Migao Corporation

Management's Discussion and Analysis

First Quarter, Fiscal 2014
Ended June 30, 2013

August 14, 2013

The following is Management's Discussion and Analysis ("MD&A") of the financial condition of Migao Corporation (the "Company" or "Migao") and its financial performance for the three months ended June 30, 2013. This MD&A should be read in conjunction with the unaudited condensed Interim Consolidated Financial Statements and related notes as at and for the period ended June 30, 2013 and the audited Consolidated Financial Statements and related notes as at and for the year ended March 31, 2013. Reference should also be made to the Company's filings, including the Company's annual information form, with Canadian securities regulatory authorities which are available at www.sedar.com.

This MD&A is the responsibility of management. The Board of Directors carries out its responsibility for the review of this disclosure directly and through its audit committee comprised exclusively of independent directors. The audit committee reviews and prior to its publication, approves, pursuant to the authority delegated to it by the Board of Directors, this disclosure.

All amounts are in Canadian dollars ("C$") unless otherwise noted (tabular amounts are in thousands of C$) and prepared in accordance with International Financial Reporting Standards ("IFRS"), as issued by the International Accounting Standard Board ("IASB").

At June 30, 2013, the Company had 52,496,160 common shares outstanding. As at market open on August 14, 2013, the Company has 52,496,160 common shares outstanding.

Forward-Looking Information

This document includes forward-looking statements within the meaning of certain securities laws, including the "safe harbour" provisions of the Securities Act (Ontario) and other provincial securities laws in Canada. These forward-looking statements include, among others, statements with respect to our objectives and goals, and strategies to achieve those objectives and goals, as well as statements with respect to our beliefs, plans, objectives, expectations, anticipations, estimates and intentions. The words "may", "will", "could", "should", "would", "suspect", "outlook", "believe", "plan", "anticipate", "estimate", "expect", "intend", "forecast", "objective", and "continue" (or the negative or grammatical variations thereof), and words and expressions of similar meaning, are intended to identify forward-looking statements.

By their very nature, forward-looking statements involve inherent risks and uncertainties, both general and specific, which give rise to the possibility that predictions, forecasts, projections and other forward-looking statements will not be achieved. Certain material factors or assumptions are applied in making forward-looking statements and actual results, performance or achievements may differ materially from those expressed or implied in such statements. We caution readers not to place undue reliance on forward-looking statements as a number of important factors, many of which are beyond our control, could cause actual results, performance or achievements to differ materially from the beliefs, plans, objectives, expectations, anticipations, estimates and intentions expressed in such forward-looking statements. These factors that relate to our company include, but are not limited to: risks related to raw materials; execution of the business plan; expansion plans; dependence on key personnel; key relationships; dependence on key customers; dependence on key suppliers; competition; market factors and volatility of commodity prices; environmental risks and hazards; operating risks; proprietary rights; infrastructure; future capital requirements; technical substitution; exchange rate fluctuations; insurance; foreign operations; tobacco industry considerations; weather conditions and natural disasters; control by management; seasonality; dividends; conflicts of interest; global financial conditions; and the implementation of the Labour Contract Law in the people's Republic of China in 2008. In addition to the foregoing risk factors, there are also risks related to doing business in China which include, but are not limited to: state ownership; government sector intervention; foreign investment; repatriation of profit and currency conversion; tax; shareholders' rights and enforcement of judgments; developing legal system; protection of intellectual property rights; permits and business licenses; appropriation; and availability of land. Should one or more of these factors materialize, or should our estimates or underlying assumptions prove incorrect, actual results, performance or achievements may vary materially from those described in forward-looking statements.

We caution that the foregoing list of important factors that may affect our future results, performance or achievements is not exhaustive. When reviewing our forward-looking statements, readers should carefully consider the foregoing factors and other uncertainties and potential events. Additional information about factors that may cause actual results to differ materially from expectations, and about material factors or assumptions applied in making forward-looking statements, may be found under the "Risk Factors" sections in our Annual Information Form, under "Risk Factors" and elsewhere in our filings with Canadian securities regulatory authorities. Except as required by Canadian securities laws, we do not undertake to update any forward-looking statements, whether written or oral, that may be made from time to time by us or on our behalf; such statements speak only as of the date made. We cannot assure readers that actual results, performance and achievements will be consistent with these forward-looking statements, and the differences may be material. The forward-looking statements included herein are expressly qualified in their entirety by this cautionary language.

