

URUGUAY MINERAL EXPLORATION



**Uruguay Mineral Exploration Inc.  
Consolidated Financial Statements  
For the years ended May 31, 2008 and 2007**

	<b>Contents</b>
<b>Management Report</b>	<b>2</b>
<b>Auditors' Report</b>	<b>3</b>
<b>Consolidated Financial Statements</b>	
<b>Consolidated Balance Sheets</b>	<b>4</b>
<b>Consolidated Statements of Income, Comprehensive Income and Retained Earnings</b>	<b>5</b>
<b>Consolidated Statements of Cash Flows</b>	<b>6</b>
<b>Consolidated Statements of Changes in Shareholders' Equity</b>	<b>7</b>
<b>Notes to Consolidated Financial Statements</b>	<b>8-27</b>

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## **Management's Responsibility for Financial Reporting**

The consolidated financial statements of Uruguay Mineral Exploration Inc. and the information contained in the annual report have been prepared by and are the responsibility of the Company's management. The consolidated financial statements have been prepared in accordance with generally accepted accounting principles (GAAP) in Canada and, where appropriate, reflect management's best estimates and judgments based on currently available information. Management has developed and is maintaining a system of internal controls to obtain reasonable assurance that the Company's assets are safeguarded, transactions are authorized and financial information is reliable.

The Company's independent auditors, PricewaterhouseCoopers LLP, who are appointed by the Audit Committee, conduct an audit in accordance with Canadian generally accepted auditing standards. The Audit Committee of the Company meets periodically with management and the independent auditors to review the scope and results of the annual audit, and to review the consolidated financial statements and related financial reporting matters prior to approval of the consolidated financial statements.

David Fowler, Chief Executive Officer  
August 12, 2008

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## Auditors' Report

### To the Shareholders of Uruguay Mineral Exploration Inc.

We have audited the consolidated balance sheets of Uruguay Mineral Exploration Inc. as at May 31, 2008 and 2007 and the consolidated statements of income, comprehensive income and retained earnings, cash flows and changes in shareholders' equity for the years then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated 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 May 31, 2008 and 2007 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

(Signed) PricewaterhouseCoopers LLP

Chartered Accountants  
Licensed Public Accountants  
Toronto, Ontario, Canada  
August 12, 2008

**Uruguay Mineral Exploration Inc.**  
**Consolidated Balance Sheets**  
Thousands of United States Dollars, except where indicated

**As at May 31** **2008** **2007**

**Assets**

**Current assets**

Cash	\$ 18,601	\$ 13,978
Accounts receivable (Note 4)	2,810	2,275
Inventories (Note 5)	16,749	8,484
Prepaid expenses and other	1,004	647
	39,164	25,384

Property, plant and equipment and mineral properties (Note 6)	29,681	30,714
Deferred exploration (Note 7)	8,948	16,316
Future income tax assets (Note 12)	5,375	2,387
Restricted cash	191	140
<b>Total assets</b>	<b>\$ 83,359</b>	<b>\$ 74,941</b>

**Liabilities and Shareholder's Equity**

**Current liabilities**

Accounts payable and accrued liabilities	\$ 8,816	\$ 6,238
Current portion of long term debt (Note 8)	2,275	1,231
	11,091	7,469

Long term tax payable (Note 12)	2,414	2,414
Long term debt (Note 8)	25	2,154
Asset retirement obligation (Note 9)	2,869	2,036
<b>Total liabilities</b>	16,399	14,073

Capital stock	35,043	34,592
Warrants and Convertible notes (Note 10)	12	12
Contributed surplus	3,882	3,297
Accumulated other comprehensive income	(19)	(19)
Retained earnings	28,042	22,986
<b>Total shareholders' equity</b>	66,960	60,868

<b>Total liabilities and shareholders' equity</b>	<b>\$ 83,359</b>	<b>\$ 74,941</b>
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Commitments and contingencies (Note 11)

Approved on behalf of the Board:

David Fowler Director	Tony Shearer Director
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The accompanying notes are an integral part of these consolidated financial statements.

**Uruguay Mineral Exploration Inc.**  
**Consolidated Statements of Income, Comprehensive Income and Retained Earnings**

(Thousands of United States Dollars, except for earnings per share amounts and weighted average number of shares outstanding)

<b>For the years ended May 31</b>	<b>2008</b>	<b>2007</b>
<b>Net sales</b>	<b>\$ 79,061</b>	<b>\$ 63,056</b>
Operating expenses	38,947	31,928
Amortization and depreciation	15,724	8,361
<b>Operating expenses</b>	<b>54,671</b>	<b>40,289</b>
<b>Sub-total</b>	<b>24,390</b>	<b>22,767</b>
<b>Other expenses (income)</b>		
Stock based compensation expense	792	975
Fair value adjustment for derivatives	0	(2,317)
Exploration expenses written off	11,103	2,129
General and administrative expense	4,605	4,347
Interest expense, debt accretion and financing fees	371	314
Interest earned and other income	(923)	(510)
Foreign exchange	(238)	225
	<b>15,710</b>	<b>5,163</b>
<b>Income before taxes</b>	<b>8,680</b>	<b>17,604</b>
Current income taxes provision (Note 12)	3,870	3,582
Future income taxes recovery (Note 12)	(2,988)	(532)
<b>Net and comprehensive income for the year</b>	<b>7,798</b>	<b>14,554</b>
<b>Retained earnings, beginning of year</b>	<b>22,986</b>	<b>10,775</b>
<b>Dividends</b>	<b>(2,742)</b>	<b>(2,343)</b>
<b>Retained earnings, end of year</b>	<b>\$ 28,042</b>	<b>\$ 22,986</b>
<b>Earnings per common share</b>		
<b>Basic (Note 16)</b>	<b>0.16</b>	<b>0.30</b>
<b>Diluted (Note 16)</b>	<b>0.16</b>	<b>0.30</b>
<b>Weighted average shares outstanding</b>		
Basic	48,911,779	48,258,892
Diluted	48,924,272	48,668,269

The accompanying notes are an integral part of these consolidated financial statements.

**Uruguay Mineral Exploration Inc.**  
**Consolidated Statements of Cash Flows**  
Thousands of United States Dollars, except where indicated

<b>For the years ended May 31</b>	<b>2008</b>	<b>2007</b>
<b>Operating activities</b>		
Net income for the year	\$ 7,798	\$ 14,554
Adjustments for :		
mortization and depletion	15,724	8,361
Exploration expenses written off	11,103	2,129
Accretion of debt	252	159
Future income taxes	(2,988)	(532)
Tax deferred payment	0	928
Fair value adjustment of derivatives	0	(2,317)
Stock based compensation	792	975
Others	384	(80)
	<u>33,065</u>	<u>24,177</u>
Net change in non-cash working capital balances (Note 16)	<u>(6,579)</u>	<u>1,181</u>
	<u>26,486</u>	<u>25,358</u>
<b>Financing activities</b>		
Proceeds from the issue of share capital	592	1,515
Share repurchases (Note 10 (c))	(406)	0
Payments of finance lease net of drawdowns	(188)	(57)
Dividends	(2,742)	(2,343)
	<u>(2,744)</u>	<u>(885)</u>
<b>Investing activities</b>		
Purchase of property, plant and equipment and development costs	(9,159)	(12,350)
Exploration expenditure	(9,960)	(7,076)
	<u>(19,119)</u>	<u>(19,426)</u>
Increase in cash	4,623	5,047
Cash at the beginning of year	<u>13,978</u>	<u>8,931</u>
<b>Cash at the end of year</b>	<b>\$ 18,601</b>	<b>\$ 13,978</b>

The accompanying notes are an integral part of these consolidated financial statements.

