

Management's Discussion and Analysis

This management's discussion and analysis ("MD&A") of the consolidated operating results and financial position of Caledonia Mining Corporation Plc ("Caledonia" or the "Company") is for the quarter ended June 30, 2019 ("Q2 2019" or the "Quarter"). It should be read in conjunction with the Unaudited Condensed Consolidated Interim Financial Statements of Caledonia for the Quarter ("the Unaudited Condensed Consolidated Interim Financial Statements") which are available from the System for Electronic Data Analysis and Retrieval at www.sedar.com or from Caledonia's website at www.caledoniamining.com. The Unaudited Condensed Consolidated Interim Financial Statements and related notes have been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board. In this MD&A, the terms "Caledonia", the "Company", the "Group", "we", "our" and "us" refer to the consolidated operations of Caledonia Mining Corporation Plc and its subsidiaries unless otherwise specifically noted or the context requires otherwise.

Note that all currency references in this document are to US Dollars, unless otherwise stated. Amounts are expressed in thousands of US Dollars, unless otherwise stated or the context requires otherwise.

TABLE OF CONTENTS

1. Overview
2. Highlights
3. Summary Financial Results
4. Operations at the Blanket Gold Mine, Zimbabwe
 - 4.1. Safety, Health and Environment
 - 4.2. Social Investment and Contribution to the Zimbabwean Economy
 - 4.3. Gold Production
 - 4.4. Underground
 - 4.5. Metallurgical Plant
 - 4.6. Production Costs
 - 4.7. Capital Projects
 - 4.8. Indigenisation
 - 4.9. Zimbabwe Commercial Environment
 - 4.10. Opportunities and Outlook
5. Exploration and Project Development
 - 5.1. Blanket Exploration
 - 5.2. Blanket Satellite Prospects
6. Investing
7. Financing
8. Liquidity and Capital Resources
9. Off-Balance Sheet Arrangements, Contractual Commitments and Contingencies
10. Non-IFRS Measures
11. Related Party Transactions
12. Critical Accounting Estimates
13. Financial Instruments
14. Dividend Policy
15. Management and Board
16. Securities Outstanding
17. Risk Analysis
18. Forward-Looking Statements
19. Controls
20. Qualified Person

1. OVERVIEW

Caledonia is an exploration, development and mining corporation focused on Zimbabwe. Following the implementation of indigenisation at the Blanket Mine (“Blanket” or the “Blanket Mine”) in September 2012, Caledonia’s primary asset is a 49% legal ownership in Blanket, an operating gold mine in Zimbabwe. Pursuant to the signing of an agreement announced on November 6, 2018, Caledonia intends to purchase a further 15% of Blanket from one of Blanket’s indigenous shareholders. The transaction, which is discussed further in section 4.8, remains subject to approvals from various Zimbabwean regulatory authorities. Caledonia continues to consolidate Blanket, as explained in note 5 to the Unaudited Condensed Consolidated Interim Financial Statements; accordingly, operational and financial information set out in this MD&A is on a 100% basis, unless otherwise specified. Caledonia’s shares are listed on the NYSE American stock exchange (symbol - “CMCL”) and on the Toronto Stock Exchange (symbol - “CAL”). Depository interests in Caledonia’s shares are admitted to trading on AIM of the London Stock Exchange plc (symbol - “CMCL”).

2. HIGHLIGHTS

	Q2 2018	Q2 2019	H1 2018	H1 2019	Comment
Gold produced (oz)	12,657	12,712	25,582	24,660	Production was broadly similar, but lower than expected due to lower than expected mine production and grade
On-mine cost per ounce (\$/oz) ¹	717	534	702	662	On-mine costs are lower primarily due to lower electricity costs due to the devaluation of the Zimbabwe currency
All-in sustaining cost (\$/oz) ¹ (“AISC”)	856	656	843	797	AISC is lower due to lower on-mine costs and benefits from lower administrative expenses and sustaining capital expenditure.
Average realised gold price (\$/oz) ¹	1,278	1,298	1,296	1,291	The average realised gold price reflects international spot prices and excludes revenues from the gold support price or the export credit incentive
Gross profit ²	5,144	7,033	11,367	11,317	Gross profit is higher in the Quarter due to lower on-mine costs
Net profit attributable to shareholders	2,604	23,303	5,758	32,621	Net profit in the Quarter includes net foreign exchange gains of \$22.8 million; net profit for the six months to June 30, 2019 also includes profit of \$5.4 million arising on the sale of a subsidiary
Adjusted basic earnings per share (“EPS”) ³ (cents)	33.3	26.8	72.0	53.5	Adjusted EPS excludes, inter alia, the foreign exchange gains and related deferred tax implications.
Net cash and cash equivalents	5,308	7,875	5,308	7,875	Cash excludes term debt (repayable in 2022); cash position remains robust
Net cash (used in)/from operating activities	(1,216)	2,138	5,829	8,413	Continued robust cash generation

¹ Non-IFRS measures such as “On-mine cost per ounce”, “AISC” and “average realised gold price” are used throughout this document. Refer to section 10 of this MD&A for a discussion of non-IFRS measures.

² Gross profit is after deducting royalties, production costs and depreciation but before administrative expenses, other income, interest and finance charges and taxation.

³ Adjusted EPS is a non-IFRS measure which aims to reflect Caledonia’s ordinary trading performance. Refer to section 10 of this MD&A for a discussion of non-IFRS measures.

Completion of shaft sinking at Central Shaft

As announced on July 24, 2019 the Central Shaft has reached its target depth of 1,204 metres, which means that the shaft sinking phase of the project has been completed. Work has now commenced on equipping the shaft, which will take approximately 12 months, after which production from Central Shaft can commence. Production in 2021 is expected to be approximately 75,000 ounces, increasing to the target rate of 80,000 ounces in 2022.

Completion of the shaft-sinking phase at Central Shaft is a significant milestone and substantially de-risks the remainder of the project.

Production guidance reduced: earnings guidance maintained

12,712 ounces of gold were produced during the Quarter, 0.4% higher than in the second quarter of 2018 (the “comparable quarter” or “Q2 2018”). Mine production was adversely affected by Zimbabwe’s economic difficulties and technical problems; grade in the Quarter was lower than planned due to mining dilution. To a lesser extent, production was also adversely affected by lower than expected tonnes mined and milled and lower than expected recovery. Production in July continued to be hampered by lower than expected grade and interruptions to the electricity supply. To address the lower grade, underhand stoping will be re-introduced in certain areas in conjunction with improved support so that safety is not compromised. In the light of these difficulties, management has reduced production guidance for 2019 from a range of 53,000 to 56,000 ounces of gold to a range of 50,000 to 53,000 ounces. Notwithstanding the lower production guidance, earnings guidance for 2019 is maintained in the range of 86 to 117 cents due to the beneficial effects of the gold support price, the higher gold price and an anticipated further reduction in costs which are expected to outweigh the effects of lower production.

Zimbabwe commercial environment

Zimbabwe has a severe shortage of foreign exchange which hampers Blanket’s ability to procure the consumables and services it needs to sustain its current operations, to implement the investment programme and to remit funds from Zimbabwe that are needed to sustain Caledonia’s international operations and fund Caledonia’s dividend. Zimbabwe’s rate of inflation has also increased, which has an indirect effect on Blanket’s operations due to the adverse effect on workers morale.

Provided the exchange rate used to calculate Blanket’s locally denominated gold receipts is at an inter-bank rate that recognises economic fundamentals and Blanket continues to receive its gold proceeds promptly and in full, management is optimistic that government policy may create a more stable economic environment. Investors should recognize that Blanket’s ability to implement the investment programme and Caledonia’s ability to sustain its operations outside Zimbabwe and pay future dividends depends, inter alia, on the ability to continue to externalise cash from Zimbabwe.

In addition to the unstable incoming supply from the grid, from early July, Blanket (in common with other industrial users) has suffered extensive interruptions to its electricity supply due to a worsening in the supply and demand balance for electricity in Zimbabwe. After intensive discussions with all relevant parties, management is optimistic this matter will be resolved quickly. Management is well-advanced in the evaluation of a possible solar project which would reduce Blanket’s dependence on grid power and improve the quality and security of Blanket’s electricity supply.

Caledonia welcomes the recent changes which will reduce the burden of the royalty regime from September 1, 2019 (as discussed in section 4.9 of this MD&A).

Devaluation of the Zimbabwe Dollar results in substantial foreign exchange gains

The financial results for the quarter under IFRS include a substantial net foreign exchange profit due to the re-introduction of a Zimbabwe local currency and its devaluation against the US Dollar (which is the functional currency for Blanket mine and Caledonia) and the prohibition on the use of currencies other than the local currency for domestic transactions. The net foreign exchange gain in the quarter was \$21.6 million the largest components of which relate to the reduced US Dollar values of the deferred tax liability and the term loan. If the Zimbabwe currency remains at the current level against the US Dollar, Caledonia shareholders will eventually benefit from the devaluation, but only when the underlying liability falls due

for settlement. Caledonia presents “adjusted earnings”, a non-IFRS measure which aims to present the underlying commercial performance of the business. Adjusted earnings exclude, inter alia, unrealised foreign exchange losses and gains; a discussion of adjusted earnings, including a reconciliation to IFRS earnings, is included in section 10 of this MD&A. In the Quarter management restated the “adjusted earnings” to present the exclusions noted above net of the Non-controlling interest share to present adjusted earnings per share for the Company. Refer to section 10.3 for the effect of the Adjusted earnings.

Dividend Policy

Caledonia’s dividend policy is to pay a dividend of 6.875 US cents per share at the end of January, April, July and October. The profitability and cash generation of Blanket Mine remains strong. As discussed further in section 4.9, there is a risk that Caledonia may not be able to effect payments from Zimbabwe which are sufficient to fund further dividend payments.

Strategy and Outlook

Caledonia’s strategic focus is the implementation of the investment programme at Blanket, the main component of which is the Central Shaft project, which is outlined in section 4.7. Caledonia’s board and management believe the successful completion of the Central Shaft is in the best interests of all stakeholders because it is expected to result in increased production, reduced operating costs and increased flexibility to undertake further exploration and development, thereby safeguarding and enhancing Blanket’s long-term future. Caledonia intends to evaluate further investment opportunities in Zimbabwe that would not fall underneath Blanket’s ownership.

As noted above and as discussed in section 4.9, difficulties in obtaining adequate foreign currency may jeopardise Caledonia’s ability to implement its strategy.

3. SUMMARY FINANCIAL RESULTS

The table below sets out the consolidated profit and loss for the six months and quarters ended June 30, 2019 and 2018 prepared under IFRS.

Condensed Unaudited Consolidated Statement of Profit or Loss and Other Comprehensive Income				
(\$'000's)	3 months ended		6 months ended	
	June 30		June 30	
	2018	2019	2018	2019
Revenue	16,198	16,520	34,257	32,440
Royalty	(811)	(864)	(1,715)	(1,683)
Production costs	(9,297)	(7,571)	(19,307)	(17,340)
Depreciation	(946)	(1,052)	(1,868)	(2,100)
Gross profit	5,144	7,033	11,367	11,317
Other income	1,720	749	3,101	2,038
Other expenses	-	(220)	-	(309)
Administrative expenses	(1,660)	(1,309)	(3,202)	(2,705)
Profit on sale of subsidiary	-	-	-	5,409
Net foreign exchange gains	89	21,645	160	24,925
Cash-settled share-based payment	(223)	(9)	(337)	(370)
Equity-settled share-based payment	-	-	(14)	-
Gold hedge expense	-	(194)	-	(324)
Operating profit	5,070	27,695	11,075	39,981
Net finance (cost)/income	(29)	28	(45)	(20)
Profit before tax	5,041	27,723	11,030	39,961
Tax expense	(1,787)	223	(3,897)	(1,296)
Profit for the period	3,254	27,946	7,133	38,665
Other comprehensive income/(loss)				
<i>Items that are or may be reclassified to profit or loss</i>				
Foreign currency translation differences for foreign operations	(648)	144	(440)	-
Reclassification of accumulated exchange differences on the sale of subsidiary	-	-	-	(2,109)
Total comprehensive income for the period	2,606	28,090	6,693	36,556
Profit attributable to:				
Shareholders of the Company	2,604	23,303	5,758	32,621
Non-controlling interests	650	4,643	1,375	6,044
Profit for the period	3,254	27,946	7,133	38,665
Total comprehensive income attributable to:				
Shareholders of the Company	1,956	23,447	5,318	30,512
Non-controlling interests	650	4,643	1,375	6,044
Total comprehensive income for the period	2,606	28,090	6,693	36,556
Earnings per share (cents)				
Basic	24.1	210.9	53.4	299.4
Diluted	24.1	210.8	53.3	299.3
Adjusted earnings per share (cents) ⁽ⁱ⁾				
Basic	33.3	26.8	72.0	53.5

(i) *Adjusted EPS is a non-IFRS measure which aims to reflect Caledonia's ordinary trading performance. Refer to section 10 for a discussion of non-IFRS measures.*

Revenue in the Quarter was 2.0% higher than in Q2 2018 due to a 0.4% increase in ounces sold and a 1.6% increase in the average realised price of gold. The royalty rate payable to the Government of Zimbabwe was unchanged at 5% in the Quarter. Production for the Quarter is discussed in section 4.3 of this MD&A.

