



**MANAGEMENT'S DISCUSSION AND ANALYSIS**

**FOR THE NINE MONTHS ENDED MARCH 31, 2013**

**SOUTHERN ARC MINERALS INC.**  
**Management's Discussion and Analysis**  
**For the Nine Months Ended March 31, 2013**

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*This Management's Discussion and Analysis ("MD&A"), prepared as of May 28, 2013, should be read in conjunction with the audited consolidated annual financial statements of Southern Arc Minerals Inc. ("Southern Arc" or the "Company") for the year ended June 30, 2012, and the unaudited condensed consolidated interim financial statements for the nine month period ended March 31, 2013, which have been prepared in accordance with International Financial Reporting Standards ("IFRS"). All amounts are stated in Canadian dollars unless otherwise indicated. Additional information related to the Company can be found on SEDAR at [www.sedar.com](http://www.sedar.com) and on the Company's website at [www.southernarcminerals.com](http://www.southernarcminerals.com).*

*Statements in this MD&A that are not historical facts are "forward-looking statements" that are subject to risk factors set out in a cautionary note contained herein. Readers are cautioned not to put undue reliance on forward-looking statements.*

## **COMPANY OVERVIEW**

Southern Arc, through its subsidiaries (collectively "Southern Arc" or "the Company") is a mineral exploration company exploring for gold and copper-gold. The Company's current portfolio includes three exploration-stage projects with epithermal gold and copper-gold porphyry prospects on the Lombok and Sumbawa islands in Indonesia. The Company has completed approximately 47,720 metres of drilling at its flagship West Lombok project, which hosts several gold-rich copper porphyry and epithermal gold vein prospects. The Company's East Elang project is a grassroots exploration property that will be advanced in partnership with Vale S.A. ("Vale"). The Company has reached an agreement to sell its third property, Taliwang, to Coke Resources Limited ("Coke") in exchange for US\$500,000 and 15 million shares in Coke, contingent on Coke completing its initial public offering on the Australian Securities Exchange.

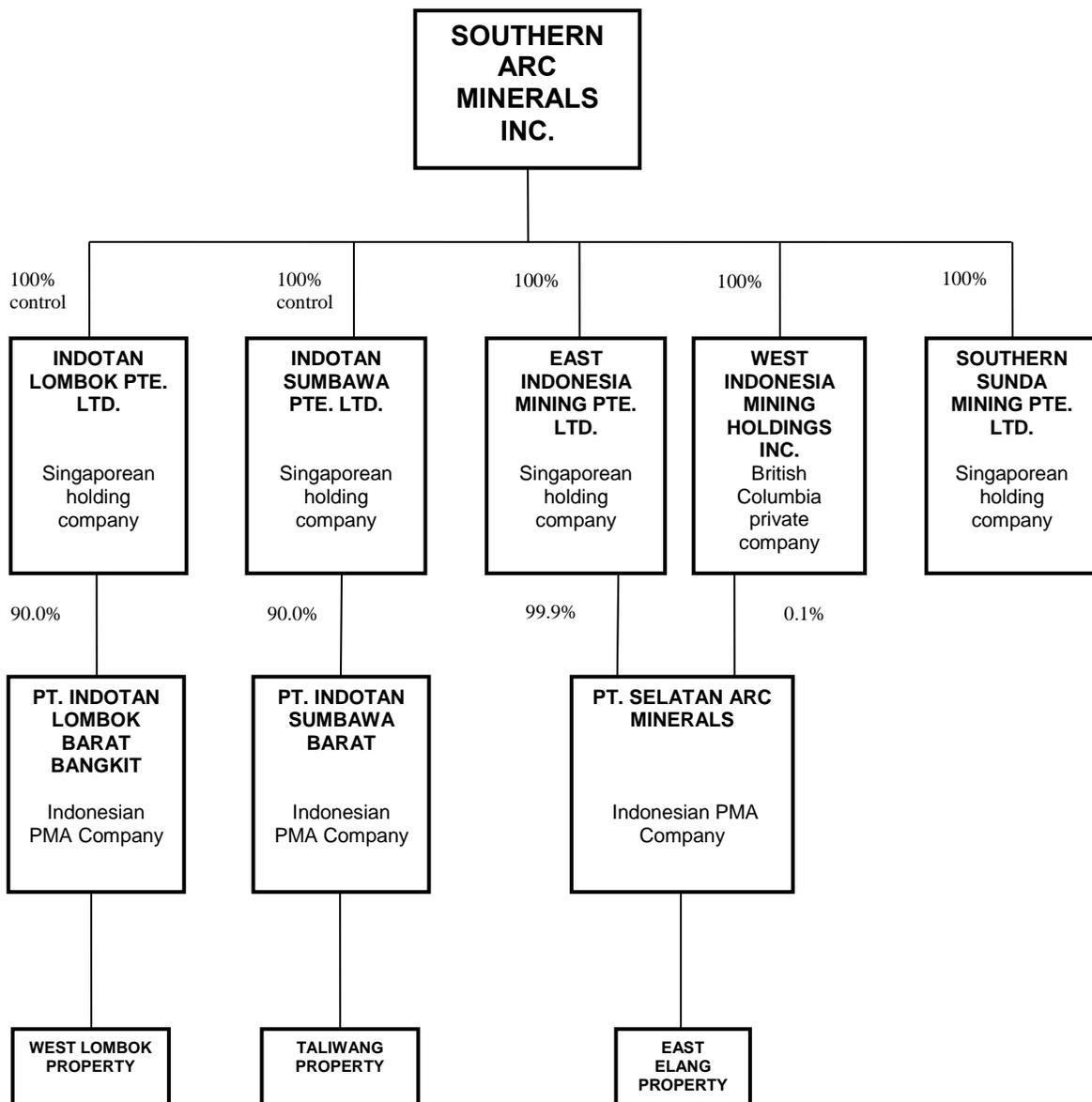
The Company has been actively exploring in Indonesia since 2005 and has assembled a technical team with decades of Indonesian experience, from grassroots exploration through to feasibility studies and production. The technical team is supported by executives, directors and advisors with extensive experience in corporate governance, business development and government relations, much of it Indonesian focused.

Southern Arc is committed to building strong relationships and bringing long-term benefits to its community partners, communicating openly and supporting local infrastructure and community initiatives through the Company's fully-funded foundation. The Company has forged cooperation agreements with the local government for two of its projects, offering the local government a 10% free-carry interest in the project. This relationship ensures it is in the local government's interest to support the Company's activities and that local communities will receive long-term benefits as the projects advance.

Southern Arc was incorporated in British Columbia, Canada on August 19, 2004, and is trading on the TSX Venture Exchange under the symbol "SA" and on the OTCQX International Exchange under the symbol "SOACF". To date, the Company has not generated revenues from operations and is considered to be in the exploration stage. The Company conducts its activities through wholly-owned subsidiaries, limited liability companies, partnerships and joint ventures, as outlined in the corporate chart below.

