



KGHM INTERNATIONAL LTD.
Condensed Interim Consolidated Financial Statements
June 30, 2014
(Expressed in millions of U.S. dollars, except where indicated)
(Unaudited)

**CONDENSED INTERIM CONSOLIDATED STATEMENTS OF
FINANCIAL POSITION**

(US Dollars in Millions)
(Unaudited)

	<i>Notes</i>	June 30, 2014	December 31, 2013
ASSETS			
Current			
Cash and cash equivalents		118.4	140.0
Trade and other receivables	6	159.8	192.8
Notes receivable	21	-	104.9
Inventory	5	187.9	157.7
Current corporate tax receivables		28.8	16.6
Total Current Assets		494.9	612.0
Mineral properties, property, plant and equipment	8	950.6	923.5
Intangible assets	9	418.2	398.8
Sierra Gorda JV- Investment	4(a)	466.1	494.2
Sierra Gorda JV- Subordinated loans	4(b)	1,484.3	1,121.5
Environmental trust and bonds		42.7	48.1
Other non-current assets	7	73.9	54.2
Deferred income tax assets		83.9	89.3
Total Non-Current Assets		3,519.7	3,129.6
Total Assets		4,014.6	3,741.6
LIABILITIES AND SHAREHOLDERS' EQUITY			
Current			
Accounts payable and accrued liabilities	10	112.4	125.1
Current provisions	14	18.0	17.4
Other current liabilities		4.4	5.3
KGHM Cash Pooling	13	25.0	-
Derivative liabilities	15	8.6	9.3
Current portion of deferred revenue	11	11.6	9.5
Current corporate tax liabilities		2.6	8.2
Total Current Liabilities		182.6	174.8
Borrowings and finance lease liabilities	12	617.9	498.5
Deferred revenue	11	150.0	156.8
Provisions	14	140.6	134.5
Derivative liabilities	15	41.8	42.4
Deferred income tax liabilities		206.6	205.5
Total Non-Current Liabilities		1,156.9	1,037.7
Total Liabilities		1,339.5	1,212.5
Shareholders' Equity			
Share capital	16	1,995.5	1,851.5
Accumulated other comprehensive gain		0.3	0.1
Retained earnings		679.3	677.5
Total Shareholders' Equity		2,675.1	2,529.1
Total Liabilities and Shareholders' Equity		4,014.6	3,741.6

Commitments (Note 23), Contingencies (Note 24)

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

KGHM International Ltd.

**CONDENSED INTERIM CONSOLIDATED STATEMENTS OF
COMPREHENSIVE INCOME (LOSS)**

(US Dollars in Millions)
(Unaudited)

	<i>Notes</i>	Three months ended June 30, 2014	Three months ended June 30, 2013	Six months ended June 30, 2014	Six months ended June 30, 2013
Net revenues	17	178.5	314.3	326.2	586.3
Cost of sales	17	155.2	287.4	325.6	495.5
Income from mining operations		23.3	26.9	0.6	90.8
General and administrative	19	8.1	9.0	19.8	26.7
Finance income	20(a)	(22.6)	(19.5)	(44.1)	(36.1)
Finance expense	20(b)	14.4	11.7	28.3	22.7
Other income	20(c)	(2.7)	(11.4)	(9.2)	(17.8)
Other expense		1.4	0.4	2.9	2.5
Impairment of marketable securities		-	8.3	-	35.1
Foreign exchange (gain) loss		(2.1)	15.8	0.5	15.4
Earnings before income taxes		26.8	12.6	2.4	42.3
Income tax expense	18	(4.4)	(10.9)	(0.6)	(25.8)
Earnings for the period		22.4	1.7	1.8	16.5
Other comprehensive income					
Unrealized gain (loss) on marketable securities		-	0.1	0.2	(4.5)
Reversal due to impairment of marketable securities		-	-	-	26.8
Total comprehensive income		22.4	1.8	2.0	38.8
Earnings per share					
Basic		\$ 0.08	\$ 0.01	\$ 0.01	\$ 0.08
Diluted		\$ 0.08	\$ 0.01	\$ 0.01	\$ 0.08
Weighted average shares outstanding - basic		296.0	199.8	247.9	199.8
Weighted average shares outstanding - diluted		296.0	199.8	247.9	199.8

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

KGHM International Ltd.

**CONDENSED INTERIM CONSOLIDATED STATEMENTS OF
CHANGES IN SHAREHOLDER'S EQUITY**

(US Dollars in Millions)
(Unaudited)

	<i>Notes</i>	Share capital	Accu. other comp. income	Retained earnings	Total
Balances, January 1, 2014		1,851.5	0.1	677.5	2,529.1
Issue of common shares	<i>16</i>	144.0	-	-	144.0
Unrealized gain on marketable securities		-	0.2	-	0.2
Earnings for the year		-	-	1.8	1.8
Balances, June 30, 2014		1,995.5	0.3	679.3	2,675.1

	<i>Notes</i>	Share capital	Accu. other comp. income	Retained earnings	Total
Balances, January 1, 2013		1,851.5	(22.2)	668.1	2,497.4
Unrealized loss on marketable securities		-	(4.5)	-	(4.5)
Reversal due to impairment of marketable securities		-	26.8	-	26.8
Earnings for the year		-	-	16.5	16.5
Balances, June 30, 2013		1,851.5	0.1	684.6	2,536.2

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

KGHM International Ltd.

