



CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS

**FOR THE THREE MONTHS ENDED
SEPTEMBER 30, 2011 and 2010**

(Expressed in Canadian dollars)

SOUTHERN ARC MINERALS INC.**CONDENSED CONSOLIDATED INTERIM STATEMENTS OF FINANCIAL POSITION**

(Unaudited – Prepared by Management)

(Expressed in Canadian dollars)

	September 30, 2011	June 30, 2011 (Note 15)	July 1, 2010 (Note 15)
ASSETS			
Current			
Cash	\$ 35,463,524	\$ 38,632,091	\$ 1,604,476
Receivables	79,036	155,528	29,668
Prepaid expense and deposit	125,644	94,816	7,534
Investment (Note 6)	-	-	835,799
	<u>35,668,204</u>	<u>38,882,435</u>	<u>2,477,477</u>
Equity investment (Note 3)	330,678	357,871	-
Property, plant and equipment (Note 4)	299,674	234,965	11,074
Exploration properties (Note 5)	26,345,975	23,401,805	22,410,416
Loans receivable (Note 5)	<u>467,505</u>	<u>433,935</u>	<u>-</u>
Total Assets	\$ 63,112,036	\$ 63,311,011	\$ 24,898,967

LIABILITIES AND SHAREHOLDERS' EQUITY**Current**

Accounts payable and accrued liabilities	\$ 1,494,651	\$ 1,529,554	\$ 383,246
Loans payable (Note 7)	-	-	1,614,600
	<u>1,494,651</u>	<u>1,529,554</u>	<u>1,997,846</u>

Shareholders' equity

Capital stock (Note 8)	74,151,488	74,151,488	30,474,172
Treasury stock (Note 8)	(1,170,000)	(1,170,000)	-
Share-based payment reserve (Note 8)	10,559,298	10,461,028	5,926,928
Non-controlling interest reserve	-	-	221,008
Deficit	<u>(22,339,970)</u>	<u>(22,066,164)</u>	<u>(15,692,612)</u>
Capital and reserve attributable to shareholders of Southern Arc Minerals Inc.	61,200,816	61,376,352	20,929,496
Non-controlling interest (Note 3)	<u>416,569</u>	<u>405,105</u>	<u>1,971,625</u>
Total equity	<u>61,617,385</u>	<u>61,781,457</u>	<u>22,901,121</u>

Total Liabilities and Shareholders' Equity	\$ 63,112,036	\$ 63,311,011	\$ 24,898,967
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Nature and continuance of operations (Note 1)

Subsequent events (Note 14)

Approved by the Board of Directors and authorized for issue on December 29, 2011:

“John Proust”

Director

“David Stone”

Director

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

SOUTHERN ARC MINERALS INC.**CONDENSED CONSOLIDATED INTERIM STATEMENTS OF COMPREHENSIVE LOSS
FOR THE THREE-MONTH PERIOD ENDED SEPTEMBER 30**

(Unaudited – Prepared by Management)

(Expressed in Canadian dollars)

	2011	2010 (Note 15)
EXPENSES		
Depreciation	\$ 5,764	\$ 554
Consulting fees	36,963	35,538
Foreign exchange gain	(341,462)	(15,371)
Investor relations	49,036	-
Management fees (Note 10)	141,000	100,500
Office and miscellaneous (Note 10)	211,960	60,340
Professional fees	66,778	159,314
Property investigation costs	-	74,302
Rent	25,524	4,086
Share-based compensation (Note 8)	98,270	2,665,816
Transfer agent and filing fees	6,883	1,872
Travel	48,700	12,813
Loss before other items	(349,416)	(3,099,764)
OTHER ITEMS		
Interest income	91,339	-
Loss on equity investment (Note 3)	(27,193)	-
	64,146	-
Loss before income taxes	(285,270)	(3,099,764)
Future income tax recovery	-	-
Comprehensive loss for the period	\$ (285,270)	\$ (3,099,764)
Comprehensive loss attributable to:		
Shareholders of Southern Arc Minerals Inc.	\$ (273,806)	\$ (3,034,677)
Non-controlling interests	(11,464)	(65,087)
	\$ (285,270)	\$ (3,099,764)
Basic and diluted loss per share	\$ (0.00)	\$ (0.04)
Weighted average number of shares outstanding	106,964,510	77,329,990

