SouthGobi Energy Resources Ltd.

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

September 30, 2009

(Stated in U.S. dollars)

SOUTHGOBI ENERGY RESOURCES LTD

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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 mining, development and exploration 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 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 to Ivanhoe as of December 30, 2008, the Company's principal focus is on mining, developing and exploring of coking and thermal coals in Mongolia's South Gobi Province.

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

In addition, the Company owns the Tsagaan Tolgoi Deposit in Mongolia and holds and 85% interest in the Mamahak Deposit in Indonesia.

Recent Developments

Ovoot Tolgoi Complex

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

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

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

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

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

On October 12, 2009, the Company announced that it completed a prefeasibility study for the Ovoot Tolgoi Mine resulting in the identification of Proven and Probable Mineral Reserves. The independent estimate prepared by Norwest Corporation ("Norwest") calculated 114.1 million tonnes of Proven and Probable surface coal reserves at July 1, 2009.

Surface Mineable Reserves as of July 1, 2009

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

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

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

The Company also announced that it had received an updated independent NI 43-101 compliant resource estimate for the Ovoot Tolgoi Complex, prepared by Norwest.

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

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

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

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

Soumber Deposit

On October 12, 2009, the Company reported that it had received an initial independent NI 43-101 compliant resource estimate for the Soumber coal project, prepared by Norwest.

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

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

*medium-volatile bituminous coal based on ASTM D388 standards

Mamahak Deposit

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

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

In October 2009, SMG Consultants ("SMG") updated a resource estimate as at September 11, 2009 for the E and SW resource blocks. SMG has estimated that the resource blocks on the Mamahak Deposit contain 6.9 million tonnes of measured resources, 3.2 million tonnes of indicated resources and 161,000 tonnes of inferred resources. The resource estimates have been calculated to Joint Ore Reserves Committee ("JORC") standards. The JORC resource quantities 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 Resource Report entitled, "Mamahak Coal Project" dated October 12, 2009 and available at www.sedar.com.

As the Company progressed with efforts to prepare for the mining and shipment of the targeted 30,000 tonne trial cargo from Mamahak, the Company became aware of the requirement for additional capital expenditure beyond what was originally budgeted to develop the project. After the initial review of the project expenditures and related budgets, the Company suspended further development works at Mamahak pending a detailed operational review and analysis.

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

Jess Harding has been appointed the Company's Vice-President, Evaluations and Project Development. Mr. Harding has more than 15 years' experience in the mining industry and assumes the same role that he presently holds at Ivanhoe 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 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 estimation of open pit and underground coal resources and will be assuming the role of Qualified Person to oversee future independent resource estimates for SouthGobi.

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

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

In July 2009, the Company announced the resignation of Gene Wusaty as the Company's Chief Operating Officer.

In July 2009, the Company and Ivanhoe agreed to increase an existing working capital credit facility from $30 million to $60 million. The amended credit facility will mature on December 31, 2010, is unsecured and bears interest at LIBOR plus 750 basis points. The amended facility also requires repayment in the event that the Company acquires additional financing from a third party source and provides for an extension fee of $1.5 million payable in the event any portion of the facility is outstanding past March 31, 2010. This additional $30 million working capital facility allowed the Company to continue to fund its expansion plans and current operations in Mongolia and its operations in Indonesia.

Effective September 1, 2009, Denis Lehoux, SouthGobi Sands LLC's ("SGS"), in country Operations Director in Mongolia retired. David Bartel, who has been with SGS since January 2007, has been appointed Operations and Executive Director and Vice President. Mr. Bartel has over 30 years of experience in the coal industry and will be the key representative for the Company in Mongolia.

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

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

On October 26th, 2009, the Company announced financing had been secured from a wholly-owned subsidiary of China Investment Corporation ("CIC"), which will provide $500 million in the form of a secured, convertible debenture bearing interest at 8.0% (Please see the Liquidity, Financing and Working Capital Resources section for more details).

Ivanhoe, directly and indirectly, currently owns 105,782,155 common shares representing approximately 79% of the issued and outstanding common shares of SouthGobi.

FORWARD LOOKING STATEMENTS

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

INTERNATIONAL FINANCIAL REPORTING STANDARDS (IFRS)

Transition to IFRS from GAAP

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

As previously disclosed, the Company 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 Consolidated Interim 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 IFRS requires the Company to establish accounting policies and to make estimates that affect both the amount and timing of the recording of assets, liabilities, revenues and expenses.

A detailed summary of all of the Company's significant accounting policies is included in Note 4 to the Consolidated Interim Financial Statements for the three and nine months ended September 30, 2009. Note 3 to the Consolidated Interim Financial Statements for the three and nine months ended September 30, 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 property, plant and equipment ("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 the end of each reporting period, 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 provision for statutory, contractual, constructive or legal obligations, including those associated with the reclamation of mineral properties and mineral assets under PPE, when those obligations result from the acquisition, construction, development or normal operation of the assets. Initially, a provision for an asset retirement obligation is recognized as its present value in the period in which it is incurred. Upon initial recognition of the liability, the corresponding asset retirement obligation is added to the carrying amount of the related asset and the cost is amortized as an expense over the economic life of the asset using either the unit-of-production method or the straight-line method, as appropriate. Following the initial recognition of the asset retirement obligation, the carrying amount of the liability is increased for the passage of time and adjusted for changes to the current market-based discount rate, amount or timing of the underlying cash flows needed to settle the obligation.

Inventory valuation

Coal inventories are stated at lower of production cost and net realizable value. Production costs include direct and indirect 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.

