



Consolidated Interim Financial Statements of  
**MKANGO RESOURCES LTD.**

For the three months ended March 31, 2014 and 2013

**Unaudited interim financial statements**

**In accordance with National Instrument 51-102 released by the Canadian Securities administrators, the Company discloses that its auditors have not reviewed these interim financial statements for the three months ended March 31, 2014 and 2013.**

**MKANGO RESOURCES LTD.**  
**Consolidated Interim Statements of Financial Position**  
**Reported in US dollars**

As at:	Notes	March 31, 2014	December 31, 2013
<b>ASSETS</b>			
Current			
Cash and cash equivalents		<b>\$1,433,497</b>	\$437,378
Restricted cash	5	<b>3,171</b>	2,941
Accounts receivable		<b>4,375</b>	3,475
Prepaid expenses and deposits		<b>6,512</b>	58,242
Total currents assets		<b>1,447,555</b>	502,036
Property and equipment	6	<b>4,740</b>	5,051
Total assets		<b>1,452,295</b>	507,087
<b>LIABILITIES</b>			
Current			
Accounts payable and accrued liabilities		<b>207,486</b>	185,112
Due to related party	7	<b>7,690</b>	6,540
Warrants - derivative financial instruments	8(b)	<b>18,115</b>	18,115
Total current liabilities		<b>233,291</b>	209,767
Long term			
Warrants - derivative financial instruments	8(b)	<b>1,364,923</b>	-
Total liabilities		<b>1,598,214</b>	209,767
<b>EQUITY</b>			
Share capital	8(a)	<b>7,224,823</b>	7,370,698
Subscription receivable		<b>4,872</b>	-
Contributed surplus		<b>2,212,572</b>	2,080,195
Deficit		<b>(9,588,186)</b>	(9,153,573)
Total equity		<b>(145,919)</b>	297,320
Total liabilities and equity		<b>\$1,452,295</b>	\$507,087
Going concern	2		
Commitments	10		
Subsequent events	12		

Approved on behalf of the Board:

(signed) "*William Dawes*"

William Dawes, CEO and Director

(signed) "*David Berg*"

David Berg, Director

Refer to accompanying notes to the consolidated interim financial statements.

# MKANGO RESOURCES LTD.

## Consolidated Interim Statements of Comprehensive Loss Reported in US dollars

		For the three months ended	
		March 31,	
	Notes	2014	2013
<b>Expenses</b>			
General and administrative		\$ 243,991	\$ 318,503
Mineral exploration expenditures		153,583	86,839
Depreciation	6	311	615
Share based payments	8(c)	73,009	9,332
		<b>470,895</b>	<b>415,289</b>
<b>Other items</b>			
Unrealized (gain) loss on revaluation of warrants	8(b)	(805)	(5,918)
Unrealized foreign exchange (gain) loss		-	9,544
Realized foreign exchange (gain) loss		(35,476)	(339)
<b>Net loss and comprehensive loss</b>		<b>\$ (434,613)</b>	<b>\$ (418,576)</b>
<b>Net loss per share - basic and diluted</b>			
		<b>\$ (0.01)</b>	<b>\$ (0.01)</b>
<b>Weighted average shares outstanding basic and diluted</b>			
		<b>51,829,472</b>	<b>38,871,426</b>

Refer to accompanying notes to the consolidated interim financial statements.

**MKANGO RESOURCES LTD.**  
**Consolidated Interim Statements of Cash Flows**  
**Reported in US dollars**

	Notes	For the three months ended	
		March 31,	
		2014	2013
<b>Cash flow from operating activities</b>			
Net loss and comprehensive loss for the year		<b>\$(434,613)</b>	\$(418,576)
Items not affecting cash:			
Share based payments	8(c)	<b>73,009</b>	9,332
Gain on revaluation of warrants	8(b)	<b>(805)</b>	(5,918)
Depreciation	6	<b>311</b>	615
Unrealized foreign exchange (gain) loss		-	9,205
Change in non-cash operating capital			
Accounts receivable, prepaid expenses and deposit		<b>50,830</b>	(11,560)
Accounts payable, accrued liabilities and due to related party		<b>23,523</b>	122,342
Cash used by operating activities		<b>(287,744)</b>	(294,560)
<b>Cash flow from financing activities</b>			
Issue of share capital, net of issue costs		<b>1,277,031</b>	685,714
Subscriptions received		<b>4,872</b>	221,951
		<b>1,281,904</b>	907,665
Effect of exchange rate changes on cash		<b>(1,212)</b>	(661)
<b>Change in cash and cash equivalents</b>		<b>992,948</b>	612,444
Cash and cash equivalents at the beginning of the period		<b>437,378</b>	320,766
Cash reclassified to restricted cash		<b>3,171</b>	4,018
<b>Cash and cash equivalents at the end of the period</b>		<b>\$1,433,497</b>	\$937,228

