

Condensed Interim Consolidated Financial Statements
ESSAR STEEL ALGOMA INC.
(Unaudited)
For the three and six-month periods ended September 30, 2011

ESSAR Steel Algoma Inc.

Condensed Interim Consolidated Statement of Comprehensive Income

(Unaudited)

Expressed in millions of Canadian dollars

	Three months ended September 30, 2011	Six months ended September 30, 2011	Three months ended September 30, 2010 <small>(Note 18)</small>	Six months ended September 30, 2010 <small>(Note 18)</small>
Revenue (Note 4)	\$ 564.0	\$ 1,130.0	\$ 469.9	\$ 945.6
Operating expenses				
Cost of sales (Note 5)	484.1	967.4	476.7	911.1
Administrative and selling	18.6	40.5	25.8	44.9
Income (loss) from operations	<u>61.3</u>	<u>122.1</u>	<u>(32.6)</u>	<u>(10.4)</u>
Finance income	(1.0)	(1.1)	-	-
Finance costs	21.0	42.0	21.1	42.4
Foreign exchange (gain) loss	(69.6)	(71.8)	31.5	(9.2)
	<u>(49.6)</u>	<u>(30.9)</u>	<u>52.6</u>	<u>33.2</u>
Income (loss) before income taxes	110.9	153.0	(85.2)	(43.6)
Income taxes (recovery) (Note 13)	37.2	46.1	(27.1)	(6.6)
Net income (loss)	73.7	106.9	(58.1)	(37.0)
Other comprehensive income (loss), net of income tax				
Unrealized foreign exchange gain (loss) on translation to presentation currency	1.4	1.3	(9.6)	3.5
Total comprehensive income (loss)	<u>\$ 75.1</u>	<u>\$ 108.2</u>	<u>\$ (67.7)</u>	<u>\$ (33.5)</u>

ESSAR Steel Algoma Inc.

Condensed Interim Consolidated Statements of Changes in Shareholder's Equity (Deficit)

(Unaudited)

Expressed in millions of Canadian dollars

	Capital Stock	Contributed surplus	Accumulated other comprehensive income (loss)	Deficit	Total shareholder's equity
Balance at April 1, 2011	\$ 490.4	\$ 58.2	\$ (22.7)	\$ (593.6)	\$ (67.7)
Net income				106.9	106.9
Other comprehensive income (loss)					
Foreign exchange gain on translation to presentation currency			1.3		1.3
Balance at September 30, 2011	<u>\$ 490.4</u>	<u>\$ 58.2</u>	<u>\$ (21.4)</u>	<u>\$ (486.7)</u>	<u>\$ 40.5</u>

	Capital Stock	Contributed surplus	Accumulated other comprehensive income (loss)	Deficit	Total shareholder's equity
Balance at April 1, 2010	\$ 490.4	\$ 58.2	\$ -	\$ (289.6)	\$ 259.0
Net loss				(37.0)	(37.0)
Other comprehensive income (loss)					
Foreign exchange gain on translation to presentation currency			3.5		3.5
Balance at September 30, 2010 (Note 18)	<u>\$ 490.4</u>	<u>\$ 58.2</u>	<u>\$ 3.5</u>	<u>\$ (326.6)</u>	<u>\$ 225.5</u>

See accompanying notes to the condensed interim consolidated financial statements

ESSAR Steel Algoma Inc.
Condensed Interim Consolidated Statement of Financial Position

(Unaudited)

Expressed in millions of Canadian dollars

	<u>September 30, 2011</u>	<u>March 31, 2011</u>
Assets		
Current		
Cash	\$ 13.9	\$ 5.7
Accounts receivable	244.2	160.4
Income taxes receivable	3.5	2.5
Loan receivable from related party (Note 16)	12.1	11.0
Inventories	365.3	278.4
Prepaid expenses	11.1	4.5
Total current assets	<u>650.1</u>	<u>462.5</u>
Non-current		
Property, plant and equipment, net (Note 6)	1,325.7	1,277.8
Intangible assets, net (Note 7)	90.8	90.6
Other assets	0.7	1.2
Deferred income tax assets	1.0	1.4
Total non-current assets	<u>1,418.2</u>	<u>1,371.0</u>
Total assets	<u>\$ 2,068.3</u>	<u>\$ 1,833.5</u>
Liabilities and shareholder's equity		
Current		
Bank indebtedness (Note 8)	\$ 175.4	\$ 184.5
Accounts payable and accrued liabilities	214.4	181.4
Current portion of provisions (Note 12)	-	1.1
Current portion of other long term liabilities	0.8	0.9
Total current liabilities	<u>390.6</u>	<u>367.9</u>
Non-current		
Long term debt (Note 9)	806.2	742.8
Accrued pension liability	298.2	308.1
Accrued post-employment benefit obligation	448.9	440.9
Provisions (Note 12)	3.4	3.8
Other long term liabilities	1.1	1.6
Deferred income tax liabilities	79.4	36.1
Total non-current liabilities	<u>1,637.2</u>	<u>1,533.3</u>
Total liabilities	<u>2,027.8</u>	<u>1,901.2</u>
Shareholder's equity (deficit)		
Accumulated other comprehensive loss	(21.4)	(22.7)
Deficit	(486.7)	(593.6)
	<u>(508.1)</u>	<u>(616.3)</u>
Capital stock	490.4	490.4
Contributed surplus	58.2	58.2
	<u>40.5</u>	<u>(67.7)</u>
Total liabilities and shareholder's equity (deficit)	<u>\$ 2,068.3</u>	<u>\$ 1,833.5</u>

See accompanying notes to the condensed interim consolidated financial statements

ESSAR Steel Algoma Inc.
Condensed Interim Consolidated Statements of Cash Flows
(Unaudited)

Expressed in millions of Canadian dollars

	Three months ended September 30, 2011	Six months ended September 30, 2011	Three months ended September 30, 2010 <small>(Note 18)</small>	Six months ended September 30, 2010 <small>(Note 18)</small>
Operating activities				
Net income (loss)	\$ 73.7	\$ 106.9	\$ (58.1)	\$ (37.0)
Adjustments and items not affecting cash:				
Depreciation on property, plant and equipment	38.9	81.4	44.0	91.9
Amortization of intangible assets and depreciation of non-productive property, plant and equipment	5.3	10.9	7.9	13.4
Deferred income tax expense (recovery)	36.9	43.7	(31.4)	(19.0)
Current income tax expense	0.3	2.4	4.2	12.4
Pension current funding in excess of expense	(7.4)	(8.5)	41.0	36.1
Unrealized foreign exchange (gain) loss on accrued pension liability	(24.1)	(23.6)	8.6	(3.4)
Post-employment benefit expense in excess of payments	4.0	8.1	7.6	10.4
Unrealized foreign exchange (gain) loss on accrued post-employment benefit obligation	(36.4)	(34.2)	13.8	(5.3)
Change in the fair value of embedded derivatives	-	-	(0.9)	(0.9)
Finance costs	21.0	42.0	21.1	42.4
Loss on disposal of property, plant and equipment	-	-	0.6	1.3
Unrealized foreign exchange (gain) loss on deferred income taxes	(5.2)	(5.1)	5.3	(2.0)
Other	1.3	1.6	(1.3)	(0.2)
	<u>108.3</u>	<u>225.6</u>	<u>62.4</u>	<u>140.1</u>
Changes in non-cash operating working capital (Note 15)	(60.0)	(119.6)	(40.9)	(40.9)
Cash generated from operating activities before interest and taxes	48.3	106.0	21.5	99.2
Interest paid	(19.8)	(39.6)	(20.2)	(41.5)
Income taxes recovered	-	1.2	10.7	10.3
Cash generated from operating activities	<u>28.5</u>	<u>67.6</u>	<u>12.0</u>	<u>68.0</u>
Investing activities				
Acquisition of property, plant and equipment	(22.8)	(34.9)	(13.0)	(27.0)
Acquisition of intangible asset	(1.3)	(2.3)	(0.5)	(1.1)
Loan receivable from related party (Note 16)	(0.1)	(0.2)	(0.1)	(11.2)
Cash used for investing activities	<u>(24.2)</u>	<u>(37.4)</u>	<u>(13.6)</u>	<u>(39.3)</u>
Financing activities				
Bank indebtedness, net	(6.9)	(22.3)	(27.8)	(54.0)
Other	(0.5)	(0.6)	0.4	-
Cash used for financing activities	<u>(7.4)</u>	<u>(22.9)</u>	<u>(27.4)</u>	<u>(54.0)</u>
Effect of exchange rate changes on cash	1.1	0.9	(1.4)	1.1
Cash				
Change	(2.0)	8.2	(30.4)	(24.2)
Opening balance	15.9	5.7	46.4	40.2
Ending balance	<u>\$ 13.9</u>	<u>\$ 13.9</u>	<u>\$ 16.0</u>	<u>\$ 16.0</u>

See accompanying notes to the condensed interim consolidated financial statements

ESSAR STEEL ALGOMA INC.
Notes to the Condensed Interim Consolidated Financial Statements (Unaudited)
Expressed in millions of Canadian dollars

1. GENERAL INFORMATION

Essar Steel Algoma Inc. (the "Company") is an integrated steel producer with its active operations located entirely in Canada. The Company produces sheet and plate products that are sold primarily in Canada and the United States. The Company is incorporated under the laws of Ontario, Canada. The Company's ultimate parent company is Essar Global Limited. The address of the Company's registered office is 105 West Street, Sault Ste. Marie, Ontario, P6A 7B4, Canada. The condensed interim consolidated financial statements of the Company for the three and six month periods ended September 30, 2011, are comprised of the Company and its subsidiaries.

