Northern Dynasty Minerals Ltd.

CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEARS ENDED
DECEMBER 31, 2012 AND 2011

(Expressed in thousands of Canadian Dollars)

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Report of Independent Registered Chartered Accountants

To the Board of Directors and Shareholders of
Northern Dynasty Minerals Ltd.

We have audited the accompanying consolidated financial statements of Northern Dynasty Minerals Ltd. and subsidiaries (the "Company"), which comprise the consolidated statements of financial position as at December 31, 2012 and December 31, 2011, and the consolidated statements of comprehensive loss, consolidated statements of cash flows, and consolidated statements of changes in equity for the years ended December 31, 2012 and December 31,2011, and a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards as issued by the International Accounting Standards Board, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor’s Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards and the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

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

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of Northern Dynasty Minerals Ltd. and subsidiaries as at December 31, 2012 and December 31, 2011 and their financial performance and cash flows for the years ended December 31, 2012 and December 31, 2011 in accordance with International Financial Reporting Standards as issued by the Intema1ional Accounting Standards Board.

Other Matter

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the Company's internal control over financial reporting as of December 31, 2012, based on the criteria established in *Internal Control - Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated March 27, 2013 expressed an unqualified opinion on the Company's internal control over financial reporting.

(Signed) Deloitte LLP

Independent Registered Chartered Accountants
March 27, 2013

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Report of Independent Registered Chartered Accountants

To the Board of Directors and Shareholders of
Northern Dynasty Minerals Ltd.

We have audited the internal control over financial reporting of Northern Dynasty Minerals Ltd. and subsidiaries (the "Company") as of December 31, 2012, based on the criteria established in *Internal Control* **-** *Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. The Company's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed by, or under the supervision of, the company's principal executive and principal financial officers, or persons performing similar functions, and effected by the company's board of directors, management, and other personnel to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (l) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of the inherent limitations of internal control over financial reporting, including the possibility of collusion or improper management override of controls, material misstatements due to error or fraud may not be prevented or detected on a timely basis. Also, projections of any evaluation of the effectiveness of the internal control over financial reporting to future periods are subject to the risk that the controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2012, based on the criteria established in *Internal Control - Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission.

We have also audited, in accordance with Canadian generally accepted auditing standards and the standards of the Public Company Accounting Oversight Board (United States), the consolidated financial statements as at and for the year ended December 31, 2012 of the Company and our report dated March 27, 2013 expressed an unqualified opinion on those financial statements.

(Signed) Deloitte LLP

Independent Registered Chartered Accountants
March 27, 2013

Northern Dynasty Minerals Ltd.

Consolidated Statements of Financial Position

(Expressed in thousands of Canadian Dollars)

	Notes	December 31 2012	December 31 2011
ASSETS			
Non-current assets			
Investment in the Pebble Limited Partnership	3	$ 99,336	$ 101,542
Exploration and evaluation assets	4	1,055	1,055
Total non-current assets		100,391	102,597
Current assets			
Amounts receivable from a related party	8	3	483
Amounts receivable and other prepaid expenses	5	5,003	4,704
Cash and cash equivalents	6	27,537	37,457
Total current assets		32,543	42,644
Total Assets		**$ 132,934**	**$ 145,241**
EQUITY			
Capital and reserves			
Share capital	7	$ 389,189	$ 388,987
Reserves		51,129	48,132
Deficit		(311,425)	(295,763)
Total Equity		128,893	141,356
LIABILITIES			
Non-current liabilities			
Deferred income taxes	13	3,632	3,715
Total non-current liabilties		3,632	3,715
Current liabilities			
Payable to a related party	8	148	–
Trade and other payables	9	261	170
Total current liabilities		409	170
Total Liabilities		4,041	3,885
Total Equity and Liabilities		**$ 132,934**	**$ 145,241**

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

These consolidated financial statements are authorized for issue by the Board of Directors on March 27, 2013.
They are signed on the Company's behalf by:

/s/ Ronald W. Thiessen

Ronald W. Thiessen
Director

/s/ Peter Mitchell

Peter Mitchell
Director

Northern Dynasty Minerals Ltd.

Consolidated Statements of Comprehensive Loss

(Expressed in thousands of Canadian Dollars, except for share information)

		Year ended December 31	
	Notes	2012	2011
Expenses			
Exploration and evaluation expenses	11	4,461	819
General and administrative expenses	11	6,780	6,168
Share-based compensation	7(b), 11	5,225	14,205
Loss from operating activities		16,466	21,192
Foreign exchange loss (gain)		83	(58)
Interest income		(887)	(944)
Loss before tax		15,662	20,190
Income tax recovery	13	–	(51)
Loss for the year		**$ 15,662**	**$ 20,139**
Other comprehensive loss (income)			
Unrealized loss on available-for-sale marketable securities		–	1
Exchange difference arising on translation of investment in the Pebble Limited Partnership	3, 7(c)	2,206	(2,236)
Deferred income tax on investment	7(c)	(83)	82
Other comprehensive loss (income) for the year		**$ 2,123**	**$ (2,153)**
Total comprehensive loss for the year		**$ 17,785**	**$ 17,986**
Basic and diluted loss per common share	10	$ 0.16	$ 0.21

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

Northern Dynasty Minerals Ltd.

Consolidated Statements of Cash Flows

(Expressed in thousands of Canadian Dollars)

		Year ended December 31	
	Notes	2012	2011
Cash flows from operating activities			
Loss for the year		$ (15,662)	$ (20,139)
Adjustments for items not affecting cash:			
Donation of shares		–	866
Foreign exchange loss (gain)		93	(65)
Interest receivable on loan	5(a)	(442)	(334)
Share-based compensation		5,225	14,205
		4,876	14,672
Changes in non-cash working capital items			
(Decrease) increase in amounts receivable and other prepaid expenses		48	(616)
Decrease (increase) in amounts receivable from a related party		480	(408)
Increase (decrease) in trade and other payables		91	(282)
Increase (decrease) in payable to related party		148	(102)
		767	(1,408)
Interest on cash reallocated to investing activities		(445)	(610)
Net cash used in operating activities		(10,464)	(7,485)
Cash flows from investing activities			
Interest received		445	610
Loan advanced	5(a)	–	(265)
Net cash from investing activities		445	345
Cash flows from financing activity			
Common shares issued for cash	7	97	4,211
Net cash from financing activity		97	4,211
Net decrease in cash and cash equivalents		(9,922)	(2,929)
Effect of exchange rate fluctuations on cash held		2	(16)
Cash and cash equivalents at beginning of the year		37,457	40,402
Cash and cash equivalents at end of the year	6	**$ 27,537**	**$ 37,457**

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

Northern Dynasty Minerals Ltd.

Consolidated Statements of Changes in Equity

(Expressed in thousands of Canadian Dollars, except for share information)

	Share capital		Reserves				
	Number of shares	Amount	Equity settled share-based payments reserve	Foreign currency translation reserve (note 7(c))	Investment revaluation reserve	Deficit	Total equity
Balance at January 1, 2011	94,177,066	$ 380,570	$ 34,799	$ 316	$ (1)	$ (275,624)	$ 140,060
Shares issued for cash on exercise of share purchase options	726,698	4,211	–	–	–	–	4,211
Fair value of options allocated to shares issued on exercise	–	3,340	(3,340)	–	–	–	–
Shares donated	75,000	866	–	–	–	–	866
Share-based compensation	–	–	14,205	–	–	–	14,205
Loss for the year	–	–	–	–	–	(20,139)	(20,139)
Other comprehensive income for the year net of tax	–	–	–	2,154	(1)	–	2,153
Balance at December 31, 2011	94,978,764	$ 388,987	$ 45,664	$ 2,470	$ (2)	$ (295,763)	$ 141,356
Shares issued for cash on exercise of share purchase options	21,000	97	–	–	–	–	97
Fair value of options allocated to shares issued on exercise	–	105	(105)	–	–	–	–
Share-based compensation	–	–	5,225	–	–	–	5,225
Loss for the year	–	–	–	–	–	(15,662)	(15,662)
Other comprehensive loss for the year net of tax	–	–	–	(2,123)	–	–	(2,123)
Balance at December 31, 2012	94,999,764	$ 389,189	$ 50,784	$ 347	$ (2)	$ (311,425)	$ 128,893

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

1. NATURE OF OPERATIONS AND CONTINUANCE OF OPERATIONS

Northern Dynasty Minerals Ltd. (the "Company") is incorporated under the laws of the Province of British Columbia, Canada, and its principal business activity is the exploration of mineral properties. The Company is listed on the Toronto Stock Exchange ("TSX") under the symbol "NDM" and on the New York Stock Exchange-MKT (formerly NYSE-AMEX) under the symbol "NAK". The Company's corporate office is located at 1040 West Georgia Street, 15th floor, Vancouver, British Columbia.

The consolidated financial statements ("Financial Statements") of the Company as at and for the year ended December 31, 2012, include financial information for the Company and its subsidiaries (note 2(c)) (together referred to as the "Group" and individually as "Group entities") and the Group's interest in jointly controlled entities. The Company is the ultimate parent. The Group owns a 50% share in the Pebble Limited Partnership (the "Pebble Partnership") (note 3). The Pebble Partnership owns the Pebble Copper-Gold-Molybdenum Project (the "Pebble Project"), the Group's principal mineral property interest located in Alaska, United States of America ("USA" or "US").

The Group is in the process of exploring the Pebble Project and has not yet determined whether the Pebble Project contains mineral reserves that are economically recoverable. The Group's continuing operations and the underlying value and recoverability of the amounts shown for the investment in the Pebble Partnership is entirely dependent upon the existence of economically recoverable mineral reserves; the ability of the Group to obtain financing of its share to complete the exploration and development of the Pebble Project; the Pebble Partnership obtaining the necessary permits to mine; and future profitable production or proceeds from the disposition of the investment in the Pebble Partnership.

2. SIGNIFICANT ACCOUNTING POLICIES

(a) Statement of Compliance

These Financial Statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB") and interpretations issued by the IFRS Interpretations Committee ("IFRIC"s). These Financial Statements have been prepared on the basis of IFRS standards that are effective for the Group's reporting year ended December 31, 2012.

(b) Basis of Preparation

These Financial Statements have been prepared on a historical cost basis using the accrual basis of accounting, except for cash flow information and for financial instruments classified as available-for-sale, which are stated at their fair value.

The accounting policies set out below have been applied consistently to all periods presented in these Financial Statements.

(c) Basis of Consolidation

These Financial Statements incorporate the financial statements of the Company and its subsidiaries listed below:

Name of Subsidiary	Place of Incorporation	Ownership Interest	Principal Activity
3537137 Canada Inc.	Canada	100%	Holding Group
0796412 BC Ltd.	British Columbia, Canada	100%	Not active
Northern Dynasty Partnership[1]	Alaska, USA	100%	Holding Group
U5 Resources Inc.[2]	Nevada, USA	100%	Holding Company

1 Holds the Group's 50% interest in Pebble Mines Corp. and the Pebble Partnership (notes (e) and 3).
2 Holds the claims purchased from Liberty Star (note 4).

The Group has determined that its investment in the Pebble Partnership qualifies as an interest in a jointly controlled entity under IAS 31, *Interests in Joint Ventures* ("IAS 31") and applies the equity method to account for this interest. The investment is carried in the statement of financial position at cost and adjusted by post-acquisition changes in the Group's share of the net assets of the joint venture, less any impairment losses. As the Group's investment is carried in US dollars, the investment is translated at the end of each reporting period (note 3).

Intra-Group balances and transactions, including any unrealized income and expenses arising from intra-Group transactions, are eliminated in preparing the Financial Statements. Unrealized gains arising from transactions with equity accounted investees are eliminated against the investment to the extent of the Group's interest in the investee. Unrealized losses are eliminated in the same way as unrealized gains, but only to the extent that there is no evidence of impairment.

(d) Interests in Joint Ventures

A joint venture is a contractual arrangement whereby the Group and other parties undertake an economic activity that is subject to joint control (i.e. when the strategic financial and operating policy decisions relating to the activities of the joint venture require the unanimous consent of the parties sharing control).

Joint venture arrangements that involve the establishment of a separate entity in which each venturer has an interest are referred to as jointly controlled entities. The Group reports its interests in a jointly controlled entity ("JCE"), under the equity method of accounting, except when the investment is classified as held for sale, in which case it is accounted for in accordance with IFRS 5, *Non-current Assets Held for Sale and Discontinued Operations*. Under the equity method, the Group's interest in the JCE is carried in the consolidated financial statement of financial position at cost as adjusted for post-acquisition changes in the Group's share of the net assets of the JCE less any impairment in the value of the investment. Losses in excess of the Group's interest in that JCE are recognized only to the extent that the Group has incurred legal or constructive obligations or made payments on behalf of the JCE.

Any excess of the cost of the acquisition over the Group's share of the fair value of the identifiable assets, liabilities and contingent liabilities of the JCE recognized at the date of the acquisition is recognized as goodwill. The goodwill is included within the carrying amount of the JCE and is assessed for impairment as part of that JCE. Any excess of the Group's share of the net fair value of the identifiable assets, liabilities and contingent liabilities over the cost of acquisition, after reassessment, is recognized immediately in profit or loss.

When a group entity transacts with a JCE of the Group, unrealized profits and losses are eliminated to the extent of the Group's interest in the joint venture. The Group's interests in JCEs are as follow:

Name of JCE	Place of Incorporation	Proportion of Ownership Interest	Principal Activity
Pebble Mines Corp.	Delaware, USA	50%	General partner
Pebble Limited Partnership	Alaska, USA	49.95%[1]	Exploration of Pebble Project

[1] Pebble Mines Corp. has a 0.1% ownership interest in the Pebble Limited Partnership.

(e) *Foreign Currencies*

The functional currency is the currency of the primary economic environment in which the entity operates and has been determined for each entity within the Group. The functional currency of the Pebble Partnership and Pebble Mines Corp. is US dollars and for all other entities within the Group, the functional currency is Canadian dollars. The functional currency determinations were conducted through an analysis of the consideration factors identified in IAS 21, *The Effects of Changes in Foreign Exchange Rates*.

Transactions in currencies other than the functional currency are recorded at the rates of exchange prevailing on dates of transactions. At the end of each reporting period, monetary assets and liabilities that are denominated in foreign currencies are translated at the rates prevailing at that date. Non-monetary assets and liabilities carried at fair value that are denominated in foreign currencies are translated at rates prevailing at the date when the fair value was determined. Non-monetary items that are measured in terms of historical cost in a foreign currency are not retranslated.

(f) *Financial Instruments*

Non-derivative financial assets:

The Group has the following non-derivative financial assets: available-for-sale financial assets (currently only of nominal value), and loans and receivables.

Available-for-sale financial assets

Available-for-sale ("AFS") financial assets are non-derivatives that are either designated as AFS or are not classified as (i) loans and receivables, (ii) held-to-maturity investments or (iii) financial assets at fair value through profit and loss. The Group's investments in marketable securities are classified as AFS financial assets. Subsequent to initial recognition, they are measured at fair value and changes therein, other than impairment losses, are recognized in other comprehensive income or loss and accumulated in the investment revaluation reserve within equity. When an investment is derecognized, the cumulative gain or loss in the investment revaluation reserve is transferred to profit or loss.

The fair value of AFS monetary assets denominated in a foreign currency is determined in that foreign currency and translated at the spot rate at the end of the reporting period. The change in fair value attributable to translation differences that result from the amortized cost of the monetary asset is recognized within other comprehensive income or loss. The change in fair value of AFS equity investments is recognized in other comprehensive income or loss.

Loans and receivables

Loans and receivables are financial assets with fixed or determinable payments that are not quoted in an active market. Such assets are initially recognized at fair value plus any directly attributable transaction costs. Subsequent to initial recognition loans and receivables are measured at amortized cost using the effective interest method, less any impairment losses.

Loans and receivables currently comprise amounts receivable including the loan receivable from Liberty Star (note 5(a)), amounts receivable from a related party and cash and cash equivalents (see below).

Cash and cash equivalents

Cash and cash equivalents in the statement of financial position comprise cash and investments held at major financial institutions that are readily convertible into a known amount of cash and which are only subject to an insignificant risk of change in value, and are measured at amortized cost.

The Group's cash and cash equivalents are invested in business and savings accounts and guaranteed investment certificates which are available on demand by the Group for its programs.

Non-derivative financial liabilities:

The Group's non-derivative financial liabilities comprise amounts payable which are only trade and other payables (note 9) and a payable to a related party.

All financial liabilities fall within the classification of other financial liabilities versus financial liabilities through profit and loss and are recognized initially at fair value net of any directly attributable transaction costs. Subsequent to initial recognition these financial liabilities are measured at amortized cost using the effective interest method.

