DEFIANCE SILVER CORP.

(an exploration stage company)

CONSOLIDATED FINANCIAL STATEMENTS

FOR THE QUARTER ENDED

DECEMBER 31, 2012

(expressed in Canadian dollars)

DEFIANCE SILVER CORP.
CONSOLIDATED STATEMENTS OF FINANCIAL POSITION
December 31, 2012
(Canadian dollars)

	December 31, 2012	June 30, 2012
ASSETS		
Current assets		
Cash *(Note 3)*	$ 431,405	$ 339,848
Receivables *(Note 4)*	102,020	38,803
Advances and prepaid expenses	7,856	2,143
	541,281	380,794
Mineral property interests *(Note 5)*	1,882,925	1,619,110
	$ 2,424,206	$ 1,999,904
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities		
Accounts payable and accrued liabilities *(Note 7)*	$ 235,669	$ 317,723
Shareholders' equity		
Share capital *(Note 6)*	4,108,794	3,253,665
Share subscription received	-	30,000
Reserves	371,726	219,777
Deficit	(2,291,983)	(1,821,261)
	2,188,537	1,682,181
	$ 2,424,206	$ 1,999,904

Nature and continuance of operations (Note 1)

On behalf of the Board:

"Darrell A. Rader"	*"Bruce Winfield"*
Darrell A. Rader	Bruce Winfield

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

DEFIANCE SILVER CORP.
CONSOLIDATED STATEMENTS OF OPERATIONS & COMPREHENSIVE LOSS
For the three months and six months ended December 31
(Canadian dollars)

	Three months ended		Six months ended	
	2012	2011	2012	2011
EXPENSES				
Investor relations and promotion	$ 6,462	$ 14,222	$ 19,929	$ 25,216
Legal and audit	28,615	17,340	39,414	66,657
Management fees	95,927	77,576	175,169	116,396
Office and administration	28,752	10,787	42,624	14,356
Project evaluation	1,937	1,907	1,937	3,626
Share- based compensation	151,949	-	151,949	-
Travel	7,040	7,420	14,090	16,902
Transfer agent and filing fees	5,576	14,295	6,100	20,594
LOSS BEFORE OTHER ITEMS	(326,258)	(139,547)	(451,212)	(263,747)
Write-off mineral property interest	-		-	(60,750)
Loss on foreign exchange	(1,571)	(1,908)	(20,709)	(701)
Interest income	1,094	532	1,199	1,472
NET LOSS AND COMPREHENSIVE LOSS FOR THE PERIOD	$ (326,735)	$ (140,923)	$ (470,722)	$ (323,726)
Loss per common share - basic and diluted	$ (0.01)	$ (0.01)	$ (0.02)	$ (0.03)
Weighted average number of common shares outstanding- basic and diluted	21,797,750	10,363,654	19,914,799	9,680,469

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

DEFIANCE SILVER CORP.
CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY
(Canadian dollars)

	Number of Shares	Share Capital	Share Subscriptions Received	Reserves	Deficit	Total
Balance, June 30, 2011	13,406,250	1,241,927	-	181,177	(600,591)	822,513
Shares issued for:						
Mineral property Interests	150,000	40,000	-	-	-	40,000
Net loss for the period	-	-	-	-	(323,726)	(323,726)
Balance, December 31, 2011	13,556,250	1,281,927	-	181,177	(924,317)	681,710
Shares issued for:						
Mineral property Interests	2,680,500	1,410,665	-	-	-	1,410,665
Private placement	1,144,500	572,250	-	-	-	572,250
Share issue costs	-	(11,177)	-	-	-	(11,177)
Share-based compensation	-	-	-	38,600	-	38,600
Share subscriptions Received	-	-	30,000	-	-	30,000
Net loss for the period	-	-	-	-	(896,944)	(896,944)
Balance, June 30, 2012	17,381,250	$ 3,253,665	$ 30,000	$ 219,777	$ (1,821,261)	$ 1,682,181
Shares issued for:						
Private placement	4,416,500	883,300	(30,000)	-	-	853,300
Share issue costs	-	(28,171)	-	-	-	(28,171)
Share-based compensation	-	-	-	151,949	-	151,949
Net loss for the period	-	-	-	-	(470,722)	(470,722)
Balance, December 31, 2012	21,797,750	$ 4,108,794	$ -	$ 371,726	$ (2,291,983)	$ 2,188,537