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**FINANCIAL SNAPSHOT**

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	<b>March 31, 2013</b>	<b>June 30, 2012</b>
Total assets	\$ 53,939,440	\$ 60,884,512
Exploration properties	37,212,907	37,430,624
Working capital	15,164,760	21,035,112
Comprehensive loss	(6,457,199)	(4,312,411)
Basic and diluted loss per share	(0.06)	(0.04)

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**EXPLORATION UPDATE AND OUTLOOK**

At the end of 2012 Southern Arc's Board of Directors conducted a strategic review of the Company's projects and exploration strategy. The Board ranked the Company's projects and considered the best strategy to protect and promote shareholder value. On December 13, 2012, Southern Arc announced the Board's decision to: proceed with drilling at the West Lombok project; retain the Company's no-cost joint venture interest in the East Elang project; sell the Taliwang project, subject to certain conditions; relinquish the Sabalong project; and actively pursue new advanced-stage, gold-focused opportunities within Indonesia and other countries. This narrowed focus enabled Southern Arc to dedicate resources in the near-term to advancement of the West Lombok project while retaining the financial flexibility to consider new opportunities.

Following the Board's decision, Southern Arc commenced exploration in the Mencanggah prospect focused on epithermal gold-bearing structural breccias. Since mid-December 2012, Southern Arc has drilled 14 holes at the Bising target and 16 holes at the Tibu Serai target. With this phase of drilling complete, Southern Arc now has enough data to complete a preliminary National Instrument 43-101 compliant resource estimate for portions of the property. Since December 2011, Southern Arc has worked closely with SRK Consulting (Canada) Inc. ("SRK"), an internationally renowned, independent consulting service to major, intermediate and junior mining and exploration companies. SRK helped to prepare the drill program for epithermal gold targets within the Pelangan and Mencanggah prospects and has been reviewing the data throughout the drilling process. Southern Arc expects to have a technical report by mid-2013 that provides an inferred resource estimate for the property incorporating epithermal-gold mineralization from parts of the Raja target (Pelangan prospect), Bising and Tibu Serai targets (Mencanggah prospect), as well as porphyry copper-gold mineralization from the Selodong prospect. The report will also include SRK's recommendations for additional drilling for both resource upgrade and expansion, which will help to focus next steps for the project.

Recent results have demonstrated the prospectivity of the Mencanggah prospect, and many targets with high-grade surface results remain untested at Mencanggah and other parts of the property. While awaiting results of the resource estimate, Southern Arc's exploration team will continue to work with SRK to plan next steps at the property, which may include engineering and metallurgical studies.

**West Lombok Property (Lombok Island)**

The West Lombok project covers a 13-km long by 7-km wide structural corridor of mineralization and alteration hosting porphyry copper-gold and epithermal gold deposits. The two main epithermal prospects on the property, Pelangan and Mencanggah, cover broad areas of 4 km by 5 km and 6.5 km by 4.5 km, respectively, that host numerous structurally-controlled silica ledges variably overprinted by high-grade quartz veins and breccias. Individual tabular ledge bodies range in thickness from 2 to 66 metres, with a strike length of up to 1,000 metres and a vertical extent of greater than 300 metres. Southern Arc has completed 26,477 metres of drilling to date on epithermal gold mineralization in the Pelangan and Mencanggah prospects, confirming broad zones of low-grade mineralization throughout the property, high-grade events typical of epithermal boiling zones and several high-grade shoots. At the Selodong porphyry copper-gold intrusive complex in the southeastern end of the property, Southern Arc has completed 20,046 metres of drilling to date with the majority of drill holes intersecting broad zones of significant copper-gold mineralization. In 2011, the Company completed an airborne geophysical survey of the West Lombok project at 50-metre spacings to define both near-surface and buried copper-gold porphyry targets. Industry experts including Dr. Steve Garwin, Southern Arc's Senior Technical Advisor, modelled and interpreted the results of the survey in conjunction with the Company's geological and geochemistry database, and identified 17 porphyry targets on the property. A number of these targets have already had a limited amount of drill testing and

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demonstrated zones hosting high-grade gold-rich porphyry copper mineralization, supporting the outcome of the prospectivity analysis.

On November 20, 2012, Southern Arc announced that the forestry permit required to conduct drilling on the property, known as a *Pinjam Pakai* (borrow to use) permit, had been received. On December 13, 2012, Southern Arc announced that it was commencing drilling at West Lombok, with a near-term focus on epithermal gold-bearing structural breccias in the Mencanggah prospect. Southern Arc mobilized three drill rigs to the Bising target and initiated a Phase 2 drill program to infill and expand the zones of mineralization adjacent to wide mineralized intercepts identified with Phase 1 drilling. Southern Arc completed 11 Phase 2 holes at Bising (1,375.6 metres, Appendix 1). Based on those results, the Company drilled three additional holes (423.0 metres, Appendix 1) to test an inferred plunge to higher-grade mineralization and infill in a 200-metre wide gap between previous drill holes MCG031 and MCG032 to test for continuity of mineralization.

The extensive width (up to 66 metres width in surface outcrop) of the main Bising epithermal body is inferred to result from the intersection of geological structures: a major west-northwest trending fault intersected by several north-northwest trending faults, the latter of which form the dominant gold mineralized trend in the West Lombok district. Phase 2 drilling at the Bising target has demonstrated the consistency and width of mineralization in the area, with a large proportion of the drill holes intersecting wide intervals averaging greater than 1 g/t gold mineralization. Particularly encouraging is the result from MCG057, which confirmed continuity between other wide > 1 g/t gold intervals intersected to the west (MCG030, 041, 042, 028) and east (MCG032) of this location.

Highlight Phase 2 drilling intercepts from the Bising target include:

MCG041	66.8 m @ 0.66 g/t gold and 2.4 g/t silver from 20.0 m including 22.9 m @ 1.16 g/t gold and 2.7 g/t silver from 22.0 m
MCG042	53.2 m @ 1.04 g/t gold and 1.4 g/t silver from 16.0 m including 1.0 m @ 9.67 g/t gold and 0.8 g/t silver from 32.2 m and 0.30 m @ 10.2 g/t gold and 61.3 g/t silver from 46.3 m
MCG043	42.4 m @ 0.51 g/t gold and 1.1 g/t silver from 20.7 m including 10.1 m @ 1.0 g/t gold and 1.9 g/t silver from 39.0 m
MCG044	58.15 m @ 0.61 g/t gold from 87.85 m including 11.0 m @ 1.3 g/t gold from 104.6 m and 7.5 m @ 1.1 g/t gold from 123.0 m
MCG056	41.40 m @ 0.69 g/t gold and 1.4 g/t silver from 97.50 m including 13.70 m @ 0.94 g/t gold and 0.9 g/t silver from 105.00 m
MCG057	52.70 m @ 0.68 g/t gold and 2.3 g/t silver from 7.55 m including 27.15 m @ 1.00 g/t gold and 3.4 g/t silver from 28.40 m
MCG059	34.15 m @ 0.52 g/t gold and 1.1 g/t silver from 94.85 m 17.35 m @ 0.78 g/t gold and 1.7 g/t silver from 111.65 m

In 2013 Southern Arc also commenced Phase 1 drilling at the Tibu Serai target in the Mencanggah prospect, where surface channel samples have returned the highest-grade mineralization on the property to date. Tibu Serai comprises a 2 km by 2 km area at the northern end of the Mencanggah prospect and hosts numerous northwest and north-northwest trending linear gold mineralized structures. The majority of these well-exposed mineralized zones have been systematically channel sampled and have returned numerous highly gold-anomalous intervals. Highlight channel samples include 7.1 m @ 53.53 g/t gold, 2.25 m @ 12.13 g/t gold, 0.6 m @ 69.0 g/t gold and 2.0 m @ 9.8 g/t gold. Southern Arc initially drilled seven widely spaced shallow holes (1,124.2 metres, Appendix 2) targeting down-dip extensions from high-grade surface channel samples. The results confirmed the down-dip continuity of mineralization below surface but tested only a fraction of the strike of the mineralized breccias at Tibu Serai. Drillhole MCG055 was particularly encouraging, as this mineralization lies adjacent to an inferred major cross-cutting structural break evidenced from the magnetic survey data and mapped outcrop patterns. Southern Arc's exploration team believes this major structural break may be influencing higher gold grades in its proximity, and drilled nine