Production costs in the Quarter decreased by 18.6% compared to the comparable quarter mainly due to a lower electricity charge for the Quarter due to the devaluation in US Dollar terms of the RTGS\$-denominated electricity cost. Employee and consumable costs were also slightly below budget. Costs are discussed further in section 4.6 of this MD&A.

Depreciation was higher in the Quarter compared to the comparable quarter due to more items of property, plant and equipment being brought into use and depreciated.

Other income in the Quarter comprises the revenues arising from the gold support price; other income in the comparable quarter mainly comprised income in respect of the export credit incentive ("ECI"). The ECI and the gold support price are discussed in section 4.9 of this MD&A. The benefit arising from the gold support price diminished as the gold price increased to (and eventually exceeded) the gold support price of \$1,368 per ounce. Revenues arising from the ECI and the gold support price are recognised as "Other Income – Government Grant" on a receivable basis.

Other expenses in the Quarter include an impairment charge of \$149 arising on the damage to Blanket's auto tap changer which resulted from the instability of the incoming grid power, as discussed in section 4.4.

Administrative expenses comprise the costs of Caledonia's offices in Johannesburg, St Helier, Harare and London and include the costs of Caledonia's board and executives, the finance and procurement teams based in Johannesburg, investor relations, corporate development, legal and secretarial costs. Administrative expenses decreased in the Quarter by 21% compared to the comparable quarter and reflects the continued efforts by management to reduce administrative costs. Administrative expenses are analysed in note 8 to the Unaudited Condensed Consolidated Interim Financial Statements.

Net foreign exchange movements relate to gains and losses arising on monetary assets and liabilities that are held in currencies other than the US Dollar. Following the introduction of interbank trading between RTGS\$ and foreign currencies (as discussed in section 4.9 of this MD&A), the interbank rate was initially introduced at 2.5 RTGS\$ to 1 US Dollar and continued to weaken throughout the Quarter and at June 30, 2019 the rate was 6.5432 RTGS\$ to 1 US Dollar. The introduction of the interbank rate resulted in foreign exchange gains and losses in the Blanket Mine accounts as most transactions were previously denominated in US Dollar.

As a result of the introduction of the RTGS\$ on February 20, 2019, uncertainty was created as to what currency government and government parastatal liabilities were denominated in. On June 24, 2019 the Zimbabwean government issued Statutory Instrument 142 ("SI142") which required all transactions in Zimbabwe to be paid in RTGS\$ and the RTGS\$ was made the only legal tender. The announcement of SI142 clarified the Zimbabwean government's position as to what currency Zimbabwean transactions should be based in and indicated to management, government's intention to create a new currency and denominate their transactions in RTGS\$. The devaluation of the deferred tax and the electricity liabilities comprised the largest portion of the foreign exchange gain. The net foreign exchange gain in the Quarter was \$21.6 million of which approximately \$22.2 million related to the revaluation of the deferred tax and electricity liabilities in the Quarter. The change was applied in the Unaudited Condensed Consolidated Interim Financial Statements in the Quarter.

The cash-settled share-based payment expense reflects an accrual for a payment which is expected to arise from the long-term incentive plan ("LTIP") awards under the Company's 2015 Omnibus Equity Incentive Compensation Plan (the "Plan") to certain executives in the form of Restricted Share Units ("RSUs") and Performance Units ("PSUs"). LTIP awards may be settled in cash, shares or a combination of both at the discretion of the award holder. The LTIP expense in the Quarter was \$9 (2018: \$223) and reflects a combination of factors which include: the change in the Company's share price (which increased from \$6.02 in the Quarter to \$6.38); the increase in the number of RSUs due to the re-investment of attributable dividends; and the erosion of the time period until vesting. Further information on the calculation of the

charge is set out in note 10 to the Unaudited Condensed Consolidated Interim Financial Statements.

In January 2019 Caledonia entered into gold price hedging contracts for the 5 months from February 2019 until June 2019 for 22,500 ounces of production through the purchase of put options with a strike price of \$1,250 per ounce at a cost of \$324, which resulted in an expense for the Quarter of \$194. The hedge ensured that Caledonia received a minimum price of \$1,250 per ounce of gold for the duration of the contracts whilst maintaining full upside participation. Caledonia will re-assess the requirement for any hedging in the context of, inter alia, the prevailing gold price, Blanket's production rate and cash generation capacity and Blanket's capital expenditure programme.

The tax credit comprises the following:

Analysis of Consolidated Tax expense/(credit) for the Quarter				
(\$'000's)				
	Zimbabwe	South Africa	GMS-UK	Total
Income tax	1,665	190	-	1,855
Withholding tax				
Dividend	-	-	40	40
Management Fee	-	32	-	32
Deemed Dividend	35	-	-	35
Deferred tax	(2,177)	(8)	-	(2,185)
	<u>(477)</u>	<u>214</u>	<u>40</u>	<u>(223)</u>

The overall effective taxation rate in the Quarter was (0.8%) compared to 35% in the comparable quarter. The overall effective taxation rate in the Quarter was significantly affected by the high unrealised foreign exchange profit in the Quarter and a deferred tax credit.

Zimbabwean deferred tax, which reflects *inter alia* the difference between the accounting and tax treatments of capital investment, has historically been a large component of the overall tax charge. (100% of capital expenditure is deductible in the year in which it is incurred for the purposes of calculating Zimbabwean income tax, whereas for accounting purposes depreciation commences when the project enters production.) However, in the Quarter there was a substantial deferred tax credit (rather than an expense) due to the calculation of Blanket's tax liability using RTGS\$-denominated accounts.

Withholding tax is Zimbabwean withholding tax on dividends and management fees.

The non-controlling interests are 16.2% of Blanket's net profit which is attributable to Blanket's indigenous Zimbabwean shareholders and reflects their participation in the economic benefits generated by Blanket from the effective date of the indigenisation. This is explained in note 5 of the Unaudited Condensed Consolidated Interim Financial Statements.

Adjusted EPS is a non-IFRS measure which reflects Caledonia's ordinary trading performance. Refer to section 10 of this MD&A for a reconciliation of adjusted EPS to basic EPS on an IFRS basis.

Risks that may affect Caledonia's future financial condition are discussed in sections 4.9 and 17.

The table below sets out the consolidated statements of cash flows for the six months and quarters ended June 30, 2019 and 2018 prepared under IFRS.

Condensed Consolidated Statement of Cash Flows (unaudited)				
(\$'000's)				
	3 months ended		6 months ended	
	June 30		June 30	
	2018	2019	2018	2019
Cash flows from operating activities				
Cash generated from operations	749	2,484	8,433	9,117
Net interest paid	(44)	16	(82)	(96)
Tax paid	(1,921)	(362)	(2,522)	(608)
Net cash (used in)/from operating activities	(1,216)	2,138	5,829	8,413
Cash flows used in investing activities				
Acquisition of Property, plant and equipment	(5,618)	(4,186)	(10,776)	(9,326)
Proceeds from disposal of subsidiary	-	-	-	1,000
Net cash used in investing activities	(5,618)	(4,186)	(10,776)	(8,326)
Cash flows from financing activities				
Dividends paid	(862)	(882)	(1,761)	(1,620)
Repayment of term loan facility	(375)	-	(750)	-
Net cash used in financing activities	(1,237)	(882)	(2,511)	(1,620)
Net decrease in cash and cash equivalents	(8,071)	(2,930)	(7,458)	(1,533)
Effect of exchange rate fluctuations on cash held	(1)	1,063	10	(1,779)
Net cash and cash equivalents at beginning of the period	13,380	9,742	12,756	11,187
Net cash and cash equivalents at end of the period	5,308	7,875	5,308	7,875

Cash generated from operating activities is analysed in note 16 to the Unaudited Condensed Consolidated Interim Financial Statements.

Cash generated from operations in the Quarter was \$2,484, higher than the \$749 in the comparable quarter. The increase was largely due to a reduction in working capital of approximately \$2.4 million (2018: increase of approximately \$5.6 million).

Net investment in property, plant and equipment remains high in terms of the Central Shaft project, which is discussed further in section 4.7 of this MD&A and in sustaining capital investment.

The dividends paid relate to the quarterly dividend paid by Caledonia in the Quarter.

The effect of exchange rate fluctuations on cash held reflects the devaluation of RTGS\$-denominated cash balances following the introduction of the inter-bank trading mechanism by the Reserve Bank of Zimbabwe (the "RBZ") which is discussed in section 4.9. The adverse effect on cash balances forms part of an overall foreign exchange gain arising on the devaluation of all affected financial assets and liabilities.

The table below sets out the consolidated statements of Caledonia's financial position at the end of the Quarter and December 31, 2018 prepared under IFRS.

Consolidated Statements of Financial Position (unaudited)			
<i>(\$'000's)</i>	<i>As at</i>	June 30	Dec 31
		2019	2018
Total non-current assets		105,671	97,525
Inventories		9,729	9,427
Prepayments		1,550	866
Trade and other receivables		6,492	6,392
Cash and cash equivalents		7,875	11,187
Assets held for sale		-	296
Total assets		131,317	125,693
Total non-current liabilities		7,411	34,687
Trade and other payables		7,601	10,051
Income tax payable		1,598	1,538
Liabilities associated with assets held for sale		-	609
Total liabilities		16,610	46,885
Total equity		114,707	78,808
Total equity and liabilities		131,317	125,693

Non-current assets increased due to the continued investment in terms of the Central Shaft project and investment to sustain existing operations.

Prepayments represents deposits and advance payments for goods and services, including capital items that are being fabricated and which will be delivered to Blanket in due course.

Trade and other receivables are analysed in note 15 to the Unaudited Condensed Consolidated Interim Financial Statements and include \$3,575 (December 31, 2017: \$2,695) due from Fidelity in respect of gold deliveries prior to the close of business on June 30, 2019 and \$1,435 (December 31, 2017: \$2,743) due from the Government of Zimbabwe in respect of VAT refunds. The increased amount due from Fidelity reflects the extension of the payment cycle following the implementation of the monetary policy announced by the RBZ on February 20, 2019 as discussed in section 4.9. The amounts due from Fidelity were received in full after the end of the Quarter. The amount due in respect of VAT refunds is denominated in RTGS Dollars and was similar in RTGS Dollar terms at the end of the Quarter compared to December 31, 2018. However, following the devaluation of the RTGS Dollar after the implementation of the February 20, 2019 monetary policy the amount receivable in US Dollar terms was significantly reduced. Trade receivables include \$1,961 (2018: nil) in respect of deferred consideration due on the disposal of Eersteling Gold Mine, the sale of which was concluded in the previous quarter and is discussed in the previous MD&A.

Non-current liabilities reduced from \$34,687 at December 31, 2018 to \$7,411 at the end of the Quarter mainly due to the conversion of the RTGS\$ 6 million term facility and the deferred tax liability into US Dollars as these balances are denominated in RTGS\$.

