



XANADU MINES



2018 ANNUAL REPORT

Xanadu Mines Limited ASX | TSX: XAM
For the year ended December 31, 2018

Corporate Directory

Directors

Kevin Tomlinson	Independent Non-Executive Chairman
Andrew Stewart	Managing Director & Chief Executive Officer
Ganbayar Lkhagvasuren	Executive Director
Hannah Badenach	Non-Executive Director
Marcus Engelbrecht	Non-Executive Director
Darryl Clark	Independent Non-Executive Director
Michele Muscillo	Independent Non-Executive Director

Company Secretary

Phil Mackey

Registered Office - Australia

c/o Company Matters Pty Limited
Level 12, 680 George Street
Sydney NSW 2000
Tel: +61 2 8280 7497
Fax: +61 2 9287 0350

Registered Office - Mongolia

Suite 23, Building 9B
Olympic Street, Khoroo 1, Sukhbaatar District
Ulaanbaatar 14240
Tel: +976 11 7012 0211

Share Registry

Computershare Investor Services Pty Limited
Level 3, 60 Carrington Street
Sydney, NSW 2000
Tel: +61 1300 855 080

Auditor

Ernst & Young
200 George Street
Sydney, NSW 2000

Stock Exchange Listings



Xanadu Mines Ltd shares are listed on the Australian Securities Exchange and Toronto Stock Exchange (ASX and TSX code: XAM)

ABN 92 114 249 026

Contents

Overview

Letter from the Chairman	1
--------------------------	---

Governance

Management's Discussion and Analysis	2
Auditor's Independence Declaration	28

Financial Report

Statement of Profit or Loss and Other Comprehensive Income	29
Statement of Financial Position	30
Statement of Changes in Equity	31
Statement of Cash Flows	32
Notes to the Financial Statements	33
Directors' Declaration	54
Independent Auditor's Report to the Members of Xanadu Mines Ltd	55

Additional Information

ASX Additional Information	60
----------------------------	----

Letter from the Chairman

Dear Shareholder

2018 marks another year of solid progress for Xanadu Mines Ltd (“Xanadu”, “Xanadu Mines” or the “Company”) in which we have added to our track record of exploration success in Mongolia’s highly prospective South Gobi region and have turned our minds firmly towards bringing the globally significant Kharmagtai copper-gold project into an exciting period of cost-effective discovery and growth.

Prior to the start of 2018, Kharmagtai already stood out as one of the biggest and best undeveloped copper-gold projects in Asia. That status was further cemented in October 2018, with the release of an interim open-pit resource estimate for the project, delivering a 400% increase in contained copper and a 249% increase in contained gold.

As it stands now, Kharmagtai contains an open-pit indicated and inferred resource of 598 million tonnes (“Mt”) containing 1.9Mt copper and 4.3 million ounces (“Moz”) gold (129.3Mt indicated containing 0.5Mt copper and 1.5Moz gold and; 468.9Mt inferred containing 1.5Mt copper and 2.8Moz gold). A scoping study/preliminary economic assessment of the resource is due for completion in the first half 2019.

On the exploration front, arguably the most significant development was the discovery of a new “blind” porphyry copper-gold centre at Zaraa, approximately 2km east-southeast of the three porphyries deposits that make up the current Kharmagtai resource: Copper Hill, Stockwork Hill and White Hill. Zaraa was one of 19 large-scale priority targets identified by Xanadu in the Kharmagtai area and the discovery hole ended up producing the largest intercept of continuous mineralisation drilled at the project to date - 928 metres at 0.3% copper and 0.27 grams of gold per tonne (0.47% copper equivalent) from 458 metres.

Needless to say, Zaraa will elevate Kharmagtai to a new level. It was not included in the October 2018 resource update but will be factored into a new global resource estimate expected for release in the second half of 2019 and should have a positive impact on the overall scale, grade and economics of the project. It is worth noting that the future development of Zaraa could be aided by the delineation of the orebody closer to surface. The exploration team believes it has identified the surface expression of the mineralisation and is currently working to better define this oxide zone above the Zaraa porphyry deposit.

There remains much more untapped potential within the Kharmagtai tenements. To date, at least five mineralised porphyry centres have been identified out of the nine priority targets drilled, with ten targets remaining untested, representing an excellent strike rate. Zaraa and the nearby Golden Eagle oxide gold discovery, count amongst this number; the others require further drilling to firm up as genuine discoveries in the same vein.

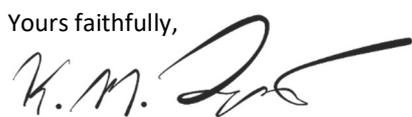
For a significant period during 2018, Xanadu had four rigs operating around the clock at Kharmagtai as it progressed with resource drilling. This level of activity would not have been possible without a robust balance sheet. The Company completed a share placement to institutional and sophisticated investors in June 2018, raising A\$10 million. As well as being well supported by existing shareholders, we were pleased to welcome several new international institutions as investors, and in a move designed to help build awareness of the Xanadu story in the North American market where companies such as Ivanhoe Mines were so successful, the Company listed its shares on the Toronto Stock Exchange in October 2018. We intend to maintain our primary listing on the Australian Securities Exchange (“ASX”) and believe that having a presence on the two-premier resource-focused stock exchanges in the world, will raise Xanadu’s profile and access to capital as we move forward.

As I write this address to our stakeholders, it is important to note that our exploration team has made a significant discovery of a new zone of bornite gold-rich porphyry mineralisation at Stockwork Hill that returned 102 metres grading 1.00% Cu and 1.67g/t Au (2.06% eCu or 3.23g/t eAu) from a depth of 572 metres. This hole has successfully demonstrated the existence of high-grade mineralisation along strike and at depth of the current open pit resource and represents an exciting new development for the project. We are very confident these results will provide the basis for a significant increase in the size and grade of the overall Kharmagtai deposit and have a positive impact on ongoing economic studies.

The long-term fundamentals for the global copper market remain sound, with the distinct lack of large, new projects forecast to give rise to a significant supply deficit over coming years. Kharmagtai is ideally located on the doorstep of the world’s largest copper consumer and stands to benefit from demand growth resulting from the “One Belt, One Road” initiative.

I would like to personally thank you for your support over the past 12 months. We look forward to unlocking more value from Kharmagtai and our other Mongolian exploration projects over the course of 2019.

Yours faithfully,



Kevin Tomlinson

Non-Executive Chairman
March 15, 2019

Management's Discussion and Analysis

General

This Management's discussion and analysis ("MD&A") is current to March 15, 2019 and is Management's assessment of the operations and the financial results together with future prospects of Xanadu Mines Ltd. This MD&A should be read in conjunction with the Company's audited consolidated financial statements for the years ended December 31, 2018 and 2017 and notes thereto, prepared in accordance with International Financial Reporting Standards ("IFRS"). Management is responsible for the preparation of the financial statements and this MD&A.

All dollar figures in this MD&A are expressed in Australian dollars ("A\$") unless stated otherwise.

This MD&A contains forward-looking statements and should be read in conjunction with the risk factors described in the "Risks and Uncertainties" and the "Cautionary Note Regarding Forward-Looking Information" sections at the end of this MD&A.

Additional information relating to the Company, including the Company's most recent financial reports, are available on SEDAR at www.sedar.com and on the ASX Announcements platform under the Company's code "XAM".

The information in this MD&A relating to the broader Kharmagtai Project is supported by the technical report titled "Independent Technical Report on the Kharmagtai Property, Mongolia" prepared by Andrew Vigar and Rod Graham of Mining Associates Limited, dated June 8, 2018.

The information in this MD&A that relates to Mineral Resources is based on information compiled by Dmitry Pertel who is responsible for the Mineral Resource estimate. Mr Pertel is a full-time employee of CSA Global and is a Member of the Australian Institute of Geoscientists, has sufficient experience relevant to the style of mineralisation and type of deposit under consideration and to the activity he is undertaking to qualify as the "Qualified Person" as defined in the CIM Guidelines and National Instrument 43-101. Mr Pertel consents to the inclusion in the report of the matters based on this information in the form and context in which it appears.

The information in this MD&A that relates to exploration results is based on information compiled by Dr Andrew Stewart who is responsible for the exploration data, comments on exploration target sizes, QA/QC and geological interpretation and information. Dr Stewart, who is an employee of Xanadu and is a Member of the Australian Institute of Geoscientists, has sufficient experience relevant to the style of mineralisation and type of deposit under consideration and to the activity he is undertaking to qualify as the "Competent Person" as defined in the 2012 Edition of the "Australasian Code for Reporting of Exploration Results, Mineral Resources and Ore Reserves" and the National Instrument 43-101. Dr Stewart consents to the inclusion in the report of the matters based on this information in the form and context in which it appears.

Forward-looking statements

This MD&A contains forward-looking statements, which are based on certain assumptions and analyses made by the Company derived from its experience and perceptions. The forward-looking statements in this MD&A are subject to important risks, uncertainties, and assumptions, which are difficult to predict and which may affect the Company's operations that may include, amongst other things, statements regarding targets, estimates and assumptions in respect of mineral reserves and mineral resources and anticipated grades and recovery rates, production and prices, recovery costs and results, capital expenditures and are or may be based on assumptions and estimates related to future technical, economic, market, political, social and other conditions. These 'forward-looking statements' are necessarily based upon a number of estimates and assumptions that, while considered reasonable by Xanadu, are inherently subject to significant technical, business, economic, competitive, political and social uncertainties and contingencies and involve known and unknown risks and uncertainties that could cause actual events or results to differ materially from estimated or anticipated events or results reflected in such forward-looking statements. The words 'believe', 'expect', 'anticipate', 'indicate', 'contemplate', 'target', 'plan', 'intends', 'continue', 'budget', 'estimate', 'may', 'will', 'schedule' and similar expressions identify forward-looking statements. The forward-looking statements included in this MD&A are made as of the date of this MD&A and other than as required by law, the Company disclaims any intention or obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

Description of Business

Xanadu is an Australian and Canadian listed public company with its shares traded on the Australian ("ASX") and Toronto Stock Exchange ("TSX") under the code "XAM". The principal activity of the Company (and its subsidiaries) is copper-gold exploration in Mongolia. The Company holds interests in three tenements: the Kharmagtai copper-gold project, the Red Mountain copper-gold project and Yellow Mounting copper project (Figure 1).

Management's Discussion and Analysis

continued

Review of Operations

Xanadu continued to make significant progress in its Mongolian copper and gold strategy over the 12 months ended December 31, 2018. The Company controls one of the most promising porphyry copper and gold projects in Asia with Kharmagtai, and has a portfolio of advanced district-scale exploration projects including Red Mountain and Yellow Mountain (Figure 1).

The planned exploration programs, among the largest to be undertaken by a junior ASX-TSX-listed exploration company last year, targeted the discovery of additional copper-gold deposits on the Company's South Gobi porphyry projects at Kharmagtai and Red Mountain where a total of 26,700 metres of diamond drilling, 8,333 metres reverse circulation drilling, and 5,600 metres of Polycrystalline Diamond Composite ("PCD") drilling was completed during the 2018 calendar year (Figure 2).

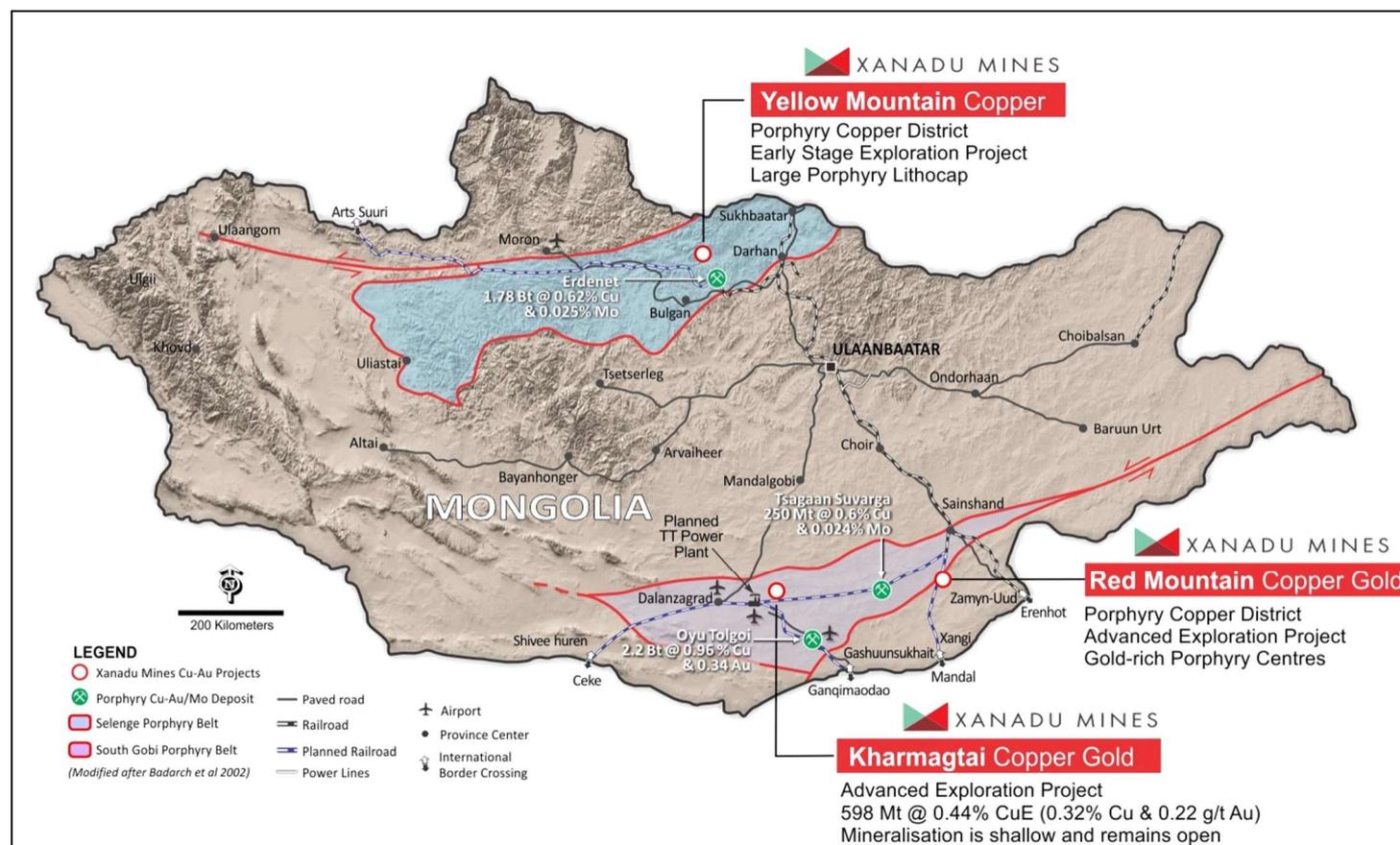


FIGURE 1: Location of Xanadu's copper-gold projects, within Mongolia's highly mineralised and vastly underexplored mineral belts. The resource figure above (598Mt) includes both indicated (129.3Mt) and inferred (468.9Mt) resource categories. Both at the same 0.3eCu cut-off grade. See ASX|TSX release of October 31, 2018.

Kharmagtai Copper-gold Project (Xanadu earning up to 76.5%)

The flagship Kharmagtai project has continued to emerge as one of the premier undeveloped copper and gold assets globally. The project is located within the Omnogovi Province, approximately 420 kilometres southeast of Ulaanbaatar and 120 kilometres north of the Rio Tinto-controlled Oyu Tolgoi deposit. Xanadu and its joint venture partner, Mongol Metals LLC, announced the acquisition of a 90% interest in the Kharmagtai porphyry copper-gold project from Turquoise Hill Resources in February 2014. Under the Mongol Metals LLC joint venture terms, Xanadu has earned an 85% interest in the Kharmagtai project, equivalent to a 76.5% effective interest, by funding acquisition and exploration costs.

The Kharmagtai project is key to Xanadu's short-term growth. Previous exploration has focused on the three outcropping porphyry deposits (Stockwork Hill, White Hill and Copper Hill) in the central part of Mining Licence 17387A. In addition to these three deposits, the prospective rocks of the Kharmagtai Igneous Complex are covered by either younger unconsolidated gravels or are obscured by younger rocks.

Exploration in 2018 was designed with a dual strategy to expand current resources and identify new, high-grade porphyry deposits under shallow cover. This strategy resulted in the discovery of the Zaraa deposit, a new, large scale porphyry discovery and the expansion of the 2015 resource by 400% in contained copper and 249% in contained gold within the open cut.

Management's Discussion and Analysis

continued

Updated mineral resource estimate

The Company's updated Mineral Resource Estimate is the first Resource estimate completed since the maiden Resource announced in March 2015 (ASX release dated March 19, 2015). The upgraded interim Mineral Resource Estimate is summarised in Table 1. The Mineral Resources are quoted above 0.3% CuEq cut-off within a conceptual constraining open pit shell. The parameters used to generate an optimised ultimate open pit shell are provided in Table 2.

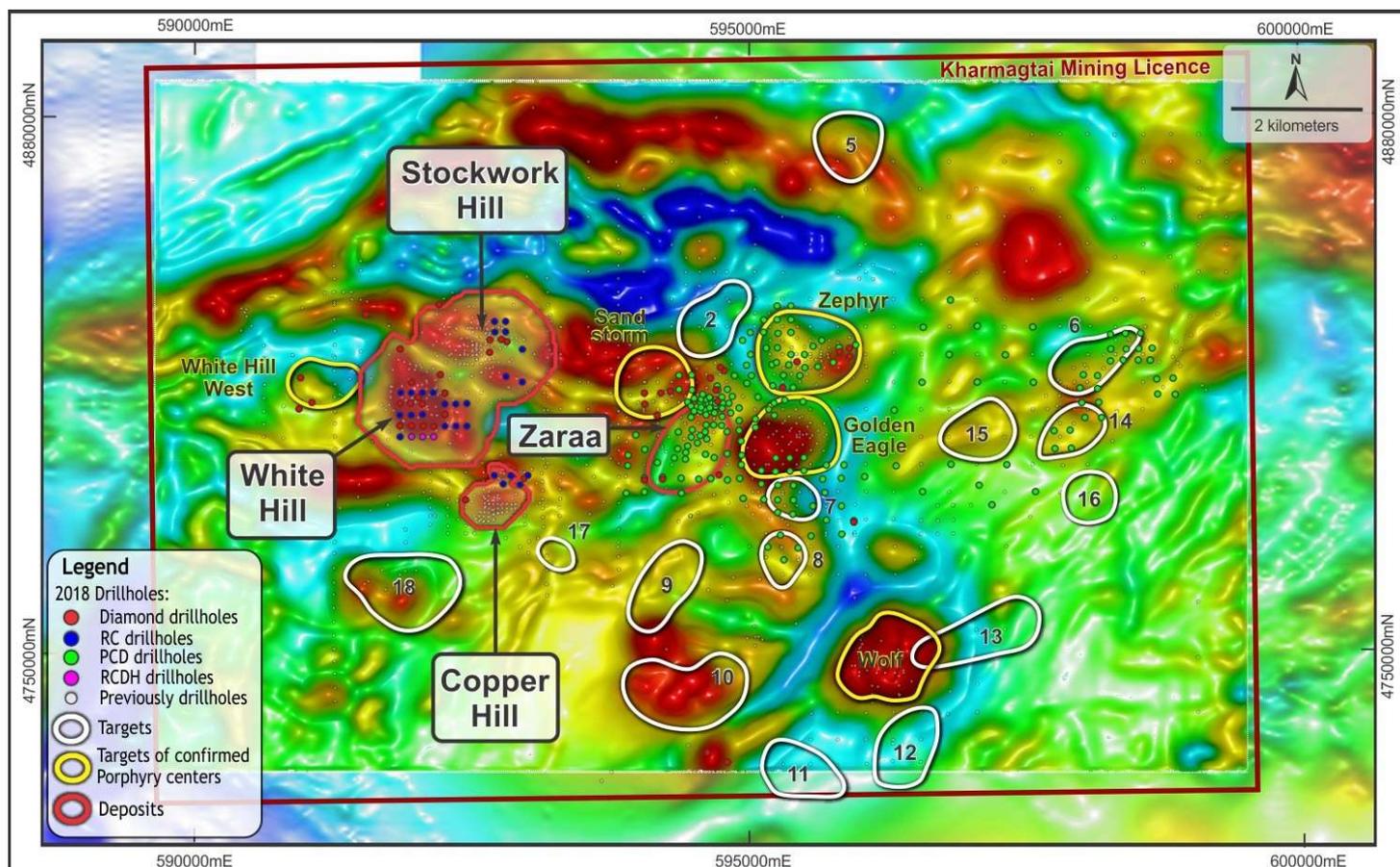


FIGURE 2: The Kharmagtai Mining License showing known porphyry deposits, new targets and holes completed in 2018.

The resource models are well understood and there is significant upside potential to be realised by better understanding the economics of the deposit. As demonstrated in the images above, significant volumes of mineralisation have been modelled that fall outside of the constraining pit wireframe. These parts of the model will be targeted for further investigation through economic studies to assess if more of this material can be brought into the Mineral Resource.

