

SOUTHERN ARC MINERALS INC.

FINANCIAL STATEMENTS
(Unaudited)

DECEMBER 31, 2005

UNAUDITED INTERIM FINANCIAL STATEMENTS

In accordance with National Instrument 51-102 released by the Canadian Securities Administrators, the Company disclosed that its auditors have not reviewed the unaudited financial statements for the period ended December 31, 2005.

SOUTHERN ARC MINERALS INC.
BALANCE SHEETS
(Unaudited)

	December 31, 2005	June 30, 2005
ASSETS		
Current		
Cash	\$ 566,668	\$ 1,013,447
Prepaid expense and deposit	7,550	-
Receivables	29,495	29,672
Subscriptions receivable	<u>604,983</u>	<u>-</u>
	1,208,696	1,043,119
Resource properties (Note 3)	<u>3,651,387</u>	<u>2,683,876</u>
	<u>\$ 4,860,083</u>	<u>\$ 3,726,995</u>

LIABILITIES AND SHAREHOLDERS' EQUITY

Current		
Accounts payable and accrued liabilities	<u>\$ 202,008</u>	<u>\$ 225,640</u>
Shareholders' equity		
Capital stock (Note 4)	5,150,583	3,703,212
Contributed surplus (Note 4)	386,486	379,461
Subscriptions receivable	(12,600)	-
Deficit	<u>(866,394)</u>	<u>(581,318)</u>
	<u>4,685,075</u>	<u>3,501,355</u>
	<u>\$ 4,860,083</u>	<u>\$ 3,726,995</u>

Nature and continuance of operations (Note 2)

Commitment (Note 7)

Subsequent events (Note 8)

On behalf of the Board:

_____ Director _____ Director

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

SOUTHERN ARC MINERALS INC.
STATEMENTS OF OPERATIONS AND DEFICIT
(Unaudited)

	Three Month Period Ended December 31, 2005	Three Month Period Ended December 31, 2004	Six Month Period Ended December 31, 2005	Period From Incorporation on August 19, 2004 to December 31, 2004
EXPENSES				
Consulting fees	\$ 55,900	\$ 38,200	\$ 102,418	\$ 46,200
Investor relations costs	-	-	7,294	-
Office and miscellaneous	16,776	10,268	32,415	11,411
Professional fees	37,068	19,273	71,818	23,416
Rent	7,335	5,800	14,385	7,400
Stock-based compensation (Note 4)	17,597	-	20,541	-
Transfer agent and filing fees	8,379	1,850	16,170	1,850
Travel	1,207	11,250	20,035	11,250
Loss for the period	(144,262)	(86,641)	(285,076)	(101,527)
Deficit, beginning of period	(722,132)	(14,886)	(581,318)	-
Deficit, end of period	\$ (866,394)	\$ (101,527)	\$ (866,394)	\$ (101,527)
Basic and diluted loss per share	\$ (0.00)	\$ (0.01)	\$ (0.01)	\$ (0.01)
Weighted average number of shares outstanding	34,859,348	9,000,001	34,733,343	9,000,001

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

SOUTHERN ARC MINERALS INC.
STATEMENTS OF CASH FLOWS
(Unaudited)

	Three Month Period Ended December 31, 2005	Three Month Period Ended December 31, 2004	Six Month Period Ended December 31, 2005	Period From Incorporation on August 19, 2004 to December 31, 2004
CASH FLOWS FROM				
OPERATING ACTIVITIES				
Loss for the period	\$ (144,262)	\$ (86,641)	\$ (285,076)	\$ (101,527)
Item not affecting cash:				
Stock-based compensation	17,597	-	20,541	-
Changes in non-cash working capital items:				
(Increase) decrease in receivables	(9,219)	(6,834)	177	(6,961)
Increase in prepaid expense and deposit	(7,550)	-	(7,550)	-
Increase (decrease) in accounts payable and accrued liabilities	<u>(958)</u>	<u>77,920</u>	<u>(57,967)</u>	<u>85,920</u>
Net cash used in operating activities	<u>(144,392)</u>	<u>(15,555)</u>	<u>(329,875)</u>	<u>(22,568)</u>
CASH FLOWS FROM				
INVESTING ACTIVITY				
Additions to resource properties	<u>(462,271)</u>	<u>(338,029)</u>	<u>(933,176)</u>	<u>(429,386)</u>
Net cash used in investing activity	<u>(462,271)</u>	<u>(338,029)</u>	<u>(933,176)</u>	<u>(429,386)</u>
CASH FLOWS FROM				
FINANCING ACTIVITIES				
Proceeds from issuance of shares	784,111	378,751	825,735	675,001
Share issue costs	(8,407)	-	(9,462)	-
Deferred financing costs	<u>-</u>	<u>(86,301)</u>	<u>-</u>	<u>(86,301)</u>
Net cash provided by financing activities	<u>775,704</u>	<u>292,450</u>	<u>816,272</u>	<u>588,700</u>
Change in cash during period	169,041	(61,134)	(446,779)	136,746
Cash, beginning of period	<u>397,627</u>	<u>197,880</u>	<u>1,013,447</u>	<u>-</u>
Cash, end of period	\$ 566,668	\$ 136,746	\$ 566,668	\$ 136,746
Cash paid for interest	\$ -	\$ -	\$ -	\$ -
Cash paid for income taxes	\$ -	\$ -	\$ -	\$ -

