



SouthGobi
Energy Resources

SouthGobi Energy Resources Ltd.

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

March 31, 2009

(Stated in U.S. Dollars)

SOUTHGOBI ENERGY RESOURCES LTD

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(Unaudited)

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OVERVIEW

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

The Company's common shares trade on the TSX Venture Exchange ("TSX-V") under the symbol SGQ.

Prior to the May 2007 coal transaction, the Company was a mineral exploration company with a focus on precious and base metal exploration and development in Mongolia, and elsewhere. Having completed the coal transaction in May 2007 and with the sale of its Metals Division on December 30, 2008, which was completed in the first quarter of 2009, the Company's principal focus is now on its Mongolian coal operation at Ovoot Tolgoi and coal exploration and development in southern Mongolia and Indonesia.

Recent Developments

Ovoot Tolgoi Project Development

Coal shipments commenced late September 2008, and continued throughout the fourth quarter 2008. During November 2008, the Company reached its budgeted production target of 1 million tonnes of coal. Total production for 2008 was 1.16 million tonnes.

In January and February 2009, the Company experienced difficulty expediting the movement of its coal shipments through the Mongolia-China border at Ceke due to relatively erratic and unpredictable opening hours and sporadic closures of the border point. Through early 2009 shipments across the border point were limited. As a result, the Company initiated a production curtailment program in January 2009, decreasing production to preserve cash and to manage stockpiles.

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

As discussions continued with the Mongolian Government, border access improved towards the end of the first quarter of 2009 and in March 2009 the border point started operating eight hours per day, seven days per week. This resulted in increased shipments for the month of March, with sales of over 115,000 tonnes of coal.

Work continues on construction activities for the permanent man camp and permanent shop facility, with these facilities scheduled for completion in mid-2009. The mine airstrip surfacing has been completed and final permitting was received for the concrete airstrip.

In January 2009, the Mongolian Government formally recognized the Company's strong exploration program and timely government reporting process, with two separate awards.

In July 2008, the Company announced that it had received an updated resource estimate in respect of the West Field portion of the Ovoot Tolgoi coal project in Mongolia from an independent third party technical consultant. The consultant subsequently advised the Company, and the Company announced in March 2009, that errors had been discovered in the resource estimate and that these errors resulted in an overstatement of the resources in the West Field reported by the Company in July 2008, primarily in the indicated and inferred categories. In the March 2009 announcement, the Company published a corrected resource estimate and further noted that the current mine plan and operations are not impacted by the revision. See "MINERAL PROPERTIES – Properties in Mongolia – Ovoot Tolgoi Open Pit Project".

Mamahak Project Development

In April 2008, the Company entered into a Joint Venture Earn-In Agreement with an Indonesian company to explore and develop a coal project, in East Kalimantan, Indonesia, known as the Mamahak coal project ("MCM"). In September 2008, based on positive exploration results, the Company increased its working interest in MCM to 85%.

In early January 2009, the Company announced that a location permit was issued, which allows the Company to commence surface coal mining on MCM.

During the first quarter of 2009, the Company received a series of results from its coal sampling programs on the MCM concession. The results suggest the coal is of a premium character and has some unique characteristics suitable for coking processes. In particular, the coal has high fluidity. The results prompted the Company to continue efforts to develop an operating mine at the site. The mine, infrastructure and barge load out are being completed. The intent is to mine and ship test cargoes of approximately 30,000 tonne lots to customers. The Company has engaged two smaller mining contractors who have significant experience in operations similar to Mamahak.

In February 2009, the Company announced that it had received an initial resource estimate from its independent consultants, SMG Consultants ("SMG") in respect of the E resource block and the SW resource block on the MCM concession. The Company filed a technical report supporting the resource estimate in March 2009, which is available at www.sedar.com. See "MINERAL PROPERTIES – Properties in Indonesia – Mamahak Coal Project.

Corporate Activity

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

On February 10, 2009, the Company announced the appointment of Alexander Molyneux as its new President, effective April 27, 2009. Based in Hong Kong, he was most recently Managing Director, Head of Metals & Mining Investment Banking, Asia Pacific, with Citigroup.

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

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

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

Ivanhoe, directly and indirectly, currently owns 106,804,155 common shares representing approximately 80% of the issued and outstanding common shares of SouthGobi.

FORWARD LOOKING STATEMENTS

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

INTERNATIONAL FINANCIAL REPORTING STANDARDS (IFRS)

Transition to IFRS from GAAP

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

As previously disclosed, the Company is in the application process for a secondary listing of its common shares on an Asian stock exchange. As part of the application process, the Company is required to provide financial statements under IFRS with three years of comparative data. In order to produce the required International Accounting Standards Board (“IASB”) financial statements the Company has produced 2008 interim IFRS statements with an IFRS adoption date of January 1, 2009 and IFRS transition date of January 1, 2005. As per Appendix A of IFRS 1 “An entity cannot have more than one set of IFRS financial statements. Therefore, it must have only one starting point for transition to IFRS”. In March 2009, the Company was granted exemptive relief by Canadian securities regulatory authorities under Staff Notice 52-321 and has been permitted to adopt IFRS for Canadian reporting purposes for reporting periods beginning on or after January 1, 2009. The Company has adopted IFRS with an adoption date of January 1, 2009 and a transition date of January 1, 2005.

IFRS Conversion

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

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

Impact of IFRS

IFRS employs a conceptual framework that is similar to Canadian GAAP; however significant differences exist in certain matters of recognition, measurement and disclosure. While the adoption of IFRS will not change the actual cash flows of the Company, the adoption will result in changes to the reported financial position and results of operations of the Company. In order to allow the users of the financial statements to better understand these changes, we have provided the reconciliations between

Canadian GAAP and IFRS for the total assets, total liabilities, shareholders equity and net earnings in Note 3 to the interim consolidated financial statements. The adoption of IFRS has had no significant impact on the net cash flows of the Company. The changes made to the statements of financial position and comprehensive income have resulted in reclassifications of various amounts on the statements of cash flows, however as there has been no change to the net cash flows, no reconciliations have been presented.

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

Initial Adoption of International Accounting Standards

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

Comparative Information

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

CRITICAL ACCOUNTING ESTIMATES

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

A detailed summary of all of the Company's significant accounting policies is included in Note 4 to the Consolidated Financial Statements for the three months ended March 31, 2009. Note 3 to the Consolidated Interim Financial Statements for the three months ended March 31, 2009 provides a review of the significant changes to the reported financial position and results of operations of the Company under Canadian GAAP and IFRS.

