Condensed Interim Consolidated Financial Statements

Three and Six Months Ended June 30, 2014 and 2013

(Unaudited – expressed in US Dollars)

NOTICE OF NO AUDITOR REVIEW OF CONDENSED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

The accompanying unaudited condensed interim consolidated financial statements of the Company and all information contained in the second quarter 2014 report have been prepared by and are the responsibility of the Company's management.

The Audit Committee of the Board of Directors has reviewed the condensed interim consolidated financial statements and related financial reporting matters.

The Company's independent auditor has not performed a review of these condensed interim consolidated financial statements in accordance with standards established by the Canadian Institute of Chartered Accountants for a review of condensed interim consolidated financial statements by an entity's auditor.

Santacruz Silver Mining Ltd.
Condensed Interim Consolidated Statements of Financial Position
(Unaudited – expressed in US Dollars)

	Note	June 30, 2014 $	December 31, 2013 $
ASSETS			
Current			
Cash and cash equivalents	**4**	1,852,987	1,618,472
VAT recoverable and receivables	**5**	7,253,078	5,637,805
Inventory	**6**	810,575	633,580
Prepaid expenses and deposits		198,162	135,794
Deferred financing costs		7,381	-
		10,122,183	8,025,651
Plant and equipment	**7**	12,058,971	10,632,230
Mine property	**8**	8,642,419	8,770,992
Exploration and evaluation properties	**9**	39,020,158	33,583,145
		69,843,731	61,012,018
LIABILITIES			
Current			
Accounts payable and accrued liabilities		2,954,682	1,045,846
		2,954,682	1,045,846
Decommissioning and restoration provision	**10**	618,903	595,953
Deferred income tax liability		3,916,391	3,974,151
		7,489,976	5,615,950
EQUITY			
Share capital	**11**	85,606,637	75,912,147
Stock options and warrants reserve	**11(d)**	5,665,827	5,316,201
Accumulated other comprehensive loss		(436,256)	(503,931)
Deficit		(28,482,453)	(25,328,349)
		62,353,755	55,396,068
		69,843,731	61,012,018

Commitments *(Notes 8, 9 and 16)*
Subsequent Event *(Note 17)*

Approved on behalf of the Board:

"Arturo Préstamo Elizondo"
Director – Arturo Préstamo Elizondo

"Craig A. Angus"
Director – Craig A. Angus

(The accompanying notes are an integral part of these condensed interim consolidated financial statements)

Santacruz Silver Mining Ltd.
Condensed Interim Consolidated Statements of Loss and Comprehensive Loss
For the three and six months ended June 30, 2014 and 2013
(Unaudited – expressed in US Dollars)

	Note	Three months ended June 30, 2014 $	2013 $	Six months ended June 30, 2014 $	2013 $
Revenues		2,302,056	-	4,233,623	-
Expenses					
Operating expenses		2,256,465	-	5,222,073	-
Amortization and depletion		453,735	-	766,805	-
		2,710,200	-	5,988,878	-
Mine operating loss		(408,144)	-	(1,755,255)	-
General and administrative expenses					
Administrative		88,821	141,999	284,639	247,230
Depreciation		1,901	25,178	3,798	26,194
Management and consulting fees	**12**	140,727	102,322	319,242	175,259
Other		50,647	-	102,847	385
Professional fees	**12**	166,330	124,546	296,849	194,557
Salaries and benefits		45,674	44,003	91,419	92,995
Share-based payments	**11(e)**	141,465	56,838	149,957	427,809
Shareholder communications		51,612	136,592	97,008	269,490
Transfer agent and filing fees		47,654	21,143	74,327	68,575
Travel		33,713	34,694	71,964	88,465
		(768,544)	(687,315)	(1,492,050)	(1,590,959)
Other income (expenses)					
Accretion	**10**	(10,487)	-	(20,783)	-
Foreign exchange gain		70,853	67,847	9,435	184,926
Other income		54,104	55,838	92,798	99,859
		114,470	123,685	81,450	284,785
Loss before income tax		(1,062,218)	(563,630)	(3,165,855)	(1,306,174)
Income tax recovery (expense)					
Current		(29,609)	(1,614)	(46,009)	(1,824)
Deferred		-	-	57,760	-
		(29,609)	(1,614)	11,751	(1,824)
Net loss for the period		(1,091,827)	(565,244)	(3,154,104)	(1,307,998)
Other comprehensive income (loss)					
Exchange differences on translating foreign operations		61,561	(320,049)	67,675	(473,820)
Comprehensive loss for the period		(1,030,266)	(885,293)	(3,086,429)	(1,781,818)
Loss per share – basic and diluted		(0.01)	(0.01)	(0.03)	(0.02)
Weighted average number of common shares outstanding		103,493,484	89,973,369	98,789,755	83,830,482