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

1. BASIS OF PRESENTATION

The interim period financial statements have been prepared by the Company in accordance with Canadian generally accepted accounting principles. All financial summaries included are presented on a comparative and consistent basis showing the figures for the corresponding period in the preceding year. The preparation of financial data is based on accounting principles and practices consistent with those used in the preparation of annual financial statements. Certain information and footnote disclosure normally included in financial statements prepared in accordance with generally accepted accounting principles has been condensed or omitted. These interim period statements should be read together with the audited financial statements and the accompanying notes included in the Company's latest annual report. In the opinion of the Company, its unaudited interim financial statements contain all adjustments necessary in order to present a fair statement of the results of the interim periods presented.

Certain reclassifications have been made to the prior period financial statements to conform to the current period presentation.

2. NATURE AND CONTINUANCE OF OPERATIONS

The Company was incorporated in British Columbia on August 19, 2004. To date, the Company has not generated significant revenues from operations and is considered to be in the development stage. The Company initially entered into an agreement with Sunda Mining Corporation ("Sunda") pursuant to which Sunda assigned its option to acquire an interest in certain mineral properties located in Indonesia from Indotan Inc. ("Indotan") (Note 3).

The Company completed an Initial Public Offering ("IPO") on June 2, 2005 and its common shares commenced trading on the TSX Venture Exchange ("TSX-V") on June 30, 2005.

The Company's continuing operations, as intended, are dependent on its ability to secure equity financing with which it intends to identify and evaluate opportunities for the acquisition of an interest in properties, corporations, assets or businesses, and once identified and evaluated, to negotiate an acquisition thereof or participation therein subject to receipt of shareholder and regulatory approval.

SOUTHERN ARC MINERALS INC.
NOTES TO THE FINANCIAL STATEMENTS
(Unaudited)
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3. RESOURCE PROPERTIES

December 31, 2005	Lombok Property	Sumbawa Property	Flores Property	Other Property	Total
Acquisition costs					
Balance, beginning of period	\$ 1,025,852	\$ 439,651	\$ -	\$ -	\$ 1,465,503
Additions	<u>25,402</u>	<u>10,886</u>	<u>17,941</u>	<u>23,797</u>	<u>78,026</u>
Balance, end of period	<u>1,051,254</u>	<u>450,537</u>	<u>17,941</u>	<u>23,797</u>	<u>1,543,529</u>
Deferred exploration costs					
Incurred during the period:					
Assaying, testing, surveying and analysis	29,432	62,899	-	-	92,331
Camp construction, supplies and accommodation	114,394	166,682	-	-	281,076
Geological and other consulting	187,591	208,553	-	-	396,144
Drilling	-	108,022	-	-	108,022
Travel	<u>4,291</u>	<u>7,621</u>	<u>-</u>	<u>-</u>	<u>11,912</u>
Total deferred exploration costs	335,708	553,777	-	-	889,485
Balance, beginning of period	<u>670,425</u>	<u>547,948</u>	<u>-</u>	<u>-</u>	<u>1,218,373</u>
Balance, end of period	<u>1,006,133</u>	<u>1,101,725</u>	<u>-</u>	<u>-</u>	<u>2,107,858</u>
Total resource property costs	<u>\$ 2,057,387</u>	<u>\$ 1,552,262</u>	<u>\$ 17,941</u>	<u>\$ 23,797</u>	<u>\$ 3,651,387</u>

