (19,365)	$ 60,412
Cost of sales	(69,904)	17,253	(52,651)
Other operating expenses	(12,643)	218	(12,425)
Net income/(loss)	(116,195)	(1,421)	(117,616)
Basic income/(loss) per share	$ (0.66)	$ (0.01)	$ (0.67)

	December 31, 2010		
	As previously reported	Adjustment	Restated
Trade and other receivables	$ 30,246	$ (10,911)	$ 19,335
Inventories	26,160	17,253	43,413
Deferred revenue	-	10,827	10,827

Following the correction in the Company's point of revenue recognition, revenues from affected coal sales contracts are recognized in later periods than previously reported and some revenue has been reported after December 31, 2012 as not all contracted coal has been collected by customers. This change results in lower revenues and cost of sales in 2010 and 2011 followed by higher revenues and cost of sales in 2012.

The adjustments to other operating expenses in each applicable period primarily result from the reversal of provisions for doubtful trade and other receivables in those periods.

1. INTRODUCTION AND RESTATEMENT (Continued)

The impact on the net income/(loss) for the restated periods follows from the restated revenues, net of cost of sales and adjustments to other operating expenses. The net loss for the year 2010 increases, the net income for the year 2011 decreases and the net loss for the year 2012 decreases.

During the periods from 2010 to December 31, 2012, trade and other receivables have been adjusted lower and deferred revenue recognized to reflect revenue being recorded in later periods than previously reported. The inventory balance increased over the same period to reflect higher coal inventory stockpile balances. Prepaid expenses also increased, with a corresponding decrease in trade and other payables, as coal sales royalty expenses were recognized in later periods than previously reported. Further information on these adjustments and a reconciliation of amounts previously reported is contained in Note 2 of the consolidated financial statements.

The restatements do not result in a change in cash at the end of any period. The statement of cash flows as reported does not change except for the reclassification of various items within operating activities. Financing activities, investing activities, change in cash, cash at the beginning of period and cash at the end of period remain unchanged from previously filed financial statements.

Internal controls over financial reporting

In conjunction with the matter described above, the Company's management has identified a material weakness in the Company's internal controls over financial reporting as of December 31, 2012 and December 31, 2011, resulting in the failure to properly account for revenues in complex transactions. Specifically, the Company did not ensure that all aspects of sales arrangements were considered in the determination of the appropriate accounting for contracts in which the specified location of transfer of title in the contracts is the customer's stockpile in a stockyard located within the SouthGobi Ovoot Tolgoi mining license area. As a result of the material weakness, the Company's Chief Executive Officer and Chief Financial Officer have concluded that internal controls over financial reporting were not effective as of December 31, 2012 and December 31, 2011.

Management has been enhancing internal controls over financial reporting by developing a more thorough review process in evaluating complex sales arrangements in each reporting period. The remedial controls that have now been implemented must operate for a sufficient period of time before management can conclude, through testing, that these controls are effective. Management expects this to be achieved by December 31, 2013.

2. OVERVIEW

SouthGobi is an integrated coal mining, development and exploration company. SouthGobi's common shares trade on the Toronto Stock Exchange ("TSX") under the symbol SGQ and on the Hong Kong Stock Exchange ("HKEX") under the stock code symbol 1878.

The Company's immediate parent company is Turquoise Hill Resources Ltd. ("Turquoise Hill") and at December 31, 2012, Turquoise Hill owned approximately 58% of the outstanding common shares of the Company. Turquoise Hill is controlled by Rio Tinto plc ("Rio Tinto").

The Company owns the following significant coal projects in Mongolia: the Ovoot Tolgoi open pit coal mine ("Ovoot Tolgoi Mine") and three development projects, the Soumber Deposit, the Zag Suuj Deposit and the Ovoot Tolgoi Underground Deposit. These projects are located in the Umnugobi Aimag (South Gobi Province) of Mongolia, within 150 kilometers ("km") of each other and in close proximity to the Mongolia-China border.

The Ovoot Tolgoi Mine, together with the Ovoot Tolgoi Underground Deposit, forms the Ovoot Tolgoi Complex. The Ovoot Tolgoi Complex is separated into two distinct areas, the Sunrise and Sunset Pits.

The Ovoot Tolgoi Mine, strategically located approximately 40km from the Shivee Khuren-Ceke crossing at the Mongolia-China border ("Shivee Khuren Border Crossing"), is the Company's flagship asset. SouthGobi commenced mining at the Ovoot Tolgoi Mine in April 2008 and commenced coal sales in September 2008. Saleable products from the Ovoot Tolgoi Mine will primarily be based on a two product strategy and will consist of SouthGobi standard ("Standard") and SouthGobi premium ("Premium") semi-soft coking coal products. The Standard and Premium semi-soft coking coal products will be produced from raw semi-soft coking coals, together with raw medium and higher-ash coals which can be washed and blended into the Standard and Premium semi-soft coking coal products. Some higher-ash product will be sold as a thermal coal product as required. The Ovoot Tolgoi Mine is covered by a single 9,308 hectare ("ha") mining license and a corresponding permit to mine.

The Soumber Deposit, comprising the Central Soumber, East Soumber, Biluut, South Biluut and Jargalant Fields, is located approximately 20km east of the Ovoot Tolgoi Mine, which will allow any future mining operation at the Soumber Deposit to share existing infrastructure with the Ovoot Tolgoi Mine. A National Instrument 43-101 ("NI 43-101") compliant resource has been established and exploration results indicate potential for thick coking coal seams. The Mineral Resources Authority of Mongolia ("MRAM") has issued the Company a 10,993ha mining license pertaining to the Soumber Deposit.

2. OVERVIEW (Continued)

In addition to the existing mining license, the Company also holds two exploration licenses pertaining to the Soumber Deposit for which pre-mining agreements ("PMAs") have been issued. The Company has applied for a mining license on the area covered by the PMA issued on January 18, 2013. The Company plans to progress to the mining license application process for the PMA issued on August 14, 2013 (refer to Section 4.1 "withdrawal of notice of investment dispute" for additional information).

The Zag Suuj Deposit is located approximately 150km east of the Ovoot Tolgoi Mine and approximately 80km north of the Mongolia-China border. A NI 43-101 compliant resource has been established for the Zag Suuj Deposit. Exploration results indicate potential for thick coal seams and it is anticipated that the coals from the Zag Suuj Deposit can be washed to produce a coking coal or coking coal blend product. The Company holds two exploration licenses pertaining to the Zag Suuj Deposit for which PMAs have been issued. The PMAs were issued on August 14, 2013 and the Company plans to progress to the mining license application process (refer to Section 4.1 "withdrawal of notice of investment dispute" for additional information).

The Company has conducted substantial exploration activities at the Ovoot Tolgoi Underground Deposit and has delineated mineral resources. The Ovoot Tolgoi Underground Deposit is covered by the existing Ovoot Tolgoi mining license.

As at December 31, 2012, SouthGobi owned 19.9% of Aspire Mining Limited ("Aspire"), a company listed on the Australian Securities Exchange under the symbol AKM. Aspire's primary focus is its Mongolian coal assets, particularly those pertaining to the Ovoot Coking Coal Project.

2.1 Significant Events

Mining activities at the Ovoot Tolgoi Mine were curtailed to varying degrees in the second quarter of 2012, with mining activities being fully curtailed at the end of the second quarter, to manage coal inventories and to maintain efficient working capital levels. Mining activities remained fully curtailed for the remainder of 2012; however, operations at the Ovoot Tolgoi Mine resumed on March 22, 2013. The Company continues to minimize uncommitted capital expenditures and exploration expenditures in order to preserve the Company's financial resources.

2. OVERVIEW (Continued)

Sales volumes and revenue declined to 1.98 million tonnes and $78.1 million, respectively, in 2012 compared to 3.09 million tonnes and $130.8 million in 2011. In 2012, the Company's operations were impacted by infrastructure constraints in Mongolia, the significant uncertainty resulting from regulatory issues facing the Company and the softening of inland China coking coal markets.

On February 13, 2012, the Company announced the successful commissioning of the dry coal-handling facility ("DCHF") at the Ovoot Tolgoi Mine. The DCHF has capacity to process nine million tonnes of run-of-mine ("ROM") coal per year. The DCHF includes a 300-tonne-capacity dump hopper, which receives ROM coal from the Ovoot Tolgoi Mine and feeds a coal rotary breaker that sizes coal to a maximum of 50 millimeters ("mm") and rejects oversize ash. The objective of the DCHF is to reduce screening costs and improve yield recoveries. A review of the DCHF, including the upgrade to the DCHF, and its future contribution to the Company's product strategy is ongoing. The total construction capital investment at September 30, 2013 was $85.0 million. An impairment loss on the DCHF may be recorded depending on the outcome of the review.

On April 2, 2012, SouthGobi announced that it had signed a cooperation agreement with the Aluminum Corporation of China Limited ("CHALCO") and received official notification of CHALCO's intention to make a proportional takeover bid for up to 60% of the issued and outstanding common shares of SouthGobi at Cdn$8.48 per share. Subsequently, on September 3, 2012, SouthGobi was notified that CHALCO's proportional takeover bid had been terminated, which also resulted in the termination of the cooperation agreement (refer to Section 10 for additional information).

On April 16, 2012, SouthGobi announced that MRAM held a press conference announcing a request to suspend exploration and mining activity on certain licenses owned by SouthGobi Sands LLC, a wholly-owned subsidiary of SouthGobi Resources Ltd. SouthGobi never received formal notification from MRAM requesting to suspend any of the Company's licenses. On September 6, 2012, the Company received a letter from MRAM confirming that as of September 4, 2012 all exploration and mining licenses held by the Company were in good standing.

On May 29, 2012, SouthGobi announced the opening of expanded border crossing infrastructure at the Shivee Khuren Border Crossing. The eight new border gates, exclusively for coal transportation, will significantly increase the capacity for exportation of coal from Mongolia to China.

On June 19, 2012, the Company announced that a ribbon cutting ceremony had been held to commemorate the start of construction on the new paved coal highway from the Ovoot Tolgoi Complex to the Shivee Khuren Border Crossing.

2. OVERVIEW (Continued)

On July 11, 2012, the Company announced that SGQ Coal Investment Pte. Ltd., a wholly-owned subsidiary of SouthGobi Resources Ltd. that owns 100% of the Company's Mongolian operating subsidiary SouthGobi Sands LLC, filed a Notice of Investment Dispute on the Government of Mongolia pursuant to the Bilateral Investment Treaty between Singapore and Mongolia. On August 22, 2013, the Company announced that it had withdrawn the Notice of Investment Dispute with the Government of Mongolia in recognition of the fact that the dispute was resolved following the grant of three PMAs on August 14, 2013, and the earlier grant of a PMA on January 18, 2013 pertaining to the Soumber Deposit. The PMAs relate to the Zag Suuj Deposit and certain areas associated with the Soumber Deposit (refer to Section 4.1 "withdrawal of notice of investment dispute" for additional information).

On September 4, 2012, SouthGobi announced changes to its Board of Directors, accepting the resignations of Mr. Edward Flood, the Honorable Robert Hanson and Mr. Peter Meredith (Chairman) and subsequently appointing Ms. Kay Priestly (Chairman), Mr. Sean Hinton (Deputy Chairman), Mr. Lindsay Dove, Mr. Brett Salt and Mr. Kelly Sanders. On September 17, 2012, Mr. Alexander Molyneux tendered his resignation as a director of the Company. Further, on November 8, 2012, Mr. Ross Tromans was appointed as an Executive Director.

In the third and fourth quarters of 2012, the Company also announced senior management changes with the departures of Mr. Alexander Molyneux, former President and Chief Executive Officer, Mr. Curtis Church, former Chief Operating Officer and Mr. Matthew O'Kane, former Chief Financial Officer. Mr. Tromans was appointed as President and Chief Executive Officer. Mr. Tromans also assumed the duties formerly handled by the Chief Operating Officer. On March 28, 2013, SouthGobi announced the appointment of Bertrand Troiano as its Chief Financial Officer, effective April 8, 2013.

On March 25, 2013, SouthGobi announced updated NI 43-101 compliant resource estimates for the Soumber and Zag Suuj Deposits, which increased the Company's total measured and indicated resources to 533 million tonnes (8% increase) and inferred resources to 302 million tonnes (24% increase).

On July 16, 2013, SouthGobi announced the appointment of Enkh-Amgalan Sengee as President and Executive Director of SouthGobi Sands LLC, effective July 15, 2013.

On July 31, 2013, SouthGobi announced the appointment of Brett Salt as Chief Commercial Officer and his resignation as a non-executive director, effective August 1, 2013.

On September 3, 2013, the Company announced the appointment of Bold Baatar as a non-executive director of the Company.

3. SELECTED ANNUAL INFORMATION

($ in thousands, except per share information)

	Year ended December 31,		
	2012 (i)	**2011 (i)**	**2010 (i)**
Revenue	**$ 78,061**	$ 130,756	$ 60,412
Gross profit/(loss)	**(49,346)**	38,578	7,761
Net income/(loss)	**(97,502)**	48,552	(117,616)
Net income/(loss) per share - basic	**(0.54)**	0.27	(0.67)
Net loss per share - diluted	**(0.60)**	(0.24)	(0.67)
Adjusted net loss (ii)	**(36,292)**	(21,009)	(50,629)
Cash and cash equivalents	**19,674**	123,567	492,038
Short term investments	**15,000**	-	17,529
Long term investments			
Money market investments	**-**	44,967	45,173
Other long term investments (iii)	**24,084**	54,271	62,243
Total assets	**732,452**	918,680	968,682
Total long term liabilities	**103,771**	145,607	252,527

(i) Restated, see Section 1 of this MD&A and Note 2 to the consolidated financial statements for the year ended December 31, 2012 (restated).
(ii) A non-IFRS financial measure, see Section 6.
(iii) As at December 31, 2012, other long term investments include a $1.5 million investment in Kangaroo Resources Ltd. ("Kangaroo"), a $8.7 million investment in Aspire and a $13.9 million investment in RDCC LLC ("RDCC").

Mining activities at the Ovoot Tolgoi Mine were curtailed to varying degrees in the second quarter of 2012, with mining activities being fully curtailed at the end of the second quarter, to manage coal inventories and to maintain efficient working capital levels. Mining activities remained fully curtailed for the remainder of 2012; however, operations at the Ovoot Tolgoi Mine resumed on March 22, 2013.

In 2012, SouthGobi recorded revenue of $78.1 million compared to $130.8 million in 2011 and $60.4 million in 2010. In 2012, the Company's operations were impacted by infrastructure constraints in Mongolia, the significant uncertainty resulting from regulatory issues facing the Company and the softening of inland China coking coal markets. These issues led to decreased sales volumes and decreased selling prices for individual coal products.

In 2012, the Company's gross loss was negatively impacted by $53.0 million of idled mine costs, resulting in a gross loss of $49.3 million. The Company recorded a gross profit excluding idled mine costs of $3.7 million in 2012 compared to a gross profit excluding idled mine costs of $38.6 million in 2011 and $7.8 million in 2010. Gross profit excluding idled mine costs will vary by year depending on sales volumes, sales prices and unit costs.

3. SELECTED ANNUAL INFORMATION (Continued)

The Company recorded a net loss of $97.5 million in 2012 compared to a net income of $48.6 million in 2011 and a net loss of $117.6 million in 2010. In 2010, $250.0 million of the China Investment Corporation ("CIC") convertible debenture was converted to common shares resulting in a $151.4 million non-cash loss on partial conversion of the debt.

The Company's 2012 net loss includes a gross loss of $49.3 million (2011: gross profit of $38.6 million), other operating expenses of $41.6 million (2011: $28.3 million), administration expenses of $24.6 million (2011: $28.7 million) and evaluation and exploration expenses of $8.6 million (2011: $31.8 million). The Company's 2012 net loss also includes financing costs related to the CIC convertible debenture. In 2012, the fair value change of the embedded derivatives in the CIC convertible debenture resulted in a non-cash gain of $39.5 million (2011: $106.5 million gain).

Adjusted net loss (a non-IFRS financial measure, see Section 6) was $36.3 million in 2012 compared to $21.0 million in 2011 and $50.6 million in 2010. Adjusted net loss increased compared to 2011 primarily due to decreased gross profits excluding idled mine costs and coal stockpile impairments, mainly as a result of lower sales volumes and lower sales prices, and an increased proportion of interest expense on the CIC convertible debenture being expensed as opposed to capitalized, partially offset by lower exploration costs.

The Company's total assets at December 31, 2012 were $732.5 million compared to $918.7 million at December 31, 2011 and $968.7 million at December 31, 2010. At December 31, 2012, the Company had $19.7 million in cash, $15.0 million in short term money market investments and $24.1 million in long term investments compared to $123.6 million in cash and $99.2 million in long term investments at December 31, 2011. Long term investments include $nil of money market investments (2011: $45.0 million), a $1.5 million investment in Kangaroo (2011: $7.4 million), a $8.7 million investment in Aspire (2011: $46.8 million) and a $13.9 million investment in RDCC (2011: $nil). The decrease in cash from 2011 primarily resulted from the purchase of property, plant and equipment for the Ovoot Tolgoi Mine. These purchases were committed prior to operations being fully curtailed at the end of the second quarter of 2012.

The Company's long term liabilities at December 31, 2012 were $103.8 million compared to $145.6 million at December 31, 2011 and $252.5 million at December 31, 2010. The decrease in the long term liabilities is primarily due to the $39.5 million and $106.5 million fair value change of the embedded derivatives in the CIC convertible debenture in 2012 and 2011, respectively.

4. MINERAL PROPERTIES

4.1 Mongolian Coal Division

SouthGobi currently holds three mining licenses and four exploration licenses, which in total cover an area of approximately 325,000ha. The mining licenses pertain to the Ovoot Tolgoi Complex, the Soumber Deposit and the Tsagaan Tolgoi Deposit.

In addition to the existing mining license, the Company also holds two exploration licenses (9443X and 9449X) pertaining to certain areas associated with the Soumber Deposit for which PMAs have been issued. The Company holds two exploration licenses (13779X and 5267X) pertaining to the Zag Suuj Deposit for which PMAs have been issued.

Unless stated otherwise, the Company owns a 100% interest in its coal projects.

Regulatory Issues

Status of Mining and Exploration Licenses

On April 16, 2012, SouthGobi announced that MRAM held a press conference announcing a request to suspend exploration and mining activity on certain licenses owned by SouthGobi Sands LLC. The request for suspension included the mining license pertaining to the Ovoot Tolgoi Mine.

