

Interim Consolidated Financial Statements of

ERDENE GOLD INC.

Second Quarter 2007

Three and six months ended June 30, 2007 and 2006
(unaudited)

Prepared by Management - See Notice to Reader

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August 10, 2007

NOTICE TO READER

Under National Instrument 51-102, Part 4, subsection 4.3 (3) (a), if an auditor has not performed a review of the interim financial statements, they must be accompanied by a notice to this effect. These interim consolidated financial statements have been prepared by management of the Company. Management have compiled the unaudited interim consolidated balance sheet of Erdene Gold Inc. as at June 30, 2007, the audited consolidated balance sheet as at December 31, 2006 and the unaudited interim consolidated statements of operations and deficit and cash flows for the three and six months ended June 30, 2007 and 2006. The Company's independent auditors have not audited, reviewed or otherwise attempted to verify the accuracy or completeness of the June 30, 2007 and 2006 consolidated interim financial statements. Readers are cautioned that these statements may not be appropriate for their intended purposes.

ERDENE GOLD INC.

Interim Consolidated Balance Sheets

June 30, 2007, with comparative figures for December 31, 2006

| | 2007 (unaudited) | 2006 (audited) |
|---|----------------------|----------------------|
| Assets | | |
| Current assets: | | |
| Cash and cash equivalents | \$ 11,646,771 | \$ 3,047,970 |
| Marketable securities (note 2) | — | 164,333 |
| Accounts receivable (note 3) | 272,883 | 363,147 |
| Prepaid expenses | 53,758 | 43,719 |
| | <u>11,973,412</u> | <u>3,619,169</u> |
| Cash – flow-through funds (note 4) | 1,948,523 | 4,598,523 |
| Resource property interests (note 5) | 20,511,843 | 16,754,731 |
| Capital assets, net (note 6) | 2,273,581 | 2,281,140 |
| Intangible assets, net (note 7) | 1,115,583 | 1,123,433 |
| Goodwill | 5,800,079 | 5,800,079 |
| | <u>\$ 43,623,021</u> | <u>\$ 34,177,075</u> |
| Liabilities and Shareholders' Equity | | |
| Current liabilities: | | |
| Accounts payable and accrued liabilities | \$ 485,430 | \$ 353,755 |
| Future income taxes (notes 8 and 13) | 5,179,290 | 2,899,290 |
| Shareholders' equity: | | |
| Share capital (note 8) | 54,919,639 | 44,611,619 |
| Contributed surplus (note 9) | 4,789,953 | 3,753,241 |
| Deficit | (21,751,291) | (17,440,830) |
| | <u>37,958,301</u> | <u>30,924,030</u> |
| Commitments (note 15) | | |
| | <u>\$ 43,623,021</u> | <u>\$ 34,177,075</u> |

See accompanying notes to consolidated financial statements.

Approved on behalf of the Board:

Signed "Stu Rath" Director

Signed "Ken MacDonald" Director

ERDENE GOLD INC.

Interim Consolidated Statements of Operations and Deficit
(unaudited)

| | 3 months ended June 30, 2007 | 3 months ended June 30, 2006 | 6 months ended June 30, 2007 | 6 months ended June 30 2006 |
|---|---------------------------------------|---------------------------------------|---------------------------------------|--------------------------------------|
| Revenue: | | | | |
| Lab Services | \$ 74,793 | \$ 22,929 | \$ 107,280 | \$ 22,929 |
| | 74,793 | 22,929 | 107,280 | 22,929 |
| Expenses: | | | | |
| Exploration and Operating expenses | | | | |
| Diamond drilling | 826,172 | 143,127 | 828,959 | 144,950 |
| Analytical and assaying | 31,993 | 70,157 | 36,466 | 79,380 |
| Geological services | 833,082 | 258,168 | 1,062,827 | 566,209 |
| Geo-technical surveys | 55,030 | 34,510 | 55,030 | 34,510 |
| Logistical and field support | 231,603 | 148,715 | 267,083 | 207,259 |
| Professional services | 3,431 | - | 3,431 | - |
| Travel | 40,989 | 96,132 | 80,720 | 116,954 |
| Lab and property maintenance | 132,611 | 22,674 | 230,162 | 22,674 |
| Write down of resource properties | 42,209 | 90,898 | 109,025 | 90,898 |
| Amortization of intangible assets | 817 | - | 7,850 | - |
| Other | 3,982 | 1,503 | 9,891 | 1,563 |
| | 2,201,919 | 865,884 | 2,691,444 | 1,264,397 |
| General and administrative expenses | | | | |
| Depreciation | 7,555 | 8,462 | 21,531 | 15,888 |
| Insurance | 19,155 | 17,067 | 35,690 | 29,390 |
| Investor relations and communications | 56,544 | 77,703 | 92,673 | 141,258 |
| Office | 28,703 | 23,526 | 57,859 | 53,589 |
| Professional services | 59,578 | 108,436 | 103,930 | 162,052 |
| Regulatory compliance | 62,605 | 119,562 | 103,494 | 141,787 |
| Administrative services | 109,120 | 139,995 | 236,013 | 239,648 |
| Stock-based compensation | 869,663 | - | 869,663 | 52,920 |
| Travel | 24,693 | 36,642 | 78,846 | 93,279 |
| Other | 9,326 | 4,983 | 12,123 | 8,141 |
| | 1,246,942 | 536,376 | 1,611,822 | 937,952 |
| Other income (expenses) | | | | |
| Interest revenue | 135,486 | 65,892 | 202,037 | 109,769 |
| Exploration partner contributions | 169,568 | 139,693 | 216,421 | 180,431 |
| Gain (loss) on sale of marketable securities | (2,669) | - | 469,569 | - |
| Gain on sale of resource properties | - | - | 70,666 | 32,667 |
| Foreign exchange | 10,602 | (33,311) | 3,775 | (27,470) |
| Other | (20,399) | 21,393 | (101,009) | 21,393 |
| | 292,625 | 193,667 | 861,459 | 316,790 |
| Loss for the period | 3,081,480 | 1,185,664 | 3,334,527 | 1,862,630 |
| Deficit, beginning of period | 17,693,877 | 12,880,589 | 17,440,830 | 12,203,623 |
| Share issue costs | 975,934 | - | 975,934 | - |
| Deficit, end of period | \$ 21,751,291 | \$ 14,066,253 | \$ 21,751,291 | \$ 14,066,253 |
| Basic and diluted loss per share (note 10) | \$ 0.05 | \$ 0.04 | \$ 0.06 | \$ 0.06 |
| Weighted average number of common shares outstanding | 58,509,026 | 32,073,361 | 58,509,026 | 32,073,361 |

See accompanying notes to the interim consolidated financial statements.

ERDENE GOLD INC.

Interim Consolidated Statements of Cash Flows
(unaudited)

| | 3 months ended June 30, 2007 | 3 months ended June 30, 2006 | 6 months ended June 30, 2007 | 6 months ended June 30 2006 |
|---|---------------------------------------|---------------------------------------|---------------------------------------|--------------------------------------|
| Cash provided by (used in): | | | | |
| Operations: | | | | |
| Loss for the period | \$(3,081,480) | \$(1,185,664) | \$(3,334,527) | \$(1,862,630) |
| Item not involving cash: | | | | |
| Depreciation | 10,772 | 10,363 | 30,528 | 18,789 |
| Amortization of intangible assets | 817 | - | 7,850 | - |
| Stock-based compensation | 1,492,336 | - | 1,492,336 | - |
| Write down of resource properties | 42,209 | 90,898 | 109,025 | 90,898 |
| Gain on sale of marketable securities | 2,669 | - | (469,569) | - |
| Gain on sale of resource properties | - | - | (70,666) | (32,667) |
| Change in non-cash working capital | 154,169 | 210,107 | 376,233 | 132,777 |
| | (1,378,508) | (874,296) | (1,858,790) | (1,525,825) |
| Financing: | | | | |
| Issue of common shares for cash | 10,000,000 | - | 10,000,000 | - |
| Share issue costs | (726,934) | - | (726,934) | - |
| Issue of common shares on exercise of options and warrants | 938,226 | 37,925 | 1,058,226 | 849,789 |
| | 10,211,292 | 37,925 | 10,331,292 | 3,849,789 |
| Investments: | | | | |
| Proceeds on sale of resource properties | - | - | 70,666 | 32,667 |
| Proceeds on sale of marketable securities | 67,997 | - | 704,568 | - |
| Resource property interests | (1,000,833) | 71,906 | (3,275,966) | (151,229) |
| Purchase of capital assets | (22,154) | (2,321) | (22,969) | (5,296) |
| | (954,990) | 69,585 | (2,523,701) | (123,858) |
| Increase (decrease) in cash | 7,877,794 | (766,786) | 5,948,801 | 2,200,106 |
| Cash, beginning of period | 5,717,500 | 7,236,883 | 7,646,493 | 4,269,991 |
| Cash, end of period | \$13,595,294 | \$ 6,470,097 | \$13,595,294 | \$ 6,470,097 |
| Cash is defined as: | | | | |
| Cash and cash equivalents | 11,646,770 | 6,470,097 | 11,646,770 | 6,470,097 |
| Cash – flow through funds | 1,948,524 | - | 1,948,524 | - |
| | \$ 13,595,294 | \$ 6,470,097 | \$ 13,595,294 | \$ 6,470,097 |

See accompanying notes to the interim consolidated financial statements.

ERDENE GOLD INC.

Notes to the Interim Consolidated Financial Statements

Six months ended June 30, 2007
(unaudited)

Nature of business:

Erdene Gold Inc. (the "Company") was incorporated by Articles of Incorporation dated June 27, 2000, pursuant to the provisions of the Canada Business Corporations Act. The principal business of the Company is the exploration and development of mineral deposits. The Company is principally focused on the discovery of large tonnage, low cost, gold, copper, molybdenum, coal and uranium deposits primarily in Mongolia; and the development of its coal and industrial mineral interests in North America with near-term cash flow potential. To date the Company has not yet earned any significant operating revenues and is considered to be in the exploration and development stage.

The Company is listed on the Toronto Stock Exchange (TSX - ERD).

1. Summary of significant accounting policies:

(a) Principles of consolidation:

These consolidated financial statements are presented in Canadian dollars and include the accounts of the Company and its wholly-owned subsidiaries Erdene Gold International Inc. and Erdene International Exploration Inc. (Barbados); Tamerlane International Limited (Bermuda); Erdene Mongol XXK, Erdene Energy XXK and Anian Resources XXK (Mongolia); Erdene Resources Inc. (formerly Kaoclay Resources Inc ("Kaoclay")) and 6531954 Canada Limited (Canada); and Sparta Kaolin Corporation (Delaware). Inter-company accounts and transactions have been eliminated.

(b) Changes in accounting policies:

On January 1, 2007, the Company adopted recommendations of CICA handbook sections 1530 "Comprehensive Income", Section 3251 "Equity", Section 3855 "Financial Instruments – Recognition and measurement", Section 3861 "Financial Instruments – Disclosure and Presentation" and Section 3865 "Hedges".

Section 1530 establishes standards for reporting and presenting comprehensive income, which is defined as the change in equity from transactions and other events from non-owner sources. Other comprehensive income refers to items recognized in comprehensive income that are excluded from net income calculated in accordance with generally accepted accounting principles.

Section 3855 prescribes when a financial asset, financial liability or non-financial derivative is to be recognized on the balance sheet and at what amount, requiring fair value or cost-based measures under different circumstances. Under Section 3855, financial instruments must be classified into one of five categories: held-for-trading, held-to-maturity, loans and receivables, available-for-sale financial assets or other financial liabilities. All financial instruments, including derivatives, are measured in the balance sheet at fair value except for loans and receivables, held to maturity investments and other financial liabilities which are measured at amortized cost. Subsequent measurement and changes in fair value will depend on their initial

ERDENE GOLD INC.

Notes to the Interim Consolidated Financial Statements, page 2

Six months ended June 30, 2007
(unaudited)

(b) Changes in accounting policies (continued):

classification, as follows: held-for-trading financial assets are measured at fair value and changes in fair value are recognized in net earnings; available-for-sale financial instruments are measured at fair value with changes in fair value recorded in other comprehensive income until the investment is derecognized or impaired at which time the amounts would be recorded in net earnings.

Under adoption of these new standards, the Company designated marketable securities as available-for-sale securities. Such securities are measured at fair value in the consolidated financial statements with unrealized gains or losses recorded in comprehensive income (loss). At the time securities are sold, or otherwise disposed of, gains or losses are included in net earnings (loss). The Company designated cash, accounts receivable, cash flow through funds and accounts payable and accrued liabilities as held-for-trading, which is measured at fair market value,

Section 3251 of the CICA Handbook requires the separate presentation of the components of equity (retained earnings, accumulated other comprehensive income, the total of retained earnings and accumulated other comprehensive income, contributed surplus, share capital and reserves) and the changes in equity arising from each of these components.

Section 3861 establishes standards for presentation of financial instruments and non-financial derivatives, and identifies the information that should be disclosed about them. Under the new standards, policies followed for periods prior to the effective date generally are not reversed and therefore, the comparative figures have not been restated.

Section 3865 specifies the circumstances under which hedge accounting is permissible and how hedge accounting may be performed. The Company currently does not have any hedges.

