

Migao Corporation

**Consolidated Financial Statements
September 30, 2008 and 2007**

Migao Corporation

Table of Contents

September 30, 2008 and 2007

	Page
Auditor's Report	1
Consolidated Financial Statements	
Balance Sheets	2
Statements of Operations and Retained Earnings	3
Statements of Comprehensive Income	4
Statements of Cash Flows	5 - 6
Notes to Financial Statements	7 - 27

MOORE STEPHENS COOPER MOLYNEUX LLP
CHARTERED ACCOUNTANTS

8th Floor, 701 Evans Avenue
Toronto, Ontario
Canada M9C 1A3

Telephone: (416) 626-6000
Facsimile: (416) 626-8650
Web Site: www.mscom.ca

Auditors' Report

To the Shareholders of
Migao Corporation

We have audited the consolidated balance sheets of Migao Corporation as at September 30, 2008 and 2007 and the consolidated statements of operations and retained earnings, comprehensive income and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at September 30, 2008 and 2007 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

Signed: "MSCM LLP"

**Chartered Accountants
Licensed Public Accountants**

Toronto, Ontario
December 3, 2008

Migao Corporation

Consolidated Balance Sheets

September 30, 2008 and 2007

(in thousands of Canadian dollars)

	2008	2007
Assets		
Current assets		
Cash and cash equivalents	\$ 16,850	\$ 17,453
Accounts receivable	8,598	6,373
Prepayments, deposits and other receivables (note 3)	38,724	10,614
Inventory (note 4)	78,430	19,101
Due from related party (note 5)	36	-
Income taxes receivable	526	1,159
Future income tax assets (note 12)	60	-
	143,224	54,700
Plant and equipment (note 6)	34,303	20,518
Construction in progress	10,272	5,972
Land use rights (note 7)	21,077	18,367
Future income tax assets (note 12)	518	470
	\$ 209,394	\$ 100,027
Liabilities		
Current liabilities		
Bank loans (note 8)	\$ 13,855	\$ 4,578
Accounts payable and accrued liabilities (note 7)	10,902	9,958
Customer deposits	14,671	3,451
Due to related party (note 5)	-	45
Income taxes payable	1,168	-
Future income tax liabilities (note 12)	420	-
	41,016	18,032
Shareholders' equity		
Share capital (note 9)	94,608	54,013
Contributed surplus (note 9)	7,891	8,551
Retained earnings (note 10)	53,830	26,527
Accumulated other comprehensive income (loss) (note 11)	12,049	(7,096)
	168,378	81,995
Commitments (note 15)		
	\$ 209,394	\$ 100,027

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

Approved on behalf of the Board of Directors

Signed by "Guocai Liu"

Director

Signed by "Keith Attoe"

Director

Migao Corporation

Consolidated Statements of Operations and Retained Earnings

For the years ended September 30, 2008 and 2007

(in thousands of Canadian dollars, except per share amounts)

	2008	2007
Revenues	\$ 187,028	\$ 101,804
Cost of goods sold (note 6)	141,508	80,264
Gross profit	45,520	21,540
Operating expenses		
Selling	6,334	4,030
General and administrative (note 6 and 7)	6,618	4,285
Stock-based compensation (note 9)	1,888	908
Pre-operating costs	419	368
Finance costs	461	288
	15,720	9,879
Income from operations	29,800	11,661
Other income	180	202
Gain on sale of non-operating subsidiary (note 1)	98	-
Income before income taxes	30,078	11,863
Provision for income taxes (note 12)	2,775	657
Net income for the period	27,303	11,206
Retained earnings, beginning of period	26,527	15,321
Retained earnings, end of period	\$ 53,830	\$ 26,527
Income per share: (note 13)		
Basic	\$ 0.67	\$ 0.33
Diluted	\$ 0.63	\$ 0.32
Weighted average number of common shares outstanding: (note 13)		
Basic	40,658,089	33,479,987
Diluted	43,099,724	35,074,923

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

Migao Corporation

Consolidated Statements of Comprehensive Income

For the years ended September 30, 2008 and 2007

(in thousands of Canadian dollars)

	2008		2007
Net income	\$ 27,303	\$	11,206
Other comprehensive income (loss), net of tax:			
Unrealized gains (losses) on translating financial statements of self-sustaining foreign operations	19,145		(6,949)
Comprehensive income	\$ 46,448	\$	4,257

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

Migao Corporation

Consolidated Statements of Cash Flows

For the years ended September 30, 2008 and 2007
(in thousands of Canadian dollars)

	2008	2007
Cash flows from operating activities		
Net income	\$ 27,303	\$ 11,206
Items not affecting cash:		
Amortization	2,471	1,943
Stock-based compensation	1,888	908
Gain on sale of non-operating subsidiary	(98)	-
Future income taxes	312	(470)
Changes in non-cash working capital items:		
Accounts receivable	(1,089)	(2,076)
Prepayments, deposits, and other receivables	(19,301)	(4,930)
Inventory	(51,818)	(16,789)
Accounts payable and accrued liabilities	(608)	5,452
Customer deposits	9,798	590
Income taxes payable	1,586	(1,350)
	(29,556)	(5,516)
Cash flows from investing activities		
Purchase of plant and equipment	(6,724)	(12,386)
Construction in progress	(12,857)	(145)
Refund on land use rights	1,866	-
Payments for land use rights	(3,321)	(8,927)
Proceeds from sale of non-operating subsidiary	1,143	-
	(19,893)	(21,458)
Cash flows from financing activities		
Proceeds from bank loans	12,750	7,830
Repayment of bank loans	(4,915)	(4,530)
Repayment on advances from related party	(45)	(569)
Issuance of common shares, net	26,478	22,993
Payment on behalf of related party	33	-
Proceeds from exercise of underwriters' compensation options	454	1,565
Proceeds from exercise of warrants	10,116	5,127
Proceeds from exercise of stock options	898	285
	45,769	32,701