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

DEFIANCE SILVER CORP.
CONSOLIDATED STATEMENTS OF CASH FLOWS
For the six months ended December 31
(Canadian dollars)

		2012		2011
Operating Activities				
Net loss for the period	$	(470,722)	$	(323,726)
Adjustments for:				
Write-off of mineral property interest		-		60,750
Share-based compensation		151,949		-
Interest expense		-		-
Net changes in non-cash working capital items:				
Receivables		(63,217)		(14,071)
Advances and prepaid expenses		(5,712)		6,680
Accounts payables & accrued liabilities		(82,055)		86,767
Cash used in operating activities		(469,757)		(183,610)
Investing Activities				
Expenditures on mineral property interests		(263,815)		(140,012)
Cash used in investing activities		(263,815)		(140,012)
Financing Activities				
Share capital issued for cash (net of share issue costs)		825,129		-
Cash provided by financing activities		825,129		-
Increase (Decrease) in Cash		91,557		(323,622)
Cash – Beginning of Period		339,848		453,955
Cash – End of Period	$	431,405	$	130,333

Supplemental disclosure with respect to cash flows (Note 9)

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

1. NATURE AND CONTINUANCE OF OPERATIONS

The Company was incorporated on July 19, 2007 under the Business Corporations Act of the Province of British Columbia under the name Defiance Capital Corp. The name was changed to Defiance Silver Corp. in June 2011. The Company's principal business is the acquisition, exploration and development of mineral properties. The Company's registered and records office is at Suite 700, 625 Howe Street, Vancouver, BC, V6C 2T6. The Company's head office is at Suite 1610, 409 Granville Street, Vancouver, BC, V6C 1T2.

During the year ended June 30, 2012, the Company's shareholders approved the stock split of the Company's common shares on the basis of three new shares in exchange for two old shares.. All references to number of common shares and per common share amounts have been retroactively restated to reflect this common share split.

At the date of these consolidated financial statements, the Company has not been able to identify a known body of commercial grade ore on any of its mineral property interests. The ability of the Company to realize the costs it has incurred to date on these mineral property interests is dependent upon the Company being able to identify a commercial ore body, to finance its exploration costs and to resolve any environmental, regulatory or other constraints which may hinder the successful development of the mineral property interest. To date, the Company has not earned revenues and is considered to be in the exploration stage.

These consolidated financial statements have been prepared assuming the Company will continue on a going-concern basis. The Company has incurred losses since inception and the ability of the Company to continue as a going-concern depends upon its ability to develop profitable operations and to continue to raise adequate financing. Management is actively targeting sources of additional financing through alliances with financial, exploration and mining entities, or other business and financial transactions which would assure continuation of the Company's operations and exploration programs. In order for the Company to meet its liabilities as they come due and to continue its operations, the Company is solely dependent upon its ability to generate such financing. These material uncertainties may cast significant doubt on the Company's ability to continue as a going concern.

2. BASIS OF PREPARATION

This condensed interim consolidated financial information for the six months ended December 31, 2012, has been prepared in accordance with IAS 34, 'Interim Financial Reporting'. The condensed interim consolidated financial information should be read in conjunction with the annual financial statements for the year ended June 30, 2012, which have been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB").

These unaudited condensed interim consolidated financial statements have been prepared using accounting policies consistent with those used in the Company's annual financial statements for the year ended June 30, 2012,

The financial statements were authorized for issue by the Board of Directors (the "Board") on February 25, 2013.