Overview

Migao, through its wholly-owned operating subsidiaries (referred to herein as "Sichuan Migao", "Guangdong Migao", "Liaoning Migao", "Shanghai Migao", "Changchun Migao", "Tianjin Migao", "Zunyi Migao"), and through its 50% ownership of SQM JV, owns land use rights and operates fertilizer production plants in various strategic locations in the People's Republic of China (the "PRC") for the production and sale of specialty potash fertilizer potassium nitrate and potassium sulphate along with their co-products, specialty compound fertilizers, granulated potassium chloride, and standard potassium chloride. The products are for the Chinese domestic agricultural market. These fertilizers provide China's economic crop (i.e. tobacco, fruit and vegetable) growers added opportunities for improving crop quality and increasing crop yield in an environmentally responsible manner, and contributing to the overall agricultural development of China.

In addition to measures based on IFRS in this MD&A, we use the term earnings before interest, taxes, depreciation and amortization ("EBITDA"). EBITDA is not defined by IFRS, and our use of such terms or measurement of such items may vary from that of other companies. In this MD&A, we may describe certain 'income' and 'expense' items as unusual or non-recurring. These terms are not defined by IFRS. Our usage of these terms may vary from the usage adopted by other companies. We provide this detail so that readers have a better understanding of the significant events and transactions that have had an impact on our results.

Highlights for the Quarter

On April 8, 2013, the Company announced the appointment of Pingfu Sun to the board of directors. Based in China, Mr. Sun leads the technical committee of experts for Migao at the Sichuan facility. Mr. Sun has worked at Migao since 2007 and was responsible for the successful design and implementation of Migao's joint venture with SQM for the production of soluble potassium nitrate. Mr. Sun has led the Company's research and development team in designing and implementing improvements to production processes that have increased Migao's economic and environmental performance. Mr. Sun has 28 years of professional experience, having worked at a variety of chemical plants in China, focusing on inorganic chemical, organic chemical and fine chemical industries, as well as having experience in engineering economics research. Mr. Sun's addition to the board further enhances the Company's already strong industry and technical expertise.

Performance of Migao

Key performance indicators

The key performance indicators for Migao are revenue growth, gross profit, EBITDA, net income, and earnings per share.

The success of the Company to expand will be measured by revenue and product tonnage growth. Revenue growth will be dependent on the Company being able to expand production capacity either at existing locations or by building facilities at new locations and maintaining or increasing average selling prices.

Gross profit will be an indicator of how well the Company is managing its raw material costs, variable production costs, and customer contract negotiations.

Management believes that EBITDA is a measure of how efficiently and effectively the Company's business is running. Net income is also viewed as an important measure for determining the value created for shareholders.

Measurement

Below under "Quarterly Results" and "Results of Operations" are two tables the Company uses to assess performance. The first table presents the Company's consolidated results for the last eight quarters. The second table sets out the Company's consolidated results for the quarter ended June 30, 2013, compared with the same periods last year.

Table 1 - Quarterly Results

in thousands of Canadian dollars except per share and percentage data	***Fiscal 2014 Q1***	Fiscal 2013 Q4	Fiscal 2013 Q3	Fiscal 2013 Q2	Fiscal 2013 Q1	Fiscal 2012 Q4	Fiscal 2012 Q3	Fiscal 2012 Q2
		(Restated for entire Fiscal 2013)#						
Revenue	***29,405***	188,801	53,801	9,204	32,535	138,797	97,360	66,028
Gross profit (loss) *	***1,987***	1,244	1,090	(1,545)	2,821	12,712	15,704	14,123
Gross profit (loss) (% of revenue)	***6.8%***	0.7%	2.4%	(16%)	8.7%	9.2%	16.1%	21.4%
Selected operating expenses:								
Selling	***1,254***	3,983	2,960	655	1,186	1,970	2,972	1,676
General and administrative	***4,672***	6,044	5,197	5,446	4,856	5,843	6,099	4,076
Finance costs	***1,459***	570	1,102	744	1,140	1,423	1,059	850
Pre-operating costs	***38***	-	-	-	890	526	322	330
Impairment loss	***-***	18,402	-	-	-	4,569	-	-
Other income	***448***	6,447	3,691	453	900	332	122	305
Share of income from a joint venture	***50***	(109)	153	15	342	-	-	-
Income taxes (recovery)	***185***	800	185	(460)	(90)	(361)	1,439	1,735
Income taxes (% of revenue)	***0.6%***	0.4%	0.3%	(5.0%)	(0.3%)	(0.3%)	1.5%	2.6%
Effective tax rate (% of income before taxes)	***(3.7%)***	(3.7%)	(4.3%)	5.4%	2.2%	26.1%	27.3%	22.6%
Net (loss) profit	***(5,128)***	(22,311)	(4,512)	(8,100)	(3,919)	(1,023)	3,838	5,956
Net (loss) profit (% of revenue)	***(17.4)***	(11.8%)	(8.4%)	(88%)	(12.1%)	(0.7%)	3.9%	9.0%
EBITDA	***(1,460)***	(18,900)	(1,136)	(5,804)	(652)	994	8,046	10,316
EBITDA (% of revenue)	***(5.0%)***	(10.0%)	(2.1%)	(63.1%)	(2.0%)	0.7%	8.3%	15.6%
(Loss) earnings per share (in $)								
Basic	***(0.10)***	(0.43)	(0.09)	(0.15)	(0.07)	(0.02)	0.07	0.11
Diluted	***(0.10)***	(0.43)	(0.09)	(0.15)	(0.07)	(0.02)	0.07	0.11

