



DIA BRAS EXPLORATION INC.
(An Exploration-Stage Company)

Consolidated Financial Statements

Year ended December 31, 2006
and
Nine-month period ended December 31, 2005

April 27, 2007

Auditor's report

To the Shareholders of Dia Bras Exploration Inc.

We have audited the consolidated balance sheets of **Dia Bras Exploration Inc.** as at December 31, 2006 and 2005 and the consolidated statements of operations and deficit and cash flows for the year and the nine-month period then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2006 and 2005 and the results of its operations and its cash flows for the year and nine-month period then ended in accordance with Canadian generally accepted accounting principles.

PricewaterhouseCoopers LLP

Chartered Accountants

Dia Bras Exploration Inc.

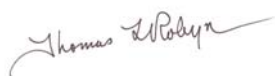
(an exploration-stage company)

Consolidated Balance Sheets

As at December 31, 2006 and 2005

	2006 \$	2005 \$
Assets		
Current assets		
Cash and cash equivalents	19,704,587	3,556,961
Receivables (note 4)	3,347,046	327,000
Sales tax and other receivables	3,981,826	1,037,122
Inventories from pilot-mining program (note 5)	471,981	142,239
Temporary investment (note 6)	340,000	42
Prepaid expenses	20,168	94,048
Future income tax assets	758,402	-
	<u>28,624,010</u>	<u>5,157,412</u>
Mining assets (note 7)	24,126,921	19,912,804
Deferred costs – Advance on royalty payment (note 8)	-	350,000
	<u>52,750,931</u>	<u>25,420,216</u>
Liabilities		
Current liabilities		
Accounts payable and accrued liabilities	830,978	749,676
Income taxes payable (note 14)	57,425	45,000
Current portion of obligation related to assets under capital lease (note 9)	-	90,904
	<u>888,403</u>	<u>885,580</u>
Obligation related to assets under capital lease (note 9)	-	137,947
Excess cost recovery – pilot mining (note 7 (a) (i))	6,770,293	-
Future income tax liabilities (note 14)	727,765	397,600
	<u>8,386,461</u>	<u>1,421,127</u>
Shareholders' Equity		
Share capital (note 10)	51,308,067	26,921,601
Warrants and compensation options (note 11)	193,603	2,880,496
Contributed surplus (note 13)	6,590,223	4,802,240
Deficit	<u>(13,727,423)</u>	<u>(10,605,248)</u>
	<u>44,364,470</u>	<u>23,999,089</u>
	<u>52,750,931</u>	<u>25,420,216</u>
Commitments and Contingency (notes 18 and 19)		

Approved by the Board of Directors,



Thomas L. Robyn, Director



Philip Renaud, Director

Dia Bras Exploration Inc.

(an exploration-stage company)

Consolidated Statements of Operations and Deficit

	For the year ended December 31, 2006 \$	For the nine-month period ended December 31, 2005 \$
Income		
Interest income	277,440	19,904
Gain on disposal of temporary investment (note 6)	152,800	26,218
Net gain on currency exchange	289,784	36,895
Miscellaneous revenues	5,000	-
	<u>725,024</u>	<u>83,017</u>
Expenses		
Administrative expenses	631,131	371,123
Professional and consulting fees	341,017	194,926
Information to shareholders and trustee fees	227,358	193,382
Investor relations and corporate development	395,968	50,586
Stock-based compensation costs (note 12)	694,846	249,808
Interest on obligation related to assets under capital lease	48,898	3,396
Other project costs	29,069	-
Loss on disposal of mining assets – Land, exploration buildings and equipment	10,448	-
Write-off of mining assets – Costs and deferred exploration expenses and deposits on mining assets (note 7(a) (iii), (v) and (vi))	280,117	557,588
Write-off of mining assets – Land, exploration buildings and equipment	-	58,070
Write-off of deferred costs – Advance on royalty payment (note 8)	350,000	-
Write-down of temporary investment	-	18,333
Amortization of property, plant and equipment	-	12,268
Amortization of intangible asset – Licence	-	27,102
	<u>3,008,852</u>	<u>1,736,582</u>
Loss before income taxes for the period	<u>(2,283,828)</u>	<u>(1,653,565)</u>
Income tax provision (recovery) (note 14)		
Current	57,425	45,000
Future	(428,237)	397,600
	<u>(370,812)</u>	<u>442,600</u>
Loss for the period	<u>(1,913,016)</u>	<u>(2,096,165)</u>
Deficit – Beginning of period	(10,605,248)	(8,468,556)
Share and warrant issue expenses	(1,209,159)	(40,527)
Deficit – End of period	<u>(13,727,423)</u>	<u>(10,605,248)</u>
Basic and diluted loss per share	<u>(0.02)</u>	<u>(0.04)</u>
Basic and diluted weighted average number of outstanding shares	<u>89,634,481</u>	<u>58,376,171</u>

Dia Bras Exploration Inc.
(an exploration-stage company)
Consolidated Statements of Cash Flows

