Karnalyte RESOURCES

MANAGEMENT'S DISCUSSION AND ANALYSIS

This Management's Discussion and Analysis ("MD&A") is intended to provide a summary of the operational and financial results of Karnalyte Resources Inc. ("Karnalyte" or the "Company") for the period ended March 31, 2012 and 2011. This MD&A should be read in conjunction with the unaudited interim financial statements of the Company and the related notes thereto for the period ended March 31, 2012. This commentary is dated May 10, 2012. The financial statements have been prepared in accordance with International Accounting Standard ("IAS") 34. These documents, including the Annual Information Form, and additional information about the Company are available on SEDAR at www.sedar.com. Some of the statements made herein contain "forward-looking information" and accordingly please refer to the "Forward-Looking Statements" section at the end of the MD&A.

OVERVIEW

Karnalyte was incorporated under the Alberta Corporations Act on November 16, 2007 and is an Alberta headquartered company focused on exploration and development of potash in Saskatchewan. The Company holds subsurface mineral Permit KP 360A comprising 68,301 acres as well as lease KSLA 010 comprising 16,825 acres near Wynyard, Saskatchewan. The Company has completed seismic testing as well as drilling programs bringing the total acres explored to 17,544 or 20% of the total permit area.

On March 30, 2012, the Company filed an Amended and Restated Reserve and Resource Estimate for the Wynyard Carnallite Project ("Restated Report"). The Restated Report updated the Company's reserve calculations to 62.9 million tonnes of proven and 92 million tonnes of probable KCl. The report indicates that the manufacturing plant is planned to have an initial production capacity of 625,000 tonnes per year of potash and expand to 2,125,000 per year. At this projected production rate the mine life is estimated at 68 years.

Karnalyte plans to use solution mining to extract a brine rich in potash (KCl), magnesium chloride ($MgCl_2$) and sodium chloride (NaCl) which can then be processed into marketable products. The first phase of the Wynyard Carnallite Project (the "Project") will concentrate on the production of high quality potash products with a brine rich in magnesium chloride and sodium chloride treated as waste and disposed back underground into the spent caverns. In a subsequent phase of the Project these waste streams are planned to be treated to produce marketable sodium chloride and magnesium-products. The products in the current phase are expected to be a granulated potash pellets for the agricultural market and industrial grade for the industrial market.

Based on the results of the feasibility study and the Restated Report, the Company is now planning and preparing to launch construction of the processing facility and mine field and ultimately enter into production. Expenditures to date were focused on setting the stage for this feasibility study and Restated Report which, in turn, is expected to then lead into the actual construction phase. Plant construction is expected to take approximately 18 - 24 months following the completion of additional financing and regulatory approvals. Preparation of the brine field is expected to be completed concurrently with plant construction. Within a 10 month period following the completion of the plant the Company expects production to be up to a full run rate of 625,000 tonnes per year. Subsequent phases of the Project, including the construction phase will form the vast majority of the total expected project cost anticipated to be approximately $593 million.

Karnalyte RESOURCES

RESULTS OF OPERATIONS

General and administrative expenses (G&A)

G&A costs for the period ended March 31, 2012 amounted to $798,307, a decrease of $12,118 from the comparative 2011 amount of $810,425.

The key components of the G&A costs are as follows:

G&A Expenditures		
	Period ended March 31,	
	2012	2011
Salary, wages and benefits	$ 394,220	$ 363,587
Accounting and legal	79,950	107,130
Regulatory	65,011	42,751
Director fees	60,750	41,750
Business and corporate development and investor relations	48,752	62,694
Rent	46,724	52,357
Consulting	17,243	33,920
Other	85,657	106,236
Total general and administrative	$ 798,307	$ 810,425

Salaries, wages and benefits for the period ended March 31, 2012 was $394,220 compared to $363,587 in 2011. The increase is mainly due to reclassification of an employee from capital to expense who was working on capital projects last year but has since been moved to the marketing department. There was also an increase as a result of annual employee reviews and corresponding raises for employees. During the period ended March 31, 2012, the Company focused on a variety of capital projects and the employee remuneration related to these projects was capitalized. A total of $227,495 of salary and benefits costs were capitalized during the period ended March 31, 2012 which is an increase of $40,098 over the comparative period March 31, 2011. This increase is mainly due to the Company hiring two new employees that are being capitalized to work on product development and help move the project forward.

