SouthGobi Resources Ltd.
Condensed Consolidated Interim Financial Statements

March 31, 2018
(Expressed in U.S. Dollars)
(Unaudited)

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SOUTHGOBI RESOURCES LTD.

Condensed Consolidated Interim Statement of Comprehensive Income

(Unaudited)

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

		Three months ended March 31,	
	Notes	**2018**	**2017**
Revenue	4	**$ 23,223**	$ 25,254
Cost of sales	6	**(16,507)**	(23,759)
Gross profit		**6,716**	1,495
Other operating expenses	7	**(1,338)**	(3,208)
Administration expenses		**(2,377)**	(2,385)
Evaluation and exploration expenses		**(124)**	(29)
Profit/(loss) from operations		**2,877**	(4,127)
Finance costs	8	**(6,006)**	(5,715)
Finance income	8	**258**	4
Share of earnings of a joint venture	14	**340**	266
Loss before tax		**(2,531)**	(9,572)
Current income tax expense	9	**(929)**	(45)
Net loss attributable to equity holders of the Company		**(3,460)**	(9,617)
Other comprehensive income to be reclassified to profit or loss in subsequent periods			
Exchange differences on translation of foreign operation		**(3,328)**	259
Net comprehensive loss attributable to equity holders of the Company		**$ (6,788)**	$ (9,358)
Basic and diluted loss per share		**$ (0.01)**	$ (0.04)

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

SOUTHGOBI RESOURCES LTD.

Condensed Consolidated Interim Statement of Changes in Equity

(Unaudited)

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

	Notes	As at March 31, 2018	As at December 31, 2017
Assets			
Current assets			
Cash and cash equivalents		**$ 11,265**	$ 6,471
Trade and other receivables	11	**19,307**	16,486
Notes receivables		**11,498**	12,520
Inventories	12	**33,235**	36,389
Prepaid expenses and deposits		**7,430**	6,286
Total current assets		**82,735**	78,152
Non-current assets			
Properties for resale		**$ 8,906**	$ 8,906
Property, plant and equipment	13	**153,297**	152,457
Investment in a joint venture	14	**21,142**	21,052
Total non-current assets		**183,345**	182,415
Total assets		**$ 266,080**	$ 260,567
Equity and liabilities			
Current liabilities			
Trade and other payables	15	**$ 81,239**	$ 79,219
Deferred revenue		**32,769**	27,644
Provision for commercial arbitration	16	**14,108**	13,884
Interest-bearing borrowings	17	**7,107**	7,352
Convertible debenture	18	**123,047**	116,374
Total current liabilities		**258,270**	244,473
Non-current liabilities			
Interest-bearing borrowings	17	**89**	341
Decommissioning liability		**5,283**	5,213
Total non-current liabilities		**5,372**	5,554
Total liabilities		**263,642**	250,027
Equity			
Common shares	19	**1,098,625**	1,098,623
Share option reserve		**52,479**	52,463
Exchange reserve		**(8,065)**	(4,737)
Accumulated deficit	19	**(1,140,601)**	(1,135,809)
Total equity		**2,438**	10,540
Total equity and liabilities		**$ 266,080**	$ 260,567
Net current liabilities		**$ (175,535)**	$ (166,321)
Total assets less current liabilities		**$ 7,810**	$ 16,094

Corporate information and going concern (Note 1), commitments for expenditure (Note 23) and contingencies (Note 24)

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

APPROVED BY THE BOARD:

"Mao Sun"
Director

"Yulan Guo"
Director

SOUTHGOBI RESOURCES LTD.

Condensed Consolidated Interim Statement 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	Exchange fluctuation reserve	Accumulated deficit	Total
Balances, January 1, 2017	257,698	$ 1,094,619	$ 52,340	$ (5,158)	$ (1,095,788)	$ 46,013
Shares issued for:						
Interest settlement on convertible debenture	14,892	4,000	-	-	-	4,000
Employee share purchase plan	2	-	-	-	-	-
Share-based compensation charged to operations	-	-	37	-	-	37
Net loss for the period	-	-	-	-	(9,617)	(9,617)
Exchange differences on translation of foreign operations	-	-	-	259	-	259
Balances, March 31, 2017	272,592	$ 1,098,619	$ 52,377	$ (4,899)	$ (1,105,405)	$ 40,692
Balances, January 1, 2018	**272,607**	**$ 1,098,623**	**$ 52,463**	**$ (4,737)**	**$ (1,135,809)**	**$ 10,540**
Change in accounting policy due to IFRS 9	**-**	**-**	**-**	**-**	**(1,332)**	**(1,332)**
Restated balances, January 1, 2018	**272,607**	**$ 1,098,623**	**$ 52,463**	**$ (4,737)**	**$ (1,137,141)**	**$ 9,208**
Shares issued for:						
Employee share purchase plan	**17**	**2**	**-**	**-**	**-**	**2**
Share-based compensation charged to operations	**-**	**-**	**16**	**-**	**-**	**16**
Net loss for the period	**-**	**-**	**-**	**-**	**(3,460)**	**(3,460)**
Exchange differences on translation of foreign operations	**-**	**-**	**-**	**(3,328)**	**-**	**(3,328)**
Balances, March 31, 2018	**$ 272,624**	**$ 1,098,625**	**$ 52,479**	**$ (8,065)**	**$ (1,140,601)**	**$ 2,438**

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

SOUTHGOBI RESOURCES LTD.

Condensed Consolidated Interim Statement of Cash Flows

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

		Three months ended March 31,	
	Notes	**2018**	**2017**
Operating activities			
Loss before tax		**$ (2,531)**	$ (9,572)
Adjustments for:			
Depreciation and depletion		**4,645**	9,874
Share-based compensation	20	**16**	37
Finance costs	8	**6,006**	5,715
Finance income	8	**(258)**	(4)
Share of earnings of a joint venture	14	**(340)**	(266)
Interest paid		**(591)**	(4,081)
Income tax paid		**(131)**	-
Unrealized foreign exchange loss		**-**	300
Loss on disposal of property, plant and equipment	7	**67**	-
Penalty on late settlement of trade payables	7	**104**	268
Provision for commercial arbitration	16	**224**	-
Provision for doubtful trade and other receivables	11	**1,103**	-
Impairment of inventories	12	**-**	2,331
Operating cash flows before changes in non-cash working capital items		**8,314**	4,602
Net change in non-cash working capital items	22	**4,108**	4,560
Cash generated from operating activities		**12,422**	9,162
Investing activities			
Expenditures on property, plant and equipment		**(7,898)**	(1,390)
Proceeds from disposal of property, plant and equipment		**320**	-
Interest received		**10**	4
Dividend from a joint venture	14	**488**	422
Cash used in investing activities		**(7,080)**	(964)
Financing activities			
Proceeds from issuance of common shares, net of issue costs		**2**	-
Repayment of interest-bearing loans		**(523)**	(3,894)
Cash used in financing activities		**(521)**	(3,894)
Effect of foreign exchange rate changes on cash		**(27)**	3
Increase in cash		**4,794**	4,307
Cash and cash equivalents, beginning of period		**6,471**	966
Cash and cash equivalents, end of period		**$ 11,265**	$ 5,273

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 Hong Kong Stock Exchange (Symbol: 1878). The company, together with its subsidiaries (collectively referred to as the “Company”), is an integrated coal mining, development and exploration company. At March 31, 2018, Land Breeze II S.a.r.l., a wholly-owned subsidiary of China Investment Corporation (“CIC”) owned approximately 23.8% of the outstanding common shares of the Company. Novel Sunrise Investments Limited ("Novel Sunrise"), a wholly-owned subsidiary of China Cinda (HK) Investments Management Company Limited (“Cinda”) and Voyage Wisdom Limited each owned approximately 17.0% and 9.5% of the outstanding common shares of the Company, respectively.