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further holes (1,273.0 metres, Appendix 2) to test extensions of this high-grade intercept. Eight of the holes successfully encountered mineralization, demonstrating continuity of mineralization along strike and at depth. Results showed localized development of high-grade shoot zones which remain open and will require further drilling to quantify, and also gave strong encouragement for drill testing of numerous other untested high-grade surface anomalies within Mencanggah and Pelangan. Highlight intercepts from Phase 1 drilling at the Tibu Serai target include:

MCG055	24.8 m @ 4.27 g/t gold and 0.6 g/t silver from 48.6 m including 0.5 m @ 71.0 g/t gold and 1.9 g/t silver from 49.4 m and 5.4 m @ 9.44 g/t gold and 1.3 g/t silver from 67.2 m including 0.55 m @ 71.0 g/t gold and 6.8 g/t silver from 71.75 m
MCG050	10.77 m @ 1.01 g/t gold and 4.0 g/t silver from 100.23 m including 2.15 m @ 3.87 g/t gold and 17.0 g/t silver from 108.85 m including 0.5 m @ 15.0 g/t gold and 67.4 g/t silver from 110.5 m
MCG051	8.7 m @ 1.56 g/t gold and 0.71 g/t silver from 114.7 m including 3.5 m @ 3.33 g/t gold and 1.0 g/t silver from 119.9 m 8.85 m @ 0.74 g/t gold and 0.4 g/t silver from 136.45 m
MCG049	12.1 m @ 1.07 g/t gold and 1.2 g/t silver from 31.3 m including 4.2 m @ 2.17 g/t gold and 1.7 g/t silver from 34.65 m 3.3 m @ 1.21 g/t gold and 1.2 g/t silver from 78.7 m
MCG058	0.70 m @ 13.50 g/t gold and 2.3 g/t silver from 3.20 m 18.70 m @ 2.46 g/t gold and 0.4 g/t silver from 58.80 m including 6.90 m @ 5.65 g/t gold and 0.5 g/t silver from 70.60 m including 1.10 m @ 31.97 g/t gold and 1.9 g/t silver from 76.40 m
MCG060	22.50 m @ 1.60 g/t gold and 1.5 g/t silver from 60.30 m including 5.10 m @ 5.29 g/t gold and 5.3 g/t silver from 76.70 m
MCG067	4.50 m @ 7.79 g/t gold and 0.7 g/t silver from 70.60 m including 0.60 m @ 16.60 g/t gold and 1.6 g/t silver from 70.60 m and 1.05 m @ 20.94 g/t gold and 1.0 g/t silver from 73.40 m
MCG061	26.30 m @ 1.22 g/t gold and 0.2 g/t silver from 96.50 m including 8.00 m @ 3.21 g/t gold and 0.3 g/t silver from 114.80 m including 0.90 m @ 11.20 g/t gold and 0.2 g/t silver from 117.60 m and 0.80 m @ 13.80 g/t gold and 0.7 g/t silver from 122.00 m
MCG062	3.95 m @ 3.55 g/t gold and 0.2 g/t silver from 21.65 m including 0.80 m @ 11.70 g/t gold and 0.2 g/t silver from 23.90 m

In March 2013, Southern Arc also drilled two holes (1,197.7m) to test deep porphyry targets beneath the Mencanggah lithocap. The holes were targeting modeled magnetic geophysical anomalies underlying the Tibu Serai area. Neither hole encountered significant porphyry-style mineralization, instead intersecting magnetite rich diorite and volcanics, respectively. Southern Arc remains very optimistic about porphyry copper exploration on the property. Areas in the Selodong prospect where previous drilling encountered gold-rich high-grade porphyry drill intersections have similar geophysical signatures to other porphyry targets on the property. Porphyry deposits often occur in clusters, and numerous porphyry targets remain to be drill tested beneath the lithocaps at Mencanggah, Pelangan and Selodong.

**East Elang Property (Sumbawa Island)**

The East Elang property is located adjacent to Newmont's Elang-Dodo property, which hosts a large copper-gold porphyry deposit. Aerial photography and lithographical studies suggest that the Elang mineralized structure may extend onto Southern Arc's East Elang property. While the property is considered highly prospective due to its location and results from aerial surveys, exploration has been deferred pending reclassification of the property's forestry status and issuance of the appropriate permits.

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Under the terms of the October 2010 option and joint venture agreement, the property will be advanced in partnership with Vale, whereby Vale can earn a 75% interest in the East Elang property by advancing the property to bankable feasibility study with a minimum Phase 1 expenditure of US\$1.2 million within one year from the date on which Southern Arc receives a Ministry of Forestry *Pinjam Pakai* permit for the property. Southern Arc has not yet applied for the *Pinjam Pakai* permit because the majority of the East Elang property, including the most prospective areas, is designated as primary forest and subject to a moratorium on exploration and mining activities. In May 2013 the Indonesian government extended the moratorium to May 2015. As a result, there can be only very limited exploration activity on the property until either a reclassification is granted or the moratorium is lifted. Southern Arc has requested a reclassification of the property's forestry status and has also applied for suspension (back-dated for two years) of the mining business license ("IUP") until the reclassification process has been completed, ensuring that Southern Arc and Vale have adequate time to evaluate the property once exploration commences. In the interim, Company field activities continue to focus on CSR engagement at the village and sub-district levels.

**Other properties**

Southern Arc is actively pursuing a number of acquisition and partnership opportunities, both within Indonesia and in other countries, with the objective of adding value for shareholders by expanding the Company's project portfolio.

**PROPERTY REVIEW**

The Company's accounting policy is to record its exploration properties at cost. Exploration and evaluation expenditures relating to exploration properties are deferred until either the properties are brought into production, at which time they are amortized on a unit of production basis, or the properties are sold or abandoned, at which time the deferred costs are written off.

Southern Arc has acquired and relinquished a number of properties since its inception in 2004, choosing to focus its effort on areas determined, by management, to have the highest prospectivity for gold and copper-gold mineralization in areas amenable to both exploration and production. Following a strategic review of the Company's projects and exploration strategy at the end of 2012, Southern Arc further narrowed its focus to two core properties: West Lombok and East Elang. Southern Arc has accepted an offer to sell its Taliwang project, subject to certain conditions, and has relinquished all rights to its Sabalong project.

**West Lombok Property (Lombok Island)**

The Company acquired its original interest in the West Lombok property in 2005 by paying \$57,100 and issuing 8,050,000 common shares (valued at \$603,750) to Sunda Mining Corporation ("Sunda") and by paying \$126,000 and issuing 700,000 common shares (valued at \$87,500) to Indotan Inc. ("Indotan"). The Company also granted a 0.5% net smelting royalty ("NSR") to individuals related to Sunda and a 1% NSR to Indotan on approximately 8% of the current West Lombok property, which excludes Block 1 described below.

The West Lombok property comprises a 13-km long by 7-km wide northwest-trending structural corridor of hydrothermal mineralization and alteration that hosts the Pelangan epithermal gold prospect, the Mencanggih epithermal/porphyry copper-gold district and the Selodong porphyry copper-gold prospect. This area was previously held by PT Newmont Nusa Tenggara ("Newmont"), a subsidiary of Newmont Mining Corporation. In August 2005, Southern Arc entered into an agreement with Newmont regarding a property ("Block 1") that now forms the western portion of the West Lombok property and is included in the West Lombok 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.