June 30, 2005	Lombok Property	Sumbawa Property	Total
Acquisition costs			
Balance, beginning of period	\$ 22,798	\$ 9,770	\$ 32,568
Additions	<u>1,003,054</u>	<u>429,881</u>	<u>1,432,935</u>
Balance, end of period	<u>1,025,852</u>	<u>439,651</u>	<u>1,465,503</u>
Deferred exploration costs			
Incurred during the period:			
Assaying, testing and analysis	72,327	27,598	99,925
Camp construction, supplies and accommodation	162,005	142,055	304,060
Geological and other consulting	137,470	133,005	270,475
Drilling	<u>58,216</u>	<u>88,879</u>	<u>147,095</u>
Total deferred exploration costs	430,018	391,537	821,555
Balance, beginning of period	<u>240,407</u>	<u>156,411</u>	<u>396,818</u>
Balance, end of period	<u>670,425</u>	<u>547,948</u>	<u>1,218,373</u>

Total resource property costs	\$	1,696,277	\$	987,599	\$	2,683,876
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3. RESOURCE PROPERTIES (cont'd...)

Title to resource properties involves certain inherent risks due to the difficulties of determining the validity of certain mineral property interests as well as the potential for problems arising from the frequently ambiguous conveyancing history characteristic of many mineral properties. The Company has investigated title to all of its resource property interests and, to the best of its knowledge, title to all of its resource property interests are in good standing.

Lombok and Sumbawa Properties, Indonesia

The Company entered into an agreement with Sunda pursuant to which Sunda assigned its option to acquire certain rights on the Lombok property ("Lombok") and the Sumbawa property ("Sumbawa")(collectively the "Properties") to the Company, which Sunda had obtained from Indotan. In consideration for the assignment, the Company paid \$81,572 and issued 11,500,000 common shares valued at \$862,500 to Sunda. Effective February 25, 2005, the Company and Indotan entered into a settlement agreement with respect to certain outstanding matters related to the Properties. Pursuant to this settlement, the Company and Indotan entered into an amended and restated option agreement (the "Option Agreement") which sets out all of the rights and responsibilities of the Company and Indotan with respect to the Properties.

Pursuant to the Option Agreement, the Company has the option, directly with Indotan, to acquire all of its rights to the Properties in consideration for which the Company issued 1,000,000 common shares, valued at \$125,000, and paid \$180,000. The Company now has an option, until February, 2010 to acquire 50% of Indotan's 1% net smelter returns royalty ("NSR") on the Properties in consideration for the payment of \$500,000. Concurrently with the signing of the Option Agreement, the Company received an option to acquire the remaining 50% of the 1% NSR, held by Indotan, on the Properties in consideration for \$60,000 (paid) and \$500,000, which can be paid prior to the expiry of the option in February, 2010. All of the holders of the NSR agreed that the NSR only applies to the Properties as at July 21, 2004 and not to any additional property interests which the Company acquires after that date. In accordance with the terms of the Option Agreement, the Company also filed a listing application with the TSX-V and filed a prospectus for a public offering which has been completed.

In accordance with a limited power of attorney granted by Indotan pursuant to the Option Agreement, the Company caused Indotan to enter into two joint venture agreements (the "JV Agreements") with Indotan's Indonesian partner, PT Puri Permata Mega ("PTPM"), on the Properties. The Company has an initial 90% interest in the Lombok joint venture (the "Lombok JV") and the Sumbawa joint venture (the "Sumbawa JV"). At any time after a joint venture company is formed with respect to the Lombok JV and that company enters into a Contract of Work ("COW"), the Company can acquire a further 5% interest in the Lombok JV by providing funds to the Lombok JV in the amount of US\$700,000. At any time after a joint venture company is formed with respect to the Sumbawa JV and that company enters into a COW, the Company can acquire a further 5% interest in the Sumbawa JV by providing funds to the Sumbawa JV in the amount of US\$300,000. The Company has funded the respective amounts to each of the Lombok JV and Sumbawa JV.

3. RESOURCE PROPERTIES (cont'd...)

Lombok and Sumbawa Properties, Indonesia (cont'd...)