2. BASIS OF PRESENTATION

Statement of compliance

These condensed interim consolidated financial statements, including comparatives, have been prepared in accordance with International Accounting Standard ("IAS") 34 *Interim Financial Reporting* and using the accounting policies the Company expects to adopt in its consolidated financial statements for the year ending March 31, 2012. These accounting policies are disclosed in Note 3 of the Company's condensed interim consolidated financial statements for the three month period ended June 30, 2011.

As these condensed interim consolidated financial statements are prepared in accordance with IAS 34, certain information and footnote disclosure normally included in annual financial statements prepared in accordance with International Financial Reporting Standards ("IFRS"), as issued by the International Accounting Standards Board ("IASB"), have been omitted or condensed. The preparation of financial statements in accordance with IAS 34 requires the use of certain critical accounting estimates. It also requires management to exercise judgment in applying the Company's accounting policies. The areas involving a higher degree of judgment or complexity, or areas where assumptions and estimates are significant to the financial statements have been set out in Note 4 of the Company's condensed interim consolidated financial statements for the three month period ended June 30, 2011.

These condensed interim consolidated financial statements should be read in conjunction with the Company's consolidated financial statements for the year ended March 31, 2011 and in consideration of the IFRS transition disclosures and additional annual disclosures included in Note 27 and Note 28 respectively of the Company's condensed interim consolidated financial statements for the three month period ended June 30, 2011.

The Company's annual consolidated financial statements, formerly prepared in accordance with previous Canadian Generally Accepted Accounting Principles ("previous CGAAP"), differ from IFRS in some areas. In preparing the IFRS statements, the Company amended certain accounting and valuations methods that had been applied under previous CGAAP. The 2011 comparative figures have been restated to reflect these adjustments. Note 18 contains reconciliations and descriptions of the effect of the transition from Canadian GAAP to IFRS on equity, earnings and other comprehensive income for the three and six month periods ended September 30, 2010.

Basis of presentation

The condensed interim consolidated financial statements have been prepared on a going concern assumption using historical cost basis and financial instruments that are measured at fair values, as explained in the accounting policies as disclosed in Note 3 of the Company's condensed interim consolidated financial statements for the three month period ended June 30, 2011.

ESSAR STEEL ALGOMA INC.
Notes to the Condensed Interim Consolidated Financial Statements (Unaudited)
Expressed in millions of Canadian dollars

2. BASIS OF PRESENTATION *(continued)*

Functional and presentation currency

The Company's functional currency is the United States dollar ("US dollar"). The US dollar is the currency of the primary economic environment in which the Company and subsidiaries operates. The items included in the condensed interim consolidated financial statements are measured using the US dollar.

The condensed interim consolidated financial statements are presented in millions of Canadian dollars ("C\$").

3. FUTURE ACCOUNTING CHANGES

Financial Instruments

In November 2009 and October 2010, the IASB issued IFRS 9 – Financial Instruments ("IFRS 9"), Classification and Measurement of Financial Assets and Financial Liabilities, respectively. IFRS 9 will replace IAS 39 – Financial Instruments: Recognition and Measurement ("IAS 39") in its entirety. IFRS 9 uses a single approach to determine whether a financial asset or liability is measured at amortized cost or fair value, replacing the multiple rules in IAS 39. For financial assets, the approach in IFRS is based on how an entity manages its financial instruments in the context of its business model and the contractual cash flow characteristics of the financial assets. The new standard also requires a single impairment method to be used, replacing the multiple impairment methods in IAS 39. For financial liabilities measured at fair value, fair value changes due to changes in the Company's credit risk are presented in other comprehensive income ("OCI"), instead of net income (loss), unless this would create an accounting mismatch. IFRS 9 is effective for annual periods beginning on or after January 1, 2013. Early adoption is permitted. The Company is assessing the potential impact of this standard.

Financial Instruments: Disclosure

In October 2010, the IASB amended IFRS 7 – Financial instruments: Disclosures, which will be applied prospectively for annual periods beginning on or after July 1, 2011. The amendments require additional disclosures on transferred financial assets. The Company is assessing the potential impact of these amendments.

Consolidated Financial Statements

In May 2011, the IASB issued IFRS 10 which provides additional guidance to determine whether an investee should be consolidated. The guidance applies to all investees, including special purpose entities. The standard is required to be adopted for periods beginning January 1, 2013. The Company is assessing the potential impact of this standard.

Joint Arrangements

In May 2011, the IASB issued IFRS 11 which presents a new model for determining whether an entity should account for joint arrangements using proportionate consolidation or the equity method. An entity will have to follow the substance rather than legal form of a joint arrangement and will no longer have a choice of accounting method. The standard is required to be adopted for periods beginning January 1, 2013. The Company is assessing the potential impact of this standard.

Disclosure of Interests in Other Entities

In May 2011, the IASB issued IFRS 12 which aggregates and amends disclosure requirements included within other standards. The standard requires a company to provide disclosures about subsidiaries, joint arrangements, associates and unconsolidated structured entities. The standard is required to be adopted for periods beginning January 1, 2013. The Company is assessing the potential impact of this standard.

ESSAR STEEL ALGOMA INC.
Notes to the Condensed Interim Consolidated Financial Statements (Unaudited)
Expressed in millions of Canadian dollars

3. FUTURE ACCOUNTING CHANGES *(continued)*

Fair Value Measurement

In May 2011, the IASB issued IFRS 13 to provide comprehensive guidance for instances where IFRS requires fair value to be used. The standard provides guidance on determining fair value and requires disclosures about those measurements. The standard is required to be adopted for periods beginning January 1, 2013. The Company is assessing the potential impact of this standard.

Presentation of Items of Other Comprehensive Income

In June 2011, the IASB issued amendments to IAS 1 Presentation of Financial Statements to split items of OCI between those that are reclassified to net earnings and those that do not. The standard is required to be adopted for periods beginning on or after July 1, 2012. The Company is assessing the potential impact of this standard.

Employee Benefits

In June 2011, the IASB issued amendments to IAS 19 that introduced changes to the accounting for defined benefit plans and other employee benefits. The amendments include elimination of the options to defer or recognize in full in earnings, actuarial gains and losses and instead mandates the immediate recognition of all actuarial gains and losses in other comprehensive income and requires use of the same discount rate for both the defined benefit obligation and the expected return on assets when calculating interest cost. Other changes include modification of the accounting for termination benefits and classification of other employee benefits. The amendment is effective for annual period beginning on or after January 1, 2013. The company is assessing the potential impact of this standard.

4. REVENUE AND SEGMENTED INFORMATION

The Company is viewed as a single business segment involving basic steel production for purposes of internal performance measurement and resource allocation.

The total revenue is comprised of:

	Three months ended 9/30/11	Six months ended 9/30/11	Three months ended 9/30/10	Six months ended 9/30/10
Sheet and strip	\$ 402.8	\$ 808.7	\$ 326.6	\$ 664.5
Plate	114.8	225.9	97.1	190.6
Freight	37.7	72.1	30.7	64.7
Non-steel revenue	8.7	23.3	15.5	25.8
	\$ 564.0	\$ 1,130.0	\$ 469.9	\$ 945.6

The geographical distribution of total revenue is as follows:

Sales to customers in Canada	\$ 272.0	\$ 573.5	\$ 226.7	\$ 484.2
Sales to customers in the United States	252.7	508.2	218.6	409.8
Sales to customers in the rest of the world	39.3	48.3	24.6	51.6
	\$ 564.0	\$ 1,130.0	\$ 469.9	\$ 945.6

For the periods ended September 30, 2011 and September 30, 2010, no single customer represented greater than 10% of total revenue.

