SouthGobi Resources Ltd.
Condensed Consolidated Interim Financial Statements

June 30, 2015
(Expressed in U.S. Dollars)
(Unaudited)

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SOUTHGOBI RESOURCES LTD.

Condensed Consolidated Interim Statements of Comprehensive Income

(Unaudited)

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

	Notes	Three months ended June 30, 2015	Three months ended June 30, 2014	Six months ended June 30, 2015	Six months ended June 30, 2014
Revenue		**$ 2,951**	$ 6,691	**$ 4,536**	$ 11,828
Cost of sales	4	**(11,835)**	(20,086)	**(29,511)**	(38,452)
Gross loss		**(8,884)**	(13,395)	**(24,975)**	(26,624)
Other operating expenses	5	**(19,450)**	(1,776)	**(18,479)**	(2,849)
Administration expenses	6	**(1,961)**	(2,253)	**(3,388)**	(4,490)
Evaluation and exploration expenses		**22**	(107)	**(56)**	(279)
Loss from operations		**(30,273)**	(17,531)	**(46,898)**	(34,242)
Finance costs	7	**(5,222)**	(5,215)	**(11,605)**	(10,240)
Finance income	7	**273**	127	**16**	1,134
Share of earnings/(losses) of joint venture	11	**151**	(3)	**133**	(29)
Loss before tax		**(35,071)**	(22,622)	**(58,354)**	(43,377)
Current income tax expense		**(1)**	(546)	**(1)**	(546)
Net loss attributable to equity holders of the Company		**(35,072)**	(23,168)	**(58,355)**	(43,923)
Other comprehensive income/(loss) to be reclassified to profit or loss in subsequent periods					
Change in value of available-for-sale financial asset, net of tax		**-**	414	**-**	(100)
Net comprehensive loss attributable to equity holders of the Company		**$ (35,072)**	$ (22,754)	**$ (58,355)**	$ (44,023)
Basic loss per share		**$ (0.15)**	$ (0.12)	**$ (0.25)**	$ (0.23)
Diluted loss per share		**$ (0.15)**	$ (0.12)	**$ (0.25)**	$ (0.23)

The accompanying notes are an integral part of these condensed consolidated interim financial statements.

SOUTHGOBI RESOURCES LTD.

Condensed Consolidated Interim Statements of Financial Position

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

	Notes	As at June 30, 2015	As at December 31, 2014
Assets			
Current assets			
Cash		**$ 901**	$ 3,789
Trade and other receivables	8	**3,327**	462
Inventories	9	**31,001**	31,255
Prepaid expenses and deposits		**3,951**	4,192
Total current assets		**39,180**	39,698
Non-current assets			
Property, plant and equipment	10	**334,967**	349,867
Long term investments	11	**26,840**	26,574
Total non-current assets		**361,807**	376,441
Total assets		**$ 400,987**	$ 416,139
Equity and liabilities			
Current liabilities			
Trade and other payables	12	**$ 24,466**	$ 18,124
Provision for court case penalty	21	**18,049**	-
Deferred revenue		**11,506**	11,898
Interest-bearing borrowings	13	**4,158**	3,945
Current portion of convertible debenture	14	**12,278**	2,301
Total current liabilities		**70,457**	36,268
Non-current liabilities			
Convertible debenture	14	**94,249**	92,886
Decommissioning liability		**2,830**	2,704
Total non-current liabilities		**97,079**	95,590
Total liabilities		**167,536**	131,858
Equity			
Common shares		**1,087,759**	1,080,417
Share option reserve		**52,224**	52,041
Accumulated deficit	15	**(906,532)**	(848,177)
Total equity		**233,451**	284,281
Total equity and liabilities		**$ 400,987**	$ 416,139
Net current assets		**$ (31,277)**	$ 3,430
Total assets less current liabilities		**$ 330,530**	$ 379,871

Corporate information and going concern (Note 1), commitments for expenditure (Note 20) and contingencies (Note 21)

The accompanying notes are an integral part of these condensed consolidated interim financial statements.

APPROVED BY THE BOARD:

"Andre Deepwell"
Director

"Pierre Lebel"
Director

SOUTHGOBI RESOURCES LTD.

Condensed Consolidated Interim Statements of Changes in Equity

(Unaudited)

(Expressed in thousands of U.S. Dollars and shares/units in thousands)

	Number of shares/units	Share capital	Share option reserve	Investment revaluation reserve	Accumulated deficit	Total
Balances, January 1, 2014	187,309	$ 1,067,839	$ 51,198	$ 514	$ (744,494)	$ 375,057
Shares issued for:						
Employee share purchase plan	8	7	-	-	-	7
Share-based compensation charged to operations	-	-	382	-	-	382
Net loss for the period	-	-	-	-	(43,923)	(43,923)
Change in value of available-for-sale financial asset, net of tax	-	-	-	(100)	-	(100)
Balances, June 30, 2014	187,317	$ 1,067,846	$ 51,580	$ 414	$ (788,417)	$ 331,423
Balances, January 1, 2015	**218,752**	**$ 1,080,417**	**$ 52,041**	**$ -**	**$ (848,177)**	**$ 284,281**
Shares issued for:						
Private placement	**11,619**	**3,812**	**-**	**-**	**-**	**3,812**
Exercise of stock options, net of redemptions	**12**	**9**	**(3)**	**-**	**-**	**6**
Employee share purchase plan	**5**	**3**	**-**	**-**	**-**	**3**
Conversion of mandatory convertible units	**10,131**	**-**	**-**	**-**	**-**	**-**
Mandatory convertible units issued for:						
Private placement	**10,131**	**3,518**	**-**	**-**	**-**	**3,518**
Conversion of mandatory convertible units	**(10,131)**	**-**	**-**	**-**	**-**	**-**
Share-based compensation charged to operations	**-**	**-**	**186**	**-**	**-**	**186**
Net loss for the period	**-**	**-**	**-**	**-**	**(58,355)**	**(58,355)**
Balances, June 30, 2015	**240,519**	**$ 1,087,759**	**$ 52,224**	**$ -**	**$ (906,532)**	**$ 233,451**

The accompanying notes are an integral part of these condensed consolidated interim financial statements.

SOUTHGOBI RESOURCES LTD.

Condensed Consolidated Interim Statements of Cash Flows

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

	Notes	Six months ended June 30, 2015	Six months ended June 30, 2014
Operating activities			
Loss before tax		**$ (58,354)**	$ (43,377)
Adjustments for:			
Depreciation and depletion		**17,447**	14,149
Share-based compensation	16	**186**	381
Finance costs	7	**11,605**	10,240
Finance income	7	**(16)**	(1,134)
Share of losses/(earnings) of joint venture	11	**(133)**	29
Interest paid		**-**	(7,958)
Commitment fee and front end fee		**-**	(133)
Income tax paid		**(2)**	(5)
Unrealized foreign exchange gain		**(160)**	(405)
Loss on disposal of property, plant and equipment		**(6)**	-
Provision for doubtful trade and other receivables	8	**157**	-
Impairment loss on available-for-sale financial asset		**-**	1,766
Impairment of inventories	9	**3,111**	13,527
Impairment of property, plant and equipment		**-**	277
Net proceeds from disposal of mining license		**-**	(1,273)
Operating cash flows before changes in non-cash working capital items		**(26,165)**	(13,916)
Net change in non-cash working capital items	19	**20,007**	(140)
Cash used in operating activities		**(6,158)**	(14,056)
Investing activities			
Expenditures on property, plant and equipment		**(4,028)**	(4,059)
Interest received		**2**	5
Proceeds from maturity or disposal of short and long term investments		**-**	74
Net proceeds from disposal of mining license		**-**	1,273
Investment in joint venture		**(30)**	-
Cash generated used in investing activities		**(4,056)**	(2,707)
Financing activities			
Proceeds from issuance of common shares		**7,340**	7
Drawings under borrowing from immediate holding company		**-**	3,800
Cash generated from financing activities		**7,340**	3,807
Effect of foreign exchange rate changes on cash		**(14)**	(92)
Decrease in cash		**(2,888)**	(13,048)
Cash, beginning of period		**3,789**	21,837
Cash, end of period		**$ 901**	$ 8,789

Supplemental cash flow information (Note 19)

The accompanying notes are an integral part of these condensed consolidated interim financial statements.

1. CORPORATE INFORMATION AND GOING CONCERN

SouthGobi 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 (Symbol: SGQ) and Stock Exchange of Hong Kong (Symbol: 1878). The company, together with its subsidiaries (collectively referred to as the "Company"), is an integrated coal mining, development and exploration company. At June 30, 2015, Novel Sunrise Investments Limited owned approximately 30% of the outstanding Common Shares of the Company while Turquoise Hill Resources Ltd. ("Turquoise Hill") owned approximately 23% of the outstanding Common Shares of the Company. Turquoise Hill is controlled by Rio Tinto plc ("Rio Tinto").

The Company owns the following significant coal projects in Mongolia: the Ovoot Tolgoi open pit producing coal mine ("Ovoot Tolgoi Mine") and the following significant development projects, the Soumber Deposit, the Zag Suuj Deposit and the Ovoot Tolgoi Underground Deposit. These projects are located in the Umnugobi Aimag (South Gobi Province) of Mongolia, within 150 kilometers of each other and in close proximity to the Mongolia-China border. The Company owns a 100% interest in these coal projects.

The head office, principal address and registered and records office of the Company is located at 1100 - 355 Burrard Street, Vancouver, British Columbia, Canada, V6C 2G8.

<u>Going concern assumption</u>

Several adverse conditions and material uncertainties cast significant doubt upon the going concern assumption. The Company had limited cash of $901 at June 30, 2015 and anticipates that coal prices in the People's Republic of China ("China") will remain under pressure for the remainder of 2015, which will continue to impact the Company's margins and liquidity. Therefore, the Company is actively seeking prepaid coal offtake agreements and other additional sources of financing to continue operating and meet its business objectives, while remaining focused on minimizing uncommitted capital expenditures and preserving the Company's growth options. The Company, together with its new strategic partner and significant shareholder, Novel Sunrise Investments Ltd. ("Novel Sunrise"), has developed a funding plan (the "Proposed Funding Plan") in order to pay the interest due under the China Investment Corporation ("CIC") convertible debenture (the "CIC Convertible Debenture"), meet its obligations as they fall due and achieve its business objectives in 2015 and beyond. These obligations include the tax penalty ($18,049) (Refer to Note 21.1 for details). However, there is no guarantee that the Company will be able to implement this Proposed Funding Plan or secure other sources of financing. If it fails to do so, or is unable to secure additional capital or otherwise restructure or refinance its business in order to address its cash requirements through June 30, 2016, then the Company is unlikely to have sufficient capital resources or cash flows from mining operations in order to satisfy its ongoing obligations and future contractual commitments, including cash interest payments due on the CIC convertible debenture (approximately $16,300 on November 19, 2015). As a result, the Company may not be able to continue as a going concern.

1. CORPORATE INFORMATION AND GOING CONCERN (CONTINUED)

The Company's consolidated financial statements have been prepared on a going concern basis which assumes that the Company will continue operating until at least June 30, 2016 and will be able to realize its assets and discharge its liabilities in the normal course of operations as they come due. However, in order to continue as a going concern, the Company must generate sufficient operating cash flows, secure additional capital or otherwise pursue a strategic restructuring, refinancing or other transaction to provide it with additional liquidity. If it fails to do so, or is unable to secure additional capital or otherwise restructure or refinance its business in order to address its cash requirements through June 30, 2016, then the Company is unlikely to have sufficient capital resources or cash flows from mining operations in order to satisfy its ongoing obligations and future contractual commitments, including cash interest payments due on the CIC convertible debenture. As a result, it may not be able to continue as a going concern.

If for any reason, the Company is unable to secure the additional sources of financing and continue as a going concern, then this could result in adjustments to the amounts and classifications of assets and liabilities in the Company's consolidated financial statements and such adjustments could be material.

While the Company intends to secure additional sources of financing as soon as possible, a continued delay in securing additional financing could ultimately result in an event of default of the CIC Convertible Debenture, which if not cured within applicable cure periods in accordance with the terms of such debenture, may result in the principal amount owing and all accrued and unpaid interest becoming immediately due and payable upon notice to the Company by CIC.

The Company is also subject to a remedial delisting review by the TSX in connection with its reliance on the financial hardship exemption from approval by its shareholders of the private placement with Novel Sunrise as announced on February 24, 2015. The TSX has advised that the Company's financial and operating results may not warrant that its securities continue to be listed on the TSX. The failure by the Company to clear the TSX delisting review may result in the delisting of the Common Shares from the TSX which may result in an event of default under the CIC convertible debenture. An event of default may result in the principal amount owing and all accrued and unpaid interest becoming immediately due and payable upon notice to the Company by CIC.

On February 25, 2015, the TSX confirmed that the Company had been placed on remedial delisting review in connection with its reliance on the financial hardship exemption from approval by its shareholders of the private placement with Novel Sunrise. A delisting review is customary practice under TSX policies when a listed company relies on the financial hardship exemption.

Following extension requests by the Company to address delays in the implementation of its Proposed Funding Plan, a meeting of the TSX Committee has been deferred until August 25, 2015 to consider whether the Company has met the listing requirements of the exchange or delist the Common Shares. The TSX Committee has determined to defer its delisting decision until no later than August 28, 2015.

2. BASIS OF PREPARATION

2.1 Statement of compliance

These condensed consolidated interim financial statements, including comparatives, have been prepared in accordance with International Accounting Standard 34 "Interim Financial Reporting" using accounting policies in compliance with the International Financial Reporting Standards ("IFRS") issued by the International Accounting Standards Board ("IASB") and Interpretations of the IFRS Interpretations Committee ("IFRIC").

The condensed consolidated interim financial statements of the Company for the three months ended June 30, 2015 were approved and authorized for issue by the Board of Directors of the Company on August 13, 2015.

2.2 Basis of presentation

These condensed consolidated interim financial statements have been prepared using accounting policies and methods of computation consistent with those applied in the Company's December 31, 2014 consolidated annual financial statements, except for those accounting policies which have changed as a result of the adoption of new and revised standards and interpretations as described below. These condensed consolidated interim financial statements do not include all the information and note disclosures required by IFRS for annual financial statements and therefore should be read in conjunction with the Company's annual consolidated financial statements for the year ended December 31, 2014.

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 the Company operates.

2.3 Adoption of new and revised standards and interpretations

A number of new standards and amendments to standards and interpretations are effective for annual periods beginning after January 1, 2015, and have not been applied in preparing these consolidated financial statements. None of these are expected to have a significant effect on the consolidated financial statements of the Company, except the following set out below:

IFRS 9, Financial Instruments ("IFRS 9"), addresses the classification, measurement and recognition of financial assets and financial liabilities. The complete version of IFRS 9 was issued in July 2014. It replaces the guidance in IAS 39 that relates to the classification and measurement of financial instruments. IFRS 9 retains but simplifies the mixed measurement model and establishes three primary measurement categories for financial assets: amortized cost, fair value through other comprehensive income ("OCI") and fair value through profit or loss ("FVTPL"). There is now a new expected credit losses model that replaces the incurred loss impairment model used in IAS 39. For financial liabilities there were no changes to classification and measurement except for the recognition of changes in own credit risk in OCI, for liabilities designated as FVTPL. The standard is effective for accounting periods beginning on or after January 1, 2018. Early adoption is permitted. The Company has yet to assess the full impact of IFRS 9.

2. BASIS OF PREPARATION (CONTINUED)

IFRS 15, Revenue from Contracts with Customers ("IFRS 15"), deals with revenue recognition and establishes principles for reporting useful information to users of financial statements about the nature, timing and uncertainty of revenue and cash flows arising from an entity's contracts with customers. Under IFRS 15, revenue is recognized when a customer obtains control of a good or service and thus has the ability to direct the use and obtain the benefits from the good or service. The standard replaces IAS 18, Revenue, and IAS 11, Construction Contracts, and related interpretations. The standard is effective for annual periods beginning on or after January 1, 2017, with early adoption permitted. In July 2015, the IASB voted to confirm the deferral of the effective date of IFRS 15 to January 1, 2018, with early adoption permitted. The formal amendment to IFRS 15, specifying the new effective date, is expected to be issued in September 2015. Management is assessing the impact, if any, on the financial statements of this new standard.
There are no other IFRSs or IFRS Interpretations Committee interpretations that are not yet effective that would be expected to have a material impact on the financial statements of the Company.

2.4 Significant accounting judgments and estimates

Information about judgments and estimates in applying accounting policies that have the most significant effect on the amounts recognized in the Company's consolidated financial statements are included in Note 3.22 to the Company's December 31, 2014 consolidated annual financial statements. Except for the significant accounting judgments and estimates disclosed below, the significant accounting judgments and estimates remain substantially unchanged from December 31, 2014.

Liquidity and the going concern assumption

In the determination of the Company's ability to meet its ongoing obligations and future contractual commitments, management relies on the Company's planning, budgeting and forecasting process to help determine the funds required to support the Company's normal operations on an ongoing basis and its expansionary plans. The key inputs used by the Company in this process include forecasted capital deployment, results from operations, results from the exploration and development of its properties and general industry conditions.

2. BASIS OF PREPARATION (CONTINUED)

Several adverse conditions and material uncertainties cast significant doubt upon the going concern assumption. The Company had limited cash of $901 at June 30, 2015 and anticipates that coal prices in China will remain under pressure for the remainder of 2015, which will continue to impact the Company's margins and liquidity. Therefore the Company is actively seeking prepaid coal offtake agreements and other additional sources of financing to continue operating and meet its business objectives, while remaining focused on minimizing uncommitted capital expenditures and preserving the Company's growth options. The Company, together with its new strategic partner and significant shareholder, Novel Sunrise, has developed the Proposed Funding Plan in order to pay the interest due under the CIC convertible debenture, meet its obligations as they fall due and achieve its business objectives in 2015 and beyond. These obligations include the tax penalty ($18,049) (Refer to Note 21.1 for details). However, there is no guarantee that the Company will be able to implement this Proposed Funding Plan or secure other sources of financing. If it fails to do so, or is unable to secure additional capital or otherwise restructure or refinance its business in order to address its cash requirements through June 30, 2016, then the Company is unlikely to have sufficient capital resources or cash flows from mining operations in order to satisfy its ongoing obligations and future contractual commitments, including cash interest payments due on the CIC convertible debenture (approximately $16,300 on November 19, 2015). As a result, the Company may not be able to continue as a going concern.

The Company's consolidated financial statements have been prepared on a going concern basis which assumes that the Company will continue operating until at least June 30, 2016 and will be able to realize its assets and discharge its liabilities in the normal course of operations as they come due; however, in order to continue as a going concern, the Company must generate sufficient operating cash flows, secure additional capital or otherwise pursue a strategic restructuring, refinancing or other transaction to provide it with additional liquidity. If it fails to do so, or is unable to secure additional capital or otherwise restructure or refinance its business in order to address its cash requirements through June 30, 2016, then the Company is unlikely to have sufficient capital resources or cash flows from mining operations in order to satisfy its ongoing obligations and future contractual commitments, including cash interest payments due on the CIC convertible debenture. As a result, it may not be able to continue as a going concern.

If for any reason, the Company is unable to secure the additional sources of financing and continue as a going concern, then this could result in adjustments to the amounts and classifications of assets and liabilities in the Company's consolidated financial statements and such adjustments could be material.

While the Company intends to secure additional sources of financing as soon as possible, a continued delay in securing additional financing could ultimately result in an event of default of the CIC Convertible Debenture, which if not cured within applicable cure periods in accordance with the terms of such debenture, may result in the principal amount owing and all accrued and unpaid interest becoming immediately due and payable upon notice to the Company by CIC.

The Company is also subject to a remedial delisting review by the TSX in connection with its reliance on the financial hardship exemption from approval by its shareholders of the private placement with Novel Sunrise as announced on February 24, 2015. The TSX has advised that the Company's financial and operating results may not warrant that its securities continue to be listed on the TSX. The failure by the Company to clear the TSX delisting review may result in the delisting of the Common Shares from the TSX which may result in an event of default under the CIC convertible debenture. An event of default may result in the principal amount owing and all accrued and unpaid interest becoming immediately due and payable upon notice to the Company by CIC.

2. BASIS OF PREPARATION (CONTINUED)

On February 25, 2015, the TSX confirmed that the Company had been placed on remedial delisting review in connection with its reliance on the financial hardship exemption from approval by its shareholders of the private placement with Novel Sunrise. A delisting review is customary practice under TSX policies when a listed company relies on the financial hardship exemption.

Following extension requests by the Company to address delays in the implementation of its Proposed Funding Plan, a meeting of the TSX Committee has been deferred until August 25, 2015 to consider whether the Company has met the listing requirements of the exchange or delist the Common Shares. The TSX Committee has determined to defer its delisting decision until no later than August 28, 2015.

Ovoot Tolgoi Mine cash generating unit

The Company determined that an indicator of impairment existed for its Ovoot Tolgoi Mine cash generating unit as at June 30, 2015. The impairment indicator was the continued weakness in the Company's share price during the three months ended June 30, 2015 and the fact that the market capitalization of the Company, as at June 30, 2015, was less than the carrying value of its net assets.

Therefore, the Company conducted an impairment test whereby the carrying value of the Company's Ovoot Tolgoi Mine cash generating unit was compared to its "value in use" using a discounted future cash flow valuation model. The Company's cash flow valuation model has been updated to take into consideration the latest available information to the Company, including but not limited to, sales price, sales volumes and washing assumptions, operating cost assumptions and life of mine coal production assumptions as at June 30, 2015. The Company's Ovoot Tolgoi Mine cash generating unit carrying value was $340,600 as at June 30, 2015.

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

- Long term price estimates from an independent market consulting firm;
- Forecasted sales volumes in line with production levels as per the updated mine plan;
- Updated life-of-mine coal production, strip ratio, capital costs and operating costs;
- A pre-tax discount rate of 17.3% based on an analysis of market, country and the Company specific factors; and
- Coal processing yield of 75%.

Key sensitivities in the valuation model are as follows:

- For each 1% increase/(decrease) in the long term price estimates, the calculated fair value of the cash generating unit increases/(decreases) by approximately $22,200/($22,200);
- For each 1% increase/(decrease) in the discount rate, the calculated fair value of the cash generating unit (decreases)/increases by approximately ($23,400)/$25,800; and
- For each 1% increase/(decrease) in the cash mining cost estimates, the calculated fair value of the cash generating unit (decreases)/increases by approximately ($13,200)/$13,200.

2. BASIS OF PREPARATION (CONTINUED)

The impairment analysis did not result in the identification of an impairment loss and no charge was required as at June 30, 2015. A decline of more than 2% in the long term price estimates, an increase of more than 2% in the pre-tax discount rate or an increase of more than 3% in the cash mining cost estimates may trigger an impairment charge on the cash generating unit. The Company believes that the estimates and assumptions incorporated in the impairment analysis are reasonable; however, the estimates and assumptions are subject to significant uncertainties and judgments.

The Company is currently still reviewing its mine plan for the Ovoot Tolgoi project. Changes to the mine plan may have an impact on the quantities of measured and/or indicated resources and reserves of the Ovoot Tolgoi project.

Investment in RDCC LLC

The Company determined that an indicator of impairment existed for its investment in RDCC LLC as at June 30, 2015. The impairment indicator was the continued delay in the commencement of operation of the paved highway from the Company’s Ovoot Tolgoi Mine to the Mongolia-China border.

Therefore, the Company conducted an impairment test whereby the carrying value of the Company’s investment in RDCC LLC compared to its “value in use” using a discounted future cash flow valuation model. The carrying value was $26,840 as at June 30, 2015.

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

- Toll fee estimates reference to the concession agreement;
- Traffic volume;
- Repair, maintenance and operating cost; and
- A pre-tax discount rate of 13.7% based on a weighted average cost of capital of the Company.

Key sensitivities in the valuation model are as follows:

- For each 1% increase/(decrease) in the toll fee estimates or traffic volume, the calculated fair value of the carrying unit increases/(decreases) by approximately $300/($300); and
- For each 1% increase/(decrease) in the discount rate, the calculated fair value of the carrying unit (decreases)/increases by approximately ($1,700)/$1,800.

The impairment analysis did not result in the identification of an impairment loss and no charge was required as at June 30, 2015. The Company believes that the estimates and assumptions incorporated in the impairment analysis are reasonable; however, the estimates and assumptions are subject to significant uncertainties and judgments.