(The accompanying notes are an integral part of these condensed interim consolidated financial statements)

Santacruz Silver Mining Ltd.
Condensed Interim Consolidated Statements of Cash Flows
For the six months ended June 30, 2014 and 2013
(Unaudited – expressed in US Dollars)

Cash Provided By (Used In):	**2014** **$**	**2013** **$**
Operations:		
Net loss for the period	(3,154,104)	(1,307,998)
Items not affecting cash:		
Deferred income tax recovery	(57,760)	-
Accretion	20,783	-
Amortization and depletion	766,805	-
Depreciation	3,798	26,194
Share-based payments	149,957	427,809
Gain on disposal of equipment	-	(1,046)
Changes in non-cash working capital:		
VAT recoverable and receivables	(1,615,273)	(2,994,789)
Prepaid expenses and deposits	(62,368)	(54,999)
Inventory	(176,995)	(185,036)
Deferred financing costs	(7,381)	61,748
Accounts payable and accrued liabilities	1,908,836	(85,751)
	(2,223,702)	(4,113,868)
Investing:		
Exploration and evaluation properties	(5,430,613)	(19,892,163)
Acquisition and development costs on mine property	(220,000)	(2,209,660)
Proceeds from disposal of equipment	-	12,880
Acquisition of plant and equipment	(1,855,226)	(3,011,360)
	(7,505,839)	(25,100,303)
Financing:		
Issuance of common shares, net	9,894,159	37,278,580
Due to shareholders	-	(119,713)
	9,894,159	37,158,867
Net increase in cash	164,618	7,944,696
Effect of exchange rate changes on cash	69,897	(473,111)
Cash and cash equivalents – beginning of period	1,618,472	2,879,378
Cash and cash equivalents – end of period	1,852,987	10,350,963

Non-cash Transactions *(Note 13)*

Santacruz Silver Mining Ltd.

Consolidated Statements of Changes in Equity

(Expressed in US Dollars)

	Share Capital		Stock Options and Warrants Reserve			
	Number of Shares	**Amount $**	**$**	**AOCI $**	**Deficit $**	**Total $**
Balance, December 31, 2012	67,846,439	38,186,694	3,797,949	(89,198)	(19,009,017)	22,886,428
Issued pursuant to prospectus offering	21,910,000	39,949,557	-	-	-	39,949,557
Exercise of warrants	224,545	296,064	(73,928)	-	-	222,136
Share issuance costs	-	(3,903,509)	997,642	-	-	(2,905,867)
Share-based payments	-	-	427,809	-	-	427,809
Net loss and comprehensive loss for the period	-	-	-	(473,820)	(1,307,998)	(1,781,818)
Balance, June 30, 2013	89,980,984	74,528,806	5,149,472	(563,018)	(20,317,015)	58,798,245
Issued for mineral properties	1,250,000	1,292,961	-	-	-	1,292,961
Exercise of warrants	100,000	90,380	(80,667)	-	-	9,713
Share-based payments	-	-	247,396	-	-	247,396
Net loss and comprehensive loss for the period	-	-	-	59,087	(5,011,334)	(4,952,247)
Balance, December 31, 2013	91,330,984	75,912,147	5,316,201	(503,931)	(25,328,349)	55,396,068
Issued pursuant to prospectus offering	12,162,500	10,864,694	-	-	-	10,864,694
Share issuance costs	-	(1,170,204)	199,669	-	-	(970,535)
Share-based payments	-	-	149,957	-	-	149,957
Net loss and comprehensive loss for the period	-	-	-	67,675	(3,154,104)	(3,086,429)
Balance, June 30, 2014	103,493,484	85,606,637	5,665,827	(436,256)	(28,482,453)	62,353,755

(The accompanying notes are an integral part of these condensed interim consolidated financial statements)

1. Nature of Operations

Santacruz Silver Mining Ltd. (the "Company") 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 is listed for trading on the TSX Venture Exchange ("TSX-V") under the symbol "SCZ". The Company also trades on the OTCQX under the trading symbol "SZSMF".

The Company is engaged in the exploration and commercial exploitation of mining concessions in Mexico, with a primary focus on silver, but also including gold, lead and zinc. The Company has acquired the mining concession rights to the following properties:

- Rosario in the mining municipality of Charcas, state of San Luis Potosi, Mexico.
- San Felipe de Jesús in the mining municipality of Sonora, Mexico.
- Gavilanes in the mining municipality of San Dimas, Durango, Mexico.