Management and consulting expenses for the period ended March 31, 2012 amounted to $17,243 compared to $33,920 in the comparative 2011 period. As the staffing levels continue to increase there are fewer consultants required to move the Project forward. In 2011 consulting fees incurred was the result of the Company enlisting accounting advisory services in preparation for the transition to IFRS. The Company also utilized an engineering consultant to assist with product development. The Company continues to utilize certain consultants focused on marketing and human resources where specific skill sets were required outside of the Company.

Accounting and legal expenses for the period ended March 31, 2012 was $79,950 compared to $107,130 in the comparative period. The decrease is a result of additional legal fees required in 2011 to assist the company with setting up contracts related to the feasibility and environmental impact study. The expenses incurred in the period ended March 31, 2012 consist of general matters. The accounting fees decreased $4,250 over the comparative periods due to higher fees associated with the transition to IFRS in 2011.

Business and corporate development and investor relations expenses for the period ended March 31, 2012 amounted to $48,752 compared to $62,694 in the 2011 comparative period. In the period ended

March 31, 2012 the Company traveled to India to give presentations to potential investors as well as attended the World Fertilizer Conference in Chicago. The Company has also participated in various trade shows and secured a marketing agreement with a third party to assist with website development and maintenance, press releases and other services as required. The higher costs associated with the comparative period relates to a series of presentations called "On the Radar" that the Company participated in to market the Company and seek potential investors.

Regulatory expense for the period ended March 31, 2012 amounted to $65,011 compared to $42,751 for the comparative period. The regulatory expenses are related to the annual TSX listing fees as well as fees incurred for public filing requirements on SEDAR. The increase of $22,260 is due to the market capitalization of the Company going over $250M which pushes the fee structure to a new level of higher remittances.

Director fees for the period ended March 31, 2012 amounted to $60,750 compared to $41,750 for the 2011 comparative period. The director fees increased in the current period but continue to be held at modest levels. The increase was related to bringing in two new directors to add to the growing skill set the Company requires to move the project forward to the next levels.

Other expenses for the period ended March 31, 2012 amounted to $85,657 compared to $106,236 for the comparative period representing a decrease of $20,579. This decrease resulted from a variety of other G&A costs with the primary decreases in the current period relating to additional office space being set up in the comparative period. In order to set up the new space there were wiring expenditures as well as equipment and furniture purchases which amounted to approximately $15K in additional expenditures. In addition, other personnel costs including but not limited to subscriptions, meals, travel and entertainment and motor vehicle decreased over the period ended March 31, 2011 due to decreased activity over the comparative quarter when many employees were travelling as a result of the recently completed IPO. These decreases are slightly offset by general corporate costs (such as property taxes, insurance and repairs and maintenance) were higher for the period ended March 31, 2012 compared to the prior period due to additional office space for the entire period.

Non G&A costs

Transaction costs for the period ended March 31, 2012 was $108,984 compared to $nil in the 2011 comparative period. These expenses were related to an equity financing that was withdrawn late in the year due to comments raised by the securities commissions over the technical report that could not be answered in the required time period.

Depreciation and amortization for the period ended March 31, 2012 was $193,345 compared to $56,656 in the 2011 comparative period. These expenses were related to the purchases and subsequent depreciation of machinery and equipment including but not limited to two loaders, drilling mats and two pumphouses.

Share-based payments for the period ended March 31, 2012 was $130,521 compared to $458,204 in the 2011 comparative period. The expenditures relate to the same options expensed on a quarterly basis where the terms contain vesting over a two year period. Options are expensed in a manner where the higher expenditures are incurred at the start of the option period and then decrease over time. As a result the stock-based expenses were higher in the comparative period March 31, 2011 as compared to the current period ending March 31, 2012.

Finance income for the period ended March 31, 2012 was $117,775 compared to $38,188 in the 2011 comparative period. The income is a direct correlation to the amount of funds the Company had to invest over the periods and the interest income generated from the cash on hand.