The Company owns the following significant coal projects in Mongolia: the Ovoot Tolgoi open pit producing coal mine (“Ovoot Tolgoi Mine”) and the following 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 registered and records office of the Company is located at 20th Floor, 250 Howe Street, Vancouver, British Columbia, Canada, V6C 2G8. The head office and principal place of business of the Company is located at 1150 – 355 Burrard Street, Vancouver, British Columbia, Canada, V6C 2G8.

Going concern assumption

The Company’s condensed consolidated interim financial statements have been prepared on a going concern basis which assumes that the Company will continue operating until at least March 31, 2019 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 transactions to provide it with additional liquidity.

Several adverse conditions and material uncertainties cast significant doubt upon the going concern assumption. The Company had a working capital deficiency (excess current liabilities over current assets) of $175,535 as at March 31, 2018 compared to $166,321 of working capital deficiency as at December 31, 2017. Included in the working capital deficiency at March 31, 2018 are significant obligations, which include the obligation to pay CIC under the deferral agreement dated June 12, 2017 (the “June 2017 Deferral Agreement”) in which the Company was required to pay $9,731 of cash interest and associated costs on November 19, 2017 (the “June 2017 Deferral Agreement Payment”). In addition, pursuant to the terms of CIC Convertible Debenture, the Company was required to pay $8,066 of anniversary cash interest on November 19, 2017 (the “November Interest Payment” and together with the June 2017 Deferral Agreement Payment, the “November 19th Payments”) and will be required to pay $7,934 of cash interest on May 19, 2018 (the “May 2018 Payment”). As of the date hereof, the Company expects that it will be unable to pay the May 2018 Payment to CIC on the due date. The Company is in discussion with CIC for a deferral of the November 19th Payments and the May 2018 Payment; however, there can be no assurance that a favorable outcome will be reached. Accordingly the principal amount outstanding and all accrued and unpaid interest and other amounts owing under the CIC Convertible Debenture and the June 2017 Deferral Agreement would immediately become due and payable in the event that CIC provides notice to the Company.

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

1. CORPORATE INFORMATION AND GOING CONCERN (CONTINUED)

Pursuant to a confidential partial award (final except as to costs) (“Arbitration Award”) with respect to an the commercial arbitration on January 10, 2018 involving SouthGobi Sands LLC (“SGS”), a subsidiary of the Company, and First Concept Industrial Group Limited (“First Concept”), SGS has been ordered to repay the sum of $11,500 to First Concept, together with accrued interest at a simple interest rate of 6% per annum from the date which the prepayment was made until the date of the Arbitration Award, and then at a simple interest rate of 8% per annum until full payment. On March 23, 2018, SGS received a notice from First Concept demanding payment of the full amount of the Arbitration Award, together with the accrued interest thereon, by no later than March 30, 2018, otherwise First Concept intends to commence enforcement proceedings against SGS in respect of the Arbitration Award. On May 10, 2018, SGS received a notice from First Concept advising that First Concept has obtained a court order dated April 27, 2018 from the High Court of Hong Kong granting leave to First Concept to enforce the Arbitration Award against SGS in Hong Kong. The Company is consulting with its independent litigation counsel regarding this matter. However, as SGS does not have any material assets, properties or place of business in Hong Kong, the Company is of the view that this court order will have little or no immediate impact on its ongoing operations. In the event that First Concept applies to enforce the Arbitration Award against SGS through judicial measures in courts of Mongolia or any other jurisdiction in which SGS has assets or properties, the Company intends to take appropriate steps to respond to such enforcement proceedings in the best interests of the Company through independent litigation counsel which has been retained by the Company for this purpose. If First Concept is successful in enforcing the Arbitration Award, the Company may not be able to re-pay the sum of $11,500 and the associated interest. In such case, this will represent another event of default under the CIC Convertible Debenture and CIC would have another basis to declare the full principal and accrued interest owing thereunder immediately due and payable. Such an event of default under the CIC Convertible Debenture or the Company’s inability to re-pay the sum of $11,500 and associated interest to First Concept could result in voluntary or involuntary proceedings involving the Company (including bankruptcy).

Further, the trade and other payables of the Company continue to accumulate due to liquidity constraints. The aging profile of the trade and other payables has risen as compared to that as at December 31, 2017, as follows:

	As at	
	March 31, 2018	**December 31, 2017**
Less than 1 month	**$ 18,762**	$ 20,664
1 to 3 months	**15,414**	16,132
3 to 6 months	**14,556**	8,825
Over 6 months	**32,507**	33,598
Total trade and other payables	**$ 81,239**	$ 79,219

The Company may not be able to settle all trade and other payables on a timely basis, while continuing postponement in settling the trade payables may impact the mining operations of the Company and result in potential lawsuits and/or bankruptcy proceedings being filed against the Company. No such lawsuits or proceedings are pending as at May 14, 2018.

1. CORPORATE INFORMATION AND GOING CONCERN (CONTINUED)

The Company also has other current liabilities, which require settlement in the short-term, including: the $1,514 undiscounted balance of the Turquoise Hill Resources Limited (“Turquoise Hill”) shareholder loan (“TRQ Loan”) and the principal amount of equipment loan of $2,393 and associated interest due in August 2018.

In the fourth quarter of 2016, the Company initiated a plan to change the existing product mix to higher value and higher margin outputs by washing certain grades of coal in order to produce more premium semi-soft coking coal and to initiate more processing of the lower grades of coal in order to reduce the ash content and improve the selling price and margins on its thermal coal product. The construction of the wash plant was substantially completed in 2017, however commencement of washing has been delayed to the second quarter of 2018.

The current mine plan incorporates the coal washing and processing systems and contemplates significantly higher volumes of production in order to complement the Company’s new product mix and sales volume targets. Such plans will require a significant level of stripping activities over the next two years and certain capital expenditures to achieve the designed production outputs. Such expenditures and other working capital requirements will require the Company to seek additional financing in the form of finance leases, debt or equity.

There is no guarantee that the Company will be able to successfully execute the measures mentioned above and 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 March 31, 2019, then the Company is unlikely to have sufficient capital resources or cash flows from mining operations in order to satisfy its current ongoing obligations and future contractual commitments. 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.

Unless the Company acquires additional sources of financing and/or funding in the short term, the ability of the Company to continue as a going concern is threatened. If the Company is unable to continue as a going concern, it may be forced to seek relief under applicable bankruptcy and insolvency legislation.

As of the date hereof, the Company is in default under the CIC Convertible Debenture and the TRQ Loan. Pursuant to the terms of the CIC Convertible Debenture, CIC may, in its discretion, provide notice to the Company and declare all principal, interest and other amounts owing under the CIC Convertible Debenture immediately due and payable, and take steps to enforce payment thereof. Pursuant to the terms of the TRQ Loan, all of the outstanding obligations under the TRQ Loan are immediately due and payable to Turquoise Hill as of the date hereof. As of the date hereof, the Company has received no indication from CIC of any intention to deliver a notice of default under the CIC Convertible Debenture or to accelerate the amounts outstanding under the CIC Convertible Debenture, and has not received any indication from Turquoise Hill of any intention to demand payment of the amounts outstanding under the TRQ Loan. In addition, SGS received notice from First Concept demanding payment of the full amount of the Arbitration Award, together with the accrued interest thereon, by no later than March 30, 2018, otherwise First Concept intends to commence enforcement proceedings against SGS in respect of the Arbitration Award. On May 10, 2018, SGS received a notice from First Concept advising that First Concept has obtained a court order dated April 27, 2018 from the High Court of Hong Kong granting leave to First Concept to enforce the Arbitration Award against SGS in Hong Kong. If First Concept is successful in enforcing the Arbitration Award, the Company may not be able to re-pay the sum of $11,500 and the associated interest.

