
SouthGobi
ENERGY RESOURCES
ANNUAL REPORT 2009

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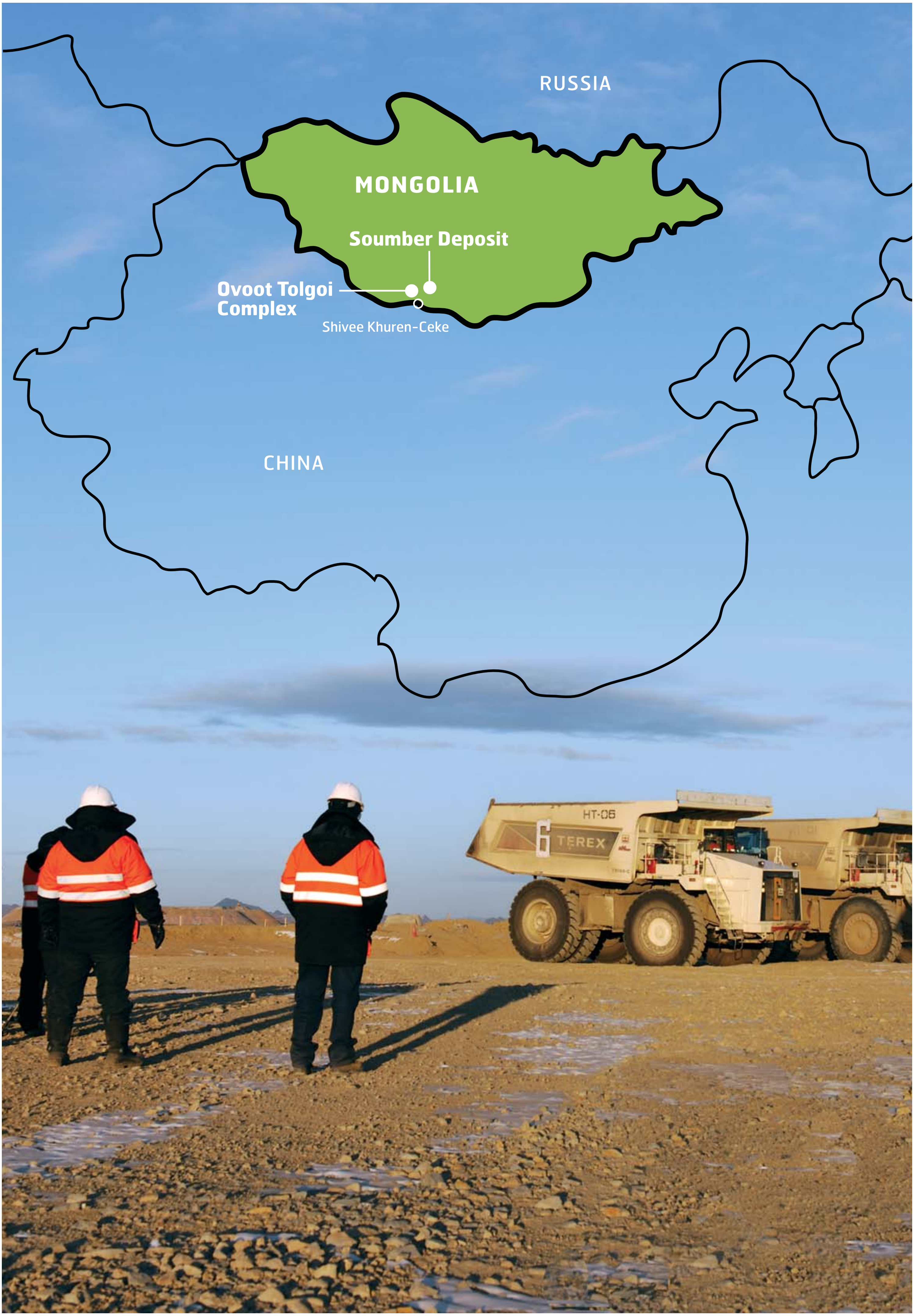
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SOUTHGOBI ENERGY RESOURCES LTD. COMPANY HIGHLIGHTS

The Company

SouthGobi Energy Resources Ltd. is a premium coal company with an operating mine and several development projects in Mongolia. The company is one of the largest coal producers in Mongolia in terms of coal sales for export. The company is listed on both the main boards of the Toronto (TSX: SGQ) and Hong Kong (HKEX: 1878) stock exchanges.

The company's flagship project is the Ovoot Tolgoi open pit mine located in the South Gobi province of Mongolia, approximately 40 kilometers from the Mongolia-China border (Shivee Khuren-Ceke). Since the commencement of mining operations in mid-2008 the mine has produced over 1.8 million tonnes of coal. The most important of the company's development projects is the Soumber deposit. The Soumber deposit is located approximately 20 kilometers east of the Ovoot Tolgoi mine, which could allow the operations to share existing infrastructure. SouthGobi's coals at both Ovoot Tolgoi and Soumber have the properties of higher value premium coking coals.

In addition, the company holds 18 mineral exploration licenses in Mongolia covering approximately 784,000 hectares. Each of these licenses and the related mining assets are wholly owned by the company.

Major Achievements

Some of the major achievements of the company since January 1, 2009 include:

- The Company has sold 1.3 million tonnes of coal in 2009 for export to China at an average sales price of US$28.97 per tonne.
- On October 12, 2009, the company announced it had completed a pre-feasibility study for the Ovoot Tolgoi mine and a resource estimate for the Soumber deposit. Total measured and indicated resources increased by 39% across all assets.
- In November of 2009, the China Investment Corporation ("CIC") invested US$500 million (gross) in the company through a convertible debenture, representing a strong endorsement for SouthGobi's future plans and prospects.
- On December 3, 2009, the company transferred the listing of its common shares from the TSX Venture Exchange to the main board of the Toronto Stock Exchange ("TSX"). The TSX, serving the senior equity market, is the largest stock exchange in Canada and the third largest in North America.
- In December of 2009, SouthGobi successfully commissioned the first of its new Liebherr 996 mining shovels at Ovoot Tolgoi. The Liebherr 996 shovel has a bucket capacity of around two and a half times that of the existing Liebherr 994 shovel that was in sole operation. The Company has two additional Liebherr 996 fleets on order or under option for expansion at Ovoot Tolgoi.
- On January 29, 2010, the company successfully completed an international share offering for gross proceeds of US$437 million. Simultaneously with the international offering, the company's shares began trading on the Hong Kong Stock Exchange under the ticker HKEX:1878.

Our Reserves and Resources

Below is a summary of the company's reserves and resources *(expressed in millions of tonnes)*:

RESERVES

Area	Proven	Probable	Total
Ovoot Tolgoi Mine	105.0	9.1	114.1

RESOURCES

Area	Measured	Indicated	Inferred	Total
Ovoot Tolgoi Mine	135.9	35.1	13.0	184.0
Ovoot Tolgoi Underground	45.8	33.0	20.5	99.3
Soumber	13.1	8.3	55.5	76.9
Tsagaan Tolgoi	23.4	13.0	9.0	45.4
Total Resources	**218.2**	**89.4**	**98.0**	**405.6**

MESSAGE FROM THE CHAIRMAN

2009 was a transformational year for SouthGobi, which is now the largest purely coal focused company listed on the Toronto Stock Exchange by market capitalization and has also successfully listed on the Hong Kong Stock Exchange. We have established ourselves as a fully fledged coal producer, strengthened our balance sheet, internationalized our investor base and added a number of senior executives to our management team. SouthGobi is now exceptionally well placed with the financial and leadership resources to accelerate the development of its Mongolian coal assets and lead its sector in terms of growth in the coming years.

Despite the remnants of the global financial crisis, 2009 was a very positive year for SouthGobi. Firstly, Mongolia, where our core premium coal resources are located, continued to mature as a positive investment destination. Mongolia has been a constitutional democracy since 1992 and today has two strong political parties, the Mongolian People's Revolutionary Party (MPRP) and the Democratic Party (DP). In late 2008 the two parties formed a coalition government and during 2009 a number of significant milestones were achieved towards supporting economic reform and growth in Mongolia, including avid support for accelerated development of the nation's key mining sector. In October 2009 the Government of Mongolia, Ivanhoe Mines and Rio Tinto signed an investment agreement to support the development of Oyu Tolgoi, the world's largest undeveloped copper-gold deposit located in Mongolia. The signing of this agreement and the various legislative changes to support the mining industry is clear evidence that Mongolia has strong policies to drive the development of the industry. Various international agencies now forecast Mongolia to be one of the fastest growing global economies over the next ten years. The IMF projects Mongolia's GDP will more than double by 2014.

The second supportive macro trend that became very clear during 2009 was the continued growth in China's requirements for imported coal. China has been a coal producer in transition for the last decade as its domestic economic activity has grown. After being a significant coal exporter for many years, China became a net coal importer in 2006. China increasingly needs to import coal for a variety of reasons. There are certain types of coal, in particular coking coal, which China does not possess in great quantities. Furthermore, China's coal resources are generally becoming higher cost to mine or must be transported long distances to various regional markets. The continuation of the trend established in 2006 was clear in 2009 as China imported 130 million tonnes of coal, more than twice the imports of the prior year. Mongolia, being uniquely situated to supply coal to inland regions of China, benefited from the trend with total coal exports of 7.2 million tonnes in 2009, almost entirely to China.

SouthGobi is a first mover in Mongolia and a first mover in terms of selling its coal to China. 2009 was a very successful year for the company in terms of being able to produce and sell 1.3 million tonnes of coal in the first full calendar year of production at its flagship Ovoot Tolgoi Mine. Our business stands to benefit from the continuation of the positive trends observed. SouthGobi's premium coal resources are located entirely in Mongolia and are benefiting from a stable investment environment there. Ovoot Tolgoi is situated only 40 kilometers from the Chinese border and our Ovoot Khural Basin coal assets are the closest producing coal assets to China. Furthermore, Ovoot Tolgoi is closer to coal markets in the Gansu province of China than most Chinese producers.

STRATEGY

Having succeeded in becoming a premium coal producer and exporter, SouthGobi's core strategy is to extract full value from our leadership position in the Ovoot Khural Basin. The Ovoot Khural Basin hosts Permian Age coals generally with the properties of higher value coking coals and typically in open pit mineable deposits. Our first producing coal mine, Ovoot Tolgoi and 89% of the company's total resource base is located within the Ovoot Khural Basin. SouthGobi intends to create value through focusing on the integrated advancement of the Ovoot Khural Basin involving: identification of additional premium coal resources through exploration; development and growth of existing mines and resources; construction of lasting infrastructure; and the introduction of value-added processing such as coal washing.

PEOPLE

At the end of 2009, SouthGobi had 334 employees. The majority of our workforce is located in Mongolia at our mining and exploration operations in the Ovoot Khural Basin and our Ulaanbaatar office. I'm proud to say that of the 316 employees the company had in Mongolia, 98% were Mongolian nationals and 33% were from the local soum (district) of Gurvantes that surrounds our Ovoot Tolgoi Mine. It's also exciting for us to see how quickly SouthGobi is adding employment opportunities. We grew our workforce in Mongolia by 42% in 2009. It's also pleasing that Mongolia's National Chamber of Commerce and Industry recognized our success by awarding SouthGobi "Local Job Creator of the Year" for 2009.

During the year, SouthGobi substantially built-out its executive team as well. In February, the company announced the recruitment of former senior mining sector investment banker, Alexander Molyneux as President and in October I stepped down as Chief Executive Officer, handing those responsibilities to Alexander. In September, Gavin May joined the company as Chief Operating Officer. Gavin has more than 28 years experience in the coal industry, including as Chief Executive Officer of Gloucester Coal, a successful Australian coking coal producer.

On behalf of shareholders, I would like to thank Alexander and his team for their efforts in 2009 and resultant success.

SOCIAL CONTRIBUTION

SouthGobi is committed to contributing to our communities. Among other contributions, SouthGobi has donated 10 million Tugriks to the Gobi Development Fund, computers and beds to the Gurvantes hospital and office furniture to local organizations. The company has also renovated the Gurvantes secondary school dormitory to provide the students with a better learning and living environment. In addition, SouthGobi runs a university scholarship program, and provided six students from Gurvantes Soum with scholarships to study at respected universities in the Mongolian capital of Ulaanbaatar and Dornogobi Aimag.

As Chairman of SouthGobi, I look forward to working with my board to support our management team in achieving the goals they have set for 2010.

Peter G. Meredith
DIRECTOR, CHAIRMAN OF THE BOARD

MESSAGE FROM THE PRESIDENT AND CEO

SouthGobi, through its extensive existing resources and prospective exploration permits across the Ovoot Khural Basin in Mongolia has tier one global coking coal assets.

The quality of SouthGobi's business is represented by a number of factors including:

- *Strategic location* – Our Ovoot Tolgoi producing mine and the Ovoot Khural Basin more broadly is the closest coal resource to China. Furthermore, China has developed infrastructure on its side of the border such that Ovoot Tolgoi is only around 50 kilometers away from the nearest dedicated coal carrying railway. The markets in Northern China near our properties are also very attractive. For example, Inner Mongolia is currently China's fastest growing province in terms of GDP growth.

- *Substantial yet growing resources* – SouthGobi has 308 million tonnes of measured and indicated resources with a further 98 million tonnes in the inferred category. However, exploration is still a core part of the company's medium term future. SouthGobi has 784,358 hectares of exploration permits in Mongolia and intends to accelerate exploration expenditure.

- *Premium quality coal* – Generally the coal contained in our Ovoot Khural Basin deposits have coking characteristics and coal at our Soumber deposit is considered hard coking coal.

- *Leading cost structure* – Last year AME Mineral Economics assessed cash costs for the open pit Ovoot Tolgoi Mine in the lowest 10% of its global semi-soft/PCI coking coal industry cost curve.

- *Strong growth potential* – The capital expansion plan at Ovoot Tolgoi Mine aims to expand the potential for coal sales over 2009 levels by five to six fold. Furthermore, Soumber appears to be an attractive deposit that will be our priority for an additional open pit mine for development.

Our goals for 2009 were based on establishing a platform from which we could realize the latent value we recognize in SouthGobi. In an operating context, we established safe, consistent and reliable mining and sales of our coal. In a capital market context, we secured the funding to finance the next stage of development of our assets and established liquid main board listings where a variety of investors can join the opportunity by investing with us.

MINING AND EXPLORATION

Having commenced operations in 2008, 2009 was the first full year of sales for Ovoot Tolgoi Mine, the company's first producing mine. 1.3 million tonnes of coal was sold to Chinese customers at an average cash margin of US$12.39 per tonne at the mine gate.

Relative to sales, substantially less coal was mined at 0.7 million tonnes. The reason is that mining was curtailed and then suspended during the first half of the year due to difficulty expediting coal shipments at the Mongolia-China border in the first quarter. The issue was rectified in March but mining remained suspended until July 1, 2009, to manage the size of the company's coal inventory, which at one stage was over 1 million tonnes.

Mining continued smoothly in the second half of the year predominantly with the company's first mining fleet (based around a Liebherr 994 shovel and seven Terex TR100 trucks). In December 2009, SouthGobi commissioned its first Liebherr 996 hydraulic shovel (34 m^3 scoop capacity vs. 994's 13.5 m^3) and its first two Terex MT4400 trucks (218 tonne vs. 91 tonne for TR100) at Ovoot Tolgoi, which will transformationally increase mining capacity there.

For exploration, SouthGobi established a focus on the Ovoot Khural Basin properties that are to the east and west of the existing Ovoot Tolgoi mining license. In October 2009, SouthGobi was able to reveal an NI 43-101 compliant resource for Soumber. Soumber is important because it is the first new significant deposit along strike from Ovoot Tolgoi in the Ovoot Khural Basin. It is approximately 20 kilometers to the east of Ovoot Tolgoi and could therefore likely benefit from some combined infrastructure.

FUNDING AND CAPITAL MARKETS

During 2009 and in January 2010 SouthGobi raised approximately US$900 million in net proceeds from two major financing events.

In November 2009, China Investment Corporation ("CIC") became an important stakeholder by investing US$500 million (gross) in SouthGobi through a convertible debenture. The investment represents a strong endorsement of SouthGobi's business plan and prospects. As a sovereign wealth fund, SouthGobi anticipates a strong long term relationship with CIC as an investor. Its strong knowledge of China and willingness to assist SouthGobi in the areas of coal sales, logistics and procurement in China could create substantial incremental value to be shared by all investors.

In January 2010, SouthGobi completed its long planned Asian secondary listing by listing its shares on the Hong Kong Stock Exchange and raising US$437 million (gross) with a concurrent offering. Being listed in Hong Kong is an important milestone. The company's peer investment opportunities are generally listed in Hong Kong, which is not only the most important investment market for regional coal stocks but is also emerging as a global center for coal equities.

With the capital raised, SouthGobi repaid the line of credit facility to Ivanhoe Mines Ltd., which was its primary source of funding in 2009. The company now has substantial cash resources and will be able to commit to the medium-term plan to grow its business without relying on external capital markets.

SouthGobi is now listed on the main boards of both the Toronto and Hong Kong Stock Exchanges so we have established two significant liquid markets for our shares where a variety of investors will be able to 'come on board'.

SAFETY AND ENVIRONMENT

SouthGobi delivered its 2009 goals without any major safety or environmental incidents. We're proud of that achievement and continue to view our operating excellence in these fields as the most important discipline.

OBJECTIVES FOR 2010

Our objectives for 2010 are as follows:

- *Grow Ovoot Tolgoi Mine* – The additional capacity of the already commissioned Liebherr 996 fleet should support strong growth in coal availability and sales for 2010 over 2009. Additional Terex MT4400 trucks are planned to be commissioned in the first half of 2010 and an additional Liebherr 996 fleet is expected to arrive before the end of the year.

- *Continue to develop regional infrastructure* – Our immediate priority centers on improving roads in the area around Ovoot Tolgoi Mine and contributing to new road development.

- *Advancing the Soumber deposit* – SouthGobi intends to further define the deposit with continued exploration work whilst also substantially advancing the feasibility, planning and licensing for a mine at Soumber.

- *Value-adding/upgrading coal* – We intend to embark on the construction of our first coal handling/processing facility. This first stage will involve basic coal crushing and screening for Ovoot Tolgoi coals to create a more consistent higher quality product for customers.

- *Exploration* – Further green fields exploration will take place, with the company planning an exploration campaign budget in the order of US$10 to 20 million.

- *Continuing to focus on production safety, environmental protection, operational excellence and community relations.*

I believe SouthGobi has both the people and financial resources to deliver on our objectives, which will set the company up for yet another transformational leap in its development and I look forward to participating.

Alexander Molyneux
PRESIDENT AND CHIEF EXECUTIVE OFFICER

BOARD OF DIRECTORS

Peter Meredith
CHAIRMAN OF THE BOARD, NON-EXECUTIVE DIRECTOR

Mr. Meredith, 66, joined the Company on August 13, 2003 and has been a Director since then. He was the Chief Executive Officer of the Company from June 2007 to October 2009, and Chairman of the Board since October 2009. He has served as the Deputy Chairman of Ivanhoe Mines Ltd., the Corporation's principal shareholder, since May 2006, overseeing Ivanhoe's business development and corporate relations. Prior to joining Ivanhoe, Mr. Meredith spent 31 years with Deloitte and Touche LLP, Chartered Accountants, and retired as a partner in 1996.

Mr. Meredith is a Chartered Accountant, certified by the Canadian Institute of Chartered Accountants and is a member of the Institute of Chartered Accountants of British Columbia, the Institute of Chartered Accountants of Ontario and the Ordre des Comptables Agréés du Québec. He is also a Certified Management Accountant, certified by the Society of Management Accountants of Canada and is a member of the Certified Management Accountants Society of British Columbia.

Alexander Molyneux
PRESIDENT AND CHIEF EXECUTIVE OFFICER, DIRECTOR

Mr. Molyneux, 35, joined the Company as President in April 27, 2009. On October 11, 2009, he was given the additional responsibilities of Chief Executive Officer and appointed as a Director. He is based in Hong Kong, and was most recently Managing Director, Head of Metals & Mining Investment Banking, Asia Pacific, with Citigroup. He has spent approximately 10 years providing specialist advice and investment banking services to mining and industrial corporations, including nine years involved in coal-related transactions. Over the past nine years, he has advised coal-related public offerings, mergers and acquisitions, bond and debt offerings totaling several billion dollars. He joined Citigroup from UBS in early-2007 as Head of Metals & Mining Investment Banking.

Mr. Molyneux holds a Bachelor degree in Economics from Monash University in Australia.

Pierre Lebel
INDEPENDENT NON-EXECUTIVE DIRECTOR AND LEAD DIRECTOR

Mr. Lebel, 60, joined the Company on August 13, 2003 and has been a Director since then. Mr. Lebel is the Company's Lead Director and served as its Chairman from 2003 until June 2007. He has a distinguished career in mining spanning over 25 years, with a primary focus on mine financing, construction and development. Mr. Lebel currently serves as Chairman and a Director of Imperial Metals Corporation, a TSX-listed mine developer and operator. In 1998, Mr. Lebel was awarded the E.A. Scholz Medal by the BC and Yukon Chamber of Mines in recognition of his outstanding contribution towards the construction and development of Imperial's Mount Polley copper/gold mine in British Columbia.

Mr. Lebel holds a Masters of Business Administration from McMaster University and a Bachelor of Laws (LLB) from the University of Western Ontario. He is a barrister and solicitor admitted by the Law Societies of British Columbia and Alberta. He is also a member of the Board of Directors of the Mining Association of British Columbia and a member of the Institute of Corporate Directors.

André Deepwell
INDEPENDENT NON-EXECUTIVE DIRECTOR

Mr. Deepwell, 55, joined the Company on August 13, 2003 and has been a Director since then. He has been the Chief Financial Officer and Corporate Secretary of a number of natural resource companies over the last fifteen years and is currently Chief Financial Officer and Corporate Secretary of Imperial Metals Corporation, a TSX-listed mine developer and operator. Mr. Deepwell has been involved in all aspects of debt and equity financings and financial reporting for mining enterprises ranging from grassroots exploration to mine development and production.

Mr. Deepwell is a Chartered Accountant, certified by the Institute of Chartered Accountants of British Columbia. He is a member of the Institute of Corporate Directors.

R. Stuart (Tookie) Angus
INDEPENDENT NON-EXECUTIVE DIRECTOR

Mr. Angus, 61, joined the Company on May 25, 2007 and has been a Director since then. Mr. Angus is an independent consultant to the mining industry and has over 12 years experience advising companies in the mineral resources industry. Previously, he was Managing Director – Mergers and Acquisitions with Endeavour Financial Corporation, which provides financial advisory services to the mining and minerals industries. Prior to joining Endeavour Financial in 2003, he was a senior partner in the law firm, Fasken Martineau DuMoulin, as head of its Global Mining Group.

Mr. Angus holds a Bachelor of Laws (LLB) from the University of British Columbia and is a retired member of the Law Society of British Columbia. He is a member of the Institute of Corporate Directors.

Robert Hanson
INDEPENDENT NON-EXECUTIVE DIRECTOR

Mr. Hanson, 49, joined the Company on May 25, 2007 and has been a Director since then. He has been an independent Non-Executive Director of Ivanhoe Mines Ltd., the Corporation's principal shareholder, since February 2001. He is the Chairman of Hanson Capital Investments Limited, Strand Hanson Group and the Hanson Family Holdings (formerly Hanson Transport Group Limited), and he is also Managing Partner of Millennium Hanson Internet Partners. He was Chairman of Hanson Westhouse Limited from February 1998 to April 2009 and an Associate Director of N.M. Rothschild & Sons from 1983 to 1990, serving in London, Hong Kong, Chile and Spain. From 1990 to 1997, he served on the Board of Directors of Hanson PLC, responsible for strategy, mergers and acquisitions transactions.

Mr. Hanson was educated at Eton and received his Master of Arts in English Language & Literature from St Peter's College, Oxford. He is a trustee of the Hanson Foundation and a founding trustee of the Raisa Gorbachev Foundation fighting child cancers. He is a member of the Institute of Corporate Directors.

John Macken
NON-EXECUTIVE DIRECTOR

Mr. Macken, 58, joined the Company as a Non-Executive Director on June 25, 2007. He was the Chairman of SouthGobi Energy Resources Ltd. from June 2007 to October 2009. He joined Ivanhoe Mines Ltd., the Corporation's principal shareholder, in 2003 and is its President and Chief Executive Officer. He has been a member of Ivanhoe's Executive Committee since its formation in March 2005. Prior to joining Ivanhoe, Mr. Macken spent 19 years with Freeport McMoran Copper and Gold, most recently as Freeport's Senior Vice-President of Strategic Planning and Development.

Mr. Macken holds a Bachelor of Arts and a Bachelor of Arts in Engineering (Hons.) from Trinity College at Dublin University in Ireland. He is a Chartered Engineer certified by the Institute of Engineers in Ireland and was a Professional Engineer certified by the Province of Ontario, Canada.

R. Edward Flood
NON-EXECUTIVE DIRECTOR

Mr. Flood, 64, joined the Company on August 13, 2003 and has been a Director since then. He was its interim President and Chief Executive Officer from August 2006 to June 2007. He has been a Director of Ivanhoe Mines Ltd., the Corporation's principal shareholder, since its founding in 1994 and was also its President from founding until May 1999. He is the Chairman of Western Uranium Corporation, a mineral exploration corporation with a focus on uranium. Mr. Flood served as Deputy Chairman of Ivanhoe Mines Ltd. until February 2007, assisting in developing Ivanhoe's growth and its establishment as a significant presence in Asia's mineral exploration and mining sectors. Mr. Flood was Ivanhoe's founding President. Prior to joining Ivanhoe, from 1993 to 1995, Mr. Flood was a principal at Robertson Stephens & Co., a U.S. investment bank, and a member of Robertson Stephens' investment team. He also held the position of senior mining analyst with Haywood Securities Inc. from 1999 to 2001, and Managing Director, Investment Banking, Haywood Securities (UK) Ltd. from March 2007 to March 2010.

Mr. Flood holds a Masters of Science in Geology from the University of Montana and a Bachelor in Science in Geology from the University of Nevada. He is a member of the Institute of Corporate Directors.

SENIOR MANAGEMENT

Gavin May
CHIEF OPERATING OFFICER

Mr. May, 49, joined the Company on September 1, 2009 and has been the Chief Operating Officer since then. He has primary responsibility for operating aspects of the business. Mr. May has over 21 years experience in the coal industry. He was a Director of Noble Resources Australia Pty. Ltd., a trading company which is a member of Singapore Exchange-listed Noble Group, from January 2008. From 1997 to July 2007, he held various positions including the Chief Executive Officer, a Director and a Marketing Director at Gloucester Coal Ltd., an ASX-listed coal company, and its predecessor company.

Mr. May holds a Bachelor of Science degree in Geology from Macquarie University in Australia. He completed the Australian Institute of Company Director's Course with an Order of Merit in 2000.

Terry Krepiakevich
CHIEF FINANCIAL OFFICER

Mr. Krepiakevich, 57, joined the Company on July 17, 2006 and has been the Chief Financial Officer since then. He has been a Director of Alexco Resource Corp., a TSX-listed and NYSE-listed mineral resources company, since July 2009. He was previously the Chief Financial Officer of Extreme CCTV Inc., a formerly TSX-listed company (since acquired), from November 2000 to July 2006 and was also a Director from June 2001 to July 2006. Mr. Krepiakevich was the Chief Executive Officer and a Director of First Industrial Capital Corp. from September 1997 to March 2004. He was the Vice President of Finance and Chief Financial Officer of Maynards Industries from July 1988 to June 2000.

Mr. Krepiakevich is a Chartered Accountant, certified by the Institute of Chartered Accountants of British Columbia.

DIRECTORS' REPORT

The Board of Directors (the "Board") of SouthGobi Energy Resources Ltd. is pleased to present their report together with the audited consolidated financial statements (the "Financial Statements") of SouthGobi Energy Resources Ltd. together with its subsidiaries (collectively the "Company") for the financial year ended December 31, 2009 ("Financial Year").

PRINCIPAL ACTIVITIES AND GEOGRAPHICAL ANALYSIS OF OPERATIONS

The principal activity of the company is to provide business services and general mining support services for its subsidiaries and the principal activities of the Company are the acquisition, exploration, development and production of coal properties. The Company's principal subsidiaries are set out in Note 30 of the Financial Statements and the activities of the principal subsidiaries of the Company at December 31, 2009 are set out in the table below:

Name	Country of incorporation	Issued and fully paid share capital	Principal activities
Asia Gold International Holding Company Ltd.	British Virgin Islands	Nil	Investment holding
SouthGobi Energy Resources (Hong Kong) Ltd.	Hong Kong	HK$1	Business services
Dayarbulag LLC	Mongolia	MNT 12,120,000	Investment holding
SouthGobi Sands LLC	Mongolia	MNT 11,655,000	Exploration and development of mineral properties in Mongolia
Transbaikal Gold	Russia	10,000 Russian Roubles	Research, exploration and extraction of minerals
SGQ Coal Investment Pte. Ltd.	Singapore	US$1	Investment holding
SGQ Dayarcoal Mongolia Pte. Ltd.	Singapore	US$1	Investment holding

The analysis of the principal activities by geographical location of the operations of the Company for the Financial Year is set out in Note 5 of the Financial Statements.

RESULTS

The results of the Company for the Financial Year are set out in the Consolidated Statement of Comprehensive Income on page 68.

DIVIDENDS

The Board has not recommended, declared or paid any dividends for the Financial Year.

PROPERTY, PLANT AND EQUIPMENT

Details of the movement in the property, plant and equipment of the Company during the Financial Year are set out in Note 20 of the Financial Statements.

SHARE CAPITAL

Details of the movement in the share capital of the Company during the Financial Year are set out in Note 25 of the Financial Statements.

RESERVES

Details of the reserves available for distribution to the shareholders as at December 31, 2009 are set out in the Consolidated Statement of Changes in Equity on page 70.

DIRECTORS

The directors during the Financial Year and up to the date of this report are as follows:

Executive Directors

Mr. Alexander Molyneux

Non-Executive Directors

Mr. Peter Meredith *(Chairman)*
Mr. John Macken
Mr. R. Edward Flood

Independent Non-Executive Directors

Mr. Pierre Lebel *(Lead Director)*
Mr. André Deepwell
Mr. R. Stuart (Tookie) Angus
Mr. Robert Hanson

The term of office for each of the directors will end at the conclusion of the forthcoming annual general meeting. Each of the directors offers themselves for re-election at the annual general meeting scheduled for May 11, 2010.

In accordance with article 14.1 of the articles of continuation for the Company, each of the directors, including the independent non-executive directors, are subject to retirement and re-election annually at the annual general meeting.

DIRECTORS' SERVICE CONTRACTS

None of the directors proposed for re-election at the forthcoming annual general meeting has a service contract with the Company which is not determinable by the Company within one year without payment of compensation, other than statutory compensation.

DIRECTORS' INTERESTS IN CONTRACTS OF SIGNIFICANCE

No contracts of significance to which the Company was a party and in which a director of the Company had a material interest, whether directly or indirectly, subsisted at December 31, 2009 or at any time during the Financial Year.

DIRECTORS' INTERESTS IN COMPETING BUSINESSES

During the Financial Year and up to the date of this report, to the best knowledge of the directors, none of the directors had any interests in businesses that compete or are likely to compete, either directly or indirectly with the Company.

DIRECTORS' AND CHIEF EXECUTIVES' INTERESTS IN SHARES AND SHARE OPTIONS

At December 31, 2009, the interests of the directors, Mr. Gavin May, the Chief Operating Officer of the Company and Terry Krepiakevich, the Chief Financial Officer of the Company, in the shares and share options of the Company and its associated corporations were as follows:

Shares

Name	Name of company	Nature of interest	Shares held	Approximate percentage interest in the company
Peter Meredith	SouthGobi Energy Resources Ltd.	N/A	nil	nil
	Ivanhoe Mines Ltd.	Personal	22,000	0.005%
Alexander Molyneux	SouthGobi Energy Resources Ltd.	N/A	nil	nil
	Ivanhoe Mines Ltd.	N/A	nil	nil
Pierre Lebel	SouthGobi Energy Resources Ltd.	Personal	5,100	0.004%
	Ivanhoe Mines Ltd.	N/A	nil	nil
André Deepwell	SouthGobi Energy Resources Ltd.	Personal	2,000	0.001%
	Ivanhoe Mines Ltd.	N/A	nil	nil
R. Stuart (Tookie) Angus	SouthGobi Energy Resources Ltd.	N/A	nil	nil
	Ivanhoe Mines Ltd.	N/A	nil	nil
Robert Hanson	SouthGobi Energy Resources Ltd.	Personal	17,500	0.013%
	Ivanhoe Mines Ltd.	Personal	150,000	0.035%
John Macken	SouthGobi Energy Resources Ltd.	N/A	nil	nil
	Ivanhoe Mines Ltd.	Personal	97,177	0.023%
R. Edward Flood	SouthGobi Energy Resources Ltd.	N/A	nil	nil
	Ivanhoe Mines Ltd.	Personal	102,534	0.024%
Gavin May	SouthGobi Energy Resources Ltd.	N/A	nil	nil
	Ivanhoe Mines Ltd.	N/A	nil	nil
Terry Krepiakevich	SouthGobi Energy Resources Ltd.	N/A	nil	nil
	Ivanhoe Mines Ltd.	N/A	nil	nil

Share Options

Name	Name of company	Number of options held
Peter Meredith	SouthGobi Energy Resources Ltd.	665,000
	Ivanhoe Mines Ltd.	2,102,500
Alexander Molyneux	SouthGobi Energy Resources Ltd.	625,000
	Ivanhoe Mines Ltd.	100,000
Pierre Lebel	SouthGobi Energy Resources Ltd.	190,000
	Ivanhoe Mines Ltd.	nil
André Deepwell	SouthGobi Energy Resources Ltd.	165,000
	Ivanhoe Mines Ltd.	nil
R. Stuart (Tookie) Angus	SouthGobi Energy Resources Ltd.	200,000
	Ivanhoe Mines Ltd.	nil
Robert Hanson	SouthGobi Energy Resources Ltd.	230,000
	Ivanhoe Mines Ltd.	147,500
John Macken	SouthGobi Energy Resources Ltd.	376,000
	Ivanhoe Mines Ltd.	4,900,000
R. Edward Flood	SouthGobi Energy Resources Ltd.	130,001
	Ivanhoe Mines Ltd.	329,500
Gavin May	SouthGobi Energy Resources Ltd.	400,000
	Ivanhoe Mines Ltd.	nil
Terry Krepiakevich	SouthGobi Energy Resources Ltd.	400,000
	Ivanhoe Mines Ltd.	25,000

Other than holdings in the preceding table none of the directors, senior management or their associates had any interests or short positions in any shares, underlying shares or debentures of the Company or of its associated corporations as at December 31, 2009.