PREVIOUSLY DISCLOSED USE OF PROCEEDS

Analysis of Prospectus Use of Proceeds				
	Current Expectation	Prospectus	Variance	Notes
Geological Analysis	$ 3,000,000	$ 3,000,000	$ -	
Feasibility Study Costs	9,000,000	17,000,000	(8,000,000)	a
Additional Exploration Seismic and Drilling	16,000,000	10,000,000	6,000,000	b
Environmental Impact Assessment	2,000,000	2,000,000	-	
Infrastructure Preparation and Equipment Deposits	5,000,000	9,400,000	(4,400,000)	c
Magnesium Pre-Feasibility Study	350,000	-	350,000	d
Contingencies	15,050,000	9,000,000	6,050,000	e
General, Administrative and Corporate Purposes	5,046,300	5,046,300	-	
Total	$ 55,446,300	$ 55,446,300	$ -	

Notes

a) Feasibility Study Costs estimated in the Prospectus, dated December 6, 2010 (the "Prospectus"), were based on expectations of at least four additional drill cores being required to fully understand the rock mechanical properties and geological structure related to constructing the processing facility and preparing the solution mine area. Upon further review of existing information and considering the results of the two drill hole geological analysis drilling program conducted, the co-authors of the feasibility study determined the additional drill holes would not be required. The Company included an estimate of approximately $6 million for these holes in the $17 million feasibility study costs. In addition, the Company had included $2 million in additional contingencies for the surface facility and other portions of the feasibility study that are not required based on the proposals received and accepted.

b) The Company decided subsequent to the Prospectus to increase the drilling and exploration program planned for 2011. No additional 3D seismic activity was planned in the Prospectus but has since been determined to be important to gaining a better understanding of up to one-half of the total permit area under control, estimated at $2.5 million. This 3D is still being considered in 2012 and will be funded out of the proceeds of the IPO. In addition, the Company had planned on additional drill holes being required in the feasibility study that were subsequently removed as described above. As a result, the Company decided to add two additional drill targets to the exploration plan at a cost of up to $3.5 million.

c) Given the results of the feasibility study and the Restated Report and the recommendations contained therein, the expenditures allocated to infrastructure preparation and equipment deposits have been decreased. The funds have now been allocated to contingencies until such time that decisions are made on where the funds are required.

Karnalyte RESOURCES

d) A contract was entered into with Lyntek Incorporated to prepare a pre-feasibility study for magnesium compounds in the amount of $350,000.

e) The Company incurred some unanticipated expenditures including a failed financing that resulted in recognition of significant offering expenses together with expenditures made to support the filed Technical Report. As the Company continues the planning phases of the project decisions may be made to proceed with various initiatives that were not in the original scope of the Project. As a result the contingencies have been increased by $6 million. Expenditures against this contingency will be considered provided they allow for the Company to protect its ultimate timeline as much as possible.

The amounts above exclude gross proceeds of $4,042,000 ($3,799,480 net of commissions) related to the closing of the over-allotment option on January 13, 2011. These proceeds will be allocated to general, administrative and corporate purposes.

SUMMARY OF QUARTERLY RESULTS

The following table provides selected financial information of the Company for each of the last eight quarters ended at March 31, 2012:

Selected Quarterly Results								
	2012	2011				2010		
	Mar 31	Dec 31	Sep 30	Jun 30	Mar 31	Dec 31	Sep 30	Jun 30
Total revenue	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -
Comprehensive loss	(1,090,733)	(2,347,228)	(549,778)	(1,172,229)	(1,284,601)	(817,645)	(663,815)	(1,859,032)
Basic and diluted loss per share	(0.05)	(0.11)	(0.03)	(0.06)	(0.06)	(0.06)	(0.05)	(0.15)
Total current assets	32,644,537	35,166,003	38,184,599	45,131,091	57,527,453	59,356,598	4,909,484	5,624,365
Total assets	74,462,061	75,847,125	75,436,477	76,256,815	74,310,804	70,689,252	14,463,689	14,722,994
Total liabilities	1,435,257	2,558,416	3,619,114	4,579,036	2,515,976	2,417,970	520,239	395,729
Total shareholders' equity	73,026,804	73,288,709	71,817,363	71,677,779	71,794,828	68,271,282	13,943,450	14,327,265

Comparability between quarters is difficult due to the development of the Company from a start up operation, to being a public entity throughout the periods presented. However, general trends can be summarized as follows:

Comprehensive loss was driven primarily by G&A expenses incurred to fund the continued growth of the Company. The loss has ranged from $549,778 for the quarter ended September 30, 2011 to $2,347,228 for the quarter ended December 31, 2011. The loss for the quarter ended December 31, 2011 was inflated from writing off financing expenses as a result of pulling the bought-deal financing in December 2011 and therefore not representative of a typical quarter. The varied results over the quarters can be attributed to a few main factors, the first being increased activity in becoming a public entity, establishing operations, growing staff levels, increase in staff support costs and other G&A costs associated with continuing to grow the business. The increased losses in the quarters ended June 30, 2010, March 31, 2011, June 30, 2011 and December 31, 2011 increased due to the senior management team being larger, along with share-based payment expenses of $1,023,339, $458,204, $434,753 and $1,722,291 respectively, from stock options expensed in those quarters. Income of $61,429, $449,957, $32,616 and $11,578 was generated in the quarters ended June 30, 2011, September 30, 2011, December 31, 2011 and

March 31, 2012 respectively from mat rentals resulting in a lower net loss compared to comparative quarters.