Table 1: Interim Kharmagtai Mineral Resource Estimate

Deposit	Classification	Tonnes		Grades			Contained Metal		
		Mt	CuEq, %	Cu, %	Au, g/t	CuEq, Kt	Cu, Kt	Au, Koz	
White Hill	Indicated	45.2	0.42	0.30	0.23	189	135	340	
Stockwork Hill		74.4	0.59	0.38	0.41	441	286	972	
Copper Hill		9.7	0.76	0.48	0.54	73	47	167	
Total Indicated		129.3	0.54	0.36	0.36	703	468	1,479	
White Hill	Inferred	412.8	0.40	0.31	0.17	1,653	1,299	2,227	
Stockwork Hill		55.4	0.47	0.30	0.34	263	167	601	
Copper Hill		0.7	0.39	0.31	0.16	3	2	4	
Total Inferred		468.9	0.41	0.31	0.19	1,919	1,468	2,832	

- Mineral Resources are classified according to JORC 2012.
- Mineral Resources for open pit mining are estimated within the limits of an ultimate pit shell.
- A cut-off grade of 0.3% CuEq has been applied for open pit resources.

Management's Discussion and Analysis

continued

- Density values of 2.65 t/m³ for oxide zones; 2.76, 2.74, 2.73 and 2.71 t/m³ for country rocks, 2.78, 2.80, 2.77, 2.81 and 2.76 t/m³ for porphyries and 2.76 t/m³ for andesite dyke were used for the model cells.
- CuEq – copper equivalent was calculated using conversion factor 0.62097 for gold. Metal prices used were 3.1 \$/lb for copper and 1320 \$/oz for gold, recoveries – 70% for gold and 85% for copper (82.35% relative gold to copper recovery), copper equivalent formula applied: $CuEq = Cu + Au * 0.62097 * 0.8235$.
- Rows and columns may not add up exactly due to rounding.

The updated Mineral Resource Estimate incorporates the results from all drill programs completed since 2015 including the latest infill drilling program which was completed in the September 2018 quarter and totalled approximately 8,725m in 27 drill holes. The primary aim of the drilling program was to infill the deposit within the conceptual pit to focus on converting the Inferred Mineral Resource to the Indicated category.

The completed JORC (2012) Resource demonstrates that the mineralisation is robust and continuous with over 22% of the Resource classified in the Indicated Mineral Resource category. The substantial increase in the updated Mineral Resource Estimate combined with higher confidence from the recent drilling is expected to positively impact the life of mine at Kharmagtai. Table 3 provides a summary of the Resource model at various cut off grades.

Xanadu is now focused on the completion of the Scoping Study which is expected in the June 2019 quarter and is expected to reflect the Company's strategy of delivering a significant Resource upgrade, with an initial focus on a higher-grade open pit starter project to demonstrate project economics. The optimal marginal cut-off for Resources is under review as part of the Scoping Study with consideration of a cut-off of approximately 0.6% CuEq.

Table 2: Constraining Pit Parameters

Parameters	Units	Value
1. Mining		
Ore mining cost	\$/t	2.49
Waste mining cost	\$/t	2.49
Mining losses	%	0
Mining dilution	%	5
2. Processing		
Processing cost (including G&A costs)	g/t	4.2
Processing recovery:		
Gold	%	70
Copper	%	85
3. Pricing		
Elements price:		
Gold	\$/oz	1,320
Copper	\$/t	6,834
Selling cost for Au	\$/oz	4
Selling cost for Cu	\$/t	1,030
4. Other to optimization		
SG parameters	t/m ³	2.75
General pit slopes	°	50

Table 3: Grade-tonnage table summary

Cut-Off	Mining	Resource	Material	CuEq (%)	Cu (%)	Au (g/t)	Cu (kt)	Au (Koz)	CuEq
0.2	OC	Indicated	187.6	0.45	0.31	0.29	572.5	1737.0	848.8
0.2	OC	Inferred	854.5	0.34	0.26	0.15	2205.6	4228.6	2878.2
0.2	Total	Ind + Inf	1042.1	0.36	0.27	0.18	2778.1	5965.6	3727.0
0.3	OC	Indicated	129.3	0.54	0.36	0.36	468.0	1478.9	703.2
0.3	OC	Inferred	468.9	0.41	0.31	0.19	1468.2	2831.7	1918.6
0.3	Total	Ind + Inf	598.2	0.44	0.32	0.22	1936.2	4310.6	2621.8
0.4	OC	Indicated	80.0	0.67	0.43	0.46	346.0	1172.7	532.5
0.4	OC	Inferred	189.9	0.50	0.38	0.24	718.5	1479.1	953.7
0.4	UG	Indicated	2.3	0.59	0.40	0.37	9.1	27.1	13.4

Management's Discussion and Analysis

continued

0.4	UG	Inferred	28.4	0.51	0.38	0.26	106.6	232.9	143.7
0.4	Total	Ind + Inf	300.6	0.55	0.39	0.30	1180.2	2911.8	1643.3
0.5	OC	Indicated	49.4	0.80	0.51	0.57	251.1	912.2	396.2
0.5	OC	Inferred	68.2	0.60	0.44	0.33	297.3	723.4	412.4
0.5	UG	Indicated	1.5	0.67	0.45	0.44	6.6	20.6	9.9
0.5	UG	Inferred	8.3	0.63	0.44	0.37	36.7	98.4	52.4
0.5	Total	Ind + Inf	127.4	0.68	0.46	0.43	591.7	1754.6	870.9
0.6	OC	Indicated	33.0	0.93	0.57	0.69	189.6	736.1	306.7
0.6	OC	Inferred	20.7	0.75	0.50	0.49	103.8	323.9	155.3
0.6	UG	Indicated	0.9	0.75	0.49	0.50	4.5	14.9	6.9
0.6	UG	Inferred	3.9	0.74	0.49	0.49	19.1	60.8	28.7
0.6	Total	Ind + Inf	58.5	0.85	0.54	0.60	317.0	1135.7	497.6

Geology and geological interpretation

New geological understanding of intrusive units and structures controlling mineralisation at Kharmagtai has driven the formation of a high-quality 3D geological model. This 3D geological model was used to define hard boundaries around which the Mineral Resource Estimate could be built, resulting in a more realistic and accurate estimation. The 3D model was based on a complete relogging of the +110km of diamond drilling conducted within the Mineral Resource volume over the past 30 years. This relogging has standardised the geology across the deposits and many phases of drilling/previous loggers, allowing a high-quality 3D model to be generated. This model not only forms a robust framework for the mineral resource update but allows predictions as to extensions to the deposits to be identified and drilled.

3D geological wireframes were developed for all major geological formations of the deposits, including country rock, all porphyry phases, andesite dykes and breccia pipes. The base of oxidation surface was developed based on geological logging and used to domain the deposits. In addition, three wireframe solid models were developed for the level of veining: <0.5%, 0.5 to 1.5% and >1.5% of veining for each deposit. All geological domains were sub-domained using the wireframes for veining and divided into oxidised and fresh material.

The additional drilling incorporated in the Updated Mineral Resource Estimate and other exploration and evaluation programs such as relogging of historic core, geophysical review and geochemistry studies, have delivered superior understanding of the deposit geometry. This has led to greater confidence in the geological and grade continuity and has infilled several areas of the deposit. These programs have collectively allowed us to deliver a more robust and larger Mineral Resource.

Drilling techniques

The Mineral Resources have been estimated using all available analytical data. This has included diamond core drilling (NQ, PQ and HQ, reverse circulation percussion drilling and in some areas channel samples taken at surface. Additional data on drilling and sampling procedures is provided in Table 1.

Significant drilling has taken place since the last Resource in 2015, which has driven the increase in resources. The drilling pre-2015 and since the last resource is provided in the collar plan and Table 4.

Table 4. Drill hole summary

Timing	Reverse Circulation	Metres	Diamond Core	Metres	RC and Diamond	Metres	Trenches	Metres
Drilling <2015	155	24553	252	88511.1	0	0	106	39774
Drilling >2015+	68	13107	116	57876.7	22	5323.1	17	5618
Total	223	37660	368	146387.8	22	5323.1	123	45392

Estimation methodology

A block model was created to encompass the full extent of the Kharmagtai deposits (White Hill, Copper Hill and Stockwork Hill - other exploration areas were excluded). The block model used a parent cell size of 20 m(E) x 20 m(N) x 20 m(RL) with sub-celling to 4 m(E) x 4 m(N) x 4 m(RL) to maintain the resolution of the wireframed geological domains and rock types.

An empty block model was created within the closed wireframe models for the geological domains, rock types, barren dykes, level of veining (stockwork) and breccia. The model was also coded according to the oxide zones. Each modelled geological domain was

Management's Discussion and Analysis

continued

assigned several unique codes in the model file (geology, veining and breccia). The block model was then restricted below the topography surface.

Copper and gold grade values were interpolated into the empty block models separately for each modelled geological domain of the deposits using the Ordinary Kriging method. The Ordinary Kriging process was performed at different search radii until all cells were interpolated. The search radii were determined for each domain based on the parameters of the modelled semi-variogram ranges averaged for each direction for copper and gold. The blocks were interpolated using only assay composites restricted by the corresponding domain for each deposit. When model cells were estimated using radii not exceeding the full semi-variogram ranges, a restriction of at least three samples from at least two drill holes or trenches was applied to increase the reliability of the estimates.

Criteria used for classification

The classification level was based upon an assessment of geological understanding, geological continuity, mineralization continuity, drill hole spacing, QC results, search and interpolation parameters and an analysis of available density information.

The following approach was adopted:

- Measured Resources: Not reported.
- Indicated Resources: Were classified where the drill density did not exceed 65 m x 65 m with at least two mineralisation intersections on a drilled cross section. Geological and structural continuity have been interpreted with moderate confidence levels and blocks were interpolated at least the second run.
- Inferred Resources: Inferred Mineral Resources was assigned to all model blocks lying outside the Indicated wireframes, which still display reasonable strike continuity and down dip extension, based on the current drill hole and trench intersections.

Cut-off grades

The Mineral Resources have been reported above a cut-off of 0.3% CuEq for open pit mining and above 0.5% CuEq for potential underground mining areas and are current to October 1, 2018.

Copper equivalent grade values were calculated in the block model post estimation of copper and gold grades. The following formula was applied to each cell in the block model: $CuEq = Cu + Au * 0.62097 * 0.8235$,

where:

Cu	-	copper grade (%)
Au	-	gold grade (g/t)
0.62097	-	conversion factor (gold to copper)
0.8235	-	relative recovery of gold to copper (82.35%)

The copper equivalent formula was based on the following parameters (prices are in USD):

Cu price	-	3.1 \$/lb (or 6834 \$/t)
Au price	-	1320 \$/oz
Cu recovery	-	85%
Au recovery	-	70%

Relative recovery of gold to copper = $70\% / 85\% = 82.35\%$.

Mining and metallurgical methods and parameters

The project has undergone several phases of preliminary metallurgical test work. The most recent flotation test work was completed by Resources Engineering & Management in 2016. The tested material was described as deeper, tourmaline breccia from drill hole KHDD371. A composite was produced from the drill core interval assay rejects provided, with a measured grade of 4.71% Cu and 2.10 g/t Au. The sample was then the subject of standard laboratory grinding and flotation tests carried out at nominal grind sizes of p80 125µm, 150µm and 180µm.

The sample produced from the material provided responded very well to simple flotation testing with low collector dosage. The reported copper recovery varied from 95.3 to 93.6% depending on the grind size, and between 93.4 to 95.5% for gold.

Earlier work completed in 2008 by the previous owners, tested samples more closely aligned with the grades expected for the life of mine, and are likely more representative of the deposit overall. These samples achieved recoveries between 80% and 90% for copper and 70% for gold. The following recoveries were used for the conceptual pit optimisation study and for the copper equivalent formula - 70% recovery for gold and 85% recovery for copper, which are well supported by the results of the metallurgical test work.

Management's Discussion and Analysis

continued

The next phase of test work that has commenced will aim to optimise recoveries of copper and gold into concentrate as well as investigate more value can be added from other minerals such as silver, bismuth or molybdenum can be extracted.

The Zaraa discovery

In April 2018, Xanadu discovered a new, large-scale porphyry deposit within the Kharmagtai lease with KHDDH462 returning 928.4m @ 0.3% Cu and 0.25g/t Au (0.47% eCu or 0.73g/t eAu) including 622m @ 0.37% Cu and 0.32g/t Au (0.57% eCu or 0.9 g/t eAu) (see ASX release dated April 19, 2018).

A further six diamond drill holes have been drilled into Zaraa defining a body of mineralisation approximately 700m vertically, 400m long and 200m wide (Figure 3). Mineralisation is open at depth and along strike. Five diamond drill holes are planned to bring the drill spacing close enough to generate a maiden inferred mineral resource for Zaraa and planning is underway to drill at greater depths where Xanadu's geologists believe mineralisation broadens and a higher-grade bornite zone may occur.

Exploration at Kharmagtai during 2019 will focus on continuing to expand the current resources and advancing the highest priority exploration targets to provide additional high-grade resources.

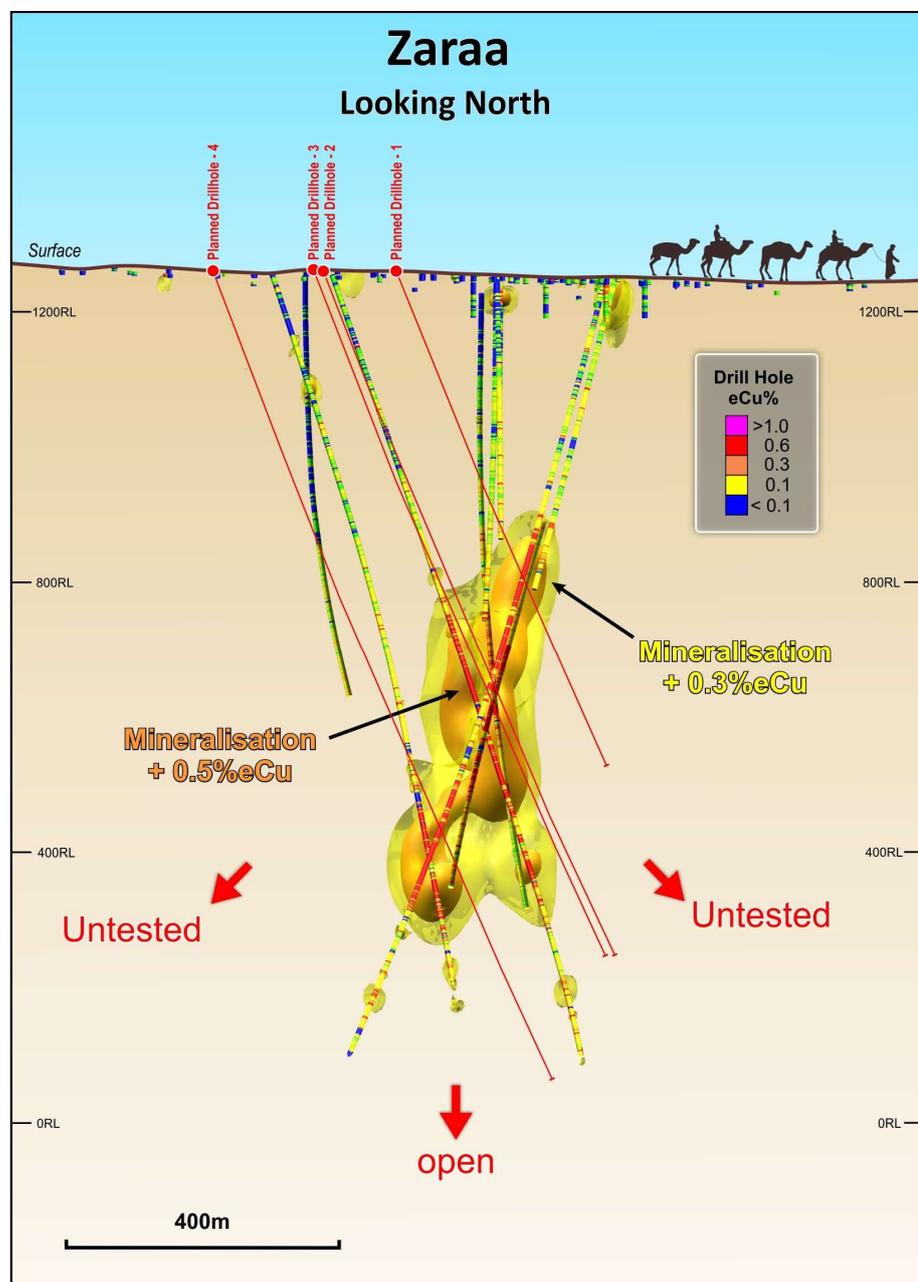


Figure 3: Cross section through the new Zaraa discovery showing existing drilling, planned drilling and mineralisation envelopes.

Management's Discussion and Analysis

continued

Red Mountain Project (Xanadu 90%)

The Red Mountain copper-gold project is located in the Dornogovi Province of southern Mongolia, approximately 70 kilometres west of the future industrial centre of Sainshand. Red Mountain is a highly prospective porphyry copper-gold project. The project comprises a large and underexplored porphyry district (covering approximately 40km²) and consists of multiple co-genetic porphyry copper-gold centres, mineralised tourmaline breccia pipes and copper-gold/base metal magnetite skarns, which occur within the central part of Mining Licence 17129A (Figure 4).

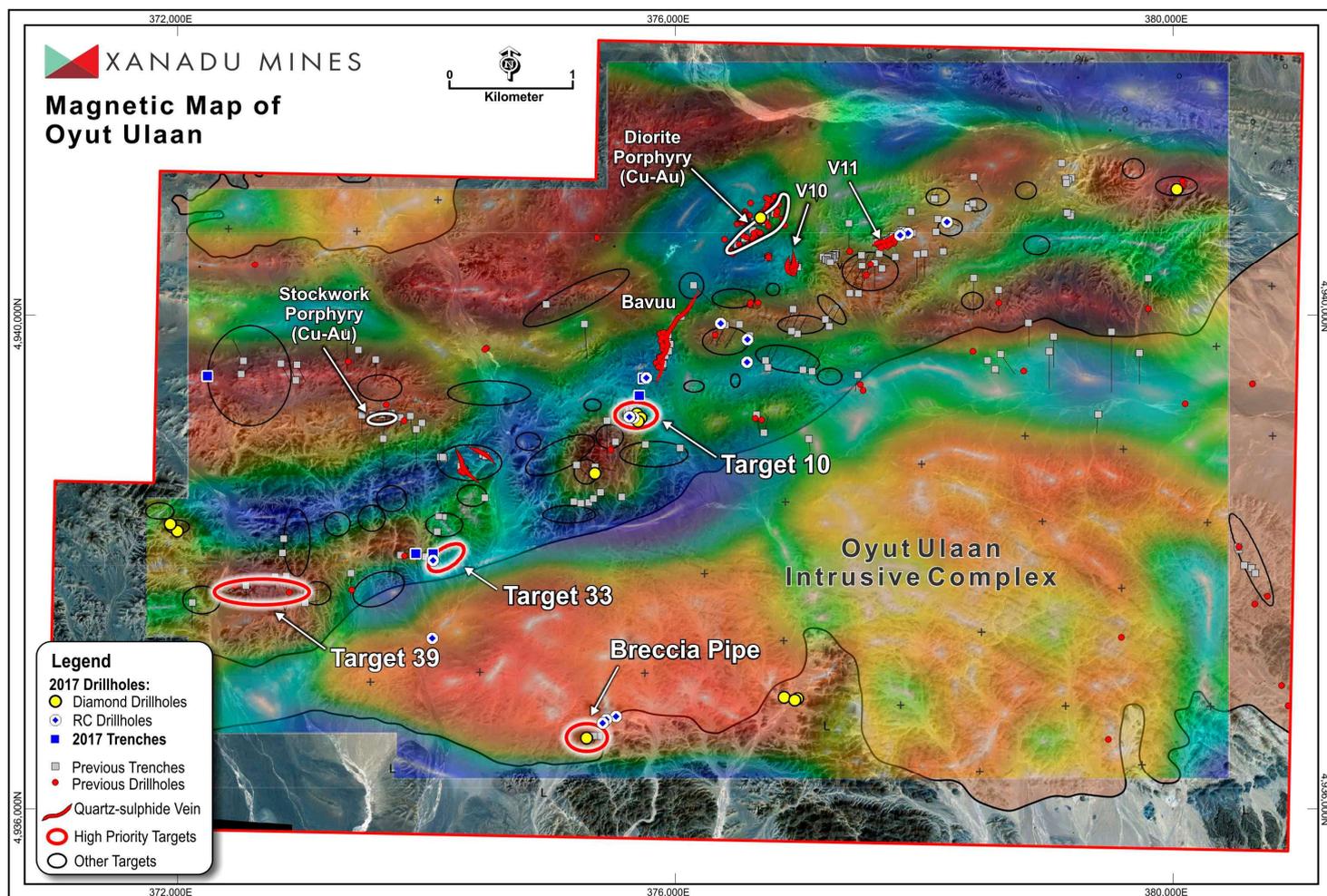


FIGURE 4: The Red Mountain Mining Licence showing known porphyry deposits and new targets.

Exploration at Red Mountain during 2018 continued to define the projects potential through a combination of mapping, geophysics and geochemistry identifying multiple drill-ready targets. Exploration work indicates that outcropping mineralisation may represent the shallow part of a deeper, more continuous porphyry system. A tourmaline breccia complex is also present at Red Mountain with similarities to the mineralised tourmaline breccia dike complex at Kharmagtai. The Company will continue its systematic and low-cost exploration program at Red Mountain. The next phase of exploration will focus on delineating potential large-scale porphyry deposits via testing the many geophysical and geochemical anomalies which remain within the Red Mountain licence area.