**Uruguay Mineral Exploration Inc.**  
**Consolidated Statements of Changes in Shareholders' Equity**  
Thousands of United States Dollars, except where indicated

For the years ended May 31	May 31, 2008		May 31, 2007	
	Number (000's)	Amount	Number (000's)	Amount
<b>Common shares</b>				
Balance at beginning of year	48,531	\$ 34,592	47,525	\$ 32,670
Exercise of stock options	410	857	756	910
Share repurchases	(130)	(406)	0	0
Exercise of warrants	0	0	250	1,012
Balance at end of year	<u>48,811</u>	<u>\$ 35,043</u>	<u>48,531</u>	<u>\$ 34,592</u>
<b>Warrants and Convertible notes (Note 10)</b>				
Balance at beginning of year	520	\$ 12	1,000	\$ 188
Issued for farm in agreements	0	0	20	12
Expired warrants	(250)	0	(250)	0
Exercise of warrants	0	0	(250)	(188)
Balance at end of year	<u>270</u>	<u>\$ 12</u>	<u>520</u>	<u>\$ 12</u>
<b>Contributed surplus</b>				
Balance at beginning of year		\$ 3,297		\$ 1,625
Employee stock based compensation recognised		792		975
Commitment to issue stock options		0		917
Transfer to common shares		(207)		(220)
Balance at end of year		<u>\$ 3,882</u>		<u>\$ 3,297</u>
<b>Accumulated other comprehensive income</b>				
Balance at beginning of year		\$ (19)		0
Adjustment to opening other comprehensive income		0		(19)
Balance at end of year		<u>\$ (19)</u>		<u>\$ (19)</u>
<b>Retained earnings</b>				
Balance at beginning of year		\$ 22,986		\$ 10,775
Net income for the year		7,798		14,554
Dividends		(2,742)		(2,343)
Balance at end of year		<u>\$ 28,042</u>		<u>\$ 22,986</u>
Shareholders' equity at end of year		<u>\$ 66,960</u>		<u>\$ 60,868</u>

The accompanying notes are an integral part of these consolidated financial statements.

May 31, 2008 and 2007

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## 1. Nature of Operations

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Uruguay Mineral Exploration Inc is a gold producer and exploration company focused on identifying and developing mineral opportunities either directly or through joint ventures.

Uruguay Mineral Exploration Inc is governed by the corporate laws of the Yukon Territory. The Company's shares are listed on the TSX Venture Exchange in Canada and the Alternative Investment Market of the London Stock Exchange in the United Kingdom.

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## 2. Significant Accounting Policies

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The consolidated financial statements of the Company have been prepared by management in accordance with Canadian generally accepted accounting principles. The reference to "the Company" in these consolidated financial statements includes the parent and all of its subsidiaries.

The preparation of consolidated financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. Actual results could differ from those estimates. The consolidated financial statements have, in management's opinion, been properly prepared using careful judgment with reasonable limits of materiality and within the framework of the significant accounting policies summarized below.

- (a) Consolidation: The consolidated financial statements include the accounts of the Company and its controlled subsidiaries from their respective dates of acquisition. All inter-company transactions have been eliminated.
- (b) Reporting currency and foreign currency translation: Most of the Company's operations are conducted by its Uruguayan subsidiaries in United States Dollars. The Company has adopted the United States Dollar as its functional and reporting currencies. The Company has determined that all of its operations are integrated, as such, the Company translates foreign currencies into the reporting currency on the following basis:
- Non-monetary assets and liabilities using historical rates;
  - Monetary assets and liabilities using period end rates; and
  - Income and expenses are translated at average rates of exchange during the period.

Gains and losses arising from the translation of foreign currency balances into US dollars and from foreign currency transactions related to integrated operations are recorded in earnings.

- (c) Cash and equivalents: Cash and equivalents consist of cash in bank, deposits held at call with banks and other short term highly liquid investments with original maturity dates of three months or less.

May 31, 2008 and 2007

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## 2. Significant Accounting Policies - continued

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- (d) Property, plant and equipment & mineral properties: Property, plant and equipment is recorded at cost less accumulated amortization. Plant and other equipment are amortized on a straight line method over the estimated productive life of the asset. Productive lives for mobile and other equipment range from 2 to 5 years.

Mineral properties include:

- Development costs incurred to bring a mining property into production, develop new ore bodies or develop mining areas in advance of production, including stripping cost in a pre-production phase. Development costs are capitalized when a mine plan has been prepared proved and probable reserves have been established, and the Company has decided to commercially develop the property. Development expenditure is accumulated separately for each area in which economically recoverable mineral resources have been identified and are reasonably assured.
- Deferred Exploration once mineral resources have been identified in the property and incorporated to the Company's resource statements.

No amortization is provided in respect of mineral properties until commencement of commercial production. Mineral properties are amortized and charged to operations using the units of production method based on the estimated life of mine considering recoverable proven and probable reserves. All expenditure incurred prior to the commencement of commercial levels of production from each development property is carried forward to the extent to which recoverable from cash flows to be derived from the sale of production is reasonably assured. Amounts shown as development costs are net of revenue prior to commercial production.

- (e) Impairment of assets: The Company regularly reviews the carrying values of its producing mining assets for possible impairment. The Company estimates future cash flows from those assets and compares this amount with the carrying value. An impairment loss is recognized when the asset's carrying amount is not recoverable and exceeds its fair value.

Estimated future cash-flows includes estimates of recoverable resources and commodity prices (considering historical prices, price trends and related factors) and estimated production related expenses discounted by the Company's weighted average cost of capital with appropriate adjustment for the risk associated with the relevant unit. Estimates of future net cash flows are based on ore reserves and mineral resources for which there is a high degree of confidence of economic extraction.

- (f) Deferred exploration and evaluation: Exploration and evaluation expenditure is capitalized under areas of interest defined by the Company and carried forward as an asset until management has made a positive decision to develop the project or written down when events or changes in circumstances indicate that its carrying amount may not be recoverable. The excess of carrying value over fair value is charged to income. When mineral resources are to develop the area of interest exploration and evaluation expenditures are reclassified and shown as a Mineral Property asset.

