



International Corporation

**Third Quarter 2006**

Report to Shareholders

For Quarter Ending September 30, 2006



## Contents

<b>Corporate Profile</b>	3
<b>Highlights</b>	4
<b>Management's Discussion &amp; Analysis</b>	
Significant Transactions	17
Change in Accounting for Royal Utilities	17
Consolidated Earnings	18
Consolidated Cash Flow	21
Consolidated Financial Position	22
Outlook and Review of Operations	
Metals	25
Oil & Gas	28
Power	32
Coal	35
Other	37
Summary of Quarterly Results	38
Accounting Changes	39
Comparative Amounts	40
Accounting Pronouncements	40
Critical Account Estimates	43
Off Balance Sheet Arrangements	43
Transactions with Related Parties	43
Contractual Obligations and Commitments	43
Additional Information	44
Disclosure Controls and Procedures	44
<b>Interim Consolidated Financial Statements</b>	
Consolidated Balance Sheets	45
Consolidated Statements of Operations	46
Consolidated Statements of Retained Earnings	46
Consolidated Statements of Cash Flow	47
Notes to Interim Consolidated Financial Statements	48
<b>Supplementary Financial Information</b>	
Schedule of Selected Current Assets and Accounts Payable by Operating Segment	61

## Corporate Profile

Sherritt International Corporation is a diversified resource company involved in the production of coal, nickel, cobalt, oil and electricity. Its success is built upon utilizing innovative technologies and the breadth of its financial and operational expertise to increase productivity and profitability. Sherritt continues to explore opportunities to grow its \$2.5 billion asset base through expansion of its existing businesses and strategic acquisitions.

A leader in employee health and safety, Sherritt is also dedicated to ensuring that its operations meet the highest standards in environmental stewardship.

Sherritt's 152 million common shares and \$142 million 7% convertible debentures trade on the Toronto Stock Exchange under the symbols S and S.DB.A respectively. Sherritt's \$274 million of 7.875% Senior Unsecured Debentures Series A, due November 26, 2012 trade on the over-the-counter bond market.

## Forward-looking Statements

*This interim report contains forward-looking statements. Forward-looking statements generally can be identified by the use of statements that include words such as "believe", "expect", "anticipate", "intend", "plan", "likely", "will" or other similar words or phrases. Similarly, statements contained in each of the "Outlook" sections of this interim report including those with respect to expectations concerning assets, prices, foreign exchange rates, earnings, production, market conditions, capital expenditures, commodity demand, risks, availability of regulatory approvals, corporate objectives and plans or goals, are or may be forward-looking statements. These forward-looking statements are not based on historic facts, but rather on current expectations, assumptions and projections about future events. These forward-looking statements are subject to known and unknown risks, uncertainties and other factors that are beyond the Corporation's ability to control or predict. Actual results and developments may differ materially from those contemplated by this interim report depending on, among others, such key factors as business and economic conditions in Canada, Cuba and the principal markets for Sherritt's products.*

*Key factors that may result in material differences between actual results and developments and those contemplated by this interim report also include the supply, demand and prices for Sherritt's products; dependence on significant customers; deliveries; production levels, production and other anticipated and unanticipated costs and expenses; energy costs; premiums or discounts realized over LME cash and other benchmark prices; interest rates; foreign exchange rates; rates of inflation; changes in tax legislation; the timing, capital costs and financing arrangements associated with development projects; the timing of the receipt of government and other approvals; political unrest or instability in the countries where Sherritt is active; risks related to collecting accounts receivable and repatriating profits and dividends from Cuba; risks related to foreign exchange controls on Cuban government enterprises to transact in foreign currency; risks associated with the United States embargo on Cuba and the Helms-Burton Act; risks associated with mining, processing and exploration activities; potential imprecision of reserve estimates; market competition; developments affecting labour relations; environmental regulation and other risk factors listed from time to time in Sherritt's continuous disclosure documents such as its annual report, annual information form and management information circular.*

*The Corporation does not intend, and does not assume any obligations, to update these forward-looking statements.*

## Highlights

- Third-quarter earnings per share increased 188% from prior year to \$0.49 per share
- Operations capitalize on strong commodity prices to drive EBITDA up by 48%
- Metals expansion construction proceeding in a phased approach
- Additional \$50 million of principal amount convertible debt purchased in October

### Financial Highlights (unaudited)

(millions of dollars, except per share amounts)	Q3 2006	Q2 2006 (restated) <sup>(2)</sup>	Q3 2005 (restated) <sup>(2)</sup>	Nine months ended September 30	
				2006	2005 (restated) <sup>(2)</sup>
Revenue	\$ 285.5	\$ 306.6	\$ 257.3	\$ 853.4	\$ 836.9
EBITDA <sup>(1)</sup>	148.3	124.8	100.1	385.3	369.2
Net earnings	74.1	57.2	26.1	167.0	115.2
Basic earnings per share	0.49	0.38	0.17	1.10	0.77
Diluted earnings per share	0.43	0.36	0.15	1.00	0.64
Basic book value per share <sup>(3)</sup>	9.02	8.57	8.97	9.02	8.97
Total cash and cash equivalents	416.0	367.5	368.7	416.0	368.7
Total assets	2,473.3	2,354.3	2,790.7	2,473.3	2,790.7
Weighted average number of shares (millions)					
Basic	151.3	151.3	155.2	151.3	149.6
Diluted	179.1	179.4	199.8	179.2	199.0

<sup>(1)</sup> EBITDA is a non-GAAP measure. Reference should be made to the Summary Financial Results by Segment later in this interim report for a description of EBITDA and for reconciliation to GAAP measures. EBITDA does not have a standardized meaning and is, therefore, unlikely to be comparable with similar measures presented by other issuers.

<sup>(2)</sup> Comparable periods have been restated to reflect a change in the methodology of accounting for income taxes in the Cuban oil and gas business and the reclassification and adjustment of certain revenues, operating, selling, general and administrative costs in the Metals business.

<sup>(3)</sup> Basic book value per share, a non-GAAP measure, is calculated by dividing shareholders' equity by the outstanding number of shares of 151.7 million as at September 30, 2006, 151.3 million as at June 30, 2006 and 155.4 million as at September 30, 2005.

Sherritt International Corporation ("Sherritt" or the "Corporation") announced record earnings in the third quarter of \$74.1 million or \$0.49 per share. Operations capitalized on strong commodity prices to drive net earnings up by \$48.0 million from the third quarter of 2005.

After adjusting for Royal Utilities, consolidated revenues in the third quarter were \$83.4 million higher than the comparable period in 2005. Unlike the third quarter of 2005, revenues recorded in the third quarter of 2006 do not reflect Royal Utilities' revenues. Sherritt now accounts for Royal Utilities using the equity method of accounting. All business segments posted higher revenues compared to the same quarter last year.

EBITDA for the quarter was \$148.3 million, an increase of \$23.5 million over the second quarter, and an increase of \$48.2 million from the comparable period last year. Increased capacity in certain business segments and stronger commodity pricing continued to drive EBITDA. Cash and cash equivalents, restricted cash and short-term investments totalled \$417.8 million as at September 30, 2006. The \$50.3 million increase over the previous quarter is mainly due to cash from operations of \$99.5 million, exceeding capital expenditures of \$55.3 million.

Capital expenditures of \$55.3 million in the third quarter included \$30.0 million in drilling activity and facilities construction in Oil and Gas and \$17.3 million in expansion and maintenance in Metals. Power expenditures were \$13.0 million, including progress payments of \$7.3 million that are recorded in other assets, mainly for the Phase 7 expansion.

## Significant Events in the Quarter

In Metals, Sherritt and its joint venture partner have agreed to modify the original expansion plans at Moa Nickel and Fort Saskatchewan (16,000 tonnes per annum on a 100% basis) and proceed instead with a phased expansion. Phase 1 will result in 4,000 tonnes per annum (100% basis) of new production and is projected to be commissioned at the end of 2007. Phase 2 will be approximately 9,000 tonnes per annum (100% basis) and is projected to be commissioned in 2009. Phase 3 will likely include over 3,000 tonnes per annum (100% basis) of additional capacity and is projected to be commissioned in 2011. Delivery of Phase 1 production will come online prior to the original timeline outlined for the expansion. The decision to phase the expansion lowers execution risk and provides for an optimal utilization of available labour in Canada and Cuba.

The IPO of Sherritt's thermal coal assets was favourably received in the market. In the quarter, Royal Utilities' units appreciated by 13%. Sherritt holds 40.3 million units.

Subsequent to quarter end, Sherritt purchased \$50 million principal amount of its outstanding 7% convertible unsecured subordinated debentures due December 15, 2013 by way of an issuer bid. Total consideration for the purchase was \$80.5 million. Sherritt considers this purchase to be an effective use of its cash while still providing the Corporation with the flexibility to pursue growth opportunities. Additional purchases of outstanding debentures may be considered. The \$143 million principal amount of convertible debentures that remain outstanding are redeemable in whole or in part at the option of the Corporation, starting December 16, 2006.

## Outlook for 2006 (see "Forward-looking Statements")

Sherritt anticipates that prices for nickel, cobalt and oil will continue to be above historical averages. Pricing similar to that seen at the end of the quarter is expected for the remainder of the year. .

Overall, all business segments within Sherritt are undertaking growth initiatives seeking to capitalize on the strong commodities environment by increasing productive capacity while simultaneously improving cost competitiveness.

Sherritt expects to confirm higher oil reserves in the fourth quarter which will reduce depletion expense. In addition, as the drilling and classification of concessions in the Metals business nears completion, Sherritt will be incorporating significant additional nickel and cobalt reserves.

Factoring in timing adjustments for ongoing capital projects, full year 2006 capital expenditures are expected to be approximately \$268 million. This amount includes \$87 million in Metals, \$38 million in Power and \$125 million in Oil and Gas.

**Metals** – Taking into consideration process bottlenecks experienced in prior quarters, full year nickel production is expected to be approximately 30,000 tonnes (100% basis). Cobalt production for the year remains inline with initial expectations of approximately 3,000 tonnes (100% basis).

Operating costs in the fourth quarter are expected to be similar to those recorded in the third quarter.

Metals capital expenditures, adjusted to realign with the phased expansion, are expected to be \$41 million in the fourth quarter.

**Oil and Gas** – Gross working-interest oil production in Cuba is expected to remain relatively constant into the fourth quarter as new production from development drilling offsets natural reservoir declines. The outlook for net oil production for the remainder of 2006 is dependent on several factors, including gross working-interest production volumes, fuel oil reference prices and capital spending. Average gross working-interest production volumes for the year are expected to be approximately 30,500 boepd.

Sherritt applied in the third quarter for production from the Majaguillar block to be declared commercial. Majaguillar is expected to help oil production growth in 2007.

Oil and Gas capital expenditures are expected to be \$35 million in the fourth quarter. As compared to previous guidance, full-year capital expenditures will be lower than previously anticipated due to the timing of capital expenditures associated with Oil and Gas facilities.

**Power** – Production for 2006 remains on track to surpass two million megawatt (MW) hours.

The first of two Phase 7 turbines for the 65 MW expansion at Boca de Jaruco is scheduled to be delivered in November, with the second turbine expected in January. Commissioning of both turbines is expected in the second quarter of 2007. The total cost of the project is estimated to be \$60 million, with approximately \$18 million to be spent in the fourth quarter.

As of September 2005, the tariff for the initial 226 MW of capacity decreased to US\$38 per megawatt hour as per the terms of the contract. The tariff for subsequent operations including Phase 6 (85 MW) and Phase 7 (65MW), is US\$45 per megawatt hour until financing provided by Sherritt for these phases is repaid. This financing is expected to be repaid by 2010, but the repayment period may be extended if subsequent expansions proceed. The full-year 2006 weighted average tariff is expected to be approximately US\$39.50 per megawatt hour.

Operating costs are expected to be slightly higher in the fourth quarter, compared to the third quarter, due to additional scheduled maintenance.

**Coal** – Positive cash flow generated at Coal Valley operations is projected to continue into the fourth quarter. In the final quarter of 2006, Coal Valley expects to maintain the record production levels that were achieved in the third quarter.

Sherritt is actively moving forward with the Dodds-Roundhill coal gasification project (formerly known as Camrose Ryley) and preliminary engineering has commenced. Negotiations with oxygen and gasification suppliers for the project are underway. Discussions have also begun with off-take customers for all syngas production from the first phase of the proposed four-stage project.

Preliminary engineering has begun for the first coal gasification complex in western Canada. Near surface coal reserves of approximately 500 million tonnes (equivalent to approximately nine trillion cubic feet of gas) have been earmarked for the gasification project. Public consultations for the proposed Dodds-Roundhill mine were initiated in the third quarter and a preliminary disclosure document has been submitted to the Alberta government.

Sherritt intends to demonstrate that proven gasification technologies can be successfully deployed in western Canada. With control over approximately 12 billion tonnes of near surface coal reserves in this area, Sherritt believes that the potential exists to have its coal reserves revalued on an energy equivalent basis.

Capital expenditures for the remainder of the year are expected to be \$0.4 million.

## Metals

	Q3 2006	Q2 2006	Q1 2006	Q4 2005	Q3 2005	Nine months ended September 30, 2006		2005
Production (tonnes)								
Nickel	3,878	3,338	3,681	3,854	3,825	10,897		12,085
Cobalt	419	370	409	409	417	1,198		1,287
Sales (thousands of pounds)								
Nickel	8,795	7,213	8,283	9,275	7,619	24,291		26,289
Cobalt	879	861	923	963	955	2,663		2,768
EBITDA (mm of \$)	\$ 78.9	\$ 46.3	\$ 30.1	\$ 20.5	\$ 34.3	\$ 155.3		\$ 145.9
Realized Prices <sup>(1)</sup>								
Nickel (\$/lb)	\$ 14.42	\$ 10.42	\$ 7.77	\$ 6.91	\$ 8.02	\$ 10.96		\$ 8.68
Cobalt (\$/lb)	17.77	16.46	14.56	16.08	17.64	16.24		19.62
Reference Prices								
Nickel (US\$/lb)	\$ 13.24	\$ 9.09	\$ 6.72	\$ 5.73	\$ 6.61	\$ 9.69		\$ 7.00
Cobalt (US\$/lb) <sup>(2)</sup>	15.59	14.43	12.43	12.50	13.41	14.15		15.16
Capital Expenditures (mm of \$)	\$ 17.3	\$ 12.9	\$ 15.1	\$ 12.8	\$ 10.8	\$ 45.3		\$ 24.4

<sup>(1)</sup> Comparable periods have been restated to reflect the change in accounting for certain selling expenses which were previously netted against revenues and have now been reclassified to operating, selling, general and administrative costs

<sup>(2)</sup> Average Metal Bulletin: 99.3% cobalt published price

Mixed sulphide production at Moa recovered during the quarter and contributed to a 16% increase in nickel production over the second quarter of 2006. Nickel sales quarter-over-quarter grew 22%, increasing from 7.2 million pounds to 8.8 million pounds. Operations in Moa during the quarter focused on maintaining mixed sulphides production at the 33,000 tonne production rate (100% basis).

Capitalizing on the strong commodity prices, EBITDA in the quarter was a record \$78.9 million. This represents a 70% increase over last quarter and 130% increase over the third quarter of 2005.

During the quarter, nickel prices remained well above historical averages and reached a 15-year high in August. Subsequent to quarter end, nickel prices surpassed a 19-year old record of US\$15.56 per pound in mid October.

Annual planned maintenance activities were initiated at the Fort Saskatchewan site in the third quarter. In addition, autoclave maintenance outlined in the second quarter is proceeding and is expected to be concluded during the fourth quarter.

Capital expenditures for the period totalled \$17.3 million, with the majority of that spent on Phase 1 activities in Moa.

## Oil and Gas

Daily Production Volumes <sup>(1) (2)</sup>	Q3 2006	Q2 2006	Q1 2006	Q4 2005	Q3 2005	Nine months ended September 30, 2006 2005	
Production (boepd)							
Gross working-interest production in Cuba <sup>(3) (5)</sup>	29,855	30,330	30,891	29,714	29,600	30,355	31,257
Net production <sup>(4)</sup>							
Cuba (heavy oil)							
Cost recovery <sup>(5)</sup>	6,480	6,074	7,303	6,189	5,764	6,616	8,462
Profit oil <sup>(5)</sup>	<u>9,088</u>	<u>9,535</u>	<u>9,215</u>	<u>9,255</u>	<u>9,408</u>	<u>9,279</u>	<u>8,922</u>
Total Cuba	15,568	15,609	16,518	15,444	15,172	15,895	17,384
Spain (light/medium oil) <sup>(4)</sup>	505	457	495	592	569	486	498
Pakistan (natural gas) <sup>(4)</sup>	<u>403</u>	<u>375</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>261</u>	<u>-</u>
Total	16,476	16,441	17,013	16,036	15,741	16,642	17,882
EBITDA (mm of \$)	\$ 52.6	\$ 54.7	\$ 56.2	\$ 49.1	\$ 52.1	\$ 163.5	\$ 150.2
Realized Prices							
Cuba (per bbl)	\$ 41.88	\$ 45.20	\$ 43.14	\$ 38.28	\$ 39.65	\$ 43.40	\$ 34.74
Spain (per bbl)	77.32	78.09	71.28	65.96	73.46	75.53	66.04
Reference Prices							
US Gulf Coast Fuel Oil							
#6 (US\$ per bbl)	\$ 46.38	\$ 48.88	\$ 45.86	\$ 40.31	\$ 39.88	\$ 47.11	\$ 34.43
Capital Expenditures	\$ 30.0	\$ 33.0	\$ 23.7	\$ 28.9	\$ 27.9	\$ 86.7	\$ 93.2

(1) Production figures exclude production from wells for which commerciality has not been established.

(2) Oil production is stated in barrels per day ("bpd"). Natural gas production is stated in barrels of oil equivalent per day ("boepd"), which is converted at 6,000 cubic feet per boepd.

(3) In Cuba, Oil and Gas delivers all of its gross working-interest oil production to CUPET at the time of production. Gross working-interest oil production excludes (i) production from wells for which commerciality has not been established in accordance with production sharing contracts; and (ii) working interests of other participants in the production sharing contracts.

(4) Net production (equivalent to net sales volume) represents the Corporation's share of gross working-interest production. In Spain and Pakistan, net oil production volumes equal 100% of gross working-interest production volumes.