Refer to accompanying notes to the consolidated interim financial statements.

**MKANGO RESOURCES LTD.**  
**Consolidated Interim Statements of Changes in Equity**  
**Reported in US dollars**

	Share capital	Subscriptions received	Contributed Surplus	Deficit	Total
Balance at December 31, 2012	\$ 5,632,076	\$ -	\$ 1,928,324	\$ (7,255,680)	\$ 304,720
Common shares issued	730,000				730,000
Subscriptions received		221,951			221,951
Share issue costs	(44,286)				(44,286)
Warrant valuation	(123,732)				(123,732)
Share based payments			9,332		9,332
Net loss and comprehensive loss				(418,576)	(418,576)
Balance at March 31, 2013	\$ 6,194,058	\$ 221,951	\$ 1,937,656	\$ (7,674,256)	\$ 679,409
Common shares issued	1,522,209				1,522,209
Subscriptions received		(221,951)			(221,951)
Share issue costs	(132,468)		39,195		(93,273)
Warrant valuation	(213,101)				(213,101)
Share based payments			103,344		103,344
Net loss and comprehensive loss				(1,479,317)	(1,479,317)
Balance at December 31, 2013	\$ 7,370,698	\$ -	\$ 2,080,195	\$ (9,153,573)	\$ 297,320
Common shares issued	1,464,933				1,464,933
Subscriptions received		4,872			4,872
Share issue costs	(185,717)				(185,717)
Warrant valuation	(1,425,091)		59,363		(1,365,728)
Share based payments			73,014		73,014
Net loss and comprehensive loss				(434,613)	(434,613)
Balance at March 31, 2014	\$ 7,224,823	\$ 4,872	\$ 2,212,572	\$ (9,588,186)	\$ (145,919)

Refer to accompanying notes to the consolidated interim financial statements.

# **MKANGO RESOURCES LTD.**

Notes to the Consolidated Interim Financial Statements

For the three months ended March 31, 2014 and 2013

(Reported in US dollars unless indicated otherwise)

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## **1. GENERAL INFORMATION**

The principal business of Mkango Resources Ltd (the “Company” or “Mkango”) is rare earth element and associated minerals exploration and development with a portfolio of properties in the Republic of Malawi, Africa, including the Phalombe exploration license (“Phalombe License”) and the Thambani exploration license (“Thambani License”).

Mkango was originally incorporated under the name Alloy Capital Corp. (“Alloy”) on November 13, 2007, under the laws of the Province of Alberta, Canada. On December 20, 2010, Alloy was acquired through a “reverse takeover” by Lancaster Exploration (“Lancaster”). The articles of the Company were amended to change the name of the Company from Alloy Capital Corp. to Mkango Resources Ltd. Mkango’s head office is located at 259 Windermere Road SW, Calgary, Alberta Canada, T3C 3L2.

Lancaster was incorporated August 3, 2007 by Memorandum and Articles of Association issued pursuant to the provisions of the BVI Companies Act. Lancaster’s registered office is located at 56 Administration Drive, Wickhams Cay 1, Road Town, Tortola, British Virgin Islands.

On May 19, 2011, Lancaster Exploration Limited was incorporated under the laws of Blantyre, Malawi. Lancaster Exploration Limited is a wholly owned subsidiary of Lancaster.

The consolidated interim financial statements were authorized for issuance by the Board of Directors of the Company on May 30, 2014.

