

# **Migao Corporation**

**Interim Consolidated Financial Statements  
Second Quarter, Fiscal 2007  
Ended March 31, 2007**

**(Unaudited)**

# Migao Corporation

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*For the three and six month periods ended March 31, 2007 and 2006*

*(Unaudited)*

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# Migao Corporation

## Interim Consolidated Balance Sheets

(in Canadian dollars)

	March 31, 2007 (Unaudited)	September 30, 2006 (Audited)
<b>Assets</b>		
<b>Current assets</b>		
Cash and cash equivalents	\$ 25,567,799	\$ 16,315,835
Accounts receivable	5,285,257	4,435,769
Prepayments, deposits and other receivables (note 2)	9,259,601	4,891,382
Inventory (note 3)	10,935,624	3,947,193
	51,048,281	29,590,179
<b>Plant and equipment (note 5)</b>	23,449,089	13,464,499
<b>Construction in progress</b>	2,209,236	6,203,587
<b>Land use rights (note 6)</b>	13,091,910	7,828,983
	\$ 89,798,516	\$ 57,087,248
<b>Liabilities</b>		
<b>Current liabilities</b>		
Bank indebtedness	\$ -	\$ 1,410,000
Accounts payable and accrued liabilities (note 6)	6,673,023	5,213,106
Customer deposits	1,973,942	2,965,101
Due to related party (note 4)	1,169,841	530,672
Income taxes payable	197,680	109,308
	10,014,486	10,228,187
<b>Shareholders' equity</b>		
Share capital (note 7)	46,484,887	28,729,591
Contributed surplus (note 7)	9,913,447	2,955,592
Retained earnings (note 9)	21,068,014	15,320,755
Accumulated other comprehensive income (loss) (note 10)	2,317,682	(146,877)
	79,784,030	46,859,061
<b>Commitments (note 12)</b>		
<b>Subsequent events (note 13)</b>		
	\$ 89,798,516	\$ 57,087,248

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

Approved on behalf of the Board of Directors

Signed by "Guocai Liu" \_\_\_\_\_

Director

Signed by "Keith Attoe" \_\_\_\_\_

Director

# Migao Corporation

## Interim Consolidated Statements of Operations and Retained Earnings

(in Canadian dollars)

(Unaudited)

	For the three months ended		For the six months ended	
	March 31, 2007	March 31, 2006	March 31, 2007	March 31, 2006
<b>Revenues</b>	\$ 27,711,766	\$ 15,100,436	\$ 49,443,160	\$ 27,488,786
<b>Cost of goods sold</b>	21,431,246	10,790,204	38,488,985	20,477,266
<b>Gross profit</b>	6,280,520	4,310,232	10,954,175	7,011,520
<b>Operating expenses</b>				
Selling	1,334,573	770,542	2,314,318	1,233,639
General and administrative	1,018,055	366,737	1,763,884	770,225
Professional and consulting	178,834	68,620	390,698	219,823
Stock-based compensation	245,055	-	495,555	-
	2,776,517	1,205,899	4,964,455	2,223,687
<b>Income from operations</b>	3,504,003	3,104,333	5,989,720	4,787,833
Other income	34,492	2,041	85,566	4,454
<b>Income before income taxes</b>	3,538,495	3,106,374	6,075,286	4,792,287
Provision for income taxes	200,199	156,939	328,027	156,939
<b>Net income for the period</b>	3,338,296	2,949,435	5,747,259	4,635,348
<b>Retained earnings, beginning of period</b>	17,729,718	8,409,106	15,320,755	6,723,193
<b>Retained earnings, end of period</b>	\$ 21,068,014	\$ 11,358,541	\$ 21,068,014	\$ 11,358,541
<b>Income per share: (note 8)</b>				
Basic	\$ 0.10	-	\$ 0.19	-
Diluted	\$ 0.10	-	\$ 0.19	-
<b>Weighted average number of common shares outstanding: (note 8)</b>				
Basic	31,859,414	-	30,491,712	-
Diluted	32,726,894	-	30,875,196	-