Current assets trends principally reflect activity in the cash account. This account comprises the vast majority of current assets with relatively minor balances in prepaid expenses and miscellaneous receivables. Starting with the quarter ended June 30, 2010 and through the third quarter of 2010, spending increased, resulting in decreased current assets, to fund the expenditures as the Project activity increased. The quarter ended December 31, 2010, reflects a large increase in current assets as a result of the Company successfully completing an IPO on December 14, 2010. The IPO raised $59,985,000 from the offering with underwriting fees and related share issue costs resulting in net proceeds of $55,014,993. On January 14, 2011 the over-allotment related to the IPO was fulfilled which resulted in additional gross proceeds of $4,042,000 which after deducting underwriting fees, net proceeds equalled $3,799,480. During the quarters ending June 30, 2011, September 30, 2011, December 31, 2011 and March 31, 2012 spending continued to increase and therefore current assets decreased as a result of the progression and completion of the feasibility study and continued work on the environmental impact study and the prefeasibility report for magnesium. Throughout that time period a seven well drilling program also took place which resulted in additional spending.

Total assets on a quarterly basis reflect two main components, cash from financings still available to the Company and capitalized expenditures on capital assets and mineral properties for moving the Project forward. Total assets remained relatively constant for the majority of the periods above. The quarterly fluctuations generally reflect cash expended on G&A expenses. The significant increase for the quarter ended December 31, 2010 reflects the completion of the IPO which generated net proceeds of over $55.0 million and $3.8 million in the first quarter of 2011, as a result of the overallotment being fulfilled. Significant levels of capital spending continued throughout the quarter ended March 31, 2012 as many of the Company's large cash outlays were completed including but not limited to the feasibility study and the environmental impact study.

Total liabilities for the periods illustrated relate primarily to trade and other payables. These balances vary in the analysis due to timing of payments that are required on the various work performed on bringing the Project to the current level. The large increase in the quarters ended December 31, 2010, March 31, 2011, June 30, 2011, September 30, 2011 are a result of drilling projects and the feasibility study which were in process over the quarter end dates and a large amount of payables and accruals were generated to account for the extra expenditures. The decrease in the quarter ended December 31, 2011 and March 31, 2012 is due to the completion of the feasibility study and other related activities.

FINANCING

2010

The IPO was completed on December 14, 2010 with 6,975,000 common shares being issued at a price of $8.60 per share for total gross proceeds of $59,985,000. Share issue costs related to this offering were $4,970,007.

In conjunction with the IPO, the Company granted 418,500 non-transferable broker warrants to the underwriters with an exercise price of $8.60 per warrant that will expire on or about on June 14, 2012.

On November 12, 2010 the Company issued 278,540 common shares for no consideration to comply with the terms of the liquidity penalty granted to subscribers of the 2009 private placement. The filing of the

final prospectus in December 2010 constituted the liquidity event as defined in the private placement which results the terms of the private placement being fulfilled. No further obligations exist.

During the year ended December 31, 2010 a total of 176,400 stock options were exercised by employees, directors and consultants for gross proceeds to the Company of $395,600.

2011

The over-allotment related to the IPO was completed on January 14, 2011 where 470,000 common shares were issued at a price of $8.60 per share for total gross proceeds of $4,042,000. Share issue costs related to this offering were $325,472. The proceeds from the IPO will be used for general corporate purposes.

Along with the over-allotment, the Company granted 28,200 non-transferable broker warrants to the agents with an exercise price of $8.60 per warrant that will expire on or about July 13, 2012.

In December 2011 a bought-deal financing was pulled due to insufficient time to gather additional information to respond to securities commissions comments that were raised on the Company's technical report. Expenditures of $696,408 were incurred in 2011 and an additional $108,984 in the three months ended March 31, 2012 in relation to the financing.