May 31, 2008 and 2007

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## **2. Significant Accounting Policies - continued**

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Expenditure to be capitalized includes direct cost attributable to the exploration and evaluation projects, such as topographical, geological, geochemical and geophysical studies, exploratory drilling, trenching and sampling and of the acquisition of rights to explore. Overhead costs that are directly attributable to exploration and evaluation activities, but not directly attributable to an individual project or area, such as general advisory, the cost of a central exploration office or the cost of a mining tenements office are allocated to areas of interest and capitalized. Borrowing costs derived from the exploration and evaluation activities financing, exchange differences related to monetary assets and liabilities associated to the exploration activities and depreciation of property, plant and equipment used in the exploration activities are not capitalized and recognized as expenses as they are incurred.

The recoverability of amounts shown for deferred exploration and evaluation is dependent upon the discovery of economically recoverable reserves. The exploration assets are reassessed on a regular basis for impairment. An impairment of an exploration asset occurs when at least one the following conditions are met:

- the Company's right to explore in an area of interest has expired or will expire in the near future and is not expected to be renewed;
- the Company has strategically decided to discontinue activities in the area of interest;
- substantive exploration expenditure on further exploration in the area of interest is neither budgeted nor planned in the near future and no negotiations to sell the project or farm it out are planned or considerably advanced.
- no substantive exploration expenditure has been done in the area of interest during the last three years.

The exploration asset is written off in the period it is considered impaired under the criteria outlined above.

- (g) Inventories: Inventories include supplies and materials, ore stockpiles, gold in circuit and finished goods, and are measured at the lower of cost or net realizable value.

Materials and supplies include consumable stores and spare parts used in operations. Appropriate allowances for damage, obsolescence and slow moving items are recorded based on an identification process. Spare parts include spares that are regularly replaced, usually as part of a replacement programme (circulating spares). However, major spare parts on hand to ensure the uninterrupted operation of the production equipment before an unexpected breakdown or equipment failure and stand-by equipment are accounted for as property, plant and equipment and depreciated over the same period as the component they are associated with.

Ore stockpiles are comprised of coarse ore that has been extracted from the mine and is available for processing. Stockpiles are valued at the lower of average cost or net realizable value with quantities determined through physical measurement and grade determined through assay testing. Ore with a marginal cutoff grade is stockpiled for potential future processing but is carried at zero value.

In process inventories represent materials that are currently being converted to a saleable product. In process materials are measured based on assays of the material fed to the processing plants and expected recoveries. In process inventories are valued at the lower of average cost and net realizable value.

May 31, 2008 and 2007

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## 2. Significant Accounting Policies - continued

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Finished metal inventories include gold and silver dore bullions before refining, and finished gold and silver ingots, and are valued at average production cost and are not marked to market. Average production cost represents the average cost of in process inventories prior to the refining process and any relevant refining costs. Sales and refining costs are not part of the cost of inventories.

Cost of inventories are determined using the absorption method which includes all the costs of purchase and conversion, including costs that are directly related to production and an allocation of fixed and variable production overheads, including depreciation of mine properties and of property, plant and equipment used in mining and processing the ore.

- (h) Future income taxes: The Company uses the assets and liability method to account for future income taxes. Under this method, future income tax assets and liabilities are determined based on differences between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements and calculated using tax rates (and laws) that have been enacted or substantially enacted by the balance sheet date and are expected to apply when the related future income tax asset is realised or the future income tax liability is settled.

Future income tax assets are recognized to the extent that it is more likely than not that losses available for carry forward will be used to offset future income taxes. The effect on future income tax assets and liabilities of a change in rates is included in the period during which the change is substantively enacted.

- (i) Asset retirement obligations: Asset retirement obligations include the dismantling and demolition of infrastructure and the removal of residual materials and remediation of disturbed areas.

The estimated fair value of asset retirement obligations is provided for in the accounting period when the legal obligation arising from the related disturbance occurs. A technique based on the net present value of estimated future costs is used to estimate the fair value of the liability. Asset retirement obligations are a normal consequence of mining, and the majority of close down and restoration expenditure is spent at the end of the life of the mine. Costs are annually estimated on the basis of a closure plan to reflect known developments, update costs estimates and revise estimated lives of operations, and are subject to formal reviews at regular intervals. Although the ultimate cost to be incurred is uncertain, the Company's businesses estimate their respective costs based on feasibility and engineering studies using current restoration standards and techniques and industry guidelines, on a site by site basis.

Upon initial recognition of a liability for an asset retirement obligation, an asset retirement obligation is capitalized by the same amount of the liability within property, plant and equipment. The asset retirement cost is expensed using a systematic and rational method over its useful life, mostly the unit of production method based on estimated proven and probable reserves as determined by independent engineers, and is included as an operation cost. In subsequent periods, the Company recognizes the changes in the liability for an asset retirement obligation resulting from the passage of time and the revisions to either the timing or amount of the original estimate of undiscounted cash flows.

Changes resulting from revisions to the timing or the amount of the original undiscounted cash flows are recognized as an increase or decrease in the carrying amount of the liability for an

May 31, 2008 and 2007

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## 2. Significant Accounting Policies - continued

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asset retirement obligation against the related asset retirement cost capitalized as part of the carrying amount of the related long-lived asset.

Changes due to the passage of time, meaning the “unwinding” of the discount applied in establishing the net present value of the liability, is charged to the income statement in each accounting period.

As noted above, the ultimate cost of the close down and restoration is uncertain and costs estimated can vary in response to many factors including changes to the relevant legal requirements, the emergence of new restoration techniques or experiences at other mine sites. The expected timing of expenditure can also change, for example in response to changes in ore reserves or production rates. As a result, there could be significant adjustments to the provision for close down and restoration which would affect future financial results.

- (j) Revenue recognition: Revenue from mining operations is recognized after shipment of gold to third party refineries, when the sales price is determinable, title has passed to the customer and collection of the sale is reasonably assured. Sales include government incentives provided to the Company for the export sales as the incentive is based on the value of exports.
- (k) Stock-based compensation plan: The Company has a stock-based compensation plan and recognizes compensation expense for option awards. Compensation expense is measured at fair value at the grant date using the Black-Scholes option pricing model and is recognized over the vesting period with a corresponding increase to contributed surplus. Upon exercise, the proceeds of the options are credited to capital stock at the option price and the fair value of the options, as previously recorded, is reclassified from contributed surplus to capital stock. Stock options issued to persons other than employees are accounted for at fair value and deferred and amortized over the relevant service period.

The Company elected to adopt the fair value base method of accounting for stock-based compensation on a prospective basis, applied to awards granted under the plan since March 2003. For awards granted prior to that date the Company applies the settlement method, in that no compensation expense is recorded, and when the options are exercised, share capital is increased in the amounts of the proceeds received.

- (l) Derivatives: Financial derivatives are marked to market with the fair value of the derivative instruments recognized as unrealized gains and losses in the statement of income.
- (m) Earnings per share amounts: Basic earnings per common share are computed by dividing the net profit by the weighted average number of common shares outstanding during the year. Diluted per share amounts reflect the potential dilution effect of “in the money” securities or other contracts to issue common shares were exercised or converted to common shares. The treasury stock method is used to determine diluted per share amount which assumes that all outstanding stock options grants are exercised, if dilutive, and the assumed proceeds are used to purchase the Company’s common share at the average market price during the year.