## **2. GOING CONCERN**

These consolidated interim financial statements have been prepared on a going concern basis, which contemplates the realization of assets and the payment of liabilities in the ordinary course of business. The Company incurred a net loss of \$434,613 for the three months ended March 31, 2014 (2013 - \$418,576) and has a deficit of \$9,588,186 (Dec 31, 2013 - \$9,153,573). The Company is in the process of acquiring, exploring and developing its mineral interests.

The operations of the Company for the next 12 months will be funded by a non-brokered private placement (“Financing”), which closed in two tranches on March 24, 2014 and April 3, 2014 (Note 8 and Note 12).

Should the Company be unable to continue as a going concern, it may be unable to realize the carrying value of its assets and to meet its liabilities as they become due. These consolidated financial statements do not reflect the adjustments or reclassification of assets and liabilities, which would be necessary if the Company were unable to continue its operations.

## **3. BASIS OF PRESENTATION**

### **(a) Statement of compliance**

These consolidated interim financial statements have been prepared in accordance with International Financial Reporting Standards (“IFRS”) as issued by the International Accounting Standards Board (“IASB”) and interpretations issued by the International Financial Reporting Interpretations Committee (“IFRIC”), in effect on March 31, 2014.

### **(b) Basis of presentation and measurement**

These consolidated interim financial statements have been prepared using the historical cost convention, except for certain financial instruments measured at fair value through profit and loss (“FVTPL”) and share-based payment transactions measured at fair value.

### **(c) Functional and presentation currency**

The consolidated interim financial statements are presented in US dollars, which is the functional currency of the Company and its subsidiaries.

### **(d) Principles of consolidation**

The consolidated interim financial statements of the Company include the accounts of the Company and its wholly owned subsidiaries. All intercompany balances and transactions are eliminated upon consolidation.

## **MKANGO RESOURCES LTD.**

Notes to the Consolidated Interim Financial Statements

For the three months ended March 31, 2014 and 2013

(Reported in US dollars unless indicated otherwise)

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### **3. BASIS OF PRESENTATION (continued)**

#### **(e) Use of estimates and judgments**

The preparation of the consolidated interim financial statements in conformity with IFRS requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimates are revised and in any future periods affected.

Key areas of judgement made in applying the Company's accounting policies are as follows:

#### **(i) Exploration and evaluation expenditures**

Costs incurred in respect of properties that have been determined to have proved reserves and for which an environmental impact study has been completed, are classified as development and production assets. In such circumstances, technical feasibility and commercial viability are considered to be established. Costs incurred in respect of new prospects with no established development past or present and no proved or probable reserves assigned are classified as exploration and evaluation expenses and are recognized in the statement of comprehensive loss. The decision to transfer assets from exploration and evaluation to property and equipment is subject to management's judgement regarding the project's commercial viability and technical feasibility. As at March 31, 2014, management has determined that the Company has not yet reached the development and production stage.

#### **(ii) Functional currency**

The functional currency of the Company and its subsidiaries is the currency of the primary economic environment in which each entity operates. The Company has determined the functional currency of each consolidated entity as the US dollar. Determination of functional currency may involve certain judgments to determine the primary economic environment and the Company reconsiders the functional currency of each entity if there is a change in events and conditions, which determine the primary economic environment.

Key areas of estimation where management has made difficult, complex or subjective assumptions, often as a result of matters inherently uncertain are as follows:

#### **(i) Measurement of share based payments and warrant valuation (Note 8(c))**

The Company uses an option-pricing model to determine the fair value of share-based payments and warrants. Inputs to the model are subject to various estimates about volatility, interest rates, dividend yields, forfeiture rates and expected life of the equity instruments issued. Fair value inputs are subject to market factors as well as internal estimates. The Company considers historic trends together with any new information to determine the best estimate of fair value at the date of grant.

#### **(ii) Determination of fair values (Note 9)**

The estimated fair value of financial assets and liabilities, by their very nature, are subject to measurement uncertainty.

## MKANGO RESOURCES LTD.

Notes to the Consolidated Interim Financial Statements

For the three months ended March 31, 2014 and 2013

(Reported in US dollars unless indicated otherwise)

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### 3. BASIS OF PRESENTATION (continued)

#### (f) New IFRS pronouncements not yet implemented

The following IFRS pronouncements have been issued by the IASB as at March 31, 2014 but are not yet effective. The Company does not plan to early adopt any of these new or amended standards and interpretations and is currently assessing the impact of these new or amended standards and interpretations. Certain other new standards and interpretations have been issued but are not shown as they are not expected to have a material impact on the Company's financial statements.