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

Migao Corporation

Consolidated Statements of Cash Flows - continued

For the years ended September 30, 2008 and 2007

(in thousands of Canadian dollars)

	2008	2007
Foreign exchange gain (loss) on cash held in foreign currency	\$ 3,077	\$ (4,590)
Increase in cash and cash equivalents	(603)	1,137
Cash and cash equivalents, beginning of period	17,453	16,316
Cash and cash equivalents, end of period	\$ 16,850	\$ 17,453
Cash and cash equivalents consist of:		
Cash on hand	\$ 15,728	\$ 14,399
Term deposit	40	40
Bank notes	1,082	3,014
	\$ 16,850	\$ 17,453

Total interest paid during the year ended September 30, 2008 was \$455 (RMB 3.2 million) (September 30, 2007 - \$274 or RMB 1.9 million). Total tax paid during the year ended September 30, 2008 was \$695 (RMB 4.9 million) (September 30, 2007 - \$489 or RMB 4.0 million). Total tax refunded during the year ended September 30, 2008 was \$1,331 (RMB 9.3 million) (September 30, 2007 nil).

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

Migao Corporation

Notes to Consolidated Financial Statements

September 30, 2008 and 2007

(in thousands of Canadian dollars, except per share amounts)

1. Nature of Operations

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 four 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 ("H.K. Migao"), which in turn holds 100% of the issued and outstanding capital of Sichuan Migao Chemical Fertilizer Industry Co., Ltd. ("Sichuan Migao"), Guangdong Migao Chemical Co., Ltd. ("Guangdong Migao"), Liaoning Migao Chemical Co., Ltd. ("Liaoning Migao"), Migao Chemical Industry (Shanghai) Co., Ltd. ("Shanghai Migao"), Migao Chemical (Changchun) Co., Ltd. ("Changchun Migao"), and Migao Chemical (Tianjin) Co., Ltd. ("Tianjin Migao") (collectively, the "Subsidiaries").

During the year, the Company disposed of Migao Business Hotel Limited, a non-operating subsidiary of Guangdong Migao, for a gross proceeds of \$1,143 (RMB 8.0 million) and a gain of \$98 (RMB 0.7 million).

2. Significant Accounting Policies

Basis of presentation

These 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.

Cash equivalents

The Company considers cash equivalents to be cash and highly liquid investments with original maturities of three months or less.

Inventory

Raw materials are valued at the lower of cost and replacement cost. Finished goods are valued at the lower of cost and net realizable value. The cost of finished goods comprises direct materials and, where applicable, direct labor costs and overhead costs. Cost is determined using the weighted-average method. Net realizable value represents the anticipated selling price less all further costs for distribution.

Plant and equipment

Plant and equipment are recorded at cost. Amortization is provided over the expected useful lives of the plant and equipment with a 10% residual value using the following methods and annual rates:

Building and improvements	-	10 to 20 years straight-line
Machinery and equipment	-	10 years straight-line
Vehicles	-	5 years straight-line
Office equipment	-	5 years straight-line

Migao Corporation

Notes to Consolidated Financial Statements

September 30, 2008 and 2007

(in thousands of Canadian dollars, except per share amounts)

2. Significant Accounting Policies - continued

Construction in progress

Construction in progress represents properties under construction and is stated at cost. Construction in progress is not amortized until such time as the assets are completed and put into operational use.

Land use rights

Land use rights are recorded at cost and are amortized over 50 years, which are the terms of the land use rights set by the Chinese government.

Impairment of long-lived assets

Long-lived assets held for use are reviewed for impairment when events or changes in circumstances indicate that their carrying value may not be recoverable. When the carrying value is not recoverable from future cash flows on an undiscounted basis and the carrying value exceeds the assets' fair value, an impairment loss is recorded for the excess of carrying value over fair value.

Income taxes

The Company uses the liability method of accounting for income taxes. Under this method, income tax assets and liabilities are recognized for the future income tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Income tax assets and liabilities are measured using enacted or substantively enacted tax rates expected to apply to income in the years in which those temporary differences are expected to be recovered or settled. The effect of a change in tax rates on income tax assets and liabilities is reflected in operations in the period in which the change occurs. Valuation allowances are established when necessary to reduce future tax assets to the amount expected to be realized.

Income per share

Basic income per share is computed using the weighted average number of common shares outstanding during the year. Diluted income per share is computed giving effect to the potential dilution that would occur if securities or other contracts to issue common shares were exercised or converted to common shares using the treasury stock method, except when their effect would be anti-dilutive. The treasury stock method assumes that proceeds received from the exercise of stock options and warrants are used to repurchase common shares at the prevailing market rate.

Revenue recognition

Revenue is recognized when goods are shipped and all significant risks and rewards of ownership are passed to the customer with collection of revenue reasonably assured. Payments received in advance for orders that do not yet qualify for recognition under the Company's policies are recorded as customer deposits.

Pre-operating costs

All expenditures incurred prior to the commencement of commercial operations are expensed.

Migao Corporation

Notes to Consolidated Financial Statements

September 30, 2008 and 2007

(in thousands of Canadian dollars, except per share amounts)

2. Significant Accounting Policies - continued

Foreign exchange

The Company's functional currency is the Canadian dollar and the Subsidiaries' functional currency is the Chinese Renminbi ("RMB"). The accounts of the Subsidiaries are translated into Canadian dollars using the current rate method. Under this method, assets and liabilities are translated at the year end rate of exchange. Revenues and expenses are translated into Canadian dollars at the average rate of exchange for the period. Exchange gains and losses from foreign currency translations are recorded in shareholders' equity as other comprehensive income.

Financial instruments

The Company has classified its cash and cash equivalents as held-for-trading, which are measured at fair value. Accounts receivable, other receivables, and due from related party are classified as loans and receivables, which are measured at amortized cost. Payables, accruals, and due to related party are classified as other financial liabilities, which are measured at amortized cost. Bank loans are classified as loans and are measured at amortized cost.

