



Xanadu Mines Ltd

ACN 114 249 026

Half Year Financial Report

December 2011

CORPORATE DIRECTORY

Board of Directors:

Brian Thornton *Executive Chairman*

Rod Williams *Executive Director*

Ganbayar Lkhagvasuren *Non-Executive Director*

Ron Heeks *Non-Executive Director*

Robert Westphal *Non-Executive Director*

Hannah Badenach *Non-Executive Director (Appointed 4 October 2011)*

Roger Perry *Non-Executive Director (Resigned 7 November 2011)*

Company Secretaries:

Brendan Evans *(Appointed 4 July 2011)*

Roger Perry *(Resigned 4 July 2011)*

Richard Pillinger *(Resigned 4 July 2011)*

Management:

Dr. Andrew Stewart *Manager Mongolia & Chief Geologist*

Registered Office Australia:

Suite 4, Level 2

66 Oxford Street

Darlinghurst, NSW 2010, Australia

Telephone: +612 9332 4332

Facsimile: +612 9332 3269

Email: info@xanadumines.com

Website: www.xanadumines.com

Registered Office Mongolia:

2nd Khoroo, AOS Street

Military Town, Bayanzurkh District

Ulaanbaatar, Mongolia

Telephone: +976 11 5011 0211

Share Registry:

Computershare Investor Services Pty Ltd

Level 3, 60 Carrington Street

Sydney, NSW 2000, Australia

Auditors

Ernst & Young

680 George Street

Sydney, NSW 2000, Australia

Solicitors - Australia

Baker & McKenzie

Level 27, AMP Centre

50 Bridge Street

Sydney, NSW 2000, Australia

Solicitors - Mongolia

Anand & Batzaya Advocates

10F Metro Business Centre

Sukhbaatar Street

Sukhbaatar District

Ulaanbaatar 210646, Mongolia

Stock Exchange Listing

Xanadu Mines Ltd shares are listed on the Australian Stock Exchange (ASX: XAM)

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Chairman's Report

HIGHLIGHTS FOR THE SIX MONTH PERIOD TO 31 DECEMBER 2011

- Discovery of coking coal at Nuurstei as part of the Xanadu Noble Alliance (Xanadu 50%, Noble 50%) with initial coal wash results indicative of a premium coking coal.
- Key milestone for the Galshar project with the establishment of a JORC coal resource of 170 Mt, and the application for a 30-year mining licence (Xanadu 100%).
- A 30-year mining licence granted for the Khar Tarvaga thermal coal deposit (Xanadu 100%).
- Acquisition of the Khavtsgait coking coal project in Northern Mongolia by the Xanadu Noble Alliance.
- Scout Drilling commenced at the Javkhlant metallurgical coal project on the Chinese Border, as part of the Xanadu Noble Alliance.
- Detailed geophysics program completed at the Sharchuluut porphyry copper project (Xanadu 100%).
- Amgalant and Argalant Uul porphyry copper-gold exploration joint venture established.
- Drilling at the Elgen-Zos-Suug epithermal gold projects (Xanadu 80%).
- A\$19.7 million cash balance at 31 December 2011 to fund exploration and pursue new opportunities.
- An experienced team of geologists and technical support personnel totalling 32 is employed by Xanadu in Mongolia.

COAL PROJECTS

Ekhgoviin Chuluu LLC - Noble Joint Venture (Xanadu 50%)

The Strategic Alliance with Noble Group continues to explore for and acquire high priority coking coal opportunities in Mongolia. This program has targeted areas of significant known coal resources and focused on green field exploration opportunities identified via information synthesis and geological mapping.

Ekhgoviin Chuluu (EC) has three exploration projects in Mongolia, all of which are focused on coking coal (Nuurstei, Javkhlant and Khavtsgait).

(a) Nuurstei

The Nuurstei Project, which was the first project of the Xanadu Noble Strategic Alliance ("EC"), covers an area of more than 3,000ha and is located in a newly identified coking coal province in northern Mongolia. EC committed to spend US\$1.5m on exploration as part of its earn in on the project (now completed) and could move to 80% following the establishment of a resource compliant with the JORC code.

