



**ANNUAL REPORT**

**DECEMBER 31, 2008**





Dear Fellow Shareholder,

This past year has been one of the more volatile of recent history. Your company achieved major milestones including the announcement of new gold and silver resources at its two principal properties. The year has also been one of extraordinary challenges revealed by major disruptions in world-wide financial markets. Nevertheless Esperanza emerges as a stronger company with outstanding properties, a positive working capital position, and a deep talent pool dedicated to generating shareholder value.

### **Cerro Jumil, Mexico**

We began the year with two rigs turning at Cerro Jumil and proceeded to complete a multi-year program of over 30,000 meters of drilling. An initial resource estimate was published on October 1 consisting of 642,000 gold-equivalent ounces in the measured and indicated category and 442,000 ounces in the inferred category. The attached table provides the details.

Esperanza has initiated a number of complementary studies aimed at moving the project forward to a development stage. A follow-up metallurgical study has been commissioned to expand upon the prior work. Early indications are that simple and cost effective gold recovery methods can be used. Other investigations that were begun include preliminary mine design and planning, hydrological studies, socio-economic studies as well as additional exploration for resource expansion.

Much of this work will be incorporated into a Preliminary Economic Assessment (“PEA”) that we anticipate by early in the third quarter of 2009. The PEA, a study preliminary to a full feasibility investigation, has two purposes: to demonstrate potential economic viability of the project under known conditions and to help our geologists and engineers more precisely define the required follow up study. We anticipate that further work, particularly drilling on new exploration targets contiguous to the known resource, will allow the project to grow in scale. Those further results will be incorporated into a future feasibility study.

### **San Luis, Peru**

The San Luis project achieved two significant milestones in 2008: the announcement of a measured and indicated resource containing 9 million ounces of silver and 348,000 ounces of gold (see attached table) plus the launch of a feasibility study for the initial development of a mine.

The estimated resource is on one defined ore body contained by the Ayelén vein and is characterized by exceptionally high grades of both silver and gold known by geologists as “bonanza” type mineralization. Numerous additional exploration targets exist throughout the 30,000 hectare claim block and will be the focus of future geologic investigation.

The feasibility study is expected to be completed by the end of the second quarter 2009. After a period of review a production decision will be evaluated by the joint-venture. The property is currently operated by Silver Standard Resources Inc. which will earn a 70% percent interest by producing the feasibility study. It has the option to earn an additional 10% interest by providing all funding to place a mine into commercial production.

## **Project Generation**

A key component in your Company's success to date has been its ability to successfully generate new exploration projects. Cerro Jumil and San Luis are the result of generative efforts. This endeavor continued at full pace in both Mexico and Peru during 2008. Our geologists evaluated 44 new exploration plays. Of these, three new properties were acquired. Additionally, another 14 properties previously acquired were abandoned because they did not meet Esperanza's criteria for continued work.

We intend to continue these efforts during 2009. Work in Peru will be centered on advancing our current property portfolio of seven properties and new project generation centered in the Cordillera Negra – the same region where Esperanza's geologists discovered San Luis. Mexican efforts are centered in the Cerro Jumil area where new areas of potential mineralization have already been identified and new claims staked.

## **2009**

We begin the current year in an enviable position. We have two advanced stage projects, an excellent exploration portfolio and sufficient working capital to meet our forecast needs. Esperanza's status combined with the current distressed economic situation in financial markets actually provides a new opportunity. The Company has been actively evaluating acquisition objectives. A wide variety of property and corporate targets have been reviewed. We will also evaluate the possibility of monetizing some of our assets if that capital can be re-applied to growing the company and creating greater shareholder value.

As always, I would like to close this letter by thanking our fellow shareholders. There is no doubt that these have been trying times. Nevertheless, we here at Esperanza are focusing all of our efforts on not just surviving but thriving through it all. Our combination of assets and talent together with a positive precious metals environment let me believe that our best days are in front of us. But without your continued support nothing would be possible.

Sincerely

Signed: *“William J. Pincus”*

William J Pincus  
President and CEO

| <b>Cerro Jumil Resource<br/>(as at October 1, 2008)</b> |                         |                       |                         |  |  |   |
|---|-------------------------|-----------------------|-------------------------|--|--|---|
| <b>Category</b>   | <b>Tonnes<br/>(000)</b> | <b>Gold<br/>(g/t)</b> | <b>Silver<br/>(g/t)</b> | <b>Contained<br/>Gold<br/>(oz 000)</b> | <b>Contained<br/>Silver<br/>(oz 000)</b> | <b>Gold<br/>Equivalent<br/>(oz 000)</b> |
| <b>Measured</b>   | 8,003                   | 0.90                  | 0.01                    | 232                                    | 4  | 232                                     |
| <b>Indicated</b>  | 15,225                  | 0.83                  | 1.0                     | 405                                    | 476                                      | 410                                     |
| <b>Measured<br/>and<br/>Indicated</b>                   | <b>23,227</b>           | <b>0.85</b>           | <b>0.6</b>              | <b>636</b>                             | <b>479</b>                               | <b>642</b>                              |
| <b>Inferred</b>   | <b>15,810</b>           | <b>0.74</b>           | <b>11.9</b>             | <b>378</b>                             | <b>6,068</b>                             | <b>442</b>                              |

Gold-equivalent values are based upon prices of US\$ 700/oz gold and US\$ 12.50/oz silver, and a silver to gold metal recovery ratio of 0.62. Totals may not sum due to rounding.

Dean Turner, P.Geo., a Qualified Person under National Instrument 43-101 and an independent consulting geologist, is responsible for the Cerro Jumil mineral resource estimate.

Further particulars are set out in Esperanza's news release dated October 1, 2008.

| <b>San Luis Resource<br/>(as at December 2, 2008 and on 100% basis*)</b> |                |                       |                         |  |  |  |
|--|----------------|-----------------------|-------------------------|--|--|--|
| <b>Category</b>  | <b>Tonnes</b>  | <b>Gold<br/>(g/t)</b> | <b>Silver<br/>(g/t)</b> | <b>Contained<br/>Gold<br/>(oz 000)</b> | <b>Contained<br/>Silver<br/>(oz 000)</b> | <b>Gold-<br/>Equivalent<br/>(oz 000)</b> |
| <b>Measured</b>  | 55,222         | 34.3                  | 757.6                   | 61                                     | 1,345                                    | 81                                       |
| <b>Indicated</b>   | 429,183        | 20.8                  | 555.0                   | 287                                    | 7,658                                    | 404                                      |
| <b>Measured<br/>and<br/>Indicated</b>                                    | <b>484,405</b> | <b>22.4</b>           | <b>578.1</b>            | <b>348</b>                             | <b>9,003</b>                             | <b>486</b>                               |
| <b>Inferred</b>  | <b>20,145</b>  | <b>5.6</b>            | <b>270.1</b>            | <b>3</b>                               | <b>174</b>                               | <b>6</b>                                 |

*\* Currently Esperanza has a 45% interest in the project that may be diluted to 20% if Silver Standard elects to exercise its option to advance all funds necessary to initiate commercial production.*

Gold-equivalent ounces assume a 65:1 gold to silver ratio based on US\$600/troy ounce gold and US\$9.25/troy ounce silver.

Contained metal may differ due to rounding. Metallurgical recoveries are assumed to be 100%. Prepared by independent National Instrument 43-101 Qualified Persons Michael Lechner of Resource Modeling, Inc. and Donald Earnest of Resource Evaluations, Inc.

Further particulars are set out in Esperanza's news release dated December 2, 2008

**CAUTIONARY NOTE to U.S. investors concerning disclosure of estimates of mineral resources and contained ounces of gold and silver:** *The terms “measured resource”, “indicated resource” and “inferred resource” used in this news release are Canadian geological and mining terms as defined in accordance with National Instrument 43-101, Standards of Disclosure for Mineral Projects of the Canadian Securities Administrators using the guidelines set out in the Canadian Institute of Mining, Metallurgy and Petroleum (the “CIM”) Standards on Mineral Resources and Mineral Reserves, adopted by the CIM Council as may be amended from time to time by the CIM. We advise U.S. investors that while such terms are recognized and permitted under Canadian regulations, the SEC does not recognize them. U.S. investors are cautioned not to assume that any part or all of the mineral deposits in the measured and indicated categories will ever be converted into reserves.*

*“Inferred resources” have a greater amount of uncertainty as to their existence, and greater uncertainty as to their economic and legal feasibility. It cannot be assumed that all or any part of an inferred mineral resource will ever be upgraded to a higher category. Under Canadian rules estimates of inferred mineral resources may not form the basis of feasibility or other economic studies. U.S. investors are cautioned not to assume that any part or all of an inferred resource exists, or is economically or legally mineable.*

*Disclosure of gold and silver resources expressed in ounces in the mineral resource categories in this news release are in compliance with Canadian National Instrument 43-101, but does not meet the requirements of Industry Guide 7, Description of Property by Issuers Engaged or to be Engaged in Significant Mining Operations, of the SEC, which will accept only the disclosure of tonnage and grade estimates for non-reserve mineralization.*

**ESPERANZA SILVER CORPORATION**  
**(An Exploration-Stage Company)**

**Management's Discussion and Analysis**

**Year Ended December 31, 2008**

This discussion and analysis of financial position and results of operations is prepared as at April 9, 2009 and should be read in conjunction with the audited consolidated financial statements of Esperanza Silver Corporation (the "Company" or "Esperanza") for the years ended December 31, 2008 and 2007 and the related notes thereto. Those consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles. These documents and other information relevant to the Company's activities are available for viewing on SEDAR at [www.sedar.com](http://www.sedar.com). All dollar amounts included therein and in the following management discussion and analysis ("MD&A") are in Canadian dollars except where noted.

This discussion contains forward-looking statements that involve risks and uncertainties. Such information, although considered to be reasonable by the Company's management at the time of preparation, may prove to be inaccurate and actual results may differ materially from those anticipated in the statements made.

**Description of Business**

Esperanza Silver Corp. is dedicated to the development of its two advanced-stage projects: Cerro Jumil and San Luis. It has entered into a joint-venture concerning its San Luis project in Peru and continues to hold 100% of the Cerro Jumil project in Mexico. This allows Esperanza to most effectively deploy its human and financial capital to further the project's development. Additionally the Company continues to identify and explore new precious metal projects in Mexico and Peru. Additional information is available at the Company's website at [www.esperanzasilver.com](http://www.esperanzasilver.com).