(c) Use of estimates:

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the dates of the financial statements and the reported amounts of revenue and expenses during the years. Significant estimates and assumptions relate to the recoverability of resource property interests and the calculation of stock-based compensation. While management believes that these estimates and assumptions are reasonable, actual results could differ.

(d) Cash and cash equivalents:

The Company considers deposits in banks and highly liquid investments with remaining maturities of three months or less at the date of acquisition as cash and cash equivalents.

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Notes to the Interim Consolidated Financial Statements, page 3

Six months ended June 30, 2007
(unaudited)

(e) Marketable securities:

Marketable securities are carried at fair market value.

(f) Resource property interests:

All direct costs related to the acquisition of resource property interests are capitalized by property. Exploration costs are charged to operations in the period incurred until such time as it has been determined that a property has good potential for an economically recoverable resource, in which case subsequent exploration costs and the costs incurred to develop a property will be capitalized. When a resource property is brought into commercial production, the capitalized costs of that property will be depleted over the estimated economic life of the property.

Gains or losses are recognized on property dispositions when the value of the consideration received exceeds or is less than, respectively, the carrying value of the property. Partial dispositions or option proceeds with respect to undeveloped properties are credited against the cost of the related property except that, when the proceeds exceed the costs, the excess is credited to operations. The aggregate costs related to abandoned properties are charged to operations.

Contributions from exploration partners to fund explorations expenses are recorded on the accrual basis as reduction of other expenses.

The Company reviews the carrying values of its resource property interests on a regular basis by reference to the project economics, including the timing of the exploration and/or development work, the work programs and exploration results. When the carrying value of a property exceeds its estimated net recoverable amount, an impairment provision is made.

(g) Capital assets:

Capital assets are recorded at cost and are amortized over their estimated useful lives at the following annual rates and methods:

| Asset | Basis | Rate |
|-----------------------------------|-------------------|------|
| Building | Declining balance | 10% |
| Equipment, furniture and fixtures | Declining balance | 20% |
| Software and computers | Declining balance | 33% |
| Vehicles | Declining balance | 30% |

ERDENE GOLD INC.

Notes to the Interim Consolidated Financial Statements, page 4

Six months ended June 30, 2007
(unaudited)

1. Summary of significant accounting policies (continued):

(h) Foreign currency translation:

Integrated subsidiaries are financially or operationally dependent on the parent company. The accounts of Erdene Gold International Inc., Erdene International Exploration Inc., Tamerlane International Limited, Erdene Mongol XXK, Erdene Energy XXK, Anian Resources XXK, Erdene Resources Inc. (formerly Kaoclay Resources Inc.), 6531954 Canada Limited, and Sparta Kaolin Corporation which are considered to be integrated operations use the temporal method to translate their financial statements. Under this method monetary items are translated at exchange rates in effect at the balance sheet date, non-monetary assets and liabilities are translated at historical exchange rates, and revenues and expenses are translated at average exchange rates for the period.

Realized and unrealized exchange gains and losses are included in earnings.

(i) Income taxes:

The Company uses the asset and liability method of accounting for income taxes. Under the asset and liability method, future tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Future tax assets and liabilities are measured using enacted or substantively enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on future tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the date of enactment or substantive enactment. A valuation allowance is provided when it is more likely than not that a future tax asset will not be recognized.

(j) Stock-based compensation:

The Company has a stock-based compensation plan, which is described in note 8. The Company accounts for all stock-based payments to non-employees and employee awards that are direct awards of stock using the fair value based method. Consideration paid by employees on the exercise of stock options is recorded as share capital.

Under the fair value based method, compensation cost attributable to awards to employees is measured at fair value at the grant date. Stock-based payments to non-employees are measured at the fair value of the consideration received, or the fair value of the equity instruments issued, or liabilities incurred, whichever is more reliably measurable at the grant date.

ERDENE GOLD INC.

Notes to the Interim Consolidated Financial Statements, page 5

Six months ended June 30, 2007
(unaudited)

1. Summary of significant accounting policies (continued):

(k) Flow-through shares:

The Company has financed a portion of its exploration activities through the issue of flow-through shares. As permitted under the Income Tax Act (Canada), the tax attributes of eligible expenditures incurred with the proceeds of flow-through share issuances are renounced to subscribers. On the date that the Company files the renouncement documents with the tax authorities, a future income tax liability is recognized and shareholders' equity is reduced, for the tax effect of expenditures renounced to subscribers (see note 13).

(l) Intangible assets:

Intangible assets represent the value of certain customer relationships and contracts, as well as the brand value of an acquired subsidiary, and are amortized on a straight-line basis over their estimated useful lives of 15 years.

(m) Goodwill:

Goodwill is the residual amount that results when the purchase price of an acquired business exceeds the sum of the amounts allocated to the assets acquired, less liabilities assumed, based on their fair values. Goodwill is allocated, as of the date of the business combination, to the Company's reporting units that are expected to benefit from the synergies of the business combination.

Goodwill is tested for impairment annually. The fair value of each reporting unit that includes goodwill is compared to the total carrying amount (including goodwill) of that reporting unit. If the fair value exceeds the carrying value, goodwill is not considered to be impaired. If the fair value is less than the carrying value, the fair values of the assets and liabilities within the reporting unit are estimated. The difference between the fair value of the assets and liabilities within the reporting unit and the fair value of the entire reporting unit represents the deemed fair value of the goodwill of the reporting unit. When the carrying value of goodwill exceeds the deemed fair value, the excess is charged to earnings in the period in which the impairment is determined.

ERDENE GOLD INC.

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Six months ended June 30, 2007
(unaudited)

2. Marketable Securities:

| | | | June 30 2007 | December 31 2006 |
|-----------------------|------|---------------------|-----------------|---------------------|
| | Cost | Unrealized gains | Fair value | Fair value |
| Marketable securities | \$ - | \$ - | \$ - | \$ 522,667 |
| | \$ - | \$ - | \$ - | \$ 522,667 |

3. Accounts receivable:

| | June 30 2007 | December 31 2006 |
|------------------------------|-----------------|---------------------|
| Trade receivables | \$ 46,393 | \$ 47,392 |
| Exploration partner recovery | 169,662 | 251,149 |
| Other | 56,828 | 64,606 |
| | \$ 272,883 | \$ 363,147 |

Other receivables includes an amount receivable of \$43,500 (2006 - \$44,700) from a director and officer, which is non-interest bearing and repayable on demand.

4. Cash – flow-through funds:

On July 14, 2006 The Company completed a \$6,000,000 flow-through financing to fund its commitment under the Donkin Coal Alliance (see note 5) regarding the exploration and evaluation of the Donkin Coal Resource Block located in Cape Breton, Nova Scotia. The use of these funds is restricted to qualifying Canadian Exploration Expenditures (“CEE”) under the Income Tax Act (Canada) and is therefore shown separately. To June 30, 2007 \$4,051,477 was advanced to the project manager Xstrata Coal Donkin Management Limited leaving a balance of \$1,948,523. It is the Company's intention to advance these funds to the project manager who anticipates expending these funds on CEE before the end of the 2007 fiscal year.

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Six months ended June 30, 2007
(unaudited)

5. Resource property interests:

The Company's mineral exploration licenses in Mongolia are held by its subsidiaries, Erdene Mongol XXK, Erdene Energy XXK and Anian Resources XXK. Mineral exploration licenses in Mongolia are valid for a period of three years and, through renewals, can be extended to a maximum of nine years. These rights are held in good standing through the payment of an annual license fee. The Company's mineral exploration licenses in Georgia are held by its subsidiary, Sparta Kaolin Corporation, and in Nova Scotia the Company's interest in the Donkin coal project is held through Erdene Resources Ltd.'s wholly owned subsidiary, 6531954 Canada Limited. Resource property interests include the cost of acquisition of resource properties and exploration and development costs incurred on properties determined to have good potential for an economically recoverable resource.

| | Jan - Jun 2007 | Jan - Dec 2006 |
|--|----------------------|----------------------|
| Balance, beginning of period | \$ 16,754,731 | \$ 2,001,708 |
| Additions during period | 1,216,137 | 1,852,006 |
| Deferred exploration expenditures (Donkin) | 2,650,000 | 1,401,477 |
| Acquired via plan of arrangement | – | 11,999,500 |
| Write-downs | (109,025) | (460,178) |
| Exploration partner contributions | – | (39,782) |
| | \$ 20,511,843 | \$ 16,754,731 |

The Company's significant resource properties and joint venture agreements are outlined below:

a) Xstrata Copper agreement:

In January 2007, the Company entered into an agreement with Xstrata Copper to acquire the rights to two Mongolian copper-gold properties, subject to certain vendor back-in rights. These projects were acquired through Xstrata plc's acquisition of Falconbridge Limited ("Falconbridge"), in August 2006.

The two core licenses over the main prospects are under option from the vendor of the property, a group of three local Mongolians. The four larger surrounding licenses, obtained in November 2006, are owned 100% by Xstrata Copper and are currently held in trust by their Mongolian geologic consultant, Mine Info, via a separate Letter Agreement.

The Company and Xstrata Copper entered into an Assignment and Option Agreement in January 2007 whereby the Company can acquire 100% of Falconbridge's rights and interest in an option agreement with a Mongolian company ("Mongolian Agreement") covering two copper-gold exploration licenses located in south central Mongolia. The Company assumed responsibility for all of Falconbridge's remaining obligations to the license owners as defined in the Mongolian Agreement. In addition, Xstrata Copper has agreed to assign its 100% interest in four exploration licenses that are contiguous to the optioned properties.

ERDENE GOLD INC.

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Six months ended June 30, 2007
(unaudited)

a) Xstrata Copper agreement (continued):

The remaining obligations under the Mongolian Agreement include incurring US\$450,000 in exploration expenditures by January 2009 and by making cash payments of US\$40,000 in January 2007 (paid on January 30, 2007) and US\$50,000 in January 2008. To June 30, 2007 the Company has incurred US\$83,848 of its US\$450,000 obligation. After fulfilling these remaining obligations, the Company will have earned an 80% interest in the two properties with the Mongolian company retaining the remaining 20%. The Company can earn a 100% interest in the properties, subject to a 2.5% net smelter royalty, by making a US\$2 million advance royalty payment over a five year period. The Company also has the option to reduce the net smelter royalty to 0.5% by making cash payments of US\$1 million for each 0.5% reduction in the net smelter royalty over an eight year period.

In exchange for granting the Company the rights and interest described above, Xstrata Copper has the right to acquire 75% of the Company's interest in the optioned properties and the four Falconbridge licenses by making a payment to the Company equal to 200% of the funds expended on the properties by the Company. Xstrata Copper must exercise its option within 60 days of receipt of a full feasibility study.

b) Sparta:

The Company, through its subsidiary Sparta Kaolin Corporation, has entered into lease agreements and exploration agreements with options to lease and/or purchase kaolin properties in the United States. The aggregate commitment associated with the cancelable agreements over the next twelve months is US \$46,000. These agreements also provide that the Company will pay a royalty based on either the production of finished product or crude tons extracted from the related properties. The majority of the payments to land-owners pursuant to these agreements are creditable against future royalty payments or, where applicable, the purchase price of the property. The Maddox property, which is owned by Sparta Kaolin Corporation, is under long term lease to Rinker Materials Corporation and is in the process of permit approval for a commercial aggregate quarry with production anticipated in 2008.

c) Donkin:

In December 2004, the Nova Scotia Department of Natural Resources ("NSDNR") issued a "Call for Proposals for the Exploration/Development of the Donkin Coal Resource Block". The Donkin Coal Resource Block is the largest remaining undeveloped coal resource in the Sydney, Nova Scotia coalfield that has the potential to be mined by underground methods.

The Donkin Coal Alliance was formed by or on behalf of Xstrata Coal Pty Limited (66%), Kaoclay Resources Inc. ("Kaoclay") (20%), American Transbridge Technologies LLC (9.3%) and PDC Resources Corporation (4.67%) to submit a proposal to the Province of Nova Scotia to secure the exclusive right to the Donkin Coal Project; namely, the project to explore, assess, study and, if feasible, develop the Donkin Coal Resource Block into an operating coal mine. On December 14,

ERDENE GOLD INC.

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(unaudited)

5. Resource property interests (continued):

c) Donkin (continued):

2005 the Province of Nova Scotia announced that the Donkin Coal Alliance was the successful proponent. Effective June 12, 2006, Kaoclay amalgamated with Erdene Resources Inc., a wholly-owned subsidiary of the Company, under a court approved Plan of Arrangement and Kaoclay is now a wholly-owned subsidiary of the Company operating under the name of Erdene Resources Inc. On April 23, 2007 the Company concluded agreements with minority partners to increase its ownership in the Donkin Coal Alliance from 20% to 25% in exchange for cash consideration of \$10,625 (paid in fiscal 2006) and 360,000 common shares of the Company which were issued on April 23, 2007 with a fair value of \$529,200 giving a total consideration of \$539,825 for the purchase of the additional 5% interest in the Donkin Coal Alliance. Under the agreements, Xstrata Coal Donkin Limited ("XCDL"), a related party to Xstrata Coal Pty Limited has also increased its interest in the Donkin Coal Alliance from 66% to 75% in exchange for cash.