	For the year ended December 31, 2006 \$	For the nine-month period ended December 31, 2005 \$
Cash flows from		
Operating activities		
Loss for the period	(1,913,016)	(2,096,165)
Adjustments for		
Future income taxes (note 14)	(428,237)	397,600
Gain on disposal of temporary investment (note 6)	(152,800)	(26,218)
Stock-based compensation costs (note 12)	694,846	249,808
Loss on disposal of mining assets	10,448	-
Write-off of mining assets – Costs and deferred exploration expenses (note 7 (a) (iii), (v) and (vi))	280,117	557,588
Write-off of deferred costs – Advance on royalty payment (note 8)	350,000	-
Write-down of temporary investment	-	18,333
Write-off of mining assets – Land, exploration buildings and equipment	-	58,070
Amortization of property, plant and equipment	-	12,268
Amortization of intangible asset – Licence	-	27,102
Unrealized loss on currency exchange	-	6,239
	<u>(1,158,642)</u>	<u>(795,375)</u>
Changes in non-cash working capital items (note 16)	(3,089,719)	(705,899)
	<u>(4,248,361)</u>	<u>(1,501,274)</u>
Financing activities		
Payment of obligation related to assets under capital lease (note 9)	(228,851)	(10,846)
Issuance of share capital (note 10)	20,829,934	5,820,439
Share and warrant issue expenses	(1,015,556)	(40,527)
Short-term loan	-	582,618
Reimbursement of short-term loan	-	(582,618)
	<u>19,585,527</u>	<u>5,769,066</u>
Investing activities		
Increase in mining assets	(31,595,096)	(9,184,506)
Sales of concentrate	32,568,792	5,235,402
Acquisition of temporary investment (note 6)	(600,000)	-
Disposal of temporary investment (note 6)	412,842	254,510
Disposal of mining assets	23,922	18,373
Disposal of property, plant and equipment	-	1,759
	<u>810,460</u>	<u>(3,674,462)</u>
Translation adjustments on cash and cash equivalents	-	(6,239)
Increase in cash and cash equivalents during the period	16,147,626	587,091
Cash and cash equivalents – Beginning of period	<u>3,556,961</u>	<u>2,969,870</u>
Cash and cash equivalents – End of period	<u>19,704,587</u>	<u>3,556,961</u>

Dia Bras Exploration Inc.

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Notes to Consolidated Financial Statements

As at December 31, 2006 and 2005

and for the year ended December 31, 2006 and the nine-month period ended December 31, 2005

1 Nature of operations

Dia Bras Exploration Inc. (the “Company”), an exploration-stage company, was incorporated under the *Canada Business Corporations Act* on April 11, 1996.

The Company has mining rights and options to acquire interests in mining properties located in the State of Chihuahua, Mexico, which are presently at the exploration stage. Until it is determined that the properties contain mineral reserves or resources that can be economically mined, they are classified as mining properties. The economic viability of these mining properties has not yet been assessed. The recoverability of costs relating to the mining properties, including deferred exploration expenses, is dependent upon the discovery of economically recoverable reserves and resources, confirmation of the Company’s interest in the underlying mineral claims, the ability of the Company to obtain the necessary financing to complete the development and construction of processing facilities, as well as future profitable production or, alternatively, upon disposal of such properties at an amount equal to the Company’s investment therein.

In 2005, the Company began a pilot-mining program at the Bolivar Mine property in order to gather information and data in view of a pre-feasibility study. However, the Company has not yet reached the commercial production stage.

In accordance with industry standards for properties at that stage of exploration, the Company has taken reasonable measures to ensure proper title to its properties. However, there is no guarantee that title to any of its properties will not be challenged or impugned. The Company’s properties may be subject to prior unregistered agreements or transfers, and title may be affected, among other things, by undetected defects.

In 2005, the Company changed its year-end from March 31st to December 31st.

2 Significant accounting policies

Basis of consolidation

These consolidated financial statements include the accounts of the Company and its wholly owned foreign subsidiaries, Dia Bras Mexicana S. de R.L. de C.V., Servicios de Minería de la Sierra S. de R.L. de C.V., and Nichromex S. de R.L. de C.V.

Asesores Administrativos y Recursos Humanos S. de R.L. de C.V. and Compañía Minera Metalúrgica Malpaso S. de R.L. de M.I. are consolidated in the accounts of the Company as they are variable interest entities (“VIE”) and the Company is the primary beneficiary of these two entities.

Dia Bras Exploration Inc.

(an exploration-stage company)

Notes to Consolidated Financial Statements

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Use of estimates

The preparation of financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Significant areas where management judgment is applied are allowance for doubtful accounts, mining asset valuations, contingent liabilities, and future income taxes. Actual results could differ from those estimates, and such differences could be material.

Cash and cash equivalents

Cash and cash equivalents consist of bank balances and interest-bearing, short-term liquid investments repurchasable at all times without penalties.

Temporary investment

The temporary investment is recorded at the lower of cost and quoted market value.

Inventories from pilot mining

Inventories from pilot mining consist of material and concentrate located at the plant and are recorded at the lower of cost and net realizable value.

Mining assets

Mining assets include mining rights and options to acquire interests in mining properties, deferred exploration expenses, land, exploration buildings and equipment, supplies inventory that will be used for exploration, and deposits on future mining assets. All costs directly related to foreign projects are capitalized.

Costs and deferred exploration expenses

Costs and exploration expenses are deferred until the economic viability of the project has been established, at which time costs are added to property, plant and equipment. Costs are written off when properties are abandoned or when cost recovery is uncertain. Management has defined uncertainty as either there being no financial resources available for development over a period of three consecutive years or results from exploration work not warranting further investment.

Proceeds from the sale of a mining asset are applied against related carrying costs, and any excess is reflected as a gain in the Consolidated Statements of Operations and Deficit. In the case of a partial sale, if carrying costs exceed the proceeds, only the loss is reflected.

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Notes to Consolidated Financial Statements

As at December 31, 2006 and 2005

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Revenue from sales of concentrate from a pilot-mining program prior to commencement of commercial production is recorded as a reduction of the related costs and deferred exploration expenses and is recognized when the following conditions are met:

- ♦ persuasive evidence of an arrangement exists;
- ♦ delivery has occurred under the terms of the arrangement;
- ♦ the price is fixed or determinable; and
- ♦ collection is reasonably assured.

The Company's concentrate is sold under pricing arrangements whereby final settlement prices are determined by quoted market prices in a period subsequent to the date of sale. The concentrate is provisionally priced at the time of sale based on forward prices for the expected date of the final settlement. Subsequent variations of the price are recognized as sales adjustments as they occur and until the price is settled.