During the year ended December 31, 2011 there were 50,000 options issued to new directors of the Company. There were 609,500 stock options exercised by employees, directors or consultants and 245,296 broker warrants exercised for gross proceeds to the Company of $4,567,999.

2012

During the period ended March 31, 2012 there were no new options issued. There were 133,200 stock options exercised by employees, directors or consultants for gross proceeds to the Company of $666,000.

INVESTING

The Company capitalizes costs incurred on projects that are determined to provide future benefit and charges other costs to operations including administrative salaries, support and office costs, community relations programs and other administrative related expenditures. Costs directly related to capital assets are capitalized to appropriate categories and depreciated over their useful lives. Costs of personnel related entirely to preparation of mineral properties on the Company's permit areas and for the future construction of facilities and product development are capitalized as part of the mineral properties or of the processing facilities.

Karnalyte RESOURCES

Intangible assets

During the period ended March 31, 2012, the Company capitalized $1,224,923 to intangible assets in the following areas:

Intangible Assets		
Period ended	March 31, 2012	December 31, 2011
Mineral property		
Surface land	$ 1,434,723	$ 1,415,249
Permits	218,847	201,897
Geophyics	4,262,672	4,262,672
Product Development	52,590	-
Drilling	19,099,108	18,646,659
Engineering	905,854	806,777
Feasibility study	10,827,683	10,753,396
Environmental	1,392,399	887,146
Process patent	86,256	75,722
Computer software	26,992	32,683
Balance, end of period	$ 38,307,124	$ 37,082,201

Mineral property expenditures in the quarter ended March 31, 2012 related to moving the various projects including feasibility study, environmental impact study and the prefeasibility study for magnesium forward. The additional land expenditures in the period ending March 31, 2012 related to leveling land and other preparations to build a staging yard near the plant site in Wynyard. Permits increase a small amount as a result of the annual fees paid to maintain the Companies permit (KP 360A) and lease (KLSA 010) areas. Product development is now being capitalized due to the progressed nature of the work that is being done in preparation for the testing of the products. The majority of the expenditures related to drilling over the period ending March 31, 2012 mainly related to moving a drilling rig from its original location to a staging area closer to Wynyard. Additional drilling is anticipated to begin in the third quarter of 2012 but is contingent on new developments regarding project financing. There was a small amount of engineering expenditures incurred over the period in relation to ongoing engineering requirements from the companies various third party consultants. The additional expenditures relating to the feasibility study were incurred as a result of the release of the Restated Report. Environmental expenditures will continue as the Company continues to move the environmental impact assessment to the final stages.

Patent expenditures have increased slightly from additional work done on patents as well as registering patents in the United States.

Computer software decreased for the quarter ended March 31, 2012 as a result amortization.

Decommissioning obligations

The Company's decommissioning obligations are based on the Company's ownership in wells and facilities. Management estimates the costs to abandon and reclaim the wells and the facilities and the estimated time period during which these costs will be incurred in the future. The majority of these costs are expected to be incurred over the next 30 years. The undiscounted amount of estimated costs required to settle the obligations at March 31, 2012 is $270,000 (March 31, 2012 – $212,000). The estimated costs have been inflated at 2.0 percent and discounted at a risk free rate of 2.45 percent as at March 31, 2012.

Capital assets

During the period ended March 31, 2012, the Company capitalized $79,540 to machinery and equipment and leasehold improvements. These expenditures were offset by depreciation of $168,061 which resulted in an overall decrease to capital assets of $88,521. Expenditures were capitalized to the following areas:

Capital Assets		
Period ended	March 31, 2012	December 31, 2011
Buildings	$ 225,347	$ 227,942
Land	124,656	124,656
Machinery and equipment	2,718,866	2,788,506
Leasehold improvements	26,176	37,833
Equipment under capital lease	4,027	5,753
Furniture and equipment	36,328	39,231
Balance, end of period	$ 3,135,400	$ 3,223,921

Buildings decreased by $2,595 during the period ended March 31, 2012. This decrease is a result of depreciation on a building in Wynyard, Saskatchewan.

Machinery and equipment purchased in the period ending March 31, 2012 was a Cat Loader that will be located in the staging yard and used to move material and equipment. Depreciation for the period ending March 31, 2012 amounted to $144,059.

Leasehold improvements decreased by $11,657 as a result of depreciation recorded in the period ended March 31, 2012.

Furniture and equipment decreased by $2,903 during the period ended March 31, 2012 as a result of depreciation which has been calculated on a straight line basis over five years.