IFRS 2, "Share-based Payment". The amendments to IFRS 2, issued in December 2013, were made to the definitions of "vesting conditions" and "market conditions" and the definitions of "performance condition" and "service condition" were added. A performance condition requires the counterparty to complete a specified period of service and to meet a specified performance target during the service period. A service condition solely requires the counterparty to complete a specified period of service. The amendments are to be prospectively applied to share-based payment transactions for which the grant date is on or after July 1, 2014.

IFRS 3, "Business combinations". The amendments to IFRS 3, issued in December 2013, clarify the accounting for contingent consideration in a business combination. At each reporting period, an entity measures contingent consideration classified as an asset or a financial liability at fair value, with changes in fair value recognized in profit or loss. The amendments are effective for business combinations for which the acquisition date is on or after July 1, 2014.

IFRS 9, "Financial instruments". In November 2013, IFRS 9 was amended with significant changes to hedge accounting. In addition, an entity can now apply the "own credit requirement" in isolation without the need to change any other accounting for financial instruments. The standard is effective for annual periods beginning on or after January 1, 2018.

IAS 24, "Related party disclosures". The amendments to IAS 24, issued in December 2013, clarify that a management entity, or any member of a group of which it is a part, that provides key management services to a reporting entity, or its parent, is a related party of the reporting entity. The amendments also require an entity to disclose amounts incurred for key management personnel services provided by a separate management entity. This replaces the more detailed disclosure by category required for other key management personnel compensation. The amendments will only affect disclosure and are effective for annual periods beginning on or after July 1, 2014.

### 4. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

These consolidated interim financial statements should be read in conjunction with the annual consolidated financial statements for the year ended December 31, 2013. Details outlining the Company's accounting policies are contained in the notes to the financial statements for the year ended December 31, 2013.

### 5. RESTRICTED CASH

The Malawi Revenue Authority, customs and excise division ("MRA"), required a 1,300,000 MWK bank guarantee from the Company in order to allow drilling equipment to be imported into the country for its Stage 2 drilling program which was equivalent to \$3,171 as at March 31, 2014 (2013 - \$2,941)

### 6. PROPERTY AND EQUIPMENT

	Cost	Accumulated Depreciation	Net Book Value
Balance at December 31, 2012	10,020	(3,707)	6,313
Less Depreciation	-	(615)	(615)
Balance at March 31, 2013	10,020	(4,322)	5,698
Less Depreciation	-	(647)	(647)
Balance at December 31, 2013	\$10,020	\$(4,969)	\$5,051
Less Depreciation	-	(311)	(311)
Balance at March 31, 2014	\$10,020	\$(5,280)	\$4,740



## MKANGO RESOURCES LTD.

Notes to the Consolidated Interim Financial Statements

For the three months ended March 31, 2014 and 2013

(Reported in US dollars unless indicated otherwise)

### 7. RELATED PARTY TRANSACTIONS

- a) As of March 31, 2014 the Company had an outstanding payable to Leo Mining and Exploration Ltd. (“Leo Mining”) in the amount of \$6,294 (2013 – nil). The amount is unsecured and due on demand. Interest of 2% may be incurred on the outstanding amount annually; however this has been waived. Leo Mining is considered related by virtue of common directors and officers who have an ownership in and exercise significant influence over both companies. The Company and Leo Mining have formalized their relationship with respect to services provided by Leo Mining. A written agreement sets out the types of services, which may be provided and the costs associated with such services. Generally the Company repays the disbursements made by Leo Mining on its behalf.
- b) Digby Wells Environmental (“Digby”), by virtue of a common director, is considered a related party. During the three months ended March 31, 2014, the Company had paid Digby \$12,370 (2012 – nil) for environmental services. As of March 31, 2014, there was an outstanding payable to Digby for \$5,248 (2013 – nil).
- c) A partner of Stikeman Elliott (London) LLP (“Stikeman”) is a director of the Company and Stikeman is, therefore, considered a related party. During the three months ended March 31, 2014, the Company accrued \$91,628 (2012 – nil) for legal services. These amounts remain unpaid as of March 31, 2014 (2013 – nil).
- d) The Company paid \$89,678 (2012 - \$75,000) for key management fees and related costs for the three months ended March 31, 2014. Included in accounts payable and accrued liabilities at March 31, 2014, was \$6,705 (2012 - \$32,289) due to directors and officers. The amounts owed are unsecured, due on demand and non-interest bearing.