**Cerro Jumil, Mexico**

The Company completed an initial resource estimate on the Cerro Jumil property which includes 642,000 gold-equivalent ounces in the measured and indicated categories and a further 442,000 gold equivalent ounces in the inferred category. The Company filed an NI 43-101 Technical Report on Cerro Jumil dated September 30, 2008 and issued a news release on October 1, 2008. Both of these documents are available for viewing on SEDAR at [www.sedar.com](http://www.sedar.com). The deposit currently contains three contiguous zones – Southeast, Las Calabazas and West. The latter two may be extended by future drilling. Gold is found in all three areas while silver is concentrated in the West and Las Calabazas zones.

A Preliminary Economic Assessment is now being conducted for the property. Metallurgical testing of bulk-sample material is ongoing. Previous metallurgical testing has confirmed the amenability of Cerro Jumil gold mineralization to both conventional and heap-leach processing with recovery rates of up to 95% and 73% respectively. The new work will focus on the initial flow sheet development and optimization of various processing alternatives. Additionally preliminary mine design and scheduling is being investigated. Estimates of both operating and capital costs at a level of detail sufficient for the Preliminary Economic Assessment will also be conducted.

The Company has submitted a permit application for an infill drilling campaign designed to test a newly identified target immediately west of the Las Calabazas area, as well as the northern extension of the West Zone where high grade silver has been discovered.

Dean Turner, P. Geo., a Qualified Person as defined by National Instrument 43-101 and an independent consulting geologist, is responsible for the Cerro Jumil mineral resource estimate.

### **San Luis Project, Peru**

The property is currently held 55% by Silver Standard Resources Inc. (“Silver Standard”) and 45% by the Company. On March 26, 2007, Silver Standard elected to exercise its option to earn up to 70% of the San Luis project in Peru by funding all activities necessary to complete a feasibility study. Silver Standard also became the operator of the project. Upon acceptance of a feasibility study recommending commercial production Silver Standard will have the option to increase its share to 80% by funding all pre-production capital.

The Company has been informed by Silver Standard Resources Inc. that a feasibility study is now underway and results are expected before the end of the first half of 2009.

On December 2, 2008, the Company issued a news release disclosing that the revised resource estimate for San Luis was 485,400 gold equivalent ounces. The news release and an NI 43-101 Technical Report on San Luis dated January 9, 2009 are available for viewing on SEDAR at [www.sedar.com](http://www.sedar.com).

The mineral resource estimate was prepared by independent qualified persons Michael Lechner of Resource Modeling, Inc. and Donald Earnest of Resource Evaluation, Inc.

### **AT Properties, Mexico**

On August 20, 2007 the Company announced the acquisition of seven exploration properties in northern Mexico known collectively as the AT properties. Under the terms of the agreement Esperanza paid US\$30,000 and issued 20,000 common shares upon the signing of the definitive agreement for a four-year purchase option of the seven properties and paid a further US\$60,000 and issued an additional 65,000 shares as a result of starting drilling on six of the properties. Esperanza was committed to drill a minimum of 1,200 meters per property during the first 12 months.

In October, 2008, the Company terminated the option agreements with Exploraciones del Altiplano S.A. de C.V. and Compana Minera Terciario S.A. de C.V., on the seven AT Properties in Mexico. The Company wrote-off the accumulated capitalized costs for these properties in the fourth quarter of 2008 which amounted to \$1,814,649.

### **Flor de Loto Project, Peru**

During 2008 no physical work has been conducted on the property. In December 2008, the Company decided to abandon the property and has no further obligations under the option agreement.

### **Pucarana, Peru**

On March 5, 2007 the Company announced it had reached an agreement on the Pucarana, Peru mineral property with Canadian Shield Resources Inc. Pursuant to the agreement, Esperanza has an option to earn

a 51% interest by expending US\$650,000 over a two year period commencing upon receipt of drill permits, with a commitment to fund US\$200,000 in exploration expenditures in the first year. Esperanza also has the option to earn a subsequent 9% interest (for a total of 60%) by making additional exploration expenditures of US\$650,000 over a two year period. A cash payment of US\$30,000 was paid on signing of a definitive agreement and a second payment of US\$50,000 is due if Esperanza elects to exercise the right to earn the additional 9% interest. The expenditure commitments are contingent upon Esperanza receiving a drill permit. To date the Company has not received a drill permit and as a result the timing of exploration expenditures and cash payment commitments cannot be determined.

During 2007 and 2008 the Company initiated its exploration activities, identifying target areas for subsequent trenching and drilling and completed social baseline and hydrogeology studies. The Company is still negotiating an exploration agreement with the local community and has prepared an application for drilling permits.

### **Atocha Property, Bolivia**

On December 23, 2003, the Company acquired a 100% indirect interest in the Atocha Project concessions, comprising approximately 7,250 hectares located in West Central Bolivia. During the year ended December 31, 2005 the Company wrote-down the carrying value of the Atocha property to \$25,000. The Company determined that it will not conduct any further exploration on this property and wrote-off the balance of capitalized costs in the quarter ended September 30, 2008.

### **Exploration Expenditures**

In the year ended December 31, 2008, Esperanza capitalized the following expenditures on its exploration properties in Mexico and Peru:

#### **MEXICO**

|                         | AT                  |                     |                 |                  |                  | Total               |
|-------------------------|---------------------|---------------------|-----------------|------------------|------------------|---------------------|
|                         | Cerro Jumil         | Properties          | Fortuna         | Galindo          | Sabinal          |                     |
| Acquisition costs       | \$ -                | \$ 95,706           | \$ -            | \$ -             | \$ -             | \$ 95,706           |
| Assays                  | 242,694             | 131,817             | -               | 21,445           | 1,287            | 397,243             |
| Community programs      | 46,118              | -                   | -               | -                | -                | 46,118              |
| Drilling                | 1,103,367           | 566,449             | -               | -                | -                | 1,669,816           |
| Environmental           | 54,851              | -                   | -               | -                | -                | 54,851              |
| Field costs             | 167,094             | 61,582              | -               | 99               | 95               | 228,870             |
| Geological studies      | 608,048             | 245,754             | 5,854           | 17,450           | 24,373           | 901,479             |
| Geophysics              | -                   | 1,909               | -               | -                | -                | 1,909               |
| Office & administrative | 1,666               | 16,150              | -               | 94               | 3                | 17,913              |
| Property tax            | 24,759              | 15,397              | -               | -                | -                | 40,156              |
| Road and access costs   | 53,989              | 150,004             | -               | -                | -                | 203,993             |
| Travel                  | 46,094              | 27,338              | -               | 3,909            | 6,133            | 83,474              |
| Vehicles                | 55,258              | 23,954              | -               | -                | -                | 79,212              |
| <b>Total 2008 Costs</b> | <b>\$ 2,403,938</b> | <b>\$ 1,336,060</b> | <b>\$ 5,854</b> | <b>\$ 42,997</b> | <b>\$ 31,891</b> | <b>\$ 3,820,740</b> |

**PERU**

|                         | <b>Flor De Lotto</b> | <b>Pucarana</b> | <b>San Luis</b> | <b>Utcucocha</b> | <b>Other</b> | <b>Total</b> |
|-------------------------|----------------------|-----------------|-----------------|------------------|--------------|--------------|
| Assays                  | \$ -                 | \$ -            | \$ -            | \$ 11,262        | \$ 3,558     | \$ 14,820    |
| Community programs      | 7,692                | 271             | -               | 861              | 4            | 8,828        |
| Field costs             | 15,884               | 5,320           | 23,349          | 1,026            | 1,715        | 47,294       |
| Geological studies      | 45,374               | 50,443          | 25,825          | 132,928          | 50,738       | 305,308      |
| Office & administrative | 10,046               | 8,922           | 30              | 17,843           | 7,031        | 43,872       |
| Property tax            | -                    | -               | -               | 135              | -            | 135          |
| Travel                  | 4,768                | 3,227           | 10,116          | 6,938            | 3,425        | 28,474       |
| Vehicles                | 13,709               | 3,859           | -               | 11,721           | 3,308        | 32,597       |
| <b>Total 2008 Costs</b> | \$ 97,473            | \$ 72,042       | \$ 59,320       | \$ 182,714       | \$ 69,779    | \$ 481,328   |

In the year ended December 31, 2007, Esperanza capitalized the following expenditures on its exploration properties in Mexico and Peru:

**MEXICO**

|                         | <b>Cerro Julim</b> | <b>AT Properties</b> | <b>Total</b> |
|-------------------------|--------------------|----------------------|--------------|
| Acquisition costs       | \$ 32,800          | \$ 94,960            | \$ 127,760   |
| Assays                  | 213,085            | 44,626               | 257,711      |
| Communications          | 25,048             | -                    | 25,048       |
| Drilling                | 2,200,860          | 105,641              | 2,306,501    |
| Field costs             | 227,685            | 2,848                | 230,533      |
| Geological studies      | 688,987            | 48,856               | 737,843      |
| Geophysics              | 4,569              | 995                  | 5,564        |
| Office & administrative | 58,126             | 33,404               | 91,530       |
| Property tax            | 29,345             | 16,816               | 46,161       |
| Roads and access        | 161,683            | 10,888               | 172,571      |
| Travel                  | 98,772             | 7,281                | 106,053      |
| Vehicles                | 98,052             | 1,099                | 99,151       |
| <b>Total 2007 Costs</b> | \$ 3,839,012       | \$ 367,414           | \$ 4,206,426 |

**PERU**

|                         | <b>Flor de Loto</b> | <b>Pucarana</b> | <b>San Luis</b> | <b>Utcucocha</b> | <b>Other</b> | <b>Total</b> |
|-------------------------|---------------------|-----------------|-----------------|------------------|--------------|--------------|
| Acquisition costs       | \$ 5,616            | \$ 33,195       | \$ -            | \$ 4,714         | \$ -         | \$ 43,525    |
| Assays                  | 657                 | 308             | 60,953          | 792              | 8,850        | 71,560       |
| Communications          | 14                  | 4               | 6,419           | 2                | 1            | 6,440        |
| Drilling                | -                   | -               | 875,916         | -                | -            | 875,916      |
| Field costs             | 436                 | 19,135          | 91,987          | 918              | 2,348        | 114,824      |
| Geological studies      | 34,019              | 82,471          | 198,790         | 13,260           | 58,514       | 387,054      |
| Office & administrative | 12,814              | 617             | 33,972          | 2,669            | 14,094       | 64,166       |
| Property tax            | 13,038              | -               | -               | 113              | 196          | 13,347       |
| Site supervision        | -                   | -               | 47,808          | -                | -            | 47,808       |
| Travel                  | 2,136               | 11,231          | 37,290          | 1,896            | 7,726        | 60,279       |
| Vehicles                | 3,244               | 7,816           | 102,591         | 646              | 3,246        | 117,543      |
| <b>Total 2007 Costs</b> | 71,974              | 154,777         | 1,455,726       | 25,010           | 94,975       | 1,802,462    |
| <b>Recoveries</b>       | -                   | -               | (1,290,410)     | -                | -            | (1,290,410)  |
| <b>Net 2007 Costs</b>   | \$ 71,974           | \$ 154,777      | \$ 165,316      | \$ 25,010        | \$ 94,975    | \$ 512,052   |