LIQUIDITY AND CAPITAL RESOURCES

At March 31, 2012, the Company had net working capital of $31,390,734 compared to $55,133,689 at March 31, 2011 including $32,032,143 and $56,384,392, respectively, in cash. As at March 31, 2012, the Company also had $375,000 in restricted cash that was set up as a requirement from the Government of Saskatchewan in order to operate the test plant in Saskatchewan. The Company maintains cash in bank accounts for day to day operations and invests the excess in overnight financial instruments in high interest saving accounts that are highly liquid. No investments are made in commercial paper instruments.

The Company has sufficient cash to meet its short-term corporate costs and existing capital plans and has sufficient funds to finance exploration and ongoing corporate functions. There is no certainty, however, that the Company will be able to raise additional funds to obtain the necessary capital to move the Project forward to the production stage.

CONTRACTUAL OBLIGATIONS

The following table summarizes the commitments of the Company as at March 31, 2012:

Contractual Obligations					
	Payments due by period				
	Total	Less than 1 year	2-3 years	4-5 years	More than 5 years
Trade and other payables	$ 1,248,625	$ 1,248,625	$ -	$ -	$ -
Capital lease	$ 5,178	$ 5,178	$ -	$ -	$ -
Office lease	$ 219,900	$ 219,900	$ -	$ -	$ -
Permit/lease on mineral property	$ 656,801	$ 67,800	$ 75,838	$ 67,300	$ 445,863
Project contracts	$ 1,290,511	$ 1,290,511	$ -	$ -	$ -
Feasibility/environmental studies	$ 391,859	$ 391,859	$ -	$ -	$ -
Total	$ 3,812,874	$ 3,223,873	$ 75,838	$ 67,300	$ 445,863

Professional services contracts are in place for various technical, geological, environmental, engineering and consulting services. The Company entered into a drilling contract that requires a minimum commitment of 100 operating days to be completed by August 12, 2012. If the Company fails to meet that commitment they are required to pay the drilling company $950,000.

CRITICAL ACCOUNTING ESTIMATES

The preparation of financial statements in accordance with IFRS requires management to make estimates and assumptions that affect the reported amount of assets, liabilities and expenses. The Company evaluates the estimates periodically. In making judgments about the carrying values, the Company uses estimates based on historical experience and various assumptions that are considered reasonable in the circumstances. Actual results may differ from those reported. The Company reviews significant areas subject to estimation with the Audit Committee. Significant areas requiring estimate include the determination of impairment of assets, mineral properties and capital assets, the related depletion and depreciation and the calculation of share-based payments. See note 2 to the December 31, 2011 financial statements.

Stage of development

The Company is in the early development stage of its history and at this stage of the Company's growth, it is subject to the risks associated with early stage companies, including uncertainty of future revenues, developing acceptable markets and growth into established markets, profitability and the need to raise additional financing to continue to progress its Project.

Continued exploration and development of the Property is dependent on Karnalyte's ability to obtain necessary financing. As the Company is not currently producing from its property, it will be necessary for the Company to seek additional equity or debt to finance its programs.

Intangible assets

The Company's expenditures relating to the acquisition of mineral properties, leases, permits and the exploration and development thereon are recorded at cost and include direct and indirect acquisition and exploration costs associated with specific mineral properties. These costs are capitalized on the basis of

the potential realization from the underlying asset. Amortization of these amounts will be recognized using the unit-of-production method over shorter of estimates of reserves or service life following the commencement of production or written off, if the properties are sold or abandoned.

The Company reviews capitalized amounts for impairment whenever events or changes in circumstances indicate its carrying amount may not be recoverable. The carrying value of assets is assessed for indications that the carrying amounts recorded may not be recoverable from estimated current and future cash flows. Estimating future cash flows requires assumptions about future business conditions and other developments. Significant, unanticipated changes to these assumptions could require a provision for impairment in the future.

Upon indication that impairment may exist, carrying values of assets would be adjusted. Impairment conditions may result from any of the following items, but not limited to: cessation of exploration activities; exploration results are not promising such that exploration will not be planned for the foreseeable future; permit or lease ownership rights expire; sufficient funding is not expected to be available to complete the exploration program; an exploration property is deemed to have no material economic value to the Company's business plan or future development of the property becomes uneconomical.

