**MANAGEMENT'S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS
FOR THE YEAR ENDED DECEMBER 31, 2013**

The following management's discussion and analysis of financial condition and results of operations ("MD&A") for the year ended December 31, 2013 prepared as of April 30, 2014, should be read in conjunction with the audited consolidated financial statements for the year ended December 31, 2013 and the related notes thereto of Santacruz Silver Mining Ltd. ("the Company" or "Santacruz") ("the 2013 Annual Financial Statements").

The referenced consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS"). All amounts are expressed in US dollars unless otherwise indicated.

Forward-Looking Statements
This MD&A and the documents incorporated herein by reference contain "forward-looking information" within the meaning of applicable Canadian securities regulations and "forwarding-looking statements" within the meaning of the United States Private Securities Litigation Reform Act of 1995 (collectively, "**forward-looking information**"). The forward-looking information contained in this MD&A is made as of the date hereof. Except as required under applicable securities legislation, the Company does not intend, and does not assume any obligation, to update forward-looking information.

Forward-looking information includes, but is not limited to, statements with respect to the future price of silver, gold and other metals and the effects thereof on the Company's mineral resources; statements relating to the potential mineralization and geological merits of the Company's Rosario mine (the "**Rosario Mine**"), San Felipe project (the "**San Felipe Project**") and Gavilanes property (the "**Gavilanes Property**" or "**Gavilanes Project**"), as described below; the Company's expected production and recoveries for its Rosario Mine; the expectations for the development of the main access ramp and the installation of a third ball to the milling facility at the Rosario Mine; expectations regarding the continuity of mineral deposits; the Company's goals regarding raising capital and developing its projects; the Company's proposed development and exploration plans for the San Felipe Project and the Gavilanes Property; timing of a preliminary economic assessment or a pre-feasibility study for the San Felipe Project; plans for drilling; expectations regarding environmental issues that may affect the exploration progress; project capital cost estimates; and the Company's other plans for development of its projects. Often, but not always, forward-looking information can be identified by the use of words such as "plans", "expects", "is expected", "budget", "scheduled", "estimates", "forecasts", "intends", "anticipates", or "believes" or the negatives thereof or variations of such words and phrases or statements that certain actions, events or results "may", "could", "would", "might" or "will" be taken, occur or be achieved.

This forward-looking information is based on certain assumptions that the Company believes are reasonable, including that: the Company is able to obtain any required government or other regulatory approvals and adequate financing to complete its current and future exploration and development programs; current gold, silver and base metal prices will not materially decrease; the proposed development of the Company's mineral projects will be viable operationally and economically and proceed as expected; the Company will not experience any material accident, labour dispute or failure of plant or equipment; any additional financing needed by the Company will be available on reasonable terms; that planned drilling at its mineral properties will be completed and that the results of such drilling will be sufficient to expand the existing resources at the Gavilanes Property consistent with management's expectations; that general business and economic conditions will not change in a material adverse manner; that the Company's exploration of its properties is not adversely affected by unexpected adverse weather conditions; that the estimates of the resources at the Rosario Mine, the San Felipe Project and the Gavilanes Project obtained by the Company are within reasonable bounds of accuracy (including with respect to size, grade and recovery); and that the Company's current exploration and development programs and objectives can be achieved.

Any financial outlook contained herein, as defined by applicable securities legislation, is provided for the purpose of providing information about management's current expectations and plans relating to the future. Readers are cautioned that reliance on such information may not be appropriate for other purposes.

Forward-looking information involves known and unknown risks, uncertainties and other factors which may cause the actual results, performance or achievements of the Company to be materially different from any future results, performance or achievements expressed or implied by the forward-looking information. Such factors include, among others, the risk that actual results of exploration activities will be different than anticipated, that cost of labour, equipment or materials increase more than expected, that the future price of silver, gold and base metals will decline, that mineral resources are not as estimated, that actual costs of reclamation activities are greater than expected; that changes in project parameters as plans continue to be refined result in increased costs, that lower rates of production are achieved than are expected, that unexpected variations in ore grade or recovery rates occur, that plant, equipment or processes fail to operate as anticipated, that accidents of labour disputes occur, that unanticipated delays occur in obtaining governmental approvals or financing or in the completion of development or construction activities, as well as those factors discussed in the section entitled "Risks and Uncertainties" in this MD&A, at pages 7 to 18 of the annual information form of the Company for the year ended December 31, 2012 dated November 19, 2013 (the "AIF"), filed on SEDAR on November 21, 2013. Although the Company has attempted to identify important factors that could cause actual actions, events or results to differ materially from those described in forward-looking information, there may be other factors that cause actions, events or results not to be as anticipated, estimated or intended. There can be no assurance that forward-looking information will prove to be accurate, as actual results and future events could differ materially from those anticipated in such statements. Readers are cautioned not to place undue reliance on forward-looking information due to the inherent uncertainty thereof.

General

Santacruz was incorporated pursuant to the Business Corporations Act of British Columbia on January 24, 2011. The Company's registered office is located at 10th Floor, 595 Howe Street, Vancouver, British Columbia, Canada V6C 2T5. The Company's shares are listed for trading on the TSX Venture Exchange under the symbol "SCZ".

The Company is engaged in the acquisition, exploration and development of mineral properties in Mexico, with a primary focus on silver, but also including gold, zinc and lead. The Company is currently focused on meeting and maintaining its primary production objective of producing approximately 2 million silver equivalent ounces on a yearly basis by the end of the second quarter of 2014 at its producing property, the Rosario Mine. In addition, the Company is exploring three other mineral properties, being the San Felipe Project (an advanced stage project), the Gavilanes Project (an exploration project), and the El Gachi Property (an early stage exploration project).

The Company's strategic objective is to become a mid-tier silver producer in Mexico. To achieve this objective, the Company is focused in the near term (mid 2014), on the following:

• Continuing to increase production at the Rosario Mine;

• Initiating preliminary development activities at the San Felipe Project; and

• Continuing exploration on the Gavilanes Property.

Recent Highlights

- On January 23, 2014, the Company filed a technical report in respect of a previously announced independent NI 43-101 Mineral Resource estimate on the Gavilanes Property with an effective date of November 13, 2013. The Mineral Resource estimate was prepared by Gary Giroux, P.Eng. of Giroux Consultants Ltd. and utilized a geological model completed by Hans Smit, P.Geo and Fletcher Bourke, P.Geo. See resource categories and further details in the section of this MD&A titled Gavilanes Property, San Dimas, Durango, Mexico.

- On March 17, 2014, the Company completed a prospectus offering (including the full exercise of an over-allotment option) for gross proceeds of CDN$12,062,500.

- On March 18, 2014, the Company reported that the main access ramp at the Rosario Mine had reached Level 2 and initial stope development on this level had begun.

2013 Highlights

- On February 19, 2013, the Company completed a prospectus offering for gross proceeds of CDN$40,422,500.

- On March 7, 2013, the Company announced that it had acquired the 48,057.33 hectare El Gachi Property located 30 kilometers from the San Felipe Project in Sonora State.

- On April 4 and June 13, 2013, the Company announced positive drilling results at the Gavilanes Project.

- On July 11, 2013, the Company announced that drilling at the San Felipe Project confirmed continuity of high-grade mineralization.

- On August 14, 2013, the Company announced that it had successfully renegotiated terms to acquire a 100% interest in the San Felipe Project and adjacent El Gachi Property.

- On September 12, 2013, the Company reported that the main access ramp at the Rosario Mine had intersected the Rosario I vein while a crosscut from the Northwest Ramp had intersected the Rosario II vein.

- On October 2 and 9, 2013, the Company reported additional results from the 2013 diamond drilling program being conducted on the San Felipe Project. The program continued to intercept high-grade mineralization.

Rosario Mine, Charcas, San Luis Potosi, Mexico

Operations Review

The Rosario Mine comprises the Rey David and San Rafael mining concessions located in the Municipality of Charcas in the State of San Luis Potosi, Mexico, 184 kilometres north of the capital city of San Luis Potosi. Details of the acquisition terms are contained in Note 11 of the 2013 Annual Financial Statements. The property covers 500 hectares.

On April 18, 2013, based upon the operating staff's assessment that the mill had demonstrated its ability to operate continually at rated capacity while maintaining forecasted recoveries, the Company announced that the Rosario Mine had achieved commercial production. Such consistent mill performance, however, does not in and of itself satisfy the definition of "commercial production" for accounting purposes pursuant to IFRS. For the year ended December 31, 2013, the IFRS definition of "commercial production" was not satisfied. Accordingly, the Company did not report the Rosario Mine's results of operations in its consolidated statement of loss for the year but instead capitalized the operating costs less proceeds from the sale of concentrates as "Mine under construction and development costs" on the Company's consolidated statement of financial position at December 31, 2013. Effective for the period commencing January 1, 2014 the Company will be reporting its results of operations from the Rosario Mine in its consolidated statement of operations.