**Results of Operations****Year Ended December 31, 2008**

The Company recorded a loss of \$5,129,245 for the year ended December 31, 2008 (2007 - \$2,839,379). The loss was much higher than in the prior year due to the write-off of capitalized mineral properties in the amount of \$2,236,319. There were a number of other offsetting variances. Higher expenses for consulting fees, directors' fees, investor relations and office and sundry were substantially offset by lower costs for stock-based compensation, foreign exchange and transfer agent and regulatory fees. At year-end the Company wrote off mineral property costs of \$1,814,649 in Mexico, \$396,670 in Peru and \$25,000 in Bolivia, whereas there were no write-offs in the prior year. Consulting fees were higher in 2008 mainly due to the higher US exchange rate in the last half of the year compared to 2007. Most of the consulting fees are denominated in US dollars. The Company began paying directors' fees in 2008 and therefore there were no comparable expenses in 2007. Investor relations expenses were higher in 2008 because the Company increased its level of investor relations activities. Office costs have increased over 2007 because the new Denver office has been operating for all of 2008 compared to operating for only one quarter in 2007. Stock-based compensation costs were lower in 2008 because a lower amount of options were granted during the year and they were granted at significantly lower prices than in 2007 which reduced the value per option. Foreign exchange was lower in 2008 due to the strengthening of the US dollar against the Canadian dollar during the year. The Company's operations are funded in US dollars. Transfer agent and regulatory fees were lower in 2008 because there was no private placement, as there was in 2007 and because TSX Venture exchanges annual fees were lower in 2008 due to the Company's lower stock price.

**Three Months Ended December 31, 2008**

The Company recorded a loss of \$2,844,589 for the three months ended December 31, 2008 (2007 - \$484,024). The increase in the loss was due to mineral property write-offs, higher exploration expense

and lower interest income partially offset by lower stock-based compensation. The Company wrote off capitalized mineral property expenditures for all of the properties it held in Mexico except for Cerro Jumil and also wrote off capitalized exploration costs on five properties in Peru. There were no mineral property write-offs in 2007. Exploration expense was higher in the quarter ended December 31, 2008 because the Company was conducting a higher level of mineral property examinations in 2008 than in 2007. Stock-based compensation was lower because the Company's stock price was much lower at December 31, 2008 than at the same date in the prior year. The lower stock price resulted in significantly lower accruals for stock-based compensation in 2008 than for 2007. Interest income was lower in the quarter ended December 31, 2008 compared to the prior year due to the lower amount of cash available to invest.

### **Liquidity and Capital Resources**

The Company started 2008 with working capital of \$15,037,240 and had working capital of \$9,351,557 at December 31, 2008. The decrease in working capital of \$5,685,683 was due mainly to the investment in mineral properties of approximately \$5,048,000 and the loss from operations, partially offset by cash received on the exercise of stock options. Most of the expenditures on mineral properties were incurred completing a drilling program and field work on the Cerro Jumil property in Mexico and field work done on the AT Properties in Mexico. Working capital includes a receivable from the Mexican government for value added tax in the amount of \$975,000. The Company is in the process of filing claims for this outstanding balance and expects that the full amount will be recoverable. Esperanza is dependent on raising funds through the issuance of shares and attracting joint venture partners in order to finance further property acquisitions and to explore and develop its mineral properties. Esperanza currently has sufficient working capital to fund its exploration and administrative expenditures for the next twelve months.

### **Off-Balance Sheet Arrangements**

There are no off-balance sheet arrangements or obligations that are not disclosed in the financial statements.

## Quarterly Information

|                                    | 2008        | 2008       | 2008       | 2008        |
|------------------------------------|-------------|------------|------------|-------------|
| Quarter Ended                      | Dec. 31     | Sept. 30   | Jun. 30    | Mar. 31     |
| Operating expenditures             | \$ 703,980  | \$ 534,226 | \$ 481,479 | \$1,545,925 |
| Loss for the period                | (2,844,589) | (480,046)  | (396,045)  | (1,408,565) |
| Loss per share (basic and diluted) | (0.06)      | (0.01)     | (0.01)     | (0.03)      |

|                                    | 2007       | 2007       | 2007        | 2007       |
|------------------------------------|------------|------------|-------------|------------|
| Quarter Ended                      | Dec. 31    | Sept. 30   | Jun. 30     | Mar. 31    |
| Operating expenditures             | \$ 659,475 | \$ 760,409 | \$1,303,518 | \$ 768,421 |
| Loss for the period                | (484,024)  | (573,778)  | (1,102,944) | (678,633)  |
| Loss per share (basic and diluted) | (0.01)     | (0.01)     | (0.02)      | (0.02)     |

### 2008

For the quarter ended December 31, 2008, operating expenditures were higher than in the prior quarter due to higher exploration expenses as a result of allocating more resources to finding new properties as opposed to working on projects already owned or under option agreements. The loss for the quarter ended December 31, 2008 was much higher than in the prior quarter because Esperanza wrote off a significant amount of capitalized mineral property costs in Mexico and Peru whereas in the prior quarter there was only a minor write-off pertaining to the Atocha property.

For the quarter ended September 30, 2008, operating expenditures were higher than in the prior quarter due to: an unfavourable foreign exchange variance and higher exploration expenses partially offset by lower investor relations and lower stock-based compensation costs. The unfavourable exchange variance was mainly due to the weakening of the Mexican peso against the Canadian dollar in the quarter, whereas the peso strengthened against the Canadian dollar in the prior quarter. Exploration expenses were higher than in the prior quarter due to an increase in regional exploration in Peru. Investor relations costs were lower in the current quarter due to attending fewer trade shows. Lower stock-based compensation costs in the current quarter were the result of the Company's lower share price which reduced the values generated by the Black-Scholes option pricing model.

For the quarter ended June 30, 2008, operating expenditures were significantly lower than in the prior quarter due to: lower stock-based compensation, consulting and investor relations costs and a favourable foreign exchange variance. Stock-based compensation was lower because there were no grants in the current quarter whereas there were 1,100,500 options granted in the previous quarter. Consulting costs were lower because bonuses were awarded in the prior quarter and none in the current quarter. Investor relations costs were lower mainly due to the seasonality of trade shows. The favourable foreign exchange variance was due to the strengthening of the Mexican peso against the Canadian dollar in the current quarter.

In the first quarter of 2008 operating expenditures increased significantly over the prior quarter due to higher costs for stock-based compensation, consulting fees and investor relations. Stock-based

compensation was higher due to the granting of over one million stock options that were fully vested compared to the prior quarter when no options were granted and there were only accruals for previously granted stock options. Consulting fees were higher than in the prior quarter due to additional consultants being hired and due to bonus payments. Investor relations costs were higher due to higher activity at trade shows and due to increased use of other media for investor relations compared to the prior quarter.

## **2007**

For the quarter ended December 31, 2007, operating costs were lower than for the prior quarter due to lower stock-based compensation expense. The loss for the period was lower than the prior quarter for the same reason.

Operating expenditures were lower in the third quarter than in the second quarter of 2007 due to lower stock-based compensation expense, property examination costs and a lower foreign exchange loss. Property examination costs were lower as a result of lower activity as several new properties were acquired. The foreign exchange loss was higher in the second quarter because the US dollar weakened by 10 cents against the Canadian dollar compared to only 5 cents in the third quarter.

In the second quarter of 2007 both operating expenses and the loss were higher than in the prior quarter due to increased stock-based compensation.

### **Selected Annual Financial Information**

|                                     | <b>December 31,<br/>2008</b> | <b>December 31,<br/>2007</b> | <b>December 31,<br/>2006</b> |
|-------------------------------------|------------------------------|------------------------------|------------------------------|
| Operating Expenses                  | \$ 3,265,610                 | \$ 3,491,824                 | \$ 1,727,889                 |
| Net Loss                            | (5,129,245)                  | (2,839,379)                  | (1,572,623)                  |
| Loss per Share – Basis and Diluted  | (0.11)                       | (0.06)                       | (0.04)                       |
| Capitalized Minerals Property Costs | 5,048,383                    | 3,859,162                    | 2,617,592                    |
| Total Assets                        | 21,250,623                   | 25,817,957                   | 10,209,823                   |

### **Cash Flows (Used In):**

|                                 |                |               |                |
|---------------------------------|----------------|---------------|----------------|
| Operating                       | \$ (2,408,992) | \$ (720,945)  | \$ (1,735,607) |
| Investing                       | (5,058,177)    | (3,974,597)   | (2,643,991)    |
| Financing                       | 325,800        | 16,174,455    | 4,990,872      |
| Net Increase (Decrease) in Cash | \$ (7,141,369) | \$ 11,478,913 | \$ 611,274     |

In 2008 Esperanza had lower operating expenses due to lower stock-based compensation and a favourable variance on foreign exchange. Stock-based compensation was lower than in 2007 mainly because the value per option was significantly lower because the weighted average exercise price declined from \$3.27 in 2007 to \$1.34 in 2008. The foreign exchange variance was favourable because the Company invested about \$3.9 million in mineral properties in 2007 and during 2007 the US dollar weakened significantly against the Canadian dollar and Esperanza incurred a significant loss on translation of the accounts of its Mexican subsidiary as a result. These favourable variances were partially offset by higher office and rent costs as a result of moving the Denver personnel into better office space. The Company also began paying directors' fees in 2008 which partially offset the lower costs for stock-base compensation and foreign exchange. The net loss in 2008 was higher than for 2007 as a result of writing off a number of properties in Mexico and Peru and due to lower interest income because there was less cash to invest than in the prior year.

Cash used in operations in 2008 was well above 2007 because the IVA receivable in Mexico increased significantly and the Company used working capital to reduce the accounts payable balance during the year whereas in 2007 Esperanza collected on amounts due from its JV partner and reduced the cash outflow as a result of increasing accounts payable during the year. In addition the Company generated less interest on invested cash in 2008 than in 2007. Investing activity was higher in 2008 because in 2007 the Company received a significant cash contribution for development activities from its joint venture partner in Peru. In 2008, Esperanza was incurring the bulk of its development costs in Mexico and there was no contribution during the year from a joint venture partner. Cash from financing activities was much lower in 2008 because the Company did not do a private placement compared to 2007 when the Company raised over \$16 million from a private placement and the exercise of warrants.

