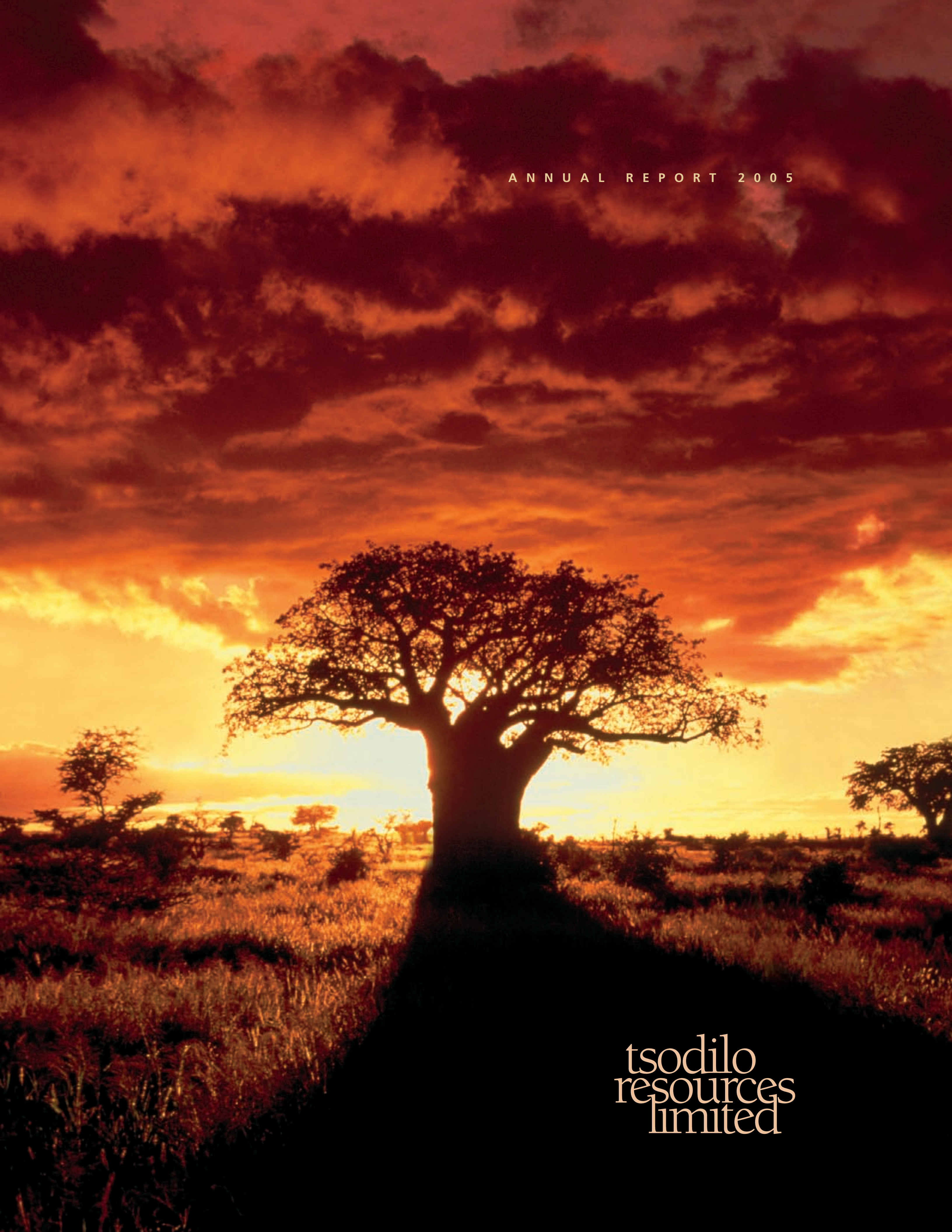


ANNUAL REPORT 2005

# tsodilo resources limited



## Dolerite Dyke Swarm, Venetia - Nxau Nxau


*Front cover photo courtesy of www.game-reserve.com*

## President's Message

A tremendous amount of work was initiated and completed during the year even though the drilling program did not progress as anticipated. Set forth below are some of the highlights of this past year and a brief look of the work program which is planned for 2006.

Drilling in the Kalahari

## Fellow Shareholders,

For the first time since the former minority shareholders assumed control of the Company in 2002, we were not able to achieve the goals and objectives which were set with respect to the drilling program. As a result of our drilling contractor's delay in arriving on site due to equipment problems and the lack of alternative drill rigs in southern Africa caused by the high demand in the exploration sector for evaluation of water and mineral resource deposits, only 25% of the planned drilling was completed. To ensure that the exploration program is not again delayed due to reliance on outside contractors, the Company has ordered an Atlas Copco CT14 diamond core drill rig. After an initial break-in period, we expect to be able to achieve the drill production rates that we have projected enabling the exploration program to advance without disruption.

A tremendous amount of work was initiated and completed during the year even though the drilling program did not progress as anticipated. Set forth below are some of the highlights of this past year and a brief look of the work program which is planned for 2006.

## EXPLORATION PROGRAM UPDATE

### NEWDICO (Pty) Limited ("Newdico")

#### Summary of work completed in 2005

- Ground geophysical surveys, both magnetic and gravity, were completed over seven airborne magnetic anomalies.
- Follow-up kimberlitic indicator mineral ("KIM") sampling grids over two target anomalies were completed.
- Our geophysical consultants assessed the near-surface magnetic component of the airborne magnetic data in order to define paleo-drainage channels in the basement and Kalahari sequences. The results will direct drill investigation of these possible paleo-drainage channels in order to trace back secondary deposits of KIM including G10 garnet and diamond to their source kimberlite(s).
- A Geographical Information System was initiated with all available geological, geophysical and geochemical data captured onto the system. The data is being used to prioritize target areas for further exploration.
- On July 1, 2005, an application for 18 prospecting license areas, totaling 16,800 square kilometers, was approved by the Minister of Mineral, Energy and Water Affairs effectively extending Newdico's tenancy until 2012.
- Our remote sensing consultant completed a first-pass interpretation of the various forms of satellite and radar imagery and has recommended priority areas for further investigation where the evidence suggests the alluvial G10 and diamond deposits at Tsumkwe and Omatako were sourced.
- Kimberlite indicator mineral sampling over and around two target areas, the Morama Anomaly and a portion of the satellite feature - Section Line 2, was completed.
- The planned drilling campaign for 2005 was affected by the drilling contractor's delay in arriving on site due to equipment problems and the lack of alternative drill rigs in southern Africa as a result of the high demand in the exploration sector for evaluation of water and mineral resource deposits. Three A15 evaluation holes were completed and sections of the A15 kimberlite samples were evaluated using petrography, the chemistry of indicator mineral grains and micro-diamond analysis.

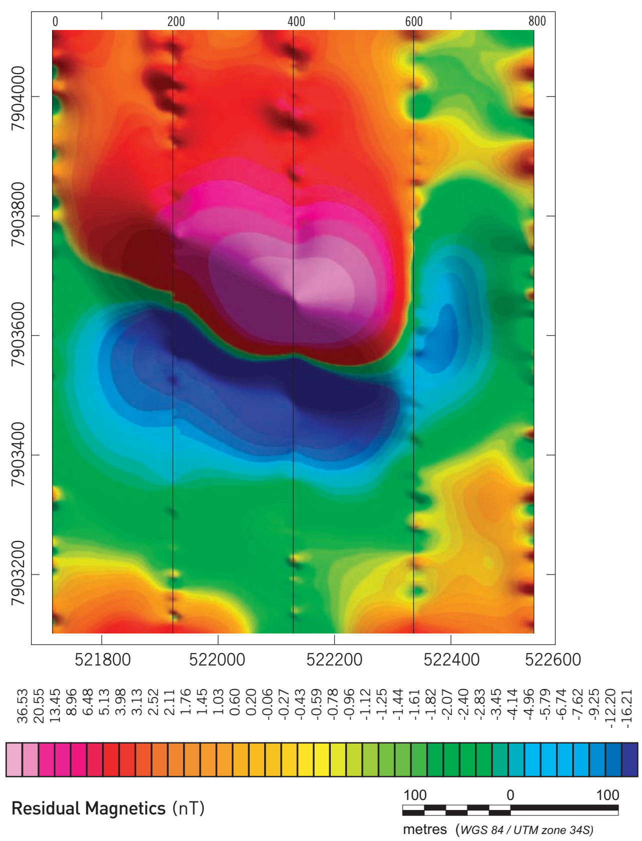
## Planned Exploration Program for 2006

The program is based on our strategy of using a combination of indicator mineral sampling, magnetic and gravity data to generate individual targets for drill evaluation and our regional strategy of evaluating possible transport corridors giving rise to the alluvial secondary KIM and diamond deposits at Tsumkwe and Omatako. Our program for 2006 will include the following:

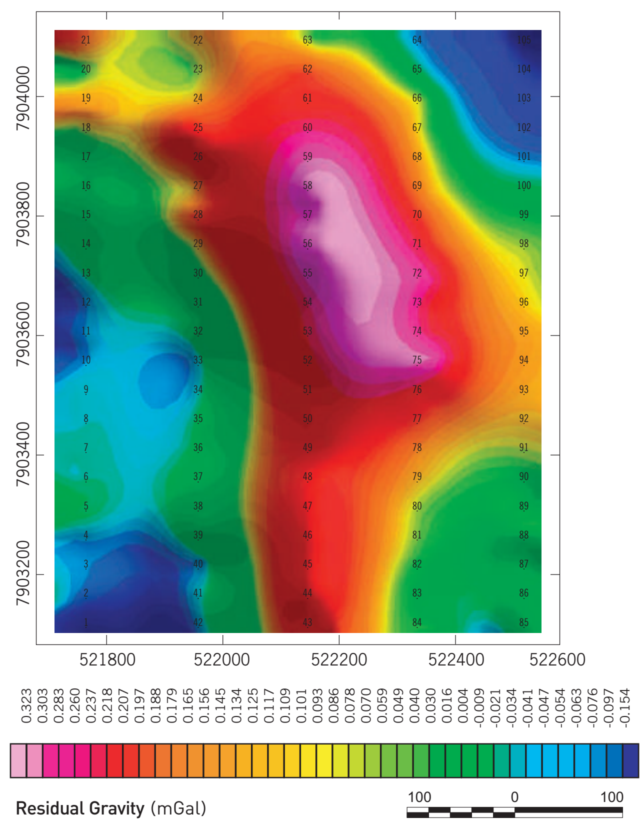
- Extend the 2x2 kilometer KIM sampling grid for 24 kilometers to the south of the Nxau Nxau kimberlite field to cover the western 40 kilometers of the Okavango Dyke Swarm. This will involve the collection and processing of some 240 deflation soil samples.
- Prepare drill access roads and collect KIM samples along two 17 kilometer sections across interpreted paleo-drainage channel transport corridors.
- Perform a trial airborne survey over the western portion of the dyke swarm using low-level flying, close-spaced survey lines and gradiometer array magnetometers to distinguish dolerite from kimberlite magnetic responses.
- Drill evaluation of the 16 high-priority targets in the Guma District.
- Drill evaluation of the current 4 high-priority targets in the Nxau-Nxau kimberlite field.
- Drill evaluation of transport corridor sections.
- Drill evaluation of any high-priority airborne test survey magnetic anomaly targets.
- If time allows, drill evaluation of 18 second-priority targets in the Nxau-Nxau kimberlite field.

The favorable chemistry and diamond preservation potential of the kimberlites in our license blocks together with the known secondary alluvial diamond discoveries down slope across the border in Namibia establish the greater Nxau Nxau field as highly prospective with the possibility of several economic kimberlites present within our ground. To date, at least 18% of the kimberlites discovered in the Nxau Nxau field are known to be diamondiferous. Our target selection is and remains focused and we look forward to drill testing and analysis of further selected anomalies in the Nxau Nxau field once the rains have ceased. C15 and A41 are just two of the multiple priority kimberlite targets to be drilled in the next few months. We remain on track to locating the source of the alluvial G10 and diamond deposits at Tsumkwe and Omatako.

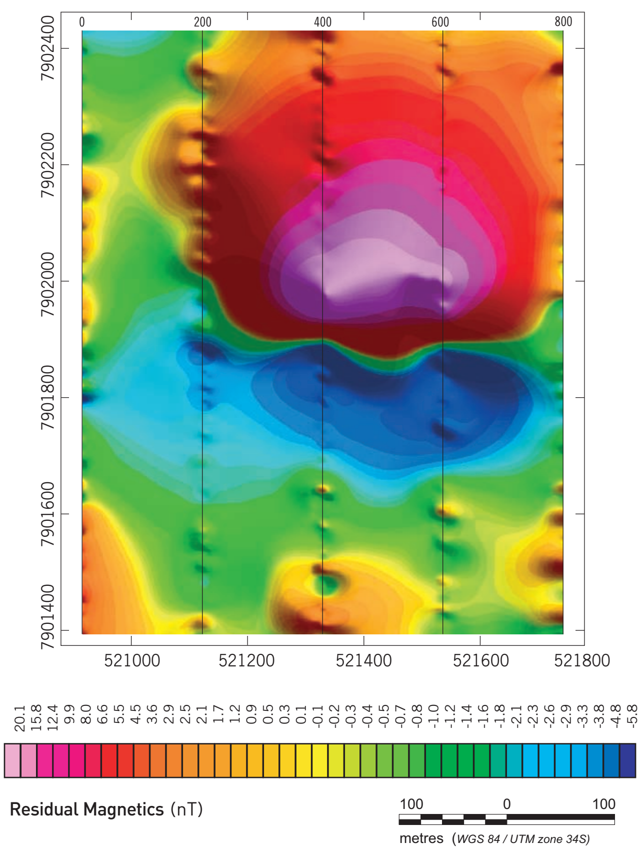
**Newdico -** Anomaly C15 - 1st Order - Residual Magnetic



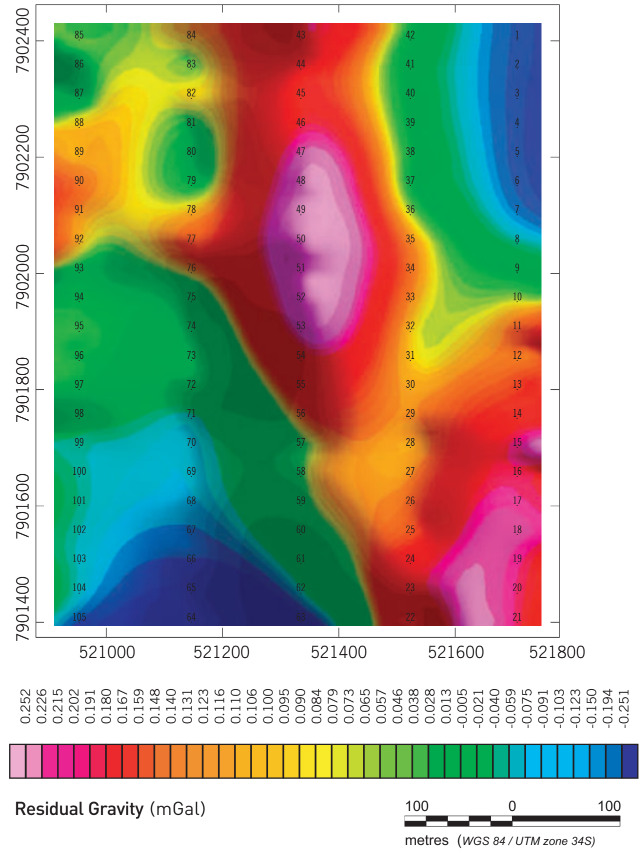

**Newdico -** Anomaly C15 - 1st Order - Residual Gravity



**Newdico -** Anomaly A41 - 1st Order - Residual Magnetic




**Newdico -** Anomaly A41 - 1st Order - Residual Gravity




## GCWIHABA Resources (Pty) Limited ("Gcwihaba")

### Diamond Licenses

### Summary of work completed in 2005

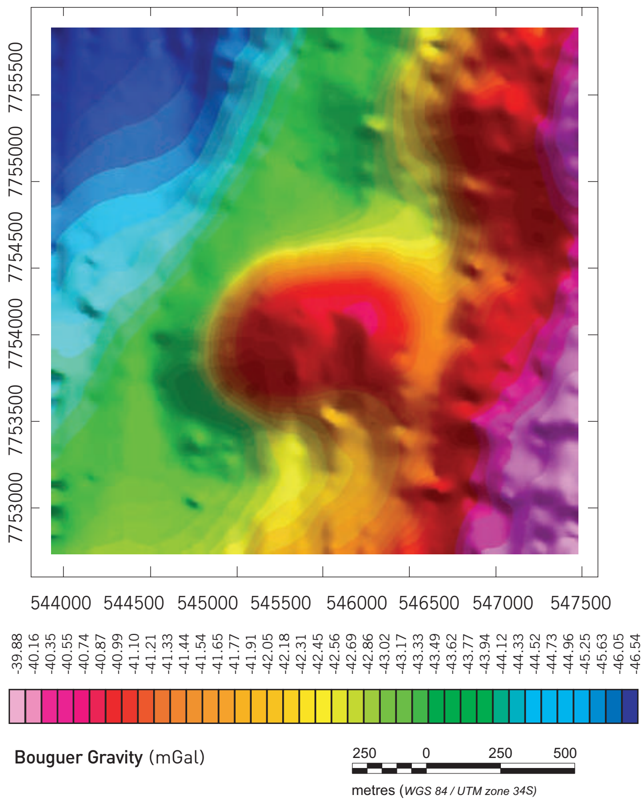
- A large ground geophysical survey grid, using both magnetic & gravity over the 2021 A7 airborne magnetic anomaly was completed.
- As with our Newdico licenses, our geophysical consultants assessed the near-surface magnetic component of the airborne magnetic data in order to define paleo-drainage channels in the basement and Kalahari sequences. The results will be used to direct drill investigation of these possible paleo-drainage channels in order to trace back secondary deposits of KIM and diamond to their source kimberlite(s).
- During the year our Geographical Information System was initiated with all available geological, geophysical and geochemical data for these licenses captured onto the system. The data is being used to prioritize target areas for further exploration.
- Our remote sensing consultant extended his first-pass interpretation of the various forms of satellite and radar imagery into the Gcwihaba licenses and has recommended priority areas for further investigation where the evidence suggests the alluvial KIM and diamond deposits at Tsumkwe and Omatako could have been sourced.