### 8. SHARE CAPITAL

#### a) Common Shares

The Company is authorized to issue an unlimited number of common and preferred shares without nominal or par value. The Company has not issued any preferred shares to date. The holders of common shares are entitled to one vote for each share on all matters submitted to a shareholder vote and are entitled to share in all dividends that the Company’s board of directors, in its discretion, declares from available funds.

	Ref	Number	Amount
Closing balance December 31, 2011 and 2012		37,442,855	\$5,632,076
Non-brokered offering	(i)	4,285,715	730,000
Share issue costs cash	(iii)	-	(123,732)
Warrants valuation - March 1, 2013	(i)	-	(99,771)
Closing balance March 31, 2013		41,728,570	\$6,138,573
Brokered offering	(ii)	8,836,033	1,522,209
Share issue costs cash	(iii)	-	(13,827)
Share issue costs – agent warrants	(ii)	-	(39,195)
Warrants valuation - April 11, 2013	(ii)	-	(237,062)
Closing balance December 31, 2013		50,564,603	\$7,370,698
Brokered offering	(iv)	16,262,603	1,462,748
Shares issued - agent shares	(iv)	24,500	2,184
Share issue costs cash	(v)	-	(185,717)
Share issue costs - agent warrants	(iv)	-	(59,363)
Warrants valuation - March 24, 2014	(iv)	-	(1,365,728)
Shares certificate to be cancelled		142,857	-
Closing balance March 31, 2014		66,994,563	\$7,224,823

## MKANGO RESOURCES LTD.

Notes to the Consolidated Interim Financial Statements

For the three months ended March 31, 2014 and 2013

(Reported in US dollars unless indicated otherwise)

### 8. SHARE CAPITAL (continued)

- (i) On March 1, 2013, the Company issued 4,285,715 units at C\$0.175 per unit pursuant to the non-brokered offering to Leo Mining, a related party. The C\$750,000 (US\$730,000) gross proceeds of the non-brokered offering were allocated between common shares C\$647,518 (US\$630,229) and warrants C\$102,482 (US \$99,771) based on the fair value of the warrants using the Black-Scholes option pricing model. Each unit consists of one common share and one-half of a common share purchase warrant of Mkango. Each whole warrant entitles the holder to acquire one common share for C\$0.35 for a period of 12 months following the closing date of the financing. Leo Mining is the Company's majority shareholder and is considered a related party by virtue of common directors and officers who have an ownership in and exercise significant influence over the Company.
- (ii) On April 11, 2013, the Company issued 8,836,033 units at C\$0.175 per unit pursuant to the non-brokered offering. The C\$1,545,544 (US \$1,522,209) gross proceeds of the non-brokered offering were allocated between common shares C\$1,304,848 (US \$1,285,147) and warrants C\$240,696 (US \$237,062) based on the fair value of the warrants using the Black-Scholes option pricing model. Each unit consists of one common share and one-half of a common share purchase warrant of Mkango. Agents received 431,266 agents warrants valued at US\$39,195. Each whole warrant entitles the holder to acquire one common share for C\$0.35 for a period of 12 months following the closing date of the financing.
- (iii) Share issue costs of US \$137,559 were paid for agent and legal services and regulatory exchange filing fees.
- (iv) On March 24, 2014, the Company issued 16,262,603 units at C\$0.10 per unit pursuant to the non-brokered offering. The C\$1,626,260 (US \$1,462,748) gross proceeds of the non-brokered offering were allocated between common shares C\$94,323 (US\$97,026) and warrants C\$1,531,937 (US\$1,365,728) based on the fair value of the warrants using the Black-Scholes option pricing model. Each Unit consists of one common share and one common share purchase warrant of Mkango. Each Warrant entitles the holder to acquire one Common Share for C\$0.20 until March 24, 2019. The Corporation issued 24,500 Units and 880,782 agents warrants valued at US\$59,363. Each whole warrant entitles the holder to acquire one common share for C\$0.10 until March 24, 2016. The securities issued, have a hold period of four months and one day from the date of issue.
- (v) Share issue costs of US \$185,717 were paid for agent and legal services and regulatory exchange filing fees.

