

# NEMI Northern Energy & Mining Inc.

## Management's Discussion and Analysis of Financial Position and Results of Operations

The following information, prepared as of May 7, 2009, should be read in conjunction with the unaudited consolidated financial statements of NEMI Northern Energy & Mining Inc. ("NEMI" or the "Company") for the six months ended March 31, 2009, as well as the audited consolidated financial statements for the year ended September 30, 2008, and the related management's discussion and analysis (the "Annual MD&A"). All amounts are expressed in Canadian dollars unless otherwise indicated.

### *Forward-Looking Statements*

Forward-looking statements look into the future and provide an opinion as to the effect of certain events and trends on the business. Forward-looking statements may include words such as "plans", "intends", "anticipates", "should", "estimates", "expects", "believes", "indicates", "suggests" and similar expressions.

This MD&A, and in particular the "Outlook" and "Peace River Coal LP" sections, contains forward-looking statements. These forward-looking statements are based on current expectations and various estimates, factors and assumptions and involve known and unknown risks, uncertainties and other factors.

It is important to note that:

- Unless otherwise indicated, forward-looking statements in this MD&A describe the Company's expectations as of May 7, 2009.
- Readers are cautioned not to place undue reliance on these statements as the Company's actual results, performance or achievements may differ materially from any future results, performance or achievements expressed or implied by such forward-looking statements if known or unknown risks, uncertainties or other factors affect the Company's business, or if the Company's estimates or assumptions prove inaccurate. Therefore, the Company cannot provide any assurance that forward-looking statements will materialize.
- The Company assumes no obligation to update or revise any forward-looking statement, whether as a result of new information, future events or any other reason.

The material assumptions that were applied in making the forward looking statements in this MD&A include the future business prospects of the Peace River Coal Limited Partnership.

For a description of material factors that could cause the Company's actual results to differ materially from the forward-looking statements in this MD&A, please see "General" and "Risks and Uncertainties".

### *General*

NEMI is a Canadian company incorporated under the Business Corporations Act of Alberta and extra-provincially registered under the Business Corporations Act of British Columbia.

On November 29, 2006, the Company concluded an agreement with Hillsborough Resources Limited ("Hillsborough") and Anglo Coal Canada Limited ("Anglo"), indirectly a wholly-owned subsidiary of Anglo American plc, wherein the north-eastern British Columbia metallurgical coal assets of the Company, Hillsborough and Anglo have been consolidated into a new entity, Peace River Coal Limited Partnership ("Peace River Coal LP") which, as at March 31, 2009, is owned 74.5% by Anglo, 13.4% by Hillsborough, and 12.1% by NEMI. The assets transferred to Peace River Coal LP by the Company include the Trend mine and related facilities, and NEMI's 50% interest in the Belcourt Saxon Coal Limited Partnership.

The Company's principal assets are accordingly the interests it holds in Peace River Coal LP.

Significant risk factors affecting the development of Peace River Coal LP's properties include the determination of coal resource to support mine operations; the successful execution of mine plans; the long term strength of metallurgical coal markets; and the ability to secure permits should commercial production from properties be demonstrated to be feasible. It is expected that the capital requirements to develop the various properties now held within Peace River Coal LP over the coming years will be significant. Accordingly, the Company's investment in Peace River Coal LP is subject to financing and dilution risk.

### ***Peace River Coal LP***

On October 13, 2006, the Company signed an asset transfer agreement among the Company, Anglo, and Hillsborough whereby the three parties agreed to combine their respective northeast British Columbia metallurgical coal assets and interests (the "Transaction"). In addition, the Company voluntarily sought and obtained protection under the *Companies' Creditors Arrangement Act* ("CCAA") pursuant to an Order of the Supreme Court of British Columbia (the "Court").

The purpose of obtaining the Order was to afford the Company an opportunity to preserve the going concern value of its assets pending completion of the Transaction. Under the Order, the Company was authorized to obtain debtor-in-possession financing comprised of a \$20 million credit facility to be provided by Anglo (the "DIP Loan"). The DIP Loan was secured by a first-priority charge on the Company's assets. The Transaction also formed the basis for the Company's CCAA Plan of Arrangement, which was approved by the Court on November 23, 2006.