ESSAR STEEL ALGOMA INC.
Notes to the Condensed Interim Consolidated Financial Statements (Unaudited)
Expressed in millions of Canadian dollars

5. COST OF SALES

	Three months ended 9/30/11	Six months ended 9/30/11	Three months ended 9/30/10	Six months ended 9/30/10
Cost of steel revenue	\$ 396.6	\$ 788.3	\$ 384.1	\$ 726.3
Cost of freight revenue	37.7	72.1	30.7	64.7
Cost of non-steel revenue	8.7	23.4	15.5	25.8
Depreciation included in cost of sales	41.1	83.6	46.4	94.3
	<u>\$ 484.1</u>	<u>\$ 967.4</u>	<u>\$ 476.7</u>	<u>\$ 911.1</u>
<i>Inventories recognized as cost of sales:</i>				
	<u>\$ 455.6</u>	<u>\$ 916.8</u>	<u>\$ 439.2</u>	<u>\$ 850.3</u>
<i>Inventory write-downs as a result of net realizable value lower than cost included in cost of sales:</i>				
	<u>\$ 0.3</u>	<u>\$ 0.4</u>	<u>\$ 0.8</u>	<u>\$ 1.4</u>

For the three month period ended September 30, 2011, \$18.6 million has been recognized in cost of steel revenue, which is a result of the settlement agreement reached with the Company's insurers on September 30, 2011 in connection with the losses that resulted from the chilling of Blast Furnace #7 in January 2011.

For the three and six month periods ended September 30, 2010, \$8.9 million and \$18.5 million have been recognized in cost of steel revenue, respectively, which are a result of insurance claim payments received in connection with the Blast Furnace #7 bustle main failure that occurred in September 2009.

There have been no reversals of any previously recorded inventory write-down during the three and six month periods ended September 30, 2011 (September 30, 2010 - nil).

6. PROPERTY PLANT AND EQUIPMENT

Carrying amount of	September 30, 2011	March 31, 2011
Freehold Land	\$ 19.1	\$ 17.7
Buildings	114.4	110.4
Machinery and Equipment	1,095.1	1,080.0
Computer Hardware	4.5	4.7
Mill Rolls	22.4	20.5
Assets under finance lease	1.7	2.0
Property under construction	68.5	42.5
	<u>\$ 1,325.7</u>	<u>\$ 1,277.8</u>

ESSAR STEEL ALGOMA INC.
Notes to the Condensed Interim Consolidated Financial Statements (Unaudited)
Expressed in millions of Canadian dollars

6. PROPERTY PLANT AND EQUIPMENT *(continued)*

Cost:	Freehold Land	Buildings	Machinery and Equipment	Mill Rolls	Computer Hardware	Assets under finance lease	Property under Construction	Total
Balance at March 31, 2011	\$ 17.7	\$ 181.5	\$ 1,621.8	\$ 30.5	\$ 8.5	\$ 5.5	\$ 42.5	\$ 1,908.0
Additions	-	2.1	6.2	5.2	0.1	0.1	21.2	34.9
Disposals	-	-	-	(2.4)	-	-	-	(2.4)
Foreign Exchange	1.4	14.9	131.9	2.8	0.6	0.4	4.8	156.8
Balance at September 30, 2011	\$ 19.1	\$ 198.5	\$ 1,759.9	\$ 36.1	\$ 9.2	\$ 6.0	\$ 68.5	\$ 2,097.3

Accumulated Depreciation:	Freehold Land	Buildings	Machinery and Equipment	Mill Rolls	Computer Hardware	Assets under finance lease	Property under Construction	Total
Balance at March 31, 2011	\$ -	\$ 71.1	\$ 541.8	\$ 10.0	\$ 3.8	\$ 3.5	\$ -	\$ 630.2
Eliminated on disposals of assets	-	-	-	(2.4)	-	-	-	(2.4)
Depreciation Expense	-	6.8	73.5	4.7	0.6	0.5	-	86.1
Foreign Exchange	-	6.2	49.5	1.4	0.3	0.3	-	57.7
Balance at September 30, 2011	\$ -	\$ 84.1	\$ 664.8	\$ 13.7	\$ 4.7	\$ 4.3	\$ -	\$ 771.6

Depreciation of property, plant and equipment

During the period July 1, 2011 to September 30, 2011 depreciation of property, plant and equipment was \$40.7 million (July 1, 2010 to September 30, 2010 - \$47.6 million). During the period April 1, 2011 to September 30, 2011 depreciation of property, plant and equipment was \$86.1 million (April 1, 2010 to September 30, 2010 - \$94.5 million).

Depreciation included in inventories

Depreciation included in inventories at September 30, 2011 amounted to \$11.3 million (March 31, 2011 - \$8.5 million).

Assets pledged as security

All of the Company's assets have been pledged to secure the borrowings of the Company. Please see Note 8.

ESSAR STEEL ALGOMA INC.
Notes to the Condensed Interim Consolidated Financial Statements (Unaudited)
Expressed in millions of Canadian dollars

7. INTANGIBLE ASSETS

The following table presents the changes to accumulated amortization on the Company's intangible assets for the period ended September 30, 2011.

Carrying amount of	September 30, 2011	March 31, 2011
Customer relationships	\$ 66.2	\$ 64.7
Technology	5.4	5.5
In-process research and development	2.0	2.1
Supply agreements	5.1	5.5
Essar Centre naming rights	1.0	1.0
Software	4.8	8.2
Software in development	6.3	3.6
	<u>\$ 90.8</u>	<u>\$ 90.6</u>

Cost	Customer Relationships	Technology	In-process research and development	Supply agreements	Essar Centre naming rights	Software	Software in Development	Total
Balance at March 31, 2011	\$ 90.8	\$ 9.5	\$ 4.1	\$ 11.4	\$ 1.4	\$ 34.7	\$ 3.6	\$ 155.5
Additions	-	-	-	-	-	-	2.3	2.3
Disposals	-	-	-	-	-	-	-	-
Foreign Exchange	7.4	0.8	0.3	0.9	0.1	2.8	0.4	12.7
Balance at September 30, 2011	\$ 98.2	\$ 10.3	\$ 4.4	\$ 12.3	\$ 1.5	\$ 37.5	\$ 6.3	\$ 170.5

Accumulated Amortization	Customer Relationships	Technology	In-process research and development	Supply agreements	Essar Centre naming rights	Software	Software in Development	Total
Balance at March 31, 2011	\$ 26.1	\$ 4.0	\$ 2.0	\$ 5.9	\$ 0.4	\$ 26.5	\$ -	\$ 64.9
Eliminated on disposals of intangible assets	-	-	-	-	-	-	-	-
Amortization Expense	3.5	0.6	0.3	0.8	0.1	3.7	-	9.0
Foreign Exchange	2.4	0.3	0.1	0.5	-	2.5	-	5.8
Balance at September 30, 2011	\$ 32.0	\$ 4.9	\$ 2.4	\$ 7.2	\$ 0.5	\$ 32.7	\$ -	\$ 79.7

Amortization of intangible assets

During the period July 1, 2011 to September 30, 2011 amortization of intangible assets was \$4.7 million (July 1, 2010 to September 30, 2010 – \$5.3 million). During the period April 1, 2011 to September 30, 2011 depreciation of property, plant and equipment was \$9.0 million (April 1, 2010 to September 30, 2010 - \$9.3 million).

All of the Company's assets have been pledged to secure the borrowings of the Company. Please see Note 8.

ESSAR STEEL ALGOMA INC.**Notes to the Condensed Interim Consolidated Financial Statements (Unaudited)**

Expressed in millions of Canadian dollars

8. BANKING FACILITIES

On June 20, 2007, the Company entered into a five-year Revolving Credit Agreement. The agreement provides the Company with a revolving credit facility ("Revolving Facility") equal to the lesser of a maximum lender commitment and a calculated borrowing base determined by the levels of the Company's accounts receivable and inventories, less certain reserves. The Revolving Facility is secured by substantially all of the Company's assets. Under the General Security Agreement, the Revolving Facility has priority claim on the accounts receivable and inventories of the Company and a secondary claim on the rest of the Company's assets. In addition to satisfying the borrowing base requirements in order to make borrowings under the Revolving Facility, the Company is required to either meet a fixed charge coverage ratio test or maintain a minimum excess availability of 10% of the Revolving Facility commitment. At September 30, 2011, the Company is required to maintain a minimum excess availability equal to US \$35 million.

