

Hong Kong Exchanges and Clearing Limited and The Stock Exchange of Hong Kong Limited (the “Hong Kong Stock Exchange”) take no responsibility for the contents of this announcement, make no representation as to its accuracy or completeness and expressly disclaim any liability whatsoever for any loss howsoever arising from or in reliance upon the whole or any part of the contents of this announcement.



SOUTHGOBI RESOURCES LTD.

南戈壁資源有限公司*

(A company continued under the laws of British Columbia, Canada with limited liability)

(Hong Kong Stock Code: 1878)

(Toronto Stock Code: SGQ)

SouthGobi Resources announces fourth quarter and full year 2017 financial and operating results

SouthGobi Resources Ltd. (the “**Company**”) today announces its financial and operating results for the quarter and the year ended December 31, 2017.

Please see the attached announcement for more details. The information per the attached announcement is available on the SEDAR website at www.sedar.com and the website of the Hong Kong Stock Exchange at www.hkexnews.hk.

By order of the Board
SouthGobi Resources Ltd.
Mao Sun

Interim Independent Lead Director

Vancouver, March 28, 2018

Hong Kong, March 28, 2018

As at the date of this announcement, the Executive Director of the Company is Mr. Yulan Guo; the Independent Non-executive Directors are Messrs. Yingbin Ian He, Zhu Liu and Mao Sun and Ms. Jin Lan Quan; and the Non-executive Directors are Messrs. Wen Yao and Aminbuhe.

* *For identification purposes only*



March 28, 2018

SOUTHGOBI RESOURCES ANNOUNCES FOURTH QUARTER AND FULL YEAR 2017 FINANCIAL AND OPERATING RESULTS

HONG KONG – SouthGobi Resources Ltd. (TSX: **SGQ**, HK: **1878**) (the “Company” or “SouthGobi”) today announces its financial and operating results for the quarter and the year ended December 31, 2017. All figures are in U.S. dollars (“USD”) unless otherwise stated.

SIGNIFICANT EVENTS AND HIGHLIGHTS

The Company’s significant events and highlights for the year ended December 31, 2017 and the subsequent period to March 28, 2018 are as follows:

- **Operating Results** – As a result of improved market conditions and prices for coal in China, the Company experienced an increase in the average selling price of coal from \$16.44 per tonne in 2016 to \$28.31 per tonne in 2017. The volume of coal sales has also increased from 3.91 million tonnes in 2016 to 4.65 million tonnes in 2017.
- **Financial Results** – The Company recorded a gross profit of \$15.1 million in 2017 compared to a gross loss of \$28.6 million in 2016 while \$16.8 million loss from operations was recorded in 2017 compared to a \$38.1 million loss from operations in 2016. Revenue increased from \$58.5 million in 2016 to \$121.0 million in 2017. As a result of improved market conditions and prices for coal in China, the overall financial results improved when compared to 2016, which was principally attributable to increased coal sales as well as higher average selling price achieved during the year.
- **China Investment Corporation (“CIC”) Convertible Debenture (the “CIC Convertible Debenture”)** – Pursuant to the terms of the deferral agreement dated June 12, 2017 (the “June 2017 Deferral Agreement”) with CIC in relation to a revised payment schedule on the \$22.3 million of cash interest and associated costs originally due under the CIC Convertible Debenture on May 19, 2017 (the “May 2017 Interest Payable”), the Company was required to pay \$9.7 million of cash interest and associated costs to CIC on November 19, 2017 (the “June 2017 Deferral Agreement Payment”). In addition, pursuant to the terms of the CIC Convertible Debenture, the Company was required to pay \$8.1 million of anniversary cash interest to CIC on November 19, 2017 (the “November Interest Payment” and together with the June 2017 Deferral Agreement Payment, the “November 19th Payments”). Pursuant to the CIC Convertible Debenture, the Company was also obliged to issue \$4.0 million worth of PIK interest shares (the “November 2017 PIK Interest”) to CIC on November 19, 2017.

As of the date of this press release, 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 under 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, at 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 of this press release, 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 discussions with CIC for a deferral of the November 19th Payments and the November 2017 PIK Interest; however, there can be no assurance that a favorable outcome will be reached.

As a consequence of the Company not entering into a deferral agreement with CIC as at December 31, 2017, International Accounting Standard 1 (“IAS 1”) requires the Company to classify the entire balance of the CIC Convertible Debenture as a current liability as at December 31, 2017, notwithstanding the fact that CIC has not indicated any intention to deliver notice of default or accelerate the maturity of the CIC Convertible 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.

- **Notice of Arbitration** – On January 10, 2018, the Company received a confidential partial award (final except as to costs) (the “Arbitration Award”) with respect to an arbitration proceeding in Hong Kong related to a dispute concerning a coal supply agreement between SouthGobi Sands LLC (“SGS”), a subsidiary of the Company, and First Concept Industrial Group Limited (formerly known as First Concept Logistics Limited) (“First Concept”).

Pursuant to the Arbitration Award, SGS has been ordered to repay the sum of \$11.5 million (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 December 31, 2017, the Company recorded a provision of \$13.9 million for the commercial arbitration.

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. The Company is currently considering and reviewing its options with respect to the Arbitration Award, including exploring ways to work together 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 in other applicable jurisdiction(s), the Company intends to defend itself against such enforcement proceedings through independent litigation counsel retained by the Company for this purpose. However, due to the inherent uncertainties of litigation, it is not possible to predict whether the Company will be successful in defending itself against any such enforcement proceedings.

- **Tax Investigation Case in Mongolia** – On January 10, 2018, SGS was informed by the Court Decision Implementation Agency of Capital City in Mongolia that the enforcement procedure in relation to the previously disclosed judgment of the Mongolian Second Criminal Court (the “Tax Verdict”) rendered against SGS in January 2015 has been terminated and no party shall have any right to make any further claims in connection with the Tax Verdict. As of the date hereof, SGS has fulfilled its obligations under the Tax Verdict.

- **Settlement of Lawsuit Notice from a Former Fuel Supplier** – On January 20, 2017, SGS received a notice from the Khan-Uul District Civil Court of First Instance in Mongolia (the “DC Court”) in relation to a claim for damages from Magnai Trade LLC (“MTLLC”), a former fuel supplier of SGS, in the aggregate amount of MNT 22.2 billion (approximately \$8.9 million) representing outstanding fuel supply payments and related penalties and interest costs. On January 25, 2017, the DC Court dismissed the litigation and the matter was referred to arbitration. The Company signed a settlement agreement with MTLLC on February 10, 2017, pursuant to which SGS would pay MTLLC \$8.0 million in equal monthly installments from March 2017 to June 2017 in full satisfaction of the debt outstanding. The terms of the settlement agreement was subsequently acknowledged by the arbitrator in the arbitration award.

On June 30, 2017, the Company signed a triparty settlement agreement (the “Triparty Settlement Agreement”) with MTLLC and ICIC LLC (“ICIC”) (an independent fuel supplier of the Company), pursuant to which: (i) MTLLC transferred to ICIC its right to receive payment from the Company for the outstanding balance of approximately \$8.0 million owing under the settlement agreement dated February 10, 2017 (the “Outstanding Amount”) and its right to enforce the arbitration award against the Company; and (ii) the Company and ICIC agreed to a revised payment schedule for repayment of the Outstanding Amount. Pursuant to the Triparty Settlement Agreement, the Company agreed to pay interest on the Outstanding Amount, which accrues at a monthly rate of 1.8% and will be settled on a monthly basis. The Company was required to repay on average \$1.3 million monthly during the period from July 2017 to November 2017.

As of the date of this press release, the Company has fulfilled its obligations under the Triparty Settlement Agreement and has fully repaid the Outstanding Amount.

- **Class Action Lawsuit** – On September 18, 2017, the Ontario Court of Appeal dismissed the Company’s appeal of the original Ontario lower court decision to permit the plaintiff to commence and proceed with a class action (the “Class Action”) against the Company claiming damages under the Ontario Securities Act in connection with the Company’s restatement of certain financial statements previously disclosed in the Company’s public filings (the “Restatement”). Concurrently, the Ontario Court of Appeal allowed the plaintiff’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 of the Company.

The Company has 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 May 2018. If leave to appeal is granted, the appeal would likely be scheduled to be heard in early 2019.

- **Ceke Logistics Park Project** – On October 10, 2017, the Company entered into an investment agreement (the “Investment Agreement”) with Beijing De Rong Tai Investment Co., Ltd. (“BDRT”) in connection with the Company’s development of the Ceke Port Eco-friendly Bonded Logistics Park project (the “Ceke Logistics Park”). Pursuant to the Investment Agreement, BDRT has agreed, subject to fulfilment of certain conditions, to invest RMB231 million in installments by July 30, 2018 in return for a 30% interest in Inner Mongolia SouthGobi Enterprise Co. Ltd. (“IMSE”), while the Company will hold the remaining 70% interest in IMSE. Proceeds from BDRT’s equity investment will be used by IMSE for the construction of the Ceke Logistics Park. IMSE is the project company which holds a 100% interest in the Ceke Logistics Park. As of the date of this press release, IMSE has received RMB15 million from BDRT pursuant to the Investment Agreement.
- **Novel Sunrise Investments Limited (“Novel Sunrise”) Sold 25.8 million Shares to a Company Owned by Members of Management** – On January 11, 2017, Novel Sunrise, the Company’s largest shareholder at the time, reported that it had sold 25.8 million Common Shares of the Company effective December 31, 2016 to Voyage Wisdom Limited (“Voyage Wisdom”), a company owned by three members of the Company’s management team, for consideration of \$24 million.
- **Equipment Loan** – Inner Mongolia SouthGobi Energy Ltd., a subsidiary of the Company executed a \$10.4 million loan agreement on August 31, 2017 with Beijing Jin Rui Tian Chen Asset Management Co Ltd. (the “Equipment Loan”) for the purpose of financing the purchase of mining equipment to increase the production capacity of the Company. As at December 31, 2017, the outstanding principal and accrued interest for the Equipment Loan amounted to \$2.3 million and \$0.1 million, respectively (December 31, 2016: nil).

- **Changes in Management and Directors**

Mr. Yingbin Ian He: Mr. He was appointed as an independent non-executive director on May 16, 2017.

Mr. Wen Yao: Mr. Yao was appointed as a non-executive director on May 18, 2017.

Mr. Joseph Belan: Mr. Belan did not stand for the re-election at the Company's Annual General Meeting (the "AGM") and ceased to be an independent non-executive director on June 30, 2017.

Mr. Ningqiao Li: Mr. Li did not stand for the re-election at the AGM and ceased to be an executive director and the Executive Chairman of the Board of Directors of the Company (the "Board") on June 30, 2017.

Mr. Huiyi Wang: Mr. Wang resigned as a non-executive director on July 24, 2017.

Mr. Aminbuhe: Mr. Aminbuhe commenced a leave from his role as the Chief Executive Officer of the Company effective as of November 13, 2017. The Board subsequently terminated the employment of Mr. Aminbuhe due to his incapability to fulfil his daily duties and responsibilities as the Chief Executive Officer of the Company effective as of November 22, 2017. Mr. Aminbuhe was also removed as the Chairman of the Board, but remains on the Board as a non-executive director of the Company.

The Company learned that Mr. Aminbuhe was arrested on October 11, 2017 and is being detained at Rizhao City Detention Center in China as a suspect in a fraudulent loan case. The Board has formed a special committee of independent non-executive directors (the "Special Committee") to initiate a formal internal investigation into the charges against Mr. Aminbuhe and the connection, if any, between those charges and the Company and his conduct as Chairman and Chief Executive Officer of the Company, which includes engaging external advisors to assist in the investigation. The Special Committee is required to report to the Board from time to time with respect to the results and status of its investigation and the potential impact of these matters, if any, on the business and affairs of the Company.

Mr. Bing Wang: Mr. Wang was appointed as interim Chief Executive Officer of the Company, effective as of November 13, 2017.

- **Strategic Advisory Board** – In light of the reconstitution of the Board and appointment of new directors, the Company's Strategic Advisory Board was dissolved on June 30, 2017.

- **Going Concern** – 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 commencing the washing of certain grades of coal in order to produce more premium semi-soft coking coal upon the successful commissioning of the coal washing facility under construction at the mine 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, the 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 December 31, 2018, 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. See section “Liquidity and Capital Resources”. As at March 28, 2018, the Company had \$7.1 million of cash.

OVERVIEW OF OPERATIONAL DATA AND FINANCIAL RESULTS

Summary of Annual Operational Data

	Year ended December 31,	
	2017	2016
Sales Volumes, Prices and Costs		
Premium semi-soft coking coal		
Coal sales (<i>millions of tonnes</i>)	0.86	0.28
Average realized selling price (<i>per tonne</i>) ⁽ⁱ⁾	\$ 47.84	\$ 31.14
Standard semi-soft coking coal		
Coal sales (<i>millions of tonnes</i>)	2.44	2.52
Average realized selling price (<i>per tonne</i>) ⁽ⁱ⁾	\$ 28.72	\$ 16.71
Thermal coal		
Coal sales (<i>millions of tonnes</i>)	1.35	1.11
Average realized selling price (<i>per tonne</i>) ⁽ⁱ⁾	\$ 15.24	\$ 12.16
Total		
Coal sales (<i>millions of tonnes</i>)	4.65	3.91
Average realized selling price (<i>per tonne</i>) ⁽ⁱ⁾	\$ 28.31	\$ 16.44
Raw coal production (<i>millions of tonnes</i>)	6.38	3.38
Cost of sales of product sold (<i>per tonne</i>)	\$ 22.77	\$ 22.26
Direct cash costs of product sold (<i>per tonne</i>) ⁽ⁱⁱ⁾	\$ 9.32	\$ 8.66
Mine administration cash costs of product sold (<i>per tonne</i>) ⁽ⁱⁱⁱ⁾	\$ 2.80	\$ 2.32
Total cash costs of product sold (<i>per tonne</i>) ⁽ⁱⁱ⁾	\$ 12.12	\$ 10.98
Other Operational Data		
Production waste material moved (<i>millions of bank cubic meters</i>)	20.79	7.38
Strip ratio (<i>bank cubic meters of waste material per tonne of coal produced</i>)	3.26	2.18
Lost time injury frequency rate ⁽ⁱⁱⁱ⁾	0.03	0.00

(i) Average realized selling price is presented before deduction of royalties and selling fees.