Yellow Mountain Project (Xanadu 100%)

Sharchuluut Uul is an early stage project focused on what is an extensive advanced argillic (high-sulphidation porphyry lithocap) alteration above a deeper porphyry centre. Limited drilling to date has intersected broad zones of porphyry alteration. Xanadu has outlined two main target areas that are yet to be tested.

Competent Person's Statements

The information in this announcement that relates to Mineral Resources is based on information compiled by Dmitry Pertel who is responsible for the Mineral Resource estimate. Mr Pertel, is a full time employee of CSA Global and is a Member of the Australasian Institute of Geoscientists, has sufficient experience relevant to the style of mineralisation and type of deposit under consideration and to the activity he is undertaking to qualify as the "Competent Person" as defined in the 2012 Edition of the "Australasian Code for

Management's Discussion and Analysis

continued

Reporting Exploration Results, Mineral Resources and Ore Reserves" and the National Instrument 43-101. Mr Pertel consents to the inclusion in the report of the matters based on this information in the form and context in which it appears.

The information in this announcement that relates to exploration results is based on information compiled by Dr Andrew Stewart who is responsible for the exploration data, comments on exploration target sizes, QA/QC and geological interpretation and information. Dr Stewart, who is an employee of Xanadu and is a Member of the Australasian Institute of Geoscientists, has sufficient experience relevant to the style of mineralisation and type of deposit under consideration and to the activity he is undertaking to qualify as the "Competent Person" as defined in the 2012 Edition of the "Australasian Code for Reporting Exploration Results, Mineral Resources and Ore Reserves" and the National Instrument 43-101. Dr Stewart consents to the inclusion in the report of the matters based on this information in the form and context in which it appears.

Results of Operations

Selected annual information

	Year ended December 31, 2018 \$'000	Year ended December 31, 2017 \$'000	Year ended December 31, 2016 \$'000
Exploration expenditures	8,290	7,086	4,764
Corporate general and administration	4,630	3,208	2,651
Share-based payments	1,696	326	249
Depreciation and amortisation	81	91	114
Total comprehensive loss	5,625	5,788	9,567
Basic loss per share	1.00	0.72	0.47
Diluted loss per share	1.00	0.72	0.47

	As at December 31, 2018 \$'000	As at December 31, 2017 \$'000	As at December 31, 2016 \$'000
Deferred exploration expenditures	45,903	37,157	31,952
Total assets	52,076	47,213	41,051
Total liabilities	814	1,421	4,285
Net assets	51,262	45,792	36,766

The Company is in the exploration stage and does not generate operating revenue.

Expenditures arising from exploration and evaluation activities relating to an area of interest are carried forward, provided such costs are expected to be recouped through successful development, or by sale, or where exploration and evaluation activities have not, at balance date, reached a stage to allow a reasonable assessment regarding the existence of economically recoverable resources. Rights of tenure must be current to carry forward deferred exploration and evaluation expenditure. Costs carried forward in respect of an area of interest that is abandoned are written off in the year in which the decision to abandon is made.

Exploration expenditures in the reporting increased due to increased volume of drilling at the Kharmagtai project and the discovery of the Zarea prospect. A total of 26,700 metres of diamond drilling, 8,333 metres of reverse circulation drilling, 5,600 metres of PCD drilling has been completed during the calendar year at the Kharmagtai and Red Mountain projects.

Corporate general and administration expenses increased due to the dual-listing on the Toronto Stock Exchange, increased corporate consultancies, professional fees, and promotional expenses.

Share-based payments expense increased due to the equity incentive plan granted to the Key Management Personnel. Share-based payments is measured by reference to the fair value at the date at which they are granted. The fair value of the options is determined by an independent written valuation. Share-based payments expense is amortised over the vesting period. No expense is recognised for awards that do not ultimately vest, except for awards where vesting is only conditional upon a market condition.

Total assets increased due to the increase in the deferred exploration expenditures.

Total liabilities decreased due to the decrease in trade payables at the end of the reporting year.

Management's Discussion and Analysis

continued

Selected quarterly information

	Quarter ended December 31, 2018 \$'000	Quarter ended September 30, 2018 \$'000	Quarter ended June 30, 2018 \$'000	Quarter ended March 31, 2018 \$'000
Exploration expenditures	762	2,109	2,709	2,710
Corporate general and administration	1,615	996	965	1,054
Share-based payments	164	164	684	684
Depreciation and amortisation	18	19	17	27
Loss after income taxes	1,828	1,176	1,522	1,801
Basic loss per share	0.24	0.16	0.25	0.30
Diluted loss per share	0.24	0.16	0.25	0.30

	Quarter ended December 31, 2017 \$'000	Quarter ended September 30, 2017 \$'000	Quarter ended June 30, 2017 \$'000	Quarter ended March 31, 2017 \$'000
Exploration expenditures	2,408	2,276	1,166	1,236
Corporate general and administration	1,201	643	769	596
Share-based payments	178	-	5	6
Depreciation and amortisation	23	19	31	18
Loss after income taxes	1,505	713	885	728
Basic loss per share	0.22	0.13	0.17	0.15
Diluted loss per share	0.22	0.13	0.17	0.15

Exploration expenditures in the reporting quarter decreased due to the decrease in volume of drilling. In the first three quarters of the year, the Company had undertaken the majority of the exploration plan for the year.

Corporate general and administration expenses increased due to the dual-listing on the Toronto Stock Exchange, increased corporate consultancies, professional fees, and promotional expenses.

Share-based payments is measured by reference to the fair value at the date at which they are granted. The fair value of the options is determined by an independent written valuation. Share-based payments expense is amortised over the vesting period. No expense is recognised for awards that do not ultimately vest, except for awards where vesting is only conditional upon a market condition.

Capital Management

The Company had \$5.2 million cash on hand as at December 31, 2018 (December 31, 2017: \$9.1 million). On June 27, 2018, Xanadu successfully completed a share placement to domestic and international institutional and sophisticated investors raising approximately \$10.0 million. The placement of approximately 58.8 million ordinary share units were issued pursuant to Xanadu's 15% placement capacity in accordance with ASX Listing Rule 7.1 at an issue price of \$0.17 per ordinary share. Each ordinary share unit comprised one ordinary share and 1 free attaching unlisted option, with every two unlisted options exercisable into one ordinary share at \$0.25 for a two-year term.

The primary use of funds over 2019 will be the continuation of exploration activities at the Company's Kharmagtai and Red Mountain copper-gold projects and for working capital purposes. The Company may need to raise additional capital for its exploration activities or seek joint venture partners. There is a risk that capital or joint venture partners may not be available or available on acceptable terms. Capital management is a priority of Management and the Company retains the flexibility to reduce its cost base while preserving its exploration projects if required.

Financial instruments and risk management

The Board of Directors is responsible for the determination of the Company's risk management objectives and policies. The Board has delegated to the Company's management the authority for designing and operating processes that ensure the effective implementation of the objectives and policies.

The overall objective of the Board is to set policies that seek to reduce risk as much as possible without unduly affecting the Company's competitiveness and flexibility. Further details regarding these policies are set out below.

Management's Discussion and Analysis

continued

Market risk

Market risk is the risk that the fair value of future cash flows of a financial instrument will fluctuate because of changes in market prices. Market prices are comprised of four types of risk: foreign currency risk, interest rate risk, commodity price risk and equity price risk.

- *Foreign currency risk:* The Company is exposed to foreign exchange fluctuations with respect to Australian Dollars (A\$), US Dollars (US\$), Mongolian Tughrik (MNT), and Canadian Dollars (C\$). The Company's financial results are reported in A\$. Salaries for certain local employees in Mongolia may be paid in MNT. The Company's operations are in Mongolia and some of its payment commitments and exploration expenditures under the various agreements governing its rights are denominated in MNT and US\$. As a result, the Company's financial position and results are impacted by the exchange rate fluctuations among A\$, US\$, MNT and C\$. Such fluctuations may materially affect the Company's financial position and results.

Xanadu's currency risk to US\$ foreign denominated financial assets and liabilities at the end of the reporting period, expressed in A\$, was as follows:

Consolidated	Assets	
	2018 \$'000	2017 \$'000
Cash and cash equivalents	524	6,883

The following sensitivity is based on the foreign currency risk exposures in existence at the balance date:

Consolidated - 2018	AUD strengthened			AUD weakened		
	% change	Effect on profit before tax	Effect on equity	% change	Effect on profit before tax	Effect on equity
A\$/US\$	10%	52	52	(10%)	(52)	(52)

Consolidated - 2017	AUD strengthened			AUD weakened		
	% change	Effect on profit before tax	Effect on equity	% change	Effect on profit before tax	Effect on equity
A\$/US\$	10%	688	688	(10%)	(688)	(688)

- *Interest Rate Risk:* Interest rate risk is the risk that future cash flows will fluctuate as a result of changes in market interest rates. The Company does not have any borrowings at variable rates. Interest rate risk is limited to potential decreases on the interest rate offers on cash and cash equivalents held with chartered financial institutions. The Company considers this risk to be immaterial.

As at the reporting date, Xanadu had the following cash and cash equivalents and variable rate borrowings outstanding:

Consolidated	2018		2017	
	Weighted average interest rate %	Balance \$'000	Weighted average interest rate %	Balance \$'000
Cash and cash equivalents	2.40%	5,225	2.40%	9,065
Net exposure to cash flow interest rate risk		5,225		9,065

The following sensitivity is based on the interest rate risk exposures in existence at the balance date:

Consolidated - 2018	Basis points increase			Basis points decrease		
	Basis points change	Effect on profit before tax	Effect on equity	Basis points change	Effect on profit before tax	Effect on equity
Net interest rate risk exposure	100	52	52	(100)	(52)	(52)

Management's Discussion and Analysis

continued

Consolidated - 2017	Basis points increase			Basis points decrease		
	Basis points change	Effect on profit before tax	Effect on equity	Basis points change	Effect on profit before tax	Effect on equity
Net interest rate risk exposure	100	90	90	(100)	(90)	(90)

- *Commodity Price Risk:* Even if commercial quantities of mineral deposits are discovered, there is no guarantee that a profitable market will exist for the sale of the metals produced. Factors beyond the control of the Company may affect the marketability of any minerals discovered. The prices of various metals have experienced significant movement over short periods of time, and are affected by numerous factors beyond the control of the Company, including, among other things, international economic and political trends, expectations of inflation, currency exchange fluctuations, interest rates and global or regional consumption patterns, speculative activities and increased production due to improved mining and production methods. The Company is particularly exposed to the risk of movement in the price of copper and gold.
- *Equity Price Risk:* Equity risk is the uncertainty associated with the valuation of assets arising from changes in equity markets. The Company is exposed to this risk through its equity holdings.

Credit Risk

Credit risk is the risk that one party to a financial instrument will fail to discharge an obligation and cause the other party to incur a financial loss. Financial instruments which are potentially subject to credit risk for the Company consist primarily of cash and amounts receivable. Cash is maintained with financial institutions of reputable credit and may be redeemed upon demand.

The Company's maximum exposure to credit risk at the reporting date is the carrying value of its cash and cash equivalents of \$5.2 million (December 31, 2017 \$9.1 million) and amounts receivable of \$0.4 million (December 31, 2017 \$0.5 million).

Liquidity Risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they fall due. The primary source of funds available to the Company is from equity financing. The Company has in place a planning and budgeting process to help determine the funds required to support the Company's normal operating requirements on an ongoing and going concern basis, to support its exploration plans, and to ensure that it will have sufficient liquidity to meet its liabilities when due. To the extent the Company does not believe it has sufficient liquidity to meet these obligations, management will consider securing additional funds through equity or debt transactions.

The Company does not have unlimited financial resources and there is no assurance that sufficient additional funding or financing will be available to the Company or its direct and indirect subsidiaries on acceptable terms, or at all, for further exploration or development of its properties or to fulfill its obligations under any applicable agreements.

Failure to obtain such additional funding could result in the delay or indefinite postponement of the exploration and development of the Company's properties.

Other business risks

Political and Legal Risks

The Company's mineral projects are located in Mongolia, where mineral exploration and mining activities may be affected in varying degrees by political instability, economic conditions, expropriation or nationalization of property and changes in government regulations such as foreign investment laws, tax laws, business laws, environmental laws and mining laws, affecting the Company's business in that country. Government policy may change to discourage foreign investment, nationalization of the mining industry may occur and other government limitations, restrictions or requirements may be implemented. There can be no assurance that the Company's assets will not be subject to nationalization, requisition, expropriation or confiscation, whether legitimate or not, by any authority or body.

In addition, there can be no assurance that neighbouring countries' political and economic policies in relation to Mongolia will not have adverse economic effects on the development of the Company's mineral projects, including with respect to the ability to access power, transport and sell products and access construction labour, supplies and materials. The political, social and economic environment in Mongolia presents a number of serious risks, including, among other things: uncertain legal enforcement; invalidation, confiscation, expropriation or rescission of governmental orders, permits, licences, agreements and property rights; the effects of local political, labour and economic developments, instability and unrest; corruption, requests for improper payments or other corrupt practices; and significant or abrupt changes in the applicable regulatory or legal climate.

Management's Discussion and Analysis

continued

Licence Risks

The Company's most significant licences are the licence covering the Kharmagtai Project and the licence covering the Red Mountain Project. The Government of Mongolia could revoke either of these licenses if the Company fails to satisfy its obligations, including payment of royalties and taxes to the Government of Mongolia and the satisfaction of certain mining, environmental, health and safety requirements. A termination of the Company's mining licences covering the Kharmagtai Project or the Red Mountain Project by the Government of Mongolia could materially and adversely affect the Company's reputation, business, prospects, financial conditions and results of operations. In addition, the Company would require additional licences or permits to conduct the Company's mining or exploration operations in Mongolia. There can be no assurance that the Company will be able to obtain and maintain such licences or permits on terms favorable to it, or at all, for the Company's future intended mining or exploration targets in Mongolia, or that such terms would not be subject to various changes.

On July 16, 2009, the Mongolian Parliament enacted legislation to *Prohibit Mineral Exploration and Mining Operations in Headwaters of Rivers, Protected Zones of Water Reservoirs and Forested Areas* (the "Long Name Law") which prohibits minerals exploration and mining in areas such as headwaters of rivers and lakes, forest areas as defined in the Forest Law of Mongolia and areas adjacent to rivers and lakes as defined in the Water Law of Mongolia. New exploration licences and mining licences overlapping with the defined prohibited areas will not be granted and previously granted licences that overlap with the defined prohibited areas will be terminated within five months following the adoption of the Long Name Law. The Company's license under the Yellow Mountain Project overlaps with the border zone of a forested area and zones allocated to the protection of water basins/reservoirs under the Long Name Law. Pursuant to the Minerals Law and the Long Name Law, minerals licences which overlap with restricted areas will be revoked by the mineral's authority only if, and when, compensation is paid in full to the holder of the relevant licence. The Company has not received any such notice from any Government Authority, indicating the revocation of the Yellow Mountain Licence or inviting the Company to discuss the revocation of its licence. Notwithstanding the validity of the Yellow Mountain Licence, as a matter of law, the Company will not be entitled to undertake any exploration activities in any portion of the Yellow Mountain Licence area that overlaps with a restricted area.

Mineral Resource Assumptions Risk

The Company's mineral resource and mineral reserve estimates for the Kharmagtai Project are based on a number of assumptions. There are numerous uncertainties inherent in estimating quantities of mineral reserves and grades of mineralization, including many factors beyond the control of the Company. There can be no assurance that the mineral resources and mineral reserve estimates will be recovered in the quantities, qualities or yields presented in this prospectus or set out in the Kharmagtai Technical Report.

Copper and gold mineral resource and mineral reserve estimates are inherently prone to variability. They involve expressions of judgment with regard to the presence and quality of mineralization and the ability to extract and process the mineralization economically. These judgments are based on a variety of factors, such as knowledge, experience and industry practice.

Environmental Risk

Existing and possible future environmental legislation, regulations and actions could cause significant expense, capital expenditures, restrictions and delays in the activities of the Company, the extent of which cannot be predicted and which may well be beyond the capacity of the Company to fund. Failure to comply with applicable environmental laws and permitting requirements may result in enforcement actions thereunder, including orders issued by regulatory or judicial authorities causing operations to cease, and may include corrective measures requiring capital expenditures, installation of additional equipment or remedial actions.

Operational Risk

The Company's activities are subject to a number of operational risks and hazards, some of which are beyond its control. These risks and hazards include unexpected maintenance or technical problems, periodic interruptions due to inclement or hazardous weather conditions, natural disasters such as earthquakes, industrial accidents, power, water or fuel supply interruptions or the increase in the price of such supplies, critical equipment failure, malfunction and breakdowns of information management systems, fires, and unusual or unexpected variations in mineralization, geological or mining conditions.

Contractual Risk

Xanadu's key project (the Kharmagtai Project) is held pursuant to a joint venture arrangement. Additionally, the Company may wish to develop its projects or future projects through further joint venture arrangements.

As in any contractual relationship, the ability for Xanadu to ultimately receive benefits from these contracts is dependent upon the relevant third party complying with its contractual obligations. Specifically, Xanadu's ability to further its flagship Kharmagtai Project therefore depends upon the strength and enforceability of these contracts and the ability to enforce them against the relevant counterparties, under relevant laws.

Management's Discussion and Analysis

continued

Further, under the terms of the Company's original acquisition of the Kharmagtai Project, the Company agreed to assume certain royalty obligations, the precise terms of which are unclear or not in existence. There is therefore some doubt as to the precise nature of the Company's obligations to the extent they exist.

In respect of these agreements and obligations, it may be necessary for Xanadu to enforce its rights under any of the contracts or pursue legal action to clarify their terms. Such legal action may be costly and no guarantee can be given by Xanadu that a legal remedy will ultimately be granted on appropriate terms.

Significant changes in the state of affairs

There were no significant changes in the state of affairs of the Company during the financial period.

Matters subsequent to the end of the financial period

On January 14, 2019, 35,000,000 options, issued pursuant to the Red Mountain Project acquisition terms, expired. The vesting of 15,000,000 Series A Options was contingent on recognition of a JORC resource of at least 300,000 tonnes contained copper equivalent and the vesting of 20,000,000 Series B Options was contingent on the recognition of a JORC resource of at least 900,000 tonnes contained copper equivalent.

No other matter or circumstance has arisen since December 31, 2018 that has significantly affected, or may significantly affect Xanadu's operations, the results of those operations, or the Company's state of affairs in future financial years.

Commitments

Commitments in relation to exploration licences contracted at the reporting date, including regulatory charges such as licence fees, and corporate administrations, but not recognised as liabilities within one year are \$0.7 million (December 31, 2017: \$0.7 million). As the future exploration activity is in most cases dependent upon reserves being found, it is not possible to set out the funds due to be contributed in more than one year's time. No other commitments or contingencies existed at December 31, 2018.

Commitments recognised as liabilities within one year are trade payables and vehicle leases totalling \$0.6 million.

Related party transactions

Parent entity and subsidiaries

Xanadu Mines Ltd is the parent entity. Interests in subsidiaries are set out in Note 26 to the financial statements.

Key management personnel

Disclosures relating to key management personnel are set out in Note 20 to the financial statements and the Remuneration Report.

Transactions with related parties

On January 2, 2017, the Company relocated its Ulaanbaatar office and entered into a rental agreement with Mr Ganbayar Lkhagvasuren, an Executive Director of the Company. The transaction between these related parties is on normal commercial terms and conditions, no more favourable than those available to other parties that are arm's length. The Company paid rental totalling \$89,438 (December 31, 2017: \$88,428) for the year ended December 31, 2018.

Receivable from and payable to related parties

There were no trade receivables from or trade payables to related parties at the current and previous reporting date.

Loans to/from related parties

There were no loans to or from related parties as at December 31, 2018.

Terms and conditions

All transactions were made on normal commercial terms and conditions and at market rates.

Likely developments and expected results of operations

Information on likely developments in the operations of the Company and the expected results of operations have been included in the review of operations report. Xanadu intends to continue to invest and explore the projects described in this report.

Dividends

There were no dividends paid, recommended or declared during the current or previous financial period.

Management's Discussion and Analysis

continued

Off balance sheet arrangements

The Company has not entered into any off-balance sheet transactions.

Fair value estimate

Fair value hierarchy

The following tables detail Xanadu's assets, measured or disclosed at fair value, using a three-level hierarchy, based on the lowest level of input that is significant to the entire fair value measurement, being:

Level 1: Quoted prices (unadjusted) in active markets for identical assets that the entity can access at the measurement date;

Level 2: Inputs other than quoted prices included within Level 1 that are observable for the asset, either directly or indirectly; and

Level 3: Unobservable inputs for the asset.

Consolidated - 2018	Level 1 \$'000	Level 2 \$'000	Level 3 \$'000	Total \$'000
<i>Assets</i>				
Ordinary shares - Aspire Mining Limited (ASX code: AKM)	190	-	-	190
Total assets	190	-	-	190

Consolidated - 2017	Level 1 \$'000	Level 2 \$'000	Level 3 \$'000	Total \$'000
<i>Assets</i>				
Ordinary shares - Aspire Mining Limited (ASX code: AKM)	100	-	-	100
Total assets	100	-	-	100

There were no transfers between levels during the financial period.