If the accumulated revenue from sales of concentrate from the pilot-mining program exceeds the related costs and deferred exploration costs, then the excess cost recovery is included in long-term liabilities until (i) the situation is reversed, or (ii) commercial production has begun at which time it will be netted against construction costs, if any, of the new facilities, or (iii) the property is abandoned.

The Company expects commercial production on the Bolivar project to commence no later than the end of 2009. Commercial production has been defined as being the stage where the Company reaches a production level of 65% of mill capacity for a consecutive period of 90 days within a maximum period of six months. The production level will be calculated on the rated capacity of an on-site mill.

The development of the mine and the construction of the on-site mill are planned to commence in mid-2008 after reception of a bankable feasibility study to be commissioned in 2007.

Land, exploration buildings and equipment

Land, exploration buildings and equipment are recorded at cost.

Amortization of exploration buildings and equipment is capitalized as deferred exploration expenses when related to a specific project. Amortization is computed using the following methods and rates or period:

	Method	Rate/Period
Buildings	Declining balance	10%
Equipment and rolling stock	Declining balance	30%
Computers and office furniture	Straight-line	3 years

Supplies inventory

Supplies inventory is recorded at the lower of cost and replacement value.

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Notes to Consolidated Financial Statements

As at December 31, 2006 and 2005

and for the year ended December 31, 2006 and the nine-month period ended December 31, 2005

Deferred costs – Advance on royalty payment

Deferred costs in reference to the Nichromet licence as at December 31, 2005 were recorded at cost. They were to be expensed as royalty payments on mineral production on properties covered by the agreement using the Nichromet technology, on the basis of a 1% net smelter return royalty, or written off upon non-performance of the Company's obligations or upon its decision not to use the license. The license was written off during the year ended December 31, 2006.

Stock option plan and stock-based compensation costs

The Company applies the fair value method to account for options granted to its employees, officers, directors and consultants. Any consideration paid on exercise of stock options is credited to share capital. The stock-based compensation cost is stated as per the periods of option vesting. The contributed surplus resulting from the stock-based compensation is transferred to share capital when the options are exercised.

Foreign currency translation

Foreign currency

Monetary assets and liabilities in foreign currencies are remeasured into Canadian dollars at the exchange rates in effect at the balance sheet date. Other assets and liabilities as well as items from the Consolidated Statements of Operations and Deficit are remeasured at the rates of exchange in effect on each transaction date. Gains and losses resulting from remeasurement are reflected in the Consolidated Statements of Operations and Deficit.

Foreign operations

The Company's subsidiaries and consolidated VIEs are considered to be integrated. As a result, the accounts of the subsidiaries and VIEs are remeasured into the functional currency using the temporal method. Under this method, monetary assets and liabilities are remeasured at the exchange rates in effect at the balance sheet date. Non-monetary assets and liabilities are remeasured at the historical rates. Revenues and expenses are remeasured at the average rates for the periods. Gains and losses resulting from remeasurement are reflected in the Consolidated Statements of Operations and Deficit.

Income taxes

The Company provides for income taxes using the liability method of tax allocation. Under this method, future income tax assets and liabilities are determined based on deductible or taxable temporary differences between the accounting and tax bases of assets and liabilities using substantively enacted income tax rates expected to be in effect in the fiscal year in which the differences are expected to reverse.

The Company establishes a valuation allowance against future income tax assets when, from available information, it is more likely than not that some or all of such assets will not be realized.

Share and warrant issue expenses

Share and warrant issue expenses are accounted for in the period in which they are incurred and recorded as an increase in deficit in the period in which the shares are issued.

Dia Bras Exploration Inc.

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Notes to Consolidated Financial Statements

As at December 31, 2006 and 2005

and for the year ended December 31, 2006 and the nine-month period ended December 31, 2005

Earnings (loss) per share

Earnings (loss) per share are calculated using the weighted average number of shares outstanding during the year. Diluted earnings (loss) per share are calculated using the weighted average number of shares outstanding during the year based on the application of the treasury stock method for the calculation of the dilutive effect of stock options and other dilutive securities.

The diluted loss per share is equal to the basic loss per share due to the antidilutive effect of the stock options and other dilutive securities.

Asset retirement obligations

Asset retirement obligations are recognized at fair value in the period in which the Company incurs a legal obligation associated to the retirement of an asset. The associated costs are capitalized as part of the carrying value of the related asset and amortized over its remaining useful life. The liability is accreted using a credit-adjusted, risk-free interest rate.

3 Financial instruments

Fair value

The Company has determined the estimated fair value of its financial instruments based on estimates and assumptions. The actual results may differ from those estimates, and the use of different assumptions or methodologies may have material effects on the estimated fair value amounts.

The fair value of cash and cash equivalents, receivables, sales tax and other receivables and accounts payable and accrued liabilities is comparable to their carrying value due to the relative short period to maturity of the instruments.

Interest rate risk

The Company's receivables, sales tax and other receivables, and accounts payable and accrued liabilities are non-interest bearing. Cash and cash equivalents bear interest at variable and fixed rates.

Foreign exchange risk

The Company's sales of concentrate and part of its purchases are denominated in foreign currencies, primarily in U.S. dollars and Mexican pesos. Consequently, certain assets and liabilities namely, cash and cash equivalents, receivables, sales tax and other receivables, accounts payable and accrued liabilities, as well as certain revenues and expenses, include amounts that are exposed to currency fluctuations.

Dia Bras Exploration Inc.

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As at December 31, 2006 and 2005

and for the year ended December 31, 2006 and the nine-month period ended December 31, 2005

Credit risk

The Company is subject to concentrations of credit risk through cash and cash equivalents, receivables, and sales tax and other receivables. The Corporation maintains substantially all of its cash and cash equivalents with major financial institutions in Canada and in Mexico. Therefore, credit risk of counterparty non-performance is remote. The totality of the Company's receivables is with a sole client and is subject to normal credit risks. The totality of sales tax receivable is with the Government of Mexico, and, as such, management believes it also represents a normal credit risk.