(ii) A Non-International Financial Reporting Standards ("IFRS") financial measure, see "Non-IFRS Financial Measures" section. Cash costs of product sold exclude idled mine asset cash costs.

(iii) Per 200,000 man hours and calculated based on a rolling 12 month average.

Overview of Annual Operational Data

As at December 31, 2017, the Company had a lost time injury frequency rate of 0.03 per 200,000 man hours based on a rolling 12 month average.

As a result of improved market conditions and prices for coal in China, the Company experienced an increase in the average selling price of coal as compared to 2016. The Company increased its sales volume from 3.91 million tonnes in 2016 to 4.65 million tonnes in 2017. The average realized selling price increased from \$16.44 per tonne in 2016 to \$28.31 per tonne in 2017, which was mainly a result of improved market conditions as well as an improved product mix. The product mix for 2017 consisted of approximately 19% of premium semi-soft coking coal, 52% of standard semi-soft coking coal and 29% of thermal coal compared to approximately 7% of premium semi-soft coking coal, 64% of standard semi-soft coking coal and 29% of thermal coal in 2016.

The Company's production in 2017 was higher than 2016 as a result of ramping up production to meet the expected increase in sales, yielding 6.38 million tonnes for 2017 as compared to 3.38 million tonnes for 2016.

The Company's unit cost of sales of product sold remained similar to 2016 (2017: \$22.77 per tonne; 2016: \$22.26 per tonne).

Summary of Annual Financial Results

<i>\$ in thousands, except per share information</i>	Year ended December 31,	
	2017	2016
Revenue ^{(i),(ii)}	\$ 120,973	\$ 58,450
Cost of sales ⁽ⁱⁱⁱ⁾	(105,858)	(87,045)
Gross profit/(loss) excluding idled mine asset costs	27,747	(16,490)
Gross profit/(loss) including idled mine asset costs	15,115	(28,595)
Other operating expenses	(11,264)	(50)
Administration expenses	(9,181)	(7,888)
Evaluation and exploration expenses	(273)	(422)
Impairment of property, plant and equipment	(11,171)	(1,152)
Loss from operations	(16,774)	(38,107)
Finance costs	(22,958)	(22,314)
Finance income	164	239
Share of earnings of a joint venture	1,287	806
Income tax expense	(1,740)	(1,470)
Net loss	(40,021)	(60,846)
Basic and diluted loss per share	\$ (0.15)	\$ (0.24)

(i) Revenue is presented after the deduction of royalties and selling fees.

(ii) Revenue and cost of sales relate to the Company's Ovoot Tolgoi Mine within the Coal Division operating segment. Refer to note 2 of the selected information from the notes to the consolidated financial statements for further analysis regarding the Company's reportable operating segments.

Overview of Annual Financial Results

The Company recorded a \$16.8 million loss from operations in 2017 compared to a \$38.1 million loss from operations in 2016. As a result of improved market conditions and prices for coal in China, the overall financial results improved when compared to 2016, which were principally attributable to increased coal sales as well as higher average selling price achieved during the year.

Revenue was \$121.0 million in 2017 compared to \$58.5 million in 2016. The Company's revenue is presented after deduction of royalties and selling fees. The Company's effective royalty rate for 2017, based on the Company's average realized selling price of \$28.31 per tonne, was 5.8% or \$1.65 per tonne compared to 7.0% or \$1.14 per tonne based on the average realized selling price of \$16.44 per tonne in 2016.

Royalty regime in Mongolia

The royalty regime in Mongolia is evolving and has been subject to change since 2012.

On February 1, 2016, the Government of Mongolia issued a resolution in connection with the royalty regime. From February 1, 2016 onwards, royalties are to be calculated based on the actual contract price in which transportation cost to the Mongolia border should have been included. If such transportation cost was not included in the contract, the relevant transportation costs, custom documentation fees, insurance and loading cost should be estimated for the calculation of royalties. In the event that the calculated sales price as described above differs from the contract sales price of other entities in Mongolia (same quality of coal and same border crossing) by more than 10%, the calculated sales price will be deemed to be "non-market" under Mongolian tax law and the royalty will then be calculated based on a reference price as determined by the Government of Mongolia.

Cost of sales was \$105.9 million in 2017 compared to \$87.0 million in 2016. The increase in cost of sales in 2017 was mainly due to the increased sales during the year. Cost of sales comprises operating expenses, share-based compensation expense, equipment depreciation, depletion of mineral properties, coal stockpile inventory impairments and idled mine asset costs. Operating expenses in cost of sales reflect the total cash costs of product sold (a Non-IFRS financial measure, see section "Non-IFRS financial measures" of this press release for further analysis) during the year.

<i>\$ in thousands</i>	Year ended December 31,	
	2017	2016
Operating expenses	\$ 55,451	\$ 41,452
Share-based compensation expense/(recovery)	30	(8)
Depreciation and depletion	20,719	26,142
Impairment of coal stockpile inventories	<u>17,026</u>	<u>7,354</u>
Cost of sales from mine operations	93,226	74,940
Cost of sales related to idled mine assets	<u>12,632</u>	<u>12,105</u>
Cost of sales	<u>\$ 105,858</u>	<u>\$ 87,045</u>

Operating expenses in cost of sales were \$55.5 million in 2017 compared to \$41.5 million in 2016. The overall increase in operating expenses was primarily due to the increased sales volume from 3.91 million tonnes in 2016 to 4.65 million tonnes in 2017.

Cost of sales in 2017 and 2016 included coal stockpile impairments of \$17.0 million and \$7.4 million, respectively, to reduce the carrying value of the Company's coal stockpiles to their net realizable value. The coal stockpile impairments recorded in both years primarily related to the Company's higher-ash content products.

Cost of sales related to idled mine asset costs primarily consisted of periodic costs, which were expensed as incurred and included mainly depreciation expense. Cost of sales related to idled mine assets in 2017 included \$12.6 million related to depreciation expenses for idled equipment (2016: \$12.1 million).

Other operating expenses was \$11.3 million in 2017 (2016: negligible).

<i>\$ in thousands</i>	Year ended December 31,	
	2017	2016
Mining services, net	\$ (2,395)	\$ (1,006)
Provision of commercial arbitration	(2,384)	–
Impairment of properties for resale	(1,718)	–
Impairment of prepaid expenses and deposits	(2,517)	–
Underprovision of miscellaneous taxes	(1,421)	–
Foreign exchange gain/(loss)	(1,116)	5,423
Reversal of provision/(provision) for doubtful trade and other receivables	682	(2,641)
Discount on settlement of trade payables	–	1,009
Settlement of civil claims	–	(2,652)
Other	(395)	(183)
Other operating expenses	<u>\$ (11,264)</u>	<u>\$ (50)</u>

Mining services at the Tavan Tolgoi deposit were provided by the Company to Erdenes Tavan Tolgoi JSC (“Erdenes”) in connection with settlement of the Tax Penalty (as hereinafter defined) at a net cost of \$2.4 million in 2017 (direct mining costs and depreciation totaling \$8.0 million, net of service revenue of \$5.6 million) (2016: net cost of \$1.0 million (direct mining costs and depreciation totaling of \$3.1 million, net of service revenue of \$2.1 million) (see section “*Regulatory Issues and Contingencies – Governmental and Regulatory Investigations*” for more details).

In connection with the Arbitration Award involving First Concept, the Company recorded a provision for this commercial arbitration in the amount of \$2.4 million in 2017.

An impairment of \$1.7 million was recorded for certain properties for resale by the Company that were obtained by the Company pursuant to a settlement agreement with one of its major customers in connection with outstanding trade receivables, which reflects the drop in market value.

Administration expenses were \$9.2 million in 2017 as compared to \$7.9 million in 2016, as follows:

<i>\$ in thousands</i>	Year ended December 31,	
	2017	2016
Corporate administration	\$ 2,534	\$ 2,724
Professional fees	2,464	2,022
Salaries and benefits	3,726	2,820
Share-based compensation expense	89	58
Depreciation	368	264
Administration expenses	<u>\$ 9,181</u>	<u>\$ 7,888</u>

The increase in salaries and benefits was mainly due to the increase of headcount during the year, which is to support the expansion of the sales channels in China.

Evaluation and exploration expenses were \$0.3 million in 2017 as compared to \$0.4 million in 2016. The Company continued to minimize evaluation and exploration expenditures in 2017 in order to preserve the Company's financial resources. Evaluation and exploration activities and expenditures in 2017 were limited to ensuring that the Company met the Mongolian Minerals Law requirements in respect of its mining licenses.

A specific impairment charge of \$11.2 million was made for the year ended December 31, 2017 on the deposits related to pending purchases of property, plant and equipment (2016: \$1.2 million).

Finance costs were \$23.0 million and \$22.3 million in 2017 and 2016 respectively, which primarily consisted of interest expense on the \$250.0 million CIC Convertible Debenture.

Finance income remained at \$0.2 million for both 2017 and 2016, which primarily related to unrealized gains on the change in fair value of the embedded derivatives in the CIC Convertible Debenture (\$0.1 million and \$0.2 million for 2017 and 2016, respectively). The fair value of the embedded derivatives in the CIC Convertible Debenture is driven by many factors, including the Company's common share price, the USD and Canadian dollar exchange rate, and share price volatility.

Summary of Quarterly Operational Data

Quarter Ended	2017				2016			
	31-Dec	30-Sep	30-Jun	31-Mar	31-Dec	30-Sep	30-Jun	31-Mar
Sales Volumes, Prices and Costs								
Premium semi-soft coking coal								
Coal sales (millions of tonnes)	0.37	0.12	0.18	0.19	0.15	0.07	–	0.06
Average realized selling price (per tonne) ⁽ⁱ⁾	\$ 50.47	\$ 46.55	\$ 45.67	\$ 45.61	\$ 40.49	\$ 21.04	\$ –	\$ 21.38
Standard semi-soft coking coal								
Coal sales (millions of tonnes)	0.60	0.41	0.79	0.64	0.65	0.77	0.52	0.58
Average realized selling price (per tonne) ⁽ⁱ⁾	\$ 37.49	\$ 28.32	\$ 26.69	\$ 23.36	\$ 16.79	\$ 15.66	\$ 16.27	\$ 18.42
Thermal coal								
Coal sales (millions of tonnes)	0.29	0.27	0.51	0.28	0.28	0.29	0.30	0.24
Average realized selling price (per tonne) ⁽ⁱ⁾	\$ 16.98	\$ 14.48	\$ 15.79	\$ 13.17	\$ 15.26	\$ 14.79	\$ 9.17	\$ 9.19
Total								
Coal sales (millions of tonnes)	1.26	0.80	1.48	1.11	1.08	1.13	0.82	0.88
Average realized selling price (per tonne) ⁽ⁱ⁾	\$ 36.54	\$ 26.41	\$ 25.24	\$ 24.52	\$ 19.55	\$ 15.79	\$ 13.65	\$ 16.11
Raw coal production (millions of tonnes)	0.51	2.47	1.89	1.51	1.21	1.13	0.67	0.37
Cost of sales of product sold (per tonne)	\$ 23.54	\$ 31.31	\$ 18.50	\$ 21.40	\$ 21.15	\$ 19.53	\$ 28.01	\$ 21.62
Direct cash costs of product sold (per tonne) ⁽ⁱⁱ⁾	\$ 9.91	\$ 10.98	\$ 7.84	\$ 9.42	\$ 7.97	\$ 7.13	\$ 12.47	\$ 7.88
Mine administration cash costs of product sold (per tonne) ⁽ⁱⁱⁱ⁾	\$ 4.92	\$ 2.98	\$ 2.22	\$ 1.01	\$ 3.23	\$ 2.26	\$ 2.32	\$ 1.24
Total cash costs of product sold (per tonne) ⁽ⁱⁱⁱ⁾	\$ 14.83	\$ 13.96	\$ 10.06	\$ 10.43	\$ 11.20	\$ 9.39	\$ 14.79	\$ 9.12
Other Operational Data								
Production waste material moved (millions of bank cubic meters)	4.36	6.77	6.36	3.30	2.62	2.22	1.82	0.72
Strip ratio (bank cubic meters of waste material per tonne of coal produced)	8.59	2.74	3.37	2.18	2.16	1.96	2.71	1.94
Lost time injury frequency rate ⁽ⁱⁱⁱ⁾	0.03	0.04	0.04	0.02	0.00	0.00	0.00	0.00

(i) Average realized selling price is presented before deduction of royalties and selling fees.

(ii) A non-IFRS financial measure, see section “Non-IFRS Financial Measures”. Cash costs of product sold exclude idled mine asset cash costs.

(iii) Per 200,000 man hours and calculated based on a rolling 12 month average.

Overview of Quarterly Operational Data

For the fourth quarter of 2017, the Company had a lost time injury frequency rate of 0.03 per 200,000 man hours based on a rolling 12 month average.