2. BASIS OF PREPARATION (CONTINUED)

On April 30, 2015 in response to the Road and Transportation Minister’s Order no. 115 dated April 29, 2015 a working group was established to assist in the commencement of commercial operations of the paved highway from the Ovoot Tolgoi Complex to the Shivee Khuren border crossing (“Paved Highway”). Subsequently, on May 8, 2015 a three month trial period of operation in respect of the Paved Highway commenced. This trial period imposes a nine hundred (900) MNT charge per tonne of coal hauled on the Paved Highway in the Nariinsukhait-Shiveekhuren direction. This charge is lower than the fifteen hundred (1500) MNT charge per tonne stated in the signed concession agreement between RDCC LLC and the State Property Committee of Mongolia which formed the basis for the Company’s investment decision. As at August 13, 2015, discussions are ongoing with respect to the pricing levels beyond the initial trial period and in respect to how RDCC LLC will be reimbursed for any difference between the actual rate per tonne charged and the rate per tonne as stated in the concession agreement. RDCC has notified the Company that it expects to be reimbursed or compensated for the reduced pricing levels. However, should the Government of Mongolia not honor the pricing as per the concession agreement or provide sufficient compensation to the Company for the reduced rate, this may lead to an impairment of the Company’s investment in RDCC LLC.

3. SEGMENTED INFORMATION

The Company’s one reportable operating segment is its Mongolian Coal Division. The Company’s Executive Director (chief operating decision maker) reviews the Mongolian Coal Division’s discrete financial information in order to make decisions about resources to be allocated to the segment and to assess its performance. The division is principally engaged in coal mining, development and exploration in Mongolia. The Company’s Corporate Division does not earn revenues and therefore does not meet the definition of an operating segment.

During the six months ended June 30, 2015, the Mongolian Coal Division had 4 active customers with the largest customer accounting for 56% of revenues, the second and third largest customer accounting for 35% and 5% of revenue, respectively.

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

3. SEGMENTED INFORMATION (CONTINUED)

The carrying amounts of the Company's assets, liabilities, reported income or loss and revenues analyzed by operating segment are as follows:

	Mongolian Coal Division	Unallocated (i)	Consolidated Total
Segment assets			
As at June 30, 2015	**$ 398,221**	**$ 2,766**	**$ 400,987**
As at December 31, 2014	411,816	4,323	416,139
Segment liabilities			
As at June 30, 2015	**$ 46,419**	**$ 121,117**	**$ 167,536**
As at December 31, 2014	22,770	109,088	131,858
Segment loss			
For the three months ended June 30, 2015	**$ (28,676)**	**$ (6,396)**	**$ (35,072)**
For the three months ended June 30, 2014	(16,163)	(7,005)	(23,168)
For the six months ended June 30, 2015	**$ (44,365)**	**$ (13,990)**	**$ (58,355)**
For the six months ended June 30, 2014	(29,381)	(14,542)	(43,923)
Segment revenues			
For the three months ended June 30, 2015	**$ 2,951**	**$ -**	**$ 2,951**
For the three months ended June 30, 2014	6,691	-	6,691
For the six months ended June 30, 2015	**$ 4,536**	**$ -**	**$ 4,536**
For the six months ended June 30, 2014	11,828	-	11,828
Impairment charge on assets (ii) (iii)			
For the three months ended June 30, 2015	**$ 2,718**	**$ -**	**$ 2,718**
For the three months ended June 30, 2014	9,928	-	9,928
For the six months ended June 30, 2015	**$ 3,268**	**$ -**	**$ 3,268**
For the six months ended June 30, 2014	17,209	1,766	18,975

(i) The unallocated amount contains all amounts associated with the Corporate Division.
(ii) The impairment charge on assets for the three and six months ended June 30, 2015 relates to inventories (Note 9) and trade and other receivables (Note 8).
(iii) The impairment charges on assets for the three and six months ended June 30, 2014 relates to inventories (Note 9) and investments.

The operations of the Company are primarily located in Mongolia, Hong Kong and Canada.

	Mongolia	Hong Kong	Canada	Consolidated Total
Revenues				
For the three months ended June 30, 2015	**$ 2,951**	**$ -**	**$ -**	**$ 2,951**
For the three months ended June 30, 2014	6,691	-	-	6,691
For the six months ended June 30, 2015	**$ 4,536**	**$ -**	**$ -**	**$ 4,536**
For the six months ended June 30, 2014	11,828	-	-	11,828
Non-current assets				
As at June 30, 2015	**$ 361,784**	**$ 23**	**$ -**	**$ 361,807**
As at December 31, 2014	375,588	13	840	376,441

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

4. COST OF SALES

The Company's cost of sales consists of the following amounts:

	Three months ended June 30,		Six months ended June 30,	
	2015	2014	2015	2014
Operating expenses	**$ 4,571**	$ 6,754	**$ 6,498**	$ 12,317
Share-based compensation expense (Note 16)	**4**	127	**32**	143
Depreciation and depletion	**832**	2,061	**1,141**	4,540
Impairment of coal stockpile inventories (Note 9)	**2,561**	6,246	**3,111**	13,527
Cost of sales from mine operations	**7,968**	15,188	**10,782**	30,527
Cost of sales related to idled mine assets (i)	**3,867**	4,898	**18,729**	7,925
Cost of sales	**$ 11,835**	$ 20,086	**$ 29,511**	$ 38,452

(i) Cost of sales related to idled mine assets for the three months ended June 30, 2015 includes $3,867 of depreciation expense (2014: includes $4,857 of depreciation expenses). Cost of sales related to idled mine assets for the six months ended June 30, 2015 includes $15,755 of depreciation expense (2014: includes $7,846 of depreciation expenses). The depreciation expense relates to the Company's idled plant and equipment.

5. OTHER OPERATING EXPENSE

The Company's other operating expense consist of the following amounts:

	Three months ended June 30,		Six months ended June 30,	
	2015	2014	2015	2014
Sustainability and community relations	**$ 48**	$ 58	**$ 135**	$ 129
Foreign exchange loss/(gain)	**1,196**	(146)	**138**	(910)
Mark-to-market loss on available-for-sale financial asset	**-**	-	**-**	1,766
Provision for doubtful trade and other receivables (Note 8)	**157**	-	**157**	-
Impairment of property, plant and equipment (Note 10)	**-**	277	**-**	277
Impairment of prepaid expenses and deposits	**-**	3,405	**-**	3,405
Proceeds from disposal of mining license	**-**	(1,818)	**-**	(1,818)
Provision for court case penalty (Note 21)	**18,049**	-	**18,049**	-
Other operating expenses	**$ 19,450**	$ 1,776	**$ 18,479**	$ 2,849

6. ADMINISTRATION EXPENSES

The Company's administration expenses consist of the following amounts:

	Three months ended June 30,		Six months ended June 30,	
	2015	2014	2015	2014
Corporate administration	**$ 512**	$ 523	**$ 958**	$ 1,183
Professional fees	**890**	779	**1,365**	1,465
Salaries and benefits	**472**	825	**852**	1,553
Share-based compensation expense (Note 16)	**47**	94	**147**	225
Depreciation	**40**	32	**66**	64
Administration expenses	**$ 1,961**	$ 2,253	**$ 3,388**	$ 4,490

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

7. FINANCE COSTS AND INCOME

The Company's finance costs consist of the following amounts:

	Three months ended, June 30,		Six months ended, June 30,	
	2015	**2014**	**2015**	**2014**
Unrealized loss on embedded derivatives in convertible debenture (Note 14)	**$ -**	$ -	**$ 1,279**	$ -
Interest expense on convertible debenture (Note 14)	**5,089**	5,021	**10,061**	9,986
Unrealized loss on FVTPL investments (i)	**-**	8	**-**	48
Interest expense on borrowing (Note 13)	**107**	24	**213**	24
Commitment fee and front end fee (Note 13)	**-**	133	**-**	133
Realized loss on disposal of FVTPL investments	**-**	5	**-**	5
Accretion of decommissioning liability	**26**	24	**52**	44
Finance costs	**$ 5,222**	$ 5,215	**$ 11,605**	$ 10,240

(i) FVTPL is defined as "fair value through profit or loss".

The Company's finance income consists of the following amounts:

	Three months ended, June 30,		Six months ended, June 30,	
	2015	**2014**	**2015**	**2014**
Unrealized gain on embedded derivatives in convertible debenture (Note 14)	**$ 265**	$ 121	**$ -**	$ 1,120
Interest income	**8**	6	**16**	14
Finance income	**$ 273**	$ 127	**$ 16**	$ 1,134

8. TRADE AND OTHER RECEIVABLES

The Company's trade and other receivables consist of the following amounts:

	As at	
	June 30, 2015	**December 31, 2014**
Trade receivables	**$ 3,167**	$ -
Other receivables	**160**	462
Total trade and other receivables	**$ 3,327**	$ 462

The aging of the Company's trade and other receivables is as follows:

	As at	
	June 30, 2015	**December 31, 2014**
Less than 1 month	**$ 2,495**	$ 305
1 to 3 months	**805**	123
3 to 6 months	**6**	34
Over 6 months	**21**	-
Total trade and other receivables	**$ 3,327**	$ 462

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

8. TRADE AND OTHER RECEIVABLES (CONTINUED)

Trade receivables are normally due within 30 days from the date of billing. Customers with balances that are more than 30 days past due are normally requested to settle all outstanding balances before any further credit is granted.

9. INVENTORIES

The Company's inventories consist of the following amounts:

	As at	
	June 30, 2015	**December 31, 2014**
Coal stockpiles	**$ 4,997**	$ 3,765
Materials and supplies	**26,004**	27,490
Total inventories	**$ 31,001**	$ 31,255

Cost of sales for the three months and six months ended June 30, 2015 includes an impairment loss of $2,561 and $3,111, respectively, related to the Company's coal stockpile inventories (For three and six months ended June 2014: $6,246 and $13,527, respectively). As at June 30, 2015, $1,901 of the Company's coal stockpile inventories are carried at their net realizable value (December 31, 2014: $1,220).

10. PROPERTY, PLANT AND EQUIPMENT

The Company's property, plant and equipment consist of the following amounts:

	Mobile equipment	Other operating equipment	Buildings and roads	Mineral properties	Construction in progress	Total
Cost						
As at December 31, 2014	$ 366,427	$ 28,615	$ 72,194	$ 133,486	$ 6,268	$ 606,990
Additions	**1,495**	**23**	**-**	**8,564**	**-**	**10,082**
Disposals	**(225)**	**(101)**	**-**	**-**	**-**	**(326)**
Reclassifications	**2,189**	**-**	**-**	**-**	**(2,189)**	**-**
As at June 30, 2015	**$ 369,886**	**$ 28,537**	**$ 72,194**	**$ 142,050**	**$ 4,079**	**$ 616,746**
Accumulated depreciation and impairment charges						
As at December 31, 2014	$ (188,175)	$ (19,834)	$ (33,052)	$ (15,785)	$ (277)	$ (257,123)
Charge for the period	**(20,181)**	**(1,212)**	**(2,674)**	**(909)**	**-**	**(24,976)**
Eliminated on disposals	**219**	**101**	**-**	**-**	**-**	**320**
As at June 30, 2015	**$ (208,137)**	**$ (20,945)**	**$ (35,726)**	**$ (16,694)**	**$ (277)**	**$ (281,779)**
Carrying amount						
As at December 31, 2014	$ 178,252	$ 8,781	$ 39,142	$ 117,701	$ 5,991	$ 349,867
As at June 30, 2015	**$ 161,749**	**$ 7,592**	**$ 36,468**	**$ 125,356**	**$ 3,802**	**$ 334,967**

As at June 30, 2015, the cost of the Company's property, plant and equipment includes $24,027 of prepayments to vendors (December 31, 2014: $28,232). The prepayments primarily relate to ordered but not yet delivered mobile equipment or mobile equipment delivered to the location of its intended use but not yet commissioned.

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

11. LONG TERM INVESTMENTS

The Company's investments consist of the following amounts:

	As at	
	June 30, 2015	December 31, 2014
Non-current investment in joint venture		
Investment in RDCC LLC	**$ 26,840**	$ 26,574
Total investments	**$ 26,840**	$ 26,574

The Company has a 40% interest in RDCC LLC, a joint venture. RDCC LLC has a concession agreement with the State Property Committee of Mongolia to construct a Paved Highway from the Company's Ovoot Tolgoi Mine to the Mongolia-China border. The concession agreement is structured as a 17-year build, operate and transfer agreement. The construction was completed in 2014 and operations commenced in the second quarter of 2015.

The movement of the Company's investment in RDCC LLC is as follows:

	Three months ended June 30,		Six months ended June 30,	
	2015	2014	2015	2014
Balance, beginning of period	**$ 26,689**	$ 24,517	**$ 26,574**	$ 24,205
Funds advanced	**-**	-	**133**	338
Share of earnings/(losses) of joint venture	**151**	(3)	**133**	(29)
Balance, end of period	**$ 26,840**	$ 24,514	**$ 26,840**	$ 24,514

For the three and six months ended June 30, 2015, RDCC LLC recognized revenue of $467 (2014: nil). For the three and six months ended June 30, 2015, RDCC LLC had a net income of $378 and $333, respectively. For the three and six months ended June 30, 2014, RDCC LLC had a net loss of $7 and $72, respectively.

12. TRADE AND OTHER PAYABLES

Trade and other payables of the Company primarily consists of amounts outstanding for trade purchases relating to coal mining, development and exploration activities and mining royalties payable. The usual credit period taken for trade purchases is between 30 to 90 days. The aging of the Company's trade and other payables is as follows:

	As at	
	June 30, 2015	December 31, 2014
Less than 1 month	**$ 9,944**	$ 6,706
1 to 3 months	**3,184**	1,703
3 to 6 months	**1,521**	2,705
Over 6 months	**9,817**	7,010
Total trade and other payables	**$ 24,466**	$ 18,124

Included in trade and other payables are amounts due to related parties which are further disclosed in Note 18.

13. INTEREST-BEARING BORROWING

Turquoise Hill Loan Facility

On May 25, 2014, the Company announced it has obtained a $10,000 revolving credit facility from Turquoise Hill to meet its short term working capital requirements (the “Turquoise Hill Loan Facility”). The key commercial terms of the facility were as follows:

- Original maturity date of August 30, 2014 (subsequently extended; refer below for details);
- Interest rate of one month US dollar LIBOR Rate in effect plus 11% margin per annum;
- Commitment fee of 35% of interest rate payable quarterly in arrears on undrawn principal amount of facility;
- Front end fee of $100;
- Draws subject to customary closing conditions and the Company’s cash requirements in the ordinary course of business;
- Facility is subject to certain mandatory prepayment and termination provisions; and
- The Company to continue to seek other funding alternatives.

On August 30, 2014, subject to certain conditions and limitations, Turquoise Hill agreed to grant a deferral of payment of $3,800 plus accrued interest thereon owing by the Company under the Turquoise Hill Loan Facility and reduced the revolving credit facility to the same $3,800. This deferral of payment and repayment was granted to the Company without prejudice to Turquoise Hill’s right and ability to assert and re-assert at any point in time to demand payment and repayment of all amounts owing to Turquoise Hill under the Turquoise Hill Loan Facility.

On May 4, 2015, following the expiry of the Sale and Purchase agreement (“NUR SPA”), between Turquoise Hill and National United Resources Holdings Limited (“NUR”) on April 30, 2015, Turquoise Hill agreed to a further limited deferral of repayment, subject to certain conditions and limitations, on the $3,800 principal and accrued interest owing on the Turquoise Hill Loan Facility as follows:

(i) $1,900 in principal and all interest that has accrued on and under the Turquoise Hill Loan Facility up to and including August 31, 2015 shall become due and payable on August 31, 2015; and

(ii) $1,900 in principal and all interest that has accrued on and under the Turquoise Hill Loan Facility from September 1, 2015 up to and including November 30, 2015 shall become due and payable on November 30, 2015.

At June 30, 2015 in addition to the principal of $3,800 the Company owed accrued interest of $358 under this facility (December 31, 2014 the Company had drawn $3,800 and owed accrued interest of $145).

Interim Funding Loan Commitment

On June 17, 2015, the Company negotiated an interim loan (“Interim Loan”) for up to $8,000 from Mr. Wilson Chen (a former principal of Novel Sunrise), with immediate availability, intended to address funding obligations pending the closing of the private placements between the Company and CITIC Merchant and Swiss Life GP. In accordance with the terms of the agreement the advances will be in a minimum amount of $2,000, with interest at LIBOR + 12% per annum, payable in cash on a quarterly basis in arrears, and maturing on June 18, 2016. The loan is unsecured and is subject to mandatory repayment upon completion of $30,000 of equity or other debt financing.

13. INTEREST-BEARING BORROWING (CONTINUED)

As at June 30, 2015 the Company had not drawn down any funds under the Interim Loan. The Company has requested a funding drawdown on the Interim Loan multiple times; however, the Company has to date not received such funding.

Revolving Loan Commitment

On June 22, 2015, the Company announced it had negotiated a revolving loan commitment (the "Revolving Loan") of RMB200 million (approximately $32,000) from a Chinese commercial bank, subject to the finalization of definitive documentation. The revolving loan commitment is intended to provide additional support to the Company in funding its operational objectives. The Company is negotiating with the bank to finalize the terms with a view to obtaining the Revolving Loan.

14. CONVERTIBLE DEBENTURE

14.1 Key commercial terms

On November 19, 2009, the Company issued a convertible debenture to a wholly owned subsidiary of CIC for $500,000. The convertible debenture bears interest at 8.0% per annum (6.4% payable semi-annually in cash and 1.6% payable annually in the Company's shares) and has a maximum term of 30 years. The convertible debenture is secured by a first charge over the Company's assets, including shares of its material subsidiaries. An event of default on the convertible debenture can be triggered as a result of certain encumbrances on the Company's assets (refer to Note 21.3). During 2010, the Company exercised a right within the debenture to call and convert $250,000 of the debenture for 21,471 Common Shares. Following the conversion the outstanding principal balance was $250,000 and has remained unchanged at that balance to June 30, 2015.

Under certain conditions, including the non-payment of interest amounts as the same become due, amounts outstanding under the CIC convertible debenture may be accelerated. Bankruptcy and insolvency events with respect to the Company or its material subsidiaries will result in an automatic acceleration of the indebtedness under the CIC convertible debenture. Subject to notice and cure periods, certain events of default under the CIC convertible debenture will result in acceleration of the indebtedness under such debenture at the option of CIC. Such other events of default include, but are not limited to, non-payment, breach of warranty, non-performance of obligations under the convertible debenture, default on other indebtedness and certain adverse judgments.

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 Common 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. An event of default on the convertible debenture can be triggered as a result of certain encumbrances on the Company's assets (Note 21.3).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;

14. CONVERTIBLE DEBENTURE (CONTINUED)

- CIC's conversion right - CIC has the right to convert the convertible debenture, in whole or in part, into Common Shares twelve months after the date of issue;
- Company's normal conversion right – After sixty months from the issuance date, and when the conversion price is greater than Cdn$10.66, the Company is entitled to force 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 convertible debenture 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 of Directors. The Company currently has nine Board of Directors members of which none were elected by CIC;
- 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;
- Pre-emption rights - While the convertible debenture 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 convertible 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 convertible 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 Turquoise Hill's ownership stake in the Company; and
- Registration rights - CIC has registration rights under applicable Canadian provincial securities laws in connection with the Common Shares issuable upon conversion of the convertible debenture.

14.2 Debt host and embedded derivatives

The convertible debenture is presented as a liability since it contains no equity components. 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 and is measured at amortized cost using the effective interest rate method and the embedded derivatives are classified as FVTPL and all changes in fair value are recorded in profit or loss. The difference between the debt host component and the principal amount of the loan outstanding is accreted to profit or loss over the expected life of the convertible debenture.

The embedded derivatives were valued upon initial measurement and subsequent periods 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 include: the floor and ceiling conversion prices, the Company's Common Share price, the risk-free rate of return, expected volatility of the Company's Common Share price, forward foreign exchange rate curves (between the Cdn$ and U.S. Dollar) and spot foreign exchange rates.

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

14. CONVERTIBLE DEBENTURE (CONTINUED)

14.3 Valuation assumptions

The assumptions used in the Company's valuation models are as follows:

	As at	
	June 30, 2015	**December 31, 2014**
Floor conversion price	**Cdn$8.88**	Cdn$8.88
Ceiling conversion price	**Cdn$11.88**	Cdn$11.88
Common share price	**Cdn$0.80**	Cdn$0.50
Historical volatility	**71%**	69%
Risk free rate of return	**2.27%**	2.24%
Foreign exchange spot rate (Cdn$ to U.S. Dollar)	**0.80**	0.86
Forward foreign exchange rate curve (Cdn$ to U.S. Dollar)	**0.80 - 0.81**	0.85 - 0.86

14.4 Presentation

Based on the Company's valuation as at June 30, 2015, the fair value of the embedded derivatives decreased by $265 and increased by $1,279 compared to March 31, 2015 and December 31, 2014, respectively. The change in fair value was recorded as finance income and finance expense for the three and six months ended June 30, 2015, respectively.

For the three months ended June 30, 2015, the Company recorded interest expense of $5,089 related to the convertible debenture as a finance cost (2014: $5,021). For the six months ended June 30, 2015, the Company recorded interest expense of $10,061 related to the convertible debenture as a finance cost (2014: $9,985). The interest expense consists of the interest at the contract rate and the accretion of the debt host component of the convertible debenture. To calculate the accretion expense, the Company uses the contract life of 30 years and an effective interest rate of 22.2%.

The movements of the amounts due under the convertible debenture are as follows:

	Three months ended June 30,		Six months ended June 30,	
	2015	**2014**	**2014**	**2014**
Balance, beginning of period	**$ 101,703**	$ 100,568	**$ 95,187**	$ 96,603
Interest expense on convertible debenture	**5,089**	5,021	**10,061**	9,985
Increase/(decrease) in fair value of embedded derivatives	**(265)**	(121)	**1,279**	(1,120)
Interest paid	**-**	(7,934)	**-**	(7,934)
Balance, end of period	**$ 106,527**	$ 97,534	**$ 106,527**	$ 97,534

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

14. CONVERTIBLE DEBENTURE (CONTINUED)

The convertible debenture balance consists of the following amounts:

	As at	
	June 30, 2015	**December 31, 2014**
Current convertible debenture		
Interest payable	**$ 12,278**	$ 2,301
Non-current convertible debenture		
Debt host	**91,136**	91,052
Fair value of embedded derivatives	**3,113**	1,834
	94,249	92,886
Total convertible debenture	**$ 106,527**	$ 95,187

On May 20, 2015 under the terms of the CIC Convertible Debenture, CIC confirmed to the Company that subject to certain conditions and limitations, it had agreed to grant a deferral of payment of the approximately $7,900 in cash interest which was due by the Company to CIC on May 19, 2015 ("May 2015 cash interest installment") until July 22, 2015, subject to a three day cure period which expires on July 27, 2015.

On July 27, 2015, CIC confirmed to the Company that, subject to certain conditions and limitations, it had agreed to grant a further deferral of payment of the May 2015 cash interest installment until November 19, 2015 to allow the Company to execute its Proposed Funding Plan.

15. EQUITY

15.1 Share capital

The Company has authorized an unlimited number of common and preferred shares with no par value. At June 30, 2015, the Company had 240,519 common shares outstanding (December 31, 2014: 218,752) and no preferred shares outstanding (December 31, 2014: nil). The Company's volume weighted average share price for the six months ended June 30, 2015 was Cdn$0.75 (2014: Cdn$0.71).

15.2 Accumulated deficit and dividends

At June 30, 2015, the Company has accumulated a deficit of $906,532 (December 31, 2014: $848,177). No dividends have been paid or declared by the Company since inception.

15.3 Mandatory convertible units

On February 24, 2015 the Company entered into a private placement with Novel Sunrise. On March 3, 2015 pursuant to the private placement agreement Novel Sunrise subscribed for an initial tranche of 10,131 mandatory convertible units for subscription proceeds of $3,500. Each mandatory convertible unit issued to Novel Sunrise in the initial tranche is convertible on a one for one basis into a Common Share of the Company, resulting in a deemed issue price of CAD$0.432 per Common Share.

On April 23, 2015, the mandatory convertible units were converted into 10,131 Common Shares in the company.

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

16. SHARE-BASED PAYMENTS

16.1 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 Company is authorized to issue stock 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 plan include a maximum exercise period of 5 years and a vesting period of 3 years with 33% of the grant vesting on the first anniversary of the grant, 33% vesting on the second anniversary of the grant and 34% vesting on the third anniversary of the grant.