Impairment of financial assets:

When an AFS financial asset is considered to be impaired, cumulative gains or losses previously recognized in other comprehensive income or loss are reclassified to profit or loss in the period. Financial assets are assessed for indicators of impairment at the end of each reporting period. Financial assets are impaired when there is objective evidence that, as a result of one or more events that occurred after the initial recognition of the financial assets, the estimated future cash flows of the investments have been impacted. For marketable securities classified as AFS, a significant or prolonged decline in the fair value of the securities below their cost is considered to be objective evidence of impairment.

For all other financial assets objective evidence of impairment could include:

- significant financial difficulty of the issuer or counterparty; or
- default or delinquency in interest or principal payments; or
- it becoming probable that the borrower will enter bankruptcy or financial re-organization.

For certain categories of financial assets, such as amounts receivable, assets that are assessed not to be impaired individually are subsequently assessed for impairment on a collective basis. The carrying amount of financial assets is reduced by the impairment loss directly for all financial assets with the exception of amounts receivable, where the carrying amount is reduced through the use of an allowance account. When an amount receivable is considered uncollectible, it is written off against the allowance account. Subsequent recoveries of amounts previously written off are credited against the allowance account. Changes in the carrying amount of the allowance account are recognized in profit or loss.

With the exception of AFS equity instruments, if, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized, the previously recognized impairment loss is reversed through profit or loss to the extent that the carrying amount of the investment at the date the impairment is reversed does not exceed what the amortized cost would have been had the impairment not been recognized. In respect of AFS equity securities, impairment losses previously recognized through profit or loss are not reversed through profit or loss. Any increase in fair value subsequent to an impairment loss is recognized directly in equity.

When an AFS financial asset is considered to be impaired, cumulative gains or losses previously recognized in other comprehensive income are reclassified to profit or loss in the period.

Derivative financial assets and liabilities:

The Group has no derivative financial assets or liabilities. Although the loan receivable from Liberty Star has an equity conversion option, it is not exercisable as the Group has not meet the terms as laid out in the letter agreement (note 5(a)).

(g) Exploration and Evaluation Expenditure

Exploration and evaluation expenditures include the costs of acquiring licenses, costs associated with exploration and evaluation activity, and the acquisition date fair value of exploration and evaluation assets acquired in a business combination or an asset acquisition. Exploration and evaluation expenditures are expensed as incurred except for expenditures associated with the acquisition of exploration and evaluation assets through a business combination or an asset acquisition. Costs incurred before the Group has obtained the legal rights to explore an area are expensed.

Acquisition costs, including general and administrative costs, are only capitalized to the extent that these costs can be related directly to operational activities in the relevant area of interest where it is considered likely to be recoverable by future exploitation or sale or where the activities have not reached a stage which permits a reasonable assessment of the existence of reserves.

Exploration and evaluation ("E&E") assets are assessed for impairment only when facts and circumstances suggest that the carrying amount of an E&E asset may exceed its recoverable amount and when the Group has sufficient information to reach a conclusion about technical feasibility and commercial viability.

Industry-specific indicators for an impairment review arise typically when one of the following circumstances applies:

- Substantive expenditure on further exploration and evaluation activities is neither budgeted nor planned;
- title to the asset is compromised;
- adverse changes in the taxation and regulatory environment;
- adverse changes in variations in commodity prices and markets; and
- variations in the exchange rate for the currency of operation.

Once the technical feasibility and commercial viability of the extraction of mineral resources in an area of interest are demonstrable, exploration and evaluation assets attributable to that area of interest are first tested for impairment and then reclassified to mining property and development assets within property, plant and equipment.

Recoverability of the carrying amount of any exploration and evaluation assets is dependent on successful development and commercial exploitation, or alternatively, sale of the respective areas of interest.

(h) *Property, Plant and Equipment*

Property, plant and equipment ("PPE") are carried at cost, less accumulated depreciation and accumulated impairment losses.

The cost of an item of PPE consists of the purchase price, any costs directly attributable to bringing the asset to the location and condition necessary for its intended use and an initial estimate of the costs of dismantling and removing the item and restoring the site on which it is located.

Depreciation is provided at rates calculated to write off the cost of PPE, less their estimated residual value, using the declining balance method at various rates ranging from 20% - 30% per annum.

An item of PPE is derecognized upon disposal or when no future economic benefits are expected to arise from the continued use of the asset. Any gain or loss arising on disposal of the asset, determined as the difference between the net disposal proceeds and the carrying amount of the asset, is recognized in profit or loss.

Where an item of plant and equipment consists of major components with different useful lives, the components are accounted for as separate items of plant and equipment. Expenditures incurred to replace a component of an item of PPE that is accounted for separately, including major inspection and overhaul expenditures, are capitalized.

Residual values and estimated useful lives are reviewed at least annually.

(i) Impairment of Non-Financial Assets

At the end of each reporting period the carrying amounts of the Group's assets are reviewed to determine whether there is any indication that those assets are impaired. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss, if any. Where it is not possible to estimate the recoverable amount of an individual asset, the Group estimates the recoverable amount of the cash-generating unit to which the asset belongs. The recoverable amount is the higher of fair value less costs to sell and value in use. Fair value is determined as the amount that would be obtained from the sale of the asset in an arm's length transaction between knowledgeable and willing parties. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. If the recoverable amount of an asset is estimated to be less than its carrying amount, the carrying amount of the asset is reduced to its recoverable amount and the impairment loss is recognized in profit or loss for the period. For an asset that does not generate largely independent cash inflows, the recoverable amount is determined for the cash generating unit to which the asset belongs.

Where an impairment loss subsequently reverses, the carrying amount of the asset (or cash-generating unit) is increased to the revised estimate of its recoverable amount. This increase in the carrying amount is limited to the carrying amount that would have been determined had no impairment loss been recognized for the asset (or cash-generating unit) in prior years. A reversal of an impairment loss is recognized immediately in profit or loss.

The Group has not recorded any impairment charges in the years presented.

(j) Share Capital

Common shares are classified as equity. Transaction costs directly attributable to the issue of common shares and share purchase options are recognized as a deduction from equity, net of any tax effects.

(k) Share-based Payment Transactions

Equity-settled share-based payments

The Group operates an equity-settled share-based option plan for its employees and service providers (note 7(b)). The fair value of share purchase options granted is recognized as an employee or consultant expense with a corresponding increase in the equity-settled share-based payments reserve in equity. An individual is classified as an employee when the individual is an employee for legal or tax purposes ("direct employee") or provides services similar to those performed by a direct employee.

The fair value is measured at grant date for each tranche which is expensed on a straight line basis over the vesting period with a corresponding increase in the *equity-settled share-based payments reserve* in equity. The fair value of the share purchase options granted is measured using the Black-Scholes option pricing model taking into account the terms and conditions upon which the share purchase options were granted and forfeiture rates as appropriate. At the end of each reporting period, the amount recognized as an expense is adjusted to reflect the actual number of share purchase options that are expected to vest.

(l) Income Taxes

Income tax on the profit or loss for the years presented comprises current and deferred tax. Income tax is recognized in profit or loss except to the extent that it relates to items recognized in other comprehensive income or loss or directly in equity, in which case it is recognized in other comprehensive income or loss or equity.

Current tax expense is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at year end, adjusted for amendments to tax payable with regards to previous years.

Deferred tax is provided using the balance sheet liability method, providing for unused tax loss carry forwards and temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. The following temporary differences are not provided for: goodwill not deductible for tax purposes; the initial recognition of assets or liabilities that affect neither accounting nor taxable profit; and differences relating to investments in subsidiaries, associates, and joint ventures to the extent that they will probably not reverse in the foreseeable future. The amount of deferred tax provided is based on the expected manner of realization or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantively enacted at the end of the reporting period applicable to the period of expected realization or settlement.

A deferred tax asset is recognized only to the extent that it is probable that future taxable profits will be available against which the asset can be utilized.

Additional income taxes that arise from the distribution of dividends are recognized at the same time as the liability to pay the related dividend.

Deferred tax assets and liabilities are offset when there is a legally enforceable right to set off current tax assets against current tax liabilities and when they relate to income taxes levied by the same taxation authority and the Group intends to settle its current tax assets and liabilities on a net basis.

(m) Restoration, Rehabilitation, and Environmental Obligations

An obligation to incur restoration, rehabilitation and environmental costs arises when environmental disturbance is caused by the exploration or development of a mineral property interest. Such costs arising from the decommissioning of plant and other site preparation work, discounted to their net present value, are provided for and capitalized at the start of each project to the carrying amount of the asset, along with a corresponding liability as soon as the obligation to incur such costs arises. The timing of the actual rehabilitation expenditure is dependent on a number of factors such as the life and nature of the asset, the operating license conditions and, when applicable, the environment in which the mine operates.

Discount rates using a pre-tax rate that reflects the time value of money are used to calculate the net present value. These costs are charged against profit or loss over the economic life of the related asset, through amortization using either the unit-of-production or the straight line method. The corresponding liability is progressively increased as the effect of discounting unwinds, creating an expense recognized in profit or loss.

Decommissioning costs are also adjusted for changes in estimates. Those adjustments are accounted for as a change in the corresponding capitalized cost, except where a reduction in costs is greater than the unamortized capitalized cost of the related assets, in which case the capitalized cost is reduced to nil and the remaining adjustment is recognized in profit or loss.

The operations of the Group have been, and may in the future be, affected from time to time in varying degree by changes in environmental regulations, including those for site restoration costs. Both the likelihood of new regulations and their overall effect upon the Group are not predictable.

The Group has no material restoration, rehabilitation and environmental obligations as the disturbance to date is immaterial.

(n) Loss per Share

The Group presents basic and diluted loss per share data for its common shares, calculated by dividing the loss attributable to common shareholders of the Group by the weighted average number of common shares outstanding during the period. Diluted loss per share does not adjust the loss attributable to common shareholders or the weighted average number of common shares outstanding when the effect is anti-dilutive.

(o) Segment Reporting

The Group operates in a single reportable operating segment – the acquisition, exploration and development of mineral properties. The Group's core asset is its interest in the Pebble Partnership, whose assets are located in Alaska, USA.

(p) Significant Accounting Estimates and Judgments

The preparation of these Financial Statements requires management to make certain estimates, judgments and assumptions that affect the reported amounts of assets and liabilities at the date of the Financial Statements and reported amounts of expenses during the reporting period. Actual outcomes could differ from these estimates. These Financial Statements include estimates which, by their nature, are uncertain. The impacts of such estimates are pervasive throughout the Financial Statements, and may require accounting adjustments based on future occurrences. Revisions to accounting estimates are recognized in the period in which the estimate is revised and future periods if the revision affects both current and future periods. These estimates are based on historical experience, current and future economic conditions and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

Sources of estimation uncertainty

Significant assumptions about the future and other sources of estimation uncertainty that management has made at the end of the reporting period, that could result in a material adjustment to the carrying amounts of assets and liabilities, in the event that actual results differ from assumptions made, relate to, but are not limited to, the following:

i. The Group uses the Black-Scholes Option Pricing Model to calculate the fair value of share purchase options granted for determining share-based compensation included in the loss for the year. Inputs used in this model require subjective assumptions including the expected price volatility from three to five years. Changes in the subjective input assumptions can affect the fair value estimate, and therefore the existing models do not necessarily provide a reliable single measure of the fair value of the Group's share purchase options. The weighted average assumptions applied are disclosed in Note 7(b).
ii. The loan receivable from Liberty Star Uranium & Metals Corp (note 5(a)), which is secured by certain mineral claims, was past due at the end of the reporting period however the Group has not recognised an allowance for doubtful debts because the Group has a reasonable expectation that the loan will be settled by the transfer of the underlying mineral claims by the debtor.
iii. Provision for the deferred income tax expense included in the loss for the year (nil for the current year) and the composition of deferred income tax liabilities included in the consolidated statements of financial position.

Critical accounting judgments

These include:

i. In terms of IFRS 6, *Exploration and Evaluation of Mineral Resources,* the Group used judgment in determining whether there are facts and circumstances suggesting that the carrying amount of its investment in the Pebble Partnership and the Group's exploration and evaluation assets ("E&E assets") may exceed their recoverable amount. The Group's E&E assets represent a mineral property interest (note 4) in certain mineral claims located to the west of the Pebble Project.
ii. IAS 21, *The Effects of Changes in Foreign Exchange Rates* ("IAS 21") defines the functional currency as the currency of the primary economic environment in which an entity operates. IAS 21 requires the determination of functional currency to be performed on an entity by entity basis, based on various primary and secondary factors. In identifying the functional currency of the parent and of its subsidiaries and jointly controlled entities, management considered the currency that mainly influences the cost of undertaking the business activities in each jurisdiction in which the Group operates.
iii. The Group used judgment in determining that its investment in the Pebble Partnership qualifies as an interest in a jointly controlled entity under IAS 31, *Interests in Joint Ventures,* and that the equity method is applicable to account for this interest.

(q) Accounting Standards, Amendments and Revised Standards Not Yet Effective

(i) Effective for the Group's financial year commencing on January 1, 2013

Consolidation, joint arrangements, associates, disclosures and other

In May 2011, the IASB issued new and revised standards on consolidation, joint arrangements, associates and disclosures: IFRS 10, *Consolidated Financial Statements;* IFRS 11, *Joint Arrangements*; IFRS 12, *Disclosure of Interests in Other Entities;* IAS 27*, Separate Financial Statements* (as revised in 2011) and IAS 28*, Investments in Associates and Joint Ventures* (as revised in 2011). In June 2011, IAS 1, *Presentation of Financial Statements,* was amended. In October 2011, IFRIC 20, *Stripping Costs in the Production Phase of a Surface Mine,* was issued. In December 2011, an amendment to IFRS 7, *Financial Instruments: Disclosures* relating to disclosures around information about rights of offset and related arrangements was issued.

The Group has not early adopted these new or revised standards, interpretation and amendments. Based upon its current facts and circumstances, the Group does not expect these new and revised standards to have a material impact on its consolidated financial statements except for change in disclosure and presentation.

The Pebble Partnership

IFRS 11 replaces IAS 31, *Interests in Joint Ventures* and SIC-13, *Jointly Controlled Entities – Non-Monetary Contributions by Venturers*. Under IFRS 11, an entity's interest in an arrangement subject to joint control is classified based on the rights and obligations of the parties to the joint arrangement rather than its legal form as follows:

- A joint operation is a joint arrangement whereby the parties that have joint control of the arrangement ("joint operators") have rights to the assets and obligations for the liabilities relating to the arrangement. IFRS 11 requires that a joint operator recognize its portion of assets, liabilities, revenues and expenses of the joint arrangement.
- A joint venture is a joint arrangement whereby the parties that have joint control of the arrangement ("joint venturers") have rights to the net assets of the arrangement, which is determined by considering the structure and form of the arrangement, the terms agreed by the parties in the contractual arrangement and other facts and circumstances. A joint venturer recognizes its investment in a joint arrangement using the equity method.

The Group's interest in the Pebble Partnership was classified as a jointly controlled entity under IAS 31 and was accounted for using the equity method (note 2(d)). As required under IFRS 11, the Group has reviewed and assessed the structure and legal form, the terms of the contractual arrangements, and other facts and circumstances in relation to its interest in the Pebble Partnership. The Group has concluded that, under IFRS 11, its interest in the Pebble Partnership will be classified as a joint venture and, hence, will continue to be accounted for under the equity method.

Fair value measurement

In May 2011, the IASB issued IFRS 13, Fair Value Measurement. This standard defines fair value, sets out a single IFRS framework for measuring fair value and outlines disclosure requirements about fair value measurements. IFRS 13 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair value is a market-based measurement, not an entity-specific measurement, so assumptions that market participants would use should be applied in measuring fair value.

IFRS 13 is effective for annual periods on or after January 1, 2013, with earlier application permitted. This standard is to be applied prospectively as of the beginning of the annual period in which it is initially applied and the disclosure requirements do not need to be applied in comparative periods before initial application. The Group anticipates that the application of the new standard may result in more extensive disclosures in the future.

(ii) Effective for the Group's financial years commencing on January 1, 2014 and 2015

Amendments to IAS 32, *Financial Instruments: Presentation,* issued in December 2011 which clarify existing application issues relating to the offset of financial assets and financial liabilities requirements applies to annual periods beginning on or after January 1, 2014.

IFRS 9, *Financial Instruments, Classification and Measurement*, originally issued in November 2009 and reissued in October 2010, applies to annual periods beginning on or after January 1, 2015. IFRS 9 is the first phase of three phases to replace IAS 39, *Financial Instruments: Recognition and Measurement*, in its entirety. The Group has not early adopted this standard.

The Group anticipates that the adoption of the amendments and standard will have no material impact on its consolidated financial statements given the extent of its use of financial instruments in the ordinary course of business.