(5) Gross working-interest oil production is allocated between Oil and Gas and CUPET in accordance with production sharing contracts. CUPET's share is analogous to Crown royalty interests under Canadian hydrocarbon fiscal regimes. The Corporation's share, referred to as 'net oil production', includes (i) cost recovery oil (based upon the recoverable capital and operating costs incurred by Oil and Gas under each production sharing contract) and (ii) a percentage of profit oil (gross working-interest production remaining after cost recovery oil is allocated to Oil and Gas). Cost recovery pools for each production sharing contract include cumulative recoverable costs, subject to certification by CUPET, less cumulative proceeds from cost recovery oil allocated to Oil and Gas. Cost recovery revenue equals capital and operating costs eligible for recovery under the production sharing contracts. Therefore, cost recovery oil volumes increase as a result of higher capital expenditures and decrease when selling prices increase. When oil prices increase, the resulting reduction in cost recovery oil volumes is partially offset by an increase in profit oil barrels.

EBITDA for the quarter was comparable with the second quarter of 2006 and third quarter of 2005. Year-to-date EBITDA was \$13.3 million higher due to increased realized prices, partly offset by higher operating and administration costs resulting from inflationary cost pressures in the industry.

Total net production of 16,476 boepd reflects the impact of current oil prices, as well as, increased cost recoverable spending in the quarter. Production for the Spain and Pakistan assets continued to support the overall net barrel production.

During the third quarter of 2006, as many as eight drill rigs were active. Four rigs were drilling in the Santa Cruz field and four rigs were active in Canasi, Seboruco and Yumuri fields. During the quarter 6 wells were initiated, 5 wells completed with 3 being successful. Current production from these successful wells is just over 2,600 bpd.

In the quarter, a record was achieved when a 5,175 metre horizontal well was completed at Seboruco. Given the distance and complexity of this well, the achievement illustrates the technology and expertise that Sherritt has in Cuba. This achievement should allow for drilling initiatives to proceed on fields previously considered unreachable. Current production from this well is approximately 1,500 bpd.

Exploration drilling is progressing at Playa Larga. San Anton is still production testing; however, initial results indicate that there may be a limited reservoir.

At Varadero West, the electrical submersible pump that was placed earlier this year has performed without complications. Initial results are encouraging as normal production declines have reduced. Additional results are required before this technology can be deemed successful and applied on other producing wells.

Oil and Gas capital expenditures in the third quarter totalled \$30.0 million.

## Power

	Q3 2006	Q2 2006	Q1 2006	Q4 2005	Q3 2005	Nine months ended September 30	
						2006	2005
Electricity sold (000's of MWh) <sup>(1)</sup>	566	549	431	409	377	1,547	1,223
EBITDA (mm of \$)	\$ 20.8	\$ 20.7	\$ 15.1	\$ 14.4	\$ 18.7	\$ 56.6	\$ 53.3
Realized price per MWh	\$ 44.43	\$ 44.46	\$ 44.61	\$ 44.57	\$ 50.67	\$ 44.49	\$ 53.67
Capital Expenditures (mm of \$)	\$ 5.7	\$ 6.6	\$ 8.1	\$ 9.2	\$ 19.6	\$ 20.4	\$ 68.7

<sup>(1)</sup> Includes non-controlling interest.

Full-year production remains on track to surpass two million megawatt hours. Electricity generation in the third quarter was higher than previous quarters. This increase was the result of additional capacity from Phase 6, which came online at the beginning of 2006. The average tariff charged for power production declined for periods subsequent to the third quarter of 2005 as financing for all phases, except Phase 6, was repaid.

Availability in the quarter was 86% as planned maintenance on several units was conducted. As equipment continues to age, planned maintenance activities will lead to availability levels in the mid-to-high eighties.

Activities remain on track to commission both turbines of Phase 7 in the second quarter of 2007. When fully commissioned, power production capacity will be approximately 385 megawatts of electricity.

Capital expenditures for the third quarter were \$5.7 million, the majority of which can be attributed to Phase 7.

## Coal

	Q3 2006	Q2 2006	Q1 2006	Q4 2005	Q3 2005	Nine months ended September 30	
						2006	2005
<b>Coal</b>							
<b>EBITDA</b>							
Coal Valley and other coal development assets	\$ 0.6	\$ (0.4)	\$ (2.1)	\$ (4.2)	\$ (4.2)	\$ (1.9)	\$ (6.1)
Royal Utilities <sup>(1)</sup>	-	13.7	20.9	20.0	18.7	34.6	55.6
Total	0.6	13.3	18.8	15.8	14.5	32.7	49.5
<b>Equity-accounted earnings in Royal Utilities <sup>(1)</sup></b>							
	\$ 5.2	\$ -	\$ -	\$ -	\$ -	\$ 5.2	\$ -
<b>Distribution received from Royal Utilities <sup>(1)</sup></b>							
	\$ 10.0	\$ -	\$ -	\$ -	\$ -	\$ 10.0	\$ -
<b>Capital Expenditures</b>							
Coal Valley and other coal development assets	\$ 1.3	\$ 1.0	\$ 2.5	\$ 19.6	\$ 14.2	\$ 4.8	\$ 18.9
Royal Utilities <sup>(1)</sup>	-	2.6	0.6	1.9	3.7	3.2	6.1
Total	1.3	3.6	3.1	21.5	17.9	8.0	25.0
<b>Royal Utilities <sup>(2)</sup></b>							
Realized prices (\$/tonne)	\$ 12.45	\$ 12.63	\$ 11.31	\$ 11.10	\$ 11.10	\$ 12.10	\$ 10.98
Sales volumes (millions of tonnes) <sup>(4)</sup>	9.0	8.5	9.7	9.7	9.0	27.2	27.2
Production volumes (millions of tonnes) <sup>(4)</sup>	8.4	8.3	10.0	9.8	9.1	26.7	27.4
<b>Coal Valley <sup>(3)</sup></b>							
Realized prices (\$/tonne)	\$ 48.47	\$ 47.05	\$ 46.45	\$ 45.77	\$ 50.85	\$ 47.58	\$ 51.19
Sales volumes (millions of tonnes) <sup>(4)</sup>	0.6	0.4	0.3	0.1	0.2	1.3	0.6
Production volumes (millions of tonnes) <sup>(4)</sup>	0.5	0.4	0.4	0.1	0.1	1.3	0.6

<sup>(1)</sup> For all periods prior to June 27, 2006, the Corporation proportionately consolidated its 50% interest in Royal Utilities. Subsequent to June 27, 2006, the Corporation is equity-accounting for Royal Utilities.

<sup>(2)</sup> Royal Utilities include the two contract operations, five mine-mouth operations, and the Bienfait mine and Char plant.

<sup>(3)</sup> Coal Valley mine is primarily an export market mine.

<sup>(4)</sup> Coal Valley sales and production volumes are presented on a 50% basis. Royal Utilities sales and production volumes are presented on a 100% basis.

Royal Utilities sales volumes were 9.0 million tonnes (100% basis) for the third quarter in both 2006 and 2005. Realized prices per tonne (excluding royalty revenue) for the third quarter were \$12.45 in 2006 compared to \$11.10 in 2005. Higher realized prices were mostly offset by higher operating costs mainly due to increased fuel costs. The Corporation's share of equity accounted earnings from Royal Utilities was \$5.2 million for the third quarter of 2006 and distributions received were \$10.0 million. Sherritt owns 40.3 million Royal Utilities' units.

Coal Valley operations during the quarter reached several milestones as increased capacity translated into record production and sales. Production of 0.5 million tonnes in the quarter supported record coal sales of 0.6 million tonnes. Increased availability of rail sets and strong demand led to the significant quarter-over-quarter increases compared to the second quarter of 2006 and the third quarter of 2005.

Realized prices per tonne were up marginally compared to the second quarter of 2006 as higher US dollar export coal prices were offset by the strength of the Canadian dollar.

Coal Valley capital expenditures for the quarter were \$1.3 million.

## **Other**

Sherritt's soybean-based food processing business generated revenue of \$14.3 million and EBITDA of \$1.5 million in the third quarter as compared to revenue of \$20.9 million and EBITDA of \$1.5 million for the comparative quarter of 2005. The decrease in revenue was mostly due to lower realized prices and volumes which were offset by lower procurement and operating costs to record comparable EBITDA. Capital expenditures are estimated at \$1 million for 2006. Overall, this business continues to develop new products and uncover additional markets for its value-added products.

## Summary Financial Results by Segment (unaudited)

The tables on pages 13 and 14 present EBITDA and operating earnings from continuing operations by segment and reconciles these non-GAAP measures to earnings before income taxes. The Corporation discloses EBITDA in order to provide an indication of revenue less cash operating expenses. Operating earnings is a measure used by Sherritt to evaluate the operating performance of its businesses as it excludes interest charges, which are a function of the particular financing structure for the business, and certain other charges. EBITDA and operating earnings do not have any standardized meaning prescribed by Canadian generally accepted accounting principles and are, therefore, unlikely to be comparable with similar measures presented by other issuers.

All amounts in this interim report represent Sherritt's 100% interest unless otherwise indicated. Amounts relating to Metals and Coal Valley reflect the Corporation's 50% interest in these operations. Amounts relating to Coal reflect the Corporation's 50% proportionate interest in Royal Utilities up to June 27, 2006. Subsequent to June 27, 2006, the Corporation changed its accounting for Royal Utilities to the equity method. Sherritt holds a one-third interest in the Power business and a 49% interest in the soybean-based food processing business. The non-controlling interests are disclosed separately in the consolidated financial statements.

### Three months ended September 30, 2006

(\$ millions)	Coal <sup>(3)</sup>	Metals	Oil and Gas	Power	Other <sup>(1)</sup>	Corporate	Consolidated
Revenue	\$ 29.1	\$ 148.0	\$ 65.1	\$ 29.0	\$ 14.3	\$ -	\$ 285.5
Operating, selling, general and administrative	28.5	69.1	12.5	8.2	12.8	6.1	137.2
EBITDA	0.6	78.9	52.6	20.8	1.5	(6.1)	148.3
Depletion, amortization and accretion	2.1	5.1	22.5	6.3	0.6	1.1	37.7
Operating earnings (loss) from continuing operations	(1.5)	73.8	30.1	14.5	0.9	(7.2)	110.6
Share of earnings of equity investments <sup>(2)</sup>	5.2	-	-	-	-	-	5.2
Net financing expense							(6.0)
Income taxes							(30.3)
Non-controlling interests							(5.4)
Gain on disposition of investments							-
Net earnings							74.1
Capital expenditures	\$ 1.3	\$ 17.3	\$ 30.0	\$ 5.7	\$ -	\$ 1.0	\$ 55.3

<sup>(1)</sup> Other includes the consolidated results of the Corporation's soybean-based food processing business as a Variable Interest Entity under Accounting Guideline 15.

<sup>(2)</sup> Share of earnings of equity investments includes Royal Utilities and the tourism businesses.

<sup>(3)</sup> Coal includes Royal Utilities on proportionate consolidation basis up to June 27, 2006, and the Corporation's 50% proportionate interest in the Coal Valley export thermal coal mine and coal development assets.

### Three months ended September 30, 2005 (restated) <sup>(2)</sup>

(\$ millions)	Coal <sup>(3)</sup>	Metals	Oil and Gas	Power	Other <sup>(1)</sup>	Corporate	Consolidated
Revenue	\$ 64.8	\$ 86.6	\$ 60.8	\$ 24.2	\$ 20.9	\$ -	\$ 257.3
Operating, selling, general and administrative	50.3	52.3	8.7	5.5	19.4	21.0	157.2
EBITDA	14.5	34.3	52.1	18.7	1.5	(21.0)	100.1
Depletion, amortization and accretion	14.2	4.8	19.8	5.6	0.8	1.0	46.2
Operating earnings (loss) from continuing operations	0.3	29.5	32.3	13.1	0.7	(22.0)	53.9
Share of earnings of equity investments	-	-	-	-	-	0.1	0.1
Net financing expense							(5.3)
Income taxes							(15.2)
Non-controlling interests							(7.4)
Net earnings							26.1
Capital expenditures	\$ 17.9	\$ 10.8	\$ 27.9	\$ 19.6	\$ -	\$ 0.3	\$ 76.5

<sup>(1)</sup> Other includes the consolidated results of the Corporation's soybean-based food processing business as a Variable Interest Entity under Accounting Guideline 15.

<sup>(2)</sup> Comparable periods have been restated to reflect a change in the methodology of accounting for income taxes in the Cuban oil and gas business and the reclassification and adjustment of certain revenues, operating, selling, general and administrative costs in the Metals business.

<sup>(3)</sup> Coal results include the Corporations 50% proportionate interest in Royal Utilities, and the Corporation's 50% proportionate interest in the Coal Valley export thermal coal mine and the coal development assets.

## Nine months ended September 30, 2006

(\$ million)	Coal <sup>(3)</sup>	Metals	Oil and Gas	Power	Other <sup>(1)</sup>	Corporate	Consolidated
Revenue	\$ 176.1	\$ 351.1	\$ 203.4	\$ 79.6	\$ 43.2	\$ -	\$ 853.4
Operating, selling, general and administrative	143.4	195.8	39.9	23.0	39.3	26.7	468.1
EBITDA	32.7	155.3	163.5	56.6	3.9	(26.7)	385.3
Depletion, amortization and accretion	29.7	14.7	64.4	19.3	2.0	3.5	133.6
Operating earnings (loss) from continuing operations	3.0	140.6	99.1	37.3	1.9	(30.2)	251.7
Share of earnings of equity investments <sup>(4)</sup>	5.2	-	-	-	-	0.9	6.1
Net financing expense							(25.8)
Income taxes							(56.3)
Non-controlling interests							(13.7)
Gain on disposition of investments							5.0
Net earnings							167.0
Capital expenditures	\$ 8.0	\$ 45.3	\$ 86.7	\$ 20.4	\$ 0.9	\$ 1.1	\$ 162.4

## Nine months ended September 30, 2005 (restated) <sup>(2)</sup>

(\$ million)	Coal <sup>(3)</sup>	Metals	Oil and Gas	Power	Other <sup>(1)</sup>	Corporate	Consolidated
Revenue	\$ 193.0	\$ 330.8	\$ 178.9	\$ 76.5	\$ 57.7	\$ -	\$ 836.9
Operating, selling, general and administrative	143.5	184.9	28.7	23.2	51.7	35.7	467.7
EBITDA	49.5	145.9	150.2	53.3	6.0	(35.7)	369.2
Depletion, amortization and accretion	42.3	15.0	58.8	16.2	2.2	3.1	137.6
Operating earnings (loss) from continuing operations	7.2	130.9	91.4	37.1	3.8	(38.8)	231.6
Share of earnings of equity investments	-	-	-	-	-	0.6	0.6
Net financing expense							(34.1)
Income taxes							(60.7)
Non-controlling interests							(22.2)
Gain on disposition of investments							-
Net earnings							115.2
Capital expenditures	\$ 25.0	\$ 24.4	\$ 93.2	\$ 68.7	\$ 0.2	\$ 1.8	\$ 213.3

<sup>(1)</sup> Other includes the consolidated results of the Corporation's soybean-based food processing business as a Variable Interest Entity under Accounting Guideline 15.

<sup>(2)</sup> Comparable periods have been restated to reflect a change in the methodology of accounting for income taxes in the Cuban oil and gas business and the reclassification and adjustment of certain revenues, operating, selling, general and administrative costs in the Metals business.

<sup>(3)</sup> Coal results include the Corporations 50% proportionate interest in Royal Utilities for the nine months ended September 30, 2005 and up to June 27, 2006 for the nine months ended September 30, 2006, and the Corporation's 50% proportionate interest in the Coal Valley export thermal coal mine and the coal development assets.

<sup>(4)</sup> Share of earnings of equity investments includes Royal Utilities since June 28, 2006 and the tourism business.

## Supplementary Information

The tables below present EBITDA and operating earnings from continuing operations by segment and reconcile these non-GAAP measures to earnings before income taxes. The Corporation discloses EBITDA in order to provide an indication of revenue less cash operating expenses. Operating earnings is a measure used by Sherritt to evaluate the operating performance of its businesses as it excludes interest charges, which are a function of the particular financing structure for the business, and certain other charges. EBITDA and operating earnings do not have any standardized meaning prescribed by Canadian generally accepted accounting principles and are, therefore, unlikely to be comparable with similar measures presented by other issuers.

### Three months ended June 30, 2006

(\$ millions)	Coal <sup>(3)</sup>	Metals <sup>(2)</sup>	Oil and Gas	Power	Other <sup>(1)</sup>	Corporate	Consolidated
Revenue	\$ 73.2	\$120.3	\$ 69.6	\$ 28.4	\$ 15.1	\$ -	\$ 306.6
Operating, selling, general and administrative	59.9	74.0	14.9	7.7	13.9	11.4	181.8
EBITDA	13.3	46.3	54.7	20.7	1.2	(11.4)	124.8
Depletion, amortization and accretion	13.6	5.0	21.3	6.7	0.6	1.2	48.4
Operating earnings (loss)	(0.3)	41.3	33.4	14.0	0.6	(12.6)	76.4
Share of earnings of equity accounted investments							0.3
Net financing expense							(11.5)
Income taxes							(8.0)
Non-controlling interests							(5.0)
Gain on disposition of investments							5.0
Net earnings							57.2
Capital expenditures	\$ 3.6	\$ 12.9	\$ 33.0	\$ 6.6	\$ 0.4	\$ -	\$ 56.5

### Three months ended March 31, 2006

(\$ millions)	Coal <sup>(3)</sup>	Metals <sup>(2)</sup>	Oil and Gas	Power	Other <sup>(1)</sup>	Corporate	Consolidated
Revenue	\$ 73.8	\$ 82.8	\$ 68.7	\$ 22.2	\$ 13.8	\$ -	\$ 261.3
Operating, selling, general and administrative	55.0	52.7	12.5	7.1	12.6	9.2	149.1
EBITDA	18.8	30.1	56.2	15.1	1.2	(9.2)	112.2
Depletion, amortization and accretion	14.0	4.6	20.6	6.3	0.8	1.2	47.5
Operating earnings (loss)	4.8	25.5	35.6	8.8	0.4	(10.4)	64.7
Share of earnings of equity accounted investments							0.6
Net financing expense							(8.3)
Income taxes							(18.0)
Non-controlling interests							(3.3)
Net earnings							35.7
Capital expenditures	\$ 3.1	\$ 15.1	\$ 23.7	\$ 8.1	\$ 0.5	\$ 0.1	\$ 50.6

<sup>(1)</sup> Other includes the consolidated results of the Corporation's soybean-based food processing business as a Variable Interest Entity under Accounting Guideline 15.