As a result of improved market conditions and prices for coal in China, the Company experienced an increase in the average selling price of coal as compared to the fourth quarter of 2016. The Company increased its sales volume from 1.08 million tonnes in the fourth quarter of 2016 to 1.26 million tonnes in the fourth quarter of 2017. The average realized selling price increased from \$19.55 per tonne in the fourth quarter 2016 to \$36.54 per tonne in the fourth quarter of 2017, which was mainly a result of improved market conditions as well as an improved product mix.

Summary of Quarterly Financial Results

The Company's consolidated financial statements are reported under IFRS issued by the International Accounting Standards Board ("IASB"). The following table provides highlights, extracted from the Company's annual and interim financial statements, of quarterly results for the past eight quarters:

<i>\$ in thousands, except per share information</i>	2017				2016			
	31-Dec	30-Sep	30-Jun	31-Mar	31-Dec	30-Sep	30-Jun	31-Mar
Financial Results								
Revenue ^{(i), (ii)}	\$ 41,698	\$ 19,356	\$ 34,665	\$ 25,254	\$ 18,983	\$ 16,379	\$ 10,361	\$ 12,727
Cost of sales ⁽ⁱⁱⁱ⁾	(29,665)	(25,049)	(27,385)	(23,759)	(22,842)	(22,018)	(23,105)	(19,080)
Gross profit/(loss) excluding idled mine asset costs	15,682	(2,094)	9,445	4,714	(2,353)	(3,162)	(9,926)	(1,049)
Gross profit/(loss) including idled mine asset costs	12,033	(5,693)	7,280	1,495	(3,859)	(5,639)	(12,744)	(6,353)
Other operating income/(expenses)	(7,488)	3,477	(4,045)	(3,208)	(3,782)	4,631	812	(1,711)
Administration expenses	(2,111)	(2,451)	(2,234)	(2,385)	(2,378)	(2,042)	(1,826)	(1,642)
Evaluation and exploration expenses	(52)	(48)	(144)	(29)	(222)	(101)	(52)	(47)
Impairment of property, plant and equipment	(11,171)	-	-	-	(1,152)	-	-	-
Profit/(loss) from operations	(8,789)	(4,715)	857	(4,127)	(11,393)	(3,151)	(13,810)	(9,753)
Finance costs	(6,250)	(5,674)	(5,494)	(5,715)	(5,645)	(6,358)	(5,377)	(5,497)
Finance income	143	142	50	4	472	5	324	1
Share of earnings of a joint venture	368	265	388	266	378	89	256	83
Income tax credit/(expense)	781	238	(2,714)	(45)	(1,294)	82	(23)	(235)
Net loss	(13,747)	(9,744)	(6,913)	(9,617)	(17,482)	(9,333)	(18,630)	(15,401)
Basic and diluted loss per share	\$ (0.05)	\$ (0.04)	\$ (0.03)	\$ (0.04)	\$ (0.07)	\$ (0.04)	\$ (0.07)	\$ (0.06)

- (i) Revenue is presented after deduction of royalties and selling fees.
- (ii) Revenue and cost of sales relate to the Company's Ovoot Tolgoi Mine within the Coal Division operating segment. Refer to note 2 of the selected information from the notes to the consolidated financial statements for further analysis regarding the Company's reportable operating segments.

Overview of Quarterly Financial Results

The Company recorded a \$8.8 million loss from operations in the fourth quarter of 2017 compared to a \$11.4 million loss from operations in the fourth quarter of 2016.

Revenue was \$41.7 million in the fourth quarter of 2017 compared to \$19.0 million in the fourth quarter of 2016. The Company sold 1.26 million tonnes of coal at an average realized selling price of \$36.54 per tonne in the fourth quarter of 2017 compared to sales of 1.08 million tonnes at an average realized selling price of \$19.55 per tonne in the fourth quarter of 2016. Revenue increased in the fourth quarter of 2017 compared to the fourth quarter of 2016 as a combined result of the higher sales volumes as well as the improved average selling price.

The Company's revenue is presented after deduction of royalties and selling fees. The Company's effective royalty rate for the fourth quarter of 2017, based on the Company's average realized selling price of \$36.54 per tonne, was 5.9% or \$2.15 per tonne while the Company's effective royalty rate was 7.0% or \$1.36 per tonne based on the average realized selling price of \$19.55 per tonne in the fourth quarter of 2016.

Cost of sales was \$29.7 million in the fourth quarter of 2017 compared to \$22.8 million in the fourth quarter of 2016. Cost of sales comprises operating expenses, share-based compensation expense, equipment depreciation, depletion of mineral properties, coal stockpile inventory impairments and idled mine asset costs. Operating expenses in cost of sales reflect the total cash costs of product sold (a non-IFRS financial measure, see section "Non-IFRS Financial Measures" for further analysis) during the period.

<i>\$ in thousands</i>	Three months ended	
	December 31,	
	2017	2016
Operating expenses	\$ 18,695	\$ 12,095
Share-based compensation recovery	-	(2)
Depreciation and depletion	3,429	9,127
Impairment of coal stockpile inventories	3,892	116
	<hr/>	<hr/>
Cost of sales from mine operations	26,016	21,336
Cost of sales related to idled mine assets	3,649	1,506
	<hr/>	<hr/>
Cost of sales	<u>\$ 29,665</u>	<u>\$ 22,842</u>

Operating expenses included in cost of sales were \$18.7 million in the fourth quarter of 2017 as compared to \$12.1 million in the fourth quarter of 2016. The overall increase in operating expenses was primarily the result of the increase in sales volume from 1.08 million tonnes in the fourth quarter of 2016 to 1.26 million tonnes in the fourth quarter of 2017.

Cost of sales in the fourth quarter of 2017 and the fourth quarter of 2016 included coal stockpile impairments of \$3.9 million and \$0.1 million, respectively, to reduce the carrying value of the Company's coal stockpiles to their net realizable value. The coal stockpile impairments recorded in both years primarily related to the Company's higher-ash content products.

Idled mine asset costs in the fourth quarter of 2017 included depreciation expense for idled mine equipment of \$3.6 million (2016: \$1.5 million).

Other operating expenses were \$7.5 million in the fourth quarter of 2017 (2016: \$3.8 million). In connection with the Arbitration Award involving First Concept, the Company recorded a provision for this commercial arbitration in the amount of \$2.4 million in the fourth quarter of 2017.

<i>\$ in thousands</i>	Three months ended	
	December 31,	
	2017	2016
Provision of commercial arbitration	\$ (2,384)	\$ —
Underprovision of miscellaneous taxes	(1,421)	—
Foreign exchange gain/(loss)	(1,139)	2,281
Impairment of prepaid expenses and deposits	(2,517)	—
Impairment of properties for resale	(643)	—
Reversal of provision/(provision) for doubtful trade and other receivables	629	(2,639)
Mining services, net	—	(1,006)
Settlement of civil claims	—	(2,362)
Other	(13)	(56)
Other operating expenses	<u>\$ (7,488)</u>	<u>\$ (3,782)</u>

Administration expenses were \$2.1 million in the fourth quarter of 2017 as compared to \$2.4 million in the fourth quarter of 2016. The increase in salaries and benefits was mainly due to the increase of headcount during the year, which is to support the expansion of the sales channel in China.

<i>\$ in thousands</i>	Three months ended December 31,	
	2017	2016
Corporate administration	\$ 579	\$ 689
Professional fees	505	727
Salaries and benefits	891	787
Share-based compensation expense	22	26
Depreciation	114	149
	<hr/>	<hr/>
Administration expenses	<u>\$ 2,111</u>	<u>\$ 2,378</u>

Evaluation and exploration expenses were \$0.1 million in the fourth quarter of 2017 as compared to \$0.2 million in the fourth quarter of 2016. The Company continued to minimize evaluation and exploration expenditures in order to preserve the Company's financial resources. Evaluation and exploration activities and expenditures in the fourth quarter of 2017 were limited to ensuring that the Company met the Mongolian Minerals Law requirements in respect of its mining licenses.

Finance costs were \$6.3 million in the fourth quarter of 2017 compared to \$5.6 million in the fourth quarter of 2016, which primarily consisted of interest expense on the CIC Convertible Debenture.

Finance income was \$0.1 million in the fourth quarter of 2017 compared to \$0.5 million in the fourth quarter of 2016, which primarily consisted of unrealized gains on the fair value change of the embedded derivatives in the CIC Convertible Debenture. The fair value of the embedded derivatives in the CIC Convertible Debenture is driven by many factors, including the Company's common share price, the USD and Canadian dollar exchange rates and share price volatility.

RESOURCE AND RESERVE ESTIMATE – OVOOT TOLGOI MINE

Resource

The term "resource" is utilized to quantify coal contained in seams occurring within specified limits of thickness and depth from surface considered by the Qualified Person to have reasonable prospects for eventual economic extraction. For a complete description of a resource, refer to "mineral resource" under the heading "DEFINITIONS AND OTHER INFORMATION – Glossary of Geological and Mining Terms" in the Company's Annual Information Form dated March 31, 2017. The resource estimates presented are on an in-place basis, i.e., without adjustment for mining losses or coal recovery. Minimum seam thickness and maximum parting thickness are considered and coal intervals not meeting these criteria are not included in the reported resources.

In accordance with National Instrument 43-101 of the Canadian Securities Administrators (“NI 43-101”), Dragon Mining Consulting Limited (“DMCL”) has made reference to the GSC Paper 88-21 during the classification, estimation and reporting of coal resources for the Ovoot Tolgoi deposit. The exercise of resource classification is initially made based on the Geology-Type of the coal deposits as defined in the GSC Paper 88-21. According to the level of confidence of coal resource existence and data density, the resources are further classified into three categories respectively: Measured, Indicated and Inferred. These were considered by the Qualified Person during the classification of the resources at the Ovoot Tolgoi deposit.

As a consequence of material changes in some key assumptions underlying the analysis of its resources subsequent to the last detailed review of the project in 2016, particularly those relating to ongoing changes in coal market conditions in China, geologic analysis, optimized mining strategy and processing strategy, the Company has updated its resource and reserve estimate for the Ovoot Tolgoi deposit.

The resource estimate presented in this announcement is materially different from the previous estimate made in the technical report entitled “Coal Geology and Resources, Ovoot Tolgoi Deposit, Mongolia – SouthGobi Resources Ltd” dated May 6, 2016 prepared by Minacro-MineConsult (known as RungePincoMinarco as of the date of such report) (the “2016 Technical Report”) due to the following factors:

- The Geology Type classification has been re-categorized from “Severe” to “Complex”, which led to a different requirement of spatial distribution of geological data and thus resource categorization according to GSC 88-21. Resource categories have been re-classified accordingly and this has resulted in the re-designation of Measured Resources in the overall resource portfolio of SGS.
- In-pit (surface) resources have been more conservatively constrained to a depth of 300m from the ground surface, compared to a depth of 350m used in the 2016 Technical Report.
- Underground resources have been re-established, as resources and considered to be a reasonable prospect for eventual economic extraction due to recovering coal market conditions in China and Company’s long-term plan for a thermal power plant for a location near the mine site which is expected to generate substantial demand for thermal coal for electricity generation.
- A more conservative approach was adopted, compared to the last technical report in 2012 that contemplated potential economic extraction for the underground portion of the Ovoot Tolgoi deposit (the “2012 Technical Report”), such that only underground resources to a depth of 500m were considered to be of a reasonable prospect for eventual economic extraction.

Resources have been estimated for the Ovoot Tolgoi deposit as of December 31, 2016, including Measured Resources of 201.9 million tonnes (“Mt”), Indicated Resources of 100.3 Mt and Inferred Resources of 89.0 Mt.

Resource categorization was completed on a Seam Group basis. The resource categorization also took into account the continuity and confidence in drill hole intersections along each section.

The estimate of resources at the Ovoot Tolgoi deposit is summarized in the following table.

Ovoot Tolgoi Deposit – Surface Resource Estimate

Coalfield	Seam Group	Resource (Mt)		
		Measured	Indicated	Inferred
Sunrise Pit (depth <300m)	7	2.2	2.9	2.0
	6	3.4	4.8	4.2
	5U	39.6	20.5	22.6
	5L	18.2	4.1	1.0
	4	0.4	0.7	0.6
	subtotal	63.8	33.0	30.4
Sunset Pit (depth <300m)	11	0.1	–	–
	10	8.8	2.1	0.1
	9	17.8	3.4	0.2
	8	16.4	3.2	0.3
	5U	25.6	6.3	0.3
	5L	11.8	2.3	0.8
	subtotal	80.5	17.3	1.7
Grand Total		144.3	50.3	32.1

Totals may not add up due to rounding.

Ovoot Tolgoi Deposit – Underground Resource Estimate

Coalfield	Seam Group	Resource (Mt)		
		Measured	Indicated	Inferred
Sunrise (depth 300m to 500m)	5U	2.0	4.9	13.1
	5L	6.0	12.0	25.0
	Total	8.0	16.9	38.1
Sunset (depth 300m to 500m)	10	3.0	1.9	–
	9	6.2	4.6	0.4
	8	6.9	3.8	2.2
	5U	27.9	14.9	3.4
	5L	5.6	7.9	12.8
	Total	49.6	33.1	18.8
Grand Total		57.6	50.0	56.9

Totals may not add up due to rounding.

Resources have been estimated as of December 31, 2016 using the Minex™ models provided by SGS. The key assumptions used for the resource estimation are:

- Minimum coal thickness = 0.6m;
- Maximum coal parting = 0.3m;
- Surface resources were constrained to a depth of 300m, the same as the pit design used in the 2012 Technical Report;
- Volumes were converted to tonnages using laboratory relative density analytical results converted to an estimated in-situ basis;
- Resources were constrained to the mining lease held by SGS only;
- Resources were estimated on an in-situ basis (i.e. as an in-situ tonnage and not adjusted for mining recovery);
- Resources were depleted by mined out tonnage; and
- Resources were estimated based on the survey data made available as of December 20, 2016 for the Sunrise and Sunset coalfields.