1. CORPORATE INFORMATION AND GOING CONCERN (CONTINUED)

Furthermore, continuing delay in securing additional financing could ultimately result in an event of default of the equipment loan, which if not cured within cure periods in accordance with the terms of equipment loan, may result in the principal amounts owing and all accrued and unpaid interest becoming immediately due and payable upon notice to the Company by the lender of the equipment loan.

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

As at March 31, 2018, the Company's gearing ratio was 0.02 (December 31, 2017: 0.02), which was calculated based on the Company's long term liabilities to total assets. As at March 31, 2018 and December 31, 2017, the Company has not been subject to any externally imposed capital requirements.

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 ("IAS") 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 March 31, 2018 were approved and authorized for issue by the Board of Directors of the Company on May 14, 2018.

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, 2017 consolidated annual financial statements, with the exceptions as discussed 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, 2017.

Prior to January 1, 2018, the functional currency of the Company's Mongolian operations (SGS, Mazaalai Resources LLC, Mazaatt Holdings LLC and Dayarbulag LLC), was the United States Dollar. The functional currency of the Company's Chinese subsidiaries (SouthGobi Trading (Beijing) Co., Ltd., Inner Mongolia SouthGobi Energy Co., Ltd., and Inner Mongolia SouthGobi Enterprise Co., Ltd.) was Renminbi ("RMB") and the functional currency for the Company's joint venture (RDCC LLC) was the Mongolian Tugrik ("MNT"). Per IAS 21 - The Effects of Changes in Foreign Exchange Rates, an entity's functional currency should be determined based on the underlying transactions, events and conditions relevant to the entity.

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

2. BASIS OF PREPARATION (CONTINUED)

Determination of functional currency involves certain judgments to determine the primary economic environment and this is re-evaluated if events or conditions change. Based on management's re-evaluation, taking into consideration the primary economic environment in which the Mongolian operations carries on its business, management determined that the functional currency of the Mongolian operations changed from US dollars to MNT as at January 1, 2018 given increased mining cost and administrative cost that are denominated in MNT.

The change in functional currency of the Mongolian operations was applied prospectively from January 1, 2018 in accordance with IAS 21. On the date of the change of functional currency, all items on the statement of financial position of the Mongolian operations were translated into MNT at the exchange rate on that date.

2.3 Adoption of new and revised standards and interpretations

The following new IASB standard was adopted by the Company on January 1, 2018.

IFRS 9	Financial Instruments[(i)]
IFRS 15	Revenue from Contracts with Customers[(i)]

(i) Effective for annual periods beginning on or after January 1, 2018

IFRS 9, Financial Instruments ("IFRS 9"), addresses the classification, measurement and derecognition of financial assets and financial liabilities, introduces new rules for hedge accounting and a new impairment model for financial assets. The Company adopted IFRS 9 on a retrospective basis without restating prior period comparatives.

IFRS 9 requires financial assets to be classified as measured at fair value through profit and loss (FVTPL), fair value through other comprehensive income/loss (FVTOCI), and those measured at amortized cost. As a result of the adoption of this standard, the Company has changed its accounting policy for financial assets. The change did not impact the carrying value of any financial assets on the transition date, January 1, 2018. The Company's cash and trade and other receivables, and notes receivables, were reclassified from loans and receivable to amortized cost.

For financial liabilities, the standard retains most of the IAS 39 requirements except when there is a modification of the terms of any financial liability, non-substantial modifications do not result in derecognition. IFRS 9 requires the Company to recalculate the amortized cost of the modified financial liability by discounting the modified contractual cash flows using the original effective interest rate and recognizing any adjustment in profit or loss. The Company has had several past modifications of its CIC Convertible Debenture and the TRQ Loan. Therefore, on initial application of IFRS 9, due to the modification of the financial liabilities, $1,332 was recorded to increase the opening accumulated deficit and increase the carrying value of the financial liabilities upon the application of the transitional relief.

2. BASIS OF PREPARATION (CONTINUED)

Additionally, the new impairment model requires the recognition of impairment provisions based on expected credit losses ("ECL") rather than only incurred credit losses as is the case under IAS 39. It applies to financial assets classified at amortized cost. The ECL model requires judgement as to how changes in economic factors affect ECLs, which are determined on a probability-weighted basis. The Company applies the IFRS 9 simplified approach to measuring expected credit losses on its trade receivables and estimates expected credit loss based on the possible default events on its trade and other receivables within the next twelve months. The Company has determined that, due to the unsecured nature of its trade and other receivables, the loss allowance on its trade receivables increased by $1,103 during the period relating to an expected loss rate of 10% for trade receivables 60 days past due and 100% for trade receivables 180 days past due.

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. 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 Company has concluded there were no significant changes in the accounting for sales as a result of the transition to IFRS 15. The Company produces coal products and the relevant performance obligations relate primarily to the delivery of the coal products to customers, with each delivery representing a separate performance obligation.

Revenue from the sale of coal product is recognized at the point the customer obtains control of the product, in which the significant risks and rewards of ownership pass to the buyer and the Company has a present right to payment for the product.

There have been no other new IFRSs or IFRIC interpretations that is not yet effective that would be expected to have a material impact on the Company, except those disclosed in the Company's annual consolidated financial statements for the year ended December 31, 2017.

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 3.23 to the Company's December 31, 2017 consolidated annual financial statements. The significant accounting judgments and estimates remain substantially unchanged from December 31, 2017.

<u>Liquidity and the going concern assumption</u>

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 as well as the expected timing of payments of suppliers and the repayment of debt and other financial liabilities. Refer to Note 1 for details.

2. BASIS OF PREPARATION (CONTINUED)

Review of carrying value of assets and impairment charges

As of the date hereof, the Company is in default under the CIC Convertible Debenture and the TRQ Loan. Pursuant to the terms of the CIC Convertible Debenture, CIC may, in its discretion, provide notice to the Company and declare all principal, interest and other amounts owing under the CIC Convertible Debenture immediately due and payable, and take steps to enforce payment thereof. Pursuant to the terms of the TRQ Loan, all of the outstanding obligations under the TRQ Loan are immediately due and payable to Turquoise Hill as of the date hereof. As of the date hereof, the Company has received no indication from CIC of any intention to deliver a notice of default under the CIC Convertible Debenture or to accelerate the amounts outstanding under the CIC Convertible Debenture, or from Turquoise Hill of any intention to demand payment of the amounts outstanding under the TRQ Loan.

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 equipment loan, which if not cured within applicable cure periods in accordance with the terms of such instruments, may result in the principal amounts owing and all accrued and unpaid interest becoming immediately due and payable upon notice to the lender of the equipment loan.

In the determination of carrying values and impairment charges, management of the Company reviews the recoverable amount (the higher of the fair value less costs of disposal or the value in use) in the case of non-financial assets and objective evidence indicating impairment in the case of financial assets. These determinations and their individual assumptions require that management make a decision based on the best available information at each reporting period. Changes in these assumptions may alter the results of non-financial asset and financial asset impairment testing, impairment charges recognized in profit or loss and the resulting carrying amounts of assets.

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 March 31, 2018. The impairment indicator was the uncertainty of future coal prices in China.