The members of the Donkin Coal Alliance signed an agreement ("Alliance Agreement") effective March 11, 2005, and amending agreements dated April 23, 2006, October 26, 2006 and October 27, 2006. The Company and XCDL are presently negotiating the terms of a definitive joint venture agreement and sales agency agreement. Pursuant to the April 23, 2006 amending agreement, the Company's interest in the Donkin Alliance is held by 6531954 Canada Limited, a wholly owned subsidiary of Erdene Resources Inc., and Xstrata Coal Pty Limited's interest is held by XCDL. Xstrata Coal Donkin Management Limited, a related party to XCDL is acting as manager for the Donkin Coal Project. If the Donkin Coal Project is approved to proceed to development, the manager will be responsible for mine development, including infrastructure, coal mining and processing, and coal distribution and sales programs.

In June 2006, Xstrata Coal Donkin Management Limited acquired the surface lands relating to the Donkin Coal Resource Block from the Cape Breton Development Corporation ("CBDC"). The Donkin Coal Alliance began its exploration program and evaluation and scoping study ("Exploration Program") in June 2006.

Pursuant to the Alliance Agreement, the Company is committed to fund up to \$10,000,000 ("Initial Funding") of the expenditures incurred during the exploration program of the Donkin Coal Project provided such expenses qualify as CEE. Xstrata Coal Donkin Limited agreed to pay any other costs up to a maximum of \$5,000,000 but if the Company only pays a portion of the Initial Funding, XCDL is only obliged to pay a corresponding portion of the \$5,000,000. The Company is responsible to fund 25% of any additional expenditures incurred in the exploration program if it is to maintain its 25% interest in the Donkin Coal Project. A preliminary estimate of the total budget for the Exploration Program is approximately \$17,200,000 and the exploration program is expected to be complete in the first quarter of 2008. In July 2006, the Company completed a \$6,000,000 flow-through financing to partially fund its obligation.

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Notes to the Interim Consolidated Financial Statements, page 10

Six months ended June 30, 2007
(unaudited)

5. Resource property interests (continued):

d) Gallant agreement:

On March 1, 2005 the Company entered into an agreement with Gallant Minerals Limited ("Gallant") to acquire certain uranium property licenses and license applications in Mongolia, obtain possession and control of certain assets and geological data pertaining to Mongolia and an exclusive and irrevocable option to acquire all of the issued and outstanding shares of Gallant's wholly-owned subsidiary, Tamerlane International Limited ("Tamerlane") which controls 100% ownership of mineral properties in Mongolia through it's wholly owned subsidiary Anian Resources XXK.

On February 28, 2007, the Company met all conditions of the agreement and has acquired 100% ownership of Tamerlane.

Gallant is entitled to a net smelter return royalty on certain properties ranging from 1% to 1.5%, subject to a buy-down provision.

e) Xstrata Coal agreement:

On February 16, 2006 the Company concluded an agreement ("Alliance Agreement (Mongolia)") with Xstrata Coal Canada Limited ("Xstrata") a subsidiary of Xstrata plc (London Stock Exchange: XTA.L; Zurich Stock Exchange: XTA.S), pursuant to which Xstrata subscribed for 3,000,000 common shares of the Company at \$1.00/share.

Under the agreement, Xstrata was granted a first option to enter into a joint venture and earn a 75% interest in any coal opportunity in Mongolia identified by the Company by funding all work through completion of a feasibility study. Should the Company elect to develop or pursue third party participation in any non-coal projects or properties in Mongolia or elsewhere, Xstrata has a 60-day right to review all supporting project information and, if it wishes to participate in the project, to negotiate the terms of its participation before the Company may make the opportunity available to another party or develop the property itself. As part of the agreement Xstrata named a nominee to the Board of Directors of the Company. The rights granted to Xstrata under the agreement expire if Xstrata does not maintain a 5% equity position in the Company although parties' rights and obligations for any established joint venture survive.

Under the agreement, Xstrata is entitled to participate in all future financings of the Company to allow them to hold up to 9.9% of the common shares of the Company.

As a result of share issuances since the agreement was concluded, Xstrata Coal's equity position has been reduced to 4.6%. However, due to current discussions involving Xstrata Coal, Erdene has waived, until September 30, 2007 ("Waiver Date"), the requirement that Xstrata Coal maintain a 5% equity position in order to be able to exercise its rights under the Alliance Agreement (Mongolia). Erdene has agreed that Xstrata Coal may, prior to the Waiver Date, increase its equity interest to in excess of 5% by way of an issuance from treasury at an issue price to be agreed between Erdene and Xstrata Coal.

ERDENE GOLD INC.

Notes to the Interim Consolidated Financial Statements, page 11

Six months ended June 30, 2007
(unaudited)

5. Resource property interests (continued):

f) Denison Mines Corporation joint venture agreement:

On June 14, 2005, pursuant to an April 4, 2005 Memorandum of Understanding with International Uranium Corporation ("IUC"), now Denison Mines Corporation, the Company granted International Uranium Mongolia Ltd. ("IUM") the exclusive right and option to acquire a 65% interest in its uranium properties. IUM must spend \$6,000,000 of eligible expenditures on the properties over a period of up to four years. The Company and IUM have also formed a strategic alliance for the purpose of staking additional ground in Mongolia for the exploration of uranium over a three year period. In addition, IUC purchased one million common shares of the Company at a price of \$1.00 per share by way of a private placement. A finder's fee totaling \$60,000 was paid in connection with this transaction.

6. Capital assets:

| | | | June 30 2007 | December 31 2006 |
|-----------------------------------|--------------|-----------------------------|-------------------|---------------------|
| | Cost | Accumulated depreciation | Net book value | Net book value |
| Land | \$ 1,894,364 | \$ – | \$ 1,894,364 | \$ 1,874,766 |
| Building | 386,830 | 211,416 | 175,414 | 184,525 |
| Equipment, furniture and fixtures | 627,102 | 492,789 | 134,313 | 148,181 |
| Software and computer | 119,437 | 64,911 | 54,526 | 57,742 |
| Vehicles | 27,267 | 12,303 | 14,964 | 15,926 |
| | \$ 3,055,000 | \$ 781,419 | \$ 2,273,581 | \$ 2,281,140 |

ERDENE GOLD INC.

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Six months ended June 30, 2007
(unaudited)

7. Intangible assets:

| | | | June 30 2007 | December 31 2006 |
|--------------------------------------|--------------|-----------------------------|-------------------|---------------------|
| | Cost | Accumulated amortization | Net book value | Net book value |
| Customer relationships and contracts | \$ 984,500 | \$ 89,792 | \$ 894,708 | \$ 898,683 |
| Brand | 232,500 | 11,625 | 220,875 | 224,750 |
| | \$ 1,217,000 | \$ 101,417 | \$ 1,115,583 | \$ 1,123,433 |

8. Share capital:

Authorized and issued

| | Three Months Ended June 30, 2007 | | Six Months Ended June 30, 2007 | |
|--|-------------------------------------|---------------|-----------------------------------|---------------|
| | Number of shares | \$ | Number of shares | \$ |
| Authorized: | | | | |
| Unlimited number of common shares without par value | | | | |
| Issued: | | | | |
| Balance, beginning of period | 53,951,127 | \$ 43,147,947 | 53,051,127 | \$ 44,611,619 |
| Issued for cash | 10,000,000 | 10,000,000 | 10,000,000 | 10,000,000 |
| Issued on buyout of minority partners (Note 5 (c)) | 360,000 | 529,200 | 360,000 | 529,200 |
| Issued pursuant to option agreement | - | - | 700,000 | 574,000 |
| Tax effect of renunciation (Note 13) | - | - | - | (2,280,000) |
| Issued on exercise of options and warrants | 1,327,438 | 1,242,492 | 1,527,438 | 1,484,820 |
| Balance, end of period | 65,638,565 | \$ 54,919,639 | 65,638,565 | \$ 54,919,639 |

ERDENE GOLD INC.

Notes to the Interim Consolidated Financial Statements, page 13

Six months ended June 30, 2007
(unaudited)

The following table summarizes the continuity of the warrants for June 30, 2007.

Warrants

| | Three months ended June 30, 2007 | | Six months ended June 30, 2007 | |
|-----------------|-------------------------------------|---------------------------------|-----------------------------------|---------------------------------|
| | Number of Warrants | Weighted Avg. Exercise Price | Number of Warrants | Weighted Avg. Exercise Price |
| Opening balance | 5,665,725 | \$ 1.40 | 6,465,725 | \$ 1.33 |
| Issued | 600,000 | 1.15 | 600,000 | 1.15 |
| Exercised | (887,938) | 0.69 | (1,087,938) | 0.67 |
| Expired | - | - | (600,000) | 0.96 |
| Closing balance | 5,377,787 | \$ 1.49 | 5,377,787 | \$ 1.49 |

The following is a summary of the warrants outstanding as of June 30, 2007:

| Exercise Price | Expiry Date | Number of Warrants |
|----------------|------------------|--------------------|
| \$ 1.00 | January 14, 2008 | 296,812 |
| 0.43 | January 23, 2008 | 231,000 |
| 1.15 | April 11, 2008 | 360,000 |
| 1.60 | June 15, 2009 | 4,489,975 |
| \$ 1.49 | | 5,377,787 |

On April 12, 2007 the Company issued 600,000 broker warrants with a fair value of \$249,000 as part of an agreement with National Bank Financial and Wellington West Capital to purchase, on a private placement bought deal basis, 10,000,000 shares of the Company at \$1.00 per share.

The Company estimates the fair value of warrants at the date of grant using the Black-Scholes model, recognized over the vesting period with the following assumptions:

| | 2007 | 2006 |
|-------------------------|--------|--------|
| Dividend yield | 0% | 0% |
| Risk-free interest rate | 4.15% | 5.0% |
| Expected volatility | 90% | 80% |
| Expected life | 1 year | 2 year |

ERDENE GOLD INC.

Notes to the Interim Consolidated Financial Statements, page 14

Six months ended June 30, 2007
(unaudited)

8. Share capital (continued):

The following table summarizes the continuity of the stock options for June 30, 2007.

| Options | Three Months Ended June 30, 2007 | | Six Months Ended June 30, 2007 | |
|-----------------|-------------------------------------|---------------------------------|-----------------------------------|---------------------------------|
| | Number of Options | Weighted Avg. Exercise Price | Number of Options | Weighted Avg. Exercise Price |
| Opening balance | 3,254,000 | \$0.80 | 3,259,000 | \$0.80 |
| Granted | 1,500,000 | 1.36 | 1,500,000 | 1.36 |
| Exercised | (439,500) | 0.75 | (439,500) | 0.75 |
| Expired | - | - | (5,000) | 1.05 |
| Closing balance | 4,314,500 | \$1.00 | 4,314,500 | \$1.00 |

The following is a summary of the options outstanding and exercisable as of June 30, 2007:

| Exercise price | Expiry date | Number of options |
|----------------|-------------------|-------------------|
| \$0.43 | May 8, 2008 | 104,000 |
| \$0.43 | November 18, 2008 | 187,500 |
| \$0.85 | March 31, 2009 | 100,000 |
| \$0.85 | April 6, 2009 | 620,000 |
| \$0.85 | August 26, 2009 | 100,000 |
| \$0.70 | February 4, 2010 | 118,000 |
| \$0.77 | May 1, 2010 | 90,000 |
| \$0.74 | July 1, 2010 | 10,000 |
| \$0.85 | August 5, 2010 | 125,000 |
| \$1.05 | March 31, 2011 | 170,000 |
| \$0.85 | August 23 2011 | 1,190,000 |
| \$1.35 | May 11, 2012 | 1,225,000 |
| \$1.43 | May 25, 2012 | 275,000 |
| \$1.00 | | 4,314,500 |

Stock Based Compensation:

During the six months ended June 30, 2007, 1,500,000 options (2006 - 180,000) were granted to certain directors, officers, employees, and consultants of the Company. The fair value of the options on the date granted of \$1,492,336 (2006 - \$127,008) was expensed as \$869,662 in administrative stock-based compensation (2006 - \$52,920) and \$622,674 in geological services (2006 - \$74,088). The Company estimates the fair value of stock based incentives at the date of grant using the Black-Scholes model, recognized over the vesting period with the following assumptions:

ERDENE GOLD INC.

Notes to the Interim Consolidated Financial Statements, page 15

Six months ended June 30, 2007
(unaudited)

8. Share Capital (continued):

Stock Based Compensation (continued):

| | 2007 | 2006 |
|-------------------------|---------|---------|
| Dividend yield | 0% | 0% |
| Risk-free interest rate | 4.15% | 5.0% |
| Expected volatility | 90% | 80% |
| Expected life | 5 years | 5 years |

9. Contributed surplus:

The following summarizes amounts recorded as contributed surplus during the period:

| | Jan - Jun 2007 | Jan - Dec 2006 |
|---|---------------------|---------------------|
| Opening balance | \$ 3,753,241 | \$ 1,201,779 |
| Warrants/options relating to issue costs | 249,000 | 141,362 |
| Warrants relating to purchase of subsidiary | – | 1,744,731 |
| Warrants/options exercised or expired | (704,624) | (228,545) |
| Options expensed | 1,492,336 | 893,914 |
| | <u>\$ 4,789,953</u> | <u>\$ 3,753,241</u> |

10. Basic and diluted loss per share:

As the Company incurred losses in the periods reported, the effect of outstanding warrants and options have been excluded from the computation of loss per share as their impact would be anti-dilutive, reducing loss per share.