In 2007, Esperanza incurred significantly higher operating expenses than in 2006 due to higher costs for: stock-based compensation, exploration expenses, consulting fees, investor relations and a higher foreign exchange loss. The net loss for 2007 was higher than the loss for 2006 for the same reasons except that the higher operating expenses were partially offset by increased interest income due to interest earned on much higher balances of cash and cash equivalents on hand as a result of the February, 2007 private placement. Capitalized mineral property costs were higher than in 2006 due to a significant drilling program on the Cerro Jumil property. Total assets were much higher in 2007 due to the February private placement plus cash proceeds from the exercise of a significant amount of warrants and stock options during the year.

## **New Accounting Policies**

### **Capital Disclosures**

The Company has adopted CICA Handbook Section 1535, Capital Disclosures, which establishes standards for disclosing information about the Company's capital and how it is managed. Under this standard the Company must disclose the following, based on the information provided internally to the Company's key management personnel:

- (a) qualitative information about its objectives, policies and processes for managing capital;
- (b) summary quantitative data about what it manages as capital;
- (c) whether during the period it complied with any externally imposed capital requirement to which it is subject;
- (d) when the company has not complied with such externally imposed capital requirements, the consequences of such non-compliance.

### **Financial Instruments Disclosures**

CICA Handbook Section 3862, Financial Instruments – Disclosures, requires entities to provide disclosure of quantitative and qualitative information in their financial statements that enable users to evaluate (a) the significance of financial instruments for the company's financial position and performance; and (b) the nature and extent of risks arising from financial instruments to which the company is exposed during the period and at the balance sheet date, and management's objectives, policies and procedures for managing such risks.

The Company will be required to disclose the measurement basis or bases used, and the criteria used to determine classification for different types of instruments. The Section requires specific disclosures to be made, including the criteria for:

- (a) designating financial assets and liabilities as held for trading;
- (b) designating financial assets as available-for-sale; and
- (c) determining when impairment is recorded against the related financial asset or when an allowance account is used.

### **General Standards on Financial Statements**

CICA Handbook Section 1400, General Standards on Financial Statements Presentation, has been amended to include requirements to assess and disclose a company's ability to continue as a going concern.

### **Recent Accounting Pronouncements**

#### **Convergence with International Financial Reporting Standards**

A Decision of the CICA Accounting Standards Board (the "AcSB") will require the Company to report under International Financial Reporting Standards in fiscal 2011. The transition date of January 1, 2011 will require the restatement for comparative purposes of amounts reported by the Company for the year ended December 31, 2010. The Company has completed a scoping study which identifies the mandatory and optional exemptions from retrospective application of IFRS accounting policies and provides a comparison of the Company's current accounting policies with those prescribed under IFRS. The Company is reviewing and assessing this information but has not determined the impact on the consolidated financial statements at this time.

### **Risks and Uncertainties**

The business of mineral deposit exploration and extraction involves a high degree of risk. Few properties that are explored ultimately become producing mines. At present, none of the Company's properties has a known commercial ore deposit. The main operating risks include: securing adequate funding to maintain and advance exploration properties; ensuring ownership of and access to mineral properties by confirmation that claims and leases are in good standing and obtaining permits for drilling and other exploration activities.

The market prices for silver, gold and other metals can be volatile and there is no assurance that a profitable market will exist for a production decision to be made or for the ultimate sale of the metals even if commercial quantities of precious and other metals are discovered.

Esperanza is currently earning an interest in certain of its properties through option agreements and acquisition of title to the properties is only completed when the option conditions have been met. These conditions generally include making property payments, incurring exploration expenditures on the properties and can include the satisfactory completion of pre-feasibility studies. If the Company does not satisfactorily complete these option conditions in the time frame laid out in the option agreements, the Company's title to the related property will not vest and the Company will have to write-off the previously capitalized costs related to that property.

The Company is operating in countries that currently have varied political environments. Changing political situations may affect the manner in which the Company operates. The Company's equity financings are sourced in Canadian dollars but for the most part it incurs its expenditures in local currencies or in US dollars. At this time there are no currency hedges in place. Some work is carried out

through independent consultants and the Company requires that all consultants carry their own insurance to cover any potential liabilities as a result of their work on a project.

### **Outstanding Share Data**

As at April 9, 2009 there were 47,521,821 common shares issued and outstanding. There were also 4,183,500 stock options outstanding with exercise prices ranging between \$0.40 and \$3.70 per share. Of the options outstanding 3,789,332 have vested.

Consolidated Financial Statements

**ESPERANZA SILVER CORPORATION**

For the Years Ended December 31, 2008, 2007 and 2006

**DE VISSER GRAY LLP**  
**CHARTERED ACCOUNTANTS**

401 - 905 West Pender Street  
Vancouver, BC Canada  
V6C 1L6

Tel: (604) 687-5447  
Fax: (604) 687-6737

**AUDITORS' REPORT**

To the Shareholders of Esperanza Silver Corporation,

We have audited the consolidated balance sheets of Esperanza Silver Corporation as at December 31, 2008 and 2007 and the consolidated statements of operations, comprehensive loss and deficit and cash flows for each of the years in the three year period then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2008 and 2007 and the results of its operations and cash flows for each of the years in the three year period ended then ended in accordance with Canadian generally accepted accounting principles.

"De Visser Gray LLP"

**CHARTERED ACCOUNTANTS**

Vancouver, British Columbia  
April 1, 2009

# ESPERANZA SILVER CORPORATION

Consolidated Balance Sheets

(Expressed in Canadian Dollars)

As at December 31, 2008 and 2007

|   | 2008          | 2007          |
|---|---------------|---------------|
| <b>ASSETS</b>                               |               |               |
| <b>Current assets</b>                       |               |               |
| Cash and cash equivalents                   | \$ 8,429,832  | \$ 15,571,201 |
| Receivables                                 | 1,089,455     | 517,485       |
| Prepaid expenses                            | 21,578        | 24,316        |
|   | 9,540,865     | 16,113,002    |
| Equipment (Note 4)                          | 77,415        | 138,361       |
| Mineral properties (Note 5)                 | 11,632,343    | 9,566,594     |
|   | \$ 21,250,623 | \$ 25,817,957 |
| <b>LIABILITIES AND SHAREHOLDERS' EQUITY</b> |               |               |
| <b>Current liabilities</b>                  |               |               |
| Accounts payable and accrued liabilities    | \$ 189,308    | \$ 1,075,762  |
| <b>Shareholders Equity</b>                  |               |               |
| Share capital (Note 6)                      | 34,611,921    | 34,012,973    |
| Contributed surplus (Note 6)                | 5,752,140     | 4,902,723     |
| Deficit                                     | (19,302,746)  | (14,173,501)  |
|   | 21,061,315    | 24,742,195    |
|   | \$ 21,250,623 | \$ 25,817,957 |

**Nature of operations** (Note 1)

**Commitments and contingencies** (Note 8)

See accompanying notes to the consolidated financial statements.

Approved on behalf of the Board

"George Elliott" Director

"William J. Pincus" Director

**ESPERANZA SILVER CORPORATION**

Consolidated Statements of Operations, Comprehensive Loss and Deficit

*(Expressed in Canadian Dollars)*

Years ended December 31, 2008, 2007 and 2006

|   | 2008            | 2007            | 2006            |
|---|-----------------|-----------------|-----------------|
| <b>Operating expenses</b>                         |                 |                 |                 |
| Accounting and legal                              | \$ 119,639      | \$ 126,898      | \$ 68,787       |
| Amortization                                      | 30,489          | 12,325          | 8,142           |
| Consulting fees                                   | 684,285         | 623,116         | 207,020         |
| Directors' fees                                   | 78,526          | -               | -               |
| Foreign exchange                                  | 19,192          | 203,053         | (15,317)        |
| Investor relations and shareholder communications | 359,921         | 312,755         | 152,237         |
| Office and sundry                                 | 219,962         | 136,566         | 80,290          |
| Exploration expenses                              | 481,773         | 490,023         | 307,822         |
| Rent  | 102,555         | 75,927          | 50,706          |
| Stock-based compensation (Note 6 (e))             | 1,066,015       | 1,336,658       | 750,524         |
| Transfer agent and regulatory fees                | 86,735          | 138,008         | 93,020          |
| Travel  | 16,518          | 36,494          | 24,658          |
| Loss before other items                           | (3,265,610)     | (3,491,823)     | (1,727,889)     |
| <b>Other items</b>                                |                 |                 |                 |
| Interest income                                   | 372,684         | 646,281         | 155,266         |
| Gain on the disposal of fixed assets              | -               | 6,163           | -               |
| Write-off of mineral properties (Note 5)          | (2,236,319)     | -               | -               |
| Net loss and comprehensive loss for the year      | (5,129,245)     | (2,839,379)     | (1,572,623)     |
| <b>Deficit, beginning of year</b>                 | (14,173,501)    | (11,334,122)    | (9,761,499)     |
| <b>Deficit, end of year</b>                       | \$ (19,302,746) | \$ (14,173,501) | \$ (11,334,122) |
| Basic and diluted loss per share                  | \$ (0.11)       | \$ (0.06)       | \$ (0.04)       |
| Weighted average number of shares outstanding     | 47,299,635      | 44,550,285      | 36,715,551      |

See accompanying notes to the consolidated financial statements.

# ESPERANZA SILVER CORPORATION

Consolidated Statements of Cash Flows

(Expressed in Canadian Dollars)

Years ended December 31, 2008, 2007 and 2006

|   | 2008           | 2007           | 2006           |
|---|----------------|----------------|----------------|
| <b>Cash provided by (used in):</b>                  |                |                |                |
| <b>Operations:</b>                                  |                |                |                |
| Net loss for the year                               | \$ (5,129,245) | \$ (2,839,379) | \$ (1,572,623) |
| Items not affecting cash:                           |                |                |                |
| Amortization  | 37,822         | 20,634         | 8,142          |
| Gain on disposal of equipment                       | -              | (6,163)        | -              |
| Stock-based compensation                            | 1,066,015      | 1,336,658      | 750,524        |
| Write-off of mineral property costs                 | 2,236,319      | -              | -              |
| Changes in non-cash working capital items:          |                |                |                |
| Receivables   | (571,970)      | 69,995         | (524,458)      |
| Due from joint venture partner                      | -              | 597,840        | (457,474)      |
| Prepaid expenses                                    | 2,738          | 13,450         | (652)          |
| Accounts payable and accrued liabilities            | (50,671)       | 86,020         | 60,934         |
|   | (2,408,992)    | (720,945)      | (1,735,607)    |
| <b>Investments:</b>                                 |                |                |                |
| Mineral property costs                              | (5,048,383)    | (3,859,162)    | (2,617,952)    |
| Proceeds from the disposal of equipment             | -              | 23,540         | -              |
| Purchase of equipment                               | (9,794)        | (138,975)      | (26,039)       |
|   | (5,058,177)    | (3,974,597)    | (2,643,991)    |
| <b>Financings:</b>                                  |                |                |                |
| Shares issued for cash                              | 325,800        | 17,102,643     | 5,068,992      |
| Shares issue costs                                  | -              | (928,188)      | (78,120)       |
|   | 325,800        | 16,174,455     | 4,990,872      |
| Increase (decrease) in cash and cash equivalents    | (7,141,369)    | 11,478,913     | 611,274        |
| <b>Cash and cash equivalents, beginning of year</b> | 15,571,201     | 4,092,288      | 3,481,014      |
| <b>Cash and cash equivalents, end of year</b>       | \$ 8,429,832   | \$ 15,571,201  | \$ 4,092,288   |
| Supplementary information:                          |                |                |                |
| Cash received for interest                          | \$ 240,163     | \$ 753,885     | \$ 57,025      |
| Shares issued for mineral properties                | 56,550         | 85,000         | 1,067,812      |
| Securities issued as part of share issue costs      | -              | 346,211        | 49,715         |

During the year ended December 31, 2008, there was \$29,077 (2007 -\$864,860; 2006 -\$99,480) in accounts payable that related to mineral property costs.