Mining of the Rosario I vein from the Main Access Ramp commenced during the third quarter of 2013. The Company also developed the Northwest Ramp in order to expedite access to the Rosario I and II veins. A crosscut from the Northwest Ramp at Level 1 reached the Rosario II vein on September 5, 2013.

During the third quarter the Company began delivering lead and zinc concentrates to Metagri S.A. de C.V., a Mexican subsidiary of Glencore International AG, pursuant to separate agreements that run until December 2014.

During the fourth quarter of 2013 production levels at the Rosario Mine continued to increase. Milling facility throughput at the end of the fourth quarter was approximately 250 tpd. In addition, in mid-December the Company commenced development of the Main Access Ramp to Level 2. This work was completed in March 2014 and initial stope development on this level is scheduled to be completed during the second quarter of 2014. Further, during the first quarter of 2014, a sub-level has been developed to allow access to the R-30 zone, a newly discovered zone situated parallel and proximate to the Rosario I vein. Two working faces have been prepared on this zone which are providing mill feed at a grade in excess of the average resource estimate grades.

The Company is in the preliminary stages of installing a third ball mill to increase milling capacity from the current 300 tpd to 700 tpd. This project is expected to be completed in May 2014.

Management intends to maintain production from the Rosario Mine at approximately 500 tpd and utilize the excess capacity to source third party ore from local miners in order to increase overall production and generate further cashflow from operations.

Production Data

	Quarter Ended Dec. 31, 2013	Quarter Ended Mar. 31, 2014
Tonnes Milled – Rosario Ore	4172*	8,994
– Third Party Ore	4,414	-11,453
Head Grade – Ag (g/t)	107.53***	167
– Au (g/t)	0.07***	0.33
– Pb (%)	0.48***	1.02
– Zn (%)	1.13***	2.34
Recovery – Ag (%)	86.6	85.7
– Au (%)	69.7	77.3
– Pb (%)	84.4	89.7
– Zn (%)	82.5	76.8
Ag Equivalent Production – Ounces***	61,153	159,729
Production – Ag (ounces)	35,482	94,312
– Au (ounces)	66	166
– Pb (tonnes)	61	186
– Zn (tonnes)	165	367

* Low-grade oxide ore and/or development ore from the Rosario I vein.
** The reported recoveries reflect the fact that oxide material was included in the mill feed.
***Ag Equivalent Production Ounces =
((Au*Pau/31.1035)+(Ag*Pag/31.1035)+(Pb*Ppb*22.05)+(Zn*Pzn*22.05))/(Pag)
where metal prices are: Ag $20.49 (=Pag), Au $1,295.95 (=Pau), Pb $0.95 (=Ppb), Zn $0.91 (=Pzn)

Mineral Resource Estimate

With reference to the updated technical report on the Rosario Mine dated December 19, 2012 as prepared pursuant to NI 43-101 by Donald E. Hulse, P.E. and SME-RM and Patrick F. Daniels SME-RM of Gustavson Associates, LLC, ("Gustavson") which was filed on SEDAR at www.sedar.com on December 28, 2012, and remains current, Gustavson performed a combination of grid modeling and three dimensional block modeling and developed the mineral resource estimate for the Rosario Mine effective December 1, 2012. The cutoff for resource reporting is based on underground vein mining with long hole or shrinkage stoping with milling and flotation. Gustavson has assumed similar metallurgical recoveries for all metals. Gustavson is reporting the resources at a silver equivalent cutoff of 75g/t. The silver equivalent ("**AgEq**") calculation is described after the resource tables which follow.

Table 1-1 Rosario I Vein Mineral Resource Estimate at 75g/t AgEq

	TONNAGE	Thickness	Silver Equivalent		Gold		Silver		Lead		Zinc	
Classification	**k tonne**	**m**	**gpt**	**k-oz**	**gpt**	**oz**	**gpt**	**k-oz**	**pct**	**lbsx1000**	**pct**	**lbsx1000**
Measured	126.7	1.01	305	1,243.3	0.988	4,025	157.2	640.2	1.21	3,393.1	2.64	7,385.4
Indicated	408.4	0.85	273	3,579.4	0.904	11,873	136.0	1,785.7	1.14	10,306.5	2.43	21,911.8
Meas+Ind	535	0.88	280	4,822.7	0.924	15,898	141.0	2,425.9	1.16	13,699.6	2.48	29,297.2
Inferred	164.0	0.73	190	1,001.0	0.995	5,246	74.7	393.6	0.81	2,943.5	1.74	6,276.1

Table 1-2 Rosario II Vein Mineral Resource Estimate at 75g/t AgEq

	TONNAGE	Thickness	Silver Equivalent		Gold		Silver		Lead		Zinc	
Classification	**k tonne**	**m**	**gpt**	**k-oz**	**gpt**	**Oz**	**gpt**	**k-oz**	**pct**	**lbsx1000**	**pct**	**lbsx1000**
Measured	143.4	1.17	447	2,062.2	0.897	4,137	256.9	1,184.6	1.13	3,559.3	4.62	14,611.1
Indicated	302.6	1.10	345	3,351.3	0.852	8,286	198.6	1,932.5	1.22	8,123.7	2.82	18,778.6
Meas+Ind	446	1.12	378	5,413.5	0.955	12,423	217.4	3,117.1	1.19	11,683.0	3.40	33,389.7
Inferred	222.2	0.99	213	1,521.8	0.673	4,807	102.4	731.9	0.67	3,262.8	2.37	11,598.0

Table 1-3 Total Mineral Resource for Rosario I and II Veins at 75g/t AgEq

	TONNAGE	Thickness	Silver Equivalent		Gold		Silver		Lead		Zinc	
Classification	**k tonne**	**m**	**gpt**	**k-oz**	**gpt**	**oz**	**gpt**	**k-oz**	**pct**	**lbsx1000**	**pct**	**lbsx1000**
Measured	270	2.18	381	3,305.5	0.940	8,162	210.1	1,824.8	1.17	6,952	3.69	21,997
Indicated	711	1.95	303	6,930.7	0.882	20,159	162.7	3,718.2	1.18	18,430	2.60	40,690
Meas+Ind	981	2.01	325	10,236.2	0.898	28,320	175.7	5,543.0	1.17	25,383	2.90	62,687
Inferred	386	1.72	203	2,522.8	0.810	10,053	90.6	1,125..5	0.73	6,206	2.10	17,874

Note: Mineral resources which are not mineral reserves do not have demonstrated economic viability. The quantity and grade of inferred resources reported herein are uncertain in nature and exploration completed to date is insufficient to define these mineral resources as indicated or measured. There is no guarantee that further exploration will result in the inferred mineral resources being upgraded to an indicated or measured mineral resource category.

*AgEq is the silver equivalent in ppm used to calculate the cutoff. The silver equivalent was calculated with the following equation:

$$\mathbf{AgEq} = \frac{\underline{(Ag * P_{ag}/31.1035) + (Pb * P_{pb} * 22.05) + (Zn * P_{zn} * 22.05) + (Au * P_{au}/31.1035)}}{(P_{ag})}$$

Where:

Metal	**Symbol**	**Grade Units**	**Price**	**Price Symbol**
Silver Eq	AgEq	g/t		
Silver	Ag	g/t	26.28 $/tOz	$\underline{P_{ag}}$
Gold	Au	g/t	1,341.00 $/tOz	$\underline{P_{au}}$
Lead	Pb	%	0.9988 $/lb	$\underline{P_{pb}}$
Zinc	Zn	%	0.9531 $/lb	$\underline{P_{zn}}$

* The calculation assumes equal recoveries in all metals pending further metallurgical work.

- The grades for copper, lead, and zinc are multiplied by each metal's three year trailing average price.
- The quantity and grade or quality is an estimate and is rounded to reflect the fact that it is an approximation.

The decision to commence production at the Rosario Mine was not based on a feasibility study of mineral reserves demonstrating economic and technical viability, but rather on a more preliminary estimate of inferred mineral resources. Accordingly, there is increased uncertainty and economic and technical risks of failure associated with this production decision. Production and economic variables may vary considerably, due to the absence of a complete and detailed site analysis in accordance with NI 43-101.

