

**LYDIAN INTERNATIONAL LIMITED  
MANAGEMENT DISCUSSION AND ANALYSIS**

**March 31, 2012**

## MANAGEMENT DISCUSSION AND ANALYSIS

The following is Management's Discussion and Analysis ("MD&A") of the consolidated interim financial condition and results of operations of Lydian International Limited ("Lydian" or the "Company") for the three month period ended March 31, 2012. This discussion should be read in conjunction with the interim consolidated financial statements and the notes thereto for the three month period ended March 31, 2012, prepared in accordance with International Financial Reporting Standards ("IFRS"). The information provided herein supplements, but does not form part of, the consolidated financial statements. This discussion covers three month period to March 31, 2012 as well as the subsequent period up to the date of this MD&A, May 14, 2012. All monetary figures are expressed in British Pounds unless otherwise indicated.

### CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS

*This MD&A contains "forward-looking statements" that involve a number of risks and uncertainties. Forward-looking statements include, but are not limited to, statements with respect to the future price and the estimation of mineral reserves and resources, the realisation of mineral estimates, the timing and amount of estimated future production, costs of production, capital expenditures, costs and timing of the development of new deposits, success of exploration activities, permitting time lines, currency fluctuations, requirements for additional capital, government regulation of mining operations, environmental risks, unanticipated reclamation expenses, title disputes or claims, limitations on insurance coverage and timing and possible outcome of pending litigation.*

*Often, but not always, forward-looking statements can be identified by the use of words such as "plans", "expects", or "does not expect", "is expected", "budget", "scheduled", "estimates", "forecasts", "intends", "anticipates", or "does not anticipate", or "believes", or variations of such words and phrases or that state that certain actions, events or results "may", "could", "would", "might" or "will" be taken, occur or be achieved. Forward-looking statements are based on the opinions and estimates of management as of the date such statements are made and they involve known and unknown risks, uncertainties and other factors which may cause the actual results, performance or achievements of the Company to be materially different from any other future results, performance or achievements expressed or implied by the forward-looking statements. Such factors include, among others: the actual results of current exploration activities; actual results of current reclamation activities; conclusions of economic evaluations; changes in project parameters as plans continue to be refined; future prices of mineral resources; fluctuations in metal prices, as well as those risk factors discussed or referred to in this MD&A under the heading "Risk and Uncertainties" and other documents filed from time to time with the securities regulatory authorities in all provinces and territories of Canada and Jersey. Although the Company has attempted to identify important factors that could cause actual actions, events or results to differ materially from those described in forward-looking statements, there may be other factors that cause actions, events or results not to be anticipated, estimated or intended. There can be no assurance that forward-looking statements will prove to be accurate, as actual results and future events could differ materially from those anticipated in such statements. Such statements are based on a number of assumptions which may prove to be incorrect, including, but not limited to, assumptions about:*

- *general business and economic conditions;*

- *the supply and demand for, deliveries of, and the level and volatility of prices of gold;*
- *the timing of the receipt of regulatory and governmental approvals for the Company's projects;*
- *the availability of financing for the Company's development of its properties on reasonable terms;*
- *the ability to procure equipment and operating supplies in sufficient quantities and on a timely basis;*
- *the ability to attract and retain skilled staff;*
- *exploration timetables;*
- *planned production timetables;*
- *market competition; and*
- *the accuracy of the Company's resource estimate (including, with respect to size, grade and recoverability) and the geological, operational and price assumptions on which it is based.*

*The Company undertakes no obligation to update forward-looking statements if circumstances or management's estimates or opinions should change except as required by securities regulatory requirements. Accordingly, readers are cautioned not to place undue reliance on forward-looking statements.*

*Cautionary Note to United States Investors Concerning Estimates of Measured, Indicated and Inferred Resources: This MD&A uses the terms "Measured", "Indicated" and "Inferred" Resources. United States investors are advised that while such terms are recognised and required by Canadian regulations, the U.S. Securities and Exchange Commission ("SEC") does not recognise them. "Inferred Mineral Resources" have a great amount of uncertainty as to their existence and as to their economic and legal feasibility. It cannot be assumed that all or any part of an Inferred Mineral Resource will ever be upgraded to a higher category. Under Canadian rules, estimates of Inferred Mineral Resources may not form the basis of feasibility or other economic studies. United States investors are cautioned not to assume that all or any part of Measured or Indicated Mineral Resources will ever be converted into Mineral Reserves. United States investors are also cautioned not to assume that all or any part of an Inferred Mineral Resource exists, or is economically or legally mineable.*

## **BUSINESS OVERVIEW**

The Company is a gold-focused mineral exploration and development company specialising in emerging and transitional environments. Currently the Company is focused on Eastern Europe, primarily in the Caucasus region, exploring and developing precious metal assets. The Company's main project is a gold exploration and development project (the "Amulsar Project") located in Armenia. In addition, the Company holds a license covering an early-stage gold prospect (the "Zoti Project") in the Guria region of Georgia.

The Company's principal objective is to continue its exploration and development of the Amulsar Project. The Company will continue the ongoing exploration drilling and mine development program at the Amulsar Project and is conducting a bankable feasibility study, for which the financial numbers are expected to be completed around the end of the second quarter of 2012. The Company will also conduct detailed engineering studies to finalise mine design and complete the permitting process at Amulsar. Developing the Amulsar Project into a profitable gold mining operation will depend upon the Company's ability to raise sufficient project financing, acquire all permits and complete construction. The Company currently does not have any commercial operations or revenue. The Company expects that its current assets are sufficient to finance the Amulsar Project to and through the completion of the bankable feasibility study and the necessary detailed engineering stages, carry out the work recommended in the Technical Report (as defined below), continue exploration work on the

Zoti Project in Georgia and pay all amounts that become due on or prior to December 31, 2012 to Newmont Overseas Exploration Limited (“Newmont”) pursuant to the purchase agreement (the “Newmont Purchase Agreement”) dated February 26, 2010 between the Company and Newmont.