### Planned Exploration Program for 2006

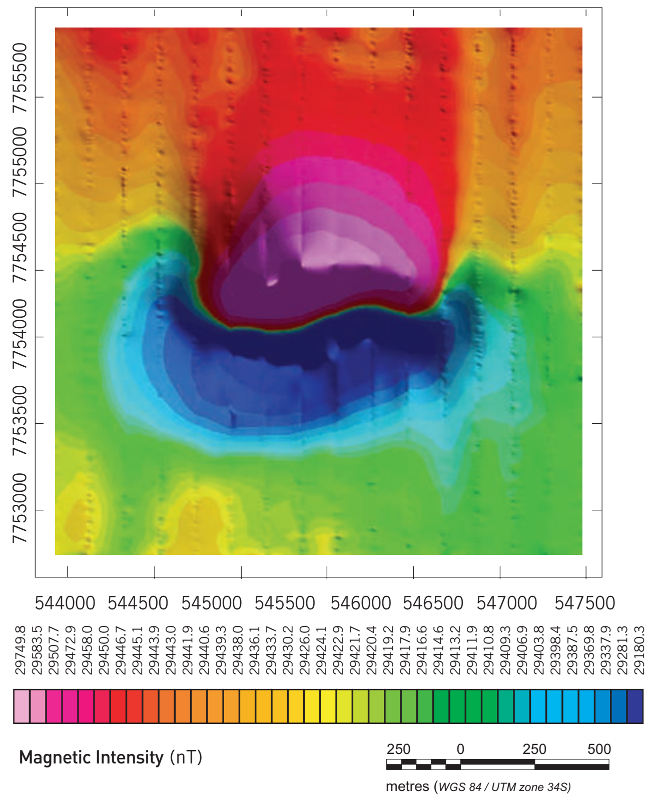
- Drill evaluation of Anomaly 2021 A7 is a high priority.
- The Company currently has 6,800 square kilometers under license. Pursuant to the provisions of the Botswana Mines and Minerals Act No 17 of 1999 (the "Act"), the Company is required to relinquish a minimum of 50% of the initial license area after a period of three years. The Company is currently reviewing its license block holdings in order to comply with the relinquishment provisions of the Act on or before the expiry date of June 30, 2006.

### Planned Exploration Program for 2006

**Gcwihaba -** Anomaly 2021A7 - Bouguer Gravity




**Gcwihaba -** Anomaly 2021A7 - Total Magnetic Intensity




### Base and Precious Metals Licenses

### Summary of work completed in 2005

- Four new base and precious metal licenses were granted to the Company on October 1, 2005, and encompass an area of some 3,780 square kilometers. These licenses were issued for an initial period of three years, renewable for 2 two-year periods.
- The license areas were selected based on the results of a 1999 government geochemical soil sampling program, released and partially reported on in November 2001.
- One of the nickel anomalies, named the Morama Anomaly, has been checked with a total of 15 soil samples collected for multi-element analysis – results are pending.

### Planned Exploration Program for 2006

- There are several zones of co-incident base metal anomalies that require follow-up sampling as a first step in the evaluation process. A Chalcophyle Index is currently in preparation to assist in the prioritization of these zones.
- Exploratory drilling of suspected base metal deposits to determine their nature, composition and size.

### Financing the Company's exploration programs

During the past year, the Company funded exploration activity by raising funds in the capital markets through the successful issuance of stock by way of private placements. This process will continue in the coming year. Our current share base consists of 11,832,929 issued and outstanding (14,070,079 on a fully diluted basis) common shares. Tsodilo has no debt, an 81% interest in our Botswana Newdico project and a 100% interest in our Botswana Gcwihaba projects. The Company is well positioned to meet the challenges in the upcoming year.

A very busy and exciting year lies ahead as we make progress in the exploration for an economic kimberlite below the Kalahari cover on this sector of the Congo craton. Please follow our progress carefully and remain informed by regular visits to our website, www.TsodiloResources.com.

James M. Bruchs
President and Chief Executive Officer
March 20, 2006

# Management's Discussion and Analysis

This management's discussion and analysis ("MD&A") should be read in conjunction with the Consolidated Annual Financial Statements for the period ended December 31, 2005 and comments on the factors that affected the Company's performance during the periods covered by the Consolidated Annual Financial Statements as well as the Company's financial condition and future prospects. The Company's functional and reporting currency was changed to United States dollars and all amounts stated are in United States dollar unless otherwise noted. During the third quarter, the board decided that it was in the best interests of the Company to change its financial year end from March 31 to December 31 effective December 31, 2005. The change in financial year to December 31 was made to align with the reporting schedule of comparable public companies. The period December 31, 2005 is the transitional period and has a nine month reporting period. This management's discussion and analysis has been prepared as at March 20, 2006.

## OVERVIEW

Tsodilo Resources Limited ("Tsodilo" or the "Company") was organized under the laws of the Province of Ontario in 1996 and continued under the laws of the Yukon in 2002. The shares of the Company are listed and posted for trading on the TSX Venture Exchange under the symbol: TSD. Tsodilo is an international diamond exploration company with the majority interest in a kimberlite exploration project in northwest Botswana. The Company has not yet determined whether these properties contain reserves that can be economically mined. As an exploration stage company, the recoverability of amounts shown for exploration expenditures is dependent upon the discovery of reserves that can be economically mined, the securing and maintenance of the interests in the properties, the ability of the Company to obtain the necessary financing to complete the development, and future production or proceeds from the disposition thereof. The Company is also actively reviewing additional opportunities within southern Africa.

### Corporate

At a special meeting of the holders of common shares of the Company held on April 9, 2002 shareholders approved a restructuring of the Company that incorporated the sale of substantially all of the Company's assets. The assets were transferred in settlement of debt due and owing to Trans Hex Group Limited ("Trans Hex Group"), the principal shareholder and creditor of the Company prior to restructuring, of $612,783. The Company retained an interest in all future dividends that may be paid by either Northbank Diamonds Limited, Hoanib Diamonds (Proprietary) Limited or Trans Hex (Zimbabwe) Limited. In addition, the Company was released from the long-term loans due to Trans Hex Group by the subsidiaries being sold, of $3,341,690, and Trans Hex Group agreed to return the 10,688,137 common shares in the capital of the Company, representing 73.22% of the issued and outstanding shares of the Company at that time, to treasury for cancellation. The special meeting of shareholders also approved the discontinuance of the Company from the Province of Ontario and its continuance under the Business Corporations Act (Yukon), the change of name of the Company from Trans Hex International Ltd. to Tsodilo Resources Limited, the election of new directors and the repeal of the existing stock option plan of the Company and adoption of a new stock option plan. Following the restructuring of the Company, as approved by shareholders in April 2002, Tsodilo has no long-term debt.

### Outstanding Share Data

As of March 20, 2006, 11,832,929 common shares of the Company were outstanding. Of the options to purchase common shares issued to eligible persons under the stock option plan of the Company, 1,070,000 options remain outstanding of which 680,000 are exercisable at exercise prices ranging from Canadian $0.15 - $1.85. If all options were vested and exercised, 1,070,000 common shares of the Company would be issued.

As of March 20, 2006, 1,167,330 warrants are outstanding. The warrants were issued by way of the private placements utilized by the Company for financing purposes. Each warrant entitles the holder thereof to purchase one common share of the Company at purchase prices ranging from Canadian $0.75 - $2.35 for a period of two years from the date of issuance. If converted, 1,167,330 common shares of the Company would be issued.

### Principal Shareholders of the Company:

The largest shareholder of the Company is its President and Chief Executive Officer, James M. Bruchs, who currently owns, controls or directs 2,545,983 or 21.52% of the issued and outstanding common shares as of March 20, 2006. The Firebird Global Master Fund, Ltd. controls 1,875,630 or 15.85% of the issued and outstanding shares as of March 20, 2006 and John R. Redmond, a Director of the Company, currently owns, controls or directs 1,602,773 or 13.55% of the issued and outstanding shares as of March 20, 2006

### Subsidiaries

The Company has an 81% operating interest in its Botswana subsidiary, Newdico (Proprietary) Limited ("Newdico"), which holds prospecting licenses and applications covering approximately 16,800 square kilometers in northwest Botswana on which there is encouragement for the existence of undiscovered kimberlites in at least three separate areas of the property. The Company's minority partner (19%) in this project, Trans Hex Group, is an established South African diamond mining company. Some, or all, of the current licenses held by Newdico may be subject to the granting of a 2% free carried interest in any mine or mines that may result thereon.

The Company has a 100% interest in its wholly owned Botswana subsidiary, Gcwihaba Resources (Proprietary) Limited ("Gcwihaba"), which has diamond prospecting licenses covering approximately 6,800 square kilometers and base and precious metal licenses covering 3,780 square kilometers.

### Exploration Activities

### Newdico (Proprietary) Limited - Botswana

### Summary of work completed in 2005

- Ground geophysical surveys, both magnetic and gravity, were completed over seven airborne magnetic anomalies.
- Follow-up kimberlitic indicator mineral ("KIM") sampling grids over two target anomalies were completed.
- Our geophysical consultants assessed the near-surface magnetic component of the airborne magnetic data in order to define paleo-drainage channels in the basement and Kalahari sequences. The results will direct drill investigation of these possible paleo-drainage channels in order to trace back secondary deposits of KIM including G10 garnet and diamond to their source kimberlite(s).
- A Geographical Information System was initiated with all available geological, geophysical and geochemical data captured onto the system. The data is being used to prioritize target areas for further exploration.
- On July 1, 2005, an application for 18 prospecting license areas, totaling 16,800 square kilometers, was approved by the Minister of Mineral, Energy and Water Affairs effectively extending Newdico's tenancy until 2012.
- Our remote sensing consultant completed a first-pass interpretation of the various forms of satellite and radar imagery and has recommended priority areas for further investigation where the evidence suggests the alluvial G10 and diamond deposits at Tsumkwe and Omatako were sourced.
- Kimberlite indicator mineral sampling over and around two target areas, the Morama Anomaly and a portion of the satellite feature - Section Line 2, was completed.
- The planned drilling campaign for 2005 was affected by the drilling contractor's delay in arriving on site due to equipment problems and the lack of alternative drill rigs in southern Africa as a result of the high demand in the exploration sector for evaluation of water and mineral resource deposits. Three A15 evaluation holes were completed and sections of the A15 kimberlite samples were evaluated using petrography, the chemistry of indicator mineral grains and micro-diamond analysis.