The preparation of these consolidated financial statements requires management to make certain estimates, judgments and assumptions that affect the reported amounts of assets and liabilities at the date of the consolidated financial statements and the reported expenses during the period. Actual results could differ from these estimates.

Significant assumptions about the future and other sources of estimation uncertainty that management has made at the end of the reporting period, that could result in a material adjustment to the carrying amounts of assets and liabilities in the event that actual results differ from assumptions made, relate to, but are not limited to, the following:

i) The recoverability of receivables which are included in the consolidated statements of financial position;

ii) The carrying value and the recoverability of mineral property interests, which are included in the consolidated statements of financial position;

iii) The inputs used in accounting for share-based compensation expense, which are included in the consolidated statements of operations & comprehensive loss; and

(Canadian Dollars)

2. BASIS OF PREPARATION (cont'd…)

iv) The amount of deferred income taxes recognized.

Basis of consolidation

These consolidated financial statements include the financial statements of the Company and the entities controlled by the Company. Control exists when the Company has the power, directly or indirectly, to govern the financial and operating policies of an entity so as to obtain benefits from its activities. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases. All intercompany transactions and balances have been eliminated.

Subsidiaries

Subsidiaries are entities controlled by the Company. Control exists when the Company has the power, directly or indirectly, to govern the financial and operating policies of an entity so as to obtain benefits from its activities. Where necessary, adjustments are made to the financial statements of subsidiaries to bring their accounting policies into line with those used by the Company.

The principal subsidiaries of the Company as of December 31, 2012 are as follows:

Name of subsidiary	Principal activity	Place of Incorporation	Ownership Interest December 31, 2012	Ownership Interest June 30, 2012
Minera Santa Remy S.A. de CV	Mineral property exploration	Mexico	100%	100%
DefCap (BVI) Inc.	Holding company	British Virgin Islands	100%	100%

3. CASH

Cash consists of the following:

	December 31, 2012	June 30, 2012
Cash on deposit	$ 40,042	$ 299,684
Liquid short-term deposit	391,363	40,164
	$ 431,405	$ 339,848

4. RECEIVABLES

The Company's receivables arise mainly from refundable sales tax receivable from government taxation authorities. These are broken down as follows:

	December 31, 2012	June 30, 2012
Harmonized sales tax ("HST")	$ 40,284	$ 30,845
Value added tax ("VAT")	61,015	6,140
Other	721	1,818
	$ 102,020	$ 38,803

(Canadian Dollars)

5. MINERAL PROPERTY INTERESTS

Title to mineral property interests involves certain inherent risks due to the difficulties of determining the validity of certain claims as well as the potential for problems arising from the frequently ambiguous conveyancing history characteristic of many mineral claims. The Company has investigated title to all of its mineral property interests and, to the best of its knowledge, title to all of its interests are in good standing.

	Santa Gabriela Project	San Acacio Project	Minerva Property	Storm Property	Santa Elena Property	Total
Acquisition costs						
Balance, July 1, 2011	-	-	-	229,304	60,750	290,054
Additions during the year	1,455,880	82,090	9,574	50,000	-	1,597,544
Written-off during the year	-	-	-	(279,304)	(60,750)	(340,054)
Balance, June 30, 2012	1,455,880	82,090	9,574	-	-	1,547,544
Additions during the period		191,351				191,351
Balance, December 31, 2012	1,455,880	273,441	9,574	-	-	1,738,895
Exploration costs						
Balance, July 1, 2011	-	-	-	97,754	-	97,754
Additions during the year:	13,185	44,707	13,674	31,134	-	102,700
Written-off during the year	-	-	-	(128,888)	-	(128,888)
Balance, June 30, 2012	13,185	44,707	13,674	-	-	71,566
Additions during the period:						
Claim fees	-	-	-	-	-	-
Consulting fees	22,067	7,054	-	-	-	29,121
Camp fees	5,234	5,233	-	-	-	10,467
Due diligence	-	-	-	-	-	-
Extraction fees	11,305	11,305	-	-	-	22,610
Geology & mapping fees	3,917	6,349	-	-	-	10,266
	55,708	74,648	13,674	-	-	144,030
Balance, December 31, 2012	$ 1,511,588	$ 348,089	$ 23,248	$ -	$ -	$ 1,882,925

