Southern Arc
MINERALS INC.

CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEARS ENDED
JUNE 30, 2012 AND 2011

(Expressed in Canadian dollars)

CHARTERED ACCOUNTANTS
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Independent Auditor's Report

To the Shareholders of
Southern Arc Minerals Inc.

We have audited the accompanying consolidated financial statements of Southern Arc Minerals Inc. and its subsidiaries, which comprise the consolidated statements of financial position as at June 30, 2012, June 30, 2011, and July 1, 2010, and the consolidated statements of comprehensive loss, changes in equity and cash flows for the years ended June 30, 2012 and June 30, 2011, and a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Consolidated Financial Statements
Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility
Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audits to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained in our audits is sufficient and appropriate to provide a basis for our audit opinion.

Opinion
In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of Southern Arc Minerals Inc. and its subsidiaries as at June 30, 2012, June 30, 2011, and July 1, 2010 and its financial performance and its cash flows for the years ended June 30, 2012 and June 30, 2011 in accordance with International Financial Reporting Standards.

"MacKay LLP"

Chartered Accountants
Vancouver, British Columbia
October 25, 2012

SOUTHERN ARC MINERALS INC.

CONSOLIDATED STATEMENTS OF FINANCIAL POSITION
(Expressed in Canadian dollars)

	June 30, 2012	June 30, 2011 (Note 14)	July 1, 2010 (Note 14)
ASSETS			
Current			
Cash	$ 22,441,567	$ 38,632,091	$ 1,604,476
Receivables	40,701	155,528	29,668
Prepaid expense and deposit	117,280	94,816	7,534
Investment (Note 6)	-	-	835,799
	22,599,548	38,882,435	2,477,477
Equity investment (Note 3)	-	357,871	-
Property, plant and equipment (Note 4)	344,790	234,965	11,074
Exploration properties (Note 5)	37,430,624	22,796,908	22,410,416
Loans receivable (Note 5)	509,550	433,935	-
Total Assets	**$ 60,884,512**	**$ 62,706,114**	**$ 24,898,967**
LIABILITIES AND EQUITY			
Current			
Accounts payable and accrued liabilities	$ 1,564,436	$ 924,657	$ 383,246
Loans payable (Note 7)	-	-	1,614,600
	1,564,436	924,657	1,997,846
Equity			
Capital stock (Note 8)	74,891,487	74,151,488	30,474,172
Treasury stock (Note 8)	(1,170,000)	(1,170,000)	-
Share-based payment reserve (Note 8)	11,498,915	10,461,028	5,926,928
Non-controlling interest reserve	-	-	221,008
Deficit	(26,255,249)	(22,066,164)	(15,692,612)
Capital and reserve attributable to shareholders of Southern Arc Minerals Inc.	58,965,153	61,376,352	20,929,496
Non-controlling interest	354,923	405,105	1,971,625
Total equity	59,320,076	61,781,457	22,901,121
Total Liabilities and Equity	**$ 60,884,512**	**$ 62,706,114**	**$ 24,898,967**

Nature and continuance of operations (Note 1)
Subsequent events (Note 17)

Approved by the Board of Directors and authorized for issue on October 25, 2012:

"John Proust" Director *"David Stone"* Director

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

SOUTHERN ARC MINERALS INC.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS
(Expressed in Canadian dollars)

	June 30, 2012	June 30, 2011 (Note 14)
EXPENSES		
Office and miscellaneous (Notes 10, 15)	$ 1,613,100	$ 551,506
Share-based compensation (Note 8)	1,037,887	4,060,214
Management fees (Note 10)	614,000	348,000
Professional fees	553,324	507,547
Foreign exchange (gain) loss	(354,697)	50,406
Travel	188,260	209,242
Investor relations	184,318	-
Rent	103,665	32,169
Transfer agent and filing fees	87,820	142,783
Consulting fees	73,259	227,067
Depreciation	29,006	5,970
Exploration properties written-off	-	87,693
Loss before other items	**(4,129,942)**	**(6,222,597)**
OTHER ITEMS		
Interest income	278,209	90,294
Other income	-	28,295
Gain on sale of investment	-	54,852
Impairment on other investment	(102,807)	-
Loss on equity investment (Note 3)	(52,289)	(534,197)
Impairment on equity investment (Note 3)	(305,582)	-
	(182,469)	(360,756)
Net and comprehensive loss for the year	**$ (4,312,411)**	**$ (6,583,353)**
Comprehensive loss attributable to:		
Shareholders of Southern Arc Minerals Inc.	$ (4,189,085)	$ (6,373,552)
Non-controlling interests	(123,326)	(209,801)
	$ (4,312,411)	$ (6,583,353)
Basic and diluted loss per share	**$ (0.04)**	**$ (0.08)**
Weighted average number of shares outstanding	107,056,976	84,293,973

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

SOUTHERN ARC MINERALS INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Expressed in Canadian dollars)

	June 30, 2012	June 30, 2011 (Note 14)
CASH FLOWS FROM OPERATING ACTIVITIES		
Comprehensive loss for the year	$ (4,312,411)	$ (6,583,353)
Items not affecting cash:		
Share-based compensation	1,037,887	4,060,214
Depreciation	29,006	5,970
Loss on equity investment	52,289	534,197
Impairment on equity investment	305,582	-
Gain on sale of investment	-	(54,852)
Foreign exchange loss (gain)	(354,697)	50,406
Changes in non-cash working capital items:		
Receivables	114,827	(132,907)
Prepaid expense and deposit	(22,464)	(91,476)
Accounts payable and accrued liabilities	(305,783)	92,359
Net cash used in operating activities	(3,455,764)	(2,031,749)
CASH FLOWS FROM INVESTING ACTIVITIES		
Investment in exploration properties	(12,847,509)	(3,973,673)
Acquisition of property, plant and equipment	(205,090)	(241,455)
Exploration advances received (prepayment)	(31,886)	836,357
Repayment of investment	-	374
Sale of investment	-	890,277
Net cash used in investing activities	(13,084,485)	(2,488,120)
CASH FLOWS FROM FINANCING ACTIVITIES		
Share issuance (net of cost) by Nickel Oil & Gas	-	189,042
Proceeds from loan	-	1,966,400
Treasury shares purchased	-	(1,170,000)
Loan repayment	-	(2,961,000)
Repayment of non-revolving bridge loan	-	(550,000)
Proceeds from issuance of shares, net of share issue costs	(2,501)	44,151,202
Net cash provided (used) by financing activities	(2,501)	41,625,644
Effect of exchange rate changes on cash	352,226	(78,160)
Change in cash during year	(16,190,524)	37,027,615
Cash, beginning of year	38,632,091	1,604,476
Cash, end of year	**$ 22,441,567**	**$ 38,632,091**
Cash paid for income taxes	$ -	$ -
Cash paid for interest	$ -	$ 5,200

Supplemental disclosure with respect to cash flows (Note 9)

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

SOUTHERN ARC MINERALS INC.

CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY

(Expressed in Canadian dollars)