ERDENE GOLD INC.

Notes to the Interim Consolidated Financial Statements, page 16

Six months ended June 30, 2007
(unaudited)

11. Financial instruments:

(a) Fair values:

The fair values of the Company's financial assets and liabilities included in current assets and liabilities approximate their carrying values at each period-end.

(b) Credit risks:

The Company places its cash and cash equivalents with high-quality financial institutions and public companies and believes that no significant concentration of credit risk exists with respect to cash and cash equivalents.

12. Foreign currency risks:

The Company operates in Mongolia, giving rise to foreign exchange risk in the Mongolian Tugrik. To limit the Company's exposure to this risk, cash and cash equivalents are primarily held in Canadian and U.S. dollar bank accounts.

13. Future income taxes:

| | June 30 2007 | December 31 2006 |
|------------------------------------|---------------------|---------------------|
| Kaoclay acquisition | \$ 2,100,983 | \$ 2,100,983 |
| Anian Resources acquisition | 798,307 | 798,307 |
| Renouncement of \$6 million in CEE | 2,280,000 | – |
| | <u>\$ 5,179,290</u> | <u>\$ 2,899,290</u> |

As permitted under the Income Tax Act (Canada), the tax attributes of eligible expenditures incurred with the proceeds of flow-through share issuances are renounced to subscribers. On February 28, 2007, the Company filed the renouncement documents with the tax authorities and recognized a future income tax liability of \$2,280,000, and reduced shareholders' equity, for the tax effect of expenditures renounced to subscribers.

ERDENE GOLD INC.

Notes to the Interim Consolidated Financial Statements, page 17

Six months ended June 30, 2007
(unaudited)

14. Segmented information:

The Company's executive office is located in Nova Scotia, Canada with resource properties and exploration and development activities in Canada, United States and Mongolia. The following table presents selected financial information by geographic origin (in thousands):

| | June 30, 2007 | | | | December 31, 2006 | | | |
|---------------------|---------------|--------|----------|--------|-------------------|--------|----------|--------|
| | Canada | USA | Mongolia | Total | Canada | USA | Mongolia | Total |
| Working capital | 11,273 | 70 | 145 | 11,488 | 3,122 | 118 | 25 | 3,265 |
| Capital assets | 60 | 2,148 | 66 | 2,274 | 68 | 2,145 | 68 | 2,281 |
| Resource properties | 10,103 | 6,523 | 3,886 | 20,512 | 6,924 | 6,523 | 3,308 | 16,755 |
| Total assets | 25,404 | 13,914 | 4,305 | 43,623 | 16,612 | 14,008 | 3,557 | 34,177 |

15. Commitments:

The Company has an operating lease for office premises until August 31, 2011. The Company has the right to terminate the lease by giving notice prior to the anniversary date, after 2007. Annual payments are as follows:

| | | |
|------|----|---------|
| 2007 | \$ | 29,495 |
| 2008 | | 57,733 |
| 2009 | | 58,888 |
| 2010 | | 60,065 |
| 2011 | | 30,633 |
| | \$ | 236,814 |

16. Accumulated other comprehensive income:

| | June 30, 2007 |
|---|---------------|
| Opening balance | \$ — |
| Adjustment to opening balance on adoption of new accounting policy | 358,334 |
| Unrealized gain of marketable securities | — |
| Reclassification of earnings on available for sales marketable securities | (358,334) |
| | \$ — |

17. Comparative figures:

Certain comparative financial data for 2006 has been reclassified to conform to the presentation adopted in the 2007 financial statements.



ERDENE GOLD INC.

Management Discussion and Analysis Second quarter - June 30, 2007

This Management Discussion and Analysis of Erdene Gold Inc. (the "Company") provides analysis of the Company's financial results for the three and six months ended June 30, 2007 and its financial position as at June 30, 2007. The following discussion and analysis provides a summary of selected consolidated financial information for the three and six month period ended June 30, 2007 and 2006 and includes financial information relating to the Company and its wholly owned subsidiaries, Erdene Gold International Inc. and Erdene International Exploration Inc., both incorporated under the laws of Barbados, Tamerlane International Limited incorporated under the laws of Bermuda, Erdene Resources Inc. and its wholly owned subsidiary 6531954 Canada Limited, both incorporated under the laws of Canada, Sparta Kaolin Corporation, incorporated under the laws of Delaware as well as Erdene Mongol XXK, Erdene Energy XXK and Anian Resources XXK which are incorporated under the laws of Mongolia. The consolidated financial statements of the Company have been prepared by management, in Canadian dollars, in accordance with Canadian generally accepted accounting principles (see note 1: Summary of Significant Accounting Policies). The following information should be read in conjunction with the unaudited consolidated financial statements of the Company for the three and six months ended June 30, 2007 and 2006, and the audited consolidated financial statements of the Company for the year ended December 31, 2006, including all accompanying notes to the consolidated financial statements.

This discussion includes certain statements that may be deemed "forward-looking statements". All statements in this discussion, other than statements of historical fact, that address reserve potential, exploration drilling, exploitation activities and events or developments that the Company expects, are forward-looking statements. Although the Company believes the expectations expressed in such forward-looking statements are based on reasonable assumptions, such statements are not guarantees of future performance and actual results or developments may differ materially from those in the forward-looking statements. Factors that could cause actual results to differ materially from those in forward-looking statements include market prices, exploitation and exploration results, continued availability of capital and financing and general economic, market or business conditions. Investors are cautioned that any such statements are not guarantees of future performance and actual results or developments may differ materially from those projected in the forward-looking statements. The information contained herein is stated as of August 10, 2007 and is subject to change after that date.

This Management Discussion and Analysis ("MD&A") has been prepared in accordance with the provisions of National Instrument 51-102, Section 5 and Form 51-102F1 and has been approved by the Company's Board of Directors.

1.01 Date of MD&A

This MD&A is prepared as of August 10, 2007

1.02 Nature of Business and Overall Performance

General

The Company is a resource exploration company listed on the Toronto Stock Exchange which, through the acquisition of Kaoclay Resources Inc. ("Kaoclay") in the second quarter of 2006, now owns three advanced-stage projects including coal assets in Nova Scotia and aggregate and kaolin clay assets in Georgia, U.S.A. The Georgia kaolin project began commercial production in January 2005. Cash flow is expected to increase over the next five years conditional on the Georgia aggregate project commencing production, anticipated in late 2008, and culminating with the potential production from the Donkin coal exploration and development project in Cape Breton, Nova Scotia. Until a decision is made to proceed with commercial development of the aggregate and coal projects, to expand the scope of the kaolin operations and until resultant cash flows increase substantially over current, the annual level of exploration expenditures of the Company is dependent primarily on the sale of share capital to finance its exploration programs. The Company has minimal sources of income other than revenue from an industrial lab in Eatonton, Georgia, royalty income from its kaolin and aggregate properties which are early stage, and interest earned on cash and short-term money market instruments. It is therefore difficult to identify any meaningful trends or develop an analysis from the Company's cash flows.

The Company is well-funded with its focus on the discovery of large tonnage, low cost, gold, copper, molybdenum, uranium and coal deposits primarily in Mongolia; and the development of its coal and industrial mineral interests in North America with near term cash flow potential. At June 30, 2007 the Company held 33 mineral licenses in Mongolia representing 14 projects covering approximately 1.1 million acres.

The following summarizes the Company's significant strategic alliances and agreements:

Xstrata Copper Agreement

In January 2007, the Company entered into an agreement with Xstrata Copper to acquire the rights to two Mongolian copper-gold properties, subject to certain vendor back-in rights. These projects were acquired through Xstrata plc's acquisition of Falconbridge Limited ("Falconbridge"), in August 2006.

The two core licenses over the main prospects are under option from the vendor of the property, a group of three local Mongolians. The four larger surrounding licenses, obtained in November 2006, are owned 100% by Xstrata Copper and are currently held in trust by their Mongolian geologic consultant, Mine Info, via a separate Letter Agreement.

The Company and Xstrata Copper entered into an Assignment and Option Agreement in January 2007 whereby the Company can acquire 100% of Falconbridge's rights and interest in an option agreement with a Mongolian company ("Mongolian Agreement") covering two copper-gold exploration licenses located in south central Mongolia. The Company assumed responsibility for all of Falconbridge's remaining obligations to the license owners as defined in the Mongolian Agreement. In addition, Xstrata Copper has agreed to assign its 100% interest in four exploration licenses that are contiguous to the optioned properties.

The remaining obligations under the Mongolian Agreement include incurring US\$450,000 in exploration expenditures by January 2009 and by making cash payments of US\$40,000 in January 2007 (paid on January 30, 2007) and US\$50,000 in January 2008. To June 30, 2007 the Company has incurred US\$83,848 of its US\$450,000 obligation. After fulfilling these remaining obligations, the Company will have earned an 80% interest in the two properties with the Mongolian company retaining the remaining 20%. The Company can earn a 100% interest in the properties, subject to a 2.5% net smelter royalty, by

making a US\$2 million advance royalty payment over a five year period. The Company also has the option to reduce the net smelter royalty to 0.5% by making cash payments of US\$1 million for each 0.5% reduction in the net smelter royalty over an eight year period.

In exchange for granting the Company the rights and interest described above, Xstrata Copper has the right to acquire 75% of the Company's interest in the optioned properties and the four Falconbridge licenses by making a payment to the Company equal to 200% of the funds expended on the properties by the Company. Xstrata Copper must exercise its option within 60 days of receipt of a full feasibility study.

Donkin Coal Alliance

The Donkin Coal Alliance was formed by or on behalf of Xstrata Coal Pty Limited (66%), Kaoclay Resources Inc. ("Kaoclay") (20%), American Transbridge Technologies LLC (9.33%) and PDC Resources Corporation (4.67%) to submit a proposal to the Province of Nova Scotia to secure the exclusive right to the Donkin Coal Project; namely, the project to explore, assess, study and, if feasible, develop the Donkin Coal Resource Block into an operating coal mine. On December 14, 2005, the Province of Nova Scotia announced that the Donkin Coal Alliance was the successful proponent. Effective June 12, 2006, Kaoclay amalgamated with Erdene Resources Inc., a wholly-owned subsidiary of the Company, under a court approved Plan of Arrangement and Kaoclay is now a wholly-owned subsidiary of the Company operating under the name of Erdene Resources Inc. On April 23, 2007 the Company concluded agreements with minority partners to increase its ownership in the Donkin Coal Alliance from 20% to 25% in exchange for cash consideration of \$10,625 (paid in fiscal 2006) and 360,000 common shares of the Company which were issued on April 23, 2007 with a fair value of \$529,200 giving a total consideration of \$539,825 for the additional 5% interest in the Donkin Coal Alliance. Under the agreements, Xstrata Coal Donkin Limited ("XCDL"), a related party to Xstrata Coal Pty Limited has also increased its interest in the Donkin Coal Alliance from 66% to 75% in exchange for cash.

The members of the Donkin Coal Alliance signed an agreement ("Alliance Agreement") effective March 11, 2005, and amending agreements dated April 23, 2006, October 26, 2006 and October 27, 2006. Pursuant to the April 23, 2006 amending agreement, the Company's interest in the Donkin Coal Alliance is held by 6531954 Canada Limited, a wholly owned subsidiary of Erdene Resources Inc., and Xstrata Coal Pty Limited's interest is held by XCDL. The Company and XCDL are presently negotiating the terms of a definitive joint venture agreement and a sales agency agreement. Xstrata Coal Donkin Management Limited, a related party to XCDL, is acting as manager for the Donkin Coal Project. If the Donkin Coal Project is approved to proceed to development, the manager will be responsible for mine development, including infrastructure, coal mining and processing, and coal distribution and sales programs.

In June 2006, Xstrata Coal Donkin Management Limited acquired the surface lands relating to the Donkin Coal Resource Block from the Cape Breton Development Corporation ("CBDC"). The Donkin Alliance began its exploration program and evaluation and scoping study ("Exploration Program") in June 2006.

Pursuant to the Alliance Agreement, the Company is committed to fund up to \$10,000,000 ("Initial Funding") of the expenditures incurred during the Exploration Program of the Donkin Coal Project provided such expenses qualify as Canadian Exploration Expenses ("CEE"). XCDL agreed to pay any other costs up to a maximum of \$5,000,000 but if the Company only pays a portion of the Initial Funding, XCDL is only obliged to pay a corresponding portion of the \$5,000,000. The Company is responsible to fund 25% of any additional expenditures incurred in the Exploration Program if it is to maintain its 25%

interest in the Donkin Coal Project. A preliminary estimate of the total budget for the Exploration Program is approximately \$17,200,000 and the Exploration Program is expected to be complete in the first quarter of 2008. In July 2006, the Company completed a \$6,000,000 flow-through financing to partially fund its obligation.