### **FIRST QUARTER AND RECENT HIGHLIGHTS**

- The Company completed a bought deal equity financing, pursuant to which it issued 15,625,000 and 2,343,750 ordinary shares (the “Ordinary Shares”) of the Company on March 9, 2012 and March 15, 2012, respectively, at a purchase price of CAD \$2.56 per Ordinary Share, for aggregate gross proceeds to the Company of CAD \$46 million.
- On March 21, 2012, the Company announced that the European Bank of Reconstruction and Development (the “EBRD”) were to exercise their pre-emptive rights in full with respect to the bought deal above by purchasing an aggregate of 1,419,732 Ordinary Shares (the “New Shares”) at a purchase price per Ordinary Share of CAD \$2.56 for an aggregate purchase price of CAD \$3,634,514.
- On March 13, 2012 the Company announced that it received its environmental approval for the processing of gold-silver ore using heap leach technology as part of the permitting process at its Amulsar Project in Armenia.
- On March 9, 2012, the Company filed a technical report (the “Technical Report”) titled “2012 Mineral Resource Estimate Amulsar Gold Project NI 43-101 Technical Report” prepared by Independent Mining Consultants, Inc., dated March 3, 2012, in respect of an updated resource estimate for its Amulsar Project announced by the Company on January 23, 2012 (see below).
- On March 5, 2012, the Company announced the appointment of Mr. Tim Richards as Senior Mine Manager to oversee the development of its Amulsar Project.
- On March 5, 2012, the Company announced the engagement of Endeavour Financial to provide financial advisory services with respect to financing the development of the Amulsar Project.
- On January 3, 2012, the Company announced that it notified Newmont of its deferral of payment of US \$5 million owing to Newmont until no later than December 31, 2012, which was then made in full together with interest (US \$100,000) owing thereon on March 13, 2012.

### **Recent Developments**

#### ***Update of Mineral Resource***

On March 9, 2012, the Company filed the Technical Report in respect of an updated mineral resource estimate for its Amulsar Project that was announced by the Company on January 23, 2012. The updated resource estimate comprises 68.2 Mt at 1.0 g/t Au (2.1 million ounces) of indicated category resources and 36.1 Mt at 0.9 g/t Au (1.1 million ounces) of inferred category resources (see Table 1), based on a 0.40 g/t gold cutoff grade.

The resource estimate in the Technical Report and summarised below updates the resource estimate contained in the preliminary economic assessment (the “PEA”) report on the Amulsar property titled “Development of Amulsar Heap Leach Facility, Preliminary Economic Assessment” dated August 12, 2011 and prepared by K D Engineering Company, Inc. (KDE). The resource estimate contained in the PEA does not include the results of any drilling since December 31, 2010.

The updated resource in the Technical Report was developed from approximately 39,000 meters of additional combined diamond and reverse circulation exploration drilling (for a total of approximately 90,000 meters) carried out in 2011. Gold at the Amulsar Project is

hosted primarily in sub-vertical faults, associated breccia veins and sheeted fractures with faults and breccia veins generally trending northwest-southeastwards and sheeted fracture zones trending northeast-southwestwards. Sub-horizontal possibly strata-bound mineralisation also controls some of the gold at the Amulsar Project.

The updated resource estimate comprised a total of 1.7 million ounces gold in the indicated category and 0.6 million ounces gold in inferred category (using a 0.4g/t cut-off) from the contiguous Tigranes and Artavasdes areas and 0.5 million ounces gold in the indicated category and 0.4 million ounces inferred category from the Erato prospect, which is located approximately 900 meters to the north-northwest of Tigranes&Artavasdes (see Table 2).

**Table 1 Gold-Silver Mineral Resource**

Gold Cutoff Grade, g/t	Indicated Mineral Resource					Inferred Mineral Resource				
	Tonnes (x 1000)	Gold, g/t	Silver, g/t	Ounces Gold	Ounces Silver	Tonnes (x 1000)	Gold, g/t	Silver, g/t	Ounces Gold	Ounces Silver
0.75	28,107	1.61	4.90	1,453,109	4,428,007	15,235	1.45	4.55	709,265	2,228,700
0.50	51,153	1.16	4.17	1,902,840	6,858,117	27,189	1.08	4.37	943,219	3,820,079
<b>0.40</b>	<b>68,207</b>	<b>0.98</b>	<b>3.84</b>	<b>2,146,888</b>	<b>8,420,888</b>	<b>36,056</b>	<b>0.92</b>	<b>4.00</b>	<b>1,069,983</b>	<b>4,636,980</b>
0.30	95,798	0.80	3.47	2,454,779	10,687,685	48,907	0.77	3.63	1,212,336	5,707,887
0.20	140,336	0.62	3.13	2,806,449	14,122,486	75,461	0.59	3.10	1,421,733	7,521,111

**Table 2 Amulsar Gold-Silver Mineral Resource by Project Area**

TIGRANES & ARTAVASDES AREAS										
Gold Cutoff Grade, g/t	Indicated Mineral Resource					Inferred Mineral Resource				
	Tonnes (x 1000)	Gold, g/t	Silver, g/t	Ounces Gold	Ounces Silver	Tonnes (x 1000)	Gold, g/t	Silver, g/t	Ounces Gold	Ounces Silver
0.75	21,409	1.61	5.29	1,108,893	3,641,244	8,204	1.31	5.44	344,482	1,434,902
0.50	39,749	1.15	4.48	1,465,843	5,725,349	16,808	0.95	4.85	512,838	2,620,930
<b>0.40</b>	<b>53,337</b>	<b>0.97</b>	<b>4.12</b>	<b>1,661,690</b>	<b>7,065,185</b>	<b>23,142</b>	<b>0.81</b>	<b>4.36</b>	<b>603,420</b>	<b>3,244,032</b>
0.30	73,478	0.80	3.76	1,885,202	8,882,657	32,771	0.67	3.92	710,145	4,130,223
0.20	105,303	0.63	3.44	2,136,327	11,646,540	48,790	0.53	3.55	836,095	5,568,739