Commodity price risk

The Company is exposed to commodity price risk for variations in concentrate prices, as final prices are determined by quoted market price in a period subsequent to the date of sale. The Company does not use derivative instruments to mitigate this risk.

4 Receivables

The Company's receivables are detailed as follows:

	As at December 31,	
	2006	2005
	\$	\$
Receivables from pilot-mining ⁽ⁱ⁾	1,568,683	-
Provision for final settlement ⁽ⁱⁱ⁾	1,778,363	327,000
	<u>3,347,046</u>	<u>327,000</u>

⁽ⁱ⁾ Receivables have been collected subsequent to year-end.

⁽ⁱⁱ⁾ The provision for final settlement represents the estimated amount to be recovered as at December 31, 2006 on shipments of concentrate for which the Company received provisional payments of approximately 90% at the date of shipment. Shipments which have not reached final settlement stage as at December 31, 2006 comprise approximately 7,430 tonnes of zinc concentrate and 4,090 tonnes of copper concentrate for which sales were valued at their forward price at year-end of US\$1,494/t and US\$1,585/t, respectively. These amounts do not take into account any changes in price after year-end, and therefore the realization value will differ when final settlement occurs.

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Notes to Consolidated Financial Statements

As at December 31, 2006 and 2005

and for the year ended December 31, 2006 and the nine-month period ended December 31, 2005

5 Inventories from the pilot-mining program

	As at December 31,	
	2006	2005
	\$	\$
Material	10,928	83,921
Concentrate	461,053	58,318
	<hr/>	<hr/>
	471,981	142,239
	<hr/>	<hr/>

6 Temporary investment

	As at December 31,	
	2006	2005
	\$	\$
Pershimco Resources Inc. ("Pershimco") (a) 850,000 common shares and 850,000 warrants – Quoted market value of \$501,500 as at December 31, 2006	340,000	-
Ecu Silver Mining Inc. (b) (as at December 31, 2005 – 166 common shares and 666,666 warrants – quoted market value of the common shares was \$73)	-	42
	<hr/>	<hr/>
	340,000	42
	<hr/>	<hr/>

(a) Pursuant to the provisions of the Pershimco Agreement, the Company acquired, in November 2006, 850,000 units of Pershimco at \$0.40 per unit, for a total amount of \$340,000. Each unit is comprised of one common share of Pershimco and one common share purchase warrant entitling the holder thereof to subscribe for one additional common share of Pershimco at a price of \$0.40 during a period of 12 months after the closing.

(b) As at December 31, 2005, the Company owned 666,666 warrants of Ecu Silver Inc. exercisable at a price of \$0.39 per warrant. During the year ended December 31, 2006, the Company exercised all the warrants for \$260,000 and disposed of all the shares for a total consideration of \$412,842, thereby realizing a gain on disposal of \$152,800.

Dia Bras Exploration Inc.

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Notes to Consolidated Financial Statements

As at December 31, 2006 and 2005

and for the year ended December 31, 2006 and the nine-month period ended December 31, 2005

7 Mining assets

	As at December 31,	
	2006	2005
	\$	\$
Costs and deferred exploration expenses (a)	11,672,155	13,537,347
Land, exploration buildings and equipment (b)	10,446,092	4,979,639
Supplies inventory	1,366,801	1,119,116
Deposits on mining assets	641,873	276,702
	24,126,921	19,912,804

(a) Costs and deferred exploration expenses

	Costs		Deferred exploration expenses		Total	
	As at December 31,		As at December 31,		As at December 31,	
	2006	2005	2006	2005	2006	2005
	\$	\$	\$	\$	\$	\$
Mexico (State of Chihuahua)						
Bolivar projects (options)						
Bolivar Mine* (i) (note 19)	-	1,433,381	-	7,858,922	-	9,292,303
Piedras Verdes (ii)	313,102	301,828	2,073,771	2,072,362	2,386,873	2,374,190
San José (iii)	141,288	74,864	271,504	271,504	412,792	346,368
Mezquital	27,299	24,495	99,105	99,105	126,404	123,600
La Cascada	10,110	8,282	133,577	133,577	143,687	141,859
Val	2,684	2,560	100,928	100,928	103,612	103,488
Other	68,860	27,158	43,564	33,714	112,424	60,872
Promontorio projects (options)						
Promontorio and Hidalgo (iv)	249,425	135,702	948,505	811,330	1,197,930	947,032
El Magistral (v)	-	147,635	-	-	-	147,635
Cusi projects (vii)						
India – Marisa (a)	239,997	-	1,667,335	-	2,002,617	-
Holguin – San Juan (b)	1,463,823	-	-	-	1,368,538	-
San Miguel – La Bamba (c) (option)	221,285	-	1,204,497	-	1,425,782	-
Mineria Cusi – Santa Edwiges/San Nicolas (d) (option)	1,127,048	-	1,254,744	-	2,381,792	-
DBM	4,269	-	5,435	-	9,704	-
	3,869,190	2,155,905	7,802,965	11,381,442	11,672,155	13,537,347

	Costs		Deferred exploration expenses		Total	
	As at December 31,		As at December 31,		As at December 31,	
	2006	2005	2006	2005	2006	2005
	\$	\$	\$	\$	\$	\$

*Bolivar Mine

Costs and deferred exploration expenses	1,630,929	1,433,381	32,750,018	13,421,324	34,380,947	14,854,705
Less: Accumulated sales of concentrate	(1,630,929)	-	(39,520,311)	(5,562,402)	(41,151,240)	(5,562,402)
Less: Transfer to excess cost recovery – pilot mining	-	1,433,381	(6,770,293)	7,858,922	(6,770,293)	9,292,303
	-	-	6,770,293	-	6,770,293	-
	-	1,433,381	-	7,858,922	-	9,292,303

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Notes to Consolidated Financial Statements

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(i) Bolivar Mine

In August 2004, the Company entered into a commercial agreement with the owners of the Bolivar Mine property (Bolivar III and Bolivar IV). The agreement provides for the acquisition by the Company of 100% of the Bolivar Mine property for a consideration of US\$1,200,000 payable over a two-year period. The remaining payment of \$189,313⁽¹⁾ (US\$162,500) has yet to be made.