3. INVESTMENT IN THE PEBBLE LIMITED PARTNERSHIP

On July 26, 2007, the Group converted a wholly-owned general partnership that held its Pebble Property interest into a limited partnership, the Pebble Partnership. Anglo American plc ("Anglo American") through a wholly-owned subsidiary subscribed for 50% of the Pebble Partnership's equity effective July 31, 2007. The Group (through a wholly-owned subsidiary) and Anglo American have equal rights in the Pebble Partnership. To maintain its 50% interest in the Pebble Partnership, Anglo American is required to commit staged cash investments into the Pebble Partnership aggregating to US$1.5 billion.

Anglo American's staged investment requirements include an initial minimum expenditure of US$125 million (completed in 2008) towards a prefeasibility report. The prefeasibility report is to be approved by the Board of the general partner (Pebble Mines Corp.), and is to summarize all previous prefeasibility studies. The Board of the general partner is also to approve the alternatives for a final feasibility study. Anglo American is required, in order to retain its 50% interest in the Pebble Partnership, to commit within 90 days of the later of the receipt of the approved prefeasibility report and the approved study alternatives, to fund further expenditures which would bring its total investment to at least US$450 million, which amount is to be expended in producing a final feasibility study and in related activities, which is expected to take the Pebble Partnership to a production decision. Upon an affirmative decision by the Pebble Partnership to develop a mine, Anglo American is required to commit to the remaining portion of the total investment of US$1.5 billion in order to retain its interest in the Pebble Partnership. Following completion of the US$1.5 billion expenditure, any further expenditure will be funded by Anglo American and the Group on a 50/50 basis. To December 31, 2012, Anglo American has funded US$504 million ($524 million). The Pebble Partnership agreement provides for equal project control rights for both partners with no operator's fees payable to either party.

(Expressed in thousands of Canadian Dollars, unless otherwise stated, except per share or option)

The Group has determined that its investment in the Pebble Partnership qualifies as an interest in a jointly controlled entity under IAS 31 and applies the equity method in accounting for this interest. The Group has not recognized any share of the losses in the Pebble Partnership since inception as the Group has no obligation in respect to these losses as the agreement with Anglo American states that the distribution of losses funded by Anglo American are allocated 100% to Anglo American until the total investment of US$1.5 billion is met. For the year ended December 31, 2012, the Pebble Partnership has incurred losses totaling $102,863 (2011 – $84,517). Cumulative losses since inception of the Pebble Partnership to December 31, 2012 total $522,110 (2011 – $419,247). The accounting policies of the Pebble Partnership are the same as those followed by the Group. The Group's investment in the Pebble Partnership is carried in US dollars. Exchange differences arising from the translation of the Group's investment in the Pebble Partnership are recognized directly in the foreign currency translation reserve through other comprehensive loss.

Investment in the Pebble Partnership	December 31 2012	December 31 2011
Carrying value at the beginning of the year	$ 101,542	$ 99,306
Foreign currency translation (note 7(c))	(2,206)	2,236
Carrying value at the end of the year	**$ 99,336**	**$ 101,542**

Summary financial information for the equity accounted investee on a100% basis is as follows:

Assets and Liabilities	December 31 2012	December 31 2011
Non-current assets	$ 101,344	$ 101,311
Current assets	11,890	14,095
Total assets	**$ 113,234**	**$ 115,406**
Current liabilities	9,902	10,522
Total liabilities	**$ 9,902**	**$ 10,522**

Losses	Year ended December 31	
	2012	2011
Net loss for the year	$ 102,863	$ 84,517
Net cumulative losses	522,110	419,247

The Group has not included the net loss and net cumulative losses of the Pebble Partnership in the Financial Statements of the Group.

(Expressed in thousands of Canadian Dollars, unless otherwise stated, except per share or option)

4. EXPLORATION AND EVALUATION ASSETS

	December 31 2012	December 31 2011
Total	$ 1,055	$ 1,055

Pursuant to a letter agreement dated June 29, 2010 with Liberty Star Uranium & Metals Corp. and its subsidiary, Big Chunk Corp. (together, "Liberty Star"), the Group acquired 60.7 square kilometers of mineral claims located to the west of the Pebble Project mineral claims in consideration for a US$1,000 ($1,055) cash payment.

5. AMOUNTS RECEIVABLE AND OTHER PREPAID EXPENSES

	December 31 2012	December 31 2011
Sales tax receivable	$ 177	$ 236
Loan receivable (a)	4,639	4,292
Prepaid expenses	187	176
Total	$ 5,003	$ 4,704

(a) Loan Receivable

The loan receivable at December 31, 2012 and 2011 comprised the amount advanced to Liberty Star in cash, expenditures incurred by the Group in relation to Liberty Star's mineral claims in Alaska and interest accrued thereon (together; the "Loan") pursuant to a letter agreement dated June 2010 and subsequent amendments thereof (together; the "Letter Agreement"). The Loan is repayable in cash upon demand by the Group. The Loan accrues interest at 10% per annum, compounded monthly, and is secured by assets and mining claims owned by Liberty Star in Alaska, USA.

The principal amount and accrued interest relating to the Loan are as follows:

	December 31 2012	December 31 2011
Balance of the principal sum:		
Cash advance (US$3,000)	$ 2,985	$ 3,051
Expenses incurred on behalf of Liberty Star (US$730)	726	743
Total principal sum receivable at year end	3,711	3,794
Accumulated accrued interest at year end	928	498
Balance at end of year	$ 4,639	$ 4,292

The Loan was advanced in conjunction with and in anticipation of the acquisition of a mineral property interest, pursuant to the Letter Agreement, which is summarized as follows:

(Expressed in thousands of Canadian Dollars, unless otherwise stated, except per share or option)

(i) the Group acquired certain mineral claims from Liberty Star outboard of and adjacent to the Pebble Project mineral claims (note (4)); and

(ii) the Group and Liberty Star agreed to enter into a joint venture arrangement whereby the Group, subject to a certain earn-in expenditure requirement, may acquire 60% interest in certain of Liberty Star's mineral claims adjacent to the mineral claims acquired in (i) above. Liberty Star's assets held as collateral for the Loan include, but are not limited to, these mineral claims. The Letter Agreement provides that, in the event of execution of the joint venture agreement, the Group at its sole election can deem all or any part of the Loan to constitute part of the Group's contribution to the earn-in expenditure requirement or can convert the Loan into Liberty Star's common shares upon completion of a certain amount of minimum earn-in expenditure.

As the joint venture agreement contemplated in the Letter Agreement was not executed, in October 2012 the Group delivered a notice of repayment of the Loan to Liberty Star. In November 2012, the Group and Liberty Star negotiated a loan settlement agreement and an amendment thereto (together; the "Loan Settlement Agreement") whereby the Group agreed to extinguish the Loan in consideration for receiving the title to certain of the mineral claims owned by Liberty Star and which were held as collateral for the Loan. At December 31, 2012 as Liberty Star had not completed valid transfer of the claims to the Group in accordance with the terms of the Loan Settlement Agreement, the Loan Settlement Agreement had not closed and the Group retained all its rights under the Letter Agreement. Accordingly, the Group has recognized the Loan as a financial asset in these Financial Statements.

The Group believes that, at December 31, 2012, the Loan was past due 40 days but was not impaired. The Group has a reasonable expectation that it will recover the carrying amount of the Loan by enforcing the legal rights conferred by the Letter Agreement and/or the Loan Settlement Agreement including, but not limited to, the right to receive all or any portion of the mineral claims held as collateral for the Loan.

6. CASH AND CASH EQUIVALENTS

	December 31 2012	December 31 2011
Business and savings accounts	$ 5,921	$ 28,055
Guaranteed investment certificates	21,616	9,402
Total	$ 27,537	$ 37,457

7. CAPITAL AND RESERVES

(a) *Authorized Share Capital*

At December 31, 2012, the authorized share capital comprised an unlimited (2011 – unlimited) number of common shares with no par value. All issued shares are fully paid.

(Expressed in thousands of Canadian Dollars, unless otherwise stated, except per share or option)

(b) *Share Purchase Option Compensation Plan*

The Group has a share purchase option plan approved by the Group's shareholders that allows the Board of Directors to grant share purchase options, subject to regulatory terms and approval, to its officers, directors, employees, and service providers. The share purchase option plan (the "2011 Rolling Option Plan") is based on the maximum number of eligible shares equaling a rolling percentage of 10% of the Group's outstanding common shares, calculated from time to time. Pursuant to the 2011 Rolling Option Plan, if outstanding share purchase options are exercised and the number of issued and outstanding common shares of the Group increases, then the share purchase options available to grant under the plan increase proportionately. The exercise price of each share purchase option is set by the Board of Directors at the time of grant but cannot be less than the market price, being the 5-day volume weighted average trading price calculated the day before the grant. Share purchase options can have a maximum term of ten years (although share purchase options have generally been granted with terms of three or five years) and typically terminate 90 days following the termination of the optionee's employment or engagement. In the case of death or retirement, any outstanding vested share purchase options will expire the earlier of the expiry date or one year from date of death or retirement. The vesting period for share purchase options is at the discretion of the Board of Directors at the time the options are granted.

The following reconciles the Group's share purchase options outstanding at the beginning and end of the year:

	2012		2011	
Continuity of share options	Number of share purchase options	Weighted average exercise price ($/option)	Number of share purchase options	Weighted average exercise price ($/option)
Balance at beginning of year	8,306,782	8.71	6,795,110	6.19
Granted	2,199,500	3.00	2,323,400	15.23
Forfeited	(82,700)	7.77	(75,030)	10.73
Exercised	(21,000)	4.62	(726,698)	5.79
Expired	(1,930,052)	6.01	(10,000)	9.74
Cancelled	(861,000)	15.44	–	–
Balance at end of year	7,611,530	7.00	8,306,782	8.71

During the year the Group did not enter into any share-based transactions with parties other than employees. In 2011, the Group granted 132,000 share purchase options to non-employees; 15,000 to a consultant for the provision of investor relations advisory services; 90,000 to a former director for engineering consulting services; and 27,000 to a consultant for geological advisory services. The Group determined that given the nature of the services being provided and that continued to be provided, it could not determine the fair value of these services reliably. As a consequence, the Group estimated that the value of these services approximated the fair value of the share purchase options granted measured using the Black-Scholes option pricing model which at December 31, 2012 amounted to ($8) (2011 – $458).

(Expressed in thousands of Canadian Dollars, unless otherwise stated, except per share or option)

Share purchase options exercised during the year were as follows:

Period	Share purchase options exercised	Weighted average exercise price ($/option)	Weighted average market share price on exercise ($)
January 27, 2012	17,000	5.00	7.88
October 5, 2012	4,000	3.00	4.45
	21,000	4.62	7.23

Share purchase options exercised during the year ended December 31, 2011 were as follows:

Period	Share purchase options exercised	Weighted average exercise price ($/option)	Weighted average share price ($)
January 1 – January 31, 2011	287,795	6.06	16.81
February 1 – February 28, 2011	257,818	5.03	19.34
March 4 – March 30, 2011	27,470	5.95	14.80
April 1 – April 29, 2011	134,375	6.91	13.37
May 6, 2011	4,000	7.59	11.52
June 3 and June 27, 2011	10,650	3.00	11.32
October 12 – October 27, 2011	2,620	4.18	7.70
November 24, 2011	1,020	3.00	6.42
December 7, 2011	950	3.00	6.96
	726,698	5.79	16.83

The following table summarizes information about the Group's share options outstanding at the end of the year:

	Share purchase options outstanding			**Share purchase options exercisable**		
Exercise prices ($)	Number of share purchase options outstanding	Weighted average exercise price ($/option)	Weighted average remaining contractual life (years)	Number of share purchase options exercisable	Weighted average exercise price ($/option)	Weighted average remaining contractual life (years)
3.00	2,240,600	3.00	2.86	1,171,750	3.00	2.79
5.00 – 5.35	1,643,000	5.01	1.08	1,643,000	5.01	1.08
7.59	2,331,030	7.59	1.15	2,331,030	7.59	1.15
9.74 – 11.55	200,000	10.87	2.25	158,334	10.69	1.94
15.44	1,196,900	15.44	1.73	803,600	15.44	1.72
	7,611,530	7.00	1.76	6,107,714	7.13	1.54

During the year the Group granted 2.2 million share purchase options (2011 – 2.3 million). The weighted average fair value per share purchase options granted using the Black-Scholes option pricing model was $0.87 per option (2011 – $6.34 per option). The fair value was estimated with the following weighted average assumptions:

(Expressed in thousands of Canadian Dollars, unless otherwise stated, except per share or option)

	2012	2011
Risk-free interest rate	1.11%	2.25%
Expected life	3.43 years	4.20 years
Expected volatility	60%	64%
Grant date share price	$2.38	$13.37
Expected dividend yield	Nil	Nil

Refer to discussion on assumptions in Note 2(p) under sources of estimation uncertainty.

(c) *Foreign Currency Translation Reserve*

	Year ended December 31	
	2012	2011
Balance at beginning of year	$ 2,470	$ 316
Exchange (loss) gain on translation of investment in the Pebble Partnership	(2,206)	2,236
Deferred income tax on investment	83	(82)
Balance at the end of year	$ 347	$ 2,470

The foreign currency translation reserve represents accumulated exchange differences arising on the translation of the investment in the Pebble Partnership which has a US dollar functional currency and the related tax effect that has been recognized in other comprehensive loss.

8. RELATED PARTY BALANCES AND TRANSACTIONS

Balances and transactions between the Company and its subsidiaries, which are related parties of the Company, have been eliminated on consolidation and are not disclosed in this note. Details between the Group and other related parties are disclosed below:

Transactions and balances with Key Management Personnel

The aggregate value of transactions with key management personnel, being directors and senior management including the Senior Vice President, Corporate Development; Vice President ("VP") Corporate Communications, VP, Engineering and VP, Public Affairs, were as follows:

	Year ended December 31	
Compensation	2012	2011
Short-term employee benefits [(i)]	$ 2,222	$ 1,834
Share-based compensation	2,781	7,948
Total	$ 5,003	$ 9,782

(i) Short-term employee benefits include salaries and directors fees.

(Expressed in thousands of Canadian Dollars, unless otherwise stated, except per share or option)

Transactions and balances with other Related Parties

The aggregate value of transactions and outstanding balances with other related parties were as follows:

	Year ended December 31	
Transactions	2012	2011
Entity with significant influence [(a)]		
Services rendered to the Group	$ 3,531	$ 3,504
Reimbursement of third party expenses incurred on behalf of the Group	1,129	1,074
Total paid by the Group	$ 4,660	$ 4,578
Jointly controlled entity [(b)]		
Reimbursement of third party expenses incurred by the Group	$ (25)	$ –
Total reimbursed (to) the Group	$ (25)	$ –

Balances receivable from related parties	December 31 2012	December 31 2011
Entity with significant influence [(a)]	$ –	$ 483
Jointly controlled entity [(b)]	3	–
Total	$ 3	$ 483

Balances payable to related parties	December 31 2012	December 31 2011
Entity with significant influence [(a)]	$ 148	$ –
Total	$ 148	$ –

(a) A private company provides geological, corporate development, administrative and management services to the Group and its subsidiaries at annually set rates pursuant to a management services agreement. The private company also incurs third party costs on behalf of the Group which is reimbursed by the Group at cost. The Group may also make pre-payments for services under terms of the services agreement. Several directors and other key management personnel of the private company, who are close business associates, are also key management personnel of the Group.

(b) The Group incurred costs on behalf of the Pebble Partnership (note 3), which were reimbursed at cost.

9. TRADE AND OTHER PAYABLES

Falling due within the year	December 31 2012	December 31 2011
Trade payables	$ 261	$ 170

(Expressed in thousands of Canadian Dollars, unless otherwise stated, except per share or option)

10. BASIC AND DILUTED LOSS PER SHARE

The calculation of basic and diluted loss per share for the year ended December 31, 2012 was based on the following:

	December 31 2012	December 31 2011
Loss attributable to common shareholders	$ 15,660	$ 20,139
Weighted average number of common shares outstanding	94,995,127	94,851,589

Diluted loss per share did not include the effect of the weighted average number of share purchase options outstanding as they are anti-dilutive.

11. EMPLOYMENT COSTS

The amount of salaries and benefits included in expenses are as follows:

	Year ended December 31	
	2012	2011
Salaries included in:		
Exploration and evaluation expenses	$ 856	$ 933
General and administration expenses	2,874	2,765
Share-based compensation	5,225	14,205
Total	**$ 8,955**	**$ 17,903**

12. FINANCIAL RISK MANAGEMENT

The Group is exposed in varying degrees to a variety of financial instrument related risks. The Board approves and monitors the risk management processes, inclusive of documented investment policies, counterparty limits, and controlling and reporting structures. The type of risk exposure and the way in which such exposure is managed is provided as follows:

(a) Credit Risk

Credit risk is the risk of potential loss to the Group if a counterparty to a financial instrument fails to meet its contractual obligations. The Group's credit risk is primarily attributable to its liquid financial assets, including cash and cash equivalents, amounts receivable and amounts receivable from related parties. The Group limits the exposure to credit risk by only investing its cash and cash equivalents with high-credit quality financial institutions in business and saving accounts, guaranteed investment certificates, and in government treasury bills which are available on demand by the Group for its programs.

