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**Sherritt International Corporation
Management's
Discussion and Analysis**
For the three and six months ended June 30, 2009

Second Quarter - Management's Discussion and Analysis

We prepared this Management's discussion and analysis for the three months and six months ended June 30, 2009 as of July 24, 2009 and it should be read in conjunction with our audited consolidated financial statements and our management's discussion and analysis for the year ended December 31, 2008. Additional information relating to the Corporation, including the Corporation's Annual Information Form, is available on SEDAR at www.sedar.com or on the Corporation's web site at www.sherritt.com.

References to "Sherritt", "the Corporation", "we", "us", and "our" refer to Sherritt International Corporation and its share of consolidated subsidiaries and joint ventures, unless the context indicates otherwise. All amounts are in Canadian dollars, unless otherwise indicated. References to "US\$" are to United States dollars.

Securities regulators encourage companies to disclose forward-looking information to help investors understand a company's future prospects. This discussion contains statements about our future financial condition, results of operations and business. See page 39 of this report for further information on forward-looking statements.

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Second-quarter highlights

- The Corporation's net earnings during the second quarter of 2009 were \$24.4 million compared to \$80.3 million in the same period in the prior year.
- Revenue of \$357.7 million and EBITDA¹ of \$112.2 million in the second quarter of 2009 compared to revenue of \$441.2 million and EBITDA of \$190.4 million in the same period in the prior year. Lower revenue and EBITDA were primarily a result of lower nickel, cobalt, and oil prices and lower net production volume at Oil and Gas as a result of the termination by Sherritt's joint operating partner of the Block 7 production-sharing contract, partially offset by the additional contribution from the consolidation of Royal Utilities Income Fund (Royal Utilities) following the acquisition by the Corporation of the remaining units of Royal Utilities in May 2008.
- Net oil and gas production in Cuba during the second quarter was 5,100 barrels per day or 30% lower than the same period in the prior year, primarily due to the termination of the Block 7 production-sharing contract.
- At June 30, 2009, engineering was virtually complete on the Ambatovy Project.
- On June 24, 2009, Sherritt finalized arrangements with its partners in the Ambatovy Project that established a mechanism through which the partners could finance the Corporation's pro rata share of shareholder funding requirements for the Project.
- The Corporation continues to maintain a strong liquidity position with a current ratio of 2.06:1; a net working capital balance of \$861.8 million; cash, cash equivalents, and short-term investments of \$1.0 billion; and a long-term debt-to-capitalization ratio of 33%².

¹For additional information, see the Non-GAAP Measures section.

²Calculated as Total long-term debt divided by the sum of Total long-term debt, Non-controlling interests and Shareholders' equity.

Key financial and operational data

| \$ millions | For the three months ended | | For the six months ended | |
|---|----------------------------|-----------------|--------------------------|-----------------|
| | 2009 June 30 | 2008 June 30 | 2009 June 30 | 2008 June 30 |
| Financial highlights⁽¹⁾ | | | | |
| Revenue | \$ 357.7 | \$ 441.2 | \$ 706.7 | \$ 755.4 |
| EBITDA ⁽²⁾ | 112.2 | 190.4 | 209.4 | 366.1 |
| Operating earnings ⁽²⁾ | 52.4 | 126.3 | 81.0 | 262.3 |
| Net earnings (loss) | 24.4 | 80.3 | (18.5) | 169.3 |
| Net earnings (loss) per share, diluted (\$ per share) | 0.08 | 0.28 | (0.07) | 0.65 |
| Cash flow⁽¹⁾ | | | | |
| Cash provided by operating activities | \$ 47.0 | \$ 21.3 | \$ 142.3 | \$ 172.8 |
| Capital expenditures⁽¹⁾ | | | | |
| | \$ 388.2 | \$ 619.3 | \$ 805.1 | \$ 1,081.5 |
| Production volumes | | | | |
| Nickel (tonnes)(50% basis) | 4,261 | 3,704 | 8,334 | 7,452 |
| Cobalt (tonnes)(50% basis) | 470 | 406 | 939 | 813 |
| Coal - Prairie Operations ⁽³⁾ (millions of tonnes) | 8.4 | 8.8 | 16.9 | 17.6 |
| Coal - Mountain Operations (millions of tonnes)(50% basis) | 0.5 | 0.4 | 1.0 | 0.8 |
| Oil - Cuba - net production (barrels per day) | 12,099 | 17,199 | 12,878 | 17,336 |
| Electricity (gigawatt hours) | 515 | 567 | 1,056 | 1,164 |
| Unit operating costs | | | | |
| Nickel ⁽⁴⁾ (US\$ per pound) | \$ 2.85 | \$ 2.41 | \$ 3.43 | \$ 2.18 |
| Coal - Prairie Operations (\$ per tonne) | 11.19 | 11.88 | 11.41 | 11.04 |
| Coal - Mountain Operations (\$ per tonne) | 63.17 | 72.19 | 61.01 | 63.44 |
| Oil - Cuba (\$ per barrel of oil) | 7.87 | 5.51 | 8.48 | 5.82 |
| Electricity (\$ per megawatt hour) | 15.14 | 11.80 | 16.49 | 10.13 |
| Averaged-realized sales prices | | | | |
| Nickel (\$ per pound) | \$ 6.86 | \$ 12.12 | \$ 6.30 | \$ 12.53 |
| Cobalt (\$ per pound) | 16.62 | 45.67 | 16.43 | 45.90 |
| Coal - Prairie Operations (\$ per tonne) | 14.35 | 14.61 | 14.68 | 14.12 |
| Coal - Mountain Operations (\$ per tonne) | 85.86 | 87.87 | 92.72 | 77.56 |
| Oil - Cuba (\$ per barrel of oil) | 43.18 | 62.01 | 39.40 | 56.63 |
| Electricity (\$ per megawatt hour) | 47.93 | 40.83 | 49.23 | 40.72 |

\$ millions, except as noted, as at 2009
June 30 2008
December 31

Financial Condition

| | | |
|---|----------|----------|
| Current ratio | 2.06:1 | 1.68:1 |
| Long-term debt-to-capitalization ⁽⁵⁾ | 33% | 32% |
| Net working capital balance | \$ 861.8 | \$ 554.3 |
| Cash, cash equivalents and short-term investments | 1,015.9 | 607.3 |
| Total assets | 10,076.6 | 9,547.2 |
| Total long-term debt | 2,847.0 | 2,550.1 |
| Non-controlling interests | 2,156.4 | 1,668.4 |
| Shareholders' equity | 3,586.7 | 3,727.1 |

(1) Results include those of Royal Utilities from date of acquisition, May 2, 2008.

(2) For additional information see the Non-GAAP Measures section.

(3) For Prairie Operations volumes are presented on a 100% basis.

(4) Net direct cash cost inclusive of by-product credits and third-party feed costs.

(5) Calculated as Total long-term debt divided by the sum of Total long-term debt, Non-controlling interests and Shareholders' equity.

Current market environment

Impact on operating results

Our results were significantly impacted by commodity prices and by changes in the Canadian dollar relative to the U.S. dollar. Nickel and oil average-realized prices strengthened during the second quarter of 2009 compared to the prior two quarters; however, these prices were still considerably lower than those realized in the second quarter of 2008. Compared to the second quarter of 2008, operating results in the second quarter of 2009 were significantly impacted by: a 50% reduction in the average-reference price of nickel to US\$5.89 per pound; a 71% reduction in the average-reference price of cobalt to US\$13.53 per pound; and a 39% reduction in the average-reference price for Gulf Coast Fuel Oil No. 6 to US\$51.68 per barrel. The approximate impact of these decreases in commodity prices was a \$143 million reduction in operating earnings in the second quarter of 2009 compared to the same period in the prior year (for the first six months of 2009, the approximate impact was \$311 million).

Our results are reported in Canadian dollars and the fluctuation in foreign exchange rates has the potential to cause significant volatility in our results. Changes in commodity prices also have a significant impact on the majority of our input costs, such as natural gas, sulphur and sulphuric acid that impact our operating earnings. We have provided estimates of the sensitivity of our second-quarter earnings to changes in key parameters on page 34.

Impact on liquidity

We continue to maintain our strong financial position despite challenges resulting from a weaker economy. At June 30, 2009, total cash, cash equivalents and short-term investments were \$1.0 billion. This amount includes \$341.7 million held by the Ambatovy Joint Venture to be used towards the development of the Project. The majority of the remaining \$674.2 million was held in Canada in Government of Canada treasury bills or in cash deposit accounts with major Canadian financial institutions rated A- or higher by Standard and Poor's.

We continue to implement the following cost containment initiatives: restricting divisional capital spending to divisional cash flows; the suspension of certain expansion programs; the reduction of controllable operating costs and the continuing review of Ambatovy Project costs.

During the second quarter of 2009, the Corporation completed negotiations with its partners in the Ambatovy Project that established a mechanism through which the partners could finance the Corporation's pro rata share of shareholder funding requirements for the Project. As a result, Sherritt will not be required to directly contribute any new shareholder funding to the Project. See page 28 for further information.

In respect of Oil and Gas and Power receivables due in 2009, the Corporation received \$135.1 million to June 30, 2009 and \$20.0 million subsequent to that date. At June 30, 2009, \$40.2 million of Oil and Gas and \$4.5 million of Power receivables were overdue. The amounts outstanding are guaranteed by the National Bank of Cuba. The Corporation and certain Cuban government agencies continue to negotiate an agreement with respect to 2009 Oil and Gas and Power receivables that would require the payment of all amounts due in 2009 to be made in approximately-equal monthly installments. The Cuban government agencies continue to make equal monthly payments against outstanding balances. We expect that all 2009 receivables will be collected by the end of first quarter 2010.

The Corporation amended the terms of its short-term credit facilities that provide liquidity of up to \$200.0 million. The amended facilities contain less restrictive financial covenants and revised interest rates. See page 28 for further information

On June 29, 2009, DBRS Limited confirmed our unsecured debt rating at BB (high) and removed the “Under Review with Negative Implications” condition in light of the completion of the Ambatovy Joint Venture additional partner loan agreements and the renewal of our syndicated 364-day revolving term credit facility.

Ambatovy Project

The recent political unrest in Madagascar has not resulted in any material disruptions in activities at the Project and there has been no targeting of Project personnel or assets. See Review of operations – Metals section on page 9 for further information.