#### b) Derivative financial instruments

The exercise price of the share purchase warrants is fixed in Canadian dollars and the functional currency of the Company is the US dollar. Warrants are considered a derivative, as a variable amount of cash in the Company's functional currency will be received on exercise. Warrants issued do not include warrants issued to brokers and agents since they fall into the scope of IFRS 2.

	Exercise Price (CDN\$)	Weighted Average Years Remaining	Number of Warrants	Amount
Balance at December 31, 2012			-	-
Warrants issued – March 1, 2013 - expired	0.35	-	-	-
Warrants issued – April 11, 2013	0.35	0.03	4,418,016	18,115
Warrants issued – March 24, 2014	0.20	4.97	16,262,603	1,365,728
Fair value change at year end	-	-	-	(805)
Balance at March 31, 2014	\$ 0.23	3.91	20,680,619	\$ 1,383,038

## MKANGO RESOURCES LTD.

Notes to the Consolidated Interim Financial Statements

For the three months ended March 31, 2014 and 2013

(Reported in US dollars unless indicated otherwise)

### 8. SHARE CAPITAL (continued)

The fair value of each warrant issued is determined at each reporting period using the Black-Scholes pricing model. The following assumptions were used in arriving at the fair value estimate for the warrants:

	April 11, 2013 (Second Tranche)	March 24, 2014	March 31, 2014 (Second Tranche)	March 31, 2014
Risk free interest rate	0.95%	1.69%	0.91%	1.69%
Expected volatility	142%	142%	188%	142%
Share price	\$0.16	\$0.11	\$0.11	\$0.11
Foreign exchange rate	1.0101	1.1217	1.1053	1.1053
Remaining life	1.0	5.0	0.03	4.97

#### c) Share-based payments

The Company has a rolling stock option plan (the "Plan") established to recognize contributions made by key personnel, to provide incentive to qualified parties to increase their proprietary interest in the Company and thereby encourage their continued association with the Company. The number of options granted under the Plan is limited to 10% in the aggregate of the number of issued and outstanding common shares of the Company at the date of the grant of the options.

The share-based payments expense that has been recognized in the consolidated interim statement of comprehensive loss for the three months ended March 31, 2014 and 2013 is \$73,009 and \$9,332 respectively. The corresponding amount has been recognized in contributed surplus. The options vest over a term of 24 months.

The following table provides a summary of the status of the Company's stock option plan and changes during the years ended:

	Options Outstanding	Weighted Average Exercise Price (CDN\$)	Options Exercisable	Weighted Average Remaining Contractual Life (years)
Balance at December 31, 2011	2,742,500	\$ 0.50	1,457,708	6.9
Granted - December 11, 2012	200,000	0.50	200,000	1.6
Balance at December 31, 2012	2,942,500	0.50	2,742,500	6.5
Granted - September 25, 2013	1,980,000	0.20	495,000	9.5
Balance at December 31, 2013	4,922,500	\$ 0.39	3,437,500	7.7

The fair value of each option granted is estimated as of the grant date using the Black-Scholes option-pricing model. The following assumptions were used in arriving at the fair value for the options:

	September 25, 2013	December 11, 2012
Risk free interest rate	2.57%	1.13%
Expected life	10 years	3 years
Expected volatility	128%	118%
Dividends	Nil	Nil
Forfeiture rate	5%	5%
Fair value at issuance	\$0.17	\$0.44

## **MKANGO RESOURCES LTD.**

Notes to the Consolidated Interim Financial Statements

For the three months ended March 31, 2014 and 2013

(Reported in US dollars unless indicated otherwise)

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### **9. FINANCIAL INSTRUMENTS**

#### **Determination of fair values**

Financial assets and liabilities have been classified into categories that determine their basis of measurement and for items measured at fair value, whether changes in fair value are recognized in the statement of comprehensive loss. Those categories are fair value through profit or loss; loans and receivables; and, for most liabilities, amortized cost.