The Company believed that the action was taken under the broad national security powers of the Government of Mongolia. MRAM stated that the move was in connection with the proposed proportional takeover bid by CHALCO and the agreement by Turquoise Hill to tender its controlling interest in SouthGobi to such a takeover. On September 3, 2012, the proposed proportional takeover bid by CHALCO was terminated (refer to Section 10 for additional information).

Subsequently, on September 6, 2012, the Company received official notification from MRAM confirming that as of September 4, 2012 all exploration and mining licenses held by the Company were in good standing. On August 22, 2013, SouthGobi announced that it had withdrawn the Notice of Investment Dispute in recognition of the fact that the dispute was resolved following the grant of three PMAs on August 14, 2013 relating to the Zag Suuj Deposit and certain areas associated with the Soumber Deposit, and the earlier grant of a PMA on January 18, 2013 pertaining to the Soumber Deposit. Each of the PMAs was granted and executed by MRAM in accordance with Mongolian law (refer to Section 4.1 "withdrawal of notice of investment dispute" for additional information).

4. MINERAL PROPERTIES (Continued)

Governmental, Regulatory and Internal Investigations

The Company is subject to investigations by the IAAC and the Mongolian State Investigation Office (the "SIA") regarding allegations against SouthGobi and some of its former employees. The IAAC investigation concerns possible breaches of Mongolia's anti-corruption laws, while the SIA investigation concerns possible breaches of Mongolia's money laundering and taxation laws.

While the IAAC investigation into allegations of possible breaches of Mongolian anti-corruption laws has been suspended, the Company has not received notice that the IAAC investigation is complete. To date, four former SouthGobi employees have been named as suspects in the IAAC investigation and are subject to a continuing travel ban imposed by the IAAC. The IAAC has not formally accused any current or former SouthGobi employees of breach of Mongolia's anti-corruption laws.

The SIA has not accused any current or former SouthGobi employees of money laundering. However, three former SouthGobi employees have been informed that they have each been designated as "accused" in connection with the allegations of tax evasion, and are subject to a travel ban. The Company has been designated as a "civil defendant" in connection with the tax evasion allegations, and it may potentially be held financially liable for the criminal misconduct of its former employees under Mongolian Law. The Company has shown full cooperation with the investigation by providing relevant information. The relevant authorities are yet to conclude on this information. Accordingly, the likelihood or consequences for the Company of a judgment against its former employees is unclear at this time.

The SIA also continues to enforce administrative restrictions, which were initially imposed by the IAAC investigation, on certain of the Company's Mongolian assets, including local bank accounts, in connection with its continuing investigation of these allegations. While the orders restrict the use of in-country funds pending the outcome of the investigation, they are not expected to have a material impact on the Company's activities in the short term, although they could create potential difficulties for the Company in the medium to long term. SouthGobi will continue to take all appropriate steps to protect its ability to conduct its business activities in the ordinary course.

4. MINERAL PROPERTIES (Continued)

Certain of the allegations raised by the SIA and IAAC against SouthGobi (concerning allegations of bribery, money laundering and tax evasion) have been the subject of public statements and Mongolian media reports, both prior to and in connection with the recent trial, conviction, and unsuccessful appeal of the former Chairman and the former director of the Geology, Mining and Cadastral Department of the MRAM, and others. SouthGobi was not a party to this case. The Company understands that the court process is now concluded following the decision of the Supreme Court of Mongolia to uphold the convictions. As far as the Company is aware from publicly available information, the court concluded that the transfer of one of SouthGobi Sands LLC's licenses (5261X) involved government officials and violated applicable Mongolian anti-corruption laws. License 5261X was transferred to an entity nominated by MRAM, after the license had been reinstated by MRAM for this purpose, in exchange for MRAM renewing certain SouthGobi Sands LLC licenses (5259X, 5277X, 12388X and 9442X) that were due to expire. As a result the court invalidated the transfer of 5261X and cancelled the other licenses. At that time only one of the licenses at issue (9442X) was held by SouthGobi Sands LLC, with the other licenses having earlier been allowed to lapse when they were determined not to be prospective. The Company considers that it was entitled under applicable law to the renewal of the relevant licenses and that it received reasonable payment for the transfer of license 5261X.

Through its Audit Committee (comprised solely of independent directors), SouthGobi is conducting an internal investigation into possible breaches of law, internal corporate policies and codes of conduct arising from the allegations which have been raised. The Audit Committee has the assistance of independent legal counsel in connection with its investigation.

The Chair of the Audit Committee is also participating in a tripartite committee, comprised of the Audit Committee Chairs of the Company and Turquoise Hill and a representative of Rio Tinto, which is focused on the investigation of a number of those allegations, including possible violations of anti-corruption laws. Independent legal counsel and forensic accountants have been engaged by this committee to assist it with its investigation. The tripartite committee substantially completed the investigative phase of its activities during the third quarter of 2013. The Company continues to cooperate with the IAAC, SIA and with Canadian and United States government and regulatory authorities that are monitoring the Mongolian investigations. It is possible that these authorities may subsequently conduct their own review or investigation or seek further information from the Company and until all such reviews or investigations are complete the Audit Committee's and the tripartite committee's work may be considered ongoing.

4. MINERAL PROPERTIES (Continued)

The investigations referred to above could result in one or more Mongolian, Canadian, United States or other governmental or regulatory agencies taking civil or criminal action against the Company, its affiliates or its current or former employees. The likelihood or consequences of such an outcome are unclear at this time but could include financial or other penalties, which could be material, and which could have a material adverse effect on the Company. Refer to the risk factor, "the Company is subject to continuing governmental, regulatory and internal investigations, the outcome of which is unclear at this time but could have a material adverse effect on the Company", in Section 14.

The Company, through its Board of Directors and new management, has taken a number of steps to address issues noted during the investigations and to focus ongoing compliance by employees with all applicable laws, internal corporate policies and codes of conduct, and with the Company's disclosure controls and procedures and internal controls over financial reporting.

Withdrawal of Notice of Investment Dispute

On July 11, 2012, SouthGobi announced that SGQ Coal Investment Pte. Ltd., a wholly-owned subsidiary of SouthGobi Resources Ltd. that owns 100% of the Company's Mongolian operating subsidiary SouthGobi Sands LLC, filed a Notice of Investment Dispute on the Government of Mongolia pursuant to the Bilateral Investment Treaty between Singapore and Mongolia. The Company filed the Notice of Investment Dispute following a determination by management that they had exhausted all other possible means to resolve an ongoing investment dispute between SouthGobi Sands LLC and the Mongolian authorities.

The Notice of Investment Dispute principally concerned the failure by MRAM to execute the PMAs associated with certain exploration licenses of the Company pursuant to which valid PMA applications had been lodged in 2011. The areas covered by the valid PMA applications included the Zag Suuj Deposit and certain areas associated with the Soumber Deposit outside the existing mining license.

On August 22, 2013, SouthGobi announced that it had withdrawn the Notice of Investment Dispute in recognition of the fact that the dispute was resolved following the grant of three PMAs on August 14, 2013 relating to the Zag Suuj Deposit and certain areas associated with the Soumber Deposit, and the earlier grant of a PMA on January 18, 2013 pertaining to the Soumber Deposit. Each of the PMAs was granted and executed by MRAM in accordance with Mongolian law.

4. MINERAL PROPERTIES (Continued)

Mining Prohibition in Specified Areas Law

Pursuant to the Mining Prohibition in Specified Areas Law, the Government of Mongolia has defined the boundaries of certain areas in which exploration and mining is purportedly prohibited. A list of licenses has been prepared that overlap with the prohibited areas described in the law based on information submitted by water authority agencies, forest authority agencies and local authorities for submission to the Government of Mongolia.

Portions of the Company's Ovoot Tolgoi and Tsagaan Tolgoi mining licenses and exploration licenses pertaining to the Zag Suuj Deposit and the South Biluut and Jargalant Fields within the Soumber Deposit are included on the list of licenses published by the Government of Mongolia, potentially affecting the status of those licenses under the Mining Prohibition in Specified Areas Law.

In regard to the Ovoot Tolgoi mining license, the potential area which may be affected is a relatively small area which represents approximately 3% of the entire area of the mining license and does not contain any of the Company's NI 43-101 reserves or resources or immovable assets. Accordingly, the loss of the potentially affected area would not materially and adversely affect the existing operations.

Activities historically carried out on the other licenses referred to above include drilling, trenching and geological reconnaissance. The Company has no immovable assets located in any of the potentially affected areas of these licenses and the loss of any or all of these potentially affected properties would not materially and adversely affect the existing operations.

The Company understands that the status of the Mining Prohibition in Specified Areas Law is unclear and it has not been enforced to date. Reports from Mongolia suggest that the law may be amended. The Company will continue to monitor developments and will ensure that it is fully compliant with Mongolian law.

Operating Mines

Ovoot Tolgoi Mine

The Ovoot Tolgoi Mine is located in the southwest corner of the Umnugobi Aimag (South Gobi Province) of Mongolia. The deposit is within the administrative unit of Gurvantes Soum, 270km southwest of the provincial capital of Dalanzadgad and 700km southwest of the nation's capital of Ulaanbaatar. To date, mining operations at the Ovoot Tolgoi Mine have been carried out in two distinct areas, the Sunset Pit to the west and the Sunrise Pit to the east.

4. MINERAL PROPERTIES (Continued)

Saleable products from the Ovoot Tolgoi Mine will primarily be based on a two product strategy and will consist of Standard and Premium semi-soft coking coal products. The Standard and Premium semi-soft coking coal products will be produced from raw semi-soft coking coals, together with raw medium and higher-ash coals which can be washed and blended into the Standard and Premium semi-soft coking coal products. Some higher-ash product will be sold as a thermal coal product as required.

Reserves and Resources

On March 19, 2012, the Company announced an updated NI 43-101 compliant independent resource estimate prepared by RungePincockMinarco ("RPM"). RPM estimated that the Ovoot Tolgoi Mine contains 175.7 million tonnes of proven and probable surface coal reserves, 133.3 million tonnes of measured coal resources, 59.9 million tonnes of indicated coal resources and 24.0 million tonnes of inferred coal resources as at October 31, 2011. All of these resources are located above 300m and are amenable to surface mining. The mineral resources are inclusive of mineral reserves. Details of the assumptions and parameters used to calculate the reserves, resources and coal quality estimates and information on data verification are set out in the Annual Information Form dated March 25, 2013, and available at www.sedar.com.

The coal rank at the Ovoot Tolgoi Mine is high volatile B to A bituminous based on the ASTM D388 standard. High volatile B produces between 7,212 to 7,785 kcal/kg and high volatile A produces greater than 7,785 kcal/kg heat output.

Select Financial and Operational Data

On March 22, 2013, SouthGobi announced the resumption of operations at the Ovoot Tolgoi Mine after having been fully curtailed since the end of the second quarter of 2012. The 2013 mine plan assumes a conservative resumption of operations, designed to achieve a cost effective approach that will allow operations to continue on a sustainable basis and align production levels with forecast market conditions. The Company is focused on delivering on its commercial strategy and targets.

4. MINERAL PROPERTIES (Continued)

	Year ended December 31, 2012 (i)	Year ended December 31, 2011 (i)
Volumes, Prices and Costs		
Raw coal production *(millions of tonnes)*	**1.33**	4.57
Coal sales *(millions of tonnes)*	**1.98**	3.09
Average realized selling price *(per tonne)* (ii)	**$ 47.49**	$ 50.64
Direct cash costs of product sold excluding idled mine costs *(per tonne)* (iii)	**$ 16.86**	$ 22.81
Total cash costs of product sold excluding idled mine costs *(per tonne)* (iii)	**$ 20.01**	$ 23.93
Operating Statistics		
Production waste material moved *(millions of bank cubic meters)*	**3.36**	16.61
Strip ratio *(bank cubic meters of waste material per tonne of coal produced)*	**2.52**	3.63
Pre-production waste material moved *(millions of bank cubic meters)*	**-**	1.68
Operating Results *($ in thousands)*		
Revenue	**$ 78,061**	$ 130,756
Cost of sales		
Mine operations	**74,449**	92,178
Idled mine costs	**52,958**	-
Gross profit/(loss)	**$ (49,346)**	$ 38,578

(i) Restated, see Section 1 of this MD&A and Note 2 to the consolidated financial statements for the year ended December 31, 2012 (restated).
(ii) Average realized selling price excludes royalties and selling fees.
(iii) A non-IFRS financial measure, see Section 6.

In 2012, the Company produced 1.33 million tonnes of raw coal with a strip ratio of 2.52 compared to production of 4.57 million tonnes of raw coal with a strip ratio of 3.63 in 2011. The decrease in production primarily related to the curtailment of the Company's mining operations in the last three quarters of the year; whereas, the decrease in the strip ratio primarily related to the below-trend strip ratio in the first quarter of 2012 which will be normalized over the life-of-mine.

In 2012, the Company sold 1.98 million tonnes of coal at an average realized selling price of $47.49 per tonne compared to sales of 3.09 million tonnes of coal at an average realized selling price of $50.64 per tonne in 2011. The Company's average realized selling price was negatively impacted by the softening of the inland China coking coal markets closest to SouthGobi's operations throughout 2012. The Company's higher-ash coals were impacted more substantially than its other products.

4. MINERAL PROPERTIES (Continued)

Revenue decreased to $78.1 million in 2012 from $130.8 million in 2011 primarily due to decreased sales volumes and lower average realized selling prices.

In the last three quarters of 2012, customers were reluctant to enter into new sales contracts primarily due to the following:

- Customers' ability to export coal through the Shivee Khuren Border Crossing for the first half of 2012 was significantly below their projections due to: a) the delayed opening of the expanded border crossing infrastructure at the Shivee Khuren Border Crossing; b) the extended closure of the Shivee Khuren Border Crossing for the Chinese New Year and Mongolian Tsagaan Sar public holidays in the first quarter of 2012; c) the closure of the existing gravel road used to transport coal from the Ovoot Tolgoi Mine and neighboring mines to the Shivee Khuren Border Crossing for over four weeks in the second quarter of 2012;
- The uncertainty with respect to whether SouthGobi would receive a formal request from MRAM to suspend mining activities on its Ovoot Tolgoi mining license, which caused customers concern that they would be unable to collect and export additional coal purchased from the Ovoot Tolgoi Mine in the second and third quarters of 2012; and
- The softening of inland China coking coal markets closest to SouthGobi's operations throughout the last three quarters of 2012.

Revenues are presented net of royalties and selling fees. The Company is subject to a 5% royalty on all coal sales exported out of Mongolia based on a set reference price per tonne published monthly by the Government of Mongolia. Effective January 1, 2011, the Company is also subject to a sliding scale additional royalty of up to 5% on coal sales exported out of Mongolia based on the set reference price. Based on the 2012 reference prices, the Company was subject to an average 8% royalty based on a weighted average reference price of $88.07 per tonne. The Company's effective royalty rate for 2012, based on the Company's average realized selling price of $47.49 per tonne, was 15%.

4. MINERAL PROPERTIES (Continued)

SouthGobi, together with other Mongolian mining companies impacted by the escalation of effective royalty rates, opened a dialog with the appropriate Government of Mongolia authorities with a view of moving to a more equitable process for setting reference prices. Effective October 1, 2012 (for a six month trial period), the royalty was determined using the contracted sales price per tonne, not the reference price per tonne published by the Government of Mongolia. As a result, the Company's effective royalty rate was reduced significantly over the six month trial period. Despite SouthGobi, together with other Mongolian mining companies, engaging the appropriate Government of Mongolia authorities, the six month trial period was not extended and effective April 1, 2013, the royalty on all coal sales exported out of Mongolia was once again based on a set reference price per tonne published monthly by the Government of Mongolia.

In the fourth quarter of 2012 (a full quarter under the trial period), the Company's effective royalty rate was 6%, a significant reduction from prior quarters in 2012.

Cost of sales was $127.4 million in 2012 compared to $92.2 million in 2011. Cost of sales comprise the direct cash costs of product sold, mine administration cash costs of product sold, idled mine costs, inventory impairments, equipment depreciation, depletion of mineral properties and share-based compensation expense. Of the $127.4 million recorded as cost of sales in 2012, $74.4 million related to mine operations and $53.0 million related to idled mine costs. Cost of sales related to mine operations decreased in 2012 compared to 2011 primarily due to lower sales volumes and lower unit costs, partially offset by coal stockpile impairments totaling $20.5 million. Cost of sales related to idled mine costs primarily consist of period costs, which are expensed as incurred, and depreciation expense. The depreciation expense relates to the Company's idled plant and equipment.

Direct cash costs of product sold excluding idled mine costs (a non-IFRS financial measure, see Section 6) were $16.86 per tonne in 2012 compared to $22.81 per tonne in 2011. Direct cash costs of product sold excluding idled mine costs primarily decreased due to a lower strip ratio and reduced fuel prices.

Mine administration cash costs of product sold excluding idled mine costs (a non-IFRS financial measure, see Section 6) increased to $3.15 per tonne in 2012 from $1.12 per tonne in 2011 due to increased mine administration costs being allocated over lower sales volumes.

4. MINERAL PROPERTIES (Continued)

Processing Infrastructure

On February 13, 2012, the Company announced the successful commissioning of the DCHF at the Ovoot Tolgoi Mine. The DCHF has capacity to process nine million tonnes of ROM coal per year. The DCHF includes a 300-tonne-capacity dump hopper, which receives ROM coal from the Ovoot Tolgoi Mine and feeds a coal rotary breaker that sizes coal to a maximum of 50mm and rejects oversize ash. The objective of the DCHF is to reduce screening costs and improve yield recoveries.

The Company has received all permits to operate the DCHF. The 2013 mine plan considered limited utilization of the DCHF at the latter end of 2013, however there is now no plan to use the DCHF in 2013 due to higher quality coals being mined that likely will not require processing through the DCHF. The Company has delayed construction to upgrade the DCHF to include dry air separation modules and covered load out conveyors with fan stackers to take processed coals to stockpiles and enable more efficient blending. Uncommitted capital expenditures have been minimized to preserve the Company's financial resources.

A review of the DCHF, including the upgrade to the DCHF, and its future contribution to the Company's product strategy is ongoing. The total construction capital investment to date is $85.0 million. An impairment loss on the DCHF may be required depending on the outcome of the review.

To further enhance product value, in 2011, the Company entered into an agreement with Ejinaqi Jinda Coal Industry Co. Ltd. ("Ejin Jinda"), a subsidiary of China Mongolia Coal Co. Ltd to toll-wash coals from the Ovoot Tolgoi Mine. The agreement has a duration of five years from commencement and provides for an annual wet washing capacity of approximately 3.5 million tonnes of input coal. Pursuant to the terms of the agreement, the Company prepaid $33.6 million of toll washing fees.