**CONDENSED INTERIM CONSOLIDATED STATEMENTS OF
CASH FLOWS**

(US Dollars in Millions)

(Unaudited)

	<i>Notes</i>	Three months ended June 30, 2014	Three months ended June 30, 2013	Six months ended June 30, 2014	Six months ended June 30, 2013
OPERATING ACTIVITIES					
Earnings for the period		22.4	1.7	1.8	16.5
Adjustment for:					
Amortization, depletion and depreciation		30.4	37.3	66.1	68.5
Depreciation capitalized to deferred stripping asset		(1.0)	(0.9)	(2.1)	(0.9)
Impairment of marketable securities		-	8.3	-	35.1
Non-cash loss (gain) on derivatives	15	1.2	(5.1)	(1.3)	(5.2)
Amortization of deferred revenue	11	(2.6)	(2.5)	(4.7)	(5.6)
Foreign exchange (gain) loss		(0.7)	13.2	0.7	11.8
Income tax expense	18	4.4	10.9	0.6	25.8
Finance income		(22.7)	(17.5)	(43.9)	(32.2)
Finance expense		13.5	10.6	26.2	20.8
Other income		(1.0)	(0.3)	-	(0.3)
Other expense		3.0	1.6	5.4	3.6
		46.9	57.3	48.8	137.9
Net changes in non-cash working capital	22	(38.5)	91.8	(28.8)	59.3
Interest paid on borrowings and finance lease		(21.2)	(19.4)	(23.5)	(19.5)
Income taxes paid		(0.1)	(0.9)	(11.9)	(14.3)
Cash (used in) provided from operating activities		(12.9)	128.8	(15.4)	163.5
INVESTING ACTIVITIES					
Additions to mineral properties, plant and equipment		(57.9)	(43.5)	(106.2)	(63.0)
Proceeds from disposal of mineral properties, plant and equipment		0.1	0.1	0.2	0.5
Decrease in restricted cash		-	137.1	-	-
Deposits for environmental trust and bonds		-	(5.5)	-	(5.4)
Cash released from environmental trust and bonds		5.1	1.1	5.4	1.1
Proceeds from sale of marketable securities		-	7.8	-	7.8
Increase in Sierra Gorda JV- Subordinated loans	4	(166.3)	(141.6)	(298.3)	(275.2)
Increase in Sierra Gorda JV- Investments	4	-	(0.9)	-	(0.9)
Notes receivable	21	-	-	105.6	34.6
Cash used in investing activities		(219.0)	(45.4)	(293.3)	(300.5)
FINANCING ACTIVITIES					
Proceeds from KGHM Cash Pooling	13	25.0	-	25.0	-
Finance lease payments		(0.6)	(0.3)	(1.2)	(0.3)
Draw down of Corporate Facility	12	25.0	-	120.0	-
Payments for issuance cost related to Corporate Facility		-	(2.4)	-	(2.4)
Proceeds from issue of common shares	16	144.0	-	144.0	-
Cash provided from (used in) financing activities		193.4	(2.7)	287.8	(2.7)
Effect of foreign exchange rate changes on cash and cash equivalents		0.7	(13.2)	(0.7)	(11.8)
Net (decrease) increase in cash and cash equivalents during the period		(37.8)	67.5	(21.6)	(151.6)
Cash and cash equivalents, beginning of period		156.2	318.4	140.0	537.4
Cash and cash equivalents, end of period		118.4	385.9	118.4	385.9

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

**NOTES TO CONDENSED INTERIM CONSOLIDATED
FINANCIAL STATEMENTS**

(US Dollars in Millions)
Six months ended June 30, 2014
(Unaudited)

1. NATURE OF OPERATIONS

KGHM International Ltd. (“KGHMI” or the “Group”) (formerly Quadra FNX Mining Ltd) (“Quadra FNX”) was incorporated in Canada on May 15, 2002 under the British Columbia Company Act. KGHMI is a subsidiary of KGHM Polska Miedź S.A (“KGHM”), a company based in Poland that operates three mines and two smelter/refineries in Poland. KGHM acquired the Group through a court-approved Plan of Arrangement that closed on March 5, 2012.

The Group is in the business of developing and operating mines, with a focus on base metals, particularly copper. The Group’s principal place of business is Canada. KGHMI’s head office is located at Suite 500-200 Burrard Street, Vancouver, British Columbia, V6C 3L6. The Group has five operating mines: the Robinson mine in Nevada; the Levack mine, including the Morrison deposit, in Ontario; the Franke mine in Chile; the Carlota mine in Arizona; and the McCreedy West mines in Ontario. The Podolsky mine substantially ceased operations during the first quarter of 2013 and is currently under care and maintenance, pending environmental closure. On September 14, 2011, the Group formed a joint venture (“Sierra Gorda JV”) with Sumitomo Metal Mining Co. Ltd. and Sumitomo Corporation (collectively “Sumitomo”) to develop the Sierra Gorda copper-molybdenum project in Chile (Note 4). The Group also owns an advanced exploration project (“Victoria”) in Sudbury, Ontario.

The Robinson, Franke and Carlota mines are open pit copper mines, with some byproduct gold and molybdenum at Robinson, and Levack/Morrison and McCreedy West (collectively “the Sudbury Operations”) are underground mines producing copper with byproduct nickel, platinum, palladium and gold. The Sudbury Operations, the Victoria project and a mining services business (“DMC”), were acquired on May 20, 2010, when the Group completed a merger with FNX Mining Company Ltd. (“FNX”).

2. BASIS OF PRESENTATION

a) Basis of presentation and measurement

The unaudited condensed interim consolidated financial statements have been prepared in accordance with IAS 34 Interim financial reporting as issued by the International Accounting Standards Board (“IASB”). The consolidated financial statements should be read in conjunction with the annual financial statements for the year ended December 31, 2013, which have been prepared in accordance with IFRS as issued by the IASB.

The Board of Directors (“BoD”) approved these financial statements for issue on August 12, 2014.

b) Basis of consolidation

These condensed interim consolidated financial statements include the accounts of the Group and its controlled subsidiaries. Control is achieved when the Group has the rights to variable returns and rights to affect those returns from its involvement with its subsidiaries. All subsidiaries are wholly-owned. The Sierra Gorda JV, of which the Group owns 55%, is accounted for using the equity method. The results of subsidiaries acquired or disposed of during the period are included in the condensed interim consolidated statements of comprehensive income (loss) from the effective date of acquisition or to the date of disposal. Intergroup balances and transactions are eliminated on consolidation.

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c) Use of estimates and judgments

Areas of critical accounting estimates and judgments that have the most significant effect on the amounts recognized in the financial statements are disclosed in Note 2(c) of the Group's consolidated financial statements as at and for the year ended December 31, 2013.

3. SIGNIFICANT ACCOUNTING POLICIES

These financial statements have been prepared using the same accounting policies as those disclosed in Note 3 to the Group's annual audited consolidated financial statements for the year ended December 31, 2013.

New pronouncements adopted

IFRIC 21 Accounting for levies imposed by governments

IFRIC 21 is an interpretation of IAS 37 Provisions, Contingent Liabilities and Contingent Assets. IFRIC 21 clarifies that the obligating event giving rise to a liability to pay a levy is the activity described in the relevant legislation that triggers payment of the levy. IFRIC 21 was adopted by the Group on January 1, 2014.