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

Mineral Property and Exploration Costs

All direct costs related to the acquisition of mineral property interests are capitalized into intangible assets on a property by property basis. Exploration costs, net of incidental revenues, are charged to operations in the period incurred until such time as it has been determined that a property has economically recoverable reserves, in which case subsequent exploration costs and the costs incurred to develop a property are capitalized into PPE. Exploration costs include value-added taxes incurred in foreign jurisdictions when recoverability of these taxes is uncertain. On the commencement of

commercial production, depletion of each mining property will be provided on a unit-of-production basis using estimated resources as the depletion base.

At each date of the statement of financial position, the Company reviews the carrying values of its mineral property interests to determine whether there is an indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss (if any). Recoverable amount is the higher of fair value less costs to sell and value in use. If the recoverable amount is estimated to be less than its carrying amount, the carrying amount is reduced to its recoverable amount.

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

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

Inventory valuation

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

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

Stripping costs

Stripping costs incurred during the development of a mine are capitalized into PPE. Stripping costs incurred during the production phase are variable production costs that are included in the costs of inventory produced during the period that the stripping costs are incurred, unless the stripping activity can be shown to give rise to future benefits from the mineral property, in which case the stripping costs would be capitalized into PPE. Future benefits arise when stripping activity increases the future output of the mine by providing access to a new ore body. Capitalized stripping costs are depleted on a unit-of-production basis, using estimated resources as the depletion base.

Effective April 2, 2008, on commencement of mining operations, the Company has capitalized its stripping costs.

Income taxes

Current income tax assets and liabilities for the current and prior periods are measured at the amount expected to be recovered from or paid to the taxation authorities. The tax rates used to compute the amount are those that are enacted or substantively enacted by the date of the statement of financial position..

Deferred income tax is provided using the liability method on temporary differences at the date of the statement of financial position between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

Stock-based compensation

The Company accounts for stock options granted to directors, officers, employees and service providers using the Black-Scholes option pricing model. Option pricing models require the input of highly subjective assumptions regarding the expected volatility. Changes in assumptions can materially affect the fair value estimate, and therefore, the existing models do not necessarily provide a realistic measure of the fair value of the Company's stock options at the date of the grant or thereafter.

Revenue recognition

Sales revenues are recognized when the risk and rewards of ownership pass to the buyer, collection is reasonably assured and the price is reasonably fixed and determinable. This occurs when the coal is either loaded onto a truck or when it is unloaded at the financial destination, depending on the terms of the contract.

Depletion and depreciation of property, plant and equipment

Property, plant and equipment comprise the largest component of the Company's assets and, as such, the depreciation of these assets has a significant effect on the Company's financial statements.

On the commencement of commercial production, depletion of each individual mining property is provided on the unit-of-production basis using estimated resources as the depletion basis.

The mining equipment and other capital assets are depreciated, over their expected economic lives using either the unit-of-production or straight-line method. Capital projects in progress are not depreciated until the capital asset has been put into operation.

The estimates of the resources for the depletion basis are determined based on professional evaluation, but may change based on additional knowledge gained subsequent to the initial assessment. A change in the original resource estimates would result in a change in the rate of depletion of the related mining assets.

CHANGE IN ACCOUNTING POLICIES

On January 1, 2009, the Company adopted IFRS. The provisions of new and revised standards and interpretations are applicable and effective for the Company's financial year beginning on or after January 1, 2009.

A summary of the new and revised standards and interpretations are outlined in Note 2.3 of the Consolidated Interim Financial Statements for three months ended March 31, 2009.

NON-IFRS FINANCIAL MEASURES

(\$ in thousands, unless otherwise stated)

This management discussion and analysis refers to certain financial measures, such as "cash costs", which are not standardized measures recognized under IFRS and do not have a standardized meaning prescribed by IFRS. These measures are commonly utilized in the mining industry and are considered informative for management, shareholders and analysts. These measures may differ from those made by other corporations and accordingly may not be comparable to such measures as reported by other companies.

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

	Three Months Ended		
	March 31, 2009	December 31, 2008	March 31, 2008
Cash costs, continuing operations			
Cost of sales per financial statements	\$ 3,213	\$ 2,178	-
Less non-cash adjustments	(855)	(586)	-
Total cash costs	2,358	1,592	-
Coal sales (<i>tonnes</i>)	127,366	113,000	-
Total cash costs of product sold (<i>per tonne</i>)	\$ 18.51	\$ 14.09	-

	Three Months Ended		
	March 31, 2009	December 31, 2008	March 31, 2008
Cash costs, continuing operations			
Direct cash costs of product sold (<i>per tonne</i>)	\$ 14.29	\$ 8.30	-
Mine administration cash costs of product sold (<i>per tonne</i>)	4.22	5.79	-
Total cash costs of product sold (<i>per tonne</i>)	\$ 18.51	\$ 14.09	-

MINERAL PROPERTIES

Qualified Persons

Disclosure of a scientific or technical nature in this Management Discussion and Analysis of Financial Condition and Results of Operations (“MD&A”) with respect to the Company’s Coal Division was prepared by, or under the supervision of Gene Wusaty, P.Eng, and Chief Operating Officer and Stephen Torr (P.Geo.), Resource Manager. Each of Messrs. Torr and Wusaty is a “qualified person” for the purposes of National Instrument 43-101 of the Canadian Securities Administrators (“NI 43-101”).

Mr Torr was appointed the Company’s new Resource Manager on March 20, 2009.

Coal Group Profile

Mongolia Exploration Licenses

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

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

As at April, 9 2009, the Company held 43 licenses, which in total cover an area of approximately 1.7 million hectares (“ha”).

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

Properties in Mongolia

Ovoot Tolgoi Open Pit Project

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

The Nariin Sukhait property was renamed “Ovoot Tolgoi” to differentiate the Company’s coal exploration and development project in Mongolia’s South Gobi Province from the adjoining Nariin Sukhait coal mine owned by the Mongolian-Chinese joint venture company, MAK/Qinhua.

Ivanhoe first initiated coal exploration in the Ovoot Tolgoi area in October 2004 and extensive exploration programs were also carried out in 2005, 2006 and 2007. Resources at the Ovoot Tolgoi property are found in two different areas, referred to as the South-East and the West Fields. The Company’s independent consultant, Norwest Corporation (“Norwest”) estimated that, as of December 31, 2006, the South-East Field hosted 49.8 million tonnes of measured resources, 15.9 million tonnes of

indicated resources and 6.5 million tonnes of inferred resources. Norwest also estimated 55.1 million tonnes of measured resources, 28.7 million tonnes of indicated resources and 22.6 million tonnes of inferred resources for the West Field.