The Revolving Facility permits borrowings of Canadian or US dollars. Canadian borrowings bear interest at either the Canadian bankers' acceptance rate plus a margin of 1.25% - 2.0% or Canadian prime rate plus a margin of 0.25% - 1.0%. US borrowings bear interest at either the London Inter-Bank Overnight Rate ("LIBOR") plus a margin of 1.25% - 2.0% or the lender's corporate base rate plus a margin of 0.25% - 1.0%. The applicable margin is dependent on the average excess availability under the Revolving Facility for the preceding fiscal quarter.

The Revolving Facility also provides for payment to the lenders of an unused line fee on the average daily excess availability of 0.25% per annum and a letter of credit fee ranging from 1.25% to 2.00%, depending on the average excess availability under the Revolving Facility. A commitment fee of 0.25% of the full amount of the Revolving Facility and a funding fee of 0.75% of the full amount of the Revolving Facility were incurred to establish the Revolving Facility and are being amortized to expenses using a straight-line method over 5 years. The unamortized balance of the Revolving Facility fees at September 30, 2011 is \$0.7 million (March 31, 2011 - \$1.2 million).

At September 30, 2011, there was \$175.4 million (includes US dollar denominated borrowings of US \$167.3 million) and \$184.5 million at March 31, 2011 (includes US dollar denominated borrowings of US \$185.0 million) outstanding under the Revolving Facility and \$136.1 million (March 31, 2011 - \$71.0 million) of unused availability after taking into account \$18.7million (March 31, 2011 - \$16.8 million) of outstanding letters of credit and the US \$35 million minimum excess availability requirement. In addition, the Company had \$13.6 million of unrestricted cash at September 30, 2011 (March 31, 2011 - \$5.7 million)

Under the terms of the Revolving Facility, the Company is required to be in compliance with various restrictive covenants which, among other things, limit the incurrence of additional indebtedness, limit investments, capital expenditures and dividends and restrict transactions with affiliates, permitted acquisitions, asset sales, liens and encumbrances and other matters customarily restricted in such agreements. The Company was in compliance with the financial covenant requirements of the Revolving Facility at September 30, 2011.

9. LONG TERM DEBT

	September 30, 2011	March 31, 2011
9.375 Senior Secured Notes denominated in US dollars due March 15, 2015	\$ 419.2	\$ 387.8
9 7/8 Senior Notes denominated in US dollars due June 15, 2015	<u>403.2</u>	<u>373.0</u>
	\$ 822.4	\$ 760.8
Less unamortized financing costs, premiums and/or discounts	<u>16.2</u>	<u>18.0</u>
	<u>\$ 806.2</u>	<u>\$ 742.8</u>

ESSAR STEEL ALGOMA INC.
Notes to the Condensed Interim Consolidated Financial Statements (Unaudited)
Expressed in millions of Canadian dollars

9. LONG TERM DEBT *(continued)*

The aggregate amount of principal repayments in each of the next five years and thereafter at current exchange rates is as follows:

2012	\$ -
2013	-
2014	-
2015	419.2
2016	403.2
	<u>\$ 822.4</u>

On December 14, 2009, the Company issued US \$400 million of 9.375% Senior Secured Notes (“Secured Notes”). The Secured Notes bear interest at 9.375% per annum which is payable on March 15 and September 15 of each year and will mature on March 15, 2015. Under an Inter-creditor Agreement, the Secured Notes have priority claim on all of the Company's assets except for accounts receivable and inventories. In addition, the Secured Notes have a secondary claim on accounts receivable and inventories. The Company applied the net proceeds from the sale of the Secured Notes to repay all amounts outstanding on the Term Loan facility that was in place prior to the Secured Notes issue, and to reduce the balance of the Revolving Facility and for general corporate purposes.

Subject to certain conditions, at any time prior to March 15, 2013, the Company may redeem up to 35% of the principal amount of the Secured Notes at a redemption price of 109.375% of the principal amount plus accrued and unpaid interest with the proceeds of a public equity offering. At any time prior to March 15, 2013, the Company may also redeem all or a part of the Secured Notes at a redemption price equal to 100% of the principal amount of the Secured Notes redeemed plus accrued and unpaid interest and a specified premium. On or after March 15, 2013, the Company may redeem all or a part of the Secured Notes at the following redemption prices, plus accrued and unpaid interest:

	<u>%</u>
2013	104.6875
2014 and thereafter	<u>100.0000</u>

The prepayment options in the Secured Notes are required to be accounted for as embedded call option derivative instruments, which require bifurcation and are accounted for at fair value. The embedded call options have an estimated fair value of nil at September 30, 2011 (March 31, 2011 - nil).

The Company also has US \$384.7 million of 9 7/8% Senior Notes (“Senior Notes”) outstanding. The Senior Notes were issued on June 20, 2007. The Senior Notes bear interest of 9 7/8% per annum which is payable on June 15 and December 15 each year. The Senior Notes are unsecured and are subordinated in right of payment to all existing and future secured indebtedness of the Company to the extent of the assets securing such indebtedness. The total Senior Notes outstanding on the issue date was \$450 million. During fiscal 2009, the Company purchased and cancelled US \$65.3 million of Senior Notes, leaving a remaining balance of US \$384.7 million.

ESSAR STEEL ALGOMA INC.

Notes to the Condensed Interim Consolidated Financial Statements (Unaudited)

Expressed in millions of Canadian dollars

9. LONG TERM DEBT *(continued)*

Subject to certain conditions, at any time prior to June 15, 2011, the Company was allowed to redeem all or a part of the Senior Notes at a redemption price equal to 100% of the principal amount of the Senior Notes redeemed plus accrued and unpaid interest and a specified premium. On or after June 15, 2011, the Company may redeem all or a part of the Senior Notes at the following redemption prices, plus accrued and unpaid interest:

	<u>%</u>
2011	104.938
2012	102.469
2013 and thereafter	<u>100.000</u>

The prepayment options in the Senior Notes are required to be accounted for as embedded call option derivative instruments, which require bifurcation and are accounted for at fair value. The embedded call options have an estimated fair value of nil at September 30, 2011 (March 31, 2011 - nil).

Total transaction costs and discounts related to the Secured Notes and Senior Notes amounted to \$30.3 million. Unamortized financing costs and discounts or premiums related to the Secured Notes and the Senior Notes totalling \$16.2 million at September 30, 2011 (March 31, 2011 - \$18.0 million) are recorded as a component of the carrying amount of the related debt and are amortized to net earnings using the effective interest rate method.

Under the terms of the Secured Notes and the Senior Notes, the Company is required to be in compliance with various restrictive covenants which, among other things, limit the incurrence of additional indebtedness, limit investments and dividends and restrict transactions with affiliates, permitted acquisitions, asset sales, liens and encumbrances and other matters customarily restricted in such agreements. The Company was in compliance with these requirements at September 30, 2011.

10. PENSION BENEFITS

Defined contribution plans

The Company initiated a defined contribution pension plan in 2004 for non-unionized employees joining the Company after January 1, 2003. As part of the contract negotiations with the Company and its locals which concluded on July 31, 2010, the locals and the Company agreed to include in this plan all unionized employees hired subsequent to August 1, 2010 and to offer to all the current employees the option to move to the Defined Contribution Pension Plan. The plan was revised during the year; these revisions went into effect March 1, 2011. Prior to March 1, 2011 the Company provided a base contribution of 3% of salary and also matched employee contributions to a maximum of 4%, depending on years of service. After March 1, 2011, the Company provides a base contribution of 5% of salary and also matches employee contributions to a maximum of 2%, depending on years of service for non-unionized employees. Additionally, the Company provides a contribution for unionized employees equal to two dollars and fifty cents per qualified hour. The pension expense under this plan is equal to the Company's contribution. The pension expense for the period ended September 30, 2011 was \$0.2 million (September 30, 2010 - \$0.2 million).

Defined benefit plans

The Company maintains non-contributory defined benefit pension plans that cover all employees not covered under the Defined Contribution Pension Plan (including pensioners retiring after January 1, 2002, which is the date that the Ontario Pension Benefit Guarantee Fund assumed some of the assets and obligations of the pension plans). The benefits are based on years of service and average earnings for a defined period prior to retirement.