* There was an inventory write-down of $1,405 included in the calculation of gross profit for the fourth quarter of fiscal 2013, an inventory write-down of $222 included in the calculation of gross profit for the third quarter of fiscal 2013, and an inventory write-down of $1,546 included in the calculation of gross profit for the second quarter of fiscal 2013 (All numbers in this note have excluded the impact from SQM JV due to change of accounting policies effectively April 1, 2012).

Effective April 1, 2013, the Company implemented IFRS 11 – Joint Arrangement on its 50% interest evaluation in its joint arrangement, SQM JV, by using the equity method instead of proportionate consolidation. Prior periods have been restated for this change in accounting policy in accordance with the requirement of the new standard.

Table 2 – Selected Quarterly Results

in thousands of Canadian dollars except per share and percentage data	**Quarter ended June 30, 2013**	**Quarter ended June 30, 2012 (restated)**
Revenue	**29,405**	32,535
Loss for the period	**(5,128)**	(3,919)
Loss per share		
Basic	**(0.10)**	(0.07)
Diluted	**(0.10)**	(0.07)
Total Assets	**561,940**	496,148
Total Current Liabilities	**234,534**	147,946
Total Non-Current Liabilities	**4,724**	5,238

Table 3 – Results of Operations

Consolidated Results

The following table sets out the Company's consolidated results for the quarter ended and year to date June 30, 2013, compared with the same periods last year.

In thousands of Canadian dollars except per share and percentage data	Q1 2014	Q1 2013 (restated)	Increase (Decrease)
Revenue	**29,405**	32,535	(3,130)
Gross profit	**1,987**	2,821	(834)
Gross profit (% of revenue)	**6.8%**	8.7%	(1.9%)
Selling expenses	**1,254**	1,186	68
Selling expenses (% of revenue)	**4.3%**	3.6%	0.7%
General and administrative expenses	**4,672**	4,856	(184)
General and administrative expenses (% of revenue)	**15.9%**	14.9%	1.0%
Other income	**448**	900	(452)
Other income (% of revenue)	**1.5%**	2.8%	(1.3%)
Income tax (provision) recovery	**(185)**	90	(275)
Income taxes (% of revenue)	**(0.6%)**	0.3%	(0.9%)
Effective tax rate (% of net loss (profit) before taxes)	**(3.7%)**	2.2%	5.9%
EBITDA	**(1,460)**	(652)	(808)
EBITDA (% of revenue)	**(5.0%)**	(2.0%)	(3.0%)
Loss for the period	**(5,128)**	(3,919)	(1,209)
Loss for the quarter (% of revenue)	**(17.4%)**	(12.1)%	(5.3%)
Loss per share			
Basic	**(0.10)**	(0.07)	(0.03)
Diluted	**(0.10)**	(0.07)	(0.03)
Weighted average number of common shares outstanding			
Basic	**52,496,160**	52,496,160	
Diluted	**52,496,160**	52,496,160	

Table 4 - Reconciliation to IFRS Net Income

The following table sets out the reconciliation of the Company's consolidated IFRS profit to earning measure not recognized under IFRS, specifically EBITDA, for the quarter ended June 30, 2013 compared with the same period last year. Management believes that EBITDA is a measure of how efficiently and effectively the Company's business is running.

in thousands of Canadian dollars	**Q1 2014**	**Q1 2013 (restated)**
Loss for the quarter	**(5,128)**	(3,919)
Add:		
Amortization	**2,024**	2,217
Interest Expense	**1,459**	1,140
Income Tax Expense (Recovery)	**185**	(90)
EBITDA	**(1,460)**	(652)