New or amended Accounting Standards and Interpretations adopted

The Company has adopted all of the new or amended AASB Standards that are mandatory for the applicable annual reporting periods. Any new or amended Accounting Standards or Interpretations that are not yet mandatory have not been early adopted.

AASB 9 Financial Instruments

AASB 9 contains accounting requirements for financial instruments, replacing AASB 139 *Financial Instruments: Recognition and Measurement*. The standard contains requirements in the areas of classification and measurement, impairment, hedge accounting and derecognition. This standard applies to annual reporting periods beginning on or after January 1, 2018. The Company has applied the new standard for the current annual financial report for the year ended December 31, 2018, and there has been no material impact.

AASB 15 Revenue from Contracts with Customers

AASB 15 provides a single, principles-based five-step model to be applied to all contracts with customers. Guidance is provided on topics such as the point in which revenue is recognised, accounting for variable consideration, costs of fulfilling and obtaining a contract and various related matters. New disclosures about revenue are also introduced. This standard applies to annual reporting periods beginning on or after January 1, 2018. The Company has no revenue and the application of the new standard for the current annual financial report for the year ended December 31, 2018, had no impact.

AASB 16 Leases

AASB 16 provides a new lessee accounting model which requires a lessee to recognise assets and liabilities for all leases with a term of more than 12 months, unless the underlying asset is of low value. A lessee will be required to measure right-of-use assets in a manner similar to how other non-financial assets, lease liabilities and other financial liabilities are measured. Assets and liabilities arising from a lease are initially measured on a present value basis. The measurement includes non-cancellable lease payments (including inflation-linked payments), and also includes payments to be made in optional periods if the lessee is reasonably certain to exercise an option to extend the lease, or not to exercise an option to terminate the lease. AASB 16 contains disclosure requirements for lessees. The company has assessed the potential impact of the new standard on the Company's financial report and expects no material impact. This standard applies to annual reporting periods beginning on or after January 1, 2019.

AASB 2016-5 Amendments to Australian Accounting Standards - Classification and Measurement of Share-based Payment Transactions

This standard amends AASB 2 *Share-based Payments*, clarifying how to account for certain types of share-based payment transactions. The amendments provide requirements on the accounting for the:

- effects of vesting and non-vesting conditions on the measurement of cash-settled share-based payments;

Management's Discussion and Analysis

continued

- share-based payment transactions with a net settlement feature for withholding tax obligations; and
- modification to the terms and conditions of a share-based payment that changes the classification of the transaction from cash-settled to equity-settled.

This standard applies to annual reporting periods beginning on or after January 1, 2018. The Company has applied the new standard for the current annual financial report for the year ended December 31, 2018, and there has been no material impact.

AASB Interpretation 22 Foreign Currency Transactions and Advance Considerations

The Interpretation clarifies that, in determining the spot exchange rate to use on initial recognition of the related asset, expense or income (or part of it) or on the derecognition of a non-monetary asset or non-monetary liability relating to advance consideration, the date of the transaction is the date on which an entity initially recognises the non-monetary asset or non-monetary liability arising from the advance consideration. If there are multiple payments or receipts in advance, then the entity must determine the date of the transactions for each payment or receipt of advance consideration.

This Interpretation does not have any material impact on the current annual financial report for the year ended December 31, 2018.

Directors' Report

Directors

The following individuals were Directors of Xanadu during the whole of the financial period and up to the date of this report, unless otherwise stated:

Kevin Tomlinson – Independent Non-Executive Chairman
Andrew Stewart – Managing Director and Chief Executive Officer
Ganbayar Lkhagvasuren – Executive Director
Hannah Badenach – Non-Executive Director
Marcus Engelbrecht – Non-Executive Director
Darryl Clark – Independent Non-Executive Director
Michele Muscillo – Independent Non-Executive Director.

Information on Directors

Name:	Kevin Tomlinson
Title:	Independent Non-Executive Chairman
Qualifications:	MAIG, FSI, MSc
Experience and expertise:	Kevin has more than 35 years' experience in the resource sector, firstly as a geologist and then moving into the finance sector where he worked extensively in the finance sectors within the Canadian (TSXV, TSX), Australian (ASX) and United Kingdom (AIM, LSE) stock markets. In Australia, Kevin held senior executive roles with Plutonic Resources and Hartleys Australia as Head of Research. In London, he was Managing Director of Investment Banking at Westwind Partners/Stifel Nicolaus raising equity and providing corporate advice for many resource companies. Kevin brings extensive experience in exploration, development and financing of mining projects internationally.
Other current directorships:	Cardinal Resources Limited (ASX/TSX: CDV) (appointed November 7, 2016 - current), Infinity Lithium Limited (ASX:INF) (appointed June 8, 2017 - current), Samco Gold Limited (TSX:SGA) (appointed January 16, 2012 - current)
Former directorships (last three years):	Centamin plc (LSE:CEY/TSX:CEE) (appointed January 2012 - ceased May 2016)
Special responsibilities:	Member of the Audit and Risk Committee, Nomination and Remuneration Committee and Safety, Health and Environment Committee
Interests in shares:	394,547
Interests in rights:	3,000,000

Management's Discussion and Analysis

continued

Name: Dr Andrew Stewart
Title: Managing Director and Chief Executive Officer
Qualifications: BSc, PhD, MAIG, MSEG, MAICD
Experience and expertise: Andrew is a geologist with over 15 years' experience in mineral exploration; primarily focussed on project generation, project evaluation and exploration strategy development throughout Asia and Eastern Europe. Andrew has particular expertise in porphyry copper and epithermal gold deposits, but has worked across a diverse range of commodities. He holds a BSc (Hons) from Macquarie University and a PhD from the Centre of Ore Deposits and Exploration Studies at the University of Tasmania. During his time at Ivanhoe Mines and Vale, Andrew held various technical and management positions in Mongolia and Indonesia and has been involved in several green field discoveries. After providing technical and program management for Vale in Indonesia and Mongolia, Andrew joined Xanadu Mines as Chief Geologist leading the gold and base metals project generation and evaluation team in Mongolia. In 2016, Andrew became the Managing Director and Chief Executive Officer of Xanadu Mines.

Other current directorships: None
Former directorships (last three years): None
Special responsibilities: Managing Director
Interests in shares: 4,292,083
Interests in rights: 7,000,000

Name: Ganbayar Lkhagvasuren
Title: Executive Director
Qualifications: M.IBL
Experience and expertise: Ganbayar is a co-founder of Xanadu and has been a Director since 2006. He is the joint venture partner in Mongol Metals LLC and brings a vital Mongolian perspective to the Board of Directors.

Other current directorships: None
Former directorships (last three years): None
Special responsibilities: Member of the Safety, Health and Environment Committee
Interests in shares: 16,558,329
Interests in rights: 4,000,000

Name: Hannah Badenach
Title: Non-Executive Director
Qualifications: B. Laws (Hons), B. Arts
Experience and expertise: Hannah is a lawyer and an Executive Director at Noble Resources International Pte Ltd ("Noble"). Hannah has worked in various markets globally and has extensive commercial and business development experience. She has been responsible for the development and execution of business development strategies for over 15 years.

Other current directorships: Aspire Mining Limited (ASX:AKM) (appointed April 18, 2013 - current)
Former directorships (last three years): None
Special responsibilities: None
Interests in shares: 1,410,738
Interests in rights: None

Name: Dr Darryl Clark
Title: Independent Non-Executive Director
Qualifications: B.Sc (Honours), Phd (Economic Geology), FAusIMM
Experience and expertise: Darryl is an exploration geologist whose career has taken him throughout Australia, Central Asia and South East Asia for over 23 years. His responsibilities over the last 14 years have involved him in a diverse range of technological, political and cultural environments with unique challenges. During previous corporate roles with both Vale and BHP Billiton, and in consulting roles including SRK, he has been responsible for business development strategies, designing multi-commodity exploration programs and the co-ordination of exploration teams to deliver discovery events.

Other current directorships: None
Former directorships (last three years): DGO Gold Limited (ASX:DGO) (appointed October 15, 2018 –ceased January 29, 2019)

Management's Discussion and Analysis

continued

Special responsibilities: Chairman of Safety, Health and Environment Committee and a member of the Nomination and Remuneration Committee and a member of Audit and Risk Committee

Interests in shares: 1,921,500

Interests in rights: 1,000,000

Name: Marcus Engelbrecht

Title: Non-Executive Director

Qualifications: MAICD, H Compt

Experience and expertise: Marcus is a well-rounded senior mining executive with considerable experience in the international mining industry. He has worked in various emerging markets across the globe, including South East Asia, Africa and South America and brings a good network and reputation across the international institutional investment community. Marcus has worked in the mining industry since 1985 and spent 20 years at BHP Billiton through to 2005 where he served as Chief Financial Officer for their Diamonds and Specialty Products business. From 2009 to 2011, he served as Chief Financial Officer of ASX/TSX/NZX listed OceanaGold Corporation and from 2011 to 2013, he served as Managing Director and Chief Executive Officer of London AIM listed and Singapore based Archipelago Resources Plc, a gold producer in Indonesia. From 2016 he served as Managing Director of Stratex, an AIM listed company and from 2017 to 2019 he was Managing Director of Crusader Resources, a dual ASX/AIM listed company.

Other current directorships: None

Former directorships (last three years): Stratex International plc (LON:STI) (appointed September 2016 - ceased November 2017), Crusader Resources Limited (ASX:CAS) (appointed November 20, 2017 – February 28, 2019)

Special responsibilities: None

Interests in shares: 1,000,000

Interests in rights: None

Name: Michele Muscillo

Title: Independent Non-Executive Director

Qualifications: LL.B

Experience and expertise: Michele is a Partner with HopgoodGanim Lawyers in Brisbane. He has practised exclusively in corporate law for the duration of his legal career and has extensive experience in mergers and acquisitions and capital markets transactions, including the negotiation of significant commercial contracts and agreements. His key areas of practice include Corporate Advisory and Governance, Mergers and Acquisitions, Capital Markets and Resources and Energy. Michele is also currently a Non-Executive Director with ASX-Listed Aeris Resources Limited (ASX: AIS), a Non-Executive Director with ASX/TSX listed Cardinal Resources Limited (ASX/TSX: CDV) and a Non-Executive Director with ASX listed Mako Gold Limited (ASX: MKG). Formerly, Michele was also Non-Executive Director of Orbis Gold Limited from the time of its ASX listing, through the discovery of its flagship Natougou project and ultimately to the sale of the Company to TSX-Listed SEMAFO Inc. (TSX: SMF) in 2015.

Other current directorships: Cardinal Resources Limited (appointed October 12, 2017 - current), Aeris Resources Limited (appointed May 2, 2013 - current), Mako Gold Limited (appointed April 20, 2017 - current)

Former directorships (last three years): None

Special responsibilities: Chairman of the Audit and Risk Committee and Nomination and Remuneration Committee

Interests in shares: 54,037

Interests in rights: 1,000,000

'Other current directorships' quoted above are current directorships for listed entities only and excludes directorships of all other types of entities, unless otherwise stated.

'Former directorships (last three years)' quoted above are directorships held in the last three years for listed entities only and excludes directorships of all other types of entities, unless otherwise stated.

Management's Discussion and Analysis

continued

Company Secretary

Phil Mackey, B Bus

Phil was appointed Company Secretary of Xanadu in May 2017. Phil has over three decades of listed and unlisted company secretarial and commercial experience, including multi-jurisdictional board practice as both a company secretary and a director. Previously, Phil served as Company Secretary of ASX and SGX dual listed Australand Group Limited (a quadruple stapled group) and Deputy Company Secretary of AMP Limited (ASX:AMP). Phil's commercial experience includes appointment as Chief Operating Officer (Specialised Funds) at Babcock & Brown. Phil is a Fellow of the Governance Institute Australia and a Graduate Member of the Australian Institute of Company Directors.

Meetings of Directors

The number of meetings of the Company's Board of Directors ('the Board') and of each Board committee held during the period ended December 31, 2018 and the number of meetings attended by each Director were:

	Full Board		Audit & Risk Committee		Nomination & Remuneration Committee		Safety, Health and Environment Committee	
	Attended	Held	Attended	Held	Attended	Held	Attended	Held
K Tomlinson	12	12	1	2	2	2	2	2
A Stewart	12	12	–	–	–	–	–	–
G Lkhagvasuren	11	12	–	–	–	–	2	2
H Badenach	12	12	–	–	1	1	–	–
D Clark	11	12	1	1	3	3	2	2
M Engelbrecht	11	12	1	1	1	1	–	–
M Muscillo	11	12	2	2	2	2	–	–

Held: represents the number of meetings held during the time the Director held office or was a member of the relevant Committee.

As at the date of this MD&A the Company has a Safety, Health and Environment Committee, an Audit and Risk Committee and a Nomination and Remuneration Committee. Further details are set out in the Corporate Governance Statement on the Company's website at www.xanadumines.com.

Management's Discussion and Analysis

continued

Remuneration Report (audited)

The Remuneration Report, which has been audited, outlines the key management personnel ('KMP') remuneration arrangements for the Group, in accordance with the requirements of the Corporations Act 2001 and its Regulations.

KMP have authority and responsibility for planning, directing and controlling the activities of the Company and the consolidated entity, including directors of the Company and other executives. KMP comprise the Directors of the Company and executives of the Company and the Group including the most highly remunerated executives.

The remuneration report is set out under the following main headings:

- Principles used to determine the nature and amount of remuneration;
- Details of remuneration;
- Service agreements;
- Share-based compensation;
- Additional information; and
- Additional disclosures relating to key management personnel.

Principles used to determine the nature and amount of remuneration

Xanadu is a Mongolian-focused exploration company. Our strategy is to convert our South Gobi porphyry copper and gold projects into mineable deposits and build long-term value for shareholders by becoming the next internationally competitive mid-tier copper and gold company in Asia.

The Company's remuneration philosophy is to ensure that the level and composition of remuneration is competitive, reasonable and appropriate to attract, retain and motivate the directors and employees with the skills required to deliver on the Company's strategy. Our philosophy recognises the importance of people and a team approach.

Important attributes that impact on Xanadu's success are:

- exploration and safety excellence, dedication and persistence;
- understanding of Mongolia and a strong national team;
- ability to communicate exploration success in the public markets to attract capital and increase shareholder value; and
- adherence to good corporate governance principles.

When considering remuneration matters, the Governance Committee reviews and recommends to the Board on matters of remuneration policy, specific recommendations in relation to senior management and all matters concerning equity plans and awards.

Executive Remuneration

There are up to three categories of remuneration employed to reward employees depending on their role and responsibility within Xanadu:

1. Total Fixed Remuneration;
2. Short Term Incentive; and
3. Long Term Incentive.

The remuneration mix consists of fixed and variable or "at-risk" pay and of short and longer-term rewards.

Total Fixed Remuneration

Total Fixed Remuneration ("TFR") comprises base salary, any relevant allowances and statutory contributions that the Company is legally required to make in the local jurisdiction. TFR is set with reference to market data and will reflect the scope of the role and the size and activities of the Company.

TFR is reviewed annually as part of the performance appraisals undertaken in the fourth quarter of the calendar year (prior to finalisation of the following year's budget).

Within Mongolia, the term net and gross TFR is used. Net TFR is fixed remuneration net of all taxes including Personal Income Tax and Social Insurance Tax and the Company is responsible for paying these taxes. Gross TFR includes personal income tax but excludes employer social insurance tax. Within Australia, the term TFR is inclusive of personal income tax but excludes payroll tax.

Variable or At-Risk Incentive Remuneration

It is the Board's policy to deliver at-risk incentive remuneration to employees as both a Short-Term Incentive ("STI") and a Long-Term

Management's Discussion and Analysis

continued

Incentive ("LTI"). The payment of STIs and LTIs are linked to achievement of agreed performance measures and establishes a variable remuneration arrangement that links short- and long-term performance with short- and longer-term rewards.

Any equity awarded will be governed by the Xanadu Equity Incentive Plan ("Plan"), and if awarded to a Director, the award will be subject to shareholder approval.

The Plan was initially approved by shareholders at the 2013 Annual General Meeting, reapproved at the 2016 Annual General meeting, and permits the award of a number of styles of awards including Options and Share Rights to employees. The issue of securities under the Plan is subject to the Xanadu Securities Trading Policy. Shares issued may be acquired on-market, transferred or issued from the capital of the Company.

Short Term Incentive ("STI")

Xanadu has established the STI to achieve the following objectives:

- focus employees on the achievements of annual key safety, financial and business targets that the Board believes will lead to sustained and improved business performance; and
- reward and recognise superior performance, if achieved.

The incentive offered under the STI will vary depending upon individual performance against key performance indicators ("KPIs") and any discretion employed by the Board. KPIs for the Non-Executive Chairman (for the relevant period), Managing Director & Chief Executive Officer (MD & CEO) and MD & CEO direct reports are approved by the Board upon recommendation from the Nomination and Remuneration Committee. KPIs for all other employees are approved by the MD & CEO. Depending on the individual's position, KPIs will include a range of metrics including health and safety, exploration results, corporate governance, financial stewardship, risk management, business development and leadership. Payment of STIs can be cash or shares which is also at the discretion of the Board.

Long Term Incentive ("LTI")

The Board believes that an appropriately designed LTI is an important component of the Group's remuneration arrangements. The LTI is a key tool to allow the Group to attract and retain talented directors, executive and managers and ensure the interests of LTI participants are aligned with those of shareholders in creating long-term shareholder value.

The Board's policy is to design equity style awards as LTIs. The vesting of an LTI award is dependent on the achievement of longer-term objectives, at least including share price growth over a three-year performance period.

Total Reward Mix - Executives

As a guide, the proportion of remuneration attributable to each component of the Xanadu remuneration philosophy is dependent on the level of seniority of the employee.

The target total reward mix on average is as follows:

	Total Fixed Remuneration %	STI % of TFR	LTI % of TFR
Managing Director & Chief Executive Officer and Executive Director	100	50	50
MD & CEO Direct Reports	100	30	30

The STI and LTI percentages of TFR are the maximum payable and the overall mix may vary depending on individual circumstances, legacy contracts and other benefits associated with expatriate allowances. The value of equity-based awards is determined at the time of grant using industry standard valuation techniques.

Non-Executive Remuneration

The aggregate cash remuneration for Non-Executive Directors will not exceed the maximum approved amount of \$350,000. The Board seeks to set aggregate remuneration at a level which provides the Company with the ability to attract and retain directors of the highest calibre, whilst incurring a cost which is acceptable by shareholders. Non-Executive Directors may also participate in the Plan if participation is approved by shareholders.

The amount of aggregate remuneration sought to be approved by shareholders and the manner in which it is apportioned amongst Directors is reviewed annually. The Board considers fees paid and securities issued to Non-Executive Directors of comparable companies when undertaking the annual review as well as the time commitment of directors in discharging duties at Board, Committee work and additional assistance provided to the Company. Currently, the Non-Executive Director base fee is \$52,000 per annum and a Committee Chairman receives \$4,000 per annum per committee. The Non-Executive Chairman receives fee of \$120,000 per annum.

Management's Discussion and Analysis

continued

Non-Executive Directors are encouraged by the Board to hold shares purchased on market in accordance with the Xanadu Securities Trading Policy. The Board considers that by holding shares in the Company, the Non-Executive Directors are aligning themselves with the best interests of the shareholders.

Details of remuneration

Amounts of remuneration

Details of the remuneration of key management personnel of the Group are set out in the following tables.

The key management personnel of the Group consisted of the Directors of Xanadu Mines Ltd and the following persons:

- M Dambiinyam - Chief Financial Officer
- M Brown - Chief Geologist

Year ended	Short-term benefits			Post-employment	Share-based	Total
	Cash salary and fee	Bonus	Others/ Non-monetary	benefits Super- annuation	payments Equity- settled	
December 31, 2018	\$	\$	\$	\$	\$	\$
<i>Non-Executive Directors:</i>						
K Tomlinson	142,732	-	-	-	274,868	417,600
D Clark	54,714	-	-	1,619	96,598	152,931
M Engelbrecht	48,097	-	-	4,569	-	52,666
M Muscillo	59,000	-	-	-	96,598	155,598
<i>Executive Directors:</i>						
A Stewart	388,266	129,726	61,825	-	641,358	1,221,175
G Lkhagvasuren	306,562	47,516	-	-	378,715	732,793
<i>Other KMP:</i>						
M Dambiinyam	195,353	34,305	-	-	104,548	334,206
M Brown	184,756	33,722	-	-	104,548	323,026
	<u>1,379,480</u>	<u>245,269</u>	<u>61,825</u>	<u>6,188</u>	<u>1,697,233</u>	<u>3,389,995</u>

H Badenach did not receive any remuneration.

Year ended	Short-term benefits			Post-employment	Share-based	Total
	Cash salary and fee	Bonus	Others/ Non-monetary	benefits Super- annuation	payments Equity- settled	
December 31, 2017	\$	\$	\$	\$	\$	\$
<i>Non-Executive Directors:</i>						
K Tomlinson*	98,913	-	-	-	67,462	166,375
D Clark	56,000	-	-	-	13,698	69,698
M Engelbrecht	51,142	-	-	4,858	18,799	74,799
M Muscillo**	19,500	-	-	-	13,698	33,198
M Wheatley***	38,214	18,415	-	3,630	-	60,259
B Lavin***	22,434	-	-	2,131	(42,506)	(17,941)
<i>Executive Directors:</i>						
A Stewart	378,170	72,872	70,395	-	157,412	678,849
G Lkhagvasuren	226,462	35,699	-	-	70,352	332,513
<i>Other KMP:</i>						
M Dambiinyam	152,440	21,380	-	-	13,463	187,283
M Brown	220,000	-	-	-	13,463	233,463
	<u>1,263,275</u>	<u>148,366</u>	<u>70,395</u>	<u>10,619</u>	<u>325,841</u>	<u>1,818,496</u>

* appointed May 29, 2017

** appointed August 14, 2017

*** ceased May 29, 2017 and forfeited share rights

Management's Discussion and Analysis

continued

H Badenach did not receive any remuneration.