	Attributable to owners of the Company							
	Capital Stock	Treasury Stock	Share-based Payment Reserve	Non-controlling Interest Reserve	Deficit	Total	Non-controlling Interest	Total Equity
Balance at June 30, 2011 (Note 14)	**$ 74,151,488**	**$ (1,170,000)**	**$ 10,461,028**	**$ -**	**$ (22,066,164)**	**$ 61,376,352**	**$ 405,105**	**$ 61,781,457**
Comprehensive loss for the year	-	-	-	-	(4,189,085)	(4,189,085)	(123,326)	(4,312,411)
Shares issued for exploration properties	742,500	-	-	-	-	742,500	-	742,500
Share issue cost	(2,501)	-	-	-	-	(2,501)	-	(2,501)
Share-based compensation	-	-	1,037,887	-	-	1,037,887	-	1,037,887
Change in non-controlling interest	-	-	-	-	-	-	73,144	73,144
	739,999	-	1,037,887	-	(4,189,085)	(2,411,199)	(50,182)	(2,461,381)
Balance at June 30, 2012	**$ 74,891,487**	**$ (1,170,000)**	**$ 11,498,915**	**$ -**	**$ (26,255,249)**	**$ 58,965,153**	**$ 354,923**	**$ 59,320,076**
Balance at July 1, 2010 (Note 14)	**$ 30,474,172**	$ -	**$ 5,926,928**	**$ 221,008**	**$ (15,692,612)**	**$ 20,929,496**	**$ 1,971,625**	**$ 22,901,121**
Comprehensive loss for the year	-	-	-	-	(6,373,552)	(6,373,552)	(209,801)	(6,583,353)
Private placement, net of transaction costs	-	-	-	-	-	-	623,674	623,674
Private placements, net of transaction costs	43,488,202	-	-	-	-	43,488,202	-	43,488,202
Repurchase of shares	-	(1,170,000)	-	-	-	(1,170,000)	-	(1,170,000)
Agent warrants (Stock-based financing costs)	(1,013,070)	-	1,013,070	-	-	-	-	-
Gain on diluted interest in subsidiary (Note 3)	-	-	-	43,466	-	43,466	(43,466)	-
Adjustment for elimination of subsidiary (Note 3)	-	-	-	(264,474)	-	(264,474)	(1,936,927)	(2,201,401)
Share-based compensation	-	-	4,060,214	-	-	4,060,214	-	4,060,214
Exercise of options	1,202,184	-	(539,184)	-	-	663,000	-	663,000
	43,677,316	(1,170,000)	4,534,100	(221,008)	(6,373,552)	40,446,856	(1,566,520)	38,880,336
Balance at June 30, 2011 (Note 14)	**$ 74,151,488**	**$ (1,170,000)**	**$ 10,461,028**	**$ -**	**$ (22,066,164)**	**$ 61,376,352**	**$ 405,105**	**$ 61,781,457**

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

1. NATURE AND CONTINUANCE OF OPERATIONS

Southern Arc Minerals Inc. ("Southern Arc" or "the Company") was incorporated in British Columbia, Canada on August 19, 2004. The Company is a natural resource company engaged in the acquisition and exploration of resource properties in Indonesia. To date, the Company has not generated significant revenues from operations and is considered to be in the exploration stage. The Company's head office is located at Suite 1680-200 Burrard Street, Vancouver, British Columbia, Canada, V6C 3L6.

The Company is in the process of exploring and developing its exploration properties and has not yet determined whether the properties contain reserves that are economically recoverable. The recoverability of the amounts shown for exploration properties are dependent upon the existence of economically recoverable reserves, the ability of the Company to obtain necessary financing to complete the development of those reserves and upon future profitable production.

These consolidated financial statements have been prepared on the basis of accounting principles applicable to a "going concern", which assumes that the Company will continue its operations for the foreseeable future and will be able to realize its assets and discharge its liabilities in the normal course of operations for the foreseeable future. Based on its current plans, budgeted capital expenditures, and cash requirements, the Company has sufficient cash to finance its current plans for the 24 months from the date of approval of the financial statements. However, the Company recognizes that exploration expenditures may change with ongoing results and, as a result, it may be required to obtain additional financing. While the Company has been successful at securing financing in the past, there can be no assurance that it will be able to do so in the future. These consolidated financial statements do not include any adjustments to the amounts and classification of assets and liabilities that might be necessary should the Company be unable to continue business.

2. SIGNIFICANT ACCOUNTING POLICIES

Adoption of IFRS and statement of compliance

These are the Company's first annual financial statements prepared in accordance with IFRS in effect at June 30, 2012. These financial statements have been prepared in accordance with IAS 1, Presentation of Financial Statements and IFRS 1, First Time Adoption of International Financial Reporting Standards and the impact of the transition from previous Canadian GAAP to IFRS is explained in Note 14, including the effects of the transition to IFRS on the Company's financial position, equity, comprehensive loss and cash flows.

Subject to the application of the transition elections described in Note 14, the accounting policies applied in these financial statements and described below, have been applied consistently to all periods presented, including the opening statement of financial position as at July 1, 2010 (the Company's "transition date"), except where the Company applied certain exemptions upon transition to IFRS.

Basis of presentation

These financial statements have been prepared on a historical cost basis except for financial instruments that have been measured at fair value. In addition, these financial statements have been prepared using the accrual basis of accounting, except for cash flow information.

2. SIGNIFICANT ACCOUNTING POLICIES (cont'd…)

Principles of consolidation

These consolidated financial statements include the accounts of the Company; and

i) its wholly-owned Canadian subsidiary West Indonesia Mining Holdings Inc.; and
ii) its wholly-owned Singapore subsidiaries: Indotan Lombok Pte. Ltd., Indotan Sumbawa Pte. Ltd., East Indonesia Mining Pte. Ltd. and Southern Sunda Mining Pte. Ltd.; and
iii) its wholly-owned Indonesian subsidiary PT. Selatan Arc Minerals; and
iv) its 90%-owned Indonesian subsidiaries PT. Indotan Lombok Barat Bangkit and PT. Indotan Sumbawa Barat.

Significant intercompany balances and transactions have been eliminated upon consolidation.

Significant accounting judgement and estimates

The preparation of these financial statements requires management to make certain estimates, judgements and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and reported amounts of expenses during the reporting period. Actual outcomes could differ from these estimates. These financial statements include estimates which, by their nature, are uncertain. The impacts of such estimates are pervasive throughout the financial statements, and may require accounting adjustments based on future occurrences. Revisions to accounting estimates are recognized in the period in which the estimate is revised and future periods if the revision affects both current and future periods. These estimates are based on historical experience, current and future economic conditions and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

Critical accounting estimates

Significant assumptions about the future and other sources of estimation uncertainty that management has made at the end of the reporting period, that could result in a material adjustment to the carrying amounts of assets and liabilities, in the event that actual results differ from assumptions made, relate to, but are not limited to the following:

i) The estimated fair value of the Company's financial assets and liabilities are by their nature, subject to measurement uncertainty.
ii) The calculation of share-based compensation requires estimates of volatility, forfeiture rates and market prices surrounding the issuance of share options. These estimates impact share-based compensation expense and share-based payment reserve.
iii) The estimated fair value of the Company's equity investments.
iv) The collectability of loans receivable which may impact bad debt expense.
v) The estimated rehabilitation provision.

Critical accounting judgements

Critical accounting judgements are accounting policies that have been identified as being complex or involving subjective judgements or assessments.

i) A deferred income tax asset is recognized to the extent that it is probable that future income tax profits will be available against which the asset can be used. To the extent that management does not consider it probable that a defer income tax asset will be recovered, a deferred income tax asset is not recognized.

ii) The application of the Company's accounting policy for exploration expenditure requires judgement in determining whether it is likely that future economic benefits will flow to the Company, which may be based on assumptions about future events or circumstances. Estimates and assumptions made may change if new information becomes available. If, after expenditure is capitalized, information becomes available suggesting that the recovery of expenditure is unlikely, the amount capitalized is written off in the profit or loss in the year the new information becomes available.

2. SIGNIFICANT ACCOUNTING POLICIES (cont'd…)

Significant accounting judgement and estimates (cont'd…)

iii) The determination of a subsidiary's functional currency often requires significant judgement where the primary economic environment in which they operate may not be clear. This can have a significant impact on the consolidated results of the Company based on the foreign currency translation method.

Property, plant and equipment

Telephone equipment is recorded at cost and amortized using the declining balance method at 20% per year. Vehicles, furniture, computers, field equipment and leasehold improvements are recorded at cost and amortized on a straight-line basis over the estimated useful lives of the assets. The estimated useful lives are as follows:

Vehicles, furniture, computers and field equipment	4 years
Leasehold improvements	10 years

Depreciation of vehicles, computers (field) and field equipment were allocated to exploration properties.

Exploration properties

(i) Exploration properties

Once the legal right to explore a property has been acquired, costs directly related to exploration and evaluation are recognized and capitalized by geographical area, in addition to the acquisition costs by geographical area. These direct expenditures include such costs as materials used, surveying costs, drilling costs, payments made to contractors and depreciation on plant and equipment during the exploration phase. Costs not directly attributable to exploration activities, including general administrative overhead costs, are expensed in the period in which they occur.

