SouthGobi Resources Ltd.

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

June 30, 2010

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

TABLE OF CONTENTS

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

1. OVERVIEW

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

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

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

The Ovoot Tolgoi Mine, strategically located approximately 40 kilometers ("km") from the China-Mongolia border, is the Company's flagship producing asset. The Company commenced mining at Ovoot Tolgoi's Sunset Pit in April 2008 and commenced coal sales in September 2008. The products from the Ovoot Tolgoi Mine include coals with coking (or metallurgical) applications primarily a semi-soft coking coal, and a thermal coal, which are sold to customers in China. Since the commencement of production in late 2008 until June 30, 2010, the Company has sold approximately 2.2 million tonnes of coal from the Ovoot Tolgoi Mine. During the quarter ended June 30, 2010, the Company sold approximately 449,000 tonnes of coal. The Ovoot Tolgoi Mine is covered by a single 9,308 hectare ("ha") mining license and a corresponding permit to mine.

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

The Company has conducted substantial exploration activities at the Ovoot Tolgoi Underground Deposit and has delineated mineral resources at this project. The Ovoot Tolgoi Underground Deposit is covered by the existing Ovoot Tolgoi Mining License. In addition, the Company owns the Tsagaan Tolgoi Deposit in Mongolia, which has a mining license.

1. OVERVIEW (Continued)

1.1 Corporate Developments

Ovoot Tolgoi Complex

Coal shipments from the Ovoot Tolgoi Mine commenced in late September 2008. Throughout 2009, the Company continued coordinating efforts with the Mongolian Government and various agencies to improve border crossing access for coal shipments. In July 2009, Mongolian and Chinese officials met at the Mongolian-Chinese border and allocated designated gates for coal exports to create an expedited coal border crossing corridor.

As a result of continuing discussions with the Mongolian Government, border access has improved through early 2010, which has allowed for increased shipments to the Company's market in China.

Total shipments for the year ended December 31 2009 were 1.3 million tonnes with an average realized selling price of $29 per tonne. Total shipments for the quarter ended June 30, 2010 were 449,000 tonnes with an average realized selling price of $43 per tonne. Total shipments for the first half of 2010 are 874,000 tonnes at an average realized price of $39 per tonne.

The Company continues to ramp up production at the Ovoot Tolgoi Mine. The additional equipment for the second mining fleet including the larger Liebherr 996 shovel, four 218 tonne Terex haul trucks and various auxiliary equipment was delivered throughout the fourth quarter of 2009 and early 2010 and full commissioning was completed in June 2010. The Company expects that the third mining fleet, already ordered, will be commissioned in late 2010. An additional fourth fleet of equipment has been ordered for delivery in 2011.

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 105 million tonnes of proven and 9.1 million tonnes of probable surface coal reserves at July 1, 2009. Details of the assumptions and parameters used to calculate these coal resources and coal quality estimates are set out in the Technical Report entitled, "Coal Geology, Resources and Reserves Ovoot Tolgoi: A Production Property. Omnogovi Aimag, Mongolia" dated October 21, 2009, and available at www.sedar.com.

1. OVERVIEW (Continued)

The Company also announced that it had received an updated independent NI 43-101 compliant resource estimate for the Ovoot Tolgoi Complex, prepared by Norwest. Details of the assumptions and parameters used to calculate these coal resources and coal quality estimates are set out in the Technical Report entitled, "Coal Geology, Resources and Reserves Ovoot Tolgoi: A Production Property. Omnogovi Aimag, Mongolia" dated October 21, 2009, and available at www.sedar.com.

The Ovoot Tolgoi Complex surface and underground resources contain measured resources of 181.7 million tonnes plus indicated coal resources of 68.1 million tonnes, with an additional inferred coal resource of 33.5 million tonnes as at June 1, 2009.

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

To further enhance the value of our products, the Company commenced construction of a basic coal-handling facility in June 2010. The coal-handling facility is planned to be operational in early 2011.

Soumber Deposit

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

The Soumber coal project and resource area is estimated to contain initial measured resources of 13.1 million tonnes plus indicated coal resources of 8.3 million tonnes, with an additional inferred coal resource of 55.5 million tonnes as at August 11, 2009.

In March 2010, drilling re-commenced at the Soumber Deposit to expand and better define the resource. Preparatory work for a formal mining license application continues.

1. OVERVIEW (Continued)

1.2 Corporate Activity

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

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

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

On February 26, 2010, Citigroup Global Markets Canada Inc. and Macquarie Capital Markets Canada, representatives of the Canadian underwriters of the Company's global equity offering, partially exercised their over-allotment option and purchased an additional 228,100 common shares of the Company at a price of Cdn$17.00 per share for gross proceeds of Cdn$3.9 million.

On March 29, 2010 the Company converted $250 million of the $500 million convertible debenture into 21,471,045 common shares of the Company. Following the conversion China Investment Corporation ("CIC), through its indirect wholly owned subsidiary, owns approximately 13% of the Company.

On May 11, 2010, the Company's shareholders approved the Company's name change to SouthGobi Resources Ltd. (formerly SouthGobi Energy Resources Ltd.).

On June 8, 2010, the Company announced that its Board of Directors authorized a share repurchase program to purchase up to 2.5 million common shares of the Company on each or either of the Toronto Stock Exchange and the Hong Kong Stock Exchange, in aggregate representing up to 5 million common shares of the Company. As of August 11, 2010, the Company had not repurchased any common shares.

1. OVERVIEW (Continued)

On June 28, 2010, the Company announced it had commenced construction of a basic coal-handling facility at its producing Ovoot Tolgoi Complex in southern Mongolia.

As of August 11, 2010, Ivanhoe directly and indirectly, owned 105,332,155 common shares representing approximately 57% of the issued and outstanding common shares of SouthGobi.

2. 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.

3. CRITICAL ACCOUNTING ESTIMATES

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

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

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

Mineral properties

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

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

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

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

3. CRITICAL ACCOUNTING ESTIMATES (Continued)

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

3. CRITICAL ACCOUNTING ESTIMATES (Continued)

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

Income taxes

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

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

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.

Share-based payments

Share-based payment transactions

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

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

3. CRITICAL ACCOUNTING ESTIMATES (Continued)

Equity-settled transactions

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

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

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

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

Property, plant and equipment

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

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

4. MINERAL PROPERTIES

4.1 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").

4.2 Mongolia Exploration and Mining 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 June 30, 2010, the Company held 18 licenses, including the two mining licenses, which in total cover an area of approximately 784,000 ha.

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

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

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

4. MINERAL PROPERTIES (Continued)

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

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

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

4.3 Properties in Mongolia

Ovoot Tolgoi Mine

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

The Ovoot Tolgoi Mine is located in the southwest corner of the Omnogovi Aimag (South Gobi Province) of Mongolia. The deposit is within the administrative unit of Gurvantes Soum, 270km southwest of the provincial capital of Dalanzadgad and 700km southwest of the nation's capital of Ulaanbaatar.