Ejin Jinda's wet washing facility is located approximately 10km inside China from the Shivee Khuren Border Crossing, approximately 50km from the Ovoot Tolgoi Mine. Primarily, medium and higher-ash coals with only basic processing through Ovoot Tolgoi's on-site DCHF will be transported from the Ovoot Tolgoi Mine to Ejin Jinda's wet washing facility under a separate transportation agreement. Ejin Jinda will charge the Company a single toll washing fee which will cover their expenses, capital recovery and profit.

Based on preliminary studies, the Company expected coals processed through Ovoot Tolgoi's on-site DCHF to then be washed to produce coals with ash in the range of 8% to 11% at a yield of 85% to 90% that generally meet semi-soft coking coal specifications. However, the Company is currently reassessing these preliminary studies and is currently cooperating with Ejin Jinda in studying the utilization of the wet washing facility.

4. MINERAL PROPERTIES (Continued)

Construction of Ejin Jinda's wet washing facility is now complete and it has been connected to utility supply. To date, the delay in commencing wet washing coals has had no impact on the carrying value of the Company's prepaid toll washing fees of $33.6 million.

Transportation Infrastructure

On August 2, 2011, the State Property Committee of Mongolia awarded the tender to construct a paved highway from the Ovoot Tolgoi Complex to the Shivee Khuren Border Crossing to consortium partners NTB LLC and SouthGobi Sands LLC (together referred to as "RDCC"). SouthGobi Sands LLC holds a 40% interest in RDCC. On October 26, 2011, RDCC signed a concession agreement with the State Property Committee of Mongolia. RDCC has the right to conclude a 17 year build, operate and transfer agreement under the Mongolian Law on Concessions. Construction on the paved highway re-commenced in the second quarter of 2013 and remains ongoing. During the third quarter of 2013, a sub-contractor employee was fatally injured by a vehicle at the construction site. Following the fatality, additional safety training was carried out by RDCC and its sub-contractors in order to reinforce compliance with safety protocols.

Construction of the paved highway is expected to be substantially complete by the end of 2013. The remaining construction work and commissioning of the paved highway is expected to be completed by the end of the first half of 2014.

The paved highway will have an intended carrying capacity upon completion in excess of 20 million tonnes of coal per year.

A north-south railway line currently connects Ceke with Jiayuguan City in Gansu Province and with the interior of China. Another east-west railway line connects Ceke to Linhe, an industrial city in eastern Inner Mongolia. This line has a stated initial transportation capacity of approximately 15 million tonnes per year, with a planned increase to 25 million tonnes per year.

Mining Equipment

The key elements of the currently commissioned mining fleet includes: two Liebherr 996 ($34m^3$) hydraulic excavators, three Liebherr R9250 ($15m^3$) hydraulic excavators, 22 Terex MT4400 (218 tonne capacity) haul trucks and two Terex TR100 (91 tonne capacity) haul trucks, together with various pieces of ancillary equipment.

SouthGobi has secured mining capacity to achieve an annual production level of approximately 7.2 million tonnes in 2014, though the Company's 2013 mine plan does fully utilize its existing mining fleet.

4. MINERAL PROPERTIES (Continued)

Workforce

As at December 31, 2012, SouthGobi Sands LLC employed 451 employees, of which only 269 were active due to the curtailment of the mining operations. Of the 451 employees, 61 are employed in the Ulaanbaatar office, 3 in outlying offices and 388 at the Ovoot Tolgoi Mine site. Of the total 451 employees based in Mongolia, 443 (98%) are Mongolian nationals and of those, 226 (50%) are residents of the local Gurvantes, Dalanzadgad, Sevrei and Noyon Soums.

Development Projects

Soumber Deposit

The Soumber Deposit, comprising the Central Soumber, East Soumber, Biluut, South Biluut and Jargalant Fields, is located approximately 20km east of the Ovoot Tolgoi Mine. It lies within the administrative units of Gurvantes and Noyon Soums in the Umnugobi Aimag (South Gobi Province), approximately 50km northeast of the Shivee Khuren Border Crossing. The proximity of the Soumber Deposit to the Ovoot Tolgoi Mine will allow any future mining operation at the Soumber Deposit to share existing infrastructure with the Ovoot Tolgoi Mine.

The Central and East Soumber Fields include six major seam groups. Approximately 40% of the resources are contained in one seam, averaging 5.9m in thickness. All seam groups consist of a number of coal plies of highly variable thickness, separated by stone partings. Interburden between the seam groups is mainly sandstone and conglomerate, whilst partings within the seam groups tend to be dominated by mudstone and carbonaceous mudstone.

Three major seams have been identified at the Biluut, South Biluut and Jargalant Fields. Correlation of these seams with the Central and East Soumber Fields has not been undertaken. Approximately 60% of the resources are contained in one seam, averaging 5.5m in thickness.

On March 25, 2013, the Company reported an updated NI 43-101 compliant independent resource estimate prepared by RPM. RPM estimated that the Soumber Deposit contains measured coal resources of 62.4 million tonnes, indicated coal resources of 110.3 million tonnes and inferred coal resources of 123.0 million tonnes as at January 10, 2013. Approximately 76% of the Soumber Deposit resource is located above 300m and is amenable to surface mining.

4. MINERAL PROPERTIES (Continued)

The increase in resource estimate when compared to the previous NI 43-101 compliant independent resource estimate prepared by RPM was identified by RPM when reviewing the technical data for the resources in the course of on-going mine planning studies for the Company. These studies included the reconciliation of RPM Minescape and McElroy Bryan Geological Services Pty Ltd ("MBGS") Minex models. This reconciliation identified aggregation anomalies which resulted in an increase in the resource estimates that were originally reported. Details of the assumptions and parameters used to calculate the resources and coal quality estimates and information on data verification are set out in the Annual Information Form dated March 25, 2013, and available at www.sedar.com.

The coal rank at the Soumber Deposit is low to medium volatile bituminous based on the ASTM D388 standard producing between 5,000 to 7,800 kcal/kg of heat output. Laboratory data demonstrated that some of the coal benches exhibit potential coking coal characteristics.

On July 6, 2011, SouthGobi announced that MRAM issued the Company a mining license pertaining to the Soumber Deposit. The 10,993ha mining license was granted for an initial term of 30 years with an option for two 20 year extensions. In addition to the existing mining license, the Company also holds two exploration licenses pertaining to certain areas associated with the Soumber Deposit for which PMAs have been issued. The Company has applied for a mining license on the area covered by the PMA issued on January 18, 2013. The Company plans to progress to the mining license application process for the PMA issued on August 14, 2013 (refer to Section 4.1 "withdrawal of notice of investment dispute" for additional information).

Environmental baseline studies have been completed and general environmental impact assessments have been approved. The Company has delayed a pre-feasibility study for the Soumber Deposit, pertaining to resources located above 300m, to the first half of 2014; however, the Company will work to continue to further define the Soumber Deposit in the fourth quarter of 2013. The Company also continues to delay studying the feasibility of building a coal preparation plant for the Soumber Deposit coals to preserve the Company's financial resources and is reviewing other alternatives.

Zag Suuj Deposit

The Zag Suuj Deposit, located approximately 150km east of the Ovoot Tolgoi Mine and approximately 80km north of the Mongolia-China border, lies within the administrative units of Noyon and Bayandalai Soums in the Umnugobi Aimag (South Gobi Province).

4. MINERAL PROPERTIES (Continued)

Based on the exploration results to date, the coal occurrence at the Zag Suuj Deposit can be divided into four major seam groups. Each of the seam groups split into a number of coal plies of highly variable thickness, separated by stone partings. Interburden between the seams is mainly sandstone and conglomerate, whilst partings within the seams tend to be dominated by mudstone and carbonaceous mudstone. Correlation of the coal seams at the Zag Suuj Deposit with the Ovoot Tolgoi Complex and the Soumber Deposit has not been undertaken.

Several of the seams at the Zag Suuj Deposit have an average free swell index greater than 5, indicating metallurgical properties; however, limited metallurgical testing has been undertaken to date.

On March 25, 2013, the Company reported an updated NI 43-101 compliant independent resource estimate for the Zag Suuj Deposit prepared by RPM. RPM estimated that the Zag Suuj Deposit contains indicated coal resources of 21.5 million tonnes and inferred coal resources of 84.0 million tonnes as at January 10, 2013. The entire Zag Suuj resource is located above 300m and is amenable to surface mining.

The increase in resource estimate when compared to the previous NI 43-101 compliant independent resource estimate prepared by RPM was identified by RPM when reviewing the technical data for the resources in the course of on-going mine planning studies for the Company. These studies included the reconciliation of RPM Minescape and MBGS Minex models. This reconciliation identified aggregation anomalies which resulted in an increase in the resource estimates that were originally reported. Details of the assumptions and parameters used to calculate the resources and coal quality estimates and information on data verification are set out in the Annual Information Form dated March 25, 2013, and available at www.sedar.com.

The coal rank at the Zag Suuj Deposit ranges between low to medium volatile bituminous coal based on the ASTM D388 standard. The average calorific value for individual coal seams ranges between 5,600 and 6,100 kcal/kg (ad).

The Company holds two exploration licenses pertaining to the Zag Suuj Deposit for which PMAs were issued on August 14, 2013 by MRAM. The Company plans to progress to the mining license application process for the PMAs (refer to Section 4.1 "withdrawal of notice of investment dispute" for additional information).

It is anticipated that coals from the Zag Suuj Deposit can be washed to produce a coking coal product or a coking coal blend product. Limited exploration activities are planned for the Zag Suuj Deposit in 2013. Exploration activities will ensure to meet the requisite requirements under the Mongolian Minerals Law.

4. MINERAL PROPERTIES (Continued)

Ovoot Tolgoi Underground Deposit

The Ovoot Tolgoi Underground Deposit is contiguous to, and located directly below, the Ovoot Tolgoi Mine. The entire extension of the coal at depth from 300m to 600m that is designated for potential underground development is located inside the existing Ovoot Tolgoi mining license.

On March 19, 2012, the Company announced an updated NI 43-101 compliant independent resource estimate prepared by RPM. RPM estimated that the Ovoot Tolgoi Underground Deposit contains measured coal resources of 65.8 million tonnes, indicated coal resources of 43.3 million tonnes and inferred coal resources of 62.0 million tonnes as at October 31, 2011. Details of the assumptions and parameters used to calculate the resources and coal quality estimates and information on data verification are set out in the Annual Information Form dated March 25, 2013, and available at www.sedar.com.

The coal rank at the Ovoot Tolgoi Underground Deposit is high volatile B to A bituminous based on the ASTM D388 standard. High volatile B produces between 7,212 to 7,785 kcal/kg and high volatile A produces greater than 7,785 kcal/kg heat output.

The Company has indefinitely delayed studies to determine the feasibility and economics of conducting an underground mining operation at the Ovoot Tolgoi Underground Deposit.

Tsagaan Tolgoi Deposit

The Tsagaan Tolgoi Deposit is located in south-central Mongolia. The property is located in the Umnugobi Aimag (South Gobi Province) approximately 570km south of Ulaanbaatar and 113km southeast of the provincial capital of Dalanzadgad, and approximately 115km west of Oyu Tolgoi.

In February 2008, Norwest estimated 23.4 million tonnes of measured coal resources, 13.0 million tonnes of indicated coal resources and 9.0 million tonnes of inferred coal resources. The coal is of volatile B to C bituminous rank based on ASTM D388 standards and is suitable for use as a thermal coal. Details of the assumptions and parameters used to calculate these coal resources and coal quality estimates are set out in the Technical Report entitled, "Coal Geology and Resources – Tsagaan Tolgoi Property" dated March 25, 2008, and available at www.sedar.com.

Effective August 12, 2009, the Government of Mongolia issued a mining license for the Tsagaan Tolgoi Deposit. The Technical and Economic Study has been completed and was approved by the Government of Mongolia on March 4, 2010. The Detailed Environmental Impact Assessment was approved on April 9, 2010.

4. MINERAL PROPERTIES (Continued)

On March 5, 2012, SouthGobi announced an agreement to sell the Tsagaan Tolgoi Deposit to Modun Resources Limited ("Modun"), a company listed on the Australian Securities Exchange under the symbol MOU. Under the transaction, SouthGobi expected to receive $30.0 million of total consideration, comprising $7.5 million up-front in cash, $12.5 million up-front in Modun shares and deferred consideration of an additional $10.0 million also payable in Modun shares. Subsequently, on August 29, 2012, SouthGobi announced that the proposed sale of the Tsagaan Tolgoi Deposit to Modun had been cancelled by mutual agreement of both parties. The Company is evaluating its strategic options with respect to the Tsagaan Tolgoi Deposit.

Investments

Aspire

As at December 31, 2012, SouthGobi owned 19.9% of Aspire, a company listed on the Australian Securities Exchange under the symbol AKM. Aspire's primary focus is its Mongolian coal assets, particularly those pertaining to the Ovoot Coking Coal Project. The Company's interest in Aspire was primarily acquired through a placement in December 2010 whereby SouthGobi acquired a 19.9% interest in Aspire for $20.3 million. On October 12, 2011, Aspire completed a private placement issuing 80 million additional common shares. SouthGobi participated in the placement, exercising its right to maintain its 19.9% ownership interest. On February 21, 2013, Aspire completed a private placement, diluting SouthGobi's interest to 18.8%. As at December 12, 2013, SouthGobi has invested a total of $27.9 million in Aspire and its interest in Aspire has a market value of $6.8 million.

On August 28, 2012, Aspire announced that it had received a mining license for the Ovoot Coking Coal Project. On December 6, 2012, Aspire announced that a pre-feasibility study review was completed for the Ovoot Coking Coal Project. Based on information provided by Aspire, coking coal from the Ovoot Coking Coal Project has been classified as a low ash quality blending feedstock for coke manufacture. Indicative washed coking coal average specifications are an ash content of 9%, volatiles of 25-28% and crucible swelling number of 9. Subsequently, on July 31, 2013, Aspire announced an upgraded JORC compliant reserve and resource estimate of 255.0 million tonnes of probable coal reserves, 197.0 million tonnes of measured coal resources, 72.3 million tonnes of indicated coal resources and 11.8 million tonnes of inferred coal resources. Coal resources are inclusive of coal reserves.

4. MINERAL PROPERTIES (Continued)

Exploration Program

Exploration expenses in 2012 were $8.6 million compared to $31.8 million in 2011. Exploration expenses will vary period to period depending on the number of projects and the related seasonality of the exploration programs. The 2012 exploration program was suspended in the second quarter of 2012 in order to preserve the Company's financial resources while mining operations at the Ovoot Tolgoi Mine were curtailed, with the exception of certain water exploration activities and minimum exploration activities required on exploration licenses held by the Company.

The 2012 exploration program originally planned to include further drilling of prospective greenfields exploration properties, as well as the broader Ovoot Tolgoi Complex, the Soumber Deposit and the Zag Suuj Deposit. The Company also planned to complete a pre-feasibility study for its Soumber Deposit and continue its detailed water exploration program.

The Company's 2013 exploration program is focused on further defining the Soumber Deposit. Other exploration activities are limited to ensuring that the Company meets the Mongolian Minerals Law requirements. The Company is also continuing its water exploration program throughout 2013.

4.2 Administrative and Other

Other operating expenses in 2012 increased to $41.6 million compared to $28.3 million in 2011. The increase in other operating expenses primarily relates to an impairment loss on available-for-sale financial assets, partially offset by reduced public infrastructure costs.

In 2012, the Company recorded $35.5 million of provisions and impairments in other operating expenses related to the following:

- Trade and other receivables – the Company recorded a loss provision of $1.0 million in 2012. The loss provision relates to a reduction in expected insurance proceeds of $1.0 million.
- Available-for-sale financial asset – in 2012, the Company determined that objective evidence of impairment in the Company's investment in Aspire existed. Therefore, an impairment loss of $19.2 million was recognized in other operating expenses.

4. MINERAL PROPERTIES (Continued)

- Property, plant and equipment – the Company recorded $15.2 million of impairment charges to reduce various items of property, plant and equipment to their recoverable amounts. The impairment charges consist of a $14.1 million impairment pertaining to non-refundable prepayments made on cancelled mobile equipment orders to preserve the Company's financial resources and a $1.1 million impairment of construction in progress expenditures that were not expected to be recovered.

Public infrastructure costs decreased in 2012 compared to 2011 due to reduced maintenance costs on transportation infrastructure from the Ovoot Tolgoi Mine to the Shivee Khuren Border Crossing and reduced works on the expanded border crossing infrastructure at the Shivee Khuren Border Crossing.

In 2011, other operating expenses primarily consisted of a $16.6 million impairment charge on various capitalized construction projects and $8.1 million of public infrastructure costs.

Administration expenses in 2012 were $24.6 million compared to $28.7 million in 2011. The decrease in administration expenses primarily related to reduced corporate administration and share-based compensation expense, partially offset by increased legal and professional fees. Legal and professional fees were higher due to additional legal fees as a result of the CHALCO proportional takeover bid (refer to Section 10 for additional information), the Notice of Investment Dispute (refer to Section 4.1 "withdrawal of notice of investment dispute" for additional information) and in support of the ongoing investigations (refer to Section 4.1 "governmental, regulatory and internal investigations" for additional information).