Measurement uncertainty

The preparation of the financial statements in conformity with Canadian GAAP requires management to make estimates and assumptions that affect the reported amount of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the year. Significant items subject to such estimates and assumptions include the carrying amounts of plant and equipment, intangible assets, valuation allowances for receivables and inventories, and future income taxes. Actual results could differ from those estimates.

Comparative Figures

Certain comparative figures have been reclassified to conform to the presentation adopted in the current year.

Adoption of New Accounting Policies

Effective October 1, 2007, the Company adopted the following new accounting standards.

Capital Management

The new standard 1535 – Capital Disclosures requires the Company to disclose information about the Company's objectives, policies and processes for the management of its capital.

Financial Instruments – Disclosure and Presentation

The new standards 3862 – Financial Instruments – Disclosures and 3863 – Financial Instruments – Presentation require the disclosure of information with regards to the significance of financial instruments for the Company's financial position and performance and the nature and extent of risks arising from financial instruments to which the Company is exposed during the period and at the balance sheet date, and how the Company manages those risks.

Migao Corporation

Notes to Consolidated Financial Statements

September 30, 2008 and 2007

(in thousands of Canadian dollars, except per share amounts)

2. Significant Accounting Policies - continued

Recent Accounting Pronouncements

Inventories

In June 2007, the Canadian Institute of Chartered Accountants ("CICA") released new Handbook Section 3031 - Inventories, replacing Section 3030, effective for annual and interim periods for fiscal years beginning on or after January 1, 2008. This Section provides guidance on the determination of cost and its subsequent recognition as an expense, including any write-down to net realizable value. It also provides guidance on the cost formulas that are used to assign costs to inventories. The Company's consolidated results of operations and financial position are not materially affected by the new handbook section.

Goodwill and Intangible Assets

The CICA issued the new Handbook Section 3064 - Goodwill and intangible assets, which replaces Section 3062 - Goodwill and Other Intangible Assets and Section 3450 - Research and Development Costs. The new standard establishes revised standards for the recognition, measurement, presentation and disclosure of goodwill and intangible assets. The new standard also provides guidance for the treatment of preproduction and start-up costs and requires that these costs be expensed as incurred. The new standard applies to annual and interim financial statements relating to fiscal years beginning on or after October 1, 2008. The Company is already expensing its pre-operating cost and the impact of the other parts of this new handbook section on the consolidated financial statements cannot be determined until the transactions occur.

International Financial Reporting Standards ("IFRS")

In 2006, the Canadian Accounting Standards Board ("AcSB") published a new strategic plan that will significantly affect financial reporting requirements for Canadian companies. The AcSB strategic plan outlines the convergence of Canadian GAAP with IFRS over an expected five year transitional period. In February 2008 the AcSB announced that 2011 is the changeover date for publicly-listed companies to use IFRS, replacing Canadian GAAP for interim and annual financial statements relating to fiscal years beginning on or after January 1, 2011. The transition date of October 1, 2011 will require the restatement for comparative purposes of amounts reported by Migao for the year ended September 30, 2012. While the Company has begun assessing and reviewing the impact of IFRS, and engaged in professional development for its adoption in 2011, the financial reporting impact of the transition to IFRS cannot be reasonably estimated at this time.

3. Prepayments, Deposits, and Other Receivables

	2008	2007
Prepayments for raw materials	\$ 25,817	\$ 7,478
Prepayments for construction costs	5,485	904
Prepayments for transportation services	357	23
Prepayments for machinery	1,380	632
Deposits for the supply of utilities	224	151
Deposits on obtaining sales contracts	777	-
VAT receivable	3,711	583
Other receivables and deposits	973	843
	\$ 38,724	\$ 10,614

Migao Corporation

Notes to Consolidated Financial Statements

September 30, 2008 and 2007

(in thousands of Canadian dollars, except per share amounts)

4. Inventory

	2008	2007
Raw materials	\$ 66,313	\$ 13,931
Finished goods	11,795	1,075
Packing materials	124	90
Goods in transit	198	4,005
	\$ 78,430	\$ 19,101

5. Related Party Balances

At the end of the year, the Company had the following related party balances:

	2008	2007
Amount due from (to):		
Migao New Energy (Sichuan) Co. Ltd. ("MNEC")	\$ 36	\$ -
Liaoning Yongcheng Economic and Trade Development Co. Ltd. ("LYEDC")	-	(45)
	\$ 36	\$ (45)

During the year, the Company paid \$36 (September 30, 2007 - \$Nil) of land evaluation and business registration fees on behalf of MNEC. The Company also prepaid \$297 (September 30, 2007 - \$Nil) of import agency fees to Beijing Wei De Sen ("BWDS"). These transactions were in the normal course of business and were measured at the exchange amounts, which are the amounts agreed upon by the parties. In addition, the Company paid or accrued service fees of \$Nil (September 30, 2007 - \$Nil) for services performed by LYEDC. Because of the difficulty in determining the fair market value, the values of these contributed services were not recognized in the financial statements. Lastly, LYEDC has provided corporate guarantees on \$6,192 of the Company's short-term bank loans outstanding as of September 30, 2008.

MNEC, LYEDC, and BWDS are all controlled by an officer and director of Migao.

6. Plant and Equipment

	2008		
	Cost	Accumulated Amortization	Net Book Value
Buildings and improvements	\$ 20,772	\$ 1,630	\$ 19,142
Machinery and equipment	18,148	4,024	14,124
Vehicles	1,138	497	641
Office equipment	603	207	396
	\$ 40,661	\$ 6,358	\$ 34,303

Migao Corporation

Notes to Consolidated Financial Statements

September 30, 2008 and 2007

(in thousands of Canadian dollars, except per share amounts)

6. Plant and Equipment - continued

	2007		
	Cost	Accumulated Amortization	Net Book Value
Buildings and improvements	\$ 10,684	\$ 701	\$ 9,983
Machinery and equipment	11,984	2,181	9,803
Vehicles	794	289	505
Office equipment	338	111	227
	\$ 23,800	\$ 3,282	\$ 20,518

Amortization expense for the year ended September 30, 2008 was \$2,328 (September 30, 2007 - \$1,720) and is included in cost of goods sold and general and administrative expense.