The adoption of IFRIC 21 did not affect the Group's financial results or disclosures as the Group's analysis determined that no changes were required to the Group's existing accounting treatment of levies.

New IFRS Pronouncements

In May 2014, IFRS 15 Revenue from Contracts with Customers ("IFRS 15") was issued, which is applicable for annual reporting periods beginning on or after January 1, 2017, with an option for early adoption. IFRS 15 establishes principles to address the nature, amount, timing and uncertainty of revenue and cash flows arising from an entity's contracts with customers. The Group is in the process of analyzing the impact of IFRS 15 and determining the effect on the consolidated financial statement.

4. SIERRA GORDA JV

(a) Sierra Gorda JV- Investment

The Group and Sumitomo formed a joint venture on September 14, 2011 to develop the Sierra Gorda copper-molybdenum project in Chile. The joint venture operates through a jointly-controlled entity owned 55% by the Group and 45% by Sumitomo and is being accounted for using the equity method.

The Group's investment in the Sierra Gorda JV at June 30, 2014 was \$466.1 (December 31, 2013- \$494.2).

(b) Sierra Gorda JV- Subordinated loans

As of June 30, 2014 the Group had funded \$1,322.8 (December 31, 2013- \$1,024.5) to the Sierra Gorda JV through subordinated loan agreements. The balance as at June 30, 2014 includes accrued interest of \$161.5 (December 31, 2013- \$97.1). For the period ended June 30, 2014, the Group recorded interest income of \$64.4

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(June 30, 2013- \$30.3) (Note 20(a)). Subject to the subordinated conditions to the Senior Project loans, interest and principal of the subordinated loans are payable on demand. The subordinated loans form part of the security arrangement under the Senior Project loans.

(c) Contractual Commitments

At June 30, 2014, the Group's proportionate 55% share of the contractual commitments with respect to the Sierra Gorda JV related to the construction and operation of the mine were as follows: \$377.3 in 2014, \$146.3 in 2015 and \$1,258.4 for 2016.

During the year ended December 31, 2013, Sierra Gorda entered into lease agreements to lease various mine equipment. The Group's proportionate share of the minimum lease payments totaled \$159.8 as at June 30, 2014 (December 31, 2013- \$34.3). These leases are accounted for as finance leases with a term of 84 months and most bear an interest rate of 90-day LIBOR plus a spread.

As at June 30, 2014, the Sierra Gorda JV had cash and cash equivalents of \$257.7 (December 31, 2013- \$285.8).

(d) Contingencies

Port Matters

In January 2014, some citizens of Antofagasta, including the Major, a Deputy, neighbours associations, local professionals, and some owners and tenants of buildings close to the area, filed two Constitutional legal actions before the Court of Appeals of Antofagasta to stop the construction of the warehouse at the port of Antofagasta. The claims were against the Regional Environment agency, Antofagasta Railway Company PLC, International Port of Antofagasta and the Sierra Gorda JV.

The intention of the legal action is for the annulment of the permits to transport and store of Sierra Gorda JV's copper concentrate. All three companies, together with the environmental agency challenged such claims. However, on February 26, 2014, the Court of Appeals of Antofagasta ruled in favour of the plaintiffs and annulled all permits, requesting the Sierra Gorda JV to re-enter the environmental evaluation system including all activities. All companies and the "Servicio de Evaluacion Ambiental" (SEA) appealed to the Supreme Court. On April 15, 2014 oral hearings were done and strong intents for conciliation were being conducted.

On August 4, 2014, the Supreme Court reversed the judgment of the Court of Appeals of Antofagasta made in February 2014 which annulled permits to transport and store Sierra Gorda's copper concentrate, which would have also caused Sierra Gorda to re-enter the environmental evaluation system on all related activities. Due to reversals of such annulments, the construction of the warehouse at the port of Antofagasta can legally continue.

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FINANCIAL STATEMENTS**

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(Unaudited)

5. INVENTORY

	June 30, 2014	December 31, 2013
Robinson copper concentrate	34.9	8.5
Carlota leach pad inventory	67.8	59.9
Franke leach pad inventory	16.1	15.4
Copper cathode	10.2	4.8
Supplies	50.8	51.9
Robinson ore stockpile	8.1	16.6
Sudbury crushed ore inventory	-	0.6
	187.9	157.7

For the six months ended June 30, 2014 (June 30, 2013- \$Nil), cost of sales includes \$14.6 of inventory write down at Robinson during the first quarter to reduce the concentrate and ore stockpile inventory to net realizable value.

During the second quarter of 2014, a reversal of impairment was recognized in cost of sales which increased Carlota's leach pad inventory by \$11.5. The reversal of impairment was triggered by a new leaching methodology which is expected to recover copper in areas of the leach pad where lower than expected recovery was experienced and therefore written down in 2010.

6. TRADE AND OTHER RECEIVABLES

	June 30, 2014	December 31, 2013
Trade receivables	132.2	163.7
Receivable from Sierra Gorda JV (Note 21)	11.6	9.5
Receivable from Bidco	0.3	-
Receivable from KGHM and other related parties	0.7	0.8
Prepaid expenses and advances to suppliers	11.6	14.8
Other receivables	3.4	4.0
	159.8	192.8

The net carrying value of trade and other receivables approximates fair value. The Group has multiple terms of payment with its customers depending on type of product shipped, and as such, the carrying values are the Group's maximum credit risk associated with each classification of receivables. These receivables are neither collateralized nor secured.

The Group's allowance for doubtful accounts is \$Nil for the period ended June 30, 2014 (December 31, 2013- \$0.4).

Trade receivables as at June 30, 2014 include receivables that pertain to construction contracts of \$39.3 (December 31, 2013- \$13.4) and retention on construction contracts of \$11.8 (December 31, 2013- \$21.6).

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7. OTHER NON-CURRENT ASSETS

	June 30, 2014	December 31, 2013
Security deposits for equipment	1.4	1.4
Receivable from Sierra Gorda JV (Note 21)	23.7	9.2
Prepaid on long term contracts	6.1	6.7
Restricted cash	37.0	30.9
Other	5.7	6.0
	73.9	54.2

Restricted cash relates to various cash backed letters of credit including letters of credit to BHP Billiton Canada Inc. for the work being performed by DMC Mining Services.