During the year ended December 31, 2006, the Company continued its pilot-mining program on the Bolivar Mine property. During that period, the Company sold zinc and copper concentrate in the amount of \$35,588,838 (for the nine-month period ended December 31, 2005 – \$5,562,402). In accordance with the Company's accounting policy, the income from sales of concentrate prior to the commencement of commercial production is accounted for as a reduction of related costs and deferred exploration expenses. Consequently, the \$6,770,293 excess cost and deferred accumulated exploration expense recovery on the Bolivar Mine property is shown as a long-term liability on the Consolidated Balance Sheets.

(ii) Piedras Verdes

During the year ended March 31, 2004, the Company entered into an option agreement to acquire a 100% interest in the Piedras Verdes property for a cash consideration of US\$200,000 payable over a two-year period. The remaining payment of \$23,300⁽¹⁾ (US\$20,000) will be made at the time of transfer of the property titles.

(iii) Santa María and San José projects

In July 2003, the Company entered into an option agreement with El Paso Partners, Ltd. ("EPP") to acquire a cumulative interest of up to 100% in the Santa María and San José, silver and base metal properties by incurring exploration expenditures of US\$4,000,000.

In December 2005, the Company decided to abandon the Santa María project. Therefore, no further payment will be made. Consequently, the Company recorded, during the nine-month period ended December 31, 2005, a write-off of mining assets of \$403,152.

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The remaining payments for the San José project, as at December 31, 2006, are as follows:

	<u>Equivalent in C\$</u>	<u>Payments in US\$</u>
January 2007	43,687 ⁽¹⁾	37,500
July 2007	43,687 ⁽¹⁾	37,500
January 2008	43,687 ⁽¹⁾	37,500

Starting July 2008, the Company will pay a yearly advance royalty payment of \$72,811⁽¹⁾ (US\$62,500).

(iv) Promontorio and Hidalgo properties

In May 2004, the Company entered into a purchase option agreement whereby it could earn a 100% interest in the Promontorio and Hidalgo properties by paying the vendors a total of US\$3,000,000. The remaining payments are as follows:

	<u>Equivalent in C\$</u>	<u>Payments in US\$</u>
June 2007	174,750 ⁽¹⁾	150,000
June 2008	174,750 ⁽¹⁾	150,000
June 2009	2,912,500 ⁽¹⁾	2,500,000

(v) El Magistral

In November 2004, the Company entered into a purchase option agreement whereby the Company could purchase a 100% interest in the El Magistral property for the sum of US\$1,000,000, payable over a five-year period, including US\$50,000 at the signing of the agreement.

In 2006, the Company decided to abandon the project and therefore did not make the November 2006 payment of \$87,375⁽¹⁾ (US\$75,000). Consequently, the Company wrote off the accumulated costs incurred of \$147,635.

(vi) El Cumbre

All costs and deferred exploration expenses allocated to this project amounting to \$154,436 were written off during the nine-month period ended December 31, 2005.

(vii) Cusi Project

In May and June, 2006, the Company staked ground and entered into agreements in order to earn interest in more than 7,500 hectares of contiguous property (the "Cusi Properties"), including 12 former mines, in the Cusihiuriachic ("Cusi") silver district in Chihuahua State, Mexico, located within 40 kilometres of the Company's Malpaso mill, as follows:

- (a) On May 2, 2006, the Company entered into a purchase agreement with Hector Sanchez Villalobos and Carmen Saenz Rodriguez ("Villalobos and Rodriguez") to acquire a property

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covering 21.08 hectares for a cash payment of US\$100,000 and the issue by the Company of 200,000 common shares of the Company at a price of \$0.64 per share for a total of \$128,000. The portion of the transaction payable in shares has been recorded at the fair value of the common shares issued, based on their quoted market value at the date of the transaction. The property is subject to a 1.5% NSR of up to a maximum of \$1,747,500⁽¹⁾ (US\$1,500,000) in favour of Villalobos and Rodriguez with a \$1,165,000⁽¹⁾ (US\$1,000,000) buy-back option.

- (b) On May 2, 2006, the Company entered into a purchase agreement with Manuel Holguin Aragonéz ("Holguin") to acquire properties covering 1,676 hectares for an aggregate cash payment of US\$740,000, and the issuance by the Company of 1,000,000 common shares of the Company at a price of \$0.64 per share for a total of \$640,000. The portion of the transaction payable in shares has been recorded at the fair value of the common shares issued, based on their quoted market value at the date of the transaction. The properties are subject to a 1.5% NSR of up to a maximum of \$1,747,500⁽¹⁾ (US\$1,500,000) in favour of Holguin. The NSR can be purchased for \$1,165,000⁽¹⁾ (US\$1,000,000). As at December 31, 2006, an amount of \$191,225⁽¹⁾ (US\$165,000) remains to be paid.
- (c) On May 31, 2006, the Company entered into an option agreement with Pershimco Resources Inc. ("Pershimco") pursuant to which the Company could earn up to a 70% interest in the San Miguel-La Bamba property covering 36 hectares located in the Cusi District owned by Pershimco by making a cash payment of US\$200,000 and fulfilling work commitments as follows:

Equivalent in C\$	Work commitment in US\$	Cumulative interest earned %	Period
1,747,500 ⁽¹⁾	1,500,000	50	until May 31, 2007
2,912,500 ⁽¹⁾	2,500,000	20	until November 30, 2008
<u>4,660,000</u>	<u>4,000,000</u>	<u>70</u>	

The property is subject to a 2% NSR of which 1% may be bought back for \$1,165,000⁽¹⁾ (US\$1,000,000).