Exploration and Pre-Production Costs

During the year ended December 31, 2013, mineral property acquisition costs, and exploration and development costs were $622,182 and $4,314,213 respectively for the Rosario Mine. Included in the exploration expenditures are diamond drilling costs incurred as part of a 4,000-metre diamond drilling program north-west of the current Rosario resource to test the extension of the high-grade silver mineralization within the Rosario I and II veins. As at December 31, 2013, for financial reporting purposes the Rosario Mine was determined to be in the pre-commercial production phase. As such the ore purchase costs of $367,144 and the net operating costs, including net revenues of $1,441,602 from concentrate sales, are capitalized to mine under construction and development costs.

During the year ended December 31, 2013, the Company incurred $5,471,593 of expenditures in connection with the initial equipment procurement and construction costs of the Rosario milling facility and mine.

San Felipe Project, Sonora, Mexico

The San Felipe Project consists of 15 concessions and is a late stage exploration project, located in the State of Sonora, approximately 130 kilometers north-west of Hermosillo City, the state capital of Sonora. Santacruz acquired exploration rights with the right to purchase the project from Minera Hochschild Mexico, S.A. de C.V. ("Hochschild") pursuant to the terms of a mining exploration and promissory sale agreement dated August 3, 2011, as amended December 9, 2011 and October 8, 2012 (the "San Felipe Agreement"). The terms of the San Felipe Agreement were further amended on August 13, 2013 to defer $16 million of the final option payment from October 1, 2014 to October 31, 2015 in exchange for accelerating certain other payments. Details of the restructured payment schedule are included in note 12(b) to the 2013 Annual Financial Statements.

Seven mineralized structures are known to exist within the San Felipe Project area: the Santa Rosa, La Ventana, Transversales, San Felipe, Artemisa, Cornucopia, and Las Lamas. In most cases, the mineralized structures are silicified and form resistant, high-relief ridges.

Hochschild explored and developed the project from 2001 to 2008, with more than 18,500 meters of diamond drilling and significant development work completed on the project at the La Ventana, San Felipe and Las Lamas veins. A copy of the most recent and updated NI43-101 Technical Report dated December 19, 2012 for the San Felipe Project is available on the Company's website at www.santacruzsilver.com and on SEDAR. The Report was prepared by Donald E. Hulse, P.E. and SME-RM of Gustavson, who is an independent "qualified person" under NI 43-101. The Report disclosed the measured, indicated, and inferred mineral resources estimated within the San Felipe Project, with an effective date of April 5, 2012, and remains current. A mineral reserves estimate was not prepared. Mineral Resources are not Mineral Reserves and do not demonstrate economic viability. There is no certainty that all or any part of the Mineral Resource will be converted to Mineral Reserves. The Report indicates that the San Felipe Project contains a mineral resource of 3 million metric tons of measured and 900 thousand metric tons of indicated mineralization, containing 31 million and 8 million troy ounces of silver equivalent, respectively, above a cutoff grade of 75g AgEq/t. The report estimates that there is an additional 1.5 million metric tons of inferred mineral resource above the 75g AgEq/t cutoff containing 11 million troy ounces of silver equivalent.

All Veins Total								
	Measured							
Ag Eq Cutoff	Tonnes (x1000)	Ounces Ag (x1000)	Equivalent Ounces Ag (x1000)	Ag gpt	Equivalent Ag gpt	Cu %	Pb %	Zn %
50	4,314	8,919	37,718	64.30	271.94	0.25	2.56	4.51
75	3,133	7,313	30,887	**72.60**	**306.64**	**0.29**	**2.83**	**5.11**
100	2,420	6,193	25,970	79.59	333.76	0.32	3.02	5.58
150	1,524	4,519	18,913	92.21	385.95	0.38	3.40	6.52
	Indicated							
Ag Eq Cutoff	Tonnes (x1000)	Ounces Ag (x1000)	Equivalent Ounces Ag (x1000)	Ag gpt	Equivalent Ag gpt	Cu %	Pb %	Zn %
50	1,546	2,663	11,679	53.58	235.05	0.20	2.29	3.96
75	936	1,876	8,188	**62.33**	**272.09**	**0.24**	**2.56**	**4.63**
100	621	1,408	6,116	70.50	306.13	0.27	2.81	5.26
150	329	860	3,869	81.35	366.05	0.34	3.38	6.32
	Measured + Indicated							
Ag Eq Cutoff	Tonnes (x1000)	Ounces Ag (x1000)	Equivalent Ounces Ag (x1000)	Ag gpt	Equivalent Ag gpt	Cu %	Pb %	Zn %
50	5,860	11,582	49,397	61.48	262.21	0.23	2.49	4.37
75	4,069	9,188	39,074	**70.24**	**298.69**	**0.28**	**2.77**	**5.00**
100	3,042	7,601	32,086	77.73	328.12	0.31	2.98	5.51
150	1,853	5,378	22,782	90.28	382.42	0.37	3.39	6.49
	Inferred							
Ag Eq Cutoff	Tonnes (x1000)	Ounces Ag (x1000)	Equivalent Ounces Ag (x1000)	Ag gpt	Equivalent Ag gpt	Cu %	Pb %	Zn %
50	3,084	4,140	19,913	41.75	200.80	0.16	2.17	3.35
75	1,495	2,149	11,347	**44.70**	**236.08**	**0.20**	**2.68**	**3.92**
100	750	1,281	6,742	53.16	279.68	0.25	3.02	4.74
150	317	651	3,533	63.82	346.58	0.33	3.63	6.01

*Ag Eq is the silver equivalent used to calculate the cutoff. The silver equivalent was calculated with the following equation:

$$\mathbf{AgEq} = \frac{(Ag * P_{ag}/31.1035)+(Pb*P_{pb}*22.05)+(Cu*P_{cu}*22.05)+(Zn*P_{zn}*22.05)+(Au*P_{au}/31.1035)}{(P_{ag})}$$

Where:

Metal	Symbol	Grade Units	Price	Price Symbol
Silver Eq	AgEq	g/t		
Silver	Ag	g/t	26.28 $/tOz	P_{ag}
Copper	Cu	%	3.491 $/lb	P_{cu}
Lead	Pb	%	0.9988 $/lb	P_{pb}
Zinc	Zn	%	0.9531 $/lb	P_{zn}

* The calculation assumes equal recoveries in all metals pending further metallurgical work.

- The grades for copper, lead, and zinc are multiplied by each metal's 3 year trailing average price.
- The quantity and grade or quality is an estimate and is rounded to reflect the fact that it is an approximation.

Current Exploration Activities

The Company has completed approximately 14,000 metres over 80 drill holes of its planned 25,000 metre diamond drill program at its San Felipe Project, and has received assay results in respect of 4,811 meters. Highlights of drilling results (reported as true widths and assays uncut) include:

Las Lamas Vein:

- SCLL-05: 6.46 m @ 721 g/t Ag eq. (212 g/t Ag, 0.01 g/t Au, 15.83% Zn, 0.44% Cu and 0.55% Pb)
- SCLL-04: 2.41 m @ 823 g/t Ag eq. (324 g/t Ag, 0.01 g/t Au, 14.99% Zn, 0.45% Cu and 0.93% Pb)
- SCLL-15: 6.95 m @ 355 g/t Ag eq. (93 g/t Ag, 0.01 g/t Au, 8.06% Zn, 0.22% Cu and 0.24% Pb)
- SCLL-23: 1.40 m @ 542 g/t Ag eq. (383 g/t Ag, 0.05 g/t Au, 3.78% Zn, 0.13% Cu and 1.12% Pb)

La Ventana Vein:

- SCLV-01: 5.75 m @ 918 g/t Ag eq. (142 g/t Ag, 0.02 g/t Au, 13.01% Zn, 1.53% Cu and 8.04% Pb)
- SCLV-04: 2.80 m @ 810 g/t Ag eq. (215 g/t Ag, 0.02 g/t Au, 11.05% Zn, 1.13% Cu, and 4.93% Pb)

Transversales Vein:

- SCVT-02: 11.80 m @ 116 g/t Ag eq. (84 g/t Ag, 0.02 g/t Au, 0.41% Zn, 0.04% Cu and 0.45% Pb) including; 3.35 m @ 283 g/t Ag eq. (209 g/t Ag, 0.04 g/t Au, 1.05% Zn, 0.05% Cu and 1.17% Pb)
- SCVT-07: 3.35 m @ 324 g/t Ag eq. (81 g/t Ag, 0.03 g/t Au, 5.03% Zn, 0.35% Cu and 1.90% Pb)
- SCVT-16: 2.60 m @ 409 g/t Ag eq. (122 g/t Ag, 0.04 g/t Au, 8.77% Zn, 0.23% Cu and 0.28% Pb)

Results from the initial holes have generally returned higher silver and zinc grades over wider intervals than expected. To date, drilling has intersected the Las Lamas vein for 300 meters on strike. The Las Lamas vein is open for 700 metres along strike and is open at depth. The Transversales vein can be traced over a strike length of 200 metres and to a depth of 250 metres and remains open along strike in both directions and to depth. In addition, drilling is proving the La Ventana vein to be a robust silver-polymetallic vein with high copper, zinc and lead grades.