Southern has given a free-carry interest for 10% of the West Lombok project to the local Regency Government as per a cooperation agreement signed in December 2010, ensuring government support for the project and long-term benefits for local communities as the project advances. Southern Arc believes that having the local Regency Government as an equity partner creates a synergistic and mutually beneficial environment for advancement of the project. This relationship ensures it

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is in the local government's interest to support the Company's activities and that local communities will receive benefits directly from Southern Arc's success at the project. The Regency interest is loan-carried through to a production scenario, whereby debt and equity contribution are paid back through dividends or other financial means.

The exploration stage of the West Lombok IUP (encompassing 10,088 hectares), issued in January 2011, is initially valid for five years and permits the Company to pursue exploration activities up to the conclusion of a feasibility study. This period may be extended with approval of the Indonesian Government. On approval of a feasibility study, the Company can automatically transition the IUP into the exploitation stage, with the right to conduct mining production on this property for 20 years with the potential for two further 10-year extension periods. In addition to the IUP, the Ministry of Forestry *Pinjam Pakai* permit required for exploration activities within areas designated as production forest was issued in November 2012. On the West Lombok property, 1.1% of the area is designated protected forest (no open-pit mining), 55.1% is designated production forest (open-pit mining allowed) and 43.8% has no forestry designation (no restriction on mining activities).

Since receiving its West Lombok IUP in January 2011, Southern Arc has proactively engaged with local communities to discuss its exploration and development plans and to address questions and concerns. The Company offers employment and training programs and undertakes an extensive CSR program through its fully-funded foundation, with an emphasis on education, community health, environmental protection and economic empowerment of local communities. In 2012, Southern Arc granted six micro-credit loans to local village members to support entrepreneurial initiatives in 2013 has continued to support local communities by assisting with road maintenance and supporting requests for assistance with educational programs and maintaining religious buildings.

*Pelangan prospect*

The Pelangan prospect, covering an approximate 4-km by 5-km area in the northwest part of the property, comprises four main epithermal gold targets including Tanjung-Jati, Kayu Putih, Raja and Lala. Southern Arc has completed 13,295 metres of drilling on the Pelangan prospect. Phase 1 drilling was completed at the Pelangan prospect in 2007, together with geological mapping and outcrop channel sampling of sub-parallel vein structures. Phase 2 drilling was focused on identifying and defining high-grade shoots within large continuous structures. The presence of such shoots are suggested by a high-grade quartz episode within the mineralized structural breccias and increasing gold grade with depth. Drilling shows that these breccia bodies range in true width between 3 metres and 20 metres. Phase 2 drilling confirmed high-grade events typical of epithermal boiling zones at both the Central Raja and Tanjung Lode structures and identified three high-grade shoots that will be examined further with future drilling. All results are available on SEDAR at [www.sedar.com](http://www.sedar.com) on the Company's website at [www.southernarcminerals.com](http://www.southernarcminerals.com).

*Mencanggah prospect*

The Mencanggah prospect comprises a large cluster of west-northwest to north-trending, gold-bearing epithermal mineralized structural breccias concentrated in a 6.5-km by 4.5-km area, with the potential to host copper-gold porphyry mineralization at depth. Channel sampling indicates that these breccia bodies range in true width between 3 metres and 66 metres. The Bising and Waterfall targets have been drill tested and show encouraging results, especially at the Bising target. Part of the drilling completed at the Tibu Serai target will be incorporated into the pending resource estimate. Drilling at the Tibu Serai target has demonstrated the contiguous nature of high-grade mineralization along one of the mineralized structures at Mencanggah and highlights the potential of numerous other high-grade surface indications yet to be drill tested at Mencanggah and the rest of the project. Southern Arc completed 13,182 metres of drilling for epithermal gold on the Mencanggah prospect in Phase 1 and Phase 2 exploration. All results are available on the Company's website and on SEDAR.

*Mencanggah prospect – porphyry copper-gold exploration*

While the majority of porphyry exploration has focused on the Selodong prospect, two holes were drilled in March 2013 (1,197 metres) to test deep targets beneath the Mencanggah lithocap (Appendix 3). Neither hole encountered significant porphyry-style mineralization, instead intersecting magnetite rich diorite and volcanics, respectively. Numerous porphyry targets remain to be tested beneath the lithocaps at Mencanggah, Pelangan prospect and Selodong.

*Selodong prospect*

As a result of the porphyry prospectivity study, in calendar Q1-2012 the Company initiated drilling at the Belikat and Blongas East targets in the Selodong prospect and completed 974 metres in two holes. Drilling returned encouraging results

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and confirmed the methodology behind the prospectivity study for targeting shallow or blind porphyry mineralization throughout the property. The Company completed Phase 1 drilling at Selodong in September 2008 with 30 holes totaling 17,859 metres. These holes tested seven of the 14 porphyry copper-gold targets, with the majority intersecting broad zones (126.45 to 855.11 m) of significant copper-gold mineralization. All results are available on the Company's website and on SEDAR.

**East Elang Property (Sumbawa Island)**

The East Elang property covers 9,670 hectares immediately to the east of Newmont's Elang-Dodo property, which hosts a large copper-gold porphyry deposit. Southern Arc acquired the East Elang property in 2006 by way of a mining license, which was subsequently transitioned into a seven-year IUP license in December 2009. The IUP is held by Southern Arc's subsidiary, PT. Selatan Arc Minerals.

In October 2010, the Company entered into an option and joint venture agreement with Vale to advance the East Elang property. Vale can earn a 75% interest in PT. Selatan Arc Minerals by funding exploration through to completion of a bankable feasibility study within an agreed-upon time frame. Phase 1 exploration would require a minimum of US\$1,200,000 of exploration expenditures within one year from the date that Southern Arc receives a *Pinjam Pakai* permit from the Ministry of Forestry.

On the East Elang property, 60.3% of the area is designated primary forest, 34.2% is designated production forest and 5.5% has no forestry classification. The Indonesian government has imposed a moratorium on exploration and mining activities in areas designated as primary forest, and has extended the moratorium to May 2015. While the property is considered highly prospective due to its location and results from aerial surveys, exploration of this property has been deferred pending reclassification of the property's forestry status and receipt of the appropriate permits. Unless such reclassification is granted or the moratorium lifted, the Company cannot commence any significant exploration activities on the property. Southern Arc has requested reclassification of the property and has applied to the Regency authorities for suspension (back-dated for two [four?] years) of the IUP license until the reclassification process has been completed, to ensure Southern Arc and Vale have adequate time to evaluate the property once exploration commences.

**Taliwang Property (Sumbawa Island)**

During 2005, the Company acquired its original interest in the Taliwang property by paying \$24,472 and issuing 3,450,000 common shares (valued at \$258,750) to Sunda Mining Corporation ("Sunda") and by paying \$54,000 and issuing 300,000 common shares (valued at \$37,500) to Indotan Inc. ("Indotan"). The Company also granted a 0.5% NSR to individuals related to Sunda and a 2% NSR to Indotan.