Management assesses the recoverability of the loan receivable from Liberty Star as at the end of each reporting period based on financial information available. In October 2012, the Group delivered notice to Liberty Star for repayment of the loan and interest. In November 2012, the Group and Liberty Star negotiated the Loan Settlement Agreement in which Liberty Star was to transfer certain Alaska mineral claims held as collateral for the loan receivable in payment of the loan including accrued interest. As of December 31, 2012 and the date of these Financial Statements, as Liberty Star had not completed the valid transfer of the claims to the Group as per the Loan Settlement Agreement, the Loan Settlement Agreement had not closed and accordingly the Group continues to retain its rights under the Letter Agreement. The Group has a reasonable expectation that it will recover the carrying amount of the Loan by enforcing the legal rights conferred by the Letter Agreement and/or the Loan Settlement Agreement including, but not limited to, the right to receive all or any portion of the mineral claims held as collateral for the Loan (note 5(a)).

(b) Liquidity Risk

Liquidity risk is the risk that the Group will not be able to meet its financial obligations when they become due. The Group ensures, as far as reasonably possible, it will have sufficient capital in order to meet short to medium term business requirements, after taking into account cash flows from operations and the Group's holdings of cash and cash equivalents. The Group's cash and cash equivalents are currently invested in business accounts and guaranteed investment certificates which are available on demand.

The funding of expenditures on the Pebble Project held through the Pebble Partnership is currently being provided by Anglo American (discussed below). Excluding cash and cash equivalents in the Pebble Partnership, Northern Dynasty has approximately $28 million in cash and cash equivalents for its own operating requirements. With the Pebble Project's 2013 funding to be funded by Anglo American, and given the Group's holdings of cash and cash equivalents, the Group believes it has sufficient resources to cover its short to medium term cash requirements.

As discussed in Note 3, the Group is in a 50:50 limited partnership with Anglo American on the Pebble Project. To maintain its 50% interest in the Pebble Partnership, Anglo American is required to make staged cash investments into the Pebble Partnership aggregating to US$1.5 billion over a period of several years. To December 31, 2012, Anglo American has invested US$504 million ($524 million). When the prefeasibility study is completed and if the decision is to proceed, Anglo American is required to commit to further expenditures to be expended producing a final feasibility study and in related activities, the completion of which may take the Pebble Partnership to a production decision. Upon an affirmative decision to develop a mine, Anglo American is required to commit to the remaining portion of the total investment of US$1.5 billion.

At December 31, 2012, the Group had working capital of approximately $32.1 million as compared to $42.5 million at December 31, 2011.

The Group has no contractual obligations other than current trade payables (note 9) and amounts payable to a related party (note 8).

(c) Foreign exchange risk

The Group is exposed to foreign exchange risk in respect to its loan receivable which is denominated in US dollars. Additionally certain of the Group's corporate expenses are incurred in US dollars. As a consequence, the Group's results from its operations are subject to currency transaction risk and currency translation risk. The operating results and financial position of the Group are reported in Canadian dollars in the Group's consolidated financial statements. The fluctuation of the US dollar in relation to the Canadian dollar will consequently have an impact upon the losses incurred by the Group and may also affect the value of the Group's assets and the amount of shareholders' equity.

(Expressed in thousands of Canadian Dollars, unless otherwise stated, except per share or option)

The Group has not entered into any agreements or purchased any instruments to hedge possible currency risks.

The exposure of the Group's financial assets to foreign exchange risk is as follows:

Currency	December 31, 2012		December 31, 2011	
US dollars – Financial assets	Foreign currency amount	Amount in Canadian dollars	Foreign currency amount	Amount in Canadian dollars
Amounts receivable	$ 4,663	$ 4,639	$ 4,220	$ 4,292
Cash and cash equivalents	45	45	36	36
Total exposed to currency risk	**$ 4,708**	**$ 4,684**	**$ 4,256**	**$ 4,328**

The exposure of the Group's financial liabilities to foreign exchange risk is as follows:

Currency	December 31, 2012		December 31, 2011	
US dollars – Financial liabilities	Foreign currency amount	Amount in Canadian dollars	Foreign currency amount	Amount in Canadian dollars
Trade and other payables	$ 40	$ 40	$ 1	$ 1
Total exposed to currency risk	**$ 40**	**$ 40**	**$ 1**	**$ 1**

Based on the above net exposures and assuming that all other variables remain constant, a 10% depreciation of the Canadian dollar relative to the US dollar would result in a decrease in the loss of approximately $465 in the year (2011 – $433). This sensitivity analysis includes only outstanding foreign currency denominated monetary items, and excludes the effect of any translation adjustments for the investment in the Pebble Partnership.

(d) Interest rate risk

The Group is subject to interest rate cash flow risk with respect to its investments in cash and cash equivalents. The Group's policy is to invest cash at fixed rates of interest and cash reserves are to be maintained in cash and cash equivalents in order to maintain liquidity, while achieving a satisfactory return for shareholders. Fluctuations in interest rates when the cash and cash equivalents mature impact interest income earned.

(Expressed in thousands of Canadian Dollars, unless otherwise stated, except per share or option)

Assuming that all other variables remain constant, a 100 basis points change representing a 1% increase or decrease in interest rates would have resulted in a decrease or increase in the loss as follows:

	December 31 2012	December 31 2011
Effect on loss	$ 325	$ 389

(e) Capital Management

The Group's policy is to maintain a strong capital base so as to maintain investor and creditor confidence and to sustain future development of the business. The capital structure of the Group consists of equity, comprising share capital, net of accumulated deficit.

There were no changes in the Group's approach to capital management during the year.

The Group is not subject to any externally imposed capital requirements.

(f) Fair value

The fair value of the Group's financial assets and liabilities approximates the carrying amount.

Financial instruments measured at fair value are classified into one of three levels in the fair value hierarchy according to the relative reliability of the inputs used to estimate the fair values. The three levels of the fair value hierarchy are:

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

The Group's marketable securities are classified under Level 1 of the hierarchy however at December 31, 2012, the fair value of these securities was nominal (2011 – $nil).

(Expressed in thousands of Canadian Dollars, unless otherwise stated, except per share or option)

13. INCOME TAX EXPENSE

	Year ended December 31	
	2012	2011
Current tax expense (recovery)		
Current period	$ –	$ (51)
Current income tax recovery	$ –	$ (51)

Reconciliation of effective tax rate		
(Loss) for the period	$ (15,662)	$ (20,139)
Total income tax expense (recovery)	–	(51)
(Loss) excluding income tax	(15,662)	(20,190)
Income tax using the Company's domestic tax rate	(3,916)	(5,350)
Non-deductible expenses	1,323	3,761
Reduction in statutory tax rates	–	90
Foreign exchange	83	(82)
Other	(1)	(51)
Deferred income tax assets not recognized	2,511	1,581
	$ –	$ (51)

The Company's domestic tax rate for the year was 25.00% (2011 - 26.50%) and the effective tax rate was Nil% (2011 - Nil%).

Deferred income tax assets (liabilities)	December 31 2012	December 31 2011
Resource pool	$ 21,144	$ 21,614
Tax losses	58	57
Net deferred income tax assets	21,202	21,671
Investment in the Pebble Partnership	(24,834)	(25,386)
Net deferred income tax liability	$ (3,632)	$ (3,715)

The Group had the following temporary differences at December 31, 2012 in respect of which no deferred tax asset has been recognized:

Expiry	Tax Losses	Resource Pools	Other
Within one year	$ –	$ –	$ –
One to five years	–	–	1,311
After five years	34,174	–	–
No expiry date	169	111,680	66
Total	$ 34,343	$ 111,680	$ 1,377

14. COMMITMENTS AND CONTINGENCIES

Due to the nature of the Group's operations, various legal and tax matters are outstanding from time to time. In the opinion of management, there are no matters that could have a material effect on the Group's consolidated financial position or results of operations which require additional disclosure in these Financial Statements.

15. EVENTS AFTER THE REPORTING PERIOD

Share purchase options cancelled

32,900 share purchase options were forfeited with an average exercise price of $5.46 per option with expiry dates of March 15, 2014 and June 29, 2015.

Northern Dynasty Minerals Ltd.

MANAGEMENT'S DISCUSSION AND ANALYSIS

YEAR ENDED DECEMBER 31, 2012

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1.1 Date

This Management's Discussion and Analysis ("MD&A") should be read in conjunction with the audited consolidated financial statements of Northern Dynasty Minerals Ltd. ("Northern Dynasty" or the "Company") for the year ended December 31, 2012 as publicly filed under the Company's profile on SEDAR at www.sedar.com.

The Company reports in accordance with International Financial Reporting Standards as issued by the International Accounting Standards Board ("IASB") and interpretations of the IFRS Interpretations Committee (together, "IFRS"). The following disclosure and associated consolidated financial statements are presented in accordance with IFRS. This MD&A is prepared as of March 27, 2013. All dollar amounts herein are expressed in Canadian dollars, unless otherwise specified.

This discussion includes certain statements that may be deemed "forward-looking statements" or "forward looking information" within the meaning of Canadian and United States securities law.

All statements in this disclosure, other than statements of historical facts, that address permitting, exploration drilling, exploitation activities and events or developments that the Company expects are forward-looking statements. Although the Company believes the expectations expressed in such forward-looking statements are based on reasonable assumptions, such statements are not guarantees of future performance and actual results or developments may differ materially from those in the forward-looking statements. Factors that could cause actual results to differ materially from those in forward-looking statements include market prices, exploitation and exploration successes, continuity of mineralization, potential environmental issues and liabilities associated with exploration, development and mining activities, uncertainties related to the ability to obtain necessary permits, licenses and title and delays due to third party opposition, changes in government policies regarding mining and natural resource exploration and exploitation, continued availability of capital and financing, and general economic, market or business conditions. Investors are cautioned that any such statements are not guarantees of future performance and actual results or developments may differ materially from those projected in the forward-looking statements. For more information on the Company, investors should review the Company's continuous disclosure filings that are available under the Company's profile at www.sedar.com.

For more information on the Company, Investors should review the Company's annual information form and Form 40-F filing with the United States Securities and Exchange Commission (the "SEC") at www.sec.gov and its home jurisdiction filings that are available on SEDAR at www.sedar.com.

The Company reviews its forward looking statements on an ongoing basis and updates this information when circumstances require it.

Unless otherwise noted, Northern Dynasty is solely responsible for the content of the disclosure set out herein.

Cautionary Note to Investors Concerning Estimates of Measured and Indicated Resources

The following section uses the terms "measured resources" and "indicated resources". The Company advises investors that although those terms are recognized and required by Canadian regulations, the SEC does not recognize them. **Investors are cautioned not to assume that all or any part of mineral deposits in these categories will ever be converted into reserves.**

Cautionary Note to Investors Concerning Estimates of Inferred Resources

The following section uses the term "inferred resources". The Company advises investors that although this term is recognized and required by Canadian regulations, the SEC does not recognize it. "Inferred resources" have a great amount of uncertainty as to their existence, and as to their economic and legal feasibility. It cannot be assumed that all or any part of a mineral resource will ever be upgraded to a higher category. Under Canadian rules, estimates of inferred mineral resources may not form the basis of economic studies, except in rare cases. **Investors are cautioned not to assume that all or any part of an inferred resource exists, or is economically or legally mineable.**

1.2 Overview

1.2.1 Summary

Northern Dynasty is a mineral exploration company which holds indirect interests in 637 square miles of mineral claims in southwest Alaska, USA. These claims are part of or in the vicinity of the Pebble Copper-Gold-Molybdenum Project (the "Pebble Project").

1.2.1.1 Pebble Project

The Pebble property ("Pebble") is located in southwest Alaska, 19 miles (30 kilometers) from the villages of Iliamna and Newhalen, and approximately 200 miles (320 kilometers) southwest of the city of Anchorage. Situated approximately 1,000 feet above sea-level and 65 miles from tidewater on Cook Inlet, the site conditions are favorable for successful mine site and infrastructure development.

Mineralization indicating the presence of the Pebble deposit was discovered in 1987 by a prior operator. By 1997 an initial outline of a deposit of copper, gold and molybdenum had been identified.

Northern Dynasty acquired the right to earn an interest in the Pebble property in late 2001. Over the next 5½ years, the Company explored the Pebble deposit and surrounding property. This work led to the discovery of a substantial volume of higher grade mineralization to the east and an overall expansion of the deposit, as well as the discovery of another porphyry copper-gold-molybdenum deposit, a porphyry copper zone, a gold-copper skarn occurrence, and gold showings along the extensive northeast-trending mineralized system underlying the property. Comprehensive environmental, social and engineering studies for the Pebble deposit began in 2004.

In mid-2007, a wholly-owned affiliate of Northern Dynasty and a wholly-owned subsidiary of Anglo American plc, Anglo American US (Pebble) LLC ("Anglo American") established the Pebble Limited Partnership (the "Pebble Partnership") to engineer, permit, construct and operate a modern, long-life mine at the Pebble Project. The 50/50 Pebble Partnership owns the Pebble Project, which consists of the Pebble deposit and 350 square miles of associated resource lands, along with a stream of financing being provided by Anglo American for comprehensive exploration, engineering, environmental and socioeconomic programs and, if warranted, development of the Pebble Project. Work programs at Pebble since mid-2007 have been carried out by the Pebble Partnership. These programs include detailed engineering, environmental and socioeconomic studies toward the completion of a prefeasibility study for the Pebble Project which will enable the Pebble Partnership to engage stakeholders in the planning process and prepare for permitting under the National Environmental Policy Act ("NEPA").

The estimate of the Pebble deposit mineral resources has been updated several times as exploration advanced. The most recent estimate was announced in February 2010. At a 0.30% copper equivalent (CuEQ)[1] cut-off, the Pebble deposit comprises:

- 5.94 billion tonnes of Measured and Indicated Mineral Resources grading 0.42% copper, 0.35 g/t gold and 250 ppm molybdenum (0.78% CuEQ), containing 55 billion pounds of copper, 67 million ounces of gold, and 3.3 billion pounds of molybdenum; and
- 4.84 billion tonnes of Inferred Mineral Resources grading 0.24% copper, 0.26 g/t gold and 215 ppm molybdenum (0.53% CuEQ), containing 25.6 billion pounds of copper, 40.4 million ounces of gold, and 2.3 billion pounds of molybdenum.

In February 2011, Northern Dynasty announced the results of an independent Preliminary Assessment of the Pebble Project that it had commissioned ("2011 PA"). The study was completed by Wardrop, a Tetra Tech Company ("Wardrop").[2]

The study describes the potential economic value to three successive mine development cases comprising 25, 45 and 78 years of open pit mining and at a nominal processing rate of 200,000 tons per day. The results of the Preliminary Assessment confirm that the Pebble Project has the potential to generate substantial annual revenues, with increasingly better returns over decades of production.

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[1] Mineral resources at February 2010 estimated within a volume or shell defined by long-term metal price estimates of US$2.50/lb copper, US$900/oz gold and US$25/lb molybdenum. M+I include 527 million tonnes in the measured category grading 0.33% copper, 0.35 g/t gold and 178 ppm molybdenum and 5,414 million tonnes in the indicated category grading 0.43% copper, 0.35 g/t gold and 257 ppm molybdenum. Copper equivalent calculations used metal prices of US$1.85/lb for copper, US$902/oz for gold and US$12.50/lb for molybdenum, and metallurgical recoveries of 85% for copper, 69.6% for gold, and 77.8% for molybdenum in the Pebble West area and 89.3% for copper, 76.8% for gold, 83.7% for molybdenum in the Pebble East area. Mineral resources that are not mineral reserves do not have demonstrated economic viability.

[2] The economic assessment and other opinions expressed in the Preliminary Assessment are strictly those of Northern Dynasty and Wardrop, and do not reflect the views of any other stakeholder in the project. Additional details can be found in the following documents posted under the Company's profile at www.sedar.com:

- **Technical Report entitled "Preliminary Assessment of the Pebble Project, Southwest Alaska, effective date February 15, 2011,"** by Wardrop. Qualified Persons include Hassan Ghaffari, P.Eng, Robert Morrison, P.Geo, Andre de Ruijter, P.Eng, Tysen Hantelmann, P.Eng, Aleksandar Zivkovic, P.Eng, and Scott Cowie, MAusIMM; Doug Ramsey, P.R. Bio is author of sustainability section. All of these qualified persons are independent of Northern Dynasty.
- **Northern Dynasty's Annual Information Form for fiscal 2010 and fiscal 2011.**

The Pebble Partnership has continued to undertake detailed engineering, environmental and socioeconomic studies toward the completion of a prefeasibility report for the Pebble Project, including ongoing programs to engage project stakeholders in the planning process. The project which is ultimately put forward by the Pebble Partnership for permitting under NEPA and the Alaska State Large Mine Permitting Process may differ from those mine models presented in the Preliminary Assessment.