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

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

On October 12, 2009, the Company announced an independent resource estimate prepared by Norwest under the requirements of NI 43-101. Norwest estimated that the Ovoot Tolgoi Mine contained approximately 114.1 million tonnes of reserves, calculated as 105 million tonnes of proven and 9.1 million tonnes of probable surface coal reserves at July 1, 2009, 135.9 million tonnes of measured resources, 35.1 million tonnes of indicated resources and 13.0 million tonnes of inferred resources. The Mineral Resources are inclusive of Mineral Reserves.

4. MINERAL PROPERTIES (Continued)

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.

Products that are presently being mined or are expected to be produced at the Ovoot Tolgoi Mine include coals with coking (or metallurgical) applications, primarily a semi-soft coking coal, and a thermal coal product for use in power generation.

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

To further enhance product value, the Company commenced construction of a basic coal-handling facility in June 2010. The coal-handling facility will allow the Company to remove ash (waste rock) and enable the blending of coal from different seams to create higher-value products. Expected to be operational in early 2011, the coal-handling facility will include a 300-tonne–capacity dump hopper, which will receive run-of-mine coal from the Ovoot Tolgoi Mine and feed a coal rotary breaker that will size coal to a maximum of 50 millimeters and reject oversize ash. A radial stacker will facilitate loading of the sized coal into customers' trucks. The coal-handling facility will be located between Ovoot Tolgoi's Sunset and Sunrise open-pits and is expected to initially operate on one 12-hour shift per day, six days per week. Annual capacity on that basis will be up to six million tonnes of coal and can be adjusted upwards as mining capacity increases.

In 2010, coal shipments in the second quarter were approximately 449,000 tonnes compared to total shipments in the second quarter of 2009 of approximately 384,000 tonnes. Total shipments since the mine commenced production have now exceeded 2.2 million tonnes.

4. MINERAL PROPERTIES (Continued)

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 predominantly complete and is already in partial use. It permits 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 substantially increase the amount of coal shipped into China. On April 28, 2010, the Mongolian Government approved a plan that would allow the border check-point to operate 24 hours per day, seven days per week.

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

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

Since December 2008, the Company has been engaged in various levels of discussions with railway contractors regarding the feasibility of developing a coal railway spur from the Ovoot Tolgoi Mine to the Mongolia-China border. Discussions by the Mongolian parliament and the Government of Mongolia during the second quarter of 2010 indicate an increased willingness to approve development of new north-south railway spurs linking Mongolian mines to China at some point in the future. However, while the Company continues to evaluate a north-south railway spur from the Ovoot Tolgoi Mine, it is currently focusing on improving truck transportation. Coal trucked to China through the Shivee Khuren/Ceke checkpoint can readily be loaded onto the Chinese rail lines mentioned above.

SouthGobi Sands LLC, a wholly owned Mongolian subsidiary of SouthGobi, employed 406 employees as at June 30, 2010. Of the 406 employees, 51, including expatriates, are employed in the Ulaanbaatar office, 4 in outlying smaller offices, including the Ceke border point, and 351 at the mine site. Of the total 406 employees based in Mongolia, 395 (97%) are Mongolian nationals and of those, 125 (31%) are residents of the local Gurvantes Soum.

4. MINERAL PROPERTIES (Continued)

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

Additional equipment will be required as production at the mine expands. The Company has entered into an agreement with a Mongolian supplier for a third mining fleet including an additional Liebherr 996 hydraulic excavator (34m^3), five Terex MT4400 (218-tonne capacity) trucks and various auxiliary equipment. Trucks for this third fleet have already begun to arrive on site and are being assembled. The hydraulic excavator has been shipped from Europe and is expected to be delivered in late 2010 along with various other pieces of ancillary equipment.

An additional fourth fleet of equipment, which includes another Liebherr 996 shovel, trucks and other support equipment, was ordered in April 2010 for delivery in 2011. The additional larger equipment fleets are expected to increase productive capacity. However, the Company will continue to employ the smaller initial fleet in areas of thinner seams and to supplement the larger equipment.

SouthGobi continues to assess fleet requirements at Ovoot Tolgoi Mine including the consideration of adding additional equipment to expand capacity beyond current plans.

Throughout the current quarter ended June 30, 2010, the Company continued to develop its coal markets in China. Total sales in the quarter ended June 30, 2010 were 449,000 tonnes consisting of premium and thermal coal. Although the Company continues to sell its coal on shorter term contracts, with consistent pricing increases, longer term contracts will be pursued as the Company develops contacts with larger customers in China.

4. MINERAL PROPERTIES (Continued)

Soumber Deposit

The Soumber Deposit is located approximately 20km east of the Ovoot Tolgoi Mine. It lies within the administrative unit of Gurvantes Soum in the Omnogovi Aimag (South Gobi Province), approximately 50km 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 meters ("m") of drilling were completed. In 2009, the Company conducted geotechnical and hydrological programs in the Soumber central field. The exploration geology fieldwork included reconnaissance mapping, trenching, geologic descriptions of drilling returns, geotechnical data, field logs and database development.

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

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

Additional drilling commenced in March 2010. The drilling will expand and better define the resource and includes a series of open-holes and core holes. Over 38,000m of core and RC holes have already been drilled on the Soumber Deposit and surrounding areas to the end June 30, 2010.

4. MINERAL PROPERTIES (Continued)

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

SouthGobi is currently preparing revised studies on the Soumber Deposit, incorporating the additional geological data, according to Mongolian regulatory requirements to enable the Company to proceed to a formal registration of the resource and application for a mining license.

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 600m that is designated for potential underground development is located inside the existing Ovoot Tolgoi mining license.

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

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

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

4. MINERAL PROPERTIES (Continued)

Tsagaan Tolgoi Deposit

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

A coal delineation program was first carried out in 2004, but no work was conducted in 2005. Exploration programs were carried out during 2006 and 2007 to provide the basis for a resource estimate. In February 2008, Norwest estimated 23.4 million tonnes of measured resources, 13.0 million tonnes of indicated resources and 9.0 million tonnes of inferred resources. The coal is of volatile bituminous B to C in rank based on ASTM D388 standards and is suitable for use as a thermal coal. The resources appear to be amenable to surface extraction down to a planned depth of 150 m. Details of the assumptions and parameters used to calculate these coal resources and coal quality estimates are set out in the Technical Report entitled, "Coal Geology and Resources – Tsagaan Tolgoi Property" dated March 25, 2008, and available at www.sedar.com.

Effective August 12, 2009, the Mongolian Government issued a mining license for the Tsagaan Tolgoi coal field. The Technical and Economic Study has been completed, and is currently under government review. The Detailed Environmental Impact Assessment was approved on April 9, 2010.

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 400km to the east at the Chinese border. Limited infrastructure exists at Tsagaan Tolgoi and will need to be developed prior to commencing 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 established there.