The following information is provided for each of the eight most recent quarterly periods ending on the dates specified. The figures are extracted from underlying unaudited interim financial statements that have been prepared using accounting policies consistent with IFRS.

	Sept 30,	Dec 31,	Mar 31,	June 30,	Sept 30,	Dec 31,	Mar 31,	June 30,
(\$'000's except per share amounts)	2017	2017	2018	2018	2018	2018	2019	2018
Revenue from operations	18,230	19,599	18,059	16,198	16,647	17,495	15,920	16,520
Profit attributable to owners of the Company	3,120	3,232	3,154	2,604	2,224	2,784	9,318	23,303
Earnings per share – basic (cents)	29.4	29.5	29.3	24.1	20.4	25.1	88.6	210.8
Earnings per share – diluted (cents)	29.4	29.4	29.2	24.1	20.4	25.2	88.5	210.9
Net cash and cash equivalents	11,830	12,765	13,380	5,308	5,896	11,187	9,742	7,875

The quarterly results fluctuate materially from quarter to quarter primarily due to changes in production levels and gold prices but also due to the recording of impairments and other unusual costs and incomes. Significant changes relating to prior quarters are discussed in the relevant MD&As and financial statements.

4. OPERATIONS AT THE BLANKET GOLD MINE, ZIMBABWE

4.1 Safety, Health and Environment

The following safety statistics have been recorded for the Quarter and the preceding seven quarters.

Blanket Mine Safety Statistics								
Classification	Q3 2017	Q4 2017	Q1 2018	Q2 2018	Q3 2018	Q4 2018	Q1 2019	Q2 2019
Fatal	1	0	1	0	1	0	0	0
Lost time injury	5	0	1	3	1	0	2	0
Restricted work activity	2	4	6	5	4	1	3	7
First aid	1	2	1	2	6	0	0	0
Medical aid	9	4	4	2	1	6	1	1
Occupational illness	0	0	0	0	0	0	0	0
Total	18	10	13	12	13	7	6	8
Incidents	10	11	7	10	8	7	12	15
Near misses	6	2	4	1	2	4	5	2
Disability Injury Frequency Rate	0.95	0.00	0.31	0.44	0.29	0.00	0.32	0.00
Total Injury Frequency Rate	2.86	1.57	2.03	1.77	1.78	1.12	0.97	1.23
Man-hours worked (thousands)	1,257	1,271	1,278	1,352	1,371	1,252	1,240	1,296

Following the high level of accidents in 2018 a safety training facility (called the Nyanzvi initiative) was established at the mine using dedicated facilities and specially trained facilitators. Two teams are withdrawn from production each week for a 5-day period to be retrained with particular focus on behavioural changes and reinforcing safety standards and practices. 763 employees participated in the Nyanzvi scheme during the Quarter, increasing the total number of employees who have passed through the scheme to 1,766. As a result of this increased focus on safety training, there has been a reduction in the number of accidents. Safety training is an ongoing exercise and it will remain an area of focus for management.

4.2 Social Investment and Contribution to the Zimbabwean Economy

Blanket's investment in community and social projects which are not directly related to the operation of the mine or the welfare of Blanket's employees, the payments made to the Gwanda Community Share Ownership Trust ("GCSOT") in terms of Blanket's indigenisation, and payments of royalties, taxation and other non-taxation charges to the Government of Zimbabwe and its agencies are set out in the table below.

Payments to the Community and the Zimbabwe Government (\$'000's)					
Period	Year	Community and Social Investment	Payments to GCSOT	Payments to Zimbabwe Government	Total
Year	2013	2,147	2,000	15,354	19,501
Year	2014	35	-	12,319	12,354
Year	2015	50	-	7,376	7,426
Year	2016	12	-	10,637	10,649
Year	2017	5	-	11,988	11,993
Year	2018	4	-	10,140	10,144
Q1	2019	14	-	2,567	2,581
Q2	2019	27	-	2,360	2,387

Payments in respect of community and social investment includes a donation of food and materials to the victims of cyclone Idai, and allowances paid to students from tertiary institutions who are on attachment to Blanket Mine.

4.3 Gold Production

Tonnes milled, average grades, recoveries and gold produced during the Quarter, the preceding 9 quarters, the years 2016, 2017 and 2018 and July 2019 are shown in the table below.

Blanket Mine Production Statistics					
		Tonnes Milled	Gold Head (Feed) Grade (g/t Au)	Gold Recovery (%)	Gold Produced (oz)
Year	Year	(t)			
Year	2016	510,661	3.30	93.0	50,351
Quarter 1	2017	124,225	3.42	93.7	12,794
Quarter 2	2017	136,163	3.08	92.8	12,518
Quarter 3	2017	136,064	3.52	93.6	14,396
Quarter 4	2017	150,755	3.62	93.6	16,425
Year	2017	547,207	3.41	93.4	56,133
Quarter 1	2018	123,628	3.48	93.4	12,924
Quarter 2	2018	132,585	3.19	92.8	12,657
Quarter 3	2018	151,160	3.12	92.6	13,978
Quarter 4	2018	153,540	3.27	92.8	14,952
Year	2018	560,913	3.26	92.9	54,511
Quarter 1	2019	122,389	3.26	93.4	11,948
Quarter 2	2019	135,847	3.11	93.2	12,712
July	2019	44,682	3.01	92.4	3,996

Gold production for the Quarter was 0.4% higher than the comparable quarter and 6.4% higher than the previous quarter. Mine production was adversely affected by Zimbabwe's economic difficulties and technical problems; grade in the Quarter was lower than in the comparable quarter and was lower than planned due to continued incidence of mining dilution. To a lesser extent, production was also adversely affected by lower than expected tonnes mined and milled and lower than expected recovery. Grade and tonnes milled discussed in section 4.4 of this MD&A; gold recoveries are discussed in section 4.5 of this MD&A. Production in July 2019 continued to be affected by lower than expected grade and interruptions to the electricity supply.

4.4 Underground

Tonnes milled in the Quarter were 2.5% higher than the comparable quarter and 11% higher than the preceding quarter. Ore production continues to be hampered by a high number of shifts lost due to an increase in unauthorised employee absences ("AWOLs") and employee desertions, which resulted in the loss of critical skilled workers such as long-hole drillers and LHD drivers. The situation has improved somewhat since the preceding quarter. Management believes that a contributory factor to the higher levels of AWOLs and desertions is the economic hardship felt by employees following the sharp reduction in their spending power after the introduction of new monetary policies in October 2018 and Blanket's inability to pay salaries or part thereof in US Dollars (as certain other mining companies were able to do) due to Blanket's US Dollar-denominated capital commitments at Central Shaft. The introduction in late February 2019 of an interbank trading market between RTGS Dollars and foreign currencies has allowed management to increase the RTGS\$-denominated remuneration of employees. This has gone some way to alleviate the hardship that employees previously experienced and has resulted in improved morale in March and April. Buffer teams have also been introduced to cater for the effects of unforeseen employee absences due to AWOL's.

Ore production was also adversely affected by mechanical breakdowns of trackless equipment in the declines which contribute approximately 20% of production. These breakdowns are due to the shortage of US dollars since October 2018 which, as previously disclosed, resulted in the loss of skilled LHD drivers and caused Blanket to run out of critical spares for a period. Measures have been taken to improve the maintenance and

use of such equipment and to improve the availability of critical spares.

Blanket continues to experience an unstable electricity supply from the grid due to lack of maintenance by the government-owned utility (ZESA). In the preceding quarter, the high frequency of power surges damaged Blanket's auto tap changer which enables the transformer to accommodate voltage surges. Without the auto tap changer the transformer has only a finite capacity to regulate surges and much more power trips are experienced. The auto tap changer was repaired and re-installed in May. However, whilst it was being repaired Blanket experienced an increased incidence of production delays due to power surges. Although Blanket has back-up diesel generators to maintain production, each power surge results in the loss of up to an hour of production as electrical equipment has to be re-set, the generators are started and the compressed air system is re-charged. Generator usage in the Quarter totalled 686 hours, compared to 1,486 hours in the whole of 2018. Management is evaluating a range of solutions to this problem as discussed in section 4.9 of this MD&A.

The grade in the Quarter was lower than planned due to a re-occurrence of mining dilution. Measures taken in previous quarters to improve the accuracy of drilling have had some effect. However, in certain areas, after accurate blasting took place, sloughing of the hanging wall and footwall has introduced waste material into the draw points. To address this problem, under-hand stoping will be re-introduced into certain areas with additional measures to enhance safety.

Primary development advanced in the Quarter by 2,482 metres compared to 2,070 metres in the previous quarter and a plan of 2,901 metres. The shortfall against plan was largely due to an excessive number of lost shifts due to absenteeism by experienced workers.

Production in July was adversely affected by the introduction of load-shedding by ZESA. From early July, Zimbabwe's electricity supply was substantially reduced and ZESA required industrial users to substantially reduce their power consumption. Blanket currently has enough back-up diesel generators to run the entire mining and processing operation; however, it does not have enough standby capacity to maintain production and continue work at Central Shaft. Additional diesel generators to supply Central Shaft have been purchased and will be installed in August. Zimbabwe's electricity situation and the measures that are being taken to address it is discussed in section 4.9 of this MD&A.

4.5 Metallurgical Plant

Plant throughput in the Quarter was 69.4 tonnes per hour ("tph") compared to 68.1 tph in the previous quarter due to higher ore production as discussed in section 4.4. Recoveries in the Quarter were 93.2% compared to 93.4% in the previous quarter. The lower recovery was mainly due to the lower plant feed grade.

Recoveries continue to be adversely affected by the failure of the oxygen plant which is now beyond repair. Lower oxygen concentrations also resulted in increased cyanide consumption, which contributed to increased consumable costs at the metallurgical plant. A new oxygen plant has been purchased and is expected to be commissioned in the fourth quarter of 2019.

4.6 Production Costs

A narrow focus on the direct costs of production (mainly labour, electricity and consumables) does not fully reflect the total cost of gold production. Accordingly, cost per ounce data for the Quarter and the comparable quarter have been prepared in accordance with the Guidance Note issued by the World Gold Council on June 23, 2013 and is set out in the table below on the following bases:

- i. **On-mine cost per ounce⁴**, which shows the on-mine costs of producing an ounce of gold and includes direct labour, electricity, consumables and other costs that are incurred at the mine including insurance, security and on-mine administration;
- ii. **All-in sustaining cost per ounce⁴**, which shows the on-mine cost per ounce *plus* royalty paid, additional costs incurred outside the mine (i.e. at offices in Harare, Johannesburg, London and Jersey), costs associated with maintaining the operating infrastructure and resource base that are required to maintain production at the current levels (sustaining capital investment), the share-based expense (or credit)

⁴ *On-mine cost per ounce, all-in sustaining cost per ounce and all-in cost per ounce are non-IFRS measures. Refer to section 10 for a reconciliation of these amounts to IFRS*

arising from the LTIP awards less silver by-product revenue. The all-in sustaining cost also includes as a credit (i.e. as a deduction from costs) the ECI and the gold support price; and

- iii. **All-in cost per ounce⁴**, which shows the all-in sustaining cost per ounce *plus* the costs associated with activities that are undertaken with a view to increasing production (expansion capital investment).

Cost per Ounce of Gold Sold (US\$/ounce)	3 Months to June 30		6 Months to June 30	
	2018	2019	2018	2019
	On-mine cost ⁴	717	534	702
All-in sustaining cost per ounce ⁴	856	656	843	797
All-in cost per ounce ⁴	1,254	976	1,204	1,163

Per-ounce costs are calculated based on gold ounces sold and not produced, so that an accurate value can be ascribed to the royalty and the ECI. A reconciliation of costs per ounce to IFRS production costs is set out in section 10.

On-Mine costs

On-mine costs comprises labour, electricity, consumables and other costs such as safety and on-mine administration costs which include security and insurance. On-mine costs are analysed in note 6 to the Unaudited Condensed Consolidated Interim Financial Statements. On-mine costs per ounce decreased by 25% from \$717 in Q2 2018 to \$534 in the Quarter.

