# CHINA EDUCATION RESOURCES INC.

**Management's Discussion and Analysis**
**For the year ended December 31, 2013**

**FORM 51-102F1**

This Management Discussion and Analysis ("MD&A") reviews the activities of China Education Resources Inc. ("CER"), its Chinese operating subsidiaries, Today's Teachers Technology & Culture Ltd. ("TTTC"), CEN Smart ("CEN") and Zhong Yu Cheng Yuan Education Technology Ltd. (previously known as Zhong Yu Cheng Yuan Curriculum Development Center Ltd.) ("ZYCY"**)** (and/or collectively the "Group") and compares the financial results for the year ended December 31, 2013 with the same period of 2012. The MD&A should be read in conjunction with the audited consolidated financial statements and accompanying notes for the year ended December 31, 2013, copy of which is filed on the SEDAR website.

All financial information in this MD&A is prepared in accordance with International Financial Reporting Standards ("IFRSs"), except those exceptions specially mentioned. All dollar amounts presented are expressed in United States dollars unless otherwise noted.

**FORWARD LOOKING INFORMATION**

Except for statements of historical fact, the discussion and analysis of financial performance and position including, without limitation, statements regarding projections, future plans, and objectives of CER are forward-looking statements that are subject to various risks and uncertainties. Forward-looking statements are based on management experience, historical results, current expectations and analyses, trends, government policies, and current business and economic conditions, including CER's analysis of its product and distribution system and its expectations regarding the effects of anticipated product and distribution changes and the potential benefits of such efforts and activities on CER's results of operations in future periods. There can be no assurance that such statements will prove to be accurate; actual results and future events could differ materially from those anticipated in such statements.

**DATE OF REPORT – April 30, 2014**

**DESCRIPTION AND OVERVIEW OF BUSINESS**

CER is a corporation organized under the predecessor to the *Business Corporations Act* of British Columbia. CER is public company traded on the TSX Venture Exchange with the trading symbol "CHN" and OTCQX with the trading symbol "CHNUF". The Group, through its subsidiaries in China, is a leading provider of kindergarten to grade 12 ("K-12") education resources and services through its national internet portal, China Education Resources and Services Platform ("CERSP"), www.cersp.com, to China's kindergarten to grade 12 education market.

The Group has worked in all areas of education resources development, marketing and sales. Working with the Curriculum Development Center ("CDC") of China's Ministry of Education ("MOE") and Chinese Society of Education ("CSE") the largest academic association in China, CER has developed a unique national education portal (www.CERSP.com) to help the Central Government implement policy reform. This reform effort is designed to bring China's education system into the twenty first century by changing teaching methods from rote memory learning to a more individualized and creative approach. Teachers completed the national or provincial online training programs on CERSP.com will receive teacher's continuing education credit from either MOE or provincial education authorities. In collaboration with China’s various education authorities and experts, the CERSP portal is designed to support all stakeholders and participants in the K-12 education domain; teachers, students, administrators, subject matter experts, and parents.

The Group’s comprehensive Education Services Portal (“ESP”) is a natural extension of CERSP, and helps to organize the wealth of teaching, learning, and administrative resources available through CERSP at the individual school level.

CERSP is the equivalent of a mega-portal. It is designed to be accessible by everyone associated with K-12 education across China and is loaded with robust features and resources that enable the development, delivery, and support of resources and activities related to the national K-12 education reform initiative. CERSP is a primary venue for teacher training in schools, districts, cities, and provinces. It is also the aggregator for subject matter experts in all K-12 subject areas and a place where they can gather virtually to improve upon the work they have done in response to national mandates.

ESP, on the other hand, is a commercial service for the K-12 education marketplace that extends the reach and relevance of the CERSP portal at the school and individual level. Its primary function is to support the administrative, teaching, learning, testing, and assessment needs of an individual school, and it does so in a way that is standardized, allowing for combined results to the district, city, province, or national level. CERSP can be regarded as a large "back-end" resource that greatly enriches each instance of ESP. ESP can be considered as a way to monetize the momentum of CERSP by creating a direct, revenue producing relationship with every school, administrator, teacher, parent and student that subscribes.

Currently, our ESP provides the following services:

(a) School Platform

The school platform provides a link between a school with its teachers, students and parents. Through the platform, the school can send messages to the teachers, students and parents. The teachers can upload homework and tests to the platform and the students can go to the platform to complete and submit their homework and write the tests. The school can automatically collect the markings received by each student. Each teacher and student has his or her own account number registered with the platform. Currently, the Group is adding mobile learning solutions to the School Platform for both of the students and teachers.

(b) Online tutoring program

Online tutoring program is a platform developed for a teacher to provide online tutoring services through the internet to his or her students. This program still has not started to generate revenue. Students have to prepay for the services to TTTC and TTTC pays the net amount to the teachers after deducting our share of revenue.

(c) Digital education products

Digital education products are the products containing digital textbook tutorial materials, digital supplementary materials such as lesson plans, course modules and tests. CER has had more than 100,000 lesson plans, course modules and continues to develop the materials.