The Taliwang property covers 31,200 hectares on Sumbawa Island. An IUP for the property was issued by the Regent of West Sumbawa in July 2010. Southern Arc drilled 63 drill holes on the Taliwang property for a total of 8,786.6 metres, identifying a gold-silver bearing epithermal vein system, near-surface porphyry copper-gold targets with associated surface high-sulphidation epithermal signatures, and sedimentary gold-hosted targets. In December 2012, following a strategic review of the Company's projects and exploration strategy, the Company agreed to sell its 90% interest in the Taliwang project in exchange for US\$500,000 and 15 million shares of the acquiring company, Coke Resources Limited ("Coke"). The transaction is contingent on Coke completing its initial public offering on the Australian Securities Exchange and certain other conditions. With 15 million shares, Southern Arc would own approximately 8% of Coke. The shares will be held in escrow for a period of six months from the date Coke lists on the Australian Securities Exchange. Based on an expected value of A\$0.20 per share, the transaction values the Company's interest in the Taliwang property at approximately \$3.6 million. As a result, during the period ended December 31, 2012, the Company recognized a \$3,348,260 impairment provision against its book value of the Taliwang property.

**Sabalong Property (Sumbawa Island)**

The Sabalong property covers 9,950 hectares on Sumbawa Island. Southern Arc acquired the Sabalong property in 2007 and in 2010 entered into an option and joint venture agreement with Vale to advance the property. Southern Arc and Vale drilled three holes on the property commencing in October 2011, for a total of 1,811 metres, with Vale funding all exploration expenditures. As no significant assay results were returned, Vale elected not to proceed to Phase 2 exploration at Sabalong and relinquished all rights to the property. Subsequent to completion of Vale's Phase 1 work on the property, Southern Arc

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regained a 100% economic interest in the Sabalong property and between July and September 2012 completed a six-hole drill program totaling 1,035.6 metres to test epithermal gold vein targets in the Toyang prospect as defined by historical Newmont (1986–92), Rio Tinto Zinc (“RTZ”) (1993–98) and Company (2007–present) exploration work. While a number of the holes revealed mineralized intervals similar in scale and tenor to historical RTZ results, Southern Arc’s drilling failed to demonstrate any increase in grade or width with depth, and did not establish lateral extension of the mineralization.

In December 2012, the Company decided that it would not pursue any further exploration at the property and that it would relinquish all rights to the Sabalong property. As a result, the Company has written down the book value of the property to \$nil during the period ended December 31, 2012 and recorded an impairment charge of \$1,192,789.

**Nickel Oil & Gas Corp.**

At December 31, 2011, the Company concluded that the decline in the value of its equity investment in the private company Nickel Oil & Gas Corp. (“Nickel”), due to continued low natural gas prices, is other than temporary. Therefore it wrote down the remaining value of the investment to \$nil and recorded an impairment loss of \$305,582 during the period. As at March 31, 2013 and June 30, 2012, the Company holds 15.3 million Nickel shares (37.6%) with a carrying value of \$nil.

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

**SUMMARY OF QUARTERLY RESULTS**

	March 31, 2013	December 31, 2012	September 30, 2012	June 30, 2012
Total assets	\$ 53,939,440	\$ 54,333,738	\$ 60,321,920	\$ 60,884,512
Exploration properties	37,212,907	35,612,324	38,808,405	37,430,624
Working capital	15,164,760	17,208,413	19,027,865	21,035,112
Net loss	(527,628)	(5,172,518)	(757,053)	(1,184,372)
Basic and diluted loss per share	(0.00)	(0.05)	(0.01)	(0.01)

	March 31, 2012	December 31, 2011	September 30, 2011	June 30, 2011
Total assets	\$ 60,884,512	\$ 61,274,365	\$ 63,112,036	\$ 62,706,114
Exploration properties	37,430,624	29,634,073	26,345,975	22,796,908
Working capital	21,035,112	29,897,586	34,173,553	37,957,778
Net loss	(1,272,920)	(1,569,849)	(285,270)	(1,224,222)
Basic and diluted loss per share	(0.01)	(0.01)	(0.00)	(0.01)

**RESULTS OF OPERATIONS FOR THE THREE MONTHS ENDED MARCH 31, 2013**

During the three-month period ended March 31, 2013, the Company had a loss of \$527,628 compared to a loss of \$1,272,920 for the three-month period ended March 31, 2012. Significant fluctuations occurred in the following categories:

- a) Share-based compensation of \$65,707 (2012: \$282,135) decreased due to lower calculated cost for options granted during the period. Share-based compensation expense is accounted for at fair value as determined by the Black-Scholes Option Pricing Model using estimates that are believed to approximate the volatility of the trading price of the Company’s stock, the expected lives of awards of share-based compensation, the fair value of the Company’s stock and the risk-free interest rate.
- b) Foreign exchange gain of \$70,666 was realized during the three-month period ended March 31, 2013 (2012: \$81,154) primarily due to lower US\$ cash balances and the effect the fluctuation of the US\$/CDN\$ exchange

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rate had on the Canadian equivalent of the Company's holdings and transactions in its US\$ bank balance and US\$ payables balance.

- c) Management fees decreased to \$202,500 compared to \$278,140 in 2012 and are discussed in detail in the Related Parties section.
- d) Professional fees of \$66,696 (2012: \$213,042) decreased due to lower corporate activity in the period.
- e) Travel expenses of \$17,248 (2012: \$68,293) decreased as a result of reduced executive travel during the period.
- f) Interest income of \$38,548 (2012: \$70,693) decreased during the period as a result of lower cash balances.
- g) The Company invested \$1,507,932 cash (2012: \$3,541,092) on exploration properties and \$2,445 on property, plant and equipment (2012: \$9,488).

**RESULTS OF OPERATIONS FOR THE NINE MONTHS ENDED MARCH 31, 2013**

During the nine-month period ended March 31, 2013, the Company had a loss of \$6,457,199 compared to loss of \$3,128,038 for the nine-month period ended March 31, 2012. Significant fluctuations incurred in the following categories:

- a) Share-based compensation of \$294,060 (2012: \$837,053) decreased as a result of fewer share options granted during the period. Share-based compensation expense is accounted for at fair value as determined by the Black-Scholes Option Pricing Model using estimates that are believed to approximate the volatility of the trading price of the Company's stock, the expected lives of awards of share-based compensation, the fair value of the Company's stock and risk-free interest rate.
- b) Consulting fees of \$nil (2012: \$333,573) were paid as no consultants were engaged during the period.
- c) Foreign exchange gain of \$6,718 was lower during the period ended March 31, 2013 (2012: \$473,267 gain) primarily due to lower US\$ balances and reduced fluctuation of the US\$/CDN\$ exchange rate and the net effect on the CDN\$ equivalent of the Company's holdings and transactions in its US\$ bank balance and US\$ payables balance.
- d) Management fees decreased to \$622,000 from \$635,140 in 2012 and are discussed in detail in the Related Parties section.
- e) Office and miscellaneous expenses decreased to \$595,455 (2012: \$694,968) as a result of lower levels of corporate activities.
- f) Professional fees of \$236,203 (2012: \$434,670) decreased as a result of lower corporate legal activity during the period.
- g) Travel expenses of \$40,749 (2012: \$172,967) decreased as a result of reduced executive travel during the period.
- h) Interest income of \$135,782 (2012: \$217,710) decreased during period due to lower cash balances.
- i) The Company invested \$5,586,044 cash (2012: \$10,288,639) on exploration properties and \$2,445 on property, plant and equipment (2012: \$206,090).
- j) The Company wrote down the value of the Sabalong property to \$nil and recognized a \$1,192,789 impairment provision.
- k) The Company recognized a \$3,348,260 impairment provision against its book value of the Taliwang property.
- l) In 2013 the Company recorded an impairment loss of \$7,086 on equipment. Under other items in 2012, the Company recorded its share of the equity loss of Nickel of \$52,289 and recorded an impairment charge related to Nickel of \$305,582.