8. MINERAL PROPERTIES, PROPERTY, PLANT AND EQUIPMENT

	Land and buildings	Mineral property acquisition and development	Machinery and equipment	Assets under construction	Total
At December 31, 2013					
Cost	60.5	1,481.8	609.4	23.2	2,174.9
Accumulated depletion, depreciation and amortization	(24.0)	(376.8)	(258.5)	-	(659.3)
Accumulated impairment	(20.8)	(421.6)	(149.7)	-	(592.1)
Net book value	15.7	683.4	201.2	23.2	923.5
Period ended June 30, 2014					
Change in Cost					
Additions	-	64.6	1.8	21.4	87.8
Disposal	-	-	(1.6)	(0.8)	(2.4)
Increase in site closure and reclamation asset	-	5.2	-	-	5.2
Transfers	0.5	-	5.8	(6.3)	-
Subtotal	0.5	69.8	6.0	14.3	90.6
Change in Accumulated Amortization					
Reversal of accumulated depletion, depreciation and amortization on disposal	-	-	1.6	-	1.6
Depletion, depreciation and amortization charge	(1.1)	(45.0)	(19.0)	-	(65.1)
Subtotal	(1.1)	(45.0)	(17.4)	-	(63.5)
At June 30, 2014					
Cost	61.0	1,551.6	615.4	37.5	2,265.5
Accumulated depletion, depreciation and amortization	(25.1)	(421.8)	(275.9)	-	(722.8)
Accumulated impairment	(20.8)	(421.6)	(149.7)	-	(592.1)
Net book value	15.1	708.2	189.8	37.5	950.6

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Machinery and equipment includes \$11.8 related to two finance leases agreements entered during the year ended December 31, 2013. Finance lease obligations are \$2.5 due within one year, \$4.6 due within one to three years and \$1.8 due after three years.

Additions to mineral property include deferred stripping cost at Robinson of \$49.3 (December 31, 2013-\$89.3).

9. INTANGIBLE ASSETS

	Exploration and evaluation assets	Water rights	Other intangible assets	Software	Goodwill	Total
At December 31, 2013						
Cost	153.0	59.1	2.4	9.7	180.6	404.8
Accumulated depletion, depreciation and amortization	-	-	(0.3)	(5.7)	-	(6.0)
Net book value	153.0	59.1	2.1	4.0	180.6	398.8
Period ended June 30, 2014						
Change in Cost						
Additions	20.0	0.1	-	0.3	-	20.4
Subtotal	20.0	0.1	-	0.3	-	20.4
Change in Accumulated Amortization						
Depletion, depreciation and amortization charge	-	-	(0.2)	(0.8)	-	(1.0)
Subtotal	-	-	(0.2)	(0.8)	-	(1.0)
At June 30, 2014						
Cost	173.0	59.2	2.4	10.0	180.6	425.2
Accumulated depletion, depreciation and amortization	-	-	(0.5)	(6.5)	-	(7.0)
Net book value	173.0	59.2	1.9	3.5	180.6	418.2

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10. ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

	June 30, 2014	December 31, 2013
Liabilities from deliveries and services	53.4	59.9
Payables to Sierra Gorda JV (Note 21)	0.3	-
Payables to KGHM	0.7	-
Liabilities from employee taxes and social security	3.6	3.9
Liabilities for wages	1.9	2.2
Other financial liabilities	1.1	1.8
Accrued expenses	51.4	57.3
	112.4	125.1

11. DEFERRED REVENUE

The Group has recognized, as deferred revenue, a prepayment received previously by FNX from Franco-Nevada Corporation for the delivery of 50% of the contained gold, platinum and palladium in ore mined and shipped from the existing Sudbury Operations.

Balance - December 31, 2013	166.3
Recognized into revenue	(4.7)
Balance - June 30, 2014	161.6
Current	(11.6)
Non-Current	150.0

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12. BORROWINGS AND FINANCE LEASE LIABILITIES

	June 30, 2014	December 31, 2013
Borrowings	611.5	490.7
Finance lease	6.4	7.8
	617.9	498.5

Borrowings

	June 30, 2014	December 31, 2013
Senior notes	500.0	500.0
Senior note issue costs	(12.3)	(12.3)
Cumulative amortization of senior note issue costs	3.8	3.0
Corporate Facility	120.0	-
	611.5	490.7

i. Borrowings

In June 2011, the Group issued \$500.0 aggregate principal amount of 7.75% senior unsecured notes (“Notes”) due 2019 in a private placement. The Notes are carried at amortized cost. The fair market value of the notes at June 30, 2014 is \$539.0 (December 31, 2013 - \$525.5) based on a trading price of 107.8 (December 31, 2013-105.1) per 100.

These Notes contain certain covenants that limit the Group’s ability and the ability of certain subsidiaries to, incur additional indebtedness and issue preferred stock, create liens, make restricted payments, create or permit to exist restrictions on the ability of the Group or certain subsidiaries to make certain payments and distributions, engage in amalgamations, mergers or consolidations, make certain dispositions and transfers of assets, or engage in transactions with affiliates.

The Group may redeem, prior to June 15, 2015 the Notes in whole or in part at 100.0% of their principal amount, plus accrued interest plus the greater of 1.0% of the principal amount of the note to be redeemed and the excess, if any, of the present value of the June 15, 2015 redemption price plus required interest payments through June 15, 2015 over the principal amount of the note.

The group may redeem the Notes at any time on or after June 15, 2015 at the redemption prices and periods set forth below, plus accrued and unpaid interest:

June 15, 2015.....	103.875%
June 15, 2016.....	101.938%
June 15, 2017 and thereafter	100.000%

Upon specified change of control events, each holder of a note will have the right to require the Group to purchase all or a portion of the Notes at a purchase price in cash equal to 101% of the principal amount, plus accrued interest to the date of purchase.

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At June 30, 2014, no mandatory principal repayments are required in the next five years.

ii. Corporate Facility

During the second quarter of 2013, the Group entered into a \$200.0 senior secured revolving corporate credit facility (“the Corporate Facility”) with a syndicate of banks dated for reference June 19, 2013. The Corporate Facility matures on June 19, 2017 and bears interest at LIBOR plus a margin dependent on the Group’s net indebtedness to rolling EBITDA ratio.