May 31, 2008 and 2007

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## **2. Significant Accounting Policies - continued**

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- (n) Joint venture: Certain of the Company's exploration and development activities may be conducted jointly with others. These consolidated financial statements reflect only the Company's proportionate interest in such activities.
  - (o) Reclassification: Certain comparative figures have been reclassified to conform to the presentation adopted in the current year.
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## **3. Changes in accounting policies**

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- (a) Deferred Stripping Costs: The Company is engaged in open pit mining and incurs costs in removing overburden and waste rock (stripping costs) during mine development and production phase.

Up to and including the financial statements for the year ended May 31, 2007, when stripping costs in the production phase were higher with respect to those arising from applying the expected average stripping ratio (the ratio of waste material to ore extracted) for the mine life, a portion of the waste removal costs has been attributed to future production and deferred, as it was considered a development cost incurred to gain access to the ore body. The amount deferred was subsequently amortized to the income statement when the actual stripping ratio falls below the expected average stripping ratio. These costs include the cost of drilling, blasting, loading and haulage of waste rock from the open pit to the waste pile.

Effective June 1, 2007, the Company adopted the new recommendations issued by the Canadian Institute of Chartered Accountants (CICA) (EIC 160 "Stripping costs incurred in the production phase of a mining operation"), which require the costs associated with the removal of overburden and another mine waste materials that are incurred in the production phase of mining operations to be charged to income in the period in which they are incurred, except when the costs represent a betterment to the mineral property. Costs represent betterment when the stripping activity provides access to reserves that would not have been accessible in the absence of the stripping activity.

The new policy has been applied on a prospective basis to stripping costs incurred since June 1, 2007, and the accumulated deferred costs at the beginning of the financial year are being amortized over the remaining reserves accessed by the stripping activity using the units of production method. The accumulated deferred cost are shown under Mineral Properties while in the past have been shown as Other Deferred costs. The depreciation of the asset is charged to depreciation while it was charged to operating expenses in the past. Necessary reclassifications have been done in the balance, profit and loss and cashflow statements for last year's presentation to reflect comparative figures. The adoption of this standard had no material financial impact on the financial statements of the Company.

- (b) Changes in accounting policies: Effective June 1, 2007 the Company applied CICA Handbook Section 1506, Accounting Changes. This standard allows for voluntary changes in accounting policy only when they result in the financial statements providing reliable and more relevant information, requires changes in accounting policy to be applied retrospectively unless doing so is impracticable, requires prior period errors to be corrected retrospectively and calls for enhanced disclosures about the effects of changes in accounting policies, estimates and errors on the financial statements. The impact that the adoption of Section 1506 will have on the Company's

May 31, 2008 and 2007

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### **3. Changes in accounting policies – continued**

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results of operations and financial condition will depend on the nature of future accounting changes.

- (c) Financial instruments: Effective June 1, 2007, the Company applied CICA Handbook Sections 3855, "Financial Instruments – Recognition and Measurement", and 3865, "Hedges". Section 3855 prescribes when a financial instrument is to be recognized on the balance sheet and at what amount. It also specifies how financial instrument gains and losses are to be presented. Section 3865 provides alternative treatments to Section 3855 for entities which choose to designate qualifying transactions as hedges for accounting purposes. It replaces and expands on Accounting Guideline 13 "Hedging Relationships", and the hedging guidance in Section 1650 "Foreign Currency Translation" by specifying how hedge accounting is applied and what disclosures are necessary when it is applied.

Effective June 1, 2007 the Company applied CICA Handbook Section 3862, Financial Instruments -Disclosures; Section 3863, Financial Instruments - Presentation; and Section 1535, Capital Disclosures were issued. Section 3862 on financial instrument disclosures places an increased emphasis on disclosures about risks associated with both recognized and unrecognized financial instruments and how these risks are managed and is consistent with Section 3861. The new Section removes duplicative disclosures and simplifies the disclosures relating to concentrations of risk, credit risk, liquidity risk and price risk currently found in Section 3861. Section 3863 on the presentation of financial instruments is unchanged from the presentation requirements included in Section 3861. Section 1535 on capital disclosures requires the disclosure of information about an entity's objectives, policies and processes for managing capital. The adoption of these standards had no financial impact on the financial statements of the Company.

- (d) Comprehensive income: Effective June 1, 2007, the Company applied CICA Handbook Sections 1530, "Comprehensive Income". Section 1530 introduces a new requirement to temporarily present certain gains and losses from changes in fair value outside net income. It includes unrealized gains and losses, such as: changes in the currency translation adjustment relating to self-sustaining foreign operations; unrealized gains or losses on available-for-sale investments; and the effective portion of gains or losses on derivatives designated as cash flow hedges or hedges of the net investment in self-sustaining foreign operations.

The Company has not incurred any other comprehensive income during the year but actually carried a historical accumulated currency translation adjustment for self-sustaining foreign operations that is reclassified to accumulated other comprehensive income upon transition to the new standard. Other than this transition adjustment, the adoption of this standard had no financial impact on the financial statements of the Company.

- (e) Future accounting changes: In June 2007, a replacement section for inventories, Section 3031 "Inventories" was issued and provides guidance on the determination of cost and its subsequent recognition as an expense, including any write-down to net realizable value. It also provides guidance on the cost formulas that are used to assign costs to inventories and eliminates the use of the "last-in, first-out" method of accounting and is effective for the fiscal years beginning on or after June 1, 2008. The Company has not yet determined the impact of adopting the above accounting standards.

May 31, 2008 and 2007

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### 3. Changes in accounting policies – continued

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- (f) Goodwill and intangible assets: The CICA has issued CICA 3064 'Goodwill and intangible assets' which may affect the financial disclosures and results of operations of the Company. This Section applies to annual and interim financial statements relating to fiscal years beginning on or after October 1, 2008 and the Company will adopt the requirements commencing in the quarter ended August 31, 2009. Section 3064, Goodwill and intangible assets, establishes revised standards for recognition, measurement, presentation and disclosure of goodwill and intangible assets. Concurrent with the introduction of this standard, the CICA withdrew EIC 27, Revenues and Expenses during the pre-operating period. As a result of the withdrawal of EIC 27, the Company will no longer be able to defer costs incurred and revenues received prior to commercial production at new mine operations. The Company is considering the impact this will have on the Company's financial statements.
- (g) After October 1, 2008 and the Company will adopt the requirements commencing in the quarter ended August 31, 2009. Section 3064, Goodwill and intangible assets, establishes revised standards for recognition, measurement, presentation and disclosure of goodwill and intangible assets. Concurrent with the introduction of this standard, the CICA withdrew EIC 27, Revenues and Expenses during the pre-operating period. As a result of the withdrawal of EIC 27, the Company will no longer be able to defer costs incurred and revenues received prior to commercial production at new mine operations. The Company is considering the impact this will have on the Company's financial statements.
- (h) Convergence with International Financial Reporting Standards: The Canadian Institute of Chartered Accountants plans to transition Canadian GAAP for public companies to International Financial Reporting Standards ("IFRS"). The effective changeover date is for interim and annual financial statements relating to fiscal years beginning on or after June 1, 2011. The impact of the transition to IFRS on the Corporation's consolidated financial statements is not yet determinable.