The initial raw coal washability results are encouraging and are indicative of a premium quality coking coal at the project.

(b) Javkhlant

Javkhlant is an exciting exploration project which has the potential to host a large premium coking and /or thermal coal deposit of Permian and Carboniferous age very close to the Chinese market. The project is located in the south western Gobi Altai Province of Mongolia, approximately 22km from the Burgastai border crossing point into China and only 200km from the Chinese rail network at the industrial centre of Hami. Reconnaissance mapping and exploration has identified numerous coal and carbonaceous mudstone subcrops, containing coal fragments, which occur over a strike of approximately 40km. Exploration drilling commenced in late 2011 and will continue in April 2012.

The joint venture vehicle Ekhgoviin Chuluu LLC ("EC") can earn up to 80% of the Javkhlant coal exploration licence by meeting various spending commitments over two years, including completion of a JORC code compliant resource.

Chairman's Report (continued)

(c) Khavtsgait

The acquisition of the Khavtsgait coal project was completed during the last quarter of 2011. The project is located in the Khuvsgul province of northern Mongolia, approximately 60km east of the Province centre of Moron and the Nuurstei project, and 230km west from the established rail spur at Erdenet. Under the terms of the agreement EC has acquired 100% of the Khavtsgait exploration licence (15142X), which covers approximately 2,869ha. The highly prospective exploration licence overlies an early to middle Mesozoic aged coal-bearing sedimentary basin; similar aged basins in northern Mongolia (such as the Ovoot Coking Coal Project owned by ASX-listed Aspire Mining Limited) are known to host potentially world-class premium hard coking coal deposits.

Initial exploration indicates the early to middle Mesozoic stratigraphic sequence at Khavtsgait is consistent with that at the Nuurstei coking coal project located approximately 60km to the west. Logantek Mongolia LLC recently completed a ground magnetic survey on the most prospective area within the licence, totalling 40 contiguous-line-kilometres. This data will assist drill targeting in 2012.

Thermal Coal Projects (Xanadu 100%)

(a) Galshar Coal Project (Xanadu 100% subject to a royalty to Erdene Mongol XXX)

Xanadu has successfully defined a thermal coal resource of 170Mt to JORC classification code at Galshar. The coal at Galshar is suitable for power generation and proven coal to liquids ("CTL") technologies. In conjunction with Xanadu's Khar Tarvaga thermal coal project, the addition of Galshar represents a 51% increase in the Company's JORC compliant coal resources inventory to 497Mt.

Xanadu has a 100% interest in this project in the Dornogovi Province of eastern Mongolia, 65km from a rail spur at the Bor Undor fluorite mine, which connects to the Trans Mongolian Rail system to China, and lies only 200km from the China border. The Company has also commenced the necessary permit process for a Mining Licence. During the period, Xanadu decided to seek offers of interest in the Galshar thermal coal project. The decision came after a strategic review recommended increased focus on Xanadu's coking coal and copper/gold opportunities in Mongolia.

(b) Khar Tarvaga

The Mineral Authority of Mongolia has granted a mining licence (MV16871) for the Khar Tarvaga Coal Project, covering a total area of 83.5km² (8,350.76ha). The Khar Tarvaga Project mining licence has been granted for an initial term of 30 years with an option for two 20-year extensions, providing for a total of 70 years of mining operations.

Xanadu has a 100% interest in the Khar Tarvaga Project, which is located in the Tov Province in Eastern Mongolia approximately 150km south east of Ulaanbaatar. The project is very well situated, being proximal to both rail, road and power infrastructure, approximately 36km from the Trans-Mongolian railway.

Drilling by Xanadu at the Khar Tarvaga Project has identified a significant sub-bituminous coal resource in excess of 327Mt, of which more than half is indicated status and described as being amenable to mining by open cut methods.

The coal within the Khar Tarvaga mining licence is a sub-bituminous, high volatile coal suitable for mine mouth power generation and potentially gasification as part of a CTL or synthetic natural gas ("SNG") production facility. During the period, Xanadu decided to seek offers of interest in the Khar Tarvaga thermal coal project. The decision came after a strategic review recommended increased focus on Xanadu's coking coal and copper/ gold opportunities in Mongolia.