The resource estimate for the Ovoot Tolgoi deposit was derived from the Ovoot Tolgoi Technical Report, which was prepared by DMCL on behalf of the Company. A copy of the Ovoot Tolgoi Technical Report was filed under the Company's profile on SEDAR at www.sedar.com on May 15, 2017.

Reserves

The Company previously reported 175.7 Mt of proven and probable reserves in respect of the Ovoot Tolgoi deposit based on the 2012 Technical Report. Subsequently, the total resources estimated for the Ovoot Tolgoi deposit in the 2016 Technical Report significantly decreased from the 2012 Technical Report principally due to the exclusion of previously estimated underground resources, which were assessed as not having a reasonable prospect for eventual economic extraction. In response to the declining coal prices and weak coal transaction conditions in China, the previously established underground resource at the Ovoot Tolgoi Deposit was not considered to be reasonably economically viable in the 2016 Technical Report, significantly reducing the Company's reported resources, which, together with the reclassification of the Geology Type of the deposit from "Complex" to "Severe", eliminated the Company's mineable reserves that had previously been established for the Ovoot Tolgoi deposit.

In late 2016, the Company and DMCL engaged in a comprehensive review of all relevant information including technical data, mining strategy, pit optimization, mine design, production scheduling, coal processing strategy, sales strategy, coal prices and recovering coal transaction conditions, in order to prepare and update its resources and reserve estimates and prepare a new mine plan. This process resulted in re-estimation of reserves by DMCL which appears in the table below.

The reserve estimate presented below is derived from the Ovoot Tolgoi Technical Report and is materially different from the previous estimate made in the 2016 Technical Report due to the following factors:

- The Geology Type classification has been re-categorized from “Severe” to “Complex”, which led to a different requirement of spatial distribution of geological data and thus resource categorization according to GSC 88-21. Resource categories were re-classified accordingly such that portions of the Indicated and Inferred Resources were reclassified as Measured and Indicated Resources respectively. Such resource reclassification further resulted in the fact that the overall resource estimation and classification could be used in mine planning in conformity with the industry practice and NI 43-101 requirements; and
- In-pit (surface) resources are more conservatively constrained to a depth of 300m from the ground surface, compared to a depth of 350m used in the 2016 Technical Report.

Ovoot Tolgoi Deposit – Reserve Estimate

Pit	Seam Group	Reserve (Mt)		Total
		Proven	Probable	
Sunrise Pit	7	0.4	0.5	0.9
	6	1.7	1.4	3.1
	5U	29.3	6.3	35.6
	5L	12.4	1.7	14.1
	4	0.4	0.5	0.9
	Sub-total	44.3	10.3	54.6
Sunset Pit	11	0.1	–	0.1
	10	5.0	0.6	5.6
	9	10.2	0.5	10.7
	8	10.4	0.5	10.9
	5U	21.1	1.8	22.9
	5L	8.6	0.9	9.5
	Sub-total	55.2	4.3	59.5
Grand Total		99.5	14.6	114.1

Totals may not add up due to rounding.

The above estimate of Reserves at the Ovoot Tolgoi deposit have been estimated as of December 31, 2016 based on the resource model provided by SGS. Measured and Indicated Resources are inclusive of those Mineral Resources modified to produce the Reserves, i.e., Reserves are not additional to Resources.

The key assumptions used for the reserve estimation are:

- The reserve estimation used coal selling prices provided by an independent market consulting firm which was commissioned by the Company in December 2016 and subsequently confirmed as reasonable and appropriate by the qualified person responsible for this reserve estimate;
- Reserves do not include any Inferred Resources which have been treated as waste (i.e. their mining costs have been covered but no revenue has been assumed for the Inferred Resources);
- A recovery factor of 95% and a dilution factor of 2.5% have been applied in the Reserve estimate;
- The pits design (and thus Reserves) was designed to a depth of 300m below the original ground surface, which is same as the pit design used in the 2012 Technical Report;
- Reserves are constrained to the mining lease held by SGS only although the open pit limits will extend across the lease boundary into the adjacent lease held by Mongolyn Alt Corporation (“MAK”). SGS and MAK have an agreement in place that allows SGS to strip off the overburden in MAK’s lease. Coal within the pits and within the MAK’s lease has been treated as generating no revenue and having no associated cost whereas the waste within the pits and MAK’s lease will be stripped off at SGS’ cost; and
- Reserves are estimated to account for coal and waste that was mined as of December 31, 2016.

The reserve estimate for the Ovoot Tolgoi deposit was derived from the Ovoot Tolgoi Technical Report, which was prepared by DMCL on behalf of the Company. A copy of the Ovoot Tolgoi Technical Report was filed under the Company’s profile on SEDAR at www.sedar.com on May 15, 2017.

Mining Operations

Mining Method

The mining method employed at the Ovoot Tolgoi deposit could be described as open pit terrace mining utilizing large scale hydraulic excavators and shovels and trucks. Terrace mining is utilized where coal seams dip steeply and operating machinery on the coal seam roof and floor is not possible, due to the steep seam dips. Terraces, or benches, are excavated along fixed horizontal horizons and these benches intersect both coal and waste. Coal and waste are mined separately on each bench with dozers being used, as needed, to push coal or waste down to the excavator for loading onto trucks. This mining method allows large scale open pit mining to occur productively in steeply dipping coal seam environments. All waste is dumped ex-pit, as the steep dips preclude in-pit dumping.

The open pit limits extend across the Ovoot Tolgoi Mining Licence boundary into the adjacent lease held by MAK. As described previously, the Company and MAK have a cooperation agreement in place to allow mining across the boundary, which stipulates that SGS is responsible for removal of MAK waste but MAK is responsible for mining of MAK coal. Accordingly, the current reserve estimate does not include any coal within the MAK lease that must be extracted as part of the Company mining operation. Therefore in the current mine plan, no revenue has been assumed for the MAK coal whereas costs have been assumed for stripping off the MAK waste.

LIQUIDITY AND CAPITAL RESOURCES

Liquidity and Capital Management

The Company has in place a 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.

Turquoise Hill Resources Ltd. ("Turquoise Hill") shareholder loan (the "TRQ Loan")

On May 25, 2014, the Company announced it obtained the TRQ Loan in the form of a \$10 million revolving credit facility to meet its short term working capital requirements. The terms and conditions of this facility were filed on SEDAR (www.sedar.com) on June 2, 2014. 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 \$0.1 million.

During 2014 to 2016, the due date of the TRQ Loan, was extended several times and the maximum amount of the facility was reduced to \$3.8 million.

On May 16, 2016, the Company and Turquoise Hill entered into a deferral agreement (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) \$0.15 million per month from May 2016 to April 2017; (ii) \$0.2 million per month from May 2017 to December 2017; and (iii) the remaining balance on December 29, 2017 (the payments in (i) 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 September, 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 of this press release, 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 of this press release, 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 December 31, 2017, the outstanding principal and accrued interest under this facility amounted to \$1.0 million and \$0.7 million, respectively (at December 31, 2016, the outstanding principal and accrued interest under this facility amounted to \$2.2 million and \$0.7 million, respectively).

Equipment Loan

Inner Mongolia SouthGobi Energy Ltd., a subsidiary of the Company, executed a \$10.4 million 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 \$10.4 million;
- 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 December 31, 2017, the outstanding principal and accrued interest for the equipment loan amounted to \$2.3 million and \$0.1 million, respectively (December 31, 2016: nil).

A loan arrangement fee of 1% of the loan principal drawn was charged and will be amortized throughout the loan term. For the year ended December 31, 2017, \$8,000 of loan arrangement fee was amortized (2016: 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 of the press release.

Bank loan

On May 6, 2016, SGS obtained a bank loan (the "Bank Loan") in the principal amount of \$2.0 million 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 \$3.0 million;
- \$2.3 million of the principal amount will mature on May 6, 2018 while the remaining balance of the principal amount of \$0.7 million will mature on January 4, 2019;
- Interest rate of 15.8% per annum applies to the \$2.3 million portion of the principal amount, while an interest rate of 15.0% per annum applies to the remaining \$0.7 million portion of the principal amount; in each case, interest is payable monthly; and
- Certain items of property, plant and equipment with value of \$4.5 million as at December 31, 2017 were pledged as security.

As at December 31, 2017, the outstanding balance for the Bank Loan was \$3.0 million (December 31, 2016: \$2.0 million) and the Company owed accrued interest of \$0.1 million (December 31, 2016: \$0.1 million).

Short-term bridge loan

On October 27, 2015, the Company executed a \$10.0 million bridge loan agreement with an independent Asian based private equity fund. The bridge loan accrues interest at a rate of 8% per annum with interest payable upon the repayment of loan principal.

The Company repaid the first tranche of the short-term bridge loan with interest of \$5.0 million up to August 11, 2016. During June and July 2016, the Company drew the second tranche of \$5.0 million, of which \$1.5 million was to mature in March 2017 and \$3.5 million was to mature in April 2017. In December 2016, \$1.5 million was repaid for the short-term bridge loan and a further \$1.8 million and \$1.6 million was subsequently repaid in January 2017 and March 2017, respectively and the loan principal was fully settled. The outstanding interest was settled in April 2017.

A loan arrangement fee of 5% of the loan principal drawn was charged, totaling \$0.3 million for the loans drawn during June and July 2016 and amortized throughout the loan term. For the year ended December 31, 2017, \$0.1 million of loan arrangement fee was amortized (2016: \$0.2 million).

Costs reimbursable to Turquoise Hill

Prior to the completion of the private placement with Novel Sunrise on April 23, 2015, Rio Tinto plc ("Rio Tinto") was the Company's ultimate parent company. In the past, Rio Tinto sought reimbursement from the Company for the salaries and benefits of certain Rio Tinto employees who were assigned by Rio Tinto to work for the Company, as well as certain legal and professional fees incurred by Rio Tinto in relation to the Company's prior internal investigation and Rio Tinto's participation in the tripartite committee. Subsequently Rio Tinto transferred and assigned to Turquoise Hill its right to seek reimbursement for these costs and fees from the Company.

As at December 31, 2017, the amount of reimbursable costs and fees claimed by Turquoise Hill (the "TRQ Reimbursable Amount") amounted to \$8.1 million (such amount is included in the aging profile of trade and other payables set out below). On October 12, 2016, the Company received a letter from Turquoise Hill, which proposed an arrangement for regular payments of the outstanding TRQ Reimbursable Amount. The Company has been in negotiations with Turquoise Hill regarding the proper quantum of the TRQ Reimbursable Amount and the terms for repayment. There can be no assurance, however, that any such terms can be successfully negotiated by the Company either at all or on favorable terms.

Going concern considerations

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 December 31, 2018 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 \$166.3 million as at December 31, 2017 compared to \$59.4 million of working capital deficiency as at December 31, 2016. Included in the working capital deficiency at December 31, 2017 are significant obligations, which include obligation to pay CIC under the June 2017 Deferral Agreement in which the Company was required to pay \$9.7 million of cash interest and associated costs on November 19, 2017. In addition, pursuant to the terms of CIC Convertible Debenture, the Company was required to pay \$8.1 million of anniversary cash interest on November 19, 2017. The Company is in discussions with CIC for a deferral of the November 19th Payments; 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.

Pursuant to the Arbitration Award, SGS has been ordered to repay the sum of \$11.5 million 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. In the event that First Concept applies to enforce the Arbitration Award against SGS, the Company intends to defend itself against such enforcement proceedings through independent litigation counsel, however, due to the inherent uncertainties of litigation, it is not possible to predict whether the Company will be successful in defending itself against any such enforcement proceedings. If First Concept is successful in enforcing the Arbitration Award, the Company may not be able to re-pay the sum of \$11.5 million 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 \$11.5 million 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, 2016, as follows:

<i>\$ in thousands</i>	As at December 31,	
	2017	2016
Less than 1 month	\$ 20,664	\$ 14,640
1 to 3 months	16,132	2,493
3 to 6 months	8,825	2,648
Over 6 months	<u>33,598</u>	<u>23,847</u>
Total trade and other payables	<u>\$ 79,219</u>	<u>\$ 43,628</u>

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 March 28, 2018.

The Company also has other current liabilities, which require settlement in the short-term, including: the \$1.7 million balance of the TRQ Loan; the principal amount of the Bank Loan of \$2.3 million and associated interest due in May 2018 and the principal amount of the Equipment Loan of \$2.3 million 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 December 31, 2018, 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 of this press release, 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, at 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 of this press release, 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. In addition, 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. If SGS fails to satisfy the Arbitration Award, First Concept intends to enforce the Arbitration Award against SGS and, if First Concept is successful in enforcing the Arbitration Award, the Company may not be able to re-pay the sum of \$11.5 million and the associated interest. Furthermore, continuing delay in securing additional financing could ultimately result in an event of default of the Equipment Loan and the Bank Loan, which if not cured within applicable cure periods in accordance with the terms of respective instruments, 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 and the lender of the Bank Loan, respectively.

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 December 31, 2017, the Company's gearing ratio was 0.02 (2016: 0.37), which was calculated based on the Company's long term liabilities to total assets. As at December 31, 2017 and December 31, 2016, the Company is not subject to any externally imposed capital requirements.

As at March 28, 2018, the Company had \$7.1 million of cash.