If economically recoverable ore reserves are developed, capitalized costs of the related property are reclassified as mining assets and amortized using the unit of production method. When a property is abandoned, all related costs are written off to operations. If, after management review, it is determined that the carrying amount of an exploration property is impaired, that property is written down to its estimated fair value. An exploration property is reviewed for impairment annually and whenever events or changes in circumstances indicate that its carrying amount may not be recoverable.

As the Company currently has no operational income, any incidental revenues earned in connection with exploration activities are applied as a reduction to capitalized exploration costs.

The amounts shown for exploration properties do not necessarily represent present or future values. Their recoverability is dependent upon the discovery of economically recoverable reserves, the ability of the Company to obtain the necessary financing to complete property development and future profitable production or proceeds from the disposition thereof.

Title and permits to exploration properties involves certain inherent risks due to the difficulties of determining the validity of certain exploration property interests as well as the potential for problems arising from the frequently ambiguous conveying characteristics of many exploration properties. The Company has investigated title to all of its exploration property interests and, to the best of its knowledge, title to all of its exploration property interests are in good standing. The Company is in various stages of applying for permits for ongoing exploration activities related to the exploration properties.

2. SIGNIFICANT ACCOUNTING POLICIES (cont'd…)

Exploration properties (cont'd…)

(ii) Joint interest

A portion of the Company's development activities are conducted jointly with others. These financial statements reflect only the Company's proportionate interest in such activities.

The Company does not record any exploration expenditures made by the joint venture partner on its account. It also does not recognize any gain or loss on its option and joint venture agreement arrangement, but re-designates any costs previously capitalized in relation to the whole interest as relating to the partial interest retained. Exploration advances received from a joint venture partner in accordance with the terms of the option and joint venture agreement are recorded as current liabilities until the exploration expenditure is incurred.

(iii) Rehabilitation provision

The Company is subject to various government laws and regulations relating to environmental disturbances caused by exploration and evaluation activities. The Company records the present value of the estimated costs of legal and constructive obligations required to restore the exploration sites in the period in which the obligation is incurred. The nature of the rehabilitation activities includes restoration, reclamation and re-vegetation of the affected exploration sites.

The rehabilitation provision generally arises when the environmental disturbance is subject to government laws and regulations. When the liability is recognized, the present value of the estimated costs is capitalized by increasing the carrying amount of the related mining assets. Over time, the discounted liability is increased for the changes in present value based on current market discount rates and liability specific risks.

Additional environmental disturbances or changes in rehabilitation costs will be recognized as additions to the corresponding assets and rehabilitation liability in the period in which they occur.

Foreign currency transactions

The functional and reporting currency of the Company and its subsidiaries is the Canadian dollar. Transactions in currencies other than the functional currency are recorded at the rates of exchange prevailing on dates of transactions. Monetary assets and liabilities that are denominated in foreign currencies are translated at the rates prevailing at each reporting date. Non-monetary assets and liabilities denominated in foreign currencies that are measured at fair value are re-translated to functional currency at the exchange rate at the date the fair value was determined. Non-monetary items that are measured in terms of historical cost in a foreign currency are not re-translated. Foreign currency translation differences are recognized in profit or loss.

Loss per share

The Company presents basic per share data for its common shares, calculated by dividing the net loss attributable to common shareholders of the Company by the weighted average number of common shares outstanding during the period. Diluted loss per share is determined by adjusting the loss attributable to common shareholders and the weighted average number of common shares outstanding for the effects of all dilutive potential common shares. In reporting periods when a loss is incurred, potential issuance of shares would be anti-dilutive and, therefore, basic and diluted loss per share are the same.

Investment

Investments in companies over which the Company can exercise significant influence are accounted for using the equity method. When there is a loss in value of an investment that is other than a temporary decline, the investment is written down to recognize the loss in the determination of comprehensive income or loss.

2. SIGNIFICANT ACCOUNTING POLICIES (cont'd…)

Share-based payment transaction

The share option plan allows the Company to grant options to its employees and consultants. The fair value of options granted is recognized as a share-based payment expense with a corresponding increase in share-based payment reserve. An individual is classified as an employee when the individual is an employee for legal or tax purposes (direct employee) or provides services similar to those performed by a direct employee.

The fair value for employee options is measured at grant date and each tranche is recognized on a graded-vesting basis over the period during which the options vest. The fair value of the options granted is measured using the Black-Scholes option pricing model taking into account the terms and conditions upon which the options were granted. At each financial position reporting date, the amount recognized as an expense is adjusted to reflect the actual number of share options that are expected to vest.

Equity-settled share-based payment transactions with non-employees are measured at the fair value of the goods or services received. However, if the fair value cannot be estimated reliably, the share-based payment transaction is measured at the fair value of the equity instruments granted at the date the non-employee provides the goods or the services.

Income taxes

Income tax expense comprises current and deferred tax. Current tax and deferred tax are recognized in net income except to the extent that they relate to a business combination or items recognized directly in equity or in other comprehensive loss/income.

Current income taxes are recognized for the estimated income taxes payable or receivable on taxable income or loss for the current year and any adjustment to income taxes payable in respect of previous years. Current income taxes are determined using tax rates and tax laws that have been enacted or substantively enacted by the year-end date.

Deferred tax assets and liabilities are recognized where the carrying amount of an asset or liability differs from its tax base, except for taxable temporary differences arising on the initial recognition of goodwill and temporary differences arising on the initial recognition of an asset or liability in a transaction which is not a business combination and at the time of the transaction affects neither accounting nor taxable profit or loss.

Recognition of deferred tax assets for unused tax losses, tax credits and deductible temporary differences is restricted to those instances where it is probable that future taxable profit will be available against which the deferred tax asset can be applied. At the end of each reporting period, the Company reassesses unrecognized deferred tax assets. The Company recognizes a previously unrecognized deferred tax asset to the extent that it has become probable that future taxable profit will allow the deferred tax asset to be recovered.

Financial instruments

On initial recognition, all financial assets and financial liabilities are recorded at fair value plus directly attributable transaction costs, other than financial assets and liabilities classified as at fair value through profit or loss. The directly attributable transaction costs of financial assets and liabilities classified as at fair value through profit or loss are expensed in the period they are incurred.

Subsequent measurement

<u>Financial assets</u>

The Company classifies its financial assets into one of the following categories, depending on the purpose for which the asset was acquired. The Company's accounting policy for each category is as follows:

2. SIGNIFICANT ACCOUNTING POLICIES (cont'd…)

Financial instruments (cont'd…)

Fair value through profit or loss - This category comprises derivatives, or assets acquired or incurred principally for the purpose of selling or repurchasing it in the near term. They are carried in the statement of financial position at fair value with changes in fair value recognized in the statement of operations and comprehensive loss. Cash is classified as fair value through profit or loss.

Loans and receivables - These assets are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They are carried at amortized cost using the effective interest method less any provision for impairment. Individually significant receivables are considered for impairment when they are past due or when other objective evidence is received that a specific counterparty will default. Accounts receivable and loans receivable are classified as loans and receivables.

Held-to-maturity investments - These assets are non-derivative financial assets with fixed or determinable payments and fixed maturities that the Company's management has the positive intention and ability to hold to maturity. These assets are measured at amortized cost using the effective interest method. If there is objective evidence that the investment is impaired, determined by reference to external credit ratings and other relevant indicators, the financial asset is measured at the present value of estimated future cash flows. Any changes to the carrying amount of the investment, including impairment losses, are recognized in the statement of operations and comprehensive loss. The Company has not classified any financial assets as held-to-maturity.

Available-for-sale - Non-derivative financial assets not included in the above categories are classified as available-for-sale. They are carried at fair value with changes in fair value recognized directly in other comprehensive income (loss). Where a decline in the fair value of an available-for-sale financial asset constitutes objective evidence of impairment, the amount of the loss is removed from equity and recognized in the statement of operations and comprehensive loss. The Company has not classified any financial assets as available-for-sale.

All financial assets except for those recognized at fair value through profit or loss are subject to review for impairment at each reporting date. Financial assets are impaired when there is any objective evidence that a financial asset or a group of financial assets is impaired. Different criteria to determine impairment are applied for each category of financial assets, which are described above.

<u>Financial liabilities</u>

The Company classifies its financial liabilities into one of two categories. The Company's accounting policy for each category is as follows:

Fair value through profit or loss - This category comprises derivatives, or liabilities acquired or incurred principally for the purpose of selling or repurchasing it in the near term. They are carried in the statement of financial position at fair value with changes in fair value recognized in the statement of operations and comprehensive loss.