The Corporate Facility is secured against the present and future real property of the Group, excluding assets related to Sierra Gorda and is subject to maintenance of ratios relating to (i) interest coverage (ii) net indebtedness to rolling EBITDA and maintenance of tangible net worth. In addition until certain security interests are perfected, such interests to be completed by June 19, 2014, the Group must maintain a cash balance of \$100.0 in North American based accounts. Failure to maintain these and other standard covenants for the facility of this type could result in the termination and repayment of the Corporate Facility.

In June 2014, the Group received a 60 day extension to perfect security interests required under the Corporate Facility to August 18, 2014. The security interests were perfected pursuant to an amendment to the Corporate Facility dated July 28, 2014. The registration of the security interest was completed on August 1, 2014 and the requirement to maintain a cash balance of \$100.0 in North America is no longer required.

The Group was in compliance with the covenants of the Corporate Facility during the period ended June 30, 2014.

During the first quarter of 2014, KGHM replaced the letter of credit of \$137.5 that had been issued on behalf of the Group for the Sierra Gorda JV power purchase agreement under the Corporate Facility thereby releasing \$137.5 of capacity in the Corporate Facility. During the second quarter of 2014, KGHM replaced the remaining letters of credit that were issued under the Corporate Facility as well as issued an additional \$5.4 letter of credit to replace the environmental bonds redeemed at Robinson.

During the six months ended June 30, 2014, the Group drew \$120.0 in cash from the Corporate Facility. The below table summarizes the usage of the Corporate Facility:

	Letters of Credit	Loans	Total
Balance at December 31, 2013	198.5	-	198.5
Issued for reclamation bonding during the period	11.1	-	11.1
Replaced by KGHM for Sierra Gorda JV	(137.5)	-	(137.5)
Replaced by KGHM for reclamation bonding	(72.1)	-	(72.1)
Draw down of the Corporate Facility	-	120.0	120.0
Balance at June 30, 2014	-	120.0	120.0

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13. KGHM Cash Pooling

During the second quarter of 2014, the Group entered into a \$100.0 cash pooling agreement with its parent company KGHM (“Cash Pooling”). The Cash Pooling bears interest at LIBOR plus margin. The Cash Pooling is unsecured and is subordinated and postponed to the Corporate Facility; in addition repayments of advances are subject to limitations governed by the Corporate Facility and there are no fixed terms of repayment. As of June 30, 2014 the Group had utilized \$25.0 under the Cash Pooling.

14. PROVISIONS

Site closure and reclamation provisions by mineral property are as follows:

	June 30, 2014	December 31, 2013
Site closure and reclamation provision	154.8	148.8
Carlota termination benefits and others	3.8	3.1
Total provisions	158.6	151.9
Current	18.0	17.4
Long term	140.6	134.5
Total provisions	158.6	151.9

Site closure and reclamation provisions are as follows:

Balance at December 31, 2013	148.8
Change in estimated timing and amount of closure cost	1.8
Increase in provision due to change in discount rate	3.4
Reclamation work done to reduce liability	(0.9)
Unwinding of discount	1.7
Balance at June 30, 2014	154.8
Current	16.7
Non Current	138.1

Discount rates used in the estimation of the provision at June 30, 2014 were 1.7% - 2.6% for US operations, 2.3% for Chile operations and 2.2% - 2.8% for Canadian operations (for December 31, 2013 the discount rates used were 1.8% - 3.4%, 2.3% and 2.6% - 2.8% respectively).

The reclamation cost estimates are discounted at a pre-tax risk free rate specific to each liability.

The closure cost estimates are subject to change based on amendments to laws and regulations. The Group is not able to determine the impact on its financial position, if any, of environmental laws and regulations that may be enacted in the future.

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15. DERIVATIVE INSTRUMENTS

As at June 30, 2014 the Group's derivative instruments comprised of long-term supply contracts.

(Gains) and losses on derivatives are comprised of the following:

	Three months ended June 30, 2014	Three months ended June 30, 2013	Six months ended June 30, 2014	Six months ended June 30, 2013
Long-term supply contracts (a)	1.2	(5.1)	(1.3)	(5.2)
Foreign currency forward contracts (b)	-	-	1.4	-
	1.2	(5.1)	0.1	(5.2)

Gains on derivatives are included in other income (Note 20 (c)) and losses are included in other expenses.

(a) Long-term supply contracts

The Group has long-term supply contracts for sulphuric acid and water with contracted prices that are subject to adjustment based on the prevailing copper prices. The acid contract has a low base price, but requires an additional \$2.50/tonne to be paid for each \$0.10/lb that the copper price exceeds \$1.10/lb. Similarly, the water contract requires that an additional \$0.08/cubic metre be paid for each \$0.15/lb that copper price exceeds \$1.50/lb. The minimum commitment under the contracts is estimated to be \$4.1 per annum for acid and \$1.1 per annum for water.

These copper price escalation clauses create embedded derivatives in the acid and water supply contracts. As of June 30, 2014, the fair value of the embedded derivative liabilities was \$50.4 (December 31, 2013 - \$51.7), based on the following significant assumptions:

- Copper price in the range of \$3.02/lb to \$3.39/lb from 2014 to 2022.
- Discount rate: 11%

(b) Foreign currency supply contracts

The Group entered into a number of foreign currency contracts to sell \$200.0 in CLP with a strike price of 525 at a cost of \$1.4 which expired between January and March 2014 unexercised. As of June 30, 2014 no foreign currency forward contracts were outstanding.

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16. SHARE CAPITAL

(a) Common Shares

The Group has authorized share capital of 1,000,000,000 common shares (“Shares”) with no par value.

	Number of Shares	Amount
Balance at January 1, 2014	199,836,316	1,851.5
Capital Stock issued	157,932,000	144.0
Balance at June 30, 2014	357,768,316	1,995.5

During the six months ended June 30, 2014, the Group issued 157,932,000 common shares to its shareholder KGHM for total proceeds of \$144.0 increasing the total outstanding shares to 357,768,316.

17. SEGMENTED INFORMATION

The Group’s reportable operating segments are individual mine operations and development projects, being Robinson, Carlota, Franke, Sudbury Operations, DMC, other mineral properties and Corporate. The corporate segment is responsible for the oversight of the Group’s mineral properties and corporate administration. The Sudbury operations of the Group holds the goodwill established during the merger with FNX Mining Ltd. on May 20, 2010.