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 "fair value less costs of disposal" ("FVLCTD") using a discounted future cash flow valuation model. The Company's cash flow valuation model takes into consideration the latest available information to the Company, including but not limited to, sales price, sales volumes, operating cost and life of mine coal production assumptions as at March 31, 2018. The Company's Ovoot Tolgoi Mine cash generating unit carrying value was $81,253 as at March 31, 2018.

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

- Coal resources and reserves as estimated by an independent third party engineering firm;
- Sales price estimates from an independent market consulting firm;
- Forecasted sales volumes in line with production levels as per the updated mine plan;
- Life-of-mine coal production, strip ratio, capital costs and operating costs;
- Coal processing to increase the grade and qualities of the thermal coal produced and sold; and
- A post-tax discount rate of 13.4% based on an analysis of the market, country and asset specific factors.

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

2. BASIS OF PREPARATION (CONTINUED)

The impairment analysis did not result in the identification of an impairment loss or an impairment reversal and no charge or reversal was required as at March 31, 2018. 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.

3. SEGMENTED INFORMATION

The Company's one reportable operating segment is its Coal Division. The Company's Interim Chief Executive Officer (chief operating decision maker) reviews the 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, and logistics and trading of coal in Mongolia and China. The Company's Corporate Division does not earn revenues and therefore does not meet the definition of an operating segment.

During the three months ended March 31, 2018, the Coal Division had 13 active customers with the largest customer accounting for 16% of revenues, the second largest customer accounting for 14% of revenues, the third largest customer accounting for 13% of revenues and the other customers accounting for the remaining 57% of revenues.

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

	Coal Division	Unallocated (i)	Consolidated Total
Segment assets			
As at March 31, 2018	**$ 261,771**	**$ 4,309**	**$ 266,080**
As at December 31, 2017	253,256	7,311	260,567
Segment liabilities			
As at March 31, 2018	**$ 129,203**	**$ 134,439**	**$ 263,642**
As at December 31, 2017	119,095	130,932	250,027
Segment revenues			
For the three months ended March 31, 2018	**$ 23,223**	**$ -**	**$ 23,223**
For the three months ended March 31, 2017	25,254	-	25,254
Segment loss			
For the three months ended March 31, 2018	**$ (2,377)**	**$ (1,083)**	**$ (3,460)**
For the three months ended March 31, 2017	(1,896)	(7,721)	(9,617)

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

3. SEGMENTED INFORMATION (CONTINUED)

	Coal Division	Unallocated (i)	Consolidated Total
Impairment charge on assets (ii), (iii)			
For the three months ended March 31, 2018	$ 1,103	$ -	$ 1,103
For the three months ended March 31, 2017	2,331	-	2,331
Depreciation and amortization			
For the three months ended March 31, 2018	$ 9,641	$ 25	$ 9,666
For the three months ended March 31, 2017	11,631	72	11,703
Share of earnings of a joint venture			
For the three months ended March 31, 2018	$ 340	$ -	$ 340
For the three months ended March 31, 2017	266	-	266
Finance cost			
For the three months ended March 31, 2018	$ 707	$ 5,299	$ 6,006
For the three months ended March 31, 2017	258	5,457	5,715
Finance income			
For the three months ended March 31, 2018	$ 168	$ 90	$ 258
For the three months ended March 31, 2017	4	-	4
Current income tax			
For the three months ended March 31, 2018	$ 929	$ -	$ 929
For the three months ended March 31, 2017	45	-	45

(i) The unallocated amount contains all amounts associated with the Corporate Division.
(ii) The impairment charges on assets for the three months ended March 31, 2018 relate to trade and other receivables (Note 11).
(iii) The impairment charge on assets for the three months ended March 31, 2017 related to inventories (Note 12).

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

	Mongolia	Hong Kong	China	Consolidated Total
Revenue (i)				
For the three months ended March 31, 2018	$ -	$ -	$ 23,223	$ 23,223
For the three months ended March 31, 2017	-	-	25,254	25,254
Non-current assets				
As at March 31, 2018	$ 182,948	$ 87	$ 310	$ 183,345
As at December 31, 2017	181,603	467	345	182,415

(i) The revenue information above is based on the locations of the customers.

4. REVENUE

Revenue represents the net invoiced value of goods sold which arises from the trading of coal.

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

5. EXPENSES BY NATURE

The Company's expenses by nature are summarized as follows:

	Three months ended March 31, 2018	Three months ended March 31, 2017
Depreciation	**$ 6,419**	$ 10,848
Auditors' remuneration	**111**	102
Employee benefit expense (including directors' remuneration)		
Wages and salaries	**$ 1,241**	$ 1,906
Equity-settled share option expense (Note 20)	**16**	37
Pension scheme contributions	**102**	205
	$ 1,359	$ 2,148
Minimum lease payments under operating leases	**$ 156**	$ 203
Foreign exchange loss/(gain)	**(779)**	510
Impairment of coal stockpile inventories (Note 12)	**-**	2,331
Provision for doubtful trade and other receivables (Note 11)	**1,103**	-
Loss on disposal of property, plant and equipment (Note 13)	**67**	-
Provision for commercial arbitration (Note 18)	**224**	-
Penalty on late settlement with trade payables (Note 7)	**104**	268
Mining services, net (Note 7)	**-**	2,395
Mine operating costs and other	**11,582**	10,576
Total expenses	**$ 20,346**	$ 29,381

6. COST OF SALES

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

	Three months ended March 31, 2018	Three months ended March 31, 2017
Operating expenses	**$ 10,132**	$ 10,700
Share-based compensation expense (Note 20)	**-**	23
Depreciation and depletion	**2,841**	7,486
Impairment of coal stockpile inventories (Note 12)	**-**	2,331
Cost of sales from mine operations	**12,973**	20,540
Cost of sales related to idled mine assets (i)	**3,534**	3,219
Cost of sales	**$ 16,507**	$ 23,759

Cost of inventories recognized as expense in cost of sales for the three months ended March 31, 2018 totaled $11,848 (2017: $14,765).

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

7. OTHER OPERATING EXPENSES

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

	Three months ended March 31, 2018	2017
Foreign exchange loss/(gain)	**$ 779**	$ (510)
Mining services, net	**-**	(2,395)
Penalty on late settlement of trade payables	**(104)**	(268)
CIC management fee	**(583)**	-
Provision for doubtful trade and other receivables (Note 11)	**(1,103)**	-
Loss on disposal of property, plant and equipment (Note 13)	**(67)**	-
Provision for commercial arbitration (Note 18)	**(224)**	-
Other	**(36)**	(35)
Other operating expenses	**$ (1,338)**	$ (3,208)

8. FINANCE COSTS AND INCOME

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

	Three months ended, March 31, 2018	2017
Interest expense on convertible debenture (Note 18)	**$ 5,294**	$ 5,277
Unrealized loss on embedded derivatives in convertible debenture (Note 18)	**-**	177
Interest expense on borrowings (Note 17)	**653**	143
Loan arrangement fee (Note 17)	**13**	81
Accretion of decommissioning liability	**46**	37
Finance costs	**$ 6,006**	$ 5,715

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

	Three months ended, March 31, 2018	2017
Unrealized gain on embedded derivatives in convertible debenture (Note 18)	**$ 90**	$ -
Interest income	**10**	4
Fair value gain on notes receivable upon redemption	**158**	-
Finance income	**$ 258**	$ 4

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

9. TAXES

The Canadian statutory tax rate was 26% (2017: 26%) on the estimated assessable profits arising in Canada during the period. Taxes on profits assessable elsewhere have been calculated at the rates of tax prevailing in the countries/jurisdictions in which the Company operates.