<sup>(2)</sup> Comparable periods have been restated to reflect a change in the reclassification and adjustment of certain revenues, operating, selling, general and administrative costs in the Metals business.

<sup>(3)</sup> Coal results include the Corporation's 50% proportionate interest in Royal Utilities for the three months ended March 31, 2006 and up to June 27, 2006 for the three months ended June 30, 2006, and the Corporation's 50% proportionate interest in the Coal Valley export thermal coal mine and the coal development assets.

**Three months ended December 31, 2005 <sup>(2)</sup>**

(\$ millions)	Coal <sup>(3)</sup>	Metals	Oil and Gas	Power	Other <sup>(1)</sup>	Corporate	Consolidated
Revenue	\$ 62.7	\$ 98.0	\$ 58.6	\$ 22.0	\$ 17.4	\$ -	\$ 258.7
Operating, selling, general and administrative	46.9	77.5	9.5	7.6	17.2	6.8	165.5
EBITDA	15.8	20.5	49.1	14.4	0.2	(6.8)	93.2
Depletion, amortization and accretion	14.8	5.1	22.5	5.6	0.7	1.3	50.0
Operating earnings (loss)	1.0	15.4	26.6	8.8	(0.5)	(8.1)	43.2
Share of earnings of equity accounted investments							-
Net financing expense							(30.8)
Income taxes							2.6
Non-controlling interests							(5.9)
Net earnings							9.1
Capital expenditures	\$ 21.5	\$ 12.8	\$ 28.9	\$ 9.2	\$ 0.5	\$ 0.3	\$ 73.2

<sup>(1)</sup> Other includes the consolidated results of the Corporation's soybean-based food processing business as a Variable Interest Entity under Accounting Guideline 15.

<sup>(2)</sup> Comparable periods have been restated to reflect a change in the methodology of accounting for income taxes in the Oil and Gas to provide a clearer presentation of income taxes in that business. Certain selling expenses in Metals which were previously netted against revenue were reclassified to operating, selling and administrative costs.

<sup>(3)</sup> Coal results include the Corporation's 50% proportionate interest in Royal Utilities, and the Corporation's 50% proportionate interest in the Coal Valley export thermal coal mine and the coal development assets.

## **Management's Discussion and Analysis**

(all tabular dollar amounts expressed in millions of Canadian dollars, except per share amounts)

The following Management's Discussion and Analysis of the consolidated financial results of Sherritt International Corporation for the three and nine months ended September 30, 2006 should be read in conjunction with the unaudited consolidated financial statements and related notes contained in this interim report and the interim reports issued for the first and second quarter of 2006, as well as the Management's Discussion and Analysis, audited consolidated financial statements and related notes contained in the Corporation's 2005 annual report. Additional information relating to the Corporation, including the Corporation's 2005 Annual Information Form, is on SEDAR at [www.sedar.com](http://www.sedar.com) or on the Corporation's web site at [www.sherritt.com](http://www.sherritt.com). This Management's Discussion and Analysis is as of October 27, 2006.

### **Significant Transaction**

On September 13, 2006, the Corporation announced its third offer in 2006 to purchase a portion of its outstanding 7% convertible debentures due December 15, 2013 (the "Debentures"). Pursuant to this offer, \$50 million principal amount of debentures at a price of \$1,610 per \$1,000 principal, plus accrued interest, were purchased. The purchase was completed on October 23, 2006.

### **Change in Accounting for Royal Utilities**

The Corporation has prospectively changed the method of accounting for Royal Utilities Income Fund ("Royal Utilities") as a result of the initial public offering ("IPO") of Royal Utilities on June 27, 2006. Up to and including June 27, 2006, the Corporation proportionately consolidated its 50% interest in Royal Utilities. Subsequent to June 27, 2006, the Corporation is equity accounting for Royal Utilities.

On the consolidated statement of earnings, the proportionate consolidation method presented separately the Corporation's proportionate interest in the revenues and expenses of Royal Utilities. The change to the equity method of accounting results in the net revenues and expenses of Royal Utilities being reported as earnings of equity-accounted investments.

On the consolidated balance sheet, the change to the equity method of accounting resulted in reporting the net investment in Royal Utilities as a one-line item, as opposed to the Corporation's proportionate interest in the assets and liabilities of Royal Utilities.

The Corporation continues to proportionately consolidate its 50% interest in the Coal Valley mine and other coal development assets in Coal.

## Consolidated Earnings

Net earnings for the third quarter of 2006 were \$74.1 million or \$0.49 per share, compared to net earnings of \$26.1 million or \$0.17 per share for the third quarter of 2005. The increase in net earnings was mainly due to higher earnings in Metals from increased nickel prices and lower stock-based compensation costs resulting from the change in stock price and timing of vesting.

For the nine months ended September 30, 2006, net earnings of \$167.0 million or \$1.10 per share were higher than net earnings of \$115.2 million or \$0.77 per share for the comparable period last year. The increase was mainly due to higher earnings in Metals and Oil and Gas resulting from increased commodity prices and lower stock-based compensation costs. In addition, during the second quarter, the Corporation benefited from a one-time tax rate change, and recognized a \$4.7 million gain on disposition of its interest in Royal Utilities Income Fund ("Royal Utilities"), partly offset by a \$3.1 million loss on purchase of convertible debentures.

	<b>Q3 2006</b>	Q3 2005 (restated)	<b>Nine Months 2006</b>	Nine Months 2005 (restated)
Revenue	\$ <b>285.5</b>	\$ 257.3	\$ <b>853.4</b>	\$ 836.9

Consolidated revenues were \$28.2 million higher than the comparable third-quarter period of 2005, or \$83.4 million higher after adjusting for the change in accounting for Royal Utilities. The increase in revenue is mainly due to higher realized nickel prices in Metals, increased export sales volumes from Coal Valley and higher commodity prices and volumes in Oil and Gas. Consolidated revenue include \$nil revenue related to Royal Utilities for the three months ended September 30, 2006 (2005 - \$55.2 million).

Consolidated revenues were \$16.5 million higher than the comparable nine-month period of 2005, or \$62.3 million higher after adjusting for Royal Utilities. The increase is due to higher commodity prices in Metals and Oil and Gas and increased export sales volumes in Coal Valley. Metals revenue was positively driven by higher nickel prices and negatively impacted earlier in the year from process bottlenecks which have since been rectified. Consolidated revenue include \$116.2 million of revenue related to Royal Utilities for the nine months ended September 30, 2006 (2005 - \$162.0 million).

	<b>Q3 2006</b>	Q3 2005 (restated)	<b>Nine Months 2006</b>	Nine Months 2005 (restated)
Operating costs	\$ <b>121.7</b>	\$ 127.7	\$ <b>406.2</b>	\$ 404.2
Selling costs	<b>2.0</b>	2.2	<b>9.4</b>	9.2
General and administrative costs	<b>13.5</b>	27.3	<b>52.5</b>	54.3
Operating, selling, general and administrative costs	\$ <b>137.2</b>	\$ 157.2	\$ <b>468.1</b>	\$ 467.7

Operating costs were \$6.0 million lower than the comparable third-quarter period in 2005, or \$30.0 million higher after adjusting for Royal Utilities. The increase after adjustment is mainly due to higher operating costs in Metals and higher sales volumes from Coal Valley. Metals operating costs have increased as a result of higher repair and maintenance costs, combined with higher electricity, fuel oil and diesel costs. Consolidated operating costs include \$nil costs related to Royal Utilities for the three months ended September 30, 2006 (2005 - \$36.0 million).

Operating costs were \$2.0 million higher than the comparable nine-month period in 2005, or \$29.6 million higher after adjusting for Royal Utilities. The increase after adjustment is mainly due to higher export sales volumes from Coal Valley and higher operating costs in Metals as described above. Operating costs in Oil and Gas have also increased due to new wells, facilities and equipment, combined with general cost increases in the industry. Consolidated operating costs include \$76.6 million of costs related to Royal Utilities for the nine months ended September 30, 2006 (2005 - \$104.2 million).

Selling costs were consistent for both the three- and nine-month periods.

Lower general and administrative costs were mainly due to lower stock-based compensation costs. The decrease in the Corporation's share price and timing of vesting resulted in a \$3.5 million recovery for the three months ended September 30, 2006 compared to a \$14.5 million expense in the third quarter of 2005. For the nine months ended September 30, 2006, the Corporation recorded a \$0.1 million recovery compared to a \$14.2 million expense in 2005. The effect of lower stock-based compensation costs was partly offset by higher general and administrative costs in Oil and Gas mainly due to higher compensation costs.

	<b>Q3 2006</b>	Q3 2005 (restated)	<b>Nine Months 2006</b>	Nine Months 2005 (restated)
Depletion, amortization and accretion	\$ 37.7	\$ 46.2	\$ 133.6	\$ 137.6

Depletion, amortization and accretion were \$8.5 million lower than the comparable third-quarter period in 2005, or \$4.2 million higher after adjusting for Royal Utilities. The increase after adjustment is mainly due to higher depletion rates in Oil and Gas related to increased capital spending over the past two years, and higher depreciation in Power from the expansion. Consolidated depletion, amortization and accretion include \$nil costs related to Royal Utilities for the three months ended September 30, 2006 (2005 - \$12.7 million).

Depletion, amortization and accretion were \$4.0 million lower than the comparable nine-month period in 2005, or \$11.3 million higher after adjusting for Royal Utilities. The increase after adjustment is due to higher depletion in Oil and Gas and depreciation in Power as described above. Consolidated depletion, amortization and accretion include \$23.4 million of Royal Utilities costs for the nine months ended September 30, 2006 (2005 - \$38.7 million).

	<b>Q3 2006</b>	Q3 2005 (restated)	<b>Nine Months 2006</b>	Nine Months 2005 (restated)
Net financing expense	\$ 6.0	\$ 5.3	\$ 25.8	\$ 34.1

Net financing expense is mainly composed of interest income, interest expense and foreign exchange losses. Third-quarter net financing expense was \$0.7 million higher than the comparable period. Higher foreign exchange losses of \$4.2 million due to the strengthening of the Canadian dollar, were mostly offset by Power reinvestment credits received for the expansion and lower interest expense due to the redemption and purchase of debentures.

Net financing expense for the comparable nine-month periods were lower in 2006 due to a \$7.5 million decrease in interest expense, \$3.1 million of reinvestment credits received by Power and \$2.5 million decrease in foreign exchange losses. This was partly offset by a loss of \$3.1 million on purchase of convertible debentures during the second quarter.

	<b>Q3 2006</b>	Q3 2005 (restated)	<b>Nine Months 2006</b>	Nine Months 2005 (restated)
Share of earnings of equity-accounted investments	\$ 5.2	\$ 0.1	\$ 6.1	\$ 0.6

The Corporation's equity-accounted investments includes the investment in Royal Utilities from June 28, 2006 onward and the tourism businesses. The Corporation's equity earnings for the three- and nine-month periods increased due to the change in accounting for Royal Utilities.

	<b>Q3 2006</b>	Q3 2005 (restated)	<b>Nine Months 2006</b>	Nine Months 2005 (restated)
Effective tax rate	<b>28%</b>	31%	<b>24%</b>	31%

The effective tax rate was slightly lower between comparable third-quarter periods. The Corporation recognized tax assets during the quarter associated with the reorganization of the Coal business, thereby reducing the tax expense. However, this reduction was offset by the change in accounting for Royal Utilities to the equity method. The Corporation no longer includes a portion of Royal Utilities' tax provision in its consolidated tax expense as the equity earnings are net of tax. Instead, the Corporation records taxes on the distributions received.

The lower effective tax rate for the first nine months of 2006, as compared to the prior period, was mainly the result of tax-rate reductions by the Alberta and Federal governments, including the elimination of the Federal large corporations tax, as well as the recognition of tax assets associated with the reorganization of the Coal business. This reduction was partially offset by the change in accounting for Royal Utilities as described previously. Without the impact of the rate reductions and the reorganization of the Coal business, the Corporation's tax rate for the first nine months would have been approximately 33%.

	<b>Q3 2006</b>	Q3 2005 (restated)	<b>Nine Months 2006</b>	Nine Months 2005 (restated)
Non-controlling interests	\$ 5.4	\$ 7.4	\$ 13.7	\$ 22.2

Non-controlling interests reflects the two-thirds outside interest in the net earnings of a variable interest entity in Power. The decrease in non-controlling interest is primarily the result of the variable interest entity becoming taxable in Cuba on profits from the original 226 MW facilities, partly offset by increased earnings from the expansion completed early in 2006.

## Consolidated Cash Flow

	Q3 2006	Q3 2005 (restated)	Nine Months 2006	Nine Months 2005 (restated)
Cash from operating activities before working capital changes	\$ 99.3	\$ 74.2	\$ 269.2	\$ 269.3
Decrease (increase) in non-cash working capital changes	0.2	42.0	(46.1)	2.4
Cash provided by operating activities	\$ 99.5	\$ 116.2	\$ 223.1	\$ 271.7

Cash provided by operating activities before working capital changes increased for the three- and nine-month periods. The third quarter increase was primarily due to higher earnings from increased nickel commodity prices in Metals.

Cash provided by non-cash working capital of \$0.2 million in the third quarter of 2006, was mainly the result of increased accounts payable in Metals due to higher current taxes resulting from increased earnings and the timing of payments. This was mostly offset by higher accounts receivable in Metals mainly due to the timing of collection of nickel sales combined with higher realized nickel prices. In addition, inventory increased in Metals mainly due to the timing of fall fertilizer sales.

Cash used for non-cash working capital of \$46.1 million for the nine-month period resulted from increased accounts receivable arising from higher realized prices for nickel and oil and increased Metals inventory. Metals inventory increased due to higher nickel and cobalt volumes and the timing of fall fertilizer sales, combined with higher production costs resulting from increased electricity, fuel oil and diesel costs. This was partly offset by higher accounts payable in Metals due to higher current taxes resulting from increased earnings and the timing of payments.

	Q3 2006	Q3 2005 (restated)	Nine Months 2006	Nine Months 2005 (restated)
Capital expenditures	\$ 55.3	\$ 76.5	\$ 162.4	\$ 213.3
Cash provided by (used for) other investing activities	2.8	(137.8)	139.1	(133.9)
Cash provided by (used for) financing activities	(3.4)	(17.2)	(237.1)	14.7

Capitals expenditures in the third quarter were mainly in support of development and exploration drilling in Oil and Gas and the expansion of facilities in Metals. For the nine months ended September 30, 2006, in addition to the ongoing capital expenditures described previously, the Corporation completed the 85 MW Power expansion during the first half of the year.

Cash provided by other investing activities in the third quarter of 2006 was \$2.8 million. This mainly comprises \$10.0 million of distributions received from Royal Utilities, \$10.6 million from the exercise of the over-allotment option by the underwriters as part of the Royal Utilities IPO and \$1.6 million of distributions received from other investments, offset by a \$12.6 million increase in Other assets and a \$5.0 million increase in restricted cash associated with joint operations in Oil and Gas. Other assets related to increases in advances for the Metals expansion and progress payments for the Power expansion.

Cash provided by other investing activities for the nine months ended September 30, 2006, mainly relate to \$127.8 million of proceeds and distributions received as a result of the restructuring of Coal and the disposition of the interest in Royal Utilities, \$10.0 million of distributions received from Royal Utilities following the IPO, coupled with a decrease in short-term investments of \$40.1 million due to the timing in

maturations of these investments. Cash used for Other assets of \$30.6 million mainly relate to increased advances for the Metals expansion and progress payments for the Power expansion.

Cash used for financing activities for the third quarter of 2006, mainly relate to \$5.8 million of dividends paid to the non-controlling interests in Power and \$3.8 million of dividends paid to shareholders of Sherritt, partly offset by an increase in long-term debt.

For the nine months ended September 30, 2006, cash used for financing activities primarily relate to the purchase of \$107 million principal of 7% convertible debentures. The total cost on purchase was \$181.6 million. In addition, dividends of \$28.1 million were paid to the non-controlling interests in Power.

## **Consolidated Financial Position**

The consolidated financial position of the Corporation has changed significantly as a result of the IPO of Royal Utilities. This transaction resulted in the Corporation prospectively changing the method of accounting for this business from proportionate consolidation to equity accounting. The change to the equity method of accounting resulted in reporting the net investment of Royal Utilities as a one-line item on the balance sheet, whereas the proportionate consolidation separately presented the Corporation's proportionate interest in the assets and liabilities of Royal Utilities.

Total assets at September 30, 2006 were \$2.5 billion. Cash and cash equivalents, restricted cash and short-term investments totalled \$417.8 million at September 30, 2006, a decrease of \$67.4 million since year end. The cash decrease is mainly due to the purchase of \$107 million principal of 7% convertible debentures at a cost of \$181.6 million, capital expenditures of \$162.4 million, \$28.1 million of dividends paid to non-controlling interests, \$11.4 million of dividends paid to shareholders and a \$30.6 million increase in other advances and payments related to the expansion projects in Metals and Power. This was partly offset by \$128.2 million of proceeds received as a result of the restructuring and IPO of Royal Utilities combined with \$223.1 million of cash generated from operations.

Current advances and loans receivable of \$33.1 million remained relatively unchanged in the third quarter of 2006. Accounts receivable were \$308.7 million as at September 30, 2006, an increase of \$58.4 million increase since year end after adjusting for \$27.9 million of receivables related to Royal Utilities. Metals and Oil and Gas accounts receivable increased mainly due to higher realized prices for nickel and oil sales.

Oil and Gas accounts receivable include amounts due from oil sales to Cuban government agencies. For oil sales from its 100%-owned blocks, Oil and Gas provides extended credit terms (up to 180 days) with interest at 14% per annum after 90 days. These accounts receivable are secured by formal agreements under which Cuban government agencies have pledged certain taxes and other cash flows toward payment of Oil and Gas and Power receivables.

As at September 30, 2006, Oil and Gas accounts receivable included US\$26.8 million from oil sales to Cuban government agencies from a jointly-owned block. These accounts receivable are administered and collected by the joint operating partner.

Oil and Gas accounts receivable also include US\$39.0 million of cost recovery claims which are subject to approval by the Cuban agency pursuant to the Cuban production sharing contracts.