In July 2008, the Company announced that its independent technical consultant, The Americas Group, Inc. ("TAG") of Lakewood, Colorado had prepared a new resource estimate for the West Field portion of the Ovoot Tolgoi coal project in Mongolia. TAG subsequently advised the Company, and the Company announced in March 2009, that errors had been discovered in the resource estimate and that these errors resulted in an overstatement of the resources in the West Field reported by the Company in July 2008, primarily in the indicated and inferred categories. The current resource estimates for the separate South-East Field and the Ovoot Tolgoi underground project were not affected by the errors. An amended report updating the resource estimate was filed on May 1, 2009 and is available at www.sedar.com.

The corrected West Field resource estimate is 75.0 million tonnes of measured resources, 27.7 million tonnes of indicated resources and 18.8 million tonnes of inferred resources.

The Company has engaged Norwest to complete a new technical report for the Ovoot Tolgoi project incorporating outstanding data obtained from drilling to the end of 2008, reflecting a redesign of the surface mine to a depth of 300 metres from the present 250 metres, updating the resource models and delineating reserves based on a pre-feasibility level of engineering. The Company expects to receive this report later in 2009. Management believes this new report will more fully demonstrate the potential of the Ovoot Tolgoi coal deposit.

The Company made considerable progress in identifying additional resources at Ovoot Tolgoi in 2008, drilling over 23,200 metres down to a depth of 800 metres in the West Field. In addition, there are 3,800 metres of drill data from 2007 in the South-East Field that still requires modelling. Based on 2008 drill data, the coal potential is continuous along strike and at depth. Management is very encouraged by the results from the drilling completed in 2008 and believes that the data obtained will provide a basis for establishing additional resources.

Including the restated West Field resource estimate, the estimated combined resources for the South-East Field and the West Field of the Ovoot Tolgoi Project are shown in Table 3 below. The restated West Field resource estimate is based on data to June 20, 2008. The resource estimate for the South-East Field is based on data to December 31, 2006.

Table 3: Restated Ovoot Tolgoi West Field and South-East Field In-Place Surface Coal Resources Summary

Resource Area	ASTM Coal Rank	Resources at Ovoot Tolgoi		
		Measured (tonnes)	Indicated (tonnes)	Inferred (tonnes)
South-East Field	h v B to h v A	49,752,000	15,987,000	6,502,000
West Field	h v B to h v A	74,972,951	27,687,201	18,761,047
Total		168,399,152		25,263,047

The current mining plan and operations at Ovoot Tolgoi, which are based on an earlier estimate of the West Field coal resources as of December 31, 2006, are unaffected.

After obtaining its Permit to Mine on March 31, 2008, the Company started operations at Ovoot Tolgoi in April 2008. Coal shipments began in September 2008.

For the three month period ending March 31 2009, the total waste mined was 344,850 Bank Cubic Meters ("BCM") and the total coal mined was 157,115 tonnes at a strip ratio of approximately 2.19 BCM waste per tonne of saleable coal. Of the total coal mined, approximately 47,000 tonnes are oxidized steam coal and 110,000 tonnes are premium coal. Coal sales to December 31 2008 were approximately 113,000 tonnes. Coal sales in the first quarter were approximately 127,000 tonnes. The average selling price for existing premium coal contracts is approximately \$29 per tonne.

Due to erratic and unpredictable border openings, coal shipments in January and February 2009 were lower than expected. Consequently, and in order to preserve cash and manage stockpiles, a production curtailment program was initiated in January 2009 decreasing production to a dayshift basis. This was followed by a full mine shut down in late February 2009, except for coal loading of customer trucks from coal stockpiles.

The Company has been engaged in ongoing discussions with the Mongolian Government with the objective of establishing a border crossing at the Ceke border point that will be open for a full 24 hours per day, 365 days per year. This is expected to allow increasing daily distribution of Ovoot Tolgoi coal to customers in China. At present the border crossing operates on an eight hour per day basis. SouthGobi has purchased an automated 150 tonne scale which has been set up at the border to expedite coal traffic crossing the border into China from Ovoot Tolgoi.

The Company employed 227 employees for the Ovoot Tolgoi operation as at March 31, 2009. Of the 227 employees, 35, including expatriates, are employed in the Ulaanbaatar office, 4 in outlying smaller offices including the Ceke border point and 188 at the mine site. Of the 188 employees at the mine site, 105 employees are on a temporary layoff status due to the temporary production curtailment initiative at the mine site. The remaining 77 employees at the mine site are considered essential services but have had their hours of work and pay reduced beginning in March 2009. Laid off employees will be recalled on a systematic re-employment schedule to coincide with startup activities. Startup activities are currently being reviewed, but a planned startup date has not been confirmed.

In April 2008, the Company purchased a second fleet of coal mining equipment for the open pit mine, which is scheduled to be commissioned in September 2009. The new shovel / truck mining fleet consists of a Liebherr 996 hydraulic excavator (34 cubic m) and four Terex MT4400 (260-ton capacity) trucks. The new fleet will supplement the existing mine fleet consisting of a Liebherr 994 hydraulic excavator (13.5-cubic m capacity) and 7 Terex TR100 (100-ton capacity) trucks. The additional equipment will expand annual production capacity for the Ovoot Tolgoi mine to approximately 5.0 million tonnes in 2010.

Work on the new shop complex, mancamp and airstrip surfacing at Ovoot Tolgoi continued throughout the first quarter. The airstrip surfacing project was completed at year end and was certified in early 2009. The mancamp and shop building completion is scheduled by mid-2009.

The Ovoot Tolgoi mine is 45 km north of Mongolia's border with China. A Chinese steel mill has built a north / south railway line to the Ceke border point, where a major automated railcar loading facility opened in 2007. A new east / west railway is proposed to be completed by the end of 2009. In December 2008, the Company entered into preliminary discussions with major railway contractors on the development of a coal railway from the Ovoot Tolgoi mine to a point across the Chinese border. These discussions also contemplated a mine load out facility and a coal distribution centre in Ceke. The

Company intends to carry out further studies with respect to these proposed facilities during the first half of 2009.

Ovoot Tolgoi Underground Project

The Ovoot Tolgoi Underground Project is contiguous to and located directly below the surface mine development. The entire extension of the coal at depth from 300 to 700 m that is designated for the underground development is located inside the existing Ovoot Tolgoi mining license.

In March 2008, TAG prepared a resource estimate for underground resources in the West Field. Estimated underground resources for the West Field are approximately 3.9 million tonnes of measured resources, 12.6 million tonnes of indicated resources and 36.7 million tonnes of inferred resources. The coal rank is volatile B to A bituminous based on ASTM D388 standards. Holes drilled in the 2007 exploration program were not included in the resource estimation. Details of the assumptions and parameters used to calculate these coal resources and coal quality estimates are set out in the Technical Report entitled "Underground Resources at Ovoot Tolgoi – West Field" dated March 28, 2008 and available at www.sedar.com.