MANAGEMENT CONTRACTS

No contracts concerning the management and administration of the Company were entered into or existed during the Financial Year.

SHARE OPTION SCHEME

The particulars of the Company's share option scheme are set out in Note 26 of the Financial Statements.

The following table discloses movements in the Company's share options for the Financial Year:

Name	Outstanding at beginning of year	Granted during year	Exercised during year	Forfeited during year	Expired during year	Outstanding at year end
Peter Meredith	670,000	75,000	(80,000)	–	–	665,000
Alexander Molyneux	–	625,000	–	–	–	625,000
Pierre Lebel	200,000	35,000	(45,000)	–	–	190,000
André Deepwell	175,000	35,000	(45,000)	–	–	165,000
R. Stuart (Tookie) Angus	165,000	35,000	–	–	–	200,000
Robert Hanson	195,000	35,000	–	–	–	230,000
John Macken	340,000	36,000	–	–	–	376,000
R. Edward Flood	95,001	35,000	–	–	–	130,001
Gavin May	–	400,000	–	–	–	400,000
Terry Krepiakevich	325,000	75,000	–	–	–	400,000
Total for directors and senior management	2,165,001	1,386,000	(170,000)	–	–	3,381,001
Total for other share option holders	4,421,054	1,285,000	(1,153,914)	(679,420)	–	3,872,720
Total	**6,586,055**	**2,671,000**	**(1,323,914)**	**(679,420)**	**–**	**7,253,721**

ARRANGEMENT TO PURCHASE SHARES AND DEBENTURES

Other than the option holdings disclosed above, at no time during the Financial Year was the Company a party to an arrangement to enable the directors of the Company to acquire benefits by means of the acquisition of shares in, or debentures of, the Company.

SUBSTANTIAL SHAREHOLDERS

The register of interests in shares and short positions of the Company showed that as at December 31, 2009, the Company has been notified of the following interests in shares representing 10% or more of the Company's issued share capital:

Name	Nature of interest	Shares held	Approximate percentage of issued shares
Ivanhoe Mines Ltd.	Beneficial	105,782,155	79%

Other than as disclosed above, the Company has not been notified of any relevant interests or short positions in the issued share capital of the Company as at December 31, 2009.

EMOLUMENT POLICY

The emolument policy of the executives of the Company is set up by the Compensation and Benefits Committee on the basis of merit, qualifications and competence. 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 decided by the Compensation and Benefits Committee and approved by the Board, having regard to comparable market statistics.

The Company has also adopted a share option plan as incentive to directors and eligible employees, details of the plan are set out in Note 26 of the Financial Statements.

PRE-EMPTIVE RIGHTS

There are no provisions for pre-emptive rights under the Company's articles of continuation or under the laws of Canada which would oblige the Company to offer new shares on a pro-rata basis to existing shareholders.

SUFFICIENCY OF PUBLIC FLOAT

The requirement that a prescribed percentage of shares of any class of listed securities must at all times be held by the public does not apply to the Company.

MAJOR CUSTOMERS AND SUPPLIERS

Details of the Company's transactions with its major suppliers and customers during the Financial Year are set out below:

Purchases

The largest supplier accounted for 32% of the Company's purchases.

The five largest suppliers accounted for 67% of the Company's purchases.

Sales

The largest customer accounted for 64% of the Company's sales.

The three largest customers accounted for 100% of the Company's sales.

At no time during the Financial Year did a director, an associate of a director or a shareholder of the Company (which to the knowledge of the directors owns more than 5% of the Company's share capital) have an interest in any of the Company's five largest suppliers or three largest customers.

CHARITABLE DONATIONS

During the Financial Year the Company made charitable donations amounting to MNT 10,000,000.

EVENTS AFTER REPORTING PERIOD

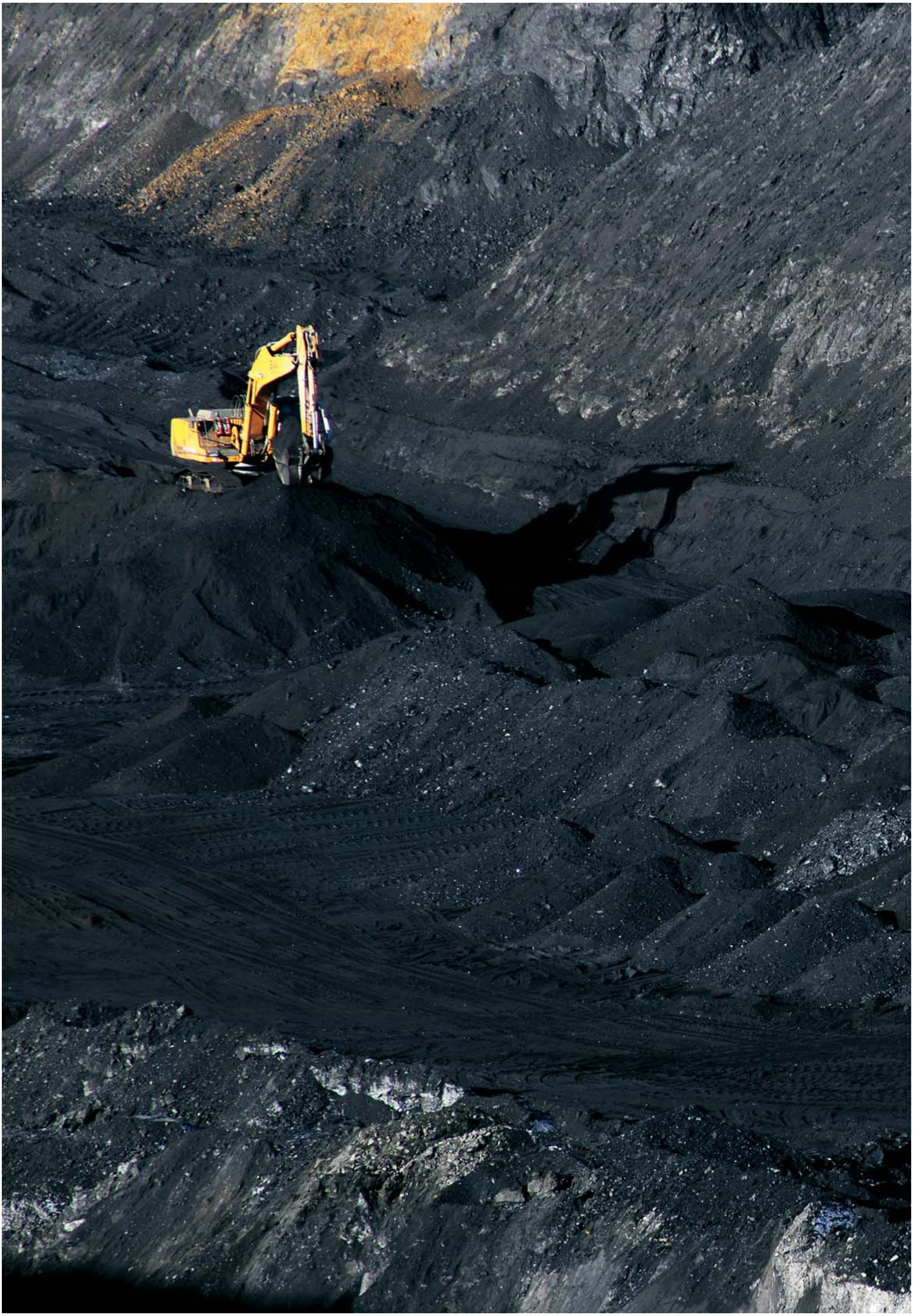
Details of the significant events occurring after December 31, 2009 are set out in Note 35 of the Financial Statements.

INDEPENDENT AUDITOR

A resolution will be submitted at the annual general meeting to re-appoint Deloitte & Touche LLP as auditors of the Company.

On behalf of the Board

Peter G. Meredith
DIRECTOR, CHAIRMAN OF THE BOARD
March 22, 2010



CORPORATE GOVERNANCE REPORT

CORPORATE GOVERNANCE

The Board of Directors (the "Board") considers good corporate governance practices to be an important factor in the continued and long term success of the Company by helping to maximize shareholder value over time.

To further this philosophy and ensure the Company follows good governance practices the Board has taken the following steps:

- approved and adopted a mandate for the Board;
- appointed Pierre Lebel an independent non-executive director, as "Lead Director", with specific responsibility for maintaining the independence of the Board and ensuring the Board carries out its responsibilities contemplated by applicable statutory and regulatory requirements and stock exchange listing standards;
- appointed an Audit Committee, a Nominating and Corporate Governance Committee and a Compensation and Benefits Committee consisting solely of independent directors;
- established an Environmental, Health and Safety Committee;
- approved charters for all of the Company's Board committees except the newly formed Environmental, Health and Safety Committee formalizing the mandates of those committees;
- established a management Disclosure Committee for the Company, with the mandate to oversee the Company's disclosure practices including the establishment of a sub-committee charged with overseeing the company's technical disclosure;
- formalized the Company's Corporate Disclosure, Confidentiality and Securities Trading Policy, and Disclosure Controls and Procedures;
- adopted a formal Code of Business Conduct and Ethics for the Company that governs the behavior of directors, officers and employees and which is also distributed to consultants;
- adopted formalized written position descriptions for the Chairperson, Lead Director, CEO and CFO, clearly defining their respective roles and responsibilities;
- adopted a whistleblower policy administered by an independent third party;
- formalized a process for assessing the effectiveness of the Board as a whole, the committees of the Board and the contribution of individual directors, on a regular basis; and
- adopted an executive compensation model for the Company.

COMPLIANCE WITH CORPORATE GOVERNANCE

The Company has, throughout the Financial Year, applied the principles and complied with the requirements of its corporate governance practices as defined by the Board and all applicable statutory, regulatory and stock exchange listings standards. The Company's current practices are reviewed and updated regularly to ensure that the latest developments in corporate governance are followed and observed.

BOARD COMPOSITION

Corporate governance guidelines adopted by the Canadian Securities Administrators ("CSA") recommend that a majority of the directors of a corporation be independent directors. Under the CSA corporate governance guidelines, an "independent director" is a director who has no direct or indirect material relationship with the Company, including as a partner, shareholder or officer of an organization that has a relationship with the Company. A "material relationship" is one that would, or in the view of the Board could be reasonably expected to, interfere with the exercise of a director's independent judgment. The Board believes that as at December 31, 2009 and as at the date of this report four of its eight directors are "independent directors" under the CSA corporate governance guidelines.

As at the date of this report, the Board has determined that it consists of four independent directors and four non-independent directors, as follows:

Independent directors	Non-independent directors
Mr. Pierre Lebel *(Lead Director)*	Mr. Alexander Molyneux *(President and Chief Executive Officer)*(1)
Mr. André Deepwell	Mr. Peter Meredith *(Chairman)*(2)
Mr. R. Stuart (Tookie) Angus	Mr. John Macken(2)
Mr. Robert Hanson	Mr. R. Edward Flood(3)

(1) *Mr. Molyneux is a non-independent director in his capacity as a senior officer of the Company.*
(2) *Messrs. Macken and Meredith, executive officers of Ivanhoe, are considered to be non-independent directors as a result of the material relationship between the Company and Ivanhoe, and in the case of Mr. Meredith, as a former member of management of the Company.*
(3) *Until February 15, 2010, Mr. Flood was considered to be a non-independent director as a former executive officer of Ivanhoe, as a result of the material relationship between the Company and Ivanhoe. Until June 25, 2010, Mr. Flood will be considered non-independent as the former interim President and Chief Executive Officer of the Company.*

As at the date of this report, Ivanhoe held approximately 65% of the Company's issued and outstanding common shares. The Board has determined that the Company currently has four of eight directors in Mr. Lebel, Mr. Hanson, Mr. Deepwell and Mr. Angus who are independent of Ivanhoe. The Board believes that it includes half of its directors who do not have an interest in or relationships with either the Company or its principal shareholder and which fairly reflects the investment in the Company by shareholders other than the principal shareholder.

The directors are satisfied with the size and composition of the Board and believe that the current board composition results in a balanced representation on the Board among management and non-management directors, and the Company's major shareholder. While the Board functions effectively given the Company's stage of development and the size and complexity of its business, the Board, through its Nominating and Corporate Governance Committee, will continue to seek qualified candidates to augment its experience and expertise and to enhance the Company's ability to effectively develop its business interests.

Mr. Meredith currently serves as Chairman of the Board and from June 2007 to October 2009 was the Chief Executive Officer of the Company. Mr. Molyneux was appointed as Chief Executive Officer of the Company on October 11, 2009. The Board is of the view that appropriate structures and procedures are in place to allow the Board to function independently of management while continuing to provide the Company with the benefit of having a Chairman of the Board with extensive experience and knowledge of the Company's business.

The Board has created the position of Lead Director, with specific responsibility for maintaining the independence of the Board and ensuring that the Board carries out its responsibilities. Mr. Lebel has served as the Company's Lead Director since 2007. Mr. Lebel does not serve in a similar capacity with any other company.

The Company has received from each of the independent non-executive directors, the respective confirmation of independence pursuant to listing rules in all applicable jurisdictions. The Company considers all the independent non-executive directors as independent.

To the best knowledge of the Company none of the directors of the Company are related. Relationships include financial, business or family relationships. Each director is free to exercise their independent judgment.

MANDATE OF THE BOARD

Under the British Columbia Business Corporations Act ("BCBCA"), the directors of the Company are required to manage the Company's business and affairs, and in doing so to act honestly and in good faith with a view to further the best interests of the Company. In addition, each director must exercise the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances. The Board is responsible for supervising the conduct of the Company's affairs and the management of its business. The Board's mandate includes setting long term goals and objectives for the Company, formulating the plans and strategies necessary to achieve those objectives and supervising senior management in their implementation. Although the Board delegates the responsibility for managing the day-to-day affairs of the Company to senior management personnel, the Board retains a supervisory role in respect of, and ultimate responsibility for, all matters relating to the Company and its business.

The Board's mandate requires that the Board be satisfied that the Company's senior management will manage the affairs of the Company in the best interest of the shareholders, in accordance with the Company's principles, and that the arrangements made for the management of the Company's business and affairs are consistent with their duties described above. The Board is responsible for protecting shareholder interests and ensuring that the incentives of the shareholders and of management are aligned. The obligation of the Board must be performed continuously, and not merely from time to time, and in times of crisis or emergency the Board may have to assume a more direct role in managing the affairs of the Company.

In discharging this responsibility, the Board's mandate provides that the Board oversees and monitors significant corporate plans and strategic initiatives. The Board's strategic planning process includes annual budget reviews and approvals, and discussions with management relating to strategic and budgetary issues.

As part of its ongoing review of business operations, the Board periodically reviews the principal risks inherent in the Company's business, including financial risks, through periodic reports from management of such risks, and assesses the systems established to manage those risks. Directly and through the Audit Committee, the Board also assesses the integrity of internal control over financial reporting and management information systems.

In addition to those matters that must, by law, be approved by the Board, the Board is required under its mandate to approve annual operating and capital budgets, any material dispositions, acquisitions and investments outside of the ordinary course of business or not provided for in the approved budgets, long-term strategy, organizational development plans and the appointment of senior executive officers. Management is authorized to act, without Board approval, on all ordinary course matters relating to the Company's business.

The mandate provides that the Board also expects management to provide the directors, on a timely basis, with information concerning the business and affairs of the Company, including financial and operating information and information concerning industry developments as they occur, all with a view to enabling the Board to discharge its stewardship obligations effectively. The Board expects management to efficiently implement its strategic plans for the Company, to keep the Board fully apprised of its progress in doing so and to be fully accountable to the Board in respect to all matters for which it has been assigned responsibility.

The Board has instructed management to maintain procedures to monitor and promptly address shareholder concerns and has directed and will continue to direct management to apprise the Board of any major concerns expressed by shareholders.

Each Committee of the Board is empowered to engage external advisors as it sees fit. Any individual director is entitled to engage an outside advisor at the expense of the Company provided such director has obtained the approval of the Nominating and Corporate Governance Committee to do so. In order to ensure that the principal business risks borne by the Company are identified and appropriately managed, the Board receives periodic reports from management of the Company's assessment and management of such risks. In conjunction with its review of operations, the Board considers risk issues when appropriate and approves corporate policies addressing the management of the risk of the Company's business.

The Board takes ultimate responsibility for the appointment and monitoring of the Company's senior management. The Board approves the appointment of senior management and reviews their performance on an ongoing basis.

The Company has a disclosure policy addressing, among other things, how the Company interacts with analysts and the public, and contains measures for the Company to avoid selective disclosure. The Company has a Disclosure Committee responsible for overseeing the Company's disclosure practices. This committee consists of the President and Chief Executive Officer, Chief Financial Officer, Vice President and Corporate Secretary, Corporate Communications and Investor Relations, the Vice President – Project Evaluation and Development and the Resource Manager – Project Evaluation and Development, and receives advice from the Company's outside legal counsel. The Disclosure Committee assesses materiality and determines when developments justify public disclosure. The committee reviews the disclosure policy annually and as otherwise needed to ensure compliance with regulatory requirements as well as review all documents which are reviewed by the Board and Audit Committee. The Board reviews and approves the Company's material disclosure documents, including its annual report, annual information form and management proxy circular. The Company's annual and quarterly financial statements, Management's Discussion and Analysis and other financial disclosure is reviewed by the Audit Committee and recommended to the Board prior to its release.

COMMITTEES OF THE BOARD

Audit Committee

The Board has established an Audit Committee, which operates under a charter approved by the Board. It is the Board's responsibility to ensure that the Company has an effective internal control framework. This includes internal controls to deal with both the effectiveness and efficiency of significant business processes, the safeguarding of assets, the maintenance of proper accounting records, and the reliability of financial information as well as non-financial considerations such as the benchmarking of operational key performance indicators. The Company's Audit Committee consists of Mr. Deepwell, Mr. Lebel and Mr. Angus. Mr. Deepwell is the chairman of the Audit Committee.

The primary objective of the Audit Committee of the Company is to act as a liaison between the Board and the Company's independent auditors (the "Auditors") and to assist the Board in fulfilling its oversight responsibilities with respect to (a) the financial statements and other financial information provided by the Company to its shareholders, the public and others, (b) the Company's compliance with legal and regulatory requirements, (c) the qualification, independence and performance of the Auditors and (d) the Company's risk management and internal financial and accounting controls, and management information systems.

Although the committee has the powers and responsibilities set forth in its charter, the role of the committee is oversight. The members of the committee are not full-time employees of the Company and may or may not be accountants or auditors by profession or experts in the fields of accounting or auditing and, in any event, do not serve in such capacity. Consequently, it is not the duty of the committee to conduct audits or to determine that the Company's financial statements and disclosures are complete and accurate and are in accordance with generally accepted accounting principles and applicable rules and regulations. These are the responsibilities of management and the Auditors.

All services to be performed by the Company's independent auditor must be approved in advance by the Audit Committee or a designated member of the Audit Committee ("Designated Member"). The Designated Member is a member of the Audit Committee who has been given the authority to grant pre-approvals of permitted audit and non-audit services. Pre-approvals by the Designated Member are ratified by the Audit Committee at the next meeting thereof.

The Audit Committee has considered whether the provision of services other than audit services is compatible with maintaining the auditors' independence and has adopted a policy governing the provision of these services. This policy requires the pre-approval by the Audit Committee or the Designated Member of all audit and non-audit services provided by the external auditor, other than any de minimis non-audit services allowed by applicable law or regulation. The decisions of the Designated Member to pre-approve permitted services need to be reported to the Audit Committee at its regularly scheduled meetings. Pre-approval from the Audit Committee or Designated Member can be sought for planned engagements based on budgeted or committed fees. No further approval is required to pay pre-approved fees. Additional pre-approval is required for any increase in scope or in final fees. Pursuant to these procedures, 100% of each of the services provided by the Company's external auditor relating to the fees reported as audit, audit-related, tax and other fees were pre-approved by the Audit Committee or the Designated Member.

The committee held four meetings during the Financial Year. In performing its duties in accordance with the Audit Committee Charter, the Audit Committee has:

- overseen the relationship with the Company's auditors;
- reviewed the interim and annual financial statements;
- reviewed and assessed the effectiveness of systems of risk management and internal controls; and
- reported to the Board on the proceedings and deliberations of the Committee.

Nominating and Corporate Governance Committee

The Board has established a Nominating and Corporate Governance Committee, which operates under a charter approved by the Board. The primary objective of the Nominating and Corporate Governance Committee is to assist the Board in fulfilling its oversight responsibilities by (a) identifying individuals qualified to become Board and committee of the Board members and recommending that the Board select director nominees for appointment or election to the Board; and (b) developing and recommending to the Board corporate governance guidelines for the Company and making recommendations to the Board with respect to corporate governance practices. The Nominating and Corporate Governance Committee monitors the disclosure of conflicts of interest to the Board and ensures that no director will vote or participate in a discussion on a matter in respect of which such director has a material interest. Committee Chairs perform the same function with respect to meetings of each Board committee. The members of the Nominating and Corporate Governance Committee are Mr. Deepwell, Mr. Lebel, Mr. Hanson and Mr. Angus. Mr. Hanson is the chairman of the Nominating and Corporate Governance Committee.

Compensation and Benefits Committee

The Board has established a Compensation and Benefits Committee, which operates under a charter approved by the Board. The primary objective of the Compensation and Benefits Committee is to discharge the Board's responsibilities relating to compensation and benefits for the directors and executive officers of the Company. This role includes reviewing and approving executive compensation including long-term incentive components and making applicable recommendations to the Board, administering the Employee Incentive Plan ("EIP"), determining the recipients of, and the nature and size of share compensation awards and bonuses granted from time to time, and reviewing reports as may be required under applicable laws and regulations. The members of the Compensation and Benefits Committee are Mr. Angus, Mr. Deepwell, Mr. Hanson and Mr. Lebel. Mr. Angus is the chairman of the Compensation and Benefits Committee.

Ad Hoc/Special Committees

In appropriate circumstances, the Board may establish a special committee to review a matter in which several directors or management may have a conflict of interest.

MEETINGS OF THE BOARD AND COMMITTEES OF THE BOARD

The Board holds regular quarterly meetings. Between quarterly meetings, the Board meets as required, generally by means of telephone conferencing facilities. As part of the quarterly meetings, the non-management directors also have the opportunity to meet separate from management. If required, between regularly scheduled Board meetings, a meeting of non-management Directors, chaired by the Lead Director, is held by teleconference to update the Directors on corporate developments since the last Board meeting. Management also communicates informally with members of the Board on a regular basis, and solicits the advice of the Board members on matters falling within their special knowledge or experience.

During the Financial Year, eight meetings of the Board of Directors, four meetings of the Audit Committee, four meetings of the Nominating and Corporate Governance Committee, four meetings of the Compensation and Benefits Committee and no meetings of the Environment, Health and Safety Committee were held. Attendance by directors at the Board and Committee meetings is shown below:

Attendance record for the Board and Board Committee meetings during the Financial Year	Board meetings	Audit committee meetings	Nominating and corporate governance committee meetings	Compensation and benefits committee meetings	Environmental, health and safety committee meetings
	(Number of Attendances/Number of Meetings)				
Executive Directors					
Mr. Alexander Molyneux[(i)]	3/3	N/A	N/A	N/A	0/0
Non-Executive Directors					
Mr. Peter Meredith *(Chairman)*	8/8	N/A	N/A	N/A	N/A
Mr. John Macken	8/8	N/A	N/A	N/A	0/0
Mr. R. Edward Flood	7/8	N/A	N/A	N/A	N/A
Independent Non-Executive Directors					
Mr. Pierre Lebel *(Lead Director)*	8/8	4/4	4/4	4/4	N/A
Mr. André Deepwell	7/8	4/4	4/4	4/4	N/A
Mr. R. Stuart (Tookie) Angus	8/8	4/4	4/4	4/4	N/A
Mr. Robert Hanson	7/8	N/A	4/4	4/4	0/0

(i) *Mr. Molyneux was appointed as a Director of the Company on October 11, 2009*

CODE OF BUSINESS CONDUCT AND ETHICS

The Company has adopted a Code of Business Conduct and Ethics and a Statement of Values and Responsibilities applicable to all employees, consultants, officers and directors regardless of their position in the organization, at all times and everywhere the Company does business. The Code of Business Conduct and Ethics provides that the Company's employees, consultants, officers and directors will uphold its commitment to a culture of honesty, integrity and accountability and the Company requires the highest standards of professional and ethical conduct from its employees, consultants, officers and directors.

Company supervisors and employees are required to confirm, on an annual basis, that they have reviewed the Company's Code of Business Conduct and Ethics.

The Audit Committee monitors compliance with the Code of Business Conduct and Ethics. The Nominating and Corporate Governance Committee monitors the disclosure of conflicts of interest by directors with a view to ensuring that no director votes or participates in any board deliberations on a matter in respect of which such director has a material interest.

APPOINTMENT AND RE-ELECTION OF DIRECTORS

The Board determines, in light of the opportunities and risks facing the Company, what competencies, skills and personal qualities it should seek in new board members in order to add value to the Company. Based on this framework, the Nominating and Corporate Governance Committee developed a skills matrix outlining the Company's desired complement of directors' competencies, skills and characteristics. The specific make-up of the matrix includes such items and experiences as international experience, leading growth-orientated companies, mining exploration, diversity, financial literacy, legal knowledge, corporate governance, etc. The committee annually assesses the current competencies and characteristics represented on the Board and utilizes the matrix to determine the Board's strengths and identify any gaps that need to be filled. This analysis assists the committee in discharging its responsibility for approaching and proposing to the full Board new nominees to the Board, and for assessing directors on an ongoing basis.

Unless a director dies, resigns or is removed from office in accordance with the BCBCA, the term of office of each of the incumbent directors ends at the conclusion of the next annual meeting of the shareholders following his or her most recent election or appointment.

At every annual general meeting the shareholders entitled to vote at the annual general meeting for the election of directors are entitled to elect a board consisting of the number of directors for the time being set under the articles of continuation for the Company and all the directors cease to hold office immediately before such election but are eligible for re-election. If the Company fails to hold an annual general meeting on or before the date by which the annual general meeting is required to be held under the BCBCA or the shareholders fail, at the annual general meeting, to elect or appoint any directors then each director then in office continues to hold office until the earlier of:

- the date on which his or her successor is elected or appointed; and
- the date on which he or she otherwise ceases to hold office under the BCBCA or the articles of continuation.

SECURITIES TRANSACTIONS BY DIRECTORS

The Company has adopted policies in its Corporate Disclosure, Confidentiality and Securities policy that has terms that are no less exacting than those set out in Appendix 10 of the rules governing the listing of securities on the Hong Kong Stock Exchange.

Furthermore, if a director (a) enters into a transaction involving a security of the Company or, for any other reason, the direct or indirect beneficial ownership of, or control or direction over, securities of the Company changes from that shown or required to be shown in the latest insider report filed by the director, or (b) the director enters into a transaction involving a related financial instrument, the director must, within the prescribed period, file an insider report in the required form on the SEDI website at www.sedi.ca.

A "related financial instrument" is defined as: (a) an instrument, agreement, security or exchange contract the value, market price or payment obligations of which are derived from, referenced to or based on the value, market price or payment obligations of a security, or (b) any other instrument, agreement or understanding that affects, directly or indirectly, a person's economic interest in respect of a security or an exchange contract.

REMUNERATION OF DIRECTORS

The Compensation and Benefits Committee periodically reviews and makes recommendations to the Board regarding the adequacy and form of the compensation for non-management directors to ensure that such compensation realistically reflects the responsibilities and risks involved in being an effective director, without compromising a director's independence. Directors who are executives of the Company receive no additional remuneration for their services as directors.

All non-management directors receive Cdn$25,000 per annum for acting as such. Mr. Lebel receives an additional Cdn$60,000 per annum for acting as the Lead Director of the board. The chair of the Audit Committee receives an additional Cdn$40,000 per annum, for acting in such capacity. The respective chairs of the Compensation and Benefits Committee and the Corporate Governance Committee each receive an additional payment of Cdn$25,000 per annum for acting as such. Additionally, non-management directors receive Cdn$1,500 per in-person Board or Committee meeting attended and Cdn$600 per Board or Committee conference call in which they participate.

In addition to their cash compensation, non-management directors also receive a grant of 35,000 stock options per annum, such options having a five-year term and fully vesting on the first anniversary of the date of the grant.

Details regarding the remuneration of directors of the Company are set out in Note A2 of the Financial Statements.

INTERNAL CONTROLS

The Board is responsible for overseeing the internal controls of the Company. Internal controls are used by the Board to: facilitate the effectiveness and efficiency of operations, safeguard the investment of shareholders and assets of the Company and to ensure compliance with relevant statutory and regulatory requirements. The Company's internal control policies are designed to provide reasonable, but not absolute, assurance against material misstatements and help the Board identify and mitigate, but not eliminate, risk exposure.

The Board conducts annual reviews of the internal controls of the Company to ensure that internal control policies and procedures are adequate. The Audit Committee reviewed the effectiveness of the Company's internal control policies as at December 31, 2009, and is of the view that the internal control system in place is effective in safeguarding the investment of shareholders and assets of the Company.

AUDITORS

Deloitte & Touche LLP is the auditor of SouthGobi Energy Resources Ltd. and is independent within the meaning of the Rules of Professional Conduct of the Institute of Chartered Accountants of British Columbia. The financial reporting responsibilities and audit report of the independent auditors are set out on page 67.

Deloitte & Touche LLP will be nominated at the upcoming annual general meeting for reappointment as auditors of the Company at remuneration to be fixed by the Board. Deloitte & Touche LLP have served as the Company's auditors since August 14, 2003.

Fees paid/payable to the external auditors, Deloitte and Touche LLP, in respect of audit and non-audit services provided during the year ended December 31, 2009 were as follows:

Nature of services rendered	Fee paid/payable (US$ 000's)
Audit fees[(a)]	215
Non-audit fees[(b)]	890
Total	1,105

(a) *Fees for audit services billed consisted of:*
- *audit of the Company's annual financial statements*
- *reviews of the Company's interim financial statements*
- *comfort letters, consents and other services related to the Canadian securities regulatory and authorities' matters*

(b) *Non-audit fees include fees for:*
- *fees for tax services consisting of income tax compliance and tax planning and advice relating to transactions and proposed transactions of the Company and its subsidiaries*
- *fees incurred in connection with work conducted by Deloitte & Touche LLP for the Company on its application for listing on the Hong Kong Stock Exchange.*

RESPONSIBILITIES IN RESPECT OF THE FINANCIAL STATEMENTS

The directors acknowledge their responsibility in overseeing the preparation of financial statements that give a true and fair view of the financial affairs of the Company. With the assistance of the management of the Company, the directors ensure that the financial statements of the Company are being prepared and published in a timely manner and in accordance with the applicable accounting standards and statutory requirements.


HT-07
TEREX

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

DECEMBER 31, 2009
(Unaudited)
(expressed in U.S. Dollars)

OVERVIEW

SouthGobi Energy Resources Ltd., (which, together with its subsidiaries, is collectively referred to as the "Company" or "SouthGobi") is an integrated exploration, development and coal mining company. Since acquiring significant coal assets in Mongolia in a series of transactions (the "coal transaction") with Ivanhoe Mines Ltd. ("Ivanhoe"), the Company's strategic focus has been in developing and operating coal mining projects.

The Company's common shares trade on the Toronto Stock Exchange ("TSX") under the symbol SGQ. Upon completion of the International Offering and the Canadian Offering and the secondary listing of the common shares on the Hong Kong Stock Exchange on January 29, 2010, the Company's shares also trade on the Hong Kong Stock Exchange under stock code symbol 1878.

Prior to the coal transaction, the Company was a mineral exploration company with a focus on precious and base metal exploration and development in Mongolia, and elsewhere. The coal transaction was completed in May 2007 and with the sale of its Metals Division to Ivanhoe as of December 30, 2008, the Company's principal focus no longer includes precious or base metals.

The Company owns the following significant coal projects in Mongolia: the Ovoot Tolgoi open pit producing coal mine ("Ovoot Tolgoi Mine"), and two development projects, the Soumber Deposit, and the Ovoot Tolgoi Underground Deposit. The Ovoot Tolgoi Complex comprises the Ovoot Tolgoi Mine together with the Ovoot Tolgoi Underground Deposit.

The Ovoot Tolgoi Mine, strategically located approximately 40 kilometers ("km") from the China-Mongolia border, is the Company's flagship producing asset. The Company commenced mining at Ovoot Tolgoi's Sunset Pit in April 2008 and commenced coal sales in September 2008. The products from the Ovoot Tolgoi Mine include coking, premium and thermal coals, which are being sold to customers in China. Since the commencement of production in late 2008 until December 31, 2009, the Company has sold approximately 1.4 million tonnes of coal from the Ovoot Tolgoi Mine. The Ovoot Tolgoi Mine is covered by a single 9,308 hectare ("ha") mining license and a corresponding permit to mine.

The Soumber Deposit is located approximately 20 km to the east of the Ovoot Tolgoi Mine, which could allow the operations to share existing infrastructure in the event a mine is developed there. Preliminary exploration results show potential for thick seams of coking coal, and a resource has been established confirming the deposit. The Company is planning to do more exploration work on the deposit to fully investigate the feasibility of this project and to prepare for licensing.

The Company has conducted substantial exploration activities at the Ovoot Tolgoi Underground Deposit and has delineated mineral resources at this project. The Ovoot Tolgoi Underground Deposit is covered by the existing Ovoot Tolgoi Mining License.

In addition, the Company owns the Tsagaan Tolgoi Deposit in Mongolia, which has a mining licence, and prior to December 23, 2009, held an 85% interest in the Mamahak Deposit in Indonesia.

Corporate Developments

Ovoot Tolgoi Complex

Coal shipments from the Ovoot Tolgoi Mine commenced in late September 2008 and continued throughout the fourth quarter of 2008. In January and February 2009, the Company experienced difficulty expediting the movement of its coal shipments through the Mongolia-China border crossing check point at Ceke due to erratic and unpredictable opening hours and sporadic closures. As a result, the Company initiated a production curtailment program in January 2009, decreasing production to preserve cash and to manage stockpiles.

The Company continued coordinating efforts with the Mongolian Government and various agencies to improve border crossing access for coal shipments. On February 24, 2009, in a further effort to minimize costs, the Company shut down production at the Ovoot Tolgoi Mine operation. All production equipment was demobilized, except for coal loading of customer trucks from the coal stockpile.