CIC Convertible Debenture

In November 2009, the Company entered into a financing agreement with a wholly owned subsidiary of CIC for \$500 million in the form of a secured, convertible debenture bearing interest at 8.0% (6.4% payable semi-annually in cash and 1.6% payable annually in the Company's shares) with a maximum term of 30 years. The CIC Convertible Debenture is secured by a first ranking charge over the Company's assets and certain subsidiaries. The financing was used primarily to support the accelerated investment program in Mongolia and for working capital, repayment of debt, general and administrative expenses and other general corporate purposes.

On March 29, 2010, the Company exercised its right to call for the conversion of up to \$250.0 million of the CIC Convertible Debenture into approximately 21.5 million shares at a conversion price of \$11.64 (CAD\$11.88). As at December 31, 2017, CIC owned, through its indirect wholly owned subsidiary, approximately 23.8% of the issued and outstanding Common Shares of the Company.

On June 12, 2017, the Company executed the June 2017 Deferral Agreement with CIC for a revised repayment schedule on 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 \$2.2 million 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 \$9.7 million 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.

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 \$8.1 million of anniversary cash interest to CIC on November 19, 2017. Pursuant to the CIC Convertible Debenture, the Company was also obliged to issue \$4.0 million worth of November 2017 PIK Interest shares to CIC on November 19, 2017.

As of the date of this press release, 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, at 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 of this press release, 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 discussions with CIC for a deferral of the November 19th Payments and the November 2017 PIK Interest; however, there can be no assurance that a favorable outcome will be reached. As part of these discussions, 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 of this press release.

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.

As a consequence of the Company not entering into a deferral agreement with CIC as at December 31, 2017, IAS 1 requires the Company to classify the entire balance of the CIC Convertible Debenture as a current liability as at December 31, 2017, 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.

Commercial Arbitration in Hong Kong

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 \$11.5 million.

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 \$11.5 million (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 December 31, 2017, the Company has recorded a provision of \$13.9 million for the commercial arbitration. (2016: nil, during which the \$11.5 million in relation to First Concept was recorded in deferred revenue).

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. The Company is currently considering and reviewing its options with respect to the Arbitration Award, including exploring ways to work together 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 any event, if SGS fails to satisfy the Arbitration Award, First Concept may apply to enforce the Arbitration Award against SGS through judicial measures in courts of Mongolia or in other applicable jurisdiction(s). In the event that First Concept applies to enforce the Arbitration Award against SGS through judicial measures in courts of Mongolia or in other applicable jurisdiction(s), the Company intends to defend itself against such enforcement proceedings through independent litigation counsel retained by the Company for this purpose. However, due to the inherent uncertainties of litigation, it is not possible to predict whether the Company will be successful in defending itself against any such enforcement proceedings.

If First Concept is successful in enforcing the Arbitration Award against SGS, the Company may not be able to re-pay the sum of \$11.5 million 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 \$11.5 million and associated interest to First Concept could result in voluntary or involuntary proceedings involving the Company (including bankruptcy).

Ovoot Tolgoi Mine Impairment Analysis

The Company determined that an indicator of impairment existed for its Ovoot Tolgoi Mine cash generating unit as at December 31, 2017. 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 and washing assumptions, operating cost and life of mine coal production assumptions as at December 31, 2017. The Company's Ovoot Tolgoi Mine cash generating unit carrying value was \$86.9 million as at December 31, 2017.

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 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 15.5% based on an analysis of the market, country and asset specific factors.

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 December 31, 2017. 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.

REGULATORY ISSUES AND CONTINGENCIES

Governmental and Regulatory Investigations

In May 2016, the Resolution 258 was issued by the Government of Mongolia, which approved the Company's proposal to partially settle a prior written verdict of the Mongolian Second District Criminal Court which declared SGS to be financially liable as a "civil defendant" for a penalty (the "Tax Penalty") of MNT 35.3 billion (approximately \$18.2 million on February 1, 2015) by way of certain cash payments in 2016 and 2017 and by the Company performing certain mining operations at the Tavan Tolgoi deposit on behalf of Erdenes.

In compliance with Resolution 258, in November 2016, the Company entered into an agreement with Erdenes under which the Company agreed to perform certain mining operations equivalent to MNT 20.3 billion (approximately \$8.1 million) in the West Tsankhi section of the Tavan Tolgoi deposit during the period from November 2016 to February 2017. In February 2017, the Company completed mining operations at the Tavan Tolgoi deposit equivalent to MNT 20.3 billion (approximately \$8.1 million) as set out in the agreement with Erdenes.

On January 10, 2018, SGS was informed by the Court Decision Implementation Agency of Capital City in Mongolia that the enforcement procedure in relation to the Tax Verdict has been terminated and no party shall have any right to make any further claims in connection with the Tax Verdict. As of the date hereof, SGS has fulfilled its obligations under the Tax Verdict.

The decrease from the initial \$18.2 million owing as of February 1, 2015 is as a result of transfers from frozen bank accounts of \$1.2 million, additional cash payments by the Company of \$5.4 million, the provision of mining services at the Tavan Tolgoi deposit of \$8.1 million and the foreign exchange adjustments.

Mongolia's Independent Authority Against Corruption (the "IAAC") Investigation

In the first quarter of 2013, the Company was subject to orders imposed by 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 investigations of the Company as described under the section entitled "Governmental and Regulatory Investigations" above. The restrictions on the assets were reaffirmed in the Tax Verdict and formed part of the Tax Penalty payable by the Company.

Following the termination of enforcement procedures in relation to the Tax Verdict, the orders imposed by the IAAC were removed on January 10, 2018.

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 Company’s restatement of certain financial statements previously disclosed in the Company’s public filings (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 May, 2018. If leave to appeal is granted, the appeal would likely be scheduled to be heard in early 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 December 31, 2017 was not required.

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 had a duration of five years from commencement of the contract and provided 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 \$18.5 million. At each reporting date, the Company assesses the agreement with Ejin Jinda and has determined it is not probable that these \$18.5 million will be required to be paid. Accordingly, the Company has determined a provision for this matter at December 31, 2017 is not required.

Mining Prohibition in Specified Areas Law

In July 2009, Mongolia promulgated the Law on Prohibiting Mineral Exploration and Extraction Near Water Sources, Protected Areas and Forests (the “Mining Prohibition in Specified Areas Law”). Pursuant to the Mining Prohibition in Specified Areas Law, the Government of Mongolia has defined the boundaries of certain areas in which exploration and mining is purportedly prohibited. A list of licenses was prepared that overlap with the prohibited areas described in the law based on information submitted by water authority agencies, forest authority agencies and local authorities for submission to the Government of Mongolia.

In order to address the issues facing its implementation, in February 2015 the Parliament of Mongolia adopted an amendment to the Law on Implementation of the Mining Prohibition in Specified Areas Law (the “Amended Law on Implementation”). The Amended Law on Implementation provided an opportunity for license holders covered within the scope of application of the Mining Prohibition in Specified Areas Law to continue their mining operations subject to advance placement of funds to cover 100% of the future environmental rehabilitation costs. A model contract and a specific Government regulation on this requirement will be adopted by the Government. The license holders were required to apply within 3 months after the amendment to the Law on Implementation came into effect for permission to the Mineral Resources Authority of Mongolia to resume activities. The Company considered that its development projects may be affected, but not its operating mines. The Company submitted its application with respect to its mining licenses before the deadline set on June 16, 2015.

Pursuant to the Mongolian Law “To prohibit mineral exploration and mining operations at headwaters of rivers, water protection zones and forested areas”, the Government administrative agency has notified the Company that special license area 12726A is partly overlapping with a water reservoir. The Company has inspected the area together with the Cadastral Division of the Mineral Resource Authority as well as through the cadastral registration system of the Ministry of Environment, and determined that 29 hectares of Sukhait Bulag was partly overlapping with a water reservoir, of which has been partly handed over. (Resolution No.6/7522 issued on September 29, 2015 by the Head of Cadastral Division of the Mineral Resource Authority).

In accordance with Article 22.3 of Law of Mongolia on Water, 5,602.96 hectares of land, including Sukhaityn Bulag, Uvur Zadgai, and Zuun Shand pertaining to exploration license 9443X, which was converted to mining license MV-0125436 in January 2016, was overlapping with a protected area boundary. The overlapping area has been officially handed over to the local administration. (Resolution No.688 issued on September 24, 2015 by the Head of Cadastral Division of the Mineral Resource Authority). In connection with the nullification of Annex 2 of Government order No.194 “On determining boundary” issued on June 5, 2012, the area around the water reservoir located at MV-016869 license area and Soumber exploration license 9449X, which was converted to mining license MV-020451 in January 2016, was annulled from the Specified Area Law.

Therefore, mining licenses 12726A and MV-016869 and exploration licenses 9443X and 9449X were removed from the list of licenses that overlaps with the prohibited areas described in the law.

Areas specified in all 6 of the Company’s mining licenses do not overlap with any areas provided in the “Law on prohibition of mineral exploration and mining operations at headwaters of rivers, water protection zones and forested areas” as referenced in No.194 Resolution dated 2012 and No.289 Resolution dated 2015 of the Government of Mongolia.

There has been limited development of the law since 2016, while two exploration licenses of the Company (13779X and 5267X) were converted to mining licenses (MV-020676 and MV-020675) in November 2016. The Company will continue to monitor the developments and ensure that it follows the necessary steps in the Amended Law on Implementation to secure its operations and licenses and is fully compliant with Mongolian law.

Special Needs Territory in Umnugobi

On February 13, 2015, the entire Soumber mining license and a portion of SGS’ exploration license 9443X (9443X was converted to mining license MV-020436 in January 2016) (the “License Areas”) were included into a special protected area (to be further referred as Special Needs Territory, the “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.

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. Mining activities at the Soumber property cannot proceed until the License Areas are removed from the SNT.

On June 29, 2016, the Mongolian Parliament and CRKh election was held. As a result, the Company was aware that additional action may be taken in respect of the SNT; however, the Company has not yet received any indication on the timing of the next session of the CRKh.

Settlement of Lawsuit Notice from a Former Fuel Supplier

On June 30, 2017, the Company signed the Triparty Settlement Agreement with MTLLC and ICIC pursuant to which: (i) MTLLC transferred to ICIC its right to receive payment from the Company of the Outstanding Amount and its right to enforce the arbitration award against the Company in connection therewith; and (ii) the Company and ICIC agreed to a revised payment schedule for repayment of the Outstanding Amount. Pursuant to the Triparty Settlement Agreement, the Company will pay interest on the Outstanding Amount, which shall accrue at a monthly rate of 1.8% and will be settled on a monthly basis. The Company was required to repay on average \$1.3 million monthly during the period from July 2017 to November 2017 pursuant to the Triparty Settlement Agreement.

As of the date of this press release, the Company has fulfilled its obligations under the Triparty Settlement Agreement and has fully repaid the Outstanding Amount.

Mongolian royalties

During the year ended December 31, 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.

Management believes that its interpretation of the relevant legislation is appropriate and the Company's positions related to royalty will be sustained. As of December 31, 2017, recognition of a provision for addition Mongolian royalties is not necessary.

TRANSPORTATION INFRASTRUCTURE

On August 2, 2011, the State Property Committee of Mongolia awarded the tender to construct a paved highway from the Ovoot Tolgoi Mine to the Shivee Khuren Border Crossing (the "Paved Highway") to consortium partners NTB LLC and SGS (together referred to as "RDCC LLC"). The Company has an indirect 40% shareholding in RDCC LLC through its Mongolian subsidiary SGS.

On October 26, 2011, RDCC LLC signed a concession agreement with the State Property Committee of Mongolia. RDCC LLC has the right to conclude a 17 year build, operate and transfer agreement under the Mongolian Law on Concessions.

On May 8, 2015, the commercial operation of the Paved Highway commenced. The Paved Highway has significantly increased the safety of coal transportation, reduced environmental impacts and improved efficiency and capacity of coal transportation. The toll rate was set at MNT 900 per tonne of coal (subsequently increased) as compared to MNT 1,500 as stated in the signed concession agreement between RDCC LLC and the State Property Committee of Mongolia.

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.

On February 4, 2017, the Board of RDCC LLC increased the toll rate from MNT 900 per tonne of coal to MNT 1,200, effective from March 1, 2017.

The Paved Highway has a carrying capacity in excess of 20 million tonnes of coal per year.

For the three months ended and the year ended December 31, 2017, RDCC LLC recognized toll fee revenue of \$1.8 million (2016: \$1.7 million) and \$6.1 million (2016: \$5.0 million), respectively.

PURCHASE, SALE OR REDEMPTION OF THE COMPANY'S LISTED SECURITIES

The Company did not redeem its listed securities nor the Company or any of its subsidiaries purchase, or sell such securities during the year ended December 31, 2017.

CORPORATE GOVERNANCE PRACTICES

The Company has, throughout the year ended December 31, 2017, applied the principles and complied with the requirements of its corporate governance practices as defined by the Board and all applicable statutory, regulatory and stock exchange listings standards, which include the code provisions set out in the Corporate Governance Code (the “Corporate Governance Code”) as set out in Appendix 14 to the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the “Hong Kong Stock Exchange” and the “Hong Kong Listing Rules”, respectively), except for the following:

Pursuant to code provision E.1.2 of the Corporate Governance Code, the chairman of the board of directors should attend the annual general meeting. However, Mr. Ningqiao Li, the former Executive Chairman, was unable to attend the AGM due to other significant business commitments. In the absence of the Executive Chairman, Mr. Mao Sun, an independent non-executive director and the Interim Independent Lead director (the “Lead Director”), acted as chairman of the AGM to ensure an effective communication with the shareholders.