COPPER PROJECTS (100% Xanadu owned)

(a) Sharchuluut Uul Copper-Gold Porphyry Project

Sharchuluut is Xanadu's 100% owned copper-gold porphyry project in the northern province of Bulgan, 40km northwest, and along strike from the world-class Erdenet porphyry copper-molybdenum deposit. The Company has just completed a detailed geophysics program at this project which will assist in drill targeting a porphyry copper system within the 488km² exploration license. Exploration drilling is scheduled to commence in April 2012.

Chairman's Report (continued)

(b) Amgalant and Argalant Uul Copper Porphyry Projects

Finalisation of a farm-in agreement on the Amgalant and Argalant Uul porphyry copper-gold exploration licences occurred during the last quarter of 2011. Both exploration licences are located in the South Gobi region of southern Mongolia, approximately 460km south east of Ulaanbaatar. They are in the central part of the highly prospective south Gobi porphyry belt, approximately 110km northeast of the world-class Oyu Tolgoi Cu-Au Project, and proximal to the large undeveloped Tsagaan Suvarga copper molybdenum deposit. The southern Mongolian Palaeozoic magmatic belt hosts most of the known porphyry and intrusion-related mineralisation in the South Gobi.

Xanadu Mines can earn up to 80% of the Amgalant and Argalant Uul exploration licences by meeting various spending commitments over two years. A substantial exploration effort will commence in the current field season on the two exploration licences given the potential to discover a large buried porphyry deposit.

GOLD PROJECTS

(a) Elgen-Zos-Suug Gold Project (Xanadu 80%)

Elgen-Zos-Suug is Xanadu's joint venture epithermal gold project in south east Mongolia and is located within the Dornogovi Province, approximately 680km south-southeast of Ulaanbaatar. This advanced exploration project is strategically situated 30km north of the Chinese border and the Mandal border crossing. An intensive drilling campaign is planned in 2012.

CORPORATE

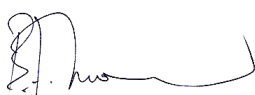
The Annual General Meeting was held on 8 November 2011 and all resolutions were passed by members. Ms Hannah Badenach of Noble Group was appointed as a Non-Executive Director on 4 October 2011, and Mr Roger Perry resigned as a Director on 7 November 2011.

Following a strategic review of the operations of the Company, Xanadu has decided to increase the focus on its highly prospective coking coal and copper/gold opportunities in Mongolia. Consequently the Board has decided to seek offers of interest in the Galshar and Khar Tarvaga Projects and is currently conducting an active sale program on these two projects.

Xanadu has continued to invest in its Mongolian exploration team which now totals 32 personnel, this will enhance our chances of success across both the coking coal and copper-gold disciplines in 2012 and lay the foundations for future growth.

The World Bank has predicted that the Mongolian economy will experience growth of 14.9% in 2012, which is six times the rate of the global economy and almost double the growth rate of China. Furthermore, the Business Council of Mongolia has projected that 2013 growth in the nation will exceed 25%. Mongolia was ranked as the second best equity market globally in 2011 and experienced a record level of foreign investment.

As at 31 December 2011, Xanadu had A\$19.7 million cash on hand to fund exploration and pursue new opportunities in this burgeoning and exciting market.



Brian Thornton
Chairman

Competent Person Statement

Information on the Company's exploration results is sourced from information compiled by Mr Rod Williams. Mr Williams is an employee of Xanadu Mines and is a Member of the Australasian Institute of Mining and Metallurgy and has sufficient experience in the areas being reported on to qualify as the "Competent Person" as defined in the 2004 Edition of the "Australasian Code for the Reporting of Mineral Resources and Reserves". Mr Williams consents to the information in the form and context in which it appears.

Directors' Report

The directors submit their report for the half year ended 31 December 2011.

DIRECTORS

The names of the Company's directors in office during the half year and until the date of this report are as follows. Directors were in office for this entire period unless otherwise stated.

Brian F Thornton (Executive Chairman)
Rodney E Williams (Non-Executive Director)
Ronald Heeks (Non-Executive Director)
Ganbayar Lkhagvasuren (Executive Director)
Robert G Westphal (Non-Executive Director)
Hannah Badenach (Non-Executive Director) (appointed 4 October 2011)
Roger J Perry (resigned 7 November 2011)

DIVIDENDS

No dividends have been paid during the period (2010: nil) and no dividend is recommended.