	Three months ended, March 31, 2018	Three months ended, March 31, 2017
Current - Canada		
Charge for the period	$ -	$ -
Current - elsewhere		
Charge for the period	929	45
Total tax charge for the period	$ 929	$ 45

10. LOSS PER SHARE

The calculation of basic loss and diluted loss per share is based on the following data:

	Three months ended March 31, 2018	Three months ended March 31, 2017
Net loss	$ (3,460)	$ (9,617)
Weighted average number of shares	272,624	270,935
Basic and diluted loss per share	$ (0.01)	$ (0.04)

11. TRADE AND OTHER RECEIVABLES

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

	As at March 31, 2018	As at December 31, 2017
Trade receivables	$ 15,979	$ 12,901
Other receivables	3,328	3,585
Total trade and other receivables	$ 19,307	$ 16,486

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

	As at March 31, 2018	As at December 31, 2017
Less than 1 month	$ 4,945	$ 15,962
1 to 3 months	6,380	296
3 to 6 months	7,982	19
Over 6 months	-	209
Total trade and other receivables	$ 19,307	$ 16,486

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

11. TRADE AND OTHER RECEIVABLES (CONTINUED)

Trade receivables are normally paid within 30 days from the date of billing. Overdue balances are reviewed regularly by senior management. The Company does not hold any collateral or other credit enhancements over its trade and other receivable balances.

The Company made a provision of $1,103 on its trade and other receivables for the three months ended March 31, 2018 (2017: nil). As at March 31, 2018, the provision for doubtful trade and other receivables amounted to $1,800 (December 31, 2017: $697).

12. INVENTORIES

The Company's inventories consist of the following amounts:

	As at	
	March 31, 2018	**December 31, 2017**
Coal stockpiles	**$ 15,238**	$ 18,223
Materials and supplies	**17,997**	18,166
Total inventories	**$ 33,235**	$ 36,389

No impairment was recorded for the three months ended March 31, 2018 related to the Company's coal stockpile inventories (2017: $2,331 included in cost of sales). As at December 31, 2017, $13,500 of the Company's coal stockpile inventories are carried at their net realizable value.

13. 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	Non-depreciable assets	Total
Cost						
As at January 1, 2018	$ 350,540	$ 28,874	$ 72,194	$ 173,401	$ 28,967	$ 653,976
Additions	**406**	**29**	**-**	**10,143**	**77**	**10,655**
Disposals	**(539)**	**-**	**-**	**-**	**-**	**(539)**
Exchange realignment	**72**	**45**	**-**	**-**	**142**	**259**
As at March 31, 2018	**$ 350,479**	**$ 28,948**	**$ 72,194**	**$ 183,544**	**$ 29,186**	**$ 664,351**
Accumulated depreciation and impairment charges						
As at January 1, 2018	$ (297,264)	$ (28,326)	$ (51,443)	$ (100,297)	$ (24,189)	$ (501,519)
Depreciation for the period	**(8,143)**	**(66)**	**(1,183)**	**(274)**	**-**	**(9,666)**
Eliminated on disposals	**153**	**-**	**-**	**-**	**-**	**153**
Exchange realignment	**(3)**	**(19)**	**-**	**-**	**-**	**(22)**
As at March 31, 2018	**$ (305,257)**	**$ (28,411)**	**$ (52,626)**	**$ (100,571)**	**$ (24,189)**	**$ (511,054)**
Carrying amount						
As at December 31, 2017	$ 53,276	$ 548	$ 20,751	$ 73,104	$ 4,778	$ 152,457
As at March 31, 2018	**$ 45,222**	**$ 537**	**$ 19,568**	**$ 82,973**	**$ 4,997**	**$ 153,297**

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

13. PROPERTY, PLANT AND EQUIPMENT (CONTINUED)

13.1 Non-depreciable assets

The non-depreciable assets include the construction in progress and deposits on purchasing items of property, plant and equipment of $4,230 (December 31, 2017: $4,169), which 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.

13.2 Pledge on items of property, plant and equipment

As at March 31, 2018, certain of the Company's property, plant and equipment of $3,771 (December 31, 2017: $4,539) were pledged as security for a bank loan granted to the Company (Note 17).

13.3 Items of property, plant and equipment held under finance leases

As at March 31, 2018, certain of the Company's mobile equipment of $246 (December 31, 2017: $672) were held under finance leases.

14. INVESTMENT IN A JOINT VENTURE

The Company's investment consists of the following amounts:

	As at	
	March 31, 2018	December 31, 2017
Non-current investment in joint venture		
Investment in RDCC LLC	**$ 21,142**	$ 21,052
Total investment	**$ 21,142**	$ 21,052

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 for the exclusive use of third party coal transport companies. In October 2012, the concession agreement was 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. On September 17, 2015, the Invest Mongolia Agency signed an amendment to the concession agreement with RDCC LLC to extend the exclusive right of ownership to 30 years.

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

	Three months ended March 31,	
	2018	2017
Balance, beginning of period	**$ 21,052**	$ 21,335
Dividend received	**(488)**	(422)
Share of earnings of a joint venture	**340**	266
Share of other comprehensive income of a joint venture	**238**	259
Balance, end of period	**$ 21,142**	$ 21,438

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

14. INVESTMENT IN A JOINT VENTURE (CONTINUED)

For the three months ended March 31, 2018, RDCC LLC recognized toll fee revenue of $1,557 (2017: $1,181). For the three months ended March 31, 2018, RDCC LLC had a net income of $849 (2017: $664).

15. 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	
	March 31, 2018	**December 31, 2017**
Less than 1 month	**$ 18,762**	$ 20,664
1 to 3 months	**15,414**	16,132
3 to 6 months	**14,556**	8,825
Over 6 months	**32,507**	33,598
Total trade and other payables	**$ 81,239**	$ 79,219

16. PROVISION FOR COMMERCIAL ARBITRATION

On June 24, 2015, 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") for a total consideration of $11,500.

On January 10, 2018, the Company received a confidential partial award (final except as to costs) with respect to the commercial arbitration. Pursuant to the Arbitration Award, SGS has been ordered to repay the sum of $11,500 (which SGS had received as a prepayment for the purchase of coal) to First Concept, together with accrued interest at a simple interest rate of 6% per annum from the date which the prepayment was made until the date of the Arbitration Award, and then at a simple interest rate of 8% per annum until full payment. The Arbitration Award is final, except as to costs which have been reserved for a future award. As at March 31, 2018, the Company has recorded a provision of $14,108 for the commercial arbitration. (December 31, 2017: $13,884).

On March 23, 2018, SGS received a notice from First Concept demanding payment of the full amount of the Arbitration Award, together with the accrued interest thereon, by no later than March 30, 2018, otherwise First Concept intends to commence enforcement proceedings against SGS in respect of the Arbitration Award. On May 10, 2018, SGS received a notice from First Concept advising that First Concept has obtained a court order dated April 27, 2018 from the High Court of Hong Kong granting leave to First Concept to enforce the Arbitration Award against SGS in Hong Kong. The Company is consulting with its independent litigation counsel regarding this matter. However, as SGS does not have any material assets, properties or place of business in Hong Kong, the Company is of the view that this court order will have little or no immediate impact on its ongoing operations.

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

16. PROVISION FOR COMMERCIAL ARBITRATION (CONTINUED)

The Company is currently considering and reviewing its options with respect to the Arbitration Award, including exploring ways to work with First Concept on payment arrangements that are practical to and are in best interests of both parties; however, there can be no assurance that a favorable outcome will be reached.