The 2008 exploration program concentrated on the underground located in the West Field. This drilling was conducted to obtain additional information respecting the structure and quality of the deep underground coal mineralization. The drilling conducted in 2006 and 2007 has identified coking and semi-soft coal at depths of between 250 m and 600 m below surface beneath the lower boundaries of the planned open pits at the South-East and West Fields. The 2008 program in the West Field has extended the depth of the potential mine to 700 m. The No. 5 coal seam continues to be open to depth and along strike. The results from the 2008 drilling program will be incorporated into an updated resource expected to be finished later in 2009.

Sumber Project

The Sumber Project is comprised of N, O and E Fields. This coal field starts 16 km east of Ovoot Tolgoi and stretches for approximately 18 km to the east. The N, O and E fields are covered by Mineral Exploration License #9443, which also encompasses part of the Ovoot Tolgoi project. N field is located approximately 16 km east of the Ovoot Tolgoi South-East pit and 8 km west of O Field. E Field is located approximately 10 km west of O Field.

In 2005, coal occurrences were identified in the N and O fields. N Field coal occurrences have been identified approximately 2 km north of the east-west trending Nariin Sukhait thrust fault, the major structural feature of the Ovoot Tolgoi region. Further exploration drilling in 2006 suggests that these coal occurrences may in fact be one coal field. The 2007 exploration drilling provided additional structure and quality information, where significant intersections were encountered and potential exists for expanding known mineralization along strike and down dip.

In June 2008, the Company announced that it intersected significant thicknesses in near-surface seams of high-quality coking and thermal coal, including one intercept of 51.5 m. The 2008 drilling program was completed during the fourth quarter of 2008 and the results are expected to provide the basis for a resource estimate in 2009. The company has initiated mine planning and an application for a mining license, which will be submitted for development of this project.

Tsagaan Tolgoi Project

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

A coal delineation program was first carried out in 2004, but no further work was conducted in 2005. Exploration programs were carried out during 2006 and 2007 to provide the basis for a resource estimate. A resource estimate prepared by Norwest in February 2008, estimated 23.4 million tonnes of measured resources, 13.0 million tonnes of indicated resources and 9.0 million tonnes of inferred resources. The coal is of volatile bituminous B to C in rank based on ASTM D 388 standards and is suitable for use as a thermal coal. The resources appear to be amenable to surface extraction down to a planned depth of 150 m. Details of the assumptions and parameters used to calculate these coal resources and coal quality estimates are set out in the Technical Report entitled "Coal Geology and Resources – Tsagaan Tolgoi Property" dated March 25, 2008 and available at www.sedar.com.

The Company has initiated an application for a mining license for the Tsagaan Tolgoi coal field. Any development of the field would be expected to occur only if Tsagaan Tolgoi were to be selected as a supplier of thermal coal for a power plant to be constructed to support Ivanhoe's Oyu Tolgoi copper and gold project. The timing of the continued development of the Oyu Tolgoi project is contingent upon a number of factors beyond the control of the Company and Ivanhoe, including the approval by the government of Mongolia of an investment agreement.

Tavan Tolgoi Extension Project

The Tavan Tolgoi Extension Project is composed of seven exploration licenses located east of Dalanzadgad, the provincial capital in the Omnogovi Aimag. The Company also holds an option to acquire three additional exploration licenses from Ivanhoe covering areas in the vicinity.

These exploration licenses surround the third party-owned Tavan Tolgoi coal project. The Tavan Tolgoi coalfield was discovered in the 1950s by a joint Mongolian/Soviet team and is believed to be one of the largest undeveloped metallurgical coal deposits in the world.

A field reconnaissance program was carried out on the Tavan Tolgoi Extension licenses in 2006. The exploration area has been surveyed for copper and gold exploration using BHP Falcon aerial geophysics. The Company has obtained the aeromagnetic and aero gravity survey data and is using the results of the upcoming analysis of the Falcon data to help delineate potential coal targets. A significant exploration program was started in the third and fourth quarters of 2007, and the results are being used to delineate further potential coal targets. Exploration work on the extension continued in 2008 and is currently being updated.

Properties in Indonesia

Mamahak Coal Project

SouthGobi has commenced the development of green fields' surface coal deposits in four concessions covering 22,968 ha in East Kalimantan, Indonesia, through its participation in the Mamahak coal project.

The Company holds its interest in the Mamahak coal project through a joint venture. In September 2008, the Company increased its working interest in the original joint venture from 56% to 85%. Under the terms of the Joint Venture Earn-In Agreement ("JVA"), the Company has the right to increase its working interest position based on a predetermined pricing mechanism. The terms of the JVA allow the Company to increase its working interest to 100% in the project.

The Company has contracted a local consultant to assist in the field programs, and site investigation indicates the potential for continuous coal structures over a large area. Geological mapping delineated encouraging coal outcrops with over thirty coal seams being identified to date.

The Company has also contracted the Jakarta office of Australian based SMG to assist in the field programs. All drill holes are being geophysically logged with detailed intersection data delivered to the SMG office in Jakarta for the preparation of a geological model to be used for mine planning.

The 2008 drilling program identified quantities of high fluidity coking coal that appear to be amenable to surface mining. At the end of 2008, 220 drill holes had been completed on the SW and E resource blocks on the MCM concession. The SW and E blocks cover approximately 638 hectares of the MCM concession. Further drilling is ongoing. The intent of the drilling program is to determine down-dip continuity, thickness variations, coal quality and structure. Reconnaissance and initial field mapping has been initiated over the larger concession areas.

The drilling results received to date support the quality data from the initial field outcrop test results. In November 2008, the company received independent laboratory analysis of a recent bulk sample that confirms high volatile, high-fluidity coking coal at the project. The bulk sample was taken on the SW resource block within the MCM concession and was comprised of proportioned blending of several coal seams from an area where the Company plans to commence mining in 2009. The proximate analysis and related testing of the bulk sample raw coal was carried out by PT Geoservices Ltd. of Jakarta, Indonesia.

In February 2009, SMG prepared a resource estimate for then E and SW resource blocks. SMG has estimated that the E resource block on the MCM concession contains 5.0 million tonnes of measured resources, 7.3 million tonnes of indicated resources and 2.7 million tonnes of inferred resources, while the SW resource block contains 2.6 million tonnes of inferred resources. The resource estimates have been calculated to Joint Ore Reserves Committee ("JORC") Standards. The resource quantities estimated pursuant to JORC Standards are equivalent to the resource quantities that would have been estimated using the CIM Definition Standards on Mineral Resources and Reserves mandated by National Instrument 43-101. Details of the assumptions and parameters used to calculate these coal resources and coal quality estimates are set out in the Technical Report entitled "Mamahak Coal Project" dated March 26, 2009 and available at www.sedar.com.