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### 4. Accounts Receivable

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	<u>2008</u>	<u>2007</u>
Receivables	\$ 46	\$ 38
Other Tax receivables	<u>2,764</u>	<u>2,237</u>
	<u>\$ 2,810</u>	<u>\$ 2,275</u>

Other tax receivables consist of refunds for Canadian GST, Uruguayan Value Added Tax (VAT) refunds and Uruguayan export tax refunds (based on a percentage of FOB value of the export value of dore).

**Uruguay Mineral Exploration Inc.**  
**Notes to Consolidated Financial Statements**  
Thousands of United States Dollars, except where indicated

May 31, 2008 and 2007

**5. Inventories**

	<b>2008</b>	2007
Finished metals	\$ 1,052	\$ 1,107
Ore in stockpiles	5,168	455
Gold in circuit	1,462	1,033
Materials and supplies	9,067	5,889
	<u>\$ 16,749</u>	<u>\$ 8,484</u>

**6. Property, Plant and Equipment and Mineral Properties**

	<u>Cost</u>	<b>2008</b>	<u>Net Book Value</u>
		<u>Accumulated Amortization and Depletion</u>	
<b>Land and lease rights</b>	\$ 2,088	\$ 0	\$ 2,088
<b>Plant and equipment</b>	28,015	16,274	11,741
<b>Asset retirement obligation</b>	2,762	1,752	1,010
<b>Deferred stripping asset</b>	4,829	2,480	2,349
<b>Mineral properties</b>	26,906	14,413	12,493
	<u>\$ 64,600</u>	<u>\$ 34,919</u>	<u>\$ 29,681</u>
		<b>2007</b>	
	<u>Cost</u>	<u>Accumulated Amortization and Depletion</u>	<u>Net Book Value</u>
Land and lease rights	\$ 2,077	\$ -	\$ 2,077
Plant and equipment	25,411	12,391	13,020
Asset retirement obligation	2,044	1,385	659
Deferred stripping asset	4,829	-	4,829
Mineral properties	17,210	7,081	10,129
	<u>\$ 51,571</u>	<u>\$ 20,857</u>	<u>\$ 30,714</u>

- (a) The plant is located on leased land. The lease expires in 2026. No further payments are due on the lease.
- (b) Included in property, plant and equipment is \$ 814 (2007 - \$ 1,114) of major spare parts that are amortized over 5 years. These major spare parts are maintained to ensure the uninterrupted operation of the production equipment before an unexpected breakdown or equipment failure.

May 31, 2008 and 2007

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**6. Property, Plant and Equipment and Mineral Properties – continued**

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- (c) Included under Mineral properties are \$ 3,691 (2007 - \$ 2,830) of pre-production stripping costs that have not yet began to be amortized as are costs related to deposits from which production has not commenced.
- (d) Included under Mineral properties is the expenditure incurred to divert the Arroyo Corrales river that allowed access to reserves of El Arenal deposit. The accumulated costs were \$ 4,644 with associated accumulated amortization of \$ 3,624 (2007 - \$ 2,100 and \$1,778 respectively).
- (e) During October 2005, the Company acquired the 10% net profit interest over key tenements within the Minas de Corrales project, including the tenement on which Arenal deposit is located. This agreement terminates the Company's obligation to pay the holder the 10% Net Profit Interest (NPI) of the net profits derived from gold produced from the NPI area as part of the acquisition of the tenements. An amount of \$ 4,471 is shown under mineral properties and is amortized using the unit of production method based on the estimated life of mine with an associated accumulated amortization of \$ 3,229 (2007 - \$1,919).
- (f) Effective June 1, 2007, the Company reclassified its deferred stripping asset into mineral properties while in the past was shown under "Other Deferred Costs". Balances for last year's presentation have been reclassified to allow comparative figures.
- (g) Included under Property, plant and Equipment are leased vehicles which are depreciated on a straight line method over four years. At May 31, 2008, the leased vehicles presented a total gross value of \$ 457 and an accumulated depreciation of \$ 210 (2007 – \$ 99).

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**7. Deferred Exploration**

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	<b>2008</b>	2007
Balance at beginning of year	<b>\$ 16,316</b>	\$ 11,184
Payments for exploration expenditure during the year	<b>9,910</b>	6,934
Payments for exploration acquisitions and options during the year	<b>50</b>	142
Reclassification from (to) Mine properties	<b>(6,225)</b>	185
Exploration expenses written off	<b>(11,103)</b>	(2,129)
Balance at the end of the year	<b>\$ 8,948</b>	\$ 16,316

During the year, management determined that the carrying value of certain capitalized exploration expenditure was impaired. The total amount written off was \$ 11,103 (2007 - \$ 2,129).

**Farm-in agreements:**

- (a) The Company has signed in March 2007 a farm-in agreement giving it the option to acquire a 100% interest in exploration permits along the Florida Greenstone Belt of southern Uruguay owned by a Uruguayan-based mineral exploration company, Delcosur S.A. ("Delcosur").

The Company is required to spend \$ 1,050 on exploration over three years to exercise its option to acquire 100% of Delcosur tenements. Upon exercising this option, the Company is required to

May 31, 2008 and 2007

## 7. Deferred Exploration – continued

grant Delcosur a 1% Net Smelter Return on metal sales resulting from production sourced from the Delcosur tenements. Additionally, in the event that the Company develops a mining operation on the tenements, it will issue Delcosur or its nominees a further 350,000 non-transferable warrants to purchase common shares of the Company at a price calculated at a 20% premium over the five day average trading price prior to the issuance and will be exercisable for a period of two years from the date of issuance.

- (b) The Company has the right to purchase shares of a Uruguayan company, Davinco S.A (“Davinco”) that owns the Presidente Terra project pursuant to an agreement dated May 14, 1997. Under this agreement the Company has the option to purchase 80% of the issued share capital of Davinco for the amount of \$ 750 payable in installments, and the remaining 20% once a decision has been made to develop a mining operation, at a variable price.

\$ 475 of the \$ 750 in initial installments for the purchase of the 80% of Davinco shares have been settled in the past, with the remaining installment of \$ 275 is due within five days after completing a feasibility study on the Presidente Terra Project.

### **Acquisitions:**

- (c) The Company previously purchased a Uruguayan diamond database. Under the terms of the agreement the vendor was paid \$ 20 and is entitled to an additional 0.8% royalty on any net diamond sales from any diamond deposit discovered by the Company in Uruguay. A further 0.2% royalty will be paid to a third party, who has an interest in the database.
- (d) For the Texas and Mal Abrigo projects the Company has committed to pay a 2% net profits interest and a 2% net smelter return respectively, payable to the vendor. The Company may repurchase the net smelter return of the Mal Abrigo project at any time by paying a lump sum of \$ 650.