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

Stripping costs

Stripping costs incurred during the development of a mine are capitalized into PPE. Stripping costs incurred during the 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.

Income taxes

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

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

Stock-based compensation

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

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

Revenue recognition

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

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 the nine months ended September 30, 2009.

NON-IFRS FINANCIAL MEASURES

($ in thousands, unless otherwise stated)

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

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

Prior year comparatives are not provided as the Company did not have sales in the nine months ended September 30, 2008.

	Three Months Ended		Nine Months Ended
	September 30, 2009	June 30, 2009	**September 30, 2009**
Cash costs, continuing operations			
Cost of sales per financial statements	**$ 8,637**	$ 9,139	**$ 20,989**
Less non-cash adjustments	**(2,510)**	(2,171)	**(5,536)**
Total cash costs	**6,127**	6,968	**15,453**
Coal sales *(tonnes)*	**456,819**	384,305	**968,490**
Total cash costs of product sold *(per tonne)*	**$ 13.41**	$ 18.13	**$ 15.96**

	Three Months Ended		Nine Months Ended
	September 30, 2009	June 30 2009	**September 30, 2009**
Cash costs, continuing operations			
Direct cash costs of product sold *(per tonne)*	**$ 11.16**	$ 16.64	**$ 13.75**
Mine administration cash costs of product sold *(per tonne)*	**2.25**	1.49	**2.21**
Total cash costs of product sold *(per tonne)*	**$ 13.41**	$ 18.13	**$ 15.96**

MINERAL PROPERTIES

Qualified Persons

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

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

Coal Group Profile

Mongolia Exploration Licenses

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

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

As at October 23, 2009 the Company held 23 licenses, including the two mining licenses, which in total cover an area of approximately 859,000 ha.

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

Properties in Mongolia

Ovoot Tolgoi Mine

The Ovoot Tolgoi mine is located in the southwest corner of the Omnogovi Aimag (South Gobi Province) of Mongolia. The deposit is within the administrative unit of Gurvantes Soum, 320 km southwest of the provincial capital of Dalanzadgad and 950 km 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. Mining operations at the Ovoot Tolgoi property are found in two distinct areas, referred to as the Sunset Pit to the west and the Sunrise Pit to the east.

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

The following tables summarize the estimated reserves and resources at the Ovoot Tolgoi Mine. The estimates are based on exploration activities undertaken up to the end of 2008. The Mineral Resources are inclusive of the Mineral Reserves.

Summary of Coal Reserves at the Ovoot Tolgoi Mine as of July 1, 2009

Reserve Area	Proven	Probable	Total
	(million tonnes)		
Ovoot Tolgoi Mine	105.0	9.1	114.1

Summary of Coal Resources at Ovoot Tolgoi Mine as of June 1, 2009

Resource Area	Measured	Indicated	Total Measured and Indicated	Inferred
	(million tonnes)			
Ovoot Tolgoi Mine				
Sunset Pit	82.1	19.4	101.5	8.1
Sunrise Pit	53.8	15.7	69.5	4.9
Total Ovoot Tolgoi Mine	135.9	35.1	171.0	13.0

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

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

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.

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

For the three month period ending June 30, 2009, the mine ceased coal production in order to reduce costs and coal inventory. Coal sales to December 31 2008 were approximately 113,000 tonnes. In 2009, coal shipments in the first quarter were approximately 127,000 tonnes; in the second quarter approximately 384,000 tonnes; and in the third quarter approximately 457,000 tonnes. Total shipments since the mine commenced production have now exceeded one million tonnes.

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

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

A north-south railway line currently connects Ceke with Jiayuguan City in Gansu Province and with the interior of China. Another east-west railway line from Ceke to Linhe, an industrial city in eastern Inner Mongolia, is expected to be operational in 2010. This line is anticipated to have an initial transportation capacity of approximately 15 million tonnes per year, later increasing to 25 million tonnes per year. Using this route coal can be shipped to Baotou and further east to ports on China's Bohai Gulf.

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

The Company employed 278 employees as at September 30, 2009. Of the 278 employees, 39, including expatriates, are employed in the Ulaanbaatar office, 7 in outlying smaller offices including the Ceke border point and 232 at the mine site. Of the total 278 employees based in Mongolia, 270 (97%) are Mongolian nationals and 81 (29%) are residents of the local Gurvantes Soum.

In April 2008, the Company purchased a second fleet of coal mining equipment for the open pit mine, which is scheduled to be commissioned in the fourth quarter of 2009. The new shovel / truck mining fleet consists of a Liebherr 996 hydraulic excavator (34 cubic m) and four Terex MT4400 (218-tonne capacity) trucks. The new fleet will supplement the existing mine fleet consisting of a Liebherr 994 hydraulic excavator (13.5-cubic m capacity) and 7 Terex TR100 (91-tonne capacity) trucks.

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

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

The Company is currently completing construction of the Ovoot Tolgoi customs bonded yard situated to the east of the Sunset Pit boundary. This is a customs controlled impound area which will allow mine operations to safely and efficiently load coal trucks destined for China from the stockpiles under the direct supervision of Mongolian customs officers.

Ovoot Tolgoi Underground Deposit

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

In March 2008, The America's Group (TAG) prepared a resource estimate for underground resources in the Sunset Pit (formerly the West Field). Estimated underground resources for the Sunset Pit were 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 Sunset Pit. This drilling was conducted to obtain additional information respecting the structure and quality of the deep underground coal mineralization. The drilling conducted in 2006 and 2007 identified coking and semi-soft coal at depths of between 250 m and 600 m beneath the lower boundaries of the planned open pits at Sunrise and Sunset. The No. 5 coal seam continues to be open at depth and along strike.