Revenue

Table 5 – Average Foreign Exchange Rates for Revenue

Average Foreign Exchange Rates	**Q1 2014**	**Q1 2013**
RMB to Canadian dollars	0.1662	0.1596
Canadian dollars to RMB	6.0169	6.2657

Table 6 – Revenue in Chinese RMB and Canadian dollars

Revenue (in thousands)	**Q1 2014**	**Q1 2013 (restated)**
Revenue in RMB	176,927	203,853
Revenue in Canadian dollars	29,405	32,535

Revenue was $29.4 million for the quarter ended June 30, 2013, compared with $32.5 million for the same period last year, representing a $3.1 million reduction in revenue. Comparing the first quarter of fiscal 2014 to fiscal 2013:

- Decrease in revenue of potassium nitrate, although volume was similar, average selling price was lower;
- Increase in revenue of potassium sulphate;
- Increase revenue and selling price of hydrochloric acid
- Significantly lower sales of potassium chloride, offset by higher selling prices

Annual run rate capacity for the core products was 620,000 tonnes as of June 30, 2013.

Migao earns all of its revenue in Chinese Renminbi ("RMB"). Accordingly, reported revenue will fluctuate with changes in the exchange rate of RMB to C$. Table 5 is a summary of the average foreign exchange rates between RMB and C$. Table 6 are revenue in C$ and RMB.

Table 7 - The following is a summary of the Company's average selling prices by products for the quarters ended June 30, 2013 and March 31, 2013. (Below analysis incorporates the data from SQM using proportional consolidation method)

Products	Q1 2014 (RMB)	Q1 2013 (RMB)
Potassium Nitrate	4,568	5,394
Potassium Sulphate	3,188	3,436
Ammonium Chloride	766	1,247
Hydrochloric Acid	257	246
Specialty Compound	-	4,264
Direct Sale of Compound	4,960	-
Potassium Chloride	3,428	3,311

Table 8 - The following is a summary of the Company's facilities and production capacities as of June 30, 2013. (Below analysis incorporates the data from SQM using proportional consolidation method)

	Core Product	Annual Capacity (tonnes)		Co-Product	Annual Capacity (tonnes)	Production Commencement
Sichuan	Potassium Nitrate	80,000		Ammonium Chloride	44,800	December 2003
SQM JV[1]	Potassium Nitrate	20,000		Ammonium Chloride	11,200	January 2011
Guangdong	Potassium Sulphate	160,000		Hydrochloric Acid	192,000	December 2004
Liaoning	Potassium Sulphate	40,000		Hydrochloric Acid	48,000	December 2005
Changchun[2]	Potassium Sulphate	80,000		Hydrochloric Acid	96,000	January 2012
Shanghai	Potassium Sulphate	40,000		Hydrochloric Acid	48,000	January 2011
Sichuan	Specialty Compound	100,000		N/A	N/A	January 2010
Zunyi	Specialty Compound	100,000		N/A	N/A	February 2012
Total		**620,000**			**440,000**	

	Other Product	Annual Capacity (tonnes)	Production Commencement
Liaoning[3]	Sulphuric Acid	120,000	See note [3] below

[1] The SQM JV output capacity is 40,000 tonnes. The chart shows only the Company's proportionate share.

[2] Changchun Migao's 80,000 tonnes of capacity was built in two phases. The original 40,000 tonnes of output commenced production in December 2007 while another 40,000 tonnes of output capacity was added in January 2012.

[3] An impairment test was completed at March 31, 2012 on the sulphuric acid plant of Liaoning Migao and resulted in an impairment charge of $4.6 million. As at March 31, 2013, an impairment test was again conducted and it was determined to further write down the remaining sulphuric acid plant assets by $4.0 million.

The Company still anticipates demand for its core products: potassium nitrate, potassium sulphate and specialty compound fertilizers, as well as one of its co-products: ammonium chloride. The Company's other co-product, hydrochloric acid, has been severely impacted by the global economic slowdown and its effect on many Chinese exports, which use hydrochloric acid in their production. The storage of hydrochloric acid inventory is limited to the Company's storage tank capacity since the product is in a liquid form. Therefore, the Company has limited stockpiling capabilities.