Ongoing Prefeasibility Study and Environmental and Socioeconomic Work

The Pebble Partnership has assembled an experienced engineering and permitting team for the Pebble Project, consisting of more than 20 senior engineers and technical specialists (many of whom are from the Anglo American group or Northern Dynasty), as well as engineering firms and specialized consultancies from around the world.

The team has continued to advance engineering and project design initiatives for the Pebble Project. Public consultation forums in Alaska are planned to gain input from stakeholders prior to the completion of a Prefeasibility Study and the submission of permit applications.

In January 2012, the Pebble Partnership publicly released the Environmental Baseline Document ("EBD") for the Pebble Project, characterizing existing physical, biological and social conditions in the project area, in anticipation of initiating project permitting. It contains more than 27,000 pages of scientific data and analyses, characterizing a broad range of environmental and social conditions in southwest Alaska – including climate, water quality, wetlands, fish and aquatic habitat, wildlife, land and water use, socioeconomics and subsistence. The EBD is based primarily on research collected between 2004 and 2008, although baseline data collecting and monitoring of environmental and socioeconomic conditions surrounding the Pebble Project continue today. Public and expert review of the EBD facilitated under the Keystone initiative (see further details in section 1.2.1.3 below) began in October 2012. The Pebble Partnership plans to complete its compilation of 2009 to 2012 environmental baseline data reports, and this material will also be shared with state/federal agencies and the public.

Permitting will be initiated once the Pebble Partnership submits its Project Description and other documents to the government agencies which, with the EBD, provides the foundation for an Environmental Impact Statement ("EIS"). Often prepared by a third-party contractor under the direction of a lead federal agency, the EIS will assess the proposed project's potential environmental/socioeconomic effects and development alternatives, and will provide the basis for federal, state and local government agencies to make individual permitting decisions.

The board of the Pebble Partnership adopted a budget of approximately US$107 million for a comprehensive work program in 2012 that included exploration, geotechnical and metallurgical drilling and geo-hydrological testing as well as engineering studies to work toward completion of a Project Description and Prefeasibility Study. The Pebble Partnership also continued environmental baseline data collection, monitoring and synthesis, and community engagement and workforce development programs to advance the project and prepare for permitting under NEPA.

Objectives for 2013 are to focus on finalizing the Project technical studies, including fish/water mitigation and closure plans. Similar data collection programs will continue with a focus on monitoring. Permitting under NEPA is expected to begin in 2013 with a stakeholder engagement program to precede that process.

Corporate

Northern Dynasty has cash and cash equivalents on hand of $27.5 million for its operating requirements. With the Pebble Project being financed by Anglo American, management believes that the Company has sufficient capital resources to cover its short to medium term cash requirements.

1.2.1.2 Limited Partnership Established to Advance the Pebble Project

On July 26, 2007, the Company converted a wholly-owned general partnership that held its Pebble property interests into a limited partnership, the Pebble Partnership. Anglo American, through its wholly-owned affiliate, subscribed for 50% of the Pebble Partnership's equity effective July 31, 2007. The Company (through a wholly-owned affiliate) and Anglo American have equal rights in the Pebble Partnership. To maintain its 50% interest in the Pebble Partnership, Anglo American is required to commit staged cash investments into the Pebble Partnership aggregating to US$1.5 billion.

Anglo American's staged investment requirements include an initial minimum expenditure of US$125 million (completed in 2008) towards a prefeasibility report. The prefeasibility report is to be approved by the Board of the general partner (Pebble Mines Corp.), and is to summarize all previous prefeasibility studies. The Board of the general partner is also to approve the alternatives for a final Feasibility Study. Anglo American is required, in order to retain its 50% interest in the Pebble Partnership, to commit within 90 days of the later of the receipt of the approved prefeasibility report and the approved study alternatives, to fund further expenditures which would bring its total investment to at least US$450 million, with further expenditures towards producing a final feasibility study and related activities, the completion of which is expected to take the Pebble Partnership to a production decision. Upon an affirmative decision by the Pebble Partnership to develop a mine following approval of a positive Feasibility Study, Anglo American is required to commit to the remaining portion of the total investment of US$1.5 billion in order to retain its interest in the Pebble Partnership. Following completion of the US$1.5 billion expenditure, any further expenditure will be funded by Anglo American and the Company (through its affiliate) on a 50:50 basis (subject to dilution for non-contribution). The Pebble Partnership agreement provides for equal project control rights with no operator's fees payable to either party.

The Company determined in accordance with IAS 31, *Interests in Joint Ventures* that its investment in the Pebble Partnership is an interest in a jointly controlled entity. The Company applies the equity method to account for its interest in the Pebble Partnership.

Anglo American's cash contribution since the formation of the Pebble Partnership on July 31, 2007 to December 31, 2012 amounts to $523.8 million (US$504.2 million).

The corporate office of the Pebble Partnership is located in Anchorage, Alaska. The Alaska-based operations are guided by the Board of the general partner with equal representation from Anglo American and Northern Dynasty.

1.2.1.3 Technical Programs

Exploration and Drilling

Site work in 2012 included exploration drilling, hydrogeochemical sampling surveys to access and prioritize numerous geophysical exploration targets on the property, soil sampling and geological and alteration mapping.

The 2012 drilling program began in the second quarter and continued through the third quarter. A total of 35,760 feet in 81 holes were drilled in 2012, of which 7,392 feet totaling 17 holes were drilled in the fourth quarter. In 2012, 17 core holes (8,363.15 feet) were drilled for exploration purposes; 38 core holes (15,973 feet) were drilled to collect geotechnical data, and 26 sonic holes (11,424 feet) were drilled for hydrological investigations.

Engineering

The current phase of the engineering program is designed to advance toward completion of the prefeasibility study for the Pebble Project. The work, which commenced in 2011, has continued through 2012 and includes additional analysis of the open pit, ongoing design of the process plant and associated infrastructure, and compilation of the designs for the access roads, port and power plant. The Pebble Partnership continues to evaluate development options and component alternatives. The Pebble Partnership engineering team is also making contributions to the development of a Project Description to support permit applications under NEPA.

Environmental and Socioeconomic Studies

Environmental Baseline Document

The EBD provides information and analysis on baseline physical, chemical, biological and social conditions based upon ongoing data collection by the Pebble Project environmental study team from 2004 to 2008. Its purpose is to provide the public, regulatory agencies and the Pebble Partnership with a detailed compendium of pre-development environmental and socioeconomic conditions in the project area.

Research for the Pebble EBD was conducted by more than 40 respected independent research firms, utilizing over 100 scientific experts and engineering groups, laboratories and support services. Researchers were selected for their specific areas of expertise and Alaskan experience, with cooperating government agencies participating in several studies. Information for the EBD was gathered through field studies, laboratory tests, review of government records and other third-party sources, and interviews with Alaska residents.

The compilation of environmental studies undertaken in support of mine development is more commonly presented to regulatory agencies as part of a broader permitting package, which includes a Project Description. Given its importance and the public interest in the Pebble Project, the Pebble Partnership released the EBD to provide stakeholders with additional time to review the substantial document in advance of project permitting. A Project Description for the Pebble Project will need to be finalized before permitting commences.

The Pebble Partnership facilitated a four-day workshop with federal and state regulatory agencies in January 2012 to present the EBD findings. The workshop was broadcast publicly via the

Internet. A series of public presentations has also been coordinated in more than 20 communities throughout southwest Alaska and elsewhere around the State to present the EBD findings. These presentations involved several of the authors of the document.

Ongoing Programs

Comprehensive environmental and socioeconomic baseline study programs continue at the Pebble Project site. The 2012 field programs have primarily focused on surface and groundwater hydrology, water quality and fish resources. Objectives for 2013 include completion of fish/water mitigation and closure plans. Similar data collection programs will continue in 2013 with a focus on monitoring.

Cultural Resource Studies

Cultural resource studies have been carried out by the Pebble Partnership on all areas that might be affected by the Pebble Project, with the exception of possible road and port locations. Examination of the potential road and port sites will be undertaken once a decision is made regarding the exact location of these project features.

Community Engagement

An active program of stakeholder outreach has continued in 2012, including community meetings, stakeholder visits, presentations and event appearances, as well as stakeholder tours to the Pebble Project site and to operating mines in the United States ("US") and Canada. The focus of these outreach activities is to update stakeholders on the Pebble Project, to receive feedback on stakeholder priorities and concerns, and to advise participants about modern mining practices.

The Pebble Partnership has a number of other initiatives underway to enhance stakeholder relationships, including:

1. The *Pebble Fund for Sustainable Bristol Bay Fisheries & Communities* – Established in 2008 with a five-year, US$5 million commitment, with the goal of enhancing the health and sustainability of regional fisheries and the communities they support. Grants are determined based on criteria and selections made by an advisory board comprised of citizens from communities throughout the Bristol Bay region. In 2012, 36 grants totaling approximately US$2 million have funded community-based projects throughout southwest Alaska. Grants totaling more than US$4.7 million have been awarded to date, leveraging nearly US$13 million in matching funds from other organizations.

   The Bristol Bay Marketplace Business Idea Competition for residents of Bristol Bay communities was introduced in 2011. The competition, sponsored by the Pebble Partnership and the Pebble Fund, provides the opportunity for local entrepreneurs to compete for funding to start or expand Bristol Bay-based businesses. In 2012, awards totaling US$235,000 were disbursed for the period January to April 2012. A second grant cycle for 2012 included 19 awards, totaling $730,519, with matching funds totaling $776,193.

   The 2012 award winners were also invited to a two-day workshop held in Anchorage on August 16 and 17 where local entrepreneurs and CEOs offered general small business success tips and basic training in accounting, management and marketing.

2. An independent stakeholder dialogue process concerning the Pebble Project was initiated in late 2010 by the Keystone Center – a non-profit organization specializing in facilitating stakeholder-driven consultation processes concerning contentious, science-based issues. Independent Science Panels ("ISP"), consisting of respected experts in a range of technical, scientific and sociological fields, were assembled to review environmental and socioeconomic data compiled by the Pebble Partnership for the purpose of project engineering and permitting, while providing expert insight to Pebble Project stakeholders. The process is designed to address: geology and geochemistry; hydrology and water quality; fish, wildlife and habitat; and social, economic and cultural dynamics. Four ISP events were held in October 2012 and one session is planned for the spring of 2013.

In 2012, 67 site tours have been provided to share project updates with a total of 312 stakeholders from across the region and Alaska. In addition, the Pebble Partnership continues to host regional stakeholders at tours of operating mines, including the Bingham Canyon Mine in Utah, Gibraltar Mine in British Columbia and the Fort Knox Mine in Alaska.

In order to increase stakeholder understanding of the Pebble Project, the Pebble Partnership has commissioned a National Economic Impact Study to be released in the coming months. As the Pebble Project advances toward the completion of a prefeasibility study and preparation for project permitting under NEPA, it is expected that the Pebble Partnership will initiate a broad-based stakeholder engagement program to involve stakeholders in the process by which the project is being designed.

Employment and Workforce Development

The Pebble Partnership is one of the most important private sector employers in southwest Alaska. In 2012, Pebble had 79 direct employees (34 in Anchorage, 39 on site, and six community associates), along with 260 contractors (258 at site and two in Anchorage).

Employee training and workforce development initiatives continue to expand. Workforce development initiatives at the Pebble Project include the provision of training in the areas of equipment operations, health, safety and environment. Working with the U.S. and Alaska Departments of Labor, the Pebble Partnership has established the first-ever registered apprenticeship training program to help local drill helpers become certified drillers. The Company is also investing in programs to train local workers to become environmental technicians, emergency medical technicians and bear guards. In addition, scholarships are available to high school students from the Bristol Bay region who are interested in pursuing studies at college and vocational/technical schools in the fields of project management, operations, geology, science, engineering and other disciplines related to responsible resource development. In 2012, 44 students have been supported through scholarships totaling $186,000. Some $336,500 has been awarded since the scholarship program was established in 2010.

1.2.1.4 Legal Matters

On February 23, 2011, the Company issued a news release announcing that it was in receipt of a new independent Preliminary Assessment of the Pebble Project, which is based on the information generated and provided by the Pebble Partnership and Northern Dynasty. The information provided by the Pebble Partnership and the Preliminary Assessment constitute a material change in the affairs of the Company because it changed the technical parameters and provided an estimated net present value of the property that deviated by billions of dollars from the last such assessment done in 2004. Anglo American, the Company's 50% partner in the Pebble Partnership, has asserted that the news release contained confidential information which is the property of the Pebble Partnership and was not authorized to be released, and Anglo American reserves all rights to claim that the release has damaged Anglo American and/or the Pebble Partnership. The Company has received legal advice that the news release was a permitted disclosure under the various agreements with Anglo American, and its issuance was a mandatory requirement under Canadian and US regulatory requirements. The Company does not believe that Anglo American's allegations have any merit; however, it cannot give assurances about future events or actions by Anglo American.

In October 2011, a lawsuit filed in July 2009 by the Trustees for Alaska (an environmental law firm) on behalf of Nunamta Aulukestai – an organization established and funded to oppose development of the Pebble Project - was rejected by the Anchorage Superior Court. The lawsuit alleged that the Alaska Department of Natural Resources ("DNR") had violated the state constitution by granting exploration and temporary water use permits to the Pebble Partnership, and exploration activities had caused harm to vegetation, water, fish and wildlife. The Pebble Partnership actively participated in the trial proceedings after being granted intervener status. Superior Court Judge Aarseth denied each of the allegations made by Nunamta Aulukestai, and ruled that no evidence of environmental harm was presented. The plaintiffs have filed an appeal that is now pending before the Alaska Supreme Court.

In November 2011, by a narrow 280 – 246 (53% – 47%) margin, voters in Southwest Alaska's Lake & Peninsula Borough supported a ballot measure sponsored by anti-Pebble activists that, if upheld by the courts, might restrict future development that affects more than one square mile of land within the 31,000 square mile borough.

The initiative was opposed by a broad spectrum of Alaska interests, including a group of four Alaska Native village corporations representing seven Lake & Peninsula Borough communities whose private land holdings would be affected by the ordinance, the State of Alaska and the Pebble Partnership. It was also opposed by the Resource Development Council for Alaska, the Alaska State Chamber of Commerce, the Alaska Miners Association, Council of Alaska Producers, the Alaska Oil and Gas Association and the Alaska Industry Support Alliance, among others.

The Pebble Partnership and the State of Alaska view the initiative as unconstitutional and unenforceable because it seeks to restrict development of state-owned resources on state lands through a municipal ordinance. The State of Alaska and the Pebble Partnership have filed legal challenges in the Alaska Superior Court, which will hear summary judgment motions from both parties in April 2013. A trial on the issue is scheduled for December 2013.

1.2.1.5 Bristol Bay Watershed Assessment

In February 2011, the US Environmental Protection Agency ("EPA") announced it would undertake a Bristol Bay Watershed Assessment study focusing on the potential effects of large-scale mine development in all of the Bristol Bay area, subsequently narrowed to the Nushagak and Kvichak drainages. This process was initiated in response to calls from persons and groups opposing the Pebble Project for the EPA to pre-emptively use its asserted authority under Section 404(c) of the Clean Water Act to prohibit discharges of dredged or fill material in waters of the US within these drainages. Rather than acceding to this request, the EPA embarked on a scientific study to assess potential impacts of hard rock mining in the two drainages.

The EPA's draft Bristol Bay Watershed Assessment ("BBWA") report was released on May 18, 2012. The draft report is a fundamentally flawed document. By the EPA's own admission, it has evaluated the effects of a 'hypothetical project' – a project that has not been defined or proposed – and for which key environmental mitigation strategies are not known. The assessment was rushed – it is based on studies conducted over only one year in an area of 20,000 square miles. In comparison, the Pebble Partnership has studied the ecological and social environment surrounding Pebble for more than eight years. The EPA also failed to fully consider the data that the Pebble Partnership provided as part of its 27,000-page Environmental Baseline Document.

The EPA called for public comment on the quality and sufficiency of scientific information presented in the draft BBWA report. In response, Northern Dynasty made a presentation highlighting these shortcomings at the public hearings held in Seattle, Washington, on May 31, 2012 and in Anchorage, Alaska, on August 7, 2012. In July 2012, the Company also submitted a 635-page critique of the draft report in response to the EPA's call for public comment, and has called upon the EPA to cease action on the watershed assessment until such time as the Pebble Partnership submits a definitive proposal for the development of the Pebble deposit. Additional information on Northern Dynasty's submission to the EPA and the Company's critique of the BBWA report, see http://www.northerndynastyminerals.com/ndm/BristolBay.asp.