On November 29, 2006, the Company successfully closed the Transaction, which resulted in the creation of the Peace River Coal LP, initially owned as to 60% by Anglo and 20% by each of the Company and Hillsborough. On the closing of the Transaction, the Company received a \$10 million cash payment, including \$3.5 million held in trust pending resolution of whether a break fee was payable to Western Canadian Coal Corp. ("Western") (subsequently settled by the Company paying \$1.275 million to Western), and a free cash carry in the Peace River Coal LP to December 31, 2007 to a maximum of \$18 million. In addition, the DIP Loan provided by Anglo during CCAA proceedings was assumed by the Peace River Coal LP and all of the Company's creditors, secured and unsecured, were paid in full, including Anglo and Itochu Corporation. Following the closing of the Transaction, the Company filed with the Court a closing certificate which resulted in the Company's full emergence from CCAA protection.

The Company accounts for its interest in the Peace River Coal LP under the equity method. Upon formation, the net book value of the net assets of the Peace River Coal LP was \$173 million and the partnership accounts of Anglo, the Company and Hillsborough were credited with the amounts of \$103.8 million (60%), \$34.6 million (20%) and \$34.6 million (20%), respectively, being the fair values of contributed property interests as determined by a formal valuation process and as agreed by the parties.

The Peace River Coal LP was formed pursuant to and is governed by a limited partnership agreement made as of October 16, 2006, and as amended November 24, 2006. Under the terms of the limited partnership agreement, the partners are not obliged to fully participate in any of the partnership's programs and budgets, but they are subject to dilution provisions should they elect not to fully participate.

In May 2007, the Peace River Coal LP delivered its 2007 Program and Budget, including capital expenditures and working capital to fund net operating losses through the pre-commercial operation phase, for expenditures amounting to \$53 million, of which the Company's 20% share was \$10.6 million and was funded by the free cash carry. Hillsborough elected not to participate in either the 2007 Program and Budget or its share of NEMI's carry, allowing its interest in the partnership to be diluted to 14.1%.

The Peace River Coal LP subsequently approved a 2007 Supplemental Program and Budget for expenditures amounting to \$25 million, of which the Company's 20% share was \$5 million and was also funded by the free cash carry. The cash calls for the 2007 Programs and Budgets increased the partners' equity, prior to considering results of operations, to \$251 million, with the Company's partnership account at \$50.2 million representing a 20% interest in the Peace River Coal LP. For the 2007 Programs and Budgets, the Company used \$15.6 million of its \$18 million free cash carry, leaving \$2.4 million unused.

The 2008 Program and Budget called for expenditures amounting to \$198 million, of which the Company's 20% share was \$39.6 million. The Company elected to participate in the amount of \$5 million, and as a result it was expected that

the Company's interest in the Peace River Coal LP would be diluted, on a provisional basis, to approximately 12% (the "Provisional Interest") as of December 31, 2008. On December 24, 2007, the Peace River Coal LP made an initial \$14.1 million cash call in respect of the 2008 Program and Budget, of which the Company's share was \$1.7 million based on its Provisional Interest. The Company funded the \$1.7 million cash call and took the position that any cash calls until December 31, 2007 should be covered by the free cash carry (of which \$2.4 million remained unused). The parties are currently undertaking a resolution process and hope to have the matter determined within the next 90 days. The return of the \$1.7 million would be recorded as a gain if received.

During the calendar year ended December 31, 2008, the Peace River Coal LP approved Supplemental Programs and Budgets for the Trend Transition Project and existing operations for aggregate expenditures amounting to \$101 million, of which the Company's share was \$12.1 million based on its Provisional Interest. The Company elected to fully fund its share of these Supplemental Programs and Budgets. For the calendar year ended December 31, 2008, the partners of the Peace River Coal LP were presented with aggregate Programs and Budgets totaling \$299 million, of which the Company elected to fund \$17.1 million. Actual cash calls in respect of those Programs and Budgets totaled \$289 million, with the Company funding \$15.9 million. At year end, the Peace River Coal LP recalculated the Company's and Hillsborough's partnership interest based on actual contributions and distributions, resulting in the Company's partnership interest being reduced to 12.0% and the Company receiving a rectifying cash distribution of \$16 million. As a result of the change in the methodology used in accounting for cash calls and distributions, the Company is at this time seeking credit for the entire unused portion of its original free cash carry plus interest, as the Company is of the view that the new methodology, if applied to 2007, would have resulted in the entire free cash carry being used. This matter is being considered as part of the resolution process mentioned above.