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

SOUTHERN ARC MINERALS INC.**CONDENSED CONSOLIDATED INTERIM STATEMENTS OF CASH FLOWS
FOR THE THREE-MONTH PERIOD ENDED SEPTEMBER 30**

(Unaudited – Prepared by Management)

(Expressed in Canadian dollars)

	2011	2010 (Note 15)
CASH FLOWS FROM OPERATING ACTIVITIES		
Comprehensive loss for the period	\$ (285,270)	\$ (3,099,764)
Items not affecting cash:		
Share-based compensation	98,270	2,665,816
Depreciation	5,764	554
Loss on equity investment	27,193	-
Foreign exchange gain	(341,462)	(15,371)
Changes in non-cash working capital items:		
Increase (decrease) in receivables	76,493	(31,507)
Prepaid expense and deposit	(30,828)	(7,630)
Increase (decrease) in accounts payable and accrued liabilities	<u>(78,113)</u>	<u>224,550</u>
Net cash used in operating activities	<u>(527,953)</u>	<u>(263,352)</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Investment in exploration properties	(3,322,226)	(430,806)
Acquisition of property, plant and equipment	(82,281)	-
Exploration advances received (Note 5)	432,861	-
Repayment of investment	<u>-</u>	<u>374</u>
Net cash used in investing activities	<u>(3,080,396)</u>	<u>(430,432)</u>
CASH FLOWS FROM FINANCING ACTIVITIES		
Share issuance cost paid by Nickel Oil and Gas	<u>-</u>	<u>(44,098)</u>
Net cash provided by financing activities	<u>-</u>	<u>(44,098)</u>
Effect of exchange rate changes on cash	<u>331,033</u>	<u>(19,829)</u>
Change in cash during period	(3,168,567)	(757,711)
Cash, beginning of period	<u>38,632,091</u>	<u>1,604,476</u>
Cash, end of period	\$ 35,463,524	\$ 846,765
Cash paid for income taxes	\$ -	\$ -
Cash paid for interest	\$ -	\$ -

Supplemental disclosure with respect to cash flows (Note 9)

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

SOUTHERN ARC MINERALS INC.

CONDENSED CONSOLIDATED INTERIM STATEMENTS OF CHANGES IN EQUITY

FOR THE THREE-MONTH PERIOD ENDED SEPTEMBER 30, 2011

(Unaudited – Prepared by Management)

(Expressed in Canadian dollars)

	Capital Stock	Treasury Stock	Share-based Payment Reserve	Non-controlling Interest Reserve	Deficit	Total	Non-controlling Interest	Total Equity
Balance at July 1, 2011 (Note 15)	\$ 74,151,488	\$ (1,170,000)	\$ 10,461,028	\$ -	\$ (22,066,164)	\$ 61,376,352	\$ 405,105	\$ 61,781,457
Comprehensive loss for the period	-	-	-	-	(273,806)	(273,806)	(11,464)	(285,270)
Share-based compensation	-	-	98,270	-	-	98,270	-	98,270
	-	-	98,270	-	(273,806)	(175,536)	(11,464)	187,000
Balance at September 30, 2011	\$ 74,151,488	\$ (1,170,000)	\$ 10,559,298	\$ -	\$ (22,339,970)	\$ 61,200,816	\$ 416,569	\$ 61,617,385
Balance at July 1, 2010 (Note 15)	\$ 30,474,172	\$ -	\$ 5,926,928	\$ 221,008	\$ (15,692,612)	\$ 20,929,496	\$ 1,971,625	\$ 22,901,121
Comprehensive loss for the period	-	-	-	-	(3,034,677)	(3,034,677)	(65,087)	(3,099,764)
Share issuance costs	-	-	-	(4,223)	-	(4,223)	(6,734)	(10,957)
Share-based compensation	-	-	2,665,816	-	-	2,665,816	-	2,665,816
	-	-	2,665,816	(4,223)	-	(303,084)	(71,821)	(444,905)
Balance at September 30, 2010 (Note 15)	\$ 30,474,172	\$ -	\$ 8,592,744	\$ 216,785	\$ (18,727,289)	\$ 20,556,412	\$ 1,899,804	\$ 22,456,216

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

SOUTHERN ARC MINERALS INC.

NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS

SEPTEMBER 30, 2011

(Expressed in Canadian dollars)

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 and Canada. 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 1500-885 West Georgia Street, Vancouver, British Columbia, Canada, V6C 3E8.

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 condensed consolidated interim 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 at least 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 condensed consolidated interim 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

Conversion to International Financial Reporting Standards

The Canadian Accounting Standards Board (“AcSB”) has replaced Canadian generally accepted accounting principles (“CAGAAP”) with International Financial Reporting Standards (“IFRS”) for publicly accountable enterprises for financial periods beginning on or after January 1, 2011.

These condensed consolidated interim financial statements have been prepared in accordance with International Accounting Standard 34, Interim Financial Reporting (“IAS 34”) and IFRS 1, *First-time adoption of IFRS* (“IFRS 1”) using accounting policies consistent with IFRS as issued by the International Accounting Standards Board (“IASB”) and interpretations of the International Financial Reporting Interpretations Committee (“IFRIC”).

These are the Company’s first IFRS condensed consolidated interim financial statements for part of the period covered by the first IFRS annual financial statements to be presented in accordance with IFRS for the year ending June 30, 2012. Previously, the Company prepared its annual and interim financial statements in accordance with CAGAAP.

As these are the Company’s first condensed consolidated interim financial statements prepared in accordance with IFRS, the Company’s disclosures exceed the minimum requirements under IAS 34. The Company has elected to exceed the minimum requirements in order to present the Company’s accounting policies in accordance with IFRS and the additional disclosures required under IFRS, which also highlight the changes from the Company’s June 30, 2011 annual consolidated financial statements prepared in accordance with CAGAAP. In fiscal 2013 and beyond, the Company may not provide the same amount of disclosure in the Company’s condensed consolidated interim financial statements under IFRS as the reader will be able to refer to the annual consolidated financial statements which will be prepared in accordance with IFRS.

SOUTHERN ARC MINERALS INC.

NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS

SEPTEMBER 30, 2011

(Expressed in Canadian dollars)

2. SIGNIFICANT ACCOUNTING POLICIES (cont'd...)

Principles of consolidation

These consolidated financial statements include:

- i) the accounts of the Company; and
- ii) its wholly-owned Canadian subsidiary West Indonesia Mining Holdings Inc.; and
- iii) 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
- iv) its wholly-owned Indonesian subsidiary PT. Selatan Arc Minerals; and
- v) its 85%-owned Indonesian subsidiaries: PT. Indotan Lombok Barat Bangkit and PT. Indotan Sumbawa Barat.

Significant intercompany balances and transactions have been eliminated upon consolidation.

Basis of presentation

The condensed interim financial statements have been prepared on a historical cost basis, as modified by the revaluation of available-for-sale financial assets.

Significant accounting judgement and estimates

The preparation of financial statements in conformity with IFRS requires the use of judgements and/or estimates that affect the amounts reported and disclosed in the consolidated financial statements and related notes. These judgements and estimates are based on management's best knowledge of the relevant facts and circumstances, having regard to previous experience, but actual results may differ materially from the amounts included in the financial statements. Information about such judgements and estimation is contained in the accounting policies and/or notes to the financial statements, and the key areas are summarized below:

- 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 income taxes requires judgement in applying tax laws and regulations, estimating the timing of the reversal of temporary differences, and estimating the realizability of future tax assets. These estimates impact current and future income tax assets and liabilities, and current and future income tax expenses (recovery).
- iii) 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.
- iv) 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.
- v) Although the Company has taken steps to verify title to mineral properties in which it has an interest, these procedures do not guarantee the Company's title. Such properties may be subject to prior agreements or transfers and title may be affected by undetected defects.
- vi) 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.

SOUTHERN ARC MINERALS INC.

NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS

SEPTEMBER 30, 2011

(Expressed in Canadian dollars)

2. SIGNIFICANT ACCOUNTING POLICIES (cont'd...)**The acquisition of Indotan Lombok Pte. Ltd. and Indotan Sumbawa Pte. Ltd.**

In December 2009, the Company acquired the right to the name Indotan Inc. as well as control over two companies (Indotan Lombok Pte. Ltd. and Indotan Sumbawa Pte. Ltd.) (each a "Singapore Company"). As consideration, the Company issued 3,500,000 common shares with a value of \$2,415,000 subject to two assignable options. The first option, which entitled the Company to acquire 500,000 of these shares at a price of \$0.50 per common share until August 15, 2010 at a price of \$0.50 per common share, was assigned to a related party in relation to a loan agreement (see Note 7(iii)) and was exercised during the period ended December 31, 2010. The second option entitled the Company 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. The Company exercised the remaining 1,300,000 \$0.90 options and currently holds those shares.

