SouthGobi Resources Ltd.
Condensed Consolidated Interim Financial Statements

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

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SOUTHGOBI RESOURCES LTD.

Condensed Consolidated Interim Statements of Comprehensive Income

(Unaudited)

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

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

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

SOUTHGOBI RESOURCES LTD.

Condensed Consolidated Interim Statements of Financial Position

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

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

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

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

APPROVED BY THE BOARD:

"Andre Deepwell"
Director

"Pierre Lebel"
Director

SOUTHGOBI RESOURCES LTD.

Condensed Consolidated Interim Statements of Changes in Equity

(Unaudited)

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

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

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

SOUTHGOBI RESOURCES LTD.

Condensed Consolidated Interim Statements of Cash Flows

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

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

Supplemental cash flow information (Note 19)

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

1. CORPORATE INFORMATION AND GOING CONCERN

SouthGobi Resources Ltd. is a publicly listed company incorporated in Canada with limited liability under the legislation of the Province of British Columbia and its shares are listed on the Toronto Stock Exchange (Symbol: SGQ) and Stock Exchange of Hong Kong (Symbol: 1878). The company, together with its subsidiaries (collectively referred to as the "Company"), is an integrated coal mining, development and exploration company. At June 30, 2015, Novel Sunrise Investments Limited owned approximately 30% of the outstanding Common Shares of the Company while Turquoise Hill Resources Ltd. ("Turquoise Hill") owned approximately 23% of the outstanding Common Shares of the Company. Turquoise Hill is controlled by Rio Tinto plc ("Rio Tinto").

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

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

Going concern assumption

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

1. CORPORATE INFORMATION AND GOING CONCERN (CONTINUED)

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

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

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

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

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

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

2. BASIS OF PREPARATION

2.1 Statement of compliance

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

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

2.2 Basis of presentation

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

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

2.3 Adoption of new and revised standards and interpretations

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

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

2. BASIS OF PREPARATION (CONTINUED)

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

2.4 Significant accounting judgments and estimates

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

Liquidity and the going concern assumption

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

2. BASIS OF PREPARATION (CONTINUED)

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

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

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

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

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

2. BASIS OF PREPARATION (CONTINUED)

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

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

Ovoot Tolgoi Mine cash generating unit

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

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

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

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

Key sensitivities in the valuation model are as follows:

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

2. BASIS OF PREPARATION (CONTINUED)

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

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

Investment in RDCC LLC

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

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

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

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

Key sensitivities in the valuation model are as follows:

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

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

2. BASIS OF PREPARATION (CONTINUED)

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

3. SEGMENTED INFORMATION

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

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

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

3. SEGMENTED INFORMATION (CONTINUED)

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

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

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

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

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

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

4. COST OF SALES

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

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

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

5. OTHER OPERATING EXPENSE

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

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

6. ADMINISTRATION EXPENSES

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

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

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

7. FINANCE COSTS AND INCOME

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

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

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

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

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

8. TRADE AND OTHER RECEIVABLES

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

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

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

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

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

8. TRADE AND OTHER RECEIVABLES (CONTINUED)

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

9. INVENTORIES

The Company's inventories consist of the following amounts:

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

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

10. PROPERTY, PLANT AND EQUIPMENT

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

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

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

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

11. LONG TERM INVESTMENTS

The Company's investments consist of the following amounts:

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

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

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

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

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

12. TRADE AND OTHER PAYABLES

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

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

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

13. INTEREST-BEARING BORROWING

Turquoise Hill Loan Facility

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

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

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

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

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

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

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

Interim Funding Loan Commitment

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

13. INTEREST-BEARING BORROWING (CONTINUED)

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

Revolving Loan Commitment

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

14. CONVERTIBLE DEBENTURE

14.1 Key commercial terms

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

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

The key commercial terms of the financing include:

- Interest - 8% per annum (6.4% payable semi-annually in cash and 1.6% payable annually in the Company's Common Shares, where the number of shares to be issued is calculated based on the 50-day volume-weighted average price ("VWAP"));
- Term - Maximum of 30 years;
- Security - First charge over the Company's assets, including shares of its material subsidiaries. An event of default on the convertible debenture can be triggered as a result of certain encumbrances on the Company's assets (Note 21.3).Conversion price - The conversion price is set as the lower of Cdn$11.88 or the 50-day VWAP at the date of conversion, with a floor price of Cdn$8.88 per share;

14. CONVERTIBLE DEBENTURE (CONTINUED)

- CIC's conversion right - CIC has the right to convert the convertible debenture, in whole or in part, into Common Shares twelve months after the date of issue;
- Company's normal conversion right – After sixty months from the issuance date, and when the conversion price is greater than Cdn$10.66, the Company is entitled to force conversion of the outstanding convertible debenture, in whole or in part, into Common Shares at the conversion price;
- Representation on the Company's Board - While the convertible debenture is outstanding, or while CIC has a minimum 15% direct or indirect stake in the Company, CIC has the right to nominate one director to the Company's Board of Directors. The Company currently has nine Board of Directors members of which none were elected by CIC;
- Voting restriction - CIC has agreed that it will not have any voting rights in the Company beyond 29.9% if CIC ever acquires ownership of such a shareholder stake;
- Pre-emption rights - While the convertible debenture is outstanding, or while CIC has a 15% direct or indirect stake in the Company, CIC has certain pre-emption rights on a pro-rata basis to subscribe for any new shares to be allotted and issued by the Company for the period which the convertible debenture is outstanding. The pre-emption rights will not apply to new shares issued pursuant to pro-rata public equity offerings made to all shareholders, exercise of stock options and shares issued to achieve a 25% public float;
- Right of first offer - While a portion of the convertible debenture is outstanding, or while CIC has a 15% direct or indirect stake in the Company, CIC has the right of first offer for any direct and indirect sale of Turquoise Hill's ownership stake in the Company; and
- Registration rights - CIC has registration rights under applicable Canadian provincial securities laws in connection with the Common Shares issuable upon conversion of the convertible debenture.