During the year, Guangdong Migao and Sichuan Migao were approved by the local tax authority for tax credits totaling \$272 (RMB 1.8 million) (September 30, 2007 - \$1,383 or RMB 10.4 million) and \$105 (RMB 0.7 million) (September 30, 2007 - \$370 or RMB 2.8 million), respectively, on purchases of domestic equipment. Changchun Migao was approved by the local tax authorities for value-added tax refunds on purchases of domestic equipment of \$327 (RMB 2.2 million) (September 30, 2007 - \$Nil). These credits and value-added tax refunds were recorded as a reduction of the cost of the related equipment and the tax credits will be applied against profit taxes levied to subsidiaries.

7. Land Use Rights

	2008		2007	
Land use rights	\$	21,501	\$	18,597
Less: accumulated amortization		424		230
	\$	21,077	\$	18,367

As of September 30, 2008, the Company had fifteen land leases from the Chinese government with terms of fifty years.

Amortization expense for the year ended September 30, 2008 was \$143 (September 30, 2007 - \$224), and is included in general and administrative expense.

As of September 30, 2008, the Company had not obtained the land use right certificates for six of the land leases and approximately \$4.1 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 Consolidated Financial Statements

September 30, 2008 and 2007

(in thousands of Canadian dollars, except per share amounts)

8. Bank Loans

At September 30, 2008, the Company has short-term bank loans outstanding totaling \$13,855 (RMB 89.5 million) (September 30, 2007 - \$4,578 or RMB 34.5 million) for working capital purposes.

<u>Amount</u>	<u>Due Date</u>	<u>Interest Rate</u>	<u>Interest Rate at Year End</u>	<u>Secured by</u>
\$ 2,322	April 29, 2009	110% of prime rate in China ("PC")	8.217%	two land use rights
\$ 3,096	June 20, 2009	PC	7.47%	corporate guarantees from Sichuan Migao and LYEDC
\$ 3,096	June 25, 2009	PC	7.47%	corporate guarantees from Sichuan Migao and LYEDC
\$ 3,096	March 29, 2009	130% of PC	9.62%	one land use right and a building
\$ 1,239	August 13, 2009	110% of PC	8.217%	one land use right
<u>\$ 1,006</u>	August 18, 2009	110% of PC	8.217%	one land use right
\$ 13,855				

Total carrying value of the security was \$5,099 (RMB 32.9 million). Total interest paid during the year ended September 30, 2008 was \$455 (RMB 3.2 million) (September 30, 2007 - \$274 or RMB 1.9 million).

9. Share Capital

(a) **Authorized:**

Unlimited common shares without par value.

(b) **Issued common shares**

	Number of Shares	Amount
Balance - September 30, 2006	29,111,921	\$ 28,730
Issued on exercise of underwriters' compensation options (i)	514,860	1,565
Fair value of underwriters' compensation options (i)	-	655
Fair value of warrants issued (i)	-	(378)
Exercise of warrants (ii)	1,288,647	5,128
Fair value of warrants exercised (ii)	-	1,113
Issued pursuant to a private placement at \$4.15 per share (iii)	6,025,000	25,004
Share issuance costs (iii)	-	(2,011)
Fair value of warrants issued on private placement (iii)	-	(5,513)
Fair value of underwriters' compensation options issued (iii)	-	(705)
Exercise of stock options (iv)	100,000	285
Fair value of stock options exercised (iv)	-	140
Balance - September 30, 2007	37,040,428	\$ 54,013

Migao Corporation

Notes to Consolidated Financial Statements

September 30, 2008 and 2007

(in thousands of Canadian dollars, except per share amounts)

9. Share Capital - continued

(b) Issued common shares - continued	Number of Shares	Amount
Balance – September 30, 2007	37,040,428	\$ 54,013
Issued on exercise of underwriters' compensation options (v)	111,300	454
Fair value of underwriters' compensation options (v)	-	253
Fair value of warrants issued (v)	-	(93)
Exercise of warrants (vi)	2,615,133	10,116
Fair value of warrants exercised (vi)	-	2,048
Exercise of stock options (vii)	315,000	898
Fair value of stock options exercised (vii)	-	441
Issued pursuant to a private placement (viii)	3,593,750	28,750
Share issuance costs (viii)	-	(2,272)
Balance – September 30, 2008	43,675,611	\$ 94,608

(i) During the year ended September 30, 2007, a total of 514,860 underwriters' compensation options were exercised. They consisted of one common share and one-half common share purchase warrant. The fair value of these options were estimated using the Black-Scholes option pricing model at the grant date for a weighted average value of \$1.27 per option. The warrants issued on the exercise of these options had a weighted average fair value of \$1.47 per warrant with the following weighted average assumptions: dividend yield 0%; risk-free interest rate 4.52%; expected volatility 105%; and expected life of 1.09 years.

(ii) During the year ended September 30, 2007, a total of 1,288,647 of the common share purchase warrants were exercised. The weighted average fair value, estimated using the Black-Scholes option pricing model at the grant date of these warrants was \$0.86 per warrant using the following weighted average assumptions: dividend yield 0%; risk-free interest rate 4.02%; expected volatility 73%; and expected life of 2 years.