2. Basis of Presentation

These condensed interim consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB") applicable to the preparation of interim financial statements, including IAS 34, *Interim Financial Reporting*. These condensed interim consolidated financial statements should be read in conjunction with the annual consolidated financial statements for the year ended December 31, 2013 which have been prepared in accordance with IFRS as issued by the IASB.

These condensed interim consolidated financial statements have been prepared on a basis consistent with the significant accounting policies disclosed in Note 3 of the annual consolidated financial statements for the year ended December 31, 2013 and were approved for issue by the Board of Directors on August 28, 2014.

3. Significant Accounting Policies

The accounting policies applied by the Company in these condensed interim consolidated financial statements are the same as those applied by the Company in its consolidated financial statements as at and for the year ended December 31, 2013, except for the following policies and disclosure requirements adopted in the current financial period:

a) 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.

(Unaudited – expressed in US Dollars)

When management determines that a property has reached commercial production, costs capitalized during development are amortized. The Company determined its Rosario Mine to be in commercial production effective January 1, 2014.

b) IFRIC 21 – Levies Imposed by Governments

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 has evaluated the impact of IFRIC 21 and has determined that it has no material impact on its financial statements.

c) IAS 32 – Offsetting of Financial Instruments ("IAS 32")

The amendments to IAS 32, *Financial Instruments: Presentation*, clarify the criteria that should be considered in determining whether an entity has a legally enforceable right of set off in respect of its financial instruments. Amendments to IAS 32 are applicable to annual periods beginning on or after January 1, 2014, with retrospective application required. The Company has evaluated the impact of IAS 32 and has determined that it has no material impact on its financial statements.

4. Cash and Cash Equivalents

	June 30, 2014 $	December 31, 2013 $
Cash on hand or held with banks:		
US dollar	1,728,479	32,969
Canadian dollar	44,695	1,089,535
Mexican peso	69,036	485,156
	1,842,210	1,607,660
Short-term investments	10,777	10,812
Total	1,852,987	1,618,472

5. VAT recoverable and receivables

	June 30, 2014 $	December 31, 2013 $
Value added taxes recoverable	6,591,363	5,226,118
Trade receivables	618,867	310,810
Other receivables	42,848	100,877
Total	7,253,078	5,637,805

(Unaudited – expressed in US Dollars)

6. Inventory

	June 30, 2014 $	December 31, 2013 $
Mined ore inventory	202,956	265,636
Concentrate inventory	277,823	238,800
Supplies inventory	329,796	129,144
Total	810,575	633,580

7. Plant and Equipment

Cost	Office Furniture and Equipment $	Assets under Construction $	Plant and Equipment $	Vehicles $	Computer Hardware $	Total $
Balance, December 31, 2012	39,573	-	5,671,066	197,642	82,045	5,990,326
Additions	16,309	-	5,471,593	147,214	56,792	5,691,908
Disposals	-	-	-	(32,180)	(466)	(32,646)
Foreign exchange	(948)	-	-	-	-	(948)
Balance, December 31, 2013	54,934	-	11,142,659	312,676	138,371	11,648,640
Additions	682	462,088	1,348,146	35,464	8,846	1,855,226
Foreign exchange	(44)	-	-	-	-	(44)
Balance, June 30, 2014	55,572	462,088	12,490,805	348,140	147,217	13,503,822
Accumulated Depreciation						
Balance, December 31, 2012	3,056	-	598	30,553	12,251	46,458
Additions	4,389	-	878,670	59,408	31,347	973,814
Disposals	-	-	-	(3,626)	(128)	(3,754)
Foreign exchange	(108)	-	-	-	-	(108)
Balance, December 31, 2013	7,337	-	879,268	86,335	43,470	1,016,410
Additions	2,483	-	381,261	30,096	14,590	428,430
Foreign exchange	11	-	-	-	-	11
Balance, June 30, 2014	9,831	-	1,260,529	116,431	58,060	1,444,851
Carrying amount at December 31, 2013	47,597	-	10,263,391	226,341	94,901	10,632,230
Carrying amount at June 30, 2014	45,741	462,088	11,230,276	231,709	89,157	12,058,971

Depreciation during the three and six months ended June 30, 2014 was $254,755 and $428,430 (2013 – $219,860 and $236,884). During the three and six months ended June 30, 2014, $nil and $nil of the depreciation was capitalized to mine property (2013 – $72,527 and $88,535), and $3,430 and $6,400 of the depreciation was capitalized to exploration and evaluation properties (2013 – $nil and $nil). The Company does not have any equipment under lease for any of the periods presented.