As discussions continued with the Mongolian Government, border access improved towards the end of the first quarter of 2009. In March 2009, the border crossing check point started operating on a more formal basis, with a schedule of eight hours per day, seven days per week. This resulted in increased shipments for the month of March, with sales of over 115,000 tonnes of coal. In April and May 2009, shipments totaled approximately 152,000 tonnes. In June, the border crossing check point started operating 11 hours per day, six days per week. Total shipments in June were approximately 232,000 tonnes, a new record for the Company. In July 2009, Mongolian and Chinese officials met at the Mongolian-Chinese border and allocated designated gates for coal exports to create an expedited coal border crossing corridor.

With increasing sales and a reduction in its coal inventory, the Company resumed full mining operations effective July 1, 2009, on a 24 hours per day, seven days per week basis. For the third quarter of 2009, total shipments were 457,000 tonnes, and for the fourth quarter of 2009, total shipments were 359,000 tonnes. Total shipments since the mine commenced production have now exceeded 1.4 million tonnes.

Construction of the permanent on-site employee housing facility and permanent maintenance workshop facility were completed during the third quarter of 2009. The Company moved into the workshop/warehouse complex in August 2009 and into the permanent housing facility in September 2009. The mine airstrip surfacing has been completed and final permitting was received for the concrete airstrip.

On October 12, 2009, the Company announced that it completed a prefeasibility study for the Ovoot Tolgoi Mine resulting in the identification of Proven and Probable Mineral Reserves. The independent estimate prepared by Norwest Corporation ("Norwest") calculated 114.1 million tonnes of proven and probable surface coal reserves at July 1, 2009. 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, Resources and Reserves Ovoot Tolgoi: A Production Property. Omnogovi Aimag, Mongolia" dated October 21, 2009, and available at www.sedar.com.

Surface Mineable Reserves as of July 1, 2009

Reserve Area	ASTM Coal Rank	Proven (million tonnes)	Probable (million tonnes)	Total (million tonnes)
Ovoot Tolgoi Mine	hvB to hvA*	105.0	9.1	114.1

** hvB to hvA – high-volatile bituminous coal B to A rank based on ASTM D388 standards*

Total Surface and Underground Coal Resource Summary as of June 1, 2009

The Company also announced that it had received an updated independent NI 43-101 compliant resource estimate for the Ovoot Tolgoi Complex, prepared by Norwest. 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, Resources and Reserves Ovoot Tolgoi: A Production Property. Omnogovi Aimag, Mongolia" dated October 21, 2009, and available at www.sedar.com.

The Ovoot Tolgoi Complex surface and underground resources contain measured plus indicated coal resources of 249.8 million tonnes, with an additional inferred coal resource of 33.5 million tonnes as at June 1, 2009.

				In-Place Resources (million tonnes)		
Resource Area	Type	Resource Limits Depth (metres)	ASTM Group	Measured	Indicated	Inferred
Sunrise Field	Surface	Surface to 250m	hvB to hvA*	53.8	15.7	4.9
Sunset Field	Surface	Surface to 250m	hvB to hvA	82.1	19.4	8.1
Sub-Total				**135.9**	**35.1**	**13.0**
Sunrise Field	Underground	250m to 600m	hvB to hvA	11.2	5.2	11.2
Sunset Field	Underground	250m to 600m	hvB to hvA	34.6	27.8	9.3
Sub-Total				**45.8**	**33.0**	**20.5**
Total				**181.7**	**68.1**	**33.5**

** hvB to hvA – high-volatile bituminous coal B to A rank based on ASTM D388 standards*

Ovoot Tolgoi Complex resources are found in two different resource areas, referred to as the Sunrise and Sunset Fields (formerly the South-East and West Fields, respectively). The Mineral Resources are inclusive of the Mineral Reserves.

Soumber Deposit

On October 12, 2009, the Company reported that it had received an initial independent NI 43-101 compliant resource estimate for the Soumber coal project, prepared by Norwest. Details of the assumptions and parameters used to calculate these coal resources and coal quality estimates are set out in the Technical Report entitled, "Soumber Property Umnugobi Aimag, Mongolia" dated October 21, 2009, and available at www.sedar.com.

The Soumber coal project and resource area is estimated to contain initial measured plus indicated coal resources of 21.4 million tonnes, with an additional inferred coal resource of 55.5 million tonnes as at August 11, 2009.

Resource Area	ASTM Coal Rank	Measured (million tonnes)	Indicated (million tonnes)	Inferred (million tonnes)
Soumber	Medium volatile bituminous*	13.1	8.3	55.5
Total		21.4		55.5

** medium-volatile bituminous coal based on ASTM D388 standards*

Mamahak Deposit

In April 2008, the Company entered into a Joint Venture Earn-In Agreement with an Indonesian company to explore and develop a coal project in East Kalimantan, Indonesia, known as the Mamahak Coal project ("Mamahak").

As the Company progressed with efforts to prepare for the mining and shipment of the targeted 30,000 tonne trial cargo from Mamahak, the Company became aware of the requirement for additional capital expenditure beyond what was originally budgeted to develop the project. After the initial review of the project expenditures and related budgets, the Company suspended further development work. On December 15, 2009, the Company announced that it had entered into an agreement to divest the 85% interest in the Mamahak Deposit in Indonesia to Kangaroo Resources Limited ("KRL") for consideration comprising $1.0 million in cash and 50 million shares of KRL. The sale of the interest in the Mamahak Deposit was completed on December 23, 2009.

Corporate Activity

On December 31, 2008, the Company announced the sale of its Metals Division to Ivanhoe for $3 million and other non-cash consideration, with an effective date of December 30, 2008, and a closing date of February 2, 2009. As part of the transaction, the Company obtained a $30 million working capital credit facility from Ivanhoe.

On February 10, 2009, the Company announced the appointment of Alexander Molyneux as its new President, effective April 27, 2009. Effective October 12, 2009, Mr. Molyneux assumed the dual role of President and Chief Executive Officer. Based in Hong Kong, he was most recently Managing Director, Head of Metals & Mining Investment Banking, Asia Pacific, Citigroup.

On March 20, 2009, the Company announced two new appointments to its Management and Resource Development team: Jess Harding and Stephen Torr.

Jess Harding has been appointed the Company's Vice-President, Evaluations and Project Development. Mr. Harding has more than 15 years' experience in the mining industry and assumes the same role that he presently holds at Ivanhoe. Mr. Harding has a Bachelor of Chemical Engineering from the University of Leeds, UK.

Stephen Torr (P.Geo.), has been appointed the Company's Resource Manager. Mr. Torr has 19 years of experience in the mining industry and currently is the Resource Manager for Ivanhoe. Mr. Torr has a B.Sc. (Hons) Degree in Geology from the University of Southampton and a M.Sc. in Applied Geoscience from the University of Leicester. Mr. Torr has previous experience in estimation of open pit and underground coal resources and will be assuming the role of Qualified Person to oversee future independent resource estimates for SouthGobi.

In June 2009, Jay Gow was appointed the Company's Vice-President, Coal Marketing. Mr. Gow has extensive experience in international and domestic resource marketing, which will be important as the Company develops its international customer base.

In July 2009, the Right Honourable Jean Chrétien, the 20th Prime Minister of Canada, was appointed as a senior international adviser to the Company as part of a broader engagement of Mr. Chrétien's services by Ivanhoe and certain other companies with which the Company shares access to corporate administrative facilities, employees and service providers. See "Related Party Transactions". Mr. Chrétien will advise the Company with respect to international business opportunities in the energy and mineral resource sectors.

In July 2009, the Company and Ivanhoe agreed to increase an existing working capital credit facility from $30 million to $60 million. The amended credit facility had an original maturity date of December 31, 2010, was unsecured and had an interest rate of LIBOR plus 750 basis points. The amended facility required repayment in the event that the Company acquired additional financing from a third party source and provided for an extension fee of $1.5 million payable in the event any portion of the facility was outstanding past March 31, 2010. This additional $30 million working capital facility allowed the Company to continue to fund its expansion plans and current operations in Mongolia and its operations in Indonesia. The outstanding line of credit facility plus interest was repaid and cancelled in November 2009.

On September 8, 2009, the Company announced the appointment of Gavin May as the Company's new Chief Operating Officer. Mr. May has more than 25 years of experience in the coal industry and is uniquely qualified to plan for the next stage of development and build out of the Company's significant projects in Mongolia. He was formerly Chief Executive Officer and Managing Director of Gloucester Coal Ltd., a company listed on the Australian Stock Exchange.

On November 19, 2009, the Company announced financing had been secured from a wholly-owned subsidiary of China Investment Corporation ("CIC"), which will provide $500 million in the form of a secured, convertible debenture bearing interest at 8.0% (Please see the Liquidity, Financing and Working Capital Resources section for more details).

The Company's common shares began trading on the TSX on December 3, 2009. SouthGobi was previously listed on the TSX Venture Exchange.

On December 23, 2009, the Company announced the closing of the sale of its Mamahak coal project to KRL.

On January 29, 2010, the Company closed a global equity offering of 27 million common shares at a price of Cdn$17.00 per common share, for gross proceeds of Cdn$459 million. The Company commenced trading on the Main Board of the Hong Kong Stock Exchange on the same day and became the first Canadian mining company to have dual listings on the Hong Kong Stock Exchange and the TSX.

Effective February 8, 2010, the Company appointed Tony Pearson as the new Vice-President, Corporate Development. Mr. Pearson has an extensive background in infrastructure financing in the mining industry and has held senior positions with the Australian Securities & Investments Commission, Citigroup's Metals and Mining Investment banking team, and Westpac Banking Corporation.

On February 10, 2010, the Mongolian National Chamber of Commerce and Industry selected SouthGobi Sands LLC, a wholly-owned subsidiary of SouthGobi, as the "Local Job Creator of the Year" for 2009. The purpose of this commemorative prize is to encourage and support the hiring of local residents in remote areas of Mongolia.

On February 26, 2010, Citigroup Global Markets Canada Inc. and Macquarie Capital Markets Canada, representatives of the Canadian underwriters of the Company's recently closed global equity offering, partially exercised their over-allotment option and purchased an additional 228,100 common shares of the Company at a price of Cdn$17.00 per share for gross proceeds of Cdn$3,877,700.

As of March 15, 2010, Ivanhoe directly and indirectly, currently owns 105,557,155 common shares representing approximately 65% of the issued and outstanding common shares of SouthGobi.

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 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.

INTERNATIONAL FINANCIAL REPORTING STANDARDS (IFRS)

Transition to IFRS from GAAP

In February 2008, the Canadian Accounting Standards Board confirmed that Canadian publicly accountable enterprises will be required to adopt International Financial Reporting Standards ("IFRS") for financial periods beginning on and after January 1, 2011. In the Canadian Securities Administrators ("CSA") Staff Notice 52-321 – Early Adoption of International Financial Reporting Standards, use of US GAAP and Reference to IFRS-IASB, CSA has indicated that it would be prepared to provide exemptive relief to permit a Canadian reporting issuer to prepare its financial statements in accordance with IFRS for financial periods beginning before January 1, 2011.

As previously disclosed, the Company completed its secondary listing on the Hong Kong Stock Exchange on January 29, 2010. As part of the application process for the secondary listing, the Company was required to provide financial statements under IFRS with three years of comparative data. In order to produce the required IFRS financial statements, the Company has produced IFRS financial statements with an IFRS transition date of January 1, 2005. As per Appendix A of IFRS 1, "An entity cannot have more than one set of IFRS financial statements. Therefore, it must have only one starting point for transition to IFRS". In March 2009, the Company was granted exemptive relief by Canadian securities regulatory authorities under Staff Notice 52-321 and has been permitted to adopt IFRS for Canadian reporting purposes for reporting periods beginning on or after January 1, 2009. The Company has adopted IFRS with an adoption date of January 1, 2009, and a transition date of January 1, 2005.

IFRS Conversion

The Company's IFRS conversion plan was comprehensive and addressed matters including changes in accounting policies, restatement of comparative periods, organizational and internal controls and any required changes to business processes. To facilitate this process and ensure the full impact of the conversion was understood and managed reasonably, the Company retained an external third party accounting firm and hired an IFRS conversion project manager. The accounting staff attended several training courses on the adoption and implementation of IFRS. Through in-depth training and the preparation of reconciliations of historical Canadian GAAP financial statements to IFRS, the Company believes that its accounting personnel have obtained a thorough understanding of IFRS. Further, the accounting personnel at the Company's Mongolian and Indonesian subsidiaries are already familiar with IFRS and have been working with IFRS due to either local adoption of IFRS or convergence of local standards to IFRS in those jurisdictions.

In conjunction with the adoption of IFRS, the Company has implemented a new accounting system, which will satisfy all the information needs of the Company under IFRS. The Company has also reviewed its current internal and disclosure control processes and believes they will not need significant modification as a result of the Company's conversion to IFRS.

Impact of IFRS

IFRS employs a conceptual framework that is similar to Canadian GAAP; however significant differences exist in certain matters of recognition, measurement and disclosure. While the adoption of IFRS will not change the actual cash flows of the Company, the adoption will result in changes to the reported financial position and results of operations of the Company. In order to allow the users of the financial statements to better understand these changes, the Company has provided the reconciliations between Canadian GAAP and IFRS for the total assets, total liabilities, shareholders' equity and net earnings in Note 3 to the annual Consolidated Financial Statements. The adoption of IFRS has had no impact on the net cash flows of the Company. The changes made to the statements of financial position and comprehensive income have resulted in reclassifications of various amounts on the statements of cash flows, however as there has been no change to the net cash flows, no reconciliations have been presented.

In preparing the reconciliations, the Company applied the principles and elections of IFRS 1, with a transition date of January 1, 2005, consistent with those assumed in the documentation for the secondary listing on the Hong Kong Stock Exchange. As the Company has been permitted to adopt IFRS effective January 1, 2009, it will apply the provisions of IFRS 1 as described under the section entitled "Initial Adoption – IFRS 1", with a January 1, 2005, transition date. The Company will also apply IFRS standards in effect at December 31, 2009, as required by IFRS 1.

Initial Adoption of International Accounting Standards

IFRS 1 ''First Time Adoption of International Accounting Standards'' sets forth guidance for the initial adoption of IFRS. Under IFRS 1 the standards are applied retrospectively at the transitional date of the statement of financial position with all adjustments to assets and liabilities as stated under GAAP taken to retained earnings unless certain exemptions are applied. The Company is not applying any exemptions on first-time adoption.

Comparative Information

The Company has restated all prior period figures in accordance with IFRS.

CRITICAL ACCOUNTING ESTIMATES

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 for the year ended December 31, 2009. Note 3 to the annual Consolidated Financial Statements for the year ended December 31, 2009, provides a review of the significant changes to the reported financial position and results of operations of the Company under Canadian GAAP and IFRS.

The following is an outline of the estimates that the Company considers as critical in the preparation of its consolidated financial statements.

Mineral properties

All direct costs related to the acquisition of mineral property interests are capitalized into intangible assets on a property by property basis. Exploration costs, net of incidental revenues, are charged to operations in the period incurred until such time as it has been determined that a property has economically recoverable reserves, in which case subsequent exploration costs and the costs incurred to develop a property are capitalized into property, plant and equipment ("PPE"). On the commencement of commercial production, depletion of each mining property will be provided on a unit-of-production basis using estimated resources as the depletion base.

The commencement of commercial production is deemed to occur on a determination made by management. Management's determination of when commercial production commences is based on several qualitative and quantitative factors including but not limited to the following:

- the elevation or bench where the coal to be mined has been reached
- the commissioning of major mine and plant equipment is completed
- operating results are being achieved in a consistent manner

However, the production phase does not commence with the removal of *de minimis* saleable mineral materials that occur in conjunction with the removal of overburden or waste material for the purpose of obtaining access to an ore body.

Decommissioning, restoration and similar liabilities (Asset retirement obligation or "ARO")

The Company recognizes provision for statutory, contractual, constructive or legal obligations, including those associated with the reclamation of mineral properties and mineral assets under PPE, when those obligations result from the acquisition, construction, development or normal operation of the assets. Initially, a provision for an asset retirement obligation is recognized as its present value in the period in which it is incurred. Upon initial recognition of the liability, the corresponding asset retirement obligation is added to the carrying amount of the related asset and the cost is amortized as an expense over the economic life of the asset using either the unit-of-production method or the straight-line method, as appropriate. Following the initial recognition of the asset retirement obligation, the carrying amount of the liability is increased for the passage of time and adjusted for changes to the current market-based discount rate, amount or timing of the underlying cash flows needed to settle the obligation.

Inventory valuation

Coal inventories are stated at lower of production cost and net realizable value. Production costs include direct and indirect labor, operating materials and supplies, transportation costs and an appropriate portion of fixed and variable overhead expenses, including depreciation and depletion. Net realizable value represents the estimated selling price for inventories less all estimated costs of completion and costs necessary to make the sale.

Materials and supplies inventory consists of consumable parts and supplies which are valued at lower of weighted average cost and net realizable value. Supplies used in the production of inventories are not written down below cost if the finished products in which they will be incorporated are expected to be sold at or above cost. Net realizable value is defined as the selling price of the finished product less any provisions for obsolescence and costs of completion.

Stripping costs

Stripping costs incurred during the development of a mine are capitalized into PPE. Stripping costs incurred during the commercial production phase are variable production costs that are included in the costs of inventory produced during the period that the stripping costs are incurred, unless the stripping activity can be shown to give rise to future benefits from the mineral property, in which case the stripping costs would be capitalized into PPE.

Future benefits arise when stripping activity increases the future output of the mine by providing access to a new ore body that the previously deferred stripping costs in an area did not give access to. When stripping activities give rise to a future economic benefit, the costs associated with these activities are capitalized into PPE. Capitalized stripping costs are depleted on a unit-of-production basis, using estimated resources as the depletion base.

Income taxes

Current income tax assets and liabilities for the current and prior periods are measured at the amount expected to be recovered from or paid to the taxation authorities. The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted at the end of each reporting period.

Deferred income tax is provided using the liability method on temporary differences, at the end of each reporting period, between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

Share-based payments

Share-based payment transactions

Employees (including directors and senior executives) of the Company receive a portion of their remuneration in the form of share-based payment transactions, whereby employees render services as consideration for equity instruments ("equity-settled transactions").

In situations where equity instruments are issued to non-employees and some or all of the goods or services received by the entity as consideration cannot be specifically identified, they are measured at fair value of the share-based payment. Otherwise, share-based payments are measured at the fair value of goods or services received.

Equity-settled transactions

The costs of equity-settled transactions with employees are measured by reference to the fair value at the date on which they are granted.

The costs of equity-settled transactions are recognized, together with a corresponding increase in equity, over the period in which the performance and/or service conditions are fulfilled, ending on the date on which the relevant employees become fully entitled to the award ("the vesting date"). The cumulative expense is recognized for equity-settled transactions at each reporting date until the vesting date reflects the Company's best estimate of the number of equity instruments that will ultimately vest. The profit or loss charge or credit for a period represents the movement in cumulative expense recognized as at the beginning and end of that period and the corresponding amount is represented in share option reserve. No expense is recognized for awards that do not ultimately vest.

Where the terms of an equity-settled award are modified, the minimum expense recognized is the expense as if the terms had not been modified. An additional expense is recognized for any modification which increases the total fair value of the share-based payment arrangement, or is otherwise beneficial to the employee as measured at the date of modification.

The dilutive effect of outstanding options is reflected as additional dilution in the computation of earnings per share.

Revenue recognition

Revenue represents the fair value of consideration received and receivable that is derived from the sales of coal. Sales revenues are recognized when the risks and rewards of ownership pass to the buyer, collection is reasonably assured and the price is reasonably determinable. The revenue from sales of coal in the ordinary course of business is recognized when coal is either loaded onto a truck or when it is unloaded at the final destination, depending on the terms of the contract.

Property, plant and equipment

PPE is stated at cost less accumulated depreciation and accumulated impairment losses. The cost of an item of PPE consists of the purchase price, any costs directly attributable to bringing the asset to the location and condition necessary for its intended use and an initial estimate of the costs of dismantling and removing the item and restoring the site on which it is located.

Depreciation is provided at rates calculated to write off the cost of PPE, less their estimated residual value, using the straight-line method or unit-of-production method.

CHANGE IN ACCOUNTING POLICIES

On January 1, 2009, the Company adopted IFRS. Note 3 to the annual Consolidated Financial Statements for the year ended December 31, 2009, provides a review of the significant changes to the reported financial position and results of operations of the Company under Canadian GAAP and IFRS. The provisions of new and revised standards and interpretations are applicable and effective for the Company's financial year beginning on or after January 1, 2009.

A summary of the new, future and revised standards and interpretations are outlined in Note 2.3 of the annual Consolidated Financial Statements.

MINERAL PROPERTIES

Qualified Persons

Disclosure of a scientific or technical nature in this MD&A with respect to the Company's Coal Division was prepared by, or under the supervision of Stephen Torr (P.Geo.) and Resource Manager. Mr. Torr is a "qualified person" for the purposes of National Instrument 43-101 of the Canadian Administrators ("NI 43-101").

Mr. Torr was appointed the Company's Resource Manager on March 20, 2009. Prior to March 20, 2009, Gene Wusaty, P.Eng., and Chief Operating Officer was the Company's "qualified person" for the purposes of the NI 43-101.

Coal Group Profile

Mongolia Exploration Licenses

The coal transaction was completed in May 2007, when the Company acquired Ivanhoe's Coal Division, including Ivanhoe's entire interest in the Ovoot Tolgoi Complex (formerly Nariin Sukhait), the Tsagaan Tolgoi Deposit and various coal exploration projects in Mongolia. To complete the transaction, 35 coal exploration licenses held by Ivanhoe, along with other assets and personnel, were transferred to the Company. The Company already owned a further 19 exploration licenses with coal potential, and with the additional 35 licenses, a total of 54 licenses covering an area of approximately 2.1 million hectares ("ha") were then available for coal exploration.

The Company regularly targets and prioritizes a number of licenses on the basis of potential, age, and cost.

As at January 29, 2010, the Company held 18 licenses, including the two mining licenses, which in total cover an area of approximately 784,000 ha.

The 18 licenses are located around the existing mining area in the western part of the South Gobi Province, but also further east, including a substantial holding around another known third-party owned Mongolian coal deposit called Tavan Tolgoi. Out of these 18 licenses, four may be affected by a new Mongolian law that prohibits minerals exploration and mining in certain areas.

Pursuant to the Mining Prohibition in Specified Areas Law, the Mongolian Government was instructed to define the boundaries of the areas in which exploration and mining would be prohibited by October 16, 2009. However, the Mongolian Government has not yet approved and published this information.

A draft list of licenses has been prepared that overlap with the prohibited areas described in the new law based on information submitted by water authority agencies, forest authority agencies and local authorities for submission to the Mongolian Government. The Mongolian Government must give its final approval before the final list can be published; licenses may be added or subtracted to the list at any time prior to approval and publication of the final list.

Four of the Company's exploration licenses may be included on the draft list of licenses published by the Mongolian Government, potentially affecting the status of those licenses under the Mining Prohibition in Specified Areas Law.

Activities currently being carried out on these properties 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 the existing operations or resources.

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

Properties in Mongolia

Ovoot Tolgoi Mine

The Ovoot Tolgoi Complex comprises the Ovoot Tolgoi Mine together with the Ovoot Tolgoi Underground Deposit.

The Ovoot Tolgoi Mine is located in the southwest corner of the Omnogovi Aimag (South Gobi Province) of Mongolia. The deposit is within the administrative unit of Gurvantes Soum, 320 km southwest of the provincial capital of Dalanzadgad and 950 km southwest of the nation's capital of Ulaanbaatar.

Ivanhoe first initiated coal exploration in the Ovoot Tolgoi area in October 2004 and extensive exploration programs were also carried out in 2005, 2006 and 2007. Mining operations at the Ovoot Tolgoi property are found in two distinct areas, referred to as the Sunset Pit to the west and the Sunrise Pit to the east.

In 2009, the Company engaged Norwest to complete a new technical report for the Ovoot Tolgoi area incorporating outstanding data obtained from drilling to the end of 2008, reflecting a redesign of the surface mine, updating the resource models and delineating reserves based on a pre-feasibility level of engineering.

On October 12, 2009, the Company announced an independent resource estimate prepared by Norwest under the requirements of NI 43-101. Norwest estimated that the Ovoot Tolgoi Mine contained approximately 114.1 million tonnes of reserves, 135.9 million tonnes of measured resources, 35.1 million tonnes of indicated resources and 13.0 million tonnes of inferred resources. The Mineral Resources are inclusive of Mineral Reserves.

The coal rank at the Ovoot Tolgoi Mine is high volatile B to A bituminous. 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.

Three coal products are presently being mined or are expected to be produced at the Ovoot Tolgoi Mine; a coking (or metallurgical) coal, a premium coal with applications for semi-soft/PCI coking coal or a high-quality thermal coal, and a thermal coal product for use in power generation.

All three coal types are currently sold directly from the mine without any beneficiation or washing. In-pit sampling and on-site laboratory analysis determines which product is currently being mined and the products are then separately stockpiled and blended to meet specific customer requirements. The Company is currently considering plans for a beneficiation facility.

After obtaining its Permit to Mine on March 31, 2008, the Company started operations at Ovoot Tolgoi in April 2008. Coal shipments began in September 2008. Coal sales to December 31, 2008, were approximately 113,000 tonnes.

Due to erratic and unpredictable Mongolia-China border access, coal shipments in January and February 2009 were lower than expected. Consequently, and in order to preserve cash and manage stockpiles, a production curtailment program was initiated in January 2009 decreasing production to a dayshift basis. This was followed by a full mine shutdown in late February 2009, except for coal loading of customer trucks from coal stockpiles. The mine resumed full mining operations effective July 1, 2009.

In 2009, coal shipments in the first quarter were approximately 127,000 tonnes; in the second quarter approximately 384,000 tonnes; the third quarter approximately 457,000 tonnes; and the fourth quarter approximately 359,000 tonnes. Total shipments since the mine commenced production have now exceeded 1.4 million tonnes.

In order to increase the amount of coal traffic across the border, in July 2009, Chinese and Mongolian authorities agreed to create a designated coal transportation corridor at the Shivee Khuren-Ceke border crossing. This facility is currently under construction and is expected to be operational in 2010. When completed, it will permit coal to be transported across the border through three corridors that are separate from other, non-coal, border traffic. The Company believes that these improvements in the border crossing capacity will allow the Company to continue to substantially increase the amount of coal shipped into China.

The Ovoot Tolgoi Mine's proximity to the Shivee Khuren-Ceke border crossing allows the Company's customers to transport coal by truck on an unpaved road from the mine site to China. The Company is currently studying the feasibility of building additional road infrastructure from the Ovoot Tolgoi Complex to the Mongolia-China border.

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 from Ceke to Linhe, an industrial city in eastern Inner Mongolia, is expected to be operational in 2010. This line is anticipated to have an initial transportation capacity of approximately 15 million tonnes per year, later increasing to 25 million tonnes per year. Using this route coal can be shipped to Baotou and further east to ports on China's Bohai Gulf.

Since December 2008, the Company has been engaged in various levels of discussions with railway contractors regarding the feasibility of developing a coal railway spur from the Ovoot Tolgoi Mine to the Mongolia-China border.

SouthGobi Sands LLC, a wholly owned Mongolia subsidiary of SouthGobi, employed 317 employees as at December 31, 2009. Of the 317 employees, 41, including expatriates, are employed in the Ulaanbaatar office, 4 in outlying smaller offices including the Ceke border point and 272 at the mine site. Of the total 316 employees based in Mongolia, 310 (98%) are Mongolian nationals and 103 (33%) are residents of the local Gurvantes Soum.

In April 2008, the Company purchased a second fleet of coal mining equipment for the open pit mine, with some equipment commissioned in the fourth quarter of 2009 and the remaining equipment scheduled to be commissioned in the first quarter of 2010. The new shovel and truck mining fleet consists of a Liebherr 996 hydraulic excavator ($34m^3$) and four Terex MT4400 (218-tonne capacity) trucks. The new fleet will supplement the existing mine fleet consisting of a Liebherr 994 hydraulic excavator (13.5 m^3) and seven Terex TR100 (91-tonne capacity) trucks.

Additional equipment will be required as production at the mine expands, including larger hydraulic shovels, larger end dump trucks and larger dozers and graders. The Company has entered into an agreement with a Mongolian supplier for a third fleet including an additional larger Liebherr 996 hydraulic excavator ($34m^3$), four Terex MT4400 (218-tonne capacity) trucks and various auxiliary equipment. The third fleet is expected to be delivered in mid-2010, with an additional fourth fleet of equipment likely to be ordered for 2011. The additional larger equipment will increase productivity. However, the Company will continue to employ the smaller initial fleet in areas of thinner seams and to supplement the larger equipment.

The airstrip surfacing project was completed at year end 2008 and was certified in early 2009. The on-site employee housing facility and maintenance workshop building complexes were completed during the third quarter of 2009. Both complexes are now occupied.

Ovoot Tolgoi Underground Deposit

The Ovoot Tolgoi Underground Deposit is contiguous to, and located directly below, the surface mine development. The entire extension of the coal at depth from 250 to 600 m that is designated for potential underground development is located inside the existing Ovoot Tolgoi mining license.

The 2008 exploration program concentrated on the underground located in the Sunset Pit. This drilling was conducted to obtain additional information respecting the structure and quality of the deep underground coal mineralization. The drilling conducted in 2006 and 2007 identified coking and semi-soft coal at depths of between 250 m and 600 m beneath the lower boundaries of the planned open pits at Sunrise and Sunset. The No. 5 coal seam continues to be open at depth and along strike.

On October 12, 2009, the Company announced an independent resource estimate prepared by Norwest under the requirements of NI 43-101. Norwest estimated that the Ovoot Tolgoi Underground Deposit contained approximately 45.8 million tonnes of measured resources, 33 million tonnes of indicated resources and 20.5 million tonnes of inferred resources.

Having identified underground resources at the Ovoot Tolgoi Underground Deposit, the Company is investigating the possibility of mining these resources using underground mining methods.

Soumber Deposit

The Soumber Deposit is located approximately 20 km east of the Ovoot Tolgoi Mine. It lies within the administrative unit of Gurvantes Soum in the Omnogovi Aimag (South Gobi Province), approximately 50 km northeast of the Shivee Khuren-Ceke border crossing.

Exploration and drilling programs at Soumber first started in 2005 in the western field. Sixty-two holes were drilled during 2005 and 2006 that confirmed the potential for a significant coal deposit in the area. Between 2007 and 2008, over 121 drill holes, totaling 24,512 m of drilling were completed. In 2009, the Company conducted geotechnical and hydrological programs in the Soumber central field. The exploration geology fieldwork included reconnaissance mapping, trenching, geologic descriptions of drilling returns, geotechnical data, field logs and database development.

Based on the drill hole data distribution, the Soumber coal field can be divided into three prospective areas: central, east and west. The majority of exploration activity has focused on the central Soumber field. The coal occurrence on the Soumber central field can be divided into seven separate seams, or benches of a seam separated by rock interburden. The seams themselves are composed of coal intercalated with numerous rock partings. The coal seams in the Soumber field may not be directly correlative to the Ovoot Tolgoi coal seams.

On October 12, 2009, the Company announced that it had received an initial independent resource estimate for the Soumber Deposit. The coal resources estimated at the Soumber central field are comprised of measured coal resources of 13.1 million tonnes, indicated coal resources of 8.3 million tonnes and inferred coal resources of 55.5 million tonnes. Laboratory data demonstrated that some of the coal benches exhibit potential coking coal characteristics. The coal rank ranges between high to medium volatile bituminous coal, having an average calorific value range of 5,172 to 6,728 kcal/kg. The Soumber Deposit has potential to increase coal resources to the east and to the west as well as at depth. The resource estimate incorporates exploration data up to August 11, 2009, down to a depth of 250 m below surface.

Due to the proximity to the Ovoot Tolgoi Mine, any future mining operation at the Soumber Deposit would likely be able to share common infrastructure with the Ovoot Tolgoi Mine. The Company has initiated mine planning and an application for a mining license, which will be submitted for development of this project. Environmental baseline studies have been completed and general environmental impact assessments have begun. The Company is also studying the feasibility of building a coal preparation plant for the Soumber coal to remove rock partings and produce a hard coking coal product.

Tsagaan Tolgoi Deposit

The Tsagaan Tolgoi coal field is located in south-central Mongolia. The property is located in the Omnogovi Aimag approximately 570 km south of Ulaanbaatar and 113 km southeast of the provincial capital of Dalanzadgad, and approximately 115 km west of Oyu Tolgoi.

A coal delineation program was first carried out in 2004, but no further work was conducted in 2005. Exploration programs were carried out during 2006 and 2007 to provide the basis for a resource estimate. In February 2008, Norwest estimated 23.4 million tonnes of measured resources, 13.0 million tonnes of indicated resources and 9.0 million tonnes of inferred resources. The coal is of volatile bituminous B to C in rank based on ASTM D388 standards and is suitable for use as a thermal coal. The resources appear to be amenable to surface extraction down to a planned depth of 150 m. 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 Mongolian Government issued a mining license for the Tsagaan Tolgoi coal field. The Technical and Economic Study has been completed, and is currently under government review. Detailed Environmental Impact Assessment is underway and will be submitted following the approval of the Technical and Economic Study.

The nearest in-country rail line is the Trans-Mongolia Railway that runs northwest to southeast and connects Ulaanbaatar to Beijing. The nearest point on this line to the Tsagaan Tolgoi Deposit is approximately 400 km to the east at the Chinese border. Limited infrastructure exists at Tsagaan Tolgoi and will need to be developed prior to any mining operations.

The Tsagaan Tolgoi Deposit is located close to Ivanhoe's Oyu Tolgoi copper and gold project and has the potential to supply coal to any power project that may, in the future, be there.

The Company is not currently planning to develop the Tsagaan Tolgoi Deposit, although the property remains a deposit that could be developed in the future.

Tavan Tolgoi Extension Area

The Tavan Tolgoi Extension Area is composed of seven exploration licenses located east of Dalanzadgad, the provincial capital in the Omnogovi Aimag. These exploration licenses surround the third party-owned Tavan Tolgoi coal project. The Tavan Tolgoi coal field was discovered in the 1950's by a joint Mongolian/Soviet team and is believed to be one of the largest undeveloped metallurgical coal deposits in the world.