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

Summary of Underground Resources at Ovoot Tolgoi Mine as of June 1, 2009

Resource Area	Measured	Indicated	Total Measured and Indicated	Inferred
	(million tonnes)			
Ovoot Tolgoi Underground Deposit				
Sunset Field	34.6	27.8	62.4	9.3
Sunrise Field	11.2	5.2	16.4	11.2
Total Ovoot Tolgoi Underground Deposit	45.8	33.0	78.8	20.5

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

Soumber Deposit

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

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

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

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

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

Tsagaan Tolgoi Deposit

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

A coal delineation program was first carried out in 2004, but no further work was conducted in 2005. Exploration programs were carried out during 2006 and 2007 to provide the basis for a resource estimate. In February 2008, Norwest estimated 23.4 million tonnes of measured resources, 13.0 million tonnes of indicated resources and 9.0 million tonnes of inferred resources. The coal is of volatile bituminous B to C in rank based on ASTM 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.

Effective August 12, 2009, the Mongolian government issued a mining license for the Tsagaan Tolgoi coal field. The Technical and Economic Study has been completed, and is currently under government review. Detailed Environmental Impact Assessment is underway and will be submitted following the approval of the Technical and Economic Study.

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

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

Tavan Tolgoi Extension Area

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

A field reconnaissance program was carried out on the Tavan Tolgoi Extension licenses in 2006. The exploration area has been surveyed for copper and gold exploration using BHP Falcon aerial geophysics. The Company has obtained the aeromagnetic and aero gravity survey data and is using the results of the upcoming analysis of the Falcon data to help delineate potential coal targets. 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 2009 and is currently being updated.

Exploration Program

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

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

Properties in Indonesia

Mamahak Deposit

The Company holds its 85% 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.

In October 2009, SMG updated a resource estimate as at September 11, 2009 for the E and SW resource blocks. SMG has estimated that the resource blocks on the Mamahak Deposit contain 6.9 million tonnes of measured resources, 3.2 million tonnes of indicated resources and 161,000 tonnes of inferred resources. The resource estimates have been calculated to Joint Ore Reserves Committee ("JORC") standards. The JORC resource quantities 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 Resource Report entitled, "Mamahak Coal Project" dated October 12, 2009 and available at www.sedar.com.

As the Company progressed with efforts to prepare for the mining and shipment of the targeted 30,000 tonne trial cargo from Mamahak, the Company became aware of the requirement for additional capital expenditure beyond what was originally budgeted to develop the project. After the initial review of the project expenditures and related budgets, the Company suspended further development works at Mamahak pending a detailed operational review and analysis.

Metals Division Profile and Discontinued Operations

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

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

SELECTED QUARTERLY DATA

($ in thousands, except per share information)

	2009			2008				2007
QUARTER ENDED	**30-Sep**	30-Jun	31-Mar	31-Dec	30-Sep	30-Jun	31-Mar	31-Dec
Revenue	**$ 11,871**	$ 10,667	$ 3,540	$ 3,126	$ -	$ -	$ -	$ -
Impairments	**23,029**	-	-	-	-	-	-	-
Exploration expenses	**5,011**	4,641	4,130	8,104	11,356	10,358	6,375	5,992
Loss from continuing operations	**23,782**	7,910	9,960	14,457	21,110	11,189	14,909	42,500
Loss from discontinued operations	**-**	-	-	2,549	1,667	2,392	1,302	-
Net loss	**23,782**	7,910	9,960	17,006	22,777	13,581	16,211	42,500
Net loss per share	**(0.18)**	(0.06)	(0.07)	(0.13)	(0.17)	(0.11)	(0.19)	(0.57)

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: revenue, exploration expenses, stock-based compensation charges, foreign exchange gains and losses, interest expense, interest accretion on line of credit facility and fair value of embedded derivative on debt. These latter two items are described in Note 3 and 16 to the Consolidated Interim Financial Statements.

Coal shipments began at the end of September 2008, and increased during the quarter ended December 31, 2008. For the three months ended September 30, 2009, revenue increased compared to the three months ended June 30, 2009. Major factors contributing to the increase in sales volumes through 2009 were the mobilization by customers of larger truck fleets and enhancements at 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. Expenditures on the Indonesian Coal Division began in the first quarter of 2008. The net loss in the third quarter of 2009 includes an impairment of Mamahak for $23.0 million offset by a future income tax recovery of $8.6 million related to the Mongolian operations.

RESULTS OF OPERATIONS

	Three Months Ended			Nine Months Ended	
	September 30, 2009	June 30, 2009	September 30, 2008	**September 30, 2009**	September 30, 2008
Volumes, Prices and Costs					
Coal production *(millions of tonnes)*	**0.36**	-	-	**0.51**	-
Coal sales *(millions of tonnes)*	**0.46**	0.38	-	**0.97**	-
Average sales price *(per tonne)*	**$ 27.82**	$ 29.71	-	**$ 28.76**	-
Total cash costs of product sold *(per tonne)*	**$ 13.41**	$ 18.13	-	**$ 15.96**	-
Direct cash costs of product sold *(per tonne)*	**$ 11.16**	$ 16.64	-	**$ 13.75**	-
Operating Statistics					
Total waste material moved *(millions of bank cubic metres)*	**1.06**	-	-	**1.41**	-
Strip ratio *(bank cubic metres of waste rock per tonne of clean coal produced)*	**2.98**	-	-	**2.74**	-
Operating Results *(thousands of dollars)*					
Revenue	**$ 11,871**	$ 10,667	$ -	**$ 26,078**	$ -
Cost of Sales	**(8,637)**	(9,139)	-	**(20,989)**	-
Income from mine operations	**3,234**	1,528	-	**5,089**	-
Adminstration expenses	**(6,234)**	(4,444)	(10,339)	**(16,783)**	(12,851)
Evaluation and exploration expenses	**(5,011)**	(4,641)	(11,356)	**(13,781)**	(28,088)
Impairment charge on Mamahak Coal project	**(23,029)**	-	-	**(23,029)**	-
Operating loss from continuing operations	**$ (31,040)**	$ (7,557)	$ (21,695)	**$ (48,504)**	$ (40,939)

Three Months Ended September 30, 2009 and 2008

The Company incurred an operating loss from continuing operations for the three months ended September 30, 2009 of $31.0 million compared to $21.7 million for the same period in 2008. The variance is due to the factors discussed below.