Pursuant to code provision A.2.7 of the Corporate Governance Code, the chairman of the Board should at least annually hold meetings with the non-executive directors (including independent non-executive directors) without the executive directors present. There were no standalone meetings between the former Executive Chairman with the non-executive directors without the other executive directors present during the period from January 1, 2017 to June 30, 2017, being the date of the retirement of the former Executive Chairman as a director. However, the opportunity for such communication channel was always offered at the end of the Board meetings. The Company does not have a Chairman since the conclusion of the AGM held on June 30, 2017. A meeting between the Chairman (if any) or the Lead Director who is fulfilling the duties of the Chairman and the non-executive directors will be scheduled for 2018 and annually going forward.

SECURITIES TRANSACTIONS BY DIRECTORS

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 for Securities Transactions by Directors of Listed Issuers contained in Appendix 10 to the Hong Kong Listing Rules.

In response to a specific enquiry made by the Company on each of the directors, all directors, except Mr. Aminbuhe whom was not able to confirm because of his current situation (refer to the section “Changes in Management and Directors” under the heading “Significant Events and Highlights”), confirmed that they had complied with the required standards as set out in the Model Code and in the Company’s Corporate Disclosure, Confidentiality and Securities Trading Policy throughout the year ended December 31, 2017.

EMPHASIS OF MATTER – GOING CONCERN ASSUMPTION

Without qualifying their opinion, the auditors' report is likely to include a paragraph to draw the attention of the Company's shareholders to notes to the consolidated financial statements which indicate that several adverse conditions and material uncertainties cast significant doubt upon the going concern assumption. 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 December 31, 2018 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 December 31, 2018, 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. As a result, it may not be able to continue as a going concern.

OUTLOOK

Following the termination of enforcement procedures in relation to the Tax Verdict in January 2018, the dispute giving rise to the Tax Verdict has been fully resolved. The Company will continue to work closely with the Mongolian authorities to ensure compliance with all applicable Mongolian rules and regulations.

With the implementation of the "One Belt, One Road" program in China, the Company is well positioned to capture the resulting business opportunities between the two countries given the potential strategic support from its largest shareholders (CIC and Cinda), which are both state-owned-enterprises in China, and its strong operational record for the past ten years in Mongolia, being one of the largest enterprises in the country.

Assuming the successful launching of the Company's processing facilities in the coming months, the Company expects to produce and sell higher volumes of higher-quality coal products to the Chinese market at improved margins. The Company will continue to strive for revenue growth by expanding its customer base further inland into China.

Looking forward to 2018, the Company remains cautiously optimistic regarding the Chinese coal market.

The Company continues to make efforts to strengthen cost management to ensure operating efficiency.

The Company remains well positioned in the market, with a number of key competitive strengths, including:

- **Bridge between Mongolia and China** – The Company is well positioned to capture the resulting business opportunities between the two countries given the potential strategic support from its largest shareholders (CIC and Cinda), which are both state-owned-enterprises in China, and its strong operational record for the past ten years in Mongolia, being one of the largest enterprises in the country.
- **Strategic location** – The Ovoot Tolgoi Mine is located approximately 40km from China, which represents the Company's main coal market. The Company has an infrastructure advantage, being approximately 50km from a major Chinese coal distribution terminal with rail connections to key coal markets in China.
- **A large resources and reserves base** – As a result of work performed by DMCL for the Ovoot Tolgoi Deposit, the Company's aggregate coal resources include measured and indicated mineral resources of 194.6 million tonnes and inferred resources of 32.1 million tonnes while 114.1 million tonnes were declared as mineral reserves.
- **Several growth options** – The Company has several growth options including the Soumber Deposit and Zag Suuj Deposit, located approximately 20km east and approximately 150km east of the Ovoot Tolgoi Mine, respectively.

Objectives

The Company's objectives for 2018 and the medium term are as follows:

- **Enhance product mix** – The Company is committed to enhancing the product quality by completing the commissioning of the new wash plant, and completing a study of refurbishing, completing and implementing certain components of the former dry coal handling facility, which would enable the processing of lower grade coal into higher margin products on a larger scale.
- **Expand customer base** – The Company aims to strengthen its sales and logistics capabilities to expand the customer base further inland in China.
- **Optimize cost structure** – The Company is focused on further cost reduction by improving productivity and operational efficiency with the engagement of third party contract mining companies while maintaining product quality and the sustainability of production. Meanwhile, the Company is expecting there will be a significant level of stripping work to be performed at the Sunrise pit in the upcoming 12 months to ensure a sustainable coal production over the mine life. In order to finance the stripping work, the Company will reduce the production level while utilizing the existing balance of inventory to meet the sales target.

- **Progress growth options** – Subject to available financial resources, the Company plans to further the development of the Soumber Deposit, while complying with all government requirements in relation to its licenses and agreements.
- **Diversify the risk profile of the Company** – The Company is evaluating various business opportunities besides coal mining, coal trading and real estate in Mongolia including, but not limited to, the Ceke Logistics Park.
- **Operate in a socially responsible manner** – The Company is focused on maintaining the highest standards in health, safety and environmental performance.

NON-IFRS FINANCIAL MEASURES

Cash Costs

The Company uses cash costs to describe its cash production costs. Cash costs incorporate all production costs, which include direct and indirect costs of production, with the exception of idled mine asset costs and non-cash expenses which are excluded. Non-cash expenses include share-based compensation expense, impairments of coal stockpile inventories, depreciation and depletion of property, plant and equipment and mineral properties. The Company uses this performance measure to monitor its operating cash costs internally and believes this measure provides investors and analysts with useful information about the Company's underlying cash costs of operations. The Company believes that conventional measures of performance prepared in accordance with IFRS do not fully illustrate the ability of its mining operations to generate cash flows. The Company reports cash costs on a sales basis. This performance measure is commonly utilized in the mining industry.

Consolidated Statement of Comprehensive Income

(Expressed in thousands of USD, except for share and per share amounts)

	Year ended December 31,	
	2017	2016
Revenue	\$ 120,973	\$ 58,450
Cost of sales	<u>(105,858)</u>	<u>(87,045)</u>
Gross profit/(loss)	15,115	(28,595)
Other operating expenses	(11,264)	(50)
Administration expenses	(9,181)	(7,888)
Evaluation and exploration expenses	(273)	(422)
Impairment of property, plant and equipment	<u>(11,171)</u>	<u>(1,152)</u>
Loss from operations	(16,774)	(38,107)
Finance costs	(22,958)	(22,314)
Finance income	164	239
Share of earnings of a joint venture	<u>1,287</u>	<u>806</u>
Loss before tax	(38,281)	(59,376)
Current income tax expense	<u>(1,740)</u>	<u>(1,470)</u>
Net loss attributable to equity holders of the Company	<u>(40,021)</u>	<u>(60,846)</u>
Other comprehensive income/(loss) to be reclassified to profit or loss in subsequent periods		
Exchange differences on translation of foreign operations	<u>421</u>	<u>(3,883)</u>
Net comprehensive loss attributable to equity holders of the Company	<u>\$ (39,600)</u>	<u>\$ (64,729)</u>
Basic and diluted loss per share	\$ (0.15)	\$ (0.24)

Consolidated Statement of Financial Position
(Expressed in thousands of USD)

	As at December 31,	
	2017	2016
Assets		
Current assets		
Cash and cash equivalents	\$ 6,471	\$ 966
Trade and other receivables	16,486	19,434
Notes receivables	12,520	–
Inventories	36,389	28,583
Prepaid expenses and deposits	6,286	8,194
	<u>78,152</u>	<u>57,177</u>
Total current assets		
Non-current assets		
Properties for resale	8,906	–
Property, plant and equipment	152,457	180,809
Investment in a joint venture	21,052	21,335
	<u>182,415</u>	<u>202,144</u>
Total non-current assets		
Total assets	<u>\$ 260,567</u>	<u>\$ 259,321</u>
Equity and liabilities		
Current liabilities		
Trade and other payables	\$ 79,219	\$ 43,628
Deferred revenue	27,644	29,849
Interest-bearing borrowings	7,352	8,454
Current portion of convertible debenture	116,374	25,597
Provision for commercial arbitration	13,884	–
Provision for court case penalty	–	9,074
	<u>244,473</u>	<u>116,602</u>
Total current liabilities		
Non-current liabilities		
Interest-bearing borrowings	341	425
Convertible debenture	–	91,993
Decommissioning liability	5,213	4,288
	<u>5,554</u>	<u>96,706</u>
Total non-current liabilities		
Total liabilities	<u>250,027</u>	<u>213,308</u>
Equity		
Common shares	1,098,623	1,094,619
Share option reserve	52,463	52,340
Exchange reserve	(4,737)	(5,158)
Accumulated deficit	(1,135,809)	(1,095,788)
	<u>10,540</u>	<u>46,013</u>
Total equity		
Total equity and liabilities	<u>\$ 260,567</u>	<u>\$ 259,321</u>
Net current liabilities	\$ (166,321)	\$ (59,425)
Total assets less current liabilities	\$ 16,094	\$ 142,719

SELECTED INFORMATION FROM THE NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Additional information required by the Hong Kong Stock Exchange and not disclosed elsewhere in this announcement is as follows. All amounts are expressed in thousands of USD and shares in thousands, unless otherwise indicated.

1. BASIS OF PREPARATION

1.1 Corporate information and liquidity

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 December 31, 2018 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 \$166,321 as at December 31, 2017 compared to \$59,425 of working capital deficiency as at December 31, 2016. Included in the working capital deficiency at December 31, 2017 are significant obligations, which include the obligation to pay CIC under the June 2017 Deferral Agreement in which the Company was required to pay the June 2017 Deferral Agreement Payment. In addition, pursuant to the terms of CIC Convertible Debenture, the Company was required to pay the November Interest Payment. The Company is in discussions with CIC for a deferral of the November 19th Payments; 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.

Pursuant to the Arbitration Award, 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. In the event that First Concept applies to enforce the Arbitration Award against SGS, the Company intends to defend itself against such enforcement proceedings through independent litigation counsel; however, due to the inherent uncertainties of litigation, it is not possible to predict whether the Company will be successful in defending itself against any such enforcement proceedings. 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 to First Concept.

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, 2016, as follows:

	As at December 31,	
	2017	2016
Less than 1 month	\$ 20,664	\$ 14,640
1 to 3 months	16,132	2,493
3 to 6 months	8,825	2,648
Over 6 months	<u>33,598</u>	<u>23,847</u>
Total trade and other payables	<u>\$ 79,219</u>	<u>\$ 43,628</u>

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 March 28, 2018.

The Company also has other current liabilities, which require settlement in the short-term, including: the \$1,708 balance of the TRQ Loan; the principal amount of the Bank Loan of \$2,300 and associated interest due in May 2018 and the principal amount of the Equipment Loan of \$2,309 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 December 31, 2018, 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, at 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. In addition, 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. If SGS fails to satisfy the Arbitration Award, First Concept intends to enforce the Arbitration Award against SGS and, 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).

Furthermore, continuing delay in securing additional financing could ultimately result in an event of default of the Equipment Loan and the Bank Loan, which if not cured within applicable cure periods in accordance with the terms of respective instruments, 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 and the lender of the Bank Loan, respectively.

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 December 31, 2017, the Company's gearing ratio was 0.02 (2016: 0.37), which was calculated based on the Company's long term liabilities to total assets. As at December 31, 2017 and December 31, 2016, the Company is not subject to any externally imposed capital requirements.

1.2 Statement of compliance

The consolidated financial statements, including comparatives, have been prepared in accordance with and using accounting policies in compliance with the IFRS issued by the IASB.

The consolidated financial statements of the Company for the year ended December 31, 2017 were approved and authorized for issue by the Board of Directors of the Company on March 28, 2018.

1.3 Basis of presentation

The consolidated financial statements have been prepared on a historical cost basis except for certain financial assets and financial liabilities which are measured at fair value.

2. 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 year ended December 31, 2017, the Coal Division had 20 active customers with the largest customer accounting for 25% of revenues, the second largest customer accounting for 19% of revenues, the third largest customer accounting for 11% of revenues, the fourth largest customer accounting for 10% of revenues and the other customers accounting for the remaining 35% 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 December 31, 2017	\$ 253,256	\$ 7,311	\$ 260,567
As at December 31, 2016	257,256	2,065	259,321
Segment liabilities			
As at December 31, 2017	\$ 119,095	\$ 130,932	\$ 250,027
As at December 31, 2016	81,288	132,020	213,308
Segment loss			
For the year ended December 31, 2017	\$ (12,280)	\$ (27,741)	\$ (40,021)
For the year ended December 31, 2016	(31,943)	(28,903)	(60,846)
Segment revenues			
For the year ended December 31, 2017	\$ 120,973	\$ –	\$ 120,973
For the year ended December 31, 2016	58,450	–	58,450
Impairment charge on assets⁽ⁱⁱ⁾			
For the year ended December 31, 2017	\$ 32,432	\$ –	\$ 32,432
For the year ended December 31, 2016	11,147	–	11,147
Depreciation and amortization			
For the year ended December 31, 2017	\$ 46,142	\$ 273	\$ 46,415
For the year ended December 31, 2016	46,132	185	46,317
Share of earnings of a joint venture			
For the year ended December 31, 2017	\$ 1,287	\$ –	\$ 1,287
For the year ended December 31, 2016	806	–	806
Finance cost			
For the year ended December 31, 2017	\$ 913	\$ 22,045	\$ 22,958
For the year ended December 31, 2016	816	21,498	22,314
Finance income			
For the year ended December 31, 2017	\$ 24	\$ 140	\$ 164
For the year ended December 31, 2016	21	218	239
Current income tax charge			
For the year ended December 31, 2017	\$ 1,740	\$ –	\$ 1,740
For the year ended December 31, 2016	1,470	–	1,470

(i) The unallocated amount contains all amounts associated with the Corporate Division.