### Planned Exploration Program for 2006

The program is based on our strategy of using a combination of indicator mineral sampling, magnetic and gravity data to generate individual targets for drill evaluation and our regional strategy of evaluating possible transport corridors giving rise to the alluvial secondary KIM and diamond deposits at Tsumkwe and Omatako. Our program for 2006 will include the following:

- Extend the 2x2 kilometer KIM sampling grid for 24 kilometers to the south of the Nxau Nxau kimberlite field to cover the western 40 kilometers of the Okavango Dyke Swarm. This will involve the collection and processing of some 240 deflation soil samples.
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- Perform a trial airborne survey over the western portion of the dyke swarm using low-level flying, close-spaced survey lines and gradiometer array magnetometers to distinguish dolerite from kimberlite magnetic responses.
- Drill evaluation of the 16 high-priority targets in the Guma District.
- Drill evaluation of the current 4 high-priority targets in the Nxau-Nxau kimberlite field.
- Drill evaluation of transport corridor sections.
- Drill evaluation of any high-priority airborne test survey magnetic anomaly targets.
- If time allows, drill evaluation of 18 second-priority targets in the Nxau-Nxau kimberlite field.

The favorable chemistry and diamond preservation potential of the kimberlites in our license blocks together with the known secondary alluvial diamond discoveries down slope across the border in Namibia establish the greater Nxau Nxau field as highly prospective with the possibility of several economic kimberlites present within our ground. To date, at least 18% of the kimberlites discovered in the Nxau Nxau field are known to be diamondiferous. Our target selection is and remains focused and we look forward to drill testing and analysis of further selected anomalies in the Nxau Nxau field once the rains have ceased. C15 and A41 are just two of the multiple priority kimberlite targets to be drilled in the next few months. We remain on track to locating the source of the alluvial G10 and diamond deposits at Tsumkwe and Omatako.

### GCWIHABA RESOURCES (Pty) Limited ("Gcwihaba")

### Diamond Licenses

### Summary of work completed in 2005

- A large ground geophysical survey grid, using both magnetic & gravity over the 2021 A7 airborne magnetic anomaly was completed.
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basement and Kalahari sequences. The results will be used to direct drill investigation of these possible paleo-drainage channels in order to trace back secondary deposits of KIM and diamond to their source kimberlite(s).

- During the year our Geographical Information System was initiated with all available geological, geophysical and geochemical data for these licenses captured onto the system. The data is being used to prioritize target areas for further exploration.
- Our remote sensing consultant extended his first-pass interpretation of the various forms of satellite and radar imagery into the Gcwihaba licenses and has recommended priority areas for further investigation where the evidence suggests the alluvial KIM and diamond deposits at Tsumkwe and Omatako could have been sourced.

### Planned Exploration Program for 2006

- Drill evaluation of Anomaly 2021 A7 is a high priority.

### Base and Precious Metals Licenses
### Summary of work completed in 2005

- Four new base and precious metal licenses were granted to the Company on October 1, 2005, and encompass an area of some 3,780 square kilometers and are for an initial period of three years, renewable for two two-year periods.
- The licenses were selected based on the results of a 1999 government geochemical soil sampling program, released and partially reported on in November 2001.
- One of the nickel anomalies, named the Morama Anomaly has been checked with a total of 15 soil samples collected for multi-element analysis – results are pending.

### Planned Exploration Program for 2006

- There are several zones of co-incident base metal anomalies that require follow-up sampling as a first step in the evaluation process. A Chalcophyle Index is currently in preparation to assist in the prioritization of these zones.
- Exploratory drilling of suspected base metal deposits to determine their nature, composition and size.

## LIQUIDITY AND CAPITAL RESOURCES

As at December 31, 2005, the Company had net working capital of $296,541 (March 31, 2005: $609,979), which included cash and equivalents $289,810 (March 31, 2005: $637,805). These funds are managed in-house in accordance with specific investment criteria approved by the board of directors, the primary objective being the preservation of capital to assure funding for exploration activities. The Company does not hedge its activities or otherwise use derivatives. At year end the Company did not have any material contractual obligations. The Company is required to spend a minimum on prospecting over the period of its licenses (Newdico: $1.6 million, Gcwihaba: $0.34 milion). To date, the Company has exceeded this requirement in the Newdico project. The Company has recently ordered a mobile diamond core drill rig and transport at a cost of $650,400 and is expecting delivery at the beginning of the second quarter of 2006.

### Financial Instruments

The carrying amounts reflected in the consolidated balance sheets for cash and equivalents, accounts receivable and accounts payable and accrued liabilities approximate their fair values due to the short maturities of these instruments. Due to the nature of the Company's operations, there is no significant credit or interest rate risk.

### Operating Activities

Cash outflow used in operating activities decreased from $473,835 in fiscal March 31, 2005 to $340,924 for the period ended December 31, 2005. Although this is a transitional period, proportionally there is also a decrease in cash outflow. This decrease reflects reductions in professional fees, both legal and audit and, a reduction in investor relations expense.

## SELECTED ANNUAL AND QUARTERLY FINANCIAL INFORMATION

## ANNUAL INFORMATION

| (in US dollars) | Nine Months Ended | Fiscal Year | |
|---|---|---|---|
| | Dec. 31 2005 | Mar. 31 2005 | Mar. 31 2004 |
| Total Revenues | – | – | – |
| Loss before non-controlling interest | 470,811 | 620,822 | 405,814 |
| Basic and diluted loss per share - cents | $0.04 | $0.07 | $0.06 |
| Non-controlling interest | – | – | – |
| Loss for the Year | 470,811 | 620,822 | 405,814 |
| Basic and diluted loss per share - cents | $0.04 | $0.07 | $0.06 |
| Total Assets | 2,032,426 | 2,087,421 | 1,010,432 |
| Total long term liabilities | 280,642 | 237,008 | 213,549 |
| Cash dividends declared | – | – | – |

## QUARTERLY INFORMATION

The quarterly results have been as follows:

(in US dollars)

| | Quarter 1 | Quarter 2 | Quarter 3 | Quarter 4 |
|---|---|---|---|---|
| **Fiscal Year 2004** (ended March 31, 2004) | | | | |
| Total Revenues | – | – | – | – |
| Loss for the period | 54,423 | 87,810 | 82,849 | 180,732 |
| Basic and diluted loss per share - cents | $0.01 | $0.01 | $0.01 | $0.03 |
| Total assets | 631,366 | 1,016,261 | 979,147 | 1,010,432 |
| Total long term liabilities | 158,770 | 189,249 | 189,249 | 213,549 |
| **Fiscal Year 2005** (ended March 31, 2005) | | | | |
| Total Revenues | – | – | – | – |
| Loss for the period | 75,106 | 185,742 | 113,981 | 245,993 |
| Basic and diluted loss per share - cents | $0.01 | $0.01 | $0.01 | $0.03 |
| Total assets | 1,422,230 | 1,408,529 | 1,842,605 | 2,087,421 |
| Total long term liabilities | 213,549 | 237,245 | 237,245 | 237,008 |
| **Fiscal Period 2005*** (ended December 31, 2005) | | | | |
| Total Revenues | – | – | – | |
| Loss for the period | 83,068 | 190,070 | 197,673 | |
| Basic and diluted loss per share - cents | $0.01 | $0.02 | $0.02 | |
| Total assets | 2,171,006 | 2,166,670 | 2,032,426 | |
| Total long term liabilities | 294,236 | 294,236 | 280,642 | |

* Transitional period for year end change to December 31

### Investing Activities

Cash flow applied in investing activities decreased to $281,249 for the period ended December 31, 2005 (March 31, 2005: $589,095). $239,505 or 84.6% of the exploration expenditures were spent on the Newdico properties and $43,472 or 15.4% of the expenditures were on the Gcwihaba properties. All expenditures on exploration properties for the period ended December 31, 2005 were attributable to the Newdico and Gcwihaba projects in northwest Botswana and included the 19% share funded by the Trans Hex Group for the Newdico project. There were no material acquisitions or disposals of capital assets or investments during the year.

In February 2006, the board of directors of Newdico approved an exploration program and budget for the period April 2006 to December 31, 2006 that calls for expenditures totaling approximately Pula 11.6 million (approximately $2.2 million as of March 20, 2006). Trans Hex Group is presently responsible for funding 19% of the expenses of this company. The approved exploration program includes provision for additional soil sampling, airborne and ground magnetics and ground gravity surveying, geophysical interpretation, and drilling equipment.

The required third year of the diamond exploration program expenditures, including license fees, for Gcwihaba amount to approximately Pula 0.42 million (approximately $0.07 million as of March 20, 2006). Gcwihaba's expenditures will exceed this required amount. The required expenditure in the first year of the base metal exploration program amounts to approximately Pula 0.20 million (approximately $0.04 million as of March 20, 2006). Gcwihaba expects to meet or exceed this requirement.

### Financing Activities

Following the restructuring of Tsodilo in April 2002 and the cancellation of the shares formerly held by Trans Hex, the source of financing for the Company's activities changed from debt (related party) finance to equity, through the issue of units by way of non-brokered private placements. Each unit has consisted of one common share of the Company and one or one-half a warrant of the Company, with each full such warrant entitling the holder to purchase one common share of the Company for a purchase price equal to the unit price for a period of two years from the date of issuance. During the period ended December 31, 2005 the Company received proceeds in the amount of $230,544 from the issuance of common shares upon the exercise of warrants during the fiscal period.