PRINCIPAL ACTIVITIES

The principal activity of the group is exploration in Mongolia for gold, copper and coal.

REVIEW OF OPERATIONS

During the period the Company focused on exploration on its existing licences, the acquisition of additional licence areas, a review of existing exploration data with a view to progressing the Company's exploration plans in the 2012 field season.

The loss after tax of the consolidated entity for the half year ended 31 December 2011 was \$5,846,633 (31 December 2010: \$1,367,001) of which \$4.38 million relates to an adjustment to the carrying amount of the Hutag Uul and Hust Uul licenses. The Company had approximately \$19.7 million in cash at 31 December 2011.

SIGNIFICANT CHANGES IN THE STATE OF AFFAIRS

Significant changes in the state of affairs of the Company during the period were:

- Discovery of coking coal at Nuurstei as part of the Xanadu Noble Alliance (Xanadu 50%, Noble 50%);
- Key milestone for the Galshar project with the establishment of a JORC coal resource of 170Mt, and the application for a 30 year mining license (Xanadu 100%);
- A 30-year mining license granted for the Khar Tarvaga thermal coal deposit (Xanadu 100%);
- Acquisition of the Khavtsgait coking coal project in Northern Mongolia by the Xanadu Noble Alliance;
- Xanadu made an impairment adjustment downwards of \$4.38 million in relation to the carrying value of its Hutag Uul and Hust Uul tenements following a detailed review of the Company's licenses in Mongolia;
- Xanadu decided to seek offers of interest in the Khar Tarvaga and Galshar thermal coal projects. The decision came after a strategic review recommended increased focus on Xanadu's coking coal and copper and gold opportunities in Mongolia; and
- An experienced team of geologists and technical support personnel totalling 32 is employed by Xanadu in Mongolia.

Directors' Report (continued)

SIGNIFICANT EVENTS AFTER THE BALANCE DATE

On 23 January 2012, Xanadu Mines Ltd announced the finalisation of a farm-in agreement on the Amgalant and Argalant Uul porphyry copper-gold exploration licenses. Under the terms of the agreement, Xanadu can earn up to 80% of the exploration licenses by meeting certain spending commitments over 2 years. Initially as consideration for the licenses, Xanadu issued 1,396,990 Xanadu shares to the vendor on 23 January 2012.

On 3 February 2012, Xanadu Mines Ltd issued 1,500,000 incentive options to Chief Financial Officer and Company Secretary Mr Brendan Evans under the terms of the Xanadu Employee Share Option Plan.

LIKELY DEVELOPMENTS AND EXPECTED RESULTS

The directors foresee that the 2012/2013 financial year will focus on increased exploration at the Company's various coal and base metal projects in Mongolia. The Company is also committed to identifying and pursuing new investment opportunities in Mongolia to maximise shareholder value.

ENVIRONMENTAL REGULATION AND PERFORMANCE

Entities in the extractive industries incur rehabilitation obligations which are imposed under contractual or licensing arrangements, or by legislation, or are undertaken on the basis of entity policy or in accordance with industry best practice. While the Company's activities are still in the exploration phase, no provision for rehabilitation work has been recognised in relation to expenditures for dismantling and removing structures, rehabilitating quarries and mines, dismantling operating facilities and restoring affected areas expected to be incurred as the level of disturbance to date has been minimal. However, the Company recognises that such remedial work will be required should mining operations commence and is committed to the adoption of industry best practice in regard to any remediation required. The Company has adopted a Code of Environmental Practice that is implemented on all field operations in which the company engages.

ROUNDING

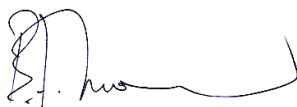
The amounts contained in this report and in the financial report have been rounded to the nearest \$1,000 (unless otherwise stated) under the option available to the Company under ASIC Class Order 98/0100. The Company is an entity to which the Class Order applies.

AUDITOR'S INDEPENDENCE DECLARATION

The auditor's independence declaration is included on page 17.