**LIQUIDITY AND CAPITAL RESOURCES**

The Company's cash position at March 31, 2013 was \$15,854,622, a decrease of \$6,586,945 from June 30, 2012. As at March 31, 2013, the Company's working capital was \$15,164,760 compared to a working capital of \$21,035,112 as at

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June 30, 2012. The decrease is primarily due to cash used for operating activities and exploration activities on the Indonesian properties. As at the date of this MD&A, the Company's working capital balance is approximately \$14.0 million.

Net cash used in operating activities for the nine-month period ended March 31, 2013 was \$1,000,077 compared to net cash used of 2,418,442 during the nine-month period ended March 31, 2012. The cash used in operating activities reflects the lower level of exploration and corporate activity and an increase in the accounts payable balance during the period.

Net cash used in investing activities during the nine-month period ended March 31, 2013 was \$5,588,489 compared to net cash used of \$10,596,429 during the nine-month period ended March 31, 2012. The cash used in investing activities for the period consists primarily of additions to exploration properties. In 2012, the Company received \$432,861 of exploration advances from Vale that offset expenditures on the Sabalong property.

There were no financing activities during the nine-month period ended March 31, 2013 (2012: \$2,501 expenditure).

**RELATED PARTY TRANSACTIONS**

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

	Three months ended March 31, 2013	Three months ended March 31, 2012	Nine months ended March 31, 2013	Nine months ended March 31, 2012
Management fees	\$ 270,750	\$ 512,105	\$ 924,314	\$ 736,261
Drilling services	\$ 620,293	\$ 627,836	\$ 986,038	\$ 2,881,592
Share-based compensation	\$ 42,424	\$ 30,208	\$ 249,478	\$ 533,848

During the period ended March 31, 2013, the Company paid \$622,000 (2012: \$635,140) for management fees to a private company controlled by the Chief Executive Officer and director of the Company. This fee is inclusive of administrative, finance, accounting, investor relations and management consulting fees, as well as certain office expenses. The above transactions occurred in the normal course of operations and are recorded at the consideration established and agreed to by the 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 period ended March 31, 2013, the Company paid a total of \$849,593 (US\$852,744) (2012: \$2,881,592 (US\$2,863,625)) for drilling services pursuant to the contract. A balance of \$136,445 (March 31, 2012: \$27,411) is included in accounts payable for drilling services incurred during the period ended March 31, 2013.

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

**CURRENT SHARE DATA**

As at the date of this MD&A, the Company has 109,214,510 common shares issued, of which 107,914,510 are outstanding and 1,300,000 are treasury shares.

The Company has the following share options outstanding:

	Number of Shares	Exercise Price	Expiry Date
<b>Options</b>	300,000	\$ 0.25	November 23, 2013
	100,000	\$ 0.40	November 23, 2013
	350,000	\$ 0.80	November 23, 2013
	3,050,000	\$ 0.40	September 16, 2014
	2,850,000	\$ 0.80	July 19, 2015

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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
935,000	\$	0.90	November 14, 2016
300,000	\$	0.25	July 18, 2017
<u>9,285,000</u>			

As at the date of this MD&A, the Company has no share purchase warrants outstanding.

**RISKS AND UNCERTAINTIES**

The nature of the Company's operations exposes the Company to credit risk, liquidity risk, market risk and geopolitical 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 counter-party'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/GST 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 in the accompanying Financial Statements.

**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 resource interests in Indonesia. The Company could accordingly be at risk for foreign currency fluctuations, devaluations 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 March 31, 2013, the Company had US\$2,122,339 (approximately CDN\$2,155,447) and Indonesian Rupiah ("Rph") 196,171,071 (approximately CDN\$20,598) in cash, and US\$724,797 (approximately CDN\$736,104) and Rph 88,394,871 (approximately CDN\$9,281) in accounts payable and accrued liabilities. As at March 31, 2013, US\$ amounts were converted at a rate of US\$0.98 to CDN\$1 and Rph amounts were converted at a rate of Rph 9,524 to CDN\$1.

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**Geopolitical Risk**

All of the Company's properties and operations are currently located in Indonesia. As such, the Company is subject to political, economic and other uncertainties, including, but not limited to, changes in policies and regulations or the personnel administering them, changes with regard to foreign ownership of property rights, exchange controls and royalty and tax increases, and other risks arising out of foreign governmental sovereignty over the areas in which the Company's operations are to be conducted, as well as risks of loss due to civil strife, acts of war and insurrections. If a dispute arises regarding the Company's property interests, the Company cannot rely on western legal standards in defending or advancing its interests.

**Fair value**

The fair value of the Company's financial instruments is approximated by their carrying value as at December 31, 2012 due to their short-term nature.

International Financial Reporting Standards ("IFRS") require 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 December 31, 2012 and June 30, 2012 are summarized in levels of fair value hierarchy as follows:

March 31, 2013	Level 1	Level 2	Level 3
Assets			
Cash	\$ 15,854,622	\$ -	\$ -

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June 30, 2012	Level 1	Level 2	Level 3
Assets			
Cash	\$ 22,441,567	\$ -	\$ -

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

**INDUSTRY**

The Company is engaged in the acquisition and exploration of resource properties, an inherently risky business, and there is no assurance that an economic mineral deposit will ever be discovered and subsequently put into production. Most exploration projects do not result in the discovery of economically mineable deposits. The focus of the Company is on areas in which the geological setting is well understood by management.

**GOLD AND METAL PRICES**

The price of gold is affected by numerous factors beyond the control of the Company including central bank sales, producer hedging activities, the relative exchange rate of the US\$ with other major currencies, demand, political and economic conditions and production levels. In addition, the price of gold has been volatile over short periods of time due to speculative activities. The prices of other metals and mineral products for which the Company may explore all have the same or similar price risk factors.

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**TRENDS**

Continued strength in gold and other commodity prices, increasing demand, especially from Asia, and perception of increased risk in major financial markets has supported a discernible need for the development of commodity exploration projects. Junior companies, like Southern Arc, are key participants in identifying properties of merit to explore and develop.

**SHAREHOLDER RIGHTS PLAN AND BONUS AND COMPENSATION PLAN**

The Company's Shareholder Rights Plan dated effective October 21, 2010 (the "Plan") is designed to ensure the fair treatment of shareholders in connection with any take-over bid for outstanding common shares of the Company. The Plan seeks to provide shareholders with adequate time to properly assess a take-over bid without undue pressure. It also provides the Board of Directors with adequate time to fully assess an unsolicited take-over bid, to allow competing bids to emerge, and, if applicable, to explore other alternatives to the take-over bid to maximize shareholder value.

The Plan is not intended to prevent or deter take-over bids that treat shareholders fairly. Under the Plan, those bids that meet certain requirements intended to protect the interests of all shareholders are deemed to be "Permitted Bids". Permitted Bids must be made by way of a take-over bid circular prepared in compliance with applicable securities laws and, among other conditions, must remain open for 60 days. In the event a take-over bid does not meet the Permitted Bid Requirements of the Plan, the rights will entitle shareholders, other than any shareholder or shareholders making the take-over bid, to purchase additional common shares of the Company at a substantial discount to the market price of the common share at that time. The Plan has an initial term of three years. The Plan is similar to plans adopted by other Canadian companies and ratified by their shareholders.