The acquisition of the Singapore Companies has been accounted for using the purchase method and the purchase price of \$2,415,000 has been allocated to exploration properties.

Property, plant and equipment

Telephone equipment is recorded at cost and amortized using the declining balance method at 20% per year.

Vehicle, furniture, computer, 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:

	Years
Vehicles	4
Furniture	4
Computers	4
Field equipment	4
Leasehold improvement	10

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.

SOUTHERN ARC MINERALS INC.

NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS

SEPTEMBER 30, 2011

(Expressed in Canadian dollars)

2. SIGNIFICANT ACCOUNTING POLICIES (cont'd...)**Exploration properties (cont'd...)**

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 characteristic 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 (see also Note 14., Subsequent Events).

(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.

(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.

SOUTHERN ARC MINERALS INC.**NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS**

SEPTEMBER 30, 2011

(Expressed in Canadian dollars)

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 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.

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.

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.

SOUTHERN ARC MINERALS INC.

NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS

SEPTEMBER 30, 2011

(Expressed in Canadian dollars)

2. SIGNIFICANT ACCOUNTING POLICIES (cont'd...)

Financial instruments (cont'd...)

Subsequent measurement

Financial assets

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:

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.

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.

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.

Financial liabilities

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.

SOUTHERN ARC MINERALS INC.

NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS

SEPTEMBER 30, 2011

(Expressed in Canadian dollars)

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 our accounting periods beginning on or after January 1, 2013. These include:

- IFRS 9 – Financial Instruments: Classification and Measurement
- IFRS 10 – Consolidated Financial Statements
- IFRS 11 – Joint Arrangement
- IFRS 12 – Disclosure of Interests in Other Entities
- IFRS 13 – Fair Value Measurement

3. INVESTMENT IN NICKEL OIL & GAS CORP.

On July 7, 2008, the Company acquired 15,300,000 common shares of Nickel Oil & Gas Corp. (“Nickel”), a related corporation by way of a common director, for a purchase price of \$5,355,000 representing 59.77% of the outstanding shares of Nickel at the time of acquisition. As a result of the share purchase, the Company acquired control of Nickel and, accordingly, effective July 7, 2008, the Company consolidated the financial results of Nickel. The acquisition of Nickel was accounted for using the purchase method. The total purchase price of \$5,355,000 was allocated as follows:

Cash	\$ 5,669,935
Exploration property	1,966,801
Receivables, payables and accrued liabilities	(752)
Non-controlling interest	<u>(2,280,984)</u>
	<u>\$ 5,355,000</u>

During the year ended June 30, 2010 and 2009, Nickel issued additional common shares to third parties, which diluted the Company’s ownership of Nickel to 38.54% (2009: 43.56%). During the year ended June 30, 2011, Nickel issued additional common shares to a director, which diluted the Company’s ownership percentage of Nickel to 37.59%, resulting in a gain on diluted interest in subsidiary of \$43,466 (2010: \$221,008).

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.

As at September 30, 2011 and June 30, 2011, the Company held 15,300,000 Nickel shares (37.59%) with a carrying value of \$330,678 (June 30, 2011: \$357,871). Under the equity method of accounting, the Company recorded a loss of \$27,193, which represented its equity ownership proportion of Nickel’s loss for the three-month period ended September 30, 2011.

Nickel holds a joint venture interest in the Brewster area of Alberta, Canada, where a party holding a 20% interest elected not to participate and has forfeited its interest until such time as the parties participating have collectively recovered a penalty equal to 400% of the costs of drilling and completion of these wells. Therefore, Nickel effectively holds a 40% interest in one section and a 68% interest in a second section until such time as the penalty has been recovered. Nickel’s joint venture partner solely funded the completion, equipping and tie-in costs of the well and will receive 100% of all revenue from the well until it recoups 125% of the payout costs incurred.