Concerns about the reasonableness of the basis of risk assessment in the draft EPA report were stated by many of the independent experts on the peer review panel assembled to review the BBWA in a report entitled *'External Peer Review of EPA's Draft Document: An Assessment of Potential Mining Impacts on Salmon Ecosystems of Bristol Bay, Alaska"* released in November 2012. In a wide-ranging critique of the draft report's methodology and findings, many peer review panelists called the EPA's effort to evaluate the effects of a 'hypothetical mining scenario' on the water, fish, wildlife and cultural resources of Southwest Alaska *"inadequate*", *"premature", "unreasonable", "suspect" and "misleading*". The full peer review report can be found at:
http://www.epa.gov/ncea/pdfs/bristolbay/Final-Peer-Review-Report-Bristol-Bay.pdf.

"The authors have attempted to develop a hypothetical mine and attempted to assess possible environmental effects associated with mine development, operation, and closure," said Dr. William Stubblefield, a senior professor at Oregon State University and an expert in environmental toxicology. "Although interesting, the potential reality of the assessment is somewhat questionable. It is also unclear why EPA undertook this evaluation, given that a more realistic assessment could probably have been conducted once an actual mine was proposed and greater detail about operational parameters available."

The EPA states it is now working to complete a revised draft BBWA by spring 2013 for an additional round of public comment and review by the original peer review panel, to be followed by report completion toward the end of 2013.

1.2.2 Other Properties

1.2.2.1 South Pebble, SP and KAK Claims

Agreement between Full Metal Minerals and the Pebble Partnership

On January 31, 2012, the Pebble Partnership entered into a Limited Liability Company Agreement (the "FMM Agreement") of Kaskanak Copper LLC (the "LLC") with Full Metal Minerals (USA) Inc. ("FMMUSA"), a wholly-owned subsidiary of Full Metal Minerals Corp. Under the FMM Agreement, the Pebble Partnership can earn a 60% interest in the LLC which owns 100% of FMM's South Pebble Claims (the "FMM Properties"), by incurring exploration expenditures of at least US$3 million and making annual payments of US$50,000 to FMMUSA over a period ending on December 31, 2013. The Pebble Partnership has been appointed as the manager of the LLC and will continue as manager until it resigns or is deemed to resign in certain defined circumstances which include a reduction of its ownership interest in the LLC to below 50%.

For the duration of the earn-in period and the term of the Pebble Partnership's membership in the LLC, the Pebble Partnership will have an option to select and purchase claims that form part of the FMM Properties (the "Purchased Claims") at a price of US$25 per acre payable to FMMUSA, provided that the Purchased Claims are declared or agreed to be outside of the current scope of operations of the LLC, constitute no more than 20,000 acres, constitute a continuous block of claims and are located outside an "Exclusion Area" specified in the FMM Agreement.

The FMM Properties total 542 claims covering approximately 135 square miles located west of the ground held 100% by the Pebble Partnership; 99 of these claims, covering an area of 24.3 square miles, form the "Exclusion Area".

1.2.2.2 Big Chunk North and South

Northern Dynasty's Purchase and Option Agreement with Liberty Star

On June 29, 2010, Northern Dynasty entered into an agreement with Liberty Star Uranium and Metals Corp. and its subsidiary, Big Chunk Corp. (together, "Liberty Star"), pursuant to which Liberty Star sold 23.8 square miles of claims (the "Purchased Claims") to a US subsidiary of Northern Dynasty in consideration for both a US$1 million cash payment and a secured convertible loan from Northern Dynasty in the amount of US$3 million which accrues interest at 10% per annum compounded monthly and which is repayable 45 days after it is called (the "Loan"). The parties agreed, through various amendments to the original agreement, to increase the principal amount of the Loan by US$730,174 (the "Additional Loan Amount"), being the amounts expended by Northern Dynasty on annual assessment work, rental and related fees relating to the maintenance of Liberty Star's claims in Alaska. Northern Dynasty called for the repayment of the Loan in October 2012 and, after failure by Liberty Star to make any repayment, Northern Dynasty agreed to accept transfer of 199 claims (the "Settlement Claims") covering 47.9 square miles located north of the ground held 100% by the Pebble Partnership in settlement of the Loan. Prior to transfer of the Settlement Claims to Northern Dynasty, a third party purported to register a lien on the Settlement Claims in respect of a debt allegedly owed by Liberty Star, which Liberty Star disputes. Liberty Star has filed a claim against the third party, who has in turn filed a counterclaim against Liberty Star and has sought to join Northern Dynasty as a party to the lawsuit. Northern Dynasty intends to tender its defense of such counterclaim to Liberty Star, which is obligated to indemnify Northern Dynasty from any losses arising from the failure of Liberty Star to transfer clear title to the Settlement Claims.

The total area of the properties is 71.6 square miles, and includes 95 Purchased Claims and 199 Settlement Claims. All of these claims are located in the vicinity of Pebble. Northern Dynasty carried out initial exploration surveys in 2010.

1.2.3 Market Trends

Copper prices showed a significant increase between late 2003 and mid-2008, and after a steep decline in late 2008 and early 2009, steadily increased until late 2011. The price of copper has been variable in 2012 and so far in 2013, ranging between US$3.32/lb and $3.93/lb.

Although gold prices have dropped from time to time, over the past five years the average annual price has steadily increased. This overall trend continued in 2013.

Molybdenum prices have been more volatile than gold or copper, beginning an upward trend in 2003 that reached a peak of US$34/lb in October 2005, decreasing through 2006, then rising in 2007 until the latter part of 2008, when they dropped significantly. This decrease continued until May 2009. Prices improved, but were variable in 2010 and 2011. The average price increased to US$15.00/lb in early April 2012 but has decreased since that time.

Average annual prices as well as the average price so far in 2013 for copper, gold and molybdenum are shown in the table below:

Year	**Average metal price (US$)**		
	Copper	**Gold**	**Molybdenum**
2008	3.16/lb	871/oz	29.70/lb
2009	2.34/lb	974/oz	11.29/lb
2010	3.42/lb	1,228/oz	15.87/lb
2011	4.00/lb	1,572/oz	15.41/lb
2012	3.61/lb	1,669/oz	12.81/lb
2013 (to the date of this MD&A)	3.61/lb	1,364/oz	11.47/lb

Source: LME Official Cash Price as provided at www.metalprices.com

1.3 Selected Annual Information

The following selected annual information is from the audited consolidated financial statements which have been prepared in accordance with IFRS. All figures are expressed in thousands of Canadian dollars unless otherwise stated except per share amounts.

Statements of Financial Position	December 31 2012	December 31 2011	December 31 2010
Investment in the Pebble Partnership ("PLP")	$ 99,336	$ 101,542	$ 99,306
Exploration and evaluation assets	1,055	1,055	1,055
Current assets	32,543	42,644	43,886
Total assets	**132,934**	**145,241**	**144,247**
Shareholders' equity	128,893	141,356	140,060
Other liabilities	3,632	3,715	3,633
Current liabilities	409	170	554
Total shareholders' equity and liabilities	**132,934**	**145,241**	**144,247**
Working capital	**$ 32,134**	**$ 42,474**	**$ 43,332**

Expenses (income)	Year ended December 31 2012	Year ended December 31 2011	Year ended December 31 2010
Exploration and evaluation	$ 4,461	$ 819	$ 1,800
General and administrative	6,780	6,168	4,318
Share-based compensation	5,225	14,205	8,373
Exchange loss (gain)	83	(58)	138
Interest income	(887)	(944)	(544)
Loss before tax	15,662	20,190	14,085
Income tax (recovery) expense	–	(51)	30
Loss for the year	$ 15,662	$ 20,139	$ 14,115
Basic and diluted loss per common share	$ 0.16	$ 0.21	$ 0.15
Weighted average number of common shares outstanding	94,995	94,852	93,779

1.4 Summary and Discussion of Quarterly Results

All monetary amounts are expressed in thousands of dollars except per share amounts and where otherwise indicated. Minor differences are due to rounding.

Statements of Financial Position	Dec 31 2012	Sep 30 2012	Jun 30 2012	Mar 31 2012	Dec 31 2011	Sep 30 2011	June 30 2011	Mar 31 2011
Exploration and evaluation assets	$ 1,055	$ 1,055	$ 1,055	$ 1,055	$ 1,055	$ 1,055	$ 1,055	$ 1,055
Investment in PLP	99,336	98,168	101,652	99,595	101,542	104,658	96,301	96,810
Current assets	32,543	35,623	38,605	40,811	42,644	43,792	44,925	45,302
Total assets	**132,934**	**134,846**	**141,312**	**141,461**	**145,241**	**149,505**	**142,281**	**143,167**
Equity	128,893	130,214	137,191	137,282	141,356	145,550	138,566	139,261
Deferred income tax	3,632	3,589	3,719	3,643	3,715	3,829	3,523	3,542
Current liabilities	409	1,043	402	536	170	126	192	364
Total shareholders' equity and liabilities	**132,934**	**134,846**	**141,312**	**141,461**	**145,241**	**149,505**	**142,281**	**143,167**
Working capital	32,134	34,580	38,203	40,275	42,474	43,666	44,733	44,938
Comprehensive (Income) Loss								
Expenses								
Exploration and evaluation	663	1,255	1,274	1,269	(86)	448	141	316
General and administrative	2,076	2,472	1,136	1,096	1,497	1,143	2,129	1,399
Share-based compensation	486	1,260	1,702	1,777	2,170	2,752	2,782	6,501
Exchange (gain) loss	(48)	136	(87)	82	118	(272)	17	79
Interest income	(233)	(240)	(251)	(163)	(270)	(252)	(225)	(197)
Loss before tax	2,944	4,883	3,774	4,061	3,429	3,819	4,844	8,098
Income tax loss (recovery)	2	(2)	–	–	(51)	–	–	–
Loss for the quarter	2,946	4,881	3,774	4,061	3,378	3,819	4,844	8,098
Loss on marketable securities	–	–	–	–	1	–	–	–
Exchange difference on translation of PLP	(1,168)	3,484	(2,057)	1,947	3,116	(8,357)	509	2,496
Deferred income tax	41	(128)	76	(72)	(114)	306	(19)	(91)
Comprehensive loss (income)	**$ 1,819**	**$ 8,237**	**$ 1,793**	**$ 5,936**	**$ 6,381**	**$ (4,232)**	**$ 5,334**	**$ 10,503**
Basic and diluted loss per common share	$ 0.03	$ 0.05	$ 0.04	$ 0.04	$ 0.04	$ 0.04	$ 0.05	$ 0.09

Discussion of Quarterly Trends

The Company's investment in the Pebble Partnership is carried in US dollars. Exchange differences arising from the translation of the Company's investment in the Pebble Partnership are taken directly to the foreign currency translation reserve through other comprehensive loss. The Company has recorded translation losses in five quarters as a result of appreciation of the Canadian dollar relative to the US dollar and gains in three quarters as a result of the depreciation of the Canadian dollar relative to the US dollar. The following table summarizes the movement in the US dollar to the Canadian dollar and the resulting exchange differences recognized in each quarter:

		1CAD for 1USD		
Period	USD movement to CAD	Start	End	Recognized (gain) loss
Q1 2011	Depreciation	$0.99	$0.97	$ 2.5 million
Q2 2011	Depreciation	$0.97	$0.96	$ 0.5 million
Q3 2011	Appreciation	$0.96	$1.05	$ (8.4) million
Q4 2011	Depreciation	$1.05	$1.02	$ 3.1 million
Q1 2012	Depreciation	$1.02	$1.00	$ 1.9 million
Q2 2012	Appreciation	$1.00	$1.02	$ (2.1) million
Q3 2012	Depreciation	$1.02	$0.98	$ 3.5 million
Q4 2012	Appreciation	$0.98	$0.99	$ (1.1) million
FY 2011	Appreciation	$0.99	$1.02	$ (2.2) million
FY 2012	Depreciation	$1.02	$0.99	$ 2.2 million

Share-based compensation expense has fluctuated due to the timing of share purchase option grants and the vesting periods associated with these grants. The fair value of share purchase options is determined at the grant date and the compensation expense for each tranche is recognized over the period during which the share purchase options vest. The Company granted share purchase options in Q2 of 2012 and Q1 of 2011. This resulted in an increase in share-based compensation recognized in Q1 of 2011. In Q2 of 2012 however, share-based compensation did not increase notwithstanding the vesting of one-half of the share purchase options granted, as the fair value of share purchase options granted was $0.87 per option as compared to $6.56 per option for the Q1 2011 grant. From Q2 to Q4 of 2011, and Q1 and Q4 of 2012 share-based compensation related to the amortization of share-based compensation on share purchase options that were still vesting. In Q3 of 2012, the directors of the Company voluntarily agreed to cancel 861,000 of their options with an exercise price of $15.44 of which two-thirds had vested. The impact of the cancellation was the acceleration of vesting of one-third of these options that had not vested which resulted in the Company recognizing an additional $458,000 in share-based compensation.

Exploration and evaluation expenses have fluctuated from quarter to quarter. In 2011, the Company completed and announced the results of the 2011 PA, conducted further ongoing analysis thereof and paid annual fees and rentals on Liberty Star claims. In Q4 of 2011, the Company agreed to treat certain of the 2011 and 2010 payments in respect to Liberty Star claims as an advance and increased the principal amount of the loan outstanding from Liberty Star resulting in a credit in exploration costs for the quarter. In Q1 through Q4 of 2012, the Company commenced and focused on a further technical study to advance work completed since the issue of the 2011 PA.

1.5 Results of Operations

The following financial data has been prepared in accordance with IFRS effective for the year ended December 31, 2012 and are expressed in Canadian dollars unless otherwise stated.

The Company's operations and business are not driven by seasonal trends, but rather are driven towards the achievement of project milestones relating to the Pebble Project such as the achievement of various technical, environmental, socio-economic and legal objectives, including obtaining the necessary permits, the completion of pre-feasibility and final feasibility studies, preparation of engineering designs, as well as receipt of financings to fund these objectives along with mine construction.

1.5.1 Results of Operations for the Year Ended December 31, 2012 vs. 2011

The Company recorded a total comprehensive loss of $17.8 million for the current year as compared to $18.0 million in 2011. The decrease was mainly attributable to lower share-based compensation being recognized in the current year which was offset by an increase in exploration and evaluation expenses ("E&E") in 2012 and recording of an exchange loss on translation of the equity investment in the Pebble Partnership (as opposed to a gain in 2011).

The Company recorded E&E of $4.5 million in 2012 as compared to $0.8 million in 2011 as the Company commenced work on a technical study that advances work that was undertaken since the issue of the 2011 PA.

General and administrative expenses ("G&A") increased to $6.8 million in 2012 from $6.2 million in 2011. The increase was due mainly to retaining US political and scientific representatives to assist and represent the Company and evaluate the EPA's draft Bristol Bay Watershed Assessment report (refer 1.2.1.4 *Legal Matters)*. In 2011, costs were impacted by a donation of the Company's shares.

The following table provides a breakdown of G&A incurred, expressed in thousands of dollars:

G&A	2012	2011
Conference and travel	$ 566	$ 525
Consulting	1,761	–
Donations	–	866
Insurance	343	296
Legal, accounting and audit	255	328
Office costs	702	980
Salaries	2,593	2,334
Shareholder communication	332	517
Trust and filing	228	322
Total	$ 6,780	$ 6,168

The Company incurred consulting fees as it retained US political and scientific representatives to assist and represent the Company and evaluate the EPA's draft BBWA report (refer 1.2.1.5 *Bristol Bay Watershed Assessment)*. Salaries were slightly higher in the year due in part to increased support for the aforementioned corporate activities to respond to the EPA's initiative and other corporate activities including public affairs.

Share-based compensation decreased to $5.2 million from $14.2 million in 2011. In 2012, the lower fair value estimated for share purchase options ($0.87 per option) reduced the amount of amortization of share-based compensation on share-purchase options vesting in the year as compared to 2011 ($6.34 per option).

Other comprehensive loss was $2.1 million in the year as compared to other comprehensive income of $2.2 million in 2011. The turnaround is due to the Company recording a $2.2 million exchange loss on translation of the investment in the Pebble Partnership in 2012 as compared to a gain of $2.2 million in 2011. As the Pebble Partnership has a US dollar functional currency, the Company is impacted by movements in the US / Canadian dollar exchange rate (see 1.4, *Discussion of Quarterly Trends).*

1.5.2 Cash Flows for the Year Ended December 31, 2012 vs. 2011

Net cash used in operations increased to $10.5 million in the current year from $7.5 million in the prior year. The increase was due in part to the increase in G&A costs and the increase in exploration and evaluation expenses incurred (as discussed in section 1.5.1).

The Company received $0.4 million in interest on cash balances which was lower than in 2011 ($0.6 million) due to lower average cash balances held.

The Company received $97,000 in 2012 on the exercise of share purchase options as compared to $4.2 million received from the exercise of options in 2011.