- (d) On June 14, 2006, the Company signed a letter of intent to enter into an option agreement to earn a 100% interest in several properties (883 hectares) with Compañía Minera Cusi ("Minera Cusi"), a private Mexican company, for US\$5,000,000 payable over three years. The properties are subject to a sliding scale royalty in favour of Minera Cusi as follows: 2% NSR if the price of silver is equal to a maximum of \$12.82⁽¹⁾ (US\$11.00) per ounce or 3% NSR if the price of silver exceeds \$12.82⁽¹⁾ (US\$11.00) per ounce. The royalty is in favour of Minera Cusi. The Company may withdraw from its option agreement under the proposed acquisition, over the three-year period, by simple notice to Minera Cusi and the forfeiture of payments.

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In exchange for the control obtained of the common shares in CMMM, the Company advanced to the nominee, in the nine-month period ended December 31, 2005, an amount of \$417,409 and committed itself to an additional amount of \$233,180 (US\$200,000). This latter consideration was included in accounts payable and accrued liabilities as at December 31, 2005 and was fully paid in 2006.

All additions to original milling capacity have been made by Nichromex S. de R.L. de C.V., a wholly owned foreign subsidiary.

8 Deferred costs – Advance on royalty payment

On August 26, 2003, the Company acquired from Nichromet Extraction Inc., an unrelated entity, the rights of a licence for the use and marketing of a metallurgical extractive technology for Mexico in consideration for a 1% NSR payment on all mineral production using the technology from any of the Company's Mexican properties. As part of the agreement, the Company made a non-refundable royalty advance of \$350,000.

In addition, the agreement gave the Company the right to act as an agent for the purpose of sourcing the licence to third parties in Mexico. Any consideration received will be shared equally with Nichromet.

In 2005, following certain conditions, Nichromet agreed to extend the expiry date of the Nichromet licence to July 2008.

Although the license is still in effect as at December 31, 2006, the Company has no current plan to use this technology and therefore will not benefit economically from it. Consequently, the Company wrote off the deferred costs.

9 Obligation related to assets under capital lease

During the year, the Company paid off the amount due under capital lease. At December 31, 2006, there is no balance due.

(a) Future minimum payments required to satisfy payment terms under a capital lease in each of the next three years are as follows:

	As at December 31,	
	2006	2005
	\$	\$
Years ending December 31, 2006	-	130,166
2007	-	96,599
2008	-	66,569
	-	293,334
Less: Interest	-	64,483
Total liability (b)	-	228,851
Less: Current portion	-	90,904
	-	137,947

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- (b) As at December 31, 2005, the obligation in the amount of \$228,851 includes \$68,259 payable in US dollars (US\$59,355) and \$160,592 payable in Mexican pesos (MP\$1,461,369).

10 Share capital

Authorized

An unlimited number of common shares without par value

Issued

Changes in the Company's share capital were as follows:

	For the year ended December 31, 2006		For the nine-month period ended December 31, 2005	
	Number of shares	Amount \$	Number of shares	Amount \$
Balance – Beginning of period	81,724,769	26,921,601	51,457,477	20,782,703
Issued and paid in cash (i)	14,950,000	10,465,000	22,500,000	4,500,000
Issued for the acquisition of mining assets (note 7 (vii) (a) (b))	1,200,000	768,000	-	-
Issued following exercise of warrants ((ii) and note 11)	11,423,219	13,022,470	7,767,292	1,638,898
Issued following exercise of stock options (notes 12 and 13)	252,917	130,996	-	-
Balance – End of period	109,550,905	51,308,067	81,724,769	26,921,601

- (i) (a) On August 17, 2006, the Company closed an offering on a bought-deal basis of 13,000,000 common shares at a price of \$0.70 per common share, for gross proceeds of \$9,100,000. The underwriters for the offering also exercised their over-allotment options to purchase an additional 1,950,000 common shares at \$0.70 per common share for additional gross proceeds of \$1,365,000, raising the total gross proceeds of the offering to \$10,465,000.

As a commission, the Company paid a cash consideration of \$732,550 and issued to the agent 1,046,500 compensation options evaluated at \$193,603 (note 11). This amount is included in share and warrant issue expenses in the Consolidated Statements of Operations and Deficit under share and warrant issue expenses. The compensation options entitle the holder to subscribe for the same number of common shares at a price of \$1.00 per share until August 16, 2007.

The fair value of the compensation options was estimated using the Black-Scholes model based on the following assumptions:

Dividend yield	0%
Volatility	87.83%
Risk-free interest rate	4.33%
Expected life	1 year

As a result, the fair value of the compensation option was estimated at \$193,603.

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(b) In November 2005, the Company completed a series of private placements of common shares whereby the Company issued a total of 22,500,000 common shares at a price of \$0.20 per share for a total consideration of \$4,500,000.

(ii) (a) In November 2006, 11,423,219 warrants were exercised at the price of \$0.90, for a total cash consideration of \$10,280,897, including 1,100,067 warrants by directors and officers of the Company or company controlled by a director or officer of the Company for a total amount of \$990,060. Consequently, the Company issued 11,423,219 common shares.

(b) In September 2005, a total of 7,767,292 warrants entitling their holders to purchase 7,767,292 common shares at a price of \$0.17 per share were exercised for a total amount of \$1,320,439.