The Company has no current plans to develop the Tsagaan Tolgoi Deposit, although the property remains a deposit that could be developed in the future.

4. MINERAL PROPERTIES (Continued)

Tavan Tolgoi Extension Area

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

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

Exploration Program

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

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

Substantive physical exploration for 2010 commenced in March. For the six months ended June 30, 2010, $8.3 million has been spent, including 62,270m^3 of trenching and over 64,000m of drilling (both core and reverse circulation). Key targets so far have been the Soumber Deposit and the fields surrounding the Soumber Deposit and a target approximately six kilometers to the south-west of the Ovoot Tolgoi Complex known as the SW target. For the six months ended June 30, 2010 $5.9 million has been spent on the Soumber Deposit and surrounding area.

The drilling program will focus primarily on further definition of known coal occurrences to bring them to a 43-101 compliant resource definition stage and to allow for registration with the Mongolian Government as the next step toward expanding the Company's mining license holdings.

5. SELECTED QUARTERLY DATA

($ in thousands, except per share information)

	2010	2010	2009				2008	
QUARTER ENDED	**30-Jun**	31-Mar	31-Dec	30-Sep	30-Jun	31-Mar	31-Dec	30-Sep
Revenue	**$ 17,668**	$ 13,917	$ 9,960	$ 11,871	$ 10,666	$ 3,541	$ 3,126	$ -
Income from mine operations	**4,400**	1,187	1,524	3,234	1,527	328	949	-
Evaluation and exploration expenses	**(6,659)**	(1,651)	(739)	(2,149)	(1,742)	(768)	(4,959)	(8,468)
Net interest (expense)/income	**(4,384)**	(9,024)	(8,246)	(643)	(356)	(57)	147	584
Other finance income /(costs)	**67,677**	(153,410)	(53,536)	-	-	-	-	-
Total finance income /(costs)	**63,293**	(162,434)	(61,782)	(643)	(356)	(57)	147	584
Net (loss)/income from continuing operations before other finance income/(costs)	**(14,376)**	(14,861)	(16,651)	2,224	(5,139)	(6,616)	(11,370)	(18,222)
Income/(loss) from continuing operations	**53,301**	(168,271)	(70,187)	2,224	(5,139)	(6,616)	(11,370)	(18,222)
Income/(loss) from discontinued operations	**-**	-	1,034	(26,006)	(2,772)	(3,344)	(5,637)	(4,555)
Net income/(loss)	**53,301**	(168,271)	(69,153)	(23,782)	(7,911)	(9,960)	(17,007)	(22,777)
Net income/(loss) per share	**0.29**	(1.09)	(0.52)	(0.18)	(0.06)	(0.08)	(0.13)	(0.17)

Review of Quarterly Financial Results

The changes in comparative results of operations on a quarter over quarter basis are due primarily to significant fluctuations in the following areas: revenue, exploration expenses, stock-based compensation charges, foreign exchange gains and losses, interest expense, loss on partial conversion of the convertible debenture and fair value change of embedded derivatives in convertible debt. These latter two items are described in Notes 7 and 16 of the Condensed Consolidated Interim Financial Statements.

The Company recorded net income for the three months ended June 30, 2010 of $53.3 million compared to a net loss $168.3 million for the three months ended March 31, 2010 and a net loss of $7.9 million for the three months ended June 30, 2009. The net income in the second quarter of 2010 is due primarily to the $72.2 million gain on the fair value change of the embedded derivatives in the CIC convertible debenture.

The net loss from continuing operations before other finance income/(costs) was $14.4 million for the second quarter of 2010 compared to $14.9 million for the first quarter of 2010. In the second quarter of 2010, other finance income/(costs) includes a gain of $72.2 million on the fair value change of the embedded derivatives in the convertible debenture and a $4.6 million mark to market loss on investments. In the first quarter of 2010, other finance income/(costs) includes a $151.4 million loss on partial conversion of the convertible debenture, a $1.4 million loss on the fair value change on the embedded derivatives in the convertible debenture and a $0.7 million mark to market loss on investments.

5. SELECTED QUARTERLY DATA (Continued)

Revenue and income from mine operations relate to the Mongolian Coal Division. Revenues increased to $17.7 million in the second quarter of 2010 from $13.9 million in the first quarter of 2010 and from $10.7 million in the second quarter of 2009. Revenues have increased due to both higher sales volumes and higher realized sales prices.

In the second quarter of 2010, the Company shipped approximately 449,000 tonnes at an average realized price of $43 per tonne. This compares to approximately 426,000 tonnes at an average realized selling price of $36 per tonne in the first quarter of 2010 and 384,000 tonnes of coal at an average realized selling price of $30 per tonne in the second quarter of 2009. Variability in the realized selling price relates primarily to increased prices of individual customer contracts.

Income from mine operations increased to $4.4 million in the second quarter of 2010 from $1.2 million in the first quarter of 2010 and $1.5 million in the second quarter of 2009. Income from mine operations in the second quarter of 2010 was higher than all previous quarters due primarily to the higher average realized sales price. Income from mine operations will vary depending on sales volume, sales price, production and unit costs.

Exploration costs for the three months ended June 30, 2010, increased to $6.7 million as drilling continued on Soumber and additional greenfield targets in Mongolia. Exploration costs will vary from quarter to quarter depending on the number of projects and the related seasonality of the exploration programs.

The income from continuing operations includes finance income for the three months ended June 30, 2010 of $72.9 million compared to $0.6 million in the first quarter of 2010. The significant increase in finance income relates to the fair value change of embedded derivatives in the CIC convertible debenture. The Company incurred finance costs for the three months ended June 30, 2010 of $9.6 million compared to $171.2 million for the three months ended March 31, 2010. In the first quarter of 2010, finance costs included a $151.4 million loss on partial conversion of the CIC convertible debenture. The large fluctuations in finance income and finance costs in 2010 are due primarily to fluctuations in the Company's share price which impact the carrying value of the CIC convertible debenture. (See Finance Income/(Costs) section).

Discontinued operations for the three months ended June 30, 2009 relate to the Indonesia Coal Division.