Required permit applications for mining, coal transportation and a barge load-out facility for the area have been filed. In December 2008 a permit was issued, which will allow the Company to commence

surface coal mining at the SW deposit on the MCM concession. A site office, accommodation camp and a satellite communication system are being mobilized for the project. An administrative project office has been established at the port village of Melak on the Mahakam River approximately 90 km from the site. Construction activity continued through year end at the project site and is focused on the completion of a 30 km haul road from the SW deposit to the barge port on the Mahakam River. Construction is in progress on the installation of a river barge loading terminal which will be located at Long Habung on the Mahakam River. The Company is planning to ship test cargoes from the Mamahak coal project to potential customers during 2009.

The Indonesian central Government announced a new law on mineral and coal mining, known as Minerba, at the end of 2008, which was signed by the President of the Republic of Indonesia on January 12, 2009. The Company is currently reviewing the details, but the new law seeks to clarify the issues on the role of government in the mining license process; the introduction of two new types of mining concessions; changes regarding related parties and mining services agreements; a transition period for the current Contract of Work system and a change that allows direct ownership of mining concessions by foreign companies. Much of the detail surrounding the development and application of the new rules under Minerba is not yet clear and is to be provided for in a series of Government implementing regulations. The Indonesian Government is required to issue the implementing regulations under Minerba before January 12, 2010.

Metals Division Profile and Discontinued Operations

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

The Company also received a 1% net returns royalty in certain mineral projects in Indonesia, and retained the rights to the Kharmagtai and Chandman Uul properties in Mongolia.

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

SELECTED QUARTERLY DATA

(\$ in thousands, except per share information)

	2009	2008				2007		
QUARTER ENDED	31-Mar	31-Dec	30-Sep	30-Jun	31-Mar	31-Dec	30-Sep	30-Jun
Revenue	\$ 3,540	\$ 3,126	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Exploration expenses	4,130	8,104	11,361	10,364	6,374	5,992	5,274	18,306
Loss from continuing operations	9,960	14,457	21,110	11,189	14,909	42,500	10,836	53,212
Loss from discontinued operations	-	2,549	1,667	2,392	1,302	-	-	-
Net loss	9,960	17,006	22,777	13,581	16,211	42,500	10,836	53,212
Net loss per share	(0.07)	(0.13)	(0.17)	(0.10)	(0.19)	(0.57)	(0.15)	(1.43)

Selected Quarterly Information

The changes in comparative results of operations on a quarter over quarter basis are due primarily to significant fluctuations in the following areas: exploration expenses, stock-based compensation charges, foreign exchange gains and losses, interest expense, interest accretion on line of credit facility and fair value of embedded derivative on debt. These latter two items are described in note 3 and 20 to the Consolidated Interim Financial Statements.

Revenue from coal sales, which began at the end of September 2008, increased during the quarter ended December 31, 2008. For the 3 months ended March 31, 2009 lower than expected revenue from coal sales were impacted by the border crossing. Exploration expenses will vary from quarter to quarter depending on the number of projects and the related seasonality of the exploration programs. Exploration costs for the Metals Division are classified as a loss from discontinued operations and were incurred for exploration projects in Mongolia and Indonesia. Coal expenditures in Mongolia were initially incurred during the quarter ended June 30, 2007. Expenditures on the Indonesian Coal Division began in the first quarter of 2008.

RESULTS OF OPERATIONS

	Three Months Ended		
	March 31, 2009	December 31, 2008	March 31, 2008
Volumes, Prices and Costs			
Coal production (<i>millions of tonnes</i>)	0.16	1.16	-
Coal sales (<i>millions of tonnes</i>)	0.13	0.11	-
Average sales price (<i>per tonne</i>)	\$ 29.26	\$ 29.20	-
Total cash costs of product sold (<i>per tonne</i>)	\$ 18.51	\$ 14.09	-
Direct cash costs of product sold (<i>per tonne</i>)	\$ 14.29	\$ 8.30	-
Operating Statistics			
Total waste material moved (<i>millions of bank cubic metres</i>)	0.34	2.54	-
Strip ratio (<i>bank cubic metres of waste rock per tonne of clean coal produced</i>)	2.19	2.19	-
Operating Results (<i>thousands of dollars</i>)			
Revenue	\$ 3,540	\$ 3,126	\$ -
Cost of Sales	(3,213)	(2,178)	-
Income from mine operations	327	948	-
Administration expenses	(6,105)	(7,473)	(1,106)
Evaluation and exploration expenses	(4,130)	(8,104)	(6,375)
Operating loss from continuing operations	\$ (9,908)	\$ (14,629)	\$ (7,481)

The Company incurred an operating loss from continuing operations for the three months ended March 31, 2009 of \$9.9 million compared to \$7.5 million for the same period in 2008. This change is due to the factors discussed below.

Revenue, net of royalty expense and cost of sales relates to the Company's operations in Mongolia. The Company commenced initial deliveries of coal in late September 2008, with shipments continuing throughout the fourth quarter 2008 and the first quarter 2009.

In the first quarter of 2009, the Company shipped approximately 127,000 tonnes of coal at an average realized selling price of approximately \$29 per tonne. This compares to 113,000 tonnes of coal shipped in the fourth quarter 2008 at the same approximate average realized selling price.

Shipments in the quarter were affected by the erratic and unpredictable border openings. Coal shipments in January and February 2009 were lower than expected. Consequently, and in order to manage costs and stockpiles, a production curtailment program was initiated in January 2009 decreasing production to a dayshift basis. This was followed by a full mine shut down on February 24, 2009, except for coal loading of customer trucks from coal stockpiles.

The Company incurred cost of sales of \$3.2 million in the current quarter, which comprise the cost of the product sold, mine administration costs, equipment depreciation, and depletion of stripping costs. Total cash costs per tonne of product sold in the fourth quarter of 2008 were \$14.09 compared to \$18.51 for the first quarter of 2009. The increase is due primarily to operational costs of approximately \$4.00 per tonne that were expensed in the quarter due to the full mine shut down at the end of February 2009.

Exploration expenses for the three months ended March 31, 2009 were lower than the quarter ended March 31, 2008. Exploration expenditures in Mongolia were incurred in the first quarter of 2008 as the Coal Division assembled equipment, hired additional personnel and began pre-development activities at the Ovoot Tolgoi mine site. Throughout 2008 the exploration program concentrated on drilling in the West Field. The Coal Division continued its exploration activities in Indonesia throughout the first quarter 2009.