Santa Gabriela Project

The Company entered into an option agreement on September 9, 2011 (the Execution Date) with IMPACT Silver Corp. ("Impact") for the acquisition of the Santa Gabriela mill in Zacatecas, Mexico. The Company and IMPACT are related by way of one common director. The Santa Gabriela mill consists of the Santa Gabriela (formerly Veta Grande) processing plant, and associated surface rights as well as a 100% interest in 10 mining claims and a 27% interest in 3 concessions under joint venture with an arm's length party. Subsequently the Company and IMPACT agreed to exclude the 27% interest in the three concessions.

Terms of the agreement for the Company to exercise the option to purchase the assets from IMPACT include:

- Issuance of 2,680,500 shares of the Company to IMPACT (issued with a value of $1,420,665);
- Payment of $1,955,200 on the earlier of (a) 24 months from the Execution Date; or (b) on the plant reaching commercial production. Commercial production is defined as the first day after the Mill has achieved a production rate averaging 160 tonnes per day over a 30 day period.

5. MINERAL PROPERTY INTERESTS (cont'd…)

San Acacio Project

The Company entered into an option agreement on October 24, 2011 with the Mexican owners ("the Vendors") for an option to purchase a 100% interest in the San Acacio property consisting of 10 mining concessions and associated surface rights and tailings deposit ("the Assets"). The San Acacio property is located approximately 6.5 km north of the city of Zacatecas, Mexico and is in close proximity to the Company's Santa Gabriela mill.

Terms of the original option to purchase agreement are as follows:

- Payment of US$25,000 (paid) for an initial 90 day due diligence period on the date of signing on October 24, 2011
- Optional Payment of US$50,000 (paid) for an additional 90 day due diligence extension from the initial 90 day due diligence period; and
- Payment of US$200,000 (paid) for a 12 month period from signing of the trust agreement in which to acquire the assets.

Purchase price of the Assets ("Final Payment") under the original option to purchase agreement consists of the following payments which are due one year from signing of the trust agreement:

- 10 mining concessions for US$5,500,000;
- 1 parcel of surface rights for US$ 5,000; and
- 1 parcel of land with a tailings deposit for US$1.50 per tonne of tailings estimated in the amount of 300,000 tonnes.

On July 25, 2012, the Company and the Vendors entered into an amending purchase agreement to extend the Final Payment. The terms of the amended purchase agreement are as follows:

- Payment of US$150,000 for a 24 month extension from the date of signing the trust agreement ("First Extension Period);
- Payment of US$225,000 for a 36 month extension from the date of signing the trust agreement ("Second Extension Period); and
- Final Payment for the Assets at the end of the selected extension period.

On September 27, 2012, the Company and the Vendors entered into the trust agreement with the initial 12 month option period set to expire on September 27, 2013.

The property is subject to a 2.5% net smelter return royalty ("NSR") payable to the vendors on production from the property. The Company will have the right to purchase the NSR at any time for US$2,500,000 which will escalate with the official Mexican Inflation Index after a five year period.

Following the first anniversary of the purchase of the Assets, the Company must make minimum annual royalty payments of US$125,000. The minimum royalty commitment terminates in the event that the production royalty paid is equal to or higher than the equivalent to the minimum that would have been due during 6 consecutive months.

Minerva property

During the year ended June 30, 2012, the Company staked a mining claim located in Coahuila State, Mexico, known as the Minerva property.