On-mine costs benefitted from a change in the estimated electricity costs incurred after the introduction of the interbank exchange rate mechanism in late February 2019. The power supply agreement which expired on December 31, 2018 provided for uninterrupted power supply at a cost of 12.8 cents per kilowatt hour. After the introduction of the interbank mechanism it was unclear whether the rate was denominated in US cents, local currency units or in local currency but at a rate that reflected the interbank exchange rate. Following the introduction of SII42 (as discussed in section 4.9 of this MD&A) management believes it is appropriate to recognise a cost for electricity supply in the period from late February 2019 until June 30, 2019 at a rate of RTGS\$12.8 cents per kilowatt hour.

During the Quarter, it was decided that all employee payments be benchmarked to the US Dollar (i.e. including overtime and holiday pay) and be paid at the interbank rate that prevails at the time of payment in RTGS\$. Thus, the benefit of the weakening RTGS\$ was not reflected in the employee expenses in the previous quarter and the effect of the Quarter 1 saving were corrected in the Quarter for the devalued payments made in February and March. Otherwise than for the effect of the above, labour costs were slightly below budget for the Quarter. On-mine costs reflected the budgeted increase in certain consumable costs and the increased costs of the larger fleet of underground trackless equipment as more ore is mined from the declines and costs associated with planned activities such as mill re-lines.

All-in sustaining costs

All-in sustaining costs per ounce were 23% lower in the Quarter compared to the comparable quarter. The decrease reflects the lower on-mine costs per ounce, lower administrative expenses and reduced sustaining capital expenditure which outweighed the lower income arising from the gold support price, the value of which diminished as the gold price increased through the support price of \$1,368/ounce during the Quarter.

All-in costs

All-in costs include investment in expansion projects which remained at a high level in the Quarter due to the continued investment at Blanket, as discussed in section 4.7 of this MD&A.

4.7 Capital Projects

The main capital development project is the Central Shaft, which was originally intended to be sunk in one single phase from surface to 1,080 metres. Continued exploration has improved the understanding of the ore bodies and has resulted in progressive increases in resources below 750 metres. Accordingly, in November 2017, the Company announced that it intended to continue to sink the Central Shaft by two further production

levels to a depth of 1,330 metres. Progress on sinking the shaft since late 2017 was adversely affected by the increased frequency of power trips due to the unstable incoming supply from the grid. Due to these delays in the MD&A for the third quarter of 2018 we announced that the vertical shaft sinking would be reduced by one level and the shaft would be sunk to a depth of 1,204 metres. The fourth level is intended to be added via a decline construction of which will start in approximately 3-4 years. The decline will put the mine in a good position to go deeper in future if needed without affecting the hoisting at the then operational Central Shaft. As announced on July 24, 2019 the Central Shaft has reached its target depth of 1,204 metres, which means that the shaft sinking phase of the project has now been completed. Work has now commenced on equipping the shaft, which will take approximately 12 months, after which production from Central Shaft can commence. Production in 2021 is expected to be approximately 75,000 ounces, increasing to the target rate of 80,000 ounces in 2022. Our ability to achieve these milestones will depend on the availability of foreign currency and a stable and un-interrupted power supply.

4.8 Indigenisation

Transactions that implemented the indigenisation of Blanket (which expression in this section and in certain other sections throughout this MD&A refers to the Zimbabwe company that owns Blanket Mine) were completed on September 5, 2012 following which Caledonia owns 49% of Blanket and has received a Certificate of Compliance from the Government of Zimbabwe which confirms that Blanket is fully compliant with the *Indigenisation and Economic Empowerment Act*.

As a 49% shareholder, Caledonia receives 49% of Blanket's dividends plus the repayment of vendor facilitation loans which were extended by Blanket to certain of the indigenous shareholders. The outstanding balance of the facilitation loans as at June 30, 2019 was \$30.98 million (December 31, 2018: \$31.99 million). The facilitation loans (including interest thereon) are repaid by way of dividends from Blanket; 80% of the dividends declared by Blanket which are attributable to the beneficiaries of the facilitation loans are used to repay such loans and the remaining 20% unconditionally accrues to the respective indigenous shareholders. The dividends attributable to GCSOT, which holds 10% of Blanket, will be withheld by Blanket to repay the advance dividends which were paid to GCSOT in 2012 and 2013 and which had an outstanding balance of \$2.19 million at June 30, 2019 (December 31, 2017: \$2.84 million).

On June 23, 2017 a modification to the facilitation loans was agreed which reduced the rate of interest on the facilitation loans from LIBOR plus 10% to the lower of 7.25% payable quarterly, or 80% of the dividend paid in the quarter by Blanket which is attributable to indigenous shareholders. The reduction in the interest rate is retrospectively applied from January 1, 2017 and reflects the general lowering of interest rates in Zimbabwe.

The facilitation loans are not shown as receivables in Caledonia's financial statements in terms of IFRS. These loans are effectively equity instruments as their only means of repayment is via dividend distributions from Blanket. Caledonia continues to consolidate Blanket for accounting purposes. Further information on the accounting effects of indigenisation at Blanket is set out in note 5 to the Unaudited Condensed Consolidated Interim Financial Statements and in a Frequently Asked Questions page which is available on Caledonia's website.

Pronouncements from the Zimbabwe Government following the appointment of the new President in late 2017 indicated that the indigenisation policy would be relaxed, including the removal of an indigenisation requirement for gold mining companies. These pronouncements were passed into law in March 2018. On November 6, 2018, the Company announced that it had entered into a sale agreement with Fremiro Investments (Private) Limited ("Fremiro") to purchase Fremiro's 15% shareholding in Blanket for a gross consideration of \$16.667 million to be settled through a combination of the cancellation of the loan between the two entities which stood at \$11.467 million as at June 30, 2018 and the issue of 727,266 new shares in Caledonia at an issue price of \$7.15 per share. On completion of the transaction, Caledonia will have a 64% shareholding in Blanket and Fremiro will hold approximately 6.4% of Caledonia's diluted equity. The transaction remains subject to, amongst other things, approvals from various Zimbabwean regulatory authorities including the RBZ and the Zimbabwe Revenue Authority. Caledonia has indicated to the Government of Zimbabwe a desire to engage in discussions to purchase the shareholding in Blanket that is currently held by the National Indigenisation and Economic Empowerment Fund ("NIEEF"). There is no certainty that agreement will be reached on a transaction in respect of NIEEF's shareholding.

4.9 Zimbabwe Commercial Environment

Monetary Conditions

The current situation in Zimbabwe can be summarized as follows:

- There continues to be a severe shortage of foreign currency.
- The rate of inflation has increased since October 2018: the annual rate of inflation in September 2018 was approximately 5%, however by June 2019, the annual inflation rate had increased to 175%. A high rate of inflation has little effect on Blanket's operations other than the adverse effect on employee morale if their remuneration is not adjusted to reflect the increased cost of living – this is discussed further below.
- Since October 2018, bank accounts in Zimbabwe have been bifurcated between Foreign Currency Accounts (“FCA”), which can be used to make international payments, and local currency (known as “RTGS Dollars” or “RTGS\$”) accounts which can only be used for domestic transactions. Previously all bank accounts in Zimbabwe were in the RTGS\$ system;
- On February 20, 2019 the RBZ allowed inter-bank trading between currency held in the RTGS\$ system and the FCA system. Prior to this, the RBZ had stipulated that a Dollar in the RTGS system was worth 1 US Dollar in the FCA system. Initially the interbank rate was 2.5 RTGS Dollars to 1 US Dollar; this rate weakened to RTGS\$3.003:US Dollar 1 as at March 31, 2019 and has weakened further to RTGS\$6.5432: US Dollar 1 as at June 30, 2019. The RTGS Dollar has continued to weaken after the end of Quarter.
- The interbank trading mechanism has addressed the most pressing difficulty that emerged after the October 2018 policy implementation, being the erosion of the purchasing power of Blanket's employees due to rapidly increasing retail prices, which had an adverse effect on employee morale. Management has increased RTGS\$-denominated remuneration so that it remains more closely aligned to the US Dollar value using the interbank rate. This has alleviated some of the financial distress experienced by Blanket employees.
- Zimbabwean gold producers, including Blanket, are required to sell their gold to Fidelity Printers and Refiners Limited (“Fidelity”), a subsidiary of the RBZ. 55% of the sale proceeds are received in FCA and the balance is received in RTGS\$. Blanket uses the FCA component to pay for imported goods and services, the RTGS component is used to pay for goods and services which are procured in Zimbabwe and to pay employees, taxes and electricity. A 55% allocation is insufficient to allow Blanket to continue normal mining operations, to fully implement the investment plan as scheduled and allow Caledonia to also remit dividends and loan repayments from Zimbabwe.
- If Blanket or Caledonia require additional FCA, they must make an application to the RBZ for an additional allocation of foreign exchange as there is insufficient liquidity on the interbank market to make any significant purchases of FCA. The RBZ considers requests for additional foreign currency in specific circumstances from individual gold miners and Caledonia has continued its engagement with the RBZ and the government to secure the additional foreign currency it requires. This requirement to make specific application for foreign currency is no different from the situation which existed before the implementation of the new policy. Hitherto, Blanket and Caledonia have operated satisfactorily under this system, although it requires constant management attention.
- On October 1, 2018 the RBZ issued a directive to Zimbabwean banks to separate foreign currency from RTGS\$ on the accounts held by their clients and pegged the RTGS\$ at 1:1 to the US Dollar. On February 20, 2019 the RBZ issued a further monetary policy statement, which allowed inter-bank trading between RTGS\$ and foreign currency. The interbank rate was introduced at 2.5 RTGS\$ to 1 US Dollar and traded at 6.5432 RTGS\$ to 1 US Dollar as at June 30, 2019. On June 24, 2019 the Government issued S.I. 142 which stated: “*Zimbabwe dollar (RTGS\$) to be the sole currency for legal tender purposes for any transactions in Zimbabwe*”. Throughout these announcements and to the date of issue of these financial statements the US Dollar has remained the primary currency in which the Group's Zimbabwean entities operate and the functional currency of these entities. Previously there was uncertainty as to what currency would be used to settle amounts owed to the Zimbabwe government. The announcement of

S.I.142 clarified the Zimbabwean Government's intentions that these liabilities were always denominated in RTGS\$ and that RTGS\$ would be the currency in which they would be settled. The devaluation of the deferred tax and electricity liabilities contributed the largest portion of the foreign exchange gain

- Blanket's borrowings are denominated in RTGS Dollars, which means their value in US Dollars has reduced due to the devaluation of the RTGS Dollar. In the ordinary course of events, Blanket would increase its RTGS-denominated debt so that the US Dollar value remains broadly unchanged; in particular, Blanket requires an overdraft facility of approximately US\$4 million for working capital purposes. Policy interventions by the RBZ have reduced the lending capacity of Blanket's domestic bankers and they are unable to restore Blanket's overdraft limit to the historic US-Dollar value. Management is therefore exploring other sources of local finance. In the context of Blanket's restricted access to foreign exchange (because it receives only 55% of its revenues in FCA), management does not think it prudent to seek debt funding outside Zimbabwe. The interest rate on RTGS\$-denominated borrowings has increased: after the end of the Quarter the Company was notified that the interest rate on Blanket's unsecured overdraft facility will increase from 6.875% to 35.78%.
- Provided the interbank exchange rate is efficient and Blanket continues to receive the amounts due promptly, in full and at an exchange rate which reflects economic fundamentals, management is optimistic the revised policy may create a more stable environment. Investors should recognize that Blanket's ability to implement its investment plan and Caledonia's ability to sustain its operations outside Zimbabwe and pay future dividends depends, inter alia, on the ability to continue to externalise cash from Zimbabwe.

Export credit incentive ("ECI") and Gold support price

Blanket sells gold to Fidelity and is contractually entitled to receive a price which is derived from the afternoon price fixed by the London Bullion Market Association (the "LBMA price") the day after the bullion delivered by Blanket has been assayed. 55% of Blanket's proceeds are received in US Dollars and the remainder is received in RTGS\$ using the interbank exchange rate for RTGS\$ and US Dollars.