The Company's Bonus and Compensation Plan permits the Company to distribute or option up to 1.3 million common shares of the Company from time to time to eligible persons, including directors, officers, employees or consultants of Southern Arc.

**CRITICAL ACCOUNTING POLICIES**

Reference should be made to the Company's significant accounting policies contained in Note 2 of the Company's consolidated financial statements as at June 30, 2012 and 2011. These accounting policies can have a significant impact on the financial performance and financial position of the Company.

**Basis of presentation**

These condensed consolidated interim financial statements have been prepared in accordance with IFRS as issued by the International Accounting Standards Board ("IASB") applicable to the preparation of interim financial statements, including IAS 34, Interim Financial Reporting. The condensed consolidated interim financial statements should be read in conjunction with the annual consolidated financial statements for the year ended June 30, 2012, which have been prepared in accordance with IFRS as issued by the IASB.

The Company has used the same accounting policies and methods of computation as in the annual consolidated financial statements for the year ended June 30, 2012.

**Significant accounting judgement and estimates**

Preparation of the condensed consolidated interim 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.

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*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 deferred 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.
- 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.

**The acquisition of Indotan Lombok Pte. Ltd. and Indotan Sumbawa Pte. Ltd.**

In December 2009, the Company acquired control over two companies (Indotan Lombok Pte. Ltd. and Indotan Sumbawa Pte. Ltd.). As consideration, the Company issued 3,500,000 common shares with a value of \$2,415,000 (allocated to exploration properties) subject to two assignable options. The first option, which entitled the Company to acquire 500,000 of these shares 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 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 share-based compensation. The Company exercised the remaining 1,300,000 \$0.90 options and currently holds those shares.

As announced May 17, 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 in exchange for US\$1,500,000 and 2,250,000 Southern Arc shares valued at \$742,500.

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**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 are allocated to exploration properties.

**Exploration properties**

*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 a resource property is impaired, that property is written down to its estimated fair value. A resource 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 resource 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 resource properties involves certain inherent risks due to the difficulties of determining the validity of certain resource property interests as well as the potential for problems arising from the frequently ambiguous conveying history characteristics of many resource properties. The Company has investigated titles 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. The Company is in various stages of applying for permits for ongoing exploration activities related to the exploration properties.

*Joint interest*

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

The Company does not record any exploration expenditure 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 redesignates any costs previously capitalized in relation to the whole interest as relating to the partial interest retained. Exploration advances received from joint venture partner in accordance with the terms of the option and joint venture agreement are recorded as current liabilities until exploration expenditure is incurred.

*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 explorations sites. The

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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 environment 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.

**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.

**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.

**Income taxes**

Income tax expense comprises of current and deferred tax. Current tax and deferred tax are recognized in net income except to the extent that it relates 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

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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 utilized. 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.

**Investments**

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 would be 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 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*

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 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

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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, 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 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.

**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. These include:

- 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
- 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

**QUALIFIED PERSON AND QUALITY CONTROL AND ASSURANCE**

The technical information in this document has been reviewed by Southern Arc's Executive Vice President, Andrew Rowe, B. App. Sc. Geology, MAusIMM. Mr. Rowe has over 20 years of international mineral exploration experience throughout Southeast and Central Asia and Australia. During this time he has held such positions as Principal Geologist – Feasibility Studies, Senior Geologist and Consulting Geologist. The technical information in this document has also been reviewed by Southern Arc's President & Chief Operating Officer, Dr. Mike Andrews, PhD, FAusIMM, who has sufficient experience relevant to the style of mineralization under consideration and qualifies as a Qualified Person as defined by National Instrument 43-101.

The drill program and sampling protocol is managed by Southern Arc under the supervision of Andrew Rowe. The diamond drill holes are drilled at PQ, HQ and NQ sizes depending on hole depth and core recovery to date has averaged 98.0%. Half core is cut by rock saw and is generally sampled using nominal 1-metre intervals; however, sample intervals are varied according to geological contacts and have ranged between 0.2 to 2.5 metres in length. Three quality control samples (one blank and two standards) are inserted into each batch of 40 samples. The half core samples are securely transported from the project site to the Intertek Testing Services ("ITS") sample preparation laboratory in Sumbawa Besar via private truck hired by Southern Arc. Sample pulps are then sent to the ITS Jakarta laboratory by ITS. Gold is analysed by fire assay with AAS finish and a four-acid digestion with ICP-MS finish is used to analyse a full suite of elements including silver and base metals. ITS is one of the world's largest product and commodity testing, inspection and certification organizations. The Jakarta laboratory is ISO 17025 accredited and employs a Laboratory Information Management System for sample tracking, quality control and reporting.

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**CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS**

Certain of the statements made and information contained herein is "forward-looking information" within the meaning of the British Columbia Securities Act. These statements relate to future events or the Company's future performance. All statements, other than statements of historical fact, may be forward-looking statements. Generally, these forward-looking statements can be identified by the use of forward-looking terminology such as "anticipates", "plans", "budget", "scheduled", "continue", "estimates", "forecasts", "expect", "is expected", "project", "propose", "potential", "targeting", "intends", "believes" or variations of such words and phrases or statements that certain actions, events or results "may", "could", "would", "might", or "will be taken", "occur" or "be achieved" or the negative connotation thereof. These statements involve known and unknown risks, uncertainties and other factors that may cause actual results or events to differ materially from those anticipated in such forward-looking statements. The Company believes that the expectations reflected in those forward-looking statements are reasonable, but no assurance can be given that these expectations will prove to be correct and such forward-looking statements included in this MD&A should not be unduly relied upon by readers, as actual results may vary. These statements speak only as of the date of this MD&A and are expressly qualified, in their entirety, by this cautionary statement. In particular, this MD&A contains forward-looking statements, pertaining to the following: capital expenditure programs, development of resources, treatment under governmental and taxation regimes, expectations regarding the Company's ability to raise capital, expenditures to be made by the Company and its joint venture partners on its properties and work plans to be conducted. With respect to forward-looking statements listed above and contained in the MD&A, the Company has made assumptions regarding, among other things:

- uncertainties relating to receiving mining, exploration and other permits in Indonesia;
- the impact of increasing competition;
- unpredictable changes to the market prices for gold, copper and other commodities;
- exploration and developments costs for its properties in Indonesia;
- availability of additional financing and farm-in or joint-venture partners;
- anticipated results of exploration and development activities;
- the Company's ability to obtain additional financing on satisfactory terms.

The Company's actual results could differ materially from those anticipated in these forward-looking statements as a result of the risk factors set forth below and elsewhere in this MD&A: volatility in the market price for minerals; uncertainties associated with estimating resources; geological, technical, drilling and processing problems; liabilities and risks, including environmental liabilities and risks, inherent in mineral and oil and gas operations; fluctuations in currencies and interest rates; incorrect assessments of the value of acquisitions; unanticipated results of exploration activities; competition for, amongst other things, capital, undeveloped lands and skilled personnel; lack of availability of additional financing and farm-in or joint venture partners and unpredictable weather conditions. Although the Company has attempted to identify important factors that could cause results to differ materially from those contained in forward-looking statements, there may be other factors that cause results not to be as anticipated, estimated or intended. There can be no assurance that such statements will prove to be accurate, as actual results and future events could differ materially from those anticipated in such statements. Accordingly, readers should not place undue reliance on forward-looking statements. Readers are cautioned that the foregoing lists of factors are not exhaustive. Forward looking statements are made as of the date hereof and accordingly are subject to change after such date. The forward-looking statements contained in this MD&A are expressly qualified by this cautionary statement. The Company does not undertake to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise, except in accordance with applicable securities laws.