Table 9 - The following are summaries of the Company's productions and sales of its core products for the quarter ended June 30, 2013 and 2012. (Below analysis incorporates the data from SQM using proportional consolidation method)

Quarter ended June 30, 2013:

Core Product	Quarterly Design Capacity (tonnes)	Volume Produced During the Quarter (tonnes)	Deliveries During the Quarter (tonnes)
Potassium Nitrate	25,000	21,510	16,962
Potassium Sulphate	80,000	33,696	21,939
Potassium Chloride and Value Added Potassium Chloride	N/A	Nil	2,307
Compound Fertilizer	50,000	200	Nil
Direct Sale of Compound Fertilizer	N/A	Nil	8,031
Total	**155,000**	**55,406**	**49,239**

Quarter ended June 30, 2012:

Core Product	Quarterly Design Capacity (tonnes)	Volume Produced During the Quarter (tonnes)	Deliveries During the Quarter (tonnes)
Potassium Nitrate	25,000	21,186	14,940
Potassium Sulphate	80,000	23,191	13,324
Potassium Chloride and Value Added Potassium Chloride	N/A	Nil	22,254
Compound Fertilizer	50,000	511	2,899
Total	**155,000**	**44,888**	**53,417**

Geographic Revenue

The Company earns virtually all of its revenue in the PRC. At the moment, there is no expectation of significant export sales until the current 75% or related export tax is reduced or at such time that Migao builds a production facility outside of the PRC. Currently, domestic Chinese demand consumes almost all of Migao's production output.

Gross Profit

Gross Profit was $2.0 million for the quarter ended June 30, 2013, compared to a gross profit of $2.8 million for the same period last year, representing a decrease of $0.8 million. Gross profit margin was 6.8% for the quarter ended June 30, 2013, compared 8.7% for the same period last year.

Table 10 - The following is a summary of the Company's gross margin by products for the quarters ended June 30, 2013 and 2012. (Below analysis incorporates the data from SQM using proportional consolidation method)

Products	Q1 2014	Q1 2013
Potassium Nitrate	5.7%	17.4%
Potassium Sulphate	8.6%	(0.8%)
Ammonium Chloride	5.8%	19.7%
Hydrochloric Acid	17.48%	1.1%
Compound Fertilizer	N/A	15.7%
Direct Sale of Compound	0.3%	N/A
Potassium Chloride	10.5%	3.8%

Selling Expenses

Selling expenses for the quarter ended June 30, 2013 increased by $0.1 million to $1.3 million compared to $1.2 million for the same period last year. Selling expenses as a percentage of sales for the quarter ended June 30, 2013 was 4.3% compared to 3.6% for the same period last year.

General and Administrative Expenses

General and administrative expenses for the quarter ended June 30, 2013 decreased by $0.2 million to $4.7 million (from $4.9 million), compared with the same period last year.

Other Income

Other income for the quarter ended June 30, 2013 was $0.4 million compared to $0.9 million for the same period last year.

Other income are primarily rebates on value added tax which Migao is eligible for on certain agricultural designated transactions in China.

Income Taxes

Income taxes for the quarter ended June 30, 2013 increased by $0.3 million to a tax expense of $0.2 million (from tax recovery of $0.1 million), compared with the same period last year. Income taxes as a percentage of sales for the quarter ended June 30, 2013 were 0.6% compared to (0.3%) for the same period last year. Effective tax rate for the quarter ended June 30, 2013 was (3.7%) provision of taxes compared to 2.2% for the same period last year.

Income Tax Rates

Table 11 - The following is a step analysis of the Company's effective tax rate for the quarters ended June 30, 2013 and 2012.

	Q1 2014	**Q1 2013 (restated)**
PRC Subsidiaries	(6.7)%	(3.2)%
Corporate Entities	1.4%	1.7%
Deferred Income Taxes	1.6%	3.8%
Total	**(3.7)%**	**2.2%**

Loss and Loss per Share

Loss for the quarter increased by $1.2 million to $5.1 million (from $3.9 million) for the quarter ended June 30, 2013 compared to the same period last year. The increase in net loss during the quarter was mainly due to lower overall gross profit margin and lower average selling prices of potassium nitrate.

Loss per share was $0.10 for the quarter ended June 30, 2013, compared with loss per share of $0.07 for the same period last year, representing an increase of loss of $0.03 per share.

EBITDA (please see table 3)

EBITDA for the quarter ended June 30, 2013 decreased by $0.8 million to a loss of $1.5 million from $0.7 million for the same period last year. EBITDA as a percentage of sales for the quarter decreased by 3.0% to (5.0%) from (2.0%) compared with the same periods last year.