In establishing fair value, the Company used a fair value hierarchy based on levels defined below:

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

Cash and cash equivalents and restricted cash are measured at level 1; warrant derivative liability is measured at level 2.

The carrying value of accounts receivable, accounts payable and accrued liabilities and due to related party approximates the fair value due to their short-term nature and maturity. Warrants with an exercise price in a currency other than the functional currency are to be recorded as a derivative liability and carried at fair value, see Note 8(b).

#### **Financial risk management**

The Company's management monitors and manages the financial risks relating to the operations of the Company. These include foreign currency, interest rate, liquidity and credit risks.

#### **Foreign currency rate risk**

The functional and reporting currency of the Company is the United States dollar. The Company enters into transactions denominated in the Canadian Dollar, the United States dollar, and the local currency in Malawi (Kwacha). The Company raises its equity in the Canadian dollar and then purchases United States dollar and Malawi Kwacha funds to settle liabilities, as required. As at March 31, 2014 and 2013, the following balances were held by the Company:

	As at March 31,	
	2014	2013
Canadian dollar	\$ 1,420,548	\$ 82,521
United States dollar	8,000	849,829
Malawi Kwacha	8,120	4,878
	<u>\$ 1,436,668</u>	<u>\$ 937,228</u>

A 5% change in the value of the Canadian dollar in comparison to the United States dollar would cause a change in net loss of approximately \$72,000. A 5% change in the value of the Malawi Kwacha in relationship to the United States dollar would not cause a material change in net loss.

#### **Interest rate risk**

The Company's exposure to interest rate risk relates primarily to its cash and cash equivalents at banks. However, the interest rate risk is expected to be minimal. The Company does not presently hedge against interest rate movements.

#### **Liquidity risk**

Liquidity risk includes the risk that, as a result of the Company's operational liquidity requirements:

- a) The Company will not have sufficient funds to settle a transaction on the due date;
- b) The Company will be forced to sell financial assets at a value which is less than the fair value; or

## MKANGO RESOURCES LTD.

Notes to the Consolidated Interim Financial Statements

For the three months ended March 31, 2014 and 2013

(Reported in US dollars unless indicated otherwise)

### 9. FINANCIAL INSTRUMENTS (continued)

- c) The Company may be unable to settle or recover a financial asset at all. The Company's operating cash requirements including amounts projected to complete the Company's existing capital expenditure program are continuously monitored and adjusted as input variables change. As these variables change, liquidity risks may necessitate the Company to conduct equity issues or obtain project debt financing.

The Company manages its liquidity risk by maintaining adequate cash and cash equivalents. The Company is actively seeking additional funding to improve its exposure to liquidity risk. The Company continually monitors its actual and forecast cash flows to ensure that there are adequate reserves to meet the maturing profiles of its financial assets and liabilities.

The following table outlines the maturities of the Company's liabilities:

	Contractual Cash Flows	Less than 1 Year
Accounts payable and accrued liabilities	\$ 207,486	\$ 207,486
Due to related party	\$ 7,690	\$ 7,690

#### Credit risk

The Company's principal financial assets are cash and cash equivalents. The credit risk on cash and cash equivalents is limited because the majority are deposited with banks with high credit ratings assigned by international credit-rating agencies. Accounts receivable consists of GST and interest on investments with a credible financial institution.

### 10. COMMITMENTS

The Company was granted the Phalombe Licence for the Songwe property on January 21, 2010. The license was issued by the Malawi Government on a three-year basis, originally, and on January 20, 2013 was renewed for an additional two years. The future spending commitments for the exploration rights with the Government of Malawi are 150,000,000 Kwacha, annually (foreign exchange rate MWK410):

Exploration commitments	\$ 365,854
Ground rent	31,292
<b>Total annual commitment</b>	<b>\$ 397,146</b>

On September 10, 2010, the Company was granted an additional exploration licence by the Malawi Minister of Natural Resources, Energy and Environment in respect of an area of 468 km<sup>2</sup> in Thambani, Mwanza District, Malawi. The license was issued on a three-year basis, originally, and as of September 10, 2013 was renewed for an additional two years. The future spending commitments for exploration expenses with the Government of Malawi are 250,000,000 Kwacha, annually (foreign exchange rate MWK410):

Exploration commitments	\$ 609,756
Ground rent	11,414
<b>Total annual commitment</b>	<b>\$ 621,170</b>

The Company expects to use the funds received from private placement equity financings to meet these commitments.