1.5.3 Financial position as at December 31, 2012 vs. December 31, 2011

The Company's total assets decreased to $132.9 million from $145.2 million. The decrease was due to the decrease in current assets of $10.1 million and a decrease of $2.2 million in the carrying value of the Company's investment in the Pebble Partnership as a result of the exchange loss recognized on translation (refer 1.5.1). The decrease in current assets is due mainly to the $9.9 million decrease in cash and cash equivalents as the Company utilized $10.5 million of its cash in its operations and received inflows of $0.5 million from the exercise of share purchase options and interest on cash balances. Other changes in current assets included a decrease in related party receivables of $0.5 million due to the utilization of services from the related party by the Company and an increase of $0.4 million in amounts receivable and other assets due mainly to accrued interest.

1.5.5 Investment in the Pebble Partnership

As indicated in section 1.2.1.2, the Company has determined that, in accordance with IFRS, it has joint control of the Pebble Partnership and applies the equity method to account for its investment in the Pebble Partnership.

Expenditures incurred by the Pebble Partnership on the Pebble Project are being funded 100% by Anglo American. Anglo American's total contributions from inception to December 31, 2012 total $523.8 million (US$504.2 million). For the year ended December 31, 2012, the Pebble Partnership incurred losses of $102.9 million (2011 – $84.5 million). E&E costs increased to $93.3 million from $78.0 million in the previous year as the Pebble Partnership focused on various programs to advance the completion of a prefeasibility study for the Pebble Project, the development of a Project

Description and the release of the EBD in January 2012. The main E&E costs during the year ended December31, 2012, were for:

- engineering (2012 – $19.1 million; 2011 – $20.0 million);
- environmental planning and testing (2012 – $20.0 million; 2011 – $12.8 million);
- site activities (2012 – $36.6 million; 2011 – $32.1 million);
- corporate affairs (2012 – $16.5 million; 2011 – $12.3 million); and
- business development (2012 – $1.1 million; 2011 - $nil).

For further discussion on exploration activities and the technical programs underway on the Pebble Project, see section 1.2.1.3, *Technical Programs*.

1.6 Liquidity

Historically, the Company's sole source of funding has been the issuance of equity securities for cash, primarily through private placements to sophisticated investors and institutions. In 2008, the Company completed its last private placement financing and since then has continued each year to see inflows to the treasury through the issue of common shares pursuant to the exercise of share purchase options. The Company's access to financing is always uncertain. There can be no assurance of continued access to significant equity funding.

The funding of expenditures on the Pebble Project held through the Pebble Partnership is currently being provided by Anglo American (described below). Excluding cash and cash equivalents in the Pebble Partnership, Northern Dynasty has $27.5 million in cash and cash equivalents for its own operating requirements. With the Pebble Project funded by Anglo American, the Company believes it has sufficient resources to cover its short to medium term cash requirements.

As discussed in section 1.2.1.2, the Company is in a 50:50 limited partnership with Anglo American. To maintain its 50% interest in the Pebble Partnership, Anglo American is required to make staged cash investments into the Pebble Partnership aggregating to US$1.5 billion (refer 1.2.1.2). On completion of the US$1.5 billion investment by Anglo American, any further expenditure will need to be funded by the Company and Anglo American on a 50:50 basis. The Company currently does not have the required funding to meet these long term obligations should they arise.

At December 31, 2012, the Company had working capital of approximately $32.1 million as compared to $42.5 million at December 31, 2011.

The Company has no long term debt, capital lease obligations, operating leases or any other long term obligations.

The Company has no "Purchase Obligations", defined as any agreement to purchase goods or services that is enforceable and legally binding on the Company that specifies all significant terms, including: fixed or minimum quantities to be purchased; fixed, minimum or variable price provisions; and the approximate timing of the transaction.

The Pebble Partnership has purchase orders for goods and services relating to its activities on the Pebble Project. It also is responsible for all maintenance payments on the property and routine office leases. All costs are funded through existing cash resources in the Pebble Partnership which are being funded by Anglo American and are in the normal course of operations.

The Company is responsible for all maintenance payments on the Purchased Claims (refer 1.2.2.2).

1.7 Capital Resources

The Company has no long-term debt and had 94,999,764 common shares issued and outstanding at December 31, 2012.

The Company had no commitments for material capital expenditures as of December 31, 2012.

The Pebble Partnership, which is being funded by Anglo American, has an approximate US$0.3 million commitment to the Pebble Fund for Sustainable Bristol Bay Fisheries & Communities until 2013 (refer to C*ommunity Engagement* in 1.2.1.3).

The Company has no lines of credit or other sources of financing.

1.8 Off-Balance Sheet Arrangements

None.

1.9 Transactions with Related Parties

The Company and its subsidiaries transact with Hunter Dickinson Services Inc. ("HDSI"), a private company which has certain directors and other key management personnel and whom are close business associates who are also key management personnel of the Company. Pursuant to a management services agreement with HDSI, HDSI provides geological, corporate development, administrative and management services to the Company at annually set rates and incurs third party costs on behalf of the Company which are reimbursed by the Company at cost. The following summarizes the transactions with HDSI expressed in thousands of dollars:

	Year ended December 31	
Transactions	2012	2011
Services rendered by HDSI	$ 3,531	$ 3,504
Reimbursement of third party expenses incurred by HDSI	1,129	1,074
Total paid by the Company	$ 4,660	$ 4,578

The Company continues to use resources provided by HDSI to assist with ongoing administration and management of the Company including continuous disclosure obligations, shareholder communications and investor relations, as well as assisting with the Company's role as partner in the Pebble Partnership.

Other related party transactions include compensation paid to key management personnel (directors and senior management including the Senior Vice President, Corporate Development; Vice President ("VP"), Corporate Communication, VP, Engineering and VP, Public Affairs). For the year ended December 31 2012, this comprised salaries of $2.2 million (2011 – $1.8 million) and share-based compensation of $2.8 million (2011 – $7.9 million).

During the year, the Company also paid for services that were provided to the Pebble Partnership totaling $25,000 which were reimbursed at cost by the Pebble Partnership.

1.10 Fourth Quarter

The Company recorded a total comprehensive loss of $2.9 million for the current quarter as compared to $3.4 million in the same period in 2011. The decrease was mainly attributable to a decrease in share-based compensation in the current quarter which more than offset the increase in E&E and G&A as compared to the 2011 comparative period.

The Company recorded E&E of $0.7 million as compared to a recovery of ($0.1) million in 2011. In 2012, the Company continued working on a technical study to advance work since the issue of the 2011 PA. In 2011, the Company agreed to increase the loan advanced to Liberty Star by approximately $726,000 in respect to certain 2011 and 2010 payments made on Liberty Star claims which resulted in a recovery in E&E recognized in the quarter.

G&A increased to $2.1 million in 2012 from $1.6 million in 2011. The following table provides a breakdown of expenses incurred, expressed in thousands of dollars:

	Three months ended December 31	
G&A	2012	2011
Conference and travel	$ 230	$ 242
Consulting	564	–
Insurance	89	83
Legal, accounting and audit	175	196
Office costs	147	272
Salaries	808	531
Shareholder communication	58	114
Trust and filing	5	59
Total	$ 2,076	$ 1,497

The Company incurred consulting fees as it retained US political and scientific representatives to assist and represent the Company and to evaluate the EPA's draft BBWA report (refer 1.2.1.5 *Bristol Bay Watershed Assessment)*. Salaries were higher in the current quarter due in part to increased support for the aforementioned corporate activities to respond to the EPA's initiative and other corporate activities, including public affairs.

Share-based compensation decreased to $0.5 million from $2.2 million in 2011. In 2012, the lower fair value estimated for share purchase options ($0.87 per option) reduced the amount of amortization of share-based compensation on share-purchase options vesting in the quarter as compared to the comparative quarter of 2011 ($6.34 per option).

The Company recorded other comprehensive gain of $1.1 million in the quarter as compared to a comprehensive loss of $3.0 million in Q4 2011. The Company recorded a $1.1 million exchange gain on translation of the investment in the Pebble Partnership in the current quarter as compared to a loss of $3.1 million in Q4 of 2011. As the Pebble Partnership has a US dollar functional currency, the Company is impacted by movements in the US / Canadian dollar exchange rate (see 1.4, *Discussion of Quarterly Trends).*

1.11 Proposed Transactions

There are no proposed asset or business acquisitions or dispositions, other than those in the ordinary course, before the Board of Directors for consideration.

1.12 Critical Accounting Estimates

The Company's significant accounting policies are presented in Note 2 in the notes to the consolidated financial statements for the year ended December 31, 2012. The preparation of the consolidated financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the end of the reporting period presented and reported amounts of expenses during said reporting period. Actual outcomes could differ from these estimates. The consolidated financial statements include estimates which, by their nature, are uncertain. The impacts of such estimates are pervasive throughout the consolidated financial statements, and may require accounting adjustments based on future occurrences. Revisions to accounting estimates are recognized in the year in which the estimate is revised and future years if the revision affects both current and future years. These estimates are based on historical experience, current and future economic conditions and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

Significant assumptions about the future and other sources of estimation uncertainty at the end of the reporting period, that could result in a material adjustment to the carrying amounts of assets and liabilities in the event that actual results differ from assumptions made, include, but are not limited to, the following:

i. The Company uses the Black-Scholes Option Pricing Model to calculate the fair value of share purchase options granted for determining share-based compensation included in the loss for the year. Inputs used in this model require subjective assumptions including the expected price volatility from three to five years. Changes in the subjective input assumptions can affect the fair value estimate, and therefore the existing models do not necessarily provide a reliable single measure of the fair value of the Company's share purchase options. The weighted average assumptions applied are disclosed in 1.12.4.

ii. The loan receivable from Liberty Star Uranium & Metals Corp (refer Note 5(a) in the Notes to the Consolidated Financial Statements), which is secured by certain mineral claims, was past due at the end of the reporting period however the Company has not recognized an allowance for doubtful debts because the Company has a reasonable expectation that the loan will be settled by the transfer of the underlying mineral claims by the debtor.

iii. Provision for the deferred income tax expense included in the loss for the year (nil for the current year) and the composition of deferred income tax liabilities included in the Statement of Financial Position in the Consolidated Financial Statements.

1.12.1 Mineral resources and the carrying value of the Company's investment in the Pebble Partnership

Mineral resources are estimated by professional geologists and engineers in accordance with recognized industry, professional and regulatory standards. These estimates require inputs such as future metals prices, future operating costs, and various technical geological, engineering, and construction parameters. Changes in any of these inputs could cause a significant change in the resources estimates which in turn could have a material effect on the carrying value of the Company's investment in the Pebble Partnership.

1.12.2 Impairment analysis of assets

At the end of each reporting period, the carrying amounts of the Company's assets which comprise mainly its interest in the Pebble Partnership, exploration and evaluation assets and the Liberty Star loan receivable are reviewed to determine whether there is any indication that those assets are impaired. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment, if any. The recoverable amount is the higher of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. If the recoverable amount of an asset is estimated to be less than its carrying amount, the carrying amount of the asset is reduced to its recoverable amount and the impairment loss is recognized in the profit or loss for the period. For the purposes of impairment testing, exploration and evaluation assets are allocated to cash-generating units to which the exploration activity relates. For an asset that does not generate largely independent cash inflows, the recoverable amount is determined for the cash generating unit to which the asset belongs.

Recoverability of the carrying amount of the exploration and evaluation assets is dependent on successful development and commercial exploitation, or alternatively, sale of the respective assets.

Changes in any of the assumptions used to determine impairment testing could materially affect the results of the analysis.

At December 31, 2012, the Company reviewed the carrying value of its assets and determined that there were no indicators of impairment.

1.12.3 Restoration, rehabilitation, and environmental obligations

An obligation to incur restoration, rehabilitation and environmental costs arises when environmental disturbance is caused by the exploration or development of a mineral property interest. Such costs arising from the decommissioning of plant and other site preparation work, discounted to their net present value, are provided for and capitalized at the start of each project to the carrying amount of the asset, along with a corresponding liability as soon as the obligation to incur such costs arises. The timing of the actual rehabilitation expenditure is dependent on a number of factors such as the life and nature of the asset, the operating license conditions, and when applicable, the environment in which the mine operates.

Discount rates using pre-tax rates that reflect the time value of money are used to calculate the net present value. These costs are charged against profit or loss over the economic life of the related asset, through amortization using either the unit-of-production or the straight line method. The corresponding liability is progressively increased as the effect of discounting unwinds creating an expense recognized in profit or loss.

Decommissioning costs are also adjusted for changes in estimates. Those adjustments are accounted for as a change in the corresponding capitalized cost, except where a reduction in costs is greater than the unamortized capitalized cost of the related assets, in which case the capitalized cost is reduced to nil and the remaining adjustment is recognized in profit or loss.

The operations of the Company may in the future be affected from time to time in varying degree by changes in environmental regulations or changes in estimates used in determining restoration and rehabilitation obligations. Both the likelihood of new regulations or degree of changes in estimates and their overall effect upon the Company are not predictable.

At December 31, 2012, the Company has no material restoration, rehabilitation and environmental obligations as the disturbance to date is minimal.

1.12.4 Share-based compensation expense

As indicated in 1.12 (i) the Company uses the Black-Scholes option pricing model to estimate the fair value of share purchase options granted through its Board of Directors, to directors, employees and service providers. During the year the Company granted 2.2 million share purchase options (2011 – 2.3 million). The weighted average fair value of share purchase options granted was estimated at $0.87 per option (2011 - $6.34 per option) based on the following weighted average assumptions and inputs:

	2012	2011
Risk-free interest rate	1.11%	2.25%
Expected life	3.43 years	4.20 years
Expected volatility	60%	64%
Grant date share price	$2.38	$13.37
Expected dividend yield	Nil	Nil

Changes in any of these inputs could cause a significant change in the share-based compensation expense charged in a period.

1.12.5 Income Taxes

The Company uses the asset and liability method of accounting for income taxes. Under this method, deferred income tax assets and liabilities are computed based on differences between the carrying amounts of assets and liabilities on the statements of financial position and their corresponding tax values, generally using the substantively enacted or enacted income tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. Deferred income tax assets also result from unused loss carry forwards, resource-related pools and other deductions. A deferred tax asset is only recognized to the extent that it is probable that future taxable profits will be available against which the asset can be utilized.

A deferred tax liability would arise on the carrying value of the investment in the Pebble Partnership as a result of historical transactions. The Company recognizes net deferred tax liabilities as it believes it does not control the timing of the reversal of these temporary differences even though management has made the judgment that the reversal is not expected to occur in the foreseeable future.

1.13 Changes in Accounting Policies including Initial Adoption

Accounting Standards, Amendments and Revised Standards Not Yet Effective

Effective for the Company's financial year commencing on January 1, 2013

Consolidation, joint arrangements, associates, disclosures and other

In May 2011, the IASB issued new and revised standards on consolidation, joint arrangements, associates and disclosures: IFRS 10, *Consolidated Financial Statements;* IFRS 11, *Joint Arrangements*; IFRS 12, *Disclosure of Interests in Other Entities;* IAS 27*, Separate Financial Statements* (as revised in 2011) and IAS 28*, Investments in Associates and Joint Ventures* (as revised in 2011). In June 2011, IAS 1, *Presentation of Financial Statements,* was amended. In October 2011, IFRIC 20, *Stripping Costs in the Production Phase of a Surface Mine,* was issued. In December 2011, amendments to IFRS 7, *Financial Instruments: Disclosures* relating to disclosures around information about rights of offset and related arrangements were issued.

The Company has not early adopted these new or revised standards, interpretation and amendments. Based upon its current facts and circumstances, the Company does not expect these new and revised standards to have a material impact on its consolidated financial statements except for change in disclosure and presentation.

The Pebble Partnership

IFRS 11 replaces IAS 31, Interests in Joint Ventures and SIC-13, Jointly Controlled Entities – Non-Monetary Contributions by Venturers. Under IFRS 11, an entity's interest in an arrangement subject to joint control is classified based on the rights and obligations of the parties to the joint arrangement rather than its legal form as follows:

- A joint operation is a joint arrangement whereby the parties that have joint control of the arrangement ("joint operators") have rights to the assets and obligations for the liabilities relating to the arrangement. IFRS 11 requires that a joint operator recognize its portion of assets, liabilities, revenues and expenses of the joint arrangement.
- A joint venture is a joint arrangement whereby the parties that have joint control of the arrangement ("joint venturers") have rights to the net assets of the arrangement, which is determined by considering the structure and form of the arrangement, the terms agreed by the parties in the contractual arrangement and other facts and circumstances. A joint venturer recognizes its investment in a joint arrangement using the equity method.

The Company's interest in the Pebble Partnership was classified as a jointly controlled entity under IAS 31 and was accounted for using the equity method (refer note 2(e) in the notes to the audited consolidated financial statements). As required under IFRS 11, the Company has reviewed and assessed the structure and legal form, the terms of the contractual arrangements, and other facts and circumstances in relation to its interest in the Pebble Partnership. The Company has concluded that, under IFRS 11, its interest in the Pebble Partnership will be classified as a joint venture and, hence, will continue to be accounted for under the equity method.