Included in cash and cash equivalents at December 31, 2008 is \$8,250,000 (2007 - nil; 2006 - \$3,800,000) in guaranteed income certificates and \$179,832 (2007 - \$15,571,201; 2006 - \$292,288) held in bank accounts.

See accompanying notes to the consolidated financial statements.

# ESPERANZA SILVER CORPORATION

Notes to the Consolidated Financial Statements

(Expressed in Canadian Dollars)

Years ended December 31, 2008, 2007 and 2006

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## 1. Nature of operations

Esperanza Silver Corporation (the “Company”) was formed effective December 1, 1990 by way of amalgamation pursuant to the Company Act (British Columbia). The Company’s principal business activities include the acquisition, exploration and development of resource properties.

The Company is in the process of exploring its mineral properties and has not yet determined whether they contain resources that are economically recoverable. The recoverability of amounts shown for mineral properties is dependent upon the discovery of economically recoverable reserves, the ability of the Company to obtain the necessary financing to complete their exploration and development, confirmation of the Company’s interest in the underlying claims and leases, and from future profitable production or proceeds from the disposition of the mineral properties.

## 2. Significant accounting policies

### Basis of presentation and consolidation

These consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles (“GAAP”). They include the accounts of the Company and its wholly-owned subsidiaries. All significant intercompany transactions and balances have been eliminated.

### Cash and cash equivalents

Cash and cash equivalents are comprised of cash and highly liquid investments having original terms to maturity of 90 days or less when acquired.

### Equipment

Equipment is recorded at cost less accumulated amortization. Amortization is provided on a straight-line basis over three to five years, which represents the estimated useful lives of the assets.

### Mineral properties

Exploration and development expenditures incurred prior to the acquisition of a property have occurred are charged to operations. Expenditures incurred subsequent to such an event are capitalized and will be amortized on the unit-of-production method when, and if, estimated proven reserves can be determined by independent consulting engineers and production has begun. When there is little prospect of further work on a property being carried out by the Company, the deferred costs associated with that property are charged to operations during the year such determination is made. The amounts shown for mineral properties represent acquisition costs and exploration costs incurred to date after the property was acquired or optioned, less recoveries and write-offs, and are not intended to reflect present or future values.

### Asset retirement obligations

The Company recognizes a liability for an asset retirement obligation when it is determinable and calculates the liability based upon discounted future payments to be made. A corresponding amount is added to the carrying amount of the related long-lived asset, and this amount is subsequently allocated to expense over its expected life. Adjustments will also be made in subsequent periods to changes in asset retirement obligations due to changes in estimates. As at December 31, 2008, the present value of the Company’s asset retirement obligations is nominal.

### Retirement of long-lived assets

Long-lived assets are assessed for impairment when events and circumstances warrant, when the carrying amounts of the assets exceeds its estimated undiscounted net cash flow from use or its fair value, at which time the impairment is charged to earnings.

# ESPERANZA SILVER CORPORATION

Notes to the Consolidated Financial Statements

(Expressed in Canadian Dollars)

Years ended December 31, 2008, 2007 and 2006

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## 2. Significant accounting policies (continued)

### Foreign Currency Translation

The Company translates its foreign operations on the following basis: monetary assets and liabilities are translated at the rate of exchange in effect as at the balance sheet date and non-monetary assets and liabilities are translated at their applicable historical rates. Revenues and expenses are translated at the average rates prevailing for the year, except for amortization that is translated at the historical rates associated with the assets being amortized.

Foreign exchange gains and losses from the translation of foreign operations are recognized in the current period.

### Stock-based compensation

The Company has a stock option plan which is described in note 6(c) and accounts for all grants of options to employees, non-employees and directors in accordance with the fair value method for accounting for stock-based compensation as defined by accounting principles generally accepted in Canada. Stock-based compensation expense is calculated using the Black-Scholes option pricing model ("Black-Scholes") (see Note 6 (e)).

### Income taxes

The Company uses the asset and liability method of accounting for income taxes. Under this method of tax allocation, future income tax assets and liabilities are determined based on differences between the financial statement carrying values of existing assets and liabilities and their respective income tax bases (temporary differences), and losses carried forward. Future income tax assets and liabilities are measured using the tax rates expected to be in effect when the temporary differences are likely to reverse. The effect on future income tax assets and liabilities of a change in tax rates is included in operations in the period in which the change is substantively enacted. The amount of future income tax assets recognized is limited to the amount of the benefit that is more likely than not to be realized.

### Loss per share

Basic loss per share has been calculated using the weighted average number of common shares issued and outstanding during the year. Diluted earnings per share is calculated using the treasury stock method. However, in the Company's case, diluted loss per share is the same as basic loss per share, as the effect of outstanding options and warrants on loss per share would be anti-dilutive.

### Estimates

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Significant areas requiring the use of management estimates include the determination of impairment of mineral properties and the variables used in the calculation of stock-based acquisition costs and compensation expense. Actual results could differ from these estimates.

### Comparative figures

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

### New Accounting Policies

The Company has adopted the following new accounting policies effective January 1, 2008.

### Capital Disclosures

The Company has adopted CICA Handbook Section 1535, Capital Disclosures, which establishes standards for disclosing information about the Company's capital and how it is managed. Under this standard the Company must disclose the following, based on the information provided internally to the Company's key management personnel:

# ESPERANZA SILVER CORPORATION

Notes to the Consolidated Financial Statements

(Expressed in Canadian Dollars)

Years ended December 31, 2008, 2007 and 2006

## 2. Significant accounting policies (continued)

### Capital Disclosures (continued)

- (a) qualitative information about its objectives, policies and processes for managing capital;
- (b) summary quantitative data about what it manages as capital;
- (c) whether during the period it complied with any externally imposed capital requirement to which it is subject;
- (d) when the company has not complied with such externally imposed capital requirements, the consequences of such non-compliance.

### New Accounting Policies

#### Financial Instruments Disclosures

The Company has adopted CICA Handbook Section 3862, Financial Instruments – Disclosures, which requires entities to provide disclosure of quantitative and qualitative information in their financial statements that enable users to evaluate (a) the significance of financial instruments for the company's financial position and performance; and (b) the nature and extent of risks arising from financial instruments to which the company is exposed during the period and at the balance sheet date, and management's objectives, policies and procedures for managing such risks. The Company is required to disclose the measurement basis or bases used, and the criteria used to determine classification for different types of instruments.

#### General Standards on Financial Statements

CICA Handbook Section 1400, General Standards on Financial Statements Presentation, has been amended to include requirements to assess and disclose a company's ability to continue as a going concern. Refer to Note 10 "Management of capital".

### Recent Accounting Pronouncements

#### Convergence with International Financial Reporting Standards

A Decision of the CICA Accounting Standards Board (the "AcSB") will require the Company to report under International Financial Reporting Standards in fiscal 2011. The transition date of January 1, 2011 will require the restatement for comparative purposes of amounts reported by the Company for the year ended December 31, 2010. The Company has completed a scoping study which identifies the mandatory and optional exemptions from retrospective application of IFRS accounting policies and provides a comparison of the Company's current accounting policies with those prescribed under IFRS. The Company is reviewing and assessing this information but has not determined the impact on the consolidated financial statements at this time.

## 3. Financial instruments

The Company's financial instruments are comprised of cash and cash equivalents, receivables and accounts payable. Unless otherwise noted, it is management's opinion that the Company is not exposed to significant interest, currency or credit risks arising from financial instruments. Receivables had been designated as "Loans and receivables" and have been measured at cost. Accounts payable have been designated as "Other" and have been measured at cost. The fair value of cash and cash equivalents approximates their carrying value due to their short-term maturity or capacity of prompt liquidation.

## 4. Equipment

|  | 2008       |                          | 2007           | 2006           |
|--|------------|--------------------------|----------------|----------------|
|  | Cost       | Accumulated Amortization | Net Book Value | Net Book Value |
|  | \$ 188,644 | \$ 111,229               | \$ 77,415      | \$ 46,333      |

# ESPERANZA SILVER CORPORATION

Notes to the Consolidated Financial Statements

(Expressed in Canadian Dollars)