(iii) 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 of 2 years. In addition to the agency fee of \$1,750 paid in cash, the Company granted compensation options entitling the agents to acquire 301,250 compensation units at price of \$4.15 per unit within two years from the closing date. Each compensation unit comprises of

Migao Corporation

Notes to Consolidated Financial Statements

September 30, 2008 and 2007

(in thousands of Canadian dollars, except per share amounts)

9. Share Capital - continued

(b) Issued common shares - continued

one common share 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 \$2.34 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 of 2 years.

(iv) During the year ended September 30, 2007, 100,000 of the common share purchase options issued to the employees and directors of the Company were exercised by a former director of the Company at a price of \$2.85 per common share. The stock options were valued at the grant date at \$1.40 per stock option using the following assumptions: dividend yield 0%; risk-free interest rate 4%; expected volatility 66%; and expected life of 5 years.

(v) During the year ended September 30, 2008, a total of 111,300 underwriters' compensation options were exercised at an average price of \$4.08 per option. They consisted of one common share and one-half common share purchase warrant. The fair value of these options were estimated at the grant date using the Black-Scholes option pricing model for a weighted average value of \$2.27 per option. The warrants issued on the exercise of these options had a weighted average fair value of \$1.68 per warrant with the following weighted average assumptions: dividend yield 0%; risk-free interest rate 3.06%; expected volatility 97%; and expected life of 0.73 years.

(vi) During the year ended September 30, 2008, a total of 2,615,133 of the common share purchase warrants were exercised with an average exercise price of \$3.87. The weighted average fair value at the grant date, estimated using the Black-Scholes option pricing model, of these warrants was \$0.78 per warrant using the following weighted average assumptions: dividend yield 0%; risk-free interest rate 4.01%; expected volatility 70%; and expected life of 2 years.

(vii) During the year ended September 30, 2008, 315,000 of the common share purchase options with an exercise price of \$2.85 per common share issued to the employees and directors of the Company were exercised. The stock options were valued at the grant date at \$1.40 per stock option using the following assumptions: dividend yield 0%; risk-free interest rate 4%; expected volatility 66%; and expected life of 5 years.

(viii) On March 13, 2008, the Company completed a public offering of 3,593,750 common shares priced at \$8.00 per share. Pursuant to the Underwriting Agreement, the Company paid the underwriters an underwriting commission of \$0.46 per share, reflecting a commission of 5.75%. In addition to the underwriting commission, the Company paid \$618 in total for expenses incurred on this private placement.

Migao Corporation

Notes to Consolidated Financial Statements

September 30, 2008 and 2007

(in thousands of Canadian dollars, except per share amounts)

9. Share Capital - continued

(c) Contributed surplus

	Amount
Balance - September 30, 2006	\$ 2,956
Fair value of exercised underwriters' compensation options	(655)
Fair value of warrants issued on the exercise of underwriters' compensation options	378
Stock-based compensation expense	907
Fair value of warrants exercised	(1,113)
Fair value of private placement warrants issued	5,513
Fair value of underwriters' compensation options issued	705
Fair value of stock options exercised	(140)
Balance - September 30, 2007	\$ 8,551
Fair value of exercised underwriters' compensation options	(253)
Fair value of warrants issued on the exercise of underwriters' compensation options	93
Stock-based compensation expense	1,888
Fair value of warrants exercised	(2,048)
Fair value of stock options exercised	(441)
Forgiven officer's salaries	101
Balance - September 30, 2008	\$ 7,891

(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 Black-Scholes option valuation model, used by the Company to determine fair values, was developed for use in estimating the fair value of freely traded options. This model requires the input of highly subjective assumptions including future stock price volatility and expected time until exercise. Changes in the subjective input assumptions can materially affect the fair value estimate, and therefore the existing model does not necessarily provide a reliable single measure of the fair value of the Company's stock options granted during the year.

Migao Corporation

Notes to Consolidated Financial Statements

September 30, 2008 and 2007

(in thousands of Canadian dollars, except per share amounts)

9. Share Capital - continued

(d) Stock options

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

	Options	Weighted average exercise price
Outstanding - September 30, 2006	1,165,000	\$ 2.85
Granted during the year	120,000	8.08
Exercised during the year	(100,000)	2.85
Outstanding – September 30, 2007	1,185,000	\$ 3.38
Granted during the year	515,000	9.51
Exercised during the year	(315,000)	2.85
Outstanding – September 30, 2008	1,385,000	\$ 5.78

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

As of September 30, 2008

Exercise price	Number outstanding	Weighted average remaining contractual life (years)	Number exercisable	Exercise Price for exercisable options
\$2.85	750,000	2.63	361,666	\$2.85
\$7.69	60,000	3.75	20,000	\$7.69
\$8.46	60,000	3.75	40,000	\$8.46
\$9.93	40,000	4.25	NIL	N/A
\$9.48	300,000	4.67	50,000	\$9.48
\$9.48	175,000	4.67	NIL	N/A
\$5.78	1,385,000	3.47	471,666	\$4.23

During the year ended September 30, 2007, a total of 120,000 options were issued to a director and employees of the Company. Each option entitles the holder to purchase one common share of the Company at a weighted average price of \$8.08 per common share. These options have vesting periods of up to three years and an exercise period of up to five years, expiring on June 27, 2012. The fair value of the options issued was estimated using the Black-Scholes option pricing model on the date of issue with a weighted average value of \$6.10 per option. Weighted average assumptions used to determine the value of the options were: dividend yield 0%; risk-free interest rate 4.5%; expected volatility 108%; and expected life of 5 years. Stock-based compensation expense on these options for the year ended September 30, 2008 was \$441 (2007 – \$116).