ESSAR STEEL ALGOMA INC.**Notes to the Condensed Interim Consolidated Financial Statements (Unaudited)**

Expressed in millions of Canadian dollars

10. PENSION BENEFITS *(continued)*

The Company also maintains a closed plan for pensioners who retired prior to January 1, 2002. This plan provides the pensioners with a pension benefit in excess of the limits provided by the Ontario Pension Benefit Guarantee Fund.

The most recent actuarial valuations of plan assets and the present value of the defined benefit obligation were carried out at August 1, 2010 by Mercer (Canada) Limited. In August of 2010 the collective bargaining agreements with both local union groups were settled. The settlement resulted in a past service cost adjustment of \$44.6 million.

Amounts recognized in net earnings in respect of these defined benefit plans are as follows:

	Three months ended 9/30/11	Six months ended 9/30/11	Three months ended 9/30/10	Six months ended 9/30/10
Current service cost	\$ 5.8	\$ 11.4	\$ 5.6	\$ 11.2
Interest cost	14.4	29.0	14.6	28.9
Expected return on plan assets	(10.2)	(20.5)	(10.3)	(21.2)
Past service cost	-	-	44.6	44.6
Change in pension costs in inventory	-	1.2	(1.1)	(1.1)
Total defined benefit cost recognized in the condensed interim consolidated statement of comprehensive income	<u>\$ 10.0</u>	<u>\$ 21.1</u>	<u>\$ 53.4</u>	<u>\$ 62.4</u>
Defined benefit costs recognized in cost of sales	9.0	19.0	48.0	56.1
Defined benefit costs recognized in administrative and selling expense	1.0	2.1	5.4	6.3
	<u>\$ 10.0</u>	<u>\$ 21.1</u>	<u>\$ 53.4</u>	<u>\$ 62.4</u>
Cash flow information				
Total pension funding	<u>\$ 17.4</u>	<u>\$ 29.6</u>	<u>\$ 12.4</u>	<u>\$ 26.3</u>

Contributions for the period ended September 30, 2011 were based on actuarial valuations at August 1, 2010.

11. OTHER POST-EMPLOYMENT BENEFITS

The Company offers post-employment life insurance, health care and dental care to some of its retirees. These obligations are not pre-funded.

The most recent actuarial valuations of the present value of the other post-employment benefit obligation were carried out at March 31, 2011 by Mercer (Canada) Limited. In August of 2010 the collective bargaining agreements with both local union groups were settled. The settlement resulted in a past service cost adjustment of \$3.7 million.

ESSAR STEEL ALGOMA INC.
Notes to the Condensed Interim Consolidated Financial Statements (Unaudited)
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11. OTHER POST-EMPLOYMENT BENEFITS *(continued)*

Amounts recognized in net earnings in respect of these post-retirement benefit plans are as follows:

	Three months ended 9/30/11	Six months ended 9/30/11	Three months ended 9/30/10	Six months ended 9/30/10
Current service cost	\$ 1.2	\$ 2.4	\$ 1.1	\$ 2.3
Net interest cost	6.2	12.4	6.4	12.3
Past service cost	-	-	3.7	3.7
Change in other post employment benefit costs in inventory	-	0.1	(0.1)	(0.8)
Total other post employment benefit costs recognized in the condensed interim consolidated statement of comprehensive income	<u>\$ 7.4</u>	<u>\$ 14.9</u>	<u>\$ 11.1</u>	<u>\$ 17.5</u>
Other post employment benefit costs recognized in cost of sales	6.6	13.4	10.0	15.7
Other post employment benefit costs recognized in administrative and selling expense	0.8	1.5	1.1	1.8
	<u>\$ 7.4</u>	<u>\$ 14.9</u>	<u>\$ 11.1</u>	<u>\$ 17.5</u>
Cash flow information				
Payments made for other post-employment benefits on a pay-as-you-go basis	<u>\$ 3.4</u>	<u>\$ 6.8</u>	<u>\$ 3.5</u>	<u>\$ 7.1</u>

12. PROVISIONS

	Mining Related Obligations	Site Restoration & Decommissioning	Total
Balance at March 31, 2011	\$ 3.2	\$ 1.7	\$ 4.9
Charges net of reversals	-	0.1	0.1
Utilizations	-	(0.7)	(0.7)
Change in discount rate	(0.4)	(0.5)	(0.9)
Balance at September 30, 2011	<u>\$ 2.8</u>	<u>\$ 0.6</u>	<u>\$ 3.4</u>
March 31, 2011			
Current Portion	\$ 0.1	\$ 1.0	\$ 1.1
Long Term Portion	3.1	0.7	3.8
Total	<u>\$ 3.2</u>	<u>\$ 1.7</u>	<u>\$ 4.9</u>
September 30, 2011			
Current Portion	\$ -	\$ -	\$ -
Long Term Portion	2.8	0.6	3.4
Total	<u>\$ 2.8</u>	<u>\$ 0.6</u>	<u>\$ 3.4</u>

ESSAR STEEL ALGOMA INC.
Notes to the Condensed Interim Consolidated Financial Statements (Unaudited)
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12. PROVISIONS *(continued)*

Mining related obligations

Obligations are related to site restoration and closure for inactive iron ore mines located in northern Ontario. As there is no associated tangible long-lived asset, changes in the obligation are expensed.

Site restoration and decommissioning provision / Asset retirement obligations

This liability represents the Company's obligations associated with site restoration and decommissioning determined based on the Company's best estimate of the costs to be incurred, discounted at risk free rate adjusted for the risk specific to the liabilities. Changes in future conditions could require a change in this liability.

13. TAX MATTERS

The components of income tax expense are as follows:

	Three months ended 9/30/11	Six months ended 9/30/11	Three months ended 9/30/10	Six months ended 9/30/10
Current tax expense	\$ 0.3	\$ 2.4	\$ 4.3	\$ 12.4
Deferred income tax expense	<u>36.9</u>	<u>43.7</u>	<u>(31.4)</u>	<u>(19.0)</u>
Income tax expense	<u>\$ 37.2</u>	<u>\$ 46.1</u>	<u>\$ (27.1)</u>	<u>\$ (6.6)</u>

The composition of the deferred income tax expense is as follows:

Initiating and reversing temporary differences:

Accounting reserves and book-tax basis differences on inventories	\$ (0.5)	\$ 0.5	\$ (1.0)	\$ (0.4)
Pension and post-employment benefit expense	1.0	0.5	(12.2)	(12.1)
Tax depreciation less than book depreciation	(7.8)	(17.0)	(9.5)	(19.7)
Unrealized gain (loss) on foreign exchange translation on US dollar debt	(8.1)	(7.6)	3.5	(1.3)
Tax loss carry-forward	15.2	30.4	2.1	4.2
Foreign exchange (loss) gain on translation to presentation currency	36.6	35.1	(15.3)	9.0
Financing expenses	0.3	0.6	1.1	1.1
Other	\$ 0.2	\$ 1.2	\$ (0.1)	\$ 0.2
	<u>\$ 36.9</u>	<u>\$ 43.7</u>	<u>\$ (31.4)</u>	<u>\$ (19.0)</u>

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14. COMMITMENTS AND CONTINGENCIES

Operating leases

Under operating leases for premises and equipment, the Company is obligated to make aggregate payments of \$7.3 million, comprised of:

2012	\$	2.9
2013		2.8
2014		0.9
2015		0.5
2016 and thereafter		0.2
	<u>\$</u>	<u>7.3</u>

Key inputs to production

The Company requires large quantities of iron ore, coal, oxygen, electricity and natural gas in order to satisfy the demands of the steel manufacturing operation. The Company makes most of its purchases of these principal raw materials at negotiated prices under annual and multi-year agreements. These agreements provide the Company with comfort that an adequate supply of these key raw materials will be available to the Company at a price acceptable to the Company. The pricing of the iron ore purchased under these contracts is based on certain published benchmark pricing factors.

Legal Matters

From time to time, in the ordinary course of business, the Company is a defendant or party to a number of pending or threatened legal actions and proceedings. Although such matters cannot be predicted with certainty, management currently considers the Company's exposure to such claims and litigation, to the extent not covered by the Company's insurance policies or otherwise provided for, not to have a material adverse effect on these consolidated financial statements. In addition, the Company is involved in and potentially subject to regular audits from federal and provincial tax authorities relating to income, capital and commodity taxes and, as a result of these audits, may receive assessments and reassessments.