Financial results

| \$ millions | For the three months ended | | For the six months ended | |
|---|----------------------------|-----------------|--------------------------|-----------------|
| | 2009 June 30 | 2008 June 30 | 2009 June 30 | 2008 June 30 |
| Revenue by segment | | | | |
| Metals | \$ 111.1 | \$ 177.7 | \$ 190.8 | \$ 340.0 |
| Coal ⁽¹⁾ | 165.7 | 124.5 | 354.6 | 155.4 |
| Oil and Gas | 50.2 | 104.5 | 96.8 | 192.0 |
| Power | 28.6 | 30.3 | 59.0 | 60.1 |
| Corporate and other | 2.1 | 4.2 | 5.5 | 7.9 |
| | 357.7 | 441.2 | 706.7 | 755.4 |
| EBITDA⁽²⁾ by segment | | | | |
| Metals | \$ 26.5 | \$ 71.3 | \$ 25.1 | \$ 160.5 |
| Coal ⁽¹⁾ | 41.9 | 22.0 | 101.9 | 27.3 |
| Oil and Gas | 33.6 | 86.5 | 60.8 | 154.5 |
| Power | 19.7 | 22.9 | 39.4 | 46.7 |
| Corporate and other | (9.5) | (12.3) | (17.8) | (22.9) |
| | 112.2 | 190.4 | 209.4 | 366.1 |
| Operating earnings (loss)⁽²⁾ by segment | | | | |
| Metals | \$ 20.0 | \$ 65.5 | \$ 11.2 | \$ 149.8 |
| Coal ⁽¹⁾ | 17.9 | 1.3 | 52.7 | 4.4 |
| Oil and Gas | 13.3 | 57.3 | 13.3 | 101.6 |
| Power | 12.0 | 15.7 | 24.1 | 32.0 |
| Corporate and other | (10.8) | (13.5) | (20.3) | (25.5) |
| | 52.4 | 126.3 | 81.0 | 262.3 |
| Loss on disposal of property, plant and equipment | - | - | 79.5 | - |
| Net financing expense | 15.9 | 13.5 | 13.8 | 12.6 |
| Share of earnings of equity accounted investments | - | (3.0) | - | (9.4) |
| Other items | (0.7) | - | 1.5 | - |
| Income taxes | 5.9 | 28.3 | (9.1) | 76.2 |
| Non-controlling interests | 5.6 | 6.7 | 11.7 | 12.9 |
| Earnings (loss) from continuing operations | \$ 25.7 | 80.8 | \$ (16.4) | 170.0 |
| Loss from discontinued operation | (1.3) | (0.5) | (2.1) | (0.7) |
| Net earnings (loss) | \$ 24.4 | 80.3 | \$ (18.5) | 169.3 |
| Earnings (loss) from continuing operations per share | | | | |
| Basic | \$ 0.09 | \$ 0.29 | \$ (0.06) | \$ 0.66 |
| Diluted | \$ 0.09 | \$ 0.28 | \$ (0.06) | \$ 0.65 |
| Net earnings (loss) per share | | | | |
| Basic | \$ 0.08 | \$ 0.28 | \$ (0.07) | \$ 0.66 |
| Diluted | \$ 0.08 | \$ 0.28 | \$ (0.07) | \$ 0.65 |
| Effective Tax Rate | 16% | 24% | 66% | 29% |

(1) The Coal segment includes the following:

- The Corporation's 50% proportionate interest in Mountain Operations and coal development assets.
- The Corporation's consolidated results of Royal Utilities since the date of acquisition, May 2, 2008. Prior to the date of acquisition, the Corporation recognized its share of earnings in "Share of earnings in equity accounted investments".

(2) For additional information see the Non-GAAP Measures section.

On a consolidated basis, for the second quarter and first six months of 2009, our revenue was \$357.7 million and \$706.7 million, respectively, and EBITDA was \$112.2 million and \$209.4 million, respectively. We had net earnings of \$24.4 million for the second quarter of 2009 reducing our year-to-date loss to \$18.5 million.

Our diverse asset base and the implementation of cost containment initiatives has allowed us to generate positive operating cash flows despite a significant decline in the market price of nickel, cobalt, and oil as compared to the prior-year periods. For the first six months of 2009, higher prices for coal and higher coal royalty revenue have partially offset the negative impact of lower nickel, cobalt, oil and gas prices. Detailed information on the performance of each of our operations can be found in the Review of operations sections. In summary:

- Metals' operating earnings of \$20.0 million and \$11.2 million for the second quarter and the first six months of 2009, respectively, were lower than operating earnings of \$65.5 million and \$149.8 million in the same periods in the prior year primarily due to significantly lower average-realized prices for nickel and cobalt, despite higher nickel and cobalt sales volumes resulting from incremental production following completion of the Phase 1 expansion in the second quarter of 2008. During the second quarter of 2009, the average-realized price of nickel increased by 21% and the net direct cash cost per pound of nickel, before cobalt by-product credits, decreased by 20% compared to the first quarter of 2009.
- Coal's operating earnings increased by \$16.6 million and \$48.3 million to \$17.9 million and \$52.7 million, respectively, for the second quarter and first six months of 2009 compared to the same periods in the prior year. These increases are primarily due to the inclusion of the operating results of Royal Utilities in Prairie Operations for each of the 2009 periods compared to 2008 results which only include results from May 2, 2008, the date of the acquisition of the remaining units of Royal Utilities by Sherritt. In addition, due to the carryover in the first quarter of contracts based on last year's record export thermal coal prices, for the six months ended June 30, 2009, Coal realized a 20% increase in the average-realized price of thermal export coal at Mountain Operations compared to the same period in the prior year.
- Oil and Gas' operating earnings of \$13.3 million for both the second quarter and first six months of 2009 were \$44.0 million and \$88.3 million lower, respectively, than in the same periods in the prior year primarily due to a reduction in net oil production resulting from the termination of the Block 7 production-sharing contract and a 30% decrease in the average-realized price for oil produced in Cuba over each period. The current year-to-date net earnings reflect a \$79.5 million (\$57.4 million after tax) loss on disposal of assets associated with Block 7 that was recognized in the first quarter of 2009.
- Power's operating earnings decreased \$3.7 million and \$7.9 million to \$12.0 million and \$24.1 million for the second quarter and first six months of 2009, respectively, primarily due to higher maintenance and repair costs which were partially offset by higher average-realized electricity prices primarily due to changes in the foreign exchange rate.
- The effective consolidated tax rate for the second quarter and first six months of 2009 was 16% and 66%, respectively, compared to 24% and 29% for the same periods in 2008 primarily due to changes in the relative mix of earnings and losses incurred by our divisions, which are carried out in different tax rate jurisdictions. Removing the impact of the \$79.5 million (\$57.4 million after tax) loss on disposal of assets realized by Oil and Gas, the normalized effective consolidated tax rate for the first six months of 2009 was 20%.

Review of operations - Metals

Financial data

| \$ millions | For the three months ended | | For the six months ended | |
|---------------------------------------|----------------------------|-----------------|--------------------------|-----------------|
| | 2009 June 30 | 2008 June 30 | 2009 June 30 | 2008 June 30 |
| Revenue | | | | |
| Nickel | \$ 65.7 | \$ 99.4 | \$ 115.4 | \$ 207.5 |
| Cobalt | 17.9 | 41.1 | 34.1 | 83.6 |
| Fertilizers | 25.5 | 33.5 | 37.6 | 42.0 |
| Other | 2.0 | 3.7 | 3.7 | 6.9 |
| | 111.1 | 177.7 | 190.8 | 340.0 |
| Operating costs ⁽¹⁾ | | | | |
| Mining, processing and refining | (54.6) | (59.9) | (113.5) | (109.6) |
| Third-party feed costs | (1.5) | (8.4) | (5.3) | (19.5) |
| Fertilizers | (21.9) | (31.7) | (34.2) | (40.4) |
| Other | (0.9) | (0.5) | (3.3) | (0.5) |
| | (78.9) | (100.5) | (156.3) | (170.0) |
| Selling costs | (4.2) | (4.9) | (7.0) | (7.3) |
| General and administrative costs | (1.5) | (1.0) | (2.4) | (2.2) |
| EBITDA ⁽²⁾ | 26.5 | 71.3 | 25.1 | 160.5 |
| Depletion, amortization and accretion | (6.5) | (5.8) | (13.9) | (10.7) |
| Operating earnings ⁽²⁾ | \$ 20.0 | \$ 65.5 | \$ 11.2 | \$ 149.8 |

(1) Excluding depreciation and amortization of \$6.4 million and \$3.4 million for the three-month periods ended June 30, 2009 and June 30, 2008, respectively, and \$10.9 million and \$6.5 million for the six-month periods ended June 30, 2009 and June 30, 2008, respectively.

(2) For additional information see the Non-GAAP Measures section.

The change in operating earnings between comparative periods in 2009 and 2008 is detailed below.

| \$ millions | For the three months ended 2009 June 30 | For the six months ended 2009 June 30 |
|---|---|---|
| | Lower realized nickel prices | \$ (69.1) |
| Lower realized cobalt prices | (39.2) | (80.1) |
| Higher metals sales volumes net of lower fertilizer sales volumes | 10.3 | 15.1 |
| Lower mining, processing, refining and third-party feed costs | 36.0 | 49.9 |
| Impact of stronger U.S. dollar | 17.1 | 43.7 |
| Other | (0.6) | (7.8) |
| Decrease in operating earnings, compared to 2008 | \$ (45.5) | \$ (138.6) |

Metal prices

| Prices \$ millions | For the three months ended | | For the six months ended | |
|---|----------------------------|-----------------|--------------------------|-----------------|
| | 2009 June 30 | 2008 June 30 | 2009 June 30 | 2008 June 30 |
| Nickel - average-realized (\$/lb) | \$ 6.86 | \$ 12.12 | \$ 6.30 | \$ 12.53 |
| Cobalt - average-realized (\$/lb) | 16.62 | 45.67 | 16.43 | 45.90 |
| Nickel - average-reference (US\$/lb) | 5.89 | 11.67 | 5.31 | 12.38 |
| Cobalt - average-reference (US\$/lb) ⁽¹⁾ | 13.53 | 45.93 | 13.91 | 46.06 |

(1) Average low-grade cobalt published price per Metals Bulletin.

During the second quarter of 2009, the average nickel and cobalt reference prices decreased by US\$5.78 per pound and US\$32.40 per pound, respectively, compared to the same period in the prior year. For the first six months of 2009, average nickel and cobalt reference prices decreased US\$7.07 and US\$32.15, respectively, compared to the same period in the prior year. During 2009, the average-realized prices benefited from a stronger U.S. dollar relative to the Canadian dollar.

Production and sales

| Production tonnes (50% basis) | For the three months ended | | For the six months ended | |
|----------------------------------|----------------------------|-----------------|--------------------------|-----------------|
| | 2009 June 30 | 2008 June 30 | 2009 June 30 | 2008 June 30 |
| Mixed sulphides | 4,639 | 4,323 | 9,325 | 8,647 |
| Finished nickel | 4,261 | 3,704 | 8,334 | 7,452 |
| Finished cobalt | 470 | 406 | 939 | 813 |

| Sales (50% basis) | | | | |
|---------------------------------------|--------|--------|---------|---------|
| Finished nickel (thousands of pounds) | 9,582 | 8,200 | 18,318 | 16,562 |
| Finished cobalt (thousands of pounds) | 1,078 | 902 | 2,076 | 1,822 |
| Fertilizer (tonnes) | 68,787 | 83,326 | 100,438 | 105,705 |

Production of 9,277 tonnes (100% basis) of contained nickel and cobalt in mixed sulphides in the second quarter of 2009 was 631 tonnes higher than in the same period in the prior year reflecting the contribution of Phase 1 expansion assets commissioned during the second quarter of 2008 and the timing of maintenance activities at Moa. Total finished metals production was also higher during the second quarter and the first six months of 2009, reflecting increased mixed sulphide availability, the positive impact resulting from the contribution of Phase 1 expansion assets at the Fort Saskatchewan site and the timing of maintenance activities. Negotiations to finalize the terms of the mixed-sulphide supply agreement that expired on June 30, 2007 are ongoing. In the interim, as negotiations proceed, the joint venture companies continue to operate under the terms of the expired agreement.

Sales of finished nickel and cobalt were higher during the second quarter and for the first six months of 2009 reflecting the impact of higher finished metals production. Nickel sales exceeded production in the second quarter of 2009, drawing down nickel inventory to more normal levels in response to improved global nickel demand. Fertilizer sales volumes decreased 14,539 tonnes in the second quarter and 5,267 tonnes in the first six months of 2009 compared to the same periods in the prior year reflecting poor spring weather conditions and the impact of an extended acid plant maintenance outage in Fort Saskatchewan.