During the year ended September 30, 2008, a total of 515,000 options were issued to an employee, officers, and directors of the Company. Each option entitles the holder to purchase one common share

Migao Corporation

Notes to Consolidated Financial Statements

September 30, 2008 and 2007

(in thousands of Canadian dollars, except per share amounts)

9. Share Capital - continued

(d) Stock options - continued

of the Company at a weighted average price of \$9.51 per common share. Upon granting of the options, 50,000 options were vested immediately and the balance of the options have vesting periods of up to three years and an exercise period of up to five years, expiring between January 7, 2013 to June 1, 2013. The fair value of the options issued was estimated using the Black-Scholes option pricing model on the date of issue with a weighted average value of \$7.10 per option. Weighted average assumptions used to determine the value of the options were: dividend yield 0%; risk-free interest rate 3.15%; expected volatility 97%; and expected life of 5 years. Stock-based compensation expense on these options for the year ended September 30, 2008 was \$1,096 (2007 – \$Nil).

For the year ended September 30, 2008, total stock-based compensation expense on the options granted prior to the year ended September 30, 2007 was \$351 (2007 - \$791).

(e) Warrants

As at September 30, 2008 and 2007, the following share purchase warrants were outstanding:

September 30, 2007	Issued	Exercised	Expired	September 30, 2008	Exercise Price	Expiry Date
2,337,333	2,931	2,340,264	-	-	\$ 3.70	May 18, 2008
2,825,450	52,719	274,869	-	2,603,300	\$ 5.30	February 22, 2009
5,162,783	55,650	2,615,133	-	2,603,300		

September 30, 2006	Issued	Exercised	Expired	September 30, 2007	Exercise Price	Expiry Date
3,181,500	219,774	1,063,941	-	2,337,333	\$ 3.70	May 18, 2008
-	3,050,156	224,706	-	2,825,450	\$ 5.30	February 22, 2009
3,181,500	3,269,930	1,288,647	-	5,162,783		

Migao Corporation

Notes to Consolidated Financial Statements

September 30, 2008 and 2007

(in thousands of Canadian dollars, except per share amounts)

9. Share Capital - continued

(f) Underwriters' Compensation Options

As at September 30, 2008 and 2007, the following underwriters' compensation options were outstanding:

September 30, 2007 (outstanding and exercisable)	Issued	Exercised	Expired	September 30, 2008 (outstanding and exercisable)	Exercise Price	Weighted average remaining contractual life (years)
5,862	-	5,862	-	-	\$ 2.85	-
225,938	-	105,438	-	120,500	\$ 4.15	0.40
231,800	-	111,300	-	120,500	\$ 4.15	0.40

September 30, 2006 (outstanding and exercisable)	Issued	Exercised	Expired	September 30, 2007 (outstanding and exercisable)	Exercise Price	Weighted average remaining contractual life (years)
445,410	-	439,548	-	5,862	\$ 2.85	0.63
-	301,250	75,312	-	225,938	\$ 4.15	1.40
445,410	301,250	514,860	-	231,800	\$ 4.12	1.38

10. 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. As of September 30, 2008, the total paid in capital of the Company's PRC entities is \$83,535 (RMB 539.6 million; September 30, 2007 - \$46,557 or RMB 350.8 million). 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 September 30, 2008 was \$5,432 (RMB 38.1 million; September 30, 2007 - \$2,284 or RMB 17.2 million).

11. Accumulated Other Comprehensive Income (Loss)

Unrealized gains (losses) on translating financial statements of self-sustaining foreign operations:	2008	2007
Balance – beginning of year	\$ (7,096)	\$ (147)
Unrealized foreign currency translation losses during the period	19,145	(6,949)
Balance – end of year	\$ 12,049	\$ (7,096)

Migao Corporation

Notes to Consolidated Financial Statements

September 30, 2008 and 2007

(in thousands of Canadian dollars, except per share amounts)

12. Income Tax

The components of income before income taxes are as follows:

	2008	2007
Pre-tax income (loss) from operations:		
Canada	\$ (4,133)	\$ (2,709)
Foreign - China	34,211	14,573
	\$ 30,078	\$ 11,864

The provision for income taxes consists of the following:

	2008	2007
Income taxes for operations:		
Current		
Foreign - China	\$ 2,463	\$ 1,127
Future		
Foreign - China	312	(470)
	\$ 2,775	\$ 657

The Subsidiaries are governed by the Income Tax Laws of the PRC concerning Foreign Investment Enterprises and various local income tax laws. Pursuant to the relevant laws and regulations in the PRC, the Subsidiaries are subject to income tax at effective rates of 15% to 25% on income as reported in their statutory financial statements. The operating Subsidiaries are entitled to a full exemption from PRC income tax for two years starting from their first profitable year and a 50% exemption from PRC income tax for three years starting two years after the first profitable year.

Each subsidiary maintains a December 31st year end for tax purposes. Sichuan Migao received a full exemption from tax for the years ended December 31, 2004 and 2005 having incurred a loss in its first year of operations being December 31, 2003. Sichuan Migao also received a 50% exemption from tax for the years ended December 31, 2006 and 2007. Guangdong Migao received a full exemption from tax for the years ended December 31, 2005 and 2006 having incurred a loss in its first year of operations being December 31, 2004. Guangdong Migao also received a 50% exemption from tax for the year ended December 31, 2007. Liaoning Migao received a full exemption from tax for the years ending December 31, 2006 and 2007 having incurred a loss in the first year of operations being December 31, 2005. Changchun Migao is expected to receive full exemptions from tax for the years ending December 31, 2008 and 2009. Shanghai Migao is expected to receive full exemptions from tax for the years ending December 31, 2009 and 2010. As a result of their operating results, the Subsidiaries will be eligible for the 50% exemption from tax as follows: Sichuan Migao for the years ending December 31, 2008; Guangdong Migao for the years ending December 31, 2008 and 2009; Liaoning Migao for the years ending December 31, 2008 through 2010; Changchun Migao for the years ending December 31, 2010 through 2012; and Shanghai Migao for the years ending December 31, 2011 through 2013.

The Company (legal parent) is governed by the Income Tax Act of Canada. It is not anticipated to incur income taxes as no operational revenue is to be generated.