Years ended December 31, 2008, 2007 and 2006

## 5. Mineral properties

The continuity of expenditures on mineral properties is as follows:

|   | Mexico       | Peru         | Bolivia   | Total         |
|---|--------------|--------------|-----------|---------------|
| Balance, December 31, 2006                | \$ 4,028,857 | \$ 794,259   | \$ 25,000 | \$ 4,848,116  |
| Acquisition costs and option payments     | 127,760      | 43,525       | -         | 171,285       |
| <b>Exploration and Development:</b>       |              |              |           |               |
| Assays                                    | 257,711      | 71,560       | -         | 329,271       |
| Communications                            | 25,048       | 6,440        | -         | 31,488        |
| Drilling                                  | 2,306,501    | 875,916      | -         | 3,182,417     |
| Field costs                               | 230,533      | 114,824      | -         | 345,357       |
| Geological studies                        | 737,843      | 387,054      | -         | 1,124,897     |
| Geophysics                                | 5,564        | -            | -         | 5,564         |
| Office and administrative                 | 91,530       | 64,166       | -         | 155,696       |
| Property tax                              | 46,161       | 13,347       | -         | 59,508        |
| Road and access costs                     | 172,571      | -            | -         | 172,571       |
| Site supervision                          | -            | 47,808       | -         | 47,808        |
| Travel                                    | 106,053      | 60,279       | -         | 166,332       |
| Vehicles                                  | 99,151       | 117,543      | -         | 216,694       |
|   | 8,235,283    | 2,596,721    | 25,000    | 10,857,004    |
| Less: Recovery from joint venture partner | -            | (1,290,410)  | -         | (1,290,410)   |
| Balance, December 31, 2007                | \$ 8,235,283 | \$ 1,306,311 | \$ 25,000 | \$ 9,566,594  |
| Acquisition costs and option payments     | 95,706       | -            | -         | 95,706        |
| <b>Exploration and Development:</b>       |              |              |           |               |
| Assays                                    | 397,243      | 14,820       | -         | 412,063       |
| Community programs                        | 46,118       | 8,828        | -         | 54,946        |
| Drilling                                  | 1,669,816    | -            | -         | 1,669,816     |
| Environmental                             | 54,851       | -            | -         | 54,851        |
| Field costs                               | 228,870      | 47,294       | -         | 276,164       |
| Geological studies                        | 901,479      | 305,308      | -         | 1,206,787     |
| Geophysics                                | 1,909        | -            | -         | 1,909         |
| Office and administrative                 | 17,913       | 43,872       | -         | 61,785        |
| Property tax                              | 40,156       | 135          | -         | 40,291        |
| Road and access costs                     | 203,993      | -            | -         | 203,993       |
| Travel                                    | 83,474       | 28,474       | -         | 111,948       |
| Vehicles                                  | 79,212       | 32,597       | -         | 111,809       |
|   | 12,056,023   | 1,787,639    | 25,000    | 13,868,662    |
| Less: mineral property write-offs         | (1,814,649)  | (396,670)    | (25,000)  | (2,236,319)   |
| Balance, December 31, 2008                | \$10,241,374 | \$ 1,390,969 | \$ -      | \$ 11,632,343 |

## ESPERANZA SILVER CORPORATION

Notes to the Consolidated Financial Statements

(Expressed in Canadian Dollars)

Years ended December 31, 2008, 2007 and 2006

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### 5. Mineral properties (continued)

#### (a) Cerro Jumil (formerly La Esperanza), Mexico

The Company entered into an option agreement with Recursos Cruz del Sur, S.A. de C.V. ("Recursos") dated May 7, 2003 whereby it obtained the option to acquire a 100% interest, subject to a 3% net smelter royalty, in the Esperanza silver/gold project in Morelos State, Mexico. The exercise price of the option was US\$2,000,000 plus value-added tax payable in Mexico, and the issuance of 170,000 common shares of the Company. From May, 2003 to October 2006, the Company made cash option payments of US\$80,000 and issued 170,000 common shares to Recursos in accordance with the option agreement.

In October 2006, the Company renegotiated the option agreement and earned its option by paying US\$417,375 plus VAT and issuing 500,000 common shares plus VAT in conjunction with the early exercise of the Company's option to purchase a 100% interest in the property. The property is subject to a 3 percent net smelter return royalty on any mineral production.

#### (b) AT Properties, Mexico

In September 2007, the Company agreed to acquire a four-year option on seven gold and silver exploration properties in Mexico's Durango and Chihuahua states from Exploraciones del Altiplano S.A. de C.V. and Compana Minera Terciario S.A. de C.V., two privately-held companies. Under the terms of the agreement Esperanza paid US\$30,000 and issued 20,000 common shares upon signing the definitive agreement for the four-year purchase option of the seven properties. In 2008, the Company paid an additional \$39,156 and issued 45,000 more shares valued at \$56,550. These costs were capitalized as acquisition costs.

In October 2008, the Company terminated the option agreements with Exploraciones del Altiplano S.A. de C.V. and Compana Minera Terciario S.A. de C.V., on the seven AT Properties in Mexico. The Company wrote-off the accumulated capitalized costs for these properties in the fourth quarter of 2008 which amounted to \$1,814,649.

#### (c) San Luis, Peru

During the year ended December 31, 2005, the Company announced the acquisition of the San Luis project via claim-staking. The project was subject to the exploration agreement, described below in Note 5 (d), with Silver Standard Resources Inc. ("Silver Standard"), a company that had a director in common until February, 2008. Silver Standard elected to form a separate 50%-50% joint-venture for the San Luis project. Under the terms of the agreement, Silver Standard has increased its ownership to 55% by funding the first US\$500,000 of exploration expenditures subsequent to the acquisition of the property. Silver Standard has subsequently elected to increase its ownership to 70 percent by funding all activities required to complete a feasibility study and it may further increase its ownership to 80 percent by funding all development activities necessary to place the property into production. Silver Standard announced in November, 2008 that it had commenced a feasibility study on the San Luis property.

#### (d) Silver Standard Exploration Agreement

In the first quarter of 2005, the Company entered into a prospecting agreement with Silver Standard to explore for bulk mineable silver deposits in central Peru. Under the terms of the agreement, Silver Standard would contribute US\$300,000 and the Company would contribute US\$200,000 during the first two years of the program. In March of 2007, this agreement was allowed to expire.

## ESPERANZA SILVER CORPORATION

Notes to the Consolidated Financial Statements

(Expressed in Canadian Dollars)

Years ended December 31, 2008, 2007 and 2006

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### 5. Mineral properties (continued)

#### (e) Flor de Loto, Peru

The Flor de Loto project is located in Lima Department, Peru approximately 150 kilometers northeast of Lima. The property consists of two concessions totaling 1000 hectares. On December 15, 2003, the Company, through its Peruvian subsidiary, signed an option-to-purchase agreement with the owner. In December 2008, the Company decided to abandon this property and has no further obligations under the option agreement. In the fourth quarter of 2008, the Company wrote-off the accumulated capitalized costs for this property which amounted to \$307,418.

#### (f) Pucarana, Peru

In May 2007, the Company announced that it had finalized an earn-in agreement whereby it can earn up to a 60% interest in Canadian Shield's Pucarana Gold Property ("Pucarana"), located in southern Peru. The Company has the right to earn a 60% interest in Pucarana by expending US\$1,300,000 over a four year period commencing upon receipt of a drill permit (the "Effective Date"), and by making payments of US\$80,000 to Gallant Minerals Peru Ltd. S.A. (Canadian Shield's Peruvian subsidiary). The Company must make the following expenditures: US\$200,000 prior to the first anniversary of the Effective Date; US\$450,000 prior to the second anniversary of the Effective Date; US\$325,000 prior to the third anniversary of the Effective Date; and US\$325,000 prior to the fourth anniversary of the Effective Date. The Company must also make the following cash payments: US\$30,000 upon signing the agreement (paid) and US\$50,000 upon exercising the option to earn an additional 9% interest. The work commitments for the first twelve months from the Effective Date and the first payment are a firm commitment and all additional work commitments and payments are at the sole discretion of the Company. Upon the Company earning either its 51% interest, or 60% interest if it so elects, the two companies will form a joint venture in which all future expenditures shall be made on a pro rated basis, with standard dilution formulas applied if either party elects not to participate in funding further exploration expenses. In the event either party is diluted to a joint venture interest of 10% or less, that interest will be converted to a 2% NSR with the right of the other party to purchase each 0.5% interest in the NSR for US\$500,000. If the price of gold exceeds US\$500, the purchase price for the NSR increases proportionately to the price of gold. The Company has not received a drill permit at this time and accordingly the Effective Date of the agreement has not been determined.

#### (g) Other Properties, Peru

The Company currently holds interests in five properties besides San Luis and Pucarana. The Company also conducted exploration work on four other properties during the year ended December 31, 2008 and decided to abandon those properties. At year-end the Company wrote-off \$89,252 with respect to those properties.

#### (h) Atocha Property, Bolivia

On December 23, 2003, the Company acquired a 100% indirect interest in the Atocha Project concessions, comprising approximately 7,250 hectares located in West Central Bolivia. The vendor also received a 1.5% NSR royalty for any minerals produced from this property. The Company, at its option, can purchase the royalty for US\$202,000. During the year ended December 31, 2005 the Company wrote-down the carrying value of the Atocha property to \$25,000. In the quarter ended September 30, 2008 the Company decided that no further exploration work would be done on this property and wrote-off the remaining balance of capitalized costs in the amount of \$25,000.

# ESPERANZA SILVER CORPORATION

Notes to the Consolidated Financial Statements

(Expressed in Canadian Dollars)

Years ended December 31, 2008, 2007 and 2006

## 6. Share capital

(a) Authorized

An unlimited number of common shares without par value.

(b) Issued and outstanding

|   | Number<br>Of shares | Stated<br>Value | Contributed<br>Surplus |
|---|---------------------|-----------------|------------------------|
| Balance, December 31, 2005                                    | 33,506,010          | \$ 11,707,396   | \$ 2,802,979           |
| Shares issued for property option (Note 5(a))                 | 540,000             | 1,067,812       | -                      |
| Shares issued for exercise of options                         | 420,000             | 198,400         | -                      |
| Shares issued for exercise of warrants                        | 4,022,535           | 3,070,592       | -                      |
| Shares issued on private placement                            | 1,500,000           | 1,800,000       | -                      |
| Shares issued as finders' fees on private placement           | 18,300              | -               | -                      |
| Less: share issuance costs                                    | -                   | (78,120)        | -                      |
| Warrants issued as finders' fees on private placement         | -                   | (49,715)        | 49,715                 |
| Reclassification on exercise of stock options                 | -                   | 131,956         | (131,956)              |
| Reclassification on exercise of agents' warrants              | -                   | 163,559         | (163,559)              |
| Stock based compensation                                      | -                   | -               | 750,524                |
| Balance December 31, 2006                                     | 40,006,845          | \$ 18,011,880   | \$ 3,307,703           |
| Shares issued for property option                             | 40,000              | 85,000          | -                      |
| Shares issued for exercise of options                         | 232,000             | 179,245         | -                      |
| Shares issued for exercise of warrants                        | 1,937,976           | 1,921,898       | -                      |
| Shares issued on private placement                            | 4,110,000           | 15,001,500      | -                      |
| Less: share issuance costs                                    | -                   | (928,188)       | -                      |
| Less: Agents options and warrants issued on private placement | -                   | (346,211)       | 346,211                |
| Reclassification on exercise of stock options                 | -                   | 79,392          | (79,392)               |
| Reclassification on exercise of agents' warrants              | -                   | 8,457           | (8,457)                |
| Stock based compensation                                      | -                   | -               | 1,336,658              |
| Balance, December 31, 2007                                    | 46,326,821          | \$ 34,012,973   | \$ 4,902,723           |
| Shares issued on the exercise of options                      | 1,150,000           | 325,800         | -                      |
| Shares issued for exploration properties                      | 45,000              | 56,550          | -                      |
| Reclassify contributed surplus on exercise of options         | -                   | 216,598         | (216,598)              |
| Stock-based compensation                                      | -                   | -               | 1,066,015              |
| Balance December 31, 2008                                     | 47,521,821          | \$ 34,611,921   | \$ 5,752,140           |

On February 8, 2007, the Company closed a private placement of 4,110,000 units at a price of \$3.65 each for gross proceeds of \$15,001,500. Each unit consisted of one common share and one half share purchase warrant, with each whole warrant entitling the holder to purchase one additional common share at a price of \$4.35 until February 8, 2009. Finders' fees relating to this private placement were comprised of a cash payment of \$899,949, the issuance of agents' options enabling the agents to acquire up to 232,864 units with an exercise price of \$3.65 per unit on the same terms as the private placement.