For the six months ended June 30, 2015, the Company granted 539 stock options (2014: 482) to officers, employees, directors and other eligible persons at exercise prices of Cdn$0.92 (2014: exercise price ranging from Cdn$0.65 to Cdn$0.84) and expiry dates of April 1, 2020 (2014: expiry date from January 13, 2019 to March 26, 2019). The weighted average fair value of the options granted in the six months ended June 30, 2015 was estimated at $0.15 (Cdn$0.16) per option at the grant date using the Black-Scholes option pricing model. (2014: $0.24 (Cdn$0.27))

The weighted average assumptions used for the Black-Scholes option pricing model were as follows:

	Six months ended June 30,	
	2015	**2014**
Risk free interest rate	**0.69%**	1.43%
Expected life	**3.5 years**	3.5 years
Expected volatility (i)	**65%**	56%
Expected dividend per share	**$nil**	$nil

(i) Expected volatility has been calculated based on historical volatility of the Company's publicly traded shares over a period equal to the expected life of the options.

A share-based compensation expense of $147 for the options granted in the six months ended June 30, 2015 (2014: $98) will be amortized over the vesting period, of which $23 was recognized in the six months ended June 30, 2015 (2014: $18).

The total share-based compensation expenses for the three months ended June 30, 2015 was $54 (2014: $230). Share-based compensation expense of $44 (2014: $94) has been allocated to administration expenses, $6 (2014: $127) has been allocated to cost of sales and $4 (2014: $9) has been allocated to evaluation and exploration expenses.

The total share-based compensation expenses for the six months ended June 30, 2015 was $186 (2014: $381). Share-based compensation expense of $145 (2014: $224) has been allocated to administration expenses, $34 (2014: $143) has been allocated to cost of sales and $7 (2014: $14) has been allocated to evaluation and exploration expenses.

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

16. SHARE-BASED PAYMENTS (CONTINUED)

16.2 Outstanding stock options

The option transactions under the stock option plan are as follows:

	Six months ended June 30, 2015		Six months ended June 30, 2014	
	Number of options	Weighted average exercise price (Cdn$)	Number of options	Weighted average exercise price (Cdn$)
Balance, beginning of period	3,052	$ 3.63	2,583	$ 8.48
Options granted	539	0.92	482	0.68
Options exercised	(12)	0.65	-	-
Options forfeited	(792)	0.72	(166)	1.79
Options expired	(455)	8.02	(751)	11.25
Balance, end of period	2,332	$ 3.15	2,148	$ 6.28

The stock options outstanding and exercisable as at June 30, 2015 are as follows:

	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)
0.65 to 1.92	1,760	$ 0.81	4.11	174	$ 1.55	2.81
6.16 to 9.43	290	8.19	1.35	290	8.19	1.35
12.58	282	12.58	0.12	282	12.58	0.12
	2,332	$ 3.15	3.29	746	$ 8.30	1.23

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

17. FAIR VALUE MEASUREMENTS

The fair value of all the 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 June 30, 2015			
Recurring measurements	**Level 1**	**Level 2**	**Level 3**	**Total**
Financial liabilities at fair value				
Convertible debenture - embedded derivatives	$ -	$ 3,113	$ -	$ 3,113
Total financial liabilities at fair value	**$ -**	**$ 3,113**	**$ -**	**$ 3,113**

	As at December 31, 2014			
Recurring measurements	**Level 1**	**Level 2**	**Level 3**	**Total**
Financial iabilities at fair value				
Convertible debenture - embedded derivatives	$ -	$ 1,834	$ -	$ 1,834
Total financial liabilities at fair value	**$ -**	**$ 1,834**	**$ -**	**$ 1,834**

At June 30, 2015, certain coal stockpile inventories were written down to their net realizable value of $1,901 (December 31, 2014: $1,220). The net realizable value has become the carrying value and will not be revalued. Certain assumptions used in the calculation of the net realizable value are categorized as Level 3 in the fair value hierarchy. There were no transfers between Level 1, 2 and 3 for the three months ended June 30, 2015.

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

18. RELATED PARTY TRANSACTIONS

During the six months ended June 30, 2015 and 2014, the Company had related party transactions with the following companies related by way of directors or shareholders in common:

- Turquoise Hill – Prior the completion of the Novel SPA and private placement with Novel Sunrise on April 23, 2015, Turquoise Hill was the Company's immediate parent company. TRQ's shareholding at April 1, 2015 was approximately 48% which declined to 23% at June 30, 2015 of the outstanding Common Shares following the completion of the Novel SPA. Turquoise Hill provides various administrative services to the Company on a cost-recovery basis.
- Rio Tinto – Prior to the completion of the Novel SPA and private placement with Novel Sunrise on April 23, 2015, Rio Tinto was the Company's ultimate parent company. The Company recovers administration and other costs incurred on behalf of Rio Tinto on a cost-recovery basis. Rio Tinto recovers from the Company the costs of salaries and benefits of employees assigned to work for the Company and recovers legal and professional fees from the Company in respect of the internal and tripartite committees.
- Turquoise Hill Resources Singapore Pte. Ltd. ("Turquoise Hill Singapore") – Turquoise Hill Singapore (formerly I2MS.NET Pte. Ltd.) is a private company 100% owned by Turquoise Hill. Turquoise Hill Singapore provides information technology and other related services to the Company on a cost-recovery basis.
- Mr. Wilson Chen – Mr. Chen is the former principal of Novel Sunrise. He was a related party for the period March 3, 2015 until July 16, 2015 and during this period the Interim Loan agreement was entered into, refer to note 13 for further details.

18.1 Related party expenses

The Company's related party expenses consist of the following amounts:

	Three months ended June 30,		Six months ended June 30,	
	2015	2014	2015	2014
Corporate administration	$ 130	$ 161	$ 211	$ 373
Salaries and benefits	204	350	144	899
Finance costs	107	157	213	157
Related party expenses	$ 441	$ 668	$ 568	$ 1,429

The Company's related party expenses relate to the following related parties:

	Three months ended June 30,		Six months ended June 30,	
	2015	2014	2015	2014
Turquoise Hill	$ 107	$ 227	$ 213	$ 241
Rio Tinto	251	358	192	911
Turquoise Hill Singapore	83	83	164	278
Related party expenses	$ 441	$ 668	$ 569	$ 1,430

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

18. RELATED PARTY TRANSACTIONS (CONTINUED)

18.2 Related party expenses recoveries

The Company's expenses recovered from a related party consist of the following amounts:

	Three months ended June 30,		Six months ended June 30,	
	2015	2014	2015	2014
Corporate administration	$ -	$ 17	$ -	$ 17

	Three months ended June 30,		Six months ended June 30,	
	2015	2014	2015	2014
Turquoise Hill	$ -	$ 17	$ -	$ 17
Related party expense recovery	$ -	$ 17	$ -	$ 17

18.3 Related party liabilities

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

	As at	
	June 30, 2015	December 31, 2014
Amounts payable to Rio Tinto	$ 8,093	$ 8,047
Accounts payable to Turquoise Hill Singapore	383	278
Accounts payable to Turquoise Hill	4,327	4,151
Total liabilities due to related parties	$ 12,803	$ 12,476

19. SUPPLEMENTAL CASH FLOW INFORMATION

19.1 Net change in non-cash working capital items

The net change in the Company's non-cash working capital items is as follows:

	Six months ended June 30,	
	2015	2014
Decrease/(increase) in inventories	$ 90	$ (7,121)
Decrease/(increase) in trade and other receivables	(3,126)	1,436
Decrease in prepaid expenses and deposits	241	5,840
Increase/(decrease) in trade and other payables	5,145	(13,290)
Increase in provision for court case penalty	18,049	-
Increase/(decrease) in deferred revenue	(392)	12,995
Net change in non-cash working capital items	$ 20,007	$ (140)

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

20. COMMITMENTS FOR EXPENDITURE

As at June 30, 2015, the Company's commitments for expenditure that have not been disclosed elsewhere in the consolidated financial statements are as follows:

	As at June 30, 2015			
	Within 1 year	2-3 years	Over 3 years	Total
Capital expenditure commitments	$ 2,205	$ 15,826	$ -	$ 18,031
Operating expenditure commitments	9,838	963	263	11,064
Commitments	**$ 12,043**	**$ 16,789**	**$ 263**	**$ 29,095**

21. CONTINGENCIES

	As at	
	June 30, 2015	December 31, 2014
Provision for court case penalty	$ 18,049	$ -

21.1 Governmental and regulatory investigations

The Company was subject to investigations by the IAAC regarding allegations of breaches of Mongolia's anti-corruption laws (the "Anti-Corruption Case"), tax evasion and money laundering (the "Tax Evasion Case"). On March 18, 2013 the Prosecutor's Office decided to split the Tax Evasion Case from the Anti-Corruption Case and on April 12, 2013, the Public Prosecutor of Capital city Prosecutor's Office issued a resolution that the jurisdiction to conduct the investigation on Tax Evasion Case was with the SIA and not the IAAC, and the Tax Evasion Case was transferred to SIA.

While the IAAC has not made any formal accusations against any current or former employee of the Company or the Company under the Anti-Corruption Case, administrative penalties were imposed on certain of the Company's Mongolian assets in connection with the investigation, including a restriction of the use of $1,200 (the "Restricted Funds") held in bank accounts in Mongolia to spending in Mongolia. The Company has been informed that the Anti-Corruption Case has been suspended; however, it has not received formal notice that the investigation is completed and the restriction on the Restricted Funds remains in place. The Restricted Funds are included within the prepaid expenses and deposits balance in the Company's financial statements. This restriction may have a material impact on the Company's activities in light of the tax penalty (MNT 35.3 billion as declared by the tax verdict).

Investigations under the Tax Evasion Case included investigations of three of the Company's former employees (the "Former Employees"). On December 30, 2014, the Capital City Prosecutor's Office (Ulaanbaatar, Mongolia) dismissed the allegations of money laundering as not having been proven during the investigation. The Former Employees were indicted for tax evasion by the Prosecutor General on March 14, 2014. The case was sent to the First Instance Second District Criminal Court of Justice (the "District Court"). The Company was advised on May 12, 2014 that the appointed judge of the District Court concluded that the investigation of the Tax Evasion Case initiated by IAAC and continued by SIA was incomplete and ordered the case to be returned to the Prosecutor General for additional investigation. The additional investigation was subsequently completed and the case was sent to the District Court again on June 4, 2014. The trial took place on August 25 and 26, 2014. A panel of three judges appointed to the case returned the case to the Prosecutor General once again for further investigation due to insufficient evidence presented by the prosecutor.

21. CONTINGENCIES (CONTINUED)

On October 7, 2014, based on the District Court verdict, the SIA ordered a re-investigation (the "Fourth Investigation") into allegations of violations of Mongolian tax laws by the Former Employees. Following the completion of the Fourth Investigation, the Former Employees were indicted again on December 31, 2014 and were subsequently tried in the District Court. On January 30, 2015, the panel of appointed judges from the District Court found the Former Employees guilty of tax evasion and imposed sentences on the Former Employees ranging from 5 years and 6 months to 5 years and 10 months of imprisonment in the correctional facilities of strict regimen in Mongolia. The Former Employees were immediately imprisoned. The Company was informed that, following the receipt of the Tax Verdict, the Former Employees requested pardons from the President of Mongolia and waived their right of appeal. On February 26, 2015 the President of Mongolia issued a decree to pardon to the Former Employees. The Former Employees were released from imprisonment following the decree and departed Mongolia.

The Tax Verdict declared SouthGobi Sands LLC ("SGS"), the Company's wholly-owned subsidiary, to be financially liable as a "civil defendant" for a penalty (the "Tax Penalty") of MNT35.3 billion (approximately $18,049 on June 30, 2015). The Company firmly rejects this conclusion.

On February 18, 2015, the Company appealed the Tax Verdict (the "Tax Verdict Appeal") on the grounds that it has prepared its financial statements, including those of SGS, in compliance with IFRS, and lodged all its tax returns in the required format under Mongolian tax law. The hearing of the Tax Penalty Appeal took place on March 25, 2015 at the 10th Appeal Court for Criminal Case of Mongolia (the "Court of Appeal") and a panel of three appointed judges decided to uphold the Tax Verdict and dismissed the Tax Verdict Appeal by the Company. It is the view of the Company that there is a lack of evidence to support both the Tax Verdict and the Appeal Verdict. The Company received the written version of the Appeal Court's verdict ("Appeal Verdict") on April 10, 2015. The Company lodged a final appeal with the Supreme Court of Mongolia on April 22, 2015. In accordance with Mongolia's criminal procedure law, SGS filed the appeal with the Supreme Court of Mongolia through the Second District Criminal Court of Justice.

On April 29, 2015 the Second District Criminal Court refused to advance SGS's appeal to the Supreme Court. Following an immediate protest by SGS, the Second District Criminal Court delivered SGS's appeal to the Supreme Court of Mongolia.

On May 20, 2015, SGS was informed that the Supreme Court had refused to hear the appeal and had returned the appeal to the Second Criminal Court of Justice. The Supreme Court based its decision on a restrictive reading of Article 342 of the Criminal Procedure Law of Mongolia which stipulates that "the defendant, person acquitted, the victim, and their respective defense counsel have the right to lodge a complaint to the Supreme Court". The Supreme Court concluded that the omission of a specific reference to a civil defendant in Article 342, in and of itself denies SGS, in such capacity, the right to lodge an appeal to the Supreme Court.

In its decision, the Supreme Court did not address other provisions of the Criminal Procedure Law and the Law on Courts of Mongolia, which provide that civil defendants have standing to appeal to the Supreme Court and that no judicial proceedings or decisions in Mongolia are outside of the scope of supervision by the Supreme Court.

21. CONTINGENCIES (CONTINUED)

On May 21, 2015, SGS sent an official letter of protest to the Presiding Justice of the Criminal Chamber of the Supreme Court (the "Presiding Justice"), challenging the decision to refuse to hear the tax case on appeal. On June 2, 2015, SGS received a formal response from the Presiding Justice, confirming the Supreme Court's refusal to hear the tax case. In the letter, the Presiding Justice reaffirmed the restrictive interpretation of Article 342 of the Criminal Procedure Law.

With the refusal by the Supreme Court to hear the case on appeal, the Tax Verdict has entered into force. The Tax Verdict is, however, not immediately payable and enforceable against SGS absent further actions prescribed by the laws of Mongolia. In particular, SGS has not received a copy of the bailiff's resolution on execution of the Tax Verdict, as required under the Law of Mongolia on Execution of Court Decisions in order for any judgment execution process to happen. However, the Company made a corresponding provision for the court case penalty of $18,049 as at June 30, 2015 given the Tax Verdict has entered into force.

The Company continues to believe that there is a lack of evidence to support the Tax Verdict and that the Tax Verdict and the subsequent decisions of the higher courts on appeal were substantively and procedurally in error under the laws of Mongolia.

While the Company had various additional legal avenues available to it to continue defending itself, it has decided to and is currently seeking to resolve amicably the dispute giving rise to the Tax Verdict in a manner that is both appropriate having regard to the Company's limited financial resources and supportive of a positive environment for foreign investment in Mongolia. There can be no assurance, however, that any such resolution can be successfully negotiated by the Company either at all or on favourable terms, or that the terms of any resolution to which the Government would be prepared to agree would not be materially adverse to the Company. In such case, this may result in an event of default under the Debenture held by CIC and CIC would have the right to declare the full principal and accrued interest owing thereunder immediately due and payable. Such an event of default under the Debenture or the Company's inability to pay the penalty could result in voluntary or involuntary proceedings involving the Company (including bankruptcy). However, with the Presiding Justice having upheld the decision to refuse to hear the case on appeal, this exhausts the legal appeals available to the Company in Mongolia.

21. CONTINGENCIES (CONTINUED)

21.2 Internal investigations

Commencing in September 2012, through its Audit Committee (comprised solely of independent directors), the Company has conducted an internal investigation into possible breaches of law, internal corporate policies and codes of conduct arising from the allegations which have been raised through the investigations in Mongolia. The Chair of the Audit Committee has also participated in a tripartite committee, comprised of the Audit Committee Chairs of the Company and Turquoise Hill and a representative of Rio Tinto, which focused on the investigation of a number of those allegations, including possible violations of anti-corruption laws. The tripartite committee substantially completed the investigative phase of its activities during the third quarter of 2013. There have been no significant developments in respect of the internal investigations since the completion of the investigative phase during the third quarter of 2013.

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

In the opinion of management of the Company, at June 30, 2015 a provision for this matter is not required.

21.3 Mongolian IAAC investigation

In the first quarter of 2013, the Company was subject to orders imposed by Mongolia's Independent Authority against Corruption (the "IAAC") which placed restrictions on certain of the Company's Mongolian assets. The orders were imposed on the Company in connection with the IAAC's investigation of the Company and were continued to be enforced by the Mongolian State Investigation Office (the "SIA"). The restrictions on the assets were reaffirmed in the Tax Verdict and form part of the Tax Penalty payable by the Company.

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

Following a review by the Company and its advisers, it is the Company's view that the orders placing restrictions on certain of the Company's Mongolian assets did not result in an event of default as defined under the terms of the CIC Convertible Debenture. However, the enforcement of the orders could ultimately result in an event of default of the Company's CIC Convertible Debenture, which if remains uncured for ten business days, would result in the principal amount owing and all accrued and unpaid interest will become immediately due and payable upon notice to the Company by CIC.

21. CONTINGENCIES (CONTINUED)

21.4 Class action lawsuit

On or about January 6, 2014, Siskinds LLP, a Canadian law firm, filed a proposed securities class action (the "Ontario Action") against the Company, certain of its former senior officers and current directors, and its former auditors, Deloitte LLP, in the Ontario Superior Court of Justice in relation to the Company's restatement of financial statements as previously disclosed in the Company's public filings.

There have been no significant developments in respect of the class action lawsuit since the first quarter ended March 31, 2014.

The Company disputes and will vigorously defend itself against these claims through independent Canadian litigation counsel retained by the Company and the other defendants for this purpose. Due to the inherent uncertainties of litigation, it is not possible to predict the final outcome of the Ontario Action or determine the amount of any potential losses, if any. However, the Company has judged a provision for this matter at June 30, 2015 is not required.

21.5 Toll wash plant agreement with Ejin Jinda

In 2011, the Company entered into an agreement with Ejin Jinda, a subsidiary of China Mongolia Coal Co. Ltd. to toll-wash coals from the Ovoot Tolgoi Mine. The agreement has a duration of five years from commencement of the contract and provides for an annual wet washing capacity of approximately 3.5 million tonnes of input coal.

In 2011, the Company made an initial payment of $33,556 in respect of prepaid toll washing fees. The Company recorded a $30,152 impairment loss on the $33,556 of prepaid toll washing fees during the year ended December 31, 2013 and in the quarter ended June 30, 2014, the Company recorded an additional impairment of $3,405 to fully impair the deposit. As at June 30, 2015 the Company has reassessed the carrying value of this prepayment and continues to believe it is appropriate for the balance to be fully impaired. This impairment continues to be recognized due to the continued delay in starting the commercial operations at the wet washing facility and the continued soft coal market in China.

Under the original agreement with Ejin Jinda, which required the commercial operation of the wet washing facility to commence on October 1, 2011, the additional fees payable by the Company under the wet washing contract would have been $18,500. The Company assesses on a continuous basis the agreement with Ejin Jinda and has determined it is not probable that the $18,500 will be required to be paid.

The Company's objective continues to be the implementation of an effective and profitable wet washing solution, and the Company is cooperating with Ejin Jinda in reviewing the utilization of the wet washing facility.

21. CONTINGENCIES (CONTINUED)

21.6 Special Needs Territory in Umnugobi

On February 13, 2015, the whole of the Soumber mining license and a portion of SGS' exploration license No.9443 X (the "License Areas") were included into a special protected area (to be further referred as Special Needs Territory "SNT") newly set up by the Umnugobi Aimag's Civil Representatives Khural (the "CRKh") to establish a strict regime on the protection of natural environment and prohibit mining activities in the territory of the SNT.

In March 2015, SGS filed a complaint with the 12th Court for Administrative Cases of First Instance (the "Administrative Court") seeking the annulment of CRKh's decision to the extent it impacted the License Areas. In parallel, SGS initiated negotiations with the CRKh in order to reach an acceptable solution.

On July 8, 2015, SGS and the Chairman of the CRKh, in his capacity as the respondent's representative, reached an agreement (the "Amicable Resolution Agreement") to exclude the License Areas from the territory of the SNT in full, subject to confirmation of the Amicable Resolution Agreement by the session of the CRKh. The parties formally submitted the Amicable Resolution Agreement to the appointed judge of the Administrative Court for her approval and requested a dismissal of the case in accordance with the Law of Mongolia on Administrative Court Procedure. On July 10, 2015, the judge issued her order approving the Amicable Resolution Agreement and dismissing the case, while reaffirming the obligation of CRKh to take necessary actions at its next session to exclude the License Areas from the SNT and register the new map of the SNT with the relevant authorities. The Company has not yet received any indication on the timing of the next session of the CRKh.

21.7 Commercial arbitration in Hong Kong

On June 24, 2015, First Concept Logistics Limited ("First Concept") served a notice of arbitration (the "Notice") on SGS in respect of a coal supply agreement dated May 19, 2014 as amended on June 27, 2014 (the "Coal Supply Agreement"). The arbitral proceedings (the "Arbitration") are deemed to have commenced on June 24, 2015, as the date when the respondent received the Notice.

According to the Notice, First Concept: alleged, *inter alia*, (i) that SGS had failed and/or wrongfully refused to sell any coal to First Concept; (ii) expressed its wish to have the dispute settled in an arbitration to be administered by the Hong Kong International Arbitration Centre; and (iii) sought the repayment of the prepayment, in the sum of $11,500, it made to SGS under the Coal Supply Agreement, as well as any and all damages that may be due to it.

Under the Coal Supply Agreement, SGS agreed to sell coal to First Concept between May 22, 2014 and May 31, 2015 for a total consideration of $11,500. It was also agreed that that First Concept would pre-pay the $11,500. While First Concept fulfilled its payment obligation under the contract, it totally failed to fulfill its obligation to collect and transport the coal. Pursuant to the Coal Supply Agreement that obligation fell squarely on First Concept, while SGS was only obliged to make the coal available at its stockpile. The sole reason for the lack of coal sales to First Concept was the continued failure of First Concept to complete the necessary legal requirements for collection and transportation of coal and to provide a pickup schedule in accordance with industry practice. Contrary to the allegation by First Concept that SGS "wrongfully refused" to sell the coal, SGS has repeatedly advised First Concept of its willingness, ability and readiness to make available the coal for collection at its stockpile. In fact, SGS, at all times during the term of the Coal Supply Agreement, had more than sufficient coal at its stockpile to meet its obligations.

21. CONTINGENCIES (CONTINUED)

The Company, therefore, firmly rejects the allegations of First Concept in the Notice as lacking any merit and will vigorously defend itself in the Arbitration, including claiming the relevant fees and damages from First Concept.

There can be no assurance, however, that the Company will prevail in the Arbitration. Should SGS be unsuccessful in the Arbitration, the Company may not be able to re-pay the sum of $11,500. In such case, this may result in an event of default under the Debenture held by CIC and CIC would have the right to declare the full principal and accrued interest owing thereunder immediately due and payable. Such an event of default under the Debenture or the Company’s inability to re-pay the $11,500 to First Concept could result in voluntary or involuntary proceedings involving the Company.

21.8 Notice of claim by former Chief Executive Officer

On June 30, 2015, the Company was served with a Notice of Civil Claim filed by the Company's former President and Chief Executive Officer, Alexander Molyneux, in the British Columbia Supreme Court. The claim relates to alleged breaches of Mr. Molyneux's employment agreement by the Company. In addition to the Company, Turquoise Hill Resources Ltd., the Company's largest shareholder at the time of Mr. Molyneux's employment, was also named in the claim.

Mr. Molyneux acted as the Company's President (from April 2009) and Chief Executive Officer (from October 2009) until September 2012, when the Company terminated his employment.

Mr. Molyneux is seeking damages in excess of $1,000 in his Notice of Claim. The Company considers the action is without merit. SouthGobi intends to vigorously defend the action and reserves its right to pursue all legal rights and remedies available to it in connection with the proceedings.

21.9 Tax legislation

Mongolian tax, currency and customs legislation is subject to varying interpretations, and changes, which can occur frequently. Management’s interpretation of such legislation as applied to the transactions and activity of the Company may be challenged by the relevant authorities. The Mongolian tax authorities may be taking a more assertive position in their interpretation of the legislation and assessments, and it is possible that transactions and activities that have not been challenged in the past may be challenged by tax authorities. As a result, significant additional taxes, penalties and interest may be assessed. Fiscal periods remain open to review by the authorities in respect of taxes for five calendar years preceding the year of review. Under certain circumstances reviews may cover longer periods.