Operating costs

| Unit operating costs | For the three months ended | | For the six months ended | |
|--|----------------------------|---------|--------------------------|---------|
| | 2009 | 2008 | 2009 | 2008 |
| | June 30 | June 30 | June 30 | June 30 |
| Mining, processing and refining costs | \$ 4.34 | \$ 6.91 | \$ 4.65 | \$ 6.26 |
| Third-party feed costs | 0.13 | 1.02 | 0.24 | 1.17 |
| Cobalt by-product credits | (1.61) | (4.96) | (1.55) | (5.01) |
| Other ⁽¹⁾ | (0.01) | (0.56) | 0.09 | (0.24) |
| Net direct cash cost (US\$/lb of nickel) | \$ 2.85 | \$ 2.41 | \$ 3.43 | \$ 2.18 |
| Natural gas costs (\$/gigajoule) | 4.01 | 9.63 | 4.01 | 8.54 |
| Sulphur costs (US\$/tonne) | 184.43 | 383.71 | 168.62 | 320.21 |
| Sulphuric acid costs (US\$/tonne) | 134.76 | 224.73 | 159.85 | 217.54 |

(1) Includes fertilizer profit or loss, marketing costs, premiums, and other by-product credits.

| Components of mining, processing and refining costs | For the three months ended | | For the six months ended | |
|---|----------------------------|---------|--------------------------|---------|
| | 2009 | 2008 | 2009 | 2008 |
| | June 30 | June 30 | June 30 | June 30 |
| Fixed Costs | 23% | 16% | 22% | 17% |
| Sulphur | 9% | 11% | 9% | 10% |
| Sulphuric acid | 20% | 20% | 20% | 20% |
| Fuel oil | 14% | 14% | 13% | 15% |
| Maintenance | 12% | 13% | 12% | 12% |
| Other variables ⁽¹⁾ | 22% | 26% | 24% | 26% |
| | 100% | 100% | 100% | 100% |

(1) Approximate breakdown of mining, processing and refining costs based on a breakdown of production costs in the period excluding the impact of opening and closing inventory values on the cost of sales.

Net direct cash cost in the second quarter and for the first six months of 2009 increased compared to the same periods in the prior year as the benefit of lower mining, processing, refining and third-party feed costs were more than offset by lower cobalt by-product credits resulting from lower cobalt prices. Lower mining, processing and refining costs largely reflect lower commodity-input prices and the impact of the stronger U.S. dollar on Canadian dollar denominated refining costs. Lower third-party feed costs are a result of lower nickel and cobalt reference prices and the increased availability of Moa mixed sulphides, which have partially displaced third-party feed.

Capital spending

| Capital Spending ⁽¹⁾ | For the three months ended | | For the six months ended | |
|---------------------------------|----------------------------|-----------------|--------------------------|-----------------|
| | 2009 | 2008 | 2009 | 2008 |
| \$ millions | June 30 | June 30 | June 30 | June 30 |
| Moa Joint Venture | | | | |
| Sustaining | \$ 3.9 | \$ 12.7 | \$ 6.8 | \$ 22.8 |
| Expansion | 3.4 | 51.9 | 6.0 | 92.1 |
| | 7.3 | 64.6 | 12.8 | 114.9 |
| Ambatovy Joint Venture | 326.8 | 501.7 | 703.7 | 884.6 |
| Total | \$ 334.1 | \$ 566.3 | \$ 716.5 | \$ 999.5 |

(1) Capital expenditures include the Corporation's 50% interest in the Moa Joint Venture, 100% of utility and fertilizer operations in Fort Saskatchewan and 100% of the Ambatovy Joint Venture.

Capital spending by the Moa Joint Venture was \$57.3 million and \$102.1 million lower for the second quarter and for the first six months of 2009, respectively, compared to the same periods in the prior period, reflecting the suspension of expansion activities and curtailment of the sustaining capital program in light of lower nickel reference prices. Expansion spending during the second quarter of 2009 reflected the ongoing capitalization of interest related to financing of the Phase 2 expansion and the Moa acid plant, and the construction of certain Phase 2 expansion assets at Fort Saskatchewan.

Capital spending for the Ambatovy Project was primarily for site-based construction activities.

2009 Quarterly Ambatovy Project Update

- At June 30, 2009, engineering was virtually complete.
- Capital spending for the project was \$326.8 million in the second quarter.
- A total of \$493.0 million was provided by the Ambatovy Joint Venture partners during the second quarter. Sherritt contributed \$273.1 million of the \$493.0 million, primarily through loans from the other joint venture partners.
- The projected capital cost of the Project remains unchanged at US\$4.52 billion, excluding accrued financing charges, foreign exchange and working capital requirements. Initiatives are ongoing to realize reductions in material and labour costs.
- Mechanical completion is anticipated to occur by the latter part of 2010.

Ambatovy Project Financing

On June 24, 2009 Sherritt announced that it has finalized arrangements with its Ambatovy Joint Venture partners, Sumitomo Corporation (Sumitomo), Korea Resources Corporation (Kores) and SNC-Lavalin Inc. (SNC-Lavalin) that established a mechanism through which the partners could finance the Corporation's pro rata share of shareholder funding requirements for the Project.

The Project's US\$2.1 billion (100% basis) senior project financing is unaffected by these arrangements.

For additional information on these agreements, please refer to page 28.

Madagascar Political Update

In January 2009, Andry Rajoelina, the opposition leader and former elected Mayor of the capital city, Antananarivo, called on the President of Madagascar, Marc Ravalomanana, to resign, citing improper use of public money, and other charges. In March 2009, after a period of civil unrest, Mr. Ravalomanana resigned as President. Mr. Rajoelina assumed power with the backing of the military and the high court and established a transitional government to lead the country for a period not to exceed 24 months with the expectation that elections will be held within that time frame.

The United States, the European Union and the International Monetary Fund have all curtailed non-humanitarian aid to Madagascar, and the African Union has suspended Madagascar's membership in the organization.

There were no material disruptions in activities at the Ambatovy Project and no targeting of Project personnel or assets. The Corporation has established communication with the transitional government officials and continues its communication with multilateral institutions and key embassies.

Outlook for 2009

| Production volumes and capital spending | Actual 2009 | Projected 2009 |
|---|----------------|-------------------|
| For the six and twelve months ended | June 30 | December 31 |
| Production | | |
| Mixed sulphides (tonnes, 100% basis) | 18,649 | 37,000 |
| Finished Nickel (tonnes, 100% basis) | 16,668 | 33,500 |
| Finished Cobalt (tonnes, 100% basis) | 1,877 | 3,500 |
| Capital Expenditures (\$ millions) | | |
| Moa Joint Venture (50% basis) | \$ 13 | \$ 39 |
| Ambatovy (100% basis, U.S.\$) | \$ 580 | \$ 1,800 |

In Metals, the majority benefit of lower commodity input prices is expected to continue for the balance of 2009, with any change in unit operating costs from the first half of the year largely dependent on cobalt prices. Annual maintenance activities are being completed in three windows in May, June and September/October, subject to finalization of the schedule. This staged approach is proving less disruptive and more cost efficient than a single shut-down. Capital expenditure guidance in Metals has been adjusted to reflect the capitalization of interest on the Moa/Fort expansion financing, partly offset by lower-than-planned sustaining capital expenditures.

In the Ambatovy Project, approximately US\$0.6 billion of the estimated US\$1.8 billion in 2009 capital expenditures is expected to be financed through drawdowns on the senior project financing. Sherritt's contribution of partner funding for the remainder of 2009 is expected to be funded through the Ambatovy Joint Venture additional partner loans.

Review of operations – Coal

Financial data

| \$ millions | For the three months ended | | For the six months ended | |
|--|----------------------------|-----------------|--------------------------|-----------------|
| | 2009 June 30 | 2008 June 30 | 2009 June 30 | 2008 June 30 |
| Prairie Operations (100% basis) ⁽¹⁾⁽²⁾ | | | | |
| Mining revenue | \$ 116.7 | \$ 123.6 | \$ 244.6 | \$ 247.4 |
| Coal royalties | 13.2 | 11.0 | 26.1 | 19.5 |
| Potash royalties | 2.3 | 4.6 | 6.6 | 8.1 |
| | 132.2 | 139.2 | 277.3 | 275.0 |
| Operating costs ⁽³⁾ | (91.0) | (100.4) | (190.2) | (193.3) |
| General and administrative costs ⁽⁴⁾ | (6.9) | (8.6) | (8.5) | (11.5) |
| EBITDA ⁽⁵⁾ | 34.3 | 30.2 | 78.6 | 70.2 |
| Depletion, amortization and accretion | (20.2) | (26.7) | (42.3) | (51.8) |
| Operating earnings ⁽⁵⁾ | \$ 14.1 | \$ 3.5 | \$ 36.3 | \$ 18.4 |
| Mountain Operations and coal development assets (50% basis) | | | | |
| Revenue | \$ 33.5 | \$ 34.2 | \$ 77.3 | \$ 65.1 |
| Operating costs ⁽⁶⁾ | (24.6) | (28.0) | (50.9) | (53.1) |
| General and administrative costs | (1.3) | (0.6) | (3.1) | (1.1) |
| EBITDA ⁽⁵⁾ | 7.6 | 5.6 | 23.3 | 10.9 |
| Depletion, amortization and accretion | (3.8) | (2.6) | (6.9) | (4.8) |
| Operating earnings ⁽⁵⁾ | \$ 3.8 | \$ 3.0 | \$ 16.4 | \$ 6.1 |

- (1) The results of Prairie Operations have been consolidated from May 2, 2008. Prior to May 2, 2008, Sherritt equity accounted for its investment in Royal Utilities. In order to provide a meaningful discussion of results on a consolidated basis, the table above and the financial analysis below discusses Prairie Operations on a 100% basis for the prior-year periods. Prairie Operations' results have been included in revenue and EBITDA in the financial statements of the Corporation since May 2, 2008.
- (2) For the three-month and six-month periods ended June 30, 2008, the Corporation recognized in its financial statements total division operating earnings of \$1.3 million and \$4.4 million, respectively, including an operating loss for Prairie Operations of \$1.7 million for the period May 2, 2008 to June 30, 2008. In addition to operating earnings, the Corporation recognized in its financial statements \$1.9 million and \$8.3 million in the three-month and six-month periods ended June 30, 2008, respectively, as its share of equity earnings for the period January 1, 2008 to May 2, 2008..
- (3) Excluding depreciation and amortization of \$11.4 million and \$9.7 million for the three-month periods ended June 30, 2009 and June 30, 2008, respectively, and \$23.8 million and \$18.2 million for the six-month periods ended June 30, 2009 and June 30, 2008, respectively.
- (4) Includes restructuring and other costs of \$5.5 million and \$6.8 million for the three-month and six-month periods ended June 30, 2008, respectively, related to the acquisition of the remaining units of Royal Utilities.
- (5) For additional information see the Non-GAAP Measures section.
- (6) Excluding depreciation and amortization of \$3.3 million and \$2.1 million for the three-month periods ended June 30, 2009 and June 30, 2008, respectively, and \$6.0 million and \$4.0 million for the six-month periods ended June 30, 2009 and June 30, 2008, respectively.

The change in operating earnings between comparative periods in 2009 and 2008 is detailed below.

| \$ millions | For the three months ended 2009 June 30 | For the six months ended 2009 June 30 |
|---|---|---|
| Prairie Operations: | | |
| (Lower)/higher royalties | \$ (0.1) | \$ 5.1 |
| Lower operating costs, net of mining revenue | 2.5 | 0.3 |
| Higher pension expense | (4.4) | (4.3) |
| Lower general and administrative costs | 6.1 | 7.3 |
| Lower depletion, amortization and accretion | 6.5 | 9.5 |
| Increase in operating earnings, compared to 2008 | \$ 10.6 | \$ 17.9 |
| Mountain Operations and coal development assets: | | |
| (Lower)/Higher coal prices, denominated in U.S. dollars | \$ (6.4) | \$ 0.3 |
| Impact of stronger U.S. dollar | 5.8 | 12.4 |
| Lower operating costs | 3.4 | 2.2 |
| Higher depletion, amortization and accretion | (1.2) | (2.1) |
| Other | (0.8) | (2.5) |
| Increase in operating earnings, compared to 2008 | \$ 0.8 | \$ 10.3 |

Coal prices and royalty revenue

| Prices (\$/tonne) | For the three months ended | | For the six months ended | |
|--|----------------------------|-----------------|--------------------------|-----------------|
| | 2009 June 30 | 2008 June 30 | 2009 June 30 | 2008 June 30 |
| Prairie Operations - average-realized ⁽¹⁾ | \$ 14.35 | \$ 14.61 | \$ 14.68 | \$ 14.12 |
| Mountain Operations - average-realized | 85.86 | 87.87 | 92.72 | 77.56 |

(1) Excludes royalty revenue.