5. SUMMARY OF QUARTERLY RESULTS

($ in thousands, except per share information unless otherwise indicated)

	2012 (i)				2011 (i)				2010 (i)
QUARTER ENDED	**31-Dec**	30-Sep	30-Jun	31-Mar	31-Dec	30-Sep	30-Jun	31-Mar	31-Dec
Revenue	**$ 1,186**	$ 3,804	$ 46,575	$ 26,497	$ 33,626	$ 50,616	$ 25,966	$ 20,547	$ 22,230
Gross profit/(loss) excluding idled mine costs	**(12,601)**	(8,719)	20,277	4,657	4,639	16,129	8,769	9,040	$ 1,838
Gross profit margin excluding idled mine costs	***-1063%***	*-229%*	*44%*	*18%*	*14%*	*32%*	*34%*	*44%*	*8%*
Gross profit/(loss) including idled mine costs	**(31,043)**	(27,650)	4,690	4,657	4,639	16,129	8,769	9,040	1,838
Other operating expenses	**(19,282)**	(18,315)	(1,344)	(2,702)	(24,426)	80	(2,806)	(1,165)	(1,903)
Administration expenses	**(6,080)**	(5,178)	(7,497)	(5,882)	(8,612)	(7,993)	(6,808)	(5,336)	(6,599)
Evaluation and exploration expenses	**(508)**	(958)	(2,099)	(5,033)	(14,513)	(10,908)	(4,356)	(1,991)	(4,144)
Income/(loss) from operations	**(56,913)**	(52,101)	(6,250)	(8,961)	(42,912)	(2,692)	(5,201)	548	(10,808)
Net income/(loss)	**(56,564)**	(46,413)	15,955	(10,480)	(27,732)	54,955	66,755	(45,426)	(30,140)
Basic income/(loss) per share	**(0.31)**	(0.26)	0.09	(0.06)	(0.16)	0.29	0.36	(0.25)	(0.17)
Diluted income/(loss) per share	**(0.31)**	(0.26)	(0.04)	(0.06)	(0.18)	(0.03)	(0.01)	(0.25)	(0.17)

	2012 (i)				2011 (i)				2010 (i)
QUARTER ENDED	**31-Dec**	30-Sep	30-Jun	31-Mar	31-Dec	30-Sep	30-Jun	31-Mar	31-Dec
Raw coal production *(millions of tonnes)*	**-**	-	0.27	1.07	1.34	1.25	0.87	1.11	1.38
Sales volumes and prices (ii)									
SouthGobi premium semi-soft coking coal									
Coal sales *(millions of tonnes)*	**0.03**	-	0.42	0.33	0.26	0.56	0.39	0.34	0.35
Average realized selling price *(per tonne)* (iii)	**$ 47.86**	$ -	$ 67.46	$ 67.58	$ 66.91	$ 66.73	$ 65.83	$ 56.50	$ 47.08
SouthGobi standard semi-soft coking coal									
Coal sales *(millions of tonnes)*	**-**	0.01	0.36	0.10	0.26	0.20	-	-	-
Average realized selling price *(per tonne)* (iii)	**$ -**	$ 49.91	$ 49.74	$ 49.43	$ 48.48	$ 48.17	$ -	$ -	$ -
SouthGobi thermal coal									
Coal sales *(millions of tonnes)*	**-**	0.31	0.28	0.15	0.37	0.41	0.17	0.13	0.31
Average realized selling price *(per tonne)* (iii)	**$ -**	$ 15.87	$ 34.10	$ 30.29	$ 29.92	$ 35.49	$ 29.00	$ 31.10	$ 26.24
Total									
Coal sales *(millions of tonnes)*	**0.03**	0.32	1.06	0.58	0.89	1.17	0.56	0.47	0.65
Average realized selling price *(per tonne)* (iii)	**$ 47.86**	$ 16.98	$ 52.86	$ 54.60	$ 46.18	$ 52.55	$ 54.66	$ 49.49	$ 37.31
Costs									
Direct cash costs of product sold excluding idled mine costs *(per tonne)* (iv)	**$ 11.67**	$ 9.56	$ 16.52	$ 22.09	$ 24.70	$ 21.69	$ 22.01	$ 16.79	$ 8.58
Total cash costs of product sold excluding idled mine costs *(per tonne)* (iv)	**$ 16.75**	$ 13.31	$ 17.85	$ 28.25	$ 25.92	$ 22.31	$ 23.57	$ 18.43	$ 10.20
Waste movement and stripping ratio									
Production waste material moved *(millions of bank cubic meters)*	**-**	-	1.16	2.20	4.58	4.10	4.08	3.85	3.56
Strip ratio *(bank cubic meters of waste material per tonne of coal produced)*	**-**	-	4.31	2.07	3.42	3.28	4.74	3.47	2.58
Pre-production waste material moved *(millions of bank cubic meters)*	**-**	-	-	-	-	0.39	0.80	0.49	0.73
Other operating capacity statistics									
Capacity									
Number of mining shovels/excavators available at period end	**5**	4	4	3	3	3	4	3	3
Total combined stated mining shovel/excavator capacity at period end *(cubic meters)*	**113**	98	98	64	64	64	98	83	82
Number of haul trucks available at period end	**27**	27	27	27	25	16	16	16	15
Total combined stated haul truck capacity at period end *(tonnes)*	**4,743**	4,743	4,743	4,743	4,561	2,599	2,599	2,599	2,254
Employees and safety									
Employees at period end	**465**	644	693	720	720	695	658	600	544
Lost time injury frequency rate (v)	**0.1**	0.2	0.2	0.3	0.2	0.2	0.1	0.1	0.2

(i) Restated, see Section 1 of this MD&A and Note 2 to the consolidated interim financial statements (restated) for the year ended December 31, 2012.
(ii) The sales volumes previously disclosed as raw semi-soft coking coal, raw medium-ash coal and raw higher-ash coal have now been reclassified as SouthGobi premium semi-soft coking coal, SouthGobi standard semi-soft coking coal and SouthGobi thermal coal, respectively, to reflect the Company's new product strategy.
(iii) Average realized selling price excludes royalties and selling fees.
(iv) A non-IFRS financial measure, see Section 6.
(v) Per 200,000 man hours.

5. SUMMARY OF QUARTERLY RESULTS (Continued)

Summary of key impacts of restatement on quarterly results

	Three months ended December 31, 2012			Three months ended September 30, 2012		
	As previously reported	Adjustment	Restated	As previously reported	Adjustment	Restated
Raw coal production *(millions of tonnes)*	-	-	-	-	-	-
Coal sales *(millions of tonnes)*	0.03	-	0.03	0.31	0.01	0.32
Average realized selling price *(per tonne)*	$ 47.86	$ -	$ 47.86	$ 15.79	$ 1.19	$ 16.98
Revenue	$ 1,213	$ (27)	$ 1,186	$ 3,337	$ 467	$ 3,804
Cost of sales	(26,549)	(5,680)	(32,229)	(30,869)	(585)	(31,454)
Other operating expenses	(18,664)	(618)	(19,282)	(29,301)	10,986	(18,315)
Net income/(loss)	(51,818)	(4,746)	(56,564)	(54,564)	8,151	(46,413)
Basic income/(loss) per share	$ (0.28)	$ (0.03)	$ (0.31)	$ (0.30)	$ 0.04	$ (0.26)

	Three months ended June 30, 2012			Three months ended March 31, 2012		
	As previously reported	Adjustment	Restated	As previously reported	Adjustment	Restated
Raw coal production *(millions of tonnes)*	0.27	-	0.27	1.07	-	1.07
Coal sales *(millions of tonnes)*	0.16	0.90	1.06	0.84	(0.26)	0.58
Average realized selling price *(per tonne)*	$ 62.56	$ (9.70)	$ 52.86	$ 56.79	$ (2.19)	$ 54.60
Revenue	$ 8,412	$ 38,163	$ 46,575	$ 40,153	$ (13,656)	$ 26,497
Cost of sales	(22,221)	(19,663)	(41,884)	(17,479)	(4,361)	(21,840)
Other operating expenses	(3,803)	2,459	(1,344)	(2,578)	(124)	(2,702)
Net income/(loss)	237	15,718	15,955	3,126	(13,606)	(10,480)
Basic income/(loss) per share	$ -	$ 0.09	$ 0.09	$ 0.02	$ (0.08)	$ (0.06)

	Three months ended December 31, 2011			Three months ended September 30, 2011		
	As previously reported	Adjustment	Restated	As previously reported	Adjustment	Restated
Raw coal production *(millions of tonnes)*	1.34	-	1.34	1.25	-	1.25
Coal sales *(millions of tonnes)*	1.15	(0.26)	0.89	1.37	(0.20)	1.17
Average realized selling price *(per tonne)*	$ 55.51	$ (9.33)	$ 46.18	$ 54.01	$ (1.46)	$ 52.55
Revenue	$ 51,064	$ (17,438)	$ 33,626	$ 60,492	$ (9,876)	$ 50,616
Cost of sales	(34,427)	5,440	(28,987)	(42,856)	8,369	(34,487)
Other operating expenses	(24,644)	218	(24,426)	(138)	218	80
Net income/(loss)	(18,897)	(8,835)	(27,732)	55,921	(966)	54,955
Basic income/(loss) per share	$ (0.10)	$ (0.06)	$ (0.16)	$ 0.31	$ (0.02)	$ 0.29

	Three months ended June 30, 2011			Three months ended March 31, 2011		
	As previously reported	Adjustment	Restated	As previously reported	Adjustment	Restated
Raw coal production *(millions of tonnes)*	0.87	-	0.87	1.11	-	1.11
Coal sales *(millions of tonnes)*	1.05	(0.49)	0.56	0.45	0.02	0.47
Average realized selling price *(per tonne)*	$ 54.06	$ 0.60	$ 54.66	$ 50.29	$ (0.80)	$ 49.49
Revenue	$ 47,336	$ (21,370)	$ 25,966	$ 20,158	$ 389	$ 20,547
Cost of sales	(37,592)	20,395	(17,197)	(12,468)	961	(11,507)
Other operating expenses	(3,024)	218	(2,806)	(1,383)	218	(1,165)
Net income/(loss)	67,323	(568)	66,755	(46,602)	1,176	(45,426)
Basic income/(loss) per share	$ 0.37	$ (0.01)	$ 0.36	$ (0.25)	$ 0.00	$ (0.25)

5. SUMMARY OF QUARTERLY RESULTS (Continued)

		Three months ended				
		December 31, 2010				
		As previously reported		Adjustment		Restated
Raw coal production *(millions of tonnes)*		1.38		-		1.38
Coal sales *(millions of tonnes)*		1.47		(0.81)		0.65
Average realized selling price *(per tonne)*	$	31.56	$	5.75	$	37.31
Revenue	$	41,595	$	(19,365)	$	22,230
Cost of sales		(37,645)		17,253		(20,392)
Other operating expenses		(2,121)		218		(1,903)
Net income/(loss)		(28,720)		(1,421)		(30,140)
Basic income/(loss) per share	$	(0.16)	$	(0.01)	$	(0.17)

The changes in comparative results of operations on a quarter over quarter basis are due primarily to fluctuations in the following areas:

In the fourth quarter of 2012, the Company's mining activities remained fully curtailed; however, the Company generated revenue through the sale of existing coal stockpiles. The Company recognized revenue of $1.2 million in the fourth quarter of 2012 compared to $3.8 million in the third quarter of 2012 and $33.6 million in the fourth quarter of 2011. The significant decrease in revenue in the fourth and third quarters of 2012 compared to the fourth quarter of 2011 can be attributed to decreased sales volume.

SouthGobi's effective royalty rate in the fourth quarter of 2012 was 6%, a significant reduction from prior quarters in 2012. Effective October 1, 2012 (for a six month trial period) the royalty rate was determined using the contracted sales price per tonne, not the reference price per tonne published by the Government of Mongolia. Despite SouthGobi, together with other Mongolian mining companies, engaging the appropriate Government of Mongolia authorities, the six month trial period was not extended and effective April 1, 2013, the royalty on all coal sales exported out of Mongolia was once again based on a set reference price per tonne published monthly by the Government of Mongolia. Although discussions have not been successful to date, SouthGobi, together with other Mongolian mining companies, continue the dialog with the appropriate Government of Mongolia authorities with the goal of moving to a more equitable process for setting reference prices.

5. SUMMARY OF QUARTERLY RESULTS (Continued)

Cost of sales was $32.2 million in the fourth quarter of 2012 compared to $31.5 million in the third quarter of 2012 and $29.0 million in the fourth quarter of 2011. Cost of sales comprise the direct cash costs of product sold, mine administration cash costs of product sold, idled mine costs, inventory impairments, equipment depreciation, depletion of mineral properties and share-based compensation expense. Of the $32.2 million and $31.5 million recorded as cost of sales in the fourth and third quarters of 2012, $13.8 million and $12.6 million related to mine operations and $18.4 million and $18.9 million related to idled mine costs, respectively. Cost of sales related to mine operations increased in the fourth quarter of 2012 compared to the third quarter of 2012 primarily due to the inclusion of a $15.8 million coal stockpile impairment to reduce the carrying value to its net realizable value. Cost of sales related to mine operations decreased in the fourth quarter of 2012 compared to the fourth quarter of 2011 primarily due to lower sales volumes, partially offset by the coal stockpile impairment.

In the fourth and third quarters of 2012, gross profit was negatively impacted by $18.4 million and $18.9 million of idled mine costs, respectively, contributing to a gross loss of $31.0 million in the fourth quarter of 2012 and $27.7 million in the third quarter of 2012. The Company recorded a gross loss excluding idled mine costs of $12.6 million in the fourth quarter of 2012 compared to a gross loss excluding idled mine costs of $8.7 million in the third quarter of 2012 and a gross profit excluding idled mine costs of $4.6 million in the fourth quarter of 2011. Gross profit will vary by quarter depending on sales volumes, sales prices and unit costs.

Direct cash costs of product sold excluding idled mine costs (a non-IFRS financial measure, see Section 6) were $11.67 per tonne in the fourth quarter of 2012 compared to $9.56 per tonne in the third quarter of 2012 and $24.70 in the fourth quarter of 2011.

Mine administration cash costs of product sold excluding idled mine costs (a non-IFRS financial measure, see Section 6) were $5.08 per tonne in the fourth quarter of 2012 compared to $3.75 per tonne in the third quarter of 2012 and $1.22 in the fourth quarter of 2011. Mine administration cash costs of product sold excluding idled mine costs increased in the fourth quarter of 2012 due to mine administration costs being allocated over lower sales volumes.

Other operating expenses in the fourth quarter of 2012 were $19.3 million compared to $18.3 million in the third quarter of 2012 and $24.4 million in the fourth quarter of 2011. The change in other operating expenses compared to the third quarter of 2012 primarily relates to recognizing a smaller impairment loss on available-for-sale financial assets, partially offset by an increased impairment of property, plant and equipment. The decrease in other operating expenses compared to the fourth quarter of 2011 primarily relates to recognizing a smaller impairment of property, plant and equipment.

5. SUMMARY OF QUARTERLY RESULTS (Continued)

For the three months ended December 31, 2012, the Company recorded $17.2 million of provisions and impairments in other operating expenses related to the following:

- Trade and other receivables – the Company recorded a reduction in the expected insurance proceeds of $1.0 million.
- Available-for-sale financial asset – in the fourth quarter of 2012, the Company determined that objective evidence of impairment in the Company's investment in Aspire existed. Therefore, a further impairment loss of $3.1 million was recognized in other operating expenses.
- Property, plant and equipment – the Company recorded $13.0 million of impairment charges to reduce non-refundable prepayments made on cancelled mobile equipment orders to their recoverable amounts. The mobile equipment orders were cancelled to preserve the Company's financial resources.

Administration expenses in the fourth quarter of 2012 were $6.1 million compared to $5.2 million in the third quarter of 2012 and $8.6 million in the fourth quarter of 2011. Administration expenses increased in the fourth quarter of 2012 compared to the third quarter of 2012 primarily due to increased corporate administration, legal and professional fees and salaries and benefits, partially offset by reduced share-based compensation expenses. Administration expenses decreased in the fourth quarter of 2012 compared to the fourth quarter of 2011 primarily due to decreased salaries and benefits and share-based compensation expenses, partially offset by increased legal and professional fees.

Exploration expenses in the fourth quarter of 2012 were $0.5 million compared to $1.0 million in the third quarter of 2012 and $14.5 million in the fourth quarter of 2011. Exploration expenses will vary from quarter to quarter depending on the number of projects and the related seasonality of the exploration programs. The Company curtailed exploration activities in the fourth and third quarters of 2012 to preserve financial resources. The majority of the exploration activities in these periods related to water exploration activities. Exploration expenses in the fourth quarter of 2011 included a higher proportion of the 2011 exploration program expenses due to delays in receiving required government approvals in the first half of 2011.

Finance costs in the fourth quarter of 2012 were $5.6 million compared to $1.1 million in the fourth quarter of 2011. Finance costs in the fourth quarter of 2012 primarily consisted of $4.8 million of interest expense on the CIC convertible debenture and a $0.7 million unrealized loss on fair value through profit or loss ("FVTPL") investments; whereas, finance costs in the fourth quarter of 2011 primarily consisted of $0.9 million of interest expense on the CIC convertible debenture.

(Expressed in U.S. Dollars)

5. SUMMARY OF QUARTERLY RESULTS (Continued)

Finance income in the fourth quarter of 2012 was $0.7 million compared to $11.0 million in the fourth quarter of 2011. In the fourth quarter of 2012, finance income primarily consisted of a $0.7 million unrealized gain on the fair value change of the embedded derivatives in the CIC convertible debenture; whereas, in the fourth quarter of 2011, finance income primarily consisted of a $10.8 million unrealized gain on the fair value change of the embedded derivatives in the CIC convertible debenture. The fair value of the embedded derivatives in the CIC convertible debenture is driven by many factors including: share price, foreign exchange rates and share price volatility.

In the fourth quarter of 2012, the Company recorded a current income tax expense of $0.1 million related to its Mongolian operations compared to a current income tax recovery of $0.4 million in the fourth quarter of 2011. The Company has recorded a deferred income tax recovery related to deductible temporary differences of $5.1 million in the fourth quarter of 2012 compared to a deferred income tax recovery of $5.0 million in the fourth quarter of 2011.

As a result of the above factors, the Company recorded a net loss of $56.6 million in the fourth quarter of 2012 compared to a net loss of $46.4 million in the third quarter of 2012 and a net loss of $27.7 million in the fourth quarter of 2011.

Adjusted net loss (a non-IFRS financial measure, see Section 6) was $16.9 million in the fourth quarter of 2012 compared to adjusted net loss of $19.4 million in the third quarter of 2012 and adjusted net loss of $10.7 million in the fourth quarter of 2011. Adjusted net loss increased in the fourth quarter of 2012 compared to the fourth quarter of 2011 primarily due to decreased gross profits excluding idled mine costs and coal stockpile impairments, mainly as a result of lower sales volumes, and an increased proportion of interest expense on the CIC convertible debenture being expensed as opposed to capitalized, partially offset by lower exploration costs.

	2012 (i)				2011 (i)				2010 (i)
QUARTER ENDED	**31-Dec**	30-Sep	30-Jun	31-Mar	31-Dec	30-Sep	30-Jun	31-Mar	31-Dec
Net income/(loss)	**$ (56,564)**	$ (46,413)	$ 15,955	$ (10,480)	$ (27,732)	$ 54,955	$ 66,755	$ (45,426)	$ (30,140)
Income/(loss) adjustments, net of tax									
Idled mine costs	**14,474**	13,572	10,966	-	-	-	-	-	-
Share-based compensation expense/(recovery)	**(1,144)**	1,490	4,383	3,799	4,050	4,296	3,349	2,715	3,840
Net impairment loss/(recovery) on assets	**25,375**	23,258	-	-	23,818	(2,925)	-	-	574
Unrealized foreign exchange losses/(gains)	**906**	335	(355)	(794)	(184)	(115)	45	(1,211)	(1,837)
Unrealized loss/(gain) on embedded derivatives in CIC debenture	**(662)**	(12,856)	(26,770)	776	(10,790)	(62,058)	(70,422)	36,780	19,995
Realized loss/(gain) on disposal of FVTPL investments	**15**	-	46	(85)	-	-	-	-	-
Unrealized loss/(gain) on FVTPL investments	**664**	1,197	2,282	339	155	2,449	(3,629)	4,116	(4,375)
Adjusted net income/(loss) (ii)	**(16,935)**	(19,418)	6,507	(6,446)	(10,683)	(3,398)	(3,902)	(3,026)	(11,943)

(i) Restated, see Section 1 of this MD&A and Note 2 to the consolidated financial statements for the year ended December 31, 2012 (restated).
(ii) A non-IFRS financial measure, see Section 6.