Table 12 - Liquidity and Capital Resources

(in thousands of Canadian dollars except for ratios)	**June 30, 2013**	**March 31, 2013 (restated)**
Current Ratio	**1.75:1**	1.80:1
Cash and Cash Equivalents	**17,232**	10,192
Restricted cash	**84,310**	66,848
Working Capital	**184,239**	183,037
Total Assets	**561,940**	542,804
Total Liabilities	**239,258**	234,363
Total Equity	**322,682**	308,441
Non-Current Bank Debt to Equity Ratio	**0.02:1**	0.02:1

The Canadian dollar/RMB foreign exchange rate used to translate the assets and liabilities was 5.8377 at June 30, 2013, compared to 6.2150 at March 31, 2013, representing a 6.1% appreciation in RMB.

Cash Position

Cash and cash equivalents totaled $17.2 million as of June 30, 2013, representing an increase of $7.0 million compared with the balances as of March 31, 2013. The increase in cash for the quarter ended June 30, 2013 is a result of $25.7 million in cash inflow from operations, a $7.7 million cash outflow from investing activities, and a cash outflow from financing activities due to $21.6 million net of a reduction in bank loans, and an impact of $0.9 million from realized foreign exchange gains.

Table 13 - The following shows the Company's cash and cash equivalents as well as restricted cash positions as of June 30, 2013 and March 31, 2013.

(in thousands of dollars)	**June 30, 2013**	**March 31, 2013 (restated)**
Cash and cash equivalents	17,232	10,192
Restricted cash	84,310	66,848
Total	**101,542**	**77,040**

The Company believes that its current cash position, working capital and cash flow is sufficient to meet the current ongoing needs of the business, which includes budgeted production expansion activities and budgeted production levels.

Working Capital

Working capital was $184.2 million as of June 30, 2013, representing an increase of $1.2 million compared with $183.0 million of March 31, 2013. This change is primarily a result of changes to the cash position noted above and the following:

Trade receivables decreased by $70.7 million to $116.8 million at June 30, 2013 compared to $187.5 million at March 31, 2013. Trade receivables decreased as a result of the Company's continued collection on previous outstanding receivable amount during the quarter and a reduced level of sales during the quarter. The Company's year to date average days of sales outstanding (DSO) at June 30, 2013 and March 31, 2013 were 362 and 211 days respectively. Customers have been slower in paying in fiscal 2013 compared to prior years. The slow payments are as a result of customers holding onto their cash longer as a result of the overall economic slowdown in the Chinese economy. The Company had no bad debt expense in the quarter ended June 30, 2013.

Restricted cash increased by $17.5 million to $84.3 million at June 30, 2013 compared to $66.8 million at March 31, 2013. Restricted cash increased due to an increase in notes payables, resulting in banks requiring more cash deposits as pledge for notes payables. Notes payable were used primarily to finance inventory requirements.

Current portion of prepayments, other receivables, deposits and other assets increased by $30.2 million at June 30, 2013 to $113.8 million compared to $83.6 million at March 31, 2013. Prepayments, other receivables, deposits and other assets increased due to prepayment for future raw material purchases to build inventory for new contracts and expected increase in production capacity during fiscal 2014. The deposits were placed primarily for raw materials purchases from Migao's current suppliers of potassium chloride.

Customer deposits decreased by $2.2 million to $10.4 million at June 30, 2013 compared to $12.6 million at March 31, 2013. This decrease is due to the timing of contracts as well as state owned enterprise customers conserving cash.

Total inventory increased by $23.3 million to $86.2 million at June 30, 2013 compared to $62.9 million at March 31, 2013. Inventory increased due to timing of raw material purchases and deliveries, and is in line with planned production requirements.

At the end of the period, the Company had $30.4 million (63,475 tonnes) of potassium chloride inventory with an average delivered price of $479 per tonne (March 31, 2013 - $491). In addition, during the quarter, the Company sold 16,962 tonnes of potassium nitrate, 21,939 tonnes of potassium sulphate, 4,853 tonnes of ammonium chloride, and at the end of the period, the Company had $43.9 million (112,190 tonnes) of finished goods inventory on hand, including co-products.

Accounts payable and accrued liabilities decreased by $1.2 million to $16.6 million at June 30, 2013 compared to $17.8 million at March 31, 2013, and notes payable increased by $30.8 million to $163.2 million at June 30, 2013 compared to $132.4 million at March 31, 2013. Facility managements are using notes payable as a low cost form of financing working capital primarily deposits for raw materials.