6. RESULTS OF OPERATIONS

	Three months ended June 30,		Six months ended June 30,	
	2010	2009	2010	2009
Volumes, Prices and Costs				
Coal production *(millions of tonnes)*	**0.62**	-	**0.84**	0.16
Coal sales *(millions of tonnes)*	**0.45**	0.38	**0.87**	0.51
Average realized sales price *(per tonne)*	**$ 42.63**	$ 29.71	**$ 39.17**	$ 29.60
Total cash costs of product sold *(per tonne)*	**$ 22.30**	$ 18.13	**$ 22.80**	$ 18.23
Direct cash costs of product sold *(per tonne)*	**$ 21.37**	$ 16.64	**$ 21.81**	$ 16.05
Operating Statistics				
Sunset				
Total waste material moved *(millions of bank cubic metres)*	**1.73**	-	**3.22**	0.34
Strip ratio *(bank cubic metres of waste rock per tonne of clean coal produced)*	**2.79**	-	**3.84**	2.19
Sunrise				
Total waste material moved *(millions of bank cubic metres)*	**0.02**	-	**0.02**	-
Operating Results ***(thousands of dollars)***				
Revenue	**$ 17,668**	$ 10,666	**$ 31,585**	$ 14,207
Cost of sales	**(13,268)**	(9,139)	**(25,998)**	(12,352)
Income from mine operations	**4,400**	1,527	**5,587**	1,855
Administration expenses	**(8,336)**	(4,568)	**(14,370)**	(10,687)
Evaluation and exploration expenses	**(6,659)**	(1,742)	**(8,310)**	(2,511)
Operating loss from continuing operations	**$ (10,595)**	$ (4,783)	**$ (17,093)**	$ (11,343)

6.1 Three Months Ended June 30, 2010 and 2009

In December 2009, the Company commenced realigning the open-pit for a north-south entry. Waste removal at Ovoot Tolgoi was originally along the seam's strike-length, i.e. east-west. This allowed for better utilization of capital when financing was more constrained. Strip ratio and waste movements were lower and customer trucks were allowed to enter directly in the shallow pit for loading. However, such alignment is not beneficial for the longer-term because it becomes less efficient as the pit depth increases.

Realigning for a north-south entry is expected to provide the following long-term benefits:

- allow for longer mining faces to be exposed for larger shovels (eg Liebherr 996) to access;
- enable mining of the thinner 8, 9 and 10 seams 'face on' as opposed to 'along strike' enabling cleaner mining and a lower ash, higher value product; and
- allow more efficient access for haul trucks as the pit deepens.

6. RESULTS OF OPERATIONS (Continued)

Realigning the pit has impacted operations because the process requires substantial above-trend waste removal. The open-pit realignment was the primary cause of the increase in direct cash costs of production and a constrained availability of coal in the first quarter of 2010. The open-pit realignment has been completed but continues to impact cost per tonne sold in the second quarter of 2010. Higher cost inventory from the first quarter was sold in the second quarter and direct cash cost per tonnes produced started decreasing towards the end of the second quarter.

In addition to the impact of the pit-realignment, costs were adversely impacted by fleet issues. Delayed commissioning of the final two Terex MT4400 (218 tonne) haul trucks from the second mining fleet meant the Liebherr 996 shovel was not operating efficiently. Furthermore, the Company's Terex TR100 (91-tonne capacity) haul trucks from the first mining fleet have been experiencing poor equipment availability ratios (approximately 72% availability for the second quarter of 2010), leading to lower productivity and increased maintenance costs.

In the three months ended June 30, 2010, 0.62 million tonnes of coal was produced with a strip ratio of 2.79 compared to no production in the three months ended June 30, 2009. In 2009, there was a full mine shutdown from the end of February 2009 to the end of June 2009.

The Company incurred an operating loss from continuing operations for the three months ended June 30, 2010 of $10.6 million compared to $4.8 million loss in the same period in 2009. The operating loss is impacted by the factors discussed below.

In the three months ended June 30, 2010, the Company shipped approximately 0.45 million tonnes of coal at an average realized selling price of approximately $43 per tonne. This compares to 0.38 million tonnes of coal shipped in the three months ended June 30, 2009 at an average realized selling price of $30 per tonne. The increased sales volume and average realized price in the second quarter of 2010 resulted in higher sales revenue compared to the second quarter of 2009.

6. RESULTS OF OPERATIONS (Continued)

Cost of sales was $13.3 million in the three months ended June 30, 2010, compared to $9.1 million for the three months ended June 30, 2009. The increase in cost of sales relates to the higher sales volume and higher costs in 2010. Also, during the quarter ended June 30, 2010, the Company continued to realign the open-pit resulting in higher operating costs. Additional mobile equipment acquired in 2009 and 2010, resulted in higher depreciation in the quarter ended June 30, 2010. Cost of sales is comprised of three main components, direct cash costs of products sold, mine administration costs and non-cash items. Non-cash items include depreciation, depletion of stripping costs and stock-based compensation. Cost of sales will vary depending on sales volume, production and unit costs which directly affects income from mine operations.

Direct cash costs of product sold were $21.37 per tonne in the three months ended June 30, 2010 compared to $16.64 for the same period in 2009. The increase in direct cash costs is due to the continuing realignment of the open-pit in the second quarter of 2010 and higher maintenance costs as a result of the increase in mobile equipment on site.

Mine administration costs per tonne decreased to $0.93 per tonne for the three months ended June 30, 2010, compared to $1.50 per tonne for the three months ended June 30, 2009. The decrease per tonne is due to the higher sales volume in 2010 and lower mine administration costs.

Exploration expenses for the three months ended June 30, 2010, were higher than the three months ended June 30, 2009. Increased exploration expense in 2010 relates to increased drilling at the Soumber deposit and additional greenfield targets.

Administration expenses for the three months ended June 30, 2010 were $8.3 million compared to $4.6 million for the three months ended June 30, 2009. Administration expenses for the three months ended June 30, 2010, includes approximately $2.3 million of stock-based compensation compared to approximately $2.6 million for the three months ended June 30, 2009.

The administration expenses consist of the following major categories broken down for comparative purposes (see Note 6 of the Condensed Consolidated Interim Financial Statements).

6. RESULTS OF OPERATIONS (Continued)

Legal fees for the three months ended June 30, 2010, were higher than the three months ended June 30, 2009. Legal fees include costs associated with the Company's regulatory affairs including expenses associated with corporate governance, contract negotiations, filing, registration and disclosure. Legal fees increased in 2010 due to increased regulatory requirements and corporate activity.

Corporate administration fees are higher in the three months ended June 30, 2010, compared to the three months ended June 30, 2009. The increase predominantly relates to additional administration costs incurred as the Company continues to expand its management team, higher investor relations costs, travel costs and administration support costs. 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 June 30, 2010, as compared to the three months ended June 30, 2009. The three months ended June 30, 2010 included a corporate consulting contract cost of $0.5 million for the Mongolian operations. Professional fees include the cost of internal computer systems training and planning, technical reports for the Mongolia project and accruals related to the review and audit of the Company's financial statements.

Salaries and benefits, excluding stock-based compensation costs, increased in the three months ended June 30, 2010 to $0.95 million as compared to $0.55 million for the three months ended June 30, 2009. The increase relates to additional staff for the three months ended June 30, 2010.

Sustainability and community relations are costs incurred in Mongolia. Sustainability and community relations expenses were $0.1 million in the second quarter of 2010. The Company is committed to contributing to communities in Mongolia and developing and maintaining a positive relationship with the various communities in which the Company operates.

Public infrastructure costs were $1.6 million in the second quarter of 2010. These costs relate to the upgrading of transportation infrastructure from the Ovoot Tolgoi Mine to the Chinese border.

6. RESULTS OF OPERATIONS (Continued)

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.