Prior to February 20, 2019, Blanket in common with the other gold producers, received the ECI which was a 10% premium to the LMBA price. On February 27, 2019 Caledonia announced the termination of the ECI programme and the financial effect thereof.

From March 6, 2019 it became apparent that Blanket's sales proceeds received from Fidelity were calculated at a gross price of \$44,000 per kilogram (\$1,368.58 per ounce), which exceeded the prevailing LBMA price. On May 12, 2019 the Company received confirmation from Fidelity of this arrangement, called the "gold support price", which has been implemented to incentivize gold producers to increase gold production. The gold support price has not been increased as the LMBA gold price has subsequently increased above \$1,368.58 per ounce; Caledonia has no information whether the gold support price would be re-introduced if the LMBA price fell below \$1,368.58 per ounce.

The income arising from the gold support price is included as "Other Income". Management has not adjusted earnings guidance for 2019 which remains unchanged from the announcement of February 27, 2019.

Electricity supply

Zimbabwe's electricity generation is mainly from the Kariba hydro station on the Zambezi and the Hwange coal-fired station with several other much smaller coal-fired power stations. Even if Zimbabwe's installed generating capacity is fully operational, it cannot generate enough electricity to meet its requirements and therefore Zimbabwe imports electricity from Mozambique and South Africa. Until recently, Zimbabwe managed its electricity supply and demand such that there were no significant power outages arising from supply shortages. In any event, since 2010 Blanket mine, along with most other gold producers, had a supply agreement with ZESA in terms of which the consumers paid a premium rate in return for uninterrupted power. This agreement expired on December 31, 2018 and was not renewed as ZESA demanded that payment should be in US Dollars – which was neither practical (due to insufficient access to US Dollars) nor permissible in terms of Zimbabwean foreign exchange controls.

In recent months, the generating capacity at the Kariba hydro generating station has been significantly reduced due to low water levels caused by insufficient rain in the catchment area. In addition, South Africa has reduced its deliveries of electricity to Zimbabwe due to non-payment for historic deliveries. The combined effect of these factors is that Zimbabwe now experiences a severe electricity shortage and has resorted to “load-shedding” whereby electricity consumers experience prolonged power outages. Initially the load-shedding targeted domestic consumers however, from early July 2019, Blanket and other industrial users have experienced substantial interruptions to their electricity supply. In the case of Blanket which has a maximum demand of 18MW, it is regularly required to reduce its consumption by up to 8 MW for periods of up to 16 hours each day. As a result of load-shedding, Blanket’s use of diesel for generating electricity increased from approximately 30,000 litres per month in 2018 to 265,000 litres in July 2019.

Blanket and Caledonia management have had constructive engagement with the relevant authorities both directly and via the Chamber of Mines to find an urgent resolution to this matter. All parties understand that without sufficient power, Zimbabwe’s gold production and hence its ability to earn foreign exchange, will be very severely affected if the gold industry does not receive sufficient power to maintain production.

Although it is hoped that power production from Kariba will increase when water levels return to normal, it is likely that Zimbabwe will continue to experience severe electricity shortages. The situation may be exacerbated by the increasing difficulties experienced by the South African state-owned electricity generator, which has been a substantial supplier to Zimbabwe.

An additional difficulty, which Blanket has experienced for many months, is that the electricity supply from the grid is highly unstable and is subject to frequent surges and dips in voltage. Power surges, if not controlled, cause severe damage to Blanket’s electrical equipment. Blanket has therefore installed its own equipment to regulate the incoming power however this equipment was itself damaged by the incoming supply.

Caledonia’s approach to the electricity situation is threefold:

- i. To continue to engage constructively with ZESA with the objective of securing cheap, reliable and stable power from the grid. This includes agreeing a realistic electricity pricing formula in the context of the current monetary conditions; assisting ZESA to repair and maintain its own equipment and may include participating in an industry-wide scheme to import power. On August 9, 2019 Blanket signed a new power supply agreement in terms of which Blanket will receive uninterrupted power in return for an FCA-denominated tariff which will be cheaper than the tariff which prevailed until December 31, 2018.
- ii. To increase Blanket’s stand-by diesel generating capacity. Blanket already has 12.5MW of installed diesel generators which is sufficient to maintain production but is not enough to allow work to continue on the Central Shaft at the same time as maintaining production. Blanket has placed orders for a further 6MW of diesel generators which should be commissioned in August 2019. However, diesel generators are not, by themselves, a long-term solution to the electricity problem: diesel power is expensive and requires the import of large quantities of diesel which is not always easily available and may require payment in FCA;
- iii. To explore the installation of a solar power plant to supply some or all of Blanket’s requirements. Management is currently completing financial and technical evaluations of a solar project and has started the process of obtaining the necessary permits and licences so that it can move quickly if the evaluations indicate that a solar project will be cost effective.

Water supply

Blanket uses water in the metallurgical process, some of which is pumped from the deeper levels of the mine but most of which is obtained from the “Blanket dam” (which, despite its name, is neither owned nor managed by Blanket Mine) which also supplies water to the nearby town of Gwanda. Blanket is situated in a semi-arid region and rainfall typically only occurs in the period November to February. The last rainy season was very poor and water levels in the dam are significantly lower than usual. The water authority has released water from an upstream dam to replenish the Blanket dam and management believes that with careful management, there is enough water in the Blanket dam to maintain normal operations until the start of the next rainy season. However, it is important that the forthcoming rainy season is successful. Blanket

has some boreholes which it could use to augment other water supplies; however, the boreholes would not produce enough to meet all of Blanket's water requirements.

Taxation

The main elements of the Zimbabwe tax regime insofar as it affects Blanket Mine and Caledonia are as follows:

- A royalty is levied on gold revenues at a rate of 5%. Historically, the royalty has not been an allowable expense for the purposes of calculating taxable profits. In the Mid-Year Budget Review, published on August 1, 2019 it was announced that the royalty would be allowable as a deductible expense. It was also announced that from September 1, 2019 the royalty rate would be calculated on a sliding scale based on gold prices: a royalty rate at 3% will apply if the gold price is below \$1,200 and a royalty of 5% will apply if the gold price is over \$1,200 per ounce. The overall effect of this proposal will be to reduce the royalty and tax burden on Blanket: illustratively, the effect of these changes for each 10,000 ounces per annum of gold production at an assumed gold price of \$1,450 per ounce would be a post-tax benefit of approximately \$360,000.
- Income tax is levied at 25.75% on profits as adjusted for tax purposes. The main adjustments to profit for the purposes of calculating tax are the add-back of depreciation, most of the management fees paid by Blanket to Caledonia's subsidiary in South Africa and the royalty on gold sales. 100% of all capital expenditure incurred in the year of assessment is allowed as a deductible expense. As noted above, on August 1, 2019, the Zimbabwe government proposed that the royalty would henceforth be deductible for income tax purposes.
- Withholding tax is levied on certain remittances from Zimbabwe i.e. dividend payments from Zimbabwe to the UK and payments of management fees from Blanket to Caledonia in South Africa.

4.10 Opportunities and Outlook

Central Shaft Project to Increase Production and Extend Mine Life

As discussed in section 4.7 the Company has sunk a new shaft to a depth of 1,204 metres and has now commenced the equipping phase. Once commissioned, the shaft should allow production to increase to the targeted rate of approximately 80,000 ounces per annum from 2022 onwards. Subject to the continued availability of foreign currency (as discussed in section 4.9), Caledonia intends to continue to implement the Central Shaft project.

Production Guidance

Due to the increased incidence of power outages and the continued difficulties with grade, production guidance for 2019 is revised downwards from between 53,000 and 56,000 ounces of gold to a range of 50,000 to 53,000 ounces of gold. This is forward looking information as defined by National Instrument 51-102. Refer to section 18 of this MD&A for further information on forward looking statements.

Cost Guidance

On-mine cost guidance for 2019 is in the range of \$735 to \$817 per ounce; guidance for AISC is \$933 to \$1,022 per ounce.

On-mine cost and AISC per ounce for the 6 months to June 30, 2019 are below guidance due to stringent cost controls, the effect of the devaluation of the RTGS Dollar, sterling and the South African rand against the US Dollar, the reversal of a production bonus accrual because production was below target and the effect of the change in estimated costs of electricity in the period after the introduction of the interbank rate. Management re-iterates cost guidance for 2019.

This is forward looking information as defined by National Instrument 51-102. Refer to section 18 of this MD&A for further information on forward looking statements.

Earnings Guidance

Guidance for adjusted earnings per share for 2019 was 86 to 117 cents assuming a gold price of \$1,300 per ounce and assuming previous production guidance of 53,000 to 56,000 ounces of gold and the cost targets set out above are achieved. Notwithstanding the reduced production guidance for 2019, due to the higher gold price and lower costs, there is no change to earnings guidance for 2019. Adjusted earnings per share for the first six months of 2019 were 53.5 cents, which on an annualised basis, is within earnings guidance for 2019.

This is forward looking information as defined by National Instrument 51-102. Refer to section 18 of this MD&A for further information on forward looking statements.

The Company's ability to achieve the production, cost and earnings guidance set out above will be influenced by many factors which are discussed in section 17 of this MD&A.

Changes in Indigenisation Legislation

As discussed in section 4.8 of this MD&A, following changes in legislation, Caledonia has entered into a sale agreement to acquire a further 15% of Blanket and it will evaluate the potential to buy back the shareholding of NIEEF and restructure the shareholding of Blanket's employees. Any transactions would reflect the value of the indigenous shareholder's shareholdings in Blanket after deducting the value of the outstanding facilitation loans. There is no certainty that agreement will be reached on any transaction with NIEEF or Blanket's employees nor that the conditions to the sale agreement with Fremiro will be fulfilled.

Strategy

Caledonia's strategic focus is on implementing the Central Shaft project at Blanket on schedule and within budget. Subject to the continued availability of foreign currency, Caledonia's board and management believe the successful implementation of the Central Shaft project remains in the best interests of all stakeholders because it is expected to result in increased production, reduced operating costs and greater flexibility to undertake further exploration and development, thereby safeguarding and enhancing Blanket's long-term future. Caledonia will also evaluate further investment opportunities in Zimbabwe that would not fall underneath Blanket's ownership.

5 EXPLORATION AND PROJECT DEVELOPMENT

Caledonia's exploration activities are focussed on the growth and development of Blanket Mine and its satellite properties.

5.1 Blanket Exploration

3,596 metres were drilled in the Quarter compared to 3,983 metres in the previous quarter. Drilling has been focussed on two areas: AR South, and Blanket Section. The drilling program has had a good degree of success with indications that mineralisation extends beyond the deepest hole yet drilled (approximately 1,150 metres below surface).

5.2 Blanket Satellite Prospects

Blanket Mine has exploration title holdings in the form of registered mining claims in the Gwanda Greenstone Belt totalling 237 claims covering properties with a total area of about 2,500 hectares. Included within these claim areas are 18 previously operated small gold workings which warrant further exploration.

Blanket's exploration on the satellite properties has been focused on the GG and the Mascot exploration prospects which, based on past production records, are believed to have the greatest potential. Due to the continued high level of capital investment on the Central Shaft and Blanket's limited funding capacity, exploration work at GG and Mascot was suspended in 2016 and resources were re-deployed at Blanket.

6. INVESTING

An analysis of investment in the Quarter, the preceding quarter and the years 2017 and 2018 is set out below.

(\$'000's)	2017	2018	2019	2019
	Year	Year	Q1	Q2
Total Investment	20,949	19,915	5,209	4,208
Blanket	20,939	19,900	5,045	4,203
Other	10	15	164	5

Investment at Blanket is in terms of the investment plan that was announced in October 2014 and which is discussed in section 4.7 of this MD&A. Investment that takes place other than at Blanket largely comprises capital items that are purchased by Caledonia in South Africa which will be sold on to Blanket in due course. All further investment at Blanket is expected to be funded from Blanket's internal cash flows and its Zimbabwean borrowing facilities.