During the second quarter and for the first six months of 2009, coal royalties in Prairie Operations increased due to the timing of mining in royalty areas. Potash royalties fell as a result of lower production as potash producers reacted in an effort to support higher market prices. Also in Prairie Operations, changes in the average-realized price of coal reflected index-adjusted prices at owned mines and lower cost and capital recoveries at the contract and Genesee mines.

In Mountain Operations, the average-realized price decreased \$2.01 per tonne in the second quarter of 2009 compared to the same period in the prior year due to reduced pricing on export thermal coal contracts; however, the reduced price was partially offset by the stronger U.S. dollar relative to the Canadian dollar. For the first six months of 2009, the average-realized price increased \$15.16 per tonne compared to the same period in the prior year primarily due to impact of the stronger U.S. dollar relative to the Canadian dollar on thermal coal contracts prices entered into in the prior year at record prices that carried into the first quarter of 2009.

Operating costs

| Unit operating costs (\$/tonne) | For the three months ended | | For the six months ended | |
|---------------------------------|----------------------------|----------|--------------------------|----------|
| | 2009 | 2008 | 2009 | 2008 |
| | June 30 | June 30 | June 30 | June 30 |
| Prairie Operations | \$ 11.19 | \$ 11.88 | \$ 11.41 | \$ 11.04 |
| Mountain Operations | 63.17 | 72.19 | 61.01 | 63.44 |

| Components of Operating Costs (%) | For the three months ended | | For the six months ended | |
|-----------------------------------|----------------------------|-------------|--------------------------|-------------|
| | 2009 | 2008 | 2009 | 2008 |
| | June 30 | June 30 | June 30 | June 30 |
| Prairie Operations | | | | |
| Labour | 43% | 37% | 42% | 38% |
| Repairs and maintenance | 29% | 24% | 28% | 25% |
| Fuel | 11% | 16% | 12% | 16% |
| Other ⁽¹⁾ | 17% | 23% | 18% | 21% |
| Total | 100% | 100% | 100% | 100% |
| Mountain Operations | | | | |
| Labour | 26% | 18% | 24% | 19% |
| Repairs and maintenance | 17% | 14% | 14% | 12% |
| Fuel | 11% | 13% | 11% | 13% |
| Rentals and contractors | 15% | 14% | 14% | 12% |
| Ex-Mine ⁽²⁾ | 31% | 28% | 36% | 33% |
| Other ⁽³⁾ | 0% | 13% | 1% | 11% |
| Total | 100% | 100% | 100% | 100% |

(1) Comprised of rentals, subcontracts, explosives, power, taxes, tires, licenses and other miscellaneous expenses.

(2) Comprised largely of commissions, royalties, freight and port fees.

(3) Comprised of tires, explosives, power, taxes, licenses, other miscellaneous expenses and the impact of changes in coal inventory levels during the period.

In Prairie Operations, operating costs decreased \$0.69 per tonne in the second quarter of 2009 compared to the same period in the prior year primarily due to a decline in commodity prices, particularly diesel, and reduced production at the contract mines. These cost reductions were partially offset by major repairs at certain owned mines on equipment that had reached specified operating hour thresholds. During the first six months of 2009, operating costs were also affected by unseasonably cold weather in Saskatchewan and two unplanned dragline outages at the Boundary Dam mine, both of which required more costly mining techniques to be employed in the first quarter.

In Mountain Operations, operating costs per tonne decreased in both the second quarter and first six months of 2009 compared to the same periods in the prior year, primarily due to lower commodity prices and higher production.

Production and sales

| Production (millions of tonnes) | For the three months ended | | For the six months ended | |
|-----------------------------------|----------------------------|-----------------|--------------------------|-----------------|
| | 2009 June 30 | 2008 June 30 | 2009 June 30 | 2008 June 30 |
| Prairie Operations (100% basis) | 8.4 | 8.8 | 16.9 | 17.6 |
| Mountain Operations (50% basis) | 0.5 | 0.4 | 1.0 | 0.8 |
| Sales (millions of tonnes) | | | | |
| Prairie Operations (100% basis) | 8.2 | 8.4 | 16.7 | 17.5 |
| Mountain Operations (50% basis) | 0.4 | 0.4 | 0.8 | 0.8 |

In Prairie Operations, reduced production and sales volumes for the second quarter and for the first six months of 2009 compared to the same period in the prior year were primarily due to lower volumes at the contract mines as a result of reduced demand by our customers due to higher repair outages at the generating stations.

In Mountain Operations, production was higher due to improved equipment availability.

Capital Spending

| Capital Spending \$ millions | For the three months ended | | For the six months ended | |
|---------------------------------|----------------------------|-----------------|--------------------------|-----------------|
| | 2009 June 30 | 2008 June 30 | 2009 June 30 | 2008 June 30 |
| Prairie Operations (100% basis) | | | | |
| Sustaining | \$ 16.4 | \$ 7.5 | \$ 25.0 | \$ 11.5 |
| Growth | 3.8 | - | 5.6 | - |
| Mountain Operations (50% basis) | | | | |
| Sustaining | 1.9 | 0.5 | 3.1 | 1.1 |
| Growth ⁽¹⁾ | 11.4 | - | 12.6 | - |
| Total | \$ 33.5 | \$ 8.0 | \$ 46.3 | \$ 12.6 |

(1) Includes \$6.5 million of equipment financed through a bank credit facility that ordinarily would have been acquired under a capital lease.

Prairie Operations leases the majority of its mobile equipment under long-term mine support equipment agreements entered into in 2004. In the first six months of 2009, working capital was used to purchase \$18.9 million of equipment due to limited availability of lease financing at acceptable terms. In the same period, Prairie Operations incurred capital costs of \$6.1 million for infrastructure development and capital repairs on mobile equipment.

During the second quarter of 2009, \$3.8 million (our proportionate contribution pursuant to the joint venture with Norit Canada Inc.) was spent for the construction of the activated carbon plants at the Bienfait mine bringing total 2009 spending to \$5.6 million. Commissioning is expected in early 2010.

In Mountain Operations, capital spending for infrastructure development was higher than in the prior year periods as the Coal Valley mine prepared to enter new mining areas. Growth capital spending related to the Obed Mountain mine project was predominantly for refurbishing the wash plant and conveyor system and also included in the second quarter \$6.5 million of equipment financed through a bank credit facility.

Outlook for 2009

| Production volumes, royalties and capital expenditures | Actual 2009 | Projected 2009 |
|--|----------------|-------------------|
| For the six and twelve months ended | June 30 | December 31 |
| Production | | |
| Prairie Operations (millions of tonnes, 100% basis) | 16.9 | 36.0 |
| Mountain Operations (millions of tonnes, 100% basis) | 2.0 | 4.4 |
| Royalties (\$ millions) | | |
| Coal | 26 | 41 |
| Potash | 7 | 15 |
| Capital Expenditures (\$ millions) | | |
| Prairie Operations ⁽¹⁾ | 25 | 35 |
| Mountain Operations (50% basis) | 3 | 9 |
| Activated carbon project (50% basis) | 6 | 27 |
| Obed Mountain mine (50% basis) ⁽²⁾ | 6 | 8 |

(1) Excludes equipment expected to be financed through new borrowings in the second half of 2009.

(2) Excludes equipment financed through a bank credit facility.

In Coal, annual production levels are expected to be consistent with prior years and all production has been contracted. Price settlement for the majority of Mountain Operations export contracts occurred in late March and early April 2009. Export settlement prices are significantly lower than the record prices of 2008 due to current market conditions. Approximately 50% of Coal Valley mine's contract year production will be linked to the Newcastle FOB settlement price, which settled at approximately US\$70.00 per tonne, down over 40% from last year. This has resulted in a corresponding reduction in the average-realized price per tonne at Mountain Operations for second-quarter 2009 that will continue for the balance of 2009, although the impact will be somewhat offset if the Canadian dollar remains weaker than last year. Additional production from the Obed Mountain mine (scheduled to re-open in the third quarter) is estimated to be approximately 0.4 million tonnes for the year. Sustaining capital expenditures for Prairie Operations are expected to increase as working capital or other credit facilities are used to fund capital purchases that otherwise would have been leased. The commissioning of the first activated carbon plant is on schedule for early 2010.

Review of operations – Oil and Gas

Financial data

| \$ millions | For the three months ended | | For the six months ended | |
|---------------------------------------|----------------------------|---------|--------------------------|----------|
| | 2009 | 2008 | 2009 | 2008 |
| | June 30 | June 30 | June 30 | June 30 |
| Revenue | | | | |
| Cuba | \$ 47.5 | \$ 97.1 | \$ 91.8 | \$ 178.7 |
| Spain | 1.8 | 5.4 | 3.3 | 9.8 |
| Pakistan | 0.3 | 0.3 | 0.6 | 0.5 |
| Processing and other | 0.6 | 1.7 | 1.1 | 3.0 |
| | 50.2 | 104.5 | 96.8 | 192.0 |
| Operating costs | (10.7) | (10.1) | (23.4) | (21.2) |
| General and administrative costs | (5.9) | (7.9) | (12.6) | (16.3) |
| EBITDA ⁽¹⁾ | 33.6 | 86.5 | 60.8 | 154.5 |
| Depletion, amortization and accretion | (20.3) | (29.2) | (47.5) | (52.9) |
| Operating earnings ⁽¹⁾ | \$ 13.3 | \$ 57.3 | \$ 13.3 | \$ 101.6 |

(1) For additional information see the Non-GAAP Measures section.

The change in operating earnings between comparable periods in 2009 and 2008 is detailed below.

| \$ millions | For the three | For the six |
|--|---------------|-------------|
| | months | months |
| | ended | ended |
| | 2009 | 2009 |
| | June 30 | June 30 |
| Operating earnings from Block 7 in 2008 | \$ (16.2) | \$ (29.0) |
| Continuing operations: | | |
| Decrease in oil and gas prices | (34.2) | (71.9) |
| Decrease (increase) in depletion, amortization and accretion | 0.9 | (4.4) |
| Impact of stronger U.S. dollar | 6.6 | 16.5 |
| Other | (1.1) | 0.5 |
| Decrease in operating earnings, compared to 2008 | \$ (44.0) | \$ (88.3) |

Oil prices

| Prices | For the three months ended | | For the six months ended | |
|----------------------------------|----------------------------|----------|--------------------------|----------|
| | 2009 | 2008 | 2009 | 2008 |
| | June 30 | June 30 | June 30 | June 30 |
| Average-realized prices: | | | | |
| Cuba (\$/barrel) | \$ 43.18 | \$ 62.01 | \$ 39.40 | \$ 56.63 |
| Spain (\$/barrel) | 70.75 | 124.76 | 62.92 | 110.78 |
| Pakistan (\$/boe) ⁽¹⁾ | 7.90 | 7.36 | 8.41 | 7.21 |
| Reference price (U.S.\$/barrel) | | | | |
| Gulf Coast Fuel Oil No. 6 | 51.68 | 84.44 | 45.38 | 77.11 |
| Brent | 58.89 | 121.38 | 51.85 | 109.46 |

(1) Average-realized price for natural gas production is stated in barrels of oil equivalent (boe), which is converted at 6,000 cubic feet per boe.

The average-realized price for net oil production in Cuba decreased by \$18.83 per barrel in the second quarter and by \$17.23 per barrel for the first six months of 2009 as a result of lower oil reference prices, partially offset by a stronger U.S. dollar relative to the Canadian dollar. The average-realized price in Spain in the second quarter of 2009 was lower for the same reasons.