Lombok and Sumbawa are currently comprised of two separate applications to the Indonesian Government for a COW to conduct mining activities and earn mineral rights to certain mineral tenements. Upon the approval in principle of the COW, preliminary general survey licenses ("SIPPs") were granted for the properties. The SIPP permits the Company to conduct preliminary general survey work over the COW application areas. The Sumbawa SIPP was granted on January 2, 2004 for an initial 12 month period. On April 19, 2005, an extension and expansion of the Sumbawa Property SIPP was granted until April 19, 2006. The Lombok SIPP was granted on December 4, 2002. A 12 month extension was granted on February 16, 2004. On July 15, 2005, an extension and expansion of the Lombok SIPP was granted until February 16, 2006. The granting of a SIPP is not a guarantee that a COW will be entered into.

Flores Property, Indonesia

The Company has been granted four new exploration licenses over part of West Flores Island through its locally controlled Indonesian entity. The areas have been previously explored under fourth and seventh generation COW. The licenses were granted for twelve months and can be extended for a further twelve months.

Other Property, Indonesia

On September 7, 2005, the Company entered into an arms-length letter agreement pursuant to which it can acquire a 75% interest in an Indonesian mineral property (the "Property") by paying US\$25,000 and:

Upon execution of a formal agreement:

- ?? Paying US\$100,000;
- ?? Issuing 100,000 common shares; and
- ?? Paying US\$6,000 per month, increasing after one year to US\$10,000 per month.

Upon completion of the first 3,000 metres of drilling on the Property:

- ?? Paying US\$200,000;
- ?? Issuing 200,000 common shares; and

Upon commencement of commercial production:

- ?? Paying US\$3,000,000 less previous advances.

SOUTHERN ARC MINERALS INC.
NOTES TO THE FINANCIAL STATEMENTS
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4. CAPITAL STOCK AND CONTRIBUTED SURPLUS

	Number of Shares	Capital Stock	Contributed Surplus
Authorized			
Unlimited common shares without par value			
Issued			
Balance as at December 31, 2004	9,000,001	\$ 675,001	\$ -
Issued for cash	13,000,000	2,525,000	-
Issued for resource properties	12,500,000	987,500	-
Agent shares	100,000	25,000	-
Stock-based financing fees	-	-	67,456
Stock-based compensation	-	-	187,205
Share issuance costs	-	(384,489)	-
Agent warrants	-	(124,800)	124,800
	<u>34,600,001</u>	<u>3,703,212</u>	<u>379,461</u>
Balance as at June 30, 2005	34,600,001	3,703,212	379,461
Issued for cash	4,000,000	1,400,000	-
Exercise of warrants	173,275	56,834	(13,516)
Stock-based compensation	-	-	20,541
Share issuance costs	-	(9,463)	-
	<u>38,773,276</u>	<u>\$ 5,150,583</u>	<u>\$ 386,486</u>

The Company completed a private placement of 4,000,000 units at \$0.35 per unit. Each unit consists of one common share and a one-half of one common share purchase warrant. Each whole warrant entitles the holder to acquire one additional common share at \$0.50 for a period of two years. At December 31, 2005, subscriptions of \$617,584 were receivable, \$604,983 of which has been received subsequent to December 31, 2005.

During the six month period ended December 31, 2005, the Company issued 173,275 common shares at \$0.25 per share for total proceeds of \$42,791 pursuant to the exercise of agent option warrants previously granted.

The Company had 9,191,125 shares in escrow at December 31, 2005.

Stock options

The Company has a rolling stock option plan whereby, from time to time, at the discretion of the Board of Directors, stock options are granted to directors, officers and certain consultants. 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 exercise price of each option is based on the market price of the Company's common stock at the date of the grant less an applicable discount. The options can be granted for a maximum term of 5 years.

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4. CAPITAL STOCK AND CONTRIBUTED SURPLUS (cont'd...)

Stock options (cont'd...)

The Company has granted directors, officers and consultants, stock options to purchase common shares. A summary of the stock options granted is presented below.

	Number of Options	Weighted Average Exercise Price
Outstanding, December 31, 2004	-	\$ -
Granted	<u>3,400,000</u>	0.25
Outstanding, June 30, 2005	3,400,000	0.25
Granted	<u>75,000</u>	0.35
Outstanding, December 31, 2005	3,475,000	\$ 0.25
Number of options currently exercisable	3,307,686	\$ 0.25

During the six month period ended December 31, 2005, the Company reported stock-based compensation of \$20,541. This is a result of 100,000 options granted June 29, 2005, vesting as to 50,000 on June 30, 2006 and 50,000 on June 30, 2007 and 75,000 options granted on October 12, 2005, vesting as to 25,000 on December 12, 2005, 25,000 on February 12, 2006, 12,250 on July 12, 2006 and 12,250 on October 12, 2006. The fair value of compensatory options granted is estimated on the grant date using the Black-Scholes option pricing model.