6. NON-IFRS FINANCIAL MEASURES

($ in thousands, unless otherwise stated)

The Company has included certain non-IFRS financial measures including "cash costs" and "adjusted net income/(loss)" to supplement its consolidated financial statements, which are presented in accordance with IFRS.

The Company believes that these measures, together with measures determined in accordance with IFRS, provide investors with useful information to evaluate the underlying performance of the Company. Non-IFRS financial measures do not have a standardized meaning prescribed under IFRS and therefore may not be comparable to similar measures employed by other companies. The non-IFRS financial measures are intended to provide additional information and should not be considered in isolation or as substitute for measures of performances prepared in accordance with IFRS.

Cash costs

The Company uses cash costs to describe its cash production costs. Cash costs incorporate all production costs, which include direct and indirect costs of production, with the exception of idled mine costs and non-cash expenses which are excluded. Non-cash adjustments include share-based compensation expense, inventory impairments, depreciation and depletion of mineral properties.

The Company uses this performance measure to monitor its operating cash costs internally and believes this measure provides investors and analysts with useful information about the Company's underlying cash costs of operations. The Company believes that conventional measures of performance prepared in accordance with IFRS do not fully illustrate the ability of its mining operations to generate cash flows. The Company reports cash costs on a sales basis. This performance measure is commonly utilized in the mining industry.

The cash costs of product sold presented below may differ from cash costs of product produced depending on the timing of stockpile inventory turnover.

6. NON-IFRS FINANCIAL MEASURES (Continued)

	Year ended December 31, 2012 (i)	Year ended December 31, 2011 (i)
Cash costs		
Cost of sales per financial statements	**$ 127,407**	$ 92,178
Less non-cash expenses	**(34,778)**	(18,261)
Less non-cash idled mine costs	**(34,300)**	-
Total cash costs	**58,329**	73,917
Less idled mine cash costs	**(18,658)**	-
Total cash costs excluding idled mine costs	**39,671**	73,917
Coal sales *(000's of tonnes)*	**1,983**	3,088
Total cash costs of product sold excluding idled mine costs *(per tonne)*	**$ 20.01**	$ 23.93

	Year ended December 31, 2012 (i)	Year ended December 31, 2011 (i)
Cash costs		
Direct cash costs of product sold excluding idled mine costs *(per tonne)*	**$ 16.86**	$ 22.81
Mine administration cash costs of product sold excluding idled mine costs *(per tonne)*	**3.15**	1.12
Total cash costs of product sold excluding idled mine costs *(per tonne)*	**$ 20.01**	$ 23.93

(i) Restated, see Section 1 of this MD&A and Note 2 to the consolidated financial statements for the year ended December 31, 2012 (restated).

Adjusted net income/(loss)

Adjusted net income/(loss) excludes idled mine costs, share-based compensation expense/(recovery), net impairment loss/(recovery) on assets, unrealized foreign exchange losses/(gains), unrealized loss/(gain) on the fair value change of the embedded derivatives in the CIC convertible debenture, the loss on the partial conversion of the CIC convertible debenture, realized losses/(gains) on the disposal of FVTPL investments and unrealized losses/(gains) on FVTPL investments. The Company excludes these items from net income/(loss) to provide a measure which allows the Company and investors to evaluate the results of the underlying core operations of the Company and its profitability from operations. The items excluded from the computation of adjusted net income/(loss), which are otherwise included in the determination of net income/(loss) prepared in accordance with IFRS, are items that the Company does not consider to be meaningful in evaluating the Company's past financial performance or the future prospects and may hinder a comparison of its period-to-period results.

(Expressed in U.S. Dollars)

6. NON-IFRS FINANCIAL MEASURES (Continued)

	Year ended December 31,		
	2012 (i)	**2011 (i)**	**2010 (i)**
Net income/(loss)	**$ (97,502)**	$ 48,552	$ (117,616)
Income/(loss) adjustments, net of tax			
Idled mine costs	**39,012**	-	-
Share-based compensation expense	**8,528**	14,410	13,260
Net impairment loss on assets	**48,634**	20,893	7,584
Unrealized foreign exchange gains	**91**	(1,465)	(3,703)
Unrealized gain on embedded derivatives in CIC debenture	**(39,512)**	(106,490)	(100,637)
Loss on partial conversion of CIC debenture	**-**	-	151,353
Realized gain on disposal of FVTPL investments	**(24)**	-	-
Unrealized loss/(gain) on FVTPL investments	**4,482**	3,091	(870)
Adjusted net loss	**$ (36,292)**	$ (21,009)	$ (50,629)

(i) Restated, see Section 1of this MD&A and Note 2 to the consolidated financial statements for the year ended December 31, 2012 (restated).

7. LIQUIDITY AND CAPITAL RESOURCES

Liquidity and capital management

The Company has in place a planning, budgeting and forecasting process to help determine the funds required to support the Company's normal operations on an ongoing basis and its expansionary plans.

The Company expects to have sufficient liquidity and capital resources to be able to continue as a going concern until at least December 31, 2013 based on existing capital resources and estimated cash flows from mining operations. Estimated cash flows from mining operations are subject to a number of external market factors including supply and demand and pricing in the coal industry. The Company continues to minimize uncommitted capital expenditures and exploration expenditures in order to preserve the Company's financial resources.

Factors that could impact the Company's liquidity are monitored regularly and include, but are not limited to, Chinese economic growth, market prices of coal, production levels, operating cash costs, capital costs, exchange rates of currencies of countries where the Company operates and exploration and discretionary expenditures. Factors currently creating uncertainty for the Company's operations include coal prices and the ongoing governmental, regulatory and internal investigations (refer to section 4.1 "governmental, regulatory and internal investigations" for additional information).

7. LIQUIDITY AND CAPITAL RESOURCES (Continued)

As at December 31, 2012, the Company had cash of $19.7 million and short term money market investments of $15.0 million for a total of $34.7 million in cash and money market investments compared to cash of $123.6 million and long term money market investments of $45.0 million for a total of $168.6 million in cash and money market investments as at December 31, 2011. Working capital (excess current assets over current liabilities) was $120.4 million as at December 31, 2012 compared to $221.9 million as at December 31, 2011.

As at December 31, 2012, the Company's gearing ratio was 0.14 (December 31, 2011: 0.16), which was calculated based on the Company's long term liabilities to total assets. As at December 31, 2012, the Company is not subject to any externally imposed capital requirements.

Financings

In November 2009, the Company entered into a financing agreement with a wholly owned subsidiary of the CIC for $500 million in the form of a secured, convertible debenture bearing interest at 8.0% (6.4% payable semi-annually in cash and 1.6% payable annually in the Company's shares) with a maximum term of 30 years. The CIC convertible debenture is secured by a charge over the Company's assets and certain subsidiaries. The financing was required primarily to support the accelerated investment program in Mongolia and up to $120 million of the financing could also be used for working capital, repayment of debt due on funding, general and administrative expenses and other general corporate purposes.

On March 29, 2010, the Company exercised its right to call for the conversion of up to $250.0 million of the CIC convertible debenture into 21.5 million shares at a conversion price of $11.64 (Cdn$11.88). As at December 31, 2012, the CIC owned through its indirect wholly owned subsidiary approximately 14% of the Company.

On January 29, 2010, the Company announced that it had closed the global equity offering of 27.0 million common shares of the Company at a price of Cdn$17.00 per common share, for gross proceeds of $437.4 million. On February 26, 2010, the Company announced a partial exercise of the over-allotment option and issued an additional 0.2 million common shares of the Company at a price of Cdn$17.00 per share for gross proceeds of $3.7 million.

7. LIQUIDITY AND CAPITAL RESOURCES (Continued)

At the time of the financings, the Company planned to use the net proceeds to carry out the following activities:

- Expansion of the production capacity at the Company's Ovoot Tolgoi Mine
- Assessment, construction and development of regional transportation infrastructure
- Assessment and construction of value added facilities such as a coal-handling facility and a washing plant
- Exploration and development of the Soumber Deposit
- General exploration, development and acquisition activities
- Working capital, general and administrative expenses and other general corporate purposes

To date, the Company's actual use of such proceeds has not varied from the anticipated use of proceeds at the time of the financing.

Foreign Strategic Sectors Law

The terms of the CIC convertible debenture provide for the 1.6% share interest payment of $4.0 million to be paid annually in common shares of the Company. On May 17, 2012, the Parliament of Mongolia approved a Law on Regulation of Foreign Investment in Business Entities Operating in Sectors of Strategic Importance ("Foreign Strategic Sectors Law") that regulated foreign direct investment into a number of key sectors of strategic importance, which includes mineral resources.

As a result of the Foreign Strategic Sectors Law, the Company expected that it would require parliamentary approval for the shares to be issued for the November 19, 2012 share interest payment to the CIC. As a result, in the first quarter of 2013, the Company settled the 1.6% share interest payment of $4.0 million in cash.

Following amendments to the Foreign Strategic Sectors Law, passed in the second quarter of 2013, the requirement for parliamentary approval was limited to circumstances where a state owned entity is to exceed 49% share ownership of a strategic asset, irrespective of the amount of investment. As a result, the Company is only required to give notice, rather than obtaining parliamentary or other approval, under the Foreign Strategic Sectors Law for the 1.6% share interest payment to the CIC.

7. LIQUIDITY AND CAPITAL RESOURCES (Continued)

On October 3, 2013 Mongolia's foreign investment environment changed again when the Parliament of Mongolia passed the Investment Law to repeal and replace the Foreign Strategic Sectors Law. The Investment Law regulates, amongst other things, investment by Foreign State Owned Entities ("FSOEs") in sectors of strategic importance, which includes mineral resources, by requiring that FSOEs obtain a permit from Mongolia's Ministry of Economic Development if they are to acquire 33% or more of the shareholding of a Mongolian entity operating in a sector of strategic importance. The Company understands that it will not be required to obtain a permit from the Ministry of Economic Development in connection with the 1.6% share interest payment to CIC, unless such share interest payment will result in CIC acquiring 33% or more of the shareholding in the Company. The Company will fully comply with the requirements of the Investment Law in connection with share interest payments.

Interest payment deferral and settlement

During the second quarter of 2013, the Company and the CIC mutually agreed upon a three month deferral of the convertible debenture semi-annual $7.9 million cash interest payment due on May 19, 2013. The Company and the CIC subsequently agreed to an additional deferral of one month, and the cash interest payment became due on September 19, 2013.

On September 19, 2013, the Company settled the $7.9 million amount, plus additional accrued interest of $0.2 million, as follows:

- The Company issued 1.8 million shares to the CIC for the November 19, 2012 1.6% share interest payment, where the number of common shares was based on the 50-day volume-weighted average share price on November 19, 2012 of Cdn$2.16;
- In consideration of the common share issue, the CIC applied the $4.0 million in cash already paid by the Company in the first quarter of 2013 for the November 19, 2012 share interest payment against the amount due on September 19, 2013; and
- The Company paid the remaining $4.1 million balance in cash.

The mutually agreed upon deferral of the cash interest payment, and subsequent settlement in cash and common shares of the Company, did not trigger an event of default and all other terms of the convertible debenture remain unchanged.

On November 21, 2013, the Company issued 3.5 million common shares to settle the $4.0 million November 19, 2013 share interest payment. The number of common shares was based on the 50-day volume-weighted average share price on November 19, 2013 of Cdn$1.21.

7. LIQUIDITY AND CAPITAL RESOURCES (Continued)

Mongolian IAAC investigation

Subsequent to December 31, 2012, the Company was subject to orders imposed by the IAAC which placed restrictions on certain of the Company's Mongolian assets. The orders were imposed on the Company in connection with the IAAC's investigation of the Company. The SIA also continues to enforce the orders on the Company.

The orders placing restrictions on certain of the Company's Mongolian assets could ultimately result in an event of default of the Company's CIC convertible debenture. This matter remains under review by the Company and its advisers but to date, it is the Company's view that this would not result in an event of default as defined under the CIC convertible debenture terms. However, in the event that the orders result in an event of default of the Company's CIC convertible debenture that remains uncured for ten business days, the principal amount owing and all accrued and unpaid interest will become immediately due and payable upon notice to the Company by CIC.

The orders relate to certain items of operating equipment and infrastructure and the Company's Mongolian bank accounts. The orders related to the operating equipment and infrastructure restricts the sale of these items; however, the orders do not restrict the use of these items in the Company's mining activities. The orders related to the Company's Mongolian bank accounts restrict the use of in-country funds. While the orders restrict the use of in-country funds pending outcome of the investigation, they are not expected to have any material impact on the Company's activities.

Cash Flow Highlights

($ in thousands)

	Year ended December 31, 2012	Year ended December 31, 2011
Cash used in operating activities	**$ (26,283)**	$ (70,023)
Cash used in investing activities	**(77,737)**	(270,432)
Cash used in financing activities	**(51)**	(27,574)
Effect of foreign exchange rate changes on cash	**178**	(442)
Decrease in cash for the year	**(103,893)**	(368,471)
Cash balance, beginning of the year	**123,567**	492,038
Cash balance, end of the year	**$ 19,674**	$ 123,567

7. LIQUIDITY AND CAPITAL RESOURCES (Continued)

Cash used in operating activities

Cash used in operating activities for the year ended December 31, 2012 was $26.3 million compared to cash used in operating activities for the year ended December 31, 2011 of $70.0 million. The decreased outflows in 2012 primarily related to reduced working capital requirements partially offset by reduced cash flow from operations.

Cash used in investing activities

Cash used in investing activities was $77.7 million for the year ended December 31, 2012 compared to $270.4 million for the year ended December 31, 2011 primarily due to decreased purchases of property, plant and equipment and long term investments partially offset by decreased proceeds from maturing long term investments and an investment in RDCC.

Cash used in financing activities

Cash used in financing activities was $0.1 million for the year ended December 31, 2012 compared to $27.6 million for the year ended December 31, 2011. In 2012, the Company repurchased $1.0 million of its common shares. This amount was primarily offset by the $0.9 million received from the issuance of common shares and exercise of stock options.

As at December 31, 2012, the Company had a twelve month revolving line of credit facility with Golomt Bank in Mongolia. The maximum draw-down available was $3.5 million and 8.1 billion Mongolian Tugriks (approximately $5.8 million) and the line of credit incurred interest at 11% for any U.S. Dollar amounts outstanding and 12% for any Mongolian Tugrik amounts outstanding. The line of credit was secured by operating equipment in Mongolia to a value of not less than 150% of the total facility amount.

The line of credit facility was used by the Company's Mongolian Coal Division as part of its working capital management. There were no amounts due under the line of credit facility at both December 31, 2012 and December 31, 2011. Subsequent to December 31, 2012, the line of credit facility expired and was not renewed.

7. LIQUIDITY AND CAPITAL RESOURCES (Continued)

Contractual Obligations and Guarantees

Day-to-day mining, expansionary and sustaining capital expenditures as well as administrative operations give rise to commitments for future minimum payments. Consistent with the Company's capital risk management strategy, the Company expects to have sufficient liquidity and capital resources to meet its ongoing obligations and future contractual commitments for at least twelve months from the end of the December 31, 2012 reporting period. The Company expects its liquidity to remain sufficient based on existing capital resources and income from mining operations.

($ in thousands)	As at December 31, 2012			
	Within 1 year	2-3 years	Over 3 years	Total
Capital expenditure commitments	$ 13,105	$ 21,406	$ -	$ 34,511
Operating expenditure commitments (i)	23,226	1,820	-	$ 25,045
Commitments	$ 36,331	$ 23,226	$ -	$ 59,556

(i) Operating expenditure commitments include $17,500 of fees related to the Company's toll wash plant agreement with Ejin Jinda. This amount reflects the minimum expenditure due under this agreement.

Share repurchase program

On June 8, 2010, the Company announced that its Board of Directors authorized a share repurchase program to purchase up to 2.5 million common shares of the Company on each or either of the TSX and the HKEX, in aggregate representing up to 5.0 million common shares of the Company. On June 8, 2011, the Company announced the renewal of its share repurchase program. The share repurchase program concluded on June 14, 2012. As at June 14, 2012, the Company had repurchased 1.6 million shares on the HKEX and 2.8 million shares on the TSX for a total of 4.4 million common shares. The Company cancelled all repurchased shares.

Impairment analysis

As at December 31, 2012, the Company determined that the decline in the Company's common share price and continued curtailment of mining activities at the Ovoot Tolgoi Mine constituted impairment indicators. Therefore, the Company conducted an impairment test whereby the carrying value of the Company's Ovoot Tolgoi Mine cash generating unit was compared to its "value-in-use" using a discounted future cash flow valuation model as at December 31, 2012. The Company's Ovoot Tolgoi Mine cash generating unit carrying value was $588.5 million as at December 31, 2012.

7. LIQUIDITY AND CAPITAL RESOURCES (Continued)

Key estimates and assumptions incorporated in the valuation model included the following:

- Inland Chinese coking coal market coal prices;
- Life-of-mine coal production and operating costs; and
- A discount rate based on an analysis of market, country and company specific factors

The impairment analysis did not result in the identification of an impairment loss and no charge was required as at December 31, 2012. The Company believes that the estimates and assumptions incorporated in the impairment analysis are reasonable; however, the estimates and assumptions are subject to significant uncertainties and judgments.

Financial instruments

The fair value of financial assets and financial liabilities at amortized cost is determined in accordance with generally accepted pricing models based on discounted cash flow analysis or using prices from observable current market transactions. The Company considers that the carrying amount of all its financial assets and financial liabilities recognized at amortized cost in the financial statements approximates their fair value.

The fair values of financial instruments that are traded on an active liquid market are determined with reference to the quoted market prices. The fair value of the Company's investment in the shares of Kangaroo, Aspire and its money market investments are determined using this methodology. The Company's investment in the shares of Kangaroo and its money market investments are classified as FVTPL. The Company's investment in the shares of Aspire is classified as available-for-sale.

The fair values of the embedded derivatives within the CIC convertible debenture are determined using a Monte Carlo simulation. The risks associated with the CIC convertible debenture relate to a potential breach of the Company's obligations under the terms of the CIC convertible debenture. The Company mitigates these risks by ensuring its corporate activities comply with all of its contractual obligations under the CIC convertible debenture.