Other financial liabilities - This category includes accounts payable and accrued liabilities, and loans payable all of which are recognized at amortized cost at the settlement date using the effective interest method of amortization.

2. SIGNIFICANT ACCOUNTING POLICIES (cont'd…)

New accounting standards and recent pronouncement

The Company has not yet adopted certain new standards, amendments and interpretations to existing standards, which have been published but are effective only for accounting periods beginning on or after January 1, 2013 (except as otherwise noted), including:

- IFRS 9 – Financial Instruments: Classification and Measurement, effective January 1, 2015
- IFRS 10 – Consolidated Financial Statements
- IFRS 11 – Joint Arrangements
- IFRS 12 – Disclosure of Interests in Other Entities
- IFRS 13 – Fair Value Measurement
- IAS 12 – Income Taxes, effective for accounting periods beginning on or after January 1, 2012
- IFRIC 20 – Stripping Costs in the Production Phase of a Surface Mine
- IAS 27 – Separate Financial Statements
- IAS 28 – Investments in Associates and Joint Ventures
- IAS 32 – Financial Instrument Presentation

3. INVESTMENT IN NICKEL OIL & GAS CORP.

At December 31, 2011, the Company concluded that the decline in the value of its equity investment in Nickel Oil & Gas Corp. ("Nickel"), due to continued low natural gas prices, is other than temporary. Therefore it has written the remaining value of the investment down to $nil and has recorded an impairment loss of $305,582 during the year ended June 30, 2012. As at June 30, 2012 and 2011, the Company held 15.3 million Nickel shares (37.6%) with a carrying value of $nil (June 30, 2011: $357,871). Under the equity method of accounting, the Company recorded a loss of $52,289 (2011: $534,197), which represented its equity ownership proportion of Nickel's loss for the six-month period ended December 31, 2011.

On July 7, 2008, the Company acquired 15.3 million common shares of Nickel, a related corporation by way of a common director, for a purchase price of $5,355,000, representing 59.8% of the outstanding shares of Nickel. As a result of acquiring control, the Company consolidated the financial results of Nickel from that date. The acquisition of Nickel was accounted for using the purchase method. The purchase price of $5,355,000 was allocated to cash $5,669,935; exploration property $1,966,801; payables ($752); and to non-controlling interest ($2,280,984).

During the period since the acquisition, Nickel issued additional common shares to third parties, which diluted the Company's ownership of Nickel to 38.5% at June 30, 2010. During the year ended June 30, 2011, Nickel issued additional common shares to a director, which further diluted the Company's ownership to 37.6%, resulting in a gain on diluted interest in subsidiary of $43,466.

During the year ended June 30, 2010, Nickel entered into a farm-out and option agreement granting it the option to earn certain oil and gas rights with respect to property in the Brewster and Pine Creek areas in Alberta, Canada. At Brewster, Nickel's joint venture partner solely funded the completion, equipping and tie-in costs of one well and will receive 100% of all revenue from the well until it recoups 125% of the payout costs incurred. At Pine Creek, a horizontal well was drilled by Nickel and its joint venture partner solely funded the completion, equipping and tie-in costs of the well. According to the amended agreement, the joint venture partner receives 100% of all revenue from the well until it recoups 125% of the payout costs incurred.

Effective April 1, 2011, due to the changes in voting relationships, ownership and the Board of Directors, the Company determined that it no longer controlled Nickel. The Company's March 31, 2011 non-controlling interest and reserve balance were restored to their $nil balances on the same date on a non-consolidated basis by upward adjustments of $1,936,927 and $264,474, respectively.

In January 2012 Nickel agreed to sell all of its interests in its wells to its joint venture partner in settlement of amounts owed of $452,731. This sale was completed with an effective date of July 1, 2012.

(Expressed in Canadian dollars)

4. PROPERTY, PLANT AND EQUIPMENT

	Telephone equipment	Vehicles	Furniture	Computer	Field equipment	Leasehold improvement	Total
Costs							
Balance, July 1, 2010	$ 26,278	$ -	$ -	$ -	$ -	$ -	$ 26,278
Additions	-	8,677	16,504	95,216	86,342	34,716	241,455
Balance, June 30, 2011	26,278	8,677	16,504	95,216	86,342	34,716	267,733
Additions	-	113,987	16,435	12,091	62,577	-	205,090
Balance, June 30, 2012	**$ 26,278**	**$ 122,664**	**$ 32,939**	**$ 107,307**	**$ 148,919**	**$ 34,716**	**$ 472,823**
Accumulated depreciation							
Balance, July 1, 2010	$ (15,204)	$ -	$ -	$ -	$ -	$ -	$ (15,204)
Depreciation for the year	(2,216)	(720)	(784)	(7,825)	(5,730)	(289)	(17,564)
Balance, June 30, 2011	(17,420)	(720)	(784)	(7,825)	(5,730)	(289)	(32,768)
Depreciation for the year	(1,772)	(21,521)	(8,158)	(25,205)	(35,138)	(3,471)	(95,265)
Balance, June 30, 2012	**$ (19,192)**	**$ (22,241)**	**$ (8,942)**	**$ (33,030)**	**$ (40,868)**	**$ (3,760)**	**$ (128,033)**
Net carry value							
Balance, July 1, 2010	$ 11,074	$ -	$ -	$ -	$ -	$ -	$ 11,074
Balance, June 30, 2011	$ 8,858	$ 7,957	$ 15,720	$ 87,391	$ 80,612	$ 34,427	$ 234,965
Balance, June 30, 2012	**$ 7,086**	**$ 100,423**	**$ 23,997**	**$ 74,277**	**$ 108,051**	**$ 30,956**	**$ 344,790**

During the year ended June 30, 2012, $66,259 (2011: $11,594) of depreciation was capitalized to exploration properties.

(Expressed in Canadian dollars)

5. EXPLORATION PROPERTIES

	Lombok Property, Indonesia	Sumbawa Properties, Indonesia	Oil & Gas Properties, Canada	Total
Balance, July 1, 2010	**$13,200,709**	**$ 5,954,900**	**$ 3,254,807**	**$ 22,410,416**
Acquisition costs				
Adjustment to eliminate subsidiary (Note 3)	-	-	(1,691)	(1,691)
Total acquisition costs	-	-	(1,691)	(1,691)
Deferred exploration costs				
Assaying, surveying and analysis	30,052	5,582	-	35,634
Camp construction and other	1,343,056	331,416	-	1,674,472
Drilling (Note 10)	781,624	-	-	781,624
Geological and other consulting	586,631	186,718	-	773,349
Labour	314,508	149,405	-	463,913
Write-off during the year	-	(87,693)	-	(87,693)
Adjustment to eliminate subsidiary (Note 3)	-	-	(3,253,116)	(3,253,116)
Total deferred exploration costs	3,055,871	585,428	(3,253,116)	388,183
Balance, June 30, 2011 (Note 14)	**16,256,580**	**6,540,328**	-	**22,796,908**
Acquisition costs	2,198,147	843,850	-	3,041,997
Deferred exploration costs				
Incurred during the year:				
Assaying, surveying and analysis	446,493	-	-	446,493
Camp construction and other	56,372	192,950	-	249,322
Drilling (Note 10)	3,116,458	-	-	3,116,458
Geological and other consulting	1,285,612	66,071	-	1,351,683
Labour	6,343,019	84,744	-	6,427,763
Total deferred exploration costs	11,247,954	343,765	-	11,591,719
Balance, June 30, 2012	**$29,702,681**	**$ 7,727,943**	**$ -**	**$ 37,430,624**

Lombok and Taliwang (Sumbawa) Properties, Indonesia

During 2005, the Company acquired its original interests in the Lombok and Taliwang properties by paying $81,572 and issuing 11,500,000 common shares (valued at $862,500) to Sunda Mining Corporation ("Sunda") and by paying $180,000 and issuing 1,000,000 common shares (valued at $125,000) to Indotan Inc. ("Indotan"). The Company also granted a 0.5% NSR to individuals related to Sunda and a 2% NSR to Indotan on the Taliwang property, and a 0.5% NSR to individuals related to Sunda and a 1% NSR to Indotan on approximately 8% of the current Lombok property, which excludes Block 1 described below.