Listing fees consist of legal, accounting and professional fees incurred for a secondary listing on the Hong Kong stock exchange. On January 29, 2010 the Company closed a global equity offering and commenced trading on the Main Board of the Hong Kong Stock Exchange. Normally the Company would treat all charges as share issue costs upon a successful equity fundraising, however due to the uncertainty in the timing of a possible equity financing in 2009, listing fees were expensed in the first and second quarter of 2009.

6.2 Six Months Ended June 30, 2010 and 2009

The Company incurred an operating loss from continuing operations for the six months ended June 30, 2010 of $17.1 million compared to $11.3 million for the same period in 2009. This variance is due to the factors discussed below.

In the six month period ended June 30, 2010, the Company shipped approximately 874,000 tonnes at an average realized selling price of approximately $39 per tonne compared to 512,000 tonnes at an average realized selling price of approximately $30 per tonne in the six month period ended June 30, 2009.

Cost of sales was $26.0 million in the six months ended June 30, 2010, which includes the direct cash cost of products sold, mine administration costs, equipment depreciation, depletion of stripping costs and stock-based compensation. Cost of sales was $12.4 million for the six months ended June 30, 2009. The increase in cost of sales for the six months ended June 30, 2010 is due to the higher sales volumes and higher unit costs.

Direct cash costs of product sold were $21.81 per tonne for the six months ended June 30, 2010 compared to $16.05 for the same period in 2009. The increase in direct cash costs is due primarily to the realignment of the open-pit which began in December 2009.

Mine administration costs per tonne decreased to $0.99 per tonne for the six months ended June 30, 2010, compared to $2.18 per tonne for the six months ended June 30, 2009. The decrease per tonne is due to the higher sales volume in 2010 and a reduction in mine administration costs.

Exploration expenses for the six months ended June 30, 2010, were $5.8 million higher than the six months ended June 30, 2009. Increased exploration expense in 2010 relates to drilling at the Soumber deposit and other greenfield targets.

6. RESULTS OF OPERATIONS (Continued)

Administration expenses for the six months ended June 30, 2010 were $14.4 million compared to $10.7 million for the six months ended June 30, 2009. Stock based compensation expense allocated to administration expenses was $4.8 million for the six months ended June 30, 2010 and $5.8 million for the same period in 2009. Other amounts included in the six months ended June 30, 2010 that account for the increase compared to 2009 are public infrastructure costs.

The administration expenses consist of the following major categories broken down for comparative purposes (see Note 6 of the Condensed Consolidated Interim Financial Statements).Legal fees for the six months ended June 30, 2010 and June 30, 2009 were for costs associated with the Company's regulatory affairs including expenses associated with corporate governance, contract negotiations, filing, registration and disclosure. Legal fees increased in 2010 due to increased regulatory requirements and corporate activity.

Corporate administration fees increased in the six months ended June 30, 2010 compared to the same period in 2009. The increase predominantly relates to additional administration costs incurred through the continued expansion of the Company's employee base, higher regulatory and filing fees, investor relations costs and administration support costs.

Professional fees are slightly higher in the six months ended June 30, 2010 compared to the same period in 2009. Professional fees include the cost of internal computer systems training and planning, technical reports for the Mongolia project and accruals for the review and audit of the Company's financial statements.

Salaries and benefits, excluding stock-based compensation costs, increased in the six months ended June 30, 2010, to $1.8 million as compared to $1.0 million for the six months ended June 30, 2009. The increase relates to additional staff in 2010.

Sustainability and community relations are costs incurred in Mongolia. Sustainability and community relations expenses were $0.3 million in the six months ended June 30, 2010. The Company is committed to contributing to communities in Mongolia and developing and maintaining a positive relationship with the various communities in which the Company operates.

Public infrastructure costs were $2.1 million in the six months ended June 30, 2010. These costs relate to the upgrading of transportation infrastructure from the Ovoot Tolgoi Mine to the Chinese border.

6. RESULTS OF OPERATIONS (Continued)

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.

Listing fees consist of legal, accounting and professional fees incurred for a secondary listing on the Hong Kong stock exchange. On January 29, 2010 the Company closed a global equity offering and commenced trading on the Main Board of the Hong Kong Stock Exchange. Listing fees incurred in 2010 were capitalized as share issue costs. Listing fees incurred in the six months ended June 30, 2009 were expensed. Normally the Company would treat all charges as share issue costs upon a successful equity fundraising, however due to the uncertainty in the timing of a possible equity financing in 2009, listing fees were expensed in the six months ended June 30, 2009.

7. NON-IFRS FINANCIAL MEASURES

($ in thousands, unless otherwise stated)

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

Cash costs is the term used by the Company to describe the cash production costs and consists of cost of product, which includes direct and indirect costs of production. The figures disclosed below are for cash cost of product sold and may differ from cash cost of product produced depending on stockpile inventory turnover.

	Three months ended June 30,		Six months ended June 30,	
	2010	**2009**	**2010**	**2009**
Cash costs, continuing operations				
Cost of sales per financial statements	**$ 13,268**	$ 9,139	**$ 25,998**	$ 12,352
Less non-cash adjustments	**(3,263)**	(2,171)	**(6,060)**	(3,026)
Total cash costs	**10,005**	6,968	**19,938**	9,326
Coal sales *(000's of tonnes)*	**449**	384	**874**	512
Total cash costs of product sold *(per tonne)*	**$ 22.30**	$ 18.13	**$ 22.80**	$ 18.23

	Three months ended June 30,		Six months ended June 30,	
	2010	**2009**	**2010**	**2009**
Cash costs, continuing operations				
Direct cash costs of product sold *(per tonne)*	**$ 21.37**	$ 16.64	**$ 21.81**	$ 16.05
Mine administration cash costs of product sold *(per tonne)*	**0.93**	1.49	**0.99**	2.18
Total cash costs of product sold *(per tonne)*	**$ 22.30**	$ 18.13	**$ 22.80**	$ 18.23

8. EXPLORATION COSTS AND DISCONTINUED OPERATIONS BY DIVISION

($ in thousands)

	Three months ended June 30,		Six months ended June 30,	
	2010	**2009**	**2010**	**2009**
Mongolian Coal Division	**$ 6,659**	$ 1,742	**$ 8,310**	$ 2,511
Indonesian Coal Division - Discontinued Operations	**-**	2,898	**-**	6,260
Total Exploration	**$ 6,659**	$ 4,640	**$ 8,310**	$ 8,771

Mongolian Coal Division

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

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

The exploration expenditures for the three months ended June 30, 2010 were $6.7 million compared to $1.7 million in the three months ended June 30, 2010. The exploration for the three months ended June 30, 2009 includes a recovery on licenses sold in June 2009. Exploration activities include drilling, trenching and geological reconnaissance. The Soumber exploration program accounts for the majority of the exploration expenditures and involves reverse circulation work, core diamond drilling, hole logging as well as a water and a geotechnical study program. The 2010 exploration expenditures also include the Company's greenfields exploration.