The Mongolian tax legislation does not provide definitive guidance in certain areas, specifically in areas such as Value-Added Tax, withholding tax, corporate income tax, personal income tax, transfer pricing and other areas. From time to time, the Company adopts interpretations of such uncertain areas that reduce the overall tax rate of the Company. As noted above, such tax positions may come under heightened scrutiny as a result of recent developments in administrative and court practices. The impact of any challenge by the tax authorities cannot be reliably estimated; however, it may be significant to the financial position and/or the overall operations of the entity.

21. CONTINGENCIES (CONTINUED)

Management believes that its interpretation of the relevant legislation is appropriate and the Company's positions related to tax and other legislation will be sustained. Management believes that tax and legal risks are remote at present. The management performs regular re-assessment of tax risk and its position may change in the future as a result of the change in conditions that cannot be anticipated with sufficient certainty at present.

As of June 30, 2015, management has assessed that recognition of a provision for uncertain tax position is not necessary.

22. SUBSEQUENT EVENTS

Novel Sunrise change in ownership

The Company notes the announcement by Novel Sunrise, the largest shareholder of the Company, on July 20, 2015 which reported that China Cinda (HK) Investments Management Company Limited ("Cinda"), a wholly-owned subsidiary of China Cinda Asset Management Corporation Limited, acquired ownership and control of all of the outstanding voting (ordinary) shares of Novel Sunrise through Hope Rosy Limited, a wholly-owned subsidiary of Cinda.

(Expressed in thousands of U.S. Dollars and shares/units in thousands, unless otherwise indicated)

ADDITIONAL STOCK EXCHANGE INFORMATION

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

A1. TAXATION ON PROFITS

The Company and its subsidiaries are subject to income or profits tax in the jurisdictions in which the Company operates, including Canada, Hong Kong, Singapore and Mongolia. Income or profits tax was not provided for the Company's operations in Canada, Hong Kong or Singapore as the Company had no assessable income or profit arising in or derived from these jurisdictions.

For the six months ended June 30, 2015 the Company recorded current income tax expense of $1 (2014: $546) related to withholding tax and assessable profit derived from Mongolia at prevailing rates. For the six months ended June 30, 2015, the Company did not record any deferred income tax expenses (2014: nil).

A2. FINANCIAL INSTRUMENTS

Cash

The Company's cash is denominated in the following currencies:

	As at	
	June 30, 2015	**December 31, 2014**
Denominated in U.S. Dollars	**$ 417**	$ 2,553
Denominated in Chinese Renminbi	**1**	587
Denominated in Mongolian Tugriks	**128**	77
Denominated in Canadian Dollars	**70**	333
Denominated in Hong Kong Dollars	**285**	239
Cash	**$ 901**	$ 3,789

Exposure to fluctuations in foreign exchange rates

The sensitivity of the Company's comprehensive income due to changes in the carrying values of assets and liabilities denominated in foreign currencies is as follows. A positive number indicates an increase in comprehensive income, whereas a negative number indicates a decrease in comprehensive income.

	As at	
	June 30, 2015	**December 31, 2014**
Increase/ decrease in foreign exchange rate against US Dollar		
+5%	**$ 29**	$ 66
–5%	**(29)**	(66)

A3. COMPLIANCE WITH THE CODE ON CORPORATE GOVERNANCE PRACTICES

The Company has, throughout the six months ended June 30, 2015, applied the principles and complied with the requirements of its corporate governance practices as defined by the Board of Directors and all applicable statutory, regulatory and stock exchange listings standards.

A4. COMPLIANCE WITH MODEL CODE

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

The Board of Directors confirms that all of the Directors of the Company have complied with the required policies in the Company's Corporate Disclosure, Confidentiality and Securities Trading policy throughout the six months ended June 30, 2015.

A5. DIRECTORS' INTERESTS IN SHARES AND SHARE OPTIONS

As at June 30, 2015, the interests of the Company's directors in the shares and share options of the Company and its associated corporations are presented in the following tables.

A5. DIRECTORS' INTERESTS IN SHARES AND SHARE OPTIONS (Continued)

Shares (i)

Name	Name of company	Nature of interest	Shares held	Percentage interest in the
Ted Chan	SouthGobi Resources Ltd.	N/A	Nil	Nil
	Turquoise Hill Resources Ltd.	N/A	Nil	Nil
	Rio Tinto Limited	N/A	Nil	Nil
	Rio Tinto plc	N/A	Nil	Nil
	Novel Sunrise Investments Limited	N/A	Nil	Nil
André Deepwell (ii)	SouthGobi Resources Ltd.	Direct/Indirect	45,000	0.02%
	Turquoise Hill Resources Ltd.	N/A	Nil	Nil
	Rio Tinto Limited	N/A	Nil	Nil
	Rio Tinto plc	N/A	Nil	Nil
	Novel Sunrise Investments Limited	N/A	Nil	Nil
Yulan Guo	SouthGobi Resources Ltd.	N/A	Nil	Nil
	Turquoise Hill Resources Ltd.	N/A	Nil	Nil
	Rio Tinto Limited	N/A	Nil	Nil
	Rio Tinto plc	N/A	Nil	Nil
	Novel Sunrise Investments Limited	N/A	Nil	Nil
Gordon Lancaster	SouthGobi Resources Ltd.	N/A	Nil	Nil
	Turquoise Hill Resources Ltd.	N/A	Nil	Nil
	Rio Tinto Limited	N/A	Nil	Nil
	Rio Tinto plc	N/A	Nil	Nil
	Novel Sunrise Investments Limited	N/A	Nil	Nil
Pierre Lebel	SouthGobi Resources Ltd.	Direct	5,100	0.00%
	Turquoise Hill Resources Ltd.	N/A	Nil	Nil
	Rio Tinto Limited	N/A	Nil	Nil
	Rio Tinto plc	N/A	Nil	Nil
	Novel Sunrise Investments Limited	N/A	Nil	Nil
Ningqiao Li	SouthGobi Resources Ltd.	N/A	Nil	Nil
	Turquoise Hill Resources Ltd.	N/A	Nil	Nil
	Rio Tinto Limited	N/A	Nil	Nil
	Rio Tinto plc	N/A	Nil	Nil
	Novel Sunrise Investments Limited	N/A	Nil	Nil
Kelly Sanders (iii)	SouthGobi Resources Ltd.	N/A	Nil	Nil
	Turquoise Hill Resources Ltd.	N/A	Nil	Nil
	Rio Tinto Limited	N/A	Nil	Nil
	Rio Tinto plc	Direct	103,556	0.01%
	Novel Sunrise Investments Limited	N/A	Nil	Nil

(i) Amounts are presented in total shares held and are not in thousands of shares.
(ii) Included 43,000 shares of SouthGobi Resources held by the spouse of Mr. Deepwell
(iii) Includes 36,556 vested shares and 67,000 unvested shares

A5. DIRECTORS' INTERESTS IN SHARES AND SHARE OPTIONS (Continued)

Options (i)

Name	Name of company	Number of options held
Ted Chan	SouthGobi Resources Ltd.	Nil
	Turquoise Hill Resources Ltd.	Nil
	Rio Tinto Limited	Nil
	Rio Tinto plc	Nil
	Novel Sunrise Investments Limited	Nil
André Deepwell	SouthGobi Resources Ltd.	367,352
	Turquoise Hill Resources Ltd.	Nil
	Rio Tinto Limited	Nil
	Rio Tinto plc	Nil
	Novel Sunrise Investments Limited	Nil
Yulan Guo	SouthGobi Resources Ltd.	Nil
	Turquoise Hill Resources Ltd.	Nil
	Rio Tinto Limited	Nil
	Rio Tinto plc	Nil
	Novel Sunrise Investments Limited	Nil
Gordon Lancaster	SouthGobi Resources Ltd.	477,352
	Turquoise Hill Resources Ltd.	Nil
	Rio Tinto Limited	Nil
	Rio Tinto plc	Nil
	Novel Sunrise Investments Limited	Nil
Pierre Lebel	SouthGobi Resources Ltd.	372,352
	Turquoise Hill Resources Ltd.	Nil
	Rio Tinto Limited	Nil
	Rio Tinto plc	Nil
	Novel Sunrise Investments Limited	Nil
Ningqiao Li	SouthGobi Resources Ltd.	Nil
	Turquoise Hill Resources Ltd.	Nil
	Rio Tinto Limited	Nil
	Rio Tinto plc	Nil
	Novel Sunrise Investments Limited	Nil
Kelly Sanders	SouthGobi Resources Ltd.	Nil
	Turquoise Hill Resources Ltd.	Nil
	Rio Tinto Limited	Nil
	Rio Tinto plc	9,601
	Novel Sunrise Investments Limited	Nil

(i) Amounts are presented in total options held and are not in thousands of options.

SouthGobi Resources Ltd.

Management's Discussion and Analysis of Financial Condition and Results of Operations

June 30, 2015
(Expressed in U.S. Dollars)

FORWARD-LOOKING STATEMENTS

Except for statements of fact relating to the Company, certain information contained herein constitutes forward-looking statements. Forward-looking statements are frequently characterized by words such as "plan", "expect", "project", "intend", "believe", "anticipate", "could", "should", "seek", "likely", "estimate" 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 times 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 statements include, but are not limited to, statements regarding:

- anticipated stock market conditions, the future prices of the Company's common shares (the "Common Shares") and ownership thereof;
- the Company's anticipated business activities, planned expenditures and corporate strategies;
- the Company's intention to develop markets for its semi-soft coking coal brands and to pursue long-term supply offtake agreements with end users in the People's Republic of China ("China");
- costs relating to anticipated capital expenditures and the 2015 exploration program;
- the Company's anticipated financing needs, development plans and future production levels;
- expected impacts of the administrative restrictions on certain of the Company's Mongolian assets and the anticipated impact on the Company's activities;
- the impact of future disclosure of the results of the internal investigations being conducted by the Company's Audit Committee;
- the results and impact of the Ontario Action (as defined under the heading "REGULATORY ISSUES AND CONTINGENCIES – Contingencies – Class Action Lawsuit" in this Management Discussion and Analysis of Financial Condition and Results of Operations ("MD&A"));
- the ability of the Company to pay the Tax Penalty and the possible consequences to the Company of the Tax Verdict and Appeal Verdict (each as defined under the heading "OVERVIEW – *Significant Events and Highlights*" in this MD&A);
- the potential effect of the list of licenses published by the Government of Mongolia covering areas in which exploration and mining is purportedly prohibited on the Company's mining licenses;
- the Company's expectations of sufficient liquidity and capital resources to meets its ongoing obligations and future contractual commitments, including the Company's ability to secure additional funding and to meet its obligations under the China Investment Corporation ("CIC") convertible debenture (the "CIC Convertible Debenture") as the same become due;
- the possible impact of changes to the inputs to valuation model used to value the embedded derivatives in the CIC Convertible Debenture;
- the estimates and assumptions included in the Company's impairment analysis and the possible impact of changes thereof;
- the possible impacts of changes in useful life or depreciation rates on depreciation expenses;
- the potential effects of a difference between future cash flows and profits from estimates;
- estimates of the Company's mineral reserves and resources; the possible impact of the review of the geology type at the Ovoot Tolgoi Mine and the as yet uncompleted revisions to Ovoot Tolgoi mine plan on quantities of measured and/or indicated resources and reserves of the Ovoot Tolgoi project; the impact of the completion of the paved highway;
- the ability for higher-ash product to be sold as a thermal coal product; the type of coal products being produced; the ability to preserve liquidity and continue on a sustainable basis; the ability of the Company to meet the targeted annual capacity of run-of-mine production; the anticipated increase of production from the Ovoot Tolgoi Mine (as defined under the heading "OVERVIEW" in this MD&A) to anticipated annual capacity of 9 million tonnes run-of-mine production;

- the ability of the Company to successfully review the utilization of the wet washing facility and enhance the quality of its coal products through a beneficiation process based on wet washing;
- the agreement with Ejin Jinda and payments thereunder;
- the Company's review of the use of the dry coal handling facility ("DCHF") (as defined under the heading "OVERVIEW OF OPERATIONAL DATE AND FINANCIAL RESULTS – Overview of Quarterly Financial Results" in this MD&A) and plans regarding the use of the DCHF;
- the future mining operations at the Soumber Deposit (as defined under the heading "PROPERTIES – Development Projects and Exploration Program – Soumber Deposit" in this MD&A) being allowed to share the existing infrastructure with the Ovoot Tolgoi Mine;
- plans for the progress of mining license application processes;
- future coal market conditions in China and the related impact on the Company's margins and liquidity;
- the outcome of the issues described under the heading "REGULATORY ISSUES AND CONTINGENCIES" in this MD&A;
- business outlook, including the outlook for the remainder of 2015 and beyond;
- the implementation and impact of the Proposed Funding Plan (as defined under the heading "OVERVIEW – Going Concern" in this MD&A) and actions to be taken under the Proposed Funding Plan;
- the outcome and results of the TSX's (as defined under the heading "OVERVIEW" in this MD&A) remedial delisting review of the Company;
- the Company continuing as a going concern and its ability to realize its assets and discharge its liabilities in the normal course of operations as they become due; adjustments to the amounts and classifications of assets and liabilities in the Company's financial statements and the impact thereof; the Company's objectives for the remainder of 2015 and beyond, including plans regarding the 2015 exploration program;
- expected production at the Ovoot Tolgoi Mine;
- the capacity of the paved highway;
- the impact of amendments to, or the application of the laws of Mongolia and other countries in which the Company carries on business;
- the impact of the Company's activities on the environment and actions taken for the purpose of mitigation of potential environmental impacts and planned focus on health, safety and environmental performance;
- the outcome of legal proceedings involving the Company and its former Chief Executive Officer, Mr. Alexander Molyneux;
- the outcome of arbitration proceedings involving the Company and First Concept Logistics Limited with respect a coal supply agreement and payments thereunder;
- greenfield development options with the Soumber Deposit and Zag Suuj Deposit (as defined under the heading "PROPERTIES – Development Projects and Exploration Program" in this MD&A); and
- other statements that are not historical facts.

This list is not exhaustive of the factors that may affect any of the Company's forward-looking statements. Except as required by law, the Company undertakes no obligation to update forward-looking statements if circumstances or management's estimates or opinions should change. The reader is cautioned not to place undue reliance on forward-looking statements.

TABLE OF CONTENTS

INTRODUCTION

This Management's Discussion and Analysis of Financial Condition and Results of Operations ("MD&A") of SouthGobi Resources Ltd. (which, together with its subsidiaries, is collectively referred to as the "Company") should be read in conjunction with the condensed consolidated interim financial statements of the Company and the notes thereto for the three and six months ended June 30, 2015. The Company's condensed consolidated interim financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") issued by the International Accounting Standards Board and Interpretations of the IFRS Interpretations Committee.

The functional currency of all of the Company's operations is the U.S. Dollar. All figures in this MD&A are presented in U.S. Dollars unless otherwise stated.

Disclosure of a scientific or technical nature in this MD&A, as derived from the technical report on the Ovoot Tolgoi Deposit dated March 19, 2012 (the "Ovoot Tolgoi Technical Report"), the technical report on the Soumber Deposit dated March 25, 2013 (the "Soumber Technical Report") and the technical report on the Zag Suuj Deposit dated March 25, 2013 (the "Zag Suuj Technical Report"), in respect of the Company's applicable material mineral projects was prepared by or under the supervision of the Qualified Persons (as that term is defined in NI 43 – 101) ("QPs") listed below. Copies of the Ovoot Tolgoi Technical Report, the Soumber Technical Report and the Zag Suuj Technical Report are available on SEDAR at www.sedar.com.

Property	Qualified Persons	Field of Expertise	Relationship to Company
Ovoot Tolgoi	Merryl Peterson	Resources	Independent Consultant
Ovoot Tolgoi	Robert Mackenzie	Reserves	Independent Consultant
Ovoot Tolgoi	Ross Seedsman	Geotechnical	Independent Consultant
Ovoot Tolgoi	David Morris	Dry Coal Processing	Independent Consultant
Ovoot Tolgoi	Michael Evans	Wet Coal Processing	Independent Consultant
Soumber	Merryl Peterson	Resources	Independent Consultant
Zag Suuj	Merryl Peterson	Resources	Independent Consultant

Other disclosures of a scientific or technical nature in this MD&A in respect of the Ovoot Tolgoi Mine and the Soumber and Zag Suuj projects were prepared by employees of the Company and reviewed by Robert Mackenzie, an employee of RungePincockMinarco, a registered member and Chartered Professional (Mining) of the Australasian Institute of Mining and Metallurgy (Member No. 103878) and a Qualified Person, as that term is defined in NI 43-101. Robert Mackenzie was the Qualified Person responsible for overall preparation of and the coal reserve estimates in the Ovoot Tolgoi Technical Report.

1. OVERVIEW

The Company is an integrated coal mining, development and exploration company with 346 employees as at June 30, 2015. The Common Shares trade on the Toronto Stock Exchange ("TSX") under the symbol "SGQ" and on the Stock Exchange of Hong Kong ("HKEX") under the stock code symbol "1878".

The Company owns the following significant coal project in Mongolia: the Ovoot Tolgoi open pit coal mine (the "Ovoot Tolgoi Mine") and the following significant development projects, the Ovoot Tolgoi Underground Deposit, the Soumber Deposit and the Zag Suuj Deposit. These projects are located in the Umnugobi Aimag (South Gobi Province) of Mongolia, within 150 kilometers ("km") of each other and in close proximity to the Mongolia-China border. The Ovoot Tolgoi Mine, together with the Ovoot Tolgoi Underground Deposit, forms the Ovoot Tolgoi Complex. The Company owns a 100% interest in these coal projects.

The Ovoot Tolgoi Mine, strategically located approximately 40km from the Shivee Khuren-Ceke crossing at the Mongolia-China border ("Shivee Khuren Border Crossing"), is the Company's flagship asset. The Company commenced mining at the Ovoot Tolgoi Mine in 2008 and the Company sells coal at the mine-gate to Chinese customers. Ceke, at the Chinese side of the Shivee Khuren Border Crossing, is a major Chinese coal distribution terminal with rail connections to key coal markets in China.

Saleable products from the Ovoot Tolgoi Mine include the SouthGobi standard ("Standard") and SouthGobi premium ("Premium") semi-soft coking coal products as well as higher-ash product which is sold as a thermal coal product.

COAL RESERVES *(millions of tonnes)* (i)

Property	Proven	Probable	Total
Ovoot Tolgoi Mine (ii)	**119**	**57**	**176**

COAL RESOURCES *(millions of tonnes)* (i)

Property	Measured	Indicated	Measured & Indicated	Inferred
Ovoot Tolgoi Mine (ii)	133	60	193	24
Ovoot Tolgoi Underground	66	43	109	62
Soumber Deposit	63	110	173	123
Zag Suuj Deposit	-	22	22	84
Total coal resources	**262**	**235**	**497**	**293**

(i) As at June 30, 2015 Reserves and resources estimates have been prepared in compliance with NI 43-101. The measured and indicated coal resources are inclusive of those coal resources modified to produce the coal reserves. Details of the assumptions and parameters used to estimate the reserves and resources and information on data verification are set out in the Annual Information Form dated March 30, 2015 and available on SEDAR at www.sedar.com.

(ii) Mine plan and geology for the Ovoot Tolgoi project are currently under review as discussed under the heading "Overview" of this MD&A below.

The Company and the responsible QPs are currently reviewing the geology and mine plan for Ovoot Tolgoi and changes thereto may impact anticipated production levels, and the quantities of measured and/or indicated resources and reserves of Ovoot Tolgoi. The review of the geology and mine plan for the Ovoot Tolgoi Complex has not yet been completed, nor has a new mine plan been presented to or been approved by the Company's board of directors. As a result of the significant changes in some of the mining planning factors compared to those used for the Ovoot Tolgoi Technical Report, this review may result in material changes to the reserves for the Ovoot Tolgoi Deposit.

Until the Company has completed this review and adopted a new mine plan, it is unable to conclude that a change in the coal reserve estimates has occurred compared to previous studies and it is also unable to conclude on the potential materiality of any such change for the Company. Upon the completion of the review and potential adoption of a new mine plan, the Company intends to have all input parameters, procedures and forecasts fully verified and reviewed in accordance with NI 43-101. This may lead, if required, to the preparation of a new technical report containing updated coal reserves estimates for the Ovoot Tolgoi Deposit.

As a result of this review, estimates of the Company's mineral reserves and resources may change significantly, and existing interpretations and deductions on which the current reserves and resources estimates are based may prove to be inaccurate. Any downward adjustments to the Company's mineral resource or reserve estimates resulting from this review could materially affect the Company's development and mining plans, which could materially and adversely affect its business and results of operations.

For more information on the risks associated with classification of geology type of coal deposits, refer to the Risk Factor entitled "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" in the section entitled "Risk Factors" of the December 31, 2014 MD&A available on www.sedar.com.

Significant Events and Highlights

The Company's significant events and highlights for the three months ended June 30, 2015 and subsequent period to August 13, 2015 are as follows:

- ***Operating results*** – The Company continues to operate under difficult market conditions as prices for coal remained weak in China through the second quarter of 2015. The impact of these conditions on the Company's operations continues to be exacerbated given the Company's liquidity constraints. The Company sold 0.19 million tonnes of its coal products during the quarter. After the resumption of mining operations on March 30, 2015, production for the second quarter of 2015 was 0.62 million tonnes, allowing the Company to position itself to meet its commitments under existing and expected new coal offtake contracts.

- ***Tax investigation case in Mongolia*** - On January 30, 2015, the panel of appointed judges from the Second District Criminal Court of Justice found three of the Company's former employees guilty of tax evasion and gave sentences ranging from 5 years and 6 months to 5 years and 10 months of imprisonment in the correctional facilities of strict regimen in Mongolia. Although SouthGobi Sands LLC ("SGS"), the Company's wholly-owned subsidiary, was not a party to the criminal proceedings, the court declared it to be financially liable as a "civil defendant" for a penalty (the "Tax Penalty") of MNT 35.3 billion (approximately $18.0 million at June 30, 2015), the corresponding balance has been provided for in the second quarter of 2015.

  Subsequent to an unsuccessful appeal to the Second District Criminal Court of Justice, on April 22, 2015, SGS filed an appeal with the Supreme Court against the decision of the 10th Appeal Court for Criminal Case of Mongolia upholding the tax verdict against SGS (the "Tax Verdict"). SGS has been informed that the Supreme Court has refused to hear the tax case on appeal and as such the Tax Verdict has entered into force.

The Tax Verdict is however not immediately payable and enforceable against SGS absent further actions prescribed by the laws of Mongolia. In particular, SGS has not received a copy of the bailiff's resolution on execution of the Tax Verdict, as required under the Law of Mongolia on Execution of Court Decisions in order for any judgment execution process to happen.

The Company continues to believe that there is a lack of evidence to support the Tax Verdict and that the Tax Verdict and the subsequent decisions of the higher courts on appeal were substantively and procedurally in error under the laws of Mongolia.

The Company has assessed other available judicial avenues to continue defending itself. However, it believes it can and is currently seeking to resolve amicably with the Mongolian authorities the dispute giving rise to the Tax Verdict in a manner that is both appropriate having regard to the Company's limited financial resources and supportive of a positive environment for foreign investment in Mongolia. There can be no assurance, however, that any such resolution can be successfully negotiated by the Company either at all or on favourable terms, or that the terms of any resolution to which the Government of Mongolia would be prepared to agree would not be materially adverse to the Company. In such case, this may result in an event of default under the CIC Convertible Debenture and CIC would have the right to declare the full principal and accrued interest owing thereunder immediately due and payable. Such an event of default under the CIC Convertible Debenture or the Company's inability to pay the penalty could result in voluntary or involuntary proceedings involving the Company (including bankruptcy) as discussed under the heading Risk Factors in the MD&A issued on March 30, 2015 and available on SEDAR at www.sedar.com.

- ***Novel Sunrise Private Placement*** - On February 24, 2015, the Company announced it had entered into a private placement for proceeds of up to $7.5 million with Novel Sunrise Investments Limited ("Novel Sunrise") as a proposed new significant investor and strategic partner.

  On March 3, 2015, following the successful closing of the first tranche of the Novel Sunrise private placement, including the receipt of $3.5 million, the Company issued 10,131,113 Mandatory Convertible Units to Novel Sunrise and in accordance with the terms of the agreement Mr. Ted Chan was appointed as the Executive Director of the Company. On July 26, 2015, Mr. Ted Chan ceased to be the Executive Director of the Company. Refer to "Changes in Management and Directors" section below for more details.