15. NET CHANGE IN NON-CASH OPERATING WORKING CAPITAL

	Three months ended 9/30/11	Six months ended 9/30/11	Three months ended 9/30/10	Six months ended 9/30/10
Accounts receivable	\$ (3.0)	\$ (67.9)	\$ (32.8)	\$ (5.7)
Income and other taxes payable	(1.9)	(4.3)	4.0	4.2
Inventories	(50.5)	(59.1)	(40.4)	(31.4)
Prepaid expenses and other current assets	(3.1)	(5.3)	(4.6)	(2.6)
Accounts payable and accrued liabilities	(1.7)	13.8	32.9	(5.1)
Loan receivable from related party	0.2	3.2	(0.1)	(0.4)
	<u>\$ (60.0)</u>	<u>\$ (119.6)</u>	<u>\$ (41.0)</u>	<u>\$ (41.0)</u>

ESSAR STEEL ALGOMA INC.

Notes to the Condensed Interim Consolidated Financial Statements (Unaudited)

Expressed in millions of Canadian dollars

16. RELATED PARTY TRANSACTIONS AND BALANCES

The Company's shareholder, ESSAR Steel Holdings Limited and its commonly controlled affiliates are related parties. Related party transactions which occur in the ordinary course of business are measured at the exchange amount, which is the amount of consideration agreed to between the parties.

The following transactions are reflected in the condensed interim consolidated statement of comprehensive income:

	Three months ended 9/30/11	Six months ended 9/30/11	Three months ended 9/30/10	Six months ended 9/30/10
Sales to affiliated companies under common control	\$ -	\$ -	\$ -	\$ 17.1
Purchases of raw materials from Essar Steel Holdings Limited, the Company's shareholder	30.8	45.9	15.3	18.6
Fees received for services provided to affiliated companies under common control	0.6	1.2	0.6	1.2
Interest income earned from an affiliated company under common control	0.1	0.2	0.1	0.2
Fees paid for services purchased from affiliated companies under common control	4.6	8.2	6.0	10.8
Fees paid for services purchased from a company owned by a director	-	-	0.4	0.6

The following balances are reflected in the condensed interim consolidated statement of financial position:

	September 30, 2011	March 31, 2011
The following balances with affiliated companies under common control were outstanding at the end of the reporting period:		
Accounts receivable	<i>a</i> \$ 0.7	\$ 3.8
Loan receivable from related party	<i>b</i> 11.5	10.7
Interest receivable	<i>c</i> 0.6	0.3
Accounts payable	<i>a</i> 0.5	0.7

The following balances with the Company's shareholder were outstanding at the end of the reporting period:

Prepaid expenses	<i>a</i> 0.6	0.3
Accounts payable	<i>a</i> 3.6	-

a Trade balances, bearing no interest due within 30 and 60 days.

b Promissory Note bearing interest at a rate of 3.29% per annum, due on demand.

c Interest receivable under promissory note "b" due on demand.

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16. RELATED PARTY TRANSACTIONS AND BALANCES *(continued)*

Contractual relationships with related parties:

The Company holds a promissory note in the amount of US dollar 11.0 million. The note is due from Essar Minerals Canada Limited. The note is due on demand, and bears interest at a rate of 3.29% per annum.

In November 2009, the Company entered into 20-year agreements with Essar Power Canada Limited as follows:

- [i] Energy Supply Agreement to purchase electricity at the Hourly Ontario Energy Price.
- [ii] A Shared Services Agreement to provide employees and other services.
- [iii] A Lease Agreement for the land on which the facility is built is for a nominal amount annually.

The Company's purchases and income under this agreement are reflected above.

The Company has entered into agreements with a related party to source its coal requirements until June 30, 2012 at predetermined prices. The Company's purchases under these agreements are reflected above.

17. FINANCIAL INSTRUMENTS

Financial risk management

The Company's activities expose it to a variety of financial risks including credit risk, liquidity risk and market risk. The Company may use derivative financial instruments to hedge certain of these risk exposures. The use of derivatives is based on established practices and parameters, which are subject to the oversight of the Board of Directors. The Company does not utilize derivative financial instruments for trading or speculative purposes.

Fair value of financial instruments

The fair value of cash, accounts receivable, loan receivable from related party, bank indebtedness and accounts payable and accrued liabilities approximates their carrying value due to the short-term nature of these instruments. At September 30, 2011, the fair value of the Senior Notes, including the embedded call options, was approximately \$312.5 million (March 31, 2011 - \$351.6 million) based on market pricing for the Senior Notes on or about that date. At September 30, 2011, the fair value of the Secured Notes, including the embedded call options, was approximately \$371.1 million (March 31, 2011 - \$393.7 million) based on market pricing for the Secured Notes on or about that date.

The following table represents the fair value hierarchy of derivative financial instruments by level:

	Reporting Period	Measurement	Total Carrying Value	Level One	Level Two	Level Three
Natural gas commodity contracts	September 30, 2011	Fair value	\$ (0.4)	\$ -	\$ (0.4)	\$ -
Natural gas commodity contracts	March 31, 2011	Fair value	(0.5)	-	(0.5)	-

ESSAR STEEL ALGOMA INC.

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17. FINANCIAL INSTRUMENTS *(continued)*

Credit risk

Credit risk is the risk of financial loss to the Company if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises primarily from the Company's receivables from customers. The Company has an established credit policy under which each new customer is analyzed individually for creditworthiness before the Company's standard payment and delivery terms and conditions are offered. The Company's review includes a review of the potential customer's financial information, external credit ratings and bank and supplier references. Credit limits are established for each new customer and customers that fail to meet the Company's credit requirements may transact with the Company only on a prepayment basis.

The maximum credit exposure at September 30, 2011 is the carrying amount of accounts receivable of \$244.2 million (March 31, 2011 - \$160.4 million). At September 30, 2011 there was no one customer account that represented 10% of this amount (March 31, 2011 - one customer greater than 10%). As at September 30, 2011 \$8.2 million or 3.4% of accounts receivable were more than 90 days overdue (March 31, 2011 - \$7.3 million or 4.5%).

The Company establishes an allowance for doubtful accounts that represents its estimate of incurred losses in respect of accounts receivable. The main components of this allowance are a specific provision that relates to individual exposures and a provision for expected losses that have been incurred but not yet identified. The allowance for doubtful accounts at September 30, 2011 was \$2.1 million (March 31, 2011 - \$1.6 million).

The Company may be exposed to certain losses in the event of non-performance by counterparties to derivative financial instruments such as commodity price contracts and foreign exchange contracts. The Company mitigates this risk by entering into transactions with highly rated major financial institutions.

Liquidity risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they come due. The Company manages liquidity risk by maintaining adequate cash balances and by appropriately utilizing the Revolving Facility to ensure that there is sufficient availability under the facility. The details of the Revolving Facility are described in Note 8. The Company continuously monitors and reviews actual and forecasted cash flows to ensure adequate liquidity and anticipate liquidity requirements.

Capital Management

The Company's objectives when managing capital are:

- 1) to maintain a flexible capital structure which optimizes the cost of capital at acceptable risk;
- 2) to meet external capital requirements on debt and credit facilities;
- 3) to ensure adequate capital to support long-term growth strategy; and
- 4) to provide an adequate return to shareholders.

The Company continuously monitors and reviews the capital structure to ensure the objectives are met.

Management defines capital as the combination of its indebtedness and equity balances and manages the capital structure within the context of the business strategy, general economic conditions, market conditions in the steel industry and the risk characteristics of assets.

External factors, such as the economic environment and the transition to IFRS have not changed the Company's objectives in managing capital.

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17. FINANCIAL INSTRUMENTS *(continued)*

The Company is in compliance with the covenants under its existing debt agreements at September 30, 2011 and throughout the first half of the Company's 2012 fiscal year.