7. LIQUIDITY AND CAPITAL RESOURCES (Continued)

The fair value of all the other financial instruments of the Company approximates their carrying value because of the demand nature or short-term maturity of these instruments.

	As at	
Financial assets ***($ in thousands)***	**December 31, 2012 (i)**	**December 31, 2011 (i)**
Loans-and-receivables		
Cash	**$ 19,674**	$ 123,567
Trade and other receivables	**3,292**	16,234
Available-for-sale		
Investment in Aspire	**8,727**	46,837
Fair value through profit or loss		
Investment in Kangaroo	**1,455**	7,431
Money market investments	**15,000**	44,967
Total financial assets	**$ 48,148**	$ 239,036
Financial liabilities ***($ in thousands)***		
Fair value through profit or loss		
Convertible debenture - embedded derivatives	**$ 8,876**	$ 48,389
Other-financial-liabilities		
Trade and other payables	**10,216**	43,552
Convertible debenture - debt host	**97,092**	96,997
Total financial liabilities	**$ 116,184**	$ 188,938

(i) Restated, see Section 1 of this MD&A and Note 2 to the consolidated financial statements for the year ended December 31, 2012 (restated).

Net income for the year ended December 31, 2012 and December 31, 2011 included the following amounts of unrealized losses/(gains) from the fair value adjustments to certain financial instruments which are classified as FVTPL:

	Year ended December 31,	
($ in thousands)	**2012**	**2011**
Unrealized loss on FVTPL investments	**$ 4,482**	$ 3,091
Unrealized gain on embedded derivatives in CIC debenture	**(39,512)**	(106,489)

7. LIQUIDITY AND CAPITAL RESOURCES (Continued)

Other comprehensive income for the year ended December 31, 2012 consists of a reclassification of the unrealized gain (net of tax) on the Company's investment in Aspire. In 2012, the Company determined that objective evidence of impairment in the Company's investment in Aspire existed. Therefore, an impairment loss of $19.2 million was recognized in other operating expenses. Other comprehensive income for the year ended December 31, 2011 consists of an unrealized loss (net of tax) of $11.2 million related to the Company's investment in Aspire.

8. ENVIRONMENT

The Company is subject to the Environmental Protection Law of Mongolia ("EPL") and has the following duties with respect to environmental protection:

- To comply with the EPL and the decisions of the government, local self-governing organizations, local governors and Mongolian state inspectors;
- To comply with environmental standards, limits, legislation and procedures and to supervise their implementation within their organization;
- To keep records on toxic substances, adverse impacts, and waste discharged into the environment; and
- To report on measures taken to reduce or eliminate toxic chemicals, adverse impacts, and waste.

In addition to those duties imposed on them by the EPL, mining license holders are required to prepare an initial environmental impact assessment analysis before the mine comes into production. The mining license holders must also annually develop and implement an environmental protection plan (including reclamation measures) in co-operation with the Ministry of Environment, which should take into account the results of the environmental impact assessment. The Company received approval of its detailed Environmental Impact Assessment and Environmental Protection Plan from the Mongolian Ministry of Environment for the mining operation at the Ovoot Tolgoi Mine in 2007.

The Company has implemented a number of internal policies to embrace responsibility for the impact of its business activities on the environment. By conducting studies, carefully designing mine plans, implementing pollution control recommendations from internal and external sources, monitoring the effects of mining on mining areas and carefully designing mine closure plans, the Company seeks to minimize the impact of its activities on the environment.

8. ENVIRONMENT (Continued)

The Company established an environmental policy in 2008. The environmental policy affirms the Company's commitment to environmental protection. The Company monitors its operations to ensure that it complies with all applicable environmental requirements, and takes actions to prevent and correct problems if needed.

The Board maintains a Health, Environment, Safety and Social Responsibility Committee. The Committee is composed of non-executive and executive directors. The primary objective of the Health, Environment, Safety and Social Responsibility Committee is to review and oversee the Company's established health, environmental, safety and social responsibility policies and procedures at the Company's project sites. The Committee also reviews any incidents that may occur and provides guidance on how to prevent any recurrences.

9. RELATED PARTY TRANSACTIONS

The Company had related party transactions with the following companies related by way of directors or shareholders in common:

- Turquoise Hill – Turquoise Hill is the Company's immediate parent company and at December 31, 2012 owned approximately 58% of the outstanding common shares of the Company. Turquoise Hill provides various administrative services to the Company on a cost-recovery basis. The Company also provided some office and investor relations services to Turquoise Hill in the Company's Hong Kong office and recovered the costs for those services on a cost-recovery basis. The Company's provision of office and investor relations services to Turquoise Hill ceased on June 30, 2012.
- Rio Tinto – Rio Tinto is the Company's ultimate parent company and at December 31, 2012 Rio Tinto controlled Turquoise Hill. The Company recovers administration and other costs incurred on behalf of Rio Tinto on a cost-recovery basis. Rio Tinto recovers from the Company the costs of salaries and benefits of employees assigned to work for the Company.
- Global Mining Management ("GMM") – GMM is a private company owned equally by seven companies, two of which include the Company and Turquoise Hill. GMM provides administration, accounting and other office services to the Company on a cost-recovery basis.
- Turquoise Hill Resources Singapore Pte. Ltd. ("Turquoise Hill Singapore") – Turquoise Hill Singapore (formerly I2MS.NET Pte. Ltd) is a private company 100% owned by Turquoise Hill. Turquoise Hill Singapore provides information technology and other related services to the Company on a cost-recovery basis.

9. RELATED PARTY TRANSACTIONS (Continued)

- Ivanhoe Energy Inc. ("Ivanhoe Energy") – Ivanhoe Energy is a publicly listed company and previously had two directors in common with the Company. During the year ended December 31, 2012, Ivanhoe Energy ceased being a related party. The Company provided some office and investor relations services to Ivanhoe Energy in the Company's Hong Kong office and recovered the costs for those services on a cost-recovery basis. The Company's provision of office and investor relations services to Ivanhoe Energy ceased on June 30, 2012.

The following tables summarize related party expenses incurred by the Company with the companies listed above:

($ in thousands)	Year ended December 31, 2012	Year ended December 31, 2011
Corporate administration	**$ 1,309**	$ 1,990
Salaries and benefits	**919**	1,389
Total related party expenses	**$ 2,228**	$ 3,379

($ in thousands)	Year ended December 31, 2012	Year ended December 31, 2011
GMM	**$ 1,012**	$ 2,014
Turquoise Hill	**7**	94
Rio Tinto	**68**	-
Turquoise Hill Singapore	**1,141**	1,271
Total related party expenses	**$ 2,228**	$ 3,379

The Company recorded recoveries of $0.6 million for the year ended December 31, 2012 compared to recoveries of $0.5 million for the year ended December 31, 2011 for administration expenses with Turquoise Hill, Ivanhoe Energy and Rio Tinto.

The Company had accounts receivable of $0.7 million as at December 31, 2012 (December 31, 2011: $0.6 million) and accounts payable of $0.1 million as at December 31, 2012 (December 31, 2011: $0.4 million) with related parties.

9. RELATED PARTY TRANSACTIONS (Continued)

Emolument Policy

The emolument policy of the executives of the Company is administered by the Compensation and Benefits Committee on the basis of merit, qualifications and competence and approved by the Board. The emolument policy for the rest of the employees is determined on a department by department basis with the executive in charge of each department determining the emoluments for senior employees and managers in the department and the emoluments for non-senior employees being determined by an appropriately designated manager. The emolument policy for non-executives is administered in conjunction with the human resources department and is done on the basis of merit, qualifications and competence.

The emolument policy for the directors of the Company is administered by the Compensation and Benefits Committee and approved by the Board, having regard to comparable market statistics.

The Company has also adopted an equity incentive plan to incentivize directors and eligible employees. Details of the plan are set out in Note 23 of the consolidated financial statements.

As at December 31, 2012, the Company employed 465 employees, of which only 283 are active due to the curtailment of the mining operations.

10. PROPOSED TRANSACTION

On April 2, 2012, SouthGobi announced a cooperation agreement with CHALCO and received official notification of CHALCO's intention to make a proportional takeover bid for up to 60% of the issued and outstanding common shares of SouthGobi at Cdn$8.48 per share ("Proportional Offer"). SouthGobi was also informed by its 58% major shareholder, Turquoise Hill, that Turquoise Hill had signed a lock-up agreement with CHALCO, committing to tender all of its shares held or thereafter acquired by it during the offer period of CHALCO into the Proportional Offer. The Proportional Offer was to be made by way of a takeover bid circular under British Columbia law and would be made to all SouthGobi shareholders. If shareholders tendered more than 60% of the outstanding common shares of SouthGobi to the takeover bid, a proportional amount of shares were to be taken up from each shareholder.

In conjunction with the Proportional Offer, CHALCO and SouthGobi entered into a cooperation agreement. CHALCO's obligations under the cooperation agreement were to become effective upon CHALCO acquiring a shareholding in SouthGobi.

10. PROPOSED TRANSACTION (Continued)

SouthGobi had also been notified that CHALCO entered into consultancy agreements with nine key senior executives, officers and staff to assist CHALCO with the integration and transition following CHALCO's acquisition of a shareholding in SouthGobi.

CHALCO stated that it expected to mail the takeover bid circular in connection with the Proportional Offer on or about July 5, 2012. On July 3, 2012, CHALCO and Turquoise Hill announced a 30 day extension for CHALCO to mail the takeover bid circular. Subsequently, on August 2, 2012, an additional 30 day extension was announced by CHALCO and Turquoise Hill. Finally, on September 3, 2012, SouthGobi was notified that CHALCO's Proportional Offer had been terminated, which also resulted in the termination of the cooperation agreement and the consultancy agreements.

11. OUTSTANDING SHARE DATA

The Company is authorized to issue an unlimited number of common shares without par value and an unlimited number of preferred shares without par value. As at December 12, 2013, 187.3 million common shares were issued and outstanding. There are also incentive share options outstanding to acquire 2.6 million unissued common shares with exercise prices ranging from Cdn$1.16 to Cdn$14.25. There are no preferred shares outstanding.

As at December 12, 2013, Turquoise Hill directly owned 104.8 million common shares representing approximately 56% of the issued and outstanding common shares of the Company.

12. INTERNAL CONTROLS OVER FINANCIAL REPORTING

Disclosure controls and procedures are designed to provide reasonable assurance that information required to be disclosed by the Company in its annual filings, interim filings or other reports filed or submitted by it under securities legislation is recorded, processed, summarized and reported within the time periods specified in the securities legislation and include controls and procedures designed to ensure that information required to be disclosed by the Company in its annual filings, interim filings or other reports filed or submitted under securities legislation is accumulated and communicated to the Company's management, including its Chief Executive Officer and Principal Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

12. INTERNAL CONTROLS OVER FINANCIAL REPORTING (Continued)

In conjunction with the financial statement restatement described in Section 1 of this MD&A, the Company's management has identified a material weakness in the Company's internal controls over financial reporting as of December 31, 2012 and as of December 31, 2011, resulting in the failure to properly account for revenues in complex transactions. Specifically, the Company did not ensure that all aspects of sales arrangements were considered in the determination of the appropriate accounting for contracts in which the specified location of transfer of title in the contracts is the customer's stockpile in a stockyard located within the SouthGobi Ovoot Tolgoi mining license area. As a result of the material weakness, the Company's Chief Executive Officer and Chief Financial Officer have concluded that internal controls over financial reporting were not effective as of December 31, 2012 and as of December 31, 2011.

Management has been enhancing internal controls over financial reporting by developing a more thorough review process in evaluating complex sales arrangements in each reporting period. The remedial controls that have now been implemented must operate for a sufficient period of time before management can conclude, through testing, that these controls are effective. Management expects this to be achieved by December 31, 2013.

13. CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS

The preparation of financial statements in conformity with IFRS requires the Company to establish accounting policies and to make estimates that affect both the amount and timing of the recording of assets, liabilities, revenues and expenses.

A detailed summary of all of the Company's significant accounting policies is included in Note 4 to the annual consolidated financial statements (restated) for the year ended December 31, 2012. Information about judgments and estimates in applying accounting policies that have the most significant effect on the amounts recognized in the consolidated financial statements are as follows:

13. CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS (Continued)

Valuation of embedded derivatives

The embedded derivatives in the Company's convertible debenture are valued using a Monte Carlo simulation valuation model. A Monte Carlo simulation model is a valuation model that relies on random sampling and is often used when modeling systems with a large number of inputs and where there is significant uncertainty in the future value of inputs and where the movement of the inputs can be independent of each other. The key inputs used by the Company in its Monte Carlo simulation are further disclosed in Note 20.2 and Note 20.3 to the annual consolidated financial statements for the year ended December 31, 2012. Changes in the inputs to the valuation model could impact the carrying value of the embedded derivatives in the convertible debenture and the amount of unrealized gains or losses recognized in profit or loss.

Review of carrying value of assets and impairment charges

In the determination of carrying values and impairment charges, management of the Company reviews the recoverable amount (the higher of the fair value less costs to sell or the value in use) in the case of non-financial assets and objective evidence indicating impairment in the case of financial assets. These determinations and their individual assumptions require that management make a decision based on the best available information at each reporting period. Changes in these assumptions may alter the results of non-financial asset and financial asset impairment testing, impairment charges recognized in profit or loss and the resulting carrying amounts of assets.

Estimated recoverable reserves

Reserve estimates involve expressions of judgment based on various factors such as knowledge, experience and industry practice, and the accuracy of these estimates may be affected by many factors, including estimates and assumptions with respect to coal prices, operating costs, mine plan and life, coal quality and recovery, foreign currency exchange rates and inflation rates. Reserve estimates are made by qualified persons, but will be impacted by changes in the above estimates and assumptions.

Estimated recoverable reserves are used to determine the depletion of mineral properties, in accounting for deferred production stripping costs, in performing impairment testing and for forecasting the timing of the payment of decommissioning, restoration and similar costs. Therefore, changes in the estimates and assumptions used to determine recoverable reserves could impact the carrying value of assets, depletion expense and impairment charges recognized in profit or loss and the carrying value of the decommissioning, restoration and similar liabilities.

13. CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS (Continued)

Useful lives and depreciation rates for property, plant and equipment

Depreciation expense is allocated based on estimated property, plant and equipment useful lives and depreciation rates. Therefore, changes in the useful life or depreciation rates from the initial estimate could impact the carrying value of property, plant and equipment and an adjustment would be recognized in profit or loss.

Income taxes and recoverability of deferred tax assets

Actual amounts of income tax expense are not final until tax returns are filed and accepted by the taxation authorities. Therefore, profit or loss in future reporting periods will be affected by the amount that income tax expense estimates differ from the final tax returns.

Judgment is required in determining whether deferred tax assets are recognized on the statement of financial position. Deferred tax assets, including those arising from unutilized tax losses, require management of the Company to assess the likelihood that the Company will generate sufficient taxable profit in future periods in order to utilize recognized deferred tax assets. Estimates of future taxable profit are based on forecast cash flows from operations and the application of existing tax laws in each jurisdiction. To the extent that future cash flows and taxable profit differ from estimates, the ability of the Company to realize the deferred tax assets recorded on the statement of financial position could be impacted.

14. RISK FACTORS

There are certain risks involved in the Company's operations, some of which are beyond its control. These risks can be broadly categorized into: (i) risks relating to its projects in Mongolia; and (ii) risks relating to its business and industry. Additional risks and uncertainties not presently known, or not expressed or implied below, or that are presently deemed immaterial, could also harm the Company's business, financial condition and operating results. Some of the following statements are forward-looking and actual results may differ materially from the results anticipated in these forward-looking statements.

14. RISK FACTORS (Continued)

Risks Relating to the Company's Projects in Mongolia

The Company is subject to continuing governmental, regulatory and internal investigations, the outcome of which is unclear at this time but could have a material adverse effect on the Company

The investigations referred in Section 4.1 "governmental, regulatory and internal investigations" could result in one or more Mongolian, Canadian, United States or other governmental or regulatory agencies taking civil or criminal action against the Company, its affiliates or its current or former employees. The likelihood or consequences of such an outcome are unclear at this time but could include financial or other penalties, which could be material, and which could have a material adverse effect on the Company.

Legislation in Mongolia may be subject to conflicting interpretations, which may have adverse consequences on the Company's business

The Mongolian legal system shares several of the qualitative characteristics typically found in a developing country and many of its laws, particularly with respect to matters of taxation, are still evolving. A transaction or business structure that would likely be regarded under a more established legal system as appropriate and relatively straightforward might be regarded in Mongolia as outside the scope of existing Mongolian law, regulation or legal precedent. As a result, certain business arrangements or structures and certain tax planning mechanisms may carry significant risks. In particular, when business objectives and practicalities dictate the use of arrangements and structures that, while not necessarily contrary to settled Mongolian law, are sufficiently novel within a Mongolian legal context, it is possible that such arrangements may be invalidated.

The legal system in Mongolia has inherent uncertainties that could limit the legal protections available to the Company, which include: (i) inconsistencies between laws; (ii) limited judicial and administrative guidance on interpreting Mongolian legislation; (iii) substantial gaps in the regulatory structure due to delay or absence of implementing regulations; (iv) the lack of established interpretations of new principles of Mongolian legislation, particularly those relating to business, corporate and securities laws; (v) a lack of judicial independence from political, social and commercial forces; and (vi) bankruptcy procedures that are not well developed and are subject to abuse. The Mongolian judicial system has relatively little experience in enforcing the laws and regulations that currently exist, leading to a degree of uncertainty as to the outcome of any litigation; it may be difficult to obtain swift and equitable enforcement, or to obtain enforcement of a judgment by a court of another jurisdiction.

14. RISK FACTORS (Continued)

In addition, while legislation has been enacted to protect private property against expropriation and nationalization, due to the lack of experience in enforcing these provisions and political factors, these protections may not be enforced in the event of an attempted expropriation or nationalization. Expropriation or nationalization of any of the Company's assets, or portions thereof, potentially without adequate compensation, could materially and adversely affect its business and results of operations.

If an event of default occurs under the convertible debenture, CIC has the right to accelerate amounts owing thereunder

With the exception of an insolvency event, if an event of default occurs under the convertible debenture, and such event of default has not been cured or waived, the principal amount owing and all accrued and unpaid interest will become immediately due and payable upon notice to the Company by CIC which would have a material adverse affect on the business and operations of the Company.

If an insolvency event occurs under the convertible debenture, the principal amount owing and all accrued and unpaid interest will become immediately due and payable without the necessity for notice to the Company by CIC, which would have a material adverse affect on the business and operations of the Company.