On February 21, 2006, the Company closed a private placement of 1,500,000 units at a price of \$1.20 each for gross proceeds of \$1,800,000. Each unit consisted of one common share and one half share purchase warrant, with each whole warrant entitling the holder to purchase one additional common share at a price of \$1.50 until August 21, 2007. Finders' fees for this private placement included cash payments totaling \$78,120, the issuance of 18,300 units on the same terms as the private placement and the issuance of 83,400 Broker's Warrants exercisable at \$1.50 and expiring August 21, 2007.

# ESPERANZA SILVER CORPORATION

Notes to the Consolidated Financial Statements

(Expressed in Canadian Dollars)

Years ended December 31, 2008, 2007 and 2006

## 6. Share capital (continued)

### (c) Options

The Company adopted a share option plan (“the Plan”) pursuant to the policies of the TSX Venture Exchange (“the Exchange”). The maximum aggregate number of shares that may be reserved for issuance under the Plan is limited to 10% of the issued common shares of the Company. The maximum term of the options is five years and the vesting requirements are determined at the time of each grant.

The Plan has been approved by the Exchange and is approved by the shareholders of the Company each year at its annual general meeting. During the years ended December 31, 2008, 2007 and 2006 the change in stock options outstanding was as follows:

|                                 | Number<br>of Shares | Weighted<br>Average<br>Exercise<br>Price |
|---------------------------------|---------------------|--|
| Balance as of December 31, 2005 | 2,610,000           | \$ 0.39                                  |
| Granted                         | 892,500             | 1.56                                     |
| Exercised                       | (420,000)           | 0.47                                     |
| Balance as of December 31, 2006 | 3,082,500           | 0.72                                     |
| Granted                         | 1,540,364           | 3.27                                     |
| Exercised                       | (232,000)           | 0.77                                     |
| Balance as of December 31, 2007 | 4,390,864           | 1.61                                     |
| Granted                         | 1,210,500           | 1.34                                     |
| Exercised                       | (1,150,000)         | 0.28                                     |
| Expired                         | (267,864)           | 3.27                                     |
| Balance as of December 31, 2008 | 4,183,500           | 1.79                                     |

As at December 31, 2008, stock options are outstanding enabling the holders to acquire up to 4,183,500 common shares with a weighted average remaining contractual life of 2.96 years. The weighted average exercise price for options exercisable at year-end was \$1.65. The details of the outstanding options at year-end are as follows:

| Grant Date                 | Number<br>Outstanding | Exercise<br>price | Number<br>vested | Expiry<br>date |
|----------------------------|-----------------------|-------------------|------------------|----------------|
| September 9, 2004          | 300,000               | 0.53              | 300,000          | 09/09/09       |
| June 14, 2005              | 450,000               | 0.40              | 450,000          | 06/14/10       |
| July 5, 2005               | 5,000                 | 0.355             | 5,000            | 07/05/10       |
| September 23, 2005         | 75,000                | 0.65              | 75,000           | 09/23/10       |
| May 18, 2006               | 835,500               | 1.56              | 835,500          | 05/18/11       |
| January 8, 2007            | 25,000                | 3.70              | 25,000           | 01/08/12       |
| January 22, 2007           | 100,000               | 3.35              | 100,000          | 01/22/12       |
| April 18, 2007             | 942,500               | 3.48              | 628,333          | 04/18/12       |
| April 25, 2007             | 5,000                 | 3.48              | 3,333            | 04/25/12       |
| August 2, 2007             | 35,000                | 2.41              | 23,333           | 08/02/12       |
| September 12, 2007         | 200,000               | 1.91              | 133,333          | 09/12/12       |
| February 8, 2008           | 900,500               | 1.40              | 900,500          | 02/08/13       |
| February 27, 2008          | 200,000               | 1.40              | 200,000          | 02/27/13       |
| August 20, 2008            | 10,000                | 0.73              | 10,000           | 08/20/13       |
| October 6, 2008            | 100,000               | 0.69              | 100,000          | 10/06/13       |
| Balance, December 31, 2008 | 4,183,500             | 1.79              | 3,789,332        |                |

## ESPERANZA SILVER CORPORATION

Notes to the Consolidated Financial Statements

(Expressed in Canadian Dollars)

Years ended December 31, 2008, 2007 and 2006

### 6. Share capital (continued)

#### (d) Warrants

During the years ended December 31, 2008, 2007 and 2006 the change in warrants outstanding was as follows:

|  | Number<br>of Shares | Weighted<br>Average<br>Exercise<br>Price |
|--|---------------------|--|
| Balance as of December 31, 2004          | 8,474,922           | 0.89                                     |
| Issued                                   | 3,375,801           | 0.82                                     |
| Exercised                                | (1,057,562)         | 0.43                                     |
| Expired                                  | (5,675,200)         | 1.09                                     |
| Balance as of December 31, 2005          | 5,117,961           | 0.73                                     |
| Issued                                   | 842,550             | 1.50                                     |
| Exercised                                | (4,022,535)         | 0.76                                     |
| Balance as of December 31, 2006          | 1,937,976           | 0.99                                     |
| Issued                                   | 2,055,000           | 4.35                                     |
| Exercised                                | (1,937,976)         | 0.99                                     |
| Balance as of December 31, 2007 and 2008 | 2,055,000           | 4.35                                     |

As at December 31, 2008, share purchase warrants are outstanding enabling the holders to acquire up to 2,055,000 common shares with a weighted average exercise price of \$4.35 per share, as follows:

|                            | Number outstanding | Exercise price | Expiry date |
|----------------------------|--------------------|----------------|-------------|
| Private placement warrants | 2,055,000          | \$ 4.35        | 02/08/09    |

The value of \$nil (2007 - \$346,211; 2006 - \$49,715) represented by the agent's warrants and/or options issued as finders' fees (Note 6 (b)), have been measured on a fair value basis using the Black-Scholes option pricing model, with the following assumptions:

|                                 | 2008 | 2007   | 2006   |
|---------------------------------|------|--------|--------|
| Expected dividend yield         | -    | 0%     | 0%     |
| Expected stock price volatility | -    | 71%    | 72%    |
| Risk-free interest rate         | -    | 4.05%  | 3.50%  |
| Expected life in years          | -    | 1.00   | 1.50   |
| Fair value                      | -    | \$0.99 | \$0.54 |

## ESPERANZA SILVER CORPORATION

Notes to the Consolidated Financial Statements

(Expressed in Canadian Dollars)

Years ended December 31, 2008, 2007 and 2006

### 6. Share capital (continued)

#### (e) Stock-based compensation and contributed surplus

During the year ended December 31, 2008, the Company granted 1,210,500 stock options to directors, officers and consultants with a weighted average exercise price of \$1.34 and expiry dates ranging from February 8, 2013 to October 6, 2013. Of these options, 1,110,500 vested immediately and 100,000 vested six months after the grant date. In 2007, the Company granted 1,307,500 stock options to directors, officers and consultants with a weighted average exercise price of \$3.21 and expiry dates ranging from January 8 to September 12, 2012. Of these options, 519,167 vested immediately and 394,167 vested one year after the grant date and 394,166 vested two years after the grant date. In 2006, the Company granted 892,500 stock options with an exercise price of \$1.56 per share and an expiry date of May 18, 2011. All of those options vested immediately. The options have been measured on a fair value basis using the Black-Scholes option pricing model, with the following weighted average assumptions:

|  | 2008   | 2007   | 2006   |
|--|--------|--------|--------|
| Expected dividend yield                | 0%     | 0%     | 0%     |
| Expected stock price volatility        | 71%    | 71%    | 79%    |
| Risk-free interest rate                | 3.03%  | 4.08%  | 4.16%  |
| Expected life of options in years      | 3.0    | 2.9    | 3.0    |
| Weighted average fair value of options | \$0.62 | \$1.50 | \$0.84 |

Based on these inputs, under the fair value based method of accounting for stock-based compensation, the Company recorded stock-based compensation expense of \$1,066,015 (2007 - \$1,336,658; 2006 - \$750,524) with the offsetting amount credited to contributed surplus. Of the total stock based compensation expense of \$1,066,015, \$752,409 was for options granted in the year with the balance of \$313,606 for options granted in prior years. The weighted average grant date fair value for options granted in the year was \$0.62 per option.

### 7. Related party transactions

In 2007 and 2006 Ionic Management Ltd. ("Ionic"), a private company related by virtue of a director in common, provided office space on a monthly rental basis. In 2007 Ionic charged \$11,900 (2006 - \$15,000) for rent. At December 31, 2007, the Company owed Ionic \$nil (2006 - \$1,326) which is included in accounts payable. These transactions were in the normal course of operations and are measured at the exchange amount which is the amount established and agreed to by the related parties.

### 8. Commitments and contingencies

At December 31, 2008, the Company had a commitment on an office lease in Denver which expires June 30, 2012. The estimated total rent payable on the remaining portion of this lease is US\$244,600

## ESPERANZA SILVER CORPORATION

Notes to the Consolidated Financial Statements

(Expressed in Canadian Dollars)

Years ended December 31, 2008, 2007 and 2006

### 9. Income taxes

A reconciliation of income tax recovery at statutory rates compared to reported income tax recovery is as follows:

|  | 2008           | 2007           | 2006           |
|--|----------------|----------------|----------------|
| Statutory tax rate                         | 31.00%         | 34.12%         | 34.12%         |
| Loss for the year                          | \$ (5,129,245) | \$ (2,839,379) | \$ (1,572,623) |
| Expected income tax recovery               | (1,590,100)    | (968,200)      | (536,300)      |
| Non-deductible expenses and other          | (1,052,400)    | (584,700)      | 253,500        |
| Effect of foreign tax rate differences     | 241,500        | 212,000        | 5,700          |
| Unrecognized benefit of non-capital losses | 2,401,000      | 1,340,900      | 277,100        |
| Total income tax recovery                  | \$ -           | \$ -           | \$ -           |

The significant components of the Company's future income tax assets and liabilities are as follows:

|   | 2008        | 2007         | 2006         |
|---|-------------|--------------|--------------|
| Future income tax assets:               |             |              |              |
| Non-capital loss carry forwards         | 5,170,500   | \$ 3,298,500 | \$ 2,787,900 |
| Capital loss carry forwards             | 1,744,200   | -            | -            |
| Resource and capital asset expenditures | (427,500)   | (657,500)    | (526,300)    |
| Share issuance costs                    | 160,700     | 318,300      | 81,300       |
| Future income tax assets                | 6,647,900   | 2,959,300    | 2,342,900    |
| Valuation allowance                     | (6,647,900) | (2,959,300)  | (2,342,900)  |
| Net future income tax assets            | \$ -        | \$ -         | \$ -         |

As at December 31, 2008, the Company has non-capital losses from operations of approximately \$18.7 million available for deduction against future taxable income. Non-capital losses, if not utilized, will expire through 2028. The realization of future tax benefits which may arise as a result of these non-capital losses and other income tax pools cannot be viewed as more likely than not. Accordingly, no future income tax assets have been recognized in these financial statements and have been offset by a valuation allowance.