7. FINANCING

Caledonia financed all its operations using funds on hand and those generated by its operations. No equity financing took place in the Quarter other than the issue of 13,137 new shares in settlement of certain LTIP awards to a member of staff. The Company currently has no plans to raise equity. Blanket has an unsecured RTGS\$4 million overdraft facility in Zimbabwe which is repayable on demand. As at June 30, 2019 the facility was undrawn. In December 2018, Blanket drew down a RTGS\$ 6 million 3-year facility which is repayable by a single bullet payment in December 2021.

8. LIQUIDITY AND CAPITAL RESOURCES

An analysis of Caledonia's capital resources as at June 30, 2019 and at the end of each of the preceding 5 quarters is set out below.

Liquidity and Capital Resources							
(\$'000's)							
	As at	Mar 31	June 30	Sept 30	Dec 31	Mar 31	June 30
		2018	2018	2018	2018	2019	2019
Overdraft		1,604	2,749	3,931	-	-	-
Term facility		1,117	746	374	5,960	1,987	912
Cash and cash equivalents in the statement of cashflows (net of overdraft)		13,380	5,308	5,896	11,187	9,742	7,875
Working capital		12,593	11,119	10,151	15,970	14,498	16,447

Movements in Caledonia's net cash, the overdraft and working capital and an analysis of the sources and uses of Caledonia's cash are discussed in section 3 of this MD&A. The overdraft facility is held by Blanket with a Zimbabwean bank and is unsecured and repayable on demand. The term facility is held by Blanket with a Zimbabwean bank, is secured and has a three-year term at draw-down in December 2018 with a single bullet repayment in December 2021. The term facility is repayable in RTGS\$ and accordingly has been revalued from approximately \$6 million to approximately \$912 following the introduction of inter-bank trading between RTGS\$ and foreign currencies and the subsequent devaluation of the RTGS\$ as discussed in section 4.9 of this MD&A. The Company's liquid assets as at June 30, 2019 exceed its planned and foreseeable commitments as set out in section 9 of this MD&A.

9. OFF-BALANCE SHEET ARRANGEMENTS, CONTRACTUAL COMMITMENTS AND CONTINGENCIES

There are no off-balance sheet arrangements apart from the facilitation loans of \$30.98 million which are not reflected as loans receivable for IFRS purposes (refer to note 5 of the Unaudited Condensed Consolidated Interim Financial Statements). The Company had the following contractual obligations at June 30, 2019:

Payments due by Period					
<i>(\$'000's)</i>					
	Within 1			After 5	
Falling due	year	1-3 Years	4-5 Years	Years	Total
Trade and other payables	7,601	-	-	-	7,601
Term loan	-	912	-	-	912
Provisions	244	137	670	2,268	3,319
Capital expenditure commitments	5,754	-	-	-	5,754

The capital expenditure commitments relate primarily to the new oxygen plant and materials and equipment which have been ordered by Caledonia in South Africa to equip the Central Shaft once the shaft sinking phase has been completed. In addition to the committed purchase obligations set out above, Blanket currently intends to invest approximately \$4 million between June 2019 and December 2019 which is not yet committed and a further \$26 million in the years 2020 and 2021, which is also uncommitted. The committed and uncommitted investment will be used to maintain Blanket's existing operations and implement the Central Shaft which is discussed in section 4.7 of this MD&A. Committed and uncommitted purchase obligations are expected to be met from the cash generated from Blanket's existing operations and Blanket's existing borrowing facility. Caledonia has no obligations in respect of capital or operating leases. As of June 30, 2019, Caledonia had potential liabilities for rehabilitation work on Blanket – if and when it is permanently closed – at an estimated discounted cost of \$3.9 million.

10. NON-IFRS MEASURES

Throughout this document, we have provided measures prepared in accordance with IFRS in addition to some non-IFRS performance measures for investors who use them to evaluate our performance. Since there is no standard method for calculating non-IFRS measures, they are not a reliable way to compare Caledonia against other companies. Non-IFRS measures should be used along with other performance measures prepared in accordance with IFRS. We have defined below the non-IFRS measures we have used in this document and provide a reconciliation of such non-IFRS measures to the IFRS measures we report.

10.1 Cost per ounce

Non-IFRS performance measures such as “on-mine cost per ounce”, “all-in sustaining cost per ounce” and “all-in cost per ounce” are used in this document. Management believes these measures assist investors and other stakeholders in understanding the economics of gold mining over the life-cycle of a mine. These measures are calculated on the basis set out by the World Gold Council in a Guidance Note published on June 23, 2013 and accordingly differ from the previous basis of calculation. The table below reconciles “on-mine cost per ounce”, “all-in sustaining cost per ounce” and “all-in cost per ounce” to the production costs shown in the financial statements which have been prepared under IFRS.

Reconciliation of IFRS Production Cost to Non-IFRS Costs per ounce				
<i>(\$'000's unless otherwise indicated)</i>				
	3 Months to June 30		6 Months to June 30	
	2018	2019	2018	2019
Production cost (IFRS)	9,297	7,571	19,307	17,340
Cash-settled share-based expense	-	(2)	-	(70)
Less exploration and site restoration costs	(290)	(179)	(559)	(399)
Other cost and intercompany adjustments	69	(597)	(218)	(245)
On-mine production cost	9,076	6,793	18,530	16,626
Gold sales (oz)	12,657	12,712	26,412	25,102
<i>On-mine costs per ounce (\$/oz)</i>	717	534	702	662
Royalty	811	864	1,715	1,683
Export incentive	(1,621)	(741)	(2,985)	(1,930)
Exploration, remediation and permitting cost	80	(94)	151	211
Sustaining capital expenditure	615	209	1,353	308
Administrative expenses	1,660	1,309	3,202	2,705
Silver by-product credit	(15)	(14)	(31)	(27)
Share-based payment expense	223	11	337	440
All in sustaining cost	10,829	8,337	22,272	20,016
Gold sales (oz)	12,658	12,712	26,412	25,102
<i>All-in sustaining costs per ounce (\$/oz)</i>	856	656	843	797
Permitting and exploration expenses	21	66	60	69
Non-sustaining capital expenditure	5,021	3,999	9,469	9,109
Total all in cost	15,871	12,402	31,801	29,194
Gold sales (oz)	12,658	12,712	26,412	25,102
<i>All-in costs per ounce (\$/oz)</i>	1,254	976	1,204	1,163

10.2 Average realised gold price per ounce

“Average realised gold price per ounce” is a non-IFRS measure which, in conjunction with the cost per ounce measures described above, allows stakeholders to assess our performance. The table below reconciles “Average realised gold price per ounce” to the Revenue shown in the financial statements which have been prepared under IFRS. The average realised gold price is after deduction of an “early settlement discount” by Fidelity of 1.25% of the gross sale proceeds.

Reconciliation of Average Realised Gold Price per Ounce				
<i>(\$'000's unless otherwise indicated)</i>				
	3 Months to June 30		6 Months to June 30	
	2018	2019	2018	2019
Revenue (IFRS)	16,198	16,520	34,257	32,440
Revenues from sales of silver	(15)	(14)	(31)	(27)
Revenues from sales of gold	16,183	16,506	34,226	32,413
Gold ounces sold (oz)	12,658	12,712	26,412	25,102
Average realised gold price per ounce (US\$/oz)	1,278	1,298	1,296	1,291

10.3 Adjusted earnings per share

“Adjusted earnings per share” is a non-IFRS measure which management believes assists investors in understanding the Company’s underlying performance. The table below reconciles “adjusted earnings per share” to the Profit/Loss attributable to owners of the Company shown in the financial statements which have been prepared under IFRS.

Reconciliation of Adjusted Earnings per Share (“Adjusted EPS”) to IFRS Profit Attributable to Owners of the Company				
<i>(\$’000’s unless otherwise indicated)</i>				
	3 Months to 30 June		6 Months to 30 June	
	<i>*2018</i>	2019	<i>*2018</i>	2019
Profit for the period (IFRS)	3,254	27,946	7,133	38,665
Non-controlling interest share of profit for the period	(605)	(4,643)	(1,375)	(6,044)
Profit attributable to owners of the Company	2,604	23,303	5,758	32,621
Add back/(deduct) amounts in respect of:				
Blanket Mine Employee Trust adjustment	(35)	(35)	(75)	(35)
Equity-settled share-based payments	-	-	14	-
Unrealised foreign exchange	(89)	(22,167)	(125)	(25,447)
Deferred tax	1,249	(2,185)	2,439	(1,358)
Profit on sale of subsidiary	-	-	-	(4,409)
	1,125	(24,387)	2,253	(31,249)
Non-controlling interest share of add backs and deductions in respect of:				
Blanket Mine Employee Trust adjustment	<i>*6</i>	6	<i>*12</i>	6
Unrealised foreign exchange	<i>*12</i>	3,584	<i>*12</i>	4,113
Deferred tax	<i>*(213)</i>	349	<i>*(406)</i>	220
Net add back and deductions	(195)	3,939	(382)	4,339
Adjusted profit	<i>*3,534</i>	2,855	<i>*7,629</i>	5,711
Weighted average shares in issue (m)*	10.6	10,6	10.6	10,6
Adjusted EPS (cents)	<i>*33.3</i>	26.8	<i>*72.0</i>	53.5

**Restated period and numbers*

In the Quarter management restated the comparative Adjusted EPS to present the Add back/deduct amounts in the table above with the deduction of the Non-controlling interest share to present adjusted earnings per share for the Company excluding any effects of Non-controlling interest.

11. RELATED PARTY TRANSACTIONS

There were no related party transactions in the Quarter.

12. CRITICAL ACCOUNTING ESTIMATES

Caledonia’s accounting policies are set out in the Audited Consolidated Financial Statements which have been publicly filed on SEDAR at www.sedar.com. In preparing the Unaudited Condensed Consolidated Interim Financial Statements, management is required to make estimates and assumptions that affect the amounts represented in the Unaudited Condensed Consolidated Interim Financial Statements and related disclosures. Use of available information and the application of judgement are inherent in the formation of estimates. Estimates and underlying assumptions are reviewed on an on-going basis. Revisions to accounting estimates are recognised in the period in which the estimates are revised and in any future periods affected. Discussion of recently issued accounting pronouncements is set out in note 4 of the Audited Consolidated Financial Statements.

Information about critical judgements in applying accounting policies that have the most significant effect on the amounts recognised in the Unaudited Condensed Consolidated Interim Financial Statements is included in the following notes:

i) Indigenisation transaction

The directors of Caledonia Holdings Zimbabwe (Private) Limited (“CHZ”), a wholly owned subsidiary of the Company, performed an assessment, using the requirements of IFRS 10: *Unaudited Condensed Consolidated Interim Financial Statements* (IFRS 10), and concluded that CHZ should continue to consolidate Blanket and accounted for the transaction as follows:

- Non-controlling interests (“NCI”) are recognised on the portion of shareholding upon which dividends declared by Blanket accrue unconditionally to equity holders as follows:
 - (a) 20% of the 16% shareholding of NIEEF;
 - (b) 20% of the 15% shareholding of Fremiro; and
 - (c) 100% of the 10% shareholding of GCSOT.
- This effectively means that NCI is recognised at Blanket at 16.2% of its net assets.
- The remaining 80% of the shareholding of NIEEF and Fremiro is recognised as non-controlling interests to the extent that their attributable share of the net asset value of Blanket exceeds the balance on the facilitation loans including interest. At June 30, 2019 the attributable net asset value did not exceed the balance on the respective loan accounts and thus no additional NCI was recognised.

The transaction with Blanket Employee Trust Services (Private) Limited (“BETS”) is accounted for in accordance with IAS 19 *Employee Benefits* (profit sharing arrangement) as the ownership of the shares does not ultimately pass to the employees. The employees are entitled to participate in 20% of the dividends accruing to the 10% shareholding in Blanket if they are employed at the date of such distribution. To the extent that 80% of the attributable dividends exceed the balance on BETS’ facilitation loan they will accrue to the employees at the date of such declaration.