Metals accounts receivable include receivables from finished nickel and cobalt sales to customers primarily located in Europe and Asia, receivables from fertilizer sales to customers in Canada and receivables from by-product sales to China. Power and soybean-based food processing receivables include amounts due from Cuban government agencies. Coal Valley accounts receivable arise principally from sales of export coal to Asia and South America.

Inventories were \$111.9 million as at September 30, 2006, an increase of \$1.9 million since year end, or a \$20.5 million increase since year end after adjusting for \$18.6 million of inventory related to Royal

Utilities. The increase primarily relates to higher Metals inventory due to higher nickel and cobalt volumes and the timing of fall fertilizer sales, combined with increased production costs resulting from higher electricity, fuel oil and diesel costs.

Capital assets of \$1,035.5 million as at September 30, 2006 decreased by \$613.3 million compared with \$1,648.8 million as at December 31, 2005. The reduction in capital assets was primarily due to the change in accounting for Royal Utilities. Capital expenditures of \$162.4 million were mainly in support of development and exploration drilling in Oil and Gas and the expansion of facilities in Metals.

The Corporation and its joint venture partner have funding agreements with companies within the Metals business to finance the Metals expansion. Under these agreements, capital cost up to US\$500 million is to be funded equally by the Corporation and its joint venture partner. As at September 30, 2006, the proportionally consolidated loan from the joint venture partners was \$24.4 million.

The future tax asset (including current portion) of \$85.1 million at September 30, 2006 represented primarily the tax benefit of approximately of \$97.1 million of non-capital losses and \$141.7 million of capital losses. The non-capital losses have been generated primarily through interest on the Corporation's debt. The tax benefit of the losses has been recognized in the financial statements in the expectation that sufficient taxable income will be realized in the future to utilize these losses.

Investments of \$363.2 million as at September 30, 2006, comprised the Corporation's \$342.6 million equity investment in Royal Utilities and \$20.6 million equity investment in the tourism and other businesses. The increase from the year-end balance is due to the change in accounting for Royal Utilities.

Other assets were \$104.2 million as at September 30, 2006, compared with \$104.1 million at the end of 2005. Advances with respect to the Metals expansion increased \$18.9 million and progress payments for the Power expansion have increased by \$16.3 million. These increases were offset by the change in accounting for Other assets related to Royal Utilities, repayment of other loans receivable and amortization of deferred financing costs.

Short-term debt of \$52.8 million as at September 30, 2006 decreased by \$31.5 million from year end, of which \$29.0 million related to the change in accounting for Royal Utilities.

Accounts payable and accrued liabilities were \$205.6 million at the end of the third quarter, an increase of \$31.3 million from year end, or a \$46.3 million increase since year end after adjusting for \$15.0 million of payables related to Royal Utilities. Accounts payable have increased by \$25.3 million in Metals and \$8.0 million in Oil and Gas, mainly due to a combination of higher current taxes resulting from increased earnings and the timing of payments. In addition, Corporate accounts payable have increased mainly due to the timing of payments for interest and other payables.

The future income tax liability of \$69.1 million at September 30, 2006 decreased from the year-end amount of \$231.2 million. Almost all of the decrease relates to the change in accounting for Royal Utilities. The majority of the liability relates to the future income tax liability of the Oil and Gas business, which is not a current cash tax liability, but is a result of the temporary differences between the values of capital assets for tax purposes versus accounting purposes. The remainder of the future income tax liability is associated with the repatriation to Canada of untaxed profits in the Power business.

Long-term debt and other liabilities (including current portion) were \$523.7 million at the end of the third quarter compared with \$649.0 million at the end of 2005. The decrease is mainly attributable to the purchase of \$107 million of the 7% convertible debentures during the second quarter and the cash redemption of \$14.4 million on the remaining 9.875% senior unsecured debentures during the first quarter. These decreases were partially offset by an \$18.6 million increase in the Metals expansion loan.

Non-controlling interests reflects third-party interests in Energas. Energas is a variable interest entity in Power. The decrease in non-controlling interest from \$211.8 million as at December 31, 2005 to \$197.4 million as at September 30, 2006, relates to the payment of \$28.1 million of dividends to the non-controlling interests, partly offset by \$13.7 million of income attributed to non-controlling interests.

The cumulative translation account ("CTA") component of shareholders' equity relates to the change in the foreign currency translation method of certain foreign operations as described in notes 2 and 17 to the interim consolidated financial statements. The CTA balance of \$70.6 million represents the unrealized foreign exchange loss on the Corporation's net investment in its self-sustaining foreign operations of which \$47.7 million relates to the translation of the opening balances, mostly capital assets, and a translation loss of \$22.9 million related to the net foreign exchange change during the nine-month period.

During the quarter, the Corporation entered into capital leases for equipment totalling \$0.1 million.

During the quarter, the Board of Directors of the Corporation approved a quarterly dividend of \$0.025 per share payable October 13, 2006 to shareholders of record as at the close of business on September 30, 2006.

Under a normal-course issuer bid, which expired July 4, 2006, the Corporation acquired 200,000 shares at an average price of \$10.31 per share during the first quarter of 2006.

## Review of Operations

### Metals

Metals continues to focus on the low-cost production of finished nickel and cobalt through development of Cuba's extensive nickel resources. The Metals business, conducted through a joint venture with a Cuban company, mines, processes and refines nickel and cobalt for sale worldwide (except the United States of America) with mining operations and associated processing facilities in Moa, Cuba; refining facilities in Fort Saskatchewan, Alberta; and international marketing and sales operations.

### ***Outlook (refer to "Forward-looking Statements")***

Taking into consideration process bottlenecks experienced in prior quarters, full-year nickel production is expected to be approximately 30,000 tonnes (100% basis). This rate is expected to continue into the fourth quarter. Cobalt production for the year remains inline with initial expectations of approximately 3,000 tonnes (100% basis).

During the third quarter, Sherritt and its joint venture partner have agreed to modify the original expansion plans at Moa Nickel and Fort Saskatchewan for 16,000 tonnes per annum (100% basis) and proceed instead with a phased expansion. Phase 1 will result in 4,000 tonnes per annum (100% basis) of new production and is projected to be commissioned at the end of 2007. Phase 2 will be for approximately 9,000 tonnes per annum (100% basis) and is projected to be commissioned during 2009. Phase 3 is likely to include over 3,000 tonnes per annum (100% basis) of additional capacity and be commissioned during 2011. Delivery of Phase 1 production will come online prior to the original timeline outlined for the expansion. This decision to phase the expansion lowers execution risk and provides for an optimal utilization of available labour in Canada and Cuba for such projects.

Metals capital expenditures, adjusted to realign with the phased expansion, are expected to be \$41 million in the fourth quarter.

### ***Highlights***

- Record high nickel prices result in record operating earnings for the quarter
- Cobalt prices remain strong

	<b>Q3 2006</b>	Q3 2005 (restated)	<b>Nine Months 2006</b>	Nine Months 2005 (restated)
Revenue	\$ 148.0	\$ 86.6	\$ 351.1	\$ 330.8
Operating costs	(66.4)	(49.2)	(184.6)	(173.3)
Selling costs	(1.9)	(2.1)	(8.9)	(8.8)
General and administrative costs	(0.8)	(1.0)	(2.3)	(2.8)
EBITDA	78.9	34.3	155.3	145.9
Depletion, amortization and accretion	(5.1)	(4.8)	(14.7)	(15.0)
Operating earnings	\$ 73.8	\$ 29.5	\$ 140.6	\$ 130.9

Higher revenue between comparative third-quarter periods, reflects higher nickel sales and higher realized nickel prices, partly offset by the lower cobalt sales. Year-to-date revenue was higher than the comparative period as higher realized prices for nickel more than offset the impact of lower nickel and cobalt sales volumes and lower realized prices for cobalt.

Higher operating costs for the comparable third quarter and year-to-date periods was mainly the result of higher maintenance costs at the refinery, reflecting timing of the shutdown and additional repair on the reduction autoclaves during the quarter, combined with higher electricity, fuel oil and diesel costs.

Selling cost, general and administrative costs, depletion, amortization and accretion remain essentially unchanged from the same periods last year.

Prices	Q3 2006	Q3 2005 (restated)	Nine Months 2006	Nine Months 2005 (restated)
Nickel – realized (\$/lb)	\$ 14.42	\$ 8.02	\$ 10.96	\$ 8.68
Cobalt – realized (\$/lb)	17.77	17.64	16.24	19.62
Nickel – reference (US\$/lb)	13.24	6.61	9.69	7.00
Cobalt – reference (US\$/lb)	15.59	13.41	14.15	15.16

The quarter and year-to-date nickel reference prices continue to be driven by strong physical demand, uncertain supply and speculative interest.

During the quarter, cobalt reference prices reached their highest level since February 2005 mostly driven by high superalloy demand, decreased trading for heterogenite ore and higher prices posted by Internet sellers. On a year-to-date basis, increased global availability and inventory buildup in the first half of the year contributed to a slight decrease in the cobalt reference price compared to the same period last year.

Production (tonnes)	Q3 2006	Q3 2005 (restated)	Nine Months 2006	Nine Months 2005 (restated)
Mixed sulphides	4,029	4,116	11,248	12,458
Finished nickel	3,878	3,825	10,897	12,085
Finished cobalt	419	417	1,198	1,287

While unplanned maintenance activities impacted mixed sulphide production in the quarter, the process bottlenecks that affected production in the first half of the year have since been rectified. Finished nickel and cobalt production in the quarter was marginally ahead of production in the same quarter last year, but lower year-to-date mixed sulphide production impacted finished metal production. Securing cobalt-rich third-party feeds has helped to maintain finished cobalt production close to prior year levels.

Sales (thousands of pounds)	Q3 2006	Q3 2005 (restated)	Nine Months 2006	Nine Months 2005 (restated)
Finished nickel	8,795	7,619	24,291	26,289
Finished cobalt	879	955	2,663	2,768

Increased nickel sales for the quarter were achieved through higher nickel production and lower finished nickel inventories. Lower cobalt sales reflect timing of shipments close to quarter end.

Compared to last year, nickel and cobalt sales have been affected by lower production in the first half of this year. The impact on cobalt sales has been mitigated through purchase of third-party feeds.

	<b>Q3 2006</b>	Q3 2005 (restated)	<b>Nine Months 2006</b>	Nine Months 2005 (restated)
Capital expenditures	\$ 17.3	\$ 10.8	\$ 45.3	\$ 24.4

Quarter and year-to-date capital expenditures increased over the comparative periods as a result of increased spending associated with the expansion of the facilities at Moa and Fort Saskatchewan. Excluding the expansion, \$5.2 million and \$16.4 million were spent on sustaining, upgrading, compliance and environmental initiatives in the third quarter and the first nine months of 2006.

	<b>Q3 2006</b>	Q3 2005 (restated)	<b>Nine Months 2006</b>	Nine Months 2005 (restated)
Fertilizer sales (tonnes)	<b>7,614</b>	21,039	<b>107,830</b>	143,222
Revenue	\$ 3.1	\$ 6.8	\$ 35.8	\$ 45.0
Operating (loss) earnings	<b>(1.7)</b>	(2.3)	<b>1.3</b>	2.5

Weather resulted in a late start to fall fertilizer application, decreasing granular ammonium sulphate sales in the quarter compared to last year. Year-to-date sales were also impacted by lower granular ammonium sulphate demand in the spring and lower crystalline ammonium sulphate sales in the first quarter. Lower crystalline ammonium sulphate sales reflect the realignment of profitability on crystalline ammonium sulphate sales to the Metals Enterprise.

Revenues for the quarter reflect lower sales and lower netbacks compared to last year. Year-to-date, higher netbacks earlier in the year partly offset the impact of lower sales volumes.

Operating earnings in the quarter and year to date reflect the impact of lower revenue and the increased proportion of ammonia sales in the quarter, which carry a higher production cost than ammonium sulphate.

## Oil and Gas

Oil and Gas continues to focus its operations on exploration, development and production from offshore oil deposits in Cuba, which are drilled from nearby onshore locations using specialized skills in fold and thrust belt geology and directional drilling.

### **Outlook (refer to “Forward-looking Statements”)**

Gross working-interest oil production in Cuba is expected to remain relatively constant into the fourth quarter as new production from development drilling offsets natural reservoir declines. The outlook for net oil production for the remainder of 2006 is dependent on several factors, including gross working-interest production volumes, fuel oil reference prices and capital spending. Average gross working-interest production volumes for the year are expected to be approximately 30,500 boepd.

Sherritt applied in the third quarter for production from the Majaguillar block to be declared commercial. Majaguillar is expected to help oil production growth in 2007.

Oil and Gas capital expenditures are expected to be \$35 million in the fourth quarter.

### **Highlights**

- Continuing with full field development at Santa Cruz
- Application for commerciality on Majaguillar oil field in Block 9

	<b>Q3 2006</b>	Q3 2005 (restated)	<b>Nine Months 2006</b>	Nine Months 2005 (restated)
Revenue	\$ <b>65.1</b>	\$ 60.8	\$ <b>203.4</b>	\$ 178.9
Operating costs	<b>(7.4)</b>	(5.9)	<b>(25.9)</b>	(19.6)
General and administrative costs	<b>(5.1)</b>	(2.8)	<b>(14.0)</b>	(9.1)
EBITDA	<b>52.6</b>	52.1	<b>163.5</b>	150.2
Depletion, amortization and accretion	<b>(22.5)</b>	(19.8)	<b>(64.4)</b>	(58.8)
Operating earnings	\$ <b>30.1</b>	\$ 32.3	\$ <b>99.1</b>	\$ 91.4

Revenue increased between comparative third-quarter periods due to higher oil prices and cost recovery barrels, partly offset by the strengthening of the Canadian dollar. For the nine months ended September 30, 2006, higher revenue was due to record oil prices, partly offset by a decrease in production volumes, lower cost recoverable spending and the strengthening of the Canadian dollar.

Third-quarter operating costs increased between comparative third-quarter periods due to (i) new wells, facilities and equipment, including the Santa Cruz field, (ii) price increases for manpower, services and material inputs and (iii) renegotiation of service and equipment rates with Cuban agencies. For the same reasons, operating costs were higher for the comparative nine-month periods. A retroactive impact on operating costs was recognized during the second quarter of 2006, as the effective date for the renegotiated Cuban service and equipment rates was fiscal 2003.

Higher general and administrative costs for the third quarter were mainly due to higher compensation costs resulting from industry inflation, and higher cost allocations from other operators. For the same reasons, general and administrative costs for the year-to-date period increased by \$4.9 million compared with the same period last year.

For the third quarter of 2006, higher depletion, amortization and accretion costs were mainly due to higher depletion rates due to higher capital spending over the past two years. For the first nine months of 2006, the impact of higher depletion rates was partially offset by lower gross working-interest production volumes.

Prices	Q3 2006	Q3 2005 (restated)	Nine Months 2006	Nine Months 2005 (restated)
Realized prices :				
Cuba (\$/barrel)	\$ 41.88	\$ 39.65	\$ 43.40	\$ 34.74
Spain (\$/barrel)	77.32	73.46	75.53	66.04
Reference price (US\$/barrel)				
Gulf Coast Fuel Oil No. 6	46.38	39.88	47.11	34.43
Brent	68.97	61.76	66.59	53.50

The average realized prices for Cuban oil production increased by 5% from the same quarter last year and 25% for the comparative nine-month period. The impact of higher fuel oil reference prices was partially reduced by the strengthening of the Canadian dollar. Currently, all of the net oil production allocated to Oil and Gas under the Cuban production sharing contracts is sold to the state oil company ("CUPET"), generally at selling prices based on 79% to 83% of the Gulf Coast Fuel Oil No. 6 reference price.

Similarly, realized prices for production in Spain rose by 5% for the third quarter and by 14% for the year-to-date period due to the impact of higher Brent reference prices, partially reduced by the strengthening of the Canadian dollar. Natural gas selling prices in Pakistan are indexed to international crude oil prices. The indexed selling price is currently higher than the maximum selling price under the Company's long-term sales contract with an agency of the Government of Pakistan. There was no natural gas production from Pakistan during the comparable periods last year as the production came on-stream in April 2006.

Daily Production Volumes <sup>(1) (2)</sup>	Q3 2006	Q3 2005	Nine Months 2006	Nine Months 2005
Gross working-interest oil production in Cuba <sup>(3) (5)</sup>	<b>29,855</b>	29,600	<b>30,355</b>	31,257
Net oil production <sup>(4)</sup>				
Cuba (heavy oil)				
Cost recovery <sup>(5)</sup>	<b>6,480</b>	5,764	<b>6,616</b>	8,462
Profit oil <sup>(5)</sup>	<b>9,088</b>	<u>9,408</u>	<b>9,279</b>	<u>8,922</u>
Total	<b>15,568</b>	15,172	<b>15,895</b>	17,384
Spain (light / medium oil) <sup>(4)</sup>	<b>505</b>	569	<b>486</b>	498
Pakistan (natural gas) <sup>(4)</sup>	<b>403</b>	-	<b>261</b>	-
Total	<b>16,476</b>	15,741	<b>16,642</b>	17,882

- (1) Production figures exclude production from wells for which commerciality has not been established.
- (2) Oil production is stated in barrels per day ("bpd"). Natural gas production is stated in barrels of oil equivalent per day ("boepd"), which is converted at 6,000 cubic feet per boepd.
- (3) In Cuba, Oil and Gas delivers all of its gross working-interest oil production to CUPET at the time of production. Gross working-interest oil production excludes (i) production from wells for which commerciality has not been established in accordance with production sharing contracts; and (ii) working-interests of other participants in the production sharing contracts.
- (4) Net production (equivalent to net sales volume) represents the Corporation's share of gross working-interest production. In Spain and Pakistan, net oil production volumes equal 100% of gross working-interest production volumes.
- (5) Gross working-interest oil production is allocated between Oil and Gas and CUPET in accordance with production sharing contracts. CUPET's share is analogous to Crown royalty interests under Canadian hydrocarbon fiscal regimes. The Corporation's share, referred to as 'net oil production', includes (i) cost recovery oil (based upon the recoverable capital and operating costs incurred by Oil and Gas under each production sharing contract) and (ii) a percentage of profit oil (gross working-interest production remaining after cost recovery oil is allocated to Oil and Gas). Cost recovery pools for each production sharing contract include cumulative recoverable costs, subject to certification by CUPET, less cumulative proceeds from cost recovery oil allocated to Oil and Gas. Cost recovery revenue equals capital and operating costs eligible for recovery under the production sharing contracts. Therefore, cost recovery oil volumes increase as a result of higher capital expenditures and decrease when selling prices increase. When oil prices increase, the resulting reduction in cost recovery oil volumes is partially offset by an increase in profit oil barrels.