The Application of the Foreign Investment Law approved by the Parliament of Mongolia is uncertain

The Company considers that this risk factor has been substantially mitigated following the repeal of the Foreign Investment Law and introduction of the Investment Law on October 3, 2013, which appears to provide greater certainty for foreign investment in Mongolia.

14. RISK FACTORS (Continued)

Application of and amendments to legislation could adversely affect the Company's mining rights in its projects or make it more difficult or expensive to develop its projects and carry out mining

The 2006 Minerals Law of Mongolia (the "2006 Minerals Law"), which preserves to a limited extent some of the substance of the former 1997 minerals legislation, was drafted with the assistance of legal experts in the area of mining legislation and was widely regarded as progressive, internally consistent and effective legislation. However, the 2006 Minerals Law contains new provisions that have increased the potential for political interference and weakened the rights and security of title holders of mineral tenures in Mongolia. Certain provisions of the 2006 Minerals Law are ambiguous and it is unclear how they will be interpreted and applied in practice. Examples of such provisions include those relating to the designation of a mineral deposit as a Mineral Deposit of Strategic Importance. The Government of Mongolia could determine that any one or more of the Company's projects in Mongolia is a Mineral Deposit of Strategic Importance.

In addition, the introduction of new Mongolian laws and regulations and the interpretation of existing ones may be subject to policy changes reflecting domestic political or social changes. For example, on July 16, 2009, Parliament enacted the Mining Prohibition in Specified Areas Law that prohibits minerals exploration and mining in areas such as headwaters of rivers and lakes, forest areas as defined in the Forest Law of Mongolia and areas adjacent to rivers and lakes as defined in the Water Law of Mongolia. Pursuant to the Mining Prohibition in Specified Areas Law, the Government of Mongolia has defined the boundaries of certain areas in which exploration and mining is purportedly prohibited. A list of licenses has been prepared that overlap with the prohibited areas described in the law based on information submitted by water authority agencies, forest authority agencies and local authorities for submission to the Government of Mongolia. New exploration licenses and mining licenses overlapping the defined prohibited areas will not be granted, and previously granted licenses that overlap the defined prohibited areas will be terminated within five months following the adoption of the law. It is not clear whether such termination will only apply to the overlap areas. The Mining Prohibition in Specified Areas Law provides that affected license holders shall be compensated, but there are no specifics as to the way such compensation will be determined. The Company understands that the status of the Mining Prohibition in Specified Areas Law is unclear and it has not been enforced to date.

Portions of the Company's Ovoot Tolgoi and Tsagaan Tolgoi mining licenses and exploration licenses pertaining to the Zag Suuj Deposit and the South Biluut and Jargalant Fields within the Soumber Deposit are included on the list of licenses published by the Government of Mongolia, potentially affecting the status of those licenses under the Mining Prohibition in Specified Areas Law.

14. RISK FACTORS (Continued)

In regard to the Ovoot Tolgoi mining license, the potential area which may be affected is a relatively small area which represents approximately 3% of the entire area of the mining license and does not contain any of the Company's NI 43-101 reserves or resources or immovable assets. Accordingly, the loss of the potentially affected area would not materially and adversely affect the existing operations.

Activities historically carried out on the other licenses referred to above include drilling, trenching and geological reconnaissance. The Company has no immovable assets located in any of the potentially affected areas and the loss of any or all of the potentially affected properties would not materially and adversely affect its existing operations. However, the loss of the Tsagaan Tolgoi mining license and exploration licenses pertaining to the Zag Suuj Deposit and the South Biluut and Jargalant fields within the Soumber Deposit would impact the Company's resources.

The Minerals Law has been subject to proposals for reform, including draft amendments developed by the President's Office of Mongolia in December 2012. The main focus of the draft amendments is to encourage and enhance the involvement of local communities to participate more effectively in investment decisions and benefits arising from mine development. To date, the status of the Minerals Law remains uncertain, however reports from Mongolia indicate that MRAM is now responsible for reforming the law and that its proposed amendments will be made publicly available and submitted to the Parliament for review and approval in 2014.

As such, there can be no assurance that future political and economic conditions in Mongolia will not result in the Government of Mongolia adopting different policies in relation to foreign development and ownership of mineral resources. Any such changes in government or policy may result in changes in laws affecting ownership of assets, environmental protection, labor relations, repatriation of income, return of capital, investment agreements, income tax laws, royalty regulation, government incentive and other areas, each of which may materially and adversely affect the Company's ability to undertake exploration and development activities in the manner currently contemplated. Similarly, any restrictions imposed, or Government of Mongolia charges levied or raised (including royalty fees), under Mongolian law for the export of coal could harm the Company's competitiveness.

The Company's ability to carry on business in Mongolia is subject to political risk

The Company's ability to efficiently conduct its exploration and development activities is subject to changes in government policy or shifts in political attitudes within Mongolia that are beyond the Company's control.

14. RISK FACTORS (Continued)

Government policy may change to discourage foreign investment, nationalization of mining industries may occur or other government limitations, restrictions or requirements not currently foreseen may be implemented. There is no assurance that the Company's assets will not be subject to nationalization, requisition or confiscation, whether legitimate or not, by any authority or body. The provisions under Mongolian law for compensation and reimbursement of losses to investors under such circumstances may not be effective to restore the value of the Company's original investment.

In addition, Mongolia may experience political instability. Such instability could have a material adverse effect on economic or social conditions in Mongolia and may result in outbreaks of civil unrest, terrorist attacks or threats or acts of war in the affected areas, any of which could materially and adversely affect the Company's business and results of operations.

The Government of Mongolia could determine that any one or more of the Company's projects in Mongolia is a Mineral Deposit of Strategic Importance

Pursuant to the 2006 Minerals Law, the Parliament has wide discretion to designate mineral deposits to be Mineral Deposits of Strategic Importance. The Government of Mongolia is empowered to participate on an equity basis with the license holder in the exploitation and/or mining of each Mineral Deposit of Strategic Importance on terms to be negotiated between the Government of Mongolia and such license holder. Details of any minerals reserves must be filed by the relevant license holder with the Government of Mongolia, and those deposits on the Strategic Deposits List represent most of the largest and highest profile deposits in Mongolia. In addition to deposits currently on the Strategic Deposits List and the additional Tier 2 Deposits List, the Parliament may at any time designate other deposits not yet currently on such Lists to be Mineral Deposits of Strategic Importance, add such deposits to either the Strategic Deposits List or the Tier 2 Deposits List and, in the former case, commence negotiations with the relevant license holder with respect to the terms under which the Government of Mongolia will take an interest in such deposit. While the Government of Mongolia is in the process of adding the exact location and coordinates for each Mineral Deposit of Strategic Importance, a number of deposits on the Strategic Deposits List are identified by name only with no indication of the latitude and longitude coordinates for the deposit, and it is therefore not always possible to precisely determine the intended geographic area covered by each designated Mineral Deposit of Strategic Importance or to accurately determine whether or not any given license area is within, or overlaps, a Mineral Deposit of Strategic Importance.

14. RISK FACTORS (Continued)

Under the 2006 Minerals Law, the size of the Government of Mongolia's participation is determined largely by the level of state funding which has been provided for the exploration and development of any deposit, with the Government of Mongolia entitled to participate up to 50% in the event that there has been state funding of such deposit and up to 34% if there has not. However, the 2006 Minerals Law is very vague as to the details and method by which the Government of Mongolia will take its interest and the final arrangements in respect of the Government of Mongolia's interest in each Mineral Deposit of Strategic Importance, including the amount of compensation to be paid to the license holder and the actual form of the Government of Mongolia's interest are subject to negotiation between the Government of Mongolia and the license holder.

The 2006 Minerals Law also contains provisions requiring any company which holds a Mineral Deposit of Strategic Importance to list no less than 10% of its shares on the Mongolian Stock Exchange. This particular provision of the 2006 Minerals Law has not yet been enforced and it is not clear how it will work in practice.

In recent years there have been a number of proposed amendments to the 2006 Minerals Law suggested by various parties, many of which have centered on amending the 2006 Minerals Law to increase the Government of Mongolia's participating interest in excess of 50%. While the 2006 Minerals Law provides that the interest of the Government of Mongolia should take the form of an equity interest, based on past practice, and depending on the results of individual negotiations, the interest may be in the form of production or profit sharing or some other arrangement negotiated between the license holder and the Government of Mongolia. There can be no assurance that legislation will not be enacted which further strengthens the Government of Mongolia's right to participate in privately held mineral resources in Mongolia.

None of the deposits covered by the Company's existing mining licenses or exploration licenses are currently designated as Mineral Deposits of Strategic Importance. However, there can be no assurance that any one or more of these deposits will not be so designated in the future, in which case the Company's business and results of operations may be materially and adversely affected.

14. RISK FACTORS (Continued)

Risks relating to the Company's business and industry

Some of the Company's projects may not be completed as planned; costs may exceed original budgets and may not achieve the intended economic results or commercial viability

The Company's business strategy depends in large part on expanding its production capacity at the Ovoot Tolgoi Mine and further developing its other coal projects into commercially viable mines. Whether a mineral deposit will be commercially viable depends on a number of factors, including: (i) the particular attributes of the deposit, such as size, grade and proximity to infrastructure; (ii) commodity prices, which are highly cyclical; and (iii) government regulations, including regulations relating to prices, taxes, royalties, land tenure, land use, importing and exporting of mineral resources and environmental protection. The Company's long term intention to develop mines at the Soumber Deposit, the Zag Suuj Deposit, and the Ovoot Tolgoi Underground Deposit in the future is based on geological, engineering, environmental and mine planning evaluations. The feasibility of mining at these projects as well as at the Tsagaan Tolgoi Deposit has not been and may never be established. If the Company is unable to develop all or any of its projects into a commercial working mine, its business, financial condition and results of operations will be materially and adversely affected.

The Company's projects are subject to technical risk in that they may not perform as designed. Increased development costs, lower output or higher operating costs may all combine to make a project less profitable than expected at the time of the development decision. This would have a negative impact on the Company's business and results of operations. No assurance can be given that the Company would be adequately compensated by third party project design and construction companies (if not performed by the Company) in the event that a project did not meet its expected design specification.

The Ovoot Tolgoi Technical Report assumed that the Ejin Jinda wet wash plant at Ceke would process 1.5 million tonnes of coal in 2012. Construction of the wet wash plant was completed in 2012. The Ovoot Tolgoi Technical Report also assumes that the Ejin Jinda wet wash plant is expanded to process 7.0 million tonnes annually from mid-2014. The Company is currently cooperating with Ejin Jinda in studying the utilization of the wet washing facility. Any delay in expanding annual capacity to 7.0 million tonnes by mid-2014, would likely impact the project economics, as the coal would be sold as lower value coal; however, these delays would be unlikely to impact on total reserve estimates.

14. RISK FACTORS (Continued)

As with all exploration properties or projects taken on by mining companies, there is a risk that exploration projects will not be converted to commercially viable mines, in part because actual costs from capital projects may exceed the original budgets. As a result of project delays, cost overruns, changes in market circumstances or other reasons, the Company may not be able to achieve the intended economic benefits or demonstrate the commercial feasibility of these projects, which in turn may materially and adversely affect the Company's business, results of operations and growth projects.

The Company's coal reserves and resources are estimates based on a number of assumptions, and the Company may produce less coal than its current estimates

The coal reserve and resource estimates are based on a number of assumptions that have been made by the qualified persons in accordance with NI 43-101. Reserve and resource estimates involve expressions of judgment based on various factors such as knowledge, experience and industry practice, and the accuracy of these estimates may be affected by many factors, including quality of the results of exploration drilling and analysis of coal samples, as well as the procedures adopted by and the experience of the person making the estimates.

The Ovoot Tolgoi Technical Report assumes that the Company's mining activity will extend across its lease boundary and into the lease held by Mongolyn Alt Corporation ("MAK"). A memorandum of understanding covering mining across the lease boundary was signed in May 2007. Discussions are continuing with an in-principle agreement, subject to legal documentation and relevant authorities' expected approval to be finalized in 2013. The resource and reserve estimates in the Ovoot Tolgoi Technical Report do not include any coal within the MAK lease; however, the geological models and mining pits extend into the MAK lease. If an operational agreement cannot be finalized, then the reserve estimate could be materially affected.

Estimates of the reserves and resources at the Company's projects may change significantly when new information becomes available or new factors arise, and interpretations and deductions on which reserves and resources estimates are based may prove to be inaccurate. Should the Company encounter mineralization different from that predicted by past drilling, sampling and similar examination, mineral resource and/or reserve estimates may have to be adjusted downward. This downward adjustment could materially affect the Company's development and mining plans, which could materially and adversely affect its business and results of operations.

14. RISK FACTORS (Continued)

In addition, the rank of coal ultimately mined may differ from that indicated by drilling results. There can be no assurance that coal recovered in laboratory tests will be duplicated under on-site conditions or in production-scale operations. In the event that the actual level of impurities is higher than expected or the coal mined is of a lower quality than expected, the demand for, and realizable price of, the Company's coal may decrease. Short term factors relating to reserves, such as the need for orderly development of coal seams or the processing of new or different quality coals, may also materially and adversely affect the Company's business and results of operations.

The inclusion of reserve and resource estimates should not be regarded as a representation that all these amounts can be economically exploited and nothing contained herein (including, without limitation, the estimates of mine lives) should be interpreted as assurance of the economic lives of the Company's coal reserves and resources or the profitability of its future operations.

The Company commenced mining in April 2008, and has recorded operating losses and operating cash outflows to date. From the second quarter of 2012 until March 22, 2013, the Company's operations at the Ovoot Tolgoi Mine were curtailed. Due to the Company's limited operating history and curtailment of operations, there may not be an adequate basis on which to evaluate the Company's future operating results and prospects. Investors may have difficulties evaluating the Company's business and prospects because the Company's past results may not be indicative of the Company's results in the future.

The Company does not insure against all risks to which it may be subject to in planned operations and insurance coverage could prove inadequate to satisfy potential claims

For certain aspects of the Company's business operations, insurance coverage, in particular business interruption insurance, is restricted or prohibitively expensive. The Company currently holds its primary insurance policies through Canadian insurance providers to insure its properties. The Company has taken out insurance for risks including commercial general liability and aviation premises liability. The Company maintains mining property insurance for all of its mining assets wherever located, property insurance on its office premises and liability insurance for its directors and officers. However, no assurance can be given that the Company will elect or be able to obtain such insurance coverage at economically reasonable premiums (or at all), or that any coverage it obtains will be adequate to cover the extent of any claims brought against it.

14. RISK FACTORS (Continued)

Exploration, development and production operations on mineral properties involve numerous risks, including environmental risks, such as unexpected or unusual geological operating conditions, rock bursts or slides, fires, floods, earthquakes or other environmental occurrences, and political and social instability. The Company does not maintain insurance against any environmental or political risks. Should any liabilities arise for which it is not insured or insurance coverage is inadequate to cover the entire liability, they could reduce or eliminate the Company's actual or prospective profitability, result in increasing costs and a decline in the value of the common shares and could materially and adversely affect the Company's business and results of operations.

Licenses and permits are subject to renewal and various uncertainties and the Company may only renew its exploration licenses a limited number of times for a limited period of time

In Mongolia, the Company's exploration licenses are subject to periodic renewal and may only be renewed a limited number of times for a limited period of time. There is no assurance that such renewals will be given as a matter of course and there is no assurance that new conditions will not be imposed in connection therewith. Although the Mongolian Government may have renewed the Company's licenses and permits in the past, the Mongolian Government may retroactively revoke such renewals which could potentially result in the loss of the Company's exploration licenses, PMA's or mining licenses. The Company's business objectives may also be impeded by the costs of holding and/or renewing the exploration licenses in Mongolia. License fees for exploration licenses increase substantially upon the passage of time from the original issuance of each individual exploration license. The Company needs to continually assess the mineral potential of each exploration license, particularly at the time of renewal, to determine if the costs of maintaining the exploration licenses are justified by the exploration results to date, and may elect to let some of its exploration licenses lapse. A moratorium on transfers of exploration licenses has been imposed on two separate occasions and there is a risk that a similar moratorium could be imposed such that letting the exploration licenses lapse may be the only practical option in some circumstances. Furthermore, the Company will require mining licenses and permits to mine in order to conduct mining operations in Mongolia. There can be no assurance, however, that such licenses and permits will be obtained on terms favorable to it or at all for the Company's future intended mining and/or exploration targets in Mongolia.

14. RISK FACTORS (Continued)

In April 2012, MRAM announced the suspension of exploration and mining activity on certain of the Company's licenses including the license pertaining to the Ovoot Tolgoi Mine. Although the Company did not receive official notification of a suspension of licenses and had no reason to believe its licenses were not in good standing, this announcement caused a significant disruption in the Company's business which ultimately led to the curtailment of operations at the Ovoot Tolgoi Mine. Although the Company received a letter from MRAM on September 6, 2012 confirming that all exploration and mining licenses were in good standing there is still a risk that its licenses could be revoked.

In addition, certain provisions of the Land Law of Mongolia and the 2006 Minerals Law provide for the revocation of previously granted land use rights, exploration licenses or mining licenses on the grounds that the affected area of land has been designated as "special needs" territory. The Land Law of Mongolia grants the discretion to declare an area of land for special needs purposes to local governing authorities and identifies various broad categories which qualify as special needs. The 2006 Minerals Law requires the local governing authority that designates an area of land as a special needs territory to compensate the license holder whose rights or license status are affected. If any of the Company's land use rights, exploration licenses or mining licenses in Mongolia are revoked because the underlying land is declared as special needs territory, there is no assurance that the Company will receive adequate compensation or any compensation at all and its business and results of operation might be adversely and materially affected. The Company has had no land use rights or exploration/mining licenses revoked to date.

Prolonged periods of severe weather conditions could materially and adversely affect the Company's business and results of operations

Severe weather conditions may require the Company to evacuate personnel or curtail operations and may cause damages to the project site, equipment or facilities, which could result in the temporary suspension of operations or generally reduce the Company's productivity. Severe weather conditions have not caused any delay or damages to the Company's operations to date. However, there can be no assurance that severe weather will not occur. Any damages to the Company's projects or delays in its operations caused by prolonged periods of severe weather could materially and adversely affect its business and results of operations.