A field reconnaissance program was carried out on the Tavan Tolgoi Extension licenses in 2006. The exploration area has been surveyed for copper and gold exploration using BHP Falcon aerial geophysics. The Company has obtained the aeromagnetic and aero gravity survey data and is using the results of the upcoming analysis of the Falcon data to help delineate potential coal targets. Exploration work on the extension continued in 2007, 2008 and 2009. A minimum amount of work will be carried out in 2010 to maintain the exploration licenses.

Exploration Program

A number of the exploration licenses are associated with the broader Ovoot Tolgoi Complex and the Soumber Deposit. The Company considers many of these to be prospective exploration properties, which have yet to be fully explored.

The exploration program in 2010 includes drilling, trenching and geological reconnaissance on a number of license areas which are identified as having good potential for coking and thermal coal deposits.

Indonesia Operations and Discontinued Operations

Prior to December 23, 2009, the Company held its 85% interest in the Mamahak Coal project through a joint venture.

As the Company progressed with efforts to prepare for the mining and shipment of the targeted 30,000 tonne trial cargo from Mamahak, the Company became aware of the requirement for additional capital expenditure beyond what was originally budgeted to develop the project. After the initial review of the project expenditures and related budgets, the Company suspended further development works at Mamahak pending a detailed operational review and analysis. The Company recorded an impairment charge of $15.1 million in 2009 (see Note 6 of the annual Consolidated Financial Statements).

On December 15, 2009, the Company announced that it had entered into an agreement to divest our 85% interest in the Mamahak Deposit in Indonesia to KRL, a mining company focused on the development of a series of coal projects in East Kalimantan, Indonesia, for consideration comprising $1 million in cash and 50 million shares of KRL. The receipt of shares as partial consideration is a common practice in the mining industry, particularly for companies in the early stages of development, such as KRL, that wish to preserve their capital for use in developing their projects. The sale of the Company's interest in the Mamahak Deposit was completed on December 23, 2009.

Metals Division Profile and Discontinued Operations

On December 31, 2008, the Company announced the sale of its Metals Division to Ivanhoe for $3 million and other non-cash consideration. The Metals Division consisted of a series of base and precious metal exploration properties in Mongolia and Indonesia, related assets, employees and contracts. As part of the sale transaction, the Company obtained a credit facility from Ivanhoe, providing for loan advances from Ivanhoe up to $30 million. The credit facility is for a one year term with a one year discretionary extension. The credit facility is unsecured and carries an interest rate equal to LIBOR plus 750 basis points.

The transaction was completed on February 2, 2009, following receipt of regulatory approval.

SUMMARIZED ANNUAL FINANCIAL RESULTS

($ in thousands, except per share information)

	2009	2008	2007
Revenue	**$ 36,038**	$ 3,126	$ –
Operating loss from continuing operations	**$ (23,321)**	$ (45,854)	$ (20,979)
Loss from continuing operations[i]	**$ (79,717)**	$ (51,975)	$ (92,061)
Loss from discontinued operations	**$ (31,088)**	$ (17,601)	$ (4,676)
Net loss[i]	**$(110,805)**	$ (69,576)	$ (96,736)
Loss per share from continuing operations	**$ (0.60)**	$ (0.40)	$ (1.80)
Loss per share from discontinued operations	**$ (0.23)**	$ (0.14)	$ (0.09)
Net loss per share	**$ (0.83)**	$ (0.54)	$ (1.89)
Cash and cash equivalents	**$ 357,342**	$ 10,117	$ 1,394
Short term investments	**$ 14,999**	$ –	$ –
Long term investments	**$ 57,070**	$ –	$ –
Total assets	**$ 560,684**	$ 99,948	$ 5,610
Total long term liabilities	**$ 543,086**	$ 329	$105,673

(i) *Includes the loss of $45.0 million for the fair value change of the embedded derivative in the CIC convertible debenture*

The year ended December 31, 2009, was the first full year of mining operations for the Company. The Company reported its first sales revenue in the fourth quarter of 2008.

Prior to the completion of the coal transaction in May 2007, the Company was a mineral exploration company with a principal focus on precious and base metals exploration and development.

Throughout 2008, the Company continued to explore for precious and base metals, however the purchase of the Coal Division from Ivanhoe transformed SouthGobi into a coal exploration, development and production company with revenue, cost of sales and significantly higher corporate administration and exploration costs. In December 2008 the Company sold its Metals Division to Ivanhoe for $3 million and other non-cash consideration. The transaction closed on February 2, 2009.

The Company's net loss for 2009 was $110.8 million or $0.83 per share compared with $69.6 million or $0.54 per share in 2008 and $96.7 million or $1.89 per share in 2007.

The loss from continuing operations was $79.7 million in 2009 compared to $52.0 million in 2008. The increase is due to the additional financing costs related to the line of credit facility with Ivanhoe and the CIC convertible debenture. The fair value change of the embedded derivative in the CIC convertible debenture resulted in a loss of $45.0 million in the year ended December 31, 2009. (See Other Income/Expense section for more details.) The loss from continuing operations excluding the fair value change of the embedded derivative in the CIC convertible debenture is $34.7 million.

The operating loss from continuing operations decreased to $23.3 million in 2009 from $45.9 million in 2008 due to higher revenues and lower exploration expense in 2009.

The net loss in 2009 includes $31.1 million in discontinued operations for the Indonesia Coal Division ("Mamahak Deposit"). In October 2009, the Company suspended further development works at Mamahak pending a detailed operational review and analysis. As a result of the suspension the Company recorded an impairment charge of $15.1 million in 2009. In the fourth quarter of 2009, the Indonesia Coal Division was sold to KRL for consideration comprising $1 million in cash and 50 million shares of KRL.

The Company's total assets at the end of 2009 were $560.7 million compared with $99.9 million at the end of 2008 and $5.6 million at the end of 2007. The Company had $357.3 million in cash, $15.0 million in short term investments and $57.1 million in long term investments at December 31, 2009, compared to cash of $10.1 million at December 31, 2008. The short and long term investments include money market investments and the Company's investment of $9.9 million in KRL which was obtained from the sale of the Indonesia Coal Division. The increase in cash and money market investments relate to the CIC financing. The increase in total assets relates to the CIC financing and the continuing development of the Mongolia Coal Division.

The Company's long term liabilities at the end of 2009 were $543.1 million compared with $0.3 million at the end of 2008 and $105.7 million at the end of 2007. The increase in long term liabilities in 2009 relates to the convertible debenture received from CIC in November 2009.

SELECTED QUARTERLY DATA

($ in thousands, except per share information)

	2009				2008			
Quarter ended	31-Dec	30-Sep	30-Jun	31-Mar	31-Dec	30-Sep	30-Jun	31-Mar
Revenue	**$ 9,960**	**$ 11,871**	**$ 10,667**	**$ 3,540**	$ 3,126	$ –	$ –	$ –
Income from mine operations	**1,524**	**3,234**	**1,528**	**327**	949	–	–	–
Exploration expenses	**(739)**	**(2,149)**	**(1,743)**	**(768)**	(4,959)	(8,468)	(9,125)	(3,893)
(Loss)/Income from continuing operations	**(70,187)**	**2,224**	**(5,138)**	**(6,616)**	(11,370)	(18,222)	(9,956)	(12,427)
Income/(Loss) from discontinued operations	**1,034**	**(26,006)**	**(2,772)**	**(3,344)**	(5,637)	(4,555)	(3,625)	(3,784)
Net loss	**(69,153)**	**(23,782)**	**(7,910)**	**(9,960)**	(17,007)	(22,777)	(13,581)	(16,211)
Net loss per share	**(0.52)**	**(0.18)**	**(0.06)**	**(0.07)**	(0.13)	(0.17)	(0.11)	(0.19)

Review of Quarterly Financial Results

The changes in comparative results of operations on a quarter over quarter basis are due primarily to significant fluctuations in the following areas: revenue, exploration expenses, stock-based compensation charges, foreign exchange gains and losses, interest expense, interest accretion on line of credit facility and fair value of embedded derivative on debt. These latter two items are described in Notes 22 and 23 of the annual Consolidated Financial Statements.

The Company incurred a net loss for the three months ended December 31, 2009, of $69.2 million compared to a net loss of $23.8 million for the three months ended September 30, 2009, and $17.0 million for the three months ended December 31, 2008. The change is due to the factors discussed below:

Revenue and cost of sales relate to the Mongolia Coal Division. Revenues increased to $10.0 million in the fourth quarter of 2009 from $3.1 million in the comparative quarter in 2008. Revenues however decreased from $11.9 million in the September 30, 2009 quarter due to lower customer shipments.

In the fourth quarter of 2009, the Company shipped approximately 359,000 tonnes of coal at an average realized selling price of $29 per tonne. This compares to 113,000 tonnes at an average realized price of $29 in the fourth quarter of 2008 and 457,000 tonnes at an average realized price of $28 in the third quarter of 2009. Variability in the realized selling price relates to a change in sales mix in terms of coal quality and changed prices of individual customer contracts.

Cost of sales is comprised of three main components, direct cash costs, mine administration costs and non-cash items. Non-cash items include depreciation, depletion and stock-based compensation. Cost of sales will vary depending on sales volume, production and unit costs which directly affects income from mine operations.

Direct cash costs per tonne increased to $16.97 per tonne in the fourth quarter of 2009 compared to $8.30 per tonne in the fourth quarter of 2008 and $11.16 in the third quarter of 2009. The increase can be attributed to the lower coal production in the fourth quarter of 2009. Direct cash costs per tonne will fluctuate from quarter to quarter due to variations in production, sales and unit costs. The Company continuously reviews the direct cash costs and believes they are in line with the expected life of mine cash costs of $15 per tonne as outlined in the Norwest technical report.

Corporate administration expenses in the fourth quarter of 2009 were higher than the September 30, 2009, quarter but comparable to the fourth quarter of 2008. The fourth quarter of 2009 included higher salaries and professional fees, while the September 30, 2009, quarter included higher listing fees and the fourth quarter of 2008 included a foreign exchange loss of $3.9 million.

Exploration expenses for the three months ended December 31, 2009, were $0.7 million compared to $5.0 million for the three months ended December 31, 2008, and $2.1 million for the three months ended September 30, 2009. Exploration expenses are for the Mongolia Coal Division. Exploration expenses related to the Indonesia Coal Division have been classified as discontinued operations in 2009 and in 2008. Exploration expenses related to the Metals Division have been classified as discontinued operations in 2008. Exploration expenses were lower in the fourth quarter of 2009 as the 2009 exploration program in Mongolia was close to completion at the end of the third quarter of 2009.

Finance costs for the three months ended December 31, 2009, were $61.9 million compared to $23,000 for the three months ended December 31, 2008. The significant increase in the fourth quarter is due to the CIC convertible debenture financing and the fair value change of the embedded derivative of $45.0 million, $3.0 million for the interest accretion on the convertible debenture, $4.7 million for interest expense on the convertible debenture and $9.4 million for transaction costs related to the CIC financing.

Income tax expense for the three months ended December 31, 2009, was $1.5 million compared to nil in the comparative period for 2008 and an $8.6 million recovery in the three months ended September 30, 2009.

Discontinued operations for the three months ended December 31, 2009, relate to the disposal of the Indonesia Coal Division. The Company had income in the fourth quarter of 2009 as the impairment of Mamahak of $23.0 million recorded in the third quarter was reduced to $15.1 million upon the sale of Mamahak in December 2009.

RESULTS OF OPERATIONS

	Year Ended December 31,		
	2009	2008	2007
Volumes, Prices and Costs			
Coal production *(millions of tonnes)*	**0.67**	1.16	–
Coal sales *(millions of tonnes)*	**1.33**	0.11	–
Average sales price *(per tonne)*	**$ 28.97**	$ 29.20	–
Total cash costs of product sold *(per tonne)*	**$ 16.58**	$ 14.09	–
Direct cash costs of product sold *(per tonne)*	**$ 14.61**	$ 8.30	–
Operating Statistics			
Total waste material moved *(millions of bank cubic metres)*	**2.27**	2.54	–
Strip ratio *(bank cubic metres of waste rock per tonne of clean coal produced)*	**3.36**	2.19	–
Operating Results *(thousands of dollars)*			
Revenue	**$ 36,038**	$ 3,126	$ –
Cost of sales	**(29,425)**	(2,177)	–
Income from mine operations	**6,613**	949	–
Administration expenses	**(24,535)**	(20,358)	(7,191)
Evaluation and exploration expenses	**(5,399)**	(26,445)	(13,788)
Operating loss from continuing operations	**$ (23,321)**	$ (45,854)	$ (20,979)

In 2009, 0.67 million tonnes of coal was produced with a strip ratio of 3.36 compared to 1.16 million tonnes produced in 2008 with a strip ratio of 2.19. Lower production in 2009 was the result of the full mine shutdown from March 2009 to July 2009 and the re-configuring of the pit which began in December 2009.

The Company incurred an operating loss from continuing operations for the year ended December 31, 2009, of $23.3 million compared to $45.9 million for the same period in 2008. The decrease in the operating loss is due to the factors discussed below.

Revenue and cost of sales relate to the Company's operations in Mongolia. Through early 2009, shipments across the border were limited and as a result the Company initiated a production curtailment program in January 2009. This was followed by a full mine shut down on February 24, 2009, except for coal loading of customer trucks from coal stockpiles.

With increasing sales and a reduction in its coal inventory, the Company resumed full mining operations effective July 1, 2009, on a 24 hours per day, seven days per week basis.

In 2009, the Company shipped approximately 1.33 million tonnes of coal at an average realized selling price of approximately $29 per tonne. This compares to 0.11 million tonnes of coal shipped in 2008 at an average realized selling price of $29 per tonne.

Cost of sales was $29.4 million in the year ended December 31, 2009, compared to $2.2 million for the year ended December 31, 2008. The increase in cost of sales relates to the higher sales volume in 2009. In 2008 there were only sales in the fourth quarter compared to a full year of sales in 2009. Cost of sales comprise the cost of the product sold, mine administration costs, equipment depreciation, depletion of stripping costs and stock-based compensation costs.

Direct cash costs were $14.61 per tonne in 2009 compared to $8.30 in 2008. The increase in direct cash costs is due to the full mine shut down from March 2009 to July 2009, which resulted in operational costs being expensed. The Company continuously reviews the direct cash costs and believes they are in line with the expected life of mine cash costs of $15 per tonne as outlined in the Norwest technical report.

Mine administration costs per tonne decreased to $1.97 per tonne for the year ended December 31, 2009, compared to $5.79 per tonne for the year ended December 31, 2008. The decrease per tonne is due to the higher sales volume in 2009.

Exploration expenses for the year ended December 31, 2009, were lower than the year ended December 31, 2008. Exploration expenses include expenses for the Mongolia Coal Division. Exploration expenses were higher in 2008 as prior to the commencement of sales in late September 2008, certain operational costs were classified as exploration expense.

Administration expenses for the year ended December 31, 2009, were $24.5 million compared to $20.4 million for the year ended December 31, 2008. The increase predominantly relates to salaries and benefits and professional fees. Administration expenses for the year ended December 31, 2009, includes approximately $10.5 million of stock-based compensation compared to approximately $3.8 million for the year ended December 31, 2008.

The administration expenses consist of the following major categories broken down for comparative purposes (see Note 8 of the annual Consolidated Financial Statements).

Legal fees for the year ended December 31, 2009, were higher than the year ended December 31, 2008. Legal fees include costs associated with the Company's regulatory affairs including expenses associated with corporate governance, contract negotiations, filing, registration and disclosure. Legal fees increased in 2009 due to higher contract negotiation fees.

Corporate administration fees are slightly higher in the year ended December 31, 2009, compared to the year ended December 31, 2008. The increase predominantly relates to additional administration costs incurred in the Hong Kong office. Certain of the Company's administrative staff and office facilities are provided by Global Mining Management Ltd. (see 'Related Party Transactions') on a cost recovery basis. Accordingly, quarterly fluctuations in the costs of administrative and personnel costs can be expected commensurate with increases or decreases in quarterly corporate activity and the level of personnel employed.

Professional fees have increased for the year ended December 31, 2009, as compared to the year ended December 31, 2008. Professional fees include the cost of quarterly reviews, internal computer systems training and planning, and accruals for the year-end audit of the Company's financial statements. The increase in 2009 relates predominantly to costs related to the various technical reports for the Mongolia project.

Salaries and benefits, excluding stock-based compensation costs, increased in the year ended December 31, 2009, to $3.6 million as compared to $1.8 million for the year ended December 31, 2008. The increase relates to the additional staff and bonuses for the year ended December 31, 2009.

The foreign exchange losses are primarily the result of changes of the U.S. to Canadian dollar ("Cdn$") and the U.S. to Mongolian Tugrik exchange rates during the period. The higher foreign exchange loss of $4.7 million for the year ended December 31, 2008, compared to $1.1 million in 2009 relates to the higher Canadian cash balances in 2008.

Listing fees consist of legal, accounting and professional fees incurred for a secondary listing on the Hong Kong stock exchange. Normally the Company would treat all charges as share issue costs upon a successful equity fundraising. In 2008, uncertainty in the timing of a possible equity financing led to a decision to expense $6.7 million in listing fees. In 2009, the Company continued with the secondary listing application and in October 2009 achieved milestones that strongly indicated that the secondary listing application would lead to an equity financing. All costs subsequent to this date were capitalized. In 2009, listing costs of $2.5 million were expensed and listing costs of $4.6 million were capitalized.

NON-IFRS FINANCIAL MEASURES

This Management's Discussion and Analysis of Financial Condition and Results of Operations ("MD&A") refers to certain financial measures, such as "cash costs", which are not standardized measures recognized under IFRS and do not have a standardized meaning prescribed by IFRS. These measures are commonly utilized in the mining industry and are considered informative for management, shareholders and analysts. These measures may differ from those made by other corporations and accordingly may not be comparable to such measures as reported by other mining companies.

Cash costs is the term used by the Company to describe the cash production costs and consists of cost of product, which includes direct and indirect costs of production.

($ in thousands, unless otherwise stated)

	Year Ended December 31,		
	2009	2008	2007
Cash costs, continuing operations			
Cost of sales per financial statements	**$ 29,425**	$ 2,177	$ –
Less non-cash adjustments	**(7,405)**	(586)	–
Total cash costs	**22,020**	1,591	–
Coal sales *(000's of tonnes)*	**1,328**	113	–
Total cash costs of product sold *(per tonne)*	**$ 16.58**	$ 14.09	$ –

	Year Ended December 31,		
	2009	2008	2007
Cash costs, continuing operations			
Direct cash costs of product sold *(per tonne)*	**$ 14.61**	$ 8.30	$ –
Mine administration cash costs of product sold *(per tonne)*	**1.97**	5.79	–
Total cash costs of product sold *(per tonne)*	**$ 16.58**	$ 14.09	$ –

EXPLORATION COSTS AND DISCONTINUED OPERATIONS BY DIVISION

($ in thousands)

	Year Ended December 31,		
	2009	2008	2007
Mongolian Coal Division	**$ 5,399**	$ 26,445	$ 13,788
Indonesian Coal Division – Discontinued Operations	**15,916**	9,740	–
Metals Division – Discontinued Operations	**–**	7,911	4,676
Total Exploration	**$ 21,315**	$ 44,096	$ 18,464

Mongolia Coal Division

Exploration costs are charged to operations until such time as it has been determined that a property has economically recoverable reserves, in which case the costs incurred to develop a property are capitalized. Exploration expenditures include consulting-geological, drilling, license fees, office costs and salaries and benefits.

The costs of pre-development, overburden removal and stripping activities, which are incurred in the pre-production stage are expensed as incurred. The Company commenced mining operations in Mongolia on April 2, 2008, and costs incurred for site development prior to the production phase were expensed.

The exploration expenditures in 2009 were $5.4 million compared to $26.4 million in 2008. The exploration costs in 2008 were higher as the Company acquired equipment, hired additional personnel and began pre-development activities at the Ovoot Tolgoi Mine. Pre-development of the Ovoot Tolgoi open pit mine site included road construction, site clearing, drainage control and topsoil removal. The 2008 exploration program concentrated on drilling in the Sunset Pit. The exploration continued to expand the extent of the known mineralization in both the underground and surface coal deposits as well as increase the knowledge level of the quality and structure of the deposit. The 2009 exploration program focused on Soumber, Greenfields and Tsagaan Tolgoi. The Soumber exploration program is a full geotechnical and hydrological study and is a follow-up to the exploration activities that were conducted in 2008. Greenfields has also shown new coal occurrences of high quality coal and therefore exploration was also focused on this area.

Indonesia Coal Division – Discontinued Operations

The sale of the Mamahak Deposit is disclosed as discontinued operations in 2008 and 2009. Exploration expenditures were $15.9 million for the year ended December 31, 2009, compared to $9.7 million for the year ended December 31, 2008. Exploration costs in 2008 were incurred to carry out geological reconnaissance, licensing, mapping, initial drilling, and a documentation program on the new concession in East Kalimantan. The Company continued exploration activities in Indonesia in 2009 until development work was suspended in October 2009.

Metals Division – Discontinued Operations

In 2008, the sale of the Metals Division was disclosed as a discontinued operation and its financial position and results were presented as separate items in the consolidated statement of financial position and statements of comprehensive income and cash flows.

The Company explored the Indonesian and Mongolian properties during 2008. The majority of the expenditures incurred were related to ongoing licence fees, drilling, and salaries.

OTHER INCOME/EXPENSE

($ in thousands)

	Year Ended December 31,		
	2009	2008	2007
Fair value change of embedded derivatives in convertible debenture	**$ 44,980**	$ –	$ –
Fair value change of embedded derivative in line of credit facility	**–**	7,223	63,286
Interest accretion on convertible debenture	**2,972**	–	–
Interest accretion on line of credit facility	**–**	598	6,481
Interest expense on convertible debenture	**4,712**	–	–
Interest expense on line of credit facilities	**1,651**	149	1,359
Transaction costs on issuance of convertible debenture	**9,399**	–	–
Mark to market gain on investments	**(843)**	–	–
Accretion of asset retirement obligation	**40**	19	–
Interest income	**(77)**	(1,868)	(44)
	$ 62,834	$ 6,121	$ 71,082

In November 2009, the Company entered into a financing agreement with a wholly owned subsidiary of CIC for $500 million in the form of a secured, convertible debenture bearing interest at 8.0% with a maximum term of 30 years. The financing is required primarily to support the accelerated investment program in Mongolia and up to $120 million of the financing may also be used for working capital, repayment of debt due on funding, general and administrative expense and other general corporate purposes.

The convertible debenture is a hybrid debt instrument, containing a debt host component and three embedded derivatives. The debt host is measured at amortized cost using the effective interest method. The embedded derivatives are measured at fair value and all changes in fair value will be recognized in profit or loss immediately. The transaction costs are allocated on a pro-rata basis between the embedded derivative and the debt host based on the fair value of the embedded derivative and the residual value of the debt host. For the year ended December 31, 2009, the fair value change on the embedded derivative was a $45.0 million loss, the interest accretion was $3.0 million, the interest expense was $4.7 million and the transaction fees were $9.4 million. The interest expense includes $3.8 million in cash and $0.9 million in shares.

In 2009, as part of the sale of the Metals Division, the Company obtained a $30 million working capital credit facility from Ivanhoe. The credit facility was for a one year term with a one year discretionary extension. The credit facility was unsecured and carried an interest rate equal to LIBOR plus 750 basis points. In July 2009, the Company and Ivanhoe agreed to increase the existing working capital credit facility from $30 million to $60 million. The amended credit facility had an original maturity date of December 31, 2010, was unsecured and had an interest rate of LIBOR plus 750 basis points. The amended facility also required repayment in the event that the Company acquired additional financing from a third party source and provided for an extension fee of $1.5 million payable in the event any portion of the facility was outstanding past March 31, 2010. In November 2009, after receiving the financing from CIC, the Company repaid the $50 million in principal plus $1.6 million in interest expense.

The mark to market gain on investments includes the mark to market on the 50 million shares of KRL, which were received as proceeds for the sale of the Indonesia Coal Division, and certain money market instruments.

On April 26, 2006, in conjunction with the coal transaction, the Company entered into a line of credit facility (the "First Funding Agreement") with Ivanhoe whereby Ivanhoe agreed to make available to the Company an unsecured line of credit of up to $10 million which was extended to a maximum of $15 million on June 6, 2007. Attached to the First Funding Agreement was a conversion option which became effective upon the completion of the coal transaction. On January 23, 2008, concurrent with the closing of equity private placements and at the Company's request, Ivanhoe converted the then principal balance of $30 million into 14,709,701 common shares of the Company. As a result of this conversion the amount due under the First Funding Agreement was eliminated.

Under IFRS, the conversion feature is considered an embedded derivative liability that must be recorded at its fair value upon initial measurement and revalued at each subsequent reporting period. The difference between the debt host component and the principal amount of the loan outstanding is accreted to income over the remaining term of the debt. (Please refer to Note 22 of the annual Consolidated Financial Statements for further details.)

The Company recognizes asset retirement obligations in the period in which they are incurred. The liability component is measured at fair value and is adjusted to its present value as accretion expense is recorded.

Interest income was higher in 2008, due to higher cash balances which relate to the completion of the equity financings in early 2008. Lower interest income during 2009 reflects lower average cash balances during this period as well as very low interest rates. The current economic climate has resulted in very low interest rates especially in the United States and rates are not expected to increase in the near term.

In 2009, the Company recorded current income tax expense of $0.5 million related to its Mongolian operations. The Company believes profitable operations in Mongolia are probable and has therefore recorded a future income tax asset of $6.9 million related to deductible temporary differences and the carry forward of unused tax losses.

LIQUIDITY AND CAPITAL RESOURCES

Cash Flow Highlights

($ in thousands)

	Year Ended December 31,		
	2009	2008	2007
Cash used in operating activities	**$ (35,230)**	$ (63,588)	$ (17,008)
Cash used in investing activities	**(105,105)**	(57,669)	(611)
Cash generated by financing activities	**487,332**	134,306	18,065
Effect of foreign exchange rate changes on cash	**5**	(4,103)	(17)
Increase in cash for the year	**347,002**	8,946	429
Cash balance, beginning of the year	**10,340**	1,394	965
Cash balance, end of the year	**$357,342**	$ 10,340	$ 1,394

General market conditions

Global economic conditions have improved during 2009. Despite the improvements the Company remains cautious about the speed and strength of the economic recovery. Labor markets continue to be weak, excess production capacity exists in developed economies and China appears to be taking measures to control growth and inflation. Notwithstanding the Company's caution in the short term, the Company expects demand for coal in China and India to grow through 2010 and into the foreseeable future. Management continues to monitor external conditions and their impact on the Company's business plans for the upcoming year.

Cash used in operating activities

At December 31, 2009, the Company had cash resources of $357.3 million compared to cash resources of $10.3 million at December 31, 2008.

Cash used in continuing operations was $16.0 million for the year ended December 31, 2009, compared to $48.6 million for the year ended December 31, 2008. Cash used in discontinued operations for the year ended December 31, 2009, was $19.2 million compared to $15.0 million for the year ended December 31, 2008.

The Company incurred a net loss from continuing operations before tax of $86.2 million for the year ended December 31, 2009 compared to a net loss from continuing operations of $52.0 million for the year ended December 31, 2008. Continuation of the Company's build out of the Ovoot Tolgoi mining operation, finance costs and evaluation and exploration costs contributed to the losses in 2008. In 2009, the Company recorded revenue of $36.0 million compared to 2008 when the Company recorded revenue of $3.1 million. The higher revenue in 2009 was offset by higher administration expenses, finance costs and interest expense. With the increased activities at the Ovoot Tolgoi site and the operations in Mongolia, accounts receivable, prepaid expenses, and accounts payable increased during the year ended December 31, 2009.

Accounts receivable include funds due from government taxation authorities (Goods and Services Tax or Value Added Tax). Verification of the collectability of the funds from government taxation authorities was conducted in the fourth quarter of 2008, early 2009 and the fourth quarter of 2009. Payment of accounts receivable due from government taxation authorities in Mongolia could be delayed, and is being used to offset future income taxes payable on account.

In July 2009, Mongolian tax law was amended to preclude producers and exporters of unfinished mineral products from claiming back VAT. The Mongolian Government has yet to define what products will qualify as finished mineral products and any VAT amounts impacted will be prospective from the effective date of the law, August 16, 2009. The Company is monitoring the amendments to the tax law regarding current claims for Value Added Tax.

The Company is also closely monitoring collectability of outstanding accounts receivable for current coal sales. Although all accounts are currently in order, unfavorable market conditions may have an impact on future collectability.

Prepaid balances and deposits have increased during 2009. The increase relates to the timing of prepayments for Mongolian exploration licenses, supplies, and insurance.

Coal and supplies inventory have increased to $16.4 million at December 31, 2009, from $13.7 million at the year ended December 31, 2008. Coal and supplies inventory is valued at the lower of cost and net realizable value. Coal inventory cost of $9.6 million includes direct and indirect labor, operating materials and supplies, transportation costs and an appropriate portion of fixed and variable overhead expenses including depreciation and depletion. Supplies inventory consists of consumable parts and supplies.

The Company had a stockpile of approximately 390,000 tonnes of coal inventory at December 31, 2009, and 1.1 million tonnes at December 31, 2008.

Accounts payable have increased in the year ended December 31, 2009, due to increased corporate activity related to the secondary listing on the Hong Kong Stock Exchange.

Cash used for investing activities

Cash used for investing activities was $105.1 million for the year ended December 31, 2009, compared to $57.7 million for the year ended December 31, 2008.

The Company's investment in property, plant and equipment was higher during 2008 as the Company prepared the Ovoot Tolgoi Mine for production. Deposits for further mining equipment are included as plant and equipment. The Company incurred expenditures in 2009 for mobile and mining equipment and deferred stripping in Mongolia.

In the fourth quarter of 2009, after the receipt of the proceeds from the CIC financing, the Company invested $15.0 million and $47.5 million in short and longer term money market instruments respectively.

Interest income will increase or decrease depending on the cash position and interest rates. Interest was higher in 2008 due to higher cash balances which related directly to the completion of the equity financings. Lower interest income during 2009 reflects lower average cash balances during this period as well as very low interest rates. The current economic climate has resulted in very low interest rates especially in the United States and rates are not expected to increase in the near term.

Cash provided by financing activities

In November 2009, the Company entered into a financing agreement with a wholly owned subsidiary of CIC for $500 million in the form of a secured, convertible debenture bearing interest at 8.0% with a maximum term of 30 years. The financing is required primarily to support the accelerated investment program in Mongolia and up to $120 million of the financing may also be used for working capital, repayment of debt due on funding, general and administrative expense and other general corporate purposes.

On December 31, 2008, the Company announced the sale of its Metals Division to Ivanhoe for $3 million and other non-cash consideration. As part of the sale transaction, the Company obtained a $30 million credit facility from Ivanhoe. The credit facility was for a one year term with a one year discretionary extension. The credit facility was unsecured and carried an interest rate equal to LIBOR plus 750 basis points. In July 2009, the Company and Ivanhoe agreed to increase the existing working capital credit facility from $30 million to $60 million. The amended credit facility had an original maturity date of December 31, 2010, was unsecured and had an interest rate of LIBOR plus 750 basis points. The amended facility also required repayment in the event that the Company acquired additional financing from a third party source and provided for an extension fee of $1.5 million payable in the event any portion of the facility was outstanding past March 31, 2010. In November 2009, after receiving the financing from CIC, the Company repaid the $50 million in principal plus $1.6 million in interest expense.

In 2008, the Company completed a series of equity financing transactions and received proceeds from the exercise of stock options. The total proceeds net of issue costs were $140.4 million for the year ended December 31, 2008, compared to proceeds received for the exercise of stock options for the year ended December 31, 2009, of $3.9 million.

The proceeds from the equity financings in 2008 were used for the initial development of the open-pit coal mine at the Company's Ovoot Tolgoi project, and for additional drilling and engineering focused on the Ovoot Tolgoi site and development of the Indonesia coal project. Proceeds have also been used for investigating new projects, equipment expenditures and for general corporate and administrative purposes. The proceeds were also used to repay amounts advanced under the line of credit facility obtained from Ivanhoe in October 2007.

Contractual Obligations and Guarantees

In the normal course of business, the Company enters into contracts that give rise to commitments for future minimum payments. The following table summarizes the remaining contractual maturities of the Company's operating and capital commitments at December 31, 2009.

	As at December 31, 2009				
Contractual obligations	**Within 1 year**	**2–3 years**	**4–5 years**	**Over 5 years**	**Total**
Capital expenditure commitments	$ 17,563	$ –	$ –	$ –	$ 17,563
Minimum rental and lease payments	1,352	2,014	578	–	3,944
	$ 18,915	$ 2,014	$ 578	$ –	$ 21,507

Liquidity, Financing and Working Capital Resources

The Company is an integrated coal exploration, development and production company. Based on proceeds from CIC and the net proceeds from the International Offering, the Company does not anticipate any additional funding requirements in the near future.

In November 2009, the Company entered into a financing agreement with a wholly owned subsidiary of CIC for $500 million in the form of a secured, convertible debenture bearing interest at 8.0% with a maximum term of 30 years. The financing is required primarily to support the accelerated investment program in Mongolia and up to $120 million of the financing may also be used for working capital, repayment of debt due on funding, general and administrative expense and other general corporate purposes.

Key commercial terms of the financing include:

- Interest – 8% per annum (6.4% payable semi-annually in cash and 1.6% payable annually in the Company's shares, where the number of shares to be issued is calculated based on the 50-day volume-weighted average price (VWAP);
- Term – Maximum of 30 years;
- Security – First charge over the Company's assets, including shares of its material subsidiaries;
- Conversion price – The conversion price is set as the lower of Cdn$11.88 or the 50-day VWAP at the date of conversion, with a floor price of Cdn$8.88 per share;
- Conversion timing – The Company and CIC each have various rights to call conversion of the debenture into common shares. CIC has the right to convert the debenture, in whole or in part, into common shares 12 months after the date of issue. The Company has the right to call for the conversion of up to $250 million of the debenture on the earlier of 24 months after the issue date, if the conversion price is greater than Cdn$10.66, or upon the Company achieving a public float of 25% of its common shares under certain agreed circumstances if the conversion price is greater than Cdn$10.66;
- Company's normal conversion right – After 60 months from the issuance date, at any time that the conversion price is greater than Cdn$10.66, the Company will be entitled to require conversion of the outstanding convertible debenture in whole or in part, into common shares at the conversion price;
- Representation on the Company's Board – While the debenture loan is outstanding, or while CIC has a minimum 15% direct or indirect stake in the Company, CIC has the right to nominate one director to the Company's Board. The Company currently has eight Board members;
- Voting restriction – CIC has agreed that it will not have any voting rights in the Company beyond 29.9% if CIC ever acquires ownership of such a shareholder stake through exercising the debenture;
- Pre-emption rights – While the debenture loan is outstanding, or while CIC has a 15% direct or indirect stake in the Company, CIC has certain pre-emption rights on a pro-rata basis to subscribe for any new shares to be allotted and issued by the Company for the period which the debenture is outstanding. The pre-emption rights will not apply to new shares issued pursuant to pro-rata public equity offerings made to all shareholders, exercise of stock options and shares issued to achieve a 25% public float;
- Right of first offer – While a portion of the debenture is outstanding, or while CIC has a 15% direct or indirect stake in the Company, CIC has the right of first offer for any direct and indirect sale of Ivanhoe's ownership stake in the Company. As at March 15, 2010, Ivanhoe owned directly and indirectly approximately 105.6 million of the Company's shares, or approximately 65% of the Company's current issued and outstanding shares; and
- Registration rights – CIC has registration rights under applicable Canadian provincial securities laws in connection with the common shares issuable upon conversion of the debenture.