In the event that First Concept applies to enforce the Arbitration Award against SGS through judicial measures in courts of Mongolia or any other jurisdictions in which SGS has assets or properties, the Company intends to take appropriate steps to respond to such enforcement proceedings in the best interests of the Company through independent litigation counsel which has been retained by the Company for this purpose.

If First Concept is successful in enforcing the Arbitration Award against SGS, the Company may not be able to re-pay the sum of $11,500 and the associated interest. In such case, this will represent another event of default under the CIC Convertible Debenture and CIC would have another basis to declare the full principal and accrued interest owing thereunder immediately due and payable. Such an event of default under the CIC Convertible Debenture or the Company's inability to re-pay the sum of $11,500 and associated interest to First Concept could result in voluntary or involuntary proceedings involving the Company (including bankruptcy).

17. INTEREST-BEARING BORROWINGS

The Company's interest-bearing borrowings consist of the following amounts:

	As at	
	March 31, 2018	**December 31, 2017**
Turquoise Hill Loan Facility (i)	**$ 1,377**	$ 1,708
Equipment loan (ii)	**2,600**	2,441
Bank loan (iii)	**3,039**	3,041
Finance leases payable (iv)	**180**	503
Total interest-bearing borrowings	**$ 7,196**	$ 7,693

(i) Turquoise Hill Loan Facility

On May 25, 2014, the Company announced it obtained a loan from Turquoise Hill in the form of a $10,000 revolving credit facility to meet its short term working capital requirements (the "TRQ Loan"). The key commercial terms of the facility were: an original maturity date of August 30, 2014 (subsequently extended as described below); an interest rate of one month US dollar LIBOR Rate in effect plus 11% per annum; a commitment fee of 35% of interest rate payable quarterly in arrears on undrawn principal amount of facility and a front end fee of $100.

During 2014 and 2016, the due date of the TRQ Loan, was extended several times and the maximum amount of the facility was reduced to $3,800.

17. INTEREST-BEARING BORROWINGS (CONTINUED)

On May 16, 2016, the Company and Turquoise Hill entered into the May 2016 Deferral Agreement, whereby Turquoise Hill agreed to a limited deferral of repayment of all remaining amounts and obligations owing under the TRQ Loan to December 29, 2017 in accordance with the schedule of repayments set out below:

- The Company agreed to effect monthly repayments on the last business day of each month in an amount of (i) $150 per month from May 2016 to April 2017; (ii) $200 per month from May 2017 to December 2017; and (iii) the remaining balance on December 29, 2017 (the payments in (i), (ii) and (iii), the "Repayments"); and
- Interest shall continue to accrue on all outstanding obligations at the 12-month US dollar LIBOR rate.

As of the date hereof, the Company has not paid its October, November and December 2017 monthly payments and the accrued interest. Pursuant to the terms of the TRQ Loan and the May 2016 Deferral Agreement, the Company is, as of the date hereof, in default of its obligations under the TRQ Loan and the May 2016 Deferral Agreement as a result of the Company failing to make the Repayments in its entirety on or before the dates set out above. Consequently, all of the outstanding obligations under the TRQ Loan and the May 2016 Deferral Agreement are immediately due and payable to Turquoise Hill as of the date hereof. As of the date hereof, the Company has received no indication from Turquoise Hill of any intention to demand payment of the amounts outstanding under the TRQ Loan and the May 2016 Deferral Agreement.

As at March 31, 2018, the outstanding principal and accrued interest under this facility amounted to $800 and $714, respectively (at December 31, 2017, the outstanding principal and accrued interest under this facility amounted to $1,000 and $708, respectively). A fair value gain of $137 was credited to accumulated deficit upon the adoption of IFRS 9 starting from January 1, 2018.

(ii) Equipment Loan

Inner Mongolia SouthGobi Energy Ltd., a subsidiary of the Company executed a $10,369 loan agreement on August 31, 2017 with Beijing Jin Rui Tian Chen Asset Management Co Ltd. for the purpose of financing the purchase of mining equipment to increase the production capacity of the Company.

The key terms of the equipment loan are as follows:

- Principal amount of $10,369;
- Maturity date set at 12 months from each drawdown;
- Interest rate of 12% per annum and payable upon maturity; and
- The Company was to have provided a corporate guarantee to cover the principal and interest owed and certain items of property, plant and equipment were to have been pledged as security upon the completion of equipment purchase.

As at March 31, 2018, the outstanding principal and accrued interest for the equipment loan amounted to $2,393 and $207, respectively (at December 31, 2017, the outstanding principal and accrued interest for the equipment loan amounted to $2,309 and $132, respectively).

A loan arrangement fee of 1% of the loan principal drawn was charged and will be amortized throughout the loan term. For the period ended March 31, 2018, $13 of loan arrangement fee was amortized (2017: nil). The Company believes the principal amount is capped at the amount drawn down to date and the related mining equipment has not been purchased as of the date hereof.

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

17. INTEREST-BEARING BORROWINGS (CONTINUED)

(iii) Bank Loan

On May 6, 2016, SGS obtained a bank loan (the "Bank Loan") in the principal amount of $2,000 from a Mongolian bank (the "Bank"). The principal terms of the Bank Loan include, among other things, an interest rate of 15.8% per annum, a maturity date of May 6, 2017 (subsequently extended as described below) and SGS being required to pledge certain of its mobile equipment in favour of the Bank as collateral for the Bank Loan.

On July 6, 2017, the Company and the Bank entered into a supplementary agreement with the key commercial terms of the Bank Loan modified as follows:

- Principal amount increased to $3,000;
- $2,300 of the principal amount matured on May 6, 2018 while the remaining balance of the principal amount of $700 will mature on January 4, 2019;
- Interest rate of 15.8% per annum applies to the $2,300 portion of the principal amount, while an interest rate of 15.0% per annum applies to the remaining $700 portion of the principal amount; in each case, interest is payable monthly; and
- Certain items of property, plant and equipment with value of $3,771 as at March 31, 2018 were pledged as security.

As at March 31, 2018, the outstanding balance for the bank loan was $3,000 (December 31, 2017: $3,000) and the Company owed accrued interest of $39 (December 31, 2017: $41).

Subsequently in May 2018, $2,300 of the loan principal was repaid to the Bank by the Company.

(iv) Finance Leases Payable

The Company leases certain of its mobile equipment for daily operations. These leases are classified as finance leases and have remaining lease terms ranging from 2 to 5 years.

At March 31, 2018, the total future minimum lease payments under finance leases and their present values were as follows:

	Minimum lease payments As at		Present value of minimum lease payments As at	
	March 31, 2018	**December 31, 2017**	**March 31, 2018**	**December 31, 2017**
Amounts payable:				
Within one year	**$ 107**	$ 192	**$ 91**	$ 162
In the second year	**77**	174	**72**	160
In the third to fifth years, inclusive	**17**	188	**17**	181
Total minimum finance lease payments	**$ 201**	$ 554	**$ 180**	$ 503
Future finance charges	**(21)**	(51)		
Total net lease finance payables	**$ 180**	$ 503		
Portion classified as current liabilities	**(91)**	(162)		
Non-current portion	**$ 89**	$ 341		

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

18. CONVERTIBLE DEBENTURE

18.1 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. 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 March 31, 2018.

18.2 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 CAD$ and U.S. Dollar) and spot foreign exchange rates.