Administration expenses for the quarter ended March 31, 2009 were \$6.1 million compared to \$1.1 million for the quarter ended March 31, 2008. Administration expenses for the quarter ended March 31, 2009 include approximately \$3.3 million of stock based compensation compared to approximately \$583,000 for the same period last year. Other amounts that are included in the quarter ended March 31, 2009 that are not comparable to the 2008 quarter are listing fees of approximately \$235,000, a corporate consulting cost of \$500,000 and a foreign exchange loss of approximately \$843,000 compared to a foreign exchange gain of approximately \$462,000 for the quarter ended March 31, 2008.

Administration expenses for the quarter ended December 31, 2008 included approximately \$3.8 million of foreign exchange losses, \$835,000 of listing fees and \$1.5 million of stock based compensation.

The administration expenses consist of the following major categories broken down for comparative purposes.

Legal fees decreased for the quarter ended March 31, 2009 compared to the same period in 2008. The majority of these charges were for costs associated with the Company's regulatory affairs including expenses associated with corporate governance, filing, registration and disclosure.

Corporate administration fees increased in the three months ended March 31, 2009 compared to the same period in 2008. The increases relate to added personnel and office and administration support costs, insurance, travel and filing fees. Certain of the Company's administrative staff and office facilities are provided by Global Mining Management Ltd ("GMM") (see 'Related Party Transactions' below) on a cost recovery basis. Accordingly, quarterly fluctuations in the costs of administrative and personnel costs can be expected commensurate with increases or decreases in quarterly corporate activity and the level of personnel employed.

Professional fees have increased for the three months ended March 31, 2009 as compared to the same period in 2008. Quarterly charges include the cost of quarterly reviews, internal computer systems training and planning, and accruals for the year end audit of the Company's financial statements. The current quarter increase relates predominantly to a corporate consulting contract cost of \$500,000 for our Mongolian operations.

Salaries and benefits, excluding stock based compensation costs, increased in the three months ended March 31, 2009 to \$422,000 as compared to \$293,000 for the three months ended March 31, 2008. Salary and benefits compared to the same period in 2008 have increased due to the increased corporate activities related to the Coal Division.

The foreign exchange losses/ (gains) are primarily the result of changes of the U.S. to Canadian dollar and the U.S to Mongolian Tugrik exchange rates during the period.

Listing fees consist of legal, accounting and professional fees. The Company had planned to treat the charges as share issue costs upon a successful equity fundraising for a secondary listing on an Asian

stock exchange. However, current liquidity issues in the credit markets, along with the increased cost of obtaining capital and the reduced availability of equity funding have led to a decision to expense these costs. In the first quarter of 2008 the Company had capitalized the listing fees. The Company is continuing with the secondary listing application.

EXPLORATION COSTS AND DISCONTINUED OPERATIONS BY DIVISION

(\$ in thousands)

	Three Months Ended	
	March 31,	
	2009	2008
Mongolian Coal Division	\$ 768	\$ 3,893
Indonesian Coal Division	3,362	2,482
Total Exploration	<u>\$ 4,130</u>	<u>\$ 6,375</u>

Coal Division

The total coal exploration expenditures in the three months ended March 31, 2009 were \$4.1 million compared to \$6.4 million for the same period in 2008.

Exploration costs are charged to operations until such time as it has been determined that a property has economically recoverable reserves, in which case the costs incurred to develop a property are capitalized.

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

The Mongolian Coal Division started exploration and development subsequent to the completion of the coal transaction at the end of May 2007. Expenditures in the first quarter 2008 were incurred as the Coal Division assembled equipment, hired additional personnel and began pre-development activities at the Ovoot Tolgoi mine site. Pre-development of the Ovoot Tolgoi open pit mine site included road construction, site clearing, drainage control and topsoil removal. The exploration expenditures also included consulting-geological, drilling, license fees, office and salary and benefits.

Exploration expenditures in Mongolia were approximately \$768,000 for the three months ended March 31, 2009 and included consulting-geological, drilling, license fees, office and salary and benefits. Exploration expenditures will vary from quarter to quarter and are also related to the seasonality of the exploration programs.

The exploration programs in 2009 will continue to expand the extent of the known mineralization in both the underground and surface coal deposits as well as increase the knowledge level of the quality and structure of the deposit.

In Indonesia, exploration expenditures were \$3.4 million for the three months ended March 31, 2009. The Company began its exploration activities in Indonesia in early 2008. The drilling results received to date support the quality data from the initial field outcrop test results. The 2008 drilling program identified quantities of coking coal that appear to be amenable to surface mining. To date, the Company

has incurred expenditures to carry out geological reconnaissance, licensing, mapping, initial drilling, and a documentation program on the new concessions in East Kalimantan.

In January 2009, a permit was issued which will allow the Company to commence surface coal mining at the SW deposit on the MCM concession.

Metals Division – Discontinued Operations

The Company sold the Metals Division to Ivanhoe in December 2008. The Metals Division consists of a series of base and precious metal exploration properties in Mongolia and Indonesia. In 2008, the proceeds of \$3 million were classified as a deposit received for the sale of the division. The gain on sale of the Metals Division is \$2.6 million and is classified in the consolidated statement of changes in equity.

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

During the three months ended March 31, 2008, exploration expenses were \$1.3 million and the majority of the expenses incurred in Mongolia and Indonesia were related to ongoing license fees, drilling, and salaries.

The exploration expenditures of \$1.3 million have been classified as a loss from discontinued operations. The basic and diluted loss per share from discontinued operations is \$0.02 for 2008.

OTHER INCOME/(EXPENSE)

(\$ in thousands)

	Three Months Ended	
	March 31,	
	2009	2008
Fair value change on embedded derivative	\$ -	\$ (7,223)
Interest accretion on line of credit facilities	-	(598)
Interest expense	(53)	(134)
Accretion expense	(9)	
Interest income	9	528
	\$ (52)	\$ (7,427)

On April 26, 2006, in conjunction with the coal transaction, the Company entered into a line of credit facility (the “First Funding Agreement”) with Ivanhoe whereby Ivanhoe agreed to make available to the Company an unsecured line of credit of up to \$10 million which was extended to a maximum of \$15 million on June 6, 2007. Attached to the First Funding Agreement was a conversion option which became effective upon the completion of the coal transaction. On January 23, 2008, concurrent with the closing of equity private placements and at the Company’s request, Ivanhoe converted the then principal balance of \$29,982,631 into 14,709,701 common shares of the Company. As a result of this conversion the amount due under the line of credit facility was eliminated.

Under IFRS, the conversion feature is considered an embedded derivative liability that must be recorded at its fair value upon initial measurement and revalued at each subsequent reporting period. The difference between the debt host component and the principal amount of the loan outstanding is accreted to income over the remaining term of the debt. (Please refer to Note 20.4 of the Consolidated Interim Financial Statements for further details).