### **Exploration performance bonds:**

- (e) The Uruguay Mining legislation requires all mining titles to be supported by guarantees for any environmental rehabilitation requirements resulting from exploration activities. The Company has facility agreements with Uruguayan local insurance companies and banks to support the required guarantees. The total guarantees provided at May 31, 2008 to support exploration activities on tenements granted were approximately \$ 2,164 (2007 - \$ 2,381).

## 8. Long Term Debt

	<b>2008</b>	2007
Deferred payment on net profit interest acquisition (a)	\$ 2,088	\$ 2,985
Finance lease (b)	212	400
	<b>2,300</b>	3,385
Less current portion	<b>(2,275)</b>	(1,231)
	<b>\$ 25</b>	\$ 2,154

May 31, 2008 and 2007

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## 8. Long Term Debt – continued

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(a) On November 30, 2005 a subsidiary of the Company issued three unsecured convertible notes with a face value of \$ 1,050 pursuant to the acquisition of the 10% net profit interest over key tenements within the Minas de Corrales project. The three convertible notes are payable on or before July 30, 2006, July 30, 2007 and July 30, 2008 respectively. Each convertible note can be converted into 250,000 ordinary shares during a 30 day period prior to the final payment date for each installment. No interest accrues on the notes. As a part of the agreement, an additional \$ 1,050 is also payable after the third anniversary date if the average monthly price of gold for the previous 36 months exceeds \$ 400 per ounce. Management believes this condition has been met and the additional contingent payment has been recognized as a liability.

The two unsecured convertible notes expiring July 30, 2006 and 2007 were paid in cash and not converted into shares. The remaining convertible note plus the additional contingent payment (for a total nominal value of \$ 2,100) are shown recorded at their net present value using an 8.5% discount rate.

The remaining debt was finally settled in cash in July 2008.

(b) On May 31, 2006 a subsidiary of the Company signed a financial lease facility agreement of \$ 500 with ABN AMRO N.V. Sucursal Montevideo for the purchase of light vehicles. The facility is payable in equal monthly installments over a three year period at 180 days LIBOR plus 2.5% rate of interest. As at 31 May 2008, \$ 212 has been drawn under this facility. The vehicles purchased are included under Property, Plant and Equipment.

(c) Long term debt repayments are as follow:

Year ending	Net profit interest debt Nominal Value	Lease installments Nominal value
2009	\$ 2,100	\$ 187
2010	---	25
Total	<u>\$ 2,100</u>	<u>\$ 212</u>

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## 9. Asset Retirement Obligations

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The Company's asset retirement obligations relates to the retirement and remediation of the San Gregorio Operation.

The asset retirement obligations have been recorded as a liability at estimated fair value determined by calculating the net present value of estimated future costs, assuming a weighed average cost of capital of 8.5% (2007 – 8.5%) and an inflation factor of 3.4% (2007 – 2.7%).

The following table summarizes the movements in the asset retirement obligation for the years ended May 31, 2008 and 2007.

May 31, 2008 and 2007

**9. Asset Retirement Obligations - continued**

	2008	2007
Balance at beginning of year	\$ 2,036	\$ 1,665
Changes in cash flow estimates	735	350
Accretion expense	98	21
Balance at end of year	\$ 2,869	\$ 2,036

Management's estimates of future cash flows were revised during the year due to the appreciation of the Uruguayan peso against the United States dollar and additional rehabilitation costs of \$316. The liability for the asset retirement obligation on an undiscounted basis is estimated to be approximately \$ 3,347 of which approximately \$ 2,706 are expected to be incurred from 2012.

Uruguayan mining and environmental legislation requires environmental obligations to be supported by guarantees. As a result, a rehabilitation guarantee letter of credit of \$1,500 (2007 - \$1,500) has been provided by Macquarie Bank.

**10. Equity Instruments**

(a) Authorized: Unlimited number of Common Shares of no par value

(b) Warrants issued for farm-in agreements: On March 23, 2007 in accordance with an agreement with Delcosur (note 7a), the Company issued 20,000 non-transferable warrants to purchase common shares of the Company at an exercise price of CDN\$ 4.56, and exercisable for a period of two years from the date of issuance. The fair value of these warrants was estimated using the Black Scholes option pricing model with the following assumptions: Dividend yield (CDN\$ 0.035), Expected volatility (41%), risk free rate (3.97%) and a weighed average life of two years. As such, a fair value of \$ 12 was attributed to these warrants. The warrants are exercisable as follows:

Number of Warrants	Warrant Price CDN\$	Expiry Date
20,000	4.56	March 23, 2009

(c) Share repurchase: The Company intends to buy back, under a normal course issuer bid and over calendar year 2008, up to an equivalent of CDN\$ 2 million of its common shares for cancellation, if shares are considered to be at a price significantly lower than the Company's fair value. Up to date the following repurchase of share transactions were held:

Number of shares repurchased	Weighted average market price (CDN\$)	Total invested
130,400	3.16	406

(d) Net profit interest acquisition convertible notes: The Company issued three convertible notes that provided the holder with the option to convert the note, with a face value of \$ 1,050, into 250,000 ordinary shares. The note may be converted during a 30 day period prior to the expiry

May 31, 2008 and 2007

## 10. Equity Instruments - continued

date. The fair value of the option to convert the notes into ordinary shares was calculated as the difference between the nominal and fair value of the notes.

The convertible notes expire as follows:

Ordinary shares to be issued on conversion of promissory note	Option price (CDN\$)	Expiry date
250,000	4.20	July 30, 2008

The first two convertible notes expired in July 30, 2006 and 2007 and were not exercised.

- (e) Warrants issued in satisfaction of financing fee: During August 2004, the Company issued 250,000 warrants at an exercise price of CDN\$3.75 per share in satisfaction of a financing fee on the facilities granted by Macquarie Bank Limited. The fair value of these options was estimated using the Black Scholes option pricing model with the following assumptions: Dividend yield (nil), Expected volatility (40%), risk free rate (3%) and a weighed average life of 2 years. As such a fair value of \$ 188 was attributed to these warrants. The warrants were exercised during 2007.
- (f) Employee stock options: The Company has an option Plan for its officers, directors, employees and consultants of the Company and its subsidiaries. Options under the plan are typically granted in such numbers as reflects the responsibility of the particular optionee and his or her contribution to the business and activities of the Company. Options granted under the plan have a term of up to 5 years. Except in specified circumstances, options are not assignable and terminate on the optionee ceasing to be employed by or associated with the Company. The terms of the Plan further provide that the price at which shares may be issued under the Plan cannot be less than the market price (net of permissible discounts) of the shares when the relevant options were granted. Options vest lineally over a three year period starting on the first year anniversary after granted.

The weighted average fair values of all stock options granted during 2008 and 2007 were CDN\$ 4.26 and CDN 6.10 respectively, estimated as of the date of grant using the Black-Scholes option pricing model with the following average assumptions:

	2008	2007
Expected option life (years)	3.1	Range of 3.5 to 4 except for options granted to contractors for which the term of the contract was considered 3.0
Volatility	42%	Range of 41% to 54%
Risk-free interest rate	Range of 4.22% to 4.28%	Range of 3.45% to 4.30%
Dividend yield	CDN\$0.055	Range of Nil to CDN\$0.035

During the year \$ 792 (2007 - \$ 975) of compensation expense was recorded. At May 31, 2008 the aggregate unamortized fair value of unvested stock options granted amounted to \$ 879 (2007 - \$1,181).