Subsequent to the fiscal period end, the Company issued, through non-brokered private placements:

1) 468,776 units of the Company at a price of $1.07 (C$1.25) per unit for gross proceeds to the Company of $500,000. Each unit consists of one common share of the Company and one warrant of the Company, each warrant entitling the holder to purchase one common share of the Company at a price of C$1.00 for a period of two years. The common shares, warrants and warrant shares are subject to a hold period of 12 months, as agreed to by the parties, expiring on January 27, 2007.

2) 319,108 units of the Company at a price of $0.78 (C$0.90) per unit for gross proceeds to the Company of $250,000. Each unit consists of one common share of the Company and one warrant of the Company, each warrant entitling the holder to purchase one common share of the Company at a price of C$1.00 for a period of two years. The common shares, warrants and warrant shares are subject to a statutory hold period of 4 months, as agreed to by the parties, expiring on June 21, 2006.

Tsodilo expects to raise the amounts required to fund its 81% share of the Newdico project, the Gcwihaba projects and corporate general and administration expenses, by way of negotiated non-brokered private placements.

## RESULTS OF OPERATIONS

On a consolidated basis Tsodilo recorded a net loss of $470,811 in the fiscal period ended December 31, 2005 ($0.04 cents per common share) compared to a net loss of $620,822 in the fiscal year ended March 31, 2005 ($0.07 cents per common share). Eliminating the effect of non-cash charges relating to stock-based compensation and the effects of foreign exchange gains and losses totaling $213,302 for the period ended December 31, 2005 (March 31, 2005: $172,955), general and administration expenses at December 31, 2005 amounted to $257,509 compared with $447,867 at March 31, 2005 after eliminating these items. This decrease was due to an overall reduction of operating and administrative expenses and overheads both proportionally and in total for the period.

Exploration expenditure incurred during the period ended December 31, 2005 at the Newdico project in Botswana was $239,505 compared to $472,814 during the year ended March 31, 2005. Exploration expenditure on all projects amounted to $282,977 during the period compared to $592,199 for the year ended March 31, 2005 The principal components of the Newdico exploration program were: (a) additional soil sampling and the completion of the processing and analysis of the soil samples; (b) commissioning of further ground magnetic and gravity survey of selected aeromagnetic anomalies; (c) analyzing detailed proprietary aeromagnetic maps covering the target areas; and (d) commencement of a reverse circulation drilling program on selected targets.

## PERSONNEL

At December 31, 2005 the Company and its subsidiaries employed the same number of personnel (6) as at March 31, 2005, including senior officers, administrative and operations personnel including those on short-term contract bases. Individual components of the exploration program, such as soil sampling, geophysical surveying and reverse circulation drilling, are contracted out to independent third parties operating under the control and direction of the Company's subsidiaries' Managing Director, James M. Bruchs, and the Company's Exploration Vice President, Peter W. A. Walker.

## THIRD QUARTER - 2005

During the third quarter, the board decided that it was in the best interests of the Company to change its financial year end from March 31 to December 31 effective December 31, 2005. The change in financial year to December 31 was made to align with the reporting schedule of comparable public companies. The period ended December 31, 2005 is the transitional year and has a nine month reporting period. The third quarter was a normal operating period for a quarter and year end.

## RISKS AND UNCERTAINTIES

Tsodilo's primary objective is the discovery of an economic kimberlite diamond deposit capable of rapid advancement to feasibility stage and ultimate development as a producing property. The discovery of a kimberlite is only the first step in the exploration process. Subsequent evaluation begins with caustic fusion diamond analysis of the kimberlite and, if results warrant, continues through progressively larger mini-bulk and bulk samples in order to make an increasingly accurate determination of the content and quality of the diamonds. Early stages of kimberlite evaluation provide an initial qualitative assessment rather than an accurate indication of either the grade of the ore body or the value per carat of the diamonds. Collection of larger bulk samples and formal appraisal of a commercial-size parcel of diamonds are necessary to make an accurate determination of these parameters. At any stage in the process, the results may indicate that the deposit lacks the required economic value.

### Capital Requirements

In the absence of cash flow from operations, Tsodilo relies on capital markets to fund its operations. The ongoing exploration and eventual successful development of a diamond mine would require significant additional financing. There can be no assurance that adequate funding will be available, or available under terms favorable to the Company, for these purposes when ultimately required. The exploration and development of mineral deposits involve significant financial risks over an extended period of time. Even a combination of careful evaluation, experience and knowledge may not eliminate these risks. While discovery of a diamond deposit may result in substantial rewards, few exploration properties ultimately become producing mines.

### Off-Balance Sheet Arrangements

The Company has not entered into any off-balance sheet financing arrangements.

### Exploration Risks

The Company's operations are subject to all the hazards and risks normally incident to the exploration, development and mining of diamond deposits, any of which could result in damage to life or property, environmental damage and possible legal liability for any or all damage. Whether a diamond deposit will ultimately be commercially viable depends on a number of factors, including the particular attributes of the deposit such as the deposit's size; the quality and quantity of the diamonds; its proximity to existing infrastructure; financing costs and the prevailing prices for diamonds. Also of key importance are government regulations, including those relating to prices, taxes, royalties, land tenure, land use, the importing and exporting of diamonds and production plant and equipment, and environmental protection. The effects of these factors cannot be accurately predicted, but any combination of them may impede the development of a deposit or render it uneconomic.

At this time, the major portion of the Company's exploration activity is carried out in partnership with another party. Doing so allows the Company to maximize its exposure to promising exploration opportunities, to manage the risks inherent in diamond exploration, and to optimize its use of financial and management resources.

### Currency Risks

The Company's financing has generally been received in United States dollars while significant portions of its operating expenses has been and will be incurred in Botswana Pula. On May 29, 2005, the Botswana Minister of Finance and Development Planning announced a 12% devaluation of the pula against a basket of currencies, as well as a change in the system of exchange-rate adjustments to a crawling peg rather than the discrete steps previously used, in order to improve Botswana's competitiveness. This action has stabilized the current pula / dollar rates similar to those in 2002.

### Key Personnel

The Company is dependent upon on a relatively small number of key employees, the loss of any of whom could have an adverse effect on the Company. The Company currently does not have key personal insurance on these individuals.

## ACCOUNTING STANDARDS

Tsodilo follows Canadian generally accepted accounting principles. In line with accepted industry practice, the Company has adopted the policy of deferring property specific acquisition and exploration costs. Deferred costs relating to properties that are relinquished, or where continued exploration is deemed inappropriate, are written off in the year such assessment is made. If Tsodilo adopted a policy of expensing all exploration costs, the Company's asset base, shareholders' equity, and loss from operations would be materially different.

### Related Party Transactions

The Company has not entered into related parties transactions during the nine month period ended December 31, 2005 or the year ended March 31, 2005.

## OUTLOOK

Diamond exploration remains a high-risk undertaking requiring patience and persistence. Despite difficult capital markets in the junior resource sector, the Company remains committed to international diamond exploration through carefully managed programs. Peter W. A. Walker, a professional geologist registered with the South African Council for Natural Scientific Professions is the qualified person responsible for the design and conduct of the Company's exploration programs.

## ADDITIONAL INFORMATION

Additional information relating to Tsodilo Resources Limited is available on its website www.TsodiloResources.com or through SEDAR at www.sedar.com.

## FORWARD-LOOKING STATEMENTS

The Annual Report, including this MD&A, contains certain forward-looking statements related to, among other things, expected future events and the financial and operating results of the Company. Forward-looking statements are subject to inherent risks and uncertainties including, but not limited to, market and general economic conditions, changes in regulatory environments affecting the Company's business and the availability and terms of financing. Other risks are outlined in the Uncertainties and Risk Factors section of this MD&A. Consequently, actual results and events may differ materially from those included in, contemplated or implied by such forward looking statements for a variety of reasons. Readers are therefore cautioned not to place undue reliance on any forward-looking statement. The Company disclaims any intention and assumes no obligation to update any forward-looking statement even if such information becomes available as a result of future events or for any other reason.

L. Kirk Boyd

Chief Financial Officer

March 20, 2006

## Financial Reporting Responsibility of Management

The annual report and consolidated financial statements have been prepared by management. The consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles and include amounts that are based on informed judgments and best estimates. The financial information presented in this annual report is consistent with the consolidated financial statements. Management acknowledges responsibility for the fairness, integrity and objectivity of all information contained in the annual report including the consolidated financial statements. Management is also responsible for the maintenance of financial and operating systems, which include effective controls to provide reasonable assurance that assets are properly protected and that relevant and reliable financial information is produced. Our independent auditors have the responsibility of auditing the consolidated financial statements and expressing an opinion on them.

The Board of Directors, through its Audit Committee, is responsible for ensuring that management fulfills its responsibilities for financial reporting and internal control. The Audit Committee is composed of three directors, all of whom qualify as unrelated directors and are independent of management and free from any interest or business relationship which could, or could be perceived to, materially interfere with their ability to act in the best interests of the Company. This committee meets periodically with management and the external auditors to review accounting, auditing, internal control and financial reporting matters. The Audit Committee reviews the annual financial statements before they are presented to the Board of Directors for approval and considers the independence of the auditors.

The financial statements for the period ended December 31, 2005 have been audited by KPMG Inc., the external auditors, in accordance with Canadian generally accepted auditing standards on behalf of the shareholders. Their report follows hereafter.

James M. Bruchs
President and Chief Executive Officer
March 20, 2006

L. Kirk Boyd
Chief Financial Officer
March 20, 2006

## Auditors' Report to the Shareholders of Tsodilo Resources Limited

We have audited the consolidated balance sheet of Tsodilo Resources Limited as at December 31, 2005 and the consolidated statements of operations, deficit and cash flows for the nine months 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 audit.