Gross working-interest oil production in Cuba typically decreases over time due to natural reservoir declines, which vary from field to field. Through its ongoing exploration and development programs, Oil and Gas expects to realize production increases from new oil wells and from workovers and other production enhancement initiatives. The Corporation's focus on exploration drilling in the second half of 2005 and early 2006 resulted in fewer new development wells coming into production during that period. The long-term benefits of the exploration program include commercialization of the Santa Cruz oil field in the first quarter of 2006 and the recent application for commercialization of the Majaguillar oil field, which the Corporation expects to be approved in early 2007.

For the comparative third-quarter periods, net production increased by 735 boepd due to higher production allocations from Cuban production sharing contracts and 403 boepd from the new Badar natural gas field in Pakistan. Production from the Casablanca platform in Spain decreased by 64 bpd due to natural reservoir declines. Gross working-interest production from Cuban oil fields was comparable to the same quarter in 2005, as renewed focus on development drilling resulted in new production that substantially offset natural reservoir declines. Oil and Gas realized an increase of 716 bpd in cost recovery oil from higher cost recoverable spending, partially offset by the impact of higher fuel oil prices. The increase in cost recovery barrels reduced the volume of profit oil available for allocation between CUPET and Oil and Gas. The increase in cost recoverable spending includes less exploration drilling in non-commercial blocks, higher operating costs and increased development drilling activity.

For the comparative nine-month periods, net oil production decreased by 1,240 boepd. Production allocated under the Cuban production sharing contracts decreased by 1,489 bpd, primarily due to lower gross working-interest oil production and the impact of higher fuel oil prices and non-recoverable exploration drilling on cost recovery barrels. The decrease in cost recovery oil was partially offset by an increase in profit oil. Gross working-interest oil production in Cuba was 3% lower than the same period last year due to natural reservoir declines, partially offset by retroactive oil production upon commercialization of the Santa Cruz oil field and by production from new oil wells. Production from the Badar gas field in Pakistan contributed 261 boepd while production from Spain decreased by only 12 bpd.

	<b>Q3 2006</b>	Q3 2005 (restated)	<b>Nine Months 2006</b>	Nine Months 2005 (restated)
Capital expenditures	\$ <b>30.0</b>	\$ 27.9	\$ <b>86.7</b>	\$ 93.2

Capital expenditures for the comparative third-quarter periods increased due to higher drilling activity, partially offset by strengthening of the Canadian dollar. As many as eight drilling rigs were active during the quarter, compared with six active rigs during the same period in 2005. Four rigs were drilling in the Santa Cruz field (45% working-interest) and the other four rigs drilled development wells in the Canasi, Seboruco and Yumuri fields. During the third quarter, six wells (3.2 net) were initiated, and four development wells (1.8 net) and one exploration well (1.0 net) were completed. In addition, Oil and Gas plans to continue testing and evaluating secondary production horizons encountered in the Playa Larga and San Anton exploration wells, which were drilled in the past year. However, initial results indicate that there may be a limited reservoir at San Anton.

For the nine months ended September 30, 2006, capital expenditures were lower than the same period in 2005. Although drilling activity increased with commercialization of the Santa Cruz field, capital spending on facility projects decreased year-over-year, and the strength of the Canadian dollar reduced capital expenditures denominated in US and Cuban currencies.

## **Power**

Power continues to focus on the effective utilization of energy resources in the production of electricity. Power is an advocate of the construction of electric generating facilities that derive both an economic and environmental benefit from processing natural gas produced in Cuba, which may otherwise be flared.

Power conducts business in Cuba through Energas S.A. ("Energas"), a Cuban entity in which Power holds a one-third equity interest. Each of two Cuban agencies also hold a one-third equity interest in Energas. Energas supplies electricity to one of these Cuban agencies under long-term fixed-price contracts. The other Cuban agency supplies natural gas to Energas at no cost.

Current production capacity of 311 megawatts (MW) will increase to 376 MW with the completion of a 65 MW expansion in the second quarter of 2007. As with previous facilities, Power will finance and construct the new facility.

Production from the 85 MW Phase 6 expansion completed in the first quarter of 2006 is sold at a tariff of US\$45 per MWh. Power's investment in this expansion, as well as the 65 MW Phase 7 expansion currently underway, will generate a reinvestment credit for Power of up to 30% of the amount invested. This reinvestment credit will be paid to Power by the Cuban state at the rate of one-third of Energas taxes paid. This equates to Power's share of Energas taxes.

### ***Outlook (refer to "Forward-looking Statements")***

Production for 2006 remains on track to surpass two million megawatt hours.

The first of two Phase 7 turbines for the 65 MW expansion at Boca de Jaruco is scheduled to be delivered in November, with the second turbine expected in January. Commissioning of both turbines is expected in the second quarter of 2007. The total cost of the project is estimated to be \$60 million, with approximately \$18 million to be spent in the fourth quarter.

As of September 2005, the tariff for the initial 226 MW of capacity decreased to US\$38 per megawatt hour as per the terms of the contract. The tariff for subsequent operations including Phase 6 (85 MW) and Phase 7 (65MW), is US\$45 per megawatt hour until financing provided by Sherritt for these phases is repaid. This financing is expected to be repaid by 2010, but the repayment period may be extended if subsequent expansions proceed. The full-year 2006 weighted-average tariff is expected to be approximately US\$39.50 per megawatt hour.

### ***Highlights***

- Third consecutive quarter with record production

As defined in Accounting Guideline AcG-15, Energas is a variable interest entity of which Power is the primary beneficiary. Accordingly, the results of Energas are shown on a consolidated basis and the two-thirds non-controlling interest in Energas are disclosed separately on the consolidated balance sheets and the statements of operations.

	<b>Q3 2006</b>	Q3 2005	<b>Nine Months 2006</b>	Nine Months 2005 (restated)
Revenue	\$ <b>29.0</b>	\$ 24.2	\$ <b>79.6</b>	\$ 76.5
Operating costs	<b>(8.1)</b>	(4.7)	<b>(22.1)</b>	(21.6)
General and administrative costs	<b>(0.1)</b>	(0.8)	<b>(0.9)</b>	(1.6)
EBITDA	<b>20.8</b>	18.7	<b>56.6</b>	53.3
Depletion, amortization and accretion	<b>(6.3)</b>	(5.6)	<b>(19.3)</b>	(16.2)
Operating earnings	\$ <b>14.5</b>	\$ 13.1	\$ <b>37.3</b>	\$ 37.1

Revenue for the third quarter and the nine months ended September 30, 2006 were higher than the comparative periods due to higher production as a result of increased capacity, partly offset by lower realized electricity prices. Revenue from the sale of by-products was \$3.8 million during the quarter (2005 - \$5.1 million) and \$10.8 million year to date (2005 - \$10.8 million). Lower third-quarter by-product revenue was due to a temporary increase in revenue during 2005 for the processing of natural gas.

Operating costs were higher for the comparable third-quarter periods, mainly due to the addition of the 85 MW expansion in the first quarter of 2006, the timing of maintenance work and increased freight and duty costs. Year-to-date operating costs reflect costs for the expansion while 2005 costs include a \$3.8 million reduction in an expected insurance recovery. Lower general and administrative costs in the third quarter and nine months ended September 30, 2006 were due to higher cost recoveries.

The increase in depletion, amortization and accretion for the third-quarter and year-to-date periods were due to the expansion completed in the first quarter of 2006.

	<b>Q3 2006</b>	Q3 2005	<b>Nine Months 2006</b>	Nine Months 2005
Realized prices (\$/MWh) <sup>(1)</sup>	\$ <b>44.43</b>	\$ 50.67	\$ <b>44.49</b>	\$ 53.67

<sup>(1)</sup> Megawatt hours ("MWh").

The tariff for electricity sales is fixed by long-term US dollar contracts. The tariff for electricity sold from the original 226 MW Power facilities decreased to US\$38 per MWh from US\$45 per MWh on September 1, 2005. The tariff for production from the 85 MW expansion is currently US\$45 per MWh. The decrease in realized prices was due to the reduction in the tariff in September 2005, combined with a stronger Canadian dollar.

	<b>Q3 2006</b>	Q3 2005 (restated)	<b>Nine Months 2006</b>	Nine Months 2005 (restated)
Electricity sold <sup>(1)</sup> (MWh)	<b>566,443</b>	377,014	<b>1,547,035</b>	1,222,731

<sup>(1)</sup> Including non-controlling interest's share

Electricity sales for the third quarter and nine months ended September 30, 2006 were higher than the comparative periods due to the addition of 85 MW of capacity during the first quarter of 2006.

	<b>Q3 2006</b>	Q3 2005 (restated)	<b>Nine Months 2006</b>	Nine Months 2005 (restated)
Capital expenditures	\$ 5.7	\$ 19.6	\$ 20.4	\$ 68.7

Capital expenditures thus far in 2006 have been primarily directed to the new 65 MW expansion project and the 85 MW expansion completed during the first quarter.

In addition to the amounts recorded as capital expenditures, Power incurred \$7.3 million during the quarter (\$16.6 million year to date) for progress payments, mainly in respect of equipment purchases for the expansion project. These expenditures are included in Other Assets in the investing section of the consolidated statement of cash flows. These assets will be reclassified to Capital assets when the Corporation takes possession of them.

## Coal

Coal includes the Corporation's 50% proportionate interest in the Coal Valley export thermal coal mine and coal development assets, and the Corporation's 50% proportionate interest in Royal Utilities up to June 27, 2006.

### **Outlook (refer to "Forward-looking Statements")**

Coal Valley is projected to maintain the record production levels that were achieved in the third quarter.

Sherritt is actively moving forward with the Dodds-Roundhill coal gasification project (formerly known as Camrose-Riley) and preliminary engineering has commenced. Negotiations have commenced with oxygen and gasification suppliers for the project. Negotiations have also begun with off-take customers for all syngas production from the first phase of the proposed four-stage project.

Preliminary engineering has begun for the first coal gasification complex in western Canada. Near surface coal reserves of approximately 500 million tonnes (equivalent to approximately nine trillion cubic feet of gas) have been earmarked for the proposed gasification project. Public consultations for the proposed Dodds-Roundhill mine were initiated in the third quarter and a preliminary disclosure document has been submitted to the Alberta government.

Sherritt intends to demonstrate that proven gasification technologies can be successfully deployed in western Canada. With approximately 12 billion tonnes of near surface coal reserves in this area, Sherritt believes that the potential exists to have its coal reserves revalued on an energy equivalent basis.

	<b>Q3 2006</b>	Q3 2005 (restated)	<b>Nine Months 2006</b>	Nine Months 2005 (restated)
Revenue	\$ <b>29.1</b>	\$ 64.8	\$ <b>176.1</b>	\$ 193.0
Operating costs	<b>(27.4)</b>	(48.9)	<b>(135.9)</b>	(139.5)
Selling costs	<b>(0.1)</b>	(0.1)	<b>(0.5)</b>	(0.4)
General and administrative costs	<b>(1.0)</b>	(1.3)	<b>(7.0)</b>	(3.6)
EBITDA	<b>0.6</b>	14.5	<b>32.7</b>	49.5
Depletion, amortization and accretion	<b>(2.1)</b>	(14.2)	<b>(29.7)</b>	(42.3)
Operating (loss) earnings	\$ <b>(1.5)</b>	\$ 0.3	\$ <b>3.0</b>	\$ 7.2
Equity-accounted earnings in Royal Utilities <sup>(1)</sup>	\$ <b>5.2</b>	\$ -	\$ <b>5.2</b>	\$ -

<sup>(1)</sup> The Corporation's share of earnings from its equity-accounted investment in Royal Utilities is from June 28, 2006 onwards.

The financial results for Coal have changed significantly due to the change in accounting for Royal Utilities from proportionate consolidation to equity accounting. For all periods up to and including June 27, 2006, Royal Utilities was proportionately consolidated. Subsequent to June 27, 2006, Royal Utilities is equity accounted.

Revenue was \$35.7 million lower between comparable third-quarter periods and \$16.9 million lower between comparable nine-month periods. Excluding the impact of Royal Utilities, revenue was \$19.5 million higher for the comparable third-quarter periods and \$28.9 million higher for the comparable nine-month periods. The increase in revenue, after adjusting for Royal Utilities, for both the three- and nine-month periods was mainly due to record sales volumes following the expansion in 2005, partly offset by the strengthening of the Canadian dollar.

Operating costs were \$21.5 million lower between comparable third-quarter periods and \$3.6 million lower between comparable nine-month periods. Excluding the impact of Royal Utilities, operating costs were \$14.5 million higher for the comparable third-quarter periods and \$24.0 million higher for the comparable nine-month periods. The increase in operating costs, after adjusting for Royal Utilities, was mainly due to higher sales volumes following the expansion in 2005.

Selling costs did not change significantly for the three- and nine-month periods.

General and administrative costs were \$0.3 million lower for the comparable third-quarter periods, or \$0.1 million higher after adjusting for Royal Utilities. For the comparable nine-month periods, general and administrative costs were \$3.4 million higher, or \$0.8 million higher after adjusting for Royal Utilities. The increase in general and administrative costs, after adjusting for Royal Utilities, is mainly due to higher project spending on the coal development assets.

Depletion, depreciation and accretion costs were \$12.1 million lower between comparable third-quarter periods and \$12.6 million lower between comparable nine-month periods. Excluding the impact of Royal Utilities, depletion, depreciation and accretion were \$0.6 million higher between the comparable third-quarter periods and \$2.7 million higher between the comparable nine-month periods. The increase, after excluding Royal Utilities, was mainly due to higher amortization resulting from the Coal Valley expansion.

Royal Utilities sales volumes were 9.0 million tonnes (100% basis) for the third quarter in both 2006 and 2005. Realized prices per tonnes (excluding royalty revenue) for the third quarter was \$12.45 in 2006 compared to \$11.10 in 2005. Higher realized prices were mostly offset by higher operating costs mainly due to increased fuel costs. The Corporation's share of equity-accounted earnings from Royal Utilities was \$5.2 million for the third quarter of 2006 and distributions received were \$10.0 million.

	<b>Q3 2006</b>	Q3 2005	<b>Nine Months 2006</b>	Nine Months 2005
Coal Valley <sup>(1)</sup>				
Realized prices (\$/tonne)	<b>\$ 48.47</b>	\$ 50.85	<b>\$ 47.58</b>	\$ 51.19
Sales volumes (millions of tonnes)	<b>0.6</b>	0.2	<b>1.3</b>	0.6
Production volumes (millions of tonnes)	<b>0.5</b>	0.1	<b>1.3</b>	0.6

<sup>(1)</sup> The Coal Valley mine is primarily an export market mine.

Although the current US dollar export coal price is strong, realized prices at Coal Valley for the three- and nine-month periods were lower than the comparable periods due primarily to a stronger Canadian dollar. However, as a result of the wash-plant expansion in 2005, sales and production volumes from Coal Valley have more than doubled which has led to significant increases in revenues.

	<b>Q3 2006</b>	Q3 2005 (restated)	<b>Nine Months 2006</b>	Nine Months 2005 (restated)
Capital expenditures	<b>\$ 1.3</b>	\$ 17.9	<b>\$ 8.0</b>	\$ 25.0

Capital expenditures were \$1.3 million in 2006 and \$14.2 million in 2005, for the comparable third-quarter periods, and \$4.8 million in 2006 and \$18.9 million in 2005, for the comparable nine-month periods, after adjusting for Royal Utilities. Capital expenditures at Coal Valley in 2006 mainly relate to permitting work and mining equipment and expenditures at the start of the year to support the final stages of the Coal Valley expansion. In 2005, capital expenditures were mainly in support of the expansion. Capital expenditures related to Royal Utilities were \$nil for the three months ended September 30, 2006 (2005 - \$3.7 million), and \$3.2 million for the nine months ended September 30, 2006 (2005 - \$6.1 million).

## Other

Other primarily comprises the consolidated results of the Corporation's soybean-based food processing business as a Variable Interest Entity under Accounting Guideline AcG-15.

### **Outlook (refer to "Forward-looking Statements")**

The soybean-based food processing business continues to pursue opportunities to maximize consumption of its products in Cuba by continuing to improve production facilities and optimizing the distribution of its products.

	<b>Q3 2006</b>	Q3 2005 (restated)	<b>Nine Months 2006</b>	Nine Months 2005 (restated)
Revenue	\$ <b>14.3</b>	\$ 20.9	\$ <b>43.2</b>	\$ 57.7
Operating costs	<b>(12.4)</b>	(19.0)	<b>(37.7)</b>	(50.2)
General and administrative costs	<b>(0.4)</b>	(0.4)	<b>(1.6)</b>	(1.5)
EBITDA	<b>1.5</b>	1.5	<b>3.9</b>	6.0
Depletion, amortization and accretion	<b>(0.6)</b>	(0.8)	<b>(2.0)</b>	(2.2)
Operating earnings	\$ <b>0.9</b>	\$ 0.7	\$ <b>1.9</b>	\$ 3.8

Lower revenues for comparable three- and nine-month periods, were due to lower realized sales prices, a stronger Canadian dollar and slightly lower sales volumes.

Operating costs for the comparable three- and nine-month periods were due to lower soybean procurement costs and lower sales volumes.

General and administrative costs, depletion, amortization, and accretion, did not change significantly between comparable third-quarter and year-to-date periods.

## Summary of Quarterly Results (unaudited)

The following table presents a summary of the segments and consolidated operating results for each of the eight quarters from December 2004 to September 2006.