The Group, through TTTC, acquired a 60% interest in Zhong Yu Cheng Yuan Education Technology Ltd. (previously known as Zhong Yu Cheng Yuan Curriculum Development Center Ltd.) ("ZYCY"), a distributor of education products in China for RMB6,000,000 ($878,460) payable in 2,860,000 shares of common stock of the CER at a deemed value of CND0.35 ($0.30) per share. On top of increasing its book selling business, the Group can also strengthen its sales and distribution of its national CERSP and ESP web portal services in China through the sales team of ZYCY.

Due to the size of the Group, the provision of education internal portal services and distribution of educational textbooks and materials were considered in one segment based on the organizational structure, strategies, decision making and the availability of financial information.

**OVERALL PERFORMANCE**

During the three months ended December 31, 2013, the Company generated revenue of $154,273 as compared with $312,801 for the same period of last year. The net loss attributable to the owners of the Company for the period was $3,336,429 as compared to $2,237,622 for the same period of last year. The material increase of net loss for the current period was due to the impairment of goodwill of $2,221,441 (non-cash item).

During the year ended December 31, 2013, the Company generated revenue of $10,085,422 as compared with $7,391,934 for the last year. The net loss attributable to the owners of the Company for the current year was $2,718,360 as compared to $1,295,110 for the last year. The material increase of net loss for the current year was due to the impairment of goodwill of $2,221,441 (non-cash item).

**Selected Annual Information**

| | 2013 | 2012 | 2011 |
|---|---|---|---|
| Total revenue | $ 10,085,422 | $ 7,391,934 | $ 6,553,140 |
| Net gain (loss) | (2,469,961) | (1,503,652) | 83,481 |
| Net loss per share | (0.06) | (0.03) | (0.01) |
| Total assets | 6,709,095 | 7,259,378 | 7,963,826 |
| Long-term liabilities | 7,100 | 31,440 | 252,951 |

The net loss for 2013 was increased significantly due to the increase in goodwill impairment of $2,221,441 (non-cash item).

The net loss for 2012 was increased significantly due to the increase in selling expenses to market our new products and services and a goodwill impairment of $500,000 (non-cash item).

The significant increase of the net loss for 2013 was mainly as a result of the goodwill impairment incurred in the current year. However, revenue increased materially along with the better control on the spending of the general and administration expenses in 2013.

**Results of Operations**

***For the three months ended December 31, 2013:***

For the three months ended December 31, 2013, the Group reported aggregate sales revenue of $154,273 (2012: $312,801). There was a decrease in book sales for the current quarter as compared to the sales of the same quarter of previous year.

The Group recognized a net loss attributable to owners of the Company for the three months ended December 31, 2013 of $3,336,429 as compared to $2,737,622 for the comparable 2012 period. The net loss per share was $0.07 for the three months ended December 31, 2013 as compared to $0.06 for comparable period ended December 31, 2012. The increase was primarily attributed to the goodwill impairment of $2,221,441 (non-cash item).

The following is a discussion of certain expense categories:

*General and administrative expenses*

For the three months ended December 31, 2013, general and administrative expenses were $404,270 compared to $912,322 recorded in 2012. The decrease in general and administrative expenses was a result of the effective control of the operating expenses within the Group:

Salaries, wages, commission and benefits incurred $141,113 for the three months ended December 31, 2013 from $32,872 for the comparable 2012 period.

Bad debt expenses decreased to $114,060 for the three months ended December 31, 2013 from $467,354 for the comparable 2012 period.

Rent expense in the amount of $44,005 for the three months ended December 31, 2013 was comparable with $46,494 for the 2012 period.

*Amortization*

The amortization decreased to $3,667 for the three months ended December 31, 2013 as compared to $12,973 in the same period of 2012.

*Selling expenses*

The selling expenses of $283,019 for the three months ended December 31, 2013 decreased as compared to $1,143,623 in the same period of 2012 which was a result of the effective control of the operating expenses within the Group and the reduction of sales in the current quarter.

*Stock based compensation*

During the three months ended December 31, 2013, the Group recorded a non-cash stock based compensation expense of $14,537 (2012: $29,831) for options previously granted.

*Finance cost*

The Company incurred finance costs of $82,671 for the three months ended December 31, 2013 as compared to $40,754 in the same period of 2012 which was largely due to the higher interest payments on the bank loan and other loan payables as of December 31, 2013.

The Company wrote off the remaining goodwill balance of $2,221,441 (non-cash item) after the impairment test performed under restrictive assumptions allowed under IFRS.

***For the year ended December 31, 2013:***

For the year ended December 31, 2013, the Group reported aggregate sales revenue of $10,085,422 (2012: $7,391,934). There was an increase in book sales for the current year as compared to the sales of the previous year.