Indonesia Coal Division – Discontinued Operations

The sale of the Mamahak Deposit is disclosed as discontinued operations in 2009. Exploration expenditures were $2.9 million for the three months ended June 30, 2009. The Company continued exploration activities in Indonesia in 2009 until development work was suspended in October 2009.

9. FINANCE INCOME/(COSTS)

($ in thousands)

	Three months ended June 30, 2010	Three months ended June 30, 2009	Six months ended June 30, 2010	Six months ended June 30, 2009
Fair value change of embedded derivatives in convertible debenture	**$ 72,232**	$ -	**$ 70,861**	$ -
Loss on partial conversion of convertible debenture	**-**	-	**(151,353)**	-
Interest expense on convertible debenture	**(4,982)**	-	**(14,508)**	-
Interest expense on line of credit facilities	**(32)**	(345)	**(89)**	(398)
Mark to market loss on investments	**(4,555)**	-	**(5,241)**	-
Accretion of asset retirement obligation	**(19)**	(11)	**(33)**	(20)
Interest income	**649**	-	**1,224**	5
	$ 63,293	$ (356)	**$ (99,139)**	$ (413)

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

The convertible debenture is a hybrid debt instrument, containing a debt host component and three embedded derivatives. The debt host is measured at amortized cost using the effective interest method. The embedded derivatives are measured at fair value and all changes in fair value will be recognized in profit or loss immediately.

Pursuant to the debenture conversion terms, the Company had the right to call for the conversion of up to $250 million of the debenture upon achieving a public float of 25% of its common shares based on a conversion price of the lower of Cdn$11.88 and the 50-day volume-weighted average price ("VWAP"). On March 29, 2010, the Company exercised this right and completed the conversion of $250 million of the convertible debenture into 21,471,045 shares at a conversion price of $11.64 (Cdn$11.88). On March 29, 2010, the Company also settled all the accrued interest payable in shares on the converted $250 million by issuing 90,000 shares for the $1.4 million in accrued interest converted at the 50-day VWAP conversion price of $15.97 (Cdn$16.29). On April 1, 2010, the Company also settled the outstanding accrued interest payable in cash on the converted $250 million with a cash payment of $5.7 million.

9. FINANCE INCOME/(COSTS) (Continued)

For the three months ended June 30, 2010, the fair value change on the embedded derivative was a gain of $72.2 million, compared with a $1.4 million loss in the first quarter of 2010. The fair value of the embedded derivatives is driven by many factors including, share price, foreign exchange rates and volatility. During the second quarter of 2010, the share price dropped from $16.05 at March 31, 2010 to $12.50 at June 30, 2010 resulting in a significant decrease in the fair value of the embedded derivative which resulted in a gain of $72.2 million. Finance costs for the six months ended June 30, 2010 include a $151.4 million loss on partial conversion of the convertible debenture and interest expense of $14.5 for the six months ended June 30, 2010.

In 2009, as part of the sale of the Metals Division, the Company obtained a $30 million working capital credit facility from Ivanhoe. The credit facility was for a one year term with a one year discretionary extension. The credit facility was unsecured and carried an interest rate equal to LIBOR plus 750 basis points. In July 2009, the Company and Ivanhoe agreed to increase the existing working capital credit facility from $30 million to $60 million. The amended credit facility had an original maturity date of December 31, 2010, was unsecured and had an interest rate of LIBOR plus 750 basis points. The amended facility also required repayment in the event that the Company acquired additional financing from a third party source and provided for an extension fee of $1.5 million payable in the event any portion of the facility was outstanding past March 31, 2010. In November 2009, after receiving the financing from CIC, the Company repaid the $50 million in principal plus $1.6 million in accrued interest. The Company incurred interest expense of $0.3 million for the three months ended June 30, 2009 and $0.4 million for the six months ended June 30, 2009.

On December 18, 2009, the Company established a line of credit facility with Golomt Bank in Mongolia ("Bank line of credit"). The Bank line of credit is a twelve month revolving line of credit facility with a maximum draw-down available of $3.0 million. The Bank line of credit facility is used by the Company's Mongolian subsidiaries as part of their working capital management. The Company incurred interest expense of $0.03 million for the three months ended June 30, 2010 and $0.09 million for the six months ended June 30, 2010.

The mark to market loss on investments was $4.6 million and $5.2 million for the three and six months ended June 30, 2010 compared to $nil for both the three and six month period ended June 30, 2009. The mark to market loss includes a loss on the 50 million shares of Kangaroo Resources Ltd., which were received as proceeds for the sale of the Indonesia Coal Division, and certain money market instruments.

9. FINANCE INCOME/(COSTS) (Continued)

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 the three and six months ended June 30, 2010 compared to the same periods in 2009, due to higher cash balances which relate to the CIC convertible debenture and the completion of the equity financings in early 2010. Lower interest income during 2009 reflects lower average cash balances. The current economic climate has resulted in very low interest rates especially for $US denominated investments.

10. TAXES

In the three and six months ended June 30, 2010, the Company recorded current income tax expense of $0.37 million and $0.38 million respectively related to its Mongolian operations compared to $nil in the same periods in 2009. The Company believes profitable operations in Mongolia are probable and has therefore recorded a deferred income tax recovery related to deductible temporary differences and the carry forward of unused tax losses of $1.6 million in the first six months of 2010 and $nil in the first six months of 2009.

11. LIQUIDITY AND CAPITAL RESOURCES

Cash Flow Highlights

($ in thousands)

	Three months ended June 30, 2010	Three months ended June 30, 2009	Six months ended June 30, 2010	Six months ended June 30, 2009
Cash used in operating activities	**$ (27,671)**	$ (6,684)	**$ (35,135)**	$ (16,098)
Cash used in investing activities	**(29,148)**	(10,047)	**(75,915)**	(15,805)
Cash generated by financing activities	**629**	16,158	**420,840**	24,380
Effect of foreign exchange rate changes on cash	**(21)**	(26)	**72**	(11)
Increase/(decrease) in cash for the period	**(56,211)**	(599)	**309,862**	(7,534)
Cash balance, beginning of the period	**723,415**	3,405	**357,342**	10,340
Cash balance, end of the period	**$ 667,204**	$ 2,806	**$ 667,204**	$ 2,806

General market conditions

The Company remains cautious about the speed and strength of the economic recovery. Growth in China is expected to slow as China takes measures to control growth and inflation. Notwithstanding the current volatility in the global economy and the Company's caution in the short term, the Company expects demand for imported coal in China and other markets to increase into the foreseeable future. Management continues to monitor external conditions and their impact on the Company's business plans for the remainder of the year.

Cash used in operating activities

At June 30, 2010, the Company had cash resources of $667.2 million compared to cash resources of $357.3 million at December 31, 2009. At June 30, 2010, the Company also had short and long term money market investments of $77.2 million for a total of $744.4 million in cash and cash equivalents and money market investments.