Production and sales

| Daily Production Volumes ⁽¹⁾⁽²⁾ | For the three months ended | | For the six months ended | |
|--|----------------------------|---------------|--------------------------|---------------|
| | 2009 | 2008 | 2009 | 2008 |
| | June 30 | June 30 | June 30 | June 30 |
| For the three months ended March 31 | | | | |
| Gross working-interest oil production in | | | | |
| Cuba ⁽³⁾⁽⁵⁾ | 20,167 | 33,813 | 20,923 | 32,409 |
| Net oil production ⁽⁴⁾ | | | | |
| Cuba (heavy oil) | | | | |
| Cost recovery ⁽⁵⁾ | 6,589 | 5,320 | 7,380 | 6,683 |
| Profit oil ⁽⁵⁾ | 5,510 | 11,879 | 5,498 | 10,653 |
| Total | 12,099 | 17,199 | 12,878 | 17,336 |
| Spain (light/ medium oil) ⁽⁴⁾ | 276 | 476 | 290 | 485 |
| Pakistan (natural gas) ⁽⁴⁾ | 382 | 385 | 376 | 392 |
| Total | 12,757 | 18,060 | 13,544 | 18,213 |

(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 delivered 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) For further information on gross working-interest oil production in Cuba, cost recovery, and profit oil see page 51 of the 2008 annual report.

In January 2009, Sherritt's joint operating partner, Peberco Limited, entered into an agreement with an agency of the Cuban government which resulted in the termination of the production-sharing contract related to Block 7. As a result, no Block 7 production was recorded in the first six months of 2009. Excluding Block 7, gross working-interest production in the second quarter of 2008 and for the first six months of 2008 was 24,925 bpd and 23,612 bpd, respectively.

Excluding Block 7, gross working-interest oil production in Cuba decreased by 4,758 bpd and 2,689 bpd in the second quarter and in the first six months of 2009, respectively, primarily due to the temporary suspension of development drilling activity during the fourth quarter of 2008 and the first quarter of 2009. Drilling activity resumed late in the first quarter of 2009.

Net production in Cuba in the second quarter of 2008, excluding Block 7, was 12,872 bpd including 4,366 bpd for cost recovery and 8,506 bpd for profit oil. Excluding Block 7, the cost recovery component of net production in Cuba increased by 2,223 bpd in the second quarter of 2009 due largely to a significant decrease in the price of oil. For the six months ended June 30, 2008, net production in Cuba, excluding Block 7, was 13,004 bpd and was made up of 5,648 bpd of cost recovery oil and 7,356 bpd of profit oil. The increase in cost recovery oil, excluding Block 7, for the first six months of 2009 was due mainly to the decrease in the oil price. The profit oil component of net production is Sherritt's contractual share of production after the cost recovery component is subtracted from gross working-interest production. Sherritt's average share of profit oil in Cuba was 46% and 43% for the second quarter of 2009 and for the first six months of 2009, respectively.

Production in Spain was lower due to natural reservoir declines and the impact of a series of workovers.

Operating costs

| Unit operating costs (\$/boe) ⁽¹⁾ | For the three months ended | | For the six months ended | |
|--|----------------------------|---------|--------------------------|---------|
| | 2009 | 2008 | 2009 | 2008 |
| | June 30 | June 30 | June 30 | June 30 |
| Cuba | \$ 7.87 | \$ 5.51 | \$ 8.48 | \$ 5.82 |
| Spain | 81.49 | 32.44 | 67.99 | 31.39 |
| Pakistan | 1.12 | 1.06 | 1.22 | 1.00 |
| Weighted-average | \$ 9.26 | \$ 6.13 | \$ 9.55 | \$ 6.39 |

(1) Excludes the impact of loss on disposal of Block 7 assets.

| Components of Unit Operating Costs - Cuba (%) | For the three months ended | | For the six months ended | |
|---|----------------------------|---------|--------------------------|---------|
| | 2009 | 2008 | 2009 | 2008 |
| | June 30 | June 30 | June 30 | June 30 |
| Cuba | | | | |
| Labour | 2% | 10% | 3% | 10% |
| Maintenance | 10% | 30% | 9% | 32% |
| Treatment and transportation | 42% | 38% | 44% | 36% |
| Other ⁽¹⁾ | 46% | 22% | 44% | 22% |
| | 100% | 100% | 100% | 100% |

(1) Comprised mainly of chemicals, insurance, yard maintenance costs and fuel.

Unit operating costs in Cuba increased by \$2.36 per barrel and \$2.66 per barrel in the second quarter and first six months of 2009, respectively, due largely to fixed operating costs being applied against a smaller production base following the termination of Block 7 and higher treatment and transportation rates. In addition, a retroactive adjustment to 2008 treatment and transportation rates was recorded during the first quarter of 2009.

Capital Spending

| Capital Spending \$ millions | For the three months ended | | For the six months ended | |
|---------------------------------|----------------------------|-----------------|--------------------------|-----------------|
| | 2009 June 30 | 2008 June 30 | 2009 June 30 | 2008 June 30 |
| Development and facilities | \$ 8.8 | \$ 21.9 | \$ 19.2 | \$ 44.6 |
| Exploration | 1.5 | 8.9 | 3.2 | 10.5 |
| Total | \$ 10.3 | \$ 30.8 | \$ 22.4 | \$ 55.1 |

In the second quarter of 2009, capital spending included \$3.1 million related to development drilling activities, \$2.0 million related to equipment, \$1.6 million related to workovers, and \$0.4 million with respect to facilities. In the first six months of 2009, capital spending included \$4.1 million related to development drilling activities, \$3.5 million related to equipment, \$1.9 million related to workovers and \$6.4 million related to facilities. Exploration costs were mainly related to advance costs for a well to be drilled offshore in Turkey and were net of funds received for the sale of one-half of Sherritt's interest in several licenses in Turkey. Sherritt retains a 21% interest in the licenses. The first exploration well in Turkey commenced drilling early in the third quarter of 2008.

Reduced expenditures in 2009 reflect the suspension of drilling activity in Cuba up to the end of the first quarter of 2009. In the second quarter of 2009, three development wells were initiated and one development well was completed.

Outlook for 2009

| Production volumes and capital expenditures | Actual 2009 June 30 | Projected 2009 December 31 |
|---|---------------------------|----------------------------------|
| Production | | |
| Gross working-interest oil (Cuba) (bpd) | 20,923 | 21,000 |
| Net oil production, all operations (bpd) ⁽¹⁾ | 13,544 | 13,000 |
| Capital Expenditures (\$ millions) | | |
| Cuba | \$ 18 | \$ 119 |
| Other | \$ 5 | \$ 16 |

(1) Net oil production predicated on the WTI/Fuel Oil No. 6 price differential remaining consistent with historical levels.

In Oil and Gas, the extent of the drilling program in 2009 will be dictated largely by the receipt of payments in Cuba. The reduction in second-quarter guidance for full-year 2009 GWI production in Cuba to 21,000 bpd is due to a decrease in expected production from new wells in 2009. The reduction in the second-quarter guidance for full-year 2009 net production to 13,000 boepd results mainly from the decrease in the gross working-interest production in Cuba. Plans for an enhanced oil recovery pilot project in Cuba have been delayed pending the issuance of required permits. In July, drilling was initiated on an exploratory well in Turkey which is expected to be completed in third-quarter 2009.

Review of operations - Power

Financial data

| \$ millions | For the three months ended | | For the six months ended | |
|---------------------------------------|----------------------------|---------|--------------------------|---------|
| | 2009 | 2008 | 2009 | 2008 |
| | June 30 | June 30 | June 30 | June 30 |
| Revenue | | | | |
| Electricity sales | \$ 25.0 | \$ 23.3 | \$ 52.3 | \$ 47.9 |
| By-products and other | 3.6 | 7.0 | 6.7 | 12.2 |
| | 28.6 | 30.3 | 59.0 | 60.1 |
| Operating costs | (7.8) | (6.7) | (17.4) | (11.8) |
| General and administrative costs | (1.1) | (0.7) | (2.2) | (1.6) |
| EBITDA ⁽¹⁾ | 19.7 | 22.9 | 39.4 | 46.7 |
| Depletion, amortization and accretion | (7.7) | (7.2) | (15.3) | (14.7) |
| Operating earnings ⁽¹⁾ | \$ 12.0 | \$ 15.7 | \$ 24.1 | \$ 32.0 |

(1) For additional information see the Non-GAAP Measures section.

The change in operating earnings between comparable periods in 2009 and 2008 is detailed below.

| \$ millions | For the three | For the six |
|---|---------------|-------------|
| | months | months |
| | ended | ended |
| | 2009 | 2009 |
| | June 30 | June 30 |
| Higher realized electricity prices, denominated in Canadian dollars | \$ 3.3 | \$ 8.6 |
| Lower by-products prices | (3.3) | (5.6) |
| Lower electricity and by-products sales volumes | (3.4) | (5.5) |
| Higher maintenance costs | (1.1) | (2.9) |
| Higher costs related to turbine rotor overhaul | - | (2.7) |
| Other | 0.8 | 0.2 |
| Decrease in operating earnings, compared to 2008 | \$ (3.7) | \$ (7.9) |

Electricity Prices

| Prices (\$/MWh) ⁽¹⁾ | For the three months ended | | For the six months ended | |
|--------------------------------|----------------------------|----------|--------------------------|----------|
| | 2009 | 2008 | 2009 | 2008 |
| | June 30 | June 30 | June 30 | June 30 |
| Average-realized price | \$ 47.93 | \$ 40.83 | \$ 49.23 | \$ 40.72 |

(1) Megawatt hours (MWh).

The average-realized price of electricity increased \$7.10 per MWh in the second quarter and \$8.51 per MWh for the first six months of 2009 primarily due to a stronger U.S. dollar relative to the Canadian dollar.

During the second quarter and first six months of 2009, by-product revenue decreased compared to the same periods in the prior year mainly a result of lower commodity prices, which are linked to market prices for petroleum products.

Production and sales

| Production/Sales | For the three months ended | | For the six months ended | |
|--|----------------------------|---------|--------------------------|---------|
| | 2009 | 2008 | 2009 | 2008 |
| | June 30 | June 30 | June 30 | June 30 |
| Electricity sold ⁽¹⁾ (GWh) ⁽²⁾ | 515 | 567 | 1,056 | 1,164 |

(1) Including non-controlling interest's share.

(2) Gigawatt hours (GWh).

Electricity sales volume decreased 52 GWh and 108 GWh in the second quarter and for the first six months of 2009, respectively, due to several turbine failures and an increase in scheduled maintenance compared to the same periods in the prior year. All of the affected turbines returned to service by the end of June.

Operating costs

| Unit operating costs (\$/MWh) | For the three months ended | | For the six months ended | |
|-------------------------------|----------------------------|----------|--------------------------|----------|
| | 2009 | 2008 | 2009 | 2008 |
| | June 30 | June 30 | June 30 | June 30 |
| Operating cost | \$ 15.14 | \$ 11.80 | \$ 16.49 | \$ 10.13 |

| Components of Unit Operating Costs (%) | For the three months ended | | For the six months ended | |
|--|----------------------------|-------------|--------------------------|-------------|
| | 2009 | 2008 | 2009 | 2008 |
| | June 30 | June 30 | June 30 | June 30 |
| Labour | 36% | 40% | 33% | 45% |
| Maintenance | 49% | 43% | 57% | 36% |
| Other ⁽¹⁾ | 15% | 17% | 10% | 19% |
| Total | 100% | 100% | 100% | 100% |

(1) Comprised mainly of insurance, freight and duty.

Unit operating costs increased by \$3.34 per MWh in the second quarter of 2009 and \$6.36 per MWh in the first six months of 2009 due to higher costs and lower production resulting primarily from turbine failures and scheduled maintenance.

Capital Spending

| Capital Spending | For the three months ended | | For the six months ended | |
|------------------|----------------------------|---------------|--------------------------|----------------|
| | 2009 | 2008 | 2009 | 2008 |
| | June 30 | June 30 | June 30 | June 30 |
| \$ millions | | | | |
| Sustaining | \$ 6.8 | \$ 2.9 | \$ 8.1 | \$ 4.6 |
| Growth | 3.2 | 4.6 | 10.9 | 6.7 |
| Total | \$ 10.0 | \$ 7.5 | \$ 19.0 | \$ 11.3 |

Growth capital spending of \$3.2 million in the second quarter of 2009 and \$10.9 million in the first six months of 2009 related mainly to construction activity and equipment purchases for the 25 MW project in Madagascar as well as engineering and infrastructure preparation for the 150 MW combined cycle project in Cuba.