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

## Migao Corporation

### Interim Consolidated Statements of Comprehensive Income

(in Canadian dollars)

(Unaudited)

	<u>For the three months ended</u>		<u>For the six months ended</u>	
	March 31, 2007	March 31, 2006	March 31, 2007	March 31, 2006
<b>Net income for the period</b>	\$ 3,338,296	\$ 2,949,435	\$ 5,747,259	\$ 4,635,348
Other comprehensive income (loss), net of tax:				
Unrealized gains (losses) on translating financial statements of self-sustaining foreign operations	(351,019)	177,697	2,464,560	244,903
<b>Comprehensive income</b>	\$ 2,987,277	\$ 3,127,132	\$ 8,211,819	\$ 4,880,251

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

# Migao Corporation

## Interim Consolidated Statements of Cash Flows

(in Canadian dollars)

(Unaudited)

	For the three months ended		For the six months ended	
	March 31, 2007	March 31, 2006	March 31, 2007	March 31, 2006
<b>Cash flows from operating activities</b>				
Cash receipts from customers	\$ 33,043,461	\$ 12,177,064	\$ 47,624,720	\$ 24,300,578
Cash paid to suppliers and employees	(29,823,262)	(11,094,593)	(49,776,126)	(22,673,950)
Income taxes paid	(134,228)	-	(239,654)	-
Interest received	18,489	2,041	47,357	4,454
Interest paid	(95,911)	-	(95,911)	-
	3,008,549	1,084,512	(2,439,614)	1,631,082
<b>Cash flows from investing activities</b>				
Purchase of plant and equipment	(1,294,472)	(193,594)	(4,553,501)	(433,774)
Construction in process	(938,621)	(334,485)	(2,257,875)	(2,784,922)
Payments for land use rights	(2,399,886)	(883,001)	(4,920,124)	(1,296,984)
	(4,632,979)	(1,411,080)	(11,731,500)	(4,515,680)
<b>Cash flows from financing activities</b>				
Proceeds from (payment of) bank loan	(4,926,900)	1,456,000	(1,410,000)	1,456,000
Advances from related parties, net	280,878	252,224	615,482	1,634,808
Issuance of common shares, net	23,016,491	-	23,016,491	-
Proceeds from exercise of underwriters' compensation options	28,500	-	180,830	-
Proceeds from exercise of warrants	1,020,275	-	1,020,275	-
Advances from director	-	-	-	20,546
	19,419,244	1,708,224	23,423,078	3,111,354
<b>Increase in cash and cash equivalents</b>	17,794,814	1,381,656	9,251,964	226,756
<b>Cash and cash equivalents, beginning of period</b>	7,772,985	1,300,671	16,315,835	2,455,571
<b>Cash and cash equivalents, end of period</b>	\$ 25,567,799	\$ 2,682,327	\$ 25,567,799	\$ 2,682,327
<b>Cash and cash equivalents consist of:</b>				
Cash on hand	\$ 18,249,038	\$ 2,682,327		
Term deposit	40,000	-		
Bank notes	7,278,761	-		
	\$ 25,567,799	\$ 2,682,327		

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

# Migao Corporation

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## Notes to Interim Consolidated Financial Statements

*For the three and six month periods ended March 31, 2007 and 2006*

*(in Canadian dollars)*

*(Unaudited)*

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### 1. Nature of Operations and Basis of Presentation

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#### Nature of Operations

Migao Corporation (“the Company” or “Migao”), through its wholly owned Subsidiaries, is a manufacturer of specialty potash-based fertilizers, produced at its three operational facilities in the People’s Republic of China (“PRC”).