ERATO PROSPECT										
Gold Cutoff Grade, g/t	Indicated Mineral Resource					Inferred Mineral Resource				
	Tonnes (x 1000)	Gold, g/t	Silver, g/t	Ounces Gold	Ounces Silver	Tonnes (x 1000)	Gold, g/t	Silver, g/t	Ounces Gold	Ounces Silver
0.75	6,698	1.60	3.64	344,558	783,870	7,030	1.62	3.51	365,027	793,341
0.50	11,403	1.19	3.08	436,645	1,129,191	10,380	1.29	3.59	430,178	1,198,090
<b>0.40</b>	<b>14,871</b>	<b>1.02</b>	<b>2.84</b>	<b>486,249</b>	<b>1,357,864</b>	<b>12,914</b>	<b>1.13</b>	<b>3.34</b>	<b>467,101</b>	<b>1,386,772</b>
0.30	22,320	0.79	2.52	568,352	1,808,391	16,136	0.97	3.06	502,710	1,587,505
0.20	35,032	0.60	2.18	670,162	2,455,382	26,671	0.68	2.28	584,819	1,955,113

This mineral resource estimate has been confined within a theoretical floating cone open pit geometry which ensures an extra level of confidence by precluding ounces that are unlikely to be mined. The floating cone parameters used a US\$1,300/oz gold price and current estimates of project operating costs and gold recovery. At the 0.40 g/t gold cutoff grade, 98% of the unconfined global gold ounce estimate lies within this theoretical open pit geometry, which the Company believes indicates the robustness of the mineral resource.

*Exploration Update and Activities*

### Amulsar Project

The Company's Amulsar Project area covers a region of high-sulphidation, epithermal-type gold mineralisation located in central Armenia and was discovered by Lydian in 2006. The exploration licences for the Amulsar Project are held 100% by Geoteam CJSC, an Armenian registered closed joint stock company. The outstanding shares of Geoteam are held 95% by Lydian Resources Armenia Ltd. (a 100% owned indirect subsidiary of the Company) and 5% by Lydian's local director. In December 2010, the Company acquired an option to purchase this minority interest. The Company has made all of the payments of cash and Ordinary Shares that were required to be made by it prior to the date of this MD&A in order to maintain the option.

On August 22, 2011, the Company filed the PEA in connection with the Amulsar Project on SEDAR. The PEA is based on the estimated resources (inferred and indicated) at only the Tigranes and Artavasdes areas (i.e. not including the Erato area) and shows a pre-tax Base Case Net Present Value using a 5% discount rate amounting to US \$515 million, with an IRR of 45%. The PEA was based on a US \$1,000 optimised pit-shell, 1.64m mineable ounces, US\$1,200 gold price, 85% recoveries and had a +30% contingency capital tolerance. The mineable ounces used in the PEA were the then resource numbers (inferred and indicated) that were contained in the optimized pit-shell.

In 2011, the Company completed approximately 39,000 meters of combined diamond and reverse circulation exploration drilling. Results indicate that the current resource shell may extend further in all directions. This further drilling resulted in the updated resource estimate summarised above. In addition, the Company identified further gold mineralisation one kilometre away towards the southwest at the Orontes prospect area. On November 15, 2011, the Company also reported metallurgical results from Amulsar showing average recoveries of 94% for Master Composite Samples obtained after only 47 days leaching.

The Company contracted KDE to conduct a bankable feasibility study (BFS) at the Amulsar Project. The study team comprises KDE (process design), Golder Associates (USA; leach pads and geotechnical work), Independent Mining Consultants (USA; resources and pits) and Wardell Armstrong International (UK; environment and social). The BFS is expected to be completed around the end of Q2 2012.

On March 12, 2012, the Company announced that as part of the permitting process for the development of its Amulsar project, it has received approval for the Company's planned processing of gold-silver using heap leach technology. The Company now requires environmental impact assessment approval for its expanded open-pit and waste dump facilities and land status change for the surface rights underlying the project infrastructure.

### Zoti Project

On October 11, 2011, the Company announced that its 100% own subsidiary Georgian Resource Company LLC acquired a 40 year combined exploration-mining license over a new gold project in Georgia known as the Zoti Project. The Company currently plans to carry out approximately 1,500 meters of exploratory drilling at the Zoti Project in 2012.

## **FINANCIAL RESULTS OF OPERATIONS SELECTED FINANCIAL INFORMATION**

The financial information has been prepared in accordance with International Financial Reporting Standards (IFRS). All monetary amount references in this document are to British Pounds unless otherwise indicated.

### Statement of Operations

The following is a summary of selected information for the three month period ended March 31, 2012 and comparative financial information for the corresponding period in the Company's previous financial period.

	Three months ended March 31,	
	2012	2011
	£	£
Interest income	19,501	14,050
Total expenses	(1,610,956)	(1,367,461)
Net loss	(1,591,455)	(1,353,411)
Loss per share (basic and diluted)	0.01	0.01

During the three month periods ended March 31, 2012 and 2011 the Company had no revenues. Its only income was bank interest. In the three month period ended March 31, 2012, the Company recorded a loss of £1,591,455 (1 pence per share) compared to £1,353,411 (1 pence per share) during the corresponding period in 2011. There were several increases in the Company's cost structure in 2012 compared to 2011, including an increase of: £216,731 of funds allocated to employee benefit reserves in respect of option vesting; £47,369 of administrative expenses, £47,369 of services and consumables.