Signed in accordance with a resolution of the directors.

On behalf of the Directors



Brian Thornton

Chairman

Sydney

Dated: 6 March 2012

Consolidated Statement of Comprehensive Income for the Half-Year Ended 31 December 2011

	Notes	31-Dec-11 \$'000s	31-Dec-10 \$'000s
Revenue	4(a)	435	111
Total revenue		435	111
Other income / (expenses)	4(b)	487	194
Depreciation and amortisation expense		(44)	(20)
Administrative expenses	4(c)	(2,349)	(1,652)
Deferred exploration and evaluation expenditure written off	4(d)	(4,376)	-
Loss before income tax		(5,847)	(1,367)
Income tax expense		-	-
Loss after income tax		(5,847)	(1,367)
Other comprehensive loss, net of tax		-	-
Total comprehensive loss for the period		(5,847)	(1,367)
Loss per share for loss attributable to the ordinary equity holders of the parent			
Basic loss per share (cents per share)		(3.13)	(1.12)
Diluted loss per share (cents per share)		(3.13)	(1.12)

The above Statement of Comprehensive Income should be read in conjunction with the accompanying notes.

Consolidated Statement of Financial Position as at 31 December 2011

	Notes	31-Dec-11 \$'000s	30-Jun-11 \$'000s
ASSETS			
Current assets			
Cash and cash equivalents	5	19,665	23,586
Prepayments and other assets		182	5
Other receivables		1,333	1,347
		21,180	24,938
Assets classified as held for sale	6	8,028	-
Total current assets		29,208	24,938
Non current assets			
Deferred exploration and evaluation costs	6	9,035	18,483
Property, plant and equipment		1,116	1,094
Intangible assets		4	5
Total non current assets		10,155	19,582
Total assets		39,363	44,520
LIABILITIES			
Current liabilities			
Trade and other payables		2,647	2,441
Total current liabilities		2,647	2,441
Total liabilities		2,647	2,441
Net assets		36,716	42,079
Equity			
Equity attributable to equity holders of the parent			
Issued capital	7	53,594	53,594
Reserves	8	5,988	5,336
Accumulated losses		(23,255)	(17,408)
Parent entity interest		36,327	41,522
Non-controlling interest		389	557
Total equity		36,716	42,079

The above Statement of Financial Position should be read in conjunction with the accompanying notes.

Consolidated Statement of Cash Flows for the Half-Year Ended 31 December 2011

	31-Dec-11 \$'000s	31-Dec-10 \$'000s
Cash flows from operating activities		
Payments to suppliers and employees	(1,087)	(1,360)
Net cash flows used in operating activities	(1,087)	(1,360)
Cash flows from investing activities		
Interest received	289	111
Acquisition of exploration and evaluation assets	-	(2,076)
Purchase of property, plant and equipment and intangible assets	(65)	(122)
Loans to other entities	-	(181)
Deferred exploration and evaluation costs	(3,545)	(1,150)
Net cash flows used in investing activities	(3,321)	(3,418)
Cash flows from financing activities		
Proceeds from issue of shares (net of share issue costs)	-	28,334
Net cash flows from financing activities	-	28,334
Net increase/(decrease) in cash and cash equivalents	(4,408)	23,556
Net foreign exchange differences	487	(330)
Cash and cash equivalents at beginning of period	23,586	677
Cash and cash equivalents at end of period	19,665	23,903

The above Statement of Cash Flows should be read in conjunction with the accompanying notes.

Consolidated Statement of Changes in Equity for the Half-Year Ended 31 December 2011