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	Robinson (USA) ^(a)	Carlota (USA)	Franke (Chile)	Sudbury Operations (Cda) ^(a)	DMC	Corporate & Other	Total
Copper revenues	61.5	18.5	24.3	29.9	-	-	134.2
Nickel revenues	-	-	-	15.5	-	-	15.5
Other by - product revenues	10.9	-	-	8.5	-	-	19.4
Contract mining revenues	-	-	-	-	26.5	-	26.5
Treatment charges	(7.3)	-	-	(9.8)	-	-	(17.1)
Net revenues	65.1	18.5	24.3	44.1	26.5	-	178.5
Depreciation and amortization	13.5	-	(0.4)	14.5	1.2	-	28.8
Employee benefits expense	10.2	3.7	7.4	8.5	11.7	-	41.5
Raw materials, other consumables and energy	23.7	8.2	14.9	7.0	-	-	53.8
Office expenses	2.3	0.9	2.5	1.8	0.5	-	8.0
External services	5.5	0.8	3.7	5.0	13.5	-	28.5
Royalties and mineral taxes	1.6	0.7	-	-	-	-	2.3
Reversal of leach pad inventory impairment (Note 5)	-	(11.5)	-	-	-	-	(11.5)
Changes in inventories	(3.1)	1.3	(5.5)	(0.1)	-	-	(7.4)
Distribution costs	9.4	-	0.4	1.4	-	-	11.2
Income (loss) from operations	2.0	14.4	1.3	6.0	(0.4)	-	23.3
General and administrative	-	-	-	-	-	8.1	8.1
Finance income	-	-	-	-	-	(22.6)	(22.6)
Finance expense	-	-	-	-	-	14.4	14.4
Other income	-	-	-	-	-	(2.7)	(2.7)
Other expense	-	-	-	-	-	1.4	1.4
Foreign exchange gain	-	-	-	-	-	(2.1)	(2.1)
Segment earnings (loss) before tax	2.0	14.4	1.3	6.0	(0.4)	3.5	26.8
Capital expenditures	31.6	-	3.9	8.2	0.5	16.8	61.0
Segment non-current assets as at June 30, 2014	332.1	68.1	126.0	735.3	40.1	2,218.1	3,519.7
Segment assets as at June 30, 2014	469.6	152.7	180.8	822.0	111.4	2,278.1	4,014.6

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	Robinson (USA)	Carlota (USA)	Franke (Chile)	Sudbury Operations (Cda)	DMC	Corporate & Other	Total
Copper revenues	132.5	18.1	28.6	32.6	-	-	211.8
Nickel revenues	-	-	-	15.1	-	-	15.1
Other by-product revenues	27.5	-	-	7.7	-	-	35.2
Contract mining revenues	-	-	-	-	71.0	-	71.0
Treatment charges	(9.5)	-	-	(9.3)	-	-	(18.8)
Net revenues	150.5	18.1	28.6	46.1	71.0	-	314.3
Depreciation and amortization	8.4	-	4.4	21.9	1.1	-	35.8
Employee benefits expense	11.2	4.2	6.6	11.0	10.4	-	43.4
Raw materials, other consumables and energy	27.2	9.0	19.3	10.5	0.8	-	66.8
Office expenses	6.3	0.7	1.9	3.1	0.6	-	12.6
External services	4.7	1.3	4.3	7.1	53.1	-	70.5
Royalties and mineral taxes	4.8	0.6	-	-	-	-	5.4
Changes in inventories	36.4	(2.1)	4.3	1.3	-	-	39.9
Distribution costs	10.3	-	0.4	2.3	-	-	13.0
Income (loss) from operations	41.2	4.4	(12.6)	(11.1)	5.0	-	26.9
General and administrative	-	-	-	-	-	9.0	9.0
Finance income	-	-	-	-	-	(19.5)	(19.5)
Finance expense	-	-	-	-	-	11.7	11.7
Other income	-	-	-	-	-	(11.4)	(11.4)
Other expense	-	-	-	-	-	0.4	0.4
Impairment of marketable securities	-	-	-	-	-	8.3	8.3
Foreign exchange loss	-	-	-	-	-	15.8	15.8
Segment earnings (loss) before tax	41.2	4.4	(12.6)	(11.1)	5.0	(14.3)	12.6
Capital expenditures	28.4	-	2.7	9.2	1.8	2.0	44.1
Segment non-current assets as at June 30, 2013	323.6	87.1	128.4	779.4	42.0	1,578.3	2,938.8
Segment assets as at June 30, 2013	521.8	145.9	194.0	862.7	124.6	1,848.0	3,697.0

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	Robinson (USA)^(a)	Carlota (USA)	Franke (Chile)	Sudbury Operations (Cda)^(a)	DMC	Corporate & Other	Total
Copper revenues	87.3	35.2	59.1	54.5	-	-	236.1
Nickel revenues	-	-	-	31.7	-	-	31.7
Other by-product revenues	18.8	-	-	15.9	-	-	34.7
Contract mining revenues	-	-	-	-	53.1	-	53.1
Treatment charges	(10.4)	-	-	(19.0)	-	-	(29.4)
Net revenues	95.7	35.2	59.1	83.1	53.1	-	326.2
Depreciation and amortization	26.5	-	4.8	29.5	2.3	-	63.1
Employee benefits expense	22.4	8.0	13.3	16.7	21.9	-	82.3
Raw materials, other consumables and energy	48.2	15.1	31.2	17.0	-	-	111.5
Office expenses	6.0	2.0	5.0	3.8	1.1	-	17.9
External services	11.2	2.0	7.2	11.8	27.4	-	59.6
Royalties and mineral taxes	2.7	1.3	-	-	-	-	4.0
Reversal of leach pad inventory impairment (Note 5)	-	(11.5)	-	-	-	-	(11.5)
Changes in inventories	(17.9)	2.6	(5.2)	0.4	-	-	(20.1)
Distribution costs	14.9	-	1.1	2.8	-	-	18.8
Income (loss) from operations	(18.3)	15.7	1.7	1.1	0.4	-	0.6
General and administrative	-	-	-	-	-	19.8	19.8
Finance income	-	-	-	-	-	(44.1)	(44.1)
Finance expense	-	-	-	-	-	28.3	28.3
Other income	-	-	-	-	-	(9.2)	(9.2)
Other expense	-	-	-	-	-	2.9	2.9
Foreign exchange loss	-	-	-	-	-	0.5	0.5
Segment earnings (loss) before tax	(18.3)	15.7	1.7	1.1	0.4	1.8	2.4
Capital expenditures	51.9	-	8.4	16.3	1.3	28.2	106.1
Segment non-current assets as at June 30, 2014	332.1	68.1	126.0	735.3	40.1	2,218.1	3,519.7
Segment assets as at June 30, 2014	469.6	152.7	180.8	822.0	111.4	2,278.1	4,014.6