The objective of the drill campaign is to further delineate higher grades in the south-west portion of the project. Veins believed to be the most prospective for expanding silver equivalent resources include Las Lamas, Cornucopia, Artemisia and Transversales in addition to the La Ventana vein which hosts the majority of the current 43-101 resource defined by Santacruz. More detailed information regarding the San Felipe Project is available on the Company’s website, www.santacruzsilver.com.

For full details of the drill program results, see the Company's short form prospectus dated February 28, 2014, available on SEDAR.

Preliminary results of the drilling program indicate:

- Extension of the strike length at the Las Lamas vein by an additional 450 meters plus an additional 100 metres at depth. The vein has now been systematically tested by drilling over 630 meters on strike length and to depths of 250 metres.
- Higher drill core recoveries (95%-99%) resulting in increased grades when compared to historical resources at the La Ventana and Las Lamas veins.

Exploration and Acquisition Costs

During the year ended December 31, 2013, Santacruz incurred acquisition costs and exploration expenditures of $18,176,958 and $3,468,451 respectively, at the San Felipe Project.

Gavilanes Property, San Dimas, Durango, Mexico

The Gavilanes Property comprises 10 mining concessions located in the rugged Sierra Madre Occidental mountain range in the municipality of San Dimas in the State of Durango, Mexico, approximately 110 kilometres west-north-west of Durango City. The Gavilanes Property covers a total area of 8,832.28 hectares. Details of the acquisition terms are contained in Note 12(a) of the 2013 Annual Financial Statements.

Current Exploration Activities

On January 15 and April 4, 2013, the Company announced results from its ongoing 6,000 metre Phase I drilling campaign being undertaken on the Gavilanes Property. In total the Company reported on 22 diamond drill holes with the results released in the April 4, 2013 press release relating to the final holes of the program. The drill program was designed to test three of seven known silver-bearing veins and a stockwork area within the Gavilanes Property.

The results of the Phase I program were positive and based on this Santacruz commenced a 16,000 metre Phase II drill program on the property. The objective of the Phase II program is to confirm the continuation of the GSA, Descubridora and San Nicolas veins in addition to the stockwork area of El Hundido. On July 11, 2013, the Company announced that it was temporarily suspending drilling at the property. This action was not related in any way to the positive exploration results from the project but was taken in view of then current weak resource capital markets as a means of conserving the Company's treasury while it completes the transition of the Rosario Mine to a commercial operation.

On January 23, 2014, the Company filed a technical report in respect of its previously announced independent NI 43-101 Mineral Resource estimate on the Gavilanes Property. The Mineral Resource estimate was prepared by Gary Giroux, P.Eng. of Giroux Consultants Ltd. and utilized a geological model completed by Hans Smit, P.Geo and Fletcher Bourke, P.Geo. The effective date of this mineral resource estimate is November 13, 2013. No work has been performed on the property since then.

The Gavilanes Property is an intermediate sulphidation (silver-base metal-gold) vein system, with veining identified within a 2.2 km^2 area. The present resource estimate covers only an approximately 0.2 km^2 surface area. Three domain types were used for the resource estimate – Vein, Hangingwall (HW) / Footwall (FW) and Stockwork (stx). Based upon a 75 gram per tonne ("g/t") silver equivalent ("AgEq") cut-off, the resources on three of seven known veins, Guadalupe, Descubridora and San Nicolas, as well as the El Hundido stockwork are as follows:

	(tonnes)	Ag (g/t)	Au (g/t)	Cu (%)	Pb (%)	Zn (%)	AgEQ (g/t)	AgEq Oz
Indicated	**953,000**	**164.6**	**0.09**	**0.06**	**0.42**	**0.41**	**200.5**	**6,143,000**
Inferred	**5,399,000**	**124.6**	**0.12**	**0.09**	**0.40**	**0.34**	**163.0**	**28,294,000**

*AgEq is the silver equivalent in ppm used to calculate the cutoff. The silver equivalent was calculated with the following equation:

$$AgEq = \frac{(Cu\% \times 71.65) + (Pb\% \times 21.38) + (Auppm \times 42.37) + (Agppm \times 0.69) + (Zn\% \times 19.18)}{0.69}$$

The metal prices used in the silver equivalent estimate are listed below.

		Factor
Ag	US$ 21.55 per ounce	0.69 $/gm
Au	US$ 1318.00 per ounce	42.37 $/gm
Cu	US$ 3.25 per pound	71.65 $/%
Pb	US$ 0.97 per pound	21.38 $/%
Zn	US$ 0.87 per pound	19.18 $/%

100% recovery has been assumed for all metals in this silver equivalent estimate. At this stage of the project no metallurgy has been completed and the reader is cautioned that 100% recoveries are never achieved.

Highlights of the mineral resource estimate are as follows:

- Indicated mineral resources of 6,143,000 AgEq ounces grading 200 g/t AgEq
- Inferred mineral resource of 28,294,000 AgEq ounces grading 163 g/t AgEq;
- Veins remain open along strike and to depth with intermittent surface exposures indicating an untested strike length;
- The El Hundido stockwork zone is open down-dip and to the south; and
- Four unexplored veins offer additional potential.

The identified indicated and inferred resource is significant, however engineering and economic studies have not been completed and thus no statement can be made about the project's potential economic viability. Recommended work at Gavilanes includes drilling in the area of current resources with the intent of upgrading resources to Indicated and Measured, drilling the open extent of the area with resources, testing other targets on the property and undertaking preliminary metallurgy, engineering and environmental studies.

<u>Exploration and Acquisition Costs</u>
During the year ended December 31, 2013, mineral property acquisition costs and exploration costs were $1,800,000 and $1,142,474 respectively for the Gavilanes Property.

El Gachi Property, Sonora, Mexico
The El Gachi Property covers approximately 48,057 hectares and is located approximately 30 kilometres from the San Felipe Project. To date the Company has not completed any exploration work on the property.

Selected Annual Information

The Company's fiscal period ends on December 31st of each year. The following is a summary of certain selected audited financial information for the last three completed fiscal years:

	2013	2012	2011
	$	$	$
Cash	1,618,472	2,879,378	183,072
Working Capital	6,979,805	1,729,525	395,493
Mineral Property Interests	42,354,137	15,213,035	6,960,510
Total Assets	61,012,018	25,926,144	8,149,082
Total Liabilities	5,615,950	3,039,716	3,696,583
Total Shareholders' Equity	55,396,068	22,886,428	4,452,499
Total Revenues	-	-	-
Net Loss	(6,319,332)	(18,424,919)	(580,358)
Net Loss Per Share (basic and diluted) (1)	(0.07)	(0.33)	(0.17)

(1)The basic and diluted loss per share calculations result in the same amount due to the anti-dilutive effect of outstanding stock options and warrants, if any.

Results of Operations

The Company recorded a net loss of $6,319,332 ($0.07 per share) for the year ended December 31, 2013, compared to the net loss of $18,424,919 ($0.33 per share) for the year ended December 31, 2012.

Variances of note in general and administrative expenses are detailed below:

- Management and consulting fees of $275,438 (2012 – $235,893) and salaries and benefits of $174,019 (2012 – $96,573). These expenses were higher during 2013 primarily due to increased activities at the Company's Mexican office in connection with the development of the Rosario Mine.
- Professional fees of $488,061 (2012 – $1,082,868). Professional fees were higher during the 2012 fiscal year due to the costs incurred related to the reverse takeover transaction on April 12, 2012.
- Share-based payments of $675,205 (2012 – $3,279,082). 700,000 stock options were granted during the 2013 fiscal year as compared to 5,910,000 stock options granted in 2012.
- Shareholder communications of $431,259 (2012 – $208,002). These expenses increased primarily as the result of increased costs related to investor awareness initiatives.
- Transfer agent and filing fees of $94,004 (2012 – $28,354). Transfer agent and filing fees increased due to the fact that the Company's shares were listed for trading on the TSX Venture Exchange on April 12, 2012.
- Travel expenses of $132,132 (2012 – $191,351). Travel expenses decreased due to a decrease in management's travel between the Company's Canadian and Mexican offices.