14.2 Debt host and embedded derivatives

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

The embedded derivatives were valued upon initial measurement and subsequent periods using a Monte Carlo simulation valuation model. A Monte Carlo simulation model is a valuation model that relies on random sampling and is often used when modeling systems with a large number of inputs and where there is significant uncertainty in the future value of inputs and where the movement of the inputs can be independent of each other. Some of the key inputs used by the Company in its Monte Carlo simulation include: the floor and ceiling conversion prices, the Company's Common Share price, the risk-free rate of return, expected volatility of the Company's Common Share price, forward foreign exchange rate curves (between the Cdn$ and U.S. Dollar) and spot foreign exchange rates.

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

14. CONVERTIBLE DEBENTURE (CONTINUED)

14.3 Valuation assumptions

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

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

14.4 Presentation

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

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

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

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

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

14. CONVERTIBLE DEBENTURE (CONTINUED)

The convertible debenture balance consists of the following amounts:

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

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

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

15. EQUITY

15.1 Share capital

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

15.2 Accumulated deficit and dividends

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

15.3 Mandatory convertible units

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

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

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

16. SHARE-BASED PAYMENTS

16.1 Stock option plan

The Company has a stock option plan which permits the Board of Directors of the Company to grant options to acquire Common Shares of the Company at the volume weighted average closing price for the five days preceding the date of grant. The Company is authorized to issue stock options for a maximum of 10% of the issued and outstanding Common Shares pursuant to the stock option plan. The stock option plan permits the Board of Directors of the Company to set the terms for each stock option grant; however, the general terms of stock options granted under the plan include a maximum exercise period of 5 years and a vesting period of 3 years with 33% of the grant vesting on the first anniversary of the grant, 33% vesting on the second anniversary of the grant and 34% vesting on the third anniversary of the grant.

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

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

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

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

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

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

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

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

16. SHARE-BASED PAYMENTS (CONTINUED)

16.2 Outstanding stock options

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

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

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

	Options Outstanding			Options Exercisable		
Exercise price (Cdn$)	Options outstanding	Weighted average exercise price (Cdn$)	Weighted average remaining contractual life (years)	Options outstanding and exercisable	Weighted average exercise price (Cdn$)	Weighted average remaining contractual life (years)
0.65 to 1.92	**1,760**	**$ 0.81**	**4.11**	**174**	**$ 1.55**	**2.81**
6.16 to 9.43	**290**	**8.19**	**1.35**	**290**	**8.19**	**1.35**
12.58	**282**	**12.58**	**0.12**	**282**	**12.58**	**0.12**
	2,332	**$ 3.15**	**3.29**	**746**	**$ 8.30**	**1.23**

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

17. FAIR VALUE MEASUREMENTS

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

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

- Level 1 fair value measurements are those derived from quoted prices in active markets for identical assets or liabilities;
- Level 2 fair value measurements are those derived from inputs other than quoted prices included within Level 1, that are observable either directly or indirectly;
- Level 3 fair value measurements are those derived from valuation techniques that include inputs that are not based on observable market data.

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

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

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

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

18. RELATED PARTY TRANSACTIONS

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

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

18.1 Related party expenses

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

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

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

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

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

18. RELATED PARTY TRANSACTIONS (CONTINUED)

18.2 Related party expenses recoveries

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

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

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

18.3 Related party liabilities

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

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

19. SUPPLEMENTAL CASH FLOW INFORMATION

19.1 Net change in non-cash working capital items

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

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

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

20. COMMITMENTS FOR EXPENDITURE

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

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

21. CONTINGENCIES

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

21.1 Governmental and regulatory investigations

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

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

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

21. CONTINGENCIES (CONTINUED)

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

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

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

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

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

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

21. CONTINGENCIES (CONTINUED)

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

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

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

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

21. CONTINGENCIES (CONTINUED)

21.2 Internal investigations

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

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

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

21.3 Mongolian IAAC investigation

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

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

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

21. CONTINGENCIES (CONTINUED)

21.4 Class action lawsuit

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

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

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

21.5 Toll wash plant agreement with Ejin Jinda

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

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

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

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

21. CONTINGENCIES (CONTINUED)

21.6 Special Needs Territory in Umnugobi

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

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

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

21.7 Commercial arbitration in Hong Kong

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

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

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

21. CONTINGENCIES (CONTINUED)

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

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

21.8 Notice of claim by former Chief Executive Officer

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

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

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

21.9 Tax legislation

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

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

21. CONTINGENCIES (CONTINUED)

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

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

22. SUBSEQUENT EVENTS

Novel Sunrise change in ownership

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

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

ADDITIONAL STOCK EXCHANGE INFORMATION

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

A1. TAXATION ON PROFITS

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

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

A2. FINANCIAL INSTRUMENTS

Cash

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

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

Exposure to fluctuations in foreign exchange rates

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

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

A3. COMPLIANCE WITH THE CODE ON CORPORATE GOVERNANCE PRACTICES

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

A4. COMPLIANCE WITH MODEL CODE

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

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

A5. DIRECTORS' INTERESTS IN SHARES AND SHARE OPTIONS

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

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

Shares [(i)]

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

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

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

***Options* (i)**

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

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