  On April 23, 2015, the Company successfully closed the second and final tranche of the Novel Sunrise private placement generating approximately $4.0 million in gross proceeds through the issue of approximately 11.6 million Common Shares. In addition, Novel Sunrise converted their previously acquired Mandatory Convertible Units on a one for one basis into Common Shares.

- ***CITIC Merchant and Swiss Life GP private placements*** – On June 22, 2015, the Company announced it had negotiated private placement agreements with sophisticated investors to provide additional capital resources into the Company. The terms of the subscription agreements for the private placements allowed for the issue of approximately 55 million Common Shares.

  On July 14, 2015, the Company announced it had obtained all the necessary regulatory approvals for the private placements and subsequently successfully closed the Swiss Life GP Private Placement, raising $2.9 million for the issuance of 5 million Common Shares.

On July 14, 2015, the Company agreed to an extension of the closing date of the private placement agreement between the Company and CITIC Merchant until July 20, 2015. However, the conditions precedent to the agreement were not fulfilled and CITIC Merchant informed the Company that it would not be subscribing for Common Shares pursuant to the signed private placement agreement.

- ***TSX remedial delisting review -*** As a result of relying on the financial hardship exemption to complete the Novel Sunrise private placement, the Company was placed on remedial delisting review as of February 25, 2015.

  The Company has received confirmation from the Continued Listing Committee of the TSX (the "TSX Committee") that it will further defer its scheduled meeting to consider whether the Company has met the listing requirements of the TSX until August 25, 2015. The TSX Committee has determined to defer its delisting decision until no later than August 28, 2015.

- ***CIC Convertible Debenture*** – On May 20, 2015 under the terms of the CIC Convertible Debenture, CIC confirmed to the Company that, subject to certain conditions and limitations, it would grant a deferral of payment of approximately $7.9 million in cash interest due by the Company to CIC on May 19, 2015 ("May 2015 cash interest installment") until July 22, 2015, subject to a three day cure period which expires on July 27, 2015.

  On July 27, 2015, CIC confirmed to the Company that, subject to certain conditions and limitations, it agreed to grant a further deferral of payment of the May 2015 cash interest installment until November 19, 2015 to allow the Company to execute its Proposed Funding Plan (as defined below in the section entitled "Going Concern").

- ***Novel SPA*** - On February 24, 2015, the Company was advised by Turquoise Hill Resources Ltd. ("Turquoise Hill") that they had entered into a Sale and Purchase Agreement ("Novel SPA") with Novel Sunrise for the purchase of 48,705,155 Common Shares currently held by Turquoise Hill.

  On April 23, 2015, the Company was advised that the Novel SPA, as initially announced by the Company on February 24, 2015, had received all the necessary approvals and closed. Pursuant to the Novel SPA, Novel Sunrise has purchased approximately 48.7 million Common Shares from Turquoise Hill.

- ***NUR SPA*** - On May 4, 2015, the Company announced it had been notified of the expiry of the Sale and Purchase agreement ("NUR SPA"), between Turquoise Hill and National United Resources Holdings Limited ("NUR") which provided for the sale of 56.1 million Common Shares held by Turquoise Hill.

- ***Shareholder loan extension*** - On May 4, 2015, the Company received confirmation from Turquoise Hill of an extension to the limited deferral of amounts owing under the Turquoise Hill shareholder loan facility, subject to certain conditions and limitations.

- ***Notice of arbitration*** - On June 29, 2015, the Company announced First Concept Logistics Limited ("First Concept"), a subsidiary of NUR, served a notice of arbitration (the "Notice") on SGS in respect of a coal supply agreement dated May 19, 2014 as amended on June 27, 2014 (the "Coal Supply Agreement").

  According to the Notice, First Concept alleges that SGS has breached the Coal Supply Agreement and seeks, among other items, the repayment of $11.5 million, representing the prepayment amount advanced by First Concept under such agreement. The Company firmly rejects the allegations of the First Concept in the Notice as lacking any merit and categorically denies First Concept's claim for repayment of the sum of $11.5 million as wholly misconceived and will vigorously defend itself throughout the arbitration proceedings. In addition, SouthGobi reserves the right to pursue legal action against NUR and its subsidiary for compensation for any damages that result from their actions.

- ***Notice of claim*** - On July 2, 2015, the Company announced it had been served with a notice of claim by former President and Chief Executive Officer Alexander Molyneux. The claim relates to alleged breaches of Mr. Molyneux's employment agreement by the Company and is seeking damages of $1 million. The Company considers the claim has no merit and will vigorously defend the action.

- ***Changes in Management and Directors***

  Mr. Ted Chan: Mr. Chan was initially appointed as Executive Director of the Company on March 3, 2015. On July 26, 2015, following the appointment of Mr. Yulan Guo as Interim Chief Executive Officer, Mr. Chan is no longer Executive Director but remained as a Non-Executive Director of the Company until August 6, 2015, the date of the Company's Annual Meeting of Shareholders (the "AGM"), where Mr. Chan did not stand for election.

  Mr. Yulan Guo: Mr. Guo was initially appointed to the Board of Directors as a Non-Executive Director on May 15, 2015. On July 26, 2015 Mr. Guo was appointed as Interim Chief Executive Officer and Executive Director of the Company and was elected as a director of the Company at the AGM.

  Mr. Ningqiao Li: Mr. Li was appointed to the Board of Directors as a Non-Executive Director on May 15, 2015 and was elected as a director of the Company at the AGM.

  Mr. Aminbuhe, Mr. Zhu Liu and Ms. Jin Lan Quan: On August 6, 2015, Mr. Aminbuhe, Mr. Liu and Ms. Quan were elected to the Board of Directors as Non-Executive Directors following the conclusion of the AGM.

  Mr. Kelly Sanders: On August 6, 2015, Mr. Sanders did not stand for the election at the AGM and ceased to be a Non-Executive Director.

  Mr. Bertrand Troiano: Mr. Troiano has stepped down as Chief Financial Officer of the Company following a two-year secondment from Rio Tinto which ended on July 31, 2015.

- ***Going Concern*** - As at the date hereof, the Company, together with its new strategic partner and significant shareholder, Novel Sunrise, has developed a funding plan (the "Proposed Funding Plan") in order to pay the interest due under the CIC Convertible Debenture, meet the Company's obligations as they fall due and achieve its business objectives in 2015 and beyond. However, there is no guarantee that the Company will be able to implement the Proposed Funding Plan or secure other sources of financing. See section 5 "Liquidity and Capital Resources" and section 12 "Risk Factors" for details. As at August 13, 2015, the Company had cash of $2.0 million.

2. OVERVIEW OF OPERATIONAL DATA AND FINANCIAL RESULTS

Summary of Operational Data

	Three months ended June 30,				Six months ended June 30,			
	2015		**2014**		**2015**		**2014**	
Sales Volumes, Prices and Costs								
Premium semi-soft coking coal								
Coal sales *(millions of tonnes)*		**0.02**		-		**0.02**		-
Average realized selling price *(per tonne)* (i)	**$**	**23.37**	$	-	**$**	**23.37**	$	-
Standard semi-soft coking coal								
Coal sales *(millions of tonnes)*		**0.11**		0.12		**0.16**		0.41
Average realized selling price *(per tonne)* (i)	**$**	**19.97**	$	20.33	**$**	**19.31**	$	21.52
Thermal coal								
Coal sales *(millions of tonnes)*		**0.06**		0.51		**0.19**		0.61
Average realized selling price *(per tonne)* (i)	**$**	**10.47**	$	10.72	**$**	**10.46**	$	10.94
Total								
Coal sales *(millions of tonnes)*		**0.19**		0.63		**0.37**		1.02
Average realized selling price *(per tonne)* (i)	**$**	**17.42**	$	12.52	**$**	**15.15**	$	15.22
Raw coal production *(millions of tonnes)*		**0.62**		0.55		**0.62**		1.19
Direct cash costs of product sold *(per tonne)* (ii)	**$**	**15.57**	$	8.23	**$**	**12.27**	$	9.08
Mine administration cash costs of product sold *(per tonne)* (ii)	**$**	**7.90**	$	2.49	**$**	**5.13**	$	3.00
Total cash costs of product sold *(per tonne)* (ii)	**$**	**23.47**	$	10.72	**$**	**17.40**	$	12.08
Other Operational Data								
Production waste material moved *(millions of bank cubic meters)*		**3.62**		2.17		**3.62**		4.72
Strip ratio *(bank cubic meters of waste material per tonne of coal produced)*		**5.87**		3.97		**5.87**		4.00
Lost time injury frequency rate (iii)		**0.00**		0.15		**0.00**		0.15

(i) Average realized selling price is presented before deduction of royalties and selling fees.
(ii) A non-IFRS financial measure, see section 3. Cash costs of product sold exclude idled mine asset cash costs.
(iii) Per 200,000 man hours and calculated based on a rolling 12 month average.

Overview of Operational Data

For the three months ended June 30, 2015

Market conditions and prices for coal remained weak in China through the second quarter of 2015. The Company sold 0.19 million tonnes of its coal products during the quarter. After the resumption of mining operations on March 30, 2015, production increased to 0.62 million tonnes for the quarter, allowing the Company to position itself to meet its commitments under existing and expected new coal offtake contracts.

The cash cost of product sold for the second quarter of 2015 $23.47 has significantly increased compared to the second quarter of 2014 $10.72. The reason for the increase is primarily related to the decrease in sales volumes over which the relatively fixed administration costs are allocated. The Mine administration cash costs per tonne of product sold in the second quarter of 2015 was $7.90 an increase of $5.41 compared to comparative period in 2014 of $2.49.

The Company ended the second quarter of 2015 without a lost time injury. As at June 30, 2015, the Company has a lost injury time frequency rate of nil per 200,000 man hours based on a rolling 12 month average.

For the six months ended June 30, 2015

During the first six months of 2015 market conditions and prices for coal remained weak in China.

The production in the first six months of 2015 was lower than the first six months of 2014 due to the curtailment of the Company's mining operations through to March 30, 2015. During the first quarter of 2015 the Company sold through its existing stockpiles to preserve the Company's liquidity and therefore mining operations were curtailed. On March 30, 2015, the Company resumed mining operations allowing the Company to position itself to meet its commitments under existing and expected new coal offtake contracts.

Total cash costs of product sold were $17.40 per tonne in the first six months of 2015 compared to $12.08 per tonne in the first six months of 2014. The reason for the increase is primarily related to the decrease in sales volumes over which the fixed and variable costs are allocated. At a gross level, the Mine administration cash costs of product sold in the first six months of 2015 is $1.9 million compared to $3.1 million a decrease of $1.2 million.

Summary of Financial Results

	Three months ended June 30,		Six months ended June 30,	
$ in thousands, except per share information	**2015**	**2014**	**2015**	**2014**
Revenue (i),(ii)	**$ 2,951**	$ 6,691	**$ 4,536**	$ 11,828
Cost of sales (ii)	**(11,835)**	(20,086)	**(29,511)**	(38,452)
Gross loss excluding idled mine asset costs	**(5,017)**	(8,497)	**(6,246)**	(18,699)
Gross loss including idled mine asset costs	**(8,884)**	(13,395)	**(24,975)**	(26,624)
Other operating expense	**(19,450)**	(1,776)	**(18,479)**	(2,849)
Administration expenses	**(1,961)**	(2,253)	**(3,388)**	(4,490)
Evaluation and exploration expenses	**22**	(107)	**(56)**	(279)
Loss from operations	**(30,273)**	(17,531)	**(46,898)**	(34,242)
Finance costs	**(5,222)**	(5,215)	**(11,605)**	(10,240)
Finance income	**273**	127	**16**	1,134
Share of losses of joint venture	**151**	(3)	**133**	(29)
Income tax expense	**(1)**	(546)	**(1)**	(546)
Net loss	**(35,072)**	(23,168)	**(58,355)**	(43,923)
Basic loss per share	**$ (0.15)**	$ (0.12)	**$ (0.25)**	$ (0.23)
Diluted loss per share	**$ (0.15)**	$ (0.12)	**$ (0.25)**	$ (0.23)

(i) Revenue is presented after deduction of royalties and selling fees.
(ii) Revenue and cost of sales relate to the Company's Ovoot Tolgoi Mine within the Mongolian Coal Division operating segment. Refer to note 3 of the condensed consolidated interim financial statements for further analysis regarding the Company's reportable operating segments.

Royalty regime in Mongolia

The royalty regime in Mongolia is evolving and has been subject to change since 2012. The Government of Mongolia implemented a trial period from October 1, 2012 to March 31, 2013, during which the royalty imposed on coal sales was determined using the actual contracted sales price per tonne. Subsequently, from April 1, 2013 to March 31, 2014, the royalty on all coal sales exported out of Mongolia was based on a set reference price per tonne published monthly by the Government of Mongolia.

The Government of Mongolia implemented a new royalty regime effective April 1, 2014, referred to as the "flexible tariff" royalty regime. From April 1, 2014, the royalty per tonne for export coal sales has been calculated based on the actual contracted sales price per tonne, whereby the contracted sales price includes the costs of transporting the coal to the Mongolia-China border. If transportation costs are not included in the contracted sales price between a buyer and seller, the following costs are required to be included in the contracted sales price for purposes of calculating the royalty per tonne: transportation costs and costs associated with transportation such as customs documentation fees, insurance, loading and unloading costs. In the event the actual contracted sales price calculated as described above differs by more than 10% from the contracted sales price of coal products with the same classification and quality being exported by other legal entities in Mongolia through the same border crossing, the calculated contracted sales price is deemed non-market under Mongolian tax law and the royalty per tonne is calculated based on a reference price that will be determined by the Government of Mongolia.

The Company currently sells coal from the Ovoot Tolgoi Mine ex mine gate and the coal is exported through the Shivee Khuren Border Crossing. The Company's average realized selling price excludes transportation costs.

On July 4, 2014, the Government of Mongolia made further amendments to the royalty regime. From July 4, 2014 onwards, the royalty is initially calculated and paid monthly based on the Government reference price. On a quarterly basis the royalty amount is adjusted to reflect the contracted sales price and additional documentation needs to be submitted to the Mongolian Tax Authority. Once the quarterly statement has been approved by the Mongolian Tax Authority, any adjustments between the monthly payments for the quarter and the quarterly submission are adjusted in the next months' royalty calculation.

On January 1 2015, this "flexible tariff" royalty regime ended and royalty payments reverted to the previous regime which is based on a set reference price per tonne published monthly by the Government of Mongolia.

On March 16, 2015, the Government of Mongolia issued an amendment resolution to the "flexible tariff" regime changing the coal classification methodology from which to base the royalty calculation. The resolution is effective from May 1, 2015 and the Government of Mongolia has published reference price classifications subdivided into additional classifications since that date. According to the resolution, Company's coal is mainly divided into 2 classifications depending on coal quality under raw coal type.

The Company and other Mongolian coal producers are actively engaging the Mongolian authorities to seek the continuation of the "flexible tariff" regime. See "Risk Factors - Company's Projects in Mongolia" in the MD&A issued on March 30, 2015 and available on SEDAR at www.sedar.com.

Overview of Financial Results

For the three months ended June 30, 2015

The Company recorded a $30.3 million loss from operations in the second quarter of 2015 compared to a $17.5 million loss from operations in the second quarter of 2014. The operations for the three months ended June 30, 2015 were impacted by continuing difficult market conditions and weak coal prices in China. Whilst the Company resumed production on March 30, 2015 in anticipation of increased sales volumes, the results for the second quarter of 2015 were primarily impacted as a consequence of the tax investigation case in Mongolia as a provision of $18.0 million was recorded in respect of the Tax Penalty during the three months ended June 30, 2015.

Revenue was $3.0 million in the second quarter of 2015 compared to $6.7 million in the second quarter of 2014. The Company sold 0.19 million tonnes of coal at an average realized selling price of $17.42 per tonne in the second quarter of 2015 compared to sales of 0.63 million tonnes at an average realized selling price of $12.52 per tonne in the second quarter of 2014. Despite the continued difficult market conditions there was an increase in the average realized selling price which is attributed to a change in sales mix. The product mix for the second quarter of 2015 consisted of approximately 69% of Premium and Standard semi-soft coking coal and 31% of Thermal coal compared to approximately 19% of Premium and Standard semi-soft coking coal and 81% of Thermal coal in the second quarter of 2014.

The Company's revenue is presented after deduction of royalties and selling fees. The Company's effective royalty rate for the second quarter of 2015, based on the Company's average realized selling price of $17.42 per tonne, was 10.7% or $1.86 per tonne compared to 8.1% or $1.00 per tonne based on the average realized selling price of $12.52 per tonne in the second quarter of 2014.

Cost of sales was $11.8 million in the second quarter of 2015 compared to $20.1 million in the second quarter of 2014. Cost of sales comprises operating expenses, share-based compensation expense, equipment depreciation, depletion of mineral properties, coal stockpile inventory impairments and idled mine asset costs. Operating expenses in cost of sales reflect the total cash costs of product sold (a non-IFRS financial measure, see section 3 for further analysis) during the period.

	Three months ended June 30,	
$ in thousands	**2015**	**2014**
Operating expenses	**$ 4,571**	$ 6,754
Share-based compensation expense	**4**	127
Depreciation and depletion	**832**	2,061
Impairment of coal stockpile inventories	**2,561**	6,246
Cost of sales from mine operations	**7,968**	15,188
Cost of sales related to idled mine assets	**3,867**	4,898
Cost of sales	**$ 11,835**	$ 20,086

Operating expenses in cost of sales were $4.6 million in the second quarter of 2015 compared to $6.8 million in the second quarter of 2014. The overall decrease in operating expenses is primarily the result of the impact of increasing the coal stockpile levels during the second quarter of 2015 to allow the Company to meet its existing and anticipated coal sales commitments compared to a reduction in the coal stockpile in the second quarter of 2014.

Cost of sales in the second quarter of 2015 and 2014 included coal stockpile impairments of $2.6 million and $6.2 million, respectively, to reduce the carrying value of the Company's coal stockpiles to their net realizable value. The coal stockpile impairments recorded in both the second quarter of 2015 and 2014 reflect the challenging coal market conditions and primarily related to the Company's higher-ash products.

Cost of sales related to idled mine asset costs primarily consisted of period costs, which were expensed as incurred and included mainly depreciation expense. Cost of sales related to idled mine assets in the second quarter of 2015 included $3.9 million related to depreciation expenses for idled equipment compared to $4.9 million in the second quarter of 2014.

Other operating expense was $19.5 million in the second quarter of 2015 compared to $1.8 million in the second quarter of 2014 as follows:

	Three months ended June 30,	
$ in thousands	**2015**	**2014**
Foreign exchange loss/ (gain)	**$ 1,196**	$ (146)
Impairment loss on prepaid expenses and deposits	**-**	3,405
Impairment loss on property, plant and equipment	**-**	277
Proceeds on disposal of mining license	**-**	(1,818)
Provision for doubtful trade and other receivable	**157**	-
Provision for court case penalty	**18,049**	-
Other	**48**	58
Other operating expense	**$ 19,450**	$ 1,776

The Company recognized an expense for the provision of the Tax Penalty in respect of the tax investigation case in Mongolia. The Tax Penalty amounts to MNT35.3 billion (approximately $18.0 million on June 30, 2015). For further detail refer to section 6. "Regulatory Issues and Contingencies" under the heading "Governmental and Regulatory Investigations".

The Company recognized an impairment loss of $3.4 million in the second quarter of 2014 related to prepaid toll washing fees under the contract with Ejinaqi Jinda Coal Industry Co. Ltd. ("Ejin Jinda"). The impairment charge was the result of the continued delay in starting the commercial operations at the wet washing facility and the continued soft coal market in China. No corresponding impairment charge was required in the second quarter of 2015.

In the second quarter of 2014, the Company completed the sale of the Tsagaan Tolgoi mining license. The gross proceeds of the sale were $2.0 million, indirect taxes and costs totaled $0.2 million and a withholding tax totaling $0.5 million was incurred. The net proceeds generated for the Company after taxes and costs were $1.3 million.

Administration expenses were $2.0 million in the second quarter of 2015 compared to $2.3 million in the second quarter of 2014 as follows:

	Three months ended June 30,	
$ in thousands	**2015**	**2014**
Corporate administration	**$ 512**	$ 523
Legal and professional fees	**890**	779
Salaries and benefits	**472**	825
Share-based compensation expense	**47**	94
Depreciation	**40**	32
Administration expenses	**$ 1,961**	$ 2,253

Administration expenses were lower for the second quarter of 2015 compared to the second quarter of 2014 primarily as a result of cost reduction measures.

Evaluation and exploration expenses were negligible in the second quarter of 2015 compared to $0.1 million in the second quarter of 2014. The Company continued to minimize evaluation and exploration expenditures in the second quarter of 2015 in order to preserve the Company's financial resources. Evaluation and exploration activities and expenditures in the second quarter of 2015 were limited to ensuring that the Company met the Mongolian Minerals Law requirements in respect of its mining and exploration licenses.

Finance costs were $5.2 million and $5.2 million respectively in the second quarter of 2015 and the second quarter of 2014. Finance costs primarily consisted of interest expense in respect of the $250.0 million CIC Convertible Debenture ($5.1 million for the second quarter of 2015 and $5.0 million for the second quarter of 2014).

Finance income was $0.3 million in the second quarter of 2015 compared to $0.1 million in the second quarter of 2014 which, primarily consists of an unrealized gain in respect of the embedded derivative in the CIC Convertible Debenture.

For the six months ended June 30, 2015

The Company recorded a $46.9 million loss from operations in the first six months of 2015 compared to a $34.2 million loss from operations in the first six months of 2014. The operations for the six months ended June 30, 2015 were impacted by continuing difficult market conditions and weak coal prices in China. Whilst the Company resumed production on March 30, 2015 in anticipation of increased sales volumes, the results for the first six months of 2015 were primarily impacted as a consequence of the Tax investigation case in Mongolia as a provision of $18.0 million was recorded in respect of the Tax Penalty during the three months ended June 30, 2015.

Revenue was $4.5 million in the first six months of 2015 compared to $11.8 million in the first six months of 2014. The Company sold 0.37 million tonnes of coal at an average realized selling price of $15.15 per tonne in the first six months of 2015 compared to sales of 1.02 million tonnes at an average realized selling price of $15.22 per tonne in the first six months of 2014. The benefit of the improved product mix has been more than offset by continued declining prices for the first six months of 2015 when compared to the first six months of 2014.

The Company's revenue is presented net of royalties and selling fees. With the changes affecting the royalty regime in Mongolia, the Company's effective royalty rate for the first six months of 2015, based on the Company's average realized selling price of $15.15 per tonne, was 18.0% or $2.73 per tonne compared to 16.2% or $2.46 per tonne based on the average realized selling price of $15.22 per tonne in the first six months of 2014.

Cost of sales was $29.5 million in the first six months of 2015 compared to $38.5 million in the first six months of 2014. Cost of sales comprises operating expenses, share-based compensation expense, equipment depreciation, depletion of mineral properties, coal stockpile inventory impairments and idled mine asset costs. Operating expenses in cost of sales reflect the total cash costs of product sold (a non-IFRS financial measure, see section 3 for further analysis) during the period.

$ in thousands	Six months ended June 30, 2015		Six months ended June 30, 2014	
Operating expenses	**$**	**6,498**	$	12,317
Share-based compensation expense		**32**		143
Depreciation and depletion		**1,141**		4,540
Impairment of coal stockpile inventories		**3,111**		13,527
Cost of sales from mine operations		**10,782**		30,527
Cost of sales related to idled mine assets		**18,729**		7,925
Cost of sales	**$**	**29,511**	$	38,452

Operating expenses in cost of sales were $6.5 million in the first six months of 2015 compared to $12.3 million in the first six months of 2014. The overall decrease in operating expenses is the result of both (i) different production profiles, in the first six months of 2015 there was a period of curtailment until March 30, 2015 whilst in the first six months of 2014 production was impacted by a decision by the Company in June 2014 in response to market conditions to reduce production and place approximately half of its workforce on furlough; and (ii) a greater increase in coal stockpiles during the first six months of 2015 when compared to the first six months of 2014.

Cost of sales in the first six months of 2015 and the first six months of 2014 included coal stockpile impairments of $3.1 million and $13.5 million, respectively, to reduce the carrying value of the Company's coal stockpiles to their net realizable value. The coal stockpile impairments recorded in both 2015 and 2014 reflect the challenging coal market conditions and primarily related to the Company's higher-ash products.