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

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2005 and the results of its operations and its cash flows for the nine months then ended in accordance with Canadian generally accepted accounting principles.

The consolidated financial statements as at March 31, 2005 and for the year then ended were audited by another firm of chartered accountants who expressed an opinion without reservation on those statements in their report, dated June 28, 2005.

KPMG Inc.

KPMG Inc.

Chartered Accountants (SA)
Johannesburg, South Africa
March 20, 2006

# Tsodilo Resources Limited

## Consolidated Balance Sheets

As at December 31, 2005 and March 31, 2005
*(in United States dollars – note 2)*

| | **December 31, 2005** | March 31, 2005 |
|---|---|---|
| **ASSETS** | | |
| **Current** | | |
| Cash and equivalents | **289,810** | 637,805 |
| Amounts receivable and prepaid expenses | **28,055** | 14,616 |
| | **317,865** | 652,421 |
| **Exploration Properties** *(note 3)* | **1,679,616** | 1,396,639 |
| **Property, Plant and Equipment** *(note 4)* | **34,945** | 38,361 |
| | **2,032,426** | 2,087,421 |
| **LIABILITIES** | | |
| **Current** | | |
| Accounts payable and accrued liabilities | **21,324** | 42,442 |
| **NON-CONTROLLING INTEREST** *(note 3)* | **280,642** | 237,008 |
| **SHAREHOLDERS' EQUITY** | | |
| **Share Capital** *(note 5)* | **26,218,172** | 25,909,032 |
| **Warrants** *(note 5)* | **140,112** | 233,057 |
| **Contributed Surplus** *(note 5)* | **6,023,823** | 5,846,718 |
| **Cumulative Translation** *(note 2)* | **(837,425)** | (837,425) |
| **Deficit** | **(29,814,222)** | (29,343,411) |
| | **1,730,460** | 1,807,971 |
| | **2,032,426** | 2,087,421 |

**Going Concern** *(note 1)*
**Subsequent events** *(note 5,11)*
**Commitments** *(note 11)*

**APPROVED ON BEHALF OF THE BOARD OF DIRECTORS**

James M. Bruchs
Director

Patrick C. McGinley
Director

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

# Tsodilo Resources Limited

## Consolidated Statements of Operations

For the nine months ended December 31, 2005
and for the year ended March 31, 2005
*(in United States dollars – note 2)*

| | **December 31, 2005** | March 31, 2005 |
|---|---|---|
| **EXPENSES** | | |
| Consulting fees | **17,939** | 29,933 |
| Corporate remuneration | **99,844** | 135,113 |
| Corporate travel and subsistence | **5,029** | 52,190 |
| Investor relations | **35,374** | 61,541 |
| Legal and audit | **56,799** | 112,059 |
| Office and administration | **40,836** | 54,642 |
| Amortization | **1,688** | 2,389 |
| Foreign exchange loss | **50,546** | 49,915 |
| Stock-based compensation *(note 5)* | **162,756** | 123,040 |
| | **470,811** | 620,822 |
| Loss before non-controlling interest | **(470,811)** | (620,822) |
| Non-controlling interest | **-** | – |
| Loss for the period | **(470,811)** | (620,822) |
| Basic and diluted loss per share - cents *(note 7)* | **($0.04)** | ($0.07) |

## Consolidated Statements of Deficit

For the nine months ended December 31, 2005
and for the year ended March 31, 2005
*(in United States dollars – note 2)*

| | **December 31, 2005** | March 31, 2005 |
|---|---|---|
| **Deficit – Beginning of period** | **(29,343,411)** | (28,722,589) |
| Loss for the year | **(470,811)** | (620,822) |
| **Deficit - End of year** | **(29,814,222)** | (29,343,411) |

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

Tsodilo Resources Limited

## Consolidated Statements of Cash Flows

For the nine months ended December 31, 2005
and for the year ended March 31, 2005
*(in United States dollars – note 2)*

| | **December 31, 2005** | March 31, 2005 |
|---|---|---|
| **CASH PROVIDED BY (USED IN):** | | |
| **OPERATING ACTIVITIES** | | |
| Loss for the year | **(470,811)** | (620,822) |
| Adjustments for non-cash items: | | |
| Amortization | **1,688** | 2,389 |
| Stock-based compensation *(note 5)* | **162,756** | 123,040 |
| | **(306,367)** | (495,393) |
| Net change in non-cash working capital balances | **(34,557)** | 21,558 |
| | **(340,924)** | (473,835) |
| **INVESTING ACTIVITIES** | | |
| Exploration properties | **(273,924)** | (592,199) |
| Disposals of / (Additions to) Property, Plant and Equipment | **(7,325)** | 3,104 |
| | **(281,249)** | (589,095) |
| **FINANCING ACTIVITIES** | | |
| Issue of common shares | **230,544** | 1,528,905 |
| Contribution from non-controlling interest | **43,634** | 23,459 |
| | **274,178** | 1,552,364 |
| **Change in cash and equivalents - For the period** | **(347,995)** | 489,434 |
| **Cash and equivalents - Beginning of period** | **637,805** | 148,371 |
| **Cash and equivalents - End of period** | **289,810** | 637,805 |

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

# Tsodilo Resources Limited
## Notes to the Consolidated Financial Statements

For the nine months ended December 31, 2005 and for the year ended March 31, 2005

### 1. NATURE OF OPERATIONS AND GOING CONCERN

Tsodilo Resources Limited ("Tsodilo" or the "Company") is an international diamond exploration company engaged in the process of exploring its mineral properties in northwest Botswana. The Company has not yet determined whether these properties contain reserves that can be economically mined. As an exploration stage company, the recoverability of amounts shown for exploration expenditures is dependent upon the discovery of reserves that can be economically mined, the securing and maintenance of the interests in the properties, the ability of the Company to obtain the necessary financing to complete the development, and future production or proceeds from the disposition thereof. The Company is also actively reviewing additional opportunities within southern Africa.

As at December 31, 2005, the Company reported an accumulated deficit of $29,814,222 (March 2005: $29,343,411) and cash outflows from operations $340,924 (March 2005: $473,835) for the period then ended. The cash position of the Company is insufficient to finance continued exploration. The continuity of the Company's operations is dependent on Tsodilo raising future financing for working capital, the continued exploration and development of its properties, and for acquisition and development costs of new project opportunities. There can be no assurance that adequate financing will be available, or available under terms favorable to the Company. These financial statements have been prepared on a going concern basis that assumes the continuity of operations and realization of assets and settlement of liabilities in the normal course of business. Should it be determined that the Company is no longer a going concern, adjustments, which could be significant, would be required to the carrying value of assets.

Tsodilo expects to raise amounts to fund continued exploration by way of negotiated non-brokered private placements (refer note 5).

### 2. SIGNIFICANT ACCOUNTING POLICIES

#### Basis of consolidation and preparation of the consolidated financial statements

The consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles ("GAAP") and include the accounts of the Company and its direct and indirect subsidiaries. All inter-company transactions and balances have been eliminated.

Group Companies: December 31,2005 and March 31, 2005

| | |
|---|---|
| Tsodilo Resources Bermuda Limited | 100% |
| Gcwihaba Resources (Proprietary) Ltd (Botswana) ("Gcwihaba") | 100% |
| Newdico (Proprietary) Limited (Botswana) ("Newdico") | 81% *(note 3)* |

#### Change in reporting currency

For the year ended March 31, 2005, management elected to change the functional and reporting currency of the Company from Canadian to United States dollars, as this more accurately reflects the requirements of the Company's investors and other users of the financial statements.

Accordingly, all prior period financial information has been presented in US dollars, to provide information on a consistent basis.

## Earnings per share

Basic Earnings-Per-Share (EPS) is computed as net income (loss) applicable to common stockholders' divided by the weighted average number of common shares outstanding for the period. Diluted EPS reflects the potential dilution that could occur from common shares issued through stock options, warrants and other convertible securities when the effect would be dilutive.

## Use of estimates

The preparation of the consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the consolidated financial statements. The most significant estimates are related to the recoverability of exploration expenditures, fixed assets and contingencies. Actual results could differ from those estimates.

## Exploration properties

All costs relating to the acquisition, exploration and development of non-producing mining properties are capitalized as incurred. The amounts capitalized represent costs to be charged to operations in the future and do not necessarily reflect the present or future values of the particular properties.

If a property proceeds to development, these costs become part of preproduction and development costs of the mine and will be amortized over the expected life of the mine. If a property is abandoned, sold or continued exploration is not deemed appropriate in the foreseeable future or when other events and circumstances indicate that the carrying amount may not be recovered, the related costs and expenditures are written down to the net recoverable amount at the time the determination is made. Proceeds from the sale of exploration properties are credited to the costs of the relevant property.

Exploration costs that do not relate to specific non-producing mining properties are expensed as incurred.

## Amortization

Property, plant and equipment are amortized principally on a straight-line basis over their estimated useful lives of three to ten years. Property, plant and equipment awaiting installation on site are not amortized until they are commissioned, but are reviewed for impairment and if deemed impaired, an impairment loss is measured and recorded based on the net recoverable value of the asset.

## Foreign currency translation

The US dollar is the currency in which the financial statements are presented. Foreign currency transactions and balances, and the financial statements of foreign operations, all of which are integrated, are translated into US dollars using the temporal method. Under this method, monetary assets and liabilities of the Company and its subsidiaries denominated in foreign currencies are translated into US dollars at the exchange rates in effect at the balance sheet date. Non-monetary assets and liabilities are translated at the historical rates. Revenue and expense items are translated at the average rate prevailing during the year, except for depreciation, depletion, amortization and write downs, which are translated at the same exchange rates as the assets to which they relate with gains and losses arising on settlement recognized in the statement of operations.