SOUTHERN ARC MINERALS INC.**NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS**

SEPTEMBER 30, 2011

(Expressed in Canadian dollars)

3. INVESTMENT IN NICKEL OIL & GAS CORP. (cont'd...)

Nickel entered into a farmout and option agreement, as amended, granting Nickel the option to earn certain oil and gas rights with respect to property in the Pine Creek area, Alberta. Under the amended agreement, Nickel earned a 60% working interest in two sections by funding 100% of the costs of drilling a horizontal well. Nickel's joint venture partner solely funded the completion, equipping and tie-in costs of the well. According to the amended agreement, the joint venture partner shall receive 100% of all revenue from the well until it recoups 125% of the payout costs incurred.

Nickel also holds a royalty equal to a 1.5% net smelter return ("NSR") in the Nickel Bay Project, Ontario. Nickel has granted an exclusive option to purchase up to two-thirds of this 1.5% NSR as follows: 0.33% for \$833,333 before November 26, 2014, an additional 0.33% for \$833,333 before November 26, 2014, and a further 0.34% for \$833,334 before the second anniversary of commercial production.

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	-	18,818	3,111	3,023	57,329	-	82,281
Balance, September 30, 2011	\$ 26,278	\$ 27,495	\$ 19,615	\$ 98,239	\$ 143,671	\$ 34,716	\$ 350,014
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 period	(443)	(907)	(1,130)	(5,472)	(8,750)	(870)	(17,572)
Balance, September 30, 2011	\$ (17,863)	\$ (1,627)	\$ (1,914)	\$ (13,297)	\$ (14,480)	\$ (1,159)	\$ (50,340)
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, September 30, 2011	\$ 8,415	\$ 25,868	\$ 17,701	\$ 84,942	\$ 129,191	\$ 33,557	\$ 299,674

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5. EXPLORATION PROPERTIES

	Lombok Property, Indonesia	Sumbawa Properties, Indonesia	Oil & Gas Properties, Canada	Total
Balance, July 1, 2010	<u>13,200,709</u>	<u>5,954,900</u>	<u>3,254,807</u>	<u>22,410,416</u>
Acquisition costs				
Adjustment to eliminate subsidiary (Note 3)	\$ -	\$ -	\$ (1,691)	\$ (1,691)
Total acquisition costs	<u>\$ -</u>	<u>\$ -</u>	<u>\$ (1,691)</u>	<u>\$ (1,691)</u>
Deferred exploration costs				
Assaying, surveying and analysis	30,052	169,637	-	199,689
Camp construction and other	1,343,056	490,888	-	1,833,944
Drilling	781,624	-	-	781,624
Geological and other consulting (Note 10)	586,631	445,591	-	1,032,222
Labour	314,508	171,902	-	486,410
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	<u>3,055,871</u>	<u>1,190,325</u>	<u>(3,253,116)</u>	<u>993,080</u>
Balance, June 30, 2011	<u>\$16,256,580</u>	<u>\$ 7,145,225</u>	<u>-</u>	<u>\$ 23,401,805</u>
Acquisition costs	<u>\$ -</u>	<u>\$ -</u>	<u>-</u>	<u>\$ -</u>
Deferred exploration costs				
Incurred during the year:				
Assaying, surveying and analysis	268,969	16,390	-	285,359
Camp construction and other	894,030	155,878	-	1,049,908
Drilling	666,299	-	-	666,299
Geological and other consulting (Note 10)	499,746	122,822	-	622,568
Labour	<u>288,163</u>	<u>31,873</u>	<u>-</u>	<u>320,036</u>
Total deferred exploration costs	<u>2,617,207</u>	<u>326,963</u>	<u>-</u>	<u>2,944,170</u>
Balance, September 30, 2011	<u>\$18,873,787</u>	<u>\$ 7,472,188</u>	<u>\$ -</u>	<u>\$ 26,345,975</u>

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, Mencanggih 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.

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5. EXPLORATION PROPERTIES (cont'd...)

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 companies has been accounted for using the purchase method and the purchase price of \$2,415,000 has been allocated to exploration properties.

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 ("PTPM") and a 10% carried interest is owned by the respective local governments.