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

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

In the third quarter of 2009, the Company shipped approximately 457,000 tonnes of coal at an average realized selling price of approximately $28 per tonne. This compares to 384,000 tonnes of coal shipped in the second quarter of 2009 at an average realized selling price of $30 per tonne. Variability in the realized selling price relates to a change in sales mix in terms of coal quality.

Cost of sales was $8.6 million in the current quarter, which comprise the cost of the product sold, mine administration costs, equipment depreciation, and depletion of stripping costs. There were no cost of sales in the third quarter of 2008. Total cash costs per tonne of product sold in the third quarter of 2009 were $13.41 compared to $18.13 for the second quarter of 2009. The decrease is due to the Company resuming full mining operations on July 1, 2009 and higher sales volumes during the third quarter of 2009. In the second quarter of 2009, operational costs were expensed due to the full mine shutdown at the end of February 2009 and therefore resulted in higher total cash costs in the second quarter of 2009.

Exploration expenses for the three months ended September 30, 2009 were lower than the quarter ended September 30, 2008. In the three months ended September 30, 2009, there were decreased drilling expenditures as non-prospective licenses in Mongolia were relinquished and no further exploration work was conducted on these licenses. As well, prior to the commencement of sales in late September 2008, certain operational costs were classified as exploration expense.

Administration expenses for the quarter ended September 30, 2009 were $6.2 million compared to $10.3 million for the quarter ended September 30, 2008. The decrease predominately relates to the listing fees and the movement in the foreign exchange. Administration expenses for the quarter ended September 30, 2009 also include approximately $2.2 million of stock based compensation compared to approximately $1.0 million for the same period last year.

The administration expenses consist of the following major categories broken down for comparative purposes (see Note 9 of the Consolidated Interim Financial Statements).

Legal fees for the quarter ended September 30, 2009 were higher than the quarter ended September 30, 2008. Legal fees include costs associated with the Company's regulatory affairs including expenses associated with corporate governance, contract negotiations, filing, registration and disclosure.

Corporate administration fees increased in the three months ended September 30, 2009 compared to the same period in 2008. The increase relates to additional administration costs incurred in the Hong Kong office. Certain of the Company's administrative staff and office facilities are provided by Global Mining Management Ltd. (see 'Related Party Transactions') on a cost recovery basis. Accordingly, quarterly fluctuations in the costs of administrative and personnel costs can be expected commensurate with increases or decreases in quarterly corporate activity and the level of personnel employed.

Professional fees have increased for the three months ended September 30, 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 increase in the current quarter relates predominantly to costs related to the various technical reports for the Mongolia project.

Salaries and benefits, excluding stock based compensation costs, increased in the three months ended September 30, 2009 to $650,000 as compared to $475,000 for the three months ended September 30, 2008. The increase mainly relates to the additional staff in the Hong Kong office.

The foreign exchange losses are primarily the result of changes of the U.S. to Canadian dollar ("Cdn$") and the U.S. to Mongolian Tugrik exchange rates during the period. The higher foreign exchange loss of $2.0 million in the third quarter of 2008 compared to $273,000 in the current quarter relates to the higher Canadian cash balances.

Listing fees consist of legal, accounting and professional fees incurred for a secondary listing on an Asian stock exchange. Normally the Company would treat the charges as share issue costs upon a successful equity fundraising and had capitalized the listing fees to June 30, 2008. However, uncertainty in the timing of a possible equity financing led to a decision to expense $5.9 million in listing fees in the third quarter of 2008. The Company is continuing with the secondary listing application and has expensed $1.6 million in the current quarter.

In the third quarter of 2009, the Company recorded an impairment charge of $23.0 million related to Mamahak. The impairment includes the impairment of inventory, fixed assets and intangible assets. As the Company progressed with efforts to prepare for the mining and shipment of the targeted 30,000 tonne trial cargo from Mamahak, the Company became aware of the requirement for additional capital expenditure beyond what was originally budgeted to develop the project. After the initial review of the project expenditures and related budgets, the Company suspended further development works at Mamahak pending a detailed operational review and analysis. As a result of the suspension the Company recorded an impairment charge in the third quarter of 2009.

Nine Months Ended September 30, 2009 and 2008

The Company incurred an operating loss from continuing operations for the nine months ended September 30, 2009 of $48.5 million compared to $40.9 million for the same period in 2008. This variance is due to the factors discussed below.

In the nine month period ended September 30, 3009, the Company shipped approximately 968,000 tonnes of coal at an average realized selling price of approximately $29 per tonne.

Cost of sales was $21.0 million in the nine months ended September 30, 2009, which includes the cost of the product sold, mine administration costs, equipment depreciation, and depletion of stripping costs. There were no cost of sales in the nine months ended September 30, 2008. Total cash costs per tonne of product sold in the nine months ended September 30, 2009 were $15.96.