Variances of note in other income and expenses are detailed below:

- Loss on derivative liabilities of $nil (2012 – $3,495). 139,239 warrants were issued during the 2011 fiscal year. As the exercise price of the share purchase warrants was fixed in Canadian dollars and the functional currency of the Company was the US dollar, the warrants were considered a derivative, as a variable amount of cash in the Company's functional currency would be received on exercise. The share purchase warrants were re-measured at fair value at each statement of financial position date with the change in fair value recorded in profit or loss during the period of change. The change in fair value for the year ended December 31, 2012 was a loss of $3,495. The share purchase warrants expired unexercised on July 20, 2012.
- Charge related to public company listing of $nil (2012 – $12,967,741). Charge related to public company listing occurred pursuant to accounting for the reverse takeover transaction on April 12, 2012 in accordance with IFRS as detailed in Note 5 to the 2013 Annual Financial Statements.

- Other income of $323,608 (2012 – $120,218). Interest income is earned on surplus cash on hand. During 2013 the Company had more surplus cash on hand than in 2012 as a result of closing the prospectus offering in February 2013.
- Income tax expense of $4,004,469 (2012 – $34,009). The deferred income tax expense increased compared to the 2012 fiscal year as a result of the Mexican tax reform enacted in December 2013.

Summary of Quarterly Results

	THREE MONTHS ENDED			
	December 31, 2013	**September 30, 2013**	**June 30, 2013**	**March 31, 2013**
Revenues	Nil	Nil	Nil	Nil
Administrative Expenses	520,005	691,827	687,315	903,644
Deferred exploration and development costs, and option payments (cash portion)	776,179	3,810,981	4,044,722	18,057,101
Net loss	(4,507,829)	(503,505)	(565,244)	(742,754)
Net loss per share(1)	(0.05)	(0.00)	(0.01)	(0.01)
	THREE MONTHS ENDED			
	December 31, 2012	**September 30, 2012**	**June 30, 2012**	**March 31, 2012**
Revenues	Nil	Nil	Nil	Nil
Administrative Expenses	645,510	760,827	4,088,820	169,622
Deferred exploration and development costs, and option payments (cash portion)	4,900,203	2,170,450	1,281,265	442,415
Net loss	(583,307)	(763,841)	(16,945,273)	(132,498)
Net loss per share(1)	(0.04)	(0.01)	(0.27)	(0.01)

(1) The basic and fully diluted calculations result in the same value due to the anti-dilutive effect of outstanding stock options and warrants for all quarters.

Administrative expenses were higher for the quarters ended June 30, 2012 and onward primarily due to increased activities at the Company’s Mexican office in connection with the development of the Rosario Mine. The deferred exploration and option payments were also higher during those quarters compared to the remaining quarters, due to the development of the Rosario Mine. During the three months ended June 30, 2012 the Company recorded $2,780,916 of share-based compensation from the grant of stock options during the period and in addition recorded a charge related to public company listing of $12,967,741 and $814,179 of professional fees as a result of the reverse takeover transaction on April 12, 2012.

During the three months ended December 31, 2013, the Company recorded deferred income tax expense of $3,974,151 as a result of the Mexican tax reform enacted in December 2013.

Fourth Quarter

The Company recorded a net loss of $4,507,829 ($0.05 per share) for the quarter ended December 31, 2013, as compared to a net loss of $583,307 ($0.04 per share) for the quarter ended December 31, 2012. The increase is primarily due to the deferred income tax expense of $3,974,151 recorded as a result of the Mexican tax reform enacted in December 2013.

Financing Activities

Details of financing activities in the year ended December 31, 2012 are as follows:

- On January 20, 2012, the Company subdivided its outstanding share capital (the "Subdivision") on the basis of 4.7722 new common shares for each existing common share. Prior to the Subdivision, the Company had outstanding 5,467,911 common shares, 83,644 special warrants, and 139,239 warrants to purchase common shares. Accordingly, the Subdivision resulted in the 5,467,911 common shares issued and outstanding being subdivided into 26,093,966 common shares on a post-Subdivision basis. In accordance with the adjustment provision of the special warrants and the warrants, the number of common shares issuable on the exercise of the special warrants and warrants had been adjusted to reflect the Subdivision. Accordingly, the special warrants were convertible into 399,166 common shares and the warrants were convertible into 664,476 common shares.
- On January 25, 2012, all of the Company's special warrants were converted into post-Subdivision 399,166 common shares.
- On January 27, 2012, the Company completed a non-brokered private placement issuing 444,444 post-Subdivision common shares for aggregate gross proceeds of $399,480.
- On April 12, 2012, the Company completed a non-brokered private placement of 555,055 common shares at $0.90 for gross proceeds of $500,000.
- On April 12, 2012, the Company completed a brokered private placement of 22,222,222 common shares at $0.90 per share for gross proceeds of $20,100,000. The agent for the offering received a commission consisting of $1,277,355 cash, 200,000 common shares, and 1,333,333 broker warrants entitling the agent to purchase 1,333,333 common shares of the Company at CDN$1.00 per share up to April 12, 2014. The Company also issued 2,375,000 common shares as corporate finance fee and incurred additional issue costs of $211,782.
- During the year ended December 31, 2012, the Company issued 116,586 common shares pursuant to exercise of warrants for total gross proceeds of $27,126.

Details of financing activities in the year ended December 31, 2013 are as follows:

- On February 19, 2013, the Company closed a prospectus offering through a syndicate of underwriters (the "Underwriters"). The Company issued 21,850,000 common shares at a price of CDN$1.85 per share for gross proceeds of $39,949,557 (CDN$40,422,500). The Underwriters received a cash fee of $2,396,973, as well as 1,311,000 warrants, each of which is exercisable to purchase one common share for a price of CDN$1.85 for a period of 24 months. The Company also issued 60,000 common shares as corporate finance fee and incurred additional issue costs of $508,894.
- On August 16, 2013, the Company issued 1,250,000 common shares at a deemed issue price of CDN$1.07 per share as an option payment pursuant to the San Felipe Agreement.
- During the year ended December 31, 2013, the Company issued 324,545 common shares pursuant to exercise of warrants for total gross proceeds of $231,849.

Details of financing activities subsequent to December 31, 2013 are as follows:

- On March 11, 2014, the Company closed a prospectus offering through a syndicate of underwriters. The Company issued 10,750,000 common shares at a price of CDN$1.00 per share for gross proceeds of CDN$10,750,000. The underwriters also exercised their over-allotment option to acquire an additional 1,312,500 common shares for additional gross proceeds of CDN$1,312,500. Including the proceeds from the exercise of the over-allotment option, the total gross proceeds of the prospectus offering were CDN$12,062,500. The underwriters received a cash fee of CDN$723,750, as well as 723,750 warrants, each of which is exercisable to purchase one common share for a price of CDN$1.00 until March 11, 2016 for 645,000 warrants and March 20, 2016 for 78,750 warrants. One of the underwriters was issued an additional 100,000 common shares as a corporate finance fee.

Capital Expenditures

The Company spent $26,688,983 on its mineral properties during the year ended December 31, 2013 (2012 – $8,794,333). The Company also spent $5,691,908 on acquisitions of plant and equipment during the year ended December 31, 2013 (2012 – $5,919,396). The Company has made no dividend payments, and currently has no plans to declare any dividends.

The Company had a commitment to incur $3,000,000 of exploration expenditures on the San Felipe Project by October 31, 2015. Any unexpended balance was to be paid to Hochschild regardless of whether the Company exercised the option. As at December 31, 2013, all $3,000,000 of the committed exploration expenditures have been incurred and $nil of the exploration obligation remains outstanding. During the 2013 fiscal year, the Company paid to Hochschild $16,700,000 and must make additional cash payments of $1,000,000 on June 15, 2014, $5,000,000 on October 31, 2014, and $15,000,000 on October 31, 2015, in order to exercise its option on the San Felipe Project and El Gachi Property. The Company issued 1,250,000 common shares to Hochschild at a deemed issue price of CDN$1.07 per share on August 16, 2013. An additional $1,000,000 for restructuring fees is due on October 31, 2015, payable in cash or through the issuance of $1,500,000 of common shares of the Company at an issue price calculated at the time of issuance subject to a minimum issue price of CDN$1.07 per share.