(millions of dollars, except per share amounts)	Quarter Ended							
	September 2006	June 2006 <sup>(2)</sup>	March 2006 <sup>(2)</sup>	December 2005	September 2005 <sup>(1)</sup>	June 2005 <sup>(1)</sup>	March 2005 <sup>(1)</sup>	December 2004 <sup>(1)</sup>
Revenue								
Coal	\$ 29.1	\$ 73.2	\$ 73.8	\$ 62.7	\$ 64.8	\$ 65.3	\$ 62.9	\$ 65.4
Metals	148.0	120.3	82.8	98.0	86.6	143.3	100.9	109.5
Oil and Gas	65.1	69.6	68.7	58.6	60.8	67.7	50.4	45.9
Power	29.0	28.4	22.2	22.0	24.2	26.6	25.7	23.5
Other	14.3	15.1	13.8	17.4	20.9	19.6	17.2	20.3
	\$ 285.5	\$ 306.6	\$ 261.3	\$ 258.7	\$ 257.3	\$ 322.5	\$ 257.1	\$ 264.6
Earnings from continuing Operations	\$ 74.1	\$ 57.2	\$ 35.7	\$ 9.1	\$ 26.1	\$ 53.7	\$ 35.4	\$ 25.8
Net earnings	74.1	57.2	35.7	9.1	26.1	53.7	35.4	27.5
Earnings from continuing operations per share								
Basic	0.49	0.38	0.24	0.06	0.17	0.35	0.25	0.18
Diluted	0.43	0.36	0.20	0.05	0.15	0.29	0.21	0.15
Earnings per share								
Basic	0.49	0.38	0.24	0.06	0.17	0.35	0.25	0.19
Diluted	0.43	0.36	0.20	0.05	0.15	0.29	0.21	0.16

<sup>(1)</sup> Restated – see note 2 of the Interim Consolidated Financial Statements.

<sup>(2)</sup> Metals revenues have been restated, with a corresponding adjustment to operating, selling, general and administrative expense, to reclassify certain revenues netted against cost of sales.

The analysis of financial results for the last eight quarters is generally consistent with the consolidated financial results and selected interim information presented previously in this document. Further details in respect of historical quarterly results can be found in the Corporation's quarterly reports filed on SEDAR at [www.sedar.com](http://www.sedar.com) or on the Corporation's web site at [www.sherritt.com](http://www.sherritt.com).

## Accounting Changes

### *Investments*

The results for Coal reflected the Corporation's 50% proportionate interest in Royal Utilities up to June 27, 2006. Subsequent to June 27, 2006, the Corporation changed its accounting for Royal Utilities to the equity method of accounting. The Corporation will continue to proportionately consolidate its 50% interest in the Coal Valley export thermal coal mine, various non-producing coal mines, certain coal and potash resources and other non-mining assets, that continue to be held jointly by Sherritt and Ontario Teachers'.

### *Translation of foreign currencies*

The method of translation of foreign operations depends on whether the foreign operations are integrated or self-sustaining. Prior to January 1, 2006, all of the Corporation's foreign operations were considered integrated and translated into Canadian dollars using current rates of exchange for monetary assets and liabilities, historical rates of exchange for non-monetary assets and liabilities and average rates of exchange for revenues and expenses, except depletion and amortization which are translated at the rates of exchange applicable to the related assets. Gains and losses resulting from these translation adjustments are included in income.

The ongoing review of the economic factors to be considered in determining whether foreign operations are integrated or self-sustaining has resulted in the determination that the Metals foreign operations and the Oil and Gas foreign operations in Cuba and Spain have changed to self-sustaining. This change was made as a result of the increasing proportion of operating, financing and investing transactions of these foreign operations that are denominated in currencies other than the Canadian dollar. This change in method was effective at January 1, 2006 and was applied prospectively. The self-sustaining operations are translated into Canadian dollars using the current-rate method, whereby assets and liabilities are translated at period-end exchange rates while revenues and expenses are converted using average rates for the period. Gains and losses on translation to Canadian dollars relating to self-sustaining operations are deferred and included in a separate component of shareholders' equity described as cumulative translation account.

### *Future income taxes*

On October 1, 2005, the Corporation changed its methodology of accounting for income taxes in its Cuban oil and gas operations to provide a clearer presentation of income taxes in that operation. Prior to this change in accounting policy, the Corporation recorded tax on the Cuban oil and gas operations on the basis that cost recovery revenue and expenses were not subject to or deductible under the Cuban tax regime resulting in no temporary differences between the book value and the tax value of the relevant assets and liabilities. This methodology resulted in significant fluctuations in the effective tax rate for the Oil and Gas operations between reporting periods when the relative percentage of cost recovery revenue changed compared to total oil revenue.

Under the newly adopted accounting policy, temporary differences are recognized for the respective assets and liabilities at the effective Cuban tax rate of approximately 30%. This results in a clearer presentation of the effective tax rate in the Cuban oil operations over the life of the operating oil fields. The Corporation has implemented this change on a retroactive basis with restatement of prior periods. The cumulative effect of the change in policy on retained earnings at January 1, 2005 was \$40.3 million. The accounting change resulted in an increase in net earnings of \$3.0 million (increase in EPS – basic and diluted \$0.02) and \$0.6 million (increase in EPS –basic and diluted \$nil) for the three and nine months ended September 30, 2005.

The Corporation also changed the methodology of accounting for income taxes paid on its behalf by an agency of the government of Cuba for the enhanced oil recovery blocks, to reflect these income taxes on a gross basis. As a result, current income tax expense and revenue have increased. This change was applied on a retroactive basis and resulted in an increase in revenue and current income tax expense of \$1.2 million and \$2.7 million for the three and nine months ended September 30, 2005, respectively.

### ***Comparative Amounts***

Certain comparative amounts have been restated to correct their classification, with no impact on net earnings, to conform to the presentation in the current period.

In the Metals business, certain selling expenses which were previously netted against revenue, have been reclassified to operating, selling, general and administrative expenses, resulting in an increase in revenue of \$2.7 million and \$5.4 million for the three- and nine-month periods ended September 30, 2005, respectively. For the three months ended March 31, 2006 and June 30, 2006, revenue reclassification resulted in an increase of \$1.6 million and \$9.8 million in revenues, respectively, with a corresponding increase in operating, selling, general and administration expenses.

Capital expenditures on the Consolidated Statements of Cash Flow in 2005 have been adjusted for non-cash capital addition of \$6.0 million and \$1.5 million for the three and nine months ended September 30, 2005, respectively.

### ***Accounting Pronouncements***

#### *Financial Instruments – Recognition and Measurement*

The Canadian Institute of Chartered Accountants (the "CICA") issued Handbook Section 3855, Financial Instruments – Recognition and Measurement in April 2005. This pronouncement establishes standards for recognizing and measuring financial assets, financial liabilities and non-financial derivatives. Under this standard, an entity would recognize a financial asset or liability only when the entity becomes party to the contractual provisions of the financial instrument. Financial assets and financial liabilities would, with certain exceptions, be initially measured at fair value. Gains and losses on financial instruments measured at fair value would be recognized in net income in the periods in which they arise, with the exception of certain gains and losses on financial assets classified as available for sale (which are recognized in other comprehensive income) and certain financial instruments that are part of a designated hedging relationship (which qualify for special accounting in accordance with Hedges, CICA Handbook Section 3865).

#### *Hedges*

The CICA issued Handbook Section 3865, Hedges in April 2005. This pronouncement establishes standards for when and how hedge accounting may be applied. Hedge accounting is a method for recognizing the gains, losses, revenues and expenses associated with the items in a hedging relationship such that those gains, losses, revenues and expenses are recognized in net income in the same period when they would otherwise be recognized in different periods. The application of hedge accounting is optional.

## *Comprehensive Income*

The CICA issued Handbook Section 1530, Comprehensive Income in April 2005. The pronouncement establishes standards for the reporting and presentation of comprehensive income. Comprehensive income is the change in equity (net assets) of an enterprise during a period from transactions and other events and circumstances from non-owner sources, except those resulting from investments by owners and distributions to owners. Other comprehensive income is revenues, expenses, gains and losses that are recognized in comprehensive income, but excluded from net income. Disclosures required under this section include net income for the period, other comprehensive income for the period classified by its nature, reclassification from other comprehensive income to net income and the tax impact of each component of other comprehensive income.

## *Equity*

The CICA issued Handbook Section 3251, Equity in January 2005. This pronouncement establishes standards for the presentations of equity and the changes in equity. An enterprise should present separately the following components of equity: retained earnings, accumulated other comprehensive income by component, the total of retained earnings and accumulated other comprehensive income, contributed surplus, share capital and reserves.

The new standards for financial instruments, hedges, comprehensive income and equity apply to interim and annual financial statements relating to fiscal years beginning on or after October 1, 2006, for which early adoption is permitted. The adoption of these pronouncements must be done concurrently. The Corporation is currently assessing the impact of these standards, which are expected to be adopted by the Corporation on January 1, 2007.

## *Non-monetary Transactions*

In June 2005, the CICA issued Handbook Section 3831, Non-Monetary Transactions, which establishes that all non-monetary transactions be measured at their fair value unless, generally, they lack commercial substance or their fair value is not reliably measurable. This new Section is effective for non-monetary transactions initiated in periods beginning on or after January 1, 2006. The adoption of this standard did not have a material impact on the interim consolidated financial statements.

## *EIC 156 – Accounting by a Vendor for Consideration Given to a Customer*

In September 2005, the Emerging Issues Committee of the CICA issued EIC-156 "Accounting by a Vendor for Consideration Given to a Customer (Including a Reseller of the Vendor's Products)". EIC-156 addresses the classification, in the financial statements of a vendor, of considerations (including sales incentives such as discounts, rebates, "free" product/services and other similar arrangement) given to its customer. Its provisions determine whether a consideration is to be treated as an adjustment of the selling price or as a cost incurred by the vendor to sell goods or services. It also establishes the time at which such an amount should be recorded and the appropriate evaluation procedure. This EIC is effective for fiscal years beginning on or after January 1, 2006 and must be applied retroactively, with appropriate adjustments to preceding financial statements. The adoption of this abstract did not have a material impact on the interim consolidated financial statements.

## *EIC 157 – Implicit Variable Interest under AcG-15*

In October 2005, the Emerging Issues Committee of the CICA issued EIC-157, "Implicit Variable Interests under AcG-15", which must be applied by the Corporation in the first interim period beginning subsequent to October 17, 2005. Under AcG-15, an enterprise holding an interest in a variable interest entity has to consolidate that entity if the interest it holds exposes the enterprise to the majority of the entity's risks or rewards. EIC-157 clarifies that such interests do not have to be explicit and may be inferred from particular facts and circumstances. Such implicit variable interests must be evaluated in accordance with

AcG-15 to determine if consolidation is appropriate. The adoption of this abstract did not have a material impact on the interim consolidated financial statements.

#### *EIC 159 – Conditional Asset Retirement Obligations*

In December 2005, the Emerging Issues Committee of the CICA issued EIC-159, "Conditional Asset Retirement Obligations". EIC-159 clarifies that the term "conditional asset retirement obligation", as used in CICA Section 3110 "Asset Retirement Obligations", refers to a legal obligation to perform an asset retirement activity in which the timing and/or method of settlement are conditional on a future event that may or may not be within the control of the entity. The accounting treatment in this Abstract should be applied retroactively, with restatement of prior periods, to all financial statements for interim and annual reporting periods ending after March 31, 2006, although earlier adoption is encouraged. The adoption of this abstract did not have a material impact on the interim consolidated financial statements.

#### *EIC 160 – Stripping Costs Incurred in the Production Phase of a Mining Operation*

In March 2006, the Emerging Issues Committee of the CICA issued EIC-160, "Stripping Costs Incurred in the Production Phase of a Mining Operation". EIC-160 clarifies that stripping costs should be accounted for according to the benefit received by the entity. Generally, stripping costs should be accounted for as variable production costs that should be included in the costs of the inventory produced (that is, extracted) during the period that stripping costs are incurred. However, stripping costs should be capitalized if the stripping activity can be shown to represent a betterment to the mineral property. Capitalized stripping costs should be amortized in a rational and systematic manner over the reserves that directly benefit from the specific stripping activity, such as the unit of production method. The accounting treatment in this Abstract should be applied to stripping costs incurred in fiscal years beginning on or after July 1, 2006, and may be applied retroactively. The adoption of this abstract did not have a material impact on the interim consolidated financial statements.

#### *EIC 161 – Discontinued Operations*

In April 2006, the Emerging Issues Committee of the CICA issued EIC-161, "Discontinued Operations". EIC-161 addresses the allocation of interest expense to discontinued operations based on the principal amount of debt that will or could be paid with the proceeds from the sale of such operations. EIC-161 also specifies that general corporate overhead expenses may not be allocated to discontinued operations. EIC-161 applies to all disposal transactions initiated after the date of issuance of EIC-161 and may be applied prospectively or retroactively. The adoption of this abstract did not have a material impact on the interim consolidated financial statements.

#### *EIC 162 - Stock-based Compensation for Employees Eligible to Retire Before the Vesting Date*

In July 2006, the Emerging Issues Committee of the CICA issued EIC-162 "Stock-based compensation for employees eligible to retire before the vesting date". EIC-162 clarifies the accounting of compensation costs relating to a stock-based award granted to employees who either are eligible for retirement at the grant date or will be eligible before the end of the vesting period. EIC-162 specifies that the compensation cost attributable to the first case should be recognized on the grant date and that the compensation cost attributable to the second case should be recognized over the period from the grant date to the date the employee becomes eligible to retire. The accounting treatment in this Abstract is to be applied retroactively, with restatement of prior periods, to all stock-based compensation awards accounted for in accordance with Section 3870 in financial statements issued for interim and annual periods ending on or after December 31, 2006, although earlier adoption is encouraged. The adoption of this standard did not have a material impact on the interim consolidated financial statements.

## *EIC 163 – Determining the Variability to be Considered in Applying AcG-15*

In September 2006, the Emerging Issues Committee of the CICA issued EIC-163 “Determining the variability to be considered in applying AcG-15”. An entity may enter into an arrangement, such as a derivative contract, to either reduce or eliminate a) the variability created by certain assets or operations of the entity; or b) mismatches between the overall asset and liability profiles of the entity, thereby protecting certain liability and equity holders from exposure to such variability. EIC-163 clarifies that variability to be considered in applying AcG-15 shall be based on an analysis of the design of the entity. The adoption of this abstract did not have a material impact on the interim consolidated financial statements.

### **Critical Accounting Estimates**

The preparation of financial statements requires the Corporation to estimate the effect of various matters that are inherently uncertain as of the date of the financial statements. Each of these required estimates varies with respect to the level of judgment involved and the potential impact on the Corporation’s reported financial results. Estimates are deemed critical when the Corporation’s financial condition, change in financial condition or results of operations would be materially impacted by a different estimate or a change in estimate from period to period. The Corporation’s significant accounting policies, including critical accounting policies that require critical accounting estimates are discussed in note 2 of the 2005 Consolidated Financial Statements.

### **Off Balance Sheet Arrangements**

#### *Financial Instruments*

As at September 30, 2006, the Corporation had no outstanding foreign exchange or commodity options, futures or forward contracts.

### **Transactions with Related Parties**

Subsidiaries of the Corporation provide goods, labour, advisory and other administrative services to joint ventures at cost, commercial rates and other various contractual terms. The Corporation and its subsidiaries also market, pursuant to sales agreements, all of the cobalt, a portion of the nickel and certain by-products produced by certain jointly-owned entities in the Metals business.

The total value of all goods and services, including labour services, that the Corporation and its subsidiaries provided to joint ventures in the third quarter of 2006 amounted to \$29.7 million (2005 - \$14.4 million) and for the nine months ended September 30, 2006 was \$75.4 million (2005 - \$34.4 million). The total value of goods and services purchased from affiliates in the third quarter of 2006 was \$nil (2005 - \$nil million) and for the nine months ended September 30, 2006 was \$12.9 million (2005 - \$1.5 million).

Accounts receivable from joint ventures at September 30, 2006, totalled \$9.3 million (2005 - \$4.4 million). Accounts payable to joint ventures at September 30, 2006 totalled \$8.9 million (2005 - \$2.1 million).

### **Contractual Obligations and Commitments**

The Corporation is committed to purchases of equipment and services in the amount of \$72.1 million. As the Power and Metals expansions progress, the Corporation expects to enter into additional commitments.

## **Additional Information**

### *Share Capital*

As at September 30, 2006 and October 27, 2006, the Corporation had 151,697,109 common shares outstanding.

If all of the 7% convertible unsecured subordinate debentures were converted into shares at the option of the holders, up to 27,438,429 additional shares would be issued on or before December 14, 2013.

### **Disclosure Controls and Procedures**

As of the end of the period covered by this quarterly report, management, with the participation of the certifying officers, has evaluated the effectiveness of the Corporation's disclosure controls and procedures (as defined by the Canadian Securities Administrators). Based on that evaluation, the certifying officers have concluded that such disclosure controls and procedures are effective to provide reasonable assurance that material information relating to the Corporation and its subsidiaries is made known to them by others within those entities.