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	Sudbury						
	Robinson	Carlota	Franke	Operations	Corporate &		
	(USA)	(USA)	(Chile)	(Cda)	DMC	Other	Total
Copper revenues	219.0	38.3	56.1	75.8	-	-	389.2
Nickel revenues	-	-	-	32.8	-	-	32.8
Other by-product revenues	46.7	-	-	18.1	-	-	64.8
Contract mining revenues	-	-	-	-	134.5	-	134.5
Treatment charges	(15.7)	-	-	(19.3)	-	-	(35.0)
Net revenues	250.0	38.3	56.1	107.4	134.5	-	586.3
Depreciation and amortization	16.3	-	9.7	38.5	2.2	-	66.7
Employee benefits expense	28.6	8.5	14.1	22.3	21.7	-	95.2
Raw materials, other consumables and energy	68.0	18.8	37.9	22.1	0.8	-	147.6
Office expenses	9.5	1.5	4.5	5.1	1.2	-	21.8
External services	9.2	2.5	9.1	16.6	94.5	-	131.9
Royalties and mineral taxes	7.8	1.6	-	-	-	-	9.4
Changes in inventories	4.0	(4.7)	(2.9)	(0.2)	-	-	(3.8)
Distribution costs	20.8	-	0.7	5.2	-	-	26.7
Income (loss) from operations	85.8	10.1	(17.0)	(2.2)	14.1	-	90.8
General and administrative	-	-	-	-	-	26.7	26.7
Finance income	-	-	-	-	-	(36.1)	(36.1)
Finance expense	-	-	-	-	-	22.7	22.7
Other income	-	-	-	-	-	(17.8)	(17.8)
Other expense	-	-	-	-	-	2.5	2.5
Impairment of marketable securities	-	-	-	-	-	35.1	35.1
Foreign exchange gain	-	-	-	-	-	15.4	15.4
Segment earnings (loss) before tax	85.8	10.1	(17.0)	(2.2)	14.1	(48.5)	42.3
Capital expenditures	33.0	-	(0.7)	8.1	0.5	2.0	42.9
Segment non-current assets as at June 30, 2013	323.6	74.4	127.2	766.0	42.0	1,603.0	2,936.2
Segment assets as at June 30, 2013	521.8	158.2	195.6	920.7	130.3	1,822.7	3,749.3

- (a) Revenues at Robinson and Sudbury Operations are from concentrate and ore sales and are recorded provisionally at the time of sale based on forward prices for the expected date of the final settlement. Subsequent variations in price are recognized as revenue adjustments as they occur until the price is finalized. At June 30, 2014, 30.8 million pounds of copper have been provisionally valued at an average price of \$3.15 per pound. The final pricing for these provisionally priced sales is expected to occur between July 2014 and October 2014.

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18. INCOME TAXES

For the six months ended June 30, 2014, the Group recognized a current income tax recovery of \$5.8 and a deferred income tax expense of \$6.4 (June 30, 2013- \$16.9 current income tax expense and \$8.9 deferred income tax expense). The income tax recovery for the six months ended June 30, 2014 has been recorded based on a forecasted effective income tax rate of negative 5% (June 30, 2013- 29%). The forecast of the annual effective income tax rate includes assumptions regarding metal prices, mine production and costs.

Management believes that uncertainty exists regarding the realization of certain deferred tax assets and therefore the economic benefit of the available related tax deduction has not been recognized. The Group has not recognized the benefit of U.S. Alternative Minimum Tax credits, the tax basis of Carlota in excess of the acquisition price and certain non-capital losses.

The Group has foreign subsidiaries that have undistributed earnings. The Group can control the timing of the repatriation of undistributed earnings, and it is probable that these earnings will not be repatriated in the foreseeable future. Therefore, deferred income taxes have not been provided in respect of these earnings.

19. GENERAL AND ADMINISTRATIVE

	Three months ended June 30, 2014	Three months ended June 30, 2013	Six months ended June 30, 2014	Six months ended June 30, 2013
Employee benefits expenses	3.1	6.7	9.7	16.0
Legal and professional services	2.5	(1.4)	4.0	3.3
Office and communication expenses	2.4	3.6	6.0	7.5
Insurance expenses and property taxes	0.1	0.1	0.1	(0.1)
	8.1	9.0	19.8	26.7

20. FINANCE INCOME AND EXPENSE

(a) Finance Income

Finance income for the six months ended June 30, 2014 of \$44.1 (June 30, 2013- \$36.1) is primarily related to interest earned on short-term investments of \$0.2 (June 30, 2013- \$3.9), interest on subordinate loans to Sierra Gorda JV of \$41.2 (June 30, 2013- \$30.3) and interest on notes receivable of \$0.7 (June 30, 2013- \$1.9) (Note 21) and letter of credit fees to Sierra Gorda JV of \$2.0 (June 30, 2013- \$Nil) (Note 21).

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(b) Finance Expenses

Finance expense for the six months ended June 30, 2014 of \$28.3 (June 30, 2013- \$22.7) is primarily comprised of \$19.4 interest expense related to senior notes (June 30, 2013- \$19.4), interest expense on the Corporate Facility of \$2.2 (June 30, 2013- \$Nil) (Note 13), accretion \$1.7 (June 30, 2013-\$0.9), guarantee fees on Sierra Gorda financing \$2.1 June 30, 2013-\$1.7) and interest to KGHM on letters of credit fees of \$1.6 (June 30, 2013- \$Nil) (Note.12).

(c) Other Income

Other Income for the six months ended June 30, 2014 of \$9.2 (June 30, 2013- \$17.8) is primarily comprised of management fees from Sierra Gorda JV of \$7.7 (June 30, 2013- \$12.5) (Note 21), and gain on derivatives of \$1.3 (June 30, 2013- \$5.2) (Note 15).