18.3 Valuation assumptions

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

	As at	
	March 31, 2018	**December 31, 2017**
Floor conversion price	**CAD$8.88**	CAD$8.88
Ceiling conversion price	**CAD$11.88**	CAD$11.88
Common share price	**CAD$0.17**	CAD$0.18
Historical volatility	**82%**	82%
Risk free rate of return	**2.20%**	2.22%
Foreign exchange spot rate (CAD$ to U.S. Dollar)	**0.78**	0.80
Forward foreign exchange rate curve (CAD$ to U.S. Dollar)	**0.776 - 0.793**	0.795 - 0.802

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

18. CONVERTIBLE DEBENTURE (CONTINUED)

18.4 Presentation

Based on the Company's valuation as at March 31, 2018, the fair value of the embedded derivatives decreased by $90 compared to December 31, 2017. The decrease was recorded as finance income for the three months ended March 31, 2018.

For the three months ended March 31, 2018, the Company recorded interest expense of $5,294 related to the convertible debenture as a finance cost (2017: $5,277). 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 March 31, 2018	Three months ended March 31, 2017
Balance, beginning of period	**$ 116,374**	$ 117,590
Interest expense on convertible debenture	**5,294**	5,277
Increase/(decrease) in fair value of embedded derivatives	**(90)**	177
Fair value adjustment upon adoption of IFRS 9	**1,469**	-
Interest paid	**-**	(7,840)
Balance, end of period	**$ 123,047**	$ 115,204

The convertible debenture balance consists of the following amounts:

	As at March 31, 2018	As at December 31, 2017
Current convertible debenture		
Interest payable	**$ 29,459**	$ 24,242
Debt host	**93,276**	91,730
Fair value of embedded derivatives	**312**	402
Total convertible debenture	**$ 123,047**	$ 116,374

18.5 Interest deferral and settlement

On June 12, 2017, the Company executed the June 2017 Deferral Agreement with CIC for a revised repayment schedule on the $22,254 of cash interest and associated costs originally due on May 19, 2017 (the "May 2017 Interest Payable"). The key repayment terms of the June 2017 Deferral Agreement are: (i) the Company was required to repay on average $2,170 of the cash interest and associated costs monthly during the period from May 2017 to October 2017; and (ii) the Company was required to repay $9,731 of cash interest and associated costs on November 19, 2017. The Company will pay a deferral fee at a rate of 6.4% per annum in consideration for the deferral.

18. CONVERTIBLE DEBENTURE (CONTINUED)

At any time before the May 2017 Interest Payable is fully repaid, the Company is required to consult with and obtain written consent from CIC prior to effecting a replacement or termination of either or both of its Chief Executive Officer and its Chief Financial Officer, otherwise this will constitute an event of default under the CIC Convertible Debenture, but CIC shall not withhold its consent if the Board proposes to replace either or both such officers with nominees selected by the Board, provided that the Board acted honestly and in good faith with a view to the best interests of the Company in the selection of the applicable replacements.

In addition, pursuant to the terms of the CIC Convertible Debenture, the Company was required to pay $8,066 of anniversary cash interest to CIC on November 19, 2017. Pursuant to the Convertible Debenture, the Company was also obliged to issue $4,000 worth of November 2017 PIK Interest shares to CIC on November 19, 2017. The Company will also be required to pay $7,934 of cash interest to CIC on May 19, 2018. As of the date hereof, the Company expects that it will be unable to pay the May 2018 Payment to CIC on the due date.

As of the date hereof, the Company: (i) has neither paid the November 19th Payments nor issued the November 2017 PIK Interest shares to CIC within the cure period provided for in the CIC Convertible Debenture; and (ii) has not agreed upon a repayment plan for such amounts with CIC. Consequently, the Company is in default under the CIC Convertible Debenture and the June 2017 Deferral Agreement. Pursuant to the terms of the CIC Convertible Debenture and the June 2017 Deferral Agreement, CIC may, in its discretion, provide notice to the Company and declare all principal, interest and other amounts owing under the CIC Convertible Debenture and the June 2017 Deferral Agreement immediately due and payable, and take steps to enforce payment thereof, which would have a material adverse effect on the business and operations of the Company and may negatively affect the price and volatility of the Common Shares and any investment in such shares could suffer a significant decline or total loss in value. As of the date hereof, the Company has received no indication from CIC of any intention to deliver a notice of default under the CIC Convertible Debenture and the June 2017 Deferral Agreement or to accelerate the amounts outstanding under the CIC Convertible Debenture and the June 2017 Deferral Agreement.

The Company is in discussion with CIC for a deferral of the November 19th Payments, the November 2017 PIK Interest and the May 2018 Payment; however, there can be no assurance that a favorable outcome will be reached. CIC has notified the Company that, as a condition to agreeing to any deferral, it requires that the mutual co-operating agreement (the “Co-Operation Agreement”) dated November 19, 2009 between the Company and CIC be amended to revise the manner in which the amount of the service fee payable to CIC under the Co-Operation Agreement is calculated with retroactive effect; however, the Company has not entered into any formal agreement in respect of the Co-Operation Agreement as of the date hereof. In addition, CIC has advised the Company that it is undertaking a review of the financial and operational performance of the Company. To the knowledge of the Company, this review remains on-going as of the date hereof.

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

18. CONVERTIBLE DEBENTURE (CONTINUED)

As a consequence of the Company not entering into a deferral agreement with CIC as at March 31, 2018, IAS 1 requires the Company to classify the entire balance of the CIC Convertible Debenture as a current liability as at March 31, 2018, notwithstanding the fact that CIC has not indicated any intention to deliver notice of default or accelerate the maturity of the debenture. The Company anticipates that both the debt host and the fair value of the embedded derivative will be classified as a non-current liability upon the execution of a deferral agreement, unless a future event of default occurs under the terms of the CIC Convertible Debenture.

19. EQUITY

19.1 Share Capital

The Company has authorized an unlimited number of common and preferred shares with no par value. At March 31, 2018, the Company had 272,624 common shares outstanding (December 31, 2017: 272,607) and no preferred shares outstanding (December 31, 2017: nil).

19.2 Accumulated deficit and dividends

At March 31, 2018, the Company has accumulated a deficit of $1,140,601 (December 31, 2017: $1,135,809). No dividends have been paid or declared by the Company since inception.

20. SHARE-BASED PAYMENTS

20.1 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 three months ended March 31, 2018 and March 31, 2017, the Company did not grant any stock options to officers, employees, directors and other eligible persons.

The total share-based compensation expense for the three months ended March 31, 2018 was $16 (2017: $37). Share-based compensation expense of $16 (2017: $11) has been allocated to administration expenses, nil has been allocated to evaluation and exploration expenses and cost of sales (2017: $3 and $23, respectively).

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

20. SHARE-BASED PAYMENTS (CONTINUED)

20.2 Outstanding stock options

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

	Three months ended March 31, 2018			Three months ended March 31, 2017		
	Number of options		Weighted average exercise price (CAD$)	Number of options		Weighted average exercise price (CAD$)
Balance, beginning of period	**2,290**	**$**	**0.36**	1,910	$	0.61
Options forfeited	**-**		**-**	(2)		0.92
Options expired	**-**		**-**	(52)		6.16
Balance, end of period	**2,290**	**$**	**0.36**	1,856	$	0.45

The stock options outstanding and exercisable as at March 31, 2018 are as follows:

	Options Outstanding				Options Exercisable			
Exercise price (CAD$)	Options outstanding		Weighted average exercise price (CAD$)	Weighted average remaining contractual life (years)	Options outstanding and exercisable		Weighted average exercise price (CAD$)	Weighted average remaining contractual life (years)
$0.25 - $0.58	**2,124**	**$**	**0.32**	**3.55**	**1,124**	**$**	**0.31**	**2.12**
$0.65 - $0.92	**166**		**0.91**	**1.95**	**113**		**0.90**	**1.93**
	2,290	**$**	**0.36**	**3.43**	**1,237**	**$**	**0.36**	**2.10**

21. FAIR VALUE MEASUREMENTS

The fair value of the Company's financial assets approximates its carrying values, however, the fair value of the Company's financial liabilities is below the carrying value of its financial liabilities given the current financial condition of the Company as disclosed in note 1 of the financial statements.