Exploration expenses for the nine months ended September 30, 2009 were $13.8 million as compared to $28.1 million for the same period in 2008. Exploration expenditures in Mongolia in 2008 were higher as the Coal Division acquired equipment, hired additional personnel and began pre-development activities at the Ovoot Tolgoi mine site. Throughout 2008, the Mongolia coal exploration program concentrated on drilling in the Sunset Field. The Coal Division continued its exploration activities in Indonesia throughout the nine months ended September 30, 2009.

Administration expenses were $16.8 million for the nine months ended September 30, 2009 as compared to $12.9 million for the nine months ended September 30, 2008. Stock based compensation expense allocated to administration expenses was $8.1 million for the nine months ended September 30, 2009 and $2.3 million for the same period in 2008. Other amounts that are included in the nine months ended September 30, 2009 that are not in the 2008 period are professional fees related to the various technical reports for the Mongolia project and a corporate consulting contract for the Mongolian operations.

The administration expenses consist of the following major categories broken down for comparative purposes (see Note 9 of the Consolidated Interim Financial Statements).

Legal fees for the nine months ended September 30, 2009 and September 30, 2008 were for costs associated with the Company's regulatory affairs including expenses associated with corporate governance, contract negotiations, filing, registration and disclosure.

Corporate administration fees increased in the nine months ended September 30, 2009 compared to the same period in 2008. The increase relates to higher insurance costs and filing fees.

Professional fees have increased for the nine months ended September 30, 2009 as compared to the same period in 2008. Included in professional fees are the cost of quarterly reviews, internal computer systems training and planning, and accruals for the year end audit of the Company's financial statements. The increase relates predominantly to increased audit fees, increased internal control costs, costs related to the various technical reports for the Mongolia project and a corporate consulting contract for the Mongolian operations.

Salaries and benefits, excluding stock based compensation costs in the nine months ended September 30, 2009 was $1.6 million which was slightly higher than the $1.5 million for the nine months ended September 30, 2008. Bonuses paid in 2008 are offset by higher director fees and the additional salary costs in the Hong Kong office in the nine months ended September 30, 2009.

A foreign exchange loss of $1.3 million was recorded for the nine months ended September 30, 2009 as compared to $808,000 for the nine months ended September 30, 2008. The foreign exchange losses 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 incurred for a secondary listing on an Asian stock exchange. Normally the Company would treat the charges as share issue costs upon a successful equity fundraising and had capitalized the listing fees to June 30, 2008. However, uncertainty in the timing of a possible equity financing led to a decision to expense $5.9 million in the third quarter of 2008. The Company is continuing with the secondary listing application and listing fees of $1.9 million have been expensed in 2009.

In the third quarter of 2009, the Company recorded an impairment charge of $23.0 million related to Mamahak. The impairment includes the impairment of inventory, fixed assets and intangible assets. As the Company progressed with efforts to prepare for the mining and shipment of the targeted 30,000 tonne trial cargo from Mamahak, the Company became aware of the requirement for additional capital expenditure beyond what was originally budgeted to develop the project. After the initial review of the project expenditures and related budgets, the Company suspended further development works at Mamahak pending a detailed operational review and analysis. As a result of the suspension the Company recorded an impairment charge in the third quarter of 2009.

EXPLORATION COSTS AND DISCONTINUED OPERATIONS BY DIVISION

($ in thousands)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2009	2008	**2009**	2008
Mongolian Coal Division	**$ 2,149**	$ 8,468	**$ 4,660**	$ 21,485
Indonesian Coal Division	**2,862**	2,888	**9,121**	6,603
Total Exploration	**$ 5,011**	$ 11,356	**$ 13,781**	$ 28,088

Coal Division

The total coal exploration expenditures in the three months ended September 30, 2009 were $5.0 million compared to $11.4 million for the same period in 2008. For the nine months ended September 30, 2009 coal exploration expenditures were $13.8 million as compared to $28.1 million for the nine months ended September 30, 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 pre-development, overburden removal and stripping activities, which are incurred in the pre-production stage are expensed as incurred. The Company commenced mining operations in Mongolia on April 2, 2008, and costs incurred for site development prior to the production phase were expensed.

The 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 nine months of 2008 were incurred as the Coal Division acquired 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 $2.1 million for the three months ended September 30, 2009 compared to $8.5 million in 2008. Prior to the commencement of sales in late September 2008, certain operational costs were treated as exploration expense. For the three months ended September 30, 2009, the Mongolia exploration expenditures 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.

In Indonesia, exploration expenditures were $2.9 million for the three months ended September 30, 2009 compared to $2.9 million in 2008. The Company began its exploration activities in Indonesia in early 2008. The 2008 drilling program identified quantities of coking coal that appeared to be amenable to surface mining. Exploration expenditures increased in 2009 as the company prepared for production.

As the Company progressed with efforts to prepare for the mining and shipment of the targeted 30,000 tonne trial cargo from Mamahak, the Company became aware of the requirement for additional capital expenditure beyond what was originally budgeted to develop the project. After the initial review of the project expenditures and related budgets, the Company suspended further development works at Mamahak pending a detailed operational review and analysis. As a result of the suspension, the Company has recorded an impairment charge of $23.0 million in the third quarter of 2009.

Metals Division – Discontinued Operations

The Company sold the Metals Division to Ivanhoe in December 2008. The Metals Division consisted 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 and nine months ended September 30, 2008, exploration expenses were $1.7 million and $5.4 million respectively. The majority of the expenses incurred in Mongolia and Indonesia were related to ongoing license fees, drilling, and salaries.