The Company has advanced loans receivable of \$467,505 (US\$450,000) 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 ended June 30, 2011, the Company and Newcrest Mining Limited ("Newcrest") announced the signing of a Heads of Agreement ("Agreement") involving a joint venture investment in the Taliwang property. The Agreement (which is non-binding other than relationship of parties, exclusivity, confidentiality, access and governing law provisions) includes the following commercial terms:

- a) Newcrest will solely fund expenditures of US\$4 million ("Minimum Spend Obligation") on the Taliwang property during the first two years of the Agreement by way of a convertible loan;
- b) Upon completion of the Minimum Spend Obligation, Newcrest may convert its loan into shares equal to 75% of the shares of the Singapore Company that will have an 85% interest in the Taliwang mining permit;
- c) Following its acquisition of the shares in the Singapore Company, Newcrest may retain its interest in the Taliwang property by solely funding additional expenditures to a maximum of US\$46 million or to a completed feasibility study, whichever occurs first, with a minimum expenditure of US\$2 million per annum; and
- d) During the period of the Minimum Spend Obligation, a joint technical committee comprised of representatives of both parties and controlled by Newcrest will supervise and direct the exploration programs.

If Newcrest fully complies with the funding terms of the Agreement, it will earn an effective 63.75% interest in the Taliwang property, leaving Southern Arc with an effective 21.25% interest. The remaining interest is held by the West Sumbawa Regency government (10%) and PTPM (5%).

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;

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5. EXPLORATION PROPERTIES (cont'd...)

- 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 timeframes, 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.

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 September 30, 2011, Vale had advanced \$1,269,218 (June 30, 2011: \$836,357) to PT SAM and PT SAM held \$405,555 (June 30, 2011: \$204,426) of these funds as cash at September 30, 2011.

6. INVESTMENT

	September 30, 2011	June 30, 2011 (Note 17)	July 1, 2010 (Note 17)
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, 2011, the Company:

- i) received repayments of investment of \$374 (2010: \$16,967); and
- ii) disposed all of its holdings in MAVII notes for proceeds of \$890,277. Concurrently, the Company repaid the demand non-revolving bridge loan of \$550,000 (Note 7(i)) to its bank and recognized a gain on sale of investment of \$54,852 (2010: \$nil).

7. LOANS PAYABLE

	September 30, 2011	June 30, 2011 (Note 17)	July 1, 2010 (Note 17)
Non-revolving bridge loan	\$ -	\$ -	\$ 550,000
Non-interest-bearing loans from a director	-	-	1,064,600
	\$ -	\$ -	\$ 1,614,600

The Company's loans payable consist of:

- i) a demand non-revolving bridge loan from its bank of \$nil (June 30, 2011: \$nil, July 1, 2010: \$550,000);
- ii) a non-interest-bearing loan of \$nil (June 30, 2011: \$nil, July 1, 2010: \$1,064,600).

SOUTHERN ARC MINERALS INC.**NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS**

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7. LOANS PAYABLE (cont'd...)

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

- iii) 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 stock-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.
- iv) 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.
- v) 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.

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	<u>1,225,000</u>	<u>1,202,184</u>	<u>-</u>	<u>-</u>	<u>(539,184)</u>
Balance as at June 30, 2011	106,964,510	\$ 74,151,488	1,300,000	\$(1,170,000)	\$ 10,461,028
Share-based compensation	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>98,270</u>
Balance as at September 30, 2011	<u>106,964,510</u>	<u>\$ 74,151,488</u>	<u>1,300,000</u>	<u>\$(1,170,000)</u>	<u>\$ 10,559,298</u>

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).

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8. CAPITAL STOCK AND RESERVES (cont'd...)**Share options**

The Company grants share options in accordance with 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.

	Number of options	Weighted average exercise price
Outstanding at July 1, 2010	4,075,000	\$ 0.41
Granted	4,650,000	1.03
Exercised	<u>(1,225,000)</u>	<u>(0.54)</u>
Outstanding at June 30, 2011	7,500,000	\$ 0.77
Granted	<u>400,000</u>	<u>1.41</u>
Outstanding at September 30, 2011	7,900,000	\$ 0.81
Number of options currently exercisable	7,500,000	\$ 0.77

During the period ended September 30, 2011, the Company recorded share-based compensation of \$98,270 (2010: \$2,665,816) fair valued using the Black-Scholes option pricing model, as a result of the granting of 400,000 (2010: 3,650,000) options. These amounts were recorded as share-based reserve on the statement of financial position. The weighted average fair value of the options granted was \$1.34 (September 30, 2010: \$0.27) 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.