During the three month period ended March 31, 2012, there were some fluctuations between the British Pound, Canadian Dollar, Euro, Armenian Dram, Georgian Lari and the US Dollar. This resulted in changes to the value of the Company's exploration assets as reported in British Pounds. Details of these changes are set out below. The Company attempts to protect itself from variations in exchange rates by holding its cash in currencies roughly in proportion to the Company's anticipated expenditures in those currencies.

### Income Tax Expense

There was no tax payable by the Company in the three month period ended March 31, 2012 and the same period in 2011. As at March 31, 2012, the Company had taxation losses of £6,163,532 (December 31, 2011; £5,986,965) that had not been recognised, as there is insufficient evidence of taxable profit in the near future.

### Summary of Operating Cash Flows, Investing and Financing Activities

The following table summarises the Company's cash flow for the three month period ended March 31, 2012 and comparative financial information for the corresponding interim periods in the Company's previous financial period.

	Three months ended March 31,	
	2012	2011
	£	£
Net cash used by operating activities	(2,573,384)	(1,338,475)
Net cash used by investing activities	(4,083,118)	(461,095)

Net cash provided by financing activities	30,059,505	328,273
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### Summary of Balance sheet data

The following table summarises the Company's financial position as at the dates indicated:

	As at March 31, 2012 £	As at December 31, 2011 £
Current assets	32,369,252	8,712,341
Property and equipment	491,012	476,012
Intangible assets	101,824	95,522
Exploration and evaluation assets	23,361,379	23,739,005
Other non-current assets	1,330,652	1,371,935
Other long-term financial assets	125,240	126,600
Total assets	57,779,359	34,521,415
Current liabilities	3,413,834	7,002,493
Non-current liabilities	27,395	28,800
Equity	54,338,130	27,490,122
Total liabilities and equity	57,779,359	34,521,415

During the first quarter of 2012 the cash and cash equivalents of the Company increased by £23,360,336 as a result of new shares issue totaling to net proceeds of £30,059,505. On March 13, 2012 the Company paid to Newmont £3,245,307 (US \$5.1 million) which represents the second settlement of US \$5 million for purchase of Newmont's interest in Amulsar project. In addition, a payment of US \$100,000 was made representing the accrued interest for deferring the payment from December 31, 2011 to the date of the payment. During the reportable period there were prepayments for exploration drilling services, payments to vendors for Amulsar Project development costs, payments to vendors for supply of services and goods, and payments to employees.

The net balance of Exploration and Evaluation assets as of March 31, 2012 decreased by £377,626 compared to December 31, 2011. This was due to the strengthening of British Pounds against Armenian Drams and Georgian Laries resulting in a reduction of £1,174,754, which was partially offset by new expenditure in the period. British Pounds to Armenian Drams exchange rate as of March 31, 2012 was 625.45 compared to 594.93 as of December 31, 2011. During three month period ended March 31, 2012, £796,675 was invested in Exploration and Evaluation assets in the development of Amulsar project. During three month period ended March 31, 2012 costs of exploration studies at Zoti project totaled to £453.

In the three month period ended March 31, 2012, investment in property, plant and equipment totaled £72,526 which was mainly aimed to support the exploration and development of the Amulsar and Zoti projects.

### Exploration and evaluation assets

Exploration and evaluation costs are costs incurred directly in exploration and evaluation as well as the purchase cost of mineral licenses as per IFRS 6.

Exploration and evaluation costs relating to Amulsar and Zoti incurred during the three month period ended March 31, 2012 were £797,128 compared to £356,754 in the corresponding period in 2011 (Zoti project began in September 2011). These exploration and evaluation costs were related to exploration work on the Company's exploration projects as follows:



Project	Cumulative as at March 31, 2012	Cumulative as at December 31, 2011
Armenia		
• Amulsar	23,165,059	23,535,396
Georgia		
• Zoti	196,320	203,609
Total	23,361,379	23,739,005

During three month period ended March 31, 2012 a total of £796,675 was invested in Amulsar Project representing costs renting of licence areas, exploration camp maintenance, cost of environmental studies etc. As a result of exchange rate differences between March 31, 2012 and December 31, 2011 there was a reduction of project balance by £1,167,012 resulting in a decrease in the Amulsar project's balance by £370,337.

The following table represents expenditures capitalised at the Amulsar project during three month period ended March 31, 2012 and corresponding period in 2011.

	Three months to March 31,	
	2012	2011
	£	£
Project development	517,042	78,357
Environmental studies	102,353	33,134
Capitalised salaries	67,286	62,575
Supplies and materials	9,153	9,388
Depreciation and amortisation	29,988	14,374
Laboratory assay	20,567	49,728
State duties and fees	16,370	44,175
Other	33,916	65,023
	796,675	356,754

During three month period ended March 31, 2012, £453 was invested in Zoti project, however the net balance of the project decreased by £7,289 as result of strengthening British Pounds exchange rate to Georgian Laries.

In Armenia and Georgia the Company's exploration activities are financed mainly in US Dollars, which are converted into Armenian Drams and Georgian Laries respectively by the Company's subsidiaries and then into British Pounds for the group accounts. The cumulative totals are therefore affected by currency fluctuations between British Pounds, US Dollars, Armenian Drams, and Georgian Laries. There has been significant devaluation of the Armenian Dram in 2012 and 2011 and slight fluctuations in Georgian Laries.