### Cash and Equivalents

Cash and equivalents are comprised of cash, term deposits and money market instruments with investment grade credit ratings and market maturity dates of 90 days or less from the date of acquisition.

### Income Taxes

The Company uses the asset and liability method of accounting for income taxes. Assets and liabilities are recognized for the estimated future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases reduced by a valuation allowance to reflect the recoverability of any future income tax asset. Future income tax assets and liabilities are measured using tax rates in effect for the period in which those temporary differences are expected to be recovered or settled. The effect on future income tax assets and liabilities of a change in tax rates or laws is recognized as part of the provision for income taxes in the period the changes are considered substantively enacted.

### Stock-Based Compensation Plans

Tsodilo has a Stock Option Plan (refer to note 5). Under the Stock Option Plan, the Company may grant options to directors, officers and employees for up to 1,789,750 shares of common stock. The exercise price is determined by the Chairman of the Compensation Committee and the President and CEO in consultation with the board of directors, but is not less than the market price of the Company's stock on the date of the grant. An option's maximum term is 5 years. The Company uses the fair value method of accounting for stock options. Under the fair value method stock-based payments are measured at the fair value of the equity investments and are amortized over the vesting period. Consideration paid on exercise of stock options is credited to common share capital.

## 3. EXPLORATION PROPERTIES

These may be summarized as follows:

| | **Newdico Botswana** | **Gcwihaba Botswana** | **Total** |
|---|---|---|---|
| | $ | $ | $ |
| Balance at March 31, 2004 | 787,733 | 16,707 | 804,440 |
| 2005 expenditures | 472,814 | 119,385 | 592,199 |
| **Balance at March 31, 2005** | **1,260,547** | **136,092** | **1,396,639** |
| Apr. to Dec. 2005 expenditures | 239,505 | 43,472 | 282,977 |
| **Balance at December 31, 2005** | **1,500,052** | **179,564** | **1,679,616** |

A summary of the significant agreements entered into by the Company is as follows:

### Newdico (Proprietary) Limited - Botswana

Newdico holds prospecting licenses in the Ngamiland District of northwest Botswana. The Company acquired the various licenses in 1999, 2001 and 2003. In 2005, the Company was reissued its prospecting licenses for an initial term of three years, and are renewable for 2 two year periods upon application and have a final expiry of 2012. The terms of the licenses also require Newdico to spend a minimum of Botswana Pula 8.6 million (approximately $1.6 million) on prospecting over this period, inclusive of the renewals.

Originally Newdico was held 75% by Tsodilo and 25% by Trans Hex Group Limited ("Trans Hex Group"), with Tsodilo being the operator. Trans Hex Group has funded its proportionate share of expenditure, and these amounts have been reflected as non-controlling interest of $280,642 (March 31, 2005: $237,008) in the financial statements. During the year ended March 31, 2005, Trans Hex decided not to fund a portion of its share of expenditures on a cash call and therefore on January 1, 2005, the Company increased its interest in Newdico from 75% to 81% in accordance with the exploration agreement between the two parties.

Trans Hex Group has also advanced funds amounting to $187,052 (March 31, 2005: $187,052) to Newdico, relating to exploration properties which have been written off in earlier years. This liability has not been recorded in these financial statements as it is repayable only from Tran Hex Group's share of any future earnings of Newdico after repayment of loans relating to the Newdico Project.

Some, or all, of the current licenses held by Newdico may be subject to the granting of a 2% free carried interest in any diamond mine or mines that may result thereon.

### Gcwihaba Resources (Proprietary) Limited - Botswana

Gcwihaba, a wholly owned subsidiary of the Company, holds prospecting licenses to the south of the Ngamiland project area.

Diamond Exploration

The terms of the licenses grant Gcwihaba the right to prospect for a total of three years to 2006, and are renewable for 2 two year periods upon application and have a final expiry of 2010. The terms require Gcwihaba to spend a minimum of Botswana Pula 1.05 million (approximately $0.20 million) on prospecting over the initial period of the licenses exclusive of the current renewals.

Base and Precious Metal Exploration

The terms of the licenses grant Gcwihaba the right to prospect for a total of three years to 2008, and are renewable for 2 two year periods upon application and have a final expiry of 2012. The terms require Gcwihaba to spend a minimum of Botswana Pula 0.72 million (approximately $0.14 million) on prospecting over this period, exclusive of their current renewals.

## 4. PROPERTY, PLANT AND EQUIPMENT

| March 31, 2005 | Cost | Accumulated amortization | Book value |
|---|---|---|---|
| Vehicles | **40,473** | **13,767** | **26,706** |
| Furniture and Equipment | **25,270** | **13,615** | **11,655** |
| | **65,743** | **27,382** | **38,361** |
| **December 31, 2005** | | | |
| Vehicles | **40,473** | **21,555** | **18,918** |
| Furniture and Equipment | **32,595** | **16,568** | **16,027** |
| | **73,068** | **38,123** | **34,945** |

## 5. SHARE CAPITAL

**Common Shares**

**Authorized**

The authorized capital stock of the Company comprises an unlimited number of common shares.

**Issued and outstanding**

Details of the issued and outstanding common shares are as follows:

| | Shares (number) | Amount $ |
|---|---|---|
| **Issued and outstanding at March 31, 2004** | 7,891,580 | 24,466,943 |
| On private placement for cash (i) | 687,409 | 379,620 |
| On private placement for cash (ii) | 113,938 | 104,643 |
| On private placement for cash (iii) | 53,336 | 102,780 |
| On private placement for cash (iv) | 461,570 | 433,371 |
| Ascribed to warrants issued (b) | - | (208,982) |
| On exercise of stock options | | |
| (including $14,406 reallocated from contributed surplus) (c) | 121,250 | 47,329 |
| On exercise of warrants (including $107,760 reallocated from warrants) (b) | 1,152,543 | 583,328 |
| **Issued and outstanding at March 31, 2005** | 10,481,626 | 25,909,032 |
| On exercise of warrants (including $78,596 reallocated from warrants) (b) | 563,419 | 309,140 |
| **Issued and outstanding at December 31, 2005** | 11,045,045 | 26,218,172 |

### (i) Private Placement

In June 2004, the Company issued, through a non-brokered private placement, 687,409 units of the Company at a price of $0.57 (C$0.75) per unit for gross proceeds to the Company of $379,620. Each unit consists of one common share of the Company and half a warrant of the Company, each full such warrant entitling the holder to purchase one common share of the Company at a price of C$0.75 for a period of two years. The common shares, warrants and warrant shares are subject to a hold period of 12 months as agreed to by the parties, expiring on June 1, 2005.

### (ii) Private Placement

In October 2004, the Company issued, through a non-brokered private placement, 113,938 units of the Company at a price of $0.92 (C$1.12) per unit for gross proceeds to the Company of $104,643. Each unit consists of one common share of the Company and half a warrant of the Company, each full such warrant entitling the holder to purchase one common share of the Company at a price of C$1.12 for a period of two years. The common shares, warrants and warrant shares are subject to a hold period of 12 months as agreed to by the parties, expiring on October 14, 2005.

### (iii) Private Placement

In November 2004, the Company issued, through a non-brokered private placement, 53,336 units of the Company at a price of $1.93 (C$2.35) per unit for gross proceeds to the Company of $102,780. Each unit consists of one common share of the Company and half a warrant of the Company, each full such warrant entitling the holder to purchase one common share of the Company at a price of C$2.35 for a period of two years. The common shares, warrants and warrant shares are subject to a hold period of 12 months as agreed to by the parties, expiring on November 8, 2005.

### (iv) Private Placement

In March 2005, the Company issued, through a non-brokered private placement, 461,570 units of the Company at a price of $0.94 (C$1.15) per unit for gross proceeds to the Company of $433,371. Each unit consists of one common share of the Company and half a warrant of the Company, each full such warrant entitling the holder to purchase one common share of the Company at a price of C$1.15 for a period of two years. The common shares, warrants and warrant shares are subject to a statutory hold period under securities laws of 4 months, expiring on July 3, 2005.

### (v) Private Placement

In January 2006, the Company issued, through a non-brokered private placement, 468,776 units of the Company at a price of $1.07 (C$1.25) per unit for gross proceeds to the Company of $500,000. Each unit consists of one common share of the Company and one warrant of the Company, each warrant entitling the holder to purchase one common share of the Company at a price of C$1.00 for a period of two years. The common shares, warrants and warrant shares are subject to a hold period of 12 months as agreed to by the parties, expiring on January 27, 2007.

### (vi) Private Placement

In February 2006, the Company issued, through a non-brokered private placement, 319,108 units of the Company at a price of $0.78 (C$0.90) per unit for gross proceeds to the Company of $250,000. Each unit consists of one common share of the Company and one warrant of the Company, each warrant entitling the holder to purchase one common share of the Company at a price of C$1.00 for a period of two years. The common shares, warrants and warrant shares are subject to a statutory hold period under securities laws of 4 months, expiring on June 21, 2006.