In conjunction with the financing, the Company also entered into a mutual co-operation agreement with a subsidiary of CIC. Under the terms of the agreement, CIC's subsidiary will provide advice and services to the Company on matters that include sales to China, procurement and logistics, and will receive a customary commercial payment for such services based on product sales from Mongolia to China.

On January 29, 2010, the Company announced that it had closed the global equity offering of 27 million common shares of the Company at a price of Cdn$17.00 per common share, for gross proceeds of Cdn$459.0 million. The Company's future plans for the proceeds include, expanding the existing production capacity of the open pit mine at the Ovoot Tolgoi Mine, assess, construct and develop the regional infrastructure and the coal transportation infrastructure, completion of technical and engineering assessment, for construction of value added facilities, exploration activities and general corporate purposes, which may include provision of working capital and general exploration, development and acquisition activities.

On March 12, 2010, the Company announced, subject to regulatory approval, a formal request for CIC to convert $250 million of its convertible debenture into common shares of the Company.

RELATED PARTY TRANSACTIONS

The Company is a party to a shareholders' cost-sharing agreement with certain other public and private companies, including Ivanhoe (the "Other Companies") pursuant to which the Company and the Other Companies are equal shareholders in Global Mining Management Ltd. ("GMM") and, through GMM, share office space, furnishings and equipment and communications facilities (on a cost recovery basis) and the employment, on a part-time basis, of various administrative, office and management personnel in Vancouver, British Columbia. Costs of the shared office facilities and the shared part-time employees and service providers are recovered from the Company proportionate to the time spent by the shared part-time employees and service providers on matters pertaining to the Company. Certain of the directors and officers of the Company are also officers and directors of GMM. The Company has utilized the services of the GMM staff and office since September 1, 2003 and has incurred costs of $1.8 million and $2.5 million for the years ended December 31, 2009, and December 31, 2008, respectively.

On December 31, 2008, the Company announced the sale of the Metals Division to Ivanhoe for $3 million and other non-cash consideration. The Metals Division consisted of a series of base and precious metal exploration properties in Mongolia and Indonesia, related assets, employees and contracts. As part of the sale transaction, the Company obtained a credit facility from Ivanhoe, which allowed the Company to receive loan advances from Ivanhoe to an aggregate maximum of $30 million. The credit facility was for a one year term with a one year discretionary extension. The credit facility was unsecured and carried an interest rate equal to LIBOR plus 750 basis points.

In July 2009, the Company and Ivanhoe agreed to increase the existing working capital credit facility from $30 million to $60 million. The amended credit facility had an original maturity date of December 31, 2010, was unsecured and had an interest rate of LIBOR plus 750 basis points. The amended facility also required repayment in the event that the Company acquires additional financing from a third party source and provided for an extension fee of $1.5 million payable in the event any portion of the facility was outstanding past March 31, 2010. In November 2009, the Company after receiving the financing from CIC repaid the $50 million in principal plus $1.6 million in interest expense.

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 March 15, 2010, there were 161,770,687 common shares issued and outstanding. There are also incentive stock options outstanding that are exercisable to acquire 7,380,961 unissued common shares. On a diluted basis, 169,151,648 common shares were outstanding. There are no preferred shares outstanding.

Ivanhoe, directly and indirectly, currently owns 105,557,155 common shares representing approximately 65% of the issued and outstanding common shares of SouthGobi.

DISCLOSURE CONTROLS AND PROCEDURES

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 Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

Management, including the Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of the design and operation of the Company's disclosure controls and procedures. As of December 31, 2009, the Chief Executive Officer and Chief Financial Officer have each concluded that the Company's disclosure controls and procedures, as defined in National Instrument 52-109 – Certification of Disclosure in Issuer's Annual and Interim Filings, are effective to achieve the purpose for which they have been designed.

INTERNAL CONTROLS OVER FINANCIAL REPORTING

Internal controls over financial reporting are designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements in accordance with IFRS. Management is also responsible for the design of the Company's internal control over financial reporting in order to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with IFRS.

The Company's internal controls over financial reporting include policies and procedures that: pertain to the maintenance of records that, in reasonable detail accurately and fairly reflect the transactions and disposition of assets; provide reasonable assurance that transactions are recorded as necessary to permit preparation of the financial statements in accordance with IFRS and that receipts and expenditures are being made only in accordance with authorization of management and directors of the Company; and provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of assets that could have a material effect on the financial statements.

Because of their inherent limitations, internal controls over financial reporting can provide only reasonable assurance and may not prevent or detect misstatements. Furthermore, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

The Company's management, under the supervision of the Chief Executive Officer and the Chief Financial Officer, has evaluated the effectiveness of the Company's internal controls over financial reporting using the framework and criteria established in *Internal Control-Integrated Framework*, issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on the evaluation, management has concluded that internal controls over financial reporting were effective as at December 31, 2009.

There has been no change in the Company's internal controls over financial reporting that occurred during the most recently completed quarter that has materially affected, or is reasonably likely to materially affect, the Company's internal controls over financial reporting.

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 business and industry; and (ii) risks relating to its projects in Mongolia. 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.

Risks Relating to the Company's Business and Industry

Some of the Company's projects may not be completed as planned, costs may exceed its 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: the particular attributes of the deposit, such as size, grade and proximity to infrastructure; commodity prices, which are highly cyclical; and 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 current intention to develop mines at the Soumber 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.

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. For example, as the Company progressed with efforts to prepare for the mining and shipment of a targeted 30,000 tonne trial cargo from the Mamahak Deposit, the Company became aware of the need for additional capital expenditure beyond what was originally budgeted. Based on these requirements and the revised resource estimates contained in the Mamahak Technical Expert Report, the Company suspended further development works at the Mamahak Deposit pending a more detailed operational review. As a result of the suspension, the Company recorded an impairment charge of US$23 million in the third quarter of 2009, which brought the value of the Mamahak Deposit assets to zero as at September 30, 2009.

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.

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.

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 and net losses and operating cash outflows to date, and therefore the Company's short operating history may make it difficult for investors to evaluate its business and growth.

The Company commenced mining in April 2008 and currently operates one revenue producing mine. In the year ended December 31, 2009, the Company recorded a net loss. As is typical for a start up mining company, the Company has recorded a deficit since inception. Although the Company has no plans to pay dividends in the near future, should such deficits continue and cash reserve be depleted, it could adversely affect the Company's ability to pay dividends in the future. Due to the Company's limited operating history, there may not be an adequate basis on which to evaluate the Company's future operating results and prospects. Because the Company's past results may not be indicative of the Company's results in the future, investors may have difficulties evaluating the Company's business and prospects.

The Company does not insure against all risks to which it may be subject 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, umbrella liability, aviation premises liability, and kidnap and ransom. 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 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.

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.

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

In Mongolia, the Company's exploration licences are subject to periodic renewal and may only be renewed a limited number of times for a limited period of time. While it anticipates that renewals will be given as and when sought, 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. The Company's business objectives may also be impeded by the costs of holding and/or renewing the exploration licences in Mongolia. Licence fees for exploration licences increase substantially upon the passage of time from the original issuance of each individual exploration licence. The Company needs to assess continually the mineral potential of each exploration licence, particularly at the time of renewal, to determine if the costs of maintaining the exploration licences are justified by the exploration results to date, and may elect to let some of its exploration licences lapse. Moratorium on transfers of exploration licences has been imposed on two separate occasions and there is a risk that a similar moratorium could be imposed such that letting the exploration licences lapse may be the only practical option in some circumstances. Furthermore, the Company will require mining licences and permits to mine in order to conduct mining operations in Mongolia. There can be no assurance, however, that such licences 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.

In addition, certain provisions of the Land Law of Mongolia enacted on June 7, 2002, and effective from January 1, 2003, (the "Land Law") and the Mineral Law of Mongolia, enacted on July 8, 2006, and effective August 26, 2006, (the "2006 Minerals Law") provide for the revocation of previously granted land use rights, exploration licences or mining licences on the grounds that the affected area of land has been designated as "special needs" territory. The Land Law 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 licence holder whose rights or licence status are affected. If any of the Company's land use rights, exploration licences or mining licences 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 licences 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.

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. If realized coal prices fall 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 losses and may decide to discontinue operations, which could require the Company to incur closure costs and result in reduced revenues.

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 shovels, 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 shovels 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 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. While the Company expects to sell and deliver most of its coal from the Ovoot Tolgoi Mine at the mine gate, 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, to a lesser extent, in 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-Ceke border crossing does not have sufficient capacity to support the increased amount of cargo traffic or is affected by external factors such as disruptions caused by bad weather. The opening hours of the Shivee Khuren-Ceke border crossing also affect the Company's ability to expedite the movement of its coal shipment. 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 limit the number of available personnel and increase competition for skilled personnel. 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.

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 into 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. Additionally, the Company has been selling its coal products only since September 2008. The Company currently has three customers with the largest customer representing approximately 64%, and the remaining customers accounting for 36% of the Company's total sales for the year ended December 31, 2009. The Company's relatively brief history of coal sales makes it difficult to evaluate the strength of its relationships with current customers and its ability to attract additional customers. Accordingly, inability to attract additional customers or the loss of, or a significant reduction in, purchases by any of the limited number of potential customers could materially and adversely affect the Company's future revenue and the economic viability of its exploration and development projects.

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 the Company's business and results of operations.

In addition, the Company is subject to reclamation requirements. The Company's mines contain a finite amount of recoverable resources and will eventually close. The key tasks in relation to the closure of the mines involve (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.

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 has not incurred any environmental research and development costs to date. 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 MNT, Renminbi 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. 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.

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, Ivanhoe, may differ from those of its other shareholders.

As of March 15, 2010, Ivanhoe holds approximately 65% of the Company's issued and outstanding shares. The interests of Ivanhoe may conflict with the interests of the Company's other Shareholders and there is no assurance that Ivanhoe will vote its shares in a way that benefits the Company's minority shareholders. Ivanhoe's ownership interest enables Ivanhoe 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, Ivanhoe is in a position to:

- control the Company's policies, management and affairs;
- subject to applicable laws, regulations and the Articles, adopt amendments to certain provisions of the Articles; and
- 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 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.

Future stock market conditions may change.

There are risks involved with any investment in Common Shares. The market price of the Company's 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 Hong Kong Stock Exchange, 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 the Company's 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.

Risks relating to the Company's Projects in Mongolia

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.

In addition, while legislation has been enacted to protect private property against expropriation and nationalisation, 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 nationalisation. Expropriation or nationalisation 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.

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.

In 2006, the Mongolian Government enacted a new minerals law. 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 Mongolian Government 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 a new law (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 Mongolian Government was instructed to define the boundaries of the areas in which exploration and mining would be prohibited by October 16, 2009. However, the Mongolian Government has not yet approved and published this information. New exploration licences and mining licences overlapping the defined prohibited areas will not be granted – and previously granted licences 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 licence holders shall be compensated, but there are no specifics as to the way such compensation will be determined.

The Mineral Resources Authority of Mongolia ("MRAM") has prepared a draft list of licences that overlap with the prohibited areas described in the new law – based on information submitted by water authority agencies, forest authority agencies and local authorities – for submission to the Mongolian Ministry of Mineral Resources and Energy (the "MMRE"). Subsequent to the MMRE's approval of this preliminary list, the Mongolian Government must still give its final approval before the final list can be published. During the MMRE's and the Mongolian Government's review of the draft list of licences prepared by MRAM, licences may be added or subtracted to the list at any time prior to approval and publication of the final list.

Four of the Company's exploration licences – included on MRAM's draft list of licences – may be included on the final list published by the Mongolian Government, potentially affecting the status of those licences under the Mining Prohibition in Specified Areas Law. Activities being carried out on these properties include drilling, trenching and geological reconnaissance. The Company has no immovable company 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.

As such, there can be no assurance that future political and economic conditions in Mongolia will not result in the Mongolian Government 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 Mongolian Government 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.

Government policy may change to discourage foreign investment, nationalisation 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 nationalisation, 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 Mongolian Government 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 of Mongolia has wide discretion to designate mineral deposits to be Mineral Deposits of Strategic Importance. The Mongolian Government is empowered to participate on an equity basis with the licence holder in the exploitation and/or mining of each Mineral Deposit of Strategic Importance on terms to be negotiated between the Mongolian Government and such licence holder. Details of any minerals reserves must be filed by the relevant licence holder with the Mongolian Government, 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 (a list of deposits designated by the parliament of Mongolia to be deposits of strategic importance) and the additional Tier 2 Deposits List (a list of 39 deposits designated by the parliament of Mongolia for further investigation by the Mongolian Government in order to determine if any or all of them should be placed on the Strategic Deposits List), the Mongolian 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 licence holder with respect to the terms under which the Mongolian Government will take an interest in such deposit. Whilst the Mongolian Government 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 licence area is within, or overlaps a Mineral Deposit of Strategic Importance.

Under the 2006 Minerals Law, the size of the Mongolian Government'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 Mongolian Government 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 Mongolian Government will take its interest and the final arrangements in respect of the Mongolian Government's interest in each Mineral Deposit of Strategic importance, including the amount of compensation to be paid to the licence holder and the actual form of the Mongolian Government's interest are subject to negotiation between the Mongolian Government and the licence 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 Mongolian Government's participating interest in excess of 50%. Whilst the 2006 Minerals Law provides that the interest of the Mongolian Government 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 licence holder and the Mongolian Government. There can be no assurance that legislation will not be enacted which further strengthens the Mongolian Government's right to participate in privately held mineral resources in Mongolia.

None of the deposits covered by the Company's existing mining licences or exploration licences 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.

OUTLOOK

The Company believes that demand for commodities is increasing. General economic conditions are showing signs of improvement. It is difficult to reliably forecast commodity prices and customer demand for the Company's products; however the Company's sales and marketing are providing positive results. The Company is continuing to pursue new customers, and maintain strong relations with its current customer base.

The Company's properties in Mongolia are well located in close proximity to China and other major industrializing economies in Asia. Furthermore, the near-term production is in high quality bituminous thermal and coking coals, which the Company anticipates will remain attractive premium products.

The western region of Gansu is one of the Company's key markets and, given the relatively close proximity of the Company's projects to the region, the Company believes that it is well positioned to exploit consumption growth in the area. Power plant expansion, currently underway, in Gansu is expected to increase thermal coal purchases from outside Gansu from approximately 13 million tonnes in 2008 to approximately 55 million tonnes in 2020. Gansu has no production of coking coal and all coking coal used in the steel industry is sourced from other provinces. The Ovoot Tolgoi Mine is located 492 km from Jiayuguan, while mines in the next closest major supply base, Hami in Xinjiang, are located 619 km away.

Furthermore, the Company has conducted a complete market analysis, with an outside consulting group of the coal markets in western Inner Mongolia and Gansu provinces, helping us to further identify potential customers in these provinces.

The success to date and potential for future growth can be attributed to a combination of the Company's competitive strengths, including the following:

- Projects are strategically located close to China, especially to the fast growing Gansu and Inner Mongolia regions;
- Substantial and growing resources and reserves;
- Produce premium quality coals;
- Low cost structure due to favorable geographic and geological conditions;
- Established production with strong growth potential through future expansion of existing mine capacity and development of the Company's priority assets; and
- Experienced management team with strong skills in mining, exploration and marketing and are able to leverage the expertise, experience and relationships of its principal shareholder, Ivanhoe.

Mongolia

Revenue was $10.0 million for the three months ended December 31, 2009, compared to $11.9 million for the three months ended September 30, 2009. The Company will continue to focus on generating higher sales volume throughout 2010.

On October 12, 2009, the Company announced that independent NI 43-101 estimates prepared by Norwest upgraded the reserves at the Ovoot Tolgoi Complex and the Soumber Deposit:

- Total surface mineable coal reserves as of July 1, 2009, at Ovoot Tolgoi were calculated and estimated to be 105 million tonnes of proven reserves and 9.1 million tonnes of probable reserves;
- Ovoot Tolgoi surface and underground resources as of June 1, 2009, were calculated and estimated to be 181.7 million tonnes of measured resources, 68.1 million tonnes of indicated resources and 33.5 million tonnes of inferred resources; and
- The Soumber resource area is estimated to contain 13.1 million tonnes of measured resources, 8.3 million tonnes of indicated resources and 55.5 million tonnes of inferred resources.

The Company is engaged in ongoing discussions with the Mongolian Government with the objective of establishing a border crossing at the Ceke border point that will be open 24 hours per day, 365 days per year. This should increase daily distribution of Ovoot Tolgoi coal to our customers in China.

The Company continues to develop markets for its premium quality coals. A China based research firm has conducted a complete market analysis of the coal markets in western Inner Mongolia and Gansu provinces, helping us to identify potential customers in these provinces. The target customer base consists of a mixture of distributors and end users of coal, including steel mills, power plants and industrial consumers.

Overview and Objectives

The Company continues to focus its efforts on mining, development and exploration of coking and thermal coal products in Mongolia for supply of quality products to customers in China. As the Company looks forward through the balance of 2010, the Company is encouraged by the positive developments in Mongolia. The Company is making progress with its sales and marketing efforts, continuing to focus on efficiency and prudent financial management and intends to manage production levels to meet anticipated demand for the Company's products.

The Company's objectives for 2010 are as follows:

- **Grow Ovoot Tolgoi Mine** – The additional capacity of the already commissioned Liebherr 996 fleet should support strong growth in coal availability and sales for 2010 over 2009. Additional Terex MT4400 trucks are planned to be commissioned in the first half of 2010 and an additional Liebherr 996 fleet is expected to arrive before the end of the year.
- **Continue to develop regional infrastructure** – Our immediate priority centers on improving roads in the area around Ovoot Tolgoi Mine and contributing to new road development.
- **Advancing the Soumber deposit** – SouthGobi intends to further define the deposit with continued exploration work whilst also substantially advancing the feasibility, planning and licensing for a mine at Soumber.
- **Value-adding/upgrading coal** – We intend to embark on the construction of our first coal handling/processing facility. This first stage will involve basic coal crushing and screening for Ovoot Tolgoi coals to create a more consistent higher quality product for customers.
- **Exploration** – Further green fields exploration will take place, with the company planning an exploration budget in the order of $10-20 million.
- **Continuing to focus on production safety, environmental protection, operational excellence and community relations.**

March 22, 2010

FINANCIAL STATEMENTS, NOTES AND APPENDIX

FINANCIAL STATEMENTS

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

ADDITIONAL STOCK EXCHANGE INFORMATION

AUDITORS' REPORT

To the Shareholders of
SouthGobi Energy Resources Ltd.

We have audited the consolidated statements of financial position of SouthGobi Energy Resources Ltd. as at December 31, 2009 and 2008 and the consolidated statements of comprehensive income, changes in equity and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2009 and 2008 and the results of its operations and its cash flows for the years then ended in accordance with International Financial Reporting Standards.

Deloitte & Touche LLP

Chartered Accountants
Vancouver, Canada
March 22, 2010

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

(expressed in thousands of U.S. Dollars, except for share and per share amounts)

		YEAR ENDED DECEMBER 31,	
	NOTES	**2009**	2008
			(restated)
CONTINUING OPERATIONS			
Revenue		**$ 36,038**	$ 3,126
Cost of sales	7	**(29,425)**	(2,177)
Income from mine operations		**6,613**	949
Administration expenses	8	**(24,535)**	(20,358)
Evaluation and exploration expenses	9	**(5,399)**	(26,445)
Operating loss from continuing operations		**(23,321)**	(45,854)
Finance costs	10	**(62,911)**	(7,989)
Interest Income		**77**	1,868
Loss before tax		**(86,155)**	(51,975)
Current income tax expense	11	**(509)**	–
Deferred income tax recovery	11	**6,947**	–
Loss from continuing operations		**(79,717)**	(51,975)
Loss from discontinued operations	6	**(31,088)**	(17,601)
Net loss and comprehensive loss attributable to equity holders of the Company		$ **(110,805)**	$ (69,576)
BASIC AND DILUTED LOSS PER SHARE FROM:			
Continuing operations	12	**(0.60)**	(0.40)
Discontinued operations	12	**(0.23)**	(0.14)
Continuing and discontinued operations		**(0.83)**	(0.54)
Weighted average number of basic and diluted shares outstanding ('000s)	12	**133,499**	128,354

The accompanying notes are an integral part of these Consolidated Financial Statements.

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

(expressed in thousands of U.S. Dollars)

		YEAR ENDED DECEMBER 31,		
	NOTES	2009	2008	2007
			(restated)	*(restated)*
ASSETS				
Current assets				
Cash and cash equivalents	13	**$ 357,342**	$ 10,117	$ 1,394
Trade and other receivables	14	**12,328**	7,290	760
Short term investments	16	**14,999**	–	–
Inventories	17	**16,384**	13,677	–
Prepaid expenses and deposits	18	**8,119**	2,578	1,890
		409,172	33,662	4,044
Assets classified as held for sale	6	**–**	638	–
Total current assets		**409,172**	34,300	4,044
NON-CURRENT ASSETS				
Property, plant and equipment	20	**82,705**	52,440	1,123
Intangible assets	19	**–**	13,208	443
Deferred listing costs	15	**4,565**	–	–
Deferred income tax assets	11	**6,947**	–	–
Long term investments	16	**57,070**	–	–
Other receivables		**225**	–	–
Total non-current assets		**151,512**	65,648	1,566
Total assets		**$ 560,684**	$ 99,948	$ 5,610
EQUITY AND LIABILITIES				
Current liabilities				
Trade and other payables	21	**$ 12,669**	$ 7,400	$ 1,768
Amounts due under line of credit facilities	22	**3,009**	–	–
Current portion of convertible debenture	23	**4,712**	–	–
Deposit received for sale of Metals Division	6	**–**	3,000	–
		20,390	10,400	1,768
Current liabilities classified as held for sale	6	**–**	255	–
Total current liabilities		**20,390**	10,655	1,768
Non-current liabilities				
Amounts due under line of credit facilities	22	**–**	–	105,673
Convertible debenture	23	**542,351**	–	–
Asset retirement obligation	24	**735**	329	–
Total non-current liabilities		**543,086**	329	105,673
Total liabilities		**563,476**	10,984	107,441
SHAREHOLDERS' (DEFICIENCY)/EQUITY				
Common shares	25	**296,419**	289,512	30,230
Preferred shares	25	**–**	–	4,189
Share option reserve	26	**22,300**	12,775	7,497
Accumulated deficit	27	**(321,511)**	(213,323)	(143,747)
Total shareholders' (deficiency)/equity		**(2,792)**	88,964	(101,831)
Total shareholders' equity and liabilities		**$ 560,684**	$ 99,948	$ 5,610
Net current assets		**$ 388,782**	$ 23,645	$ 2,276
Total assets less current liabilities		**$ 540,294**	$ 89,293	$ 3,842

Commitments for expenditure (Note 34)
Subsequent events (Note 35)

The accompanying notes are an integral part of these Consolidated Financial Statements.

APPROVED BY THE BOARD:

"André Deepwell"	**"Pierre Lebel"**
Director	**Director**

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

(expressed in thousands of U.S. Dollars)

	COMMON SHARES	PREFERRED SHARES	SHARE OPTION RESERVE	ACCUMULATED DEFICIT	TOTAL
Balance, January 1, 2008	$ 30,230	$ 4,189	$ 7,497	$ (143,747)	$ (101,831)
Shares issued for:					
Cash	139,642	–	–	–	139,642
Share issue costs	(3,303)	–	–	–	(3,303)
Mineral properties	5,198	–	–	–	5,198
Conversion of line of credit	107,552	–	–	–	107,552
Conversion of preferred shares	4,189	(4,189)	–	–	–
Exercise of stock options	6,004	–	(1,960)	–	4,044
Stock-based compensation charged to operations	–	–	7,238	–	7,238
Net loss and comprehensive loss for the year	–	–	–	(69,576)	(69,576)
Balances, December 31, 2008	$ 289,512	$ –	$ 12,775	$ (213,323)	$ 88,964
Shares issued for:					
Exercise of stock options	**$ 6,907**	**$ –**	**$ (3,010)**	**$ –**	**$ 3,897**
Stock-based compensation charged to operations	**–**	**–**	**12,535**	**–**	**12,535**
Gain on sale of Metals Division (Note 6)	**–**	**–**	**–**	**2,617**	**2,617**
Net loss and comprehensive loss for the year	**–**	**–**	**–**	**(110,805)**	**(110,805)**
Balances, December 31, 2009	**$ 296,419**	**$ –**	**$ 22,300**	**$ (321,511)**	**$ (2,792)**

For details on movement in shares please see Note 25.

The accompanying notes are an integral part of these Consolidated Financial Statements.

CONSOLIDATED STATEMENT OF CASH FLOWS

(expressed in thousands of U.S. Dollars)

	NOTES	YEAR ENDED DECEMBER 31, 2009	2008 (restated)
OPERATING ACTIVITIES			
Loss for the year from continuing operations before tax		**$ (86,155)**	$ (51,975)
Adjustments for:			
Depreciation and depletion		**5,856**	494
Share-based compensation		**12,195**	5,645
Fair value change on embedded derivative		**44,980**	7,223
Mark to market adjustment on investments		**(843)**	–
Interest income		**(77)**	(1,868)
Accrued interest expense		**4,721**	134
Interest accretion on line of credit facility		**–**	598
Interest accretion on convertible debenture		**2,972**	–
Transaction costs on issuance of convertible debenture		**9,399**	–
Unrealized foreign exchange loss		**1,213**	4,464
Loss on disposal of property, plant and equipment		**245**	6
Accretion on asset retirement obligation		**40**	19
Operating cash flows before movements in working capital		**(5,454)**	(35,260)
Increase in inventories		**(3,443)**	(10,857)
Increase in trade and other receivables		**(8,379)**	(6,801)
Increase in prepaid expenses and deposits		**(6,322)**	(959)
Increase in trade and other payables		**7,595**	5,246
Cash used in continuing operations		**(16,003)**	(48,631)
Cash used in discontinued operations	6	**(19,227)**	(14,957)
Cash used in operating activities		**$ (35,230)**	$ (63,588)
INVESTING ACTIVITIES			
Purchase of property, plant and equipment		**$ (35,770)**	$ (53,975)
Interest received		**37**	1,868
Proceeds from disposal of property, plant and equipment		**26**	10
Purchase of short term investments		**(15,000)**	–
Purchase of long term investments		**(47,450)**	–
Increase in other receivables		**(225)**	–
Cash used in continuing operations		**(98,382)**	(52,097)
Cash used in discontinued operations		**(6,723)**	(5,572)
Cash used in investing activities		**$ (105,105)**	$ (57,669)
FINANCING ACTIVITIES			
Proceeds from issuance of common shares and exercise of stock options		**$ 3,897**	$ 140,383
Increase in deferred charges		**(4,565)**	–
Proceeds from issuance of convertible debenture, net of issue costs	23	**485,000**	–
Drawings under line of credit facilities		**53,000**	2,000
Repayments of line of credit facilities		**(50,000)**	(8,077)
Cash generated from financing activities		**$ 487,332**	$ 134,306
Effect of foreign exchange rate changes on cash		**5**	(4,103)
Increase in cash and cash equivalents		**347,002**	8,946
Cash and cash equivalents, beginning of year		**10,340**	1,394
Cash and cash equivalents, end of year		**$ 357,342**	$ 10,340
COMPRISED OF:			
Cash and cash equivalents of continuing operations		**$ 357,342**	$ 10,117
Cash and cash equivalents of discontinued operations		**–**	223
Total cash and cash equivalents		**$ 357,342**	$ 10,340
Cash		**$ 242,352**	$ 6,659
Money market instruments		**114,990**	3,681
Total cash and cash equivalents		**$ 357,342**	$ 10,340

Supplemental cash flow information (Note 33)

The accompanying notes are an integral part of these Consolidated Financial Statements.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2009

(expressed in thousands of U.S. Dollars and shares in thousands, unless otherwise indicated)

1. CORPORATE INFORMATION

SouthGobi Energy Resources Ltd. is a publicly listed company incorporated in Canada with limited liability under the legislation of the Province of British Columbia and its shares are listed on the Toronto Stock Exchange and Hong Kong Stock Exchange (Note 35.1). The company together with its subsidiaries (collectively referred to as the "Company") is principally engaged in the acquisition, exploration, development and production of coal properties in Mongolia. The Company's parent is Ivanhoe Mines Ltd. (the "parent" or "Ivanhoe").

The head office, principal address and registered and records office of the Company are located at 999 Canada Place, Suite 654, Vancouver, British Columbia, V6C 3E1.

The Company's Financial Statements and those of all of its controlled subsidiaries ("Consolidated Financial Statements") are presented in U.S. dollars and all values are rounded to the nearest thousand dollars except where otherwise indicated. Information related to shares is presented in thousands except for loss per share information which is presented in U.S. cents.

The Company is a coal producer and a coal exploration and development company. These Consolidated Financial Statements have been prepared on a going concern basis, which contemplates the realization of assets and settlement of liabilities in the normal course of business.

In February 2009, the Company completed the sale of its Metals Division to Ivanhoe Mines Ltd. for $3 million. The Metals Division consisted of certain base and precious metals properties in Mongolia and Indonesia. The Company will now be focused solely on coal production, development and exploration.

2. BASIS OF PREPARATION

2.1 Statement of compliance

The Company's Consolidated Financial Statements have been prepared in accordance with and using accounting policies in full compliance with the International Financial Reporting Standards ("IFRS") issued by the International Accounting Standards Board ("IASB") and Interpretations of the International Financial Reporting Interpretations Committee ("IFRIC"), effective for the Company's reporting for the year ended December 31, 2009.

Previously, the Company prepared its Consolidated Annual and Consolidated Interim Financial Statements in accordance with Canadian Generally Accepted Accounting Principles ("GAAP").

2.2 Basis of presentation

The Company's Consolidated Financial Statements have been prepared on the historical cost basis except for certain non-current assets and financial instruments, which are measured at fair value, as explained in the accounting policies set out in Note 4. The comparative figures presented in these Consolidated Financial Statements are in accordance with IFRS and any changes from figures previously reported under GAAP have been discussed in Note 3.

2. BASIS OF PREPARATION *(continued)*

2.3 Adoption of new and revised standards and interpretations

The IASB issued a number of new and revised IASs, IFRSs, amendments and related IFRICs (hereinafter collectively referred to as the "new IFRS") which are effective for the Company's financial year beginning on January 1, 2009. For the purpose of preparing and presenting the Consolidated Financial Statements, the Company has consistently adopted all these new standards for the years ended December 31, 2009 and 2008.

At the date of authorization of these Financial Statements, the IASB and IFRIC has issued the following new and revised standards, amendments and interpretations which are not yet effective during the year ended December 31, 2009.

- IFRS (Amendments) — Amendment to IFRS 5 as part of Improvements to IFRS issued in 2008[(i)]
- IFRS (Amendments) — Improvements to IFRS issued in 2009[(ii)]
- IAS 24 (Revised) — Related party disclosures[(vi)]
- IAS 27 (Revised) — Consolidated and separate financial statements[(i)]
- IAS 32 (Amendment) — Classification of rights issues[(iv)]
- IAS 39 (Amendment) — Eligible hedged items[(i)]
- IFRS 1 (Amendment) — Additional exemptions for first-time adopters[(iii)]
- IFRS 1 (Amendment) — Limited exemption from comparative IFRS 7 disclosure for first-time adopters[(v)]
- IFRS 2 (Amendment) — Company cash-settled share-based payment transactions[(iii)]
- IFRS 3 (Revised) — Business combinations[(i)]
- IFRS 9 — Financial instruments[(vii)]
- IFRIC 14 (Amendment) — Prepayment of a minimum funding requirement[(vi)]
- IFRIC 17 — Distributions of non-cash Assets to owners[(i)]
- IFRIC 19 — Extinguishing financial liabilities with equity instruments[(v)]

(i) *Effective for annual periods beginning on or after July 1, 2009*
(ii) *Amendments are effective for annual periods beginning on or after July 1, 2009 or January 1, 2010, as appropriate*
(iii) *Effective for annual periods beginning on or after January 1, 2010*
(iv) *Effective for annual periods beginning on or after February 1, 2010*
(v) *Effective for annual periods beginning on or after July 1, 2010*
(vi) *Effective for annual periods beginning on or after January 1, 2011*
(vii) *Effective for annual periods beginning on or after January 1, 2013*

The Company anticipates that the application of these standards, amendments and interpretations will have no material impact on the results and financial positions of the Company.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2009

(expressed in thousands of U.S. Dollars and shares in thousands, unless otherwise indicated)

3. FIRST-TIME ADOPTION OF IFRS

The Company adopted IFRS on January 1, 2009 with a transition date of January 1, 2005. Under IFRS 1 *'First-time Adoption of International Financial Reporting Standards'*, the IFRS are applied retrospectively at the transition date with all adjustments to assets and liabilities as stated under GAAP taken to retained earnings unless certain exemptions are applied. The Company is not applying any exemptions on first-time adoption of IFRS.

Below is the Company's Consolidated Statement of Financial Position as at the transition date of January 1, 2005 under IFRS.