The proportion of remuneration linked to performance and the fixed proportion are as follows:

Name	Fixed remuneration		At risk - STI		At risk - LTI	
	Year ended December 31 2018	Year ended December 31 2017	Year ended December 31 2018	Year ended December 31 2017	Year ended December 31 2018	Year ended December 31 2017
<i>Non-Executive Directors:</i>						
K Tomlinson	34%	59%	-	-	66%	41%
D Clark	37%	80%	-	-	63%	20%
M Engelbrecht	100%	75%	-	-	-	25%
M Muscillo	38%	59%	-	-	62%	41%
<i>Executive Directors:</i>						
A Stewart	37%	66%	11%	11%	53%	23%
G Lkhagvasuren	42%	68%	6%	11%	52%	21%
<i>Other KMP:</i>						
M Dambiinyam	58%	81%	10%	12%	31%	7%
M Brown	57%	94%	10%	-	33%	6%

Service agreements

Remuneration and other terms of employment for key management personnel are formalised in service agreements. Details of these agreements are as follows:

Name: Andrew Stewart
 Title: Managing Director & Chief Executive Officer
 Details: Dr Stewart's fixed remuneration is an annual salary package of US\$290,173 including compulsory taxes and social insurance applicable as an employee in Mongolia. Dr Stewart also receives a rental allowance of US\$30,000 per annum, travel and health care entitlements. In the event of termination of Dr Stewart's employment other than in the case of misconduct, the executive must give a minimum of 6 months' notice prior to termination, and the Company must give 9 months' notice prior to termination. The Company may, at its discretion, provide Dr Stewart with payment of fixed remuneration in whole or in part in lieu of notice. For the avoidance of doubt, the Company's right to make such a payment does not give Dr Stewart any right to receive such a payment.

Name: Ganbayar Lkhagvasuren
 Title: Executive Director
 Details: Mr Lkhagvasuren's fixed remuneration is an annual salary package of US\$265,000 including compulsory taxes and social insurance applicable as an employee in Mongolia. In the event of Mr Lkhagvasuren's employment being terminated other than in the case of misconduct, Mr Lkhagvasuren must give a minimum of 6 months' notice prior to termination, and the Company must give 9 months' notice prior to termination.

Name: Munkhsaikhan Dambiinyam
 Title: Chief Financial Officer
 Details: Mr Dambiinyam's fixed remuneration is an annual salary package of US\$167,000 including compulsory taxes and social insurance applicable as an employee in Mongolia. In the event of termination of Mr Dambiinyam's employment other than in the case of misconduct, Mr Dambiinyam must give a minimum of 6 months' notice prior to termination, and the Company must give 6 months' notice prior to termination.

Name: Mathew Brown
 Title: Chief Geologist
 Details: Mr. Brown's remuneration is calculated on the basis of annual salary package of A\$220,000 included any applicable taxes withheld. Post June 2018, Mr. Brown had an option to work for selected days in a month and he was paid proportionately for the days worked. In the event of termination of Mr Brown's employment other than in the case of misconduct, Mr Brown must give a minimum of 6 months' notice prior to termination, and the Company must give 6 months' notice prior to termination.

Management's Discussion and Analysis

continued

Key management personnel have no entitlement to termination payments in the event of removal for misconduct.

Share-based compensation

Issue of shares

Details of shares issued to Directors and other key management personnel as part of compensation during the period ended December 31, 2018 are set out below:

Name	Date	Shares	Issue price	\$
M Engelbrecht	June 27, 2018	333,334	\$0.00	-

Options

There were no options over ordinary shares granted to or vested by Directors and other key management personnel as part of compensation during the period ended December 31, 2018.

Share rights

Details of share rights over ordinary shares granted, vested and lapsed for Directors and other key management personnel as part of compensation during the period ended December 31, 2018 are set out below:

Name	Grant date	Expiry date	Number of rights granted	Fair value of rights granted \$	Number of rights vested	Fair value of rights vested \$	Number of rights lapsed
<i>Non-Executive Directors:</i>							
M Engelbrecht	December 23, 2015	June 16, 2018	-		333,334	53,333	-

Additional information

The section below contains further detail on how the Company's performance has impacted on remuneration outcomes for executives under the Company's incentive programs.

The table below contains a snapshot of the Company's performance against annual financial Key Performance Indicators:

	Jun 2014	Dec 2014*	2015	2016	2017	2018
Share price at financial year end (\$)	0.04	0.10	0.11	0.21	0.28	0.105
Basic loss per share (cents per share)	(4.09)	(1.21)	(1.15)	(0.47)	(0.72)	(1.00)
Diluted loss per share (cents per share)	(4.09)	(1.21)	(1.15)	(0.47)	(0.72)	(1.00)

* 6 months period

Additional disclosures relating to key management personnel

Shareholding

The number of ordinary shares in the Company held during the financial period by each Director and other members of key management personnel of the Group, including their personally related parties, is set out below:

	Balance at the start of the period	On-market purchases	Vesting of share rights	Balance at the end of the period
<i>Non-Executive Directors</i>				
K Tomlinson	290,000	104,547	-	394,547
H Badenach	1,301,738	109,000	-	1,410,738
D Clark	1,661,500	260,000	-	1,921,500
M Engelbrecht	766,666	-	333,334	1,100,000
M Muscillo	-	54,037	-	54,037
<i>Executive Directors:</i>				
A Stewart	4,031,083	261,000	-	4,292,083
G Lkhagvasuren	16,558,329	-	-	16,558,329
<i>Other KMP:</i>				
M Dambiinyam	1,478,578	-	-	1,478,578
M Brown	-	-	-	-
	<u>26,087,894</u>	<u>788,584</u>	<u>333,334</u>	<u>27,209,812</u>

Management's Discussion and Analysis

continued

Share rights holding

The number of share rights over ordinary shares in the Company held during the financial period by each Director and other members of key management personnel of the Group, including their personally related parties, is set out below:

	Balance at the start of the period	Granted	Vested and exercised	Balance at the end of the period
<i>Share rights over ordinary shares</i>				
K Tomlinson	3,000,000	-	-	3,000,000
D Clark	1,000,000	-	-	1,000,000
M Engelbrecht	333,334	-	(333,334)	-
M Muscillo	1,000,000	-	-	1,000,000
A Stewart	7,000,000	-	-	7,000,000
G Lkhagvasuren	4,000,000	-	-	4,000,000
M Dambiinyam	2,000,000	-	-	2,000,000
M Brown	2,000,000	-	-	2,000,000
	<u>20,333,334</u>	<u>-</u>	<u>(333,334)</u>	<u>20,000,000</u>

This concludes the remuneration report, which has been audited.

Shares under option

Unissued ordinary shares of Xanadu Mines Ltd under option at the date of this report are as follows:

Grant date	Description	Expiry date	Exercise price	Number under option
June 26, 2018	June 2018 private placement options	June 26, 2020	\$0.25	29,411,759
				<u>29,411,759</u>

No person entitled to exercise the options had or has any right by virtue of the option to participate in any share issue of the Company or of any other body corporate.

Shares under share rights

Unissued ordinary shares of Xanadu Mines Ltd under share rights at the date of this report are as follows:

Grant date	Expiry date (vesting price)	Exercise price	Number under rights
July 26, 2017	July 26, 2019 (vesting range*: \$0.40-\$0.60)	\$0.00	4,000,000
November 16, 2017	May 29, 2019 (vesting range*: \$0.40-\$0.60)	\$0.00	10,000,000
November 16, 2017	July 26, 2019 (vesting range*: \$0.40-\$0.60)	\$0.00	4,000,000
November 16, 2017	October 11, 2019 (vesting range*: \$0.40-\$0.60)	\$0.00	2,000,000
			<u>20,000,000</u>

* The share rights vest where the volume weighted average price for 45 consecutive days during the period from the grant date to the day immediately preceding the vesting date exceeds the hurdle price.

Share-based payments is measured by reference to the fair value at the date at which they are granted. The fair value of the options is determined by an independent written valuation. Share-based payments expense is amortised over the vesting period. No expense is recognised for awards that do not ultimately vest, except for awards where vesting is only conditional upon a market condition.

No person entitled to exercise the share rights had or has any right by virtue of the share right to participate in any share issue of the Company or of any other body corporate. Details of the vesting conditions of the share rights, including share price thresholds, are described in the notes to the financial statements.

Shares issued on the exercise of options

There were no ordinary shares of Xanadu Mines Ltd issued on the vesting and exercise of options during the period ended December 31, 2018 and up to the date of this report.

Management's Discussion and Analysis

continued

Indemnity and insurance of officers

During or since the end of the year, the Company has not given any indemnity to a current or former officer or auditor against a liability or made any agreement under which an officer or auditor may be given any indemnity of the kind covered by subsection 199A(2) or (3) of the Corporations Act 2001. During the financial period, the Company paid a premium in respect of a contract to insure the Directors and Officers of the Company against a liability to the extent permitted by the Corporations Act 2001. The contract of insurance prohibits disclosure of the nature of the liability and the amount of the premium.

Indemnity and insurance of auditor

To the extent permitted by law, the Company has agreed to indemnify the auditors, Ernst & Young, as part of the terms of its audit engagement against claims by third parties arising from the audit. No payment has been made to indemnify the auditors during the financial year. During the financial period, the Company has not paid a premium in respect of a contract to insure the auditor of the Company or any related entity.

Proceedings on behalf of the Company

No person has applied to the Court under section 237 of the Corporations Act 2001 for leave to bring proceedings on behalf of the Company, or to intervene in any proceedings to which the Company is a party for the purpose of taking responsibility on behalf of the Company for all or part of those proceedings.

Non-audit services

Details of the amounts paid or payable to the auditor for non-audit services provided during the financial period by the auditor are outlined in Note 21 to the financial statements. The non-audit services in relation to reviews of the prospectus for the Company's listing on TSX and tax advice were provided by Ernst & Young during the financial year. The fees, excluding GST, were \$85,660 (2017: \$1,200) for those services. The Directors are satisfied that given the total quantum paid for the non-audit services provided during the financial year by Ernst & Young as the external auditor, the general standard of independence for auditors imposed by the Corporations Act 2001 was not compromised.

Officers of the Company who are former partners of Ernst & Young

There are no officers of the Company who are former partners of Ernst & Young.

Rounding of amounts

The Company is of a kind referred to in the Corporations Instrument 2016/191, issued by the Australian Securities and Investments Commission, relating to 'rounding-off'. Amounts in this report have been rounded off in accordance with that Corporations Instrument to the nearest thousand dollars, or in certain cases, the nearest dollar.

Auditor's independence declaration

A copy of the auditor's independence declaration as required under section 307C of the Corporations Act 2001 is set out on the following page.

Auditor

Ernst & Young continues in office in accordance with section 327 of the Corporations Act 2001.

This report is made in accordance with a resolution of directors, pursuant to section 298(2)(a) of the Corporations Act 2001.

On behalf of the Directors



Kevin Tomlinson

Non-Executive Chairman

March 15, 2019

Auditor's Independence Declaration



Ernst & Young
200 George Street
Sydney NSW 2000 Australia
GPO Box 2646 Sydney NSW 2001

Tel: +61 2 9248 5555
Fax: +61 2 9248 5959
ey.com/au

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

As lead auditor for the audit of Xanadu Mines for the financial year ended 31 December 2018, I declare to the best of my knowledge and belief, there have been:

- a) no contraventions of the auditor independence requirements of the *Corporations Act 2001* in relation to the audit; and
- b) no contraventions of any applicable code of professional conduct in relation to the audit.

This declaration is in respect of the financial report of Xanadu Mines Limited and the entities it controlled during the financial year.

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

Ernst & Young

A handwritten signature in black ink that reads 'Scott Jarrett'.

Scott Jarrett
Partner
15 March 2019

Statement of Profit or Loss and Other Comprehensive Income

For the period ended December 31, 2018

	Note	Consolidated	
		2018 \$'000	2017 \$'000
Other income	4	21	169
Expenses			
Depreciation and amortisation expense		(81)	(91)
Other expenses	5	(6,326)	(3,535)
Finance costs		(31)	(344)
Revaluation gain/(loss) on financial assets at fair value through profit or loss		90	(30)
Loss before income tax expense		(6,327)	(3,831)
Income tax expense	6	-	-
Loss after income tax expense for the period		(6,327)	(3,831)
Other comprehensive income			
<i>Items that may be reclassified subsequently to profit or loss</i>			
Foreign currency translation		702	(1,957)
Other comprehensive income for the period, net of tax		702	(1,957)
Total comprehensive income for the period		(5,625)	(5,788)
Loss for the period is attributable to:			
Non-controlling interest		(146)	11
Owners of Xanadu Mines Ltd	15	(6,181)	(3,842)
		(6,327)	(3,831)
Total comprehensive income for the period is attributable to:			
Non-controlling interest		(259)	374
Owners of Xanadu Mines Ltd		(5,366)	(6,162)
		(5,625)	(5,788)
		Cents	Cents
Basic loss per share	29	(1.00)	(0.72)
Diluted loss per share	29	(1.00)	(0.72)

The above statement of profit or loss and other comprehensive income should be read in conjunction with the accompanying notes

Statement of Financial Position

As at December 31, 2018

	Note	Consolidated	
		2018 \$'000	2017 \$'000
Assets			
Current assets			
Cash and cash equivalents	7	5,225	9,065
Financial assets at fair value through profit or loss	8	190	100
Prepayment and other assets		-	5
Other receivables	9	398	498
Total current assets		<u>5,813</u>	<u>9,668</u>
Non-current assets			
Property, plant and equipment	10	360	388
Deferred exploration expenditure	11	45,903	37,157
Total non-current assets		<u>46,263</u>	<u>37,545</u>
Total assets		<u><u>52,076</u></u>	<u><u>47,213</u></u>
Liabilities			
Current liabilities			
Trade and other payables	12	680	1,262
Total current liabilities		<u>680</u>	<u>1,262</u>
Non-current liabilities			
Other		134	159
Total non-current liabilities		<u>134</u>	<u>159</u>
Total liabilities		<u>814</u>	<u>1,421</u>
Net assets		<u><u>51,262</u></u>	<u><u>45,792</u></u>
Equity			
Issued capital	13	117,850	108,452
Reserves	14	(1)	(2,513)
Accumulated losses	15	(71,345)	(65,164)
Equity attributable to the owners of Xanadu Mines Ltd		46,504	40,775
Non-controlling interest	16	4,758	5,017
Total equity		<u><u>51,262</u></u>	<u><u>45,792</u></u>

The above statement of financial position should be read in conjunction with the accompanying notes

Statement of Changes in Equity

For the period ended December 31, 2018

Consolidated	Issued capital \$'000	Other reserves \$'000	Foreign currency translation reserve \$'000	Transactions with owners reserve \$'000	Accumulated losses \$'000	Non-controlling interest \$'000	Total equity \$'000
Balance at January 1, 2017	93,965	8,208	(8,727)	-	(61,322)	4,643	36,766
Profit/(loss) after income tax expense for the period	-	-	-	-	(3,842)	11	(3,831)
Other comprehensive income for the period, net of tax	-	-	(2,320)	-	-	363	(1,957)
Total comprehensive income for the period	-	-	(2,320)	-	(3,842)	374	(5,788)
<i>Transactions with owners in their capacity as owners:</i>							
Contributions of equity, net of transaction costs (note 13)	14,487	-	-	-	-	-	14,487
Share-based payments (note 30)	-	326	-	-	-	-	326
Balance at December 31, 2017	108,452	8,535	(11,047)	-	(65,164)	5,017	45,792

Consolidated	Issued capital \$'000	Other reserves \$'000	Foreign currency translation reserve \$'000	Transactions with owners reserve \$'000	Accumulated losses \$'000	Non-controlling interest \$'000	Total equity \$'000
Balance at January 1, 2018	108,450	8,534	(11,047)	-	(65,164)	5,017	45,792
Profit/(loss) after income tax expense for the period	-	-	-	-	(6,181)	(146)	(6,327)
Other comprehensive income for the period, net of tax	-	-	815	-	-	(113)	702
Total comprehensive income for the period	-	-	815	-	(6,181)	(259)	(5,625)
<i>Transactions with owners in their capacity as owners:</i>							
Contributions of equity, net of transaction costs (note 13)	9,398	-	-	-	-	-	9,398
Share-based payments (note 30)	-	1,697	-	-	-	-	1,697
Other	-	-	537	(537)	-	-	-
Balance at December 31, 2018	117,850	10,231	(9,695)	(537)	(71,345)	4,758	51,262

The above statement of changes in equity should be read in conjunction with the accompanying notes

Statement of Cash Flows

For the period ended December 31, 2018

	Note	Consolidated	
		2018 \$'000	2017 \$'000
Cash flows from operating activities			
Payments to suppliers and employees		(4,510)	(2,968)
Interest received		21	24
Interest and other finance costs paid		(31)	(427)
Net cash used in operating activities	28	(4,520)	(3,371)
Cash flows from investing activities			
Payments for property, plant and equipment	10	-	(220)
Payments for exploration and evaluation	11	(8,874)	(6,237)
Proceeds from disposal of property, plant and equipment		-	26
Net cash used in investing activities		(8,874)	(6,431)
Cash flows from financing activities			
Proceeds from issue of shares	13	10,000	13,945
Repayment of borrowings		-	(2,092)
Transaction costs on issue of shares		(602)	(869)
Net cash from financing activities		9,398	10,984
Net increase in cash and cash equivalents		(3,996)	1,182
Cash and cash equivalents at the beginning of the financial period		9,065	8,277
Effects of exchange rate changes on cash and cash equivalents		156	(394)
Cash and cash equivalents at the end of the financial period	7	5,225	9,065

The above statement of cash flows should be read in conjunction with the accompanying notes

Notes to the Financial Statements

For the period ended December 31, 2018

Note 1. Significant accounting policies

The principal accounting policies adopted in the preparation of the financial statements are set out below. These policies have been consistently applied to all the periods presented, unless otherwise stated.

Basis of preparation

These financial statements have been prepared in accordance with Australian Accounting Standards and Interpretations issued by the Australian Accounting Standards Board ("AASB") and the Corporations Act 2001, as appropriate for for-profit oriented entities. These financial statements also comply with International Financial Reporting Standards as issued by the International Accounting Standards Board ("IASB").

Historical cost convention

The financial statements have been prepared under the historical cost convention, except for, where applicable, the revaluation of financial assets and liabilities at fair value through profit or loss, financial assets at fair value through other comprehensive income, investment properties, certain classes of property, plant and equipment and derivative financial instruments.

Critical accounting estimates

The preparation of the financial statements requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying Xanadu's accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the financial statements, are disclosed in Note 2 to the financial statements.

Parent entity information

In accordance with the Corporations Act 2001, these financial statements present the results of Xanadu only. Supplementary information about the parent entity is disclosed in Note 25 to the financial statements.

Principles of consolidation

The consolidated financial statements incorporate the assets and liabilities of all subsidiaries of Xanadu Mines Ltd ("Company" or "parent entity") as at December 31, 2018 and the results of all subsidiaries for the period then ended. Xanadu Mines Ltd and its subsidiaries together are referred to in these financial statements as the "Group".

Subsidiaries are all those entities over which Xanadu has control. Xanadu controls an entity when the Company is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power to direct the activities of the entity. Subsidiaries are fully consolidated from the date on which control is transferred to the Company. They are de-consolidated from the date that control ceases.

Intercompany transactions, balances and unrealised gains on transactions between entities in the Company are eliminated. Unrealised losses are also eliminated unless the transaction provides evidence of the impairment of the asset transferred. Accounting policies of subsidiaries have been changed where necessary to ensure consistency with the policies adopted by the Company.

The acquisition of subsidiaries is accounted for using the acquisition method of accounting. A change in ownership interest, without the loss of control, is accounted for as an equity transaction, where the difference between the consideration transferred and the book value of the share of the non-controlling interest acquired is recognised directly in equity attributable to the parent.

Non-controlling interest in the results and equity of subsidiaries are shown separately in the statement of profit or loss and other comprehensive income, statement of financial position and statement of changes in equity of the Company. Losses incurred by the Company are attributed to the non-controlling interest in full, even if that results in a deficit balance.

When Xanadu loses control over a subsidiary, it derecognises the assets including goodwill, liabilities and non-controlling interest in the subsidiary together with any cumulative translation differences recognised in equity. The Company recognises the fair value of the consideration received and the fair value of any investment retained together with any gain or loss in profit or loss.

Notes to the Financial Statements

continued

Foreign currency translation

The financial statements are presented in Australian dollars, which is Xanadu's functional and presentation currency. The functional currencies of the Company's foreign subsidiaries are Mongolian Tughrig ("MNT") and Singapore Dollar ("SGD").

Foreign currency transactions

Foreign currency transactions are translated into Australian dollars using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at financial period-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in profit or loss.