## Consolidated Balance Sheets

[\$ millions]	September 30 2006 (unaudited)	December 31 2005
<b>ASSETS</b>		
<b>Current assets</b>		
Cash and cash equivalents	\$ 399.9	\$ 437.6
Restricted cash	16.1	5.9
Short-term investments	1.8	41.7
Advances and loans receivable	33.1	34.4
Accounts receivable	308.7	278.2
Inventories	111.9	110.0
Overburden removal costs	0.6	2.4
Prepaid expenses	13.2	9.9
Future income taxes	28.5	10.9
	<b>913.8</b>	<b>931.0</b>
<b>Capital assets</b>	<b>1,035.5</b>	<b>1,648.8</b>
<b>Investments (note 4)</b>	<b>363.2</b>	<b>21.4</b>
<b>Future income taxes</b>	<b>56.6</b>	<b>85.2</b>
<b>Other assets</b>	<b>104.2</b>	<b>104.1</b>
	<b>\$ 2,473.3</b>	<b>\$ 2,790.5</b>
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
<b>Current liabilities</b>		
Short-term debt	\$ 52.8	\$ 84.3
Accounts payable and accrued liabilities	205.6	174.3
Long-term debt and other long-term liabilities (note 6)	9.1	28.2
Asset retirement obligations (note 7)	2.2	8.8
	<b>269.7</b>	<b>295.6</b>
<b>Long-term debt and other long-term liabilities (note 6)</b>	<b>514.6</b>	<b>620.8</b>
<b>Asset retirement obligations (note 7)</b>	<b>53.6</b>	<b>72.8</b>
<b>Future income taxes</b>	<b>69.1</b>	<b>231.2</b>
<b>Non-controlling interests</b>	<b>197.4</b>	<b>211.8</b>
	<b>1,104.4</b>	<b>1,432.2</b>
<b>Shareholders' equity</b>		
Convertible debentures	8.1	12.6
Capital stock (note 8)	784.2	781.7
Contributed surplus (note 10)	191.9	192.3
Cumulative translation account (note 17)	(70.6)	-
Retained earnings	455.3	371.7
	<b>1,368.9</b>	<b>1,358.3</b>
	<b>\$ 2,473.3</b>	<b>\$ 2,790.5</b>

## Consolidated Statements of Operations (unaudited)

[\$ millions]	Three months ended September 30		Nine months ended September 30	
	2006	2005 (restated-note 2)	2006	2005 (restated-note 2)
<b>Revenue</b>	\$ 285.5	\$ 257.3	\$ 853.4	\$ 836.9
Operating, selling, general and administrative	137.2	157.2	468.1	467.7
<b>Earnings before undernoted items</b>	<b>148.3</b>	<b>100.1</b>	<b>385.3</b>	<b>369.2</b>
Depletion, amortization and accretion	37.7	46.2	133.6	137.6
Net financing expense (note 11)	6.0	5.3	25.8	34.1
Gain on disposition of investments (note 3)	-	-	(5.0)	-
Share of earnings of equity accounted investments	(5.2)	(0.1)	(6.1)	(0.6)
Earnings before income taxes and non-controlling interests	109.8	48.7	237.0	198.1
Income taxes (note 12)	30.3	15.2	56.3	60.7
Non-controlling interests	5.4	7.4	13.7	22.2
<b>Net earnings</b>	<b>\$ 74.1</b>	<b>\$ 26.1</b>	<b>\$ 167.0</b>	<b>\$ 115.2</b>
<b>Earnings per share (note 8)</b>				
Basic	\$ 0.49	\$ 0.17	\$ 1.10	\$ 0.77
Diluted	0.43	0.15	1.00	0.64
<b>Weighted average number of shares (millions of shares)</b>				
Basic	151.3	155.2	151.3	149.6
Diluted	179.1	199.8	179.2	199.0

## Consolidated Statements of Retained Earnings (unaudited)

[\$ millions]	Three months ended September 30		Nine months ended September 30	
	2006	2005 (restated-note 2)	2006	2005 (restated-note 2)
Beginning of period, as previously reported	\$ 385.0	\$ 404.5	\$ 371.7	\$ 320.8
Change in accounting policies (note 2)	-	(42.7)	-	(40.3)
Beginning of period, as restated	385.0	361.8	371.7	280.5
Net earnings	74.1	26.1	167.0	115.2
Excess of cost of repurchase of common shares over stated value	-	-	(0.8)	-
Purchase of convertible debentures (note 6)	-	-	(71.2)	-
Dividends on common shares	(3.8)	(3.8)	(11.4)	(11.6)
End of period	\$ 455.3	\$ 384.1	\$ 455.3	\$ 384.1

## Consolidated Statements of Cash Flow (unaudited)

[\$ millions]	Three months ended September 30		Nine months ended September 30	
	2006	2005 (restated-note 2)	2006	2005 (restated-note 2)
<b>Operating activities</b>				
Net earnings	\$ 74.1	\$ 26.1	\$ 167.0	\$ 115.2
Add (deduct)				
Non-controlling interests	5.4	7.4	13.7	22.2
Accretion of convertible debentures	-	0.1	0.3	0.6
Depletion, amortization and accretion	37.7	46.2	133.6	137.6
Amortization of financing costs	0.6	0.2	1.5	0.6
Loss on debt settlement	-	-	3.1	-
Share of earnings of equity accounted investments	(5.2)	(0.1)	(6.1)	(0.6)
Gain on disposition of investments	-	-	(5.0)	-
Future income taxes	(13.7)	(1.8)	(38.4)	(7.2)
Foreign exchange loss (gain)	1.3	(2.8)	2.2	4.8
Asset retirement obligations	(0.2)	(1.3)	(3.7)	(3.6)
Other items	(0.7)	0.2	1.0	(0.3)
	<b>99.3</b>	<b>74.2</b>	<b>269.2</b>	<b>269.3</b>
Net decrease (increase) in non-cash working capital (note 14)	<b>0.2</b>	<b>42.0</b>	<b>(46.1)</b>	<b>2.4</b>
Cash provided by operating activities	<b>99.5</b>	<b>116.2</b>	<b>223.1</b>	<b>271.7</b>
<b>Investing activities</b>				
Capital expenditures	(55.3)	(76.5)	(162.4)	(213.3)
Short-term investments	(1.8)	(150.9)	40.1	(145.6)
Net proceeds from sale of capital assets	-	0.1	0.4	1.7
Restricted cash	(5.0)	2.1	(10.2)	13.1
Other assets	(12.6)	10.9	(30.6)	(3.1)
Distributions from investments	22.2	-	139.4	-
Cash used for investing activities	<b>(52.5)</b>	<b>(214.3)</b>	<b>(23.3)</b>	<b>(347.2)</b>
<b>Financing activities</b>				
Increase (decrease) in short-term debt	-	(17.8)	(10.1)	20.2
Increase (decrease) in long-term debt	4.0	0.4	7.4	(2.2)
Payment of unsecured debentures	-	-	(14.4)	-
Purchase of convertible debentures	-	-	(181.6)	-
Issuance of common shares	2.2	8.6	3.2	14.4
Repurchase of common shares	-	(4.5)	(2.1)	(9.9)
Dividends paid to non-controlling interests	(5.8)	-	(28.1)	-
Dividends paid	(3.8)	(3.9)	(11.4)	(7.8)
Cash provided by (used for) financing activities	<b>(3.4)</b>	<b>(17.2)</b>	<b>(237.1)</b>	<b>14.7</b>
<b>Effect of exchange rate changes on cash and cash equivalents</b>	<b>(0.1)</b>	<b>(2.7)</b>	<b>(0.4)</b>	<b>(2.0)</b>
<b>Increase (decrease) in cash and cash equivalents</b>	<b>43.5</b>	<b>(118.0)</b>	<b>(37.7)</b>	<b>(62.8)</b>
<b>Cash and cash equivalents at beginning of period</b>	<b>356.4</b>	<b>474.8</b>	<b>437.6</b>	<b>419.6</b>
<b>Cash and cash equivalents at end of period</b>	<b>\$ 399.9</b>	<b>\$ 356.8</b>	<b>\$ 399.9</b>	<b>\$ 356.8</b>
<b>Supplementary Cash Flow Information</b>				
Cash received for interest	\$ 4.0	\$ 4.2	\$ 13.6	\$ 11.0
Cash paid for interest on debt	10.9	6.1	25.4	33.0
Cash paid for income taxes	27.2	12.7	49.9	46.7
<b>Cash and cash equivalents consist of:</b>				
Cash on hand and balances with banks	\$ 100.9	\$ 71.1	\$ 100.9	\$ 71.1
Cash equivalents	299.0	285.7	299.0	285.7
	<u>\$ 399.9</u>	<u>\$ 356.8</u>	<u>\$ 399.9</u>	<u>\$ 356.8</u>

## Notes to Interim Consolidated Financial Statements (Unaudited)

(All tabular dollar amounts expressed in millions of Canadian dollars, except per share amounts)

### 1. Summary of accounting policies

These interim consolidated financial statements have been prepared on a basis consistent with those followed in the consolidated financial statements for the year ended December 31, 2005, with the exception of the change in the foreign currency translation method as detailed in note 2(a). The disclosures contained in these interim consolidated financial statements do not include all requirements of Canadian generally accepted accounting principles for annual financial statements. Accordingly, the interim consolidated financial statements should be read in conjunction with the consolidated financial statements for the year ended December 31, 2005.

### 2. Accounting changes

#### (a) Translation of foreign currencies

The method of translation of foreign operations depends on whether the foreign operations are integrated or self-sustaining. Prior to January 1, 2006, all of the Corporation's foreign operations were considered integrated and translated into Canadian dollars using current rates of exchange for monetary assets and liabilities, historical rates of exchange for non-monetary assets and liabilities and average rates of exchange for revenues and expenses, except depletion and amortization which were translated at the rates of exchange applicable to the related assets. Gains and losses resulting from these translation adjustments were included in income.

The ongoing review of the economic factors to be considered in determining whether foreign operations are integrated or self-sustaining has resulted in the determination that the Metals foreign operations and the Oil and Gas foreign operations in Cuba and Spain have changed to self-sustaining. This change was made as a result of the increasing proportion of operating, financing and investing transactions of these foreign operations that are denominated in currencies other than the Canadian dollar. This change in method was effective at January 1, 2006 and was applied prospectively. The self-sustaining operations are translated into Canadian dollars using the current-rate method, whereby assets and liabilities are translated at period-end exchange rates while revenues and expenses are converted using average rates for the period. Gains and losses on translation to Canadian dollars relating to self-sustaining operations are deferred and included in a separate component of shareholders' equity described as cumulative translation account.

## Notes to Interim Consolidated Financial Statements (Unaudited) (continued)

(All tabular dollar amounts expressed in millions of Canadian dollars, except per share amounts)

### 2. Accounting changes (continued)

#### (b) Future income taxes

On October 1, 2005, the Corporation changed its methodology of accounting for income taxes in its Cuban oil and gas operations to provide a clearer presentation of income taxes in that operation. Prior to this change in accounting policy, the Corporation recorded tax on the Cuban oil and gas operations on the basis that cost recovery revenue and expenses were not subject to or deductible under the Cuban tax regime resulting in no temporary differences between the book value and the tax value of the relevant assets and liabilities. This methodology resulted in significant fluctuations in the effective tax rate for the Oil and Gas operations between reporting periods when the relative percentage of cost recovery revenue changed compared to total oil revenue.

Under the adopted accounting policy, temporary differences are recognized for the respective assets and liabilities at the effective Cuban tax rate of approximately 30%. This results in a clearer presentation of the effective tax rate in the Cuban oil operations over the life of the operating oil fields. The Corporation has implemented this change on a retroactive basis with restatement of prior periods. The cumulative effect of the change in policy on retained earnings at January 1, 2005 was \$40.3 million. The accounting change resulted in an increase in net earnings of \$3.0 million (increase in EPS – basic \$0.02, diluted \$0.02) in the third quarter of 2005 and an increase in net earnings of \$0.6 million (increase in EPS – basic \$nil, diluted \$nil) in the nine months ended September 30, 2005.

The Corporation also changed the methodology of accounting for income taxes paid on its behalf by an agency of the government of Cuba for the enhanced oil recovery blocks, to reflect these income taxes on a gross basis. As a result, current income tax expense and revenue have increased. This change was applied on a retroactive basis and resulted in an increase in revenue and current income tax expense of \$1.2 million and \$2.7 million for the three months and nine months ended September 30, 2005, respectively.

#### (c) Comparative amounts

Certain comparative amounts have been restated to correct their classification, with no impact on net earnings, to conform to the presentation in the current period.

In the Metals business (“Metals”), certain selling expenses which were previously netted against revenue, have been reclassified to operating, selling, general and administrative expenses, resulting in an increase in revenue of \$2.7 million and \$5.4 million for the three- and nine-month periods ended September 30, 2005, respectively. For the three months ended March 31, 2006 and June 30, 2006, revenue reclassification respectively resulted in an increase of \$1.6 million and \$9.8 million in revenues, with a corresponding increase in operating, selling, general and administration expenses.

Capital expenditures on the Consolidated Statements of Cash Flow in 2005 have been adjusted for non-cash capital addition of \$6.0 million and \$1.5 million for the three and nine months ended September 30, 2005.

## Notes to Interim Consolidated Financial Statements (Unaudited) (continued)

(All tabular dollar amounts expressed in millions of Canadian dollars, except per share amounts)

### 3. Significant Transaction

On June 27, 2006, Royal Utilities Income Fund (“Royal Utilities”), a trust in which the Corporation held a 50% indirect interest through its partnership in the Coal business (“Coal”), successfully completed an initial public offering of units (“IPO”).

Prior to the IPO, Royal Utilities transferred to certain affiliates of the Coal partnership certain non-core mining assets comprised of the Coal Valley export thermal-coal mine, other non-producing coal mines, certain coal and potash resources and other non-mining assets (the “Transferred Assets”). These transfers were recorded at their carrying value.

Following the IPO and the exercise of the over-allotment by the underwriters, the Corporation owned 41.2% of the outstanding units of Royal Utilities as at June 30, 2006. For accounting purposes, the Corporation’s dilution of its interest in Royal Utilities resulted in a gain of \$4.7 million.

The results for Coal reflected the Corporation’s 50% proportionate interest in Royal Utilities up to June 27, 2006. Subsequent to June 27, 2006, the Corporation prospectively changed its accounting for Royal Utilities to the equity method of accounting. The Corporation continues to proportionately consolidate its 50% interest in the Transferred Assets.

The gain on disposition of investments also includes a \$0.3 million gain on sale of short-term investments.

### 4. Investments

	September 30, 2006	December 31, 2005
Royal Utilities <sup>(a)</sup>	\$ 342.6	\$ -
Tourism <sup>(b)</sup>	20.2	21.0
Other	0.4	0.4
	<u>\$ 363.2</u>	<u>\$ 21.4</u>

<sup>(a)</sup> The Corporation has a 41.2% direct interest in Royal Utilities (note 3).

<sup>(b)</sup> The Corporation has a 25% indirect interest in a hotel complex in Varadero, Cuba, and a 12.5% indirect interest in a hotel complex in Havana, Cuba.

These investments are accounted for as long-term investments using the equity method of accounting.

## Notes to Interim Consolidated Financial Statements (Unaudited) (continued)

(All tabular dollar amounts expressed in millions of Canadian dollars, except per share amounts)

### 5. Post-retirement benefits

The Corporation's pension expense for the third quarter of 2006 was \$2.1 million (2005 - \$1.9 million). For the nine months ended September 30, 2006, pension expense was \$9.2 million (2005 - \$6.3 million).

### 6. Long-term debt and other long-term liabilities

	September 30, 2006	December 31, 2005
7% convertible unsecured debentures due 2013 (note 18)	\$ 188.7	\$ 293.6
7.875% senior unsecured debentures due 2012	273.6	273.6
9.875% senior unsecured debentures	-	14.4
Loan from financial institution	22.5	25.0
Other long-term debt	24.3	5.7
	<b>509.1</b>	612.3
Capital lease obligations	14.2	28.5
Other long-term liabilities	0.4	8.2
	<b>523.7</b>	649.0
Current portion of long-term debt and other long-term liabilities	<b>(9.1)</b>	<b>(28.2)</b>
	<b>\$ 514.6</b>	<b>\$ 620.8</b>

The Corporation completed two offers to purchase portions of the principal amount of its outstanding 7% convertible unsecured subordinated debentures due December 15, 2013. On the first offer, which expired in April 2006, the Corporation purchased \$7.1 million principal amount of the debentures for a total consideration of \$11.7 million, including accrued interest. On the second offer, which expired on June 26, 2006, the Corporation purchased \$100 million principal amount of the debentures for a total consideration of \$170.3 million, including accrued interest. These transactions resulted in \$3.1 million being charged to income and \$71.2 million being charged to retained earnings.

On January 16, 2006, the \$14.4 million of 9.875% debentures were redeemed for cash.

Other long-term debt reflects proportionally consolidated loans to joint ventures.

Interest and accretion on long-term debt for the third quarter of 2006 was \$9.9 million (2005 – \$12.2 million). For the nine months ended September 30, 2006, interest and accretion on long-term debt was \$34.4 million (2005 - \$38.8 million).

## Notes to Interim Consolidated Financial Statements (Unaudited) (continued)

(All tabular dollar amounts expressed in millions of Canadian dollars, except per share amounts)

### 7. Asset retirement obligations

Asset retirement obligations have been recognized in respect of the mining operations of Coal and Metals, including associated infrastructure and buildings. Obligations have also been recorded for nickel and cobalt refining facilities, fertilizers and utilities facilities and oil and gas production facilities. Reclamation of coal mining operations is typically carried out on a continuous basis over the life of each mine and is dependent on the rate that mining progresses over the area to be mined. Retirement of refinery, fertilizer and utility facilities, oil and gas production facilities, infrastructure and buildings normally takes place at the end of the assets' useful life.

The following is a reconciliation of the opening and closing asset retirement obligation balances.

	Nine months ended September 30, 2006	Year ended December 31, 2005
Balance, beginning of period	\$ 81.6	\$ 77.2
Additions to liabilities	3.3	7.6
Liabilities settled	(4.2)	(7.3)
Accretion expense	3.7	5.8
Change in foreign exchange rates	(1.4)	(1.7)
Liabilities disposed (note 3)	(27.2)	-
Balance, end of period	55.8	81.6
Current portion	(2.2)	(8.8)
	<u>\$ 53.6</u>	<u>\$ 72.8</u>

The Corporation has estimated the undiscounted cash flow required to settle the asset retirement obligation at approximately \$172.2 million. Expenditures will be made on an ongoing basis over several decades and are expected to be funded by cash generated from operations. Credit adjusted discount rates from 3% to 9% were applied to expected future cash flows to determine the carrying value of the asset retirement obligation.

In view of uncertainties concerning asset retirement obligations, the ultimate costs could be materially different from the amounts estimated. The estimate of the future asset retirement liabilities is subject to change based on amendments to applicable laws and legislation. Future changes in asset retirement liabilities, if any, could have a significant impact and would be reflected prospectively, as a change in accounting estimate.

## Notes to Interim Consolidated Financial Statements (Unaudited) (continued)

(All tabular dollar amounts expressed in millions of Canadian dollars, except per share amounts)

### 8. Capital stock

The Corporation's authorized share capital consists of an unlimited number of common shares.

The changes in the Corporation's outstanding common shares were as follows:

	Number		Stated Capital	
	September 30, 2006	December 31, 2005	September 30, 2006	December 31, 2005
Balance, beginning of year	151,333,889	131,381,776	\$ 781.7	\$ 582.4
Changes during the period:				
Share purchase plan	87,585	123,200	0.6	0.5
Repurchase of shares	(200,000)	(5,085,432)	(1.0)	(26.3)
Stock options exercised	422,780	2,164,000	2.6	13.9
6% convertible debenture conversion	-	21,923,924	-	202.4
6% convertible debenture redemption	-	811,137	-	8.7
7% convertible debenture conversion	52,855	15,284	0.3	0.1
Balance, end of period	151,697,109	151,333,889	\$ 784.2	\$ 781.7

If all of the 7% convertible debentures are converted into shares at the option of the holders, up to 27,438,429 additional common shares may be issued on or before December 14, 2013.