Fair value measurement

In May 2011, the IASB issued IFRS 13, Fair Value Measurement. This standard defines fair value, sets out a single IFRS framework for measuring fair value and outlines disclosure requirements about fair value measurements. IFRS 13 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair value is a market-based measurement, not an entity-specific measurement, so assumptions that market participants would use should be applied in measuring fair value.

IFRS 13 is effective for annual periods on or after January 1, 2013, with earlier application permitted. This standard is to be applied prospectively as of the beginning of the annual period in which it is initially applied and the disclosure requirements do not need to be applied in comparative periods before initial application. The Company anticipates that the application of the new standard may result in more extensive disclosures in the future.

Effective for the Company's financial year commencing on January 1, 2014 and 2015

Amendments to IAS 32, Financial Instruments: Presentation, issued in December 2011 which clarify existing application issues relating to the offset of financial assets and financial liabilities requirements applies to annual periods beginning on or after January 1, 2014.

IFRS 9, *Financial Instruments, Classification and Measurement,* originally issued in November 2009 and reissued in October 2010, applies to annual periods beginning on or after January 1, 2015. IFRS 9 is the first phase of three phases to replace IAS 39, *Financial Instruments: Recognition and Measurement,* in its entirety. The Company has not early adopted this standard.

The Company anticipates that the adoption of the amendments and standard will have no material impact on its consolidated financial statements given the extent of its use of financial instruments in the ordinary course of business.

1.14 Financial Instruments and Other Instruments

The Company has no derivative financial assets or liabilities. The loan receivable from Liberty Star which the Company continues to record in its consolidated financial statements has an equity conversion option however, it is not exercisable as the Company has not meet the terms as laid out in the letter agreement (refer note 5(a) in the Notes to audited consolidated financial statements).

1.14.1 Non-derivative financial assets:

The Company has the following non-derivative financial assets: available-for-sale financial assets and loans and receivables.

Available-for-sale ("AFS") financial assets

The Company has marketable securities which are classified as AFS financial assets and are measured at fair value with changes therein, other than impairment losses recognized in other comprehensive income or loss. At the reporting date these securities had a nominal value.

Loans and receivables

Loans and receivables are financial assets with fixed or determinable payments that are not quoted in an active market. Such assets are initially recognized at fair value plus any directly attributable transaction costs. Subsequent to initial recognition loans and receivables are measured at amortized cost using the effective interest method, less any impairment losses.

Loans and receivables comprise amounts receivable including the Liberty Star loan receivable, amounts receivable from a related party and cash and cash equivalents (see below).

Cash and cash equivalents

Cash and cash equivalents in the statement of financial position comprise cash and investments held at major financial institutions that are readily convertible into a known amount of cash and which are only subject to an insignificant risk of change in value, and are measured at amortized cost.

The Company's cash and cash equivalents are invested in business and savings accounts and guaranteed investment certificates which are available on demand by the Company for its programs.

1.14.2 Non-derivative financial liabilities:

The Company has the following non-derivative financial liabilities: trade and other payables and a payable to a related party.

Such financial liabilities are recognized initially at fair value net of any directly attributable transaction costs. Subsequent to initial recognition these financial liabilities are measured at amortized cost using the effective interest method.

1.14.3 Financial Risk Management

The Company is exposed in varying degrees to a variety of financial instrument related risks. The Board approves and monitors the risk management processes, inclusive of documented investment policies, counterparty limits, and controlling and reporting structures. The type of risk exposure and the way in which such exposure is managed is provided as follows:

Credit Risk

Credit risk is the risk of potential loss to the Company if a counterparty to a financial instrument fails to meet its contractual obligations. The Company's credit risk is primarily attributable to its liquid financial assets, including cash and cash equivalents, amounts receivable which includes the Company's loan receivable from Liberty Star and any amounts receivable from related parties. There has been no change in the Company's objectives and policies for managing this risk except for changes in the carrying amounts of financial assets exposed to credit risk, and there was no significant change to the Company's exposure to credit risk during the year ended December 31, 2012. Management has concluded that there is no objective evidence of impairment to its amounts receivable at December 31, 2012 which included assessing the recoverability of the loan receivable from Liberty Star (see discussion below).

Management assesses the recoverability of the loan receivable from Liberty Star as at the end of each reporting period based on financial information available. In October 2012 the Company delivered notice to Liberty Star for repayment of the loan and interest. In November 2012, the Company and Liberty Star negotiated a loan settlement agreement in which Liberty Star was to transfer certain Alaska mineral claims held as collateral for the loan receivable in payment of the loan including accrued interest. As of December 31, 2012 and the date of this MD&A, as Liberty Star had not completed the valid transfer of the claims to the Company as per the loan settlement agreement, the loan settlement agreement had not closed and accordingly the Company continues to retain its rights under the original loan letter agreement. The Company has a reasonable expectation that it will recover the carrying amount of the loan receivable by enforcing the legal rights conferred by the original loan letter agreement and/or the loan settlement agreement including, but not limited to, the right to receive all or any portion of the mineral claims held as collateral for the loan receivable.

Liquidity Risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations when they become due. There has been no change in the Company's objectives and policies for managing this risk. The Company's liquidity position has been discussed in Section 1.6 *Liquidity.*

Foreign Exchange Risk

The Company is subject to both currency transaction risk and currency translation risk: its loan receivable from Liberty Star is denominated in US dollars; the Company's equity investment in the Pebble Partnership has a US dollar functional currency; and certain of the Company's corporate expenses are incurred in US dollars. As the Company's functional currency is the Canadian dollar, the fluctuation of the US dollar in relation to the Canadian dollar will consequently have an impact upon the losses incurred by the Company as well as the value of the Company's assets (as noted above) and total shareholders' equity. The Company has not entered into any agreements or purchased any instruments to hedge possible currency risks at this time.

The exposure of the Company's financial assets to foreign exchange risk is as follows:

Currency	December 31, 2012		December 31, 2011	
US dollars – Financial assets	Foreign currency amount	Amount in Canadian dollars	Foreign currency amount	Amount in Canadian dollars
Amounts receivable	$ 4,663	$ 4,639	$ 4,220	$ 4,292
Cash and cash equivalents	45	45	36	36
Total exposed to currency risk	**$ 4,708**	**$ 4,684**	**$ 4,256**	**$ 4,328**

The exposure of the Company's financial liabilities to foreign exchange risk is as follows:

Currency	December 31, 2012		December 31, 2011	
US dollars – Financial liabilities	Foreign currency amount	Amount in Canadian dollars	Foreign currency amount	Amount in Canadian dollars
Trade and other payables	$ 40	$ 40	$ 1	$ 1
Total exposed to currency risk	**$ 40**	**$ 40**	**$ 1**	**$ 1**

A 10% depreciation of the Canadian dollar relative to the United States dollar at December 31, 2012 would have decreased loss by $465 (2011 - $433). This analysis assumes that all other variables, in particular interest rates, remain constant.

There has been no change in the Company's objectives and policies for managing this risk, except for the changes in the carrying amounts of financial assets exposed to foreign exchange risk, and there was no significant change to the Company's exposure to foreign exchange risk during the year ended December 31, 2012.

Interest rate risk

The Company is subject to interest rate risk with respect to its investments in cash and cash equivalents. There has been no change in the Company's objectives and policies for managing this risk and no significant change to the Company's exposure to interest rate risk during the year ended December 31, 2012.

Assuming that all variables remain constant, a 100 basis points change in a decrease or increase in interest rates would have resulted in a decrease or increase in interest income of approximately $325 (2011 - $389).

Commodity price risk

While the value of the Company's core mineral resource property, held through its 50% interest in the Pebble Partnership, is related to the price of gold, copper and molybdenum and the outlook for these minerals, the Company currently does not have any operating mines and hence does not have any hedging or other commodity based risks in respect of its operational activities.

Gold, copper, and molybdenum prices have fluctuated widely historically and are affected by numerous factors outside of the Company's control, including, but not limited to, industrial and retail demand, central bank lending, forward sales by producers and speculators, levels of worldwide production, short-term changes in supply and demand because of speculative hedging activities, and certain other factors related specifically to gold.

Capital Management

The Company's policy is to maintain a strong capital base so as to maintain investor and creditor confidence and to sustain future development of the business. The capital structure of the Company consists of equity, comprising share capital, net of accumulated deficit.

There were no changes in the Company's approach to capital management during the year. The Company is not subject to any externally imposed capital requirements.

1.15 Other MD&A Requirements

Additional information relating to the Company, including the Company's Annual Information Form, is available under the Company's profile on SEDAR at www.sedar.com.

1.15.1 Disclosure of Outstanding Share Data

The capital structure of the Company is shown in the following table:

Common shares issued and outstanding	
As of March 27, 2013	94,999,764
As of December 31, 2012	94,999,764
Share options – as of March 27, 2013	7,578,630
(Weighted average exercise price per share: $7.00)	

1.15.2 Disclosure Controls and Procedures

The Company's management, with the participation of its Chief Executive Officer and Chief Financial Officer, have evaluated the effectiveness of the Company's disclosure controls and procedures. Based on that evaluation, the Company's Chief Executive Officer and Chief Financial Officer have concluded that, as of the end of the period covered by this report, the Company's disclosure controls and procedures were effective to provide reasonable assurance that the information required to be disclosed by the Company in reports it files is recorded, processed, summarized and reported, within the appropriate time periods and is accumulated and communicated to management, including the Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

1.15.3 Management's Report on Internal Control over Financial Reporting

The Company's management, including the Chief Executive Officer ("CEO") and the Chief Financial Officer ("CFO"), is responsible for establishing and maintaining adequate internal control over financial reporting. Internal control over financial reporting ("ICFR") is a process designed by, or under the supervision of, the Company's principal executive and principal financial officers and effected by the Company's Board of Directors, management and other personnel, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of consolidated financial statements for external purposes in accordance with IFRS. The Company's ICFR includes those policies and procedures that:

- pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the Company;
- provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with IFRS, and that receipts and expenditures of the Company are being made only in accordance with authorizations of management and directors of the company; and
- provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the Company's assets that could have a material effect on the consolidated financial statements.

The Company's management assessed the effectiveness of the Company's internal control over financial reporting as of December 31, 2012. In making the assessment, it used the criteria set forth in the Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO"). Based on their assessment, management has concluded that, as of December 31, 2012, the Company's internal control over financial reporting was effective based on those criteria.

The Company's internal control over financial reporting as of December 31, 2012, has been audited by Deloitte & Touche LLP, Independent Registered Chartered Accountants who also audited the Company's consolidated financial statements for the year ended December 31, 2012. Deloitte & Touche LLP as stated in their report that immediately precedes the Company's audited consolidated financial statements for the year ended December 31, 2012, expressed an unqualified opinion on the effectiveness of the Company's internal control over financial reporting.

1.15.4 Changes in Internal Control over Financial Reporting

There has been no change in the design of the Company's ICFR that has materially affected, or is reasonably likely to materially affect, the Company's ICFR during the period covered by this MD&A.

1.15.5 Limitations of Controls and Procedures

The Company's management, including its CEO and CFO, believe that any system of disclosure controls and procedures or ICFR, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Furthermore, the design of a control system must reflect the fact that there are resource constraints and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, they cannot provide absolute assurance that all control issues and instances of fraud, if any, within the Company have been prevented or detected. These inherent limitations include the realities that judgments in decision-making can be faulty and breakdowns can occur because of simple error or mistake. Additionally, controls can be circumvented by the individual acts of some persons, by collusion of two or more people, or by unauthorized override of controls. The design of any system of controls is also based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions. Accordingly, because of the inherent limitations in a cost effective control system, misstatements due to error or fraud may occur and not be detected.

1.15.6 Risk Factors

The following are the principal risk factors and uncertainties which, in management's opinion, are likely to most directly affect the ultimate feasibility of the Pebble project.

The Pebble Project's mineral property interests do not contain any ore reserves or any known body of economic mineralization

Although there are known bodies of mineralization on the Pebble Project, and the Pebble Partnership has completed core drilling programs within, and adjacent to, the deposits to determine measured and indicated resources, there are currently no known reserves or body of commercially viable ore and the Pebble Project must be considered an exploration prospect only. Extensive additional work is required before the Company or the Pebble Partnership can ascertain if any mineralization may be economic and hence constitute "ore". Engineering, socioeconomic and environmental studies are ongoing. Exploration for minerals is a speculative venture necessarily involving substantial risk. If the expenditures the Company and/or the Pebble Partnership incur and have incurred in the past on the Pebble Project do not result in discovery and development of commercial quantities of ore, the value of exploration and acquisition expenditures incurred will be totally lost.

Feasibility work to determine the viability of the Pebble Project has not been completed and permits have not been applied for

Final feasibility work has not been done to confirm the pit or underground mine design, mining methods, and processing methods. Final feasibility could determine that the currently assumed pit or other mine design, mining methods, and processing methods are incorrect. Construction and operation of the mine and processing facilities depends on securing environmental and other permits on a timely basis. No permits have been applied for and there can be no assurance that required permits can be secured or secured on a timely basis. Cost estimates used are based on costs at projects believed to be comparable, and not based on firm price quotes. Costs, including design, procurement, construction, and on-going operating costs and metal recoveries could be materially different from those currently assumed. There can be no assurance that mining can be conducted at assumed rates and grades. The project requires the development of port facilities, roads and electrical generating and transmission facilities. Although the Company believes that the State of Alaska favours the development of these facilities, there can be no assurance that these infrastructure facilities can be developed on a timely and cost-effective basis. Energy risks include the potential for significant increases in the cost of fuel and electricity.

Volatility in Metal Prices

The project has been evaluated using projected long-term price levels for copper, gold and molybdenum. Prices for these commodities are historically volatile, and neither the Company nor the Pebble Partnership has control of or influence on those prices, all of which are determined in international markets. The level of interest rates, the rate of inflation, the world supplies of and demands for copper, gold and molybdenum and the stability of exchange rates can all cause fluctuations in these prices. Such external economic factors are influenced by changes in international investment patterns and monetary systems and political developments. There can be no assurance that the prices of these commodities will continue at current levels or that they will not decline below the projected prices. The prices of copper, gold and molybdenum have fluctuated in recent years and they have shown an upward trend of late. Future significant price declines could cause unfavorable changes in the economics of the project and may result in investors being unwilling to finance mineral projects, with the result that the Company may not be able to obtain sufficient financing to fund its exploration and, if warranted, development activities.

Compliance with environmental requirements will command large resources and changes to these requirements could significantly increase the costs developing the Pebble Project and could delay these activities.

The Pebble Partnership and the Company must comply with stringent environmental legislation in carrying out work on the Pebble Project. Environmental legislation is evolving in a manner that will require stricter standards and enforcement, increased fines and penalties for non-compliance, more stringent environmental assessments of proposed projects and a heightened degree of responsibility for companies and their officers, directors and employees. Changes in environmental legislation could increase the cost to the Pebble Partnership of carrying out its exploration and, if warranted, development of the Pebble Project. Further, compliance with new or additional environmental legislation may result in delays to the exploration and, if warranted, development activities.

Changes in government regulations or the application thereof and the presence of unknown environmental hazards may result in significant unanticipated compliance and reclamation costs

Government regulations relating to mineral rights tenure, permission to disturb areas and the right to operate can adversely affect the Company. Northern Dynasty and the Pebble Partnership may not be able to obtain all necessary licenses and permits that may be required to carry out exploration and development at their project. Obtaining the necessary governmental permits is a complex, time-consuming and costly process. The duration and success of efforts to obtain permits are contingent upon many variables not within the Company's or the Pebble Partnership's control. Obtaining environmental permits may increase costs and cause delays depending on the nature of the activity to be permitted and the interpretation of applicable requirements implemented by the permitting authority. There can be no assurance that all necessary approvals and permits will be obtained and, if obtained, that the costs involved will not exceed those that we previously estimated. It is possible that the costs and delays associated with the compliance with such standards and regulations could become such that we would not proceed with the development of the Pebble Project or operation.

Refer further discussion in 1.2.1.5 *Bristol Bay Watershed Assessment.*

General Mining Risks

Mining is an inherently risky business with large capital expenditures and cyclical metals markets. Although the Company and the Pebble Partnership maintain high environmental standards for their project, like most major mining projects, there are almost always public concerns about new mining projects. The opponents of the Pebble Project are well organized and are trying to bring public and political pressure against the Pebble Project. If successful, the opponents could delay or prevent the commercialization of the Pebble Project even if it is found to be economically viable and technically and legally permittable.

The Company and Pebble Partnership also compete with many companies possessing far greater financial resources and technical facilities for the acquisition of mineral concessions, claims, leases and other mineral interests, as well as for the recruitment and retention of qualified employees.

The Pebble Project will require major financing, probably a combination of debt and equity financing. There can be no assurance that debt and/or equity financing will be available on acceptable terms. A significant increase in costs of capital could materially and adversely affect the value and feasibility of constructing the project.