(Unaudited – expressed in US Dollars)

8. Mine Property

The summary of accumulated costs in the Company's mine property as of June 30, 2014 and December 31, 2013 are as follows:

	Balance, Dec 31, 2012 $	Year Ended Dec 31, 2013 $	Balance, Dec 31, 2013 $	Period Ended June 30, 2014 $	Balance, June 30, 2014 $
Rosario, Charcas, San Luis Potosi, Mexico					
Acquisition costs					
Option payments – cash	852,818	622,182	1,475,000	220,000	1,695,000
	852,818	622,182	1,475,000	220,000	1,695,000
Exploration, development and pre-production costs					
Depreciation	39,873	954,567	994,440	-	994,440
Drilling	912,865	58,673	971,538	-	971,538
Geological consulting	55,649	467,173	522,822	-	522,822
Mine development	119,627	580,038	699,665	-	699,665
Mine site support and office costs	1,345,549	1,351,194	2,696,743	-	2,696,743
Permitting and other expenses	395,963	121,989	517,952	-	517,952
Safety and maintenance	22,608	660,137	682,745	-	682,745
Water well project	89,644	598,948	688,592	-	688,592
Pre-production revenue	-	(1,441,602)	(1,441,602)	-	(1,441,602)
Ore purchased	-	367,144	367,144	-	367,144
	2,981,778	3,718,261	6,700,039	-	6,700,039
Amortization and depletion	-	-	-	(348,573)	(348,573)
Decommissioning liabilities *(Note 10)*	-	595,953	595,953	-	595,953
Total	3,834,596	4,936,396	8,770,992	(128,573)	8,642,419

Rosario, Charcas, San Luis Potosi, Mexico

Rey David, Charcas, San Luis Potosi, Mexico

Pursuant to a mining exploration and promise of assignment of rights agreement dated February 15, 2010, as amended on February 15, 2012, March 20, 2012, August 15, 2013, October 15, 2013, February 4, 2014 and April 14, 2014, the Company was granted an option to acquire a 100% interest in the Rey David property located in the municipality of Charcas, San Luis Potosi, Mexico. The property covers 42 hectares and is subject to a 0.4% Net Smelter Returns ("NSR") in favour of the optionor. The NSR increases by 0.1% per year, until it reaches a maximum of 1%. The Company has the right to buy back the NSR for a cash payment of $637,000 within the 48 months following the execution of the agreement. Following the 48-month option period, the purchase price of the buyout will increase in proportion to the 0.1% increase to a maximum of $1,592,500 in year 10.

To maintain and exercise the option, the Company must make $2,000,000 of cash payments to the property vendor. As at June 30, 2014, the Company has made total payments of $1,555,000 and is currently re-negotiating the terms of the $445,000 payment due on July 15, 2014.

San Rafael, Charcas, San Luis Potosi, Mexico

Pursuant to a mining exploration and promise of assignment of rights agreement dated February 22, 2011, the Company was granted an option to acquire a 100% interest in the San Rafael property, located in the municipality of Charcas, San Luis Potosí, Mexico. The vendor retains a 2.5% NSR. The Company also has an obligation to pay the local Ejido 300,000 Mexican pesos per year for surface access on the San Rafael concessions. To maintain and exercise the option, the Company must make $220,000 of cash payments to the property vendor. As at June 30, 2014, the Company has made total payments of $140,000 and the residual payments are as follows:

- $20,000 on August 22, 2014 (paid subsequent to June 30, 2014);
- $20,000 on February 22, 2015;
- $20,000 on August 22, 2015; and
- $20,000 on February 22, 2016.

(Unaudited – expressed in US Dollars)

9. Exploration and Evaluation Properties

The Company is actively investigating, evaluating and conducting exploration activities in Mexico. The summary of accumulated costs in its exploration and evaluation properties as of June 30, 2014 and December 31, 2013 are as follows:

		Balance, Dec 31, 2012 $	Year Ended Dec 31, 2013 $	Balance, Dec 31, 2013 $	Period Ended June 30, 2014 $	Balance, June 30, 2014 $
a)	**Gavilanes, San Dimas, Durango, Mexico**					
	Acquisition costs					
	Option payments – cash	1,515,000	1,800,000	3,315,000	1,500,000	4,815,000
		1,515,000	1,800,000	3,315,000	1,500,000	4,815,000
	Exploration costs					
	Depreciation	-	4,130	4,130	2,581	6,711
	Drilling	813,099	1,005,028	1,818,127	25,008	1,843,135
	Geological consulting	-	-	-	11,655	11,655
	Mine site support and office costs	22,263	45,557	67,820	1,037	68,857
	Professional fees	-	46,951	46,951	6,089	53,040
	Safety and maintenance	28,077	40,808	68,885	20,927	89,812
		863,439	1,142,474	2,005,913	67,297	2,073,210
		2,378,439	2,942,474	5,320,913	1,567,297	6,888,210
b)	**San Felipe de Jesús, Sonora, Mexico**					
	Acquisition costs					
	Option payments – cash	6,000,000	16,883,997	22,883,997	1,000,000	23,883,997
	Option payments – shares	-	1,292,961	1,292,961	-	1,292,961
	Exploration obligation still to be incurred	2,383,177	(2,383,177)	-	-	-
		8,383,177	15,793,781	24,176,958	1,000,000	25,176,958
	Exploration costs					
	Depreciation	-	5,778	5,778	3,819	9,597
	Drilling	102,454	2,749,794	2,852,248	1,534,107	4,386,355
	Geological consulting	-	76,608	76,608	743,898	820,506
	Mine site support and office costs	185,102	130,591	315,693	334,536	650,229
	Professional fees	106,404	27,576	133,980	-	133,980
	Safety and maintenance	222,863	478,104	700,967	253,356	954,323
		616,823	3,468,451	4,085,274	2,869,716	6,954,990
		9,000,000	19,262,232	28,262,232	3,869,716	32,131,948
Total		11,378,439	22,204,706	33,583,145	5,437,013	39,020,158

a) Gavilanes, San Dimas, Durango, Mexico

Gavilanes I, San Dimas, Durango, Mexico

Pursuant to a mining exploration and promise of assignment of rights agreement dated April 27, 2010, as amended October 12, 2010, December 27, 2010, October 29, 2011, January 30, 2012, March 20, 2012, April 26, 2013 and December 17, 2013 (the "Gavilanes I Agreement"), the Company was granted an option to acquire a 100% interest in the Gavilanes property located in San Dimas, Durango, Mexico. The property is subject to a 3% NSR in favour of the optionor, up to a maximum of $2,000,000.

As at June 30, 2014, the Company has made total payments of $3,600,000 to the vendors and accordingly has fulfilled the terms of the Gavilanes I Agreement.

Gavilanes II, San Dimas, Durango, Mexico

Pursuant to a mining exploration and promise of assignment of rights agreement dated May 1, 2010, as amended October 12, 2010, December 27, 2010, January 7, 2011, November 8, 2013 and April 10, 2014, the Company was granted an option to acquire a 100% interest in the Gavilanes property (named Gavilanes II) located in San Dimas, Durango, Mexico. The property is subject to a 2% NSR in favour of the optionor, up to a maximum of $1,000,000. The NSR may be purchased by the Company for $1,000,000. To maintain and exercise the option, the Company must make $2,265,000 of cash payments to the property vendor. As at June 30, 2014, the Company has made total payments of $1,115,000 and must make one residual payment of $1,150,000 on December 17, 2014.

Gavilanes MHM Fraccion, San Dimas, Durango, Mexico

Pursuant to an assignment of mining concession rights agreement dated January 5, 2012, as amended on February 20, 2012 and March 23, 2012, the Company acquired the Gavilanes MHM Fraccion 2 concession and two mining concession applications, Gavilanes MHM Fraccion 1 and Gavilanes HMX, for cash payments of $100,000 made on April 15, 2012 and $1,000,000 upon commencement of commercial production, and the grant to the vendor of a 3% NSR.

b) San Felipe de Jesús, Sonora, Mexico

San Felipe de Jesús

Pursuant to a mining exploration and promissory sale agreement dated August 3, 2011 and amended December 9, 2011, October 8, 2012 and August 13, 2013 (the "San Felipe Agreement"), the Company was granted an option to acquire a 100% interest in the San Felipe de Jesús project located in Sonora, Mexico. In addition to cash payments of $23,700,000 made to date and the issuance of 1,250,000 common shares of the Company at a deemed issue price of CDN$1.07 per share, in order to maintain and exercise the option, the Company must incur exploration expenditures of $3,000,000 by October 31, 2015 and make additional payments as follows:

- Annual surface right payments of 520,000 Mexican Pesos ($39,744) on or before February 19 of each year until the project reaches commercial production;
- $5,000,000 on October 31, 2014 (as described under "El Gachi" below);
- $15,000,000 on or before October 31, 2015; and
- $1,000,000 for restructuring fees on or before October 31, 2015. At the Company's election this payment may be made in cash or through the issuance of $1,500,000 of common shares of the Company, at an issuance price calculated at the time of issuance pursuant to the policies of the TSX-V and subject to a minimum issuance price of CDN$1.07 per share.