11 Warrants and compensation options

Changes in the Company's outstanding common share purchase warrants and compensation options were as follows:

	For the year ended December 31, 2006			For the nine-month period ended December 31, 2005	
	Number of warrants	Number of compensation options	Amount \$	Number of warrants	Amount \$
Balance – Beginning of period	12,002,068	-	2,880,496	29,125,399	6,165,776
Issued (note 10 (i) (a))	-	1,046,500	193,603	-	-
Exercised (note 10 (ii))	(11,423,219)	-	(2,741,573)	(7,767,292)	(318,459)
Expired (note 13)	(578,849)	-	(138,923)	(9,356,039)	(2,966,821)
Balance – End of period	-	1,046,500	193,603	12,002,068	2,880,496

A summary of outstanding compensation options, entitling their holders to subscribe for an equivalent number of common shares, as at December 31, 2006, is as follows:

Exercise price	Number of compensation options	Expiry date
\$1.00	1,046,500	August 16, 2007

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12 Stock option plan

The Company maintains a stock option plan (the "Plan") whereby the Board of Directors may, from time to time, grant to employees, officers, directors or consultants options to acquire common shares of the Company on such terms and at such exercise prices as may be determined by the Board. As of December 31, 2006, the Plan provides that: i) the maximum number of common shares in the capital of the Company that may be reserved for issuance under the Plan shall be equal to 9,700,000 (5,900,000 as of December 31, 2005) common shares, and ii) that the maximum number of common shares that may be reserved for issuance to any one optionee pursuant to a share option may not exceed 5% of the common shares outstanding at the time of grant (note 20).

The options must be exercised within five years of grant. The exercise price may not be lower than the market price of the common shares at the time of grant. All options granted before September 2006 have a vesting period of 18 months: 25% at the date of grant and 12.5% in each of the following six quarters. Beginning September 2006, options granted are entirely vested at the date of grant.

On February 2, 2006, the Board granted a total of 2,700,000 options to purchase common shares of the Company to its directors, officers and employees. The options are exercisable at a price of \$0.40 until February 2011.

On September 28, 2006, the Board granted a total of 2,000,000 options to purchase common shares of the Company to its directors, officers and employees. The options are exercisable at a price of \$0.90 until September 2011.

A summary of changes in the Company's stock options outstanding is presented below:

	For the year ended December 31, 2006		For the nine-month period ended December 31, 2005	
	Number of options	Average exercise price \$	Number of options	Average exercise price \$
Balance – Beginning of period	4,786,250	0.59	3,046,250	0.79
Granted	4,700,000	0.61	1,940,000	0.29
Exercised (note 10)	(252,917)	0.33	-	-
Expired or cancelled	(276,000)	0.72	(200,000)	0.85
Balance – End of period	8,957,333	0.60	4,786,250	0.59

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A summary of options outstanding and exercisable as at December 31, 2006 is presented below:

<u>Exercise price</u>	<u>Number of options</u>		<u>Expiry date</u>
	<u>Outstanding</u>	<u>Exercisable</u>	
\$0.85	845,000	845,000	October 2008
\$1.30	40,000	40,000	January 2009
\$0.75	1,189,000	1,189,000	August 2009
\$0.75	500,000	500,000	February 2010
\$0.30	1,598,333	1,398,541	September 2010
\$0.22	125,000	109,375	September 2010
\$0.40	2,660,000	1,662,500	February 2011
\$0.90	2,000,000	2,000,000	September 2011
	<u>8,957,333</u>	<u>7,744,416</u>	

Total stock-based compensation costs for the year ended December 31, 2006 amount to \$1,696,019 (note 13) (for the nine-month period ended December 31, 2005 – \$454,819), including \$1,001,173 (for the nine-month period ended December 31, 2005 – \$205,011) capitalized to mining assets as part of the Chihuahua project costs on the basis that the options were granted to officers and consultants involved exclusively in the exploration program in Mexico. The balance of \$694,846 (for the nine-month period ended December 31, 2005 – \$249,808) was recorded in the Consolidated Statements of Operations and Deficit.

The estimated fair value of each option granted was estimated using the Black-Scholes option pricing model based on the following weighted average assumptions:

	For the year ended December 31, 2006	For the nine-month period ended December 31, 2005
Average dividend per share	Nil	Nil
Estimated volatility	99.22%	102%
Risk-free interest rate	4.17%	3.5%
Expected life of options granted	4 years	4 years
Options granted which exercise price exceeds the market price of the stock on the grant date:		
Estimated fair value of option	\$0.55	-
Exercise price	\$0.90	-
Stock price at date of grant	\$0.80	-
Options granted which exercise price equals the market price of the stock on the grant date:		
Estimated fair value of option	\$0.28	\$0.21
Exercise price	\$0.40	\$0.29

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13 Contributed surplus

	For the year ended December 31, 2006 \$	For the nine-month period ended December 31, 2005 \$
Balance – Beginning of period	4,802,240	1,380,600
Stock-based compensation costs (note 12)	1,696,019	454,819
Exercise of options (note 10)	(46,959)	-
Warrants expired (note 11)	138,923	2,966,821
Balance – End of period	<u>6,590,223</u>	<u>4,802,240</u>

14 Income taxes

- (a) The provision for income taxes is different from what would have resulted from applying the combined Canadian statutory tax rate as a result of the following:

	For the year ended December 31, 2006 \$	For the nine-month period ended December 31, 2005 \$
Loss before income taxes	<u>(2,283,828)</u>	<u>(1,653,565)</u>
Combined federal and provincial income tax benefit at 32% (31% in 2005)	(730,825)	(514,600)
Income tax rate differential in Mexico	47,399	12,000
Impact of decrease in income tax rate on future income tax balance	149,235	-
Expired tax losses	25,338	-
Prior years reassessments	(159,295)	-
Stock-based compensation costs	222,351	77,800
Non-taxable portion of capital gain	(24,448)	-
Decrease (increase) in the valuation allowance	(120,012)	234,100
Foreign exchange gain (loss) taxable (deductible) in Mexico	(34,772)	295,000
Inflation taxable on net financial liabilities in Mexico	203,557	92,000
Permanent difference	102,864	-
Inflation on tax losses	(142,867)	-
Non-deductible items in Mexico	81,436	227,000
Other	9,227	19,300
	<u>(370,812)</u>	<u>442,600</u>