The following table summarizes information regarding the Company's outstanding options at May 31, 2008:

**Uruguay Mineral Exploration Inc.**  
**Notes to Consolidated Financial Statements**  
Thousands of United States Dollars, except where indicated

May 31, 2008 and 2007

**10. Equity Instruments - continued**

	Number of Shares (000's)	Option Price per Share Range CDN \$	Weighted Average Exercise Price CDN \$
Balance at May 31, 2007	3,304	\$0.75 - \$5.50	\$4.06
Options – granted	824	\$3.15 - \$3.30	\$3.28
Options – exercised and forfeited	(1,269)	\$0.75 - \$5.29	\$3.71
Balance at May 31, 2008	<u>2,859</u>	\$3.00 - \$5.50	\$3.99

The following table summarizes information regarding the Company's outstanding options at May 31, 2007:

	Number of Shares (000's)	Option Price per Share Range CDN \$	Weighted Average Exercise Price CDN \$
Balance at May 31, 2006	2,567	\$0.40 - \$5.50	\$3.03
Options – granted	1,601	\$3.45 - \$5.29	\$4.29
Options – exercised and forfeited	(864)	\$0.40 - \$4.50	\$1.42
Balance at May 31, 2007	<u>3,304</u>	\$0.75 - \$5.50	\$4.06

At May 31, 2008 there were 2,859,000 options outstanding, of which 1,216,000 are exercisable. The weighted average exercise price of the options outstanding at May 31, 2008 is CDN\$3.99 (May 31, 2007 CDN\$4.06)

The following table summarizes information about the stock options outstanding at May 31, 2008:

<b>Outstanding</b>				<b>Exercisable</b>	
Range of option price CDN \$	Options 000s	Weighted average Exercise Price CDN \$	Weighted average remaining contractual life Years	Options 000s	Weighted average Exercise Price CDN \$
0.00 – 3.00	75	3.00	1.01	75	3.00
3.01 – 4.00	1,835	3.60	3.57	494	3.88
4.01 – 5.00	690	4.57	2.48	407	4.55
5.01 – 5.50	259	5.42	1.80	240	5.42
	<u>2,859</u>			<u>1,216</u>	

The following table summarizes information about the stock options outstanding at May 31, 2007:

May 31, 2008 and 2007

## 10. Equity Instruments - continued

Option Range of option price CDN \$	Outstanding			Exercisable	
	Options 000s	Weighted average Exercise Price CDN \$	Weighted average remaining contractual life Years	Options 000s	Weighted average Exercise Price CDN \$
0.00 – 3.00	461	1.81	1.41	461	1.81
3.01 – 4.00	1,200	3.76	3.95	260	3.86
4.01 – 5.00	963	4.55	3.47	344	4.51
5.01 – 5.50	380	5.34	3.57	641	5.33
	<u>3,304</u>			<u>1,706</u>	

## 11. Commitments and contingencies

- (a) On May 22, 2007 the Company executed with ABN AMRO NV Sucursal Montevideo a guarantee letter by which a line of credit of \$2,500 was granted to the Company to be used for trade facilities, leasing, issuance of guarantees and general purposes. As of May 31 2008, \$ 212 was drawn for leasing, and \$ 1,634 was used for the issuance of guarantees for mining permits.
- (b) Commitments and contingencies for exploration farm in agreements exploration assets acquisitions are shown in note 7.

## 12. Income Taxes

- (a) The provision for income tax differs from the weighted average statutory tax rates as follows:

	2008	2007
Income before taxes	\$ 8,680	\$ 17,604
Income tax rate	35%	35%
Expected income tax expense	3,038	6,161
Tax effect of:		
Permanent differences	287	1,358
Inflation adjustment	(981)	(58)
Foreign exchange revaluation	(3,860)	(478)
Investment incentives (Notes 13 (e) and (f))	(322)	(1,923)
Tax losses not recognized / (utilized)	2,795	(2,507)
Other differences	(75)	497
Income tax expense	<u>\$ 882</u>	<u>\$ 3,050</u>

May 31, 2008 and 2007

**12. Income Taxes – continued**

(b) The following table sets out changes in the future income tax asset for the current year:

	<u>2008</u>	<u>2007</u>
Balance beginning of year	\$ 2,387	\$ 1,855
Recognized future tax (expense)	<u>2,988</u>	<u>532</u>
Balance end of year	<u>\$ 5,375</u>	<u>\$ 2,387</u>

The significant components of the Company's future income tax asset are as follows:

	<u>2008</u>	<u>2007</u>
Operating loss carry forwards	\$ 0	\$ 434
Closure provisions	0	431
Inventory	391	191
Deferred stripping	(587)	(1,208)
Royalty payable	195	177
Property plant and equipment and mine properties	<u>5,376</u>	<u>2,362</u>
Net future income tax asset	<u>\$ 5,375</u>	<u>\$ 2,387</u>

(c) Un-recognized tax benefits

At May 31, 2008 the Company had non capital loss carry forwards of \$ 9,662 (\$ 6,731, \$ 884 and \$ 2,047 in Uruguay, Barbados, and Canada tax jurisdictions respectively). The losses at gross value in the following jurisdictions and expire as follows:

	<u>Canada</u>	<u>Uruguay</u>	<u>Barbados</u>
Year to 31 May 2011	-	6,371	-
Year to 31 May 2017	-	-	884
Year to 31 May 2026	944	-	-
Year to 31 May 2027	<u>1,103</u>	<u>-</u>	<u>-</u>
	<u>\$ 2,047</u>	<u>\$ 6,371</u>	<u>\$ 884</u>

In Uruguay the Company has exploration deferred costs which result in available tax pools of \$ 9,752 (2007 – \$ 13,612) in exploration and development expenditures, which may be deductible against tax derived from future production income from the related properties. The deductibility of these expenditures will be based on the life of the reserves brought into production. In addition, the Company can seek tax relief for certain projects under existing Uruguayan legislation. Such relief may be granted on a project-by-project basis. It is the Company's intention to make application for such relief for projects as they near production.

(d) As a result of the Arenal project being granted national interest status under Uruguayan Investment Law, tax benefits have been granted on capital investments and utilized over the 2

May 31, 2008 and 2007

## 12. Income Taxes – continued

fiscal periods ended 2006 and 2007. The benefits utilized include a deferral of \$ 9,656 in taxable income to 2010. At the current tax rate of 25% this is equivalent to a deferred tax payment of \$ 2,414. The tax liability is shown as non current under “Long term tax payable”.