Cash used in continuing operations was $27.7 million for the three months ended June 30, 2010, compared to $1.8 million for the three months ended June 30, 2009. For the six months ended June 30, 2010 cash used in continuing operations was $35.1 million compared to $7.7 million for the six months ended June 30, 2009. Cash used in discontinued operations for the three and six months ended June 30, 2010 was $nil compared to $4.8 million and $8.4 million for the three and six months ended June 30, 2009.

11. LIQUIDITY AND CAPITAL RESOURCES (Continued)

In the three months ended June 30, 2010, the Company earned net income from continuing operations before tax of $52.7 million. In the six months ended June 30, 3010, the Company incurred a net loss from continuing operations before tax of $116.2 million. This compares to a net loss from continuing operations before tax for the three and six months ended June 30, 2009 of $5.1 million and $11.8 million, respectively. Included in the net income for the three months ended June 30, 2010 is a $72.2 million gain on the fair value change of the embedded derivatives in the convertible debenture. The net loss for the six months ended June 30, 2010 includes a $151.4 million loss on the partial conversion of the convertible debenture. In 2010, the Company recorded revenue of $17.7 million for the three months ended June 30, 2010 and $31.6 million for the six months ended June 30, 2010 compared to $10.7 million and $14.2 million for the comparative periods in 2009. With the increased activities at the Ovoot Tolgoi site and the operations in Mongolia, accounts receivable, inventory, and accounts payable increased during the six months ended June 30, 2010.

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

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

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 2010. The increase primarily relates to advances for supplies inventory.

11. LIQUIDITY AND CAPITAL RESOURCES (Continued)

Coal and supplies inventory have increased to $25.0 million at June 30, 2010 from $16.4 million at December 31, 2009 due to increased activity and more mobile equipment on site. Coal and supplies inventory is valued at the lower of cost and net realizable value. Coal inventory cost of $8.3 million at June 30, 2010 and $9.6 million at December 31, 2009 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 0.35 million tonnes of coal inventory at June 30, 2010, 0.39 million tonnes at December 31, 2009 and 0.69 million tonnes at June 30, 2009.

Accounts payable have increased slightly in the six months ended June 30, 2010. Increased activity in Mongolia has been offset by the lower corporate balances.

Cash used for investing activities

Cash used for investing activities was $29.1 million for the three months ended June 30, 2010, compared to $10.0 million for the same period in 2009. For the six months ended June 30, 2010 cash used for investing activities was $75.9 million compared to $15.8 million for the six months ended June 30, 2009.

The Company's investment in property, plant and equipment was higher during 2010 as the Company prepares to ramp up production. Deposits for further mining equipment are included as plant and equipment. The Company incurred expenditures in the three and six months ended June 30, 2010 for mobile and mining equipment, tires and deferred stripping in Mongolia. The Company began stripping the Sunrise pit in the second quarter of 2010. The Company incurred expenditures during the three and six months ended June 30, 2009 for tires, mobile and mining equipment.

In the first quarter of 2010, after the receipt of the proceeds from the equity financing, the Company invested $30.0 million in longer term money market instruments. During the first quarter of 2010, short term money market investments of $15.0 million also matured.

Interest income will increase or decrease depending on the cash position and interest rates. Interest income was higher in the three and six months ended June 30, 2010 compared to the three and six months ended June 30, 2009 due to higher cash balances which related directly to the completion of the equity financings and the proceeds from the CIC convertible debenture. The current economic climate has resulted in very low interest rates especially for $US denominated investments.

11. LIQUIDITY AND CAPITAL RESOURCES (Continued)

Cash provided by financing activities

On January 29, 2010, the Company announced that it had closed the global equity offering of 27 million common shares of the Company at a price of Cdn$17.00 per common share, for gross proceeds of $437.4 million.

On February 26, 2010, the Company announced that Citigroup Global Markets Canada Inc. and Macquarie Capital Markets Canada, representatives of the Canadian underwriters of the Company's global equity offering, partially exercised their over-allotment option and purchased an additional 228,100 common shares of the Company at a price of Cdn$17.00 per share for gross proceeds of $3.7 million.

On December 18, 2009, the Company established a line of credit facility with Golomt Bank in Mongolia. The bank line of credit facility is a twelve month revolving line of credit facility with a maximum draw-down available of $3.0 million. The line of credit facility is secured by a charge over certain equipment held by SouthGobi Sands LLC. The line of credit facility is used by the Company's Mongolian subsidiaries as part of their working capital management. During the six months ended June 30 2010, the Company had drawings of $23.1 million and repayments of $23.4 million. The principal balance outstanding as at June 30, 2010 was $2.7 million.

11. LIQUIDITY AND CAPITAL RESOURCES (Continued)

On December 31, 2008, the Company announced the sale of its Metals Division to Ivanhoe for $3.0 million and other non-cash consideration. As part of the sale transaction, the Company obtained a $30.0 million credit facility from Ivanhoe. The credit facility was for a one year term with a one year discretionary extension. The credit facility was unsecured and carried an interest rate equal to LIBOR plus 750 basis points. In July 2009, the Company and Ivanhoe agreed to increase the existing working capital credit facility from $30.0 million to $60.0 million. The amended credit facility had an original maturity date of December 31, 2010, was unsecured and had an interest rate of LIBOR plus 750 basis points. The amended facility also required repayment in the event that the Company acquired additional financing from a third party source and provided for an extension fee of $1.5 million payable in the event any portion of the facility was outstanding past March 31, 2010. In November 2009, after receiving the financing from CIC, the Company repaid the $50.0 million in principal plus $1.6 million in interest expense. During the six months ended June 30, 2009, the Company's drawings under the line of credit were $24.0 million.

Liquidity, Financing and Working Capital Resources

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

In November 2009, the Company entered into a financing agreement with a wholly owned subsidiary of CIC for $500.0 million in the form of a secured, convertible debenture bearing interest at 8.0% with a maximum term of 30 years. The convertible debenture is secured by a charge over the Company's assets and certain subsidiaries. The financing is required primarily to support the accelerated investment program in Mongolia and up to $120.0 million of the financing may also be used for working capital, repayment of debt due on funding, general and administrative expense and other general corporate purposes.

On March 29, 2010, the Company exercised the right to call for the conversion of up to $250.0 million of the convertible debenture into 21,471,045 shares at a conversion price of $11.64 (Cdn$11.88). Following the conversion CIC through its indirect wholly owned subsidiary, owns approximately 13% of the Company.

11. LIQUIDITY AND CAPITAL RESOURCES (Continued)

On January 29, 2010, the Company announced that it had closed the global equity offering of 27 million common shares of the Company at a price of Cdn$17.00 per common share, for gross proceeds of $437.4 million. On February 26, 2010, the Company announced a partial exercised of the over-allotment option and issued an additional 228,100 common shares of the Company at a price of Cdn$17.00 per share for gross proceeds of $3.7 million.