Storm Property

On August 6, 2009, the Company received approval from the TSX-V (the "Approval date"), which fulfilled its Qualifying Transaction requirement and entered into a Property Option Agreement, dated May 28, 2008, which was amended February 17, 2009, to acquire a 100% right, title and interest in 210 mineral claims referred to as the Storm Property located in Nevada, USA. The Company made the initial payment of US$10,000 (CA$11,034) to the optionor and issued 600,000 common shares with a value of $80,000. In addition to the aforementioned payments, the Company had to incur US$300,000 in exploration expenditures and was required to make cash payments and issue common shares to maintain the option.

5. MINERAL PROPERTY INTERESTS (cont'd…)

The Optionor retained a 3% net smelter returns royalty ("NSR") on all gold and silver produced from the property and a 2% NSR from all other minerals.

The Company decided to terminate the option agreement and accordingly the related acquisition and deferred exploration costs of $408,192 were written off in the year ended June 30, 2012.

Santa Elena Property

On May 20, 2011, the Company signed an assignment agreement with an individual ("the Assignor") to acquire a 100% interest in two mineral concessions, known as the Carina and Juanito claims, in the State of Zacatecas, Mexico. In consideration, the Company issued 225,000 common shares with a value of $60,750, and the assumption of existing option obligations. The two exploration concessions are optioned from two Mexican individuals for total option payments of US$315,000 plus value-added-tax ("VAT") over a period of three years.

After further evaluation, management decided not to renew the option agreement and wrote off the related costs of $60,750 during the six months ended December 31, 2011.

6. SHARE CAPITAL

Authorized

Unlimited number of common shares without par value. All issued shares are fully paid.

Private Placements

During the year ended June 30, 2012, the Company completed a private placement of 1,144,500 units at a price of $0.50 per unit for gross proceeds of $572,250. Each unit is comprised of one common share and one-half of one share purchase warrant with each whole warrant entitling the holder to purchase one additional common share for a period of twelve months from the date of closing at a price of $0.65 per share. In connection with the private placement, the Company incurred $11,177 in share issue costs.

During the quarter ended September 30, 2012, the Company closed a private placement with the issuance of 4,416,500 units at a price of $0.20 per Unit for gross proceeds of $883,300. Each Unit consists of one common share of the Company, one full common share purchase warrant ("Warrant") and one Silver Participation Right ("SPR"). Each Warrant will entitle the holder to purchase one common share of the Company for a period of 12 months at a price of $0.40 per share. Each Silver Participation Right will entitle the holder to receive 0.003 ounces of silver bullion. $30,000 in proceeds was received prior to June 30, 2012 and $853,000 was received during the six months ended December 31, 2012. The Company incurred $28,171 in share issue costs in connection with the private placement. All of the common shares issued in the private placement were placed in escrow as a condition to maintaining the SPR, however, 350,000 common shares have been released from escrow as the shareholders have renounced their SPR .

Escrow shares

At December 31, 2012, 4,066,500 (June 30, 2012 - 585,000) common shares are held in escrow in order to maintain the shareholders' silver Participation Rights.

Stock options

Under the Company's rolling stock option plan, the Company may grant options, with a maximum term of ten years, for up to 10% of the Company's issued and outstanding common shares, to directors, employees and technical consultants at exercise prices to be determined by the market value on the date of grant. The number of common shares reserved for issuance to any individual director or officer will not exceed 5% of the issued and outstanding common shares, and the number of common shares reserved for issuance to all technical consultants will not exceed 2% of the issued and outstanding common shares. Incentive stock options issued have an immediate vesting term.

(Canadian Dollars)

6. SHARE CAPITAL (cont'd…)

Stock options (cont'd…)

Stock option transactions and the number of stock options outstanding are summarized as follows:

	Number of Options	Weighted Average Exercise Price
Balance, June 30, 2011	1,080,000	0.25
Options granted	120,000	0.60
Balance, June 30, 2012	1,200,000	$ 0.29
Options granted	930,000	0.265
Balance, December 31, 2012	2,130,000	$ 0.28
Number of exercisable options	2,130,000	$ 0.28

At December 31, 2012, the following incentive stock options were outstanding to directors, officers and employees:

Number of Options Exercisable and Outstanding	Exercise Price	Expiry Date
405,000	$ 0.13	August 6, 2014
675,000	0.33	June 6 , 2016
120,000	0.60	December 19, 2016
680,000	0.265	November 22, 2017
250,000	0.265	December 10, 2017
2,130,000		

Warrants

Warrant transactions and the number of warrants outstanding are summarized as follows:

	Number of Warrants	Weighted Average Exercise Price
Balance, June 30, 2011	937,500	$ 0.32
Issued	572,250	0.65
Balance, June 30, 2012	1,509,750	$ 0.45
Issued	4,416,500	0.40
Warrants repriced from $0.65	(397,225)	(0.65)
Warrants repriced to $0.30	397,225	0.30
Balance, December 31, 2012	5,926,250	$ 0.37

(Canadian Dollars)

6. SHARE CAPITAL (cont'd…)

Warrants (cont'd…)

During the six months ended December 31, 2012, the Company repriced a total of 397,225 warrants from an exercise price of $0.65 per share to $0.30 per share. The expiry date for the warrants of April 17, 2013 was unchanged. At December 31, 2012, the following warrants were outstanding:

Number of Warrants	Exercise Price	Expiry Date
937,500	$ 0.21	April 15, 2013
397,225	0.30	April 17, 2013
175,025	0.65	April 17, 2013
2,741,500	0.40	September 20, 2013
1,675,000	0.40	September 27, 2013
5,926,250		

Share-based compensation

62he Company recognizes compensation for all stock options and warrants granted using the fair value based method of accounting. During the six months ended December 31, 2012, the Company granted a total of 930,000 options at an exercise price of $0.265 per share and recognized $151,949 in share-based compensation expense.

During the year ended June 30, 2012, the Company granted 120,000 (2011 – 675,000) stock options and recognized $38,600 (2011 – $136,913) in share-based compensation expense.

7. RELATED PARTY TRANSACTIONS

Related parties include the Board of Directors, officers, close family members and enterprises that are controlled by these individuals.

As at December 31, 2012, accounts payable and accrued liabilities include $62,360 (June 30, 2012 - $124,777) payable to directors, officers and companies controlled by directors and/or officers. Amounts payable to related parties have no specific terms of repayment, are unsecured and do not bear interest.

During the six months ended December 31, 2012, the Company:

(a) paid or accrued management fees of $67,500 (2011 – $59,460) to a company controlled by the CEO, President and director of the Company.

(b) paid or accrued management fees of $23,669 (2011 – $34,101) to an officer of the Company.

(c) paid or accrued management fees of $21,000 (2011 - $11,760) to a company controlled by a director of the Company

(d) paid or accrued management fees of $9,000 (2011 - $nil) to an officer of the Company.

8. CONVERTIBLE PROMISSORY NOTES

During the year ended June 30, 2012, the Company entered into convertible promissory note agreements with three non-arm's length lenders for a total principal amount of $120,000 ($40,000 from each lender). The loans bear interest at 10% per annum (if repayment is made within one year, the lenders will receive not less than one full year of interest on the principal). The loans are due within one year from the date of advance. At the election of the lenders, the loans are convertible into the Company's common shares at $0.50 per share.

The Company calculated the value of the equity portion of the convertible promissory notes and determined it to be immaterial for segregation between debt and equity on the statements of financial position.

The Company settled the convertible promissory notes with two lenders for a total cash payment of $88,000 ($80,000 towards the principal amount and $8,000 interest expense). The remaining outstanding principal amount of $40,000 was applied towards the private placement subscription for the benefit of the lender (80,000 shares issued for $40,000) and accrued interest of $4,000 which was repaid during the period ended September 30, 2012 with the proceeds used to subscribe for shares.

9. SUPPLEMENTAL DISCLOSURES WITH RESPECT TO CASH FLOWS

There were no significant non-cash transactions for the six months ended December 31, 2012.

Significant non-cash transactions for the six months ended December 31, 2011 included:

a) Issuance of 150,000 common shares with a value of $40,000 for mineral property interests.