21. RELATED PARTY TRANSACTIONS AND BALANCES

Upon formation of the Sierra Gorda JV, the joint venture became a related party with the Group. The amount due from the Sierra Gorda JV is \$11.6 at June 30, 2014 (December 31, 2013- \$9.5) (Note 6) and is repayable in the normal course of business. Management fees payable to the Group for the period ended June 30, 2014 was \$3.1 (June 30, 2013- \$12.5) from the Sierra Gorda JV. It was agreed that 50% of the payment of the management fees earned from July 1 to December 31, 2013, 100% of the management fees earned from January 1, 2014 onwards and 100% of the letter of credit guarantee fees payable to the Group be deferred until 2015. As at June 30, 2014, \$18.7 (December 31, 2013- \$6.3) of the management fee and \$5.0 (December 31, 2013- \$2.9) of a letter of credit guarantee fee have been deferred (Note 7). The outstanding amounts bear an interest rate of 0.75% per annum.

On March 5, 2012, the Group loaned \$110.9 to Bidco for the purchase and exercise of FNX Warrants in conjunction with the Plan of Arrangement. The obligation with respect to the loan is evidenced by a promissory note payable to the Group. In Q1 2013, the maturity date was extended to March 5, 2014. Interest on the outstanding principal is calculated at 3.75% per annum payable in arrears on the maturity date, or on the date which the principal amount is paid by Bidco. Bidco repaid \$13.2 of the above principal and interest on February 28, 2013. On March 10, 2014, Bidco repaid \$105.6 of the remaining principal and interest.

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22. SUPPLEMENTARY CASH FLOW INFORMATION

Changes in non-cash working capital consisted of the following:

	Three months ended June 30, 2014	Three months ended June 30, 2013	Six months ended June 30, 2014	Six months ended June 30, 2013
(Increase) decrease in receivables	(16.3)	57.4	33.2	91.1
(Increase) decrease in inventory	(15.7)	36.1	(30.2)	(13.6)
(Increase) decrease in other non-current asset	(14.2)	0.7	(18.1)	1.0
Decrease (increase) in accounts payable and accrued liabilities	7.0	(2.4)	(14.4)	(19.2)
Increase in provision	0.7	-	0.7	-
	(38.5)	91.8	(28.8)	59.3
Non-cash investing and financing activities:				
Increase (decrease) in mineral properties, plant and equipment purchases in accruals	3.1	(0.4)	(0.1)	(4.4)
Increase in additions to mineral properties, plant and equipment due to finance lease	-	11.8	-	11.8

23. COMMITMENTS

As at June 30, 2014 the commitments of the Group excluding Sierra Gorda were \$146.0 in relation to capital projects, rent and contractual obligations. Commitments of \$43.9 are due within one year, \$61.0 are due within one to five years and \$41.1 are due after three years. Commitments include undiscounted derivative liabilities related to the acid and water long-term supply contracts.

In addition the above commitments, Robinson mine signed a five year electricity supply contract in 2014 which expires in 2019. The minimum commitment under the contract is estimated to be \$6.6 per year over the term of the contact.

Commitments that pertain to Sierra Gorda are disclosed in Note 4(c).

24. CONTINGENCIES

- (a) In the normal course of business DMC enters into agreements that contain indemnification commitments and may contain features that meet the expanded definition of guarantees. The terms of these indemnification agreements will vary based on the contract and typically do not provide for a limit on the maximum potential liability. The Group has not made any payments under such indemnifications and no amounts have been accrued in the consolidated financial statements with respect to these indemnification commitments.

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- (b) DMC has encountered certain design issues around the shaft sinking for one of its major customers that could give rise to future liability. The Group is evaluating this issue together with its customer but at this stage the amount of any liability cannot be determined.
- (c) The Group is subject to lawsuits from time to time, existing litigation is not considered to be likely to have a material impact on the financial statements.

25. FINANCIAL INSTRUMENTS

Financial instruments are classified as held for trading, loans and receivables, available for sales or other financial liabilities. Financial instruments carried at fair value on the consolidated balance sheet are classified within a fair value hierarchy that prioritizes the inputs to fair value measurements. The three levels of the fair value hierarchy are:

- Level 1 – Quoted prices in active markets for identical assets or liabilities;
- Level 2 – Inputs other than quoted prices that are observable for the asset or liability either directly or indirectly; and
- Level 3 – Inputs that are not based on observable market data.

At June 30, 2014 and at December 31, 2013, the carrying value of financial instruments were approximately their fair value except for senior note with a carrying value of \$491.5 (December 31, 2013- \$490.7) and a fair value of \$539.0 (December 31, 2013- \$525.5) (Note 12). The fair value hierarchy for the Group's financial instruments at June 30, 2014 and December 31, 2013 was as follows:

- Level 1: Marketable securities.
- Level 2: Receivable for provisionally priced metal sales, derivative assets, derivatives and embedded derivatives liabilities

Level 1 – Quoted Prices in Active Markets for Identical assets or liabilities

Marketable equity securities are valued using quoted market prices in active markets. Accordingly, these items are included in Level 1 of the fair value hierarchy.

Level 2 – Significant other observable inputs

Derivative instruments are included in Level 2 of the fair value hierarchy as they are valued using discounted cash flow models. These models require a variety of inputs, including, but not limited to contractual terms, market prices, forward price curves, long term price estimates. These inputs are obtained from or corroborated with the market where possible. The significant assumptions are described in Note 15.

Also included in Level 2 are settlements expected from provisional pricing on concentrate and ore sales because they are valued using quoted market prices.

The Group does not have any level 3 financial instruments.

The Group's activities expose it to a variety of financial risks: currency risk, credit risk, liquidity risk, interest rate risk and commodity price risk. The condensed interim consolidated financial statements do not include all

KGHM International Ltd.

**NOTES TO CONDENSED INTERIM CONSOLIDATED
FINANCIAL STATEMENTS**

(US Dollars in Millions)

Six months ended June 30, 2014

(Unaudited)

financial risk management information and disclosures required in the annual financial statements; they should be read in conjunction with the Group's annual financial statements as at December 31, 2013. These risks are assessed regularly and when appropriate the Group takes steps to mitigate these risks. There have been no changes in the risk management department or in any risk management policies since the year end.