The following table shows the Company's contractually agreed (undiscounted) cash flows payable under financial liabilities and derivative financial instruments as at the reporting period end:

September 30, 2011

Undiscounted Cash Flows	Carrying Amount	Contractual Cash Flows	Less Than 1 year	1-2 years	2-5 years	More Than 5 years
Non-derivative financial liabilities						
Senior Notes	\$ 403.2	\$ (403.2)	\$ -	\$ -	\$ (403.2)	\$ -
Interest on Senior Notes	11.6	(159.2)	(39.8)	(39.8)	(79.6)	-
Secured Notes	419.2	(419.2)	-	-	(419.2)	-
Interest on Secured Notes	1.8	(137.6)	(39.3)	(39.3)	(59.0)	-
Revolving Facility	175.4	(175.4)	(175.4)	-	-	-
Accounts payable and accrued liabilities	201.0	(201.0)	(201.0)	-	-	-
Derivative financial instruments (a)						
Gas purchase swap	0.4	(0.4)	(0.4)	-	-	-
	\$ 1,212.6	\$ (1,496.0)	\$ (455.9)	\$ (79.1)	\$ (961.0)	\$ -

(a) – The derivative financial instruments cash outflows represent the net contractual obligation

March 31, 2011

Undiscounted Cash Flows	Carrying Amount	Contractual Cash Flows	Less Than 1 year	1-2 years	2-5 years	More Than 5 years
Non-derivative financial liabilities						
Senior Notes	\$ 373.0	\$ (373.0)	\$ -	\$ -	\$ (373.0)	\$ -
Interest on Senior Notes	10.7	(184.2)	(36.8)	(36.8)	(110.6)	-
Secured Notes	387.8	(387.8)	-	-	(387.8)	-
Interest on Secured Notes	1.5	(145.4)	(36.4)	(36.4)	(72.6)	-
Revolving Facility	184.5	(184.5)	(184.5)	-	-	-
Accounts payable and accrued liabilities	169.2	(169.2)	(169.2)	-	-	-
Derivative financial instruments (a)						
Gas purchase swap	0.5	(0.5)	(0.5)	-	-	-
	\$ 1,127.2	\$ (1,444.6)	\$ (427.4)	\$ (73.2)	\$ (944.0)	\$ -

(a) – The derivative financial instruments cash outflows represent the net contractual obligation

Market risk

Market risk is the risk that changes in market prices, such as foreign exchange rates, interest rates and commodity prices, will affect the Company's income or the value of its holdings of financial instruments.

The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimizing the return on risk.

The Company occasionally buys and sells derivatives in order to manage market risks. These activities are carried out under the oversight of the Board of Directors.

ESSAR STEEL ALGOMA INC.**Notes to the Condensed Interim Consolidated Financial Statements (Unaudited)**

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17. FINANCIAL INSTRUMENTS *(continued)***Currency risk**

The Company is exposed to currency risk on purchases, labour costs and pension (Note 10) and other post retirement employment benefits (Note 11) liabilities that are denominated in Canadian dollars. The prices for steel products sold in Canada are derived mainly from price levels in the US market in US dollars converted into Canadian dollars at the prevailing exchange rates. As a result, a stronger US dollar relative to the Canadian dollar increases the Company's Canadian dollar selling prices for sales within Canada.

The Company's Canadian dollar denominated financial instruments were as follows:

	September 30, 2011	March 31, 2011
Cash	\$ 9.9	\$ 2.1
Accounts receivable	141.2	77.5
Bank indebtedness	-	(5.2)
Accounts payable and accrued liabilities	(164.8)	(157.3)
Other long-term liabilities	1.2	(1.6)
Net Canadian dollar liability	\$ (12.5)	\$ (84.5)

A \$0.01 decrease (or increase) in the US dollar relative to the Canadian dollar at September 30, 2011 would have decreased (or increased) income from operations by \$0.1 million (September 30, 2010 - nil).

Interest rate risk

Interest rate risk is the risk that the value of the Company's assets and liabilities will be affected by a change in interest rates. The Company's interest rate risk mainly arises from the interest rate impact on its debt. The Company may manage interest rate risk through the periodic use of interest rate swaps.

For the three and six month periods ended September 30, 2011 and September 30, 2010 a one percent increase (or decrease) in interest rates would have had a negligible effect on net earnings.

Commodity price risk

The Company is subject to price risk from fluctuations in the market prices of commodities, including natural gas, iron ore and coal. The Company enters into supply agreements for certain of these commodities as disclosed in Note 14. To manage risks associated with future variability in cash flows attributable to certain commodity purchases, the Company may use derivative instruments with maturities of 12 months or less. At September 30, 2011 the company had natural gas swap contracts in place with a fair value of \$0.4 million (March 31, 2011- \$0.5 million). The fair value of these contracts is included in accounts payable and accrued liabilities.

18. TRANSITION TO INTERNATIONAL FINANCIAL REPORTING STANDARDS (IFRS)**18.1 First-time Adoption of IFRS**

The Company has adopted IFRS effective April 1, 2011. The Company's date of transition was April 1, 2010 ("Transition Date"). Prior to the adoption of IFRS, the Company presented its consolidated financial statements in accordance with Canadian Generally Accepted Accounting Principals ("Previous CGAAP"). IFRS 1 – First-time Adoption of International Financial Reporting Standards ("IFRS 1") requires first-time adopters to reconcile prior period financial statements from previous CGAAP to IFRS. The Company's adoption of IFRS did not have an impact on the total operating, investing or financing cash flows.

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18. TRANSITION TO INTERNATIONAL FINANCIAL REPORTING STANDARDS (IFRS) (continued)

The elected exemption options, the mandatory exception to retrospective application of IFRS and the reclassifications for presentation under IFRS are described in Note 27 of the Company's condensed interim consolidated financial statements for the three month period ended June 30, 2011. Significant differences exist between the Company's Previous CGAAP accounting policies and the IFRS accounting policies selected. Notes 18.2, 18.3 and 18.4 contain reconciliations of the Shareholder's Equity and Statement of Comprehensive Income for the comparative periods presented in these condensed interim consolidated financial statements. The adjustments necessary to reconcile between Previous CGAAP and the IFRS accounting policies selected are presented below:

a Property, plant and equipment

IAS 16 – Property, Plant and Equipment requires the Company to componentize the amount initially recognized in respect of an item of property, plant and equipment to its significant parts and depreciate each part separately over its useful life. The Company determined that certain of its equipment assets have additional separable parts or “components”. These components were separately depreciated over their useful lives, which are usually less than the equipment to which the components belong, resulting in a higher depreciation charge.

b Provisions

Under IFRS, reserves and/or accruals for which there is a significant degree of uncertainty about the amount or timing of the payment are classified as provisions. In addition, a provision must be discounted when the time-value of money is material. Therefore, the Company reclassified certain accruals to provisions and has discounted these provisions where applicable.

Furthermore, IFRS specifies that the discount rate applied to the provision must be the rate that reflects the risks associated with the obligation. Under previous CGAAP, the Company measured its provisions for asset retirement obligations using the credit adjusted risk-free rate. As a result, the Company has re-measured its provisions for asset retirement obligations, which are now referred to as site restoration and decommissioning provisions under IFRS.

Under previous CGAAP, reserves and accruals are only recorded when a legal obligation exists. Under IFRS provisions are recorded for both legal and constructive obligations. A constructive obligation exists when an action by the Company indicates to a third party that it will accept certain responsibilities, and creates a valid expectation on the part of that third party that it will discharge those responsibilities.

c Employee Benefits

Under previous CGAAP the Company was using the corridor method to amortize gains and losses. On transition to IFRS, the Company elected to reset all cumulative unamortized actuarial gains and losses to zero as at the Transition Date. Cumulative actuarial gains and losses that existed at the Transition Date were recognized in opening retained earnings for the Company's employee benefit plans. The Company recognized all actuarial gains and losses that arose subsequent to the Transition Date immediately in OCI.

d Foreign exchange gains (losses)

The Company elected to reset all cumulative translation differences to zero as at the Transition Date. Cumulative translation differences that existed at the Transition Date were fully recognized in opening retained earnings. This adjustment also reflects foreign exchange translation impact of changes in the value of non-monetary items resulting from IFRS adjustments.

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18. TRANSITION TO INTERNATIONAL FINANCIAL REPORTING STANDARDS (IFRS) (continued)

e Income taxes

This adjustment reflects the change in current or deferred income taxes resulting from the effect of the IFRS adjustments described as allowed under IAS 12 - Income Taxes. This adjustment also includes the impact of recognition of deferred income taxes on temporary differences on non-monetary items due to the change in the exchange rate as the Company's taxable earnings are determined in a different currency from its functional currency.

f Foreign exchange loss (gain) on translation to presentation currency

This adjustment reflects exchange translation differences resulting from the use of a presentation currency other than the functional currency on amounts as determined under IFRS. This adjustment also includes incremental foreign exchange differences on non-current non-monetary items resulting from the change in functional currency as determined under IFRS.