The Employee Trust and BETS are structured entities which are effectively controlled and consolidated by Blanket. Accordingly, the shares held by BETS are effectively treated as treasury shares in Blanket and no NCI is recognised.

ii) Site restoration provisions

The site restoration provision has been calculated for the Blanket Mine based on an independent analysis of the rehabilitation costs as performed in 2015. Estimates and assumptions are made when determining the inflationary effect on current restoration costs and the discount rate to be applied in arriving at the present value of the provision. Assumptions, based on the current economic environment, have been made which management believes are a reasonable basis upon which to estimate the future liability. These estimates take into account any material changes to the assumptions that occur when reviewed by management. Estimates are reviewed annually and are based on current regulatory requirements. Significant changes in estimates of contamination, restoration standards and techniques will result in changes to provisions from period to period. Actual rehabilitation costs will ultimately depend on future market prices for the rehabilitation costs which will reflect the market condition at the time the rehabilitation costs are incurred. The final cost of the currently recognized site rehabilitation provisions may be higher or lower than currently provided for.

iii) Exploration and evaluation (“E&E”) expenditure

The Group makes estimates and assumptions regarding the possible impairment of E&E properties by evaluating whether it is likely that future economic benefits will flow to the Group, which may be based on assumptions about future events or circumstances. Estimates and assumptions made may change if new information becomes available. If information becomes available suggesting that the recovery of expenditures is unlikely, the amount capitalized is written off in profit or loss in the period the new information becomes available. The recoverability of the carrying amounts of exploration and evaluation assets depends upon the availability of sufficient funding to bring the properties into commercial production,

the price of the products to be recovered and the undertaking of profitable mining operations. As a result of these uncertainties, the actual amount recovered may vary significantly from the carrying amount.

iv) Income taxes

Significant estimates and assumptions are required in determining the provision for income taxes. There are many transactions and calculations undertaken during the ordinary course of business for which the ultimate tax determination is uncertain. A major assumption is that the Zimbabwe Revenue Authority (“ZIMRA”) will require a tax computation to be performed using accounts denominated in RTGS\$. This results in a substantially different tax liability than if the computation is performed using accounts denominated in US Dollars, which is Blanket’s functional currency for the purposes of IFRS. Caledonia records its best estimate of the tax liability including any related interest and penalties in the current tax provision. In addition, Caledonia applies judgement in recognizing deferred tax assets relating to tax losses carried forward to the extent that there are sufficient taxable temporary differences (deferred tax liabilities) relating to the same taxation authority and the same taxable entity against which the unused tax losses can be utilized or sufficient estimated taxable income against which the losses can be utilized.

v) Share-based payment transactions

The fair value of the amount payable to employees (including any taxation thereon) in respect of share-based awards, which may be settled in cash, is recognised as an expense with a corresponding increase in liabilities, over the period over which the employee becomes unconditionally entitled to payment. The liability is re-measured at each reporting date. Any changes in the fair value of the liability are recognised as a personnel expense in profit or loss. Additional information about significant judgements and estimates and the assumptions used to estimate fair value for cash-settled share-based payment transactions are disclosed in note 10 to the Unaudited Condensed Consolidated Interim Financial Statements.

vi) Impairment

At each reporting date, Caledonia determines if impairment indicators exist and, if present, performs an impairment review of the non-financial assets held in Caledonia. The exercise is subject to various judgemental decisions and estimates. Financial assets are also reviewed regularly for impairment.

vii) Depreciation

Depreciation on mine development, infrastructure and other assets in the production phase is computed on the units-of-production method over the life-of-mine based on the estimated quantities of reserves (proven and probable) and resources (measured, indicated and inferred), which are planned to be extracted in the future from known mineral deposits. Where items have a shorter useful life than the life-of-mine, the mine development, infrastructure and other assets are depreciated over their useful life. Confidence in the existence, commercial viability and economical recovery of reserves and resources included in the life-of-mine may be based on historical experience and available geological information. This is in addition to the drilling results obtained by the Group and management’s knowledge of the geological setting of the surrounding areas, which would enable simulations and extrapolations to be done with a sufficient degree of accuracy. In instances where management is able to demonstrate the economic recovery of resources with a high level of confidence, such additional resources are included in the calculation of depreciation.

viii) Mineral reserves and resources

Mineral reserves and resources are estimates of the amount of product that can be economically and legally extracted. In order to calculate the reserves and resources, estimates and assumptions are required about a range of geological, technical and economic factors, including but not limited to quantities, grades, production techniques, recovery rates, production costs, transport costs, commodity prices and exchange rates. Estimating the quantity and grade of mineral reserves and resources requires the size, shape and depth of orebodies to be determined by analysing geological data such as the logging and assaying of drill samples. This process may require complex and difficult geological assumptions and calculations to interpret the data.

Estimates of mineral reserves and resources may change due to the change in economic assumptions used to estimate mineral reserves and resources and due to additional geological data becoming available in the course of operations.

The Group estimates its reserves (proven and probable) and resources (measured, indicated and inferred) based on information compiled by a qualified person in terms of the Canadian National Instrument 43-101 – Standards of Disclosure for Mineral Projects (“NI 43-101”) relating to geological and technical data of the size, depth, shape and grade of the ore body and suitable production techniques and recovery rates. Such an analysis requires geological and engineering assumptions to interpret the data. These assumptions include:

- correlation between drill-holes intersections where multiple reefs are intersected;
- continuity of mineralisation between drill-hole intersections within recognised reefs; and
- appropriateness of the planned mining methods.

The Group estimates and reports reserves and resources in accordance with NI 43-101 and the Canadian Institute of Mining, Metallurgy and Petroleum (the “CIM”) - *CIM Definition Standards for Mineral Resources and Mineral Reserves*. Complying with the CIM code, NI 43-101 requires the use of reasonable assumptions to calculate the recoverable resources. These assumptions include:

- the gold price based on current market price and the Group’s assessment of future prices;
- estimated future on-mine costs, sustaining and non-sustaining capital expenditures;
- cut-off grade;
- dimensions and extent, determined both from drilling and mine development, of ore bodies; and
- planned future production from measured, indicated and inferred resources.

Changes in reported reserves and resources may affect the Group’s financial results and position in a number of ways, including the following:

- asset carrying values may be affected due to changes in the estimated cash flows;
- depreciation and amortisation charges to profit or loss may change as these are calculated on the unit-of-production method or where useful lives of an asset change; and
- decommissioning, site restoration and environmental provisions may change in ore reserves and resources which may affect expectations about the timing or cost of these activities.

ix) Income and Deferred tax liabilities

Significant assumptions and estimates are required in determining the provision for income taxes. There are many transactions and calculations undertaken during the ordinary course of business for which the ultimate tax determination is uncertain. The Group records its best estimate of the tax liability including the related interest and penalties in the current tax provision. Management believes they have adequately provided for the probable outcome of these matters. In addition, the Group makes assumptions and estimates in recognising deferred tax assets as a monetary item and that the deferred tax liability will realise and that it would realise in RTG\$. The final outcome of the income and deferred tax liabilities may result in a materially different outcome than the amount included in the tax liabilities in the Statements of financial position

13. FINANCIAL INSTRUMENTS

i) Commodity risk

Subject to the recent introduction of the gold support price mechanism which is discussed in section 4.9 of this MD&A, Caledonia is exposed to fluctuations in the price of gold because Blanket produces and sells gold doré and receives the prevailing spot price for the gold contained therein. In January 2019 Caledonia entered into gold price hedging contracts for the 5 months from February 2019 until June 2019 for 4,500 ounces of production per month through the purchase of put options with a strike price of \$1,250 per ounce. The hedge ensured that Caledonia received a minimum price of \$1,250 per ounce of gold for the duration of the contracts whilst maintaining full upside participation. Caledonia currently has no gold price hedging arrangements in place. Caledonia will re-assess the requirement for any hedging in the context of, inter alia, the prevailing gold price, Blanket’s production rate and cash generation capacity and Blanket’s capital expenditure programme.

ii) Credit risk

The carrying amount of financial assets as disclosed in the statements of financial position and related notes represents the maximum credit exposure. The trade receivable relates to gold bullion sold before the end of the Quarter and VAT receivables. The amount due in respect of bullion sales was settled in July 2019; the VAT receivable is within the agreed terms of such refunds. The deferred consideration is in respect of the sale of Eersteling Gold Mine and is secured against the shares sold.

iii) Impairment losses

None of the trade and other receivables is past due at the period-end date.

iv) Liquidity risk

All trade payables and the bank overdraft have maturity dates that are expected to mature in under 6 months. A three-year facility was drawn down in December 2018 and is repayable in a single payment in December 2021.

v) Currency risk

A proportion of Caledonia's assets, financial instruments and transactions are denominated in currencies other than the US Dollar. The financial results and financial position of Caledonia are reported in US Dollars in the Unaudited Condensed Consolidated Interim Financial Statements.

The fluctuation of the US Dollar in relation to other currencies will consequently have an impact upon the profitability of Caledonia and may also affect the value of Caledonia's assets and liabilities and the amount of shareholders' equity.

Caledonia does not use any derivative instruments to reduce its foreign currency risks. To reduce exposure to currency transaction risk, where possible Caledonia maintains cash and cash equivalents in the currencies used by Caledonia to meet short-term liquidity requirements.

As discussed in section 4.9 of this MD&A, the RTGS\$ is subject to variations in the exchange rate against the US Dollar. This may result in Blanket's assets, liabilities and transactions that are denominated in RTGS Dollars being subject to further fluctuations in the exchange rate between RTGS\$ and FCA Dollars.

vi) Interest rate risk

Interest rate risk is the risk borne by an interest-bearing asset or liability as a result of fluctuations in interest rates. Unless otherwise noted, it is the opinion of management that Caledonia is not exposed to significant interest rate risk as it has limited debt financing. Caledonia's cash and cash equivalents include highly liquid investments that earn interest at market rates. Caledonia manages its interest rate risk by endeavouring to maximize the interest income earned on excess funds while maintaining the liquidity necessary to conduct operations on a day-to-day basis. Caledonia's policy focuses on preservation of capital and limits the investing of excess funds to liquid term deposits in high credit quality financial institutions.

14. DIVIDEND POLICY

Caledonia's current dividend policy is a dividend of 6.875 cents payable at the end of January, April, July and October. As discussed in section 4.9, monetary conditions in Zimbabwe have worsened and there is an increased risk that Caledonia will not be able to effect payments from Zimbabwe which are sufficient to fund further dividend payments.

15. MANAGEMENT AND BOARD

There were no changes to management or the board in the period under review.

16. SECURITIES OUTSTANDING

As at August 13, 2019 Caledonia had 10,763,041 common shares issued. 13,137 new shares were issued in the Quarter in settlement of certain LTIP awards to a member of staff. As at August 13, 2019 outstanding options to purchase Common Shares (“Options”) are as follows:

Number of Options	Exercise Price Canadian \$	Expiry Date
5,000	4.00	Oct 8, 2020
18,000	11.50	Oct 13, 2021
5,000	8.10	May 30, 2022
<u>10,000</u>	<u>9.30⁵</u>	<u>Aug 25, 2024</u>
<u>38,000</u>		

The Plan allows that the number of shares reserved for issuance to participants under the Plan, together with shares reserved for issue under any other share compensation arrangements of the Company, shall not exceed the number which represents 10% of the issued and outstanding shares from time to time. Accordingly, Caledonia could grant Options on a further 1,038,304 shares as at August 13, 2019 on the assumption that all the LTIPs are settled in cash, at the option of the LTIP holder.

17. RISK ANALYSIS

The business of Caledonia contains significant risk due to the nature of mining, exploration and development activities. Caledonia’s business contains significant additional risks due to the jurisdictions in which it operates and the nature of mining, exploration and development. Included in the risk factors below are details of how management seeks to mitigate the risks where this is possible.