#### The Company

Migao holds 100% of the issued and outstanding capital of H.K. Migao Industry Limited (“HK Migao”), which in turns holds 100% of the issued and outstanding capital of Sichuan Migao Chemical Fertilizer Industry Co. Ltd. (“Sichuan”), Guangdong Migao Chemical Co. Ltd. (“Guangdong”), Liaoning Migao Chemical Co. Ltd. (“Liaoning”), Migao Chemical Industry (Shanghai) Co. Ltd. (“Shanghai”) and Migao Chemical (Changchun) Co. Ltd. (“Changchun”) (collectively, the “Subsidiaries”).

#### Basis of Presentation

These unaudited interim consolidated financial statements (the "financial statements") have been prepared by management in accordance with Canadian generally accepted accounting principles ("GAAP") and include the accounts of the Company and its subsidiaries in the PRC. These interim financial statements have been prepared by the management of the Company using the same accounting policies and methods as the most recently audited financial statements of Migao. These financial statements do not contain all disclosures required by Canadian GAAP for annual financial statements, and accordingly, the financial statements should be read in conjunction with the audited financial statements of Migao for the year ended September 30, 2006. Interim results are not necessarily indicative of the results expected for the fiscal year. Certain comparative figures have been reclassified to conform to the current period's presentation.

#### Accounting policy change

Effective October 1, 2006, the Company implemented the new CICA accounting sections: 3855 (Financial Instruments – Recognition and Measurement), 3865 (Hedges), and 1530 (Comprehensive Income). These new accounting policy changes have been implemented prospectively with no restatement of comparative financial statements, except as noted below.

Comprehensive income includes net income and other comprehensive income. It is defined as the change in equity (net assets) of a company during the period from transactions and other events and circumstances from non-owner sources. It includes all changes in equity during the period except those resulting from investments by owners and distributions to owners. The only item included in other comprehensive income is the foreign currency translation of self-sustaining foreign operations. As a result, the previously recorded currency translation account on the consolidated balance sheets’ shareholders’ equity section has been eliminated and included as “accumulative other comprehensive income” in shareholders’ equity. Furthermore, the gain (or loss) from translating the Company’s self-sustaining foreign operations is now recorded as other comprehensive income. Prior years financial statements have been restated to reflect this change. The Company’s earnings per share presented on the consolidated statements of income is based upon its net income and not comprehensive income.

The adoption of sections 3855 and 3865 had no impact on the Company’s financial statements.

## Migao Corporation

### Notes to Interim Consolidated Financial Statements

For the three and six month periods ended March 31, 2007 and 2006

(in Canadian dollars)

(Unaudited)

## 2. Prepayments, Deposits, and Other Receivables

	March 31, 2007 (Unaudited)	September 30, 2006 (Audited)
Prepayments for raw materials	\$ 6,162,216	\$ 2,689,982
Prepayments for construction costs	374,748	1,416,103
Prepayment for transportation services	69,186	1,390
Deposits for the supply of utilities	29,098	252,816
VAT receivable	693,992	347,177
Other receivables and deposits	1,930,361	183,914
	<b>\$ 9,259,601</b>	<b>\$ 4,891,382</b>

## 3. Inventory

	March 31, 2007 (Unaudited)	September 30, 2006 (Audited)
Raw materials	\$ 9,843,216	\$ 3,670,084
Finished goods	1,007,823	213,129
Packing materials	84,585	63,980
	<b>\$ 10,935,624</b>	<b>\$ 3,947,193</b>

## 4. Related Party Balances and Related Party Transactions

At the end of the periods, the Company had related party balances as follows:

	March 31, 2007 (Unaudited)	September 30, 2006 (Audited)
Amount due to:		
Liaoning Yongcheng Economic and Trade Development Co. Ltd. ("LYEDC")	<b>\$ 1,169,841</b>	<b>\$ 530,672</b>

Migao and LYEDC are related due to common control. Expenses paid by LYEDC, on behalf of the Company, in the amount of \$1,114,089 are included in the balance due to related party. The balance of \$55,752 represents interest payable on the long-term portion of the advances, up to the date of conversion to equity on June 7, 2006. These amounts are non-interest bearing and due on demand.