Cost of sales related to idled mine asset costs primarily consisted of period costs, which were expensed as incurred and primarily included depreciation expense. Cost of sales related to idled mine assets in the first six months of 2015 included $15.8 million related to depreciation expenses for idled equipment (2014: $7.9 million). Idled mine asset costs increased in the first six months of 2015 compared to the first six months of 2014 as a result of the period of curtailment until March 30, 2014 when mining operations recommenced. However, neither the production plan for the first six months of 2014 nor for the period from March 30, 2015 until June 30, 2015 fully utilized the Company's existing mining fleet, therefore, idled mine asset costs continued to be incurred.

Other operating expenses were $18.5 million in the first six months of 2015 compared to $2.8 million in the first six months of 2014.

$ in thousands	Six months ended June 30, 2015		Six months ended June 30, 2014	
Foreign exchange loss/(gain)	**$**	**138**	$	(910)
Impairment loss on available-for-sale financial asset		**-**		1,766
Impairment loss on prepaid expenses and deposits		**-**		3,405
Impairment loss on property, plant and equipment		**-**		277
Proceeds on disposal of mining license		**-**		(1,818)
Provision for doubtful trade and other receivable		**157**		-
Provision for court case penalty		**18,049**		-
Other		**135**		129
Other operating expense	**$**	**18,479**	$	2,849

The Company recognized an expense for the provision of the Tax Penalty in respect of the tax investigation case in Mongolia. The Tax Penalty amounts to MNT35.3 billion (approximately $18.0 million at June 30, 2015). For further detail refer to section 6. "Regulatory Issues and Contingencies" under the heading "Governmental and Regulatory Investigations".

The Company recognized an impairment loss of $3.4 million in the first six months of 2014 related to prepaid toll washing fees under the contract with Ejinaqi Jinda Coal Industry Co. Ltd. ("Ejin Jinda"). The impairment charge was the result of the continued delay in starting the commercial operations at the wet washing facility and the continued soft coal market in China. No corresponding impairment charge was required in the second quarter of 2015.

In the first six months of 2014, the Company completed the sale of the Tsagaan Tolgoi mining license. The gross proceeds of the sale were $2.0 million, indirect taxes and costs totaled $0.2 million and a withholding tax totaling $0.5 million was incurred. The net proceeds generated for the Company after taxes and costs were $1.3 million.

The Company's previous investment in Aspire Mining Limited ("Aspire") was accounted for as an available-for-sale financial asset and carried at its fair value. In the first six months of 2014, Aspire's market capitalization fluctuated, in the first quarter of 2014 the market capitalization decreased and an impairment charge of $1.8 million was initially recorded. In the second quarter of 2014 the gain of $0.4 million was recorded in other comprehensive income. The Company disposed all its investment in Aspire during 2014 and did not hold any Aspire shares as at December 31, 2014 or June 30, 2015.

Administration expenses were $3.4 million in the first six months of 2015 compared to $4.5 million in the first six months of 2014.

	Six months ended June 30,	
$ in thousands	**2015**	**2014**
Corporate administration	**$ 958**	$ 1,183
Legal and professional fees	**1,365**	1,465
Salaries and benefits	**852**	1,553
Share-based compensation expense	**147**	225
Depreciation	**66**	64
Administration expenses	**$ 3,388**	$ 4,490

Administration expenses were lower in the first six months of 2015 compared to the first six months of 2014 reflecting the continued cost-cutting initiatives.
Evaluation and exploration expenses were $0.1 million in the first six months of 2015 compared to $0.3 million in the first six months of 2014. The Company continued to minimize evaluation and exploration expenditures in the first six months of 2015 in order to preserve the Company's financial resources. Evaluation and exploration activities and expenditures in the first six months of 2015 were limited to ensuring that the Company met the Mongolian Minerals Law requirements in respect of its mining and exploration licenses.

Finance costs were $11.6 million and $10.2 million in the first six months of 2015 and 2014 respectively. This primarily consisted of interest expense on the CIC Convertible Debenture ($10.1 million for the first six months of 2015 and $10.0 million for the first six months of 2014).

Finance costs for the first six months of 2015, also includes $1.3 million in respect of the unrealized fair value loss of the embedded derivative in the CIC Convertible Debenture. In comparison, in the first six months of 2014, the Company recorded within Finance income an unrealized fair value gain of the embedded derivative in the CIC Convertible Debenture ($1.1 million). The fair value of the embedded derivatives in the CIC Convertible Debenture is driven by many factors including: the Common Share price, U.S. Dollar and Canadian Dollar exchange rates and share price volatility.

Finance income was negligible in the first six months of 2015 compared to $1.1 million in the first six months of 2014. Finance income primarily consists of unrealized gains on the fair value change of the embedded derivatives in the CIC Convertible Debenture (nil and $1.1 million respectively for the first six months of 2015 and the first six months of 2014).

Income tax expense was negligible in the first six months of 2015 compared to an expense of $0.5 million in the first six months of 2014. The $0.5 million recognized in the first six months of 2014 relates to taxes paid in respect of the sale of the Tsagaan Tolgoi mining license.

Summary of Quarterly Operational Data

	2015		2014				2013	
Quarter Ended	**30-Jun**	31-Mar	31-Dec	30-Sep	30-Jun	31-Mar	31-Dec	30-Sep
Sales Volumes, Prices and Costs								
Premium semi-soft coking coal								
Coal sales *(millions of tonnes)*	**0.02**	-	0.02	-	-	-	0.21	0.04
Average realized selling price *(per tonne)* [(i)]	**$ 23.37**	$ -	$ 26.77	$ -	$ -	$ -	$ 37.54	$ 37.50
Standard semi-soft coking coal								
Coal sales *(millions of tonnes)*	**0.11**	0.05	0.14	0.31	0.12	0.29	1.40	0.87
Average realized selling price *(per tonne)* [(i)]	**$ 19.97**	$ 17.95	$ 18.32	$ 17.41	$ 20.33	$ 22.00	$ 24.49	$ 21.67
Thermal coal								
Coal sales *(millions of tonnes)*	**0.06**	0.13	0.21	0.34	0.51	0.10	0.11	0.03
Average realized selling price *(per tonne)* [(i)]	**$ 10.47**	$ 10.46	$ 11.69	$ 10.66	$ 10.72	$ 12.07	$ 12.60	$ 13.07
Total								
Coal sales *(millions of tonnes)*	**0.19**	0.18	0.37	0.65	0.63	0.39	1.72	0.94
Average realized selling price *(per tonne)* [(i)]	**$ 17.42**	$ 12.66	$ 15.04	$ 13.87	$ 12.52	$ 19.54	$ 25.30	$ 22.05
Raw coal production *(millions of tonnes)*	**0.62**	-	0.21	0.17	0.55	0.64	1.73	1.13
Direct cash costs of product sold *(per tonne)* [(ii)]	**$ 15.57**	$ 8.68	$ 8.09	$ 7.38	$ 8.23	$ 10.43	$ 11.13	$ 9.41
Mine administration cash costs of product sold *(per tonne)* [(ii)]	**$ 7.90**	$ 2.11	$ 2.44	$ 2.30	$ 2.49	$ 3.80	$ 1.39	$ 2.20
Total cash costs of product sold (*per tonne)* [(ii)]	**$ 23.47**	$ 10.79	$ 10.53	$ 9.68	$ 10.72	$ 14.23	$ 12.52	$ 11.61
Other Operational Data								
Production waste material moved *(millions of bank cubic meters)*	**3.62**	-	0.55	0.20	2.17	2.55	3.77	1.57
Strip ratio *(bank cubic meters of waste material per tonne of coal produced)*	**5.87**	-	2.61	1.20	3.97	4.02	2.18	1.39
Lost time injury frequency rate [(iii)]	**0.00**	0.25	0.21	0.17	0.15	0.00	0.00	0.00

(i) *Average realized selling price is presented before deduction of royalties and selling fees.*
(ii) *A non-IFRS financial measure, see section 3. Cash costs of product sold exclude idled mine asset cash costs.*
(iii) *Per 200,000 man hours and calculated based on a rolling 12 month average.*

Summary of Quarterly Financial Results

$ in thousands, except per share information	2015		2014				2013	
Quarter Ended	**30-Jun**	31-Mar	31-Dec	30-Sep	30-Jun	31-Mar	31-Dec	30-Sep
Financial Results								
Revenue [(i), (ii)]	**$ 2,951**	$ 1,587	$ 5,054	$ 7,611	$ 6,691	$ 5,137	$ 32,457	$ 15,652
Cost of sales [(ii)]	**(11,835)**	(17,678)	(19,757)	(23,922)	(20,086)	(18,366)	(40,359)	(33,486)
Gross loss excluding idled mine asset costs	**(5,017)**	(1,230)	(821)	(2,178)	(8,497)	(10,202)	(4,141)	(13,323)
Gross loss including idled mine asset costs	**(8,884)**	(16,091)	(14,703)	(16,311)	(13,395)	(13,229)	(7,900)	(17,834)
Other operating income/(expenses)	**(19,450)**	971	(11,989)	(2)	(1,776)	(1,073)	(109,682)	(1,003)
Administration expenses	**(1,961)**	(1,425)	(1,924)	(2,530)	(2,253)	(2,237)	(3,668)	(4,204)
Evaluation and exploration expenses	**22**	(81)	(911)	(122)	(107)	(172)	(489)	(186)
Loss from operations	**(30,273)**	(16,626)	(29,527)	(18,965)	(17,531)	(16,711)	(121,740)	(23,227)
Finance costs	**(5,222)**	(6,648)	(6,351)	(5,257)	(5,215)	(5,025)	(5,167)	(5,382)
Finance income	**273**	8	317	135	127	1,007	1,301	124
Share of earnings/(losses) of joint venture	**151**	(18)	(40)	(32)	(3)	(26)	(15)	(66)
Income tax expense	**(1)**	-	(40)	-	(546)	-	(13,109)	(13,377)
Net loss	**(35,072)**	(23,284)	(35,641)	(24,119)	(23,168)	(20,755)	(138,730)	(41,928)
Basic loss per share	**$ (0.15)**	$ (0.11)	$ (0.19)	$ (0.13)	$ (0.12)	$ (0.11)	$ (0.75)	$ (0.23)
Diluted loss per share	**$ (0.15)**	$ (0.11)	$ (0.19)	$ (0.13)	$ (0.12)	$ (0.11)	$ (0.75)	$ (0.23)

(i) Revenue is presented after deduction of royalties and selling fees.
(ii) Revenue and cost of sales relate to the Company's Ovoot Tolgoi Mine within the Mongolian Coal Division operating segment. Refer to note 3 of the condensed consolidated interim financial statements for further analysis regarding the Company's reportable operating segments.

3. NON-IFRS FINANCIAL MEASURES

The Company has included the non-IFRS financial measure "cash costs" in this MD&A to supplement its condensed consolidated interim financial statements, which have been prepared in accordance with IFRS.

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

Cash Costs

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

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

The cash costs per tonne of product sold presented below may differ from cash costs per tonne of product produced depending on the timing of coal stockpile inventory turnover and impairments of coal stockpile inventories from prior periods.

	Three months ended June 30,		Six months ended June 30,	
$ in thousands, except per tonne information	**2015**	**2014**	**2015**	**2014**
Cash costs				
Cost of sales determined in accordance with IFRS	**$ 11,835**	$ 20,086	**$ 29,511**	$ 38,452
Less non-cash expenses	**(3,397)**	(8,434)	**(4,284)**	(18,210)
Less non-cash idled mine asset costs	**(3,867)**	(4,860)	**(15,755)**	(7,850)
Total cash costs	**4,571**	6,792	**9,472**	12,392
Less idled mine asset cash costs	**-**	(37)	**(2,972)**	(75)
Total cash costs excluding idled mine asset cash costs	**4,571**	6,755	**6,500**	12,317
Coal sales *(millions of tonnes)*	**0.19**	0.63	**0.37**	1.02
Total cash costs of product sold *(per tonne)*	**$ 23.47**	$ 10.72	**$ 17.40**	$ 12.08

	Three months ended June 30,		Six months ended June 30,	
$ in thousands, except per tonne information	**2015**	**2014**	**2015**	**2014**
Cash costs				
Direct cash costs of product sold *(per tonne)*	**$ 15.57**	$ 8.23	**$ 12.27**	$ 9.08
Mine administration cash costs of product sold *(per tonne)*	**7.90**	2.49	**5.13**	3.00
Total cash costs of product sold *(per tonne)*	**$ 23.47**	$ 10.72	**$ 17.40**	$ 12.08

4. PROPERTIES

The Company currently holds two mining licenses and four exploration licenses in Mongolia, which in total cover an area of approximately 98,000 hectares ("ha"). The decrease in hectares followed the completion of a partial sale of exploration license 9449X. The mining licenses pertain to the Ovoot Tolgoi Complex (12726A) and the Soumber Deposit (MV-016869).

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

Operating Mines

Ovoot Tolgoi Mine

The Ovoot Tolgoi Mine is located in the southwest corner of the Umnugobi Aimag (South Gobi Province) of Mongolia. The deposit is within the administrative unit of Gurvantes Soum, 320km southwest of the provincial capital of Dalanzadgad and 950km southwest of the nation's capital of Ulaanbaatar. Mining operations at the Ovoot Tolgoi Mine have been carried out in two distinct areas, the Sunset pit to the west and the Sunrise pit to the east.

Saleable products from the Ovoot Tolgoi Mine primarily include the Standard and Premium semi-soft coking coal products. The Company's raw semi-soft products together with raw higher-ash coals are suitable for washing and blending in order to be sold as a 1/3 coking coal in the Chinese market. Some higher-ash product is sold as a thermal coal product as and when the market allows. The Company intends to continue to develop markets for both its Premium and Standard semi-soft coking coal brands and to pursue long-term supply offtake with end users in China to complement its existing customer base and to gain best value of the Company's coal in the Chinese market. The Company is committed to further enhancing the quality of its coal products through wet washing and increasing its market penetration in China, and as part of this strategy is cooperating with Ejin Jinda to study the utilization of the Ejin Jinda wet washing facility (refer to "Processing Infrastructure – Wet Washing Facility" section below).

Reserves and Resources

On March 19, 2012, the Company announced an updated NI 43-101 compliant independent resource estimate prepared by RPM. RPM estimated that the Ovoot Tolgoi Mine contained 175.7 million tonnes of proven and probable surface coal reserves, 133.3 million tonnes of measured coal resources, 59.9 million tonnes of indicated coal resources and 24.0 million tonnes of inferred coal resources as at October 31, 2011. All of these resources are located above 300m and are amenable to surface mining. The Measured and Indicated Mineral Resources are inclusive of those Mineral Resources modified to produce the Mineral Reserves. Details of the assumptions and parameters used to estimate the reserves, resources and coal quality estimates and information on data verification are set out in the Company's Annual Information Form dated March 30, 2015, and available on SEDAR at www.sedar.com (the "Annual Information Form").

The Company and the responsible QPs are currently reviewing the geology and mine plan for Ovoot Tolgoi and changes thereto may impact anticipated production levels, the quantities of measured and/or indicated resources and reserves of Ovoot Tolgoi. The review of the geology and mine plan for the Ovoot Tolgoi Complex has not yet been completed, nor has a new mine plan been presented to or been approved by the Company's board of directors. As a result of the significant changes in some of the mining planning factors compared to those used for the Ovoot Tolgoi Technical Report, this review may result in material changes to the reserves for the Ovoot Tolgoi Deposit.

Until the Company has completed this review and adopted a new mine plan, it is unable to conclude that a change in the coal reserve estimates has occurred compared to previous studies and it is also unable to conclude on the materiality of any such change for the Company. Upon the completion and adoption of a new mine plan, the Company intends to have all input parameters, procedures and forecasts fully verified and reviewed in accordance with NI 43-101. This may lead, if required, to the preparation of a new technical report containing updated coal reserves estimates for the Ovoot Tolgoi Deposit.

As a result of this review, estimates of the Company's mineral reserves and resources may change significantly, and existing interpretations and deductions on which the current reserves and resources estimates are based may prove to be inaccurate. Any downward adjustments to the Company's mineral resource or reserve estimates resulting from this review could materially affect the Company's development and mining plans, which could materially and adversely affect its business and results of operations.

For more information on the risks associated with classification of geology type of coal deposits, refer to the Risk Factor entitled "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" in the section entitled "Risk Factors" of the December 31, 2014 MD&A available on www.sedar.com.

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

Operational Data and Financial Results

Refer to section 2 for an overview of the operational data and financial results of the Ovoot Tolgoi Mine.

Processing Infrastructure

Dry Coal Processing

The use of mobile screens at stockpile areas closer to the pits has enabled the Company to realize a cost benefit compared to hauling the coal to the central DCHF and operating the rotary breaker. This provides a lower cost solution without adversely impacting the coal quality of the coal planned to be mined over the next year.

Assuming the Proposed Funding Plan is successfully implemented, coal markets improve and the mine plan review does not materially impact the existing mine plan, the Company expects to increase production from the Ovoot Tolgoi Mine in line with its anticipated annual capacity of 9 million tonnes run-of-mine production. At such time the Company will review the use of the DCHF as part of its existing assets and continue developing beneficiation capabilities to maximize value from its product.

Wet Washing Facility

In 2011, the Company entered into an agreement with Ejin Jinda, a subsidiary of China Mongolia Coal Co. Ltd. to toll-wash coals from the Ovoot Tolgoi Mine. The agreement has a duration of five years from commencement of the contract and provides for an annual wet washing capacity of approximately 3.5 million tonnes of input coal.

In 2011, the Company made an initial payment of $33.6 million in respect of prepaid toll washing fees. The Company recorded a $30.2 million impairment loss on the $33.6 million of prepaid toll washing fees during the year ended December 31, 2013 and in the quarter ended June 30, 2014, the Company recorded an additional impairment of $3.4 million to fully impair the deposit. As at June 30, 2015 the Company has reassessed the carrying value of this prepayment and continues to believe it is appropriate for the balance to be fully impaired. This impairment continues to be recognized due to the continued delay in starting the commercial operations at the wet washing facility and the continued soft coal market in China.

Under the original agreement which required the commercial operation of the wet washing facility to commence on October 1, 2011 the additional fees payable by the Company under wet washing contract would be $18.5 million. The Company assesses on a continuous basis the agreement with Ejin Jinda and has determined it is not probable the $18.5 million will be required to be paid as part of the initial contract.

The Company's objective continues to be the implementation of an effective and profitable wet washing solution, and the Company is cooperating with Ejin Jinda in reviewing the utilization of the wet washing facility.

Transportation Infrastructure

On August 2, 2011, the State Property Committee of Mongolia awarded the tender to construct a paved highway from the Ovoot Tolgoi Complex to the Shivee Khuren Border Crossing (the "Paved Highway") to consortium partners NTB LLC and SGS (together referred to as "RDCC LLC"). The Company has an indirect 40% shareholding in RDCC LLC through its Mongolian subsidiary SGS.

On October 26, 2011, RDCC LLC signed a concession agreement with the State Property Committee of Mongolia. RDCC LLC has the right to conclude a 17 year build, operate and transfer agreement under the Mongolian Law on Concessions.

On May 8, 2015, the commercial operation of the Paved Highway commenced and subsequently the unpaved highway which was previously used to transport coal through the Shivee Khuren Border Crossing has been closed. The Paved Highway is expected to significantly increase the safety of coal transportation, reduce environmental impacts and improve efficiency and capacity of coal transportation. For the three and six months ended June 30, 2015, RDCC LLC recognized toll fee revenue of $0.5 million (2014: nil).

The paved highway is expected to have a carrying capacity in excess of 20 million tonnes of coal per year.

Mining Equipment

The key elements of the currently commissioned mining fleet includes: two Liebherr 996 ($33m^3$ & $36m^3$) hydraulic excavators, three Liebherr R9250 ($15m^3$) hydraulic excavators, 23 MT4400AC (218 tonne capacity) haul trucks and three Terex TR100 (91 tonne capacity) haul trucks, together with various pieces of ancillary equipment.

Workforce

As at June 30, 2015, SGS employed 339 employees in Mongolia. Of the 339 employees, 38 are employed in the Ulaanbaatar office, 3 in outlying offices and 298 at the Ovoot Tolgoi Mine site. Of the 339 employees based in Mongolia, 335 (99%) are Mongolian nationals and of those, 150 (44%) are residents of the local Gurvantes, Dalanzadgad, Sevrei and Noyon Soums.

Development Projects and Exploration Program

Soumber Deposit

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

Mine will allow any future mining operation at the Soumber Deposit to share existing infrastructure with the Ovoot Tolgoi Mine.

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

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

On March 25, 2013, the Company reported an updated NI 43-101 compliant independent resource estimate prepared by RPM. RPM estimated that the Soumber Deposit contains measured coal resources of 62.4 million tonnes, indicated coal resources of 110.3 million tonnes and inferred coal resources of 123.0 million tonnes as at January 10, 2013. Approximately 76% of the Soumber Deposit resource is located above 300m and is amenable to surface mining. Details of the assumptions and parameters used to calculate the resources and coal quality estimates and information on data verification are set out in the Annual Information Form available on SEDAR at www.sedar.com.

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

On July 6, 2011, the Company announced that the Mineral Resources Authority of Mongolia ("MRAM") issued the Company a mining license pertaining to the Soumber Deposit. The 10,993ha mining license was granted for an initial term of 30 years with an option for two 20 year extensions. In addition to the existing mining license, the Company also holds two exploration licenses pertaining to certain areas associated with the Soumber Deposit for which PMAs have been issued. The Company plans to progress to the mining license application process for the PMA issued on August 14, 2013.

A territory fully covering the Soumber Deposit mining license area was designated by the provincial authorities as a special protected area (refer to section 6 "Regulatory Issues and Contingencies" for details of the status of the Soumber Deposit in respect of the latest decision by the provincial authorities).

Environmental baseline studies have been completed and general environmental impact assessments have been approved. The Company has delayed plans for a pre-feasibility study for the Soumber Deposit and intends to manage the feasibility planning and physical preparation of the Soumber Deposit with respect to ongoing market conditions, government requirements and the Company's available financial resources. The Company has engaged the relevant authorities in Mongolia concerning these planned delays.

Zag Suuj Deposit

The Zag Suuj Deposit, located approximately 150km east of the Ovoot Tolgoi Mine and approximately 45km north of the Mongolia-China border, lies within the administrative units of Noyon and Bayandalai Soums in the Umnugobi Aimag (South Gobi Province).

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

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

On March 25, 2013, the Company reported an updated NI 43-101 compliant independent resource estimate for the Zag Suuj Deposit prepared by RPM. RPM estimated that the Zag Suuj Deposit contains indicated coal resources of 21.5 million tonnes and inferred coal resources of 84.0 million tonnes as at January 10, 2013. The entire Zag Suuj Deposit resource is located above 300metres ("m") and is amenable to surface mining. Details of the assumptions and parameters used to calculate the resources and coal quality estimates and information on data verification are set out in the Annual Information Form available on SEDAR at www.sedar.com.

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

The Company holds two exploration licenses pertaining to the Zag Suuj Deposit for which PMAs were issued on August 14, 2013 by MRAM. The Company plans to progress to the mining license application process for the PMAs.

It is anticipated that coals from the Zag Suuj Deposit can be washed to produce a coking coal product or a coking coal blend product. Limited exploration activities are planned for the Zag Suuj Deposit in 2015. Exploration activities in 2015 will ensure to meet the requisite requirements under the Mongolian Minerals Law.

Ovoot Tolgoi Underground Deposit

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

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

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

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

Exploration Program

The Company continued to minimize evaluation and exploration expenditures during the first six months of 2015 in order to preserve the Company's financial resources. The 2015 exploration program will be limited to ensuring that the Company meets the Mongolian Minerals Law requirements in respect of its mining and exploration licenses including those related to the Soumber Deposit.

5. LIQUIDITY AND CAPITAL RESOURCES

Liquidity and Capital Management

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

Novel Sunrise private placement

On February 24, 2015, the Company announced it had entered into a private placement agreement with Novel Sunrise providing for the subscription of up to 21.75 million Common Shares for gross proceeds of up to approximately $7.5 million.

The initial tranche of the private placement consisting of approximately $3.5 million of Mandatory Convertible Units closed on March 3, 2015 having been subject to regulatory approvals and other customary closing conditions. On completion of the Novel SPA each Mandatory Convertible Unit was converted on a one for one basis into Common Shares.

On April 23, 2015, the Company successfully closed the second tranche of the Novel Sunrise private placement for gross proceeds of approximately $4.0 million through the issue of approximately 11.6 million Common Shares.

The issue price for both tranches of the private placement was set at CAD$0.432 ("Placing Price") and represented a discount of approximately 20% to the then 5-day volume-weighted average price per Common Share of approximately CAD$0.54, as of the date the Company received price protection from the TSX for the private placement. The Placing Price was determined with reference to the prevailing market price of the Common Shares and was negotiated on an arm's length basis between the Company's independent directors and Novel Sunrise.