The Group recognized a net loss attributable to owners of the Company for the year ended December 31, 2013 of $2,718,360 as compared to $1,295,110 for the previous year. The net loss per share was $0.06 for the year ended December 31, 2013 as compared to the earning per share of $0.03 for comparable year ended December 31, 2012. The decrease was primarily attributed to the impairment of goodwill.

The following is a discussion of certain expense categories:

*General and administrative expenses*

For the year ended December 31, 2013, general and administrative expenses were $1,497,086 compared to $2,095,877 recorded in 2012. The decrease in general and administrative expenses was a result of the effective control of the operating expenses within the Group:

Salaries, wages, commission and benefits decreased to $593,921 for the year ended December 31, 2013 from $661,067 for the comparable year ended December 31, 2012 as some staff were converted to work on a consultancy basis.

Consulting fees were $205,781 for the year ended December 31, 2013 and $169,271 for the previous year.

Rent expense decreased to $146,409 for the year ended December 31, 2013 from $189,017 for the comparable 2012 period. The decrease was due to the moving of the Beijing Office to a place with lower rental charge.

*Amortization*

The amortization decreased to $20,747 for the year ended December 31, 2013 as compared to $42,848 in the previous year as the website development cost and some of the capital assets were fully amortized.

*Selling expenses*

The selling expenses of $3,362,290 for the year ended December 31, 2013 increased as compared to $2,979,577 in the previous year which was a result of increase in promotion expenses incurred.

*Stock based compensation*

During the year ended December 31, 2013, the Group recorded a non-cash stock based compensation expense of $71,010 (2012: $150,067) for options previously granted.

*Finance cost*

The Company incurred finance costs of $237,432 for the year ended December 31, 2013 as compared to $142,891 in the previous year which was largely the higher interest payable and payments on the bank loan and other loan payables as of December 31, 2013.

The Company wrote off the remaining goodwill balance of $2,221,441 (non-cash item) after the impairment test performed under restrictive assumptions allowed under IFRS.

## SUMMARY OF QUARTERLY AND ANNUAL RESULTS

All amounts are expressed in United States dollars. In addition, all amounts are in thousands except for per share amounts.

| | **For the Quarters Ended** | | | |
|---|---|---|---|---|
| | **12/31/2013** ($'000) | **9/30/2013** ($'000) | **6/30/2013** ($'000) | **3/31/2013** ($'000) |
| Revenue | 154 | 3,475 | 4,053 | 2,403 |
| Net income (loss) for the period | (3,336) | 741 | 123 | (246) |
| Net income (loss) per share | (0.07) | 0.02 | 0.00 | (0.01) |
| Total assets | 6,709 | 11,938 | 9,898 | 6,944 |
| Total liabilities | 9,562 | 11,301 | 10,142 | 7,609 |

| | For the Quarters Ended | | | |
|---|---|---|---|---|
| | **12/31/2012** ($'000) | **9/30/2012** ($'000) | **6/30/2012** ($'000) | **3/31/2012** ($'000) |
| Revenue | 820 | 2,716 | 1,825 | 2,571 |
| Net income (loss) for the period | (2,947) | 1,009 | (177) | 611 |
| Net income (loss) per share | (0.06) | 0.02 | (0.00) | 0.01 |
| Total assets | 7,259 | 10,011 | 8,726 | 7,929 |
| Total liabilities | 7,897 | 7,342 | 7,206 | 6,410 |

Due to the seasonal factor, revenue for Q4 usually was less than other quarters. In addition, there were annual adjustments made in Q4 of the year, hence, net loss increased in the same quarter. For the year 2013, the goodwill impairment of $2,221,441 was incurred in Q4.

Net profit increased materially for Q3 of 2013 as selling expenses decreased significantly for the same quarter. Total assets also increased as an increase in accounts receivable.

## FINANCIAL POSITION, LIQUIDITY AND CAPITAL RESOURCES

Working capital deficiency decreased by $77,131 to an amount of $2,945,862 from a working capital deficiency of $3,022,993 at the beginning of the year, primarily as a result of the increase in sales during the current year.

Cash provided by operating activities was $308,280 for the year ended December 31, 2013, compared to $1,987,294 used in operating activities for the year ended December 31, 2012.

At December 31, 2013, accounts and other receivables increased to $5,375,147 from $4,202,448 at December 31, 2012. The increase was mainly due to the increase in sales during the current year.

Cash used in investing activities was $6,676 for the year ended December 31, 2013, compared to cash used in investing activities of $11,380 for the year ended December 31, 2012. The cash outflow for investing activities was related to the acquisition of equipment for the respective periods.

Cash provided by financing activities was $186,575 for the year ended December 31, 2013, compared to cash provided by financing activities of $346,131 for the year ended December 31, 2012.

The Group has increased its types of services provided through its education service portal. The revenue of the Group is expected to increase through providing additional services to the customers. The Group also plans to have equity or debt financing to maintain the Group's capacity, meet planned growth and fund development activities.