The Peace River Coal LP's 2009 Program and Budget calls for expenditures amounting to \$225 million, of which the Company's pro rata share is \$27 million. The Company has elected to fully fund its share of the 2009 Program and Budget. In the first three months of calendar 2009, the Peace River Coal LP made \$40.3 million in cash calls in respect of the 2009 Program and Budget, of which the Company's share was \$4.8 million. In addition to funding these cash calls, the Company also paid \$0.5 million to fund shortfalls created by Hillsborough's failure to fund its proportion of the January 2009 cash call. As a result of these payments and the penalty imposed on Hillsborough for failing to fund its cash call, as at March 31, 2009, the Company's interest in the Peace River Coal LP increased to 12.1%, Anglo's interest increased to 74.5%, and Hillsborough's interest was reduced to 13.4%. In March 2009, the Peace River Coal LP made a cash distribution of \$3.4 million, of which the Company received \$0.4 million.

### ***Aviva Transaction***

In October 2008, the Company and Aviva Corporation entered into a merger implementation agreement ("Agreement") to combine the businesses of the two companies to create a new international coal and energy group (the "Merger"). The Merger was expected to be completed by way of an Aviva scheme of arrangement in Australia, with the Company issuing 0.59 shares for each Aviva share held at completion. Upon closing, it was expected that the existing shareholders of the Company and the former shareholders of Aviva would each hold approximately 50% of the share capital of the merged group on a diluted basis taking into account NEMI's outstanding convertible debentures. The completion of the Merger was subject to the approval of the shareholders of both companies, regulatory authorities in Canada and Australia, and the Australian Courts.

In December 2008, Aviva cancelled the transaction, citing a material adverse change in the affairs of the Company caused by the Company's interest in PRC being diluted to 12%. Consequently, the Company paid a break fee of \$1 million to Aviva. The Company incurred \$324,000 in due diligence costs to September 30, 2008 and a further \$360,000 in costs during the six months ended March 31, 2009 associated with the Merger.

### ***Results of Operations***

#### ***- Six Month Results***

The Company recorded a loss of \$2,126,415 (\$0.04 per share) for the six months ended March 31, 2009 (the "Current Period") as compared to net income of \$3,037,498 (\$0.05 per share) reported in the same period of 2008 (the "Comparative Period"). The loss in the Current Period, as compared to net income in the Comparative Period, is in management's view largely a result of non-recurring items.

Expenses for the Current Period increased to \$1,414,359 as compared to \$509,631 in the Comparative Period, a significant portion of which should be non-recurring. In the Current Period, the Company incurred significant expenses in connection with the failed merger with Aviva Corporation, including professional fees of approximately \$360,000 (which is in addition to the \$324,000 in professional fees incurred prior to September 30, 2008), as well as in connection with the contested election of directors at the Company's Annual General Meeting held on March 30, 2009, which result in the recording of professional/legal fees of approximately \$227,000 and proxy solicitation expenses of approximately \$234,000. Overall, professional fees increased to \$702,446 during the Current Period compared to \$40,342 in the Comparative Period, and advertising and shareholder relations expense increased to \$252,839 as compared to \$20,513 in the Comparative Period.

In the Current Period, an additional non-recurring charge of \$1,000,000 was recorded as a result of the break fee paid to Aviva. In the Comparative Period, the Company also recorded a non-recurring gain of \$5 million as a result of its free cash carry in the PRC, which of itself resulted in net income being reported in the Comparative Period.

During the Current Period, the Company also incurred \$832,672 in interest on the convertible debentures as compared to \$100,721 accrued in the Comparative Period, as the debentures were only issued and commenced accruing interest in the last month of the Comparative Period. Interest and other income, as a result of its surplus cash balance, decreased to \$134,730 as compared to \$192,130 in the Comparative Period, owing to a general decrease in interest rates during the Current Period.

In the Current Period, the Company also recorded income of \$980,000 as its estimated share of income from the Peace River Coal LP (which interest is being accounted for using the equity method), as compared to a loss of \$1,544,000 during the Comparative Period.

*- Second Quarter Results*

During the second quarter (the "Current Quarter"), the Company recorded a loss of \$65,320 (\$0.00 per share), compared to a loss of \$1,675,050 (\$0.03 per share) reported for the second quarter of 2008 (the "Comparative Quarter").

Expenses for the Current Quarter increased to \$794,026 from \$280,853 in the Comparative Quarter, a significant portion of which should be non-recurring. The increased professional fees and proxy solicitation expenses resulting from the contested election of directors at the Annual General Meeting, discussed above, largely occurred in the Current Quarter.