To June 30, 2007 \$4 million was advanced to the Xstrata Coal Donkin Management Limited leaving a balance of \$2 million. It is the Company's intention to advance the remaining funds to the project manager who anticipates expending these funds on CEE before the end of fiscal 2007.

Strategic Alliance with Xstrata Coal Canada Limited

On February 14, 2006 the Company concluded an agreement ("Alliance Agreement (Mongolia)") with Xstrata Coal Canada Limited ("Xstrata") a subsidiary of Xstrata plc (London Stock Exchange: XTA.L; Zurich Stock Exchange: XTA.S), pursuant to which Xstrata subscribed for 3,000,000 common shares of the Company at \$1.00/share.

Under the agreement, Xstrata was granted a first option to enter into a joint venture and earn a 75% interest in any coal opportunity in Mongolia identified by the Company by funding all work through completion of a feasibility study. Should the Company elect to develop or pursue third party participation in any non-coal projects or properties in Mongolia or elsewhere, Xstrata has a 60-day right to review all supporting project information and, if it wishes to participate in the project, to negotiate the terms of its participation before the Company may make the opportunity available to another party or develop the property itself. As part of the agreement Xstrata named a nominee to the Company's Board of Directors. The rights granted to Xstrata under the agreement expire if Xstrata does not maintain a 5% equity position in the Company although parties' rights and obligations for any established joint venture survive.

Under the agreement, Xstrata is entitled to participate in all future financings of the Company to allow them to hold up to 9.9% of the common shares of the Company.

As a result of share issuances since the agreement was concluded, Xstrata Coal's equity position has been reduced to 4.6%. However, due to current discussions involving Xstrata Coal, Erdene has waived, until September 30, 2007 ("Waiver Date"), the requirement that Xstrata Coal maintain a 5% equity position in order to be able to exercise its rights under the Alliance Agreement (Mongolia). Erdene has agreed that Xstrata Coal may, prior to the Waiver Date, increase its equity interest to in excess of 5% by way of an issuance from treasury at an issue price to be agreed between Erdene and Xstrata Coal.

Joint Venture Agreement with Denison Mines Corporation

On June 14, 2005, pursuant to an April 4, 2005 Memorandum of Understanding with International Uranium Corporation ("IUC"), now Denison Mines Corporation, the Company granted International Uranium Mongolia Ltd. ("IUM") the exclusive right and option to acquire a 65% interest in its uranium properties. IUM must spend \$6,000,000 of eligible expenditures on the properties over a period of up to four years. The Company and IUM have also formed a strategic alliance for the purpose of staking additional ground in Mongolia for the exploration of uranium over a three year period. In addition, IUC purchased one million common shares of the Company at a price of \$1.00 per share by way of a private placement. A finder's fee totaling \$60,000 was paid in connection with this transaction.

Agreement with Gallant Minerals Limited

On March 1, 2005 the Company entered into an agreement with Gallant Minerals Limited (“Gallant”) to acquire certain uranium property licenses and license applications in Mongolia, obtain possession and control of certain assets and geological data pertaining to Mongolia and an exclusive and irrevocable option to acquire all of the issued and outstanding shares of Gallant’s wholly-owned subsidiary, Tamerlane International Limited (“Tamerlane”) which controls 100% ownership of mineral properties in Mongolia through it’s wholly owned subsidiary Anian Resources XXK.

On February 28, 2007, the Company met all conditions of the agreement and has acquired 100% ownership of Tamerlane.

Gallant is entitled to a net smelter return royalty on certain properties ranging from 1% to 1.5%, subject to a buy-down provision.

The Company’s exploration program is led by a senior management team with extensive exploration experience in Mongolia and is well positioned to maximize value from its North American assets. The total budget for 2007 is approximately \$6 million. The company will continue to fund operating losses and exploration expenditures out of existing working capital and flow through funds which amounted to approximately \$11.5 million and \$2 million respectively at June 30, 2007.

1.03 Selected Annual Information

The following information has been extracted from the Company’s audited consolidated financial statements.

Expressed in thousands of Canadian dollars except per share amounts.

| Fiscal Year Ended December 31 | 2006 | 2005 | 2004 | 2003 |
|--------------------------------------|-------------|-------------|-------------|-------------|
| Revenues | \$ 250 | \$ - | \$ - | \$ - |
| Loss for the year | \$ 4,565 | \$ 4,981 | \$ 4,437 | \$ 629 |
| Basic and diluted loss per share | \$ 0.11 | \$ 0.19 | \$ 0.19 | \$ 0.14 |
| Total assets | \$ 34,177 | \$ 6,649 | \$ 9,426 | \$ 4,161 |
| Total long-term liabilities | \$ 2,899 | \$ - | \$ - | \$ - |
| Cash dividends declared | Nil | Nil | Nil | Nil |

All financial data has been prepared in accordance with Canadian generally accepted accounting principles.

1.04 Results of Operations

Three months ended June 30, 2007 and 2006

The Company had a loss of \$3,081,480 in the three months ended June 30, 2007, as compared to a loss of \$1,185,664 during the same period last year.

With the acquisition of Sparta Kaolin Corp (“Sparta”), via the acquisition of Kaoclay on June 12, 2006 Erdene began to earn a limited amount of revenue. Sparta’s industrial lab in Eatonton, Georgia generated \$74,793 in revenue in the three months ended June 30, 2007 compared to \$22,929 during the period of June 13th to June 30th the previous year.

Total exploration and operating expenses for the three months ended June 30, 2007 amounted to \$2,201,919 compared to \$865,884 in the same period in 2006. The Company has budgeted a more robust exploration season in 2007 compared to 2006 and as a result exploration expenses are expected to be higher than the prior year.

- During the three months ended June 30, 2007 the company was drilling on three separate properties: Zuun Mod (Molybdenum), Biger (copper/gold) and Khoot (Coal). As a result drilling costs were \$683,045 higher than the prior year.
- Geological services are \$574,914 higher than last year. The increase is entirely due to non cash stock based incentives of \$622,674 being issued in the quarter, versus zero in the same quarter the prior year.
- Logistical and field support costs are \$82,888 higher due to the increased exploration activity in 2007 compared to 2006.
- Lab and property maintenance costs are for a full three months in 2007, compared to the June 13th to 30th period in 2006. This accounts for the \$109,937 increase in costs when compared to the prior year.
- The Company also wrote off \$42,209 in resource properties in the second quarter of 2007 compared to \$90,898 for the same period the prior year.

The Company charges all exploration costs to operations in the period incurred until such time as it has been determined that a property has good potential to contain an economically recoverable resource, in which case subsequent exploration costs and the costs incurred to develop a property will be capitalized. All direct costs related to the acquisition of resource property interests have been capitalized as an asset. Total resource property additions for the quarter ended June 30, 2007 amounted to \$1,453,367. The aggregate costs of resource properties that have, or plan to be abandoned have been charged to operations which during the second quarter of 2007 amounted to \$42,209 resulting in a net addition during the three months ended June 30, 2007 of \$1,411,158. Total resource property additions in the three months ended June 30, 2006 amounted to \$13,147,890 with write offs of \$90,898 for net additions of \$13,056,992. The additions in the second quarter of 2006 included the Kaoclay acquisition.

Since the Company charges exploration costs to operations until a property displays good potential for an economically recoverable resource, reported losses vary directly with the extent of the exploration programs conducted. As the Company obtains exploration results from existing resource properties (and those it acquires) that justify and enable further equity financing and continued exploration programs, reported losses will continue and will vary with the extent of exploration activity until such time as economically recoverable resources are identified that warrant development to generate sustainable revenues from operations. Conversely, should exploration results not justify further equity financing or should further equity financing not be available or be insufficient to conduct planned exploration programs, exploration activity would be reduced with exploration funds directed toward projects with highest potential, resulting in lower reported losses. All of the Company's Mongolian properties were in the exploration phase, and accordingly, all exploration costs were charged to operations in the respective periods. The funds expended on the Donkin coal project have been capitalized because in the opinion of management the project has good potential to contain an economically recoverable resource. Further exploration and development costs will continue to be capitalized unless it is determined, at a future date, the resource will not be economically recoverable.

General and administrative expenses for the three months ended June 30, 2007 were \$1,246,942 compared to \$536,376 for the same period in 2006. The increase is entirely due to \$869,663 in non-cash stock based incentives expensed in the quarter. If these are excluded, total administrative costs decreased \$159,097 compared to same quarter in 2006.

Other income amounted to \$292,625 in the quarter ended June 30, 2007 compared with \$193,667 in the same quarter in 2006. The increase from 2006 was mainly a result of higher interest income, higher exploration recovery and a foreign exchange gain versus a loss in 2006.

Six months ended June 30, 2007 and 2006

The Company had a loss of \$3,334,527 in the six months ended June 30, 2007, as compared to a loss of \$1,862,630 during the same period last year.

Sparta's industrial lab in Eatonton, Georgia generated \$107,280 in revenue in the six months ended June 30, 2007 compared to \$22,929 during the period of June 13th to June 30th the previous year (the Kaoclay acquisition closed on June 12, 2007).

Total exploration and operating expenses for the six months ended June 30, 2007 amounted to \$2,691,444 compared to \$1,264,397 during the same period in 2006. The Company has budgeted a more robust exploration program in 2007 compared to 2006 and as a result exploration expenses are expected to be higher than the prior year.

- During the six months ended June 30, 2007 the company was drilling on three separate properties: Zuun Mod (Molybdenum), Biger (copper/gold) and Khoot (Coal). As a result drilling costs were \$684,009 higher than the same period in 2006.
- Geological services for the six months ended June 30, 2007 are \$496,618 higher than the same period in 2006. The increase is entirely due to non-cash stock based incentives of \$622,674 being issued compared to \$74,088 in 2006.
- Logistical and field support costs for the six months ended June 30, 2007 are \$59,824 higher than the same period in 2006 due to the increased exploration activity in 2007.
- Travel costs for the six months ended June 30, 2007 are \$36,234 lower than the same period in 2006. The 2006 costs included a multiple day tour of numerous properties in Mongolia which necessitated chartering a helicopter. These costs were not repeated in 2007.
- Lab and property maintenance costs are for six full months in 2007, compared to the June 13th to 30th period in 2006. This accounts for the \$207,488 increase in costs when compared to the prior year.
- The Company wrote off \$109,025 in resource properties in the six months ended June 30, 2007 compared to \$90,898 for the same period in 2006

The Company charges all exploration costs to operations in the period incurred until such time as it has been determined that a property has good potential to contain an economically recoverable resource, in which case subsequent exploration costs and the costs incurred to develop a property will be capitalized. All direct costs related to the acquisition of resource property interests have been capitalized as an asset, which during the first six months of 2007 amounted to \$4,144,167. The write down and

reductions in the cost of resource properties during the six months ended June 30, 2007 amounted to \$387,055 resulting in a net addition during the six months ended June 30, 2007 of \$3,757,112. Resource property additions in the six months ended June 30, 2006 amounted to \$13,906,025, with write-offs of \$90,898 for net additions of \$13,815,127. The 2006 additions include the Kaoclay acquisition.

Since the Company charges exploration costs to operations until a property displays good potential for an economically recoverable resource, reported losses vary directly with the extent of the exploration programs conducted. As the Company obtains exploration results from existing resource properties (and those it acquires) that justify and enable further equity financing and continued exploration programs, reported losses will continue and will vary with the extent of exploration activity until such time as economically recoverable resources are identified that warrant development to generate sustainable revenues from operations. Conversely, should exploration results not justify further equity financing or should further equity financing not be available or be insufficient to conduct planned exploration programs, exploration activity would be reduced with exploration funds directed toward projects with highest potential, resulting in lower reported losses. All of the Company's Mongolian properties were in the exploration phase, and accordingly, all exploration costs were charged to operations in the respective periods. The funds expended on the Donkin coal project have been capitalized because in the opinion of management the project has good potential to contain an economically recoverable resource. Further exploration and development costs will continue to be capitalized unless it is determined, at a future date, the resource will not be economically recoverable.

General and administrative expenses for the six months ended June 30 2007 were \$1,611,822 compared to \$937,952 for the same period in 2006. The variance is entirely due to an increase of \$816,743 in non-cash stock based incentives expensed in the first six months of 2007 compared to 2006. If these are excluded, total administrative costs decreased \$142,873 compared to same period in 2006.

Other income for the six months ended June 30, 2007 amounted to \$861,459 compared with \$316,790 in 2006. The increase from 2006 was a result of a one time gain on the sale of marketable securities, higher interest income in 2007, higher exploration partner recovery and an increase in gain of the sale of resource properties. This was partially offset by other expenses of \$101,009 which includes an accrual for Part XII.6 tax. Since the Company used the look-back rule to renounce CEEs to subscribers, it is required to pay a tax under part XII.6 calculated on the portion that was unspent after February of 2007.