Pursuant to the San Felipe Agreement, if the 1,250,000 common shares issued to the optionor were sold to third parties for total proceeds of less than $1,300,000 before August 13, 2014, the Company was required to reimburse the optionor for the difference between $1,300,000 and the actual proceeds. On December 30, 2013, the 1,250,000 common shares were sold for $1,116,003. As such, the Company paid the optionor $183,997, which has been capitalized as mineral property acquisition costs.

With respect to the exploration expenditures commitment, if the Company did not incur $3,000,000 of expenditures by October 31, 2015, it was obligated to reimburse the optionor for the difference between $3,000,000 and the actual exploration expenditures incurred. As such, upon execution of the San Felipe Agreement, $3,000,000 was capitalized as mineral property acquisition costs with an offsetting charge for exploration obligations. All $3,000,000 of exploration expenditures had been incurred by December 31, 2013.

Any minerals extracted in commercially usable quantities remain the property of the optionor until the Company has exercised its option and acquired the project.

The project is subject to a 1% NSR in favour of the optionor. The Company has the right at any time to buy back the NSR for a cash payment of $3,000,000. In the event commercial production has not occurred by December 9, 2015, the Company must make an advance royalty payment of $500,000, which payment will be deducted from the royalty.

Pursuant to the terms of the San Felipe Agreement, a change of control could accelerate payments required under this agreement to acquire the rights. In the event the Company is unable to make such payments within 15 days after a change of control, it could lose its rights to the San Felipe project.

El Gachi

On March 7, 2013, pursuant to the San Felipe Agreement, the Company obtained an option to acquire a 100% interest in the 48,057.33 hectare El Gachi property located 30 kilometers from the San Felipe project in Sonora State. Under the terms of the San Felipe Agreement, the Company has the option to acquire the El Gachi property, milling equipment, buildings, land property, and water rights by making a $5,000,000 payment before or by October 2014 (as referred to above).

10. Decommissioning and Restoration Provision

The Company’s estimates of future decommissioning and restoration for reclamation and closure costs for its mines are based on reclamation standards that meet Mexican regulatory requirements. Elements of uncertainty in estimating these amounts include potential changes in regulatory requirements, reclamation plans and cost estimates, discount rates and timing of expected expenditures.

The undiscounted amount of estimated cash flows required to settle the decommissioning and reclamation costs was estimated at $956,970. The key assumptions on which this estimate was based on are:

- Expected timing of the cash flows is based on the estimated useful life of the Rosario Mine to the extent of currently known measured and indicated mineral resources. The majority of the expenditures are expected to occur in 2020, which is the anticipated closure date.
- The discount rate used is 7%.

(Unaudited – expressed in US Dollars)

The discounted liability for the decommissioning and restoration provision is as follows:

	June 30, 2014 $	**December 31, 2013 $**
Balance, beginning of period / year	595,953	-
Provision	-	595,953
Accretion	20,783	-
Foreign exchange	2,167	-
Balance, end of period / year	618,903	595,953

11. Share Capital

a) Authorized

Unlimited number of common shares without par value.

b) Share Capital Transactions

(i) On February 19, 2013, the Company closed a prospectus offering (the "2013 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 up to February 19, 2015. The fair value of the broker warrants ($997,642) was estimated using the Black Scholes option-pricing model and was charged to share issue costs and credited to warrants reserve. The assumptions used in the option pricing model are as follows: risk-free interest rate – 0.78%; expected life – 2 years; expected volatility – 77.33%; and expected dividends – nil. The Company also issued 60,000 common shares as corporate finance fee and incurred additional issue costs of $508,894.

(ii) On August 16, 2013, as described in Note 9(b), 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.

(iii) 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. A value of $154,595 was transferred from warrants reserve to share capital as a result.

(iv) On March 11, 2014, the Company closed a prospectus offering (the "2014 Offering"), pursuant to which 12,062,500 common shares were issued at a price of CDN$1.00 per share for gross proceeds of $10,864,694 (CDN$12,062,500). The underwriters received a cash fee of $651,882 (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. The fair value of the broker warrants ($199,669) was estimated using the Black Scholes option-pricing model and was charged to share issue costs and credited to warrants reserve. The assumptions used in the option pricing model are as follows: risk-free interest rate – 1.30%; expected life – 2 years; expected volatility – 51.08%; and expected dividends – nil. The Company also issued 100,000 common shares as corporate finance fee and incurred additional issue costs of $318,653.