### (b) Warrants

As at December 31, 2005, the following warrants were outstanding:

| | | Number of Warrants | | | Value | | |
|---|---|---|---|---|---|---|---|
| **Expiry Date** | **Exercise Price** | **Opening** | **Issued/ (Exercised) (Expired)** | **Closing** | **Opening (dollars)** | **Issued/ (Exercised) (Expired)** | **Closing (dollars)** |
| May 26, 2005 | C$0.50 | **241,710** | **(241,710)** | **–** | **46,292** | **(46,292)** | **–** |
| August 17, 2005 | C$0.50 | **139,789** | **(139,789)** | **–** | **14,752** | **(14,752)** | **–** |
| September 29, 2005 | C$0.50 | **268,556** | **(268,556)** | **–** | **31,901** | **(31,901)** | **–** |
| June 1, 2006 (i) | C$0.75 | **65,024** | **–** | **65,024** | **14,164** | **–** | **14,164** |
| October 14, 2006 (ii) | C$1.12 | **56,969** | **–** | **56,969** | **20,156** | **–** | **20,156** |
| November 8, 2006 (iii) | C$2.35 | **26,668** | **–** | **26,668** | **20,622** | **–** | **20,622** |
| March 4, 2007 (iv) | C$1.15 | **230,785** | **–** | **230,785** | **85,170** | **–** | **85,170** |
| | | **1,029,501** | **(650,055)** | **379,446** | **233,057** | **(92,945)** | **140,112** |

During the nine month period, 563,419 warrants were exercised for proceeds to the Company of $230,544. This exercise resulted in the issuance of 563,419 common shares. In addition, $78,596 attributed to the warrants exercised during the nine month period has been reallocated to share capital. As there were no warrants issued during the nine month period, no value was attributed as at December 31, 2005 (March 31, 2005: $208,982). During the year ended March 31, 2005 warrants were valued using the Black-Scholes model, using key assumptions of volatility ranging from 69-89%, a risk-free interest rate of 4%, a term equivalent to the life of the warrant, and reinvestment of all dividends in the Company.

### (c) Contributed Surplus

| | |
|---|---|
| As at March 31, 2004 | 5,738,084 |
| Relating to issue of stock options | 123,040 |
| Transferred to share capital on exercise of options | (14,406) |
| As at March 31, 2005 | 5,846,718 |
| Relating to the expiry of warrants | 14,349 |
| Relating to issue of stock options | 162,756 |
| As at December 31, 2005 | 6,023,823 |

### (d) Stock Option Plan

Outstanding stock options granted to directors, officers and employees at December 31, 2005 and March 31, 2005 were as follows:

| **Expiry** | **Price** | **Outstanding March 31, 2004** | **Granted/ (Cancelled/ Exercised)** | **Outstanding March 31, 2005** | **Granted/ (Cancelled)** | | **Outstanding December 31, 2005** |
|---|---|---|---|---|---|---|---|
| June 24, 2007 | C$0.15 | 200,000 | (50,000) | 150,000 | (50,000) | (i) | **100,000** |
| September 18, 2007 | C$0.23 | 200,000 | (50,000) | 150,000 | (50,000) | (i) | **100,000** |
| December 31, 2007 | C$0.41 | 165,000 | (115,000) | 50,000 | - | (ii) | **50,000** |
| July 8, 2008 | C$0.50 | 210,000 | (60,000) | 150,000 | (50,000) | (ii) | **100,000** |
| January 1, 2009 | C$0.75 | 110,000 | (50,000) | 60,000 | - | (ii) | **60,000** |
| January 26, 2009 | C$0.75 | 50,000 | (50,000) | - | - | (ii) | **–** |
| August 31, 2009 | C$0.75 | - | 260,000 | 260,000 | (50,000) | (ii) | **210,000** |
| January 3, 2010 | C$1.85 | - | 85,000 | 85,000 | - | (ii) | **85,000** |
| August 19, 2010 | C$1.25 | - | - | - | 280,000 | (ii) | **280,000** |
| | | 935,000 | (30,000) | 905,000 | 80,000 | | **985,000** |

| | | | |
|---|---|---|---|
| Options exercisable at end of year | 668,750 | 696,250 | **680,000** |
| Weighted average exercise price | | | |
| - issued | C$0.38 | C$0.55 | **C$0.67** |
| - outstanding | C$0.39 | C$0.60 | **C$0.83** |
| - exercisable | C$0.31 | C$0.46 | **C$0.65** |

All options have a term of five years.

(i) These common share purchase options vest as to one-half immediately and one-half on the six-month anniversary of the date granted.

(ii) These common share purchase options vest as to one-quarter immediately and one-quarter on each of the six-month, 12-month and 18-month anniversaries of the date granted.

(iii) The Company recognized an expense of $162,756 (March 31, 2005: $123,040) relating to the fair value of options granted or vesting during the year. The fair value of options granted was calculated using the Black-Scholes model, using key assumptions of volatility of 88%, a risk-free interest rate of 4%, a term equivalent to the life of the option, and reinvestment of all dividends in the Company. The Company will recognize expense of C$182,596 relating to options granted before December 31, 2005 but not yet vested.

## 6. INCOME TAXES

The recovery of income taxes varies from the amounts that would be computed by applying the Canadian federal and provincial statutory rate of approximately 36.12% (Mar. 2005 – 36.12%) to income before taxes as follows:

| | December 31 2005 | March 31 2005 |
|---|---|---|
| Net Income (loss) for the period | (470,811) | (620,822) |
| Income tax (recovery) provision at Canadian statutory income tax rates | (170,057) | (224,241) |
| Current year losses not recognized | 111,263 | 179,373 |
| Permanent differences | 58,794 | 44,868 |
| Provision for (recovery of ) income taxes | 0 | 0 |

The following summarizes the principal temporary differences and related future tax effect:

| | December 31 2005 | March 31 2005 |
|---|---|---|
| Property, Plant and Equipment | 12,000 | 13,000 |
| Exploration & Development - Canada | 92,000 | 90,000 |
| Exploration & Development - Botswana | (606,000) | (504,000) |
| Losses carried forward - Canada | 1,585,000 | 1,400,000 |
| Losses carried forward - Botswana | 642,000 | 507,000 |
| Other | 42,000 | 41,000 |
| Subtotal – future income tax asset | 1,767,000 | 1,547,000 |
| Valuation allowance | (1,767,000) | (1,547,000) |
| Net future income tax asset recorded | 0 | 0 |

At December 31, 2005, the Company has Canadian net operating losses carried forward that expire as follows:

| Loss | Year of Expiry | |
|---|---|---|
| **758,000** | 2006 | *(1) |
| **740,000** | 2007 | (1) |
| **818,000** | 2008 | (1) |
| **697,000** | 2009 | (1) |
| **315,000** | 2010 | (1) |
| **369,000** | 2011 | (1) |
| **492,000** | 2012 | *(1) |
| **185,000** | 2012 | *(2) |

* 2005 is a transitional year for year end change from March 31 to December 31. (1) expires March 31 and (2) expires December 31.

Total assessable losses relating to the activity in Botswana as at December 31, 2005 was $1,778,000 (March 31, 2005: $1,405,000) of which $1,680,000 (March 31, 2005: $1,397,000) have no expiry date.

### 7. LOSS PER SHARE

Loss per share is computed on the basis of the loss of $470,811 for the nine month period ended December 31, 2005 (March 31, 2005: $620,822) and the weighted average number of common or equivalent shares outstanding during period, December 31, 2005: 10,811,496 (March 31, 2005: 9,136,737). The effect of conversion in computing diluted per share amounts for December 31, 2005 and March 31, 2005 is anti-dilutive.

### 8. RELATED PARTY TRANSACTIONS

The Company did not enter into transactions with related parties during the nine month period ended December 31, 2005 or the year ended March 31, 2005.

### 9. SEGMENTED INFORMATION

Substantially all working capital balances of the Company are situated at the head office in Canada and in Botswana. Materially all of the Company's property plant and equipment is presently located in Canada ($10,131) and Botswana ($24,814). The geographic distribution of the property acquisition costs and exploration expenditures is outlined in note 3.

### 10. FINANCIAL INSTRUMENTS

The carrying amounts reflected in the consolidated balance sheets for cash and equivalents, accounts receivable and accounts payable and accrued liabilities approximate their fair values due to the short maturities of these instruments.

### 11. COMMITMENTS

All operating leases are for a period of no longer than one year and are prepaid.

The Company holds prospecting licenses which require the Company to spend a specified minimum amount on prospecting over the period of the terms as outlined in note 3.

In February 2006, the Company placed an order for a mobile diamond core drill rig and transport equipment at a cost of $650,400. The Company expects delivery early in the second quarter of the year.

# Corporate Information

## DIRECTORS

**James M. Bruchs**
Gaborone, Botswana
*Appointed as director in 2002*

**Patrick C. McGinley**
Washington, D.C.
*Appointed as director in 2002*

**R. Stuart Angus**
Vancouver, British Columbia
*Appointed as director in 2004*

**John R. Redmond**
Potomac, Maryland
*Appointed as director in 2005*

## OFFICERS

**James M. Bruchs**, B.Sc., J.D.
President and
Chief Executive Officer
*Appointed in 2002*

**Peter W.A. Walker**, B.Sc. (Honors)
MBA., Pr.Sci.Nat.
Vice President, Exploration
*Appointed in 2004*

**L. Kirk Boyd**, B.Com.
Chief Financial Officer
*Appointed in 2005*

**Gail McGinley**
Corporate Secretary
*Appointed in 2005*

## CORPORATE HEAD OFFICE

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## AUDITORS

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Johannesburg, South Africa

## LEGAL COUNSEL

Fasken Martineau DuMoulin LLP
Toronto, Ontario

## REGISTRAR AND TRANSFER AGENT

Computershare Trust
Company of Canada
Toronto, Ontario

## STOCK EXCHANGE LISTING

TSX Venture Exchange
Trading Symbol: TSD

Design: Macrae Design