### 10. Management of capital

The Company's objectives when managing capital are to safeguard the Company's ability to continue as a going concern in order to pursue the development of its mineral properties. Esperanza relies mainly on equity issuances to raise new capital and on entering joint venture agreements on certain properties which enables it to conserve capital and to reduce risk. In the management of capital, the Company includes the components of shareholders' equity as well as cash. The Company prepares annual estimates of exploration expenditures and monitors actual expenditures compared to the estimates to ensure that there is sufficient capital on hand to meet ongoing obligations. The Company's investment policy is to invest its cash in highly liquid short-term deposits with terms of one year or less and which can be liquidated after thirty days without interest penalty. The Company currently has sufficient capital to fund its exploration programs and to cover its administrative costs for the next twelve months.

# ESPERANZA SILVER CORPORATION

Notes to the Consolidated Financial Statements

(Expressed in Canadian Dollars)

Years ended December 31, 2008, 2007 and 2006

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## 11. Management of financial risk

The Company's financial instruments are exposed to certain financial risks, which include currency risk, credit risk, liquidity risk and interest rate risk.

### (a) Currency Risk

The Company is exposed to the financial risk related to the fluctuation of foreign exchange rates. The Company operates in Canada, the United States, Mexico, Peru and Bolivia. The Company funds cash calls to its subsidiary companies outside of Canada in US dollars and a portion of its expenditures are also in the other local currencies. The greatest risk is the exchange rate of the Canadian dollar relative to the US dollar and the Mexican peso and a significant change in these rates could have an effect on the Company's results of operations, financial position or cash flows. The Company has not hedged its exposure to currency fluctuations. At December 31, 2008, the Company is exposed to currency risk through the following assets and liabilities denominated in US dollars and Mexican pesos:

|  | US\$    | Pesos      |
|--|---------|------------|
| Cash and cash equivalents                | 71,400  | 68,200     |
| Receivables                              | 6,500   | 10,878,800 |
| Accounts payable and accrued liabilities | 79,700  | 3,000      |
| Net exposure                             | (2,300) | 980,800    |

Based on the above net exposures as at December 31, 2008, and assuming that all other variables remain constant, a 1% change in the value of the Canadian dollar against the US dollar and Mexican peso would result in an increase / decrease of approximately \$10,000 in the loss from operations.

### (b) Credit Risk

The Company's cash and cash equivalents are mainly held through large Canadian or US financial institutions and at December 31, 2008 are mainly cash in guaranteed investment certificates and accordingly credit risk is minimized. The Company's receivables are mainly VAT receivable from the Mexican government.

### (c) Liquidity Risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they fall due. The Company manages liquidity risk through the management of its capital resources as outlined in note 10.

### (d) 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 the market interest rates. The Company's cash is held mainly in interest bearing accounts and therefore there is currently minimal interest rate risk.

## ESPERANZA SILVER CORPORATION

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(Expressed in Canadian Dollars)

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### 12. Segmented information

The Company operates in a single reportable operating segment, being exploration and development of mineral properties.

Summarized financial information for the geographic segments the Company operates in are as follows:

|                      | North America | Mexico      | Bolivia  | Peru      | Total       |
|----------------------|---------------|-------------|----------|-----------|-------------|
| 2008                 |               |             |          |           |             |
| Revenue              | \$ 372,596    | \$ 88       | \$ -     | \$ -      | \$ 372,684  |
| Loss for the year    | (2,691,685)   | (1,695,768) | (7,942)  | (733,850) | (5,129,245) |
| Assets               | 8,485,856     | 11,170,677  | 14,681   | 1,579,409 | 21,250,623  |
| Capital expenditures | 6,819         | 4,597,078   | -        | 454,280   | 5,058,177   |
| 2007                 |               |             |          |           |             |
| Revenue              | \$ 644,148    | \$ 2,133    | \$ -     | \$ -      | \$ 646,281  |
| Loss for the year    | (2,224,170)   | (187,397)   | (29,550) | (398,262) | (2,839,379) |
| Assets               | 15,502,824    | 8,752,970   | 27,141   | 1,535,022 | 25,817,957  |
| Capital expenditures | 45,271        | 3,369,531   | -        | 583,335   | 3,998,137   |
| 2006                 |               |             |          |           |             |
| Revenue              | \$ 155,266    | \$ -        | \$ -     | \$ -      | \$ 155,266  |
| Loss for the year    | (1,434,487)   | (10,075)    | (40,380) | (87,681)  | (1,572,623) |
| Assets               | 4,687,910     | 4,289,413   | 31,770   | 1,200,730 | 10,209,823  |
| Capital expenditures | 20,459        | 1,920,615   | -        | 702,917   | 2,643,991   |

### 13. Differences between Canadian and United States generally accepted accounting principles (GAAP)

#### Mineral Exploration Costs

Under Canadian GAAP applicable to junior mining exploration companies (Note 2), mineral exploration expenditures may be deferred on prospective properties until such time as it is determined that further exploration is not warranted, at which time the property costs are written-off. Under US GAAP, in accordance with Emerging Issues Task Force (EITF No. 04-02 -- Whether Mineral Rights are Tangible or Intangible Assets), the Company has capitalized mineral property acquisition costs for United States GAAP for the periods beginning after April 30, 2004 while all exploration costs are expensed until an independent feasibility study has determined that the property is capable of economic commercial production. The following items (a) to (f) provide a summary of the impact on these financial statements that would result from the application of U.S. accounting principles to deferred property costs.

**ESPERANZA SILVER CORPORATION**

Notes to the Consolidated Financial Statements

*(Expressed in Canadian Dollars)*

Years ended December 31, 2008, 2007 and 2006

**13. Differences between Canadian and United States generally accepted accounting principles (GAAP)**

(continued)

|  | December 31,                     |                   |                   |
|--|----------------------------------|-------------------|-------------------|
|  | 2008                             | 2007              | 2006              |
|  | \$                               | \$                | \$                |
| <b>a) Assets</b>   |                                  |                   |                   |
| <b>Deferred Property Costs</b>                                       |                                  |                   |                   |
| Deferred property costs under Canadian GAAP                          | 11,632,343                       | 9,566,594         | 4,848,116         |
| Deferred property costs expensed under U.S. GAAP                     | (9,900,966)                      | (7,649,068)       | (3,101,980)       |
| Deferred property costs under U.S. GAAP                              | 1,731,377                        | 1,917,526         | 1,746,136         |
| <b>b) Operations</b>   |                                  |                   |                   |
| Loss for the year following Canadian GAAP                            | (5,129,245)                      | (2,839,379)       | (1,572,623)       |
| Deferred property costs expensed under U.S. GAAP                     | (2,493,705)                      | (4,547,088)       | (2,068,029)       |
| Deferred property costs written-off under Canadian GAAP              | -                                | -                 | -                 |
| Loss for the year under U.S. GAAP                                    | (7,622,950)                      | (7,386,467)       | (3,640,652)       |
| <b>c) Deficit</b>  |                                  |                   |                   |
| Closing deficit under Canadian GAAP                                  | (19,302,746)                     | (14,173,501)      | (11,334,122)      |
| Adjustment to deficit for deferred costs expensed under U.S. GAAP    | (10,142,773)                     | (7,649,068)       | (3,101,980)       |
| Closing deficit under U.S. GAAP                                      | (29,445,519)                     | (21,822,569)      | (14,436,102)      |
| <b>d) Cash Flows – Operating Activities</b>                          |                                  |                   |                   |
| Cash applied to operations under Canadian GAAP                       | (2,408,992)                      | (720,945)         | (1,735,607)       |
| Add net loss following Canadian GAAP                                 | 5,129,245                        | 2,839,379         | 1,572,623         |
| Less net loss following U.S. GAAP                                    | (7,622,950)                      | (7,386,467)       | (3,640,652)       |
| Less deferred property costs written-off under Canadian GAAP         | (2,236,319)                      | -                 | -                 |
| Cash applied to operations under U.S. GAAP                           | (7,139,016)                      | (5,268,033)       | (3,803,636)       |
| <b>e) Cash Flows – Investing Activities</b>                          |                                  |                   |                   |
| Cash applied under Canadian GAAP                                     | (5,058,177)                      | (3,974,597)       | (2,643,991)       |
| Add cash property costs expensed under U.S. GAAP                     | 5,009,227                        | 3,772,772         | 2,081,885         |
| Cash received from (applied to) investing activities under U.S. GAAP | (48,950)                         | (201,825)         | (562,106)         |
| <b>f) Loss per Share</b>   | For the years ended December 31, |                   |                   |
|  | 2008                             | 2007              | 2006              |
| Numerator: Loss for the year under U.S. GAAP                         | \$<br>(7,622,950)                | \$<br>(7,386,467) | \$<br>(3,640,652) |
| Denominator: Weighted-average number of shares outstanding           | 47,299,635                       | 44,550,285        | 36,715,551        |
| Basic and diluted loss per share under U.S. GAAP                     | (0.16)                           | (0.18)            | (0.10)            |



**CORPORATE HEADQUARTERS**

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*Director*

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*Director*

MICHAEL H. HALVORSON  
*Director*

GEORGE ELLIOTT  
*Director*

**OFFICERS**

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*President & Chief Executive Officer*

J. STEVENS ZUKER  
*Senior Vice-President*

PAUL J. BARTOS  
*Vice President and Chief Geologist*

WILLIAM BOND  
*VP Exploration*

DAVID L. MILES  
*Chief Financial Officer*

KIM C. CASSWELL  
*Corporate Secretary*

**REGISTRAR AND TRANSFER AGENT**

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**SHARE CAPITALIZATION**

April 15, 2009: 47,521,821

**SHARES LISTED**

TSX Venture Exchange  
Symbol: EPZ

Website: [www.esperanzasilver.com](http://www.esperanzasilver.com)