## SUMMARY OF QUARTERLY RESULTS

The following is a summary of results from the Company's eight most recently completed quarters:

	Q1 2012	Q4 2011	Q3 2011	Q2 2011
	£	£	£	£
Net sales or total revenues	-	-	-	-
Net loss	(1,591,455)	(1,600,982)	(1,402,189)	(1,598,306)
Loss per share (basic and diluted)	0.01	0.02	0.01	0.02
	Q1 2011	Q4 2010	Q3 2010	Q2 2010
	£	£	£	£
Net sales or total revenues	-	-	-	-

Net loss	(1,353,411)	(3,637,443)	(940,826)	(840,892)
Loss per share (basic and diluted)	0.01	0.04	0.01	0.01

### OUTSTANDING SHARE DATA

A summary of outstanding shares options and warrants is set out below.

	As at May 14, 2012	As at March 31, 2011	As at December 31, 2011
	Number	Number	Number
Ordinary Shares	123,554,168	104,075,686	104,075,686
Stock option plan	5,212,000	5,002,000	4,987,000
Other Options	-	-	-
Warrants	3,311,758	3,311,758	3,311,758

The Company has one class of issued equity shares, being Ordinary Shares.

### MANAGEMENT AND STAFFING

On March 5, 2012, the Company announced the appointment of Mr. Tim Richards as Senior Mine Manager to oversee the development of its Amulsar Project. Mr. Richards is an Australian Mining Engineer with 12 years open-pit mine development and production experience across Australia, Africa and Europe.

### LIQUIDITY AND CAPITAL RESOURCES

Lydian had working capital of £28,955,418 as at March 31, 2012 compared to £1,709,848 on December 31, 2011. The Company has total assets of £57,779,359 at March 31, 2012 compared to £34,521,415 on December 31, 2011, which include deferred exploration expenditures of £23,361,379 (£23,739,005 on December 31, 2011).

The Company's principal source of liquidity as at March 31, 2012 is cash and cash equivalents of £31,662,243 compared to £8,301,907 on December 31, 2011. This increase in the cash and cash equivalents balance was primarily the result of new share issues (described below) which provided net chase proceeds of £30,059,505. Within three month period ended March 31, 2012, £2,573,384 cash was used in operating activities and £4,083,118 of capital expenditures on property, equipment and intangible assets, exploration costs and payment to Newmont. Cash surplus to the Company's requirements was invested in money market deposits.

In March 2012 the Company completed a £31,941,086 equity financing, net of underwriters' fee and other share issue cost expenses totaling £1,881,581. The Company used US\$5.1 million of the net proceeds of the offering to pay all amounts that were due to Newmont as of March 13, 2012, and intends to use a portion of the net proceeds to progress the Amulsar Project to and through the completion of a BFS.

As stated above the Company now requires environmental impact assessment approval for its expanded open-pit and waste dump facilities and land status change for the surface rights underlying the project infrastructure. Subject to permitting and the BFS confirming the positive nature of the PEA then the balance of the funds will be used for purchase of mine and processing equipment ; for construction of Amulsar Project communication facilities ; for continued exploration work on the Amulsar Project ; for continued exploration work on the Zoti Project; to pay US \$5 million to Newmont on or prior to December 31, 2012 in accordance with the Newmont Purchase Agreement; and for general working capital purposes and expenditures in the normal course of business.

It is management's opinion, based on the Company's current liquidity position and estimates of project expenses, that the Company's liquid assets will be sufficient to discharge liabilities and fund the above in the manner planned over the next 12 months. The future exploration and development of the Amulsar Project and the Zoti Project will require the Company to raise additional capital through a combination of equity and debt financings. The Company is conducting a BFS, for which the financial numbers are expected to be completed around the end of the second quarter of 2012.

The Company's liquidity is affected by a number of key factors and risks. Reference is made to the "Risks and Uncertainties" section of the MD&A for a discussion of these factors and their impact on the Company's liquidity.

The Company has made certain expenditure commitments to the licensing authorities for the Company's projects. Should these expenditure targets not be met, the applicable licenses will not automatically be forfeited, but any shortfall will be considered by the applicable regulatory authority as a factor in whether to renew such licenses.

### **CONTRACTUAL OBLIGATIONS**

The Company has contractual obligations as follows:

	Total £	Up to 1 year £	1-5 years £	More than 5 years £
Operating lease obligations	2,093,547	140,090	467,975	1,485,482
Purchase obligations	-	-	-	-
Total contractual obligations	2,093,547	140,090	467,975	1,485,482

**TAXES PAID IN ARMENIA**

## LYDIAN INTERNATIONAL LIMITED IN ARMENIA

## Summary of payments to the Armenian State Budgets

The following information is provided as part of an initiative by Publish What You Pay (a global civil society coalition) to achieve transparency of oil, gas and mining company payments to agencies and representatives of those governments as a first step towards a more accountable system for the management of natural resources.

AMOUNTS PAID IN ARMENIAN DRAMS TO ARMENIAN GOVERNMENT		
Item	3 months to March 31, 2012	3 months to March 31, 2011
Fee for licenses area extension	-	8,700,000
State duty on mining license	10,000,000	-
Concession fee	26,490,400	20,097,500
Social Insurance Funds employer	9,810,000	7,749,000
Social Insurance Funds individual	5,310,000	2,939,000
Customs duty	-	3,892,989
Property tax	150,000	72,000
Income tax	19,200,000	19,127,960
Non resident withholding tax	5,000,000	6,000,000
VAT	169,066	8,968,314
Nature protection fee	18,300	-
Total	76,147,766	77,546,763
Equivalent GBP	124,653	133,098

**FINANCIAL AND OTHER INSTRUMENTS**

The Company's financial instruments consist of cash and cash equivalents, accounts receivable, accounts payable and investment in Tigris Resources Limited. The net fair value of the financial assets and financial liabilities approximates their carrying value. The Company's exposure to changes in market interest rates, relates primarily to the Company's cash deposits. The Company maintains a balance between the liquidity of cash assets and the interest rate return thereon. The carrying amount of financial assets, net of any provisions for losses, represents the Company's maximum exposure to credit risk.