(Unaudited – expressed in US Dollars)

c) Escrow

There are 6,325,856 common shares of the Company held in escrow as at June 30, 2014 (December 31, 2013 – 9,488,784 shares). Under the Escrow Agreement, the common shares held in escrow will be released from escrow as to 3,162,928 common shares on each of October 13, 2014 and April 13, 2015.

d) Stock Options and Warrants Reserve

The following is a summary of the stock options and warrants reserve:

	June 30, 2014 $	December 31, 2013 $
Stock options	4,104,244	3,954,287
Warrants	1,561,583	1,361,914
	5,665,827	5,316,201

e) Stock Options

The Company has established a stock option plan (the "Plan") for the benefit of full-time and part-time employees, officers, directors and consultants of the Company and its affiliates. The maximum number of shares available under the Plan is limited to 10% of the issued common shares. Options granted under the Plan have a maximum term of ten years and the vesting provisions of options granted are at the discretion of the Board. Details of options activity for the six months ended June 30, 2014 and the year ended December 31, 2013 are as follows:

	Number of Stock Options	Weighted Average Exercise Price CDN$	Weighted Average Remaining Contractual Life (Years)
Balance, December 31, 2012	5,906,666	0.90	4.22
Granted	700,000	1.58	-
Balance, December 31, 2013	6,606,666	0.97	3.09
Granted	400,000	1.00	-
Balance, June 30, 2014	7,006,666	0.97	2.96
Unvested	(60,000)	0.90	0.86
Exercisable, June 30, 2014	6,946,666	0.97	2.97

The balance of options outstanding as at June 30, 2014 is as follows:

Expiry Date	Exercise Price (CDN$)	Remaining Life (Years)	Options Outstanding	Unvested	Vested
April 12, 2017	0.90	2.79	4,806,666	-	4,806,666
May 10, 2015	0.90	0.86	300,000	60,000	240,000
July 24, 2017	0.90	3.07	800,000	-	800,000
February 28, 2018	1.85	3.67	400,000	-	400,000
July 29, 2018	1.22	4.08	300,000	-	300,000
April 8, 2019	1.00	4.78	400,000	-	400,000
			7,006,666	90,000	6,946,666

(Unaudited – expressed in US Dollars)

The fair values of the options granted during the six months ended June 30, 2014 were estimated using the Black Scholes option-pricing model. Assumptions used in the pricing model are as follows: risk-free interest rate – 2.20% (2013 – 1.63%); expected life – 5 years (2013 – 5 years); expected volatility – 52.75% (2013 – 80.35%); expected forfeitures – 0% (2013 – 0%); and expected dividends – $nil (2013 – $nil).

The weighted average fair value of stock options granted during the six months ended June 30, 2014 was $0.38 per option (2013 – $1.13).

During the three and six months ended June 30, 2014, the Company recorded share-based payments expense of $141,465 and $149,957 respectively (2013 – $56,838 and $427,809).

f) Warrants

Details of warrants activity for the six months ended June 30, 2014 and the year ended December 31, 2013 are as follows:

	Number of Warrants	Weighted Average Exercise Price CDN$	Weighted Average Remaining Contractual Life (Years)
Balance, December 31, 2012	1,416,747	0.94	1.24
Issued	1,311,000	1.85	-
Exercised	(324,545)	0.72	-
Balance, December 31, 2013	2,403,202	1.45	0.75
Issued	723,750	1.00	-
Expired	(1,092,202)	1.00	-
Balance, June 30 2014	2,034,750	1.50	1.02

The balance of warrants outstanding as at June 30, 2014 is as follows:

Expiry Date	Exercise Price CDN$	Remaining Life (Years)	Warrants Outstanding
February 19, 2015	1.85	0.64	1,311,000
March 11, 2016	1.00	1.70	645,000
March 20, 2016	1.00	1.72	78,750
			2,034,750

(Unaudited – expressed in US Dollars)

12. Related Party Transactions

During the three and six months ended June 30, 2014 and 2013, the Company incurred the following charges by directors and officers of the Company and by companies controlled by directors and officers of the Company:

	Three months ended June 30,		Six months ended June 30,	
	2014 $	2013 $	2014 $	2013 $
Accounting and corporate secretarial fees	66,147	37,035	98,739	70,749
Directors' fees	26,804	41,455	48,958	60,947
Management fees	148,490	54,467	251,550	147,685
Share-based payments	138,495	-	138,495	333,519

At June 30, 2014, directors and officers or their related companies were owed $54,974 (December 31, 2013 – $28,333) in respect of the services rendered.

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.

13. Non-cash Transactions

Investing and financing activities that do not have a direct impact on cash flows are excluded from the consolidated statements of cash flows. During the six months ended June 30, 2014, the following transactions were excluded from the consolidated statements of cash flows:

- The Company issued 723,750 broker warrants at the fair value of $199,669 pursuant to the 2014 Offering; and
- The Company issued 100,000 common shares as corporate finance fee at the fair value of $90,070 pursuant to the 2014 Offering.