1.05 Summary of Quarterly Results

Expressed in thousands of Canadian dollars except per share amounts

| | Fiscal 2007 | | Fiscal 2006 | | | | Fiscal 2005 | |
|-------------------------------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|
| | Q2 Jun-07 | Q1 Mar-07 | Q4 Dec-06 | Q3 Sep-06 | Q2 Jun-06 | Q1 Mar-06 | Q4 Dec-05 | Q3 Sep-05 |
| Revenue | \$74 | \$33 | (\$205) | \$301 | \$110 | \$44 | \$28 | \$54 |
| Loss | \$3,081 | \$253 | \$1,199 | \$1,504 | \$1,185 | \$677 | \$1,209 | \$1,573 |
| Basic and diluted loss per share | \$0.05 | \$0.01 | \$0.03 | \$0.03 | \$0.03 | \$0.02 | \$0.05 | \$0.06 |
| Total Assets | \$43,623 | \$34,245 | \$34,177 | \$39,170 | \$34,944 | \$10,345 | \$6,649 | \$7,924 |

All financial data has been prepared in accordance with Canadian generally accepted accounting principles.

1.06 Liquidity and Capital Resources

The Company had working capital at June 30, 2007 of \$11,487,991 representing an increase of \$8,222,577 from the December 31, 2006 working capital position of \$3,265,414. This working capital does not include \$1,948,523 in flow through cash the Company held at June 30, 2007. The flow-through funds are restricted to qualifying CEE and are therefore excluded from working capital. The increase in working capital is primarily due to an April 12, 2007 agreement with National Bank Financial together with syndicate partner Wellington West Capital who purchased, on a private placement bought deal basis, 10,000,000 shares of the Company at \$1.00 per share resulting in gross proceeds to Erdene of \$10,000,000, offset by cash issue costs of \$726,934. The company also received \$1,058,226 on the exercise of warrants and options during the six months ended June 30, 2007 and received proceeds of \$704,568 on the sale of marketable securities. These inflows were partially offset by expenditures related to Company's 2007 exploration program and general and administrative costs in support of the program.

Current working capital is sufficient to fund the company's remaining 2007 budgeted expenditures and meet its property and contractual commitments for the next 36 months. The timing for additional financing will be determined largely by market conditions and the results of the Company's ongoing exploration program.

During the six months ended June 30, 2007, \$4,144,167 was expended on additions to resource property interests offset by a write down of resource properties of \$109,025 and a reduction of \$278,030 due to the expiration of 600,000 Gallant warrants charged to resource properties in 2006. In the first quarter of 2007, the assigned value of these expired warrants was removed from resource properties and applied against contributed surplus. Of the \$4,144,167 expended in first six months of 2007, \$2,650,000 was advanced to the Donkin project manager Xstrata Coal Donkin Management Limited to fund qualifying CEE. The remaining \$1,494,167 in additions includes \$574,000 in non cash consideration made as part of the Gallant Agreement (see section 1.02)), \$529,200 in non cash consideration paid to increase the Company's ownership in the Donkin Coal Alliance (see section 1.02) and property applications and renewals on numerous Mongolian licenses.

During the six months ended June 30, 2007, the Company expended \$22,969 on capital assets compared to \$5,296 in 2006. The majority of the capital asset additions relate to the final payment on land in Georgia, USA.

Other than as discussed herein, the Company is not aware of any trends, demands, commitments, events or uncertainties that may result in the Company's liquidity or capital resources either materially increasing or decreasing at present or in the foreseeable future. Material increases or decreases in the Company's liquidity and capital resources will be substantially determined by the success or failure of the Company's exploration and development programs on its resource properties and its ability to obtain sufficient equity financing.

1.07 Contractual Obligations

As of June 30, 2007 the Company is committed to the following obligations:

- Pursuant to the Xstrata Copper Agreement (see section 1.02), the Company is committed to making a US\$50,000 payment in January 2008 and incurring US\$450,000 in exploration expenditures by January 2009. To June 30, 2007, the Company has incurred US\$83,848 of this exploration expenditure obligation.
- The Company has entered into an operating lease for office space until August 31, 2011 representing total payments of \$236,814 to the end of the lease. The Company has the right to terminate the lease by giving notice prior to the anniversary date, after 2007.
- The Company, through its subsidiary Sparta Kaolin Corporation, has entered into lease agreements and exploration agreements with options to lease kaolin properties in the United States. The aggregate commitment associated with the cancelable agreements over the next twelve months is US \$46,000.
- Pursuant to the Alliance Agreement (see section 1.02) the Company is committed to fund up to \$10,000,000 of the expenditures incurred during the Exploration Program of the Donkin Coal Project provided such expenses qualify as CEE.

1.08 Off-Balance Sheet Arrangements

As at June 30, 2007, the Company had no material off-balance sheet arrangements such as guarantee contracts, contingent interest in assets transferred to an entity, derivative instruments obligations or any obligations that trigger financing, liquidity, market or credit risk to the Company.

1.09 Critical Accounting Estimates

Critical accounting estimates used in the preparation of the Company's consolidated financial statements include the Company's estimate of the recoverable value of its resource properties, the value attributed to stock-based compensation and future taxes. These estimates could be significantly affected by factors beyond the Company's control.

The acquisition cost of resource properties are recorded as an asset on the balance sheet under the caption resource property interests until such time as the related property(ies) commence commercial production at which time it will be depleted against related mine revenue from the property(ies) or when the Company determines the carrying value of a property cannot be recovered, in which case the carrying value will be written off or down to its recoverable value. Since the Company charges all exploration costs to operations when incurred, with the exception of expenditures related to the Donkin coal project, and ultimately to deficit, until good potential for an economically recoverable resource has been identified, management feels confident that the recoverable value of its resource properties equals or exceeds its carrying value on the Company's balance sheet at June 30, 2007.

Stock-based compensation is calculated using the Black-Scholes model, a recognized option/warrant valuation formula, which is highly dependent on the expected volatility of the market price of the Company's common shares. The Company uses an expected volatility rate of 90% in 2007 (80% in 2006). This is an estimate only based on using past share trading data to predict future volatility and actual volatility may be different from the estimate used in the valuation formula. Although the actual cost

of stock-based compensation can vary materially from the estimated cost recorded in the Company's financial statements, it represents a non-cash expense and, as such, has no impact on the Company's financial position or liquidity.

Future income tax assets and liabilities are determined based on differences between the financial reporting and tax basis of assets and liabilities and on unclaimed losses carried forward and are measured using the substantively enacted tax rates expected to apply to taxable income in the years in which those differences are expected to reverse or when unclaimed losses are expected to be utilized. A valuation allowance is provided when it is more likely than not a future tax asset will not be recognized.

1.10 Changes in Accounting Policies

The accounting policies applied in the preparation of the June 30, 2007 unaudited interim consolidated financial statements did not differ materially from those applied in the preparation of the December 31, 2006 audited financial statements. A detailed summary of the Company's accounting policies and any estimates derived therefrom is described in Note 1 of the June 30, 2007 audited consolidated financial statements.

On January 1, 2007, the Company adopted recommendations of CICA handbook sections 1530 "Comprehensive Income", Section 3251 "Equity", Section 3855 "Financial Instruments – Recognition and measurement", Section 3861 "Financial Instruments – Disclosure and Presentation" and Section 3865 "Hedges".

Section 1530 establishes standards for reporting and presenting comprehensive income, which is defined as the change in equity from transactions and other events from non-owner sources. Other comprehensive income refers to items recognized in comprehensive income that are excluded from net income calculated in accordance with generally accepted accounting principles.

Section 3855 prescribes when a financial asset, financial liability or non-financial derivative is to be recognized on the balance sheet and at what amount, requiring fair value or cost-based measures under different circumstances. Under Section 3855, financial instruments must be classified into one of five categories: held-for-trading, held-to-maturity, loans and receivables, available-for-sale financial assets or other financial liabilities. All financial instruments, including derivatives, are measured in the balance sheet at fair value except for loans and receivables, held to maturity investments and other financial liabilities which are measured at amortized cost. Subsequent measurement and changes in fair value will depend on their initial classification, as follows: held-for-trading financial assets are measured at fair value and changes in fair value are recognized in net earnings; available-for-sale financial instruments are measured at fair value with changes in fair value recorded in other comprehensive income until the investment is derecognized or impaired at which time the amounts would be recorded in net earnings.

Under adoption of these new standards, the Company designated marketable securities as available-for-sale securities. Such securities are measured at fair value in the consolidated financial statements with unrealized gains or losses recorded in comprehensive income (loss). At the time securities are sold, or otherwise disposed of, gains or losses are included in net earnings (loss). The Company designated cash, accounts receivable, cash flow through funds and accounts payable and accrued liabilities as held-for-trading, which is measured at fair market value,

Section 3251 of the CICA Handbook requires the separate presentation of the components of equity (retained earnings, accumulated other comprehensive income, the total of retained earnings and

accumulated other comprehensive income, contributed surplus, share capital and reserves) and the changes in equity arising from each of these components.

Section 3861 establishes standards for presentation of financial instruments and non-financial derivatives, and identifies the information that should be disclosed about them. Under the new standards, policies followed for periods prior to the effective date generally are not reversed and therefore, the comparative figures have not been restated.

Section 3865 specifies the circumstances under which hedge accounting is permissible and how hedge accounting may be performed. The Company currently does not have any hedges.

1.11 Financial Instruments and Other Risks

The Company's financial instruments consist of cash, marketable securities, accounts receivable, prepaid expenses and accounts payable. Management does not believe these financial instruments expose the Company to any significant interest, currency or credit risks. The fair market value of these financial instruments approximates their carrying values, unless otherwise noted.

In conducting its business, the principal risks and uncertainties faced by the Company relate primarily to exploration results and, to a lesser extent, metal prices. Exploration for minerals and development of mining operations involve many risks, many of which are outside the Company's control. In addition to the normal and usual risks of exploration and mining, the Company works in remote locations that lack the benefit of infrastructure and easy access.

At this stage in the Company's development it relies on equity financing for its long-term working capital and capital requirements to fund its exploration and development programs. Future equity financing could be adversely or positively affected by many factors outside the Company's control such as market or commodity price changes, changes in the value of the Canadian dollar against the US dollar and/or the Mongolian Tugrik, general economic conditions, exploration results or political or economic changes in Mongolia. The Company does not have sufficient funds to put any of its properties into commercial production from its current financial resources. There is no assurance that such financing will be available to the Company when required, or that it will be available on acceptable terms.

1.12 Outstanding Share Data

See Note 8 to the June 30, 2007 interim consolidated financial statements for detail as to the change in the issued and outstanding common shares, warrants and options of the Company during the three months ended June 30, 2007.

Issued and Outstanding Share Capital

During the six month period ended June 30, 2007 the Company issued a total of 12,587,438 shares as follows:

- On April 12, 2007, the Company concluded an agreement with National Bank Financial together with syndicate partner Wellington West Capital who purchased, on a private placement bought deal basis subject to certain conditions, 10,000,000 shares of the Company at \$1.00 per share resulting in gross proceeds to Erdene of \$10,000,000.
- On February 28, 2007 the company issued 700,000 shares to Gallant Minerals Limited as part of the final payment concluding the agreement signed on March 1, 2005 (see section 1.02 "Agreement with Gallant Minerals Limited").

- The company issued 360,000 shares of the Company as partial consideration to increase its ownership in the Donkin project (see section 1.02 "Donkin Coal Alliance").
- The Company issued 1,527,438 shares on the exercise of warrants and options during the six months ended June 30, 2007.

This brings the total shares outstanding at June 30, 2007 to 65,638,565.

Warrants

During the six months ended June 30, 2007, 600,000 broker warrants were issued as part of the \$10 million financing mentioned above, 1,087,938 warrants were exercised at an average price of \$0.67 per share for gross proceeds of \$728,263, and 600,000 warrants expired. This brings the outstanding warrants at June 30, 2007 to 5,377,787.

Stock Options

During the six months ended June 30, 2007, 1,500,000 options were granted to certain directors, employees and contractors of the Company, 439,500 options were exercised at an average price of \$0.75 for gross proceeds of \$329,963 and 5,000 options expired bringing the outstanding options at June 31, 2007 to 4,314,500.

1.13 Exploration Results

Overview

At June 30, 2007 the Company was actively carrying out its 2007 exploration season field work. Exploration costs incurred in the second quarter were predominantly associated with the drilling program at the Company's Mongolian Zuun Mod molybdenum project and to a lesser extent on drilling at the Biger copper-gold-PGE project and exploration work on the Mogoit Tsagaan Owoo copper-gold projects. The following is a brief summary for each of the Company's exploration projects which are expected to work in 2007.

Zuun Mod Porphyry Molybdenum Project

The Zuun Mod property is a porphyry molybdenum prospect located in Bayankhongor Province approximately 950 kilometres southwest of Ulaanbaatar and 180 kilometres north of the Mongolia-China border. The property consists of a single exploration license totaling 49,538 hectares. The license is registered in the name of Anian Resources XXK a wholly owned subsidiary of the Company. This project was acquired from Gallant Minerals Limited and is subject to a net smelter royalty (refer to section 1.02).

The Zuun Mod project has been under exploration and evaluation since 2002. Subsequent to signing an agreement with Gallant Minerals Limited in March 2005 to acquire the licence, the Company carried out extensive exploration that has resulted in the delineation of multiple targets with significant molybdenum intersections, locally proximal to surface. The type and styles of alteration and mineralization within the Company's Zuun Mod property are consistent with many characteristics documented from other porphyry-type deposits within Mongolia and worldwide.