The exploration expenditures of $1.7 million for the quarter ended September 30, 2008 and $5.4 million for the nine months ended September 30, 2008 have been classified as a loss from discontinued operations. The basic and diluted loss per share from discontinued operations is $0.01 for the quarter ended September 30, 2008 and $0.04 for the nine months ended September 30, 2008.

OTHER INCOME/EXPENSE

($ in thousands)

	Three Months Ended September 30		**Nine Months Ended September 30,**	
	2009	2008	**2009**	2008
Fair value change on embedded derivative	**$ -**	$ -	**$ -**	$ (7,223)
Interest accretion on line of credit facilities	**-**	-	**-**	(598)
Interest expense	**(632)**	-	**(1,030)**	(134)
Accretion expense	**(11)**	(5)	**(31)**	(10)
Interest income	**4**	589	**16**	1,698
	$ (639)	$ 584	**$ (1,045)**	$ (6,267)

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 First Funding Agreement was eliminated.

Under IFRS, the conversion feature is considered an embedded derivative liability that must be recorded at its fair value upon initial measurement and revalued at each subsequent reporting period. The difference between the debt host component and the principal amount of the loan outstanding is accreted to income over the remaining term of the debt. (Please refer to Note 16.4 of the Consolidated Interim Financial Statements for further details).

Interest expense was higher in the quarter ended September 30, 2009 and the nine months ended September 30, 2009 compared to the same periods in 2008. 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 interim 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. In July 2009, the Company and Ivanhoe agreed to increase the existing working capital credit facility from $30 million to $60 million. The amended credit facility will mature on December 31, 2010, is unsecured and bears interest at LIBOR plus 750 basis points. The amended facility also requires repayment in the event that the Company acquires additional financing from a third party source and provides for an extension fee of $1.5 million payable in the event any portion of the facility is outstanding past March 31, 2010. This additional $30 million working capital facility allowed the Company to continue to fund its expansion plans and current operations in Mongolia. The Company has received advances of $36 million against the line of credit facility in the first nine months of 2009.

On October 26, 2009, the Company announced it had secured financing from a wholly owned subsidiary of CIC for $500 million and this additional financing will be used to repay the credit facility with Ivanhoe (Please refer to the Liquidity, Financing and Working Capital Resources section for more details).

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

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

In the third quarter of 2009, the Company recorded current income tax expense $712,000 related to its Mongolian operations. The Company's believes profitable operations in Mongolia are probable and has therefore recorded a future income tax asset of $8.6 million related to deductible temporary differences and the carry forward of unused tax losses.

LIQUIDITY AND CAPITAL RESOURCES

Cash Flow Highlights
($ in thousands)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2009	2008	**2009**	2008
Cash used in operating activities	**$ (4,119)**	$ (17,470)	**$ (20,216)**	$ (44,181)
Cash used in investing activities	**(8,598)**	(13,040)	**(24,403)**	(51,782)
Cash generated by financing activities	**12,626**	629	**37,006**	134,227
Effect of foreign exchange rate changes on cash	**(4)**	(2,260)	**(16)**	(866)
(Decrease) increase in cash for the period	**(95)**	(32,141)	**(7,629)**	37,398
Cash balance, beginning of period	**2,806**	70,933	**10,340**	1,394
Cash balance, end of period	**$ 2,711**	**$ 38,792**	**$ 2,711**	**$ 38,792**

General market conditions

In 2008 and in early 2009, market events and conditions, including the disruptions in the international credit markets and other financial systems and deterioration of global economic conditions, caused significant volatility in commodity prices. General economic conditions are showing signs of improvement, and demand for coal in China and India is expected to grow through 2010 and into the foreseeable future. Management continues to monitor external conditions and their impact on the Company's business plans for the upcoming year.

Cash used in operating activities

At September 30, 2009, the Company had cash resources of $2.7 million compared to cash resources of $10.3 million at December 31, 2008.

Cash used in continuing operations was $4.1 million for the three months ended September 30, 2009 compared to $16.0 million for the same period in 2008. For the nine months ended September 30, 2009 cash used in continuing operations was $20.2 compared to $39.9 million for the nine months ended September 30, 2008. Cash used in discontinued operations for the three and nine month periods ended September 30, 2008 was $1.5 million and $4.2 million, respectively.

In the three and nine month period ended September 30, 2009, the Company incurred a net loss from continuing operations of $23.8 million and $41.7 million, respectively, compared to a net loss from continuing operations for the three and nine months ended September 30, 2008 of $21.1 million and $47.2 million respectively. The impairment of Mamahak in the third quarter of 2009 resulted in higher losses in the third quarter of 2009 compared to 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 losses in 2008. In 2009, the Company recorded revenue of $11.9 million for the three months ended September 30, 2009 and $26.1 million for the nine months ended September 30, 2009. With the increased activities at the Ovoot Tolgoi site and the operations in Mongolia, accounts receivable, prepaid expenses, and accounts payable increased during nine months ended 2009.

The foreign exchange losses 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.

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

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

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

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

Coal and supplies inventory have decreased to $10.7 million at September 30, 2009 from $13.7 million at the year ended December 31, 2008. Coal and supplies inventory is valued at the lower of cost and net realizable value. Coal inventory cost of $9.9 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 578,000 tonnes of coal inventory at September 30, 2009 and 688,000 tonnes at June 30, 2009.

Accounts payable have increased in the nine months ended September 30, 2009 due to increased corporate activity.

Cash used for investing activities

Cash used for investing activities was $8.6 million for the three months ended September 30, 2009 compared to $13.0 million for the same period in 2008. For the nine months ended September 30, 2009, cash used for investing activities was $24.4 million compared to $51.8 million for the nine months ended September 30, 2008.