**Equipment and website development costs**

At December 31, 2013, the Group's net equipment and website development costs were $100,237 as compared to $111,321 as at December 31, 2012. This decrease was mainly attributed to the amortization and depreciation of $20,753 for the current year. Website development costs and some of the capital assets were fully amortized by the end of 2012.

**Liabilities**

The Group's total liabilities were $9,561,820 as at December 31, 2013, which is comparable with $7,896,685 at December 31, 2012.

**Shareholders' Equity**

There was a shareholders' deficiency of $2,852,725 at December 31, 2013 as compared to $637,307 at December 31, 2012, which included the net loss of $2,718,360 for the year ended December 31, 2013.

**Outstanding share data**

The Group's common shares outstanding as at April 30, 2014 were 47,364,983.

At April 30, 2014, the Group has outstanding stock options of 1,924,000. Details are as follows:

| Exercise Prices (CND) | Number | Expiry Date |
|---|---|---|
| 0.60 | 200,000 | February 3, 2015 |
| 1.00 | 100,000 | February 3, 2015 |
| 1.05 | 624,000 | February 3, 2015 |
| 0.40 | 1,000,000 | March 15, 2017 |
| | 1,924,000 | |

At April 30, 2014, there were no outstanding stock purchase warrants.

**Dividend**

The payment of dividends to shareholders will depend on a number of factors such as earnings, CER's financial requirements and other factors that the Board of Directors considers relevant in the circumstances. The Group currently does not have intention to pay dividends on the common shares. The Board of Directors will review this policy, from time to time, as circumstances change. To date, CER has not declared or paid any dividends on any of its shares.

**OFF-BALANCE SHEET ARRANGEMENTS**

The Group does not have any off-balance sheet arrangements.

**TRANSACTIONS WITH RELATED PARTIES**

All related party transactions are recorded in the normal course of operations on normal commercial terms and conditions and at market rates, which is the amount of consideration established and agreed to by the related parties.

**Key management personnel and director transactions**

Directors of the Group control 16.9% percent of the voting shares of the Group.

A number of key management personnel, or their related parties, hold positions in other entities that result in them having control or significant influence over the financial or operating policies of these entities.

The aggregate value of transactions and outstanding balances relating to key management personnel and entities over which they have control or significant influence were as follows:

| | | December 31, | |
|---|---|---|---|
| **Director/Officer** | **Transaction** | **2013** | **2012** |
| C F Zhou (director and CEO) | Salary and benefits | $ 115 | $ - |
| C F Zhou (director and CEO) | Consulting fees | 175,161 | 42,300 |
| C F Zhou (director and CEO) | Interest expense | 17,049 | 3,233 |
| Danny Hon (director and CFO) | Accounting fees (ii) | 57,222 | 35,284 |
| Danny Hon (director and CFO) | Interest expense | 10,931 | 2,808 |
| | | $ 260,478 | $ 83,626 |

| | | Balance outstanding | |
|---|---|---|---|
| **Director/Officer** | **Transaction** | **December 31, 2013** | **December 31, 2012** |
| C F Zhou (director and CEO) | Salary and benefits | $ 228,542 | $ 245,415 |
| C F Zhou (director and CEO) | Consulting fees | 511,561 | 336,400 |
| C F Zhou (director and CEO) | Loan payable (i) | 129,278 | 87,949 |
| C F Zhou (director and CEO) | Loan interest payable (i) | 28,586 | 12,909 |
| Danny Hon (director and CFO) | Accounting fees payable (ii) | 316,252 | 285,758 |
| Danny Hon (director and CFO) | Loan payable (iii) | 70,565 | 75,438 |
| Danny Hon (director and CFO) | Loan interest payable (iii) | 26,051 | 16,535 |
| | | $ 1,310,834 | $ 1,060,404 |

(i) During the year ended December 31, 2013, the Group has received short term loan of CND $50,000 from C F Zhou, director and CEO of the Group (During the year ended December 31, 2012 - $CDN 44,000). The short-term loans were unsecured and due on demand with an annual interest rate of 15%. At December 31, 2013, there was an interest payable balance of $28,586 (December 31, 2012: $12,909) owed to director of the Group.

(ii) The Group engaged a company, which is controlled by Danny Hon, to provide accounting services.

(iii) During the year ended December 31, 2013, the Group has received short term loan of CND $nil from Danny Hon, director and CFO of the Group (During the year ended December 31, 2012 - $CDN 10,000). The short-term loans were unsecured and due on demand with an annual interest rate of 15%. At December 31, 2013, there was an interest payable balance of $26,051 (December 31, 2012: $16,535) owed to director of the Group.