	Attributable to equity holders					Total \$'000s
	Issued capital \$'000s	Share-based compensation reserve \$'000s	Acquisition reserve \$'000s	Accumulated losses \$'000s	Non- Controlling Interest \$'000s	
Balance as at 1 July 2010	15,445	6,791	-	(13,253)	-	8,983
Adjustment for restatement	-	(1,702)	-	-	-	(1,702)
Restated total equity at the beginning of the financial period	15,445	5,089	-	(13,253)	-	7,281
Total comprehensive loss for the period	-	-	-	(1,367)	-	(1,367)
Transactions with owners in their capacity as owners						
Shares issued for the period	30,642	-	-	-	-	30,642
Cost of share issue	(2,308)	-	-	-	-	(2,308)
Share-based payments	-	247	-	-	-	247
Balance as at 31 December 2010	43,779	5,336	-	(14,620)	-	34,495
Balance as at 1 July 2011	53,594	5,336	-	(17,408)	557	42,079
Total comprehensive loss for the period	-	-	-	(5,847)	-	(5,847)
Transactions with owners in their capacity as owners						
Share-based payments	-	484	-	-	-	484
Asset acquisition reserve	-	-	168	-	(168)	-
Balance as at 31 December 2011	53,594	5,820	168	(23,255)	389	36,716

The above Statement of Changes in Equity should be read in conjunction with the accompanying notes.

Notes to the Consolidated Financial Statements

FOR THE HALF YEAR ENDED 31 DECEMBER 2011

1. CORPORATE INFORMATION

Xanadu Mines Ltd (“the Company”) was incorporated on 12 May 2005. The financial report of the Company for the half year ended 31 December 2011 was authorised for issue in accordance with a resolution of the directors on 3 March 2012.

Xanadu Mines Ltd is a company limited by shares incorporated in Australia.

The nature of the operations and principal activities of the Group are described in the directors’ report.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

(a) Basis of preparation

This general purpose condensed financial report for the half year ended 31 December 2011 has been prepared in accordance with AASB 134 *Interim Financial Reporting* and the *Corporations Act 2001*. The half year financial report does not include all notes of the type normally included within the annual financial report and therefore cannot be expected to provide an understanding of the financial performance, financial position and financing and investing activities of the consolidated entity as the full financial report.

It is recommended that the half year financial report be read in conjunction with the annual report for the year ended 30 June 2011 and considered together with any public announcements made by Xanadu Mines Ltd during the half year ended 31 December 2011 in accordance with continuous disclosure obligations of the ASX listing rules.

(b) Significant Accounting Policies

The accounting policies and methods of computation are the same as those adopted in the most recent annual financial report.

No new standards or interpretations have been issued (either effective or not yet effective) which are considered to have a material impact on the financial statements or performance of the Company.

3. SEGMENT INFORMATION

The consolidated entity operates predominantly in the minerals exploration sector. The principal activity of the consolidated entity is exploration for gold, copper and coal. The consolidated entity classifies these activities under a single operating segment; the Mongolian exploration projects.

Regarding the exploration operating segment, the Chief Operating Decision Maker (determined to be the Board of Directors) receives information on the exploration expenditure incurred. This information is disclosed in Note 6 of the half year financial report. No segment revenues are disclosed as each exploration tenement is not at a stage where revenues have been earned. Furthermore, no segment costs are disclosed as all segment expenditure is capitalised, with the exception of expenditure written off. Refer to Note 6.

Notes to the Consolidated Financial Statements (continued)

FOR THE HALF YEAR ENDED 31 DECEMBER 2011

4. REVENUE AND EXPENSES

	31-Dec-11 \$'000s	31-Dec-10 \$'000s
(a) Revenue		
Finance income	430	111
Other income	5	-
Total revenue	435	111
(b) Other income / (expense)		
Net foreign currency gains/ (losses)	487	(99)
Cost recovery	-	9
Discount recognised on business combination	-	284
Total other income / (expense)	487	194
(c) Administrative expenses		
Share based payments	484	247
Salaries and directors fees	1,115	425
Administration expense	750	980
Total administrative expenses	2,349	1,652
(d) Deferred exploration and evaluation expenses written off		
Deferred exploration written off – Hutag and Hust	4,376	-
Total deferred exploration and evaluation expenses written off	4,376	-

5. CASH AND CASH EQUIVALENTS

	31-Dec-11 \$'000s	30-Jun-11 \$'000s
Cash and cash equivalents are comprised of the following:		
Cash at bank and in hand	19,665	23,586
	19,665	23,586

Notes to the Consolidated Financial Statements (continued)