In the Current Period, the Company incurred \$411,761 in interest on the convertible debentures, as compared to \$100,271 in the Comparative Quarter. Interest and other income was \$41,668 as compared to \$82,421 in the Comparative Quarter.

In the Current Period, the Company recorded income of \$1,100,000 as a result of its interest in the Peace River Coal, as opposed to a loss of \$1,377,000 in the Comparative Quarter.

***Capital Expenditures and Investments***

Investing activity during the six months ended March 31, 2009 was comprised of \$10,653,371 (2008-\$4,820,607) in funds contributed to PRC and \$19,271,583(2008-\$nil) in distributions received from PRC..

### **Summary of Quarterly Results (unaudited)**

Three months ended	Mar. 31, 2009	Dec. 31, 2008	Sept 30, 2008	June 30, 2008	Mar. 31, 2008	Dec. 31, 2007	Sept 30, 2007	June 30, 2007
Total revenues	\$nil	\$nil	\$nil	\$nil	\$nil	\$nil	\$nil	\$nil
Net earnings (loss)	(\$65,320)	\$(2,061,094)	\$(167,597)	\$193,617	(\$1,675,050)	\$4,712,548	\$7,536,820	(\$1,012,376)
Income (loss) per share (Basic and diluted)	(\$0.00)	(\$0.03)	\$0.00	\$0.00	(\$0.03)	\$0.08	\$0.14	(\$0.02)
Deferred expenditures	\$nil	\$nil	\$nil	\$nil	\$nil	\$nil	\$nil	\$nil
Total assets	\$67,991,714	\$67,369,056	\$69,624,440	\$69,450,187	\$66,747,535	\$58,095,590	\$53,402,438	\$46,119,381

The loss for the quarter ended December 31, 2008 included a \$1 million break fee payment and \$358,000 in transaction costs associated with the cancelled Aviva transaction. The loss for the quarter ended March 31, 2008 was primarily due to the Company's share of the loss of PRC of \$1.38 million, respectively. The net earnings for the quarter ended December 31, 2007 includes a \$5,000,000 gain on the Company receiving a free cash carry in funding its portion of the PRC 2007 Supplemental Program and Budget of \$25 million. This gain was partially offset by an equity loss of \$167,000 in relation to the Company's interest in PRC. The net earnings for the quarter ended September 30, 2007 included a gain on asset transfer of \$8,457,225 offset by an equity loss of \$762,000 in relation to the Company's interest in PRC.

### **Financing Activities**

The Company issued \$12.7 million in unsecured convertible debentures on March 12 and April 1, 2008 for net proceeds of \$11.8 million. The Debentures are unsecured and bear interest at a rate of 8% per annum, payable semi-annually in arrears, on June 30th and December 31st each year commencing June 30th, 2008. The Debentures mature on March 12, 2013 and are convertible into common shares of the Company at any time up until maturity at a conversion price of \$0.90 per share. After March 12, 2010, the Company has the right, under certain circumstances, to redeem the debentures in whole or in part. In addition, the Company has the right to repay the principal amount of the Debentures in common shares at a price equal to 95% of the weighted average trading price of the Company's shares on the Toronto Stock Exchange for the 20 trading day period ending 5 trading days prior to the date fixed for redemption or at maturity.

In October 2006, in order to afford the Company an opportunity to preserve the going concern value of its assets as it worked to complete the Anglo/Hillsborough transaction, the Company voluntarily sought and obtained protection under the *Companies' Creditors Arrangement Act* ("CCAA") and was authorized to obtain debtor-in-possession financing comprised of a \$20 million credit facility to be provided by Anglo, with such facility to be secured by a first-priority charge on the Company's assets.

During the period ended December 31, 2006, the Company received \$17.9 million in loans from Anglo, including \$12.9 million under the terms of its DIP loan financing. On closing of the Anglo/Hillsborough transaction, all of the loan indebtedness of the Company, including accrued interest, was repaid or assumed directly by PRC.

### **Liquidity and Capital Resources**

The closing of the convertible debenture issue in 2008 has left NEMI in a strong financial position with \$16.7 million in cash and working capital of \$16.1 million at March 31, 2009 with the debentures not due until March 2013. The Company's aggregate operating, investing and financing activities during the three month period resulted in a net cash outflow in the amount of \$5.4 million.