**Unsecured loan payables**

The Group had the following loan payables to the key management personnel of the Group with the terms and conditions summarized as follows:

| | December 31, 2013 | | | | |
|---|---|---|---|---|---|
| **Unsecured loan payables** | **RMB** | **Canadian dollars** | **U.S. dollars equivalent** | **Annual interest rate** | **Due date** |
| Chenggang Zhou (director of TTTC) [i] | 700,000 | | 115,633 | 9% | 7/27/2014 |
| Weiguo Mu (minority shareholder of ZYCY) | 500,000 | | 82,595 | 20% | due on demand |
| | 1,200,000 | | $ 198,228 | | |
| Interest payable | $ 91,082 | | $ 15,046 | | |

| | December 31, 2012 | | | | |
|---|---|---|---|---|---|
| **Unsecured loans payable** | **RMB** | **Canadian dollars** | **U.S. dollars equivalent** | **Annual interest rate** | **Due date** |
| Qi Li (minority shareholder of ZYCY) | $ 1,000,000 | - | $ 160,520 | 15% | due on demand |
| Interest payable | $ 18,336 | - | $ 2,943 | | |

**Other related party transactions**

| | December 31, 2013 | December 31, 2012 |
|---|---|---|
| Amount due from a company related to the non-controlling shareholders of ZYCY [ii] | 132,005 | 121,853 |

[i] During the year ended December 31, 2013. Chenggang Zhou, director of TTTC borrowed the loan with annual rate of 9% from Bank of Merchant under his name to finance TTTC's daily activities. The loan is secured by his personal assets.

[ii] It represents the amount collected on behalf of the Group by a company related to the non-controlling shareholders of ZYCY as non-secured and non-interest bearing short-term loan.

## RISK AND UNCERTAINTY FACTORS

**History of losses and anticipate that we may continue for the foreseeable future**
The Group has recognized a net loss of $2,718,360 (2012: $1,295,110) for the year ended December 31, 2013 and has incurred a cumulative loss of $35,597,256 since inception. The Group's future business plan includes the further development and operation of CER's education service portal and sino-foreign co-operation to develop English as a second language training program in China and Chinese Mandarin training program in U.S. The Group's ability to continue as a going concern is depending upon achieving acceptance by the users and profitable level of operations of the education service portal and on the ability to obtain necessary financing to fund our operations. The outcome of these matters cannot be predicted at this time.

**Seasonality**

Historically in its traditional distribution business, the operations of the business are highly seasonal. The Group is attempting to lessen the seasonality of the business by expanding its business into other related areas in the education sector through its internet education service portals.

**Reliance on Government Relationships**

The Group is relying upon continued good working relationships and acceptance from both the national and regional governments it works with. Additionally, continued collaboration with the CDC is important to the Group being able to sell and deliver the teacher training programs. If the CERSP portal was no longer acceptable or it failed to meet acceptable government standards for the K-12 sector, it would seriously impact the continued successful deployment of the CERSP portal and education service portal.

**Tax and Legal Systems in China**

The Group, through its subsidiaries, conducts a significant amount of its business in China. China currently has a number of laws related to various taxes imposed by both federal and regional governmental authorities. Applicable taxes include value added tax, corporate income tax (profits tax), and payroll (social) taxes, together with others. Laws related to these taxes have not been in force for a significant period, in contrast to more developed market economies; therefore, implementing regulations are often unclear or nonexistent. Often, differing opinions regarding legal interpretation exist both among and within government ministries and organizations; thus, creating uncertainties and areas of conflict. Tax declarations, together with other legal compliance areas (as examples, customs and currency control matters) are subject to review and investigation by a number of authorities, which are enabled by law to impose extremely severe fines, penalties and interest charges. These facts create tax risks in China substantially more significant than typically found in countries with more developed tax systems.

Management believes that the Group is in substantial compliance with the tax laws affecting its operations; however, the risk remains that the relevant authorities could take different positions with regard to interpretive issues and the effect could be significant. The fact that a year has been reviewed does not close that year, or any tax declaration applicable to that year, from further review.

**Competition**

Foreign direct investment in China has increased rapidly and the investment environment has further improved to encourage foreign and local investors to invest in fields, such as education, high-tech, modern agriculture and infrastructure construction. A number of large companies are involved in the publishing and distribution of educational products in the mainstream areas of math, science and language arts. There is no guarantee that other competitors will not become involved in business similar to that of the Group.

**Management**

The Group currently has a small executive management group, which is sufficient for its present stage of development. Although the Group's development to date has largely depended and in the future will continue to depend upon the efforts of certain current executive management, the loss of a member of this group could have a material adverse effect on the Group.

**Funds Remittance**

Provided that conversion of Renminbi into foreign exchange and the remittance of foreign exchange are duly arranged in accordance with the relevant laws and regulations on foreign exchange, a Foreign Investment Enterprise ("FIE") is able to remit dividends and other payments from China.

According to the 1999 Circular on Relevant Questions Concerning the Remittance of Profits, Dividends and Bonuses out of China Through Designated Foreign Exchange Banks, effective from October 1, 1999, an FIE is permitted to remit profits, dividends and bonuses out of China in proportion to the amount of registered capital that has been paid up, notwithstanding that its registered capital has not been paid up pursuant to its constitutional documents.

**Financial Instruments**

The Board of Directors has overall responsibility for the establishment and oversight of the Group's risk management framework. The Group's financial instruments consist of cash, accounts receivables, trade and other payables, loan payable and due to related parties.