FOR THE HALF YEAR ENDED 31 DECEMBER 2011

6. DEFERRED EXPLORATION AND EVALUATION COSTS (NON-CURRENT)

	31-Dec-11 \$'000s	30-Jun-11 \$'000s
Costs incurred in respect of current mining leases (net of costs expensed)	9,035	18,483
Reconciliation of movement in deferred exploration and evaluation expenditure in current period		
Balance at 1 July 2011	18,483	
Additions	2,956	
Expenditure written off during the year	(4,376)	
	17,063	
Transferred to assets classified as held for sale	(8,028)	
Balance at 31 December 2011	9,035	

During the period, Xanadu decided to seek offers of interest in the Khar Tarvaga and Galshar thermal coal projects. The decision came after a strategic review recommended increased focus on Xanadu's coking coal and copper/gold opportunities in Mongolia. As a result these assets have been transferred to assets classified as held for sale. There is no gain or loss impact in the income statement in relation to assets held for sale.

The expenditure written off during the year relates to the impairment of capitalised exploration expenditure on the Hutag Uul and Hust Uul tenement, to reduce the carrying value to the recoverable amount.

7. CONTRIBUTED EQUITY

	31-Dec-11 \$'000s	30-Jun-11 \$'000s
(a) Issued and paid up capital		
Ordinary shares fully paid (186,989,835 shares on issue)	53,594	53,594

(b) Options

At the balance date there were 24,240,000 options on issue. Details of these are as follows:

	Number of options	Exercise Price	Expiry Date
Unlisted options	14,000,000	\$0.50	31-Dec-14
ESOP options	5,240,000	\$0.50	19-Dec-14
ESOP options	1,000,000	\$0.60	30-Jun-16
ESOP options	1,000,000	\$1.20	30-Jun-16
ESOP options	1,000,000	\$1.80	30-Jun-16
ESOP options	1,000,000	\$0.70	31-Dec-14
ESOP options	1,000,000	\$1.00	31-Dec-14
	<u>24,240,000</u>		

The value of the equity-settled share options granted is estimated as at the date of grant using a Binomial Model taking into account the terms and conditions upon which the options were granted.

Notes to the Consolidated Financial Statements (continued)

FOR THE HALF YEAR ENDED 31 DECEMBER 2011

The following table lists the inputs to the models used when granting options during the half year ended 31 December 2011:

	1 July 2011			11 November 2011	
Number of options	1,000,000	1,000,000	1,000,000	1,000,000	1,000,000
Expected volatility (%)	58.13%	58.13%	58.13%	64.42%	64.42%
Risk-free interest rate (%)	4.76%	4.76%	4.76%	3.79%	3.79%
Expected life of option (years)	4.0	4.0	4.0	3.1	3.1
Exercise price	\$0.60	\$1.20	\$1.80	\$0.70	\$1.00
Vesting date	1 Jul 12	1 Jul 12	1 Jul 12	11 Nov 11	11 Nov 11
Grant date share price	\$0.515	\$0.515	\$0.515	\$0.44	\$0.44

The expected life of the options is based on historical data and is not necessarily indicative of exercise patterns that may occur. The expected volatility reflects the assumption that historical volatility is indicative of future trends, which may also not necessarily be the actual outcome.

8. RESERVES

	31-Dec-11 \$'000s	30-Jun-11 \$'000s
Share-based compensation reserve	5,820	5,336
Asset acquisition reserve	168	-
Total reserves	5,988	5,336

Reconciliation of movement in share-based compensation reserve in current period

Balance at 1 July 2011	5,336
Expense arising from amortisation of equity settled share based payment transactions	484
Balance at 31 December 2011	5,820

9. EVENTS AFTER BALANCE SHEET DATE

On 23 January 2012, Xanadu Mines Ltd announced the finalisation of a farm-in agreement on the Amgalant and Argalant Uul porphyry copper-gold exploration licenses. Under the terms of the agreement, Xanadu can earn up to 80% of the exploration licenses by meeting certain spending commitments over 2 years. Initially as consideration for the licenses, Xanadu issued 1,396,990 Xanadu shares to the vendor on 23 January 2012.

On 3 February 2012, Xanadu Mines Ltd issued 1,500,000 incentive options to Chief Financial Officer and Company Secretary Mr Brendan Evans under the terms of the Xanadu Employee Share Option Plan.