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

	Three-month period ended September 30, 2011	Three-month period ended September 30, 2010
Risk-free interest rate	2.01%	2.62%
Expected life of options	5 years	5 years
Annualized volatility	129.43%	121.25%
Dividend rate	0.00%	0.00%

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

At September 30, 2011, 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
	<u>7,900,000</u>		

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	<u>1,704,571</u>	<u>1.64</u>
Outstanding at June 30, 2011 and September 30, 2011	1,704,571	\$ 1.64

During the year ended June 30, 2011, the Company recorded share issue cost of \$1,013,070 (2010: \$nil) using the Black-Scholes option pricing model, as a result of the issuance of 1,704,571 (2010: nil) 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 (2010: \$nil) 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:

	Three-month period ended September 30, 2011	Three-month period ended September 30, 2010
Risk-free interest rate	Nil	1.56%
Expected life of options	Nil	1 year
Annualized volatility	Nil	67.93%
Dividend rate	Nil	0.00%

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8. CAPITAL STOCK AND RESERVES (cont'd...)**Warrants (cont'd...)**

At September 30, 2011, 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
	640,246	\$ 1.70	June 21, 2012
	<u>1,704,571</u>		

9. SUPPLEMENTAL DISCLOSURE WITH RESPECT TO CASH FLOWS

The Company had the following significant non-cash transactions:

During the three-month period ended September 30, 2011, the Company recorded \$98,270 (2010: \$2,665,816) to share-based reserve for share-based compensation.

At September 30, 2011, the Company had included in accounts payable \$108,749 (2010: \$29,474) of exploration expenditures.

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:

	For the three months ended September 30, 2011	For the three months ended September 30, 2010
Management and geological consulting fees	\$ 219,307	\$ 235,366
Share-based compensation	\$ 98,270	\$ 24,455,000

As at September 30, 2011, there were no related party balances arising from purchases of goods and services.

During the period ended September 30, 2011, the Company paid \$141,000 (2010: \$100,500) for management fees and \$37,500 (2010: \$10,500) 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. The related party balances have no fixed payment term and bear no interest.

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 period ended September 30, 2011, the Company paid a total of \$605,261 (US\$628,369) 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 period ended September 30, 2011 under this contract.

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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 a 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.

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.

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 September 30, 2011, the Company had US\$4,532,654 (approximately CDN\$4,708,975) and Indonesian Rupiah ("Rph") 274,054,302 (approximately CDN\$32,338) in cash and US\$1,364,751 (approximately CDN\$1,417,840) and Rph 58,181,431 (approximately CDN\$6,865) in account payable and accrued liabilities. As at September 30, 2011, US\$ amounts were converted at a rate of US\$0.9626 to CAD\$1 and Rph amounts were converted at a rate of Rph 8,475 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\$1,379,281 (approximately CDN\$1,330,040) 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.

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11. FINANCIAL INSTRUMENTS (cont'd...)**Fair value**

The fair value of the Company's financial instruments is approximated by their carrying value as at September 30, 2011, 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.

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

September 30, 2011	Level 1	Level 2	Level 3
Assets			
Cash	\$ 35,463,524	\$ -	\$ -
June 30, 2011	Level 1	Level 2	Level 3
Assets			
Cash	\$ 38,632,091	\$ -	\$ -
July 1, 2010	Level 1	Level 2	Level 3
Assets			
Cash	\$ 1,604,476	\$ -	\$ -
Investment	\$ -	\$ -	\$ 835,799

The Company's financial instruments consist of cash, receivables, loans receivable, investment, accounts payable and accrued liabilities, and loans payable.

12. COMMITMENT

The Company has committed to rent office space through August 31, 2012 totalling \$5,529 per month.

13. 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 equity issuances and advances from related parties to fund its operations and expects continued financial support through the next twelve months. 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 period ended September 30, 2011.

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(Expressed in Canadian dollars)

14. SUBSEQUENT EVENTS

- (a) On November 17, 2011 the Company granted an aggregate 1,255,000 share options to directors, officers and consultants of the Company, exercisable at a price of \$0.90 per common share, for a period of five years. The share options vest 25% every six months for a period of 24 months.
- (b) The Company curtailed drilling activity in the “production forest” areas of the Company’s West Lombok property due to an ongoing delay in receiving permits from the Ministry of Forests.