## Migao Corporation

### Notes to Interim Consolidated Financial Statements

For the three and six month periods ended March 31, 2007 and 2006

(in Canadian dollars)

(Unaudited)

## 5. Plant and Equipment

	March 31, 2007 (Unaudited)		
	Cost	Accumulated Amortization	Net Book Value
Buildings and improvements	\$ 9,628,529	\$ 548,757	\$ 9,079,772
Machinery and equipment	15,503,968	1,834,388	13,669,580
Vehicles	748,453	257,343	491,110
Office equipment	304,640	96,013	208,627
	<b>\$ 26,185,590</b>	<b>\$ 2,736,501</b>	<b>\$ 23,449,089</b>

  

	September 30, 2006 (Audited)		
	Cost	Accumulated Amortization	Net Book Value
Buildings and improvements	\$ 6,708,599	\$ 352,976	\$ 6,355,623
Machinery and equipment	7,812,532	1,202,871	6,609,661
Vehicles	477,459	184,680	292,779
Office equipment	273,120	66,684	206,436
	<b>\$ 15,271,710</b>	<b>\$ 1,807,211</b>	<b>\$ 13,464,499</b>

Amortization expense for the three and six months period ended March 31, 2007 was \$468,347 and \$821,138 (March 31, 2006 - \$201,765 and \$411,554), respectively.

## Migao Corporation

### Notes to Interim Consolidated Financial Statements

For the three and six month periods ended March 31, 2007 and 2006

(in Canadian dollars)

(Unaudited)

## 6. Land Use Rights

	<b>March 31, 2007 (Unaudited)</b>	September 30, 2006 (Audited)
Land use rights	\$ 13,271,725	\$ 7,859,142
Less: accumulated amortization	179,815	30,159
	<b>\$ 13,091,910</b>	<b>\$ 7,828,983</b>

As of March 31, 2007, the Company had thirteen land leases from the Chinese government with terms of fifty to seventy years.

Amortization expense for the three and six months period ended March 31, 2007 was \$147,524 and \$149,717 (March 31, 2006 - \$2,171 and \$4,566), respectively, and are included in general and administrative expenses.

As of March 31, 2007, the Company had not obtained the land use right certificates for nine of the land leases and approximately \$2 million has been accrued as the balance due on the issuance of the certificates. It is common practice in the PRC that the land use right certificates are only issued when the government has serviced the land ready for construction.

Under the PRC law, land use rights can be revoked and the tenants can be forced to vacate at any time when re-development of the land is in the public interest.

# Migao Corporation

## Notes to Interim Consolidated Financial Statements

For the three and six month periods ended March 31, 2007 and 2006

(in Canadian dollars)

(Unaudited)

## 7. Share Capital

(a) **Authorized:**

Unlimited common shares without par value.

(b) (i) **Issued common shares**

	<b>Number of Shares</b>	<b>Amount</b>
Balance – September 30, 2006	29,111,921	\$ 28,729,591
Issued on exercise of underwriters' compensation options (i)	53,449	152,330
Fair value of underwriters' compensation options (i)		58,259
Fair value of warrants issued (i)		(24,854)
Issued on exercise of underwriters' compensation options (ii)	10,000	28,500
Fair value of underwriters' compensation options (ii)	-	10,900
Fair value of warrants issued (ii)	-	(12,900)
Exercise of warrants (iii)	275,750	1,020,275
Fair value of warrants exercised (iii)	-	181,995
Issued pursuant to a private placement at \$4.15 per share (iv)	6,025,000	25,003,750
Share issuance costs (iv)	-	(1,987,259)
Private placement warrants (iv)	-	(5,512,875)
Underwriters' compensation options (iv)	-	(1,162,825)
<b>Balance - March 31, 2007</b>	<b>35,476,120</b>	<b>\$ 46,484,887</b>

(i) Each of the 53,449 underwriters' compensation options exercised consists of 1 common share and ½ common share purchase warrants. They were valued at \$1.09 per option. The warrants issued on the exercise of these options are valued at \$0.93 per warrant with the following assumptions: dividend yield 0%; risk-free interest rate 4.08%; expected volatility 66%; and expected life of 1.6 years.