In August 2005, the Company entered into an agreement with PT Newmont Nusa Tenggara ("Newmont") regarding a property ("Block 1") which now forms the western portion of the Company's Lombok property (including the Selodong, Mencanggah and Pelangan prospects) and is included in the mining business license ("IUP"). The acquisition was completed through a relinquishment by Newmont of the Block 1 area. The terms of the agreement include granting Newmont a 2% NSR on any mineral production from the Block 1 area and a right of first refusal should the Company wish to introduce a new partner into any development within the area originally covered by Block 1. The Company has the right to repurchase this 2% NSR for US$1 million at any time.

In December 2009, the Company acquired the right to the name Indotan Inc. as well as control over two Singapore companies by issuing 3,500,000 common shares with a value of $2,415,000. The acquisition of the Singapore

5. EXPLORATION PROPERTIES (cont'd…)

companies was accounted for using the purchase method and the purchase price of $2,415,000 was allocated to exploration properties. Related to this transaction, the Company received an option to acquire 1,500,000 of these shares at a price of $0.90 per common share during the year ended June 30, 2011. The Company assigned 200,000 of these $0.90 options to a Director of the Company as stock-based compensation. In June 2011 the Company exercised the remaining 1,300,000 $0.90 options and currently holds those shares.

During the year ended June 30, 2011, the Company established new 85%-owned Indonesian subsidiaries (PT. Indotan Lombok Barat Bangkit and PT. Indotan Sumbawa Barat) to hold its Lombok and Taliwang properties, respectively. A 5% carried interest in these companies is owned by the Company's Indonesian joint venture partner, PT Puri Permata Mega ("PT PPM") and a 10% carried interest is owned by the respective local governments.

The Company has advanced loans receivable of $509,550 (US$500,000) (2011: $433,935 (US$450,000), 2010: $nil) on an unsecured basis and without interest to the Indonesian subsidiary companies as capital contributions on behalf of the Indonesian shareholders, and these funds are to be repaid to the Company from future revenues of the subsidiaries.

During the year the Company incurred a payable of $751,097 (US$737,220) to a related party as reimbursement for payments made, on the Company's behalf, to a third party to acquire the rights to an industrial forestry permit application, to ensure the Company's priority mining rights to develop the West Lombok property. The balance of US$737,220 remains payable at June 30, 2012 (see also Note 10).

On May 17, 2012, Southern Arc announced that it has increased its interest in the West Lombok and Taliwang projects from 85% to 90% through the acquisition of additional shares in PT Indotan Lombok Barat Bangkit, and PT Indotan Sumbawa Barat from Southern Arc's Indonesian partner, PT Puri Permata Mega ("PT PPM"). In consideration for transferring its 5% interest in both companies, Southern Arc paid US$1,500,000 and issued 2,250,000 Southern Arc shares at market value of $742,500 to PT PPM. These 5% share acquisitions have been accounted for as acquisition costs of Exploration Properties.

East Elang and Sabalong (Sumbawa) Properties

The Company acquired the East Elang and Sabalong properties by way of mining licenses ("KPs") which were granted to the Company by the Sumbawa Regency in 2006 and 2007, respectively. Both KPs were subsequently transitioned into IUPs in December 2009.

In October 2010, the Company entered into an option and joint venture agreement with Vale International S.A. ("Vale"), a wholly-owned subsidiary of Vale S.A., regarding the East Elang and Sabalong properties. To exercise its option, Vale must fully fund the advancement of either or both of the East Elang or Sabalong properties, through to and including the completion of a bankable feasibility study, at no cost to the Company.

a) Phase 1 – Vale will fund US$1,000,000 (Sabalong) and US$1,200,000 (East Elang) of exploration expenditures within one year from the date the Company receives an exploration activities permit from the Ministry of Forestry for that property. Vale can then elect to proceed to;
b) Phase 2 minimum program – Vale would fund at least US$2,000,000 (Sabalong) and US$2,500,000 (East Elang) of additional exploration expenditures within 2 years of commencing Phase 2;
c) Phase 2 full program – Vale may proceed to completion of a pre-feasibility study or fund further exploration expenditures of at least US$10,000,000 (on either property) within 4 years of commencing Phase 2;
d) Upon completing the Phase 2 full program, Vale may elect to solely fund the completion of a bankable Feasibility Study within 7 years of commencing Phase 2.

If Vale completes a bankable feasibility study on either of the East Elang or Sabalong properties within the permitted time frames, Vale will be entitled to receive a 75% interest in the Company's subsidiary PT. Selatan Arc Minerals ("PT SAM") which holds the IUPs for East Elang and Sabalong. (See also Note 17)

(Expressed in Canadian dollars)

5. EXPLORATION PROPERTIES (cont'd…)

The East Elang and Sabalong properties are held by the Company's wholly-owned Indonesian subsidiary, PT SAM. Funds advanced to PT SAM by Vale are recorded as cash and as accounts payable and accrued liabilities in the Company's accounts until such time as the funds are expended on approved exploration activities. As at June 30, 2012, Vale had advanced US$2,179,000 (June 30, 2011: US$840,000) to PT SAM and PT SAM held US$166,976 (June 30, 2011: US$212,310) of these funds as cash.

6. INVESTMENT

	June 30, 2012	June 30, 2011	July 1, 2010
MAVII notes	$ -	$ -	$ 835,799

At June 30, 2010, investments included Master Asset Vehicle II ("MAVII") notes received in exchange for Canadian third-party asset-backed commercial paper that was held by the Company.

During the year ended June 30, 2012, the Company received repayments of investment of $nil (2011: $374). During the year ended June 30, 2011, the Company sold its MAVII investment for net proceeds of $890,277.

7. LOANS PAYABLE

	June 30, 2012	June 30, 2011	July 1, 2010
Non-revolving bridge loan	$ -	$ -	$ 550,000
Non-interest-bearing loans from a director	-	-	1,064,600
	$ -	$ -	$ 1,614,600

During the year ended June 30, 2011, the Company:

a) repaid a non-interest-bearing loan of US$1,000,000 (CDN$1,064,600) from a director of the Company. In consideration for granting the loan, the Company assigned its option to acquire 500,000 of the Company's shares at $0.50 per share from Indotan Inc. A fair value of $117,713 was allocated to share-based financing costs and recorded to contributed surplus in fiscal year 2010 in connection with the assignment. The director has exercised the option and acquired the mentioned shares;

b) received and repaid a non-interest-bearing loan of US$1,000,000 (CDN$994,600) from a director of the Company to the Company's 100% owned subsidiary, Indotan Lombok Pte. Ltd.; and

c) received and repaid a non-interest-bearing loan of US$1,000,000 (CDN$971,800) from a director of the Company to the Company's 100% owned subsidiary, Southern Sunda Mining Pte. Ltd.

(Expressed in Canadian dollars)

8. CAPITAL STOCK AND RESERVES

	Number of common shares	Capital stock	Number of treasury shares	Treasury stock	Share-based payment reserve
Authorized					
Unlimited common shares without par value					
Issued					
Balance as at July 1, 2010	77,329,990	$ 30,474,172	-	$ -	$ 5,926,928
Private placements	28,409,520	46,522,309	-	-	-
Share issue costs	-	(3,034,107)	-	-	-
Agent warrants issued	-	(1,013,070)	-	-	1,013,070
Share-based compensation	-	-	-	-	4,060,214
Repurchase of shares	-	-	1,300,000	(1,170,000)	-
Exercise of options	1,225,000	1,202,184	-	-	(539,184)
Balance as at June 30, 2011	106,964,510	74,151,488	1,300,000	(1,170,000)	10,461,028
Shares issued for exploration properties	2,250,000	742,500	-	-	-
Share issue costs	-	(2,501)	-	-	-
Share-based compensation	-	-	-	-	1,037,887
Balance as at June 30, 2012	109,214,510	$ 74,891,487	1,300,000	$ (1,170,000)	$ 11,498,915

During the year ended June 30, 2012, the Company increased its ownership in PT. Indotan Lombok Barat Bangkit and PT. Indotan Sumbawa Barat to 90% each by acquiring the 5% interests owned by the Company's Indonesian joint venture partner PT PPM. As part of the consideration for these 5% interests, the Company has issued to PT PPM 2,250,000 Southern Arc shares at market value of $0.33 per share.