The Group's financial instruments are exposed to the risks described below:

(a) Credit risk

Credit risk is the risk of an unexpected loss if a party to a financial instrument fails to meet its contractual obligations. The Group's credit risk is primarily attributable to cash and accounts and other receivables. The Group has no significant concentration of credit risk arising from operations. Other receivables mainly consist of an advance to a third party for project development, as well as goods and services tax due from the Federal Government of Canada, interest receivable and amounts advanced to employees and others. Management assesses the credit risk concentration with respect to accounts receivable and other receivables annually and adjusts them accordingly.

(b) Liquidity risk

Liquidity risk is the risk that the Group will not be able to meet its financial obligations as they fall due. At December 31, 2013, the Group had a working capital deficiency of $2,945,862 (December 31, 2012: working capital deficiency of $3,022,993). The Group is focused on generating sales revenue and is actively pursuing additional sources of financing to ensure that it can meet its ongoing operating requirements and planned capital expenditures.

(c) Market risk

Market risk is the risk of loss that may arise from changes in market factors such as interest rates, foreign exchange rates and equity prices.

(i) Interest rate risk

Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates. From time to time, the Group is exposed to short term interest rates through the interest earned on cash and cash equivalents. The Group only has debt with fixed interest rates. The Group's current policy is to invest excess cash in short-term deposits with its banking institutions. The Group periodically monitors the investments it makes and is satisfied with the credit ratings of its banks.

(ii) Foreign currency exchange rate risk

Foreign currency exchange rate risk is the risk that the fair value of financial instruments or future cash flows will fluctuate as a result of changes in foreign exchange rates. The majority of the Group's assets, liabilities, revenues and expenses are denominated in Chinese Renminbi ("RMB"), which was tied to the U.S. dollar and is now tied to a basket of currencies of China's largest trading partners, is not a freely convertible currency. The appreciation of the RMB against the U.S. dollar would result in an increase in the assets, liabilities, revenues and expenses of the Group and a foreign currency gain included in other comprehensive income. Conversely, the devaluation of the RMB against the US dollar would result in a decrease in the assets, liabilities, revenues and expenses of the Group and a foreign currency loss included in other comprehensive income.

The functional currency of CER is Canadian dollar and the functional currency of its China subsidiaries is RMB. Major transactions are transacted in Canadian dollars and RMB. The Group maintains Chinese RMB bank accounts in China to support monthly forecasted cash outflows. Management believes the foreign exchange risk derived from currency conversions is minimal and therefore does not hedge its foreign exchange risk.

Fluctuation in the value of Canadian dollar relative to US dollar has some impact on the Group's head office financial results. However, such exchange rate fluctuations have not materially affected the overall financial earnings and results on a consolidated basis.

## SIGNIFICANT ACCOUNTING POLICIES

The preparation of financial data is based on accounting principles and practices consistent with those used in the preparation of the audited annual financial statements as at December 31, 2013.

### New standards and interpretations adopted during the period

The Group adopted the following new standards during the period:

*IFRS 10, Consolidated Financial Statements*

On January 1, 2013, the Company adopted IFRS 10 which requires an entity to consolidate an investee when it is exposed or has rights to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. Under previous IFRS, consolidation was required when an entity has the power to govern the financial and operating policies of an entity so as to obtain benefits from is activities. IFRS 10 replaces SIC-12, Consolidation - Special Purpose Entities, and parts of IAS 27, Consolidated and Separate Financial Statements. Adoption of the new standard did not have any impact on the financial statements.

*IFRS 11, Joint Arrangements*

On January 1, 2013, the Company adopted IFRS 11 which establishes the principles that a party to a joint arrangement determines the type of joint arrangement in which it is involved by assessing its rights and obligations and accounts for those rights and obligations in accordance with that type of joint arrangement. IFRS 11 replaces IAS 31 Interests in Joint Ventures and

SIC 13 Jointly Controlled Entities - Non-Monetary Contributions by Venturers. Adoption of the new standard did not have any impact on the financial statements.

*IFRS 12, Disclosure of Interests in Other Entities*

On January 1, 2013, the Company adopted IFRS 12 which includes the disclosure requirements for all forms of interests in other entities, including joint arrangements, associates, special purpose vehicles and other off balance sheet vehicles. Adoption of the new standard did not have any impact on the financial statements.

*IFRS 13, Fair Value Measurements*

On January 1, 2013, the Company adopted IASB IFRS 13, a new comprehensive standard on measuring and disclosing fair value and will supersede all other fair value guidance in IFRS. The standard is effective for annual periods beginning on or after January 1, 2013. Adoption of the new standard did not have any impact on the financial statements.