(ii) The impairment charge on assets for the year ended December 31, 2017 relates to properties for resale, inventories, prepaid expenses and deposits and property, plant and equipment. The impairment charge on assets for the year ended December 31, 2016 relates to trade and other receivables, inventories and property, plant and equipment.

3. REVENUE

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

4. EXPENSES BY NATURE

The Company's loss before tax is arrived at after charging/(crediting):

	Year ended December 31,	
	2017	2016
Depreciation	\$ 33,719	\$ 38,511
Auditors' remuneration	430	422
Employee benefit expense (including directors' remuneration)		
Wages and salaries	\$ 7,995	\$ 6,729
Equity-settled share option expense	123	48
Pension scheme contributions	797	675
	<u>8,915</u>	<u>7,452</u>
Minimum lease payments under operating leases	\$ 864	\$ 890
Foreign exchange loss/(gain)	1,116	(5,423)
Impairment of property, plant and equipment	11,171	1,152
Impairment of coal stockpile inventories	17,026	7,354
Provision/(reversal of provision) for doubtful trade and other receivables	(682)	2,641
Penalty on late settlement of trade payables	280	-
Discounting on settlement of trade payables	-	(1,009)
Impairment of properties for resale	1,718	-
Impairment of prepaid expenses and deposits	2,517	-
Provision of commercial arbitration	2,384	-
Mining services, net	2,395	1,006
Settlement of civil claims	-	2,652
Underprovision of miscellaneous taxes	1,421	-
Mine operating costs and other	54,473	40,909
	<u>137,747</u>	<u>96,557</u>
Total expenses	\$ 137,747	\$ 96,557

5. COST OF SALES

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

	Year ended December 31,	
	2017	2016
Operating expenses	\$ 55,451	\$ 41,452
Share-based compensation expense/(recovery)	30	(8)
Depreciation and depletion	20,719	26,142
Impairment of coal stockpile inventories	17,026	7,354
	<u>93,226</u>	<u>74,940</u>
Cost of sales from mine operations	93,226	74,940
Cost of sales related to idled mine assets ⁽ⁱ⁾	12,632	12,105
	<u>105,858</u>	<u>87,045</u>
Cost of sales	\$ 105,858	\$ 87,045

(i) Cost of sales related to idled mine assets for the year ended December 31, 2017 includes \$12,632 of depreciation expense (2016: includes \$12,105 of depreciation expenses). The depreciation expense relates to the Company's idled plant and equipment.

Cost of inventories recognized as expense in cost of sales for the year ended December 31, 2017 totaled \$77,383 (2016: \$62,931).

6. OTHER OPERATING EXPENSES

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

	Year ended December 31,	
	2017	2016
Mining services, net	\$ (2,395)	\$ (1,006)
Provision of commercial arbitration	(2,384)	-
Impairment of properties for resale	(1,718)	-
Impairment of prepaid expenses and deposits	(2,517)	-
Underprovision of miscellaneous taxes	(1,421)	-
Foreign exchange gain/(loss)	(1,116)	5,423
Reversal of provision/(provision) for doubtful trade and other receivables	682	(2,641)
Discount on settlement of trade payables	-	1,009
Settlement of civil claims	-	(2,652)
Other	(395)	(183)
	<u>(11,264)</u>	<u>(50)</u>
Other operating expenses	\$ (11,264)	\$ (50)

7. ADMINISTRATION EXPENSES

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

	Year ended December 31,	
	2017	2016
Corporate administration	\$ 2,534	\$ 2,724
Professional fees	2,464	2,022
Salaries and benefits	3,726	2,820
Share-based compensation expense	89	58
Depreciation	368	264
Administration expenses	\$ 9,181	\$ 7,888

8. FINANCE COSTS AND INCOME

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

	Year ended December 31,	
	2017	2016
Interest expense on convertible debenture	\$ 21,315	\$ 21,279
Interest expense on borrowings	1,103	781
Finance costs on notes receivables	290	—
Loan arrangement fee	90	159
Accretion of decommissioning liability	160	95
Finance costs	\$ 22,958	\$ 22,314

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

	Year ended December 31,	
	2017	2016
Unrealized gain on embedded derivatives in convertible debenture	\$ 137	\$ 217
Interest income	27	22
Finance income	\$ 164	\$ 239

9. TAXES

9.1 Income tax recognized in profit or loss

The Canadian statutory tax rate was 26% (2016: 26%). A reconciliation between the Company's tax expense and the product of the Company's loss before tax multiplied by the Company's domestic tax rate is as follows:

	Year ended December 31,	
	2017	2016
Loss before tax	\$ (38,281)	\$ (59,376)
Statutory tax rate	26%	26%
Income tax recovery based on combined Canadian federal and provincial statutory rates	(9,953)	(15,438)
Lower effective tax rate in foreign jurisdictions	290	610
Tax effect of tax losses and temporary differences not recognized	7,221	6,529
Tax loss utilized	(12,164)	–
Profits or losses attributable to joint venture	322	204
Non-deductible expenses	16,024	9,565
Income tax expenses	\$ 1,740	\$ 1,470

9.2 Deferred tax balances

The Company's deferred tax assets/(liabilities) consist of the following amounts:

	As at December 31,	
	2017	2016
Tax loss carryforwards	\$ 15,568	\$ 15,339
Property, plant and equipment and other assets	(15,568)	(15,339)
Total deferred tax balances	\$ –	\$ –

9.3 Unrecognized deductible temporary differences and unused tax losses

The Company's deductible temporary differences and unused tax losses for which no deferred tax asset is recognized consist of the following amounts:

	As at December 31,	
	2017	2016
Non-capital losses	\$ 166,274	\$ 141,480
Capital losses	30,049	30,049
Foreign exchange and others	<u>392,573</u>	<u>376,531</u>
Total unrecognized amounts	<u>\$ 588,896</u>	<u>\$ 548,060</u>

9.4 Expiry dates

The expiry dates of the Company's unused tax losses are as follows:

	As at December 31, 2017	
	U.S. Dollar Equivalent	Expiry dates
Non-capital losses		
Canada	\$ 163,914	2035 – 2037
Mongolia	54	2020
China	<u>2,306</u>	2022
	<u>\$ 166,274</u>	
Capital losses		
Canada	\$ 30,049	indefinite

10. LOSS PER SHARE

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

	Year ended December 31,	
	2017	2016
Net loss	\$ (40,021)	\$ (60,846)
Weighted average number of shares	<u>272,188</u>	<u>257,692</u>
Basic and diluted loss per share	<u>\$ (0.15)</u>	<u>\$ (0.24)</u>

Potentially dilutive items not included in the calculation of diluted loss per share for the year ended December 31, 2017 include the convertible debenture and stock options that were anti-dilutive.

11. TRADE AND OTHER RECEIVABLES

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

	As at December 31,	
	2017	2016
Trade receivables	\$ 12,901	\$ 17,774
Other receivables	<u>3,585</u>	<u>1,660</u>
Total trade and other receivables	<u>\$ 16,486</u>	<u>\$ 19,434</u>

The aging of the Company's trade and other receivables, based on invoice date and net of provisions, is as follows:

	As at December 31,	
	2017	2016
Less than 1 month	\$ 15,962	\$ 5,777
1 to 3 months	296	5,622
3 to 6 months	19	7,937
Over 6 months	<u>209</u>	<u>98</u>
Total trade and other receivables	<u>\$ 16,486</u>	<u>\$ 19,434</u>

Trade receivables are normally paid within 6 months 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.

During the year ended December 31, 2016, the Company entered into a settlement agreement with one of its major customers (the "Customer") pursuant to which 200 residential units and 40 parking spaces (collectively, the "240 Units") located in Ulaanbaatar, Mongolia, were transferred to the Company as partial consideration for settling an outstanding trade receivables in the amount of \$12,000 owing by the Customer to the Company, with the balance of the receivable, totaling \$7,500, payable in cash by the Customer to the Company by March 31, 2017 (subsequently extended to June 30, 2017). In August 2017, the entirety of the \$7,500 balance has been repaid by, and collected from, the Customer.

As the transfers of title to the 240 Units were substantially completed during the first quarter of 2017, the 240 Units have been recorded at \$10,622, net of impairment, in the Company's accounts accordingly. The settlement agreement included an option for the Company to return any unsold units back to the Customer, until September 30, 2017, at the original price per unit in exchange for an immediate payment of the balance in cash. The Company did not elect to exercise the option.

For the year ended December 31, 2017, the Company recorded a reversal of provision of \$682 on its trade and other receivables in other operating expenses as a result of collecting certain long aged receivables (2016: provision of \$2,641). The Company anticipates full recovery of its remaining outstanding trade and other receivables; therefore, no further provisions have been recorded in respect of the Company's trade and other receivables.

12. NOTES RECEIVABLES

Notes receivables are financial instruments in Chinese banking system. As at December 31, 2017, bank notes receivables of \$1,898 are readily convertible into cash or can be utilized as settlement of outstanding payables while commercial notes receivables of \$10,622 with maturity within 6 months are recorded. Finance costs of \$290 was recorded for the commercial notes receivables.

13. 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, based on invoice date, was as follows:

	As at December 31,	
	2017	2016
Less than 1 month	\$ 20,664	\$ 14,640
1 to 3 months	16,132	2,493
3 to 6 months	8,825	2,648
Over 6 months	<u>33,598</u>	<u>23,847</u>
Total trade and other payables	<u>\$ 79,219</u>	<u>\$ 43,628</u>

13.1 Settlement of Lawsuit Notice from a Former Fuel Supplier

On June 30, 2017, the Company signed the Triparty Settlement Agreement with MTLLC, a former fuel supplier of SGS and ICIC (an independent fuel supplier of the Company), pursuant to which: (i) MTLLC transferred to ICIC its right to receive payment from the Company of \$8,047 (the "Outstanding Amount") owing under the settlement agreement dated February 10, 2017 between the Company and MTLLC and its right to enforce the arbitration award against the Company in connection therewith; and (ii) the Company and ICIC agreed to a revised payment schedule for repayment of the Outstanding Amount. Pursuant to the Triparty Settlement Agreement, the Company will pay interest on the Outstanding Amount, which shall accrue at a monthly rate of 1.8% and will be settled on a monthly basis. The Company was required to repay on average \$1,281 monthly during the period from July 2017 to November 2017 pursuant to the Triparty Settlement Agreement.

As of the date hereof, the Company has fulfilled its obligations under the Triparty Settlement Agreement and has fully repaid the Outstanding Amount.

14. DEFERRED REVENUE

At December 31, 2017, the Company has deferred revenue of \$27,644, which represents prepayments for coal sales from customers (2016: \$29,849).

Included in deferred revenue as at December 31, 2016 was amount prepaid by First Concept, who served the Notice on SGS of \$11,500.

15. INTEREST-BEARING BORROWINGS

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

	As at December 31,	
	2017	2016
Turquoise Hill Loan Facility (i)	\$ 1,708	\$ 2,881
Equipment loan (ii)	2,441	—
Bank loan (iii)	3,041	2,026
Finance leases payable (iv)	503	547
Short-term bridge loan (v)	—	3,425
	<hr/>	<hr/>
Total interest-bearing borrowings	\$ 7,693	\$ 8,879

(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.

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) and (ii), 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 September, 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 December 31, 2017, the outstanding principal and accrued interest under this facility amounted to \$1,000 and \$708, respectively (at December 31, 2016, the outstanding principal and accrued interest under this facility amounted to \$2,200 and \$681, respectively).

(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 be pledged as security upon the completion of equipment purchase.

As at December 31, 2017, the outstanding principal and accrued interest for the equipment loan amounted to \$2,309 and \$132, respectively (December 31, 2016: nil).

A loan arrangement fee of 1% of the loan principal drawn was charged and will be amortized throughout the loan term. For the year ended December 31, 2017, \$8 of loan arrangement fee was amortized (2016: nil). The Company believes the principal amount is capped at the amount of drawdown and related mining equipment has not been purchased as of the date hereof.

(iii) Bank Loan

On May 6, 2016, SGS obtained the Bank Loan in the principal amount of \$2,000 from 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 will mature 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 \$4,539 as at December 31, 2017 were pledged as security.

As at December 31, 2017, the outstanding balance for the Bank Loan was \$3,000 (December 31, 2016: \$2,000) and the Company owed accrued interest of \$41 (December 31, 2016: \$26).

(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 December 31, 2017, the total future minimum lease payments under finance leases and their present values were as follows:

	Minimum lease payments As at December 31,		Present value of minimum lease payments As at December 31,	
	2017	2016	2017	2016
Amounts payable:				
Within one year	\$ 192	\$ 152	\$ 162	\$ 122
In the second year	174	152	160	131
In the third to fifth years, inclusive	<u>188</u>	<u>314</u>	<u>181</u>	<u>294</u>
Total minimum finance lease payments	\$ 554	\$ 618	\$ <u>503</u>	\$ <u>547</u>
Future finance charges	<u>(51)</u>	<u>(71)</u>		
Total net lease finance payables	\$ 503	\$ 547		
Portion classified as current liabilities	<u>(162)</u>	<u>(122)</u>		
Non-current portion	\$ <u>341</u>	\$ <u>425</u>		

(v) Short-term Bridge Loan

On October 27, 2015, the Company executed a \$10,000 bridge loan agreement with an independent Asian based private equity fund. The bridge loan accrues interest at a rate of 8% per annum with interest payable upon the repayment of loan principal.