The Company's investment in property, plant and equipment was higher during 2008. Deposits for further mining equipment and maintenance facilities are included as plant and equipment. In the three months ended September 30, 2008, deferred stripping costs in Mongolia were also included. The Company incurred expenditures in 2009 for mobile and mining equipment in Mongolia and construction projects and deferred stripping in Indonesia.

Interest income will increase or decrease in a quarter depending on the cash position. Interest was higher in 2008 due to higher cash balances which related directly to the completion of the equity financings.

Cash provided by financing activities

During the nine months ended September 30, 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 $629,000 and $140.3 million for the three and nine months ended September 30, 2008, compared to proceeds received for the exercise of stock options in the three and nine months ended September 30, 2009 of $626,000 and $1.0 million, respectively.

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

On December 31, 2008, the Company announced the sale of its Metal 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. In July 2009, the Company and Ivanhoe agreed to increase the existing working capital credit facility from $30 million to $60 million. The amended credit facility will mature on December 31, 2010, is unsecured and bears interest at LIBOR plus 750 basis points. The amended facility also requires repayment in the event that the Company acquires additional financing from a third party source and provides for an extension fee of $1.5 million payable in the event any portion of the facility is outstanding past March 31, 2010. For the nine months ended September 30, 2009, the Company received advances of $36 million against the line of credit facility.

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 2010 and is prioritizing its budgeted expenditures with a current emphasis on production and near term cash flow.

On October 12, 2009, the Company announced that it completed a prefeasibility study for the Ovoot Tolgoi Mine resulting in the identification of Proven and Probable Mineral Reserves. The independent estimate prepared by Norwest calculated 114.1 million tonnes of Proven and Probable surface coal reserves at July 1, 2009.

In July 2009, the Company and Ivanhoe agreed to increase the existing working capital credit facility from $30 million to $60 million. The amended credit facility will mature on December 31, 2010, is unsecured and bears interest at LIBOR plus 750 basis points. The amended facility also requires repayment in the event that the Company acquires additional financing from a third party source and provides for an extension fee of $1.5 million payable in the event any portion of the facility is outstanding past March 31, 2010. This additional $30 million working capital facility allowed the Company to continue to fund its expansion plans and current operations in Mongolia and its operations in Indonesia.

On October 26, 2009, the Company announced that it had entered into a financing agreement with a wholly owned subsidiary of CIC for $500 million in the form of a secured, convertible debenture bearing interest at 8.0% with a maximum term of 30 years. The financing is required primarily to support the accelerated investment program in Mongolia and up to $120 million of the financing may also be used for working capital, repayment of debt due on funding, general and administrative expense and other general corporate purposes. The proposed financing has received conditional approval from Canada's TSX Venture Exchange.

Key commercial terms of the financing include:

- Interest - 8% per annum (6.4% payable in cash and 1.6% payable in SouthGobi 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 SouthGobi's assets, including shares of its material subsidiaries;
- Conversion price - The conversion price is set as the lower of Cdn$11.88 or the 50-day VWAP at the date of conversion, with a floor price of Cdn$8.88 per share. Assuming full conversion at the base price of Cdn$11.88 and that any conversion occurs following SouthGobi achieving a 25% public float (on an as converted for the debenture loan basis), CIC's overall shareholding interest in SouthGobi would be approximately 22%;
- Conversion timing - SouthGobi and CIC each have various rights to call conversion of the debenture into common shares. CIC has the right to convert the debenture, in whole or in part, into common shares 12 months after the date of issue. SouthGobi has the right to call for the conversion of up to $250 million of the debenture on the earlier of 24 months after the issue date, if the market price of its common shares is greater than Cdn$10.66, or upon SouthGobi achieving a public float of 25% of its common shares under certain agreed circumstances. If SouthGobi fully exercises its conversion right immediately following its achieving a 25% public float (on an as converted for the debenture loan basis) and assuming conversion at the Cdn$11.88 base price, CIC's initial shareholding interest in SouthGobi would be approximately 11%;
- Company's normal conversion right – After 60 months from the issuance date, at any time that the VWAP of the Company's shares for the 50 business days is 20% higher than the floor price, the Company will be entitled to require conversion of all outstanding convertible debentures into common shares at the conversion price;
- Representation on SouthGobi Board - While the debenture loan is outstanding, or while CIC has a minimum 15% direct or indirect stake in SouthGobi, CIC has the right to nominate one director to SouthGobi's Board. SouthGobi currently has eight Board members;
- Voting restriction - CIC has agreed that it will not have any voting rights in SouthGobi beyond 29.9% if CIC ever acquires ownership of such a shareholder stake through exercising the debenture;
- Pre-emption rights - While the debenture loan is outstanding, or while CIC has a 15% direct or indirect stake in SouthGobi, CIC has certain pre-emption rights on a pro-rata basis to subscribe for any new shares to be allotted and issued by SouthGobi for the period which the debenture is outstanding. The pre-emption rights will not apply to new shares issued pursuant to pro-rata public equity offerings made to all shareholders, exercise of stock options and shares issued to achieve a 25% public float;

- Right of first offer - While a portion of the debenture is outstanding, or while CIC has a 15% direct or indirect stake in SouthGobi, CIC has the right of first offer for any direct and indirect sale of Ivanhoe Mines' ownership stake in SouthGobi. Ivanhoe Mines currently owns directly and indirectly approximately 105.8 million SouthGobi shares, or approximately 79% of SouthGobi's current issued and outstanding shares; and
- Registration Rights - CIC has registration rights under applicable Canadian provincial securities laws in connection with the common shares issuable upon conversion of the debenture.