During the six months ended June 30, 2013, the following transactions were excluded from the consolidated statements of cash flows:

- The Company issued 1,311,000 broker warrants at the fair value of $997,642 pursuant to the 2013 Offering; and
- The Company issued 60,000 common shares as corporate finance fee at the fair value of $109,701 pursuant to the 2013 Offering.

14. Segmented Information

The Company has identified its operating segments based on the internal reports that are reviewed and used by the chief executive officer and the executive management in assessing performance and in determining the allocation of resources.

The Company considers the business from a geographic perspective and assesses the performance of the operating segments based on measures such as net property, plant and equipment as well as operational results.

(Unaudited – expressed in US Dollars)

a) Operating Segment

The Company's operations are limited to a single industry segment, being exploration and development of mineral properties.

b) Geographic Segments

By geographic areas, the Company's non-current assets as at June 30, 2014 and December 31, 2013 and losses by geographic areas for the three and six months ended June 30, 2014 and 2013 are as follows:

	Losses			
	Three Months Ended June 30,		Six Months Ended June 30,	
	2014	2013	2014	2013
	$	$	$	$
Canada	554,688	474,878	960,535	1,091,430
Mexico	537,139	90,366	2,193,569	216,568
Total	1,091,827	565,244	3,154,104	1,307,998

	Non-Current Assets	
	June 30, 2014	December 31, 2013
	$	$
Canada	10,741	11,462
Mexico	59,710,807	52,974,905
Total	59,721,548	52,986,367

15. Financial Instruments

The classification of the financial instruments as well as their carrying values as at June 30, 2014 and December 31, 2013 is shown in the table below:

	June 30, 2014	December 31, 2013
	$	$
Loans and receivables	2,514,702	2,030,159
Other financial liabilities	(2,954,682)	(1,045,846)

a) Fair Value 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, and accounts payable and accrued liabilities, approximate their fair values because of their short term nature.

As at June 30, 2014, the Company does not have any financial instruments measured at fair value.

b) Management of Risks Arising from Financial Instruments

The Company is exposed to credit risk and market risks including interest rate risk, liquidity risk, and foreign exchange rate risk.

(i) Credit Risk – 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.

(ii) Interest Rate Risk – 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.

(iii) Liquidity Risk – 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 cash flow requirements as at June 30, 2014 were as follows:

	< 1 year $	**1 – 2 years $**	**2 – 5 years $**	**>5 years $**	**Total $**
Accounts payable and accrued liabilities	2,954,682	-	-	-	2,954,682
Total	2,954,682	-	-	-	2,954,682

Contractual 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
Total	1,045,846	-	-	-	1,045,846

In the opinion of management, the Company's working capital at June 30, 2014 is sufficient to support the Company's commitments and further expansion and growth.

(iv) 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 $542,000.

The Company's financial assets and liabilities as at June 30, 2014 are denominated in Canadian dollars, US dollars, and Mexican pesos as follows:

	Canadian dollar $	**US dollar $**	**Mexican peso $**	**Total $**
Financial assets				
Cash and cash equivalents	55,472	1,728,479	69,036	1,852,987
Trade receivables	-	618,867	-	618,867
Other receivables	3,100	-	39,748	42,848
	58,572	2,347,346	108,784	2,514,702
Financial liabilities				
Accounts payable and accrued liabilities	(904,400)	-	(2,050,282)	(2,954,682)
	(904,400)	-	(2,050,282)	(2,954,682)
Net financial assets (liabilities)	(845,828)	2,347,346	(1,941,498)	(439,980)

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

16. Commitment

The Company has in effect a lease agreement for the use of office premises in Vancouver, BC, Canada in the amount of $4,549 (CAD$4,838) per month until February 27, 2017. The amount of the total lease payments committed is $54,588 (CAD$58,056) for the fiscal years ending December 31, 2014, 2015, and 2016, and $9,098 (CAD$9,676) for the fiscal year ending December 31, 2017.

On October 15, 2013, the Company entered into a lease agreement for the use of office premises in the municipality of Monterrey, Nuevo León, Mexico in the amount of $2,294 (30,000 Mexican pesos) per month until April 15, 2014. On April 16, 2014, the Company renewed the Monterrey office lease agreement in the amount of $2,438 (32,000 Mexican pesos) per month until April 15, 2015. The amount of the total lease payments committed is $28,727 (377,000 Mexican pesos) for the fiscal year ending December 31, 2014.

17. Subsequent Event

On August 12, 2014, the Company granted 600,000 incentive stock options to an officer having an exercise price of CDN$0.94 each expiring August 12, 2019.