### 11. CAPITAL MANAGEMENT

The Company's total capital resources for the three months ended March 31, 2014 is (\$145,919), which consists of total equity. The Company closed an equity issue in two tranches on March 1, 2013 and April 11, 2013, which provided liquidity through 2013. The Company raised additional funds through an equity issue, which closed in two tranches on March 24, 2014 and April 3, 2014. It is anticipated that these additional funds will meet working capital requirements through 2014. The Company's objective when managing its capital is to have sufficient capital to maintain its ongoing operations, pursue its strategic opportunities and maintain a flexible capital structure which optimizes the cost of capital at an acceptable risk. The Company manages its capital structure and makes adjustments to it based on the funds available to the Company. The Company does not presently utilize any quantitative measures to monitor its capital. The Company has no externally imposed capital requirements.

## MKANGO RESOURCES LTD.

Notes to the Consolidated Interim Financial Statements

For the three months ended March 31, 2014 and 2013

(Reported in US dollars unless indicated otherwise)

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### 12. SUBSEQUENT EVENTS

#### Private Placement

On February 24, 2014, the Company announced that it had entered into a non-binding term sheet with certain affiliates of Sprott Inc. (the "Finders") to act as finders for the Company under the 2014 Financing.

On April 3, 2014, the second tranche of the 2014 Financing closed. The Company issued an additional 6,445,250 units at a price of C\$0.10 per unit for gross cash proceeds of C\$644,525 under the same terms as the first tranche of the Private Placement, which closed on March 24, 2014 (Note 8(a) to the Financial Statements).

The Company paid cash finders' fees totalling C\$40,677 and issued 406,770 finders' warrants in connection with the second tranche of the 2014 Financing. Each finders' warrant entitles the holder to acquire one Common Share for C\$0.10 until April 3, 2016.

The securities issued under the second tranche of the 2014 Financing, including any Common Shares issued on the exercise of the warrants and the finders' warrants, have a hold period expiring on August 4, 2014.

If, after four months from the closing date of the Private Placement, the closing price (or the average of the 'bid' and the 'ask', if not traded) of the Common Shares on the TSX Venture Exchange exceeds C\$0.30 for a period of 20 consecutive trading days, the Company may, within three trading days thereof, accelerate the expiry of the Warrants to 20 trading days after the issuance of a news release announcing the new expiry date.

#### Grant From The South African Department Of Trade And Industry

On May 26, 2014, the Company announced that the South African Department of Trade and Industry ("DTI") has approved a grant of Rand 7,967,804 (USD\$769,323) to the Company under its Capital Projects Feasibility Program. The grant will be dispersed to the Company between June 2014 and March 2015 as the Company meets certain milestones in relation to a number of activities including environmental and social impact studies, mine planning, design of the processing plant and tailings storage facility, flotation and hydrometallurgical optimization and marketing studies.

Mkango previously appointed the following groups to complete these various aspects of the project:

SNC-Lavalin (Pty) Ltd., South Africa	Beneficiation and hydrometallurgical plant, and associated infrastructure
Digby Wells Environmental, South Africa	Environmental and social impact studies
Epoch Resources (Pty) Ltd., South Africa	Tailings storage facility
Met-Chem Consulting (Pty) Ltd., Australia	Metallurgical optimization
Mintek, South Africa	Metallurgical optimization
The MSA Group (Pty) Ltd., South Africa	Mining studies and associated infrastructure
Nagrom Laboratories, Australia	Metallurgical optimization

#### Restricted Cash

1,300,000 Kwacha (US\$3,171), which was held by the Malawi Revenue Authority, customs and excise division as a bank guarantee from the Company in order to allow drilling equipment to be imported into the country for its Stage 2 drilling program was released back to the Company's bank account on April 29, 2014.