- **Liquidity risk:** The Company needs to generate cash to be able to continue to invest in properties and projects without raising further third-party financing in addition to the existing debt facilities at Blanket. Caledonia currently has sufficient cash resources and debt facilities and continues to generate sufficient cash to cover all of its anticipated investment needs.
- **Availability of foreign currency:** The Company needs access to foreign currency in Zimbabwe so that it can pay for imported goods and equipment and remit funds to Group companies outside Zimbabwe. As discussed in section 4.9, there has been a deterioration in the availability of foreign currency and changes in the banking environment relating to payments from Zimbabwe. No assurance can be given that sufficient foreign currency will continue to be available.
- **Exploration risk:** The Company needs to identify new resources to replace ore which has been depleted by mining activities and to commence new projects. Blanket has embarked on development and exploration programmes as set out in sections 4.7 and 5. No assurance can be given that exploration will be successful in identifying sufficient mineral resources of an adequate grade and suitable metallurgical characteristics that are suitable for further development or production.
- **Development risk:** The Company is engaged in the implementation of the Central Shaft project as set out in section 4.7 of this MD&A. Construction and development of projects are subject to numerous risks including: obtaining equipment, permits and services; changes in regulations; currency rate changes; labour shortages; fluctuations in metal prices and the loss of community support. There can be no assurance that construction will commence or continue in accordance with the current expectations or at all.
- **Production estimates:** Estimates for future production are based on mining plans and are subject to change. Production estimates are subject to risk and no assurance can be given that future production estimates will be achieved. Actual production may vary from estimated production for a variety of reasons including un-anticipated variations in grades, mined tonnages and geological conditions,

⁵ The exercise price of CAD\$9.30 per share for these options was converted into a USD amount of \$7.35 at the prevailing USD/CAD exchange rate.

accident and equipment breakdown, changes in metal prices and the cost and supply of inputs and changes to government regulations.

- **Mineral rights:** The Company's existing mining claims, licences and permits are in good standing. The Company has to pay fees etc. to maintain its claims and licences.
- **Metal prices:** The Company's operations and exploration and development projects are heavily influenced by the price of gold, which is particularly subject to fluctuation, subject to the mitigating effect of the price stabilisation mechanism, which is discussed in section 4.9 of this MD&A. Caledonia entered into a 5-month hedge over 100% of Blanket's projected gold production for 5 months from February 2019 to limit the effect of adverse gold price movements. Management regularly reviews future cash flow forecasts in the context of the prevailing gold price and likely downside scenarios for future gold prices.
- **Increasing input costs:** Mining companies generally have experienced higher costs of steel, reagents, labour and electricity and from local and national government for levies, fees, royalties and other direct and indirect taxes. Blanket's planned growth should allow the fixed cost component to be absorbed over increased production, thereby helping to alleviate somewhat the effect of any further price increases.
- **Illegal mining:** There has been an increase in illegal mining activities on properties controlled by Blanket. This gives rise to increased security costs and an increased risk of theft and damage to equipment. Blanket has received adequate support and assistance from the Zimbabwean police in investigating such cases.
- **Electricity supply:** Zimbabwe produces and imports less electricity than it requires and has insufficient funds to adequately maintain or upgrade its distribution infrastructure. This has historically resulted in frequent interruptions to the power supply at Blanket Mine. Blanket addressed the issue of interrupted power supply by installing stand-by generators and by entering into an un-interrupted power supply arrangement with the state-owned electricity company in return for paying a premium tariff. The un-interrupted power supply agreement expired on December 31, 2018 and was not renewed and from July 2019, Blanket has experienced interruptions to its power supply. Negotiations continue regarding a replacement power supply agreement; Blanket has also purchased additional standby generators to increase its capacity and it continues to evaluate other sources of electricity. The un-interrupted power supply arrangement and the stand-by generators do not cover the GG and Mascot exploration properties. Production at Blanket has also been adversely affected by the instability of the incoming electricity supply.
- **Water supply:** Blanket uses water in the metallurgical process, most of which is obtained from a nearby dam. Blanket is situated in a semi-arid area and rainfall typically occurs only in the period November to February. The last rainy season was very poor and water levels in the dam are significantly lower than usual. The water authority has released water from an upstream dam to replenish the Blanket dam and management believes that with careful management, there is enough water in the Blanket dam to maintain normal operations until the next rainy season. However, it is important that the forthcoming rainy season is successful. Blanket has some boreholes which it could use to augment other water supplies, but they would not produce enough to meet all of Blanket's water requirements.
- **Succession planning:** The limited availability of mining and other technical skills and experience in Zimbabwe and the difficulty of attracting appropriately skilled employees to Zimbabwe creates a risk that appropriate skills may not be available if, for whatever reason, the current skills base at the Blanket Mine is depleted. The Caledonia management teams have been augmented so that, if required, appropriate support could be provided to Blanket if this was required.
- **Country risk:** The commercial environment in which the Company operates is unpredictable. Potential risks may arise from: unforeseen changes in the legal and regulatory framework which means that laws may change, may not be enforced, or judgements may not be upheld; restrictions on the movement of currency and the availability of foreign currency to make payments from Zimbabwe; risks relating to inflationary pressures as mentioned in section 4.9; risks relating to possible corruption, bribery, civil disorder, expropriation or nationalisation; risks relating to restrictions on access to assets and the risk that the Government of Zimbabwe is unable to pay its liabilities to Blanket. Management believes that

it has minimised such risks by complying fully with all relevant legislation, by obtaining all relevant regulatory permissions and approvals and by regular and proactive engagement with the relevant authorities.

- **Gold marketing arrangements:** In terms of regulations introduced by the Zimbabwean Ministry of Finance in January 2014, all gold produced in Zimbabwe must be sold to Fidelity, a company which is controlled by the Zimbabwean authorities. Accordingly, all of Blanket's production has been sold to Fidelity. Blanket has received all payments due from Fidelity in full and on time. However, the requirement to sell to Fidelity increases Blanket's credit risk because Fidelity failed to pay Blanket in the period of hyper-inflation which existed prior to the adoption of the multi-currency system by Zimbabwe in early 2009.

18. FORWARD LOOKING STATEMENTS

Information and statements contained in this MD&A that are not historical facts are "forward-looking information" within the meaning of applicable securities legislation that involve risks and uncertainties relating, but not limited to, Caledonia's current expectations, intentions, plans, and beliefs. Forward-looking information can often be identified by forward-looking words such as "anticipate", "believe", "expect", "goal", "plan", "target", "intend", "estimate", "could", "should", "may" and "will" or the negative of these terms or similar words suggesting future outcomes, or other expectations, beliefs, plans, objectives, assumptions, intentions or statements about future events or performance. Examples of forward-looking information in this MD&A include: implementation schedules for, and other uncertainties inherent in, the Central Shaft project; production guidance; estimates of future/targeted production rates; planned mill capacity increases; estimates of future metallurgical recovery rates and the ability to maintain high metallurgical recovery rates; timing of commencement of operations; plans and timing regarding further exploration, drilling and development; the prospective nature of exploration and development targets; the ability to upgrade and convert mineral resources to mineral reserves; capital and operating costs; our intentions with respect to financial position and third party financing; and future dividend payments. This forward-looking information is based, in part, on assumptions and factors that may change or prove to be incorrect, thus causing actual results, performance or achievements to be materially different from those expressed or implied by forward-looking information. Such factors and assumptions include, but are not limited to: failure to establish estimated resources and reserves, the grade and recovery of ore which is mined varying from estimates, success of future exploration and drilling programs, reliability of drilling, sampling and assay data, assumptions regarding the representativeness of mineralization being inaccurate, success of planned metallurgical test-work, capital and operating costs varying significantly from estimates, delays in obtaining or failures to obtain required governmental, environmental or other project approvals, changes in government regulations, legislation and rates of taxation, inflation, changes in exchange rates, fluctuations in commodity prices, delays in the development of projects and other factors.

Security holders, potential security holders and prospective investors should be aware that these statements are subject to known and unknown risks, uncertainties and other factors that could cause actual results to differ materially from those suggested by the forward-looking statements. Such factors include, but are not limited to: risks relating to estimates of mineral reserves and mineral resources proving to be inaccurate, fluctuations in gold price and payment terms for gold sold to Fidelity, risks and hazards associated with the business of mineral exploration, development and mining (including environmental hazards, industrial accidents, unusual or unexpected geological or structural formations, pressures, power outages, fire, explosions, landslides, cave-ins and flooding), risks relating to the credit worthiness or financial condition of suppliers, refiners and other parties with whom the Company does business, inadequate insurance, or inability to obtain insurance, to cover these risks and hazards, employee relations, relationships with and claims by local communities and indigenous populations, political risk, availability and increasing costs associated with mining inputs and labour, the speculative nature of mineral exploration and development, including the risks of obtaining or maintaining necessary licenses and permits, diminishing quantities or grades of mineral reserves as mining occurs, global financial condition, the actual results of current exploration activities, changes to conclusions of economic evaluations, and changes in project parameters to deal with un-anticipated economic or other factors, risks of increased capital and operating costs, environmental, safety or regulatory risks, expropriation, the Company's title to properties including ownership thereof, increased

competition in the mining industry for properties, equipment, qualified personnel and their costs, risks relating to the uncertainty of timing of events including targeted production rate increase and currency fluctuations. Security holders, potential security holders and prospective investors are cautioned not to place undue reliance on forward-looking information. By its nature, forward-looking information involves numerous assumptions, inherent risks and uncertainties, both general and specific, that contribute to the possibility that the predictions, forecasts, projections and various future events will not occur. Caledonia reviews forward-looking information for the purposes of preparing each MD&A; however, Caledonia undertakes no obligation to update publicly or otherwise revise any forward-looking information whether as a result of new information, future events or other such factors which affect this information, except as required by law.

19. CONTROLS

The Company has established and maintains disclosure controls and procedures (“DC&P”) designed to provide reasonable assurance that material information relating to the Company is made known to the Chief Executive Officer and the Chief Financial Officer by others, particularly during the period in which annual filings are being prepared, and that information required to be disclosed in the Company’s annual filings, interim filings or other reports filed or submitted by it under securities legislation is recorded, processed, summarized and reported within the time periods specified by such securities legislation.

The Company’s management, along with the participation of the Chief Executive Officer and the Chief Financial Officer, have evaluated the effectiveness of the Company’s DC&P as of June 30, 2019. Based on that evaluation, the Chief Executive Officer and the Chief Financial Officer have concluded that, as at June 30, 2019, the Company’s DC&P were effective.

The Company also maintains a system of internal controls over financial reporting (“ICFR”) designed under the supervision of the Company’s Chief Executive Officer and Chief Financial Officer to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with IFRS; however, due to inherent limitations, ICFR may not prevent or detect all misstatements and fraud. The board of directors approves the financial statements and ensures that management discharges its financial responsibilities. The Audit Committee, which is composed of independent directors, meets periodically with management and auditors to review financial reporting and control matters and reviews the financial statements and recommends them for approval to the board of directors.

The Company’s management, including the Chief Executive Officer and the Chief Financial Officer, is responsible for establishing and maintaining adequate ICFR and evaluating the effectiveness of the Company’s ICFR as at each fiscal year end. Management has used the 2013 Internal Control–Integrated Framework from the Committee of Sponsoring Organizations of the Treadway Commission (the “COSO”) to evaluate the effectiveness of the Company’s ICFR as at June 30, 2019. Based on this evaluation, the Chief Executive Officer and the Chief Financial Officer have concluded that as at June 30, 2019, the Company’s ICFR was effective.

There have been no changes in the Company’s ICFR during the period ended June 30, 2019 that have materially affected, or are reasonably likely to materially affect, the Company’s ICFR.

20. QUALIFIED PERSON

Paul Matthews (BSc (Hons) Geology), Group Mineral Resource Manager, is the Company’s qualified person as defined by Canada’s National Instrument 43-101. Mr. Matthews is responsible for the technical information provided in this MD&A except where otherwise stated. Mr. Matthews has reviewed the scientific and technical information included in this document and has approved the disclosure of this information for the purposes of this MD&A. Refer to the technical report dated 13 February 2018 entitled “National Instrument 43-101 Technical Report on the Blanket Mine, Gwanda Area, Zimbabwe (Updated February 2018)”, a copy of which was filed by the Company on SEDAR on March 2, 2018, for further technical information on Blanket Mine, the preparation of which Mr Matthews supervised.