*IAS 1, Presentation of Financial Statements*

On January 1, 2013, the Company adopted the amendments to IAS 1 "*Presentation of Financial Statements*" as it relates to the presentation of other comprehensive income (OCI). The amendments to this standard do not change the nature of the items that are currently recognized in OCI, but requires presentational changes. It requires entities to separate items presented in OCI into two groups based on whether or not they may be recycled to profit or loss in the future. Items that will not be recycled, such as re-measurements resulting from the amendments to IAS 19, will be presented separately from items that may be recycled in the future, such as deferred gains and losses on cash flow hedges. Entities that choose to present OCI items before tax will be required to show the amount of tax related to the two groups separately. The adoption of this standard did not have a material impact on the Company's financial statements.

**New standards and interpretations not yet adopted**

Standards issued but not yet effective up to the date of issuance of the Company's consolidated financial statements are listed below. This listing is of standards and interpretations issued, which the Company reasonably expects to be applicable at a future date. The Company intends to adopt those standards when they become effective. The Company does not expect the impact of such changes on the consolidated financial statements to be material.

*IFRS 2 Share-based payment*

The amendments to IFRS 2, issued in December 2013 clarify the definition of "vesting conditions", and separately define a "performance condition" and a "service condition". A performance condition requires the counterparty to complete a specified period of service and to meet a specified performance target during the service period. A service condition solely requires the counterparty to complete a specified period of service. The amendments are effective for share-based payment transactions for which the grant date is on or after July 1, 2014.

*IFRS 7, Financial instruments: disclosures and IAS 32 Financial instruments: presentation*

Financial assets and financial liabilities may be offset, with the net amount presented in the statement of financial position, only when there is a legally enforceable right to set off and when there is either an intention to settle on a net basis or to realize the asset and settle the liability simultaneously. The amendments to IAS 32, issued in December 2011, clarify the meaning of the offsetting criterion "currently has a legally enforceable right to set off" and the principle behind net settlement, including identifying when some gross settlement systems may be considered equivalent to net settlement. The amendments will only affect disclosure and are effective for annual periods beginning on or after January 1, 2014.

*IFRS 9, Financial instruments*

IFRS 9 was issued in November 2009 and subsequently amended as part of an ongoing project to replace IAS 39 Financial instruments: Recognition and measurement. The standard requires the classification of financial assets into two measurement categories based on the entity's business model for managing its financial instruments and the contractual cash flow characteristics of the instrument. The two categories are those measured at fair value and those measured at amortized cost. The classification and measurement of financial liabilities is primarily unchanged from IAS 39. However, for financial liabilities measured at fair value, changes in the fair value attributable to changes in an entity's "own credit risk" is now recognized in other comprehensive income instead of in profit or loss. This new standard will also impact disclosures provided under IFRS 7 Financial instruments: disclosures.
In November 2013, the IASB amended IFRS 9 for the significant changes to hedge accounting. In addition, an entity can now apply the "own credit requirement" in isolation without the need to change any other accounting for financial instruments. The mandatory effective date of January 1, 2015 has been removed to provide sufficient time for preparers of financial statements to make the transition to the new requirements.

*IFRS 13, Fair Value Measurement*

IFRS 13 is a comprehensive standard for fair value measurement and disclosure for use across all IFRS standards. The new standard clarifies that fair value is the price that would be received to sell an asset, or paid to transfer a liability in an orderly transaction, between market participants, at the measurement date. Under existing IFRS, guidance on measuring and disclosing fair value is dispersed among the specific standards requiring fair value measurements and does not always reflect a clear measurement basis or consistent disclosures. The amendments to IFRS 13, issued in December 2013, clarify that the portfolio exception applies to all contracts within the scope of IFRS 9 Financial instruments or IAS 39 Financial instruments: Recognition and measurement, regardless of whether they meet the definitions of financial assets or financial liabilities in IAS 32 Financial instruments: Presentation. The amendments are effective for annual periods beginning on or after July 1, 2014.

*Amendments to IAS 24, Related Party Disclosures*

The amendments to IAS 24, issued in December 2013, clarify that a management entity, or any member of a group of which it is a part, that provides key management services to a reporting entity, or its parent, is a related party of the reporting entity. The amendments also require an entity to disclose amounts incurred for key management personnel services provided by a separate management entity. This replaces the more detailed disclosure by category required for other key management personnel compensation. The amendments will only affect disclosure and are effective for annual periods beginning on or after July 1, 2014. The adoption of this issuance did not have a significant impact on the Company's financial statements.

*Amendments to IAS 36, Impairment of assets*

The amendments to IAS 36, issued in May 2013, require:

- Disclosure of the recoverable amount of impaired assets; and
- Additional disclosures about the measurement of the recoverable amount when the recoverable amount is based on fair value less costs of disposal, including the discount rate when a present value technique is used to measure the recoverable amount.

The amendments will only affect disclosure and are effective for annual periods beginning on or after January 1, 2014.

The Company is currently assessing the impact that the new and amended standards will have on its financial statements or whether to early adopt any of the new requirements.