18.2 Reconciliation of shareholder's equity from previous CGAAP to IFRS

The following is a reconciliation of the Company's total shareholder's equity reported in accordance with previous CGAAP to its shareholder's equity reported in accordance with IFRS for the following dates:

	Note	September 30, 2010	March 31, 2011
Total shareholder's equity as reported under previous CGAAP		\$ 395.1	\$ 95.5
Transitional adjustments:			
Property, plant and equipment	<i>a</i>	(46.6)	(58.0)
Provisions	<i>b</i>	2.7	3.2
Employee benefits	<i>c</i>	(145.3)	(165.3)
Foreign exchange gains (losses)	<i>d</i>	(39.7)	(31.7)
Income taxes	<i>e</i>	59.3	88.6
Total transitional adjustments		\$ (169.6)	\$ (163.2)
Total as reported under IFRS		\$ 225.5	\$ (67.7)

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18. TRANSITION TO INTERNATIONAL FINANCIAL REPORTING STANDARDS (IFRS) (continued)

18.3 Reconciliation of Comprehensive Income from previous CGAAP to IFRS

The following is a reconciliation of the Company's net income (loss) reported in accordance with previous CGAAP to its net loss in accordance with IFRS for the following periods:

	Note	Three months ended September 30, 2010	Six months ended September 30, 2010
Total net income (loss) as reported under previous CGAAP		\$ (39.6)	\$ 0.1
Transitional adjustments:			
Property, plant and equipment	<i>a</i>	(4.1)	(8.1)
Provisions	<i>b</i>	0.3	0.3
Employee benefits	<i>c</i>	(41.2)	(37.0)
Foreign exchange translation	<i>d</i>	(0.1)	5.3
Income taxes	<i>e</i>	26.6	2.4
Total transitional adjustments		\$ (18.5)	\$ (37.1)
Total net income (loss) as reported under IFRS		\$ (58.1)	\$ (37.0)
Comprehensive income (loss) as reported under previous CGAAP		\$ (54.4)	\$ 5.2
Transitional adjustments:			
Adjustments to net loss		(18.5)	(37.1)
Foreign exchange (gain) loss on translation to presentation currency	<i>f</i>	5.2	(1.6)
Total transitional adjustments		\$ (13.3)	\$ (38.7)
Total comprehensive income (loss) as reported under IFRS		\$ (67.7)	\$ (33.5)

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18. TRANSITION TO INTERNATIONAL FINANCIAL REPORTING STANDARDS (IFRS) (continued)

18.4 Reconciliation of Comprehensive Income from previous CGAAP to IFRS

18.4.1 Restated Condensed Consolidated Statement of Comprehensive Income - Function of Expense format under previous CGAAP - for the three month period ended September 30, 2010:

	Previous CGAAP	Adjustments for New Format	Function of Expense Format under previous CGAAP	
Sales	\$ 469.9		\$ 469.9	Revenue
Operating Expenses				Operating Expenses
		\$ 438.3	438.3	Cost of sales
Cost of sales excluding amortization	\$ 393.6	(393.6)		
Amortization	44.7	(44.7)		
	<u>\$ 438.3</u>			
Administrative and selling	15.9	5.8	21.7	Administrative and selling
Amortization of intangible assets and non-productive assets	<u>5.8</u>	<u>(5.8)</u>		
Income from operations	\$ 9.9		\$ 9.9	Income from operations
Interest on long-term liabilities, net	\$ 19.9	(19.9)		
Interest on short-term liabilities	1.1	(1.1)		
		21.0	\$ 21.0	Finance cost
Foreign exchange loss	29.1		29.1	
Investment income	<u>(0.1)</u>		<u>(0.1)</u>	Finance income
	<u>\$ 50.0</u>		<u>\$ 50.0</u>	
Loss before income taxes	\$ (40.1)		\$ (40.1)	Income before income taxes
Income taxes				
Current Expense	\$ 4.5	(4.5)		
Future recovery	<u>(5.0)</u>	5.0		
	<u>\$ (0.5)</u>		<u>(0.5)</u>	Income taxes
Net loss for the period	\$ (39.6)		\$ (39.6)	Net loss
Unrealized gain on foreign exchange translation	<u>(14.8)</u>		<u>(14.8)</u>	Foreign exchange gain on translation to presentation currency
Comprehensive loss	<u>\$ (54.4)</u>		<u>\$ (54.4)</u>	Total comprehensive loss

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18. TRANSITION TO INTERNATIONAL FINANCIAL REPORTING STANDARDS (IFRS) (continued)

18.4.2 Restated Condensed Consolidated Statement of Comprehensive Income under IFRS - for the three month period ended September 30, 2010:

	Function of Expense Format under Previous CGAAP	IFRS Adjustments	IFRS
Revenue	\$ 469.9		\$ 469.9
Operating expenses			
Cost of sales	438.3	\$ 38.4	476.7
Administrative and selling	21.7	4.1	25.8
Income from operations	\$ 9.9		\$ (32.6)
Finance cost	\$ 21.0	0.1	\$ 21.1
Foreign exchange loss	29.1	2.4	31.5
Finance income	(0.1)	0.1	-
	\$ 50.0		52.6
Income before income taxes	\$ (40.1)		\$ (85.2)
Income taxes	(0.5)	(26.6)	(27.1)
Net loss	\$ (39.6)		\$ (58.1)
Foreign exchange (loss) gain on translation to presentation currency	(14.8)	5.2	(9.6)
Total comprehensive loss	\$ (54.4)		\$ (67.7)

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Notes to the Condensed Interim Consolidated Financial Statements (Unaudited)

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18. TRANSITION TO INTERNATIONAL FINANCIAL REPORTING STANDARDS (IFRS) (continued)

18.4.3 Restated Condensed Consolidated Statement of Comprehensive Income - Function of Expense format under previous CGAAP - for the six month period ended September 30, 2010:

	Previous CGAAP	Adjustments for New Format	Function of Expense Format under previous CGAAP	
Sales	\$ 945.6		\$ 945.6	Revenue
Operating Expenses				Operating Expenses
		\$ 874.5	874.5	Cost of sales
Cost of sales excluding amortization	\$ 783.6	(783.6)		
Amortization	90.9	(90.9)		
	<u>\$ 874.5</u>			
Administrative and selling Amortization of intangible assets and non-productive assets	30.0 11.6	11.6 (11.6)	41.6	Administrative and selling
Income from operations	\$ 29.5		\$ 29.5	Income from operations
Interest on long-term liabilities, net	\$ 39.3	(39.3)		
Interest on short-term liabilities	3.0	(3.0)		
		42.3	\$ 42.3	Finance cost
Foreign exchange loss	(8.5)		(8.5)	
Investment income	<u>(0.2)</u>		<u>(0.2)</u>	Finance income
	\$ 33.6		\$ 33.6	
Loss before income taxes	\$ (4.1)		\$ (4.1)	Loss before income taxes
Income taxes				
Current Expense	\$ 12.5	(12.5)		
Future recovery	<u>(16.7)</u>	16.7		
	<u>\$ (4.2)</u>		<u>(4.2)</u>	Income taxes
Net income for the period	\$ 0.1		\$ 0.1	Net income
Unrealized gain on foreign exchange translation	<u>5.1</u>		<u>5.1</u>	Foreign exchange gain on translation to presentation currency
Comprehensive income	<u>\$ 5.2</u>		<u>\$ 5.2</u>	Total comprehensive income

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18. TRANSITION TO INTERNATIONAL FINANCIAL REPORTING STANDARDS (IFRS) (continued)

18.4.4 Restated Condensed Consolidated Statement of Comprehensive Income under IFRS - for the six month period ended September 30, 2010:

	Function of Expense Format under Previous CGAAP	IFRS Adjustments	IFRS
Revenue	\$ 945.6		\$ 945.6
Operating expenses			
Cost of sales	874.5	\$ 36.6	911.1
Administrative and selling	41.6	3.3	44.9
Income (loss) from operations	\$ 29.5		\$ (10.4)
Finance cost	\$ 42.3	0.1	\$ 42.4
Foreign exchange gain	(8.5)	(0.7)	(9.2)
Finance income	(0.2)	0.2	-
	<u>\$ 33.6</u>		<u>\$ 33.2</u>
Loss before income taxes	\$ (4.1)		\$ (43.6)
Income taxes	(4.2)	(2.4)	(6.6)
Net income (loss)	\$ 0.1		\$ (37.0)
Foreign exchange (loss) gain on translation to presentation currency	5.1	(1.6)	3.5
Total comprehensive income (loss)	<u>\$ 5.2</u>		<u>\$ (33.5)</u>

19. APPROVAL OF CONDENSED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

These condensed interim consolidated financial statements were approved and authorized for issue by the Audit Committee on November 9, 2011.