Other than the above, no events have occurred subsequent to balance date which would materially affect the operations or financial results of the Company.

10. COMMITMENTS AND CONTINGENCIES

There has been no change in commitments and contingent liabilities since the last annual reporting date.

Directors' Declaration

In accordance with a resolution of the directors of Xanadu Mines Ltd, I state that:

In the opinion of the directors:

- (a) the financial statements and notes of the consolidated entity are in accordance with the *Corporations Act 2001*, including:
 - (i) giving a true and fair view of the financial position as at 31 December 2011 and its performance, for the half year ended on that date of the consolidated entity; and
 - (ii) complying with Accounting Standard AASB 134 *Interim Financial Reporting* and the *Corporations Regulations 2001*; and
- (b) there are reasonable grounds to believe that the Company will be able to pay its debts as and when they become due and payable.

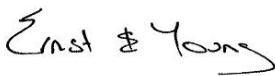
On behalf of the Board

A handwritten signature in blue ink, appearing to read 'B. Thornton', with a long horizontal flourish extending to the right.

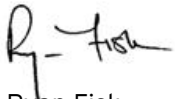
Brian Thornton
Chairman

Auditor's Independence Declaration to the Directors of Xanadu Mines Ltd

In relation to our review of the financial report of Xanadu Mines Ltd for the half-year ended 31 December 2011, to the best of my knowledge and belief, there have been no contraventions of the auditor independence requirements of the Corporations Act 2001 or any applicable code of professional conduct.

A handwritten signature in black ink that reads 'Ernst & Young'.

Ernst & Young

A handwritten signature in black ink that reads 'R. Fisk'.

Ryan Fisk
Partner
Sydney

6 March 2012

To the members of Xanadu Mines Ltd

Report on the Half-Year Financial Report

Report on the financial report

We have reviewed the accompanying half-year financial report of Xanadu Mines Ltd, which comprises the statement of financial position as at 31 December 2011, the statement of comprehensive income, statement of changes in equity and statement of cash flows for the half-year ended on that date, notes comprising a summary of significant accounting policies and other explanatory information, and the directors' declaration of the consolidated entity. The consolidated entity comprises the company and the entities it controlled at the half-year end or from time to time during the half-year.

Directors' Responsibility for the Half-Year Financial Report

The directors of the company are responsible for the preparation of the half-year financial report that gives a true and fair view in accordance with Australian Accounting Standards and the *Corporations Act 2001*. The directors are also responsible for such internal controls that the directors determine are necessary to enable the preparation of the half-year financial report that is free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express a conclusion on the half-year financial report based on our review. We conducted our review in accordance with Auditing Standard on Review Engagements ASRE 2410 *Review of Interim and other Financial Reports Performed by the Independent Auditor of the Entity*, in order to state whether, on the basis of the procedures described, we have become aware of any matter that makes us believe that the financial report is not in accordance with the *Corporations Act 2001*; and complying with Accounting Standard AASB 134 *Interim Financial Reporting* and the *Corporations Regulations 2001*. As the auditor of Xanadu Mines Ltd and the entities it controlled during the half-year, ASRE 2410 requires that we comply with the ethical requirements relevant to the audit of the annual financial report.

A review of a half-year financial report consists of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with Australian Auditing Standards and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Independence

In conducting our review we have met the independence requirements of the *Corporations Act 2001*. We have given to the directors of the company a written Auditor's Independence Declaration, a copy of which is included in the directors' report.

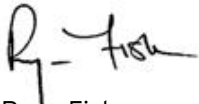
Conclusion

Based on our review, which is not an audit, we have not become aware of any matter that makes us believe that the half-year financial report of Xanadu Mines Ltd is not in accordance with the *Corporations Act 2001*, including:

- i giving a true and fair view of the consolidated entity's financial position as at 31 December 2011 and of its performance for the half-year ended on that date; and
- ii complying with Accounting Standard AASB 134 *Interim Financial Reporting* and the *Corporations Regulations 2001*.

A handwritten signature in black ink that reads 'Ernst & Young'.

Ernst & Young

A handwritten signature in black ink that reads 'R. Fisk'.

Ryan Fisk
Partner
Sydney

6 March 2012