Share-based payments

The Company has share-based payments expenses for stock option awards to employee, directors, officers and consultants, as explained in the Company's financial statements. IFRS requires that all share-based awards be accounted for using the fair value method. Under this method, the Black-Scholes option pricing model requires estimates of the expected life of the option, forfeiture rates, stock volatility and the risk-free interest rate expected over the life of the option. A change in these assumptions could materially change the amount of share-based payments expenses recorded.

Income taxes

The Company accounts for income taxes in accordance with the asset and liability method. Under this method, deferred income tax assets and liabilities are recognized for differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using substantively enacted income tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred income tax assets and liabilities of a change in income tax rates is recognized in the period that includes the date of substantive enactment. A deferred income tax asset is recognized only when it is more likely than not that the income tax asset will be realized.

FINANCIAL RISK FACTORS

Credit risk

Credit risk is the risk of an unexpected loss if a customer or third party to a financial instrument fails to meet its commercial obligations. The Company has no significant concentration of credit risk arising from operations. The Company's cash and restricted cash is held with large Canadian financial institutions and management believes the risk of loss to be remote. As at March 31, 2012 and 2011, the Company had GST receivables from the Canadian Government and a limited number of customers who rent mats on a short-term basis such that management believes that the credit risk with respect to receivables is low.

Liquidity risk

The Company manages liquidity risk by maintaining sufficient cash and investment balances to meet liabilities when due. As at March 31, 2012, the Company had cash totalling $32,032,143 to settle current liabilities of $1,253,803. As at March 31, 2012 and 2011 the Company's trade and other receivables were all considered current and are subject to normal trade terms.

Market risk

Market risk is the risk that the value of a financial instrument will fluctuate as a result of changes in market prices, whether those changes are caused by factors specific to the individual instrument or its issuer or factors affecting all instruments traded in the market. The Company will be exposed to price risk with respect to North American and international potash prices. A significant decrease in the price of potash could cause the continued exploration and future development of the Company's properties to be uneconomical.

Currency risk

The Company's functional currency is the Canadian dollar with the majority of transactions denominated in Canadian dollars. The Company has engaged third party experts to perform various reports on the future potential of its mineral properties where such contracts are denominated in United States dollars and Euros. Management believes the foreign exchange risk derived from currency conversions is not significant and therefore does not hedge its foreign exchange risk.

Interest rate risk

The Company's trade and other payables are non-interest bearing and have contractual maturities of less than 45 days. As at March 31, 2012, the Company's only interest bearing asset is cash in high interest saving accounts. Cash earns interest at prevailing short-term interest rates. During the period ended March 31, 2012 the Company earned interest income of $117,775 from its cash.

RECENT ACCOUNTING PRONOUNCEMENTS

For information on changes in accounting policies and the impact of accounting standards not yet adopted please refer to the section titled "Recent Accounting Pronouncement" in the annual Management's Discussion & Analysis dated December 31, 2011.

INTERNAL CONTROL OVER FINANCIAL REPORTING (ICFR)

The Company has designed and implemented disclosure controls and procedures and internal controls over financial reporting. In the section titled "Disclosure Controls & Procedures and Internal Control over Financial Reporting" of its annual Management's Discussion & Analysis dated December 31, 2011, the Company reported certain material weaknesses in internal controls over financial reporting as at December 31, 2011. There have been no changes during the period ended March 31, 2012 that have a material effect on the disclosure controls and procedures or the internal controls over financial reporting.

OFF BALANCE SHEET ARRANGEMENTS

The Company has no off balance sheet arrangements at the time of this MD&A.

OUTSTANDING SHARES

As of the date of this MD&A, the Company has 21,551,736 common shares, 368,528 warrants and 1,050,500 stock options issued and outstanding.

OUTLOOK

Industry Outlook

World-wide demand for potash has been volatile in the recent past with some major producers implementing short term plant shut downs to manage supply into the marketplace. This strategy is being effective in maintaining potash prices at least in the short term. The Company sees this current situation as temporary however and anticipates the market to revert back to one of future growth. Population growth and the erosion of arable land are the key factors that the Company believes will fuel future potash demand. The Company expects global fertilizer demand to continue to increase due to the expectations from this growing population base with the need to supplement soils to meet the growing demand. Potash prices are expected to see strength in the long-term as companies attempt to meet this demand.