Loans decreased by $19.4 million to $25.5 million at June 30, 2013 compared to $44.9 million at March 31, 2013 due to the facilities utilizing notes payable to reduce financing working capital and a desire to reduce bank debt.

Plant and Equipment, Construction in Progress, Land Use Rights

Plant and equipment net of accumulated depreciation was $94.4 million at June 30, 2013 compared to $89.7 million as of March 31, 2013.

Land use rights net of accumulated amortization was $23.0 million at June 30, 2013 compared with $21.8 million as of March 31, 2013. Migao has approximately $0.6 million of land use rights payable.

Contractual Obligation Summary

- Commitments on capital expenditures in the amount of approximately $5.0 million exist as of June 30, 2013 (March 31, 2013 - $2.32 million). They were entered into in the normal course of business.

The following table summarizes our contractual obligations (in thousands of C$) as at June 30, 2013, and the effect such obligations are expected to have on our liquidity and cash flows in future years. The table excludes amounts already recorded on the consolidated balance sheet as current liabilities and certain other purchase obligations discussed above.

Table 14 – Other known contractual obligation as at June 30, 2013

	2014	2015	2016	2017	2018	Total
Operating lease obligation	**213**	**33**	**-**	**-**	**-**	**246**

Report on Controls

Disclosure Controls and Procedures

An assessment of Migao's internal control over financial reporting including disclosure controls and procedures has been conducted for the fiscal year ended March 31, 2013. Refer to Internal Control over Financial Reporting section below for details. There have been no material changes in our controls over financial reporting including disclosure controls and procedures during the 3 month quarter ended June 30, 2013.

Internal Control over Financial Reporting

Management is also responsible for the design of internal controls over financial reporting in order to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with IFRS. For the year ended March 31, 2013, an assessment has been conducted under supervision of management. Professionals from Risk Enterprise Services of an independent public accounting firm ("the Firm") have been engaged to assist the management in assessing the design and operating effectiveness of the internal controls over financial reporting at the corporate office and certain operating facilities in China. As of August 14, 2013, majority of the in-scope work has been completed and no significant internal control findings have been reported. The internal control assessment findings report is in the process of being finalized pending for the verification of certain information by the Firm. Management expects the final assessment findings report will be available in Q2 of fiscal 2014.

Other control factors that readers should be aware of include the fact that the Company maintains a lean financial department in which finance staff are cross-trained to handle non-compatible functions in case of emergency, illness, staff turnover or other situations. This cross-training could result in a lack of segregation of duties. Management mitigates this risk by tracking when incompatible functions are performed and providing additional review and oversight at such times. Despite management's best efforts, there can be no assurance that the risk of material misstatement occurring during such periods can be reduced.

It should be noted that while the officers of the Company have certified the Company's Annual Filings, they do not expect that the disclosure controls and procedures or internal controls over financial reporting will prevent all errors and fraud. A control system, no matter how well conceived or implemented, can only provide reasonable, not absolute, assurance that the objectives of the control system are met. Further, no evaluation of controls can provide absolute assurance that all control issues within a company will be detected.

There have been no changes in our internal control over financial reporting during the quarter ended June 30, 2013 that have materially affected, or are reasonably likely to materially affect, internal control over financial reporting.

Capital Structure

The Company is authorized to issue an unlimited number of common shares and unlimited number of preference shares, each common share providing the holder with one vote. As of August 14, 2013, there were:

- 52,496,160 common shares outstanding.
- 2,076,666 stock options outstanding, with exercise prices of between $3.75 to $6.40, and weighted average remaining life of 3.96 years. 1,420,666 of these stock options are exercisable as of August 14, 2013.

Off-Balance Sheet Arrangements

The Company does not have any off-balance sheet arrangements that have, or are reasonably likely to have, a current or future effect on the results of operations or financial condition of Migao including, without limitation, such considerations as liquidity and capital resources that have not previously been discussed.

Transactions with Related Parties

As at June 30, 2013, the Group owes SQM JV $8,252 for natural gas, ammonium nitrate, liquid ammonium nitrate project expenses, logistics expenses, utilities, and salaries expenses of which SQM JV's paid on the Group's behalf. (March 31, 2013 - $3,638)

SQM JV is the Company's joint venture partner, which owns 50% interest in the SQM JV and SQM Europe is a subsidiary of SQM. The amount is interest-free, unsecured and due within 210 days from the date of invoice.