The Company repaid the first tranche of the short-term bridge loan with interest of \$5,042 up to August 11, 2016. During June and July 2016, the Company drew the second tranche of \$5,038, of which \$1,504 was to mature in March 2017 and \$3,534 was to mature in April 2017. In December 2016, \$1,454 was repaid for the short-term bridge loan and a further \$1,818 and \$1,592 was subsequently repaid in January 2017 and March 2017, respectively and the loan principal was fully settled. The outstanding interest was settled in April 2017.

A loan arrangement fee of 5% of the loan principal drawn was charged, totaling \$252 for the loans drawn during June and July 2016 and amortized throughout the loan term. For the year ended December 31, 2017, \$82 of loan arrangement fee was amortized (2016: \$159).

16. CONVERTIBLE DEBENTURE

On November 19, 2009, the Company issued a convertible debenture to a wholly owned subsidiary of the CIC for \$500,000.

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 fair value through profit or loss 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 stock price, forward foreign exchange rate curves (between the CAD and USD) and spot foreign exchange rates.

16.1 Partial conversion

On March 29, 2010, the Company exercised a right within the debenture to call and convert \$250,000 of the debenture for 21,471 common shares.

16.2 Presentation

Based on the Company's valuation as at December 31, 2017, the fair value of the embedded derivatives decreased by \$137 compared to December 31, 2016. The decrease was recorded as finance income for the year ended December 31, 2017.

For the year ended December 31, 2017, the Company recorded interest expense of \$21,315 related to the convertible debenture as a finance cost (2016: \$21,279). 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:

	Year ended December 31,	
	2017	2016
Balance, beginning of year	\$ 117,590	\$ 108,659
Interest expense on convertible debenture	21,315	21,279
Decrease in fair value of embedded derivatives	(137)	(217)
Interest paid	<u>(22,394)</u>	<u>(12,131)</u>
Balance, end of year	<u>\$ 116,374</u>	<u>\$ 117,590</u>

The convertible debenture balance consists of the following amounts:

	As at December 31,	
	2017	2016
Current convertible debenture		
Interest payable	\$ 24,242	\$ 25,597
Debt host	91,730	—
Fair value of embedded derivatives	<u>402</u>	<u>—</u>
	<u>116,374</u>	<u>25,597</u>
Non-current convertible debenture		
Debt host	—	91,453
Fair value of embedded derivatives	<u>—</u>	<u>540</u>
	<u>—</u>	<u>91,993</u>
Total convertible debenture	<u>\$ 116,374</u>	<u>\$ 117,590</u>

17. ACCUMULATED DEFICIT AND DIVIDENDS

At December 31, 2017, the Company has accumulated a deficit of \$1,135,809 (2016: \$1,095,788). No dividend has been paid or declared by the Company since inception.

The Board did not recommend the payment of any final dividend for the year ended December 31, 2017 (2016: nil).

REVIEW OF RESULTS AND RELEASE OF AUDITED RESULTS

The annual results of the Company for the year ended December 31, 2017 were reviewed by the Audit Committee of the Company and approved and authorized for issue by the Board on March 28, 2018.

The figures in respect of the Company's consolidated statement of financial position, consolidated statement of comprehensive income and the related notes thereto for the year ended December 31, 2017, as set out in this announcement have been agreed by the Company's independent auditor, PricewaterhouseCoopers LLP ("PwC"), to the amounts set out in the Company's audited consolidated financial statements for the year. The work performed by PwC in this respect did not constitute an assurance engagement in accordance with Hong Kong Standards on Auditing, Hong Kong Standards on Review Engagements or Hong Kong Standards on Assurance Engagements issued by the Hong Kong Institute of Certified Public Accountants and consequently, no assurance has been expressed by PwC on this announcement.

The Company's results for the year ended December 31, 2017 are contained in the audited consolidated financial statements and unaudited Management's Discussion and Analysis of Financial Condition and Results of Operations ("MD&A"), which will be available on March 28, 2018 on the SEDAR website at www.sedar.com and the Company's website at www.southgobi.com. Copies of the Company's 2017 Annual Report containing the audited consolidated financial statements and the MD&A, and the Annual Information Form will be available at www.southgobi.com. Shareholders with registered addresses in Hong Kong who have elected to receive a copy of the Company's Annual Report will receive one. Other shareholders of the Company may request a hard copy of the Annual Report free of charge by contacting our Investor Relations department by email at info@southgobi.com.

QUALIFIED PERSONS

Disclosure of a scientific or technical nature in this announcement in respect of the Company's material mineral projects was prepared by or under the supervision of the Qualified Persons (as that term is defined in NI 43-101) listed below.

Disclosure of a scientific or technical nature in respect of the Company's material mineral projects was prepared by or under the supervision of the individuals set out in the table below, each of whom is a "Qualified Person" as that term is defined in NI 43-101 of the Canadian Securities Administrators:

Property	Qualified Persons	Field of Expertise	Relationship to Company
Ovoot Tolgoi	Dr. Weiliang Wang	Resources	Independent Consultant
Ovoot Tolgoi	Vincent Li	Reserves	Independent Consultant
Soumber	Merryl Peterson	Resources	Independent Consultant
Zag Suuj	Merryl Peterson	Resources	Independent Consultant

Disclosure of a scientific or technical nature relating to the Ovoot Tolgoi Mine is derived from the Ovoot Tolgoi Technical Report prepared in accordance with NI 43-101 on the Ovoot Tolgoi Mine dated May 15, 2017, prepared by Dr. Weiliang Wang, Mr. Vincent Li and Mr. Larry Li of DMCL. A copy of the Ovoot Tolgoi Technical Report is available under the Company's profile on SEDAR at www.sedar.com.

Disclosure of a scientific or technical nature relating to the Soumber Deposit is derived from a technical report (the "Soumber Technical Report") prepared in accordance with NI 43-101 on the Soumber Deposit dated March 25, 2013, prepared by Minarco-MineConsult and scientific and technical disclosure relating to the Zag Suuj Deposit is derived from a technical report (the "Zag Suuj Technical Report") prepared in accordance with NI 43-101 on the Zag Suuj Deposit dated March 25, 2013, prepared by Minarco-MineConsult. Copies of the Soumber Technical Report and the Zag Suuj Technical Report are available under the Company's profile on SEDAR at www.sedar.com. These reports are effective as at these dates. Minarco-MineConsult has not reviewed or updated these reports since the date of publishing.

ABOUT SOUTHGOBI

SouthGobi, listed on the Toronto and Hong Kong stock exchanges, owns and operates its flagship Ovoot Tolgoi coal mine in Mongolia. It also holds the mining licences of its other metallurgical and thermal coal deposits in South Gobi Region of Mongolia. SouthGobi produces and sells coal to customers in China.

Contact:

Investor Relations

Kino Fu

Office: +852 2156 7030

Email: kino.fu@southgobi.com

Website: www.southgobi.com

Except for statements of fact relating to the Company, certain information contained herein constitutes forward-looking statements. Forward-looking statements are frequently characterized by words such as “plan”, “expect”, “project”, “intend”, “believe”, “anticipate”, “could”, “should”, “seek”, “likely”, “estimate” and other similar words or statements that certain events or conditions “may” or “will” occur. Forward-looking statements relate to management’s future outlook and anticipated events or results and are based on the opinions and estimates of management at the times the statements are made. Forward-looking statements in this press release include, but are not limited to, statements regarding:

- the Company continuing as a going concern and its ability to realize its assets and discharge its liabilities in the normal course of operations as they become due; adjustments to the amounts and classifications of assets and liabilities in the Company’s consolidated financial statements and the impact thereof;
- the Company’s expectations of sufficient liquidity and capital resources to meet its ongoing obligations and future contractual commitments, including the Company’s ability to settle its trade payables, to secure additional funding and to meet its obligations under each of the CIC Convertible Debenture, the TRQ Loan, the Equipment Loan and the Bank Loan, as the same become due;
- the Company’s anticipated financing needs, development plans and future production levels;
- the Company successfully negotiating a deferral of the November 19th Payments and the November 2017 PIK Interest under the June 2017 Deferral Agreement and CIC Convertible Debenture;

- the ability of the Company to successfully negotiate with First Concept regarding payment arrangements in respect of the Arbitration Award that are practical to and are in the best interest of the Company;
- the ability of the Company to successfully defend itself against any enforcement proceeding brought by First Concept in respect of the Arbitration Award;
- the ability of the Company to negotiate favorable repayment terms on the TRQ Reimbursable Amount;
- the results and impact of the Ontario class action;
- the estimates and assumptions included in the Company's impairment analysis and the possible impact of changes thereof;
- the agreement with Ejin Jinda and the payments thereunder;
- the commencement of the washing facilities at Ovoot Tolgoi and the timing thereof;
- the ability to enhance the product value by conducting coal processing and coal washing;
- the development of the Ceke Logistics Park project;
- the results of the internal investigation conducted by the Special Committee and the potential impact of the charges against Mr. Aminbuhe and the connection, if any, between those charges and the Company and his conduct as Chairman and Chief Executive Officer of the Company;
- the evaluation, and potential pursuit of, business opportunities other than coal mining, coal trading and real estate in Mongolia, including but not limited to the Ceke Logistic Park, power generation and contract mining;
- the impact of the Company's activities on the environment and actions taken for the purpose of mitigation of potential environmental impacts and planned focus on health, safety and environmental performance;
- the Company's outlook and objectives for 2018 and beyond; and
- other statements that are not historical facts.

Forward-looking information is based on certain factors and assumptions described below and elsewhere in this press release, including, among other things: the current mine plan for the Ovoot Tolgoi mine; mining, production, construction and exploration activities at the Company's mineral properties; the costs relating to anticipated capital expenditures; the capacity and future toll rate of the paved highway; plans for the progress of mining license application processes; mining methods; timing of the commencement of the washing facilities at Ovoot Tolgoi; the Company's anticipated business activities, planned expenditures and corporate strategies; management's business outlook, including the outlook for 2018 and beyond; currency exchange rates; operating, labour and fuel costs; the anticipated royalties payable under Mongolia's royalty regime, the future coal market conditions in China and the related impact on the Company's margins and liquidity; future coal prices, and the level of worldwide coal production. While the Company considers these assumptions to be reasonable based on the information currently available to it, they may prove to be incorrect. Forward-looking statements are subject to a variety of risks and uncertainties and other factors that could cause actual events or results to differ materially from those projected in the forward-looking statements. These risks and uncertainties include, among other things: the uncertain nature of mining activities, actual capital and operating costs exceeding management's estimates; variations in mineral resource and mineral reserve estimates; failure of plant, equipment or processes to operate as anticipated; the possible impacts of changes in mine life, useful life or depreciation rates on depreciation expenses; risks associated with, or changes to regulatory requirements (including environmental regulations) and the ability to obtain all necessary regulatory approvals; the potential expansion of the list of licenses published by the Government of Mongolia covering areas in which exploration and mining are purportedly prohibited on certain of the Company's mining licenses; the Government of Mongolia designating any one or more of the Company's mineral projects in Mongolia as a Mineral Deposit of Strategic Importance; continued delays in the custom clearance process at the Ceke border; the Company being in default under the CIC Convertible Debenture and the TRQ Loan, including the risk of CIC accelerating all amounts outstanding under the CIC Convertible Debenture and enforcing payment thereof, and the risk of Turquoise Hill demanding immediate payment of all amounts outstanding under the TRQ Loan; the risk of the Company failing to successfully negotiate a deferral of the November 19th Payments and the November 2017 PIK Interest under the June 2017 Deferral Agreement and CIC Convertible Debenture; the possible impact of changes to the inputs to the valuation model used to value the embedded derivatives in the CIC Convertible Debenture; the risk of the Company failing to successfully negotiate favorable repayment terms on the TRQ Reimbursable Amount; the risk of the Company defaulting under its existing debt obligations, including the equipment loan and bank loan; the impact of amendments to, or the application of, the laws of Mongolia, China and other countries in which the Company carries on business; modifications to existing practices so as to comply with any future permit conditions that may be imposed by regulators; delays in obtaining approvals and lease renewals; the risk of fluctuations in coal prices and changes in China and world economic conditions; the

risk of the Company failing to successfully negotiate with First Concept regarding payment arrangements in respect of the Arbitration Award; risk that First Concept may apply to enforce the Arbitration Award against SGS through judicial measures in courts of Mongolia or in other applicable jurisdiction(s) and the ability of the Company to successfully defend itself against such enforcement proceedings; the outcome of the Class Action and any damages payable by the Company as a result; the result of the internal investigation conducted by the Special Committee and the impact thereon on the Company; the risk that the calculated sales price determined by the Company for the purposes determining of the amount of royalties payable to the Mongolian government is deemed as being “non-market” under Mongolian tax law; customer credit risk; cash flow and liquidity risks; risks relating to the development of the Ceke Logistics Park project; including the risk that its investment partner may not comply with the underlying agreements governing project development and may fail to meet its obligations to the Company or third parties; risks relating to timing of the commencement of the washing facilities at Ovoot Tolgoi, including identifying a reliable water source to permit operation of the washing facilities; risks relating to the Company’s ability to raise additional financing and to continue as a going concern. This list is not exhaustive of the factors that may affect any of the Company’s forward-looking statements.

Due to assumptions, risks and uncertainties, including the assumptions, risks and uncertainties identified above and elsewhere in this press release, actual events may differ materially from current expectations. The Company uses forward-looking statements because it believes such statements provide useful information with respect to the currently expected future operations and financial performance of the Company, and cautions readers that the information may not be appropriate for other purposes. Except as required by law, the Company undertakes no obligation to update forward-looking statements if circumstances or management’s estimates or opinions should change. The reader is cautioned not to place undue reliance on the forward-looking statements, which speaks only as of the date of this press release; they should not rely upon this information as of any other date.

The English text of this press release shall prevail over the Chinese text in case of inconsistencies.