During the year ended June 30, 2011, the Company issued 1,225,000 common shares at $0.30 to $0.80 per share for total proceeds of $663,000 pursuant to the exercise of share options previously granted.

On February 24, 2011, the Company completed a private placement offering of 17,738,750 common shares at $1.60 per share for total proceeds of $28,382,000. In connection with the offering, the underwriters received a cash commission of 6% of the gross proceeds and 1,064,325 non-transferable common share purchase warrants exercisable for 18 months at $1.60 per share.

On June 21, 2011, the Company completed a private placement offering of 10,670,770 common shares at $1.70 per share for total proceeds of $18,140,309. In connection with the offering, the underwriters received a cash commission of 6% of the gross proceeds and 640,246 non-transferable common share purchase warrants exercisable for 12 months at $1.70 per share.

During the year ended June 30, 2011, the Company purchased 1,300,000 shares of the Company for $0.90 per share from Indotan Inc. (Note 5).

Share options

The Company grants share options in accordance with its stock option plan and the policies of the TSX Venture Exchange ("TSXV"). The number of shares reserved for issuance under the plan shall not exceed 10% of the issued and outstanding common shares of the Company. The terms of the option, including the vesting terms and the option price, are fixed by the directors at the time of grant subject to the price not being less than the market price of the Company's share on the date of grant. The share options granted are exercisable for a period of up to 10 years. A summary of the Company's outstanding share options granted is presented in the following table.

(Expressed in Canadian dollars)

8. CAPITAL STOCK AND RESERVES (cont'd…)

Share options (cont'd…)

	Number of options	Weighted average exercise price
Outstanding at July 1, 2010	4,075,000	$ 0.41
Granted	4,650,000	1.03
Exercised	(1,225,000)	(0.54)
Outstanding at June 30, 2011	7,500,000	0.81
Granted	1,655,000	1.02
Expired	(75,000)	0.90
Outstanding at June 30, 2012 (Remaining contractual life is 3.05 years)	9,080,000	$ 0.82
Number of options currently exercisable	8,120,000	$ 0.79

During the year ended June 30, 2012, the Company recorded share-based compensation of $1,037,887 (2011: $4,060,214) fair valued using the Black-Scholes option pricing model, as a result of the granting of 1,655,000 (2011: 4,650,000) options. These amounts were recorded as share-based payment reserve on the statement of financial position. The weighted average fair value of the options granted was $0.85 (June 30, 2011: $0.84) per option.

Option pricing models require the use of estimates and assumptions including the expected volatility. Changes in underlying assumptions can materially affect the fair value estimates.

The weighted average share price at the date of exercise of options during the year ended June 30, 2011 was $1.63 per share. No options were exercised during the year ended June 30, 2012.

The following weighted average assumptions were used for the Black-Scholes valuation of share options granted during the period:

	June 30, 2012	June 30, 2011
Risk-free interest rate	1.59%	2.36%
Expected life of options	5 years	4.8 years
Annualized volatility	127.20%	117.74%
Forfeiture rate	0.00%	0.00%
Dividend rate	0.00%	0.00%

At June 30, 2012, the Company had share purchase options outstanding enabling holders to acquire common shares as follows:

	Number of shares	Exercise price	Expiry date
Options	3,150,000	$ 0.40	September 16, 2014
	3,350,000	$ 0.80	July 19, 2015
	400,000	$ 2.00	January 18, 2016
	300,000	$ 1.85	February 11, 2016
	300,000	$ 1.70	June 22, 2016
	200,000	$ 1.71	July 11, 2016
	200,000	$ 1.11	August 17, 2016
	1,180,000	$ 0.90	November 18, 2016
	9,080,000		

(Expressed in Canadian dollars)

8. CAPITAL STOCK AND RESERVES (cont'd…)

Warrants

The Company has granted warrants to purchase common shares. A summary of warrants granted is presented below:

	Number of warrants	Weighted average exercise price
Outstanding at July 1, 2010	-	$ -
Issued	1,704,571	1.64
Outstanding at June 30, 2011	1,704,571	1.64
Expired	(640,246)	1.70
Outstanding at June 30, 2012	1,064,325	$ 1.60

At June 30, 2012, the Company had share purchase warrants outstanding enabling holders to acquire common shares as follows:

	Number of shares	Exercise price	Expiry date
Warrants	1,064,325	$ 1.60	August 24, 2012
	1,064,325		

All of these 1,064,325 warrants expired unexercised on August 24, 2012.

During the year ended June 30, 2011, the Company recorded share issue cost of $1,013,070 using the Black-Scholes option pricing model, as a result of the issuance of 1,704,571 warrants to its agents in connection with private placement offerings. These amounts were recorded as contributed surplus on the statement of financial position. The weighted average fair value of the warrants granted was $0.59 per warrant.

Fair value pricing models require the use of estimates and assumptions including the expected volatility. Changes in underlying assumptions can materially affect the fair value estimates.

The following weighted average assumptions were used for the Black-Scholes valuation of warrants granted during the period:

	June 30, 2012	June 30, 2011
Risk-free interest rate	N/A	1.56%
Expected life of options	N/A	1 year
Annualized volatility	N/A	67.93%
Forfeiture rate	N/A	0.00%
Dividend rate	N/A	0.00%

9. SUPPLEMENTAL DISCLOSURE WITH RESPECT TO CASH FLOWS

The Company had the following significant non-cash transactions:

- During the year ended June 30, 2012, the Company issued 2,250,000 common shares at $0.33 per share for a value of $742,500 for acquisition of exploration properties.
- At June 30, 2012, the Company included in accounts payable $1,507,734 (2011: $498,400) of exploration expenditures.

(Expressed in Canadian dollars)

10. RELATED PARTY TRANSACTIONS

Key management and personnel compensation

The key management personnel include the directors and other officers of the Company. Key management compensation consists of the following:

	June 30, 2012	June 30, 2011
Management fees	$ 1,118,188	$ 844,536
Drilling services	$ 3,112,916	$ 781,624
Share-based compensation	$ 635,417	$ 2,455,000

During the year ended June 30, 2012, the Company paid $614,000 (2011: $348,000) for management fees and $237,140 (2011: $112,500) for administration fees to a private company controlled by the Chief Executive Officer and director of the Company. The above transactions occurred in the normal course of operations and are recorded at the consideration established and agreed to by the related parties.

Other transactions with related parties

During the year end June 30, 2011, the Company entered into a contract with a company controlled by a director and officer of the Company for drilling services at the Company's West Lombok property. This contract was awarded under a competitive bidding process and all charges under the contract are considered to be at market rates. During the year ended June 30, 2012 the Company paid a total of $3,112,916 (US$3,097,106) (2011: $781,624 (US$807,880)) for drilling services pursuant to the contract. A balance of $nil (June 30, 2011: $297,387) is included in accounts payable for drilling services incurred during the year ended June 30, 2012. A balance of $751,097 (June 30, 2011: $nil) is included in accounts payable at June 30, 2012 to reimburse a related party for amounts paid, on the Company's behalf, to a third party to acquire the rights to an industrial forestry permit application, to ensure the Company's priority mining rights to develop the West Lombok property. The related party received no consideration from the Company, other than reimbursement of amounts paid.

The related party balances have no fixed repayment terms and bear no interest.

11. FINANCIAL INSTRUMENTS

The nature of the Company's operations expose the Company to credit risk, liquidity risk and market risk, which may have a material effect on cash flows, operations and comprehensive income.

The Company's risk management policies are established to identify and analyze the risks faced by the Company, to set appropriate risk limits and to monitor market conditions and the Company's activities. The Board of Directors has overall responsibility for the establishment and oversight of the Company's risk management framework and policies.

Credit risk

Credit risk is the risk of loss associated with counterparty's inability to fulfill its payment obligations. Financial instruments that potentially subject the Company to credit risk consist primarily of cash and accounts receivable. The maximum exposure to credit risk is equal to the fair value or carrying value of the financial assets.