Foreign operations

The assets and liabilities of foreign operations are translated into Australian dollars using the exchange rates at the reporting date. The revenues and expenses of foreign operations are translated into Australian dollars using the average exchange rates, which approximate the rates at the dates of the transactions, for the period. All resulting foreign exchange differences are recognised in other comprehensive income through the foreign currency reserve in equity.

The foreign currency reserve is recognised in profit or loss when the foreign operation or net investment is disposed of.

New or amended Accounting Standards and Interpretations adopted

The Company has adopted all of the new or amended AASB Standards that are mandatory for the applicable annual reporting periods. Any new or amended Accounting Standards or Interpretations that are not yet mandatory have not been early adopted.

AASB 9 Financial Instruments

AASB 9 contains accounting requirements for financial instruments, replacing AASB 139 *Financial Instruments: Recognition and Measurement*. The standard contains requirements in the areas of classification and measurement, impairment, hedge accounting and derecognition. This standard applies to annual reporting periods beginning on or after 1 January 2018. The Company has applied the new standard for the current annual financial report for the year ended 31 December 2018, and there has been no material impact.

AASB 15 Revenue from Contracts with Customers

AASB 15 provides a single, principles-based five-step model to be applied to all contracts with customers. Guidance is provided on topics such as the point in which revenue is recognised, accounting for variable consideration, costs of fulfilling and obtaining a contract and various related matters. New disclosures about revenue are also introduced. This standard applies to annual reporting periods beginning on or after January 1, 2018. The Company has no revenue and the application of the new standard for the current annual financial report for the year ended December 31, 2018, had no impact.

AASB 16 Leases

AASB 16 provides a new lessee accounting model which requires a lessee to recognise assets and liabilities for all leases with a term of more than 12 months, unless the underlying asset is of low value. A lessee will be required to measure right-of-use assets in a manner similar to how other non-financial assets, lease liabilities and other financial liabilities are measured. Assets and liabilities arising from a lease are initially measured on a present value basis. The measurement includes non-cancellable lease payments (including inflation-linked payments), and also includes payments to be made in optional periods if the lessee is reasonably certain to exercise an option to extend the lease, or not to exercise an option to terminate the lease. AASB 16 contains disclosure requirements for lessees. The company has assessed the potential impact of the new standard on the Company's financial report and expects no material impact. This standard applies to annual reporting periods beginning on or after January 1, 2019.

AASB 2016-5 Amendments to Australian Accounting Standards - Classification and Measurement of Share-based Payment Transactions

This standard amends AASB 2 *Share-based Payments*, clarifying how to account for certain types of share-based payment transactions. The amendments provide requirements on the accounting for the:

- effects of vesting and non-vesting conditions on the measurement of cash-settled share-based payments;
- share-based payment transactions with a net settlement feature for withholding tax obligations; and
- modification to the terms and conditions of a share-based payment that changes the classification of the transaction from cash-settled to equity-settled.

This standard applies to annual reporting periods beginning on or after January 1, 2018. The Company has applied the new standard for the current annual financial report for the year ended December 31, 2018, and there has been no material impact.

AASB Interpretation 22 Foreign Currency Transactions and Advance Considerations

Notes to the Financial Statements

continued

The Interpretation clarifies that, in determining the spot exchange rate to use on initial recognition of the related asset, expense or income (or part of it) or on the derecognition of a non-monetary asset or non-monetary liability relating to advance consideration, the date of the transaction is the date on which an entity initially recognises the non-monetary asset or non-monetary liability arising from the advance consideration. If there are multiple payments or receipts in advance, then the entity must determine the date of the transactions for each payment or receipt of advance consideration.

This Interpretation does not have any material impact on the current annual financial report for the year ended December 31, 2018.

Revenue recognition

Interest income

Interest revenue is recognised as interest accrues using the effective interest method. This is a method of calculating the amortised cost of a financial asset and allocating the interest income over the relevant period using the effective interest rate, which is the rate that exactly discounts estimated future cash receipts through the expected life of the financial asset to the net carrying amount of the financial asset.

Income tax

The income tax expense or benefit for the period is the tax payable on that period's taxable income based on the applicable income tax rate for each jurisdiction, adjusted by the changes in deferred tax assets and liabilities attributable to temporary differences, unused tax losses and the adjustment recognised for prior periods, where applicable.

Deferred tax assets and liabilities are recognised for temporary differences at the tax rates expected to be applied when the assets are recovered or liabilities are settled, based on those tax rates that are enacted or substantively enacted, except for:

- when the deferred income tax asset or liability arises from the initial recognition of goodwill or an asset or liability in a transaction that is not a business combination and that, at the time of the transaction, affects neither the accounting nor taxable profits; or
- when the taxable temporary difference is associated with interests in subsidiaries, associates or joint ventures, and the timing of the reversal can be controlled and it is probable that the temporary difference will not reverse in the foreseeable future.

Deferred tax assets are recognised for deductible temporary differences and unused tax losses only if it is probable that future taxable amounts will be available to utilise those temporary differences and losses.

The carrying amount of recognised and unrecognised deferred tax assets are reviewed at each reporting date. Deferred tax assets recognised are reduced to the extent that it is no longer probable that future taxable profits will be available for the carrying amount to be recovered. Previously unrecognised deferred tax assets are recognised to the extent that it is probable that there are future taxable profits available to recover the asset.

Deferred tax assets and liabilities are offset only where there is a legally enforceable right to offset current tax assets against current tax liabilities and deferred tax assets against deferred tax liabilities; and they relate to the same taxable authority on either the same taxable entity or different taxable entities which intend to settle simultaneously.

Income taxes relating to items recognised directly in equity are recognised in equity and not in the income statement.

Other taxes

Revenues, expenses and assets are recognised net of the amount of GST except:

- where the GST incurred on a purchase of goods and services is not recoverable from the taxation authority, in which case the GST is recognised as part of the cost of acquisition of the asset or as part of the expense item as applicable; and
- receivables and payables are stated with the amount of GST included.

The net amount of GST recoverable from, or payable to, the taxation authority is included as part of receivables or payables in the balance sheet.

Cash flows are included in the Cash Flow Statement on a gross basis and the GST component of cash flows arising from investing and financing activities, which is recoverable from, or payable to, the taxation authority are classified as operating cash flows.

Commitments and contingencies are disclosed net of the amount of GST recoverable from, or payable to, the taxation authority.

Notes to the Financial Statements

continued

Current and non-current classification

Assets and liabilities are presented in the Statement of Financial Position based on current and non-current classification.

An asset is classified as current when: it is either expected to be realised or intended to be sold or consumed in the Company's normal operating cycle; it is held primarily for the purpose of trading; it is expected to be realised within 12 months after the reporting period; or the asset is cash or cash equivalent unless restricted from being exchanged or used to settle a liability for at least 12 months after the reporting period. All other assets are classified as non-current.

A liability is classified as current when: it is either expected to be settled in the Company's normal operating cycle; it is held primarily for the purpose of trading; it is due to be settled within 12 months after the reporting period; or there is no unconditional right to defer the settlement of the liability for at least 12 months after the reporting period. All other liabilities are classified as non-current.

Deferred tax assets and liabilities are always classified as non-current.

Cash and cash equivalents

Cash and short-term deposits in the balance sheet comprise cash at bank and in hand and short-term deposits with an original maturity of three months or less.

For the purposes of the Cash Flow Statement, cash and cash equivalents consist of cash and cash equivalents as defined above, net of outstanding bank overdrafts.

Financial Assets

Financial assets are classified, at initial recognition, as subsequently measured at amortised cost, fair value through other comprehensive income ("OCI"), and fair value through profit or loss.

The classification of financial assets at initial recognition depends on the financial asset's contractual cash flow characteristics and the Company's business model for managing them. Xanadu initially measures a financial asset at its fair value plus, in the case of a financial asset not at fair value through profit or loss, transaction costs.

In order for a financial asset to be classified and measured at amortised cost or fair value through OCI, it needs to give rise to cash flows that are 'solely payments of principal and interest ("SPPI")' on the principal amount outstanding. This assessment is referred to as the SPPI test and is performed at an instrument level.

Xanadu's business model for managing financial assets refers to how it manages its financial assets in order to generate cash flows. The business model determines whether cash flows will result from collecting contractual cash flows, selling the financial assets, or both.

Financial assets at amortised cost are subsequently measured using the effective interest (EIR) method and are subject to impairment. Gains and losses are recognised in profit or loss when the asset is derecognised, modified or impaired.

Upon initial recognition, the Company can elect to classify irrevocably its equity investments as equity instruments designated at fair value through OCI when they meet the definition of equity under IAS 32 *Financial Instruments: Presentation* and are not held for trading. The classification is determined on an instrument-by-instrument basis.

Gains and losses on these financial assets are never recycled to profit or loss. Dividends are recognised as other income in the Statement of Profit or Loss when the right of payment has been established, except when Xanadu benefits from such proceeds as a recovery of part of the cost of the financial asset, in which case, such gains are recorded in OCI. Equity instruments designated at fair value through OCI are not subject to impairment assessment.

Financial assets at fair value through profit or loss are carried in the Statement of Financial Position at fair value with net changes in fair value recognised in the Statement of Profit or Loss. Typically, such financial assets will be either: (i) held for trading, where they are acquired for the purpose of selling in the short-term with an intention of making a profit, or a derivative; or (ii) designated as such upon initial recognition where permitted.

Impairment of financial assets

Xanadu recognises an allowance for expected credit losses ("ECLs") for all debt instruments not held at fair value through profit or loss. ECLs are based on the difference between the contractual cash flows due in accordance with the contract and all the cash flows that

Notes to the Financial Statements

continued

the Company expects to receive, discounted at an approximation of the original effective interest rate. The expected cash flows will include cash flows from the sale of collateral held or other credit enhancements that are integral to the contractual terms.

ECLs are recognised in two stages. For credit exposures for which there has not been a significant increase in credit risk since initial recognition, ECLs are provided for credit losses that result from default events that are possible within the next 12-months (a 12-month ECL). For those credit exposures for which there has been a significant increase in credit risk since initial recognition, a loss allowance is required for credit losses expected over the remaining life of the exposure, irrespective of the timing of the default (a lifetime ECL).

At each reporting date, Xanadu assesses whether there is any indication that an asset may be impaired. Where an indicator of impairment exists, the Company makes a formal estimate of the recoverable amount. Where the carrying amount of an asset exceeds its expected recoverable cash flows the asset is considered impaired and is written down to its recoverable amount.

Deferred exploration and evaluation expenditure

Costs arising from exploration and evaluation activities relating to an area of interest are carried forward, provided such costs are expected to be recouped through successful development, or by sale, or where exploration and evaluation activities have not, at balance date, reached a stage to allow a reasonable assessment regarding the existence of economically recoverable resources. Rights of tenure must be current to carry forward deferred exploration and evaluation expenditure.

Costs carried forward in respect of an area of interest that is abandoned are written off in the year in which the decision to abandon is made. Costs on productive areas are amortised over the life of the area of interest to which such costs relate on the production output basis.

Property, plant and equipment

Land and buildings are shown at fair value, based on periodic, at least every 3 years, valuations by external independent valuers, less subsequent depreciation and impairment for buildings. The valuations are undertaken more frequently if there is a material change in the fair value relative to the carrying amount. Any accumulated depreciation at the date of revaluation is eliminated against the gross carrying amount of the asset and the net amount is restated to the revalued amount of the asset. Increases in the carrying amounts arising on revaluation of land and buildings are credited in other comprehensive income through to the revaluation surplus reserve in equity. Any revaluation decrements are initially taken in other comprehensive income through to the revaluation surplus reserve to the extent of any previous revaluation surplus of the same asset. Thereafter the decrements are taken to profit or loss.

Plant and equipment are stated at historical cost less accumulated depreciation and impairment. Historical cost includes expenditure that is directly attributable to the acquisition of the items.

Depreciation is calculated on a straight-line basis to write off the net cost of each item of property, plant and equipment (excluding land) over their expected useful lives as follows:

Plant and equipment: 2-10 years

Motor vehicles: 4-5 years

The residual values, useful lives and depreciation methods are reviewed, and adjusted if appropriate, at each reporting date.

An item of property, plant and equipment is derecognised upon disposal or when there is no future economic benefit to the Company. Gains and losses between the carrying amount and the disposal proceeds are taken to profit or loss. Any revaluation surplus reserve relating to the item disposed of is transferred directly to retained profits.

The carrying values of property, plant and equipment are reviewed for impairment when events or changes in circumstances indicate the carrying value may not be recoverable.

For an asset that does not generate largely independent cash inflows, the recoverable amount is determined for the cash-generating unit to which the asset belongs.

If any such indication exists and where the carrying values exceed the estimated recoverable amount, the assets or cash generating units are written down to their recoverable amount. The recoverable amount of property, plant and equipment is the greater of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value

Notes to the Financial Statements

continued

using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. Impairment losses are recognised in the income statement.

Investment in Joint Venture

An associate is an entity over which the consolidated entity has significant influence. Significant influence is the power to participate in the financial and operating policy decisions of the investee, but is not control or joint control over those policies.

A joint venture is a type of joint arrangement whereby the parties that have joint control of the arrangement have rights to the net assets of the joint venture. Joint control is the contractually agreed sharing of control of an arrangement, which exists only when decisions about the relevant activities require unanimous consent of the parties sharing control.

The considerations made in determining significant influence or joint control are similar to those necessary to determine control over subsidiaries.

The consolidated entity's investments in its associate and joint venture are accounted for using the equity method.

Under the equity method, the investment in an associate or a joint venture is initially recognised at cost. The carrying amount of the investment is adjusted to recognise changes in the consolidated entity's share of net assets of the associate or joint venture since the acquisition date. Goodwill relating to the associate or joint venture is included in the carrying amount of the investment and is neither amortised nor individually tested for impairment.

The Statement of Profit or Loss reflects the consolidated entity's share of the results of operations of the associate or joint venture. Any change in OCI of those investees is presented as part of the consolidated entity's OCI. In addition, when there has been a change recognised directly in the equity of the associate or joint venture, the consolidated entity recognises its share of any changes, when applicable, in the statement of changes in equity. Unrealised gains and losses resulting from transactions between the consolidated entity and the associate or joint venture are eliminated to the extent of the interest in the associate or joint venture.

The aggregate of the consolidated entity's share of profit or loss of an associate and a joint venture is shown on the face of the Statement of Profit or Loss outside operating profit and represents profit or loss after tax and non-controlling interests in the subsidiaries of the associate or joint venture.

The financial statements of the associate or joint venture are prepared for the same reporting period as the consolidated entity. When necessary, adjustments are made to bring the accounting policies in line with those of the consolidated entity.

After application of the equity method, the consolidated entity determines whether it is necessary to recognise an impairment loss on its investment in its associate or joint venture. At each reporting date, the consolidated entity determines whether there is objective evidence that the investment in the associate or joint venture is impaired. If there is such evidence, the consolidated entity calculates the amount of impairment as the difference between the recoverable amount of the associate or joint venture and its carrying value, then recognises the loss as 'Share of profit of an associate and a joint venture' in the Statement of Profit or Loss.

Rehabilitation of property

Where conditions of title, or other rights to use property including rights to mine require that rehabilitation activities be carried out during the course of the use of the property, costs of such are brought to account as an expense at the time incurred. Where, due to current or previous activities, an obligation exists to carry out rehabilitation works in the future, provision is made for the mine site rehabilitation and restoration by recognising the present value of expected rehabilitation cash flows as a provision. These provisions include costs associated with reclamation, plant closure and monitoring activities. The discount on the provision unwinds as an interest expense. These costs have been determined on the basis of current costs, current legal requirements and current technology. Changes in estimates are dealt with on a prospective basis.

Uncertainty exists as to the amount of restoration obligations which will be incurred due to:

- uncertainty as to the remaining life of existing operating sites; and
- the impact of changes in environmental legislation.

Assumptions have been made as to the remaining useful life of existing sites based on studies conducted by independent and internal technical advisers. Such studies are conducted on an ongoing basis.

Notes to the Financial Statements

continued

Impairment of non-financial assets

Goodwill and other intangible assets that have an indefinite useful life are not subject to amortisation and are tested annually for impairment, or more frequently if events or changes in circumstances indicate that they might be impaired. Other non-financial assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount.

Recoverable amount is the higher of an asset's fair value less costs of disposal and value-in-use. The value-in-use is the present value of the estimated future cash flows relating to the asset using a pre-tax discount rate specific to the asset or cash-generating unit to which the asset belongs. Assets that do not have independent cash flows are grouped together to form a cash-generating unit.

Trade and other payables

Liabilities are recognised for amounts to be paid in the future for goods or services received, whether or not billed to Xanadu. Trade accounts payable are normally settled within 30 days.

Fair value measurement

When an asset or liability, financial or non-financial, is measured at fair value for recognition or disclosure purposes, the fair value is based on the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date; and assumes that the transaction will take place either: in the principal market; or in the absence of a principal market, in the most advantageous market.

Fair value is measured using the assumptions that market participants would use when pricing the asset or liability, assuming they act in their economic best interest. For non-financial assets, the fair value measurement is based on its highest and best use. Valuation techniques that are appropriate in the circumstances and for which sufficient data are available to measure fair value are used, maximising the use of relevant observable inputs and minimising the use of unobservable inputs.

Assets and liabilities measured at fair value are classified into three levels, using a fair value hierarchy that reflects the significance of the inputs used in making the measurements. Classifications are reviewed at each reporting date and transfers between levels are determined based on a reassessment of the lowest level of input that is significant to the fair value measurement.

For recurring and non-recurring fair value measurements, external valuers may be used when internal expertise is either not available or when the valuation is deemed to be significant. External valuers are selected based on market knowledge and reputation. Where there is a significant change in fair value of an asset or liability from one period to another, an analysis is undertaken, which includes a verification of the major inputs applied in the latest valuation and a comparison, where applicable, with external sources of data.

Issued capital

Ordinary shares are classified as equity.

Incremental costs directly attributable to the issue of new shares or options are shown in equity as a deduction, net of tax, from the proceeds.

Earnings per share

Basic earnings per share is calculated by dividing the profit attributable to the owners of Xanadu, excluding any costs of servicing equity other than ordinary shares, by the weighted average number of ordinary shares outstanding during the financial period, adjusted for bonus elements in ordinary shares issued during the financial period.

Diluted earnings per share

Diluted earnings per share adjusts the figures used in the determination of basic earnings per share to consider the after-income tax effect of interest and other financing costs associated with dilutive potential ordinary shares and the weighted average number of shares assumed to have been issued for no consideration in relation to dilutive potential ordinary shares.

Share-based payment transactions

In addition to consulting fees and salaries, the consolidated entity provides benefits to certain directors and employees of the consolidated entity in the form of share-based payment transactions, whereby directors and employees render services in exchange for shares or rights over shares ("equity-settled transactions").

The cost of equity-settled transactions with employees (including directors) is measured by reference to the fair value at the date at

Notes to the Financial Statements

continued

which they are granted. The fair value of the options is determined by an independent written valuation.

The cost of equity-settled transactions is recognised, together with a corresponding increase in equity, over the period in which the vesting conditions, if any, are fulfilled.

The cumulative expenses recognised for equity-settled transactions at each reporting date until vesting date reflects:

- i) the extent to which the vesting period, if any, has expired; and
- ii) the consolidated entity's best estimate of the number of equity instruments that will ultimately vest. No adjustment is made for the likelihood of market performance conditions being met as the effect of these conditions is included in the determination of fair value at grant date. The income statement charge or credit for a period represents the movement in cumulative expense recognised as at the beginning and end of that period.

No expense is recognised for awards that do not ultimately vest, except for awards where vesting is only conditional upon a market condition.

If the terms of an equity-settled award are modified, as a minimum an expense is recognised as if the terms had not been modified. In addition, an expense is recognised for any modification that increases the total fair value of the share-based payment arrangement, or is otherwise beneficial to the employee, as measured at the date of modification.

If an equity-settled award is cancelled, it is treated as if it had vested on the date of the cancellation, and any expense not yet recognised is recognised immediately. However, if a new award is substituted for the cancelled award and designated a replacement award on the date it is granted, the cancelled and new award are treated as if they were a modification of the original award, as described in the previous paragraph.

Goods and Services Tax ('GST') and other similar taxes

Revenues, expenses and assets are recognised net of the amount of associated GST, unless the GST incurred is not recoverable from the tax authority. In this case it is recognised as part of the cost of the acquisition of the asset or as part of the expense.

Receivables and payables are stated inclusive of the amount of GST receivable or payable. The net amount of GST recoverable from, or payable to, the tax authority is included in other receivables or other payables in the statement of financial position.

Cash flows are presented on a gross basis. The GST components of cash flows arising from investing or financing activities which are recoverable from, or payable to the tax authority, are presented as operating cash flows.

Commitments and contingencies are disclosed net of the amount of GST recoverable from, or payable to, the tax authority.

Rounding of amounts

The Company is of a kind referred to in Corporations Instrument 2016/191, issued by the Australian Securities and Investments Commission, relating to 'rounding-off'. Amounts in this report have been rounded off in accordance with that Corporations Instrument to the nearest thousand dollars, or in certain cases, the nearest dollar.

Significant accounting judgements, estimates and assumptions

The preparation of the financial statements requires management to make judgements, estimates and assumptions that affect the reported amounts in the financial statements. Management continually evaluates its judgements and estimates in relation to assets, liabilities, contingent liabilities, revenue and expenses. Management bases its judgements, estimates and assumptions on historical experience and on other various factors, including expectations of future events, management believes to be reasonable under the circumstances. The resulting accounting judgements and estimates will seldom equal the related actual results. The judgements, estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities (refer to the respective Notes to the financial statements) within the next financial year are discussed below.