Migao Corporation

Notes to Consolidated Financial Statements

September 30, 2008 and 2007

(in thousands of Canadian dollars, except per share amounts)

12. Income Tax - continued

Income tax expense varies from the amount by applying the combined Canadian federal and provincial tax rate of 34.15% (2007 – 36.12%) to income before income taxes as follows:

	2008	2007
Pre-tax income:	\$ 30,078	\$ 11,864
Income taxes at combined Canadian tax rate	\$ 10,272	\$ 4,285
Increase (decrease) in income taxes resulting from:		
Lower tax rates on earnings of foreign subsidiaries	(8,999)	(3,956)
Timing differences	(766)	-
Effect of reduction in statutory rate	355	-
Non-deductible expenses	644	328
Change in valuation allowance	1,269	-
	\$ 2,775	\$ 657

The Company's income tax expense (recovery) is split as follows:

	2008	2007
Current income tax expense	\$ 2,463	\$ 1,127
Future income tax expense (recovery)	312	(470)
	\$ 2,775	\$ 657

A summary of the future income tax assets and liabilities are as follows:

	2008	2007
Future income tax assets:		
Plant and equipment and land use rights	\$ 488	\$ 380
Share issue costs	1,318	1,381
Other timing differences	90	90
Loss carryforwards	2,256	1,043
	4,152	2,894
Less: Valuation allowance	3,574	2,424
Total future income tax assets	578	470
Future income tax liabilities:		
Other timing differences	(420)	-
Net future income tax assets	\$ 158	\$ 470

Migao Corporation

Notes to Consolidated Financial Statements

September 30, 2008 and 2007

(in thousands of Canadian dollars, except per share amounts)

12. Income Tax - continued

The Company has established the above valuation allowances as of September 30, 2008 due to the uncertainty of future realization of future income tax assets. At September 30, 2008, the Company has approximately \$7,778 of non-capital loss carry-forwards in Canada. The utilization of the loss is uncertain therefore a valuation allowance has been applied and no future income tax asset is set up for these losses. These losses expire as follows:

2026	\$ 1,116
2027	2,887
2028	<u>3,775</u>
Total	<u>\$ 7,778</u>

13. Earnings per Share

The following table sets forth the computation of basic and diluted earnings per common share for the years ended September 30:

	2008	2007
Numerator:		
Income attributable to common shareholders – basic and diluted	\$ 27,303	\$ 11,206
Denominator:		
Weighted-average common shares outstanding - basic	40,658,089	33,479,987
Effect of dilutive securities:		
Warrants	1,730,755	1,008,144
Stock options	614,824	544,374
Underwriters' compensation options	96,056	42,418
Weighted-average common shares outstanding - diluted	43,099,724	35,074,923
Basic earnings per common share	\$ 0.67	\$ 0.33
Diluted earnings per common share	\$ 0.63	\$ 0.32

For the year ended September 30, 2008, approximately 575,000 potentially dilutive stock options were excluded from the computation of weighted-average number of diluted common shares outstanding, as the applicable exercise prices were greater than the average market price of the Company's common shares for the year.

For the year ended September 30, 2007, approximately 120,000 potentially dilutive stock options were excluded from the computation of weighted-average number of diluted common shares outstanding, as the applicable exercise prices were greater than the average market price of the Company's common shares for the year.

Migao Corporation

Notes to Consolidated Financial Statements

September 30, 2008 and 2007

(in thousands of Canadian dollars, except per share amounts)

14. Segmented Information

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

Geographical information:

2008	Canada	China	Total
Sales from operations	\$ NIL	\$ 187,028	\$ 187,028
Net income (loss)	\$ (4,133)	\$ 31,436	\$ 27,303
Total assets	\$ 845	\$ 208,549	\$ 209,394
Plant and equipment, land use rights and construction in progress	\$ NIL	\$ 65,652	\$ 65,652
2007	Canada	China	Total
Sales from operations	\$ NIL	\$ 101,804	\$ 101,804
Net income (loss)	\$ (2,709)	\$ 13,915	\$ 11,206
Total assets	\$ 242	\$ 99,785	\$ 100,027
Plant and equipment, land use rights and construction in progress	\$ NIL	\$ 44,857	\$ 44,857

15. Commitments

Purchase commitments for raw materials and supplies in the amount of approximately \$23.5 million (RMB 151.7 million) exist as of September 30, 2008 (September 30, 2007 - \$2.4 million or RMB 18 million). These contracts are entered into in the normal course of business.

Commitments on capital expenditures in the amount of approximately \$10.4 million (RMB 66.9 million) exist as of September 30, 2008 (September 30, 2007 - \$3.9 million or RMB 29 million). These contracts are entered into in the normal course of business.

Migao Corporation

Notes to Consolidated Financial Statements

September 30, 2008 and 2007

(in thousands of Canadian dollars, except per share amounts)

15. Commitments - continued

The Company signed an office lease on August 14, 2006. The term of the lease is five years from October 1, 2006. The lease obligations are reflected in the following table on a fiscal year basis.

2009	\$	71
2010		72
2011		<u>73</u>
Total	\$	<u>216</u>

16. Capital Management

The Company's objective is to maintain a strong capital base so as to maintain investor, creditor and market confidence and to sustain future development of the business. Management defines capital as the Company's shareholders' equity. The Company has a small amount of debt for working capital purposes and therefore net earnings generated from operations are mostly available for reinvestment in the Company. The Board of Directors does not establish quantitative return on capital criteria for management; but rather promotes year over year sustainable profitable growth. The Company does not have a defined share repurchase plan and buy and sell decisions are made depending on market prices and regulatory restrictions. There were no changes in the Company's approach to capital management during the period. Except for as disclosed in Note 10, neither the Company nor any of its subsidiaries are subject to externally imposed capital requirements.

17. Financial Instruments and Risk Management

Market Risk

Market risk is the risk that changes in market prices, such as foreign exchange rates and interest rates, that will affect the Company's income or the value of its holding of financial instruments.