	As at January 1, 2005
ASSETS	
Current assets	
Cash and cash equivalents	$ 8,222
Trade and other receivables	80
Prepaid expenses and deposits	124
Total current assets	8,426
NON-CURRENT ASSETS	
Property, plant and equipment	149
Intangible assets	158
Total non-current assets	307
Total assets	$ 8,733
EQUITY AND LIABILITIES	
Current liabilities	
Trade and other payables	$ 1,035
Total current liabilities	1,035
Total liabilities	1,035
Shareholders' equity	
Common shares	14,183
Additional paid in capital	1,691
Share option reserve	996
Accumulated deficit	(9,172)
Total shareholders' equity	7,698
Total shareholders' equity and liabilities	$ 8,733

IFRS employs a conceptual framework that is similar to Canadian GAAP. While the adoption of IFRS has not changed the actual cash flows of the Company, the adoption has resulted in significant changes to the reported financial position and results of operations of the Company. Presented below are reconciliations prepared by the Company to reconcile to IFRS the assets, liabilities, equity, net loss and cash flows of the Company from those reported under Canadian GAAP:

3.1 Total assets

		At December 31,				At January 1,
	Notes	2008	2007	2006	2005	2005
Total assets under Canadian GAAP		$100,132	$ 5,610	$ 2,052	$ 3,775	$ 8,699
Adjustments for differing accounting treatments:						
– Inclusion of coal division assets	(i)	–	–	263	144	35
– Adjustment for asset retirement obligation	(v)	(184)	–	–	–	–
Total assets under IFRS		$ 99,948	$ 5,610	$ 2,315	$ 3,919	$ 8,734

3. FIRST-TIME ADOPTION OF IFRS *(continued)*

3.2 Total liabilities

	Notes	At December 31, 2008	2007	2006	2005	At January 1, 2005
Total liabilities under Canadian GAAP		$ 11,168	$ 36,875	$ 6,287	$ 693	$ 1,035
Adjustments for differing accounting treatments:						
– Fair value of embedded derivative on debt	(ii)	107,552	70,566	–	–	–
– Conversion of debt	(ii)	(107,552)	–	–	–	–
– Adjustment for warrant liability	(iv)	–	–	222	222	–
– Conversion of warrant liability	(iv)	–	–	(222)	–	–
– Adjustment for asset retirement obligation	(v)	(184)	–	–	–	–
Total liabilities under IFRS		$ 10,984	$107,441	$ 6,287	$ 915	$ 1,035

3.3 Total equity (deficiency)

	Notes	At December 31, 2008	2007	2006	2005	At January 1, 2005
Total equity (deficiency) under Canadian GAAP		$ 88,964	$ (31,266)	$ (4,235)	$ 3,082	$ 7,664
Adjustments for differing accounting treatments:						
– Inclusion of coal division results, net of contribution by Ivanhoe	(i)	–	–	263	144	35
– Fair value of embedded derivative on debt	(ii)	(107,552)	(70,565)	–	–	–
– Conversion of debt	(ii)	107,552	–	–	–	–
– Adjustment for warrant liability	(iv)	–	–	–	(222)	–
Total equity (deficiency) under IFRS		$ 88,964	$(101,831)	$ (3,972)	$ 3,004	$ 7,699

3.4 Net loss

	Notes	Year ended December 31, 2008	2007	2006	2005
Net loss and comprehensive loss for the period under Canadian GAAP		$ 62,386	$ 26,730	$ 9,362	$ 6,214
Basic and Diluted Loss per Share under Canadian GAAP		$ 0.49	$ 0.52	$ 0.56	$ 0.41
Adjustments for differing accounting treatments:					
– Inclusion of coal division results	(i)	–	2,546	12,168	9,923
– Fair value of embedded derivative on debt	(ii)	7,223	63,286	–	–
– Interest accretion on line of credit facility	(ii)	319	4,224	–	–
– Adjustments on stock based compensation	(iii)	(352)	(50)	(251)	(107)
– Adjustment for warrant liability	(iv)	–	–	450	80
Net loss and comprehensive loss for period under IFRS		$ 69,576	$ 96,736	$ 21,729	$ 16,110
Basic and Diluted Loss per Share under IFRS		$ 0.54	$ 1.89	$ 1.31	$ 1.06

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2009

(expressed in thousands of U.S. Dollars and shares in thousands, unless otherwise indicated)

3. FIRST-TIME ADOPTION OF IFRS *(continued)*

3.5 Cash flows

The adoption of IFRS has had no impact on the net cash flows of the Company. The changes made to the Consolidated Statements of Financial Position and Consolidated Statements of Comprehensive Income have resulted in reclassifications of various amounts on the Consolidated Statements of Cash Flows, however as there have been no changes to the net cash flows, no reconciliations have been presented.

3.6 Notes to the IFRS reconciliation above:

(i) Inclusion of coal division results

On May 29, 2007, the Company completed the purchase of the Ivanhoe coal division (Note 31) in consideration for the issuance to Ivanhoe of 57,000 common shares and 25,576 convertible preferred shares.

Under Canadian GAAP – The coal transaction was accounted for as a related party transaction at the carrying value.

Under IFRS – The coal transaction is considered a combination between businesses or entities under common control and is therefore exempt from the scope of IFRS 3 *'Business Combinations'*. The Company has accounted for the business combinations of the entities under common control by using the principles of merger accounting as if the current group structure had always been combined.

(ii) Fair value of embedded derivative on debt

On April 26, 2006, in conjunction with the coal transaction, the Company entered into a line of credit facility (the "First Funding Agreement") with Ivanhoe whereby Ivanhoe agreed to make available to the Company an unsecured line of credit of up to $10 million which was extended to a maximum of $15 million on June 6, 2007. Attached to the First Funding Agreement was a conversion option which became effective upon the completion of the coal transaction. From April 26, 2006 to May 1, 2007 the Company accounted for any amounts drawn down on the credit facility as a liability at amortized cost and considered the fair value of the conversion feature to be insignificant because the significant milestones discussed below had not been achieved. On May 1, 2007 the conversion feature was considered to have a significant value as significant milestones surrounding the completion of the coal transaction had been achieved. These significant milestones included: (i) the signing of the definitive agreement with respect to the Company's acquisition of the coal division; (ii) approval of the coal transaction by the minority shareholders of the Company; and (iii) transfer of the coal mining licenses to the Company by Ivanhoe. From May 1, 2007 onwards the Company assigned a value of $3.1 million to the conversion feature. On January 23, 2008, concurrent with the closing of equity private placements and at the Company's request, Ivanhoe converted the then principal balance of $29,963 into 14,710 common shares of the Company (Note 22). As a result of this conversion the amount due under the line of credit facility was eliminated.

Under Canadian GAAP – After the achievement of the significant milestones discussed above, the conversion feature was recorded as a separate component of equity.

Under IFRS – After the achievement of the significant milestones discussed above, the conversion feature is considered an embedded derivative liability that must be recorded at its fair value upon initial measurement and revalued at each subsequent reporting period. The difference between the debt host component and the principal amount of the loan outstanding is accreted to income over the remaining term of the debt.

3. FIRST-TIME ADOPTION OF IFRS *(continued)*

3.6 Notes to the IFRS reconciliation above *(continued)*

(iii) Adjustment on stock based compensation

Recognition of expense

Under Canadian GAAP – Prior to 2008, the Company used the straight-line method of calculating vested options. The fair value of stock-based awards with graded vesting was calculated as one grant and the resulting fair value was recognized on a straight-line basis over the vesting period. In 2008, the Company changed from the straight-line method to the graded-vesting method.

Under IFRS – Each tranche of an award with different vesting dates is considered a separate grant for the calculation of fair value, and the resulting fair value is amortized over the vesting period of the respective tranches.

Forfeitures

Under Canadian GAAP – Forfeitures of awards were recognized as they occurred.

Under IFRS – Forfeiture estimates are recognized on the grant date and revised for actual experiences in subsequent periods.

(iv) Adjustment for warrant liability

On June 28, 2005, BHP Billiton World Exploration Inc. ("BHP") purchased 1,153,998 units of the Company for $1 million. Each unit consisted of one common share and one warrant to purchase one-half a common share. The warrants had a term of two years and an exercise price of Cdn$1.395 per common share. On June 26, 2006, all outstanding warrants were exercised by BHP and the warrant liability was eliminated.

Under Canadian GAAP – The warrants were accounted for at carrying value as equity.

Under IFRS – The exercise price of the warrants is fixed in Canadian dollars. The functional currency of the Company is in U.S. dollars and therefore the conversion option is considered a derivative as the Company will receive a variable amount of cash when the warrants are exercised. As a result, the BHP warrants meet the definition of a derivative liability under IAS 39 *'Financial Instruments: Recognition and Measurement'* and is recorded as a financial liability and stated at fair value at each date of the statement of financial position.

(v) Adjustment for asset retirement obligation ("ARO")

At December 31, 2008 the Company did an analysis of the discount rate used to present-value its ARO liability.

Under Canadian GAAP – A change in the discount rate alone did not result in a re-measurement of the ARO liability.

Under IFRS – Under IAS 37 *'Provisions, Contingent Liabilities and Contingent Assets'* a change in the current market-based discount rate will result in a change in the measurement of the provision. As a result, the ARO liability recorded in 2008 has been re-measured using the discount rate in effect at year end and an adjustment has been recorded to the corresponding asset.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2009

(expressed in thousands of U.S. Dollars and shares in thousands, unless otherwise indicated)

4. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

4.1 Basis of consolidation

The Consolidated Financial Statements include the financial statements of the Company and its controlled subsidiaries (Note 30). Control is achieved when the Company has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities.

The results of subsidiaries acquired or disposed of during the year are included in the Consolidated Statement of Comprehensive Income from the effective date of acquisition or up to the effective date of disposal, as appropriate.

All intra-Company transactions, balances, income and expenses are eliminated in full on consolidation.

Minority interests in the net assets of consolidated subsidiaries are identified separately from the Company's equity therein. Minority interests consist of the amount of those interests at the date of the original business combination (see Note 4.2) and the minority interests' share of changes in equity since the date of the combination. Losses applicable to the minority interests in excess of their interest in the subsidiary's equity are allocated against the interests of the Company except to the extent that the minority interests have a binding obligation and are able to make an additional investment to cover the losses.

4.2 Business combinations

Acquisitions of subsidiaries and businesses (other than entities which were under the control of the parent) are accounted for using the acquisition method. The cost of the business combination is measured as the aggregate of the fair value (at the date of exchange) of assets given, liabilities incurred or assumed, and equity instruments issued by the Company in exchange for control of the acquiree, plus any acquisition-related costs incurred to effect a business combination. The acquiree's identifiable assets, liabilities and contingent liabilities that meet the conditions for recognition under IFRS 3 *'Business Combinations'* are recognized at their fair value at the acquisition date except for non-current assets (or disposal groups) that are classified as held for sale in accordance with IFRS 5 *'Non-current Assets Held for Sale and Discontinued Operations,'* which are recognized and measured at fair value less cost to sell.

Goodwill arising on acquisition is recognized as an asset and initially measured at cost, being the excess of the cost of the business combination over the Company's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities recognized. If, after reassessment, the Company's interest in the net fair value of the acquiree's identifiable assets, liabilities and contingent liabilities exceeds the cost of the business combination, the excess is recognized immediately in profit or loss.

A business combination involving businesses under common control is a business combination in which all of the combining businesses are ultimately controlled by the same party or parties both before and after the business combination, and that control is not transitory. Business combinations under common control are accounted for in accordance with the principle of merger accounting. In applying the principle of merger accounting, the consolidated financial statements incorporate the financial statement items of the combining businesses in which the common control combination occurs as if they had been combined from the date when the combining business first came under the control of the controlling party.

The net assets of the combining businesses are combined using the existing book values prior to the common control combinations from the controlling parties' perspective. No amount is recognized in respect of goodwill or excess of acquirer's interest in the net fair value of the acquiree's identifiable assets, liabilities and contingent liabilities over the cost at the time of common control combination, to the extent of the continuation of the controlling party's interest.

The Consolidated Statement of Comprehensive Income includes the results of each of the combining businesses from the earliest date presented or since the date when the combining businesses first came under common control, where this is a shorter period, regardless of the date of common control combination.

4. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

4.3 Interest income

Interest income from financial assets is accrued on a time basis, by reference to the principal outstanding and at the effective interest rate applicable, which is the rate that exactly discounts estimated future cash receipts through the expected life of the financial asset to that asset's net carrying amount.

4.4 Foreign currencies

The Company's reporting currency and the functional currency of all of its operations is the U.S. dollar as this is the principal currency of the economic environment in which they operate.

Transactions in foreign currencies are initially recorded at the functional currency rate at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency rate of exchange ruling at the end of each reporting period.

Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates as at the dates of the initial transactions. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value is determined.

4.5 Borrowing costs

Borrowing costs directly attributable to the acquisition, construction or production of a qualifying asset are capitalized as part of the cost of that asset. Other borrowing costs not directly attributable to a qualifying asset are expensed in the period incurred.

4.6 Retirement benefit costs

Payments to retirement benefit costs are charged as an expense when employees have rendered services entitling them to the contributions.

4.7 Inventories

Coal inventories are stated at lower of production cost and net realizable value. Production costs include direct and indirect labor, operating materials and supplies, transportation costs and an appropriate portion of fixed and variable overhead expenses, including depreciation and depletion. Net realizable value represents the estimated selling price for inventories less all estimated costs of completion and costs necessary to make the sale.

Materials and supplies inventory consists of consumable parts and supplies which are valued at lower of weighted average cost and net realizable value. Supplies used in the production of inventories are not written down below cost if the finished products in which they will be incorporated are expected to be sold at or above cost. Net realizable value is defined as the selling price of the finished product less any provisions for obsolescence and costs of completion.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

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4. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

4.8 Property, plant and equipment ("PPE")

PPE is stated at cost less accumulated depreciation and accumulated impairment losses. The cost of an item of PPE consists of the purchase price, any costs directly attributable to bringing the asset to the location and condition necessary for its intended use and an initial estimate of the costs of dismantling and removing the item and restoring the site on which it is located.

Depreciation is provided at rates calculated to write off the cost of PPE, less their estimated residual value, using the straight-line method or unit-of-production method over the following expected useful lives:

- Mobile equipment — 5 years
- Computer equipment — 1 to 5 years
- Furniture and fixtures — 5 years
- Machinery and equipment — 3 to 10 years
- Buildings and roads — 5 to 15 years
- Construction in progress — see below
- Mineral assets — based on resources on a unit-of-production basis

Construction in progress includes PPE in the course of construction for production or for its own use purposes. Construction in progress is carried at cost less any recognized impairment loss. Construction in progress is classified to the appropriate category of PPE when completed and ready for intended use. Depreciation of these assets, on the same basis as other property assets, commences when the assets are ready for their intended use.

Mineral assets include deferred stripping costs and asset retirement obligations related to the reclamation of mining properties.

An item of PPE is derecognized upon disposal, when held for sale or when no future economic benefits are expected to arise from the continued use of the asset. Any gain or loss arising on disposal of the asset, determined as the difference between the net disposal proceeds and the carrying amount of the asset, is recognized in the Consolidated Statement of Comprehensive Income.

The Company conducts an annual assessment of the residual balances, useful lives and depreciation methods being used for PPE and any changes arising from the assessment are applied by the Company prospectively.

4.9 Stripping costs

Stripping costs incurred during the development of a mine are capitalized into PPE. Stripping costs incurred during the commercial production phase are variable production costs that are included in the costs of inventory produced during the period that the stripping costs are incurred, unless the stripping activity can be shown to give rise to future benefits from the mineral property, in which case the stripping costs would be capitalized into PPE.

Future benefits arise when stripping activity increases the future output of the mine by providing access to a new ore body that the previously deferred stripping costs in an area did not give access to. When stripping activities give rise to a future economic benefit, the costs associated with these activities are capitalized into PPE. Capitalized stripping costs are depleted on a unit-of-production basis, using estimated resources as the depletion base.

4. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

4.10 Mineral properties

All direct costs related to the acquisition of mineral property interests are capitalized into intangible assets on a property by property basis. Exploration costs, net of incidental revenues, are charged to operations in the period incurred until such time as it has been determined that a property has economically recoverable reserves, in which case subsequent exploration costs and the costs incurred to develop a property are capitalized into PPE. On the commencement of commercial production, depletion of each mining property will be provided on a unit-of-production basis using estimated resources as the depletion base.

The commencement of commercial production is deemed to occur on a determination made by management. Management's determination of when commercial production commences is based on several qualitative and quantitative factors including but not limited to the following:

- the elevation or bench where the coal to be mined has been reached
- the commissioning of major mine and plant equipment is completed
- operating results are being achieved in a consistent manner.

However, the production phase does not commence with the removal of *de minimis* saleable mineral materials that occur in conjunction with the removal of overburden or waste material for the purpose of obtaining access to an ore body.

4.11 Decommissioning, restoration and similar liabilities ("Asset retirement obligation" or "ARO")

The Company recognizes provision for statutory, contractual, constructive or legal obligations, including those associated with the reclamation of mineral properties and mineral assets under PPE, when those obligations result from the acquisition, construction, development or normal operation of the assets. Initially, a provision for an asset retirement obligation is recognized as its present value in the period in which it is incurred. Upon initial recognition of the liability, the corresponding asset retirement obligation is added to the carrying amount of the related asset and the cost is amortized as an expense over the economic life of the asset using either the unit-of-production method or the straight-line method, as appropriate. Following the initial recognition of the asset retirement obligation, the carrying amount of the liability is increased for the passage of time and adjusted for changes to the current market-based discount rate, amount or timing of the underlying cash flows needed to settle the obligation.

4.12 Share-based payments

Share-based payment transactions

Employees (including directors and senior executives) of the Company receive a portion of their remuneration in the form of share-based payment transactions, whereby employees render services as consideration for equity instruments ("equity-settled transactions").

In situations where equity instruments are issued to non-employees and some or all of the goods or services received by the entity as consideration cannot be specifically identified, they are measured at fair value of the share-based payment. Otherwise, share-based payments are measured at the fair value of goods or services received.

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4. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

4.12 Share-based payments *(continued)*

Equity-settled transactions

The costs of equity-settled transactions with employees are measured by reference to the fair value at the date on which they are granted.

The costs of equity-settled transactions are recognized, together with a corresponding increase in equity, over the period in which the performance and/or service conditions are fulfilled, ending on the date on which the relevant employees become fully entitled to the award ("the vesting date"). The cumulative expense is recognized for equity-settled transactions at each reporting date until the vesting date reflects the Company's best estimate of the number of equity instruments that will ultimately vest. The profit or loss charge or credit for a period represents the movement in cumulative expense recognized as at the beginning and end of that period and the corresponding amount is represented in share option reserve. No expense is recognized for awards that do not ultimately vest.

Where the terms of an equity-settled award are modified, the minimum expense recognized is the expense as if the terms had not been modified. An additional expense is recognized for any modification which increases the total fair value of the share-based payment arrangement, or is otherwise beneficial to the employee as measured at the date of modification.

The dilutive effect of outstanding options is reflected as additional dilution in the computation of earnings per share.

4.13 Taxation

Income tax expense represents the sum of tax currently payable and deferred tax.

Current income tax

Current income tax assets and liabilities for the current and prior periods are measured at the amount expected to be recovered from or paid to the taxation authorities. The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted at the end of each reporting period.

Deferred income tax

Deferred income tax is provided using the liability method on temporary differences, at the end of each reporting period, between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred income tax liabilities are recognized for all taxable temporary differences, except:

- where the deferred income tax liability arises from the initial recognition of goodwill or of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and
- in respect of taxable temporary differences associated with investments in subsidiaries, where the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

Deferred income tax assets are recognized for all deductible temporary differences, carry forward of unused tax credits and unused tax losses, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences and the carry forward of unused tax credits and unused tax losses can be utilized except:

- where the deferred income tax asset relating to the deductible temporary difference arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and
- in respect of deductible temporary differences associated with investments in subsidiaries, deferred income tax assets are recognized only to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilized.

4. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

4.13 Taxation *(continued)*

Deferred income tax *(continued)*

The carrying amount of deferred income tax assets is reviewed at the end of each reporting period and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred income tax asset to be utilized. Unrecognized deferred income tax assets are reassessed at the end of each reporting period and are recognized to the extent that it has become probable that future taxable profit will allow the deferred tax asset to be recovered.

Deferred income tax assets and liabilities are measured at the tax rates that are expected to apply to the year when the asset is realized or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at the end of each reporting period.

Deferred income tax relating to items recognized directly in equity is recognized in equity and not in the statement of comprehensive income.

Deferred income tax assets and deferred income tax liabilities are offset if, and only if, a legally enforceable right exists to set off current tax assets against current tax liabilities and the deferred tax assets and liabilities relate to income taxes levied by the same taxation authority on either the same taxable entity or different taxable entities which intend to either settle current tax liabilities and assets on a net basis, or to realize the assets and settle the liabilities simultaneously, in each future period in which significant amounts of deferred tax assets or liabilities are expected to be settled or recovered.

4.14 Financial assets

All financial assets are initially recorded at fair value and designated upon inception into one of the following four categories: held to maturity, available for sale, loans and receivables or at fair value through profit or loss (“FVTPL”).

Financial assets classified as FVTPL are measured at fair value with unrealized gains and losses recognized through profit and loss.

Financial assets classified as loans and receivables and held to maturity are measured at amortized cost using the effective interest method less any allowance for impairment. The effective interest method is a method of calculating the amortized cost of a financial asset and of allocating interest income over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash receipts (including all fees and points paid or received that form an integral part of the effective interest rate, transaction costs and other premiums or discounts) through the expected life of the financial asset, or, where appropriate, a shorter period.

Financial assets classified as available for sale are measured at fair value with unrealized gains and losses recognized in other comprehensive income (loss) except for losses in value that are considered other than temporary or a significant or prolonged decline in the fair value of that investment below its cost.

Transactions costs associated with FVTPL financial assets are expensed as incurred, while transaction costs associated with all other financial assets are included in the initial carrying amount of the asset.

4. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

4.15 Financial liabilities

All financial liabilities are initially recorded at fair value and designated upon inception as FVTPL or other financial liabilities.

Financial liabilities classified as other financial liabilities are initially recognized at fair value less directly attributable transaction costs. After initial recognition, other financial liabilities are subsequently measured at amortized cost using the effective interest method. The effective interest method is a method of calculating the amortized cost of a financial liability and of allocating interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments through the expected life of the financial liability, or, where appropriate, a shorter period.

Financial liabilities classified as FVTPL include financial liabilities held for trading and financial liabilities designated upon initial recognition as FVTPL. Derivatives, including separated embedded derivatives are also classified as held for trading unless they are designated as effective hedging instruments. Transaction costs on financial liabilities classified as FVTPL are expensed as incurred. Fair value changes on financial liabilities classified as FVTPL are recognized through the statement of comprehensive income.

At the end of each reporting period subsequent to initial recognition, financial liabilities at FVTPL are measured at fair value, with changes in fair value recognized directly in profit or loss in the period in which they arise. The net gain or loss recognized in profit or loss excludes any interest paid on the financial liabilities.

4.16 Impairment of financial assets

The Company assesses at the end of each reporting period whether a financial asset is impaired.

Assets carried at amortized cost

If there is objective evidence that an impairment loss on assets carried at amortized cost has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the financial asset's original effective interest rate. The carrying amount of the asset is then reduced by the amount of the impairment. The amount of the loss is recognized in profit or loss.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized, the previously recognized impairment loss is reversed to the extent that the carrying value of the asset does not exceed what the amortized cost would have been had the impairment not been recognized. Any subsequent reversal of an impairment loss is recognized in profit or loss.

In relation to trade and other receivables, a provision for impairment is made and an impairment loss is recognized in profit and loss when there is objective evidence (such as the probability of insolvency or significant financial difficulties of the debtor) that the Company will not be able to collect all of the amounts due under the original terms of the invoice. The carrying amount of the receivable is reduced through use of an allowance account. Impaired debts are written off against the allowance account when they are assessed as uncollectible.

Available for sale

If an available for sale asset is impaired, an amount comprising the difference between its cost and its current fair value, less any impairment loss previously recognized in profit or loss, is transferred from equity to profit or loss. Reversals in respect of equity instruments classified as available-for-sale are not recognized in profit or loss.

4. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

4.17 Derecognition of financial assets and financial liabilities

Financial assets are derecognized when the rights to receive cash flows from the assets expire or, the financial assets are transferred and the Company has transferred substantially all the risks and rewards of ownership of the financial assets. On derecognition of a financial asset, the difference between the asset's carrying amount and the sum of the consideration received and receivable and the cumulative gain or loss that had been recognized directly in equity is recognized in profit or loss.

For financial liabilities, they are derecognized when the obligation specified in the relevant contract is discharged, cancelled or expires. The difference between the carrying amount of the financial liability derecognized and the consideration paid and payable is recognized in profit or loss.

4.18 Impairment of non-financial assets

At the end of each reporting period, the Company reviews the carrying amounts of its tangible and intangible assets to determine whether there is an indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss (if any). Where it is not possible to estimate the recoverable amount of an individual asset, the Company estimates the recoverable amount of the cash-generating unit to which the assets belong.

Recoverable amount is the higher of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

If the recoverable amount of an asset (or cash-generating unit) is estimated to be less than its carrying amount, the carrying amount of the asset (or cash-generating unit) is reduced to its recoverable amount. An impairment loss is recognized immediately in the statement of comprehensive income.

Where an impairment loss subsequently reverses, the carrying amount of the asset (cash-generating unit) is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognized for the asset (or cash-generating unit) in prior years.

4.19 Cash and cash equivalents

Cash and cash equivalents comprise cash at banks and on hand, and short term money market instruments with an original maturity of three months or less, which are readily convertible into a known amount of cash.

4.20 Revenue recognition

Revenue represents the fair value of consideration received and receivable that are derived from the sales of coal. Sales revenues are recognized when the risks and rewards of ownership pass to the buyer, collection is reasonably assured and the price is reasonably determinable. The revenue from sales of coal in the ordinary course of business is recognized when coal is either loaded onto a truck or when it is unloaded at the final destination, depending on the terms of the contract.

4.21 Provisions

Provisions are recognized when the Company has a present obligation (legal or constructive) that has arisen as a result of a past event and it is probable that a future outflow of resources will be required to settle the obligation, provided that a reliable estimate can be made of the amount of the obligation.

Provisions are measured at the present value of the expenditures expected to be required to settle the obligation using a pre-tax rate that reflects current market assessments of the time value of money and the risk specific to the obligation. The increase in the provision due to passage of time is recognized as interest expense.

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4. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

4.22 Related party transactions

Parties are considered to be related if one party has the ability, directly or indirectly, to control the other party or exercise significant influence over the other party in making financial and operating decisions. Parties are also considered to be related if they are subject to common control, related parties may be individuals or corporate entities. A transaction is considered to be a related party transaction when there is a transfer of resources or obligations between related parties.

4.23 Significant accounting judgments and estimates

The preparation of these financial statements requires management to make judgments and estimates and form assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and reported amounts of revenues and expenses during the reporting period. On an ongoing basis, management evaluates its judgments and estimates in relation to assets, liabilities, revenue and expenses. Management uses historical experience and various other factors it believes to be reasonable under the given circumstances as the basis for its judgments and estimates. Actual outcomes may differ from these estimates under different assumptions and conditions.

The most significant estimates relate to valuation of embedded derivatives and determination of their expected life; asset retirement obligations; property, plant and equipment, including coal reserves and resources, depreciation and depletion; recoverability of trade and other receivables, inventory valuation; valuation of deferred income tax amounts, impairment testing and the calculation of share-based payments.

The most significant judgments relate to recoverability of capitalized amounts, recognition of deferred tax assets and liabilities, determination of the commencement of commercial production and the determination of the economic viability of a project.

5. SEGMENTED INFORMATION

At December 31, 2009, the Company has one reportable operating segment, being the Mongolian Coal Division. In prior periods, the Company's Metals Division and Indonesia Coal Division were segments of the Company (Note 6).

An operating segment is defined as a component of the Company:

- that engages in business activities from which it may earn revenues and incur expenses;
- whose operating results are reviewed regularly by the entity's chief operating decision maker; and
- for which discrete financial information is available.

For the Mongolian Coal Division, the Company receives discrete financial information that is used by the chief operating decision maker to make decisions about resources to be allocated to the segment and to assess its performance. The division is principally engaged in the acquisition, exploration and development of coal properties in Mongolia. As at December 31, 2009, the Mongolian Coal Division has achieved commercial production and is earning revenue through the sale of coal to external customers.

The Company's Corporate Division only earns revenues that are considered incidental to the activities of the Company and therefore does not meet the definition of an operating segment as defined in IFRS 8 *'Operating Segments'*.

At December 31, 2009, the Mongolian Coal Division had three active customers with the largest customer accounting for 65% of trade receivables and the other customers accounting for the remaining 35% of trade receivables. For the year ended December 31, 2009, the largest customer accounted for 64% of revenues and the other customers accounted for the remaining 36% of revenues.

5. SEGMENTED INFORMATION *(continued)*

The following is an analysis of the carrying amounts of segment assets, segment liabilities and reported segment profit or loss, revenues, depreciation and depletion expense and impairment charge on assets analyzed by operating segment and reconciled to the Company's Consolidated Financial Statements:

		Discounted Operations			
	Mongolian Coal Division	Indonesian Coal Division(i)	Metals Division(ii)	Unallocated(iii)	Consolidated Total
Segment assets					
As at December 31, 2009	**$129,454**	**$ –**	**$ –**	**$431,230**	**$560,684**
As at December 31, 2008	76,611	14,836	638	7,863	99,948
As at December 31, 2007	2,509	–	1,132	1,969	5,610
Segment liabilities					
As at December 31, 2009	**7,300**	**–**	**–**	**556,176**	**563,476**
As at December 31, 2008	3,101	811	255	6,817	10,984
As at December 31, 2007	836	–	270	106,335	107,441
Segment (profits)/losses					
For year ended December 31, 2009	**(6,203)**	**31,088**	**–**	**85,920**	**110,805**
For year ended December 31, 2008	25,434	9,690	7,911	26,541	69,576
Segment revenues					
For year ended December 31, 2009	**36,038**	**–**	**–**	**–**	**36,038**
For year ended December 31, 2008	3,126	–	–	–	3,126
Capital expenditures					
For year ended December 31, 2009	**35,706**	**6,511**	**–**	**64**	**42,281**
For year ended December 31, 2008	53,960	481	53	15	54,509
Depreciation and depletion expense					
For year ended December 31, 2009	**5,837**	**–**	**–**	**19**	**5,856**
For year ended December 31, 2008	395	–	54	99	548
Impairment charge on assets					
For year ended December 31, 2009(iv)	**–**	**15,135**	**–**	**–**	**15,135**
For year ended December 31, 2008	–	–	493	–	493

(i) *The Indonesian Coal Division was treated as discontinued operations for the years ended December 31, 2008 and 2009 (Note 6)*
(ii) *The Metals Division was treated as discontinued operations for the years ended December 31, 2008 and 2009 and the assets and liabilities of the Metals Division were reclassified as held for sale as at December 31, 2008 (Note 6)*
(iii) *The unallocated amount contains all amounts associated with the Corporate Division*
(iv) *The impairment charge related to the Indonesia Coal Division is discussed further in Note 6*

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5. SEGMENTED INFORMATION *(continued)*

At December 31, 2009, the Company operates in three geographical areas, being Canada, Hong Kong and Mongolia. Prior to December 23, 2009, the Company had operations in Indonesia (Note 6). The following is an analysis of the revenues and non-current assets by geographical area and reconciled to the Company's Consolidated Financial Statements:

	Mongolia	Indonesia	Hong Kong	Canada	Consoli-dated Total
Revenues					
For year ended December 31, 2009	**$ 36,038**	**$ –**	**$ –**	**$ –**	**$ 36,038**
For year ended December 31, 2008	3,126	–	–	–	3,126
Non-current assets					
As at December 31, 2009	**89,587**	**–**	**49**	**61,876**	**151,512**
As at December 31, 2008	51,939	13,689	–	20	65,648
As at December 31, 2007	1,398	62	–	106	1,566

6. DISCONTINUED OPERATIONS

The loss from discontinued operations is broken down as follows:

	Year ended December 31, 2009	2008
Discontinued operations – Metals Division	**$ –**	$ 7,911
Discontinued operations – Indonesia Coal Division	**31,088**	9,690
Net loss from discontinued operations	**$ 31,088**	$ 17,601
Basic and diluted loss per share from discontinued operations	**$ 0.23**	$ 0.14

6.1 Indonesia Coal Division

The Company sold the Indonesia Coal Division, which is composed entirely of the Mamahak Coal Project ("Mamahak"), effective December 15, 2009. The Company divested its 85% interest in Mamahak to Kangaroo Resources Limited ("Kangaroo") for consideration comprising of $1 million in cash and 50 million shares of Kangaroo with a fair value of $8,776. Kangaroo is listed on the Australian Securities Exchange (KRL: ASX). The transaction was completed on December 23, 2009 and the Company incurred transaction costs of $1 million related to the disposition of Mamahak. As a result of this transaction, the Company held 6.7% of the outstanding shares in Kangaroo on the closing date of the transaction and those shares are subject to a twelve month lock-up.

Based on the terms of the agreement with Kangaroo, the estimated net recoverable value, determined by the estimated fair value of Mamahak less the selling costs, has resulted in an impairment charge of $15,135.

The losses from discontinued operations of the Indonesia Coal Division for the years ended December 31, 2009 and 2008 are as follows:

	Year ended December 31, 2009	2008
Administration expenses	**$ 40**	$ (48)
Evaluation and exploration expenses[(i)]	**15,916**	9,740
Finance costs	**8**	–
Interest income	**(11)**	(2)
Impairment charge on Indonesia Coal Division	**15,135**	–
Net loss from discontinued operations	**$ 31,088**	$ 9,690
Basic and diluted loss per share from discontinued operations	**$ 0.23**	$ 0.08

(i) *Share-based compensation (a non-cash item) of $340 (2008: $102) has been included in Evaluation and exploration expenses*

6. DISCONTINUED OPERATIONS *(continued)*

6.2 Metals Division

The Company sold the Metals Division, effective December 30, 2008 with a closing date of February 2, 2009 to Ivanhoe for $3 million. In addition, Ivanhoe provided the Company with a $30 million credit facility for a one year period (Note 22). Ivanhoe provided the Company with the economic equivalent of a 1% Net Smelter Royalty on the Sulawesi and Kerta Projects in Indonesia. The Metals Division consisted of certain base and precious metals properties in Mongolia and Indonesia. The Company received the proceeds of $3 million in December 2008 and this receipt was reflected in deposits received under current liabilities. The Company has recorded a gain of $2,617 in the year ended December 31, 2009 on the sale of the Metals Division and this gain was recorded directly into equity as the sale of the division was to the parent of the Company.

The Metals Division was presented as a discontinued operation and its financial results were presented as separate items in the Consolidated Statement of Comprehensive Income and Consolidated Statement of Cash Flows. The Metals Division assets and liabilities consolidated by the Company in 2008 were segregated in the Consolidated Statement of Financial Position and classified as assets and liabilities held for sale. Upon the closing of the sale of the Metals Division on February 2, 2009, there was a cash outflow of $223, all other assets and liabilities classified as held for sale as at December 31, 2008 were disposed upon the closing of the sale of the Metals Division.