In the first quarter 2007 Erdene appointed Minarco Asia Pacific Pty Limited ("Minarco") to evaluate strategic options and advise on project planning and design for the Zuun Mod molybdenum project. Minarco is a prominent mining and energy industry advisor in the Asia Pacific region and has recently been involved in assisting China Molybdenum with the technical aspects of its Initial Public Offering. As well, Minarco has worked on various projects with many of China's major coal and steel producers.

Minarco's review, based on the drill results and other data, indicates the Zuun Mod molybdenum project has the potential to host reserves in the two most advanced zones (Racetrack and Stockwork zones), and their extensions, of similar tonnage to other major molybdenum projects being currently developed elsewhere in the world with average grades equal to or greater than 0.05% Mo. In addition, Minarco believes there is reasonable potential to identify additional targets within the identified 7.5-kilometre long by 600 metre wide molybdenum-in-rock surface geochemical anomaly.

Minarco recommended a two-phase drilling program. Drilling of the Phase I program started in early May and the initial round of Phase I drilling was completed in early June and consisted of 17 drill holes. Based on the results of this round of drilling the Phase I program was expanded with an additional 11 holes drilled in July and early August to extend the 200 metre spaced drilling to the northeast and southwest. Results from the first 17 drill holes have been received and reported as of August 9, 2007.

The Phase I drilling program has significantly extended the area of known mineralization in the area of the Racetrack Zone. The results from the Phase I program have outlined a central mineralized zone characterized by greater than 0.06% Mo over thicknesses ranging from 58 to 194 metres with many holes open at depth. This zone ranges up to 300 metres in width over a minimum strike length of 1.4 kilometres with results pending over a total distance of 2.5 kilometres. The mineralization remains open to the north, at depth and to the west where it is overlain by volcanic cover. The central mineralized zone has been intersected over a thickness of 380 metres (ZMD-13, 0.05% Mo) and comes within 18 metres of surface (ZMD-29). Included within the larger molybdenum zones are higher grade zones proximal to surface:

- ZMD-11 and ZMD-13 indicate continuity over a 25 metre thick zone grading 0.10% Mo within 80 metres of surface; and,
- ZMD-29 intersected 28 metres of 0.11% Mo beginning at 84 metres depth.

The drill program has now advanced to Phase II to test the 2.5-kilometre strike length identified in the Phase I program at 100 metre spacing. The objective of the Phase II drill program is to identify a National Instrument 43-101 compliant molybdenum resource for the Zuun Mod project. Two drill rigs are currently operating on site.

Mogoit and Tsagaan Owoo Copper Gold Projects

In January 2007, the Corporation entered into an agreement with Xstrata Copper ("Xstrata") to acquire the rights to two Mongolian copper-gold properties, subject to certain vendor back-in rights. These projects were acquired through Xstrata plc's acquisition of Falconbridge Limited ("Falconbridge"), in August 2006. The two properties host anomalous copper-gold mineralization targets located in central Mongolia.

The two properties lie 30 kilometres apart in south central Mongolia, 460 kilometres southwest of the capital city of Ulaanbaatar and approximately 60 kilometres from Arvakheer, the provincial capital. The two properties are within a large, contiguous, six license claim group totaling 98,838 hectares. Two of the licenses were acquired by Falconbridge through an option agreement with a Mongolian company and are subject to certain cash payments, exploration expenditure requirements and royalty provisions (refer to section 1.02). The remaining four licenses were acquired by Falconbridge through staking. All of the licenses are subject to certain back-in rights in favor of Xstrata (see section 1.02).

In 2006, Falconbridge completed mapping, soil and rock sampling, and geophysical surveys to test for a porphyry-style copper-gold system beneath the mineralized surface showings on both properties. This work identified target areas characterized by coincident geophysical (IP and magnetic) and geochemical (rock and soil) anomalies in areas of historic shallow pits and trenching. Rock samples from these areas have returned significant copper (up to 14%) and gold (up to 4 g/t) values. Falconbridge identified a number of high priority drill targets on the two properties. Due diligence sampling by the Corporation in late 2006 confirmed the surface assay values reported by Falconbridge.

In the second quarter of 2007, Erdene carried out a detailed surface exploration program consisting of geological mapping, trenching, and rock, soil and stream sediment geochemical surveys. The program was designed to confirm and further determine the extent of the previously identified prospective zones, investigate the styles of mineralization, evaluate the large license area surrounding the two main prospects and generate targets for a late summer scout drilling program.

At Mogoit, in addition to geological mapping and rock sampling (68 rock chip samples), six trenches were excavated for a total of 359 metres resulting in 187, 2-metre rock chip samples being sent for analysis. In addition, the 155 soil geochemical samples were collected across the central Mogoit prospect, expanding upon the previous Falconbridge soil survey. The trenching was carried out over two zones, the North-central zone and the Northeast zone. At the north-central zone, two trenches, 30 metres apart, exposed a northwest trending, 20 to 40 metres wide strongly altered zone with copper oxide mineralization. This zone is open to the northwest and southeast. In the Northeast zone, four trenches exposed a northeast trending 10 to 20 metres wide zone of strong alteration and copper oxide mineralization over a strike length of 280 metres that remains open. This zone of alteration appears along a 250 by 1000 metres northeast trending sinuous magnetic high anomaly.

At Tsagaan Ovoo five trenches were excavated over a total of 290 metres in the vicinity of the historic trenches identified in this area with 160, 1 to 2 metre rock chip samples sent for analysis. These trenches have exposed a northwest trending 20 to 30 metres wide mineralized alteration-zone. The exposed alteration is approximately 360 metres in length and open to the northwest and southeast. The alteration zone appears to be controlled by northwest trending structural zone associated with a magnetic feature that averages 150 metres in width over more than 5 kilometres across the prospect area.

A reconnaissance geological mapping and stream sedimentary survey was carried out over the large area between the Mogoit and Tsagaan Ovoo occurrences designed to begin the evaluation of this highly prospective area.

Final results of the various geochemical surveys are pending. It is anticipated that drill targets will be generated from these surveys and that a drill program will commence near the end of August.

Biger Copper-Gold-PGE Project

The Biger property is an early stage exploration project located in a highly prospective area for copper and gold located approximately 780km southwest of Ulaanbaatar and 100 kilometres southeast of the provincial centre of Altai in Govi-Altai Province in southwestern Mongolia. The property consists of a single exploration license totaling 12,522 hectares. The license is registered in the name of Anian Resources XXK, a wholly owned subsidiary of the Company. This project was acquired from Gallant Minerals Limited and is subject to a net smelter royalty (refer to section 1.02)

Exploration work to date, including rock and soil geochemistry (including mobile metal ion (MMI)), magnetic and induced polarization (gradient and dipole-dipole) geophysical programs and a three-hole diamond drilling program have resulted in the identification of a number of significant anomalies. Rock samples have returned copper values up to 2.8%, accompanied by elevated palladium (1.37 g/t), gold (0.5 g/t), and platinum (0.29 g/t). A drill hole testing coincident geochemical and geophysical anomalies in the Altan Khad outlier intersected a 24 metre section that assayed 0.5% copper with elevated gold (86 ppb) and palladium (89 ppb) values. An area covered by recent sediments with a radius of at least 6 kilometres from this drill intersection remains untested.

In 2006, a gradient induced polarization survey and follow-up 5-line dipole-dipole survey was completed over the central Altan Khad mineralized outlier, adjoining buried pediment area and an adjacent mineralized gabbro/diorite located 7 kilometres to the east. In addition, a two line mobile metal ion (MMI) geochemical orientation survey was also completed over the central Altan Khad mineralized outlier and the mineralized zone intersected in the 2005 drill hole in an attempt to identify buried mineralized bodies. Analyses of the MMI results indicate that subtle gold and copper anomalies occur over zones of magnetic high. Five zones were identified for follow up or initial scout drill testing. Selection of these zones was based upon previous drill results, surface rock geochemistry, magnetic and IP geophysics anomalies, and MMI geochemical anomalies. The target zones include the NW pediment, Altan Khad zone, South-central pediment (south of Altan Khad), NE pediment, and SW Biger intrusive complex.

A seven-hole drill program, testing these targets was completed July 5th, 2007 totalling 1,737metres. A total of 753 samples were selected and sent to SGS in Ulaanbaatar for preparation of sampling pulps. The sample pulps have been sent to SGS China to enable the analysis of platinum group elements which can not be done at the Ulaanbaatar lab. Receipt of all analytical data is anticipated in September, 2007.

Erdenet Ikh-Tal Porphyry Copper Project

The Erdenet Project is located in Orkhon and Bulgan aimags in northern Mongolia, approximately 250 kilometres northwest of Ulaanbaatar, the capital of Mongolia. The properties are connected to Ulaanbaatar by paved road and a rail line which is a spur of the Trans Mongolian railroad which runs through Mongolia between Russia and China. The Erdenet Ikh-Tal properties consist of three contiguous exploration licenses (Ikh Tal 1 to 3) covering 8,540 hectares which surround the Erdenet Mine Corporation ("EMC") open pit copper-molybdenum mining operation. The license is registered in the name of Anian Resources XXK, a wholly owned subsidiary of the Company. This project was acquired from Gallant Minerals Limited and is subject to a net smelter royalty (see section 1.02)

The project goal is to identify extensions of porphyry-style copper/molybdenum mineralization on the Company's exploration licenses that surround the Erdenet open pit copper/molybdenum mining operation. Erdenet is the second largest porphyry copper deposit in Central Asia and one of the largest in the world, with published mining reserves in 2002 of 766.7 million tonnes grading 0.61% copper and 0.015% molybdenum.

To date the Company has carried out extensive mapping, geochemical and geophysical programs. A 12 hole reconnaissance drilling program has been carried out over the past two years testing geochemical, alteration and geophysical anomalies. The drilling program has resulted in the identification of several anomalous intersections. Drill hole, ITDD 4 in the South-Central Baglai area, located 200 metres from the EMC property boundary intersected a mineralized zone starting at 36 metres that returned 0.2% copper over 32 metres, including an 8 metre section of 0.3% copper and up to 0.65% copper over 2 metres. Locally, samples exceeding 0.2% copper over 2 metres were returned deeper in the hole. A second hole, ITDD-08, located 200 metres southeast of ITDD-04, intersected 32 metres of 0.27% copper including 0.33% copper over 12 metres, starting at 34 metres from surface. In addition, sulfide zones were intersected deeper in the hole including 8 metres of 0.3% copper at 125 metres and 25 metres of 0.23% copper from 215 metres to the bottom of the hole. A broad high chargeability anomaly has been traced for 400 metres southeast of ITDD-08 along with surface porphyry style alteration.

In the Northwest Extension area, hole ITDD-09, located 1200 metres northwest of EMC's open pit, returned a 35 metre interval with copper oxide mineralization that averaged 0.21% copper from 24 to 59 metres. This includes a five metre section of 0.71% copper at 54 metres. Hole ITDD-10, located 550 metres to the northeast of hole ITDD-09, intersected five metres of 0.25% copper at 40 metres from the surface.

These results indicate the extension of both near surface oxide and deeper sulfide porphyry copper mineralization onto the Corporation's adjoining property to the southeast as well as the northwest of EMC's mine and demonstrate potential for the discovery of economic copper concentrations in near-surface oxide zones and deeper sulfide ore-bodies.

Additional geological mapping and sampling in the Tsagaan Chuluut area in the north central part of the Ikh Tal 1 license, 4 kilometres northwest of the Erdenet open pit has outlined an area of silicification and alunite alteration coincident with a large magnetic low, high chargeability and low resistivity. During the second quarter, an 11 kilometre dipole-dipole survey was completed on four 200 metre spaced lines on the Tsagaan Chuluut property. Preliminary interpretation indicated a broad (1300m wide) moderate chargeability anomaly (up to 14mv) and a coincident resistivity low at a depth of 250 metres on the two lines adjacent to the western boundary of the property. These two dipole-dipole lines will be extended 625 metres to the south to close off the dipole anomaly. In addition, a dipole-dipole line is planned between the two anomalous dipole-dipole lines in an attempt to trace this anomaly to a depth of 500 metres. These anomalies are coincident with a large magnetic low anomaly which is a characteristic of the Erdenet Mine deposit magnetic signature. Final interpretation of geophysical results is expected in early August. Drilling is anticipated to begin in mid August to test the anomalies at Tsagaan Chuluut and to follow up mineralization intersected at Baglai and the northwest extension area.

Bayan Kharaat Copper Porphyry Project

The Bayan Kharaat property is located approximately 200 kilometres north north-west of Ulaanbaatar in Selenge province. The property is located adjacent to the paved highway leading from Ulaanbaatar to the Russian border-crossing at Sukhbaatar. Bayan Kharaat lies within the Ervana Arc Terrane which hosts numerous porphyry deposits, including Erdenet, Shand, Oyuut, and others. The property consists of a single exploration license covering 3,523 hectares. The license is registered in the name of Anian Resources XXK, a wholly owned subsidiary. This project was acquired from Gallant Minerals Limited and is subject to a net smelter royalty (refer to section 1.02)

The Company previously carried out a ground magnetic survey and gradient IP survey over the southern and central portion of the Bayan Kharaat property. The magnetics showed very strong NE-SW and NW-SE trending linear features, which appear to intersect in the area of strong alteration and associated copper mineralization. In June 2006, a systematic soil survey was carried out on a 200 metre grid over the south western and south central portions of the property. Two target areas of co-incident silicification, sericite/pyrite alteration and elevated copper in soil and chargeability have been outlined on the NE-SW trending structure in granite porphyry in the southwest central area and in felsic volcanics in the west central area. Additional exploration is planned for 2007.