The assumptions using the Black Scholes model are as follows:

	Stock Options
Expected dividend yield	0.0%
Expected volatility	75%
Risk-free interest rate	3.35%
Expected term in years	5 years

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4. CAPITAL STOCK AND CONTRIBUTED SURPLUS (cont'd...)

Warrants

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

	Number of Warrants		Weighted Average Exercise Price
Outstanding, December 31, 2004	-	\$	-
Granted	<u>2,880,000</u>		0.19
Outstanding, June 30, 2005	2,880,000		0.19
Granted	2,000,000		0.50
Exercised	<u>(173,275)</u>		0.25
Outstanding, December 31, 2005	4,706,725	\$	0.32

Share purchase options and warrants

At December 31, 2005, the Company had share purchase options and warrants outstanding enabling holders to acquire the following shares of common stock as follows:

	Number of Shares	Exercise Price	Expiry Date
Options			
	3,400,000	\$ 0.25	June 30, 2010
	75,000	0.35	October 12, 2010
Warrants			
	1,426,725	0.25	June 30, 2006
	1,280,000	0.125	April 15, 2007
	2,000,000	0.50	December 28, 2007

5. RELATED PARTY TRANSACTIONS

The Company entered into transactions with related parties as follows:

- a) Paid or accrued \$48,000 (December 31, 2004 - \$40,000) for consulting fees to a company controlled by a director of the Company.

5. RELATED PARTY TRANSACTIONS (cont'd...)

- b) Paid or accrued \$37,900 (December 31, 2004 - \$6,000) for professional fees to a firm in which an officer is a partner.
- c) Paid or accrued \$68,696 (December 31, 2004 - \$Nil) in geological consulting fees included in resource properties to an officer of the Company and a company controlled by an officer of the Company.
- d) Accounts payable included \$23,262 (December 31, 2004 - \$6,000) fees owing to a firm in which a director is a partner.

These transactions were in the normal course of operations and were measured at the exchange value, which represented the amount of consideration established and agreed to by the related parties.

6. FINANCIAL INSTRUMENTS

The Company's financial instruments consist of cash, receivables and accounts payable and accrued liabilities. Unless otherwise noted, it is management's opinion that the Company is not exposed to significant interest or credit risks arising from these financial instruments. The fair values of these financial instruments approximate their carrying values, unless otherwise noted.

Currency risk

The Company's largest non-monetary assets are its resource interests in Indonesia. The Company could accordingly be at risk for foreign currency fluctuations and developing legal and political environments.

The Company does not maintain significant cash or monetary assets or liabilities in Indonesia.

7. COMMITMENT

The Company has committed to rent office space for the following annual amounts:

2006	\$	28,000
2007		20,170

8. SUBSEQUENT EVENTS

- a) The Company entered into an agreement with PT Newmont Nusa Tenggara ("NNT") regarding a 8,860 ha property ("*Block 1*") which is contiguous with the western boundary of the Company's current Lombok Island SiPP license. The acquisition was completed through a relinquishment by NNT of *Block 1* area. The terms of the agreement include granting NNT a 2% net smelter return ("NSR") on any mineral production from the area covered by *Block 1* together with 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*.
- b) The Company issued 725,762 common shares at \$0.25 pursuant to the exercise of warrants previously granted.

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8. SUBSEQUENT EVENTS (cont'd...)

- c) The Company granted stock options to officers, directors and consultants of the company to acquire 2,275,000 common shares exercisable at \$0.56 per share exercisable for a period of five years; 250,000 of the options will be subject to vesting provisions, with one quarter of the total number vesting every three months.
- d) The Company issued 1,750,000 common shares at \$0.25 pursuant to the exercise of options previously granted to related parties.
- e) The Company re-priced 228,500 units included in the private placement pursuant to TSX-V terms. These units, originally issued at \$0.35, were adjusted to 142,812 units at \$0.56. Each re-priced unit consists of one common share and one-half of one common share purchase warrant, where one whole warrant entitles the holder to acquire one additional common share at \$0.66 for a period of two years. The total proceeds from the private placement were unchanged by the adjustment.