Seasonal Nature of Business

The Group's results for the three-month period ended June 30, 2013 are not necessarily indicative of the results that may be expected for the full year due to seasonal variations in customer order volumes. The third and fourth quarters of the fiscal year account for, and are expected to account for, a greater portion of revenue and earnings than do the first and second quarters of each fiscal year. During the low season in the current interim period, certain production plants of the subsidiaries have been produced at lower production capacities. This seasonal pattern causes the Group's operating revenue and net income to vary significantly from quarter to quarter.

Proposed Transactions

Migao is not a party to any proposed transaction or proposed asset or business acquisition or disposition, with the exception of the expansion plans described below, that may have an effect on the financial condition, results of operations or cash flows.

Outlook

Based on market information and estimates of Chinese specialty potash fertilizer companies, management believes Migao is positioned to be a leading producer of specialty potash fertilizer in the Chinese market. The first quarter of fiscal 2014 experienced improved sales volumes as market conditions reversed the negative trend of the last few quarters. Hydrochloric acid pricing also saw slight improvements.

Sichuan Migao

It is anticipated that Sichuan Migao will produce at full annual production capacity of 80,000 tonnes of potassium nitrate for fiscal 2014.

Guangdong Migao

At full capacity, Guangdong Migao produces 160,000 tonnes of potassium sulphate and 192,000 tonnes of HCL. As a result of continued Hydrochloric Acid market weakness, it is anticipated that Guangdong Migao will be at approximately 50% of capacity for fiscal 2014.

Changchun Migao

It is anticipated that Changchun Migao will be at 60% of its 80,000 tonnes per year of potassium sulphate capacity for fiscal 2014.

Liaoning Migao

It is anticipated that Liaoning Migao will be at 80% capacity for fiscal 2014.

Joint Venture with SQM

It is anticipated that the JV will be at 90% of the total annual 40,000 tonnes of potassium nitrate production capacity for fiscal 2014.

Shanghai Migao

This facility will produce at 40% - 65% capacity for fiscal 2014, however the production and deliveries could be seasonal.

Zunyi Migao

This facility will produce at 40% - 65% capacity for fiscal 2014, however the production and deliveries could be seasonal..

Tianjin Migao

A 215,000 square foot warehouse has been constructed at Tianjin Migao to handle distribution of products such as inbound potash and outbound industrial potassium nitrate. The Tianjin property is located near a deep water port. A potassium sulphate facility with 40,000 tonnes of initial annual capacity is being considered also for this site as local market demand increases.

Yunnan Migao

A wholly-owned subsidiary in Yunnan province was approved by Boards during the quarter. Total registered capital is 60 million RMB, and the Company has completed its first capital injection on July 2, 2013 for 12 million RMB.

In the future development of YN Migao, the Group also plans to create a joint venture with OJSC EuroChem Mineral Chemical Company, Russia's largest fertilizer producer and a top ten agrochemical company globally, to produce up to 60,000 tonnes of potassium nitrate and up to 200,000 tonnes of chloride-free NPK fertilizers. The joint venture has not yet been established up till the report date.

Capital Expenditure Summary

For the quarter ended June 30, 2013, the total capital expenditure paid for all of the expansion projects noted above as well as plant and equipment additions was $1.0 million.

Critical Accounting Policies

This MD&A should be read in conjunction with the Company's unaudited condensed consolidated financial statements for the quarter ended June 30, 2013 and the audited consolidated financial statements for the year ended March 31, 2013 and the notes thereto. Those Consolidated Financial Statements outline the accounting principles and policies used to prepare our financial statements. Accounting policies are critical if they rely on a substantial amount of judgment in their application or if they result from a choice between accounting alternatives and that choice has a material impact on reported results or financial position.

The judgments that management has applied in the application of accounting policies and related estimates that have the most significant effect on the amounts recognized are discussed in note 2 of the Company's June 30, 2013 condensed interim financial statements.

In the current interim period, the Group has applied for the first time IFRS 10, IFRS 11, IFRS 12 and IAS 28 (as revised in 2011) together with the amendments to IFRS 10, IFRS 11 and IFRS 12 regarding the transitional guidance. The impacts of the application of these standards are discussed in note 3 of the Company's June 30, 2013 condensed interim financial statement.

Risk Factors

The Company is exposed to a variety of risks in the normal course of operations. For the Company's risk factors, refer to the risk factors section of the Company's Annual Information Form dated June 27, 2013 for the year ended March 31, 2013 filed with the Canadian securities regulators, which is available on SEDAR at www.sedar.com.