10. SEGMENTED INFORMATION

The Company operates in one reportable operating segment, being the acquisition, exploration, and development of mineral properties in North America and Mexico. All mineral properties at June 30 and December 31, 2012 are in Mexico.

11. FINANCIAL AND CAPITAL RISK MANAGEMENT

Financial instruments measured at fair value are classified into one of three levels in the fair value hierarchy according to the relative reliability of the inputs used to estimate the fair values. The three levels of the fair value hierarchy are:

Level 1 – Unadjusted quoted prices in active markets for identical assets or liabilities;
Level 2 – Inputs other than quoted prices that are observable for the asset or liability either directly or indirectly; and
Level 3 – Inputs that are not based on observable market data.

The fair value of the Company's receivables, accounts payable and accrued liabilities, approximate carrying value, due to the short-term nature. The Company's other financial instrument, cash, under the fair value hierarchy, are based on level one quoted prices in active markets for identical assets or liabilities. The Company is exposed to varying degrees to a variety of financial instrument related risks:

Credit risk

Credit risk is the risk of an unexpected loss if a customer or third party to a financial instrument fails to meet its contractual obligations.

The Company's cash is held at large Canadian financial institutions in interest bearing accounts. The Company has no investment in asset backed commercial paper.

The Company's receivables consist mainly of HST/VAT due from the governments of Canada and Mexico. As such, the Company does not believe it is subject to significant credit risk.

11. FINANCIAL AND CAPITAL RISK MANAGEMENT (cont'd...)

Liquidity risk

The Company's approach to managing liquidity risk is to ensure that it will have sufficient liquidity to meet liabilities when due. As at December 31, 2012, the Company had cash of $431,405 (June 30, 2012 - $339,848) to settle current liabilities of $235,669 (June 30, 2012 - $317,723). Management needs to secure additional funding in order to meet its current liabilities and operating expenses as they become due while completing an equity financing.

Market risk

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

a) Interest rate risk

The Company has cash balances and interest-bearing investments. The interest earned on the investments approximates fair value rates, and the Company is not at a significant risk to fluctuating interest rates. The Company's current policy is to invest excess cash in investment-grade short-term deposit certificates issued by its financial institutions. The Company periodically monitors the investments it makes and is satisfied with the credit ratings of its banks. As at December 31, 2012, the Company had a total of $390,000 in investment-grade short-term deposit certificates.

The risk that the Company will realize a loss as a result of a decline in the fair value of the short-term investments included in cash is minimal because of the short-term nature of these investments.

b) Foreign currency risk

The Company is not exposed to significant foreign currency risk on fluctuations related to cash and accounts payable and accrued liabilities that are denominated in United States dollars ("US$") and Mexican peso ("MX$"). The Company does not use derivatives or other techniques to manage foreign currency risk.

c) Price risk

The Company is exposed to price risk with respect to commodity prices. Commodity price risk is defined as the potential adverse impact on earnings and economic value due to commodity price movements and volatilities. The Company closely monitors the commodity prices of precious metals, and the stock market to determine the appropriate course of action to be taken by the Company.

Based on management's knowledge and experience of the financial markets, management does not believe that the Company's current financial instruments will be affected by interest rate risk, currency risk and credit risk.

Capital management

The Company's objectives when managing capital are to safeguard the Company's ability to continue as a going concern in order to pursue the exploration and development of its mineral properties, acquire additional mineral property interests and to maintain a flexible capital structure which optimizes the costs of capital at an acceptable risk. In the management of capital, the Company includes components of shareholders' equity. The Company manages the capital structure and makes adjustments to it in light of changes in economic conditions and the risk characteristics of the underlying assets. To maintain or adjust the capital structure, the Company may attempt to issue new shares, issue debt, acquire or dispose of assets or adjust the amount of cash.

The Company currently is not subject to externally imposed capital requirements. There were no changes in the Company's approach to capital management.