The Company reduces its credit risk by maintaining its bank accounts at large financial institutions. Receivables are amounts receivable from the Canadian federal government for the refundable HST amounts. The credit risk on these amounts is minimal.

Liquidity risk

Liquidity risk is the risk that the Company is not able to meet its financial obligations as they fall due. All of the Company's financial liabilities are classified as current and are anticipated to mature within the next fiscal year. The Company's approach to managing liquidity risk is to ensure that it will have sufficient liquidity to meet liabilities when due. See also Note 1.

11. FINANCIAL INSTRUMENTS (cont'd…)

Market risk

Market risk is the risk of loss that may arise from changes in market factors such as interest rates, foreign exchange rates, and commodity and equity prices. The Company is exposed to the interest rate risk to the extent that the cash maintained at the financial institutions is subject to a floating rate of interest. The interest rate risk on the Company's cash is minimal. The Company is exposed to market risk as the ability of the Company to develop or market its properties and the future profitability of the Company is related to the market price of certain minerals.

Foreign exchange risk

The Company's largest non-monetary assets are its exploration interests in Indonesia. The Company could accordingly be at risk for foreign currency fluctuations and risks associated with legal and political issues in a developing-country environment. The Company minimizes cash and monetary assets or liabilities in Indonesia.

At June 30, 2012, the Company had US$1,800,937 (approximately CDN$1,835,335) and Indonesian Rupiah ("Rph") 288,313,592 (approximately CDN$31,426) in cash and US$1,388,666 (approximately CDN$1,415,190) and Rph 913,920,520 (approximately CDN$99,617) in account payable and accrued liabilities. As at June 30, 2012, US$ amounts were converted at a rate of US$0.98 to CAD$1 and Rph amounts were converted at a rate of Rph 9,174 to CAD$1.

At June 30, 2011, the Company had US$2,528,618 (approximately CDN$2,437,856) and Rph 2,657,051,280 (approximately CDN$298,098) in cash and US$751,973 (approximately CDN$725,143) and Rph 62,050,266 (approximately CDN$6,949) in account payable and accrued liabilities. As at June 30, 2011, US$ amounts were converted at a rate of US$1.0370 to CAD$1 and Rph amounts were converted at a rate of Rph 8,929 to CAD$1.

At July 1, 2010, the Company had US$1,006,195 (approximately CDN$1,071,195) in cash, US$107,216 (approximately CDN$112,277) in accounts payable and US$1,000,000 (CDN$1,064,600) in loans payable. As at July 1, 2010, US$ amounts were converted at a rate of US$1 to CDN$1.04803.

Fair value

The fair value of the Company's financial instruments is approximated by their carrying value as at June 30, 2012, June 30, 2011, and July 1, 2010 due to their short term nature.

IFRS requires disclosure about fair market value measurements for financial instruments and liquidity risk using a three-level hierarchy that reflects the significance of the inputs used in making the fair value measurements. The three-level hierarchy is as follows:

- Level 1 - Unadjusted quoted prices in active markets for identical assets or liabilities;
- Level 2 - Inputs other than quoted prices that are observable for the asset or liability either directly or indirectly; and
- Level 3 - Inputs that are not based on observable market data.

(Expressed in Canadian dollars)

11. FINANCIAL INSTRUMENTS (cont'd…)

Financial instruments measured at fair value on June 30, 2012, June 30, 2011 and July 1, 2010 is summarized in levels of fair value hierarchy as follows:

June 30, 2012	Level 1	Level 2	Level 3
Assets			
Cash	$ 22,441,567	$ -	$ -
June 30, 2011			
Assets			
Cash	$ 38,632,091	$ -	$ -
July 1, 2010			
Assets			
Cash	$ 1,604,476	$ -	$ -
Investment	$ -	$ -	$ 835,799

12. CAPITAL MANAGEMENT

The Company's objectives when managing capital are to safeguard the Company's ability to continue as a going concern in order to pursue the exploration and development of unproven mineral properties and to maintain a flexible capital structure. The capital structure of the Company consists of equity attributable to common shareholders comprising issued capital, share-based payment reserve and deficit. The Company manages the capital structure and makes adjustments to it in light of changes in economic conditions and the risk characteristics of the underlying assets.

The Company currently does not produce any revenue and has relied on existing cash balances, equity issuances and advances from related parties to fund its operations. The Company is currently not subject to externally imposed capital requirements.

There were no changes in the Company's approach to capital management in the year ended June 30, 2012.

13. INCOME TAXES

A reconciliation of income taxes at statutory rates with reported taxes is as follows:

	2012	2011
Loss for the year, before income taxes	$ (4,312,411)	$ (6,583,353)
Expected income tax recovery	$ (1,121,227)	$ (1,843,339)
Items not deductible for income tax purposes	413,461	1,327,493
Effect of change in tax rate	14,806	44,125
Effect of tax rates in other jurisdictions	55,932	18,577
Adjustment to opening tax pool	-	1,997,548
Tax benefits recognised (unrecognised)	637,028	(1,544,404)
Total income taxes	$ -	$ -

(Expressed in Canadian dollars)

13. INCOME TAXES (cont'd…)

The significant components of the Company's deferred income tax assets are as follows:

	June 30, 2012	June 30, 2011	July 1, 2010
Deferred income tax assets:			
Non-capital loss carry forwards	$ 3,256,176	$ 2,439,519	$ 1,143,620
Capital loss carry forwards	50,438	50,438	-
Share issuance costs	455,616	647,988	87,192
Finance costs	-	-	35,223
Cumulative exploration expenses	(1,459,372)	(1,408,758)	1,243,479
Equipment	6,098	7,819	3,801
Long-term investment	669,375	624,641	62,350
	2,978,331	2,361,647	2,575,665
Tax benefits unrecognized	(2,978,331)	(2,361,647)	(2,575,665)
Net deferred income tax assets	$ -	$ -	$ -

The Company has available for deduction against future years' taxable income non-capital losses of approximately $13,024,702. Non-capital losses expire as follows:

2015	$ 403,890
2016	604,856
2027	486,895
2028	511,735
2029	886,865
2030	2,938,228
2031	3,953,490
2032	3,238,743
	$ 13,024,702

In addition, the Company has $13,520,577 (2011: $13,520,577) of unclaimed resource expenses for Canadian income tax purposes that can be carried forward indefinitely and used to reduce taxable income in Canada.

Future tax benefits, which may arise as a result of these losses and resource expenditures, have not been recognized in these financial statements.

14. TRANSITION TO INTERNATIONAL FINANCIAL REPORTING STANDARDS

As stated in Note 2, these are the Company's first annual consolidated financial statements prepared in accordance with IFRS.

The accounting policies in Note 2 have been applied as follows:

- in preparing the consolidated financial statements for the year ended June 30, 2012;
- the comparative information for the year ended June 30, 2011;
- the statement of financial position as at June 30, 2011; and
- preparing the opening IFRS statement of financial position on the Transition Date, July 1, 2010.

In preparing the opening IFRS statement of financial position, comparative information for the year ended June 30, 2011, the Company has adjusted amounts reported previously in financial statements prepared in accordance with Canadian generally accepted accounting principles ("CAGAAP").

14. TRANSITION TO INTERNATIONAL FINANCIAL REPORTING STANDARDS (cont'd…)

An explanation of how the transition from CAGAAP to IFRS has affected the Company's financial position, financial performance and cash flows is set out in the table that follows.

The guidance for the first time adoption of IFRS is set out in IFRS 1. IFRS 1 provides for certain mandatory exceptions and optional exemptions for first time adopters of IFRS. In preparing these financial statements, the Company has elected to apply the following transitional arrangements:

(a) Share-based payment transactions

IFRS 2 *Share-based Payment* has not been applied to equity instruments that were granted on or before November 7, 2002, nor has it been applied to equity instruments granted after November 7, 2002 that vested before July 1, 2010.

IFRS 2, similar to CAGAAP, requires the Company to measure share-based compensation related to share purchase options granted to employees at the fair value of the options on the date of grant and to recognize such expense over the vesting period of the options. However, under IFRS 2, the recognition of such expense must be done with a "graded vesting" methodology as opposed to the straight-line vesting method allowed under CAGAAP. In addition, under IFRS, forfeiture estimates are recognized in the period they are estimated, and are revised for actual forfeitures in subsequent periods; while under CAGAAP, forfeitures of awards are recognized as they occur. There is no adjustment required to the July 1, 2010's statement of financial position on the Transition Date.