The Company plans to use the net proceeds from the financings above to carry out the following activities:

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

To date, the Company's actual use of such proceeds has not varied from the anticipated use of proceeds set out above.

On June 8, 2010, the Company announced that its Board of Directors authorized a share repurchase program to purchase up to 2.5 million common shares of the Company on each or either of the Toronto Stock Exchange and the Hong Kong Stock Exchange, in aggregate representing approximately up to 5 million common shares of the Company. As of August 11, 2010, the Company had not repurchased any common shares.

As at June 30, 2010, the Company's gearing ratio was 0.29 (December 31, 2009: 0.97) which was calculated based on the Company's long term liabilities to total assets.

12. 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 $0.88 million for the six months ended June 30, 2010 and June 30, 2009 respectively.

On December 31, 2008, the Company announced the sale of the Metals Division to Ivanhoe for $3.0 million and other non-cash consideration. The Metals Division consisted of a series of base and precious metal exploration properties in Mongolia and Indonesia, related assets, employees and contracts. As part of the sale transaction, the Company obtained a credit facility from Ivanhoe, which allowed the Company to receive loan advances from Ivanhoe to an aggregate maximum of $30.0 million. The credit facility was for a one year term with a one year discretionary extension. The credit facility was unsecured and carried an interest rate equal to LIBOR plus 750 basis points.

In July 2009, the Company and Ivanhoe agreed to increase the existing working capital credit facility from $30.0 million to $60.0 million. The amended credit facility had an original maturity date of December 31, 2010, was unsecured and had an interest rate of LIBOR plus 750 basis points. The amended facility also required repayment in the event that the Company acquires additional financing from a third party source and provided for an extension fee of $1.5 million payable in the event any portion of the facility was outstanding past March 31, 2010. In November 2009, the Company after receiving the financing from CIC repaid the $50.0 million in principal plus $1.6 million in accrued interest.

13. EMOLUMENT POLICY

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

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

The Company has also adopted a share option plan as incentive to directors and eligible employees. Details of the plan are set out in Note 18 of the Condensed Consolidated Interim Financial Statements.

As at June 30, 2010, the Company employed 421 employees.

14. OUTSTANDING SHARE DATA

The Company is authorized to issue an unlimited number of common shares without par value and an unlimited number of preferred shares without par value. As at August 11, 2010, 183,950,767 common shares were issued and outstanding. There are also incentive stock options outstanding that are exercisable to acquire 6,744,862 unissued common shares. There are no preferred shares outstanding.

As at August 11, 2010, Ivanhoe, directly and indirectly, owned 105,332,155 common shares representing approximately 57% of the issued and outstanding common shares of SouthGobi.

15. 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.

16. RISK FACTORS

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

Material risks and uncertainties affecting SouthGobi, their potential impact and the Company's principal risk management strategies are substantially unchanged from those disclosed in the Company's MD&A for the year ended December 31, 2009, which is available at www.sedar.com.

17. OUTLOOK

It is difficult to reliably forecast commodity prices and customer demand for the Company's products; however the Company's sales and marketing efforts continue to provide positive results. There is still informal evidence that suggests Mongolia will set a new record for coal shipments to China in 2010 and become a significant supplier of China's coal needs.

For the quarter ended June 30, 2010, revenue ($17.7 million) and income from mine operations ($4.4 million) were records for the Company. Also, the Company recorded its highest average realized selling price for the quarter ($43 per tonne).

From an operating perspective, the Company is encountering two issues that will impact its short term outlook. Firstly, there will be proportionately less of the better quality coal coming from the #5 seam in the near-term mine plan. Secondly, the Company is currently experiencing areas of higher sulphur than originally anticipated in mine plans and studies. Some of the higher sulphur coal will not be attractive to customers in its current form and may need to be stockpiled until appropriate processing is in place or blending opportunities arise. With these issues in mind, the Company doesn't expect the rate of coal sales volumes to be substantially different for the remainder of 2010 than for the six months ended June 30, 2010.

17. OUTLOOK (Continued)

SouthGobi continues to increase pricing of its coals. Sales contracts for the third quarter of 2010 reflect on average in excess of a further 10% increase in pricing for the premium coal product. However, the Company anticipates the sales mix to be more heavily weighted to lower value products in the third quarter of 2010 with a potential small decline in overall average selling price.

With the full commissioning of the second mining fleet, capacity to move material is now much higher than for the first half of 2010. For example, in excess of one million bank cubic meters of waste was mined in the month of July. SouthGobi has received five Terex MT4400 (218 tonne) haul trucks for the third fleet in addition to the four Terex MT4400 haul trucks commissioned for the second fleet. Those trucks are being assembled on site at Ovoot Tolgoi Mine. The hydraulic excavator has been shipped from Europe and is expected to be delivered in late-2010 along with various other pieces of ancillary equipment.

SouthGobi continues to assess fleet requirements at the Ovoot Tolgoi Mine including the consideration of adding additional equipment to expand capacity beyond current plans.

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

- Projects are strategically located close to China;
- Substantial and growing resources and reserves;
- Produce premium quality coals;
- Low cost structure due to favorable geographic and geological conditions;
- Strong financial profile after the financings in late 2009 and early 2010;
- Established production with strong growth potential through future expansion of existing mine capacity and development of the Company's priority assets; and
- Experienced management team with strong skills in mining, exploration and marketing and are able to leverage the expertise, experience and relationships of its principal shareholder, Ivanhoe.

17. OUTLOOK (Continued)

Overview and Objectives

The Company continues to focus its efforts on mining, development and exploration of coking and thermal coal products in Mongolia for supply of quality products to customers in China. As the Company looks forward through the balance of 2010, the Company is encouraged by the overall long term demand for our products. There are many positive developments in Mongolia, which provide further support that the mining sector will develop its resource base for long term growth. The Company is making progress with its sales and marketing efforts, continuing to focus on efficiency and prudent financial management and intends to manage production levels to meet anticipated demand for the Company's products.

The Company's objectives for 2010 remain unchanged from the previous quarter and are as follows:

- **Grow Ovoot Tolgoi Mine** – The additional capacity of the new mining fleets should support growth in coal availability and sales for 2010 over 2009, and the future.
- **Continue to develop regional infrastructure** – The Company's immediate priority centers on improving roads in the area around Ovoot Tolgoi Mine and contributing to new road development.
- **Advancing the Soumber deposit** – SouthGobi intends to further define the deposit with continued exploration work whilst also substantially advancing the feasibility, planning and licensing for a mine at Soumber.
- **Value-adding/upgrading coal** – The Company has commenced construction of a basic coal-handling facility at Ovoot Tolgoi Mine and anticipates commissioning that processing facility in early 2011.
- **Exploration** – Further green fields exploration will take place, with the Company planning an exploration budget in the order of $10-20 million.
- **Continuing to focus on production safety, environmental protection, operational excellence and community relations.**

August 11, 2010