The following table presents the calculation of basic and diluted earnings per common share:

	Three months ended September 30		Nine months ended September 30	
	2006	2005 (restated-note 2)	2006	2005 (restated-note 2)
Net earnings	\$ 74.1	\$ 26.1	\$ 167.0	\$ 115.2
Loss on redemption of convertible debentures included in contributed surplus	-	-	-	(0.5)
Net earnings – basic	74.1	26.1	167.0	114.7
Loss on purchase of convertible debentures	-	-	3.1	-
Interest and accretion on convertible debentures	2.3	3.6	9.4	13.4
Net earnings - diluted	\$ 76.4	\$ 29.7	\$ 179.5	\$ 128.1
Weighted average number of shares				
- basic	151.3	155.2	151.3	149.6
Weighted average effect of dilutive securities:				
Employee stock options	0.3	1.7	0.4	1.7
Convertible debentures	27.5	42.9	27.5	47.7
Weighted average number of shares - diluted	179.1	199.8	179.2	199.0
Earnings per share				
Basic	\$ 0.49	\$ 0.17	\$ 1.10	\$ 0.77
Diluted	0.43	0.15	1.00	0.64

## Notes to Interim Consolidated Financial Statements (Unaudited) (continued)

(All tabular dollar amounts expressed in millions of Canadian dollars, except per share amounts)

### 9. Stock compensation plans

The following is a summary of stock option activity during the three months and nine months ended September 30, 2006.

	Three months ended September 30, 2006		Three months ended September 30, 2005	
	Options	Weighted average exercise price	Options	Weighted average exercise price
Outstanding at beginning of period	3,075,000	\$ 9.10	5,130,000	\$ 6.66
Granted	25,000	11.57	-	-
Exercised for shares	(242,780)	6.38	(1,234,000)	6.51
Exercised for cash	-	-	(1,746,000)	7.21
Forfeited	(155,000)	9.98	-	-
Outstanding at end of period	2,702,220	\$ 9.32	2,150,000	\$ 6.31
Options exercisable, end of period	607,220	\$ 5.44	2,150,000	\$ 6.31

	Nine months ended September 30, 2006		Nine months ended September 30, 2005	
	Options	Weighted average exercise price	Options	Weighted average exercise price
Outstanding at beginning of period	2,005,000	\$ 7.97	6,040,000	\$ 6.62
Granted	1,275,000	10.45	-	-
Exercised for shares	(422,780)	6.11	(2,144,000)	6.45
Exercised for cash	-	-	(1,746,000)	7.21
Forfeited	(155,000)	9.98	-	-
Outstanding at end of period	2,702,220	\$ 9.32	2,150,000	\$ 6.31
Options exercisable, end of period	607,220	\$ 5.44	2,150,000	\$ 6.31

As at September 30, 2006, 2,095,000 (2005 – 850,000) options with a share appreciation right (“SAR”) attachment remained outstanding for which the Corporation has recognized a compensation recovery of \$0.5 million and \$nil million (2005 - expense of \$9.9 million and \$9.9 million) for the three and nine months ended September 30, 2006, respectively.

The Corporation also recorded a compensation recovery of \$3.0 million and \$0.1 million (2005 - expense of \$4.6 million and \$4.3 million) for the three and nine months ended September 30, 2006, respectively for the other stock-based compensation plans.

## Notes to Interim Consolidated Financial Statements (Unaudited) (continued)

(All tabular dollar amounts expressed in millions of Canadian dollars, except per share amounts)

### 10. Contributed surplus

	Nine months ended September 30, 2006		Year ended December 31, 2005	
Balance, beginning of period	\$	192.3	\$	199.2
Redemption of convertible debentures		-		(0.5)
Repurchase of common shares		(0.4)		(6.4)
Balance, end of period	\$	191.9	\$	192.3

Contributed surplus may be utilized to eliminate or reduce any deficit, which may arise as a result of the future payment or distribution of dividends or other distributions, from time to time, to holders of the common shares.

Contributed surplus was reduced by \$0.4 million for the nine months ended September 30, 2006 reflecting the loss on repurchase of shares during the first quarter.

### 11. Net financing expense

	Three months ended September 30 2006		Nine months ended September 30 2006	
		2005 (restated-note 2)		2005 (restated-note 2)
Interest income on cash, cash equivalents, short-term investments and loans receivable	\$	(4.4)	\$	(5.3)
Interest expense on debt		9.9		13.5
Foreign exchange losses (gains)		1.3		(2.9)
Other		(0.8)		-
	\$	6.0	\$	5.3
			\$	25.8
			\$	34.1

### 12. Income taxes

	Three months ended September 30 2006		Nine months ended September 30 2006	
		2005 (restated-note 2)		2005 (restated-note 2)
Current	\$	44.0	\$	17.0
Future		(13.7)		(1.8)
	\$	30.3	\$	15.2
			\$	94.7
			\$	67.9
			\$	(38.4)
			\$	(7.2)
			\$	56.3
			\$	60.7

## Notes to Interim Consolidated Financial Statements (Unaudited) (continued)

(All tabular dollar amounts expressed in millions of Canadian dollars, except per share amounts)

### 13. Commitments and Contingencies

As at September 30, 2006, the Corporation was committed to purchase equipment and services in the amount of \$72.1 million. At December 31, 2005, one of Royal Utilities' pension plans has an actuarially determined funding deficiency valued at \$12.9 million of which the Corporation's share is \$6.5 million. This deficit is being funded over 15 years, as required under the pension regulation. Under certain circumstances, the funding requirement for the pension plan may be accelerated and the Corporation may be responsible for this obligation.

### 14. Net decrease (increase) in non-cash working capital

	Three months ended September 30		Nine months ended September 30	
	2006	2005 (restated-note 2)	2006	2005 (restated-note 2)
Accounts receivable	\$ (31.0)	\$ 30.5	\$ (70.8)	\$ 12.7
Inventories	(8.0)	(17.7)	(24.1)	(13.3)
Overburden removal costs	0.6	0.3	(0.3)	(1.2)
Prepaid expenses	1.4	0.5	(5.0)	(0.9)
Accounts payable and accrued liabilities	37.2	28.4	54.1	5.1
	\$ 0.2	\$ 42.0	\$ (46.1)	\$ 2.4

## Notes to Interim Consolidated Financial Statements (Unaudited) (continued)

(All tabular dollar amounts expressed in millions of Canadian dollars, except per share amounts)

### 15. Segment information

Reference should be made to Sherritt's annual audited consolidated financial statements for a full description of operating segments.

#### Three months ended September 30, 2006

[\$ millions]	Coal <sup>(2)</sup>	Metals	Oil and Gas	Power	Other <sup>(1)</sup>	Corporate	Consolidated
Revenue	\$ 29.1	\$ 148.0	\$ 65.1	\$ 29.0	\$ 14.3	\$ -	\$ 285.5
Operating, selling, general and administrative	28.5	69.1	12.5	8.2	12.8	6.1	137.2
Earnings (loss) before undernoted items	0.6	78.9	52.6	20.8	1.5	(6.1)	148.3
Depletion, amortization and accretion	2.1	5.1	22.5	6.3	0.6	1.1	37.7
Operating earnings (loss)	(1.5)	73.8	30.1	14.5	0.9	(7.2)	110.6
Share of earnings of equity accounted investments	5.2	-	-	-	-	-	5.2
Net financing expense							(6.0)
Income taxes							(30.3)
Non-controlling interests							(5.4)
Net earnings							74.1
Capital expenditures	1.3	17.3	30.0	5.7	-	1.0	55.3
Assets	\$ 100.9	\$ 481.4	\$ 648.0	\$ 543.8	\$ 83.4	\$ 615.8	\$ 2,473.3

#### Three months ended September 30, 2005 (restated-note 2)

[\$ millions]	Coal <sup>(2)</sup>	Metals	Oil and Gas	Power	Other <sup>(1)</sup>	Corporate	Consolidated
Revenue	\$ 64.8	\$ 86.6	\$ 60.8	\$ 24.2	\$ 20.9	\$ -	\$ 257.3
Operating, selling, general and administrative	50.3	52.3	8.7	5.5	19.4	21.0	157.2
Earnings (loss) before undernoted items	14.5	34.3	52.1	18.7	1.5	(21.0)	100.1
Depletion, amortization and accretion	14.2	4.8	19.8	5.6	0.8	1.0	46.2
Operating earnings (loss)	0.3	29.5	32.3	13.1	0.7	(22.0)	53.9
Share of earnings of equity accounted investments	-	-	-	-	-	0.1	0.1
Net financing expense							(5.3)
Income taxes							(15.2)
Non-controlling interests							(7.4)
Net earnings							26.1
Capital expenditures	17.9	10.8	27.9	19.6	-	0.3	76.5
Assets	\$ 782.0	\$ 409.2	\$ 601.1	\$ 528.8	\$ 94.3	\$ 375.3	\$ 2,790.7

<sup>(1)</sup> Other represents the results of the soybean-based food processing business.

<sup>(2)</sup> Coal results include Royal Utilities on proportionate consolidation basis, and the Corporation's 50% proportionate interest in the Coal Valley export thermal coal mine and the coal development assets.

## Notes to Interim Consolidated Financial Statements (Unaudited) (continued)

(All tabular dollar amounts expressed in millions of Canadian dollars, except per share amounts)

### 15. Segment information (continued)

#### Nine months ended September 30, 2006

[\$ millions]	Coal <sup>(2)</sup>	Metals	Oil and Gas	Power	Other <sup>(1)</sup>	Corporate	Consolidated
Revenue	\$ 176.1	\$ 351.1	\$ 203.4	\$ 79.6	\$ 43.2	\$ -	\$ 853.4
Operating, selling, general and administrative	143.4	195.8	39.9	23.0	39.3	26.7	468.1
Earnings (loss) before undernoted items	32.7	155.3	163.5	56.6	3.9	(26.7)	385.3
Depletion, amortization and accretion	29.7	14.7	64.4	19.3	2.0	3.5	133.6
Operating earnings (loss)	3.0	140.6	99.1	37.3	1.9	(30.2)	251.7
Share of earnings of equity accounted investments	5.2	-	-	-	-	0.9	6.1
Net financing expense							(25.8)
Income taxes							(56.3)
Non-controlling interests							(13.7)
Gain on disposition of investments							5.0
Net earnings							167.0
Capital expenditures	8.0	45.3	86.7	20.4	0.9	1.1	162.4
Assets	\$ 100.9	\$ 481.4	\$ 648.0	\$ 543.8	\$ 83.4	\$ 615.8	\$ 2,473.3

#### Nine months ended September 30, 2005 (restated-note 2)

[\$ millions]	Coal <sup>(2)</sup>	Metals	Oil and Gas	Power	Other <sup>(1)</sup>	Corporate	Consolidated
Revenue	\$ 193.0	\$ 330.8	\$ 178.9	\$ 76.5	\$ 57.7	\$ -	\$ 836.9
Operating, selling, general and administrative	143.5	184.9	28.7	23.2	51.7	35.7	467.7
Earnings (loss) before undernoted items	49.5	145.9	150.2	53.3	6.0	(35.7)	369.2
Depletion, amortization and accretion	42.3	15.0	58.8	16.2	2.2	3.1	137.6
Operating earnings (loss)	7.2	130.9	91.4	37.1	3.8	(38.8)	231.6
Share of earnings of equity accounted investments	-	-	-	-	-	0.6	0.6
Net financing expense							(34.1)
Income taxes							(60.7)
Non-controlling interests							(22.2)
Gain on disposition of investments							-
Net earnings							115.2
Capital expenditures	25.0	24.4	93.2	68.7	0.2	1.8	213.3
Assets	\$ 782.0	\$ 409.2	\$ 601.1	\$ 528.8	\$ 94.3	\$ 375.3	\$ 2,790.7

<sup>(1)</sup> Other represents the results of the soybean-based food processing business.

<sup>(2)</sup> Coal results include Royal Utilities on proportionate consolidation basis up to June 27, 2006, and the Corporation's 50% proportionate interest in the Coal Valley export thermal coal mine and the coal development assets.

## Notes to Interim Consolidated Financial Statements (Unaudited) (continued)

(All tabular dollar amounts expressed in millions of Canadian dollars, except per share amounts)

### 15. Segment information (continued)

Three months ended September 30

	2006		2005 (restated – note 2)	
	Revenue	Capital Assets	Revenue	Capital Assets
Canada	\$ 17.6	\$ 205.3	\$ 67.5	\$ 816.1
Cuba	104.2	822.2	103.7	801.8
Europe	67.6	1.0	52.2	2.3
Asia	86.9	7.0	30.3	7.2
Other foreign countries	9.2	-	3.6	-
	<b>\$ 285.5</b>	<b>\$ 1,035.5</b>	<b>\$ 257.3</b>	<b>\$ 1,627.4</b>

Nine months ended September 30

	2006		2005 (restated – note 2)	
	Revenue	Capital Assets	Revenue	Capital Assets
Canada	\$ 185.9	\$ 205.3	\$ 228.3	\$ 816.1
Cuba	316.0	822.2	303.7	801.8
Europe	182.3	1.0	189.0	2.3
Asia	143.5	7.0	101.9	7.2
Other foreign countries	25.7	-	14.0	-
	<b>\$ 853.4</b>	<b>\$ 1,035.5</b>	<b>\$ 836.9</b>	<b>\$ 1,627.4</b>

### 16. Financial instruments

Unutilized lines of credit as at September 30, 2006 were \$51.0 million.

### 17. Cumulative translation account

Exchange gains and losses arising from the translation of the financial statements of the Corporation's self-sustaining foreign operations are deferred and included in the cumulative translation account (see note 2 (a)). When there is a reduction in the Corporation's net investment in a self-sustaining foreign operation, a proportionate amount of the cumulative translation account is included in the determination of consolidated net earnings. Significant changes in the cumulative translation account are as follows:

	Nine months ended September 30, 2006	Year ended December 31, 2005
Balance, beginning of period	\$ -	\$ -
Effect of change on opening balances	(47.7)	-
Effect of exchange rate changes during the period	(22.9)	-
Balance, end of period	<b>\$ (70.6)</b>	<b>\$ -</b>

## **Notes to Interim Consolidated Financial Statements (Unaudited) (continued)**

(All tabular dollar amounts expressed in millions of Canadian dollars, except per share amounts)

### **18. Subsequent Events**

On September 13, 2006, the Corporation announced its third offer in 2006 to purchase a portion of its outstanding 7% convertible debentures due December 15, 2013 (the "Debentures"). Pursuant to this offer, \$50 million principal amount of debentures at a price of \$1,610 per \$1,000 principal, plus accrued interest, were purchased. The purchase was completed on October 23, 2006.

## Schedule of Selected Current Assets and Accounts Payable by Operating Segment

### September 30, 2006

[\$ millions]	Coal	Metals	Oil and Gas	Power	Other	Corporate	Consolidated
Accounts receivable	\$ 7.7	\$ 75.5	\$ 172.3	\$ 24.4	\$ 14.5	\$ 14.3	\$ 308.7
Inventories	11.2	80.1	-	14.7	5.9	-	111.9
Overburden removal costs	0.6	-	-	-	-	-	0.6
Prepaid expenses	0.4	2.7	1.8	1.1	1.4	5.8	13.2
Future income taxes	1.3	15.9	-	-	-	11.3	28.5
	\$ 21.2	\$ 174.2	\$ 174.1	\$ 40.2	\$ 21.8	\$ 31.4	\$ 462.9
Accounts payable and accrued liabilities	\$ 13.6	\$ 80.2	\$ 41.1	\$ 14.9	\$ 11.8	\$ 44.0	\$ 205.6

### June 30, 2006

[\$ millions]	Coal	Metals	Oil and Gas	Power	Other	Corporate	Consolidated
Accounts receivable	\$ 2.1	\$ 56.4	\$ 175.3	\$ 25.8	\$ 12.5	\$ 21.1	\$ 293.2
Inventories	16.6	67.8	-	13.8	6.0	-	104.2
Overburden removal costs	1.1	-	-	-	-	-	1.1
Prepaid expenses	1.4	2.8	2.4	1.8	1.4	4.8	14.6
Future income taxes	1.3	8.9	-	-	-	-	10.2
	\$ 22.5	\$ 135.9	\$ 177.7	\$ 41.4	\$ 19.9	\$ 25.9	\$ 423.3
Accounts payable and accrued liabilities	\$ 12.1	\$ 61.8	\$ 38.6	\$ 11.6	\$ 10.7	\$ 32.3	\$ 167.1

### March 31, 2006

[\$ millions]	Coal	Metals	Oil and Gas	Power	Other	Corporate	Consolidated
Accounts receivable	\$ 26.2	\$ 42.5	\$ 197.9	\$ 23.0	\$ 10.1	\$ 12.4	\$ 312.1
Inventories	33.0	69.5	-	13.1	7.1	-	122.7
Overburden removal costs	1.9	-	-	-	-	-	1.9
Prepaid expenses	1.7	3.9	0.2	0.1	1.6	1.2	8.7
Future income taxes	5.4	5.0	-	-	-	-	10.4
	\$ 68.2	\$ 120.9	\$ 198.1	\$ 36.2	\$ 18.8	\$ 13.6	\$ 455.8
Accounts payable and accrued liabilities	\$ 26.5	\$ 50.9	\$ 36.0	\$ 11.5	\$ 11.8	\$ 40.8	\$ 177.5

### December 31, 2005

[\$ millions]	Coal	Metals	Oil and Gas	Power	Other	Corporate	Consolidated
Accounts receivable	\$ 30.5	\$ 46.8	\$ 161.2	\$ 20.2	\$ 9.4	\$ 10.1	\$ 278.2
Inventories	28.8	64.6	-	13.0	3.6	-	110.0
Overburden removal costs	2.4	-	-	-	-	-	2.4
Prepaid expenses	1.8	4.0	0.9	0.4	1.4	1.4	9.9
Future income taxes	4.2	6.7	-	-	-	-	10.9
	\$ 67.7	\$ 122.1	\$ 162.1	\$ 33.6	\$ 14.4	\$ 11.5	\$ 411.4
Accounts payable and accrued liabilities	\$ 30.1	\$ 54.9	\$ 33.1	\$ 12.2	\$ 7.7	\$ 36.3	\$ 174.3





Sherritt International Corporation  
1133 Yonge Street  
Toronto ON  
Canada M4T 2Y7

For further investor information contact

Investor Relations  
Telephone (416) 924 4551  
Toll-Free 1 800 704 6698  
Fax (416) 924 5015

[www.sherritt.com](http://www.sherritt.com)



This document has been printed on Forest Stewardship Council (FSC) certified Domtar Plainfield Opaque. FSC fibre used in the manufacture of Domtar Plainfield paper comes from well-managed forests independently certified by SmartWood according to Forest Stewardship Council rules.