The closing of the Novel Sunrise private placement and related transactions was subject to acceptance of notice of the placement by the TSX pursuant to the financial hardship exemption of the TSX Company Manual and the delisting review (For more information on the delisting review, refer to the heading "TSX Financial Hardship Exemption Application and Status of Listing on TSX" in this MD&A).

In accordance with the terms of the Novel Sunrise private placement:

- Following the closure of the initial tranche of the private placement, Mr. Chan was appointed as an Executive Director on March 3, 2015. Mr. Chan did not stand for election at the Company's AGM on August 6, 2015 and ceased to be an Executive Director of the Company as of that date.

- Following the closure of the second and final tranche, Novel Sunrise holds the right to nominate three directors, to the Company's board of directors. In accordance with this provision, Novel Sunrise nominated Mr. Aminbuhe, Mr. Yulan Guo and Mr. Ningqiao Li to the Company's board of directors and such individuals were subsequently elected at the Company's AGM on August 6, 2015.

Novel SPA

On April 23, 2015, the Company was advised that the Novel SPA, as initially announced by the Company on February 24, 2015, had received all the necessary approvals and closed. Pursuant to the Novel SPA, Novel Sunrise has purchased 48.7 million Common Shares from Turquoise Hill.

Novel Sunrise change in ownership

The Company notes the announcement by Novel Sunrise, the largest shareholder of the Company, on July 20, 2015 which reported that China Cinda (HK) Investments Management Company Limited ("Cinda"), a wholly-owned subsidiary of China Cinda Asset Management Corporation Limited, acquired ownership and control of all of the outstanding voting (ordinary) shares of Novel Sunrise through Hope Rosy Limited, a wholly-owned subsidiary of Cinda.

CITIC Merchant and Swiss Life GP private placements

On June 22, 2015, the Company announced it had negotiated private placement agreements with sophisticated investors to provide additional capital resources into the Company. The terms of the subscription agreements for the private placements allowed for the issue of approximately 55 million Common Shares, priced at C$0.71 per share (a 20% discount to the five date volume weighted average price of the common shares on the TSX at June 19, 2015).

The closing of the private placements and related transactions were subject to necessary approvals, including by the TSX and the Stock Exchange of Hong Kong Limited, and in the case of CITIC Merchant was subject to the approval of their board.

On July 14, 2015, the Company announced it had obtained all the necessary regulatory approvals for the private placements and subsequently successfully closed a portion of the overall placement by placing 5 million Common Shares for approximately $2.9 million in proceeds.

On July 14, 2015, the Company agreed to an extension of the closing date of the private placement agreement between the Company and CITIC Merchant until July 20, 2015. However, the conditions precedent to the agreement were not fulfilled and CITIC Merchant informed the Company that it would not be subscribing for Common Shares pursuant to the signed private placement agreement.

Interim Funding Loan Commitment

On June 17, 2015, the Company negotiated an interim loan ("Interim Loan") for up to $8 million from Mr. Wilson Chen (a former principal of Novel Sunrise), with immediate availability, intended to address funding obligations pending the closing of the private placements between the Company and CITIC Merchant and Swiss Life GP. In accordance with the terms of the agreement the advances will be in a minimum amount of $2 million, with interest at LIBOR + 12% per annum, payable in cash on a quarterly basis in arrears, and maturing on June 18, 2016. The loan is unsecured and is subject to mandatory repayment upon completion of $30 million of equity or other debt financing.

As at June 30, 2015, the Company had not drawn down any funds under the Interim Loan. The Company has requested a funding drawdown on the Interim Loan multiple times; however, the Company has to date not received such funding.

Turquoise Hill Loan Facility

On May 25, 2014, the Company announced it had obtained a $10 million revolving credit facility from Turquoise Hill to meet its short term working capital requirements. The terms and conditions of this facility were filed on SEDAR (www.sedar.com) on June 2, 2014. The key commercial terms of the facility were as follows:

- Original maturity date of August 30, 2014 (subsequently extended; refer below for details);
- Interest rate of one month US dollar LIBOR Rate in effect plus 11% margin per annum;
- Commitment fee of 35% of interest rate payable quarterly in arrears on undrawn principal amount of facility;
- Front end fee of $0.1 million;
- Draws subject to customary closing conditions and the Company's cash requirements in the ordinary course of business;
- Facility is subject to certain mandatory prepayment and termination provisions; and
- The Company to continue to seek other funding alternatives.

On August 30, 2014 and December 4, 2014, subject to certain conditions and limitations, Turquoise Hill agreed to grant deferrals of the payment of $3.8 million plus accrued interest thereon owing by the Company under the Turquoise Hill Loan Facility on the reduced revolving credit facility of $3.8 million. These deferrals of payment and repayment were granted to the Company without prejudice to Turquoise Hill's right and ability to assert and re-assert at any point in time to demand payment and repayment of all amounts owing to Turquoise Hill under the Turquoise Hill Loan Facility.

On May 4, 2015, following the expiry of the NUR SPA on April 30, 2015, Turquoise Hill agreed to a further limited deferral of repayment, subject to certain conditions and limitations, on the $3.8 million principal and accrued interest owing on the Turquoise Hill Loan Facility as follows:

(i) $1.9 million in principal and all interest that has accrued on and under the Turquoise Hill Loan Facility up to and including August 31, 2015 shall become due and payable on August 31, 2015; and

(ii) $1.9 million in principal and all interest that has accrued on and under the Turquoise Hill Loan Facility from September 1, 2015 up to and including November 30, 2015 shall become due and payable on November 30, 2015.

At June 30, 2015 in addition to the principal of $3.8 million the Company owed accrued interest of $0.4 million under this facility (December 31, 2014 the Company had drawn $3.8 million and owed accrued interest of $0.1 million).

Revolving Loan Commitment

On June 22, 2015, the Company announced it had negotiated a revolving loan commitment (the "Revolving Loan") of RMB200 million (approximately $32 million) from a Chinese commercial bank, subject to the finalization of definitive documentation. The revolving loan commitment is intended to provide additional support to the Company in funding its operational objectives. The Company is negotiating with the bank to finalize the terms with a view to obtaining the Revolving Loan.

Proposed Funding Plan

The Company has commenced the implementation of the Proposed Funding Plan intended to improve cash flow for the Company and support its business strategy and operations in a difficult market, with the goal of positioning the Company with a strong future as a coal producer.
On June 22, 2015, the Company announced a progress update with respect to the Proposed Funding Plan. This included the CITIC Merchant and Swiss Life GP private placements, the Interim Loan, the Revolving Loan all of which are described above and an offtake agreement with a China-based buyer for the sale of 1.8 million tonnes of coal from July 2015 to July 2016.

Subsequent to the change in ownership of Novel Sunrise the Company held discussions with Cinda who confirmed to the Company its continuing support for the Proposed Funding Plan. Therefore the Company will continue with the implementation of the Proposed Funding Plan, which includes expanding its customer base further inland in China, securing longer-term coal offtake arrangements, thereby allowing the Company to ramp up production to capacity and obtaining additional loans as required to meet existing obligations and expected further working capital requirements.

At present the Company has decided to pursue the Proposed Funding Plan described above rather than additional equity placements.

While it is the Company's intention to continue to implement the Proposed Funding Plan as soon as possible, the Proposed Funding Plan is indicative only and the Company's ability to implement it successfully is dependent on a number of factors beyond its control. Such factors include but not limited to, China's economic growth and coal demand growth, market prices of coal, the availability of credit and market interest rates, and exchange rates of currencies of countries where the Company operates. There can be no assurance that the Company will be able to implement the Proposed Funding Plan, or that it will be able to do so in sufficient time to satisfy the TSX's delisting review or to continue as a going concern. In such event, the Company is likely to be unable to meet its obligations, which could result in voluntary or involuntary insolvency proceedings involving the Company (including bankruptcy) as discussed under the heading "Risk Factors" in the December 31, 2014 MD&A issued on March 30, 2015 and available on SEDAR at www.sedar.com.

Going concern considerations

Notwithstanding the provision of the completed private placements, the coal prepayments received from customers and the Turquoise Hill Loan Facility, the Company continues to experience negative impacts on its margins and liquidity and there can be no assurance that the Company will have sufficient funding to be able to continue as a going concern.

The Company anticipates that coal prices in China will remain under pressure in 2015, which will continue to impact the Company's margins and liquidity. Therefore the Company is actively seeking prepaid coal offtake agreements and other additional sources of financing to continue operating and meet its business objectives, while continuing to be focused on minimizing uncommitted capital expenditures and preserving the Company's growth options. The Company, together with its new strategic partner, Novel Sunrise, has developed the Proposed Funding Plan in order to pay the interest due under the CIC Convertible Debenture, meet its obligations as they fall due, achieve its business objectives in 2015 and beyond. These obligations include the Tax Penalty ($18.0 million) (refer to section 6 "Regulatory Issues and Contingencies" for details). However, there is no guarantee that the Company will be able to implement this Proposed Funding Plan or secure other sources of financing. If it fails to do so, or is unable to secure additional capital or otherwise restructure or refinance its business in order to address its cash requirements through June 30, 2016, then the Company is unlikely to have sufficient capital resources or cash flows from mining operations in order to satisfy its ongoing obligations and future contractual commitments, including cash interest payments due on the CIC Convertible Debenture (approximately $16.3 million on November 19, 2015). Refer to section 11 "Risk Factors". Therefore, the Company is actively seeking additional sources of financing to continue operating and meet its objectives.

The Company's consolidated financial statements have been prepared on a going concern basis which assumes that the Company will continue operating until at least June 30, 2016 and will be able to realize its assets and discharge its liabilities in the normal course of operations as they come due; however, in order to continue as a going concern, the Company must generate sufficient operating cash flows, secure additional capital or otherwise pursue a strategic restructuring, refinancing or other transaction to provide it with additional liquidity. If it fails to do so, or is unable to secure additional capital or otherwise restructure or refinance its business in order to address its cash requirements through June 30, 2016, then the Company is unlikely to have sufficient capital resources or cash flows from mining operations in order to satisfy its ongoing obligations and future contractual commitments, including cash interest payments due on the CIC Convertible Debenture, it may not be able to continue as a going concern.

If for any reason, the Company is unable to secure the additional sources of financing and continue as a going concern, then this could result in adjustments to the amounts and classifications of assets and liabilities in the Company's consolidated financial statements and such adjustments could be material.

While the Company intends to secure additional sources of financing as soon as possible, a continued delay in securing additional financing could ultimately result in an event of default of the CIC Convertible Debenture, which if not cured within applicable cure periods in accordance with the terms of such debenture, may result in the principal amount owing and all accrued and unpaid interest becoming immediately due and payable upon notice to the Company by CIC.

The Company is also subject to a remedial delisting review by the TSX in connection with its reliance on the financial hardship exemption from approval by its shareholders of the private placement with Novel Sunrise as announced on February 24, 2015. Refer to the below section "TSX Financial Hardship Exemption Application and Status of Listing on TSX" for details. The failure by the Company to clear the TSX delisting review may result in the delisting of the Common Shares from the TSX which may result in an event of default under the CIC Convertible Debenture. An event of default may result in the principal amount owing and all accrued and unpaid interest becoming immediately due and payable upon notice to the Company by CIC.

Factors that impact the Company's liquidity are being closely monitored and include, but are not limited to, Chinese economic growth, market prices of coal, production levels, operating cash costs, capital costs, exchange rates of currencies of countries where the Company operates and exploration and discretionary expenditures.

At June 30, 2015, the Company had cash of $0.9 million compared to cash of $3.8 million at December 31, 2014. Working capital (excess current assets over current liabilities) was negative $31.3 million at June 30, 2015 compared to positive $3.4 million at December 31, 2014. At August 13, 2015, the Company had cash of $2.0 million.

At June 30, 2015, the Company's gearing ratio was 0.24 (December 31, 2014: 0.23), which was calculated based on the Company's long term liabilities to total assets. At June 30, 2015, the Company is not subject to any externally imposed capital requirements.

TSX Financial Hardship Exemption Application and Status of Listing on TSX

On February 25, 2015, the TSX confirmed that the Company had been placed on remedial delisting review in connection with its reliance on the financial hardship exemption from approval by its shareholders of the private placement with Novel Sunrise. A delisting review is customary practice under TSX policies when a listed company relies on the financial hardship exemption; refer to the Company's MD&A for the year ended December 31, 2014 available on SEDAR at www.sedar.com for additional detail.

Following extension requests by the Company to address delays in the implementation of its Proposed Funding Plan, a meeting of the TSX Committee has been deferred until August 25, 2015 to consider whether the Company has met the listing requirements of the exchange or delist the Common Shares. The TSX Committee has determined to defer its delisting decision until no later than August 28, 2015.

The Company believes the extension will provide sufficient time for the implementation of the next stage of the Proposed Funding Plan, which will allow it to meet its short term financing needs, and that it will be compliant with the continued listing requirements of the TSX; however, no assurance can be provided that the Proposed Funding Plan will be successfully implemented or to the outcome of the remedial delisting review when it occurs and the Common Shares may become subject to delisting from the TSX.

CIC Convertible Debenture

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% (6.4% payable semi-annually in cash and 1.6% payable annually in the Common Shares) with a maximum term of 30 years. The CIC Convertible Debenture is secured by a charge over the Company's assets and certain subsidiaries. The financing was required primarily to support the accelerated investment program in Mongolia and up to $120 million of the financing could also be used for working capital, repayment of debt due on funding, general and administrative expenses and other general corporate purposes. The Company's actual use of financing has been in accordance with the above.

On March 29, 2010, the Company exercised its right to call for the conversion of up to $250.0 million of the CIC Convertible Debenture into approximately 21.5 million Common Shares at a conversion price of $11.64 (Cdn$11.88) per Common Share. As at June 30, 2015, CIC owned, through its indirect wholly owned subsidiary, approximately 15.8% of the issued and outstanding Common Shares.

Under certain conditions, including the non-payment of interest amounts as the same become due, amounts outstanding under the CIC Convertible Debenture may be accelerated. Bankruptcy and insolvency events with respect to the Company or its material subsidiaries will result in an automatic acceleration of the indebtedness under the CIC Convertible Debenture. Subject to notice and cure periods, certain events of default under the CIC Convertible Debenture will result in acceleration of the indebtedness under such debenture at the option of CIC. Such other events of default include, but are not limited to, non-payment, breach of warranty, non-performance of obligations under the CIC Convertible Debenture, default on other indebtedness and certain adverse judgments.

Mongolian IAAC Investigation

In the first quarter of 2013, the Company was subject to orders imposed by Mongolia's Independent Authority against Corruption (the "IAAC") which placed restrictions on certain of the Company's Mongolian assets. The orders were imposed on the Company in connection with the IAAC's investigation of the Company and were continued to be enforced by the Mongolian State Investigation Office (the "SIA"). The restrictions on the assets were reaffirmed in the Tax Verdict and form part of the tax penalty payable by the Company.

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

Following a review by the Company and its advisers, it is the Company's view that the orders placing restrictions on certain of the Company's Mongolian assets did not result in an event of default as defined under the terms of the CIC Convertible Debenture. However, the enforcement of the orders could ultimately result in an event of default of the Company's CIC Convertible Debenture, which if remains uncured for ten business days, would result in the principal amount owing and all accrued and unpaid interest will become immediately due and payable upon notice to the Company by CIC.

Cash Flow Highlights

$ in thousands	Six months ended June 30, 2015	Six months ended June 30, 2014
Cash used in operating activities	**$ (6,158)**	$ (14,056)
Cash used in investing activities	**(4,056)**	(2,707)
Cash generated from financing activities	**7,340**	3,807
Effect of foreign exchange rate changes on cash	**(14)**	(92)
Decrease in cash for the period	**(2,888)**	(13,048)
Cash balance, beginning of period	**3,789**	21,837
Cash balance, end of period	**$ 901**	$ 8,789

Cash used in Operating Activities

The Company used $6.2 million of cash in operating activities in the first six months of 2015 compared to cash used in operating activities of $14.1 million in the first six months of 2014. The primary reason for the decrease in cash used in operating activities for the first six months of 2015 compared to the first six months of 2014 is due to the timing of the CIC Convertible Debenture interest. In May 2014 approximately $7.9 million was paid whereas the May 2015 Interest Installment has been deferred and is now due on November 19, 2015.

Cash used in Investing Activities

In the first six months of 2015, the Company used $4.1 million of cash in investing activities compared to $2.7 million in the first six months of 2014. The cash used in investing activities primarily related to capitalized deferred stripping expenditure included within property, plant and equipment being $4.0 million in the first six months of 2015 compared to a total of $4.1 million being spent on property, plant and equipment in the first six months of 2014. In the first six months of 2014, a net proceeds of $1.3 million from the sale of the Tsagaan Tolgoi mining license was offset with the spending on property, plant and equipment.

Cash generated from Financing Activities

The cash generated from financing activities in the first six months of 2015 primarily related to the proceeds from the private placement with Novel Sunrise for net proceeds of $7.3 million. The cash generated from financing activities in the six months ended June 30, 2014 primarily related to the revolving credit facility from Turquoise Hill of $3.8 million.

Contractual Obligations and Guarantees

Day-to-day mining, expansionary and sustaining capital expenditures as well as administrative operations give rise to commitments for future minimum payments. As at June 30, 2015, the Company's operating and capital commitments were:

	As at June 30, 2015							
	Within 1 year		2-3 years		Over 3 years		Total	
Capital expenditure commitments	$	2,205	$	15,826	$	-	$	18,031
Operating expenditure commitments		9,838		963		263		11,064
Commitments	**$**	**12,043**	**$**	**16,789**	**$**	**263**	**$**	**29,095**

Ovoot Tolgoi Mine Impairment Analysis

Unchanged from the assessment made as at each quarter end in 2014 and the first quarter end of 2015, the Company determined that an indicator of impairment existed for its Ovoot Tolgoi Mine cash generating unit as at June 30, 2015. The impairment indicator was the continued weakness in the Company's share price during the second quarter of 2015 and the fact that the market capitalization of the Company, as at June 30, 2015, was less than the carrying value of its net assets.

Therefore, the Company conducted an impairment test whereby the carrying value of the Company's Ovoot Tolgoi Mine cash generating unit was compared to its "value in use" using a discounted future cash flow valuation model. The Company's cash flow valuation model has been updated to take into consideration the latest available information to the Company, including but not limited to, sales price, sales volumes and washing assumptions, operating cost assumptions and life of mine coal production assumptions as at June 30, 2015. The Company's Ovoot Tolgoi Mine cash generating unit carrying value was $340.6 million as at June 30, 2015.

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

- Long term price estimates from an independent market consulting firm;
- Forecasted sales volumes in line with production levels as per the updated mine plan;
- Updated life-of-mine coal production, strip ratio, capital costs and operating costs;
- A pre-tax discount rate of 17.3% based on an analysis of market, country and the Company specific factors; and
- Coal processing yield of 75%.

Key sensitivities in the valuation model are as follows:

- For each 1% increase/(decrease) in the long term price estimates, the calculated fair value of the cash generating unit increases/(decreases) by approximately $22.2/($22.2) million;
- For each 1% increase/(decrease) in the discount rate, the calculated fair value of the cash generating unit (decreases)/increases by approximately ($23.4)/$25.8 million; and
- For each 1% increase/(decrease) in the cash mining cost estimates, the calculated fair value of the cash generating unit (decreases)/increases by approximately ($13.2)/$13.2 million.

The impairment analysis did not result in the identification of an impairment loss and no charge was required as at June 30, 2015. A decline of more than 2% in the long term price estimates, an increase of more than 2% in the pre-tax discount rate or an increase of more than 3% in the cash mining cost estimates may trigger an impairment charge on the cash generating unit. The Company believes that the estimates and assumptions incorporated in the impairment analysis are reasonable; however, the estimates and assumptions are subject to significant uncertainties and judgments.

The Company is currently reviewing its mine plan for the Ovoot Tolgoi project. Changes to the mine plan may have an impact on the quantities of measured and/or indicated resources and reserves of the Ovoot Tolgoi project.

Investment in RDCC LLC Impairment Analysis

The Company determined that an indicator of impairment existed for its investment in RDCC LLC as at June 30, 2015. The impairment indicator was the continued delay in the commencement of operation.

Therefore, the Company conducted an impairment test whereby the carrying value of the Company's investment in RDCC LLC compared to its "value in use" using a discounted future cash flow valuation model. The carrying value was $26.8 million as at June 30, 2015.

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

- Toll fee estimates reference to the concession agreement;
- Traffic volume;
- Repair, maintenance and operating cost; and
- A pre-tax discount rate of 13.7% based on a weighted average cost of capital of the Company.

Key sensitivities in the valuation model are as follows:

- For each 1% increase/(decrease) in the toll fee estimates or traffic volume, the calculated fair value of the carrying unit increases/(decreases) by approximately $0.3/($0.3) million; and
- For each 1% increase/(decrease) in the discount rate, the calculated fair value of the carrying unit (decreases)/increases by approximately ($1.7)/$1.8 million.

The impairment analysis did not result in the identification of an impairment loss and no charge was required as at June 30, 2015. The Company believes that the estimates and assumptions incorporated in the impairment analysis are reasonable; however, the estimates and assumptions are subject to significant uncertainties and judgments.

On April 30, 2015, in response to Order no. 115 of Mongolia's Ministry of Road and Transportation dated April 29, 2015, a working group was established to assist in the commencement of commercial operations of the Paved Highway. Subsequently, on May 8, 2015 a three month trial period of operation in respect of the Paved Highway commenced. This trial period imposes a nine hundred (900) MNT charge per tonne of coal hauled on the Paved Highway in the Nariinsukhait-Shiveekhuren direction. This charge is lower than the fifteen hundred (1500) MNT charge per tonne stated in the signed concession agreement between RDCC LLC and the State Property Committee of Mongolia which formed the basis for the Company's investment decision. As at August 13, 2015, discussions are ongoing with respect to the pricing levels beyond the initial trial period and in respect to how RDCC LLC will be reimbursed for any difference between the actual rate per tonne charged and the rate per tonne as stated in the concession agreement. RDCC has notified the Company that it expects to be reimbursed or compensated for the reduced pricing levels. However, should the Government of Mongolia not honor the pricing as per the concession agreement or provide sufficient compensation to the Company for the reduced rate, this may lead to an impairment of the Company's investment in RDCC LLC.

Financial Instruments

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

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

The fair values of financial instruments that are traded on an active liquid market are determined with reference to the quoted market prices. Historically, the fair value of the Company's investment in the shares of Kangaroo Resources Limited ("Kangaroo") and Aspire was determined using this methodology. The Company's investment in the shares of Kangaroo and its money market investments were classified as fair value through profit or loss ("FVTPL"). The Company's investment in the shares of Aspire was classified as available-for-sale. The Company disposed all its investment in Aspire and Kangaroo during 2014 and did not hold any Aspire or Kangaroo shares as at December 31, 2014 or June 30, 2015.

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

	As at	
$ in thousands	**June 30, 2015**	**December 31, 2014**
Financial assets		
Loans-and-receivables		
Cash	**$ 901**	$ 3,789
Trade and other receivables	**3,327**	462
Total financial assets	**$ 4,228**	$ 4,251

	As at	
$ in thousands	**June 30, 2015**	**December 31, 2014**
Financial liabilities		
Fair value through profit or loss		
Convertible debenture - embedded derivatives	**$ 3,113**	$ 1,834
Other-financial-liabilities		
Trade and other payables	**24,466**	18,124
Interest-bearing borrowing	**4,158**	3,945
Convertible debenture - debt host	**103,414**	93,353
Total financial liabilities	**$ 135,151**	$ 117,256

The net loss in the second quarter and first six months of 2015 and 2014 respectively included the following amounts of unrealized losses/(gains) from the fair value adjustments to certain financial instruments which are classified as FVTPL:

$ in thousands	Three months ended June 30, 2015	Three months ended June 30, 2014	Six months ended June 30, 2015	Six months ended June 30, 2014
Unrealized loss on FVTPL investments	**$ -**	$ 8	**$ -**	$ 48
Unrealized loss/(gain) on embedded derivatives in CIC convertible debenture	**(265)**	(121)	**1,279**	(1,120)

The Company recorded an unrealized gain of $0.4 million in other comprehensive income in the second quarter of 2014 related to the investment in Aspire compared to an impairment loss of $1.8 million in other operating expenses in the first quarter of 2014. The Company disposed all its investment in Aspire during 2014 and did not hold any Aspire shares as at December 31, 2014 or June 30, 2015.