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.

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

21. FAIR VALUE MEASUREMENTS (CONTINUED)

	As at March 31, 2018			
Recurring measurements	**Level 1**	**Level 2**	**Level 3**	**Total**
Financial liabilities measured at fair value				
Convertible debenture - embedded derivatives	$ -	$ 312	$ -	$ 312
Total financial liabilities measured at fair value	**$ -**	**$ 312**	**$ -**	**$ 312**

	As at March 31, 2018			
Financial liabilities disclosed at fair value	**Level 1**	**Level 2**	**Level 3**	**Total**
Convertible debenture - debt host	-	220,146	-	220,146
Total financial liabilities disclosed at fair value	**$ -**	**$ 220,146**	**$ -**	**$ 220,146**

	As at December 31, 2017			
Recurring measurements	**Level 1**	**Level 2**	**Level 3**	**Total**
Financial liabilities measured at fair value				
Convertible debenture - embedded derivatives	$ -	$ 402	$ -	$ 402
Total financial liabilities measured at fair value	**$ -**	**$ 402**	**$ -**	**$ 402**

	As at December 31, 2017			
Financial liabilities disclosed at fair value	**Level 1**	**Level 2**	**Level 3**	**Total**
Convertible debenture - debt host	-	216,154	-	216,154
Total financial liabilities disclosed at fair value	**$ -**	**$ 216,154**	**$ -**	**$ 216,154**

There were no transfers between Level 1, 2 and 3 for the three months ended March 31, 2018.

22. SUPPLEMENTAL CASH FLOW INFORMATION

22.1 Non-cash financing and investing activities

The Company's non-cash investing and financing transactions are as follows:

	Three months ended March 31,	
	2018	**2017**
Addition to decommissioning liability	**$ 24**	$ 215
Amortization of deferred stripping being capitalized	**4,113**	-
Convertible debenture interest settlement in shares (Note 18)	**-**	4,000
Trade receivables settled by properties held for sale (Note 11)	**-**	10,752
Settlement of court case penalty via provision of mining services	**-**	6,184
Purchase of vehicles financed by loans	**-**	100
Total non-cash financing and investing activities	**$ 4,137**	$ 21,251

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

22. SUPPLEMENTAL CASH FLOW INFORMATION (CONTINUED)

22.2 Net change in non-cash working capital items

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

	Three months ended March 31, 2018	2017
Decrease/(increase) in inventories	**$ 1,445**	$ (3,385)
Increase in trade and other receivables and notes receivables	**(2,816)**	(6,548)
Increase in prepaid expenses and deposits	**(1,160)**	(1,118)
Increase in trade and other payables	**1,406**	17,712
Increase/(decrease) in deferred revenue	**5,233**	(2,101)
Net change in non-cash working capital items	**$ 4,108**	$ 4,560

23. COMMITMENTS FOR EXPENDITURE

As at March 31, 2018, the Company's commitments for expenditure that have not been disclosed elsewhere in the condensed consolidated financial statements are as follows:

	Within 1 year	2-3 years	Over 3 years	Total
As at March 31, 2018				
Capital expenditure commitments	**$ 3,807**	**$ -**	**$ -**	**$ 3,807**
Operating expenditure commitments	**12,850**	**1,517**	**2,031**	**16,398**
Commitments	**$ 16,657**	**$ 1,517**	**$ 2,031**	**$ 20,205**
As at December 31, 2017				
Capital expenditure commitments	$ 4,363	$ -	$ -	$ 4,363
Operating expenditure commitments	3,422	622	2,350	6,394
Commitments	$ 7,785	$ 622	$ 2,350	$ 10,757

24. CONTINGENCIES

24.1 Class action lawsuit

In January 2014, Siskinds LLP, a Canadian law firm, filed a class action (the "Class Action") against the Company, certain of its former senior officers and directors, and its former auditors, Deloitte LLP, in the Ontario Court in relation to the Company's restatement of certain financial statements previously disclosed in the Company's public fillings (the "Restatement").

To commence and proceed with the Class Action, the plaintiff was required to bring a preliminary leave motion and to certify the Class Action as a class proceeding (the "Leave Motion"). The Ontario Court rendered its decision on the Leave Motion on November 5, 2015 and dismissed the plaintiff's Leave Motion as against each of the former senior officers and directors of the Company named in the Class Action on the basis that the "large volume of compelling evidence" proved the defense of reasonable investigation on the balance of probabilities and provided the basis for dismissing the Leave Motion as against them.

However, the Ontario Court allowed the Class Action to proceed under Part XXIII.1 of the Ontario Securities Act, permitting the plaintiff to commence and proceed with an action against the Company in respect of alleged misrepresentations affecting trades in the secondary market for the Company's securities arising from the Restatement. The Company appealed this portion of the decision of the Ontario Court (the "Corporation Appeal").

The plaintiff appealed that part of the November 5, 2015 Ontario Court decision dismissing the action against former officers and directors of the Company (the "Individual's Appeal"). The Individual's Appeal was brought as of right to the Ontario Court of Appeal.

On September 18, 2017, the Ontario Court of Appeal dismissed the Corporation Appeal of the original Ontario lower court decision to permit the plaintiff to commence and proceed with the Class Action. Concurrently, the Ontario Court of Appeal allowed the Individual's Appeal of the original Ontario lower court decision to dismiss the plaintiff's leave motion against certain of the Company's former officers and directors and made an order granting leave for the plaintiff to proceed against such former officers and directors of the Company in relation to the Restatement. As a result, the plaintiff is now permitted to proceed with the Class Action against both the Company and the former officers and directors.

The Company filed an application for leave to appeal to the Supreme Court of Canada in November 2017. Leave to appeal is expected to be decided by June, 2018. If leave to appeal is granted, the appeal would likely be scheduled to be heard in early 2019. A ruling on any appeal would not be expected before September 2019.

The Company firmly believes that it has a strong defense on the merits and will continue to vigorously defend itself against the Class Action through independent Canadian litigation counsel retained by the Company for this purpose. Due to the inherent uncertainties of litigation, it is not possible to predict the final outcome of the Class Action or determine the amount of potential losses, if any. However, the Company has judged a provision for this matter as at March 31, 2018 was not required.

24. CONTINGENCIES (CONTINUED)

24.2 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.

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. At each reporting date, the Company assesses the agreement with Ejin Jinda and has determined it is not probable that these $18,500 will be required to be paid. Accordingly, the Company has determined a provision for this matter as at March 31, 2018 is not required.

24.3 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 VAT, 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.

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 March 31, 2018, management has assessed that recognition of a provision for uncertain tax position is not necessary.

24.4 Mongolian royalties

During 2017, the Company has been ordered by the Mongolian tax authority to apply "reference price" determined by the Government of Mongolia as opposed to calculated sales price that derived based on the actual contract price. Although no official letter was received by the Company as of the date hereof, there can be no assurance that the Government of Mongolia will not disagree with the methodology employed by the Company in determining the calculated sales price and deem such price "non-market" under Mongolian tax law.

24. CONTINGENCIES (CONTINUED)

Management believes that its interpretation of the relevant legislation is appropriate and the Company's positions related to royalty will be sustained. As of March 31, 2018, recognition of a provision for addition Mongolian royalties is not necessary.