14. RISK FACTORS (Continued)

The Company's business and results of operations are susceptible to the cyclical nature of coal markets and are vulnerable to fluctuations in prices for coal

The Company expects to derive substantially all of its revenue and cash flow from the sale of coal. Therefore, the market price of the shares, the Company's ability to raise additional financing and maintain ongoing operations and its financial condition and results of operations will be directly related to the demand for, and price of, coal and coal-related products. Coal demand and price are determined by numerous factors beyond the Company's control, including the international demand for steel and steel products, the availability of competitive coal supplies, international exchange rates, political and economic conditions in Mongolia, the People's Republic of China (the "PRC") and elsewhere in the world, milder or more severe than normal weather conditions, and production costs in major coal producing regions. The PRC and international coal markets are cyclical and have in the past exhibited significant fluctuations in supply, demand and prices from year to year. There has been significant price volatility on the coal spot market. An oversupply of coal in the PRC or a general downturn in the economies of any significant markets for the Company's coal and coal-related products could materially and adversely affect its business and results of operations. In addition, the Company's dependence on Asian markets may result in instability in its operations due to political and economic factors in those Asian jurisdictions which are beyond the Company's control. The combined effects of any or all of these factors on coal prices or volumes are impossible for the Company to predict.

In 2012, the Company experienced a softening in the coal markets closest to its operations. The Company observed substantial deterioration in demand sentiment among its customers which led to a substantial decline in key reference prices and key end-use markets. The softening demand contributed to the decision to continue the curtailment of the Company's mining operations and has resulted in reduced revenue. If realized coal prices remain below the full cost of production of any of its future mining operations and remain at such a level for any sustained period, the Company could experience increased losses and may decide to discontinue operations, which could require the Company to incur closure costs and result in further reduced revenues.

14. RISK FACTORS (Continued)

The Company's coal mining activities are subject to operational risks, including equipment breakdown

The Company's coal mining operations are subject to a number of operational risks, some of which are beyond its control, which could delay the production and delivery of coal. These risks include unexpected maintenance or technical problems, periodic interruptions to its mining operations due to inclement or hazardous weather conditions and natural disasters, industrial accidents, power or fuel supply interruptions and critical equipment failure, including malfunction and breakdown of its excavators, upon which its coal mining operations are heavily reliant and which would require considerable time to replace. These risks and hazards may result in personal injury, damage to, or destruction of, properties or production facilities, environmental damage, business interruption and damage to its business reputation. In addition, breakdowns of equipment, difficulties or delays in obtaining replacement excavators and other equipment, natural disasters, industrial accidents or other causes could temporarily disrupt the Company's operations, which in turn may also materially and adversely affect its business, prospects, financial condition and results of operations.

The unavailability or shortage of reliable and sufficient coal transportation capacity that meets Mongolian authority regulations will reduce the Company's coal revenue by causing it to reduce its production volume or impairing its ability to supply coal to its customers

The Company anticipates that the majority of its coal production from the projects in Mongolia will be exported into the PRC. Inadequate transportation infrastructure is likely to affect the pricing terms on which it can sell the coal to customers and the willingness and ability of such customers to purchase coal from it. Potential customers are likely to factor in any delays and the costs and availability of transportation in determining the price they are prepared to pay to purchase the Company's coal. Therefore, its mining operations are anticipated to be highly dependent on road and rail services in Mongolia and the PRC.

In Mongolia, a bottleneck in the transportation of coal from the Ovoot Tolgoi Mine to customers in the PRC may arise if the road connecting the Ovoot Tolgoi Mine to the Shivee Khuren Border Crossing does not have sufficient capacity to support the increased amount of cargo traffic, is affected by external factors such as disruptions caused by bad weather or is closed for repair. During 2012, the road connecting the Ovoot Tolgoi Mine to the Shivee Khuren Border Crossing was closed for over four weeks for repair, which impacted customers' ability to export coal.

14. RISK FACTORS (Continued)

The opening hours of the Shivee Khuren Border Crossing also affect the Company's ability to expedite the movement of its coal shipments. There can be no assurance that there would be any other cost effective means of transporting the coal to the Company's primary market in the PRC. As a result, the Company may experience difficulty expediting the movement of its coal shipments and/or significant cost escalation for the transportation services, which could affect its production and reduce its profitability.

In the PRC, rail and road infrastructure and capacity has in the past been affected by extreme weather conditions, earthquakes, delays caused by major rail accidents, the diversion of rolling stock needed to deliver emergency food relief and seasonal congestion during public holidays. There can be no assurance that these problems will not recur or that new problems will not occur. In any of these circumstances, the customers may not be able to take delivery of the Company's coal, which may lead to delays in payment, or refusal to pay, for the Company's coal and, as a result, the Company's business and results of operations could be materially and adversely affected.

The Company's prospects depend on its ability to attract, retain and train key personnel

Recruiting, retaining and training qualified personnel is critical to the Company's success. The number of persons skilled in the acquisition, exploration and development of mining properties is limited and competition within the mining industry for such persons is intense, in particular, Mongolian law requires that at least 90% of a mining company's employees be of Mongolian nationality. This provision of the law, coupled with the large number of active mining projects in Mongolia, further limits the number of available personnel and increases competition for skilled personnel. The reputation and capability to operate continuously over the longer term are key factors in also attracting key personnel to its business. The Company is reinforcing its core values of ethical behavior in dealing with all its stakeholders from senior management down in order to ensure the Company attracts the right people to its business. As the Company's business activity grows, it will require additional key financial, administrative, mining, marketing and public relations personnel as well as additional operations staff. If the Company is not successful in attracting such key personnel, or retaining existing key personnel, its business and results of operations could be materially and adversely affected.

In addition, the Company's ability to train operating and maintenance personnel is a key factor for the success of its business activities. If the Company is not successful in recruiting, training and retaining such personnel, its business and results of operations could be materially and adversely affected.

14. RISK FACTORS (Continued)

Competition in the coal industry may hinder development plans and adversely affect the Company's coal sales if it is not able to compete effectively

Continued growth in mining and mineral exploration activities in Mongolia could create an increasing demand for mining equipment and related services. Shortages of, or higher costs for, equipment and services could restrict the Company's ability to carry out the exploration, development and production activities, increase its costs of operations and adversely affect its future plans.

The Company intends to sell a majority of the coal it produces to the PRC. Competition in the PRC coal industry is based on many factors, including, among others, price, production capacity, coal quality and characteristics, transportation capability and costs, blending capability and brand name. The Company's coal business will most likely compete in the PRC with other large PRC and international coal mining companies. Due to their location, some of the Company's PRC competitors may have lower transportation costs than the Company does. The PRC coal market is highly fragmented and the Company faces price competition from some small local coal producers that produce coal for significantly lower costs than the Company due to various factors, including their lower expenditure on safety and regulatory compliance. Some of the Company's international competitors, including the Mongolian coal producers, may have greater coal production capacity as well as greater financial, marketing, distribution and other resources than the Company does, and may benefit from more established brand names in international markets. The Company's future success will depend on its ability to respond in an effective and timely manner to competitive pressure.

There are a number of risks associated with dependence on a limited number of customers and inability to attract additional customers

The Company depends on a relatively small number of customers. The incremental cost of transporting coal products from the Ovoot Tolgoi Mine and its other coal projects over long distances effectively limits the Company's potential customer base to a relatively proximate geographical area. This market has also been price sensitive and significant price volatility impacts contract performance.

Additionally, the Company has been selling its coal products only since September 2008. The Company had 6 active customers with the largest customer representing approximately 30%, the second largest customer representing approximately 29%, the third largest customer representing approximately 18% and the remaining customers accounting for 23% of the Company's total sales for the year ended December 31, 2012. In order to mitigate this risk, the Company is continually expanding its customer base.

14. RISK FACTORS (Continued)

In addition, the Company expects to sell the majority of the coal from its Mongolian mining operations to the customers in the PRC. PRC law requires specific authorization to be obtained by entities responsible for the import of coal into the PRC. In the event that the Company's customers, or the agents of such customers who are responsible for importing coal into the PRC on their behalf, fail to obtain and retain the necessary authorizations, their ability to import coal into the PRC may be affected, which could materially and adversely affect the Company's business and results of operations.

The Company's operations are exposed to risks in relation to environmental protection and rehabilitation

The operations of coal mines involve substantial environmental risks and hazards and the Company's operations are subject to laws and regulations relating to the environment, health and safety and other regulatory matters in Mongolia.

The risk of environmental liability is inherent in the operation of the Company's business. Environmental hazards may occur in connection with the Company's operations as a result of human negligence, force majeure, or otherwise. Claims may be asserted against the Company arising out of its operations in the normal course of business, including claims relating to land use, safety, health and environmental matters. The Company is not insured against environmental liabilities and there can be no assurance that environmental liabilities would not materially and adversely affect its business and results of operations.

In addition, the Company is subject to reclamation requirements. The Company's mine contains a finite amount of reserves and will eventually close. The key tasks in relation to the closure of the mines involves (i) long-term management of permanent engineered structures (for example, spillways, roads, waste dumps); (ii) achievement of environmental closure standards; (iii) orderly retrenchment of employees and contractors; and (iv) relinquishment of the site with associated permanent structures and community development infrastructure and programs to new owners. The successful completion of these tasks is dependent on the Company's ability to successfully implement negotiated agreements with the relevant government, community and employees. The consequences of a difficult closure range from increased closure costs and handover delays to ongoing environmental impacts and corporate reputation damage if desired outcomes cannot be achieved, which could materially and adversely affect the Company's business and results of operations.

14. RISK FACTORS (Continued)

Environmental legislation is evolving in a manner which will require stricter standards and enforcement, increased fines and penalties for non-compliance, more stringent environmental assessments of proposed projects and a heightened degree of responsibility for companies and their officers, directors and employees. The Company may experience increased costs of production arising from compliance with environmental laws and regulations. Should the Company fail to comply with current or future environmental laws and regulations, the Company may be required to pay penalties or take corrective actions, any of which may have a material adverse effect on its results of operations and financial condition.

Foreign currency fluctuations could affect expenses and any future earnings

The Company is exposed to foreign exchange fluctuations with respect to the Mongolian Tugrik, Chinese Renminbi, Hong Kong, Australian and Canadian dollars. The Company's financial results are reported in U.S. dollars. The salaries for local laborers in Mongolia are paid in local currency. Sales of coal into the PRC have been and may continue to be settled in U.S. dollars and Renminbi. The Company has a subsidiary in Hong Kong where some expenses are incurred in Hong Kong dollars. The Company has long term investments denominated in Australian dollars. Since the Company's headquarters is in Canada, a minor portion of its expenses are in Canadian dollars and the Company holds a portion of its cash in Canadian dollars. As a result, its financial position and results are impacted by the exchange rate fluctuations between the aforementioned currencies and the U.S. dollar.

The Company's results of operations are subject, to a significant extent, to economic, political and legal developments in the PRC

The Company expects that a majority of coal sales from the Ovoot Tolgoi Mine will be made to customers based in the PRC. Accordingly, the economic, political and social conditions, as well as government policies of the PRC may affect its business. The PRC economy differs from the economies of most developed countries in many respects, including: (i) structure; (ii) level of government involvement; (iii) level of development; (iv) growth rate; (v) control of foreign exchange; and (vi) allocation of resources. The PRC economy has been transitioning from a planned economy to a more market-oriented economy. For the past two decades, the PRC government has implemented economic reform measures emphasizing the utilization of market forces in the development of the PRC economy. Changes in the PRC's political, economic and social conditions, laws, regulations and policies could materially and adversely affect the Company's business and results of operations.

14. RISK FACTORS (Continued)

In addition, the PRC government indirectly influences coal prices through its regulation of power tariffs and its control over allocation of the transportation capacity of the national rail system. Any significant downturn in the prices in the PRC could materially and adversely affect the Company's business and results of operations. Additionally, the PRC government could adopt new policies that could shift demand away from coal to other energy sources. Any significant decline in demand for, or over-supply of, coal could materially and adversely affect the Company's revenues from coal export sales.

The interests of the Company's principal shareholder, Turquoise Hill, may differ from those of its other shareholders

As of December 12, 2013, Turquoise Hill holds approximately 56% of the Company's issued and outstanding common shares. The interests of Turquoise Hill may conflict with the interests of the Company's other shareholders and there is no assurance that Turquoise Hill will vote its common shares in a way that benefits the Company's minority shareholders. Subject to the CIC's right to appoint a director, Turquoise Hill's ownership interest enables Turquoise Hill to elect the entire Board without the concurrence of any of the Company's other shareholders. Accordingly, unless applicable laws or regulations would require approval by the Company's minority shareholders, Turquoise Hill is in a position to: (i) control the Company's policies, management and affairs; (ii) subject to applicable laws, regulations and the Articles, adopt amendments to certain provisions of the Articles; and (iii) otherwise determine the outcome of most corporate actions, including a change in control, merger or sale of all or substantially all of the Company's assets.

The Company believes that third parties may be discouraged from making a tender offer or bid to acquire the Company because of this concentration of ownership.

Information in this document regarding future plans reflects current intentions and is subject to change

Whether the Company ultimately implements the business strategies described in this document will depend on a number of factors including, but not limited to: the political situation in Mongolia and the PRC; the availability and cost of capital; current and projected coal prices; coal markets; costs and availability of drilling services, costs and availability of heavy equipment, supplies and personnel; success or failure of activities in similar areas to those in which the Company's projects are situated; and changes in estimates of project completion costs. The Company will continue to gather information about its projects, and it is possible that additional information will cause it to alter its schedule or determine that a project should not be pursued at all. Accordingly, the Company's plans and objectives may change from those described in this document.

14. RISK FACTORS (Continued)

Future stock market conditions may change

There are risks involved with any equity investment. The market price of common shares may rise or fall depending upon a range of factors and stock market conditions, which are unrelated to the Company's future financial performance. Movements on international stock markets, local interest rates and exchange rates, domestic and international economic and political conditions, as well as government, taxation and other policy changes may affect the stock market. As the Company is a listed company on the TSX and the HKEX, its common share price will also be subject to numerous influences including broad trends in the stock market and the share prices of individual companies or sectors.

Future issuances or sales, or perceived possible issuances or sales, of substantial amounts of common shares in the public market could materially and adversely affect the prevailing market price of the common shares and the Company's ability to raise capital in the future

The market price of the common shares could decline as a result of future sales of substantial amounts of the common shares or other securities relating to the common shares in the public market, including sales by its substantial shareholders, or the issuance of new common shares by the Company, or the perception that such sales or issuances may occur. Future sales, or perceived possible sales, of substantial amounts of the common shares could also materially and adversely affect the Company's ability to raise capital in the future at a time and at a price favorable to it, and the Company's shareholders may experience dilution in their holdings upon issuance or sale of additional common shares or other securities in the future.

15. OUTLOOK

The year ended December 31, 2012 was a tumultuous year for the Company with full curtailment of production from the end of June 2012 with the position unchanged at year end, the announcement of a proportional takeover bid by CHALCO and subsequent termination of the bid, ongoing investigations by the Mongolian authorities and claims of wrongdoing and involvement in investigations against Mongolian public figures. In addition, there were significant changes at the board and senior management level within the organization and the year culminated in the necessity to reduce the Company's overall workforce by nearly one third. The subsequent net loss of $97.5 million recorded by the Company in 2012 reflects these conditions.

The Company resumed operations at the Ovoot Tolgoi Mine on March 22, 2013 after having been fully curtailed since the end of the second quarter of 2012. In the second quarter of 2013, the Company primarily moved waste material (overburden) and exposed coal in the pit. Sales volumes increased in the third quarter of 2013 and, as planned, raw coal production increased to meet contracted sales volumes. The rate of production in the fourth quarter of 2013 is expected to increase compared to the third quarter of 2013 as the Company provides contractual tonnages under current coal supply agreements and makes further sales. The Company expects total coal sales in excess of 1.50 million tonnes in the fourth quarter of 2013 subject to customer performance under the current coal supply agreements. As a result, the Company expects 2013 annual raw coal production of approximately 3.0 million tonnes.

Whilst SouthGobi has a predominantly two product strategy of a Premium and Standard semi-soft coking coal product from the Ovoot Tolgoi Mine, the capability to begin supplying a washed semi-soft coking coal product is an important step in improving both SouthGobi's market position and access to end customers. The Company is currently cooperating with Ejin Jinda in studying the utilization of the wet washing facility. SouthGobi has, however, commenced mining and selling some Premium semi-soft coking coal product as a raw coal in 2013.

The Company has been minimizing uncommitted capital expenditures, exploration and operational expenditures in order to preserve its financial resources.

15. OUTLOOK (Continued)

Longer term, SouthGobi remains well positioned, with a number of key competitive strengths, including:

- Strategic location – SouthGobi is the closest major coking coal producer in the world to China. The Ovoot Tolgoi Mine is approximately 40km from China, which is approximately 190km closer than Tavan Tolgoi coal producers in Mongolia and 7,000 to 10,000km closer than Australian and North American coking coal producers. The Company has an infrastructure advantage, being approximately 50km from existing railway infrastructure, which is approximately one tenth the distance to rail of Tavan Tolgoi coal producers in Mongolia.
- Premium quality coals – Most of the Company's coal resources have coking properties, including a mixture of semi-soft coking coals and hard coking coals.
- Favorable cost structure – The long-term cost structure of SouthGobi provides a strong base for sustainable growth when access to end-user markets is obtained.
- Substantial resource base – The Company's aggregate coal resources (including reserves) include measured and indicated resources of 533 million tonnes and inferred resources of 302 million tonnes.

Objectives

The Company's objectives for 2013 are as follows:

- Resume production at the Ovoot Tolgoi Mine – The Company reviewed the overall structure of its workforce and market conditions and recommenced mining activities at the Ovoot Tolgoi Mine in March 2013. The focus has been to recommence mining activities in a safe manner that provides a sustainable long-term operating base.
- Continue to develop regional infrastructure – The Company's priority was to complete the construction of the paved highway from the Ovoot Tolgoi Mine to the Shivee Khuren Border Crossing as part of the existing consortium that was awarded the tender by the end of 2013. Construction of the paved highway is expected to be substantially complete by the end of 2013. The remaining construction work and commissioning of the paved highway is expected to be completed by the end of the first half of 2014.

15. OUTLOOK (Continued)

- Advance the Soumber Deposit – The Company intends to substantially advance the feasibility, planning and physical preparation of the Soumber Deposit in order to commence small-scale mining activities in 2014.
- Value-adding/upgrading coal – Implement an effective and profitable utilization of the wet washing facility contracted with Ejin Jinda to toll-wash coal from the Ovoot Tolgoi Mine and further develop the Company's marketing plans on product mix and seek to expand the Company's customer base. The Company is currently cooperating with Ejin Jinda in studying the utilization of the wet washing facility.
- Re-establish the Company's reputation – The Company's vision is to be a respected and profitable Mongolian coal company. This will require re-establishing good working relationships with all our external stakeholders.
- Operations – Continuing to focus on production safety, environmental protection, operational excellence and community relations.

December 12, 2013