(ii) Each of the 10,000 underwriters' compensation options exercised consists of 1 common share and ½ common share purchase warrants. They were valued at \$1.09 per option. The warrants issued on the exercise of these options are valued at \$2.58 per warrant with the following assumptions: dividend yield 0%; risk-free interest rate 4.10%; expected volatility 106%; and expected life of 1.3 years.

(iii) During the quarter, 275,750 of the common share purchase warrants issued in relation to the private placement financing on May 18, 2006 were exercised at \$3.70 per share.

## Migao Corporation

### Notes to Interim Consolidated Financial Statements

For the three and six month periods ended March 31, 2007 and 2006

(in Canadian dollars)

(Unaudited)

## 7. Share Capital (continued)

### (b) (i) Issued common shares (continued)

(iv) On February 22, 2007 (the “closing date”), the Company completed a private placement of 6,025,000 units priced at \$4.15 per unit with each unit consisting of one common share and one-half of one common share purchase warrant. Each whole warrant entitles the holder to acquire one common share on payment of \$5.30 per common share within two years from the closing date. The fair value of the warrants issued with the private placement was estimated using the Black-Scholes option pricing model on the closing date of the private placement to be \$1.83 per warrant. Assumptions used to determine the value of the warrants were: dividend yield 0%; risk-free interest rate 4.11%; expected volatility 106%; and expected life 2 years. In addition to the agency fee of \$1,750,263 paid in cash, the Company granted compensation options entitling the agents to acquire 301,250 compensation units at price of \$4.15 per unit until two years from the closing date. Each compensation unit comprises of one common shares and one-half warrant. Each whole warrant entitles the agent to acquire one common share on payment of \$5.30 per common share within two years from the closing date. The fair value of the compensation options granted with the private placement was estimated using the Black-Scholes option pricing model on the closing date of the private placement to be \$3.86 per option. Assumptions used to determine the value of the compensation options were: dividend yield 0%; risk-free interest rate 4.11%; expected volatility 106%; and expected life 2 years.

### (c) Contributed surplus

	<b>Amount</b>
Balance – September 30, 2006	\$ 2,955,592
Exercise of underwriters’ compensation options	(69,159)
Fair value of warrants issued on the exercise of underwriters’ compensation options	37,754
Stock-based compensation expense	495,555
Fair value of warrants exercised	(181,995)
Private placement warrants	5,512,875
Underwriters’ compensation options	1,162,825
<b>Balance - March 31, 2007</b>	<b>\$ 9,913,447</b>

## Migao Corporation

### Notes to Interim Consolidated Financial Statements

For the three and six month periods ended March 31, 2007 and 2006

(in Canadian dollars)

(Unaudited)

## 7. Share Capital (continued)

### (d) Stock options

Under the Company's stock option plan, the Company may grant stock options to directors, senior officers, employees and advisors and is authorized to issue options to acquire up to 10% of the issued and outstanding shares of the Company. The board of directors or such other persons designated by the board administers the plan and determines the vesting and terms of each award.

The following table summarizes the activity of the Company's stock option plan.

	Shares	Weighted average exercise price
Outstanding – September 30, 2006	1,165,000	\$ 2.85
Granted during the period	-	-
<b>Outstanding - March 31, 2007</b>	<b>1,165,000</b>	<b>\$ 2.85</b>

The following table summarizes the weighted average information about the outstanding stock options.

Exercise price	Number outstanding	Weighted average remaining contractual life (years)	Number exercisable
\$ 2.85	1,165,000	4.13	NIL

During the year ended September 30, 2006, 1,165,000 options were issued to the employees and directors of the Company. Each option entitles the holder to purchase one common share of the Company at a price of \$2.85 per common share. These options have vesting periods of up to three years and an exercise period of up to five years, expiring on May 18, 2011. The fair value of the options issued was estimated using the Black-Scholes option pricing model on the date of issue to be \$1.40 per option. Assumptions used to determine the value of the options were: dividend yield 0%; risk-free interest rate 4%; expected volatility 66%; and expected life of 5 years. Stock-based compensation expense for the quarter ended March 31, 2007 was \$245,055 (2006 – NIL).