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**APPENDIX 1**

**Mencanggih Prospect, Bising Target, Phase 2 Drill Hole Statistics Summary**

Drill Hole	Target	Depth (m)	Coordinates		Az	Dip	From (m)	To (m)	Interval (m)	Gold (g/t)	Silver (g/t)
			E	N							
MCG038	Bising	101.8	388569.6	9023770.5	195	-50	27.67 89.75	58.4 91.5	30.73 1.75	0.30 1.02	1.4 0.6
MCG039	Bising	81.1	388619.8	9023743.3	195	-50	20.30	51.2	30.9	0.35	1.4
MCG040 Including	Bising	165.2	388271	9023963.9	195	-70	100.80 125.65	147.9 147.9	47.10 22.25	0.37 0.48	1.2 1.8
MCG041 Including Including Including Including	Bising	100.6	388198.51	9023870.2	195	-50	20.0 22.0 22.0 22.0 35.9	86.8 79.8 64.8 44.9 39.85	66.8 57.8 42.8 22.9 3.95	0.66 0.72 0.81 1.16 2.89	2.4 2.5 2.6 2.7 2.3
MCG042 Including Including and and	Bising	112.1	388243.64	9023869.7	195	-50	16.0 26.3 32.2 46.3 66.2	69.2 47.8 33.2 46.6 66.4	53.2 21.5 1.0 0.3 0.2	1.04 1.6 9.67 10.2 10.3	1.4 1.6 0.8 61.3 25.5
MCG043 Including	Bising	105.1	388280.57	9023858.3	195	-45	20.7 39.0	63.1 49.1	42.4 10.1	0.51 1.0	1.1 1.9
MCG044 Including Including and	Bising	172.6	388271	9023963.9	195	-50	87.85 104.6 104.6 123.0	146.0 146.0 115.6 130.5	58.15 41.4 11.0 7.5	0.61 0.73 1.3 1.1	2.5 3.3 1.1 11.0
MCG045	Bising	91.8	388104.3	9023882	195	-50	20.45	64.35	43.9	0.35	2.3
MCG046 Including	Bising	145.3	388178.3	9023954.5	195	-45	91.3 106.3	120.1 115.8	28.8 9.5	0.40 0.62	2.1 2.8
MCG047	Bising	133.1	388128.3	9023962.3	195	-50	77.45	110.8	31.25	0.35	2.3
MCG048 Including	Bising	166.9	388178.3	9023954.5	195	-70	100.6 109.5	125.4 125.4	24.8 15.9	0.55 0.65	2.3 2.9
MCG056 Including	Bising	171.0	388360.3	9023928.8	195	-60	97.50 105.00	138.90 118.70	41.40 13.70	0.69 0.94	1.4 0.9
MCG057 Including	Bising	74.0	388446.9	9023773.8	195	-60	7.55 28.40	60.25 55.55	52.70 27.15	0.68 1.00	2.3 3.4
MCG059 Including	Bising	178.0	388481.9	9023900.5	195	-50	94.85 111.65	129.00 129.00	34.15 17.35	0.52 0.78	1.1 1.7

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**APPENDIX 2**

**Mencangah Prospect, Tibu Serai Target, Phase 1 Drill Hole Statistics Summary**

Drill Hole	Target	Depth (m)	Coordinates		Az	Dip	From (m)	To (m)	Interval (m)	Gold (g/t)	Silver (g/t)
			E	N							
MCG049 Including and	Tibu Serai	144.0	387975.7	9024921.1	238	-50	31.3 34.65 78.7	43.4 38.85 82	12.1 4.2 3.3	1.07 2.17 1.21	1.2 1.7 1.2
MCG050 Including Including	Tibu Serai	156.0	387821.29	9024822.7	238	-50	100.23 108.85 110.5	111 111 111	10.77 2.15 0.5	1.01 3.87 15.0	4.0 17.0 67.4
MCG051 Including	Tibu Serai	178.4	387765.9	9025245.9	238	-50	114.7 119.9 136.45	123.4 123.4 145.3	8.7 3.5 8.85	1.56 3.33 0.74	0.71 1.0 0.4
MCG052	Tibu Serai	215.8	387704.6	9025293.3	238	-50	101.72	103.05	1.33	0.66	0.3
MCG053	Tibu Serai	146.5	387637.2	9025190.4	238	-50	31.4	41	9.6	0.35	0.3
MCG054 Including	Tibu Serai	185.9	388359.9	9025311.2	238	-50	139.1 156.6	159.2 157.7	20.1 1.1	0.56 3.11	1.4 10.9
MCG055 Including and Including	Tibu Serai	97.6	388778.8	9024790.9	238	-50	48.6 49.4 67.2 71.75	73.4 49.9 72.6 72.3	24.8 0.5 5.4 0.55	4.27 71.0 9.44 71.0	0.6 1.9 1.3 6.8
MCG058 Including Including	Tibu Serai	100.6	388755.90	9024823.56	230	-55	3.20 58.80 70.60 76.40	3.90 77.50 77.50 77.50	0.70 18.70 6.90 1.10	13.50 2.46 5.65 31.97	2.3 0.4 0.5 1.9
MCG060 Including	Tibu Serai	100.6	388813.80	9024770.78	230	-55	60.30 76.70	82.80 81.80	22.50 5.10	1.60 5.29	1.5 5.3
MCG061 Including Including and	Tibu Serai	150.3	388810.25	9024810.30	233	-65	96.50 114.80 117.60 122.00	122.80 122.80 118.50 122.80	26.30 8.00 0.90 0.80	1.22 3.21 11.20 13.80	0.2 0.3 0.2 0.7
MCG062 Including	Tibu Serai	180.4	388876.52	9024782.71	230	-55	21.65 23.90 106.20 128.80 147.20	25.60 24.70 106.50 129.70 147.80	3.95 0.80 0.30 0.90 0.60	3.55 11.70 1.44 1.02 3.30	0.2 0.2 0.7 0.2 1.2
MCG063 Including	Tibu Serai	163.5	388755.29	9024881.12	230	-55	104.90 112.70	115.90 115.90	11.00 3.20	1.02 1.93	0.3 0.3
MCG064	Tibu Serai	168.6	388730.10	9024912.87	230	-55	25.50 141.10	26.90 142.30	1.40 1.20	1.66 1.36	0.9 0.2
MCG065 Including	Tibu Serai	173.1	388902.00	9024752.00	230	-55	21.10 151.10 152.20	24.80 154.90 152.70	3.70 3.80 0.50	1.07 1.18 4.83	0.2 0.3 0.2
MCG066	Tibu Serai	118.6					No Significant Result				

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MCG067	Tibu Serai	117.3	388845.00	9024704.00	230	-55	70.60	75.10	4.50	7.79	0.7
Including							70.60	71.20	0.60	16.60	1.6
and							73.40	74.45	1.05	20.94	1.0

**APPENDIX 3**

**Mencangah Prospect, Porphyry Exploration, Drill Hole Statistics Summary**

Drill Hole	Target	Depth (m)	Coordinates		Az	Dip	From (m)	To (m)	Interval (m)	Gold (g/t)	Silver (g/t)	Copper (%)
			E	N								
MCD001	Tibu Serai	571.50	388778.8	9024790.9	37.5	-60	No significant result					
MCD002	North Bising	626.20	388439.1	9024401.5	263.65	-60	No significant result					