Tsenkher Gol Gold Project

The Tsenkher Gol property is located in Khentii Province 180 kilometres east of Ulaanbaatar and is accessible by a newly paved highway. The property consists of two contiguous licenses totaling 7,982 hectares. The license is registered in the name of Anian Resources XXK, a wholly owned subsidiary. This project was acquired from Gallant Minerals Limited and is subject to a net smelter royalty (refer to section 1.02)

Exploration work to date has included geological mapping, an extensive soil geochemical survey and geophysical surveys (magnetic and IP), and a two phase drilling program. Under the Phase I drilling program four target areas (Altan Suult and three in the Khond Uul area), 1 to 4 kilometres apart, all returned anomalous gold intersections (0.2 g/t gold and higher) commonly over significant thicknesses (up to 68 metres) including 10 metres of 1.2g/t gold and 2 metres of 6.6g/t gold at Altan Suult. This Phase I drilling program confirmed that gold mineralization is hosted in granitic, volcanic and metasedimentary rock types and extends to depth in multiple gold mineralized zones over broad thicknesses. These broad zones of low grade gold mineralization locally envelop higher grade zones.

A six-hole Phase II diamond drill program was initiated in mid October 2006 to further test mineralized zones and structural targets in the Altan Suult area. The Phase II holes were step-out holes ranging from 120 to 280 metres from the previous Phase I drilling and tested coincident surface gold geochemical and dipole-dipole geophysical anomalies. Broad zones of anomalous gold values including 62 metres (52 to 114 metres) of 0.10g/t gold in drill hole TGD-10 and narrow higher grade zones, including 2 metres (223 to 225 metres) of 1.6g/t gold in drill hole TGD-9, were intersected.

Gold bearing zones have now been traced over 7 kilometers at Khond Uul and over an area approximately 1 kilometre by 1 kilometre at Altan Suult with both areas remaining open at depth and in all directions. These results support the presence of a strong gold bearing hydrothermal system over a wide area (5 by 10 kilometres). A data compilation and comprehensive technical report on the project was underway during the second quarter. A decision on future work on the project is pending the completion of the technical report.

Energy Project – Coal

The Company is involved in a comprehensive coal generative program in cooperation with Xstrata Coal Canada Limited ("Xstrata") evaluating numerous prospective metallurgical and high quality thermal coal deposits. The Company's technical staff has compiled an extensive database on coal deposits, occurrences and prospective sedimentary basins allowing for a prioritization of targets. Data on approximately 370 coal deposits and occurrences have been entered into the database. All the Company's coal exploration in Mongolia is being fully funded by Xstrata (refer to section 1.02 for further information about the Xstrata alliance agreement) and is being carried out in consultation with Xstrata personnel.

One of the priority targets identified to date is the Galshar coal property located 300 kilometres southeast of Ulaanbaatar on the border of Dornogovi and Khentii provinces. Galshar lies 63 kilometres from the nearest rail link and 250 kilometres from the Mongolia-China border. Four exploration licenses totaling 97,338 hectares are considered to be part of the Galshar coal property. The licenses are 100% owned by the Corporation and are registered in the name of the Erdene Mongol XXX, a wholly owned subsidiary.

In 2005 and 2006, Erdene completed eleven exploration drill holes, with an average spacing of greater than 1 kilometre and totalling 1,093 metres in the Galshar basin. Drilling identified a 34.2 metre thick coal seam overlain by five smaller 1 metre thick seams. Drilling by the Corporation in 2006 (drill hole GHR-11) confirmed the coal seams extend at least 3.6 kilometres to the northeast of the Corporation's 2005 drill hole CDD-01 that returned a 21.8 metre section of greater than 10,000 BTU/lb coal with low ash (6%) and low sulfur (0.4%). Hole GHR-03, located 2.2 kilometres northeast of hole CDD-01 intersected a 17.4 metre section of the main coal seam that averaged greater than 8,000 BTU/lb. Drilling results from 2006 and historic exploration reports suggest additional seams may also occur east and south of the area currently being explored.

During the second quarter the Company was involved in preparations for the start of the resource delineation phase of the Galshar exploration project. In addition, the Company continued to evaluate its extensive coal database and was involved in the assessment of potential acquisition opportunities. On July 11, subsequent to the end of the second quarter, the Company commenced the resource delineation program at Galshar. To August 9, a total of six diamond and 14 poly-crystalline diamond (PCD) holes, totalling 2,172 metres have been completed over the Galshar deposit area, with two additional PCD holes remaining. The diamond holes were cored and samples selected for analysis. The PCD holes were not cored but were tested with downhole geophysics consisting of natural gamma, density, resistivity, and calliper which results in the identification of the coal seam. A total of 1961 meters of downhole geophysics has been complete to date. Final results of the coal sample analysis and interpretation of the geophysical logs is pending.

Energy Project - Uranium

Erdene holds five licenses specifically for uranium exploration in south eastern Mongolia totaling 92,263 hectare. All of the licenses are registered in the name of Erdene Mongol or Erdene Energy, both of which are wholly owned by the Company. Two of these licenses were acquired from Gallant Minerals Ltd and are subject to a 1% NSR Royalty, which can be reduced to 0.5% in certain circumstances by making certain payments (refer to section 1.02).

Pursuant to an agreement dated June 14, 2005, between the Company and International Uranium Corporation ("IUC") (now Denison Mines Corp.), IUC has the option to earn a 65% interest in the

uranium minerals on the properties by spending a minimum of \$6 million over a four-year period and by meeting other obligations. All necessary funds for uranium exploration were covered by IUC as per the terms of the joint venture agreement. IUC's focus is on sandstone-hosted deposits that can be mined using the "In Situ Leach" ("ISL") method. Successful ISL pilot plant testing was completed previously by IUC.

The 2006 exploration program was managed by IUC who initiated an extensive reconnaissance rotary drill program to evaluate the uranium potential of a number of the Galshar block of Licenses as well as on the Yant and Tsagaan Del Licenses. Interesting results were returned from the Ikh Het depression (western Galshar area) where one hole intersected 0.01% to 0.02% uranium over 7 metres at a depth of 7 to 14 metres and another intersected 0.01% to 0.02% uranium over 5 metre at a depth of 20 metres. A decision to follow up the anomalous results returned on four licenses is under consideration.

North American Projects

The Company's North American project portfolio includes two notable industrial mineral projects as well as a 25% interest in the Donkin coal project (pursuant to an agreement entered into on October 26, 2006, see section 1.02). The industrial mineral opportunities include the Sparta Kaolin project in Georgia, U.S., which is operated by J.M. Huber Corporation, and the Granite Hill (Maddox) Aggregate project, a royalty project in the southeast U.S. managed by Rinker Materials Corporation.

Donkin Coal Project

Erdene is a 25% joint venture partner in the Donkin Coal Alliance with Xstrata Coal Donkin Limited (Xstrata Coal Donkin). The Donkin Coal Alliance was formed to secure the rights to the Donkin coal project and to explore, assess, study and, if feasible, develop the high-grade Donkin coal resource. The Donkin Coal Project is located in Cape Breton, Nova Scotia, proximal to deep water ideal for seaborne shipping into the major markets on North America's east coast.

A 200 million tonne portion of the Donkin coal resource, considered to have very good thermal and metallurgical qualities, is targeted in the initial development planned. The project is well located to serve domestic and Eastern U.S. markets. Approximately \$100 million was spent on previous work that included the construction of two 3.5-kilometre access tunnels.

During the second quarter, the Company received an independent technical report on the Donkin Coal resource from McElroy Bryan Geological Services Pty Ltd (MBGS). The report included a compilation of all historical information on the Donkin Coal project and an updated model of the deposit. The report identified an indicated resource of 227Mt (million metric tons) and an inferred resource of 254Mt of "High Volatile A Bituminous Coal" within the confines of the Donkin coal resource block. MBGS was established in 1970 and provides independent resource appraisals, technical reviews and due-diligence reports to the coal mining industry and financial institutions within Australia and overseas.

During the quarter the dewatering and the tunnel clearing and refurbishing program was ongoing. By early August 2007 the tunnel access program was nearing completion with the base of the tunnels cleared to the 3,100 metre mark and the tunnel roof now exposed to the ceiling of the Harbour seam at the end of the 3,500 metre long twin tunnels. Extensive testing of the Harbour seam will take place via a 10,000 metre in-seam drilling program that will be initiated once access to the coal face is completed. Areas of focus for the next stage of the project include:

- Underground drilling program to better define structure, gas regime and greenhouse gas footprint and associated strategies;
- Engineering and design for the product transportation alternatives which include delivery to the domestic market via rail and to the export market either via rail through the Sydney International Pier or via a newly constructed berth near the Donkin Mine site;
- Underground design inclusive of equipment scoping;
- Detailed operating costs assessments;
- Product specification and marketing factors;
- Environmental assessment approval conditions for the project; and,
- Capital cost estimates to be improved via detailed engineering.

Sparta Kaolin Project

One of the assets acquired through the Kao clay merger is a large primary kaolin resource in Georgia, U.S.A. Due to an aggressive exploration and acquisition program by Kao clay in the late 1990s, Erdene now controls a large high brightness primary clay resource through its subsidiary, Sparta Kaolin Corporation. The Company's in-ground, "premium" quality, primary kaolin resource in Georgia amounts to 27.4 million tons. For the project's development stage, Kao clay partnered with industry leader Huber Engineered Materials (Huber), a subsidiary of J.M. Huber Corporation, a diversified multi-national company and one of the world's largest kaolin producers.

In October 2003, Kao clay entered into an agreement with Huber for prepaid tonnage of crude kaolin. Huber conducted a due diligence evaluation program of the Sparta kaolin resource and performed an extensive product development program. This led to the successful commercialization of a light-weight coater product, in late 2004. Commercial production by Huber from Kao clay's primary kaolin deposits began in 2005 under the product name HuberPrime™, a high quality light-weight coater product.

The company continues to work with Huber and other third parties to identify products and markets to increase utilization of the raw material and therefore increase revenues and volumes mined and produced.

Granite Hill (Maddox) Project

The Company has referred to this Georgia, USA, property as the Maddox project, naming it after a former owner of the property. Rinker Materials Corporation ("Rinker"), who have been granted an exclusive right by the Company to mine, process, and sell aggregate from the property have renamed the project 'Granite Hill', the historical name for the property. The sale of all aggregate is subject to an industry competitive royalty payable to the Company. The Granite Hill project is being developed as a granite quarry, primarily to serve the southeastern US markets by rail. Rinker is a major global company and one of the largest suppliers of construction aggregates in the southeast U.S. Granite Hill has an estimated start-up production of one million tonnes of granite aggregate per year with a design capacity of four million tonnes. Based on current production projections, the Granite Hill quarry would have a lifespan of at least 20 years.

Rinker has designed a quarry mining plan, processing plant and facilities, and produced an environmental impact plan. Rinker has also acquired additional land adjacent to the Granite Hill property to secure rail access to the site. During the second quarter mine permitting work was ongoing and has

entered the final Federal and State approval stages with no impediments to approval anticipated. Issuance of the mining permit is expected during 2007. The construction phase is expected to be completed nine to twelve months thereafter. Rinker is responsible for fully funding the development program.

1.14 Disclosure Controls and Procedures

The Company's Chief Executive Officer and Chief Financial Officer are responsible for establishing and maintaining the Company's disclosure controls and procedures (as defined in Multilateral Instrument 52-109, Certification of Disclosure in Issuers' Annual and Interim Filings). The Chief Executive Officer and Chief Financial Officer, after evaluating the effectiveness of the design and operation of the Company's disclosure controls and procedures as of June 30, 2007, have concluded that the Company's disclosure controls and procedures were adequate and effective to ensure that material information relating to the Company and its consolidated subsidiaries required to be disclosed in the Company's reports filed or submitted under the Multilateral Instrument would have been known to them.

1.15 Outlook

The Company continues to be optimistic about the potential demonstrated by its principal and early stage resource properties. Success from the efforts of the Company's 2007 exploration program on any of its properties will result in an expanded program on the relevant property or properties relative to the significance of the results. Conversely, if anticipated results are not forthcoming on a particular property, a disciplined review and evaluation program will be in place to ensure expenditures are scaled back where management feels they may not be warranted.

1.16 Qualified Person

J. Christopher Cowan, P.Eng., serves as the qualified person under National Instrument 43-101 and supervises all of the Company's exploration programs. Samples are assayed at SGS Laboratory in Ulaanbaatar, Mongolia or Perth Australia, Central Geological Laboratory in Ulaanbaatar or ALS Chemex in Vancouver, Canada. In addition to internal checks by SGS Laboratory, Central Geological Laboratory and ALS Chemex, the Company incorporates a QA/QC sample protocol utilizing prepared standards, sample splits and duplicates.

1.17 Other Information

Additional information regarding the Company is available on SEDAR at www.sedar.com and on the Company's website at www.erdene.com.