Outlook for 2009

| Production volumes and capital expenditures | Actual 2009 | Projected 2009 |
|---|----------------|-------------------|
| For the six and twelve months ended | June 30 | December 31 |
| Production | | |
| Electricity (GWh) | 1,056 | 2,000 |
| Capital Expenditures (\$ millions) | | |
| Cuba | \$ 14 | \$ 45 |
| Madagascar | \$ 5 | \$ 19 |

In Power, all issues related to the two turbine failures that occurred in first-quarter 2009 have been corrected, and all turbines are available for operation. A major steam turbine overhaul is scheduled for fourth-quarter 2009 and is not expected to have a significant impact on production. Full-year 2009 production is expected to reach 2,000 GWh. The turbine failures in the first quarter necessitated repairs that increased operating costs during the first two quarters of 2009, and as a result full-year 2009 unit operating costs are expected to be higher than in 2008. The 150 MW Boca de Jaruco Combined Cycle Project in Cuba continues to be reviewed in light of current economic conditions. Sherritt will continue with engineering and progress payments to maintain the Project option value while it is under review. Due to delays in equipment delivery, the 25 MW Madagascar Thermal Power Project is now expected to be operational in August 2009 compared with the previous guidance for end of June 2009.

Review of operations - Other

Technologies

For the three and six month periods ended June 30, 2009, Technologies generated revenue of \$2.1 million and \$5.5 million, respectively, as compared with \$5.2 million and \$7.9 million for the same periods in the prior year

Revenue decreased in the current second quarter and the first six months of 2009 largely due to a reduction of \$1.6 million and \$0.7 million, respectively, in licensing revenue compared with the same periods in the prior year. In addition, revenues are lower in the current periods as a result of decreased demand for services related to the current global economic conditions.

The Clean Coal Technology Centre, which develops processes for cleaning and upgrading western Canadian lignite and sub-bituminous coals, that was originally scheduled to be commissioned by the end of the second quarter of 2009 will now be commissioned in the third quarter of 2009 due to equipment delivery delays.

Liquidity and financial condition

Liquidity

In light of current economic conditions and continued depressed commodity prices, our increased focus on managing liquidity continues. The primary factors affecting our liquidity and how we manage capital are described in detail in our annual MD&A for the year ended December 31, 2008. Management believes that the Corporation will be able to satisfy its current and long-term debt obligations as they come due based on its financial position and liquidity profile at June 30, 2009.

Sources and uses of cash

| \$ millions | For the three months ended | | For the six months ended | |
|--|----------------------------|-----------------|--------------------------|-----------------|
| | 2009 June 30 | 2008 June 30 | 2009 June 30 | 2008 June 30 |
| Cash from operating activities | | | | |
| Cash from operating activities before change in non-cash working capital | \$ 105 | \$ 154 | \$ 192 | \$ 284 |
| Change in non-cash working capital | (57) | (134) | (48) | (114) |
| Cash (used for) provided by discontinued operation | (1) | 1 | (2) | 3 |
| Cash provided by operating activities | \$ 47 | \$ 21 | \$ 142 | \$ 173 |
| Cash from investing and financing | | | | |
| Cash capital spending | \$ (321) | \$ (607) | \$ (730) | \$ (900) |
| Short-term debt borrowings (repayments) | (3) | (53) | 50 | (53) |
| Long-term debt borrowings (net of repayments) | 296 | 901 | 376 | 917 |
| Funding from Ambatovy Joint Venture partners | 216 | 6 | 571 | 65 |
| Royal Utilities acquisition | - | (240) | - | (240) |
| Issuance of common shares | - | 33 | - | 417 |
| Dividends paid on common shares | (11) | (9) | (21) | (18) |
| Change in other assets | 1 | (25) | 3 | (70) |
| Other | 1 | 11 | 18 | (1) |
| | \$ 179 | \$ 17 | \$ 267 | \$ 117 |
| Increase in cash and short-term investments | \$ 226 | \$ 38 | \$ 409 | \$ 290 |
| Cash, cash equivalents, and short-term investments | | | | |
| Beginning of period | \$ 790 | \$ 711 | \$ 607 | \$ 459 |
| End of period | \$ 1,016 | \$ 749 | \$ 1,016 | \$ 749 |

Factors affecting operating cash flow

Operating cash flow for the second quarter and first six months of 2009 was significantly impacted by the reduction in earnings. The receipt of funds on the overdue 2008 Oil and Gas and Power receivables in the first quarter of 2009 of approximately US\$161.0 million had a minimal impact on our overall cash position as the Corporation was required to purchase an approximately-equal amount of certificates of deposit.

In June 2009, we completed the sale of our interest in two hotels in Cuba for gross proceeds of \$14.0 million.

Short-term facilities

In May 2009, the Corporation amended the terms of the \$140.0 million Syndicated 364-day revolving-term credit facility and the \$20.0 million 6-month liquidity line of credit. The terms of the \$40.0 million 364-day liquidity line of credit automatically track these changes. Under the terms of the amended agreements, the loans are subject to the following financial covenants: financial debt-to-equity less than 0.5:1; quarterly adjusted net financial debt-to-EBITDA not exceeding between 2.5:1 and 3.9:1 depending on the quarter; and EBITDA-to-interest greater than 3:1. The interest rate on the Syndicated 364-day revolving-term credit facility was amended to prime plus a margin of 3% per annum or Bankers Acceptances plus a margin of 4% and the facility expires on May 10, 2010.

Ambatovy Project financing

There were no amounts drawn on this facility during the second quarter. At June 30, 2009, a total of \$1,244.0 million had been drawn on this facility. Our 40% proportionate share of this amount is \$498.0 million.

Ambatovy Joint Venture additional partner loan agreements

On June 24, 2009, Sherritt finalized arrangements with its Ambatovy partners, Sumitomo, Kores and SNC-Lavalin for a mechanism to fund Sherritt's pro rata share of shareholder funding for the Ambatovy Project (the Ambatovy Joint Venture additional partner loans).

These additional loans are not committed except for a commitment of US\$22.9 million to offset a reduction in amounts available under the Ambatovy Joint Venture partner loans. They are non-recourse to Sherritt except in circumstances where there is a direct breach by Sherritt of restrictions in the loan documents, which limit the activities of certain subsidiaries and the use of proceeds from the loans to the Ambatovy Project.

Interest and principal on these loans will be repaid solely through Sherritt's share of the distributions from the Ambatovy Joint Venture. However, Sherritt has the right to prepay some or all of the loans at its option. Until the Ambatovy Joint Venture partner loans and the Ambatovy Joint Venture additional partner loans are fully repaid, 100% of Sherritt's distributions from the Ambatovy Project will be applied to these loans. Initially, 75% of Sherritt's share of distributions will be applied to the Ambatovy Joint Venture additional partner loans and 25% will be applied to the Ambatovy Joint Venture partner loans with 100% of such distributions being applied to whichever loans remain outstanding when one has been repaid in full.

Each lender has the right to exchange some or all of its Ambatovy Joint Venture additional partner loans for up to a maximum 15% equity interest, in aggregate, in the Project at any time. Exercise of this right in full would reduce Sherritt's interest in the Project to 25%. This right is subject to senior project lender consent and Sherritt's right to repay the loans and avoid the reduction in its equity interest. If the capital costs of the Project were to exceed US\$4.52 billion and Sherritt did not provide its pro rata share of funding for the cost overrun, the partners could dilute Sherritt's interest in the Project below the 25% threshold. There are no other penalties to Sherritt for a failure to fund its pro rata share of shareholder funding.

These loans carry interest at a rate of LIBOR plus 7% per annum. The interest charges on the Ambatovy Joint Venture additional partner loans will be capitalized to deferred development costs as the Project is constructed.

At June 30, 2009, the Corporation had borrowed \$342.5 million under this facility.

In conjunction with the Ambatovy Joint Venture additional partner loans, Sherritt received additional completion guarantee protection as related to the US\$2.1 billion senior project financing facility. Sherritt's pro rata share of these completion guarantees is US\$840.0 million

and, under existing arrangements, US\$598.0 million of Sherritt's obligations have been cross-guaranteed by the other partners. Under the new agreements, the other Project partners have agreed to provide letters of credit to the senior lenders to cover any guarantee obligation of Sherritt not covered by the existing cross-guarantees.

The Project's US\$2.1 billion senior project financing is unaffected by these arrangements.

Ambatovy Joint Venture partner loans

As a condition for providing funding under the Ambatovy Joint Venture additional partner loan agreements (described above), the Corporation was required to repay from the proceeds of the new loans US\$50.0 million of the existing Ambatovy Joint Venture partner loans such that the principal amount of the original loans are US\$85.4 million at June 30, 2009. Including accrued interest, \$100.7 million was outstanding on these loans at June 30, 2009. The advances that are outstanding at June 30, 2009 continue to bear interest at a rate of LIBOR plus an applicable margin of 1.125%. There is no intention to borrow additional amounts under these loan agreements. Additional advances on these loans are subject to interest at a rate of LIBOR plus an applicable margin of 10% per annum. As well, the interest and principal which is to be repaid from Sherritt's share of the distributions from the Ambatovy Joint Venture is reduced from 70% to 25%.

3-year non-revolving term facility

On March 31, 2009, Coal Valley Resources Inc. (CVRI), a subsidiary of the Coal Valley Partnership, in which the Corporation has a 50% interest, established a new non-revolving term credit facility with a Canadian financial institution to finance the purchase of certain equipment and to provide working capital in relation to the start-up of the Obed mine. The facility consists of two loans totaling \$38.0 million (100% basis) and is subject to fixed interest rates. The loans are subject to equal blended monthly payments after a six-month interest-only period following the first advance. The loans are subject to the following financial covenants based on the financial condition of CVRI: debt to tangible net worth ratio not greater than 2.5:1; current ratio of not less than 1:1; and cash flow coverage ratio not less than 1.25:1. Sherritt and its partner have each provided a \$12.5 million limited guarantee in relation to these loans. To June 30, 2009, CVRI received advances of \$38.0 million (100% basis) under this facility at an average interest rate of 6.08% per annum.

Coal - lease market

As a result of a difficult lease financing market, Coal has continued to use working capital or other credit facilities to fund purchases of certain equipment that it would have previously leased. As a result, in the three and six months ended June 30, 2009, Coal purchased approximately \$9.0 million and \$18.9 million, respectively, of equipment using working capital. A letter of intent has been signed with a leasing company to provide lease financing for \$11.0 million of equipment that has already been funded using working capital. For the balance of the year, in the absence of available lease financing under acceptable terms, an additional \$9.0 million of equipment that previously would have been leased may be purchased using working capital or other credit facilities

Short form prospectus

On June 18, 2009, the Corporation filed a Final Short Form Base Shelf Prospectus to enable it to offer, from time to time, for sale and issue up to \$500.0 million in aggregate offering amount (or the equivalent in other currencies) of (i) unsecured debt securities, (ii) common shares, (iii) subscription receipts and (iv) warrants (collectively, the Securities). The Securities may be offered separately, or together, in separate series, in amounts, at prices and on terms to be set forth in one or more accompanying shelf prospectus supplements.

Covenants

The Corporation and its affiliates were in compliance with their financial covenants as at June 30, 2009. Other than the covenants required for the debt facilities, the Corporation is not subject to any externally imposed capital restrictions.

The Corporation expects to remain in compliance with all of its financial covenants during the next twelve months, based on current market conditions.