The losses from discontinued operations of the Metals Division for the year ended December 31, 2008 are as follows:

	Year ended December 31, 2008
Evaluation and exploration expenses[i]	$ 7,418
Impairment of intangible assets	493
Net loss from discontinued operations	$ 7,911
Basic and diluted loss per share from discontinued operations	$ 0.06

(i) *Share-based compensation (a non-cash item) of $nil (2008: $1,491) has been included in Evaluation and exploration expenses*

The carrying values of net assets classified as held for sale as at December 31, 2008 are as follows:

	As at December 31, 2008
ASSETS	
Current assets	
Cash and cash equivalents	$ 223
Trade and other receivables	184
Prepaid expenses and deposits	134
Property, plant and equipment	97
Total current assets classified as held for sale	$ 638
Current liabilities	
Trade and other payables	$ 255
Total current liabilities classified as held for sale	$ 255

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7. COST OF SALES

The cost of sales of the Company is broken down into its cash and non-cash components as follows:

	Year ended December 31,	
	2009	2008
Operating expenses[(i)]	**$ 23,611**	$ 1,863
Depreciation and depletion	**5,814**	314
Cost of sales	**$ 29,425**	$ 2,177

(i) *Share-based compensation (a non-cash item) of $1,590 (2008: $540) has been included in Operating expenses*

8. ADMINISTRATION EXPENSES

The administration expenses for the Company are broken down as follows:

	Year ended December 31,	
	2009	2008
Corporate administration	**$ 2,839**	$ 2,123
Legal	**912**	305
Professional fees	**3,159**	804
Listing fees[(ii)]	**2,470**	6,715
Salaries and benefits[(i)]	**14,024**	5,618
Depreciation	**19**	98
Foreign exchange loss	**1,112**	4,695
Administration expenses	**$ 24,535**	$ 20,358

(i) *Share-based compensation (a non-cash item) of $10,471 (2008: $3,770) has been included in Salaries and benefits*
(ii) *Listing fees of $4,565 were deferred in the year ended December 31, 2009 (Note 15)*

9. EVALUATION AND EXPLORATION EXPENSES

The evaluation and exploration expenses for the Company are broken down as follows:

	Year ended December 31,	
	2009	2008
Mongolian Coal Division[(i)]	**$ 5,399**	$ 26,445
Evaluation and exploration expenses	**$ 5,399**	$ 26,445

(i) *Share-based compensation (a non-cash item) of $134 (2008: $1,335) has been included in Evaluation and exploration expenses*

10. FINANCE COSTS

The finance costs for the Company are broken down as follows:

	Year ended December 31,	
	2009	2008
Fair value change of embedded derivatives in convertible debenture[(iii)]	**$ 44,980**	$ –
Fair value change of embedded derivative in line of credit facility[(ii)]	**–**	7,223
Interest accretion on convertible debenture[(iii)]	**2,972**	–
Interest accretion on line of credit facility[(ii)]	**–**	598
Interest expense on convertible debenture[(iii)]	**4,712**	–
Interest expense on line of credit facilities[(ii)]	**1,651**	149
Transaction costs on issuance of convertible debenture[(iii)]	**9,399**	–
Mark to market gain on investments[(i)]	**(843)**	–
Accretion of asset retirement obligation	**40**	19
Finance costs	**$ 62,911**	$ 7,989

(i) *Further information regarding this charge is disclosed in Note 16*
(ii) *Further information regarding this charge is disclosed in Note 22*
(iii) *Further information regarding this charge is disclosed in Note 23*

11. TAXES

The Company and its subsidiaries in Canada are subject to Canadian federal and provincial tax for the estimated assessable profit for the years ended December 31, 2009 and 2008 at a rate of 30% and 31%, respectively. The Company had no assessable profit in Canada for the years ended December 31, 2009 and 2008.

The Company's subsidiaries in Hong Kong are subject to Hong Kong profits tax for the years ended December 31, 2009 and 2008 at a rate of 16.5%. No Hong Kong profits tax was provided for as the Company had no assessable profit arising in or derived from Hong Kong in the years ended December 31, 2009 and 2008.

The Company's subsidiaries in Mongolia are subject to Mongolian income tax for the years ended December 31, 2009 and 2008 at a rate of 25%. In the year ended December 31, 2009 the Company recorded a current income tax charge of $509 (2008: $nil) related to assessable profit derived from Mongolia.

Taxation from other relevant jurisdictions is calculated at the rates prevailing in each of those jurisdictions respectively.

The tax expense for the Company can be reconciled to the loss for the period per the Consolidated Statement of Comprehensive Income as follows:

	Year ended December 31,	
	2009	2008
Loss from continuing operations before tax	**$ 86,155**	$ 51,975
Loss from discontinued operations before tax	**31,088**	17,601
Loss from operations before tax	**117,243**	69,576
Statutory tax rate	**30.00%**	31.00%
Recovery of income taxes based on combined Canadian federal and provincial statutory rates	**35,173**	21,568
Deduct:		
Lower effective tax rate in foreign jurisdictions	**(992)**	(2,118)
Tax effect of tax losses and temporary differences not recognized	**(1,938)**	(15,712)
Non-deductible expenses	**(22,956)**	(2,902)
Effect of change in future tax rates	**(2,849)**	(836)
Tax recovery for the year	**$ 6,438**	$ –

The Company's recognized deferred income tax assets are as follows:

	As at December 31,		
	2009	2008	2007
Tax loss carry-forwards	**$ 5,793**	$ –	$ –
Property, plant and equipment	**1,135**	–	–
Other assets	**19**	–	–
Total deferred income tax assets	**$ 6,947**	$ –	$ –

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11. TAXES *(continued)*

The Company's unrecognized deferred income tax assets are as follows:

	As at December 31,		
	2009	2008[(i)]	2007
Tax loss carry-forwards	**$ 12,884**	$ 13,732	$ 14,977
Property, plant and equipment	**56**	504	1,075
Share issue costs	**4,902**	687	16
Unrealized foreign exchange losses	**5,582**	2,319	1
Convertible debenture	**–**	–	–
Fair value of embedded derivatives	**–**	–	20,930
Other assets	**1,275**	1,146	1,477
Total unrecognized deferred income tax assets	**$ 24,699**	$ 18,388	$ 38,476

(i) *2008 figures exclude deferred income tax assets associated with assets and liabilities classified as held for sale*

The Company's unrecognized deferred income tax assets associated with assets held for sale as at December 31, 2008 are as follows:

	As at December 31, 2008
Tax loss carry-forwards	$ 3,892
Property, plant and equipment	482
Total deferred income tax assets	$ 4,374

At December 31, 2009 the Company and its subsidiaries have unrecognized capital losses and non-capital losses for income tax purposes of approximately $97,869 (2008: $64,418; 2007: $56,313) that may be used to offset future taxable income as follows:

		As at December 31, 2009		
		Local currency	**U.S. Dollar Equivalent**	Expiry dates
Non-capital losses				
Canadian Dollar	Cdn$	35,922	**$ 34,108**	2010–2029
Mongolian Tugrik	MNT	33,496,611	**29,243**	2010–2020
Singapore Dollar	SGD	48	**34**	indefinite
Hong Kong Dollar	HKD	7,898	**1,018**	indefinite
			$ 64,403	
Capital losses				
Canadian Dollar	Cdn$	35,246	**$ 33,466**	indefinite

12. LOSS PER SHARE

The calculation of basic and diluted loss per share is based on the following data:

	Year ended December 31,	
	2009	2008
Net loss from continuing operations for the purpose of basic and diluted loss per share	**$ 79,717**	$ 51,975
Net loss from discontinued operations for the purpose of basic and diluted loss per share	**$ 31,088**	$ 17,601
Weighted average number of shares for the purpose of basic and diluted loss per share	**133,499**	128,354

The basic loss per share is computed by dividing the net loss by the weighted average number of common shares outstanding during the year. The diluted loss per share reflects the potential dilution of common share equivalents, such as preference shares, outstanding stock options, share purchase warrants and convertible debentures, in the weighted average number of common shares outstanding during the year, if dilutive. All of the stock options and the convertible debenture were anti-dilutive for the years ended December 31, 2009 and 2008.

13. CASH AND CASH EQUIVALENTS

Cash and cash equivalents of the Company are comprised of bank balances and short term money market instruments with an original maturity of three months or less. The Company's bank balances and cash equivalents carry prevailing market interest rates which ranged from 0.10% to 0.30% as at December 31, 2009. The Company's cash and cash equivalents are denominated in the following currencies:

	As at December 31,		
	2009	2008	2007
Denominated in U.S. dollars	**$357,163**	$ 6,126	$ 1,111
Others	**179**	3,991	283
Total cash and cash equivalents	**$357,342**	$ 10,117	$ 1,394

14. TRADE AND OTHER RECEIVABLES

The Company's trade and other receivables arise from two main sources: trade receivables due from customers for coal sales and value added tax ("VAT") and goods and services tax ("GST") receivable due from various government taxation authorities. These are broken down as follows:

	As at December 31,		
	2009	2008	2007
Trade receivables	**$ 5,200**	$ 1,743	$ –
VAT/GST receivable	**7,029**	5,357	720
Other receivables	**99**	190	40
Total trade and other receivables	**$ 12,328**	$ 7,290	$ 760

Below is an aged analysis of the Company's trade and other receivables:

	As at December 31,		
	2009	2008	2007
Less than 1 month	**$ 5,730**	$ 2,034	$ 188
1 to 3 months	**3,463**	443	300
3 to 6 months	**2,613**	1,705	272
Over 6 months	**522**	3,108	–
Total trade and other receivables	**$ 12,328**	$ 7,290	$ 760

At December 31, 2009, 91% of the trade and other receivables that were outstanding over one month are VAT/GST receivables and 100% of the trade and other receivables that were outstanding over six months are VAT/GST receivables. The Company anticipates full recovery of these amounts and therefore no impairment has been recorded against these receivables. The credit risk on the GST/VAT receivable has been further discussed in Note 29.

The Company holds no collateral for any receivable amounts outstanding as at December 31, 2009.

Included in trade and other receivables of the Company are amounts due from related parties which are disclosed in Note 30. The amounts are unsecured, interest free and repayable upon written notice given from the Company.

15. DEFERRED LISTING COSTS

The deferred listing costs consist of legal, accounting and professional fees related to equity fundraising through an international offering of shares ("international offering") (Note 35.1) and a simultaneous secondary listing on the Hong Kong Stock Exchange ("HKEX"). The Company had previously expensed all costs associated with the international offering due to the liquidity issues in the credit markets, along with the increased cost of obtaining capital and the reduced availability of equity funding. However, in the fourth quarter of 2009, the Company achieved significant milestones that provided evidence that the Company would successfully be able to raise equity through the international offering and that the secondary listing would be completed. The Company deferred listing costs that were incurred after the achievement of those milestones.

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15. DEFERRED LISTING COSTS *(continued)*

On January 29, 2010, the Company successfully concluded the international offering and began trading on the HKEX (Note 35.1). The deferred listing costs as at December 31, 2009 of $4,565 and additional listing costs incurred until the completion date of the international offering will be offset against the net proceeds from the international offering as share issue costs.

16. INVESTMENTS

The Company's investments are broken down as follows:

	As at December 31,		
	2009	2008	2007
Short term investments			
Money market investments[i]	**$ 14,999**	$ –	$ –
Long term investments			
Investment in Kangaroo Resources[iii]	**9,876**	–	–
Money market investments[ii]	**47,194**	–	–
	57,070		
Total investments	**$ 72,069**	$ –	$ –

(i) *Money market investments with original maturities greater than ninety days and less than one year*
(ii) *Money market investments with original maturities greater than one year*
(iii) *For more information regarding this investment see Note 6.1*

17. INVENTORIES

The Company's inventories are broken down as follows:

	As at December 31,		
	2009	2008	2007
Stockpiles[i]	**$ 9,553**	$ 13,158	$ –
Materials and supplies	**6,831**	519	–
Total inventories	**$ 16,384**	$ 13,677	$ –

(i) Coal inventories are stated at production cost

The amount of inventories recognized as an expense during the year ended December 31, 2009 is $22,035 (2008: $1,212). As at December 31, 2009, the Company anticipates the entire stockpiles balance of $9,553 will be realized within twelve months.

18. PREPAID EXPENSES AND DEPOSITS

The prepaid expenses and deposits for the Company are broken down as follows:

	As at December 31, 2009	2008	2007
Security deposits	**$ 619**	$ 532	$ 335
Insurance	**557**	234	71
Prepaid exploration license costs	**1,023**	1,111	1,209
Prepaid income taxes	**3,109**	–	–
Vendor pre-payments	**2,683**	609	–
Other	**128**	92	275
Total prepaid expenses and deposits	**$ 8,119**	$ 2,578	$ 1,890

19. INTANGIBLE ASSETS

The following table shows the Company's cumulative expenditures made as of December 31, 2008 and December 31, 2009:

	Mineral properties– Indonesian Coal Division	Mineral properties– Metals Division	Total
Balance, as at January 1, 2007	$ –	$ 443	$ 443
Additions	–	–	–
Depletion	–	–	–
Balance, as at December 31, 2007	–	443	443
Additions	13,208	50	13,258
Depletion	–	–	–
Impairment	–	(493)	(493)
Balance, as at December 31, 2008	13,208	–	13,208
Sale of Indonesia Coal Division (Note 6)	**(13,208)**	**–**	**(13,208)**
Balance, as at December 31, 2009	**$ –**	**$ –**	**$ –**

The Company held an interest in the Mamahak Coal project in East Kalimantan, Indonesia. The Joint Venture Earn-in Agreement with Score Resources Ltd. ("Score") included a provision allowing for the Company to increase its working interest position based on a predetermined pricing mechanism. In 2008, the Company elected to increase its working interest from 56% to 85% by paying Score $13,208, comprised of $8,014 cash and $5,168 settled by 320 common shares of the Company at Cdn$16.15 per share as specified in the agreement with Score. The Company disposed of Mamahak on December 15, 2009 (Note 6.1).

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20. PROPERTY, PLANT AND EQUIPMENT

The Property, plant and equipment for the Company is broken down as follows:

	Mobile equipment	Computer equipment	Furniture and fixtures	Machinery and equipment	Buildings and roads	Mineral assets	Con-struction in progress	Total
Cost								
As at January 1, 2007	$ 203	$ 195	$ 62	$ 108	$ –	$ –	$ 150	$ 718
Additions	152	179	81	215	–	–	235	862
Disposals	(44)	–	(14)	–	–	–	–	(58)
As at December 31, 2007	311	374	129	323	–	–	385	1,522
Additions	38,283	272	32	1,908	433	3,422	11,026	55,376
Disposals	(50)	(120)	(68)	(20)	–	–	–	(258)
As at December 31, 2008	38,544	526	93	2,211	433	3,422	11,411	56,640
Additions	**28,900**	**98**	**409**	**538**	**1,663**	**5,669**	**6,225**	**43,502**
Disposals	**(756)**	**(37)**	**(7)**	**(125)**	**–**	**–**	**(7)**	**(932)**
Sale of Indonesia Coal Division (Note 6)	**–**	**–**	**–**	**–**	**(1,820)**	**(3,006)**	**(2,738)**	**(7,564)**
Reclassifications	**–**	**–**	**4**	**598**	**13,318**	**–**	**(13,920)**	**–**
As at December 31, 2009	**$ 66,688**	**$ 587**	**$ 499**	**$ 3,222**	**$ 13,594**	**$ 6,085**	**$ 971**	**$ 91,646**
Accumulated depreciation								
As at January 1, 2007	$ (60)	$ (95)	$ (11)	$ (57)	$ –	$ –	$ –	$ (223)
Charge for the year	(70)	(42)	(3)	(62)	–	–	–	(177)
Eliminated on disposals	–	–	1	–	–	–	–	1
As at December 31, 2007	(130)	(137)	(13)	(119)	–	–	–	(399)
Charge for the year	(3,465)	(204)	(23)	(68)	(77)	(85)	–	(3,922)
Eliminated on disposals	11	84	17	9	–	–	–	121
As at December 31, 2008	(3,584)	(257)	(19)	(178)	(77)	(85)	–	(4,200)
Charge for the period	**(4,003)**	**(76)**	**(57)**	**(405)**	**(834)**	**(85)**	**–**	**(5,460)**
Eliminated on disposals	**613**	**34**	**4**	**–**	**–**	**–**	**–**	**651**
Sale of Indonesia Coal Division (Note 6)	**–**	**–**	**–**	**–**	**28**	**40**	**–**	**68**
As at December 31, 2009	**$ (6,974)**	**$ (299)**	**$ (72)**	**$ (583)**	**$ (883)**	**$ (130)**	**$ –**	**$ (8,941)**
Net book value								
As at December 31, 2007	$ 181	$ 237	$ 116	$ 204	$ –	$ –	$ 385	$ 1,123
As at December 31, 2008	$ 34,960	$ 269	$ 74	$ 2,033	$ 356	$ 3,337	$ 11,411	$ 52,440
As at December 31, 2009	**$ 59,714**	**$ 288**	**$ 427**	**$ 2,639**	**$ 12,711**	**$ 5,955**	**$ 971**	**$ 82,705**

21. TRADE AND OTHER PAYABLES

Trade and other payables of the Company are principally comprised of amounts outstanding for trade purchases relating to coal mining and exploration activities and amounts payable for financing activities. The usual credit period taken for trade purchases is between 30 to 90 days.

The following is an aged analysis of the trade and other payables:

	As at December 31,		
	2009	2008	2007
Less than 1 month	**$ 9,630**	$ 4,723	$ 76
1 to 3 months	**892**	1,960	198
3 to 6 months	**705**	701	210
Over 6 months	**1,442**	16	1,284
Total trade and other payables	**$ 12,669**	$ 7,400	$ 1,768

Included in trade and other payables are amounts due to related parties which are disclosed in Note 30.

22. LINE OF CREDIT FACILITIES

The movement of all the amounts due under the various line of credit facilities is as follows:

	First funding agreement	Second funding agreement	Ivanhoe credit facility	Bank line of credit	Total
Balance, as at January 1, 2007	$ 5,836	$ –	$ –	$ –	$ 5,836
Amounts advanced	22,712	6,000	–	–	28,712
Interest expense	1,307	51	–	–	1,358
Interest accretion	6,481	–	–	–	6,481
Fair value change on embedded derivative	63,286	–	–	–	63,286
Balance, as at December 31, 2007	99,622	6,051	–	–	105,673
Amounts advanced	–	2,000	–	–	2,000
Interest expense	108	26	–	–	134
Interest accretion	598	–	–	–	598
Fair value change on embedded derivative	7,223	–	–	–	7,223
Repayment of line of credit facility	–	(8,077)	–	–	(8,077)
Conversion of line of credit facility	(107,551)	–	–	–	(107,551)
Balance, as at December 31, 2008	–	–	–	–	–
Amounts advanced	**–**	**–**	**50,000**	**3,000**	**53,000**
Interest expense	**–**	**–**	**1,642**	**9**	**1,651**
Repayment of line of credit facility	**–**	**–**	**(51,642)**	**–**	**(51,642)**
Balance, as at December 31, 2009	**$ –**	**$ –**	**$ –**	**$ 3,009**	**$ 3,009**

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22. LINE OF CREDIT FACILITIES *(continued)*

The amounts due under the line of credit facilities are further broken down as follows:

	As at December 31,		
	2009	2008	2007
First funding agreement			
Debt host	**$ –**	$ –	$ 7,657
Interest payable	**–**	–	1,486
Interest accretion on line of credit facility	**–**	–	6,481
Fair value of embedded derivative	**–**	–	83,998
	–	–	99,622
Second funding agreement			
Principal amount	**–**	–	6,000
Interest payable	**–**	–	51
	–	–	6,051
Ivanhoe credit facility			
Principal amount	**–**	–	–
Interest payable	**–**	–	–
	–	–	–
Bank line of credit			
Principal amount	**3,000**	–	–
Interest payable	**9**	–	–
	3,009	–	–
Amounts due under line of credit facilities	**$ 3,009**	$ –	$105,673
Financial statement presentation			
CURRENT LIABILITIES			
Amounts due under line of credit facilities	**$ 3,009**	$ –	$ –
NON-CURRENT LIABILITIES			
Amounts due under line of credit facilities	**–**	–	105,673
	$ 3,009	$ –	$105,673

22.1 First funding agreement

In April 2006, the Company entered into a line of credit facility (the "first funding agreement") with Ivanhoe, whereby Ivanhoe agreed to make available to the Company an unsecured line of credit facility of up to $10 million which was extended to a maximum of $15 million, excluding interest and the interim coal expenditures.
All amounts outstanding under the line of credit bore interest at the three month London Interbank Offered Rate ("LIBOR") plus 200 basis points. In May 2007, the Company completed the purchase of the Ivanhoe coal division (Note 31) in consideration for the issuance to Ivanhoe of 57,000 common shares and 25,576 preferred shares of the Company. The first funding agreement became convertible into common shares at the election of either the Company or Ivanhoe. Until May 29, 2008, the Company had the right to require Ivanhoe to convert the outstanding amounts under the first funding agreement into common shares at a conversion price of Cdn$2.09 per share. Until August 29, 2008, Ivanhoe had the right to convert the outstanding amounts under the first funding agreement into common shares at a conversion price of Cdn$2.35 per share.

On January 23, 2008, Ivanhoe converted 25,576 preferred shares, the total sum of preferred shares held by Ivanhoe, into common shares of the Company on a one-for-one basis. At the Company's request, Ivanhoe also converted $29,983 of debt into 14,709 common shares of the Company. As a result of this conversion, the amounts due under the line of credit facility owed to Ivanhoe on the first funding agreement were eliminated. The conversion feature was considered an embedded derivative and this feature has been discussed further in Note 22.5.

22. LINE OF CREDIT FACILITIES *(continued)*

22.2 Second funding agreement

In October 2007, Ivanhoe and the Company entered into a second interim funding agreement (the "second funding agreement"). The second funding agreement provided for an additional unsecured non-convertible line of credit facility of up to $32.5 million. All amounts outstanding under the line of credit bore interest at LIBOR plus 330 basis points.

On January 18, 2008, funds in the amount of $8,077 were paid to Ivanhoe representing repayment in full of the principal of $8,000 and accrued interest of $77 owing on the second funding agreement. The second funding agreement was then terminated.

22.3 Ivanhoe credit facility

On December 30, 2009, the Company established a credit facility with Ivanhoe ("Ivanhoe credit facility") which allowed the Company to obtain advances from Ivanhoe to a maximum of $30 million. The Ivanhoe credit facility is for a term of one year and the Company may request a one year extension. Such an extension shall be at the sole discretion of Ivanhoe. The credit facility is unsecured, non-convertible and carries an interest rate equal to LIBOR plus 750 basis points.

In July 2009, the Company and Ivanhoe agreed to increase the Ivanhoe credit facility from $30 million to $60 million. The amended Ivanhoe credit facility was to mature on December 31, 2010, was unsecured and bore interest at LIBOR plus 750 basis points. The Ivanhoe credit facility also required repayment in the event that the Company acquired additional financing from a third party source and provided for an extension fee of $1.5 million payable in the event any portion of the facility is outstanding past March 31, 2010.

On November 30, 2009, funds in the amount of $51,642 were paid to Ivanhoe representing repayment in full of the principal of $50,000 and accrued interest of $1,642 owing on the Ivanhoe credit facility. The Ivanhoe credit facility was then terminated.

22.4 Bank line of credit

On December 18, 2009, the Company established a line of credit facility with Golomt Bank in Mongolia ("Bank line of credit"). The Bank line of credit facility is a twelve month revolving line of credit facility with a maximum draw-down available of $3 million. The facility bears interest at 13% per annum and is secured by equipment in Mongolia to a value of not less than 150% of the total facility amount.

The Bank line of credit facility will be used by the Company's Mongolian subsidiaries as part of their working capital management. At December 31, 2009 the Company had received advances of $3,000 against the Bank line of credit and has accrued interest expense of $9 for the year ended December 31, 2009.

22.5 Embedded derivative

The Company accounted for any amounts drawn on the first funding agreement (Note 22.1) from April 26, 2006 to May 1, 2007, as a liability recorded at amortized cost. On May 29, 2007, the entire indebtedness became convertible into ordinary shares of the Company at the election of either Ivanhoe or the Company. Until May 29, 2008, the Company had the right to require Ivanhoe to convert the outstanding loan into common shares at a conversion price of Cdn$2.09 per share. Until August 29, 2008, Ivanhoe had the right to convert the outstanding loan into common shares at a conversion price of Cdn$2.35 per share.

On January 23, 2008, at the Company's request, Ivanhoe converted $29,963 of debt into 14,709 common shares of the Company. As a result of this conversion the amount due under the convertible line of credit facility was eliminated.

At the date of conversion, the fair value of the embedded derivative and the debt outstanding was $107,551 which was converted and recorded as share capital. All preferred shares were also converted to common shares on that date.

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22. LINE OF CREDIT FACILITIES *(continued)*

22.5 Embedded derivative *(continued)*

The Company identified that the conversion feature was an embedded derivative to be presented as a liability due to the variable number of shares that would be issued on conversion. This resulted from the debt being denominated in U.S. dollar but being convertible at a fixed conversion rate into Canadian dollar denominated shares.

The debt that was recorded prior to May 1, 2007, was recorded at face value as a liability at amortized cost. On May 1, 2007, the conversion feature was considered to have a value and was recorded at fair value in addition to the value of the previously recorded debt. All subsequent advances on the line of credit were valued at fair value and the value of the debt host was deemed to be $nil on account of the beneficial feature which exceeded the fair value of the debt. The difference between the host debt component of $nil and the principal amount of the loan outstanding was accreted to income over the remaining term of the debt. At each reporting period, the embedded derivative was fair valued, with the movements recorded in income.

The embedded derivative was valued upon initial measurement and at each drawing date using the Black-Scholes option valuation model. The following variables were used to calculate the impact of the call and put option elements of the embedded derivative. Some amounts below have been stated in Cdn$, all other amounts are in U.S. dollar.

	Drawn down date					Cumulative at	
	May 10, 2007	May 29, 2007	July 4, 2007	August 21, 2007	October 1, 2007	December 31, 2007	January 23, 2008
Principal and interest borrowed	$ 1,000	$ 13,212	$ 2,000	$ 2,500	$ 2,000	$ 29,855	$ 29,963
Stock price	Cdn$4.81	Cdn$5.00	Cdn$8.00	Cdn$6.20	Cdn$6.68	Cdn$8.90	Cdn$9.45
Dividend yield	0%	0%	0%	0%	0%	0%	0%
Call option							
Interest rate	4.60%	4.60%	4.68%	4.05%	4.21%	3.93%	3.41%
Volatility	76.19%	76.19%	77.15%	76.62%	70.49%	58.66%	59.89%
Exercise price	Cdn$2.35	Cdn$2.35	Cdn$2.35	Cdn$2.35	Cdn$2.35	Cdn$2.35	Cdn$2.35
Expected life (years)	0.91	0.91	1.16	1.02	0.91	0.66	0.60
Put option							
Interest rate	4.61%	4.61%	4.68%	4.05%	4.21%	3.91%	3.41%
Volatility	76.19%	76.19%	77.15%	75.09%	75.76%	50.58%	55.06%
Exercised price	Cdn$2.09	Cdn$2.09	Cdn$2.09	Cdn$2.09	Cdn$2.09	Cdn$2.09	Cdn$2.09
Expected life (years)	0.91	0.91	0.81	0.77	0.66	0.41	0.35
Net embedded derivative	$ 1,185	$ 15,657	$ 4,893	$ 4,280	$ 3,788	$ 83,998	$ 91,222

As at December 31, 2007, $63,267 had been recorded as a charge against income within finance costs relating to the movement in fair value of the embedded derivative. At the elimination of the debt on January 23, 2008, the fair value of the embedded derivative was $91,203 and $7,223 had been recorded as a charge against income within finance costs in the year ended December 31, 2008. The debt host was recorded at fair value, with the difference between the cost and the principal amount being accreted as interest charges over the term of the debt. The total accretion expense recorded as interest cost to January 23, 2008 was $6,481.

23. CONVERTIBLE DEBENTURE

On November 19, 2009, the Company issued a convertible debenture to a wholly owned subsidiary of the China Investment Corporation ("CIC") for $500 million, which is secured and bears interest at 8.0% with a maximum term of 30 years. The financing is required primarily to support the accelerated investment program in Mongolia and up to $120 million of the financing may also be used for working capital, repayment of debt due on funding, general and administrative expense and other general corporate purposes.

23. CONVERTIBLE DEBENTURE *(continued)*

The key commercial terms of the financing include:

- Interest – 8% per annum (6.4% payable semi-annually in cash and 1.6% payable annually in the Company's shares, where the number of shares to be issued is calculated based on the 50-day volume-weighted average price ("VWAP").
- Term – Maximum of 30 years.
- Security – First charge over the Company's assets, including shares of its material subsidiaries.
- Conversion price – The conversion price is set as the lower of Cdn$11.88 or the 50-day VWAP at the date of conversion, with a floor price of Cdn$8.88 per share.
- Conversion timing – The Company and CIC each have various rights to call conversion of the debenture into common shares. CIC has the right to convert the debenture, in whole or in part, into common shares twelve months after the date of issue. The Company has the right to call for the conversion of up to $250 million of the debenture on the earlier of twenty four months after the issue date, if the conversion price is greater than Cdn$10.66, or upon the Company achieving a public float of 25% of its common shares under certain agreed circumstance, if the conversion price is greater than Cdn$10.66.
- Company's normal conversion right – After sixty months from the issuance date, at any time that the conversion price is greater than Cdn$10.66, the Company will be entitled to require conversion of the outstanding convertible debenture, in whole or in part, into common shares at the conversion price.
- Representation on the Company's Board – While the debenture loan is outstanding, or while CIC has a minimum 15% direct or indirect stake in the Company, CIC has the right to nominate one director to the Company's Board. The Company currently has eight Board members.
- Voting restriction – CIC has agreed that it will not have any voting rights in the Company beyond 29.9% if CIC ever acquires ownership of such a shareholder stake through exercising the debenture.
- Pre-emption rights – While the debenture loan is outstanding, or while CIC has a 15% direct or indirect stake in the Company, CIC has certain pre-emption rights on a pro-rata basis to subscribe for any new shares to be allotted and issued by the Company for the period which the debenture is outstanding. The pre-emption rights will not apply to new shares issued pursuant to pro-rata public equity offerings made to all shareholders, exercise of stock options and shares issued to achieve a 25% public float.
- Right of first offer – While a portion of the debenture is outstanding, or while CIC has a 15% direct or indirect stake in the Company, CIC has the right of first offer for any direct and indirect sale of Ivanhoe's ownership stake in the Company. At December 31, 2009 Ivanhoe owned directly and indirectly approximately 79% of the Company's issued and outstanding shares.
- Registration Rights – CIC has registration rights under applicable Canadian provincial securities laws in connection with the common shares issuable upon conversion of the debenture.

The Company identified that the convertible debenture is a debt host contract to be presented as a liability and contains no equity components. The Company also concluded that the convertible debenture is a hybrid instrument, containing a debt host component and three embedded derivatives – the investor's conversion option, the issuer's conversion option and the equity based interest payment provision (the 1.6% share interest payment) (the "embedded derivatives"). The debt host component is classified as other financial liabilities (Note 29.1) and will be measured at amortized cost using the effective interest rate method and the embedded derivatives are classified as FVTPL (Note 29.1) and all changes in fair value will be recorded in income. The difference between the host debt component and the principal amount of the loan outstanding will be accreted to income over the expected life of the convertible debenture.

The embedded derivative was valued upon initial measurement and at December 31, 2009 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. Some of the key inputs used by the Company in its Monte Carlo simulation included: the floor and ceiling conversion prices, the risk-free rate of return, expected volatility of the stock price, forward foreign exchange rate curves (between the Cdn$ and U.S.$) and spot foreign exchange rates.

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23. CONVERTIBLE DEBENTURE *(continued)*

Based on the Company's valuation as at November 19, 2009, the closing date of the convertible debenture, the value of the embedded derivatives was $313,292 and the value of the debt component was $186,708. The transaction costs of $15,000 were applied on a pro-rata basis to the debt host and embedded derivatives and transaction costs of $9,399 associated with the embedded derivatives were expensed as financing costs and transaction costs of $5,601 associated with the debt host were netted against the debt host component.

Based on the Company's valuation model as at December 31, 2009, the fair value of the embedded derivatives had increased by $44,980 which was expensed as financing costs for the year ended December 31, 2009. In the year ended December 31, 2009, the Company also recorded an accretion expense of $2,972 related to the debt host component of the convertible debenture and an interest expense of $4,712 related to the convertible debenture. To calculate the accretion the Company used an expected life of 30 years.

The assumptions used in Monte Carlo valuation models as at December 31, 2009 and November 19, 2009 are as follows:

	As at December 31, 2009	As at November 19, 2009
Floor conversion price	**Cdn$8.88**	Cdn$8.88
Ceiling conversion price	**Cdn$11.88**	Cdn$11.88
Expected volatility[(i)]	**75%**	80%
Risk-free rate of return	**4.09%**	3.92%
Foreign exchange spot rate (U.S.$ to Cdn$)	**0.96**	0.94
Forward foreign exchange rate curve (U.S.$ to Cdn$)	**0.90–0.95**	0.90–0.94

(i) *Expected volatility has been based on historical volatility of the Company's publicly traded shares*

The movement of all the amounts due under the convertible debenture is as follows:

Balance, as at December 31, 2007 and December 31, 2008	$ –
Amounts advanced	**500,000**
Transaction costs	**(5,601)**
Accrued interest payable	**4,712**
Interest accretion	**2,972**
Fair value change on embedded derivatives	**44,980**
Balance, as at December 31, 2009	**$547,063**

The amounts due under the convertible debenture are further broken down as follows:

	As at December 31, 2009
Debt host	**$184,079**
Fair value of embedded derivatives	**358,272**
Interest payable	**4,712**
Convertible debenture	**$547,063**
Financial Statement Presentation	
CURRENT LIABILITIES	
Current portion of convertible debenture	**$ 4,712**
NON-CURRENT LIABILITIES	
Convertible debenture	**542,351**
Convertible debenture	**$547,063**

24. ASSET RETIREMENT OBLIGATION

Reclamation and closure costs have been estimated based on the Company's interpretation of current regulatory requirements and have been measured at fair value. Fair value is determined based on the net present value of future cash expenditures upon reclamation and closure. Reclamation and closure costs are capitalized into PPE dependant on the nature of the asset related to the obligation and amortized over the life of the related asset.