Use of Proceeds from Previous Financings

During the 2012 fiscal year, the Company raised gross proceeds of CDN$20.0 million from the brokered private placement of 22,222,222 common shares at CDN$0.90 per share on April 12, 2012. The Company used the proceeds (together with an additional CDN$400,000 on hand) as follows:

Use of Proceeds Items as Stated in Filing Statement dated March 29, 2012 with respect to the Qualifying Transaction	**Original Estimated Expenditure (Cdn$)**	**Approximate Actual Expenditure (Cdn$)**
Estimated costs of Forte and Santacruz to complete the Acquisition and Financing	$375,000	$392,000
Estimated general and administrative expenses over the 12 months following the Closing Date	$1,191,000	$1,821,000
Exploration costs on the Rosario Property	$695,000	$676,000
Development costs on the Rosario Property	$10,300,000	$8,087,000
Property payments on the Rosario Property	$635,000	$386,000
Exploration costs on the Gavilanes Property	$1,191,000	$897,000
Property payments on the Gavilanes Property	744,000	$684,000
Exploration costs on non-material properties	$85,000	-
Property payments on non-material properties	$41,000	-
Property maintenance costs, including taxes	$107,000	$133,000
Exploration costs on San Felipe Property	-	$137,000
Community relations, technical report and other costs on San Felipe Property	-	$387,000
Property payment on San Felipe Property	-	$4,000,000
Unallocated working capital	$5,036,000	$2,800,000
Total	**$20,400,000**	**$20,400,000**

As detailed in the table above, proceeds from the offering were generally used as originally estimated except that the Company renegotiated the terms of the San Felipe Agreement and used $4,000,000 of the funds in October 2012 to make a payment to Hochschild that was not included in the original estimate. The impact of the payment was to reduce unallocated working capital by approximately $1.8 million and reduce the development expenditures on the Rosario Property by approximately $2.2 million.

The Company used the net proceeds of CDN$37,997,150 from the 2013 financing (which included net proceeds from the exercise of the over-allotment option) as follows:

Use of Proceeds as stated in the short form prospectus from the 2013 Financing	**Original Estimated Expenditure (Cdn$)**	**Approximate Actual Expenditure (Cdn$)**
San Felipe Project		
Property payments	$15,977,631	$16,677,000
Surface and underground mapping and permitting	$420,000	$50,000
Drilling and related infrastructure	$6,000,000	$2,550,000
Development of ramps for bulk samples and underground drilling	$1,600,000	-
Annual mining taxes, ejidal fees and sundry project costs	-	$761,000
Pre-feasibility study	$350,000	-
Subtotal:	**$24,347,631**	**$20,038,000**
Gavilanes Property		
Property payments	$3,195,526	$1,797,000
Mapping and sampling and staffing and site costs	$400,000	$260,000
Drilling and sample analysis	$650,000	$797,000
Updated resource estimate	$150,000	$50,000
Subtotal:	**$4,395,526**	**$2,904,000**
Rosario Mine		
Mill construction costs	-	$1,997,000
Pre-production costs	-	$6,267,000
Subtotal:	-	**$8,264,000**
General		
Estimated offering costs	$500,000	$520,000
Administration expenses, including corporate and financial reporting, legal and compliance and accounting costs	$900,000	$862,000
General corporate communication and corporate development	$500,000	-
General working capital(1)	$7,353,993(1)	$5,409,150(1)
Subtotal:	**$9,253,993**	**$6,791,150**
Total	**$37,997,150**	**$37,997,150**

Notes:

(1) Net proceeds from the exercise of the over-allotment option were added to general working capital, as disclosed in the short form prospectus from the 2013 financing.

As noted in the table above, the Company used approximately $8.3 million of the funds from the 2013 financing to fund ongoing pre-production and mill construction costs at the Rosario Mine. These expenditures were not included in the original estimate of use of proceeds and arose due to unforeseen delays in getting the Rosario Mine underground development sufficiently advanced to consistently supply the milling facility with ore at expected production rates. The Company delayed exploration drilling and other underground development work on the San Felipe Project as a result of the unexpected production delay at the Rosario Mine.

Liquidity and Capital Resources

As at December 31, 2013, the Company had cash and cash equivalents of $1,618,472 (December 31, 2012 – $2,879,378) and working capital of $6,979,805 (December 31, 2012 – $1,729,525). During the year ended December 31, 2013, net cash used in operating activities was $5,685,263, net cash used in investing activities was $32,365,948 primarily for acquisitions of mineral property interests, plant and equipment, and costs relating to the exploration activities on its mineral properties; and net cash provided by issuance of common shares as part of financing activities was $37,337,287. During the year ended December 31, 2013, the Company also repaid $133,089 of shareholder loans.

Pursuant to the terms of the underlying mineral property agreements to the Rosario Mine (Note 11 to the 2013 Annual Financial Statements), in order to maintain and exercise the option the Company must make aggregate cash payments of $745,000 on or before February 22, 2016. Subsequent to December 31, 2013, the Company made payments of $220,000 in accordance with the terms of these agreements.

Pursuant to the terms of the Gavilanes property agreement (Note 12(a) to the 2013 Annual Financial Statements), in order to maintain and exercise the option the Company must make aggregate cash payments of $2,650,000 on or before December 17, 2014. Subsequent to December 31, 2013 the Company made $1,500,000 of these payments.

Pursuant to the terms of the San Felipe Agreement (Note 12(b) to the 2013 Annual Financial Statements), in addition to cash payments of $22,700,000 made to December 31, 2013, in order to maintain and exercise the option, the Company must make further aggregate cash payments of approximately $21,000,000 on or before October 31, 2015. An additional $1,000,000 must be paid for restructuring fees which is due on October 31, 2015, payable in cash or in that number of the Company's common shares having a value of $1,500,000 at the date of issue, subject to a minimum issue price of CDN$1.07 per share.

During the year ended December 31, 2013, the Company's operations did not generate positive cashflow. Until such time as the Rosario Mine begins generating positive cash flow the Company is reliant on its internal cash reserves and the resource capital markets in order to fund its activities. In order to fund the further development of the San Felipe Project and the Gavilanes Property, on March 11, 2014, the Company closed a prospectus offering and issued 12,062,500 common shares for gross proceeds of CDN$12,062,500.

Funds from this financing will be expended on the San Felipe Project as to $2.25 million to complete 500 metres of access ramp at each of three veins and to conduct a preliminary tailings impoundment study and $500,000 to conduct minor infrastructure work, including water pipeline and pre-construction activities. In addition, the Company has budgeted $400,000 to pay for a preliminary economic assessment or pre-feasibility study, which is expected to be completed during 2014. On the Gavilanes Property, $3 million will be used on mapping, drilling, sample analysis, metallurgy and related infrastructure, which is expected to be carried out during 2014. The remainder of the gross proceeds will be used for costs associated with the prospectus offering, administration expenses including corporate and financial reporting, legal, accounting, general corporate communication and corporate development, and general working capital.

Transactions with Related Parties

The Company's related parties consist of the Company's directors, officers and companies associated with them including the following:

- Malaspina Consultants Inc., a company owned by Robert McMorran, the Chief Financial Officer
- Pref-Ex Geological Inc., a company owned by Marc Prefontaine, a director of the Company

During the years ended December 31, 2013 and 2012, the Company incurred the following charges by directors and officers of the Company and by companies controlled by directors and officers of the Company:

	2013 $	2012 $
Accounting and corporate secretarial fees (1)	148,844	103,092
Directors' fees (2)	102,183	-
Management fees (3)	170,535	190,058
Share-based payments	329,020	2,512,093
Salaries and benefits capitalized in mine under construction and development costs (4)	233,160	165,641

(1) The charge includes accounting and corporate secretarial fees paid to Malaspina Consultants Inc.
(2) The charge includes geological consulting fees paid to Pref-Ex Geological Inc. and directors' fees paid to Marc Prefontaine, James Hutton, and Craig Angus.
(3) The charge includes management fees paid to Arturo Préstamo Elizondo, the Chief Executive Officer.
(4) The charge includes salaries and benefits paid to Francisco Ramos, the Chief Operating Officer, which were capitalized in mine under construction and development costs.

At December 31, 2013, accounts payable and accrued liabilities include an amount of $28,333 (December 31, 2012 – $25,415), due to Malaspina Consultants Inc. for accounting services, and Marc Prefontaine, James Hutton, and Craig Angus for directors' fees.

Key management includes directors and executive officers of the Company. Other than the amounts disclosed above, there was no other compensation paid or payable to key management for employee services for the reported periods.