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(b) Future income tax balances are summarized as follows:

	As at December 31,	
	2006	2005
	\$	\$
Current future income tax assets		
Non-capital losses	746,246	26,000
Share issue costs	180,000	110,000
Other	69,156	-
	<hr/>	<hr/>
	995,402	136,000
Long-term future income tax assets		
Property, plant and equipment	29,000	32,000
Mining assets	386,000	118,000
Non-capital losses	1,077,000	3,991,600
Capital losses	58,718	90,300
Share and warrant issue expenses	266,000	156,800
Other	157,000	210,000
	<hr/>	<hr/>
	1,973,718	4,598,700
Total future income tax assets	2,969,120	4,734,700
Less: Valuation allowance	<hr/>	<hr/>
	2,210,718	1,957,100
	<hr/>	<hr/>
	758,402	2,777,600
Long-term future income tax liabilities		
Mining assets	<hr/>	<hr/>
	727,765	(3,175,200)
Total net future income tax liability	<hr/>	<hr/>
	30,637	(397,600)

(c) As at December 31, 2006, the cost for income tax purposes of the property, plant and equipment, mining assets and other costs totalled approximately \$11,885,000. The difference between this cost and the amounts capitalized in the financial statements arises mainly as a result of the write-off of some of the mining assets, the election of the Company in Mexico to deduct, in the year incurred, the exploration expenses and costs of mining claims prior to the commencement of commercial operations of a mine. This cost may be applied to reduce future taxable income over an unlimited period of time.

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- (d) The Company has accumulated non-capital losses of approximately \$3,910,963. These losses will expire from 2007 to 2026 as follows:

	\$
Years ending December 31, 2007	183,502
2008	203,336
2009	122,399
2010	121,762
2011	122,399
2014	533,468
2015	2,790,554
2026	398,093

- (e) The unamortized balance for tax purposes of share and warrant issue expenses amounting to approximately \$1,443,371 will be deductible over the next four years.
- (f) The Company's balance of capital losses amounts to \$266,426 and can be carried forward indefinitely against capital gains.
- (g) These tax values of assets and liabilities have not been agreed to by the relevant tax authorities nor have they been disputed.

15 Asset retirement obligations

As at December 31, 2006, based on its review of the status of its operations under the current Mexican environmental legislation, the Company determined it does not carry any asset retirement obligation and, therefore, has not recognised such an obligation.

A liability stemming from any asset retirement obligation will be recorded in the period in which such obligation arises.

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16 Statements of cash flows

- (a) The changes in non-cash working capital items are as follows:

	For the year ended December 31, 2006 \$	For the nine-month period ended December 31, 2005 \$
Sales tax and other receivables	(2,944,704)	(25,250)
Inventories from pilot-mining program	(329,742)	78,361
Prepaid expenses	73,880	(85,229)
Accounts payable and accrued liabilities	98,422	(718,781)
Income taxes payable	12,425	45,000
	<u>(3,089,719)</u>	<u>(705,899)</u>

- (b) Additional information – non-cash transactions

Issuance of shares for mining property	768,000	-
Stock-based compensation costs capitalized into mining assets (note 12)	1,001,173	205,011
Additions of mining assets included in accounts payable and accrued liabilities	17,120	671,150
Increase of accounts receivable included in sales of concentrate	3,020,046	327,000
Capitalized amortization of exploration building and equipment	1,686,739	833,442

- (c) Interest and income taxes

Interest paid on obligation related to assets under capital lease	48,898	3,396
Income taxes paid	45,000	-

17 Related party transactions

- (a) During the year ended December 31, 2006, companies controlled by officers of the Company charged consulting fees amounting to \$946,145 (for the nine-month period ended December 31, 2005 – \$517,688), including \$602,571 capitalized to deferred exploration costs (for the nine-month period ended December 31, 2005 – \$388,937). As at December 31, 2006, the balance due to these companies amounted to \$42,361 (as at December 31, 2005 – \$11,840).
- (b) During the nine-month period ended December 31, 2005, directors, companies controlled by directors and officers of the Company participated in private placements of common shares (see terms described in note 10 (i) (b) for a total consideration of \$886,500 (during the year ended December 31, 2006 – nil).

Related party transactions occurred in the normal course of business and were recorded at the exchange value, which is the consideration determined and agreed to by the related parties.

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18 Commitments

In February 2004, the Company and two other companies jointly signed a five-year lease for office premises. The annual rent is approximately \$150,000 which is divided on a pro rata basis among the three companies. The Company's annual gross commitment is approximately \$50,000.

In December 2006, the Company signed a five-year lease for office premises. The annual rent is approximately \$60,000.

19 Contingency

In 2005, legal proceedings were filed in Mexico against one of the Company's subsidiaries, Dia Bras Mexicana S. de R.L. de C.V. ("DBM"), by an individual claiming the annulment and revocation of the purchase contracts of the Bolivar Mine property entered into between DBM and Mr. Javier Octavio Bencomo Munoz and Minera Senda de Plata, S.A. de C.V. Following the notification of said claim against DBM, a defence was filed. Management cannot predict the outcome of these proceedings. Management is confident that the results of the proceedings will have no adverse material effect on the Company.

20 Subsequent events

On March 6, 2007, the Board of Directors approved an increase in the number of common shares reserved for issuance under the Company's stock option plan from 9,700,000 to 10,900,000. The number of common shares reserved represents approximately 10% of the number of shares issued and outstanding.

On April 3, 2007, the Board granted a total of 1,775,000 options to purchase common shares of the Company to its directors, officers and employees. The options are exercisable at any time at a price of \$1.10 until April 3, 2012.

21 Comparative figures

Certain comparative figures have been reclassified to conform to the presentation adopted for the current year.