At December 31, 2009, the asset retirement obligations relate to reclamation and closure costs of the Company's Ovoot Tolgoi project in Mongolia.

The asset retirement obligations at Ovoot Tolgoi are calculated as the net present value of estimated future net cash outflows of the reclamation and closure costs, which at December 31, 2009 total $3,449 and are required to satisfy the obligations, discounted at 10.78% per annum. The settlement of the obligations will occur through to 2024.

The following is an analysis of the asset retirement obligation:

Balance, as at December 31, 2007	$ –
Additions	310
Accretion	19
Balance, as at December 31, 2008	329
Additions	**366**
Accretion	**40**
Balance, as at December 31, 2009	**$ 735**

25. SHARE CAPITAL

25.1 Issued and outstanding capital

The Company has authorized an unlimited number of common and preferred shares with no par value. Below is an analysis in the movement of the issued and outstanding common and preferred shares.

	Common shares		Preferred shares	
	Number of shares	Amount	Number of shares	Amount
Balance, as at January 1, 2008	74,933	$ 30,230	25,576	$ 4,189
Shares issued for:				
Cash	16,211	139,642	–	–
Share issue costs	–	(3,303)	–	–
Mineral properties	322	5,198	–	–
Conversion of line of credit	14,709	107,552	–	–
Conversion of preferred shares	25,576	4,189	(25,576)	(4,189)
Exercise of stock options	1,442	6,004	–	–
Balance, as at December 31, 2008	133,193	$289,512	–	$ –
Shares issued for:				
Exercise of stock options	**1,324**	**$ 6,907**	**–**	**$ –**
Balance, as at December 31, 2009	**134,517**	**$296,419**	**–**	**$ –**

The weighted average share price during the year ended December 31, 2009 was Cdn$12.09 (2008: Cdn$11.15).

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25. SHARE CAPITAL *(continued)*

25.2 Preferred shares

On May 29, 2007, upon completion of the coal transaction (Note 31), the Company issued 25,576 preferred shares to Ivanhoe. Each preferred share issued to Ivanhoe was convertible into one common share but only if, upon any such conversion, the total number of common shares held by Ivanhoe and all other insiders of the Company or any of their respective associates or affiliates did not exceed 90% of the total number of common shares then issued and outstanding. The preferred shares were non-voting and had a preference over the common shares with respect to the payment of dividends and distribution of assets in the event of a liquidation, dissolution or winding up of the Company.

On January 23, 2008, Ivanhoe converted 25,576 preferred shares into common shares of the Company on a one to one basis. The Company has no outstanding preferred shares at December 31, 2009.

26. SHARE-BASED PAYMENTS

26.1 Stock option plan

The Company has a stock option plan which permits the Board of Directors of the Company to grant options to acquire common shares of the Company at the volume weighted average closing price for the five days preceding the date of grant. The Amended Equity Incentive Plan, approved on May 29, 2007, provides for a rolling rather than a fixed maximum number of common shares which may be issued pursuant to incentive stock options and other equity incentives, awards and issuances. The Compensation and Benefits Committee determines and makes recommendations to the Board of Directors as to the recipients of, and nature and size of, share-based compensation awards in compliance with applicable securities law, stock exchange and other regulatory requirements. The Company is authorized to issue options for a maximum of 10% of the issued and outstanding common shares pursuant to the stock option plan.

The stock option plan permits the Board of Directors of the Company to set the terms for each stock option grant, however, the general terms of stock options granted under the amended plan include a maximum exercise period of 5 years and a vesting period of 3 years with one-third of the grant vesting on the first anniversary of the grant, one-third vesting on the second anniversary of the grant and one-third vesting on the third anniversary of the grant. The options granted in the year ended December 31, 2009 were granted with a weighted average maximum exercise period of 5.95 years (2008: 5.00 years) and a weighted average vesting period of 1.82 years (2008: 1.95 years).

During the year ended December 31, 2009, the Company granted 2,671 stock options (2008: 3,184) to officers, employees, directors and other eligible persons at exercise prices ranging from Cdn$7.94 to Cdn$14.25 (2008: Cdn$5.10 to Cdn$18.86) and expiry dates ranging from May 6, 2014 to February 6, 2016 (2008: January 7, 2013 to November 27, 2013). The weighted average fair value of the options issued in the year ended December 31, 2009, was estimated at $5.95 (Cdn$6.56) (2008: $5.96, Cdn$6.31) per option at the grant date using the Black-Scholes option pricing model. The weighted average assumptions used for the calculation were:

	Year ended December 31,	
	2009	2008
Risk free interest rate	**2.17%**	2.81%
Expected life	**3.6 years**	3.5 years
Expected volatility[(i)]	**79.54%**	75.52%
Expected dividend per share	**$nil**	$nil

(i) *Expected volatility has been based on historical volatility of the Company's publicly traded shares*

A share-based compensation cost of $14,872 for the options granted in the year ended December 31, 2009 (2008: $17,623) will be amortized over the vesting period, of which $5,125 was recognized in the year ended December 31, 2009 (2008: $5,008).

The total share-based compensation calculated for the year ended December 31, 2009 was $12,535 (2008: $7,238). Share-based compensation of $10,471 (2008: $3,770) has been allocated to Administration expenses, $1,590 (2008: $540) has been allocated to Cost of sales and $474 (2008: $2,928) has been allocated to Evaluation and exploration expenses.

26. SHARE-BASED PAYMENTS *(continued)*

26.2 Outstanding stock options

The following is a summary of option transactions under the Company's stock option plan:

	Year ended December 31,			
	2009		2008	
	Number of options	Weighted average exercise price (Cdn$)	Number of options	Weighted average exercise price (Cdn$)
Balance, beginning of year	**6,586**	**$ 7.18**	4,995	$ 3.55
Options granted	**2,671**	**11.13**	3,184	11.27
Options exercised	**(1,324)**	**3.16**	(1,442)	2.80
Options forfeited	**(679)**	**9.96**	(151)	15.25
Balance, end of year	**7,254**	**$ 9.11**	6,586	$ 7.18

The following table summarizes information about stock options outstanding and exercisable at December 31, 2009:

	Options Outstanding			Options Exercisable		
Exercise price (Cdn$)	Options outstanding	Weighted-average exercise price (Cdn$)	Weighted-average remaining contractual life (years)	Options outstanding and exercisable	Weighted-average exercise price (Cdn$)	Weighted-average remaining contractual life (years)
$0.86 – $2.85	902	$ 2.16	1.45	902	$ 2.16	1.45
$3.70 – $6.00	2,166	5.57	3.10	1,500	5.78	2.73
$7.16 – $13.80	3,270	11.21	4.55	498	10.68	4.13
$15.07 – $18.86	916	16.82	3.58	333	16.74	3.58
	7,254	$ 9.11	3.61	3,233	$ 6.65	2.68

27. ACCUMULATED DEFICIT AND DIVIDENDS

The Company has incurred losses since inception and at December 31, 2009 the Company has accumulated a deficit of $321,511 (2008: $213,323).

No dividends have been paid or declared by the Company since inception.

28. CAPITAL RISK MANAGEMENT

The Company's objectives are to safeguard the Company's ability to continue as a going concern in order to support the Company's normal operating requirements, continue the development and exploration of its mineral properties and to maintain a flexible capital structure which optimizes the costs of capital at an acceptable risk.

The Company manages its capital structure and makes adjustments to it in light of changes in economic conditions and the risk characteristics of the underlying assets. In order to maintain or adjust the capital structure, the Company may issue new shares, issue new debt, acquire or dispose of assets or adjust the amount of cash and cash equivalents. In order to facilitate the management of its capital requirements, the Company prepares annual expenditure budgets that are updated as necessary depending on various factors, including capital deployment, results from operations, results from the exploration and development of its properties and general industry conditions. The annual and updated budgets are approved by the Board of Directors.

At December 31, 2009, the Company's capital structure consists of convertible debt (Note 23) and the equity of the Company (Note 25). The Company is not subject to any externally imposed capital requirements. In order to maximize ongoing development efforts, the Company does not pay dividends.

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28. CAPITAL RISK MANAGEMENT *(continued)*

In the year ended December 31, 2009, there were no significant changes in the processes used by the Company's or in the Company's objectives and policies for managing its capital. The Company expects that based on the proceeds from the convertible debenture (Note 23) and the net proceeds from the international offering concluded in January 2010 (Note 35.1), sufficient capital resources are available to support further expansion and development of its mining assets.

29. FINANCIAL INSTRUMENTS

Details of the significant accounting policies and methods adopted by the Company for each class of financial asset, financial liability and equity instrument are disclosed in Note 4 of the financial statements.

29.1 Categories of financial instruments

The Company's financial assets and financial liabilities are categorized as follows:

	As at December 31,		
	2009	2008	2007
Financial assets			
Loans and receivables			
Cash and cash equivalents	**$357,342**	$ 10,117	$ 1,394
Trade and other receivables	**12,328**	7,290	760
Other receivables	**225**	–	–
Fair value through profit and loss			
Investment in Kangaroo Resources (Note 16)	**9,876**	–	–
Money market investments (Note 16)	**62,193**	–	–
Total financial assets	**$441,964**	$ 17,407	$ 2,154
Financial liabilities			
Fair value through profit and loss			
Convertible debenture – embedded derivatives (Note 23)	**$358,272**	$ –	$ –
Other financial liabilities			
Trade and other payables	**12,669**	7,400	1,768
Amounts due under line of credit facilities	**3,009**	–	105,673
Convertible debenture – debt host (Note 23)	**188,791**	–	–
Deposit received for sale of Metals Division	**–**	3,000	–
Total financial liabilities	**$562,741**	$ 10,400	$107,441

29.2 Fair value

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 the Company's financial instruments classified as FVTPL are determined as follows:

- The fair value 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 KRL and its money market investments was determined using this methodology.
- The fair value of financial instruments that are not traded in an active market are determined using generally accepted valuation models using inputs that are directly (i.e. prices) or indirectly (i.e. derived from prices) observable. The fair value of the embedded derivatives within the convertible debenture (Note 23) was determined using a Monte Carlo simulation. None of the fair value change on the embedded derivatives for the year ended December 31, 2009 is related to a change in the credit risk of the convertible debenture. All of the change in fair value is associated with changes in market conditions.

29. FINANCIAL INSTRUMENTS *(continued)*

29.2 Fair value *(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.

The following table provides an analysis of the Company's financial instruments that are measured subsequent to initial recognition at fair value, grouped into Level 1 to 3 based on the degree to which the inputs used to determine the fair value are observable.

- Level 1 fair value measurements are those derived from quoted prices in active markets for identical assets or liabilities.
- Level 2 fair value measurements are those derived from inputs other than quoted prices included within Level 1, that are observable either directly or indirectly.
- Level 3 fair value measurements are those derived from valuation techniques that include inputs that are not based on observable market data. As at December 31, 2009, the Company does not have any Level 3 financial instruments.

	As at December 31, 2009		
	Level 1	**Level 2**	**Total**
Financial assets at FVTPL			
Investment in Kangaroo Resources	**$ 9,876**	**$ –**	**$ 9,876**
Money market investments	**62,193**	**–**	**62,193**
Total financial assets at FVTPL	**$ 72,069**	**$ –**	**$ 72,069**
Financial liabilities at FVTPL			
Convertible debenture – embedded derivatives	**$ –**	**$358,272**	**$358,272**

There were no transfers between Level 1 and 2 in the year ended December 31, 2009.

29.3 Financial risk management objectives and policies

The financial risk arising from the Company's operations are currency risk, interest rate risk, credit risk, liquidity risk and commodity price risk. These risks arise from the normal course of operations and all transactions undertaken are to support the Company's ability to continue as a going concern. The risks associated with these financial instruments and the policies on how to mitigate these risks are set out below. Management manages and monitors these exposures to ensure appropriate measures are implemented on a timely and effective manner.

Currency risk

The Company's borrowings, major operating expenses and acquisition costs are denominated in U.S. dollars and a minor portion of the expenses of the Company are in Canadian dollars. The Company's corporate office is based in Canada and the exposure to exchange rate fluctuations arise mainly on foreign currencies against the functional currency of the relevant Company entities which is the U.S. dollar. The Company does not have any significant foreign currency denominated monetary liabilities.

The Company has not entered into any derivative instruments to manage foreign exchange fluctuations; however, management monitors foreign exchange exposure.

The carrying amounts of the Company's foreign currency denominated monetary assets are as follows:

	As at December 31,		
	2009	2008	2007
Assets			
Canadian Dollar	**$ (136)**	$ 3,872	$ 225
Hong Kong Dollars	**262**	–	–
Mongolian Tugriks	**53**	104	6
Indonesian Rupiah	**–**	15	52
	$ 179	$ 3,991	$ 283

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29. FINANCIAL INSTRUMENTS *(continued)*

29.3 Financial risk management objectives and policies *(continued)*

Foreign currency sensitivity analysis

The following table details the Company's sensitivity to a 5% increase or decrease in the U.S. dollar against the foreign currency denominated monetary items in the preceding table. 5% represents management's assessment of the reasonable possible change in foreign exchange rates. The sensitivity analysis includes only outstanding foreign currency denominated monetary items and adjusts their translation at the end of the period for a 5% change in foreign currency rates. A positive number indicates a decrease in loss for the year where the foreign currencies strengthen against the U.S. dollar. The opposite number will result if the foreign currencies depreciate against the U.S. dollar.

	As at December 31,		
	2009	2008	2007
Decrease in			
Loss for the year	**$ 9**	$ 200	$ 14

Interest rate risk

The Company is exposed to interest rate risk on the variable rate of interest earned on some of its short and long term money market investments. The fair value interest rate risk on cash and cash equivalents is insignificant as the deposits are either short-term or pay interest at rates of 1.0% or less.

The Company has not entered into any derivative instruments to manage interest rate fluctuations, however, management closely monitors interest rate exposure and the risk exposure is limited.

Interest rate sensitivity analysis

The following table details the Company's sensitivity to a 50 basis points increase or decrease in the interest rate earned on the Company's money market investments with floating rates of return. 50 basis points represents management's assessment of the reasonable possible change in earned interest rates. The sensitivity analysis assumes the financial instruments outstanding at the end of each reporting period were outstanding throughout the whole year. A positive number indicates an increase in the loss for the year where the interest rate has decreased, while the opposite number will result if the interest rate increased. In prior periods, the Company was exposed to interest rate risk on debt where interest was incurred at a variable rate, at December 31, 2009, the Company has no such debt. In prior periods, the Company had conducted the sensitivity analysis on floating rate debt assuming a 500 basis point increase in the interest rate incurred.

	As at December 31,		
	2009	2008	2007
(Decrease)/increase in			
Loss for the year	**$ (87)**	$ –	$ 1,718

Credit risk

Credit risk is the risk of an unexpected loss if a customer or third party to a financial instrument fails to meet its contractual obligations. Credit risk for the Company is primarily associated with trade receivables, value added tax ("VAT") receivable, goods and services tax ("GST") receivable and cash equivalents and short and long term money market investments.

The credit risk on trade receivables is managed through an internal process whereby any potential customer is investigated before a sales contract is signed. Risk is further mitigated as the payment terms for all customers range from 10 days to 14 days, which allows the Company to actively monitor the amounts owed by customers and identify any credit risks in a timely manner and reduce the risk of a credit related loss. In addition, the Company reviews the recoverable amount of its receivables at the end of each reporting period to ensure that adequate impairment losses are made for unrecoverable amounts. In this regard, the Company considers that the credit risk associated with trade receivables is significantly reduced.

29. FINANCIAL INSTRUMENTS *(continued)*

29.3 Financial risk management objectives and policies *(continued)*

Credit risk *(continued)*

The VAT/GST receivable includes amounts that have been accumulated to date in various subsidiaries. At December 31, 2009, 98% of the VAT/GST receivable was due from the Mongolian Government Taxation Authority. As per Mongolia tax laws, a tax payer may offset future taxes and royalties payable to the Government against VAT amounts receivable from the Government. In the fourth quarter of 2009, based on a request from the Mongolian tax office, the Company was requested to reclass $3,111 from VAT receivable to prepaid taxes to offset future current income tax payments. In the year ended December 31, 2009, the Company also offset current income taxes owing of $509 against its VAT receivable balance. In July 2009, the Mongolia Tax Laws were amended to preclude producers and exporters of unfinished mineral products from claiming back VAT. The Mongolian Government has yet to define what products will qualify as finished mineral products and any VAT amounts impacted will be prospective from the effective date of the law, August 16, 2009. Based on currently available information, the Company anticipates full recoverability of amounts due on account. Verification by the Mongolian Government Taxation Authority of the collectability of the funds is conducted on an annual basis and any outstanding VAT receivable amounts at December 31, 2009, except those possibly impacted by the law change, will be available to the Company to offset future taxes and royalties or will be refunded by the Mongolian Government Taxation Authority.

The credit risk on cash equivalents is limited because the cash equivalents and short and long term money market investments are composed of money market investments issued by banks and other institutions with high credit ratings as assigned by international credit-rating agencies.

The Company is not exposed to significant credit risk and overall the Company's credit risk has not changed significantly during the year ended December 31, 2009.

Liquidity risk

Liquidity risk is the risk that the Company will not be able to settle or manage its obligations associated with financial liabilities. In the management of liquidity risk, the Company maintains a balance between continuity of funding and the flexibility through the use of borrowings. Management closely monitors the liquidity position and expects to have adequate sources of funding to finance the Company's projects and operations. The directors of the Company are of the opinion that, taking into account the Company cash reserves and external financial resources, the Company has sufficient working capital for its present obligations, that is for at least the next twelve months commencing from December 31, 2009.

The following table details the Company's and the Company's expected remaining contractual maturities for its financial liabilities with agreed repayment periods. The table is based on the undiscounted cash flows of financial liabilities based on the earliest date on which the Company can be required to satisfy the liabilities.

	0 to 6 months	6 to 12 months	1 to 5 years	Total
As at December 31, 2007				
Trade and other payables	$ 1,768	$ –	$ –	$ 1,768
Amounts due under line of credit facilities[i]	–	–	24,095	24,095
	$ 1,768	$ –	$ 24,095	$ 25,863
As at December 31, 2008				
Trade and other payables	$ 7,400	$ –	$ –	$ 7,400
	$ 7,400	$ –	$ –	$ 7,400
As at December 31, 2009				
Trade and other payables	**$ 12,669**	**$ –**	**$ –**	**$ 12,669**
Amounts due under line of credit facilities	**170**	**3,206**	**–**	**3,376**
Convertible debenture – cash interest (Note 23)	**–**	**21,874**	**64,000**	**85,874**
	$ 12,839	**$ 25,080**	**$ 64,000**	**$101,919**

(i) *Amount shown at amortized cost using a weighted average interest rate of 6.7%*

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29. FINANCIAL INSTRUMENTS *(continued)*

29.3 Financial risk management objectives and policies *(continued)*

Commodity price risk

Profitability of the Company depends on the coal prices it is able to realize. Coal prices are affected by numerous factors such as interest rates, exchange rates, inflation or deflation and global and regional supply and demand.

The Company enters into sales contracts with its customers to manage the risk of a significant decrease in the price of coal. The Company has not entered into any coal hedging instruments to manage its exposure to fluctuations in coal prices. As coal sales are the only source of revenue for the Company, a 5% increase or decrease in coal prices will result in a corresponding increase or decrease in revenue.

30. RELATED PARTY TRANSACTIONS

The financial statements include the financial statements of SouthGobi Energy Resources Ltd. and its subsidiaries listed in the following table:

		% equity interest		
		As at December 31,		
Name	Country of incorporation	**2009**	2008	2007
Asia Gold International Holding Company Ltd.	British Virgin Islands	**100%**	100%	100%
SouthGobi Energy Resources (Hong Kong) Ltd.	Hong Kong	**100%**	–	–
Dayarbulag LLC	Mongolia	**100%**	100%	100%
SouthGobi Sands LLC	Mongolia	**100%**	100%	100%
Transbaikal Gold	Russia	**100%**	100%	100%
SGQ Coal Investment Pte. Ltd.	Singapore	**100%**	100%	100%
SGQ Dayarcoal Mongolia Pte. Ltd.	Singapore	**100%**	100%	100%
PT Multi Mamahak Batubara	Indonesia	**–**	85%	–
Arkadia Indonesia Holding Company Ltd.	British Virgin Islands	**–**	100%	100%
Bacan Holding Company Ltd.	British Virgin Islands	**–**	100%	100%
Ivanhoe Coal Holding Company Ltd.	British Virgin Islands	**–**	–	100%
Mongolia Holding Company Ltd.	British Virgin Islands	**–**	100%	100%
Ivanhoe Resources Ltd.	Canada	**–**	–	100%
PT AGC Indonesia	Indonesia	**–**	100%	100%
PT ASG Harita Mining Services	Indonesia	**–**	85%	85%
Asia Gold Mongolia LLC	Mongolia	**–**	100%	100%
Bacan Indonesia Holding Company Pte. Ltd.	Singapore	**–**	100%	100%
SGQ Batubara (A) Pte. Ltd.	Singapore	**–**	85%	–
SGQ Indonesia Holding Company Pte. Ltd.	Singapore	**–**	100%	100%
SGQ Mongolia Holding Ltd.	Singapore	**–**	100%	100%
SGQ Singapore Investment Company Pte. Ltd.	Singapore	**–**	100%	100%
SGQ Singapore Projects Holding Company Pte. Ltd.	Singapore	**–**	100%	100%

30. RELATED PARTY TRANSACTIONS *(continued)*

30.1 Related party expenses

The Company incurred the following expenses with Ivanhoe, I2MS.NET PTE LTD ("I2MS") and Global Mining Management ("GMM"), companies related by way of directors or shareholders in common. As at December 31, 2009, Ivanhoe owned approximately 79% of the outstanding common shares of the Company. Below is an analysis of the Company's related party expenses:

	Year ended December 31,	
	2009	2008
Corporate administration	**$ 1,176**	$ 1,893
Salaries and benefits	**1,321**	1,824
Interest (Note 22)	**1,642**	134
Total related party expenses	**$ 4,139**	$ 3,851

The corporate administration and salaries and benefits have been recorded on a cost recovery basis and the interest expense has been recorded on the contractual amount basis.

The breakdown of the expenses between the different related parties is as follows:

	Year ended December 31,	
	2009	2008
GMM	**$ 1,844**	$ 2,455
Ivanhoe	**1,787**	134
I2MS	**508**	1,262
Total related party expenses	**$ 4,139**	$ 3,851

30.2 Related party assets

The assets of the Company include the following amounts due from related parties:

	As at December 31,		
	2009	2008	2007
Amounts due from GMM	**$ 225**	$ –	$ –

30.3 Related party liabilities

The liabilities of the Company include the following amounts due to related parties:

	As at December 31,		
	2009	2008	2007
Amounts due to GMM	**$ 240**	$ 231	$ 211
Accounts payable to Ivanhoe	**158**	61	52
Accounts payable to I2MS	**211**	285	–
Deposit received for sale of Metals Division	**–**	3,000	–
Amounts due under line of credit facilities	**–**	–	105,673
Total liabilities due to related parties	**$ 609**	$ 3,577	$105,936

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

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(expressed in thousands of U.S. Dollars and shares in thousands, unless otherwise indicated)

31. COAL TRANSACTION

In July 2006, the Company and Ivanhoe signed a definitive agreement, effective April 26, 2006, whereby the Company agreed to acquire Ivanhoe's coal division (the "Coal Transaction") in exchange for 57,000 common shares and 25,576 preferred shares of the Company.

On August 8, 2006, the Coal Transaction and the equity conversion rights under the line of credit facility (Note 22) were approved by the Company's minority shareholders at a special meeting convened for that purpose.

The Coal Transaction, which was a related party transaction, received final approval from the TSX Venture Exchange on May 28, 2007.

On May 29, 2007, the Company completed the purchase of the Ivanhoe coal division. The common shares issued to Ivanhoe, when aggregated with Ivanhoe's existing holding of common shares, represented approximately 86% of the total number of common shares currently issued and outstanding. The coal rights and licenses acquired by the Company have been recorded at $nil as the underlying assets had no carrying amount within the coal division.

With the completion of the Coal Transaction, certain coal division expenditures made by Ivanhoe between April 26, 2006 and May 29, 2007 were added to the indebtedness outstanding under the line of credit and will be repayable by the Company as if they were advances. The total coal expenditures funded by Ivanhoe from April 26, 2006 to May 28, 2007, and accepted by the Company, are approximately $13.2 million of which $13 million are related to exploration expenses and $200 are for plant and equipment.

The Coal Transaction is considered a combination between businesses or entities under common control and is therefore exempt from the scope of IFRS 3 *'Business Combinations'*. The Company has accounted for the Coal Transaction using the principles of merger accounting and the prior periods were restated as if the Company and the coal division had always been combined. The coal division consists of certain coal related assets and expenditures made by Ivanhoe from its inception in 2004 to May 29, 2007. Note 3 of the financial statements provides detailed disclosure of the impact of the principles of merger accounting.

32. KEY MANAGEMENT PERSONNEL COMPENSATION

The remuneration of directors and other members of key management were as follows:

	Year ended December 31,	
	2009	2008
Short-term benefits	**$ 1,820**	$ 1,361
Share-based payments	**5,425**	2,504
Total remuneration	**$ 7,245**	$ 3,865

33. SUPPLEMENTAL CASH FLOW INFORMATION

33.1 Non-cash financing and investing activities

The Company incurred the following non-cash investing and financing transactions:

	Year ended December 31,	
	2009	2008
Conversion of line of credit facility (first funding agreement) (Note 22)	**$ –**	$107,552
Conversion of preferred shares to common shares	**–**	4,189
Acquisition of mineral properties through the issue of common shares	**–**	5,198
Transfer of share option reserve upon exercise of options	**3,010**	1,960
Acquisition of shares of KRL (Note 6.1)	**8,776**	–
Total non-cash financing and investing activities	**$ 11,786**	$118,899

33. SUPPLEMENTAL CASH FLOW INFORMATION *(continued)*

33.2 Cash payments for interest and taxes

The Company made the following cash payments for interest and income taxes:

	Year ended December 31, 2009	Year ended December 31, 2008
Interest paid	**$ 1,642**	$ 77
Taxes paid	**–**	–
Total cash payments for interest and taxes	**$ 1,642**	$ 77

34. COMMITMENTS FOR EXPENDITURE

As at December 31, 2009, the Company had the following commitments that have not been disclosed elsewhere in the Consolidated Financial Statements:

	As at December 31, 2009				
	Within 1 year	**2–3 years**	**4–5 years**	**Over 5 years**	**Total**
Capital expenditure commitments	**$ 17,563**	**$ –**	**$ –**	**$ –**	**$ 17,563**
Minimum rental and lease payments	**1,352**	**2,014**	**578**	**–**	**3,944**
Commitments	**$ 18,915**	**$ 2,014**	**$ 578**	**$ –**	**$ 21,507**

35. SUBSEQUENT EVENTS

35.1 International offering

On January 29, 2010, the Company successfully completed an international offering of 27,000 shares for gross proceeds of $437,446. The Company incurred underwriter fees of $17,415 and other share issue costs in association with the international offering. Simultaneously with the international offering the Company's shares began trading on the HKEX under the ticker HKEX: 1878.

35.2 CIC conversion

On March 12, 2010, the Company announced, subject to regulatory approval, a formal request for CIC to convert $250,000 of its convertible debenture (Note 23) into common shares of the Company.

36. APPROVAL OF THE FINANCIAL STATEMENTS

The Consolidated Financial Statements of SouthGobi Energy Resources Ltd. for the year ended December 31, 2009 were approved and authorized for issue by the Board of Directors on March 22, 2010.

APPENDIX TO THE ANNUAL REPORT

DECEMBER 31, 2009

(expressed in thousands of U.S. Dollars and shares in thousands, unless otherwise indicated)

ADDITIONAL STOCK EXCHANGE INFORMATION

Additional information required by the Hong Kong Stock Exchange and not shown elsewhere in this report is as follows:

A1. LOSS FOR THE YEAR

	Year ended December 31, 2009	2008
Loss for the year has been arrived at after charging:		
Auditor's remuneration	**$ 198**	$ 286
Loss on disposal of property, plant and equipment	**245**	6
Depreciation		
Depreciation included in administration expenses	**19**	98
Depreciation included in exploration expenses	**23**	92
Depreciation included in cost of sales	**5,814**	304
Total depreciation included in continuing operations	**5,856**	494
Depreciation included in discontinued operations	**–**	55
Total depreciation	**$ 5,856**	$ 549
Staff costs		
Directors' emoluments (Note A2)	**$ 3,344**	$ 2,219
Other staff costs	**10,660**	3,381
Retirement benefit costs excluding directors	**20**	18
Staff costs in administration expenses	**14,024**	5,618
Staff costs included in exploration expenses	**198**	3,338
Total staff costs	**$ 14,222**	$ 8,956

A2. DIRECTOR AND EMPLOYEE EMOLUMENTS

Directors' emoluments

	Year ended December 31, 2009	2008
Directors' fees	**$ 330**	$ 213
Other emoluments for executive and non-executive directors		
Salaries and other benefits[(i)]	**372**	255
Stock-based compensation	**2,633**	1,745
Retirement benefit contribution	**8**	8
Directors' emoluments	**$ 3,343**	$ 2,221

(i) *Peter Meredith was awarded a bonus of $50 and Alexander Molyneux was awarded a bonus of $315 in light of their activities leading to the successful listing of the Company's shares on the HKEX and related equity financing. For Alexander Molyneux only $103 of the bonus is included herein representing the proportion of time served as a director.*

A2. DIRECTOR AND EMPLOYEE EMOLUMENTS *(continued)*

Directors' emoluments *(continued)*

Name of director	Directors' fees	Salaries and other benefits	Stock-based compen-sation	Retirement benefit contri-bution	Total
Year ended December 31, 2009					
Peter Meredith	**$ –**	**$ 191**	**$ 661**	**$ –**	**$ 852**
Alexander Molyneux[(i)]	**–**	**181**	**522**	**–**	**703**
John Macken	**–**	**–**	**332**	**–**	**332**
Pierre Lebel	**104**	**–**	**229**	**2**	**335**
André Deepwell	**77**	**–**	**225**	**2**	**304**
R. Edward Flood	**29**	**–**	**228**	**1**	**258**
R. Stuart (Tookie) Angus	**61**	**–**	**218**	**2**	**281**
Robert Hanson	**59**	**–**	**218**	**1**	**278**
	$ 330	**$ 372**	**$ 2,633**	**$ 8**	**$ 3,343**
Year ended December 31, 2008					
Peter Meredith	$ –	$ 255	$ 647	$ 1	$ 903
John Macken	–	–	325	–	325
Pierre Lebel	65	–	165	3	233
André Deepwell	48	–	140	2	190
R. Edward Flood	18	–	156	–	174
R. Stuart (Tookie) Angus	42	–	156	2	200
Robert Hanson	40	–	156	–	196
	$ 213	$ 255	$ 1,745	$ 8	$ 2,221

(i) *Alexander Molyneux was appointed as a director and the CEO of the Company on October 11, 2009*

Five highest paid individuals

The five highest paid individuals included two directors of the Company for the years ended December 31, 2009 and 2008. The emoluments of the remaining three highest paid individuals for the years ended December 31, 2009 and 2008 are as follows:

	Year ended December 31, 2009	2008
Salaries and other benefits	**$ 695**	$ 893
Retirement benefit contribution	**2**	6
Stock-based compensation	**1,738**	759
	$ 2,435	$ 1,658

Their emoluments were within the following bands:

	Year ended December 31, 2009	2008
HK$ 3,000,001 to HK$ 3,500,000	**–**	2
HK$ 5,000,001 to HK$ 5,500,000	**1**	–
HK$ 6,000,001 to HK$ 6,500,000	**1**	1
HK$ 7,500,001 to HK$ 8,000,000	**1**	–
	3	3

During the years ended December 31, 2009 and 2008, no emoluments were paid by the Company to the directors or the five highest paid individuals as an inducement to join or upon joining the Company or as compensation for loss of office. None of the directors of the Company has waived any emoluments during the years ended December 31, 2009 and 2008.

APPENDIX TO THE ANNUAL REPORT

DECEMBER 31, 2009

(expressed in thousands of U.S. Dollars and shares in thousands, unless otherwise indicated)

A3. FIVE YEAR SUMMARY

Below is a five year summary of the Company's results, assets and liabilities:

	Year ended December 31,				
	2009	2008	2007	2006	2005
Revenue	**$ 36,038**	$ 3,126	$ –	$ –	$ –
Income from mine operations	**6,613**	949	–	–	–
Net loss and comprehensive loss attributable to equity holders of the Company	**$(110,805)**	$ (69,576)	$ (96,736)	$ (21,729)	$ (16,110)
Basic and diluted loss per share from continuing and discontinued operations	**(0.83)**	(0.54)	(1.89)	(1.31)	(1.06)

	As at December 31,				
	2009	2008	2007	2006	2005
Total assets	**$ 560,684**	$ 99,948	$ 5,610	$ 2,315	$ 3,919
Less: Total liabilities	**(563,476)**	(10,984)	(107,441)	(6,287)	(914)
Total net (liabilities)/assets	**$ (2,792)**	$ 88,964	$(101,831)	$ (3,972)	$ 3,005

CORPORATE INFORMATION

DIRECTORS

Executive Directors:
Mr. Alexander Molyneux

Non-Executive Directors:
Mr. Peter Meredith (CHAIRMAN)
Mr. John Macken
Mr. R. Edward Flood

Independent Non-Executive Directors:
Mr. Pierre Lebel (LEAD DIRECTOR)
Mr. André Deepwell
Mr. R. Stuart (Tookie) Angus
Mr. Robert Hanson

AUDIT COMMITTEE
Mr. André Deepwell (CHAIR)
Mr. R. Stuart (Tookie) Angus
Mr. Pierre Lebel

NOMINATING AND CORPORATE GOVERNANCE COMMITTEE
Mr. Robert Hanson (CHAIR)
Mr. R. Stuart (Tookie) Angus
Mr. André Deepwell
Mr. Pierre Lebel

COMPENSATION AND BENEFITS COMMITTEE
Mr. R. Stuart (Tookie) Angus (CHAIR)
Mr. André Deepwell
Mr. Robert Hanson
Mr. Pierre Lebel

ENVIRONMENTAL, HEALTH AND SAFETY COMMITTEE
Mr. Robert Hanson (CHAIR)
Mr. John Macken
Mr. Alexander Molyneux

COMPANY SECRETARY
Beverly Ann Bartlett

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Hong Kong:
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