*IFRS 9, Financial Instruments*

On November 12, 2009, the IASB issued IFRS 9 Financial Instruments as the first step in its project to replace International Accounting Standard ("IAS") 39 *Financial Instruments: Recognition and Measurement*. IFRS 9 retains but simplifies the mixed measurement model and establishes two primary measurement categories for financial assets: amortized cost and fair value. The basis of classification is made at the time the financial asset is initially recognized, namely when the entity becomes a party to the contractual provisions of the instrument. IFRS 9 amends some of the requirements of IFRS 7 *Financial Instruments: Disclosures* including additional disclosures about investments in equity instruments measured at fair value in other comprehensive income, and guidance on financial liabilities and de-recognition of financial instruments. Although early adoption is permitted, in December 2011, the IASB issued an amendment that adjusted the mandatory effective date of IFRS 9 from January 1, 2013 to January 1, 2015. The Company is currently determining the impact of adopting IFRS 9.

**OUTLOOK**

The Group's objective is to become the leading kindergarten to grade 12 education services platform, content provider and social networking system in China's education sector. The Group provides a range of services to government education authorities, schools, teachers, students and their parents. The Group has implemented a four step growth and revenue strategy which is now being commercialized and expanded nationwide.

The first step of the strategy involves working with various levels of government to deliver government-funded online teacher training programs. The Group has developed more than 400 online teacher training courses for the continuous education of teachers. This means teachers can obtain government certificates upon successful completion of any of these courses through national, provincial and municipal teacher training programs. More than 500,000 teachers were trained in the Group's teacher training programs. CER is the only public company endorsed by China's Ministry of Education ("MOE") for national level online teacher training programs.

The Group has developed digital textbooks and also developed more than 100,000 K-12 online lesson plans and is continuing to develop new educational content and upgrade the technology and functions of its portal. The Group has been engaged by fourteen provinces to provide its online products.

The second step of the strategy involves integrating the Group's products and services into teachers' daily routines. This will allow teachers to interact and communicate with each other while establishing a close relationship with the Group and its products. These products include online teacher training, professional development and sharing of lesson plans. The CERSP portal is one of the largest and most popular K-12 teacher blog systems in China with more than one million registered and active K-12 teachers. The CERSP portal has developed into a strong national brand and it has a reputation for offering best-in-class online learning products and services. The first two steps are well underway and are expanding into more provinces.

The third step involves promoting products directly to teachers through CER's School Platform. Each school pays a subscription fee for these products, and the provinces of Gansu, Liaoning, Shanxi and Guangxi have commenced similar programs based on the Group's School Platform.

The fourth step of the growth strategy is to target students by offering a number of products and services. This includes offering our collection of online tutoring courses, customized education resources, formative assessment tools and education games, which are some of the largest in China. Students and parents pay a subscription fee for this platform. Several provinces have initiated discussions with CER for this program.

CER signed an agreement with Shanxi Provincial education authority to customize the Group's School Platform to provide services and education resources to both teachers and students for Shanxi Province education reform. The education reform emphasizes interaction between teachers and students with digitized education resources and multimedia equipment in classrooms.

CER has started to provide digital textbook to the students in Guizhou Province. This is a significant step for CER to combine the Group's internet portal with traditional textbooks, which also provides significant opportunities for CER's textbook business.

CER has also signed an agreement with the Teaching & Research Division of Gansu Provincial Education Department to add mobile learning solutions to the Company's School Platform for the students in Gansu Province. The Teaching & Research Division will organize academic experts and distinguished teachers in Gansu Province and CER will organize national academic experts to create video and written content for the program. This new digital content will be available on the School Platform and, together with CER's existing content (which includes tests, assessments, over 100,000 lesson plans, and other comprehensive education resources), will provide significant value to teachers and students. These new solutions will provide students and teachers with additional functionality for their mobile devices and will emphasize interaction among teachers and students, and their PC environment.

The Company has also signed an agreement with China Telecom (Gansu) to provide Smartphone services to the mobile learning program.

This program is a keystone to CER's business strategy, the teachers and students interact on our school platform, which is the centerpiece of our online education service business. Not only do teachers and students interact through our platform, they will propagate its use with other teachers, students and parents. Because of its advanced features and complete compliance with government programs, the Company expects that educators, students and parents will gravitate to the system to work, study, interact and develop social networks. We expect the new functions of the school platform will be an example of the high-growth potential of our products and business model in other provinces, particularly for the provinces which have started to used our school platform.

The Group has over a decade of experience operating in China, and has established a formidable position in the K-12 education sector, and is now working with over 200 education authorities in various provinces of China. CER is successfully advancing commercialization of the Group's products and services with many products and across a broad range of education related customers. The Group's four-step growth plan is currently being adopted in fourteen provinces throughout China and represents a unique opportunity for investors to participate in the rapid growth of China's education sector.

The Group has developed an unparalleled and broad portfolio of education products that it believes in unavailable in any other education market. It has been market tested and developed in the world's largest education market. The Group intends to explore the potential to provide these online, networked products and services in other education markets. It may launch these products on its own or in partnership with domestic industry players.