6. REGULATORY ISSUES AND CONTINGENCIES

Governmental and Regulatory Investigations

The Company was subject to investigations by the IAAC regarding allegations of breaches of Mongolia's anti-corruption laws (the "Anti-Corruption Case"), tax evasion and money laundering (the "Tax Evasion Case"). On March 18, 2013 the Prosecutor's Office decided to split the Tax Evasion Case from the Anti-Corruption Case and on April 12, 2013, the Public Prosecutor of Capital city Prosecutor's Office issued a resolution that the jurisdiction to conduct the investigation on Tax Evasion Case was with the SIA and not the IAAC, and the Tax Evasion Case was transferred to SIA.

While the IAAC has not made any formal accusations against any current or former employee of the Company or the Company under the Anti-Corruption Case, administrative penalties were imposed on certain of the Company's Mongolian assets in connection with the investigation, including a restriction of the use of $1.2 million (the "Restricted Funds") held in bank accounts in Mongolia to spending in Mongolia. The Company has been informed that the Anti-Corruption Case has been suspended; however, it has not received formal notice that the investigation is completed and the restriction on the Restricted Funds remains in place. The Restricted Funds are included within the prepaid expenses and deposits balance in the Company's financial statements. This restriction may have a material impact on the Company's activities in light of the Tax Penalty (MNT 35.3 billion as declared by the Tax Verdict).

Investigations under the Tax Evasion Case included investigations of three of the Company's former employees (the "Former Employees"). On December 30, 2014, the Capital City Prosecutor's Office (Ulaanbaatar, Mongolia) dismissed the allegations of money laundering as not having been proven during the investigation. The Former Employees were indicted for tax evasion by the Prosecutor General on March 14, 2014. The case was sent to the First Instance Second District Criminal Court of Justice (the "District Court"). The Company was advised on May 12, 2014 that the appointed judge of the District Court concluded that the investigation of the Tax Evasion Case initiated by IAAC and continued by SIA was incomplete and ordered the case to be returned to the Prosecutor General for additional investigation. The additional investigation was subsequently completed and the case was sent to the District Court again on June 4, 2014. The trial took place on August 25 and 26, 2014. A panel of three judges appointed to the case returned the case to the Prosecutor General once again for further investigation due to insufficient evidence presented by the prosecutor.

On October 7, 2014, based on the District Court verdict, the SIA ordered a re-investigation (the "Fourth Investigation") into allegations of violations of Mongolian tax laws by the Former Employees. Following the completion of the Fourth Investigation, the Former Employees were indicted again on December 31, 2014 and were subsequently tried in the District Court. On January 30, 2015, the panel of appointed judges from the District Court found the Former Employees guilty of tax evasion and imposed sentences on the Former Employees ranging from 5 years and 6 months to 5 years and 10 months of imprisonment in the correctional facilities of strict regimen in Mongolia. The Former Employees were immediately imprisoned. The Company was informed that, following the receipt of the Tax Verdict, the Former Employees requested pardons from the President of Mongolia and waived their right of appeal. On February 26, 2015 the President of Mongolia issued a decree to pardon to the Former Employees. The Former Employees were released from imprisonment following the decree and departed Mongolia.

The Tax Verdict declared SGS to be financially liable as a "civil defendant" the Tax Penalty of MNT35.3 billion (approximately $18.0 million on June 30, 2015). The Company firmly rejects this conclusion.

On February 18, 2015, the Company appealed the Tax Verdict (the "Tax Verdict Appeal") on the grounds that it has prepared its financial statements, including those of SGS, in compliance with IFRS, and lodged all its tax returns in the required format under Mongolian tax law. The hearing of the Tax Penalty Appeal took place on March 25, 2015 at the 10th Appeal Court for Criminal Case of Mongolia (the "Court of Appeal") and a panel of three appointed judges decided to uphold the Tax Verdict and dismissed the Tax Verdict Appeal by the Company. It is the view of the Company that there is a lack of evidence to support both the Tax Verdict and the Appeal Verdict. The Company received the written version of the Appeal Court's verdict ("Appeal Verdict") on April 10, 2015. The Company lodged a final appeal with the Supreme Court of Mongolia on April 22, 2015. In accordance with Mongolia's criminal procedure law, SGS filed the appeal with the Supreme Court of Mongolia through the Second District Criminal Court of Justice.

On April 29, 2015 the Second District Criminal Court refused to advance SGS's appeal to the Supreme Court. Following an immediate protest by SGS, the Second District Criminal Court delivered SGS's appeal to the Supreme Court of Mongolia.

On May 20, 2015, SGS was informed that the Supreme Court had refused to hear the appeal and had returned the appeal to the Second Criminal Court of Justice. The Supreme Court based its decision on a restrictive reading of Article 342 of the Criminal Procedure Law of Mongolia which stipulates that "the defendant, person acquitted, the victim, and their respective defense counsel have the right to lodge a complaint to the Supreme Court". The Supreme Court concluded that the omission of a specific reference to a civil defendant in Article 342, in and of itself denies SGS, in such capacity, the right to lodge an appeal to the Supreme Court.

In its decision, the Supreme Court did not address other provisions of the Criminal Procedure Law and the Law on Courts of Mongolia, which provide that civil defendants have standing to appeal to the Supreme Court and that no judicial proceedings or decisions in Mongolia are outside of the scope of supervision by the Supreme Court.

On May 21, 2015, SGS sent an official letter of protest to the Presiding Justice of the Criminal Chamber of the Supreme Court (the "Presiding Justice"), challenging the decision to refuse to hear the tax case on appeal. On June 2, 2015, SGS received a formal response from the Presiding Justice, confirming the Supreme Court's refusal to hear the tax case. In the letter, the Presiding Justice reaffirmed the restrictive interpretation of Article 342 of the Criminal Procedure Law.

With the refusal by the Supreme Court to hear the case on appeal, the Tax Verdict has entered into force. The Tax Verdict is, however, not immediately payable and enforceable against SGS absent further actions prescribed by the laws of Mongolia. In particular, SGS has not received a copy of the bailiff's resolution on execution of the Tax Verdict, as required under the Law of Mongolia on Execution of Court Decisions in order for any judgment execution process to happen. However, the Company made a corresponding provision for the court case penalty of $18.0 million as at June 30, 2015 given the Tax Verdict has entered into force.

The Company continues to believe that there is a lack of evidence to support the Tax Verdict and that the Tax Verdict and the subsequent decisions of the higher courts on appeal were substantively and procedurally in error under the laws of Mongolia.

While the Company had various additional legal avenues available to it to continue defending itself, it has decided to and is currently seeking to resolve amicably the dispute giving rise to the Tax Verdict in a manner that is both appropriate having regard to the Company's limited financial resources and supportive of a positive environment for foreign investment in Mongolia. There can be no assurance, however, that any such resolution can be successfully negotiated by the Company either at all or on favourable terms, or that the terms of any resolution to which the Government would be prepared to agree would not be materially adverse to the Company. In such case, this may result in an event of default under the Debenture held by CIC and CIC would have the right to declare the full principal and accrued interest owing thereunder immediately due and payable. Such an event of default under the Debenture or the Company's inability to pay the penalty could result in voluntary or involuntary proceedings involving the Company (including bankruptcy) as discussed under the heading Risk Factors in the MD&A issued on March 30, 2015 and available on SEDAR at www.sedar.com. However, with the Presiding Justice having upheld the decision to refuse to hear the case on appeal, this exhausts the legal appeals available to the Company in Mongolia.

Internal Investigations

Commencing in September 2012, through its Audit Committee (comprised solely of independent directors), the Company has conducted an internal investigation into possible breaches of law, internal corporate policies and codes of conduct arising from the allegations which have been raised through the investigations in Mongolia. The Chair of the Audit Committee has also participated in a tripartite committee, comprised of the Audit Committee Chairs of the Company and Turquoise Hill and a representative of Rio Tinto, which focused on the investigation of a number of those allegations, including possible violations of anti-corruption laws. The tripartite committee substantially completed the investigative phase of its activities during the third quarter of 2013. There have been no significant developments in respect of the internal investigations since the completion of the investigative phase during the third quarter of 2013.

The investigations referred to above could result in one or more Mongolian, Canadian, United States or other governmental or regulatory agencies taking civil or criminal action against the Company, its affiliates or its current or former employees. The likelihood or consequences of such an outcome are unclear at this time but could include financial or other penalties, which could be material, and which could have a material adverse effect on the Company. Refer to the Company's MD&A for the year ended December 31, 2014, which is available on SEDAR at www.sedar.com, section 14 risk factors, "the Company is subject to continuing governmental, regulatory and internal investigations, the outcome of which is unclear at this time but could have a material adverse effect on the Company".

Mining Prohibition in Specified Areas Law

In July 2009, Mongolia promulgated the Law on Prohibiting Mineral Exploration and Extraction Near Water Sources, Protected Areas and Forests (the "Mining Prohibition in Specified Areas Law"). Pursuant to the Mining Prohibition in Specified Areas Law, the Government of Mongolia has defined the boundaries of certain areas in which exploration and mining is purportedly prohibited. A list of licenses has been prepared that overlap with the prohibited areas described in the law based on information submitted by water authority agencies, forest authority agencies and local authorities for submission to the Government of Mongolia.

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

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

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

The Mining Prohibition in Specified Areas Law has not been adequately enforced mainly due to compensation issues due to the license holders.

In order to address the issues facing its implementation, in February, 2015 the Parliament of Mongolia adopted an amendment to the Law on Implementation of the Mining Prohibition in Specified Areas Law (the "Amended Law on Implementation"). The Amended Law on Implementation provides an opportunity for license holders covered within the scope of application of the Mining Prohibition in Specified Areas Law to continue their mining operations subject to advance placement of funds to cover 100% of the future environmental rehabilitation costs. A model contract and a specific Government regulation on this requirement will be adopted by the Government. The licence holders must also apply within 3 months after the amendment to the Law on Implementation comes into effect for permission to the Mineral Resource Authority of Mongolia (the "MRAM") to resume activities. The Company submitted its application with respect to its mining licenses before the deadline set on June 16, 2015 and hasn't yet received any communication from the MRAM on the status of its application.

The potential impact of the Mining Prohibition in Specified Areas Law on the Company's operations is unclear pending the adoption by the Government of the relevant regulations pursuant to the Amended Law on implementation. The Company will continue to monitor the developments and ensure that it follows the necessary steps in the Amended Law on Implementation to secure its operations and licenses and is fully compliant with Mongolian law.

Special Needs Territory in Umnugobi

On February 13, 2015, the whole of the Soumber mining license and a portion of SGS' exploration license No.9443 X (the "License Areas") were included into a special protected area (to be further referred as Special Needs Territory "SNT") newly set up by the Umnugobi Aimag's Civil Representatives Khural (the "CRKh") to establish a strict regime on the protection of natural environment and prohibit mining activities in the territory of the SNT.

In March 2015, SGS filed a complaint with the 12th Court for Administrative Cases of First Instance (the "Administrative Court") seeking the annulment of CRKh's decision to the extent it impacted the License Areas. In parallel, SGS initiated negotiations with the CRKh in order to reach an acceptable solution.

On July 8, 2015, SGS and the Chairman of the CRKh, in his capacity as the respondent's representative, reached an agreement (the "Amicable Resolution Agreement") to exclude the License Areas from the territory of the SNT in full, subject to confirmation of the Amicable Resolution Agreement by the session of the CRKh. The parties formally submitted the Amicable Resolution Agreement to the appointed judge of the Administrative Court for her approval and requested a dismissal of the case in accordance with the Law of Mongolia on Administrative Court Procedure. On July 10, 2015, the judge issued her order approving the Amicable Resolution Agreement and dismissing the case, while reaffirming the obligation of CRKh to take necessary actions at its next session to exclude the License Areas from the SNT and register the new map of the SNT with the relevant authorities. The Company has not yet received any indication on the timing of the next session of the CRKh.

Commercial arbitration in Hong Kong

On June 24, 2015, First Concept served the Notice on SGS in respect of the Coal Supply Agreement. The arbitral proceedings (the "Arbitration") are deemed to have commenced on June 24, 2015, as the date when the respondent received the Notice.
According to the Notice, First Concept: alleged, *inter alia*, (i) that SGS had failed and/or wrongfully refused to sell any coal to First Concept; (ii) expressed its wish to have the dispute settled in an arbitration to be administered by the Hong Kong International Arbitration Centre; and (iii) sought the repayment of the prepayment, in the sum of $11.5 million, it made to SGS under the Coal Supply Agreement, as well as any and all damages that may be due to it.

Under the Coal Supply Agreement, SGS agreed to sell coal to First Concept between May 22, 2014 and May 31, 2015 for a total consideration of $11.5 million. It was also agreed that that First Concept would pre-pay the $11.5 million. While First Concept fulfilled its payment obligation under the contract, it totally failed to fulfill its obligation to collect and transport the coal. Pursuant to the Coal Supply Agreement that obligation fell squarely on First Concept, while SGS was only obliged to make the coal available at its stockpile. The sole reason for the lack of coal sales to First Concept was the continued failure of First Concept to complete the necessary legal requirements for collection and transportation of coal and to provide a pickup schedule in accordance with industry practice. Contrary to the allegation by First Concept that SGS "wrongfully refused" to sell the coal, SGS has repeatedly advised First Concept of its willingness, ability and readiness to make available the coal for collection at its stockpile. In fact, SGS, at all times during the term of the Coal Supply Agreement, had more than sufficient coal at its stockpile to meet its obligations.

The Company, therefore, firmly rejects the allegations of First Concept in the Notice as lacking any merit and will vigorously defend itself in the Arbitration, including claiming the relevant fees and damages from First Concept.

There can be no assurance, however, that the Company will prevail in the Arbitration. Should SGS be unsuccessful in the Arbitration, the Company may not be able to re-pay the sum of $11.5 million. In such case, this may result in an event of default under the Debenture held by CIC and CIC would have the right to declare the full principal and accrued interest owing thereunder immediately due and payable. Such an event of default under the Debenture or the Company's inability to re-pay the $11.5 million to First Concept could result in voluntary or involuntary proceedings involving the Company.

Class Action Lawsuit

On or about January 6, 2014, Siskinds LLP, a Canadian law firm, filed a proposed securities class action (the "Ontario Action") against the Company, certain of its former senior officers and current directors, and its former auditors, Deloitte LLP, in the Ontario Superior Court of Justice in relation to the Company's restatement of financial statements as previously disclosed in the Company's public filings.

There have been no significant developments in respect of the class action lawsuit since the first quarter ended March 31, 2014. For more details, refer to the Company's Management Discussion and Analysis for the quarter ended March 31, 2014 available on SEDAR at www.sedar.com, and, in particular, the sub-section on "Contingencies – Class Action Lawsuit" of the "Regulatory Issues and Contingencies".

The Company disputes and will vigorously defend itself against these claims through independent Canadian litigation counsel retained by the Company and the other defendants for this purpose. Due to the inherent uncertainties of litigation, it is not possible to predict the final outcome of the Ontario Action or determine the amount of any potential losses, if any. However, the Company has judged a provision for this matter at June 30, 2015 is not required.

Notice of claim by former Chief Executive Officer

On June 30, 2015, the Company was served with a Notice of Civil Claim filed by the Company's former President and Chief Executive Officer, Alexander Molyneux, in the British Columbia Supreme Court. The claim relates to alleged breaches of Mr. Molyneux's employment agreement by the Company. In addition to the Company, Turquoise Hill Resources Ltd., the Company's largest shareholder at the time of Mr. Molyneux's employment, was also named in the claim.

Mr. Molyneux acted as the Company's President (from April 2009) and Chief Executive Officer (from October 2009) until September 2012, when the Company terminated his employment.

Mr. Molyneux is seeking damages in excess of $1 million in his Notice of Claim. The Company considers the action is without merit. SouthGobi intends to vigorously defend the action and reserves its right to pursue all legal rights and remedies available to it in connection with the proceedings.

7. RELATED PARTY TRANSACTIONS

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

- Turquoise Hill – Prior the completion of the Novel SPA and private placement with Novel Sunrise on April 23, 2015, Turquoise Hill was the Company’s immediate parent company. TRQ’s shareholding at April 1, 2015 was approximately 48% which declined to 23% at June 30, 2015 of the outstanding Common Shares following the completion of the Novel SPA. Turquoise Hill provides various administrative services to the Company on a cost-recovery basis.
- Rio Tinto – Prior to the completion of the Novel SPA and private placement with Novel Sunrise on April 23, 2015, Rio Tinto was the Company’s ultimate parent company. The Company recovers administration and other costs incurred on behalf of Rio Tinto on a cost-recovery basis. Rio Tinto recovers from the Company the costs of salaries and benefits of employees assigned to work for the Company and recovers legal and professional fees from the Company in respect of the internal and tripartite committees referred to in section 6 “Regulatory Issues and Contingencies”.
- Turquoise Hill Resources Singapore Pte. Ltd. (“Turquoise Hill Singapore”) – Turquoise Hill Singapore (formerly I2MS.NET Pte. Ltd.) is a private company 100% owned by Turquoise Hill. Turquoise Hill Singapore provides information technology and other related services to the Company on a cost-recovery basis.
- Mr. Wilson Chen – Mr. Chen is the former principal of Novel Sunrise. He was a related party for the period March 3, 2015 until July 16, 2015 and during this period the Interim Loan agreement was entered into, refer to section 5. “Liquidity and Capital Management” under the heading “Interim Funding Loan Commitment” for further details.

The following tables summarize related party expense and recovery amounts with the related parties listed above:

	Three months ended June 30,		Six months ended June 30,	
	2015	**2014**	**2015**	**2014**
Corporate administration	**$ 130**	$ 161	**$ 211**	$ 373
Salaries and benefits	**204**	350	**144**	899
Finance costs	**107**	157	**213**	157
Related party expenses	**$ 441**	$ 668	**$ 568**	$ 1,429

	Three months ended June 30,		Six months ended June 30,	
	2015	**2014**	**2015**	**2014**
Turquoise Hill	**$ 107**	$ 227	**$ 213**	$ 241
Rio Tinto	**251**	358	**192**	911
Turquoise Hill Singapore	**83**	83	**164**	278
Related party expenses	**$ 441**	$ 668	**$ 569**	$ 1,430

	Three months ended June 30,		Six months ended June 30,	
	2015	**2014**	**2015**	**2014**
Corporate administration	**$ -**	$ 17	**$ -**	$ 17

	Three months ended June 30,		Six months ended June 30,	
	2015	**2014**	**2015**	**2014**
Turquoise Hill	**$ -**	$ 17	**$ -**	$ 17
Related party expense recovery	**$ -**	$ 17	**$ -**	$ 17

As at June 30, 2015, the Company had payables totaling $12.8 million (December 31, 2014: $12.5 million) including amounts classified as interest-bearing borrowings totaling $4.2 million as at June 30, 2015, (December 31, 2014: $3.9 million) with related parties. Included in the accounts payable balance as at June 30, 2015 and at December 31, 2014 are $5.3 million of legal and professional fees payable to Rio Tinto in respect of the internal and tripartite committees referred to in section 6 "Regulatory Issues and Contingencies".

8. 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 August 13, 2015, 245.7 million Common Shares were issued and outstanding. There are also incentive share options outstanding to acquire 2.3 million unissued Common Shares with exercise prices ranging from Cdn$0.65 to Cdn$12.58. There are no preferred shares outstanding.

As at August 13, 2015 Novel Sunrise holds a total of approximately 72.1 million Common Shares representing approximately 29.4% of the issued and outstanding Common Shares.

As at August 13, 2015, Turquoise Hill directly owned approximately 54.4 million Common Shares representing approximately 22.2% of the issued and outstanding Common Shares.

As at August 13, 2015 CIC holds a total of 37.9 million Common Shares representing approximately 15.4% of the issued and outstanding Common Shares.

9. INTERNAL CONTROLS OVER FINANCIAL REPORTING

There has been no significant 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.

10. CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS

The preparation of financial statements in conformity with IFRS requires the Company to establish accounting policies and to make estimates and judgments 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 3 to the Company's consolidated financial statements for the year ended December 31, 2014. Please refer to note 3.22 of the Company's December 31, 2014 consolidated financial statements for information regarding the accounting judgments and estimates that have the most significant effect on the amounts recognized in the Company's consolidated financial statements. These significant accounting judgments and estimates remain unchanged from December 31, 2014.

11. RISK FACTORS

There are certain risks involved in the Company's operations, some of which are beyond its control. Material risks and uncertainties affecting the Company, their potential impact and the Company's principal risk management strategies are, except as updated by this MD&A, substantially unchanged from those disclosed in the Company's MD&A for the year ended December 31, 2014, which is available at www.sedar.com.

12. OUTLOOK

The outlook for Mongolian coal exports remains dependent on the Chinese economy. Market conditions and prices for coal remained weak in China during the first half of 2015.

The Company anticipates that coal prices in China will remain under pressure through the remainder of 2015, which will continue to impact the Company's margins and liquidity. The Company continues to strive for further cost reductions and where possible will delay expenditures. In addition, the Company entered into the transaction with Novel Sunrise as a new significant shareholder and strategic partner intending to bring its operational and marketing expertise to the Company. Novel Sunrise has agreed to assist the Company in implementing the Proposed Funding Plan intended to improve cash flow for the Company and support its business strategy and operations in a difficult market, with the goal of positioning the Company with a strong future as a coal producer. The Proposed Funding Plan includes introducing potential customers in China to the Company to allow the Company to expand its customer base further inland in China, and helping the Company to secure longer-term coal offtake arrangements, thereby allowing the Company to ramp up production to capacity. Novel Sunrise also intends to help the Company to establish relationships with commercial banks in China and Hong Kong to help the Company to secure short term bridge loans, trading credit facilities and other types of financing.

The Company's consolidated financial statements have been prepared on a going concern basis which assumes that the Company will continue operating until at least June 30, 2016 and will be able to realize its assets and discharge its liabilities in the normal course of operations as they come due. While the Company is actively seeking additional sources of financing to continue operating and meet its objectives, there can be no assurance that such financing will be available on terms acceptable to the Company. If for any reason, the Company is unable to implement the Proposed Funding Plan or is not able to secure additional sources of financing to continue as a going concern, adjustments to the amounts and classifications of assets and liabilities in the Company's consolidated financial statements may be required and such adjustments could be material.

A continued delay in securing additional financing could ultimately result in an event of default of the Convertible Debenture, which if not cured within applicable cure periods in accordance with the terms of such debenture, may result in the principal amount owing and all accrued and unpaid interest becoming immediately due and payable upon notice to the Company by CIC.

The Company remains well positioned in the market, with a number of key competitive strengths, including:

- **Strategic location** – The Ovoot Tolgoi Mine is located approximately 40km from China, which represents the main coal market. The Company has an infrastructure advantage, being approximately 50km from a major Chinese coal distribution terminal with rail connections to key coal markets in China.

- **Large resource base** – The Company's aggregate coal resources include measured and indicated resources of 497 million tonnes and inferred resources of 293 million tonnes. These numbers have been aggregated from the Ovoot Tolgoi Technical Report, the Soumber Technical Report and the Zag Suuj Technical Report. The Measured and Indicated Coal Resources are inclusive of those Coal Resources modified to produce the Coal Reserves.

- **Several growth options** – Assuming the Company is able to manage its liquidity issues, successfully implement the Proposed Funding Plan and there are no material changes to the Company's mine plan resulting from the mine plan review currently underway, the Company has several potential growth options, including an anticipated increase to 9 million tonnes annual run-of-mine capacity at the Ovoot Tolgoi Mine as well as greenfield options with the Soumber Deposit and Zag Suuj Deposit, located approximately 20km east and approximately 150km east of the Ovoot Tolgoi Mine, respectively.

- **Flexible product offering** – Most of the Company's coal resources have coking properties, including a mixture of semi-soft coking coals and hard coking coals. The Company is currently studying options to supply washed coal to the market to further improve its market position and access to end customers.

Objectives

The Company's objectives for 2015 and the medium term are as follows.

- Execute step change improvement in the Company's sales, marketing and logistics capabilities and expand the Company's customer base further inland in China – Subject to available financial resources and in cooperation with the Company's new strategic partner, Novel Sunrise, implement an effective business structure and production profile that is capable of delivering a profitable product mix to the Chinese market.

- Drive operational excellence – The Company is focused on further improving productivity and operational efficiency in delivering production to meet market requirements.

- Progress growth options – Subject to available financial resources, the Company plans to further the development of the Soumber Deposit, while staying compliant with all government requirements in relation to its licenses and agreements.

- Operate in a socially responsible manner – The Company is focused on maintaining the highest standards in health, safety and environmental performance.

- Enhance the Company's reputation – The Company is committed to contributing to the long term development and prosperity of Mongolia and its local communities.

August 13, 2015