Interest expense was higher in 2008 compared to the same period in 2009. This is related to advances on the line of credit to fund operations. In January 2008, with the completion of the additional equity private placements, the First Funding Agreement line of credit facility and the Second Funding Agreement were terminated.

In 2009, as part of the sale of the Metals Division, the Company obtained a \$30 million working capital credit facility from Ivanhoe. The credit facility is for a one year term with a one year discretionary extension. The credit facility is unsecured and carries an interest rate equal to LIBOR plus 750 basis points. The Company has received advances of \$8 million against the line of credit facility in the first quarter 2009.

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

Interest income was higher in 2008, which relates to the completion of the equity financings in early 2008. Lower interest income during the 2009 period reflects lower average cash balances during this period.

LIQUIDITY AND CAPITAL RESOURCES

Cash Flow Highlights

(\$ in thousands)

	Three Months Ended	
	March	March
	2009	2008
	<u> </u>	<u> </u>
Cash used in operating activities	\$ (9,414)	\$ (11,365)
Cash used in investing activities	(5,536)	(12,770)
Cash generated by financing activities	8,222	107,567
Effect of foreign exchange rate changes on cash	16	492
Cash balance, beginning of year	10,117	1,394
<u>(Decrease) increase in cash for the year</u>	<u>(6,712)</u>	<u>83,924</u>
<u>Cash balance, end of year</u>	<u>3,405</u>	<u>85,318</u>

General market conditions

Current problems in the credit markets and deteriorating global economic conditions have led to a general weakening of commodity prices. Volatility has been unusually high and it is difficult to forecast the price of and related demand for our coal products. Credit market conditions have also increased the cost of obtaining capital and limited availability of funds. Limited access to the Ceke border crossing have impacted our 2009 production levels and coal deliveries. Accordingly, management is reviewing the effects of the current conditions on our business plans for the upcoming year.

Cash used in operating activities

At March 31, 2009 the Company had cash resources of \$3.4 million compared to cash resources of \$10.1 million at December 31, 2008.

Cash used in continuing operations was \$9.4 million for the three months ended March 31, 2009 compared to \$10.9 million for the three months ended March 31, 2008. Cash used in discontinued operations was \$510,000 for the three months ended March 31, 2008. The Metals Division was sold in December 2008, which will not affect discontinued operations disclosure for periods ending in 2009.

The Company incurred a net loss from continuing operations of \$10.0 million for the three months ended March 31, 2009 compared to a \$14.9 million loss for the same period in 2008. Continuation of the Company's build out of the Ovoot Tolgoi mining operation, higher finance costs and evaluation and exploration costs contributed to the higher losses in 2008. With the increased activities at the Ovoot Tolgoi site and the operations in Mongolia, accounts receivable, prepaids, inventory and accounts payable increased during the three months ended March 31, 2009 and 2008.

In 2008, foreign exchange gains are primarily reflective of the larger US and Canadian cash balances due to the completion of the private equity placements and the related changes in the value of the Canadian dollar versus its US counterpart. The foreign exchange loss, in 2009, is primarily reflective of the change in the value of the Mongolian Tugrik versus the US dollar.

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

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

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

Coal and supplies inventory have increased to \$15.5 million in the current quarter from \$13.7 million at the year ended December 31, 2008. Coal and supplies inventory is valued at the lower of cost and net realizable value. Coal inventory cost of \$15.2 million includes direct and indirect labour, operating materials and supplies, transportation costs and an appropriate portion of fixed and variable overhead

expenses, including depreciation and depletion. Supplies inventory consists of consumable parts and supplies.

The Company had a stockpile of approximately 1.1 million tonnes of coal inventory at March 31, 2009.

Accounts payable have decreased in the current quarter but were higher in 2008 due to the additional coal exploration, administrative and mining activity.

Cash used for investing activities

Cash used for investing activities was \$5.5 million for the three months ended March 31, 2009 and \$12.8 million for the three months ended March 31, 2008.

The Company's investment in plant and equipment was higher during the quarter ended March 31, 2008. The coal mining equipment that was purchased in November 2007 was commissioned for use at Ovoot Tolgoi in March 2008. Deposits for further mining equipment and maintenance facilities are included as plant and equipment. The Company incurred expenditures during the three months ended March 31, 2009 for tires, mobile and mining equipment.

Interest income will increase or decrease in a quarter depending on the cash position. Interest was higher for the three months ended March 31, 2008, which related directly to the completion of the equity financings.

Cash provided by financing activities

During the quarter ended March 31, 2008, the Company completed a series of equity financing transactions and received proceeds from the exercise of stock options. The total proceeds net of issue costs were \$113.6 million for the three months ended March 31, 2008, compared to proceeds received for the exercise of stock options of \$222,000 for the three months ended March 31, 2009.

The proceeds from the equity financings in 2008 have been used for the initial development of the open-pit coal mine at the Company's Ovoot Tolgoi project, and for additional drilling and engineering focused on the Ovoot Tolgoi site and development of the Indonesia coal project. Proceeds have also been used for investigating new projects, equipment expenditures and for general corporate and administrative purposes.

On December 31, 2008 the Company announced the sale of its Metals Division to Ivanhoe for \$3 million and other non-cash consideration. As part of the sale transaction, the Company obtained a \$30 million credit facility from Ivanhoe. The credit facility is for a one year term with a one year discretionary extension. The credit facility is unsecured and carries an interest rate equal to LIBOR plus 750 basis points. For the quarter ended March 31, 2009, the Company received advances of \$8 million against the line of credit facility.

In October 2007, the Company entered into a second funding agreement with Ivanhoe. Amounts advanced under this line of credit facility were repaid from proceeds of the equity financings in January 2008.

Liquidity, Financing and Working Capital Resources

The Company is an integrated coal exploration, development and production company. The Company's ability to continue as a going concern is dependent upon establishing profitable operations, the confirmation of economically recoverable reserves, and the ability of the Company to obtain further financing to develop properties.

The Company has been reviewing its detailed revenue and expenditure plans, both discretionary and non-discretionary, for 2009 and has identified the need for further financing to enhance its working capital resources. The Company is prioritizing its budgeted expenditures with a current emphasis on production and near term cash flow.

As part of the sale of the Metals Division to Ivanhoe in December 2008, the Company obtained a \$30 million credit facility from Ivanhoe. The credit facility is for a one year term with a one year discretionary extension. The credit facility is unsecured and carries an interest rate equal to LIBOR plus 750 basis points.