Contractual commitments and obligations

The Corporation's significant contractual commitments and obligations and the principal repayments thereon are presented in the following table:

| \$ millions, as at | Total | Year 1 | Year 2 | Year 3 | Year 4 | Year 5 | Year 6 and thereafter |
|------------------------------|------------|----------|----------|----------|----------|----------|-----------------------|
| Capital commitments | \$ 845.9 | \$ 719.7 | \$ 126.0 | \$ 0.2 | \$ - | \$ - | \$ - |
| Long-term debt | 2,793.6 | 27.2 | 25.4 | 160.1 | 353.7 | 111.4 | 2,115.8 |
| Capital leases and other | | | | | | | |
| equipment financing | 120.3 | 38.0 | 30.6 | 23.6 | 18.3 | 9.8 | - |
| Operating leases | 66.2 | 14.1 | 13.6 | 9.8 | 7.5 | 6.3 | 14.9 |
| Pension obligations | 74.5 | 7.2 | 7.2 | 7.3 | 7.3 | 7.3 | 38.2 |
| Asset-retirement obligations | - | - | - | - | - | - | - |
| | 405.2 | 27.1 | 23.3 | 18.7 | 87.2 | 87.0 | 161.9 |
| Total | \$ 4,305.7 | \$ 833.3 | \$ 226.1 | \$ 219.7 | \$ 474.0 | \$ 221.8 | \$ 2,330.8 |

Significant commitments include:

- \$820.3 million related to capital for the Ambatovy Joint Venture.
- \$212.1 million for purchasing and leasing equipment, office space, vehicles, and services

Financial condition

Cash and short-term investments

Cash, cash equivalents and short-term investments at June 30, 2009 were \$1.0 billion. Our policy is to invest available excess cash in highly liquid investments of the highest credit quality in a given marketplace and to limit our exposure to individual counterparties in order to minimize risks associated with these investments. Our principal guideline is to maximize our investments in Government of Canada treasury bills. The Corporation's joint venture entities maintain their own investment policies, but where possible, these policies are aligned with those of the Corporation. The maximum duration of any investment is one year; however, decisions regarding the length of maturities are based on our cash flow requirements, rates of return and other factors.

As at June 30, 2009, cash and cash equivalents and short-term investments were held in:

Canada: \$691 million (invested primarily in Government of Canada treasury bills)

Cuba: \$46 million (invested primarily in cash deposit accounts)

Other: \$279 million (majority to be used for the Ambatovy project and invested primarily in cash deposit accounts)

At June 30, 2009, included in cash, cash equivalents and short-term investments was \$341.7 million of cash held by the Ambatovy Joint Venture (100% basis) and \$29.0 million held by the Moa Joint Venture (50% basis). These funds are for the use of each joint venture, respectively.

For accounting purposes, the Cuban certificates of deposit are not considered cash, cash equivalents or short-term investments but are recorded as long-term investments with the principal amount receivable within twelve months of June 30, 2009 classified as current on our balance sheet.

Share Capital

As at July 24, 2009, the Corporation had 293,051,276 common shares outstanding. An additional 4,743,335 common shares are issuable upon exercise of outstanding stock options granted to employees and directors pursuant to the Corporation's stock option plan.

An additional 2,829,830 common shares are issuable in relation to the cross-guarantees provided by certain Ambatovy Joint Venture partners. These shares are to be issued in approximately equal amounts on each December 31 of 2009 to 2011.

The Board of Directors of the Corporation approved a quarterly dividend of \$0.036 per share that was paid July 14, 2009 to shareholders of record at the close of business on June 30, 2009.

Managing risk

Sherritt manages a number of risks in each of its businesses in order to achieve an acceptable level of risk without hindering its ability to maximize returns. Management has procedures to identify and manage significant operational and financial risks. Strategies designed to manage the Corporation's significant business risks are discussed in the Corporation's Annual Information Form for the year ended December 31, 2008 (AIF) filed on SEDAR at www.sedar.com and on the Corporation's website at www.sherritt.com. We have updated the disclosure appearing in our 2008 AIF with the following:

Political unrest in Madagascar

The Ambatovy Project was developed in accordance with Madagascar's Large Mining Investment Act, *Loi sur les Grands Investissements Miniers*, (LGIM), which provides, among other things, for favourable tax, customs and royalty regimes and recourse to international arbitration. Andry Rajoelina, the President of the Transition Authority, has spoken publicly of reviewing the country's agreements with foreign resource companies to ensure the country is receiving its "fair share" of royalties from the exploitation of Malagasy resources. A French law firm engaged by the President has advanced arguments that the Ambatovy Project's LGIM eligibility certification may be invalid. The Ambatovy Project companies and their legal advisors categorically reject this position. At June 30, 2009 the government had not taken any action and no formal announcement regarding the review or findings of the review were released publicly.

It is unclear at this time if the review will have an impact on the Ambatovy Project.

Changes in accounting policies and accounting pronouncements

Changes in accounting policies

Goodwill and other Intangible Assets

Effective January 1, 2009 the Corporation adopted the new recommendations of the Canadian Institute of Chartered Accountants (CICA) Handbook Section 3064, "Goodwill and Intangible Assets", which replaced Handbook Section 3062, "Goodwill and Other Intangible Assets" and Section 3450, "Research and Development Costs". The new standard provides guidance on the recognition, measurement, presentation and disclosure of goodwill and intangible assets subsequent to their initial recognition. The adoption of this new standard did not have a significant impact on our interim consolidated financial statements.

Credit Risk and the Fair Value of Financial Assets and Financial Liabilities

In January 2009, the CICA issued EIC-173, "Credit Risk and the Fair Value of Financial Assets and Financial Liabilities" which requires the Corporation to consider its own credit risk as well as the credit risk of its counterparty when determining the fair value of financial assets and liabilities, including derivative instruments. The accounting treatments provided in EIC-173 have been applied in the preparation of these financial statements and as required have been applied retrospectively without restatement of prior periods. The adoption of this standard did not have an impact on the valuation of our financial assets or liabilities.

Mining Exploration Costs

In March 2009, the CICA issued EIC-174, "Mining Exploration Costs" which provides guidance to mining enterprises related to the accounting and the conditions that a mining enterprise should consider when determining the need to perform an impairment review of such costs. The accounting treatments provided in EIC-174 have been applied in the preparation of these financial statements and did not have an impact on the valuation of our exploration assets.

Accounting pronouncements

Convergence with International Financial Reporting Standards

The Canadian Accounting Standards Board (AcSB) requires all Canadian publicly accountable entities to adopt International Financial Reporting Standards (IFRS) for years beginning on or after January 1, 2011. The Corporation's first mandatory filing under IFRS, which will be the first quarter of 2011, will contain IFRS-compliant financial statements on a comparative basis, as well as reconciliations for that quarter and as at the January 1, 2010 transition date. Although IFRS uses a conceptual framework similar to Canadian GAAP, there are significant differences in recognition, measurement and disclosure.

The Corporation's plan for IFRS convergence is described in our 2008 annual report. We are currently engaged in the design and build phase (phase 2) of the plan, which includes an in-depth analysis of issues and accounting policy choices, designing the control framework necessary to support the IFRS reporting environment and assessing the impact of IFRS on business policies. Steps to completion of each of these key elements are underway with completion targeted for the fourth quarter of 2009. On-going training is another key aspect of the IFRS convergence project. The Corporation has conducted several training sessions with project team members and will continue to provide on-going training to accounting personnel and senior management.

Business Combinations/Consolidated Financial Statements/Non-Controlling Interests

In January 2009, the CICA issued sections 1582, "Business Combinations", 1601, "Consolidated Financial Statements", and 1602, "Non-Controlling Interests" which superseded current sections 1581, "Business Combinations" and 1600 "Consolidated Financial Statements". These new sections replace existing guidance on business combinations and consolidated financial statements to harmonize Canadian accounting for business combinations with IFRS. These sections will be applied prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after January 1, 2011. Earlier adoption is permitted. If an entity applies these sections before January 1, 2011, it is required to disclose that fact and apply each of the new sections concurrently. The Corporation is currently evaluating the impact of the adoption of these changes on its consolidated financial statements.

Supplementary information

Sensitivity analysis

The following table shows the approximate impact on the Corporation's second quarter 2009 net earnings and EPS of a change in selected key variables. The impact is measured changing one variable at a time and may not necessarily be indicative of sensitivities on future results.

| Factor | Increase | Approximate change in Q2 net earnings (\$ millions) Increase/(decrease) | Approximate quarterly change in basic EPS (\$) |
|--|--------------|---|---|
| Prices | | | |
| Nickel - LME price per pound | U.S.\$ 0.10 | 0.7 | - |
| Cobalt - Metal Bulletin price per pound | U.S.\$ 1.00 | 0.7 | - |
| Oil -U.S. Gulf Coast Fuel Oil No. 6 price per barrel | U.S.\$ 0.50 | 0.4 | - |
| Volume | | | |
| Nickel - tonnes | 1,000 | 1.9 | 0.01 |
| Cobalt - tonnes | 100 | 0.8 | - |
| Oil - barrels per day | 1,000 | 3.0 | 0.01 |
| Electricity production - MWh | 25,000 | 0.5 | - |
| Exchange Rate | | | |
| US dollar per Canadian dollar | U.S.\$ 0.05 | (7.6) | (0.03) |
| Operating costs | | | |
| Natural Gas - cost per gigajoule (Metals) | \$ 1.00 | (1.6) | (0.01) |
| Sulphur - cost per tonne (Metals) | U.S.\$ 10.00 | (0.2) | - |
| Sulphuric acid - cost per tonne (Metals) | U.S.\$ 10.00 | (0.5) | - |
| Fuel - WTI oil price (Coal Mountain Operations) | U.S.\$ 10.00 | (2.2) | (0.01) |

Non-GAAP measures

The Corporation's definition of EBITDA is earnings or loss from continuing operations as reported in the GAAP financial statements, excluding net earnings or net loss related to any non-controlling interest, amounts included in net earnings or net loss for income taxes, interest expense, depletion, amortization, accretion, depreciation, impairment charges for property, plant and equipment, goodwill and investments, and gain or loss on disposal of property, plant and equipment.

The Corporation's definition of Operating earnings is EBITDA less depletion, amortization and accretion expense and depreciation included in operating expenses.

The table below presents EBITDA and Operating earnings and reconciles these non-GAAP measures to earnings from continuing operations before income taxes and non-controlling interests.

| \$ millions | For the three months ended | | For the six months ended | |
|---|----------------------------|-----------------|--------------------------|-----------------|
| | 2009 June 30 | 2008 June 30 | 2009 June 30 | 2008 June 30 |
| Revenue | \$ 357.7 | \$ 441.2 | \$ 706.7 | \$ 755.4 |
| Operating, selling and general and administrative expenses | 266.6 | 263.4 | 538.0 | 406.9 |
| | 91.1 | 177.8 | 168.7 | 348.5 |
| Add: Depreciation included in operating expenses | 21.1 | 12.6 | 40.7 | 17.6 |
| EBITDA | 112.2 | 190.4 | 209.4 | 366.1 |
| Less: | | | | |
| Depreciation included in operating expenses | 21.1 | 12.6 | 40.7 | 17.6 |
| Depletion, amortization and accretion | 38.7 | 51.5 | 87.7 | 86.2 |
| Operating earnings | 52.4 | 126.3 | 81.0 | 262.3 |
| Loss on disposal of property, plant and equipment and investments | - | - | 79.5 | - |
| Net financing expense | 15.9 | 13.5 | 13.8 | 12.6 |
| Share of earnings of equity-accounted investment | - | (3.0) | - | (9.4) |
| Other items | (0.7) | - | 1.5 | - |
| Earnings (loss) from continuing operations before income taxes and non-controlling interests | \$ 37.2 | \$ 115.8 | \$ (13.8) | \$ 259.1 |

The Corporation is the primary beneficiary of two Variable Interest Entities (VIEs) as defined under CICA Accounting Guideline 15. The Corporation holds an indirect 40% interest in the equity of a VIE, the Ambatovy Joint Venture, and in accordance with Canadian GAAP, the accounts of the Ambatovy Joint Venture are consolidated and the 60% equity interests of the other shareholders are accounted for as non-controlling interests. The Corporation also holds an indirect one-third interest in the equity of another VIE, Energas S.A., and in accordance with Canadian GAAP, the accounts of Energas S.A. are consolidated. The two-thirds equity interests of the other shareholders are accounted for as non-controlling interests.