Company Outlook

Through the first quarter of 2012, the Company responded to the comments of securities commissions and as a result, filed an Amended and Restated Technical Report on March 30, 2012. Subsequent to this filing the Company has resumed its strategy of progressing the Project into construction. The Company still anticipates the engineering and construction phase of the Wynyard Carnallite Project to commence in the second quarter of 2012.

The Company is continuing to work with the Government of Saskatchewan and its consultants to address questions and comments on the Environmental Impact Statement ("EIS") and expects to achieve environmental approval during the third quarter 2012.

The Company continues to pursue a strategic partnership to assist with the equity requirements of the Project. Discussions with potential partners are ongoing.

With the filing of the Amended and Restated Technical Report, the Company has decided to move ahead on preparing the organization for the next phase of detailed engineering and construction. The Company has secured office space in Saskatoon, Saskatchewan that will serve as the base for the Company's engineering team through the next phases of development. In addition, the Company is currently in the process of hiring an engineering team that will staff this office. Upon hiring of these engineers, the Company will begin detailed engineering functions in conjunction with its engineering consultant partners.

As the Company is in the pre-development stage, access to capital markets is critical to the progression of the Wynyard Carnallite Project. The Company continues to pursue debt and/or equity financing to obtain the total funding required for the Project. Karnalyte is confident it has adequate access to capital for the near- and medium-term development of the initial phase of plant construction.

The Company will continue to focus on the following key initiatives;

- Pursuing a strategic partnership for potential project financing, off-take arrangements and/or marketing assistance;
- Completing its pre-feasibility level study on production and marketing of magnesium compounds;
- Hiring of internal engineering staff for detailed engineering activities and commencement of operations at its Saskatoon office;
- Working with the government of Saskatchewan to obtain the environmental approvals required for construction;
- Pursuing debt and/or equity financing to obtain the total funding required to bring the Project forward to plant and mine construction; and
- Optimizing product quality in cooperation with machinery and equipment suppliers.

FORWARD-LOOKING INFORMATION

Statements in this MD&A may constitute "forward-looking" statements which involve known and unknown risks, uncertainties and other factors which may cause the actual results, performance or achievements of the Company, or industry results, to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. Forward-looking statements may include, but are not limited to, statements regarding:

- future extraction and exploitation of mineral deposits;
- capital expenditure requirements;
- expectations regarding prices and costs;
- development of mineral resources and mineral extraction processes;
- the Company spending the funds available to it as stated in this MD&A;
- expectations regarding the Company's ability to subsequently raise capital;
- expenditures to be made by the Company to meet certain work commitments;
- work plans to be conducted by the Company; and
- reclamation and rehabilitation obligations and liabilities.

In certain cases, forward-looking statements can be identified by the use of such words as "may", "would", "could", "will", "intend", "expect", "believe", "plan", "anticipate", "estimate" and other similar terminology. These statements reflect the Company's current expectations regarding future events and operating performance and speak only as of the date of this MD&A.

Forward-looking statements in this MD&A include statements regarding:

- the Company's ability to commence production at 625,000 tonnes per year, and ramp up to production of 2.125 million tonnes per year;
- further seismic exploration and drilling;
- time to completion of plant construction of 18 to 24 months following receipt of satisfactory financing and regulatory approvals;
- brine field preparation taking between 24 and 30 months;
- production run rates achieving 625,000 tonnes per year within 10 months following the completion of the processing plant;

- total capital expenditure for a 625,000 tonne mine of $589 million;
- anticipated results of development and extraction activities and estimated future development, and
- the Company's ability to obtain additional financing on satisfactory terms.

Such forward-looking statements are based on a number of material factors and assumptions, including, that:

- the Company executes its project development plans in a manner consistent with its budgets and planning;
- studies to support the Company's current development plans, and
- the Company obtains additional financing in the future.

Forward-looking statements involve significant risks and uncertainties, should not be read as guarantees of future performance or results, and will not necessarily be accurate indications of whether or not such results will be achieved. A number of factors could cause actual results to differ materially from the results discussed in the forward-looking statements, including, but not limited to, the factors discussed under "Financial Risk Factors" elsewhere in this MD&A and under "Risk Factors" in the Company's Annual Information Form. Although the forward-looking statements contained in this MD&A are based upon what management of the Company believes are reasonable assumptions, the Company cannot assure investors that actual results will be consistent with these forward-looking statements. These forward-looking statements are made as of the date of this MD&A and are expressly qualified in their entirety by this cautionary statement. Subject to applicable securities laws, the Company assumes no obligation to update or revise them to reflect new events or circumstances.