Financial Instruments

Fair Value and Classification of Financial Instruments

The Company has classified fair value measurements of its financial instruments using a fair value hierarchy that reflects the significance of inputs used in making the measurements as follows:

- Level 1: Valuation based on quoted prices (unadjusted) in active markets for identical assets or liabilities;
- Level 2: Valuation based on directly or indirectly observable inputs in active markets for similar assets or liabilities, other than Level 1 prices, such as quoted interest or currency exchange rates;
- Level 3: Valuation based on significant inputs that are not derived from observable market data, such as discounted cash flow methodologies based on internal cash flow forecasts.

The carrying values of cash and cash equivalents, trade receivables, other receivables, accounts payable and accrued liabilities, and exploration obligations approximate their fair values because of their short term nature. The carrying value of due to shareholders approximates its fair value because it is due on demand.

On July 20, 2011, Santacruz issued 139,239 pre-Subdivision share purchase warrants, with each warrant exercisable to purchase one additional common share at a price of CDN$5.95 per common share on or before July 20, 2012. As the exercise price of the share purchase warrants was fixed in Canadian dollars and the functional currency of Santacruz at the time was the US dollar, the Company had determined that such warrants with an exercise price denominated in a currency that was different from the entity's functional currency were classified as a derivative liability based on the evaluation of the warrant's settlement provisions, and carried at their fair value.

At December 31, 2011, the fair value of share purchase warrants issued and outstanding with Canadian dollar exercise prices was $1,154. As a result of the change in functional currency from the US dollar to the Canadian dollar on April 1, 2012, the warrants were no longer considered a derivative. The fair value of the derivative for the warrants had been estimated using the Black-Scholes option pricing model as it was considered a Level 3 financial instrument in the fair value hierarchy with significant unobservable inputs.

Details of activity for the derivative liabilities for the years ended December 31, 2013 and 2012 are as follows:

	2013 **$**	**2012** **$**
Balance, beginning of year	-	1,154
Loss on derivative liabilities	-	3,495
Foreign exchange revaluation	-	31
Reallocation to warrant reserve on change of functional currency	-	(4,680)
Balance, end of year	-	-

As at December 31, 2013, the Company does not have any financial instruments measured at fair value.

Discussions of risks associated with financial assets and liabilities are detailed below:

<u>Credit Risk</u> – Credit risk is the risk of financial loss to the Company if a customer or counterparty to a financial instrument fails to fulfill its contractual obligations. The Company's credit risk consists primarily of cash and cash equivalents, trade receivables and other receivables. The credit risk is minimized by placing cash with major financial institutions. Trade receivables are due from a large, multinational corporation that has conducted business in Mexico for many years. The Company regularly reviews the collectability of its trade receivables and contractually receives up to 90% advance on all payments. The Company considers the credit risk related to cash and cash equivalents, trade receivables and other receivables to be minimal.

<u>Interest Rate Risk</u> – Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates. If interest rates decrease, the Company will generate less interest revenue. Presently the Company has minimal risk of realizing a loss as a result of a decline in the fair value of its financial instruments because of the short-term nature of the investments.

<u>Liquidity Risk</u> – Liquidity risk is the risk that the Company will not be able to meet its financial obligations when they become due. To mitigate this risk, the Company has a planning and budgeting process in place to determine the funds required to support its ongoing operations and capital expenditures. The Company ensures that sufficient funds are raised from equity offerings to meet its operating requirements, after taking into account existing cash and expected exercise of stock options and

share purchase warrants. The Company's cash is held in business accounts which are available on demand for the Company's programs.

Contractual obligated cash flow requirements as at December 31, 2012 were as follows:

	< 1 year $	1 – 2 years $	2 – 5 years $	>5 years $	Total $
Accounts payable and accrued liabilities	523,450	-	-	-	523,450
Due to shareholders	133,089	-	-	-	133,089
Exploration obligations	2,383,177	-	-	-	2,383,177
Total	3,039,716	-	-	-	3,039,716

Contractual obligated cash flow requirements as at December 31, 2013 were as follows:

	< 1 year $	1 – 2 years $	2 – 5 years $	>5 years $	Total $
Accounts payable and accrued liabilities	1,045,846	-	-	-	1,045,846
Due to shareholders	-	-	-	-	-
Exploration obligations	-	-	-	-	-
Total	1,045,846	-	-	-	1,045,846

Subsequent to the year ended December 31, 2013, the Company closed a prospectus offering for total gross proceeds of CDN$12,062,500. Therefore, in the opinion of management, the working capital at December 31, 2013, together with the proceeds from the prospectus offering, is sufficient to support the Company's commitments and further expansion and growth.

Foreign Exchange Rate Risk – The Company operates in Canada and Mexico but has the majority of its cash held in Canada in Canadian dollars. The Company is exposed to foreign exchange risk due to fluctuations in foreign currencies (Canadian dollar and Mexican peso). Foreign exchange risk arises from purchase transactions as well as financial assets and liabilities denominated in these foreign currencies. The sensitivity of the Company's net loss and other comprehensive loss to changes in the exchange rate between the US dollars and the Mexican pesos would be as follows: a 10% change in the US dollar exchange rate relative to the Mexican pesos would change the Company's net loss and comprehensive loss by approximately $470,000.

The Company does not use derivative instruments to hedge exposure to foreign exchange rate risk.

Off-balance Sheet Arrangements

The Company has not entered into any material off-balance sheet arrangements such as guarantee contracts, contingent interests in assets transferred to unconsolidated entities, derivative financial obligations, or with respect to any obligations under a variable interest equity arrangement.

Critical Judgements in Applying Accounting Policies

The critical judgements that the Company's management has made in the process of applying the Company's accounting policies, apart from those involving estimations, that have the most significant effect on the amounts recognized in the Company's consolidated financial statements are as follows:

Economic Recoverability and Probability of Future Economic Benefits of Exploration, Evaluation and Development Costs

Management has determined that exploratory drilling, evaluation, development and related costs incurred which have been capitalized are economically recoverable. Management uses several criteria in its assessments of economic recoverability and probability of future economic benefit including geologic and metallurgic information, history of conversion of mineral deposits to proven and probable reserves, scoping and feasibility studies, accessible facilities, existing permits and life of mine plans.

Commencement of Commercial Production

The Company assesses the stage of each mine under construction to determine when a property reaches the stage when it is substantially complete and ready for its intended use. Criteria used to assess when a property has commenced commercial production include, among other considerations:

- the level of capital expenditures incurred relative to the expected costs to complete;
- the completion of a reasonable period of testing of the mine plant and equipment;
- the ability to produce saleable metals;
- the attainment of relevant permits;
- the ability to sustain ongoing production; and
- the achievement of pre-determined production targets.

When management determines that a property has reached commercial production, costs capitalized during development are amortized.

Functional Currency

The functional currency for each of the Company's subsidiaries is the currency of the primary economic environment in which the entity operates. Determination of functional currency involves certain judgements to determine the primary economic environment of an entity. The Company re-evaluates the functional currency of its entities when there is a change in events and conditions which previously determined the primary economic environment of an entity.

Key Sources of Estimation Uncertainty

The preparation of consolidated financial statements requires that the Company's management make assumptions and estimates of effects of uncertain future events on the carrying amounts of the Company's assets and liabilities at the end of the reporting period. Actual results may differ from those estimates as the estimation process is inherently uncertain. Actual future outcomes could differ from present estimates and assumptions, potentially having material future effects on the Company's consolidated financial statements. Estimates are reviewed on an ongoing basis and are based on historical experience and other facts and circumstances. Revisions to estimates and the resulting effects on the carrying amounts of the Company's assets and liabilities are accounted for prospectively.

The significant assumptions about the future and other major sources of estimation uncertainty as at the end of the reporting period that have a significant risk of resulting in a material adjustment to the carrying amounts of the Company's assets and liabilities are as follows:

Depletion and Depreciation

Once in commercial production, the Company computes depletion and depreciation expense based on the mine life of each of its mines. A mine's life is determined from the tonnes of ore that are available to be extracted at the end of each reporting period. The Company initially estimates the tonnes of ore available based on the findings of qualified, independent, mining professionals. These estimates are updated from time to time as additional technical and economic information becomes available. Factors that impact the computation of tonnes of ore available include the geological data on the size, depth and shape of the ore body, the prevailing and expected market price for the underlying metals to be extracted and the expected costs to extract and process the mined material. Changes in the mineable tonnes of ore available may impact the carrying value of mine under construction and development costs, exploration and evaluation properties, plant and equipment, site closure and reclamation provision and changes in the recognition of deferred tax amounts in addition to changes in the recognition of depreciation and depletion.