15. TRANSITION TO INTERNATIONAL FINANCIAL REPORTING STANDARDS

As stated in Note 2, these are the Company’s first condensed interim financial statements for the period covered by the first annual financial statements prepared in accordance with IFRS.

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

- in preparing the condensed interim financial statements for the three months ended September 30, 2011;
- the comparative information for the three months ended September 30, 2010;
- 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 three months ended September 30, 2010 and the financial statements for the year ended June 30, 2011, the Company has adjusted amounts reported previously in financial statements prepared in accordance with CAGAAP.

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 CA GAAP 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.

SOUTHERN ARC MINERALS INC.

NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS

SEPTEMBER 30, 2011

(Expressed in Canadian dollars)

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

(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.

Reconciliations of Canadian GAAP to IFRS

IFRS 1 requires an entity to reconcile equity, comprehensive loss and cash flows for prior periods. The Company’s first time adoption of IFRS did not have an effect on the total operating, investing and financing cash flows or comprehensive income (loss) for the period ending September 30, 2010 and year ending June 30, 2011. The following table represents the reconciliations from CAGAAP to IFRS for the respective periods noted for equity.

SOUTHERN ARC MINERALS INC.

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Reconciliation of Statement of Financial Position

	Note	As at July 1, 2010			As at September 30, 2010			As at June 30, 2011		
		Canadian GAAP	Effect of transition of IFRS	IFRS	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	846,765	-	846,765	38,632,091	-	38,632,091
Receivables		29,668	-	29,668	61,175	-	61,175	155,528	-	155,528
Prepaid expenses and deposit		7,534	-	7,534	15,164	-	15,164	94,816	-	94,816
Investment		835,799	-	835,799	835,425	-	835,425	-	-	-
Total current assets		2,477,477	-	2,477,477	1,758,529	-	1,758,529	38,882,435	-	38,882,435
Equity investment		-	-	-	-	-	-	357,871	-	357,871
Property, plant and equipment		11,074	-	11,074	10,520	-	10,520	234,965	-	234,965
Exploration properties		22,410,416	-	22,410,416	22,769,384	-	22,769,384	23,401,805	-	23,401,805
Loans receivable		-	-	-	-	-	-	433,935	-	433,935
TOTAL ASSETS		24,898,967	-	24,898,967	24,538,433	-	24,538,433	63,311,011	-	63,311,011
LIABILITIES AND SHAREHOLDERS' EQUITY										
Current										
Accounts payable and accrued liabilities		383,246	-	383,246	502,817	-	502,817	1,529,554	-	1,529,554
Loan payable		1,614,600	-	11,000	1,579,400	-	11,000	-	-	11,000
		1,997,846	-	394,246	2,082,217	-	513,817	1,529,554	-	1,540,554
Shareholders' Equity										
Capital stock		30,474,172	-	30,474,172	30,474,172	-	30,474,172	74,151,488	-	74,151,488
Treasury stock		-	-	-	-	-	-	(1,170,000)	-	(1,170,000)
Contributed surplus	15c	5,926,928	(5,926,928)	-	8,592,744	(8,592,744)	-	10,461,028	(10,461,028)	-
Share-based payment reserve	15c	-	5,926,928	5,926,928	-	8,592,744	8,592,744	-	10,461,028	10,461,028
Non-controlling interest reserve		221,008	-	221,008	216,785	-	216,785	-	-	-
Deficit		(15,692,612)	-	(15,692,612)	(18,727,289)	-	(18,727,289)	(22,066,164)	-	(22,066,164)
Capital and reserve attributable to shareholders of Southern Arc Minerals Inc.		20,929,496	-	20,929,496	20,556,412	-	20,556,412	61,376,352	-	61,376,352
Non-controlling interest		1,971,625	-	1,971,625	1,899,804	-	1,899,804	405,105	-	405,105
Total equity		22,901,121	-	22,901,121	22,456,216	-	22,456,216	61,781,457	-	61,781,457
TOTAL EQUITY AND LIABILITIES		24,898,967	-	23,295,367	24,538,433	-	22,970,033	63,311,011	-	63,322,011