**SIGNIFICANT TRANSACTIONS, CONTRACTS AND OFF BALANCE SHEET ARRANGEMENTS**

Significant contracts existing as of March 31, 2012 are described below.

On April 23, 2010, the Company purchased from Newmont all of Newmont's interest in the former joint venture between the Company and Newmont known as the Caucasus Venture, including all of Newmont's interest in the Amulsar gold property in Armenia. The consideration was a mixture of committed and contingent payments. The committed payments included the issuance by Lydian of three million Ordinary Shares to Newmont on the closing of the transaction and three payments of US \$5million; the first of which was paid in 2010 and the second was due on or before December 31, 2011 and the third on or before

the earlier of December 31, 2012 and the date that is 90 days after a BFS on any portion of the Amulsar property is complete and the Company has received all the necessary material permits to move into production. The Company made the US \$5 million payment that was due on December 31, 2011 on March 13, 2012, together with interest owing thereon, calculated at the rate of 10% per annum commencing on December 31, 2011.

In addition, the Company agreed to pay Newmont, following the start of commercial production at the Amulsar Project, a 3% Net Smelter Royalty (NSR). However, at any time prior to the date that is 20 days following commencement of commercial production, Lydian may at its option elect to buy out the 3% NSR and instead pay to Newmont the aggregate sum of US \$20 million, without interest, in 20 equal quarterly installments of US \$1 million commencing on the first day of the third calendar month following the start of commercial production. Furthermore, the Company has a one-time option prior to the commencement of Commercial Production to prepay these quarterly installments in a single cash payment using an annual discount rate of 10%. This equates to a payment of approximately US \$15.6 million.

These potential post production payment(s) do not constitute an “obligation or a constructive obligation”, as the triggering event of commercial production has not yet occurred. Therefore, these potential payments are not shown on the Statement of Financial Position as of March 31, 2012.

On December 9, 2010, the Company entered into an option agreement (the “Geoteam Option Agreement”) to purchase the remaining 5% non-controlling interest (the “non-controlling interest”) of the Company’s 95% indirectly owned subsidiary. The aggregate purchase price payable by the Company in connection with any exercise of the Call Option or the Put Option will be CAD\$500,000 in cash and 2,000,000 Ordinary Shares (the “Payment Shares”) in the capital of the Company. On January 18, 2011, June 27, 2011 and December 20, 2011, the Company issued 500,000, 250,000 and 250,000 Payment Shares, respectively, pursuant to the Geoteam Option Agreement. A further four equal installments of 250,000 Ordinary Shares are issuable bi-annually in 2012 and 2013.

The Company does not have any other off-balance sheet arrangements.

## **RISKS AND UNCERTAINTIES**

The following risks and uncertainties, among others, should be considered when evaluating the Company and its outlook.

### **Mineral Resources**

The Company’s mineral resources are estimates, and no assurance can be given that the estimated resources are accurate or that the indicated level of gold will be produced. Such estimates are, in large part, based on interpretations of geological data obtained from drill holes and other sampling techniques. Actual mineralisation or formations may be different from those predicted. Further, it may take many years from the initial phase of drilling before production is possible, if at all, and during that time the economic feasibility of exploiting a discovery may change. Mineral resource estimates for properties that have not commenced production are based, in many instances, on limited and widely spaced drill hole information, which is not necessarily indicative of the conditions between and around drill holes. Accordingly, such mineral resource estimates may require revision as more drilling information becomes available or as actual production experience is gained. It should not be assumed that all or any part of the Company’s mineral resources constitutes or will be converted into reserves.

### Metal Prices

Even if the Company's exploration program is successful on its mineral projects, there are many factors beyond the control of the Company that may affect the marketability of any minerals discovered. Metal prices have historically fluctuated widely and are affected by numerous factors beyond the Company's control, including international, economic and political trends, expectations for inflation, currency exchange fluctuations, interest rates, global or regional consumption patterns, speculative activities and worldwide production levels. The effect of these factors cannot accurately be predicted.

### Price Volatility of Other Commodities

The Company's profitability is also affected by the market prices of commodities, which are consumed or otherwise used in connection with the operations, such as diesel fuel, natural gas, electricity and cement. Prices of such commodities are also subject to volatile price movements over short periods of time and are affected by factors that are beyond the Company's control.

### Foreign Operations

The Company's significant exploration and development project is located in Armenia. Such a project could be adversely affected by exchange controls, currency fluctuations, taxation and laws or policies of Armenia affecting foreign trade, investment or taxation.

Changes in mining or investment policies or shifts in political attitude in Armenia may adversely affect the Company's business. Operations may be affected by governmental regulations with respect to restrictions on production, price controls, export controls, income taxes, expropriation of property, maintenance of claims, environmental legislation, land use, land claims of local people, water use and mine safety. The factors cannot be accurately predicted.

### Foreign Exchange

The Company operates internationally and is therefore exposed to foreign exchange risks arising from foreign currency fluctuations. The Company raises finance in Canadian Dollars, accounts in British Pounds and incurs expenses mainly in six currencies – the Euro, the British Pound, the US Dollar, the Canadian Dollar, the Armenian Dram and the Georgian Lari. The Company's risk management policy is to hold cash in the Euro, British Pound, the US Dollar and the Canadian Dollar, broadly in line with its currency expenditure forecasts. The Company does not currently hedge its foreign exchange exposure.

### Counterparty Risk

The Company does not have any significant credit risk exposure to any single counterparty or any group of counterparties having similar characteristics. We do not anticipate a loss for non-performance by any counterparty with whom we have a commercial relationship.