(b) Business combinations

IFRS 1 permits the Company's to keep the original CAGAAP accounting treatment for business combinations that occurred prior to the date of transition to IFRS. The Company has applied this exemption and will not restate business combinations that occurred before July 1, 2010.

(c) Reclassification within equity section

IFRS requires an entity to present, for each component of equity, a reconciliation between the carrying amount at the beginning and end of the period, separately disclosing each change. The Company examined its "contributed surplus" account and concluded that as at the Transition Date, the entire amount of $10,461,028 relates to "share-based payment reserve". As a result, the Company believes that a reclassification would be necessary in the equity section between "contributed surplus" and the "share-based payment reserve" account.

(d) Reclassification of exploration properties

Under IFRS, the Company has chosen not to record any exploration expenditures made by its joint venture partner on account of its properties. Exploration advances received from a joint vendor partner in accordance to the terms of the option and joint venture agreement are treated as current liabilities until the exploration expenditure is incurred. Based on the new accounting policy adopted, the Company examined and adjusted its "exploration properties" and "accounts payable and accrual liabilities" balance accordingly as at the Transition Date.

Reconciliations of Canadian GAAP to IFRS

A reconciliation of the above noted changes is included in the following statements of financial position and statements of operations and comprehensive loss for the dates noted below. The changes to the financial statements as noted below have resulted in reclassifications of various amounts, within operating activities, on the statements of cash flows; however, as there have been no adjustments to net cash flows, no reconciliation of the statement of cash flows has been presented.

(Expressed in Canadian dollars)

14. TRANSITION TO INTERNATIONAL FINANCIAL REPORTING STANDARDS (cont'd…)

Reconciliation of Statement of Financial Position

	Note	As at July 1, 2010			As at June 30, 2011		
		Canadian GAAP	Effect of transition of IFRS	IFRS	Canadian GAAP	Effect of transition of IFRS	IFRS
ASSETS		$	$	$	$	$	$
Current							
Cash		1,604,476	-	1,604,476	38,632,091	-	38,632,091
Receivables		29,668	-	29,668	155,528	-	155,528
Prepaid expenses and deposit		7,534	-	7,534	94,816	-	94,816
Investment		835,799	-	835,799	-	-	-
Total current assets		2,477,477	-	2,477,477	38,882,435	-	38,882,435
Equity investment		-	-	-	357,871	-	357,871
Property, plant and equipment		11,074	-	11,074	234,965	-	234,965
Exploration properties	14(d)	22,410,416	-	22,410,416	23,401,805	(604,897)	22,796,908
Loans receivable		-	-	-	433,935	-	433,935
TOTAL ASSETS		24,898,967	-	24,898,967	63,311,011	(604,897)	62,706,114
LIABILITIES AND SHAREHOLDERS' EQUITY							
Current							
Accounts payable and accrued liabilities	14(d)	383,246	-	383,246	1,529,554	(604,897)	924,657
Loan payable		1,614,600	-	1,614,600	-	-	-
		1,997,846	-	1,997,846	1,529,554	(604,897)	924,657
Shareholders' equity							
Capital stock		30,474,172	-	30,474,172	74,151,488	-	74,151,488
Treasury stock		-	-	-	(1,170,000)	-	(1,170,000)
Contributed surplus	14(c)	5,926,928	(5,926,928)	-	10,461,028	(10,461,028)	-
Share-based payment reserve	14(c)	-	5,926,928	5,926,928	-	10,461,028	10,461,028
Non-controlling interest reserve		221,008	-	221,008	-	-	-
Deficit		(15,692,612)	-	(15,692,612)	(22,066,164)	-	(22,066,164)
Capital and reserve attributable to shareholders of Southern Arc Minerals Inc.		20,929,496	-	20,929,496	61,376,352	-	61,376,352
Non-controlling interest		1,971,625	-	1,971,625	405,105	-	405,105
Total equity		22,901,121	-	22,901,121	61,781,457	-	61,781,457
TOTAL EQUITY AND LIABILITIES		24,898,967	-	24,898,967	63,311,011	(604,897)	62,706,114

(Expressed in Canadian dollars)

14. TRANSITION TO INTERNATIONAL FINANCIAL REPORTING STANDARDS (cont'd…)

Reconciliation of Comprehensive Loss

	For the year ended June 30, 2011		
	Canadian GAAP	Effect of transition of IFRS	IFRS
Expenses	$	$	$
Amortization	5,970	-	5,970
Consuliting fees	227,067	-	227,067
Foreign exchange gain	50,406	-	50,406
Management fees	348,000	-	348,000
Office and miscellaneous	551,506	-	551,506
Professional fees	507,547	-	507,547
Rent	32,169	-	32,169
Exploration properties written-off	87,693	-	87,693
Share-based compensation	4,060,214	-	4,060,214
Transfer agent and filing fees	142,783	-	142,783
Travel	209,242	-	209,242
Loss before other items	(6,222,597)	-	(6,222,597)
Other items			
Intersest income	90,294	-	90,294
Other income	28,295	-	28,295
Loss on equity investment	(534,197)	-	(534,197)
Gain on sale of investment	54,852	-	54,852
	(360,756)	-	(360,756)
Net and comprehensive loss for the year	(6,583,353)	-	(6,583,353)
Net and comprehensive loss attibutatble to:			
Shareholders of Southern Arc Minerals inc.	(6,373,552)	-	(6,373,552)
Non-controlling interests	(209,801)	-	(209,801)
	(6,583,353)	-	(6,583,353)
Basic and diluted loss per share	(0.08)	-	(0.08)
Weighted average number of shares outstanding	84,293,973	-	84,293,973

(Expressed in Canadian dollars)

15. OFFICE AND MISCELLANEOUS EXPENSES

	2012	2011
Administrative	$ 735,062	$ 208,598
Office expense	379,594	260,223
Employee benefits	351,103	-
Insurance	54,197	25,713
Interest and bank charges	39,101	30,784
Corporate promotion	26,723	11
Telephone	18,930	14,193
Meals and entertainment	8,390	11,984
	$ 1,613,100	$ 551,506

16. SEGMENTED INFORMATION

The Company conducts its business as a single operating segment being the acquisition and exploration of resource properties.

	Canada	Singapore	Indonesia	Total
June 30, 2012				
Exploration properties	$ -	$ -	$ 37,430,624	$ 37,430,624
Total assets	$ 21,476,990	$ 1,160,408	$ 38,247,114	$ 60,884,512
June 30, 2011				
Exploration properties	$ -	$ -	$ 22,796,908	$ 22,796,908
Total assets	$ 36,275,064	$ 1,206,100	$ 25,224,950	$ 62,706,114
July 1, 2010				
Exploration properties	$ 3,254,807	$ -	$ 19,155,609	$ 22,410,416
Total assets	$ 5,743,358	$ -	$ 19,155,609	$ 24,898,967

For the year ended June 30,	**2012**	**2011**
Net loss for the year – Canada	$ 2,701,587	$ 6,091,316
Net loss for the year – Singapore	445,860	112,000
Net loss for the year – Indonesia	1,164,964	380,037
Net loss for the year	$ 4,312,411	$ 6,583,353

For the year ended June 30,	**2012**	**2011**
Exploration properties written- off – Indonesia	$ -	$ 87,693
Impairment on investments – Indonesia	$ 102,807	$ -
Impairment on investments – Canada	$ 305,582	$ -

17. SUBSEQUENT EVENTS

Subsequent to June 30, 2012:

a) On July 18, 2012 the Company announced that Vale had completed its Phase 1 exploration work on the Sabalong property, has elected not to proceed to Phase 2 and has withdrawn from the Sabalong project. Vale will continue their exploration work on the Company's East Elang property and the Company now holds a 100% economic interest in the Sabalong project.

b) The Company also announced on July 18, 2012 the grant of 600,000 stock options to an officer and a director of the Company, exercisable at $0.25 per share and expiring five years after the date of grant. The stock options vest over 24 months, with 25% to vest on the six-month anniversary of the date of grant and 25% every six months thereafter.