Foreign currency risk

The Company's global operations expose it to foreign currency fluctuations. Revenues and related expenses generated from the Company's Chinese subsidiaries are generally denominated in Chinese Renminbi ("RMB"). Head office expenditures are generally denominated in Canadian dollars. Therefore, the Company's primary currencies include RMB and Canadian dollars. The Consolidated Statements of Operations of the Company's global operations are translated into Canadian dollars at the average exchange rates in each applicable period. To the extent the Canadian dollar strengthens against foreign currencies, the foreign currency conversion of these foreign currency denominated transactions into Canadian dollars results in reduced revenues, operating expenses and net income for the Company's international operations. Similarly, the Company's revenues, operating expenses and net income will increase for its international operations if the Canadian dollar weakens against foreign currencies. The Company cannot predict the effect foreign exchange fluctuations will have on its results going forward. However, if there is an adverse change in foreign exchange rates versus the Canadian dollar, it could have a material effect on other comprehensive income.

Migao Corporation

Notes to Consolidated Financial Statements

September 30, 2008 and 2007

(in thousands of Canadian dollars, except per share amounts)

17. Financial Instruments and Risk Management - continued

Market Risk - continued

Foreign currency risk - continued

At September 30, 2008, through its wholly-owned, self-sustaining subsidiaries, the Company had cash and cash equivalents of \$16,209, accounts receivable of \$8,440, other receivables of \$4,639, accounts payable and accrued liabilities of \$10,557, and bank loans of \$13,855, which were denominated in RMB. Gains and losses arising upon translation of these amounts into Canadian dollars for inclusion in the consolidated financial statements are recorded within other comprehensive income, a component of shareholders' equity. A 10% change in the average exchange rate between C\$/RMB on the financial instruments would have a \$488 effect on the other comprehensive income in Canadian dollars.

Interest rate risk

The Company is exposed to interest rate risk on its short-term bank loans and does not currently hold any financial instruments that mitigate this risk. Management does not believe that the impact of interest rate fluctuation will be significant.

Commodity Price Risk

Manufacturing costs for the Company's products are affected by the price of raw materials, namely potassium chloride, sulfuric acid, ammonium nitrate and certain other energy generating sources. In order to manage this risk, the Company includes a clause regarding transfer of risk to customers in all the medium and long-term sales contract in order to renegotiate the prices in the event of change. In addition, the Company had been utilizing its strong working capital position in stocking raw materials when their price is anticipated to rise.

Credit Risk

Credit risk is the risk of financial loss to the Company if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Company's accounts receivable.

The Company's exposure to credit risk with its customers is influenced mainly by the individual characteristics of each customer. The Company's customers are for the most part, large PRC State-owned and private companies. A significant portion of the Company's accounts receivable is from long-term customers and the Company receives prepayments and deposits from them for a large portion of its sales. Over the last three years, the Company has not suffered any significant credit related losses with any of its customers.

At September 30, 2008, the Company does not consider any of its financial assets to be impaired.

Migao Corporation

Notes to Consolidated Financial Statements

September 30, 2008 and 2007

(in thousands of Canadian dollars, except per share amounts)

17. Financial Instruments and Risk Management - continued

Credit Risk - continued

The following table provides information regarding the ageing of financial assets that are past due but which are not impaired.

Current	90 – 180 days	180 – 365 days	365 days +	Carrying value on the balance sheet
\$7,368	\$502	\$613	\$115	\$8,598

The definition of items that are past due is determined by reference to terms agreed with individual customers. None of the amounts outstanding have been challenged by the respective customer(s) and the Company continues to conduct business with them on an ongoing basis. Accordingly, management expects that this balance is fully collectible in the future.

The Company reviews financial assets past due on an ongoing basis with the objective of identifying potential matters which could delay the collection of funds at an early stage. Once items are identified as being past due, contact is made with the respective customer to determine the reason for the delay in payment and to establish an agreement to rectify the breach of contractual terms.

The carrying amount of financial assets represents the maximum credit exposure. Based on historic default rates, the Company believes that there are minimal requirements for an allowance for doubtful accounts and as a result, no allowance has been recorded. As well, deposits by certain customers are often made which also helps to mitigate the risk if there is any.

Liquidity risk

Liquidity risk is the risk that the Company is not able to meet its financial obligations as they fall due. The Company's growth is financed through a combination of the cash flows from operations, borrowing under the existing credit facilities and the issuance of equity. One of management's primary goals is to maintain an optimal level of liquidity through the active management of the assets and liabilities as well as the cash flows. Given the Company's available liquid resources as compared to the timing of the payments of liabilities, management assesses the Company's liquidity risk to be low.

At September 30, 2008 the Company's cash and cash equivalents balance was \$16,850 and working capital balance was \$102,208. As at September 30, 2008, short-term bank loans in the amount of \$13,855 were outstanding under the Company's credit facilities.

Fair Value

The fair value of cash and cash equivalents, accounts receivable, other receivables, bank loans, accounts payable and accrued liabilities approximates their carrying values due to their short-term maturities. The fair value of the amount due from related party is not readily determinable due to the related party nature of the advances.

Migao Corporation

Notes to Consolidated Financial Statements

September 30, 2008 and 2007

(in thousands of Canadian dollars, except per share amounts)

18. Economic Dependence

During 2008, one customer comprised 36% of revenue and two suppliers individually accounted for 57% and 10% of total purchases. At September 30, 2008, one customer individually represented 56% of total accounts receivable and one supplier individually represented 10% of total accounts payable. It should be noted that the supplier accounting for 10% of total purchases is not the same as the one representing 10% of total accounts payable.

During 2007, two customers individually comprised 56% and 6% of revenue and two suppliers individually accounted for 37% and 16% of total purchases. At September 30, 2007, three customers individually represented 19%, 18% and 18% of total accounts receivable and two suppliers represented 36% and 19% of total accounts payable.