Share-based payment transactions

Xanadu measures the cost of equity-settled transactions with employees by reference to the fair value of the equity instruments at the date at which they are granted. The fair value is determined by using either the Binomial or Black-Scholes model considering the terms and conditions upon which the instruments were granted. The accounting estimates and assumptions relating to equity-settled share-based payments would have no impact on the carrying amounts of assets and liabilities within the next annual reporting period but may impact profit or loss and equity.

Notes to the Financial Statements

continued

Carrying value of exploration assets

Xanadu applies judgements in determining the carrying value of exploration assets in particular in determining which exploration costs should be capitalised or expensed. Xanadu assesses impairment of such assets at each reporting date by evaluating conditions specific to the Company.

Going concern basis of accounting

The financial statements have been prepared on a going concern basis, which contemplates the continuity of normal business activity and the realisation of assets and the settlement of liabilities in the normal course of business.

Note 2. Critical accounting judgements, estimates and assumptions

The preparation of the financial statements requires management to make judgements, estimates and assumptions that affect the reported amounts in the financial statements. Management continually evaluates its judgements and estimates in relation to assets, liabilities, contingent liabilities, revenue and expenses. Management bases its judgements, estimates and assumptions on historical experience and on other various factors, including expectations of future events, management believes to be reasonable under the circumstances. The resulting accounting judgements and estimates will seldom equal the related actual results. The judgements, estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities (refer to the respective notes) within the next financial year are discussed below.

Share-based payment transactions

Xanadu measures the cost of equity-settled transactions with employees by reference to the fair value of the equity instruments at the date at which they are granted. The fair value is determined by using either the Binomial or Black-Scholes model considering the terms and conditions upon which the instruments were granted. The accounting estimates and assumptions relating to equity-settled share-based payments would have no impact on the carrying amounts of assets and liabilities within the next annual reporting period but may impact profit or loss and equity.

Carrying value of exploration assets

Xanadu applies judgements in determining the carrying value of exploration assets in particular in determining which exploration costs should be capitalised or expensed. The Company assesses impairment of such assets at each reporting date by evaluating conditions specific to the Company and its subsidiaries.

Going concern basis of accounting

The financial statements have been prepared on a going concern basis, which contemplates the continuity of normal business activity and the realisation of assets and the settlement of liabilities in the normal course of business.

Note 3. Operating segments

Xanadu operates predominantly in the minerals exploration sector. The principle activity of the Company is exploration for copper and gold. Xanadu classifies these activities under a single operating segment, the Mongolian exploration projects. Regarding the exploration operating segment, the Chief Operating Decision Maker (determined to be the Board of Directors) receives information on the exploration expenditure incurred. This information is disclosed in deferred exploration expenditure note of the financial report. No segment revenues are disclosed, as all segment expenditure is capitalised, with the exception of expenditure written off. The non-current assets of Xanadu, attributable to the parent entity, are located in Mongolia.

Note 4. Other income

	Consolidated	
	2018	2017
	\$'000	\$'000
Interest	21	24
Gain on sale of plant and equipment	-	15
Deferred consideration received on sale of interest in tenement	-	130
Other income	21	169

Notes to the Financial Statements

continued

Note 5. Other expenses

	Consolidated	
	2018	2017
	\$'000	\$'000
Other expenses		
Administration and other expenses	2,343	1,461
Net foreign currency loss (gain)	(1)	1
Wages and management fees	2,287	1,747
Share-based payments	1,697	326
	<u>6,326</u>	<u>3,535</u>

Note 6. Income tax expense

	Consolidated	
	2018	2017
	\$'000	\$'000
<i>Numerical reconciliation of income tax expense and tax at the statutory rate</i>		
Loss before income tax expense	(6,327)	(3,831)
Tax at the statutory tax rate of 27.5% (2017: 30%)	(1,740)	(1,149)
Tax effect amounts which are not deductible/(taxable) in calculating taxable income:		
Tax effect of expenses not allowed for tax purposes	467	107
	(1,273)	(1,042)
Current period tax losses not recognised	1,147	858
Difference in overseas tax rates – Mongolia at 25% (2017: 25%)	20	57
Difference in overseas tax rates – Singapore at 17% (2017: 17%)	106	32
Income tax expense	<u>-</u>	<u>-</u>

At the reporting date, Xanadu has estimated tax losses of \$29,370,000 (Dec 2017: \$25,197,000). A deferred tax asset has not been recognised for these losses because it is not probable that future taxable income will be available to offset against such losses.

Note 7. Current assets – cash and cash equivalents

	Consolidated	
	2018	2017
	\$'000	\$'000
Cash at bank and on hand	<u>5,225</u>	<u>9,065</u>

Cash at bank earns interest at floating rates based on daily bank deposit rates.

Note 8. Current assets – financial assets at fair value through profit or loss

	Consolidated	
	2018	2017
	\$'000	\$'000
Ordinary shares - designated at fair value through profit or loss	<u>190</u>	<u>100</u>

Refer to Note 19 to the financial statements for further information on fair value measurement.

The ordinary shares relate to the 10,000,000 shares held in Aspire Mining Limited, a company listed on the ASX (ASX:AKM). The carrying value of the shares is based on the closing share price of AKM as at the reporting date.

Notes to the Financial Statements

continued

Note 9. Current assets – Other receivables

	Consolidated	
	2018	2017
	\$'000	\$'000
Sundry debtors	65	83
GST recoverable	333	415
	398	498

Sundry debtors relate to interest on term deposits accrued but not yet received, refund of goods and services tax payments due and other current loans. Balances within sundry debtors do not contain impaired assets and are not past due. It is expected that these balances will be received in full. Due to the short-term nature of these receivables, their carrying value is assumed to approximate their fair value. The maximum exposure to credit risk is the fair value of receivables.

Note 10. Non-current assets – Property, plant and equipment

	Consolidated	
	2018	2017
	\$'000	\$'000
Plant and equipment - at cost	440	393
Less: Accumulated depreciation	(302)	(259)
	138	134
Motor vehicles - at cost	352	347
Less: Accumulated depreciation	(130)	(93)
	222	254
	360	388

Reconciliations

Reconciliations of the written down values at the beginning and end of the current and previous financial period are set out below:

Consolidated	Plant & Equipment \$'000	Motor Vehicles \$'000	Total \$'000
Balance at January 1, 2017	97	210	307
Additions	82	138	220
Disposals	(1)	(54)	(55)
Exchange differences	(4)	(10)	(14)
Depreciation expense	(40)	(30)	(70)
	134	254	388
Balance at December 31, 2017	134	254	388
Exchange differences	48	5	53
Depreciation expense	(44)	(37)	(81)
	138	222	360
Balance at December 31, 2018	138	222	360

Note 11. Non-current assets – Deferred exploration expenditure

	Consolidated	
	2018	2017
	\$'000	\$'000
Deferred exploration expenditure	45,903	37,157

Notes to the Financial Statements

continued

Reconciliations

Reconciliations of the written down values at the beginning and end of the current and previous financial period are set out below:

Consolidated	Exploration & evaluation \$'000
Balance at January 1, 2017	31,952
Expenditure during the period	7,086
Exchange differences	(1,881)
	<hr/>
Balance at December 31, 2017	37,157
Expenditure during the period	8,290
Exchange differences	456
	<hr/>
Balance at December 31, 2018	<u>45,903</u>

Note 12. Current liabilities – trade and other payables

	Consolidated	
	2018	2017
	\$'000	\$'000
Trade payables	680	1,261
Accrued expenses	-	1
	<hr/>	<hr/>
	<u>680</u>	<u>1,262</u>

Refer to Note 18 to the financial statements for further information on financial risk management objectives and policies.

Trade payables and other creditors are non-interest bearing and are normally settled on 30-day terms.

Note 13. Equity – issued capital

	Consolidated			
	2018	2017	2018	2017
	Shares	Shares	\$'000	\$'000
Ordinary shares – fully paid (net of transaction cost)	<u>648,044,131</u>	<u>588,687,267</u>	<u>117,850</u>	<u>108,452</u>

Movements in ordinary share capital

Details	Date	Shares	\$'000
Balance	January 1, 2017	511,218,639	93,965
Shares issued - Equity Incentive Plan	June 29, 2017	683,333	-
Shares issued - Placement	October 5, 2017	76,785,295	15,357
Transaction costs		-	(870)
		<hr/>	<hr/>
Balance	December 31, 2017	588,687,267	108,452
Shares issued - Equity Incentive Plan	April 19, 2018	200,000	-
Shares issued - Placement	June 27, 2018	58,823,530	10,000
Share issued - Equity Incentive Plan	June 27, 2018	333,334	-
Transaction costs		-	(602)
		<hr/>	<hr/>
Balance	December 31, 2018	<u>648,044,131</u>	<u>117,850</u>

Ordinary shares

Notes to the Financial Statements

continued

Ordinary shares entitle the holder to participate in dividends and the proceeds on the winding up of the Company in proportion to the number of and amounts paid on the shares held. The fully paid ordinary shares have no par value and the Company does not have a limited amount of authorised capital.

On a show of hands, every member present at a meeting in person or by proxy shall have one vote and upon a poll, each share shall have one vote.

Share buy-back

There is no current on-market share buy-back.

Capital risk management

Xanadu's objectives when managing capital is to safeguard its ability to continue as a going concern, so that it can provide returns for shareholders and benefits for other stakeholders and to maintain an optimum capital structure to reduce the cost of capital.

Capital is regarded as total equity, as recognised in the Statement of Financial Position, plus net debt. Net debt is calculated as total borrowings less cash and cash equivalents.

Management effectively manages Xanadu's capital by assessing the Company's financial risks and adjusting its capital structure in response to changes in these risks and in the market. These responses include the management of expenditure and debt levels, distributions to shareholders and share and option issues.

The capital risk management policy remains unchanged from the Annual Report 2017.

Note 14. Equity - reserves

	Consolidated	
	2018	2017
	\$'000	\$'000
Foreign currency reserve	(9,695)	(11,047)
Share-based payments reserve	10,231	8,534
Transactions with owner's reserve	(537)	-
	<u>(1)</u>	<u>(2,513)</u>

Share-based payments

This reserve is used to record the value of equity benefits provided to directors and employees as part of their fees and remuneration, and external service providers for goods and services provided (including acquisition of tenements).

Foreign currency translation reserve

This reserve is used to accumulate the changes in the value investments in subsidiaries that arise from changes in the exchange rates.

Movements in reserves

Movements in each class of reserve during the current and previous financial period are set out below:

Consolidated	Share-based payments \$'000	Foreign currency \$'000	Transactions with owners \$'000	Total \$'000
Balance at January 1, 2017	8,208	(8,727)	-	(519)
Share based payment - employee benefits	326	-	-	326
Foreign currency translation	-	(2,320)	-	(2,320)
Balance at December 31, 2017	8,534	(11,047)	-	(2,513)
Share-based payments - employee benefits	1,697	-	-	1,697
Foreign currency translation	-	815	-	815
Other	-	537	(537)	-
Balance at December 31, 2018	<u>10,231</u>	<u>(9,695)</u>	<u>(537)</u>	<u>(1)</u>

Notes to the Financial Statements

continued

Note 15. Equity - accumulated losses

	Consolidated	
	2018	2017
	\$'000	\$'000
Accumulated losses at the beginning of the financial period	(65,164)	(61,322)
Loss after income tax expense for the period	(6,181)	(3,842)
Accumulated losses at the end of the financial period	<u>(71,345)</u>	<u>(65,164)</u>

Note 16. Equity - non-controlling interest

	Consolidated	
	2018	2017
	\$'000	\$'000
Non-controlling interest	<u>4,758</u>	<u>5,017</u>

Note 17. Equity – dividends

There were no dividends paid, recommended or declared during the current or previous financial period.

Note 18. Financial risk management objectives and policies

Financial risk management

Xanadu's principal financial instruments comprise cash, short-term deposits, receivables, payables and loans. The main purpose of these financial instruments is to raise finance for its operations. The consolidated entity has financial instruments such as debtors and creditors, which arise directly from its operations.

The Company manages its exposure to key financial risks in accordance with its Risk Management Policy with the objective to ensure that the financial risks inherent in exploration activities are identified and managed accordingly.

The main financial risks that arise in the normal course of business Xanadu's financial instruments are foreign currency risk, interest rate risk, credit risk, liquidity risk and commodity risk. Management employs different methods to measure and mitigate the different risks to which the Company is exposed. These include monitoring exposure to foreign exchange risk and assessments of market forecast for interest rate, foreign exchange and commodity prices. Liquidity risk is managed by development of rolling budgets and forecasts.

Primary responsibility for identification and control of financial risks lies with the Managing Director and Chief Executive Officer, and the Chief Financial Officer, under the authority of the Board. The Board is abreast of these risks and agrees any policies that may be implemented to manage the risks identified.

Market risk

Foreign currency risk

The Company is exposed to foreign exchange fluctuations with respect to A\$, US\$, MNT, and C\$. The Company's financial results are reported in A\$. Salaries for certain local employees in Mongolia may be paid in MNT. The Company's operations are in Mongolia and some of its payment commitments and exploration expenditures under the various agreements governing its rights are denominated in MNT and US\$. As a result, the Company's financial position and results are impacted by the exchange rate fluctuations among A\$, US\$, MNT and C\$. Such fluctuations may materially affect the Company's financial position and results.

Xanadu's currency risk to US\$ foreign denominated financial assets and liabilities at the end of the reporting period, expressed in Australian Dollars, was as follows:

	Assets	
	2018	2017
	\$'000	\$'000
Cash and cash equivalents	<u>524</u>	<u>6,883</u>

Notes to the Financial Statements

continued

The following sensitivity is based on the foreign currency risk exposures in existence at the balance date:

Consolidated – 2018	A\$ strengthened			A\$ weakened		
	% change	Effect on profit before tax	Effect on equity	% change	Effect on profit before tax	Effect on equity
A\$/US\$	10%	<u>52</u>	<u>52</u>	(10%)	<u>(52)</u>	<u>(52)</u>

Consolidated – 2017	A\$ strengthened			A\$ weakened		
	% change	Effect on profit before tax	Effect on equity	% change	Effect on profit before tax	Effect on equity
A\$/US\$	10%	<u>688</u>	<u>688</u>	(10%)	<u>(625)</u>	<u>(688)</u>

Management believe the balance date risk exposures are representative of the risk exposure inherent in the financial instruments.

Interest rate risk

The Company's exposure to market risk for changes in interest rates relates primarily to its cash held in variable interest accounts.

As at the reporting date, Xanadu had the following cash and cash equivalents and variable rate borrowings outstanding:

Consolidated	2018		2017	
	Weighted average interest rate %	Balance \$'000	Weighted average interest rate %	Balance \$'000
Cash and cash equivalents	2.40%	<u>5,225</u>	2.40%	<u>9,065</u>
Net exposure to cash flow interest rate risk		<u>5,225</u>		<u>9,065</u>

The following sensitivity is based on the interest rate risk exposures in existence at the balance date:

Consolidated - 2018	Basis points increase			Basis points decrease		
	Basis points change	Effect on profit before tax	Effect on equity	Basis points change	Effect on profit before tax	Effect on equity
Net interest rate risk exposure	100	<u>52</u>	<u>52</u>	(100)	<u>(52)</u>	<u>(52)</u>

Consolidated - 2017	Basis points increase			Basis points decrease		
	Basis points change	Effect on profit before tax	Effect on equity	Basis points change	Effect on profit before tax	Effect on equity
Net interest rate risk exposure	100	<u>90</u>	<u>90</u>	(100)	<u>(90)</u>	<u>(90)</u>

The movements in post-tax profit are due to the movements in interest amounts from higher cash balances held that balance date in comparison to the prior period.

Credit risk

Xanadu has adopted a lifetime expected loss allowance in estimating expected credit losses to trade receivables through the use of a provisions matrix using fixed rates of credit loss provisioning. These provisions are considered representative across all customers of Xanadu based on recent sales experience, historical collection rates and forward-looking information that is available.

Generally, trade receivables are written off when there is no reasonable expectation of recovery. Indicators of this include the failure of a debtor to engage in a repayment plan, no active enforcement activity and a failure to make contractual payments for a period greater than one year.

Notes to the Financial Statements

continued

Credit risk arises from the financial assets of the Company, which comprise cash and cash equivalents, and other receivables. Xanadu's exposure to credit risk arises from potential default of the counter party, with a maximum exposure equal to the carrying amount of these instruments.

The Company trades only with recognised, creditworthy third parties, and as such collateral is not requested nor is it Xanadu's policy to securitise its trade and other receivables.

In addition, receivable balances are monitored on an ongoing basis with the result that Xanadu's exposure to bad debts is not significant.

Liquidity risk

Liquidity risk arises from Xanadu's management of working capital. It is the risk that the Company will encounter difficulty in meeting its financial obligations as they fall due.

Xanadu's policy is to ensure that it will always have sufficient cash to allow it to meet its liabilities when they become due. To achieve this aim, it seeks to maintain cash balances to meet expected requirements for a period of at least 12 months.

The Board receives cash flow projections on a monthly basis as well as information regarding cash balances. At the balance sheet date, these projections indicated that Xanadu expected to have sufficient liquid resources to meet its obligations, and forward expenditure commitments, under all reasonably expected circumstances.

Commodity price risk

Even if commercial quantities of mineral deposits are discovered, there is no guarantee that a profitable market will exist for the sale of the metals produced. Factors beyond the control of the Company may affect the marketability of any minerals discovered. The prices of various metals have experienced significant movement over short periods of time, and are affected by numerous factors beyond the control of the Company, including, among other things, international economic and political trends, expectations of inflation, currency exchange fluctuations, interest rates and global or regional consumption patterns, speculative activities and increased production due to improved mining and production methods. The Company is particularly exposed to the risk of movement in the price of copper and gold.

Other business risks

The other business risks including political and legal risks, license risks, mineral resource assumption risks, environmental risks, operational risks and contractual risks are detailed in the Management's Discussion and Analysis.

Fair value

Unless otherwise stated, the carrying amounts of financial instruments reflect their fair value.

Note 19. Fair value measurement

Fair value hierarchy

The following tables detail Xanadu's assets and liabilities, measured or disclosed at fair value, using a three-level hierarchy, based on the lowest level of input that is significant to the entire fair value measurement, being:

Level 1: Quoted prices (unadjusted) in active markets for identical assets or liabilities that the entity can access at the measurement date;

Level 2: Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly; and

Level 3: Unobservable inputs for the asset or liability.

	Level 1 \$'000	Level 2 \$'000	Level 3 \$'000	Total \$'000
Consolidated - 2018				
<i>Assets</i>				
Ordinary shares - Aspire Mining Limited (ASX:AKM)	190	-	-	190
Total assets	190	-	-	190
Consolidated - 2017				
	Level 1 \$'000	Level 2 \$'000	Level 3 \$'000	Total \$'000

Notes to the Financial Statements

continued

Assets				
Ordinary shares - Aspire Mining Limited (ASX:AKM)	100	-	-	100
Total assets	100	-	-	100

There were no transfers between levels during the financial period.

Note 20. Key management personnel disclosures

Directors

The following individuals were directors of Xanadu during the financial period:

Kevin Tomlinson	Independent Non-Executive Chairman
Andrew Stewart	Managing Director and Chief Executive Officer
Ganbayar Lkhagvasuren	Executive Director
Hannah Badenach	Non-Executive Director
Marcus Engelbrecht	Non-Executive Director
Darryl Clark	Independent Non-Executive Director
Michele Muscillo	Independent Non-Executive Director

Other key management personnel

The following persons also had the authority and responsibility for planning, directing and controlling the major activities of Xanadu, directly or indirectly, during the financial period:

Munkhsaikhan Dambiinyam	Chief Financial Officer
Mathew Brown	Chief Geologist

Compensation

The aggregate compensation made to directors and other members of key management personnel of Xanadu is set out below:

	Consolidated	
	2018	2017
	\$	\$
Short-term employee benefits	1,686,574	1,482,036
Post-employment benefits	6,188	10,619
Share-based payments	1,697,233	325,841
	<u>3,369,995</u>	<u>1,818,496</u>

Note 21. Remuneration of auditors

During the financial period the following fees were paid or payable for services provided by Ernst & Young, the auditor of the Company:

	Consolidated	
	2018	2017
	\$	\$
<i>Audit services - Ernst & Young</i>		
Audit or review of the financial statements - Australia	118,284	80,374
Audit or review of the financial statements - Singapore	-	3,743
<i>Other services - Ernst & Young</i>		
Tax services	1,500	1,200
TSX prospectus reviews	85,660	-
	<u>205,444</u>	<u>85,317</u>

Note 22. Contingent liabilities

There are no material contingent liabilities relating to the Company.

Notes to the Financial Statements

continued

Note 23. Commitments

Commitments in relation to exploration licences contracted at the reporting date, including regulatory charges such as license fees, but not recognised as liabilities within one year are \$0.7 million (December 31, 2017: \$0.7 million). As the future exploration activity is in most cases dependent upon reserves being found, it is not possible to set out the funds due to be contributed in more than one year's time. No other commitments or contingencies existed at December 31, 2018.

Note 24. Related party transactions

Parent entity

Xanadu Mines Ltd is the parent entity.