Given the magnitude of these VIEs relative to the Corporation's total asset base, certain shareholders and other stakeholders have requested additional information that will help them better understand the Corporation's economic interest in and exposure to these VIEs.

To address these concerns, the Corporation has prepared an adjusted balance sheet that includes the Corporation's proportionate interest in these VIEs. The adjusted balance sheet has been prepared using an arithmetic formula and does not represent proportionate consolidation under Canadian GAAP. The adjusted balance sheet has also been condensed in order to better illustrate key financial statement line items of interest to investors and management. The adjusted balance sheet does not have a standardized meaning under Canadian GAAP and is not to be used to compare the Corporation to other companies. An investor may find this information useful in analyzing our financial information but it should not be considered in isolation or as a substitute for any information prepared in accordance with Canadian GAAP.

The adjusted balance sheet provides both investors and management with information to help better understand the Corporation's economic interest in key financial statement line items. Management also reviews key financial statement line items on this adjusted basis.

We have reconciled our adjusted balance sheet to the condensed Canadian GAAP balance sheet at June 30, 2009. This reconciliation provides a concise view of the impact of these VIEs on the Corporation's balance sheet by clearly identifying the adjustments related to each VIE by financial statement line item.

| | Less: | | | Add: | | Adjusted |
|--|--------------------|---------------------|-------------------|------------------------|-----------------|-------------------|
| | GAAP | Consolidated amount | Energas S.A | Proportionate Interest | Energas S.A | |
| \$ millions, as at June 30, 2009 | Balance Sheet | Ambatovy 100% | 100% | Ambatovy 40.0% | 33.33% | Balance Sheet |
| ASSETS | | | | | | |
| Cash, cash equivalents, short-term investments | \$ 1,015.9 | \$ (341.7) | \$ (8.0) | \$ 136.7 | \$ 2.7 | \$ 805.6 |
| Other current assets | 660.0 | (23.2) | (53.2) | 9.2 | 17.8 | 610.6 |
| Property, plant and equipment | 7,059.0 | (4,893.6) | (450.9) | 1,957.4 | 150.3 | 3,822.2 |
| Other | 1,341.7 | (3.8) | (25.1) | 1.6 | 8.3 | 1,322.7 |
| | \$ 10,076.6 | \$ (5,262.3) | \$ (537.2) | \$ 2,104.9 | \$ 179.1 | \$ 6,561.1 |
| LIABILITIES AND SHAREHOLDERS' EQUITY | | | | | | |
| Current liabilities | 814.1 | (457.5) | (44.0) | 183.0 | 14.7 | 510.3 |
| Long-term debt and other long-term liabilities | 2,788.1 | (1,185.3) | - | 474.2 | - | 2,077.0 |
| Other | 731.3 | (359.2) | (190.8) | 142.2 | 63.6 | 387.1 |
| | 4,333.5 | (2,002.0) | (234.8) | 799.4 | 78.3 | 2,974.4 |
| Non-controlling interests | 2,156.4 | (1,954.8) | (201.6) | - | - | - |
| Shareholders' equity | 3,586.7 | (1,305.5) | (100.8) | 1,305.5 | 100.8 | 3,586.7 |
| | \$ 10,076.6 | \$ (5,262.3) | \$ (537.2) | \$ 2,104.9 | \$ 179.1 | \$ 6,561.1 |

Summary of quarterly results

The following table presents a summary of the segments and consolidated operating results for each of the eight quarters from September 2007 to June 2009.

| | 2009 | 2009 | 2008 | 2008 | 2008 | 2008 | 2007 | 2007 |
|--|-----------|-----------|-------------|--------------|-----------|----------|-------------|--------------|
| \$ millions, except per share amounts, for the three months ended | June 30 | March 31 | December 31 | September 30 | June 30 | March 31 | December 31 | September 30 |
| Revenue | | | | | | | | |
| Metals | \$ 111.1 | \$ 79.7 | \$ 96.0 | \$ 137.5 | \$ 177.7 | \$ 162.3 | \$ 176.9 | \$ 150.7 |
| Coal ⁽¹⁾ | 165.7 | 188.9 | 200.7 | 189.9 | 124.5 | 30.9 | 23.2 | 28.1 |
| Oil and Gas | 50.2 | 46.6 | 44.9 | 112.9 | 104.5 | 87.5 | 85.9 | 81.5 |
| Power | 28.6 | 30.4 | 31.8 | 30.9 | 30.3 | 29.8 | 29.9 | 31.6 |
| Corporate and other | 2.1 | 3.4 | 5.6 | 6.0 | 4.2 | 3.7 | 7.7 | 9.4 |
| | \$ 357.7 | \$ 349.0 | \$ 379.0 | \$ 477.2 | \$ 441.2 | \$ 314.2 | \$ 323.6 | \$ 301.3 |
| Earnings (loss) from continuing operations | 25.7 | (42.1) | (591.6) | 135.4 | 80.8 | 89.2 | 83.1 | 66.1 |
| Earnings (loss) from discontinued operation(s) | (1.3) | (0.8) | (0.5) | (2.3) | (0.5) | (0.2) | 0.4 | (0.7) |
| Net earnings (loss) | \$ 24.4 | \$ (42.9) | \$ (592.1) | \$ 133.1 | \$ 80.3 | \$ 89.0 | \$ 83.5 | \$ 65.4 |
| Earnings (loss) from continuing operation(s) per share | | | | | | | | |
| Basic | \$ 0.09 | \$ (0.15) | \$ (2.03) | \$ 0.46 | \$ 0.29 | \$ 0.38 | \$ 0.36 | \$ 0.28 |
| Diluted | \$ 0.09 | \$ (0.15) | \$ (2.03) | \$ 0.46 | \$ 0.28 | \$ 0.38 | \$ 0.36 | \$ 0.28 |
| Loss from discontinued operation(s) per share | | | | | | | | |
| Basic | \$ (0.01) | \$ - | \$ - | \$ (0.01) | \$ (0.01) | \$ - | \$ - | \$ - |
| Diluted | \$ (0.01) | \$ - | \$ - | \$ (0.01) | \$ - | \$ - | \$ - | \$ - |
| Earnings (loss) per share | | | | | | | | |
| Basic | \$ 0.08 | \$ (0.15) | \$ (2.03) | \$ 0.45 | \$ 0.28 | \$ 0.38 | \$ 0.36 | \$ 0.28 |
| Diluted | \$ 0.08 | \$ (0.15) | \$ (2.03) | \$ 0.45 | \$ 0.28 | \$ 0.38 | \$ 0.36 | \$ 0.28 |

(1) Coal's results include the Corporation's 100% interest in Royal Utilities from the date of acquisition, May 2, 2008, and the Corporation's 50% proportionate interest in the Coal Valley export thermal coal mine and other coal development assets. In the periods prior to May 2, 2008, Royal Utilities was equity-accounted.

Operating results for the Corporation before the inclusion of unusual items are affected, primarily, by changes in commodity prices and exchange rates that impact revenue and costs. Also, during the last five quarters, our results included the consolidation of Royal Utilities from the date of acquisition, May 2, 2008. During the most recent three quarters, the Corporation's results were significantly impacted by a reduction in nickel, cobalt and oil and gas prices. In the first quarter of 2009, the Corporation recognized a loss on the disposal of Block 7 assets of \$79.5 million (\$57.4 million after tax). As a result of the weakened economic environment in the fourth quarter of 2008, the Corporation recognized \$590.7 million in unusual costs, including the impairment of goodwill related to the Ambatovy Joint Venture and impairment of certain Cuban accounts receivable balances.

Transactions with related parties

During the second quarter of 2009, the Corporation engaged in the following related-party transactions resulting in the balances at June 30, 2009 below:

| \$ millions | For the six months ended | |
|--|--------------------------|---------|
| | 2009 | 2008 |
| | June 30 | June 30 |
| Total value of goods and services during the period: | | |
| Provided to joint ventures and affiliates | \$ 57.2 | \$ 63.9 |
| Purchased from joint ventures and affiliates | 28.3 | \$ 62.7 |

| \$ millions, as at | 2008 | |
|---|---------|-------------|
| | June 30 | December 31 |
| Accounts receivable from joint ventures | \$ 9.4 | \$ 9.3 |
| Accounts payable to joint ventures | 1.5 | 3.3 |
| Advances and loans receivable from certain Moa Joint Venture entities | 271.3 | 287.3 |
| Advances and loans payable to the Moa Joint Venture partner | 141.0 | 137.9 |
| Loans payable to the Ambatovy Joint Venture partners | 440.2 | 76.2 |

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

Controls and Procedures

Our disclosure controls and procedures are designed to ensure that all important information about Sherritt, including our operating and financial activities, is communicated fully, accurately and in a timely way and that they provide us with assurance that our financial reporting is accurate.

Internal control over financial reporting means a process designed by or under the supervision of the Chief Executive Officer (CEO) and Chief Financial Officer (CFO) to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with GAAP. The internal controls are not expected to prevent and detect all misstatements due to error or fraud.

As at June 30, 2009, the Corporation's CEO and CFO have certified that the disclosure controls and procedures are effective and that during the quarter ended June 30, 2009 we did not make any material changes in our internal controls over financial reporting that materially affected or are reasonably likely to materially affect the Corporation's internal control over financial reporting.

Forward-looking statements

This discussion contains certain 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”, “forecast”, “likely”, “may”, “will”, “could”, “should”, “suspect”, “outlook”, “projected”, “continue” or other similar words or phrases. Similarly, statements with respect to expectations concerning assets, prices, costs, dividends, foreign-exchange rates, earnings, production, market conditions, capital expenditures, commodity demand, risks, availability of regulatory approvals, the impact of investments in Master Asset Vehicles, 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. There is significant risk that predictions, forecasts, conclusions or projections will not prove to be accurate, that those assumptions may not be correct and that actual results may differ materially from such predictions, forecasts, conclusions or projections. Sherritt cautions readers of this MD&A not to place undue reliance on any forward-looking statements as a number of factors could cause actual future results, conditions, actions or events to differ materially from the targets, expectations, estimates or intentions expressed in the forward-looking statements. By their nature, forward-looking statements require Sherritt to make assumptions and are subject to inherent risks and uncertainties.

Key factors that may result in material differences between actual results and developments and those contemplated by this MD&A include, global economic conditions, business, economic and political conditions in Canada, Cuba, Madagascar, and the principal markets for Sherritt’s products. Other such factors include, but are not limited to, uncertainties in the development and construction of large mining projects; risks related to the availability of capital to undertake capital initiatives; changes in capital cost estimates in respect of the Corporation’s capital initiatives; risks associated with Sherritt’s joint-venture partners; future non-compliance with financial covenants; potential interruptions in transportation; political, economic and other risks of foreign operations; Sherritt’s reliance on key personnel and skilled workers; the possibility of equipment and other unexpected failures; the potential for shortages of equipment and supplies; risks associated with mining, processing and refining activities; uncertainties in oil and gas exploration; 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 legislation; risks related to the Cuban government’s ability to make certain payments to the Corporation; development programs; uncertainties in reserve estimates; uncertainties in asset retirement and reclamation cost estimates; Sherritt’s reliance on significant customers; foreign exchange and pricing risks; uncertainties in commodity pricing; credit risks; competition in product markets; Sherritt’s ability to access markets; risks in obtaining insurance; uncertainties in labour relations; uncertainties in pension liabilities; the ability of Sherritt to enforce legal rights in foreign jurisdictions; the ability of Sherritt to obtain government permits; risks associated with government regulations and environmental health and safety matters; and other factors listed from time to time in Sherritt’s continuous disclosure documents.

Further, any forward-looking statement speaks only as of the date on which such statement is made, and except as required by law, Sherritt undertakes no obligation to update any forward-looking statements.