- (e) During the year other tax benefits applicable to investments in Uruguay were utilized determining a reduction of taxable income for \$ 1,073 (2007 - \$ 1,800)

## 13. Segmented Information

The Company has three reportable segments: gold, exploration and corporate. The corporate segment is responsible for corporate financing and other business development activities for the Company. The gold segment operates the San Gregorio gold mine and the exploration segment is devoted to the acquisition and exploration of mineral properties. The gold and exploration segments operate solely in Uruguay. Precious metals are refined and sold in Europe.

	2008			
	Gold	Exploration	Corporate	Total
Net Sales	\$ 79,061	\$ -	\$ -	\$ 79,061
Amortization and depletion	\$ 15,084	\$ 640	\$ -	\$ 15,724
Capitalized exploration write-off	\$ -	\$ 11,103	\$ -	\$ 11,103
Net Interest gain (loss)	\$ 346	\$ -	\$ -	\$ 346
Income tax	\$ 882	\$ -	\$ -	\$ 882
Net income gain (loss)	\$ 23,551	\$ (13,904)	\$ (1,849)	\$ 7,798
Property, plant and equipment	\$ 27,214	\$ 1,232	\$ 1,235	\$ 29,681
Deferred exploration and development	\$ -	\$ 8,948	\$ -	\$ 8,948
Capital Expenditure	\$ 8,834	\$ 325	\$ -	\$ 9,159
	2007			
	Gold	Exploration	Corporate	Total
Net Sales	\$ 63,056	\$ -	\$ -	\$ 63,056
Amortization and depletion	\$ 7,923	\$ 438	\$ -	\$ 8,361
Capitalized exploration write-off	\$ -	\$ 2,129	\$ -	\$ 2,129
Net Interest gain (loss)	\$ 196	\$ -	\$ -	\$ 196
Income tax	\$ 3,050	\$ -	\$ -	\$ 3,050
Net income (loss)	\$ 20,300	\$ (4,230)	\$ (1,516)	\$ 14,554
Property, plant and equipment	\$ 27,507	\$ 1,972	\$ 1,235	\$ 30,714
Deferred exploration and development	\$ -	\$ 16,316	\$ -	\$ 16,316
Capital Expenditure	\$ 10,958	\$ 8,468	\$ -	\$ 19,426

May 31, 2008 and 2007

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## 14. Financial Instruments

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The Company's activity exposes it to a variety of financial risks, mainly to commodity price risk and currency risk. The Company overall risk management programme focuses on the unpredictability of financial markets and seeks to minimize potential adverse effects on the Company financial performance.

- (a) Commodity Price Risk: The Company previously used financial derivatives to mitigate the effect of certain risks that are inherent in its business. As at May 31, 2008 the Company has settled all of its gold option contracts it has entered in the past to reduce its exposure to fluctuations in the gold price.
- (b) Currency risk: The Company operates internationally and is exposed to foreign exchange risk arising from various currency exposures, primarily with respect to its functional currency, the US dollar. Foreign exchange risks arise from future commercial transactions, recognized assets and liabilities an net investments in foreign operations.

Cash balances are held principally in US dollars, while its expenses are incurred in Uruguay pesos as well as US dollars and other currencies. The Company reports its results in United

States dollars. There would be an adverse impact on the reported results if the following situations arise:

- (i) The Uruguay inflationary impact on the peso expenses increases at more than the depreciation of the Uruguay peso against the United States dollar. This would result in an increase of the peso-based expenses.
- (ii) The United States dollar depreciates against the Uruguay peso. This would reduce the available cash resources and increase the related expense.

A significant portion of the Company's operations are located in Uruguay, and are subject to fluctuations in exchange rates. The Company manages its currency rate risk by denominating its contracts and commitments, where possible, in US dollars

- (c) Fair value: The Company's financial instruments include cash and cash equivalents, receivables, accounts payable, accrued liabilities and debt. Unless otherwise noted, it is management's opinion that the Company is not exposed to significant interest, currency or credit risks arising from these financial instruments. The fair value of these financial instruments approximates their carrying values, unless otherwise noted.
- (d) Interest rate risk: The majority of the Company's debt is non interest bearing

May 31, 2008 and 2007

#### 14. Financial Instruments -continued

(e) Credit risk: The Company is exposed to credit risk with respect to managing its cash position. This risk, from deposit granting institutions and/or commercial paper issuers, is mitigated by using well capitalized financial institutions. Credit risk relating to accounts receivable arises from the possibility that any counterparty to an instrument may fail to perform. The Company currently transacts with highly-rated counterparties for the sale of gold. Counterparties include its current lenders.

(f) Capital management: The Company manages its capital to ensure that the Company and its subsidiaries will be able to continue as a going concern while attempting to maximize the return to shareholders through the optimization of a reasonable debt and equity balance commensurate with current operating requirements. The strategy remains unchanged from 2007. The Company raises capital, as necessary, to meet its needs and take advantage of perceived opportunities and, therefore, does not have a numeric target for its capital structure.

(g) Insurance

The Company purchases limited discretionary insurance to cover catastrophic property damage, business interruption and liability risk.

#### 15. Statement of Cash Flows

(a) The net change in non-cash working capital items is as follows:

	<u>2008</u>	<u>2007</u>
Accounts receivable	\$ (535)	\$ (576)
Prepaid expenses	(357)	(35)
Inventories	(8,265)	(287)
Accounts payable and accrued liabilities	2,578	2,079
	<u>\$ (6,579)</u>	<u>\$ 1,181</u>

(b) Supplementary cash flow information:

	<u>2008</u>	<u>2007</u>
Cash income tax paid	\$ -	\$ -
Cash interest paid	\$ 119	\$ 155

May 31, 2008 and 2007

**16. Basic & Diluted earnings per share**

The reconciliation of basic and diluted earnings per share where relevant are as follows:

	<u>2008</u>	<u>2007</u>
<b>Basic earnings per share</b>		
Numerator		
Net earnings available to shareholders	\$ 7,798	\$ 14,554
nominator		
Weighted average shares outstanding	48,911,779	48,258,892
Basic earnings per share (cents per share)	0.16	0.30

	<u>2008</u>	<u>2007</u>
<b>Diluted earnings per share</b>		
Numerator		
Net earnings available to shareholders	\$ 7,798	\$ 14,554
Denominator		
Weighted average shares outstanding	48,911,779	48,258,892
Potential net incremental issue of shares from warrants	0	20,833
Potential net incremental issue of shares from stock options	12,293	138,544
Potential net incremental issue of shares from convertible notes	0	250,000
Shares outstanding plus assumed conversions	<u>48,924,272</u>	<u>48,668,269</u>
Diluted earnings per share (cents per share)	0.16	0.30

Basic earnings per common share ("EPS") have been calculated using the weighted-average number of shares outstanding during the year. The calculation of diluted earnings per common share has been computed using the treasury stock method which assumes that options and warrants with an exercise price lower than the average quoted market price were exercised at the beginning of the year, or at time of issue. In applying the treasury stock method, options and warrants with an exercise price greater than the average quoted market price of the common shares are not included in the calculation of diluted earnings per common share as the effect is anti-dilutive. The average quoted market price of the common shares during the year ended May 31, 2008 was CDN\$3.14 (2007 - CDN\$3.95).