Subsidiaries

Interests in subsidiaries are set out in Note 26 to the financial statements.

Key management personnel

Disclosures relating to key management personnel are set out in Note 20 to the financial statements and the Remuneration Report included in the Directors' Report.

Transactions with related parties

On January 2, 2017, the Company relocated its Ulaanbaatar office and entered into a rental agreement with Mr Ganbayar Lkhagvasuren, an Executive Director of the Company. The transaction between these related parties is on normal commercial terms and conditions no more favourable than those available to other parties that are arm's length. The Company paid rental totalling \$89,438 (December 31, 2017: \$88,428) for the year ended December 31, 2018.

Receivable from and payable to related parties

There were no trade receivables from or trade payables to related parties at the current and previous reporting date.

Loans to/from related parties

There were no loans to or from related parties as at December 31, 2018.

Terms and conditions

All transactions were made on normal commercial terms and conditions and at market rates.

Note 25. Parent entity information

Set out below is the supplementary information about the parent entity.

Statement of profit or loss and other comprehensive income

	Parent	
	2018	2017
	\$'000	\$'000
Loss after income tax	(4,288)	(2,507)
Total comprehensive income	(4,288)	(2,507)

Statement of financial position

	Parent	
	2018	2017
	\$'000	\$'000
Total current assets	5,325	8,754
Total assets	51,356	45,886
Total current liabilities	94	94
Total liabilities	94	94

Notes to the Financial Statements

continued

Equity		
Issued capital	117,850	108,452
Share-based payments reserve	10,655	8,534
Other reserves	256	256
Accumulated losses	(77,499)	(71,450)
Total equity	51,262	45,792

Contingent liabilities

The parent entity had no contingent liabilities as at December 31, 2018.

Capital commitments - Property, plant and equipment

The parent entity had no capital commitments for property, plant and equipment at as December 31, 2018.

Significant accounting policies

The accounting policies of Xanadu are consistent with those of the Company's subsidiaries, as disclosed in Note 1 to the financial statements, except for the following:

- Investments in subsidiaries are accounted for at cost, less any impairment, in the parent entity;
- Investments in associates are accounted for at cost, less any impairment, in the parent entity; and
- Dividends received from subsidiaries are recognised as other income by the parent entity and its receipt may be an indicator of an impairment of the investment.

Note 26. Interests in subsidiaries

The consolidated financial statements incorporate the assets, liabilities and results of the following subsidiaries in accordance with the accounting policy described in Note 1 to the financial statements:

Name	Principal place of business / Country of incorporation	Ownership interest	
		2018 %	2017 %
Xanadu Exploration Mongolia LLC	Mongolia	100.00%	100.00%
Xanadu Metals Mongolia LLC	Mongolia	100.00%	100.00%
Xanadu Copper Mongolia LLC	Mongolia	100.00%	100.00%
Xanadu Mines Singapore Pte Ltd	Singapore	100.00%	100.00%
Khuiten Metals Pte Ltd	Singapore	100.00%	100.00%
Mongol Metals LLC	Mongolia	85.00%	85.00%
Vantage LLC	Mongolia	90.00%	90.00%
Oyut Ulaan LLC	Mongolia	90.00%	90.00%

Note 27. Events after the reporting period

On January 14, 2019, 35,000,000 options, issued pursuant to the Red Mountain project acquisition terms, expired. The vesting of 15,000,000 Series A Options was contingent on recognition of a JORC resource of at least 300,000 tonnes contained copper equivalent and the vesting of 20,000,000 Series B Options was contingent on the recognition of a JORC resource of at least 900,000 tonnes contained copper equivalent.

No matter or circumstance has arisen since December 31, 2018 that has significantly affected, or may significantly affect Xanadu's operations, the results of those operations, or the Company's state of affairs in future financial years.

Note 28. Reconciliation of loss after income tax to net cash used in operating activities

	Consolidated	
	2018 \$'000	2017 \$'000
Loss after income tax expense for the period	(6,327)	(3,831)
Adjustments for:		
Depreciation and amortisation	81	91

Notes to the Financial Statements

continued

Net fair value loss/(gain) on financial assets	(90)	30
Share-based payments	1,697	326
Foreign exchange differences	(1)	1
Net loss on sale of plant and equipment	-	29
Deferred consideration received on sale of interest in tenement	-	(130)
<i>Change in operating assets and liabilities:</i>		
Decrease in trade and other receivables	105	13
Increase in trade and other payables	15	100
Net cash used in operating activities	<u>(4,520)</u>	<u>(3,371)</u>

Note 29. Earnings per share

	<u>Consolidated</u>	
	2018	2017
	\$'000	\$'000
Loss after income tax	(6,327)	(3,831)
Non-controlling interest	146	(11)
Loss after income tax attributable to the owners of Xanadu Mines Ltd	<u>(6,181)</u>	<u>(3,842)</u>
	<u>Number</u>	<u>Number</u>
Weighted average number of ordinary shares used in calculating basic earnings per share	619,297,926	530,079,477
Weighted average number of ordinary shares used in calculating diluted earnings per share	<u>619,297,926</u>	<u>530,079,477</u>
	<u>Cents</u>	<u>Cents</u>
Basic earnings per share	(1.00)	(0.72)
Diluted earnings per share	(1.00)	(0.72)

Note 30. Share-based payments

The Xanadu Equity Incentive Plan ("Plan") was approved by shareholders at the Company's 2013 Annual Greeting Meeting. Under the Plan, the Board may grant options and share rights over ordinary shares in the Company to certain key management personnel of the Company and its subsidiaries. The share rights are issued for nil consideration and are granted in accordance with performance guidelines established by the Board. No options have been granted under this Plan during the current financial year.

The vesting of awards under the Plan is subject to attainment of performance conditions as described in the Plan. No performance conditions as per the plan have yet been met hence no options are available to be exercised yet.

December 31, 2018

Grant date	Expiry date	Exercise price	Balance at the start of the period	Granted	Vested and awarded	Expired/ forfeited/ other	Balance at the end of the period
23/12/2015	16/06/2018	\$0.00	333,334	-	(333,334)	-	-
26/07/2017	26/07/2019	\$0.00	4,000,000	-	-	-	4,000,000
16/11/2017	26/05/2019	\$0.00	10,000,000	-	-	-	10,000,000
16/11/2017	26/07/2019	\$0.00	4,000,000	-	-	-	4,000,000
16/11/2017	11/10/2019	\$0.00	2,000,000	-	-	-	2,000,000
			<u>20,333,334</u>	<u>-</u>	<u>(333,334)</u>	<u>-</u>	<u>20,000,000</u>

December 31, 2017

Grant date	Expiry date	Exercise price	Balance at the start of the period	Granted	Vested and awarded	Expired/ forfeited/ other	Balance at the end of the period
28/11/2014	18/09/2017	\$0.00	1,000,000	-	-	(1,000,000)	-
01/12/2014	01/06/2017	\$0.00	350,000	-	(350,000)	-	-

Notes to the Financial Statements

continued

23/12/2015	16/06/2018	\$0.00	666,667	-	(333,333)	-	333,334
23/12/2016	23/12/2019	\$0.00	1,800,000	-	-	(1,800,000)	-
26/07/2017	26/07/2019	\$0.00	-	4,000,000	-	-	4,000,000
16/11/2017	26/05/2019	\$0.00	-	10,000,000	-	-	10,000,000
16/11/2017	26/07/2019	\$0.00	-	4,000,000	-	-	4,000,000
16/11/2017	11/10/2019	\$0.00	-	2,000,000	-	-	2,000,000
			3,816,667	20,000,000	(683,333)	(2,800,000)	20,333,334

Should the KMP remain employed with Xanadu at the date of vesting, the share rights will vest where the closing price or share price of Xanadu shares (as the case may be depending on the terms of issue) on consecutive trading days during the period exceeds the hurdle price. If hurdle price is not met, share rights get accumulated to a future vesting date until the expiry date where all unvested share rights lapse. Vesting conditions are as follows:

- 4,000,000 share rights which may vest on July 26, 2018 if the volume weighted average price for 45 consecutive days in the prior 12-month period exceeds \$0.40 (“Tranche 1 Rights Vesting Condition”). The Tier 1 Rights Vesting Condition was not satisfied and in accordance with their terms, will be subject to the Tranche 2 Rights Vesting Condition.
- 5,000,000 share rights which may vest on May 26, 2018 if the volume weighted average price for 45 consecutive days in the prior 12-month period exceeds \$0.40 (“Tranche 1 Rights Vesting Condition”). The Tier 1 Rights Vesting Condition was not satisfied and in accordance with their terms, will be subject to the Tranche 2 Rights Vesting Condition.
- 1,000,000 share rights which may vest on October 11, 2018 if the volume weighted average price for 45 consecutive days in the prior 12-month period exceeds \$0.40 (“Tranche 1 Rights Vesting Condition”). The Tier 1 Rights vesting condition was not satisfied and in accordance with their terms, will be subject to the Tranche 2 Rights Vesting Condition.
- 4,000,000 share rights which may vest on July 26, 2019 if the volume weighted average price for 45 consecutive days in the prior 12-month period exceeds \$0.60 (“Tranche 2 Rights Vesting Condition”).
- 5,000,000 share rights which may vest on May 26, 2019 if the volume weighted average price for 45 consecutive days in the prior 12-month period exceeds \$0.60 (“Tranche 2 Rights Vesting Condition”).
- 1,000,000 share rights which may vest on October 11, 2018 if the volume weighted average price for 45 consecutive days in the prior 12-month period exceeds \$0.60 (“Tranche 2 Rights Vesting Condition”).

Share-based payments expense increased due to the Plan awards granted to the Key Management Personnel in 2017. Share-based payments is measured by reference to the fair value at the date at which they are granted. The fair value of the options is determined by an independent written valuation. Share-based payments expense is amortised over the vesting period. No expense is recognised for awards that do not ultimately vest, except for awards where vesting is only conditional upon a market condition.

Directors' Declaration

In the directors' opinion:

- the attached financial statements and notes comply with the Corporations Act 2001, the Accounting Standards, the Corporations Regulations 2001 and other mandatory professional reporting requirements;
- the attached financial statements and notes comply with International Financial Reporting Standards as issued by the International Accounting Standards Board as described in note 1 to the financial statements;
- the attached financial statements and notes give a true and fair view of Xanadu's financial position as at December 31, 2018 and of its performance for the financial period ended on that date; and
- there are reasonable grounds to believe that the Company will be able to pay its debts as and when they become due and payable.

The directors have been given the declarations required by section 295A of the Corporations Act 2001.

Signed in accordance with a resolution of directors made pursuant to section 295(5)(a) of the Corporations Act 2001.

On behalf of the Directors



Kevin Tomlinson

Non-Executive Chairman

March 15, 2019

Independent Auditor's Report to the Members of Xanadu Mines Ltd



Ernst & Young
200 George Street
Sydney NSW 2000 Australia
GPO Box 2646 Sydney NSW 2001

Tel: +61 2 9248 5555
Fax: +61 2 9248 5959
ey.com/au

Independent Auditor's Report to the Members of Xanadu Mines Limited

Report on the Audit of the Financial Report

Opinion

We have audited the financial report of Xanadu Mines Limited (the Company) and its subsidiaries (collectively the Group), which comprises the consolidated statement of financial position as at 31 December 2018, the consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the year then ended, notes to the financial statements, including a summary of significant accounting policies, and the directors' declaration.

In our opinion, the accompanying financial report of the Group is in accordance with the *Corporations Act 2001*, including:

- a) giving a true and fair view of the consolidated financial position of the Group as at 31 December 2018 and of its consolidated financial performance for the year ended on that date; and
- b) complying with Australian Accounting Standards and the *Corporations Regulations 2001*.

Basis for Opinion

We conducted our audit in accordance with Australian Auditing Standards. Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Report* section of our report. We are independent of the Group in accordance with the auditor independence requirements of the *Corporations Act 2001* and the ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants* (the Code) that are relevant to our audit of the financial report in Australia. We have also fulfilled our other ethical responsibilities in accordance with the Code.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Key Audit Matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial report of the current year. These matters were addressed in the context of our audit of the financial report as a whole, and in forming our opinion thereon, but we do not provide a separate opinion on these matters. For each matter below, our description of how our audit addressed the matter is provided in that context.

We have fulfilled the responsibilities described in the *Auditor's Responsibilities for the Audit of the Financial Report* section of our report, including in relation to these matters. Accordingly, our audit included the performance of procedures designed to respond to our assessment of the risks of material misstatement of the financial report. The results of our audit procedures, including the procedures performed to address the matters below, provide the basis for our audit opinion on the accompanying financial report.

A member firm of Ernst & Young Global Limited
Liability limited by a scheme approved under Professional Standards Legislation



Carrying value of capitalised exploration and evaluation expenditure

Why significant

Capitalised exploration and evaluation assets are the Group's largest asset. The carrying value of exploration and evaluation assets is impacted by Xanadu Mines Limited's ability, and intention, to continue to explore their exploration assets. The results of exploration work also determines to what extent the mineral reserves and resources may or may not be commercially viable for extraction. Due to the quantum of this asset and the subjectivity involved in determining its carrying value, this is a key audit matter.

Refer to Note 11 - Exploration and evaluation assets to the financial statements for the amounts held on the Balance sheet by the Group as at 31 December 2018 and related disclosure.

How our audit addressed the key audit matter

Our procedures to address the Group's assessment of the carrying value of exploration and evaluation assets included:

- ▶ considered the Company's right to explore in the relevant exploration area which included obtaining and assessing relevant documentation such as license agreements;
- ▶ considered the Group's intention to carry out significant exploration and evaluation activity in the relevant exploration area which included assessment of the Group's cash-flow forecast models, discussions with senior management and Directors as to the intentions and strategy of the Group;
- ▶ assessed the commercial viability of results relating to exploration and evaluation activities carried out in the relevant licensed area; and
- ▶ assessed the ability to finance any planned future exploration and evaluation activity.

Information Other than the Financial Report and Auditor's Report Thereon

The directors are responsible for the other information. The other information comprises the information included in the Company's 2018 Annual Report other than the financial report and our auditor's report thereon. We obtained the Directors' Report that is to be included in the Annual Report, prior to the date of this auditor's report, and we expect to obtain the remaining sections of the Annual Report after the date of this auditor's report.

Our opinion on the financial report does not cover the other information and we do not and will not express any form of assurance conclusion thereon, with the exception of the Remuneration Report and our related assurance opinion.

In connection with our audit of the financial report, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial report or our knowledge obtained in the audit or otherwise appears to be materially misstated.

If, based on the work we have performed on the other information obtained prior to the date of this auditor's report, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.



Responsibilities of the Directors for the Financial Report

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

In preparing the financial report, the directors are responsible for assessing the Group's ability to continue as a going concern, disclosing, as applicable, matters relating to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the Group or to cease operations, or have no realistic alternative but to do so.

Auditor's Responsibilities for the Audit of the Financial Report

Our objectives are to obtain reasonable assurance about whether the financial report as a whole is free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with the Australian Auditing Standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of this financial report.

As part of an audit in accordance with the Australian Auditing Standards, we exercise professional judgment and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial report, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the directors.
- Conclude on the appropriateness of the directors' use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial report or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial report, including the disclosures, and whether the financial report represents the underlying transactions and events in a manner that achieves fair presentation.

Independent Auditor's Report to the Members of Xanadu Mines Ltd



- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the financial report. We are responsible for the direction, supervision and performance of the Group audit. We remain solely responsible for our audit opinion.

We communicate with the directors regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide the directors with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated to the directors, we determine those matters that were of most significance in the audit of the financial report of the current year and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

Report on the Audit of the Remuneration Report

Opinion on the Remuneration Report

We have audited the Remuneration Report included in pages 21 to 24 of the directors' report for the year ended 31 December 2018.

In our opinion, the Remuneration Report of Xanadu Mines Limited for the year ended 31 December 2018, complies with section 300A of the *Corporations Act 2001*.

Responsibilities

The directors of the Company are responsible for the preparation and presentation of the Remuneration Report in accordance with section 300A of the *Corporations Act 2001*. Our responsibility is to express an opinion on the Remuneration Report, based on our audit conducted in accordance with Australian Auditing Standards.

Ernst & Young

Scott Jarrett
Partner Sydney
15 March 2019

ASX Additional Information

Additional information required by the Australian Securities Exchange Limited (ASX) Listing Rules and not disclosed elsewhere in the Report is set out below. The information is current as at 4 March 2019.

(a) Substantial shareholders

The number of securities held by substantial shareholders and their associates, as disclosed to Xanadu and ASX are set out below:

	Fully Paid Ordinary Shares	
	Number of Shares	Percentage of Shares
CAAF Limited	154,718,956	23.87% ¹
Copper Plate Success Limited	154,718,956	23.87% ¹
Bank of Nova Scotia and 1832 Asset Management L.P.	31,639,1340	4.88% ²
Noble Resources International Pte. Ltd.	51,800,860	7.99% ³
Fast Lane Australia Pty Ltd	30,600,000	5.73% ⁴

¹ As notified to Xanadu on 5 July 2018. CAAF Limited and Copper Plate Success Limited are associates as defined in the Corporations Act 2001 (Cth).

² As notified to Xanadu on 4 December 2018.

³ As notified to Xanadu on 24 December 2018.

⁴ As notified to Xanadu on 5 January 2016.

(b) Number of security holders and securities on issue

Quoted securities

Xanadu has on issue 648,044,131 fully paid ordinary shares held by 1,181 shareholders.

Unquoted securities

Share rights

Xanadu has on issue 20,000,000 unquoted share rights ('Rights') with various vesting prices held by seven Rights holders. For the purposes of ASX Listing Rule 4.10.7, seven rights holder holds more than 100,001 rights.

Options

Xanadu has on issue 29,411,759 unquoted options with an exercise price of \$0.25 held by 35 option holders.

For the purposes of ASX Listing Rule 4.10.7, 25 option holders holds more than 100,001 options.

(c) Voting rights

Ordinary shares

The voting rights attached to ordinary shares are that on a show of hands, every member present, in person or proxy, has one vote and upon a poll, each share shall have one vote.

Share rights

Share rights holders do not have any voting rights on the share rights held by them.

Options

Option holders do not have any voting rights on the options held by them.

ASX Additional Information

(d) Distribution of security holders

	Fully paid ordinary shares		
	Number of Holders	Number of Shares	Percentage of Shares
1 - 1,000	46	10,944	0%
1,001 - 5,000	170	575,982	0.09%
5,001 - 10,000	164	1,389,557	0.21%
10,001 - 100,000	521	22,057,303	3.41%
100,001 and over	280	624,010,345	96.29%
	1,181	648,044,131	100.00%

(e) Unmarketable parcel of shares

The number of shareholders holding less than a marketable parcel of ordinary shares is 118. 5,000 shares comprise a marketable parcel at Xanadu's closing share price of \$0.145 on 4 March 2019.

(f) Twenty largest shareholders of quoted equity securities

	Fully paid ordinary shares	
	Number of Shares	Percentage of Shares
1. HSBC CUSTODY NOMINEES (AUSTRALIA) LIMITED	140,331,532	21.65
2. ASIA CAPITAL AND ADVISORS PTE LTD <COPPER PLATE SUCCESS LTD A/C>	66,756,241	10.30
3. NOBLE RESOURCES INTERNATIONAL PTE LTD	51,800,860	7.99
4. CITICORP NOMINEES PTY LTD	34,451,491	5.32
5. FAST LANE AUSTRALIA PTY LTD	30,000,000	4.63
6. SAKARI ENERGY TRADING PTE LTD	24,642,332	3.80
7. MR PAUL DAVID NEATE	18,758,119	2.89
8. CM SUPER FUND PTY LTD <CAROL MCCOLL SUPER FUND A/C>	17,000,000	2.62
9. MR GANBAYAR LKHAGVASUREN	16,558,329	2.56
10. BNP PARIBAS NOMINEES PTY LTD <AGENCY LENDING DRP A/C>	13,372,727	2.06
11. BELL POTTER NOMINEES PTY LTD <BB NOMINEES A/C>	11,369,431	1.75
12. BNP PARIBAS NOMINEES PTY LTD <IB AU NOMS RETAILCLIENT DRP>	8,732,865	1.35
13. BELLARINE GOLD PTY LTD <RIBBLESDALE SUPER FUND A/C>	8,007,788	1.24
14. TWYNAM AGRICULTURAL GROUP PTY LTD	7,299,437	1.13
15. ROJO NERO CAPITAL PTY LTD	6,819,758	1.05
16. FARRINGTON CORPORATE SERVICES PTY LTD <FARRINGTON SUPER FUND A/C>	6,098,100	0.94
17. J P MORGAN NOMINEES AUSTRALIA PTY LIMITED	5,802,072	0.90
18. BIKINI ATOLL INVESTMENTS PTY LTD	4,960,000	0.77
19. MR BRIAN MCCUBBING + MRS ADRIANA MCCUBBING <B MCCUBBING SUPER FUND A/C>	4,723,616	0.73
20. Mrs Jan Meek	4,411,144	0.68
	481,895,842	74.36%

(g) On market buy-back

There is no current on market buy-back of Xanadu shares.

(h) Tenements held as at 4 March 2018

Area of Interest	Tenements	Location	Interest
Kharmagtai	MV17387A	Omnogovi Province	76.5%
Red Mountain	MV017129	Dornogovi Province	90%
Yellow Mountain	13670x	Bulgan Province	100%