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

The Company expects this transaction to close in the fourth quarter of 2009.

RELATED PARTY TRANSACTIONS

The Company is a party to a shareholders' cost-sharing agreement with certain other public and private companies, including Ivanhoe (the "Other Companies") pursuant to which the Company and the Other Companies are equal shareholders in Global Mining Management Ltd. ("GMM") and, through GMM, share office space, furnishings and equipment and communications facilities (on a cost recovery basis) and the employment, on a part-time basis, of various administrative, office and management personnel in Vancouver, British Columbia. Costs of the shared office facilities and the shared part-time employees and service providers are recovered from the Company proportionate to the time spent by the shared part-time employees and service providers on matters pertaining to the Company. Certain of the directors and officers of the Company are also officers and directors of GMM. The Company has utilized the services of the GMM staff and office since September 1, 2003 and has incurred costs of $1.4 million and $2.0 million for the nine months ended September 30, 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 consisted of a series of base and precious metal exploration properties in Mongolia and Indonesia, related assets, employees and contracts. As part of the sale transaction, the Company obtained a credit facility from Ivanhoe, which 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.

In July 2009, the Company and Ivanhoe agreed to increase the existing working capital credit facility from $30 million to $60 million. The amended credit facility will mature on December 31, 2010, is unsecured and bears interest at LIBOR plus 750 basis points. The amended facility also requires repayment in the event that the Company acquires additional financing from a third party source and provides for an extension fee of $1.5 million payable in the event any portion of the facility is outstanding past March 31, 2010. This additional $30 million working capital facility allowed the Company to continue to fund its expansion plans and current operations in Mongolia and its operations in Indonesia.

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 November 3, 2009: 133,702,749 common shares were issued and outstanding. There are also incentive stock options outstanding that are exercisable to acquire 8,313,918 unissued common shares. On a diluted basis, 142,016,667 common shares were outstanding. There are no preferred shares outstanding.

Ivanhoe, directly and indirectly, currently owns 105,782,155 common shares representing approximately 79% 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

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

We believe that demand for commodities is increasing as the current economic crisis passes. General economic conditions are showing signs of improvement. It is still difficult to forecast commodity prices and customer demand for our products; however our sales and marketing efforts in the most recent quarter are providing positive results. The Company is continuing to pursue new customers, and maintain strong relations with its current customer base.

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

Our success to date and potential for future growth can be attributed to a combination of our competitive strengths, including the following:

- Projects are strategically located close to China, especially to the fast growing Gansu and Inner Mongolia regions;
- Substantial and growing resources and reserves;
- Produce premium quality coals;
- Low cost structure due to favorable geographic and geological conditions;
- Established production with strong growth potential through future expansion of our existing mine capacity and development of our priority assets; and

- Experienced management team with strong skills in mining, exploration and marketing and are able to leverage the expertise, experience and relationships of our principal shareholder, Ivanhoe.

Mongolia

Revenue was $11.9 million for the three months ended September 30, 2009 compared to $10.7 million for the three months ended June 30, 2009. The Company will continue to focus on generating higher sales volume throughout the remainder of 2009.

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

- Total surface mineable coal reserves as of July 1, 2009 at Ovoot Tolgoi were calculated and estimated to be 105 million tonnes of proven reserves and 9.1 million tonnes of probable reserves;

- Ovoot Tolgoi surface and underground resources as of June 1, 2009 were calculated and estimated to be 181.7 million tonnes of measured resources, 68.1 million tonnes of indicated resources and 33.5 million tonnes of inferred resources; and

- The Soumber resource area is estimated to contain 13.1 million tonnes of measured resources, 8.3 million tonnes of indicated resources and 55.5 million tonnes of inferred resources.

In March 2009, the border started opening more reliably for seven days per week on an eight hour per day basis. In April and May 2009, shipments totaled approximately 152,000 tonnes. In June, the border started operating at 11 hours per day, six days per week. Total shipments in June were approximately 232,000 tonnes, a new record for the Company. For the third quarter 2009 total shipments were 457,000 tonnes.

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

As we move to ramping up our surface production, Norwest considers it possible that our total coal production from the Ovoot Tolgoi Mine could increase to approximately 4 million tonnes in 2010 and approximately 8 million tonnes in 2012.

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

Indonesia

As the Company progressed with efforts to prepare for the mining and shipment of the targeted 30,000 tonne trial cargo from Mamahak, the Company became aware of the requirement for additional capital expenditure beyond what was originally budgeted to develop the project. After the initial review of the project expenditures and related budgets, the Company suspended further development works at Mamahak pending a detailed operational review and analysis.

Overview and Objectives

We continue to focus our efforts on mining, development and exploration of coking and thermal coal products in Mongolia for supply of quality products to our customers in China. As we look forward through the remainder of 2009, we are encouraged by the positive developments in Mongolia. We are making progress with our sales and marketing efforts, continuing to focus on efficiency and prudent financial management and intend to manage production levels to meet anticipated demand for our products.

Our objectives for the remainder of 2009 and as we look forward into 2010 are as follows:

- Expanding production at the Ovoot Tolgoi Mine;
- Developing integrated infrastructure for the area around the Ovoot Tolgoi Mine;
- Advancing the development of the Soumber Deposit;
- Enhancing the value of our products that are delivered to end customers;
- Continuing to develop attractive and value enhancing coal projects;
- Undertaking exploration initiatives to establish and expand reserves and resources; and
- Continuing to focus on production safety, environmental protection, operational excellence and community relations.

November 3, 2009