Impairment of Mineral Property Interest

The assessment of the fair value of plant and equipment, mine under construction and development costs, and exploration and evaluation properties requires the use of estimates and assumptions for recoverable production, long-term commodity prices, discount rates, foreign exchange rates, future capital requirements and operating performance. Changes in any of the assumptions or estimates used in determining the fair values could impact the impairment analysis.

Decommissioning and Restoration Provision

Mining and exploration activities are subject to various laws and regulations governing the protection of the environment. In general, these laws and regulations are continually changing and the Company has made, and intends to make in the future, expenditures to comply with such laws and regulations. Accounting for reclamation and remediation obligations requires management to make estimates of the future costs the Company will incur to complete the reclamation and remediation work required to comply with existing laws and regulations at each mining operation and exploration and development property. In addition, future changes to environmental laws and regulations may increase the extent of reclamation and remediation work required to be performed by the Company. Increases in future costs could materially impact the amounts charged to operations for site closure and reclamation. The provision represents management's best estimate of the present value of the future site closure and reclamation obligation.

Due to uncertainties concerning environmental remediation, the ultimate cost to the Company of future site restoration could differ from the amounts provided. The estimate of the total provision for future site closure and reclamation costs is subject to change based on amendments to laws and regulations, changes in technology, price increases and changes in interest rates, and as new information concerning the Company's closure and reclamation obligations becomes available.

Deferred Taxes

Deferred tax assets and liabilities are measured using the tax rates expected to be in effect in future periods. Management estimates these future tax rates based on information available at the period end. Actual future rates may be significantly different. Factors causing such differences include changes in the ruling government or changes in national or regional economic circumstances of the areas where mines are located.

Share-based Payments

Share-based payments are determined using the Black-Scholes option pricing model based on estimated fair values of all share-based awards at the date of grant and is expensed to the statement of loss and comprehensive loss over each award's vesting period. The Black-Scholes option pricing model utilizes subjective assumptions such as expected price volatility and expected life of the option. Changes in these input assumptions can significantly affect the fair value estimate.

Changes in Accounting Policies Including Initial Adoption

Certain pronouncements were issued by the IASB or the IFRS Interpretations Committee that are mandatory for accounting periods beginning before or on January 1, 2013. The following new standards, amendments and interpretations that have been adopted for the Company's current fiscal year have not had a material impact on the Company:

- IFRS 10 *"Consolidated Financial Statements"*
- IFRS 11 *"Joint Arrangements"*
- IFRS 12 *"Disclosure of Interests in Other Entities"*
- IFRS 13 *"Fair Value Measurement"*
- IAS 1 *"Presentation of Financial Statements" amendments*
- IFRIC Interpretation 20 "*Stripping Costs in the Production Phase of a Surface Mine"*

The following new standard has been issued but not yet applied:

IFRS 9, *Financial Instruments*, replaces the current standard IAS 39, *Financial Instruments: Recognition and Measurement*, replacing the current classification and measurement criteria for financial assets and liabilities with only two classification categories: amortized cost and fair value. The mandatory effective date for IFRS 9 is unspecified. The Company is currently evaluating the impact, if any, that the new guidance is expected to have on its consolidated financial statements.

In May 2013, the IASB issued IFRIC 21, *Levies* ("IFRIC 21"), an interpretation of IAS 37, *Provisions, Contingent Liabilities and Contingent Assets* ("IAS 37"), on the accounting for levies imposed by governments. IAS 37 sets out criteria for the recognition of a liability, one of which is the requirement for the entity to have a present obligation as a result of a past event ("obligating event"). IFRIC 21 clarifies that the obligating event that gives rise to a liability to pay a levy is the activity described in the relevant legislation that triggers the payment of the levy. IFRIC 21 is effective for annual periods commencing on or after January 1, 2014. The Company is currently evaluating the impact of applying IFRIC 21 on its consolidated financial statements.

Subsequent Event

Stock Options

On April 10, 2014, the Company granted 400,000 incentive stock options to a director having an exercise price of CDN$1.00 each expiring April 10, 2019.

Outstanding Share Data

Authorized share capital: Unlimited number of Common Shares

All share information is reported as of April 30, 2014 in the following table.

Issued and Outstanding Common Shares				103,493,484
	Expiry Date	Exercise Price (CDN$)		
Options	May 10, 2015	$0.90	300,000	
	April 12, 2017	$0.90	4,806,666	
	July 24, 2017	$0.90	800,000	
	February 28, 2018	$1.85	400,000	
	July 29, 2018	$1.22	300,000	
	April 10, 2019	$1.00	400,000	7,006,666
Warrants	February 19, 2015	$1.85	1,311,000	
	March 11, 2016	$1.00	645,000	
	March 20, 2016	$1.00	78,750	2,034,750
Fully Diluted				112,534,900

6,325,856 of the outstanding common shares are held in escrow.

Disclosure Controls and Procedures

Disclosure controls and procedures are intended to provide reasonable assurance that information required to be disclosed is recorded, processed, summarized, and reported within the time periods specified by securities regulations and that the information required to be disclosed is accumulated and communicated to management. Internal controls over financial reporting are intended to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with IFRS. In connection with National Instrument 52-109 (Certificate of Disclosure in Issuer's Annual and Interim Filings) ("NI 52-109"), the Chief Executive Officer and Chief Financial Officer of the Company have filed a Venture Issuer Basic Certificate with respect to the financial information contained in the consolidated financial statements for the year ended December 31, 2013 and this accompanying MD&A (together, the "Annual Filings").

In contrast to the full certificate under NI 52-109, the Venture Issuer Basic Certificate does not include representations relating to the establishment and maintenance of disclosure controls and procedures and internal control over financial reporting, as defined in NI 52-109. For further information the reader should refer to the Venture Issuer Basic Certificates filed by the Company with the Annual Filings on SEDAR at www.sedar.com.

Risks and Uncertainties

Natural resources exploration, development, production and processing involve a number of business risks, some of which are beyond the Company's control. These can be categorized as operational, financial and regulatory risks.

Operational risks include: the Company may not be able to find and develop resources economically, the Company cannot guarantee title to its properties, the Company may have difficulty in marketing production and services, the Company must manage changing governmental laws and regulations, the Company may have difficulty in hiring and retaining skilled employees and contractors, environmental hazards (including discharge of pollutants or hazardous chemicals), industrial accidents and occupational and health hazards, mechanical failures, the unavailability of materials and equipment, pit slope failures, unusual or unexpected rock formations, poor or unexpected geological or metallurgical conditions, poor or inadequate ventilation, failure of mine communication systems, poor water condition, interruptions to gas and electricity supplies, human error and adverse weather conditions, there is no assurance that the Company will acquire additional mineral properties and any acquisitions may expose the Company to new risks, and the mining industry is intensely competitive for the acquisition of new properties, access to capital and hiring of skilled personnel. The Company continuously monitors and responds to changes in these factors and seeks to adhere to all regulations governing its operations.

Financial risks include commodity prices, interest rates and fluctuating foreign exchange rates, all of which are beyond the Company's control. Additional financial risks are the Company's ability to raise capital to continue funding its operations.

Regulatory risks include the possible delays in getting regulatory approval to, and permits for, the transactions that the Board of Directors believe to be in the best interest of the Company, and include increased fees for filings, the introduction of ever more complex reporting requirements the cost of which the Company must meet in order to maintain its exchange listing.

Outlook

Notwithstanding the production challenges faced during start-up of the Rosario Mine during 2013, the Rosario Mine continues to steadily ramp up production and is approaching positive cash flow from operations. The near term focus of the Company is to continue increasing the production throughput at the Rosario Mine. To this end the Company has begun installing an additional ball mill to the milling facility. This process is expected to be completed in the second quarter of 2014 and will increase milling capacity to 700 tonnes per day.

Exploration activities will continue at the San Felipe Project including preparation of a technical engineering study. Based on the results of this study, and assuming a positive result, the Company also expects to focus its efforts in 2014 on advancing the San Felipe Project to a production decision.

Once positive cash flow is established at the Rosario Mine the Company expects to recommence exploration activities at the Gavilanes Property.

Additional Disclosure for Venture Issuers without Significant Revenue

The Company provides disclosure related to capitalized or expensed exploration and development costs in the notes to the financial statements and disclosure related to general and administration expenses in the statements of loss and comprehensive loss. The Company has no expensed research and development costs nor deferred development costs.

Qualified Persons

All technical information which is included in this statement has been reviewed and approved by Donald E. Hulse P.E. of Gustavson and is consistent with work published by Gustavson.

Other Information

Additional information related to the Company is available on SEDAR at www.sedar.com and on the Company's website, www.santacruzsilver.com.