### (e) Warrants

As at March 31, 2007, the following share purchase warrants were outstanding:

September 30, 2006	Issued	Exercised	Expired	March 31, 2007	Exercise price	Expiry Date
3,181,500	31,725	275,750	-	2,937,475	\$ 3.70	May 18, 2008
-	3,012,500	-	-	3,012,500	\$ 5.30	February 22, 2009
3,181,500	3,044,225	275,750	-	5,949,975		

## Migao Corporation

### Notes to Interim Consolidated Financial Statements

For the three and six month periods ended March 31, 2007 and 2006

(in Canadian dollars)

(Unaudited)

## 7. Share Capital (continued)

### (f) Underwriters' Compensation Options

As at March 31, 2007, the following underwriters' compensation options were outstanding:

September 30, 2006 (outstanding and exercisable)	Issued	Exercised	Expired	March 31, 2007 (outstanding and exercisable)	Exercise price	Weighted average remaining contractual life (years)
445,410	-	63,449	-	381,961	\$ 2.85	1.13
-	301,250	-	-	301,250	\$ 4.15	1.90
445,410	301,250	63,449	-	683,211		

## 8. Income per Share

The Company completed its first private placement financing and its common shares were listed on TSX Venture Exchange in May 2006. Prior to such, the Company was a private company and the number of shares outstanding was very small in comparison to after the first private placement. Comparison of income per share figures to periods before May 2006 is therefore not meaningful. The income per share and weighted average number of common shares outstanding amounts for the periods ended March 31, 2006 are therefore not presented.

## 9. Retained Earnings

Under the laws of the PRC, all wholly owned foreign investment entities have to set aside a portion of their net income each year as a general reserve fund until the fund has reached 50% of the entity's paid in capital. The Company is also required to set aside a portion of net income as an expansion fund. These funds are allowed to be distributed to shareholders at the time of winding up. The fund accumulated by the Company as at March 31, 2007 was \$2,188,319 (RMB 14,676,854; September 30, 2006 – RMB 3,153,714).

## 10. Accumulated Other Comprehensive Income

	Unrealized gains (losses) on translating financial statements of self-sustaining foreign operations
Balance – September 30, 2006	\$ (146,877)
Unrealized foreign currency translation gains during the period	2,464,559
<b>Balance – March 31, 2007</b>	<b>\$ 2,317,682</b>

# **Migao Corporation**

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## **Notes to Interim Consolidated Financial Statements**

*For the three and six month periods ended March 31, 2007 and 2006*

*(in Canadian dollars)*

*(Unaudited)*

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### **11. Segmented Information**

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The Company has one operating segment, being the production and sale of specialty potash-based fertilizer, along with their associated by-products. All of Company's assets and operations are located in the PRC.

### **12. Commitments**

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Purchase commitments for raw materials and supplies in the amount of \$26.8 million (RMB 180 million) exist as of March 31, 2007. These contracts are entered into in the normal course of business.

Commitments on capital expenditures in the amount of \$0.96 million (RMB 6.4 million) exist as of March 31, 2007. These contracts are entered into in the normal course of business.

### **13. Subsequent Events**

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Subsequent to the period end, the following transactions were completed:

On April 25, 2007, Toronto Stock Exchange ("TSX") conditionally approved the listing of the common shares of the Company. On May 8, 2007, TSX issued its final approval. On May 10, 2007, the common shares of the Company commenced trading on the TSX.

Subsequent to March 31, 2007 and as of May 14, 2007, 453,606 warrants and 90,000 underwriters' compensation options were exercised for gross proceeds of \$1,934,842.