## - Contractual Obligations

As at March 31, 2009, the Company's contractual obligations included:

(thousands of dollars)	Payments Due by Period				
	Total	Less than 1 year	1 – 3 years	3 - 5 years	After 5 years
Lease agreement for office premises	\$253	\$28	\$114	\$111	\$nil
Lease agreement for office (1)	\$485	118	\$367	\$0	\$nil
Total Contractual Obligations	\$738	\$146	\$481	\$111	\$0

(1) NEMI has sublet this office space at cost to Peace River Coal LP.

## Off-Balance Sheet Arrangements

The Company has not entered into any material off-balance sheet arrangements such as guarantee contracts, contingent interests in assets transferred to unconsolidated entities, derivative financial obligations, or with respect to any obligations under a variable interest equity arrangement.

## Transactions with Related Parties

During the six months ended March 31, 2009, consulting fees of \$39,000 (2008 - \$80,000) were charged in respect of services rendered by companies with common officers. Legal fees totaling \$nil (2008 - \$4,551) were charged by a legal firm in which a director was a member. Transactions with related parties are recorded at the exchange amount, being the price agreed between the parties.

## Critical Accounting Estimates

The Company's critical accounting estimates are as described in the Annual MD&A and include the review of the carrying values of coal properties and deferred exploration expenditures, the estimate of asset retirement obligations, the estimate of stock-based compensation expense and the valuation of the liability and equity components of the convertible debentures.

The Company has a 12% interest in Peace River Coal LP. Management reviews the carrying value of this investment on at least an annual basis. No write-down was taken during the current or previous periods, however, there is a risk that this investment could be written down in a future quarter.

## Recent Accounting Pronouncements

There are no recent accounting pronouncements impacting the current period's financial statements, except as disclosed in the Annual MD&A.

## Financial Instruments

The Company's financial instruments consist of cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities. It is management's opinion that the Company is not exposed to significant interest, currency or credit risks arising from these financial instruments. The fair values of these financial instruments approximate their carrying values, unless otherwise noted.

Cash and cash equivalents include cash and highly liquid investments held in the form of high quality commercial paper. These investments are stated at cost plus accrued value, which approximates market value. Investments of cash are of sufficient quality and diversity to ensure a high probability of liquidity at the accrued value, at such times as needed to meet financial obligations. Furthermore, the investment terms are less than three months at the time of acquisition.

## Outstanding Share Data

Authorized Capital:

- Unlimited number of Class A no par value voting common shares
- Unlimited number of Class B no par value non-voting common shares
- Unlimited number of Class C no par value non-voting common shares
- Unlimited number of Class D no par value non-voting, non-cumulative redeemable and retractable preferred shares

Issued and outstanding:

57,869,745 common shares as at May 7, 2009

Fully diluted:

71,841,967 common shares as at May 7, 2009

Outstanding options, warrants, and convertible securities as at May 7, 2009:

<u>Type of Security</u>	<u>Number</u>	<u>Exercise Price</u>	<u>Expiry date</u>
Convertible debentures	13,222,222	\$0.90	March 12, 2013
Stock options	650,000	\$0.90	April 1, 2013
Warrants	100,000	\$0.90	March 12, 2010

### ***Risks and Uncertainties***

The Company is involved in coal mining operations to the extent of its 12% partnership interest in Peace River Coal LP. The exploration for and development of coal deposits are highly speculative activities and are subject to significant risks. The Company's ability to realize its investments in exploration projects is dependent upon a number of factors, including its ability to continue to raise the financing necessary to complete the exploration and development of those projects and the existence of economically recoverable reserves within its projects. The Company's operations are subject to a number of risk factors as detailed in the Annual MD&A and in the Company's Annual Information Form dated December 23, 2008 and filed on SEDAR on December 29, 2008.

### ***Internal Control over Financial Reporting***

As at the date of this report, management is not aware of any change in the Company's internal control over financial reporting that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

### ***Outlook***

As at March 31, 2009, NEMI is in strong financial position with working capital of \$16.1 million after the issuance of \$12.7 million in convertible debentures in 2008. Management of NEMI intends to investigate and evaluate its continued investment in PRC as well as other business opportunities, including potential acquisitions of mineral assets.

PRC is being managed and operated by Anglo American which, with its extensive experience in coal mining and marketing, will play a key role in further developing British Columbia's northeast coalfields. PRC achieved commercial levels of production during the first quarter of 2008 and will also be carrying out field studies and making permitting applications for its other properties.

### ***Other Information***

Additional information related to the Company, including its Annual Information Form, is available for viewing on SEDAR at [www.sedar.com](http://www.sedar.com).