### Taxation Risk

The Armenia tax system could impose substantial burdens on the Company. The Company is subject to a broad range of taxes imposed at federal, regional and local levels. Laws related to these taxes have been in force for a relatively short period relative to tax laws in more developed market economies and few precedents with regard to the interpretation of these laws have been established. No assurances can be made that any new tax laws introduced by

the Government of Armenia will not result in the Company having to pay significantly higher taxes, which could have a materially adverse effect on the Company's business.

#### Environmental Risks and Hazards

All phases of the Company's operations are subject to environmental regulations in the various jurisdictions in which it operates. These regulations mandate, among other things, the maintenance of air and water quality standards and land reclamation. Environmental legislation is evolving in a manner which will require stricter standards and enforcement, increased fines and penalties for non-compliance, more stringent environmental assessments of proposed projects and a heightened degree of responsibility for companies and their officers, directors and employees. There is no assurance that future changes in environmental regulations, if any, will not adversely affect the Company's operations. Environmental hazards may exist on the properties in which the Company holds interests which are unknown to the Company at present and which have been caused by previous or existing owners or operators of the properties.

Failure to comply with applicable laws, regulations and permitting requirements may result in enforcement actions there under, including orders issued by regulatory or judicial authorities causing operations to cease or be curtailed and may include corrective measures requiring capital expenditures, installation of additional equipment or remedial actions. Parties engaged in the exploration or development of mineral properties may be required to compensate those suffering loss or damage by reason of the exploration activities and may have civil or criminal fines or penalties imposed for violations of applicable laws or regulations. Amendments to current laws, regulations and permits governing operations and activities of exploration companies, or more stringent implementation thereof, could have a material adverse impact on the Company and cause increases in exploration expenses.

#### Exploration

Exploration is highly speculative in nature and exploration projects involve many risks that even a combination of careful evaluation, experience and knowledge may not eliminate. If a site with gold or other precious metal mineralisation is discovered (and this may not happen), it may take several years from the initial phases of drilling until production is possible, if at all. Substantial expenditures are normally required to locate and establish mineral reserves and to construct mining and processing facilities. While the discovery of an ore body may result in substantial rewards, few properties that are explored are ultimately developed into producing mines.

#### Political

The majority of the Company's operations are carried out in Eurasia and, as such, the Company's operations are exposed to various levels of political risks and uncertainties. These risks and uncertainties vary from country to country and include, but are not limited to, terrorism; corruption; crime; hostage taking or detention of personnel; military repression; extreme fluctuations in currency exchange rates; high rates of inflation; labour unrest; the risks of war or civil unrest; expropriation and nationalisation; renegotiation or nullification of existing concessions, licenses, permits and contracts; absence of reliable regulatory and judiciary process; changes in taxation policies; restrictions on foreign exchange and repatriation; changing political conditions; currency controls; and governmental regulations that favour or require the awarding of contracts to local contractors or require foreign contractors to employ citizens of, or purchase supplies from, a particular jurisdiction. Any changes in mining or investment policies or shifts in political attitude in Eurasia may adversely affect the Company's operations and financial condition. Failure to comply with

applicable laws, regulations and local practices relating to mineral right applications and tenure could result in loss, reduction or expropriation of entitlements.

### Insurance

The Company's business is subject to a number of other risks and hazards, including adverse environmental conditions, industrial accidents, labour disputes, unusual or unexpected geological conditions, ground or slope failures, cave-ins, changes in the regulatory environment and natural phenomena such as inclement weather conditions, floods, hurricanes and earthquakes. Such occurrences could result in damage to mineral properties or production facilities, personal injury or death, environmental damage to the Company's properties or the properties of others, monetary losses and possible legal liability.

Although the Company maintains insurance to protect against certain risks in such amounts as it considers to be reasonable, its insurance will not cover all the potential risks associated with Company's operations. The Company may also be unable to maintain insurance to cover these risks at economically feasible premiums. Insurance coverage may not continue to be available or may not be adequate to cover any resulting liability. The Company might also become subject to liability for pollution or other hazards which may not be insured against or which the Company may elect not to insure against because of premium costs or other reasons. Losses from these events may cause the Company to incur significant costs that could have a material adverse effect upon its financial performance and results of operations.

### Government Laws and Regulations

The activities of the Company are subject to various laws governing prospecting, development, production, taxes, labour standards and occupational health, toxic substances, land use, water use, land claims of local people and other matters. Although the Company currently carries out its operations in accordance with all applicable rules and regulations, no assurance can be given that new rules and regulations will not be enacted or that existing rules and regulations will not be applied in a manner that could limit or curtail production or development. The Company's operations and development activities are subject to receiving and maintaining permits from appropriate governmental authorities. There is no assurance that the Company will be successful in obtaining or maintaining the necessary licences and permits to continue its exploration and development activities in the future.

### Difficulty in Obtaining Future Financing

The further development and exploration of mineral properties in which the Company holds an interest or which the Company acquires may depend upon the Company's ability to obtain financing through joint ventures, debt financing, equity financing or other means. There is no assurance that the Company will be successful in obtaining required financing as and when needed. Volatile precious metals markets may make it difficult or impossible for the Company to obtain debt financing or equity financing on favorable terms or at all. Failure to obtain additional financings on a timely basis may cause the Company to postpone development plans, forfeit rights in its properties or reduce or terminate its operations. Reduced liquidity or difficulty in obtaining future financing could have an adverse impact on the Company's future cash flows, earnings, results of operations, and financial condition and could result in a default under its agreement with Newmont pursuant to which the Company's subsidiary acquired a 100% interest in the Venture.