The Company will be incurring expenditures for the exploration, development, and production of its current coal assets, and to the extent that available financial resources permit, will incur expenditures for the acquisition of further coal assets. Revenue from current operations will not be sufficient to meet current expenditure levels.

Cash generated from operations may increase in 2009, but it may not be sufficient to meet all expenditure levels. Management believes that additional debt or equity financing, beyond the current credit facility with Ivanhoe, is available but no additional source of funding has yet been identified. The Company will be reviewing all discretionary and non-discretionary spending, which will include a review of future project costs and capital commitments.

RELATED PARTY TRANSACTIONS

The Company is a party to a shareholders' cost-sharing agreement with certain other public and private companies, including Ivanhoe (the "Other Companies") pursuant to which the Company and the Other Companies are equal shareholders in GMM and, through GMM, share office space, furnishings and equipment and communications facilities (on a cost recovery basis) and the employment, on a part-time basis, of various administrative, office and management personnel in Vancouver, British Columbia. Costs of the shared office facilities and the shared part-time employees are recovered from the Company proportionate to the time spent by the shared part-time employees on matters pertaining to the Company. Certain of the directors and officers of the Company are also officers and directors of GMM. The Company has utilized the services of the GMM staff and office since September 1, 2003 and has incurred costs of \$408,000 and \$516,000 for the quarters ended March 31, 2009 and 2008, respectively.

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

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 April 23, 2009: 133,333,282 common shares were issued and outstanding and 7,004,385 share purchase options were outstanding. On a diluted basis, 140,337,667 common shares were outstanding. There are no preferred shares outstanding.

Ivanhoe, directly and indirectly, currently owns 106,804,155 common shares representing approximately 80% of the issued and outstanding common shares of SouthGobi.

INTERNAL CONTROLS OVER FINANCIAL REPORTING

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

RISK FACTORS

The business of mineral exploration and extraction involves a high degree of risk. Few properties that are explored are ultimately developed into production.

Material risks and uncertainties affecting SouthGobi, their potential impact and the Company's principal risk management strategies are substantially unchanged from those disclosed in the Company's MD&A for the year ended December 31, 2008, which is available at www.sedar.com.

OUTLOOK

The commodity price environment generally worsened with the slower global macroeconomic environment expected for 2009. Although the full impact of the current economic volatility on coal prices remains uncertain, we are encouraged by long-term fundamentals for the Company's core commodity.

Coal remains a prime low cost energy source, and countries such as India and China account for a large percentage of the world's coal demand. As developing nations expand their urban and industrial infrastructure, we believe that demand for commodities will increase as the current economic crisis passes.

The Company's principal assets in Mongolia and Indonesia are both well located in close proximity to China and other major industrializing economies in Asia. Furthermore, our near-term production is in high quality bituminous thermal and coking coals, which we anticipate will remain attractive premium products.

Mongolia

The Company commenced initial deliveries of coal in late September 2008, which continued through the fourth quarter, with revenue at \$3.5 million for the three months ended March 31 2009 and approximately 127,000 tonnes shipped.

The Company has been engaged in ongoing discussions with the Mongolian Government with the objective of establishing a border crossing at the Ceke border point that will be open for a full 24 hours per day, 365 days per year. This is expected to increase daily distribution of Ovoot Tolgoi coal to our customers in China. In March 2009 the border started opening more reliably for seven days per week on an eight hour dayshift basis. Continuation of this situation will likely enable SouthGobi to resume mining operations at Ovoot Tolgoi in the near term.

In February 2009, the Company concluded an additional sales contract with a Mongolian company for 500,000 tonnes of premium and standard thermal coal. Existing Chinese customers are in advanced discussions with SouthGobi at present for new sales contracts to provide additional coal. The Company has also identified a number of potential new customers in Western Inner Mongolia and other parts of China. These potential new customers include end users, distributors, steel mills, power plants and industrial consumers.

SouthGobi has appointed the major international engineering firm, Norwest, to complete a new technical report for the Ovoot Tolgoi project incorporating data obtained from drilling to the end of 2008. The Company believes the new report, which is expected to be completed later in 2009, will more fully demonstrate the potential of the Ovoot Tolgoi coal deposit.

For 2009, the Company anticipates it could produce up to 2.5 million tonnes of coal from its Ovoot Tolgoi operations. However, the achievement of this target may be adversely impacted if the Ceke border crossing issues are not resolved on a long term basis. Based on our ongoing and positive discussions with the Mongolian Government, the Company believes implementation of a "24/7" border designation for Ceke could happen this year.

Indonesia

In January 2009 a permit was issued, which will allow the Company to commence surface coal mining at the SW resource block on the MCM concession.

In March 2009, the Company reported resource estimates for the E and SW resource blocks. The E resource block on the MCM concession contains 5.0 million tonnes of measured resources, 7.3 million tonnes of indicated resources and 2.7 million tonnes of inferred resources, while the SW resource block contains 2.6 million tonnes of inferred resources. Details of the assumptions and parameters used to calculate these coal resources and coal quality estimates are set out in the Technical Report entitled "Mamahak Coal Project" dated March 26, 2009 and available at www.sedar.com.

Testing of coal from the MCM concession suggests the coal is of a premium character and has some unique characteristics suitable in coking processes. In particular, the coal has high fluidity.

The Company expects to continue an integrated advanced stage exploration and development program on its Indonesian projects. While further drilling is ongoing, work to date on the MCM concession supports our objective to develop an open-pit mining operation. SouthGobi is planning to ship test cargoes from the Mamahak coal project to potential customers during 2009.

Management is currently working with potential customers and anticipates contracts may be completed in the second quarter of 2009. The Company will outsource the mining services and is currently establishing a capped mining rate contract for these services. Near term development of the MCM concession, however, will depend on demand and economical pricing for its products.

Overview and Objectives

As we look back to 2008, our accomplishments included obtaining the Ovoot Tolgoi mining license, developing the Ovoot Tolgoi mine site infrastructure, establishing ourselves as a coal producer, building our production capacity and developing our principal projects in Mongolia and Indonesia.

Our objectives for 2009 are to:

- (i) Continue evolving into a fully-fledged producer through the advancement of our key projects and, in particular, through expanded sales and production at Ovoot Tolgoi and commencement of trial shipments at Mamahak;
- (ii) Utilize our institutional knowledge of our properties in Mongolia and Indonesia to deliver continued exploration success with the aim of substantially increasing the Company's coal resource base;
- (iii) Maximize the market pricing of our coal through further development of relationships with customers that recognize the value of its premium specification; and
- (iv) Remain focused on efficiency and prudent financial management.

With the slowdown of the global economy and deteriorating global market conditions there has been a weakening of commodity prices. However, for the long term the Company believes that the fundamentals remain strong for coal.

May 1, 2009