### RELATED PARTY TRANSACTIONS

Related parties include the Board of Directors, close family members and enterprises which are controlled by these individuals as well as certain persons performing similar functions.



The sole operating director of Geoteam CJSC and Kavkaz Zoloto CJSC, Hayk Aloyan, holds 5% of the shares in Geoteam and Kavkaz Zoloto.

The directors and key management are the directors of Lydian International Limited. The remuneration of directors and key management was as follows:

	Three months ended March 31, 2012	Three months ended March 31, 2011
	£	£
Aggregate emoluments	179,038	82,948
Fair value of granted share options vest	294,860	102,154

Within the three month period ended March 31, 2012 there were no grants of stock options to the directors of the Company. The following table sets out the number of stock options awarded to directors of the Company under the Company's stock option plan during the twelve month periods ended December 31, 2011.

Date of grant	Number of options	Exercise price	Expiry
May 2, 2011	1,500,000	CAD\$2.52(1.59 pound)	May 2, 2016

There were no other share based payments during reportable periods.

## **CRITICAL ACCOUNTING ESTIMATES AND POLICIES**

### **Critical judgments in applying the Company's accounting policies**

In the application of the Company's accounting policies, the directors are required to make judgments, estimates and assumptions about the carrying amounts of assets and liabilities that are not readily apparent from other sources. The estimates and associated assumptions are based on historical experience and other factors that are considered to be relevant. Actual results may differ from these estimates.

The significant critical judgment that the directors have made in the process of applying the entity's accounting policies and that have the most significant effect on the amounts recognised in the consolidated financial statements is the policy on exploration and evaluation costs.

In particular, management is required to assess exploration and evaluation assets for impairment with reference to the indicators provided in IFRS 6. Note 14 to the Company's Interim Consolidated Financial Statements as of March 31, 2012 discloses the carrying values of such assets. As part of this assessment, management considered whether indicators of impairment exist at March 31, 2012.

The recoverability of exploration and evaluation costs is dependent on a number of factors common to the natural resource sector. These include the extent to which the Company can establish economically recoverable reserves on its properties, the availability of the Company to obtain necessary financing to complete the development of such reserves and future profitable production or proceeds from the disposition thereof. The Company will use the evaluation work of professional geologists, geophysicists and engineers for estimates in determining whether to commence or continue mining and processing. These estimates generally rely on scientific and economic assumptions, which in some instances may not be correct, and could result in the expenditure of substantial amounts of money on a deposit

before it can be determined whether or not the deposit contains economically recoverable mineralisation.

#### Key sources of estimation uncertainty

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period or in the period of the revision and future periods if the revision affects both current and future periods.

#### Changes in accounting policies

During the three month period ended March 31, 2012 there were no changes in the Company's accounting policies.

### **DISCLOSURE CONTROLS AND INTERNAL CONTROLS OVER FINANCIAL REPORTING**

Disclosure controls and procedures are designed to provide reasonable assurance that material information is gathered and reported to senior management, including the Chief Executive Officer and Chief Financial Officer, as appropriate to permit timely decisions regarding public disclosure. Management is responsible for establishing and maintaining adequate internal control over financial reporting ("ICFR"). ICFR is a process designed by or under the supervision of the Chief Executive Officer and Chief Financial Officer, and effected by the Board of Directors, management and other personnel to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with IFRS. The Company used the Internal Control – Integrated Framework issued by the Committee of Sponsoring Organisations of the Treadway Commission (COSO) for the design of the Company's ICFR. All internal control systems have inherent limitations and therefore our ICFR can only provide reasonable assurance and may not prevent or detect misstatements due to error or fraud.

The Chief Executive Officer and Chief Financial Officer have concluded, based on their evaluation of the design and operating effectiveness of the Company's disclosure controls and procedures and ICFR as of March 31, 2012, that disclosure controls and procedures and ICFR were effective.

There were no significant changes in the Company's internal controls or in other factors that could significantly affect those controls subsequent to the date the Chief Executive Officer and Chief Financial Officer completed their evaluation, nor were there any significant deficiencies or material weaknesses in the Company's internal controls requiring corrective actions.

A control system, no matter how well conceived or operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. The Company continues to review and document its disclosure controls and procedures, including internal control over financial reporting, and may from time to time make changes aimed at enhancing their effectiveness and to ensure that its systems evolve with its business.

### **MANAGEMENT'S RESPONSIBILITY FOR FINANCIAL STATEMENTS**

The information provided in this report, including the financial statements, is the responsibility of management. In the preparation of these statements, estimates are sometimes necessary to make a determination of future values for certain assets or liabilities.

Management believes such estimates are based on careful judgments and have been properly reflected in the accompanying financial statements.

Management maintains a system of internal controls to provide reasonable assurance that the Company's assets are safeguarded and to facilitate the preparation of relevant and timely information.

### INFORMATION ON INCURRED EXPENSES

Material costs incurred in the three month periods ended March 31, 2012 and 2011 were as follows:

Cost type	Three months to March 31,	
	2012 £	2011 £
<sup>(1)</sup> Exploration and evaluation deferred expenditures	797,128	450,600
<sup>(2)</sup> Employees benefit and expenses	936,202	532,976
Administrative and other expenses	340,975	284,244
Services and consumables used	280,793	207,760
Interest expenses	132,177	126,921
Depreciation and amortisation	12,402	38,633
	<u>2,499,677</u>	<u>1,641,134</u>

<sup>(1)</sup>These expenditures are capitalised as exploration and evaluation assets.

<sup>(2)</sup>Within three month period ended March 31, 2012, the allocation to employee benefit reserves fund (relating to vesting options) totaled to £450,039 while the corresponding number in the same period in 2011 was £233,308 so the net amount of increase is £216,731. The balance in the increase over this period relates to an increase in the number of employees and some increases in salaries.